

Mixed-use projects ... bringing both opportunities and risks to the commercial real estate rental industry

6 January 2020



- **Mixed-use¹ property projects are an interesting investment alternative for real estate developers, especially under the current volatile economic environment. This is because the projects diversify streams of income from the different integrated property formats, enabling a more stable recurring income as opposed to dependency on a single type of real estate format. Furthermore, mixed-use projects increase and maximize land-use efficiency, especially in prime areas with expensive land price.**

- **Going forward, the growing supply of mixed-use projects in Bangkok, especially when compared to the past, could lead to an oversupply in the real estate market. Commercial space for rent should see the most impact. Data suggests that within the next 3 years, a new mixed-use supply of approximately 900,000 square meters from commercial projects is expected, accounting for 40% of new supply within the same period. These new mixed-use supplies will be clustered in the central business district (CBD), which is already crowded with similar real estate supply. With such regards, competition in the real estate market should be fiercer in the near future.**

- **The development of several new mixed-use projects will increase competition among the mixed-use projects themselves with impact on single use buildings, such as office buildings, department stores, and hotels within the proximity as well. For this reason, single use project developers might need to lower sales/ rent, shift project launch timeline, or undergo renovations to attract tenants or customers and retain competitiveness.**

¹ Mixed-use projects are property projects with 3 or more integrated streams of recurring income with synergistic designs that integrate the different property formats in the project.

The current volatile and weakened economic environment could suppress demand for rental space in commercial real estate, which consists of office and retail rental space. Furthermore, factors such as high land prices, especially in prime areas, challenge project feasibility. These mentioned factors hence trigger various real estate developers to invest in mixed-use projects.

The 2 main features of mixed-use projects are:

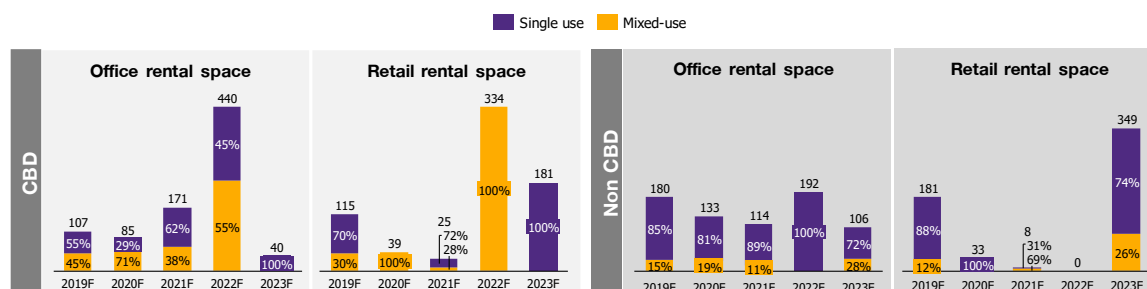
1. Mixed-use property **diversifies risks by reducing reliance on a single type of real estate format as the project has various sources of recurring income from the different integrated property formats**. During periods of economic or business slowdown, the various sources of recurring income will help the mixed-use project mitigate severe impacts. Take tourist growth slowdown for example, the slowdown will suppress rental income from retail and hotel tenants. However, in the mixed-use project, rental income from other uses, for example, the office space will not be impacted by slowing tourist growth. As such, income from the mixed-use property will not be as severely impacted as income from the single use retail building.
2. Mixed-use property **increases and maximizes land-use efficiency**, as land in prime locations is scarce and expensive. The synergy between usage of the different real estate formats within the project is key, and many areas can be shared among the different formats.

However, the rapid supply growth of mixed-use projects during 2020-2023 could intensify competition and lead to an oversupply in commercial rental space in Bangkok. In 2020-

2023, approximately 2 million square meters of new commercial rental space in Bangkok will enter the market, approximately 900,000 square meters of which are new mixed-use space, representing as high as 40% of total new rental space (Figure 1). However, EIC expects that new commercial rental space demand in Bangkok during the mentioned period will be only 1 million square meters. Therefore, oversupply risks, especially in areas with new mixed-use projects, are likely. A preliminary study based on 14 selected property projects found that most new mixed-use projects will be located in the central business district (CBD). Of which, 64% will be launched in the prime CBD areas such as Silom-Sathorn, Early Sukhumvit (Soi 1-41), and Phetchaburi, while the remaining 36% will be launched in non CBD areas such as Bang Sue, Bangna-Trat, Srinakarin, and Chaeng Watthana. Furthermore, the study suggested that of the new mixed-use project space, retail space contributed as high as 22% of the total new space followed by office space at 19% (Figure 2). Hence, mixed-use project developers and developers with single use project in the proximity could confront oversupply risks.

