SUMITOMO MITSUI TRUST RESEARCH INSTITUTE

NEWS RELEASE

Survey on Private Real Estate Funds in Japan

July 2015– Results

September 4, 2015

Sumitomo Mitsui Trust Research Institute Co., Ltd

- Starting in 2003, Sumitomo Mitsui Trust Research Institute Co., Ltd. has conducted the "Survey on Private Real Estate Funds" as part of its research activities concerning real estate investment markets. This is the 20th survey based on responses to questionnaires received from 58 real estate asset managers.
  - Survey subject: Real estate investment asset managers that set up and manage private real estate funds which focused on Japanese real estate
  - The number of questionnaires sent: 106
  - The number of responses: 58 (ratio of valid responses: 54.7%)
  - Survey period: July 2015
  - Survey methodology: Questionnaire survey sent by post and e-mail
- Based on the results of the survey, hearings and published information, we estimated the market size of private real estate funds (on an invested asset basis) as of the end of June 2015 to be 15.1 trillion yen. This figure involves Japanese assets of global funds (*) that we were aware of. Although the market size decreased approximately 50.5 billion yen (0.3%) from the previous January 2015 survey (15.1 trillion yen), it has remained almost unchanged.

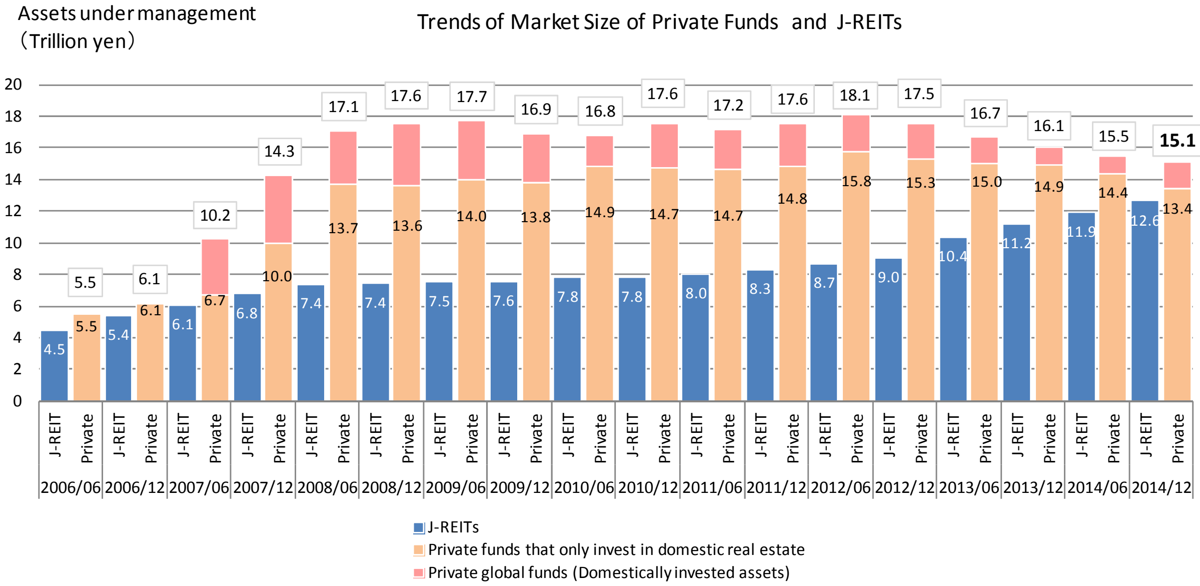
The market size of private real estate funds is 15.1 trillion yen including Japanese assets of global funds

・Assets under management (AUM) as of the end of June 2015 were 15.1 trillion yen. Although the market size decreased approximately 50.5 billion yen (0.3%) from the last survey, it has remained almost unchanged.

・The number of asset managers whose assets under management increased exceeded the number of asset managers whose assets under management decreased. Meanwhile, there were some asset managers for which assets under management decreased significantly due to factors such as the termination of funds. Overall, assets under management remained mostly flat, and the AUM of domestic private real estate funds and global private funds each remained almost unchanged from the previous survey.

・In contrast to J-REIT which has been continually expanding the market size, that of private real estate funds had been shrinking mainly due to selling part of the property holdings since the survey at the end of December 2012. In this survey, the market size remains mostly flat compared to the previous survey. It appears that the downward trend in the market may have been stemmed. Although acquiring properties in the real estate trading market remains difficult, a number of asset managers are planning to set up their funds within a year, and almost all managers show their active attitude in terms of acquiring properties. The market of private real estate funds is expected to expand again and grow healthy.

(*) We define "global fund" as a fund targeting real estate investments in various countries including Japan.



“ Survey on private real estate funds” July 2015 Survey Results

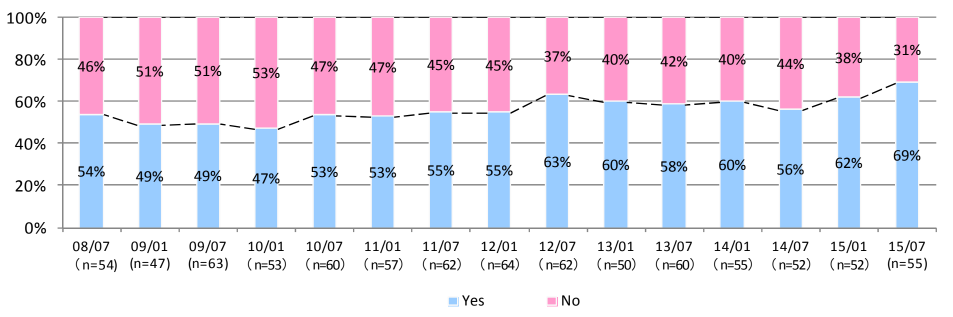
(Note) [n] shown in the figures throughout this document indicates the number of effective responses.

1. Current Status of Real Estate Fund Management Business

1) Management of Overseas Capital

In response to the question as to whether they manage overseas capital, 69% of the respondents chose “*Yes*” (Fig.1). The percentage of respondents who chose “*Yes*” was the highest since the July 2008 survey, which indicates that the interest of foreign investors has increased.

Fig.1 Do yo manage overseas capital?

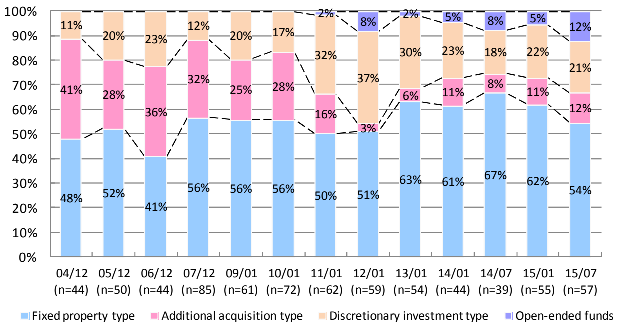


2) Status of the Funds under Management – Results of the funds currently operating and agree to disclose their data

The response from the currently operating funds showed that *“Fixed property type,”* by fund type and *“Core”* by management style continued to have a majority (Fig.2 and Fig.3), however *“Open-ended funds”* by fund type accounted for 12%, the largest share ever.

