Briefing
Industrial sector

November 2016

Image: Mapletree Business City II, Alexandra Terrace

SUMMARY

As economic and global uncertainties mount, prices and demand for industrial space continue to fall.

- The main drag on the economy is the manufacturing sector which fell 1.1% year-on-year (YoY) in the third quarter.
- The price for 30- and 60-year leasehold industrial units hit new record low prices at S$360.53 per sq ft and S$444.61 per sq ft respectively in Q3/2016. Freehold industrial development prices had the slightest fall of 1.4% quarter-on-quarter (QoQ) to S$679.59 per sq ft.
- Leasing activity in the industrial market slowed down 6.8% QoQ to a rental volume of 2,130 lettings in Q3/2016.
- The average prime monthly rent for the factory and warehouse sector slipped 6.3% QoQ to S$1.50 per sq ft in Q3/2016.
- According to JTC Corporation's rental index of industrial properties, the average monthly rent for business parks inched down 0.2% QoQ to S$4.07 in Q3/2016.
- For 2017, we expect rents for general industrial and warehouses to fall 5.0% YoY while Business Park space is expected to see rents rise 3.0% to 5.0% YoY.

"Unless global trade is reinvigorated and the new economy, like eCommerce, expands aggressively here, in the near term, the industrial and warehouse market appears to be running on empty." Alan Cheong, Savills Research

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Macro economy

According to the World Trade Organization (WTO), global GDP growth for 2016 is expected at 2.2%, with global trade down 1.7%. Despite the economic expansion of the US, which accounts for 9.5% of Singapore NODX, it is not resulting in as much trade as it used to. Furthermore, growth of exports to the US is not sufficient to make up for the drag coming from China, which accounts for about 15.0% of shipments. For the UK economy, even though the growth rate has picked up in the previous quarter, it is nevertheless likely to move along at a slower pace as the uncertainties associated with Brexit are expected to continuing weighing on investments and consumption. For the Eurozone, economy growth has also slowed down on the back of weakening consumer confidence in the region.

Based on the advanced estimates released by the Ministry of Trade and Industry (MTI), the Singapore economy expanded 0.6% YoY in Q3/2016. The main drag on the economy is the manufacturing sector, which plunged 1.1% YoY in the same quarter, as factory output of the transport engineering, biomedical manufacturing and general manufacturing clusters fell due to weak global demand.

The Economic Development Board (EDB) reported that Singapore's manufacturing output shrank 3.6% YoY in July, reversing four straight months of expansion. Local manufacturing output improved marginally by 0.1% YoY before posting a strong 6.7% YoY rebound in September. The recovery was mainly driven by the biomedical engineering (22.2% YoY) and electronics (15.9% YoY) industry clusters, offsetting the 18.9% YoY contraction in transport engineering. The upsurge in biomedical manufacturing output came from the expansion in the pharmaceuticals and medical technology segments as production of active pharmaceutical ingredients and biological products and medical instruments went up.

Although having edged up 0.5 of a percentage points (ppt) month-on-month (MoM) to 49.8 in August, the Singapore Purchasing Managers' Index (PMI) still remained in contraction mode (a reading below 50 indicates a contraction) for the 14th consecutive month. However, for the months of September and October, manufacturing output managed to expand, with the PMI moving 50.1 and 50.0 for each month, respectively. The expansion was attributable to a rise in new domestic and export orders, as well as improved rate of expansion of inventory and finished goods. Following a flat-line YoY performance in August, NODX contracted 4.8% YoY in September due to the drop in both electronic and non-electronic NODX.

Sales market

After a brief recovery in the previous quarter, transactions in the industrial property market dipped 15.8% QoQ in Q3/2016. With 317[1] caveats lodged for strata factories and warehouses, this is 12.3% lower than the 358 deals registered in Q3/2015.

According to the Urban Redevelopment Authority (URA), the total value of these transactions reached more than S$0.3 billion, just half of last quarter's value. The most frequently transacted project among the strata industrial developments was Pantech Business Hub where 14 units changed hands at an average unit price of S$443 per sq ft. In the second quarter, there was only one transaction from this development. This was followed by seven units in Trivex that transacted at an average unit price of S$630 per sq ft.

