



CAMBODIA REAL ESTATE HIGHLIGHTS

1ST HALF 2015

INTRODUCTION

Knight Frank Cambodia publishes its inaugural real estate highlights report focusing on the Phnom Penh commercial sector



ROSS WHEBLE
Country Manager

Cambodia is entering a new era of economic development and we aim to be the real estate consultant of choice, with market-leading research to aid investors, developers and end-users in their decision-making process.

The evolution of the Cambodian real estate industry

Since the signing of the Paris Peace Treaty in 1991 and the subsequent elections in 1993, the Cambodian real estate and construction industry has gone from strength to strength, underpinned by one of the strongest performing economies in Southeast Asia.

Between 2000 and 2008, construction activity increased significantly with several local developers establishing themselves as market leaders in the development of townships (locally referred to as 'Borey') and commercial projects, catering to an increasingly wealthy population.

With an open door policy on foreign direct investment (FDI), Cambodia also witnessed an influx of foreign developers seeking to take advantage of the relatively low land prices and an increasing demand for international standard real estate products. This led to a property boom and land prices increased significantly between 2003 and 2008.

Due to the economy's heavy reliance on exported goods, Cambodia was severely impacted by the global financial crisis (GFC) and land prices in prime locations declined by as much as fifty per cent between 2008 and 2010, with numerous large-scale development projects being placed on hold.

In an attempt to stimulate the market, the Cambodian Government introduced two key pieces of legislation: in 2009 the Government passed a sub-decree for the Management and Use of Co-owned Buildings which paved the way for strata titling, and in 2010 the Law on Foreign Ownership was introduced which enabled foreign purchasers under certain conditions to acquire freehold property (from 1st floor and above).

With the implementation of these policies, the decline in land prices reversed towards the second half of 2010 supported by increasing demand from foreign purchasers of condominiums and rising rents for both office and retail space due to a limited supply.

Although still in its infancy, the construction industry in Cambodia is now a significant contributor to the country's gross domestic product (GDP) and land prices have returned to, or exceeded pre-crisis levels.

With each new project that is being launched, new standards are being set with developers able to achieve benchmark prices. Since its recovery from the GFC, Cambodia has seen the completion of its first international standard shopping mall, developed and operated by Aeon, its first Grade A, LEED rated office building, the completion of the first high-rise condominium block and numerous infrastructure improvements, both hard and soft.

The need for accurate market research

In an increasingly competitive environment, comprehensive market research should form the backbone of any investment decision; one of the main challenges in entering a frontier market is access to publicly available market data.

Knight Frank Cambodia provides expert advice on acquisitions and disposals, valuation services, the consultancy, research and feasibility in relation to potential projects, and project sales and leasing services.

Knight Frank is proud to publish its inaugural Real Estate Highlights report which we hope provides a useful insight into Cambodia's flourishing real estate market.

ECONOMIC SNAPSHOT

Cambodia has been one of the fastest growing economies in Southeast Asia and this trend is set to continue for the foreseeable future

Cambodia at a glance

Metric	Value
Land Size	181,035 sq km
Bordering Countries	Vietnam, Laos, Thailand
Population	15.4 million
Urban Population	20.7%
Median Age	24.7
Adult Literacy Rate	80.0%
U/E Rate	0.3%
GDP (constant prices 2005)	10.5 billion USD
Real GDP per capita	682 USD
GDP Growth Rate	6.9%
Inflation	3.0% per annum
FDI Into Cambodia	4 billion USD

Sources: World Bank, Ministry of Tourism, CIA World Factbook, United Nations, Ministry of Planning, International Monetary Fund, National Bank of Cambodia, UN Conference on Trade and Development

(Data from 2013-2015)

Overview

Cambodia's economy has grown rapidly during the past decade and has recorded an average GDP growth of 7.0% year-on-year (y-o-y) since 2010. In 2015 its GDP growth is forecasted at 6.9%, deviating only slightly from the yearly average and from 2014's 7.0% growth rate.

