

# Third Quarter FY2019 Financial Earnings Summary



FIRST BROTHERS

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First Brothers Co., Ltd. (3454)

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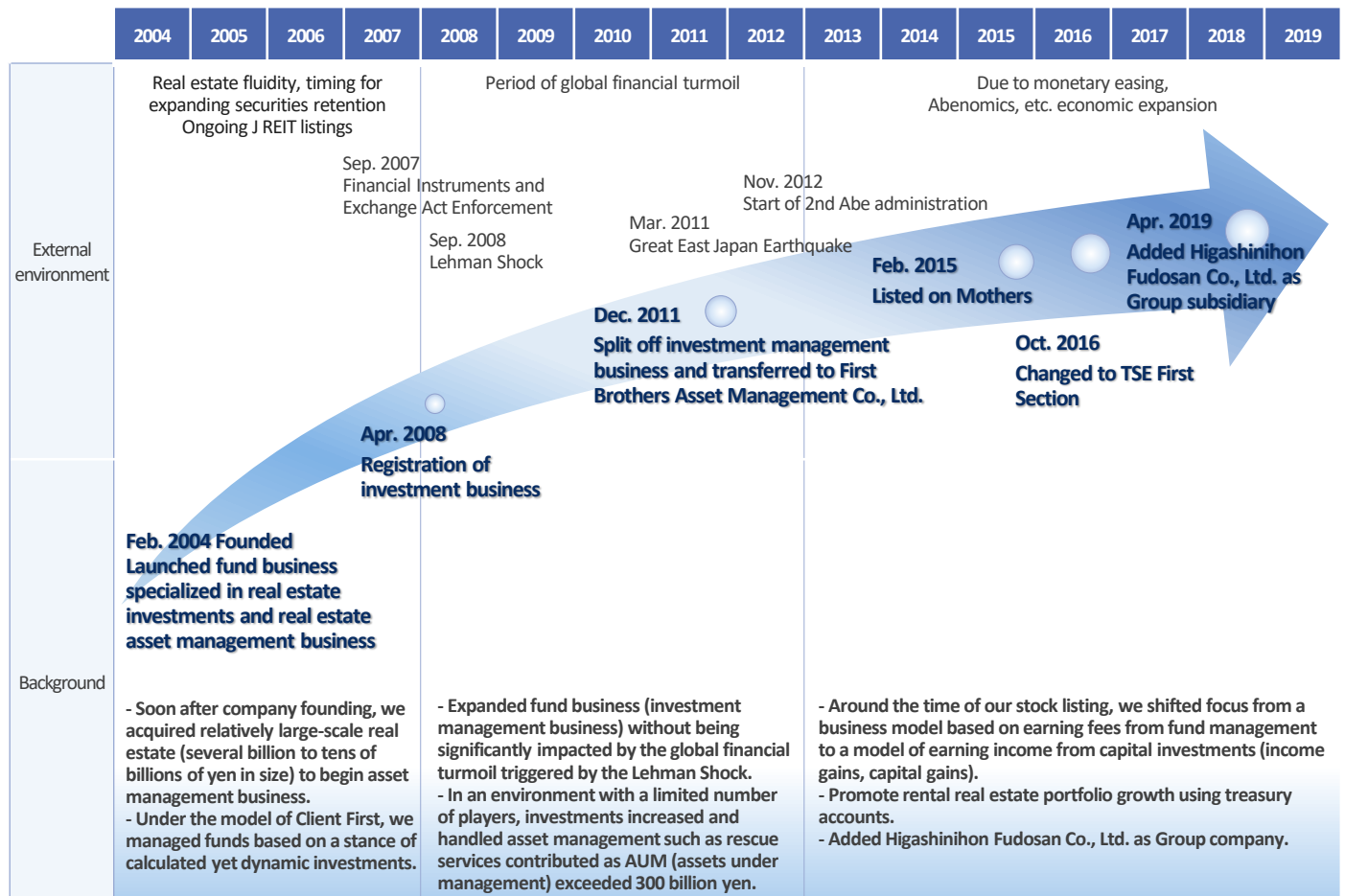
October 7, 2019

