

OFFICE

Leasing momentum softening as social unrest starts to bite

Hong Kong Island

Leasing momentum of Grade-A office space slowed considerably in July. Under the combined effects of the trade war and social unrest, some companies have adopted a “wait and see” attitude while we witnessed several lease dispositions happening in the market. With tenants being generally cautious on the market outlook, downsizing and cost savings exercises are likely in the coming months.

In Central, some landlords are taking a pro-active approach to lock in major occupiers in response to the on-going decentralization trend. Coupled with the foreseeable rise in vacancies in the coming months, many landlords are trying to secure long-term deals by providing occupiers with special offers.

Under the impact of external and local uncertainties, overall leasing momentum on the Hong Kong Island is expected to continue to soften in the short term. We also expect a correction of rents in Central due to the foreseeable increase in vacancy. Meanwhile, non-CBD districts will be less impacted as the absorption remains relatively strong.

Kowloon

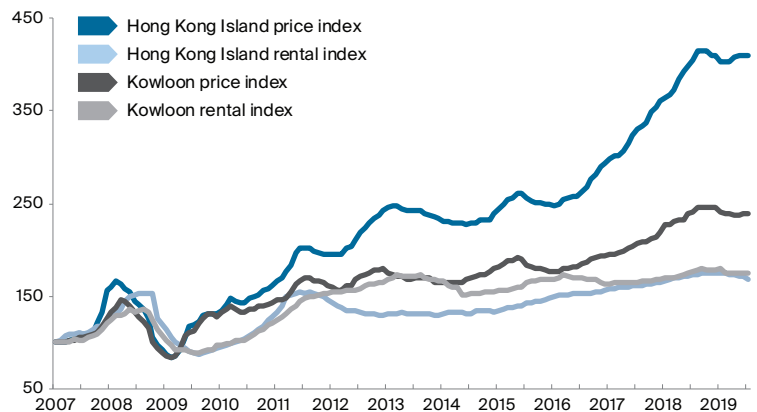
Leasing demand for Grade-A office space in Kowloon softened in July because of market uncertainty. Most of the deals were small to mid-sized and in buildings with low rents. Some tenants tightened their budgets and looked for revitalised buildings with a rent of less than HK\$20 per sq ft per month.

Despite weakening momentum, co-working space operators continued their expansion plans. WeWork rented the 20/F and 21/F in Harbourside HQ (previously called Octa Tower), with a total area of 47,600 sq ft, for HK\$25.5 per sq ft per month.

Softening demand is expected to persist in August. In the longer term, office market performance will still depend on economic and trade conditions.

FIGURE 1
Grade-A office prices and rents

2007 = 100



Source: Knight Frank Research

TABLE 1
Grade-A office market indicators (July 2019)

District	Net effective rent			Price (Gross)		
	HK\$ psf / mth	MoM %	YoY %	HK\$ psf	MoM %	YoY %
Premium Central	189.7	0.0	-4.5	-	-	-
Traditional Central	139.3	-3.3	-1.9	-	-	-
Overall Central	156.4	-2.0	-3.0	43,907	0.0	-3.2
Admiralty	110.1	-4.3	-5.3	39,184	0.0	5.4
Sheung Wan	83.7	-1.6	-1.8	34,341	0.0	-4.8
Wan Chai	77.7	-1.0	-2.5	30,476	0.0	2.3
Causeway Bay	79.6	-0.4	-4.8	26,479	0.3	2.9
North Point	51.8	0.0	-4.3	-	-	-
Quarry Bay	55.6	0.8	4.5	-	-	-
Tsim Sha Tsui	72.2	0.0	2.4	18,262	0.0	-1.2
Cheung Sha Wan	33.3	0.0	2.6	-	-	-
Hung Hom	44.5	0.2	-1.4	-	-	-
Kowloon East	31.3	-2.3	-4.3	13,243	-0.5	-1.0
Mong Kok / Yau Ma Tei	59.8	-0.4	1.4	-	-	-

Source: Knight Frank Research

Note: Rents and prices are subject to revision.