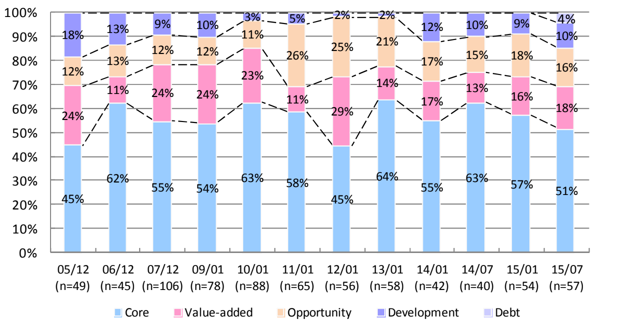
By target property type, the ratio of *“Office”* and *“Retail”* slightly increased, on the other hand, that of *“Industrial”* slightly decreased from the previous survey. (Fig.4) The breakdown of target properties by area remained almost unchanged from the previous survey. “*23 wards of Tokyo*” accounted for the largest percentage, and the percentage of “*Tokyo metropolitan area*” and “*Kinki area*” were close to that of “*23 wards of Tokyo*” (Fig.5) Taken together, these results indicate that investors’ needs for low-risk stable management funds, such as “*Fixed property type*” and “*Core*” remain strong. In addition, because acquiring properties remain difficult, a trend has emerged of diversifying target property types and areas of target properties.

Fig. 2 Fund types



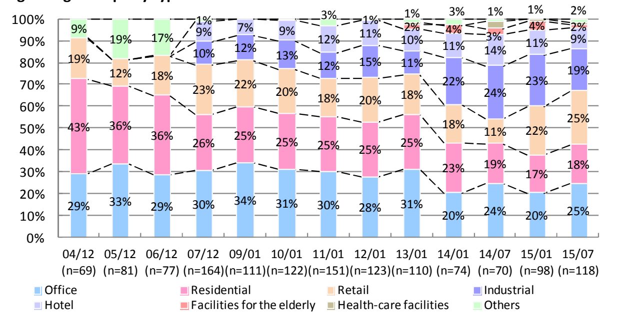
・"Open-ended funds" was added from the January 2011 survey.

Fig. 3 Management Style



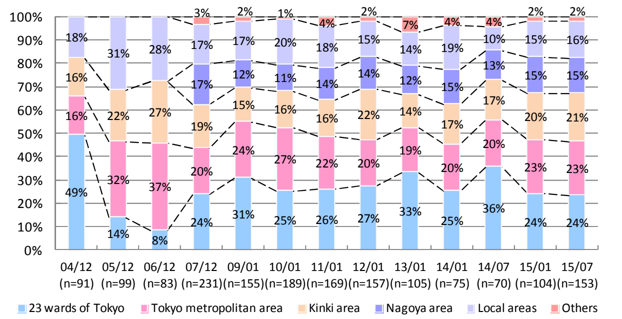
・"Debt" was added to management investment style from the January 2013 survey.

Fig. 4 Target Property Types



・In the December 2004 survey through the December 2006 survey, Industrial and Hotel types were included in "Other types."
・"Facilities for the elderly" and "Health-care facilities" was added from the January 2013 survey.

Fig. 5 Target Areas



・In the December 2003 survey, the Kinki and Nagoya areas were included in Local areas, whereas in the December 2004 survey through the December 2006 survey, the Nagoya area was included in Local areas.

The average investment period of the funds currently under management was 7.3 years and the targeted investment period of the funds scheduled to be launched within a year was 6.4 years, each of them got shorter than the previous survey. (Fig.6) Regarding the range of investment period of the funds currently under management, the share of "*At least five years but less than seven years*" rose to 51% from 29% in the previous survey, however the share of "*Ten years or more*" fell to 23% from 32%. The aggregated share of *"Less than five years"* accounted only 8%, it shows that middle and long term funds accounted for the most in the market. (Fig.7)

Fig. 6 Average Target Investment Period

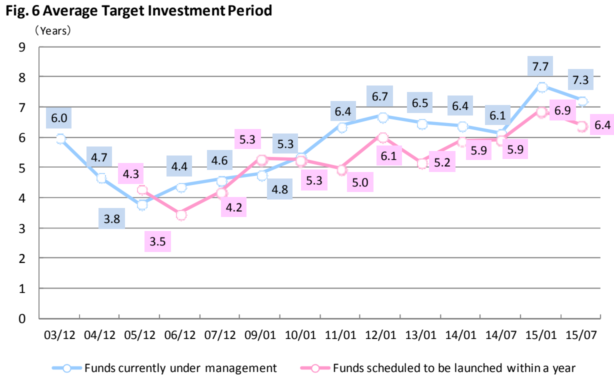
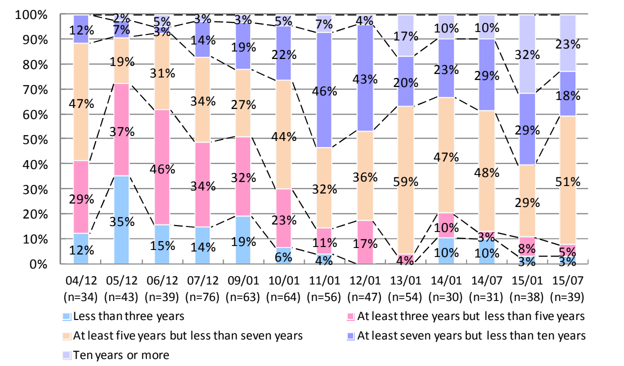


Fig. 7 Breakdown of Average Target Investment Period



With respect to the average LTV level of the funds currently under management was moderate decreasing and that of the funds scheduled to be launched within a year was generally rising since the January 2009 survey. In this survey, the average LTV level of the funds currently under management was 64.9%, that of the funds scheduled to be launched within a year was 65.3%, there is not much difference between them. (Fig.8)

Regarding the range of the LTV level of the funds currently under management, the largest share of respondents chose *"At least 60% but less than 70%"*, and the share of *" 80% or more"*, so-called highly leveraged funds, has been increasing (Fig.9). Meanwhile, the share of *"At least 40% but less than 50%"* including many answers of open-ended funds increased, the average LTV level slightly decreased from the previous survey as a result. Also, regarding the range of the LTV level of the funds scheduled to be launched within a year, the share of *"80% or more"* accounted for only 5%. (Fig.11) Considering these findings, we assume that although the environment continues to allow for debt financing to be made on favorable terms, it is unlikely that highly leveraged funds will be the mainstream as they were from 2005 to 2007. As for closed-ended funds, funds whose LTV level is from 60% to 70% will continue to be the mainstream.

With respect to the average target IRR of the funds currently under management, the average target IRR of all funds remained unchanged, there were discretionary funds aiming for high returns. The average target IRR for discretionary funds was 20.9% (Fig.10).

