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Savills World Research
Singapore

Briefing
Retail sector

November 2016

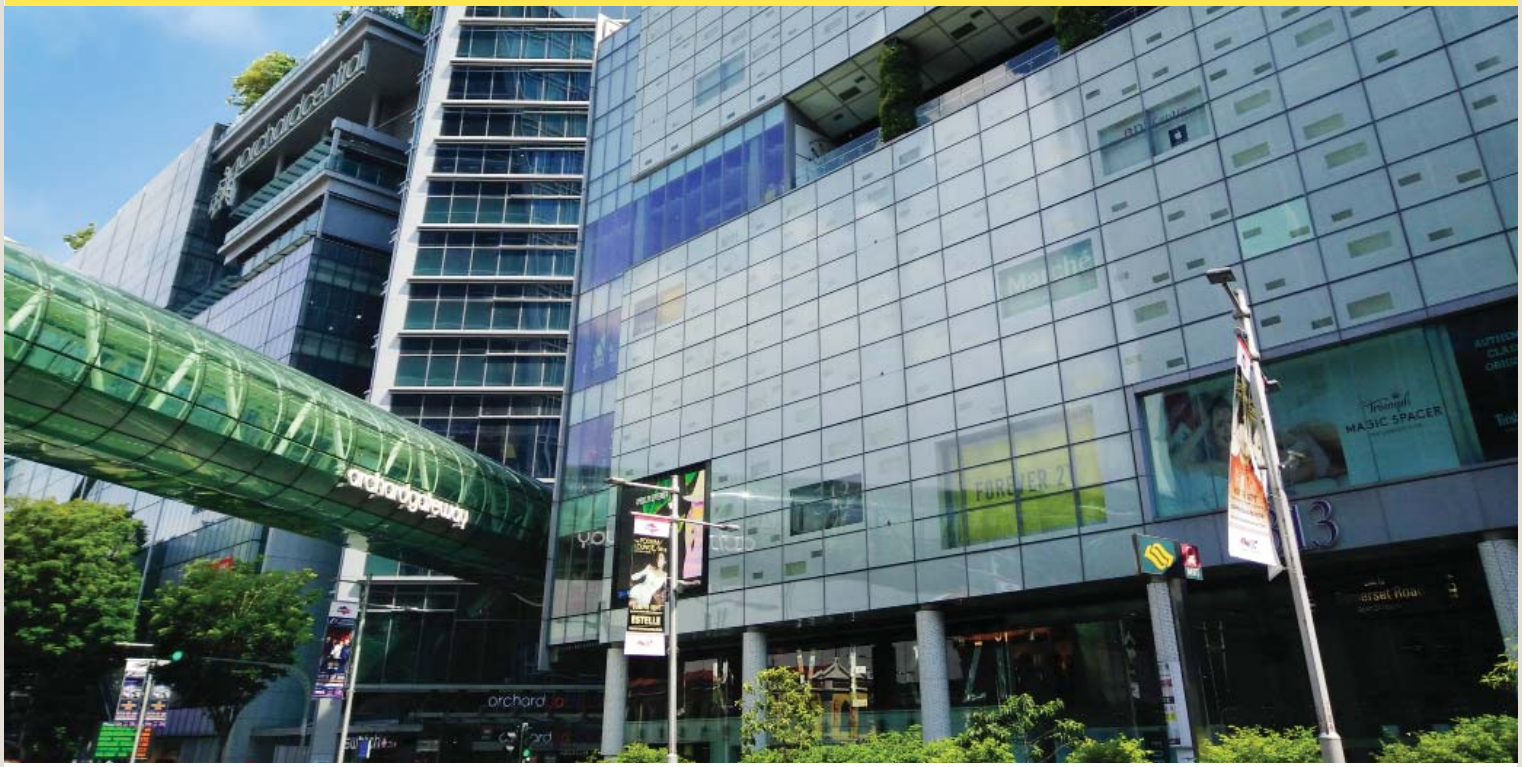

Image: Orchard Somerset, Orchard Road

SUMMARY

The main cause for the weak retail environment is the slowing of the economy and slack in the labour market, which in turn is having an impact on consumers' purchasing power and buying sentiment.

- After a 2.7% year-on-year (YoY) dip in July, retail sales (excluding motor vehicles) fell at a sharper rate of 7.3% YoY in August.

