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Japan

Spotlight
Japan retail market

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Spotlight

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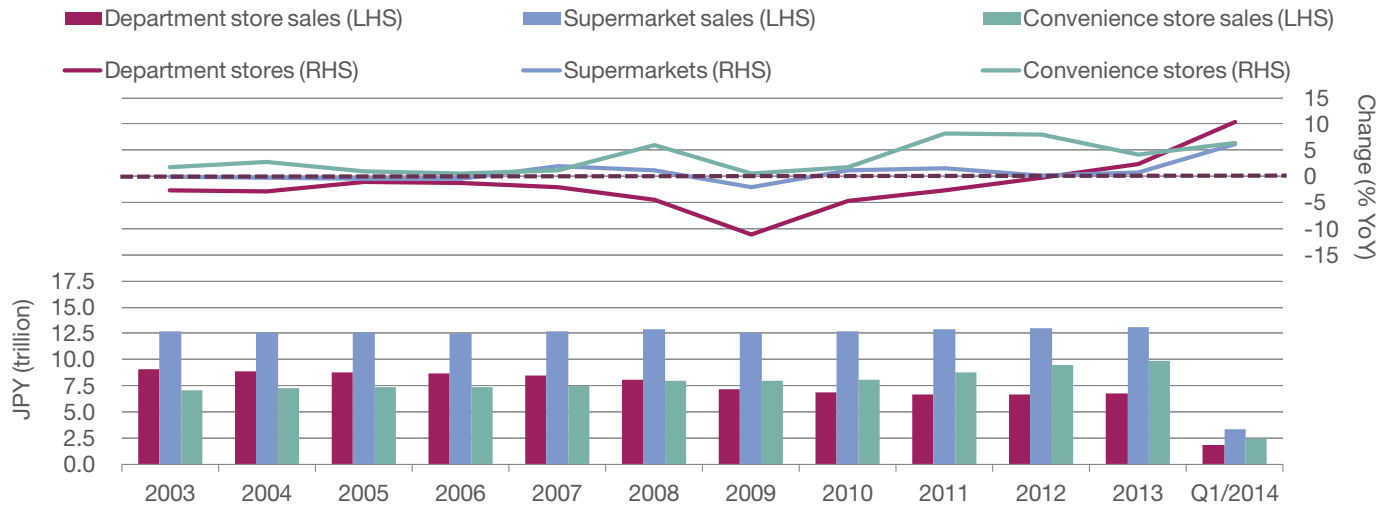
Japan continues to urbanise, with its population gravitating towards its largest cities and sleeper towns. Key high-street retail destinations and suburban shopping centres are therefore well positioned to benefit from the recent economic revival catalysed by Prime Minister Abe's cabinet and the Bank of Japan.

SUMMARY

- Sales figures at large-scale retailers proved robust in 2013, with supermarkets, department stores and convenience stores all recording growth on an annual basis.
- Especially high sales growth for luxury goods, cosmetics products and household appliances was recorded in Q1/2014. This was greatly influenced by front-loaded demand prior to the national consumption tax increase that came into effect on 1 April.
- Convenience stores have maintained a positive sales growth rate over the last ten years, strengthened through product diversification and strategic partnerships.
- While there was a sharp rise in the number of visitors from Southeast Asia countries in 2013, Chinese tourists remained the top spenders for shopping, followed by visitors from Taiwan and Korea.
- Tokyo and other major cities continue to attract global retailers and new retail outlets. Recent openings include a bespoke store for electronics giant Apple in Omotesando, the brand's first in Japan for nine years.
- The most expensive prime retail thoroughfares in Tokyo are located in Ginza and Omotesando, where monthly asking rents for ground floor units are in excess of JPY150,000 per tsubo. Rental levels in such locations are supported by very high occupancy rates.
- In 2013, retail property transactions totalled approximately JPY800 billion, up 62% YoY on the back of a turnaround in investor sentiment towards this sector.
- In geographical terms, Tokyo continues to be the focus of investor appetite, accounting for around 70% of retail property transactions by volume last year. However, other major urban centres such as Osaka and Fukuoka are also attracting investors seeking stable income and higher returns.
- Domestic purchasers have dominated retail investment activity, with J-REITs, local private investors and listed companies accounting for over 70% of transactions by volume. Nonetheless, cross-border investment in Japanese retail properties has increased steadily over the last two years.
- As location-focused buyers remain eager to enter the Tokyo market, further compression in retail transaction yields seems inevitable in the near term.

