RISKS AND OPPORTUNITIES IN THE MASS MARKET RESIDENTIAL SECTOR IN 2016

In light of the prevailing economic uncertainties and hike in SIBOR, caution amongst prospective investors and homebuyers is expected to heighten. Rents can be expected to soften further, and hence, investors are likely to be very cautious in their purchase decision.

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Growth of suburban private homes outpacing island-wide trend

An expected 21,906 private residential units are slated for completion island-wide in 2016, with more than half of them (11,507 units) located in the Outside Central Region (OCR), where the bulk of units in the so-called mass market segment can be found. Between 2010 and 2015, an annual average of 6,987 units was completed in OCR, a 5.1% growth per annum.

With a total of 157,616 available units in the OCR as at Q4 2015, the new completions in 2016 are equivalent to 7.3% of OCR stock. Although this is lower than the 9.3% increase in stock in 2015, it remains higher than the preceding five-year average of 4.6%.

This upcoming stock entering the market is likely to put further pressure on rents in the OCR. As at Q4 2015, URA's private residential rental index has declined on a quarter-on-quarter (q-o-q) basis for ten consecutive quarters. Of the three segments – Core Central Region (CCR), Rest of Central Region (RCR), and OCR -- private homes in the OCR experienced the largest decline of 9.3% since its high in Q2 2013, compared to the 5.2% and 8.9% decline since their last highs in Q3 2013 in the RCR and CCR respectively.

Reflecting the pressure from enlarged stock, vacancy rates have also increased. It stood at 8.4% in Q4 2015, significantly higher than the quarterly average vacancy rate of 4.5% in the past five-year period from 2010 to 2015.

With higher vacancy and the pending influx of completions, is there a value proposition for mass market private homes in the OCR?

Yields holding up in selected suburban planning areas

Despite weakening rents, Knight Frank's analysis of a basket of private residential properties reveals that average gross rental yields in the mass market held up at 3.58% in the last quarter of 2015, slightly higher than the 3.41% and 3.04% in the mid-tier and high-end markets respectively. Amidst rent compression across all market segments, average resale prices in the mass market have fallen at a faster rate relative to those in the mid-tier and high-end markets.

Several planning areas in the OCR have also outperformed the average yield in the region. Gross rental yields in Sengkang, Sembawang, and Pasir Ris were 3.8% to 4.0% in 2015, and were among the top five performing planning areas despite the significant growth in stock in the past five years. We surmise that this is likely due to lower average prices in these locations, as well as a larger proportion of newer units. Jurong West and Jurong East, in particular, have benefitted from the enhanced infrastructure and new commercial amenities in the Jurong Regional Centre. Gross yields in these planning areas were 3.9% to 4.1% in 2015.

However, it cannot be assumed that the best places to invest are those with strong current gross yields. The healthy yields seen in OCR during the 2012-2014 period was supported by the buoyant rental market. This compelled budget-constrained tenants to explore locations further from the city, thereby benefitting the OCR in terms of lower vacancy rate and higher rents.

However in 2015, as the rental market swung in favour of tenants, many of them have taken the opportunity to re-locate to better and newer projects with good accessibility and connectivity. The trend of flight to quality is expected to continue in 2016.

An eye on developments slated for completion this year

Given that new properties in well-connected locations have strong appeal to tenants, properties which are soon to be completed could offer a possible investment opportunity, if priced attractively. In particular, residential developments near MRT stations are typically more highly sought-after.

Exhibit 2 features a list of some non-landed projects in the OCR with 300 units and above, envisaged to obtain Temporary Occupation Permit (TOP) in 2016 and 2017. However, as most of them were launched during the buoyant period in 2013, and have since achieved very healthy absorption rates, few units are left unsold. Nevertheless, opportunities could be found in the resale market, if owners are looking to sell.

Projects close to the MRT stations on the Downtown Line could also offer good value proposition to investors. With the completion of the first two phases of the Line, connectivity to these areas, and hence rentability of the properties in close proximity, has significantly improved. It will be further enhanced with the completion of Phase 3 of the Line.

EXHIBIT 1

Average Yield and Total Stock by Planning Areas in the OCR

Planning Region	Average Yield				All Landed and Non-Landed Stock (Exclude EC) in the Outside Central Region as at Q4 2015			Vacancy Rate as at Q4 2015
	2012	2013	2014	2015	Total Available Stock (Q4 2011)	Total Available Stock (Q4 2015)	Growth in Stock	
East Region	3.99%	3.77%	3.82%	3.66%	47,761	60,750	27%	10.4%
North East Region	3.95%	3.83%	3.75%	3.67%	37,023	46,165	25%	10.3%
North Region	4.10%	3.90%	3.77%	3.64%	7,034	10,848	54%	7.0%
West Region	3.98%	3.68%	3.75%	3.60%	33,329	37,938	14%	3.1%

Source: URA Website, REALIS, Knight Frank Research

EXHIBIT 2

List of Selected Developments with 300 units or more (with written permission in 2011/2012) Slated for TOP in 2016 and 2017, as at Q4 2015

