

December 19, 2008

Ratings On Nippon Accommodations Fund Affirmed At 'A+/A-1'; Outlook Stable

Primary Credit Analyst:

Roko Izawa, Tokyo (81) 3-4550-8674; roko_izawa@standardandpoors.com

Secondary Credit Analyst:

Yumi Oikawa, Tokyo (81) 3-4550-8775; yumi_oikawa@standardandpoors.com

TOKYO (Standard & Poor's) Dec. 19, 2008--Standard & Poor's Ratings Services today affirmed its 'A+' long-term and 'A-1' short-term corporate credit ratings on Nippon Accommodations Fund Inc. (NAF). At the same time, Standard & Poor's affirmed its 'A+' long-term senior unsecured debt rating on NAF's ¥10 billion series 1 senior unsecured bond issuance. The outlook on the long-term corporate credit rating is stable.

The ratings reflect NAF's strong business position and moderately conservative financial profile. The company's real estate portfolio generates stable cash flow as it comprises residential properties that are in good locations, have a low average property age, and have good leasing conditions. NAF's operating strategy is to specialize in very high quality residential properties located mainly within the 23 wards of Tokyo, backed by the real estate development capabilities, real estate expertise, and brand recognition of the sponsor, Mitsui Fudosan Co. Ltd. (BBB+/Stable/A-2). NAF has a conservative capital structure and high financial flexibility. These strengths are partly offset by issues regarding property concentration risk in NAF's portfolio.

NAF is a Japanese real estate investment trust (J-REIT) that went public on the Tokyo Stock Exchange in August 2006. As of the end of its fifth six-month fiscal term (ended Aug. 31, 2008), NAF's portfolio featured 44 properties, consisting of 4,247 leasing units located mainly in the 23 wards of Tokyo, and had a total value of about ¥140 billion, based on purchase

price. The portfolio is diversified in terms of unit type, comprising single, family-type, and large leasing units, with a focus on comparatively high-demand compact units. The company has acquired a total of seven properties worth ¥16.8 billion in 2008, including Park Axis Nihonbashi Hamacho located in Chuo-ku, Tokyo, for ¥5.54 billion, and Park Cube Itabashi-honcho located in Itabashi-ku, Tokyo, for ¥4.17 billion. As the business environment surrounding the J-REIT market worsens further amid the dislocation in global and domestic financial and capital markets, NAF has adopted a selective asset acquisition strategy, using sponsor pipelines.

As part of its strategy, NAF limits its investments to residential properties. Activity in the residential property capital market has stagnated recently amid difficult conditions. Generally, however, Standard & Poor's considers residential properties to have more stable cash flows compared with other property types. This is generally due to high tenant diversification, relative ease in finding new tenants, and small fluctuations in rents during economic cycles. NAF's investment area is the metropolitan area of Tokyo and major ordinance-designated cities, with the company aiming to keep allocating more than 80% of its portfolio investments to properties located in the 23 wards of Tokyo. Currently, properties located within the 23 wards make up about 92% of the entire portfolio, which is in line with its investment policy.

The portfolio includes high-quality, competitive properties located in high-demand and convenient residential areas. The portfolio's occupancy rate at the end of the fifth fiscal term was 96.0 %, and contributes to the stability of cash flows. The weighted average property age of the portfolio is about 6.3 years as of Aug. 31, 2008, which is low. Moreover, the weighted average property age drops to about 2.7 years if the Okawabata Apartment communities, completed in 1988 and 1989, are excluded, since the majority of the other properties are very new.

The portfolio has asset concentration risk with the Okawabata Apartment communities comprising 21.2% of the total portfolio value. However, this risk is mitigated by such factors as good tenant diversification at the property, high occupancy rate, stable cash flows, and high competitiveness in the submarket. Asset concentration risk is expected to decline modestly over time, as NAF acquires more properties.

NAF aims to enlarge its portfolio by ¥300 billion, or by 10,000 residential units, by 2010-2011. However, the company is not focused solely on expanding its portfolio size, taking into consideration sluggish equity markets and uncertainty hanging over the real estate market. NAF's portfolio growth rate has been moderate thus far.

