MALAYSIA COMMERCIAL REAL ESTATE INVESTMENT SENTIMENT SURVEY 2018

2018 Earth Dog

looks back on 2017 performance and predicts what lies ahead.

The end of 2017 saw the Fire Rooster challenged by the property freeze.

Despite strong expansion in the country's economy with 3Q2017 GDP at 6.2%, market sentiments amongst the Rakyat remain weak amid the rising cost of living.

Our respondents have indicated that Malaysia's political uncertainty will be a major factor which will negatively impact the nation's commercial property market in the short term. Many are hoping that the upcoming general election will come into fruition as soon as possible. Will a revered former leader be able to shake things up in Malaysian politics? We'll find out soon.

In the meantime, several on-going large scale infrastructure developments will continue to be supportive of the local property market.

The performance in the real estate sector remained lacklustre in 2017, challenged by the oversupply situation in both commercial and high end housing markets.

The survey predicts that the office and retail sub-sectors will continue to be soft moving into 2018. However, there is a strong sense of optimism for the logistics / industrial and healthcare sub-sectors.

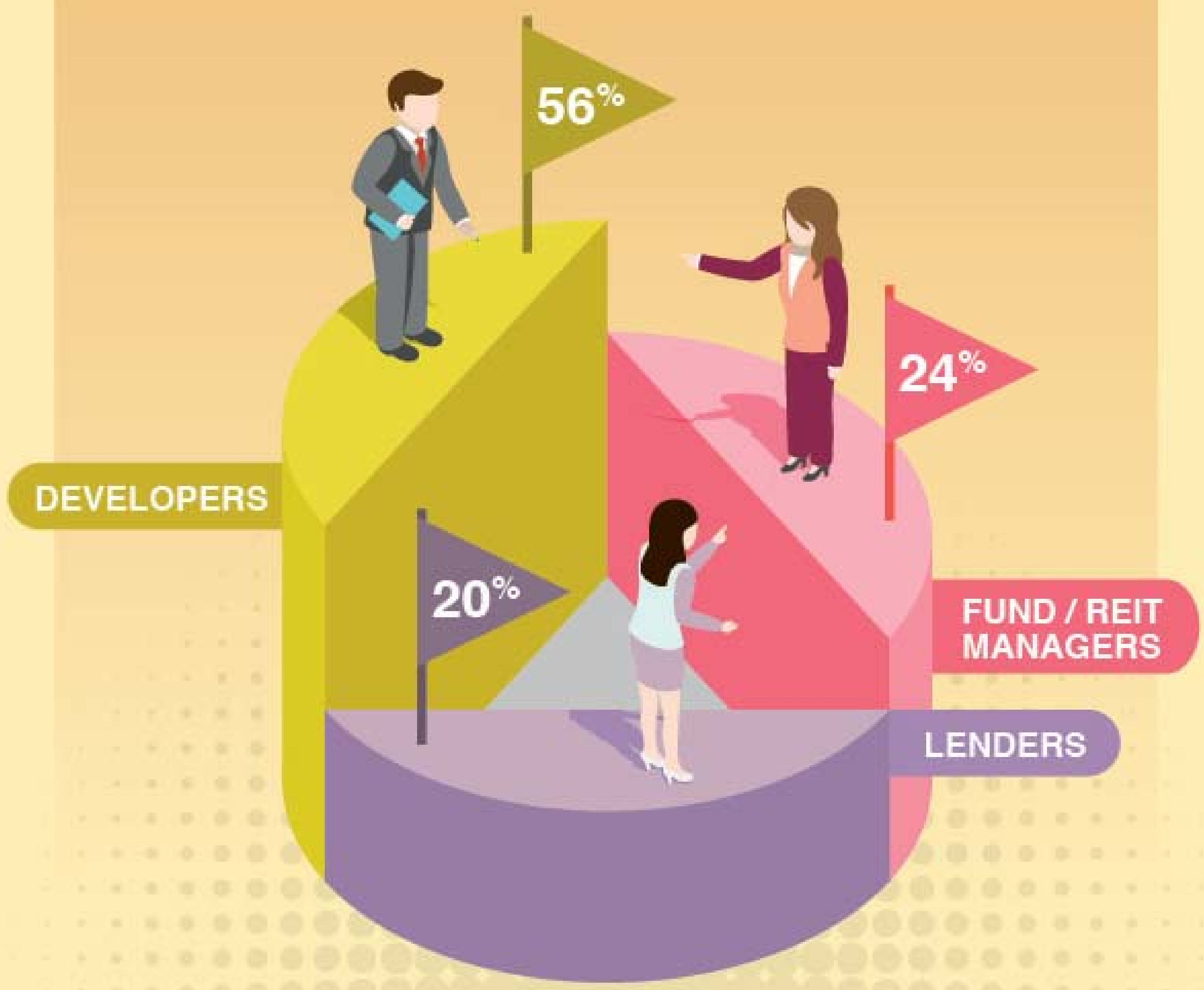
In the coming year of the Earth Dog, we hope to see some stability returning to the local property market as the earth element is believed to be favourable to real estate.

Woof! Woof!

Sarkunan Subramaniam, Managing Director, Knight Frank Malaysia

Survey Respondents

Our respondents comprised of representatives in the senior management levels within the commercial property industry, namely Developers, Fund / REIT Managers and Commercial Lenders. While about half of our respondents were Developers (56%), we had a fair share of respondents made up of Fund / REIT Managers (24%) and Commercial Lenders (20%) indicating a fair representation of the players in the commercial market.

