

Briefing Office sector

October 2012



Image: Marina Bay

SUMMARY

Activity in the office leasing market has been tepid in the third quarter of 2012.

- Corporate tenants were still looking for office space, but taking advantage of a weakening market, they sought-out bargain rents, often prolonging the negotiation process.
- In the CBD, Grade A office vacancy rates rose to 8.1% because of increasing vacant stock in the Shenton Way and Marina Bay areas.
- Monthly average rents of CBD Grade A offices declined by 1.0% quarter-on-quarter (QoQ) to S\$8.39 per sq ft.
- Grade A office capital values dipped slightly amid a slowdown in buying activity.
- Approximately 2.5 million sq ft of office space will enter the market in the remainder of 2012 and the year ahead, 17% of which has been pre-leased to-date.
- Looking ahead, the office leasing market will continue to be impacted by a worsening economic environment and the sizeable future supply over the next 12 months with rents expected to soften further.

“Given the macroeconomic backdrop, more companies are less upbeat about their business outlook and are adopting a wait-and-see approach in the leasing market. As a result, occupancy rates have been instrumental in driving rents.”

Alan Cheong, Savills Research

➔ **Market commentary**

The protracted European sovereign debt crisis, together with the weak growth in the US and China, is creating strong headwinds for the global economy. Given the macroeconomic backdrop, the Singapore government has narrowed the full-year GDP growth forecast from 1% to 3%, to 1.5% to 2.5%, after the modest expansion in the economy for the first two quarters of 2012.

Surprisingly, the labour market remained healthy as employment rose by 58,900 in the first half of 2012, compared with the increase of 53,100 in the corresponding period last year. June's unemployment rate, therefore, has reversed the slight increase in March, falling to 2.0%. Employment creation was seen in most industries, with the financial and insurance, real estate, and professional services

TABLE 1 **Micro-market Grade A office rents and vacancy rates, Q3/2012**

Location	Rent (S\$ per sq ft)	Vacancy rate (%)
Raffles Place/Marina Bay	8.87	8.2
City Hall	8.59	1.4
Shenton Way	7.54	18.5
Tanjong Pagar	7.47	7.7
Orchard Road	9.29	3.3
Beach Road/Middle Road	6.81	3.8

Source: Savills Research & Consultancy

sectors adding about 5,900 workers in Q2. Nevertheless, in view of the deteriorating economic environment, employment prospects have become less optimistic as more companies are expecting business conditions to worsen in the second half of 2012.

offset the fall in vacancy in most of the other areas. The overall vacancy rate of Grade A offices therefore rose from 6.7% in Q2/2012 to 8.1% in Q3/2012.

Thanks to the healthy pre-commitment levels at MBFC Tower 3, the net absorption of Grade A office space in Q3/2012 reached about 860,000 sq ft, more than double the 345,000 sq ft in 1H/2012. This brought the net take-up to 1.2 million sq ft in the first three quarters of 2012. However, it still fell short of the 1.6 million sq ft of supply from Q1 to Q3 of 2012, resulting in a higher vacancy rate compared with the end of last year.

Rents and capital values

The substantial amount of vacant space in the Shenton Way area has weighed heavily on rents, causing them to fall by 4.3% QoQ to S\$7.54 per sq ft in Q3/2012. The same situation is also witnessed in the Raffles Place/Marina Bay and Orchard areas, where average rents settled at S\$8.87 per sq ft and S\$9.29 per sq ft, declining 1.4% and 0.4% QoQ respectively. In contrast, rents in some other areas remained flat or even strengthened on the back of improving occupancy rates. For example, average rents in the Beach Road/Middle Road area remained at S\$6.81 per sq ft, while the Tanjong Pagar rents rose by 4.8% QoQ to S\$7.47 per sq ft. The City Hall submarket is the only exception, where occupancy rates improved but average rents slipped by 0.7% QoQ to S\$8.59 per sq ft in Q3.

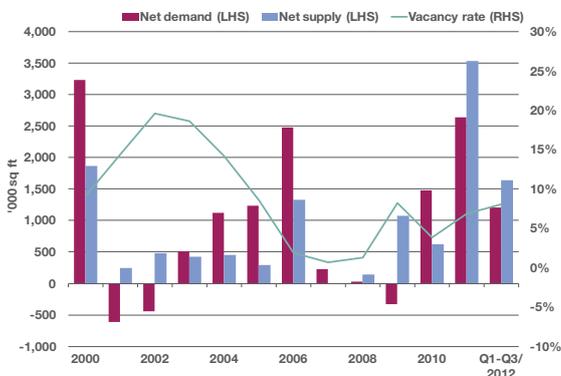
Overall, CBD Grade A office monthly rents tracked by Savills decreased marginally to S\$8.39 per sq ft in Q3/2012 from S\$8.47 per sq ft in the previous quarter. This quarterly decline

Activity in the office leasing market remained moderate in the third quarter of 2012. Aside from the banking and finance industries, corporate tenants were still looking for office space to either accommodate their expanding businesses or set-up a new presence in Singapore. Taking advantage of the weakening market, these users sought bargain rents, often leading to a prolonged negotiation process. Depending on their buildings' take-up, some landlords have become more flexible in their rental negotiations. Hence, the higher the occupancy rate of a building, the more robust are its rental rates.

