Colliers Quarterly

SINGAPORE | OFFICE

Q2 2017

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Colliers INTERNATIONAL

Accelerating success.

This report has been updated as of 4 August 2017 and supercedes all previous versions.

Green shoots

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Q2 2017 CBD Premium and Grade A office rents have continued to decline, albeit at a slower rate, and vacancy has risen under the weight of the large new completions. The first half of 2017 has seen relatively strong pre-commitments in the new developments as "flight to quality" continues. In H2, Colliers expects the staggered return of secondary space to the market and new completions to increase average vacancy further and lead to a modest rent decline by end-2017. The pace of new CBD supply would slow down in 2018-2020, and we expect the market to pick up steadily if occupier demand keeps up with the GDP growth forecast.

Forecast at a glance

Demand
Continued flight to quality but expansion in net new demand remains modest.

Supply
After a 5.5% increase in H1, we expect another 4.0% increase in Premium and Grade A stock in CBD in H2 2017. The pace of growth will ease in 2018-2020F.

Vacancy rate
The CBD Premium and Grade A vacancy rate as of Q2 2017 was 6.9%. We expect that to rise to 10.2% by end-2017, and taper off in 2018-2019.

Rent
The CBD Premium and Grade A office rents have declined 0.3% YTD. We expect rents to decline 1.0-3.0% over 2017 on higher vacancy, and to recover gradually in 2018 as supply eases.

Price
Prime office capital values could increase with continued investment demand

Signs of stabilisation

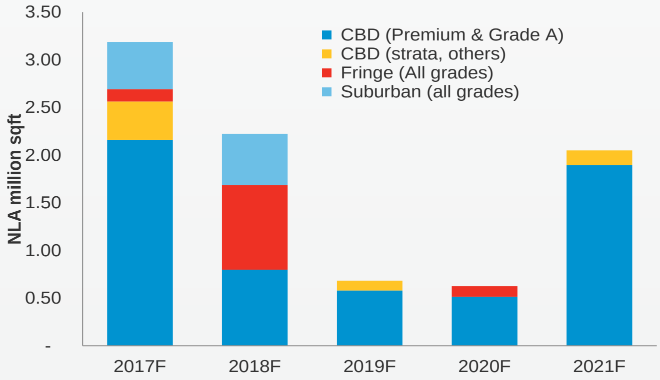
In Q2 2017, CBD Premium and Grade A average office rent have declined 0.1% QOQ and 1.2% YOY to SGD8.54 (USD6.19) psf pm. This is 9.6% below the last peak of SGD9.44 (USD6.84) psf pm in Q2 2015. Based on Colliers International's Research, CBD Premium and Grade A occupancy declined 1.0ppt to 93.1%, due mainly to an increase of 5.5% in CBD Premium and Grade A space from two major completions during Q2.

The first half of 2017 has seen relatively strong pre-commitments in the new developments as “flight to quality” continues. However, we note there has been modest expansion in net new occupier demand.

The staggered return of secondary space to the market as tenants move to the new developments should continue to put some pressure on landlords. As such, we still expect CBD Premium and Grade A rents to soften by 1.0-3.0% in 2017. With a benign supply between 2018-2020F, we expect occupier demand and rents to pick up steadily with a more broad-based economic growth.

On the other hand, the investment market for prime office assets remained robust in H1 2017, with capital values showing an upward bias. More owners are jumping on the bandwagon to redevelop older properties which could result in withdrawal of some older space in the near term, and eventually more and better space three to four years from now. A new state site will also be tendered by end of Q3. These should pave the way for a sustained supply/demand balance beyond 2019.

Islandwide Office Space Supply (2017 – 2021F)



Source: Colliers International Singapore Research

Leasing market and rental values

Eighth quarter of rental decline since recent peak in Q2 2015

In Q2 2017, office rents across Singapore on average slid for the eighth consecutive quarters, under the weight of large supply completions. However, the rate of decline has slowed down further, with some micro-markets stabilising. CBD Premium and Grade A office rents have declined on average by 0.1% QOQ, 1.2% YOY and 9.6% since the last peak in Q2 2015.

Average Monthly Gross Office Rents by Micro-market

Micro Market	Q2 2017 Average Monthly Gross Office Rents (SGD psf)	QOQ Change (%)	YOY Change (%)
Premium			
Raffles Place/New Downtown	9.97	-0.6%	-4.9%
Grade A			
Raffles Place / New Downtown	9.08	-0.2%	-4.1%
Shenton Way / Tanjong Pagar	8.38	-0.1%	2.4%
Marina / City Hall	8.94	0.0%	-3.1%
Beach Road	7.68	0.0%	2.4%
Orchard Road	8.22	0.0%	-2.1%
City Fringe	7.01	0.0%	-2.8%
Suburban	4.85	0.0%	-0.8%
CBD Premium and Grade A	**8.54**	**-0.1%**	**-1.2%**
Grade B			
Raffles Place / New Downtown	7.70	-0.3%	-2.8%
Shenton Way / Tanjong Pagar	7.13	-0.4%	-3.9%
Beach Road	6.19	0.0%	-7.1%
Orchard Road	7.72	-0.8%	-4.2%
City Fringe	6.54	0.0%	-4.0%
Suburban	4.24	0.0%	0.0%

