

# INDUSTRIAL DEMAND NOT AFFECTED BY HONG KONG'S EXTERNAL TRADE DECELERATION

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## Summary & Recommendations

Despite the deceleration of external trade figures, demand for industrial space in Hong Kong remained strong. Both rents and prices of warehouses and factories recorded an increase in Q4 2018.

Hong Kong's external trade started to slow since first recording a decrease in exports of 1.0% yoy in November. In addition, the Nikkei Hong Kong PMI remained at 48.0, below the 50 point line separating expansion from contraction and suggesting Hong Kong will see slower growth in 2019.

We expect the industrial market to benefit from the revitalisation scheme and a lack of new industrial supply. Investors should consider investment in industrial properties and their revitalisation potential into non-industrial use.

	Q4 2018	Full Year 2019	2018-23 Annual Average
 <b>Demand</b> <ul style="list-style-type: none"> <li>&gt; We expect increases in the demand for industrial space, thanks to the significant growth of e-commerce and the upcoming revitalisation scheme.</li> </ul>	 <b>HKD3.7 bn</b>	 <b>HKD37.5 bn</b>	 <b>HKD30.0 bn</b>
 <b>Supply</b> <ul style="list-style-type: none"> <li>&gt; The revitalisation scheme should further reduce existing stock while the new supply of industrial spaces remains tight.</li> </ul>	 <b>391,000 sq ft</b>	 <b>856,000 sq ft</b>	 <b>500,000 sq ft</b>
	<b>QOQ / End Q4</b>	<b>YOY / End 2019</b>	<b>Annual Average Growth 2018-23 / End 2023</b>
 <b>Rent</b> <ul style="list-style-type: none"> <li>&gt; The growth of e-commerce and online to offline (O2O) strategies by retailers have led to increasing demand for warehouse space. Rents have continued to increase steadily.</li> </ul>	 <b>1.3%</b> <b>HKD13.1 psf</b>	 <b>5.4%</b> <b>HKD13.8 psf</b>	 <b>4.5%</b> <b>HKD16.3 psf</b>
 <b>Vacancy</b> <ul style="list-style-type: none"> <li>&gt; The vacancy rate of industrial properties should continue to decrease due to tight new supply of industrial spaces as well as implementation of the revitalisation scheme.</li> </ul>	 <b>-</b> <b>5.7%</b>	 <b>-0.7pp</b> <b>5.0%</b>	 <b>-0.2pp</b> <b>4.5%</b>
 <b>Capital Values</b> <ul style="list-style-type: none"> <li>&gt; The Hong Kong Policy Address in October 2018 reaffirmed the implementation of a new round of revitalisation. We expect the scheme will drive the industrial investment demand.</li> </ul>	 <b>1.6%</b> <b>HKD4,842 psf</b>	 <b>8.4%</b> <b>HKD5,249 psf</b>	 <b>6.6%</b> <b>HKD6,651 psf</b>

Source: Colliers International  
Note: USD1 to RMB6.61 as of end-Q2. 1 sq m = 10.76 sq ft

## TRADE FIGURES RECORDED A DECELERATION

Starting from early December, the U.S-China trade war was temporarily suspended for 90 days to allow for talks at a post-G20 summit meeting in Argentina. This has the effect of delaying a planned 1 January increase in a tariff increase from 10% to 25% on USD200 billion of Chinese goods. As the trade conflict between the U.S. and China is still unresolved, the growth of Hong Kong external trade started to slow down in Q4. The combined value in October and November of total exports slowed to 6.5% yoy, compared to a growth in Q3 of 8.4% yoy. Moreover, in November the total value of exports recorded its first decrease of 1.0% on year-on-year basis since 2017.

On the other hand, according to IHS Markit, the Nikkei Hong Kong PMI in December increased by 0.1 to 48.0, showing tentative signs of improvement but remaining below 50 points for the ninth consecutive month. This highlighted a decline in new orders, particularly from China, negative business confidence as well as the acceleration of inflationary pressures.

## LEASING MOMENTUM REMAINED

Despite disappointing external trade figures in Q4, industrial leasing remained strong. Leasing demand continued to be dominated by relocation and expansion. The growth of e-commerce and increase in sales of FMCGs has led to increasing demand for industrial space.

In Q4, warehouse and factory rents increased by 1.3% qoq and 1.5% qoq, respectively. Comparing 2017 and 2018 as a whole, warehouse and factory rents increased by 7.4% yoy and 8.9% yoy respectively.

Notable deals included Bollore Logistics' lease of three floors (71,200 sq feet or 6,600 sq metres) at Tai Hing Industrial Building in Tuen Mun and JSI Logistics' lease of 28,536 sq feet (2,700 sq metres) at Watson Centre in Kwai Chung.<sup>1</sup>

In addition, the supply of industrial spaces remained low. Both ATL Logistics Centre (ATL) in Kwai Chung and Hutchison Logistics Centre (HLC) in Kwai Chung recorded full occupancy for the first time. Previously, we expected that HLC and ATL would have vacant space until mid-2019 and 2020 respectively.

