

Oct 10, 2012

R&I Affirms A, Changes Outlook to Negative: MID REIT, Inc.

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

ISSUER: MID REIT, Inc.
Issuer Rating: A, Affirmed
Rating Outlook: Negative, Changed from Stable

RATIONALE:

MID REIT, Inc. is a real estate investment trust (J-REIT) listed on the stock exchange in August 2006. The Reit focuses on investments in office buildings in the Osaka area. Its sponsor, MID Urban Development Co., Ltd., became a consolidated subsidiary of The Kansai Electric Power Co., Inc. in December 2009.

A change of the Rating Outlook this time is primarily attributable to 1) a deterioration in profitability and appraisal value-based leverage due to the harsh rental market, and 2) its sustained vulnerability to the severe environment because of the undiversified portfolio.

The market for office buildings in Osaka, MID REIT's main investment target, is harsh. Downward pressure remains on cash flows from properties held by MID REIT. Due partly to the partial exemption of rent payments from the largest tenant since April 2010, the NOI yield has fallen to 4.7%. Considering a number of office spaces scheduled to be supplied in Osaka in 2013, prospects for rent revenues are still unclear.

Under such circumstances, an excessive concentration on the Osaka Business Park area as well as some tenants is a risk factor. The three properties located in the Osaka Business Park account for approximately 63% of the total assets on an acquisition value basis, and rents from the top two tenants represent about 42% of the total rent revenues. The current rent contract with the main tenant of The Twin 21 ends in March 2013 and negotiations over the continued use of the whole building between the Reit and the tenant are ongoing.

The LTV ratio remains low at 40.8%. However, since the appraisal value of assets is about 20% below the carrying value as of end-June 2012, the debt ratio based on an appraisal value is rising. If valuation losses are taken into account, the Reit has a limited capacity for a further large increase in loans. Furthermore, the level of investment unit price suggests that it is difficult to achieve a capital increase for the time being. Accordingly, there is a marginal possibility that the Reit will soon achieve portfolio diversification, an issue to be resolved.

MID REIT has been able to raise funds smoothly on the back of favorable relationships with correspondent financial institutions. With respect to 14.5 billion yen in loans whose maturity date fell in July, the Reit has successfully refinanced loans in relatively favorable conditions with loan terms being three, five or seven years. Since loan terms are extended and due dates staggered to a certain extent, financing costs have been reduced, improving P/L performance. At present, the Reit's debts are all unsecured.

A key point for the near term is the outcome of negotiations between MID REIT and the main tenant over rent terms. R&I is focusing on whether MID REIT will be able to mitigate a fall in cash flows from its properties through negotiations with tenants while taking forward-looking measures for portfolio diversification.

The primary rating methodologies applied to this rating are provided at "Basic Methodologies for R&I's Credit Rating" and "Rating Methodology for J-REIT". 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/cfp/about/methodology/index.html>

■Contact : Investors Service Division TEL.+81-(0)3-3276-3511 E-mail. infodept@r-i.co.jp
■Media Contact : Corporate Planning Division (Public Relations) TEL.+81-(0)3-3276-3438

Rating and Investment Information, Inc. Nihonbashi 1-chome Bldg., 1-4-1, Nihonbashi, Chuo-ku, Tokyo 103-0027, Japan <http://www.r-i.co.jp>

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R&I RATINGS:**ISSUER:****MID REIT, Inc. (Sec. Code: 3227)****Issuer Rating****RATING:****A, Affirmed****RATING OUTLOOK:****Negative, Changed from Stable**

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