Singapore - January 2024

MARKET IN MINUTES

Savills Research

Office

Office rents rose 1.1% in 2023

As a result of the economic uncertainties and the continued malaise facing the tech/social media industries, it has become more difficult to identify the demand drivers of the office leasing market.

- In 2023, office leasing activity was the result of tenants renewing leases, with no significant take-up of additional space. Nevertheless, while Grade A and AA offices will come under pressure, demand for Grade AAA offices is expected to remain strong.

- The office investment market rebounded with three block transactions amounting to S$1.31 billion in Q4/2023, the highest since Q2/2022 when office block transactions reached nearly S$1.81 billion. Office strata investment value fell significantly due to lower deal sizes.

- Based on data compiled by Savills, the vacancy rate of CBD Grade A offices dipped 0.4 of a percentage point (ppt) QoQ to 6.7% in Q4/2023. For the whole of 2023, the vacancy rate of overall CBD Grade A offices rose 1.1 ppts.

- Although vacancy levels have risen, however, it is still considered a tight market. With major leases only expiring in 2025, the market could still take on the large pipeline of new supply this year without major rental dislocation. Thus, the average monthly rent of CBD Grade A offices in Savills basket still managed to inch up for an eighth consecutive quarter by 0.1% QoQ to S$9.65 per sq ft in Q4/2023. For the whole of 2023, rents rose 1.1%, a smaller growth compared to the 2.2% in 2022.

- We do not expect rents for CBD Grade AAA stock to change in 2024. Any rental adjustments may however come from buildings whose vacancy rates surpass 5% or some of the Grade A and AA buildings. However, the drop is likely to be mild. Overall, we believe that rents for the overall CBD Grade A offices may adjust down 2-3% YoY in 2024.

"Although economic headwinds may continue blowing in 2024, major leases are not due to expire until 2025 and this could lend resilience to rents this year."

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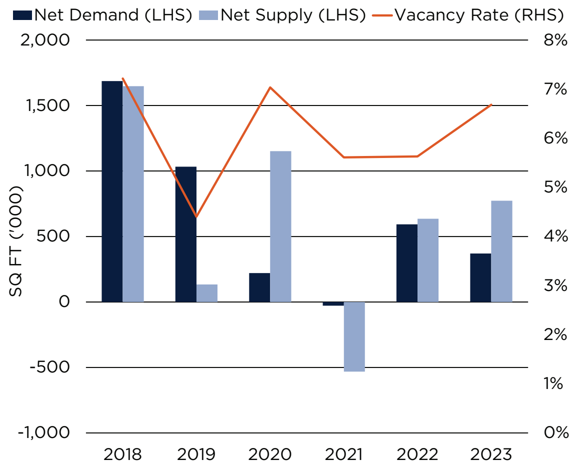
GRAPH 1: Net Demand, Net Supply and Vacancy Rate of CBD Grade A Offices, 2018 to 2023



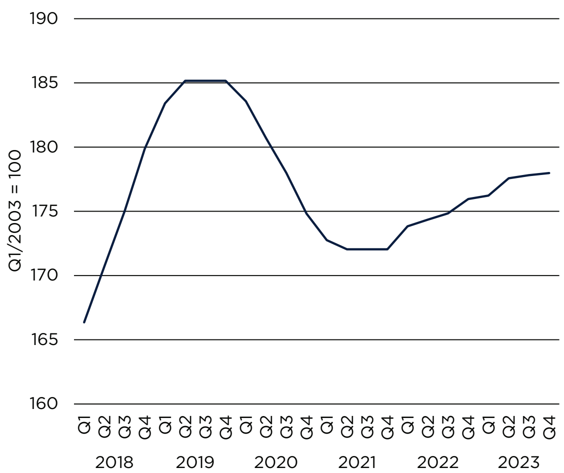
Source Savills Research & Consultancy

TABLE 1: Micro-market Grade A Office Rents and Vacancy Rates, Q4/2023

LOCATION	MONTHLY RENT (S$ PER SQ FT)	VACANCY RATE (%)
Marina Bay	12.65	4.8%
Raffles Place	9.98	7.1%
Shenton Way	8.94	8.2%
Tanjong Pagar	8.50	10.8%
City Hall	10.10	7.2%
Orchard Road	8.98	2.4%
Beach Road/ Middle Road	8.00	7.9%

