TOSEI | 8923 |

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On **August 9, 2018,** Shared Research updated the report following interviews with the company regarding 1H FY11/18 results.

1H FY11/18 results

Overview

In 1H FY11/18, Tosei posted IFRS-based consolidated revenues of JPY32.5bn (+23.4% YoY), operating profit of JPY6.9bn (+10.3%), profit before tax of JPY6.5bn (+11.2%), and profit attributable to owners of parent of JPY4.5bn (+13.2%). Versus full-year forecasts, 1H revenues reached 47.9%, operating profit 62.9%, and profit 66.5% of the full-year targets of JPY67.8bn, JPY11.0bn, and JPY6.7bn, respectively.

The Revitalization segment reported brisk sales of entire buildings (income-generating office buildings, rental condominiums and so forth), while the Development segment similarly had strong sales of condominiums and detached houses. In acquisitions, the company utilized conventional purchasing methods but also made use of M&A to buoy future earnings prospects, proactively purchasing income-generating properties and sites for development that will serve as sources of future earnings. Versus acquisition target of JPY80bn for FY11/18 (expected disposition value), in 1H the company made acquisitions worth JPY35.1bn on a delivery basis (43.8% of the full-year forecast) and JPY53.6bn on a contract basis (67.0%).

Revenue

Revenue rose 23.4% YoY to JPY32.5bn. Progress versus full-year target was 47.9%, which was broadly in line with plan according to Tosei. The company attributes the progress rate below 50% to the fact that in most years, 2H revenue includes JPY10bn in properties supplied to Tosei Reit Investment Corporation (bridge transaction for the REIT). In FY11/17, 1H revenues accounted for 38.1% of the full-year target.

By segment, revenue was down 2.0% YoY at JPY17.6bn in Revitalization, up 301.7% at JPY8.6bn in Development (with a substantial contribution from condominium sales in The Palms Yutenji Master Place), down 3.2% at JPY2.9bn in Rental, down 19.3% at JPY1.3bn in Fund and Consulting, and up 18.4% at JPY1.9bn in Property Management.

Profits

Operating profit rose 10.3% YoY to JPY6.9bn. By segment, operating profit fell 11.9% YoY to JPY4.2bn in Revitalization. Development saw an operating profit of JPY1.4bn (vs. operating loss of JPY219mn 1H FY11/17). Operating profit was down 4.4% to JPY1.2bn in Rental, down 22.7% to JPY708mn in Fund and Consulting, and up 51.9% to JPY204mn in Property Management.

Segments

Revitalization: Revenue: JPY17.6bn (-2.0% YoY); operating profit: JPY4.2bn (-11.9%)

At the Revitalization segment, the company sold 24 value-added properties and 15 units under its Restyling business. The value-added properties included Nishidai Tosei Building (Itabashi-ku, Tokyo), Kichijoji Ito Building (Musashino, Tokyo), Kunitachi 219 Building (Kunitachi, Tokyo) and T-Rhythmic SOKA (Soka, Saitama). It also sold properties such as Hilltop Yokohama Negishi (Yokohama, Kanagawa) in the Restyling business. The company forecasted a 2.2% YoY decline in revenue for the segment in FY11/17; 1H FY11/18 segment revenue also dropped by a similar extent.
The segment's GPM for 1H FY11/18 was 28.8% (-2.2pp YoY). The segment was able to sell at high margins properties acquired in the past via M&A, and properties that were entirely vacant at the time of acquisition and subsequently fully leased.

The company acquired a total of 32 income-generating office buildings and rental condominiums (vs. 24 in 1H FY11/17) and seven land lots (three).

Development: Revenue: JPY8.6bn (+301.7% YoY); operating profit: JPY1.4bn (vs. operating loss of JPY219mn in 1H FY11/17)
The company focused on sale of new condominiums and detached houses in 1H. In new condominiums, it sold 85 of 89 units at The Palms Yutenji Master Place (Setagaya-ku, Tokyo), and of the remaining four units it had inked sales contracts for two by end-June 2018. The company also sold 43 houses in developments including The Palms Court Kamakura Shiromeguri (Kamakura, Kanagawa; 86 units in total), The Palms Court Kashiwa Hatsuishi (Kashiwa, Chiba; 95 units in total) and The Palms Court Koshigaya Lake Town (Koshigaya, Saitama; 68 units in total).

The segment's GPM for 1H FY11/18 was 26.0% (+7.3pp YoY), buoyed by a 28.7% GPM for the new condominium The Palms Yutenji Master Place (the GPM for detached houses was just under 20%).

Tosei made varied acquisitions in 1H FY11/18, acquiring one land lot to build condominiums, one land lot to build a hotel, one land lot to build a logistics facility, and five land lots for developing 35 detached houses.

