Briefing
Industrial sector

February 2018

Image: Philips APAC Centre

SUMMARY

Robust growth in the manufacturing sector does not necessarily mean a demand recovery for industrial space but a recovery in the oil, gas and marine sectors may.

■ Industrial sales volume for 2017 rose 0.4% year-on-year (YoY) to 1,251 transactions, hence ending a five-year decline in sales volume since 2012.

■ Prices of freehold upper-storey and warehouse properties increased 2.5% YoY to S$681 per sq ft in Q4/2017.

■ Prices of 60- and 30-year leasehold upper-storey factory and warehouse units fell 1.9% YoY to S$445 per sq ft and 2.4% YoY to S$350 per sq ft respectively.

■ Despite the 18.8% quarter-on-quarter (QoQ) rise to 2,331 rental transactions in Q4/2017, the average prime monthly rent for factories and warehouses decreased by 4.2% QoQ to S$1.15 per sq ft.

■ Average monthly rent for business park space remained stagnant at S$4.05 per sq ft, while high-tech industrial space rose 0.3% QoQ to S$3.29 per sq ft in Q4/2017.

■ The nascent recovery in the oil, gas and marine industries may lead to a turnaround in rents sooner than expected and we believe that rents may begin to show signs of recovery by Q2/2018.

"The continued freefall in rents and prices may come to an end soon if oil prices maintain at current levels." Alan Cheong, Savills Research

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Macro economy

According to the advanced estimates released by the Ministry of Trade and Industry (MTI), the local economy expanded by 3.6% in 2017. The growth came mainly from the manufacturing sector which had demonstrated expansion, at various ranges, throughout the year, ranging from 4.8% YoY to 19.1% YoY. However, the rate of this expansion, particularly towards the end of the year, contributed to economic growth of 3.6% YoY in Q4/2017, moderating from the 5.5% growth in the preceding quarter. The turnaround in 2017 was largely due to the improving global demand for electronic products. Although the manufacturing sector growth showed signs of slowing down, due to a decline in output in the biomedical manufacturing and transport engineering clusters, it was primarily offset by the healthy level of output expansions in the electronics and precision engineering clusters.

Following the eight-year high reading of 52.6 in October, the Singapore Manufacturing Purchasing Manager's Index (PMI) in November increased further to 52.9 – the highest record since December 2009. This was attributed to a broad-based and faster rate of expansion in most key indicators, apart from the slowdown in supplier deliveries. The expansion in the employment index for the manufacturing sector was extended to December, marking the fourth straight month of expansion, further indicating that the manufacturing sector remained robust. Even though the rate of expansion in factory output and inventory eased in December to 52.8, PMI index levels still managed to record 16 months of consecutive expansion. This was driven by a slightly faster rate of expansion in new orders, new exports, and employment.

Recovering from the 1.1% YoY decline in September, non-oil domestic exports (NODX) recorded a significant expansion of 20.5% YoY in October due to the growth in both electronic (+4.5% YoY) and non-electronic exports (+28.5% YoY). The main contributor to the growth in non-electronic NODX was the exports of non-monetary gold which increased 591.5% YoY. Subsequently in November and December, the increase in NODX moderated to 9.1% and 3.1% YoY respectively because of a slowdown in expansion for non-electronic NODX in both months and a decline in electronic NODX in December. However, the slide in electronic NODX in December was partly due to a high base in December 2016 and also the strong Singapore currency which contributed to the lower trading volume.

According to International Enterprise (IE) Singapore, NODX grew about 8.8% YoY for the whole of 2017, marking the year with the strongest pace of expansion since 2010.

Sales market

Following a 24.7% YoY sales increase to 419 transactions in Q3/2017, the industrial sales volume inched up 3.9% YoY to 295[1] transactions in Q4/2017. This shows a 0.4% YoY rise to a total of 1,251 industrial sales transactions for the full year of 2017, hence ended a five-year decline in sales volume since 2012. According to the Urban Redevelopment Authority (URA), the total annual value of industrial sales transactions is S$4.2 billion in 2017, 84.2% above the sales value in 2016. However, this was mainly led by the few big-ticket land resale transactions in Q3/2017 and subsequently in Q4/2017, the total sales transacted was down by 45.2% YoY to S$535.0 million.

Even though the total sales transacted value in Q4/2017 was almost halved from last year, prices of freehold properties ended a full year decline and showed some growth in the last quarter. The prices of freehold upper-storey and warehouse properties in the Savills basket increased 2.5% YoY to S$681 per sq ft in Q4/2017. As the performance of manufacturing sector improves, the freehold properties are likely to be the first to see a price recovery due to the nature and rarity of freehold tenure.

