WHAT THE 2019 EARTH BOAR BRINGS ...

The historic electoral victory of Pakatan Harapan coalition was the ultimate highlight for the country in 2018. However, in light of the current slowdown in both global and domestic economies, there are respondents who opined that the new government should up the ante by introducing and implementing policies to spur economic activities.

The possibility of a no-deal Brexit coupled with the on-going US - China trade and tech war continues to create uncertainties and dampen investor confidence. This will inevitably lead to slower investment activities globally, commercial real estate included.

Many respondents have pointed out that in view of the current slowing economy, the government should seek to stimulate growth in key industries that will generate strong multiplier effect to the economy. For example, the tourism boom in Sabah provides tailwinds for the state's hotel / leisure and retail sub-sectors.

The commercial real estate sector had remained lacklustre in 2018. This prompted our respondents to indicate the need to curb irrational new supply and to relax property lending guidelines. These measures are seen as vital for Malaysia's property sector to achieve market equilibrium.

This year's survey findings show that respondents are generally optimistic on the logistics / industrial and healthcare / institutional sub-sectors and expect them to outperform the overall commercial real estate market in 2019. It is also worth noting that respondents from Sabah are bullish towards the hotel sub-sector, in line with the region's booming tourism industry.

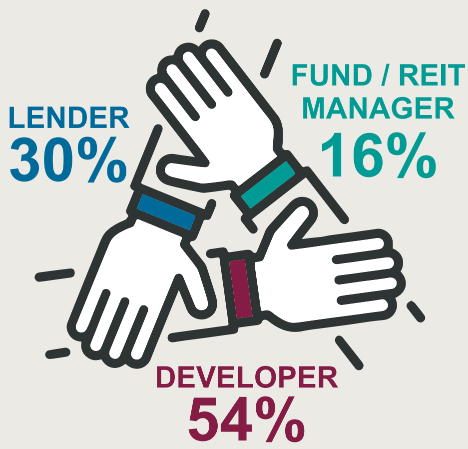
The year of Earth Boar is expected bode well with earth, fire and wood industries. Henceforth, we certainly hope that the property market, which is an earth industry, will start to show signs of recovery moving into 2020.

Hope is the beacon which points to prosperity.

Sarkunan Subramaniam,
Managing Director, Knight Frank Malaysia

SURVEY RESPONDENTS

Our respondents comprised of representatives in the senior management levels across the property industry. Developers made up half of the respondents (54%), followed by Commercial Lenders (30%) and Fund / REIT Managers (16%).



OVERALL PERFORMANCE BY SUB-SECTOR: 2018

Less Satisfied · Satisfied · Highly Satisfied

According to our respondents, their investments in the office and retail sub-sectors had generally recorded dismal performance in 2018, mainly attributed to stagnation / falling occupancy rates coupled with limited rental growth amid challenges in both these property sub-sectors.

In the hotel / leisure sub-sector, performance was mediocre. Despite missing its tourist arrivals target, Malaysia still welcomed 25.83 million tourists in 2018. This supports both overall occupancy and room rates.

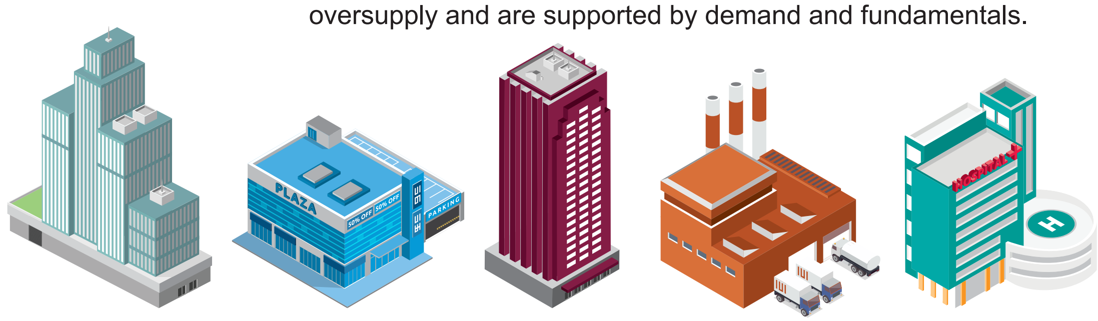
Meanwhile, selected sub-sectors like logistics / industrial and healthcare / institutional continued to outperform in 2018 despite growing global and domestic headwinds, fuelled by strong FDI in the manufacturing sector, continued strong growth in retail e-commerce and inelastic demand for healthcare services.

