

RESEARCH

February 2019

Kuala Lumpur Q4 2018

Market's cautious mode persists



Q4 2018 snapshot

The national economy grew at a slower rate of 4.4 per cent year-on-year (y-o-y) in Q3 2018. Continuous supply disruptions in the mining sector and lower agriculture production remained the main contributors to the slowdown.

Investment

Investment sales eased to
RM663.8m
from RM694.6m¹ in Q3 2018.

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

Office



The office absorption remained slow. Its average occupancy rate dropped slightly to **80.0 per cent**.

Retail



Occupancy of malls in Klang Valley improved, **estimated at 91.0 per cent**.

Residential



Prices and rents for high-end condominiums eased marginally by 2.2 per cent and 0.1 per cent quarter-on-quarter (q-o-q) to **RM1,017 per square foot (psf)** and **RM3.77 psf per month** respectively.

¹ The investment value reported in Q3 2018's publication was RM649.6m. It should have been RM694.6m.

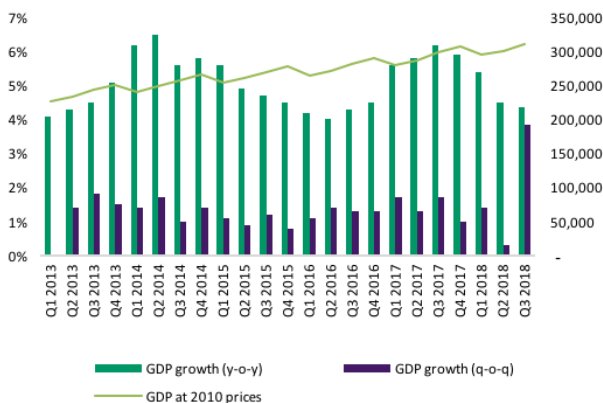
The economy

Key highlights

- The Malaysian GDP grew by 4.4 per cent in Q3 2018, 0.1 per cent lesser than Q2 2018.
- Unemployment remained unchanged for three consecutive quarters at 3.3 per cent.
- In Q3 2018, headline inflation declined to 0.5 per cent from 1.3 per cent in Q2 2018.
- Consumer Sentiment Index (CSI) slipped to 107.5 in Q3 2018 from 132.9 in Q2 2018.
- Ringgit remained on a downward trend, depreciating by 3.6 per cent in Q3 2018.

Private sector spending is pivotal to Malaysia's economic growth.

Figure 1: Malaysia GDP growth and unemployment



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

Market commentary

The national economy grew at a slower rate of 4.4 per cent y-o-y in Q3 2018, which was 0.1 per cent lower than the previous quarter. On a q-o-q seasonally adjusted basis, Malaysia's economy grew by 1.6 per cent in Q3 2018, 1.3 per cent more than Q2 2018 (Figure 1).

Domestic demand was reported as the top performer in the Malaysian economy, backed by the significant growth of private consumption at 9.0 per cent y-o-y compared to 8.0 per cent y-o-y in Q2 2018. This is mainly due to the zero-rating of the Goods and Services Tax (GST) on 1st June 2018 before the reinstatement of a less broad-based Sales and Services Tax (SST) in early September.

The manufacturing and services sectors remained pivotal to Malaysia's economy, while the mining sector slowed down due to the production shocks it endured. The manufacturing sector grew by 4.3 per cent, compared to the 5.2 per cent in Q2 2018; while the services sector was supported by the growth of wholesale and retail trade, accommodation and restaurants with a 1.8 per cent growth; transport, storage and communication with a 3.2 per cent growth and finance, insurance, real estate and business services with a 2.3 per cent growth. The mining and quarrying, and agriculture sectors contracted by 1.3 per cent in Q3 2018.

Malaysia's headline inflation declined by 0.8 per cent to 0.5 per cent in Q3 2018, continuing the impact of the GST zerorisation. The implementation of the SST has yet to show its impact on the country's inflation. Employment in Malaysia remained healthy with the unemployment rate remaining at 3.3 per cent for three consecutive quarters.

