Briefing
Retail sector

March 2018

Image: Punggol Waterway Point

SUMMARY

The outlook for suburban retail market is improving due to high footfall and AEI efforts, while Orchard remains muted amid intense regional competition.

- Owing to selective spending patterns and competition from online promotions, quarterly retail sales (excluding motor vehicles) growth moderated from 2.4% year-on-year (YoY) in Q3/2017 to 1.3% YoY in Q4/2017.

- Supported by improvement in occupancy in the central and suburban areas, the island-wide retail vacancy level dropped 0.8 of a percentage point (ppt) quarter-on-quarter (QoQ) to 7.4% in Q4/2017.

- While prime monthly rents on Orchard Road stayed flat at S$29.90 per sq ft, those in the suburban area increased 2.1% YoY to S$28.80 per sq ft, due to higher rents fetched in newly renovated malls and those with high shopper traffic.

- We forecast that prime space in well-managed malls will post positive rental growth of 3.0% YoY in 2018.

"Although structural challenges continue to plague the market, prime space remains insulated." Alan Cheong, Savills Research

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Macroeconomic overview

The advanced estimates released by the Ministry of Trade and Industry (MTI) showed that the Singapore economy expanded by 3.6% YoY in Q4/2017, easing from the 5.5% growth in the preceding quarter. Even though the growth of the manufacturing sector eased from 19.1% YoY to 4.8% YoY in the fourth quarter, it remained the strongest growth area in the economy, leading overall economic growth. For the whole year of 2017, the local economy grew 3.6%.

In the advance release of the Labour Market Report for 2017 by the Manpower Research and Statistics Department, the job market continued to improve in Q4/2017 as economic conditions brightened. Unemployment rates declined 0.1 of a ppt to 2.1% in December 2017, lower than the preceding quarter and previous year. Owing to the pick-up in economic growth and restructuring of the economy, the real median gross monthly income of residents increased by 0.8% YoY in 2017. Further bolstered by increased arrivals from Indonesia and China, visitor numbers reached a record high of almost 4.4 million in Q4/2017, 9.8% more than a year ago.

Despite the improvements in tourism and labour sector, the growth in retail sales slowed from the preceding quarter. Retail sales (excluding motor vehicles)[1] in November were expected to surge because of the shopping events such as Singles' Day, Black Friday and Cyber Monday, as well as new mobile launches which took place in the month. Nevertheless, sales mildly increased by 3.8% YoY. This could be due to competition with the overseas and local online retailers during the sales event period. Consumers also seemed to be selective in their discretionary expenditure, curbing spending on items like watches and jewellery. As a result, the growth in quarterly retail sales (excluding motor vehicles)[2] moderated from 2.4% YoY in Q3/2017 to 1.3% YoY in Q4/2017. According to the Food & Beverage Services Index[3], consumers spent more at restaurants, fast food outlets and other eating places such as cafés in Q4/2017. However, the higher spending is likely because of the year-end festive season celebrations, rather than an improvement of the overall consumer sentiment.

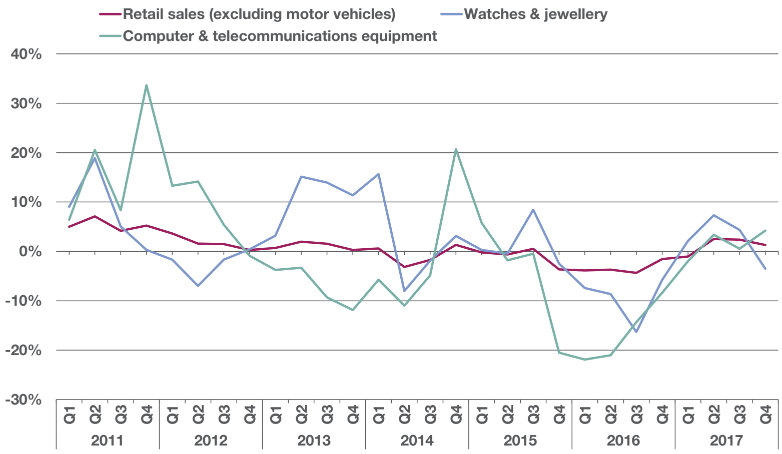
1 Retail Sales Index at Constant Prices (Seasonally Adjusted), Monthly. Updated as at 23 February 2018.

2 Retail Sales Index at Constant Prices, Quarterly. Updated as at 23 February 2018.

3 Sales Index of Food & Beverage Services at Constant Prices (Seasonally Adjusted), Monthly. Updated as at 12 February 2018.