INVESTMENT PLAN BY SUB-SECTOR: 2018 VS 2019

Developers will be building less office, retail and hotel properties in 2019. Those specialising in logistics / industrial and healthcare / institutional segments will, however, continue to remain active.

Lenders are targeting lesser investment activities in the office and retail sub-sectors in 2019. Instead, they have expressed stronger interests in the hotel / leisure, logistics / industrial and healthcare / institutional sub-sectors.

Fund / REIT Managers will remain active but selective in 2019, gravitating toward the logistics / industrial and healthcare / institutional sub-sectors where there are lesser concerns of oversupply and are supported by demand and fundamentals.



	OFFICE	RETAIL	HOTEL / LEISURE	LOGISTICS / INDUSTRIAL	HEALTHCARE / INSTITUTIONAL
DEVELOPER	Less than 2018	Less than 2018	Less than 2018	○	○
FUND / REIT MANAGER	Similar to 2018	Similar to 2018	Similar to 2018	More than 2018	More than 2018
LENDER	Less than 2018	Less than 2018	More than 2018	More than 2018	More than 2018

Less than 2018 · *Similar to 2018* · *More than 2018* · ○ *Logistics / industrial and healthcare / institutional sub-sectors comprise of specialised asset class. The majority of respondents, namely Developers, indicate that this asset class is less relevant to them.*

EXPECTATIONS BY SUB-SECTOR: YIELD, RETURN AND MARGIN

While pockets of opportunities may still be present in selected office sub-markets, the overall outlook is gloomy moving into 2019 with the majority of respondents expecting occupancy and rental rates to fall. There is no immediate catalyst to address the growing mismatch in supply and demand.

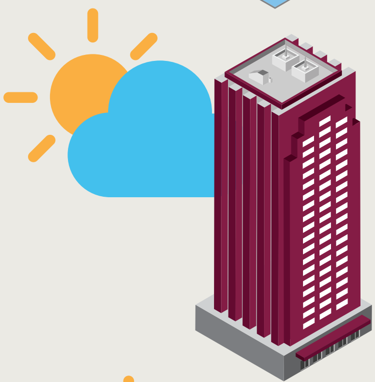
The performance of the retail sub-sector is also expected to be lacklustre with respondents expecting a more challenging market ahead with high supply pipeline of retail space.

The overall performance for the hotel / leisure sub-sector, however, is expected to be generally flat in 2019. Aided by the strengths of Sabah's tourism sector, the overall occupancy rate of hotels in the state is expected to improve.

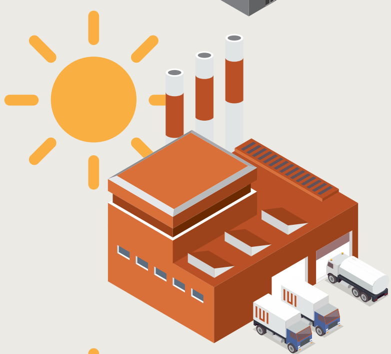
The logistics / industrial sub-sector is expected to outperform in 2019 as more businesses and manufacturers embrace the Industry 4.0 age. Similarly, the outlook for the healthcare / institutional sub-sector is also positive as more investors shift their focus on these recession-proof segments.

OFFICE
LESS OPTIMISTIC

RETAIL
LESS OPTIMISTIC



HOTEL / LEISURE
SIMILAR TO 2018



LOGISTICS / INDUSTRIAL
MORE OPTIMISTIC

HEALTHCARE / INSTITUTIONAL
MORE OPTIMISTIC

FACTORS AFFECTING COMMERCIAL REAL ESTATE INVESTMENT SENTIMENT: 2019

Favourable factors affecting commercial real estate investment sentiment are strong influx of FDI in the manufacturing sector and the rapid adoption of Industry 4.0. Also, respondents generally regard the smooth transition of power to the Pakatan Harapan coalition and improved corporate / public governance to be positive for the commercial real estate market.

In contrast, a number of respondents opined that limited access to funds resulting from stringent lending guidelines coupled with a slowdown in the economy will dampen prospects for commercial real estate in the country.

Also, while respondents were generally satisfied with the provisions of Budget 2018, a relatively high number of them are dissatisfied with Budget 2019, citing a lack of catalytic measures to spur the nation's weak commercial real estate market.

