
Mizuho Economic Outlook & Analysis

February 8, 2019

Will condominium prices in the Tokyo metropolitan area fall sharply?

< Summary >

- ◆ In 2018, new condominium prices in the Tokyo metropolitan area fell for the first time in six years. Since this was due mainly to the increase in supply in the Chiba and Saitama prefectures against a backdrop of difficulties in the acquisition of land in the Tokyo wards (“ku” area), the fall of condominium prices in the Tokyo metropolitan area does not necessarily mean property prices in Tokyo wards are collapsing.
- ◆ Based upon housing starts, prices are projected to fall along with the contraction of the supply of high-priced condominiums in Tokyo wards. However, considering factors such as a near oligopoly with respect to suppliers, the odds are low that prices will drop sharply.
- ◆ The risks to the condominium market are a downturn in the domestic economy and sharp appreciation of the yen triggered by the slowdown of the overseas economies and/or destabilization of the financial markets. A reversal of overseas fund flows may serve as a negative impact upon the condominium market.

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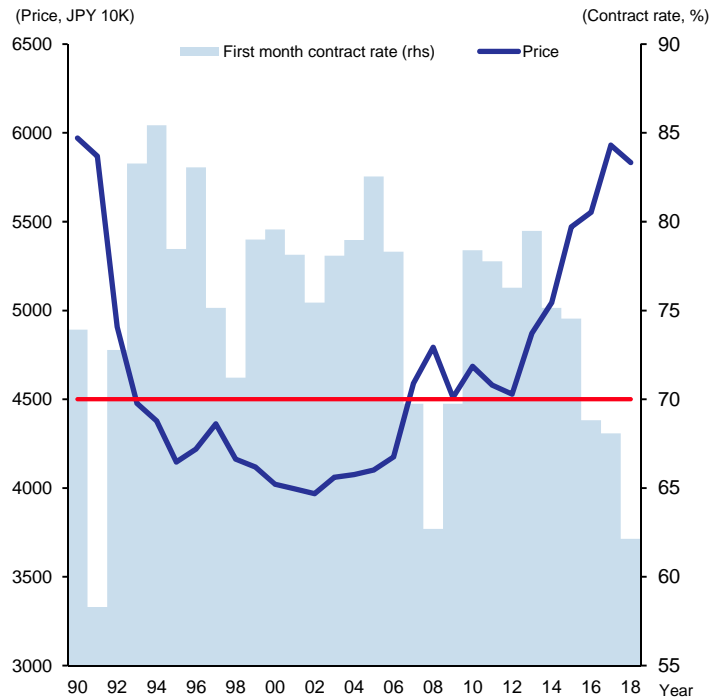
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1. As the average price of new condominiums in the Tokyo metropolitan area declined in 2018 for the first time in six years, concerns about the future are growing

There are signs of change in the average price of new condominiums in the Tokyo metropolitan area (**Chart 1**). Since the start of Abenomics in 2013, the price of new condominiums in the metropolitan area has risen sharply, reaching in 2017 the highest point since Japan's bubble economy. However, in 2018 prices fell below the previous year for the first time in six years, and the first month contract rate (the contract rate in the first month after the condominium goes up for sale), an important market indicator, fell to the lowest level in 27 years. In response to this, there

Chart 1: New condominium average prices in metropolitan areas & first month contract rate



Note: The red line highlights the first month contract rate of 70%, the threshold between favorable and unfavorable market conditions.
 Source: Made by Mizuho Research Institute Ltd. (MHR) based upon Real Estate Economic Institute Co., LTD, *Shutoken kinkiken no manshon shijo doko (Property market trends in the Tokyo and Osaka metropolitan areas)*, in Japanese only.

are rumors of a crisis that "condominium prices in metropolitan areas will finally crash".

