



Jiro Yasu and Patrick Rial

Varecs Partners



Follow Up and New Idea

April 2018

Overview of VARECS Partners Limited

- **A Tokyo-based Independent Registered Investment Adviser**
- **Established May 2006**
- **Our Strategy**
 - ✓ Investing in undervalued Japanese equities
 - ✓ Typical Profile: family control, high margin, modest growth, stable revenue stream, etc.
 - ✓ Focus on smaller capitalization companies (typically \$150 million to \$1 billion)
 - ✓ Long-term: average holding period of over 5 years (turnover has been 15-20% per year)
 - ✓ Build a constructive relationship with the management team
- **Assets Under Management**
 - ✓ Strategy AUM: Approximately US\$ 250 million
 - ✓ Yasu family invests about \$20 million in the fund
- **Investment Team**
 - ✓ Jiro Yasu, Portfolio Manager
 - ✓ Patrick Rial, Senior Analyst
 - ✓ Yosuke Yano, Analyst

Follow Up

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Company Name	Date of Presentation	Total Return(%)	Current Status	Major Developments
Toei Animation (TSE: 4816)	2013/11/05	+128.08% (Topix: +32.1%)	Closed 2015/12	<ul style="list-style-type: none"> • Shares appreciated 82% in 2017 as the company kept margins high by utilizing its IP portfolio • About 34% of market cap is in cash and securities • Trades at 8.1x LTM EBIT
Sotsu (Jasdaq: 3711)	2013/11/05	+80.0% (Topix: +57.9%)	Core	<ul style="list-style-type: none"> • Still no profit growth • Management change • About 50% of market cap in cash, trades at 5.4x LTM EBIT
EM Systems (TSE: 4820)	2015/4/7	+212.8% (Topix: +14.8%)	Core	<ul style="list-style-type: none"> • Margin improvement continued in FY2017. LTM OP margin was 22%, doubled in 3 years • Still owns the Osaka building which is fully occupied. Estimated worth 1/2 of market cap • Excluding net cash and the property, it trades around 6.5xLTM EBIT • Planning a major software upgrade. Started working with an artificial intelligence venture firm and NEC

Follow Up

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Company Name	Date of Presentation	Total Return(%)	Current Status	Major Developments
Agro Kanesho (TSE: 4955)	2016/4/5	+162.2% (Topix: +40.0%)	Core	<ul style="list-style-type: none"> • New product was filed for approval with the government in 2016. Agro was developing two more new products, but, it abandoned one. R&D costs started declining and margins started improving • Bought land in Yamaguchi prefecture and plans to build a new factory. Total investment will be about \$40 million • 50% of market cap in cash. Trades at 8.5x EBIT
Amuse (TSE: 4301)	2017/4/5	+23.3% (Topix: +15.4%)	Core	<ul style="list-style-type: none"> • Traded as high as 4,120 yen but corrected by 30% since then. • 2017 was an unfortunate year for the company: an actor was involved in a scandal, a major band's vocalist lost his voice, some new albums were delayed, etc. As a result the company missed its profit guidance. • 2018 is the 45th anniversary year since founding. The company is planning some major live events to celebrate. • About 40% of market cap in cash. Trades at 7.1x LTM EBIT

New Idea: CRE Inc (TSE: 3458)

Summary

Business Summary

- CRE is a real estate company focusing on logistics assets. It develops warehouses, provides master-lease services, manages public and private REITs, and offers other related services.

Valuation

- Share Price: 1,800 yen
- Market Cap: 22.9 billion yen (\$218 million)
- Net Debt: 5.7 billion yen (\$54 million) including debt for new developments
- Investments: 6.0 billion yen (\$57 million)
- Enterprise Value: 22.6 billion yen (\$215 million)
- EV/LTM EBIT 4.2x
- EV/LTM EBITDA: 4.0x
- PER LTM: 6.3x (before ex-item)
- PBR 1.45x