GRAPH 1

Large-scale retail and convenience store sales, 2003–Q1/2014



Source: METI, Savills Research & Consultancy

1.1. Retail sales

In its first year, Abenomics provided a shot in the arm to large-scale retailers and convenience stores

Annual statistics from the Ministry of Economy, Trade and Industry (METI) illustrate positive sales trends for Japan's large-scale retailers and convenience stores in 2013. Supermarkets – by far the largest market subsector at JPY13.06 trillion – remained stable with modest annual sales growth of 0.8%. Having overtaken department stores in 2009 to become the second largest market subsector, total sales at convenience stores rose 4.2% year-on-year (YoY) to a new high of JPY9.87 trillion. Sales at domestic department stores meanwhile rose for the first time in more than a decade, with overall sales increasing 2.3% YoY to JPY6.79 trillion.

A major contributing factor behind the pick up in retail sales last year was 'Abenomics', the government's reform package encompassing quantitative easing, fiscal policies to stimulate demand and structural deregulation. These 'three-arrows' place asset price inflation at their core and have had encouraging results to date. Upshots include improved consumer and business confidence, higher stock prices, and marked progress in nudging the national economy out of its 15-year deflationary cycle.

1.2. Impact of sales tax rate hike

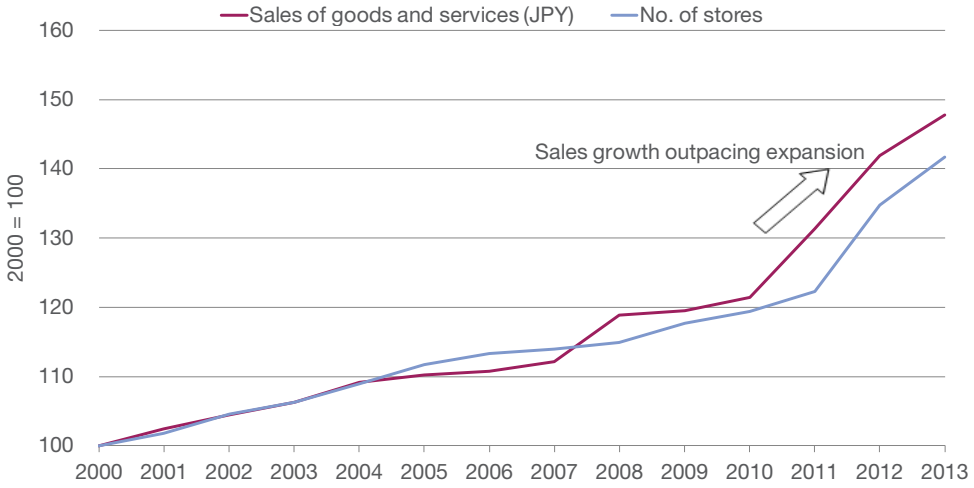
April consumption tax increase prompts Q1 shopping spree; wage rises expected to support near-term demand

While sales data for the first quarter of 2014 maintained a strong growth trend, movement was greatly influenced by the national consumption tax increase from 5% to 8%, which came into effect on 1 April.

According to the Japan Department Stores Association (JDSA), nationwide department store sales rose 10.4% YoY in Q1, driven by a 25.4% jump in sales in March alone. This sharp recovery was chiefly a result of rush buying ahead of the consumption tax hike and was predominantly focused on higher-value purchases. By item type, department stores reported especially high sales growth for luxury goods (up 57% YoY), cosmetics products (up 28% YoY) and household appliances (up 20% YoY).

GRAPH 2

Convenience store growth index, 2000–2013



Source: METI, Savills Research & Consultancy

Sales at supermarkets also witnessed healthy growth of 6.2% YoY in Q1 as shoppers stockpiled non-perishable goods before prices rose. Convenience stores reported a similar boost to sales at 6.4% YoY.