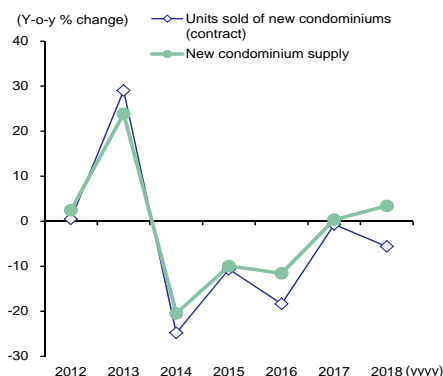
We have thus far held that condominium prices have continued to rise despite the decline of the contract rate because of the improvement of the income environment due to economic expansion and the low interest rate environment stemming from massive monetary easing, in addition to (1) the fact that condominium developers have little incentive to lower prices due to the rise of construction costs on the supply side, and (2) that dual-income households are emerging as the main buyers and are underpinning demand for high-priced condominiums on the demand side. In this report, we take another look at the newly-built condominium market of Tokyo metropolitan area in 2018 to see whether there are signs of deterioration finally appearing in the condominium market and whether there is the possibility of a rumored crisis.

2. The main reason for the decline in the 2018 average price is the increase in supply of low-priced condominiums

First, we shall consider the factors behind the fall in average prices of new condominiums in 2018. To understand supply and demand trends, **Chart 2** shows the growth in new condominium supply (supply) and the number of units sold (demand). Since 2013, sales of new condominiums have been sluggish, but a contraction of supply prevented the supply-demand balance from collapsing. In other words, the rise in condominium prices was caused by factors other than the supply-demand factor. In fact, during this time, demand has shifted to highly convenient high-priced condominiums, mainly in the wards of Tokyo, due to an increase in dual-income households. As a result, the supply share of low-priced properties declined and condominium prices surged.

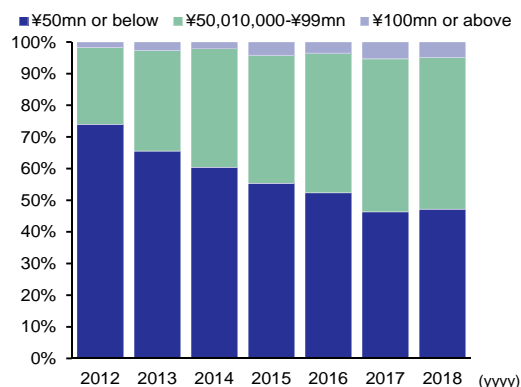
However, while the number of units sold continued to decline for the fifth consecutive year in 2018, new condominium supply increased for the second consecutive year. The contrasting result is that the growth rate also increased from the previous year. In other words, there was a change in supply. To understand this change, **Chart 3** shows the trends in the number of new condominium units put on sale in the Tokyo metropolitan area by price range. The chart shows that in 2018 the number of properties priced below 50 million yen increased for the first time in five years, and as a result it can be seen that the share of the properties priced at 50 million yen or below rose for the first time in six years. In other words, the increase in the supply of low-priced properties served to depress the average price.

Chart 2: Growth in stock of Tokyo metropolitan condominiums and units sold



Source: Made by MHRI based upon Real Estate Economic Institute Co., LTD, *Shutoken kinkiken no manshon shijo doko (Property market trends in the Tokyo and Osaka metropolitan areas)*, in Japanese only.

Chart 3: Tokyo metropolitan condominium sales stock by price range



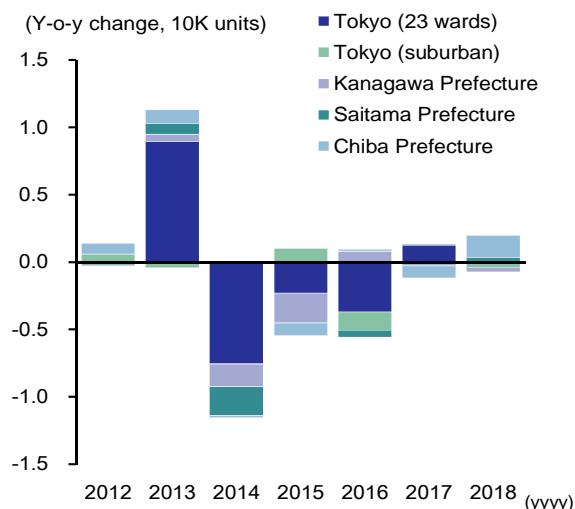
Source: Made by MHRI based upon Real Estate Economic Institute Co., LTD, *Shutoken kinkiken no manshon shijo doko (Property market trends in the Tokyo and Osaka metropolitan areas)*, in Japanese only.

