ITOCHU Advance Logistics Investment Corporation
Summary translation of transcript of presentation and Q&A
for the Fiscal Period ended January 2020

Note: Page numbers in parenthesis indicate corresponding page number of the presentation material.

Investor Presentation

Date of Presentation: March 16, 2020
Means: Video Presentation
Speaker: Junichi Shoji, Representative Director, President & CEO,
ITOCHU REIT Management Co., Ltd.

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[Operational Highlights for the 3rd Fiscal Period ended January 2020]
Please look at the indicators on this slide which highlight our operational status. NAV per unit grew 2.7%, and unrealized appraisal gain grew 10.7%. This 10.7% growth came from 10-basis-point decline in direct cap rate for IMP Noda and IMP Misato, two of the eight properties we owned at the end of the 3rd fiscal period. There are no changes in cap rate for other six properties. DPU for the 3rd fiscal period became ¥2,395, up 3.6% from the 2nd fiscal period.

[Highlights of measures taken]
External Growth: We carried out the first follow-on offering after IPO, to improve our asset size to up to ¥84.1B. The transactions will conclude during the 4th fiscal period.

Internal Growth: We had the first tenant replacement after listing, and the new tenant signed a longer contract than the previous one.

Financial: Excluding ¥1.5B consumption tax loan, post- offering LTV stands at 39.6%. Because we could manage to maintain our leverage in the 30% range, we have borrowing capacity of ¥8.5B if we are to raise the LTV to 45%, which is what we consider as the upper target for the time being. Also, 4 new lenders joined our bank formation after the follow-on offering. We currently have a total of 10 lenders.

ESG: We issued green bonds in December 2019 (for duration of 5 years, with 0.3% coupon). We will continue to maintain and make progress in various ESG certifications. As a new notice, we are planning to revise asset management fees and disposition fees at the General Meeting of Unitholders scheduled on April 28th. I will touch upon this later in this presentation.

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In the 3rd fiscal period, DPU as well as FFO per unit grew compared to the previous fiscal period. For the 3rd fiscal period result details, please refer to Actual (B) section on the middle of the slide. The difference from the forecast (announced on Sep.13, 2019) is shown on the right side.

Our distribution policy aims to payout 70% of FFO. The payout for the 3rd fiscal period was also 70%. Payout ratio relative to AFFO (which we calculate as, "FFO" minus "CAPEX" plus "loan-related non-cash expense") was 69.8%. Because our portfolio is mainly composed of young properties, we can keep our CAPEX low relative to our competitors for the time being. As a result, we can also keep AFFO payout ratio low, and we believe that these aspects would contribute to stable payout of distribution.

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This slide is about the two new properties we are acquiring through the follow-on offering.

IMP Kashiwa 2 is located very close to Joban Expressway Kashiwa interchange. It also has a good access to National Route 16. We consider it as our trophy asset for the time being. We completed acquisition on February 3rd, 2020.

IMP Inzai is an asset we already have 80% ownership. On April 1st, 2020, we will acquire the remaining 20%, to make our ownership 100%.

Appraisal NOI yield for the two properties together is 4.8%. This makes our overall portfolio NOI yield from 9 properties to 5%. Since listing, we have been persistent about not buying over-priced assets and that we would set our target portfolio NOI yield at around 5%. In that sense, we executed exactly what we have been saying.

As you can see on bottom right, our main sponsor, ITOCHU corporation's investment unit holding ratio is maintained at 7%, meaning that the follow-on offering did not result in dilution of the holding ratio. This is one of many examples that show the sponsor's commitment to support IAL.

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On the middle of this slide, you will find forecasts for the 4^{th} fiscal period. This was already announced on January 6^{th}, 2020, along with the announcement about the follow-on offering. On your right, gap analysis with the 3^{rd} fiscal period results are shown. While acquisition of two new properties will boost operating revenues, operating expenses will incur from the new assets. Also, unlike the ordinary fiscal periods, General Meeting of Unitholders related expenses will incur in the 4^{th} fiscal period.

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This is a new slide we added from this presentation, showing the trend on earnings distribution per unit. On your left, the gap between forecast and result for the 3^{rd} fiscal period is shown.

Let us remind you that when comparing the 3^{rd} fiscal period result and the 4^{th} fiscal period forecast, the number of outstanding units increased (from 357,143 units to 486,000 units) due to the offering. Therefore, denominators used for calculation of earnings per unit are not the same.