Development Name	Planning Area	Planning Region	Total No. of Units in Development	Total No. of Units Launched (Q4 2015)	Total No. of Units Sold (Q4 2015)	% Sold	Distance from Nearest MRT Station
Watertown	North East	OCR	992	992	986	99.4%	0.2km from Punggol MRT (N-E Line)
Riversails	North East	OCR	920	905	897	99.1%	1.2km from Buangkok MRT (N-E Line)
La Fiesta	North East	OCR	810	801	800	99.9%	0.2km from Sengkang MRT (N-E Line)
The Trilinq	West	OCR	755	350	220	62.9%	0.5km from Clementi MRT (E-W Line)
Q Bay Residences	East	OCR	630	630	630	100.0%	2.0km from Tampines MRT (E-W Line)
FLO Residence	North East	OCR	530	530	530	100.0%	1.8km from Punggol MRT (N-E Line)
The Hillier	West	OCR	528	528	528	100.0%	0.4km from Hillview MRT (DT Line)
Kingsford, Hillview Peak	West	OCR	512	512	242	47.3%	0.4km from Hillview MRT (DT Line)
Eco Sanctuary	West	OCR	483	483	443	91.7%	1.3km from Cashew MRT (DT Line)
SeaHill	West	OCR	478	330	323	97.9%	1.8km from Clementi MRT (E-W Line)
Skies Miltonia	North	OCR	420	420	405	96.4%	1.6km from Khatib MRT (N-S Line)
Hillsta	West	OCR	416	416	404	97.1%	0.6km from Bukit Panjang MRT (DT Line)
Stratum	East	OCR	380	380	364	95.8%	1.0km from Pasir Ris MRT (E-W Line)

Source: REALIS, Knight Frank Research

Investment interest returning with price moderation of mass market homes

New sales volume in the mass market segment was 5,149 units in 2015, an annual increase of 28.7%. While this figure is a far cry from the 16,135 units transacted in 2012, it could foreshadow a reversal of the downward trend seen in the previous two years. Perhaps as a further early sign of the return of capital, resale transaction activity in the OCR also increased by 17.0% annually to register 2,890 units in 2015.

Transaction activity picked up as prices moderated to be more in line with buyers' expectations and appetites. Average new sale prices stood at $1,151 per sq ft in 2015, 2.4% lower than in 2014; average resale prices stood at $919 per sq ft in 2015, 1.0% lower than in the preceding year.

At the same time, a tapering pipeline supply may offer some relief among developers in the new sale market, and also owners looking to sell their units in the secondary market. There were 9,735 total unsold units in OCR as at Q4 2015, and this is significantly lower than the quarterly average of 13,780 units between 2010 and 2015.

However, the lingering worry is the number of homes possibly bought for investment and which will be completed soon; this may intensify competition in the leasing market. With more investors putting up their properties for rent, tenants are likely to enjoy higher bargaining power, further driving down rents and consequently, rental yields. This could result in a fall in prices as investors are more compelled to sell, leading to rising value proposition of mass market homes for genuine owner occupiers.

Apart from the age of the property and proximity to MRT stations, investors must also consider the requirements of potential tenants in terms of the unit sizes and format type. For example, suburban locations typically see higher demand for larger unit types for the family, as opposed to smaller units. The dual attributes of larger units at lower prices (compared to mid-tier and high-end homes) present value for family homebuyers.

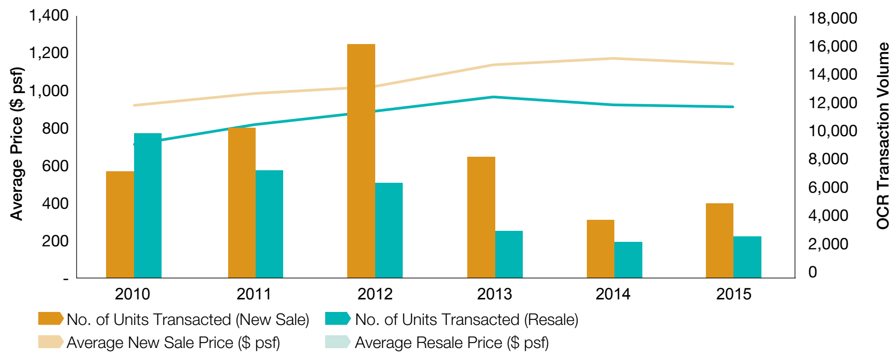
Higher value likely to emerge as market caution persist

In light of the prevailing economic uncertainties and the hike in the Singapore Interbank Offered Rate (SIBOR) since early 2016, caution amongst prospective investors and homebuyers is expected to heighten. Investors who are looking to buy lease-ready completed properties could hunt the market for properties at reasonable prices, and ensure that the target rents are achievable. Rents can be expected to soften further, and hence, investors are likely to be very cautious in their purchase decision.

Extracts of this Research House View were published in The Business Times article "Risks, bright spots in mass-market residential sector" dated 7 April 2016.

EXHIBIT 3

Average New Sale and Resale Prices and Transaction Volume in the OCR, 2010 to 2015



Source: URA Website, REALIS, Knight Frank Research

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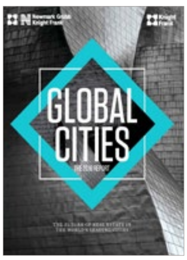

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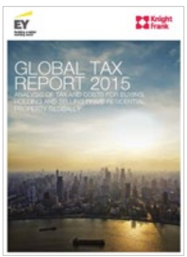

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