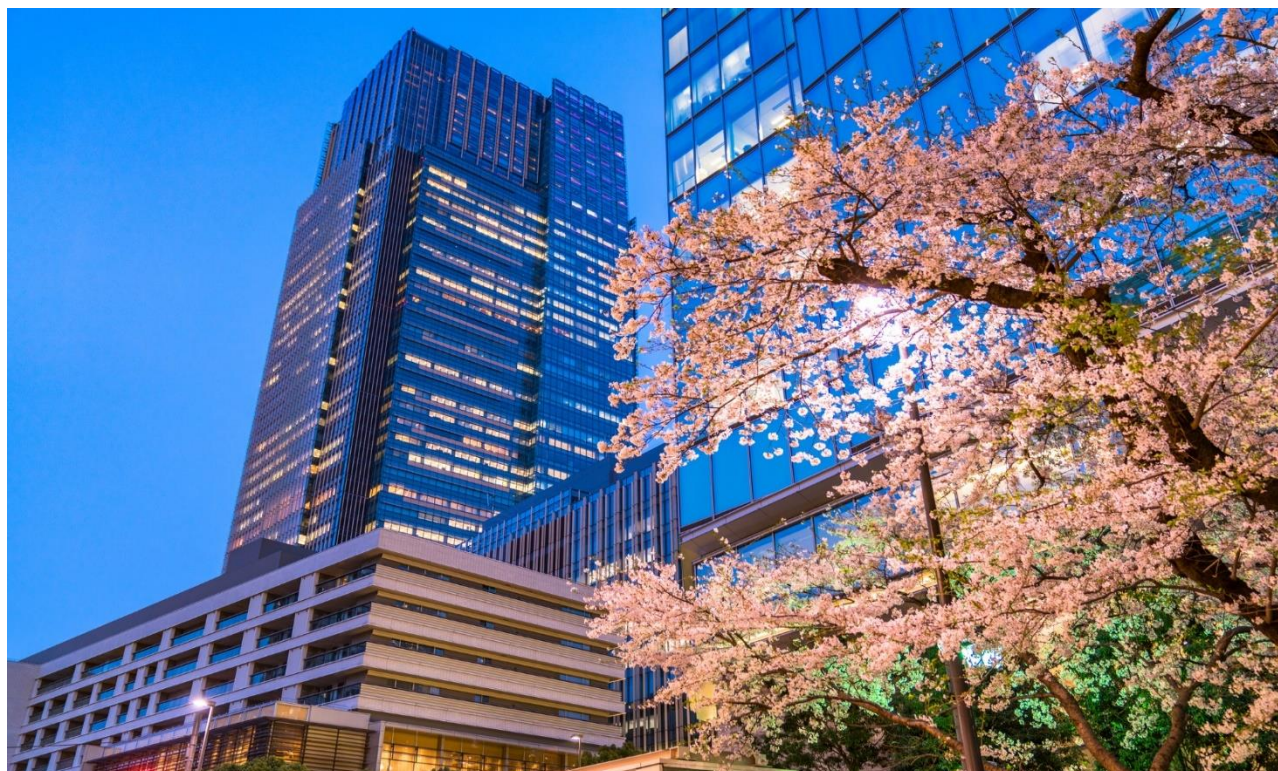


Office Market Report

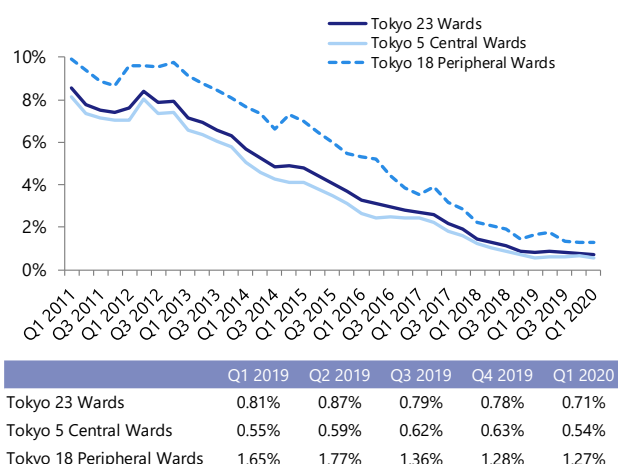
Tokyo | Q1 2020

April 28, 2020



Summary

- In Q1 (January–March) 2020, the office market of the 23 wards of Tokyo (“Tokyo 23 Wards”) remained robust as demand for office space was strong and new vacancies were filled promptly.
- The **vacancy rate** was 0.71%, down 0.07 points from the previous quarter. In terms of the **increase and decrease of vacancies**, the decrease outstripped the increase for the third consecutive quarter, as 150,000 tsubo (1 tsubo = approx. 3.3 sqm) increased and 162,000 tsubo decreased. The **vacancy turnover ratio**, which is the rate of decrease of vacant office stock, dropped 3.9 points quarter on quarter to 50.5%.
- The **new contract rent index**, the level of new lease rent, was 137, up 9 points from the previous quarter. The **contract rent diffusion index**, which is the percentage of buildings with a rise in new rent minus that of buildings with a drop in new rent, remained above zero for the twentieth consecutive quarter at +43.
- The **paying rent index**, which includes both new and existing rents, was 101, up 1 point quarter on quarter.
- The **average free rent months of lease with free rent** was 1.2 months, 0.1 months less from the previous quarter, and the ratio of free rent offered was 36.6%, down 4.2 percentage points.