With the offering, leasing business income and non-operating expenses will both increase. Leasing business income per unit will increase by ¥111. Of the increase, ¥86 is attributable to property and city planning taxes effect. The taxes for the properties acquired during the 2^{nd} fiscal period (in April 2019) will incur from the 4th fiscal period. Meanwhile, the taxes for the two new properties we acquire during the 4^{th} fiscal period will not incur until the 6^{th} fiscal period. Consequently, total property and city planning taxes will increase, but because the number of outstanding units has increased, the taxes per unit will decrease. After the 6^{th} fiscal period, the taxes will incur entirely.

The forecast comparison between the 4^{th} and the 5^{th} fiscal periods is shown on the right.

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Capital increase through the follow-on offering is expected to boost DPU by 4.2%, as disclosed in the supplementary material dated January 6^{th}, 2020. The normalized DPU shown here is the 5^{th} fiscal period DPU forecast after adjusting property and city planning taxes for new properties. NAV per unit will increase by 1.2% from new property acquisitions. In the same supplementary material, we explained that Post-offering LTV forecast (excluding consumption tax loan) would be 40.9%. However, since premium from new issuance was higher than expected, we will able to maintain LTV at low level, that is, at 39.6%, which is still in the 30% range.

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These six pie charts are what we usually include in our presentations. To control portfolio quality, we believe management with these indicators in mind is necessary. Naturally, half a year has passed since the previous fiscal period, but remaining lease term shown on top right is 6.4 years, a 0.3 years improvement. Average property age is kept at 3.1 years. “The ITOCHU Group and the Group customer tenant” on bottom left has increased. Tenant industry on bottom right shows further improvement in quality, now that it includes tenants of newly acquired properties, who are E-commerce and major 3PL operators.

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After acquisition of two new properties, we have nine properties in our portfolio. Summary of IMP Kashiwa2 is shown on the right.

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This is our updated strategic roadmap.

DPU: We will continue to seek 4% to 5% DPU growth through both external and internal growth.

External Growth: Although our asset size grew to ¥84.1B through the follow-on offering, it is still small. Therefore, we will continue to acquire properties in the pipeline. In addition, we will utilize the bridge scheme already in place hoping to acquire third party properties and what we call “other real estate.” Also, we are very conscious about becoming a component of major indices.

Internal Growth: Leasing of the rooftop of IMP Inzai for Solar Panel installation has been broadly completed. With tenants facing contract expiry down the road, we will seek to conclude longer contracts at renewal, and at the same time, will try to close as much rent gap as possible whenever we can.

LTV: While keeping LTV upper limit at 45% for the time being, we would also like to consider introducing commitment line at the appropriate timing.

ESG: We are proud of our ESG efforts we have been making in many areas. During the 4th fiscal period, the asset management company’s full-time directors are scheduled to utilize cumulative investment unit investment program. Further notice will be given upon finalization.

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The five properties on the left are the pipeline properties. For all of them we have preferential negotiation rights, and have already achieved 100% occupancy rate. We intend to acquire these properties through equity offering and through other measures. Also, our sponsor group is now working to acquire some land for development projects, including land in areas other than Kanto area. We hope to give you an update when time is ripe.

On the right, our thoughts on third-party property acquisition are explained. Currently we have increasing opportunities to receive information and inquiries, including those regarding land with leasehold interest. We will look at geographic area, and if the property is likely to generate long term stable NOI, and is likely to become long term stable distribution source, we will seriously consider acquisition.

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Let us now touch upon our thoughts on leasing. It is about how we intend to secure long term stable cash flow. The top half of the slide shows the example of recently acquired IMP Kashiwa 2. IAL, in its leasing activities aims to make "long term contracts with quality tenants". If you look at our portfolio construction, many are single tenant properties. We construct portfolio with properties meeting tenants' locational strategy, with properties that have tenant stickiness. We believe this is the most important point in securing long term stable cash flow. In that sense, IMP Kashiwa2 is a typical example in that it is a single tenant property leased to a major 3PL operator under a long-term lease contract. On the other hand, however, the specification of the property allows us to divide it and make it a multi-tenant property in the future, if necessary. So, we secure versatility of properties before securing tenant stickiness.

The bottom half shows the spread of lease expiration timing, in percentage of total rent. You can see from this chart that contract expiries are relatively far ahead. This is reflection of our long-term contract strategy.

Leasing activities are consigned to ITOCHU Corporation. They start activities one year ahead of expiries. For the contract expiring during fiscal period ending July 2020, we replaced tenant for the first time after listing, and were able to extend the expiry to fiscal term ending July 2025. For the 2.3% portion that will expire during fiscal period ending January 2021, we are in talks with the tenant (whose contract will expire on September 2020) with a high probability of renewal. The 6.9% portion expiring during fiscal period ending July 2021 comes from three tenants in two properties. Activities for this portion will also be started going forward.