Post tax hike, we expect forthcoming data to show a dip in retail sales in Q2. By retail subsector, inital figures for April show that sales fell 10.5% YoY at department stores and 3.9% YoY at supermarkets. Convenience stores bucked the trend, maintaining a positive sales growth rate of 4.2% YoY over the same month.

Given expectations for higher summer bonus payments and a gradual increase in base wages in the private sector, a measured recovery is likely to be seen in the summer sales season from July. All in all, the negative impact of April's tax increase on consumer demand is anticipated to moderate through the second half of the year.

Nonetheless, for consumers to maintain their purchasing power, wage growth will need to advance in line with price inflation over the coming years. This is particularly important given the government's plan for a second consumption tax increase (from 8% to 10%) in October 2015. Such a move could significantly shock consumer demand if implemented before wages catch up. The official decision on whether to implement this second rate rise is scheduled for the end of 2014 and is dependent on prevailing economic conditions.

1.3. Convenience stores

Expansion through diversification, strategic partnerships

Convenience stores have maintained a positive sales growth rate over the last ten years, outperforming supermarkets and marking a stark contrast to department stores in terms of business growth momentum.

Convenience stores are now considered a significant segment of the Japanese retail market due to their numerous locations in cities and rural areas. Their popularity with time-strapped single and dual-income households, as well as the elderly, lays in the diverse range of products on offer. This includes pre-cooked meals, household necessities and community services traditionally associated with post offices.

Given Japan's ageing demographics and shift towards smaller household sizes, convenience store operators are aware that location and product diversification is key, and are structuring their service lines accordingly.

In early 2014, Japan Railway West (JR West) formed a strategic partnership with Japan's largest convenience store operator, Seven and i Holdings, to convert around 500 subsidiary-dominated retail spaces in their

train stations into convenience stores under the 7-Eleven brand. As of March 2014, there were over 1,222 stations under JR West's administration.

This retail trend emerged a few years ago when convenience store chain LAWSON ventured into a partnership with Tokyu Corporation to launch "LAWSON + toks". This new brand of convenience stores is located predominantly in train stations that have connectivity to Tokyu railway lines. FamilyMart, a competing francise chain, also embraced the strategy by integrating their stores with a number of different retailers, mostly pharmacy operators. The retailer plans to open more than 1,000 such stores within five years.

Through schemes such as strategic partnerships, convenience store sales growth has outpaced new store development since 2008.

1.4. Sales efficiency by category

Convenience store sales efficiency, or sales per sq m, has proved to be durable over the last ten years despite steady floor space expansion. Like most other types of retailers, sales per sq m dipped as a result of an increase in new supply during the economic boom period before the global financial crisis (GFC). However, METI data shows that the sales efficiency of convenience stores had recovered by 2012 (the latest survey year), whereas other retail categories such as department stores and supermarkets faced a new bottom due to the market slowdown after the GFC and Great East Japan Earthquake of 2011 (Graph 3).

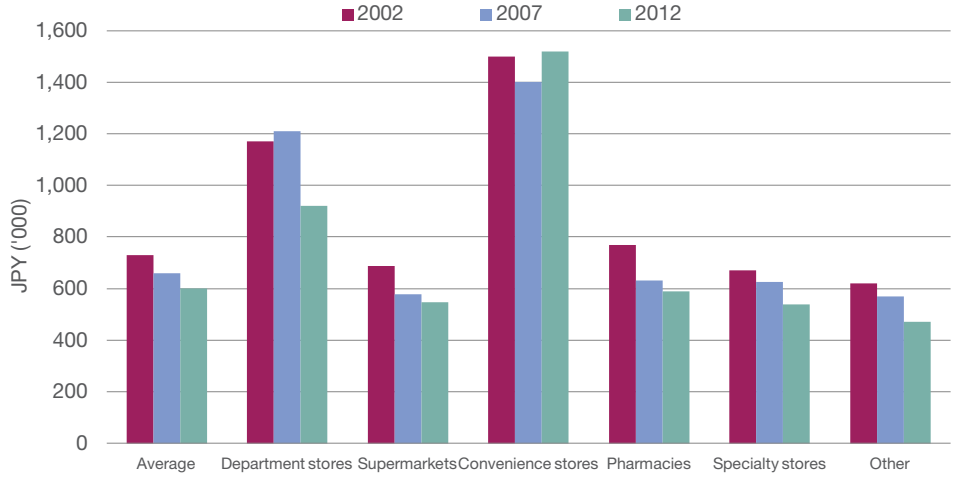
2.1. Growing number of international tourists