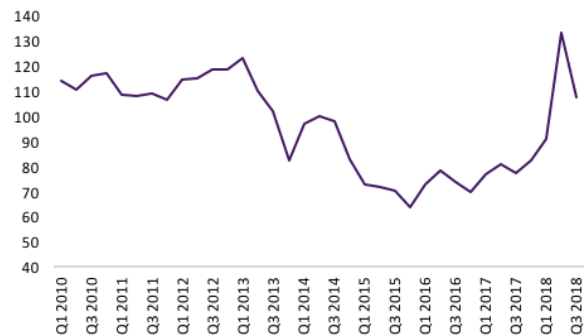
The CSI indicates that consumers were less optimistic as the General Election euphoria seemed to have subsided. CSI slipped to 107.5 points from 132.9 points in Q2 2018, even though it was above the 100 points threshold of optimism (Figure 2). Consumer spending is expected to be more selective in the upcoming quarters. The Business Conditions Index (BCI) also pointed to a slower optimism from the previous quarter of 116.3 points to 108.8 points. Business is still optimistic, as it is supported by sales that grew by 1 point, new domestic orders that expanded by 9.3 points, and new export orders that increased by 10 points.

The volatility in global crude oil prices and the anticipation of an interest rate hike by the US saw the ringgit depreciating by 3.6 per cent to an average of RM4.09 at the end of Q3 (Figure 3).

Outlook

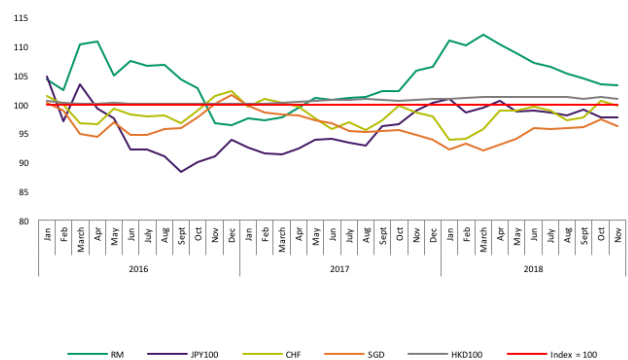
Considering external uncertainties and a slowing global economy, the Government has revised its 2018 GDP growth forecast downwards to 4.8 per cent from 5.5 per cent. Despite the short-term uncertainties, growth will remain supported by sustained domestic demand moving forward.

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

Investment sales

Key highlights

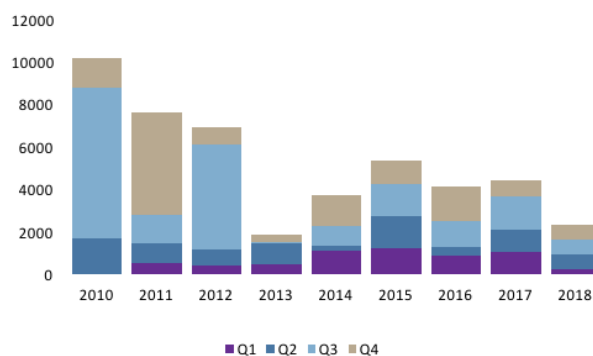
- Sales volume for Q4 2018 declined by 4.0 per cent q-o-q to RM663.8m, dominated by educational and industrial sales (Figure 4).
- The private education sector is becoming an area for diversification by funds.
- Disposal of non-core assets by Government-Linked Companies (GLCs) has increased buying opportunities and assets in the market.
- Stabilised national macroeconomic parameters and maintained credit rating will continue to cushion the economic growth.

Buying opportunities are increasing as more assets are coming into the market especially those held by GLCs such as Felda, Tabung Haji and Khazanah.

Market commentary

The investment market ended the year on a restrained note. Nine deals totalling RM663.8m were recorded, with a decrease of 4.0 per cent q-o-q in the quarter under review. The cumulative value of 2018 deals was RM2.47b, about half of 2017's figure. This was expected as the year had been relatively challenging both from a property sectoral basis as well as from a broader economic perspective. Interestingly, most of the deals are outside of the Klang Valley. Of which, three are from the private educational sector, which has grown over the years, becoming an area for diversification by funds. A portfolio of three KDU University colleges, a subsidiary of Paramount Corporation Bhd, formed part of a sale and leaseback, and securitisation deal injected into a special purpose vehicle.

