

Survey of Increase and Decrease in Vacant Office Space(Tokyo 23 Wards)

A new benchmark for gaining insight into market mechanisms that vacancy rates alone cannot offer

January 23, 2017

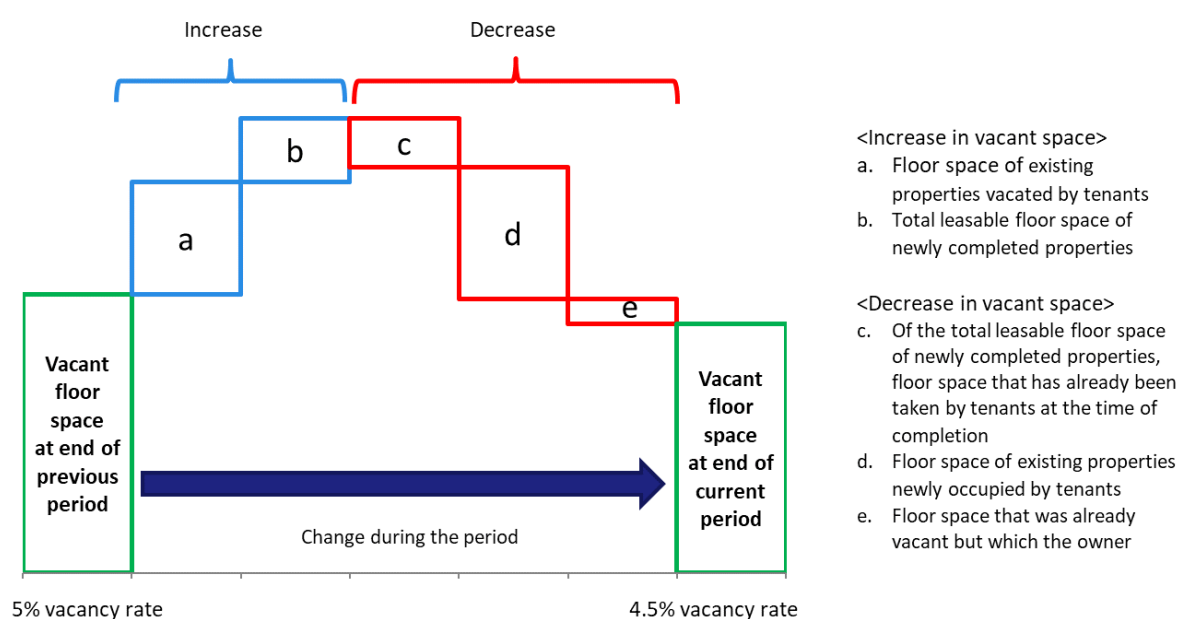
Xymax Real Estate Institute (hereinafter, "Xymax REI") has conducted a survey on the increase and decrease in vacant office space, using vacancy data obtained and accumulated by the Xymax Group. This report introduces the outline of the survey. Going forward, Xymax REI plans to include future findings in its quarterly "Office Market Report - Tokyo."

The supply-demand gap of the office space market is manifest in vacancies, which are most commonly measured in the form of vacancy rates. The vacancy rate is the ratio of vacant floor space to total leasable floor space at a certain point in time. In general, a low vacancy rate means that the stock of vacant space is small and the market is robust, while a high vacancy rate indicates a large amount of vacancy and a weak market.

However, vacancy rates are, so to say, snap shots that show the supply-demand gap as of a certain point in time. When vacancy rates fall, it is difficult to determine the background of the supply and demand, such as whether the fall was due to a rise in demand on the back of a robust market or whether it was simply the result of little supply. Furthermore, a stable vacancy rate may seem to indicate an unchanging space market, but the meaning of the number will change depending on whether the rate was attributable to demand or to supply.

As shown in **Figure 1**, the actual office space market comprises an increase in vacant space due to: (a) tenants vacating existing properties; and (b) the supply of newly completed properties, and a decrease in vacant space due to: (c) tenants occupying vacancies of existing properties; (d) pre-leasing of newly completed properties; and, although small in number, (e) refusal of renting out vacancies. Vacancy rates are an indication of the consequence of these developments.

