

Hong Kong Monthly

December 2022

OFFICE

Growing divergence between Hong Kong Island and Kowloon market performance

Hong Kong Island

The Hong Kong Island office market continued to be hit by volatile market conditions, with an accelerating rental decline. Overall net effective rents fell to HK\$69.5 per sq ft per month, dropping 2.1% MoM after falling 1.4% MoM in October. Rents in Central were down by 1.8% MoM, while Quarry Bay continued to underperform with a rental drop of 3.2% MoM.

As cautious sentiment prevailed, leasing activity remained at a low level in November. Certain upgrading cases were recorded – local financial firm Promise (Hong Kong) Co., Limited has committed to lease one floor circa. 20,000 sq ft at Central Plaza, and hedge fund Brevan Howard will relocate from Two Chinachem Central to Cheung Kong Center with a 10,000 sq ft lease.

Looking forward, 3.5 million sq ft of new office supply will enter the Hong Kong Island market by 2025, mainly in Central and Quarry Bay. Coupled with the existing high vacancy rate, rents are expected to face further pressure and continue their downward trajectory. In the short term, some landlords may offer substantial rental reductions to attract prospective tenants, given the unfavourable demand-supply dynamics. Compared to Central, rents in Quarry Bay are already at a very low level, so a smaller rental decline is expected. We expect office demand to remain sluggish in 2023 and overall rents of Hong Kong Island to fall by 3% to 5% for the whole year.

Kowloon

In November, Kowloon office market rents remained stable, which further supported our observation of a bottoming-out trend. Electronics and sourcing companies remained a major demand driver. Average monthly rents stayed broadly flat at HK\$24.5 per sq ft, and the average size of leasing transactions increased to 3,900 sq ft from below 3,000 sq ft last month.

Several sizable transactions supported market sentiment, as occupiers were keen to finalize their real estate decisions towards the end of the year. A Japanese electronics company will relocate from North Point to occupy an entire top floor with 36,000 sq ft at AIRSIDE, Kai Tak. BOC Insurance will relocate

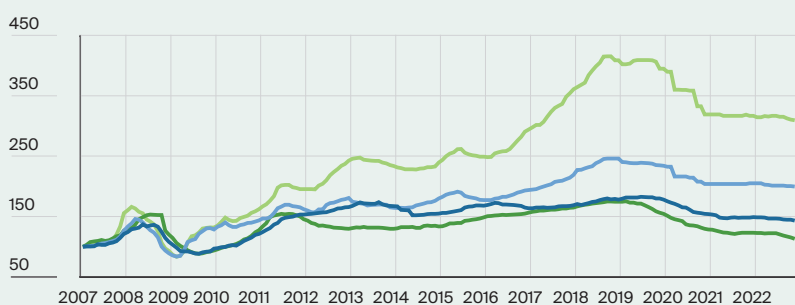
to The Gateway, Tower 5, with a floor space of 23,405 sq ft, from Harbour City office blocks. Apart from office quality upgrades, the continued rise of ESG and agile workplaces have become considerations in occupiers' real estate decisions. Office buildings with better ESG and sustainability criteria are more appealing in the market.

In the short term, we expect the Kowloon market to remain weak, but see signs of it bottoming out. With the imminent border reopening with the Chinese mainland and the removal of most travel restrictions in Hong Kong, mainland and MNC tenants are expected to return, and Kowloon rents should increase slightly by 0% to 3% in 2023.

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 (November 2022)

District	Net effective rent	Change		Price (Gross)	Change	
	HK\$ psf / mth	MoM %	YoY %	HK\$ psf	MoM %	YoY %
Premium Central	125.5	-0.5	-6.3	-	-	-
Traditional Central	96.6	-2.7	-6.3	-	-	-
Overall Central	106.4	-1.8	-6.3	32,481	-0.3	-2.6
Admiralty	66.2	-3.8	-10.0	28,455	-0.4	-2.7
Sheung Wan	55.2	-0.2	-10.5	26,859	0.0	-1.8
Wan Chai	50.4	-1.4	-5.3	24,048	-0.4	-2.0
Causeway Bay	58.5	-1.8	-4.9	20,999	-0.5	-2.3
North Point	38.1	-1.9	-10.7	-	-	-
Quarry Bay	45.8	-3.2	-14.5	-	-	-
Tsim Sha Tsui	55.6	-0.1	-2.3	14,723	-0.6	-3.2
Cheung Sha Wan	28.3	0.0	-0.4	-	-	-
Hung Hom	38.5	-0.1	-3.6	-	-	-
Kowloon East	29.5	1.7	-1.5	11,791	-0.2	-1.9
Mong Kok / Yau Ma Tei	50.7	0.2	1.2	-	-	-

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

RESIDENTIAL

Sagging residential market lacks momentum as prices and transaction volume hit bottom

The Hong Kong residential market remained sluggish and lost momentum, as rising interest rates and the weakening local economy continued to weigh on buying sentiment, resulting in a significant decrease in transaction volume. Primary sales plummeted by 45.7% MoM to 365 transactions in November, according to the Land Registry.

