

### Ongoing property sales by REITs

## Property sales constitute viable option even if pros and cons are not immediately apparent

#### **Sekisui House SI Residential Investment sells property carrying unrealized losses at a profit**

On 31 August Sekisui House SI Residential Investment [8973] (Buy) announced the sale of b-town Minamiaoyama, an urban retail facility. It has been selling off commercial facilities since June 2014 in order to turn itself into a specialist residential REIT, and to date had sold six properties. It had hitherto decided not to sell b-town Minamiaoyama because it was carrying unrealized losses, with appraisal value of ¥1.17bn at end-16/3 versus book value of ¥1.49bn. However, it has now managed to sell it to a third party based in Japan that made an offer of ¥1.56bn, well above the property's appraisal value and also higher than its book value. Sekisui House SI Residential Investment said that it received an offer for the property in excess of its book value because the real estate market has been buoyant recently.

#### **Fukuoka REIT sells property at a loss in order to avoid future management risks**

The real estate market may have been buoyant recently, but some properties are still being sold at a loss. Fukuoka REIT [8968] decided to sell the Aeon Hara Shopping Center in Fukuoka on 30 August. The selling price of ¥3.7bn is lower than the appraisal value of ¥4.0bn and the book value of ¥5.2bn. Having considered various options for the property, including eliminating unrealized losses or refurbishment at additional cost, Fukuoka REIT has decided to sell it while real estate market conditions are favorable in order to avoid future risk now that the fixed-term tenancy with Aeon Kyushu [2653] has less than three years to run. It also decided to sell Aqualia Kego, a rental housing development in Fukuoka, on the same day. The selling price of ¥4.3bn is higher than both the appraisal value of ¥3.6bn and the book value of ¥2.6bn.

These two sales will broadly net each other out, and Fukuoka REIT has also decided to acquire a sports center in Oita. However, it has lowered its 16/8 DPU projection from ¥3,560 to ¥3,430 and its 17/12 DPU projection from ¥3,560 to ¥3,300 to reflect the impact of the earthquakes in Kumamoto on properties such as the Kumamoto Intercommunity Shopping Center, and changes to the outlook for sales-linked rent at Canal City Hakata owing to changes in business conditions related to inbound spending (changes in spending behavior, a rise in the number of rival tax-free retail facilities). It is looking to minimize near-term DPU downside and ward off perceived future risks at the Aeon Hara Shopping Center.

#### **Pro and cons of property sales are not immediately apparent, but now appears to be a good time to sell**

We think now is a good time for REITs to sell properties with latent risks, while the real estate market is buoyant. Although the pros and cons of property sales will not be immediately apparent, especially if they entail the posting of losses or result in lower rental income, it will nevertheless be interesting to see what REITs decide.

### Global Markets Research

31 August 2016

### Research analysts

#### Japan REIT

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# Appendix A-1

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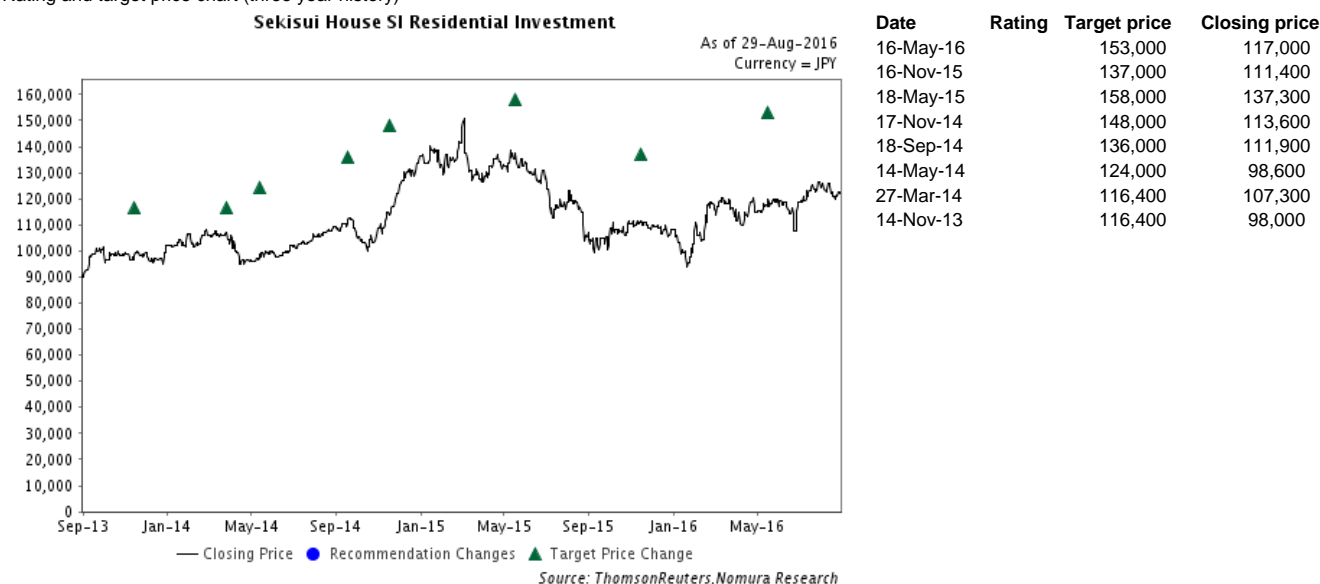
Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Sekisui House SI Residential Investment	8973 JP	JPY 119,600	31-8-2016	Buy	N/A	A6,A11

