

RESEARCH

October 2018

# Kuala Lumpur Q3 2018

Post-election euphoria boosted CSI



# 2018 Q3 snapshot

Malaysia's economy saw a slower growth expansion of 4.5 per cent in the second quarter of 2018 (Q1 2018: 5.4 per cent). Supply disruptions in the mining sector and the lower agriculture production due to the weather conditions were the main contributors to the slowdown.

## Investment

Investment sales eased to  
**RM649.6m**  
from RM709m in Q2 2018.

The investment market was dominated by **retail** and **industrial** sales.

### Office



The office absorption remained slow and average occupancy rate dropped slightly to 81.0 per cent<sup>1</sup>.

### Retail



Occupancy of malls in Klang Valley estimated at 89.0 per cent<sup>2</sup>.

### Residential



Average price and rent for high-end condominiums stood at **RM1,040 psf<sup>3</sup>** and **RM3.78 psf per month** respectively.

<sup>1,2,3</sup> Based on revised sampling at Oct 2018

# The economy

## Key highlights

- The Malaysian GDP expanded at a slower rate of 4.5 per cent year-on-year in Q2 2018 (Q1 2018: 5.4 per cent y-o-y).
- Unemployment remained unchanged as at 3.3 per cent (Q1 2018: 3.3 per cent).
- Headline inflation as measured by the annual change in percentage of the Consumer Price Index saw a decline to 1.3 per cent in Q2 2018 (Q1 2018: 1.8 per cent).
- A strong uptick in Consumer Sentiments Index (CSI) was registered at 132.9 points in Q2 (Q1 2018: 91 points).
- The Ringgit remained under pressure and depreciated by 4.6 per cent during Q2 to RM4.04 per US dollar.

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Major rail projects' cancellation and postponement and budget constraint will impact short-term growth.

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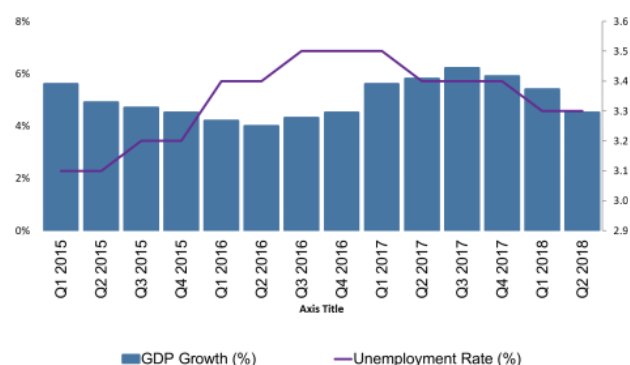
## Market commentary

The GDP continued to record a slowdown in Q2 2018 after the strong performance of the second half of 2017. It expanded at 4.5 per cent y-o-y, which was 0.9 percentage points slower than Q1 2018 (5.4 per cent). On a quarter-on-quarter (q-o-q) seasonally adjusted basis, the Malaysian GDP grew at 0.3 per cent (Q1 2018: 1.4 per cent) (Figure 1).

Domestic demand reported a substantial growth of 5.6 per cent (Q1 2018: 4.1 per cent), mainly due to the robust private sector activity, which grew at 7.5 per cent (Q1 2018: 5.2 per cent). Public spending saw a slowdown of -1.4 per cent in Q2 2018 (Q1 2018: -0.1 per cent).

On the supply side, the services and manufacturing sectors were the main contributors to the Malaysian economy. The growth of the services sector remained the fastest in the country growing at 6.5 per cent (Q1 2018: 6.5 per cent) followed by manufacturing at 4.9 per cent and construction at 4.7 per cent, while contraction was experienced in mining

Figure 1: Malaysia GDP growth and unemployment

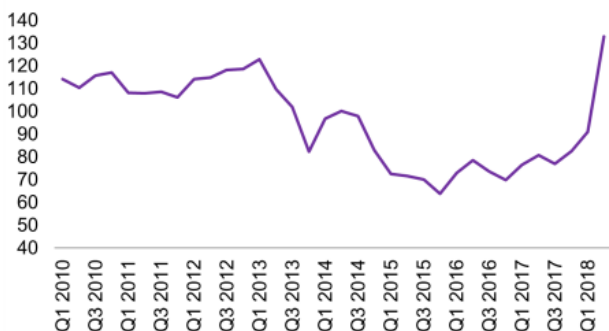


Source: Bank Negara Malaysia, Department of Statistics Malaysia, NTL Research

(-2.2 per cent) and agriculture (-2.5 per cent). The contraction was mainly due to the decline of natural gas output; and the oil palm subsector, which experienced production constraints and detrimental weather conditions.

