Starwood European Real Estate Finance Limited

Quarterly Performance Update

June 2013

Share Price / NAV at 30 June 2013

Share price (p)	102.50
NAV (p)	98.65
Premium / (discount)	3.9%
Issued shares	238,100,000
Market cap	£244.1m

Fund Information

Fund Type	Closed-ended investment company
Domicile	Guernsey
Inception Date	17 December 2012
Listing	London Stock Exchange (Main Market)
LSE Identifier	SWEF
ISIN Code	GG00B79WC100
NAV Frequency	Monthly
Dividend Frequency	Quarterly
Origination Fee	0.75%
Management Fee	0.75%
Website	www.starwoodeuropeanfinance.com

Key Portfolio Statistics at 30 June 2013

Number of issuers	1
Number of investments	1
Number of industries	1
Percentage of invested portfolio in floating rate investments	100%
Portfolio current yield	N/A (1)
Weighted average coupon	N/A (1)
Blended portfolio LTV	N/A (1)
Average loan term	5 years
Percentage of net assets in cash	91.8%
Percentage of net assets invested in senior loans	0%
Percentage of net assets invested in second lien and mezzanine loans	8.1%
Percentage invested in GBP	100%
Percentage invested in Euro	0%

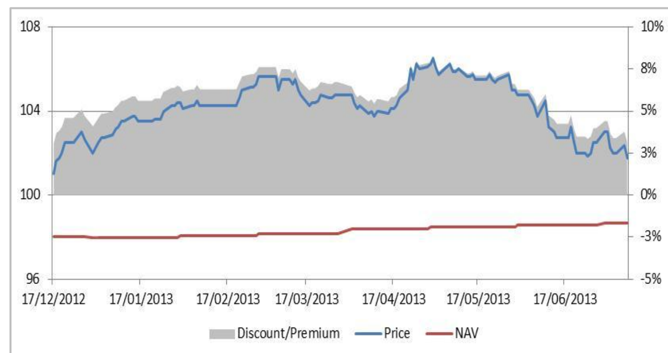
(1) Unable to disclose until the fund has greater than one investment due to confidentiality undertakings.

Summary

The investment objective of Starwood European Real Estate Finance Limited (the "Company") is to provide Shareholders with regular dividends and an attractive total return while limiting downside risk, through the origination, execution, acquisition and servicing of a diversified portfolio of real estate debt investments (including debt instruments) in the UK and Continental European markets.

The Company is targeting a net total return on invested capital of 8-9 per cent. per annum and a dividend of 7.0 pence per Ordinary Share once fully invested. See further commentary below on the amount and timing of future dividend payments.

Company Performance



Investment Adviser's Commentary

Investment portfolio

As at 30 June 2013 the Company was 8.1% invested through a mezzanine loan to the Maybourne Group. Subsequent to 30 June the Company has closed one new transaction for £10m and has two loans in final documentation amounting to a further £26.8m of commitments with imminent closure. Once these further two loans close this will bring the total invested and/or committed to 24%. Of the loan which closed subsequent to 30 June, underlying loan confidentiality prohibits full disclosure but in summary:

West End, London: The Company has provided £10m out of a £55.75m three year term loan to a very strong opportunistic property investor secured on a strongly located transitional asset in the Tottenham Court Road area of the West End. The Borrower intends to obtain a mixed use planning consent which would then facilitate a refurbishment process at which time the loan would be repaid. The initial LTV is 50% and the loan is expected to generate approximately a 7% gross IRR. The Company remains interested in participating in the next stage of the project but has no obligation to do so.

June 2013

Investment Restrictions & Guidelines

Location	UK & Continental Europe
Loan Term	Between 3 and 7 years
Loan Type	Senior, subordinated and mezzanine loans, bridge loans, selected loan on loan financing and other debt instruments
LTV	Absolute maximum of 85% with a blended portfolio LTV of no more than 75%
Real Estate Sector & Property Type	Commercial real estate sectors including office, retail, logistics, light industrial, hospitality, student accommodation, residential for sale and multi-family rented residential. Not more than 20% of NAV in residential for sale.
Counterparty & Property Diversification	Not more than 20% of NAV exposed to one Borrower legal entity and no single investment exceeding 20% of NAV at time of investment.

