savills

Briefing
Residential sector

Q1 2012

Image: Park Court Ebisu Hill Top Residence, Shibuya Ward

SUMMARY

Mid-market rents exhibited narrow seasonal volatility, with average occupancy rates exceeding 95%.

- Average asking rents for mid-market rental apartments in Tokyo's core eight wards stood at JPY3,945 per sq m (JPY13,040 per tsubo), down 0.8% on both a quarter-on-quarter (QoQ) and year-on-year (YoY) basis.

- Only one core-eight ward demonstrated rental growth: Meguro, where a 2.1% QoQ rise was recorded.

- The generally weak rental movement in Q1/2012 can largely be attributed to a seasonal fall-off in demand through the winter months.

- Average mid-market rents in Meguro Ward reached JPY4,190 per sq m (JPY13,850 per tsubo), making it the third most expensive ward after Shibuya and Minato.

- The average occupancy rate for J-REIT residential properties in the core eight wards stood at 95.9%, up 60 basis points (bps) QoQ and 30 bps over Q1/2011.

- The average monthly asking rent for luxury residential units was JPY5,485 per sq m (JPY18,130 per tsubo), reflecting declines of 0.5% QoQ and 5.5% YoY.

"Although seasonal factors prompted moderate rental declines in many submarkets in Q1/2012, the fundamentals for mid-market leasing assets in Tokyo are strong. Already high and rising occupancy levels in the J-REIT residential portfolio are testament to this."
Savills Research & Consultancy

Tokyo residential leasing market overview

The average asking rent for mid-market rental apartments[1] in Tokyo's core eight wards[2] stood at JPY3,945 per sq m (JPY13,040 per tsubo[3]) per month in Q1/2012. This rental figure reflects a fall of approximately 0.8%, both QoQ and YoY. Nominal declines were recorded in three of the core residential wards, while four experienced rental declines exceeding 1.0% over the three-month period. The only core ward to demonstrate rental growth was Meguro, where a rise of 2.1% QoQ was recorded.

[1] Rental data has been compiled by Savills utilising more than 16,000 leasing comparables published separately by Chintai, a major residential leasing broker in the Japanese market. Selection criterion for the comparables is limited to rental apartments under 100 sq m, less than ten years old and within a ten-minute walk of the nearest station.
[2] Tokyo's core eight wards are defined as Bunkyo, Chiyoda, Chuo, Meguro, Minato, Setagaya, Shibuya and Shinjuku.
[3] 1 tsubo = approximately 3.3 sq m or 35.6 sq ft

The generally weak rental movement in central Tokyo during the first quarter can be largely attributed to the seasonality of Japan's residential leasing market, where demand is often subject to tempering through the winter months. This trend is exacerbated not only by the New Year holiday period and spells of inclement weather, but also by the fact that bonuses for Japan's salaried workforce tend to be distributed at the close of the financial year in March. Given the heavy upfront costs involved in leasing a new apartment (including deposit, agency fees, moving costs and often so-called 'key money', a gratuity to the landlord), which can be equivalent to several months' rent in advance, many tenants opt to hold-off on relocation until the spring, when bonus payments are firmly in their pocket.

The healthy rental upturn in Meguro Ward in Q1/2012 reflected an increase in average advertised rents for one-bedroom apartments in popular residential locations such as Osaki, Gotanda, Aobadai, Gakugeidaigaku and Jiyugaoka. The overall average rent for the ward reached approximately JPY4,190 per sq m (JPY13,850 per tsubo), making it the third most expensive ward after Shibuya and Minato.

Average mid-market asking rents in Shibuya dipped 0.2% over the preceding quarter to stand at JPY4,390 per sq m (JPY14,510 per tsubo). This compares to a 0.7% decline in Minato, where the average apartment rent stood at approximately JPY4,245 per sq m (JPY14,030 per tsubo). This dip can be largely attributed to a squeezing of rents for smaller one-bedroom units, which make up a large proportion of the stock available for lease in the ward.

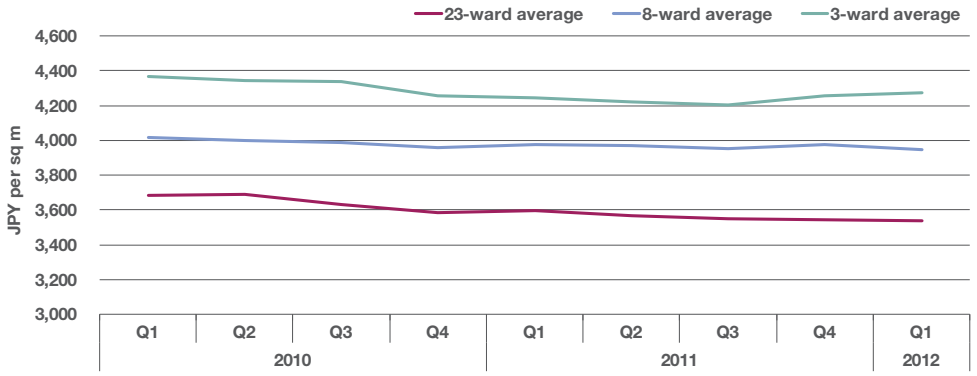
The most significant rental declines of the quarter were recorded by Bunkyo and Shinjuku wards, where average rents slipped approximately 2.4% and 2.1% QoQ respectively. For both wards, downward pressure on average rents was spurred by an increase in available inventory, predominantly unit types targeting single occupiers. As of Q1/2012, the average mid-market rental level in both Bunkyo and Shinjuku sat slightly above the JPY3,800 per sq m (JPY12,560 per tsubo) level.

