Colliers Quarterly

SINGAPORE | INDUSTRIAL

Q1 2017

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Accelerating success.

In a transitional phase

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Since Q4 2016, most manufacturing indicators have improved, despite an uneven performance across the clusters. We expect this positive performance to continue and thus leasing activities should pick up in coming quarters. We forecast overall rents to recover marginally, driven by independent hi-specification buildings, by end of 2017. We expect the strata sales market to be subdued with no known new launches planned in 2017.

Forecast at a glance

Demand

We foresee a pickup in leasing activities as tenants at the sidelines enter the market to lock in their rents in 2017.

Supply

As of Q1 2017, JTC estimated over 21.5 million sq ft GFA of new industrial space is expected to complete by end of 2017.

Vacancy rate

JTC All-industrial vacancy as of Q1 2017: 10.6% (+0.1ppt QOQ)

We expect islandwide vacancy to increase marginally in 2017

Rent

We predict overall rents to recover 1-2% YOY by end of 2017

Price (strata-titled capital values)

Capital values for prime freehold industrial space are likely to be stable in 2017

Increased enquiries

With the global economic outlook taking a positive turn, most manufacturing indicators in Singapore have seen growth since late 2016. The latest monthly manufacturing performance for March 2017, released by Economic Development Board (EDB) saw output swell by 10.2%YOY, driven mainly by the electronics segment.

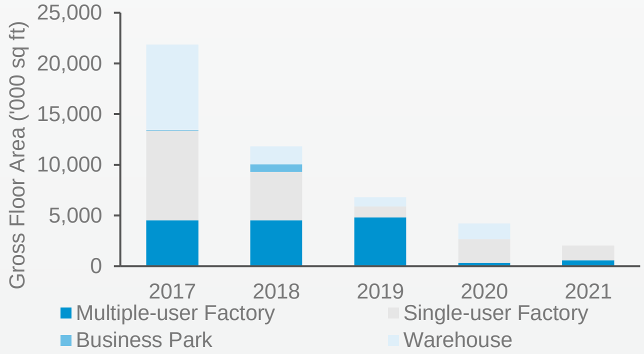
In Q1, leasing activities saw an extended quarterly decline, possibly due to the seasonal festive season in early 2017. Since April, Colliers has seen increased enquiries where potential occupiers are gradually entering the market or taking the opportunity to negotiate and finalise their lease arrangements. Hence, we expect leasing activities to improve in the coming quarters and leasing transactions to be in the range of 8,300 to 8,500 (or up to c.2% YOY growth) for the year of 2017.

Based on our estimates, industrial rents across most segments saw slight increases in Q1, while some segments stayed flat. We believe that the market could possibly be at an inflexion point and we expect clearer signs in coming quarters.

We project overall industrial rents to recover marginally towards the end of 2017, led by independent hi-specification industrial buildings.

For the strata-titled industrial sales segment, we expect the total number of caveats lodged for 2017 to be between 800 and 900. This takes into consideration that no new developer launches is expected for 2017, and cost-sensitive occupiers could turn to leasing, instead of buying, due to potential interest rate hikes.

Upcoming Industrial Supply by Types



Source: JTC

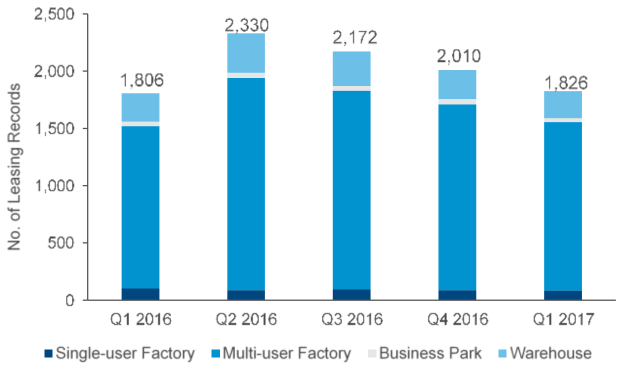
Leasing market and rental values

Leasing transactions fell for three consecutive quarters

As of 18 April 2017, a total of 1,826 leasing records were recorded in Q1 2017 by Urban Redevelopment Authority's Real Estate Information System (URA REALIS). This is a 9.2% QOQ decline from Q4 2016's 2,010 records, possibly due to the seasonal effect of festivities in the first quarter.

On an annual basis, rental transactions improved marginally by 1.1% for Q1 2017. The slight increase could be due to the better sentiment in the macroeconomic conditions, as compared to early 2016.

Breakdown of Leasing Records by Types



Source: Colliers International Singapore Research, URA REALIS (as at 18 April 2017)

While tenants adopted a "wait and see" approach in 2016, given the uncertainty of the global economy, and the results of the Brexit vote and US Presidential Election, this situation has changed in early 2017. In view of the recent strong performance from most of the manufacturing indicators, some industrialists are now entering the market gradually to negotiate and finalise their lease arrangements, as evidenced by more leasing enquiries. This is especially so for some large-scale companies which are considering future expansion while ensuring that they still comply with the JTC subletting guidelines by end 2017.