Manufacturing, agriculture, tourism and construction continue to drive Cambodia's rapid growth, with the latter playing an increasingly important role alongside the fast growing property sector. 1,960 permits for approximately USD 2.5 billion worth of construction projects were approved by the Ministry of Land Management, Urban Planning and Construction (MLMUPC) in 2014, while 915 permits worth approximately USD 808 million in investments have been released since the beginning of 2015. China, Korea and Japan

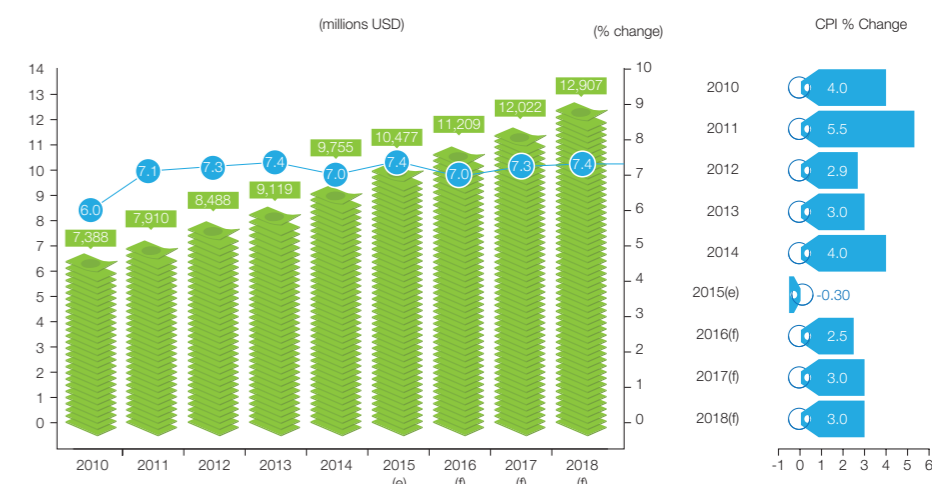
were ranked as the top three highest investors in the construction industry in Cambodia.

Inflation decreased early in 2015, largely due to the lowering of global oil prices, but is expected to increase to 2.6% during the second half of 2015 as oil prices begin to stabilise. Despite the increase, inflation levels are predicted to remain manageable over the short-term.

The abundance of low-cost labour, rapid urbanisation and high margins are factors boosting the real estate industry and the economy as a whole by attracting more overseas companies to set up operation in Cambodia. As integration into the ASEAN Economic Community (AEC) nears fruition, the free flow of trade and skilled labour is expected to attract a larger volume of FDI and bolster employment further over the medium to long term.

Despite the on-going political friction between the Cambodian People's Party and the Cambodian National Rescue Party, an agreement between the two parties to cooperate has resulted in a more stable political environment which, in turn, has led to renewed investor confidence in the market, and should have a positive impact on the real estate sector if sustained.

FIGURE 1
Cambodia's GDP and CPI Figures



Source: IMF, WEO, April 2015 (constant prices)
Note: Figures may vary due to rounding and conversion.

KEY FINDINGS

Office

Total existing office supply was recorded at 241,710 sq m

212.3% increase in net absorption of prime office space between 2H 2014 and 1H 2015

Marginal increase in overall average occupancy between 1Q 2015 and 2Q 2015

Additional 155,128 sq m set to enter market by 2018

Retail

Existing retail space was recorded at 134,153 sq m

Cambodia's per capita retail space of 0.0087 sq m highlights current undersupply

Additional 163,438 sq m set to enter the market by 2017

46% of the existing retail stock is classified as prime



PHNOM PENH OFFICE SECTOR

Despite a decline in occupancy in 1H 2015, developers aim to boost Grade A and Grade B supply ahead of AEC integration, hoping to capture potential demand from incoming investors

