KENEDIX Real Estate Market Report 2Q 2022

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Contents

Summary

Net exports pushed down the real GDP growth rate in January-March 2022

The real GDP growth rate in January-March 2022 was down 1.0% QoQ at an annualized rate, returning to negative from positive in the previous quarter. A look at the contributions of individual items shows that the quasi-state of emergency implemented in various localities from January through March 2022 also had an impact, as consumption of households was down 0.1% due to restrained consumption in food-service, lodging, and other industries, while net exports were down for the first time in 3 quarters, falling by 1.7%, as a result of rising prices of imports due to factors such as rising energy prices and the depreciation yen.

At the end of March, the TSE REIT Index was down 3.1% from the end of December, as stock prices fell in Japan and U.S.

At the end of March 2022, the TSE REIT Index was down 3.1% from the end of December 2021. TOPIX was down 2.3% during the same period, while the J-REIT market underperformed. This reflected the impact of falling stock markets in Japan and the U.S. amid rising U.S. interest rates. A look at performance by asset type shows a pronounced decrease in logistics REITs, as pressure to sell these assets appears to have strengthened in particular as their prices seemed relatively high as a result of comparatively favorable performance through now. Occupancy rates in logistics facilities remained high, and the fundamentals do not seem to have worsened. It appears that there are no causes for concern about the current state of operation of logistics facilities.

Investors' expected yields remain in a downward trend

The amount of investment in commercial properties in January-March 2022 was down 37% YoY to JPY596 billion (CBRE). This level was low for the quarter January-March. However, investors' expected yields remained in a downward trend during this quarter, and there are no signs of investors' appetite for investment drying up. The real estate investors' expected yield on office buildings in Tokyo (Marunouchi and Otemachi districts) in April 2022 was down 0.1%pt from 6 months earlier, to 3.3%. This was the second consecutive half in which the expected yield decreased, as it fell to its lowest level since the survey began in 1999 (source: Japan Real Estate Institute, "Japanese Real Estate Investor Survey").

The vacancy rate in central Tokyo continues to fluctuate

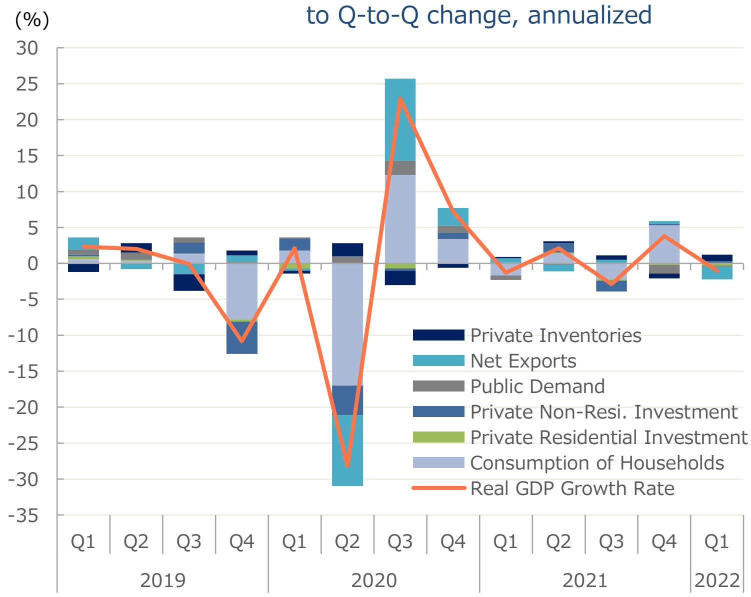
According to Miki Shoji, the vacancy rate in Tokyo business districts (the 5 central wards) stood at 6.37% at the end of March 2022, up 0.04%pt from the end of December 2021. While the vacancy rate in the 5 central wards of Tokyo had decreased for the first time in 7 quarters in the previous quarter (October-December 2021), it returned to an increasing trend this quarter, indicating that the central Tokyo office market continues to fluctuate. Cases also are apparent of office relocations for forward-looking reasons such as improving locations or building grades or expanding office space in current buildings. For this reason, conditions in the office market cannot be said to be worsening. Still, for reasons including lease terminations due to review of office strategies and the planned increase in completion of construction on new large-scale office buildings in 2023, it would appear to be difficult to expect a clear improving trend under these circumstances.

【Macroeconomic Conditions】

The real GDP growth rate in January-March 2022 decreased owing to lower net exports as a result of rising prices of imports due to factors such as rising energy prices and the depreciation yen

The real GDP growth rate in January-March 2022 was down 1.0% QoQ at an annualized rate (seasonally adjusted), returning to negative growth (Fig.1). The contributions of individual items show that the quasi-state of emergency implemented in various localities from January through March 2022 also had an impact, as consumption of households was down 0.1% due to restrained consumption in food-service, lodging, and other industries, while net exports were down for the first time in 3 quarters, falling by 1.7%, as a result of rising prices of imports due to factors such as rising energy prices and the depreciation yen.

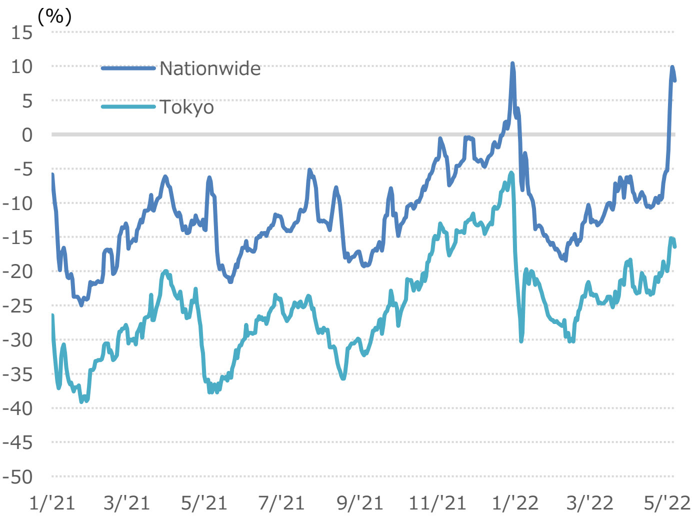
【Fig.1】Real GDP Growth Rate and Contributions to Q-to-Q change, annualized



Source : The Cabinet Office

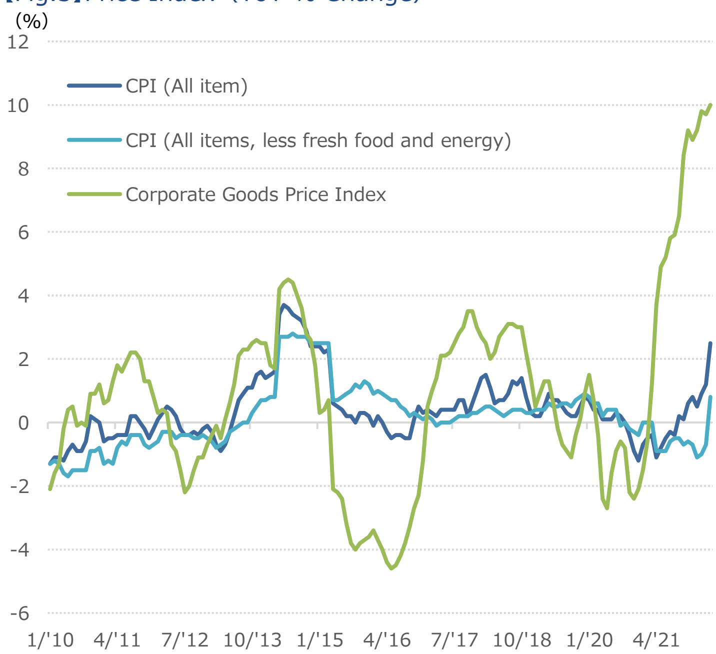
As of March 21, 2022, the quasi-state of emergency had been released in all localities, and the Golden Week holidays in May 2022 were the first ones in 3 years to be subject to no transit restrictions. These factors led to progress in recovery of consumer flows, and the trend was clear at retail, entertainment, and other facilities nationwide (Fig.2). The difference in the strength of the recovering trend is clear from a comparison with Golden Week 2021. Consumer expenditures (monthly average per household of 2 or more persons) from the 2021 Family Income and Expenditure Survey published by the Ministry of Internal Affairs and Communications, as a related indicator, show a real YoY increase of 0.7%, with the transport and communication sectors contributing. It can be expected that consumption will improve further in the future as well, as social activities return to normal in the absence of transport restrictions. In addition, the Japanese government has announced that it will ease containment measures against COVID-19 by increasing the maximum number of people admitted to the country from 10 thousand to 20 thousand per day beginning in June 2022. Stimulation of consumption activities from travelers visiting Japan from overseas is one key to Japan's economic recovery.

