The Prime Office Market in HCMC

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The prime office market has come into being to meet requirements for the national development in the integration process and the economic restructuring from agriculture into services and industry in the move to a modernized and industrialized country. As a segment of the real estate market, it is never flat but buoyant because the supply has not satisfied the rising demand. Office rents steadily increase and the office market produce high returns in a growing economy. These are factors alluring local and foreign investors into this potential market, especially since Vietnam became the 150th member of the WTO in November 2006. Nevertheless, the market supply and demand relationship should be analyzed for appropriate adjustments, sustainable development and prevention from recession.

1. EVALUATION OF OFFICE DEMAND IN HCMC

The office demand in HCMC has steadily risen over the past years in spite of uneven growth rate per year. This achievement is accompanied with the city GDP growth and increasing flows of foreign investment into the city. Table 1 shows the office demand reached 104,057 m^2 in 1997, up 31.51% as compared to 1996; 123,054m^2 in 1998, up 18.25% over 1997; 140,927m^2 in 1999, up only 14.52% over 1998. This indicates bad effects of the regional economic crisis in 1997 on Vietnam's economy on the whole and the HCMC's in particular. The HCMC office market was also affected by this event. The city faced a drastic decline in foreign direct investment (FDI) due to the 1997 crisis and restrictions of the Vietnamese 1996 Amended Law of Foreign Investment. A lot of FDI projects had to be cancelled because the investors went into the red and worried about the market contraction due to the crisis and restrictions of the 1996 Foreign Investment Law. As a result, the office demand was also badly impacted. Although the demand amount did not fall but its growth was lower.

The regional and the world economies saw strong revitalization in 2000 after the crisis. The Vietnamese economy also began to regain high growth (GDP increasing 6.79% in 2000, while up only 4.77% in 1999). In such a bright situation, the HCMC GDP also rose and so did its export value in 2000. All of this helped boost up the office demand of local and foreign businesses in HCMC, amounting to a growth of 25.28% as compared to 1999. The office demand in HCMC was steadily on the increase from 2000 to 2004 but the pace was slow. This is attributed to less foreign investors coming to the city in this period because the amended Foreign Investment Law was not attractive. Moreover, the city government changed their views and gave importance to large investors in high technology and services of finance, banking, and insurance. Consequently, small and individual investors in low technologies and labor-intensive industries moved to other provinces including Đồng Nai, Bình Dương, Long An...At the same time, large investors were investigating the city market and did not made up their mind yet.

Nevertheless, from 2005 until now, HCMC has seen promising signs of foreign investment due to the following reasons: Vietnam applied the general Investment Law in 2005 and abolished the discrimination between sectors, Vietnam was prepared to become the WTO official member, and HCMC offered new attractive incentives to foreign investors. The world giant Intel, for example, decided to invest US$605 million in the city hi-tech park. This event has made a domino effect to large corporations in the world, even banking and financial groups, and fascinated them to come to the city. All of these factors have caused a boom in the office market in HCMC. The space demand soared to 257,186m^2 in 2005, highest so far with a year-on-year growth of 10.88%, highest within the last three years (See Table 1)

The above analysis shows an upward trend of the city office demand, especially for grade A offices. Since 1997, the demand for grade A offices rose by 10,000m^2 annually on average, even there was no supply or too low vacancy rate from 1 to 12%, for example, Saigon Center (65 Lê LơVi Str.) having a vacancy rate of 1%, Metropolitan, Sunwah Tower 12%, Diamond Plaza 10%....According to estimation, the pressure of office demand in HCMC will not be reduced until 2008. The office supply will become less until prime office buildings are completely built and operational.

The factors affecting the growth in office demand are as follows:

- FDI keeps flowing into the south vital economic region including HCMC, Đồng Nai, Bình Dương and Bà Rịa – Vũng Tàu, accounting for 58% of the country's total investment capital, including many projects of properties such as trading centers, offices for lease, high-grade housing...

