



Astro Japan Property

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AUD \$3.80

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Buying into Japanese property

Today we introduce Astro Japan Property Group (ASX: AJA) into the portfolio. Astro Japan is a listed property group, which invests in the Japanese real estate market and holds interests in a portfolio of retail, office and residential properties. **We believe the Japanese property market is on the cusp of stabilisation and possibly a return to improving values**, particularly in urban areas and Astro Japan provides Australian investors with a relatively scarce exposure to the sector.



Prices are rotating swiftly off dynamic support found at the 50 day moving average of \$3.55. The bullish moving average cross in place signals momentum to favour the upside over the medium term. A decisive break above resistance located at the \$3.78/80 region would likely spark a second-round of upward momentum to follow.

By setting his 2% inflation target, **the new governor of the Bank of Japan, Haruhiko Kuroda, has declared to the world that he is going to run with "Abenomics"**. The bold plan sets out a doubling of the

monetary base (over just two years!) and will include massive bond buying and consider purchases of other asset classes such as equities, ETF's and real estate.

“Abenomics” is a term coined for Prime Minister Shinzo Abe’s approach to turning the Japanese economy around, and his platform for his political campaign. Mr. Abe has called for a comprehensive programme with monetary, fiscal and structural policies, which he has likened to holding three arrows together – held separately each could be bent or snapped, but taken together, they remain firm.

Even with expectations set high prior to Mr. Kuroda’s announcement the Yen has resumed it’s downwards slide and the Nikkei continued to surge. The slide in the value of the yen has been dramatic since last year, already working to improve the competitiveness of Japan’s large export sector. The monetary “arrow” is now well in flight and most believe it is on target. As of overnight the Japanese yen was on the cusp of breaching the big 100 level against the greenback.

For Astro Japan a weakening yen influences their results in a couple of ways. The carrying values of property will be lower when translated back to Australian dollars, as will income from tenants. This is a negative but we are wagering that a revitalised Japanese economy, and a reversal of the decline in property values, along with renewed interest in the asset class, will outweigh the impact from lower currency translation. **The J-REIT index was a strong performer in 2012 and has been continuing its run this year.**

In addition, with an improving property market we believe the company could further modify its portfolio to add value for shareholders. The company has flagged that its asset manager in Japan, Spring Investment, will increase its focus on asset sales that are smaller non-strategic holdings. The intention is to release capital from debt structures that are less efficient and either roll those into more efficiently leveraged investment opportunities, further debt reduction, distribution increases or share repurchases.

For example the company reported that the December 2012 refinancing of one of their structures which has a 13.5 billion yen loan, would result in a material reduction in both interest costs and amortization, which is expected to improve cash flow by approximately 9.8 cents per share on a full year pro-forma basis.



With reference to the weekly chart, a broad consolidation remains at play between support at \$1.60 and resistance of \$5.15. Over time, we would expect prices to continue to track north, targeting the upper boundary of \$5.15.

Astro Japan Property overview

The company has a portfolio of 37 investments in a mix of retail, office and residential buildings throughout Japan.

The following table is from the company’s half-year results presentation, dated 21 February 2013. The pro-forma column refers to the restatement of the portfolio to adjust for the company’s capital raising and property restructure 31 January. Since that time the company has released an announcement regarding an additional minority investment in a Tokyo commercial property, valued at 300 million yen (~A\$3 million).

	Pro-forma 31 December 2012 ¹	31 December 2012	30 June 2012	Change (30 June to Pro-forma 31 December 12 ¹)
Portfolio carrying value	¥85.4 bn	¥95.1 bn	¥98.3 bn	-13.1%
Total number of properties	36	39	40	-10.0%
NRA (sqm)	233,513	258,734	269,122	-13.2%
Occupancy by area	94.0%	94.0%	95.8%	-1.8%
Number of leases	226	355	366	-38.3%
% non-cancellable leases by income	53.5%	44.9%	44.4%	9.1%
Weighted average term to expiry (WALE) (non-cancellable leases) – years	4.5 years	4.5 years	4.5 years	-

Source: Company presentation

The company's retail portfolio boasts the highest occupancy rate, sitting at 98.7% by area as of 31 December 2012. Following this was the residential portfolio, with occupancy at 88.3% and office lagging with 85.6% occupancy. This led the company to have an average occupancy of 94.0% across the portfolio. In terms of property income, retail contributed approximately 51.4%, office 40.4% and residential just 8.2%.

