Intelligent Investment

Reading the Japan Office Market: The Neutral Vacancy Rate Explained

VIEWPOINT

NEUTRAL VACANCY RATES IN JAPAN VARY BY CITY, WITH VACANCY RATE MOVEMENTS AGAINST THIS BASELINE AFFECTING FUTURE RENTAL PERFORMANCE. VACANCY RATES ARE PROJECTED TO REMAIN BELOW NEUTRAL VACANCY RATES IN ALL CITIES, LEADING TO RISING RENTS.

CBRE RESEARCH
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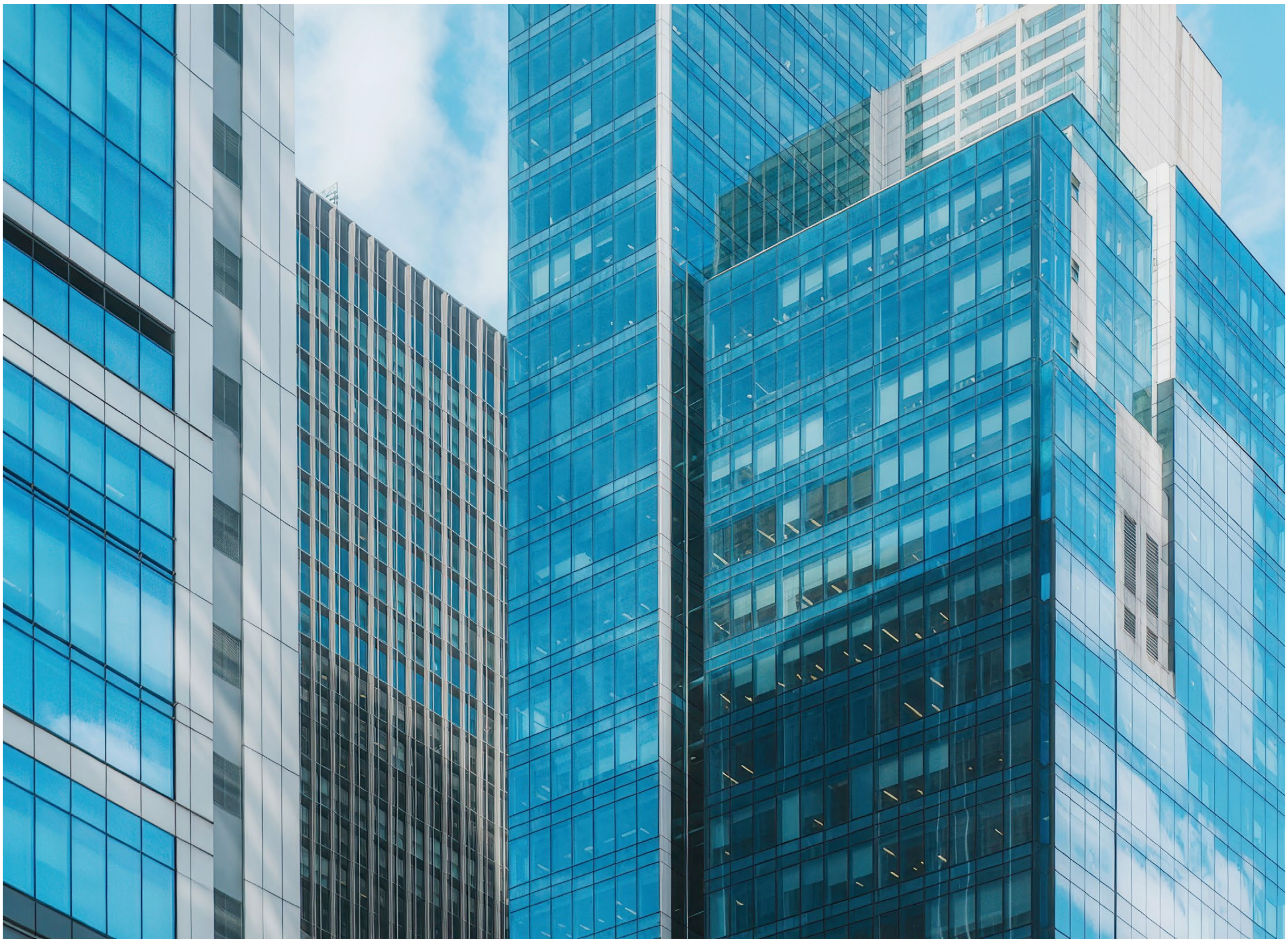