Rental: Revenue: JPY2.9bn (-3.2% YoY); operating profit: JPY1.2bn (-4.4%)
The company sold 17 buildings out of its inventory assets held for leasing purposes (vs. 22 in 1H FY11/17) and acquired a total of 24 properties including income-generating office buildings and rental condominiums (17). It focused on leasing out vacant space in newly acquired properties, as well as leasing activities for existing non-current assets and inventories Tosei owned 95 buildings in this segment as of end-1H FY11/18 (+six buildings from end-FY11/17). This can be broken down to 39 office and commercial buildings (32 at end-1H FY11/17), 53 condominiums (44), and three others (three). Rental revenue from non-current assets increased 17.9% YoY, accounting for 50.3% of total revenue (vs. 41.3% in 1H FY11/17). Activity in this segment was in line with the strategy outlined in Tosei's medium-term plan, that of achieving a greater profit weighting for the so-called "Stable business," defined by the company as the Rental business, Fund and Consulting business, and Property Management business. GPM in 1H FY11/18 was 45.9% (-1.6pp YoY).

Fund and Consulting: Revenue: JPY1.3bn (-19.3% YoY); operating profit: JPY708mn (-22.7%)
The balance of assets under management (AUM) as of end-1H FY11/18 was JPY635.3bn, up JPY83.1bn from end-FY11/17. The balance decreased by JPY8.5bn mainly from disposition of properties by funds, and increased by JPY91.6bn primarily from signing a new asset management contract involving large-scale properties. As a consequence, asset management revenue, which provides a stable source of income, increased 51.2% YoY to JPY756mn. However, revenue for the segment as a whole fell 19.3% YoY in the absence of roughly JPY500mn in one-time revenues (brokerage fees and so forth) booked in 1H FY11/17, and operating profit fell 22.7%. GPM in 1H FY11/18 was 94.4% (+3.6pp YoY), and the OPM was 52.6%, down 2.5pp.

Property Management: Revenue: JPY1.9bn (+18.4% YoY); operating profit: JPY204mn (+51.9%)

The number of managed properties rose as the company endeavored to acquire new contracts while maintaining existing contracts. As of end-1H FY11/18, the company managed a total of 667 buildings (+2 from end-FY11/17), comprising 391 non-residential properties including office and commercial buildings, schools, hotels, and nurseries (-4 from end-FY11/17) and 276 residential properties (+6) such as rental condominiums and apartments for sale. In addition to increasing managed properties, the company negotiated for higher commissions and reviewed the cost structure, and as a result segment revenue and profit margin have been trending upward. GPM in 1H FY11/18 was 30.9% (+1.5pp YoY),

Development pipeline

Including development properties already completed, the pipeline includes three hotels (four if one conversion is included), four commercial facilities, two logistics facilities, and five condominiums for sale and rental. The company made three additions to the pipeline in 1H FY11/18, comprising two logistics facilities in Sagamihara, Kanagawa, and Hasuda, Saitama, and a condominium project in Toda, Saitama.

Topics

Promoting property acquisitions via M&A

Since 2016 Tosei has acquired about 30 properties worth about JPY17.0bn (expected disposition value) through the M&A of five real estate companies. With the M&A of Company K in March 2016, Tosei acquired seven properties, including five income-generating properties on the west side of Ikebukuro Station. With Company F in July 2016 it acquired six properties on the south side of Nakano Station; with Company K in March 2017 it acquired seven properties located mainly in Tokyo; with Company M in December 2017 it acquired nine properties in the Tokyo Metropolitan area; and with Company S in March 2018, it acquired four properties near Kawasaki station. According to Tosei, real estate M&A transactions afford the seller (owner) a tax advantage, while the buyer is able to acquire properties at a discount, as even with adequate due diligence it takes on financial risk and the risk of hiring some of the acquired company's employees. As such, properties acquired through M&A have higher profitability than those acquired by normal acquisition. In 1H FY11/18, Tosei set up an M&A/Group Strategy Department to facilitate further M&A activity.

Entry into logistics business

Tosei has launched its first logistics development project, the development of a logistics facility in Sagamihara, Kanagawa, with a view to harnessing the Property Management and Fund and Consulting businesses' wealth of knowhow concerning the logistics business*. The company sees a business opportunity in logistics facilities, as investment properties for which brisk demand is likely to continue due to the increased needs of the e-commerce market (including online mail-order businesses) and 3PL service providers, where growth continues to be strong. In addition to expanding its product lineup in the Revitalization and Development businesses (selling newly built and revitalized logistics facilities to investors), Tosei aims to develop the logistics business as its sixth main business over the medium to long term. Rather than acquiring large facilities of 10,000–20,000 tsubo (approximately 33,000–66,000sqm) in the manner of large real estate companies (especially those affiliated with former zaibatsu groups), the company intends to deal in small to midsized facilities of at least 3,000 tsubo (9,900sqm), with an eye to capturing demand for extra floor space from 3PL service providers. Tosei has ample expertise in property management, which should stand the company in good stead when it comes time to lease out logistics facilities developed in-house.