As of 2018/3/28
USD/JPY 105

Thesis

- We believe it has a good risk-reward profile
 - Downside protection: properties under-development and investments equivalent to 80% of market cap (+ net debt)
 - Our estimate of intrinsic value: 2,900 yen (61% upside potential)
- Growth prospects and valuation improvement potential
 - Robust demand for warehouses due to further e-commerce penetration
 - Growth of recurring revenue businesses, which may drive multiple expansion
- Good capital allocator
 - Good acquisition track record
 - Unique shareholder returns program

New Idea: CRE Inc (TSE: 3458)

Business Snapshot

- Establishment: 2009
- Employees 170
- Offices
 - Head office Tokyo
- Market Information
 - Code: 3458
 - Exchange: TSE 1st
 - Share Price: 1,800 yen
 - Dividend 30 yen (1.6 % yield)
- Shareholders
 1. Founding family 51.0%
 2. Kenedix 14.7%
 3. VARECS/UMJ 9.0%
 4. Treasury Shares 1.3%
 - 13% foreign investor ownership

As of 2018/3/28



LogiSquare Urawa Misono



LogiSquare Moriya

New Idea: CRE Inc (TSE: 3458)

Management Team

- Chairman Mr. Shuhei Yamashita
 - 44 years old
 - Keio University
 - Grandson of Taro Yamashita, a famous industrialist. He was the first president of the Arabian Oil Company, the first Japanese organization to produce oil in the Middle East
 - His family controls a large portfolio of prime real estate assets through their family company (Kokyo Tatemono)

- President Mr. Tadahide Kameyama
 - 43 years old
 - Osaka University
 - Before CRE, he worked for Nissho Iwai (currently Sojitz)
 - Joined a predecessor company of CRE in 2002

- President / CRE REIT Advisors Mr. Tsuyoshi Ito
 - 43 years old
 - Founded the predecessor of CRE Advisors in 2006
 - Before starting his own firm, he worked for the Industrial Bank of Japan

New Idea: CRE Inc (TSE: 3458)

Share Price Performance

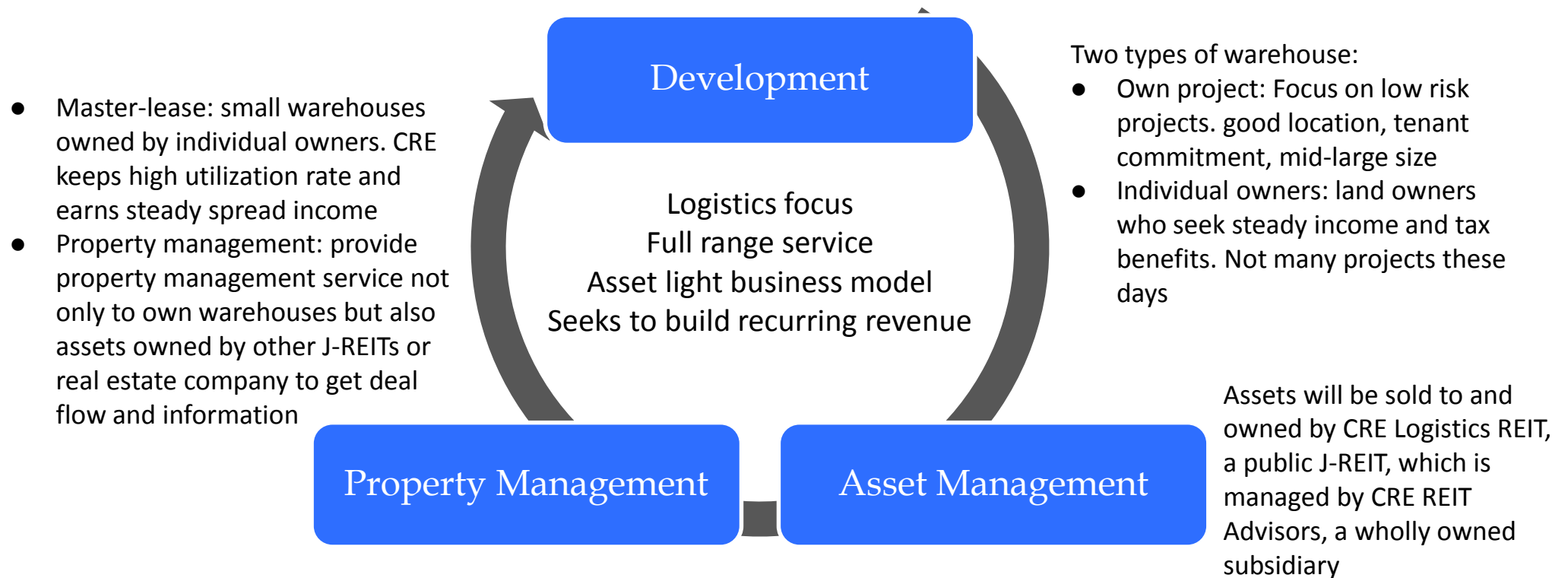
- IPO in 2015. Share price initially declined by about 50%
- Gradually recovering from the low. Now trades around the IPO price



