

# Briefing Office sector

October 2014



Image: Marina Bay

## SUMMARY

Heady days are here for the office market but the supply in store is large and may moderate rents next year.

- With the delay in the completion of South Beach Tower, as well as the tenants of Equity Plaza having to relocate to make way for its major refurbishment works (removing approximately 253,000 sq ft of existing stock by March 2015), there is a tighter squeeze on available space in the CBD prime office market.

- The overall CBD Grade A office vacancy rate dipped further, by 0.5 percentage points (ppt(s)) from 3.9% in Q2/2014 to 3.4% in Q3/2014.

- After experiencing slower growth of 2.3% in Q2/2014, the overall quarter-on-quarter (QoQ) rental growth for CBD Grade A offices in

Q2/2014 was a strong 4.4%. Average transacted rents in Q3/2014 for Savills basket of CBD Grade A office buildings stood at S\$9.63 per sq ft per month, up from S\$9.22 recorded last quarter.

- At S\$1.94 billion, the total private sector office investment sales in Q3 were the highest since Q4/2012. Capital values of Grade A offices tracked by Savills increased from S\$2,780 per sq ft in Q2/2014 to S\$2,800 per sq ft in Q3/2014.

- For CBD Grade A office rents, we maintain our view that they will continue their upward march into Q4/2014. Thereafter, for 2015, it may stabilise

due to factors such as uncertainties in the global and regional economies and landlords adjusting rates in anticipation of the deluge of supply in 2016.

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 “Office building sales and the subsequent decanting of tenants due to renovation works spring positive surprises for the market, creating short-term supply constraints.”  
 Alan Cheong, Savills Research  
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### → Market commentary

According to advance estimates from the Ministry of Trade and Industry, Singapore's economy grew 2.4% year-on-year (YoY) in the third quarter of 2014. This is the same pace of growth as in the second quarter. The economy expanded by 1.2% quarter-on-quarter (QoQ), a contrast to the 0.1% contraction in the previous quarter. There is growth across all sectors except construction, which suffered a contraction of 2.7%. Nevertheless, growth in the services industries was supported primarily by finance, insurance and business services sectors, which in turn boosted the office property market, increasing leasing and sales activity.

There is continued broad-based demand from newly set-up companies and expanding firms, mainly from the IT and telecommunications industry and legal service providers. With the delay in the completion of South Beach Tower, as well as the tenants of Equity Plaza having to relocate to make way for major refurbishment works (removing approximately 253,000 sq ft of existing stock by March 2015), the CBD prime office market faces a squeeze. This, together with rising demand and lack of new supply, gives landlords much more bargaining power on rents. Rents have therefore escalated at a much faster pace than the preceding quarter.

A few notable leasing deals in the reviewed quarter include 40,000 sq

TABLE 1 **Micro-market Grade A office rents and vacancy rates, Q3/2014**

Location	Rent (S\$ per sq ft per month)	Vacancy rate (%)
Raffles Place/Marina Bay	10.27	2.4
City Hall	9.66	1.4
Shenton Way	9.32	7.7
Tanjong Pagar	8.20	6.4
Orchard Road	9.92	1.9
Beach Road/Middle Road	7.67	2.2

Source: Savills Research & Consultancy

ft in 6 Battery Road leased by Willis Insurance and 83,000 sq ft in Westgate Tower leased by CPG Corporation. Westgate Tower at Jurong East, with a total NLA of 305,000 sq ft, is reported to be 60% leased out.

In the strata office sales market, the number of transactions dropped by 60.1% from 188 in Q2/2014 to 75 in Q3/2014. This drop was attributed to the lack of new sale launches of strata commercial projects. Meanwhile, there is continued keen investor interest in existing CBD office buildings, as seen in the three major en-bloc deals inked in the reviewed quarter. They include a 33.3% stake in Marina Bay Financial Centre (MBFC) Tower 3 (S\$1248.0 million); Straits Trading Building (S\$450.0 million); and Anson House (S\$172.0 million).

### Vacancy

The net absorption of Grade A office space in the CBD was about 130,000 sq ft in Q3/2014, totalling nearly 769,000 sq ft for the first three quarters of the year. With no new supply available, the overall vacancy rate for CBD Grade A offices fell from 3.9% in Q2 to 3.4% in Q3.

Across the submarkets, vacancy rates of Grade A offices in Shenton Way marked the greatest quarterly decline of 1.5 percentage points (ppts), followed by those in Orchard Road (0.8 ppts), Raffles Place/Marina Bay (0.4 ppts) and City Hall (0.2 ppts). Conversely, vacancy rates in the Beach Road/Middle Road area inched up by 0.1 of a ppt and the Tanjong Pagar submarket had a 0.7 ppt rise.