* Tosei has acquired a 5,885sqm (1,780 tsubo) site for the Sagamihara Logistics Development Project, where it plans to build a facility with total floor area of 11,868sqm (3,590 tsubo), with completion scheduled for March 2020. Similarly, the company plans to acquire a 17,404sqm (5,264 tsubo) site for the Hasuda Logistics Development Project, where it plans to build a facility with total floor area of 25,058sqm (7,580 tsubo), with completion scheduled for March 2020.

Quarterly earnings (cumulative)

Cumulative (JPYmn)	FY11/16				FY11/17				FY11/18			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
Revenue	13,527	30,655	39,139	49,818	14,677	26,360	41,978	57,754	18,310	32,521		
YoY	17.4%	37.2%	41.7%	15.8%	8.5%	-14.0%	7.3%	15.9%	24.7%	23.4%		
Revitalization	2,361	15,424	19,946	25,810	10,939	17,949	29,287	40,268	14,425	17,585		
YoY	-67.2%	12.1%	34.2%	-0.7%	363.4%	16.4%	46.8%	56.0%	31.9%	-2.0%		
% of revenue	17.5%	50.3%	51.0%	51.8%	74.5%	68.1%	69.8%	69.7%	78.8%	54.1%		
Development	8,724	10,097	11,211	13,139	969	2,145	3,499	5,197	766	8,614		
YoY	275.3%	142.5%	99.1%	98.9%	-88.9%	-78.8%	-68.8%	-60.4%	-20.9%	301.7%		
% of revenue	64.5%	32.9%	28.6%	26.4%	6.6%	8.1%	8.3%	9.0%	4.2%	26.5%		
Rental	1,101	2,417	3,825	5,282	1,472	2,988	4,601	6,195	1,397	2,893		
YoY	27.2%	29.6%	27.4%	25.4%	33.7%	23.6%	20.3%	17.3%	-5.1%	-3.2%		
% of revenue	8.1%	7.9%	9.8%	10.6%	10.0%	11.3%	11.0%	10.7%	7.6%	8.9%		
Fund and Consulting	563	1,078	1,711	2,303	469	1,641	2,130	2,763	674	1,325		
YoY	117.4%	39.6%	24.4%	-5.6%	-16.7%	52.3%	24.5%	20.0%	43.7%	-19.3%		
% of revenue	4.2%	3.5%	4.4%	4.6%	3.2%	6.2%	5.1%	4.8%	3.7%	4.1%		
Property Management	642	1,437	2,175	2,944	828	1,637	2,462	3,331	975	1,938		
YoY	-8.1%	-0.4%	-2.7%	-4.1%	29.0%	13.9%	13.2%	13.1%	17.7%	18.4%		
% of revenue	4.7%	4.7%	5.6%	5.9%	5.6%	6.2%	5.9%	5.8%	5.3%	6.0%		
Other	136	202	271	340	-	-	-	0	73	166		
YoY	-19.7%	-40.8%	-48.0%	-51.0%	nm	nm	nm	nm	nm	nm		
% of revenue	1.0%	0.7%	0.7%	0.7%	0.0%	0.0%	0.0%	0.0%	0.4%	0.5%		
Cost of revenue	7,347	18,907	24,921	33,468	9,188	16,859	27,884	40,938	12,119	21,749		
YoY	-7.0%	23.8%	34.0%	7.6%	25.1%	-10.8%	11.9%	22.3%	31.9%	29.0%		
Cost ratio	54.3%	61.7%	63.7%	67.2%	62.6%	64.0%	66.4%	70.9%	66.2%	66.9%		
Gross profit	6,180	11,748	14,219	16,350	5,489	9,502	14,094	16,817	6,191	10,772		
YoY	70.3%	66.2%	57.4%	37.2%	-11.2%	-19.1%	-0.9%	2.9%	12.8%	13.4%		
GPM	45.7%	38.3%	36.3%	32.8%	37.4%	36.0%	33.6%	29.1%	33.8%	33.1%		
SG&A expenses	2,053	4,073	5,396	7,070	1,661	3,260	5,013	6,983	1,849	3,885		
