SPOTLIGHT

Savills Research

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Tokyo Residential : Ultra Luxury

Tokyo's ultra-luxury market gains further momentum

Summary

- Tokyo's ultra-luxury residential market has grown on the back of the sector's sound fundamentals.
- Japan's stability has made the country a favourable avenue to preserve wealth.
- Large-scale redevelopment projects in the pipeline will add more ultra-luxury units and raise the top prices of the market to levels equivalent to those seen in Manhattan and London.
- The number of branded residences in Tokyo is likely to increase going forward, and this growth will accelerate especially if other sectors, such as offices,continue to face uncertainty.
- Some future projects are likely to change initial plans by replacing some space originally meant for offices with ultra-luxury residences.
- While there are many developments in the pipeline that are suitable to accommodate ultra-luxury units, the success of each project will be also determined by its ability to provide the expected levels of service while keeping costs under control.
- Japan's GDP growth per working age population has fared better than most of the other G7 nations over the last two decades, providing evidence of the country's long-term prospects. However, the negative impacts from the ageing population have had a lingering effect.

INTRODUCTION

Tokyo's ultra-luxury residential market[1] has continued to grow on the back of the redevelopment seen in the city. Tokyo has seen a slate of large redevelopment projects over the past few years which have added new landmarks and improved city infrastructure. Over the next decade, more projects are in store and will continue to reshape the city's physical and economic landscapes towards 2030 (please refer to our Japan's Prospects Towards 2030 report).

The ultra-luxury residential segment is expected to evolve further while Tokyo is undergoing this transformation. While the market is still considered a niche one, it is expanding. Indeed, before the pandemic, the total number of ultra-luxury units was around 50, but this figure has been steadily increasing. This could be primarily attributed to the recent mega-sized developments in areas such as Toranomon and Azabudai. Moreover, with the ambiguity about the office sector's prospects, it is also a possibility that some space originally planned for offices in new mixed-use towers will instead be sold as ultra-luxury or branded residential units.

Japan is home to one of the largest ultra-high-net-worth individual (UHNWI)[2] populations, which provides a strong demand base for the ultra-luxury market. Furthermore, overseas investors perceive the country as a suitable avenue for wealth mainly due to its economic and social stability, which have been especially attractive attributes during the pandemic. Although the world is gradually shifting towards normalcy from the pandemic, rising geopolitical tensions will likely lead to continued uncertainty.

In addition, Japan has steadily evolved into a luxury travel destination, and this could also be a tailwind for the progress of the ultra-luxury market. Despite its rich history and culture that appeal to many international visitors, the country was previously lacklustre in promoting inbound tourism. However, new initiatives by the previous Abe administration, as well as winning the right to host the 2020 Olympics changed the country's mindset, causing Japan to experience explosive growth in inbound tourism, although this was halted by the pandemic. A series of new luxury hotels openings across Japan also illustrates the gradual development of the country's luxury market. For instance, international hotel brands have been investing in new luxury hotels in Japan (please refer to Japan Hospitality February 2022). The development of ultra-luxury residences and luxury hotels are likely to have synergistic effects and solidify the country's status as a luxury destination. Moreover, the 2025 World Exposition, as well as the planned development of the country's first integrated resort (IR) in Osaka could be another boost for the ultra-luxury segment.