- While the new coronavirus is feared to have a negative impact on the economy, no impact was seen on office market indicators in the quarter under review.

Figure 1: Vacancy Rate (by Area)


Vacancy

Figure 1 shows the **vacancy rates** in Tokyo 23 Wards, 5 Central Wards (Chuo, Chiyoda, Minato, Shibuya, and Shinjuku Wards), and 18 Peripheral Wards since 2011. The rate in Q1 2020 dropped 0.07 points in the 23 Wards to 0.71%, 0.09 points in the 5 Central Wards to 0.54%, and 0.01 points in the 18 Peripheral Wards to 1.27%. Companies' needs for expanding their offices remained high, which has led to record low vacancy rates in all areas.

The reasons for the drop in vacancy rates include companies placing priority on securing office space, large, new office buildings being nearly fully occupied at the time of completion, and vacancies due to companies relocating to such new office buildings being filled immediately.

Figure 2 shows the **vacancy rates** of all sizes of buildings, large buildings (gross floor area (GFA): 5,000 tsubo or more), and small & medium buildings (GFA: less than 5,000 tsubo) in Tokyo 23 Wards since 2011. In Q1 2020, the rate dropped among large buildings by 0.16 points to 0.58% and rose among small & medium buildings by 0.02 points to 0.85%.

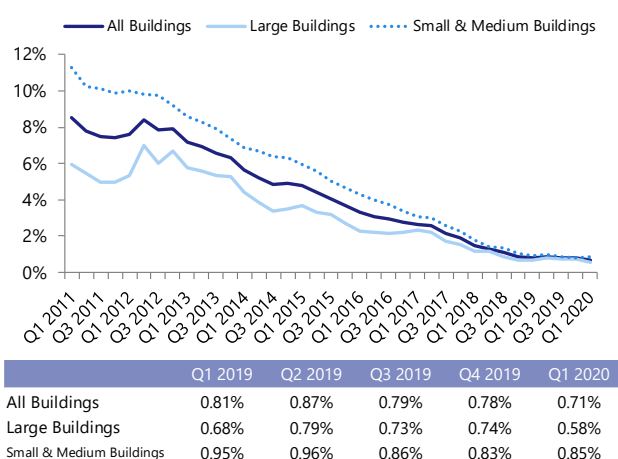
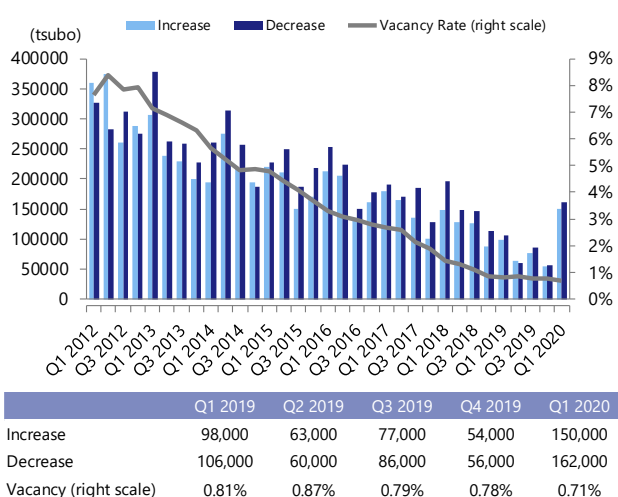
Figure 2: Vacancy Rate (by Size)

