REPORT
Savills Research

VIETNAM – Q1/2020

# Media Release
# Office

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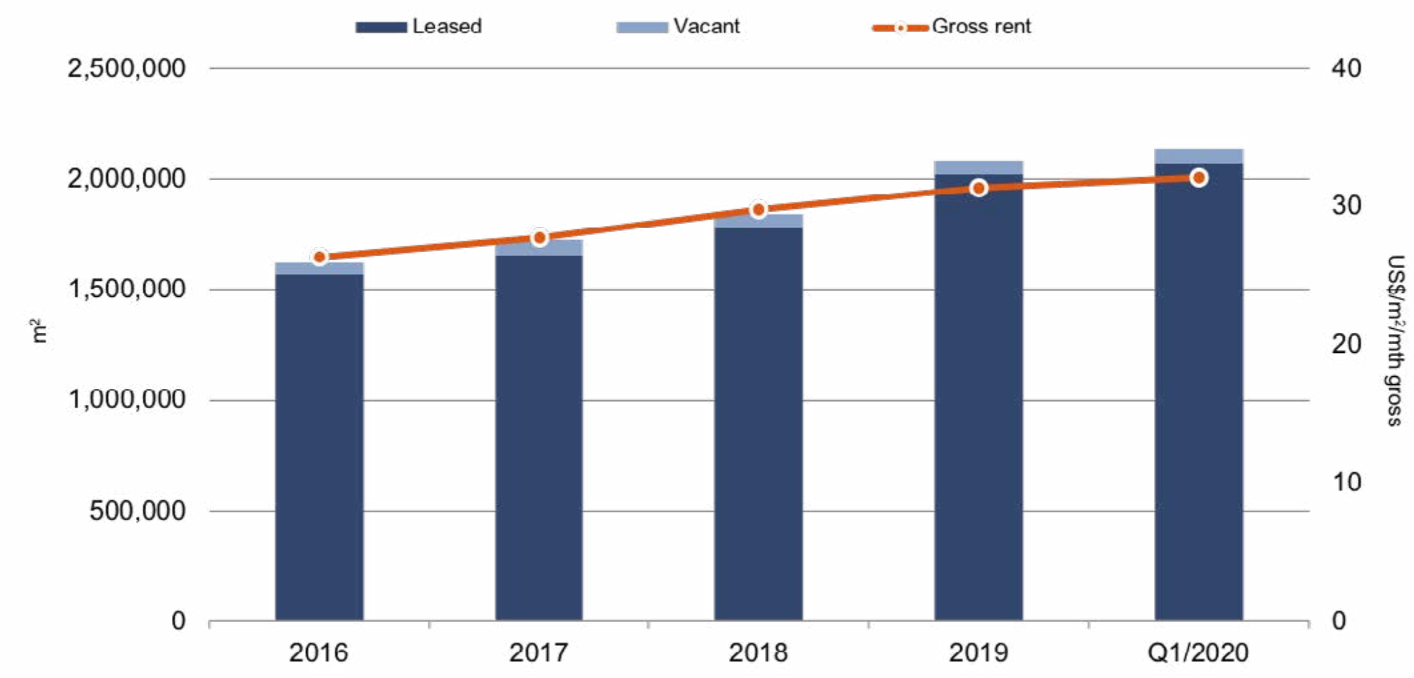
# OFFICE:

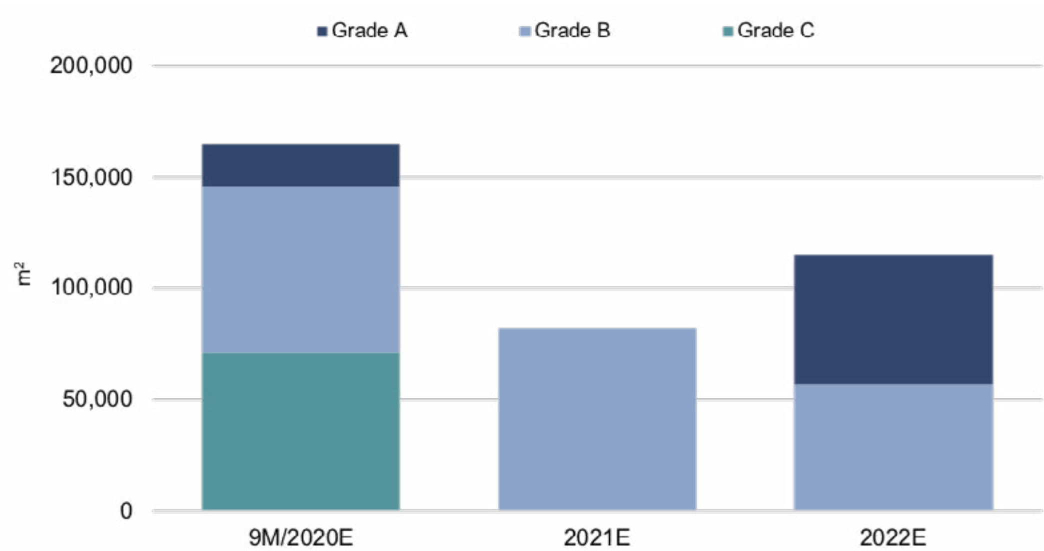
| SUPPLY | AVG. RENT | GRADE A RENT | OCCUPANCY |
|---|---|---|---|
| >2.1 mil m² | $32/m²/mnth | $62/m²/mnth | 97% |
| ▲ 3% QoQ | ▲ 2% QoQ | ▲ 2% QoQ | ▲ 1 ppt QoQ |
| ▲ 16% YoY | ▲ 4% YoY | ▲ 6% YoY | ▼ -1 ppt YoY |

## Market Performance




**Source** Savills Research and Consultancy

## Future Supply till 2022




**Source** Savills Research and Consultancy

*(1) Data collection as of Q1/2020*
*(2) Occupancy calculated by leased area divided by leasable area*
*(3) Avg. Rent: including service charge, excluding VAT*

*QoQ: Quarter on Quarter comparison*
*YoY: Year on Year comparison*

*“A change in occupier structure is coming; from open plan CoWorking to Serviced Offices. From Serviced Office to Hotel day rooms. From back office to work from home. There is an opportunity to recalibrate needs to match business objectives.”*

*Tu Thi Hong An,Director, Commercial Leasing*

# KEY FINDINGS

## Limited COVID impact, so far

The strong leasing momentum from 2019 continued at the start of Q1/2020, before the pandemic set in at the end of March.

HCMC received substantial new office supply of 61,400$m^2$ from seven Grade B and C projects in Q1/2020. In which, Grade B accounted for 80% and with two new projects in the non-CBD, had the highest growth of 4% QoQ. Total city supply reached over 2.1 million $m^2$, up 3% QoQ and 16% YoY.

By 2022, there will be an additional 360,000$m^2$ added, decentralization continues with 63% expected in the non-CBD. For the remainder of 2020, more than 160,000$m^2$ from 16 projects, will be added. However, CoVid is slowing the development pipeline. The global material supply chain is disrupted and construction projects have closed in response to social distancing. Fresh office supply could be delayed.

Average occupancy remained high at 97%, up 1ppt QoQ. The increase was a result of 2ppts QoQ improvement from Grade B, while Grade A and C remained stable. Average rents increased 2% QoQ across all grades. Since common lease terms are three to five years, external shocks do not immediately affect lease terms, rent reviews or area reductions, until contract expiry.

In late Q1/2020, the rapidly evolving COVID-19 pandemic brought business to a halt across the country. The office market will be impacted by unavoidable re-evaluations of workforce and demand requirements.

Over the last 5 years average annual take-up was approximately 140,000 $m^2$ annually, and is expected to slow.

## Initial COVID impact

Most companies are working-from-home with some rotating staff, under social distancing rules and lockdowns leading to partial or entire office closure.

Around 18,600 enterprises were temporary closed across Vietnam in Q1/2020, up 26% YoY. If COVID-19 extends to Q2/2020, the Ministry of Labour estimates 2-3 million temporary job cuts. In HCMC, the negative impact caused a sharp decrease in GDP growth (-7ppts YoY) and FDI inflows (-32% YoY).

The outbreak will hit airlines, transportation, tourism, manufacturing, real estate and finance industries. Key Grade A and B occupiers of FIRE, trading and manufacturing together accounted for more than 60% of the leased area.

- Transportation, tourism and hospitality have had massive layoffs and many companies will not survive.
- Professional services firms are re-evaluating and reducing their workforces and implementing cost reductions.

The co-working industry with shorter leases will be tested, given the need for social distancing. Growing office demand from start-ups and SMEs supports co-working space, however, these tenants are sensitive to the economic decline. Co-working will be challenged by the withdrawal of SMEs and isolation measures/ However they may also benefit on the upswing as these businesses are fast to recover and there will be a transfer of demand to non-traditional occupiers.