Pipeline

Unquestionably the real estate financing world has seen significant supply/demand changes since the end of 2012. Many of these were highlighted at the time of the Company's IPO and others are still evolving. We highlight the big picture impact on the property market in the 'Market Commentary' section below.

The Investment Adviser, Investment Manager and the Company's Board work extremely closely together with significant visible hands on involvement by Investment Manager and Board members strategically and at deal levels.

In terms of the Company's immediate investment pipeline, there are currently six other loans, two due to close imminently as noted above, three in execution and one agreed term sheet imminently moving into execution. These six loans in aggregate offer the Company a total investment potential of approximately £130m (of which £26.8m is included above). Three are in Continental Europe and three are in the UK. Sector exposures include the three main commercial real estate sectors of office, retail and light industrial/logistics as well as the residential sectors. These loans are all in line with the Company's investment return targets. We expect these transactions all to close by end-September and if this were to occur the Company would be 68% invested or committed.

We would however highlight that transactions in the current market do have an above average level of uncertainty of closing to that typically expected at such an advanced stage and, as such, this forward guidance is caveated.

More generally we have seen our transaction pipeline continue to mature and have a number of other small, mid and large positions that are progressing well.

Investment Process

It is worth discussing why the process of investment has been somewhat slower than anticipated and what has been / is being done to address this.

Given the time it takes time to convert an active pipeline into loans in execution it was always unlikely that many transactions would close in the first few months following the Company's IPO. During the course of Q2 2013 the Company, along with other Starwood affiliates and partners, devoted a reasonable degree of resources to bidding for a large loan book being sold by a prominent German bank. Such an opportunistic transaction would have been transformational as it would have permitted the deployment of much of the Company's cash in a single transaction underpinned by strong property and loans. In the end our bid, whilst extremely competitive, was insufficient to secure the transaction. However, we believe that there will be other similar opportunities in the future and the Company remains well placed to participate in this type of transaction.

During this time the Investment Adviser has continued to focus on direct client origination and we have reviewed well in excess of £1.5 billion of potential investment opportunities ranging from £20m to £300m in size. There have been numerous reasons for not proceeding including where it was a bid process and another bidder succeeded, where the implied mezzanine became too slim

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relative to the overall capital structure and where weak tenant fundamentals created binary risk in the transaction.

It is also worth noting three prevalent themes that have resulted in delay / failure in consummating transactions:

- Firstly, given the short term nature of many outstanding loan maturities, loan prolongations are now a very high level agenda item for most European banks. However, what we have found, to our frustration, is that in such refinancings, because at least one party is inevitably taking some financial pain, either monetary or performance wise, the time involved in moving a refinancing forward is excessive. In addition the relative positions of the parties involved are counter-productive and as a result many deals become derailed not least through incumbent lender extension.

- Secondly, borrowers believe they are able to refinance higher levered deals for the first time in five years and as a result a number of transactions fall down in the detailed due diligence stage.

- Thirdly, the Company simply loses transactions on the basis of pricing or structure. Whilst pricing has tightened from H2 2012 we believe the Company's targeted returns remain achievable. The more significant challenge has been the structures of transactions – for example, on some deals another lender has agreed to structural deficiencies e.g. lack of mortgage security, amortisation or weak covenants which we would not consider appropriate. The Investment Manager and Investment Adviser remain diligent on delivering not just an outsized return but a balanced risk adjusted return across the debt capital stack.

Alongside the above market challenges, the Investment Adviser is cognisant of the need to establish a diverse portfolio and reviews transaction in this light.

Future strategy/investment outlook

In terms of future investment strategy, we are building a presence in both the smaller whole loan lending market and taking a leading role in the very large one-off structured transactions (such as Maybourne). It is also likely a greater UK regional and overall continental European focus will become visible in our proactive origination strategy, as London continues to attract the vast majority of other investors' attention.

