

PROPERTY INSIGHTS

Hong Kong | Quarter 3, 2013

TMT sector emerges as a new driver of office market

Market Overview

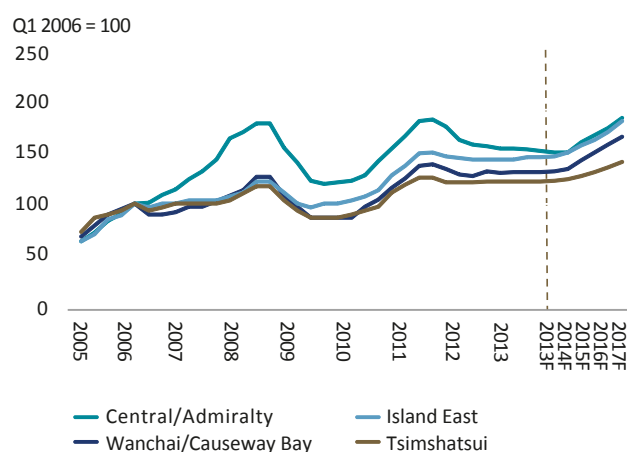
In Q3, leasing demand for office softened, and overall net absorption within the quarter reached -191,928 sq ft, attributed mainly from Sheung Wan/ Central/ Admiralty. As a result, overall rent decreased slightly by 0.72% quarter-on-quarter (q-o-q) to reach HK\$60.8 per sq ft per month. However, few stronger sectors such as technology, media and telecommunications (TMT) sector were witnessed as continuing to expand within this quarter, a phenomenon which benefited districts such as Wanchai/ Causeway Bay and Kowloon East.

As a result of increasing number of daytripping Mainland visitors from across the border, New Territories retail rent witnessed the highest year-on-year (y-o-y) rental growth within this quarter, growing by 5.5 %, as compared to much flatter performance of retail rents in Hong Kong Island and Kowloon. While competition of tier 1 high street shops in prime retail districts remained intense, vacant space is on the rise in tier 2 and 3 street shops in prime retail districts, due the gap which has opened in rental expectations between landlords and tenants in these areas.

Residential price remained stable and overall prices this quarter only decreased marginally by 0.1% q-o-q, although transaction volume continued to remain low. Supported by end-user demand, mass

Figure 1

DTZ office rental index (2005 - 2018F)



Source: DTZ Research

residential price registered an increase of 0.5% q-o-q, whereas luxury residential price decreased 0.8% within the same time frame.

Total number of deals exceeding HK\$100mn dropped further by 36% within Q3, declining from 42 in Q2 2013 to 27 in Q3 2013, and investment volume dropped even more by 43% to just HK\$7.524bn (US\$0.969bn) in Q3 2013. Only transaction in industrial, hotel, and development site did not witness a decline, as industrial properties are attractive due to their revitalization potential and the hotel sector has benefited by strong tourism growth in recent years.

Trends & Updates

Economic Overview

Real GDP annual growth rate reached 3.3% in Q2 2013, higher than the 2.9% annual growth in Q1 2013 (Table 1), reflecting some improvement in local economic activities this quarter.

The value of total exports dropped slightly by 1.3% y-o-y to reach HK\$307.5bn in August 2013 (Table 1). The decrease in total exports was particularly severe in exports to Asian destinations including Malaysia (-16.7% y-o-y), Japan (-5.2% y-o-y), and Mainland China (-3.6% y-o-y).

Inflation increased slightly in Q3. The overall composite CPI in August increased 4.5% y-o-y, lower than the 3.9% growth rate in May (Table 1).

The seasonally adjusted unemployment rate remained low at 3.3% in June - August 2013, reflecting that employers' optimism in general towards employment (Table 1).

Domestic private consumption expenditure increased 4.5% y-o-y in Q2, decelerating from the 7.0% y-o-y growth in Q1 (Table 1).

Mainland tourist growth continued to support total visitor arrival growth. In August 2013, total visitor arrival grew 9.4% y-o-y to reach 5,358,087. On the other hand, retail sales also grew by 8.1% y-o-y in May 2013 to reach HK\$38.715bn (US\$4.989bn) (Table 1).

