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The Future of the Property Sector*

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Abstract: The property sector will face new challenges in the dawn of the new millennium. After three decades of sustained rapid growth involving residential, commercial (office, retail and hotels) and more recently industrial properties, the property sector as a whole requires a fresh approach in order to remain viable, profitable and competitive. Property development is entering into a maturing phase where experience, professionalism and prudent judgement are essential ingredients for success in an increasingly discerning, competitive and complex environment. The property sector will continue to be a key economic sector in tandem with Malaysia's social and economic development programmes.

1. Introduction

Looking back to the time housing and property development first started as a commercial undertaking, progressively gaining momentum and complexity, the industry is now a little more than thirty years old. Housing has been identified as an important sector socially and economically, and has been given due priority. In fact the then government wished to make Malaysia a 'Home-owning Democracy'. Various measures were instituted to facilitate home ownership such as provision of financing facilities through financial institutions. For government employees, the government set up a special housing loan division under the Treasury. As for large corporations, staff housing loans were made available as a fringe benefit.

In the 1970s, economic growth was essentially led by the initiation of industrialisation, expansion of the primary commodities sector and the growth of basic services sector. Improvements to infrastructure, process of urbanisation and the provision of urban services and utilities also contributed to the desire for better housing conditions. The combination of these factors had created a sudden upsurge in demand for housing, which continued to grow in the ensuing decades. Alongside housing, industrialisation and planned economic development have also contributed to rapid expansion of businesses and economic activities in general. Foreign investments also made their presence felt. The growth of the private sector stimulated the demand for commercial offices as well as retail premises in the form of shopping complexes.

Towards the end of the 1970s and early 1980s the major urban centres, particularly in Kuala Lumpur, witnessed rapidly changing skylines dotted by institutional buildings, corporate head offices, hotels and other special purpose buildings. These continued to grow in significant numbers through the 1990s.

2. Aftermath of the Economic Crisis

The growth of housing and the property sector in the early till mid-1990s far surpassed

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the preceding decades. Not only had more land been opened up due to improvement in infrastructure and accessibility, housing density and commercial plot ratios were also raised significantly especially in the major urban centres, such as Klang Valley, Penang and Johor Bahru.

In early 1997, the property sector began to decline mainly due to oversupply, rising interest rates, restrictions on financing and policy changes which were instituted to control supply and over exposure of financing to the property sector.

The measures taken coupled with government policy intervention caused an abrupt decline in demand and the property sector as a whole experienced a very serious decline in mid-1997 right through to 1998. Conditions began to stabilise in the last quarter of 1998 after further government intervention by way of new policy adjustments directly affecting housing development in particular and the economy in general.

The economic crisis which beset the nation spanned beyond the cyclical recessionary phenomenon. The collapse of the stock market, the exchange rate crisis and the resultant economic turmoil dealt a serious blow to the property market and the economy as a whole. In order to counter the adverse economic conditions, the government instituted various economic revival measures at the beginning of September 1998. These measures *inter alia* benefited the property and construction sectors, which saw the gradual return of positive market sentiments and began to usher in a turnaround in 1999.

3. An Overview of the Current Situation

As the property sector comprises a number of sub-sectors, it will be unrealistic to generalise the current situation and the future outlook without examining the prevailing situation in each sub-sector.

3.1 Residential Housing

Owing to the rapid rate of growth centred mainly on middle and upper income housing accommodation, by mid-1990s upmarket housing costing above RM250,000 in major urban centres and RM150,000 outside major urban centres as a whole reached a saturation point.

As for medium and low-medium types of housing accommodation, due to current policy guidelines, they are still enjoying strong demand. This has attracted a large number of developers to reorientate their projects to fulfill this market niche. Owing to the large number of units being built, which are in various stages of implementation, it is anticipated that the saturation point will be reached before 2005.

Low cost housing which has thus far been an unprofitable undertaking was given a reprieve with an upward revision of ceiling prices, along with a revision of standards made effective in 1998. Low cost housing accommodation mainly takes the form of medium and high-rise flats, and very rarely terrace types. In line with the availability of adequate financing and easy repayment terms, many developers are taking advantage of the situation to fulfill their low cost housing quota. This, together with the public sector low cost housing programmes, will result in a massive supply to satisfy the current demand. Although Malaysia has not reached the level of adequate housing (in the form of formal, permanent accommodation), effective demand for low cost housing is projected to reach the saturation point by 2005 given the rapid rate of building activities currently being carried out.