Fig. 8 Average LTV Ratio

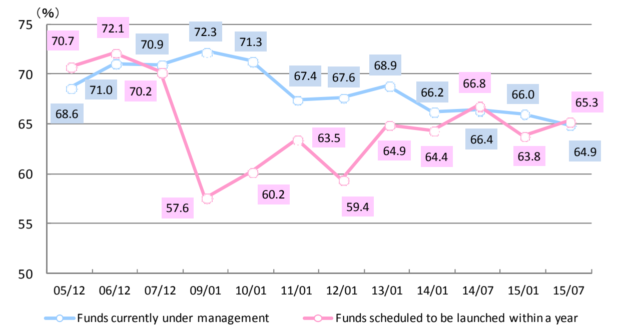


Fig. 9 Range of LTV level (Funds currently under management)

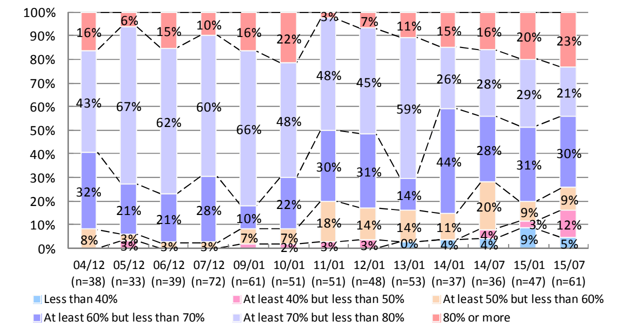


Fig.10 Average Target IRR(Funds currently under management)

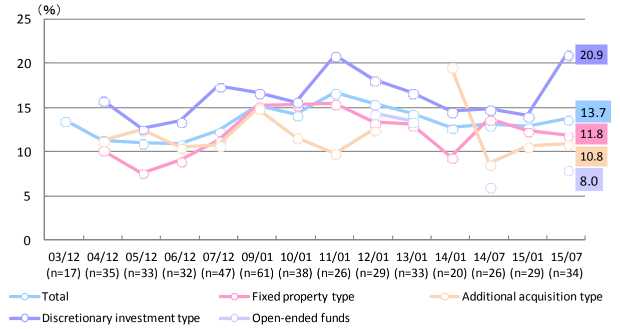
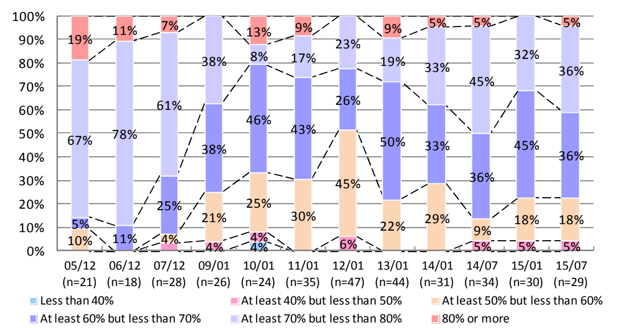


Fig. 11 Range of LTV level (Funds scheduled to be launched within a year)

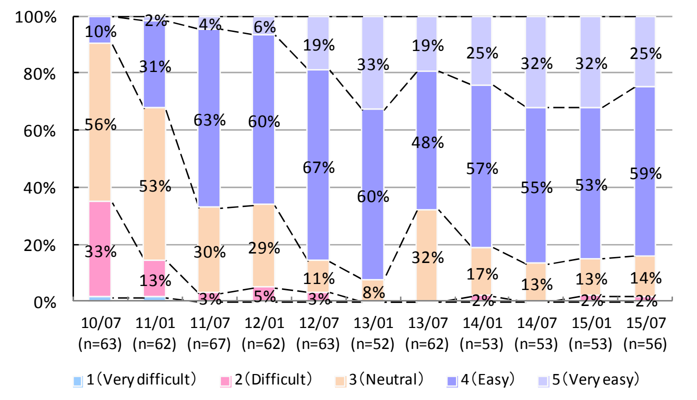


※In our questions, we distinguish the loan-to-total assets ratio and the loan-to-acquisition value ratio. The average LTV level is calculated based on the loan-to-acquisition value ratio.

3) Debt Finance

Regarding debt financing, while the share of *"5 (Very easy)"* slightly declined, the aggregated share of *"4(Easy)"* and "5" accounted for more than 80%. Looking at surveys conducted in the past, 33% of the respondents chose "Difficult" in the July 2010 survey, but the debt financing environment improved remarkably in the following two years. Since the July 2012 survey, excluding the July 2013 survey, more than 80% of the managers responded either "4" or "5", the debt financing environment seems to remain favorable for the managers (Fig.12).

Fig.12 Circumstances of Debt Financing



4) Equity Raising

a. Appetite of Equity Investors

With respect to the appetite of equity investors, no respondents answered "*Declining*", while the share of responses of "*No change*" rose to 61% from 28% in the previous survey. (Fig.13) However, it can be inferred that many asset managers who chose "*No change*" thought that investors' appetite remained strong.

As to the property type, the hotel sector had the highest percentage responding with "*Increase significantly*" and "*Increase*" for both domestic and foreign investors. The total share of "*Increase significantly*" and "*Increase*" accounted for 81% for domestic investors, 75% for foreign investors. This indicates that given an increase in the number of inbound tourists and the 2020 Tokyo Olympics, the appetite of both domestic and foreign investors rose. (Fig.14-1, Fig.14-2). Meanwhile, in the previous survey, a total of 70% of the domestic investors chose "*Increase significantly*" or "*Increase*" for elderly facilities. In this survey, the percentage fell to 50%. The share of responses of "*No change*" increased from the previous survey in all property types excluding the hotel sector for both domestic and foreign investors, as mentioned above, not showing the decline of the appetite of investors but suggesting that many managers who chose "no change" thought that investors' appetite remained strong.

