

NEWS & RELEASE

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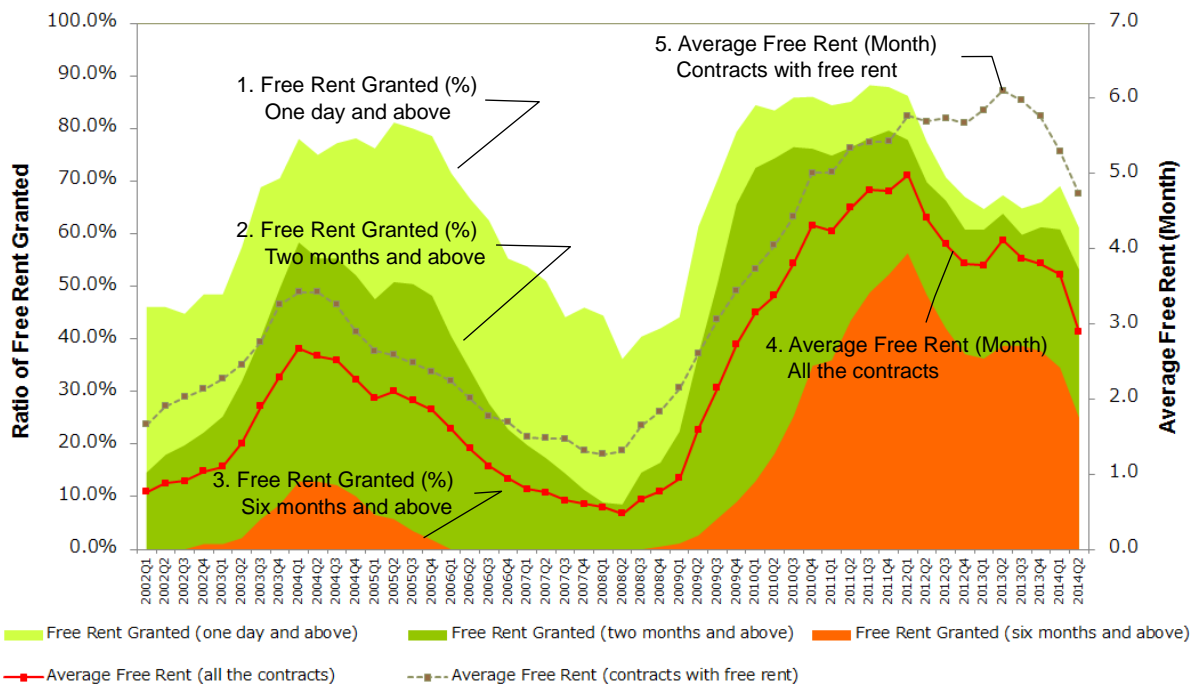
Quarterly Analysis of Free Rent (Tokyo Office)

Ratio of Free Rent Granted and Average Free Rent (Month) both show clear trends of decreasing.

The analysis of free rent is a study of current trends of free rent given to new lease. Xymax Real Estate Institute used the data of lease contracts collected through the group's business activities and has so far released Ratio of Free Rent Granted (a percentage of new lease contracts with two months or more free rent in all the new lease contracts) and Free Rent Index (an index based on average rent-free period) for FY2012 and FY2013¹.

On this occasion, we have revised the calculation method of the analysis. From this issue, we will report Ratio of Free Rent Granted and Average Free Rent (Month) on a quarterly basis. To provide a more precise picture of the overall market, we will present a breakdown of rent-free period (one day and above / two months and above / six months and above) and the average free rent in actual months rather than the indexed data.

