J-REIT Seminar (15)

Frontier Real Estate Investment (8964)
Characteristics･Valuations･Points to look at

September 13, 2016

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Characteristics

- Commercial/Retail Property Type Reit with 32 properties totaling Y288.8bn, on a purchase price basis, as of end August 2016, sponsored by Mitsui Fudosan (8801)
- Area diversification: Tokyo 5 wards 5.7%, Tokyo 23 wards (excluding 5 wards) 18.4% (together 24.1%), Other Tokyo 5.1%, Kanto 25.2%, Chubu/Kinki 26.9%,Others 18.8% (as of end Aug. 2016) It can be said as non-urban centric type retail reit. Properties includes those prefixed as Mitsui Outletpark and Mitsui Shopping Park LaLaport
- Conservative Portfolio and Balance Sheet Management: Fixed rent ratio is 99% of total rent revenues; LTV for the period ending June 2016 is 39.1%, and 42% as of end August. Hence, relatively high credit ratings; AA (JCR), AA-（R&I), A+(S&P)
- DPU for the latest period ending June was flat p.o.p, as it incurred capital loss of Y460mn from sale of Joyfultown Okayama (key tenant: Ito-Yokado) which had long been a concern, while posting Y320mn gains by drawing down retained earnings, which can be regarded as positive as it took advantage of current active real estate market.
- Recent external growth in 2016: Kojima x Bigcamera Naha for Y1.85bn, NOI 7.6% sourced from independent route, and LaLaport Shin-Misato, additional 50% co-ownership interest for Y15.1bn, NOI 5.0% sourced by sponsor.

Valuations

- Unit price: Y507,000 as of September 13, 2016
- Dividend Per Unit: Y9,500 (-2.0% p.o.p)
- Expected Dividend Yield: 3.75%, based on the company's forecast for 12/2016 annualized
- NAV multiple: 1.25x based on Y404,873 for the period ending June 2016
- Dividend Yield (E): Somewhat lower than J-REIT average of 3.53% estimated
- NAV multiple: Somewhat lower than J-REIT average of 1.3x estimated
- But 25% premium to appraisal based NAV

Points to look at

- In our estimate, dividend per unit would be stable at around Y9500 levels for the several periods to come perhaps, as the fixed rent ratio is 99% of total rent revenues; On the other hand, upside in dividend growth would be limited, in our opinion.
- Management recognitions on recent real estate market are appropriate in our opinion; i.e. 1) fewer quality properties in good locations coming on the market, 2) Intensifying competition to acquire properties, 3) Falling cap rates in major cities; growing polarization of urban and non-urban areas; We expect the management to avoid aggressive external growth and seek to capture appropriate property replacement opportunities.
- Concerns are somewhat weak personal consumption and in particular tenant appetite in non-urban markets
- Currently 2 properties are under rent revision discussion; 1) Ito-Yokado Higashi Yamato (4.0%), 2) QANAT Rakuhoku (2.9%); and TSUTAYA BOOKS TENJIN (1.9%) is subject to tenant change; figure in ( ) indicates share in total annual rent
- Conservative balance sheet policy is estimated to be positive in terms of demand related to BOJ purchase for now; however, in the medium- and long-term, appropriately higher financial leverage can be implemented to enhance dividend level, in our opinion.

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