

SLOWING RENTAL DECLINES

Rental declines slowing but economic risks rising

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Summary & Recommendations

Retail rents in general remained weak in H1 2019; the URA retail rental index in the Central Region fell 1.7% from end-2018. While rental declines have slowed, heightened economic risks could dent consumer sentiment and delay any rental recovery.

Island-wide vacancy declined 80 bps in H1 2019 to 7.7% with higher net absorption. Going forward, vacancy should decline as H2 2019 - 2023 supply eases to 380,000 sq ft (35,200 sq m) p.a. Meanwhile, transaction volumes jumped 137% HOH on higher investor interest.

We advise landlords to optimize tenant mix and retailers to adapt to changing consumer trends such as experiential retail. Investors should focus on malls with high population catchment and asset enhancement potential.

	H1 2019	Full Year 2019	2018-23 Annual Average
 Demand <ul style="list-style-type: none"> Net absorption was broad based, increasing in H1 2019 with good take-up at two new malls, Jewel at Changi and Funan. We expect demand for the upcoming well-located malls to be favourable. 	 646,000 sq ft	 1.23mn sq ft	 538,000 sq ft
 Supply <ul style="list-style-type: none"> New supply in 2019 (est. 1.8% of stock) is well-distributed across the city centre, city fringe and suburbs. Supply pipelines should taper off over 2020-2023. 	 681,000 sq ft	 1.17 mn sq ft	 477,000 sq ft
	HOH/ End H1	YOY / End 2019	Annual Average Growth 2018-23 / End 2023
 Rent <ul style="list-style-type: none"> Ground-floor rents at Orchard Road declined 1.5% HOH on weak consumer spending while ground-floor rents of Regional Centres stayed flat. We expect ground floor rents to lead recovery over 2019-2023. 	 -1.5% SGD40.60*	 -1.2% SGD40.70*	 0.6% SGD43.50*
 Vacancy <ul style="list-style-type: none"> We expect Island-wide vacancy to improve in 2020-2023 as front-loaded supply in 2018 and 2019 gets absorbed. Vacancy should trend towards 7.2% as supply tapers off. 	 -0.8pp 7.7%	 -0.8pp 7.7%	 -0.3pp 7.2%
 Capital Values/ Yields <ul style="list-style-type: none"> Transaction volumes jumped 137% HOH to SGD2.13 billion, driven by higher investor interest. We expect a marginal compression of yields by 0.1 pp through 2023, driven by increased investment volume. 	 0pp 4.7%	 -0.1pp 4.6%	 0pp 4.6%

Source: Colliers International. *Refers to ground-floor rents in prime shopping malls within the Orchard Road district. Note: USD1 to SGD1.35 as at 30 June 2019. 1 sq m = 10.764 sq ft. "pp" refers to percentage point.

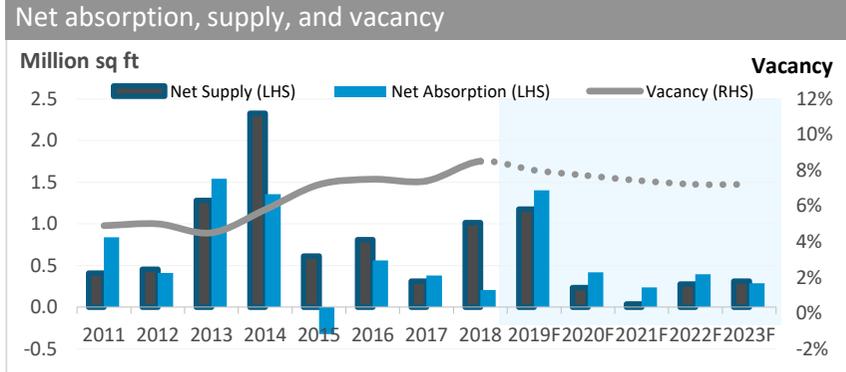
LEASING MARKET AND RENTS

Rental decline moderated, but economic risks rising

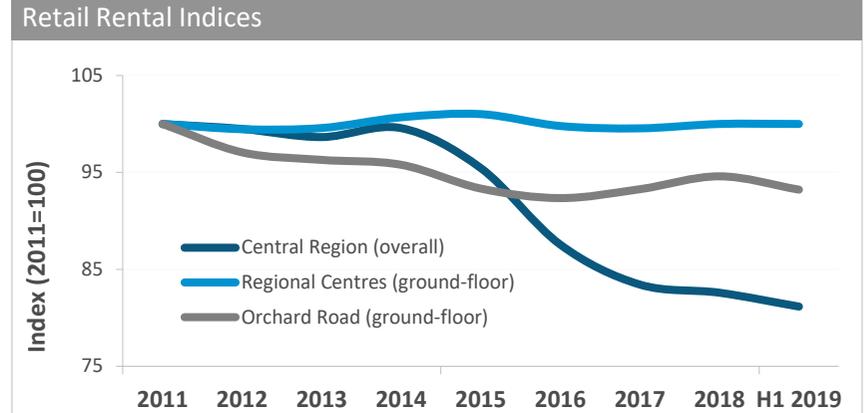
Based on Colliers' research, ground-floor rents on Orchard Road declined 1.5% HOH in H1 2019 to SGD40.60 (USD30.05) per sq foot per month, while that of Regional Centres remained flat at SGD33.60 (USD24.62) per sq foot per month. This is consistent with the Urban Redevelopment Authority's (URA) reported rental decline of 1.7% in H1 2019 for the Central Region. With the latest decline, URA's retail rental index has fallen 18.5% since its peak in Q4 2014. Rental declines have slowed since early 2018, and the large completions since 2013 should finally taper off from 2020 onwards. However, the soft economy could impact the still-fragile consumer sentiment and delay any rental increases. Retail sales (excluding motor sales), according to Department of Statistics, have also fallen for four consecutive months (on a YOY basis), declining by 1.0% YOY in May.

