Starwood European Real Estate Finance Limited

Quarterly Investment Update

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 Europe.

SHARE PRICE / NAV AT 30 JUNE 2019

Share Price (p)	NAV (p)	Premium / (discount)	Dividend Yield	Market Cap
102.00	102.82	(0.3)%	6.4%	£421.5m

FUND INFORMATION

FUND TYPE	Closed-ended investment company
DOMICILE	Guernsey
INCEPTION DATE	17 Dec 2012
LISTING	LSE (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

INVESTMENT PORTFOLIO AT 30 JUNE 2019

As at 30 June 2019, the Group had 17 investments and commitments of £478.9 million as follows:

Transaction	Sterling equivalent balance [1]	Sterling equivalent unfunded commitment [1]
Hospitals, UK	£25.0m	-
Mixed use development, South East UK	£11.1m	£1.2m
Regional Hotel Portfolio, UK	£45.9m	-
Credit Linked Notes, UK real estate	£21.8m	-
Hotel & Residential, UK	£39.9m	-
Office, Scotland	£4.3m	£0.7m
Total Sterling Loans	**£148.0m**	**£1.9m**
Logistics, Dublin, Ireland	£13.0m	-
Hotel, Barcelona, Spain	£41.3m	-
Industrial Portfolio, Central and Eastern Europe	£37.0m	-
Three Shopping Centres, Spain	£33.0m	£6.7m
Shopping Centre, Spain	£15.2m	-
Hotel, Dublin, Ireland	£53.8m	-
Residential, Dublin, Ireland	£2.0m	-
Office, Paris, France	£14.3m	-
Hotel, Spain	£26.2m	£22.4m
Office & Hotel, Madrid	£16.6m	£0.9m
Mixed Portfolio, Europe	£46.6m	-
Total Euro Loans	**£299.0m**	**£30.0m**
Total Portfolio	**£447.0m**	**£31.9m**

[1] Euro balances translated to sterling at period end exchange rates.

INVESTMENT RESTRICTIONS AND GUIDELINES

LOCATION
UK & wider European Union's internal market. No more than 50% in any country except the UK where it is unlimited (subject to sector limits below).

LOAN TERM
Between 3 and 7 years but discretion retained. At least 75% of loans 7 years or less.

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. No more than 30% of NAV in residential for sale. No more than 50% of NAV in any single sector in the UK except office which is limited to 75%.

COUNTERPARTY & PROPERTY DIVERSIFICATION
No more than 20% of NAV exposed to one borrower legal entity and no single investment exceeding 20% of NAV at time of investment.

KEY PORTFOLIO STATISTICS AT 30 JUNE 2019

Number of investments	17
Percentage of currently invested portfolio in floating rate loans	81.8%
Invested Loan Portfolio unlevered annualised total return [1]	7.2%
Invested Loan Portfolio levered annualised total return [2]	7.4%
Weighted average portfolio LTV – to Group first £ [3]	23.0%
Weighted average portfolio LTV – to Group last £ [3]	64.7%
Average loan term (stated maturity at inception)	4.0 years
Average remaining loan term	2.8 years
Net Asset Value	£424.9m
Amount drawn under Revolving Credit Facilities (excluding accrued interest)	(£45.9m)
Loans advanced	£428.6m
Financial assets held at fair value (including accrued income)	£21.9m
Cash	£28.0m
Other net assets/ (liabilities) (including hedges)	(£7.7m)
Origination Fees – current quarter	£0.4m
Origination Fees – last 12 months	£0.8m
Management Fees – current quarter	£0.8m
Management Fees – last 12 months	£2.9m

