Frontier Real Estate Investment Corporation

Supplementary Materials on Press Releases as of March 18, 2019

March 18, 2019
Mitsui Fudosan Frontier REIT Management Inc.







Summary

Frontier Real Estate Investment Corporation

Key points

Property replacement comprising the sale of risk assets and acquisition of high-quality assets leveraging the sponsor's pipeline

Sale

Mitsui Shopping Park ALPARK (East Building)

FRI to sell the property to avoid the risk in the future in the present brisk real estate market, even if doing so would result in a loss on sale(Approximately ¥900 million)

Acquisitions

Ikebukuro GLOBE, SAKAE GLOBE, and Shinsaibashi MG Building

Leveraging the sponsor's pipeline to obtain relatively new, high-quality properties in high-end shopping districts in Japan's three largest metropolitan areas

Sale of risk assets

Mitsui Shopping Park ALPARK (East Building)



Planned Sale date: May 31, 2019
Planned Sale price: ¥3,800 million
Completed Apr. 10, 1990

Acquisition of high-quality assets via the sponsor's pipeline (total: ¥22,490 million)

Ikebukuro GLOBE (50% co-ownership)



Planned Acquisition date: Mar. 22, 2019
Planned Acquisition price: ¥10,300 million
Completed Jan. 10, 2014

SAKAE GLOBE (40% quasi co-ownership)



Planned Acquisition date: Mar. 22, 2019
Planned Acquisition price: ¥6,350 million
Completed July 12, 2017

Shinsaibashi MG Building (60% co-ownership)



Planned Acquisition date: Mar. 22, 2019
Planned Acquisition price: ¥5,840 million
Completed Oct. 4, 2018

Effects of these initiatives

Boost to property leasing operating income[1]

ALPARK (East Building): -¥111mn/period
Three newly acquired properties: +¥371mn/period
↓
+¥259 mn/period

Average building age[2] down

(As of Dec. 31, 2018)
12.3 years
↓
(After sale & acquisitions)
11.2 years

Asset size expanded (acquisition price basis)

At Dec. 31, 2018: 35 properties/¥304.7 bn
After sale & acquisitions: 36 properties/¥321.8 bn
↓
+¥17.0 billion

1. Calculated based on 29th fiscal period property leasing income for ALPARK (East Building) and on property leasing operating income for the three properties to be acquired.
2. Calculated based on acquisition prices, excluding land interest properties. The figure of after sale & acquisitions is calculated based on the properties after sale & acquisitions.

Details of the asset to be sold

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1. Mitsui Shopping Park ALPARK (East Building)

Location	2-26-1 Kusatsushinmachi, Nishi Ward, Hiroshima City, Hiroshima
Lot area	Site of building: 16,682.75 m² Investment Corporation's ownership: 15,033.90 m²
Floor area	Building total: 64,720.87 m² Exclusive use portion: 60,383.72 m²
Acquisition date	February 19, 2013
Acquisition price	¥5,400 million
Contract date / Planned Delivery date	March 18, 2019 / May 31, 2019
Planned Sale price[1]	¥3,800 million
Book value	¥4,670 million (projected value at delivery)
Loss on sale[2]	Approximately ¥900 million

1. The amount noted here excludes real property taxes, consumption taxes, etc.

2. The above value is approximate, as certain sale costs had yet to be determined at the time of this publication.

■ Lease contract

Lessee	Mitsui Fudosan Co., Ltd.
Lease type	Master lease (ML) contract
Contract period	20 years (Feb. 2013–Feb. 2033)
Rent revision	Not permitted for 10 years
Termination during the contract term	Not permitted for 5 years

■ Overview of Appraisal value

As for the appraisal value as of January 31, 2019, the drop of the appraisal value(¥2billion) is due to the revision of the cap rate and other figures in the property appraisal summarized below as a result of the new consideration of a risk of decline in profitability due to the cancellation of the property's master lease agreement.

