19-D-0165
May 29, 2019

Highlights of Major Real Estate Companies' Financial Results for Fiscal Year Ended March 2019

The following are Japan Credit Rating Agency, Ltd. (JCR)'s perception of the current status and highlights for rating concerning the financial results for the fiscal year ended March 2019 (FY2018) and earnings forecasts for FY2019 of Japan's 5 major real estate companies: Nomura Real Estate Holdings, Inc. ("NREH"), Tokyu Fudosan Holdings Corporation ("TFHD"), Mitsui Fudosan Co., Ltd. ("MFC"), Mitsubishi Estate Co., Ltd. ("MEC") and Sumitomo Realty & Development Co., Ltd. ("SRD").

1. Industry Trend

The office building market has been firm in central part of Tokyo. The average vacancy rate in Tokyo's business districts (Chiyoda, Chuo, Minato, Shinjuku and Shibuya wards), which stood at 1.70% as of April 30, 2019, has been below 2.0% for 6 months in a row and been consistently declining since it peaked out at 9.43% as of June 30, 2012. Moreover, the average rent has significantly increased from the bottom amount of 16,207 yen per *tsubo* (approximately 3.3 square meters) as of December 31, 2013 to 21,279 yen per *tsubo* as of April 30, 2019. The new office building supply in 2018 was larger than the annual average in the past, but the supply-demand balance remained at a good level thanks to the needs for expansion of floor space along with good corporate performance and enhancement of strategies for offices to secure enough human resources. According to the Survey of Large-scale Office Building Market in Tokyo's 23 Ward 2019 conducted by Mori Building Co., Ltd. (released on April 16, 2019), the new supply volume in 2018 was 1.41 million square meters, exceeding the annual average of 1.03 million square meters in the past. While the supply volume for 2019 is forecast to decline to 0.99 million square meters in 2019, it is forecast to far exceed the annual average in the past in 2020, reaching as much as 1.72 million square meters. It is necessary to note that uncertainty about the future business sentiment as well as the increasing supply is growing. As the office demand in central part of Tokyo is considered firm, however, JCR sees that deterioration of the supply-demand balance will remain less likely for the time being.

The number of condominium units sold in Tokyo metropolitan area has been at a low level. A survey by Real Estate Economic Institute Co., Ltd. ("REEI") shows that the number in 2018 increased 3.4% year-on-year to 37.1 thousand units. Although the number increased for 2 years in a row over the previous year, the number is in the range of 30 to 40 thousand units. The passing of the increasing and remaining high construction cost on to the selling price as well as the rising land prices is considered as the primary factor for the low number. While there are properties in Tokyo's 23 wards that are achieving strong sales, growth in the contract rate is slowing down mainly in suburban areas such as Saitama and Chiba prefectures. In 2018, there was only once (3 times in 2017) where the first-month contract rate for condominiums in the greater Tokyo metropolitan area exceeded 70%, which is considered as an indication of good performance, and there have been no significant changes to this situation in 2019. REEI projects the sales volume for 2019 to be 37.0 thousand units, roughly flat from 2018, having an opinion that redevelopment projects in Tokyo's 23 wards and the neighboring area will lead the demand.

2. Financial Results

The total operating income of the 5 companies for FY2018 increased 6.4% year-on-year to 870.9 billion yen, increasing 7 years in a row and posting the record-high income for 4 years in a row. By segment, all segments including real estate leasing, real estate development & sales, and other increased the income.

Looking at the individual companies, all increased their operating income. In particular, SRD achieved the record for 6 years, MFC for 5 years, and MEC for 3 years in a row. Although NREH and TFHD failed to obtain their record-high income, they achieved an amount close to their record levels.

Their financial structure has also been improving backed by the good business environment. As of the end of FY2018, the combined equity ratio of the 5 companies improved to 29.5% from 28.4% and the D/E ratio improved to 1.66x from 1.77x a year before. Their equity capital further increased thanks to contributions from capital increase by public offering and hybrid financing as well as net income accumulation. Moreover, their total unrealized gains on leasing and other real estate properties grew to 9.8 trillion yen as of the end of FY2018 from 8.6 trillion yen a year earlier, resulting in a larger financial buffer. Although their total free cash flow remains in the red, the deficit level has significantly declined thanks to the increased operating cash flow.