Table 1

Economic indicators

Indicator	Period	Unit	Value	Change y-o-y (%)
GDP at constant prices*	Q2 2013	HK\$bn	482.6	+3.3
Total exports	Aug 2013	HK\$bn	307.5	-1.3
Private consumption expenditure	Q2 2013	HK\$bn	329.2	+4.2
Unemployment rate (seasonally adjusted)	Jun 2013 - Aug 2013	%	3.3	-
Visitor arrivals	Aug 2013	Million	5.4	9.4
Composite CPI	Aug 2013	-	113.2	+4.5
Total retail sales value	Aug 2013	HK\$bn	38.7	+8.1

*in chained (2011) dollars

Source: Census and Statistics Department, HK\$AR, Hong Kong Tourism Board

Residential

Under the influence of the government curbs and concerns on the earlier than expected implementation of QE “tapering” by the US, prospective buyers remained cautious. However, mortgage rates in Hong Kong remained low as competition among banks continues to be intense. Property owners therefore were not willing to offer generous discount as they have strong holding power in general under the current low interest rate environment.

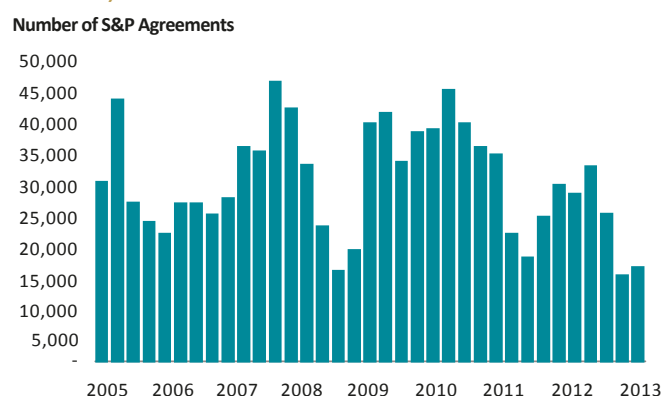
As a result of expectation gaps between property owners and prospective buyers, the transaction volume of secondary residential properties remained low throughout the quarter. Since September, as some more new projects have been launched to the market, there was some pick up in primary residential sales. Nevertheless, total transaction volume of buildings and land in Q3 only reached 16,258, which is only 57% of the volume recorded in Q3 2012, although it did increase by 9.6% compared to previous quarter (Figure 2).

Residential price remained stable despite the low transaction volume, due to the strong holding power of secondary home owners. As such, the overall residential price index decreased marginally only by 0.1% q-o-q, and it increased 3.2% y-o-y. But compared to its peak in February of this year, the price is down by 3% (Figure 3 and Table 2).

Mass residential properties demonstrated relatively stronger momentum with respect to both transaction volume and pricing as their sales are more supported by end-user demand. As such, the mass residential price index increased 0.5% q-o-q, and 6.6% y-o-y. However, since luxury residential market is more affected by the hike in sales tax, its price index dropped by more than 0.8% q-o-q, and 0.9% y-o-y (Figure 3 and Table 2).

Figure 2

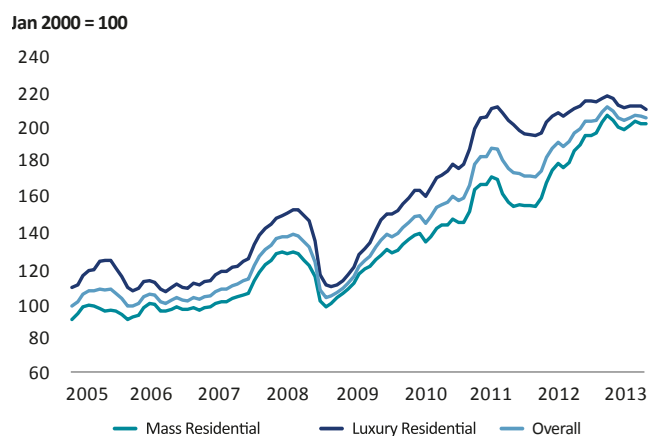
Transaction volume of S&P Agreements (Q1 2005 - Q3 2013)



Source: Land Registry

Figure 3

Residential price index (Jan 2005 - Sep 2013)



Source: DTZ Research

Table 2

Primary residential market statistics TBU

	Total stock (no. of units)	price index (Jan 2000 = 100)	q-o-q change (%)	y-o-y change (%)
Mass Market	1,032,377	211.24	0.5	6.6
Luxury Market	85,555	220.54	-0.8	-0.9
Overall	1,117,932	215.10	-0.1	3.2

Source: DTZ Research, Rating and Valuation Department HK\$AR

As at 30th September, there are 22 residential projects totalling 9,328 units pending pre-sale consent approval, according to Lands Department. It is expected that a fairly large proportion of these projects will be launched to the market by the end of this year, which should provide more choices for prospective buyers. Moreover, developers have also

Office

This quarter, the overall market witnessed deceleration as a consequence of the softening of demand. Overall net absorption this quarter reached -191,928 sq ft, and overall rent decreased slightly by 0.72% q-o-q to reach HK\$60.8 per sq ft per month (Table 3 and Figure 4).