Source Savills Research & Consultancy

GRAPH 2: Rental Indices of CBD Grade A Offices, Q1/2018 to Q4/2023



Source Savills Research & Consultancy

MARKET COMMENTARY

According to the advance estimates provided by the Ministry of Trade and Industry (MTI), Singapore's economy grew 2.8% YoY in Q4/2023, a faster pace than the 1.0% in Q3/2023. On a QoQ seasonally adjusted basis, the Singapore economy expanded by 1.7%, extending the 1.3% growth in the previous quarter. As such, for the whole of 2023, the economy grew by 1.2%, slowing from 3.6% in 2022. In the manufacturing sector, we saw a turnaround after four consecutive quarters of YoY declines with a 3.2% YoY growth in the last quarter of 2023. This was brought about by output expansions almost across all clusters, with the exception of the precision engineering cluster. In addition, the construction and services sectors continued their upward trend, increasing 9.1% and 2.4% YoY respectively. Among the services sectors, the group of sectors consisting of information & communications, finance & insurance and professional services registered the largest growth of 3.9% YoY, extending the 2.5% growth in Q3/2023. All sectors within the group expanded. Growth in the information & communications sector was led by the IT & information services segment, while that in the professional services sector was brought about by the other professional, scientific & technical services segment. The finance & insurance sector was mainly supported by activities ancillary to financial services, such as payment processing activities.

Owing to economic uncertainties which made it difficult to identify significant demand drivers to take up large amounts of space, the office leasing market remained lacklustre. Tech and social media companies, previously the mainstay of new office demand, continued to experience difficulties with layoffs blighting the industry. Without major tenants taking up additional space and a lack of fit-out budgets, the leasing market is likely to be mainly dominated by tenants renewing leases. A significant movement of tenants is likely to be seen only when the leases of major space occupiers come due in 2025. However, pressure is expected to be felt by landlords in 2024, particularly in the second half of the year. By then, the market will experience the completion of new buildings and vacancy rates are expected to increase. The largest development coming online in 2024 is IOI Central Boulevard Towers (NLA of 1.26 million sq ft) in H1/2024. Nevertheless, any rental pressure is likely to be felt in the Grade A and AA offices as demand for top premium space (Grade AAA offices), remains strong.

On the investment sales front, after the lack of block transactions in Q3/2023, Q4/2023 saw three such transactions totalling S$1.31 billion, the highest since Q2/2022 when office block transactions amounted to nearly S$1.81 billion. The largest of the three was the collective sale of Shenton House, which was sold to Shenton 101 Pte Ltd, a company owned by Lee Yeow Seng, group chief executive officer of IOI Properties, for S$538 million. After accounting for land betterment charges and a lease top-up premium to a fresh 99-year lease, the land rate was estimated to be around S$1,885 psf ppr. The two other block transactions included the sale of VisionCrest Commercial from the property unit of German asset manager Union Investment to a joint venture of Metro Holdings, TE Capital Partners and LaSalle Investment for S$426.9 million (S$2,853 psf), as well as Keppel-managed fund's acquisition of the office and retail components of Wilkie Edge for S$348 million (S$2,211 psf) from a joint venture between Lian Beng Group and Apricot Capital. Strata sales of office units were almost like the previous quarter. In Q4/2023, there were five transactions of strata office units, but the total quantum fell significantly from S$166.9 million to S$84.7 million due to the lower deal size. The largest strata transaction concluded in Q4/2023 was the sale of two units at Suntec Tower Three for S$36.2 million, or S$3,513 psf.

DEMAND AND VACANCY

From data compiled by Savills, the vacancy rate of CBD Grade A offices fell marginally by 0.4 of a ppt to 6.7% in Q4/2023. On a YoY basis, the vacancy rate of overall CBD Grade A offices rose 1.1 ppts. Quarterly declines in vacancy rates were observed across all gradings, particularly for Grade AA buildings, which fell 0.6 of a ppt to 5.5% in the quarter. This was the third consecutive quarter of decrease. After four consecutive quarters of increases, the vacancy rate of Grade AAA and A offices contracted by 0.2 of a ppt and 0.5 of a ppt to 7.0% and 7.7% respectively in Q4/2023. For the whole of 2023, only Grade AA buildings recorded a YoY decline in vacancy rates of 0.2 of a ppt, while Grade AAA and A buildings rose by 2.7 ppts and 0.9 of a ppt respectively. The increase for the latter grades was due to the inclusion of newly completed buildings such as Guoco Midtown and Hub Synergy Point as well as a YoY rise in shadow space. Net demand for CBD Grade A offices remained positive for a second consecutive year in 2023, albeit at a slower rate of 370,000 sq ft compared to 593,000 sq ft in 2022. The rise came about mainly in 2H/2023.