Both the equity ratio and D/E ratio improved for NREH, TFHD, MEC and SRD. NREH increased these ratios partly through hybrid financing, while TFHD increased them partly through capital increase by public offering. Meanwhile, MFC slightly worsened both equity ratio and D/E ratio.

3. Highlights for Rating

Both the total net sales and operating income of the 5 companies for FY2019 are expected to increase for 8 years in a row, up 5.8% and 2.5% year-on-year to 6.03 trillion yen and 892.5 billion yen, respectively. By segment, both the real estate leasing and real estate development & sales are expected to increase the income. For the individual companies, all 5 companies will increase their operating income. SRD will likely mark a record high for the 7th straight year, MFC for the 6th straight year and MEC for the 4th straight year. Although NREH and TFHD expect their operating income to be short of their records, but still expect a level that is almost equal to them. While NREH forecasts its operating income for FY2019 to reach 79.5 billion yen (peak operating income: 80.9 billion yen), TFHD forecasts it to reach 82 billion yen (peak operating income: 82.1 billion yen).

The above estimates released by the individual companies remain largely unchanged from those over the past several years. Given factors including strong demand for office buildings, JCR sees that the earnings level will stay high and is not likely to fall in the short term.

Meanwhile, JCR will continue to pay attention to trend of financial structure, because there are noticeable moves by them in overseas investments, while also investing in urban redevelopment and other domestic projects. JCR sees at this point, however, that they will maintain the conservative financial management policy and thus such investments will not significantly weaken the financial structure.

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(Chart 1) Financial Data of Major Real Estate Companies

(JPY 100 mn, %, times)

	Nomura Real Estate Holdings (3231)				Tokyu Fudosan Holdings (3289)				Mitsui Fudosan (8801)			
	A/Stable				A/Stable				AA/Stable			
	FY2016 (Actual)	FY2017 (Actual)	FY2018 (Actual)	FY2019 (Est.)	FY2016 (Actual)	FY2017 (Actual)	FY2018 (Actual)	FY2019 (Est.)	FY2016 (Actual)	FY2017 (Actual)	FY2018 (Actual)	FY2019 (Est.)
Net Sales	5,696	6,237	6,685	7,390	8,085	8,661	9,018	9,200	17,044	17,511	18,611	20,000
Operating Income	772	766	791	795	732	775	802	820	2,326	2,459	2,621	2,670
(Profit Margin)	13.6	12.3	11.8	10.8	9.1	8.9	8.9	8.9	13.6	14.0	14.1	13.4
Ordinary Income	689	680	693	700	636	686	707	710	2,196	2,403	2,541	2,460
(Profit Margin)	12.1	10.9	10.4	9.5	7.9	7.9	7.8	7.7	12.9	13.7	13.7	12.3
Net Income*	470	460	458	460	315	351	374	390	1,318	1,558	1,686	1,700
(Profit Margin)	8.3	7.4	6.9	6.2	3.9	4.1	4.1	4.2	7.7	8.9	9.1	8.5
EBITDA	944	956	984		1,023	1,067	1,110		3,096	3,221	3,483	
(vs. Net Sales)	16.6	15.3	14.7		12.7	12.3	12.3		18.2	18.4	18.7	
Operating Cash Flow	-318	214	899		689	122	445		2,274	301	2,167	
Investing Cash Flow	-545	-516	-466		-709	-964	-603		-2,015	-3,654	-3,888	
Fee Cash Flow	-863	-302	433		-20	-842	-158		259	-3,353	-1,721	
Financing Cash Flow	765	437	137		230	824	1,390		150	2,891	2,312	
Total Assets	15,930	16,736	17,594		20,671	21,767	24,052		55,707	63,012	68,027	
Equity Capital	4,813	5,264	5,792		4,423	4,681	5,614		19,846	22,048	23,425	
Interest-bearing Debt	8,114	8,543	8,615		11,514	12,241	12,898		23,019	26,186	29,066	
Interest-bearing Debt/EBITDA	8.60	8.94	8.76		11.26	11.47	11.62		7.44	8.13	8.35	
D/E Ratio	1.69	1.62	1.49		2.60	2.62	2.30		1.16	1.19	1.24	
Equity Ratio	30.2	31.5	32.9		21.4	21.5	23.3		35.6	35.0	34.4	