The political stability and social security are maintained,

Table 1: Office demand in HCMC (1997-2005)

Year	Space demand (m²)[1]	Demand growth (%)[2]	GDP growth (%)[3]	FDI in HCMC (US$mil.)[4]
1997	104,057	31.51	12.1	1,179
1998	123,054	18.25	9.0	707
1999	140,927	14.52	6.0	471
2000	176,555	25.28	9.0	224
2001	200,074	13.32	9.5	619
2002	209,589	4.75	10.2	314
2003	222,049	5.94	11.4	315
2004	231,946	4.45	11.7	459
2005	257,186[5]	10.88	12.2	604

Source:-(1) From 1996 to 2004, HCMC Office Market (March 2005); Comprehensive list of options offer by grade A,B,C- CBRE.
-(2) The authors' calculation.
-(3)HCMC Statistics Bureau (2006), 2005 Statistical Yearbook, p.34.
-(4)HCMC Statistics Bureau (2006), 2005 Statistical Yearbook, p.158.
-(5)From 2005, Office market update Q 4-2005- Chesterton Petty Vietnam

helping international investors decide and expand their long-term investment in Vietnam. The liberalization of the Enterprise Law promotes the establishment of new companies in Vietnam.

The business expansion of multinational groups and the foundation of new rep offices of foreign companies also push up the office demand.

In addition, when the competition becomes harsher even in the domestic market, national companies tend to lease high-grade offices in the city downtown including Districts 1 and 3 with the aim to increase their edges.

Prime office leasing services bring about a lot of convenience and facilities: professional administration of accommodation, modern facilities, and high-class support services. In the second quarter of 2005, several multinational companies such as Nortel, BNP - Paribas, ACE, IKEA, Panasonic, China Airlines, Maybank, Sanyo made their new rentals. At the same time, the expansion in Vietnam's services and telecommunications also enhances the office demand and rents.

Security is also a profound reason for higher values of prime office buildings. After the terrorist attack on September 11, 2001 in the US, several multinational companies have moved to high-security buildings (HSBC moved from REE (District 3) to Metropolitan (District 1) few months after this event. The ITC fire in November 2002 has forced tenants to seek prime office buildings which have high-grade management and modern security facilities.

In short, the above-mentioned reasons have boosted up the HCMC office demand. They may be helpful grounds for investors to make their business strategies and plans and decide the optimal projects of building offices for lease.

2. EVALUATION OF OFFICE SUPPLY IN HCMC

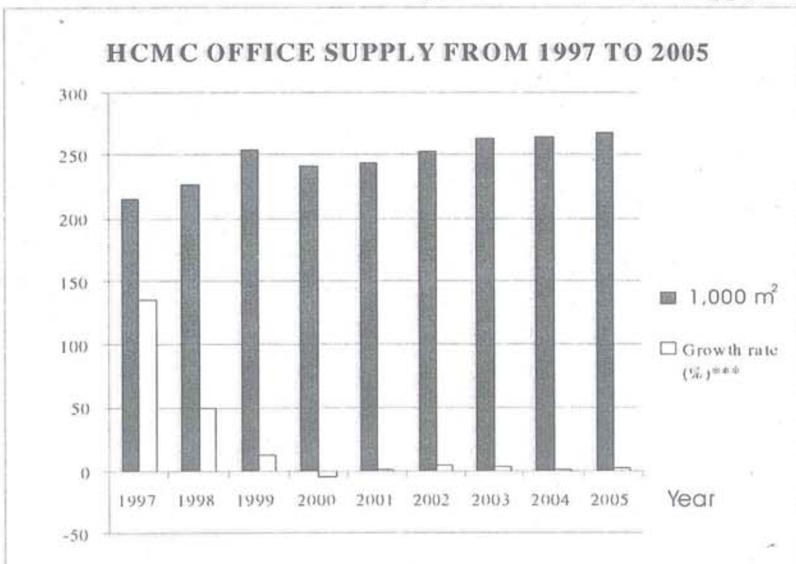
The supply of offices in HCMC

Table 2: Office supply in HCMC from 1997 to 2005

Year	Space supply (m²)[1]	Change (%)[2]
1997	214,994	135.3
1998	227,457	49.86
1999	254,656	11.95
2000	241,993	-4.97
2001	243,993	0.82
2002	252,517	3.49
2003	263,620	3.39
2004	264,460	0.31
2005	267,902[3]	1.3