Figure 4: Investment sales (RM m)



Source: NTL Research

Another major deal was the sale of an old Nestle factory in Petaling Jaya valued at RM120m, together with the existing business of chilled sauce manufacturing to Lactalis Trading. Unlike other deals in the neighbourhood that were redeveloped as mixed-use projects, the premise will remain an industrial site.

Since its listing, Atrium REIT captured this quarter's limelight as the only REIT to do a sale and leaseback deal on two assets in Penang with Lumileds at RM180m.

Buying opportunities are increasing as more assets are coming into the market, especially those held by GLCs such as Felda, Tabung Haji, and Khazanah. They are restructuring under new management and disposing their non-core assets, locally and overseas.

Outlook

While the key national macroeconomic parameters are stable with credit ratings being maintained, external uncertainties such as Brexit and the US-China trade war continue to muddy the waters. It is hoped that the political situation will settle down and provide greater stability for charting the new national agenda.

Table 1: Investment sales

Development	Buyer	Vendor	Price (RM m)
Nestle PJ Factory	Lactalis Trading Malaysia Sdn Bhd	Nestle Products Sdn Bhd and Nestle Manufacturing (M) Sdn Bhd	120.34
Bayan Lepas FIZ Phase 3 and Bayan lepas Industrial Park Phase 4	Atrium REIT Managers Sdn Bhd	Lumileds Malaysia Sdn Bhd	180
KDU Jalan Ansom Campus	Dynamic Gates Sdn Bhd	KDU Penang and KDU University College	24.7
KDU Batu Kawan Campus	Dynamic Gates Sdn Bhd	KDU Penang and KDU University College	117.2
KDU Utropolis Glenmarie Campus	Dynamic Gates Sdn Bhd	KDU Penang and KDU University College	171.8

Source: NTL Research

Office

Key highlights

- Q4 2018 saw an addition of approximately 700,000 sq ft of net leasable area (NLA), totalling 81.8m sq ft in Kuala Lumpur.
- The average occupancy rate in Kuala Lumpur dropped to 80.0 per cent, from 81.0 per cent in Q3 2018.
- Prime office rental index in Kuala Lumpur City Centre (KLCC) further dipped from RM7.33 per sq ft to RM7.21 per sq ft.
- Capital value and yield remain unchanged.

The office market remains subdued as the market is still finding its way to a state of equilibrium.

Market commentary

There were two major completions in the quarter – Equatorial Plaza (KL City Centre) and Sunway Visio Tower (KL Fringe), at 460,000 sq ft and 243,000 sq ft respectively. These led to the total completion of 2.5m sq ft in 2018, a 6.0 per cent increase from 2.35m sq ft in 2017.

Q4 2018 also saw the completion of two TRX towers - The Exchange 106 and Prudential Tower. Although they are slated to officially operate in 2019, the Certificate Completion and Compliance (CCC) has not been issued for both buildings.

Within the next three years, about 14m sq ft of office space is scheduled to be delivered, adding competition to existing stock.

The prime office rental index in KLCC dropped by 1.6 per cent to RM7.21 per sq ft, while its secondary rental index in remained steady at RM5.25 per sq ft respectively. On the other hand, the rental index in KL Sentral increased by 0.6 per cent to RM6.90 per sq ft. The yield remained at 6.25 per cent.

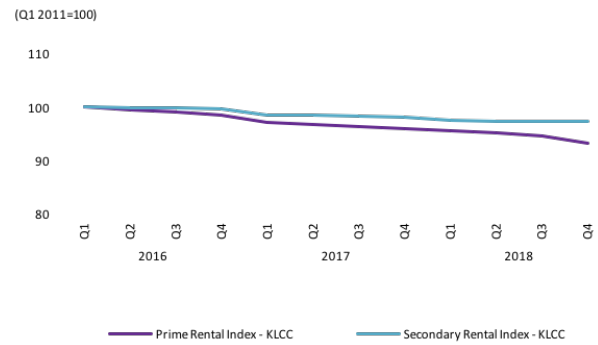
Serviced office and co-working operators continued to be active in their expansion. Hong Kong-based co-working operator, Compass Offices, opened a 30,000 sq ft co-working space at Menara Standard Chartered, while The We Company, the first American co-working space in Malaysia, is set to open its doors in early 2019 with a total NLA of approximately 100,000 sq ft.