RESIDENTIAL

Prolonged protests prompting concern about an extended price correction

Overall Hong Kong residential prices dropped for the first time in 2019, down 0.8% month on month in June, according to the latest official data. Despite the US interest rate cut, weakening confidence in the market has led to property owners slashing prices, particularly for secondary homes.

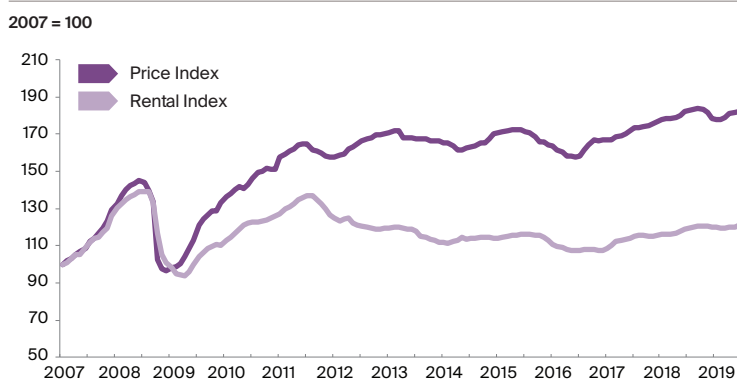
Monthly residential sales volume remained below 5,000 units for the second consecutive month, down 21% YoY to 4,805 units. The recent social upheaval has drained the appetite of potential buyers to enter the market, especially in the residential areas where the violent events have occurred.

There were forfeitures of preliminary deposits involving large sums recently. In Mount Vienna in Shatin, the transaction of a duplex unit was reportedly cancelled, with the buyer forfeiting a deposit of HK\$4.72 million. Another buyer left the market, forfeiting a deposit of about HK\$2 million at Park Yoho Napoli in Yuen Long.

The largest residential plot offered in Kai Tak, Area 4A, Site 1, was recently sold at an accommodation value of HK\$11,842 per sq ft, down 13.6% compared to that of the adjacent plot sold in March 2019. This unit price is the lowest ever tendered for any residential plot on the former airport runway. Developers are increasingly prudent in acquiring land that involves high upfront capital investment.

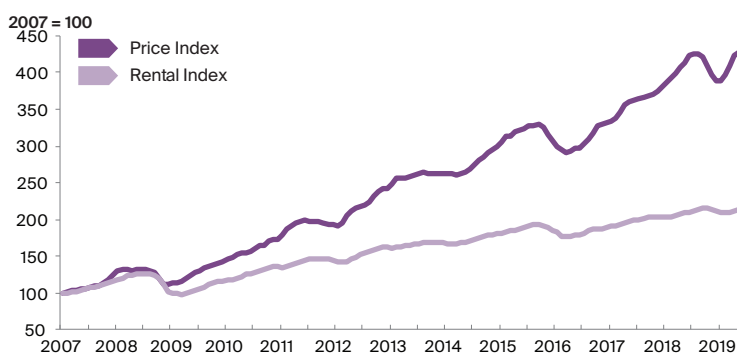
The housing market is expected to remain volatile amid deteriorating market sentiment. We expect mass residential prices to drop by 5% in 2H 2019, but the luxury residential market should remain relatively stable. Meanwhile, government tender sites continue to attract interests from developers reflecting a certain level of medium to long term confidence.

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 (July 2019)

District	Building	Tower / floor / unit	Saleable area (sq ft)	Price (HK\$ million)	Price (HK\$ per sq ft)
Mid-Levels Central	Chung Tak Mansion	Low floor	2,550	325.6	127,686
The Peak	Mount Nicholson	Apartment	4,596	455	99,000
Island South	90 Repulse Bay Road	House	5,672	489.2	86,240
Tin Hau	The Pavilia Hill	Duplex unit	2,835	156	55,026
Island South	Leighton Hill	Tower 7 / high floor / unit A+B	2,922	130	44,490

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

TABLE 3
Selected residential lease transactions (July 2019)