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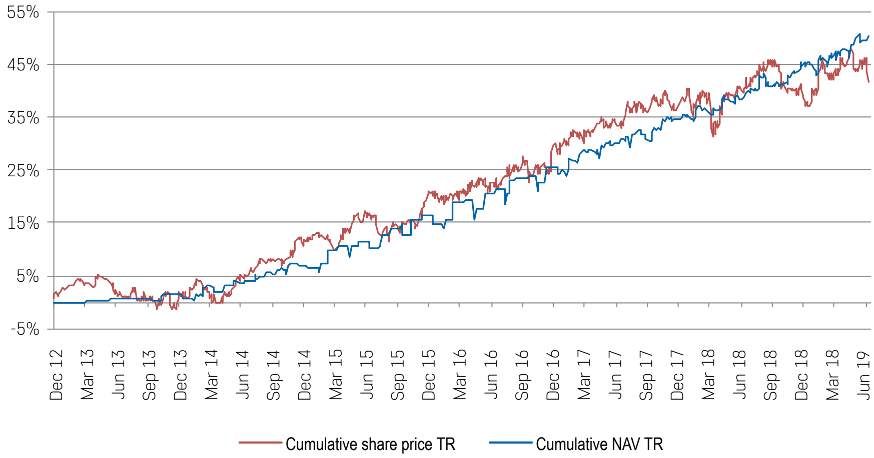
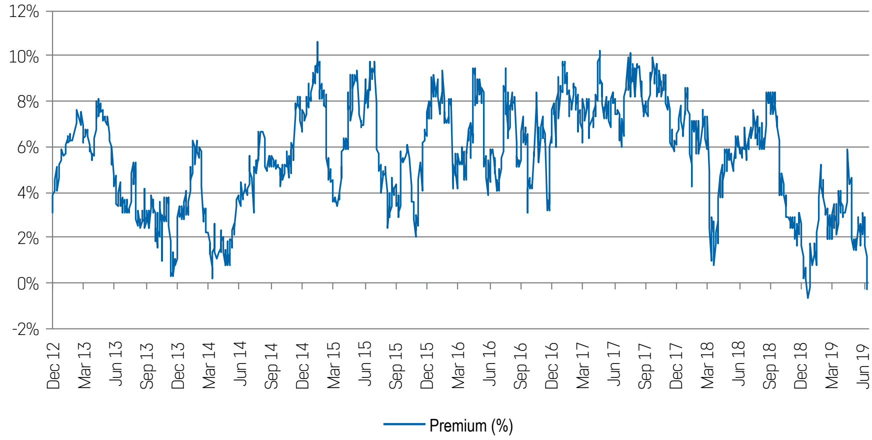
DIVIDEND

On 24 July 2019 the Directors declared a dividend in respect of the second quarter of 1.625 pence per Ordinary Share payable on 30 August 2019 to shareholders on the register at 2 August 2019.

SHARE PRICE, NAV AND DISCOUNT





[1] The unlevered annualised total return is calculated on amounts outstanding at the reporting date, excluding undrawn commitments, and assuming all drawn loans are outstanding for the full contractual term. 14 of the loans are floating rate (partially or in whole and some with floors) and returns are based on an assumed profile for future interbank rates but the actual rate received may be higher or lower. Calculated only on amounts funded at the reporting date and excluding committed amounts (but including commitment fees) and excluding cash un-invested. The calculation also excludes the origination fee payable to the Investment Manager.

[2] The levered annualised total return is calculated as per the unlevered return but takes into account the amount of net leverage in the Group and the cost of that leverage at current LIBOR/EURIBOR.

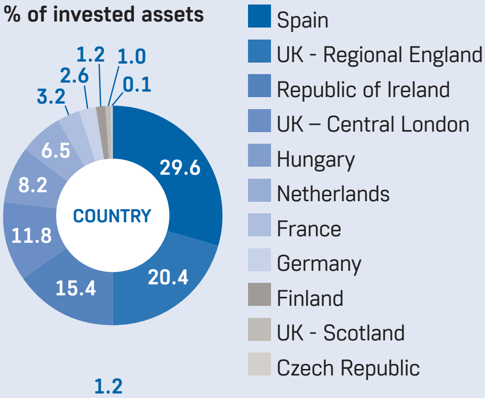
[3] LTV to Group last £ means the percentage which the total loan drawn less any amortisation received to date (when aggregated with any other indebtedness ranking alongside and/or senior to it) bears to the market value determined by the last formal lender valuation received by the reporting date. LTV to first Group £ means the starting point of the loan to value range of the loans drawn (when aggregated with any other indebtedness ranking senior to it). For development projects the calculation includes the total facility available and is calculated against the assumed market value on completion of the relevant project.

