Nippon Accommodations Fund Inc.

37th Period (March 2024 – August 2024) Investor Presentation

Q&A

Q The percentage increase in rents at the time of tenant turnover for the portfolio as a whole improved slightly compared with the previous period. Could you explain why the increase was a little lower than the improvements of close to 10% announced by other companies in the sector at their results announcements last month?

A Thanks to our prudent approach toward leasing management, we were able to minimize the decline in rents during the COVID-19 pandemic. Turnover during the 37th period included numerous tenants that executed contracts from 2021 and over 2022. Moreover, rents at the time of tenant turnover for a number of properties were already at a competitive level and not especially low. Amid the favorable market, increases in rent as a result were generally not as high as those of other companies. Another reason for the relatively subdued improvement was the fact that the period in question exhibited strong supply of new residential housing, particularly for the Harumi Flag series property in the Tokyo Bay area, where the impact on the percentage increase in rents was substantial. Against this backdrop, NAF took a cautious approach toward the properties it owns in the surrounding area, prioritizing occupancy rates over substantial increases in rent. While Harumi Flag condominium rentals had a strong impact on the percentage change at which rents increased, that impact appears to have run its course, allowing us from this point forward to focus again on increasing rents.

Q What is your outlook for regional property rents by area? In addition, could you comment on the outlook for rents in the family and large type unit categories?

A The overall economy may be following a recovery track, but the balance between supply and demand is not as tight in the regional cities as it is in the greater Tokyo area. Accordingly, significant rent increases have yet to manifest in those outlying cities. Despite the robust rate of change in rents in Fukuoka and the Kansai region, volume in those areas is not particularly large. On the other hand, the percentage change in rents in the Nagoya area, where volume is relatively large, continues to languish, which significantly impacts the strength of regional property rents on an overall basis. The percentage change in rents for family and large units has recently been hovering around the 10% level, and while not hitting a peak, we believe rents for these units are likely to continue increasing at about this rate moving forward. With market volume in these categories relatively limited, we expect supply and demand to continue to tighten.

Q Has there been any change in opportunities to acquire properties from your sponsor?

A We remain in ongoing discussions with our sponsor. Based on current conditions in our sponsor's residential properties business, there appears to be little incentive for it to sell its rental housing properties. That being said, we recognize its commitment to supporting NAF, including through the acquisition of NAF investment units through a third party in the current period. We expect to be able to acquire properties when the right opportunity presents itself.

Q In terms of rent changes at the time of tenant turnover, could you outline your progress in replacing tenants who moved in during the COVID-19 pandemic?

A Tenants who signed contracts in 2021–2022 accounted for 26% of all tenants as of the close of the 37th period. We expect these tenants to be slowly but gradually replaced as we move forward.

Q You mentioned the impact of Harumi Flag properties on rents at the time of tenant turnover, but was the Chuo Ward property impact also large? Could you compare the change in rent at the time of tenant turnover in the 37th period to that in the 36th period?

A Rent change at the time of tenant turnover for Chuo Ward properties was 10.5% in the 36th period and 9.0% in the 37th period. The same trend seen in Chuo Ward was seen in surrounding areas such as Shibaura and Toyosu, which had an impact on the overall rent change at the time of tenant turnover.

Q The rate of rent change at the time of renewal appears to be slowing. Does this represent a change in the general trend? Can you provide any additional information in this respect?

A In a tight supply and demand environment, while the ratio of units in which rent increases when the contract is renewed may not rise substantially, we believe it can be maintained at about 10%. When market prices are rising, it is only natural for us to target rent increases when contracts are renewed, and our goal in general is to ensure the maximum possible increase in rents while keeping a close eye of the balance between supply and demand. We remain acutely aware of the need to bolster EPU and DPU and even without a significant improvement in rent changes at the time of tenant turnover or renewal want to ensure that management is focused on achieving EPU and DPU growth while maintaining a firm eye on the overall supply and demand balance.