Japan has experienced a 67% increase in overseas visitors since 2011, with 2013 posting a record 10 million international tourists – up 24% compared with the previous year. Factors influencing this trend include the depreciation of the Japanese yen after Prime Minister Abe and the Bank of Japan announced their assertive quantitative easing programme in early 2013.

Other government policy measures also supported the trend. Of note,

GRAPH 3

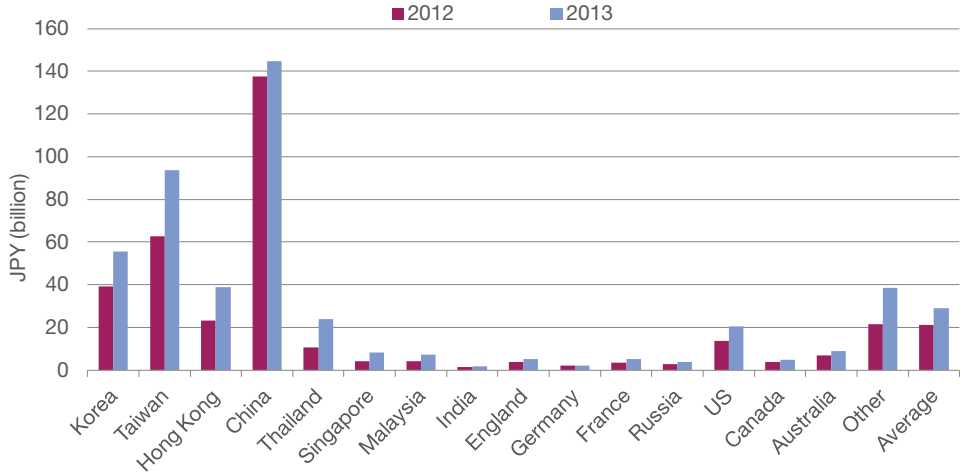
Retail sales per sq m by category, Japan nationwide



Source: METI, Savills Research & Consultancy

GRAPH 4

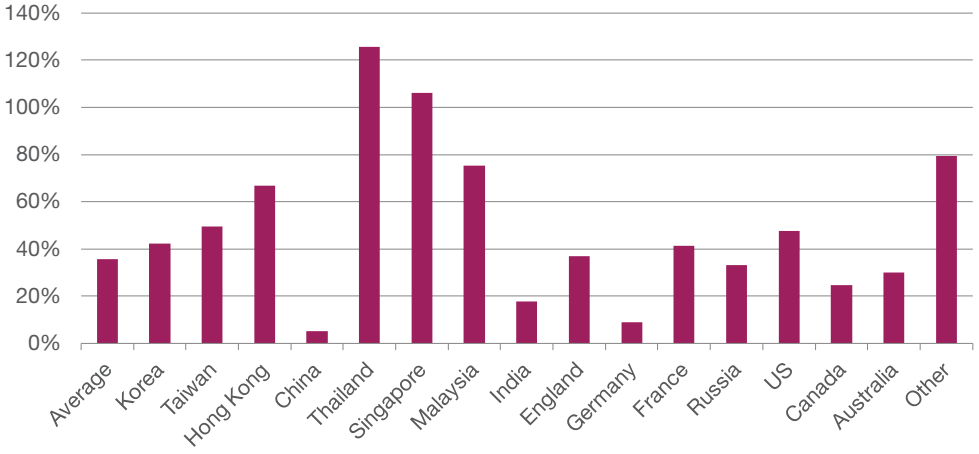
Shopping expenditure by international tourists, 2012 vs 2013



Source: Savills Research & Consultancy based on JNTO data

GRAPH 5

Annual growth in international tourist expenditure by country, 2013



Source: Savills Research & Consultancy based on JNTO data

visa requirements for travellers from countries in Southeast Asia were eased in July 2013, which brought about a sharp rise in the number of visitors from Thailand (64.0%), Malaysia (60.9%) and Vietnam (56.3%) in Q1/2014, compared with the same period of the previous year.

