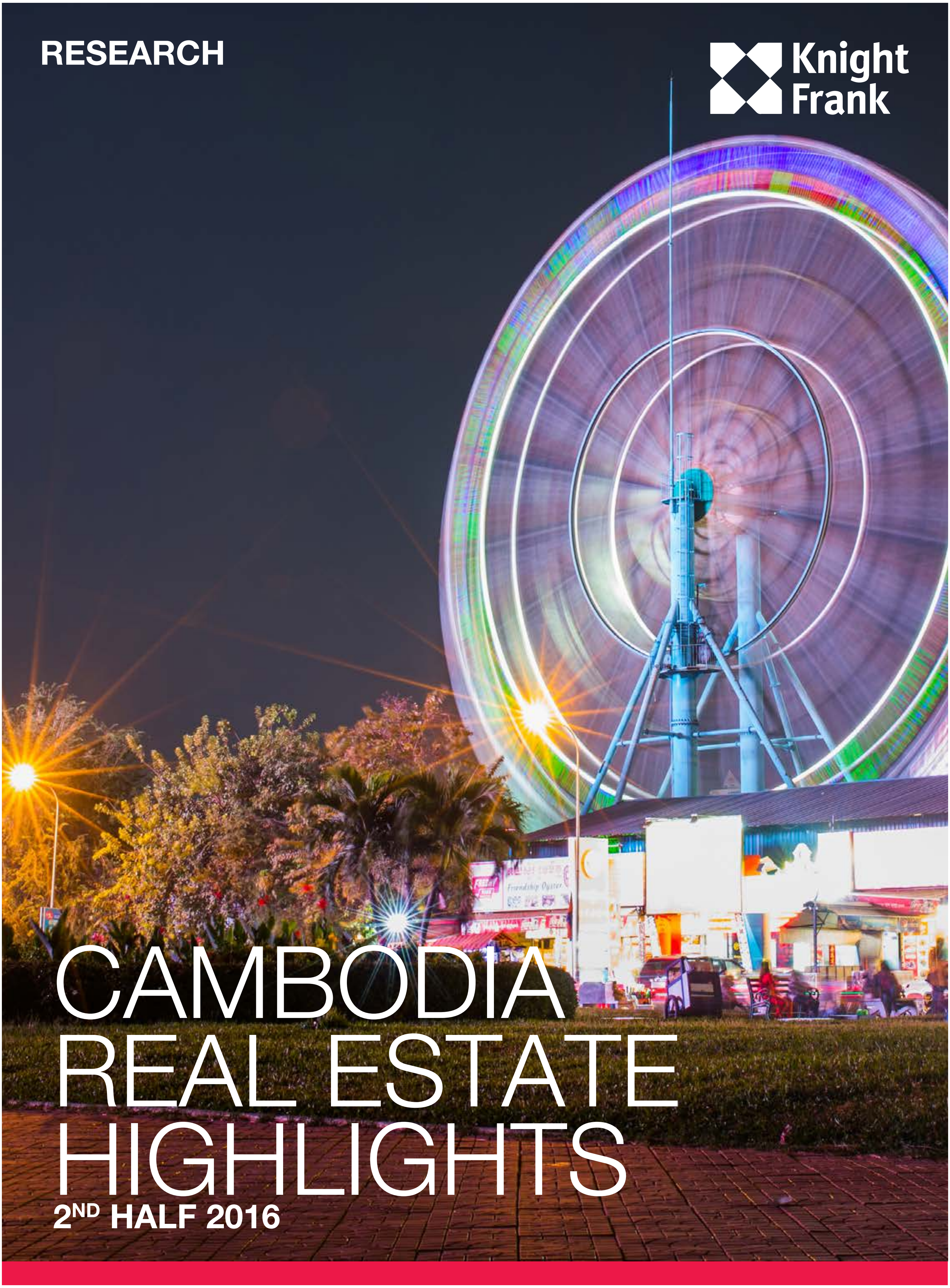


RESEARCH

Knight Frank

CAMBODIA REAL ESTATE HIGHLIGHTS

2ND HALF 2016

ECONOMIC SNAPSHOT | COMMERCIAL SECTOR | RESIDENTIAL SECTOR

ECONOMIC SNAPSHOT

On the back of a year that included Brexit, Donald Trump winning the US presidential election and a December US interest rate hike, Cambodia continued its rapid expansion

ROSS WHEBLE
Country Manager

"Whilst the global economic outlook is one of short to medium-term volatility, Cambodia continued on its upward trajectory."

2016 will go down as a historic year - whether for good or for bad - with the UK's shock vote to leave the European Union and Donald Trump's victory over Hillary Clinton in the US presidential election reverberating across the globe.

Furthermore, the US Federal Reserve announced in December that it would raise US interest rates by 0.25% and hinted at three more interest rate hikes throughout 2017, which saw the US Dollar reach a 14-year high.

