

Industrial Sales and Leasing



Warehouse rents holding up well for now

Industrial sales sentiment was subdued by external uncertainties and deal volumes declined significantly as a result.

- The sales market saw deal volumes declining due to external uncertainties, while major transactions were scarce.
 - Very few leasing transactions were concluded with many tenants adopting a cautious attitude given a worsening trading and retail performance over the first few months of the year.
 - With vacancy remaining tight (1.9% overall and 0.8% for modern warehouses), warehouse landlords were able to maintain their tough stance in negotiations, leading to further rental increases over Q2/2019.
 - The 20% plot ratio relaxation for industrial redevelopment proved to be an instant hit with at least 10 applications since the inception of the policy in October 2018, three of which have already been approved with a maximum plot ratio relaxation, showing Government's intention to encourage such redevelopment.
 - Investment sentiment is expected to remain cautious with the ongoing trade situation and the volatile stock market, and volumes are expected to remain low while prices may hold up for another few months.
- The weakening air and sea cargo throughputs put many logistics businesses under pressure, and though no large-scale contraction has yet to occur, the future for 3PLs looks less than promising if demand continues to shrink.

“The impact of the US / China trade tensions has translated into declining cargo throughput and retail sales, as well as fewer industrial sales and leasing transactions over Q2/2019, with prices and rents remaining intact for the moment.”

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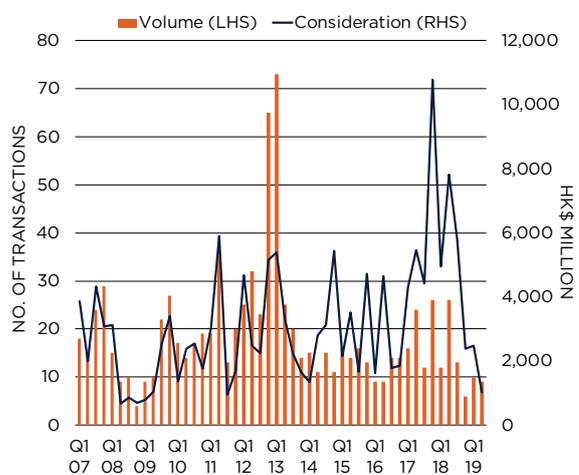
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GRAPH 1: Major Industrial Transactions Over HK\$30 Million, Q1/2007 to Q2/2019



Source Savills Research & Consultancy

TABLE 1: Industrial Price Growth By Subsector, Q2/2019

	Q2/2019 (%)	Q1/2019 (%)	2018 (%)	2017 (%)	2016 (%)
Flatted factories	+1.7	+1.1	+7.0	+10.8	+4.1
I/O	+1.3	+1.1	+7.4	+10.5	+3.4
Warehouse	+0.6	+1.5	+9.2	+16.9	-1.2

Source Savills Research & Consultancy

SALES MARKET

Investment sentiment quickly turned sour after the ongoing trade dispute between the US and China, which translated into a volatile stock market with the HSI plummeting from over 30,100 in early April to 26,700 in early June (an 11% drop), before rebounding to 28,200 (+5%) in the last week of June given some conciliatory rhetoric from the US and China during the G20 Osaka Summit as well as the US Fed’s indication of another round of rate cuts.

No en-bloc industrial transactions were recorded over Q2/2019, with only three transactions of over HK\$100 million. The sale of 45 workshops and 18 carparks in EW International Tower for HK\$306.8 million was for stratification by the new owner Wang On, while the new godown / workshop project at 22 Wing Kin Road in Kwai Chung, which was still under construction, saw two units on the first floor pre-sold to Hong Kong Interbank Clearing Limited for owner occupation.

Industrial transaction values and volumes both declined when compared with the previous quarter by 10% and 59% respectively, hitting a recent low for the total consideration at only HK\$1 billion. Despite this, industrial prices rose marginally by 1.7% while warehouse prices remained flat over Q2/2019 as a result.

LEASING MARKET

The trade conflict, which saw a 3.2% drop in total imports and exports from Jan to May 2019 as well as a 1.8% decline in retail sales over the same period, have translated into a decline in cargo throughputs, with air and container throughputs falling by 6.0% and 7.7% over the first five months of the year respectively. This was the worst start to a year since 2016, when the US Fed started raising rates.

While most logistics operators were still working on billings incurred in the first two quarters with their businesses remaining active, many are of the view that business prospects in the second half of the year will dim dramatically if a resolution to the trade war cannot be reached by then. With such a cautious attitude, leasing transactions were hard to come by with many tenants adopting a wait-and-see attitude, inducing most of them to renew their leases rather than relocating or expanding.

With no large-scale surrenders or shrinkages of businesses just yet, vacancy remained extremely low (1.9% overall and 0.8% for modern warehouses), and warehouse landlords were able to maintain their tough stance in rental negotiations, leading to further increases in rents over Q2/2019. Overall and modern warehouse rents increased further by 1.5% and 2.8% in Q2/2019 respectively as a result.

