SUMMARY

A gradual pick-up in retail rents is expected in the near term.

- For January and February, combined retail sales (excluding motor vehicles) increased 1.1% year-on-year (YoY) due to festive spending and tourism receipts, which were boosted by more visitor arrivals.

- Owing to the lack of new retail supply in Q1/2018, the island-wide retail vacancy rate saw a marginal increase of 0.1 of a percentage point (ppt) from last quarter to 7.5%.

- Prime monthly rents in Orchard Road and the suburban areas remained at S$29.90 per sq ft and S$28.80 per sq ft respectively.

- Domestic consumption is being supported by increased employment within the disruptive and augmentative business sectors while the opening of new malls is causing rents, particularly in the suburban areas, to rise 2.0% to 5.0% YoY in Q1/2018.

“Current determinants driving consumption and tenant behaviour are vectoring up rents, glossing over fundamental weaknesses.”

Alan Cheong, Savills Research
Macroeconomic overview
According to the Ministry of Trade and Industry’s (MTI) preliminary estimates, the Singapore economy grew 4.3% YoY in Q1/2018, up from the 3.6% YoY expansion in the preceding quarter. Growth was mainly led by the brisk performance in the manufacturing sector, which rose from 4.8% YoY in Q4/2017 to 10.1% YoY in Q1/2018. All clusters within the sector expanded, with the electronics and precision engineering clusters recording the highest growth.

In line with the pick-up in economic activity, the job market also improved in Q1/2018. Preliminary data from the Ministry of Manpower’s Labour Market Report Advance Release Q1/2018 showed that the unemployment rate continued to fall, down to 2.0% in March 2018 from 2.1% in December 2017. The number of retrenchments also declined from 3,680 in Q4/2017 to 2,100 in Q1/2018. Despite the drop in layoffs, consumers seem to have cut back on spending as there was no significant increase in expenditure for the first two months of 2018.

During the Chinese New Year festive period this year, consumers spent less at restaurants and on catering, resulting in a 5.1% YoY dip in the combined Food & Beverage (F&B) Services Index1 for January and February 2018. While the combined retail sales (excluding motor vehicles)2 data for the two months showed an increase of 1.1% YoY due to the expenditure on food retailers (+14.0% YoY) and apparel & footwear (+9.2% YoY), the bump could be driven by holiday spending and improved visitor arrivals. Total tourist arrivals reached a record high of almost 3.05 million in both months, 7.3% higher than a year ago. This was led by the 21.7% and 12.3% surge in arrivals from India and China respectively.

Market snapshot
Following the influx of Japanese retailers, other foreign brands recognised potential and ventured into Singapore’s retail market, particularly food chains offering takeaway options. Say Chizu cheese toast from Thailand has massive takeaway kiosks in the central and suburban areas. Within one week in January, it opened its first four branches in Singapore; at VivoCity, 313 @ Somerset, White Sands Shopping Centre and The Clementi Mall. In addition to a takeaway outlet at Waterway Point, opened in February, the Bangkok cheese toast brand opened its first and only dine-in café, with an open kitchen concept, in Singapore at Bugis+. Once it completes plans to open ten branches in Singapore by end-2018, Say Chizu will launch another outlet at Jewel @ Changi Airport in early-2019.

Some brands make Singapore their first port of call when they begin expanding their presence in Southeast Asia’s retail market. In January, Taiwanese bakery Kazo opened its first confectionary store in Singapore at Chinatown Point. Subsequently in March, Austrian bakery Guschlbauer launched its first store for Southeast Asia at Waterway Point. After operating a pop-up at Casa Verde cafe in Singapore Botanic Gardens for eight months, Mul Kee opened a permanent venue at Orchard Road. The new 50-seat restaurant will take over the space vacated by Caveau Bar in Shaw Centre. Hong Kong chain Tsui Wah is also launching in Singapore, with plans to open its first outlet in Southeast Asia soon.

Lastly, Millennium Dance Complex, a dance studio from the United States, set up its first Singapore branch at Marina Square, taking up three units on the second floor.

Orchard Road and the CBD
Facing competition from e-commerce and fast fashion labels such as Zara and H&M, less resilient brands have been forced to exit the market. As part of a shift in focus to its growing brands, Gap shut all of its stores at Suntec City and VivoCity while Banana Republic closed outlets at Paragon and MBS in February. In the same month, American Eagle Outfitters also left the market with the closures of its Suntec City outlet and VivoCity flagship store. Later in March, Cortina Holdings vacated all of its Orchard Road-facing watch boutiques on the first and second level of Wisma Atria, leaving 4,700 sq ft of space unoccupied. The retail chain retained only its Raymond Weil Boutique on the third level of Wisma Atria.