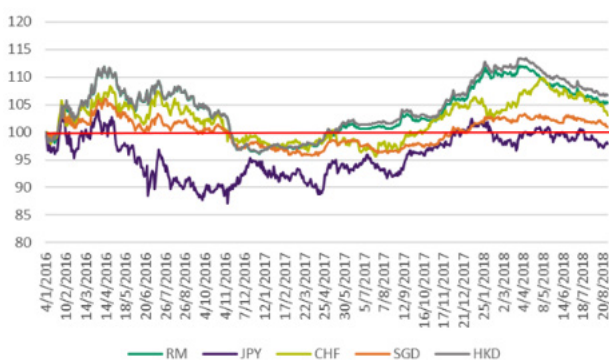
Headline inflation fell to 1.3 per cent in Q2 2018 (Q1 2018: 1.8 per cent). The decline was primarily due to the tax holiday due to the zerorisation of the GST rate pending being abolished and replaced with the new Sales and Services Tax (SST).

Figure 2: Consumer Sentiments Index (CSI)



Source: Malaysian Institute of Economic Research, NTL Research

Figure 3: Exchange Rate Index of Main Trading Partners of Malaysia vs USD



Source: Bank Negara Malaysia, NTL Research

The labour market in the second quarter of 2018 remained complementary to growth. The growth of the labour force was in line with the growth of net employment gains, which reflected the unchanged unemployment rate of 3.3 per cent.

The euphoria of a New Pakatan Harapan Administration after the May 9 General Election has lifted consumer confidence. The Consumer Sentiment Index recorded a 21-year high of 132.9 points in Q2 2018. This is the first time the index has surpassed the 100-point threshold since Q2 2014 (Figure 2). However, the cancellation of major and controversial rail infrastructure projects, such as the East Coast Rail Link (ECRL) and High-Speed Rail (HSR), and budgetary constraints will hurt growth in the short term as well as create new political risks for the private sector.

Between 30 March and 29 June 2018, the Ringgit depreciated by 4.57 per cent against the US dollar (Figure 3). This was in line with other regional currencies which was a result of the normalisation of the US monetary policy.

## Outlook

In light of external uncertainties and a slowing global economy, the Central Bank, Bank Negara Malaysia, has revised the GDP forecast for 2018 downwards to 5.0 per cent from 5.5 to 6.0 per cent and has continued to maintain a stable monetary policy to support economic activities.

# Investment sales

## Key highlights

- Sales volume declined by 2.0 per cent to RM649.6m, dominated by retail and industrial assets (Figure 4).
- Sales were driven by winding down of a real estate fund and a corporate restructuring of a media group.
- Local REITs and trust funds continued to be major buyers, due to access to liquidity and funding.
- Threat of emerging market contagion and currency volatility were affecting foreign interest, and making local buyers more cautious in the light of a slowing economy and escalation of a Transpacific trade war.

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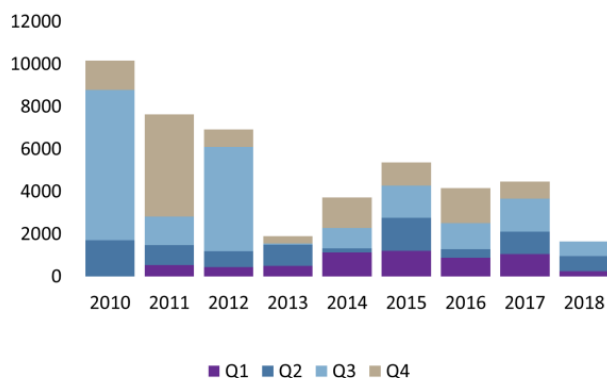
Local REITs and trust funds continue to have liquidity and access to funding.

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## Market commentary

The market is settling down to the post-election's realities of an economic slowdown. Total deals registered a value of RM649.6m, down by 2.0 per cent q-o-q (Figure 4). Several major deals in the retail sector were announced. This included the sale of Kinta Shopping Centre, Ipoh and a pending deal on Setapak Sentral Mall in Kuala Lumpur. These assets form part of an ongoing unwinding of a retail real estate fund managed by Pramerica Global Investment Management, which owns a portfolio of malls in Malaysia and the region.