In line with the lower demand in the sales market, upper-storey factory and warehouse units in the Savills basket saw marginal price decline in the third quarter. 60-year leasehold industrial units in particular suffered from the largest price decline of 4.7% QoQ, which is greater than the highest depreciation recorded last year, at 3.2% QoQ in the first quarter. The price for 60-year leasehold industrial units averaged S$444.61 per sq ft, marking the lowest recorded price since 2013. 30-year leasehold industrial units also recorded a new record low price at S$360.53 per sq ft after a drop of 2.1% QoQ in Q3/2016. Given the limited supply of freehold industrial developments in Singapore, prices had the slightest fall of 1.4% QoQ to S$679.59 per sq ft, which is still higher than the average price transacted a year ago.

Leasing market

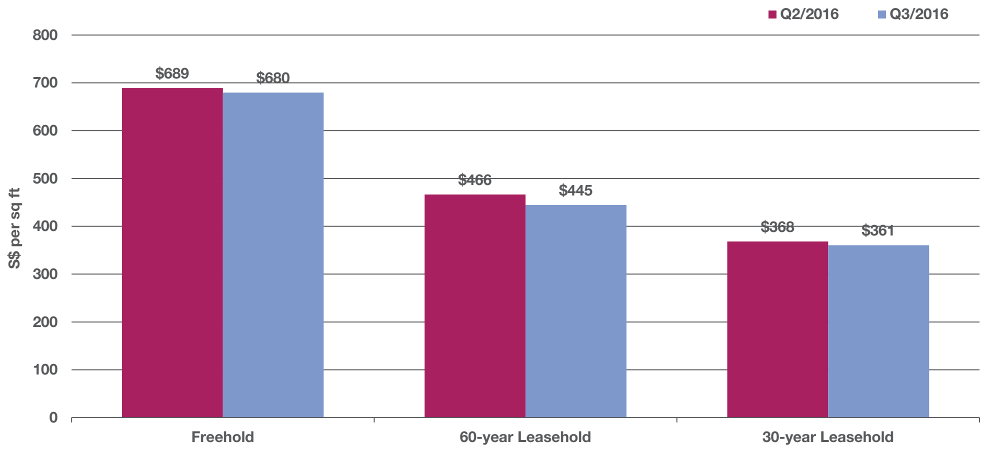
Following a QoQ rebound of 29.2% to 2,285 transactions in Q2/2016, leasing activity in the industrial market was down 6.8% QoQ to 2,130 in Q3/2016. The tepid market could be a result of the global economic slowdown. Nonetheless, it was still 4.9% YoY higher than the rental volume of 2,031 in Q3/2015.

As Singapore, a trade-oriented market economy, continues to be affected by the global economic slowdown, it remained a tenant's market in the third quarter. Especially with the plunge in oil prices, oil and gas industry players, who used to be able to afford high rents, are paring their cost and expenditure to the

1 Singapore Institute of Surveyors and Valuers REALink caveats as of 15 November 2016

GRAPH 1

Prices of upper-storey factory and warehouse units, Q2/2016 and Q3/2016



Source: Urban Redevelopment Authority (URA), Savills Research & Consultancy bare bones. As a result, the average prime monthly rent for the factory and warehouse sector[2] slipped 6.3% QoQ to S$1.50 per sq ft in Q3/2016, showing a full-year rental decline since Q4/2015.

In the same quarter, even the resilient high-tech property sector was affected. From Savills basket of high-tech buildings, the average monthly rent of high-tech spaces dipped 0.04% QoQ to S$2.75 per sq ft. The reason why the rent was not badly affected is that under more challenging business conditions, these tenants who could also take up office space, chose to move into more affordable accommodation. However, this may not be sustained if weakness in the economy persists. On a YoY basis, high-tech space rents in Q3/2016 fell 2.8%.

Business Parks

In Q3/2016, the number of leases signed for business park space eased 6.7% QoQ to 42 leases, versus the 45 leases done in the previous quarter.

