Singapore – February 2019

MARKET IN MINUTES

Savills Research

Office

savills

CBD Grade A office rents up 9.5% in 2018

Not all occupiers were able to find the type of space they were looking for, especially spaces with large floor plates.

- In 2018, leasing demand was still being led by technology, media and telecoms companies as well as the continued expansion of co-working space operators.
- In the last quarter of 2018, Savills measure of the net take-up for CBD Grade A office space was about 479,000 sq ft, bringing the whole-year total to 1.40 million sq ft.
- Vacancy levels went up to 8.1% in Q4/2018 from the 7.7% recorded in Q3/2018. The spike is not disconcerting and is due to the timing of tenants moving into new buildings.
- In Q4/2018, the average rent of CBD Grade A offices rose 2.8% quarter-on-quarter (QoQ), the highest quarterly growth since Q3/2017, to S$9.79 per sq ft per month.
- An active investment sales market and high prices achieved in recent deals have supported capital values of CBD Grade A offices, which rose 3.9% QoQ and 4.8% year-on-year (YoY) to S$2,910 per sq ft in Q4/2018.
- For now, the Grade A CBD office market's 2019 supply is tight, and whilst the vacancy level of good-quality offices has risen again to 8.1% in Q4/2018, on the ground, it feels as though vacancy levels are in the 2-3% range.

"Cross-currents in global trade issues may rein in tenant expansion plans but the lack of new supply forms a strong defensive line against rental declines."

ALAN CHEONG, SAVILLS RESEARCH

Savills team

Please contact us for further information

SINGAPORE

Marcus Loo
CEO, Singapore
+65 6415 3893
marcus.loo@savills.com.sg

Ashley Swan
Senior Director, Commercial
+65 6415 3872
ashley.swan@savills.com.sg

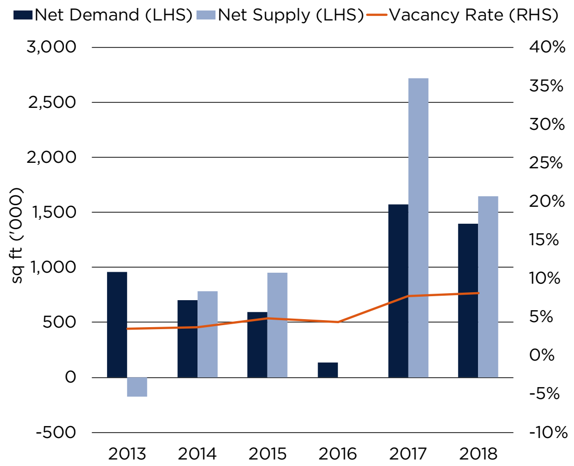
RESEARCH

Alan Cheong
Executive Director
Singapore
+65 6415 3641
alan.cheong@savills.com.sg

Simon Smith
Senior Director
Asia Pacific
+852 2842 4573
ssmith@savills.com.hk

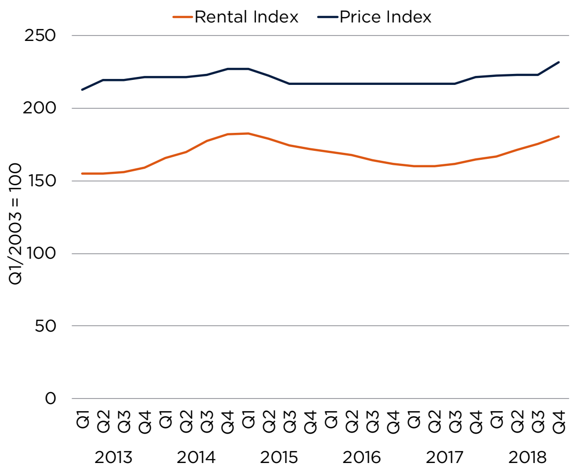
MCI (P) No. 017/10/2018
Company Reg No. 198703410D

GRAPH 1: Net Demand, Net Supply And Vacancy Rate Of CBD Grade A Offices, 2013 to 2018



Source Savills Research & Consultancy

GRAPH 2: Price And Rental Indices Of CBD Grade A Offices, Q1/2013 to Q4/2018



Source Savills Research & Consultancy

TABLE 1: Micro-Market Grade A Office Rents and Vacancy Rates, Q4/2018

LOCATION	MONTHLY RENT (S$ PER SQ FT)	VACANCY RATE (%)
Marina Bay	12.55	14.6%
Raffles Place	9.98	4.1%
Shenton Way	9.04	16.1%
Tanjong Pagar	8.68	4.2%
City Hall	10.10	3.2%
Orchard Road	9.39	3.0%
Beach Road/Middle Road	8.02	7.4%

Source Savills Research & Consultancy

MARKET COMMENTARY

Singapore's economy in 2018 grew at the relatively healthy rate of 3.2% YoY, down from 2017's growth of 3.9%. This better-than-expected GDP growth was supported mainly by the manufacturing sector and services industries, which expanded by 7.2% YoY and 3.0% YoY, respectively. The labour market also improved in 2018, with total and local employment growing and the annual average unemployment rate and retrenchments declining from a year ago.

In the last quarter of 2018, office leasing activity slowed compared with the previous quarter, which may have been due in part to the year-end festive season, which could have lengthened occupiers' decision-making processes. Aside from this, healthy demand over the last two years has taken up most of the spaces in existing office buildings, leaving mainly pocket spaces in the market available for lease, and limited options for occupants looking for large floor plates.