Figure 1: New commercial rental space in Bangkok classified by usage and format

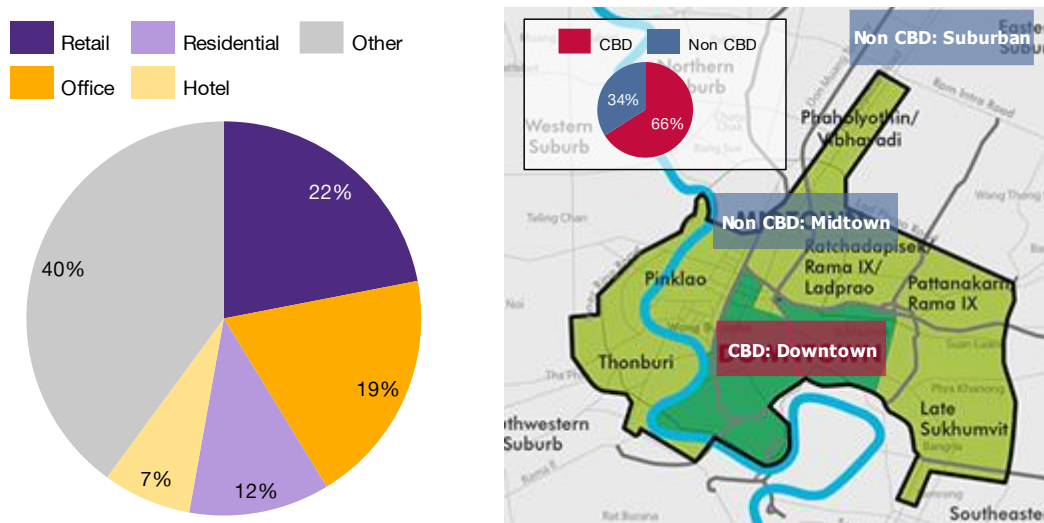
Unit: 1000 square meters



Source: EIC analysis based on data from projects, CBRE, and press search

Figure 2: Proportion of mixed-use project space classified by format and location

Unit: %



Remarks: Total space and proportions calculated from preliminary released data of the 14 selected mixed-use projects, which started operation since 2018.

Source: EIC analysis based on data from projects, CBRE, and press search

The commercial real estate rental business in Bangkok continued to grow. The office rental real estate grew mainly from increasing rental price and the retail rental real estate driven by occupied space. Analysis of CBRE data found that during 2014-2018 the market value of office rental space in Bangkok grew continuously by 8% per year and reached THB 80 billion in 2018. Constantly rising rental rate of approximately 6% per year during the mentioned period drove the growth as new occupied space grew faster than new supply. Meanwhile, the market value of retail rental space in Bangkok grew by 4% per year during the past 4 years, reaching THB 90 billion in 2018. The growth was driven by growing take-up at 4% per year during the same period, though the rental rate remained stagnant.