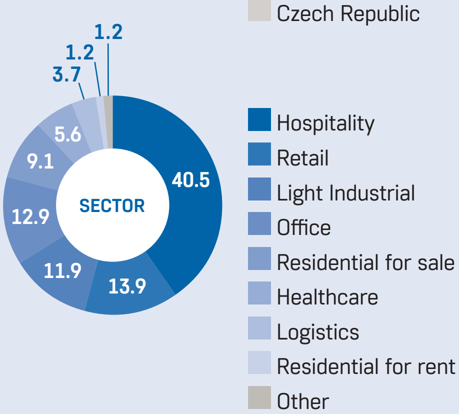
KEY PORTFOLIO STATISTICS AT 30 JUNE 2019

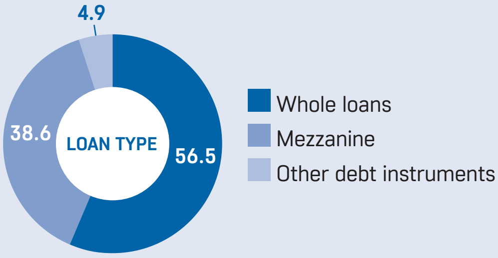
Remaining years to contractual maturity*	Value of loans (£m)	% of invested portfolio
0 to 1 years	50.1	11.2
1 to 2 years	116.7	26.1
2 to 3 years	111.0	24.8
3 to 5 years	144.2	32.3
5 to 10 years	25.0	5.6

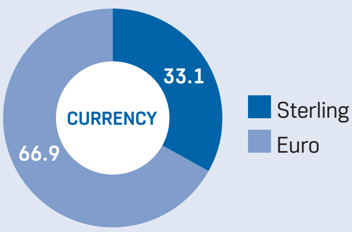
* excludes any permitted extensions. Note that borrowers may elect to repay loans before contractual maturity.

% of invested assets









* the currency split refers to the underlying loan currency, however the capital on all non-sterling exposure is hedged back to sterling.

PLACING

On 7 May 2019, the Company announced that it was seeking to issue up to 38,200,000 new ordinary shares of no par value at 104.75 pence per share. On 13 May 2019 the Company announced that the Placing was oversubscribed and a scaling back exercise was undertaken such that the targeted gross proceeds of £40.0 million were raised.

SECOND QUARTER PORTFOLIO ACTIVITY

The following portfolio activity occurred in the second quarter of 2019:

- **New Loan – Office Scotland:** On 24 April 2019 the Group committed to provide a £5 million whole loan on an office in Scotland of which £4.3 million has been funded to date.
- **New Loan – Diversified portfolio, Europe:** On 10 May 2019 the Group committed to participate in the funding of a €104 million mezzanine loan secured by a diversified portfolio of assets located in the Netherlands, Germany and Finland. Starwood Property Trust, Inc (through a wholly owned subsidiary) is participating in 50 per cent of the mezzanine loan amount, with the Group funding the balance amounting to a net commitment of €52 million. The portfolio is comprised of 165 assets and provides strong diversification in terms of tenant base, location and asset class. The loan has a term of 3 years with two, 1 year extension options and the Group expects to earn an attractive risk-adjusted return in line with its stated investment strategy.
- **Final Repayment: Irish School:** On 8 May 2019 the Group received full repayment of €18.85 million on the loan to an Irish School following completion of the borrower's business plan.

The Group also received £29.6 million of partial loan prepayments as a result of asset sales within the respective property portfolios. The Group used the proceeds of amortisation, the Irish School repayment and available cash and further drawings on its revolving credit facility to fund the new loans. The proceeds of the placing of new equity were used to partially repay the Group's revolving credit facilities.

Following this portfolio activity, the Group remained substantially fully invested at 30 June 2019 with drawings of £18.0 million (net of cash) on its £114 million credit facilities and £31.9 million of unfunded commitments.

REVIEW OF FIRST HALF INVESTMENT ACTIVITY

The table below summarises the new commitments made and repayments received in the first six months of 2015 to 2019.

	H1 2015	H1 2016	H1 2017	H1 2018	H1 2019
New Commitments	£31.3 m	£98.9m	£115.5m	£147.5m	£49.9m
Repayments & Amortisation	-£21.9 m	-£92.1m	-£85.2m	-£74.1m	-£45.9m
Net Increase in Commitments	**£9.4m**	**£6.8m**	**£30.3m**	**£73.4m**	**£4.0m**

The net increase in commitments during the first half of 2019, whilst still positive, has been lower than the last two years. The explanation for the lower than previous years increase in net commitments is seen to be one of timing of transactions rather than an overall reduction in activity for the reasons explained below.