The International Business Park (IBP) continued to lead in the third quarter, with 25 deals at an average monthly rent of S$4.27 per sq ft, up from S$4.17 per sq ft recorded in the second quarter. The improved rental rates could have been brought about by the sustained healthy demand and the government's measures in promoting the high-tech sector. However, the vacancy rate of IBP has worsened for two consecutive months this year, to 16.5% in Q3/2016.

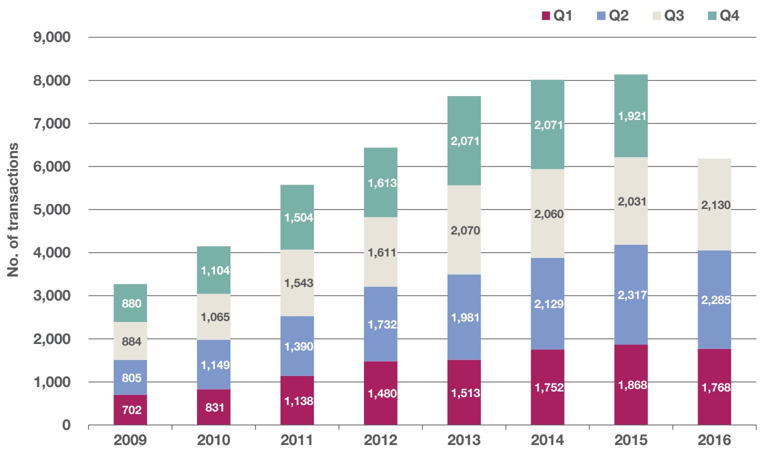
Likewise for Changi Business Park (CBP) and One-North, vacancy levels rose to 14.3% and 7.6% respectively even though there were slightly more deal closures in the third quarter. On the other hand, the vacancy rate of Queenstown improved to 32.1%. In total, the island-wide vacancy of business park space saw a marginal improvement of 0.53% QoQ to 18.9% in the reviewed quarter.

Although business park vacancy levels improved slightly after rising for four consecutive quarters, rents have hardly moved. According to JTC Corporation's rental index of industrial properties, the average monthly rent for business parks inched down 0.2% QoQ to S$4.07 in Q3/2016.

2 Prime rent for factory and warehouse units more than 10,000 sq ft on the ground floor.

GRAPH 2

Leasing volumes of factories and warehouses, 2009–Q3/2016



Source: URA, Savills Research & Consultancy

TABLE 1

Business park leasing volumes and values, Q3/2016

	No. of deals	Total value (S$)	Average value per transaction (S$)	Median rent (S$ per sq ft)
Technopark @ Chai Chee	1	4,898	4,898	3.10
Changi Business Park	6	60,585	10,098	3.80
International Business Park	25	400,894	16,036	4.27
Science Park 1	2	118,396	59,198	4.01
Science Park 2	3	78,100	26,033	4.08
Mapletree Business City	1	72,544	72,544	6.31
One-north	4	146,436	36,609	5.35

Source: URA, Savills Research & Consultancy

OUTLOOK

The prospects for the market

In the short term, the global economic outlook is expected to remain weak, owing to sluggish demand in major economies, slower growth in China, low oil prices and less active global trade flows. Britain's vote to leave the European Union and the United States presidential election have also added greater uncertainties to the outlook. For the second half of the year, lacklustre global growth continues to weigh on Singapore's small and open economy. Taking these factors into account, local economic growth is expected to slow in the last quarter of the year.

According to the Monetary Authority of Singapore (MAS) September 2016 Survey of Professional Forecasters, economic growth for 2016 is expected to be 1.8%, while the median YoY growth for the last quarter is forecasted to be 1.5%. As economic and global uncertainties linger, investor confidence tends to go down, and export driven economies like Singapore might even face a shift of economy into technical recession.

Although the niche segments of the market like warehouse space for eCommerce activities look promising, in the short term, it is expected that these cannot form a large enough bulwark to counter the strong cross-winds buffeting the traditional warehousing users. Bearing all this in mind, we believe that industrial and warehouse rents in 2017 may soften another 5.0% YoY island-wide. For business parks, given the dearth of supply in the coming years, we may see rents exhibit slight increases of about 3.0% to 5.0% YoY in 2017.

Period	YoY % change industrial and warehouse rents
Q4/2016F	-8.0%
Q4/2017F	-5.0%

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