NUS National University of Singapore

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SINGAPORE PROPERTY

Developers' margins squeezed by higher land, construction costs: survey

BT EXCLUSIVE

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THE pains of margin compression for property developers in Singapore look set to continue, given recent tightened border measures due to the surge of Covid-19 cases in India.

It comes as profit margins of developers had already thinned from the year-ago period, despite developers seeing strong private-home sales, according to a survey.

An increase in construction costs, land costs and agent commissions were among the reasons cited for these thinning margins.

For its Q1 2021 survey, the National University of Singapore Real Estate (NUS+RE) polled 49 senior executives in Singapore's real estate sector, with 24 developers among them. NUS+RE collectively represents the Department of Real Estate and Institute of Real Estate and Urban Studies (IREUS). Questions about profit margins were posed solely to the developers, while the rest of the survey involved all respondents.

Based on the responses, margins narrowed by 5-10 per cent from pre-pandemic levels for nearly half of the developers, and by 10-20 per cent for another 30 per cent of them.

About 13 per cent of developers saw margins thinning by less than 5 per cent, while 9 per cent reported contractions of over 20 per cent.

The Business Times (BT) reported in March that pre-tax profit margins for some private housing projects had fallen to around 10-12 per cent, or even sub-10 per cent.

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Developers' margins squeezed by higher land, construction costs

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The biggest reason for shrinking margins was said to be the labour crunch in the construction sector, due to border restrictions during the pandemic, according to the NUS+RE survey findings.

Besides the manpower shortage, building materials also became more expensive as both freight and raw material costs shot up last year, NUS+RE noted. This likewise drove construction costs higher.

IREUS deputy director Lee Nai Jia expects such margin compression to persist for at least six months and up to a year, especially given the recent tightened border measures with India.

The travel ban, which kicked in on April 23, has affected the flow of Indian workers into Singapore. While the Building and Construction Authority would provide temporary flexibility in recruiting workers from China, construction firms would still need time to train these new workers and get them up to speed, Dr Lee noted.

Starting this week, border restrictions will be tightened again amid the rising spread of Covid-19 in Singapore. From 11.59pm on May 7, all travellers with travel history over the past 21 days to higher-risk areas will have to serve a 21-day stay-home notice in a dedicated facility. This is up from 14 days for certain countries now.

As at May 4, all places or regions are deemed to be of "higher risk", except for Australia, Brunei, mainland China, New Zealand, Taiwan, Hong Kong, and Macao.

Meanwhile, emergency legislation will be announced here soon to address the severe disruption to the construction sector arising from curbs on the entry of migrant workers.

In the May Day Rally, Prime Minister Lee Hsien Loong said it will be aimed at making the burden to be shared more fairly between the different parties – the contractors, the developers, and the buyers.

Other factors contributing to the margin contraction included a rise in fees that developers pay real estate agents to market their properties, as well as higher land costs, according to the poll results. About 30 per cent of developers said these were the top two reasons for their depressed margins in 2020.

The uptrend in agent commission rates may have started before the Covid-19 pandemic, perhaps shortly after the last round of cooling measures in mid-2018, Dr Lee said.

"However, not all developers were into increasing commissions then. I think more of them could have raised the commission payouts during the pandemic to be on par with other developers," he added.

Cooling measures aimed at keeping property price increases in line with economic fundamentals have also limited developers' pricing power, BT earlier reported.

Separately, integrated projects may be becoming more popular with developers, going by the study results. Some 82 per cent of the 49 real estate executives polled expected an increase in the number of developers bidding for integrated developments.

"As the Covid-19 outbreak has led to more firms adopting flexible work arrangements, developers will have to rethink future designs for workplaces and home spaces, and ultimately the type of development to build," NUS+RE told BT.

Still, there are downside risks for developers in taking up integrated projects. For instance, 73 per cent of respondents said the five-year deadline to complete and sell all units in order to qualify for remittance of 25 per cent additional buyer's stamp duty would pose a challenge to those undertaking such projects.

A third of real estate executives also expressed concern about the longer construction period for integrated developments, when compared to conventional residential projects.