In the Central Financial District (CFD) of Sheung Wan/ Central/ Admiralty, where corporate in the finance sector are still in the midst of downsizing or consolidating their business, negative net absorption of 201,490 sq ft was recorded, contributing the majority of overall negative net absorption this quarter. On the other hand, rental in the CFD declined marginally by 1.2% to HK\$103.0 (US\$13.2) per sq ft per month (Table 3 and Figure 4).

Leasing activities were quiet in Island East and Tsimshatsui, which recorded negative net absorption of 48,905 sq ft and 30,550 sq ft respectively. Rentals in the two districts remained unchanged compared to last quarter, at HK\$37.4 (US\$4.8) and HK\$33.3 (US\$4.3) per sq ft per month respectively (Table 3 and Figure 4).

However, there were a few stronger sectors such as technology, media and telecommunications (TMT) sector, which continued to witness expansion. This trend in particular benefited districts such as Wanchai / Causeway Bay, and to a lesser extent Kowloon East as well. For instance, SAP leased one floor (19,500 sq ft) in Times Square; LinkedIn took a floor (16,500 sq ft) in Hysan Place. As such, net absorption in Wanchai / Causeway Bay reached 52,207 sq ft, the highest among all sub-markets this quarter. The availability ratio in the market also dropped from 3.94% in Q2 to 3.62% this quarter (Table 3).

begun to offer more incentives to buyers since September. As such, we expect a larger proportion of prospective buyers will switch their interest from secondary market to primary market due to the larger incentive and wider variety of choices, and as such residential property prices should continue to face downward pressure.

Table 3

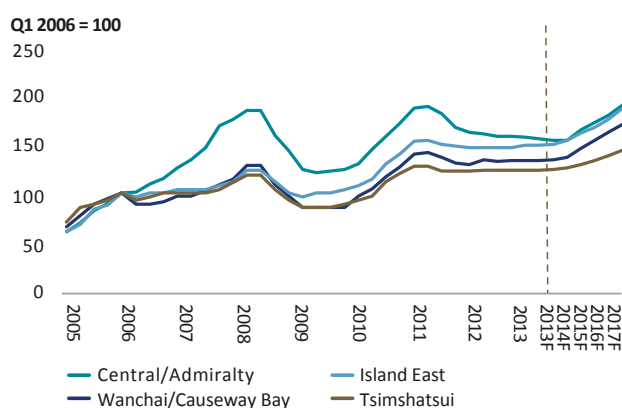
Grade A office market statistics

District	Total stock (million sq ft)	Availability ratio (%)	Monthly Rent (HKD per sq ft)	Change q-o-q (%)
Sheung Wan/ Central / Admiralty	29.31	6.25	103	-1.2
Wanchai / Causeway Bay	16.02	3.62	47	-
Island East	10.98	2.47	37	-
Tsimshatsui	9.27	4.32	33	-
Kowloon East	12.52	6.29	33	-
Overall	78.32	4.95	61	-0.8

Source: DTZ Research

Figure 4

DTZ office rental index (2005 - 2018F)



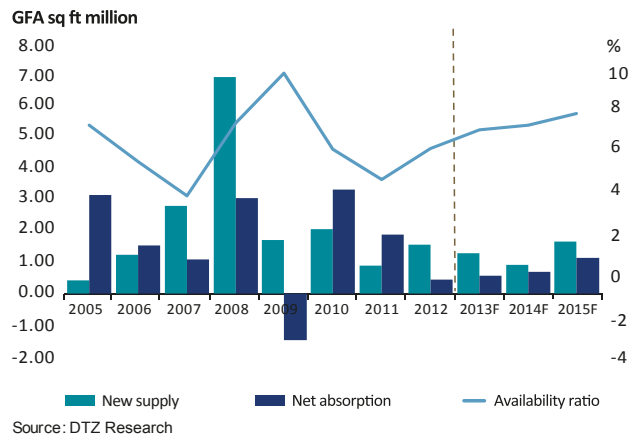
Source: DTZ Research

In Kowloon East, supported by take-up from nonfinance sectors, net absorption reached 36,810 sq ft, the second highest after Wanchai/ Causeway Bay. However, due to a new project, the Kin Seng Commercial Centre providing an additional of 120,000 sq ft office space to the market being completed within the quarter, the availability ratio increased from 5.93% in Q2 to 6.29% in Q3 (Table 3).