It is expected that the principal focus will be making whole loans that can offer "one stop" borrowing and then to carefully consider which loans should be partially syndicated to enhance returns.

We see good and growing prospects for the Company and believe the original target of full investment within 12 months could reasonably still be achieved. We expect the additional six deals mentioned above to be invested or committed by the end of September 2013 and would be 68% invested or committed at that point. In addition, as noted above, we have a number of other pipeline transactions that are progressing well.

As set out above, there are a number of factors that can act as an impediment to closing transactions within expected timeframes or at all. Within the bounds of competitive confidentiality the Company wishes to be as clear on the investment pipeline as possible and if the £130m of deals expected to close by the end of September changes materially, a further communication with regards to the pace of investment will be made.

Dividends

At launch, the Company had targeted a dividend of 3.5 pence per Ordinary Share in respect of the period from Admission (17 December 2012) to the first financial year end (31 December 2013) and 7.0 pence per Ordinary Share in subsequent financial periods. This was predicated on the assumption that 50% of the Company's available cash would be invested within six months from Admission and the remainder within 12 months.

For the period to 31 December 2013, the Company now expects to be able to pay a dividend of at least 1.0 pence based on the two deals that have closed, and if all six pipeline deals referred to above close, and no others, the dividend could be up to 2.4 pence. In the event that further transactions close prior to the year end, the total dividend will be higher and a further update in this regard will be provided in due course.

It is currently expected that a first interim dividend will be declared in October 2013 for the period ending 30 September 2013 of at least 0.70 pence.

Based on detailed projections, the Company remains comfortable that when fully invested it will be able to meet its dividend target of 7.0 pence per annum.

Market Commentary

The first four to five months of the year highlighted a much greater degree of optimism within the property markets, still cautious but certainly greater than in recent years. In the last few months this optimism has in specific markets accelerated and indeed could now be slightly ahead of actual fundamentals. Nowhere is this more apparent than in London which has recently seen some tightly priced equity investments. Notwithstanding the risk cushion implicit in lending we have also observed a small number of lending transactions that are questionable on either price or structure or both. Conversely market optimism has also engendered a resurgent desire for investors to act upon their refinancing requirements or reinvigorated interest in new investment. This typically creates a greater need for creative property lending. Finally there do remain many other sectors or geographies that still remain cautious and consistent with underlying economic fundamentals. Put together the demand for property finance has unquestionably increased offering greater opportunities but also requiring the Company to continue to be diligent in its underwriting requirements.

On the supply side, many European banks continue to focus on their withdrawal or reduction of exposure to the sector not least to meet Basel III as well as real estate finance being a non-core activity. Individual events, such as the recent nationalization of SNS by the Dutch government, also underscore continued

regulatory concerns over the carrying value of many loans on bank balance sheets. We do however see that global monetary easing has created a generic "hunt for yield" and political pressure to lend is also present, not least in the UK through the "Funding for Lending" scheme. The UK Clearing Banks have greater lending capacity but do remain, for the most part, cautious on business possibilities. An increasing US and European insurance presence means there is excess finance capacity for the prime London office market for strong sponsors and low leverage. Similarly mainstream German lending has become more competitive especially with the appetite and resultant pricing for Pfandbrief, the key covered bond issuance program for domestic German real estate lending banks. Meanwhile the mezzanine lending space continues to develop and is summarily defined by investment funds raising substantial third party capital for higher return lending strategies – we expect to observe at least £2bn of fund style investor commitments to the specialist fund managers in this field by the end of 2013.

Put together the picture is fundamentally one of increased activity and active players. The Company observes that there are now two "bookends" in the market being the attractive efficiently priced core senior market and a well-capitalised mezzanine market that has the ability to embrace quite significant risk should it choose to do so but is often hampered by quite high return requirements. Neither bookend is quite as deep as they appear when transitional assets or a broader geographical focus are concerned and the numbers of players that can embrace “one stop shop lending” in an efficient and timely manner, such as the Company, remains a much smaller sub set.

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