【Fig.2】Mobility Report (Retail & Recreation)



Note 1 : Retail, Entertainment point to a place such as restaurant, cafe, shopping center, theme park, museum, library, movie theater.
Note 2 : This data gives the rate of change of the numbers of visitors and staying time from the baseline day on a daily basis (7 days Moving Average) . The baseline day is the median value from the 5-week period Jan.3 2020- Feb.6 2020.
Source: Google LLC "Google COVID-19 Community Mobility Reports".

【Fig.3】Price Index（YoY % Change)



Source : Ministry of Internal Affairs and Communications, Bank of Japan

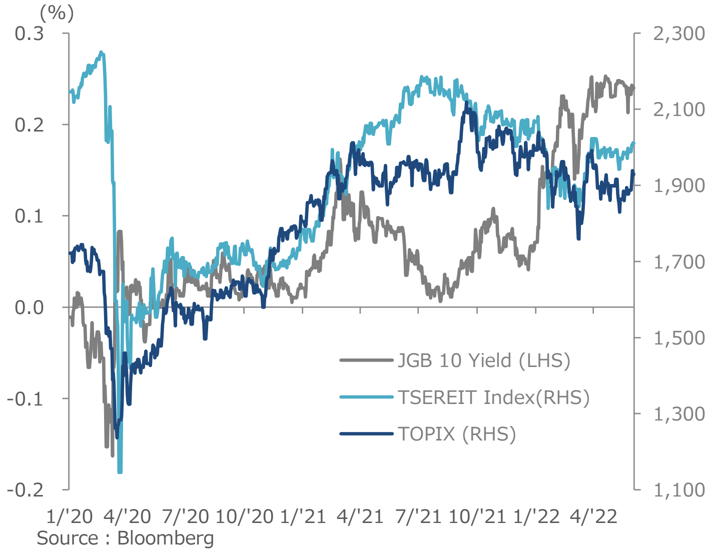
At the same time, progressive inflation, pushed by costs, is one current economic risk factor. The (national) consumer price index (CPI) (all items) in April was up 2.5% YoY, while core-core CPI (excluding fresh food and energy) was up 0.8% YoY, as the increase in general prices was driven mainly by fresh seafoods, fresh vegetables, and electricity (Fig.3). The increase in electricity prices reflects the strengthening increase in oil prices since 2021, due to growing demand as the global economic recovery, as well as a continuing increase due to disorder caused by the Ukrainian situation in 2022, along with rising prices of liquefied natural gas (LNG) due to the situation. While the rate of increase in core-core CPI (excluding fresh food and energy) had remained negative, in this period it rose into positive territory for the first time in 21 months. The corporate goods price index in April also was up 10.0% YoY, reaching double digits for the first time in about 41 years, since it recorded +10.4% in December 1980 due to the effects of the second oil crisis. There is a risk that passing along to consumers these increases in costs of corporate transactions on a wide range of products could have a negative impact on consumption.

【J-REIT Market】

The TSE REIT Index at the end of March was down 3.1% from the end of December, as stock markets fell in Japan and the U.S. amid rising U.S. interest rates

At the end of March 2022, the TSE REIT Index was down 3.1% from the end of December 2021 (Fig.4). TOPIX was down 2.3% during the same period, while the J-REIT market underperformed. This reflected the impact of falling stock markets in Japan and the U.S. amid rising U.S. interest rates. As the FRB showed signs of actively raising interest rates amid rising inflationary pressures in the U.S., the interest rate on 10-year U.S. Treasuries has been rising since the start of 2022, reaching 2% in February. The upward pressure accelerated March 15-16 when the Federal Open Market Committee (FOMC) raised interest rates by 0.25%. There has been a succession of comments acknowledging continual increases from high-ranking FRB officials as well. Under such conditions, U.S. stock markets have been bearish since the start of 2022, and this has put downward pressure on Japanese stock markets as well. In April as well, concerns including warnings of interest rate increases by the FRB, risks of a slowdown in the Chinese economy, and prospects for the Ukrainian situation led to bearish stock markets in Japan and the U.S., and the TSE REIT Index fell 1.4% from the previous month. Furthermore, the FRB raised interest rates by 0.5% at the FOMC on May 3-4 and decided on balance-sheet shrinking (quantitative tightening [QT]) beginning in June, causing rates on 10-year U.S. Treasuries to rise above the 3% level.

【Fig.4】TSE REIT Index, TOPIX, JGB 10 Yield



Source : Bloomberg

A look at REIT performance in January-March 2022 by asset type shows an increase of 1.6% for office REITs and decreases of 5.7% for residential REITs, 2.4% for retail REITs, and 11.1% for logistics REITs. The decrease in logistics REITs was particularly pronounced (Fig.5; calculated by Kenedix based on the SMTRI J-REIT Index® from the Sumitomo Mitsui Trust Research Institute). In the previous period, performance of office REITs was down 5.1%, for the only decrease among the asset types, but this period it showed a steady tone. Performance of logistics REITs has been comparatively strong until now, and it appeared that a sense that pressure to sell was strengthening particularly as prices seemed overvalued, but logistics facility occupancy rates remain high and their fundamentals are not worsening. Rent amounts continued to increase at REITs such as Japan Logistics Fund, Inc. and Nippon Prologis REIT, Inc., which announced their financial results during this quarter, and it appears that under current conditions there is slight concern about the state of operation of logistics facilities.

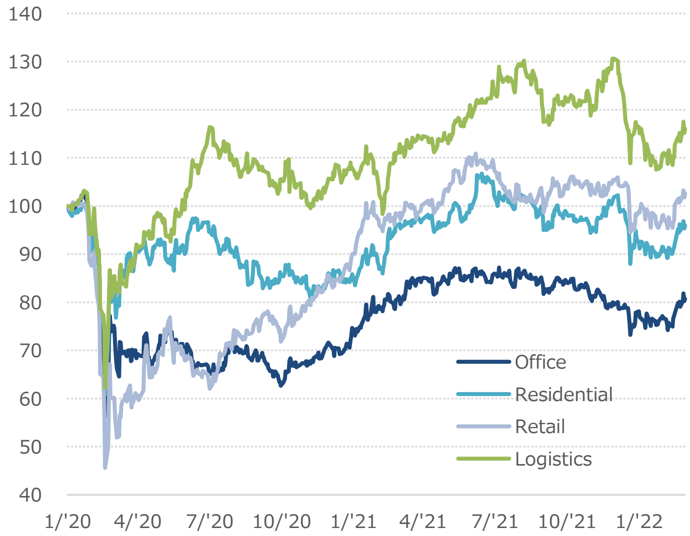
While as noted above the TSE REIT Index decreased in January-March 2022 and dividend yields at the end of March were up approximately 13bp to 3.67% from 3.54% at the end of December 2021, during the same period the interest rate on 10-year JGBs rose by approximately 15bp, affected by rising interest rates on 10-year U.S. Treasuries, and the yield spreads decreased by approximately 2bp. The yield spreads in the U.S. decreased by approximately 53bp due to rising interest rates on 10-year U.S. Treasuries, despite increased dividend yields. The NAV ratio at the end of March was 1.07 times, falling from its level of 1.14 times at the end of December 2021 due to decreasing unit prices.