New Idea: CRE Inc (TSE: 3458)

Business Model

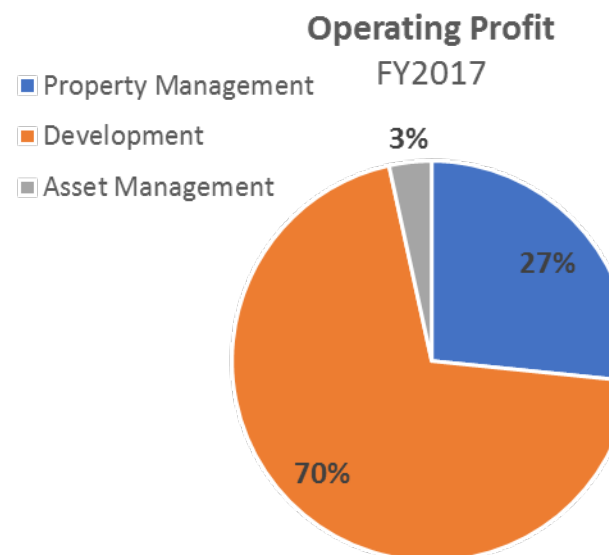
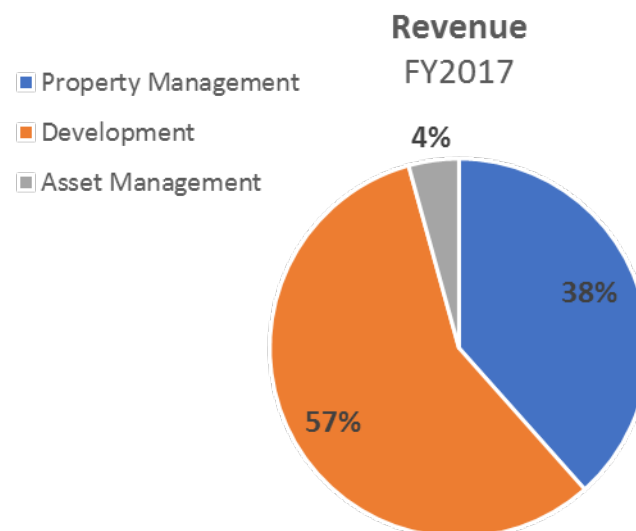
- CRE provides a full range of services related to logistics real estate such as development, tenant leasing, master-leasing, property management, REIT management, etc.
- CRE’s newly developed properties will be sold to its J-REIT and managed by CRE. Its recurring revenue stream will grow over the years