We advise tenants to take this opportunity of a still-favourable rental market to secure larger, newer or higher-specification space, or to negotiate more favourable terms to remain at their existing premises.

Therefore, we predict leasing transactions to be in the range of 8,300 to 8,500 (or up to 2.2% YOY growth) for FY2017.

Strong macroeconomic indicators

According to the advance estimates released by Ministry of Trade and Industry (MTI), Q1 2017 GDP for manufacturing goods producing industries contracted 6.6% QOQ (seasonally adjusted annualised SAA), after a very strong 39.8% QOQ growth in Q4 2016.

Nonetheless, manufacturing output increased 10.2% YOY, +5% QOQ SAA in March 2017, driven by electronics and precision engineering, partially offset by weak general manufacturing and marine and offshore engineering clusters. Singapore's non-oil domestic exports (NODX) grew for the fourth consecutive month in March 2017, and grew a 16.5% YOY, driven by both electronics and non-electronic exports.

In addition, the Singapore Purchasing Managers' Index (PMI)[1] – a barometer of the health of the manufacturing sector – has crossed the 50-point threshold for seven consecutive months, indicating expansion in manufacturing activities. Higher new orders and new exports led to March's PMI to expand at a quicker pace to reach 51.2.

Mixed rental performance in Q1

Based on Colliers International research, in Q1 2017, rents improved marginally for all industrial segments, except for prime warehouse (upper floors), independent high-specification (ground floors) and business parks which saw rents stay flat.

According to Colliers International research, the average monthly gross rents for ground and upper-level prime conventional factory premises grew by 3.2% QOQ and 1.1% QOQ to SGD 2.56 (USD1.83) per sq ft and SGD1.84 (USD1.31) per sq ft, respectively. These are slower than the 6.9% QOQ and 2.2% QOQ growth respectively in Q4 2016. Take-up has remained relatively strong from small-medium enterprises (SMEs) who prefer prime locations for their operations.

The average monthly gross rents for the ground level of prime conventional warehouse space remained unchanged, while those for upper levels grew a marginal 0.7% QOQ in Q1 2017.

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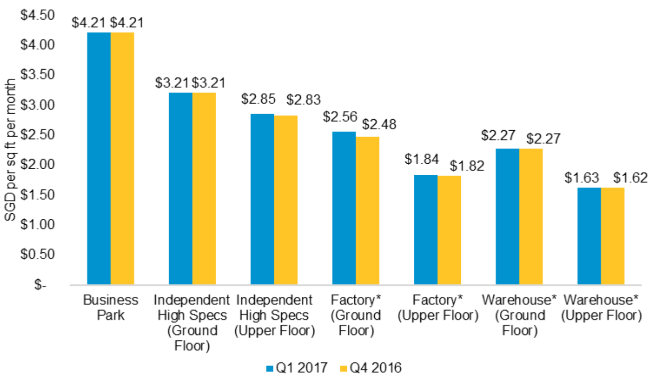
1 *A PMI reading of above 50 indicates that the manufacturing sector is expanding while a PMI reading of less than 50 indicates that the manufacturing sector is declining.*

In Q1, independent high-specification industrial space located outside science parks and business parks saw a slight recovery in upper floor rents of 0.7% QOQ. We observed that some business owners have leveraged on the cheaper rents at industrial spaces to set up childcare centres, gyms, cafes etc to cater to end-users, by applying for a temporary change of use. We also envisage higher demand for high-specification space situated near to the soon-to-be completed Downtown Line 3. As such, we predict rentals to recover gradually by up to 5% by end of 2017.

Based on Colliers International's research, business park rents remained unchanged at an average monthly gross rent of SGD4.21 (USD3.01) per sq ft in Q1 2017. Some leases were renewed, while some new tenants took up pockets of vacant space within business parks. Meanwhile, some tenants may be considering expanding their operations within the business parks. However, older developments could continue to see relatively higher vacancies. According to JTC Q1 2017 statistics, business park occupancy improved 1ppt QOQ to 84.0%. We expect business park rents to be stable for 2017.

Average Monthly Gross Rents of Prime Industrial Space (Q1 2017 vs Q4 2016)



* This refers to prime conventional factory or warehouse space.
Source: Colliers International Singapore Research

Catering to the growing needs of start-ups

With the government's drive to grow and tap on advanced technologies such as artificial intelligence and digital displays, we expect more Research and Development (R&D) activities, which increase demand for high-specification and business park space.

Singapore in recent years has been seen as one of the world's leading centres of tech entrepreneurship, with its extensive initiatives and support from the government. One of the many initiatives is the JTC LaunchPad@one-north which supplies industrial spaces to start-ups and incubators.

Private landlords could explore having start-up incubators with qualifying trades to be in their buildings. This will allow potential collaborative efforts by tapping on ready resources such as nearby tertiary institutions or within the ecosystem of business parks. We are likely to see developers or landlords providing similar spaces for start-ups. For instance, the upcoming business development in Media Circle developed by Boustead Projects will need to cater spaces for start-up graduates[2] from LaunchPad.