The NAV ratio remained above the level of 1 time. POs continued at the start of the year and were up +59.3% YoY in January-March 2022

Ten public offerings (POs) were carried out by J-REITs in January-March 2022, totaling JPY130 billion. Since the level was low at JPY81.6 billion in the same quarter last year, YoY growth was 59.3% (Fig.6; based on payment dates). While the NAV ratio decreased from 1.14 times at the end of December 2021 to 1.07 times at the end of March, since it remains greater than 1 and is at a level at which capital increases are possible there has been a steady stream of POs since the start of the year.

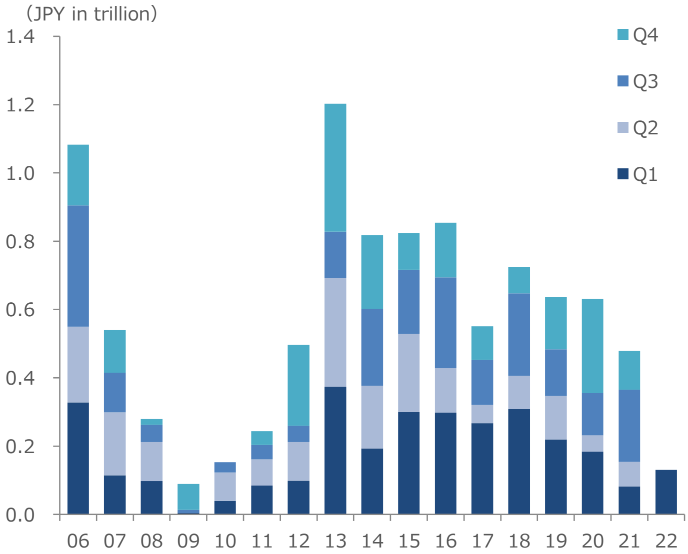
The amount of property acquisitions by J-REITs in January-March 2022 were down 18.8% YoY, to JPY360.2 billion, despite the fact that POs increased over the same period. A major contributor was the impact of the jump in acquisitions in January to JPY246.8 billion during the same quarter last year. In January 2021, Nippon Building Fund Inc. acquired the Shinjuku Mitsui Building for JPY170 billion. When this deal is omitted, acquisitions in January-March 2022 were up 31.8% YoY. In addition, amid uncertain internal growth prospects office REITs are making progress on portfolio improvements through replacement of asset portfolios. Nippon Building Fund Inc. announced the acquisitions of the Nakanoshima Mitsui Building for JPY44 billion and Iidabashi Grand Bloom (additional acquisition) for JPY36.2 billion in March 2022 and the sale of a total of 3 properties including provincial ones for JPY17 billion in July 2022.

【Fig.5】Price Performance by Asset Type (Jan.2020＝100)



Source : Sumitomo Mitsui Trust Research Institute "SMTRI J-REIT Index®"

【Fig.6】Amount of Public Offering by J-REIT



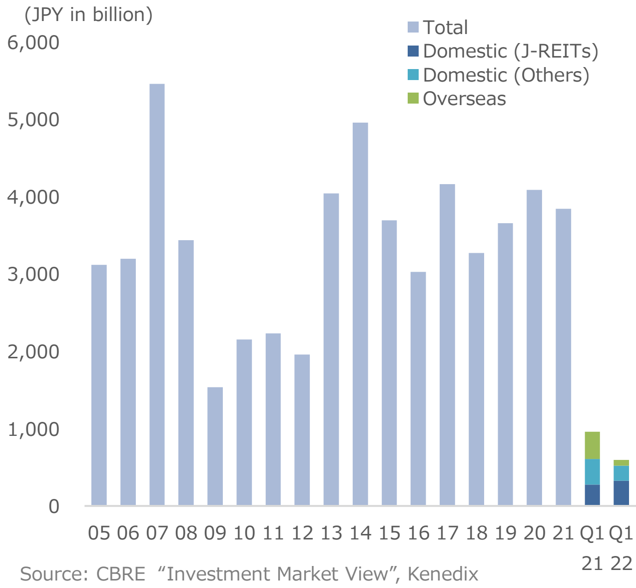
Source : The Association for Real Estate Securitization

【Real Estate Investment Market】

Commercial property transactions were down sharply YoY in January-March 2022

According to CBRE, the amount of investment in commercial real estate in January-March 2022 was down 37% YoY to JPY596 billion. This represents a substantial decrease YoY and probably could be described as a low level for the quarter January-March. While amounts of investment by both domestic and overseas investors decreased, it appears that this figure “was impacted by the small number of properties for sale, although investors’ appetite for acquisitions was strong” (according to CBRE, “Investment Market View”). As discussed below, investors’ expected yields remain in a decreasing trend this period, and there are no signs of investors’ appetite for investment diminishing. In February, it was reported that GIC (the Singaporean government’s sovereign wealth fund) would acquire 31 hotel and leisure assets owned by Seibu Holdings (for a total amount of approximately JPY150 billion) (The contract was concluded in May). In addition, although this is not a case of a property acquisition, in March the U.S. investment fund KKR announced that it would acquire all stock in Mitsubishi Corp.-UBS Realty Inc. (MC-UBSR), which manages Japan Metropolitan Fund Investment Corporation, etc. From these examples as well, it is surmised that there has been no major change in overseas investors’ appetite for investment in Japanese real estate.

【Fig.7】Major Transaction Volume by Investor Type



Source: CBRE “Investment Market View”, Kenedix

【Fig.8】Significant Deals

Property Name	Asset Type	Buyer	Prefecture	Value (JPY in bn)	TFA (sqm)	Date
Portfolio of 31 hotels and leisure properties	Hotel	GIC	Nationwide	approx. 150	-	May-22
Portfolio of 30 residential properties	Residential	M&G Asia Property Fund	Tokyo	49.2	-	Mar-22
Nakanoshima Mitsui Bldg.	Office	Nippon Building Fund	Osaka	44	67,672	Jan-22
Iidabashi Grand Bloom	Office	Nippon Building Fund	Tokyo	36.2	13,229	Jan-22
LOGIPORT Kawasaki Bay	Logistics	Mitsubishi Estate Logistics REIT	Kanagawa	36	130,455	Feb-22
Toyosu Front	Office	Japan Real Estate	Tokyo	25.5	25,124	Mar-22
Hitachi Solutions Tower	Office	Hulic	Tokyo	25	38,908	Mar-22
MFLP Yachiyo Katsutadai	Logistics	Mitsui Fudosan Logistics Park	Chiba	18	74,624	Jan-22
PASCO Megro Sakura Bldg.	Office	Hulic	Tokyo	-	8,658	Nov-21
ShinYokohama TOSHIBA Bldg.	Office	Lasertec	Kanagawa	16.7	28,822	Feb-22
Japan Oi Warehouse	Logistics	Dai-ichi Life Insurance, SPC of Prologis	Tokyo	16.1	48,945	Apr-22
MFLP Osaka I	Logistics	Mitsui Fudosan Logistics Park	Osaka	13.9	43,919	Jan-22
MFLP Hiratsuka II	Logistics	Mitsui Fudosan Logistics Park	Kanagawa	12.7	48,141	Jan-22
4 residential properties and a Student House	Residential etc.	Ascott Residence Trust	Osaka etc.	10.4	-	Mar-22