Source: Colliers International Singapore Research

Across the various micro-markets, in Q2 2017, rents at Premium, Grade A and Grade B office buildings in Raffles Place/ New Downtown and Shenton Way/Tanjong Pagar micro-markets declined 0.1-0.6% QOQ, with continued competition from the large new builds in their respective markets. Rents in the other micro-markets are largely stable, except Grade B Orchard Road which fell 0.8% QOQ due to higher vacancies.

Occupancy declined on new supply completions

So far, Singapore's GDP growth has been volatile and uneven, with trade-related sectors having risen in tandem with the global economic acceleration and global IT cycle upswing, but domestic-oriented industries have been weak on soft labour market. Q2 2017 GDP grew 2.5% YOY, +0.4% QOQ on a seasonally-adjusted annualised rate (SAAR), driven by manufacturing which grew 8.0% YOY, while the services sector lagged, growing 1.7% YOY in Q2, compared to 1.4% in Q1 2017 and 1.0% in Q4 2016.

Nonetheless, we expect growth could broaden out to financial services, business services, and wholesale and retail trade in 2018, which should benefit the office sector in the longer run. As of 31 July 2017, Oxford Economics forecasts Singapore GDP growth of 2.7% and 3.4% in 2017 and 2018 respectively, the highest since 2015's 1.9% and 2016's 2.0%.

Average Occupancy Rates for Premium and Grade A Office Space by Micro-market

Micro Market	Q2 2017 Average Occupancy Rate (%)	Q1 2017 Average Occupancy Rate (%)
Premium		
Raffles Place/ New Downtown	95.0%	96.0%
Grade A		
Raffles Place / New Downtown	96.7%	96.4%
Shenton Way / Tanjong Pagar	88.8%	92.9%
Marina / City Hall	94.2%	94.8%
Beach Road	68.4%	67.8%
Orchard Road	92.3%	96.6%
City Fringe	95.6%	95.3%
Suburban	98.2%	96.3%
CBD Premium and Grade A	**93.1%**	**94.1%**

Source: Colliers International Singapore Research

SELECTED OCCUPIER MOVEMENTS FOR CBD OFFICE BUILDINGS IN Q2 2017			
Building	Tenant	Net Floor Area (sq ft)	Relocation /Expansion /New site
Frasers Tower	Microsoft	150,000	Relocation and Expansion
Marina One	Ocean Network Express (JV of K Line, MOL, NYK Line)	50,000	Relocation and Consolidation
UE Square	TE Connectivity	18,000	New site
UE Square	Home Away	9,600	New site
Guoco Tower	Sri Trang Agro-Industry Public Company	6,000	Expansion
One Raffles Quay (North Tower)	Travelport	11,000	Relocation and Expansion

Sources: Colliers International Singapore Research, The Business Times, The Straits Times

Based on Colliers International's Research, islandwide occupancy declined 0.4 percentage point (ppt) QOQ to 93.8% in Q2 2017. Average occupancy in CBD Premium and Grade A office declined 1.0ppt QOQ to 93.1%, mainly due to declines in Premium space in Raffles Place/ New Downtown and Grade A space at Shenton Way on new stock additions.

On the other hand, occupancy in CBD Grade B space improved 0.7ppt QOQ to 94.2%, on improvements across the Raffles Place/New Downtown, Shenton Way/ Tanjong Pagar and Orchard Road micro-markets.

Marina One East Tower comprising 0.94 million sq ft (87,500 sq m) received its Temporary Occupation Permit (TOP) in June. The West Tower will likely be completed in the next few months, adding 4.0% to CBD Premium and Grade A stock. UIC Building with 0.28 million sq ft (26,000 sq m) space also received its TOP in June.

Modest expansions

H1 2017 has seen surprisingly strong pre-commitments in the new developments. The 1.88 million sq ft (175,000 sq m) Marina One is reported to be 70% pre-leased as of 12 July, while we estimate UIC Building in the Shenton Way/Tanjong Pagar micro-market is close to being 70% pre-leased. Guoco Tower, also in the Shenton Way/ Tanjong Pagar micro-market and completed in Sep 2016, saw commitment improve further to 93% from 86% in Q1 2017.

At Asia Square Tower 1, nearly all of the 130,000 sq ft or so that Google vacated last year has already been backfilled.

Despite the above, we note there has been relatively little expansion in net occupier demand. During Q2 and H1 2017, we see movements in tenants across various trade sectors including banking and financial services, business services, commodities, media, marine and shipping, and IT and eCommerce. Expansions continue to come from technology sectors and co-working operators.

