Q3 2018: Malaysia Commercial Property Monitor

Supply-demand mismatch continues to weigh on sentiment, but growth seen on the horizon

Sentiment surrounding Malaysia's commercial property market remained subdued in Q3. Although there are some concerns over potential vulnerabilities which may be exposed as the global economic expansion begins to cool, the Malaysian economy appears to be much more resilient to these than during previous economic cycles, and respondents remain more optimistic for the commercial property market's medium-term prospects.

Occupier Market

- The Occupier Sentiment Index (an amalgamated measure of occupier market indicators) rose to -24 in Q3 from -29 in Q2 (Chart 1), however, this is still indicative of a continued contraction in occupier market momentum.
- Aggregate occupier demand declined in Q3, though at a slower pace than in Q2. This was largely driven by a slowdown in the pullback in demand for office and retail properties, while demand to rent industrial space was flat for the fourth consecutive quarter.
- The supply of properties available to rent rose across the board, and at a quicker pace than in Q2. However, this was offset to some degree by an increase in incentive packages on offer, particularly for office and retail properties. Rent-free periods remained the most popular inducement offered by a fair margin.
- Development starts continued to contract, though this too was at a slower pace than in Q2 across all market segments (office, industrial, retail).
- Against this backdrop, headline rents are expected to decline over the next three and twelve months. As shown by Chart 6, prime industrial properties are seen as the only exception, with rents expected to increase 0.4% over the next year.
- Prime properties are expected to fair slightly better over the medium term, with average rents on prime office and industrial properties expected to increase 1.1% and 2.5% annually over the next three years, respectively.
- Although more than half of respondents see the market in some stage of a downturn, 27% see the market being at its bottom. This share has risen steadily over the past four quarters.

Investment Market

- The Investment Sentiment Index (an amalgamated measure of occupier market indicators) fell to -25 in Q3 from -19 in Q2 (Chart 1), indicating a modest contraction in market momentum during Q3.
- Investment enquiries declined in Q3 at a similar pace to Q2. This contraction in investor demand was reported for both domestic and foreign buyers, and was fairly uniform across market segments (office, industrial, retail).
- After being flat in Q2, the supply of properties available for sale rose at the headline level in Q3. This increase was particularly acute in Kuala Lumpur.
- Credit conditions remained evenly distributed in Q3, with the majority (56%) reporting no change (Chart 3). The remaining 44% were almost evenly split between seeing a slight improvement and slight deterioration.
- Respondents generally felt that valuations were around fair value, with 47% holding this view (Chart 4). Similar to the past several quarters, more than a third of respondents felt that valuations were slightly above fair value, though less so in Kuala Lumpur than in other parts of the country.
- Similar to rents, respondents have fairly subdued expectations for capital values, which are seen falling at the headline level over the next three and twelve months. However, prime industrial values are expected to remain unchanged over the next twelve months.
- Looking at Chart 5, secondary properties remain a drag on the outlook, as contributors revised one-year forecasts on prime office space higher in Q3. The outlook for the medium term is positive, with headline values expected to rise 0.8% annually over the next three years.

