16-D-0137
May 30, 2016

Highlights of Major Real Estate Companies' Financial Results for Fiscal Year Ended March 2016

The following is Japan Credit Rating Agency, Ltd. (JCR)'s perception of the current state and highlights for rating concerning the financial results for the fiscal year ended March 2016 (FY2015) and earnings forecasts for FY2016 of the five major real estate companies (the "Five Companies"): Nomura Real Estate Holdings, Inc., Tokyu Fudosan Holdings Corporation, Mitsui Fudosan Co., Ltd., Mitsubishi Estate Company, Limited, and Sumitomo Realty & Development Co., Ltd.

1. Industry Trend

Office building leasing is in a firm business situation. The average vacancy rate of buildings located in Tokyo's business district (Chiyoda, Chuo, Minato, Shinjuku and Shibuya wards) was 4.23% as of April 30, 2016, according to statistics by Miki Shoji Co., Ltd. The rate is somewhat higher than the most recent bottom of 4.01% as of January 31, 2016, but the general trend is in a downward direction from a peak of 9.43% as of June 30, 2012. Meanwhile, rent turned around to increase in 2014. The average rent in Tokyo's business district has been steadily increasing from a bottom of 16,207 yen per tsubo (3.3 square meters) as of December 31, 2013 to reach 18,061 yen per tsubo as of April 30, 2016. New office supply volume in Tokyo's 23 wards is expected to be 1,020,000 square meters in 2016, down 6% from the previous year and falling below the past annual average of 1,030,000 square meters, according to "Market Trend Survey of Large-Scale Office Buildings in Tokyo's 23 Wards (Bulletin Report)" released by Mori Building Co., Ltd. on April 21, 2016. The supply is forecast to further drop to 690,000 square meters in 2017. Even with the increasingly unclear outlook for corporate performance affected by the Chinese economy slowdown and the trend for a stronger yen, demands for office buildings are solid as companies are working to consolidate/ streamline their head office function and also becoming more conscious about BCP. JCR sees it less likely that the office building supply-demand balance will deteriorate in the near future. Yet, it should be noted that the supply volume is expected to increase in and after 2018. The Mori Building survey says the volume is estimated to be 1,390,000 square meters in 2018, 1,240,000 square meters in 2019 and 1,370,000 square meters in 2020. It is not that these figures represent a net increase in supply, because they are accounted for somewhat largely by the replacement buildings mainly in the three central Tokyo wards of Chiyoda, Chuo and Minato, but JCR will keep closely watching the changes in the medium-term supply-demand balance.

Condominium unit sales in the Tokyo metropolitan area is on the decrease. The number fell for the second straight year to 40,400 units in 2015, down 9.9% year-on-year, according to a survey by Real Estate Economic Institute Co., LTD. The decline is mainly attributed to the fact that increasing construction costs, etc. were passed on to selling prices. The contracted rate is decreasing mainly in suburbs such as Saitama and Chiba prefectures but sales are brisk for properties located in central Tokyo, superhigh-rise condominiums in the bay area, and large-scale ones in redevelopment projects. As for the rate of condominium units contracted in a month against the total number newly supplied in the same month, 70% is regarded as a healthy level. Having been at around 70% from January to August in 2015, the rate often falls below the level since September. The number of yet-to-be contracted units is increasing to reach 5,881 as of April 30, 2016 from a bottom of 3,426 as of August 31, 2014, becoming a cause of concern. Real Estate Economic Institute's statistics show the sales of condominiums located in the metropolitan area are expected to rise 6.3% to 43,000 units in 2016, led by large-scale properties in Tokyo. The forecast, which is also based on possible rush demands before the planned consumption tax hike mainly for properties located in suburbs, will probably not be achieved if the tax hike will be postponed. As such, the trend for demands will likely remain uncertain.

2. Financial Results

In FY2015, the Five Companies' combined operating income rose for the fourth straight year to 692.6 billion yen, up 7.6% year-on-year, and topped FY2007's 663.8 billion yen to hit a new record high. Their combined EBITDA renewed the record high in three consecutive years at 852.5 billion yen in FY2013, 871.7 billion yen in FY2014 and 933.8 billion yen in FY2015. As factors behind, in addition to the increasing operating income, depreciation costs are on the rise due mainly to an increase in redevelopment projects.

Each of the five companies achieved higher operating income in FY2015. Sumitomo Realty & Development and Mitsui Fudosan posted the record-high profit for the third straight year and second straight year, respectively, while Nomura Real Estate Holdings renewed the highest profit recorded in FY2013. All the five achieved operating income growth for the leasing business segment. Sales segment's operating income rose at Tokyu Fudosan Holdings, Mitsubishi Estate and Sumitomo Realty & Development but fell at Nomura Real Estate Holdings and Mitsui Fudosan, affected by a decline in the number of units.