Figure 3: Increase and Decrease in Vacancies (23 Wards, All Sizes)


Figure 3 indicates the **increase and decrease in vacancies**. The increase was 150,000 tsubo and the decrease was 162,000 tsubo in Q1 2020. The decrease exceeded the increase for the third consecutive quarter, as new properties were nearly fully occupied at completion and vacancies of existing buildings were also promptly filled.

Both increases and decreases in vacancies were significantly larger than in the previous quarter as there was a greater amount of new supply of vacant space from multiple large office buildings that were newly completed.

Figure 4: Vacancy Turnover Ratio
(4-quarter moving average)

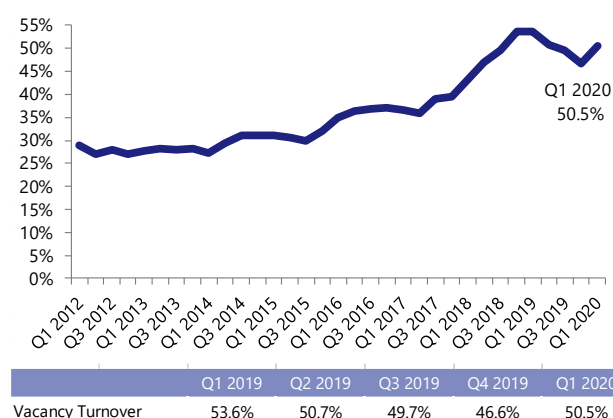
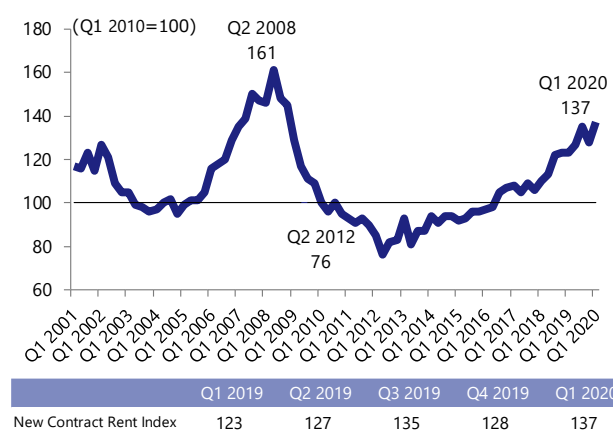


Figure 4 shows the **vacancy turnover ratio (four-quarter moving average)**, the rate of vacancies leased to tenants during the quarter to the total vacant office stock (vacant office stock at start of quarter + vacancies added during the quarter). The ratio remained high at 50.5% in Q1 2020, up 3.9 points from the previous quarter. With the ratio trending at around 50% over the past year, vacancy turnover in the office market continues to be robust.

Figure 5: New Contract Rent Index



New Contract Rent

Figure 5 is the **new contract rent index**, which is the rent level for new lease contracts. The index for Q1 2020 was 137, up 9 points quarter on quarter and up 14 points year on year. New rent has continued to rise since Q2 2012. Due to record low vacancy rates in Tokyo 23 Wards and the scarcity of vacant office stock in the market, as well as the completion of many large office buildings in central Tokyo during Q1 2020, more lease contracts were concluded at high rent levels.

