

savills

Offices

Tokyo, Japan



1H / 2009

The Office Market

Market Overview

Commentators expect key economic indicators such as export data to move in a positive direction going forward, raising GDP. Despite the relatively low levels of new supply of Grade 'A' office buildings, both vacancy rates and rental levels have followed a negative track in recent quarters. Moreover, beginning office cap rate levels and the spread between 10 year Japanese government bonds have followed suit. It is estimated that this trend will continue in the short to mid term, although to a lesser degree. Although there are no real signs of economic recovery, some players are moving forward with their investment strategies. Major transactions were also recorded in the J-REIT market.

Economic Trends

Key economic indicators such as export volume, which recorded negative growth for four consecutive months from October 2008, have shown some signs of improvement, recording positive month-on-month growth between February and April. It is largely thought that decreases in export volume have bottomed out. Although GDP growth rate projections for 2009 by major financial institutions and think tanks range between -5.40 and -6.86 per cent, growth rate projections for 2010 are more optimistic, ranging between 0.56 and 3.50 per cent.

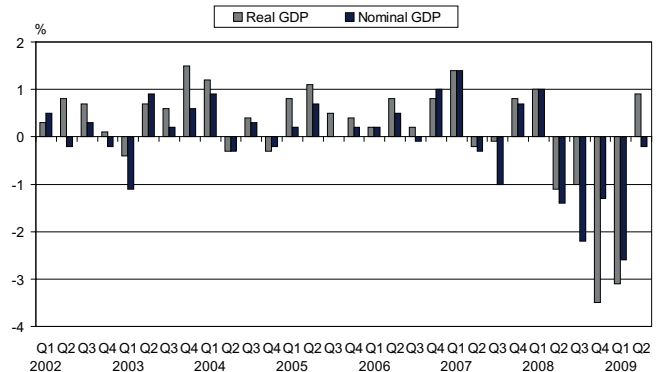
Prime Office Building Supply

The new supply of Tokyo's Grade 'A' office¹ buildings in 2009 and 2010 is expected to be below the average level recorded between 2001 and 2008. According to current estimates, the average annual new supply of Grade 'A' office buildings between 2009 and 2014 is expected to be about 640,000 sq.m. The new supply of Grade 'A' office buildings in 2009 is expected to total 690,000 sq.m., 7 per cent above the estimated average supply between 2009 and 2014. The Marunouchi Park Building, which is a B4/34F property with a GFA of 206,212 sq.m. in Chiyoda Ward, is the biggest landmark building to enter the market in 2009. New supply of Grade 'A' office buildings in 2010 will stand at about 313,000 sq.m., half of the estimated average supply between 2009 and 2014. Supply in 2011 is expected to reach it's highest level since 2007 at about 1.25 million sq.m., but is approximately 27 per cent lower than levels recorded in 2003; the highest annual supply level recorded since 2001.

Prime Office Vacancy Rate

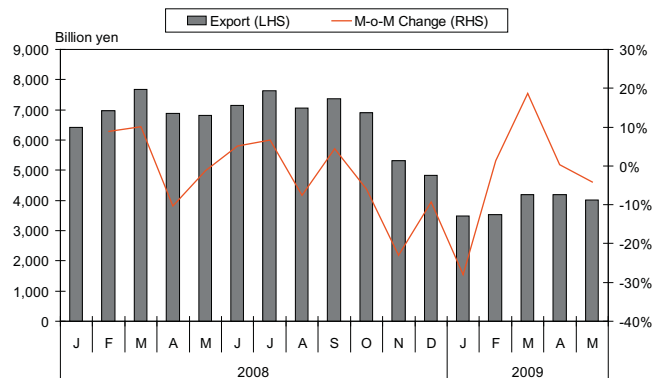
Vacancy rates for Grade 'A' office buildings in the major business districts² of Tokyo's central five wards have followed an upward track in recent quarters. At the end of Q2/2009, the estimated vacancy rate for each area stood at between 0.3 to 5.6 percentage points higher on a year-on-year basis. However, on a quarter-on-quarter basis, a decrease in vacancy rate was recorded in the Marunouchi/Otemachi, Nihombashi, and Nishi Shinjuku submarkets. This was largely due to the lease up of notable Grade 'A' office buildings such as the Marunouchi Trust Tower Main Building and the Marunouchi Trust Tower North Building. The vacancy rates of these two buildings fell from 73 per cent and 47 per cent to 29 per cent and 37 per cent on a quarter-on-quarter basis respectively.