Source:(1) From 1996 to 2004, HCMC Office Market (March 2005); Comprehensive list of options offer by grade A,B,C- CBRE.
(2) The authors' calculation.
(3) From 2005, Office market update Q4 - 2005 - Chesterton Petty Vietnam.

has experienced volatility over the past years. This is due to effects of the regional crisis in 1997 as well as restrictions from central and local government policies. In 1997, the office space supply reached 214,994m^2, up 135.3% as compared to 1996, 227,457m^2 in 1998, up only 49.86% over 1997. The following years saw a decline in supply, for



example, 241,993m^2 in 2000, down 4.97% from 1999. The growth in office supply is also slow in the 2002 -2005 period, even 0.31% as in 2004. This reveals the office supply is very scarce, not meeting enough requirements of local and foreign businesses, especially for foreigners. (See Table 2)

The office supply has a feature of low elasticity because it takes a long time to bring the office building into operation. In HCMC, one of reasons to hamper the supply is that office buildings have been built by foreign investors over the past years. There are a few of local investors having rich potentials and proper visions in this market. They commonly pour their money in building houses because of quick returns. As a result, the office supply in HCMC will be not abundant in the coming time and the rents are estimated to increase until 2008.

Nowadays, the office market is very hot because the supply is not up to the demand and it brings a lot of profits to the investor. High returns and increasing rents stimulate the growth in office supply. There are still no grade A office building operational in the near future while several projects of grade B and C are nearly completed and operational in the next few years. Most of foreign investors argue that this is an investment opportunity; therefore, the office market is capturing a series of projects capitalized at hundreds of millions of US dollars. Besides, several Vietnamese investors begin rushing to this attractive area.

According to statistics of the HCMC Service of Resources and Environment, projects building houses, offices, trading centers have been realized over the past years as follows: 23 projects on 47,000 m^2 in 2000; 20 on 1,172,684m^2 in 2001; 20 on 249,498 m^2 in 2002; 22 on 215,871m^2 in 2003; 10 on 652,402m^2 in 2004. In the first half of 2005, the HCMC Service of Construction granted more 14 construction permits.

In addition to office building of grades A, B, and C providing the market with a space of about 270,000m^2 and operational non-grade buildings, there are now 300,000m^2 of offices for lease. The building at 140 Nguyenn VaLn Thuf Str., District 1 providing 2,000 m^2 of office has just been completed and operated at the year beginning, but it is now totally occupied with a monthly rent of US$15/m^2. Most of its tenants are local companies. The building owner hopes to regain his investment within only three to four years.

The investment capital in this area mostly comes from foreign direct investors such as grade A and B buildings of Diamond Plaza, Sunhwa Tower, Metropolitan, Saigon Centre, and Saigon Tower with FDI from Korea, Hong Kong, Singapore and Australia and total capital of US$243,000,000. Most of local companies invest in grade C office buildings. The number of local entrants in this market remains modest because of huge investment capital. They must depend on supports from the bank or enter joint ventures with foreign partners, for example, Mê Linh Point Tower, joint venture between Chương Dương Beverage company and Central Point Properties Ltd (Singapore); Central Plaza between Sunimex and Pilkon Development Co (Hong Kong); United Oversea Land (Singapore); and Harbour View Tower with pooling from Vietcombank and Bonday Investment Ltd, Co (Hong Kong).

3. BALANCE OF OFFICE SUPPLY AND DEMAND IN HCMC

The HCMC office market tends to go towards balance. The supply was always much higher than the demand in the 1990s. However, in the first years of the 21st century the gap was nearly filled. In 1997, for example, the gap was 110,937 m^2, but narrowed to 10.716 m^2 in 2005 (See Table 3). The demand is exceeding the supply, so the rents tend to increase. The rent hike will boost up the supply. The office supply, nevertheless, has a far lag because investors must spend much time to provide their products for the market. In the meantime, the office demand keeps rising. More than 50 prime office buildings are operating at full capacity, having an occupancy rate of 95-99%. According to market surveyors, the grade A office buildings reach an occupancy rate of 99%, and the grade B and C buildings 90% - 95%. The rents of grade A have recently gone up to US$35/m^2/month. The office demand faces an annual increase of 20% - 25% while the supply is limited because projects are under construction. It takes few years to provide around 100,000m^2 of office for the market and then the shortage will be eased. Nevertheless, Vietnam's WTO membership and a new wave of investment will make the market hotter in the near future.