Figure 6: New Contract Rent Index (by Size)

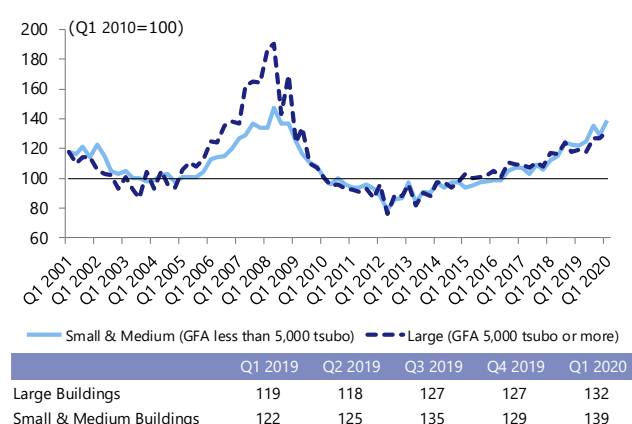


Figure 6 shows the new contract rent index **by size of building**. The index for large buildings with a GFA of 5,000 tsubo or more rose by 5 points quarter on quarter to 132, and that for small & medium buildings with a GFA of less than 5,000 tsubo increased by 10 points to 139. The rising trend since Q2 2012 has continued in both sizes of buildings.

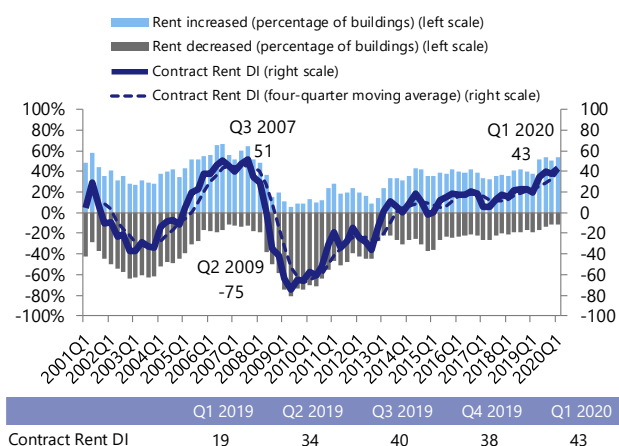
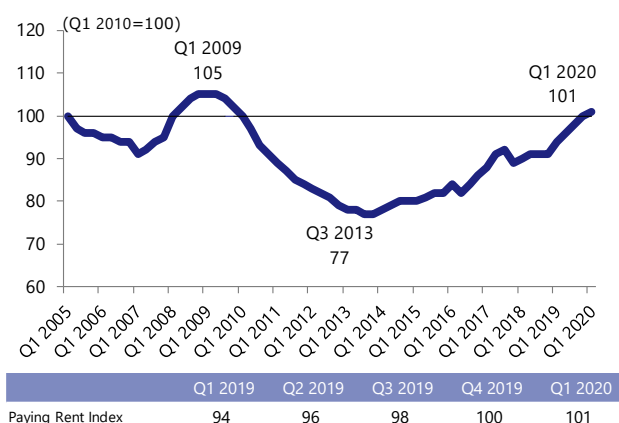
Figure 7: Contract Rent DI


Figure 7 is the **contract rent diffusion index (DI)** (the percentage of buildings with a rent rise minus that of buildings with a rent decline), which indicates the direction of changes in new contract rents. The DI in Q1 2020 was +43, indicating there were more buildings with a higher new rent than six months ago than those with a lower new rent. The DI has remained above zero for 20 consecutive quarters.

Paying Rent

Figure 8 shows the **paying rent index**, which includes both new lease rents and existing lease rents. The index in Q1 2020 was 101, up 1 point quarter on quarter and up 7 points year on year. The upward trend since Q3 2013 has continued. Negotiations for raising the rent upon renewal of contract have been taking place on the back of continued strong demand for offices, which are likely to have led to the rise in paying rent.

Figure 8: Paying Rent Index


Free Rent

Figure 9 indicates the percentage of new lease contracts with free rent to all new lease contracts (**ratio of free rent offered**) and the average free rent period (**average free rent months**). In Q1 2020, the average free rent months were 3.3 months among lease contracts with free rent, 0.1 months more than the previous quarter, and 1.2 months among all new lease contracts, 0.1 months less than the previous quarter.