PL & BS Summary

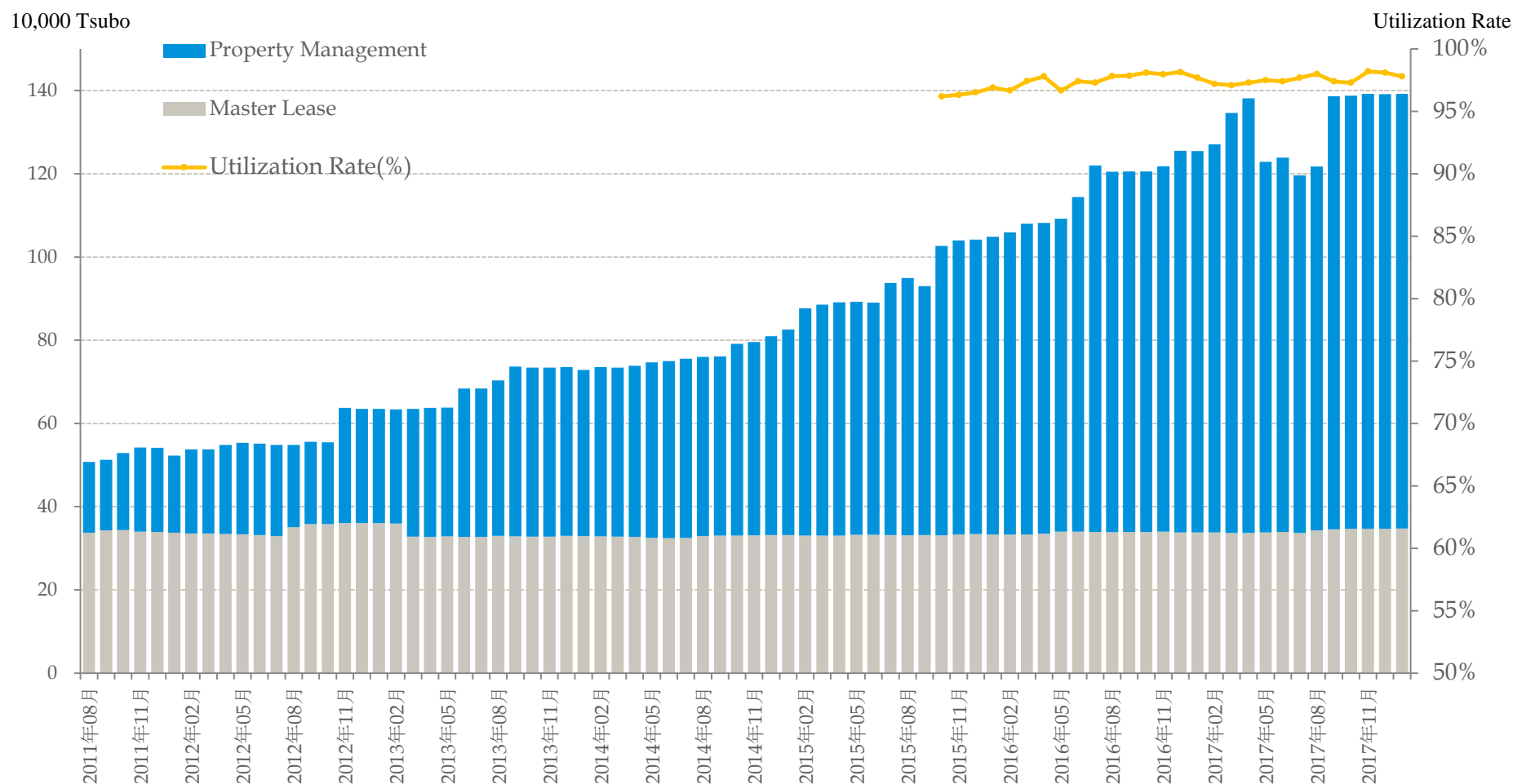
	2018/07 Guidance	2017/07	2016/07	2015/07	2014/07	2013/07
Consolidated PL						
Revenue	31,500	40,475	33,842	25,225	22,089	15,946
OP	1,700	5,188	4,386	2,373	2,537	841
Net Income	1,000	3,581	2,307	1,338	1,324	383
EBITDA	2,000	5,403	4,592	2,600	2,675	951
Property Management						
Revenue	17,500	15,552	15,253	15,590		
Operating Profit	1,600	1,610	1,522	1,515		
OPM	9.1%	10.4%	10.0%	9.7%		
Development						
Revenue	13,400	23,185	17,534	7,877		
Operating Profit	800	4,234	3,515	1,297		
OPM	6.0%	18.3%	20.0%	16.5%		
Asset Management						
Revenue	600	1,739	1,056	334		
Operating Profit	300	208	217	117		
OPM	50.0%	12.0%	20.5%	34.8%		
Adjustment						
Operating Profit	-1,000	-864	-863	-638		