# About Us

## Company overview

Company name	First Brothers Co., Ltd.
Established	February 4, 2004
Address	Marunouchi Bldg., 25th Fl. 2-4-1 Marunouchi, Chiyoda-ku, Tokyo
Capital	1,589,830,800 yen
Stock code	3454 (Tokyo Stock Exchange First Section)
Number of employees	74 employees (as of August 31, 2019 / Group consolidated)
Major subsidiaries	First Brothers Capital Co., Ltd. First Brothers Asset Management Co., Ltd. First Brothers Development Co., Ltd. Higashinihon Fudosan Co., Ltd.

## Group background



## Group major businesses

Since our founding in February 2004 our Group has formed a fund that focuses on investments in real estate and we have developed into a business whose core operations involve asset management for institutional investors\*<sup>1</sup>. Around the time of our stock listing in February 2015 we made significant changes to our business structure. Today, as an investment firm conducting our own asset management\*<sup>2</sup>, we use real estate investment as a core business for securing stable income while investing in various peripheral domains.

### **(1) Real estate investments**

We retain a rental real estate portfolio that is projected to return stable income over the medium- to long-term. For individual real estate properties in our portfolio, we carefully select and invest in small- to mid- scale properties from among the vast number of properties available on existing markets and use various methods to increase property values. Additionally, we also engage in new development when we can anticipate sufficient returns. We refresh our rental real estate portfolios as necessary and generate unrealized gains by increasing property values.

If we find opportunities for investments in large scale real estate projects, we will also conduct joint investments with institutional investors.

### **(2) Private equity investments**

In addition to real estate, we also invest in various other projects, including defaulted debt, venture capital, and unlisted company stocks.

### **(3) Renewable energy**

Among the various forms of renewable energy, we are particularly involved in business development in the geothermal energy sector. Although commercialization will take several years, we have focused on this field as an investment in which we can apply our Group knowhow and make visible contributions to society.

### **(4) Fund business**

This is the business of creating a fund and conducting asset management for institutional investors. Funds target relatively large real estate investments (several billion to tens of billions of yen) and aim to secure both income gains and capital gains.

Under the model of Client First, the First Brothers Group places our highest priority on providing investment services that put client satisfaction above all else. By conducting investment transactions based on the timing that generates the greatest level of income, Group assets under management fluctuate significantly along with fluctuations on the real estate market.

Furthermore, we apply the knowledge we have built up in the fund business to at times handle asset management of active real estate investments that investors are running independently.

#### **\*1 Investment management business ((4) above)**

This business conducts client asset management through private funds that target mainly real estate and real estate trust beneficiary rights. This involves a series of business activities, including investment strategy planning, proposals and property acquisitions, property management during the investment period, and disposition (sale of investment property). The investment management business represents the origin of our growth.

#### **\*2 Investment banking business ((1), (2), (3) above)**

This business represents the investment activities conducted by our Group, and focuses on investments in rental real estate that is projected to return stable income. This business also includes private equity investments that utilize the platform and strengths of our existing businesses, investments in renewable energy and other social infrastructure, and joint investments (same boat investments) in private funds formed by our Group. These investment activities form the pillar of our Group's growth.

## Topics for 3Q/FY2019 (1)

### Rental real estate portfolio (capital investments)

Our Group policy is to enhance our portfolio by acquiring a rental real estate that is projected to return stable income over the medium- to long-term.

During the first nine months, we continued to acquire high-quality rental real estate. The April 2019 acquisition and addition of Higashinihon Fudosan Co., Ltd., which owns and operates numerous high-quality rental real estate properties in the Tohoku area, as a Group company contributed to the significant growth of our rental real estate portfolio. We also sold certain properties as part of the refreshing of our portfolio.

Our balance of rental real estate portfolio and the relative book value, market value, and unrealized gains are as follows.