(unit: ¥million)	Appraisal value	Direct-reduction method value	Operating income	Net income	Cap rate	DCF value	Discount rate	Terminal cap rate
As of December 31, 2018	**5,470**	**5,490**	529	362	6.6%	**5,440**	6.4%	6.9%
As of January 31, 2019	**3,470**	**3,480**	529	362	10.4%	**3,460**	10.3%	10.8%

2. Factors leading to sale

Since FRI acquired the property, it has operated as one of Hiroshima City's key retail facilities. However, FRI determined that selling it in the current, brisk real estate market would be preferable to continuing to hold it, as its future cash flows are likely to fall, given the following:

① The risk of cancellation of the property's master lease agreement due to the decline in sales as a result of the development of new competing facilities

② Increasing repair and CAPEX costs associated with maintaining the competitiveness of the aging facility

■ Consideration process

Option 1. Continue to hold

- Risk of cancellation of ML contract due to continued decline in sales
- Increasing repair and CAPEX costs to maintain competitiveness
- Likely to significantly negatively impact net leasing income

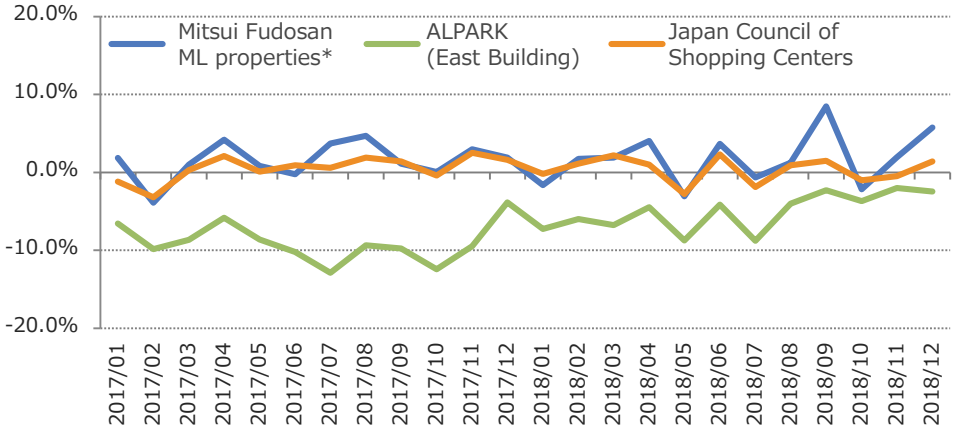
Future risk >

Option 2. Sale

- Brisk real estate sales market
- Eliminate future risk by selling early

FRI decided that **selling is the best option** at present

■ Year-on-year comparison of monthly sales



* Properties for which FRI has formed a master lease contract with Mitsui Fudosan (excluding ALPARK (East Building))