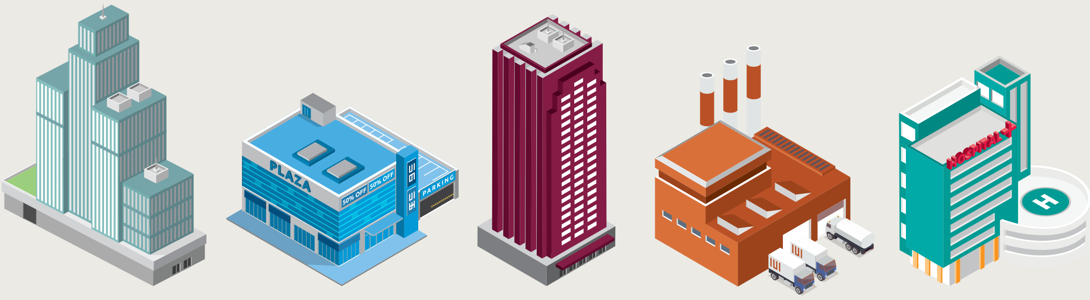
Respondents are expected to take a conservative approach on investment in 2019 given challenges in the real estate market with weak return and yield coupled with limited available investment opportunities.

2019 FORECAST PERFORMANCE BY CATEGORY AND SUB-SECTOR

Knight Frank

Capital Value by Sub-sector

The majority of respondents (50% and >) expect capital values for all sub-sectors to remain stagnant in 2019. Close to 40% of them expect an increase in the logistics / industrial & healthcare / institutional sub-sectors while another 28% expect capital values of office and retail properties to fall.



	OFFICE	RETAIL	HOTEL / LEISURE	LOGISTICS / INDUSTRIAL	HEALTHCARE / INSTITUTIONAL
INCREASE	5%	8%	18%	39%	41%
STAGNANT	67%	64%	67%	48%	56%
DECREASE	28%	28%	15%	13%	3%

Rental Rate / Average Room Rate (ARR) by Sub-sector

57% of the respondents expect office rents to fall. As for the retail sub-sector, there appears to be a more balanced outlook with 48% expecting rents to remain stable while the remaining 44% expect rents to dip.

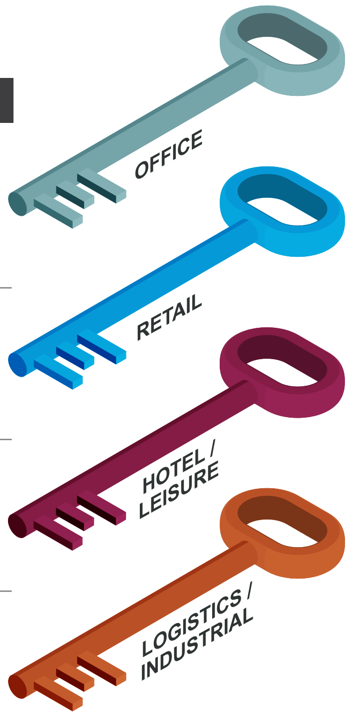
Half of the respondents expects rents to remain flat in the logistics / industrial segment.

In the hotel / leisure segment, a higher number of respondents expect the average room rate in 2019 to remain stable.

	INCREASE	STAGNANT	DECREASE
OFFICE	7%	36%	57%
RETAIL	8%	48%	44%
HOTEL / LEISURE	18%	62%	20%
LOGISTICS / INDUSTRIAL	26%	51%	23%

Knight Frank

INCREASE	STAGNANT	DECREASE
7%	51%	42%
8%	43%	49%
25%	57%	18%
28%	54%	18%



Occupancy Rate by Sub-sector

Similar to the capital value, 42% and 49% of respondents expect overall occupancy in the office and retail sub-sectors to further weaken due to the high impending supply pipeline and slow take-up. As for the hotel / leisure and logistics / industrial sub-sectors, half of the respondents opined that occupancy will continue to hold.

Yield Performance by Sub-sector

More than a third of respondents expect yield compression in the office and retail sub-sectors although circa 26% and 33% of them are optimistic about the performance in the logistics / industrial and healthcare / institutional sub-sectors respectively.

The majority of respondents (> 50%), however, expect the sub-sectors to maintain the performance at previous year's level.

	OFFICE	RETAIL	HOTEL / LEISURE	LOGISTICS / INDUSTRIAL	HEALTHCARE / INSTITUTIONAL
INCREASE	8%	8%	15%	26%	33%
STAGNANT	53%	53%	67%	54%	57%
DECREASE	39%	39%	18%	20%	10%

