RESIDENTIAL
RESEARCH

ASIA-PACIFIC RESIDENTIAL REVIEW

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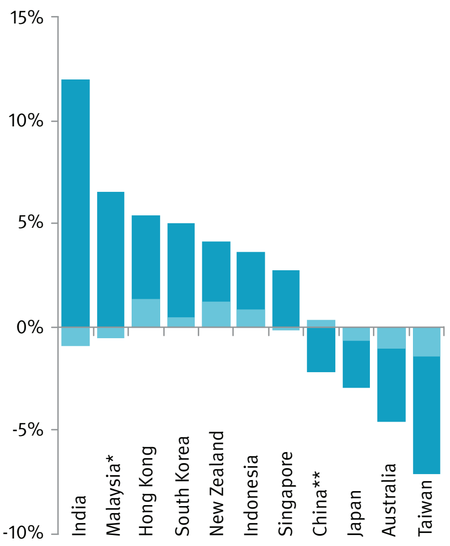
Knight Frank

INTRODUCTION

PROPERTY MARKET COOLING MEASURES AND GLOBAL ECONOMIC CONDITIONS TEMPER STRONG UNDERLYING DEMAND IN ASIA

Figure 1
Global House Price Index Q1 2012



*Data from Q4 2011
**Based on Beijing and Shanghai

Source: Knight Frank Research

Price performance across Asia Pacific residential markets varied significantly through the beginning of 2012 according to Knight Frank's latest Global House Price Index. Nicholas Holt examines the Asia Pacific numbers and trends more closely.

Continued government intervention in property markets across Asia has proved effective, as lending restrictions, additional taxes and protection from *hot foreign money* has led to a quarterly drop in mainstream prices across Malaysia, Taiwan and Singapore. China, the largest housing market on the planet also continued to see prices on a downward trend, with the central government resolute in managing a soft landing. India, which is facing a stuttering economy, also saw prices turn negative over the last three months.

In contrast to these drops however, Indonesia continued to see price rises on the back of rising incomes and urbanisation, reflecting an underlying demand for quality accommodation.

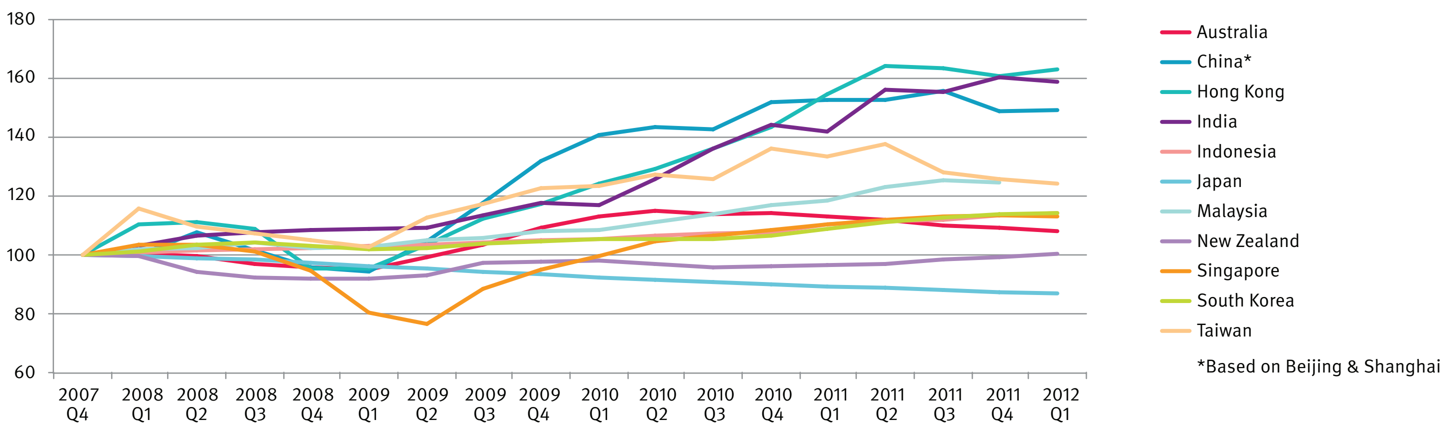
Similarly, housing markets in New Zealand and South Korea also experienced solid price appreciation over the quarter.