Environment surrounding asset to be sold

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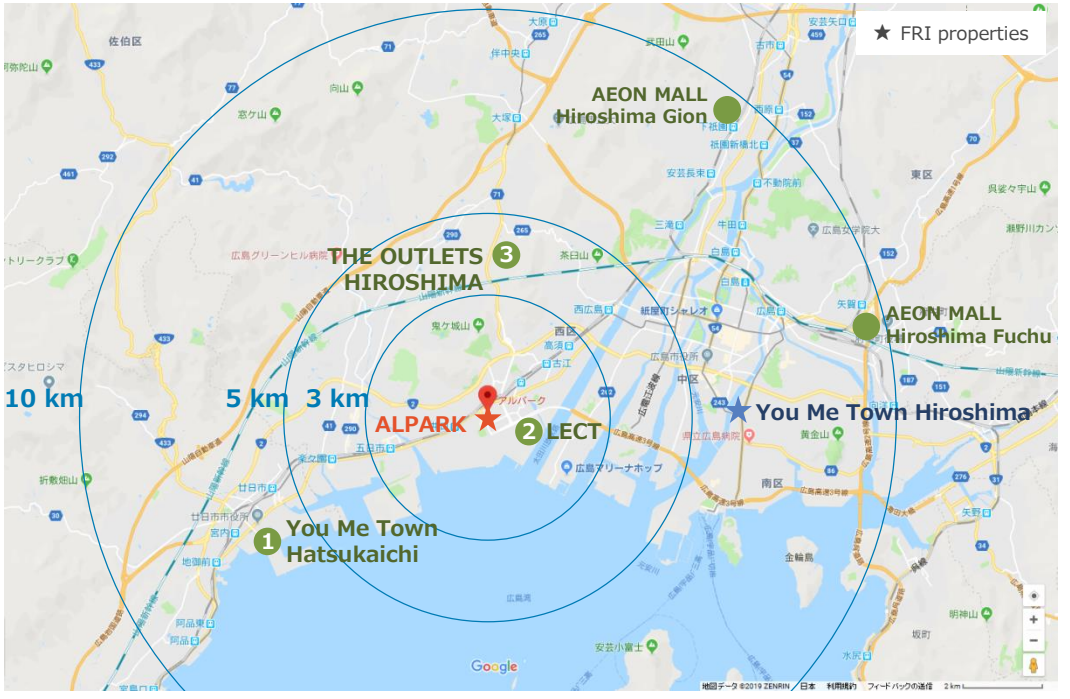
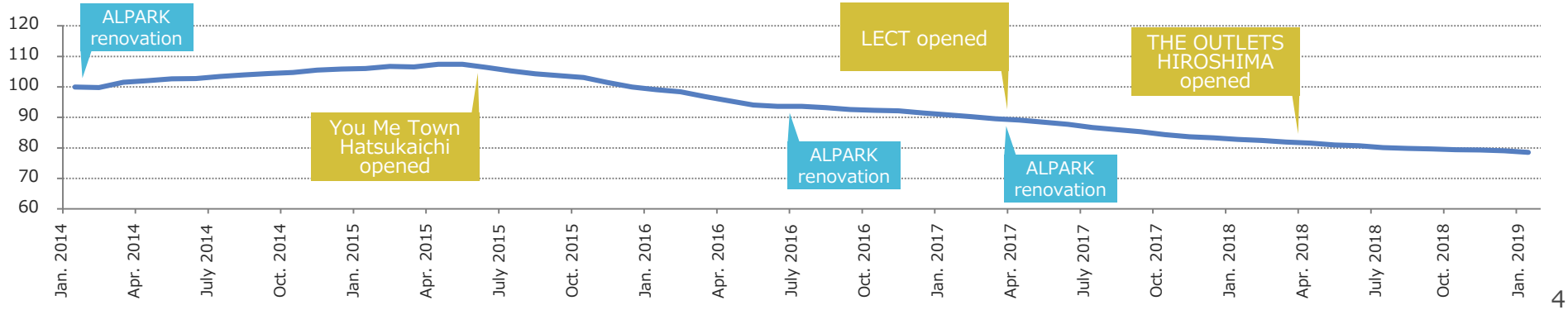
A major increase in retail floor due to the opening of several competing facilities has resulted in ALPARK (East Building)'s sales falling 27% from their peak

Competitive environment



	Opened	Store floor area	Operator
(East Building)	April 1990	20,662 m²	Mitsui Fudosan
Hatsukaichi	June 2015	46,000 m²	Izumi
	April 2017	38,980 m²	Izumi
③ THE OUTLETS HIROSHIMA	April 2018	43,500 m²	AEON Mall

■ALPARK (East Building) sales (12-month average, with January 2014 as 100)



Assets to be acquired

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Acquisitions that leverage the sponsor's pipeline to obtain high-quality, relatively new assets in Japan's three largest metropolitan areas(Tokyo, Nagoya, Osaka)

Ikebukuro GLOBE (50% co-ownership)



- Located on Sunshine 60 Street in the Ikebukuro area, one of Japan's top concentrated retail areas
- New building, completed in January 2014
- Opened as a large-scale store inspired by UNIQLO's popular flagship locations

Planned Acquisition date	March 22, 2019
Planned Acquisition price	¥10,300 million
Appraisal value	¥10,500 million
NOI yield*/NOI yield after depreciation	4.0% / 3.3%

SAKAE GLOBE (40% quasi co-ownership)



- Located on a corner lot on Otsu Avenue—Nagoya's leading street of high-end brand retailers—in the Sakae area
- Entire building leased by a globally popular fashion brand
- With this acquisition, FRI will have a 100% stake

Planned Acquisition date	March 22, 2019
Planned Acquisition price	¥6,350 million
Appraisal value	¥6,360 million
NOI yield*/NOI yield after depreciation	3.6% / 3.4%

Shinsaibashi MG Building (60% co-ownership)



- Located on the Shinsaibashi-suji shopping street, where a wide variety of stores are concentrated
- Further expansion of nearby retail facilities is expected, including the rebuilding of the Daimaru Shinsaibashi main building to open in autumn 2019
- Location expected to benefit from demand from foreign tourists

Planned Acquisition date	March 22, 2019
Planned Acquisition price	¥5,840 million
Appraisal value	¥5,920 million
NOI yield*/NOI yield after depreciation	3.4% / 3.2%

* Expected NOI divided by acquisition price

Distributions per unit

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Forecast for 30th fiscal period (ending June 2019) distribution per unit unchanged at ¥10,490