When looking at the wider 23-ward area, the average rental level fell marginally for the fourth consecutive quarter, equivalent to approximately 0.3% QoQ, to JPY3,540 per sq m (JPY11,700 per tsubo). Despite this downward trend, the Tokyo mid-market is considered to be close to the bottom of the down cycle and a gradual upswing in rents is anticipated in the near term. As evident in recent quarters, upward momentum will likely be driven by Tokyo's more central wards, which command both a demand and rental premium.

Market sources suggest that domestic occupiers are placing greater importance on the proximity

GRAPH 1

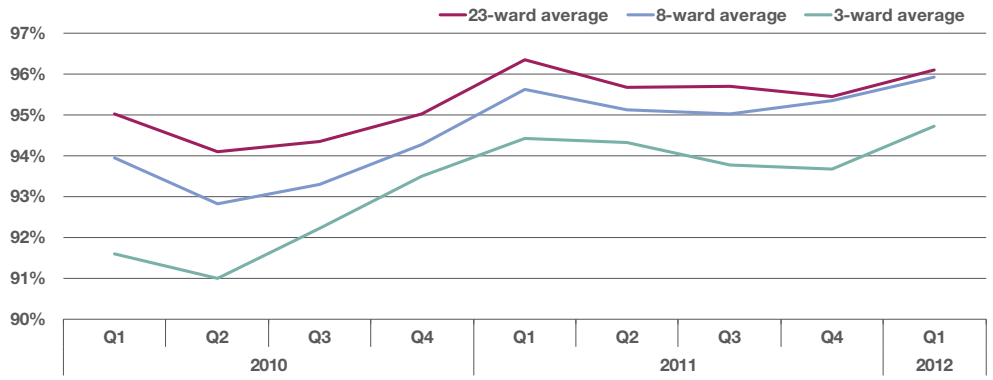
Average asking rents for mid-market rental apartments, Q1/2010–Q1/2012*



Source: Chintai, Savills Research & Consultancy
* Tokyo's core three wards are defined as Meguro, Minato and Shibuya.

GRAPH 2

Average occupancy rates for J-REIT residential assets, Q1/2010–Q1/2012



Source: J-REITs^, Savills Research & Consultancy
^ Nippon Accommodations Fund, Advance Residence (including the former Nippon Residential Fund portfolio) and Heiwa Real Estate REIT.

of their home relative to their workplace following the transport interruptions which occurred after the Great East Japan Earthquake and during the particularly disruptive typhoon season last year. The spread between the 23-ward rental average and the core eight-ward figure is illustrative of this, having moved out around 70 bps from Q1/2011 to reach approximately 10.3% in Q1/2012. The average premium commanded by the core three wards – Meguro, Minato and Shibuya – rose at the faster pace of 190 bps YoY to reach approximately 17.3%.

Tokyo residential occupancy rates

While reliable tenancy data remains limited for the Japanese residential market as a whole, analysis of J-REIT-owned assets can provide a useful benchmark upon which to gauge market occupancy levels. It should be noted that the J-REIT data relates to a somewhat narrow survey group; however, the portfolio is considered to closely mirror wider trends in mid-market rental apartments.

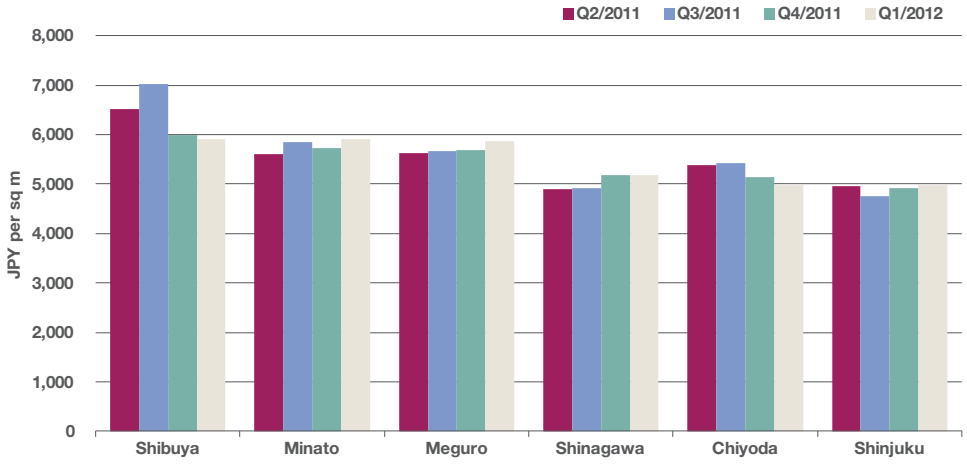
In Q1/2012, the average occupancy rate for J-REIT residential properties in Tokyo's core eight wards stood at 95.9%. This reflects a rise of 60 bps over the preceding quarter and 30 bps over Q1/2011. The occupancy rate for the Tokyo 23-ward area stood at 96.1%, also up 60 bps QoQ but down 30 bps on a YoY basis.