The outbreak opportunities are reasonable for legal services, e-commerce, fintech, software, biotech, and government. E-commerce firms are thriving as the online environment attracts more patronage after the social unrest and in turn, expect to see more office demand from such businesses providing a wider range of services.

# KEY FINDINGS

## Landlords & occupiers respond

Grade C landlords have been more flexible with rent reductions, engaging with their tenants to find pragmatic solutions that fit both parties, including up to 20% discounts in March. Grade A and B landlords have yet to respond. Its expected there will be discounts to ensure sustainability over the longer term.

Landlords will be willing to lower rentals, offer concessions, or more favorable lease terms to ensure they keep and attract building occupiers. The ‘blend and extend’ model is often touted.

## Positive outlook

Although Vietnam’s GDP growth Q1/2020 was the lowest over the last decade at 3.8%, the economic outlook is still optimistic. According to the latest ADB 2020 GDP growth forecast, Vietnam is expected to reach 4.8%, higher than regional peers: Indonesia (2.5%), Singapore (0.2%), Philippines (2%), and Thailand (-4.8%).

Governments and central banks have been responding to the situation with policy measures and financial aid to mitigate the economic impact. Vietnam is one of the global top 20 fiscal stimulators. Vietnams measures include: a credit package of VND250,000 billion with preferential interest rates, the postponement of VAT, corporate income tax and land rent payments for up to five months without penalties, the temporary payment suspension of social insurance fund and union fees until 6/2020, or longer subject to the outbreak. These initiatives help to reduce immediate costs to maintain business continuity and preserve jobs.

## Occupier opportunity

Although a massive threat to the global economy, COVID-19 may create unexpected opportunities for tenants.

In the short term, the market is likely to favor tenants. Occupiers who can make quick decisions have an opportunity to secure better deals. Vacancies are expected to increase, providing tenants leverage for cost-reduction.

The longer-term opportunity could be structural as firms look to review office work practices. Occupiers are testing in real time their capabilities to work from home (WFH), which could be adopted more widely. Companies may downsize with workplace redesigns and flexible arrangements.

‘Blend and extend’ lease terms can now be discussed. There are opportunities for both lessor and lessee, with a view to long term sustainable outcomes. If there are to be rental abatements or longer term discounting, then it is reasonable that the tenant contemplates a longer lease term to guarantee the occupancy and risk share with the lessor.

Work practices are already under review, provided productivity is maintained. As WFH evolves this will shift demand, as it did with back office functions a decade ago, being relocated away from the higher rent client facing space.

Shared or Coworking space is already under significant pressure, particularly the open plan design. There will be more disruption to this asset class as alternate models compete, and market share is lost. In the near term, the traditional Serviced Office is likely to become more popular and further erode shared work space share. Canny hotel operators are now converting their rooms to daytime offices. This model will continue for at least 6 months as international borders remain shuttered. With that lead time there will be further iterations and opportunity to establish as a defacto office provider.

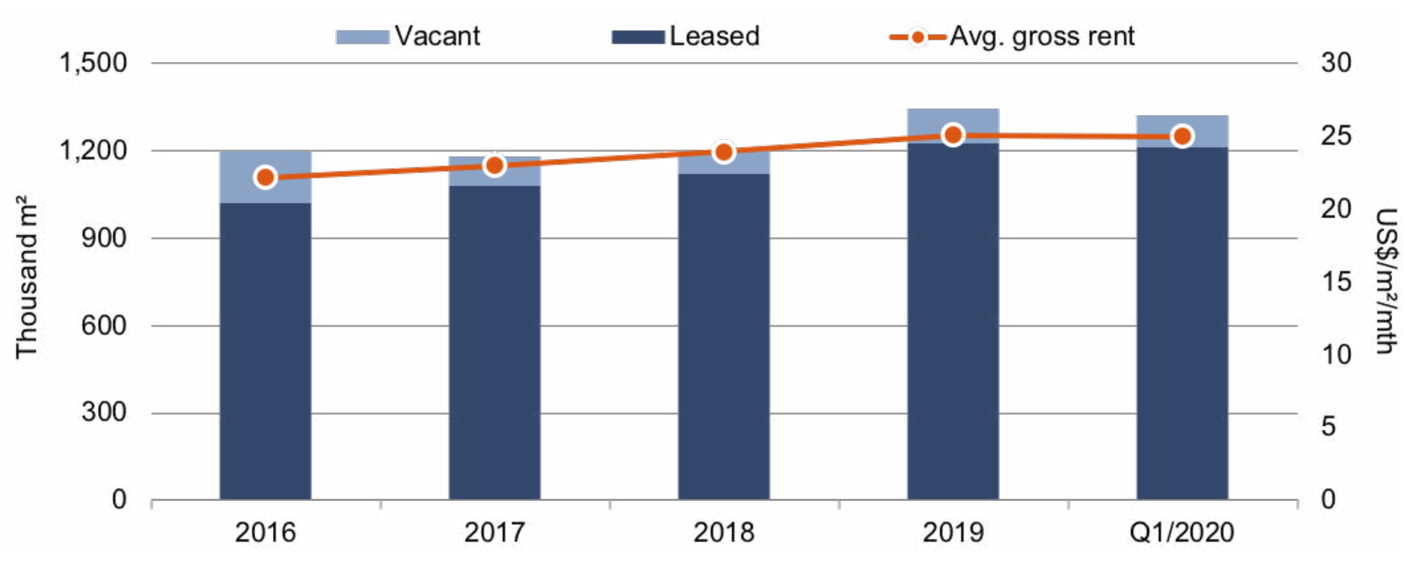
# OFFICE:

**TOTAL SUPPLY**
**1.8** mil m²
-1% QoQ
3% YoY

**AVG. RENT**
**$20**/m²/mth
-1% QoQ
1% YoY

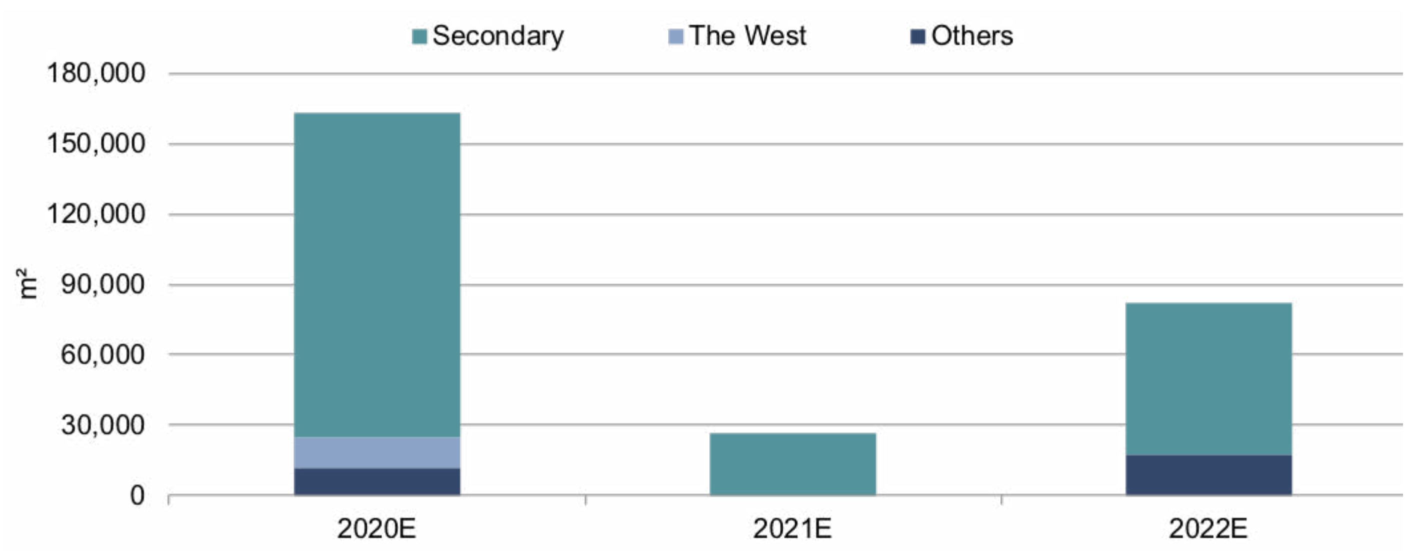
**OCCUPANCY**
**93%**
stable QoQ
1 ppt YoY

## Market Performance




**Source** Savills Research and Consultancy

## Future Supply

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> *Whilst the current office market remains healthy, there is a lag affect that may affect pricing in the future. Short term discounts and healthy lessor / lessee partnering are now considered.*
>
> *Le Tuan Binh,*
> *Head of Commercial Leasing, Savills Hanoi*

# KEY FINDINGS

## Stable Performance

Total stock was approximately 1.8 million m², decreasing -1% QoQ and up 3% YoY as two CBD Grade A projects International Centre and Vietcombank Tower were withdrawn for renovation and internal use. Grade B continued to dominate with 47%, followed by Grade C with 28 percent. Most projects are located in the West.

