II. Review of operations

1. Business and other risks

There were no business and other risks that newly arose during the three months ended February 28, 2018. In addition, there were no significant changes in “Business and other risks” described in the annual securities report for the previous fiscal year.

2. Important operational contracts, etc.

No important operational contracts, etc. were determined or entered into during the first quarter of the fiscal year under review.

3. Analysis of financial position, operating results and cash flows

Any forward-looking statements included in the following descriptions are based on the best estimates or judgment of the Tosei Group as of February 28, 2018.

(1) Analysis of operating results

During the three months ended February 28, 2018, the Japanese economy continued to recover. A moderate recovery is expected to continue going forward, backed by stable personal consumption, expansion of favorable corporate earnings, and increasing exports, despite concerns over downside risks of financial policy trends in Europe and the U.S., and geopolitical risks in Asia.

In the real estate industry where Tosei Group operates, domestic real estate transactions by listed companies and other such entities for the full year 2017 rose 14.4% year on year to ¥4.5775 trillion. While sales with the aim of locking in profits increased due to rising real estate prices, transactions were active owing to the demand for property acquisition from investors preferring stable rent income despite low investment returns. The high demand for real estate investment from investors is likely to continue for some time, with the prospect that monetary easing policies are to be sustained by the Bank of Japan (according to a survey by a private research institute).

In the Tokyo metropolitan area condominium market, the number of units sold in the full year 2017 increased 0.4% year on year to 35,898. Under the effects of rising construction costs and high land prices, the average selling price soared to ¥59.08 million, an increase of 7.6% year on year, only second to the ¥61.23 million recorded in 1990. The sluggish sales of some suburban properties resulted in the average contract rate for the first month at 68.1% (a decrease of 0.7 percentage points year on year), slightly below the 70% threshold from which market conditions are viewed as favorable. However, about 38,000 units (an increase of 5.9% year on year) are expected to be sold in the full year 2018, due to the solid sales of properties in the central Tokyo area and near stations, as well as the anticipated recovery of suburban unit sales as a result of the rush in demand caused by the increase in consumption taxes scheduled to take effect in October 2019 (according to a survey by a private research institute).

In the Tokyo metropolitan area build-for-sale detached house market, due to the soaring sales prices of newly built condominiums, a part of end-user demand flowed into the undervalued detached house market. As a result, housing starts in the full year 2017 rose 2.2% year on year to 62,028 units (according to a survey by the Ministry of Land, Infrastructure, Transport and Tourism).

The office leasing market of Tokyo’s five business wards has been performing favorably. The vacancy rate as of January 2018 declined by 0.6 percentage points from 3.7% year on year to 3.1%, and the average asking rent was ¥19,338 per tsubo (1 tsubo = 3.3m2), a 4.1% increase year on year, and increased for the 49th consecutive month. An upsurge in supply of large-scale office buildings can be anticipated in 2018, and the vacancy rate is expected to deteriorate, but corporate interest in expanding offices and their need for relocation and integration are expected to remain strong. As a result, the average asking rent in the second half of 2018 is expected to remain in an uptrend (according to a survey by a private research institute).

In the real estate securitization market, the total value of assets under management as of December 31, 2017 was ¥16.5 trillion in J-REITs (an increase of ¥1.0 trillion year on year). In an environment where real estate prices remain persistently high, property acquisitions continue to progress despite at a gradual pace, and the market scale expanded to ¥32 trillion, including ¥15.8 trillion of value under management in private placement funds (as of June 30, 2017) (according to a survey by a private research institute).

Amid this operating environment, in the Revitalization Business, the Group made steady progress in selling assets such as income-generating office buildings and apartments, while in the Development Business, the Group pushed ahead with sales of detached houses. In addition, other than normal acquisition methods, the Group also utilized an acquisition method of M&A, proactively acquiring income-generating properties and land for development as future sources of income.

As a result, consolidated revenue for the three months ended February 28, 2018 totaled ¥18,310 million (up 24.7% year on year), operating profit was ¥4,341 million (up 13.4%), profit before tax was ¥4,150 million (up 13.4%), and profit for the period was ¥2,847 million (up 13.9%).

Performance by business segment is shown below.

