RESEARCH





MILD CORRECTION IN HOME PRICES

New policies were introduced by the State Council in mid April to rein in the overheated property market, marking the start of a new phase of macroeconomic control.

The drastic tightening measures implemented prevent mortgages from being granted to two groups of potential homebuyers in cities that have experienced rapid house-price increases. The first group is those who already own two residences, while the second is cross-city buyers who cannot provide proof of local social security contributions or tax payments for at least one year.

After the announcement, the residential market swiftly cooled and saw dramatic falls in transaction volumes. In China's first-tier cities—namely Beijing, Shanghai, Guangzhou and Shenzhen—the average daily sales area of new homes in May and June plunged 70%, 65%, 20% and 52% respectively, compared with April.

Amid tightened lending policies and shrinking sales volumes, home prices also began to edge down: by the end of July, secondary home prices in the first-tier cities dropped between 3% and



7% compared to prices recorded at the end of April. At the same time, the number of unsold, developer-owned homes began to rise after declining consistently for more than a year. Between the end of April and the end of June, the total area of unsold homes in Beijing, Shanghai, Guangzhou and Shenzhen rose 8%, 13%, 24% and 3% respectively. The rise was the smallest in Shenzhen, due to a lack of new supply during the period.

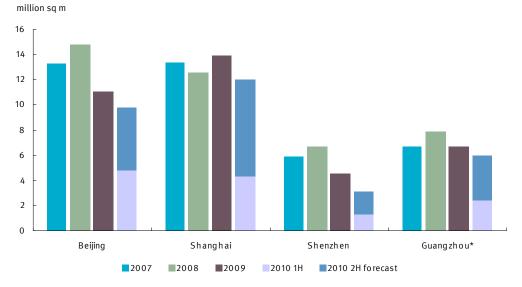
At the beginning of July, housing-market performance in the four key cities started to diverge. The monthly sales area of new homes in Beijing and Shanghai rebounded by about 30% and 4% compared with the previous month, while sales in Guangzhou and Shenzhen shrank by about 10% and 20%.

We believe the Mainland residential market in the second half of this year will be shaped by three key factors: the supply of new homes, government policies and the liquidity of real estate developers.

Because of the reduced number of housing projects that commenced in 2009, the supply of new homes in 2010 is expected to dip about 10% in Beijing, Shanghai and Guangzhou and as much as 30% in Shenzhen. Taking into account the new homes that already came onto the market, the gross area of new home supply in Beijing in the second half of the year is projected to be at a similar level as in the first half, while the new supply in Shanghai, Guangzhou and Shenzhen is expected to increase 77%, 49% and 46% respectively. Taking into consideration the impact of tightening measures and seasonal factors (home-sales volume is usually higher in the second half of year than in the first half), we can conclude that housing supply will remain balanced in Beijing in the second half of 2010, but Shanghai is likely to experience oversupply.

Figure 1

The area of primary residential properties newly launched



Note: * Guangzhou statistics cover ten districts but exclude Conghua and Zengcheng

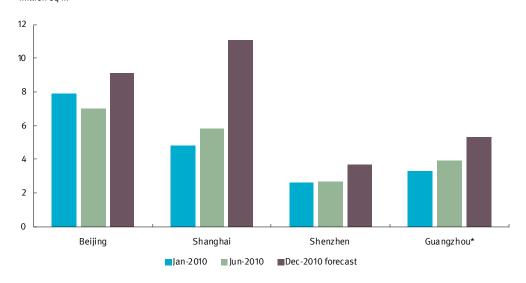
If home sales for the rest of the year remain at the same low levels of the past three months, the number of unsold, developer-owned homes in Shanghai will jump by a dramatic 90% between June and the end of the year, the sharpest rise among the four first-tier cities. Meanwhile,



inventory levels in Beijing, Guangzhou and Shenzhen are projected to rise by more moderate rates of 30%, 35% and 40% during the same period.

Figure 2

Total floor area of primary residential properties available for sale million so m



Note: * Guangzhou statistics cover ten districts but exclude Conghua and Zengcheng

On the policy front, the central bank has stated in its latest quarterly report that the European sovereign debt crisis will have limited impact on the Mainland economy. We also believe that the tightening measures recently implemented have yet to achieve the government's desired level of correction in the residential property market. Therefore, the Chinese authorities may not feel the need to support the overall economy through relaxing tightening policies aimed at combating property speculation.

