MARKET IN MINUTES

Savills Research

Industrial

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Industrial market to see uneven recovery

Industrial prices and rents remain under pressure as occupancy edges up slightly in Q3.

- The leasing volume saw a substantial jump of 27.7% year-on-year (YoY) in Q3 as Singapore began Phase 2 of reopening its economy.
- Savills average monthly rent for a multiple-user factory slipped by 0.8% quarter-on-quarter (QoQ) to S$1.71 per sq ft, while rents for warehouse & logistics space reversed a short-lived decline posting a 0.9% QoQ increase to S$1.42 per sq ft.
- Total strata sales volume more than doubled from Q2 to 372 deals in Q3, a reversal from the four-quarter decline seen since Q3/2019.
- Owing to the scarcity of freehold industrial stock, especially in prime locations, prices of freehold industrial prices edged up by 0.2% QoQ to S$694 per sq ft.
- Savills' basket of industrial properties showed that the average price for a 60-year leasehold industrial unit fell by 0.9% QoQ to S$425 per sq ft, while prices for 30-year leasehold properties fell by 2.2% QoQ to S$301 per sq ft over concerns about depleting lease terms.
- As most landlords of the prime business parks are holding their asking rents at S$6 per sq ft up, the average monthly rent in Savills basket of prime business park properties managed to stay flat from the previous quarter at S$5.81 per sq ft.
- Savills basket of standard business park properties showed that the average monthly rent weakened again for a second quarter, albeit at a slower rate of 0.4% QoQ to S$4.05 per sq ft.
- Average monthly rent for Savills high-spec industrial basket inched down marginally by 0.2% QoQ to S$3.47 per sq ft in Q3.
- We forecast rents for multiple-user factories to fall 1% to 3% while warehouses will remain flat in 2020. For 2021, the former may see rents move in a range of 0% to -3% YoY, but the latter, due to strong demand to buffer against potential supply chain disruptions, could rise by 1% to 3% YoY.

"The plight of the ubiquitous Small & Medium Sized Enterprises continues to drag down the overall industrial market."

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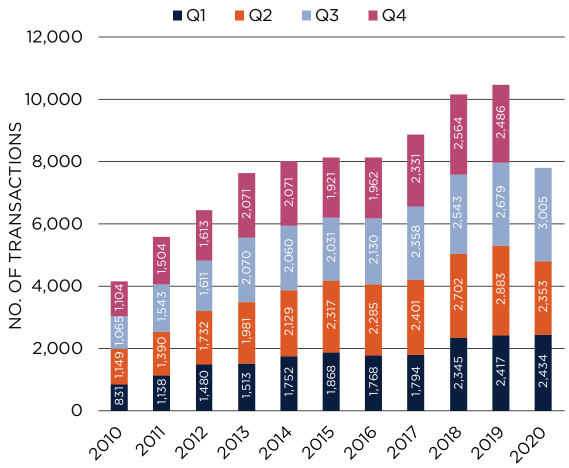
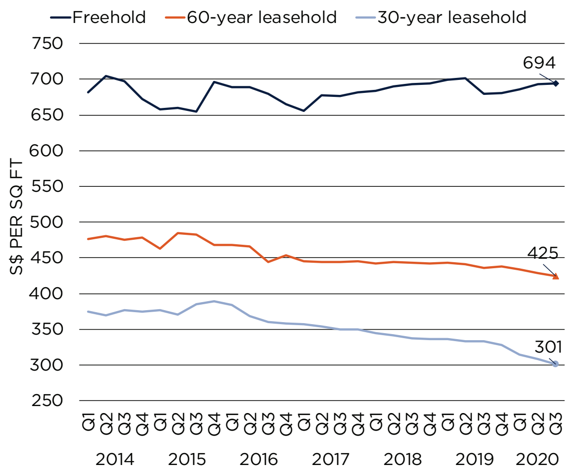
GRAPH 1: Factory And Warehouse Leasing Volumes, 2010 to Q3/2020



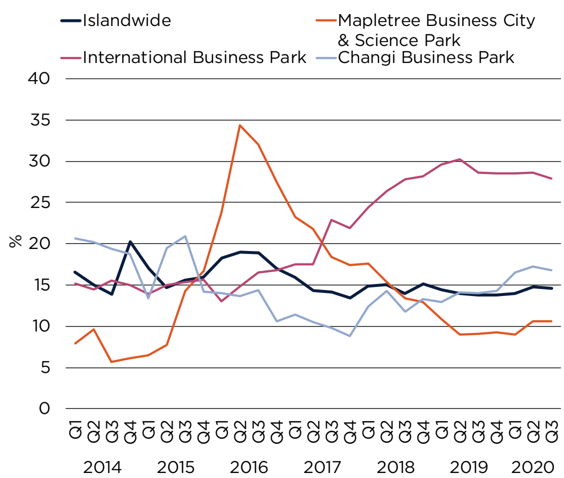
Source JTC, Savills Research & Consultancy