Fig.13 Appetite of Equity Investors

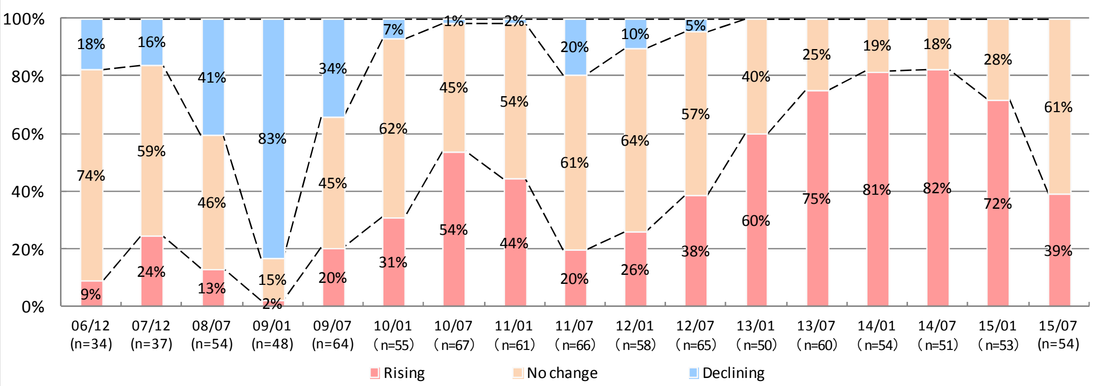


Fig. 14-1 Domestic Investors' Appetite by Type of Target Property

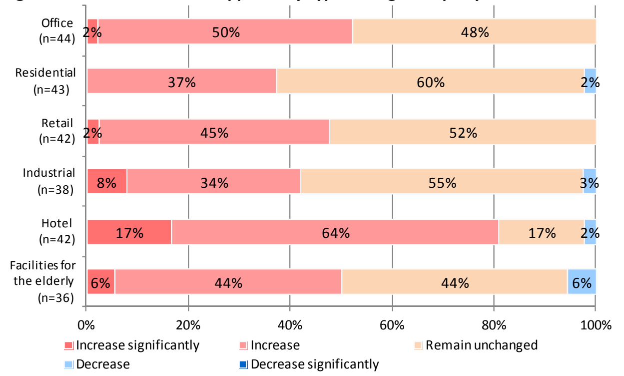
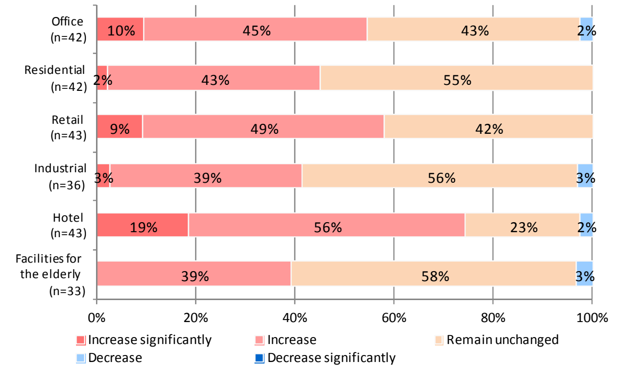


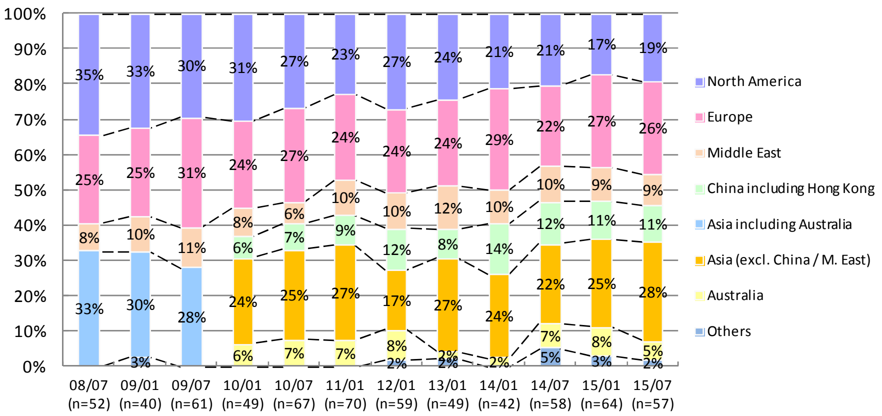
Fig. 14-2 Foreign Investors' Appetite by Type of Target Property



b. Sources of Overseas Capital (or Foreign Funds) by Country or Region

With respect to the capital sources from overseas, the highest response rate was for investors from *"Asia (excl. China /M.East)"* at 28%, followed by *"Europe"*. The share of *"Europe"* tends to exceed that of *"North America"* since the January 2014 survey. (Fig.15).

Fig. 15 Sources of Overseas Capital by Country or Region



・Since the January 2010 survey, Asia-Pacific has been broken down into China, Middle East, Asia (excl. China / M East), and Australia.
・Since the January 2010 survey, China has been changed to China including Hong Kong.

c. Reasons for Foreign Investors Investing / Not Investing in Japan (Multiple answers allowed)

As for the reasons for investors investing in Japan, majority of the respondents chose "*Relatively attractive due to the yield gap*", "*The size of the real estate market is large*"," *Highly stable income" and* "*Allocation as part of the global portfolio*". (Fig.16). These choices have been the major reasons indicated in every survey in the past, and have been established as the reasons for foreign investors investing in Japan. Meanwhile, in this survey, the number and percentage of "*Expected positive effects of exchange rates*" rose from the previous survey (10 respondents, 7% →16 respondents,11%). This indicates that the continuation of the weaker yen was an incentive for foreign investors to invest in the real estate market in Japan.

As the reasons for not investing in Japan, majority of the respondents chose *"Lack of growth potential in GDP, consumption, population, etc."*, *"Lack of attractive investment opportunities"* and *"Rising in real estate prices"* (Fig.17).

Fig.16 Reasons for Foreign Investors Investing in Japan (Multiple answers allowed) n=143（Respondents36）

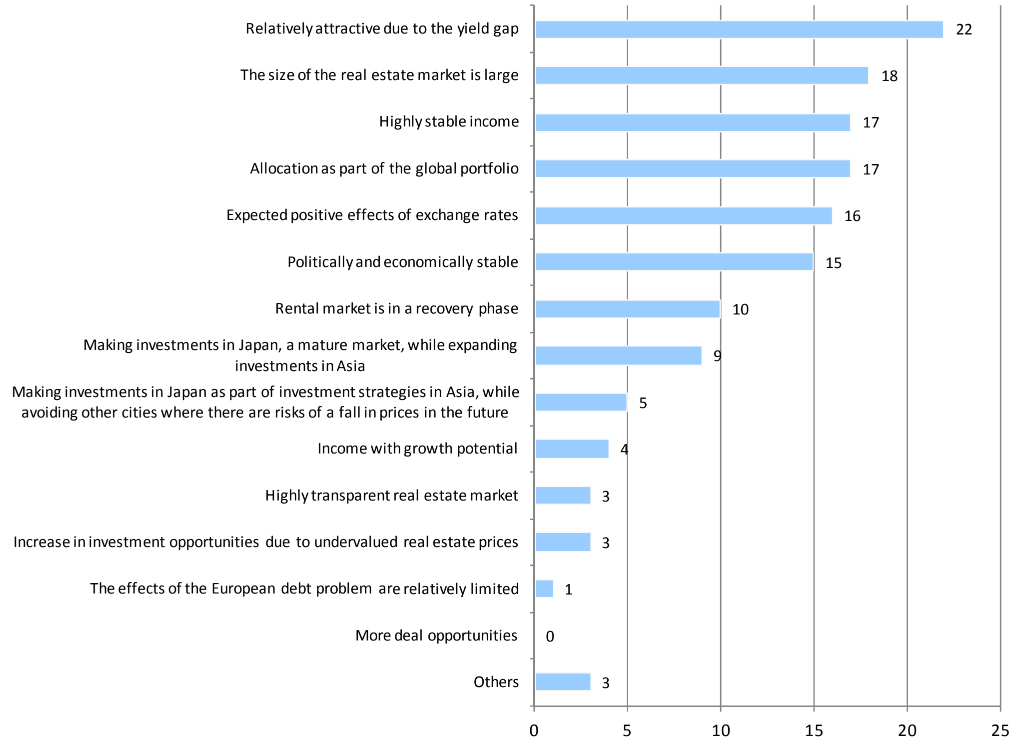
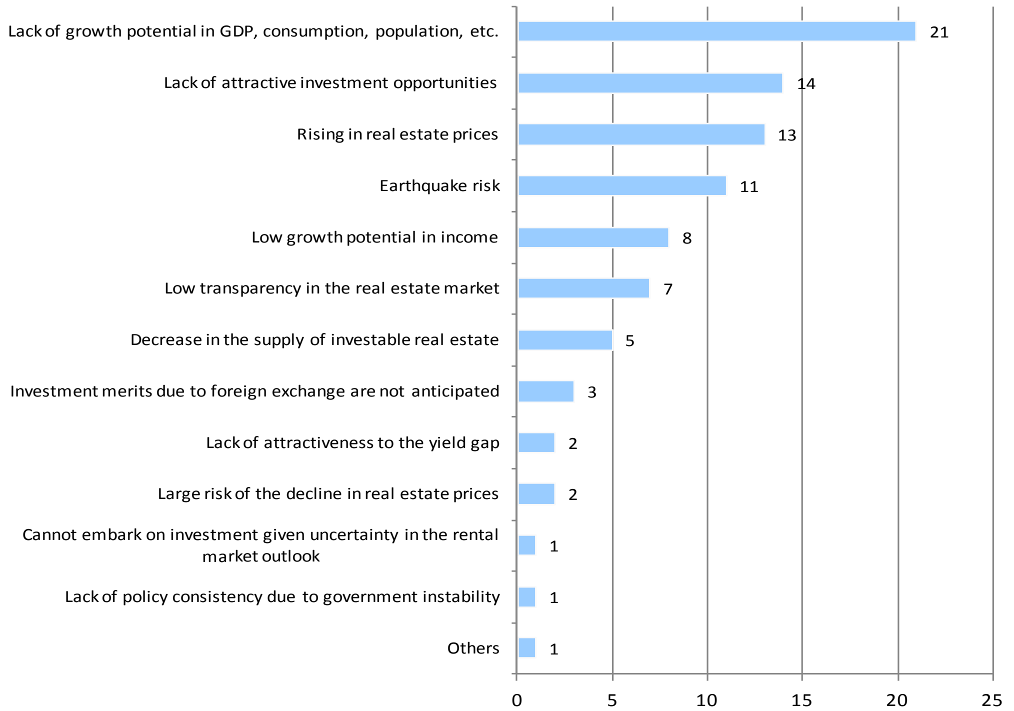