Summary

As of Q1 2026, vacancy rates vary widely throughout Japan, ranging from as low as 1.2% to as high as 12.1%. With rents continuing to trend generally upward, this suggests that the vacancy rate level that divides a market with falling rents from one with rising rents (the "neutral vacancy rate") differs from city to city. CBRE's use of historical data to calculate neutral vacancy rates for each city reveals a wide disparity, with Tokyo generally falling within the 4-6% bracket. Vacancy rates are projected to remain below the neutral vacancy rate among all cities, leading CBRE to predict that rents will continue to rise across all markets.

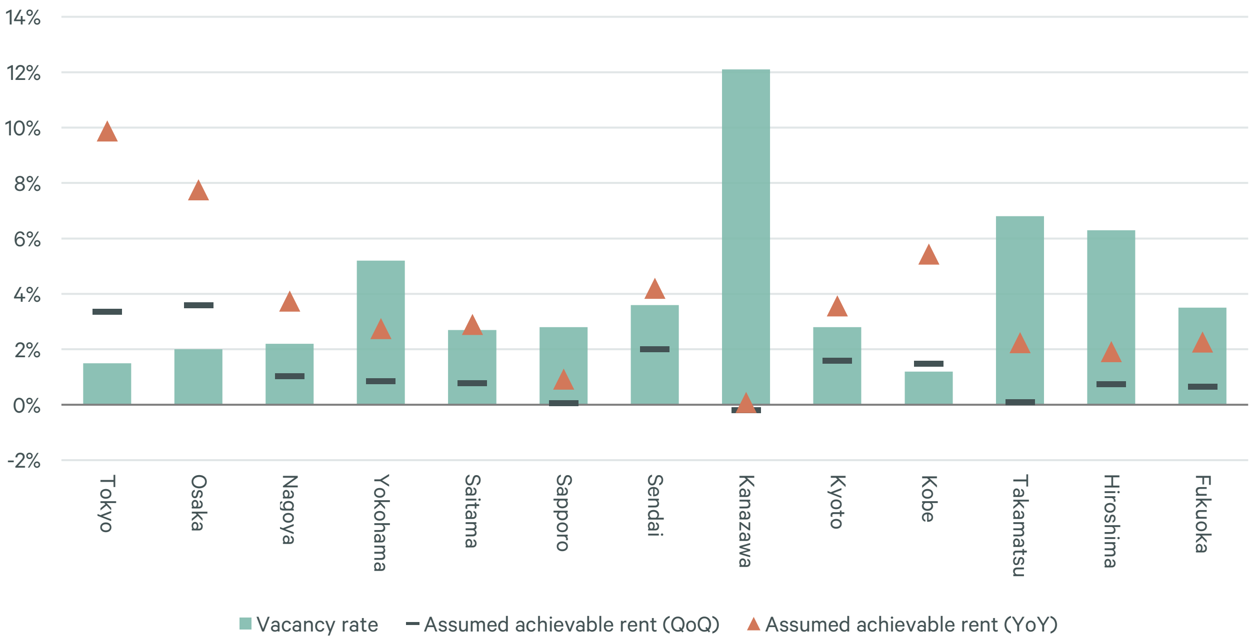
1. Rents continue to rise in all cities even as vacancy rates vary widely

Assumed achieved rents (hereafter referred to as rents) for Q1 2026 recorded q-o-q increases in all cities (other than Kanazawa which registered a marginal q-o-q decrease) and rose y-o-y in all cities nationwide (Figure 1). Vacancy rates ranged from 1.2% to 12.1% (1.2% to 6.8% if Kanazawa is excluded from the data).