TOKYO'S ULTRA-LUXURY RESIDENTIAL MARKET

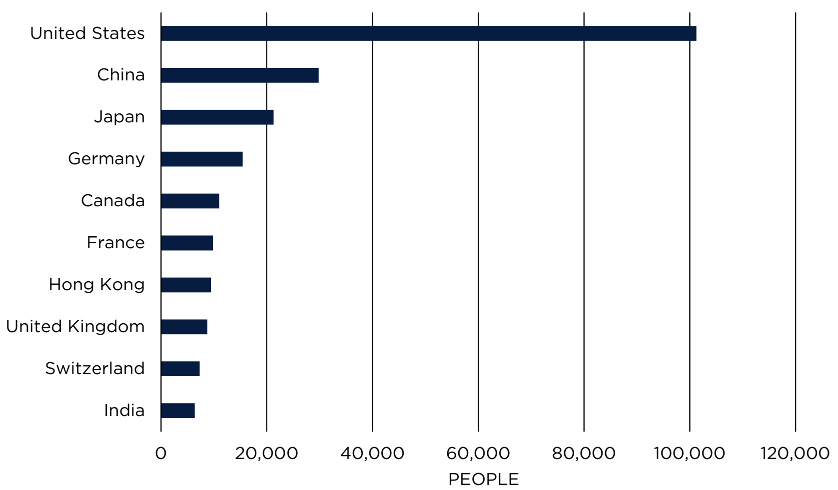
Tokyo's ultra-luxury residential market has grown over the past decade on the back of the country's stability and resilience. Considering the high concentration of UHNWIs in Tokyo, it is likely that the demand for ultra-luxury units has always existed, but remained dormant in the face of limited supply. This latent demand began to surface as some supply came to the market.

Considering that we define ultra-luxury

1 While there is no single definition of 'ultra-luxury' in the industry, for the purpose of this report, we will define ultra-luxury condominium units as those with sales prices at or more than JPY1 billion.

2 In this report, UHNWIs are individuals with over US$30 million in net worth.

GRAPH 1: Top 10 Countries/regions by UHNWI Population, 2020



Source Wealth-X, Savills Research & Consultancy residential units as those with sales prices at or more than JPY1 billion, only a small fraction of the population, even amongst UHNWIs, could afford those units. To reduce the risk of developing ultra-luxury residential units and make them more feasible for developers, they are often housed in residential towers where the majority of units are sold at more affordable prices, ensuring a steadier supply. Although ultra-luxury units are out of reach even for the majority of UHNWIs, the size of the wealthy in Japan serves as an essential foundation for the sector.

Indeed, according to a study by Wealth-X, Japan has the third largest number of UHNWIs in the world, only behind the U.S. and China. The same study shows that Tokyo ranks third, only behind New York and Hong Kong, while Osaka ranks ninth. Despite the pandemic, the population of UHNWIs has increased in Japan largely due to the appreciation of asset prices. This has demonstrated the resilience of the wealthy during tough times.

Many wealthy people are concentrated in Tokyo, and this has helped to attract and retain luxury amenities and entertainment in the city. For instance, Tokyo boasts 203 Michelin-starred restaurants according to the 2022 Michelin guide, and maintains its status as the top gourmet destination. Moreover, Tokyo hosts 12 three-stared restaurants, four of which are located in Minato. As such, Tokyo is a desirable market for the ultra-luxury residential sector, and it is unsurprising that the size of the market has been rapidly growing in recent years.

Additionally, this sector has been buttressed by growing interest from overseas investors. As explained in the appendix, Japan's resiliency and stable prospects are especially attractive during uncertain times. The explosive growth of inbound tourism prior to the pandemic has also increased the number of amenities in the country that appeal to overseas UHNWIs.

Although Tokyo's ultra-luxury residential market is considered relatively new, it is growing rapidly and has gained popularity over time. Indeed, some recent projects in this sector have proven successful, illustrating that substantial demand exists for the right products. Current developments in the pipeline will add new ultra-luxury units into the market and likely raise the top prices of the market to levels equivalent to those seen in Manhattan and London.