The implications have been far reaching; similar to the impact of Brexit, the result of the US presidential election caused further uncertainty in terms of the global economic recovery and has weighed down on market sentiment.

However, whilst the global economic outlook is one of short to medium-term volatility, Cambodia continued on its upward trajectory underpinned by investment from China as part of its 'One Belt, One Road' policy.

Notable investments included the announcement that SRE Group, a subsidiary of China Minsheng Investment Group, will invest US$1.5 billion in developing the Cambodia-China Friendship City on 550 hectares within LYP Group's Garden City, located to the north of Phnom Penh.

2016 also saw a shift in focus away from Phnom Penh towards the coastal region of Sihanoukville including the announcement that Guangzhou R & F Properties will invest US$3 billion into the hospitality sector.

According to the Council for the Development of Cambodia, China invested US$4.9 billion in Cambodia between 2011 and 2015, and was the leading source of foreign investment into the Kingdom (figure 1).

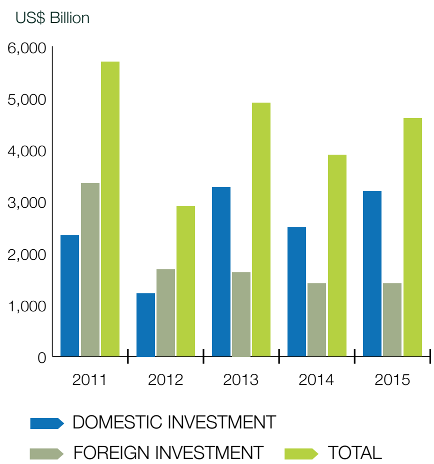
Whilst foreign investment continues to shore up economic growth in Cambodia, it is interesting to note that domestic investment has taken a leading role during the past few years (figure 2) and 2017 will be watched with much anticipation.

FIGURE 1
INVESTMENT CAPITAL BY COUNTRY (2011 - 2015)

COUNTRY	US$ Billion	%
CAMBODIA	12,527	57%
CHINA	4,919	22%
VIETNAM	1,204	5%
MALAYSIA	625	3%
KOREA	613	3%
OTHERS	2,113	10%
TOTAL	**22,001**	**100%**

Source: Council for the Development of Cambodia

FIGURE 2
TOTAL INVESTMENT IN CAMBODIA (2011 - 2015)



Source: Council for the Development of Cambodia

KEY FINDINGS

Phnom Penh's office space supply increased by 5,454 sq m in H2 2016 following the completion of TM 281 and Raintree.

Grade A and Grade B buildings make up the majority (96%) of the incoming office supply, with 185,198 sq m in the pipeline due for completion by 2020.

Office supply is expected to increase by 77% from 249,706 sq m to 441,539 sq m by 2020.

Cambodia will continue to benefit from Chinese outbound investment spurred by China's One Belt, One Road initiative, resulting in a steady inflow of Chinese companies that are likely to occupy space in purpose-built offices.

PHNOM PENH OFFICE SECTOR

Rental prices are expected to remain flat across all grades, with no significant changes expected from the demand side in the short-term

Supply and Demand

As developers shift from condominium to commercial projects, stratified offices now comprise a significant proportion (37%) of the incoming office space supply

Towards the second half of 2016, office space supply increased by 5,454 sq m upon completion of TM 281 and Raintree.

TM 281 is a 6-storey office addition to Tai Ming Hotel at the south end of Norodom Boulevard, while Raintree is a purpose-built community-centred boutique office building located in the CBD.

The completions of Exchange Square and City Tower Asia, which were initially scheduled for the second half of 2016, rolled over into the first half of 2017. Along with other ongoing projects, the two developments will introduce an additional 25,135 sq m of NLA.

As at H2 2016, completed office supply was 249,706* sq m, recording a 2.2% increase since H1 2016. By 2020, the office space supply is expected to increase by 77% reaching 441,539 sq m within the next four years.

Since Vattanac Tower's opening in 2014 only small to mid-scale office buildings have been completed, giving rise to a steady stream of office space supply which matches the current demand.

Larger projects such as East Commercial Centre and The Gateway are not expected to reach completion until 2018 to 2020, at which point there will be a substantial shift in the supply of office space. At least half of the future incoming supply is scheduled to reach completion by the end of 2018.

Of the total incoming supply, 77% (148,356 sq m) is Grade A , Grade B comprises 19% (36,842 sq m), while the remaining is Grade C office (6,635 sq m).The majority (63%) will be office for rent, while a significant proportion of the supply (37%) is stratified office units.

Net absorption of existing office space decreased significantly in H2 2016 compared with the same period in 2015

Overall occupancy showed a marginal increase QoQ from 81% in Q3 2016 to 82% in Q4 2016.