3. The increase in supply of low-priced condominiums stems from the difficulty in land acquisitions in Tokyo

What is in the background of developers increasing the supply of low-priced condominiums on the supply-side of the condominium market? To shed light upon this phenomenon, **Chart 4** shows the number of condominiums supplied in the Tokyo metropolitan area. As revealed by the chart, while the supply of condominiums in the wards of Tokyo declined for the first time in two years in 2018, the number of units sold rose sharply in Chiba Prefecture, and also increased in Saitama Prefecture. The prefectures of Chiba and Saitama, compared with Tokyo and Kanagawa Prefecture, have a large supply of low-priced condominiums; in fact, in 2018 these two prefectures had nearly 80% of properties priced at 50 million yen or less (**Chart 5**). In short, as developers increased the number of units put on the market in the Chiba and Saitama prefectures, the price in terms of the average price of condominiums in the overall Tokyo metropolitan area fell. Incidentally, as the average price of condominiums in the wards of Tokyo (71.42 million yen) rose for two years in a row (2016: 66.29 million yen; 2017 year: 70.89 million yen), this indicates that the condominium market in the wards of Tokyo has not yet started to fall sharply.

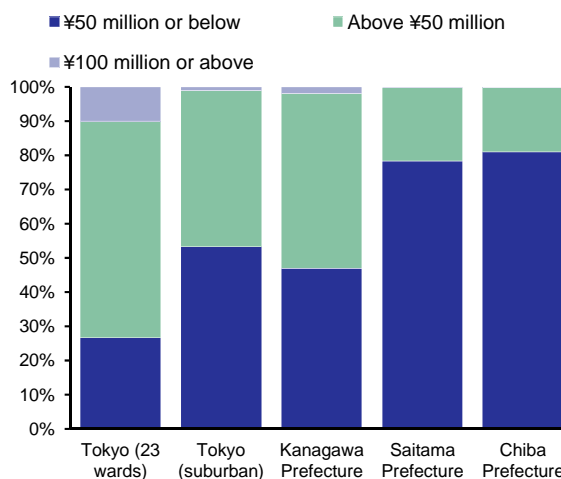
So, why has the supply of the number of condominiums in Chiba Prefecture and Saitama Prefecture increased? One reason is that land acquisition in Tokyo has become difficult. Following the decision in 2013 to have Tokyo host the Olympic Games, construction work has increased greatly in Tokyo compared with other regions (see Miyajima (2018)), causing a tightening of the supply-demand balance for land for construction. In particular, as inbound tourism demand has increased, the number of new hotel openings, mainly business hotels, is increasing (see Miyajima, Hirayoshi (2018)), and construction sites are not easy to acquire as hotels and condominiums compete against each other. As a result, residential land prices in Tokyo's wards have risen sharply compared to other regions, and are close to the high prices during the so-called “mini bubble period” from 2007 to 2008 (**Chart 6**). Based on this, developers have increased the sale of less expensive condominiums, relative to Tokyo ward prices, in Chiba and Saitama prefectures, apparently with the aim of increasing sales to those who prefer lower-priced properties.

Chart 4: Tokyo metropolitan area condominium stock by region



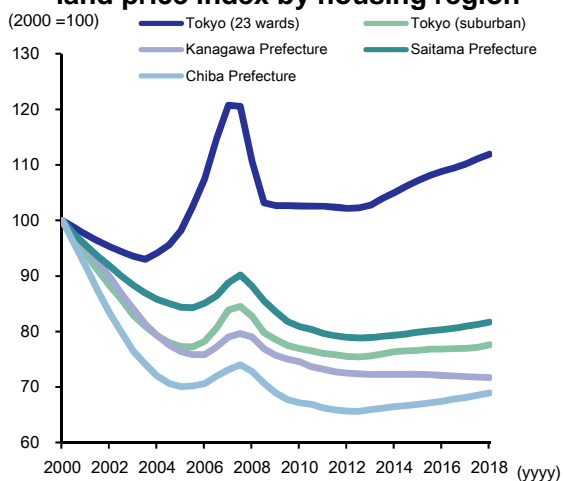
Source: Made by MHRI based upon Real Estate Economic Institute Co., LTD, *Shutoken kinkiken no manshon shijo doko (Property market trends in the Tokyo and Osaka metropolitan areas)*, in Japanese only.

