

PRIME OFFICE

Upcoming higher demand in decentralised areas

Hong Kong Island

The Grade-A office leasing market in Central was quiet in December, because of the traditional holiday season and the limited amount of space available for lease. Though rising slightly 0.2 percentage points month on month, the vacancy rate in Central remained low at 1.0%.

Despite weak business sentiment, there were some tenant replacement cases taking place. While some small-scale Mainland financial firms surrendered or downsized their offices, some multinational professional services companies expanded their presence in the city.

With a number of large tenants expected to move out of Central to decentralised areas in the coming 24 months, over 1 million sq ft of office space will be put up for lease. A leap in the vacancy rate will put downward pressure on rents in the area. However, a significant drop in rents in Central is unlikely, given the lack of supply and its advantages of being a prime location. Therefore, we expect only a slight downward rental adjustment especially for those premium Grade-A offices.

Kowloon

Following the standard year-end pattern, leasing activity in Kowloon has slowed down in December, with just around 70 major transactions recorded. Demand came mainly from the engineering and electronics sectors, which are the ones least impacted by the gloomy economic outlook so far.

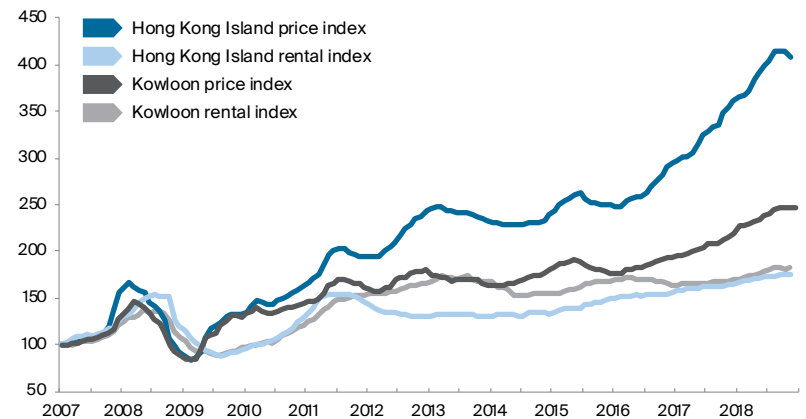
In other sectors, tenants are conservative with their real estate budgets. Most were looking for office space at mid to low rental level of less than HK\$33 per sq ft. This explains why office buildings at such rental bracket are getting absorbed very quickly. For example, the remaining whole floor on 12/F of KOHO in Kwun Tong has been leased out at about HK\$25.5 per sq ft. The nearby revitalised industrial building The Rays has also been fully leased within a few months' time.

Looking ahead, with the results of the China-US trade negotiations remaining uncertain, more companies are expected to move to smaller offices or buildings with lower rents in 2019 to reduce costs, thus benefiting most landlords in the decentralised areas.

FIGURE 1

Grade-A office prices and rents

2007 = 100



Source: Knight Frank Research

TABLE 1

Prime office market indicators (Dec 2018)

District	Net effective rent			Price (Gross)		
	HK\$ psf / mth	MoM %	YoY %	HK\$ psf	MoM %	YoY %
Premium Central	197.9	0.0	4.9	-	-	-
Traditional Central	146.2	0.0	10.7	-	-	-
Overall Central	163.7	0.0	8.2	44,563	0.0	12.0
Admiralty	116.4	0.0	3.8	38,607	0.0	17.6
Sheung Wan	85.3	0.0	6.1	35,356	0.0	15.6
Wan Chai	79.8	0.0	4.3	30,031	0.0	4.9
Causeway Bay	84.1	0.0	6.1	26,024	0.0	5.2
North Point	54.0	0.0	1.8	-	-	-
Quarry Bay	53.2	0.0	1.4	-	-	-
Tsim Sha Tsui	71.4	-0.1	12.3	18,944	0.0	18.1
Cheung Sha Wan	32.9	0.4	6.6	-	-	-
Hung Hom	43.8	0.7	2.0	-	-	-
Kowloon East	34.5	-1.9	0.7	13,533	0.0	3.8
Mong Kok / Yau Ma Tei	59.2	0.0	0.1	-	-	-

Source: Knight Frank Research

Note: Rents and prices are subject to revision.