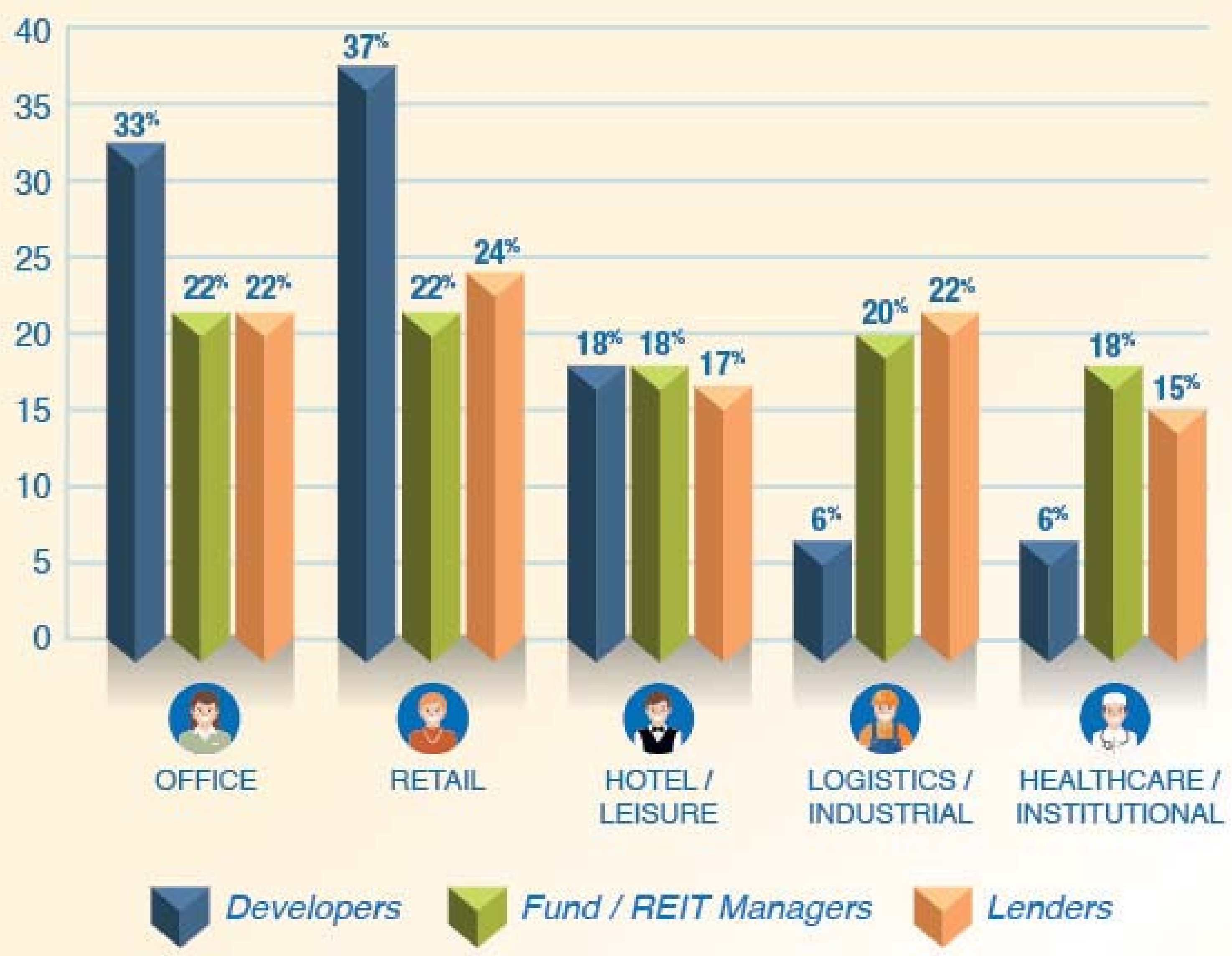


Investment by Industry Players

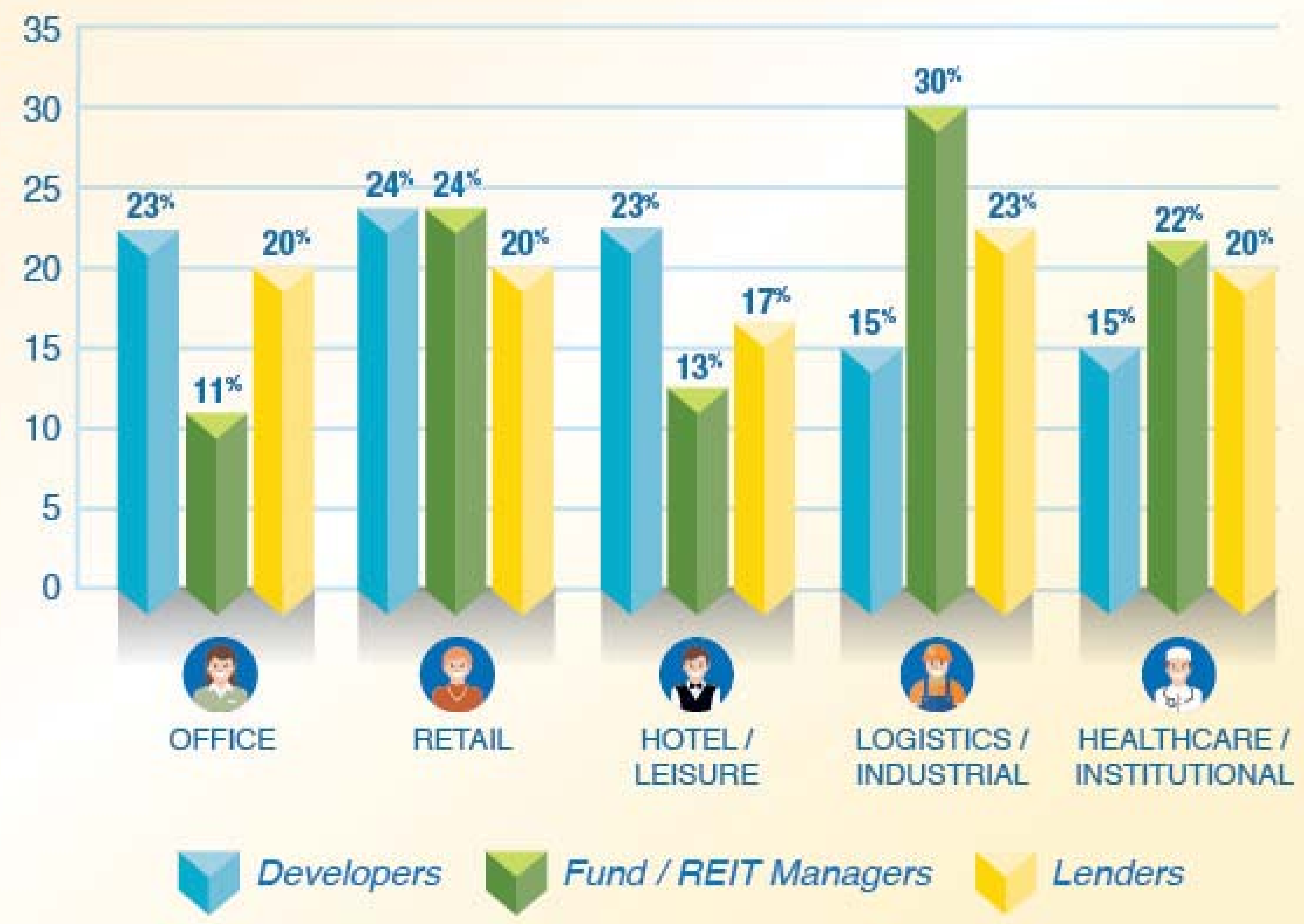
Similar to 2017, Developers and Lenders will continue to practice caution moving into 2018 as the oversupplied office and retail segments continue to challenge the market. On the other hand, Fund / REIT Managers are still willing to deploy capital into the retail sub-sector. Established REITs continue to see opportunities in the crowded retail segment despite market challenges as many of their well-managed malls continue to maintain high occupancy levels above 85%.