Rental growth can be easily explained for cities with tight supply and demand balances and low vacancy rates of below 5%. However, there are also cities such as Yokohama, Takamatsu, and Hiroshima, where vacancy rates exceed 5%, but rents have indicated an upward trend, recording both q-o-q and y-o-y increases. Even in Kanazawa, where the vacancy rate stood at 12.1% in Q1 2026, well above those of other cities, rents have not entered a downward cycle.

This suggests that the vacancy level that determines whether a city's rents increase or decrease differs from city to city. This report uses the term "neutral vacancy rate" to refer to the vacancy rate level watershed or tipping point for each city, at which rents will neither rise nor fall.

Figure 1: Vacancy Rates and Rates of Change of Assumed Achieved Rents by City (Q1 2026)



Note: *All-Grade (featuring a total floor area of in excess of 1,000 tsubo and conforming to the latest earthquake resistance standards)
Source: CBRE, Q1 2026.

2. Neutral vacancy rates differ by city

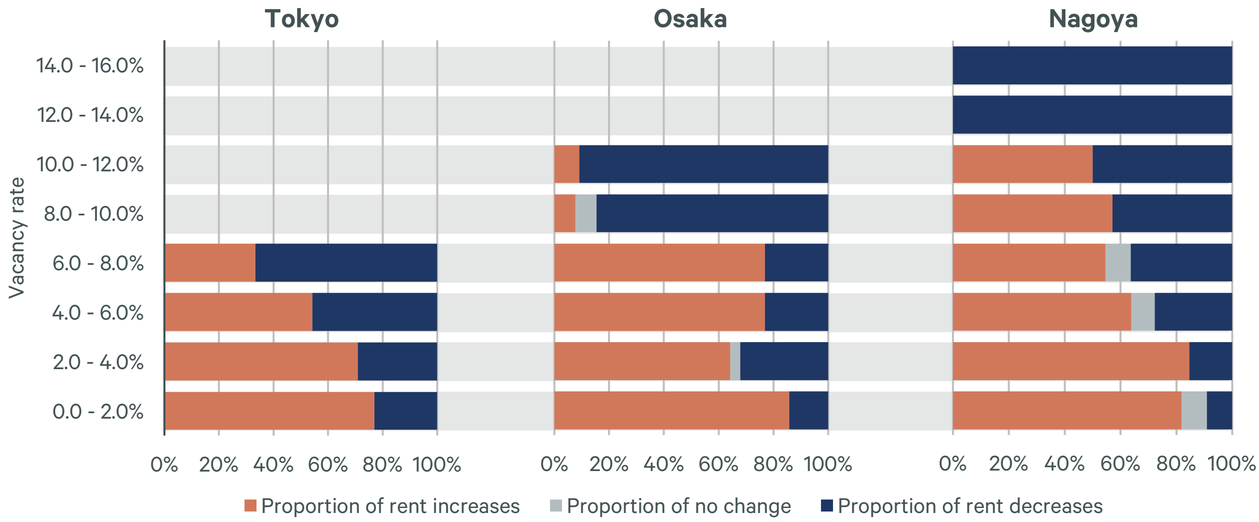
To calculate each city's neutral vacancy rate, CBRE firstly tabulated vacancy rate and rent data for each city over the past 80 quarters to ascertain the relationship between the two parameters over time. Figure 2 shows the instances in which rents rose, fell, or remained unchanged for each vacancy rate bracket in the three major metropolitan areas of Tokyo, Osaka, and Nagoya.