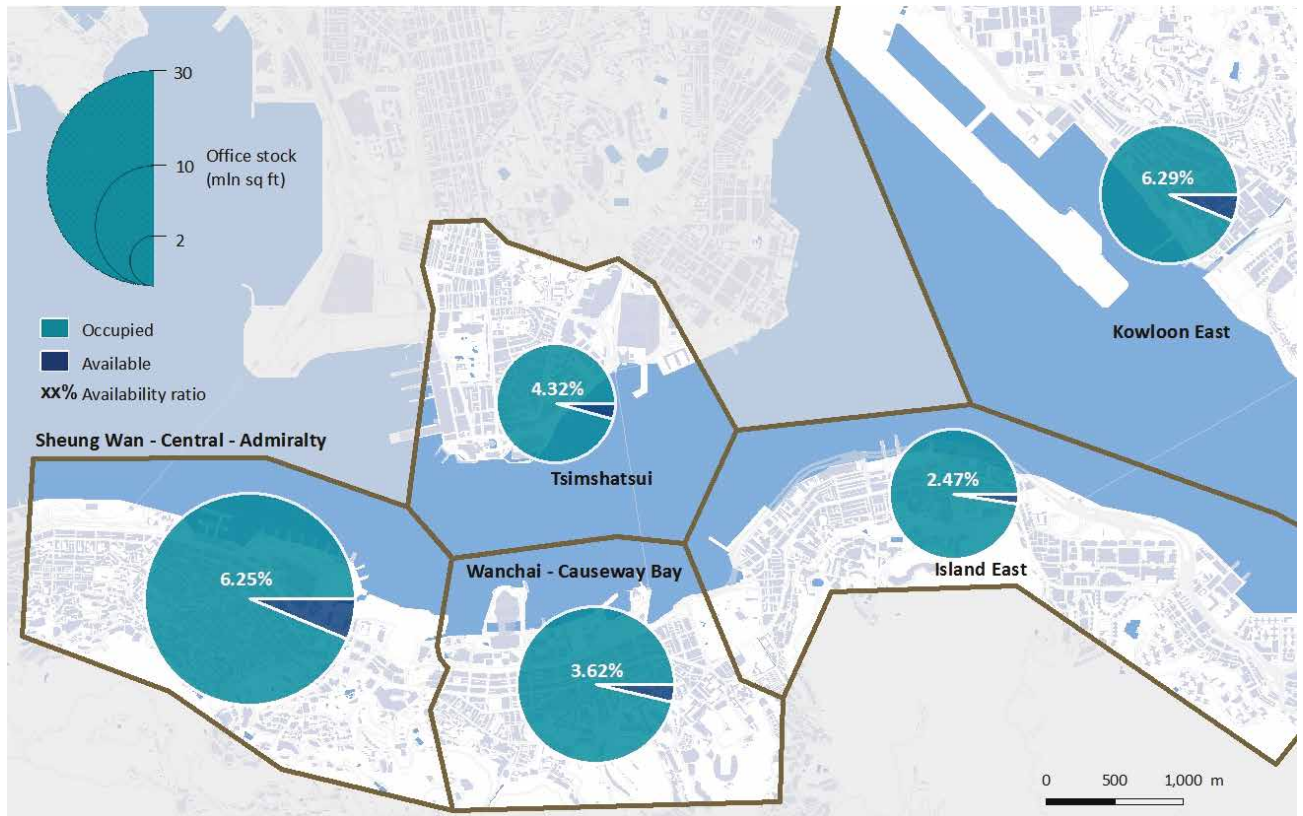
Looking forward, the market is expected to remain cautious as we expect the current downsizing trend to continue. However, the TMT sector is expected to continue to be a significant source of office demand due to the strong growth in e-commerce, social media, computer applications and sales of hi-tech products.