The above scenario does not imply that the residential housing sector beyond 2005 will offer negative prospects to developers. As a developing and growing economy, future market prospects will largely be dependent on demand arising from replacement and new needs estimated at 4 per cent per annum. Based on a current housing stock of approximately 1,925,673 units at the end of 1999, a 4 per cent growth estimate will generate a need for some 80,000 units per annum.

Additional demand over and above the growth generated by replacement and new needs will largely depend on the rate of urbanisation, infrastructure improvements and increase in income earning capacity. In other words, an overriding factor that will have a direct bearing on future demand growth is the rate of economic growth and the capacity of potential buyers to invest in the purchase of houses for rental purposes.

It is also pertinent to point out that during the economic crisis, not only had demand dropped drastically, capital and rental values of residential properties had also declined by as much as 40 per cent in the worst case scenario. The worst hit were up-market condominium apartments where demand and rental values are essentially dependent on the foreign expatriate population, which had dwindled in the wake of the economic decline. On the contrary, landed properties, being scarce in supply and much preferred by the Malaysian home owners, did not suffer serious decline in value and were the first to recover to its pre-downturn levels.

3.2 Commercial Properties

Commercial properties include several types such as office premises, shopping complexes/shop offices, hotels and resorts. The economic recession of the mid-1980s saw an over supply of commercial offices in Klang Valley to the tune of 25 per cent or approximately 6 million square feet out of a total stock of 25 million square feet available at that time. The other types of commercial properties did not show too much over supply to be of serious concern. Following economic recovery from the late 1980s and sustained high growth for the ensuing nine years, the supply of all types of commercial properties increased at a phenomenal rate.

Compared to the situation in the last economic recession of 1985-1988, the present oversupply situation of all categories of properties is far more serious. Most commercial properties are built for rental purposes, with a small percentage sold to retail buyers. In a worst case scenario, capital value had plunged as much as 45 per cent and rental levels on average declined by approximately 40 per cent todate. The outlook of a recovery is uncertain, and the general perception is that due to the huge overhang, rental values may decline further, and this will adversely implicate capital values.

Purpose-built office premises registered a stock of 9,967,916 square metres or 107.3 million square feet at the end of 1999. Of this total, Kuala Lumpur and Selangor's share is 6,524,795 square metres or 70.23 million square feet which is equivalent to 65 per cent of the national total. Currently the occupancy rate stands at 75 per cent with 25 per cent vacancies which amounts to nearly 17.5 million square feet. The excess stock will require at least 5 years to be absorbed assuming the economy achieves full recovery and a level of 7 - 8 per cent growth is attained annually. This appears unlikely and with the completion of some on-going projects coupled with government offices moving to the new seat of administration in Putrajaya, the commercial office sector is anticipated to deteriorate in the foreseeable years.

The demand and supply situation for shopping complexes shows a broadly similar pattern as in the case of commercial offices. At the end of 1999, the total completed stock stood at 5,103,321 square metres or 54.9 million square feet, out of which the Kuala Lumpur and Selangor region accounted for 2,179,102 square metres or 23.5 million square feet which is equivalent to 43 per cent of the total stock. As for occupancy rate, the national average was 72.1 per cent while the Kuala Lumpur/Selangor region registered a marginally higher figure of 77 per cent. There is no reliable pattern of take up rate and demand for retail shopping space tends to fluctuate with prevailing economic conditions and growth of residential catchments. The oversupply situation and the prospects of the excess stock being put to profitable use is no small task compared to commercial offices. For this reason, capital values and rental levels have declined since the economic turmoil set in. There is as yet no positive signs of a recovery due to the prevailing sluggish retail business.

Traditional 4-storey shophouses or shop-offices used to attract strong buying support. This was during the years when the economy was buoyant resulting in a rapid rise in capital and rental values especially in choice locations. This had the effect of a rapid increase in the development and construction of shop offices especially in new housing schemes. Additionally, developers tended to provide for the maximum number of shophouses as allowed in new growth areas. Consequently, by the end of 1999, the stock was approximately 172,772 units, with another 43,000 units in projects where construction work had started. There were a further 30,500 units in the pipeline.

There is no available statistics on occupancy rate, but a cursory observation will show that a good number of shop office/shophouses in less popular areas and new growth centres without supporting residential catchment will remain vacant for a long time. Needless to say, it is difficult to predict when these units will be occupied.

