Savills World Research
Malaysia

Asian Cities Report
Kuala Lumpur Investment

2H 2015

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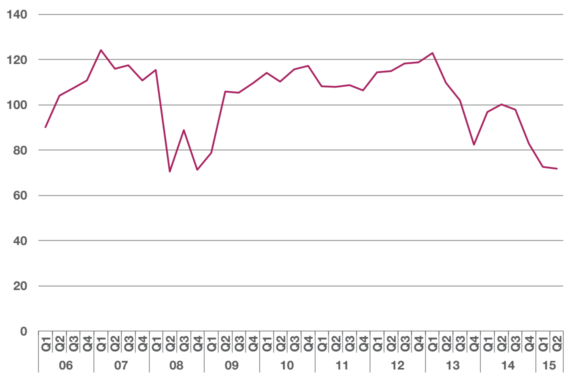
GRAPH 1

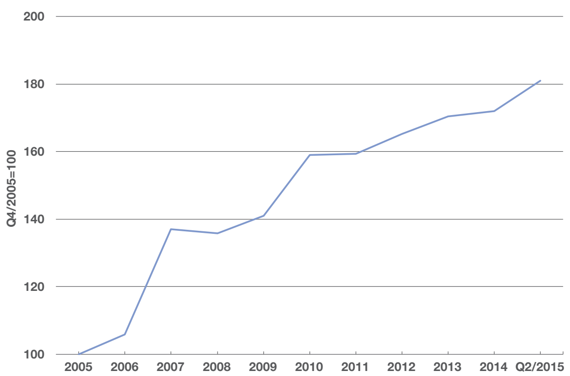
Malaysia consumer sentiment index, Q1/2006–Q2/2015



Source: Malaysia Institute of Economic Research

GRAPH 2

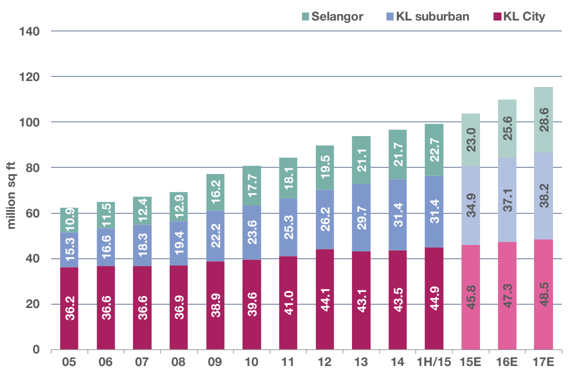
Retail prime rental index, 2005–Q2/2015



Source: Savills Research Malaysia

GRAPH 3

Greater KL office stock, 2005–2017E



Source: Savills Research Malaysia

Retail market

Malaysia retail sales growth has been revised for the fourth time by the Malaysia Retailers Association, lowered from an initial anticipated growth rate of 5% to 3.1% for 2015. 1H/2015 saw a major decline in sales, experienced by even the best malls. The Malaysia Consumer Sentiment Index has reached a low point, similar to the level recorded during the Global Financial Crisis (2008). Market expectations for Q4/2015 are for an improvement if sentiment picks up.

The implementation of the GST paired with a weak Ringgit has had a huge impact on the retail sector. Retailers' margins have been squeezed, in order to remain in this highly competitive market, especially in the fashion industry. Generally, sales have declined by about 20% in tourist related activities and purchases, partly caused by the airline mishaps of 2014.

As at August 2015, the total retail space (shopping malls) in Greater KL totalled 54.52 million sq ft. Market observers question the oversupply of shopping malls in Greater KL. Our take is that retail leakage may occur within a particular market segment i.e. PJ North where the upcoming 1.8 million sq ft Empire City Mall and 1 million sq ft Tropicana Gardens Mall compete with 1Utama Shopping Centre and The Curve. Mitsui Outlet Park which was officially opened in July 2015, received an overwhelming response from the market. However, its sales performance is below expectations. IOI City Mall located at Putrajaya received a spectacular response from the market. Prime rents at this mall have already reached RM30 per sq ft, which closely matches that of 1Utama and The Curve.

Pavilion KL, Suria KLCC and Mid Valley Megamall are the top mall performers in the country and continue to be popular among tourists, locals and retailers alike. The highest gross rent achieved in Malaysia is RM180 per sq ft for prime retail space at Suria KLCC. Malaysia remains the most affordable market in the region and continues to attract more multinational retailers. For example, the first Ferrari Junior outlet opened in Pavilion KL during Q2/2015, Catimini opened its second outlet in The Gardens Mall and Zalora, an online retailer, which has newly adopted the brick & mortar concept, opened their first outlet at Mitsui Outlet Park.