	Mitsubishi Estate (8802)				Sumitomo Realty & Development (8830)				Total			
	AA+p/Stable				A+/Stable							
	FY2016 (Actual)	FY2017 (Actual)	FY2018 (Actual)	FY2019 (Est.)	FY2016 (Actual)	FY2017 (Actual)	FY2018 (Actual)	FY2019 (Est.)	FY2016 (Actual)	FY2017 (Actual)	FY2018 (Actual)	FY2019 (Est.)
Net Sales	11,254	11,940	12,632	13,600	9,251	9,484	10,132	10,200	51,330	53,833	57,078	60,390
Operating Income	1,924	2,130	2,291	2,300	1,881	2,056	2,204	2,340	7,635	8,186	8,709	8,925
(Profit Margin)	17.1	17.8	18.1	16.9	20.3	21.7	21.8	22.9	14.9	15.2	15.3	14.8
Ordinary Income	1,698	1,905	2,065	2,070	1,676	1,868	2,042	2,200	6,895	7,542	8,048	8,140
(Profit Margin)	15.1	16.0	16.3	15.2	18.1	19.7	20.2	21.6	13.4	14.0	14.1	13.5
Net Income*	1,026	1,204	1,346	1,370	1,034	1,197	1,308	1,400	4,163	4,770	5,172	5,320
(Profit Margin)	9.1	10.1	10.7	10.1	11.2	12.6	12.9	13.7	8.1	8.9	9.1	8.8
EBITDA	2,788	3,020	3,170		2,343	2,557	2,767		10,194	10,821	11,514	
(vs. Net Sales)	24.8	25.3	25.1		25.3	27.0	27.3		19.9	20.1	20.2	
Operating Cash Flow	1,685	2,933	3,459		1,585	1,899	2,600		5,915	5,469	9,570	
Investing Cash Flow	-3,272	-2,868	-2,710		-2,741	-2,205	-2,092		-9,282	-10,207	-9,759	
Fee Cash Flow	-1,587	65	749		-1,156	-306	508		-3,367	-4,738	-189	
Financing Cash Flow	-49	372	-1,924		1,979	264	-1,460		3,075	4,788	455	
Total Assets	54,841	58,036	57,741		49,800	51,869	51,274		196,949	211,420	218,688	
Equity Capital	15,927	16,983	17,706		10,073	11,149	12,081		55,082	60,125	64,618	
Interest-bearing Debt	23,969	24,816	23,150		33,745	34,735	33,427		100,361	106,521	107,156	
Interest-bearing Debt/EBITDA	8.60	8.22	7.30		14.40	13.58	12.08		9.85	9.84	9.31	
D/E Ratio	1.50	1.46	1.31		3.35	3.12	2.77		1.82	1.77	1.66	
Equity Ratio	29.0	29.3	30.7		20.2	21.5	23.6		28.0	28.4	29.5	

(Source: Prepared by JCR based on financial materials of above companies)

Notes

*Net income attributable to owners of parent

1: Estimates are taken from each company's announcement.

2: Figures for NREH are after consideration of equity content of the subordinated bonds from FY2017.

<Reference>

Issuer: Nomura Real Estate Holdings, Inc.

Long-term Issuer Rating: A Outlook: Stable

Issuer: Tokyu Fudosan Holdings Corporation

Long-term Issuer Rating: A Outlook: Stable

Issuer: Mitsui Fudosan Co., Ltd.

Long-term Issuer Rating: AA Outlook: Stable

Issuer: Mitsubishi Estate Co., Ltd.

Long-term Issuer Rating: AA+p Outlook: Stable

Issuer: Sumitomo Realty & Development Co., Ltd.

Long-term Issuer Rating: A+ Outlook: Stable

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