MARKET IN MINUTES
Savills Research

Residential Leasing

savills

Recovery continues

Rents and occupancy rates have improved, and may be on the road to recovery.

- This quarter, rents in the Tokyo 23 wards (23W) improved 0.7% QoQ to JPY3,992 per sq m, although they have still decreased 1.3% YoY.
- Mid-market rents in the central five wards (C5W) have also increased 1.5% QoQ and 0.7% YoY to JPY4,784 per sq m.
- The C5W premium has inched up 0.9 percentage points (ppts) QoQ to 19.8%, surpassing the premium seen before the pandemic.
- Most wards have exhibited some recovery once again this quarter, with Edogawa posting the largest gain on a quarterly basis of 5.1%. On an annual basis, Toshima came on top, growing 4.9% YoY.
- In the C5W, average rents for all unit sizes have seen some rental increments this quarter.
- The average occupancy rate in the 23W increased 0.7ppts from the previous quarter to 96.8%. The C5W also saw a notable recovery of 0.6ppts to 96.2%.
- Prices of for-sale condominium have reached record-highs in Greater Tokyo. Some people will be priced out and stay in the rental market.

"Rents and occupancy rates have risen again over the past quarter, and the current spring season is likely to have contributed to this improvement. The lifting of restrictions on foreign nationals entering Japan and some decline in remote work should help further increase demand for housing in the 23W, especially the C5W. We will likely see more people move to Tokyo in 2022 than in 2021."

SAVILLS RESEARCH & CONSULTANCY

Savills team

Please contact us for further information

JAPAN

Christian Mancini
CEO, Asia Pacific
(Ex Greater China)
+81 3 6777 5150
cmancini@savills.co.jp

RESEARCH

Tetsuya Kaneko
Managing Director,
Head of Research &
Consultancy, Japan
+81 3 6777 5192
tkaneko@savills.co.jp

Yoshihiro Kanno
Senior Manager,
Research & Consultancy
+81 3 6777 5275
ykanno@savills.co.jp

Simon Smith
Regional Head of
Research & Consultancy,
Asia Pacific
+852 2842 4573
ssmith@savills.com.hk

MAP 1: Tokyo's 23 Wards by Survey Area

Source Savills Research & Consultancy

SURVEY GEOGRAPHY

In order to illustrate trends in the central Tokyo residential market, Savills has segmented Tokyo's 23 wards (23W) into seven distinct geographical areas: Central (or "central five wards"), South, West, North (Inner and Outer) and East (Inner and Outer).

RENTAL INDEX DATA CHARACTERISTICS

Savills collates thousands of leasing comparables each quarter in order to analyse trends affecting "mid-market" rental apartment units in Tokyo. Our benchmark rental data is based on average advertised monthly rents for units which fit the following criteria:

1) studio and one- or two-bedroom rental apartments of up to 100 sq m in size,

2) reinforced concrete structures built within the last ten years, and

3) properties located in Tokyo's 23 wards and situated within a ten-minute walk of the nearest station.

In contrast to the luxury residential market, advertised or "asking" rents for mid-market units fitting the above criteria are typically non-negotiable and are not subject to incentives such as rent-free periods. Savills mid-market rental indices are therefore considered to closely reflect movements in contract rents for the Tokyo market.

OVERALL RESULTS

Rents in both the 23W and C5W improved for the second straight quarter after decreasing for much of 2021. Furthermore, the number of available listings decreased by over 15%, marking the first decline seen since the pandemic begun. The moving season this spring is likely to have contributed to this improvement in the market, as Tokyo is expected to see a population influx from those seeking work and education.

The number of people moving to Tokyo this spring will likely be greater than what was seen last year as more companies have restarted their hiring processes after pausing them because of the pandemic. Indeed, the significant improvement in recent corporate earnings appears to have inspired greater confidence. Many companies are likely to continue a hybrid of predominantly going to the office and some remote work, suggesting that there is still an incentive to live closer to the city centre. Furthermore, restrictions on foreign nationals entering the country have been relaxed, providing another tailwind for Tokyo's population.

