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Savills Research
Singapore

Briefing
Office sector

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Image: Robinson Road

SUMMARY

Absorption is slow but steady with occupancy levels remaining healthy in many buildings.

- The global economic outlook has become more optimistic but challenges remain.
- The leasing market has been dominated by enquires from small- to medium-sized office space users.
- Occupancy in CBD Grade A office buildings improved slightly with vacancy rates falling from 6.8% in Q4/2011 to 6.5% by end Q1/2012.
- Grade A monthly rents averaged S$8.58 per sq ft in Q1/2012, representing a 1.7% quarterly decline.
- Investment sales stagnated with average capital values of CBD Grade A offices falling by 4.1% to S$2,445 per sq ft.
- Island-wide, the future supply between 2012 and 2015 totals about 6.90 million sq ft, of which about 59% or 4.04 million sq ft will be located in the CBD.

"Demand from investment banking institutions have tailed off. On the other hand, MNCs in the oil & gas, commodities and natural resources sector together with banks specializing in wealth management have continued expanding."

Alan Cheong, Savills Research

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Market commentary

In recent weeks, the global economic outlook has brightened a little, following the second Greek bailout package and the pickup in economic activity in the United States. However, any recent good news should be treated with caution because of the weak economic conditions in Europe and the slowdown of China's economy. Given the subdued global backdrop, growth prospects in Singapore are expected to remain tepid in 2012.

Amid these uncertainties, the financial sector has been hardest hit. According to the latest official statistics, activity in the domestic financial markets shrank significantly in Q4/2011, with average daily turnover volumes in the forex market falling by 8.4% quarter-on-quarter. In the job market, the financial services industry has been beset with restructuring, redundancies and hiring freezes mostly driven by the larger international financial institutions which reduced headcount by 3,100 in Q4/2011, making it the first quarter of job losses in 2011. Consequently, leasing enquiries from this sector have been few and far between.

Nevertheless, the economies in Asia are considered more resilient compared with their counterparts in the Euro zone and the US. In order to win a slice of the wealth management business and tap the booming trade flows in Asia, international banks and corporations in energy and natural resources have shifted their operations eastward and expanded their presence in the region. Singapore is always at the top of their list due to its political stability, favorable business environment, attractive corporate tax rate and easy access to other Asian countries.

The office leasing market has witnessed several such deals in the last few quarters. For example, Banco Santander, a leading Spanish bank, has opened a branch in OUE Bayfront. It was also reported that companies such as Pearl Energy, LDH Energy, British Gas and Sinochem have leased space ranging from 9,000 sq to 15,000 sq ft in newly completed buildings, including One Raffles Place Tower 2 and Asia Square Tower 1.

Overall, shrinking demand from investment banks and the threat of shadow space being returned are being offset by the ongoing demand from MNCs in the oil and gas, commodities and natural resources industries and banks specializing in wealth management. Consequently, vacant space is being absorbed slowly but steadily, and occupancy levels have remained healthy in many buildings. Savills observed that landlords are not reducing their asking rents as dramatically as two years ago when the global financial crisis just broke out.

The volatile office rents over the past few years may have pushed some small and medium enterprises to buy their own premises, fuelling the brisk sales activity in the strata office market in Q1/2012. During that quarter, several projects were launched island-wide, such as PS100 at Peck Seah Street, Robinson Square at Robinson Road, Paya Lebar Square in Paya Lebar Central and some small developments in the east region. The overwhelming response for these projects may have also been boosted by investors who have shifted their focus from the residential market.

Vacancy rates

By end Q1/2012, vacancy rates of overall Grade A offices fell from 6.8% in Q4/2011 to 6.5%, partly due to limited new supply during the reviewed period. Unlike the AAA and A grade office space, vacancy rate in the AA grade office buildings continued to edge up because of tenant relocation to the AAA grade buildings.

By location, the Beach Road / Middle Road and City Hall areas experienced higher vacancy rates compared with the previous quarter, whereas vacancies in other micro-markets fell by between 0.2 and 1.4 percentage points from the end of last year.

Rental and capital values

CBD Grade A office rents tracked by Savills fell by 1.7% quarter-on-quarter averaging S$8.58 per sq ft per month in Q1/2012, slightly higher than the 1.5% quarterly drop recorded in Q4/2011. Compared with the previous peak in Q2/2011, rents have softened by 4.1%. Rents in most micro-markets registered moderate declines ranging from 0.6% to 2.9% quarter-on-quarter.