Fig.17 Reasons for Foreign Investors Not Investing in the Japanese Real Estate Market (Multiple answers allowed) n=89（Respondents33）



d. Acquisition and Disposition of Properties in the January to June 2015

As to a survey on the acquisition of properties in the January to June 2015, 71% of the respondents answered that they had acquired properties. The share of respondents who answered they had acquired properties has been increased since the January 2014 survey. (Fig.18). The main reasons that the managers did not acquire any properties were *"Can't agree on prices"* and *"Severe competition in bids"* , the total share of those reason accounted for 83% (Fig.19), which suggests that the environment for acquisitions of properties remained challenging.

A survey on the disposition of properties in the January to June 2015 reveals that 64% of the managers sold properties (Fig.20). Most of them who did not sell any properties chose *"Did not plan to sell from the outset"* as their reason, while the share of *"Can't agree on prices"* accounted for only 5%. (Fig.21). The current real estate market seems to be favorable to sellers.

Fig.18 Circumstances for Acquisition

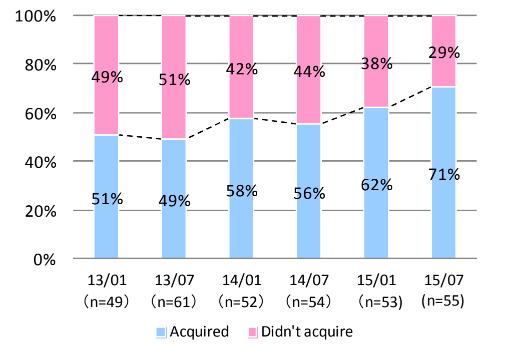


Fig.19 Reason for not acquiring property

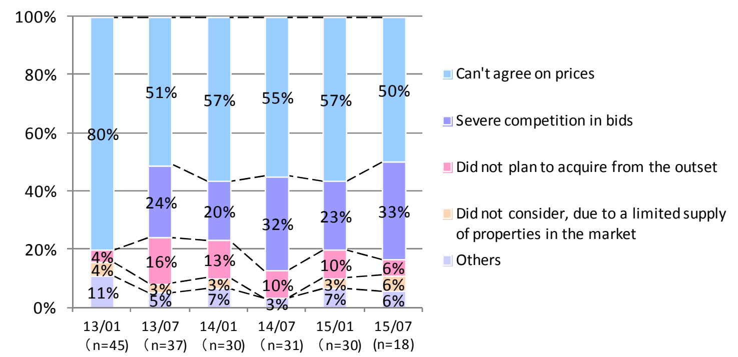


Fig. 20 Circumstances for Disposition

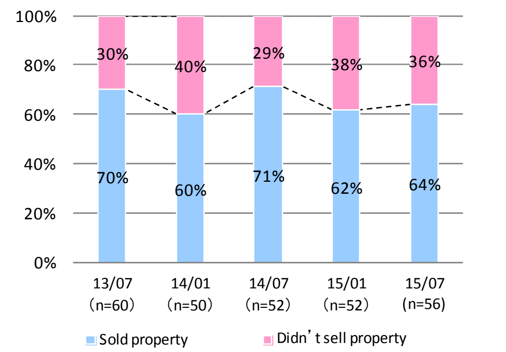
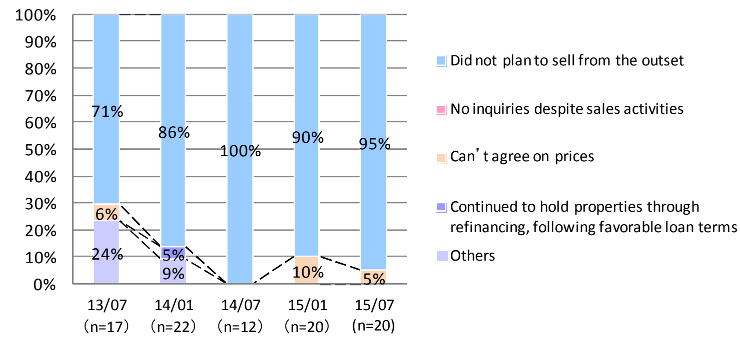


Fig. 21 Reason for not Selling Property



2. Plans and Investment Strategies of Asset Managers

1). Plans of Launch of New Funds and Acquisition /Disposition of Properties within a year

Regarding the funds scheduled to be launched within a year, 81% of respondents answered that they *"Plan to launch"*. almost 80% of managers responded that they had planned to launch new funds within a year since the January 2014 survey.(Fig.22)

As to plans of acquiring properties within a year, the share of respondents that they plan to acquire properties has been increased since the July 2014 survey, it accounted for 98% in this survey.(Fig.23). On the other hand, the share of respondents that they plan to sell properties within a year accounted for 63%.(Fig.24) . Although the supply of investment-grade properties was low throughout the entire market, most of the asset managers exhibited a positive attitude for acquisition of properties. The market is thus expected to be favorable for sellers for some time to come.