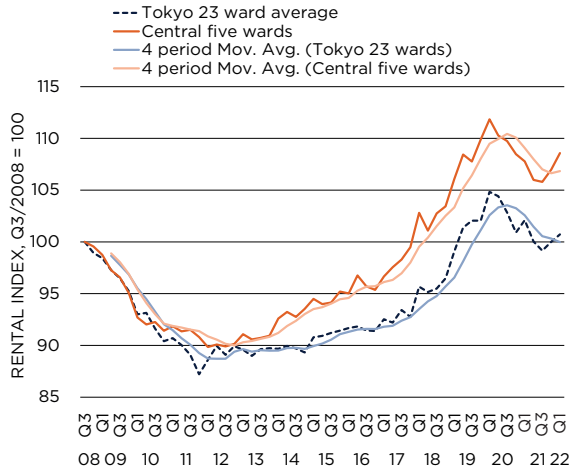
The C5W saw its premium over the 23W average increase 0.9ppts QoQ to 19.8%, and the premium of other more expensive submarkets like the Inner North and the South have also seen increments. According to a monthly survey conducted by the Tokyo Metropolitan Government, the amount of remote work in Tokyo in the past six months between September 2021 and February 2022 has decreased to 58.8% from an average of 61.3% in the previous six months. This will likely contribute to some residential demand shifting back to areas that are closer to the city centre.

MID-MARKET RENTAL TRENDS BY SURVEY AREA

In Q1/2022, although the multiple contractions over 2021 led to an annual decline of 1.3%, rents have inched up 0.7% QoQ to JPY3,992 per sq m in the 23W. In fact, most submarkets saw an uptick in rents, particularly those closer to the C5W. One key factor that likely contributed to this increment is the spring moving season that brings people into the city for work and education and is an important indicator for how rents will perform in 2022. Furthermore, restrictions on foreign nationals entering Japan have been eased, and more people are reportedly returning back to the office, all of which should drive demand for residences in the 23W. Overall, rents in more central areas have seen increments. On the other hand, other areas that performed well during the pandemic have generally seen some declines, reversing some of the growth seen. This could signal the beginning of the reversal of some of the trends induced by the pandemic.

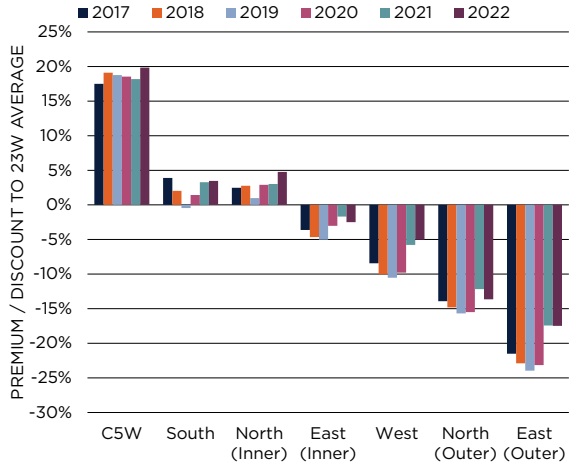
Looking more closely at the submarkets, the C5W has had good start to 2022, growing 1.5% QoQ to JPY4,784. It was also one of the few submarkets to post annual growth at 0.5%. At the ward level, Shibuya had the largest quarterly increment of 2.4% while Minato had the largest yearly increment of 2.0%. While Chuo's rents did not see increments this quarter, the ward may see improvements moving forward with the upcoming redevelopment projects in the area such as Tokyo Midtown Yaesu set to improve the liveability of the area. In addition, the relaxed border restrictions may also help drive demand in areas such as Shibuya, Shinjuku, and Minato, which have been traditionally popular with foreign residents.