In the investment sales market, a mismatch between the expectations of buyers and sellers, together with concerns over the macro-economic situation, has made negotiations more protracted. As a result, the market has

TABLE 1

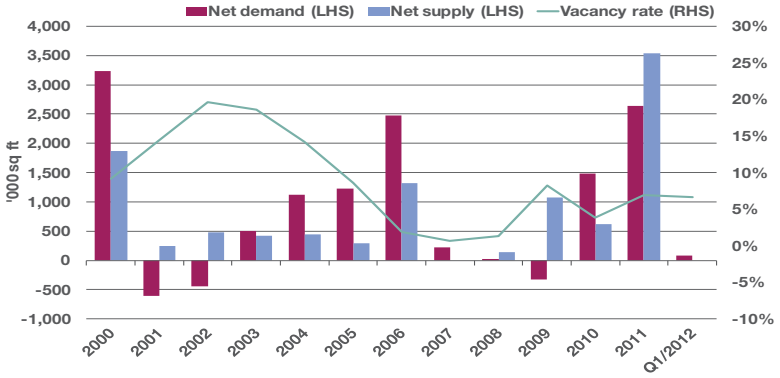
Micro-market Grade A rents and vacancy rates, Q1/2012

Location	Rent (S$ per sq ft)	Vacancy rate (%)
Raffles Place/Marina Bay	9.25	6.2
City Hall	8.72	3.7
Shenton Way	8.01	12.0
Tanjong Pagar	7.13	7.5
Orchard	9.13	3.3
Beach Road/Middle Road	6.81	4.5

Source: Savills Research & Consultancy

GRAPH 1

Net supply, net demand and vacancy rate for CBD Grade A office space, 2000–Q1/2012



Source: Savills Research & Consultancy

been lacklustre in Q1/2012 with only S$537 million worth of transactions, down by a whopping 77% from the previous quarter. The capital values of Grade A offices continued to fall for a second successive quarter, averaging S$2,445 per sq ft in Q1/2012, a 4.1% drop from the S$2,550 per sq ft in Q4/2011.

Future supply

Island-wide, there is approximately 6.90 million sq ft of office space slated for completion between 2012 and 2015, of which about 59% or 4.04 million sq ft will be located in the CBD, mainly from Marina Bay Financial Centre Tower 3, Asia Square Tower 2, CapitaGreen and South Beach. According to Savills estimates, about 1.05 million sq ft or 26% of the four-year new supply in the CBD had been pre-committed as at the end of Q1/2012. Outside the CBD, about 2.86 million sq ft is expected to come on stream over the same period. The majority of the new space is found in the regional centres, such as one-north, Jurong Lake District and Paya Lebar Central. Pre-commitment is low at about 11%, giving rise to oversupply concerns for office buildings located outside the CBD.

TABLE 2

Major projects in the pipeline, 2012–2015

Project name	Location	Estimated NLA (sq ft)	Estimated completion
Inside CBD			
Marina Bay Financial Centre, Tower 3	Marina Boulevard	1,300,000	2012*
Asia Square Tower 2	Marina View	780,000	2013
CapitaGreen	Market Street	700,000	2014
South Beach	Beach Road	506,000	2015
5 Shenton Way	Shenton Way	260,000	2015
Outside CBD			
JEM	Jurong Gateway Road	315,400	2013
The Metropolis	North Buona Vista Drive	1,000,000	2013
Paya Lebar Square	Paya Lebar Central	430,000	2014
Westgate	Boon Lay Way	315,000	2014

Source: Savills Research & Consultancy
*MBFC Tower 3 has received TOP in March 2012.

OUTLOOK

The prospects for the market

Although there are signs that the US economy is on the mend, the outlook for the global economy remains uncertain because significant risks still exist, such as protracted weakness in Europe due to the need for deleveraging and fiscal consolidation. Therefore, companies are expected to remain cautious over the year ahead and are not expected to change their stance in the near term.

Savills expects that, after factoring in new supply and possible shadow space, vacancy rates are likely to rise to 9 – 11% by the end of 2012 depending on how the global and local economies pan out. Increasing volumes of vacant space will inevitably put pressure on Grade A rents, which are expected to continue trending downwards in the next few quarters.

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