The ratio of free rent offered, which had been dropping since 2011, has remained flat since around 2016, indicating that the custom of offering free rent has become common across the market. The drop in the ratio in Q1 2020 was likely a result of lessors' long-standing advantage reflected in free rent.

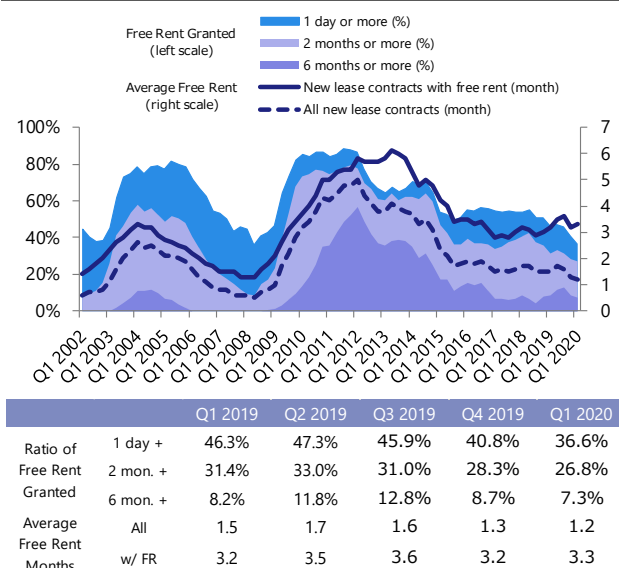
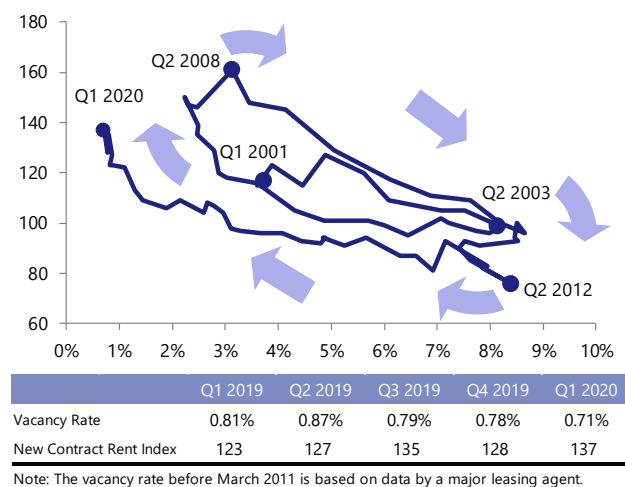
Figure 9: Free Rent


Figure 10: Market Cycle

Market Cycle

Figure 10 plots the vacancy rate on the horizontal scale and the new contract rent index on the vertical scale on a quarterly basis. It shows the cyclical nature of the market, with the chart trending to the lower right in 2001 (vacancy up, rent down), remaining flat in 2003–2004, then trending to the upper left in 2005 (vacancy down, rent up) and to the lower right again in 2008 (vacancy up, rent down).

The office lease market entered a recovery phase in 2013, with the trend continuing in Q1 2020.

However, the chart moved to the upper left due to a drop in the vacancy rate and a rise in new rent compared to the previous quarter.

Although office market indicators have continued in their trends in Q1 2020, there have been some cases where tenants have refrained from relocating their offices due to the new coronavirus outbreak.

Reference

Figure 11: Major Building Completions (Q1 2020)

| Name | Floors Above Ground / Below Ground | Ward | Address | Completion | Total floor area (tsubo) |
|--------------------------------|--|----------|------------------------|------------|--------------------------------|
| Toranomon Hills Business Tower | 36/3 | Minato | 1-17-1 Toranomon | 2020/01 | 52,310 |
| YOTSUYA TOWER | 31/3 | Shinjuku | 1-6-1 Yotsuya | 2020/01 | 42,227 |
| KANDA SQUARE | 21/1 | Chiyoda | 2-2-1 Kanda Nishikicho | 2020/02 | 25,790 |
| Otemachi One Tower | 40/5 | Chiyoda | 1-2-1 Otemachi | 2020/02 | 63,949 |
| Kamiyacho Trust Tower | 38/3 | Minato | 4-1-1 Toranomon | 2020/03 | 59,045 |
| Toyosu Bayside Cross Tower | 36/2 | Koto | 2-2-1 Toyosu | 2020/03 | 55,886 |

Source: Compiled by Xymax Real Estate Institute based on information released by the companies.

