



AUGUST 2011

HONG KONG
PRIME OFFICE

Monthly Report

Knight Frank 萊坊

LEASING ACTIVITY ROBUST DESPITE VOLITILITY

Sentiment in the office sales market weakened over the past month. The slowdown was triggered by a number of factors, including buyers' resistance to Grade-A office prices that had surged 23.7% over the past seven months; the fear of a double-dip recession in the US economy as well as volatility in the global stock market. About 250 office sales transactions were recorded in July, a drop of about 30% from the previous month and the lowest level since January this year.

Despite the fall in transaction volume, the market continued to see landmark deals. A local investor sold his 2,480-sq-ft mid-floor unit in Shun Tak Centre West Wing, Sheung Wan for HK\$60.5 million or HK\$24,395 per sq ft—a record-high price per sq ft for the building—after buying the unit for HK\$21,800 per sq ft in late June. A high-floor unit in Convention Plaza Office Tower, Wan Chai reportedly changed hands for HK\$41.8 million, setting a new price-high of HK\$25,578 per sq ft for the building.

The growth in Grade-A office prices slowed during July, compared with an average monthly growth of 3.8% recorded in the first half of the year. Prices edged up a mere 0.5% last month, the smallest gain since June 2010. Tsim Sha Tsui led the market with prices there rising 1.9% in July, while prices in major business districts on Hong Kong Island, such as Admiralty, Central and Sheung Wan, remained stable.

In contrast to the sales market, the Grade-A office rental market saw transaction volume pick up last month despite volatility in the global stock markets, thanks to sustained demand and stabilising rental growth. Relocation activity was robust: an international insurance firm moved from Central to three floors totaling 52,800 sq ft in Times Square Tower One, Causeway Bay, while Intel relocated from Admiralty to a whole floor measuring 21,000 sq ft in Central Plaza, Wan Chai. The market also saw expansion activity during the month. An example involved international auction house Sotheby's absorption of an additional office floor in One Pacific Place in Admiralty, totaling 16,800 sq ft.

Business space in Central continued to be sought after, despite an uncertain global economic outlook. A high-floor unit in Two IFC, totaling 3,700 sq ft, was leased to a financial institution for HK\$195 per sq ft per month. This represents the highest office rent achieved in Hong Kong since mid-2008. Meanwhile, China Trust Commercial bank took up seven mid-floor units totaling 10,000 sq ft in the same building and a number of units in St. George's Building were also reportedly taken up at around HK\$115 per sq ft per month.

Grade-A office rents remained relatively stable during the month, after surging 21.4% in the first six months of 2011. Rents in many of Hong Kong's major business districts, including Quarry Bay, Wan Chai, Causeway Bay and Kowloon East, were well above their 2008 peaks. Rents in Central were about 2.3% below their 2008 peak, while those in Admiralty were also very close to their previous high.

We believe demand for local office space would remain positive for the rest of the year. Asia is a major source of growth for many international corporations that wish to capitalise on the opportunities arising from China's steady economic progress and favour Hong Kong as their base of expansion into the Mainland. However, as the global economic outlook looks uncertain, the pace of local office rental growth for the rest of the year would slow, especially as office rents had soared 21.9% in the past seven months. We have revised down our previous forecast and expect Hong Kong's Grade-A office rents to grow about 25% over 2011. Rental growth in Causeway Bay and Wan Chai would lead the market, while rents in Central—where a number of large offices would be vacated over the next few months—should remain stable for the rest of the year.



Prime office report

Hong Kong's economy grew more slowly in the second quarter, due to a sharp deceleration in exports.

Table 1 Economic indicators and forecasts					
Economic indicator	Period	Latest reading	2009	2010	2011 forecast
GDP growth	Q2 2011	+5.1%#	-2.7%	+6.8%	+5.5%
Inflation rate	June 2011	+5.6%	+0.5%	+2.4%	+5.4%
Unemployment	Three months to June 2011	3.5%#	5.4%	4.4%	4.3%
Prime lending rate	Current	5.00–5.25%	5.0%*	5.0%*	5.0%*

Source: EIU CountryData / Census & Statistics Department / Knight Frank
Provisional * HSBC prime lending rate

The Grade-A office rental market saw transaction volume pick up over the past month.

Table 2 Selected office leasing transactions				
District	Building	Tower / floor / unit	Area (sq ft)	Tenant
Admiralty	One Pacific Place	5 th floor	16,800	Sotheby's
Causeway Bay	The Lee Gardens	18 th floor	15,800	Willis Hong Kong
Causeway Bay	Times Square	Tower One / 27-28 th floors, parts of 32 nd and 39 th floors	52,800	Aon Hong Kong
Central	Two IFC	21 st floor / units 4-10	10,100	China Trust Commercial Bank
Wan Chai	Central Plaza	69 th floor	21,000	Intel

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



Despite the fall in transaction volume, the sales market continued to see landmark deals.