Measures to Control Distributions

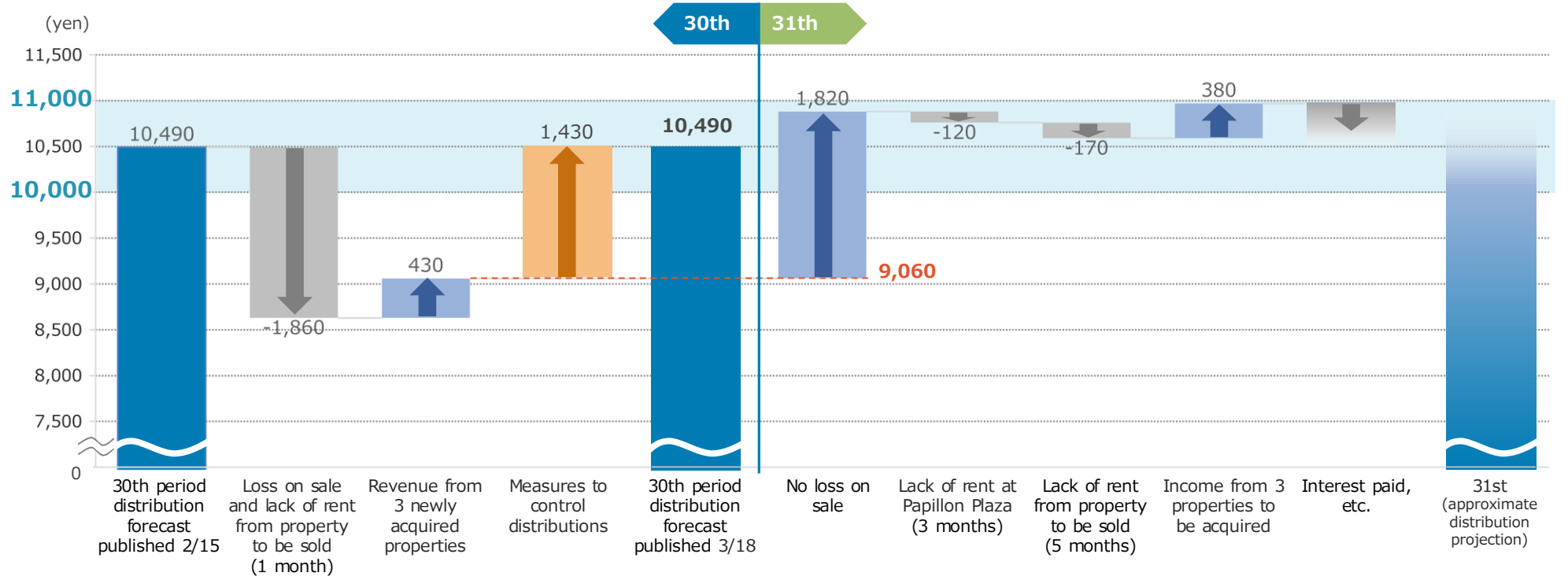
FRI plans to keep the distribution per unit at the level forecast by using the effects of asset acquisitions and sales, drawing from internal reserves (approximately ¥180 million), paying distributions in excess of earnings, and other means

→ The impact on the previously published "Forecast of Results for the 30th Fiscal Period" is expected to be modest, and FRI has not revised these forecasts

Objective of paying distributions in excess of earnings

To stabilize distributions against the sudden realization of operational risks

Factors affecting distributions per unit



* The above graph was prepared by the Asset Management Company to communicate the impact of the initiatives in question on the forecasts of the Investment Corporation's per-unit distributions for the 30th and 31st fiscal periods in an easy-to understand manner. The graph provides an overview of the main factors expected to impact per-unit distributions as a result of these initiatives and estimates of their respective amounts made at the date of this publication. However, these factors and estimates have been prepared based on certain assumptions and simplified for ease of understanding, and they are not necessarily accurate representations of the actual factors and amounts that will arise. The Investment Corporation makes no guarantee or promise with regard to the amounts of distributions per unit, factors impacting distributions per unit, their respective amounts, or other information in the above graph.

