

Main Q&As Regarding the Financial Results of NTT UD REIT Investment Corporation for the 42nd Fiscal Period

Date and time: December 18, 2023 (Monday) at 11:30 a.m. (Teleconference)

Speaker: Yutaka Torigoe, President and CEO, NTT Urban Development Asset Management Corporation

- Q. The recent public offering was a discount offering. In the Earnings Presentation Video for the 42nd Fiscal Period, you stated that you intend to procure funds by actively considering the sale of properties, among other measures going forward. Given this, I would like to ask about your approach to fundraising: will the focus be on property replacement for the time being, or will properties primarily be acquired through debt financing?
- A. Regarding our approach to financing for future acquisitions, first of all, concerning acquisitions, in addition to the negotiation underway for the residential property Garden Itabashi Hikawacho, we are also discussing new acquisitions with the sponsor. We hope to complete this acquisition by the end of the fiscal year—most likely via debt financing—but the size of the acquisition has yet to be determined. As I explained earlier, we are considering the sale of properties that are exposed to leasing or obsolescence risk. We are currently in the process of investigating a variety of options. We believe that this will, to a certain extent, enable us to raise funds. Other than the projects within the fiscal year I just mentioned, however, we do not have any specific acquisition plan at this point in time. Going forward, we intend to conduct financing by balancing acquisitions and sales.
- Q. Please tell us about upcoming property acquisitions. The recent offering was to fund the acquisition of office buildings. Please share your thoughts on acquisitions in terms of property type—will you continue to focus on offices, or will you attempt to strike a balance for the foreseeable future, since the property under negotiation on the right of first negotiation is residential?
- A. As for future acquisitions, we will first complete the acquisition of the aforementioned residential property Garden Itabashi Hikawacho, but of course we will also acquire office properties. Although as the sponsor NTT Urban Development (NTT UD) is our most significant seller, as NTT Facilities was a seller of our recent property acquisition, our sources for consultations are expanding to include NTT Group companies in general. Going forward, we expect that the scope of such consultations will broaden to include not only offices but residential properties as well. In that sense, we would like to conduct acquisitions while maintaining a favorable balance to a certain extent.
- Q. Turning to the residential market, rents in the existing portfolio rose by an average of 6.4% this fiscal period. Is this momentum likely to continue for the foreseeable future, or is it approaching its peak?
- A. Concerning the direction of upward rent revision for residential properties, net change rate at tenant turnover is 6.4%. We are seeing things moving in a somewhat positive direction upon contract renewal. These conditions appear to be stable, and we anticipate they will continue for the foreseeable future.

Q. As you noted earlier, your approach to financing is to consider acquiring properties using leverage. Would there be room, however, to reconsider this stance in the event the financial environment were to change significantly? The expectation is for central bank activity to be significant going forward. In the context of the property situation and negotiations you spoke of earlier, how much weight do you put on the financial environment? I would then like to ask approximately what LTV (loan-to-value) ratio you would consider worth bearing the risk.

A. The movements of the Bank of Japan's (such as interest rate hikes) draw considerable attention. If we speak in terms of the next three months only, however, it will depend on the extent of the change. Basically, if it were for two to three months, we would not look to a public offering or sale and instead would acquire properties on leverage during the fiscal year. As for what would happen next, we would naturally adjust the aforementioned balance between sale and acquisition in response to changes in the financial environment. With regard to LTV, as a general rule, we maintain a target LTV ratio of 50%. In addition to not exceeding 50%, we also would like to avoid consistently being at 49% or 50%.

Q. You explained the top-line for residential properties earlier. On the other hand, what about the balancing of costs, including restoration to original condition? I think you will achieve top-line growth, but as costs rise, is there the prospect of momentum slowing somewhat rather than profit expanding? Please tell us about the overall direction from the perspective of cost as well.

A. Maintenance and repair and construction costs are also rising, as you pointed out. In spite of this, at present we believe that we are essentially on track to secure profits. We do not assume that there will be a notable contraction.

Q. Regarding The Kanagawa Science Park R&D Building (KSP), large-scale repairs are scheduled for next fiscal period. Please share, to the extent possible—acknowledging that there are other owners and that you may not be able to mention them—whether this is based on the assumption that repairs are necessary to drive leasing, or that repairs will generate a substantial amount of rent upon leasing.