Chart 5: Tokyo metropolitan area condominium average price by region (2018)



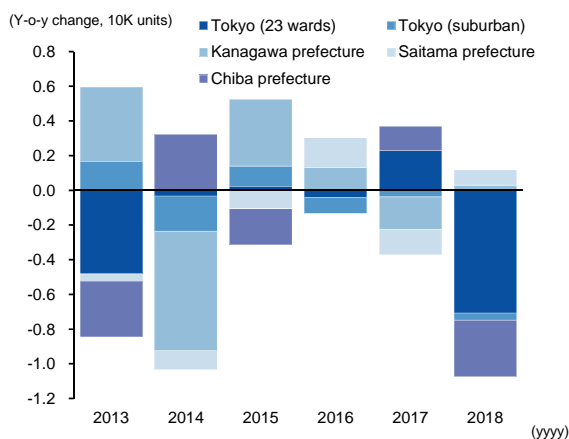
Source: Made by MHRI based upon Real Estate Economic Institute Co., LTD, *Shutoken kinkiken no manshon shijo doko (Property market trends in the Tokyo and Osaka metropolitan areas)*, in Japanese only.

Chart 6: Tokyo metropolitan area urban land price index by housing region



Source: Made by MHRI based upon Japan Real Estate Institute, *Shigaichikakakushisu, zenkoku mokuzokenchikuhishisu (Urban land price index & nationwide wooden frame house construction cost index)*, in Japanese only.

Chart 7: Tokyo metropolitan area condominium housing starts by region



Source: Made by MHRI based upon Ministry of Land, Infrastructure, Transport and Tourism, *Housing Starts*

4. Average price of condominiums in the Tokyo metropolitan area is not expected to fall sharply, and should follow a gradual decline

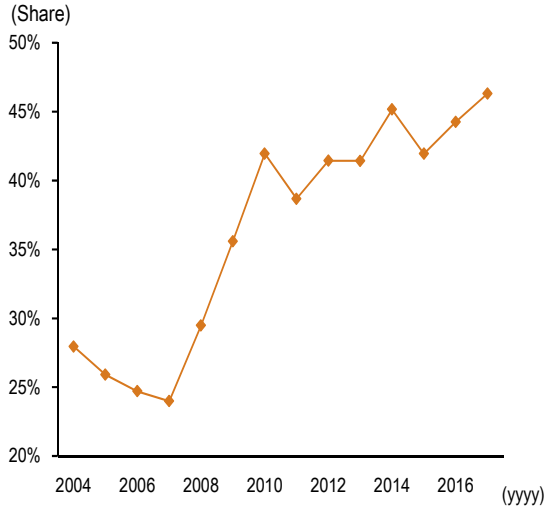
Looking ahead, the number of condominium housing starts in the Tokyo metropolitan area, a leading market indicator (**Chart 7**), fell sharply in 2018. Due to restrictions on land acquisition and other factors, a brisk rise in supply of high-priced condominiums in the wards of Tokyo is unlikely in the future. As a result, the average price of condominiums in the Tokyo metropolitan area will likely decline as the supply of low-priced property increases in regions where land acquisition is relatively easy, such as Saitama Prefecture. If the economy accelerates sharply or if monetary policy turns accommodative, demand may increase and prices may rise again, but the possibility is small at the present time.

Even so, a sharp decline of condominium prices in the Tokyo metropolitan area is also unlikely. Turning again to the number of housing starts in the Tokyo metropolitan area (**Chart 7**), Chiba Prefecture posted a sharp decline in 2018 in a backlash to the construction of large-sized buildings in the previous year. Although housing starts in Saitama Prefecture increased, the supply of low-priced condominiums is unlikely to increase as much as in 2018, considering the fall of housing starts in Chiba Prefecture.

In addition, the fact that condominium developers on the supply side are not yet ready to cut prices is also a factor that makes it difficult for condominium prices to fall (see Sato (2017)). Moreover, the construction cost deflator (Ministry of Land, Infrastructure, Transport and Tourism, *Construction Cost Deflators*) has remained at a high level. Currently, there is little room to significantly lower the selling price of condominiums, largely due to the rise of construction costs, consisting mainly of labor costs.

