

Intelligent Investment

Appetite for Japanese real estate to remain strong as investors shift strategy

VIEWPOINT

**MOST INVESTORS FORESEE
INTEREST RATES RISING, AND
ARE CALIBRATING THEIR
INVESTMENT STRATEGIES**

CBRE RESEARCH
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Introduction

Although commercial real estate transaction volume*¹ declined by 20% y-o-y globally in 2022, investment volume in Japan remained largely unchanged, with only a 2% fall from the previous year. This resilience was largely due to the Bank of Japan (BoJ) maintaining its easy monetary policy, in contrast to most of the other major central banks pursuing a monetary tightening policy to counteract inflation.

Conducted in November 2022, CBRE's 2023 Asia Pacific Investor Intentions Survey*² found more than half of the investors active in the Japanese market (including overseas-based investors) expect the BoJ to raise interest rates in 2023. Despite this assumption, appetite for investment in Japanese real estate shows no signs of weakening. However, more investors expect prices for some asset types to decline as a result of higher interest rates, while other asset types are attracting stronger interest due to potential upside in cashflow. It therefore appears that while many investors foresee interest rates rising, they plan to take the opportunity to calibrate their investment strategies based on the specific market situations of each asset type.

Based on the findings of CBRE's 2023 Asia Pacific Investor Intentions Survey, this report analyses the strategies investors intend to utilise in the Japanese real estate market this year and assesses the effects of a possible change in monetary policy by the BoJ. Some of the main points from the survey results are as follows:

- 52% of investors anticipate that their investment volume in 2023 will exceed that of the previous year, only a slight decline from the 54% who said the same in 2022.
- 56% anticipate that the BoJ will raise interest rates during 2023, while 42% expect any increase to come in 2024 or beyond.
- While offices remain the most preferred asset type, the number of investors selecting offices as their primary focus declined from the previous year, with increases seen for residential as well as hotels & resorts.
- When asked which asset type was most likely to see transaction prices exceed sellers' asking prices, hotels were the most selected answer. The number of investors selecting logistics facilities, last year's leader in this category, declined.
- While "core" remains the most popular investment strategy, interest in this approach fell slightly compared to the previous year. In contrast, "opportunistic" showed a significant surge, being selected by twice as many investors as last year and emerging as the second most preferred strategy (compared to fourth place last year, behind core, value-added, and core-plus).

*¹ [Global Investment Declines Sharply in Q4 2022, February 8, 2023](#)

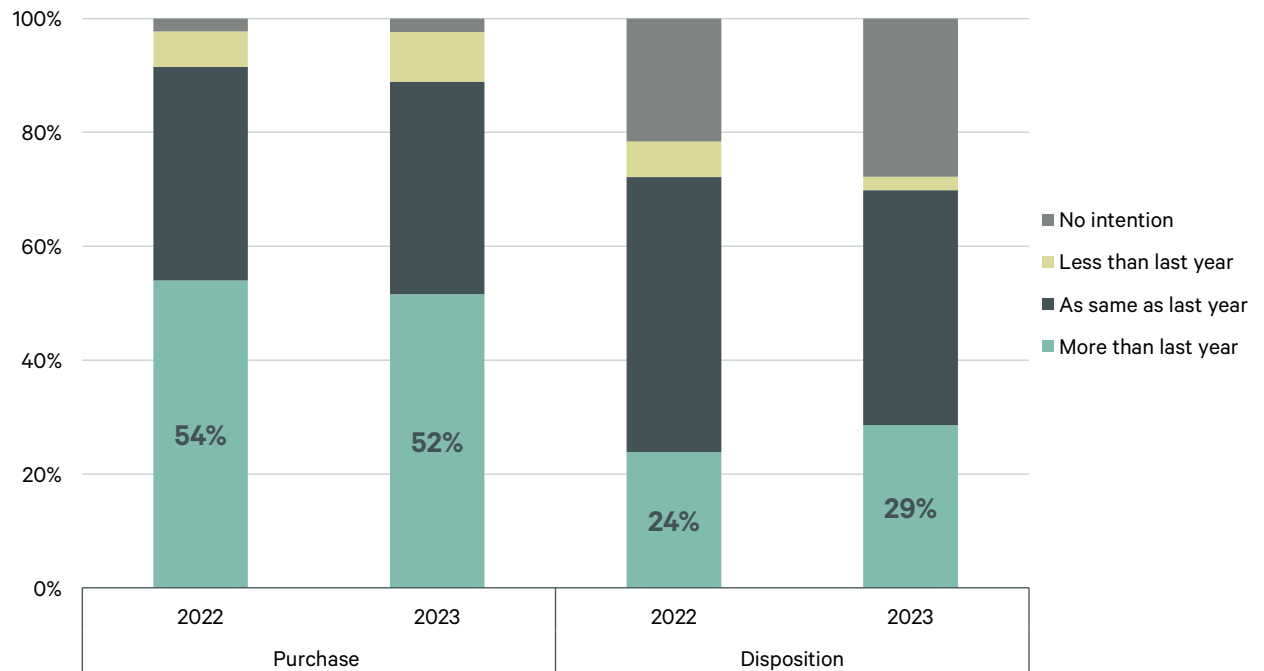
*² [2023 Asia Pacific Investor Intentions Survey: Japan Results](#)