Occupancies for Grade B and C buildings were recorded at 87%and 88% respectively in Q2 2016. Grade A office occupancy has yet to reach 50%.

Net take-up for existing offices in H2 2016 was 1,970 sq m NLA, representing a signififcant decrease in net absorption when compared with the same period in 2015. The high net-take up in 2015 was due to the completion of ACLEDA building, which is fully owner-occupied as well as the opening of V-Trust Tower.

* KF has reviewed its database criteria and is now monitoring office buildings with a minimum of 4 levels, and 1,500 sq m of net lettable office space. Properties that were previously taken out of the basket that fit the revised criteria have now been readded.

The significant decrease in net absorption could be explained by a large proportion of the market share being captured by nearly-completed office buildings. Exchange Square, which will be adding 18,500 sq m of space to the office supply by mid-2017, has secured a number of pre-leases, which shows that there is demand for Grade A offices.

Prices and Rental

Average rental prices remained flat, recorded at US$18.0 per sq m per month

Asking rental prices remained flat, ranging from US$6.0 per sq m per month up to US$38.0 per sq m, with the majority asking below US$15.0 per sq m per month excluding taxes, services charge and utility charges.

The average rental price across all office grades was recorded at US$18.0 per sq m per month as at H2 2016. Prices for stratified office units remain flat from US$2,100 per sq m for Grade B units to as high as US$4,500 per sq m for Grade A units.

Office Sector Outlook

Asking rental prices are expected to remain flat in the short-term until the completion of major office buildings near Q2 2017. More flexible negotiation terms and better building management and standards will continue to benefit newly completed buildings at the higher end of the rental scale.

Demand for 100 – 200 sq m office space around the US$15.0 mark remains the highest, with banking, logistics and transport companies driving a large portion of the demand.

There are no significant movements expected in terms of demand across the sector with Grade B and Grade C office buildings expected to maintain their current occupancy levels at 85% and above.

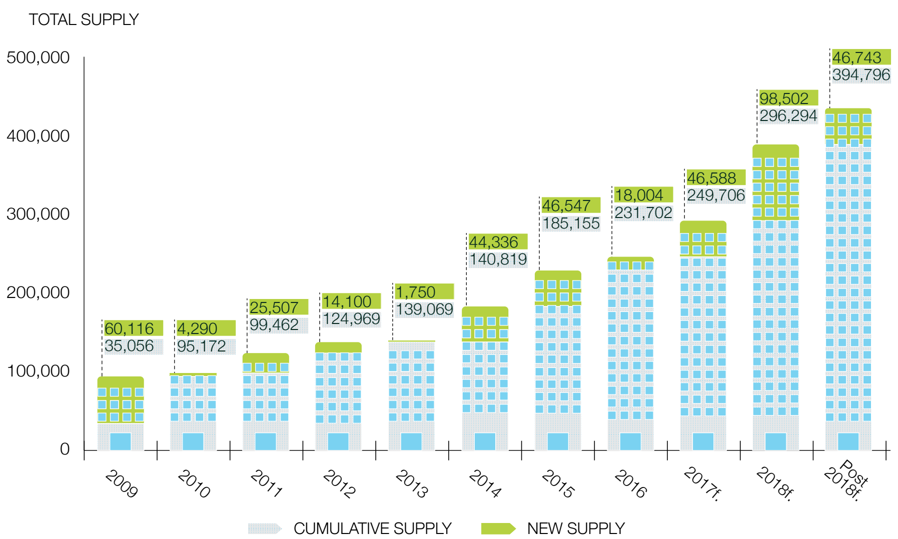
A good management team and adequate parking facilities are among some of the tenants' key considerations, which existing properties are delivering at a minimum standard. Paying greater attention and adhering to international standards will increase the chance of achieving and sustaining healthy occupancies in the long-run as the office sector expands and matures.

Regionally, there has been an influx of Thai companies that have entered Cambodia; among them is a proposed Thai SEZ along the Poipet border, Bangkok Life Assurance and Kasikorn Bank. The entry of industrial and financial companies into Cambodia shows Thailand's confidence in doing business in the Kingdom.

Cambodia will continue to benefit from Chinese outbound investment and aid promoted through the One Belt One Road initiative. Chinese companies, both state-sponsored and private, trickle into the market hoping to ride on the current real estate and construction wave. One such example is the recently announced deal between China Minsheng Investment Group (CMIG) and Ly Yong Phat Group (LYP Group), to build Cambodia-China Friendship City, an integrated development worth an estimated US$1.5 billion, on a 550 ha plot of land in the northern suburbs of Phnom Penh.

FIGURE 3

CUMULATIVE SUPPLY OF OFFICE SPACE IN PHNOM PENH (2008 – POST 2018f)



Source: Knight Frank Research

KEY FINDINGS

Supply of existing retail space in Q4 2016 was recorded at 138,154 sq m, distributed across 11 retail malls.