Whether the central government will shift its monetary policy to a more hawkish mode will depend on whether home prices resume their uptrend. Financially weak real estate developers have already begun to offer price discounts to homebuyers. Most large developers have no cash-flow issues, but will be willing to make gestures of price reductions as a move to preempt further policy intervention from the authorities.

We believe the existing tightening measures will be maintained but only mild corrections in home prices are expected in China's key cities. With the housing market in balanced conditions, Beijing is likely to see further price decline of no more than 10% in the second half of the year. Shanghai faces abundant supply in the second half, but 76% of this new supply is located in the outer ring. Therefore, home prices in the inner ring of Shanghai will remain resilient, while prices in the outer ring will face greater downward pressure. The average home price in Shanghai is likely to dive an additional 15%. Meanwhile, in Guangzhou and Shenzhen, the average home prices are expected to dip another 10%.

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Table 1 Outlook (3Q 20	10)	
City	Price	Rental
Beijing	7	7
Guangzhou	7	¥
Shanghai	↔	7
Hong Kong	7	7

Figure 1 **Grade-A office price index**

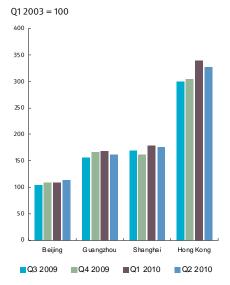
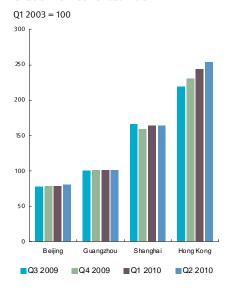


Figure 2 **Grade-A office rental index**



Prime office

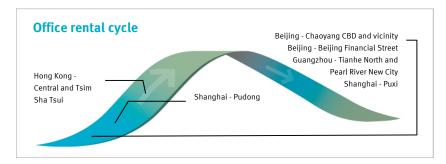


Table 2 Prices, ren t	tals, vacanc	y rates and yields [1][2	1	
City	Price (US\$ psm)	Rent (US\$ psm per month)	Vacancy rate	Yield
Beijing	\$ 3,524	\$ 28.3	17.8%	7.6%
Guangzhou	\$ 3,246	\$ 18.9	16.0%	6.1%
Shanghai	\$5,743	\$ 36.4	13.0%	7.5%
Hong Kong	\$16,198	\$ 49.8	3.9%	3.3%

Table 3 Supply and	d demand indicators	
City Beijing	 Indicators There was no new supply in Beijing's Grade-A office market in the quarter. Net take-up increased to 151,858 sq m. 	Several new office bulildings, located mainly in CBD and two other submarkets, may come onto the market in the second half of 2010. Leasing demand continued to improve.
Guangzhou	 About 300,000 sq m of new Grade-A offices have been added to the market in the quarter. Grade-A office transacted area surged 186% quarter on quarter. 	 A number of new Grade-A office buildings are scheduled for completion in the third quarter. Tightening policies targeting the residential sector as well as the poor performance in the financial markets pushed investors to the office sector.
Shanghai	The new Grade-A office spaces completed in both Puxi and Pudong were well received by the market.	The leasing market was robust with new projects recording satisfactory occupancy rates.
Hong Kong	Two Grade-A office buildings completed in non-core areas provided over 31,500 sq m of new office space.	sovereign debt crisis and a





Table 4 Major sales	transactions					
City	District	Development	Floor / Unit	Area (sq m)	Price (US\$ million)	Price (US\$ per sq m)
Beijing	Chaoyang	Prosper Center	N/A	2,401	\$14.1	\$5,889
Beijing	Chaoyang	Gongan Plaza	N/A	428	\$2.5	\$5,890
Guangzhou	Tianhe	R&F Yinxin	High floor unit	136	\$0.5	\$3,755
Guangzhou	Tianhe	CITIC Plaza	Mid floor unit	112	\$0.4	\$3,829
Shanghai	Pudong	Bank of East Asia Finance Tower	36/F unit	1,223	\$10.8	\$8,834
Shanghai	Jing'an	Haiyin International Tower	22/F unit	327	\$2.7	\$7,546
Hong Kong	North Point	Manulife Tower	En bloc	35,674	\$289.2	\$8,108
Hong Kong	Quarry Bay	Fortis Centre	En bloc	27,230	\$234.6	\$8,616

In the second half of the year, Beijing, Shanghai and Guangzhou are expected to see abundant new supply of Grade-A offices, which would boost vacancies and slow rental growth.