GRAPH 2: Prices Of Upper-Storey Strata Factory And Warehouse Units, Q1/2014 to Q3/2020



Source JTC, Savills Research & Consultancy

GRAPH 3: Business Park Space Vacancy Rates, Q1/2014 to Q3/2020



Source JTC, Savills Research & Consultancy

MACROECONOMIC OVERVIEW

Following the phased reopening of the economy in late-June, Singapore's economy rebounded in Q3/2020 from the sharp contraction in the previous quarter. According to advance estimates from the Ministry of Trade and Industry (MTI), the economy expanded by 7.9% QoQ in Q3, compared with a 13.2% QoQ contraction during the lockdown in Q2. On a yearly basis, the economic performance also improved to -7.0% in Q3, easing from -13.3% in Q2. This came on the back of a 2.0% YoY recovery in the manufacturing sector, reversing from the -0.8% YoY growth in Q2. This was fuelled by the pick-up in global demand for semiconductors and semiconductor manufacturing equipment, which drove the output of electronics and precision engineering clusters.

Following the sluggish performance of the manufacturing sector in Q2, sentiment turned positive in Q3. After five months of negative readings since February, the overall Purchasing Manager's Index (PMI) is back in expansionary mode for three consecutive months, suggesting a more upbeat economic backdrop amid a gradual reopening of the economy. This was coupled with positive momentum in Singapore's non-oil domestic exports (NODX), which continued to expand through Q3, albeit at a slower pace in September.

RENTAL MARKET

As Singapore began Phase 2 in its reopening of the economy in June, leasing activity in the industrial market picked up. There was a sharp increase of 27.7% YoY in leasing volume[1] to 3,005 transactions in Q3, a record since the data was constituted in 2000. (Graph 1) This was largely lifted by a spike in leases for multiple-user factory spaces (+16.6% YoY), which hit a new all-time high of 2,405 transactions in Q3. We believe that this could be due to tenant relocation amid enhancement works of their previous premises, as well as downsizing plans as part of cost-cutting measures. Also, some of the leasing demand could have come from the smaller ecommerce players, who needed more space to manage the surge in last mile delivery services.

Compared with the same quarter last year, leasing demand for single-user factory spaces continued to rise by 1.2% in Q3, albeit at a slower pace than the preceding quarter (+14.5% YoY). While rental demand remained stable from last year, more single-user factory tenants and owners, who operate in multiple facilities, started to consolidate their operations and put up vacant facilities for lease or sale. Meanwhile, the warehouse segment saw a 4.0% QoQ dip in tenancies signed in Q3. Even though stockpiling pushed demand for warehouse space, warehouse leasing demand began to moderate as some companies in the performing industries, such as the pharmaceutical and healthcare sectors, are combining their operations into a single build-to-suit (BTS) facility for greater operational efficiency. Coupled with the increase in volume of single-user factories up for sale combined with softer price levels, some companies are considering acquisition of a single-user facility to house their operations under one roof.

The overall industrial vacancy level eased for two straight quarters in Q3, coming off by 0.2 of a percentage point (ppt) QoQ to 10.4%. Besides limited new completions due to delays in construction work during the lockdown period, the occupancy level was largely supported by the spike in storage needs, particularly in North-East and North Planning Region where warehouse vacancy fell to the lowest levels since 2018 and 2016 respectively.

JTC's rental indices continued to weaken across all segments in Q3 as pandemic-led recession exerted downward pressure on rental levels. According to Savills basket of properties, the average monthly rent for prime multiple-user factories[2] slipped by 0.8% QoQ to S$1.71 per sq ft. On a positive note, the warehouse and logistics[3] segment performed better in Q3, with Savills average monthly rents for prime warehouse and logistics properties reversing a short-lived decline to register a 0.9% QoQ increase to S$1.42 per sq ft. Even though JTC's warehouse rental index continued to fall in Q3, prime and modern warehouse facilities helped to support the overall rental growth in light of strong demand for storage and logistics space.