Meanwhile, all respondents appear to be more bullish towards the logistics / industrial and healthcare / institutional sub-sectors in 2018.

Sub-sectors invested in 2017



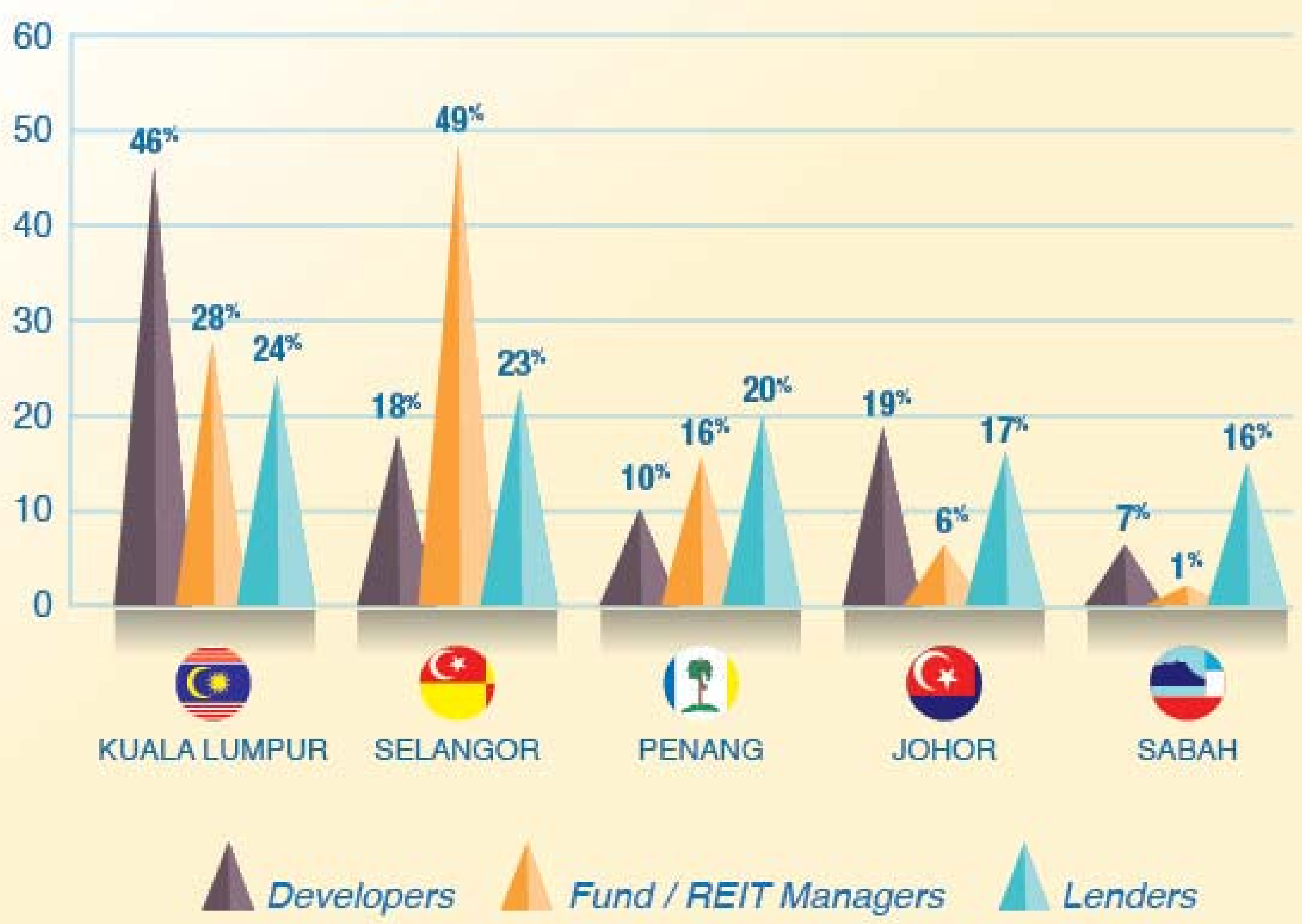
Sub-sectors to invest in 2018



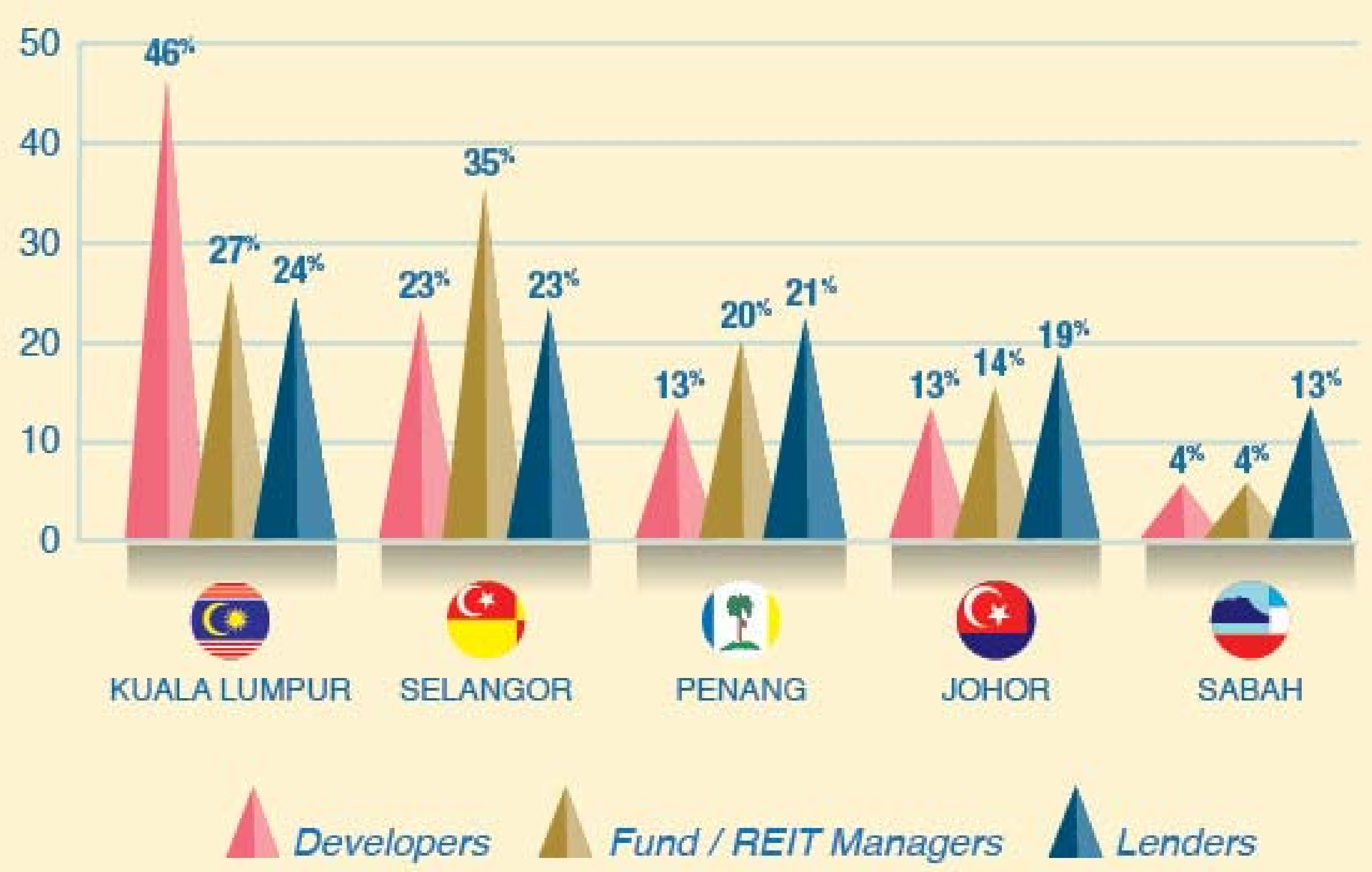
Investment by Region

Moving into 2018, investment activities in Kuala Lumpur are expected to remain stable. In Selangor, the decline in interest from Fund / REIT Managers should be insulated by higher investments from Developers. Meanwhile, Penang is expected to see a more vibrant market in 2018 with renewed optimism. As for the southern state of Johor, although pessimism is growing amongst Developers; Fund / REIT Managers and Lenders will be seeking for more opportunities in the state. Last but not least, Developers and Lenders will be taking a more conservative stance towards Sabah in 2018 although Fund / REIT Managers will be seeking for more deals there.