Amid the shrinking labour force, rising mortgage rates and the deteriorating external environment, overall residential home prices continued to slump. According to statistics from the Rating and Valuation Department, Hong Kong's home price index fell 2.4% MoM to 352.4, the lowest level since December 2017.

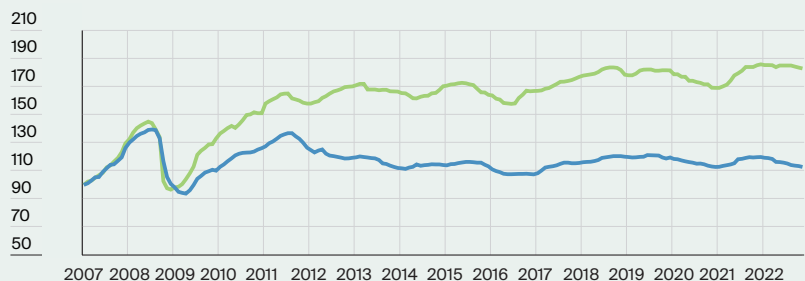
In the mass market, there was a rising number of loss-making housing transactions amid the emigration wave. Some homeowners were in a rush to sell their properties and were willing to substantially reduce their asking prices.

The luxury market performed better since homeowners were willing to provide wider room for negotiation to potential buyers. Significant transactions in November included a 9,170 sq ft house at 23-39 Blue Pool Road in Happy Valley, which was

Fig 2. Luxury residential rents and prices

2007 = 100

Price index Rental index

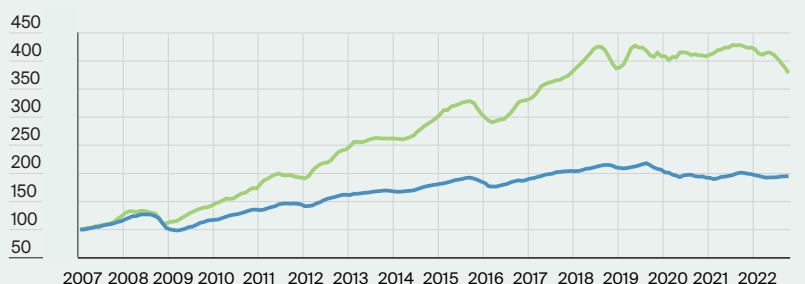


Source: Knight Frank Research

Fig 3. Mass residential rents and prices

2007 = 100

Price index Rental index



Source: Knight Frank Research / Rating and Valuation Department

sold for HK\$600 million; and a house in Overbays in Repulse Bay, which was sold for HK\$430 million, or HK\$95,556 per sq ft.

Since the current actual interest rate exceeds 3%, it has begun to have a certain

impact on the purchasing power of homeowners. We expect market activity to pick up only after Chinese New Year. Looking ahead to 2023, we expect the mass and luxury residential property prices in Hong Kong to fall by 5% to 10% and 0% to

5%, respectively, the transaction volume ratio of first- to second-hand homes to be about 30:70, and the total residential transaction volume to be 48,000 to 53,000 units.

Selected residential sales transactions (November 2022)

District	Building	Tower / floor / unit	Saleable area (sq ft)	Price (HK\$ million)	Price (HK\$ per sq ft)
Island South	Overbays	House	4,500	430	95,556
Happy Valley	23-39 Blue Pool Road	Houses A & B	9,170	600	65,431
Mid-Levels	21 Borrett Road	Mid floor	2,154	133	61,746
Beacon Hill	Mont Verra	Tower 2 / low floor / unit A	4,451	258.2	58,000
Beacon Hill	Mont Rouge	House	2,846	141	49,543

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

Selected residential lease transactions (November 2022)

District	Building	Tower / floor / unit	Lettable area (sq ft)	Monthly rent (HK\$)	Monthly rent (HK\$ per sq ft)
Mid-Levels Central	Queen's Garden	Tower A / high floor	2,299	172,000	75
Happy Valley	Leighton Hill	Tower 5 / low floor / unit B	1,724	106,000	61
Pok Fu Lam	Residence Bel-Air	Phase 5 / house	4,161	245,000	59
Mid-Levels Central	Garden Terrace	Tower 1 / high floor / unit B	3,204	135,000	42
Island East	Kennedy Height	Low floor / unit B	2,929	110,000	38