YoY	62.5%	61.7%	45.4%	40.7%	-19.1%	-20.0%	-7.1%	-1.2%	11.3%	19.2%		
SG&A ratio	15.2%	13.3%	13.8%	14.2%	11.3%	12.4%	11.9%	12.1%	10.1%	11.9%		
Operating profit	4,128	7,675	8,823	9,280	3,828	6,242	9,081	9,834	4,341	6,887		
YoY	74.5%	68.7%	65.8%	34.6%	-7.3%	-18.7%	2.9%	6.0%	13.4%	10.3%		
OPM	30.5%	25.0%	22.5%	18.6%	26.1%	23.7%	21.6%	17.0%	23.7%	21.2%		
Revitalization	182	3,627	3,963	4,001	3,418	4,800	7,310	7,845	3,794	4,228		
YoY	-90.1%	10.0%	17.7%	-4.1%	1775.3%	32.3%	84.4%	96.1%	11.0%	-11.9%		
% of total OP	4.4%	47.3%	44.9%	43.1%	89.3%	76.9%	80.5%	79.8%	87.4%	61.4%		
OPM	7.7%	23.5%	19.9%	15.5%	31.2%	26.7%	25.0%	19.5%	26.3%	24.0%		
Development	3,580	3,660	3,703	3,674	-173	-219	-311	-409	-145	1,408		
YoY	775.1%	516.7%	480.5%	586.8%	nm	nm	nm	nm	nm	nm		
% of total OP	86.7%	47.7%	42.0%	39.6%	-4.5%	-3.5%	-3.4%	-4.2%	-3.3%	20.4%		
OPM	41.0%	36.2%	33.0%	28.0%	-17.9%	-10.2%	-8.9%	-7.9%	-19.0%	16.3%		
Rental	462	1,003	1,742	2,390	661	1,303	1,935	2,582	630	1,246		
YoY	26.3%	19.3%	24.1%	33.0%	43.1%	29.9%	11.1%	8.0%	-4.6%	-4.4%		
% of total OP	11.2%	13.1%	19.7%	25.8%	17.3%	20.9%	21.3%	26.3%	14.5%	18.1%		
OPM	41.9%	41.5%	45.5%	45.2%	44.9%	43.6%	42.1%	41.7%	45.1%	43.1%		
Fund and Consulting	210	430	742	951	160	915	1,071	1,274	378	708		
YoY	312.5%	27.7%	10.0%	-35.0%	-24.0%	112.6%	44.3%	33.9%	136.5%	-22.7%		
% of total OP	5.1%	5.6%	8.4%	10.3%	4.2%	14.7%	11.8%	13.0%	8.7%	10.3%		
OPM	37.3%	39.9%	43.4%	41.3%	34.1%	55.7%	50.3%	46.1%	56.0%	53.4%		
Property Management	28	70	98	141	76	135	213	278	108	204		
YoY	7.3%	-20.8%	-3.9%	-3.8%	170.6%	91.4%	116.4%	96.9%	43.0%	51.9%		
% of total OP	0.7%	0.9%	1.1%	1.5%	2.0%	2.2%	2.3%	2.8%	2.5%	3.0%		
OPM	4.4%	4.9%	4.5%	4.8%	9.2%	8.2%	8.6%	8.4%	11.1%	10.5%		
Other	-1	-24	-22	-18	1	1	0	-75	6	53		
YoY	nm	nm	nm	nm	nm	nm	nm	nm	nm	nm		
% of total OP	0.0%	-0.3%	-0.3%	-0.2%	0.0%	0.0%	0.0%	-0.8%	0.1%	0.8%		
OPM	-0.9%	-11.8%	-8.2%	-5.3%	nm	nm	nm	nm	8.8%	32.1%		
Adjustments	-334	-1,092	-1,403	-1,861	-313	-693	-1,137	-1,661	-430	-961		
% of total OP	-8.1%	-14.2%	-15.9%	-20.0%	-8.2%	-11.1%	-12.5%	-16.9%	-9.9%	-13.9%		
Pre-tax profit	3,915	7,240	8,203	8,450	3,659	5,857	8,522	9,049	4,150	6,512		
YoY	78.7%	73.6%	72.9%	39.9%	-6.5%	-19.1%	3.9%	7.1%	13.4%	11.2%		
Pre-tax margin	28.9%	23.6%	21.0%	17.0%	24.9%	22.2%	20.3%	15.7%	22.7%	20.0%		
Profit attributable to owners of parent	2,611	4,744	5,379	5,547	2,501	3,932	5,755	6,155	2,848	4,452		
YoY	87.8%	78.8%	76.4%	34.1%	-4.2%	-17.1%	7.0%	11.0%	13.9%	13.2%		
Profit margin	19.3%	15.5%	13.7%	11.1%	17.0%	14.9%	13.7%	10.7%	15.6%	13.7%		