By 2022, new supply of approximately 272,000 m² will enter, primarily Grade A. Decentralization continues as most are in the Secondary area, none are expected in the CBD. All projects scheduled to launch in 2020 are fitting out and will deliver. However, with the on-going uncertainty, other developments may be delayed.

The office market has yet to see significant negative impact of COVID-19, and maintained stable performance this quarter. Most leases have terms of three to five years and so the cycle is smoothed. The average gross rent decreased by a slight -1% QoQ but increased 1% YoY; rent was down across all grades. Occupancy was unchanged QoQ and up 1 ppt YoY; Grade A had the strongest growth. Near term vacancies will increase as tenants tightening spending, resize or close their offices, or put expansion plans on hold.

Q1/2020 take-up was negative at -15,600 m², the lowest in the past six quarters, mainly due to the closures of two Grade A projecs. Highest take-ups were Grade B and the West; however, 2020 take-up will slow.

## Short-Term Impact

COVID-19 slowed Hanoi's Q1/2020 GDP growth, to 3.72% YoY, half of Q1/2019 (6.95 percent). Implemented FDI growth was 3.9% YoY, tremendously lower than in Q1/2019 (24.7%) since projects by Chinese, Korean and Japanese investors confronted obstacles in commercial transactions and customs clearance.

Most companies are encouraged to work from home, either entirely or on a rotating basis, leading to temporary closures of numerous workplaces, directly affecting office leases. Companies in transportation, tourism and hospitality are the most affected due to their high level of social interaction. Manufacturing and trading companies have reduced demand as production and supply chain disruption are felt. Besides, professional service providers are reassessing workforces to minimize costs.

Companies in healthcare and insurance are thriving; their demand is high. ICT firms are also strong, since technologies to optimize remote productivity are expanding.

Coworking demand has dropped significantly as it is vulnerable to the pandemic, with short leases and open plan spaces. It is expected to recover quickly with demand strongly biased to SMEs.

# KEY FINDINGS

## Landlords & Tenants

Landlords of low-grade buildings have responded quickly with rent adjustments. Concessions will need to be made for a win-win solution, that could include: rent reductions, favorable lease terms and renegotiation of essential clauses. There is also the option to 'blend and extend' to risk share and lengthen the original lease term for a stronger covenant with the landlord.

## Promising Future

Although Vietnam's Q1/2020 GDP growth was the lowest for the decade at 3.8%, the economic outlook is still optimistic. According to the latest ADB 2020 GDP growth forecast, Vietnam is expected to reach 4.8%, higher than regional peers: Indonesia (2.5%), Singapore (0.2%), Philippines (2%) and Thailand (-4.8 percent). According to GSO's survey on Q2's business trends in the manufacturing industry, 38.8% of businesses consider the trend to be better; 25.9% of enterprises forecast to be more difficult and 35.3% of enterprises thought their business and production situation would be stable.

Governments and central banks have been responding to the situation with policy measures and financial aid to mitigate the economic impact. Vietnam is one of the global top 20 fiscal stimulators, with measures such as: a credit package of VND250,000 billion with preferential interest rates, the postponement of VAT, corporate income tax and land rent payments for up to five months without penalties, the temporary payment suspension of social insurance fund and union fees until 6/2020, or longer subject to the outbreak. These initiatives help to reduce immediate costs to maintain business continuity and preserve jobs.

Many tech behemoths were founded during challenging times such as Apple and Microsoft during the 1970's recession, or Airbnb during the GFC 2008-09. Many tech companies have also risen from the last recession including Twitter, Uber, or Netflix. A new wave of startups may enter the market following the pandemic, sparking fresh office demand.

## Changing Demand

External shocks do not immediately signal lease breaks or reductions, this is more likely at contract expiry. The crisis is possibly delivering us the most comprehensive home-office experiment in history. Work-from-home may never replace offices completely, but the upcoming tech-boom will enable it further. There may be a reduction of CBD office demand as staff alternate between working in the office or from home. In the long-term, despite a rebound in employment, future office areas may not increase in absolute proportion to the number of new hires.

The shift to flexibility drives continued growth in the shared office market. By 2024, millennials will constitute 75% of the active workforce. This growing group of office users prefers different offices. Options for working from home, office design and extra amenities are part of an attractive package.


**Savills Research**
We're a dedicated team with an unrivalled reputation for producing well-informed and accurate analysis, research and commentary across all sectors of the Vietnam property market.

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