NAF's management expects to maintain the company's debt-to-capital ratio (interest-bearing debt/total assets) at an average of 40% to 50%, or at a maximum of 60%, which is a relatively conservative level. NAF recorded a debt-to-capital ratio (interest-bearing debt including security deposits/(interest-bearing debt + unitholders' capital) according to Standard & Poor's definition) of 56.4% at the end of its fifth six-month fiscal period, which was relatively high. Its debt-to-capital ratio may hover at levels higher than the cruising level until equity markets recover and may add pressure on NAF's credit quality. Any pressure, however, would be mitigated to some extent by: 1) the portfolio of high-quality residential properties for

rent with high occupancy rates that are generating stable cash flow; and 2) NAF's maintenance of ample liquidity at hand and good relations with multiple financial institutions.

Given that its leverage is relatively high, NAF intends to adopt a cautious and selective property acquisition strategy by using its sponsor's warehousing function.

As of the end of the fifth six-month fiscal period, all of NAF's long-term debt obligations carry fixed interest rates, and its debt repayment schedule is diversified through 2014. The company's EBITDA interest coverage is about 5x and its ratio of funds from operations (FFO) to total debt stands at 6.1%, both of which are lower than the previous period, reflecting relatively higher leverage. Regarding the portfolio's profitability, return on assets (ROA) stood at about 4.4%. On the other hand, the EBITDA margin (EBITDA/real estate rental revenue) is high at about 68%.

NAF currently has relatively good liquidity, with long- and short-term credit available to meet the company's near-term debt maturities, as well as to expand its portfolio. NAF's financial flexibility is considered high, reflecting its established relationships with several major financial institutions, from which it borrows on an unsecured basis.

NAF's portfolio of high-quality assets should generate stable income despite the aforesaid asset concentration and the difficult business environment. With the support of its sponsor, we expect NAF to maintain the high quality of its assets and a relatively conservative financial profile. In light of a relatively higher debt-to-capital ratio, Standard & Poor's will pay particular attention to the ratio, the company's cash flow protection, as well as its profitability.

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>.

Copyright © 2008 Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P). S&P and/or its third party licensors have exclusive proprietary rights in the data or information provided herein. This data/information may only be used internally for business purposes and shall not be used for any unlawful or unauthorized purposes. Dissemination, distribution or reproduction of this data/information in any form is strictly prohibited except with the prior written permission of S&P. Because of the possibility of human or mechanical error by S&P, its affiliates or its third party licensors, S&P, its affiliates and its third party licensors do not guarantee the accuracy, adequacy, completeness or availability of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. S&P GIVES NO EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE. In no event shall S&P, its affiliates and its third party licensors be liable for any direct, indirect, special or consequential damages in connection with subscriber's or others use of the data/information contained herein. Access to the data or information contained herein is subject to termination in the event any agreement with a third-party of information or software is terminated.

Analytic services provided by Standard & Poor's Ratings Services (Ratings Services) are the result of separate activities designed to preserve the independence and objectivity of ratings opinions. The credit ratings and observations contained herein are solely statements of opinion and not statements of fact or recommendations to purchase, hold, or sell any securities or make any other investment decisions. Accordingly, any user of the information contained herein should not rely on any credit rating or other opinion contained herein in making any investment decision. Ratings are based on information received by Ratings Services. Other divisions of Standard & Poor's may have information that is not available to Ratings Services. Standard & Poor's has established policies and procedures to maintain the confidentiality of non-public information received during the ratings process.

Ratings Services receives compensation for its ratings. Such compensation is normally paid either by the issuers of such securities or third parties participating in marketing the securities. While Standard & Poor's reserves the right to disseminate the rating, it receives no payment for doing so, except for subscriptions to its publications. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

Any Passwords/user IDs issued by S&P to users are single user-dedicated and may ONLY be used by the individual to whom they have been assigned. No sharing of passwords/user IDs and no simultaneous access via the same password/user ID is permitted. To reprint, translate, or use the data or information other than as provided herein, contact Client Services, 55 Water Street, New York, NY 10041; (1)212.438.9823 or by e-mail to: research_request@standardandpoors.com.