Revitalization Business

During the three months ended February 28, 2018, the segment sold 13 properties it had renovated, including Nishidai Tosei Building (Itabashi-ku, Tokyo), Kichichoji Ito Building (Musashino-shi, Tokyo), Kunitachi 219 Building (Kunitachi-shi, Tokyo) and T-Rhythmic SOKA (Soka-shi, Saitama). In addition, the segment sold 4 units in the Restyling Business from Hilltop Yokohama Negishi (Yokohama-shi, Kanagawa).

During the three months ended February 28, 2018, it also acquired a total of 17 income-generating office buildings and apartments and three land lots for renovation and sales purposes.

As a result, revenue in this segment was ¥14,425 million (up 31.9% year on year) and the segment profit was ¥3,793 million (up 11.0%).

Development Business

During the three months ended February 28, 2018, the segment focused on the sale of detached houses, for which there was firm demand. The segment sold 17 detached houses including THE Palms Court Kashiwa Hatsuishi (Kashiwa-shi, Chiba) , THE Palms Court Kamakura Shiromeguri (Kamakura-shi, Kanagawa), THE Palms Court Mitaka Shimorenjyaku (Mita-shi, Tokyo).

During the three months ended February 28, 2018, it also acquired one land lot for condominium project and land lot for 20 detached houses.

As a result, revenue in this segment was ¥766million (down 20.9% year on year) and the segment loss was ¥145 million (in comparison with segment loss of ¥173 million in the same period of the previous fiscal year).

Rental Business

During the three months ended February 28, 2018, while the segment sold 7 buildings of its inventory assets held for leasing purposes, it newly acquired 16 apartment. In addition, the segment made efforts to lease vacancies out following acquisitions and also focused on leasing activities for its existing non-current assets and inventory assets.

As a result, revenue in this segment was ¥1,396 million (down 5.1% year on year) and the segment profit was ¥630 million (down 4.6%).

Fund and Consulting Business

During the three months ended February 28, 2018, while ¥3,250 million was subtracted from the balance of assets under management (Note), due mainly to property dispositions by funds, ¥72,279 million was added to the balance of Assets under management ¥552,208 for the end of the previous fiscal year, due mainly to new asset management contracts of large projects the segment obtained. The balance of assets under management as of February 28, 2018, was ¥621,237 million. The acquisition of such large project contracts increased asset management fees and contributed to revenue.

As a result, revenue in this segment was ¥674 million (up 43.7% year on year) and the segment profit was ¥377 million (up 136.5%).

Note: The balance of assets under management includes the balance of assets that were subject to consulting contracts, etc.

Property Management Business

During the three months ended February 28, 2018, the segment made efforts to win new contracts and

maintain existing contracts. Consequently, the total number of properties under management was 660 as of February 28, 2018, an increase of 61 from February 29, 2017, with the total comprising 390 office buildings, hotels, schools and other such properties, and 270 condominiums and apartments.

As a result, revenue in this segment was ¥974 million (up 17.7% year on year) and segment profit was ¥108 million (up 43.0%).

Other

During the three months ended February 28, 2018, revenue in this segment was ¥72 million (there was no segment revenue in the same period of the previous fiscal year) and the segment profit was ¥6 million (in comparison with segment profit of ¥0 million in the same period of the previous fiscal year).

(2) Analysis of financial position

As of February 28, 2018, total assets were ¥124,675 million, an increase of ¥2,125 million compared with November 30, 2017, while total liabilities were ¥76,695 million, an increase of ¥303 million. This was primarily due to an increase in inventories, an increase in trade and other payables.

Total equity increased by ¥1,821 million to ¥47,980 million, mainly due to an increase in retained earnings and payment of cash dividends.

(3) Analysis of cash flows

Cash and cash equivalents (hereinafter “cash”) as of February 28, 2018 totaled ¥24,898 million, up ¥1,148 million compared with November 30, 2017.
The cash flows for the three months ended February 28, 2018 and factors contributing to those amounts are as follows:

Cash Flows from Operating Activities

Net cash provided by operating activities totaled ¥4,485 million (up 152.1% year on year). This is mainly due to profit before tax of ¥4,150 million and income taxes paid of ¥1,019 million.

Cash Flows from Investing Activities

Net cash used in investing activities totaled ¥1,483 million (in comparison with segment Net cash provided by investing activities of ¥61 million in the same period of the previous fiscal year). This is primarily due to purchase of investments in subsidiaries resulting in change in scope of consolidation of ¥1,335 million.