Other challenges included the two-envelope tender approach, which locks in funds for a longer period while proposals are being evaluated. Restrictive regulations may also prevent developers from experimenting with alternative housing models, more than half of the respondents said.

For instance, if an integrated-development site has certain tender conditions that could be expensive to fulfil, developers may in turn have less of an incentive to "offer co-living spaces or serviced apartments that are more suited to the footloose millennial workforce in the future, post-Covid-19", Dr Lee said.

Under the government land sales programme, a commercial and residential site in Jalan Anak Bukit was launched last June via a two-envelope tender. The deadline has been extended to June 29, 2021, BT reported.

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Singapore's property market risks facing cooling measures ahead: poll

Other concerns highlighted in the Real Estate Sentiment Index include construction costs and rising interest rates

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COOLING measures now make up the biggest risk faced by Singapore's real estate market.

That's according to the latest Real Estate Sentiment Index published by the National University of Singapore Real Estate (NUS+RE), which represents the Department of Real Estate and the Institute of Real Estate and Urban Studies at the university.

Out of the 40-50 real estate executives surveyed in March, 87.8 per cent indicated the possibility of cooling measures as a potential risk, which may adversely impact market sentiments in the next six months.

This is almost double the previous quarter's 44.7 per cent.

The second biggest risk was rising construction costs, which was highlighted by 77.6 per cent of respondents in Q1 2021.

This proportion is slightly down from 85.1 per cent in Q4 2020.

Meanwhile, the proportion of respondents who indicated rising inflation or interest rates in their answers jumped to 65.3 per cent from 8.5 per cent in December.

The category saw the biggest change in the two quarters and placed third on the list.

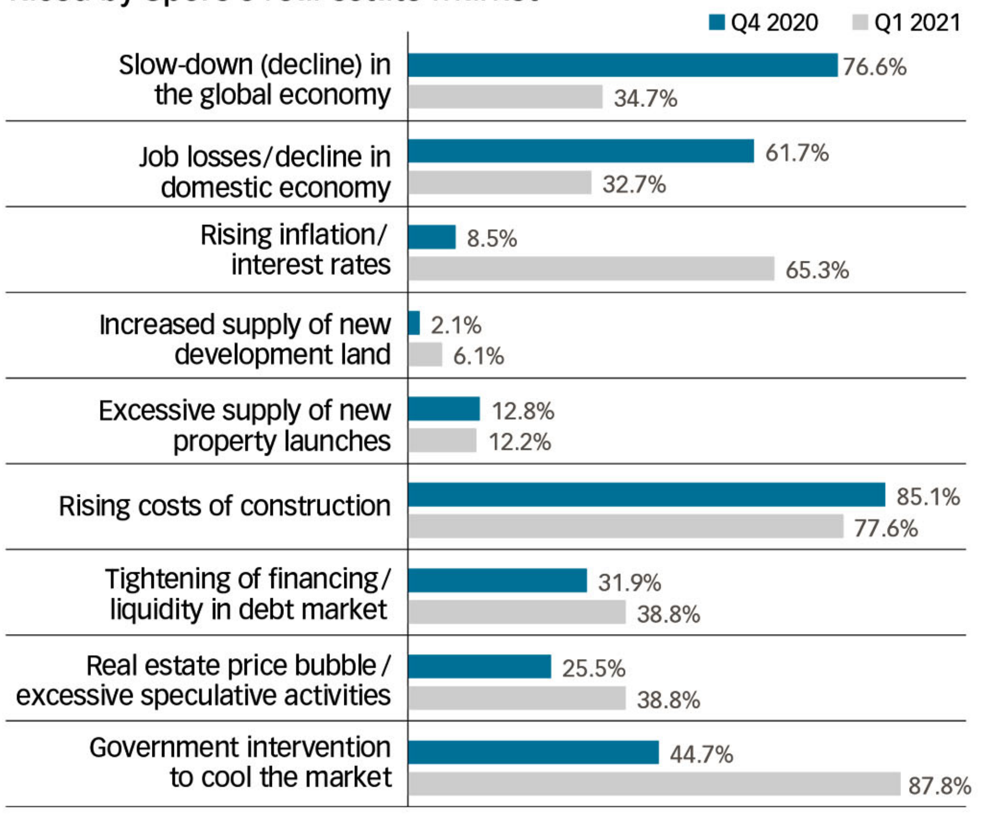
In contrast, those who indicated job losses/a decline in domestic economy as a potential risk factor fell to 32.7 per cent from 61.7 per cent, while those who were worried about the slowdown in the global economy halved to 34.7 per cent from 76.6 per cent.