	2018/07 Guidance	2017/07	2016/07	2015/07	2014/07	2013/07
Consolidated BS						
Total Assets		36,969	37,455	27,153	17,449	15,801
Cash		14,505	14,282	8,727	5,007	1,722
Debt		11,974	14,257	10,013	5,800	5,414
Net Debt		-2,531	-25	1,286	793	3,692
Net Assets		15,819	11,376	8,967	2,451	1,007
Total Assets/Net Assets		42.8%	30.4%	33.0%	14.0%	6.4%



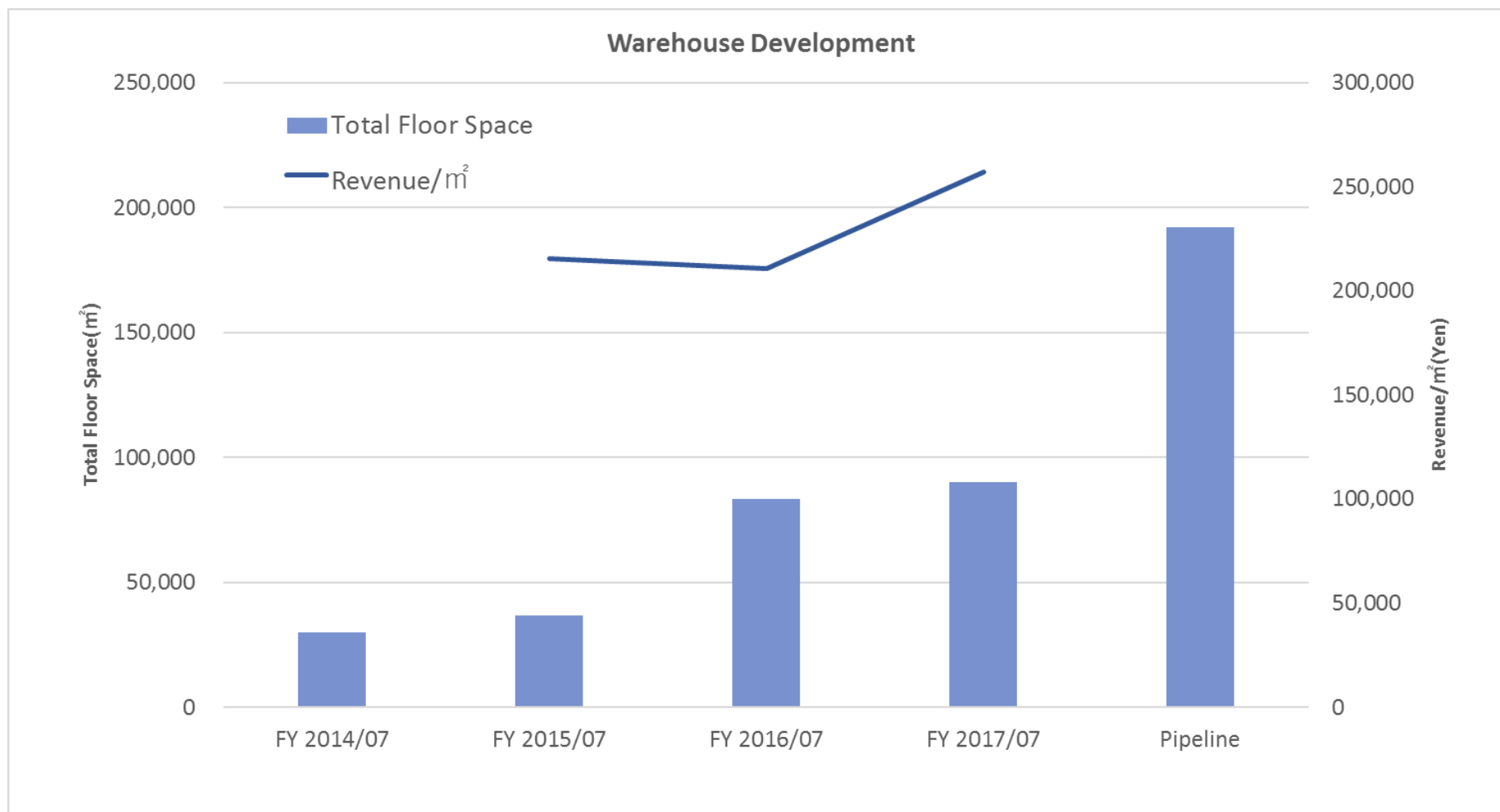
Real Estate Management

- CRE manages 1,202 warehouses held by individual owners using master leases (97.8% utilization rate)
- CRE also acts as a property manager for large warehouses



Development

- CRE develops 3-4 warehouses per year. Revenue and profit of the segment will be lumpy depend of size and location of the new warehouses