Supply and demand

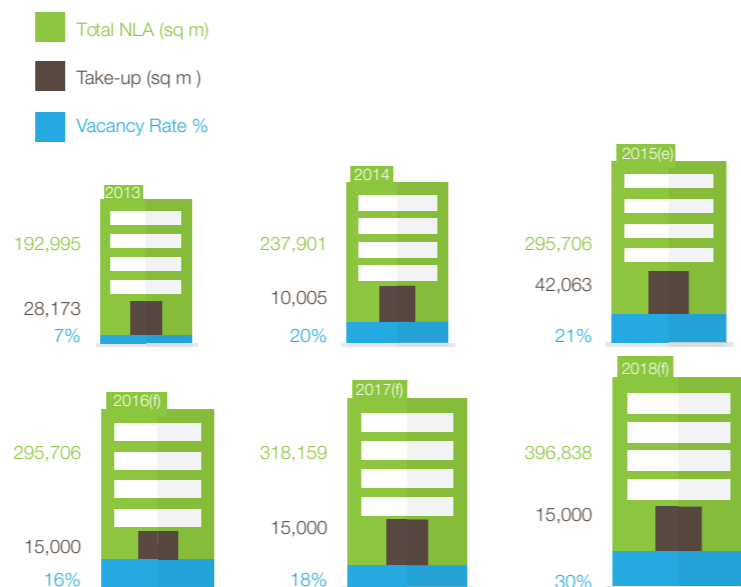
Grade C buildings continue to dominate the office sector, majority of future supply will be Grade A

The opening of Vattanac Capital Tower in 2H 2014, the first Grade A office building in Phnom Penh, added 35,400 sq m of net lettable area (NLA) to the existing office stock, creating true market segmentation for the first time in Phnom Penh. With no new completions during 1H 2015, the total cumulative supply was recorded at 241,710 sq m of NLA. Grade C buildings continue to dominate the office sector with 63% of the existing office space falling within this category.

Phnom Penh Tower, Canadia Tower and the Campu Bank Head Office make up the Grade B office stock. The majority of the office buildings monitored are located in central districts, with only 8% or approximately 18,300 sq m found in suburban locations.

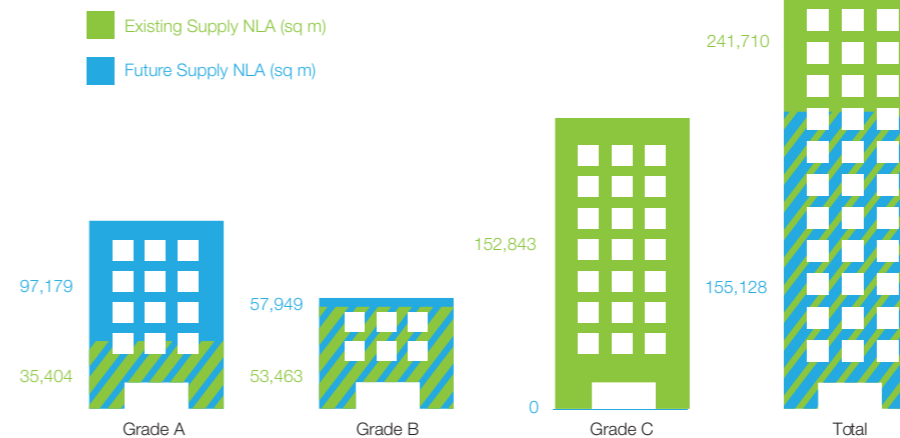
Assuming that developments under construction complete as scheduled, there will be a 64% increase in office stock by 2018, with 155,128 sq m of NLA set to enter the market. Approximately 60% of this space will be added to the Grade A category, while 40% will contribute to the Grade B category, the majority of which will be located within the districts of Daun Penh and 7 Makara. Building classification criteria is summarised in Figure 5.

FIGURE 2
Office Sector Supply, Vacancy and Take Up by Year



Source: Knight Frank Research
Note: Figures may vary due to rounding.

FIGURE 3
Future and Existing Supply of Office Space by Building Classification



Source: Knight Frank Research
Note: Figures may vary due to rounding.

Notable projects include Exchange Square by Hongkong Land, a 20-storey Grade A office building with retail podium located in Daun Penh, which will add 18,500 sq m of NLA to the current office stock. Construction for the first phase began at the end of 2013 and is expected to be ready for occupation by 2017. The property has been available for pre-leasing since launching in Feb 2015.

Olympia City, a project located in 7 Makara by local developer Overseas Cambodia Investment Corporation (OCIC), aims to integrate at least two office towers into the development. It is expected to contribute a further 67,880 sq m to the office supply divided between a purpose-built 55-storey office tower and a mixed-use 26-storey building comprising 30 office units. The project is due for completion by 2019 with several

residential buildings at advanced stages of construction as the development enters its commercial phase.