Outlook

According to the World Bank’s Doing Business 2019 Report, Malaysia is ranked at 15th place, a jump from 24th place in 2018. The Government introduced more initiatives to improve business competitiveness via the Special Task Force to Facilitate Business (Pemudah), such as tax refunds and higher efficiency for business application processes.

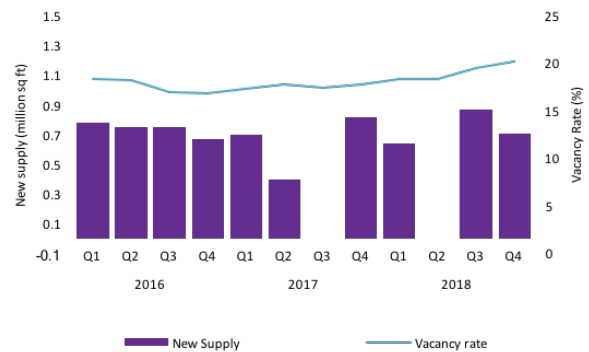
Moving forward, the demand for office space is expected to remain sluggish due to the lack of near-term catalysts. The office market is expected to remain favourable to tenants in the short- and medium-term given the volume of incoming supply. Short-term pains and uncertainties will remain for landlords as the market is still finding its equilibrium. Occupiers’ demand for office space is expected to improve when there is more clarity on major initiatives from the Government on how it intends to drive more foreign direct investments (FDI). Unfortunately, this may need some time before any impact can be felt in the market.

Figure 5: Prime & secondary rental indices – KLCC



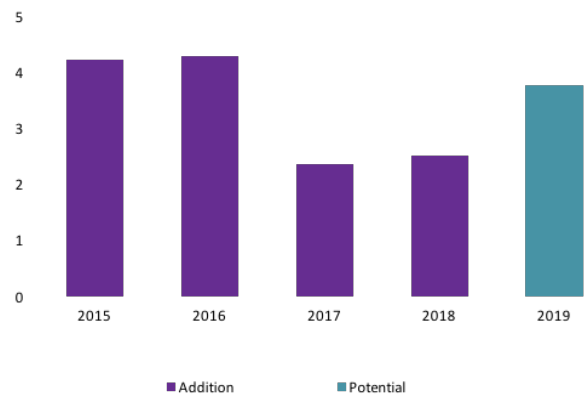
Source: NTL Research

Figure 6: Office vacancy rate



Source: NTL Research

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



Source: NTL Research

Retail

Key highlights

- Retail sales outperformed expectations of 6.1 per cent and recorded a growth of 6.7 per cent in Q3 2018.
- The existing supply of shopping malls in Klang Valley is recorded at 52.9m sq ft.
- 163 Retail Park opened its doors in November with 300,000 sq ft NLA.
- Average overall occupancy for shopping malls in Klang Valley improved from 89.0 per cent to 91.0 per cent q-o-q.

Retail sales in Q4 is estimated to expand more than earlier forecasted, backed by multiple shopping festivals.

Market commentary

The positive trend in the CSI remained, recording a 39.0 per cent increase y-o-y to 107.5 per cent in Q3 2018. This was reflected in retail sales, which grew by 6.7 per cent y-o-y in the same quarter. Performance was above expectations considering the tax holiday period between June and August.

Retail Group Malaysia (RGM) projected retail sales to expand to 4.7 per cent in Q4 2018, up from 4.3 per cent as estimated earlier, mainly driven by a streak of multiple shopping festivals and the festive Christmas season.

The shopping festivals include Singles' Day which originated in China, followed by Black Friday and Cyber Monday – a tradition in the US that has been adopted in Malaysia's retail culture as well as the recently-introduced 12.12 sales. While these shopping festivals have largely benefited e-commerce businesses in Malaysia, which is now a more mature market compared to its ASEAN counterparts, Black Friday has mostly been adopted by brick-and-mortar stores.

In November, the retail landscape welcomed the opening of 163 Retail Park with a NLA of 300,000 sq ft, located in Mont' Kiara. The mall is part of a freehold 6-acre mixed development, Kiara 163, which also consists of small office versatile office (SOVO) and hotel suites.