Rental prices remain flat with no significant movements within the retail sector since the opening of Aeon Mall and Vattanac Tower's retail podium.

Prices are likely to fluctuate closer to 2018, following the completion of large projects such as Parkson City Centre and Aeon Mall 2.

Occupancy across the sector remains high at 90%.

PHNOM PENH RETAIL SECTOR

International brands continue to trickle into Cambodia, with more expected to enter the market following the opening of Parkson City Centre and Exchange Square's retail podium

Supply and Demand

With completions of highly anticipated projects being delayed, the retail sector did not see any of the significant changes that were expected by the second half of 2016

By 2017, Exchange Square and Parkson City Centre are expected to come on stream adding 76,200 sq m of quality retail space to the market.

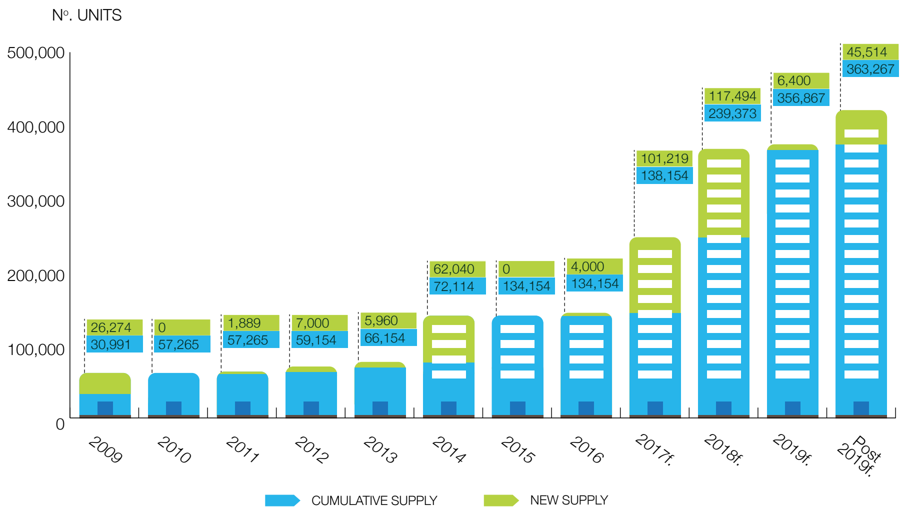
A 196% increase in the retail space supply is expected by 2020, with an additional 270,627 sq m of space spread across 9 properties scheduled to reach completion within the next 3 years.

Occupancy for prime retail properties remains healthy at 95%, with Aeon Mall keeping overall occupancy levels high with its ability to attract new tenants.

Aeon Mall 2, which will add 70,500 sq m of NLA to the retail space supply, commenced its construction shortly after it was announced, and is scheduled to be operational by 2018. The project has started to attract the attention of investors who are keen to capitalise on the expected increase in traffic in the surrounding area.

Although official plans have yet to be released, retail supply could potentially be added as part of two underground parking structures that are being built by OCIC, Canada's real estate arm, and Vattanac Capital. Both have announced the possibility that part of the space will be allocated for retail shops.

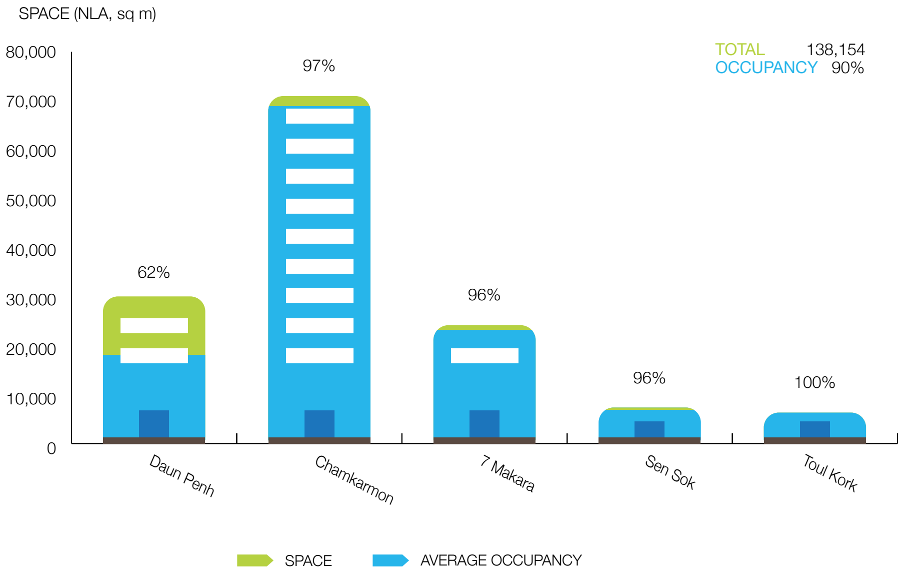
FIGURE 4
CUMULATIVE SUPPLY OF RETAIL SPACE (2009 – POST 2019f)



Source: Knight Frank Research

FIGURE 5

EXISTING SUPPLY BY DISTRICT AND OCCUPANCY RATE



Source: Knight Frank Research

A few older generation malls continue to undergo rebranding, while the rest remain relatively unchanged. These projects tend to suffer the most in terms of occupancy.