Indicators

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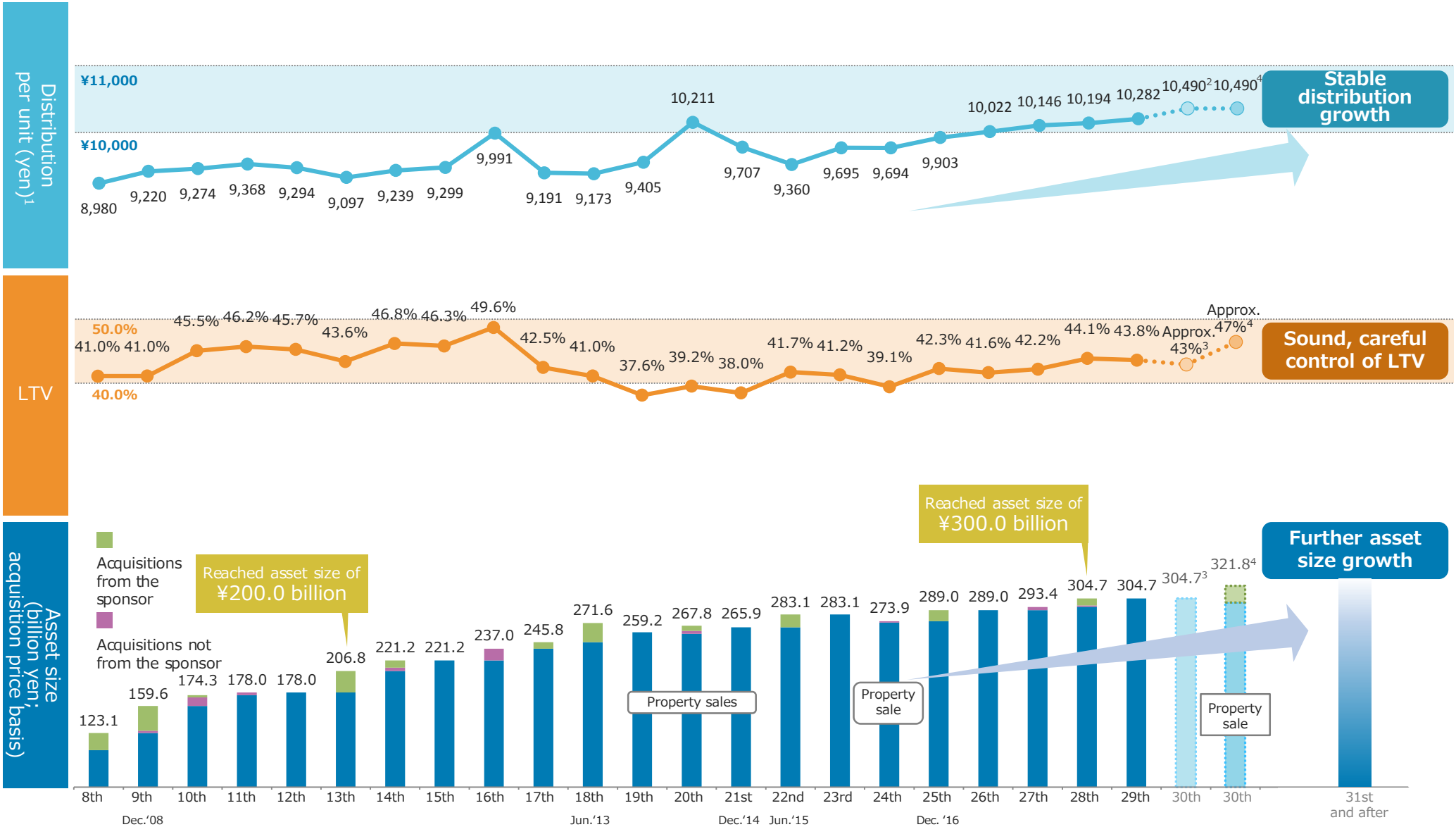

1. FRI implemented a two-for-one split of its investment units effective January 1, 2014. Distributions before the split have been divided by two and truncated to the nearest yen.
2. Forecast figures as presented in "Summary of Financial Results for the 29th Fiscal Period."
3. Forecast figures as presented under "Pre-Conditions and Assumptions for Operating Forecasts for the 30th Fiscal Period (January 1, 2019 to June 30, 2019)" in "Summary of Financial Results for the 29th Fiscal Period."
4. Forecast figures as of March 18, 2019.

