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Ratings On Japan Prime Realty Investment Affirmed At 'A/A-1', Off CreditWatch Negative; Outlook Stable

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OVERVIEW

- On March 5, 2012, we placed the ratings on JPR on CreditWatch negative. The rating actions followed JPR's announcement that it planned to acquire the Otemachi 1-6 Plan land with leasehold interest entirely with debt.
- JPR's debt-to-capital ratio rose as a result of the acquisition. However, its debt-to-capital ratio has declined since then to the level prior to the acquisition because the J-REIT conducted an equity offering and used the proceeds to repay some of its debt.
- We have affirmed our 'A' long-term corporate credit and unsecured debt ratings and our 'A-1' short-term credit rating on JPR and removed all ratings from CreditWatch negative.
- The outlook on the long-term corporate credit rating is stable, given that we expect JPR to generate generally steady cash flows without large volatility.

TOKYO (Standard & Poor's) Aug. 1, 2012--Standard & Poor's Ratings Services today said that it has affirmed its 'A' long-term corporate credit and unsecured debt ratings and its 'A-1' short-term credit rating on Japan Prime Realty Investment Corp. (JPR), and removed all ratings from CreditWatch with negative implications. We initially placed the ratings on CreditWatch with negative implications on March 5, 2012, and then maintained our CreditWatch negative placements on May 31, 2012. The outlook on the long-term corporate credit rating is stable.

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On Feb. 29, 2012, JPR announced that it would acquire the Otemachi 1-6 Plan (tentative name; Chiyoda Ward, Tokyo; purchase price: ¥36.0 billion) land with leasehold interest ("sokochi") entirely with interest-bearing debt. We therefore took the view that JPR's 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] would rise as a result of the acquisition. Accordingly, on March 5, 2012, we placed the long- and short-term corporate credit ratings and unsecured debt ratings on JPR on CreditWatch negative to reflect this view. The Japanese REIT (J-REIT) then acquired the Otemachi 1-6 Plan land on March 13, 2012.

JPR's debt-financed purchase of the Otemachi 1-6 Plan land with leasehold interest raised its debt-to-capital ratio to about 53%. However, the debt-to-capital ratio has declined since then because the J-REIT conducted an equity offering in July 2012 and used the proceeds to repay some of its debt in the following month. The offering has enabled the J-REIT to bring its ratio back down to about 48%, the level prior to its acquisition of the Otemachi 1-6 Plan land. In addition, we expect JPR's ratio of funds from operations (FFO) to debt to improve and hover between 7.0% and 8.0%, along with a decrease in its debt-to-capital ratio, over the next one to two years.

The property is located in Tokyo's central business district of Otemachi--the leading office district in Japan. Thus the property benefits from its scarcity value, given its prime location. However, this property is land with leasehold interest in a high-rise office complex to be completed in April 2014. In addition, this is the portfolio's largest property, based on purchase price, and JPR's cash flow will partly rely on land rental revenue from the property, which is under construction. Meanwhile, JPR undertook some measures to increase the likelihood that it receives timely land rent payments until the completion of the office complex.

The yield on the Otemachi 1-6 Plan land with leasehold interest is low, reflecting its scarcity value. Accordingly, the overall yield on JPR's portfolio has also declined. However, JPR has announced that it will also use the proceeds from the July 2012 equity offering to acquire Yakuin Business Garden (Fukuoka City, Fukuoka Prefecture; purchase price: about ¥11.0 billion). We expect this property to bolster the J-REIT's profitability to an extent because its yield is relatively high compared with the average yield on JPR's portfolio. Amid continued difficult conditions in Japan's leasing market, the rent levels at JPR's properties have been low. However, we expect JPR's relatively strong market position and cash flows generated from its high-quality portfolio to underpin to an extent the J-REIT's credit quality for the time being.

JPR has secured a leading position in the J-REIT market, backed by the real estate management and development capabilities of its sponsors, including Tokyo Tatemono Co. Ltd. (NR), Taisei Corp. (NR), and Meiji Yasuda Life Insurance Co. (A/Stable/A-1).

The outlook on JPR is stable. We expect JPR to generate generally stable cash flow without large volatility. To raise the ratings on JPR, we would need to see the J-REIT improve the quality and stability of its portfolio, its profitability, and its financial standing. However, we see little likelihood of upgrading JPR because business conditions for J-REITs remain challenging. On the other hand, the ratings on JPR may come under downward pressure amid the delayed recovery of the office leasing market if the J-REIT fails to maintain a clear recovery in its financial base, such as if its debt-to-capital ratio rises and remains above 50% due to such factors as its recent, relatively aggressive stance toward acquisitions. The ratings would also be constrained if the J-REIT fails to improve its profitability measures and interest coverage indicators. We would consider this to be the case if, for example, JPR's ratio of FFO to debt fell to and remained below 7%.

RELATED CRITERIA AND RESEARCH

"Key Credit Factors: 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

RATINGS LIST

Ratings Affirmed, Off CreditWatch Negative

Japan Prime Realty Investment Corp.

	To	From
Corporate credit rating	A/Stable/A-1	A/Watch Neg/A-1
J-REIT bonds*	A	A/Watch Neg

*The above 'A' rating on JPR's J-REIT bonds refers to its series three, six, seven, nine, and 11 to 14 J-REIT bonds (¥42.5 billion in total).

A Japanese-language version of this media release is available on Standard & Poor's Research Online at www.researchonline.jp, or via CreditWire Japan on Bloomberg Professional at SPCJ <GO>. Complete ratings information is available to RatingsDirect subscribers on the Global Credit Portal at www.globalcreditportal.com and RatingsDirect subscribers at www.ratingsdirect.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.