The over building of shop offices/shophouses on the whole is evident from the ratio of total housing stock to the total stock of shop offices/shophouses units i.e. 1,925,673 to 161,850 or 12:1 compared with the normal average of 40:1.

The decade of 1990s saw the most rapid increase in development of hotels and resorts. New projects undertaken during this period included luxury and budget city hotels, and resort hotels. As at the end of 1999, there were approximately 93,878 rooms with another 5,449 rooms where construction had commenced. A further 58,887 rooms were planned and they were believed to have been shelved for the time being due to oversupply. A rapid increase in new hotel rooms, with no corresponding increase in tourists inflow, resulted in most city hotels suffering a steady decline in occupancy and room tariff rates. Resort hotels were similarly affected. However, these facilities are valuable assets and significant improvement can be achieved in the light of the ongoing aggressive promotion of inbound tourism. In recent months, tourists arrival have shown signs of a gradual increase. Efforts are also being made to lure tourists to the shopping facilities as well as to appreciate Malaysia's multiracial culture. In all probability, the recovery of the hotel sector in terms of room tariff and occupancy rate should bear positive results within a shorter period compared with that of the other commercial properties.

Until the early 1990s, most industrial premises were purpose-built, intentionally tailored to the specific needs of the industrial establishments. As a result of the success of the industrialisation programme, small and medium scale industries which provide supporting functions to the big industries grew in numbers. Hence terrace industrial units were introduced. There is no readily available statistics on the existing stock. However, many such schemes were launched in 1999, registering a total of 88,721 units, with a further 16,000 units in the pipeline. Owing to the economic downturn, occupancy rate is reported to be extremely low as a large number of these premises were purchased and owned by investors for rental purposes. Most of the industrial premises completed in 1999 and pending completion in the immediate future are terrace light industrial units and some semi-detached units. In the light of economic recovery and the upgrading and increase in the number of small and medium enterprises, there is a noticeable increase in occupancy, although capital values have fallen and rentals remain at low levels.

4. Regaining Market Confidence

Property development in Malaysia is entering into a mature phase. Supply and demand for all categories of properties have reached the saturation point. The market scenario is expected to be more stable in terms of capital values and rental rates. In the years ahead, there will be keener competition in the market place. Hence, the basis for project viability and profitability requires critical study in order to ensure success in new ventures.

In light of the huge overhang in terms of excess stock on the demand side, capital and rental values will not improve unless the existing stock and the over supply situation is effectively addressed. In this regard, with the existing stock of commercial offices, retail shopping complexes, shop offices and industrial units, the massive excess supply will be more than sufficient to meet new demands for at least the next five years. Hence, there is very little prospects for new projects being undertaken in the short term.

In fact, the urgent task for the time being is to take effective measures to speed up the take up rate of the available excess stock so that these idle assets can be put to profitable use. This will go a long way to gradually restore market confidence. The available stock of light industrial units present an excellent opportunity for new SMEs as well as for relocating existing ones to modern premises in line with upgrading and modernisation. Hence, the over supply problem may not be as acute in view of the rapid expansion brought about by the industrialisation programme.

5. Conclusion

As mentioned earlier, the Malaysian property market is entering into a mature phase. In the years ahead, the market as a whole is unlikely to experience the same degree of buoyancy as witnessed in the past boom years. However, in choice localities, popular types of properties, particularly landed properties, being limited in supply, as well as viable development schemes in new growth centres are expected to continue to enjoy strong demand and capital appreciation.

For basic housing in the form of medium cost and lower priced categories, demand will remain active within an environment of economic growth and increased purchasing power of the target groups. However, due to the present rapid rate of development and construction in these categories of units, in the absence of a new cycle of sustained growth and prosperity, the market will have its limitations by 2005. Similarly, the oversupply situation of upmarket condominium apartments will persist unless a new wave of affluence comes into being, and the expatriate population grows in size to support the rental market.

However, future prospects of commercial properties looks bleak due to the massive oversupply situation in all non residential categories of properties. The capital and rental values will continue to be adversely affected. The situation is likely to decline further, albeit more gently, due to the introduction of IT and a higher degree of office automation, and the vacancies left behind in the progressive relocation of government offices to Putrajaya.

Above all, development land with potential for future development will accordingly be affected as land may not be developed in the short term. For this reason, there will be a