SALES MARKET

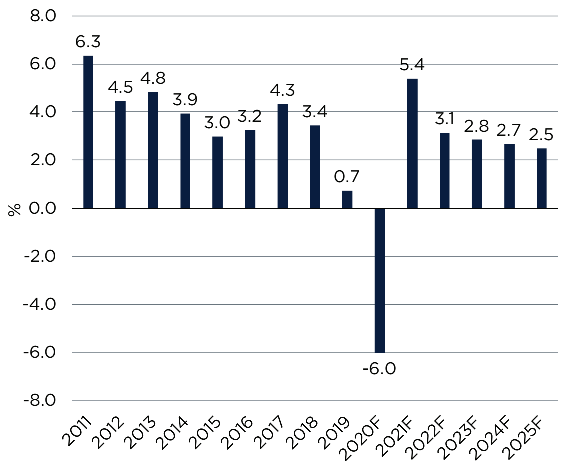
Total strata sales volume more than doubled from Q2 to 372 in Q3, a reversal from a four-quarter decline which begun in Q3/2019. It was mainly lifted by an uptick in strata sales for multiple-user factory and warehouse properties, such as Mega@Woodlands and Oxley Bizhub. The demand could have come from firms, particularly in printing as well as event organising, who are downsizing their real estate footprint. Furthermore, some companies in healthcare and the aquaculture industry (i.e. frozen seafood) are also looking

1 Based on JTC's rental data (excluding business park spaces, only comprises single- and multiple-user factory as well as warehouse spaces).

2 Based on Savills basket of private multiple-user factory properties which ranges from 1,000 sq ft to 3,000 sq ft in size, with an average monthly asking rent of at least S$1.50 per sq ft.

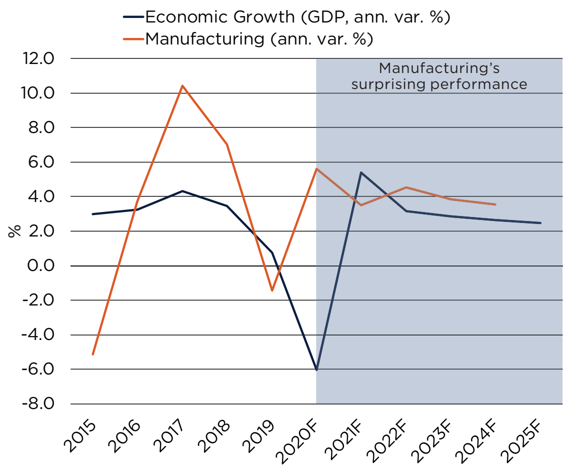
3 Based on Savills basket of private multiple-user warehouse properties which ranges from 2,000 sq ft to 80,000 sq ft in size, with an average monthly asking rent of at least S$1.40 per sq ft.

GRAPH 4: Singapore GDP Historic And Forecast, 2011 to 2025F



Source FocusEconomics

GRAPH 5: Overall And Manufacturing GDP YoY Growth, 2015 to 2025F



Source Singstat, UOB, FocusEconomics

to acquire larger facilities to support their business expansion as the pandemic has benefitted them. Although there is a growing buying interest among automotive players, especially when there are more single-user factories up for sale, most of them did not translate to actual sales as the prospects are still waiting for better offers before the lease expiry of their current premises.

While some owners maintained their price expectations, particularly for freehold assets, data from JTC showed that overall industrial prices fell by 2.2% QoQ in Q3, making it the largest decline in the last four consecutive quarters. Similarly, Savills' basket of leasehold industrial properties[4] also continued to register declining prices in Q3. Prices for 60-year leasehold properties fell at a moderate pace of 0.9% QoQ to S$425 per sq ft, while that for 30-year leasehold properties fell by 2.2% QoQ to S$301 per sq ft due to depleting lease terms. As there is a scarcity of freehold industrial stock available currently, especially in prime locations, freehold industrial prices held firm, recording a marginal rise of 0.2% QoQ to S$694 per sq ft.

BUSINESS PARKS AND HIGH-SPEC INDUSTRIAL

Having stayed in the negative for the first two quarters, the business park segment regained strength in Q3, with net demand improving across all regions. As a result, islandwide vacancy eased by 0.2 of a ppt QoQ to 14.6% in the reviewed quarter. (Graph 3) This could have arisen from financial institutions taking up new business park space for their back-end operations while reducing their office space in the Central Business District. Nonetheless, landlords' pricing power was lower with the JTC rental index for business park dropping yet again by 1.0% QoQ in Q3. This is likely to be weighed down by the older business parks which saw a further softening of rents. Concurrently, Savills basket of standard business park properties[5] showed that the average monthly rent weakened again for a second quarter, albeit at a slower rate of 0.4% QoQ to S$4.05 per sq ft. As most landlords of prime business park space maintained their monthly rental expectations of at least S$6 per sq ft, the average monthly rent in Savills basket of prime business park properties[6] remained flat from the previous quarter at S$5.81 per sq ft.

Although the on-going relocation plans by some existing office users could lend some support to the high-spec industrial market, rents continued to face pressure as prospects are only enticed if the rental savings are significant after factoring in relocation costs. Meanwhile, it is also challenging for landlords to increase rents for renewals as some existing high-spec industrial users are considering relocating to other light industrial space if capable of projecting a good corporate image, with office-like specifications and in areas with good connectivity such as Paya Lebar. As such, the average monthly rent for Savills high-spec industrial basket[7] inched down marginally by 0.2% QoQ to S$3.47 per sq ft in Q3.