FRI's portfolio in graphs

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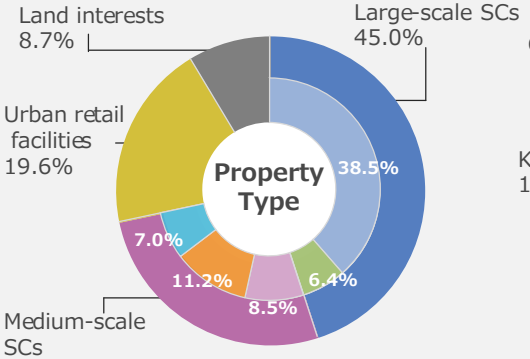
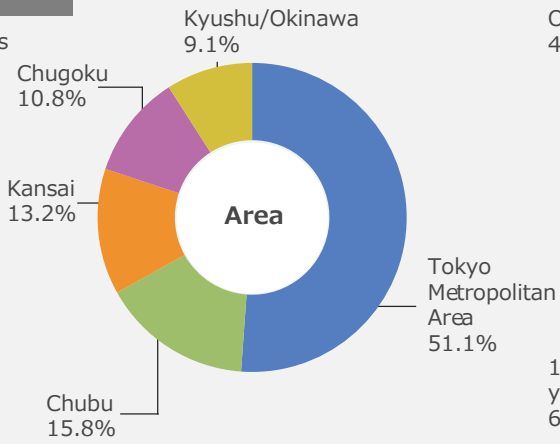
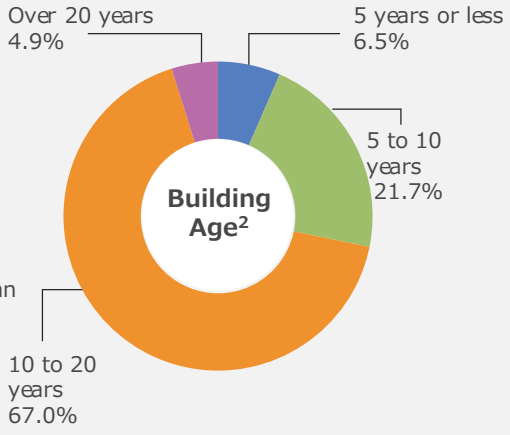
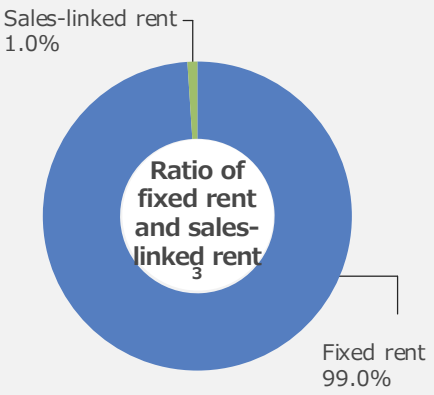
As of December 31, 2018