- Prime monthly rents on Orchard Road held firm at S$29.90 per sq ft from the preceding quarter, while suburban monthly rents slid 2.0% quarter-on-quarter (QoQ) to S$28.00 per sq ft in Q3/2016.

- In Q3/2016, island-wide vacancies reached a new record high of 8.4%, from 7.8% in the last quarter. The vacancies in the Downtown Core planning area rose by 1.6 percentage points (ppts) QoQ to 13.3%, more than the 1.0 ppt for the suburban areas which now have vacancies of 7%. Surprisingly, Orchard vacancy levels dipped 1.2 ppts QoQ to 8% in Q3/2016, making this the lowest this year.

- Even though e-retailing has been putting pressure on brick-and-mortar retail, it only accounts partly for the ailing retail market, as the slowing economy and slack in the labour market supressed purchasing power.

"Although retailers in general are afflicted with economic maladies, those still thriving will continue to expand and acquisitive interest in malls remains high."
Alan Cheong, Savills Research

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Macroeconomic overview

Based on the advanced estimates released by the Ministry of Trade and Industry (MTI), the Singapore economy expanded 0.6% (YoY in Q3/2016, making the quarter record the slowest growth since the global financial crisis for the period 2008 to 2009. The impact of the slowing economy on the job market continues to drag down consumer sentiments.

As the economy loses speed and slack within the labour market emerges, the penchant to spend by locals is reduced. After a 2.7% YoY dip in July, retail sales (excluding motor vehicles) fell at a sharper rate of 7.3% YoY in August. This marks a full year of decline in retail sales since the last increase in August 2015. Following a steep fall at 11.1% YoY in July, the food & beverage (F&B) segment slipped 10.9% YoY in August. This makes a full two years of negative YoY F&B sales growth. Likewise, for the watches and jewellery sector, the pace of decline doubled to 15.5% and 21.8% YoY in July and August, respectively.

The figures on retail spending coincide with the dip in tourist arrivals, which in August registered an influx of 1.5 million after a 6.8% YoY rise in July to 1.6 million. The drop was mainly driven by the fall in tourists travelling from Indonesia, Malaysia and Australia.

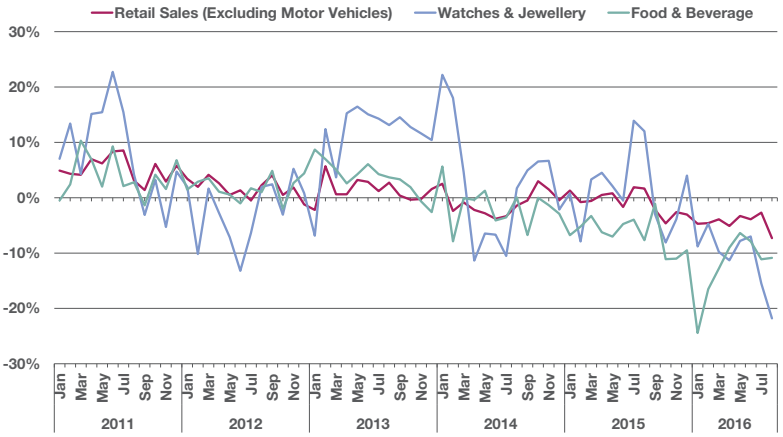
Market snapshot

Based on the MasterCard Index of Consumer Confidence, between June and July 2016, consumer confidence on the prospects of a regular income, employment and economy dived 12, 11 and 9.9 ppts respectively, reflecting the overall pessimism in the local economy, business sector and employment market for the year.

In the light of the gloomy economic outlook, where consumers tighten their belts and business costs increase, businesses continue to wind up, leaving malls vacant. Even the once-trendy gym chain, California Fitness, was forced to exit the market. Shortly after the abrupt closure of its Novena and Bugis outlets, the gym chain closed its last branch at Raffles Place in July due to cash flow issues.

GRAPH 1

Growth of retail sales (excluding motor vehicles), YoY at constant prices, Jan 2011–Aug 2016



Source: Singapore Department of Statistics, Savills Research & Consultancy

Notwithstanding the tough retail climate, in the third quarter, some retailers were still aggressive in their expansion plans. In July, the Japanese lifestyle brand Muji unveiled its tenth local outlet, together with its second Café&Meal Muji in Singapore at Raffles City. Spanning over 10,600 sq ft, the new Muji store houses the 70-seater café which introduces new items on the menu to differentiate from the first outlet at Paragon. In September, Muji reopened its store at ION Orchard after its closure for renovation in August. Besides having a complete new look, the new 9,300-sq ft store offers customised offerings such as exclusive merchandise, interior consultation services and workshops. Prior to its reopening, Muji kept shoppers engaged with a pop-up store right outside its renovating store at ION Orchard.