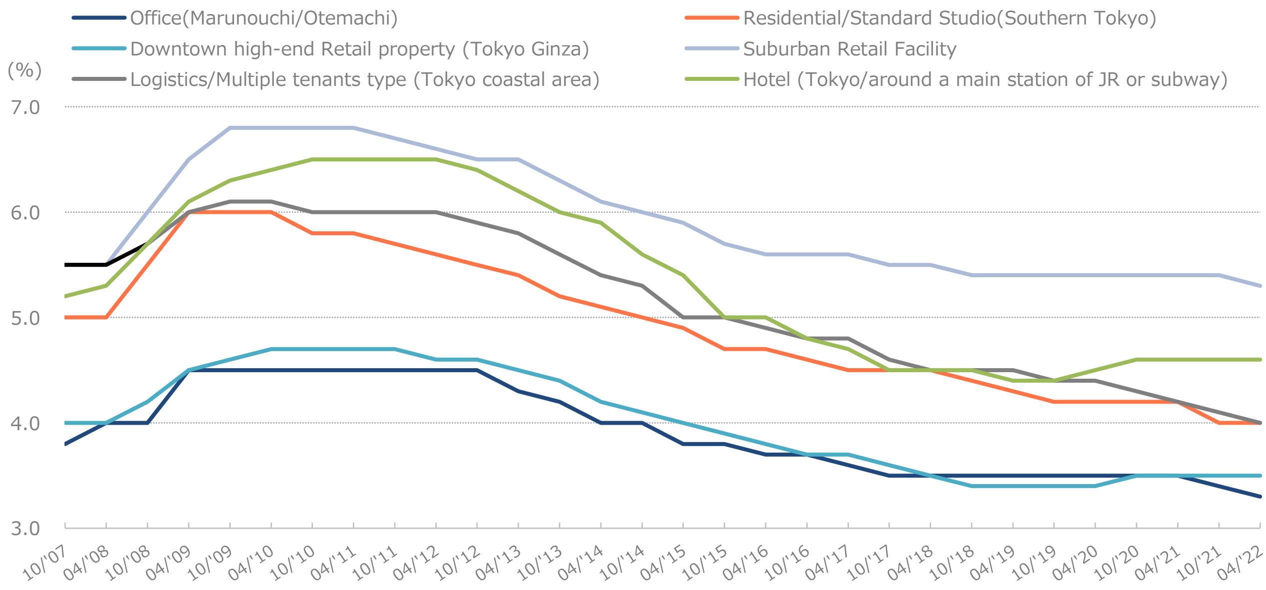
Source: Companies publication documents, News reports, Kenedix

Real estate investors' expected yields remain in a decreasing trend

Real estate investors' expected yields on office buildings in Tokyo (Marunouchi-Otemachi) in April 2022 were down 0.1%pt from 6 months earlier, to 3.3%. This was 2 consecutive half-year periods in which expected yields decreased, as they fell to their lowest level since the survey began in 1999 (source: Japan Real Estate Institute, "Japanese Real Estate Investor Survey"). Over the same period, expected yields on residential properties (southern Tokyo) remained unchanged for single-type residences but fell by 0.1pt for family-type residents, decreasing for 2 consecutive half-year periods to 4.1%. Expected yields on logistics facilities (multi-tenant facilities in the Tokyo Bay area) also decreased for 2 consecutive years to 4.0%. While expected yields on urban retail facilities (Tokyo/Ginza) remained unchanged, expected yields on suburban-type shopping centers (Tokyo) fell by 0.1%pt over the same period, to 5.3%. This is the first time in 4 years that expected yields on suburban-type shopping centers have decreased, a possible sign of a change in investors' views on this asset type. Expected yields on hotels (limited service hotels in Tokyo) remained unchanged over the same period, at 4.6%.

Despite some variation by asset type, investors' expected yields showed a decreasing trend in general. This can be said to be a sign of the continued strength of appetite for investment. The answers to another question on office rents asked at the same time in the same survey show that rent levels 2 years after are expected to be down from current levels (with a projected level of 99 vs. a current level of 100 in Tokyo/ Marunouchi-Otemachi). At the same time, when asked about their anticipated real estate investment activity in next 12 months, 93% of respondents answered that they would "actively make new investments", a sign that appetite for investment is likely to remain high in the future as well. In consideration of the fact that the current environment is not one in which it would be easy to increase rents even on non-office assets, there is a possibility that expected yields could decrease further.

【Fig.9】NOI Cap Rate (Expected Yield)



Source: Japan Real Estate Institute "Real Estate Investor's Survey, Kenedix

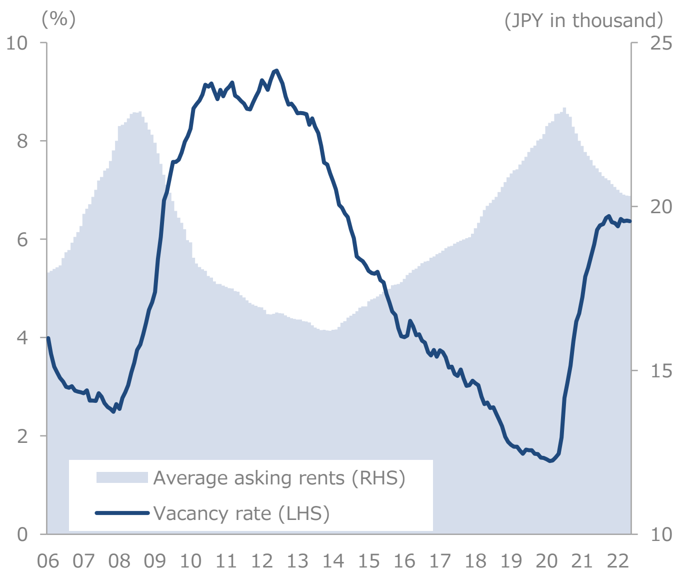
【Office Market】

The vacancy rate in central Tokyo continues to fluctuate

The vacancy rate in Tokyo business districts (the 5 central wards) announced by Miki Shoji stood at 6.37% at the end of March 2022, up 0.04%pt from the end of December 2021. While the vacancy rate in the 5 central wards of Tokyo had decreased for the first time in 7 quarters in the previous quarter (October-December 2021), it increased again this quarter, indicating that the central Tokyo office market continues to fluctuate. During this period, several new medium-sized office buildings were completed, and leasable floor area rose by approximately 20 thousand tsubo. However, the increase in vacant floor area was only about 4.7 thousand tsubo, and occupied floor area increased by 16.1 thousand tsubo. It seems unlikely that the vacancy rate alone would increase under these circumstances since demand conditions appear favorable.

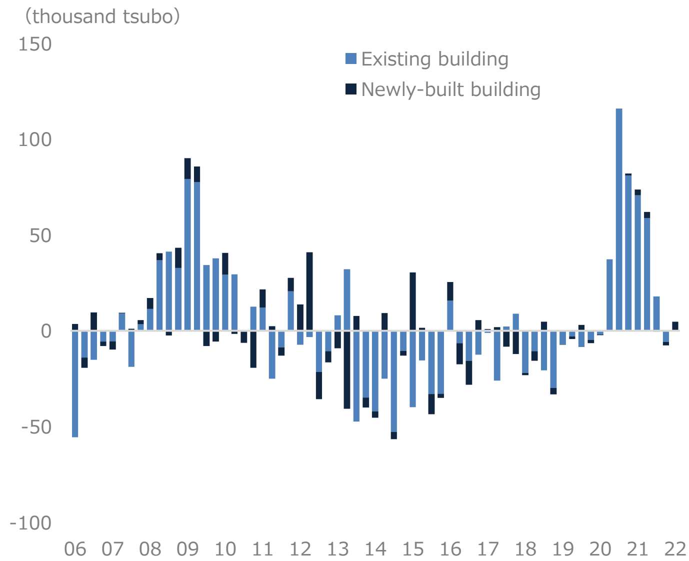
According to Sanko Estate, contracted floor area in the 23 wards of Tokyo in January-March 2022 was in a recovering trend, up 7.6% YoY to 238 thousand tsubo. At the same time, available floor space increased by 43 thousand tsubo QoQ, and the total vacancies area has not decreased. This is probably because there is new supply and net absorption does not grow. While net absorption in October-December 2021 was +15.9 thousand tsubo, it returned to negative territory at -1.7 thousand tsubo this quarter, and it can be surmised that lease cancellations remain at a certain level. Tenants seem to have consolidated office space or partially canceled leases as part of a review of corporate office strategies in response to the spread of teleworking, although cancelations due to the economic downturn appear to have levelled off to some degree. However, some positive trends such as relocation to larger spaces also are apparent, so that the picture does not seem to be one of uniform worsening of conditions.