As at 31 December 2012

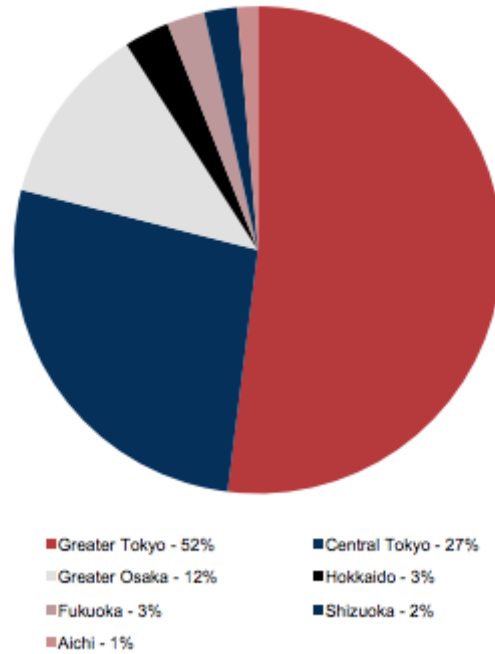
Property Income (¥ million)	Six months to 31 December 2012	Six months to 31 December 2011	Change
Retail	2,119	2,191	-3.2%
Office	1,667	1,704	-2.2%
Residential	339	366	-7.4%
Total portfolio	4,125	4,261	-3.2%

Occupancy by area	31 December 2012	30 June 2012	Change
Retail	98.7%	99.4%	-0.7%
Office	85.6%	85.5%	0.1%
Residential	88.3%	100.0%	-11.7%
Total portfolio	94.0%	95.8%	-1.8%

Source: Company presentation

We prefer the urban areas in Japan, believing they will be the first to pick up in value. The company is well positioned in this respect, with the vast majority of its portfolio in Tokyo or greater Osaka as depicted below:

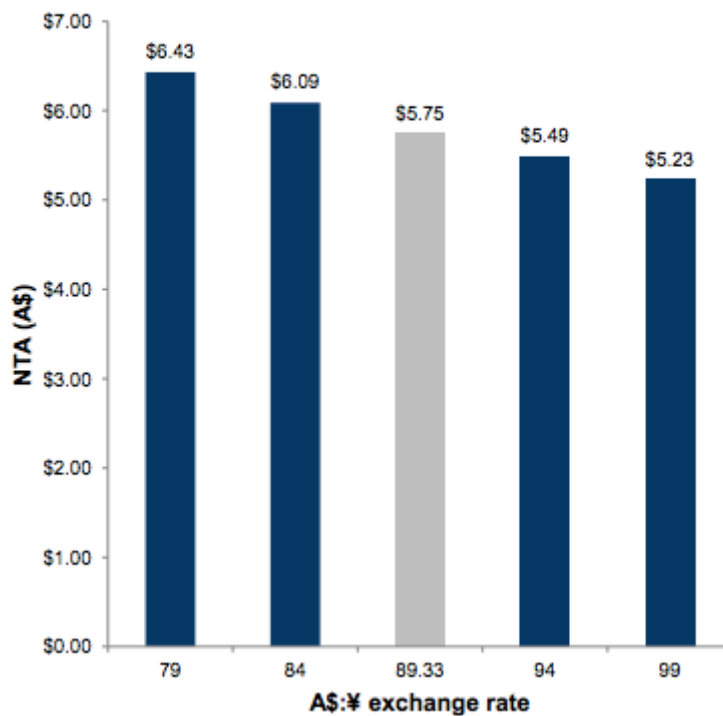
Pro-forma diversification (by value)
as at 31 December 2012¹



Source: Company presentation

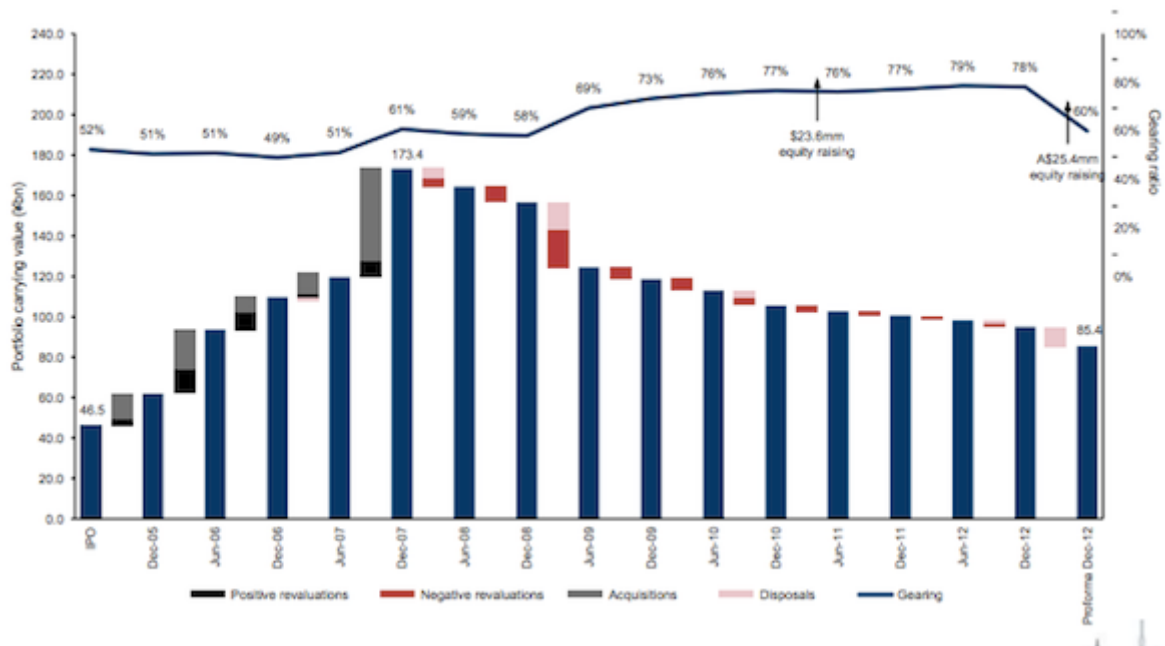
The following graphic from the company's half-year results presentation estimates the sensitivity of the company's pro-forma net tangible assets (NTA) to changes in the exchange rate between the yen and Australian dollar. We note that the yen is trading at around 101 yen to the Aussie at the time of writing and that this was prepared prior to the most recent 300 million yen investment.