Brands continue to enter and expand into the Cambodian market, many of which are coming from within the region. A good example is the Thai coffee chain Amazon owned by PTT Plc, which since entering the market in 2013 has already opened up 14 branches across prime locations in Phnom Penh.

F&B brands, particularly those already operating within the region in Singapore, Malaysia or Thailand, are generally better received by the market and tend to be more successful compared to specialty retail outlets.

Prices and Rental

Rental prices likely to fluctuate following the completion of new projects by mid-2017

Rental for prime retail space has been relatively flat given the lack of significant changes in the supply and demand. Average prime rental prices range from US$32 to US$70 per sq m per month, with Vattanac Capital's retail podium commanding the highest rates.

Asking rental prices for secondary retail space vary from US$10 to US$20 per sq m per month for anchor tenants and US$15 to US$50 per sq m per month for specialty outlets.

Retail Sector Outlook

Supply risks outpacing demand in the short term, with current demand matching available supply

Cambodian consumers' preferences and consumption behavior continue to evolve as a clear middle-class group emerges. Brands that have entered Cambodia recently tend to offer mid-range products given that demand is still largely driven by this segment of the population.

Whilst the overall average occupancy rate remains high, there's a risk that supply will outpace demand for purpose-built retail space in the short term, with 9 projects expected to come on stream in the next three years.

With the availability of centrally located villas that can easily be converted to commercial space, many retailers still choose this option because of lower associated costs and greater flexibility.

Retailers will likely continue to create stand-alone outlets in popular residential areas, as high-rise residences go up in areas such as Chamkarmon and Toul Kork, which will allow them to tap into a growing residential community.

While the growing number of condominiums presents an attractive prospect to many retailers, the ongoing construction, which further increases congestion in areas like BKK1, is becoming a significant deterrent for some.

Purpose- built malls could benefit from this in the short to medium-term as congestion and poor infrastructure becomes increasingly detrimental for businesses in areas like Chamkarmon. This could push retailers to take up space in purpose-built shopping malls at least until projects reach completion and the construction works subside.

THINKING GREEN
IN CAMBODIA

WHAT IS GREEN BUILDING?

Green building is a process that takes into consideration the relationships between the built environment and nature by minimising a building's negative impacts on its surroundings through careful planning, design, selection of materials, construction and operation. The result is an energy efficient building with minimal waste, one that creates a pleasant environment for its inhabitants, and a positive overall impact to its surroundings.

Benefits of going green include lower operating costs and long-term utility costs, a positive environmental footprint, creating a sustainable product with potentially a longer life-span, adding value to the development and improving working/living standards of tenants. Positioning a project as green is also an effective tool in promoting a development with companies and individuals becoming more interested in reducing their environmental footprint.

GREEN BUILDING

In order to promote more green building activity, an independent green council is often established, which currently does not exist in Cambodia. Archetype Group, a leading construction consultancy firm involved in the design and project management of the Laurelton Diamond Factory in the Phnom Penh Special Economic Zone, which was awarded a LEED certificate along with Vattanac Capital Tower, is now actively working with EuroCham and relevant government ministries to encourage the formation of Cambodia's own green council.

While LEED (US) is considered the gold-standard and is the most widely-recognised system globally, it is also associated with high costs and rigorous often lengthy processes. However, other certifying bodies also exist within the region that may be more suitable for Cambodia's climate and are able to award green building certificates at a fraction of the cost, examples of which are Greenmark (Singapore), LOTUS (Vietnam), BERDE (Philippines) and GB Index (Malaysia).

HOW ARE DEVELOPERS IN CAMBODIA ADOPTING GREENER MEASURES?

HARNESSING SOLAR ENERGY

Projects of varying scales across sectors are finding it necessary to use alternative sources of energy to avoid paying the high price of electricity in Cambodia. While some have installed solar panels on their roof, others have gone as far as investing in the creation of a solar farm.

Projects: (PPSEZ, Silvertown Metropolitan, Axis Residences, Le Urban Eco Park, Laurelton Diamond Factory, the Australian Embassy)

SMART DESIGN

Incorporating energy-efficient concepts through architectural design and through the use of readily accessible technologies.