NEW DEVELOPMENTS

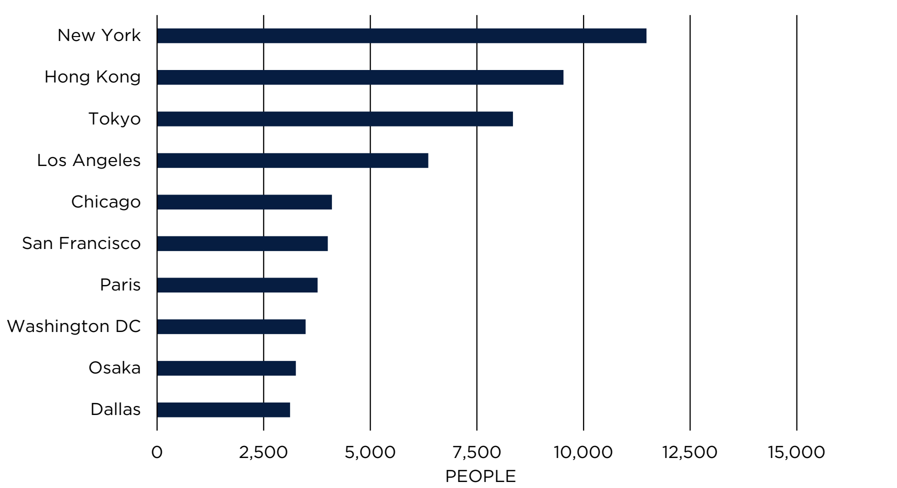
Tokyo has seen a few additions of luxury condominium towers in the past few years that can house ultra-luxury units, many of which are centred around Minato. The most recent one is Toranomon Hills Residential Tower, which opened in early 2022. This property is rumoured to house a unit priced well over JPY10 billion - the most expensive condominium unit in Japan.

In 2023, the highly anticipated Toranomon-Azabudai project is expected to further propel the growth of the ultra-luxury residential market in Minato with plans to introduce 1,400 residential units in its two main residential towers. Furthermore, the main 330-metre tower of the project will house 91 hotel-branded residences affiliated with Aman on its top floors. The most expensive unit is rumoured to be on the market for JPY20 billion - easily exceeding the most expensive unit recorded to date. Comprehensive developments like these have the necessary infrastructure and amenities prepared to ensure that high unit prices can be targeted. This small district appears to keep setting new records for Japan's most expensive residential unit.

Another project likely to house ultra-luxury units is the Mita 1-Chome project. The project will be developed by Mitsui Fudosan and Mitsubishi Estate and is expected to be completed in May 2025. The project will feature multiple buildings with over 1,000 residential units. Given the size of the development, the large players involved, and the prime location, it is likely that the development will feature ultra-luxury units, adding to Minato's stock and solidifying the ward's status as a premier residential area.

There are some developments outside of Minato as well. For instance, MARQ Omotesando One, which was developed by BPEA Real Estate, is in Shibuya and was completed in November 2021. However, while the site's proximity to Harajuku, Shibuya, and Omotesando can be attractive, the neighbourhood is not typically considered to be a luxury residential area. Additionally, in 2020, The Kita was also built near Kitasando, an area slightly north of Harajuku. The architect of the project is Kengo Kuma, who designed

GRAPH 2: Top 10 Cities by UHNWI Population, 2020



Source Wealth-X, Savills Research & Consultancy the Japan National Stadium for the Tokyo 2020 Olympics. By The Kita, Park Court Jingu Kitasando The Tower is also under construction and slated for completion in 2023.

Elsewhere, Mitsubishi Estate is reported to have acquired the negotiation rights to purchase a portion of the land occupied by the British Embassy in Tokyo and seems to be evaluating the possibility of building ultra-luxury condominiums on the site. Although the details have not been revealed, considering its prime location directly west of the imperial palace, the project could potentially see condominiums of very high calibre built on the site. Furthermore, while not technically a condominium, Mitsubishi Estate also plans to add about 50 rental residential units on some of the high floors in Torch Tower, which is expected to be the tallest building in Japan after its completion in 2027. The rents for the most expensive units are likely to be well over JPY5 million a month - comparable to other ultra-luxury residences.

Beyond the capital, Osaka has also seen some developments in the luxury sector. In 2024, Tokyo Tatemono and Hotel Properties Limited are expected to complete the One Dojima Project, which comprises the 466-unit Brillia Tower and the 178-room Four Seasons Hotel Osaka. The development site is proximate to Umeda and should benefit from the other redevelopment projects around the area.

BRANDED RESIDENCES

Branded residences are still new in Japan, but the concept is gaining popularity. The highly anticipated opening of Aman Residences Tokyo next year and many other mixed-use developments in the near future that are considered suitable to accommodate ultra-luxury residences have garnered a large amount of interest. Currently, a few examples can be found in Niseko and Kyoto.