Outlook

2015 has been a period of consolidation for the retail sector as retailers have adopted a cautious approach, delaying expansion plans or postponing sign-ups until closer to the mall's opening date with mall owners even offering rent incentives and capex contributions to tenants.

The next focus will be on affordable fashion and multi-channel retail as the younger generation will form the majority of shoppers according to demographic studies, with an increased preference for online retail purchases.

With numerous malls coming on stream, consumers can expect to be spoilt for choice, thus the shopper experience and the quality of mall management cannot be compromised. Pressure has already been felt by the older malls with the continuing dilution of shopper counts. It will be essential for mall owners to carry out asset enhancement initiatives in order to compete with the newer malls. Nonetheless, retail centres which are fundamentally strong and fulfill the basic requirements of good location and right trade mix will continue to perform well.

Office market

Supply, take-up & vacancy rates

Seven office buildings were added to the office leasing market in Greater KL during the review period. Location-wise, four of these office buildings are located in the KL city area (Menara Centara, Summer Suites, Naza Tower and Menara Bangkok Bank) and another three in Selangor (Top Glove Tower, Nexis Biz Suite and The Ascent @ Paradigm). These buildings have contributed an additional 2.74 million sq ft to overall office stock.

Due to the recent slowdown in the oil and gas sector, there was little notable sub-lease activity between the affected anchor tenants and other interested parties. The oil and gas players have also turned cautious with their expansion or relocation plans due to market uncertainties.

On a positive note, there are still other sectors such as the financial services, IT and manufacturing firms which were active in looking for space for their expansion or relocation strategies during the review period. For example, Menara One Sentrum in KL Sentral was occupied by Royal Bank of Canada and Prima 6 in Cyberjaya was leased to Ansell during the review period.

The new office stock has mostly catered to the changing demands and standards relating to sustainability and design efficiency. Kuala Lumpur's overall office market still enjoys a healthy take-up rate of new supply as demand for better quality buildings continues to rise.

The average vacancy rate in Greater KL rose to 14.1% as at 1H/2015, which is 1.0% higher than that of 2H/2014. This is supported by the inclusion of new office completions to the leasing market which have exerted upward pressure on vacancy rates, especially from newly handed-over projects in the KL City area where rivalry is intensifying.

Rents

Pressured by an influx of new supply, the rental appreciation rate has always been slow, with some barely keeping pace with the inflation. Overall, the average rent across Greater KL experienced a minimal decrease during 1H/2015, due to declining rents in some older office developments especially in the KL City zone.

Major transactions

The investment sector was very active during the review period with at least six deals recorded. There were three transactions in the KL city area which included Plaza Pekeliling, Menara Raja Laut and the Integra Tower. In Selangor, the sold properties were Tropicana City Office Tower, Quill Building 10 and Iconic Office @ Empire City Damansara. These six transactions snowballed to a value of RM2.03 billion, the highest annual transaction value recorded since 2009.

The most significant deal was the acquisition of Integra Tower by the Retirement Fund Inc (Kumpulan Wang Persaraan) from the New-York based asset manager, BlackRock for a whopping price of RM1.065 billion or about RM1,400 per sq ft.

Outlook

The current downturn in the market perhaps suggests an opportune timing for property acquisition as transactions completed in 1H/2015 have been escalating, thanks to strong demand from domestic purchasers.

Although the short-term outlook remains lackluster mainly due to the uncertainties faced by the oil and gas industry, we note that this is offset by recent leasing transactions which were mainly driven by other business sectors including computer technology, manufacturing and financial and banking services.

Residential market

Cautious market sentiment

The Goods and Services Tax (GST) which was implemented in April 2015, coupled with the weakening ringgit have made Malaysians scrutinise their shopping needs rather than exercise more caution in their spending behaviour. This situation has made developers more cautious in their new launches and some have even postponed their product launches. Although the mortgage approval rate was marginally down, the total value of mortgage applications and approvals showed an increase of 19% and 17% from Q1 to Q2/2015, respectively.