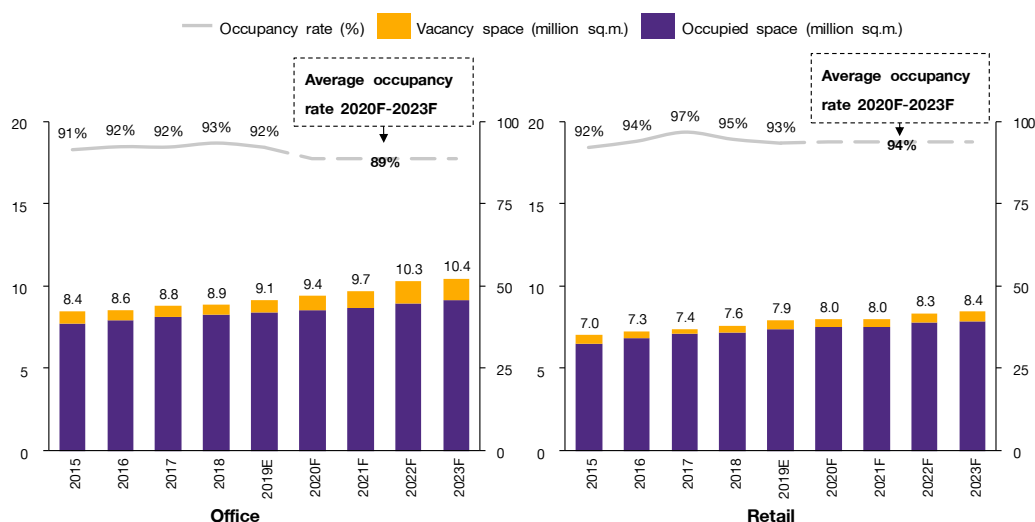
Even though occupancy and rental rate of office space in Bangkok continue to grow, the continual launch of projects, especially mixed-use projects in the next 3-4 years could lead to an oversupply in office rental space. A continual launch of real estate projects within the next 3 years (Figure 3) will put approximately 1.3 million square meters of office rental space into the market, or equivalent to 14% of existing supply. Of the new supply, 400,000 square meters will be from mixed-use projects. Such a high supply compared to projected demand could lead to an oversupply. Going forward, EIC views that the overall occupancy rate of office space will gradually drop. In 2023, the occupancy rate could decline to an 8-year low at 86-87% comparing to 93% in 2018 and 92% in 2019. Similarly, office space rental rate growth could slow as well. In 2020-2023, rent could increase by as low as 1% compared to the 4% growth in 2019 and the average 6% growth per year during 2014-2018.

On the other hand, retail rental space in Bangkok will see slowing demand due to 1) slowing retail industry momentum, which could lower occupancy rate while heightening competition and 2) competition from e-commerce growth, which could curtail demand. The retail industry outlook weakens following clouded economic conditions. Similarly, spending from tourists, both domestic and foreign is expected to grow at slower rates. Furthermore, structural changes in the retail industry, led by the growing e-commerce sector could curb retail space rental demand. This is because retailers have the option to sell products online from the support of marketplace platforms (such as Lazada and Shopee), social media, or their websites. Luckily, the growing online to offline (O2O) trend, for instance, offline Multi-Brand Stores to support online sales, can somewhat shore up retail rental demand. The offline Multi-Brand Store is popular among fashion and beauty retailers and is where the products of various retailers from various online platforms are showcased to customers.

The aforementioned factors could **slow branch expansion/ new store establishment** and lower demand for retail rental space. Prospects of rental rate of retail space² increment will hence weaken from both fixed and percent of tenant sales rent. Fixed rent growth will be challenged by lower take-up. EIC evaluates that during 2019-2023 there would be an additional 170,000 square meters of retail rental space per year (50% of which will be from mixed-use projects). On the contrary, a new take-up of only 140,000 square meters per year is expected (compared to a new take-up of 260,000 square meters per year during 2014-2018). With such regards, the occupancy rate should drop to an average of 94% in the next 4 years, a rate lower than the peak at 97% in 2017 (since data collection commenced in 2006). Meanwhile, percent of tenant sales rent will soften following **slowing retail sales**. For these reasons, retail rent should stagnate/ minimally increase during the next 3-4 years.

Figure 3: Supply and take-up of commercial rental space in Bangkok

Unit: Million square meters (LHS), % (RHS)



Source: EIC analysis based on data from CBRE

² Rent income from retail space consists of 2 types: fixed rent and percent of tenant sales rent

Growing mixed-use space rallies up competition among mixed-use developers and developers within the proximity. However, the mixed-use projects bring both positive and negative impact, in which the momentum of the impact will differ according to various factors, for example, project size, surrounding environment, properties in the project, and project success.

Positive impact on the overall commercial rental space

Some mixed-use projects will positively enhance surrounding areas, especially if **the project's core format is different from the format in the surrounding areas** and if the project is **in non CBD areas** (with low competition). The Celebrations of Glory press release revealed that after operating the ICONSIAM project for 1 year, businesses along the Chao Phraya River such as tourist spots, restaurants, and surrounding eatery saw growth of over 20%. New condominiums launched in the area during 2017-2019 also saw average sales of as high as 95%. While, occupancy of Chao Phraya riverfront hotels also improved, for instance, the 5-star hotels that saw occupancy rates of 85-90%. The Bangkok Mall with a project size of over 1.2 million square meters is another great example. The project's first phase focus on developing a large retail and recreational space, a format that accentuates family gatherings. The mentioned development could turn Bangkok Mall into Bangna's new landmark, which should benefit residential projects in the surrounding areas such as low-rise projects or condominiums.