Key retail trends in H1 2019

With ongoing consolidation in the retail industry, in H1 2019, as reported by The Straits Times, Crabtree & Evelyn shut all its physical stores in Singapore as it moved operations online with a relaunched website and new product lines. This was among several other brands which have downsized their operations over the same period, including Isetan, Cold Storage, Marks & Spencer, MPH and Kinokuniya.



Source: Colliers International, URA. *A business model by which an online retailer (clicks) integrates an offline presence (bricks) by expanding into physical marketplaces to enhance their offerings.



Source: Colliers International, URA

Love Bonito opened its third and flagship store at Funan, continuing the trend of "clicks-to-bricks*", as physical stores can also serve as a showroom for online offerings. Other retail trends that we observed include "experiential retail", the rise of "subscription ecommerce" where curated products are shipped to customers on a regular basis, as well as the quicker shipping time to differentiate from saturated online offerings.

Vacancies improved with stronger take-up

Island-wide retail vacancy declined 80 bps in H1 2019 to 7.7%, driven by higher net absorption which is likely boosted by good take-up at Jewel at Changi and Funan. On a YOY basis, vacancy increased by 40 bps.

The 325,000 sq feet (30,200 sq metres) Funan reopened on 28 June, after a major 3-year revamp, with 95% of its retail shops leased. 25% of its space is dedicated to food and beverage, with new concepts such as a 200-metre cycling path, urban farm and Singapore's first physical standalone Taobao store. Jewel at Changi also officially opened on 17 April, with 280 shops over 580,000 sq feet (54,000 sq metres) of retail net lettable space.

Key completions in H2 2019 should include the 340,000 sq feet (31,600 sq metres) PLQ Mall, the retail component of Paya Lebar Quarters (PLQ). We estimate H2 2019 - 2023 average annual new supply at 380,000 sq feet (35,200 sq metres) versus 1.04 million sq feet (96,600 sq metres) over the last decade. The lower supply should help support occupancy going forward.

INVESTMENT MARKET AND CAPITAL VALUES

Robust investment sales reflect increasing optimism

Retail transactions jumped 137% HOH

Total retail investment sales transactions jumped 137% HOH to reach SGD2.13 billion (USD1.58 billion) in H1 2019, driven by higher investor interest. Full year 2018 transactions pale in comparison, recording only SGD1.42 billion (USD1.05) billion.

Notably, the majority of H1 2019 transactions were malls in the Central Region, including: 1) Marina Square Shopping Mall (24.3% stake); 2) Chinatown Point Mall; and 3) Liang Court, as reported by the Business Times. Outside the Central region, it was also reported that Frasers Centrepoint Trust bought a one-third stake in Waterway Point from Frasers Property.

We note the buyers of these malls are spread across strategic and financial buyer types with developers and REITs seeking yields or future redevelopment potential while institutional funds look for yields and value-add opportunities.

Capital values down 0.6% HOH, expect stabilization going forward

Q2 2019 capital values in the Orchard area were down marginally 0.6% HOH, in line with the mild rental declines. As we expect rents to continue bottoming out, yields should remain relatively flat. According to Colliers International Valuation and Advisory Services (CIVAS) team, cap rates for prime shopping malls island-wide remain unchanged from the end of 2018, ranging between 4.4% and 4.9%.

We expect retail or mixed-use development transaction volumes to grow in line with global capital's increasing allocations to real estate amidst rising global volatility. However, we note prime retail assets in Singapore are often tightly-held with relatively limited stock. We view retail properties with a sizable market catchment, well-differentiated tenant mix, or potential for future catchment growth as attractive investment opportunities.

Notable retail transactions | H1 2019

Property	Transacted Price (SGD million)	Price PSF NLA (SGD)	Planning Region
Marina Square Shopping Mall (24.3% stake)	485	2,857	Central Region
Chinatown Point Mall	520	2,450	Central Region
Waterway Point (one-third stake)	441	3,502	Outside Central Region
Liang Court Mall	400	1,492	Central Region

Source: Colliers International

Retail sales index and tourist arrivals (YOY growth)



Source: Colliers International

Retail price index and total investment sales volumes



*Investment sales only include transactions over SGD5 million. "TTM" refers to trailing 12 months.

Source: Colliers International, URA

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