Commercial Property Market

Chart 1: Occupier, Investment Sentiment Indexes

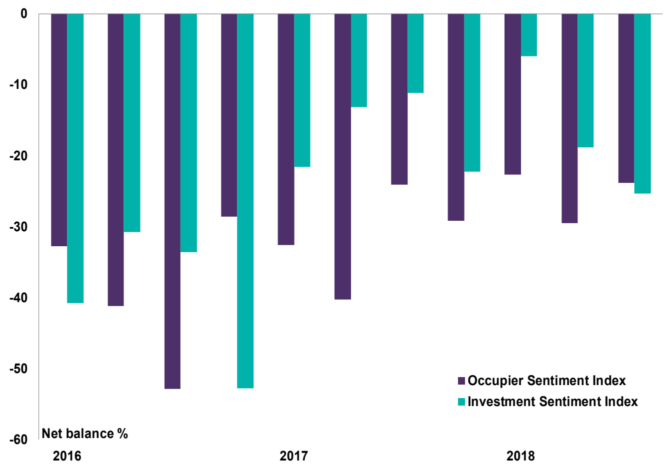


Chart 2: 3-month Rents, Capital Values

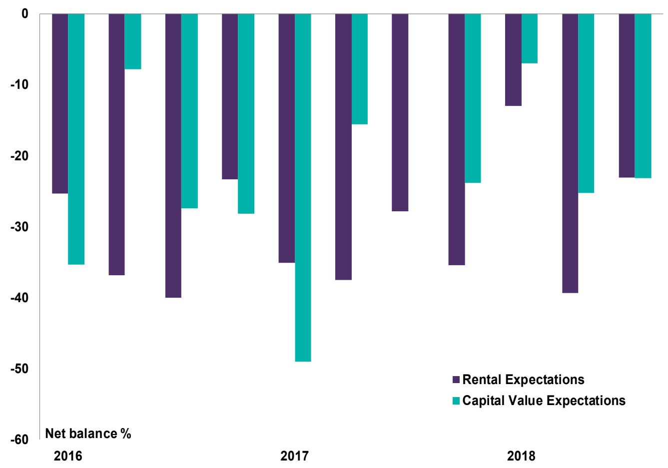


Chart 3: Credit Conditions

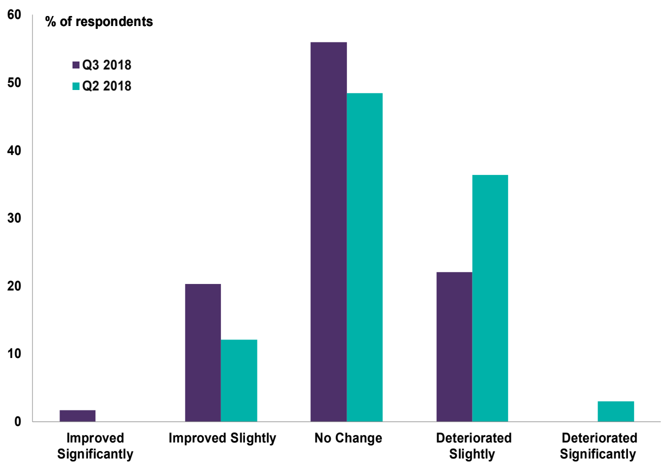


Chart 4: Valuations

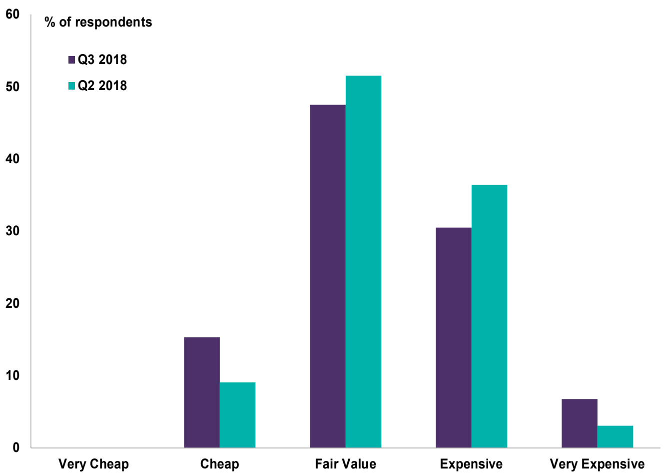


Chart 5: 12-month Capital Values Forecast

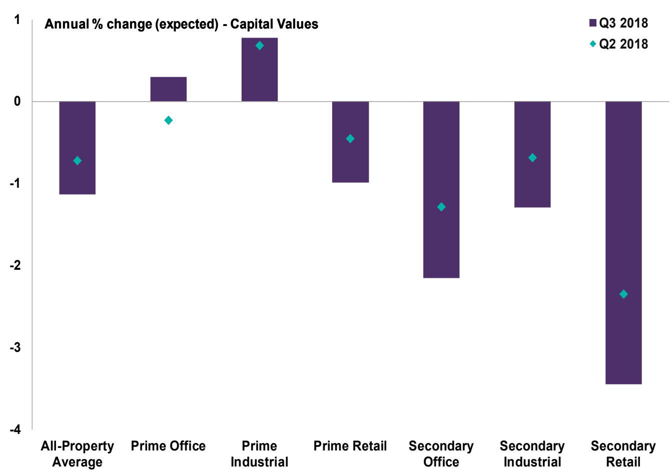
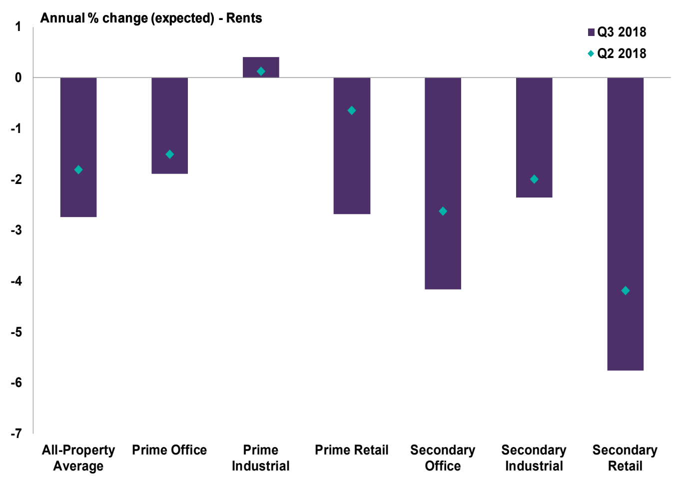


Chart 6: 12-month Rent Forecast



Information

Global Commercial Property Monitor

RICS' Global Commercial Property Monitor is a quarterly guide to the trends in the commercial property investment and occupier markets. The report is available from the RICS website www.rics.org/economics along with other surveys covering the housing market, residential lettings, commercial property, construction activity and the rural land market.

Methodology

Survey questionnaires were sent out on 13 September 2018 with responses received until 14 October 2018. Respondents were asked to compare conditions over the latest three months with the previous three months as well as their views as to the outlook. A total of 1791 company responses were received, with 341 from the UK. Responses for Ireland were collated in conjunction with the Society of Chartered Surveyors Ireland. Responses for Spain and Portugal were collated in conjunction with Iberian Property. Responses for New Zealand were collated in conjunction with Property Council New Zealand. Responses for Malaysia were collated in conjunction with the Royal Institution of Surveyors Malaysia.

Responses have been amalgamated across the three real estate sub-sectors (offices, retail and industrial) at a country level, to form a net balance reading for the market as a whole.

Net balance = Proportion of respondents reporting a rise in a variable (e.g. occupier demand) minus those reporting a fall (if 30% reported a rise and 5% reported a fall, the net balance will be 25%). Net balance data can range from -100 to +100.

A positive net balance reading indicates an overall increase while a negative reading indicates an overall decline. The RICS Occupier Sentiment Index (OSI) is constructed by taking an unweighted average of readings for three series relating to the occupier market measured on a net balance basis; occupier demand, the level of inducements and rent expectations. The RICS Investment Sentiment Index (ISI) is constructed by taking an unweighted average of readings for three series relating to the investment market measured on a net balance basis; investment enquiries, capital value expectations and the supply of properties for sale.

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