Source: Shared Research based on company data

Note: Figures less than JPY1mn are rounded up (in figures released by the company, amounts less than JPY1mn were discarded)

Quarterly earnings

Quarterly (JPYmn)	FY11/16				FY11/17				FY11/18			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
Revenue	13,527	17,128	8,484	10,679	14,677	11,683	15,618	15,776	18,310	14,211		
YoY	17.4%	58.3%	60.5%	-30.6%	8.5%	-31.8%	84.1%	47.7%	24.7%	21.6%		
Revitalization	2,361	13,063	4,522	5,864	10,939	7,009	11,338	10,981	14,425	3,160		
YoY	-67.2%	99.4%	310.3%	-47.3%	363.4%	-46.3%	150.7%	87.3%	31.9%	-54.9%		
% of revenue	17.5%	76.3%	53.3%	54.9%	74.5%	60.0%	72.6%	69.6%	78.8%	22.2%		
Development	8,724	1,373	1,114	1,927	969	1,175	1,354	1,698	766	7,847		
YoY	275.3%	-25.3%	-24.1%	97.9%	-88.9%	-14.4%	21.6%	-11.9%	-20.9%	567.6%		
% of revenue	64.5%	8.0%	13.1%	18.0%	6.6%	10.1%	8.7%	10.8%	4.2%	55.2%		
Rental	1,101	1,316	1,408	1,457	1,472	1,517	1,612	1,594	1,397	1,496		
YoY	27.2%	31.8%	23.8%	20.4%	33.7%	15.2%	14.5%	9.4%	-5.1%	-1.4%		
% of revenue	8.1%	7.7%	16.6%	13.6%	10.0%	13.0%	10.3%	10.1%	7.6%	10.5%		
Fund and Consulting	563	515	634	592	469	1,172	488	633	674	651		
YoY	117.4%	0.3%	4.9%	-44.4%	-16.7%	127.9%	-22.9%	7.1%	43.7%	-44.5%		
% of revenue	4.2%	3.0%	7.5%	5.5%	3.2%	10.0%	3.1%	4.0%	3.7%	4.6%		
Property Management	642	795	737	770	828	808	825	868	975	963		
YoY	-8.1%	6.9%	-7.0%	-7.8%	29.0%	1.7%	11.9%	12.8%	17.7%	19.2%		
% of revenue	4.7%	4.6%	8.7%	7.2%	5.6%	6.9%	5.3%	5.5%	5.3%	6.8%		
Other	136	65	69	69	-	-	-	0	73	93		
YoY	-19.7%	-61.8%	-61.6%	-59.9%	nm	nm	nm	nm	nm	nm		
% of revenue	1.0%	0.4%	0.8%	0.6%	0.0%	0.0%	0.0%	0.0%	0.4%	0.7%		
Cost of revenue	7,347	11,560	6,013	8,548	9,188	7,671	11,026	13,054	12,119	9,630		
YoY	-7.0%	56.7%	81.0%	-31.6%	25.1%	-33.6%	83.4%	52.7%	31.9%	25.5%		
Cost ratio	54.3%	67.5%	70.9%	80.0%	62.6%	65.7%	70.6%	82.7%	66.2%	67.8%		
Gross profit	6,180	5,568	2,471	2,131	5,489	4,012	4,593	2,722	6,191	4,581		
YoY	70.3%	61.8%	25.9%	-26.0%	-11.2%	-27.9%	85.9%	27.7%	12.8%	14.2%		
GPM	45.7%	32.5%	29.1%	20.0%	37.4%	34.3%	29.4%	17.3%	33.8%	32.2%		
SG&A expenses	2,053	2,020	1,323	1,674	1,661	1,598	1,754	1,969	1,849	2,035		
YoY	62.5%	60.8%	11.0%	27.6%	-19.1%	-20.9%	32.6%	17.6%	11.3%	27.3%		
SG&A ratio	15.2%	11.8%	15.6%	15.7%	11.3%	13.7%	11.2%	12.5%	10.1%	14.3%		
Operating profit	4,128	3,548	1,148	457	3,828	2,414	2,839	753	4,341	2,546		
YoY	74.5%	62.3%	48.9%	-70.9%	-7.3%	-32.0%	147.3%	64.9%	13.4%	5.5%		
OPM	30.5%	20.7%	13.5%	4.3%	26.1%	20.7%	18.2%	4.8%	23.7%	17.9%		
Revitalization	182	3,445	336	38	3,418	1,383	2,509	535	3,794	434		
YoY	-90.1%	137.8%	375.4%	-95.3%	1775.3%	-59.9%	647.2%	1298.8%	11.0%	-68.6%		
% of total OP	4.4%	97.1%	29.3%	8.4%	89.3%	57.3%	88.4%	71.1%	87.4%	17.0%		
OPM	7.7%	26.4%	7.4%	0.7%	31.2%	19.7%	22.1%	4.9%	26.3%	13.7%		
Development	3,580	79	43	-29	-173	-46	-92	-98	-145	1,554		
YoY	775.1%	-56.9%	-2.5%	nm	nm	nm	nm	nm	nm	nm		
% of total OP	86.7%	2.2%	3.8%	-6.3%	-4.5%	-1.9%	-3.2%	-13.0%	-3.3%	61.0%		
OPM	41.0%	5.8%	3.9%	-1.5%	-17.9%	-3.9%	-6.8%	-5.8%	-19.0%	19.8%		
Rental	462	541	739	648	661	642	632	647	630	616		
YoY	26.3%	13.9%	31.4%	64.5%	43.1%	18.7%	-14.4%	-0.2%	-4.6%	-4.1%		
% of total OP	11.2%	15.3%	64.3%	141.9%	17.3%	26.6%	22.3%	85.9%	14.5%	24.2%		
OPM	41.9%	41.1%	52.5%	44.5%	44.9%	42.3%	39.2%	40.6%	45.1%	41.2%		
Fund and Consulting	210	220	312	209	160	755	156	203	378	330		
YoY	312.5%	-23.0%	-7.6%	-73.5%	-24.0%	242.8%	-50.1%	-3.1%	136.5%	-56.3%		
% of total OP	5.1%	6.2%	27.2%	45.8%	4.2%	31.3%	5.5%	27.0%	8.7%	13.0%		
OPM	37.3%	42.8%	49.2%	35.4%	34.1%	64.4%	31.8%	32.0%	56.0%	50.7%		
Property Management	28	42	28	43	76	59	78	65	108	96		
YoY	7.3%	-32.5%	107.4%	-3.8%	170.6%	39.0%	179.2%	52.3%	43.0%	63.3%		
% of total OP	0.7%	1.2%	2.4%	9.4%	2.0%	2.4%	2.8%	8.7%	2.5%	3.8%		
OPM	4.4%	5.3%	3.8%	5.6%	9.2%	7.3%	9.5%	7.5%	11.1%	10.0%		
Other	-1	-23	2	4	1	0	-1	-75	6	47		
YoY	nm	nm	-98.4%	-81.6%	nm	nm	nm	nm	nm	nm		
% of total OP	0.0%	-0.6%	0.1%	0.9%	0.0%	0.0%	0.0%	-10.0%	0.1%	1.8%		
OPM	-0.9%	-34.5%	2.4%	6.1%	nm	nm	nm	nm	8.8%	50.1%		
Adjustments	-334	-758	-311	-457	-313	-380	-444	-525	-430	-531		
% of total OP	-8.1%	-21.4%	-27.1%	-100.2%	-8.2%	-15.7%	-15.6%	-69.7%	-9.9%	-20.8%		
Pre-tax profit	3,915	3,326	963	247	3,659	2,199	2,664	528	4,150	2,362		
YoY	78.7%	68.0%	68.3%	-81.0%	-6.5%	-33.9%	176.7%	113.9%	13.4%	7.4%		
Pre-tax margin	28.9%	19.4%	11.4%	2.3%	24.9%	18.8%	17.1%	3.3%	22.7%	16.6%		
Profit attributable to owners of parent	2,611	2,133	635	168	2,501	1,431	1,824	400	2,848	1,605		
YoY	87.8%	68.8%	60.7%	-84.5%	-4.2%	-32.9%	187.2%	137.2%	13.9%	12.1%		
Net margin	19.3%	12.5%	7.5%	1.6%	17.0%	12.3%	11.7%	2.5%	15.6%	11.3%		