Robust appetite among Japanese investors

CBRE’s 2023 Asia Pacific Investor Intentions Survey found that the number of Japan-focused investors (including both Japanese investors and foreign-based investors selecting Japan as their primary investment market) planning to increase their investment volume in 2023 was 52%, almost unchanged from the 54% of respondents to the previous year’s survey who indicated that they planned to increase their investment in 2022 (Figure 1).

Some 29% of the investors indicated that they plan to increase their disposition volume in 2023, a small increase from the previous year’s 24%. However, almost 70% of respondents intending to increase disposition also stated that they intend to increase their investment. This shows that even those investors planning to sell some of their assets retain a positive view towards the Japanese commercial real estate market as a whole. The findings indicate that many investors see the market reaching a turning point, with interest rates bottoming out but transaction prices remaining high for some asset classes and seeing it as an opportune timing to review their portfolios.

Figure 1: Purchase volume and disposition volume projections for 2023



Note: Answers provided by investors for whom Japan is their primary investment target. 85% of respondents invest exclusively in Japan, while foreign-based investors comprise 25% of the total.

Source: 2023 Asia Pacific Investor Intentions Survey: Japan Results, CBRE Research, March 2023

Investment appetite remains robust despite anticipated interest rate hikes

Some 81% of surveyed investors identified “changes in monetary policy” as the number one risk facing the property investment market in 2023. Asked when they anticipated the Bank of Japan to raise interest rates, 56% of respondents selected 2023. However, among those investors who anticipate an interest rate hike in 2023, 54% plan to increase investment volume in 2023 (Figure 2, left). This figure is in line with the 52% of all respondents who plan to increase investment, and identical to last year’s result for the same question. Anticipated changes in monetary policy therefore appear insufficient to deter investors from continuing to invest in the Japanese property market.

That said, when asked why they remain keen to invest in Japanese real estate, roughly 40% of those respondents who anticipated an interest rate hike in 2023 indicate that they expect asking prices to be lowered somewhat, making properties more affordable (Figure 2, right). Many among this cohort of investors, who expect interest rates to rise, expect to remain active on the purchasing side assuming some price correction.

Figure 2: Those who anticipate rate hikes remain keen with an assumption for price correction