Figure 1: Free Rent for New Lease (Tokyo 23 Wards)



Results for the last four quarters

		Q3 2013	Q4 2013	Q1 2014	Q2 2014	Quarter-on quarter
Ratio of Free Rent Granted	1. One day and above	64.8%	66.0%	69.1%	61.1%	-8.0 pts.
	2. Two months and above	59.8%	61.3%	60.8%	53.2%	-7.6 pts.
	3. Six months and above	38.7%	37.7%	34.5%	25.0%	-9.5 pts.
Average Free Rent (Month)	4. All the contracts	3.9	3.8	3.7	2.9	-0.8
	5. Contracts with free rent	6.0	5.8	5.3	4.7	-0.6

Numerical data for the entire period is available at the end of this report.

¹ The previous report was released on July 2, 2014: <http://www.xymax.co.jp/english/research/release/140702.html>

In Figure 1, the area graph shows changes in Ratio of Free Rent Granted, and the line graph shows changes in Average Free Rent (Month).

The edge of the light green area (1.) represents the rent-free period of at least one day (61.1% in Q2 2014). The white area represents lease contracts with no free rent. The figure shows that even during the strong market in 2007-2008, owners offered free rent in 30%-50% of the contracts signed, indicating that free rent is a sort of market practice in Japan.

The edge of green area (2.) represents the rent-free period of two months and above (53.2% in Q2 2014) and the edge of the orange area (3.) represents six months and above (25.0% in Q2 2014). The percentage of free rent of two months and above drastically increased in a downtrend market, because the rent-free period of such length is more like a reduction of rent than merely for avoiding double rent payment.

The line graph shows Average Free Rent (Month). The red solid line (4.) is the average of all the contracts including those with no free rent. The gray dashed line (5.) is the average of the contracts with free rent only. The former represents the overall trends whereas the latter is useful for analyzing the types of free rent offered.

Recent Free Rent Trends

Ratio of Free Rent Granted fell sharply in 2012 as the market recovered, but it slowed at the start of 2013, influenced apparently by owners who took advantage of the recovering demand to quickly achieve higher occupancy rates and offered some free rent so that tenants think it is affordable.

In the recent data, Average Free Rent (Month) of contracts with free rent (5.) stays in a relatively high level compared to that of all the contracts (4.). This is because, although office leases are becoming less dependent on free rent, some offices definitely require a very long rent-free period of 12 to 18 months. The demand gap between attractive office spaces and other office spaces are expanding. Some owners of office buildings with high occupancy rate have actually succeeded in filling vacancy by offering a long rent-free period.

Despite such slow movements, the latest data for Q2 2014 recorded a positive trend: a decrease of both Ratio of Free Rent Granted and Average Free Rent (Month). As the vacancy rate has improved, free rent campaigns aiming at quick filling of the vacancies have apparently ended.