The data underscores the fundamental tenet that lower vacancy rates generally lead to rent increases, and vice versa. The other noteworthy feature is that the specific vacancy rate at which rent increases were more common than rent decreases differed by city. For Tokyo, vacancy rates below 6% triggered rent increases more often than decreases, while the equivalent figures for Osaka and Nagoya were below 8% and below 10%, respectively. However, in order to definitively determine that rents are more likely to increase than decrease, ratios between 50% and 60% are insufficient as they represent an area of uncertainty in which increases and decreases are almost equally common.

CBRE has therefore set the threshold at 60%, meaning that vacancy rates at this level trigger rent increases at least 60% of the time. For Tokyo, this means that a vacancy rate below 4% is likely to result in rent increases, while a vacancy rate above 6% is likely to result in rent decreases. The band between these two figures of 4% and 6% is where rent increases and decreases are of similar probabilities, and therefore where supply and demand are balanced (the neutral vacancy rate). For Osaka, the neutral vacancy rate is 8%, while for Nagoya it is in the bracket between 6 and 12%.

In addition to current vacancy rates, different cities have varying sensitivity to future movements in the vacancy rate. In Tokyo, even vacancy rates below 2% only result in rent increases 77% of the time, with rent decreases recorded the remaining 23% of the time. Periods in which rents fell despite vacancy rates of below 2% were times in which there was a high probability of vacancy rates entering a rising phase, such as the period of financial instability beginning around Q4 2007 triggered by the subprime mortgage crisis, or the start of the COVID-19 pandemic in Q2 2020 and onward. This suggests that Tokyo is especially sensitive to future movements in vacancy rates.

Figure 2: Vacancy Rates and Probabilities of Rent Increases/Decreases (Q2 2003 - Q1 2026; three major cities)



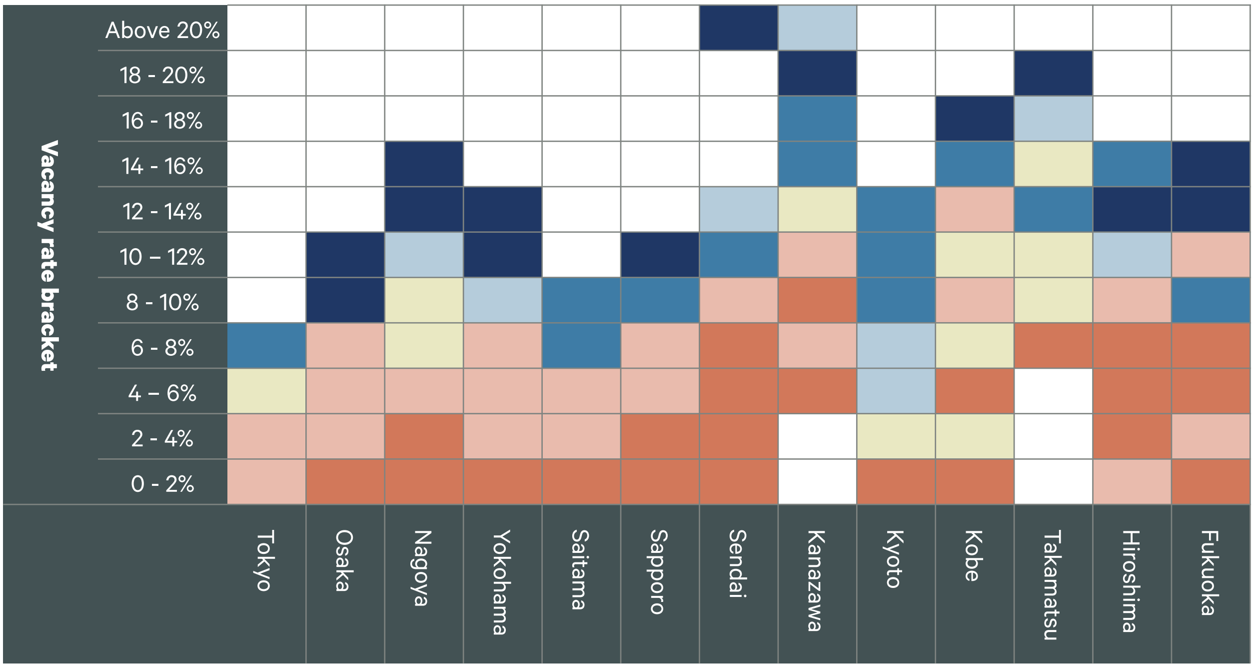
Note: Study sample consists of the period from Q2 2003 to Q1 2026. For each vacancy rate bracket with a sample of at least three instances, the number of cases in which rents rose, the number in which rents fell, and the number in which rents remained unchanged were counted, and a probability was calculated.
Source: CBRE, Q1 2026.