(1 million yen)	FY2016 (as of end of year)	FY2017 (as of end of year)	FY2018 (as of end of year)	3Q/FY2019 (as of end of 3Q)
Balance* <sup>1</sup> (Properties)	25,109 (18 properties)	28,050 (28 properties)	33,012 (27 properties)	<b>47,451</b> <b>(53 properties)</b>
Increase* <sup>1</sup>	16,952	15,527	17,934	<b>19,629</b>
Decrease* <sup>1</sup>	7,553	12,586	12,971	<b>5,191</b>
Book value* <sup>2</sup>	25,776	28,789	34,014	<b>48,600</b>
Market value* <sup>3</sup>	32,661	34,099	38,502	<b>53,118</b>
Unrealized gain* <sup>3</sup>	6,885	5,309	4,487	<b>4,518</b>
NOI yield* <sup>4</sup>	5.8%	6.1%	6.4%	<b>6.9%</b>

\*1 Balance, increase, and decrease amounts are based on acquisition price (pre-tax).

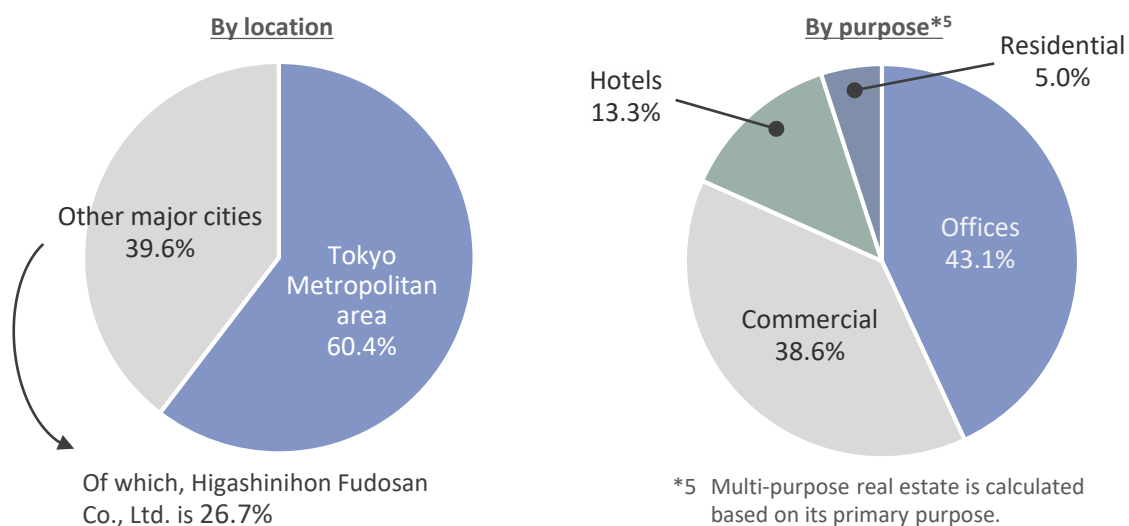
Furthermore, the acquisition price for Higashinihon Fudosan Co., Ltd. is based on the consolidated book value as of the start of consolidation.

\*2 Book value is adjusted by adding transaction costs at the time of acquisition to acquisition costs and reflecting capital expenditures and depreciation costs for the investment period.

\*3 Market value is the most recent appraised value or assessment value based on the appraised value and unrealized gains are the difference compared to the book value.

\*4 Assume APR for stable operation (cash-based net income from rents excluding administrative expenses, etc. / acquisition costs)

A breakdown of our rental real estate portfolio by location and purpose is shown in the following graph (based on acquisition cost; as of the end of 3Q/FY2019).



## Topics for 3Q/FY2019 (2)

### Rental real estate portfolio stable income and SGA cover rate

Our Group policy is to increase stable income earned from rental real estate in order to expand our rental real estate portfolio. During the first nine months, the April 2019 addition of high-quality rental real estate properties owned and operated by Higashinihon Fudosan Co., Ltd. to our portfolio contributed as we succeeded in increasing gross profit to a level that exceeded SGA.