Furthermore, a look at the earnings of large real estate companies reveals that forecasts for current profits (Bank of Japan, *Short-Term Economic Survey of Enterprises in Japan (Tankan)*) are steady, meaning that there is no need for major developers to seek quick returns on investment by cutting into profits through the reduction of condominium prices. Currently, in the Tokyo metropolitan condominium market, the share of supply of condominiums of the so-called "Major Seven" real estate developers has climbed to about 50% (**Chart 8**). As the state of the market has become more oligopolistic than in the mini bubble period, the market structure makes a price collapse due to oversupply less likely.

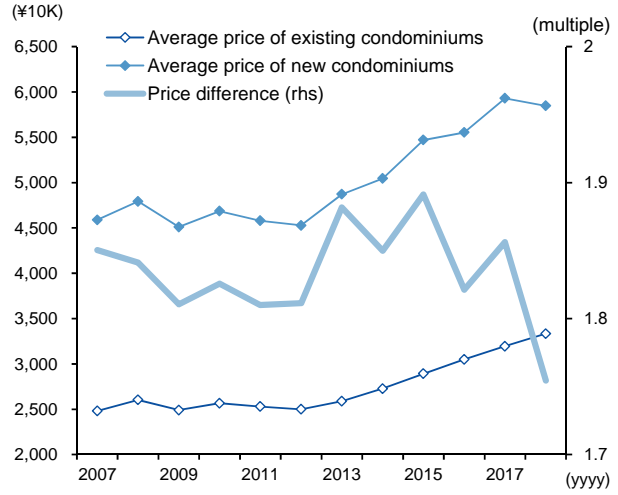
Chart 8: Share of condominium units supplied by the "Major Seven" in the Tokyo metropolitan area



Note: The "Major Seven" refers to Sumitomo Real Estate Co., Ltd., Daikyo Incorporated, Tokyu Land Corporation, Tokyo Tatemono Co., Ltd., Nomura Real Estate Co., Ltd., Mitsui Fudosan Residential Co., Ltd., Mitsubishi Estate Residence Co., Ltd.

Source: Made by MHRI based on the web page of the "Major Seven."

Chart 9: Price difference between new and existing condominiums in the Tokyo metropolitan area



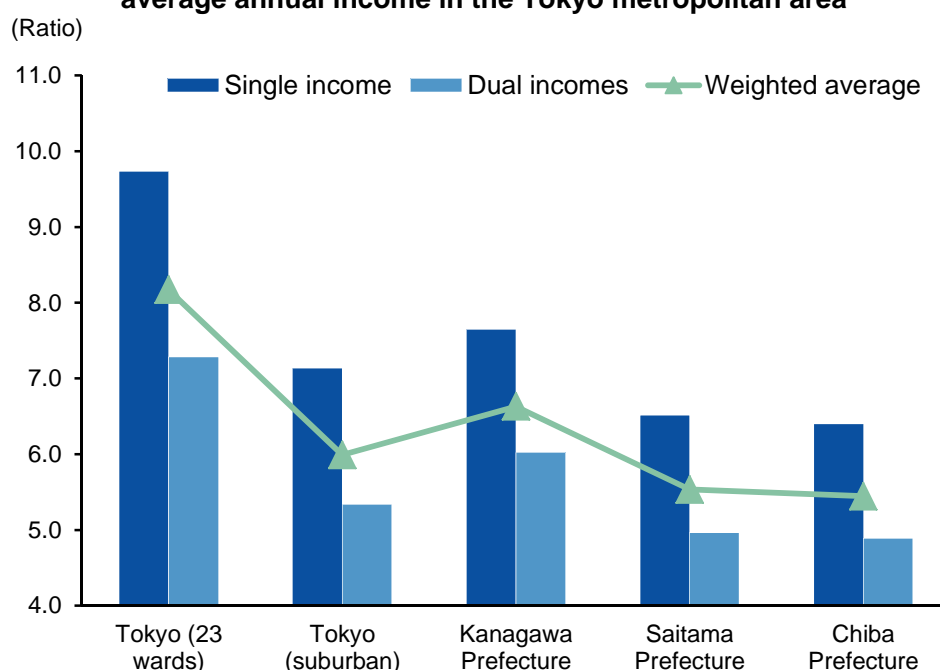
Source: Made by MHRI based upon Real Estate Economic Institute Co., LTD, *Shutoken kinkiken no manshon shijo doko (Property market trends in the Tokyo and Osaka metropolitan areas)*, in Japanese only, Real Estate Information Network for East Japan, *Shutoken fudosan ryutsushijo no doko (Tokyo metropolitan area real estate market trends)*, in Japanese only.

