

## Real Estate Strategic Outlook: Japan

### Healthy inflation for the first time in decades

#### A gradual shift of loose monetary policy is ongoing.

For the first time in decades, Japan faces inflationary pressures with the weakened yen and surging energy prices, with a CPI print of 2.9% in October 2023. The Bank of Japan maintained its loose monetary policy, while executing its gradual policy shift by raising the cap on the government bond yield or Yield Curve Control (YCC), allowing it to go above 1% in October 2023. Despite the increasing market uncertainties, the BoJ is expected to make further policy changes in 2024 such as eliminating the negative interest rate if the robust wage settlement is confirmed.

The ten-year Japanese government bond yield went up to 0.95% by end-October 2023, the highest level in a decade, and is expected to increase further in the coming years.

### A window to sell non-strategic assets and optimize portfolios towards strong long-term growth potential.

#### Mild pricing correction opens a window for portfolio optimization.

Since the end of 2021, the Japanese real estate market has been an outlier globally with continuous compression of transaction yields and stable lending circumstances, in stark contrast to significant capital value corrections in most other global real estate markets. However, the aforementioned potential monetary policy shift in 2024 may trigger a mild pricing correction in Japan's real estate market, especially in the tight Tokyo market.

This market momentum may present a window of opportunity for investors to optimize their portfolio and recycle capital for opportunities in markets with strong long-term growth potential such as regional logistics or living sectors.

### Logistics: Short-term market disruption and limited supply pipeline

New modern multi-tenant logistics supply in Greater Tokyo reached 3 million square meters in 2023, hitting record levels for three consecutive years, while the vacancy rate is likely to remain above 8% in 2024. A more modest supply is expected in Greater Osaka in 2023 and 2024 with tighter vacancy rates forecast at around 5%. On the other hand, the impact of rising construction costs is expected to potentially delay or

even cancel the planned supply beyond 2025. This should aid the rental uplift, further supported by the lack of truck drivers particularly from 2024 onwards due to regulatory changes.

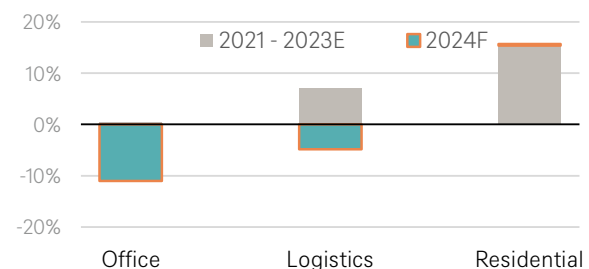
### Residential: Strong demand for family-type residential

Residential rents for family-type units with multiple bedrooms in the central nine wards in Tokyo continued to post strong growth of 8.4% year-on-year in August 2023, driven by leasing demand from working couples and professionals who prefer larger spaces for their work-from-home arrangements. The market momentum for condo price increases could weaken depending on the potential shift of monetary policy by the Bank of Japan in 2024, while leasing demand for good quality rental houses are expected to remain resilient in the coming years.

### Office: Large supply will keep the vacancy rate high

The average office vacancy rates in Tokyo's central five wards continued to hover above 6% since June 2021, reaching 6.0% in November 2023, while the vacancy of new buildings stood at 34.1% in the same period. Despite a gradual recovery of pent-up office leasing demand from relocation requirements and healthy service industries, rampant hybrid working models and unabated supply waves put continuous upward pressure on the overall office vacancy rate, leaving fringe submarkets more vulnerable to leasing competition. Tokyo's office vacancy rate is expected to remain elevated at least until 2026 due to the large incoming office supply.

### Capital Growth Movements Forecast. 2021-2024F



Source: DWS, January 2024

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