



Moody's assigns A1 issuer rating to Frontier Real Estate Investment Corporation

Tokyo, December 26, 2006 -- Moody's Investors Service has assigned an A1 issuer rating to Frontier Real Estate Investment Corporation (FRI). The rating outlook is stable.

The rating reflects FRI's strong capabilities in property acquisitions, including its utilization of the network of its asset management company's sponsor, and the stable cash flow accruing from its portfolio of mainly competitive retail properties. It also reflects its sound investment policy considering its current property acquisition market status and its highly conservative financial policy.

FRI's investments focus on suburban and urban retail properties throughout Japan. Its portfolio has nine properties worth JPY94.8billion on an acquisition price basis (excluding the properties at the stage of a provisional purchase and sales agreement), while the average age is approximately five years.

Moody's considers the portfolio as geographically well diversified and is composed as follows: Tokyo metropolitan area, 36%; Chubu area, 26%; Kansai area, 21%; Chugoku area, 12%; and Kyushu area, 5%.

On an acquisition price basis, the portfolio is biased towards its top three properties, which represent approximately 66% of its value. However, Moody's believes such concentration risk is mitigated by each property's prosperous submarket, their strong competitiveness in their respective submarkets, and long-term lease agreements with mainly high credit anchor tenants.

At present, all the properties are developed by Japan Tobacco Inc. (JT), a sponsor company for FRI's asset management company, Frontier REIT Management Inc. (FRM), utilizing the sites of factories and company housing complexes.

FRI is expected to grow its portfolio by acquiring retail establishments – developed by JT pursuant to a bilateral pipeline agreement – although uncertainty remains concerning possible setbacks due to regulatory restrictions.

Except for purchases from JT, FRI intends to invest in properties from external sources. Moody's has confirmed that, in this case, FRI will maintain its sound investment policy considering its current property acquisition market status, while at the same time continuing efforts to prevent any deterioration in the quality of its portfolio.

To enhance cash flow stability, FRI will continue seeking long-term lease agreements with strong creditworthy tenants. FRM has taken from its parent employees with experience and expertise in real estate management in its efforts to utilize the asset management expertise of its parent in retail properties.

FRM has separated itself from the risk of conflict of interest with JT by setting up [1] an in-house compliance committee that requires the unanimous consent of its members, including a third-party member and [2] a board meeting that requires consent of all outside members.

FRI has successfully reduced its interest-bearing debt obligations, including bank loans, currently outstanding at JPY3billion, by utilizing security and/or guarantee deposits funded by its tenants. FRI will continue to minimize its dependency on interest-bearing debt by utilizing them, even during the growth phase for its portfolio.

The refinance risk arising from deposit refund obligations is limited. Such obligations constitute long-term debt due in 20 years, payable in scheduled payments for 10 or 20 years, and with interest rates which are low and fixed, or zero. This is even though these obligations are mostly secured.

FRI's outstanding bank loans are all unsecured with no guarantee and extended by four domestic banks. Its financial policy is to hold its debt-to-total asset ratio (including the security/guarantee deposits from tenants) basically within the range of 30-40%. Moody's has considered this reasonably conservative financial policy in the rating.

Most of the security/guarantee deposits constitute secured obligations. The rating does not incorporate the subordinated nature of FRI's unsecured straight bonds relative to the secured obligations because Moody's considers that [1] its reasonably conservative financial policy is likely to succeed in holding its debt-to-total asset ratio in the 30's%, and [2] in consideration of the prices at which the properties were acquired, their NOI cap rates are generally higher than market benchmarks.

Frontier Real Estate Investment Corporation, listed in August 2004, is a Japanese real estate investment trust that focuses on investments in and management of retail properties. Its asset management company, Frontier REIT Management Inc, is a wholly-owned subsidiary of Japan Tobacco Inc.

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