For instance, LOFT Niseko, affiliated with YOO, opened in 2014 in Niseko as the first YOO project in Japan, and features four loft-style residential units. Additionally, Park Hyatt Niseko Hanazono Residences was completed in 2019 and comprises 113 residential units on a 24,000 sq m site in Niseko. Market rumours suggest that a studio of about 70 sq m was priced for about JPY150 million while a three-bedroom of about 150 sq m was priced for about JPY550 million. Furthermore, Aman Niseko is a wellness resort slated for opening in 2023, which will feature 31 detached residential units along with 30 hotel guestrooms. The property also features multiple restaurants, a spa, and facilities where residents can engage in nature-related activities.

On a separate note, overseas investors from regions such as Hong Kong, China, Australia, and Singapore have reportedly been especially active in acquiring properties in Hokkaido. They have remained active during the pandemic with the expectation tourists returning after the pandemic.

One example of a branded-residence development outside of Niseko is Four Seasons Kyoto, an exclusive property located in Higashiyama, Kyoto. The property opened in October 2016 and features 57 luxury residential units along with 123 hotel units, a spa, a gym, a pool, as well as a 10,000 sq m Japanese garden. As of March 2022, some units in this project appear to be listed for close to JPY30 million per tsubo.

As indicated in the examples above, branded residences in Japan were generally developed in areas that are considered tourist destinations. This is not surprising considering that potential buyers of these properties would already own primary homes, and these branded residences were mainly purchased as a place to spend their leisure time. However, the aforementioned Aman Residences Tokyo is likely to be a game changer as it will be the first urban branded residence property in the heart of Tokyo, and the project is rumoured to be getting a lot of attention. The success of Aman Residences Tokyo should spark further interest, leading to more developments of branded residences in central Tokyo.

END OF THE OFFICE-CENTRED SUPER STRUCTURE

Tokyo saw a surge of large-scale developments leading to the 2020 Tokyo Olympics, and will have more to come towards 2030. These large-scale, mixed-use projects will help the city's transformation, and introduce new landmarks and city amenities. However, the environment surrounding the real estate market has changed significantly in recent years, which may have made some adjustments to initial project plans necessary.

Many developers have been wary about the large wave of office supply in central Tokyo behind the scenes, especially on top of the declining population of Japan. However, the reality is that the accelerated urbanisation, and increments in the working population due to higher labour participation rates of female and elderly workers have helped to fill office space. On the other hand, the pandemic has changed the prospects of the office sector and the concerns by developers have become more serious. In the future, it might not be as easy to fill large floors at very high office rents.

Specifically, some office space planned for those developments in the pipeline could be excessive given the current market size and office trends. Therefore, some of that space may be replaced with other uses. For example, according to its original announcement, Torch Tower plans to offer about 60,000 of office space tsubo when completed in 2027. Considering that the total Grade A office stock in Chiyoda is currently about 1 million tsubo, this will be a sizable addition. The current workstyle shift toward hybrid or remote work also adds some risk to the future demand prospects for offices.

Given the above, replacing office space with other uses such as ultra-luxury condominiums appears to be an attractive and viable option, especially given the robust demand for luxury housing. Since the pandemic began, people have been spending more time at home, and consequently saving more to some extent. This lifestyle change has led to heightened housing demand particularly for high-end properties, overall resulting in asset prices rising on a global level. Japan is no exemption, although the impacts of the pandemic have been relatively milder.

Some ultra-luxury condominiums units have been sold for well more than JPY20 million per tsubo, suggesting that selling some floors as ultra-luxury condominiums makes financial sense. For instance, the portion of Kamiyacho Trust Tower sold to Mori Trust Sogo REIT was appraised at JPY15.6 billion as of September 2021, which is about JPY14 million on a per-tsubo basis. Although offices used to be considered less risky than ultra-luxury residences, if the ultra-luxury market continues to grow and mature, more developers are likely to start considering them as essential components of their projects. Furthermore, the ultra-luxury residential market will also help other relevant sectors that cater to UHNWIs, such as retail and hotels.

