MARKETBEAT

JAPAN

Investment H1 2023

	YoY Chg	12-Mo. Forecast
3.0% Prime Office Cap Rate*	—	—
4.7% NOI Yield (against acquisition cost), J-REIT**	▼	▼
JPY 6.3 T institutional Real Estate Investment Transaction Total***	▼	▲

MAJOR MARKET INDICATORS H1 2023

	YoY Chg	12-Mo. Forecast
0.4% 10-Year JGB Yields	▲	—
1.3% Annual Real GDP Growth Rate[1]	▲	▼
4.1% J-REIT Dividend Yield	▲	—
16.1% Real Estate Loans to GDP (%)	▲	▼

** Cushman & Wakefield*
*** The latest quarterly financial statements from respective J-REIT*
**** MSCI, Japan Real Estate Securitization Association, LTM12 total*

[1]2023 real GDP seasonally adjusted consensus estimate, annualized
Source: Ministry of Finance; Ministry of Internal Affairs and Communications; Japan Association of Real Estate Securitization; Bank of Japan.

Economy: Cost-Push Inflation to Persist, Limiting Availability of Liquidity Buffer for Some Investors

Japan's real GDP is now expected to grow at around 1.3% in 2023, reverting to the level prior to the Abenomics era, as the ongoing recovery of exports and domestic services consumption since the end of 2022 have been offset by increasing cost pressures and negative real wage growth since early spring. However, the rapid rate hike cycle in the U.S., a sustained hawkish stance in the ECB, and tightening lending standards globally, are expected to limit advanced economy economic growth to around 0.5% p.a. until 2024. Furthermore, yen weakness is expected to continue at least until the 10-year interest rate, trailing at around 0.4%, reverts to 0.8%, with a neutral interest rate policy approach under BOJ governor Ueda in response to the prevailing low economic growth. Given the widening disparity in policy rates in major markets, the yen is currently expected to drift downwards to a historical low of 150 to the U.S. dollar.

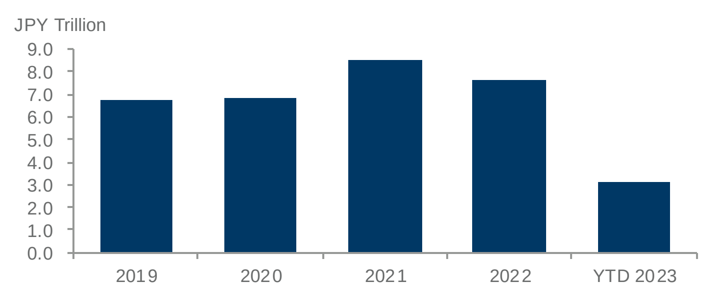
Japan's Positive Spreads Attracting Foreign Funds, Despite 22% Cyclical Dip in Transactions

Total transaction volume in the 12 months ending June 2023 totaled JPY6.3 trillion, down 22% y-o-y. The cyclical decline was attributed to an absence of large transactions, along with rising interest rates globally. In the lending environment, banks' outlook on real estate transactions remains supportive, raising the ratio of real estate loans to total loans to 16.7%. Even assuming the downside scenario of the 10-year interest rate rising toward 1%, Japan's cash-on-cash return is expected to remain positive, unlike other major markets.

By investor type, the scope of market participants has been expanding, with non-domestic investors increasing their share of large-scale transactions, together with some retail investors. Summarizing the net transaction volume since the end of 2019, foreign funds / institutional investors have emerged as the net buyers, while JREIT corporations are now the net sellers as they seek to realize their capital gains. With growing concerns on the interest rate outlook, we expect JREITs with higher financial leverage to see limited upside to NAV in the coming quarters.

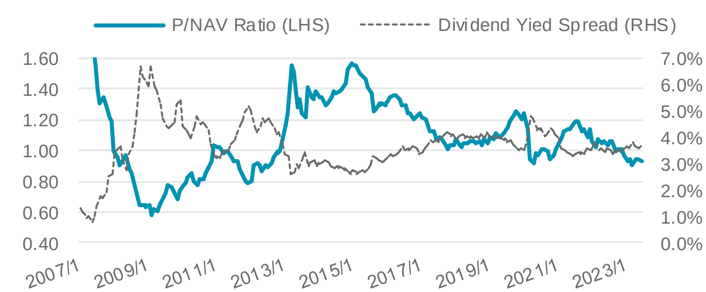
By asset sector, allocation to office property remains high, representing 43% of the total volume. In addition, allocation to hotel properties is expanding as more investors seek assets that are favorable to hold in an inflationary environment. The increasing allocation to the hotel sector mirrors the declining allocation to retail, as urban retail assets are yet to see a recovery in rent and capital values. Elsewhere, allocation to logistics remains unchanged at 16%, as some investors turn more cautious due to increasing cost pressures on logistics facilities. Allocation to the multifamily sector remains unchanged at 21% of total volume.