District	Building	Tower / floor / unit	Lettable area (sq ft)	Monthly rent (HK\$)	Monthly rent (HK\$ per sq ft)
Island South	Bel-Air Phase 5	House	3,592	300,000	84
Island South	The Lily	Tower 1 / high floor / unit A	1,388	110,000	79
Mid-Levels West	Arezzo	High floor / unit A	1,309	100,000	76
Island South	Stanley Green	Lower floor / unit B	1,836	100,000	54
Mid-Levels Central	May Tower II	Low floor	2,669	108,000	40

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

RETAIL

Retailers seeking rental cuts amid socioeconomic instability

The impact of the Sino-US trade war on the Hong Kong retail market has been felt since June. Coupled with the worsening social turbulence, the latest monthly retail sales value for June dropped by 6.7% YoY, highlighted by a 17.1% decline in luxury retail sales, according to official data.

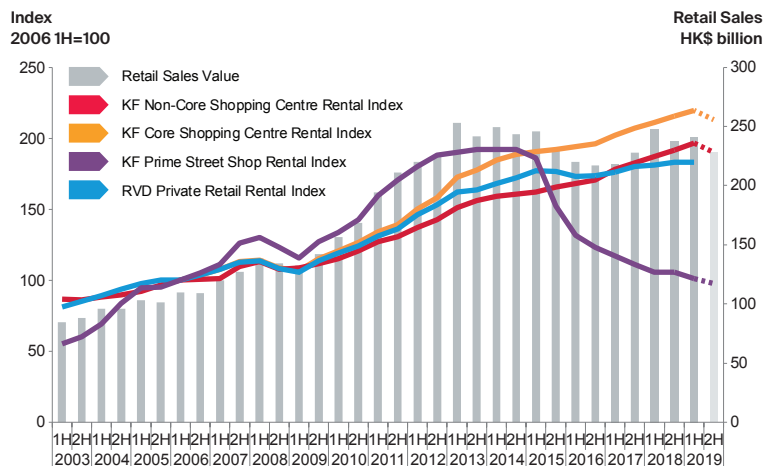
Italian luxury brand PRADA released its interim financial results, which showed a 5.1% YoY decrease in net sales performance in Greater China at a constant exchange rate in 1H 2019, as a result of social unrest in Hong Kong and unfavourable fluctuation of the renminbi. According to news reports, PRADA is considering surrendering its existing lease on Russell Street in Causeway Bay, which involves a total area of 15,000 sq ft, with a current monthly rent of HK\$9 million. In addition, Korean fast-fashion brand SPAO has announced that it will shut down its Hong Kong branch. Meanwhile, UK fashion chain Jack Wills, which has been under administration and sold to Sports Direct, will retreat from the city.

The restaurant sector has seen the worst performance in 10 years. The value of restaurant receipts and purchases dipped by 0.4% YoY in Q2 2019, the first fall since Q3 2009, according to provisional official data.

Deteriorating business prospects have driven retailers to negotiate rental reductions with landlords. To support existing tenants, shopping mall D2 Place in Cheung Sha Wan has offered a one-off rental subsidy equivalent to 20% of one month's rent.

Consumer confidence should remain weak in the short term amid continuing social tension and the worsening economic outlook. We expect retail rents in prime streets, especially Central, to fall up to 10% for the whole year.

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 (June 2019)

Outlet	Value (HK\$ billion)	Share of total %	Change MoM %	Change QoQ %	Change YoY %
Jewellery, watches and clocks, and valuable gifts	5.8	16.3	-13.9	-13.9	-17.1
Clothing, footwear and allied products	4.4	12.4	-11.4	-18.4	-7.1
Department stores	3.6	10.2	-37.9	-14.9	-6.0
Fuel	0.9	2.6	3.8	8.6	1.9
Food, alcoholic drinks and tobacco (excluding supermarkets)	3.2	9.1	-7.6	-6.4	-1.3
Consumer durable goods	4.7	13.3	-1.9	-18.1	-11.9
Supermarkets	4.5	12.7	0.8	0.6	1.6
Others	8.2	23.4	-8.4	-8.9	-2.5
All retail outlets	35.2	100.0	-11.8	-11.4	-6.7

Source: Census and Statistics Department / Knight Frank Research

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