- Focus on lower risk projects: good location, middle-large size, pre-commitment by tenants, etc.

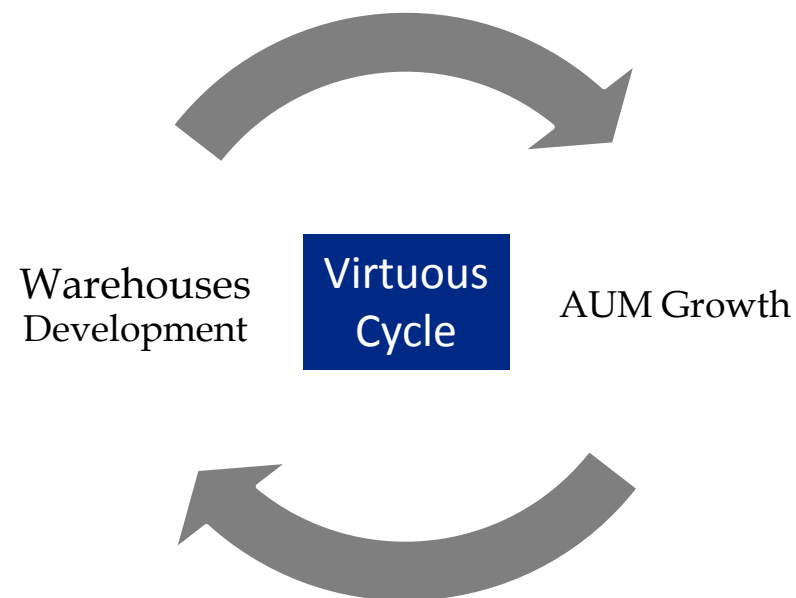


New Idea: CRE Inc (TSE: 3458)

Asset Management

- CRE Logistics REIT, Inc. (TSE: 3487) went public on February 7th 2018
- Current AUM 96.6 billion yen including non-REIT assets. Long-term AUM target 500 billion yen
- We also own about 2% of CRE Logistics REIT because the quality of assets are quite high and yield is attractive

CRE Logistics REIT	
Exchange:	Tokyo
Ticker:	3487
#of Properties	7
Total Acquisition Cost	47.7billion yen
Utilization rate	100%
LTV	Max 50%
Current Yield	5.3% (gross)
Fees	
Management Fee	0.40% of total asset
Incentive Fee	5% of net income (about 10bps)
Acquisition Fee	0.5% - 1%
Asset Sale Fee	0.5%