Let us shift the perspective to the demand side. In recent years, demand has shifted to relatively inexpensive existing condominiums due to a squeeze in the supply of new condominiums and rise of prices. However, prices for new condominiums also declined in 2018, further narrowing the price gap with existing units (**Chart 9**). Given that prices of existing condominiums are well above the mini bubble period, the chances are remote that demand for existing condominiums will rise sharply in the future.

Also, as pointed out by Hirayoshi and Miyajima (2018), due to the fact that power couples and other dual-income households are the main purchasers of condominiums, current condominium prices are not necessarily so high that they are beyond reach. **Chart 10** is a calculation of the ratio of new condominium prices to average annual household income. Since the chart shows that the price of condominiums in the wards of Tokyo is nearly 10 times the annual income of single-income households, this may be a plausible reason for these households being cautious about purchases. However, since the ratio in the case of the annual income of dual-income households is about seven times, the price is not so high as to rule out purchases. The weighted average with respect to the proportion of households with dual incomes purchasing condominiums is about eight times. Given the current low level of interest rates, condominium prices in the wards of

Tokyo would be within reach of power couples. Due to the increase in such dual-income households and low interest rates, the number of such households within reach of high-priced condominiums is increasing, providing reasons to believe that demand for highly convenient properties such as those near train stations will remain strong. This is why we believe that developers do not need to immediately come up with a supply strategy that will significantly lower prices. Based upon such perspective, we are inclined toward the view that condominium prices in the Tokyo metropolitan area will gradually decline, reflecting the fall in ratio of high-priced properties, rather than fall sharply.

Chart 10: Ratio of the average price of newly built condominiums (2018) to household average annual income in the Tokyo metropolitan area



Note: 1. The average annual income of Tokyo is used for Tokyo wards and suburban areas.
 2. Household annual income is based on the 2014 *National Survey of Family Income and Expenditure* values for each prefecture adjusted by the growth rate in the *Family Income and Expenditure Survey* (the growth rate for 2014 compared to 2017).
 3. The ratio of purchasing households with dual incomes is based on survey results (2017) provided by the Recruit Sumai Company.
 4. Due to the constraints of statistical data it is necessary to take a considerable range of results.
 Source: Made by MHRI based upon Ministry of Internal Affairs and Communications, *National Survey of Family Income and Expenditure*, *Family Income and Expenditure Survey*, Recruit Sumai Company Ltd., *2017nen Shutoken shinchiku manshon keiyakusha dokochosa (2017 Survey on contract trends of new condominium units in the Tokyo metropolitan area)* in Japanese only, Real Estate Economic Institute Co., LTD, *Shutoken kinkiken no manshon shijo doko (Property market trends in the Tokyo and Osaka metropolitan areas)*, in Japanese only.

5. Keep a close eye upon the negative risk of the overseas economic slowdown spreading to the condominium market

However, the risk is that the slowdown of overseas economies will have a negative effect on the condominium market.

Given that China's economic indicators released from the end of 2018 to the

beginning of 2019 show clear signs of an economic slowdown and that the US is likely to temporarily suffer adverse effects from the longest government shutdown in US history, the slowdown of overseas economic growth may intensify. In the event of a worse-than-expected slowdown of the US and China economies, the Japanese economy may also be subject to downward pressures upon exports and production. If clouds spread over the prospects of improvement in the income environment and consumer confidence, it may serve to suppress demand for condominiums and send downward pressures on prices.

Furthermore, there are concerns that the rise of uncertainties regarding the future will lead to the destabilization of the financial market, and serve to intensify the appreciation of the yen and downward pressures upon the stock market. Since condominium prices in Japan have been considered comparatively cheaper than major cities overseas, purchases of high-priced condominiums by foreign investors also served to support the price of new condominiums. In particular, Japanese condominium prices are relatively cheaper than those in locations such as Singapore, Hong Kong, Shanghai, Taipei. Along with environmental factors, Japanese condominiums were said to be attractive to Asian investors. In the event of a sharp appreciation of the yen, the reversal of the flow of funds from Asian investors could lead to the stagnation of the condominium market.

Refer to the original Japanese report by clicking the URL below for the reference material

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