Figure 12: Major Office Relocations (Q1 2020)

| Company | From | To | Month Year | Purpose | Size (tsubo) |
|-----------------|--|--|---------------|-----------------------|-----------------|
| Yusen Logistics | Sumitomo Fudosan Shiba-Koen Tower <i>Minato Ward</i> | Shinagawa Seaside Park Tower <i>Shinagawa Ward</i> | May 2020 | Greater efficiency | 500 |
| AI CROSS | Toranomon 30 Mori Bldg. <i>Minato Ward</i> | Atago East Bldg. <i>Minato Ward</i> | May 2020 | Expansion | 130 |
| TIS | Sumitomo Fudosan Shinjuku Grand Tower <i>Shinjuku Ward</i> | Toyosu Bayside Cross Tower <i>Koto Ward</i> | FY2021 | Consolidation | 10,000* |
| Intec | Intec Tokyo Bldg. <i>Koto Ward</i> | Toyosu Bayside Cross Tower <i>Koto Ward</i> | FY2021 | Consolidation | 10,000* |

Source: Compiled by Xymax Real Estate Institute based on information released by companies.

The sizes of office space are estimates.

*The office size for TIS and Intec is 10,000 tsubo combined.

| Survey Overview | | | | |
|-----------------------------|---|---|---|--|
| | Vacancy Rate | Increase and Decrease in Vacant Space | Vacancy Turnover Ratio | New Contract Rent Index |
| Description | Vacant space versus total office stock in the market. | A quarterly increase and a quarterly decrease in volume of vacant space in the market. | The ratio of the vacant space leased during the quarter to all the vacant office stock in the market. | Office rent index based on new contract rents. This index uses a statistical method to remove property-specific influences such as size and age of buildings. |
| Main Point | Supply and demand balance in the market | Supply and demand balance in the market | Supply and demand balance in the market | Level of contract rents |
| Sector | Office Building | | | |
| Market | Tokyo 23 Wards | | | |
| Building Size | GFA 300 tsubo or more | GFA 300 tsubo or more | GFA 300 tsubo or more | GFA 300 tsubo or more |
| Release | Every Quarter | | | |
| Data Source | Data of available vacant spaces and buildings. Independently collected by Xymax. | Data of available vacant spaces and buildings. Independently collected by Xymax. | Data of available vacant spaces and buildings. Independently collected by Xymax. | Data of new contract rents including CAM charge. Independently collected by Xymax. |
| Data Used in Recent Quarter | 8,584 buildings | 3,812 contracts | 3,812 contracts | 198 contracts |
| How to Calculate | <ul style="list-style-type: none"> • Vacancy rate = vacant space ÷ rentable space • Vacant Space Total available vacant space in completed buildings as of the time of the research. • Rentable Space Rentable space of completed buildings as of the time of the research. <p>Where rentable space is not available, the rentable space is estimated from the gross floor area of the building using the formula developed in the joint study with the laboratory of Professor Naoki Kato at Kyoto University Graduate School of Engineering.</p> | <ul style="list-style-type: none"> • Increase in volume of vacant space <ul style="list-style-type: none"> a. Space in existing buildings formerly occupied by tenants b. Total rentable area of new completions • Decrease in volume of vacant space <ul style="list-style-type: none"> a. Space in existing buildings leased under a new agreement b. Space in new completions but lease is signed prior to the completion c. Space that had been vacant but the owner decided not to lease <p>Where rentable space is not available, the rentable space is estimated from the gross floor area of the building using the formula developed in the joint study with the laboratory of Professor Naoki Kato at Kyoto University Graduate School of Engineering.</p> | <ul style="list-style-type: none"> • Vacancy Turnover Ratio = Volume of vacant space leased during the quarter ÷ (Initial vacancy + Vacancy added during the quarter) Then, compute the four-quarter moving average amount with the ratio derived from this formula. • Volume of vacant space leased during the quarter: Same as the "decrease in volume of vacant space". • Initial vacancy: Total volume of completed buildings that are available for lease as of the start of the quarter. • Vacancy added during the quarter: Same as the "increase in volume of vacant space" | <ol style="list-style-type: none"> 1) Develop a rolling hedonic model (overlapping period: five quarters) based on the collected new contract data with property-specific factors as variables (location, building size, building age, facilities, date of signing of lease, etc.). 2) Estimate the quarterly contract rent by assigning the values of a typical building to the model developed in the preceding step. 3) The New Contract Rent Index is the rent estimated in the preceding step based on Q1 2010 as the base point (=100). <p>This model shows changes in new contract rents after removing property-specific variables.</p> |