Projects: (Vattanac Capital Tower, Emion Hotel, Le Urban Eco Park, the Australian Embassy)

USE OF RECYCLED AND/OR LOCALLY SOURCED MATERIALS

Using materials that are recycled and/or those that are locally sourced to lighten the development's carbon footprint.

Projects: (Kouk Khleang Youth Center, Le Urban Eco Park, the Australian Embassy)

KEY FINDINGS

Existing supply of serviced apartments currently being monitored was recorded at 4,214 units as at Q4 2016.

A further 1,053 units will be added to the supply by 2018.

Occupancy remains stable at 71%.

Increasing competition with the entry of better quality projects will benefit the industry as a whole by providing more options for tenants while lifting the overall industry standards.

PHNOM PENH SERVICED APARTMENT SECTOR

The serviced apartment sector, which has historically performed well, is expected to experience an adjustment period following the completion of new serviced apartments and large condominium projects

Supply and Demand

Mid-Tier apartments continue to form the majority of the serviced apartment supply

The serviced apartment sector continues to expand with at least 10 new buildings being added to the existing supply during the second half of 2016.

Larger projects with well-designed units, complete with modern facilities are starting to emerge in a market which was previously dominated by small-scale apartments that offered only basic amenities and accommodation.

Newly completed apartments such as Mansion 51, ST Serviced Apartments and Modena, that cater to western tastes, are among the latest to join the upper-market category of serviced apartments located in BKK1.

As at Q4 2016, a total of 4,214 serviced apartment units in Phnom Penh were being monitored, with an additional 1,053 units expected to enter the market by 2018.

Chamkarmon continues to be the most popular residential area, in which 52% of the serviced apartments are located, followed by Daun Penh at 15% while the rest are located in Toul Kork, 7 Makara, Chroy Changva, and Meanchey.

61% of the monitored properties are categorised as mid-tier, while 20% are high-end units with the remaining 19% making up the mass-market category.

Rental

High-end developments, particularly in central locations command an average monthly rental price between US$20 to US$33 per sq m, while average rental prices for mid-tier units fall between US$9 to US$18 per sq m per month as at Q4 2016.

Occupancy

A few established serviced apartments maintain high occupancy levels by allocating units for short-term stay

Occupancy across all serviced apartment segments remains steady, at an average of 71%, despite the constantly increasing supply.

High-end buildings are registering occupancies of 60% on average, while mid-tier and mass-market apartments are able to command occupancies of 70% and 79%, respectively.

Expatriates working in Phnom Penh continue to be the main market for serviced apartments with the majority of Cambodians preferring to live in landed developments, which cater for larger households.

In an attempt to boost occupancy, a few serviced apartments have allocated some of their units for short-term stays, which merges the familiarity and comfort of living in an apartment with the convenience that is associated with staying in a hotel.

Serviced Apartment Sector Outlook

A downward adjustment in rental prices can be expected upon completion of large-scale condominium developments especially towards mid-2017 to early-2018

As the sector matures with the completion of better quality projects offering modern units, serviced apartments will continue to attract expatriates working as executives and those in higher level management positions.

Making up a small proportion of occupiers are Cambodians who lived overseas and have now relocated back to Phnom Penh.

Despite being the most popular residential option for expatriates in Phnom Penh, the serviced apartment sector will begin to face stiffer competition from the expected increase in supply within the condominium sector. Large condominium projects will begin entering the market in 2017, including some in central locations such as Casa Meridian on Koh Pich.

Following the completion of even larger projects such as The Bridge, the sector will likely experience a downward adjustment in asking rental prices.

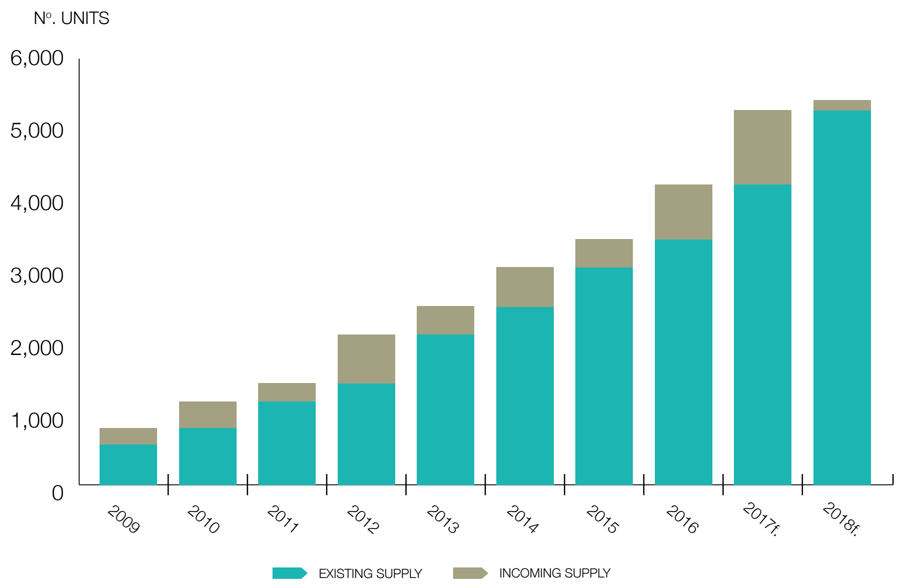
While occupiers will be the main benefactors of this increased competition, the completion of better projects that are well-managed will lift the overall industry standards.