Emerald Tower, an 11-storey mixed-use residential and office building located on Norodom Boulevard, is scheduled for completion before year end. It will add a further 3,500 sq m of NLA to the current Grade B office stock upon completion.

GT Tower and City Tower Asia are due for completion during 2H 2015, and are expected to add 15,000 sq m and 5,100 sq m of NLA respectively. Both have begun pre-leasing with Bosch and Grant Thornton among some of the first companies who are going to be tenating GT Tower.

Maybank Group's headquarters on Norodom Boulevard and ACLEDA's headquarters expansion on Monivong

Boulevard are set to be completed this year. Together, they will add a total of 30,400 sq m NLA to the existing stock. ACLEDA will be owner-occupied whilst the Maybank building will be partly occupied by the bank.

Occupancy rates remained depressed during 1H 2015

Having only opened to the market recently, Vattanac Capital Tower, the only Grade A office building in Phnom Penh recorded an occupancy rate of 25%, which has had a downward effect on the city-wide average occupancy. Grade B and Grade C office buildings recorded occupancies above 85%, while maintaining stable rental prices.

Notwithstanding a 212.3% increase in net absorption of prime office space between 2H 2014 to 1H 2015, prime vacancy rates only saw a marginal decline from 47.2% in 2H 2014 to 44.2% in 1H 2015. This was partly attributable to a lack of international companies entering the market and also several companies vacating existing buildings.

Approximately half of the occupiers of purpose built offices are international banks, insurance and investment firms, as well as logistics, construction and engineering companies, which usually take up larger office spaces. Other typical occupiers are law and accounting firms, manufacturing companies, real estate firms, energy providers and telecom groups, and firms providing a range of business consultancy services. Most foreign-owned companies are from China, Japan, Malaysia, Korea and Singapore.

FIGURE 4
Knight Frank Prime Office Rental Prices by Quarter



Source: Knight Frank Research
Note: Figures may vary due to rounding.

FIGURE 5
Office Building Classification Criteria

Classification	Design	Internal Systems	Amenities	External
Grade A	Newly built/refurbished	Self-regulating cooling system	Secure ample parking	Highly-visible
	High-standard of common area & façade finish	Modern fire security system	ATMs	Easy multiple access
	Efficient use of space	High speed elevators	Dining establishments	Prime location on main axis
	Clear ceiling height: 2.7-2.9	Extra power supply		
	Large open floor plates, not less than 1,000 sq m	Professional property management team		
Grade B	Well-organised, sizeable reception/lobby	Highly-coordinated security system		
	New or recently built	Centralised A/C	Secure parking	Good visibility
	Good quality finish of common area	Modern fire security system	ATMs	Easy access
	Efficient use of space	Reliable elevators	Dining establishments	Prime location or nearby main axes
	Well-organised sizeable reception/lobby	Professional property management team		
		Good security system		

Prices and rentals

Knight Frank research showed a 2% increase in prime rents between 2H 2014 and 1H 2015.

Prime office rents indicated a slight increase in the average prime headline rent from USD 21.6 per sq m per month in 2H 2014 to USD 22.1 per sq m per month average in 1H 2015.

Typical rental prices in Grade C office buildings range between USD 9 per sq m per month and USD 19 per sq m per month. Grade B buildings are able to command rental prices from USD 20 to USD 25 per sq m per month plus additional management fees of up to USD 5 per sq m per month. Grade A spaces are rented out for USD 28 and above depending on the level, orientation, and size of the space being occupied, with an additional monthly service fee of USD 5. The average rental rate across all office grades is USD 14 per sq m per month as at 2Q15.

Office Sector Outlook

With Cambodia's integration into the ASEAN Economic Community expected by the end of the year, the country looks forward to an influx of companies and investors wanting to take advantage of the opportunities offered by a frontier market, which bodes well for the office sector in Phnom Penh. THE AEC integration is also expected to boost the standards and volume of skilled workers.

In the short-run average rental prices may show a slight dip due to the completion of new office buildings by the end of the year. Upon completion of the larger projects sometime after 2017, a significant increase in supply may force landlords to review rental prices resulting in lower rental rates across all office grades. The demand for Grade A space has been subdued, with most companies still opting to set up in Grade B and Grade C buildings, or in some cases villas, which lower their rental

cost expenditure. With a 90% average occupancy for Grade C buildings, it appears that there is still room remaining for additional supply within the lower grade office buildings.