Regions invested in 2017



Regions to invest in 2018



2018 - The Outlook

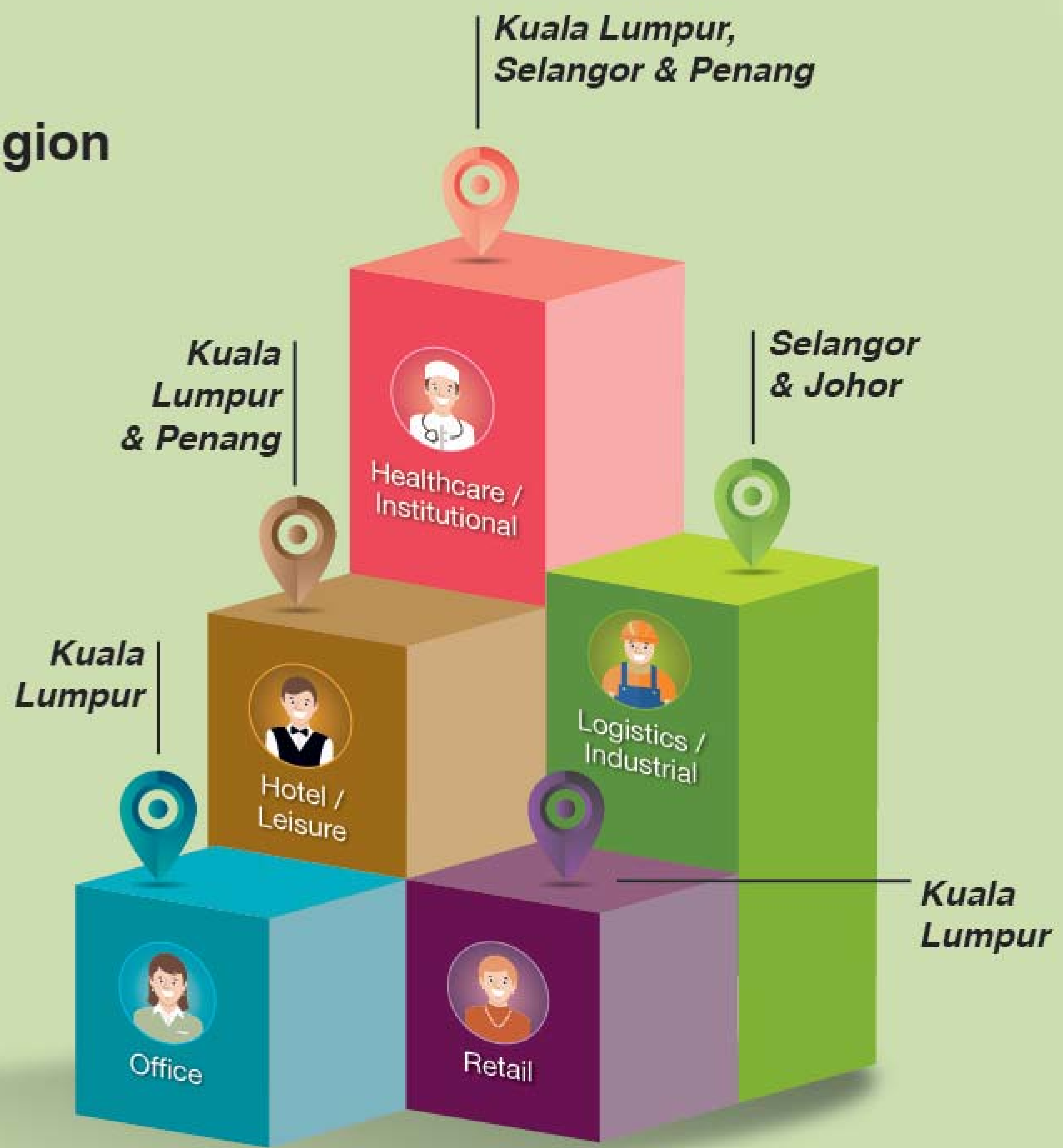
2018 Investment Plan by Region

Kuala Lumpur maintained its top position as the commercial investment / development destination in 2018, garnering 33% of responses; followed by Selangor (26%), Penang (18%), Johor (15%) and Sabah (8%).

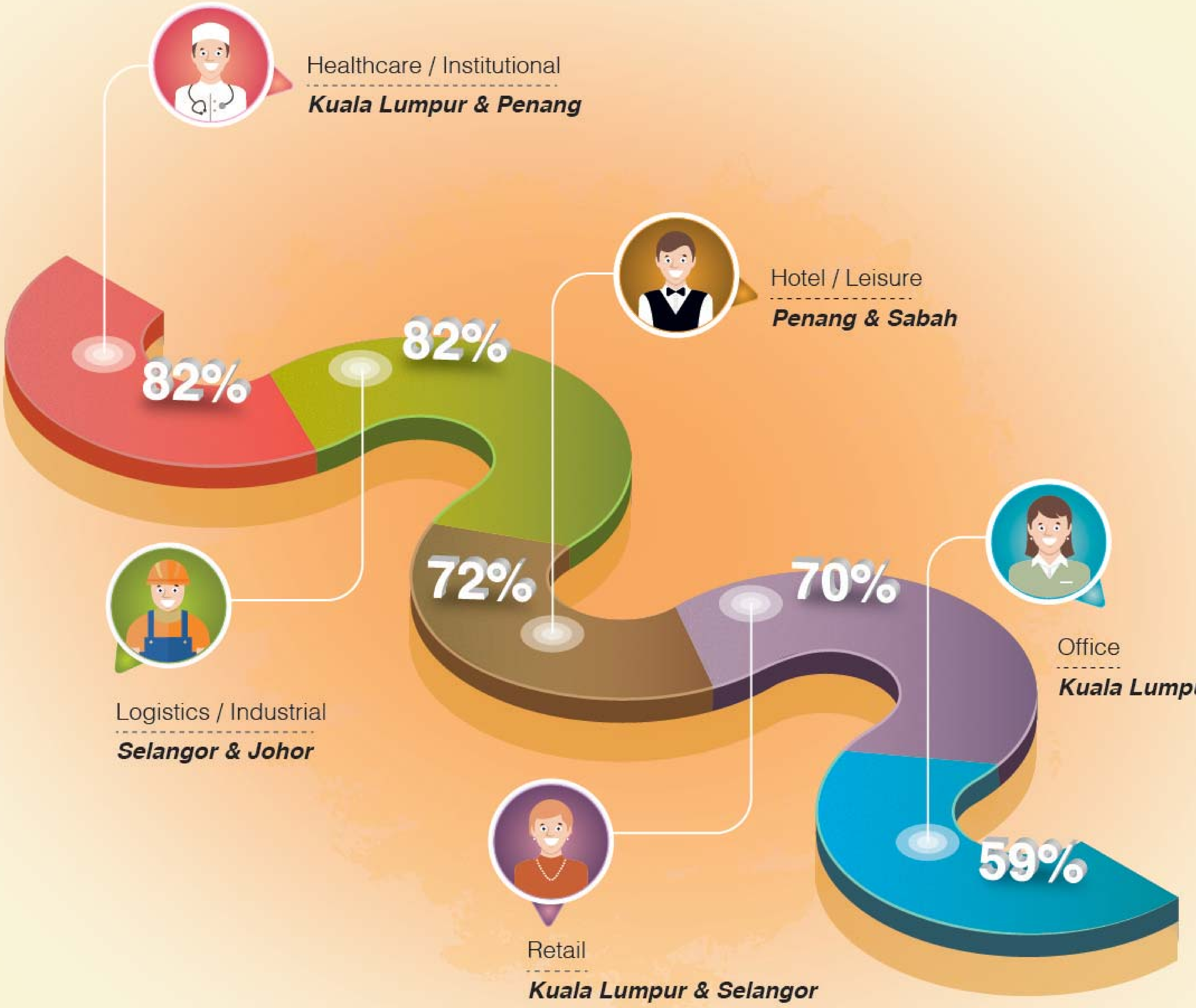
Compared to 2017, respondents' investment interest in Selangor waned in 2018 with plans to diversify into other regions, particularly Penang.