4. OFFICE RENTS IN HCMC

Office rents in HCMC have experienced big changes over years and strong effects from the regional economic volatility and the supply-demand rule of the market.

- Before the Asian economic crisis: From 1993 to 1996, office rents climbed to the peak. At that time, there were only a few grade B office buildings such as Hajn Nam, OSIC... in HCMC. Later, rents went up steadily to US$55/m^2/month. Until 1995, they were on the decline to US$44/m^2/month.

- After the Asian economic crisis: the 1997 regional economic crisis pushed office rents to the bottom, US$14.75 in 1999; then they were regained step by step to US$19.26 in late 2001; US$20.1 in 2002; US$21.8 in 2003 and US$24 in late 2004. In 2005, the rents reached to a profitable rate, so office owners could compensate for their loss in previous years.

- Current office rents in HCMC are as follows (before VAT)

Grade A: US$28 – 36/m2/month

Grade B: US$15 – 24/m2/month. The highest rents belong to the Saigon Tower with US$28 – 36USD/m2/month.

Grade C: US$14 – 20/m2/month.

Rents are adjusted in accordance with the time, and position of office in the building. There is also a service fee of US$5-7 in addition to floor rent. The fee is paid for maintenance, security, sanitary. It is included or not in the rent according to the investor's own decision. There are also charges of electricity, water, telephone, vehicle safeguarding, Internet...

According to the latest survey of CBRE Vietnam, the rent (including service fees and tax), the grade A office rent is currently US$27 – 30/m2/month, up 3.6% year-on-year in HCMC. In Har Nội it ranges from US$25 to 34/m2/month, the grade B offices have rents of US$12 - 25/m2/month. These rents are nearly double that of Bangkok (US$14/m^2/month) and equivalent to Singapore rents (US$29 /m2/month). This proves the HCMC office rents are now higher than those in other countries and keep rising until the supply meets the demand, and then they will drop in the common trend of regional countries.

Table 3: Office supply and demand in HCMC (1997-2005)

year	Space demand (m^2)*	Growth (%)***	Space supply (m^2)	Growth (%)	Balance
(1)	(2)	(3)	(4)	(5)	(6) = (4) - (2)
1997	104,057	31.51	214,994	135.3	**110,937**
1998	123,054	18.25	27,457	49.86	**104,403**
1999	140,927	14.52	254,656	11.95	**113,729**
2000	176,555	25.28	241,993	-4.97	**65,438**
2001	200,074	13.32	243,993	0.82	**43,919**
2002	209,589	4.75	252,517	3.49	**42,928**
2003	222,049	5.94	263,620	3.39	**40,674**
2004	231,946	4.45	264,460	0.31	**32,514**
2005	257,186**	10.88	267,902**	1.3	**10,716**

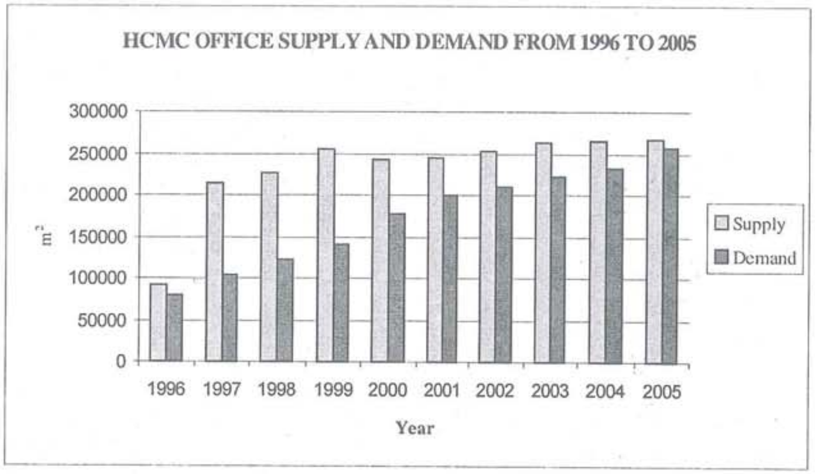
Source:-* From 1996 to 2004, HCMC Office Market (March 2005); Comprehensive list of options offer by grade A,B,C- CBRE.