Figure 4: Investment sales (RM m)



Source: NTL Research

The other major transaction involved the corporate restructuring of Media Prima Group (MPG), which sold a portfolio of three properties to PNB Development, a major GLC trust fund. These include an industrial asset that comprises a printing facility, Balai Berita Shah Alam, and another office property Balai Berita Bangsar. MPG is an UMNO-linked company and has been suffering from losses in recent years. This sale and lease back were achieved at a yield of 6.2 per cent and 7.3 per cent respectively. Thai-listed Strategic Hospitality Extendable Freehold and Leasehold Real Estate Investment Trust (SHREIT) purchased the Hilton Garden Inn at Jalan Tunku Abdul Rahman from Knights Bridge Avenue at RM240m (Table 1).

Table 1: Investment sales

Development	Buyer	Vendor	Price (RM m)
Aeon Mall Kinta City (Ipoh)	KIP REIT	Kinta City Sdn Bhd	208.0
Balai Berita Bangsar	PNB Development	New Straits Times Press (Malaysia) Berhad	118.7
Balai Berita, Shah Alam	PNB Development	New Straits Times Press (Malaysia) Berhad	127.9
Hilton Garden Inn, KL	SHREIT	Knights Bridge Avenue Sdn Bhd	240.0

Source: NTL Research

From the analysis of the buyers, these are mainly domestic listed REIT or trust funds, which continue to have the liquidity to pursue portfolio expansion. We also noted that ARA, which was formerly a shareholder in AmARA REIT, will be pursuing an IPO for their existing Malaysian portfolio.

The benchmark lending rate (BLR) remained unchanged but has a negative rating on prospect for the property sector due to general oversupply. Funding in the short-term is expected to be difficult.

## Outlook

With emerging markets upheavals in the limelight, foreign investments will be sidelined for the time being. The Ringgit is still trying to settle down to a more a stable range but this has been recently affected by external developments and contagion threats from other parts of the world. There is still a net outflow of funds since GE14.

The market will have to depend on local funds to drive activities but even these players will be cautious in such a volatile environment. The escalating trade war between China and the US is also creating more uncertainties.

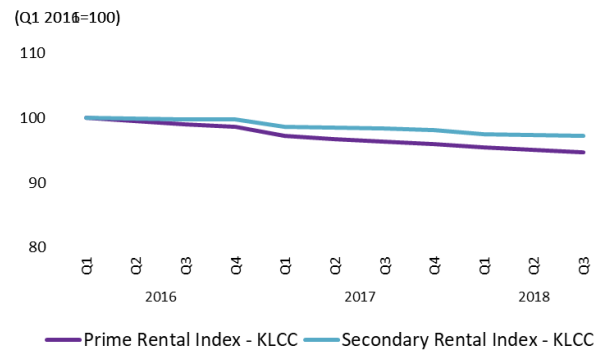
# Office

## Key highlights

- Q3 saw the completion of 870,000 square feet (sq ft) of office space, all of which are located within the KL Fringe.
- The prime office rent index in Kuala Lumpur City Centre (KLCC) registered a drop of 0.4 percent (Figure 5).
- The average occupancy rate in KL was 81.0 per cent, a slight drop from 82.0 per cent in Q2, as absorption rate lagged supply growth (Figure 6).
- Average prime rent in KLCC stood at RM7.30 per sq ft.

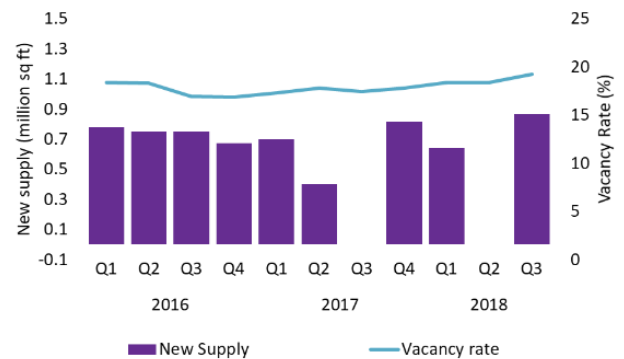
Office market remains competitive as supply continues to outstrip demand, leading to higher pressure on occupancy and rental rates.