Other than the established retailers, softened rents have also given humble and start-up brands opportunities to open up in prime malls. Previously located at Defu, Seafood Paradise moved to Marina Bay Sands in September, taking up the space at level two which was formerly occupied by a Spanish restaurant, Santi, and Chinese restaurant, Beijing No. 1.

Orchard Road & the CBD

The retail landscape in the Orchard area is slowly changing, with the increasing appearance of local fashion brands. The home-grown womenswear label, Beyond The Vines, moved from a pop-up store to a 650-sq ft unit at Mandarin Gallery in June. In July, the local jewellery designer, Choo Yilin, also opened her 1,000-sq ft boutique at Mandarin Gallery, the second outlet after the first at Joo Chiat. K+, a multi-concept shop by Kinetic Singapore, carrying six local brands, has upgraded to a 4,300-sq ft permanent shop from a pop-up store in Scotts Square. The local womenswear brand Yacht 21 also expanded to another 1,000-sq ft multi- label travel-lifestyle-themed store at Plaza Singapura and a 420-sq ft shop at Wheelock Place in September and October respectively.

International brands also took the opportunity to take up larger spaces in Singapore, consolidating both regional and local operations. In July, HP Singapore announced the opening of its 1,500-sq ft flagship store at Marina Square. Japanese retailer Uniqlo also unveiled its first global flagship store in Southeast Asia in September. Located at Orchard Central, the store has 29,000 sq ft of shopping space across three levels. In mid-September, Michael Kors opened a two-storey flagship store, spanning 6,957 sq ft at Mandarin Gallery.

There were also brands which tapped into the softer rental market to establish their presence in a high-footfall district. In August, both the American label Marc Jacobs and a United States streetwear brand, Off-White, welcomed their new stores at The Paragon and 268 Orchard Road respectively. Later that month, British designer Anya Hindmarch inaugurated her first standalone store in Singapore, occupying a 538-sq ft unit at the Takashimaya Department Store along Orchard Road.

Besides new stores opening, the French multi-brand beauty retail chain Sephora also opened its relocated flagship store at ION Orchard basement two in July. Even though the new 10,000-sq ft flagship store is smaller than the previous 14,500-sq ft store on the ground floor, its refurbished layout and additional experiential retail elements nevertheless saw overwhelming customer response.

The F&B players were also relatively active in the third quarter. In July, Japan Food Town opened its first store in Wisma Atria. After a revamp, British clothing and food retailer Marks and Spencer reopened its new 30,000-sq ft flagship store at Wheelock Place in September, which also comprises a 60-seat café near its Food Hall. Instead of increasing footfall with more F&B choices, landlords also introduced more lifestyle and entertainment aspects to keep malls occupied. GuavaLabs established a 2,000-sq ft fitness studio at Mandarin Gallery in July, while a karaoke chain, Ganso Manekineko, expanded its seventh outlet in August, a new 23,874-sq ft flagship branch at Orchard Cineleisure.

City Fringe & Suburban

As Singapore's retail scene continues to face headwinds, even strategically located suburban malls which used to stay resilient in the sluggish retail climate, find restoration and new elements necessary to attract shoppers. At the end of the third quarter, Sengkang's Compass One mall officially reopened after 11 months of upgrading works. Since the main catchment of the area – young families – tend to dine out more frequently, the refurbished mall has raised the F&B component to 33.0% from 20.0%.

Funan DigitaLife Mall, which was closed for redevelopment at the end of June, was also rebranded as a lifestyle destination, renamed Funan. Besides offering online-to-offline services, the new mall will be introducing sports amenities like a climbing wall, an experimental space and a cinema which will be Singapore's first multi-dimensional cinematic experience.