Previously, landlords could demand high asking prices merely because they were in a prime location given the limited competition. With pressure from new apartments, landlords of older properties will have to compete by employing professional management teams, conducting regular maintenance of their properties or by reducing their asking rental to avoid losing out to their competitors.

Given the availability of large land parcels not far from the city centre and with the majority of Cambodians still preferring to live in villas, the serviced apartment sector will continue to be propped up by demand from the expatriate community.

FIGURE 6

CUMULATIVE SUPPLY OF SERVICED APARTMENT UNITS (2009 – POST 2018f)



Source: Knight Frank Research

KEY FINDINGS

Higher sales rate of newly launched developments can be attributed to developers setting lower prices, removing barriers to purchase by adopting more flexible payment schemes and eliminating down payments.

Projects of varying scales continue to launch showing that developers remain optimistic about the residential market even with earlier concerns of oversupply.

By 2020, 72 projects that are currently being monitored in the pipeline will add 25,544 units to the residential market.

Despite the rising popularity of mid-tier projects, high-end condominiums continue to comprise 70% of the future supply.

PHNOM PENH CONDOMINIUM SECTOR

Trusted local developers that were previously exclusively developing borey housing are now crossing over to the condominium sector integrating more affordable high-rise residential components within their existing landed projects.

Supply and Demand

54 projects were added to the condominium supply during H2 2016 following the completion of East Pearl located in 7 Makara

As at the end of Q4 2016, 3,033 units were recorded in the existing condominium supply. Out of the 3,184 monitored units that were due to complete by Q4 2016, none reached completion; 98% rolled over to 2017 while a few were put on hold.

Sales of newly launched projects increased to 46%, a 30 percentage point rise compared to the first half of 2016, which is due to the success of a few newly launched projects within the mid-tier category catering to middle-class Cambodians.

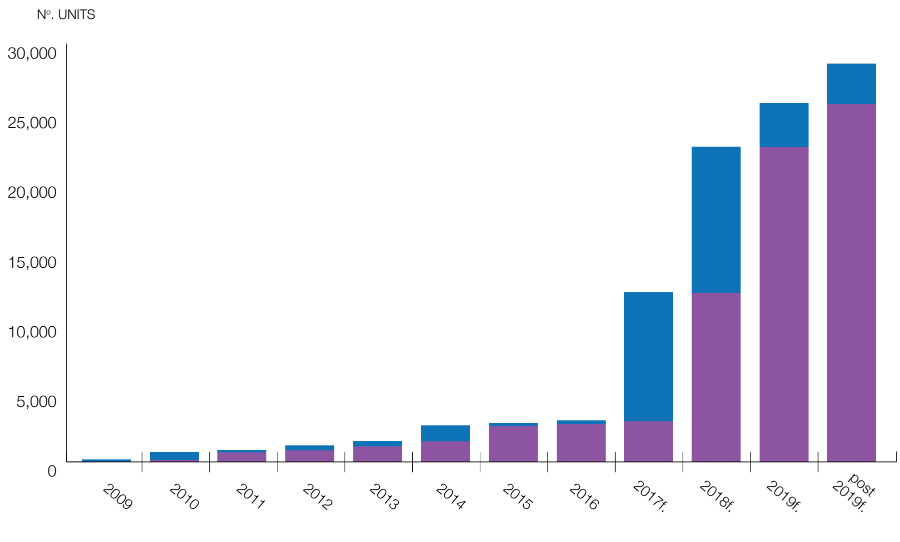
Developers are focusing more on Cambodian buyers, acknowledging the important role they place in sustaining demand for condominiums in the long-term. Local developers are beginning to reshape the condominium sector by introducing high-rise living to the familiar setting of landed developments in order to tap into the local market.

11 projects were announced in H2 2016, which will add a total of 4,102 units to the condominium supply within the next 4 to 5 years.

Chamkarmon continues to attract residential developers, with half of the supply in the development pipeline being constructed or planned in BKK, Tonle Bassac and Toul Toumpong communes.

FIGURE 7

CUMULATIVE SUPPLY OF CONDOMINIUM UNITS (2009 – POST 2019f)



Source: Knight Frank Research

Despite a number of large projects being removed from the pipeline, new projects that vary in scale, continue to be launched. The majority of these projects have between 200 – 300 units.

