

Third Quarter FY2018 Financial Earnings Summary



FIRST BROTHERS

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First Brothers Co., Ltd. (3454)

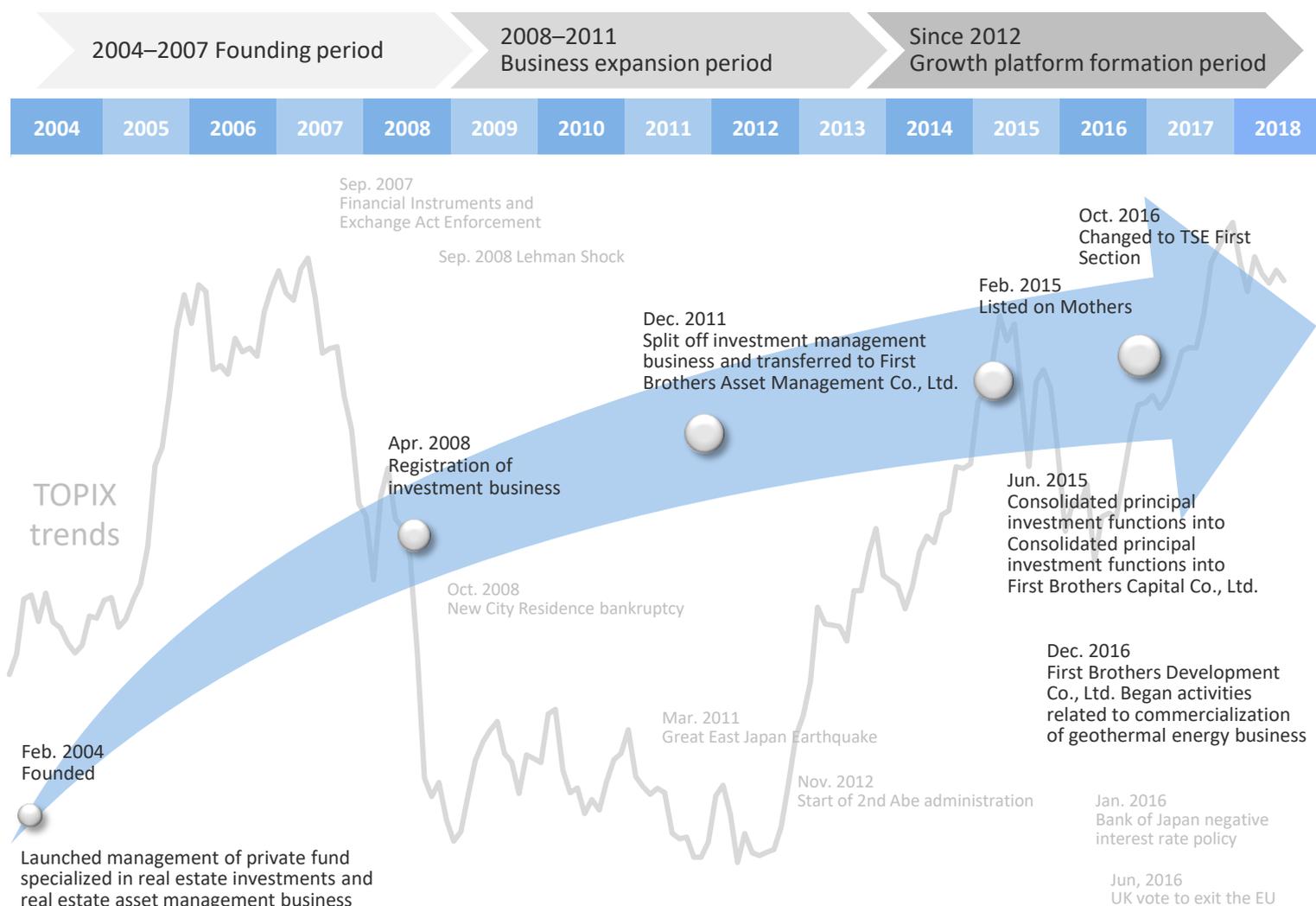
October 9, 2018

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	56 employees (as of August 31, 2018 / Group consolidated)
Major subsidiaries	First Brothers Capital Co., Ltd. First Brothers Asset Management Co., Ltd. First Brothers Development Co., Ltd. Alley 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*¹. 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*², 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. Generally speaking, the scale of an asset management firm is evaluated based on the firm's total assets under management. The compensation for asset management in the forms of regularly received asset management fees is typically based on assets under management. As such, asset management firms tend to have incentives towards increasing their assets under management. However, 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 fluctuates 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/FY2018

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 3Q/FY2018, we worked to increase our portfolio of quality rental real estate. Since entering the 4Q/FY2018, we already have acquired multiple properties and we will continue to enhance our portfolio by seeking quality properties.

