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Malaysia's property overhang — the frenzy, glut and cost

The glut is unlikely to be resolved in the next 1-2 years as biz and consumer sentiments remain below desirable thresholds

by **MARK RAO**

MALAYSIA remains saddled with a massive property overhang four years after the market nosedived as

billions of units remain idle in the market today.

It is estimated that 43,219 residential units worth RM29.7 billion remain unsold nationwide for the third quarter of 2018 (3Q18).

The situation in the near term remains bleak as there are more than 500,000 units in incoming housing supply, and that would take years for the market to absorb.

Housing prices in the country have consequently been on a mode-

rating trend, registering at an average of RM401,900 in 2Q18 — a comparatively low 1.7% year-on-year (YoY) increase.

The commercial space is also bracing for some 18 million sq ft to 20 million sq ft in incoming supply which will put pressure on occupancy and rental rates in an already soft market segment.

Developers eager to gain profit from the positive buyer sentiment, easing lending rates and rising

household debt would culminate in the oversupply situation today where the bulk of properties in the market either exceed buyers' purchasing power or demands.

The glut is unlikely to be resolved in the next one to two years as business and consumer sentiments, while improving, remain below the desirable thresholds and as the market gradually readjusts.

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RTO schemes are a sound option for readjustment, says expert

FROM P1 Property overhang

Here, *The Malaysian Reserve* (TMR) revisits market conditions that have led to the over-supply situation today:

A Boom Dating Back to the Asian Financial Crisis

Malaysia's property boom began shortly after the 1998 Asian financial crisis and its pace became stronger and more oriented towards the high-end segment at the cusp of the 2008 Great Recession, according to an economist.

Institute for Democracy and Economic Affairs senior fellow Dr Carmelo Ferlito said positive profit expectations supported and subsequently prolonged by monetary easing from the central bank drove developers' acceleration into high-end properties.

"When experiencing positive profit expectations, entrepreneurs become future-oriented and ready to invest in long-term investment projects," he told TMR.

"Such a situation encourages the onset of major investments in production assets, or capital goods, whereby the economy becomes, in general, more capital-intensive and the production period is extended."

Ferlito, who is also adjunct faculty member at INTI International College, Subang, described this as the first phase of the boom which saw strong demand for high-end or luxury properties at the time.

He said the second phase of the boom saw a second wave of developers latching onto these same profit expectations that caused a saturated market.

"The impetus becomes particularly violent when the wave of the first innovative entrepreneurs is joined by the pressure of imitators, who grasp profit opportunities only in a second stage and attempt to benefit by following the fashion."

He said the boom was sustained by credit expansion which would bring about a cumulative increase in prices.

"While profit expectations are the primary element at the root of the boom, credit support is crucial in supporting and expanding it eventually beyond its natural extent.

"A declining lending rate,

even if it cannot be considered as an element to generate a boom by itself, has played a role in supporting it and eventually prolonging it."

Bank Negara Malaysia (BNM) slashed its Overnight Policy Rate from 3.25% to 2.5% on Jan 21, 2009, before lowering the rate again to 2% on Feb 24, 2009.

The central bank cited deteriorating global economic and financial conditions brought on by the recession as reasons behind its decision. Interest rates remained below the 3% mark until May 5, 2011.

The lower lending rates encouraged many buyers to apply for housing loans and contributed to Malaysia's household debt-to-GDP rising above 80% in 2012 before peaking at 88.95% at the start of 2015.

Housing-related debt is the largest contributor to household debt in Malaysia.

The rise of housing debt can be seen clearly. Based on the central bank's data, the total borrowing for house purchase was RM69.2 billion at the end of 2002. The figure rose to RM333.4 billion at the end of 2013 and RM523.6 billion at the end of last year.

To curb the rising consumer loans, the central bank had introduced the debt-to-income level or debt service ratio (DSR) which lenders must comply with. The move had pulled the rugs under the booming property sector.

Ferlito said the economic downturn, coupled with lower lending rates had stimulated business sentiment and facilitated the emergence of positive profit expectations. This, in turn, favoured the appearance of the property market upswing, he said.

"We are now experience the turning of the tide and the property market is suffering.

"Such a difficult situation, which takes the shape of a crisis, needs to be considered as the natural readjustment process which will help the market become more consistent with real consumer preferences."

Numbers Behind the Crisis

Developers should also shoulder some of the blame for over-

building. During the market frenzy, property developers went to the market in a strong manner, irrespective of warnings by the central bank about the average buying price that Malaysians can afford.

Prices jumped, fuelled by speculative demands, hyped up interest and marketing strategies like the rebranding of an old township to a more expensive neighbourhood.

Out of the 43,219 unsold homes in 3Q18, Rahim & Co International Sdn Bhd said Johor recorded the highest count of overhang units at 13,767, followed by Selangor and Kuala Lumpur at 7,233 units and 5,114 units respectively.

High-rise property averaged at RM329,987 in 2Q18 — down 2.9% YoY — while detached and semi-detached homes averaged RM646,108 (down 3.3% YoY) and RM644,633 (down 0.02% YoY) respectively. Terrace homes was the only segment that registered higher average prices at RM371,805 — up 5.5% YoY.

For commercial property, Rahim & Co said there was 136 million sq ft of purpose-built office supply in the Klang Valley alone in 3Q18, comparable to Hong Kong which has between 150 million sq ft and 170 million sq ft.

It added that there are between 18 million sq ft and 20 million sq ft of incoming commercial supply at various stages of planning and construction which historically would take the market six years to absorb.

Oversupply in the commercial space is expected to put pressure on occupancy and rental rates, with the latter already on a declining trend in both asking and effective rental rates.

Affordability is among the factors behind the property glut today as 70% of unsold residential units in Kuala Lumpur are priced above RM500,000, according to Rahim & Co.

However, there are also a number of overhang units that fall under the affordable category in Malaysia, indicating that the property downturn reflects a readjustment to

not only prices, but location and product as well.

Market Readjustment

Budget 2019 provided a number of government-led initiatives to assist first-time homebuyers in purchasing property and they are geared at addressing the overhang situation.

This included a RM1 billion fund by BNM to assist first-time buyers earning RM2,300 or below a month and stamp duty exemptions for first-time buyers purchasing property priced between RM300,001 and RM1 million.

The federal government also allocated RML5 billion for the building of affordable homes nationwide.

Meanwhile, developers are exploring rent-to-own (RTO) schemes to convert unsold or inactive units to yielding assets. RTO allows buyers to pay rent for the first five years on the property and then can use the amount paid as a down payment towards purchasing it.

Ferlito said RTO schemes are a "sound option" to help the property market re-adjust, but he has doubts over the viability of the government-led push for more affordable homes.

"I see the government mostly focused on the attempt to build one million affordable houses and strongly believing that the market is ready to accept such additional supply. I have serious doubts regarding this," he said, adding that the government should not intervene in the readjustment process.

Going forward, Ferlito said the readjustment process will take longer than one to two years, and will depend on the actions taken by the relevant parties.

"The evolution of the situation will depend upon how developers will react to the status of the market, what the government will do and what the central bank will do," Ferlito said.

The property overhang came about from the frenzy of building, fuelled by speculations and greed to reap profits, leaving the country with a challenging task to bring balance to the sector.