In response to Japan's growing popularity, 12 international low-cost carrier airlines had launched new services to Japan by December 2013, including eight routes to the Tokyo area. Following the high demand for international flights to Japan, Haneda Airport expanded its annual number of plane slots by around 9% to 447,000, including 90,000 for international flights in March 2014.

Growth in inbound tourism is expected to have a positive and material impact on certain sectors of Japan's retail market over the coming years.

2.2. Impact of inbound tourism on Japan's retail market

The Japan National Tourism Organization (JNTO) conducts an annual survey which identifies the spending habits of tourists in different sectors, including transportation, accommodation, shopping, and food and beverage. Based on tourist numbers and typical spending habits, JNTO estimate that total expenditure by international visitors reached JPY1.4 trillion in 2013 – 30.6% higher than in the previous year's survey and reflecting per capita spending of approximately JPY136,000.

Chinese tourists were the top spenders in the shopping category, with a total expenditure of JPY145 billion, followed by tourists from Taiwan (JPY93 billion) and Korea (JPY55 billion). These three countries alone accounted for approximately 63% of total shopping expenditure by tourists last year. In fact, tourists from certain Asian countries, including China, Taiwan and Thailand, display such strong demand for shopping in Japan that their typical retail expenditure exceeds that spent on accommodation during their visit. This is in contrast to visitors from other regions, particularly western countries, who typically allocate a higher weighting to hotel expenses.

In terms of annual growth in shopping expenditure in 2013, tourists from Thailand recorded the highest growth of 126%, followed by tourists from Singapore and Malaysia, at 106% and 76% respectively. Notably, shopping expenditure by Chinese visitors rose an estimated 5.2% despite a 7.8% decline in visitor numbers last year. This is reflective of a double-digit increase in spending per head.

JNTO's survey shows that shopping centres, airport duty-free shops, convenience stores and department stores were the most popular places for tourists to shop. According to JDSA data, duty-free spending at department stores in April 2014 reached a new high at over JPY6 billion across 46 surveyed stores, representing growth of 54.3% YoY. International tourists contributed almost 5% of annual sales at Mitsukoshi's Ginza store in 2013, a figure which the retailer's president estimates could increase twofold this year.

By the 2020 Olympic Games, the Japanese government plans to double the number of outlets where duty-free purchases are available to over 10,000, led by the establishment of more stores in tourist-favoured regions, including Kyoto and Hiroshima. Additionally, beginning in October 2014, the range of items subject to consumption tax exemption will be widely expanded to include cosmetics products, local sake and souvenirs, in order to encourage more spending among tourists during their visits. This provides a brighter outlook for department stores, shopping centres and other retailers.

3.1. Retailers competing for space in prime areas

Given its large and wealthy population, Tokyo is considered a key entry point for international retailers seeking to expand their brands in Japan or a foothold in Asia. In early June, the new Apple Store in Omotesando opened for business, adding more choice to the popular high-end shopping district. While there were no new stores opened over the last nine years, this 1,868-sq m store is the eighth for Apple in Japan, and the third in Tokyo.

In terms of upcoming supply, the 16,582-sq m KIRARITO GINZA in Ginza-itchome is scheduled to open in autumn 2014, comprising over 50 stores, including the first flagship store for bag retailer HARTMANN and a re-launch for luggage retailer Samsonite. Meanwhile, Tokyu Land's Ginza-gochome Project is scheduled to complete in autumn 2015, adding 49,700 sq m of new floor space in the area.