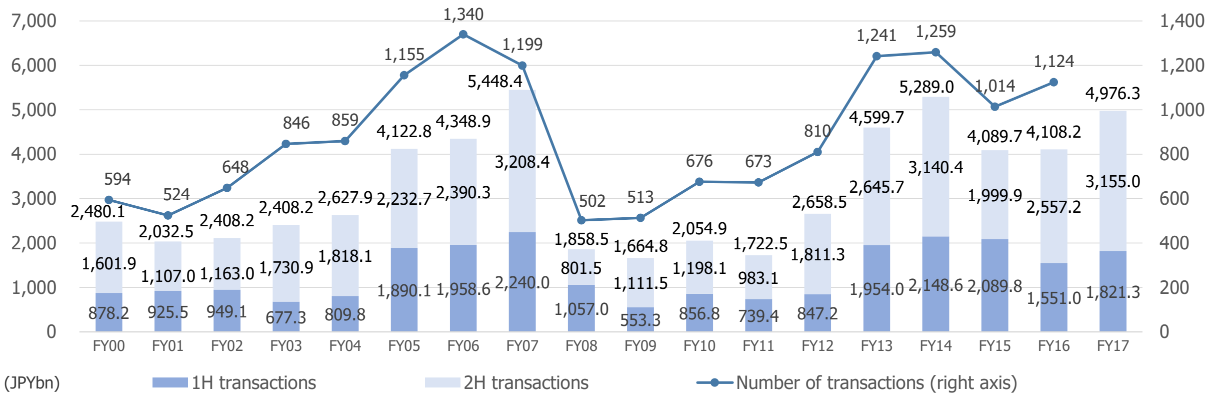
Source: Shared Research based on company data
Note: Figures less than JPY1mn are rounded up (in figures released by the company, amounts less than JPY1mn were discarded)

Real estate business environment

Overview

The real estate industry to which the Tosei group belongs saw active transactions. As a result, commercial property transactions between January and June 2018 reached JPY2.33tn, up 2% YoY (source: JLL). After a sustained decline, unit prices for listed REITs look to have bottomed and fund-raising conditions for listed REITs are improving. Also, high occupancy rates in the rental market are compelling buyers to maintain an active purchasing stance.