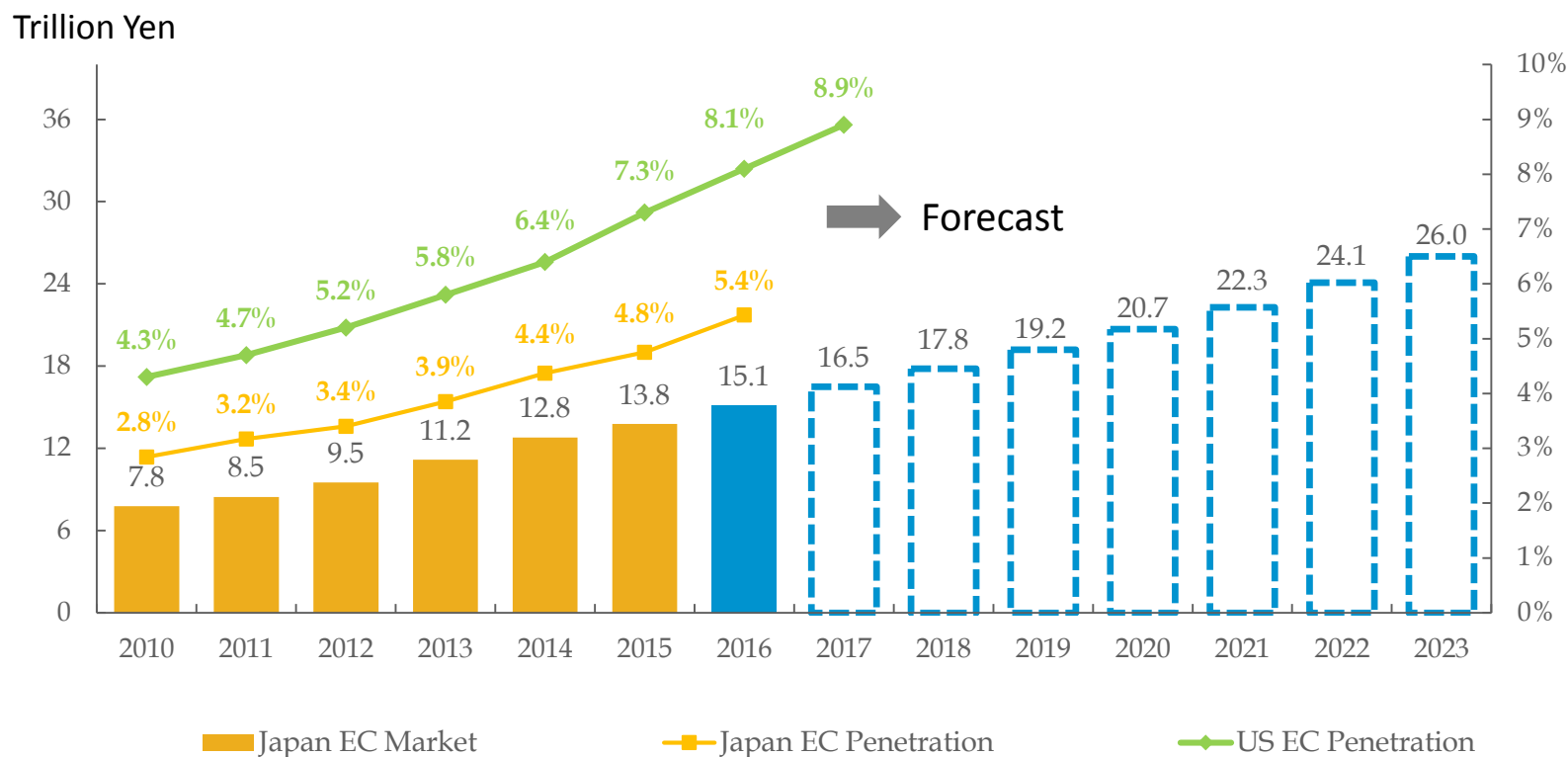
Portfolio Comparison

- CRE's disciplined approach:
 - Focus on Tokyo area
 - Avoid super large size
 - Prudent use of leverage

(mln Yen)	CRE Logistic REIT	GLP J-REIT	Lasalle Logiport REIT	Mitsui Logistics Park	Mitsubishi Logistics
<u>Mkt Data</u>					
TSE Code	3487	3281	3466	3471	3481
Mkt Cap	26,050	393,349	124,850	92,890	55,854
LTV	47%	40%	39%	23%	30%
Yield	5.3%	3.8%	4.1%	3.1%	3.6%
<u>Portfolio Data</u>					
Number of Properties	7	62	11	12	8
Total Assets	47,725	524,644	188,400	98,300	70,800
Tokyo Area	94%	62%	96%	87%	75%
Over 100,000 sq m	0%	21%	84%	39%	56%
Over 5 years old	0%	28%	81%	10%	0%
Utilization Rate	100%	100%	98%	100%	100%