GRAPH 1

Growth of retail sales (excluding motor vehicles), YoY at constant prices, 2011 – 2017



Source: Singapore Department of Statistics, Savills Research & Consultancy

Market snapshot

Some retail malls and retailers were trying to redesign their retail offerings to cater to a more discriminating consumer market, namely the millennials who were born between 1982 and 2004. According to a study conducted by research consultancy Accenture in 2016, millennials represent more than 45.0% of the population in Asia Pacific, with 60.0% of the millennials expected to stay in Asia by 2020. Moreover, millennials in Asia will have higher purchasing power than older generations, with an estimated disposable income of US$6.0 trillion (S$8.07 trillion) by 2020.

To engage this group of digital savvy consumers who are highly active and influential on social media, beauty and health retailer Watsons revamped its store in Bugis Junction with digital screens and multimedia platforms. JCube mall, which allows shorter leases of one to three years, regularly brings in different tenants with new retail concepts to keep the mall exciting for shoppers. One of its latest retail tenants, dessert cafe Fart Tartz, was given a prime central unit on the second floor because of its "garden-esque" store design which has the Instagram-worthy element, and appeals to a younger crowd. To keep up with evolving consumer trends, the mall also created a self-service zone, #PlayatJCube The Corner. Apart from e-stores, this is another alternative to leverage on technology to overcome high business costs and manpower-lean issues. Spanning across 968 sq ft and situated on level three, the new self-service lifestyle zone has 19 vending machines providing different dining, entertainment and shopping selections for extended operating hours. In November, a click-and-collect service was also launched in JCube mall to meet the evolving online shopping needs. It is a collaboration with Lazada in which shoppers can collect, try and return their purchases at a single station.

Orchard Road & the CBD

Singapore remained one of the top markets for overseas retail brands to expand into Southeast Asia. Japanese mall Lumine opened its first branch outside of Japan, taking up 10,000 sq ft of space at Clarke Quay Central, which the home-grown lifestyle store Naiise vacated in May 2017. It comprises a four-zone retail section and a café. As part of the expansion plans to Southeast Asia, the Japanese discount store Don Quijote (named Don Don Donki) has also opened its first store in Singapore in Orchard Central mall, occupying 15,037 sq ft across two levels.

Earlier in November, more Japanese food and beverage (F&B) players joined in the local retail scene. The sister brands of LeTao – Maple Mania and Tokyo Milk Cheese Factory, opened at ION Orchard and Raffles City Shopping Centre respectively. In the same month, a new Japanese drugstore Welcia-BHG also regarded Singapore as the main starting point to introduce the concept of drugstores in Southeast Asia. Taking up 2,700 sq ft on the ground floor of the BHG department store in Bugis Junction, the new store comes with a pharmacy and two zones for health and beauty.

While some overseas brands see Singapore as an ideal market to begin with, a German company Degussa GoldHandel suffered losses and shut its 1,000-sq ft store at Orchard, which also its first precious metals branch in Asia.

City Fringe & Suburban

To stay relevant in the challenging retail scene, some malls and retailers are recreating a different shopping experience to gain a competitive edge over their online competitors. The home electronics, IT and furniture retailer Courts Singapore invested S$10.0 million to refurbish all its local outlets, including the megastore in Tampines. After a two-month revamp, the flagship store, spanning over 136,000 sq ft, showcases new retail concepts and showroom areas. In order for consumers to have physical user experiences and visualise the presentation of the furniture, there is a new gallery area and design studio with furniture in an actual setting of a HDB flat. In addition, there is also a 'customisation zone' for consumers to do product personalisation based on their preferences.

As the trend of co-working spaces grows, landlords have discovered a new opportunity to explore different concepts while filling up their vacant spaces. The newly refurbished mall Katong Point brought in a new anchor tenant – creative co-working operator Mox, in October. Occupying 40,000 sq ft of co-making space across three floors, the ground floor provides retail space with "experiential retailing" while the second floor has workshop rooms for 3D printing, woodworking, leather crafting, photography and sewing. There is a co-working space on the third level, which can accommodate 200 users, offering flexible or permanent desks and private offices.

Rents & vacancy

After deteriorating for three quarters, the island-wide retail vacancy level dropped 0.8 of a ppt QoQ to 7.4% in Q4/2017, the lowest since Q1/2016. This was supported by the decline in vacancy levels in the central and suburban areas.