	FY2016 (12-month total)	FY2017 (12-month total)	FY2018 (12-month total)	3Q/FY2019 (9-month total)
Gross profit from renting* <sup>1</sup> (1 million yen)	993	1,241	1,156	1,143* <sup>3</sup>
SGA cover rate* <sup>2</sup>	79%	98%	85%	105%

\*1 Net income gained from rental real estate (NOI (excludes special factors) depreciation expenses)

\*2 Gross profit from rent selling, general and administrative expenses (excludes special factors)

\*3 About the correlation between NOI yield during stable operation (see P3 and rental real estate gross profit 3Q/2019)

• 3Q NOI during stable operation	2,021 million yen
(40,231 million yen (retained property balance average of start of FY and end of 3Q) x 6.7% (NOI yield average of start of FY and end of 3Q) x 9 months/12 months)	
• Term depreciation expenses	-350 million yen
• Vacancy losses incidental to value improvement activities and rent from properties acquired during the fiscal year	-528 million yen
• Gross profit from rental real estate (3Q/2019)	1,143 million yen

### Sales incidental to rental real estate portfolio refreshing portfolio

For acquired real estate, we work to increase property value while conducting timely market transactions by refreshing our rental real estate portfolio to earn capital gains. During 3Q/FY2019, we sold multiple properties to capture unrealized gains from our portfolio.

Sales of rental real estate were as follows.

(1 million yen)	FY2016 (12-month total)	FY2017 (12-month total)	FY2018 (12-month total)	3Q/FY2019 (9-month total)
Sell value* <sup>1</sup>	10,615	16,450	19,646	7,091
Gross profit from sales* <sup>1</sup>	2,572	3,397	5,332	1,427

\*1 Includes sale of real estate for sale in process (including land for rental real estate development)

#### ■ About low volume of sales and gross profit from sales during first nine months

During the current fiscal year (FY2019), we are planning to sell multiple properties as part of the refreshing of our rental real estate portfolio. While we sold multiple properties and concluded multiple purchasing agreements during the first nine months, the timing of property sales planned for the current fiscal year, including properties for which we have already concluded purchasing agreements, is projected 4Q.

As such, volume of sales and gross profit from sales were low during the first nine months. However, sales activities are progressing smoothly towards the achievement of our full-year earnings forecast.

## Topics for 3Q/FY2019 (3)

### Status of rental real estate portfolio / capital procurement

Since we execute loans when acquiring rental real estate, our loan balances tend to increase relative to our investment activities. In principle, we execute super long-term loans (10 years or longer) and use interest swaps\* to secure fixed rates for a certain percentage of interest.

\* Interest swap agreement market price fluctuates with interest market trends. During 3Q, interest market rates trended downward. As such, we incurred interest swap agreement valuation losses (195 million yen). However, these interest payments are stretched out over a long period of time to avoid the risk of rising interest rates, which contributes to cash flow stabilization.

	End of FY2016	End of FY2017	End of FY2018	End of 3Q/FY2019
Loan balances* <sup>1</sup> (1 million yen)	22,365	24,377	27,930	41,024
(portion of non-recourse loans)	0	748	629	618
Leverage* <sup>2</sup>	86.8%	84.7%	82.1%	84.4%
Weighted average residual period	20.7 years	22.4 years	16.2 years	15.0 years
Weighted average interest* <sup>3</sup>	0.76%	0.92%	0.79%	0.80%
Set fixed interest ratio	61.9%	56.1%	61.6%	50.7%

\*1 Indicates loans for the acquisition of rental real estate. Includes non-recourse loans and excludes other loans for the acquisition of development projects (3,774 million yen).

\*2 Loan balance rental real estate book value

\*3 Prior to fixed interest rates

### Fund business (investment management business)

During 3Q/FY2019, the relatively large-scale properties primarily targeted by the fund for investment are subject to intense acquisition competition compared to the small- to medium-sized properties we target for capital investments. As such, we have refrained from new acquisitions in funds in which the Group is managing investments independently.