In the sea change disrupting the retail landscape, pop-up stores are still on the rise as retailers test new markets with temporary stores while landlords try to fill vacancies. The pop-up concept used to be popular

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1 Sales Index of Food & Beverage Services at Constant Prices (Seasonally Adjusted), Monthly. Updated as at 13 April 2018.
2 Retail Sales Index at Constant Prices (Seasonally Adjusted), Monthly. Updated as at 13 April 2018.

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GRAPH 1
Growth of retail sales (excluding motor vehicles), YoY at constant prices, 2012 – Q1/2018

![Graph showing growth of retail sales (excluding motor vehicles), YoY at constant prices, 2012 – Q1/2018.](savills.com.sg/research)
among e-retailers trying to reach a wider audience, but the model has since grown beyond online retailers to encompass established fashion labels as well as luxury brands. In general, pop-ups benefit both landlords and retailers. While the unique concept draws in crowds to malls, pop-ups also help to build buzz for brands. As the lease terms are often shorter, pop-up stores are a more cost-effective option to create physical presence in premier shopping belts like Orchard Road and Marina Bay Sands (MBS) where rents are on the high side.

Some luxury brands have realised that pop-up stores help to promote marketing campaigns in different seasonal launches and can constantly surprise customers with refreshing shopping experiences. Following the launch of Chanel’s pop-up store at MBS last year, Miu Miu opened a 1,205-sq ft disco-themed shop space at Paragon while Fendi brought in its Fendi Kiosk to ION Orchard in February.

City fringe and suburban
In contrast to footfall decline at some shopping centres along Orchard Road, suburban malls performed better, buoyed by factors such as convenience and proximity to captive markets in perimeter neighbourhoods. For instance, the newly-expanded Northpoint City enjoys high foot traffic due to its accessibility to the MRT station and bus interchange. After the completion of enhancement works, its occupancy rate improved further, from 70.9% to 81.2%.3

Set to be a new dining destination with an array of different cuisines, Northpoint City has allotted 100 out of 400 stores across six levels for F&B use. In addition to the two food courts - Bagus (South Wing) and Kopitiam (North Wing) - the mall also offers a specialty food street, “The Makan Town”, which occupies 40,000 sq ft in the South Wing’s basement level. Korean pizza chain, Pizza Maru, and Thai smoothie brand, Fruiturday, also opened their first stores in Singapore at Northpoint City.

In addition to a variety of F&B choices, activity-driven anchor tenants also help to drive footfall traffic in malls. Later this year, one of the top Japanese cooking schools, ABC Cooking Studio, will open its second studio at Westgate.

Rents and vacancy
From Q1/2015 to Q1/2018, island-wide retail stock expanded at a compounded annual growth rate (CAGR) of 0.8%, down from the 2.3% recorded for the period Q1/2012 to Q1/2015. Owing to a lack of substantial new retail supply in Q1/2018, the island-wide retail vacancy rate had a marginal increase of 0.1 of a ppt from last quarter to 7.5%. The slight increase in vacancies was led by the addition of 118,000 sq ft of net new stock as the occupied retail space remained unchanged in the quarter.

Although retail vacancies in some areas increased marginally, spaces in prime locations (stressed) within well-managed malls are still in high demand, leading to mild rental increases. According to the Urban Redevelopment Authority (URA), the retail rental index for Fringe Area went up by 0.3 of a ppt YoY, while Central Area (including Orchard Road) rose 0.2 of a ppt YoY in Q1/2018. After three consecutive years of quarterly decline, the rental index for Central Region inched up 0.1 of a ppt. Nonetheless, some landlords may be flexible on rents in order to maintain their targeted tenant mix. As such, Savills prime monthly rents in Orchard Road stayed flat at S$29.90 per sq ft in Q1/2018.

3 Excluding Yishun 10 retail podium.
The demand for suburban retail space remained relatively strong with a net take-up of 75,000 sq ft. Thus, the 0.2 of a ppt QoQ rise in the suburban vacancy level was due to the opening of new complexes such as Oasis Terraces, which comprises a five-storey retail podium with a retail basement. Even so, suburban malls, especially those owned by strong landlords, are still achieving healthy levels of occupancy and rent because of their steady shopper traffic and strong footfall. As a result, Savills prime monthly rents in the suburban area remained unchanged at S$28.80 per sq ft.

Future supply
According to URA’s data release, around 2.8 million sq ft of new retail supply will come online in 2018, substantially more than the 1.8 million sq ft of retail stock completed in 2017. Major completions on the horizon include Paya Lebar Quarter Mall, which is more than 40.0% pre-leased with anchor tenants such as FairPrice Finest supermarket, Kopitiam foodcourt and Shaw Theatres cinema. Other upcoming projects of note are refurbishments of existing malls like Century Square and TripleOne Somerset.