Real estate transactions by listed companies (JPYbn, number of transactions)

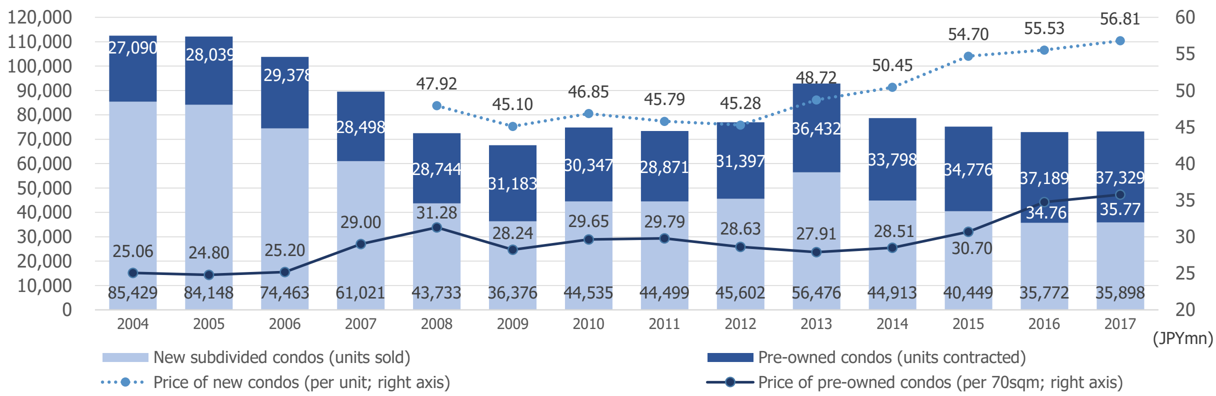


Source: Shared Research based on Urban Research Institute Corporation data

Condominiums in Greater Tokyo

In FY2017 (April 2017-March 2018), the condominium market in Greater Tokyo saw sales of 36,837 units, up 1.1% YoY for the first upswing in four years (note: in CY2017, sales were up 0.4% YoY to 35,898 units; see the graph below). Due to construction cost hikes, the average unit price of condominiums remained at a high JPY56.8mn (in CY2017, the average unit price was up 2.3% YoY to JPY56.8mn). The average initial month contract ratio was 68.8%, falling below the 70% borderline between strong sales and weak sales for the second consecutive year. The average initial month contract ratio between January and June 2018 fell 0.6pp YoY to 66.7%, still falling below 70%.

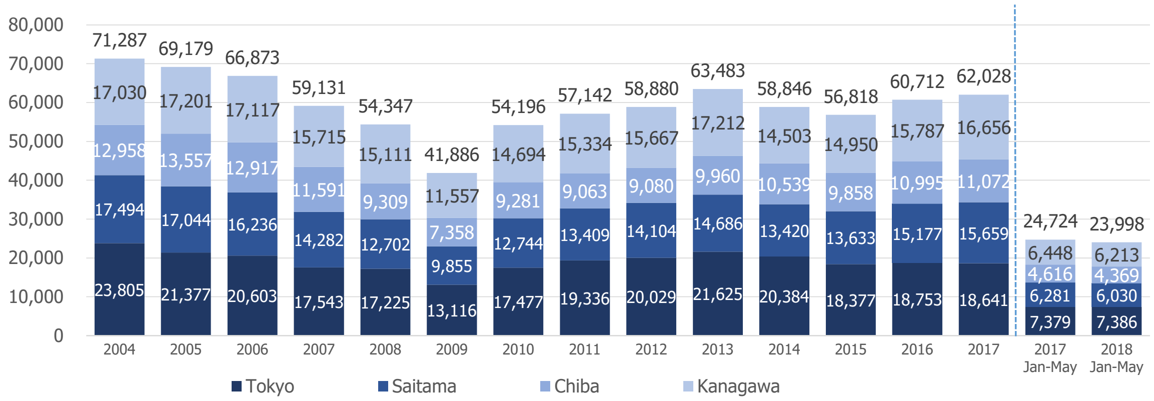
Sales and contracts of new and used condominiums in Greater Tokyo



Source: Shared Research based on data from Real Estate Economic Institute, Tokyo Kantei, and Real Estate Information Network for East Japan
Note: The price of a new condominium (annual average) is calculated as a simple average of monthly data

Meanwhile, looking at the detached house market in Greater Tokyo for FY2017, housing starts were roughly level YoY at 61,215 units (in CY2017, housing starts increased 2.2% YoY to 62,028). Housing starts between January and May 2018 were 23,998 units, down 2.9% YoY but still high. Consumers often perceive detached houses to be more reasonably priced compared with new condominiums and therefore their demand remains high. Mortgage loans offering low interest rates are also driving the demand.