Australia continued to see its housing market deflate with the fifth consecutive quarterly price fall and Japan saw a continuation of the long term price falls in the residential land markets.

With the region's economic performance tightly linked with global trade flows, the outcome of the ongoing problems in Europe will undoubtedly have an effect on domestic economies and their respective housing markets. Sentiment in Asia Pacific is generally more cautious than at the end of 2011 and we expect this to continue through 2012.

Nicholas Holt
Research Director, Asia Pacific

Figure 2
Global House Price Index (Q4 2007 = 100)



*Based on Beijing & Shanghai

Source: Knight Frank Research

THE CHINESE MARKET CONTINUES TO COOL OFF... BUT FOR HOW LONG?

The Chinese housing market has had a tough 12 months as developers and purchasers alike have had bank finance squeezed as a consequence of the ongoing cooling measures.

As highlighted in our recent China Residential Market Watch, which focuses on the primary (new build) residential market across 20 major cities, prices have dropped some 6% from the last peak in the third quarter of 2011.

However, as Thomas Lam, Knight Frank's head of Research for Greater China explains, "...these price drops have to be put in the context of a 90% rebound from the last trough in the first quarter of 2009."

With the property cooling measures likely to remain until after the leadership handover later this year, the market is likely to continue to correct before a possible gradual relaxation of the policies through 2013.

In the meantime, developers are under increasing pressure to cut prices as large inventories need to be sold to meet financing costs, while local authorities are having their main revenue source mitigated, as land sales to developers are reduced.

The current squeeze has led to a number of developers filing for bankruptcy and others moving into commercial real estate in search of higher returns. It is also likely that we will see the continuing trend of non-specialist developers, who joined the market in the boom years, exiting the market, with further consolidation in the development market likely.

A risk of future undersupply?

There is such a huge amount of underlying demand in China (see Fig. 3 and 4), that there is a possible risk that by choking the private market off from finance, the drop in development activity could lead to a future contraction in supply that could lead to price increases down the road.

The government however, in the second strand of the *regulate and subsidise* approach, has planned 36 million affordable units to be built between 2011 and 2016. This plan has already seen 10 million units commenced in 2011 and 7 million in 2012. This ambitious target should help bring supply to a large proportion of end users, ensuring that a certain amount of housing supply meets real end user demand.

DRIVERS OF DEMAND IN DEVELOPING ASIA

What are the key drivers behind the residential markets in developing Asia?

End User Demand

We can list rising income levels, urbanisation and to a certain extent the slow move away from multi-family living. These drivers coupled with a substandard existing stock, fuel what you could consider real end-user demand.

Figure 3
Estimated growth in urban households in 2012 - 2020

China
53,179,226

India
23,689,447

Indonesia
5,978,747

Source: United Nations, Department of Economic and Social Affairs, Population Division, Knight Frank

Figure 4
Decreasing size of households

Average size of Chinese family household in 2000

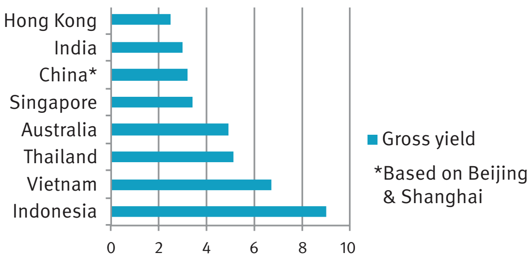
Average size of Chinese family household 2010

Source: National Bureau of Statistics for China

Investment Demand

On the other side, is the residential market as a pure investment, either for capital appreciation, wealth preservation, or both. The safe haven investment concept can also be applied in this sense. Residential yields, i.e. the gross yearly rental income as a percentage of purchase price is certainly a consideration for investors, in terms of covering finance costs and contributing to total returns.

Figure 5
Gross yield based on a well-located 100sqm apartment in good condition



Source: Knight Frank Research

MOVES TOWARDS PROTECTIONISM

While many developing Asian markets present significant barriers to entry for foreign buyers, Singapore's introduction in December last year of an Additional Buyer's Stamp Duty of 10% for foreigners was just one of the latest in a pattern of protectionist measures and rhetoric across some of the more open and developed property markets.