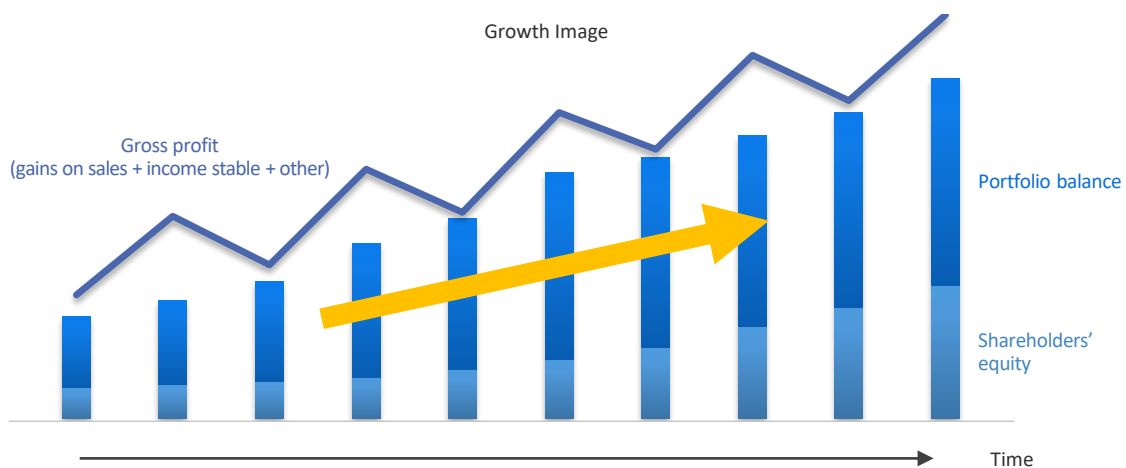
The increase during the first nine months is attributable to contracted asset management services for investor led real estate investment activities accepted by the Group during the fiscal year.

Note that the Group continues uncovering new projects for us to invest in independently in funds.

(1 million yen)	End of FY2016	End of FY2017	End of FY2018	End of 3Q/FY2019
AUM	32,183	0	8,733	13,583
Increase	0	0	8,733	4,850
Decrease	24,832	32,183	0	0

## Growth strategy and FY 2019 Full year Earnings Forecast

Our Group is positioning the expansion of our rental real estate portfolio as a core growth strategy. We will continue to acquire and manage real estate with potential for value improvements. We also will engage in development and realize sustainable growth with the region by promoting coexistence with the local society. We refresh our rental real estate portfolio during the portfolio growth process to generate unrealized gains and reinvest profits towards further portfolio growth. Our Group policy is to enhance our rental real estate portfolio while also increasing profits and shareholders' equity. At present, as our ratio of profit from the sale of real estate is relatively high, fiscal year profits or losses may fluctuate depending on the results of property sales.



### FY2019 Full year earnings forecast

During the current fiscal year, we will throttle back on sales incidental to refreshing portfolio compared to the previous fiscal year. Due to this and other factors, we forecast lower revenues and profit due to a year on year decline in revenues and income from sales.

However, our consolidated earnings forecast for the current fiscal year will progress amid the implementation of our growth strategy so we will continue to respond flexibly to market changes while working to achieve sustainable growth.

Our Group manages earnings on a full-year basis and thus our earnings forecasts are for the full-year only.

(1 million yen)	FY2017 Full-year results	FY2018 Full-year results	FY2019 Full-year forecast	YoY
Net sales	18,766	21,864	20,020	-8.4%
<b>Gross profit</b>	<b>4,720</b>	<b>6,488</b>	<b>5,380</b>	<b>-17.1%</b>
Investment management business	10	43	32	-26.4%
Investment banking business	4,710	6,444	5,347	-17.0%
Operating income	3,373	5,130	3,850	-25.0%
Ordinary income	3,060	4,700	3,170	-32.6%
Profit attributable to owners of parent	2,048	2,885	2,000	-30.7%

## 3Q/FY2019 Earnings Summary

### Matters concerning consolidated statements of income (summary)

During the first nine months, we expanded our portfolio on the April 2019 by addition of Higashinohon Fudosan Co., Ltd. but earnings during this period progressed at a rate that is below our full-year forecast. This is because Group quarterly earnings fluctuate significantly depending on the timing of investment property sales and other factors.