Q Operating income, which came in at ¥5,991 million in the period ended August 31, 2024 is expected to drop marginally to ¥5,972 million in the period ending August 31, 2025. With rents on an overall basis rising, operating income should improve as costs are managed. Could you comment on earnings prior to interest payments moving forward?

A In line with our cautious outlook on costs associated with the turnover of tenants, we expect earnings to decline in the period ending August 31, 2025. We are aware of the need to adhere to the EPU and

DPU targets previously announced, and while it may be difficult to see the potential for growth in those figures, our goal is, as in the past, to steadily improve top-line earnings, as well as EPU and DPU.

Q I would like to ask if you will be more proactive in the recycling of assets. Returning increasing unrealized gains to unitholders and improving asset quality through such measures as the disposition of the Nagoya property you mentioned earlier and replacing it with another property in a different area or of a different type, seem like good ideas. Please provide us with your specific thoughts on the replacement of assets.

A We believe it would be easier to work on the disposition of assets on the expectation of external growth. Of course, while disposing of a property could be beneficial in terms of returning profit to investors in the near term, the subsequent decline in NOI would be difficult to offset through increased earnings at the remaining properties. While there are significant unrealized gains in our portfolio, it also generates strong yields and steady cash flow. Since we would have to make up for the loss of income on any disposition, we do not believe it wise to change course at this time. Despite the sluggish change in rents at Nagoya properties, we are still able to ensure solid investment yields, and at this point we see no comparable properties in this respect. With a management approach in line with the points you have raised, we are always thinking of ways to improve the quality of our portfolio and are continually exploring property acquisition opportunities, either through replacement or two-way transactions.

Q Do you have plans with the sponsor to redevelop any of the older properties you own?

A While the general image may be to dispose of a property back to the sponsor, redevelop it, and then acquire it again, given the current environment of rising construction costs, it would be rather difficult for NAF to reacquire a property at a solid yield after the sponsor purchases, demolishes, and redevelops it. Acquiring properties at the current cap rate of around 3% would lower our portfolio yield, and while not the golden rule, we are also cognizant of the implied cap rate and understand that at this point it is difficult to find properties that meet both investment decision criteria. We will sometimes discuss the possibility of such a deal in our regular discussions with our sponsor, but for now there have been no projects meeting these requirements.

Q Acquiring new properties appears important to DPU and EPU growth, though given difficulties in acquiring properties through your sponsor, are you looking to acquire properties through third parties, and if so, can you discuss progress in any related discussions?

A The three Smile Hotel properties acquired in the 36th period and the Kuretake Inn Asahikawa property acquired in the 38th period were acquired through our own development routes. We continue to actively seek out acquisition opportunities from external parties. Many of the properties brought in are rather small in scale and many have low required cap rates. That said, there will sometimes be properties worth considering, and in cases where we will not want to miss the chance to acquire them, we will make use of a variety of methods, including not only simple bids, but also two-way transactions to acquire the properties from external sources.

Q Until now, the rate of the increase in rent when a contract is renewed has been roughly the same as at other companies in the sector, but there now appears a slight divergence. How do you think this divergence will change moving forward? Will it narrow, remain the same, or widen?

A It is difficult to give you an accurate answer because this involves a comparison with the portfolios of other companies. On the other hand, a comparison of the change in rents at the time of tenant turnover over the past five to six years shows that the figures are roughly the same for each of the companies, and even if there is a temporary divergence in those rates, they may return to about the same level. Since the rate of change reflects the difference between the rent before and after the turnover, if the rent was high to begin with, a further increase would prove difficult, with temporary ups and downs accordingly likely to even out over time. The market rent outlook, based on the Apartment Rent Index published by At Home, is for a 3.4% year-on-year increase. That appears about the pace of fundamental growth.

REIT Management Company: Mitsui Fudosan Accommodations Fund Management Co., Ltd.
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