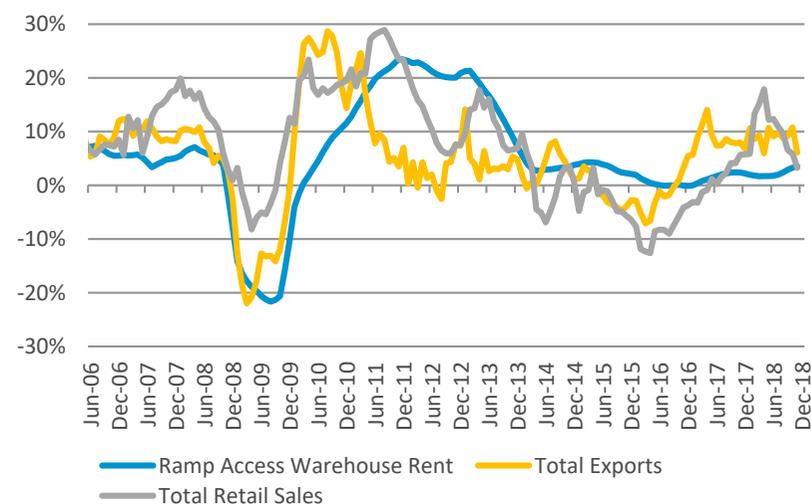
<sup>1</sup> EPRC

### Major industrial market indicators

Major industrial market indicators	Q4 2018	2018
Total Exports (Oct – Nov)	6.5% YOY	8.7% YOY
Port Container Throughput	-4.2% YOY	-5.5% YOY
Air Cargo Throughput	-1.6% YOY	1.4% YOY
Warehouse Rents	1.3% QOQ	7.4% YOY
Factory Rents	1.5% QOQ	8.9% YOY

Source: Census and Statistics Department, Colliers International

### Hong Kong warehouse rents



Note: Exports as three-month moving average

Source: Census and Statistics Department, Colliers International

## INVESTMENT: Q4 THE QUIETEST QUARTER IN 2018

On 10 October, Carrie Lam, the Chief Executive of Hong Kong, gave her second Policy Address and reaffirmed a second revitalisation scheme, allowing landlords to convert industrial use to commercial use. This has been pushing investors to continue searching for suitable industrial buildings to undergo wholesale conversion.

In Q4 2018, industrial property investment was quiet with few en-bloc transactions. The total value of strata title and en bloc transactions (with deal sizes over HKD30 million) dropped by 14% qoq and 82% qoq respectively. Compared to 2017 as a whole, the total value of strata- title and en-bloc transactions in 2018 increased by 63% yoy and 20% yoy respectively, thanks to the hot investment market in H1 2018.

Notable deals in Q4 include the Factory A on ground floor of Mai Gar Industrial Building being sold to King Opal Ltd. for HKD108 million (USD13.8 million). Based on the GFA of 7,205 sq feet (670 sq metres), the average price was HKD14,990 (USD1,900) per sq feet.<sup>1</sup>

## CAUTIOUSLY OPTIMISTIC OUTLOOK

Looking ahead, the impact of the trade war on Hong Kong external trade should be clearer in Q2 2019. Even though the trade conflict has not been completely resolved, a halt of trade tariffs is a positive sign.

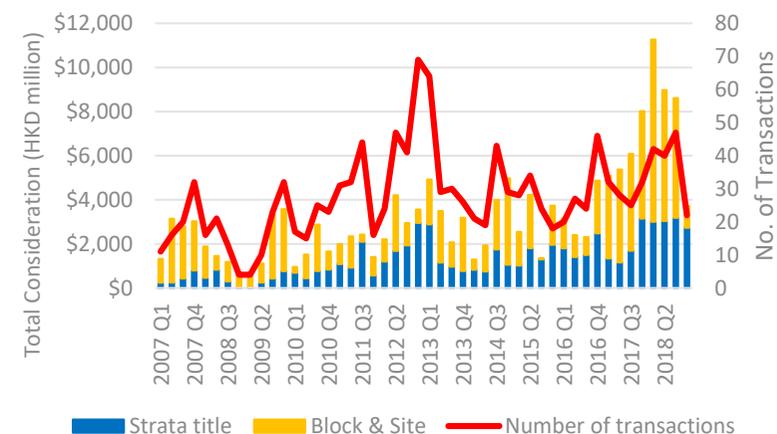
Continuous redevelopment and revitalisation will further decrease the industrial stock and keep vacancy rates low. On the demand side, we forecast retail sales growth of 6% in 2019 thanks to the likely increase in Chinese tourists permitted by the opening of the Hong Kong-Zhuhai-Macau Bridge. Moreover, the growth of e-commerce should continue to be led by Online to Offline (O2O) (i.e. customers from online channels making purchases in physical stores) transactions. According to Statista, Hong Kong e-commerce revenue should increase by 10.5% yoy in 2019 and 8.0% per annum from 2019 to 2023.<sup>2</sup> As a result, increasing demand for industrial space should drive up both rent and capital value of industrial properties.

In 2019, we expect warehouse and factory rents to increase by 5.4% yoy while the warehouse and factory prices should increase by 8.4% yoy.

<sup>1</sup> EPRC

<sup>2</sup> Statista

Value of industrial property transactions (deal size over HKD30 million)



Source: Census and Statistics Department, Colliers International

Industrial capital value and rent forecast

Subsector	Indicator	2019 (YOY)	2018-2023 (YOY)
Warehouses	Capital values	8.4%	6.6%
	Rents	5.4%	4.5%
Factories	Capital values	8.4%	6.6%
	Rents	5.4%	4.5%

Source: Colliers International

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