Historical Real Estate Transaction Volume (Annualized)



Source: MSCI, Cushman & Wakefield

Historical Trend : J-REIT Monthly P/NAV Ratio Since 2007



Source: Japan Association for Real Estate Securitization; Ministry of Finance

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Widening Bid-Ask Spreads With Rising Cost of Capital

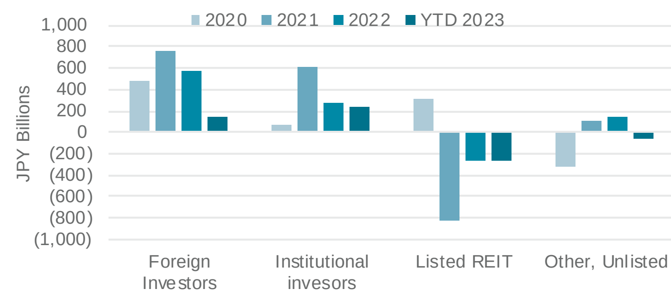
The inflation outlook resulted in little change in expected yields among domestic investors. However, with an anticipated rise in risk premiums, price expectations between buyers and sellers continues to diverge. By asset class, hotel cap rates remain elevated around the upper 4% mark, as their performance recovery is yet to be realized in cashflows. Office cap rates remain unchanged around the mid-3%, despite deteriorating cashflow yields due to weaker performance of less competitive buildings. By area, Tokyo's prime office cap rates also remain unchanged around 3%, maintaining the lowest level since 2007. Regionally, APAC office demand shows a similar trend, reflecting high office worker attendance rates, keeping office cap rates at low levels. This contrasts with U.S. gateway cities, with higher prevalence of hybrid and remote working and lower office attendance rates, tracking under 60%, resulting in elevated cap rates, tracking at 5.5% in Manhattan and 4.8% in San Francisco.

Notable investment transactions in 1H 2023 include a series of large inflows from overseas funds. Two major domestic hotel assets were sold, to KKR and Bentall Green Oak respectively. Elsewhere, Blackstone sold its logistics portfolio to GIC, as the latter expand their core investment portfolio. Sekisui REIT also reported a rare sale of an urban data center to its sole tenant, converting the usage to an owner-occupied data center.

Outlook

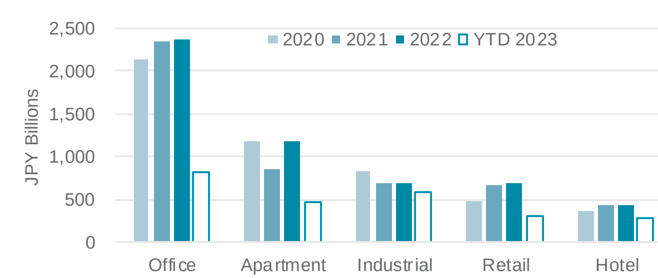
- Focus on macro factors with scenario analysis for potential monetary policy change over the next 12 months.
- Expect domestic investors' trading volume to drift lower in response to widening bid-ask spreads.
- Recommend urban logistics and high-end rental housing for core funds with large liquidity positions.
- Recommend well-located assets for (re)development and high-end hotels with (re)pricing upside for value-add funds with higher risk tolerance.