The projected timing of sales for a significant number of properties, including those for which purchasing agreements have already been concluded, this fiscal year is 4Q. As such, sales activities are progressing largely according to our full-year plan and thus there is no change in our full-year earnings forecast.

(1 million yen)	3Q/FY2017	3Q/FY2018	3Q/FY2019	YoY	3Q/FY2019 rate of progress
Net sales	10,653	16,333	9,329	-42.9%	46.6%
Gross profit	2,797	4,098	2,511	-38.7%	46.7%
Selling, general and administrative expenses	950	973	1,250	+28.4%	-
Operating income	1,847	3,124	1,260	-59.7%	32.7%
Ordinary income	1,593	2,859	612	-78.6%	19.3%
Profit attributable to owners of parent	1,078	1,798	385	-78.6%	19.3%

### Gross profit breakdown

(1 million yen)	3Q/FY2017	3Q/FY2018	3Q/FY2019	YoY
Investment management business	10	35	81	+127%
Investment banking business	2,787	4,062	2,430	-40.2%
Gross profit from real estate sales	1,830	3,220	1,427	-55.7%
Gross profit from rental real estate	875	798	1,011	+26.7%
Other	82	43	-9* <sup>1</sup>	N/A
Gross profit total	2,797	4,098	2,511	-38.7%

\*1 Includes anonymous association distribution losses (13 million yen) from the private equity investment business.

### Selling, general and administrative expenses breakdown

(1 million yen)	3Q/FY2017	3Q/FY2018	3Q/FY2019	YoY
Personnel expenses	580	618	690	+72
Land and rent	108	110	131	+20
Commission fee/compensation	122	138	282* <sup>2</sup>	+144
Duties and public taxes	64	76	56	-20
Other	73	29* <sup>1</sup>	88	+59
Selling, general and administrative expense total	950	973	1,250	+276

\*1 The reversal of allowance for doubtful account (41 million yen) due to an overdue account receivable was deducted from this item.

\*2 Includes expenses related to the acquisition of Higashinohon Fudosan Co., Ltd. Stock (158 million yen)



### Consolidated balance sheet (summary)

Although rental real estate is mainly retained to secure stable profits, on the balance sheet we record these properties as real estate for sale to enable us to conduct dynamic sales of real estate when we seek to refresh our portfolio.

During 3Q/FY2019, the acquisition of Higashinohon Fudosan Co., Ltd. contributed to increasing our portfolio, and as a result real estate for sale and long-term loans payable increased.

Consolidated / Assets (1 million yen)	FY2017 Year-end	FY2018 Year-end	FY2019 As of end of 3Q	Change
Total current assets	38,309	47,180	63,172	+15,991
Cash and deposits	6,161	7,672	7,319	-352
Trust deposits	536	505	436	-68
Real estate for sale	28,789	34,014	48,625	+14,610
Real estate for sale in process	1,215	3,265	4,685	+1,420
Other	1,606	1,722	2,104	+381
Total non-current assets	843	862	1,855	+992
Total assets	39,153	48,043	65,027	+16,983