In the same month, Abdullah Hukum station within KL Eco City commenced operations, integrating KTM and Kelana Jaya-Abdullah Hukum LRT route. This further enhances the accessibility to the recently completed mixed development comprising of office space, residential towers, hotel and a mall. The mall, or better known as KL Eco City Mall with a NLA of 250,000 sq ft is anchored by Bangsar Market by Jaya Grocery, which is set to become the largest urban grocery market occupying the entire 54,000 sq ft of Level 2.

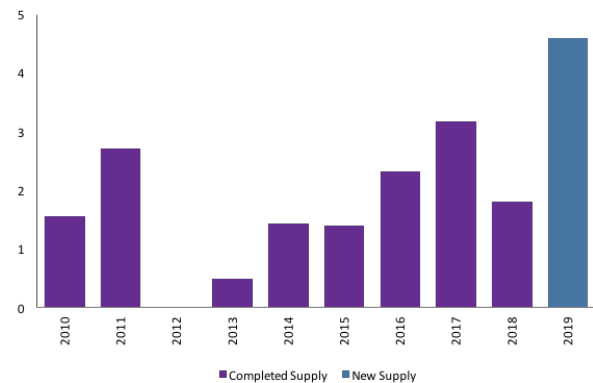
Outlook

Throughout 2018, Malaysia's retail sales have been on a roller coaster ride, recording a growth of 5.7 per cent in Q1, 2.1 per cent in Q2, 6.7 per cent in Q3, and an estimated of 4.7 per cent in Q4. 2018's forecast has been positively revised to 4.3 per cent from an earlier estimate of 4.1 per cent by RGM.

The payout of RM300 under the Government's 2019 Cost of Living Aid (Bantuan Sara Hidup) in January 2019 might have minimal impact on spending as consumers remains wary of economic uncertainties.

With household spending remaining as the anchor of Malaysia's economic growth, retail sales are forecasted to stabilise at 4.5 per cent in 2019.

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



Source: NTL Research

Table 2: Selected upcoming malls in Klang Valley by 2018

Development	Net Lettable Area (sq ft)	Location
Empire City Damansara	2,500,000	KLCC
Tropicana Gardens Mall	1,000,000	OCC
Central i-City	940,000	OCA
Datum Jelatek	491,000	OCA
Horizon Village Outlet	400,000	OCA
Setia City Mall (expansion)	400,000	OCA
Pacific Star	240,000	OCA

Source: NTL Research

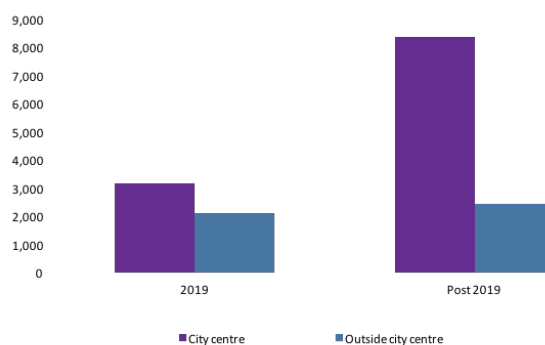
Residential

Key highlights

- The 369-unit Pavilion Suites was the only completed high-end residential project in the city centre.
- Out of 6,176 units that were scheduled to complete throughout the year, only 2,462 units or 40.0 per cent from six high-end residential projects were completed. Some 5,269 units of high-end condominiums are expected to come onboard throughout 2019, with 60.0 per cent of the upcoming supply from the city centre (Figure 9).
- Both prices and rents for high-end condominiums eased marginally by 2.2 per cent and 0.1 per cent q-o-q at RM1,017 psf and RM3.77 psf per month respectively (Figure 10).

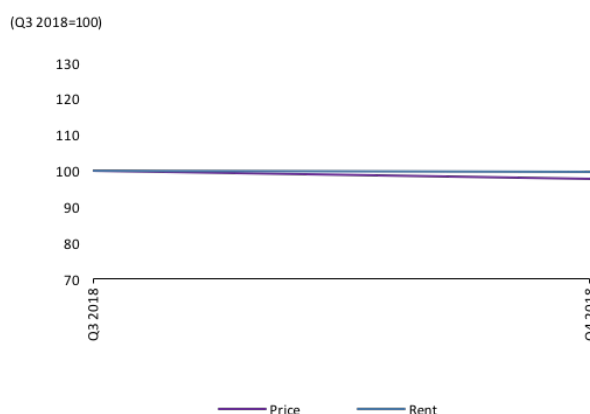
The recent upward-revision of Real Property Gains Tax (RPGT) and Stamp Duty rates are likely to further dampen sentiment in the short- to mid-term; hence slowing down property sales.