【Fig.10】Vacancy Rate in Tokyo Central 5 ward



Source: Miki Shoji, Kenedix

【Fig.11】Changes in Vacancy Area in Tokyo Central 5 Ward



Source: Miki Shoji, Kenedix

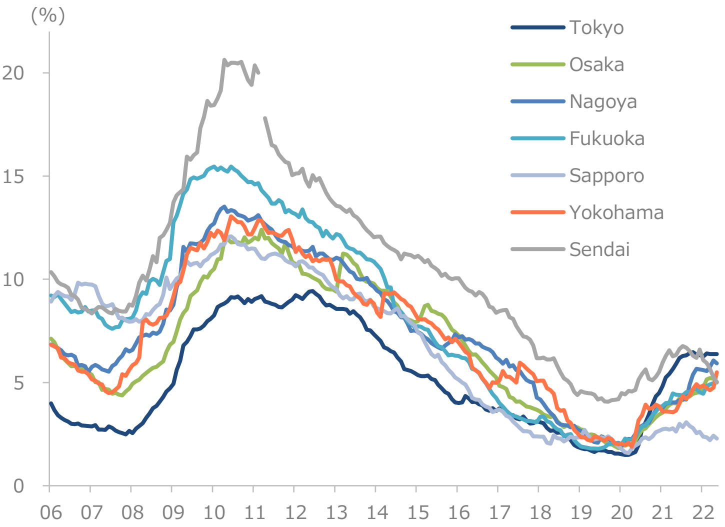
The decrease in contracted rent on class-A buildings is pronounced

According to the Office Rent Index, which is an office market index based on contracted rent developed and published jointly by Sanko Estate and NLI Research Institute, office rents in central Tokyo in January-March 2022 were down 4.9% QoQ to JPY29,185 (per month per tsubo, excluding common area charges, hereinafter the same) on class-A buildings, down 2.3% QoQ to JPY19,726 on class-B buildings, and up 1.9% QoQ to JPY17,438 on class-C buildings. This is the first time rent on class-A buildings has fallen below JPY30 thousand since April-June 2014. On the other hand, rent on class-C buildings has risen for 2 consecutive quarters, while rent on class-B buildings remains largely unchanged. While there seems to be a level of demand for small and medium-sized spaces, it appears to be difficult to fill large spaces in some cases. The supply of large-scale office buildings in the 23 wards of Tokyo is projected to rise sharply in 2023 by approximately 2.6 times vs. 2022, to 1.28 million sqm, and there is a possibility that office building owners are employing a flexible approach to pricing. Since listed companies appear to have shown a record high in net income (for the period ended March 31, 2022), the business results in general are not poor. Cases also are apparent of office relocations for forward-looking reasons such as moving to better locations or buildings or expanding office space in current buildings. For this reason, conditions in the office market cannot be said to be worsening. Still, for reasons including the expected continuation of lease terminations due to review of office strategies and the planned increase in completion of construction on new large-scale office buildings in 2023, it would appear to be difficult to expect a clear improving trend.

Vacancy rates rose in 3 urban areas due to completion of newly constructed office buildings with vacancies remaining

A look at vacancy rates in the major urban areas as of the end of March 2022 shows increases from the end of December 2021 in 3 cities—by 0.69%pt to 5.22% in Osaka, by 0.11%pt to 5.75% in Nagoya, and by 0.37%pt to 4.90% in Fukuoka—and decreases over the same period in 3 cities: by 0.40%pt to 2.21% in Sapporo, by 0.14%pt to 4.63% in Yokohama, and by 0.92%pt to 5.67% in Sendai. In each of the cities where the vacancy rate increased, leasable floor area has increased, and the vacancy rate appears to have been impacted by new supply. In Osaka in particular, 5 newly constructed office buildings, including Osaka Umeda Twin Towers South (with total floor area of approximately 78 thousand tsubo) were completed during this period, and each appears to have been completed with vacancies remaining. It also appears that secondary vacancies arose in connection with relocations to newly completed office buildings. The vacancy rate in Sapporo fell for the third consecutive quarter, while that in Sendai fell for the first time in 2 quarters. According to CBRE, "Increasingly, companies nationwide are seeking to improve their office environments in order to strengthen hiring, and relocations to higher-grade office buildings or better locations are on the rise." Since they are smaller in scale than Tokyo, the vacancy rate in the office markets in provincial cities tends to rise with new supply, but it appears that underlying demand trends are favorable in general.

【Fig.12】Vacancy Rate in Major City



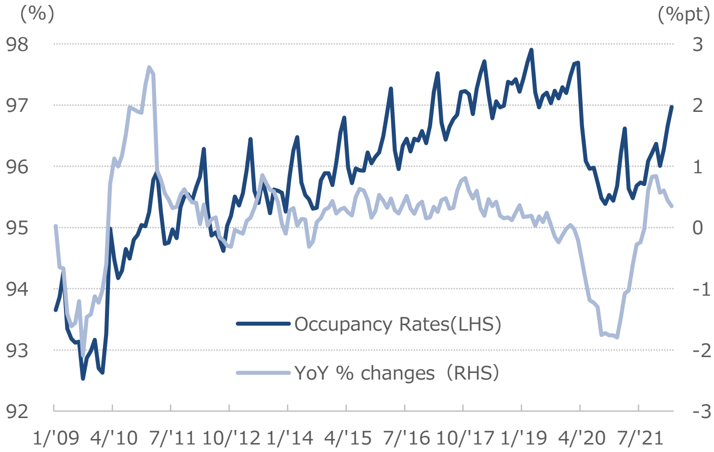
Note : Data is absent in March 2011 in Sendai

【Residential Market】

While the occupancy rate on rental residences in the greater Tokyo area at the end of March 2022 was up YoY, it has not yet recovered to its pre-COVID levels

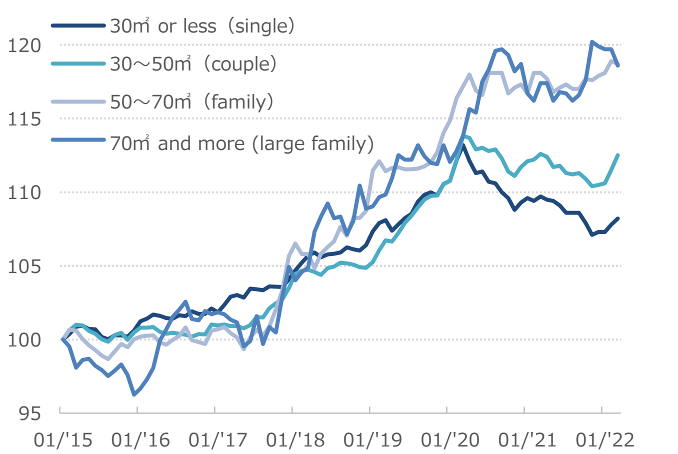
The occupancy rate on rental residences in the greater Tokyo area owned by the leading residential REITs was up 0.3%pt to 97.0% at the end of March 2022, as the rate continues to recover. It has not yet, however, returned to its levels in the same month in 2020 or 2019 (before the effects of COVID-19) (Fig.13). Asking rent in March was down 1.4% YoY on residences of 30 sqm or less, down 0.1% YoY on those of 30-50 sqm, up 0.5% YoY on those of 50-70 sqm, and up 1.0% on those of more than 70 sqm (Fig.14; calculated by Kenedix based on the trends in asking rents for apartments published by At Home Co., Ltd.). Regarding rents for single-type residences of 30 sqm or less, the decreasing trend YoY continued along with the trend among consumers toward preferring more spacious residences in light of restrictions on going out and growth in teleworking due to COVID-19. On the other hand, rents continue to improve YoY on residences of 50-70 sqm and those of more than 70 sqm, which are better able to accommodate demand from family households. Market conditions overall show that the trends continue toward difficulties for single-type residences while family-type residences recover.