In 2018, leasing demand was still led by technology, media and telecoms companies as well as the continued expansion of co-working space operators. Singapore has continued to grow its ecosystem of tech companies, in particular fintech start-ups, a trend supported by the Singapore government, which is keen for the city-state to become a global hub for fintech.

On the investment sales front, buying attention quickly turned towards the office sector on the back of strong rental growth, after private residential cooling measures came into effect 6 July 2018. As a result, a few big-ticket office deals closed in the last quarter of 2018. These included the S$908.0 million paid by OUE Commercial Real Estate Investment Trust for the office component in OUE Downtown at Shenton Way; the S$608.0 million sale of 78 Shenton Way to PGIM Real Estate; the S$555.5 million outlay made by ARA Asset Management and British property group Chelsfield for Manulife Centre at Bras Basah Road; and the S$537.3 million paid by Allianz Real Estate for a 20% stake in Ocean Financial Centre at Collyer Quay.

DEMAND AND VACANCY

In Q4/2018, Savills measure of the net take-up for CBD Grade A office space was about 479,000 sq ft, bringing the year's total to 1.40 million sq ft. Although this was a decline of 11.1% from 2017's 1.57 million sq ft, the lower take-up was not because of any softening of tenant demand for space, but rather a relative lack of new supply compared to 2017.

Vacancy levels of Grade A office space in the CBD, however, went up to 8.1% in Q4/2018 from the 7.7% recorded in Q3/2018. The spike is not disconcerting and is due to the delayed timing of tenants moving into new buildings. For example, for the newly-completed Frasers Tower included in the Savills basket in Q4/2018, although most of the 664,000-sq ft office space had already been pre-committed, many major tenants had not yet moved in. This also pushed up the vacancy rate in the Shenton Way sub-market, where the project is located, by 12.3 percentage points (ppts) QoQ to 16.1% at the end of 2018.

In fact, for most of the other micro-markets tracked by Savills, including Raffles Place, Marina Bay, City Hall, Orchard Road and Beach Road/Middle Road, vacancy rates continued to improve by 0.1% to 5.5% from a quarter ago.

RENTS AND CAPITAL VALUES

In Q4/2018, average rents of CBD Grade A offices rose 2.8% QoQ, the highest quarterly growth since Q3/2017, and stood at S$9.79 per sq ft per month. For 2018, rents increased 9.5% on a YoY basis, compared to the 1.9% increase in 2017.

The strong rental growth was led by the Grade AAA office sector, which rose 4.8% QoQ in the last quarter and 16.3% for the full year, and the Grade AA office sector, which rose 3.2% QoQ and 11.8% YoY in Q4/2018.

The strengthening of Grade A office rents was seen across the geographic sub-markets that Savills tracks. In Q4/2018, Marina Bay saw the largest rental increase on a quarterly basis (4.8%), followed by Raffles Place (3.5%) and Tanjong Pagar (3.2%). For the whole year, the top three micro-markets enjoying the strongest rental growth were Marina Bay (17.1%), Shenton Way (10.7%) and Tanjong Pagar (10.5%). Tightening available space for lease and higher rents achieved in newer prime grade developments, such as Marina One and Frasers Tower, lent support to these sub-markets.

An active investment sales market and high prices achieved in recent deals supported the capital values of CBD Grade A offices, which rose 3.9% QoQ and 4.8% YoY to S$2,910 per sq ft in Q4/2018.

OUTLOOK

Going forward, major risk factors impacting the global economy, such as increasing threats of trade conflicts possibly leading to slower world economic growth, are making financial markets nervous, which in turn causes decision makers to turn cautious in committing to major capital expenditures. As most of these key decision-makers exchange ideas and often share thinking, they can reinforce each other's fears. In January, the International Monetary Fund again downgraded its global growth forecast, to 3.5% for 2019. For Singapore, the GDP growth forecast looks softer again for 2019 and is expected to come in slightly below the mid-point of the range of "1.5 to 3.5%", according to the Ministry of Trade and Industry.

For now, supply is tight for the Grade A CBD office market in 2019. Savills expects that only about 693,000 sq ft of Grade A office space will be completed in the CBD in 2019, while some 260,000 sq ft of space from Chevron House at Raffles Place has been taken out of the market for an asset enhancement initiative in Q1/2019. In addition, although the vacancy level of CBD Grade A offices has increased to 8.1% in Q4/2018 from 7.6% in Q3/2018, on the ground, it feels as if vacancy levels are in the 2-3% range. Options are limited for tenants requiring 20,000 sq ft or more of office space to move into or to expand into, with suitable offerings in the market less than five in number.

However, there may be increasing risks that rental growth will be slowed and not fall within our 8%-10% forecast range for 2019. First, demand from co-working space operators, who have been expanding aggressively and driving the office rental market over the past two years, may be subdued in the next two years. Secondly, the recent global stock market rout that began in October 2018 and the rate of the Dow and NASDAQ falls may affect the expansion plans of multinationals this year. As equity prices reflect forward earnings, the 3% and 5% YoY decline in the tech-laden NASDAQ and Dow, respectively, for 2018 could foretell corporate conservatism in 2019. The performance of global equity markets poses the major risk factor to attaining our rental forecast of 8%-10% growth this year. However, for the first quarter of 2019, we believe that rental transactions and levels, especially with some potential leasing deals brewing in upcoming projects, will still be good, setting the outlook and tone for this year and even 2020.