| | Contract Rent DI | Paying Rent Index | Free Rent Granted (%) & Average Free Rent (Month) |
|-----------------------------|---|---|--|
| Description | Index of changes in new contract rents. Calculated by counting and comparing the buildings where rent has increased and those where rent has decreased. | Index of changes in paying rents (new and existing contract rents). | Distribution of free rent and average length of free rent period. Free rent is the time lag between the start of the contract and the start of the rent payment. |
| Main Point | Direction of contract rent trends | Level of rents paid by tenants | Market trends that are not reflected in contract rents |
| Sector | Office Building | | |
| Market | Tokyo 23 Wards | | |
| Building Size | All | GFA 300 tsubo or more | All |
| Release | Every Quarter | | |
| Data Source | Data of new contract rents including CAM charge. Independently collected by Xymax. | Data of new and existing contracts signed for buildings under management by Xymax. | Data of new contracts signed for buildings under management by Xymax. |
| Data Used in Recent Quarter | 491 contracts | 4,148 contracts | 246 contracts |
| How to Calculate | <ol style="list-style-type: none"> 1) Compare the data of new contract rent per tsubo with that in the 6-month prior period in the same building. Each contract was counted separately into three categories: buildings with "rent increase", "no change" or "rent decrease" 2) Calculate the percentage of buildings with "rent decrease" and buildings with "rent increase". 3) Subtract the percentage of buildings with "rent decrease" from the percentage of buildings with "rent increase". This outcome is the Contract Rent Diffusion Index (DI). | <ol style="list-style-type: none"> 1) Calculate the rent per tsubo of each tenant from the data of new and existing lease contracts and memorandums. 2) Develop a rolling hedonic model (overlapping period: five quarters) based on the rents calculated in the preceding step (the "paying rent") with property-specific factors as variables (location, building size, building age, facilities, date of signing of lease, etc.). 3) Estimate a quarterly contract rent by assigning the values of a typical building to the model developed in the preceding step. 4) The Paying Rent Index is the rent estimated in the preceding step based on Q1 2010 as the base point (=100). <p>With this method, influences from replacement of sample data and deterioration of buildings over age are removed from the result.</p> | <ul style="list-style-type: none"> • Free Rent Period The period between the start of the contract and the start of the rent, shown in number of days. • Ratio of Free Rent Granted The ratio of contracts with free rent in all the new contracts (excl. contracts for expansion within the building and recontracts) • Average Free Rent (Month) of All the Contracts The simple average of the free rent period including lease contracts with no free rent. • Average Free Rent (Month) of Contracts with Free Rent The simple average of the free rent period of lease contracts with free rent. <p>In some cases, the rent agreed in a lease contract includes CAM charge, and then, for a certain period of time, the rent is reduced to the CAM charge equivalent or closer level, but such contracts are excluded from this research.</p> |

Appendix: Xymax REI Research Updates (February 2020 – April 2020)

Changes in the Use of Real Estate Over Time –Fukuoka **March 24, 2020**

- This report is a summary of the results of a survey on the changes in the use of real estate in central Fukuoka, namely the Tenjin/Hakata/Gofukumachi area, between 1997 and 2017, following a report on Osaka city that was released in 2017.

Best Practices of Small-to-Medium-Sized Buildings – The 2nd Report **April 7, 2020**

- This report is a compilation of excellent initiatives by building owners who own small-to-medium-sized buildings and lease them out, based on a case study through a questionnaire survey and interview with the owners.

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