The nominal increase in occupancy from 80.9% in 1Q 2015 to 81.3% in 2Q 2015 could be due to a slowdown in investment during this period, which could be the result of a combination of factors. Regulations relating to taxes and labour permits, have been enforced more strictly since the beginning of 2015, and have added to the cost of doing business in Cambodia. Besides dealing with regulatory mechanisms, the minimum wage also saw a 28% increase from USD 100 to USD 128 at the end of 2014, which was a welcome change for many in the labour force. Others approached the topic with caution, stating that any increase in wages will need to be balanced by an improvement in labour quality for it to be justified from an economic standpoint.

PHNOM PENH RETAIL SECTOR

With a limited number of modern retail destinations, many are optimistic about the future of Phnom Penh's retail sector based on steady growth of the middle-class population in Cambodia

Supply and demand

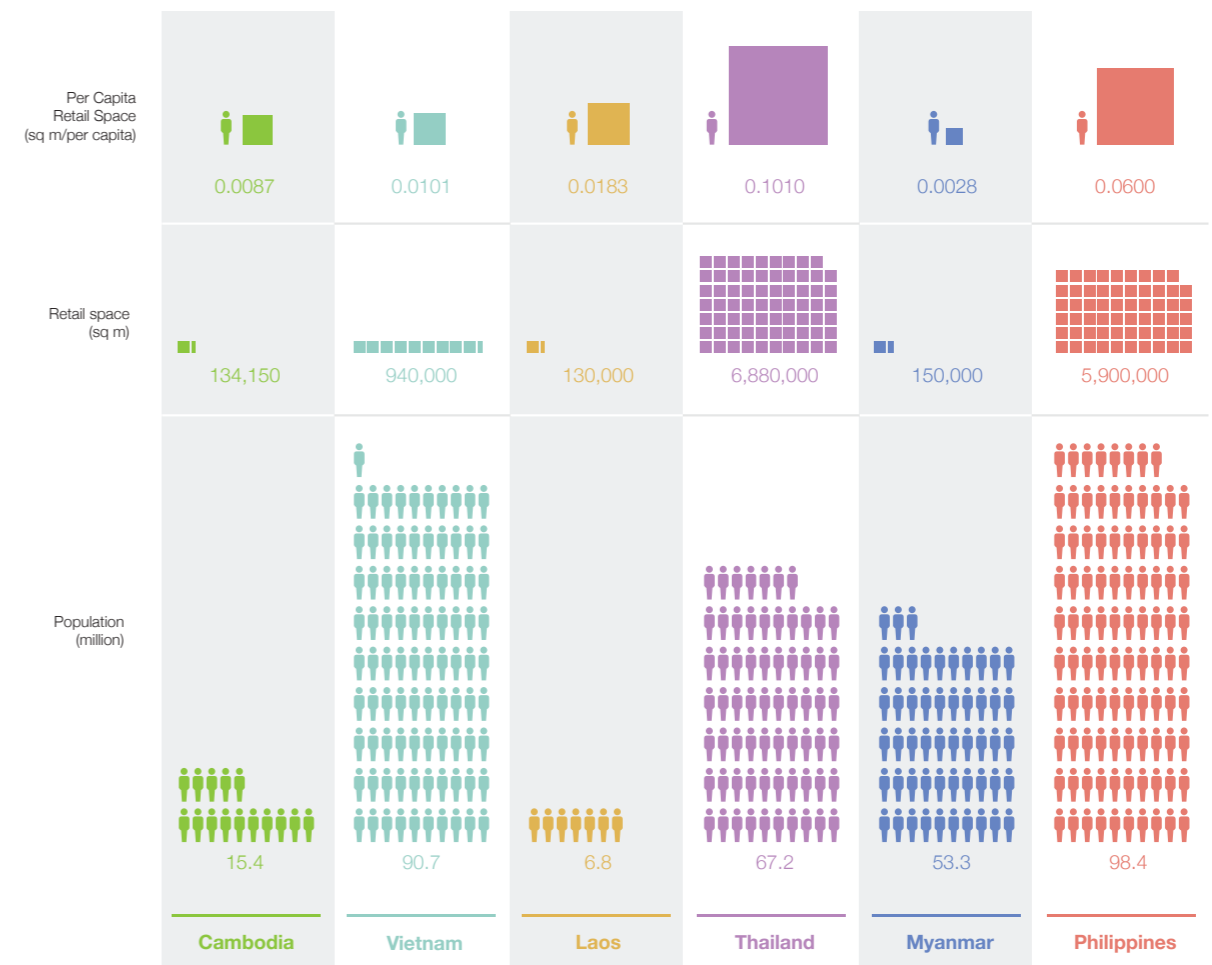
Current per capita retail space in Cambodia points to an undersupply situation when compared to its regional neighbours