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LTV stands at 39.6%, controlled successfully at low level. Average debt cost became 0.56%. As low interest rate environment continues, for our future debt financing for property acquisition and for others, we will seek to fix and further bring down borrowing rate. Average debt duration is 5.2 years, satisfying our target of 5-plus-years. Our long-term issuer rating by JCR is A+(Stable). We will continue to have regular communication with the rating agency and work toward credit rating improvement.

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The next explanation is about cash management. Left hand bars indicate the amount of FFO and how it was used. IAL's policy is to payout about 70% of FFO. Bottom right shows comparison of FFO payout ratio for J-REITs specialized in logistics facilities. We believe IAL's lower FFO payout ratio gives us advantage over the peers.

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Our ESG efforts are explained on this slide. It is the major policy of IAL as well as the asset management company to continue to proactively take ESG initiatives.

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At the first General Meeting of Unitholders after listing (scheduled to be held on April 28th, 2020), we are going to propose amendment to the Articles of Incorporation, to revise asset management fee structure, for greater alignment of interests with unitholders.

First, we will propose to revise the upper limit for one of the rates applied to calculation of asset management fees. As you can see on the slide, there are three components to calculate asset management fees. We are planning to propose to revise the first portion (which is linked to total assets) to halve the upper limit for the applicable rate from 0.2% to 0.1%. Together with this cut, as for the third portion, (which is linked to EPU), while maintaining the current upper limit of 0.005%, we would like to increase fees from the third layer as a percentage of total asset management fees. We plan to apply these changes from the 5th fiscal period ending January 2021, but even with the revision, total asset management fees will be almost the same with the one we used to calculate the 5th fiscal period forecast announced today.

In addition, revisions to upper limit on disposition fee rate will be proposed. Currently, in case the transaction involves an interested party, the maximum fee rate is 0.5%, and otherwise 1.0%. We are proposing to align these rates to the lower level, which is maximum 0.5%. At the same time, we will propose to abandon disposition fee for loss incurring transactions, although we do not intend to carry out any such transaction, in principle.

The specific rates to be applied will be decided at IAL board of directors meeting.

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This slide shows the logistics market situation. Top left shows Kanto area market, where our portfolio and pipeline properties are located. As you can see, vacancy rate is stably low, and supply-demand is balanced. In 2021, relatively high supply is expected, but we hear leasing is progressing smoothly, and there is still some time until 2021. Therefore, we expect supply-demand to ultimately balance, and the market to trend bullishly.

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One of our main tenant industries is E-commerce. The business expansion of such tenant industry is a supporting evidence for the steadiness of logistics real estate market. Compared to other major countries of the world, Japan's E-commerce ratio is still low. We can expect this ratio to go up, but it is hard to imagine it going down. We therefore believe logistics REITs that support E-commerce businesses will stay steady.

Q&A Session

Date: March 17, 2020
Means: Teleconference
Speaker: Junichi Shoji, Representative Director, President & CEO,
ITOCHU REIT Management Co., Ltd.

Q1: You mentioned that you aim for 4 to 5% distribution per unit (DPU) growth. In the current soft market, how are you planning to achieve such goal?

A1: This is a new portion that we decided to include in the material from this presentation. We aim for the 4 to 5% growth through combination of external and internal growth. As for the external growth, equity offering will be the main driver, for which we will make decisions in consideration of equity size and implied cap rates, among other things. Use of loans would also be an option depending on the circumstances. As for the internal growth, we will continue to reduce leasing costs and debt costs, and will also try to increase rent per tsubo when we can at the time of lease renewal or re-tenanting.

Q2: Are acquisition costs flexible with respect to the current pipeline properties with preferential negotiation rights? I assume that it will depend on the capital market and the real estate market at the future point in time, but would you say that the acquisition costs are flexible enough so that you can acquire those pipeline properties at higher cap rates than that of the first follow-on offering, thereby contributing to achievement of the 4 to 5 % DPU growth that you commit to?

A2: With the first follow-on offering, we acquired trophy assets for ITOCHU Advance Logistics Investment Corporation ("IAL") at an average appraisal NOI yield of 4.8%. Current pipeline properties include those located in the Tokyo bay area or within Tokyo 23 wards. We intend to acquire those properties at appropriate cap rates by, for example, combining these properties with future pipeline properties (which are yet to be disclosed) or using appropriate bridge schemes. We will continue aiming to maintain the post-acquisition portfolio NOI yield at around 5%. Having said that, if market appraisal cap rates go up in the future and properties become cheaper, we would consider that factor as well, when negotiating with the sponsors. For a small-cap REIT like IAL, each property has a relatively large impact on the portfolio, so we intend to carry out our price negotiations carefully.