Among the developers surveyed, rising labour cost was the biggest source of concern relating to development costs.

"The construction industry is facing challenges in employing workers and the limited supply of migrant workers pushes up labour costs," said one developer.

Potential Risks

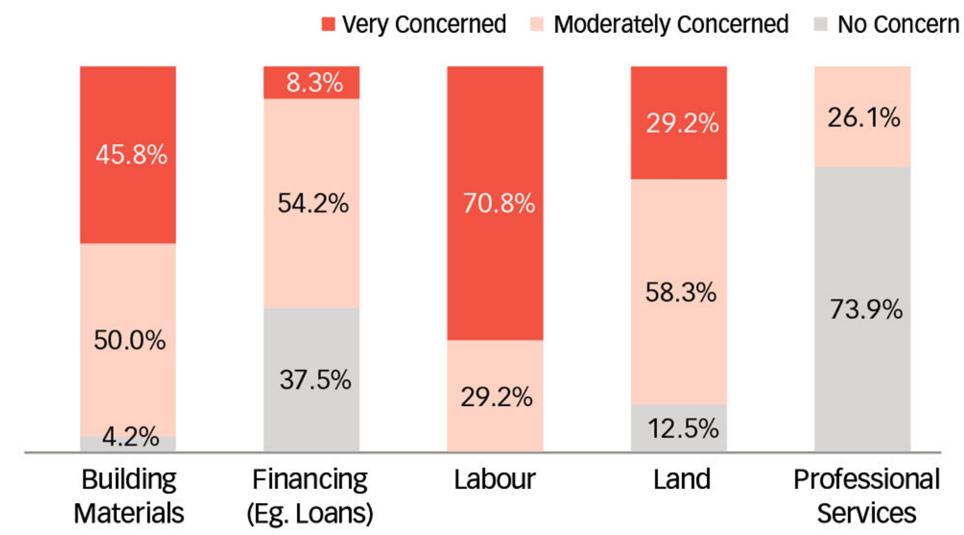
Cooling measures now make up the biggest risk faced by Spore's real estate market



Source: NUS+RE report

Level of concern

Among the developers surveyed, rising labour cost was the biggest source of concern relating to development costs



Source: NUS+RE report

Some 70.8 per cent indicated that they were "very concerned" about high labour costs, while the remaining 29.2 per cent indicated "moderate" concern.

Building materials cost was also a major source of concern.

Some 45.8 per cent said they were "very concerned", 50 per cent were "moderately concerned". The rest showed no concern.

In terms of future launches and sales, about 70 per cent expected the number of units launched to be moderately or substantially more in the next six months, while 12.5 per cent predicted moderately fewer launches.

One respondent said: "Developers would continue to push out more launches over the next six to 18 months for land parcels that were bought between 2016 and 2018, due to the additional buyers stamp duty five-year completion requirements."

About half of the developers surveyed expected moderately or substantially higher prices, while 41.7 per cent predicted that prices of the new launches in the next six months will be at the same level as prices in Q1 2021.

"The improved market sentiment and the strong demand, coupled with the depleting pool of unsold units, will allow developers to settle at higher prices," said another respondent.

The study's composite sentiment index, a derived indicator for the overall real estate market sentiment, has risen since the lifting of circuit breakers.

Measured from a scale of 0 to 10, the index reached 6.8 in the three months from its previous 6.5, with respondents observing that market conditions have improved in Q1 2021 and will continue to improve in the coming six months.