OUTLOOK

Overall, there is a growing amount of evidence that there is demand for ultra-luxury residences in Japan, and this has helped the ultra-luxury residential market grow at a rapid pace. Some of the large-scale mixed-use projects in the pipeline are expected to add more units in this category, which should expand the market size and push top prices even higher. While many of these developments are still concentrated in Minato, there are some examples outside of the ward. Going forward, the types of units on offer will also be more diverse, including low-rise properties and branded residences.

The world is gradually returning to normalcy, and international travel has been slowly resuming. While the reopening of international travel on a large scale still appears out of sight, luxury travel should come back much earlier. This timely resurgence in luxury travel should further fuel demand in the luxury sector and help Japan solidify its status as a luxury travel destination.

The high concentration of ultra-wealthy people in Tokyo and the stability of Japan's long-term prospects make it attractive to overseas buyers, and are factors that support the growth of this sector. Although Japan has its own issues such as an ageing population, they remain manageable overall. Japan's rich culture is another attractive attribute, and the growth of the luxury hotel market should serve as a tailwind for the ultra-luxury residential sector.

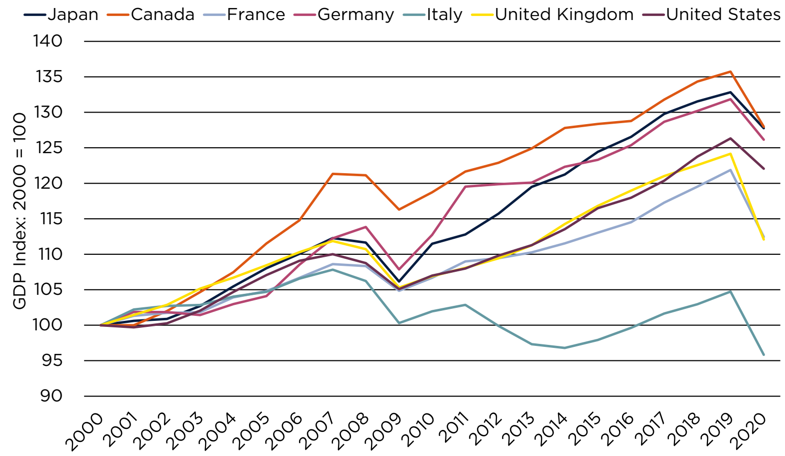
Nevertheless, this sector comes with significant challenges - the pool of potential buyers is very limited, and they are highly selective and particular about the services expected. Indeed, some new properties on the market appear to be struggling to find buyers. On the other hand, demand for exceptional properties is strong despite their high prices.

One crucial factor that will determine the success of an ultra-luxury property is its ability to provide expected quality service. Even within ultra-luxury residences, different levels of service will be required depending on the price level for the unit. The capability of management in catering the right level of service to different occupants while keeping costs under control will be essential, and it will take time to attain an optimal balance between the two.

Going forward, the market is likely to keep growing as Tokyo continues to transform through redevelopment. Presently, the two major developers leading the ultra-luxury sector are Mori Building and Mitsui Fudosan. However, as the market matures and a proof of concept has been established for the sector, the market should become more diverse with more players and products, eventually leading to Tokyo becoming an established market. Furthermore, as the world faces stiff headwinds of uncertainty, Tokyo might further gain popularity as a place to preserve wealth. In the long run, events such as the World Expo and the opening of the integrated resort may also help showcase the country's potential.