Sub-sectors Investment by Region

Our survey revealed that despite the prevailing supply glut, Kuala Lumpur will continue to be active in the office and retail sub-sectors. Meanwhile, Selangor and Johor will continue their dominance in the logistics / industrial sub-sector. As for the hotel sub-sector, Kuala Lumpur clinched the top spot with 30% of respondents opting to invest in the capital city, closely followed by Penang with a response rate of 27%. Lastly, Kuala Lumpur will also dominate investments in the healthcare / institutional sub-sector at 32%, followed closely by Selangor and Penang, with 25% each.



2018 Most Attractive Sub-sectors



Logistics / industrial and the healthcare / institutional sub-sectors are the most attractive sub-sectors among all our respondents for year 2018. Industrial strongholds, Selangor and Johor, are seen to be most attractive for the logistics / industrial sub-sector. Meanwhile, Kuala Lumpur and Penang are seen to be the most attractive for the healthcare / institutional sub-sector.

As for the hotel / leisure sub-sector, which also garnered relatively strong interests from our respondents, Penang and Sabah are seen to be viable investment destinations.

The retail and office sub-sectors are seen to be less attractive as compared to other sub-sectors. This is mainly due to the overhang present in these two sub-sectors. The retail sub-sector is slightly more robust despite the supply glut as established Fund / REIT Managers are still achieving strong performance from their retail properties. Hence, it is perceived that pockets of opportunities are still present in this sub-sector.

Favourable and Unfavourable Factors Affecting Commercial Real Estate Investment Sentiment

Factors Affecting Property Market

The on-going MRT and infrastructure remains the most favourable factor moving into 2018. The majority of respondents believe that the MRT operation will have a positive impact towards the commercial real estate market. Another notable favourable factor would be the rapid growth in e-commerce, which will be highly beneficial to the logistics / industrial sub-sector.

Compared to the previous year, respondents in this survey view the government budget more favourably. They are also more optimistic on the FDI inflow and opine that the availability of equity capital will continue to be supportive of the property market.

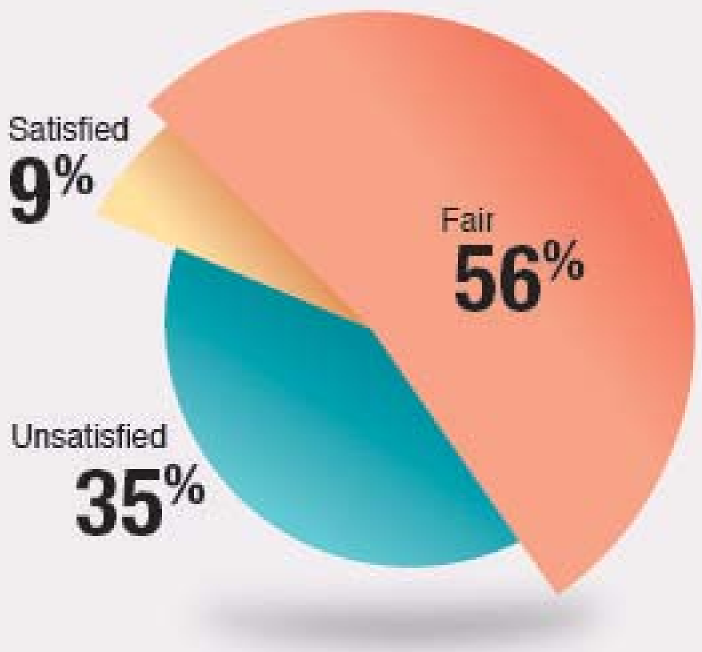
As for the unfavourable factors, the respondents still find Malaysia's unpredictable political scene to be detrimental to the property market with many expecting election jitters in early 2018. Surprisingly, despite the strong economic growth over the past year, many respondents are still not convinced that this will lead to a robust property market, as income growth remains weak.

Sentiments continue to remain weak towards property lending guidelines as well as yield / return although the upticks seen in both factors is noteworthy.

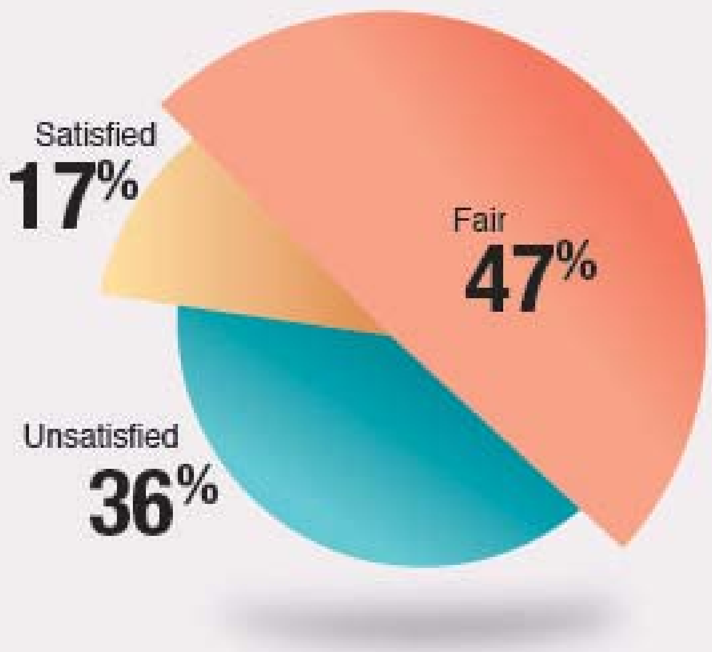
Performance of Commercial Sub-sectors

Approximately half of the respondents view the overall commercial property market performance and the overall economy in 2017 to be fair.