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### Sekisui House SI Residential Investment (8973 JP) JPY 119,600 (31-8-2016) Buy (Sector rating: N/A)

Rating and target price chart (three year history)



For explanation of ratings refer to the stock rating keys located after chart(s)

**Valuation Methodology** For REITs, our target price is the simple average of two theoretical prices derived from the fair-value dividend yield and the fair-value cap rate (in this case, ¥143,000 and ¥163,000, respectively). Our target price for this REIT is ¥153,000, based on a fair-value dividend yield of 3.0%, a fair-value cap rate of 3.75%, and earnings forecasts for 16/9 and 17/3. The discount rates we use are around 25bp lower than the weighted-average dividend yield of 3.35% and weighted-average implied cap rate of 4.07% (as of 16 May) for the 37 REITs under our coverage.

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Purchases of investment trusts (and sales of some investment trusts) are subject to a purchase or sales fee of up to 5.4% of the transaction amount. Also, a direct cost that may be incurred when selling investment trusts is a fee of up to 2.0% of the unit price at the time of redemption. Indirect costs that may be incurred during the course of holding investment trusts include, for domestic investment trusts, an asset management fee (trust fee) of up to 5.4% (annualized basis) of the net assets in trust, as well as fees based on investment performance. Other indirect costs may also be incurred. For foreign investment trusts, indirect fees may be incurred during the course of holding such as investment company compensation.

Investment trusts invest mainly in securities such as Japanese and foreign equities and bonds, whose prices fluctuate. Investment trust unit prices fluctuate owing to price fluctuations in the underlying assets and to foreign exchange rate fluctuations. As such, investment trusts carry the risk of losses. Fees and risks vary by investment trust. Maximum applicable fees are subject to change; please thoroughly read the written materials provided, such as prospectuses or documents delivered before making a contract.

In interest rate swap transactions and USD/JPY basis swap transactions ("interest rate swap transactions, etc."), only the agreed transaction payments shall be made on the settlement dates. Some interest rate swap transactions, etc. may require pledging of margin collateral. In some of these cases, transaction payments may exceed the amount of collateral. There shall be no advance notification of required collateral value or collateral ratios as they vary depending on the transaction. Interest rate swap transactions, etc. carry the risk of losses owing to fluctuations in market prices in the interest rate, currency and other markets, as well as reference indices. Losses incurred as such may exceed the value of margin collateral, in which case margin calls may be triggered. In the event that both parties agree to enter a replacement (or termination) transaction, the interest rates received (paid) under the new arrangement may differ from those in the original arrangement, even if terms other than the interest rates are identical to those in the original transaction. Risks vary by transaction. Please thoroughly read the written materials provided, such as documents delivered before making a contract and disclosure statements.

In OTC transactions of credit default swaps (CDS), no sales commission will be charged. When entering into CDS transactions, the protection buyer will be required to pledge or entrust an agreed amount of margin collateral. In some of these cases, the transaction payments may exceed the amount of margin collateral. There shall be no advance notification of required collateral value or collateral ratios as they vary depending on the financial position of the protection buyer. CDS transactions carry the risk of losses owing to changes in the credit position of some or all of the referenced entities, and/or fluctuations of the interest rate market. The amount the protection buyer receives in the event that the CDS is triggered by a credit event may undercut the total amount of premiums that he/she has paid in the course of the transaction. Similarly, the amount the protection seller pays in the event of a credit event may exceed the total amount of premiums that he/she has received in the transaction. All other conditions being equal, the amount of premiums that the protection buyer pays and that received by the protection seller shall differ. In principle, CDS transactions will be limited to financial instruments business operators and qualified institutional investors.

No account fee will be charged for marketable securities or monies deposited. Transfers of equities to another securities company via the Japan Securities Depository Center are subject to a transfer fee of up to ¥10,800 per issue transferred depending on volume.

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