RESIDENTIAL

Luxury homes stay resilient

The Hong Kong residential market reversed its uptrend since July 2018, with prices dropping over 7% from the peak, according to the Rating and Valuation Department. Average transaction volume decreased from over 5,700 per month in the first seven months to just 3,500 per month for the last five months of 2018.

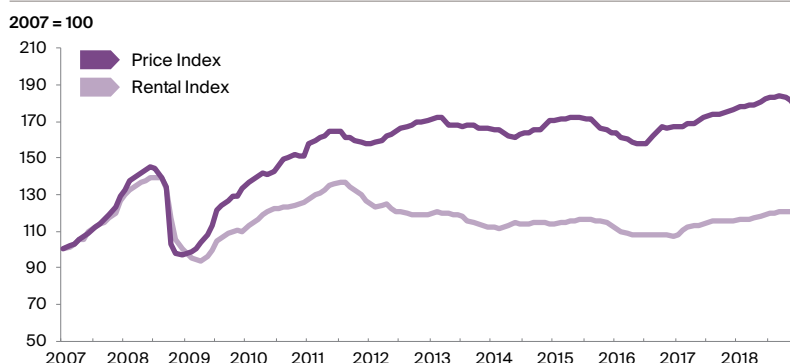
In December 2018, there are some notable residential sales with consideration of over HK\$75 million. For instance, two houses at 90 Repulse Bay Road were sold for HK\$520 million and HK\$490 million, or HK\$87,912 per sq ft and HK\$87,750 per sq ft, as reported by market news.

On the leasing front, housing allowances for expat executives in multinational companies have not been increased further. With more vacant luxury units in the market, some landlords are willing to compromise on rents and be more accommodating to tenant requirements.

With the prospect of the China-US trade talks remain unclear, market sentiment will remain weak. US interest rate hikes are expected to slow down in 2019 amid decelerating economic growth and mounting external uncertainties, easing upward pressure on Hong Kong interest rates. We expect the mass and luxury residential prices to drop up to 10% in 2019, but the decline in residential price to narrow later in the year.

FIGURE 2

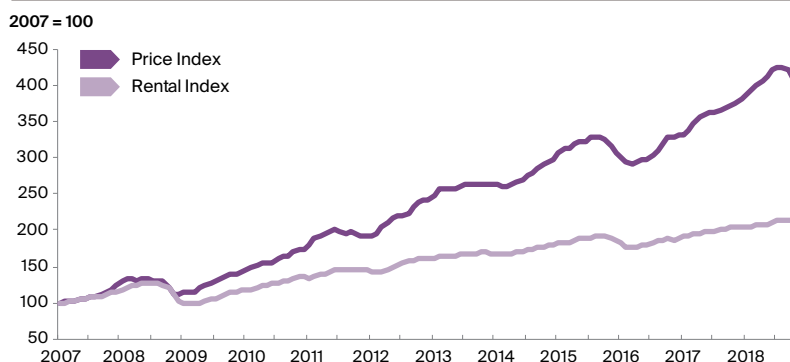
Luxury residential prices and rents



Source: Knight Frank Research

FIGURE 3

Mass residential prices and rents



Source: Knight Frank Research

TABLE 2

Selected residential sales transactions (Dec 2018)

District	Building	Tower / floor / unit	Saleable area (sq ft)	Price (HK\$ million)	Price (HK\$ per sq ft)
Southside	90 Repulse Bay Road	House	5,815	520	89,424
The Peak	Twelve Peak	House	3,657	458	125,239
Clear Water Bay	Serenity Point	House	2,692	188	69,837
Kowloon Tong	Mount Beacon	Tower 1, High floor A unit	2,361	111.3	47,141
Mid-Level Central	Garden Terrace	Tower 3, High floor B unit	2,943	100	33,979

Source: Knight Frank Research

Note: All transactions are subject to confirmation.