GRAPH 1: Mid-market Apartment Rental Index, Q3/2008 to Q1/2022



Source Savills Research & Consultancy

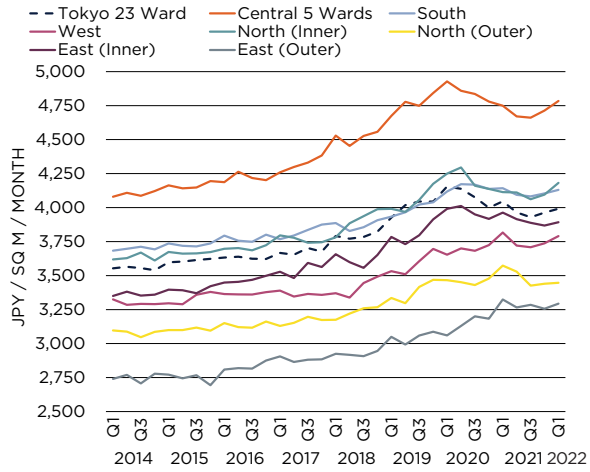
GRAPH 2: Rental Premiums/Discounts* vs 23W Average, 2017 to Q1/2022



Source Savills Research & Consultancy

* The above represents the average premium/discount over the respective year.

GRAPH 3: Mid-market Apartment Rents, Q1/2014 to Q1/2022



Source Savills Research & Consultancy

In the South submarket, rents grew for the second straight quarter at 0.6% QoQ to JPY4,130 per sq m. While the submarket saw a YoY correction of 0.3%, there were notable differences in the performances between its constituents. In particular, Setagaya was the only member to see annual growth of 3.4% while Meguro saw the largest quarterly growth of 1.6%. These areas are likely to remain popular as residential areas, particularly with families, given the amenities available and quick access to central areas.

The Inner North had both the largest quarterly and annual growth among Tokyo's submarkets at 2.1% QoQ and 1.7% YoY to JPY4,182 per sq m. Both wards within the Inner North saw a quarterly gain with Toshima and Bunkyo increasing 2.9% and 1.4%, respectively. However, the two wards exhibited diverging trends on an annual basis, with Toshima increasing 4.9% but Bunkyo decreasing 1.3%. That said, the rents of both wards are above pre-pandemic levels, and their proximity to the central wards may further boost their popularity as the pandemic winds down and people move back to Tokyo.

Although the Inner East decreased 1.8% YoY, it managed to see growth this quarter, increasing 0.6% QoQ to JPY3,892 per sq m. Quarterly growth was led by Taito at 1.0%, while Koto saw a minor increase of 0.7%. The population of the submarket has stayed almost flat since the end of the peak moving season in Q2/2021, signifying its overall popularity. Overall, the submarket's proximity to Chuo and Chiyoda, and relatively cheaper rents compared to other wards bordering the C5W may help the Inner East continue its gradual growth.

The West has had a decent start to 2022, increasing 1.4% QoQ to JPY3,791 per sq m, although it also saw a yearly dip of 0.7%. At the ward level, Suginami saw the largest increase of 2.5% QoQ, while Nakano saw an increase of 1.2%. Both wards saw a relatively large number of new units come to the market this quarter, which partially contributed to the quarterly growth. These two wards have a notable amount of greenery, and have convenient access into the city centre via the Chuo line, and are therefore likely to remain popular. The other ward in the submarket, Nerima, saw more subdued growth at 0.6% QoQ.

The Outer North had the smallest quarterly growth amongst all of Tokyo's submarkets at 0.2% to JPY3,447 per sq m. Kita declined 4.4% YoY and 0.2% QoQ while Itabashi followed a similar trend contracting 2.5% YoY, although it increased QoQ at 0.7%. While the Outer North has seen an annual decline, it should be noted that the submarket grew considerably during the pandemic, and that rents are still higher than pre-pandemic times. Moreover, its population has remained relatively stable into 2022 compared to the rest of the 23W, which is an encouraging sign for the submarket.