- Australia has removed the 50% capital gains tax discount for non-residents on capital gains accrued after 8th May 2012. This follows legislation introduced in 2010, restricting foreign buyers to new build properties only.
- In Hong Kong, the Chief Executive elect, CY Leung has signalled his intention to restrict purchases of certain classes of new housing developments to residents.
- In Malaysia, the proposed doubling of the minimum price of properties that foreigners can buy from RM500K to RM1 million could be passed into law this year.

Most of these measures and sentiment comes as a popular backlash from domestic buyers who feel priced out of their *birth right* by foreign buyers. This swing towards populism underlines how property booms have impacted affordability, especially for first time domestic buyers.

A change in land policy in the Hong Kong residential market?

Mainstream prices in Hong Kong, which have increased an eye watering 102% between 2006 and 2012 bounced back from a modest drop in the second half of 2011 to increase 1.4% in Q1 2012 from the previous quarter.

The most notable statistic from 2012 is the seeming success of Singapore's efforts to reduce the number of foreign buyers in the market, with the number of units sold to foreign (non-permanent residents) buyers down a huge 76% in Q1 2012 from Q4 2011.

These huge price increases have had an obvious impact on affordability, and one of the most interesting developments in the coming months, will be how land policy is taken on by the new Chief Executive CY Leung (a qualified surveyor). With development land having been in such tight supply, he is known to want to remedy the affordability issue, with a potential increase in land to be available for residential projects in the New Territories. Although prime central markets are unlikely to be affected, the increase in supply could have a cooling effect on prices in the coming years.

Mixed fortunes across South East Asia

The narrative around Singapore has been an intriguing one. Record volumes of residential units were sold through the beginning of 2012, but average prices softened slightly through the first quarter of 2012. Looking more deeply into the numbers, the reality is that a number of newly launched mass market projects in the outer suburbs (OCR) have sold well, with volumes and prices down in the central regions.

Indonesia has certainly been South East Asia's star performer, with consistent price growth in all segments of the market, rising 3.6% annually and 0.8% quarterly. There is certainly a positive story around Indonesia, a trillion dollar economy (in purchasing power terms), with stable growth, manageable inflation, and an emerging middle class who wish to buy property.

Jakarta Cityscape
Warren Goldswain /Shutterstock

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In sharp contrast, Vietnam, which is still suffering from high inflation (although stabilising) and a lack of bank finance, continued to struggle, with buyers adopting a cautious *wait and see* approach, as developers become even more flexible with payment terms and provide increasingly significant discounts.

In Thailand, Knight Frank's exclusive condominium index saw prices increase 2.8% quarter on quarter and 5.4% year on year in Bangkok at Q1 2012. The city's condominium market saw huge amounts of supply come on line in 2010 and 2011 with a lot of stock in the peripheral areas. Demand has been notably concentrated in the city fringe, in areas such as Ratchadapisek Road, due to the prevalence of multinational companies

Expectations of a future cut by the central bank and a potential weakening of the dollar will be a further boost to the market and could provide an uptick in interest from foreign buyers looking at Australian property.

***"During the last year we witnessed high property prices, high interest rates and low sales. The price movement in the latest quarter suggests that the stalemate between developers and prospective buyers will break in favour of the latter,"* Dr Samantak Das, Head of Research for Knight Frank India**

moving to the area as well as the convenient public transportation links.

Property prices slide in India on the back of a stuttering economy

In India, with the rupee falling to record-lows and inflation stubbornly high, the housing market has been unable to benefit from a reduction in interest rates. In 10 of the 15 tracked city markets, prices dropped from the previous quarter, with Bangalore, India's fourth largest city notably seeing a steep 8% drop in Q1 2012.

Despite an annual price growth of 12% for the year to Q1 2012, Dr Samantak Das, Head of Research for Knight Frank India feels the Indian market could be turning. "During the last year we witnessed high property prices, high interest rates and low sales. The price movement in the latest quarter suggests that the stalemate between developers and prospective buyers will break in favour of the latter."