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



Source: NTL Research

Figure 10: Price and rental indices of high-end condominiums in KL



Source: NTL Research

Market commentary

Overall sales continued to decline as buyers and developers remained cautious despite some positive impact reported by NAPIC during the post-implementation of zero-rated GST in June, which saw an increase in overall buying trend from both primary and secondary markets. However, it only lasted for a short period as sales softened following the reintroduction of SST in September.

In tandem with a slowdown in sales, new launches followed suit, particularly with the high-end and luxury projects. Nevertheless, the quarter saw the launch of the world's first AccorHotel's lifestyle brand SO Sofitel. The SO Sofitel Kuala Lumpur Residences, located at Jalan Ampang, is part of Oxley Towers, an upscale project under construction, offering 590 branded serviced apartments. Launched at an average price of RM2,200 psf, the standard units are small- to mid-sized between 566 sq ft and 1,699 sq ft with duplexes/penthouses between 1,197 sq ft and 5,044 sq ft. The layouts vary from studio, 1- to 3-bedroom as well as a duplex/penthouse.

In the current highly competitive market, developers continue to introduce more attractive packages and innovative marketing strategies to clear overhang and unsold units,

including the revision of selling prices. Sime Darby Property Bhd is considering lowering its prices, especially for overhang units after registering a sharp drop in net profits for two consecutive quarters (ending 30 June 2018 and 30 September 2018) compared with net quarterly profits made in the same corresponding period last year. Meanwhile, local-based Mah Sing Group became the first developer in Southeast Asia to sell their properties online via a strategic collaboration with Alibaba-owned e-commerce platform, Lazada.

Outlook

Several tax adjustments announced in the National Budget 2019 include Government proposals to increase existing RPGT rates by an additional 5.0 per cent for disposals of properties or shares in property holding companies from the sixth year. The increasing Stamp Duty rates from 3.0 to 4.0 per cent for the transfer of properties worth more than RM1m is expected to dampen market sentiments in the short- to mid-term.

The move will slow down the already softened property sales. Hence, the residential market is expected to remain weak throughout 2019 as buyers and developers are likely to take on a wait-and-see attitude.

Definitions

Development pipeline/potential supply:	Comprises two elements: <ol style="list-style-type: none">1. Floor space in the course of development, defined as buildings being constructed or comprehensively refurbished.2. Schemes with the potential to be built in the future, having secured planning permission/development certification.
Net absorption:	The change in the total occupied or let floor space over a specified period of time, either positive or negative.
Net supply:	<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 that are ready for occupation. Ready for occupation means practical completion, where either the building has been issued with a Temporary Occupation Permit (TOP) or Certificate of Completion and Compliance (CCC).</p>
Prime office rent:	<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>
Stock:	<p>Total accommodation in the private sector both occupied and vacant:</p> <ol style="list-style-type: none">1. Purpose-built office buildings with Net Lettable area (NLA) of at least 150,000 sq ft.2. Purpose-leased shopping centers, excluding hypermarket and stratified retail.3. Non-landed residential projects with at least 10 strata dwelling units.
Take-up:	<p>Floor space acquired for occupation or investment, including the following:</p> <ol style="list-style-type: none">1. Offices let to an eventual occupier.2. Developments pre-let or sold. <p>(NB. This includes subleases)</p> <p>Take-up also refers to units transacted in the residential market.</p>
Occupancy rate:	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).
KL City Centre	An area bordered by Jalan Tun Razak – Lebuhraya Sultan Iskandar – Jalan Damansara – Jalan Istana.
Outer City Centre	An area that refers to the Federal Territory of Kuala Lumpur, excluding the area of KL City Centre.
Other City Area	An area comprising the districts of Petaling, Gombak, Klang, Hulu Langat, and Sepang in Selangor, and Federal Territory of Putrajaya.

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