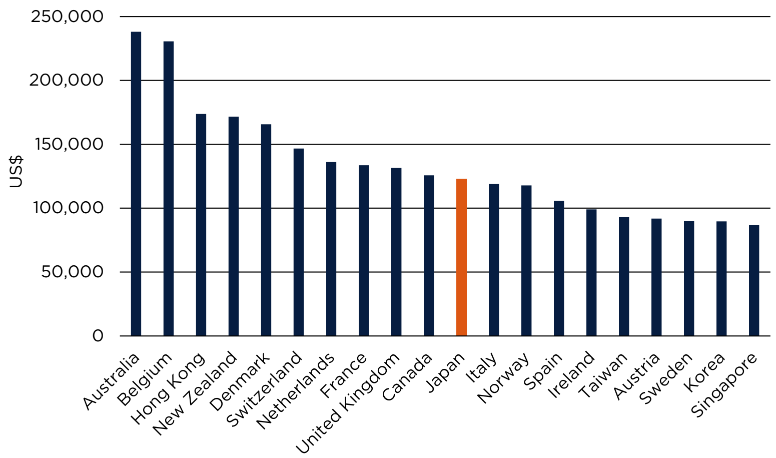
Appendix

GRAPH 3: GDP per Working Age Population, 2000 to 2020*



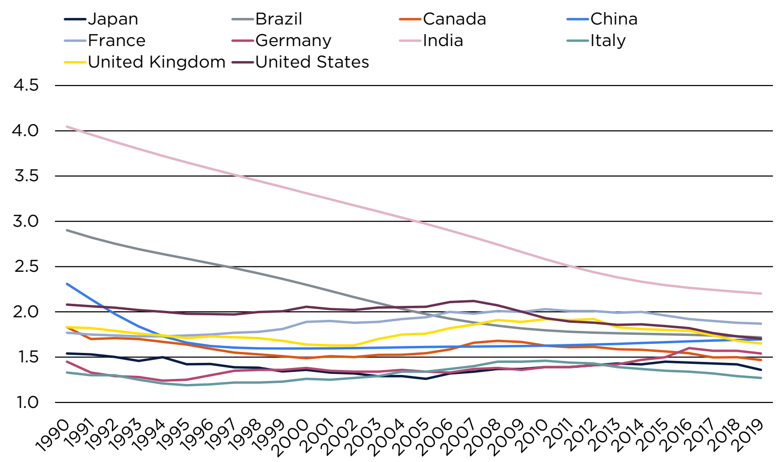
Source World Bank, Savills Research & Consultancy
*Using the data and provided by the World Bank as defined as follows: Dollar figures for GDP were converted from domestic currencies using 2015 official exchange rates before being indexed, and working age refers to those between 18-64 years old.

GRAPH 4: Median Wealth per Adult, 2020



Source Credit Suisse Global wealth report 2021, Savills Research & Consultancy

GRAPH 5: Fertility Rate of Select Major Economies, 1990 to 2019



Source World Bank, Savills Research & Consultancy

LONG TERM PROSPECTS OF JAPAN

Japan has gained undisputed popularity as a tourist destination. On the other hand, those considering the purchase of ultra-luxury properties may question the long-term prospects of its economy with the ageing and shrinking population. However, upon taking a closer look, Japan's economic performance and environment present it as a suitable place to store wealth.

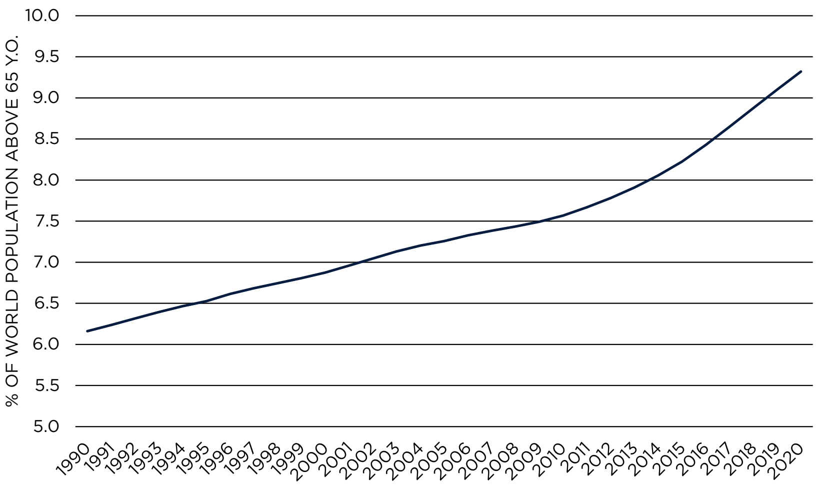
To begin, Japan is a developed country well known for its overall stability. Its citizens coexist with minimal political and social divisions, unlike many countries in the west. Indeed, Japan has enjoyed a steady inflow of foreign capital seeking stable investments in the real estate market due to the sense of stability it provides and the attractive funding options available.

