

Briefing Industrial sector

May 2015



Image: Tsuen Wan

SUMMARY

Industrial sales slowed but sentiment remained positive in Q1/2015.

- En-bloc deals were still evident, though on a much smaller scale than last quarter, with redevelopment potential the key theme behind such purchases.

- Slowing retail sales has had a knock-on effect on retail-related logistics demand.

- Some multinationals switched to cost-saving mode and were keen on one-storey sheds in the New Territories amid escalating rents.

- With warehouse vacancy gradually rising, we expect to see more space

being made available to the market in the near future.

- Investment volume and value are likely to dwindle over the next few months due to a lack of quality stock as well as increasing difficulty to secure financing.

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 “Hit by a lack of billion-dollar deals, investment sales slowed but redevelopment potential was again the catalyst behind most en-bloc transactions. Logistics demand was dragged down by the slowing retail market with some vacant space being gradually released to the market.” Simon Smith, Savills Research

→ **Sales market**

Sixteen major transactions of over HK\$30 million were concluded in Q1/2015. Almost a reverse of last quarter, volume increased by 45% quarter-on-quarter (QoQ) but total consideration declined by over 60% QoQ to reach HK\$2.1 billion.

After a busy Q4/2014, investment sentiment quietened in the first quarter of 2015, not only in the number of transactions over HK\$100 million, but also in regards to the size of the deals, as no billion dollar deals were inked over the quarter (the largest one being slightly below HK\$500 million).

Notably, the buyers of the few larger deals were more focused on their redevelopment potential, including Soundwill's purchase of the en-bloc Chip Tak Weaving Factory Building in Kwai Chung for HK\$452 million, as well as the sale of Yue Fung Industrial Building in Yuen Long for HK\$430 million.

Leasing market

Slowing retail sales has had a knock-on effect on retail-related logistics demand, and many operators stopped expanding on the back of declining demand. Coupled with the traditional quiet period for logistics between Christmas and Chinese New Year, significant leasing transactions were hard to come by.

As predicted previously, more warehouse space was released to the market towards the end of Q1, concentrated in warehouses in the Kwai Tsing/Tsuen Wan area. Nevertheless, these units were only available in smaller areas (around 10,000 to 30,000 sq ft), and thus the overall vacancy rate of warehouses only increased marginally to 1.2% over the quarter.

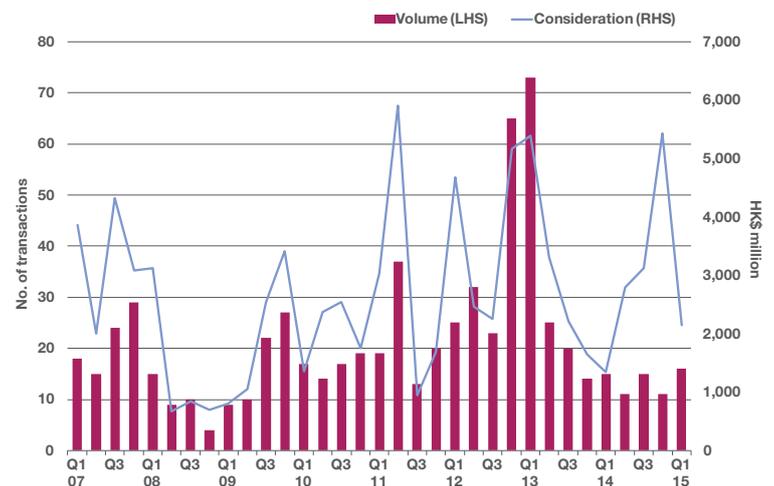
While warehouse rents continued to increase and many logistics operators, including some multinationals, switched to cost-saving mode, we nevertheless saw an upturn in interest for one-storey sheds in the New Territories, in particular those which have genuinely been granted waiver to operate as storage space. However, we saw the

TABLE 1 **Industrial price growth by subsector, Q1/2015**

| | Q1/2015 (%) | 2014 (%) | 2013 (%) |
|-------------------|-------------|----------|----------|
| Flatted factories | +2.3 | +17.4 | +5.0 |
| I/O | +2.1 | +13.2 | +5.2 |
| Warehouse | +2.5 | +9.4 | +16.3 |

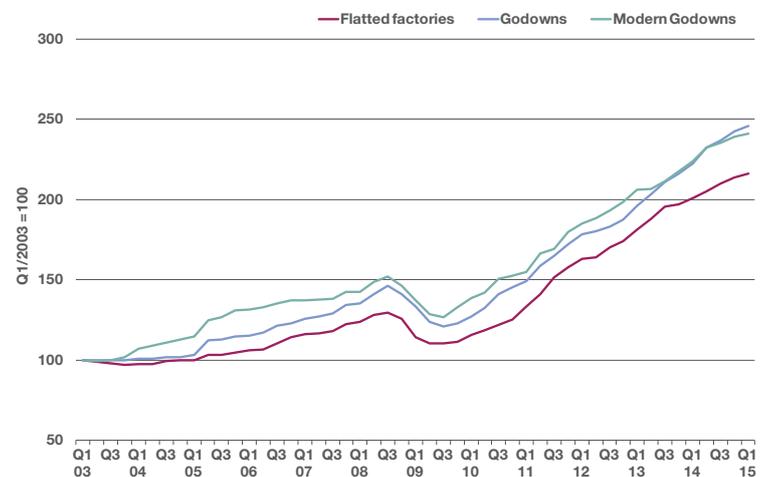
Source: Savills Research & Consultancy

GRAPH 1 **Major industrial transaction (>HK\$30 million) volumes and values, Q1/2007–Q1/2015**



Source: Savills Research & Consultancy

GRAPH 2 **Flatted factory and warehouse rental indices, Q/2003–Q1/2015**



Source: Savills Research & Consultancy

government taking a much tougher stance on handling illegal operations on these brownfield sites, which should be a welcome sign for both warehouse and one-storey shed landlords as these illegal yet low cost options are gradually being taken out of the game.

Outlook

With warehouse vacancy gradually rising, we expect to see more space being made available to the market in the next few quarters of 2015, mainly from modern warehouses in Kwai Chung/Tsing Yi, where almost all warehouses around the port areas are likely to release more space to the market over the next few months. In addition, there will also likely be a release of some single-owned, smaller warehouses in Tuen Mun and Yuen Long. With a few recently transacted industrial

buildings earmarked for revitalisation/ redevelopment also being made available for lease, we expect vacancy for both warehouses and flatted factories to rise in the near future, putting some pressure on rents.

Investment sentiment was somewhat dampened in the first quarter but this was due more to lack of quality stock for sale, and to some extent the increasing difficulty to secure financing in purchasing industrial properties (and commercial properties as well). With availability of stock likely to remain limited and the government not likely to loosen its control over credit in the near future, we expect transaction volumes to remain low, and buildings with redevelopment/revitalisation potential to continue to attract market attention. ■

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