Pro-forma NTA sensitivity to A\$:¥ exchange rate



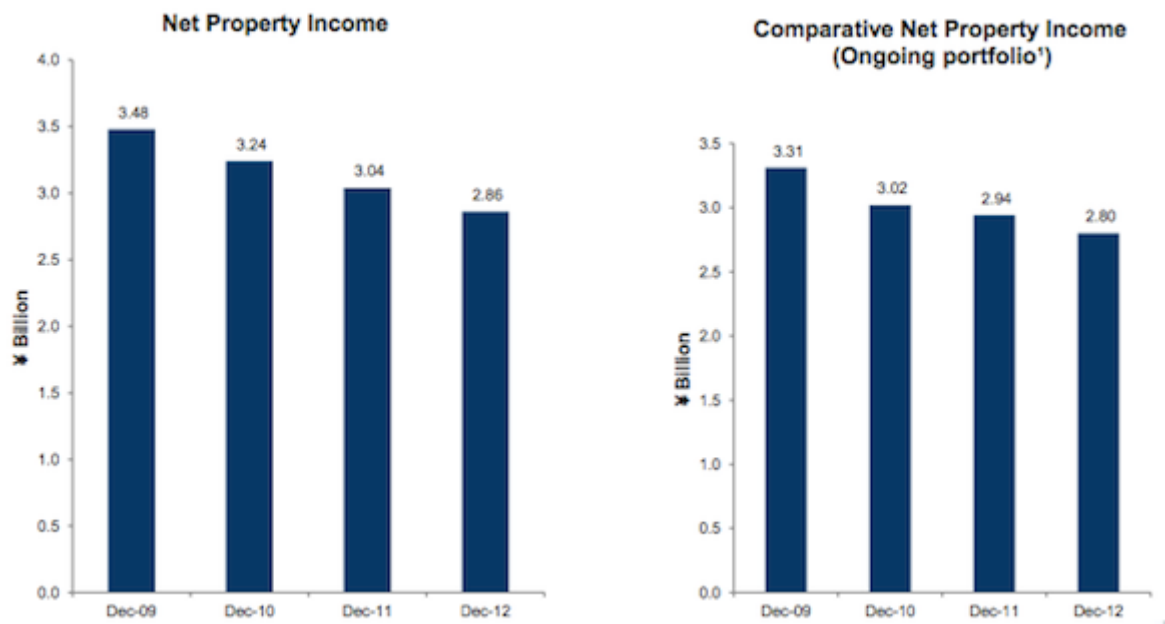
Source: Company presentation

The latest A\$25.4 million institutional placement and portfolio restructure has reduced gearing and improved the company's debt maturity profile.



Source: Company presentation

The company's operating financials have been in decline since the financial crisis but we believe this is largely reflected in the valuation. The following graphic shows the gradual decline in net property income over the past four years reflecting the softness in the Japanese property market. However the small 1.3% decline in the portfolios property value in the most recent period was the smallest change since 2008.



Source: Company presentation

Looking ahead, the company is trading on 8.1 times June 2013 earnings consensus expectations for earnings and 8.4 times 2014. On average analysts expect a dividend yield of 4.9% and 5.4%, although we feel that distributions may fall slightly short of this. The most recent half-year distribution was 7.5 cents per share, down from 10 cents per share the previous period.

Summary

We believe that Japanese property prices are on the cusp of reversing decades of decline, with corresponding increases in the rents from tenants. Certainly investor interest in Japanese equities and property has been reignited and we believe both are positive for **Astro Japan**, and this can more than offset the impact from a weakening yen, **therefore we are recommending it as a buy around current prices.**

We recommend Astro Japan Property Group (ASX: AJA) as a new buy around \$3.80.

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Snapshot AJA

Astro Japan Property

Latest Closing Price: \$3.80

As part of the separation of AJT from the Babcock & Brown Group on 16 April 2009, AJT implemented a restructure to enable the internalisation of the Responsible Entity and Australian management. On 12 November 2009, the units in AJT were stapled to the shares in Astro Japan Property Group Limited (AJCo) to form the Astro Japan Property Group (Astro Group). The Astro Group is listed on the Australian Securities Exchange and its stapled securities trade under the ASX code AJA. The company has a diversified portfolio of interests in 37 properties in Japan.

Market Capitalisation: \$249m

	FY1	FY2
Price to Earnings	8.1	8.4

Dividend Yield (%)	4.9	5.4
Price to Book	0.7	0.6
Return on Equity (%)	9.3	7.7

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