Their financial condition turned around to worsen. The combined equity capital ratio fell to 27.5% as of March 31, 2016 from 28.0% a year earlier, while the D/E ratio rose to 1.83 from 1.75, both the first worsening since FY2012. Their equity capital is growing, pushed up by accumulating net incomes. All the five saw their assets' unrealized gains increase in the solid real estate market, helped by the improved cash flow of existing properties and contribution of newly completed properties. Their combined unrealized gains totaled 6.4 trillion yen as of March 31, 2016, compared with the most recent bottom of 3.8 trillion yen as of March 31, 2012, indicating that the financial buffer is becoming even stronger. On the other hand, their interest-bearing debts increased for the second straight year due mainly to expanding investments. Their free cash flow, after having been positive for the five years until FY2013, entered the negative territory in FY2014 at more than 400 billion yen and remained negative at around 380 billion yen in FY2015.

Sumitomo Realty & Development and Tokyu Fudosan Holdings achieved an improvement in both equity capital ratio and D/E ratio, and Nomura Real Estate Holdings did so for the equity capital ratio. The both ratios worsened at Mitsui Fudosan and Mitsubishi Estate.

3. Highlights for Rating

The Five Companies' combined net sales are expected to be 5.16 trillion yen in FY2016, up 7.1% from FY2015, and operating income is forecast to be 722.0 billion yen, up 4.2%. Mitsui Fudosan, Sumitomo Realty & Development, Tokyu Fudosan Holdings and Mitsubishi Estate expect larger income, meaning that the first two will renew the record high again. Nomura Real Estate Holdings will likely suffer a decline in operating income with the absence of asset acquisition fees seen before related to a merger of REITs, but still, the income will be close to the record-high level.

The estimated figures released by each of the five companies were not surprising nor beyond the scope of the assumption, as JCR views. Their earnings will likely stay at a high level without turning around to worsen in the near future, JCR so assumes considering the solid external situation such as the office building market. As an unchanged important point for the rating in terms of earnings and cash flows, the Five Companies will need to continue to enhance the leasing business as a stable income source. They plan to supply new properties in large redevelopment projects mainly in Tokyo's wards, and JCR pays attention to whether they can increase the leasing segment's earning power by maintaining the occupancy rate and rent level.

Attention should be also paid to the financial structure. JCR particularly focuses on changes in free cash flow. During the past 10 years, their free cash flow was negative at nearly 400 billion yen in FY2006, more than 700 billion yen in FY2007 and more than 800 billion yen in FY2008, stayed in the positive territory in the following five years, and entered the negative territory in FY2014 at more than 400 billion yen and remained negative at around 380 billion yen in FY2015. Having experienced the Lehman Shock, the Five Companies stick to conservative financial policy in general, in JCR's view. JCR will carefully watch to confirm that their negative free cash flow will not become larger in and after FY2016 to worsen the financial condition.

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(Chart) Financial Data of Major Real Estate Companies

(Y100 mn, %, times)