Within the core eight wards, the average occupancy rate improved most in Shibuya Ward, increasing 170 bps QoQ to reach 95.8%. Similar movement was recorded in Meguro Ward, which saw its occupancy rate increase by 120 bps QoQ to 95.3%. The ward which exhibited the largest reduction in average occupancy levels over the three-month period was Chiyoda Ward. Remaining high, the average occupancy rate here fell by approximately 100 bps to 96.5%.

Strong leasing demand for modern mid-market Tokyo residential assets is expected to support occupancy levels over the short to mid term, bolstered in part by continued in-migration to the capital from Japan's regional towns and cities.

GRAPH 3

Tokyo luxury residential average asking rent by ward, Q2/2011–Q1/2012



Source: Tokyo Living, Savills Research & Consultancy

Tokyo luxury residential market update

Savills Research & Consultancy collates leasing data for over 200 luxury residential assets in eight Tokyo wards[4]. Luxury residential units are defined by the following criteria:

1) Each unit has a net leasable area of 100 sq m or over;

2) Asking rents per unit are in excess of JPY500,000 per month;

3) The building age is less than ten years;

4) Properties are located within a ten-minute walk of the nearest station(s);

5) Analysis excludes units with more than three bedrooms.

The average monthly asking rent for luxury residential units in the eight-ward survey area declined a modest 0.5% in Q1/2012 compared with the preceding quarter and 5.5% YoY. At approximately JPY5,485 per sq m (JPY18,130 per tsubo), this figure reflects a 39% premium over the average rent for mid-market properties. This premium remained stable compared with Q4/2011 but has moved in an estimated 70 bps from the Q1/2011 figure.

Shibuya Ward continued to command the highest luxury residential rental level in terms of asking rents for available units, although its lead over the next most expensive ward, Minato, narrowed considerably. The average rental figure here stood at approximately JPY5,910 per sq m (JPY19,540 per tsubo), down approximately 1.3% QoQ. This movement follows a decline of around 15% in Q4/2011, which was largely attributable to dataset volatility arising from one exceptionally expensive unit being removed from the market in Daikanyama.

Minato Ward, which has the highest concentration of high-end rental assets of any Tokyo district, commanded an average luxury asking rent of approximately JPY5,905 per sq m (JPY19,520 per tsubo) in Q1/2012. This figure reflects a 3.1% rise over the last quarter of 2011 and an increase of approximately 4.3% YoY. The modest rebound was due principally to an increase in advertised rents for two- and three-bedroom apartments.

Tokyo's third most expensive ward, Meguro, also demonstrated a healthy rise in luxury asking rents in Q1/2012 equivalent to approximately 3.2% QoQ – its fourth consecutive quarterly increase. Average rents here now stand at approximately JPY5,860 per sq m (JPY19,371 per tsubo). Meguro's high-end residential assets predominantly comprise two or more bedroom units, which tend

4 Bunkyo, Chiyoda, Chuo, Meguro, Minato, Shinagawa, Shibuya and Shinjuku wards.

to command lower rental values per sq m than one-bedroom units but generally exhibit less volatility in terms of demand, despite having a slightly longer lease-up period.

By contrast, the neighbouring wards of Chiyoda and Chuo recorded rental declines of approximately 3.0% and 3.8% QoQ respectively. Negative rental movement in the former ward was principally driven by a reduction in the average asking rent for two-bedroom units, for which overall availability decreased during the quarter. The decline demonstrated by Chuo Ward similarly reflects volatility arising from changes in its small sample group, as opposed to any prevailing market trend.

Although highly dependent on the individual property, lease incentives have remained an often-utilised tool to attract tenants at high-end properties in recent quarters. In many cases landlords have been willing to discount or waiver fixed costs such as agency and signing-on fees (ie, key money), while rent-free periods equivalent to one-month's rent have not been uncommon. Market sources suggest that this trend has not yet begun to ease and the luxury residential leasing market is considered to still be in the late down cycle.

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