A. Maintenance and repair costs for KSP are expected to be considerable, but the repairs are primarily a necessary allowance for deterioration over time as opposed to value enhancement. We do not foresee the repairs resulting in a notable rent increase. As for KSP, we are not the property's sole owner. We will, however, be cooperating with the other owners to deal with the situation. We would like to discuss with our partners in detail future rents, the use of maintenance and repair expenses, and other matters.

Q. Looking at internal growth, the commercial portion of the Urbannet Shijo Karasuma Building displayed on page 4 of the Earnings Presentation has vacant rooms. As the recent opening of Takashimaya S.C. shows, Kyoto is also recognized as an area with potential in terms of both office and commerce. I would like to ask if we can also anticipate commercial business amidst the recent inbound market environment.

A. The commercial portion of Urbannet Shijo Karasuma Building has commercial facilities from the basement to the third floors. B1 floor is occupied primarily by restaurants, while apparel and merchandise retailers can be found on the first and second floors, and beauty, English conversation school, and other service tenants on the third floor. Currently, sales on the first floor are performing well, but use of the second and third floors is somewhat lackluster. The team is currently discussing how best to leverage the situation. We strongly feel that the environment is one in which tenants can increase sales if they exert their potential.

- Q. A description of tenant movements is displayed on page 14. For example, occupancy rates at Tokyo Opera City Building (TOC) and Urbannet Gotanda NN Building have been impacted by the move-ins and move-outs of NTT Group companies. Is this due to a series of reviews on office strategy by the NTT Group or has the impact of these changes begun to recede? I would like to know what the impact will be on NUD.
- A. The strategy of NTT Group companies basically incorporates the proactive implementation of remote work among other measures. We believe that the movements promoting these have settled down. Apart from these movements, the NTT Group is looking to use its own floorspace to the extent possible. The NTT Group's own floors comprise those owned by NTT UD or other group companies and those belonging to NUD. The recent large-scale move-in of NTT Data into TOC also reflects this movement, with TOC being prioritized as it is NTT Group's floorspace.
- Q. Although the prearranged plan going forward is to acquire properties via property replacement and leverage, when Akihabara UDX—which is held in the form of preferred securities—is re-measured at market value, the NAV multiple is estimated to currently have fallen to nearly 0.8x. If you intend to acquire properties at the current unit price level rather than buying back units, I would like to ask why this is in the best interest of unitholders.
- A. Concerning properties that may be sold by the sponsor, there is no requirement that a listed REIT (NUD) acquires the property because the private REIT (NTT Urban Development Private REIT, Inc. (NUPR)) did not. For our part, we will naturally consider the details of the offer to determine whether it is in our interest, and unless we find it to be advantageous, we will not acquire the property. The conclusion of acquisition should not be coming first. Instead, we will acquire properties when the conditions are sufficiently favorable for us. We do not intend to acquire properties that don't have that appeal. Accordingly, as I mentioned earlier, we will balance acquisition and sale. If the prevailing environment prevents us from acquiring a sufficiently attractive property, it is possible that sale will precede acquisition, and we may consider a unit buyback contingent upon the market environment at that time.

- Q. I believe that the private REIT (NUPR) had a right of first negotiation for the office properties in regional cities you acquired via PO. But is my understanding correct in that the listed REIT (NUD) acquired the property because the private REIT did not acquire it? Assuming that, in the process of lightening its balance sheet, the sponsor will not sell properties to a third party, does this mean that NUD has no choice but to acquire properties that the private REIT (NUPR) does not?
- A. With regard to the relationship between the private REIT for regional properties, as you noted, the private REIT has a right of first negotiation. In this case, the private REIT decided not to acquire the property in consideration of its portfolio, so then we (listed REIT) considered the acquisition. As I mentioned earlier, when the private REIT does not acquire a property, there is no mandate for us (the listed REIT) to acquire it. Given this, if we (the listed REIT) deem the acquisition not in the best interest of unitholders based on our own criteria, we naturally will not acquire the property. It is not at all true that the NTT Group will not sell properties to third parties. It is natural that properties not acquired by us (the listed REIT) or the private REIT for some reasons are sold to third parties. In fact, some properties are sold to third parties.

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