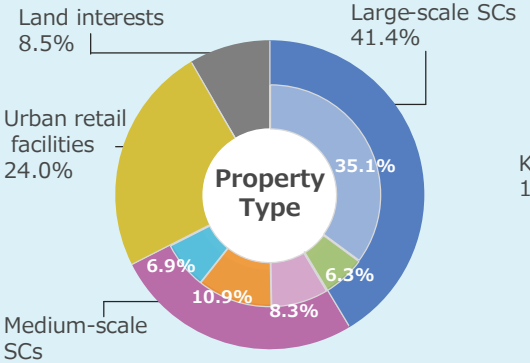


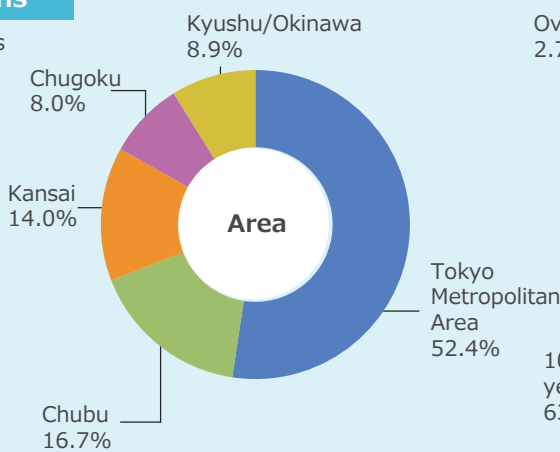


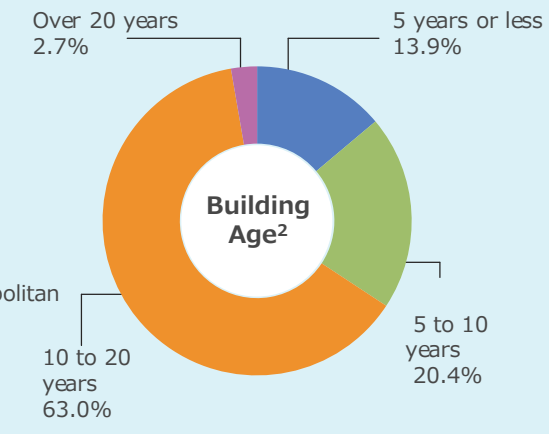
Average building age:
12.3 years



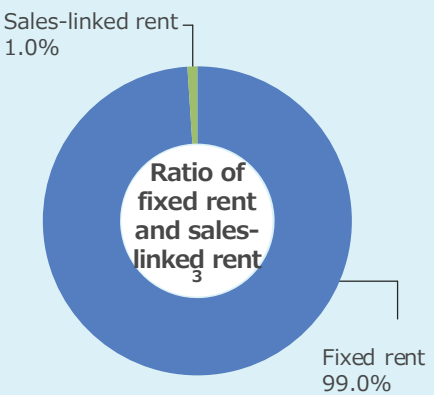
After property sale and acquisitions







Average building age:
11.2 years



1. All figures for the portfolio as of December 31, 2018 are calculated based on the annualized fixed rent (excluding common area maintenance charges) of lease contracts valid as of December 31, 2018. Variable rent is not taken into account. Figures for after the property sale acquisitions are calculated based on the annualized fixed rent (excluding common area maintenance charges) of lease contracts valid as of December 31, 2018, excluding the property to be sold, and of lease contracts for the properties to be newly acquired.
2. Based on acquisition price, excluding properties operated as land interests.
3. The ratio of fixed rent and sales-linked rent for the portfolio as of December 31, 2018 is that of the 29th fiscal period. The ratio for after the property acquisitions and sale is based on results for the 29th fiscal period and the fixed rent (excluding common area maintenance charges) of lease contracts valid as of December 31, 2018, excluding the property to be sold, and of lease contracts for the properties to be newly acquired.

Working toward future growth

Frontier Real Estate Investment Corporation

FRI's operational strategy

Internal Growth

- Secure a foundation for stable earnings based on long-term fixed rent
- Adjust to changes in the environments surrounding properties, maintaining and enhancing competitiveness through such measures as additional investment and tenant replacement
- Consider replacing properties that pose future uncertainties in order to further enhance portfolio quality

Asset disposition



ALPARK(East Building)

Maintaining and enhancing facility competitiveness through management



LaLaport SHIN-MISATO



AEON MALL Ibaraki



QANAT Rakuhoku



External Growth

- Fully utilize the sponsor's pipeline to continue acquiring excellent properties
- Selectively invest in non-sponsor properties utilizing the Asset Management Company's unique network, keeping a close eye on risk
- Carefully select properties for investment, considering the certainty of cash flows and growth potential of the surrounding retail zone
- Make acquisitions with an eye to maintaining the whole portfolio's ratio of asset value to yield after depreciation

Asset acquisitions



Ikebukuro GLOBE



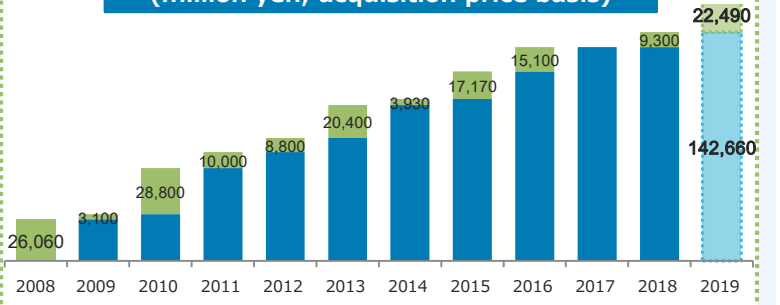
SAKAE GLOBE



Shinsaibashi MG Building

Average annual acquisitions from Mitsui Fudosan, the sponsor: ¥ 14,360 million

Cumulative assets acquired from Mitsui Fudosan, etc.* (million yen; acquisition price basis)



* The graph above shows the cumulative assets acquired from Mitsui Fudosan, etc. of the properties after the property acquisitions and sale.

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Frontier Real Estate Investment Corporation

Asset Management Company

Mitsui Fudosan Frontier REIT Management Inc.