Purpose built retail malls in Phnom Penh are classified as either prime or secondary based on location, rental price, design quality, management

standards, operators, and overall branding. The majority of the completed retail projects in Phnom Penh are Secondary Grade with only two out of ten malls classified as Prime Grade. Most existing malls are community malls and have been built to meet the daily demands of the residents within their immediate catchment. Their typical tenants include supermarkets, pharmacies, department stores, apparel shops and electronic goods.

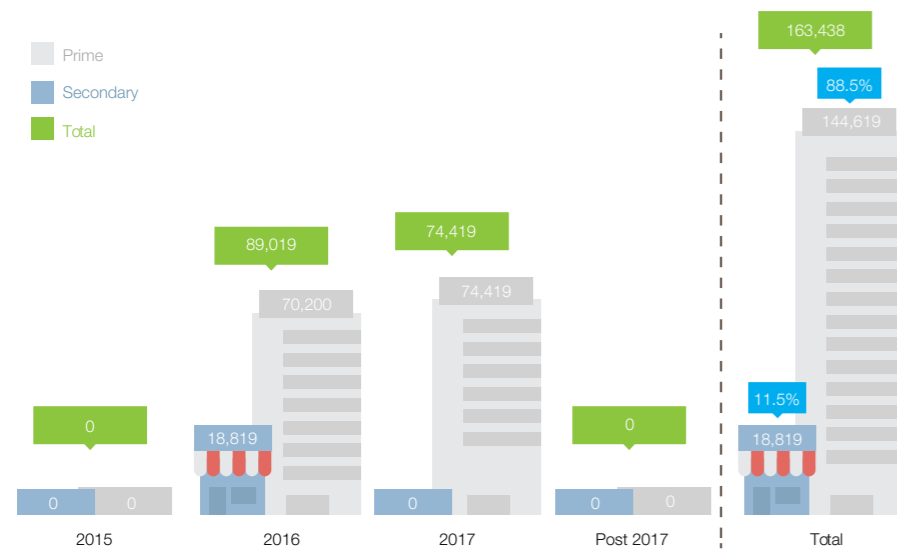
There have been no notable movements in the retail sector since Aeon mall's opening in mid 2014, except for a few expansion and repositioning works being undertaken by older malls. As at 2Q 2015, the estimated stock of available NLA was recorded at 134,153 sq m, 46% of which is classified as prime space. 95% of the total existing NLA is located within central areas, while the remaining space is located within the suburbs. There is currently an undersupply situation given Cambodia's per capita retail

FIGURE 6
Per Capita Retail Space Comparison Between Cambodia and Regional Neighbours



Source: Knight Frank Research
Note: Figures may vary due to rounding.

FIGURE 7
Retail Space Future Supply by Classification



Source: Knight Frank Research
Note: Figures may vary due to rounding.

space of 0.0087 sq m, especially when compared to its regional neighbours. Provided that all projects meet their expected date of completion, based on information that has been made available by developers, 163,438 sq m of NLA is expected to enter the market by 2019 bringing the total NLA to 297,591 sq m, a 122% increase in the existing NLA.

The future supply of retail space in Phnom Penh consists of 88% (144,619 sq m) prime space and 12% (18,819 sq m) secondary space. Central areas will see a minimum addition of 99,105 sq m of NLA, while a total of 64,333 sq m will be added to the suburban stock with Aeropod and Parkson City Centre accounting for the bulk of the upcoming retail space. The total number of malls is expected to increase from 10 to 23 within the next 4 years.