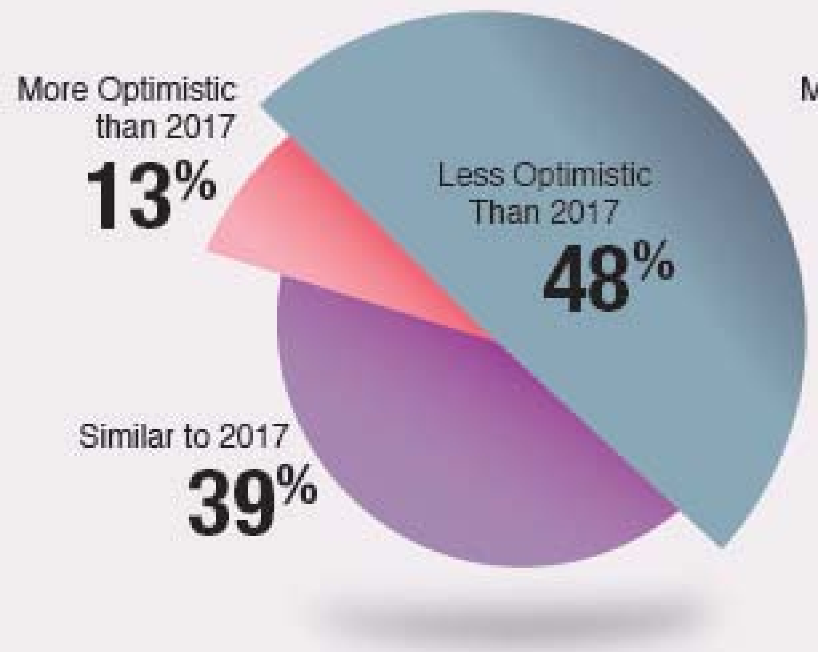
Half of the respondents are less optimistic on the performance of the economy and commercial property market moving into 2018. The general market sentiment remains cautious.



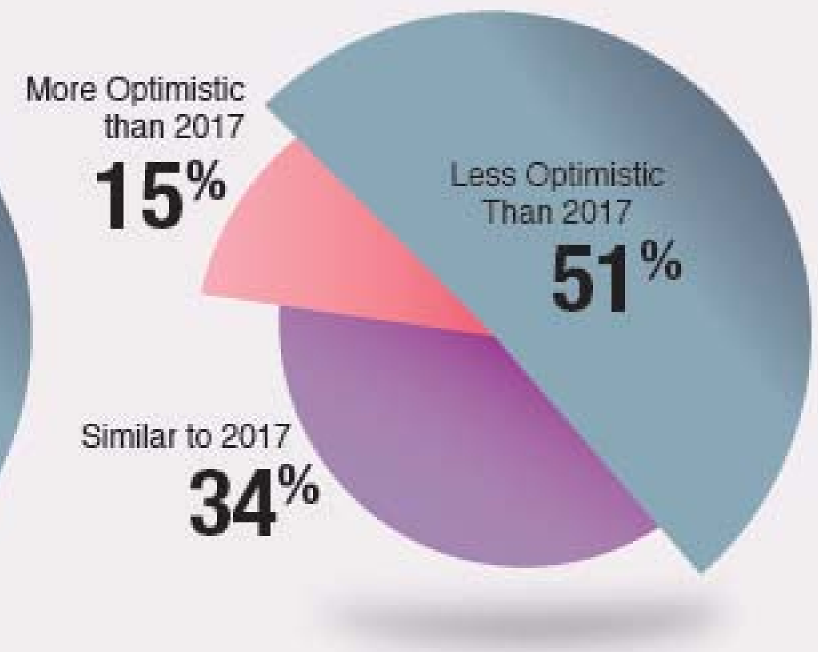
2017 overall commercial property market performance



2017 overall economic performance



2018 overall commercial property market performance

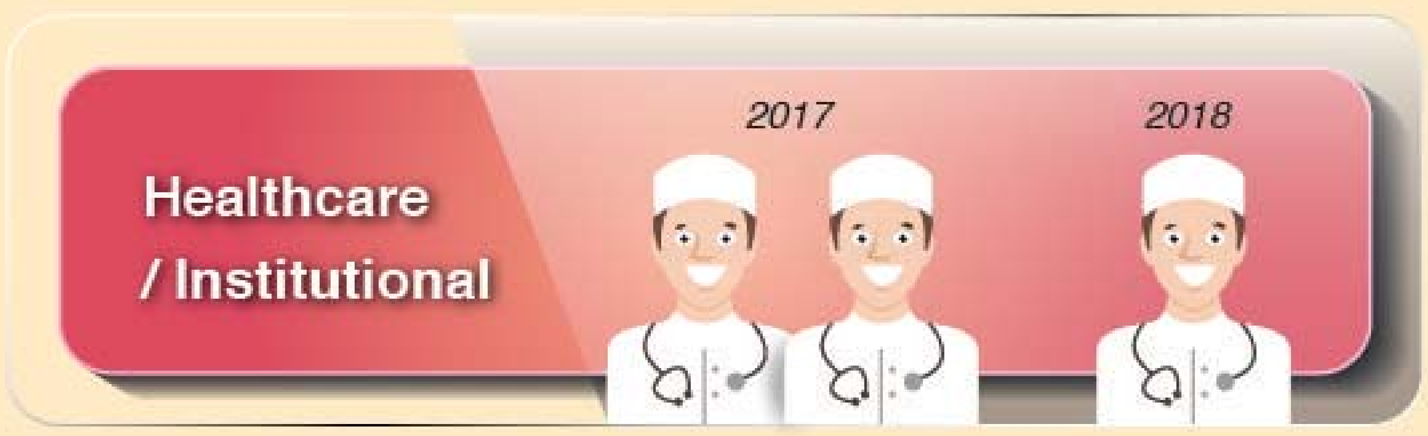


2018 overall economic performance

Overall Performance and Sentiment by Sub-sector

The respondents were generally not satisfied with the performance of the office and retail segments in 2017. Furthermore, this trend is expected to worsen moving into 2018.

Despite the overall subdued property market condition, optimism still prevails in selected sub-sectors. The respondents are generally satisfied with the performance of the hotel / leisure, logistics / industrial and healthcare / institutional sub-sectors and foresee the uptrend to continue moving into 2018 albeit at a more gradual pace.