OUTLOOK

Come spring 2021, as economic and social activity gradually resumes in advanced economies after the winter lockdown measures, overall economic conditions should begin to improve. For 2020, the International Monetary Fund (IMF) expected a less severe global economic downturn (-4.4%) this year in its latest report than the previous forecast in June. Nonetheless, the slower than expected reopening and the reinstatement of another shutdown amid a resurgence in virus in some countries could motivate the IMF to lower their growth expectations this year. The Monetary Authority of Singapore (MAS) also expected a modest pace of economic recovery in Singapore for the coming quarters in the face of a potential resurgence in worldwide infections which will drag on external demand. While MAS forecast a more modest pace of economic momentum in the last quarter of the year, the government maintained its economic forecast for between -7.0% and -5.0% YoY for this year. The consensus amongst private sector economists has GDP contracting by 6.0% YoY in 2020.

Local economists are now veering towards a U-shaped recovery scenario for Singapore with 2021 GDP growth coming in at 5.4% YoY. This is reasonable as the lockdown in Q2/2020 followed by a phased opening of the economy thereafter has stymied domestic economic activity greatly. Therefore, as the economy opens further, GDP growth should significantly increase in 2021 given the low base this year. The sharp contraction in the Construction and Services sector (part of the Services sector which constituted 65% of 2019's GDP) is very likely to reverse with similarly sharp increases albeit we may not see a return to pre-COVID levels in 2021. (Graph 4)

Drilling down to the manufacturing sector, it has been performing surprisingly well with Q3/2020 GDP Manufacturing

4 Only include upper-storey strata-titled factory (single- and multiple-user factory) and warehouse units, excluding all ground floor units.
5 Based on business park-zoned spaces in the older clusters which range from 1,000 sq ft to 5,000 sq ft in size, with an average monthly asking rent of at least S$3.50 per sq ft.
6 Based on business park-zoned spaces in the newer clusters which range from 1,000 sq ft to 5,000 sq ft in size, with an average monthly asking rent of at least S$5.50 per sq ft.
7 Based on office-like industrial space which ranges from 2,000 sq ft to 4,000 sq ft in size, with an average monthly asking rent of at least S$3 per sq ft.

posting a 2.0% YoY growth. Notwithstanding negative GDP growth, which came mainly from the Construction and Business & Services sector, the Manufacturing sector did surprisingly well with a 5.7% YoY growth for the first three quarters of 2020. For the full year, manufacturing growth could come in at 5.6% YoY. The sub-sectors which contributed to the sharp increase were from biomedical, pharmaceutical, semiconductor and the electronics manufacturing. (Graph 5)

The stellar performance of some sub-sectors within the manufacturing sector has dampened the pricing and rental downside. In fact, on the logistics front, most warehouses here are filled to capacity and some spillover demand has been seen in traditional light industrial space. Consequently, activity levels in this real estate market have held up well.

Looking ahead, despite growing interest in the industrial sales market from businesses in booming industries such as healthcare and aquaculture, the conversion rate to actual sales is likely to remain subdued because of the gap which exists between buyer and seller expectations. On the rental front, although the leasing market is expected to stay active in the coming months, it is coming from more businesses seeking to consolidate and reduce space as part of their cost-saving plans. Even though further delays in projected completions are expected, overall occupancy levels are likely to remain depressed in the near term. Industrial prices and rents will continue to be negatively impacted by Small & Medium Sized Enterprises as the pandemic has hit them hardest. Although there is increasing consensus that the economic recovery could be U-shaped, the economy is unlikely to return to pre-COVID levels soon. While the more resilient segments, including business parks, high-spec industrial and logistics space, could possibly find some support to occupancy and rental levels, the recovery has not been even across all segments. For tenants in such premises, most will rather pay a premium for better-maintained properties in prime locations with better connectivity, hence sustaining the positive take-up and rents of prime properties. On the other hand, older properties in the outskirts are expected to continue to see softer demand and weaker rents. In the coming quarters, the exception to the general industrial and business space market is logistics where we are beginning to see warehousing rents starting to stabilise and even rise marginally in some cases.

Table 1 is a summary of our view on rents for multiple-user factory and warehouse space for 2020 and 2021.

TABLE 1: Rental Forecast For Multiple-User Factory And Warehouse & Logistics Segments

PERIOD	YoY % CHANGE IN MULTIPLE-USER FACTORY RENTS	YoY % CHANGE IN WAREHOUSE & LOGISTICS RENTS
2020F	-3.0% to -1.0%	0.0%
2021F	-3.0% to 0.0%	+1.0% to 3.0%

Source Savills Research & Consultancy