Construction of Parkson City Centre along the Russian Boulevard, which is scheduled to open by mid 2016, has made significant progress since the beginning of the year and is expected to attract more international retailers into the country. A total lettable space of 70,200 sq m is set to become available to the market upon its completion, although a substantial amount of this will be anchored by Parkson.

Exchange Square, a mixed-use development by Hongkong Land in Daun Penh district, has been under

construction since the beginning of this year and will add 6,000 sq m of prime lettable retail space in the form of a 4-level retail podium. The project is slated for completion by 2016.

Located about 200-metres away from the original Naga development is Naga 2, an integrated gambling and entertainment complex, which has been under construction since the middle of 2013. Naga 2's total built up area is 110,105 sq m including a retail complex, which will add a further 16,700 sq m NLA to the existing retail stock, and is due for completion by the end of 2015.

Olympia City's mixed-use project will be located in 7 Makara and is scheduled for completion after 2017, while the D. I. Riviera mall, a 9-storey building is currently under construction on Koh Pich Island, set for completion by 2017. Both projects are currently in various stages of construction and are expected to contribute significantly to the retail stock.

Lion Group's proposed mixed-use development, located across from the Phnom Penh international airport, has started construction and is slated for completion by 2017. The development will include a 7-storey mall that will add 45,500 sq m of NLA to the retail stock.

A handful of existing malls are undergoing repositioning work in an effort to maintain

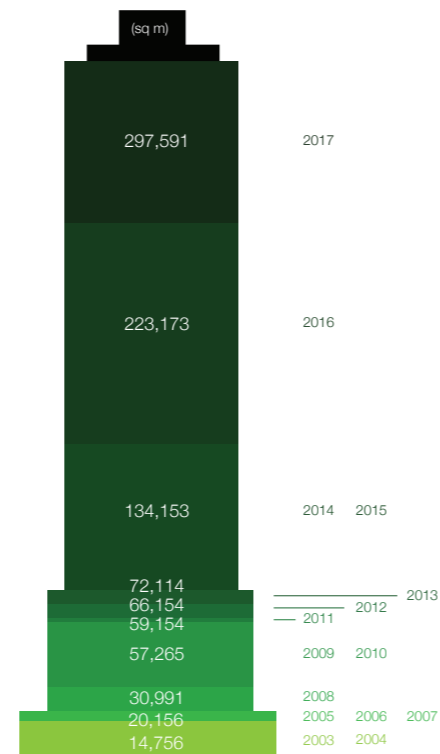
their competitiveness given the new market standards. Older malls have been forced to employ rebranding measures, and to re-evaluate their prices to retain occupiers and attract customers.

TK Avenue, an open air retail destination which opened late in 2013 saw a drop in foot traffic in the middle of 2014, but is now seeing a higher and more stable volume of visitors. Occupancy has remained full despite a few turnovers since its opening; with the mall slowly transitioning into an F&B destination.

Despite good occupancy rates, some brands vacate due to poor sales

Aeon has maintained a high occupancy, which is a positive sign for the retail market. Prime retail space is able to achieve an average occupancy above 90% while secondary grade retail malls have been able to maintain occupancies close to 80%, with the exception of a few that have stopped leasing due to closure

FIGURE 8
Retail Space Existing and Future Cumulative Supply



Source: Knight Frank Research
Note: Figures may vary due to rounding.

of their business or renovation works. One example is Young's Commercial located in Chroy Changva district, which opened in 2014 only to close shortly after to undergo renovation and expansion works. Overall retail space occupancy has reached 86% as at 2Q 2015.

Domino's Pizza, Lotteria & Pepper Lunch, are among some of the larger international F&B newcomers that can be found in Aeon Mall, while fashion retailers such as Giordano, Penshoppe and Levis have also opened their first outlets on the mall's ground level. Some high end retail outlets were initially part of the tenant mix but were forced to vacate recently due to poor sales and high rental prices. Retailers such as L'Occitane, Clarins, TWG, Hugo Boss & Eric Kaiser occupy Vattanac's retail podium, which is more than 50% occupied. Other F&B franchises such as Bonchon and BreadTalk have chosen to establish stand alone stores in the Boeung Keng Kong area or along main axes, and other similar international franchises have done the same. Rental prices of land around these areas are high but the large volume of foot traffic potentially offsets the cost.