From 2019 to 2022, over 2.9 million sq ft of new retail supply is expected to enter the market. In 2019, Project Jewel and Funan will contribute the bulk of new supply. The other significant complex under construction comes from the retail segment of Punggol Digital District, and is a new mixed-use business cluster for digital and cyber-security industries. This development will open progressively from 2023.

### TABLE 1

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<th>Major projects in the pipeline, Q2/2018 – 2023</th>
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<tr>
<td>Development</td>
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<td>Paya Lebar Quarter</td>
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<tr>
<td>Additions/alterations to existing Raffles Hotel and shopping arcade</td>
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<tr>
<td>Additions/alterations to existing Century Square shopping complex</td>
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<tr>
<td>TripleOne Somerset Podium AEI</td>
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<tr>
<td>Funan</td>
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<tr>
<td>Punggol Digital District</td>
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Source: Company announcements, URA, Savills Research & Consultancy
*Savills estimation, based on an efficiency rate of between 70% and 75%.

OUTLOOK
The prospects for the market

According to the latest Monetary Policy Statement released by the Monetary Authority of Singapore (MAS), Singapore’s economic growth for 2018 is forecast to be slightly above the middle of the range of 1.5% and 3.5%. Even though this year’s May Day Rally cited the creation of new jobs along with an increase in average wages in 2018, consumers are likely to stay cautious in their spending. Firms are still retrenching in the face of continuing disruption due to technological innovation and on-going economic restructuring related to labour cost issues. As such, the rise in retail spending may not continue now that the Lunar New Year period has passed, especially if tourism spending eases.

Although the rate of recovery seems gradual, the retail rental market is showing signs of bottoming out. We believe that there are a couple of explanations for this. On the consumption side, as mentioned in last quarter’s briefing, disruptive or augmentative business models (for example food delivery companies that help boost F&B sales) are now paying good money to those who work for their networks. By injecting consumption power into the market with their cash burn models, these establishments have softened the impact of a weaker job market for new job seekers and those affected by structural unemployment. However, we do not believe that these new sources of employment can fully offset the issues arising from an ageing population, budget air travel and online retailing which dilute retail spending on a per sq ft basis.

On the physical real estate side, thus far, the opening of new or retrofitted malls in suburban areas often helps to boost rents in the short term. As the supply of reasonably sized shopping malls island-wide is restricted by government land sales - more so for those clustered around public transport points -
OUTLOOK

The prospects for the market

urban economics would have it that such malls would exhibit a gravitational pull for shopper traffic both within the immediate catchment area and also because of the site’s accessibility by MRT. With the constrained supply of malls in each subzone, very little primary data exists for retail and F&B brands to model the potential performance of their stores in an upcoming development. Therefore, retail and F&B brands face Hobson’s choice: stay out of the market or plant a flag in a newly minted retail complex, using it as a live test case and hoping that it remains cash flow positive. From a third party’s vantage point, the results from these live experiments will only be known three years down the road when leases come up for renewal and rents go up or down. Thus, for 2018, given that there are a number of new or retrofitted malls still to open, rents will likely be affected by these rollouts. Also, looking back to 2015, retail supply was quite moderate, with Waterway Point the only large mall to open that year. Feedback from the ground indicates that the 371,800-sq ft Waterway Point has performed exceptionally well, therefore, on a weighted basis, any negative drag from renewal rents at other projects can be more than offset by this mall.

The problems besetting retailers and F&B operators, such as labour costs, high rents, and competition from regional shopping destinations and online merchants, have not gone away. The fundamental weaknesses afflicting the retail industry have only been patched over due to the current factors shoring up consumption and the ongoing need for retailers to plant their flags in new malls. For 2018, we expect suburban rents for shops in prime locations to climb 2.0% to 5.0% YoY due to the “new” mall effect. For prime locations along Orchard Road, we expect rents to stay flat in spite of the lack of new supply.

<table>
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<tr>
<th>Development</th>
<th>Location</th>
<th>Estimated completion</th>
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<tbody>
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<td>Singapore Art Gallery</td>
<td>St. Andrew’s Road</td>
<td>2015</td>
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<tr>
<td>Hillion Mall</td>
<td>Jelebu Road</td>
<td>2015</td>
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<td>South Beach</td>
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<td>Waterway Point</td>
<td>Punggol Central</td>
<td>2015</td>
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<tr>
<td>One KM</td>
<td>Tanjong Katong Road</td>
<td>2015</td>
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