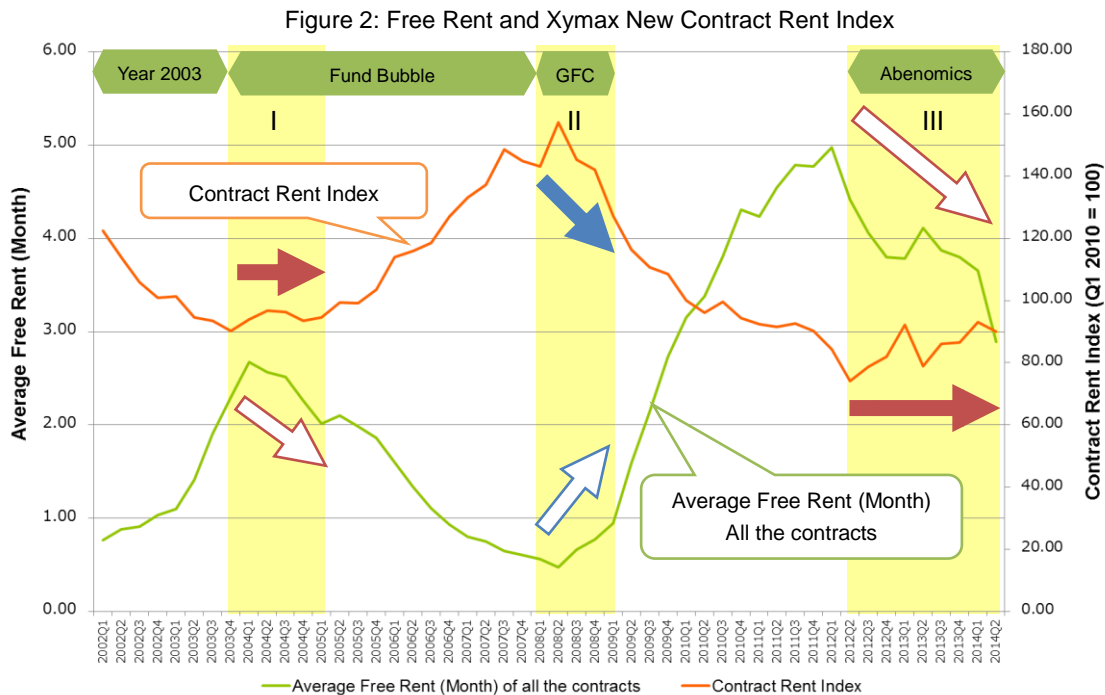
Free Rent in Japan

Free rent is the time lag between the start of contract and the start of rent. In other parts of the world, free rent is looked as incentives or concessions, whereas in Japan, free rent is originally more like an avoidance of double rent payment when moving to one place from another. Such free rent is offered by an owner of the new space. Thus, free rent is a market practice in Japan, and therefore some are offered regardless of market conditions. The free rent for the purpose of avoiding double rent payment is generally a period of roughly two months; the period longer than that can be, however, looked as a reduction of rent reflecting the market conditions.

Accordingly, not only rent but also free rent is an important element in lease contract. An analysis of the rent and free rent combined can describe accurate market conditions.

Free Rent and Xymax New Contract Rent Index

Figure 2 is a comparison of the free rent and Xymax New Contract Rent Index ². As the graph shows, the rent index and free rent are correlated. There are three notable periods as discussed below.



I End of Year 2003 Large Supply

The market showed signs of recovery following the elimination of excess supply in 2003. The rent level, however, did not increase immediately but remained flat for some period. In contrast, the free rent showed a clear decreasing trend, meaning the effective rent is actually increasing.

II Global Financial Crisis

When the market is declining, the rent level and free rent deteriorate simultaneously.

III Abenomics

The recession is over and the market is on track for recovery. Here again, the free rent is decreasing ahead of the slow recovery of the rent level. It is still difficult to raise the face rent in the early stage of market recovery. It can be explained that the free rent is the valve to adjust the effective rent for an eventual recovery.

² Xymax New Contract Rent Index http://www.xymax.co.jp/english/research/new_research.html

Xymax Real Estate Institute will continue to provide materials for market participants to understand a clearer picture of the actual market through the combined analysis of the trends of contract rent and free rent.

Data overview and analysis method

Name	Xymax Free Rent Analysis: Ratio of Free Rent Granted and Average Free Rent (Month)		
Subject Property	Office buildings in Tokyo 23 Wards		
Period	April 1, 2001 – <u>June 30, 2014</u> (to be updated quarterly)		
No. of Data	Average of 150 per quarter (252 in the latest quarter in Q2 2014)		
Analysis Method	Free rent period	The period from the start of contract to the start of rent, shown in days	
	Ratio of Free Rent Granted	The percentage of new lease contracts with free rent in all the new contracts (excl. expansion within the building and recontract)	
	Average Free Rent (Month)	All the contracts	The simple average of the free rent period including lease contracts with no free rent.
		Contracts with free rent	The simple average of the free rent period of lease contracts with free rent.