Vacancy rates

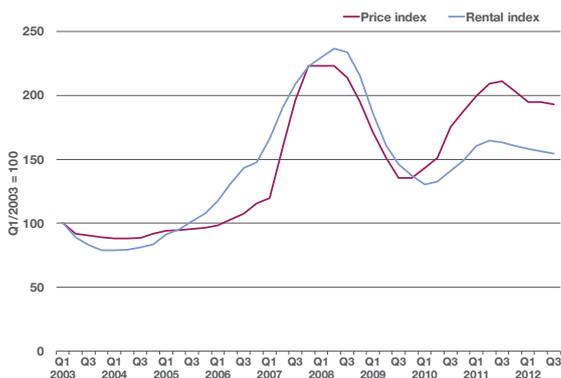
In the reviewed quarter, DBS Bank started its shift from DBS Building to the newly-completed Marina Bay Financial Centre (MBFC) Tower 3, which has contributed about 1.3 million sq ft of Grade A office space in the Marina Bay precinct. DBS Bank's relocation has created a substantial amount of vacant office space in the Shenton Way area, pushing up the vacancy rate in this submarket to 18.5% by the end of September, from 11.1% three months ago. The vacancy rate in the Raffles Place/Marina Bay area also increased about 70 basis points to 8.2% in Q3/2012, partly attributed to the remaining un-let space in MBFC Tower 3. The growing vacant stock in these two major submarkets has more than

GRAPH 1 **Net supply, net demand and vacancy rate for CBD Grade A office space, 2000–Q3/2012**



Source: Savills Research & Consultancy

GRAPH 2 **Savills Grade A office price and rental indices, Q1/2003–Q3/2012**



Source: Savills Research & Consultancy

TABLE 2
Major future projects, Q4/2012–Q4/2013

Location	Street name	Expected TOP year	Office NLA (sq ft)	Pre-commitment (%)
Central area				
One Upper Pickering	Upper Pickering Street	2012	87,000	100
Asia Square Tower 2	Marine View	2013	780,000	0
Orchard Gateway	Orchard Road	2013	37,000	0
Outside central area				
223 @ Mountbatten	Mountbatten Road	2012	123,300	0
Fusionpolis Phase 3	Fusionpolis Link	2013	93,200	0
Jem	Jurong East Street 13	2013	315,400	100
The Metropolis	North Buona Vista Drive	2013	1,058,000	1

Source: Urban Redevelopment Authority, Savills Research & Consultancy
TOP = Temporary Occupation Permit

of 1.0% is the smallest since Q4/2011. In Q3/2012, the capital values of Grade A offices also dipped 1.0% to S\$2,420 per sq ft. Buying activity in the office segment slowed significantly in view of mounting concerns over the global economy and the perennial bid-ask gap between vendors and buyers.

Just two major office deals in the CBD were sealed in the reviewed quarter. In July, the freehold property Robinson Point, located along Robinson Road, was sold for S\$284 million or S\$2,132 per sq ft based on NLA, while Alpha Investment acquired a 50% stake in

78 Shenton Way for S\$304 million or S\$1,682 per sq ft based on NLA. Outside the CBD in the Kallang area, listed company KSH Holdings bought the freehold property Sam Leong Mansion in a collective sale for S\$40.3 million or S\$1,087 per sq ft per plot ratio. A new commercial building can be developed on the site.

Future supply

Island-wide, approximately 2.5 million sq ft of office space is in the pipeline for the remainder of 2012 and the year ahead. Among these future projects, the entire office block in the mixed

OUTLOOK

The prospects for the market

The worrisome outlook for the world economy has prompted the World Trade Organization to scale-back its 2012 growth forecast from 3.7% given in April, to 2.5% in September. Singapore's economy, in particular the externally-oriented sectors, has been inevitably affected by the slowdown in advanced economies. Furthermore, the unexpected fall in factory output in August may have created concerns over a technical recession. Looking ahead, the office leasing market will continue to be impacted by a worsening economic environment and the sizeable future supply over the next 12 months with rents expected to soften further.

development on Upper Pickering Street has been pre-leased to the Attorney-General's Chambers, while Jem at Jurong East has also leased its office tower to the Ministry of National Development, Building & Construction Authority and the Agri-Food and Veterinary Authority. In addition, The Metropolis in one-north has secured Fitness First for its 12,600-sq ft space in Tower 2. Consequently, the pre-commitment level is now 17% year-to-date, leaving about 2.1 million sq ft of vacant space in these upcoming projects, mainly in Asia Square Tower 2 at Marina View and The Metropolis. ■

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