Figure 1: Mechanism of Increases and Decreases in Vacant Space



To understand such changes in the volume of vacancies in the office market, Xymax REI surveyed and aggregated the data of vacant floor space that was consumed (i.e., decreased) (mainly floor space that became occupied by tenants) during the survey period and the vacant floor space that was produced (i.e., increased) (mainly floor space that was vacated by tenants as well as newly completed floor space), and compiled the data as "increase and decrease in vacant space."

This survey aggregated the data of the increase and decrease in vacant space, adjusted by floor space in vacant block units. In addition to the floor space of newly completed properties, the survey takes account of the increase and decrease in vacant floor space of existing properties, making the survey unique in that it provides insight into the stock of vacancies and the size and changes in the corresponding transaction volume during the survey period.

Description of the Survey

In this survey we calculated the increase and decrease in vacant floor space using vacancy data collected by Xymax. The targets of the survey were office space located in Tokyo 23 Wards. Expansions in the same building are not included.

Definitions of terms are as follows.

① Increase in vacant floor space

Floor space that was occupied at the end of the previous month but became vacant during the month.

The following were treated as an increase in vacant floor space.

- ✓ Floor space of existing properties vacated by tenants
- ✓ Total leasable floor space of newly completed properties

② Decrease in vacant floor space

Floor space that was vacant at the end of the previous month but became occupied during the month.

The following were treated as a decrease in vacant floor space.

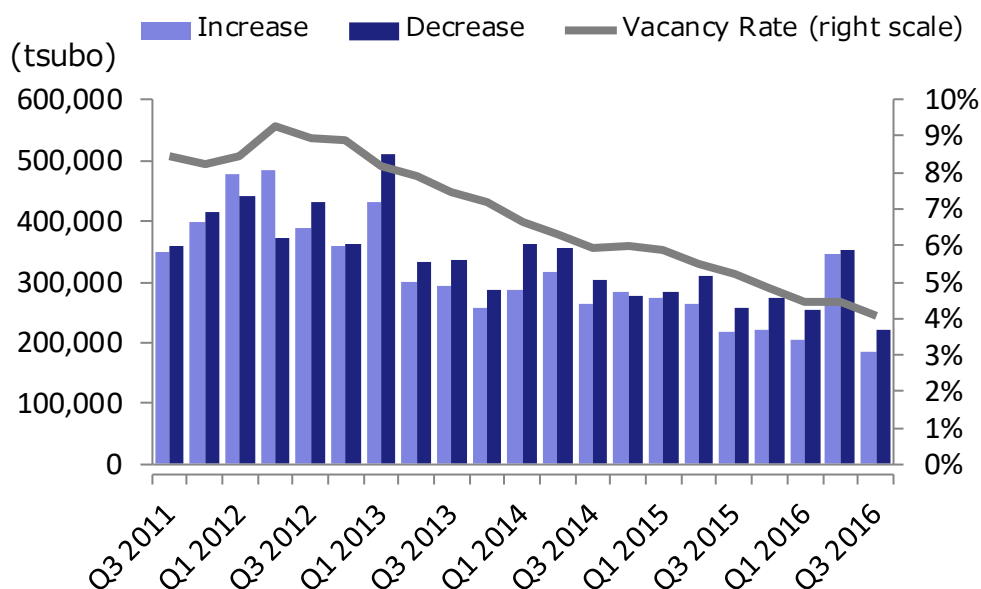
- ✓ Floor space of existing properties newly occupied by tenants
- ✓ Of the total leasable floor space of newly completed properties, the floor space that has already been taken by tenants at the time of completion
- ✓ Vacant floor space of existing properties that the owner refuses to rent out

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Survey Results

Figure 2 shows the quarterly trend of the increase and decrease in vacant floor space. The increase and decrease in vacant floor space are indicated as a bar chart, and the vacancy rate is expressed with a line chart.

Figure 2: Increase and Decrease in Vacant Space



	Q3 2015	Q4 2015	Q1 2016	Q2 2016	Q3 2016
Increase	217,000	220,000	204,000	345,000	184,000
Decrease	256,000	273,000	253,000	354,000	222,000
Vacancy (right scale)	5.21%	4.83%	4.46%	4.45%	4.08%

The above chart shows an overall trend in which the volume of vacant space decreases as the vacancy rate falls. In each quarter, the vacancy rate drops when the decrease in vacant floor space (right bar chart) exceeds the increase in vacant floor space (left bar chart). On the other hand, when the increase in vacant floor space exceeds the decrease, the vacancy rate rises.