Q3: You mentioned the 4 to 5% DPU growth target. However, based on the lease contract expiry ladder on page 18 of the presentation material, I've noticed that, as for internal growth opportunities, the timings of expiry rather seem to be apart and relatively far ahead. Based on such observation, is it fair to understand that you intend to achieve the growth target, not as a constant growth achieved in each fiscal period, but as a growth evened out across a certain period?

A3: As you have pointed out, internal growth opportunities are concentrated in certain fiscal periods. We intend to combine external growth driver with the internal growth strategically, for achieving the target.

Q4: Would you tell us the level of target cap rate you have in your mind? You seem to have attractive yield for your current portfolio, but how about for pipeline properties?

A4: Although we have not officially started price negotiations with the sponsors for the pipeline properties developed by the sponsors, we and the sponsors have exchanged thoughts and do recognize the price levels that each party has in mind. Based on that, we think that there is a possibility to maintain the portfolio NOI yield at around 5% even after the acquisition of the pipeline properties.

Q5: What are your thoughts on a share buyback? Do you have any target in mind as to the timing, such as that a certain duration of a volatile equity market would trigger a share buyback?

A5: I think we should make a cool-headed decision on that, including whether or not such initiative would be welcomed by investors in the market with almost panic-driven volatilities, like the one we are currently facing. I've seen that some stock companies have carried out share buybacks lately, but the market seems to be not reacting so much. We do not have a concrete target in mind at the moment, especially in the current market which it is hard to read. Having said that, we would consider share buyback as an option, together with a possible additional acquisition of IAL's investment units by the sponsors, if we decide that such measures are required.

Q6: Some properties in the current pipeline such as i Missions Park ("IMP") Adachi or IMP Ichikawa-Shiohama are expected to have relatively low cap rates considering their locations. If IAL is to acquire these lower cap-rate properties, I would assume that it will naturally be hard to maintain the post-acquisition portfolio NOI yield at around 5%. How do you plan to achieve the target portfolio yield?

A6: As you have indicated, it is true that some of the current pipeline properties are closer to central Tokyo, which would naturally make their cap rates relatively low. However, the sponsor group seems to be currently sourcing properties in Kanto area as well as Chubu and Keihan areas (I would like to add that these properties, located in areas other than Tokyo metropolitan area, are not being developed for the sake of improving portfolio NOI yield, but they are developed as a result of the choice of areas where long lease contracts with quality tenants can be executed). In addition, we have been receiving inquiries and information regarding the "Other Real Estate," such as process centers, as well as land with leasehold interest. One option we will consider going forward is acquiring these types of assets together with the aforementioned low cape-rate pipeline properties.

Q7: Would you say that bridge schemes you currently have in place are sustainable?

A7: The bridge schemes currently utilized by IAL consist of two types: a scheme using a lease company, and a scheme using a fund. As for the scheme using a lease company, we have been able to construct a cost-efficient scheme, which we think is highly sustainable. Both schemes are currently in use, and we will decide which scheme to use on a case-by-case basis upon discussions with the sponsors. Either case, I would say that they are highly sustainable.

Q8: How realistic is a case where the sponsor, ITOCHU Corporation, will additionally purchase IAL's investment units? Last time the sponsor purchased IAL's investment units via secondary market, IAL was struggling despite the bullish market trend. Currently, on the contrary, the market as a whole is soft. Do you think that such purchase of investment units by the sponsor is viable option in the current market as well?

A8: I agree that the sponsor might consider it difficult to carry out such action in the current, highly uncertain market. I assume that it will be hard for the sponsor to take any such action unless the market regains a certain extent of clarity.

Q9: You mentioned that some of the parcels from Asian countries are subject to delay (due to spread of Coronavirus). Are there any risk that any of the fixed rents IAL receives from tenants will be reduced or exempted?

A9: Our properties are occupied by large, quality tenants under long fixed-term lease contracts, and the supply chain in question seems to be also gradually recovering. Therefore, we think that rent reductions will not likely happen. IAL has a portfolio consisting of properties leased under fixed-term lease contracts with relatively long remaining lease periods (meaning that the timings of renewal and re-tenanting are far ahead), and which can generate highly stable NOI. We would like to turn this situation into an opportunity for having IAL's portfolio re-assessed by the investors in the context that it can generate stable NOI which translates into stable DPU.

Q10: The pie chart in page 11 shows that more than 80% of IAL's tenants consists of the ITOCHU Group and the Group customer tenants. Do you consider that such tenant composition contributes to NOI or rent stabilities even in the current market conditions?

A10: We would like you to understand that such tenant composition enables us to closely communicate with tenants and allows us to recognize their situations well enough to make the decision to have them occupy IAL's properties. In that sense, we believe that such tenant composition would contribute to the NOI and rent stabilities of IAL's portfolio

End