Figure 5

Grade A office supply, net absorption and availability ratio (2005 - 2015F)



Office availability by location



The Government of the Hong Kong SAR MAP reproduced with permission of The Directors of Lands
Source: DTZ Research

Retail

Number of total visitor arrivals in August grew 9.4% y-o-y to reach 5,358,087, of which 79% were Mainland Chinese visitors. At the same time, retail sales also grew strongly, jumping by 8.1% y-o-y to reach HK\$38.72bn (US\$4.99bn) (Figure 6).

With respect to visitors' spending pattern, while jewellery, watches and clocks, and valuable gifts still account for the largest portion of sales, sales of department store products increased more significantly by 23.2% y-o-y in August, reflecting a changing consumption pattern from high-end luxury products to more mid range products. Such change in spending pattern is to a certain extent contributed by the increased proportion of daytrip visitors, who are generally more interested in shopping for mid-range cosmetics products rather than the luxury products. The emergence of this trend is benefiting the regional shopping malls in New Territories close to the border or along the major light railway lines, such as Sheung Shui, Tuen Mun, and Shatin.

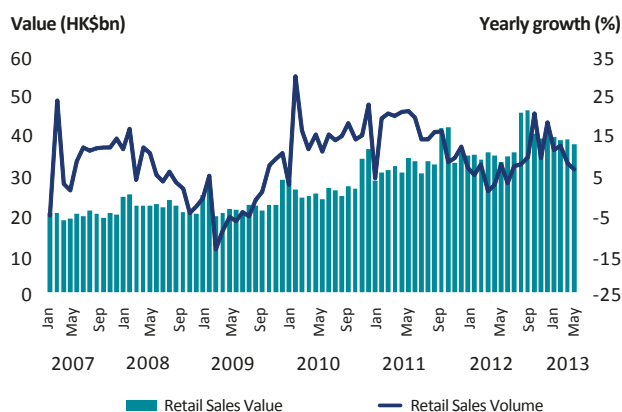
As such, New Territories retail rental index witnessed the highest y-o-y growth in Q3, rising by 5.5%, followed by Kowloon, at 4.1%. On the other hand, Hong Kong Island rental dropped 3.6% q-o-q and 4.8% y-o-y (Table 4 and Figure 7).

In the traditional prime retail districts such as Tsimshatsui and Causeway Bay and Mongkok, competition for retail space in tier 1 high street shops remained intense. In particular, cosmetics and midmarket retailers remained keen on expansion. For instance, a cosmetics company had moved to Canton Road in Tsimshatsui with a 286% increase in rentals. However, vacant space increased in tier 2 and 3 street shops within the prime retail districts as are persisting expectation gaps between landlords and tenants with respect to leasing such space.

Looking ahead, Cosmetics and medium level retailers are expected to see improved sales in the next quarter, which will be underpinned by the holidays - the October golden week and Christmas - that bookend the quarter. This trend is expected to continue to support retail rental prospects.

Figure 6

Total retail sales (Jan 2007 - Aug 2013)



Source: Census and Statistics Department HKSAR

Table 4

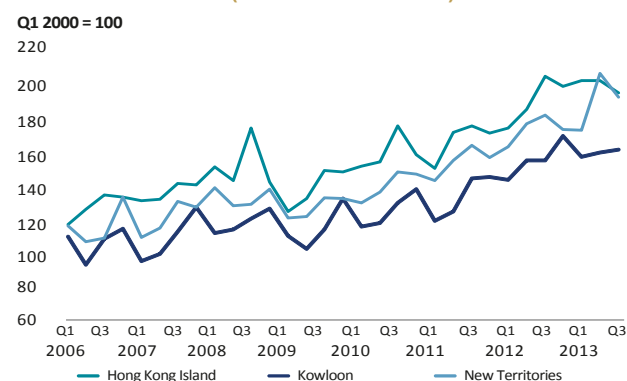
Retail market statistics

	Rental Index (Q1 2000 = 100)	q-o-q change (%)	y-o-y change (%)
Hong Kong Island	189.6	-3.6	-4.8
Kowloon	158.2	1.2	4.1
New Territories	187.4	-6.7	5.5

Source: Rating and Valuation Department HKSAR, DTZ Research

Figure 7

Retail rental index (Q1 2006 - Q1 2013)



Source: Rating and Valuation Department HKSAR, DTZ Research

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