Sentiment remains weak in Australia despite rate cut

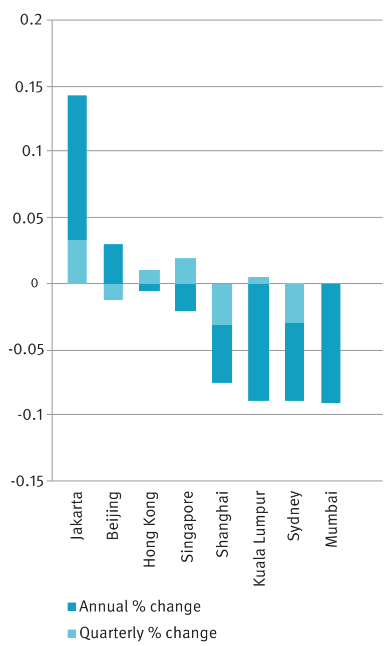
The recent 50 basis point interest rate cut brought some much-needed relief to the Australian housing market, which has seen average prices slip for the fifth consecutive quarter. Overall house prices have fallen 4.5% over the 12 months to Q1 2012, and although there were pockets performing well across the country, general sentiment remained weak. Expectations of a future cut by the central bank and a potential weakening of the dollar will be a further boost to the market and could provide an uptick in interest from foreign buyers looking at Australian property.

PRIME MARKET PERFORMANCE IN KEY ASIA PACIFIC CITIES

The prime residential markets (i.e. the top 5% of each city's respective housing stock) were subdued over the past year, with a number of key markets recording price falls. With cooling measures reducing second home ownership and weak sentiment, Asian high-net-worth-individuals were increasingly looking outside the region for safe havens for their capital.

Indonesia stood out with impressive double digit price increases, due to tight demand, rising incomes and steady confidence in the economy.

Figure 6
Prime Global Cities Index Q1 2012



Source: Knight Frank Research

ASIA PACIFIC OUTLOOK

Three important factors that will influence the region's property markets over the coming months:

- **World economic outlook**
  With the Eurozone crisis deepening, the world markets are watching intensely to see how this will be resolved. Asia Pacific is not insulated from this, with global trade a huge driver for GDP growth. A significant drop in Europe's GDP would have an effect on economies and consequently property markets in Asia Pacific.
- **China's economic performance**
  Excess savings in the Chinese economy have not only poured into property within China, but also around the region, helping fuel property booms abroad – the performance of the Chinese economy will therefore be a contributor to property market performance across the region.
- **Government intervention**
  Continued intervention across Asia Pacific to cool markets, reduce speculation or limit foreign buyers will continue to be an important factor in the region's property markets.

The **Chinese** market is expected to continue to soften, however if economic data indicates a significant weakening in the economy over the year, the central government could ease some measures to stimulate activity.

Similarly in **Malaysia**, expectations are for prices to remain steady over the coming months, with the possibility of a modest decline through the remainder of 2012.

In **Singapore**, given the large amount of supply coming onto the market, along with existing unsold inventories, prices of private residential properties are expected to continue to correct through 2012.

Indonesia is expected to continue to experience strong demand, although the effect of the new minimum down payment of 30% for mortgage loans from June 2012 could have an effect on performance, particularly in the middle to low end segments.

In **Thailand**, despite large amounts of supply, increasing labour, construction and land costs are being passed on from developers to purchasers, with modest price increases likely to continue through the year.

Vietnam, with inflation moderating, the market is looking at bottoming out and could see a pickup in activity if interest rates are able to be eased further.

In **Hong Kong**, buyers are expected to remain more reluctant to make purchase decisions, amid uncertainty in the world economy. House prices are expected to therefore soften during the year, but at a modest rate, given limited supply.

India is likely to continue to see an uneven year, with the cities that experience high levels of speculative demand likely to be more volatile than those based primarily on end user demand.

In **Australia**, with sentiment remaining weak, the market is hopefully looking to a further interest rate cut to potentially stimulate demand and bring about a pick-up in volumes and prices.

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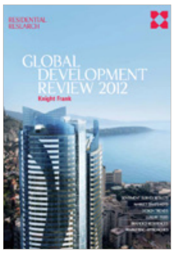
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