On the other hand, prices of 60- and 30-year leasehold industrial properties continued its downtrend since Q2/2016. After a stagnant Q3/2017, prices of 60-year leasehold upper-storey factory and warehouse units in the Savills basket dropped 1.9% YoY to S$445 per sq ft in Q4/2017. From the Savills basket of 30-year leasehold upper-storey factory and warehouse units, prices fell 2.4% YoY to S$350 per sq ft, the lowest record since the basket was constituted in 2013.

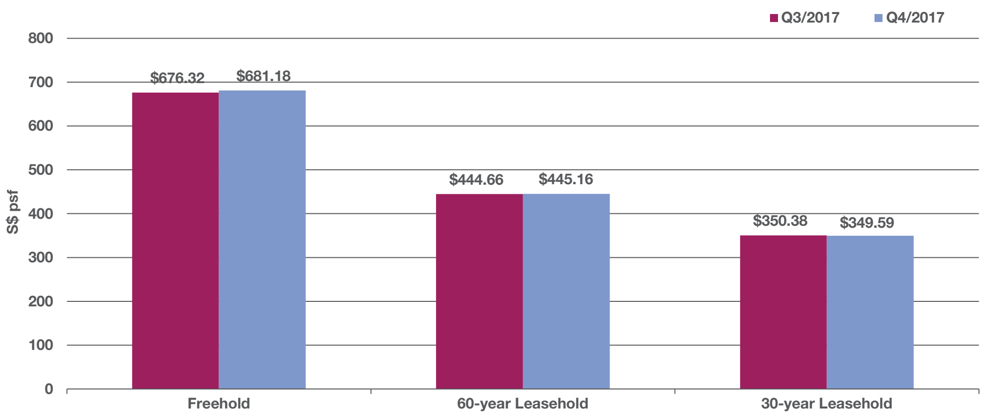
Leasing market

The industrial rental market saw its best performance in 2017, recording a total of 8,884 deals, 9.1% more than the previous high in 2016. On a quarterly basis, the market recorded 2,331 deals in Q4/2017, up 18.8% from the preceding quarter. The healthy rental market could possibly be due to the boost in manufacturing sector as the global demand and environment improves over the past few quarters. Moreover, many were still conservative as the external demand outlook for Singapore is expected to moderate

1 Singapore Institute of Surveyors and Valuers REALink caveats as of 5 February 2018.

GRAPH 1

Prices of upper-storey factory and warehouse units, Q3/2017–Q4/2017



Source: Urban Redevelopment Authority (URA), Savills Research & Consultancy in 2018, hence leasing tends to be a less risky option preferred by most industrialists. Besides, the annual new supply of 10,500 sq ft of factory spaces and 10,400 sq ft of warehouse spaces could also contributed to the rise in leases.

In Q4/2017, the vacancy rate for factory space remained unchanged at 11.0% as there was 3.1 million sq ft of net new demand to the 3.5 million sq ft of net new supply. On the other hand, the vacancy level for warehouse space slipped 1.6 percentage points (ppts) QoQ from the highest recorded at 12.5% to 10.9% in Q4/2017. This was a result of a healthy net take-up of 3.7 million sq ft, particularly in West and North Planning Regions. The uptick in occupancy rate could be due to the rise of logistics services driven by the digital economy and possibly from the recovering oil and gas and their related industries.

However, the rental market remained weak as the industrialists were still cautious over the sustainability of the recovery of the manufacturing sector. According to JTC, both industrial sites launched on 28 November 2017 were not awarded because each only attracted one bid that was below reserve price. The average prime monthly rent for factory and warehouse in the Savills basket decreased for the ninth straight quarters by 4.2% QoQ to S$1.15 per sq ft.

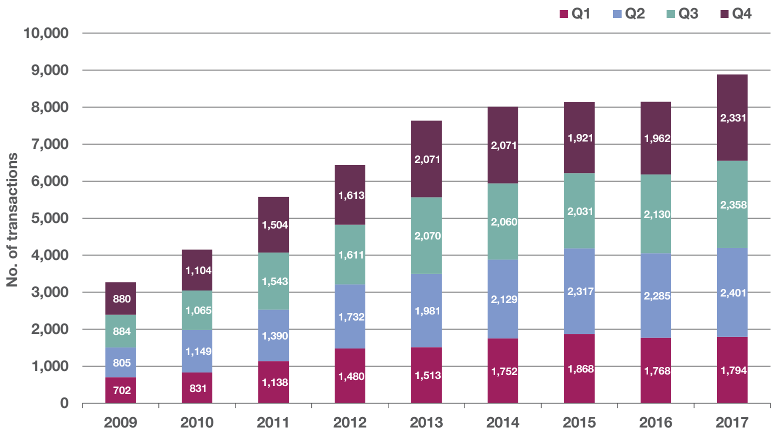
Notwithstanding the 15.7% QoQ decrease in number of leases to 75 deals, there was a 250.0% QoQ rise in net demand for business park space to 151,000 sq ft in Q4/2017. Even though the net demand is far below the average demand of 444,000 sq ft in 2016, it has brought the vacancy rate down by 0.7% QoQ to 14.1%, the lowest vacancy level since 2009. This is mainly because of a limited new supply of business park space.