Consolidated / Liabilities and net assets (1 million yen)	FY2017 Year-end	FY2018 Year-end	FY2019 As of end of 3Q	Change
Total liabilities	27,542	33,760	50,631	+16,871
Total current liabilities	2,660	3,363	4,429	+1,065
Short-term loans payable	860	600	1,763	+1,163
Current portion of long-term loans payable	698	779	1,477	+697
Current portion of long-term non- recourse loans payable	7	15	15	0
Other	1,094	1,968	1,173	-794
Total non-current liabilities	24,882	30,396	46,202	+15,805
Long-term loans payable	22,931	28,521	41,484	+12,962
Long-term non-recourse loans payable	740	613	602	-11
Other	1,210	1,261	4,116 <sup>*2</sup>	+2,854
Total net assets	11,610	14,283	14,395	+112
Total shareholders' equity	11,576	14,251	14,384	+133
Other	33	31	10	-21
Total liabilities and net assets	39,153	48,043	65,027	+16,983
Net D/E ratio <sup>*1</sup>	1.54	1.52	2.57	-

\*1 Net D/E ratio =(interest bearing loans excluding non-recourse loans - (cash and deposits + trust deposits)) / shareholders' equity

\*2 Deferred tax liabilities and deposits incidental to the Group acquisition of Higashinohon Fudosan Co., Ltd.

## Shareholder Returns

### Dividend basic policy

Dividends are issued once per year (term end)

- Issued continuously and stably regardless of short-term fluctuation in earnings
- To be increased over the medium- to long-term in line with company growth
- Goal dividend ratio on equity (DOE) of 2.0%

[Formula for calculating per share dividend amount]

Consolidated shareholders' equity (average for term beginning and term end) x 2.0% / average number of shares for fiscal year

It is typical for dividend payout ratio to be used as the standard for calculating dividends. However, instead of a dividend payout ratio that would fluctuate with each year's profits, our policy is to use consolidated shareholders' equity, a recording category on our balance sheets, to issue continuous, stable dividends regardless of fluctuations in short-term performance.

If net income results in a profit (higher than dividend amount), then consolidated shareholders' equity will increase each term, which enables us to increase dividends over the medium- to long-term in line with company growth.

We also view share buy-backs as a dynamic method for producing shareholder returns.

Reference period	FY2017	FY2018	FY2019 (Forecast)
Dividends per share	15.0 yen	18.0 yen	21.0 yen
Total dividend payout (1,000 yen)	210,176	252,211	—
Total share buy-back value (1,000 yen)	—	—	—

### About shareholder benefit plan

#### (1) Applicable shareholders

Shall apply to shareholders registered in the shareholder ledger retaining at least one unit of company stock (100 shares) as of November 30 of each year.

#### (2) Details of shareholder benefits

Applicable shareholders	Benefit details
Retained shares of 100 shares or more (persons not applicable indicated below)	Original 1,000 yen QUO Card
Shareholders retaining stock for one year or longer (Note 1) as well as retained shares of 100 or more shares, less than 200 shares	Original 2,000 yen QUO Card
Shareholders retaining stock for one year or longer (Note 1) as well as retained shares of 200 shares or more	Original 4,000 yen QUO Card

(Note 1) Shall apply to shareholders registered in the company shareholder register for three consecutive times under the same shareholder number each year as of the end of May and the end of November.

#### (3) Distribution timing

We send the certificates together with the Regular General Meeting of Shareholders Convening Notice issued every year in early February. Acceptance of requests for reissuance to shareholders unable to receive the certificates shall be up to the end of August for the year in question.

## Reference Materials

### Group strengths

Our Group boasts a team of numerous elite professionals with advanced expertise, from people who have been active at the forefront of the industry since the early days of asset backed securities in Japan to accountants, real estate appraisers, and attorneys. The depth of our elite personnel and their respective experiences as key individuals in our industry is the core strength of our Group.

### Our management

**First Brothers Co., Ltd.  
President**

**Tomoki  
Yoshihara**

- Founder of First Brothers Group Has been involved in numerous large-scale transactions and continues to be active on the front lines of the industry.
- After spending time at a trust bank where he was involved in scheme development from the early days of asset backed securities, he experienced further success at a foreign investment bank in real estate investments before going on his own in 2004.
- Has vast experience, success and connections in the investment industry.