TABLE 1

Selected leasing transactions, 1H/2014

Type	Brand	Open date	Location	Floor area (sq m)
Luxury fashion	AUDEMARS PIGUET*	Apr-14	Ginza, Tokyo	156
	Givenchy*	May-14	Omotesando, Tokyo	392
	Officine Panerai	Feb-14	Shinsaibashi, Osaka	146
High-street fashion	UNIQLO	Mar-14	Ikebukuro, Tokyo	2,644
	H&M	Mar-14	Tendo, Yamagata	1,700
	AMERICAN EAGLE OUTFITTERS	Mar-14	Nishinomiya, Hyogo	759
Interior and lifestyle	Carl Hansen & Søn*	Apr-14	Omotesando, Tokyo	185
	Zara Home	Apr-14	Omotesando, Tokyo	700
	IKEA	Mar-14	Tachikawa, Tokyo	40,000
Digital and electrical appliances	Apple Store	Jun-14	Omotesando, Tokyo	1,868
Café/restaurant	Magnolia Bakery*	Jun-14	Omotesando, Tokyo	170

Source: Savills Research & Consultancy
*First store in Japan

The majority of international retailers establish their presence in either the Ginza or Omotesando districts and later expand to cities such as Osaka, Nagoya and other regions. Sustained demand for space from major retailers has resulted in virtually zero vacancies (1/F) in Tokyo's main retail thoroughfares. It is also an important factor in supporting prime rents as the economy enters a recovery period.

3.2. Asking rents in major retail districts

In general, high-street retail rents in Tokyo and Japan's other major cities are considered strong and stable. According to data from Attractors Lab and BAC Urban Projects published in spring 2014, the most expensive prime retail streets in Tokyo are located in Ginza, on Chuo-dori and Harumi-dori. Monthly asking rents for ground floor units here are in excess of JPY150,000 per tsubo[1].

In the Omotesando-Harajuku district, which hosts a cluster of luxury and high-street fashion brands, ground floor units along Omotesando-dori command monthly asking rents in the JPY100,000 to JPY150,000 per tsubo range and upwards. Similar levels can also be achieved along the bustling Takeshita-dori, where the majority of stores have relatively small floor areas. One advantage of this area is its potential to expand, as there is upcoming supply in the west side of the district close to Meiji-dori, including a new store for electrical appliances retailer Yodobashi Camera.

In Osaka, monthly asking rents in one of the busiest pedestrian areas, Shinsaibashisuji-shotengai shopping arcade, range from around JPY60,000 to JPY100,000 per tsubo for ground floor units. Along nearby Mido-suji Street, where many luxury retailers have opened flagship stores, monthly asking rents typically range between JPY60,000 and JPY80,000 per tsubo, although higher rents can be achieved depending on the location.

In the city of Fukuoka, competition between Hakata Station, Canal City and Tenjin has led to increasing retail supply and tenancy improvement activities in each district. Ground floor monthly asking rents in Tenjin-nishi-dori Street typically range between JPY50,000 and JPY60,000 per tsubo.

1 1 tsubo = 3.306 sq m or 35.583 sq ft.

On the back of the economic recovery, competition for retail space will stiffen, compounded by the lack of available space on the market, especially in prime locations such as those listed above.

4.1. Retail investment

Tokyo dominates retail property transactions, while Osaka and Fukuoka are also attracting investors

Looking at investment volumes, it is clear that Abenomics has revived confidence in Japan's real estate investment market. This includes the retail sector.

In 2013, retail property transactions totalled approximately JPY800 billion, up 62% YoY on the back of a turnaround in investor sentiment towards this sector. Almost 70% of recorded retail transactions took place in Tokyo, where a total acquisition volume of JPY551 billion was recorded, rising 63% YoY.

Significant YoY growth in retail transaction volumes was also seen in Osaka (up 187% to JPY149 billion) and Fukuoka (up 80% to JPY53 billion) in 2013. The growing number of investments in regions outside Tokyo indicates that investors are exploring alternative markets, either to diversify their portfolios or secure higher yields.