Cash Flows from Financing Activities

Net cash used in financing activities totaled ¥1,852 million (down 5.1% year on year)This mainly reflects ¥9,815 million in the repayments of non-current borrowings and ¥1,157 million in cash dividends paid, despite ¥9,032 million in proceeds from non-current borrowings.

(4) Operational and financial issues to be addressed

During the three months ended February 28, 2018, there was no significant change in issues to be addressed by the Tosei Group.

The Company has set the basic policy regarding the persons who control the decision-making on the financial and business policies of the Company. The contents of basic policy (matters set forth in Article 118, item 3 of the Ordinance for Enforcement of the Companies Act) are as follows:

a.Contents of basic policy

The Company believes that the persons who control decisions on the Company’s financial and business policies need to be persons who fully understand the details of the Company’s financial and business affairs and the source of the Company’s corporate value and who will make it possible to continually and persistently ensure and enhance the Company’s corporate value and, in turn, the common interests of its shareholders.

The Company believes that ultimately its shareholders as a whole must make the decision on any

proposed acquisition that would involve a change of control of the Company. Also, the Company will not reject a large-scale acquisition of the shares in the Company if it will contribute to the corporate value of the Company and, in turn, the common interests of its shareholders.
Nonetheless, there are some forms of large-scale acquisition of shares that benefit neither the corporate value of the target company nor the common interests of its shareholders including those with a purpose that would obviously harm the corporate value of the target company and the common interests of its shareholders, those with the potential to substantially coerce shareholders into selling their shares; those that do not provide sufficient time or information for the target company's board of directors and shareholders to consider the details of the large-scale acquisition, or for the target company's board of directors to make an alternative proposal and those that require the target company to discuss or negotiate with the acquirer in order to procure more favorable terms for shareholders than those presented by the acquirer.

It is particularly necessary and essential for the persons who make decisions on the Company's financial and business policies to (i) maintain the system under which the Company group covers with its comprehensive capability the five business fields and peripheral fields that allow the "integration of real estate and finance," which leads to maximization of the potential of the Company group, (ii) maintain employees who support those businesses with knowledge and experience specializing in real estate and finance, etc., (iii) maintain the Company's trust in the real estate industry that has been built up over a long period of time based on the establishment of the ability and information networks supporting various value creation technologies, and (iv) master knowhow that enables comprehensive business. Unless the acquirer of a proposed large-scale acquisition of the shares in the Company understands the source of the corporate value of the Company as well as the details of financial and business affairs of the Company and would ensure and enhance these elements over the medium-to-long term, the corporate value of the Company and, in turn, the common interests of its shareholders would be harmed.

The Company believes that persons who would make a large-scale acquisition of the shares in the Company in a manner that does not contribute to the corporate value of the Company or the common interests of its shareholders would be inappropriate as persons that control decisions on the Company's financial and business policies. The Company believes that it is necessary to ensure the corporate value of the Company and, in turn, the common interests of its shareholders by taking necessary and reasonable countermeasures against a large-scale acquisition by such persons.

b.Overview of special measures to realize the basic policy

The Company group newly formulated a medium-term management plan called "Seamless Growth 2020" (the targeted period of the plan is three years from December 2017 to November 2020), kicking off in the fiscal year ending November 30, 2018. The major policy of the plan is "to continue growth as a Group to build a firm position as an original comprehensive real estate company," under which we aim to establish new income-generating business, while targeting further growth of the five existing businesses and increases in their operating profit. In addition, we will endeavor to increase profits from the Rental, Fund and Consulting and Property Management Businesses, which are positioned as the stable businesses, to enable a structural balance between profits from the Revitalization and Development Businesses so as to reinforce our resilience to changes in the business environment. On the financial front, we will enhance funding capabilities, through methods such as the extension of borrowing periods to maintain a sound financial structure as the infrastructure that supports the expansion of business scale, while aiming at effective investments. In addition, as the composition of the Company group's trade diversifies in line with the expanding business scale, we will further enhance the quality of internal control, namely, compliance, risk management, and disclosure, to establish an optimum corporate governance structure.

Furthermore, we recognize that human resources that are the most important assets of the Company, and to leverage these assets, we will drive ahead with the development of next-generation executives, all officers and employees and the fostering of human resources for the improvement of productivity, while increasing the satisfaction of employees of the entire Group. At the same time, we will strive to establish a corporate brand befitting the firm position as a group of original comprehensive real estate companies and reinforce the attractiveness of our product brand that will be trusted by the market.

c.Overview of measures to prevent decisions on the Company's financial and business policies from being controlled by persons deemed inappropriate according to the basic policy

The plan is a measure to prevent decisions on the Company's financial and business policies from being controlled by persons deemed inappropriate under the above basic policy, and its objective is to ensure and enhance the Company's corporate value and, in turn, the common interests of its shareholders.