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

RETAIL

Relaxed restrictions provide a glimmer of hope for retailers in 2023

The latest Hong Kong retail figures indicate that the local retail market has seen a gradual recovery, given the disbursement of a new batch of consumption vouchers and the traditional peak season for the retail market as the Christmas and New Year holidays approach. According to the Census and Statistics Department, total retail sales

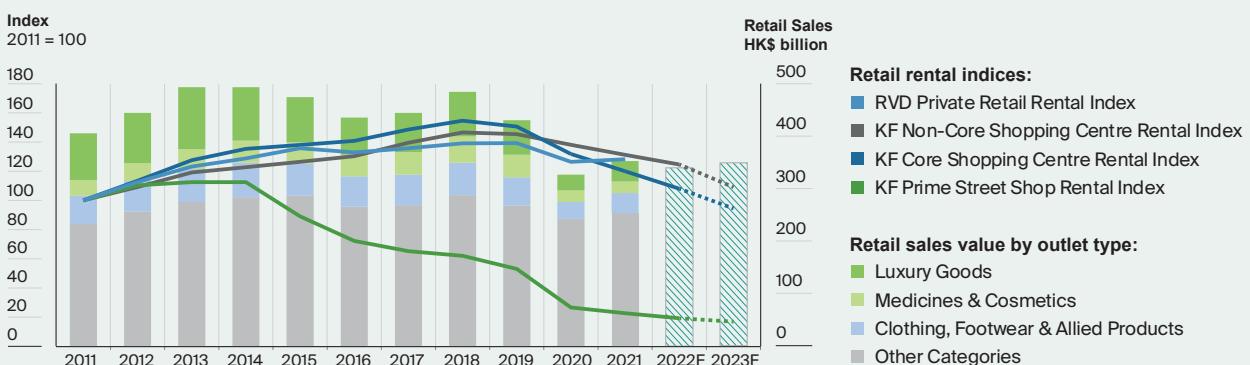
in October 2022 surged by 3.9% YoY to \$31.9 billion. However, for the first 10 months of 2022, the total value of retail sales registered a mild decrease of 0.7% YoY.

Overall, the retail market was sluggish in 2022, as local consumers remained conservative in spending, and the

Consumption Voucher Scheme provided only short-term support for the economy.

In our opinion, there were several major reasons for the drop in overall retail sales in 2022: stringent anti-epidemic measures during the pandemic; the volatile stock market, leading to weak consumption

Fig 4. Retail rents and sales



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

power; the poor performance of the residential property market, which dampened consumer sentiment; inflation and higher mortgage rates, which increased pressure on homeowners; and the Hong Kong–USD linked currency, which discouraged locals from spending, as some people preferred to leave their money in the bank to earn interest. The strong Hong Kong dollar also encouraged more locals to take overseas holidays, thus dampening domestic demand. Finally,

Hong Kong is undergoing an emigration wave, in particular among the middle class, which has structurally led to a loss of a large portion of local retail sales.

Looking ahead, the Christmas and New Year holiday period is a typical peak season for the retail market. Since the social-distancing rules have been further relaxed, with people no longer required to scan the LeaveHomeSafe QR code when entering venues; bars, nightclubs,

banquets and local tours no longer required rapid Covid tests; cinemas, theme parks and performing venues can operate at full capacity; and restrictions lifted on arrivals etc., we believe retail sales are set to pick up. In 2023, we expect to see a stable recovery trend in the retail market, but not a significant rebound. Overall retail rents will remain under pressure owing to the longstanding vacancy rates across the board.

Retail sales by outlet type (October 2022)

Outlet	Value (HK\$ billion)	Share of total%	Change MoM %	Change QoQ %	Change YoY %
Jewellery, watches and clocks, and valuable gifts	4.0	12.5	18.2	-3.2	13.6
Clothing, footwear and allied products	2.8	8.7	18.3	-16.3	-5.4
Department stores	2.8	8.8	29.3	22.8	-17.2
Fuel	1.0	3.3	-3.4	-6.0	5.3
Food, alcoholic drinks and tobacco (excluding supermarkets)	3.0	9.5	-1.5	18.2	2.1
Consumer durable goods	7.5	23.3	17.5	70.2	17.2
Supermarkets	4.5	14.2	3.4	0.3	-2.7
Others	6.3	19.7	18.3	4.8	6.6
All retail outlets	31.9	100.0	13.6	12.8	3.9

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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