Image: Apple Store Omotesando, Shibuya Ward, Tokyo

TABLE 2

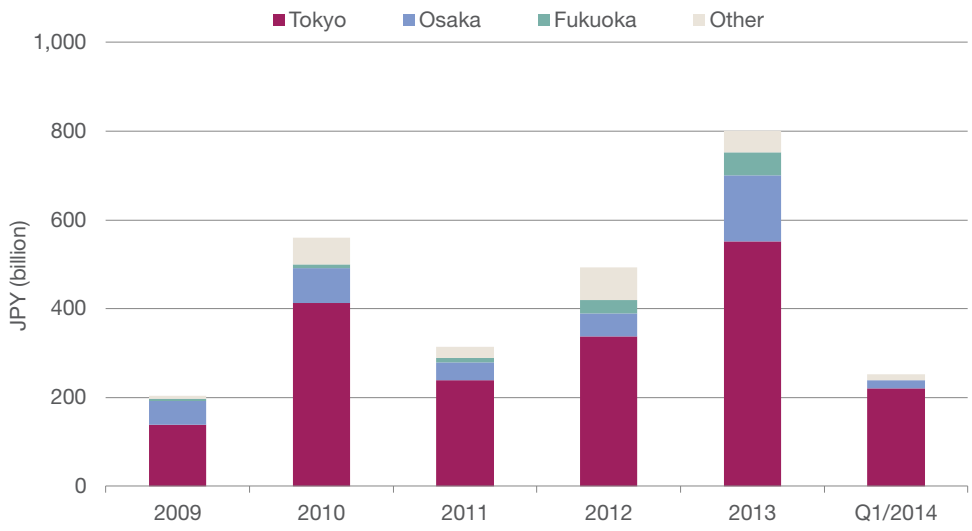
Ground floor (1/F) asking rents in major retail districts

District	Street	JPY per tsubo
Ginza	Chuo-dori	150,000 and above
	Harumi-dori	150,000 and above
Omotesando-Harajuku	Omotesando-dori	100,000–150,000 and above
	Takeshita-dori	100,000–150,000
Shinsaibashi	Shinsaibashisuji-shotengai	60,000–100,000
	Mido-suji	60,000–80,000
Tenjin	Tenjin-nishi-dori	50,000– 60,000

Source: Savills Research & Consultancy based on Attractors Lab and BAC Urban Projects, as of spring 2014

GRAPH 6

Retail property transactions by area, 2009–Q1/2014



Source: Savills Research & Consultancy based on RCA data

4.2. Robust pick-up in domestic investor appetite for retail assets

In 2013, domestic purchasers dominated retail investment activity, with J-REITs, local private investors and listed companies accounting for approximately 35%, 20% and 18% of the total transaction volume respectively.

We expect this trend to continue in 2014, with the largest transaction to date being department store operator Takashimaya's purchase of a 60% ownership interest in the Times Square Building near Tokyo's JR Shinjuku Station for JPY105 billion (approximately US$1 billion). Takashimaya already owned a 40% interest in the 174,500-sq m property, where its Shinjuku department store is located.

While outstripped by demand from domestic entities, cross-border investment in retail properties in Japan has increased steadily over the last two years. In 2013, cross-border transactions totalled almost JPY100 billion, reflecting an increase of 10% YoY and accounting for approximately 12% of last year's total transaction volume.

4.3. Lower cap rates amid rising demand

In addition to the deal by Takashimaya, the first half of 2014 saw a number of sizable retail property acquistions conducted by J-REITs, listed companies and overseas investors.

Providing a yield benchmark in a prime Tokyo retail district was the purchase of Espoir Omotesando (renamed G-Bldg. Omotesando 02), Ralph Lauren's flagship store on Omotesando-dori, by Mitsubishi Corporation. The trading company paid a reported JPY35.2 billion for the high-street asset, reflecting an NOI yield of 3.7%. The buyer subsequently agreed to sell a 50% ownership interest in the building to Japan Retail Fund (JRF), a J-REIT for which it is a sponsor.

Another J-REIT, Orix JREIT (OJR), has been active in the retail market in recent quarters. Its acquisitions include JouLe Shibuya, a 3,000-sq m facility anchored by home furnishings retailer FrancFranc in Tokyo's Shibuya district. The purchase price was JPY7.55 billion, reflecting an NOI yield of 4.1%.