Growth Opportunity: e-commerce penetration

- E-Commerce penetration: US 8.1% v.s. Japan 5.4%
- E-commerce in Japan: 2016 15.1 trillion yen → expected to grow over 20 trillion yen by 2020



Source: METI, Nomura Institute of Research, and United States Census Bureau

New Idea: CRE Inc (TSE: 3458)

Capital Allocation and Shareholder Return

- CRE has been rationally allocating its capital
- Implemented unique shareholder return program in 2016

CRE's Acquisition Track Record

- 2010 Acquired master lease business and property management business from Commercial R.E.
- Commercial RE bankrupt in 2010 May with debt of 15 billion yen
 - CRE paid 500 million yen to acquire the business
- 2011 Acquired KK Tenko-Souken, which operates mater-lease business and property management business mainly in Kanagawa prefecture
- 2014 Acquired Strategic Partners KK, the predecessor firm of CRE REIT Advisors
- 2015 Acquired 20% stake of Enbio Holdings (Mothers: 6092), which specializes in utilization of contaminated land

CRE's shareholder return program

Due to lumpy nature of profit from its development business, the company implemented the following shareholder return program

Dividend Policy: Distribute 50% of profit from recurring businesses (master-lease and asset management)

Buybacks: Use profit from development business and deploy when share price is low

CRE has been carrying out a 1 billion yen (approx. 4.7% of outstanding) buyback program this fiscal year.

New Idea: CRE Inc (TSE: 3458)

Industry Consolidation

Logistic Real Estate Companies

GLP Pte Ltd. / China Vanke, Hopu, Hillhouse, Bank of China Group Investment

- In July 2017, the consortium announced to acquire GLP for US\$11.6 billion or US\$ 15.7 billion for transaction value
- The business had revenue of \$983 million, EBIT of \$420 million, and EBITDA of \$434 million
- Valuation was 37.4x EBIT and 36.2x EBITDA

AMB Property Corp / ProLogis

- In January 2011, AMB Property acquired ProLogis for \$16.5 billion, which was 35.6x EBITDA

Asset Management Firms

Clarion Partners / Legg Mason

- In January 2016, Legg Mason acquired 83% of Clarion Partners for \$585 million
- Clarion is a leading diversified real estate investment firm with AUM of \$40 billion
- Acquisition price represented 1.8% of AUM or 10.5x EBITDA

Nuveen Investments / TIAA

- In October 2014, TIAA acquired 100% of Nuveen for \$6.25 billion, equating to 18.1x EBIT or 15.1x EBITDA

Aberdeen Asset Management / Standard Life

- In August 2017, Standard Life acquired 100% of Aberdeen Asset for \$3.6 billion which represented 19.0x EBIT or 11.4x EBITDA

Janus Capital / Henderson

- In May 2017, Henderson acquired Janus for 2.6 billion, which represents 10.1x EBIT and 7.06x of EBITDA

Epoch Holdings / Toronto Dominion Bank

- In March 2013, Toronto Dominion acquired 100% of Epoch Holdings, a boutique equity manager in NY, for \$669 million.
- Valuation was 13.9x EBIT and 13.6x EBITDA

New Idea: CRE Inc (TSE: 3458)

Valuation

- We apply 10x EBIT for Property Management, 6x EBIT for Development, and 12x EBIT for Asset Management
- We have excluded debt associated with warehouse development since it will be paid down when CRE sells the assets
- We see 61% upside potential at current share price. We also expect its IV will grow over years as its AUM of J-REIT grows

	Normalized EBIT	x Multiple	= Business Value
Property Management	1,600	10	16,000
Development	2,500	6	15,000
Asset Management	300	12	3,600
Adjustment	-1,000	8	-8,000
Business Value			26,600
Cash			8,813
Debt for operation			4,782
Investment			6,000
Total IV			36,631
Shs. Outstandings			13
IV/Share			2,900
Upside			61%

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