**First Brothers Co., Ltd. Executive  
Director**

**Kazutaka  
Tsuji**

- Joined our Group after time at a trust bank, a foreign investment bank and an asset management company
- Expert in compliance and risk management
- Real estate appraiser

**First Brothers Co., Ltd. Executive  
Director**

**Yoshinobu  
Hotta**

- Joined our Group after time at a trust bank, auditing firm, and a consulting company
- Expert in investment structures
- Certified Public Accountant, real estate appraiser

**First Brothers Co., Ltd.  
Executive Director**

**Kohtaro  
Tamura**

- Partner attorney at Ushijima & Partners, Attorneys at Law
- MLIT Real Estate Investment Market Policy Workgroup Chairman
- Pioneer of legal affairs related to real estate securitization

**First Brothers Co., Ltd. Executive  
Director (External)**

**Tatsuo  
Watanabe**

- Formerly with the Ministry of Finance, Director of FSA Securities and Exchanges Audit Committee Office, Deposit Insurance Organization board member, Vice Chairman of Japan Securities Association, Chairman of Financial Information System Center. Has long history in the field of financial administration

**First Brothers Co., Ltd. Corporate  
Strategic Business Development  
Department, Director**

**Akihito  
Sato**

- Joined our Group after time at real estate appraisal office and an asset management company
- Vast experience and knowledge related to real estate investment and portfolio management
- Real estate appraiser

**First Brothers Co., Ltd.  
Corporate Advisor**

**Tadashi  
Iwashita**

- Formerly with the Ministry of Finance. Previous posts at the ministry include Deputy Vice Minister of Finance. Also served during this time as a Japanese envoy in the USA and Secretary to the Prime Minister
- Former director of the board at the Japan Bank for International Cooperation, former chairman of Lone Star Japan, former advisor at the Daiwa Securities Group's head office
- Representative Director and Chairman of Lawson Bank Inc.

**First Brothers Capital Co., Ltd.  
President**

**Taichi  
Kano**

- Assumed current position after time as a trust bank executive and as a director of J-REIT Assets Management
- Has vast experience and connections in the financial industry
- Oversees capital investments for our Group

**First Brothers Asset Management Co., Ltd. Senior Executive  
Managing Director**

**Daisuke  
Taniguchi**

- Assumed current position after time as a trust bank executive and as a director of J REIT Assets Management
- Has vast experience and connections in the financial industry
- Oversees capital investments for our Group

**First Brothers Capital Co., Ltd.  
Executive Officer**

**Tomo  
Aoki**

- Joined our Group after time at a real estate company and an asset management company
- Vast experience as a private fund asset manager
- Vast experience in sourcing and disposition within our Group

**First Brothers Capital Co., Ltd.  
Executive Officer**

**Taichi  
Ishikawa**

- Joined our Group after time at a general real estate corporation, a foreign investment fund and an investment bank
- Expert in finance administration and real estate fund business
- Diverse experience in property acquisition and asset management

**First Brothers Capital Co., Ltd.  
Executive Officer**

**Kazunori  
Sawada**

- Joined our Group after time at the head of asset management administration at a domestic bank
- Diverse experience in traditional and alternative investments
- Has vast connections with numerous domestic and international financial institutions and investors

**First Brothers Capital Co., Ltd.  
Executive Officer**

**Yoshinori  
Tajima**

- Joined our Group after time at a hotel management company, a foreign investment bank and an asset management company
- Vast knowledge and experience in underwriting and the hospitality business

**First Brothers Development Co., Ltd.  
President**

**Yasushi  
Kotani**

- Joined our Group after time at a major general contractor and an asset management company
- Vast experience and knowledge related to real estate development and infrastructure projects
- First class architect

**First Brothers Asset Management Co., Ltd. Investment  
Management Business Director**

**Masaki  
Minemura**

- Joined our Group after time at a major general contractor and a foreign investment fund
- Experience in a wide range of asset management, including real estate investments, stocks, and infrastructure businesses

Thank you for your attention.

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Inquiries

First Brothers Co., Ltd. Business Planning Dept.  
+81-3-5219-5370  
IR@firstbrothers.com