The Main Questions and Answers during the briefing on

Financial Results for the First Six Months of the Fiscal Year Ending November 30, 2020

Event date: July 6, 2020

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*Certain questions and answers have been edited to facilitate understanding.

*The following Q&As include questions that we were unable to answer due to time constraints.

Details of the recorded valuation loss

Q You posted a large amount of valuation loss. Am I correct in understanding that values for every type of assets decreased? Is the real estate market in such poor condition?

A Look at the list below.

Most of the valuation loss of ¥7.6 billion is attributable to developed hotels (¥5.0 billion) and commercial facilities (¥0.9 billion). We thought that both types of properties should be valuated negatively based on the assumption that it would take time to attract as many customers as before. We also recorded valuation losses on other types of assets based on conservative scenarios but hotels and commercial facilities account for most of them. Going forward, we will revise valuations upward if there is any improvement in market conditions, such as a recovery in occupancy rates for hotels and commercial facilities after COVID-19 is contained.

(¥million)		Total No. of Properties	Book Value Before recording valuation loss	Recording Valuation Loss			Book Value After recording valuation loss	Preconditions for assessment based on COVID-19		Preconditions for assessment after convergence of COVID-19
				No. of Properties	Amount	%		Buyer's CAP Rate	Rental Income	
Development Business	Hotel	6	15,411	5	-5,092	-33%	10,318	＋1.0%	Occupancy rate Before : around 90% After : 60% to 70%	If occupancy rates and cap rates are seen improving due to the recovery of demand, for in-bound and business uses
	Commercial Facility	4	4,515	3	-910	-20%	3,605	＋0.5%	Revised down future rent income 20%	If rents are seen rising to expected levels due to the recovery of in-bound and domestic consumption
	Rental Apartment	3	1,424	2	-218	-15%	1,206	＋0.5%		If cap rates are seen declining due to a decrease in risk premiums
	Detached House Land Lots	17	6,839	1	-2	-0%	6,837	No Change		
	Condominium	2	1,338	0	0	-	1,338	No Change		
	Logistic Facilities	2	4,920	0	0	-	4,920	No Change		
Revitalization Business	Income-generating Properties	77	40,292	23	-1,457	-4%	38,834	＋0.5%		If cap rates are seen declining due to a decrease in risk premiums
Total		111	74,742	34	-7,680	-10%	67,061			

Q If you use the lower-of-cost-or-market method, do you think it would be better to assume a more conservative hotel occupancy rate (60% to 70%)?

A Occupancy rates for hotels owned by the Company were 90% or higher before the outbreak of COVID-19. However, recent rates have been around 20% against the backdrop of the current COVID-19 crisis. We consider that hotel occupancy rates calculated based on the lower-of-cost-or-market method reflect performance evaluations based on certain reasonable assumptions, and with this in mind, we assume that occupancy rates would rise to 60% to 70% in two to three years, when COVID-19 is expected to be contained and economic activities will return to normal to some extent. If hotel occupancy rates recover to the pre-COVID-19 level of 90% or higher, going forward, we will revise valuations upward.

Plan for the FY2020 second half

Q Why is the Revitalization Business expected to be unprofitable in the second half?

A In the second half, we expect that profit will be at a lower level compare to the first half because it is assumed that sales will include properties for which valuation losses are recorded.

Acquisition policy

Q Are there any changes in the new property acquisition strategy following the spread of COVID-19? How soon will you start to make investments again?

A Before the outbreak of COVID-19, we actively acquired land to develop hotels. Going forward, however, we will seek to acquire properties with a focus on logistics facilities, residential, and small- and medium-sized offices that are not easily affected by COVID-19.
We have restarted acquisition operations gradually. Based on the assumption that prices will be in a downward cycle, going forward, we intend to conduct acquisition selectively while carefully observing market trends. We see the current real estate market turmoil as an opportunity and seek to reinforce operation structures to ensure that we can increase acquisition at the lowest price ranges.

Real estate market

Q Some people expect demand for offices to decline due to the establishment of teleworking, among other factors, in the post-COVID-19 society. What is your medium- to long-term estimate for buildings in central Tokyo and those categorzied as B-class properties, for which Tosei has competitive advantages.

A Medium- and small-sized offices with less than 50 employees account for approximately 95% of all offices in Tokyo and progress is sluggish among small- and medium-sized companies in adopting teleworking, despite the declaration of a state of emergency attributable to COVID-19. Taking these factors into consideration, we do not expect that demand for offices in central Tokyo will decline dramatically. Indeed, the number of people who adopt teleworking or use satellite offices will increase at a certain pace, down the road. We think that such increases will have a limited impact and there will be continuous demand for buildings categorized as B- or C-class properties.

Q Is there an increase in demand for detached houses and condominiums located in the suburbs as a result of the popularization of teleworking? Or is there a decline in sales of housing units due to concern over the deterioration of economic conditions?

A Newspapers and other media report that detached houses in the suburbs will draw interest due to the popularization of work from home, because people can secure working spaces in their homes. However, demand for such houses, which may rise to some extent, will have a limited impact, and we do not think that such houses will set a significant trend. The number of inquiries we receive for such houses is very small in conjunction with our properties for sale.
With respect to our detached houses, we were unable to facilitate sales activities, because we closed sales offices in April and May to comply with the stay-at-home request due to COVID-19. After we restarted sales in June, we have seen customers starting to contact us gradually.

Trends in customer sentiment

Q Do you see any change in customer sentiment?

A Many real estate investors were taking in the wait-and-see attitude due to the spread of COVID-19. Even so, institutional investors in countries such as Europe, the United States, China, South Korea and Singapore have established new risk premiums and restarted to make investments or preparations therefor. Meanwhile, affluent individuals and companies appear to have lost interest in making investments due to banks' conservative property evaluations and their attitude to keep leverage down. Therefore, we understand that markets for income-generating properties with a value of less than ¥500 million are shrinking.

Q Do you notice any change in the lending stance of financial institutions after the outbreak of COVID-19 (such as LTV, interest rate and more selective lending stance)?

A With respect to the lending stance for customers, we see some banks providing conservative evaluations for income-generating apartments for affluent individuals and small-size properties with a value of less than ¥500 million, among other properties. On the other hand, we notice their lending stance remaining as usual with respect to large-size properties for funds and institutional investors. There is no change in their lending stance for us. They responded favorably to the speedy posting of a write down and gave an appreciation for our solid management.

Recovery scenarios

Q Looking ahead to FY2023, you envisioned a U-shaped recovery trend, indicating no growth until FY2021 as the simulation for recovery over the upcoming years in the presentation material. Is business expected to be in such a difficult environment in FY2021?

A With respect to the Rental Business, the Fund and Consulting Business and the Property Management Business that showed strong performances despite the COVID-19 crisis, we assume that profits will be secured at a certain level or higher in the next year and thereafter, which will cover the SG&A and interest expenses. For the Revitalization Business and the Development Business, given the difficulty of forecasting how soon COVID-19 will be contained, we are assuming the worst scenario in which the real estate investment market continues to be sluggish with no economic recovery in sight until the end of the next year. However, some analysts expect the real estate investment market to recover in a short period due to global financial relaxation and excess liquidity. Taking this analysis into consideration, we may be able to achieve an upswing in revenue and ride on a V-shaped, instead of U-shaped, recovery trend, depending on the containment of COVID-19, financial policies implemented by respective governments, economic trends and real estate market conditions.

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