Figure 3 shows the relationship between vacancy rates and rents for the other major cities in Japan, calculated using the same methodology. Warm colors indicate higher probabilities of rent increases and cooler colors indicate higher probabilities of rent decreases. Each cell indicates the proportion of rent increases or decreases for that vacancy bracket. The more vivid the color, the higher the probability of either a rent increase or decrease. Less vivid colors represent lower probabilities of either increases or decreases, indicating where the balance between supply and demand is reached (the neutral vacancy rate).

Data for Kanazawa show this market has tended to have a higher vacancy rate than other cities, with the lowest rate ever recorded there being 4.5% in Q3 2020. Despite this relatively high average vacancy rate, the supply-demand balance in the city has not been consistently weak and is therefore not the cause of falling rents. Once the city's vacancy rate falls below 12%, rent increases become more likely, while a vacancy rate above 14% is likely to result in rent decreases. The neutral vacancy rate for Kanazawa therefore lies in the 12-14% bracket. The most recent vacancy rate recorded in Kanazawa was 12.1%, which lies within this range. As shown in Figure 1, rents in the city have remained relatively unchanged, as predicted by CBRE's model.

The table shows that the watershed dividing rent increases from rent decreases differs by city, making it inappropriate to determine the state of the supply-demand balance according to a universal vacancy rate standard. There are also several markets which, like Tokyo, are particularly sensitive to future movements in vacancy. Assessing future movements in rents therefore must consider both each city's specific neutral vacancy rate as well as future trends in the vacancy rate.

Figure 3: Vacancy Rates and Probabilities of Rent Increases/Decreases (Q2 2003 to Q1 2026)



	Higher probability of rent increases			Sample size: Fewer than three instances	Higher probability of rent decreases			
Rent increase probability	Above 80%	60 – 80%	Below 60%	-	Below 60%	60 – 80%	Above 80%	Rent decrease probability

Note: The study sample begins in Q2 2005 for Yokohama and in Q2 2003 for all other cities. For each vacancy rate bracket with a sample of at least three instances, the number of cases in which rents rose, the number in which rents fell, and the number in which rents remained unchanged were counted, and a probability calculated. Unshaded cells represent vacancy rate brackets with fewer than three samples.
Source: CBRE, Q1 2026.

3. Vacancy rates forecasted to decline or remain at low levels

CBRE's vacancy rate projections through to the end of 2028 are displayed in Figure 4. Changes in net lettable area are expressed as an index against the current Q1 2026 level (set at 100) to illustrate the impact of new supply, which will, in turn, affect future vacancy rates.

Sapporo is projected to witness the most significant increase in market size between now and the end of 2028, expanding by 12.2% from current levels. Fukuoka is expected to follow with 9.7%, then Yokohama with 6.2%. However, any spikes in vacancy caused by the completion of new supply in these cities are expected to be relatively subdued.