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

(1 million yen)	2H/FY2016 (as of end of 2H)	1H/FY2017 (as of end of 1H)	2H/2017 (as of end of 1H)	1H/FY2018 (as of end of 1H)	3Q/FY2018 (as of end of 3Q)
Balance* ¹ (Properties)	25,109 (18 properties)	26,374 (25 properties)	28,050 (28 properties)	25,363 (21 properties)	27,438 (24 properties)
Increase* ¹	5,078	8,214	7,312	6,858	3,476
Decrease* ¹	2,340	6,950	5,636	9,546	1,400
Book value* ²	25,775	27,050	28,789	26,194	28,361
Market value* ³	32,661	32,806	34,099	30,017	31,814
Unrealized gain* ³	6,885	5,756	5,309	3,822	3,452
NOI yield* ⁴	5.8%	6.5%	6.1%	6.5%	6.4%

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

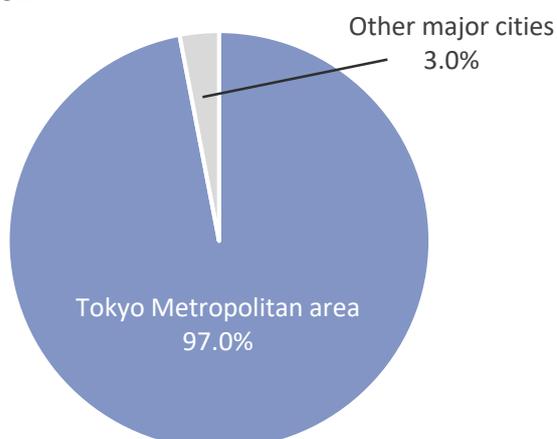
*2 Book value is adjusted by adding transaction costs at the time of acquisition to acquisition costs and reflecting capital expenditures and depreciation costs for the investment period

*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

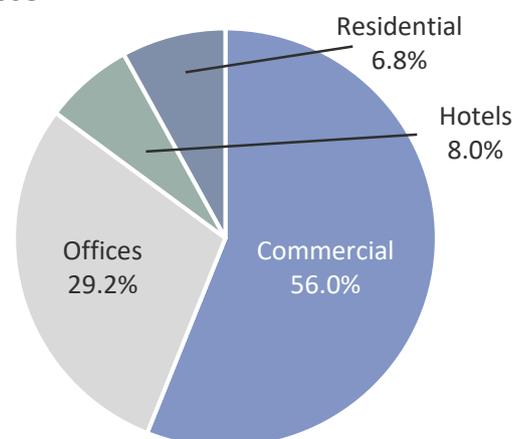
*4 Assume APR for stable operation (cash-based net income from rents excluding administrative expenses, etc. / acquisition costs)

A breakdown of our rental real estate portfolio by location and purpose (a breakdown of balances based on acquisition costs) is shown in the following graph. (as of the end of 3Q/FY2018)

By location



By purpose*⁵



*5 Multi-purpose real estate is calculated based on its primary purpose.

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/FY2018, we sold multiple properties to capture unrealized gains from our portfolio.

Sales of rental real estate were as follows.

(1 million yen)	2H/FY2016 (6-month total)	1H/FY2017 (6-month total)	2H/FY2017 (6-month total)	1H/FY2018 (6-month total)	3Q/FY2018 (3-month total)
Sell value	3,495	8,950	7,500	12,956	1,670
Gross profit from sales	876	1,829	1,568	3,094	125

Rental real estate portfolio / stable income and SGA cover rate

As we enhance our rental real estate portfolio, we also plan to earn more gross profit from rent (stable income) at those properties, but due to such factors as property sales accompanying a portfolio refresh and vacancy losses accompanying value improvement activities, gross profit from renting and the SGA cover rate may drop temporarily. In 3Q/FY2018, a decline in gross profit from renting and the SGA cover rate would be caused by the aforementioned.