Net Transaction Volume by Investor, Since the end of 2019



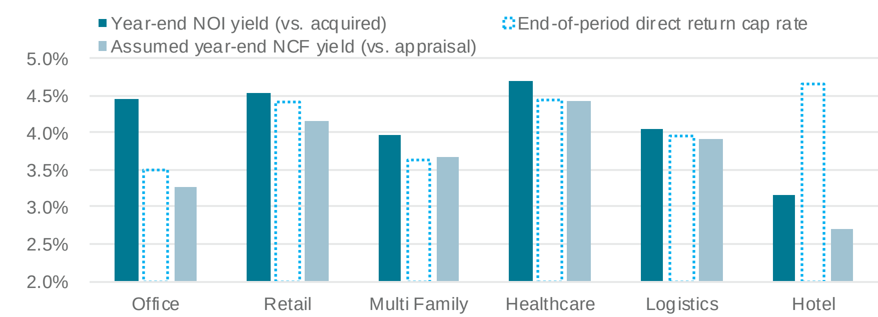
Source: MSCI, Cushman & Wakefield

Investment Transactions* by Use, Since 2019



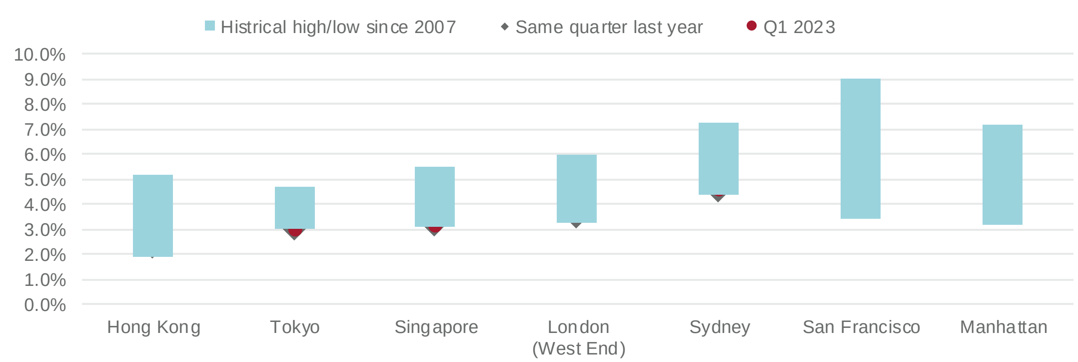
*Source: MSCI, Cushman & Wakefield, * excluding land for development*

Cap Rate / Yields by Asset Class, LTM 12



Source: Calculated based on the most recent financial results of the respective J-REIT, and assumed NCF are calculated by subtracting the previous 7 annual Average of capital expenditures from NOI, cap rates based on appraisal value

Historical Trends of Prime Office Cap Rate by City, Since Q1 2007



Source: Cushman & Wakefield

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Investment Transactions by Property Type (Last 12 Months)

PROPERTY TYPE	NUMBER OF PROPERTIES	VOLUME (JPY B)	CAP RATE (LOWER - UPPER LIMIT)
Office	262	¥1,856	2.0% - 6.3%
Logistics	82	¥693	2.8% - 5.4%
Multi-Family	383	¥825	2.5% - 5.1%
Retail	97	¥511	3.2% - 5.3%

Source: MSCI, as of the end of June 2023

Investment Assets Under Management

PROPERTY TYPE	ASSETS UNDER MANAGEMENT (JPY B)	Y-O-Y NET CHANGE	ANNUAL INCOME RETURN	ANNUAL CAPITAL RETURN
Office	¥12,004	6.5%	3.9%	1.5%
Logistics	¥6.167	12.0%	4.3%	4.0%
Multi-Family	¥4,944	11.5%	4.3%	3.4%
Retail	¥3,907	2.9%	4.5%	-0.9%

Source: Japan Real Estate Securitization Association (AJPI); Final figures as of end-September 2022 as of end-June 2023

Ratio of Unrealized Gain by Sector

PROPERTY TYPE	UNREALIZED GAIN (JPY B)	RATIO TO BOOK VALUE
Office	¥1,936	24.7%
Logistics	¥1,250	30.6%
Multi-Family	¥1,212	35.1%
Retail	¥523	18.2%

Source: Calculated based on the most recent quarterly financial results of all holding assets as reported by J-REIT

Major Transactions in the Order of Transaction Size (Last 6 Months)

PROPERTY NAME	TYPE	BUYER	SELLER	PRICE (JPY B)	GFA (Tsubo)	PRICE / JPY per Tsubo	CAP RATE	Location
Tokyu Plaza Ginza	Retail	Sumitomo Mitsui Trust Panasonic Finance	Tokyu Land	¥136.5B	14,727	¥9.3M	-	Chuo-ku, Tokyo
Logistics Facility Portfolio (6 buildings)	Logistics	GIC	Blackstone	¥106.2B	-	-	-	Includes Iwate, Aichi, Ibaraki, Nagano, Fukuoka,
Logistics Facility Portfolio (7 buildings)	Logistics	Gaw Capital Partners	Blackstone	¥80.0B	76,600[1]	-	-	Chiba, Tochigi, Ibaraki, Kanagawa, and Saitama prefectures
Odakyu Dai-ichi Life Building	Office	Domestic Corporations Contributed by Dai-ichi Life Insurance, etc.	Odakyu Electric Railway	¥71.0B	21,242[2]	¥5.3M	-	Shinjuku-ku, Tokyo
Gotenyama SH building	Data center	TIS	Sekisui House Reit Investment Corporation	¥70.0B	5,993	¥11.6M	2.9%	Shinagawa-ku, Tokyo
Odakyu Century Building	Hotel	SPC in which KKR funds and others invest	Odakyu Electric Railway	¥57.0B	21,632	¥2.6M	-	Shinjuku-ku, Tokyo
Rihga Royal Hotel	Hotel	Bentoll Green Oak	Royal Hotel	¥55.0B[3]	52,898	¥1.0M	-	Osaka-shi, Osaka

[1] Assumption, [2] Transaction area, [3] Estimate
Source: MSCI, Nikkei Real Estate Market Data, press releases on each company's website

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