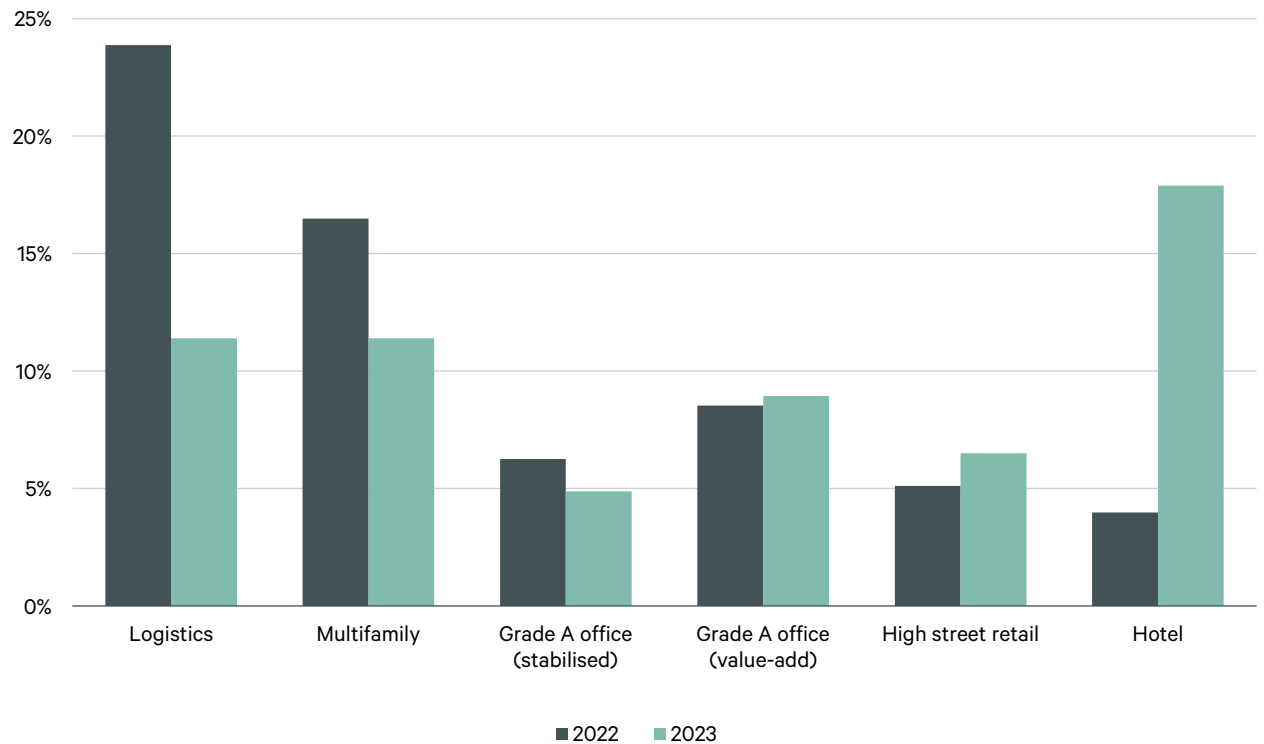


Source: 2023 Asia Pacific Investor Intentions Survey: Japan Results, CBRE Research, March 2023

Indeed, investors are already becoming more selective about asking prices for some asset types than was previously the case. The percentage of investors who project that transaction prices would exceed sellers' asking prices was down from the previous year for the logistics facility, multifamily, and office (Figure 3).

The largest decrease was seen in the logistics sector, where cap rates have come down to their lowest-ever levels despite rising market vacancy rates, causing some investors to display more caution. In contrast, the hotel sector saw a significant increase in the number of investors who anticipated transaction prices would exceed asking rates, reflecting anticipation for further improvement in hotel occupancy rates as a result of returning domestic and foreign tourists.

Figure 3: Price anticipated by investors by sector, "Willing to bid above asking prices"



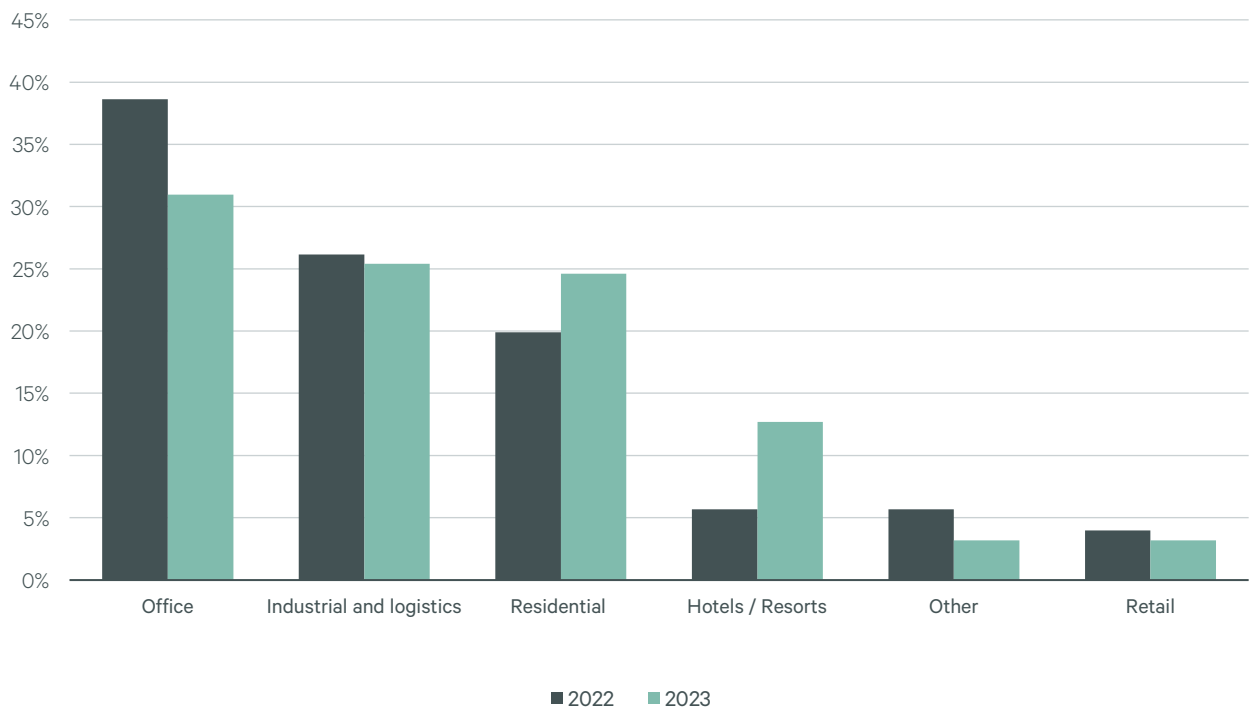
Source: 2023 Asia Pacific Investor Intentions Survey: Japan Results, CBRE Research, March 2023