Outside of Tokyo's central business district, Croesus Retail Trust (CRT) acquired Luz Omori in Ota Ward and NIS Wave I in Tachikawa City. The deals increased CRT's portfolio to six properties and reflect NOI yields of 6.2% and 6.0% respectively. The Singapore-listed REIT has been active in Japan since mid-2013.

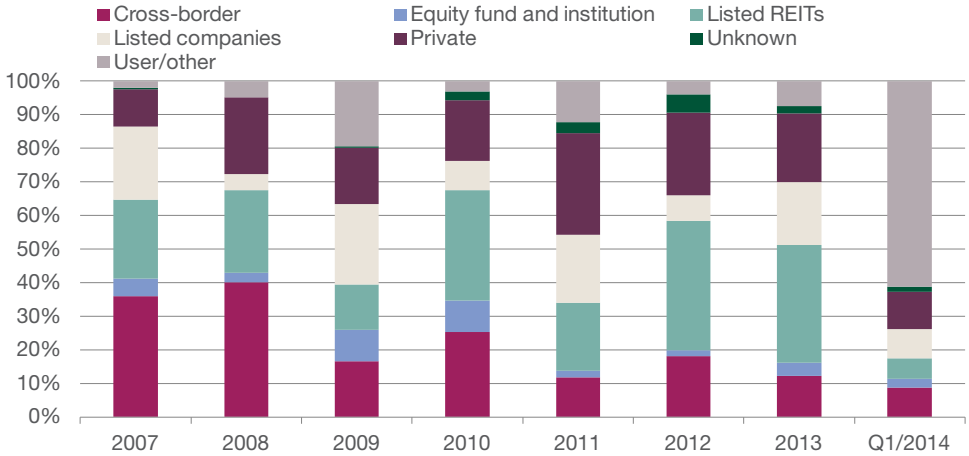
As location-focused buyers remain eager to enter the Tokyo market, we expect to see further compression in retail yields. Meanwhile, buyers with more flexibility are already starting to eye properties outside Tokyo, seeking higher returns.

Image: Espoir Omotesando, Shibuya Ward, Tokyo

Image: Takashimaya Times Square, Shinjuku Ward, Tokyo

GRAPH 7

Japan retail property acquisition volume by investor type, 2007–Q1/2014



Source: Savills Research & Consultancy based on RCA data

TABLE 3

Notable retail sales transactions, 1H/2014

Property	Location	GFA (sq m)	Price (JPY bil)	Cap rate (%)	Buyer
May					
Malera Gifu	Mitsuhashi, Motosu City, Gifu	117,000	21.0	N/A	LaSalle Investment Management
Apr					
Prime Square Shinsaibashi	Chuo Ward, Osaka City, Osaka	9,414	13.0	4.3	Elliott Management
JouLe Shibuya	Udagawacho, Shibuya Ward, Tokyo	3,032	7.55	4.1	ORIX JREIT
Mays One Building (G Bldg. Kichijoji 01)	Kichijoji, Musashino City, Tokyo	1,715	3.4	4.4	JRF / Mitsubishi Corp
Mar					
Takashimaya Times Square	Sendagaya, Shibuya Ward, Tokyo	101,855 (transacted)	105.0	N/A	Takashimaya
Espoir Omotesando (G-Bldg. Omotesando 02)	Jingumae, Shibuya Ward, Tokyo	5,556	35.2	3.7	Mitsubishi Corp
NIS Wave I	Akebonocho, Tachikawa City, Tokyo	10,534	10.8	6.0	CRT
Mitsui Shopping Park Lalaport Shin-Misato Annex	Shin-Misato, Misato City, Saitama	7,773	3.93	5.4	Frontier REIT
Luz Omori	Omorikita, Ota Ward, Tokyo	13,295	3.45	6.2	CRT
G-Building Shibuya 01	Jinnan, Shibuya Ward, Tokyo	1,894	3.23	4.7	JRF
Feb					
Tachikawa Takashimaya	Akebonocho, Tachikawa City, Tokyo	22,198 (transacted)	12.0	N/A	Takashimaya
Jan					
Primegate	Takadanobaba, Shinjuku Ward, Tokyo	4,340	5.5	N/A	SEB Asset Management

Source: RCA, Savills Research & Consultancy

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