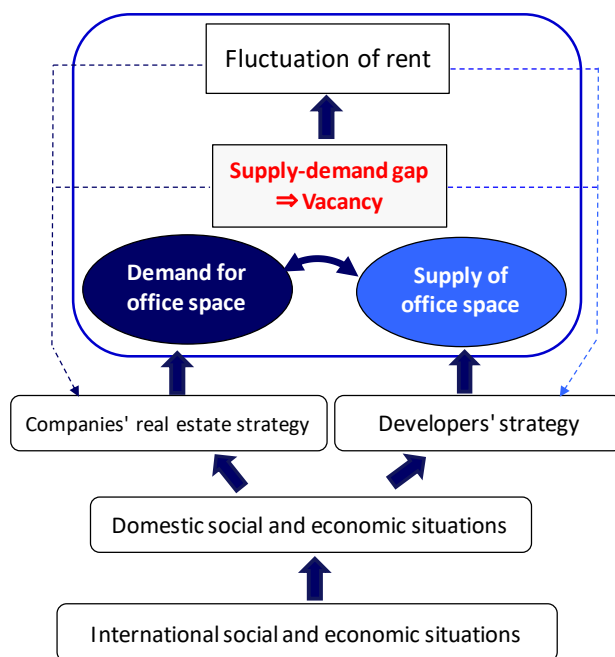
Looking at individual quarters, demand in Q2 2016 seems to be sluggish with the vacancy rate at 4.45%, only 0.01 point down from the previous quarter. However, when we look at the increase and decrease in vacant space, the data suggests that despite the increase in vacant space (supply) in Q2 2016 being larger than in the previous and following quarters, there was enough demand to absorb the increase. This was probably because tenants who potentially intended to relocate or expand but did not do so as they could not find a property that suited their needs due to lack of vacant stock took up vacancies as supply (i.e. vacant stock) increased. The data of this quarter indicates that an unchanged vacancy rate does not necessarily point to sluggish demand, and suggests that there are various backgrounds to the developments.

Market Mechanism and Indicators

Figure 3 illustrates the mechanism of fluctuation of the office space market. The supply and demand of office space are affected by domestic and international social/economic situations. For example, improved corporate earnings lead to employment and capital expenditure, giving rise to office demand. Vacancy rates will drop if demand exceeds supply, which will eventually lead to rising rent if this supply-demand situation continues. Meanwhile, the supply of office space depends largely on the business strategy of real estate developers. Excessive supply against demand for office space will lead to a widening of the supply-demand gap, an increase in vacancies and a downward pressure on rent.

Since office rent is a fixed cost that accounts for a large portion of facility costs of companies, the fluctuation of rent will have an effect on companies' real estate strategy. For real estate developers on the other hand, vacancies and rent are also important factors that impact their business profitability. Thus, vacancies and rent, which are indicators of the supply-demand gap, are "compasses" of the developments of the office space market.

Figure 3: Mechanism of the Office Space Market



In Japan, vacancy rates and asking rent are well-known indicators of the trend of the office space market. In other countries, however, contract rent is highly rated as being reliable and vacancy rates are not only offered as a simple indicator of consequences but are provided along with the background of the changes in the vacancy situation. This survey hopes to offer help in revealing the actual state of the market by supplementing vacancy rates.

As the above figure indicates, the mechanism of the office space market is complex and cannot be explained by a single indicator. It is necessary to conduct comprehensive analysis and judgment using multiple indicators to correctly understand the market's development. Going forward, Xymax REI intends to publish useful indicators such as the indicator introduced in this report on a regular basis as well as continuing to develop new indicators and provide information to achieve further transparency.

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Survey Overview

Name	Survey of increase and decrease in vacant space
Characteristics	Increase and decrease of vacant floor space during the survey period
Survey target	Office space located in Tokyo 23 Wards
Aggregation unit	Vacant block units
Aggregation period	From March 2011 to September 2016 *To be continued thereafter
Publication frequency	Quarterly
Data source	Vacant block data and property data collected by Xymax
No. of samples	Q3 2016: 31,123 blocks

Contact for inquiries concerning this report

Xymax Real Estate Institute
<https://soken.xymax.co.jp>

TEL: +81 3 3596 1477 | FAX: +81 3 3596 1478 | E-MAIL: info-rei@xymax.co.jp

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