Figure 5: Prime & secondary rental indices – KLCC



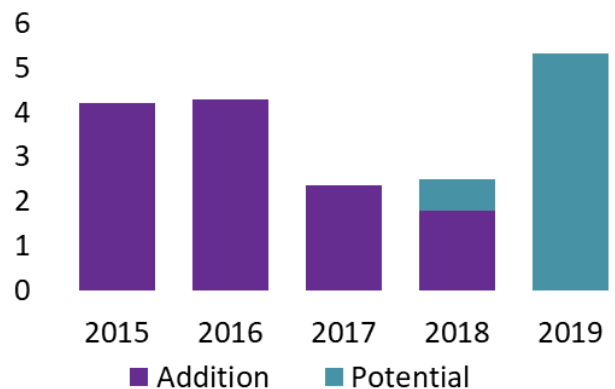
Source: NTL Research

Figure 6: Office vacancy rate



Source: NTL Research

Figure 7: Future pipeline supply (sq ft, m)



Source: NTL Research

## Market commentary

Two major office buildings were completed including Etiqa Bangsar with 380,000 sq ft of Nett Lettable Area (NLA) and Southpoint Mid Valley with 490,000 sq ft of NLA, located within KL Fringe. The low absorption of newly completed buildings had contributed to a marginal drop in average occupancy rate. Total completions for the entire year are expected to be approximate to 2017 at about 2.4 million sq ft (Figure 7).

In Q3 2018, the prime office rent index in KLCC dropped 0.4 per cent, with an average of RM7.30 per sq ft, while secondary rent in KLCC remained stable at RM5.25 per sq ft. In KL Sentral, average rent was recorded at RM6.85 per sq ft.

Increasing enquiries and leasing activities from serviced office and co-working operators looking to set up new offices or for expansion are noted in this quarter. International operator, WeWork, is expected to open its first co-working space in Kuala Lumpur by end of this year, while local operators have been actively

expanding to KL Fringe (KL Sentral and KL Eco City) or Selangor.

To date, Invest KL has attracted 73 MNCs, which collectively have taken up more than 700,000 sq ft of office space. Moving forward, Invest KL aims to secure more MNCs to achieve its target of 100 MNCs by 2020, indicating more potential demand for the office market.

## Outlook

Major office projects undertaken by Government-Linked Companies (GLC) under construction were unaffected by the austerity drive of the new Government despite initial uncertainties. The Business Conditions Index (BCI) remained above optimism threshold of 100 points albeit the decline by 7.5 points to 108.8 points in Q3. Office space demand is expected to improve only when there is clarity on new major initiatives from the Government on how it intends to drive more inward foreign direct investments (FDI) into the country. Unfortunately for the market, this may need some time before any impact can be felt.



# Retail

## Key highlights

- Retail sales recorded a lower-than-expected growth of 2.1 per cent for Q2 2018.
- As of Q3 2018, total existing supply of shopping malls in Klang Valley stood at 52.1m sq ft.
- Eko Cheras Mall commenced operation in mid-September with 625,000 sq ft of NLA with an official opening expected in Q4 2018.
- Retail mall occupancy within KLCC is estimated at 93.0 per cent, whereas the Outer City Centre (OCC) district and Other City Area (OCA) lingered at 85.0 per cent and 90.0 per cent respectively.
- Overall occupancy for shopping malls in Klang Valley is estimated at 89.0 per cent.

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Consumers' optimism was not matched by the growth of retail sales.

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## Market commentary

The positive trend in consumer sentiments gathered momentum in Q2 2018. The CSI recorded a strong uptick of 41.9 points to 132.9 points, possibly due to post-election euphoria and the promise of the removal of the unpopular GST. The CSI breached the threshold level of 100 points and recorded the highest level since two decades ago.

Nevertheless, retail sales in Q2 recorded a growth of only 2.1 per cent, far below the previous expectation of 6.0 per cent. The growth was also lower than 4.9 per cent reported in Q2 2017. Retail sales were unexciting throughout the major Raya festival in June and only spiked during the final week of August during the two-month tax holiday when GST was zero-rated before its removal.