	2H/FY2016 (6-month total)	1H/FY2017 (6-month total)	2H/FY2017 (6-month total)	1H/FY2018 (6-month total)	3Q/FY2018 (3-month total)
Gross profit from renting* ¹ (1 million yen)	553	606	634	613	270* ³
SGA cover rate* ²	89%	95%	101%	91%	85%

*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 separation (see P3) and rental real estate gross profit (3Q/FY2018)

• 3Q NOI during stable operation (26,400 million yen (average retained property balance at beginning/end of 3Q/FY2018) x 6.4% (average NOI yield beginning/end of 3Q/FY2018) x 3 months/12 months)	422 million yen
• Term depreciation expenses	- 69 million yen
• Vacancy losses incidental to value improvement activities and rent from properties acquired during the fiscal year	- 83 million yen

• Gross profit from rental real estate (3Q/FY2018)	270 million yen

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. During 1H/FY2018, we focused on sales due to a refreshing of our portfolio, which caused our loan balance to decline but this has increased with the expansion of our rental real estate portfolio since the third quarter onward.

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.

	2H/FY2016 (as of end of 2H)	1H/FY2017 (as of end of 1H)	2H/FY2017 (as of end of 2H)	1H/FY2018 (as of end of 1H)	3Q/FY2018 (as of end of 3Q)
Loan balances* ¹ (1 million yen)	22,365	23,439	24,377	22,683	23,984
(portion of non-recourse loans)	0	0	748	636	633
Leverage* ²	86.8%	86.6%	84.7%	86.6%	84.6%
Weighted average residual period	20.7 years	22.7 years	22.4 years	20.8 years	18.1 years
Weighted average interest* ³	0.76%	0.90%	0.92%	0.78%	0.72%
Set fixed interest ratio	61.9%	63.8%	56.1%	65.3%	61.5%

*1 Including non-recourse loans (excludes loans for acquisition of real estate for sale in process)

*2 Loan balance / rental real estate book value

*3 Prior to fixed interest rates

Fund business (investment management business)

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 fluctuates significantly along with fluctuations on the real estate market.

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 increased value of investments under management in 1H/FY2018 was due to the Group handling asset management of active real estate investments that investors are running independently. Note that the Group continues uncovering new projects for us to invest in independently in funds.

(1 million yen)	2H/FY2016 (as of end of 2H)	1H/FY2017 (as of end of 1H)	2H/FY2017 (as of end of 2H)	1H/FY2018 (as of end of 1H)	3Q/FY2018 (as of end 3Q)
AUM	32,183	0	0	8,733	8,733
Increase* ¹	0	0	0	8,733	0
Decrease* ¹	12,310	32,183	0	0	0

*1 Increase and Decrease include conclusion and expiration of AM agreement.

Third Quarter FY2018 Earnings Summary

Matters concerning consolidated statements of income (summary)

During 3Q/FY2018, the sale of rental real estate incidental to portfolio refreshing resulted in a significant increase in sales of real estate and gross profit from sales, resulting in increased revenues and profit compared to the previous year.

(1 million yen)	3Q/FY2016	3Q/FY2017	3Q/FY2018	YoY
Net sales	10,837	10,653	16,333	+53.3%
Gross profit	3,771	2,797	4,098	+46.5%
Selling, general and administrative expenses	1,046	950	973	+2.4%
Operating income	2,725	1,847	3,124	+69.2%
Ordinary income	2,481	1,593	2,859	+79.5%
Profit attributable to owners of parent	1,396	1,078	1,798	+66.8%

Gross profit breakdown

(1 million yen)	3Q/FY2016	3Q/FY2017	3Q/FY2018	YoY
Investment management business	516	10	35	+257.4%
Investment banking business	3,255	2,787	4,062	+45.7%
Gross profit from real estate sales	2,012	1,830	3,220	+76.0%
Gross profit from rental real estate	723	875	798	-8.8%
Same-boat investment income	527	0	0	N/A
Other	-7	82	43	-46.5%
Gross profit total	3,771	2,797	4,098	+46.5%

Selling, general and administrative expenses breakdown

(1 million yen)	3Q/FY2016	3Q/FY2017	3Q/FY2018	Change
Personnel expenses	570	580	618	+37
Land and rent	111	108	110	+2
Commission fee/compensation	135	122	138	+15
Duties and public taxes	42	64	76	+11
Duties and public taxes	185	73	29*1	-44
Selling, general and administrative expenses total	1,046	950	973	+23

*1 Due to the collection of overdue accounts receivable, the reversal of allowance for doubtful accounts (41 million yen) was eliminated from SG&A.

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 sales to enable us to conduct dynamic sales of real estate when we seek to refresh our portfolio.