Fig.22 Plans of Launch of New Funds

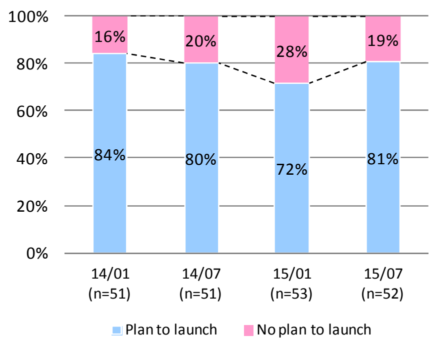


Fig.23 Plans of acquiring properties

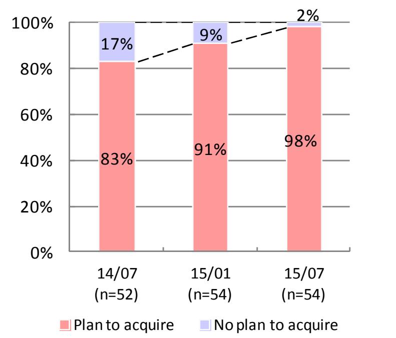
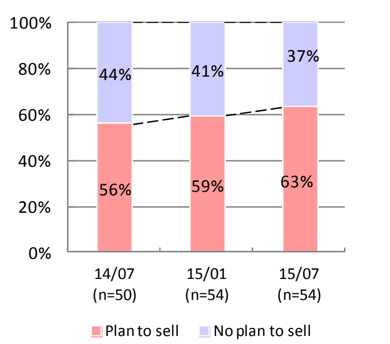


Fig.24 Plans of selling properties



2). Investment Strategies of Asset Managers

a. Target Property Types (Multiple answers allowed)

In terms of the target property types, "*Office*" was chosen by the largest percentage of the respondents, followed by "*Retail*" and "*Hotel*"(Fig.25) It is inferred that the numbers of managers who focus on the hotel sector have been increasing due to rising appetite of both domestic and foreign investors for the sector.

b. Target Areas (Multiple answers allowed)

In terms of the target area, the aggregated share of *"Central 5 wards of Tokyo"* and *"23 wards of Tokyo (excluding central 5 wards)*" slightly increased from the previous survey. The share of *"Kinki area"* accounted for 19%, the same as the previous survey, almost same as that of "*Tokyo metropolitan area* (20%)" (Fig.26) Because it remains difficult to acquire good properties, especially in central Tokyo, target properties have been dispersed to different areas. In recent surveys, the Kinki area and the Nagoya area appear to have been established as priority areas.

Fig. 25 Target Property Types (Multiple answers allowed)

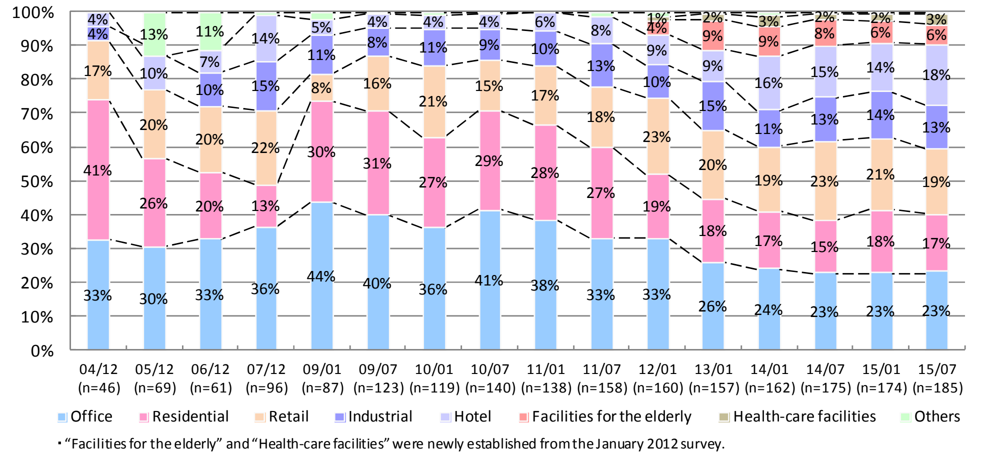
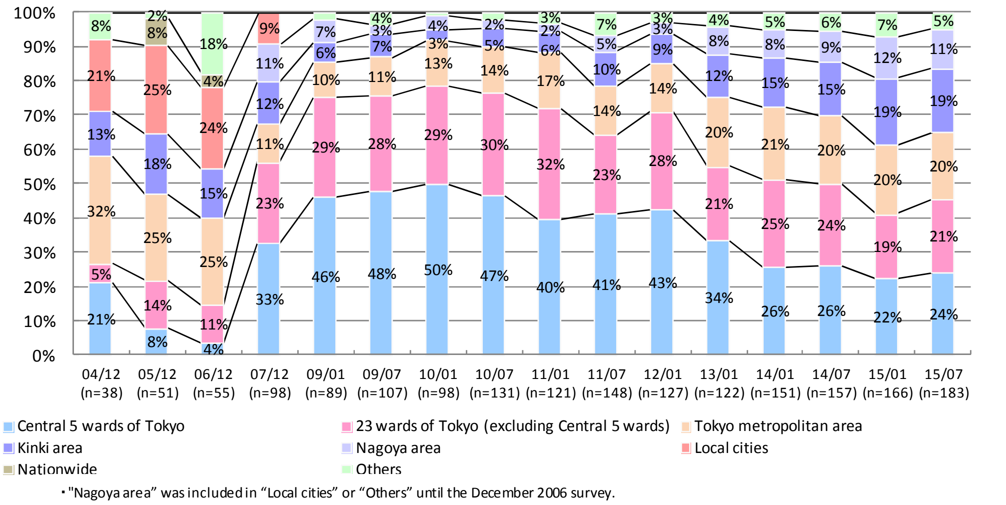


Fig. 26 Target Areas (Multiple answers allowed)



3. Business Environment of Private Real Estate Investment Management

1) Involvement in Open-Ended Private Funds (so-called Private REITs)

Regarding involvement in open-ended private funds (so-called private REITs), 20 managers, the largest number of respondents, chose "*Seek to develop a better understanding and gather information, but not working on a detailed study*". On the other hand, 10 managers answered that they "*Have already launched*", *and* 4 managers chose "*Preparing for a launch after consideration*," we expect that private REITs will increase on the back of equity investors' strong investment appetite (Fig.27).

In terms of important factors for development in the private REITs market in the future, the largest numbers, 24 managers chose "*Expansion of the numbers of private REITs and the asset size*" and "*Enhancement of the track record*", followed by "*Expansion of the number of investors to invest in funds,*" and "*Improvement in liquidity (Increase in frequency, easing on refund restrictions)*"(22 respondents each) (Fig.28).

Many asset managers believe that in order to develop the private REITs market, they need to increase liquidity in addition to expanding their asset size and enhancing their track record.