With the rapidly changing market dynamic, more traditional stores are shutting down. Recently, local music store, Rock Corner, closed its last standing store in The Gardens Mall as major music labels are now focusing on a more sophisticated and engaging medium – streaming. Similarly, Pablo Cheese Tart shuttered both its outlets in Malaysia. The seven-year-old chain originated from Japan and entered the Malaysia market in 2016 before exiting in July this year. Likewise, AEON has announced it will close its Index Living Mall Malaysia (ILMM) furniture outlets by the end

of Q3. The outlets were present in Aeon Shah Alam and Kota Bharu, IOI City Mall in Putrajaya, as well as Aeon Mall Tebrau City in Johor.

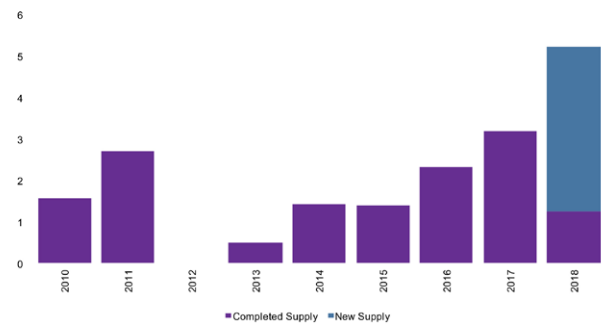
Despite the widely-chanted “retail apocalypse”, more foreign retailers have shown deeper interest in Malaysia’s market. British sporting goods retailer, Sports Direct, has recently expanded and opened a flagship store of 41,000 sq ft in Petaling Jaya. Australian-based Harvey Norman announced an expansion plan of over 40 new stores within the next five to 10 years. Similarly, A&W Malaysia is planning for seven new branches nationwide by year-end. Meanwhile, new entrant, New York-based athletic retailer, Foot Locker, has announced its expansion plan in Asia, which includes a store in Kuala Lumpur by Q4.

## Outlook

High household debt remains a concern, and the recent increase in minimum wages by RM50 to RM1050 is expected to have minimal impact to spending, and this could be countered by a proposed reduction in Bantuan Sara Hidup Rakyat (BSHR) quantum and eligible recipients.

Retail Group Malaysia has revised Q3 retail sale downward to 6.1 per cent from the 6.8 per cent estimated in June, reflecting the reintroduction of SST on 1 September. Overall sales forecast for the entire year has been revised lower to 4.1 per cent from the estimated 5.3 per cent.

Figure 8: Development pipeline supply (NLA) in KL (sq ft, mil)



Source: NTL Research

Table 2: Selected upcoming malls in Klang Valley by 2018

Development	Net Lettable Area	Est TOP
GM Bukit Bintang	122,000	KLCC
Retail Park @ Kiara 163	300,000	OCC
KIP Mall Desa Coalfields	250,000	OCA
Empire City Damansara	2,500,000	OCA
Skypark @ Cyberjaya	565,000	OCA
Pacific Star, PJ	240,000	OCA

Source: NTL Research

# Residential

## Key highlights

- Four high-end residential projects in the city centre with a total of 1,177 units were completed in Q3. The completed projects are Four Seasons Private Residences (240 units), Tropicana The Residences (353 units), The RuMa Residences (200 units) and Anggun Residences (384 units) (Table 3).
- The number of completions accounted for 34.0 per cent (2,093 units) of the pipeline for 2018 as of Q3, with some 4,083 units slated for completion in Q4 2018. About 49.0 per cent of the upcoming supply will emanate from the city centre (Figure 9).
- Prices and rents for high-end strata homes stood at RM1,040 per sq ft and RM3.78 per sq ft per month respectively.

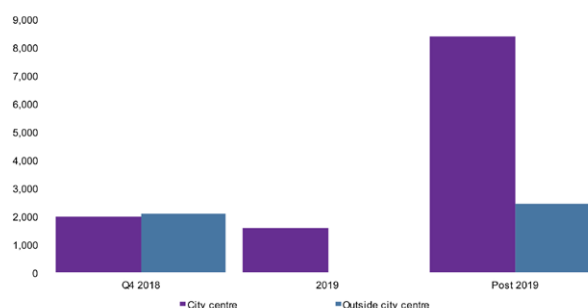
After its first 100 days in power, the PH Government has done many fiscal reforms to achieve sustainable investment climate and economic growth.

