

# Hong Kong Monthly

July 2020

## OFFICE

Chinese companies seek expansion amid the market downturn

### Hong Kong Island

The COVID-19 pandemic and local political uncertainty continued to dampen market sentiment and exert heavy pressure on office rentals in the CBD area. In June, Grade-A office rentals plummeted 26.5% in Admiralty and 22.6% in Central YoY, extending the decline to 14 consecutive months.

Despite the overall sluggish economic conditions, Chinese companies, particularly the leading players in the financial sector and tech giants, sought expansion against the backdrop of an overall downward trend in rents. Examples include CMB International Capital and China Minsheng Bank, which leased additional space in Central, while Alibaba expanded its office area in Causeway Bay to satisfy growing business demand.

Many tenants, especially small companies that are more sensitive to high rent, urged greater flexibility in lease terms, such as shorter leases, amid the current uncertainty. Looking ahead, with the worsening local economy, heightened political tension, and a third COVID-19 wave in the city, we expect both landlords and tenants to remain conservative.

### Kowloon

Tenant decentralisation from core Kowloon districts to Kowloon East continued to dominate relocation activity in the office leasing market, as tenants face mounting pressure to reduce costs by

downsizing, resulting in a large number of new lease transactions for small premises of less than 3,000 sq ft. One eye-catching case in June was the relocation of FWD Insurance, which moved from Wing On Centre in Sheung Wan to Millennium City in Kwun Tong, resulting in about a 50% reduction in unit rent.

Rents in Kowloon East continued to drop, slipping 7.8% YoY in June. An office in One Harbour Square in Kwun Tong was rented for HK\$18.5 per sq ft per month, which was far below market expectations, as the transacted rent was close to that in Grade-B office buildings and even industrial buildings. The trend of dropping rent in Kowloon East is mainly led by individual owners, though closely

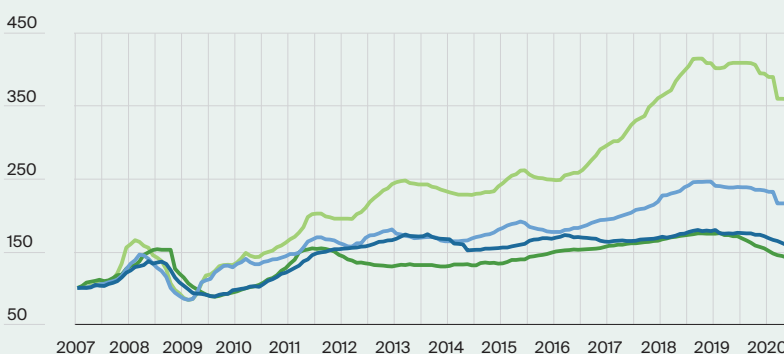
followed by the traditional landlords. More landlords are also offering non-financial incentives, such as free parking spaces, and waiving the reinstatement fee for new tenants. With the soaring vacancy rate and abundant upcoming supply, we expect traditional landlords to lower rents more aggressively, therefore lead to a further downward adjustment in the second half of the year.

A third wave of COVID-19 infections means Hong Kong's economy will inevitably take another hit, with some sectors being impacted more than others. The leasing market will therefore need a longer period to recover to pre-pandemic rental levels.

Fig 1. Grade-A office rents and prices

2007 = 100

■ Hong Kong Island price index     ■ Hong Kong Island rental index  
■ Kowloon price index             ■ Kowloon rental index



Source: Knight Frank Research

## Grade-A office market indicators (June 2020)

District	Net effective rent	Change		Price (Gross)	Change	
	HK\$ psf / mth	MoM %	YoY %	HK\$ psf	MoM %	YoY %
Premium Central	147.6	-3.3	-22.2	-	-	-
Traditional Central	111.0	-4.4	-22.9	-	-	-
Overall Central	123.4	-4.0	-22.6	38,563	0.0	-12.2
Admiralty	84.6	-4.2	-26.5	33,815	0.0	-13.7
Sheung Wan	70.3	-6.6	-17.5	30,793	0.0	-10.3
Wan Chai	64.7	-3.8	-17.6	26,950	0.0	-11.6
Causeway Bay	67.8	-4.5	-15.3	23,699	0.0	-10.3
North Point	45.6	-1.8	-11.9	-	-	-
Quarry Bay	50.8	-0.5	-7.9	-	-	-
Tsim Sha Tsui	63.8	-0.1	-11.6	16,355	0.0	-10.4
Cheung Sha Wan	30.5	-1.4	-8.5	-	-	-
Hung Hom	43.4	-0.5	-2.4	-	-	-
Kowloon East	29.5	-0.5	-7.8	12,256	0.0	-7.9
Mong Kok / Yau Ma Tei	56.0	-0.4	-6.7	-	-	-

Source: Knight Frank Research  
Note: Rents and prices are subject to revision.