The Outer East submarket rebounded from the dip seen in the last quarter, growing 1.1% QoQ to JPY3,293 per sq m. At the ward level, Edogawa saw the largest quarterly increment of 5.1%. This growth could be partially attributed to a large uptake of units priced below the market average this quarter. On the other hand, Katsushika saw a decline of 2.4% QoQ. However, similar to the Outer North, the Outer East submarket also saw notable growth during the pandemic, and average rents are higher than pre-pandemic times. In fact, average rents in the submarket as a whole are still close to record levels, and have overall seen the most growth throughout the pandemic.

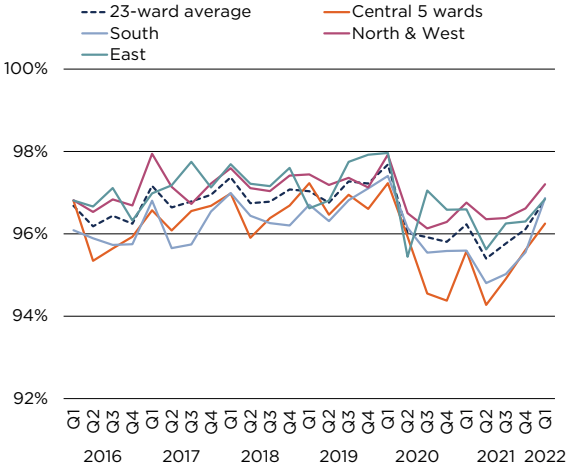
OCCUPANCY RATES

Although the population of the 23W has declined by 43,000 people since the end of the peak moving season in Q2/2021, J-REIT occupancy rates have not been negatively affected. In fact, occupancy rates in the 23W increased 0.7ppts from the previous quarter to 96.8%. The C5W also saw a notable increment in occupancy rates of 0.6ppts QoQ to 96.2%. Occupancy rates in other submarkets have also exhibited marginal increments over Q1/2022 and are above levels seen in the same period of the previous year, showing that demand was sound throughout the 23W. Nonetheless, it should also be noted that J-REITs tend to adjust rents in order to maintain high occupancy rates.

Currently, occupancy rates are around their highest levels since the pandemic began, suggesting that the demand for high-quality residences remains. Given the potential adoption of the hybrid work model by most companies, larger and high-quality residences within the 23W are likely to remain desirable for the time being. However, in line with the cyclic trend that follows the spring moving season, a dip in occupancy levels is expected in the subsequent quarter, and we will have a clearer picture of the demand for 2022 when this dust settles.

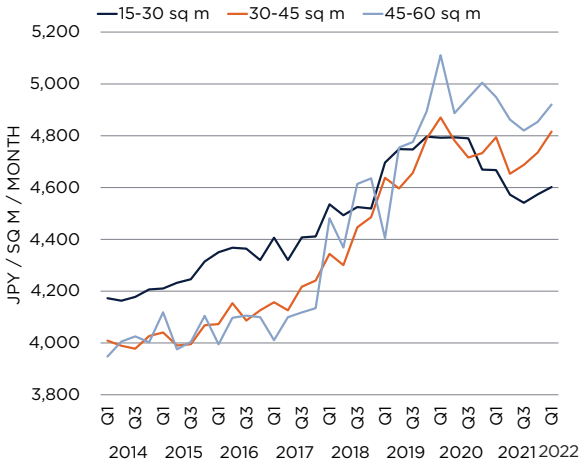
Nonetheless, there are optimistic signs for residential demand in Tokyo for 2022. The extent of remote work has decreased when compared to its peak during the pandemic, and restrictions on foreign nationals entering the country were relaxed in March. As such, demand is expected to improve when compared to 2021 given the current circumstances.