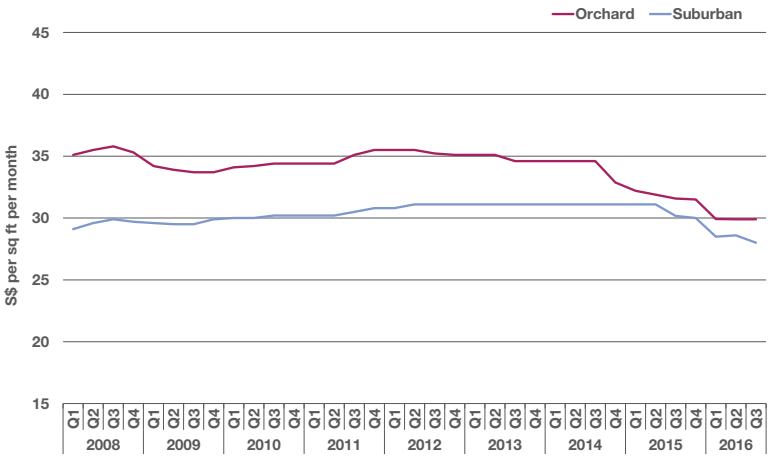
Following the closure of Funan DigitaLife Mall, Park Mall also shut down in September, for a commercial redevelopment project comprising two office towers and an ancillary retail component. As a result of the mall's closure, tenants such as Kith Café and the furniture retailer Xtra have relocated to Marina Square, sharing a 13,000-sq ft unit. The Bear Knows has also moved to a 2,500-sq ft store at The Centrepoint in Orchard Road.

Rents & vacancy

Despite the economic uncertainty and poor consumer sentiments, surprisingly for Q3/2016, prime

GRAPH 2

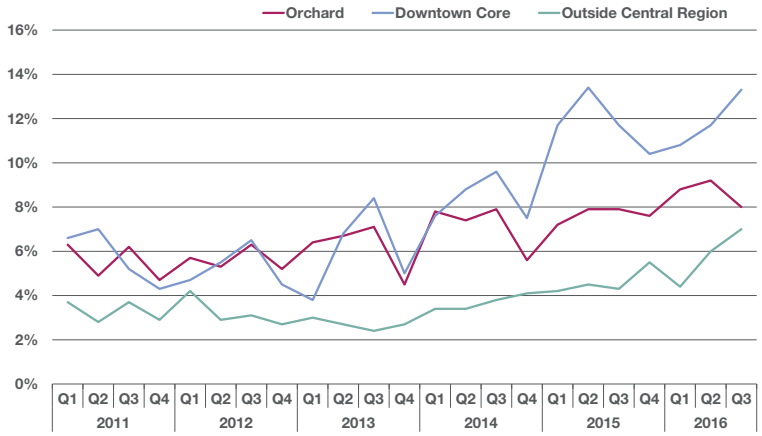
Prime retail rents, 2008–Q3/2016



Source: Savills Research & Consultancy

GRAPH 3

Vacancy rate, 2011–Q3/2016



Source: Urban Redevelopment Authority (URA), Savills Research & Consultancy

TABLE 1

Major projects in the pipeline, Q4/2016–2020

Development	Location	Estimated NLA (sq ft)	Estimated completion
Downtown Gallery	Shenton Way	160,000	2016
Singapore Post Centre AEI	Eunos Road 8	269,100	2017
Hillion Mall	Jelebu Road	152,500	2017
Marina One (The Heart)	Marina Way/Straits View	140,000	2017
Paya Lebar Quarter	Paya Lebar Road/Sims Avenue	340,000	2018
Northpoint City	Yishun Central 1	315,250*	2018
TripleOne Somerset Podium AEI	Somerset Road	88,500*	2018/2019
Jewel Changi Airport	Airport Boulevard	576,000	2019
Funan	North Bridge Road	324,000	2019

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

monthly rents on Orchard Road held firm at S$29.90 per sq ft. This could be due to the influx in the past three months of new tenants to the Orchard shopping district, thereby helping to support the demand for Orchard retail spaces. Moreover, there was no new retail supply in the Orchard Road area for the quarter. On the other hand, suburban monthly rents slid 2.0% QoQ to S$28.00 per sq ft in Q3/2016, on the back of the subdued economic condition, concerns among consumers, and a general weakening of the retail scene. The rents for suburban malls were also likely to be dampened by the additional 431,000 sq ft of new retail stock in the quarter.