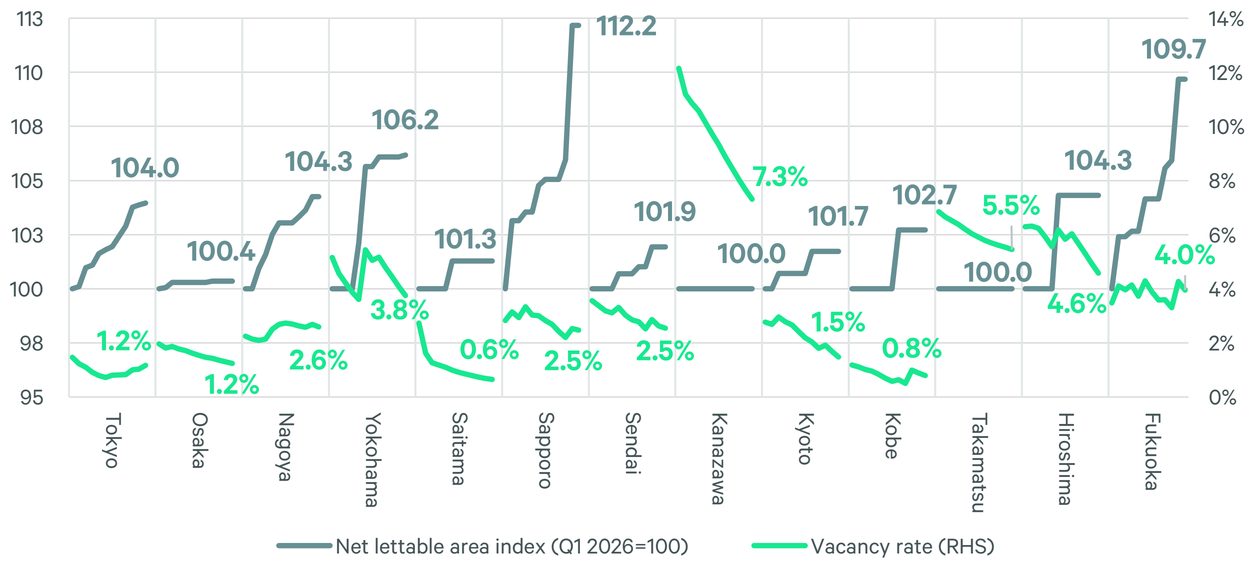
There are several reasons why CBRE anticipates only moderate increases in the vacancy rate. The Sapporo market has expanded by only 4.9% between Q1 2020 and Q1 2026 (compared with a nationwide average of 12.8% over the same period). With this market having not undergone the same level of growth as other cities, vacancies are insufficient to fulfill current demand. In addition, the upcoming simultaneous completion of several high-quality buildings with direct access to the city's underground walkway networks should stimulate new demand.

In contrast, Fukuoka's market size has expanded by a significant 32.4% since Q1 2020, with future supply anticipated to remain consistent with previous levels. Owing to the reasonable range of relocation options available, lease contracts are likely to be signed for new properties after completion. However, the emergence of a cycle of relocations triggered by ongoing redevelopment is likely ensure that demand remains robust. Although the vacancy rate is expected to remain largely stable until the end of 2028, it is likely to decrease in 2029 due to sustained strong demand for relocations and a subsequent decline in new supply.

In Yokohama, one upcoming large-scale redevelopment project has already leased out the majority of its floor space to a Tokyo-based company for use as a temporary office. This means that the vacancy rate is not expected to rise significantly following the addition of new supply.

Solid demand is expected to be witnessed in other cities as well, as companies seek to move to larger or higher-grade buildings in better locations, on the back of strong corporate earnings and an increased focus on staff recruitment and retention. Vacancy rates are therefore projected to fall from their current levels in most cities, with any rises in vacancy rates to be extremely limited in scale.