# RESIDENTIAL

## Purchase and leasing demand remained resilient amid the pandemic

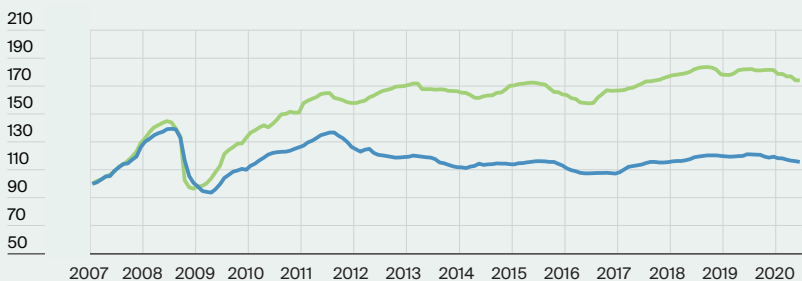
The adverse impact of the COVID-19 pandemic continued to linger in Hong Kong, with the labour market showing further deterioration. The latest unemployment rate for the April to June period climbed to the highest level in more than 15 years, hitting 6.2%. Despite this, the primary residential market received a warm response in June, with transaction volume surging 86% MoM to 2,195 cases, which shows that deferred demand returned to the market when Hong Kong's COVID-19 situation eased previously. Momentum in the secondary market also persisted, with 4,792 transactions recorded, similar to the level in the previous month. The latest official price index of mass residential property rose 1.9% MoM, resulting in a 1.5% increase year to date.

Despite the worsening economy and political uncertainty, the luxury market remained resilient, with purchase sentiment remaining strong. One major transaction was a 4,596-sq-ft unit in Mount Nicholson at the Peak, which was sold for HK\$533 million or HK\$116,000 per sq ft. The transaction price was on par with that of a similar unit that was sold in December last year for about HK\$115,000 per sq ft.

**Fig 2. Luxury residential rents and prices**

2007 = 100

Price index Rental index

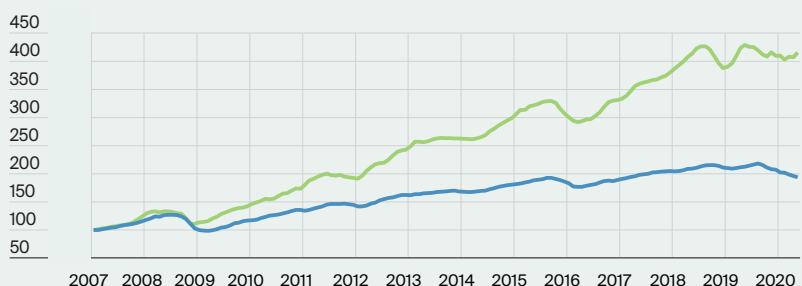


Source: Knight Frank Research / Rating and Valuation Department

**Fig 3. Mass residential rents and prices**

2007 = 100

Price index Rental index



Source: Knight Frank Research / Rating and Valuation Department

In the leasing market, we saw a revival of leasing activity for luxury properties, with demand coming mainly from local prospective tenants. Some major leasing deals were recorded in Island South, with unit rents reaching HK\$61–85 per sq ft. There was more flat-viewing activity in areas close to international schools to prepare for the coming academic year.

Several properties that had been listed for rental for a long time were leased out during the month, and the number of units available for lease in the market fell, again reflecting buoyant local demand.

With Hong Kong experiencing the third wave of COVID-19, buyer sentiment is expected to weaken in the coming weeks,

especially in the secondary market. The resurgence of COVID-19 in the city may cast a shadow over the leasing market in July and August, despite the fact that summer is the traditional peak season.

### Selected residential sales transactions (June 2020)

District	Building	Tower / floor / unit	Saleable area (sq ft)	Price (HK\$ million)	Price (HK\$ per sq ft)
<b>The Peak</b>	Mount Nicholson	Tower D / high floor	4,596	533.1	116,000
<b>Island South</b>	8 Deep Water Bay Drive	Tower 2 / low floor / unit D	2,865	175	61,082
<b>Jardine's Lookout</b>	Duke Place	Low floor / duplex unit B	2,849	172	60,372
<b>Mid-Levels Central</b>	Century Tower	Tower 2 / high floor	2,950	133.8	45,356
<b>Tai Tam</b>	Redhill Peninsula	House	4,010	112.8	28,130

Source: Knight Frank Research  
Note: All transactions are subject to confirmation.

### Selected residential lease transactions (June 2020)

District	Building	Tower / floor / unit	Lettable area (sq ft)	Monthly rent (HK\$)	Monthly rent (HK\$ per sq ft)
<b>Island South</b>	Residence Bel-Air	Tower 7 / high floor / unit A	1,295	110,000	85
<b>Mid-Levels Central</b>	Dynasty Court	Tower 2 / high floor / unit A	2,141	119,000	56
<b>Island South</b>	Hong Kong Parkview	Tower 15 / low floor	2,067	100,000	48
<b>Mid-Levels Central</b>	Tregunter	Tower 3 / high floor / unit D	3,014	129,000	43
<b>Island South</b>	Felix Villa	House	4,840	110,000	23

Source: Knight Frank Research  
Note: All transactions are subject to confirmation.