According to The Business Times, software giant Microsoft has signed up for about 125,000 sq ft in Frasers Tower ahead of its target completion in Q2 2018. Microsoft is now located at One Marina Boulevard, where its lease for about 100,000 sq ft is said to expire in 2019. Colliers estimate that coupled with the Executive Centre's 20,000 sq ft earlier, it will bring Frasers Tower's precommitment level to 22%.

Ocean Network Express, the new joint venture of Japan's "Big Three" shipping lines, is reported to be taking up some 50,000 sq ft of office space at Marina One, and will be using the 1½ floors as its regional and global headquarters. Macquarie Bank, which is now at Marina Bay Financial Centre Tower 2, is also said to be in advanced negotiations for some 50,000 sq ft of office space at Marina One.

The Business Times also reported that at Guoco Tower, Thai rubber group, Sri Trang Agro-Industry Public Company, will be moving into a 6,000 sq ft space come December 2017, a 18% expansion from its 5,100 sq ft current space in One Raffles Place.

Redevelopment bandwagon

More developers are jumping onto the bandwagon to develop new sites and redevelop old buildings to capitalise on an upcycle.

On 18 July 2017, Afro-Asia Shipping (AAS) and Shimizu Corporation Investment and Development Division announced their joint venture (JV) to redevelop Afro-Asia Building, an office block at 63 Robinson Road. The approximately 60-year-old building will be redeveloped into a new Grade-A office building with 16,908 sq m (182,000 sq ft) of GFA. Shimizu will carry out demolition in November 2017 and construction is expected to start in April 2018, with completion scheduled for mid-2020.

According to The Straits Times on 1 July 2017, the owner of Hub Synergy Point at Anson Road is also looking to redevelop the 72,000 sq ft (6,690 sq m) office block next year, and complete by 2020.

In a sign of the bullish investment sentiment for prime office assets, a Beach Road commercial site on the Reserve List of the Government Land Sale (GLS) Programme has been triggered for sale on 21 June. The minimum price of SGD1.138bn (USD825 million) translates to SGD1,197psf ppr. The tender closes on 28 September.

The Beach Road plot will have a maximum permissible gross floor area of 950,592 sq ft (88,313 sq m). At least 70% - or 665,424 sq ft (61,820 sq m) - must be used for offices, with a maximum of 32,292 sq ft (3,000 sq m) for retail space.

After this site was triggered, the H2 2017 Government Land Sale (GLS) Programme has not offered any new office sites in the CBD.

Strata sales and capital values

Continued interest in prime buildings

Based on Realis data as of 20 July, strata office sales transactions in Q2 2017 increased 10.9% QOQ to 61 from a total transaction volume of 55 in Q1 2017. However, it was 28.2% below Q2 2016's 85 transactions.

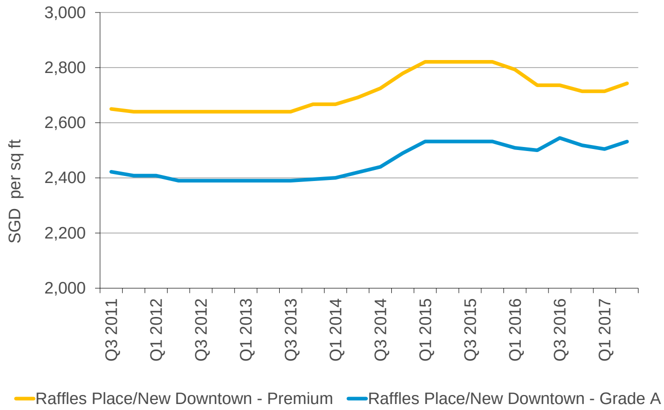
During Q2 2017, there were 13 new strata unit sales, nine of which were for suburban office Woods Square in Woodlands, three were for TripleOne Somerset in Orchard Road, and one for Centrium Square in city fringe. Median prices for these three projects were SGD1,829 psf, SGD2,649psf and SGD2,592psf respectively. The proportion of new sales to overall transactions was 21%, vs 9% in Q1 2017.

Investment sentiments for office buildings remained robust into Q2 2017 with conclusion of a major private office asset sale: the sale of a 50% stake in One George Street to FWD Insurance, a subsidiary of Hong Kong's PCCW, at an asset value of SGD591.6 million (on 100% basis, USD435 million). This implied SGD2,650 (USD1,920) psf on NLA and 3.2% net property yield.

Based on Colliers International's research, the average capital value for Grade A office space in Raffles Place/New Downtown rose 1.1% QOQ and 1.3% YOY to SGD2,532 (USD1,835) psf in Q2 2017, while the average capital value for Premium office space in Raffles Place/New Downtown also rose 1.1% QOQ and 0.3% YOY to SGD2,743 (USD1,988) psf.

The imputed average capital values for the other micro-markets across Singapore also rose marginally.

Average Capital Values[1] for Premium and Grade A Office Space in Raffles Place/ New Downtown



Note: (1) A valuation based methodology is used to derive the average capital values. Source: Colliers International Singapore Research

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