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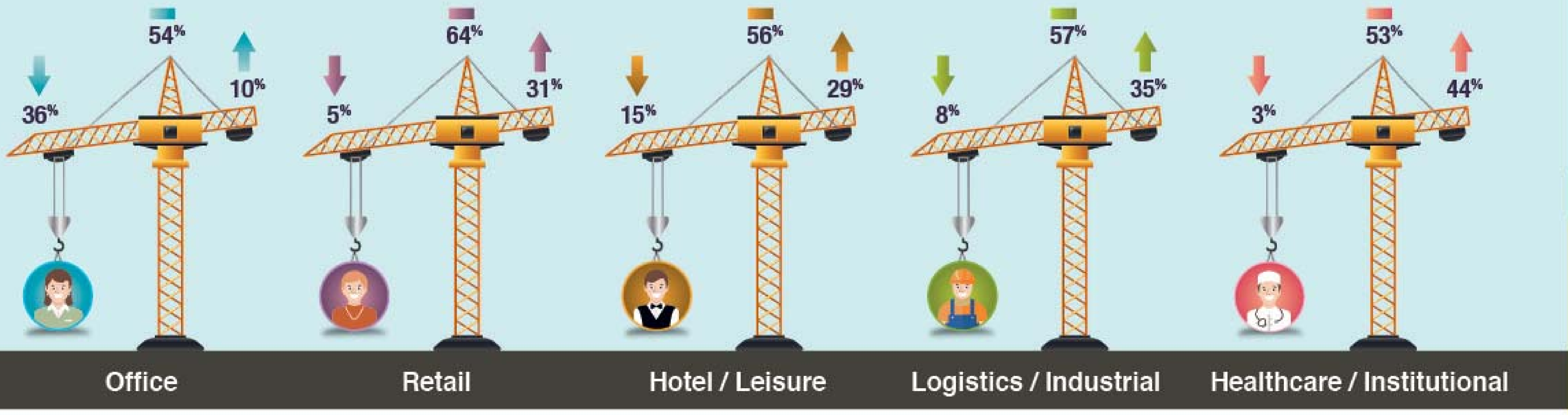
2018 Forecast Performance by Category and Sub-sector

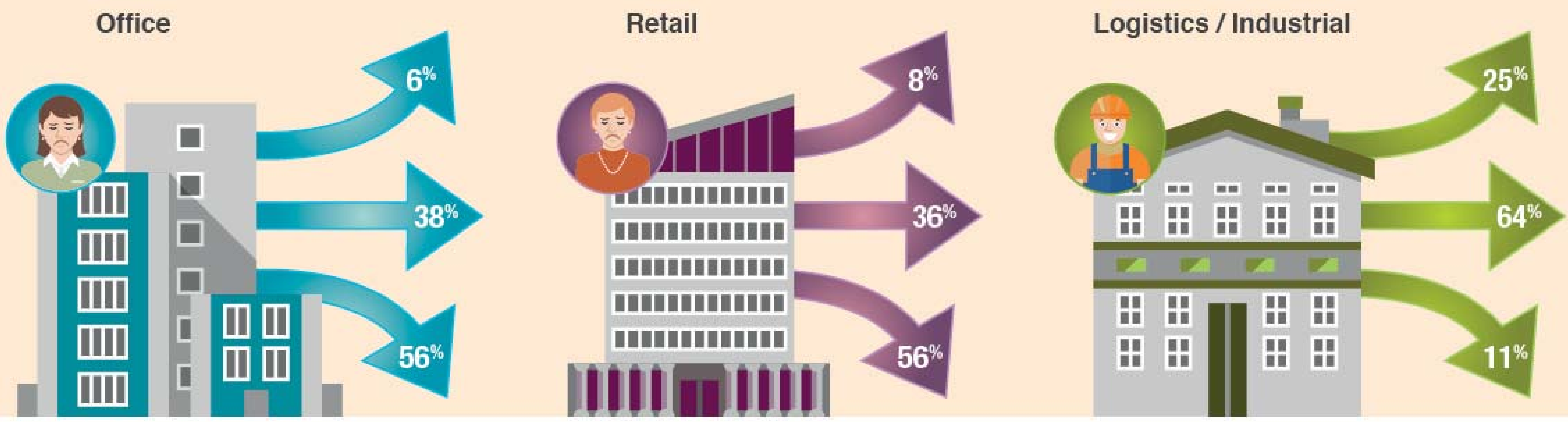
Capital Value by Sub-sector

More than half of all respondents expect the capital values for all sub-sectors to remain stagnant in 2018 while 35% and 44% of them expect an increase in the values of logistics / industrial and healthcare / institutional assets.



Rental Value of Office, Retail and Logistics / Industrial Sub-sectors

Half of all respondents expect a fall in office and retail rentals. As for the logistics / industrial sub-sector, 64% of respondents expect the rental levels to remain stable.



Average Room Rates (ARR) for Hotel Sub-sector

More optimistic outlook for the hotel / leisure segment when compared to 2017.
54% of respondents expect ARR to remain flat with another 30% projecting an increase in room rates.

2018 Forecast Performance by Category and Sub-sector

Occupancy Rates for Office, Retail, Hotel / Leisure and Logistics / Industrial Sub-sectors

Occupancy	Decrease	Stagnant	Increase
Office	51%	43%	6%
Retail	54%	41%	5%
Hotel	25%	47%	28%
Logistics / Industrial	15%	54%	31%

Pessimism prevails in the office and retail sub-sectors with half of all respondents expecting a rise in vacancy rates amidst the supply glut. Majority of respondents expect the occupancy levels in the hotel / leisure and logistics / industrial sub-sectors to remain stable.

Yield Performance by Sub-sector

About half of all respondents expect the overall yield performance to remain stagnant across all sub-sectors.

39% and 44% of respondents expect yield compression in the office and retail segments as a result of higher vacancy rates. On the other hand, more than one-third of respondents expect yields to increase in the logistics / industrial and healthcare / institutional sub-sectors as a result of the rapid growth in e-commerce and the growing need for quality healthcare respectively.

	Decrease	Stagnant	Increase
Office	39%	49%	12%
Retail	44%	48%	8%
Hotel / Leisure	16%	59%	25%
Logistics / Industrial	13%	52%	35%
Healthcare / Institutional	8%	53%	39%