*-** From 2005, Office market update Q 4-2005- Chesterton Petty Vietnam*

*-*** The authors' calculation.*

*-**** HCMC Statistics Bureau (2006), 2005 Statistical Yearbook, p.34.*

*-***** HCMC Statistics Bureau (2006), 2005 Statistical Yearbook, p.158.*



5. FORECASTS OF THE HCMC OFFICE MARKET DEVELOPMENT

5.1 The demand

First, the office market will grow incessantly along with rising growth rate of the economy, and deeper integration in the regional and the world economies, especially since Vietnam was admitted to the WTO in November 2006. The office demand is also boosted up in the near future due to increasing FDI flows into Vietnam and the national modernization and industrialization.

Second, the market will be buoyant with the participation of many new multinational companies and Asian investors in HCMC, the expansion of local businesses, the establishment of new companies and improved security, business climate and service quality.

5.2 The supply

The new supply of grade A, B, C offices is estimated at 46,000m^2 in 2006; 84,000m^2 in 2007 with 10 projects, and about 400,000m2 in 2008, 2009, 2010 with several projects which will be finished and brought into operation. These projects can meet local and foreign businesses' requirements.

+ Some buildings will be operational in 2006: Capital Place (4,800m^2), Miss Ajo Dari (3,100m^2), Rosaco Tower (12,000m^2), Vina Imex II building

(11,900m^2), Manulife Head Quarter Office (15,000m^2). E.Town 2 building will provide more 27,000 m^2 . It is owned by the REE corporation, located on Cộng Hòa Street (Tân BXnh District) and its offices have been reserved. The ITC building is located at the quadrangle of Lê Lợi - Nguyễn Trung Trực - Lê Thánh Tôn and Nam Kỳ Khởi Nghĩa streets, District 1, and under construction with total investment capital of US$50 million by the Saigon Jewelry Company (SJC). It will be completed in late 2006 with 3,805 m^2. Additionally, the Iwa Square building is also constructed with total area of 4,000m^2 in District I and operational in late 2006 ...

Table 4: Office rents in HCMC (1997-2005)

Year	Rent	Growth (%)
1997	33.15	
1998	22.87	0.68
1999	14.75	1.55
2000	16.01	1.08
2001	18.79	1.17
2002	19.83	1.05
2003	20.60	1.03
2004	21.07	1.02
2005	22.69	1.07

Source: Office market update Q4-2005-Chesterton Petty Vietnam

Investors also note that new residential areas in HCMC build in recent years, for example, Phú Mỹ Hưng new urban residence in the Sài Gòn South area will create business opportunities for companies in banking, insurance, beauty services, trading consumer goods and cosmetics and thus generate demand for offices for these companies in this area.

The office supply will be enhanced due to improved legal system, liberal policies on credit, finance, construction, land and property trading. The site area for office construction will be easily found because the Government takes effective measures to help realize feasible investment projects, for example, inspecting and stopping illegal land speculation and giving favorable conditions for revitalizing the property market.

5.3 The rents

Local and foreign investors are currently targeting at the property market, especially the office market, houses for lease due to economic growth and improved investment climate. Therefore, the shortage of prime offices will be persistent in the near future and office rents will soar.

According to forecasts of property leasing companies, office rents in HCMC may rise 10%-15% in the near future. At present, grade A office buildings increase their rent by 30 - 32% but have no vacancy. As a result, office tenants often sign leasing contracts with a minimal term of 2 years while many companies lease offices in 5 years to stabilize their accommodation, rents, and preferences or consider rents and their financial potentials to plan moving offices. Office rents remain high until the market has a lot of new supply sources.

In short, the office market in HCMC has a lot of potentials and prospects. Its development is suitable for the city's economic restructuring and expansion in favor of services, especially when Vietnam became the WTO's 150th member.■

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