Figure 4: Net Lettable Area Index (Q1 2026=100) and Vacancy Rate Projections (Q1 2026 to Q4 2028)

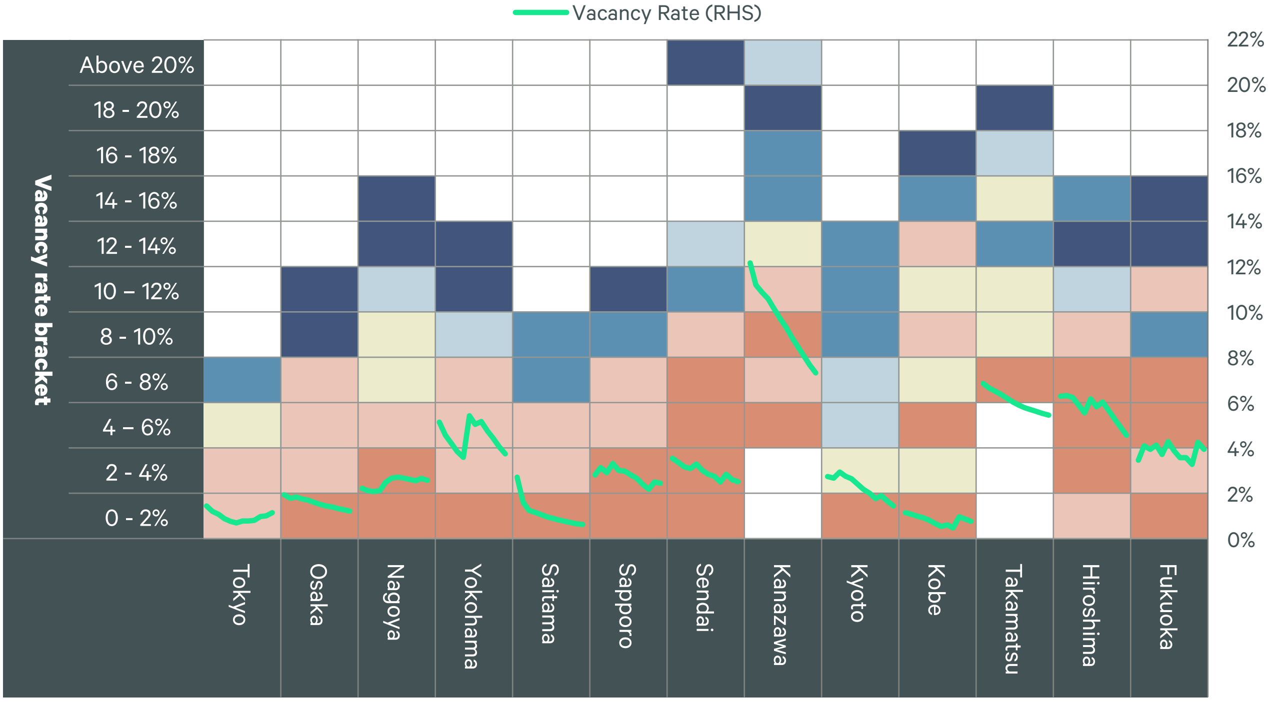


Note: Figures in the graph are values for the end of the projection period (Q4 2028). Projections made in April 2026, other than for Takamatsu (October 2025).
Source: CBRE, Q1 2026.

4. Rents projected to rise in all cities

Figure 5 combines CBRE's vacancy rate projections from Figure 4 with the rent increase/decrease probabilities of Figure 3. Vacancy rates are likely to remain at levels that ensure rents are more likely to increase in all cities. Even if demand proves lower than anticipated, vacancy rates should remain at levels at which rents are still projected to rise.

Figure 5: Vacancy Rate Projections (Q1 2026 to Q4 2028) and Probabilities of Rent Increases/Decreases



	Higher probability of rent increases			Sample size: Fewer than three instances	Higher probability of rent decreases			
Rent increase probability	Above 80%	60 – 80%	Below 60%	-	Below 60%	60 – 80%	Above 80%	Rent decrease probability