Developers change strategy

The cumulative stock of high-end condominiums (>RM800 per sq ft) in Kuala Lumpur stood at about 21,756 units as at 1H/2015 with 408 new completions. The new completions included D'Majestics (Jalan Pudu), Damai 88 (off Jalan Ampang), 9Madge (U-Thant) and Saville @ The Park (Bangsar). Kuala Lumpur's condominium market in general, has continued to see high-end products being launched despite the economic challenges. Some of these projects are located in the KLCC enclave such as Tropicana The Residences at Jalan Ampang, The Grid @ 21 Kia Peng and 8 Kia Peng. Nevertheless, we also saw developers who have shifted their interest to developing in suburban areas, with demand for lower priced products ranging from RM500 to RM800 per sq ft still strong in areas such as Cheras, Setapak, Sungai Besi and Bukit Jalil. The right product proposition, pricing and location all play a vital role in determining demand which continues to grow in some areas in spite of a general slowdown in the property market.

Subsale market remains stable

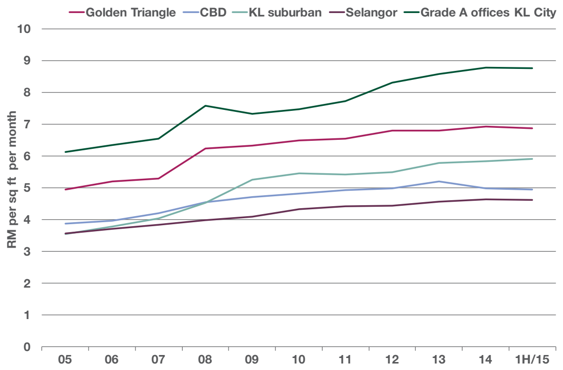
KLCC, Bangsar and Mon't Kiara are among Kuala Lumpur's hot spots in the high-end condominium market belt where prices have appreciated more than other locations. The secondary market transactions of the high-end condominiums in these three areas remain steady, with an average transacted price of RM893 per sq ft, an increase of 7% from 1H/2014. On the rental front, asking rents have continued to hold steady. Nevertheless, the influx of incoming projects might dampen the rental market amid weak occupational demand and increasing competition in selected locations.

Is the future still bright?

Notwithstanding the economic challenges which may affect property prices indirectly and/or the cautious stance adopted by some residential property buyers who may choose to stay on the sidelines, the development growth of high-end condominiums in Kuala Lumpur appears to be stable. As long as development projects possess good design concepts with high quality building specifications, are well-located in prime areas and supported by the upcoming transport infrastructure in and around Kuala Lumpur, demand for such products will be underpinned by a good employment market and a low interest rate environment.

GRAPH 4

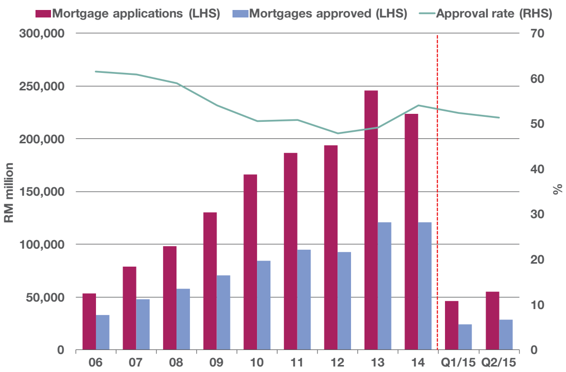
Greater KL office gross asking rents, 2005–1H/2015



Source: Savills Research Malaysia

GRAPH 5

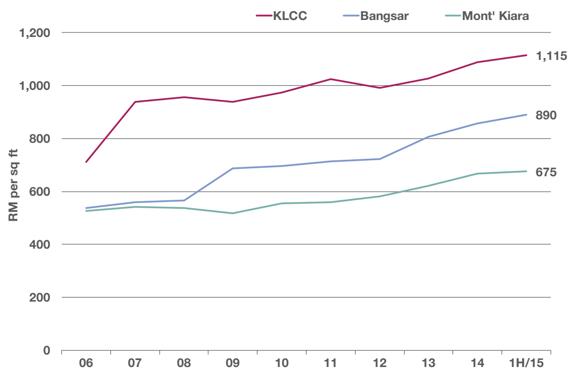
Mortgage applications vs mortgage approvals, 2006–Q2/2015



Source: Bank Negara Malaysia

GRAPH 6

Capital values for secondary market luxury condos, 2006–1H/2015



Source: Savills Research Malaysia

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