For the whole of Q3/2016, with the exception of the Orchard planning area, retail vacancy levels continued to increase. This is due to a confluence of factors, including the lack of new retail supply and sustained demand for Orchard retail spaces. Consequently, the vacancy level there dipped 1.2 ppts QoQ to 8%, the lowest this year. However, the vacancy levels in other areas have risen and are more than enough to offset the improvement in Orchard vacancies, leading to a full-year rise in island-wide vacancies to 8.4% in Q3/2016, from 7.8% in the last quarter. The third quarter's island-wide vacancy rate is a record high from the Urban Redevelopment Authority's (URA) latest data time series that was constituted in 2011. Similarly, in the Downtown Core planning area, vacancy rates rose at a higher rate of 1.6 ppts QoQ to 13.3%, almost reaching the peak of 13.4% from the second quarter last year. Suburban vacancies have also gone up by 1.0 ppt QoQ to 7% in Q3/2016, reaching the highest vacancy level in terms of URA's time series on this dataset.

Future supply

According to the latest data released by URA as of Q3/2016, there will be an estimated retail supply of 667,000 sq ft in the last quarter this year. The upcoming retail supply for the year is mainly from the new mixed-use developments in the Central planning region. The main bulk of the supply comes from two new integrated projects, namely Downtown Gallery and Tanjong Pagar Centre. The remaining supply comes from the refurbished GSH Plaza, as well as the revamped Beach Centre.

From 2017 to 2020, approximately 6.2 million sq ft of new retail space is expected to enter the physical stock. Similarly, in 2017, the new supply largely involves integrated projects in the Central planning region. The major developments consist of the new retail mall at Singapore Post Centre and The Heart at Marina One. Hillion Mall in the Bukit Panjang planning area is the only significant development in 2017 that is not located within the Central planning region. Subsequently, in 2018, the major projects are also mixed developments, such as Paya Lebar Quarter and Northpoint City. Apart from the existing podium of TripleOne Somerset, which is embarking on Asset Enhancement Initiatives (AEI), there is no planned major retail supply in the Orchard planning area in the near term.

OUTLOOK

The prospects for the market

A survey conducted by HSBC revealed that 57% of Singaporeans made online purchases in August, making Singapore the ninth largest online retail market in the world on a per capita basis, and the largest in Southeast Asia. By 2020, MTI aims to expand the local e-commerce market from the current 3.0% to 10.0%.

In line with Minister for Trade and Industry S Iswaran's call for retailers to adopt online channels as well as mobile applications to engage shoppers, more retailers are integrating e-commerce with their existing conventional channels. Nevertheless, physical stores are likely to remain as one of the crucial aspects for retailers. Traditional retailers like Courts have been investing in their web store, but they are also concurrently evolving their retail store into experiential spaces for shoppers to try out gadgets, seek assistance or collect their online orders.
While the market has been ascribing the ills of retailing to competition from online retailers and oversupply of retail space, we believe that this is only a partial answer. We believe that there are other factors and in 2016, what has been the major drag on the industry is our slow-moving economy. Together with the slack emerging in the labour market, the impact on household disposable income is more acute than in a normal economic downturn. This lack of purchasing power gels with the feedback from tenants, not only those from general retailing, but also from some F&B operators.

In the third quarter, the substantial decline of 2.0% QoQ in suburban mall rents contrasts sharply to those along Orchard Road. If, for another quarter or two, rents in the latter area continue to perform relatively better than the former, it will debunk the myth that many have subscribed to, namely suburban malls are more resilient to the downturn given that they have a captive market in the heartlands. Moving forward, another factor will increase its influence on retailing here; that of budget air travel which makes regional cities with a lower retailing cost base more accessible not only to us but to our tourism exporting countries as well. In such a situation, the sale of comparison goods, those that one buys infrequently, will be negatively impacted.

Thus far, we have only broached the revenue side of the retailing and F&B industry. On the cost side, the obsessive drive towards labour productivity is also driving up cost without a commensurate increase in productivity and service levels.

Will all this impact capital values of shopping malls? Unlikely. This is because at about 4.0%, the capitalisation rate for malls is still at a premium to those of offices. On top of that, although retailers may be afflicted by the economic slowdown, many of the better-run malls are still almost fully-tenanted. Even if passing rents were to soften, the low interest environment would still drive investor demand towards this relatively high yielding asset class. For rents, we expect gross asking rents for both prime Orchard Road and Suburban malls to soften equally, by 7.5 to 10.0% in 2017 on a YoY basis.

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