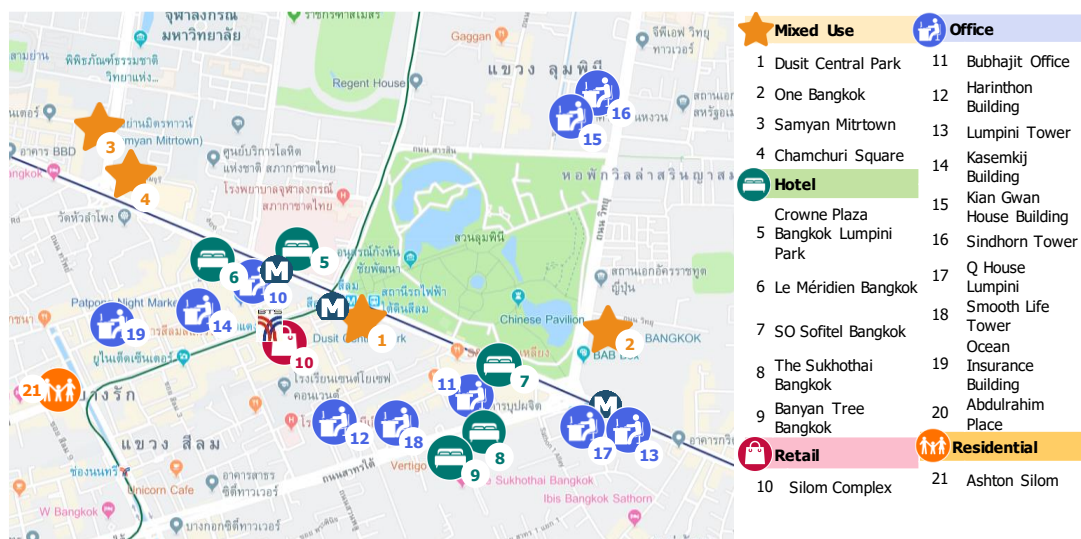
Negative impact on the overall commercial rental space due to increasing mixed-use projects

1) Mixed-use project developers could be challenged by longer project payback periods. Volatile economic conditions weaken demand. While rapid growth in mixed-use projects induces fiercer competition in the market. As such, mixed-use project investment, especially in large projects, will confront with longer payback periods.

2) Growing pressure and competition could lower revenue for single use project developers in the coming periods. The expected launch of several new mixed-use projects in the next 3-4 years will compete with single use projects in the surrounding areas. As such, single use developers will see fiercer competition:

- The Rama 4 area: Various new mixed-use projects will be launched in the Rama 4 area, for example, One Bangkok and Dusit Central Park. The launches could (1) Lower occupancy rates of existing office buildings in the Rama 4, Sathorn, and Silom area due to higher competition from new mixed-use space, (2) Lower the scarce supply advantage that existing office buildings in the CBD connecting areas had during the last 3-4 years, as once the new mixed-use projects are launched in the CBD area, the projects will better respond office space demand, (3) Lower take-up of existing hotels on the Wireless Road, Silom, and Sathorn area due to growing competition, and (4) Heat up competition for luxury condominiums, as the projects target the same group of luxury consumers.
- The Bangna area: The development of Bangkok Mall, a mega-sized mixed-use project that focuses on retail, will directly compete with surrounding department stores such as CentralPlaza Bangna or Seacon Square.

Figure 4: Key real estate projects located on the Rama 4 road



Source: EIC analysis based on data from companies and press search

Amid challenges and risks, successful mixed-use projects need to improve upon their weaknesses and differentiate to attract customers. The differing strengths among the mixed-use projects will increase the chance of success, while some projects still face fierce challenges that require solutions for a new comeback, for example:

The **Samyang Mitrtown project** was situated in a hard-to-commute location as customers who travel by MRT mass transit will need to walk for about 300 meters, including crossing a road. The project turned this weak point into a selling point by constructing a tunnel that directly links the project to the MRT station. The move facilitated travel convenience and increased foot traffic. Furthermore, the project provides 24 hours service as another key selling point, which perfectly suits the demand and lifestyle of customers in the area, for instance, students with demand for late-night studying. With such regards, the project received good feedback evident from office occupancy of 60% since the first month of the opening, a rate higher than comparable projects³ with an average 50% occupancy during the first quarter of their opening. Furthermore, the project's retail space occupancy rate was at 85%, a high rate, especially compared to other shopping malls that opened during the same period, such as, The Market Bangkok that had a 77% occupancy rate during its launch.