TABLE 3

Selected residential lease transactions (Dec 2018)

District	Building	Tower / floor / unit	Lettable area (sq ft)	Monthly rent (HK\$)	Monthly rent (HK\$ per sq ft)
Mid-Level West	39 Conduit Road	Mid floor / unit B	1,991	150,000	75
Island South	12 South Bay Road	House	3,236	185,000	57
Mid-Level West	The Belcher's	Tower 1 / high floor / unit G	2,692	130,000	48
Mid-Level East	Serenade	Tower 1 / high floor / unit A	1,990	95,000	48
Mid-Level Central	Tregunter	Tower 1 / low floor / unit A	2,559	105,000	41

Source: Knight Frank Research

Note: All transactions are subject to confirmation.

RETAIL

Record-breaking visitor arrivals brought a glimpse of hope for retailers

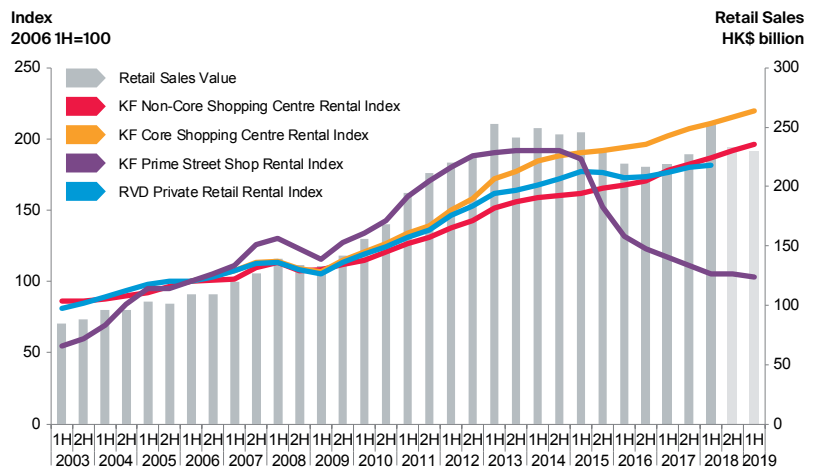
Hong Kong's retail sector is experiencing a slowdown, with total retail sales recording mild growth of 1.4% year on year in value and 1.2 % YoY in volume in November 2018, the slowest growth in 17 months. The sales value of three retail categories turned from positive growth to negative: "Clothing, footwear and allied products", "Consumer durable goods", and "Jewellery, watches and clocks, and valuable gifts". Growing economic uncertainties continued to be reflected in Hong Kong retail, while consumer sentiment was affected by weaker asset prices and external uncertainty. Nonetheless, the expected record-breaking tourism arrivals to Hong Kong to hit over 60 million in 2018 has become an impetus for retailers to put innovative retail strategies into action.

As for any new market, time is needed for the retail sector in Hong Kong to reap any concrete economic benefits from the Greater Bay Area development. Meanwhile, the overall slowdown of the economy in the region could also impact consumer spending.

We forecast that Hong Kong's slow retail market will persist in 2019 amid the softening residential market, volatile stock market and growing uncertainty over the outcome of the China-U.S. trade negotiations.

FIGURE 4

Retail sales and rents



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

TABLE 4

Retail sales by outlet type (Nov 2018)

Outlet	Value (HK\$ billion)	Share of total %	Change MoM %	Change QoQ %	Change YoY %
Jewellery, watches and clocks, and valuable gifts	5.9	15.0	-14.3	-21.4	-3.9
Clothing, footwear and allied products	4.8	12.1	0.7	7.9	-2.8
Department stores	5.6	14.2	33.8	34.4	3.9
Fuel	0.8	2.1	-10.0	-6.0	3.2
Food, alcoholic drinks and tobacco (excluding supermarkets)	3.6	9.1	-3.1	1.2	1.9
Consumer durable goods	6.7	17.0	-3.1	32.8	-2.1
Supermarkets	4.2	10.7	-6.0	-8.5	-0.1
Others	7.8	19.9	-3.7	-3.6	10.5
All retail outlets	39.2	100.0	-1.3	3.0	1.4

Source: Census and Statistics Department / Knight Frank Research

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