The plan stipulates procedures that must be followed in any cases of purchase, etc. of share certificates, etc. of the Company ((i) a purchase or other acquisition that would result in the holding ratio of share certificates, etc. (kabuken tou hoyuu wariai)of a holder (hoyuusha) totaling at least 20% of the share certificates, etc. issued by the company; or (ii) a tender offer (koukai kaitsuke) that would result in the party conducting the tender offer's ownership ratio of share certificates, etc. and the ownership ratio of share certificates, etc. of a person having a special relationship totaling at least 20% of the share certificates, etc. issued by the Company; or (iii) any similar action to (i) or (ii) above)
In practical terms, the acquirer must provide the Company a statement of undertaking (acquirer's statement) and an acquisition document that includes essential information, etc. before making the acquisition, etc.

Upon receiving these documents, the independent committee, while obtaining independent expert advice, will conduct its consideration of the acquisition terms; collection of information on materials such as the management plans and business plans of the acquirer and the Company's board of directors and comparison thereof; consideration of any alternative plan presented by the Company's board of directors, and the like; and discussion and negotiation with the acquirer. The Company will disclose information in a timely manner.

When (i) the acquisition is not in compliance with the procedures prescribed in the plan or (ii) it threatens to cause obvious harm to the corporate value of the Company, and, in turn, to the common interests of shareholders, (iii) and it is reasonable to implement the gratis allotment of stock acquisition rights, the independent committee will recommend the implementation the gratis allotment of stock acquisition rights to the Company's board of directors. In addition, when a meeting of shareholders is convened to confirm the intent of the Company's shareholders, the Company's board of directors will respond to the shareholders' intent. These stock acquisition rights will be allotted with an exercise condition that does not allow, as a general rule, the acquirer to exercise the rights and an acquisition provision to the effect that the Company may acquire the stock acquisition rights in exchange for shares in the Company from persons other than the acquirer. The Company's board of directors, in exercising its role under the Companies Act, will pass a resolution relating to the implementation or non-implementation of the gratis allotment of stock acquisition rights, respecting the recommendation of the Independent Committee to the maximum extent. In addition, when a meeting of shareholders is convened to confirm the intent of the Company's shareholders, the Company's board of directors will respond to the shareholders' intent. If the procedures for the plan have commenced, the acquirer must not effect an acquisition until and unless the Company's board of directors resolves not to trigger the plan. The effective period of the plan expires at the conclusion of the ordinary general meeting of shareholders for the last fiscal year ending within three years after the conclusion of the 68th Ordinary General Meeting of Shareholders. However, if, before the expiration of the effective period, the Company's board of directors resolves to abolish the plan, the plan will be abolished at that time.

d.Decisions by the Company's board of directors regarding specific measures and reasons therefor

Company's board of directors deems that the new medium-term management plan and other measures such as the efforts to enhance the corporate value and the strengthening of corporate governance were establishedas specific measures to continuously and sustainably enhance the corporate value of the Company and, in turn, the common interests of its shareholders, and that these are truly in accordance with the basic policy, not detrimental to the common interests of the Company's shareholders and not for the purpose of maintaining the positions of the Company's corporate officers.

In addition, the Company's board of directors deems that the plan is not detrimental to the common interests of the Company's shareholders, not for the purpose of maintaining the positions of the Company's corporate officers, and in accordance with the basic policy based on the following reasoning: approval from the general meeting of shareholders must be obtained for its renewal; its effective period is stipulated as a maximum of three years and it can be abolished at any time by the resolution of the Company's board of directors; an independent committee, which is composed of members who are independent from the management of the Company, has been established; in the event that the plan's

countermeasures are triggered, the Company must obtain a resolution by the independent committee when making a decision for triggering the countermeasures in the plan, and the plan fully satisfies the three principles set out in the Guidelines Regarding Takeover Defense for the Purposes of Protection and Enhancement of Corporate Value and Shareholders' Common Interests released by the Ministry of Economy, Trade and Industry and the Ministry of Justice on May 27, 2005.

(5) Research and development activities

No item to report.