Meanwhile, **mixed-use projects such as ICONSIAM** unveiled its project with a retail space occupancy rate of as high as 91%. Even though the project was not located in the CBD area, the project used the riverfront location as a selling point in addition to project size and diversified offerings. Furthermore, the project continually hosts events to attract customers. This strategy allowed ICONSIAM to become a large landmark in the Thonburi area.

³ Based on JLL's office space occupancy rate study of 8 key projects: AIA Capital Center (2014), AIA Sathorn (2015), Bhiraj Tower @EmQuartier (2015), FYI Center (2016), Gaysorn Tower (2017), Singha Complex (2018), and T-One Building (2018)

For the **Emsphere project**, under the management of The Mall Group, the project created its differentiation by joining hands with Anschutz Entertainment Group (AEG), a global leader in the entertainment and sports industry. Under the alliance, the project created a large arena named EmLive within the project. This project hence served as an upgrade and fulfillment for the overlying The EmDistrict project.

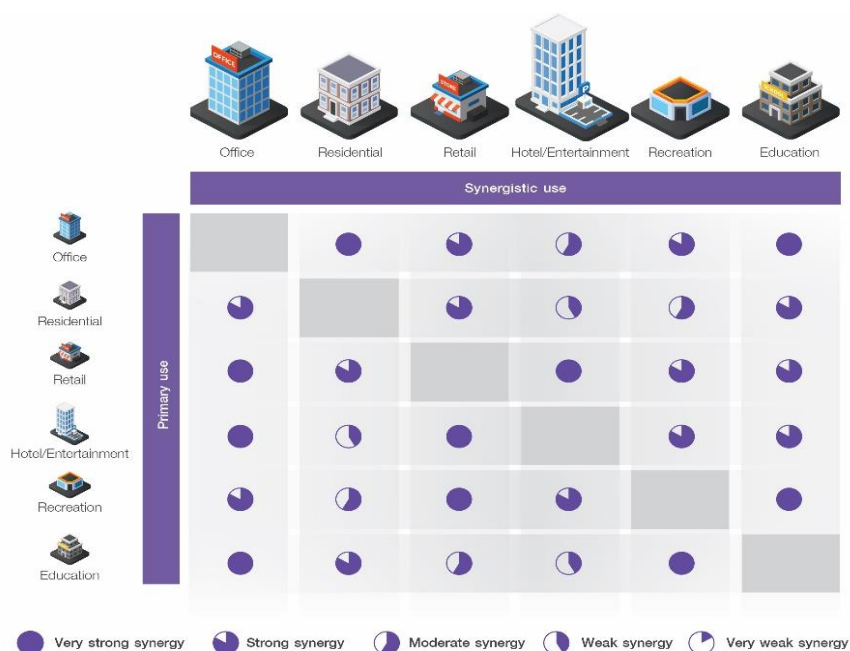
Mixed-use project developers need to possess the following key success factors to be able to compete in the market 1) experience in real estate business operations, 2) suitable and travel convenience location, and 3) synergy between the different property formats.

From the EIC's previous article (EIC NOTE 'Creating new landmarks using a mixed-use concept'⁴) found that developing mixed-use property does not guarantee success, as its success depends on many other aspects, such as the following 3 key factors:

1. **Experience in real estate business operations**, whether from the developer or the partners. The factor can be evaluated according to the synergy of the mixed-use project characteristic and past project performance, in addition to the duration of the real estate business operation. Experience in operating a particular type of real estate project is important, especially in areas that relate to property usage within the project.
2. **Suitable and accessible location**. The project design will need to consider needs in the surrounding areas as well, for example, if the project is located in a business area, the main need could be for office space such as the area on Rama 4 road that continues from the Silom and Sathorn road. While in residential areas, the main need could be for retail space to enable shopping and travel convenience. The most suitable locations would be, for example, close to the mass transit stations (not exceeding 100 meters or with direct access to the project) or close to expressways (not exceeding 1 kilometer from the entrance or exit).
3. **The synergy between the different property formats, while maximizing land-use efficiency**. The project design must consider synergistic usage among the different types of property format within the project. Furthermore, collaborating planning between the primary use areas (the main revenue-generating area in the project) and the synergistic use areas (other areas in the project) is required. According to a study by The US Urban Land Institute regarding synergistic benefits between the primary and synergistic areas (Figure 5), mixed-use projects that are predominantly retail have higher synergistic benefits. This is because retail space is compatible with many types of real estate formats. For example, in a retail/office mixed-use project, the retail space will attract customers who are office employees in the synergistic office zone of the project. Meanwhile, the mentioned mixed-use project will be more attractive than single use office buildings due to the convenience the retail space gives to the tenants. On the other hand, mixed-use projects that are predominantly residential have a lower synergistic benefit due to the need for personal space. The mixed-use combination of residential-hotel/entertainment complex is one of the combinations that receives the least synergistic benefit due to the contrasting need between quiet personal space and noisy liveliness. In such projects, the developers will need to be able to manage the rules and boundaries between private and public areas, especially regarding the safety of the residential tenants.

⁴ EIC NOTE 'Creating new landmarks using a mixed-use concept'

Figure 5: In mixed-use projects, the retail space will receive the highest synergistic benefits



Remarks: read more in EIC NOTE 'Creating new landmarks using a mixed-use concept'⁵

Source: EIC analysis based on data from the US Urban Land Institute

Apart from contemplating the success factors, mixed-use developers need to be aware of various challenges as well, namely 1) managing private space versus common area, 2) creating magnet attractions to lure in traffic, and 3) managing infrastructure within the project.

1. **Management of private space versus common area.** Some types of property formats require specific amenities such as retail space. For example, during events, the retail space will need to be managed properly so that the sound and duration of the event will not disturb other tenants in the project, especially in the residential zone that is private space. Therefore, project developers need to reduce the impacts that could occur between each type of property, such as separating the entrance-exit of each area, limit activities with loud noises, or design a soundproof area.
2. **Magnet attractions to pull in traffic.** Each project will need to have at least one magnet attraction to pull traffic into the project. For example, projects with large retail space could use its recreational area as a magnet and pull in traffic by continually hosting high-demand events. Furthermore, the projects need to attract key tenants that will offer products and services that respond customer needs, such as popular restaurants and supermarkets.

⁵ EIC NOTE 'Creating new landmarks using a mixed-use concept'

read more: <https://www.sceic.com/en/detail/product/4043>

3. **Infrastructure management.** Infrastructure needs to be properly managed for maximized efficiency and benefit. The facilities demanded for each type of property format will be different according to the purpose of use. Take the layout for amenities in the residential space, for example, the plan could place an elevator next to the entrance of the condominium, while for hotels, the layout will need a large lobby space instead. The main key point is to efficiently design, manage, and administrate the project to control costs. Moreover, the project developer should also consider efficient resource planning and design, such as water reuse systems and usage of natural lighting instead of lamps.

Launches of various new mixed-use projects will level up the competition, single use project developers will need to change and adapt to maintain the project's competitiveness. Some adjustments could be, for instance, the decision to lower rental fees of office space in single use office buildings to attract more tenants, especially for tenants that are very sensitive to price changes, or to renovate the project to attract new tenants. For single use retail rental buildings, developers could find key tenants that will attract traffic into the project or renovate the project to attract niche groups of customers with a specific concept. If the project is unable to compete regarding retail space usage variety with other large projects, the developer could, for example, focus on drawing in restaurants to create a center of food excellency. Or the developers could choose to renovate the project to maintain competitiveness. While for single use condominiums, a thorough examination of new supply that will be launched from the mixed-use projects in the area is required. If a large mixed-use project is to be launched within the area, condominium developers could work around the issue by targeting a different customer segment or reconsidering the project plan to avoid fierce competition.

By: Pattharapon Yuttharsaknukul (pattharapon.yuttharsaknukul@scb.co.th)
Analyst
Economic Intelligence Center (EIC)
Siam Commercial Bank Public Company Limited
EIC Online: www.scbeic.com
Line: [@scbeic](https://www.facebook.com/scbeic)