Changes expected in investment targets and strategies

While the survey findings indicate that appetite for investment in Japanese real estate remains strong, changes have been observed in investors’ favored asset types and overall investment strategies.

Data concerning preferred asset types for investors in the Japanese market (Figure 4) reveal that offices remain the most sought-after property type, retaining their first-placed position from the previous year. Offices’ popularity most likely stems from their superiority to other asset types in terms of tenant diversification, liquidity, and transaction scale. However, the number of respondents selecting offices as their preferred asset type declined from the previous year’s survey, while multifamily as well as hotels & resorts attracted a higher share compared to 2022. As a result of loosening of the supply-demand balance in the leasing market, office market rents have been declining. This has led to a resurgence of interest in the stable cashflow provided by multifamily, and in the hotel sector whose cashflow is anticipated to recover.

Figure 4: Preferred asset types (single answer)

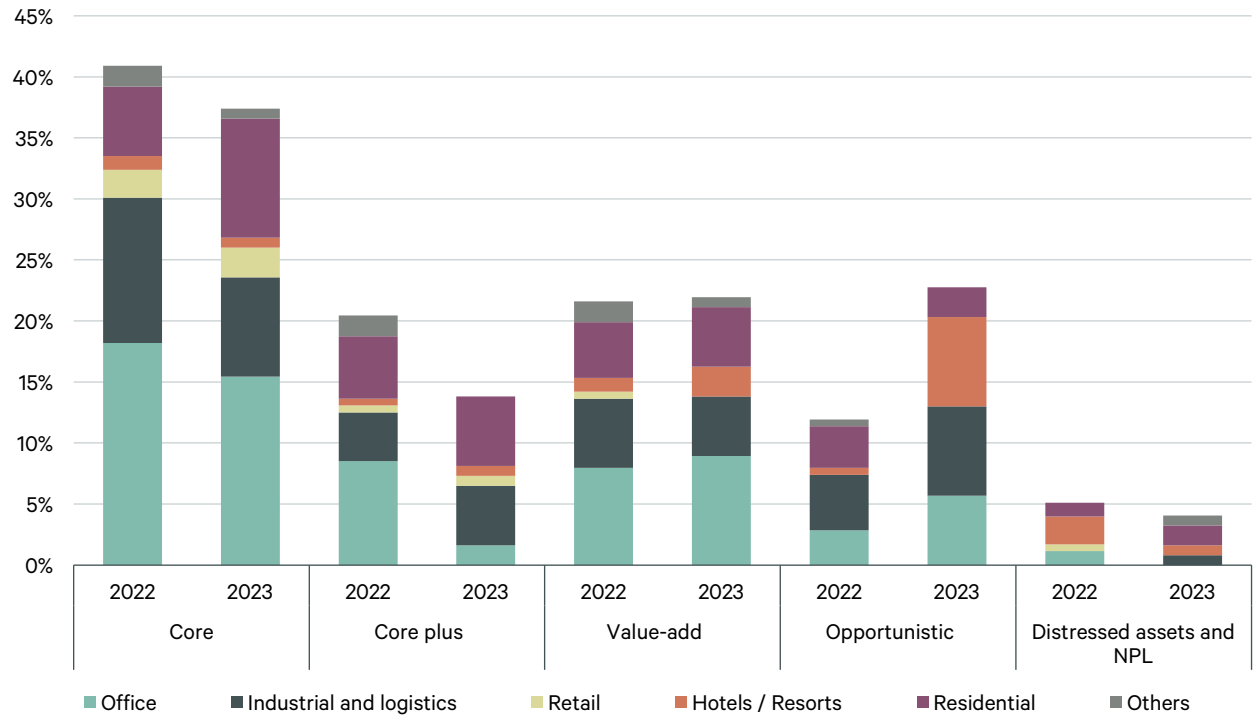


Source: 2023 Asia Pacific Investor Intentions Survey: Japan Results, CBRE Research, March 2023

When respondents were asked to select a preferred investment strategy, core remained to be the most-selected strategy. However, core’s popularity declined slightly from the previous year, while a significant increase was observed in the percentage of investors selecting opportunistic as their preferred strategy (Figure 5).

Changes were also observed in the preferred asset types within each strategy. For investors focusing on core assets, offices, and logistics facilities dropped in popularity, with the difference offset by stronger interest in multifamily. Investors planning to adopt an opportunistic strategy are focusing more on offices and logistics facilities as well as on the resurgent hotel sector. With prices for existing properties remaining high, an increasing number of investors are looking to maximise their returns by taking on the development risk. However, in metropolitan areas, it has become more difficult to secure higher returns due to the rising development costs. As such, depending on the asset type, such as logistics facilities, development projects are expanding in regional areas.

Figure 5: Preferred investment strategies (single answer)



Note: This graph features cross-plotting of the answers to “preferred investment strategy” and “preferred asset type”.
 Source: 2023 Asia Pacific Investor Intentions Survey: Japan Results, CBRE Research, March 2023

Conclusion: Investors seek greater profitability

While the BoJ did make some minor adjustments to its monetary policy on December 20, 2022, the policy remains unchanged as of March 2023. In February 2023, the incoming BoJ governor Kazuo Ueda indicated during his confirmation hearing that he intended to keep the bank's easy monetary policy in place. At present, the prevailing view of the financial market is that while the policy rate is likely to be kept at or below 0%, the cap on long-term bond yields may be raised further.