【Fig.13】Occupancy Ratio of Rental Residencies



Source : Monthly data announced by major residential REITs

【Fig.14】Rental Residencies Rent Index in Tokyo 23 Wards



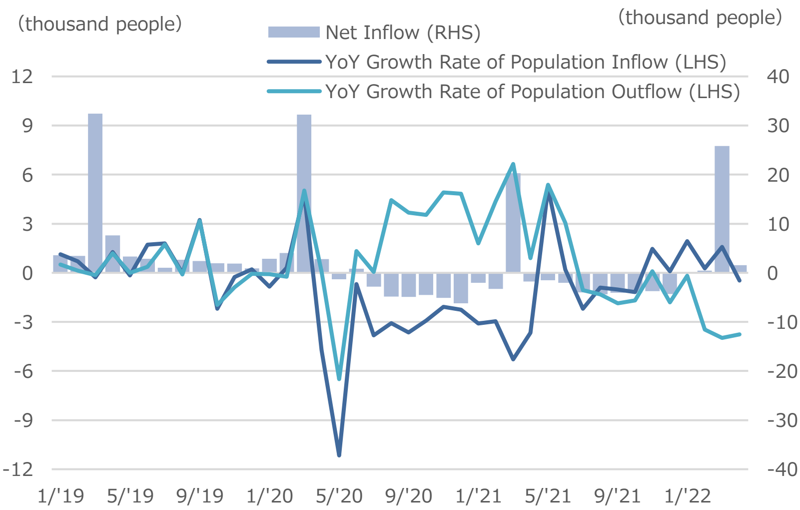
Source : At Home Co, Ltd.

The inflow of population to the 23 wards of Tokyo is recovering, as an increase in inflow and a decrease in outflow combined for a net inflow

The population of the 23 wards of Tokyo showed a net inflow of 26,336 in January-March 2022, up 11,407 YoY, as 131,113 people moved in to the 23 wards (up 3,801 YoY) while 104,777 moved out (down 7,606 YoY) (Fig.15). YoY comparison shows an increase in population inflow and a decrease in outflow, resulting in an increase in the net inflow—a positive sign for potential demand in the rental market in the 23 wards. At the same time, the net inflow remains low compared to those of 39,066 in January-March 2020 and 39,513 in January-March 2019, as the inflow trend has not yet fully regained its pre-COVID strength.

The population inflow from other areas to the Tokyo metropolitan area (Tokyo, Kanagawa, Saitama, and Chiba prefectures) in January-March 2022 was up 1,830 YoY to 189,796, while the population outflow to other areas was down 5,297 to 122,425, resulting in a YoY increase of 7,127 in net inflow, to 67,371. Thus, not only Tokyo but the Tokyo metropolitan area as a whole is experiencing an inflow of population. YoY comparison of net inflows shows that while they had continued to decrease since April-June 2020, when the effects of COVID-19 became apparent, they have been increasing since April-June 2021, and the extent of the increase grew further in January-March 2022.

【Fig.15】Population Inflow and Outflow of Tokyo23



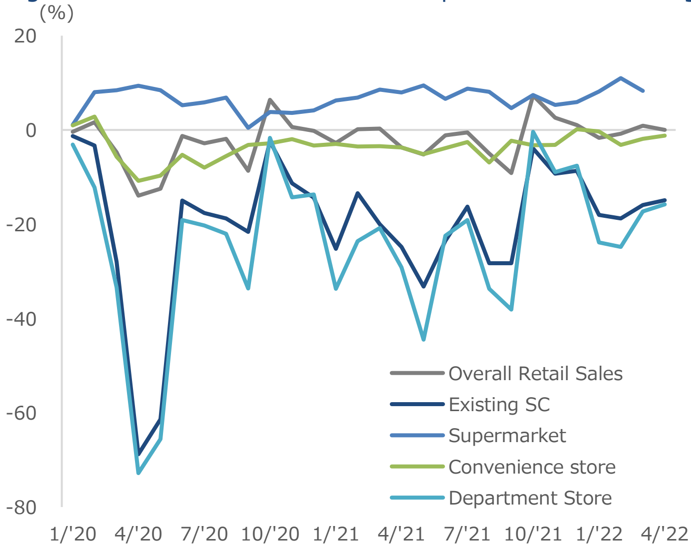
出所：Ministry of Internal Affairs and Communications

【Retail Facility Market】

Retail sales showed a small improvement in January-March 2022

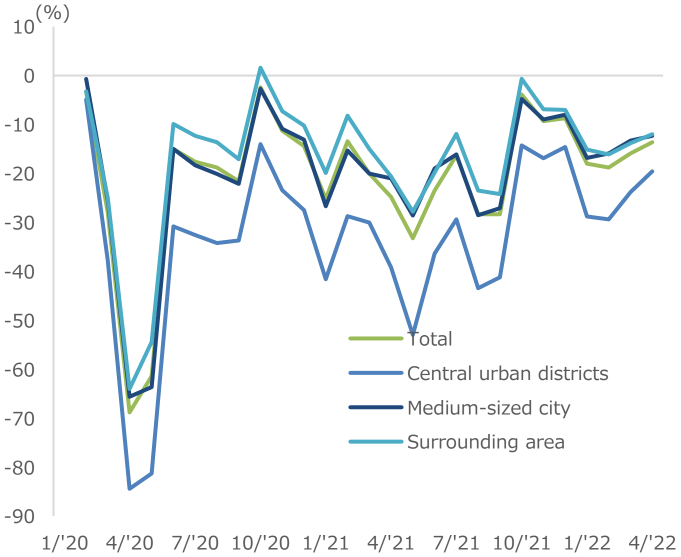
Retail sales nationwide in January-March 2022 were up 0.3% YoY, rising for the second consecutive quarter, although the rate of growth was low. This would appear to reflect the impact of the quasi-state of emergency that continued for more than 2 months from when it was instituted in January until it was lifted on March 21. Also, the hurdle for YoY growth was not very high, since some prefectures had implemented full states of emergency in the same period one year earlier. In addition, the rate of growth in retail fuel sales was high, as the impacts of rising costs of energy such as gasoline and electricity served to push up retail sales. Thus, while numerically sales increased YoY, it does not appear that the condition of the retail environment was a good one.

【Fig.16】Retail Sales Growth Rate Compared to 2019)



Source : The Ministry of Economy, Trade and Industry, Japan Council of Shopping Centers, Japan Supermarkets Association, Japan Franchise Association, Kenedix

【Fig.17】Shopping Center Sales Growth Rate Compared to 2019



Source: Japan Council of Shopping Centers, Kenedix

Retail sales nationwide showed a higher rate of growth in April 2022, rising by 2.9% YoY. Sales of large-scale retail facilities showed sharp growth in April, with shopping-center sales up 12.6% YoY and department-store sales up 19.0% YoY. Consumer activity appears to have revived as new cases of COVID-19 continued to decrease. However, YoY comparison to 2019 shows that retail sales in April were down 0.9%, with shopping-center sales down 14.9% and department-store sales down 15.8% over the same period, as retail sales have not yet recovered to pre-COVID-19 levels.

