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POSTgraphics

The significant growth forecast for Cambodia, Burma and Laos may yield big opportunities for investors, but these volatile markets aren't for the faint-hearted

By Tony Picon

As the region moves towards further integration under the Asean Economic Community in 2015, attention will be focused on the lesser developed countries that border Thailand. Cambodia, Laos and Burma will make up an essential part of the economic fabric of the region and Thailand in particular. Each is likely to be a significant growth story over the next generation. It is therefore an opportune time to analyse their property markets.

As integration continues in Asean, Thailand's three northernmost neighbours are just entering or about to embark upon the first phases of export-led development, which Thailand went through starting in the 1970s. As such, they are likely to play a strong role in the supply chain due to an abundance of cheap labour and direct access to the powerful markets of India, China and Vietnam. As a result these property markets are also likely to be of interest to investors from Thailand, and many are already involved.

Volatility is the main concern comes to property in the frontier markets, and there are a number of reasons why.

First, when a new market emerges there is very little office space due to lack of commercial activity.

Most businesses are located in shophouses, villas or even serviced apartments, hotels and condominiums. As pressure builds, office locations are highly sought after, especially in the business districts of a major city. Ho Chi Minh City in Vietnam is a good case in point. Only a few years ago, demand so far outpaced supply that a top office building could command rentals equivalent to 3,000 baht per square metre per month (700 baht will secure prime office space in Bangkok) and achieve 100% occupancy. Consider the chart on this page, which shows total office supply in Ho Chi Minh City, Vientiane and Rangoon compared to just one office building in Bangkok.

The problem arises when developers take note of such pent-up demand, which usually triggers a surge in new supply. In Bangkok an addition of 100,000 square metres in 2011 would make only a small change to the office market dynamics, but in frontier markets a sudden influx can lead to dramatic changes in occupancy and rentals.

In Ho Chi Minh City, rental rates for grade A office space dropped by 40-50% in one year due to the sudden influx of supply coming onstream in a short period. The result is often stalled or "slow-track" construction, to delay completion while giving the appearance of activity. The same thing can apply to the retail and hospitality sectors depending

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on demand and supply.

Changes to government policy can also have a significant impact on the property market in nascent economies, both negative and positive. Changes to investment or foreign ownership laws can lead to a surge of interest and this can lead to a speculative boom in prices. This in turn creates inflationary pressures that can come to a crashing halt with blunt tools to cool the market. This was the case of Vietnam in 2008, with high-end condo prices falling 40% in one quarter in Ho Chi Minh City.

In frontier markets local developers often have little experience in the property market and are normally companies involved in other industries that wish to jump on the bandwagon. This means that projects can be poorly thought out.

Even some experienced foreign developers make mistakes by not taking into account the very different conditions that exist in these markets.

That said, one key point in favour of Thailand's neighbours is demographics. Laos and Cambodia in particular are entering a strong potential growth period as a significant proportion of their population is of working age. Assuming reasonable government policies encouraging industrial and service-led development, the property market will benefit from sustained economic growth, but with convulsions on the way.

CAMBODIA: DREAMS VS REALITY

The uncompleted Gold Tower 42 is a potent reminder of the dangers of grandiose visions. Now nicknamed Gold Tower 31-and-a-half, building has been halted for over a year on the luxury apartment development with retail and commercial components. Other plans and half-completed projects such as Camko City and the International Financial Centre have been halted or never got off the ground.

This has not stopped more grand designs from being espoused, such as a plan to build the second tallest building in the world. However, the current property downturn in Phnom Penh belies the real story. Cambodia is embarking on a period of strong economic growth on the back of significant investment in manufacturing, agriculture and tourism. The Japanese, usually cautious when it comes to investing in a new country, are now entering Cambodia; as wages are lower than in China or Thailand for example.

With such growth there will be an increasing demand for quality office space and it will only be a matter of time for the existing supply to be absorbed. There will likely be a requirement for new office buildings over time but not for skyscrapers. Future office projects under construction are limited in size, which bodes well for the market.

An international airport has been constructed in Sihanoukville, but as yet there are no scheduled flights to access the pristine coastline or islands. When this changes more attractions will be on the radar for tourists than just Siem Reap, the home of Angkor Wat. A recent decree allowing for foreign ownership of condominium units above the ground floor could spur the property sector, which has relied on speculative demand and has been volatile.

LAOS: AT ITS OWN PACE

Vientiane bears more resemblance to a sleepy South American town than the commercial hub of another emerging tiger. That is its charm and the authorities appear to wish for a more moderate trajectory of growth. Office supply is limited as most business now takes place in villas. With a population of around 800,000 and extensive activity by non-governmental organisations (NGOs) a significant amount of property activity is undertaken by diplomatic missions and NGOs in villas for their own operations and as residences for expat employees, who also are a strong market for serviced apartments. However, more companies are emerging, especially in energy, mining and logistics.

Laos is attracting investment from Vietnam, China and Thailand, bringing more foreign residents and business travellers, which along with growing tourism is helping to spur hotel occupancy. Although no international hospital exists, the first private clinic recently opened and a first-class accredited international school is growing. The jigsaw pieces of an international city are fitting into place. The retail component is still mostly in the form of traditional shopping centres, but Big C will open next year and more modern retail outlets are due over the next few years.

The abundance of land in the capital and foreign ownership restrictions mean there are no apartments for sale in Vientiane. Height restrictions maintain the unique character of the capital and the riverfront area is being rejuvenated with eclectic designs that add to the city's character. Other projects are less appealing, however.

BURMA: THE LAST TIGER, YET TO ROAR

Burma has long remained largely unplugged from the rest of the world, which has dragged the economy down. Almost unbelievably for a city the size of Rangoon, office space is just 50,000 square metres, with very strong occupancy rates now being recorded as businesses set up operations, usually starting with a representative office.

Apartment and condominium development is robust, especially in the middle-income sector, as many prefer high-rise to landed properties following the damage inflicted by Cyclone Nargis in 2006. But quality and design are poor with no juristic person to ensure maintenance. Intermittent, although improving, electricity supply means that lower floors are more popular than higher levels.

Burma has all the tourism attributes that could lead to it becoming a new Thailand. Already hotels and serviced apartments in Rangoon are recording near-100% occupancy as tourists return following the release of Aung San Suu Kyi. There are concerns that severe hotel supply bottlenecks in Rangoon will hamper tourism growth. The country is still held back by sanctions, but if they are ended soon investors will flood into Burma and all property sectors will rapidly develop.

Thailand's underdeveloped neighbours offer different opportunities and challenges, and investors could be in for a roller-coaster ride. But the ride will be advantageous to the patient but brave investor. Those who become involved will also shape the landscape of these countries in the course of their development, guaranteeing exciting times ahead. ■

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