Prices and rentals Base rental rates for retail space have remained steady with no new additions to the existing stock this year

A fixed rental price on a per square meter basis is the most common rental price structure utilised by the majority of the malls in Cambodia. Charging additional rent based on monthly sales turnover or profit sharing on top of a minimum base rent is a concept only recently introduced with the opening of more modern retail malls. Other than shophouses/shopflats, sales of commercial property are relatively uncommon with most retail space available only for lease, thus there have been no recorded en bloc sales transactions in the retail sector.

Current base rents for prime retail space range from USD 10 to USD 22 per sq m per month, in addition to 10% to 25% of the tenant's monthly sales. Rental prices for secondary space can range from USD 10 to USD 22 per sq m per month for anchor tenants and USD 22 to USD 250 for non-anchor tenants per sq m per month,

with the highest prices corresponding to smaller spaces. Management fees for prime retail range from USD 6 to USD 15 per sq m while secondary retail tend to charge between USD 2 to USD 6 per sq m. Although some landlords choose to include management fees in their rental prices, both rental structures tend not to include utilities and taxes, which individual tenants are responsible for.

Retail Sector Outlook

As at 2Q 2015 research shows that a greater portion of future retail space will be located within integrated mixed-use developments, with only 2 stand-alone malls out of 13 projects being monitored in various stages of planning or construction.

Despite Aeon Mall's high occupancy, at least 12 retailers have vacated their units since its opening often citing low sales and high rent as their main reasons. Most tenants that have vacated the mall were high end retailers, and are being replaced by more affordable brands that target

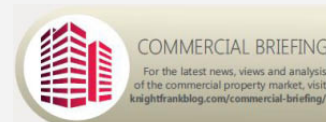
middle-income households, implying that the market may not be ready to accommodate high end brands.

However, many remain optimistic about the future of the retail market stating that careful selection of retailers with suitable products, good choice of location, and keeping a close eye on consumer preference as well as new market standards could lead to profitable rents and higher occupancy rates for new developments.

Based on official figures from the World Bank, the middle-class in Cambodia, or those with a daily consumption expenditure of between USD 2.60 and USD 5.10, has been growing steadily these past years. The emergence of a middle-class means an increasing purchasing power, which has been touted as one of Cambodia's selling points. However, it is also important to draw attention to the fact that Cambodia's middle-class is only beginning to establish itself, and its impact on the retail sector may have to be assessed over a longer period of time.

RISKS AND OPPORTUNITIES

Opportunities	Risks
AEC integration expected to increase Cambodia's competitiveness by:	Other emerging nations becoming more attractive to investors
<ul style="list-style-type: none"> Improving skilled labour Easing flow of services and investments Improving regulatory structures 	
New developments raising standards of retail and office accommodation	Loosely regulated economy and lack in vocational training
Current undersupply in modern retail space and affordable office space	Population's low GDP per capita
Emergence of a middle-class, with an increasing disposable income	
Increasingly stable political climate	
High rate of urbanisation	



CAMBODIA CONTACTS

Eric Y H Ooi

Chairman
+855 23 966 878
Eric.ooi@kh.knightfrank.com

Ross Wheble

Country Manager
+855 23 966 878
Ross.wheble@kh.knightfrank.com

VALUATION

Amaury Payen

Manager
+855 23 966 878
Amaury.payen@kh.knightfrank.com

RESEARCH & CONSULTANCY

Sofia Perez

Manager
+855 23 966 878
Sofia.perez@kh.knightfrank.com

INVESTMENTS/ COMMERCIAL AGENCY

Victor Harris

Manager
+855 23 966 878
Victor.harris@kh.knightfrank.com

RESIDENTIAL SALES & LEASING

Ross Wheble

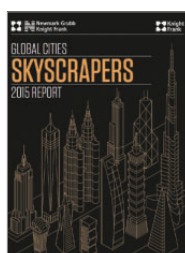
Country Manager
+855 23 966 878
Ross.wheble@kh.knightfrank.com

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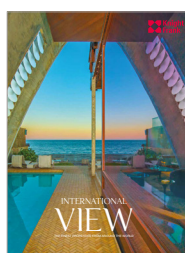
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