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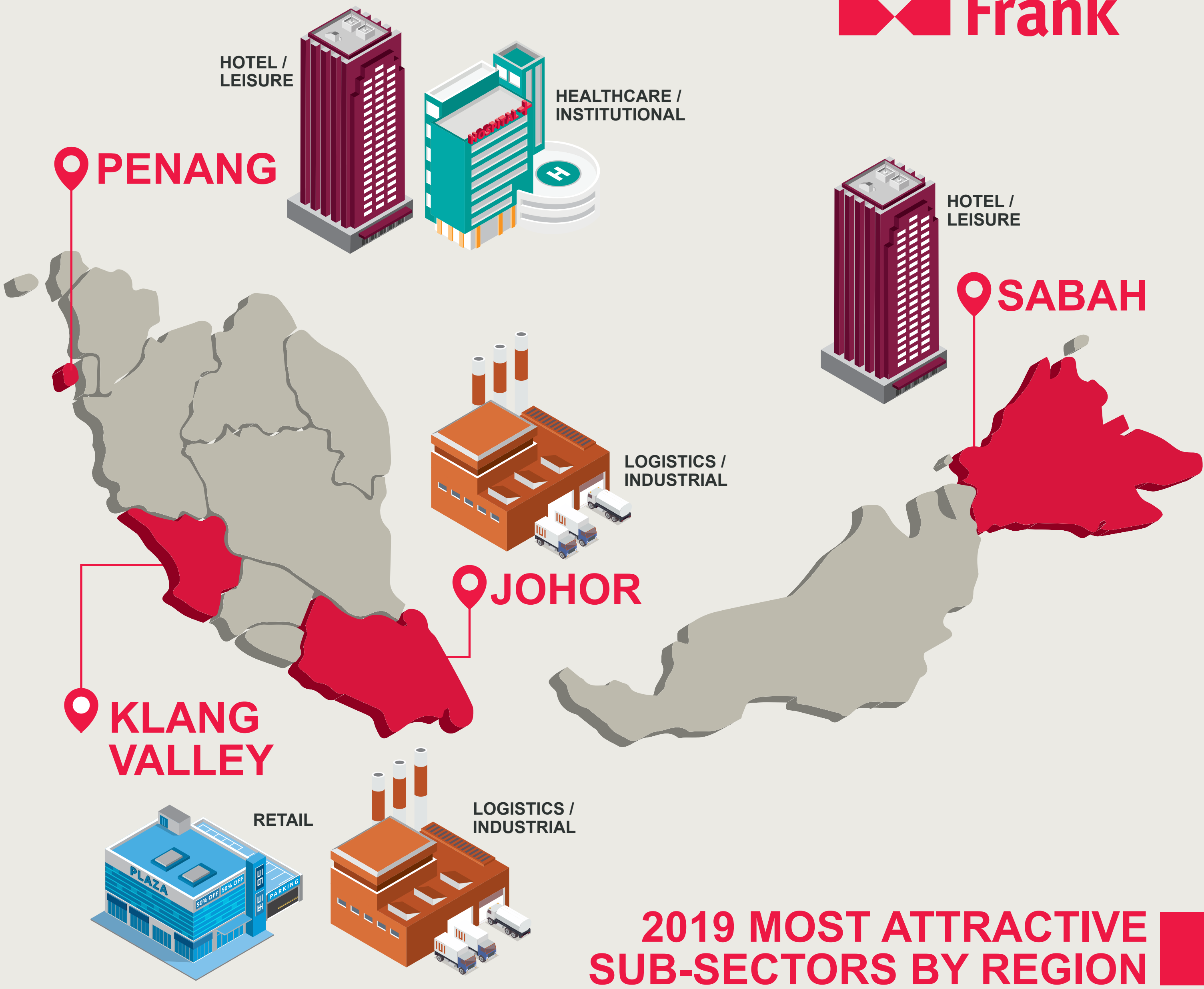


2019 MOST ATTRACTIVE SUB-SECTORS BY REGION

In Klang Valley, the logistics / industrial sub-sector is favoured, likely attributed to the strong inflow of FDI in the manufacturing sector. More than a third of respondents anticipate capital growth in this market segment.

Despite challenges in the Klang Valley retail market, this sub-sector continues to be favoured, particularly among selected developers. Besides undertaking retail developments, key players are hopeful that their retail assets can become more competitive upon completion of asset enhancement initiatives (AEIs).

Penang – The Pearl of The Orient continues to be favoured for its hotel / leisure and healthcare / institutional sub-sectors, supported by its UNESCO World Heritage Site of George Town and its many attractions as well as its position as a leading medical tourism destination in the country.

The southern region of Johor remains attractive for the logistics / industrial sub-sector as the state maintains its position as the leading investment destination in the country for the manufacturing sector.

Last but not least, Sabah – The Land Below the Wind, continues to experience tourism boom with tourist arrivals recorded at 3.8 million in 2018 *(source: Sabah Tourism, 2018)*. Supported by its rich natural environment and cultural diversity, the potential for its hotel / leisure sub-sector remains positive.