The rise in occupancy rate did not translate to higher rents. While Changi Business Park (CBP) saw the highest increase in occupancy rate by 1.03 ppts QoQ, its monthly median rent remained at S$3.85 per sq ft in the reviewed quarter. This could imply that the rental market for business park space has yet to shift in landlords' favour. The 3.5% QoQ increase in the monthly median rent reported by URA to S$4.09 per sq ft could be due to the higher rents achieved by newer developments such as Mapletree Business City (MBC), which command a rent premium. As such, the monthly average rent for business park space in Q4/2017 remained stagnant at S$4.05 per sq ft.

As the global manufacturing sector is undergoing another major transformation, to stay competitive and relevant, the government has been supporting the development of advanced manufacturing technologies in Singapore. As a result of the shift, demand is shifting from the conventional industrial spaces to high-tech spaces. In Q4/2017, the monthly prime rents of high-tech industrial space grew 0.3% QoQ to S$3.29 per sq ft.

GRAPH 2

Leasing volumes of factories and warehouses, 2006–2017



Source: URA, Savills Research & Consultancy

TABLE 1

Business parks and high-tech spaces

	No. of deals	Total value (S$)	Average value per transaction (S$)	Median rent (S$ per sq ft)
Technopark @ Chai Chee	6	169,663	27,277	3.02
Changi Business Park	12	127,242	10,604	3.85
International Business Park	30	255,802	17,427	4.27
Science Park I	9	125,234	13,915	4.40
Science Park II	9	202,688	22,521	4.00
One-North	6	436,666	72,778	5.75
Mapletree Business City	3	349,363	116,454	6.00

Source: URA, Savills Research & Consultancy

OUTLOOK

The prospects for the market

According to the World Bank's January 2018 Global Economic Prospects report, the global economy is forecast to grow by 3.1% in 2018, up from the 3.0% last year. After a robust economic growth in 2017, MTI expects the pace of economic expansion to moderate and grow slightly above the mid of the range of 1.5% to 3.5% in 2018. This will largely be driven by the manufacturing sector which is likely to sustain its growth as the electronics and precision engineering clusters continue to benefit from the healthy global demand for semiconductors and semiconductor equipment.

Even though the economic outlook may look bright with sustainable growth in the manufacturing sector, industrialists in general are still cautious about taking up new space. With the upcoming supply of 17.4 million sq ft of factory and warehouse spaces, it is unlikely to see a significant uptick in the sales and rental market. As office rents are expected to appreciate, business park and high-tech spaces may instead be a preferred option for businesses to consider for relocation. However, the room for overall rental growth is limited by the high vacancies and lower asking rents of the older buildings. The rental market for business parks and high-tech spaces would probably stay flat unless office rents escalate enough to force tenants to relocate.

There are positive signs that locally based oil and gas operators and their related companies are beginning to reinvest. However, at this early stage of recovery, they are not in the position to take up more space due to aggressive expansion prior to the oil price collapse in June 2014. Therefore, although we may still see business activity from this sector increasing rapidly (because of the low base), these companies may instead try to monetise off their industrial and/or warehousing space to free up capital for buying operating assets which are still selling at distressed levels.

Moving forward, the actions of the entrepreneurs in the oil, gas and marine industries will dictate whether we will see industrial rents and prices of industrial and warehousing space turn the corner. Although electronics and pharmaceutical industries have been expanding strongly in 2017, its impact on the lay and on the general industrial and warehousing space market is hardly felt. However, a turnaround in the oil, gas and marine industries, with its web of linkages to supporting industries, particularly the small and medium size business sectors, will no doubt have greater multiplier effects on the spatial market. We believe that the fortune of the oil, gas and marine industries has turned, yet because it is at an early stage of recovery, it may still not have an immediate effect of stabilizing rents and prices. However, if the recovery continues, positive signs may also be reflected in rents and prices by Q2/2018.

Period	QoQ % change industrial factory and warehouse rents
Q1/2018F	-0.5%
Q2/2018F	0% to 0.5%

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