As of the end of 3Q/FY2018, real estate for sale in process increased by 2,341 million yen on the acquisition of land for rental real estate development.

Consolidated balance sheet / Assets (1 million yen)	FY2017 Year-end	FY2018 (as of end of 3Q)	Change
Total current assets	38,449	41,595	+3,145
Cash and deposits	6,161	7,267	+1,106
Trust deposits	536	463	-73
Inventory assets (real estate for sale)	28,789	28,361	-428
Real estate for sale in process	1,215	3,557	+2,341
Other	1,746	1,946	+199
Total non-current assets	703	765	+62
Total assets	39,153	42,360	+3,207

Consolidated balance sheet / Liabilities and net assets (1 million yen)	FY2017 Year-end	FY2018 (as of end of 3Q)	Change
Total liabilities	27,542	29,167	+1,624
Total current liabilities	2,663	2,912	+249
Short-term loans payable	860	860	0
Current portion of long-term loans payable	698	716	+17
Current portion of long-term non-recourse loans payable	7	15	+7
Other	1,097	1,320	+223
Total non-current liabilities	24,879	26,254	+1,375
Long-term loans payable	22,931	24,634	+1,703
Long-term non-recourse loans payable	740	617	-123
Other	1,207	1,002	-205
Total net assets	11,610	13,193	+1,583
Total shareholders' equity	11,576	13,164	+1,587
Other	33	29	-4
Total liabilities and net assets	39,153	42,360	+3,207
Net D/E ratio*1	1.54	1.40	

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

FY2018 Full-year Earnings Forecast

Our group manages earnings on a full-year basis and thus our earnings forecasts are for the full-year only. Real estate investments with sales originally scheduled for FY2017 but delayed until the following year will contribute to FY2018 performance, which we project will demonstrate significantly improved performance in individual categories compared to FY2017.

(1 million yen)	FY2017 Full-year results	FY2018 Full-year forecast	YoY	FY2018 Progress rate
Net sales	18,766	22,568	+20.3%	72.4%
Gross profit	4,720	6,538	+38.5%	62.7%
Investment manage business	10	45	+339.3%	79.1%
Investment banking business	4,710	6,493	+37.9%	62.6%
Operating income	3,373	5,015	+48.7%	62.3%
Ordinary income	3,060	4,458	+45.7%	64.1%
Profit attributable to owners of parent	2,048	2,815	+37.4%	63.9%

About Group performance

Our Group's main business is real estate investments, which results in a relatively high percentage of sales and income from real estate sales. As a result, our business has the following characteristics.

(1) Short-term performance fluctuations

While the majority of our selling, general and administrative expenses are fixed expenses (personnel expenses, rent, etc.), we tend to record massive sales and income amounts when we sell real estate. As such, quarterly and annual performance may fluctuate wildly depending on sales.

In addition, as the profit margin from the sale of individual real estate investments may vary, profit margins in individual categories are also relatively susceptible to fluctuations compared to the Group's consolidated sale performance. Furthermore, while real estate transactions are influenced by a variety of circumstances, there are no specific seasonal tendencies (ex.: sales concentrated in first half, etc.).

(2) We focus on gross profit over net sales

Net sales are included in the actual sales price for real estate so we focus on gross profit when looking at Group performance. This means that our Group prefers investments with a small transaction volume and high rate of return over large volumes of low return investments.

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, then consolidated shareholders' equity will increase gradually 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	FY2016 (Before 1:2 stock split)	FY2017 (After 1:2 stock split)	FY2018 (Forecast)
Dividends per share	50 yen (Including commemorative dividend of 25 yen)	15.0 yen	18.0 yen
Total dividend payout (1,000 yen)	350,293	210,176	—
Total share buy-back value (1,000 yen)	285,698	—	—

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 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 experts, 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 greatest 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, and is an expert at increasing real estate value.

First Brothers Co., Ltd. Executive Director

Kazutaka Tsuji no

First Brothers Co., Ltd. Executive Director

Yoshinobu Hotta

- 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

- 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

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

Tatsuo Watanabe

- 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

- 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. Has long history in the field of financial administration
- Former chairman of Financial Information Systems Center

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

Akihito Sato

First Brothers Co., Ltd. Corporate Advisor

Tadashi Iwashita

- 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

- 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 at a major general contractor and a foreign investment fund
- Involved in investment projects totaling over 1 trillion yen
- Oversees asset management 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

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Inquiries

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