Alternatively, some landlords could also consider serviced offices tenants who provide serviced offices for industrial users in their premises. These could cater to individuals or small companies who occupy some industrial space and require a small office within the building to conduct simple office duties. For instance, Lock+Store and Work+Store Space are two companies that offer storage space and serviced office units to clients who need small and affordable work space to conduct administrative matters, while storing their goods within the same unit or building. This will be most suitable for individuals or small companies in the fields of e-commerce and e-retail.

Strata sales and capital values

Strata sales volume declined for three consecutive quarters

A total of 133 caveats were lodged for Q1 2017, based on preliminary records from URA Realis as of 18 April 2017. This represents a decline of 26.5% QOQ and 26.9% YOY. It is also the third consecutive quarter of decline for the strata sales market.

Potential buyers who are mostly end-users could still be evaluating their options to rent or acquire a unit for their business operations, in anticipation of future interest rate hikes that could increase their operating costs. The lack of new launches might have also contributed to the decline.

In comparison to Q4 2016, more enquiries were received from end-users for strata-titled industrial units in Q1 2017. These occupiers tend to have a higher budget,

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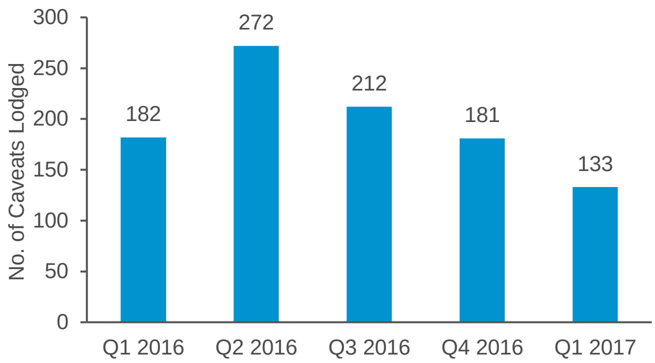
[2] Start-ups graduates are companies residing in LaunchPad and have incorporated for five years or more. The companies will need to vacate from LaunchPad by looking for other suitable spaces to continue their businesses.

especially with initial cash outlays. By owning operating premises, they will be able to minimise operational uncertainties such as future rental hikes or being asked to vacate in the future.

Number of caveats lodged for strata-titled industrial units



Source: Colliers International Singapore Research, URA REALIS (as at 18 April 2017)

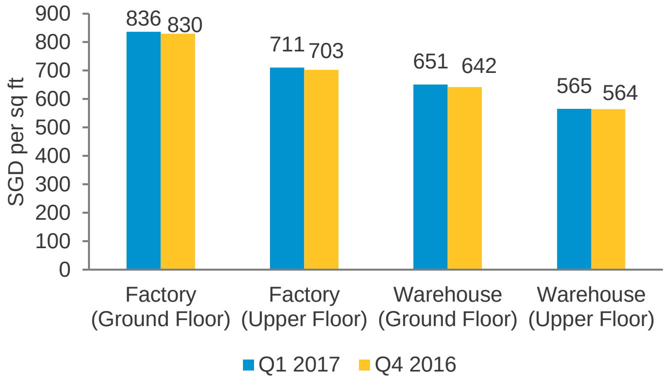
Meanwhile, some developers with unsold units are adopting aggressive marketing tactics such as giving out furnishing vouchers, absorption of legal costs or providing flexible payment options to entice potential purchasers. Unlike some developments which adopted a "lease-then-buy" schemes, a few developers prefer to sell their remaining units on a vacant possession basis.

In 2017, the strata sales market will continue to be favourable to the buyers, given that as of Q1 2017, there were 1,432 unsold units (or 73% of total uncompleted stock for uncompleted strata-titled industrial developments. Additionally, no known new developer launches are foreseen for the year. Hence, we envisage the strata sales market to remain subdued and that total number of registered caveats to hover between 800 and 900 for the year of 2017.

Capital values for prime freehold industrial space to remain stable

Based on Colliers International research, the overall average prices of prime freehold factory units recovered by 0.7% QOQ and 1.1% QOQ for ground floor and upper floor units, respectively. This is the first increase after four consecutive quarters of decline. Likewise, average capital value for prime freehold warehouse units also picked up by 1.4% QOQ and 0.2% QOQ for ground floor and upper floor units, respectively. The rise could be due to the limited freehold industrial space that is available, and in tandem with the improved rents.

Average Capital Values of Prime Freehold Industrial Space (Q1 2017 vs Q4 2016)



Source: Colliers International Singapore Research

Given that most SMEs have shorter business cycles in today's market, cost management is vital to their businesses. Therefore, occupiers who prefer their own premises could consider acquiring units of a leasehold tenure as a cheaper alternative.

We expect capital values for prime freehold industrial space to remain stable in 2017, since, while there is abundant new supply ahead, most will be on much shorter leases.

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