Table 3: Completed projects

Development	Sizes (sq ft)	Developer
Four Seasons private Residences	1,098 – 7,039	Venus Assets Sdn Bhd
Tropicana The Residences	710 – 1,604	Tropicana Corporation Bhd
The RuMa Residences	915 – 1,830	Aseana Properties Ltd and Ireka Corp Bhd
Anggun Residences	657 – 1,535	One JSI development Sdn Bhd (Subsidiary UDA Holdings Bhd)

Source: NTL Research

Figure 9: Future supply of high-end condominiums in KL



Source: NTL Research

## Market commentary

As overall sales continued to decline, developers were more cautious in launching high-end residential projects due to the shifting needs of the residential market, moving towards the middle-income segment and affordable housing. The new Pakatan Harapan (PH) Government's election manifesto has various initiatives to address critical issues involving home-ownership, especially among the middle-income households and millennials. Some examples are to build one million affordable homes and the introduction of a special housing loan scheme to encourage youth to buy their first home.

Developers continued to refine and introduce various marketing strategies to clear their completed and unsold stocks by offering attractive discounts and incentives, such as payment terms.

The number of overhang residential properties priced above RM1m in Kuala Lumpur in Q2 2018 increased by 10.7 per cent compared to Q1 2018. Overhang property are completed units that remain unsold after nine months or more.

In light of a weak long-term rental demand, residential investors are offering their units for Airbnb accommodation to generate returns.

Smaller-sized units continued to dominate the market as affordability remains the key issue in home-ownership.

In certain locations, asking prices and rentals remained depressed especially for old and/or matured developments, where units have a typically large built-up area. Developments along infrastructure projects, such as MRT and LRT lines, are expected to hold their value.

## Outlook

Although several economic indicators show signs of picking up, the overall high-end residential market is expected to remain subdued given the existing excess of the high-end segment and growing uncertainty in the external environment.

New launches are now focused on offering residential units around the RM500,000 price range in view of the affordability issue and tight credit environment.

Most of the demand are from purchasers buying for own stay while investors remain on the sidelines.

A new and strong public/private partnership will be needed to address price affordability if this segment is to drive the recovery in the residential market.

# Definitions

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<b>Development pipeline/potential supply:</b>	Comprises two elements: <ol style="list-style-type: none"><li>1. Floor space in the course of development, defined as buildings being constructed or comprehensively refurbished.</li><li>2. Schemes with the potential to be built in the future, having secured planning permission/development certification.</li></ol>
<b>Net absorption:</b>	The change in the total occupied or let floor space over a specified period of time, either positive or negative.
<b>Net supply:</b>	<p>The change in the total floor space over a specified period of time, either positive or negative. It excludes floor spaces that are not available for occupation due to refurbishment or redevelopment, but includes new supply.</p> <p>New supply refers to total floor space/units which are ready for occupation. Ready for occupation means practical completion, where either the building has been issued with a Temporary Occupation Permit or Certificate of Completion and Compliance (CCC).</p>
<b>Prime office rent:</b>	<p>The highest rent that could be achieved for a typical building/unit of the highest quality and specification in the best location to a tenant with a good (i.e. secure) covenant.</p> <p>(NB. This is a gross rent, including service charge or tax, and is based on a standard lease, excluding exceptional deals for that particular market).</p>
<b>Stock:</b>	<p>Total accommodation in the private sector both occupied and vacant:</p> <ol style="list-style-type: none"><li>1. Purpose-built office buildings with Net Lettable area (NLA) of at least 150,000 sq ft.</li><li>2. Purpose-leased shopping centers, excluding hypermarket and stratified retail.</li><li>3. Non-landed residential projects with at least 10 strata dwelling units.</li></ol>
<b>Take-up:</b>	<p>Floor space acquired for occupation or investment, including the following:</p> <ol style="list-style-type: none"><li>1. Offices let to an eventual occupier.</li><li>2. Developments pre-let or sold.</li></ol> <p>(NB. This includes subleases)</p> <p>Take-up also refers to units transacted in the residential market.</p>
<b>Occupancy rate:</b>	Total space currently occupied or not available to let as a percentage of the total stock of floor space (NB. This excludes shadow space which is space made available for sub-leasing).
<b>KL City Center</b>	An area bordered by Jalan Tun Razak – Lebuhraya Sultan Iskandar – Jalan Damansara – Jalan Istana.
<b>Outer City Center</b>	An area that refers to the Federal Territory of Kuala Lumpur, excluding the area of KL City Centre.
<b>Other City Area</b>	An area comprising the districts of Petaling, Gombak, Klang, Hulu Langat, and Sepang in Selangor, and Federal Territory of Putrajaya.

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