1. As we have reported in previous years, the first quarter is frequently quiet in the real estate market and we have only tended to see high levels of activity in the first quarter when deals which were in execution during the previous year did not complete then. This year, no deals rolled over from 2018 and the first quarter was relatively subdued as a result.
2. The Group has a number of transactions under review and two transactions in execution which it hopes to close early in the third quarter. If both transactions close, this would mean that the level of commitments made would be similar to the first half of 2018.

The Group also received a relatively low amount of repayments in the first half of 2019. However, since the end of the second quarter, the following repayments have been received:

- Mixed Use Development, UK - £8.1 million amortization following the sale of one of the properties in line with the business plan.
- Industrial Europe - €26.3 million amortization following the sale of one of the properties.
- Hotel, Barcelona, Spain – full repayment of €46 million following the sale of the hotel.

With these repayments factored in, the repayment percentage for the first seven months of the year is approximately 27 per cent of the loan book at the beginning of the year. In a normal year, we expect 30-40 per cent of the portfolio to repay on average but some years may be materially higher or lower than the average. It is difficult to accurately predict the repayment intention of borrowers as they execute on their business plans but we will continue to closely monitor this throughout the second half in order to try to minimise any potential cash drag from repayments.

The Group continues to see strong opportunities to deploy capital in our target markets. The Investment Adviser has a number of transactions under review which present solid risk adjusted returns.

REPORTED RETURNS

Reported returns have fallen in the second quarter from 7.3 per cent to 7.2 per cent unlevered, and from 7.8 per cent to 7.4 per cent levered. We would expect the levered returns to increase as the loans in execution are funded and further leverage is used for the loan portfolio.

In addition to this and as previously explained, the simplified way in which the annual return is presented does lead to the returns being a conservative estimate at any point in time. The following items enhance the actual returns achieved:

- In the quoted return, we amortise all one off fees (such as arrangement and exit fees) over the contractual life of the loan which is currently four years for the portfolio. However, it has been our experience that loans tend to repay after approximately 2.5 years and as such these fees are actually amortised over a shorter period.
- Many loans benefit from prepayment provisions which mean that if they are repaid before the end of the protected period, additional interest or fees become due. As we quote the return based on the contractual life of the loan, these returns cannot be forecast in the return.
- The quoted return excludes the benefit of any foreign exchange gains on Euro loans. We do not forecast this as the loans are often repaid early and the gain may be lower than this once hedge positions are settled.

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www.starwoodeuropeanfinance.com

The Company is the largest London-listed vehicle to provide investors with pure play exposure to real estate lending.

The Group's assets are managed by Starwood European Finance Partners Limited, an indirect wholly-owned subsidiary of the Starwood Capital Group.

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The above three upsides to quoted returns are not incorporated in the gross levered yield of 7.4 per cent as they are not guaranteed to occur, are difficult to forecast accurately and to incorporate them could overstate the expected return. However, we expect these to continue to provide an enhancement to the quoted levels of return going forward although the levels of this enhancement may vary depending on when the loans repay versus contractual maturity, the level of prepayment protection and the shape of the sterling-euro forward curve. Over the life of the Company to date, we have experienced, on average, an enhancement of 0.63 percentage points from prepayments and one-off fees when loans repay and we expect the pick up on foreign exchange to be in excess of 1 percentage point.

Finally, the Group maintains a dividend reserve to ensure that it can maintain a stable dividend during periods where modest leverage or cash drag can temporarily lower returns due to the timing of new loans and repayments.

MARKET COMMENTARY

2019 has seen slower volumes in the commercial real estate market in Europe. According to BNP Real Estate total investment volumes for the first quarter of 2019 were €43 billion which is 21 per cent lower than in the same period in 2018. The average hides different situations across the different cities. In London, Brexit uncertainties have not hit volumes much more than the average with London volume broadly in line with the European average at 23 per cent lower than last year. Germany's big markets outside of Berlin were down significantly with Munich, Frankfurt and Hamburg down 77 per cent, 67 per cent and 61 per cent respectively. Hot markets included Milan, Berlin and Madrid where investors are anticipating tight markets and strong rental growth potential were up 91 per cent, 78 per cent and 12 per cent respectively. Volume data for the second quarter was not available at the time of writing but discussions with a number of market participants suggest a similar trend is expected for the second quarter.