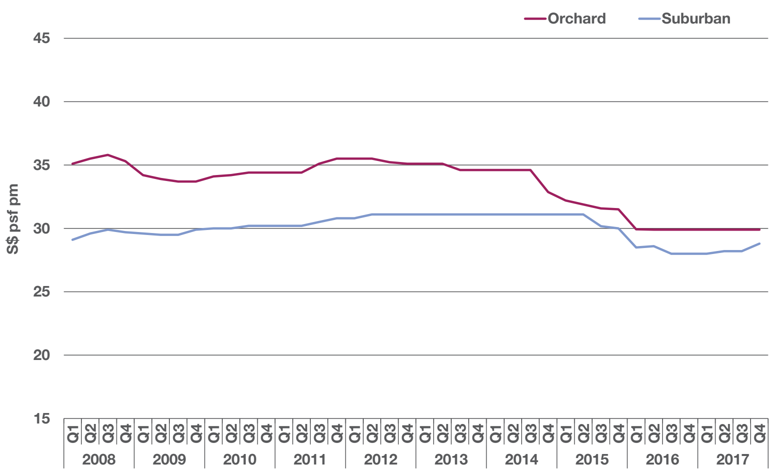
Bolstered by the healthy net take-up in the Downtown Core (97,000 sq ft) and Orchard Planning Area (86,000 sq ft), the vacancy level of the Central Region, comprising both planning areas, declined by 0.8 of a ppt QoQ to 7.9%. However, the rents in Central Region did not record the same rise. According to the Urban Redevelopment Authority (URA), the retail rental index for Central Region dipped 0.8 of a ppt QoQ in Q4/2017.

This was likely dragged by down by the competition from regional cities such as Bangkok and Hong Kong which aim for a slice of the tourist dollars. Even though tourist arrivals increased in Q4/2017, the decline in tourism receipts for F&B and shopping in Q3/2017 could have extended to Q4/2017. As the performance on Orchard Road is largely dependent on tourism arrivals and spending, the overall Orchard rental market stayed soft in Q4/2017. Nonetheless, Orchard prime rents on ground floor with high shopper traffic remained resilient. The Savills prime monthly rents in Orchard Road stayed the same at S$29.90 per sq ft for the sixth consecutive quarter in Q4/2017.

The suburban (Outside Central Region) rental market continued to fare well.

GRAPH 2

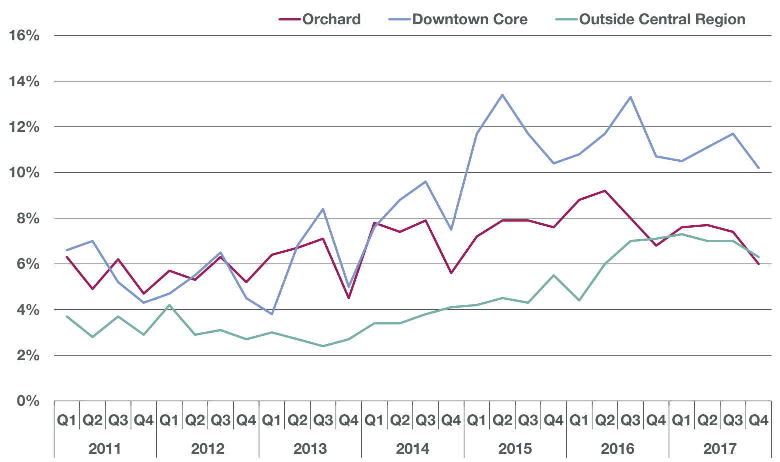
Prime retail rents, 2008 – 2017



Source: Savills Research & Consultancy

GRAPH 3

Vacancy rate, 2011 – 2017



Source: URA, Savills Research & Consultancy

Owing to the healthy take-up at the newly renovated Northpoint City, the suburban net absorption of 280,000 sq ft far exceeds the net new supply of 140,000 sq ft. As such, the suburban vacancy level decreased 0.7 ppt QoQ to 6.3% in Q4/2017. In conjunction with the improving occupancy rate, the Savills prime monthly rental measure for the suburban area increased 2.1% YoY to S$28.80 per sq ft, the highest record since 2015. This could be due to the suburban malls which transacted at high rents because of their consistent footfall and more complete tenant mix, especially Northpoint City which can command for a higher rent after the completion of Asset Enhancement Initiatives (AEI) works. Furthermore, as there are F&B tenants that take up fairly small lot sizes, the rents are usually fetch a higher rent. As a result, the average rent could be driven up by the over 100 F&B stores which took up almost 30.0% of the retail mix at Northpoint City.