Fig.27 Managers' involvement with private REITs n=55（Respondents 54）

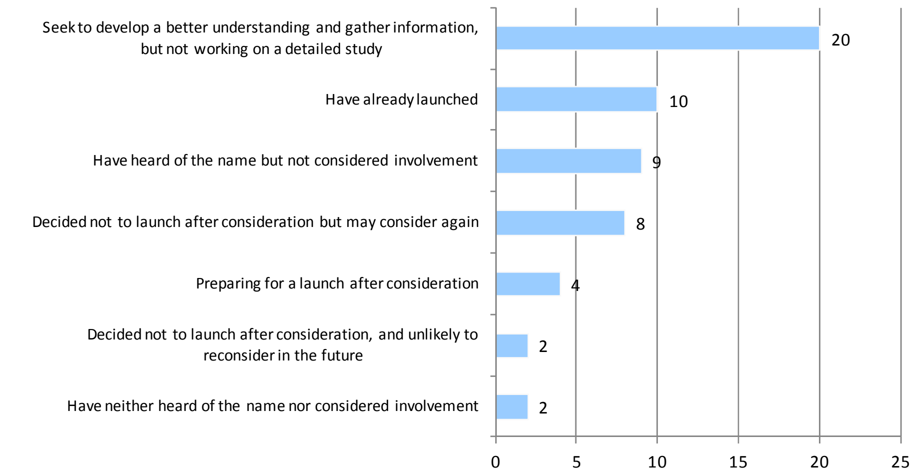
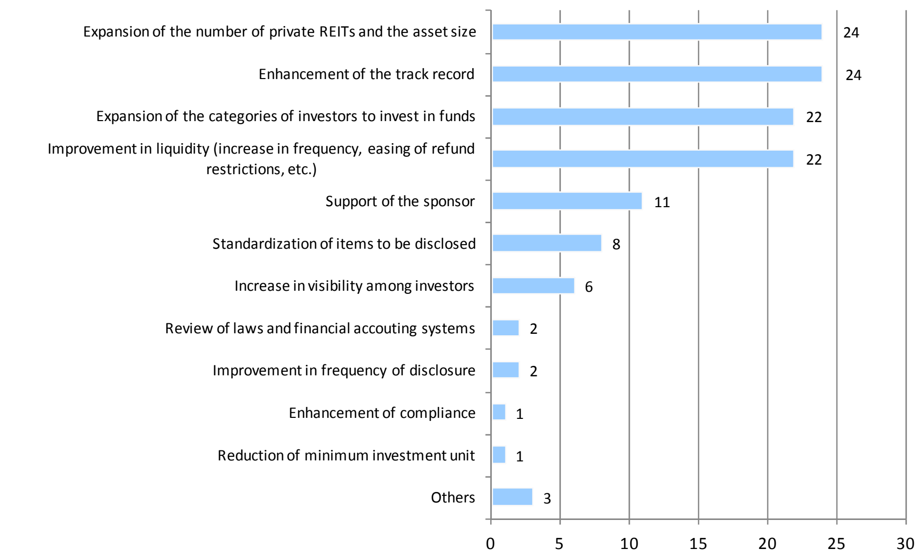


Fig.28 Important Factors for Development in the private REITs Market n=126（Respondents48）

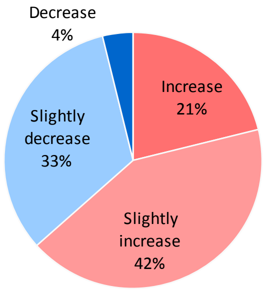


2) Closed-ended fund in the future

In regards to the future trends of assets under management of closed-ended funds, the total share of *"Increase"* and *"Slightly increase"* accounted for 63% , exceeded that of *"Decrease"* and *"Slightly decrease"*(Fig.29)

As for the reasons responding "Increase" or "Slightly increase", the majority of managers chose *"Increase of foreign investors' money"* (23 respondents) and *"Increase of domestic investors' money"* (20 respondents) , it showed that many managers expected growth in the closed-ended fund market due to increasing of both foreign and domestic investors' money.(Fig.30) Meanwhile, as for reasons responding "Decrease" or "Slightly decrease", the largest numbers of respondents chose "*Limited supply of existing investment-grade real estate*" (8 respondents). (Fig.31), a certain number of asset managers believe that the short supply will lead to a reduction in market size. "*Rise in real estate prices*" was chosen as a reason for both an increase and a decrease, which shows that asset managers have different views on how a rise in real estate prices affects the market.

Fig.29 Assets under management of closed-ended funds



(Respondents52)

Fig.30 Reasons for Increase of assets under management (Multiple answers allowed)

n=79 (Respondents33)

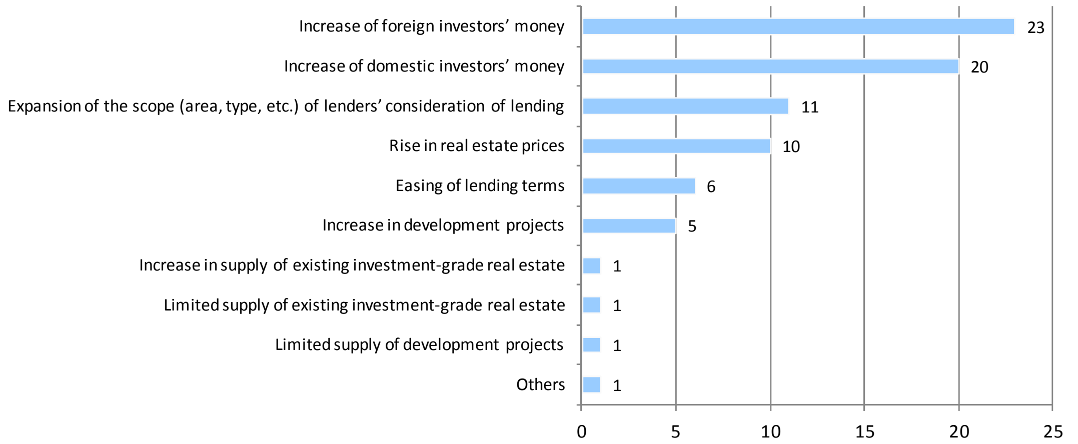
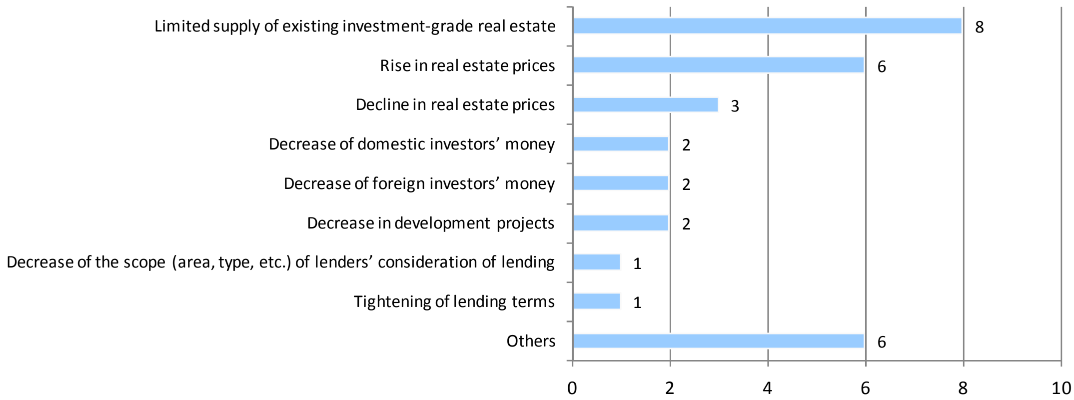


Fig.31 Reasons for Decrease of assets under management (Multiple answers allowed)