The COVID-19 pandemic appears to have had a limited impact on retail facility rents

According to the financial results announced by the Japan Metropolitan Fund Investment Corporation for the period ended February 2022, of 233 retail facility units on which leases were renewed it was able to increase rents on 85 units, while leaving rents unchanged on 115 and decreasing them on 33 units. The rate of increase in rents was 3.1%. In addition, according to the financial results announced by Kenedix Retail REIT Corporation for the period ended March 2022, the number of requests for rent reduction due to COVID-19 was just 2, down sharply from the peak of 177 requests in the period ended September 2020. Thus it would appear that the impact of COVID-19 on retail facilities now is limited.

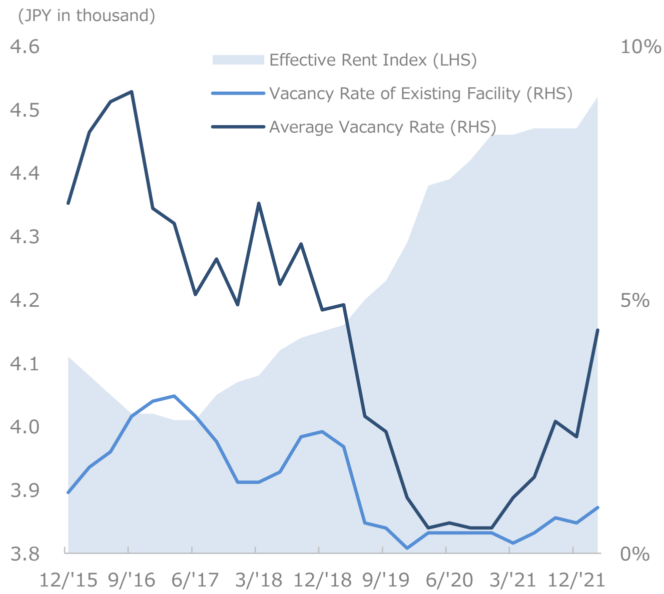
The Japan Metropolitan Fund Investment Corporation also describes leasing conditions on prime locations and in central districts as favorable. According to CBRE, high street rents in Tokyo's Omotesando and Harajuku area were up 2.3% YoY in January-March, while those in Osaka's Shinsaibashi area were up 0.7% over the same period. A change in the trend seems to be apparent, as for example properties in commercial areas in prime locations are experiencing increasing numbers of inquiries. While sales of tenants selling necessities, such as supermarkets, were favorable during the COVID-19 pandemic, sales of luxury goods appear to be favorable at present. Japan also has begun accepting travelers from overseas in June, although to a limited degree, and there are expectations of improving business performance for tenants in urban retail facilities. At the same time, the impact on consumption of rising prices due to higher costs of oil and other raw materials remains a cause for concern. There also are concerns about the negative effect of rising raw-materials prices on tenant earnings, and the indirect effect on retail facilities should be monitored closely.

【Logistics Facility Market】

The vacancy rate on multi-tenant logistics facilities in the greater Tokyo area is up due to the effect of new supply

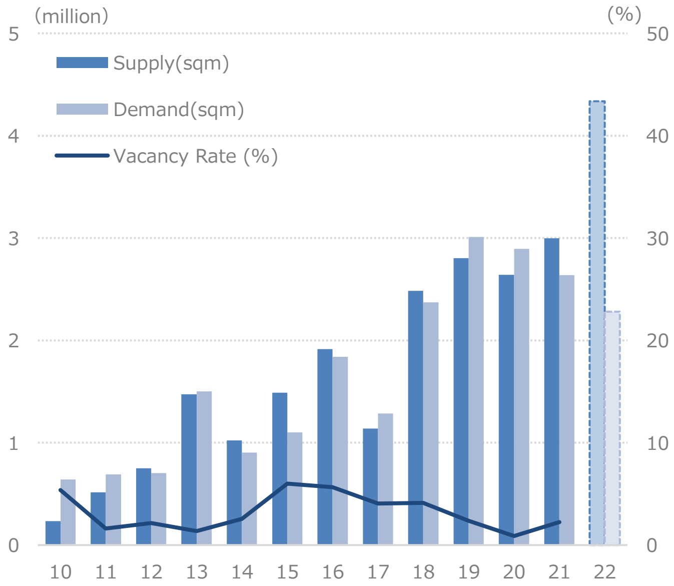
According to CBRE, the vacancy rate on large multi-tenant (LMT) logistics facilities in the greater Tokyo area in March 2022 was up sharply by 2.1% pt QoQ to 4.4%. This was the first time the vacancy rate exceeded the 4% level since March 2019. It seems that while the demand remains favorable due to new demand of approximately 150 thousand tsubo, a succession of new facilities were completed with vacancies remaining as approximately 260 thousand tsubo of facilities were newly supplied. At the same time, effective rent on LMT logistics facilities in the greater Tokyo area continues to rise, up 1.1% QoQ to JPY4,520 (per month per tsubo, CBRE).

【Fig.18】LMT Vacancy Rate and Effective Rent in Tokyo metropolitan Area



Source: CBRE, Kenedix

【Fig.19】Large-scale Logistics Facility Supply and Demand Balance of in Tokyo metropolitan Area



Note: Demand in 2022 is the accumulation of the pre-leased area
Source: Japan Logistics Field Institute, Kenedix

New supply of approximately 4 million sqm in large-scale rental logistics facilities is projected in 2022, and the pre-leasing ratio as of the end of March 2022 was 48.6%, lower that the rate as of March 2021 (source: Japan Logistics Field Institute, Inc.). While demand conditions appear likely to remain favorable, it will be difficult for this large volume of new supply to be absorbed fully, and the number of properties with spaces available even after completion of construction is likely to continue to increase. While thanks to the support of favorable demand conditions it is unlikely that the market for logistics facilities in the greater Tokyo area will worsen, there probably is a possibility of temporary easing of the balance between supply and demand in areas such as those with high levels of new supply.

The growth trend in the e-commerce market continues

The Rakuten Group, which operates one of the largest Internet shopping mall in Japan, recorded domestic e-commerce gross merchandise sales (GMS) of JPY1.25 trillion, up 10.0% YoY, as its double-digit growth continued in January-March 2022. In addition, Z Holdings Corporation, whose group company operates the major portal site Yahoo! Japan, recorded its e-commerce shopping business transaction volume in January-March 2022 that was up 10.9% YoY to JPY451.4 billion, as its figure also rose by roughly 10%. As the e-commerce market continues to grow, growth in demand for logistics facilities can be expected to continue in the future as well.