One of the newest and largest projects being developed, Star City, a mixture of residential and commercial buildings due for completion by 2018, is being developed by Thai Boon Rong Co., Ltd. and Xinghui Property in Sen Sok district. The project, which has yet to be officially launched, has already begun construction and will add approximately 1,600 residential units to the market.

A new trend that is beginning to emerge in the condominium sector is the addition of high-rise residential components to established landed developments.

Borey Peng Huoth recently announced its plan to develop Star Polaris, a 3-block high-rise residential project which will add approximately 900 units to the condominium supply by 2020. With prices starting from US$35,800 for units measuring 30 sq m, the development will be built to cater primarily to the middle class population.

On a smaller scale, Borey Toul Sangke also launched a 205-unit condominium within its borey development located in Russey Keo district.

Sales of newly launched projects in H2 2016 were recorded at 46%, which is 30 percentage points higher when compared to the same period in 2015. The increase in sales can be attributed to some developers lowering the barriers to purchase, which was achieved by adopting 0% deposits, longer installment periods and launching attractive buy-back schemes.

Prices and Rental

Many of the projects launched in H2 2016 targeted the mid-tier category with units on offer between US$1,200 to US$1,800 per sq m

Prices for newly launched developments in H2 2016 were lower by an average of 12% when compared to projects launched in H1 2016. When compared to asking prices for developments launched in H2 2015, the difference is even greater at 23%.

The majority of newly launched projects in H2 2016 were offering mid-tier residential units targeting the lower-middle class population with average prices starting from US$1,214 per sq m.

Despite the number of developers focusing on catering to the middle-class population, high-end projects are still being launched with units prices starting from US$2,368 and some offered at prices well above US$4,000 per sq m.

Asking monthly rental prices per sq m for established buildings currently start from US$4.4 going as high as US$26.0, with the highest rental per sq m applying to newly completed properties that are located in more central districts such as Daun Penh and Chamkarmon.

Expats continue to make up 80% to 100% of the tenants in condominium buildings.

Condominium Sector Outlook

Although high condominium prices and a largely traditional mindset still deter the majority of Cambodians from buying into high-rise living, there are signs that the market is slowly changing with experienced local developers paving the way.

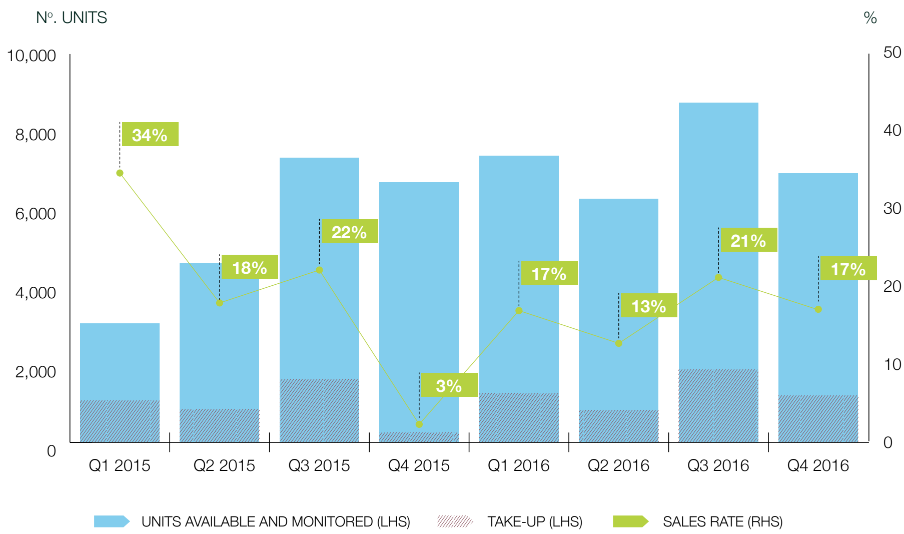
The market will likely see more interest coming from local buyers, with trusted developers anticipating and studying the needs of the emerging middle-class Cambodian population.

We foresee higher demand from both foreign and local buyers as quality projects in prime locations begin to take shape towards mid-2017 to early-2018.

However, due to mounting competition, pressure will likely be felt most by developers that are banking on off-plan sales to fund their projects. The pressure will become more palpable as Cambodia approaches its upcoming general elections in 2018, when investors are expected to be extra cautious.

FIGURE 8

QUARTERLY SALES OF MONITORED AND AVAILABLE CONDOMINIUM UNITS (1Q15 – 4Q16)



Source: Knight Frank Research

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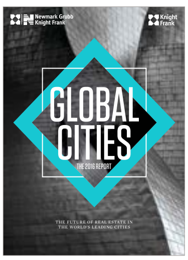

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