HEALTHCARE & INSTITUTIONAL - DIAMONDS IN THE ROUGH

Malaysia's population, estimated at 32.4 million in 2018 as compared to 32.0 million in 2017, grew 1.1% year-on-year. The percentage of old age population (65 years and above) increased from 6.3% to 6.5% for the same period *(source: Department of Statistics Malaysia [DOSM], 2018)*

By the year 2040, circa 14.5% of Malaysians will be aged 65 and older, as compared to only 5.0% in 2010. The perfect storm caused by an increase in the ageing population has created tremendous opportunities for the healthcare and its related sub-sector *(source: DOSM, 2018)*

In tandem with Malaysia's demographic shift, this presents multiple avenues for key players to capitalise on this macro trend. In fact, several notable developers have started to incorporate healthcare / wellness elements into some of their township developments.

Besides the development of hospitals, key players are also exploring the potential of age care and senior living facilities in established neighbourhoods to cater to this growing segment of urban ageing population who are independent, financially stabled and have travelled the world. However, feasibility of the various business models must be carefully evaluated by key players before making inroads in this niche market segment.

Malaysia's demographic shift, coupled with the nation's booming medical tourism industry, has made the healthcare sub-sector a diamond in the rough, due to its sustainable growth potential.

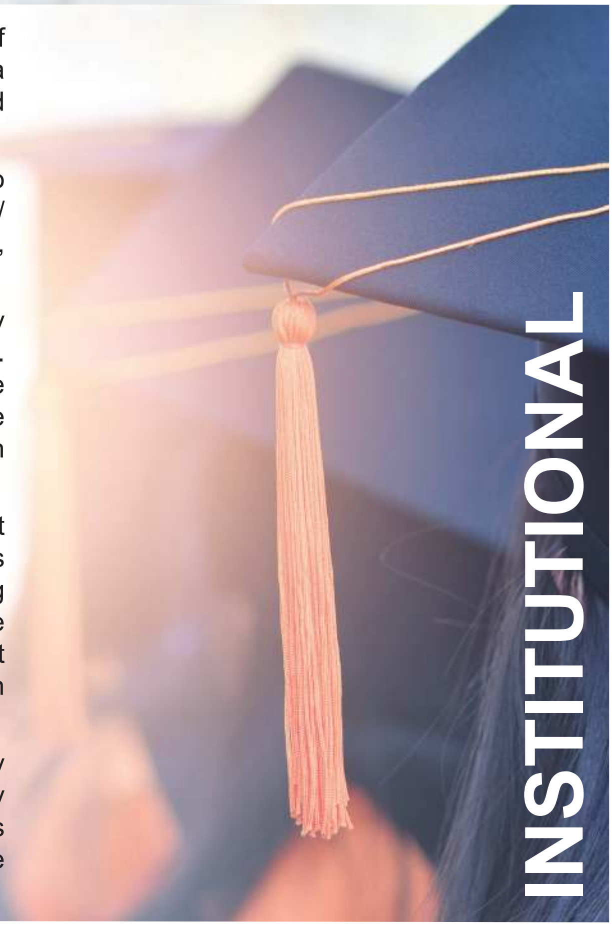
On the other hand, along with the growing importance of education, parents in Malaysia are increasingly willing to pay a premium to enrol their children in schools offering quality and holistic education.

Private and international schools have become a key driver to the success of a few townships, both existing and new / upcoming, such as Desa Parkcity, Kota Damansara, Setia Alam, Bandar Rimbayu, Tropicana Aman and Taman Equine.

Alpha REIT, Malaysia's first full-fledged education REIT, currently owns Sri KDU School and The International School @ ParkCity. Both assets cater mainly to the middle and upper income population segments. The fund is still actively seeking to acquire well performing institutional assets, capitalising on Malaysian parents' willingness to invest in their children's education.

In additional to investing merely in schools, investment opportunities are also aplenty in related assets, such as the likes of purpose-built student accommodation to cater to the changing needs of Gen Z and also co-living facilities catering to the mobile millennial workforce. As a matter of fact, purpose-built student accommodation has already become an asset class of its own in developed markets such as the United Kingdom and Australia.

In conclusion, the complementary benefits brought by institutional assets, coupled with insatiable demand for quality education, especially among elite families are strong reasons why key players shall start paying more emphasis towards the institutional sub-sector.



Footnote:
*(1) Healthcare – Hospitals (including Medical / Specialist Centres and Wellness Centres) *Niche - Nursing Home / Personal Care Home*
*(2) Institutional – Schools providing primary, secondary and tertiary education *Niche - Associated developments such as student accommodation*