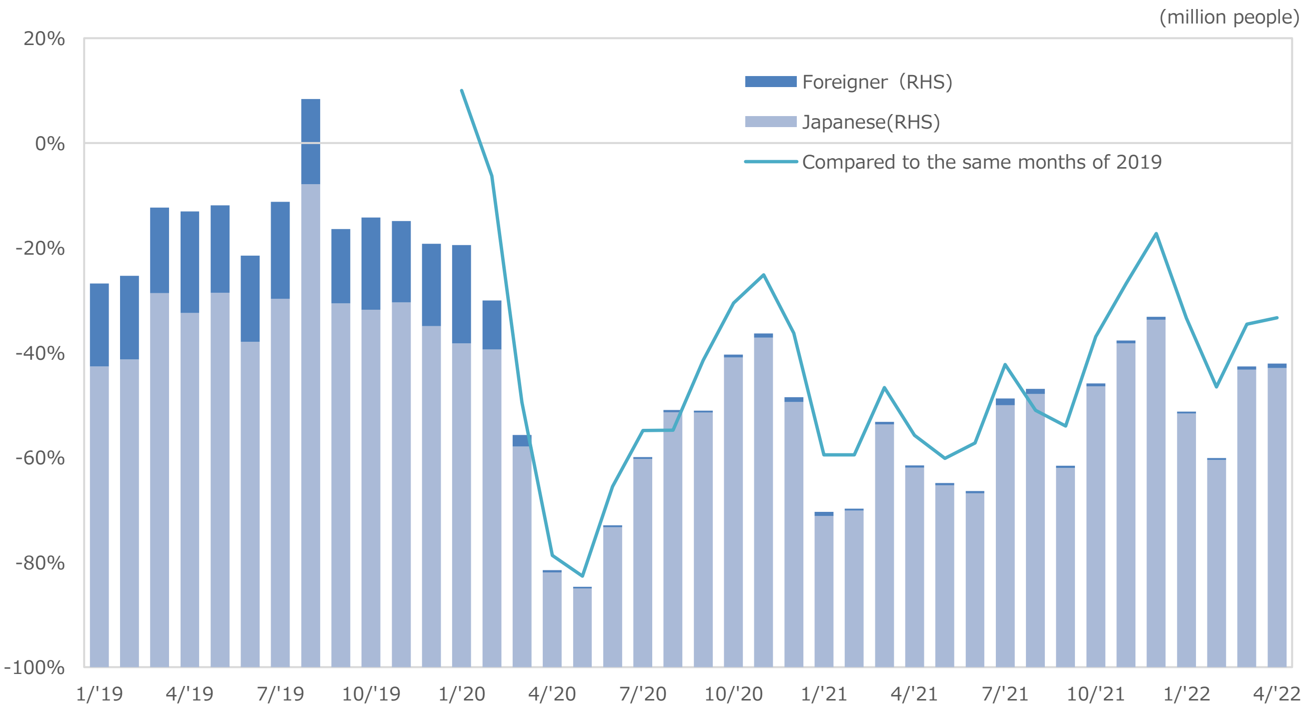
As restrictions on overtime hours for truck drivers are applied beginning in April 2024, logistics firms, major tenants of logistics facilities, expect labor costs and other logistic costs to rise. Rising gasoline prices due to surging energy costs also are expected to lead to higher costs for logistics firms, and it is difficult to be optimistic about their earnings conditions. For this reason, it can be considered not to be easy to raise rents outside of areas where supply and demand are extremely tight.

【Hotel Market】

Travel demand grew in January-March 2022 despite the quasi-state of emergency

In the quarter January-March 2022, the total number of overnight stays at lodging facilities nationwide was up 37.7% YoY to 84.4 million. The quasi-state of emergency was launched in Hiroshima, Yamaguchi, and Okinawa prefectures on January 9 and spread up to 37 prefectures. The quasi-state of emergency was lifted nationwide on March 21, so that the majority of this quarter took place under conditions of quasi-state of emergency. Although numbers of overnight stays increased over one year earlier, when a full state of emergency was in effect, they were down by approximately 20% compared to October-December 2021, when they exceeded 100 million people. In April, after the release of the quasi-state of emergency, the total number of overnight stays rose sharply by 50.6% YoY to 33.8 million. While even this number remains low, down -33% compared to the same month in 2019, since a look at figures for Japanese travelers alone shows a decrease of just 16% it is clear that domestic demand is approaching its 2019 level.

【Fig.20】Total number of Overnight Stay Guests Nationwide



Source : Japan Tourism Agency, Kenedix

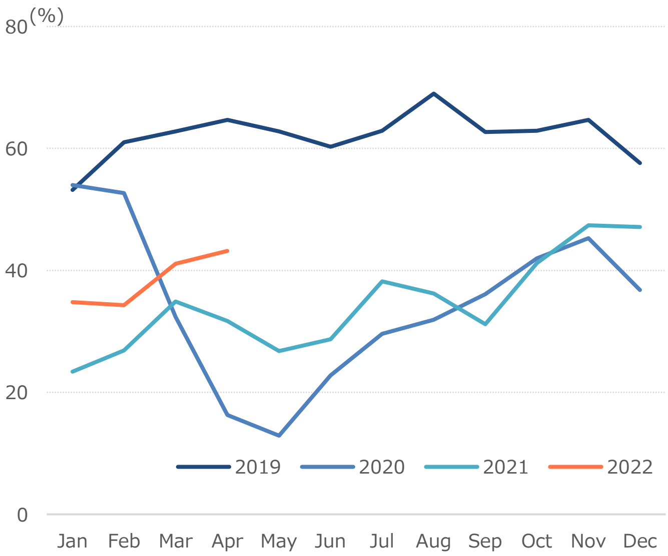
Despite an improving trend in occupancy rates, RevPAR has not yet recovered to pre-COVID-19 levels

The occupancy rate as lodging facilities nationwide in March 2022 was up 6.2%pt YoY to 41.1%. The figure has been up YoY for 5 consecutive months, since November 2021, as the improving trend continues. However, comparison with the same month in 2019 shows a decrease of 21.7%pt as the figure remains down from pre-COVID-19 levels. Hotel RevPAR (revenue per available room) in March 2022 was up 24.7% YoY to JPY5,371 as a national average (source: Weekly HOTERES, Ohta Publications). While this figure is up sharply from last year, compared to the same month in 2019 it was down 47% (JPY10,046 in March 2019). This reflects the effects of low average daily rates (ADR) in addition to the fact that occupancy rates have not yet returned to their 2019 level. Nationwide, ADR averaged JPY10,115 in March, up 3.3% YoY but down 15% from March 2019. However, in some regions ADR has recovered to 2019 levels. In March 2022 ADR was up 17% from March 2019 to JPY6,152 in the northern Kanto area and up 19% over the same period to JPY18,134 in Okinawa. At the same time, ADR in Tokyo (limited-service hotels) was down 33% over the same period to JPY6,568, while in Osaka it was down 18% to JPY10,329, as it has failed to recover to pre-COVID-19 levels in these markets.

Demand from foreign visitors to Japan is expected to increase as well

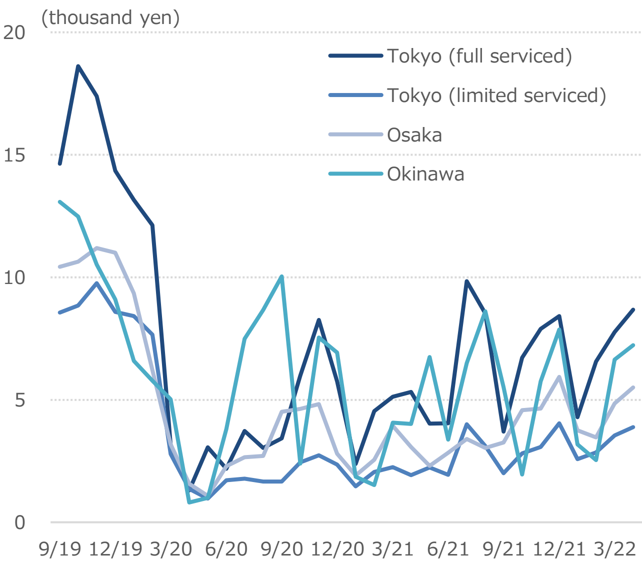
The number of foreign visitors to Japan, which was at the 10 thousand level in January and February, rose to 66 thousand in March and 139 thousand in April. Since March, the period for self-quarantine at home or elsewhere after entering the country has been shortened or eliminated and the maximum number allowed to enter the country per day also has been raised in stages, and it appears that entries to Japan by international students and business travelers are increasing. Tourists have been able to enter the country since June. While such travelers remain subject to restrictions, such as limitation to tour groups and restrictions on numbers admitted per day, there are expectations for an increase in demand from foreign visitors, which has been nonexistent for a lengthy period. According to the Central Japan Railway Company, Shinkansen traffic during the Golden Week holidays (April 28 – May 8) was up 274% YoY was at 80% of its level in FY2018 (the period ended March 2019). While it remains down about 20% compared to the pre-COVID-19 level, it is up sharply YoY and passenger demand appears to have been high in April-June as well. The recovering trend in hotel demand is likely to continue if numbers of foreign guests rise steadily in addition to growth in demand from Japanese travelers.

【Fig.21】Hotel Occupancy Rate Nationwide



Source : Japan Tourism Agency, Kenedix

【Fig.22】Hotel RevPAR



Source : Ohta Publications, "HOTERES", Kenedix

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