Table 5 Market activity					
	Sa	les	Leas	sing	
,	2Q 10 vs 1Q 10 3Q 10 Outlook 2Q 10 vs1Q 10 3Q				
Beijing					
Guangzhou	1				
Shanghai	1				
Hong Kong	+	(+	

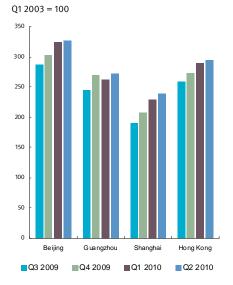
Table 6 Major leasi	ng transactions					
City	District	Development	Floor / Unit	Area (sq m)	Monthly Rental (US\$)	Monthly Rental (US\$ per sq m)
Beijing	Chaoyang	Office Park	23/F	2,500	\$69,947	\$28.0
Beijing	Chaoyang	Office Park	17/F	800	\$22,383	\$28.0
Guangzhou	Tianhe	China Shine Plaza	High floor unit	495	\$10,569	\$21.4
Guangzhou	Tianhe	CITIC Plaza	High floor unit	292	\$5,805	\$19.9
Shanghai	Changning	City Centre of Shanghai	Two floors	3,000	\$80,577	\$26.9
Shanghai	Jing'an	Plaza 66 II	High floor unit	500	\$26,411	\$52.8
Hong Kong	Kowloon Bay	Exchange Tower	9-11/F	7,432	N/A	N/A
Hong Kong	Central	One IFC	37-39/F	4,274	N/A	N/A

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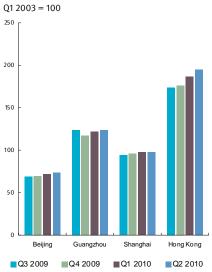
Quarterly

Table 7 Outlook (3Q 20	10)	
City	Price	Rental
Beijing	×	7
Guangzhou	×	7
Shanghai	×	7
Hong Kong	7	7

Figure 3 Luxury residental price index



Luxury residential rental index



Luxury residential

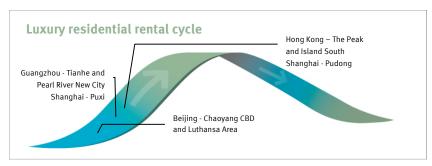


Table 8 Prices, rentals, vacancy rates and yields [1][2]					
City	Price (US\$ psm)	Rent (US\$ psm per month)	Vacancy rate	Yield	
Beijing	\$ 5,452	\$ 19.6	20.1%	3.6%	
Guangzhou	\$ 3,609	\$ 15.3	16.0%	4.5%	
Shanghai	\$ 7,283	\$ 22.5	19.0%	3.7%	
Hong Kong	\$ 25,733	\$ 60.7	11.2%[3]	2.7%	

- [1] Average prices and rentals are derived from different baskets of buildings, hence the two should not be used to
- estimate average yields.
 [2] Prices and rents are calculated on gross floor areas.
 [3] End-2009 vacancy rate of unites sized over 100 sq m from Rating and Valuation Department, HKSAR.

Table 9 Supply and	d demand indicators	
City	Indicators	Comments
Beijing	 Two new luxury residential projects were completed in the quarter, adding 468 units to the stock. 1,214 units were absorbed in the quarter, up 136.2% quarter on quarter. 	 New supply increased 15.8% quarter on quarter. Luxury residential leasing demand rose remarkbly with MNCs and overseas institutions beginning to increase their expatriate staff numbers.
Guangzhou	 The last phase of Moon Island, the only luxury project launched in the quarter, provided 13,000 sq m of new luxury homes to the market. Luxury residential sales in Guangzhou's core area plunged 42% in the second quarter. 	 The scarcity of luxury homes in Guangzhou's core area highlighted the prestigious status of such properties. The impact of tightening policies on Guangzhou's property market became apparent with luxury sales rapidly shrinking.
Shanghai	 In the leasing sector, Ascott Huaihai Road Shanghai with 278 units soft opened. In the sales sector, new supply plunged to the lowest level on record. Luxury home sales volume started to decrease, from 433 units in April to 142 in May and 136 in June. 	 The leasing market saw slight improvement. Investor sentiment was hurt by tightening policies.
Hong Kong	 Transactions of luxury homes worth HK\$10 million or above surged 12.6% to 2,000 units from the previous qaurter. 	The government's cooling measures affected market sentiment in April and May, but the market started to revive in June following encouranging land sale results.