GDP Growth Rate Q-o-Q (Seasonally Adjusted), Q1/2002 - Q2/2009



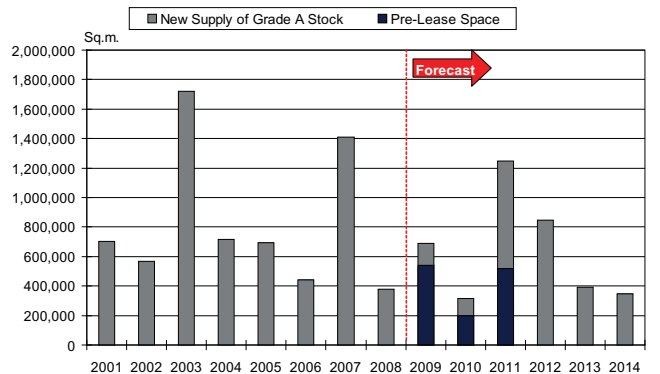
Source: Cabinet Office, Savills Research & Consultancy

Japan's Export Volume, Jan 2008 - May 2009



Source: Ministry of Finance, Savills Research & Consultancy

Grade 'A' Office Stock and Pre-lease Space, 2001 - 2014



Source: Savills Research & Consultancy

¹ Grade 'A' office refers to Tokyo central five wards office buildings with a GFA of 30,000 sq.m. (9,000 tsubo) or higher and a building age of less than 15 years.
² Marunouchi/Otemachi, Nihombashi, Akasaka/Toranomon/Roppongi, Nishi Shijuku and Shibuya/Ebisu.

Despite this, it is estimated that the average vacancy rate for Grade 'A' office buildings in the major business districts of Tokyo's central five wards will continue to increase in the short to mid term. However, the rate of increase will be significantly lower than levels recorded in recent quarters.

Prime Office Rental Levels

Rents for Grade 'A' buildings in the major business districts of Tokyo's central five wards have followed a downward trend in recent quarters. At the end of Q2/2009, each area's estimated rent decreased by between 28.4 per cent and 39.0 per cent year-on-year. Due to this decrease, the disparity of rents between the most expensive area (Marunouchi/Otemachi) and the least expensive area (Nishi Shinjuku) has narrowed substantially. On a year-on-year basis, the estimated disparity has decreased from about 20,500 yen per tsubo per month to about 15,000 yen per tsubo per month, with rents now ranging between 46,000 yen and 28,000 yen. It is estimated that the average rent for Grade 'A' office buildings in Tokyo's central five wards will continue to decrease in the short to mid term. However, the rate of decrease is expected to slow from recent quarters.

Prime Office Cap Rate and Yield Spreads

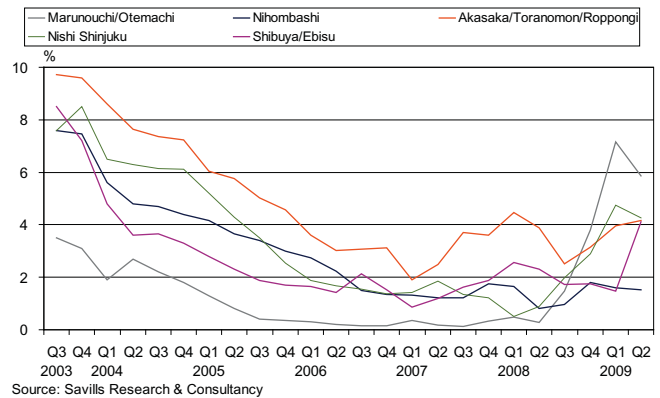
Although still low in comparison to other developed cities around the world, Tokyo's Grade 'A' beginning office cap rate ceased compressing during the second half of 2008. During the past 12 months, the office cap rate level has appreciated by about 70 percentage points from 3.50 per cent to 4.20 per cent. It is expected that beginning cap rate levels will continue to push out over the short to mid term, albeit remaining below the 5.0 per cent threshold. Moreover, the yield spread with the 10-year Japanese Government Bond (JGB) has widened in recent months. The yield spread, which hovered at around 180 basis points between the middle of 2006 and the middle of 2007, widened to about 270 basis points by the middle of 2009. It is expected that the yield spread will increase further in the mid to long term.