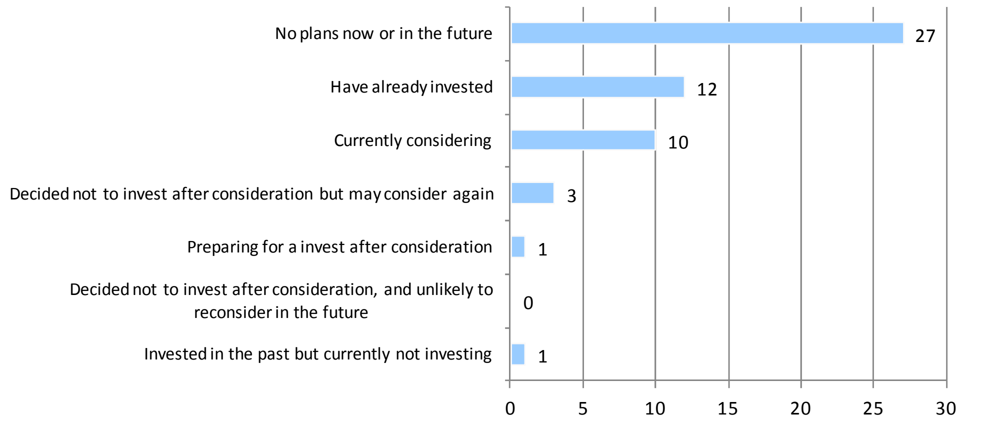
n=31 (Respondents19)



3) Fund Managers' Involvement in the Overseas Real Estate Management Business

With respect to fund managers' involvement in the overseas real estate management business, 27 respondents, the largest number of the managers chose "*No plans now or in the future*". Meanwhile, 12 respondents answered that they "*Have already invested*", 10 respondents chose "*Currently considering*", the total share of managers who have already launched or has been considering the overseas real estate management business accounted for 40%.

Fig.32 Managers' Involvement with the Overseas Real Estate Management Business (Respondents54)

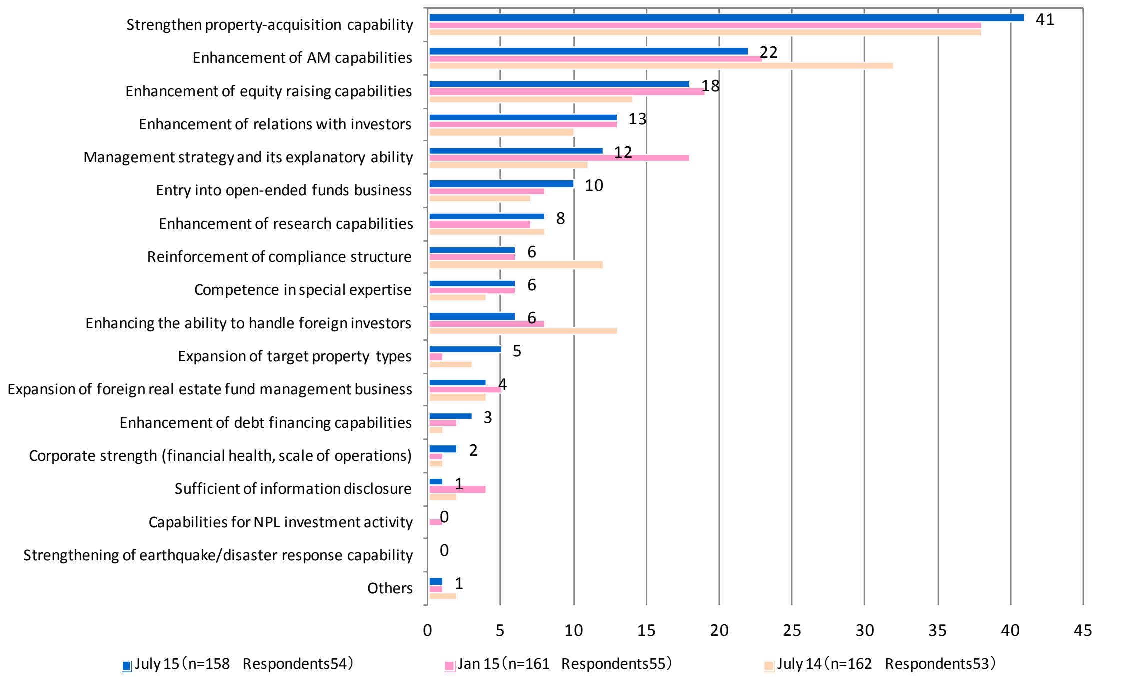


4) Manager's Requirements for Future Growth and Sustainability of their Businesses (Multiple answers allowed)

Among requirements for sustainability and growth of the asset managers, the majority of managers chose "*Strengthen property-acquisition capability*", "*Enhancement of AM capabilities*" in the last three times survey. In this survey, the number of respondents who chose "*Strengthen property-acquisition capability*" (41respondents) far exceeded the number of respondents who chose "*Enhancement of AM capabilities*" (22 respondents) (Fig.33)

Given the continued challenging market condition for acquisitions of properties, we consider that the numbers of managers who attach high priority to strengthen property-acquisition capability have been increasing.

Fig. 33 Requirements for Sustainability and Growth of Managers (choosing up to three options)



Definitions of Terms

The definitions of terms used in this report are as follows;

Private real estate fund: A private real estate fund is a structure under which investors' funds are managed by professional asset managers. In this report, commingled funds that are designed for multiple investors, and separate accounts, investment programs for single investors are both categorized as private real estate funds. This does not include products governed by the Act Concerning Designated Real Estate Joint Enterprises.

Fixed property type: A type of fund in which properties to be invested have been identified at the launch of the fund

Additional acquisition type: A type of fund in which certain percentage of properties to be invested have been identified at the launch of the fund, leaving additional investments after the launch usually at the discretion of manager subject to pre-determined investment guidelines

Discretionary investment type: A type of fund in which the properties to be invested have not been identified at the launch of the fund, and properties are acquired after the launch at the discretion of a manager subject to pre-determined investment guidelines; Also called a blind pool type

Closed-ended fund: This refers to private real estate funds with stipulations on the management period. In principle, this system does not allow reimbursement during the management period.

Open-ended fund: This refers to private real estate funds without stipulations on the management period. The system enables additional investment, cancellation and reimbursement during the management period. The value of the holding is calculated based on the appraisal value at the time. Open-ended funds currently managed in Japan take the form of a private REIT.

＜Management Style＞

Core: An investment style in which stable long-term investments are envisaged by investing in sound properties generating steady income flows.

Opportunity : An investment style in which a large capital gain is aimed at by investing in unprofitable properties and selling them after increasing value with improvements.
Some of opportunity investments invest in development projects and funds that invest in companies.

Value-added: An investment style that lies between Core and Opportunity, and aiming at both income gains and capital gains.

Development: An investment style that specializes in achieving development gains.

Debt: An investment style in which an investment is made in loans that pay the principal and interests from income from real estate and real estate trust beneficiary rights. Compared with the equity investment, the debt investment generally has a lower risk and a lower return.

＜Investment Area＞

Central 5 wards of Tokyo Chiyoda Ward, Chuo Ward, Minato Ward, Shinjuku Ward, Shibuya Ward

Tokyo Metropolitan Area: Tokyo excluding 23 Wards, Kanagawa, Saitama, and Chiba prefectures

Kinki Area: Osaka, Kyoto, Hyogo, Nara, Wakayama, and Shiga prefectures

Nagoya Area: Aichi, Gifu, and Mie prefectures

LTV (Loan To Value): The Loan to Value (LTV) ratio is a ratio of debt against asset value. Asset value represents the appraisal value, actual acquisition price or total investment cost for acquisition.

Cash-on-cash yield: The cash-on-cash yield is the yield of an annual cash flow on the total investment amount.

IRR (Gross): The Internal Rate of Return (IRR), an indication of return on investment, is the discount rate that makes the present value of future cash flow of an investment equal to its original value of the investment.

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