

S&PCORRECT: Ratings On Japan Real Estate Investment Lowered To 'A+/A-1'; Outlook Stable

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(Editor's Note: In the media release published on March 26, 2012, the as-of date for JRE's property portfolio was misstated. A corrected version follows.)

OVERVIEW

- JRE is a listed J-REIT that focuses on investments in office buildings.
- JRE's profitability measures remain weak amid lackluster conditions in the office leasing market, and its ratio of debt to total assets remains moderately high. Accordingly, we expect that the J-REIT may experience delays in restoring its conservative financial profile.
- We have lowered to 'A+' our long-term corporate credit and unsecured debt ratings and to 'A-1' our short-term credit rating on JRE.
- The outlook on the long-term corporate credit rating is stable, reflecting our view that JRE is likely to generate mostly stable cash flows, backed by its strong business position and high-quality real estate portfolio.

TOKYO (Standard & Poor's) March 26, 2012--Standard & Poor's Ratings Services today said that it has lowered to 'A+' from 'AA-' its long-term corporate credit and unsecured debt ratings, and to 'A-1' from 'A-1+' its short-term credit rating, on Japan Real Estate Investment Corp. (JRE). The outlook on the long-term corporate credit rating on JRE is stable. Prior to this action, we had maintained a negative outlook on the long-term rating on JRE.

We today lowered our ratings on JRE, a Japanese REIT (J-REIT), based on the following factors:

- JRE's profitability measures remain weak amid lackluster conditions in the office leasing market; its debt-to-total assets ratio has been hovering at levels that are moderately high compared with the target range set under its conservative financial policy as well as levels before the onset of the financial crisis in 2008; and its financial indicators are relatively weak.
- JRE has said that it will continue to actively pursue external growth to increase its cash flow, while ensuring that its financial profile remains under control. As JRE pursues external growth, we believe that the J-REIT may experience delays in restoring its conservative financial profile.
- The portfolio's unrealized gain has decreased, thereby weakening JRE's financial buffer.

JRE has said that it intends to pursue a conservative financial policy, maintaining its ratio of debt to total assets at between 30% and 40%. However, as of the end of its 20th six-month fiscal term (ended Sept. 30, 2011), JRE's ratio of debt to total assets, which has remained relatively high in recent years, stood at about 41.8%, and its debt-to-capital ratio [interest-bearing debt including hoshokin liabilities/(interest-bearing debt including hoshokin liabilities + total net assets), as defined by Standard & Poor's] was about 44.7%. Moreover, JRE's acquisition of Akasaka Park Building (Minato Ward, Tokyo; purchase price: ¥60.8 billion) in November 2011 raised the J-REIT's ratio of debt to total assets to about 46%. We expect the ratio to decline to about 40% because, in addition to an equity offering it launched in February 2012, JRE will conduct an equity offering in late March 2012 with a greenshoe option that enables it to issue more investment units (equity shares) than that specified in its original public offering plan. Nevertheless, the debt-to-total assets ratio is still high compared with previous levels. Meanwhile, although the portfolio's average occupancy rate is improving, declining rent levels continue to constrain JRE's rental revenue, and the J-REIT's profitability measures are relatively weak.

JRE believes that real estate market prices are nearing the bottom, and thus intends to shift the focus of its operations to external growth to increase its cash flow, while ensuring that its financial profile remains under control. As JRE pursues external growth, we believe that the J-REIT may experience delays in restoring its conservative financial profile. Furthermore, the unrealized gain (the difference between the appraisal value and the book value of the portfolio at the end of a fiscal term) on JRE's portfolio has decreased to about 1.9% as of Sept. 30, 2011, far below the levels seen when real estate market conditions were favorable. Nevertheless, the rate of the decrease in unrealized gains has moderated.

JRE's ratings are underpinned by its strong business position in the J-REIT market and high market recognition, backed by the strong brand recognition and credit quality of its sponsors, Mitsubishi Estate Co. Ltd. (A+/Stable/A-1), The Dai-ichi Life Insurance Co. Ltd. (A/Negative/--), and Mitsui & Co. Ltd.

(A+/Stable /A-1), as well as its mostly stable cash flow from its high-quality portfolio. JRE boasts the second largest asset portfolio among the listed J-REITs that focus on investments in office buildings. As of Feb. 29, 2012, JRE owned a portfolio of 57 office properties throughout Japan, located mainly in the 23 wards of Tokyo, worth about ¥718.7 billion based on total purchase price. The diversification and competitiveness of its portfolio have improved as a result of its recent acquisitions. The J-REIT maintains good relationships with multiple financial institutions and high financial flexibility. It increased its total amount of committed credit lines in the 20th fiscal term.

The outlook on the long-term corporate credit rating on JRE is stable. We may raise our ratings on JRE if the J-REIT's profitability measures recover, its debt-to-total assets ratio declines to around 35%, and prospects for clear improvement in its financial indicators emerge as it pursues external growth. On the other hand, we may consider lowering the ratings on JRE again if the J-REIT's profitability measures and financial indicators worsen.

RELATED CRITERIA AND RESEARCH

"Global Criteria For Rating Real Estate Companies," June 21, 2011

"Principles Of Credit Ratings," Feb. 16, 2011

"Rating Policy For Japanese Real Estate Investment Trusts," May 9, 2001

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