Recent Sales and Investment Activity

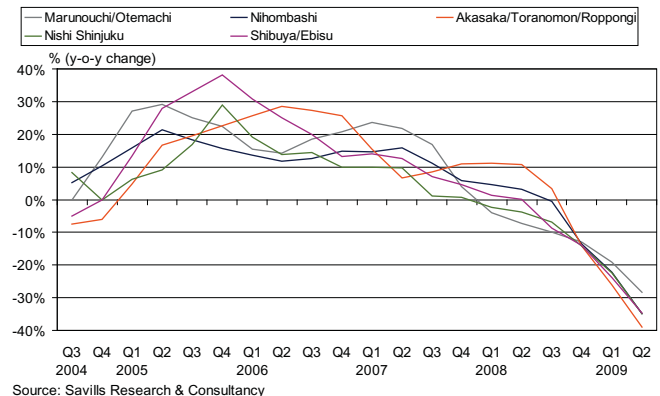
Although the key indices of Tokyo's real estate market continue to show no signs of sound recovery, some domestic institutions have moved forward with large-scale investment transactions. The most notable examples are Mitsubishi Estate's acquisition of Asahi Life Insurance Building and Nippon Life Insurance's acquisition of the AIG Building. The acquisition prices of these properties were reported at 80 billion yen and 115 billion yen respectively. The estimated transaction cap rates from a current income approach were 3.1 per cent and sub-three per cent respectively.

Furthermore, notable transactions have been executed in the J-REIT market. In June, Daiwa Securities Group became the first domestic securities company to acquire a major stake (13 per cent ownership) in a J-REIT through its 10 billion yen investment in DA Office Investment, sponsored by da Vinci Holdings. In July, it was announced that Crescendo Investment will dispose Ebisu Square, its trophy asset, for about 6.9 billion yen, approximately 2.3 per cent below its acquisition price in March 2005. Also in July, Japan Prime Realty Investment purchased the strata title ownership of Olinas Tower for 31.3 billion yen from Tokyo Tatemono, its main sponsor. In exchange, Japan Prime Realty Investment disposed office buildings located in Osaka and Sendai to Tokyo Tatemono.

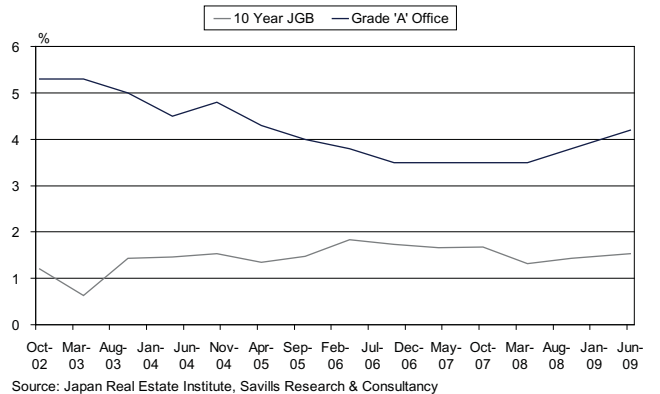
Grade 'A' Office Vacancy in the Major Business Districts of Tokyo's Central 5 Wards, Q3/2003 - Q2/2009



Rental Levels of Grade 'A' Buildings in the Major Business Districts of Tokyo's Central 5 Wards, Q3/2004 - Q2/2009



Yield Spread between 10 year JGB and Tokyo Grade 'A' Office, Oct 2002 - Jun 2009



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