GRAPH 4: Average Occupancy for J-REIT Residential Assets, Q1/2016 to Q1/2022*



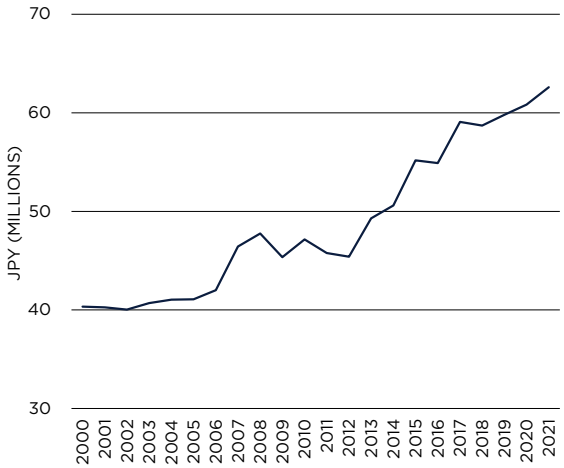
Source Savills Research & Consultancy based on publicly disclosed J-REIT property data.
*Q1/2022 is as of February 2022.

GRAPH 5: Rents by Unit Size, C5W, Q1/2014 to Q1/2022



Source Savills Research & Consultancy

GRAPH 6: Average Price of New Condominium in Greater Tokyo, 2000 to 2021



Source Real Estate Economic Institute, Savills Research & Consultancy

RENTS BY UNIT SIZE

Tokyo's rental market is principally made up of compact single-occupier units, typically less than 45 sq m (13.6 tsubo) in size. Such units can often make up as much as 75% or more of the 23W area's rental listings. Unlike other major global cities such as London and New York, house or apartment sharing does not form a major segment of the rental market. As a result, there is a large, stable market for small- to mid-sized units.

All size bands in the C5W have seen upticks in rents in line with the overall rental increment observed in the market. In detail, the smaller size band of 15-30 sq m increased by 0.6% QoQ. This size band typically caters to single residents, and comprises most of the rental unit supply in the C5W. It was the most affected by the pandemic because fewer of its target demographic moved into Tokyo than in previous years, and it is likely to take longer than other size-bands to recover.

Meanwhile, the 45-60 sq m band rose 1.4% QoQ while the 30-45 sq m band saw an increase of 1.7% QoQ. Looking at the overall trend compared to pre-pandemic times, the premium of larger size bands over the smaller 15-30 sq m size band has increased, likely due to the prolonged pandemic extending remote work arrangements. The degree to which the hybrid model and other flexible working arrangements become established will likely be a determining factor for the popularity of larger residences moving forward.

FOR-SALE RESIDENTIAL MARKET IN TOKYO

The residential rental market in Tokyo, while still sound overall, has corrected slightly because of the pandemic. On the other hand, the prices of for-sale condominiums have continued their upward trend. Indeed, according to the Real Estate Economic Institute, average prices for new condominiums in Greater Tokyo reached JPY62.6 million in 2021, surpassing the peak of the bubble era. Within the 23W, prices are also approaching all-time highs and stand at an average of JPY82.9 million. The contract rate for new condominiums averaged above 70% in 2021, showing that the market has been receptive despite the high prices. Furthermore, the second-hand condominium market has also seen prices increase in tandem, displaying that there is strong demand for for-sale condominiums overall.

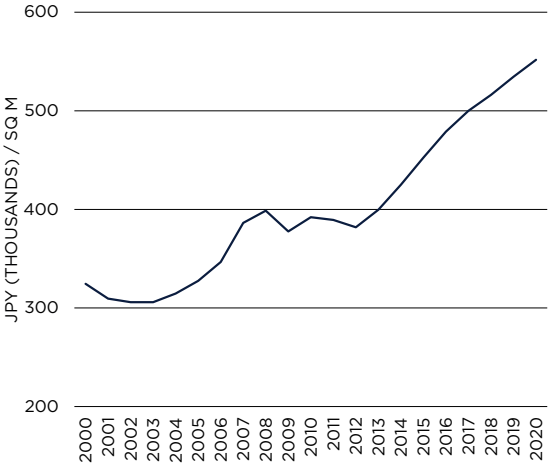
A few factors have contributed to these high prices. From a demand-side perspective, interest rates have been kept at historical lows, and the government also kept tax incentives for home buyers. In addition, the pandemic has also increased the average amount of time spent at home due to remote work, consequently increasing the amount of desired space in the home. Large rental units are more difficult to find, and this may have been enough of an impetus for some to look to the for-sale market instead. From a supply-side perspective, land prices and construction costs have been rising. The cumulation of these factors has led to a decrease in supply of new condominiums. In fact, the new condominium supply over the past decade was about half the supply of the previous decade.