# RETAIL

## Retail sales forecast to fall about one-fourth given the loss of inbound tourism

Hong Kong's retail market continued to suffer, with visible shrinkage in retail sales and a spate of store closures, as the protracted pandemic hit inbound tourism hard. Given the travel restrictions, visitor arrivals plummeted 99.9% YoY to only about 8,000 in May. With the drastic decline in inbound

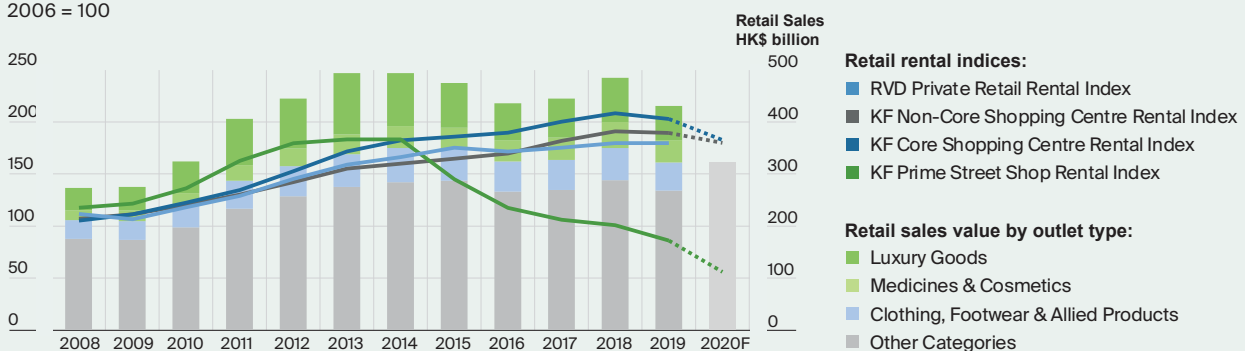
tourism, total retail sales value dropped 32.8% YoY in May to HK\$26.8 billion. In the first five months of 2020, retail sales value declined by 34.8% YoY.

As the retail market continued to be devastated by the evaporation of tourist receipts and weak local consumption,

a number of international brands closed their flagship stores in core retail areas. For example, American retailer Victoria's Secret closed its 51,000-sq-ft six-storey flagship store – its last outlet remaining in Hong Kong – in Capitol Centre in Causeway Bay. British beauty retailer Lush shut down its five-storey

**Fig 4. Retail rents and sales**

2006 = 100



Source: Knight Frank Research / Rating and Valuation Department / Census and Statistics Department

shop of about 7,000 sq ft in Central. Topshop announced that it will close its 14,000-sq-ft store on Queen's Road Central, its last store in Hong Kong, when its lease expires in October. Local media have reported that Gap will close half of its eight stores in Hong Kong, including its 13,000-sq-ft flagship store on Queen's Road Central and its store in Hysan Place in Causeway Bay.

With the COVID-19 pandemic continuing to weigh heavily on the retail property

market, prime retail districts have seen alarming signs of an abundance of vacant shops. Given the current weakening demand in the market, especially for large shops, landlords are dividing some into smaller shops to make it easier to rent vacant space. Some landlords of Ginza-style buildings have considered converting part of the vacant floors from food and beverage use to offices.

The recent return of social-distancing rules will further deplete consumer

confidence and spending. Given the significant reduction in tourism receipts (2019: HK\$121 billion), we forecast that total retail sales in 2020 will drop about 25% from last year's HK\$431 billion to about HK\$320 billion. We also expect the vacancy rate in core retail areas to continue to surge and prime street rents to continue to seek bottom during the rest of 2020, following a 30% downward adjustment in the first half of the year.

## Retail sales by outlet type (May 2020)

Outlet	Value (HK\$ billion)	Share of total%	Change MoM %	Change QoQ %	Change YoY %
Jewellery, watches and clocks, and valuable gifts	2.0	7.5	48.8	30.6	-69.7
Clothing, footwear and allied products	3.1	11.7	61.9	84.9	-36.2
Department stores	3.6	13.4	15.8	102.4	-37.8
Fuel	0.8	3.1	15.7	19.0	-5.0
Food, alcoholic drinks and tobacco (excluding supermarkets)	2.9	10.7	-4.0	-16.4	-17.0
Consumer durable goods	4.4	16.5	5.4	14.1	-7.2
Supermarkets	4.7	17.7	-0.5	-0.7	7.3
Others	5.2	19.3	3.5	5.6	-42.5
<b>All retail outlets</b>	<b>26.8</b>	<b>100.0</b>	<b>11.3</b>	<b>18.1</b>	<b>-32.8</b>

Source: Knight Frank Research / Census and Statistics Department

**We like questions, if you've got one about our research, or would like some property advice, we would love to hear from you.**

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