



NEWS RELEASE

Dec 16, 2010

R&I Affirms A-, Stable: Japan Hotel and Resort, Inc.

Rating and Investment Information, Inc. (R&I) has announced the following.

ISSUER: Japan Hotel and Resort, Inc. (Sec. Code: 8981)
Issuer Rating

R&I RATING: A- (Affirmed)

RATING OUTLOOK: Stable

RATIONALE:

Japan Hotel and Resort, Inc. (JHR) is a real estate investment trust (J-REIT) which was listed on the stock exchange in February 2006. It specializes in hotels and is sponsored by the Goldman Sachs Group.

JHR has a policy of investing in highly competitive hotels that are located in major cities throughout Japan and are superior in both hard (e.g. locations, building and facilities specifications) and soft (e.g. the hotel operator's capabilities) aspects. As of the end of November 2010, it owns eight properties with the total acquisition value of 85.1 billion yen.

In the term ending August 2010, operating revenues and net income grew approximately 4% and 6%, respectively, from the previous term. While total annual revenues of the five hotels with variable rents were slightly lower than the previous term's level, their profit levels rose driven by cost-cutting efforts. As a result, JHR's variable rent revenues also rose approximately 15%. For the term ending August 2011, JHR forecasts that operating revenues will be almost flat and net income will increase approximately 14% compared with the previous term due partly to lower financial expenses.

JHR's profit and cash flow levels appear to have bottomed, and in general, occupancy rates are recovering. Furthermore, its five major hotels maintain strong competitiveness and brand power in their respective markets, and profit margins are improving thanks to management efforts. Meanwhile, a recovery in revenue per available room is slow. This, combined with the effects of new competitors' entry, will likely hinder a rapid recovery of JHR's operating performance.

The amendment to the articles of incorporation in September 2010 has enabled JHR to employ a management contract scheme in addition to the existing lease scheme. In general, the volatility of hotel performance is reflected in the revenues of the hotel owner (REIT) more directly under the management contract scheme compared with the lease scheme. This will increase the risk of cash flow fluctuations. In light of such characteristics, JHR will carefully consider using the management contract scheme so that it will not have a material impact on overall cash flow.

At present, JHR owns only eight properties, of which five account for over 90% of the total acquisition value. It will be essential for JHR to resume the acquisition of new properties promptly so as to mitigate concentration risk and improve profitability of its asset portfolio.

The ratio of debt to total assets remains low, standing at 41.6% as of the end of August 2010. Although additional acquisition of properties may raise the debt ratio going forward, JHR intends to keep the ratio at no higher than 50%.

A loan worth 19 billion yen, or approximately 52% of total debt, will mature in February 2011. As JHR appears to have good relationships with its existing three partner financial institutions, no particular problems are anticipated in fund raising. That said, in order to further strengthen the funding base, JHR may need to extend the maturity profile, stagger maturities, reduce borrowing costs, and diversify sources of funding, among others.

The Rating Outlook is Stable. Although the business environment for hotels has bottomed out, a rapid recovery is unlikely partly because of the entry of new competitors and uncertainty over the future economic conditions. Amid the still challenging environment, R&I will keep a close eye on the extent to which JHR is able to recover profit and cash flow levels by capitalizing on the expertise of its asset manager and sponsor. Other important challenges include further bolstering the funding base and diversifying the asset portfolio through property acquisition.

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The primary rating methodologies applied to this rating are provided at "R&I J-REIT Rating Methodology" and "Basic Methodologies for R&I's Credit Rating". The methodologies are available at the web site listed below, together with other rating methodologies that are taken into consideration when assigning the rating.

<http://www.r-i.co.jp/eng/sf/about/methodology/index.html>

<http://www.r-i.co.jp/eng/cfp/about/methodology/index.html>

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