Table 10 Major sales	transactions					
City	District	Development	Floor / Unit	Area (sq m)	Price (US\$ million)	Price (US\$ per sq m)
Beijing	Chaoyang	Pangu Plaza	N/A	619	\$9.0	\$14,573
Beijing	Chaoyang	Chang'an Avenue No 8	N/A	480	\$5.8	\$12,042
Guangzhou	Tianhe	Favorview Palace	Six-storey villa	728	\$4.7	\$6,449
Guangzhou	Tianhe	R & F International Garden	Mid floor unit	273	\$1.0	\$3,534
Shanghai	Pudong	Tomson Riviera	Tower 5 / 27/F / unit 3101	434	\$9.8	\$22,686
Shanghai	Luwan	Lakeville	Tower 1 / 2/F / unit 501	326	\$5.6	\$17,127
Hong Kong	The Peak	Peak Gardens	4/F / unit 16	152	\$6.1	\$40,080
Hong Kong	Island South	Grosvenor Place	17/F	261	\$8.8	\$33,893

In the second quarter, while mass residential prices fell in Beijing, Shanghai and Guangzhou, luxury residential prices bucked the trend with cash-rich homeowners withdrawing their properties from the market.

Table 11 Market activity					
	Sa	les	Leas	sing	
-	2Q 10 vs 1Q 10	3Q 10 Outlook	2Q 10 vs 1Q 10	3Q 10 Outlook	
Beijing					
Guangzhou	1	1	7		
Shanghai				\Leftrightarrow	
Hong Kong	7	\Leftrightarrow	7	\Leftrightarrow	

Table 12 Major leasi	ng transaction	s				
City	District	Development	Floor / Unit	Area (sq m)	Monthly Rental (US\$)	Monthly Rental (US\$ per sq m)
Beijing	Chaoyang	United Apartment US	21/F	236	\$3,534	\$15.0
Beijing	Chaoyang	Central Park	Tower 13 / 21/F	138	\$2,798	\$20.3
Guangzhou	Haizhu	Poly Cambridge	Low floor unit	259	\$1,914	\$7.4
Guangzhou	Tianhe	The Castle Peak	Low floor unit	124	\$1,318	\$10.6
Shanghai	Pudong	Lanson Place Jinqiao Residence	Unit 1002A	81	\$2,209	\$27.3
Shanghai	Xuhui	Shama Xujiahui	Unit 12	110	\$2,651	\$24.1
Hong Kong	Island South	56 Repulse Bay Road	Duplex (with terrace)	385	\$35,997	\$93.5
Hong Kong	The Peak	9 Coombe Road	House	307	\$25,712	\$83.9

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Quarterly

Table 13 Outlook (3Q 20	10)	
City	Price	Rental
Beijing	N/A	7
Guangzhou	7	\leftrightarrow
Shanghai	7	7
Hong Kong	7	7

Figure 5 Prime retail price index

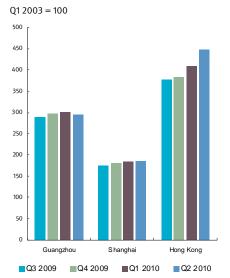
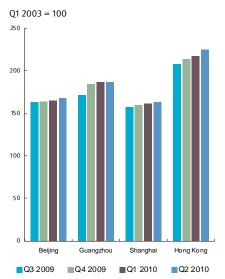


Figure 6 Prime retail rental index



Prime retail

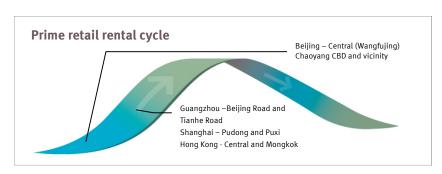


Table 14 Prices, rentals, vacancy rates and yields [1][2]					
City	Price (US\$ psm)	Rent (US\$ psm per month)	Vacancy rate	Yield	
Beijing	N/A	\$ 97.1	10.1%	5.5%	
Guangzhou	\$ 27,217	\$203.8	5.0%	7.3%	
Shanghai	\$ 15,895	\$ 115.9	6.0%	7.0%	
Hong Kong	\$ 187,291	\$ 553.6	8.7%[3]	3.6%[4]	
[1] Average prices and rentals are derived from different baskets of huildings, hence the two should not be used to					