The cold storage segment of the market saw the leases of two of Hong Kong’s largest cold stores, namely Brilliant Cold Storage I & II, expire in the first half of 2019. While the former renewed its lease for another eight years for an undisclosed rent, the latter saw a newly formed cold storage operator taking up the space with a potential 10-year lease (3 years initially with an option to renew for seven more years). These two moves are further proof of the long-term demand and lack of choice for food processing and storage space in temperature-controlled environments.

20% GFA CONCESSION FOR INDUSTRIAL REDEVELOPMENT POPULAR

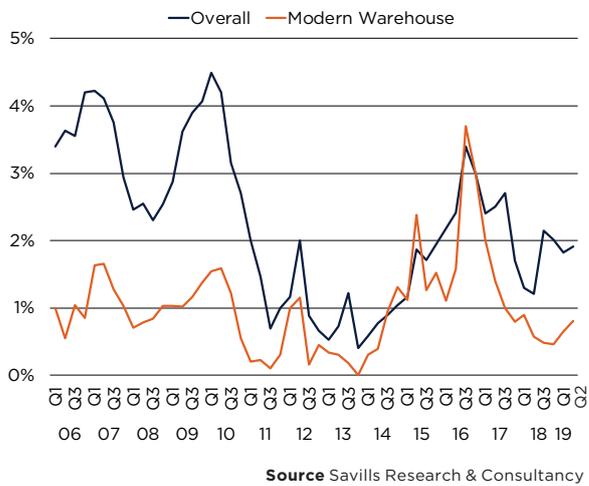
The 20% plot ratio relaxation for industrial redevelopment proved to be an instant hit with at least 10 applications since the inception of the policy in October 2018,

TABLE 2: Major Industrial Transactions Over HK\$100 Million, Q2/2019

DISTRICT	LOCATION	FLOOR	TOTAL GFA (SQ FT GROSS)	CONSIDERATION (HK\$)	AVERAGE PRICE (HK\$ PER SQ FT)	DATE	SELLER	PURCHASER	TYPE	REMARKS
Tsuen Wan	EW International Tower, 120-124 Texaco Road	45 workshops and 18 car parking spaces	90,700	\$306,800,000	\$3,383	Apr 2019	First Trading Co. Ltd	Wang On	I	For stratification
Kwai Chung	22 Wing Kin Road	Units 1A & 1B	29,341	\$193,651,000	\$6,600	Apr 2019	Billion Development	Hong Kong Interbank Clearing Ltd.	I	Owner occupation
Hung Hom	Gemstar Tower, 23 Man Lok Street	Units E & F, 13/F	TBC	\$112,266,000	TBC	Apr 2019	ISA Property Investments Ltd	Maruya (HK) Ltd	I	Investment

Source Savills Research & Consultancy

GRAPH 2: Warehouse Vacancy Rates, Q1/2006 to Q2/2019



three of which have already been approved with a maximum plot ratio relaxation, showing Government’s intention to encourage such redevelopment.

OUTLOOK

Investment sentiment is expected to remain cautious with the ongoing trade conflict and volatile stock market, and volumes are expected to remain low while prices may hold up for another few months. Though there are new hopes of a possible US / China trade agreement after the conclusion of the G20 Osaka Summit, there are guaranteed to be more twists and turns before any meaningful resolution is reached, so we believe investment sentiment as well as business prospects will remain clouded over the next few months.

The weakening air and sea cargo throughputs have put many logistics businesses under pressure, and though a large-scale contraction has yet to occur, the future for 3PLs looks less than promising if demand continues to shrink. Nevertheless, with vacancy remaining tight and new supply hard to come by, warehouse rents may hold up for another three to six months given no worsening of the external environment, while the longer-term prospects of the logistics sector will depend on any ultimate rapprochement between the US and China.

TABLE 3: Industrial Rental Growth By Subsector, Q2/2019

	Q2/2019 (%)	Q1/2019 (%)	2018 (%)	2017 (%)	2016 (%)
Flatted factories	+0.2	+1.0	+7.9	+7.0	-3.9
I/O	+0.8	+2.1	+3.9	+2.9	-0.3
Warehouse	+1.5	+1.6	+8.3	+0.1	-0.6
Modern warehouse	+2.8	+2.6	+10.2	-4.2	-1.8

Source Savills Research & Consultancy

TABLE 4: Approved Applications For Additional Plot Ratio For Industrial Redevelopment

ADDRESS	BUILDING TYPE	ZONING	SITE AREA (SQ FT)	CURRENT PLOT RATIO	NEW PLOT RATIO	TOTAL GFA (SQ FT)	STATUS
13 Hok Yuen Street, Hung Hom	Commercial building	Other Specified Uses (Business)	39,813	12.0x	12.78x	508,889	Approved with conditions on 17th May 2019
1 Tsat Po Street, San Po Kong	Industrial building	Other Specified Uses (Business)	14,920	12.0x	14.4x	214,846	Approved with conditions on 12th April 2019
350 Kwun Tong Road, Kwun Tong	Commercial building	Other Specified Uses (Business)	19,181	12.0x	14.4x	276,180	Approved with conditions on 22nd March 2019

Source Lands Department