Increased expectations of further rate cuts and quantitative easing has driven asset pricing across the board. Investors were already expecting the ECB to supply fresh monetary stimulus to help alleviate the ongoing economic stress within the region and the nomination of the International Monetary Fund's Christine Lagarde to be the next ECB president has raised expectations of continued loosening monetary policy. The EUR interest rate curve has significantly flattened so now the 5 year swap is now in line with 3 month EURIBOR at -33 basis points. Government bond yields have continued to push down with all European 2 year sovereign debt now yielding negative returns and with German 10 year bonds having yielded as low as -0.4 per cent in recent days. Even peripheral European debt such as Portugal and Greece is trading at significantly lower yields than in recent years. Greek 10 year bonds have priced almost as tight as at 2 per cent having been almost 20 per cent in 2016 and Portugal is now at 0.3 per cent versus over 4.4 per cent just 18 months ago.

With low asset yields we have seen increased formation of lower priced debt funds and direct investing by insurance companies and pension funds in more vanilla senior commercial real estate debt as an alternative for sovereign and corporate bonds. Insurance companies such as Axa and Allianz have been expanding their senior commercial real estate lending strategies and we are seeing some new players with similar mandates emerging. We have also seen good pricing on the two recent CMBS issuances with Morgan Stanley's Eos (European Loan Conduit No. 35) pricing at a blended 137 bps over EURIBOR for a 58.7 per cent Note to Value ("NTV") and Goldman and CA-CIB's cold storage securitisation pricing at 184 bps over LIBOR for a 65.2 per cent NTV.

For other types of alternate lenders there have been a mixed bag of results. Lendy, a peer to peer lender making small property loans was put into administration in May after issues on its loan book including a reported 66 per cent of loans past due as of late 2018. Funding Circle, which makes small business loans, recently reported the

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tougher lending criteria it was imposing would halve its expected revenue growth for 2019. The FCA has increased regulation in the space with investors no longer be able to put more than 10 per cent of their investable assets into peer to peer lending and another part of the new rules is the introduction of an appropriateness test for investors that considers a client's knowledge and experience of peer to peer lending. In better news, Lendinvest which provides a variety of property finance has successfully completed its first securitisation. We have also seen varied fortunes for the challenger banks. Oaknorth appears to be doing well having grown its total loan book 160 per cent in a year to £2.2 billion and with new commercial development loans as large as £60 million reported. Meanwhile fellow challenger bank Metro has had issues with its loan book having announced it had been miscategorising the risk-weightings for a large numbers of its loans when working out how much capital it needed to protect against losses, which has led to reports of weakened investor and customer confidence and a new capital raise in May.

On the UK residential side, London peaked in 2014 and according to Savills as a whole the prime central London market has fallen 19.4 per cent in sterling terms between June 2014 and the end of the first quarter of 2019. The second quarter saw a return to positive house price appreciation in London with the Nationwide reporting a 0.6 per cent quarter on quarter growth in the second quarter of 2019. Across the market as a whole, the number of surveyors reporting rises in the amount of new enquiries and new instructions both increased significantly in May. This has reversed a downward trend seen since the summer of last year. Both metrics are still negative meaning that the majority of surveyors are still reporting falling numbers of enquiries and instructions but with a smaller majority this month. For the parts of the market that attract high proportions of international buyers the continued devaluation of sterling means that foreign buyers denominated in USD, EUR and RMB currencies are viewing the all-in discount from peak as especially attractive in their domestic currency basis.

As we have commented in recent factsheets, the market for UK retail debt is yet to settle. According to Property Week the market will be tested with two of the largest and highest quality retail assets in the UK a refinancing of the £750 million Westfield Stratford CMBS coming due in November this year and Intu reported to be looking at a refinancing of £1 billion of debt secured by the Trafford Centre. It will be an interesting test of sentiment to the sector to follow the progress of the refinancing of these very high profile assets over the coming months.

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