- [1] Average prices and rentals are derived from different baskets of buildings, hence the two should not be used to [2] Prices and rents are calculated on gross floor areas.
 [3] End-2009 overall vacancy rate from Rating and Valuation Department, HKSAR.
 [4] Overall yield from Rating and Valuation Department, HKSAR.

Table 15 Supply and demand indicators						
City	Indicators	Comments				
Beijing	 Cuiweilu Capital Mall and Chaoyang JoyCity opened in the quarter. 	The two malls added 56,000 and 230,000 sq m of space to the prime retail market.				
Guangzhou	 The transacted area of retail space grew 10% quarter on quarter. 	 Abundant high-end retail supply will hit the market in the second half of the year before the launch of the Asian Games. 				
		New shopping centres are inviting quality brands to enter their malls before the Asian Games.				
Shanghai	 Retail supply reached 265,000 sq m with new malls opening in Luwan, Putuo, Pudong and Huangpu. 					
	• The retail market was active.	• The World Expo boosted local consumption.				
Hong Kong	 The One, a 29-storey ginza-type new shopping centre in Tsim Sha Tsui, will provide over 37,000 sq m of new retail space within the year. 	 The government's cooling measures to curb the overheated residential market lured some investors to shift to the retail property market. 				



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Table 16 Major sales transactions							
City	District	Development	Floor / Unit	Area (sq m)	Price (US\$ million)	Price (US\$ per sq m)	
Beijing	Chaoyang	Chang'an Avenue No 8	N/A	1,543	\$18.2	\$11,778	
Beijing	Chaoyang	KUN LUN Apartmen	N/A	260	\$4.3	\$16,708	
Guangzhou	Yuexiu	North Beijing Road	En bloc	450	\$1.9	\$4,254	
Shanghai	Baoshan	Star Moon International Plaza	1/F / unit 52	58	\$0.4	\$6,079	
Shanghai	Jiading	Fine World Business Plaza	1/F / unit 7	98	\$0.4	\$4,540	
Hong Kong	Causeway Bay	13 Pak Sha Road	G/F	93	\$20.6	\$221,410	
Hong Kong	Central	Tak Wo House	G/F / units 1-1A	139	\$17.9	\$128,400	
Hong Kong	Tsim Sha Tsui	National Court	G/F / units 3-5	167	\$18.6	\$111,475	

In Guangzhou, the continual openings of high-end shopping centres will usher in more international brands, uplifting the standard of the city's retail market.

Table 17 Market activity						
	Sa	les	Leas	ing		
	2Q 10 vs 1Q 10	3Q 10 Outlook	2Q 10 vs 1Q 10	3Q 10 Outlook		
Beijing						
Guangzhou	7	—	7	7		
Shanghai		\Leftrightarrow	7	7		
Hong Kong	7		7	7		

Table 18 Major leasi	ng transactions					
City	District	Development	Floor / Unit	Area (sq m)	Monthly Rental (US\$)	Monthly Rental (US\$ per sq m)
Beijing	Chaoyang	Waingjing NOVO	B1/F	280	\$6,185	\$22.1
Beijing	Fengtai	CAH Grand Canyon	1-2/F	1,800	7% of turnover	N/A
Guangzhou	Tianhe	Park Royal	G/F unit	89	\$6,553	\$73.6
Shanghai	Jing'an	In Point	1/F unit	81	\$8,702	\$107.4
Shanghai	Pudong	96 Plaza	1/F unit	239	\$10,164	\$42.5
Hong Kong	Tsim Sha Tsui	Majestic House	G/F / unit C	20 [5]	\$32,140	\$1,609.1
Hong Kong	Causeway Bay	Plaza 2000	G/F / units 5-6	20 [5]	\$23,141	\$1,158.5
Hong Kong	Tsim Sha Tsui	Manley House	G/F / unit 6	88	\$67,622	\$764.6
[5] saleable area	a					

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