- The original research report in Japanese and translated reports in Chinese and Korean are also available online.
 Japanese <http://www.xymax.co.jp/>
 Chinese <http://www.xymax.co.jp/cn/index.html>
 Korean <http://www.xymax.co.jp/ko/index.html>

Reference: Numerical data for the entire period

	1. Free Rent Granted (1 day +)	2. Free Rent Granted (2 months +)	3. Free Rent Granted (6 months +)	4. Average Free Rent (Month) (All the contracts)	5. Average Free Rent (Month) (Contracts With free rent)
Q1 2002	46.1%	14.6%	0.0%	0.8	1.7
Q2 2002	46.1%	18.0%	0.0%	0.9	1.9
Q3 2002	44.8%	19.8%	0.0%	0.9	2.0
Q4 2002	48.5%	22.2%	1.0%	1.0	2.1
Q1 2003	48.5%	25.3%	1.0%	1.1	2.3
Q2 2003	57.4%	31.9%	2.1%	1.4	2.5
Q3 2003	68.9%	40.2%	5.7%	1.9	2.8
Q4 2003	70.5%	49.6%	8.5%	2.3	3.3
Q1 2004	78.0%	58.3%	12.9%	2.7	3.4
Q2 2004	75.0%	55.3%	12.9%	2.6	3.4
Q3 2004	77.2%	55.3%	12.2%	2.5	3.3
Q4 2004	78.2%	52.1%	10.1%	2.3	2.9
Q1 2005	76.2%	47.5%	6.6%	2.0	2.6
Q2 2005	81.1%	50.8%	5.7%	2.1	2.6
Q3 2005	80.0%	50.4%	3.5%	2.0	2.5
Q4 2005	78.6%	48.2%	1.8%	1.9	2.4
Q1 2006	71.6%	40.5%	0.0%	1.6	2.2
Q2 2006	66.7%	34.1%	0.0%	1.3	2.0
Q3 2006	62.5%	27.7%	0.0%	1.1	1.8
Q4 2006	55.3%	22.8%	0.0%	0.9	1.7
Q1 2007	53.8%	19.8%	0.0%	0.8	1.5
Q2 2007	51.0%	17.3%	0.0%	0.8	1.5
Q3 2007	44.1%	14.4%	0.0%	0.7	1.5
Q4 2007	46.0%	11.3%	0.0%	0.6	1.3
Q1 2008	44.4%	8.9%	0.0%	0.6	1.3
Q2 2008	36.2%	8.6%	0.0%	0.5	1.3
Q3 2008	40.4%	14.6%	0.0%	0.7	1.6
Q4 2008	42.0%	16.5%	0.5%	0.8	1.8
Q1 2009	44.1%	22.3%	1.1%	0.9	2.1
Q2 2009	61.4%	37.0%	2.6%	1.6	2.6
Q3 2009	70.2%	50.5%	5.9%	2.1	3.1
Q4 2009	79.4%	65.6%	9.0%	2.7	3.4
Q1 2010	84.5%	72.5%	13.0%	3.2	3.7
Q2 2010	83.4%	74.3%	18.2%	3.4	4.0
Q3 2010	85.9%	76.5%	25.3%	3.8	4.4
Q4 2010	86.0%	76.2%	34.9%	4.3	5.0
Q1 2011	84.4%	74.9%	35.9%	4.2	5.0
Q2 2011	85.1%	76.4%	43.5%	4.5	5.3
Q3 2011	88.2%	78.2%	48.8%	4.8	5.4
Q4 2011	87.9%	79.6%	52.2%	4.8	5.4
Q1 2012	86.2%	77.8%	56.3%	5.0	5.8
Q2 2012	77.5%	69.8%	48.4%	4.4	5.7
Q3 2012	70.7%	66.3%	42.0%	4.1	5.7
Q4 2012	67.0%	60.8%	37.1%	3.8	5.7
Q1 2013	64.7%	60.8%	36.3%	3.8	5.8
Q2 2013	67.3%	63.8%	38.7%	4.1	6.1
Q3 2013	64.8%	59.8%	38.7%	3.9	6.0
Q4 2013	66.0%	61.3%	37.7%	3.8	5.8
Q1 2014	69.1%	60.8%	34.5%	3.7	5.3
Q2 2014	61.1%	53.2%	25.0%	2.9	4.7