TABLE 1

Major projects in the pipeline, 2018 – 2020

Development	Location	Estimated NLA (sq ft)	Estimated completion
Paya Lebar Quarter	Paya Lebar Road/Sims Avenue	340,000	2018
Additions/alterations to existing Raffles Hotel and shopping arcade	Beach Road/North Bridge Road	234,000*	2018
Additions/alterations to existing Century Square shopping complex	Tampines Central 5	200,000	2018
TripleOne Somerset Podium AEI	Somerset Road	88,500	2018/2019
Project Jewel	Airport Boulevard	576,000	2019
Funan	North Bridge Road	324,000	2019
Northshore Plaza I	Northshore Drive	67,000*	2020

Source: Company announcements, URA, Savills Research & Consultancy
*Savills estimation, based on an efficiency rate of between 70% and 75%.

Future supply

URA estimates about 3.0 million sq ft of new retail space to be completed in 2018. Other than Century Square shopping complex which is closed for a one-year makeover, there is no significant upcoming retail supply in the suburban area. The other new projects include the development of Paya Lebar Quarter, and refurbishment of existing buildings such as Raffles Hotel and shopping arcade as well as TripleOne Somerset.

From 2019 to 2022, over 2.7 million sq ft of new retail stock is expected to enter the market. The major upcoming projects in 2019 include the development of Project Jewel and revamp of Funan. The Woodleigh Mall, the commercial component of Woodleigh Residences in the new Bidadari Estate, is slated to complete in 2022.

OUTLOOK

The prospects for the market

Following a strong economic turnaround over the past year, MTI expects a stable but slower economic expansion in 2018. The Singapore economy is projected to expand slightly above the mid of the range of 1.5% to 3.5%. According to the Monetary Authority of Singapore (MAS) in the recent annual review of financial stability, there is unlikely to be substantial increase in wages though the overall employment outlook is set to improve in 2018. Furthermore, the labor market is still facing challenges in job skills mismatch due to on-going economic restructuring. These could imply that consumers' spending habits may be conservative this year.

Whilst the Savills prime retail rents are stable for Orchard Road, the URA's numbers for the Orchard Planning area have slide in Q4/2017. This divergence in performance is due to the differences in compiling rents. Savills only account for prime ground floor rents for top grade malls while the URA statistics are for general retail rents in the area. Therefore, while the rents for prime Orchard location are holding up, they belie the fact that retailers and F&B operators there may not on the whole be fairing that well.

The continuing decline in retail rents and prices is not surprising. On the rental front, the decline is due to landlords' combative action to keep their malls and shops occupied and this they have done so when we see vacancy levels fall significantly from 8.2% in Q3/2017 to 7.4% in Q4/2017. Although the vacancy rate for the Orchard Planning Area fell sharply from 7.4% in Q3/2017 to 6.0% in Q4/2017 while that of the Outside Central Region (OCR) fell from 7.0% to 6.3% over the similar period, the median rents for Orchard Road rents fell 11.0% QoQ, whilst those in the latter rose significantly by 15.4%. It is noteworthy that on a QoQ basis, retail rents for the

OUTLOOK

The prospects for the market

OCR rose across the discrete spectrum of rental measures the URA provided, from the minimum to the maximum. However, for the Orchard Planning Area, QoQ rental growth was negative across the discrete spectrum.

An explanation for this is that because the takings for shops and F&B outlets in Orchard Road tend to have a higher percentage of tourist dollars, the shopping belt is facing competition for the tourist dollar from regional cities like Bangkok and Hong Kong. For the suburban market, the captive market are those of the domestic spending dollar which in the period 2014 to 2016 was deteriorating. However, with disruptive business models burning a great amount of cash to hand to those who had previously been made structurally irrelevant and had signed on to work for these businesses, the drop in spending power had not only been arrested but reversed.

From July 1 2018, the imposition of an additional S$13.30 in airport departure charges is still unlikely to act as a deterrent to locals flying to regional cities for short holidays or for the weekends, thus siphoning consumption expenditures from the retail and F&B outfits here.

For 2018, we forecast rents from the Savills basket of prime (stressed) retail space to rise 0.0% to 3.0% in general with the suburban market rising marginally but Orchard Road rents staying flat. Although broader structural issues confront the retail and overprovided F&B market, the demand for prime locations in well-managed malls with heavy footfalls is unlikely to abate.

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