Going forward, the growing difficulty of securing land suitable for developing for-sale condominiums is likely to continue pushing land prices up, and further tighten new supply. Labour shortages in the construction industry and increasing commodity prices are unlikely to disappear soon, and this will put additional pressure on supply. In addition, the historically low interest rates in combination with high housing demand also suggest that the prices of new and second-hand condominiums still have room to grow. Unlike the bubble era, mortgage rates are significantly lower, meaning that overall payments are also lower when factoring the cost of the loan, and the housing supply is around a third of what it was then. Global interest rate hikes may also prompt some to expedite the buying of properties. The number of dual-income households has also increased as more women have entered the workforce, and these households with greater purchasing power are likely to contribute to strong housing demand. Even if high prices were to cause contract rates to dip, major developers with healthy balance sheets control more than 50% of the condominium supply, and are unlikely to lower prices soon.

At the same time, there are some potential concerns in the market. For instance, the price of an average new condominium in the 23W was JPY82.9 million in 2021, around 19 times the average annual taxpayer's income in Japan. While this may question the affordability of new condominiums in the 23W, it should be noted that prices are still significantly cheaper than cities such as Hong Kong or London. Furthermore, the shrinking size of new condominiums might create some demand mismatch in a market that generally desires more space at home due to increased remote work and lead to some to consider landed properties instead.

With condominium prices rising, some potential buyers might gradually be priced out of the for-sale market and have to stay in the rental market. This should provide some additional support for the growth of the rental market. Indeed, many international investors have made large acquisitions of rental apartments in Tokyo in the past few years, showing the high levels of confidence for the sector in the market.

GRAPH 7: Average Price of Second-hand Condominium in Greater Tokyo, 2000 to 2020



Source REINS, Savills Research & Consultancy

OUTLOOK

In Q1/2022, rents saw a mild improvement from the previous quarter even though the population saw a decline. However, it should be noted that listed rents are generally a coincident indicator, while population changes are a lagging indicator. The population is expected to increase over the next quarter as many people are forecast to move to the capital for work and education. Occupancy rates have seen notable improvement, and the number of listings has gone down for the first time since the pandemic began, which are encouraging signs for the market.

While Tokyo has seen some exodus of its population during the period of the pandemic, a closer inspection reveals that a majority of those leaving are older than 40 years old and with kids younger than 9 years old. On the other hand, Tokyo has a large positive net migration of people in the 10-29-year-old age bracket – the young demographic that all cities are trying to attract. Tokyo will retain its popularity as a centre that people will flock to for employment and education opportunities. Furthermore, the capital's population decline is decelerating, and will likely reverse to some extent as the pandemic ends. In fact, in January 2022, the Ministry of Internal Affairs and Communications reported that there was a net increase in the number of people moving into Tokyo from other prefectures for the first time in nine months, which is an encouraging sign for the market.

Overall, there are many factors that should contribute to the recovery of the market in the 23W going forward. Firstly, restrictions on foreign nationals entering Japan have been relaxed, which should boost the demand for housing in the 23W. Furthermore, the amount of remote work has been decreasing, and people may therefore look to living closer to the office. While more people are expected to move to Tokyo this year than in 2021, we will have a clearer picture of the market and the outlook for the rest of the year once the spring moving season is over and the dust settles.