Housing starts for detached houses in Greater Tokyo



Source: Shared Research based on data from Ministry of Land, Infrastructure, Transport and Tourism

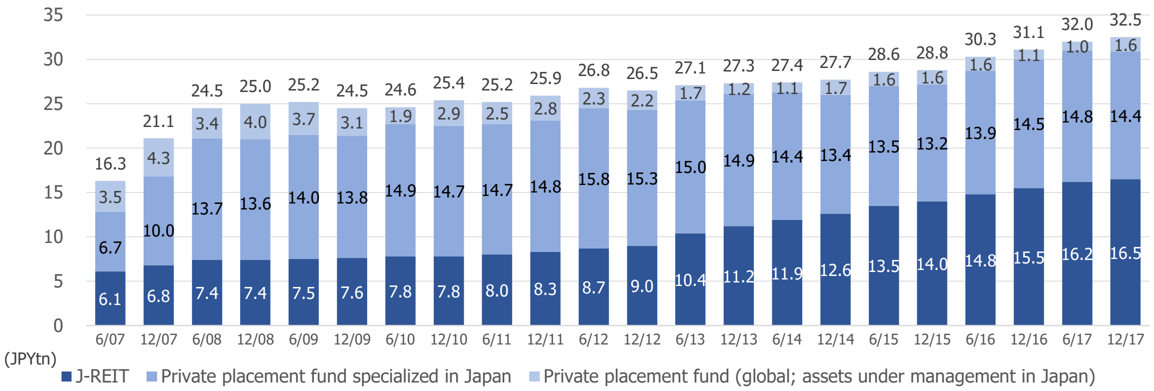
Rental market

In the rental market, office buildings have seen brisk demand as strong business performances among companies generated needs for office expansion and relocation. In June 2018, the average vacancy rate in Tokyo's five wards (prime business districts) was 2.57% (-0.11% YoY) and the average rent was JPY6,093/sqm (+0.44%). The average rent thus has been rising for 54 straight months. While some have expressed concern about a glut of large office buildings in central Tokyo, rents continue to rise as brisk earnings encourage companies to hire more staff, requiring office expansion and relocation.

Real estate securitization market

The size of the real estate fund market as of end-December 2017 was JPY32.5tn (+JPY1.4tn YoY), which breaks down to JPY16.5tn in AUM held by J-REITs (+JPY1.0tn) and JPY16.0tn in AUM held by major private placement funds (+JPY0.4tn) (Source: *Survey on Private Placement Funds* by Sumitomo Mitsui Trust Research Institute).

Real estate fund market



Source: Shared Research based on Sumitomo Mitsui Trust Research Institute data

FY11/18 earnings forecasts

Full-year FY11/18 forecasts released at the beginning of the fiscal period remain unchanged.

- Revenues: JPY67.8bn (+17.4% YoY)
- Operating profit: JPY10.9bn (+11.3%)
- Profit before tax: JPY10.0bn (+10.9%)
- Net income: JPY6.7bn (+8.8%)

*Net income is net income attributable to parent company shareholders.

As in most years, for the Revitalization segment in 2H FY11/18, the company has factored in about JPY10.0bn in properties supplied to Tosei Reit Investment Corporation (bridge transaction for the REIT) based on a sponsorship agreement. Tosei's understanding of the business climate is as follows. First, real estate prices continue to increase at a modest pace, although some observers believe the property investment market is getting overheated. Second, Tosei thinks that neither a significant increase in real estate prices nor a significant decline in cap rates is likely to occur. The company expects demand from investors to remain upbeat, underpinned by the Bank of Japan's monetary easing policy. Against this backdrop, Tosei's plan is to focus on the acquisition, revitalization, and sale of investment properties for funds and corporations, an area of strong demand. Heading into FY11/19, Tosei will also promote the development and sale of condominiums for end-users.

In the Revitalization segment, the company will focus on sales of small size properties for less than JPY1bn. In 2H, it plans to sell 29 small-sized properties and six mid- to large-sized properties (in 1H, it sold 22 small-sized properties and two mid- to large-sized properties). In the Development segment, Tosei will focus on sales of detached houses and the development and sale of whole buildings for FY11/19. It also plans to promote preselling of The Palms Chofu Manor Garden (162 units in total; delivery scheduled to start in December 2018). In 2H, the company aims to deliver 93 detached houses (45 in 1H) and four condominium units (85), as well as two commercial facilities (none in 1H).

In terms of acquisition strategy, Tosei intends to continue investing selectively by mainly targeting mid-to-small size properties in the Greater Tokyo Area. The company aims to discover undervalued properties with refurbishment potential by leveraging its existing strength in planning revitalization. In the suburbs, Tosei will invest only in properties with high liquidity and profitability expectations. In adding logistics to the product lineup, the company will consider acquisitions for a wide variety of uses and exit strategies. It plans to implement efficient acquisitions using a range of methods such as M&A, and to that end has established the M&A/Group Strategy Department.

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