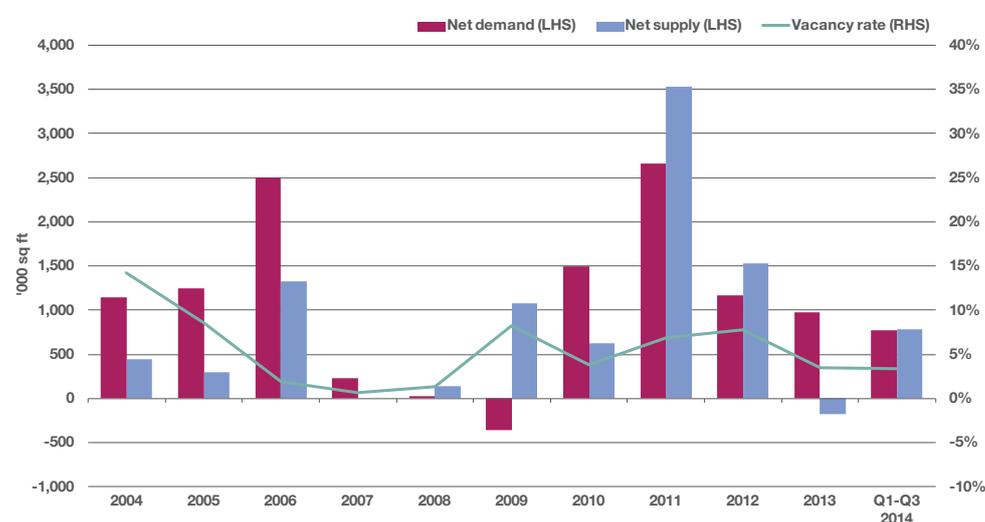
By grade, the AAA segment saw the greatest fall in vacancy level by 0.9 ppts to 5.0% by the end of September. This was followed by the AA Grade segment which dipped 0.7 ppts to 1.9%, and the A Grade segment slipping 0.1 ppts to 3.2%.

### Rents and capital values

Average transacted rents in Q3/2014 for Savills basket of CBD Grade A office buildings stood at S\$9.63 per sq ft per month, up from S\$9.22 recorded last quarter. By location, Raffles Place/Marina Bay led the market with rents at a record high of S\$10.27 per sq ft since Q3/2010, followed by Orchard Road at S\$9.92 per sq ft and City Hall at S\$9.66 per sq ft.

Overall rental growth for CBD Grade A offices surged 4.4% quarter-on-quarter (QoQ) in Q3/2014, after experiencing a slower growth of 2.3% last quarter. The rental growth is seen across all submarkets, with the exception of Beach Road/Middle Road and Tanjong Pagar, which dipped 1.2 ppts to 2.2%

GRAPH 1 **Net demand, net supply and vacancy rate of CBD Grade A offices, 2004–Q3/2014**



Source: Savills Research & Consultancy

→ and 0.9 of a ppt to 0.6% respectively. The City Hall area had the steepest increase in rental growth at 6.1 ppts to 7.5%, followed by Orchard Road with a 4.0 ppts increase to 4.4% rental growth.

By grade, AAA office rents recorded the highest growth, with a sharp rise of 8.8% QoQ to S\$12.79 per sq ft. This represents a 6.6 ppts increase in QoQ rent growth. The A Grade segment saw a 1.9 ppt increase in rent growth to 3.4% in Q3, standing at S\$8.71 per sq ft. AA Grade office rents, which led Q2's rent growth, were the worst performers this quarter, slowing to a 3.3% growth at S\$10.20 per sq ft. It suggests that there is greater resistance in this market segment as

AA Grade office rents have reached double-digits per sq ft.

Capital values of Grade A offices tracked by Savills increased marginally from S\$2,780 per sq ft in Q2/2014 to S\$2,800 per sq ft in Q3/2014. The total tally of private sector office investment sales in Q3 was the highest since Q4/2012 at S\$1.94 billion. Anson House on Anson Road, Straits Trading Building on Battery Road, and MBFC Tower 3 (33.3% stake) at Marina Boulevard were transacted at S\$2,252 per sq ft based on NLA, while the 18th storey of Samsung Hub on Church Street was sold for S\$3,225 per sq ft on its strata area. ■

GRAPH 2 Price and rental indices of CBD Grade A offices, Q1/2004–Q3/2014



Source: Savills Research & Consultancy

## OUTLOOK

### The prospects for the market

For CBD Grade A office rents, we maintain our view that they will continue their upward march into Q4/2014. Thereafter, for 2015, they may stabilise due to factors such as uncertainties in the global and regional economies and landlords adjusting rates in anticipation of the deluge of supply in 2016. The decanting of tenants from Equity Plaza, many of whom take up only smaller spaces, may support older Grade A office building rents, particularly those with units that are less than 5,000 sq ft in size.

Capital values for CBD Grade A buildings should hold steady well into 2015 as only a few, if any, transactions of entire buildings are expected due to their large ticket size and also the current environment of low initial yields.

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### Savills Research

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