CBRE's 2023 Asia Pacific Investor Intentions Survey reveals that appetite for investment in the Japanese property market remains robust, even when a potential interest rate hike during the year is factored into account. However, changes in investment strategy suggest that investors are becoming more selective. Transactional yields have compressed to record low levels for properties in certain sectors and/or grades, making them less attractive to buyers. With interest rates anticipated to rise, investors of all strategies are expected to look for greater levels of profitability. Figure 6 summarises CBRE's investment projections and recommended investment strategies for each sector of the Japanese property investment market in 2023.

Figure 6: Real estate investment strategies for Japan in 2023

	2023 investment market projections	Recommended investment strategies
Office	New rents are set to continue to fall on the back of new supply, particularly in Tokyo. At the same time, an increasing number of tenants are seeking offices of higher quality. Strategies may focus on long-term investment in prime offices with high occupancy rates offering stable cashflow, or the value-added strategies in buildings with the potential for improved cashflow.	Core Value-added
Logistic	While occupier demand continues to grow, record amounts of new supply are planned in all major metropolitan areas. In terms of existing properties, only those in locations or with specs in high occupier demand are likely to be selected. Due to increased demand for dispersed logistics networks, investment in regional developments should also increase.	Core-plus Value-added Opportunistic
Multifamily	With demand for rental properties among the Japanese populace continuing to strengthen, and social and economic activity normalizing, stable demand can be expected in urban areas. Increases in the cost of living and labor shortages are also likely to exert upward pressure on wage. This may lead to higher asking rents, if real wage growth is realized.	Core Core-plus
Hotel	The recovery of domestic and foreign tourist demand has already led to significant recovery in hotel occupancy rates. Once Chinese tourist numbers recover, revenue should gain further momentum. In highly competitive areas where new developments started prior to the pandemic have come on stream, properties may offer prospects of improved cashflow through a change in operators.	Value-added Opportunistic
Retail (high street)	Encouraged by the return of both domestic and inbound tourist spending, broader range of retailers are keen to open new stores. However, most retailers remain cost-conscious. Owners will need to demonstrate flexibility with respect to retailer needs, by subdividing units or being amenable to short-term contracts, to improve occupancy rates and add value.	Core Value-added

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