Retail property market challenged by tough business climate

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The retail leasing market saw fewer transactions and declining rents in Q1 2016. Given the tough business operating climate, retailers’ cost consciousness and landlords’ more realistic rental expectations, we expect prime ground level rents in shopping malls to remain under pressure for the rest of 2016, with a full year slide of up to 3% in Orchard Road and up to 2% in the Regional Centres. We think the easing rents will create opportunities for new and existing retailers to expand or set up shops in prime shopping malls previously deemed expensive. Since competition for tenants and shoppers will intensify, landlords should look at their tenant repositioning initiatives more closely and have their asset enhancement strategies in place to remain competitive. We also foresee the weak leasing market, softening rents and subdued buying sentiment amid the economic uncertainties and risk of further interest rate hikes to weigh down on the imputed average capital values in 2016.

2016 Forecast at a Glance

**Orchard Road**
- **Prime rents (Ground floor)**: Up to 3.0%
- **Imputed average capital value**: Up to 2.0%

**Regional Centres**
- **Prime rents (Ground floor)**: Up to 2.0%
- **Imputed average capital value**: Up to 1.0%

*Note: All forecast herein refers to islandwide, except for rents and capital values. Source: Colliers International Singapore Research*
Leasing Market and Rental Values

A lacklustre start to 2016

Reflecting the lacklustre retail leasing market, rental records sourced from the Urban Redevelopment Authority’s Real Estate Information System (URA REALIS) showed the number of leasing deals shrank by 32.4% quarter on quarter (QOQ) to 1,725 transactions in Q1 2016.

The sixth consecutive quarter of decline also brought the number of leasing deals to the lowest level since the 1,771 transactions in Q1 2012.

This was underpinned by cautious consumer spending, as reflected in the official retail sales index (excluding motor vehicles sales). During the quarter, the retail sales index fell 10.5% year on year (YOY) in February 2016, after inching up 0.5% YOY in January 2016.

Prime rents in the Regional Centres succumbed to downward pressure in Q1 2016

Against this challenging operating environment, which added to the stress that retailers are already experiencing over proportionally higher operating costs, manpower constraints and stiff competition from e-commerce, retailers remained cost cautious.

Landlords, especially those with more vacant stock, were also seen lowering their rental expectations and exhibited flexibility during lease negotiations to fill vacancies.

Consequently, the average monthly rents for prime ground floor shop space in both the Orchard Road and Regional Centres submarkets eased in Q1 2016.
Over the same quarter, the average monthly gross rents for similar ground level shopping mall space in the Regional Centres – the premium category of suburban malls – also succumbed to the tough leasing climate and slipped by 0.5% QOQ. This was the first rental decline since the 0.1% QOQ dip in Q1 2013.

Notwithstanding, rents in the Regional Centres were still more resilient than those in Orchard Road which has a higher dependency on tourist traffic. These sizeable regional retail centres were also able to attract quality tenants as they are well-located, easily accessible with good connection to the Mass Rapid Transit (MRT) network, and enjoy high footfall traffic supported by a larger ready catchment population. Colliers anticipate this trend to continue into 2017.

Retailers re-strategise, providing opportunities to refresh Singapore’s retail scene

Meanwhile, the burgeoning online retailing segment, fuelled also by the rapidly growing mobile and internet penetration, is expected to pile more pressure on traditional bricks-and-mortar retailers to evolve or face obsolescence.

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Landlords focused on enhancing shopping experience, upgrading malls, repositioning tenant mix

Meanwhile, landlords focused on enhancing the shopping experience by increasing the number and variety of events and activities within the malls. The rationale for this is that creating a positive emotional link between shoppers and the malls will boost shopper traffic and in turn drive the sales of the tenants.

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Sales stayed muted
In the strata-titled sales segment, sales remained muted in Q1 2016. Caveat records downloaded from URA REALIS on 5 May 2016 showed 45 caveats were lodged in Q1 2016, just slightly more than the 41 caveats lodged in Q4 2015. Generally, investors stayed cautious and held back on their purchases or investments in retail shops amid the challenging economic and retail operating environment. This was in addition to the slowdown in leasing activity, the effect of the Total Debt Servicing Ratio (TDSR) requirement, the turbulent stock market, job insecurity and risk of further interest rate hikes.

In the Orchard Road micro-market, the imputed average capital values of prime strata-titled retail space eased by 0.3% QOQ on the back of moderating rents. However, the imputed average capital values in the Regional Centres – where rents were more resilient – remained stable for the eighth consecutive quarter in Q1 2016.

“For progressive landlords and retailers, 2016 is time for a change of gear with fresh strategies and a new offer responding to softer economic conditions and well-informed consumers. Those continuing to follow established formulae are likely to experience weaker performance sustained well into the future. Punchy new openings underpinned by a strong data led approach and supporting digital strategies will be the headline takers through the latter part of 2016 and into 2017.

For landlords, Asset Enhancement programmes must be based on up to date consumer analysis and not merely treated as refurbishment projects, as the void period for capital works will damage investment returns without a compensating upside in operating income.”

- Simon Baxter, Executive Director, Retail Development and Asset Management | Asia
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