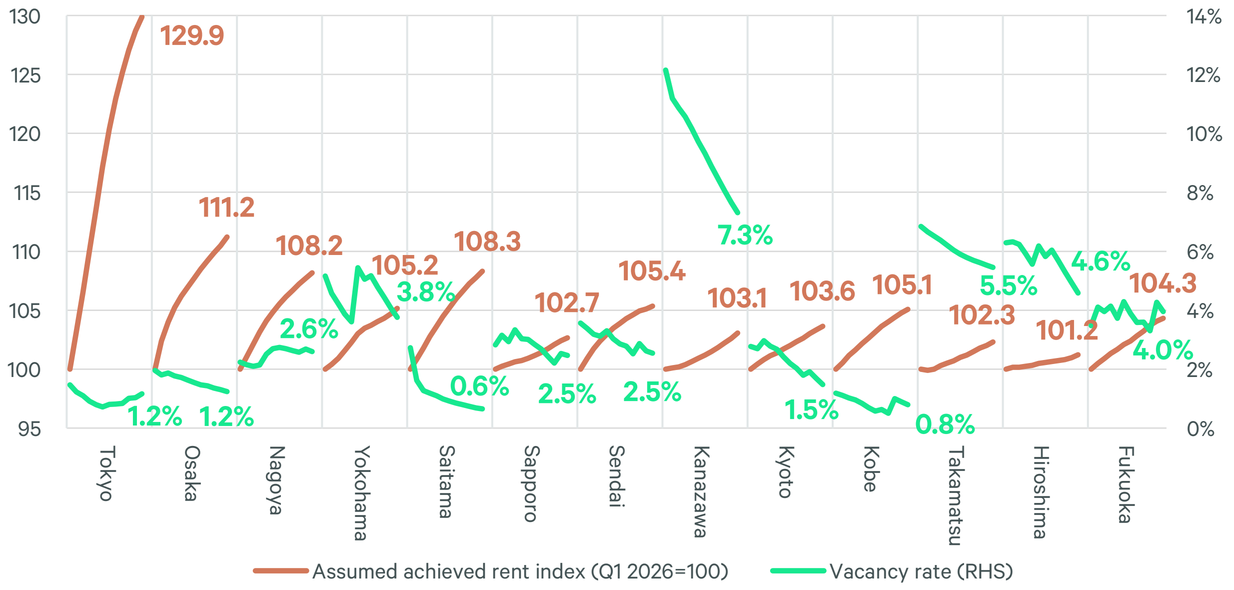
Source: CBRE, Q1 2026.

The aforementioned factors underpin CBRE's projection for rents to increase from their current levels across all cities (Figure 6). Tokyo is expected to experience the highest rate of increase, with an estimated rise of 29.9% forecasted to occur between Q1 2026 and Q4 2028. When remote work began to proliferate during the COVID-19 pandemic, Tokyo was most significantly affected by the initial but ultimately mistaken belief that offices would no longer be required. As a result, rents fell by 9.5% from their peak levels in Q1 2020 to their nadir in Q3 2023, only recently recovering to pre-pandemic levels in Q1 2026. In addition, future new supply includes high-quality buildings with asking rents notably higher than surrounding properties. With pre-leasing proceeding smoothly for these buildings, a knock-on effect on the rents of existing buildings is emerging.

High-quality buildings are also in the supply pipeline in other cities. Although differences in market scale mean that new supply has a greater impact on vacancy rates in regional cities than in Tokyo, should demand be secured to keep vacancy rates below each city's neutral vacancy rate, rents could increase more sharply than expected.

The concept of “neutral vacancy rate” provides an effective new means for predicting future movements in rent levels. This is not an absolute line in the sand; rather, it considers the distance between each city’s current vacancy rate and its own distinct rate at which supply and demand are evenly balanced. CBRE believes that analyzing the current vacancy rate's proximity to the neutral vacancy rate, and its trajectory, could enhance the accurancy of rental forecasts.

Figure 6: Assumed Achieved Rent Index (Q1 2026=100) and Vacancy Rate Projections (Q1 2026 to Q4 2028)



Note: Figures in the graph are values for the end of the projection period (Q4 2028). Projections made in April 2026, except for Takamatsu (October 2025).
Source: CBRE, Q1 2026.

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