District	Building	Tower / floor / unit	Area (sq ft)	Price (HK\$M)	Price (HK\$psf)
Sheung Wan	Shun Tak Centre West Wing	21 st floor / unit 11	2,480	\$60.5	\$24,395
Central	World-Wide House	8 th floor / units 5A–6	3,351	\$63.67	\$19,000
Admiralty	Lippo Centre	Tower 2 / 38 th floor / units 2–11	12,265 (net)	\$222	\$18,100
Wan Chai	Convention Plaza Office Tower	49 th floor / unit 5	1,635	\$41.82	\$25,500
Wan Chai	Bank of East Asia Harbour View Centre	15 th floor / unit 2	1,672	\$24.55	\$14,682
Tsim Sha Tsui	Silvercord	Tower 1 / low floor / unit 3	1,424	\$20.2	\$14,185

Source: Economic Property Research Centre / Knight Frank
Note: All transactions are subject to confirmation.

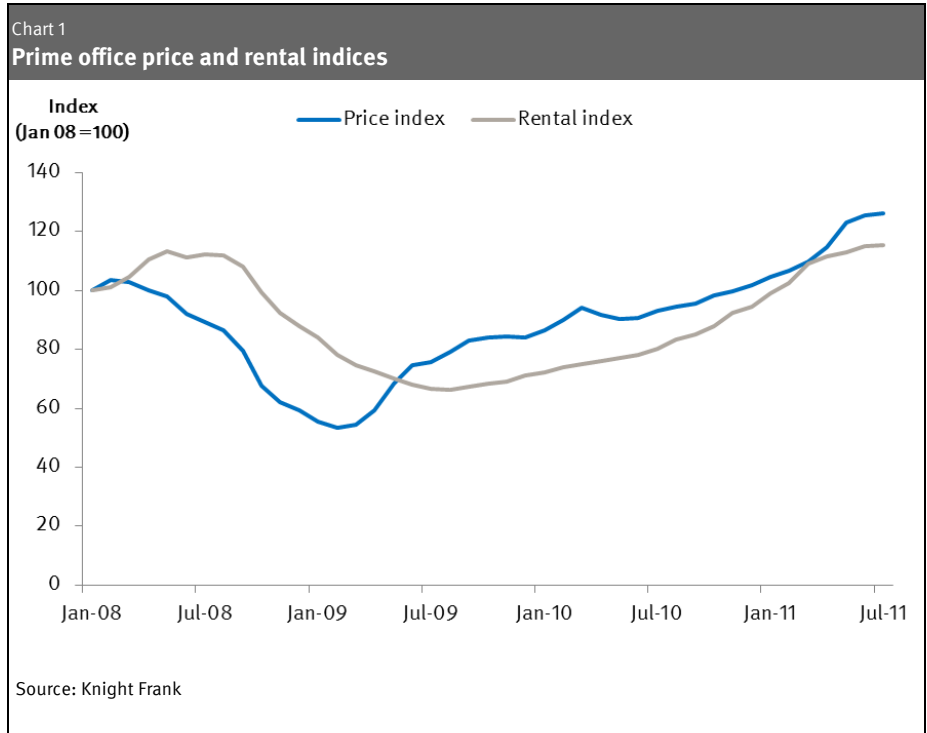
Both Grade-A office prices and rents remained relatively stable during the past month.

District	Net effective rent		Change		Price		Change	
	HK\$psf /mth	From Jun 11	From Apr 11	From Jul 10	HK\$psf	From Jun 11	From Apr 11	From Jul 10
Premium Central	182.1	0.0%	0.8%	31.7%	n/a	n/a	n/a	n/a
Traditional Central	137.6	0.0%	3.1%	56.4%	24,659	0.0%	5.5%	52.2%
Admiralty	91.3	0.0%	2.0%	41.0%	19,023	0.6%	10.7%	38.0%
Sheung Wan	61.5	0.0%	1.7%	31.7%	16,709	0.0%	12.9%	27.9%
Wan Chai	63.9	0.0%	4.7%	50.2%	14,216	0.4%	8.7%	39.1%
Causeway Bay	62.6	1.0%	3.0%	53.9%	14,840	0.0%	8.4%	41.7%
North Point	35.5	0.0%	3.4%	47.9%	n/a	n/a	n/a	n/a
Quarry Bay	48.3	0.0%	0.0%	40.2%	n/a	n/a	n/a	n/a
Tsim Sha Tsui	46.5	2.0%	7.7%	38.7%	11,397	1.9%	9.0%	24.7%
Cheung Sha Wan	21.0	0.0%	4.5%	16.8%	n/a	n/a	n/a	n/a
Hung Hom	28.0	1.2%	10.2%	21.3%	n/a	n/a	n/a	n/a
Kowloon East	30.9	1.7%	8.5%	46.5%	n/a	n/a	n/a	n/a
Mong Kok / Yau Ma Tei	49.0	0.0%	9.2%	36.2%	n/a	n/a	n/a	n/a

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



We have revised down our previous forecast and expect Hong Kong's Grade-A office rents to grow about 25% over 2011.



Even if the global economic outlook turns sour, we believe this could only temper the pace of office rental growth in Hong Kong.



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