By location, quarterly declines in vacancy rates outweighed the increases in vacancy rates. Decreases in vacancy rates were registered for City Hall, Shenton Way, Tanjong Pagar and Beach Road/Middle Road. Of these, the largest contraction in vacancy rate was observed in City Hall, falling 2.2 ppts to 7.2% in Q4/2023 after a surge in vacancy in the previous quarter. The fall in the vacancy rate for the area was due to more tenants moving in to the newly completed Guoco Midtown. On the other hand, vacancy rates in Marina Bay and Orchard Road rose 0.6 of a ppt and 1.3 ppts to 4.8% and 2.4% respectively in the quarter.

On a YoY basis, the vacancy rates across almost all micro-markets recorded increases. The exception was Shenton Way, where it fell 1.1 ppts after an increase of 0.7 ppts for the whole of 2022. On the opposite end of the spectrum, the largest growth in vacancy rate was observed in Tanjong Pagar, increasing 4.1 ppts for the whole of 2023, a reversal from the 2.7 ppts decline in 2022.

RENTS

Although the economy faced strong headwinds in 2023, the office market remained relatively tight (as new buildings have yet to be completed and major leases will only expire in 2025). Consequently, a marginal rental increase was observed for CBD Grade A offices in the last quarter of 2023. The average monthly rents of CBD Grade A offices in Savills basket rose for an eighth consecutive quarter by 0.1% QoQ to S$9.65 psf in Q4/2023. For the whole of 2023, rents rose 1.1%, slowing from the 2.2% growth in 2022. Nevertheless, this was still the second consecutive year of increase.

Across the grades, only Grade A office rents in the CBD registered a quarterly increase in the quarter, by 0.2% to S$8.56 psf. On the other hand, rents of offices of the higher grades (Grades AA and AAA) remained unchanged at S$10.53 and S$12.70 per sq ft in the quarter. This came after nine and seven consecutive quarters of increase for the Grades AA and AAA offices respectively. Nonetheless, on a YoY basis, office rents across all grades rose, particularly for Grade AAA buildings, increasing 1.7% for the whole of 2023. Rents of Grade AA and A offices rose by 0.9% and 1.2% respectively. However, compared to 2022, the rental increment has slowed.

By micro-market, only rents of Grade A offices in Raffles Place and Orchard Road rose in Q4/2023, by 0.1% and 0.7% QoQ respectively. For offices in Orchard Road, the quarterly increase came after nine consecutive quarters of no rental movement. This was led by higher rents at Wisma Atria and Ngee Ann City. Rents of Grade A offices in Shenton Way, Tanjong Pagar, City Hall and Beach Road/Middle Road remained unchanged in the quarter. On the other hand, rents of Grade A offices in Marina Bay declined for the first time by 0.2% QoQ since Q4/2021. On a YoY basis, Grade A office rents across all micro-markets recorded increases except for Tanjong Pagar with the rents holding constant. The largest YoY growth was from Raffles Place and Beach Road/Middle Road, which rose 2.3% for the whole of 2023.

OUTLOOK

This year will see more tenants, whose leases are due in 2025, begin their search for renewal options. The momentum of this is expected to gather steam as the year progresses. Therefore, the activity level of lease negotiations will not be felt in Q4/2023 and the first few months of 2024. With no new completions in the CBD Grade A space until the end of Q1/2024, the market will remain quiet until pressure builds from an increasing number of tenants negotiating for better rates, right sizing or opting to move to another building.

Given the malaise affecting many economic sectors, affected tenants, whose leases are coming due usually do not have large fit-out budgets. With these constraints, such tenants are likely to renew their leases and/or right size their premises. The prospects of rightsizing however does not necessarily come at the time of lease expiry. With this comes the possibility that shadow space may start increasing in 2024. Nevertheless, as the main tenant is still paying rent, should a replacement tenant be found, often, the landlord must agree on the rental rate. All this means that the pressure to lower rents is reduced.

On the supply front, there is just one new building on the way, IOI Central Boulevard Towers. With close to half of its 1.26 million sq ft (NLA) pre-committed, there is very much reduced pressure for this prime site to upset the present rental harmony in the CBD Grade AAA office market. It is only towards the end of the year that we may see another batch of completions coming in the form of Keppel South Central, Labrador Tower and Paya Lebar Green.

For these reasons, we believe that although elevated levels of new supply is coming online in 2024, the market will still be able to hold up reasonably well, especially in CBD Grade AAA buildings. We do not expect rents for the premium buildings to change in 2024. Any rental adjustments may however come from buildings whose vacancy rates surpass 5% or some of the Grade A and AA buildings. However, the drop is likely to be mild. Overall, we believe that rents for overall CBD Grade A offices may adjust down by 2% to 3% YoY in 2024.