Going forward, the global interest rate environment may have a significant impact on the mid-term prospects of the world, including Japan. The strong real estate market worldwide has been supported by the low interest rates maintained by central banks across the globe. Presently, central banks are worried about historically high inflation rates, which is likely to trigger continuous interest rate hikes.

However, looking at world demographic trends, many countries, even China and India, are or will soon be characterized by an ageing population and a subsequently declining population. This ageing population trend has caused savings to rise, and consequentially an increase in investment volumes from pension managers. Overall, many major economies around the world are likely to increase their record-low interest rates to prevent overheating in the market and counter inflation. However, these increments are expected to be mild because of saving glut stemming from the ageing demographic across the globe.

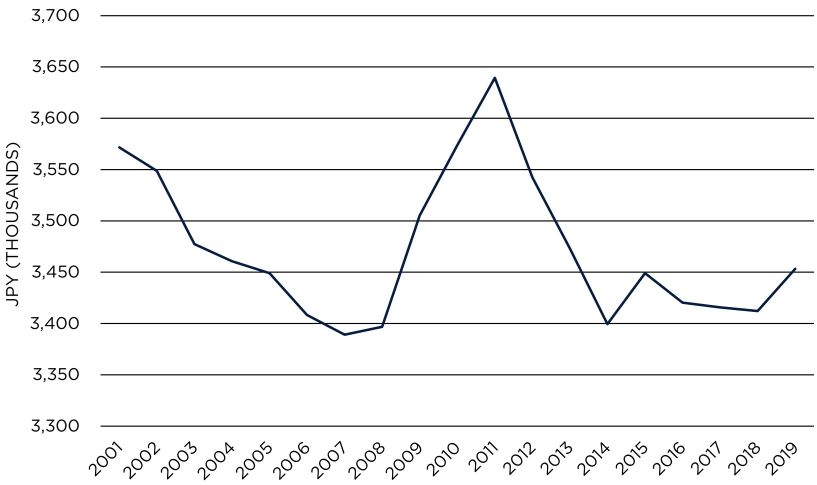
When considering Japan's prospects, the country's ageing population is admittedly a problem, and causes worry for its economic outlook. On the other hand, Japan's GDP growth per working age population has fared better than most of the other G7 nations over the last two decades. This suggests that the economy has been performing well overall, although negative impacts from the ageing population have a lingering effect. Furthermore, it should be noted that Japan's spending on social benefits per elderly person has decreased over the past decade. Indeed, spending on pensions were reduced due to reforms made to the national pension law in 2012.

GRAPH 6: Percentage of World Population Above 65 Years of Age, 1990 to 2020



Source World Bank, Savills Research & Consultancy

GRAPH 7: Social Benefit per Elderly Person in Japan*, FY2001 to FY2019



Source Ministry of Health, Labour and Welfare, Ministry of Internal Affairs and Communications, Savills Research & Consultancy
*Defined as older than 65 years of age.

Japan has also made additional plans like decreasing spending on medical insurance and increasing the retirement age to make spending practices more sustainable in the long term. From 2022, for example, elderly individuals above the age of 75 that meet a minimum income threshold have to bear 20% of medical costs, up from 10%. While there should be challenges going forward, Japan seems to be reasonably prepared for them. Indeed, at over US$120,000, the median amount of wealth per adult in Japan is high, meaning that the country and many of its citizens should be able to brace themselves for tougher times ahead.

Overall, Japan has many pull-factors as world-class tourist destination with a sustainable economic base. Therefore, the country appears suitable as a place for ultra-high net worth individuals to store wealth.

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