Company	Nomura Real Estate Holdings (3231)				Tokyu Fudosan Holdings (3289)				Mitsui Fudosan (8801)			
Rating/Outlook	A/Stable				A-/Stable				AA/Stable			
FY ended	14/3 (result)	15/3 (result)	16/3 (result)	17/3 (forecast)	14/3 (result)	15/3 (result)	16/3 (result)	17/3 (forecast)	14/3 (result)	15/3 (result)	16/3 (result)	17/3 (forecast)
Net Sales	5,320	5,672	5,695	5,890	7,141	7,731	8,155	8,400	15,153	15,290	15,680	17,500
Operating Income	743	719	809	760	614	633	688	730	1,726	1,861	2,025	2,200
(Profit Margin)	14.0	12.7	14.2	12.9	8.6	8.2	8.4	8.7	11.4	12.2	12.9	12.6
Ordinary Income	641	637	727	670	506	517	564	610	1,446	1,634	1,825	1,980
(Profit Margin)	12.0	11.2	12.8	11.4	7.1	6.7	6.9	7.3	9.5	10.7	11.6	11.3
Net Income	268	384	472	430	237	252	287	315	768	1,002	1,177	1,250
(Profit Margin)	5.0	6.8	8.3	7.3	3.3	3.3	3.5	3.8	5.1	6.6	7.5	7.1
EBITDA	896	883	980		849	885	952		2,329	2,516	2,748	
(vs. Net Sale)	16.8	15.6	17.2		11.9	11.4	11.7		15.4	16.5	17.5	
Operating Cash Flow	835	238	133		▲ 135	▲ 385	879		1,899	303	322	
Investing Cash Flow	▲ 202	▲ 325	▲ 597		197	▲ 1,003	▲ 1,124		▲ 441	▲ 2,616	▲ 2,397	
Free Cash Flow	633	▲ 87	▲ 464		62	▲ 1,388	▲ 245		1,458	▲ 2,313	▲ 2,075	
Financial Cash Flow	▲ 579	▲ 90	536		30	1,392	▲ 305		▲ 1,237	2,215	2,011	
Total Assets	13,139	13,692	14,854		17,898	19,738	19,844		45,488	50,771	53,743	
Equity Capital	3,557	3,941	4,449		3,645	3,953	4,188		12,744	18,719	19,223	
Interest-bearing Debt	6,188	6,178	7,219		9,994	11,343	11,061		20,559	19,893	22,262	
Interest-bearing Debt/EBITDA	6.91	7.00	7.37		11.77	12.82	11.62		8.83	7.91	8.10	
D/E Ratio	1.74	1.57	1.62		2.74	2.87	2.64		1.61	1.06	1.16	
Equity Ratio	27.1	28.8	30.0		20.4	20.0	21.1		28.0	36.9	35.8	

Company	Mitsubishi Estate (8802)				Sumitomo Realty & Development (8830)				Total			
Rating/Outlook	AA+p/Stable				A+/Stable							
FY ended	14/3 (result)	15/3 (result)	16/3 (result)	17/3 (forecast)	14/3 (result)	15/3 (result)	16/3 (result)	17/3 (forecast)	14/3 (result)	15/3 (result)	16/3 (result)	17/3 (forecast)
Net Sales	10,753	11,103	10,094	11,020	7,803	8,068	8,550	8,800	46,170	47,864	48,174	51,610
Operating Income	1,613	1,563	1,662	1,750	1,605	1,659	1,742	1,780	6,301	6,435	6,926	7,220
(Profit Margin)	15.0	14.1	16.5	15.9	20.6	20.6	20.4	20.2	13.6	13.4	14.4	14.0
Ordinary Income	1,396	1,331	1,449	1,500	1,305	1,391	1,484	1,550	5,294	5,510	6,049	6,310
(Profit Margin)	13.0	12.0	14.4	13.6	16.7	17.2	17.4	17.6	11.5	11.5	12.6	12.2
Net Income	643	733	834	860	697	806	878	970	2,613	3,177	3,648	3,825
(Profit Margin)	6.0	6.6	8.3	7.8	8.9	10.0	10.3	11.0	5.7	6.6	7.6	7.4
EBITDA	2,448	2,386	2,514		2,004	2,047	2,144		8,526	8,717	9,338	
(vs. Net Sale)	22.8	21.5	24.9		25.7	25.4	25.1		18.5	18.2	19.4	
Operating Cash Flow	3,365	2,001	1,358		1,170	351	961		7,134	2,508	3,653	
Investing Cash Flow	▲ 1,335	▲ 466	▲ 2,310		▲ 2,954	▲ 2,209	▲ 1,054		▲ 4,735	▲ 6,619	▲ 7,482	
Free Cash Flow	2,030	1,535	▲ 952		▲ 1,784	▲ 1,858	▲ 93		2,399	▲ 4,111	▲ 3,829	
Financial Cash Flow	▲ 1,775	▲ 1,891	3,092		975	1,878	450		▲ 2,586	3,504	5,784	
Total Assets	47,654	49,015	53,118		42,204	45,238	46,759		166,383	178,454	188,318	
Equity Capital	13,291	14,958	15,097		7,229	8,475	8,881		40,466	50,046	51,838	
Interest-bearing Debt	19,730	19,294	22,842		28,801	30,857	31,589		85,272	87,565	94,973	
Interest-bearing Debt/EBITDA	8.06	8.09	9.09		14.37	15.07	14.73		10.00	10.05	10.17	
D/E Ratio	1.48	1.29	1.51		3.98	3.64	3.56		2.11	1.75	1.83	
Equity Ratio	27.9	30.5	28.4		17.1	18.7	19.0		24.3	28.0	27.5	

Source: financial statements of each company

Notes

1: Earnings forecasts are figures published by each company.

2: For Sumitomo Realty & Development, figures after consideration of equity content of the subordinated loan are used for FY ended 14/3 and 15/3.

<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 Company, Limited

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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