

OFFICE

Sentiment wavers but no sign of retreating from HK

Hong Kong Island

As the Grade-A office market continued to be hit by the volatile and uncertain market conditions, overall rent on Hong Kong Island dropped 10.6% from January to November this year.

As cautious sentiment prevails, many tenants have placed emphasis on cost saving. While some tenants have moved to buildings in the same district but with lower rents, others have relocated to non-core areas. In the past two to three months, we have seen many tenants reduce their lease area by 20–30%. Although some companies are downsizing, we do not see them retreating from Hong Kong, since they see Hong Kong's position as an international financial centre in Asia not easily replaced by other markets. Meanwhile, a small number of premium Grade-A office buildings reported lease surrenders, leading to some supply re-entering the market.

Although the market continues to face rising uncertainty, we have noticed that firms are accepting and adapting to Hong Kong's new market norm. Therefore, a significant drop in rents is unlikely, but we expect overall Hong Kong Island rents to decline 6–8% next year.

Kowloon

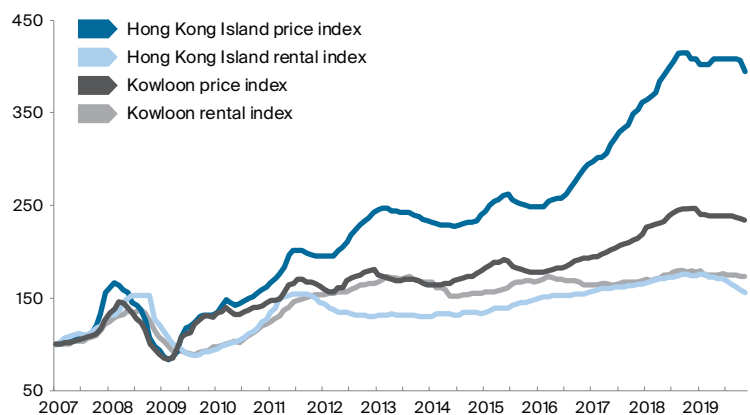
Leasing activity was slow in November, with most tenants preferring lease renewals rather than relocation. Most leasing transactions were recorded in Kwun Tong and Kowloon Bay, for areas of less than 3,000 sq ft. Demand was mainly from decentralisation and downsizing, but there was also activity from new companies seeking space at low rents in a downbeat market.

One of the significant decentralisation cases was the relocation of FWD Insurance from Hong Kong Island to Kwun Tong. The company rented about 30,000 sq ft in Millennium City 1 Tower 1 for HK\$30.5 per sq ft per month.

We expect office supply to spike in 2020, mainly because new offices in 2019 have not yet been fully absorbed, and there is additional supply from lease disposition cases. Coupled with softening demand, we expect office rents in Kowloon to drop by 2–4% next year.

FIGURE 1
Grade-A office prices and rents

2007 = 100



Source: Knight Frank Research

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

District	Net effective rent			Price (Gross)		
	HK\$ psf / mth	MoM %	YoY %	HK\$ psf	MoM %	YoY %
Premium Central	162.7	-3.3	-17.8	-	-	-
Traditional Central	131.5	-1.1	-10.1	-	-	-
Overall Central	142.0	-1.9	-13.2	42,676	0.0	-4.2
Admiralty	97.8	-2.3	-15.9	37,189	-5.1	-3.7
Sheung Wan	82.4	0.0	-3.5	33,860	0.0	-4.2
Wan Chai	74.4	-1.2	-6.8	29,264	-4.0	-2.6
Causeway Bay	77.7	0.0	-7.5	26,249	-0.6	0.9
North Point	49.5	0.0	-8.2	-	-	-
Quarry Bay	54.5	0.0	2.4	-	-	-
Tsim Sha Tsui	70.7	-0.3	-1.1	17,983	0.0	-5.1
Cheung Sha Wan	33.0	0.5	0.6	-	-	-
Hung Hom	45.7	3.9	5.2	-	-	-
Kowloon East	31.6	0.0	-4.6	13,025	-0.4	-3.8
Mong Kok / Yau Ma Tei	60.1	0.0	1.5	-	-	-

Source: Knight Frank Research

Note: Rents and prices are subject to revision.

RESIDENTIAL

Transaction increases despite a downbeat market

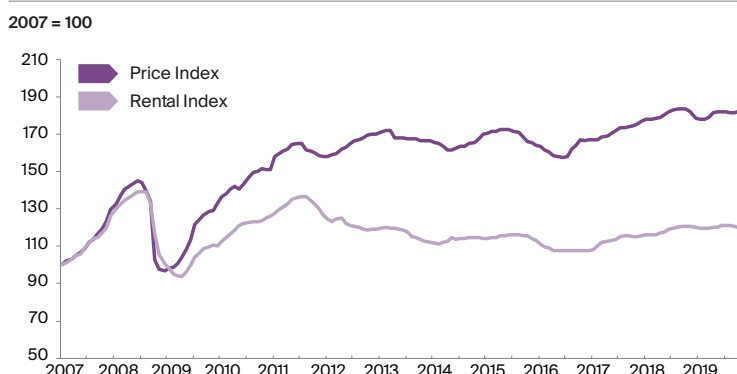
In November, Hong Kong's residential market was lifted by the government's relaxation of the mortgage cap for first-time buyers. According to the Land Registry, November sales reversed five months of declines, surging 43.9% MoM to 5,756 units.

Although Hong Kong's one-month interbank rate rose to 2.53% in November from an average of 1.72% in October, the borrowing cost is still relatively low from a long-term perspective. The lower down-payment requirement under the new mortgage rules enables more potential buyers to get on the property ladder. Given the new mortgage rules, we expect properties worth between HK\$6 and \$8 million to drive demand, boosting transaction volume by as much as 20–30% in the next three to four months.

In the leasing market, there was ample supply of leasing units owing to a number of newly completed projects, including Cullinan West II and Ocean Pride, which placed downward pressure on rents. To attract more tenants, landlords were more flexible and were willing to offer short-term leases. For instance, the minimum leasing term at Townplace Kennedy Town was shortened to one month, compared to two months previously.

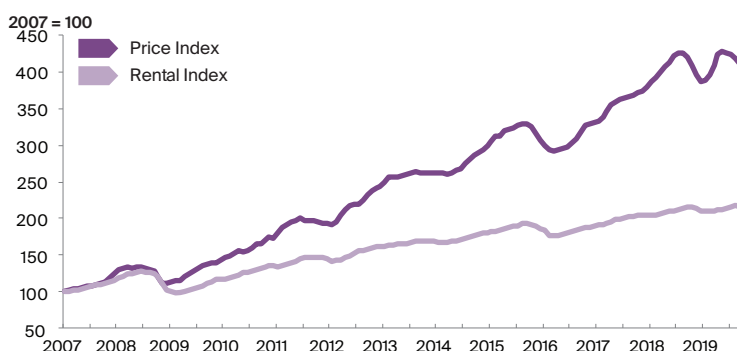
Looking ahead, against the backdrop of an economic recession and unresolved social unrest, we expect mass residential home prices to drop by 5–10% in 2020 and the luxury segment to have a minor correction.

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 (Nov 2019)

District	Building	Tower / floor / unit	Saleable area (sq ft)	Price (HK\$ million)	Price (HK\$ per sq ft)
Ho Man Tin	Ultima	Tower 3 / duplex unit C	2,090	125.4	60,000
Tsim Sha Tsui	Masterpiece	Duplex unit	1,974	108.8	55,117
Mid-Levels Central	Estoril Court	High floor / unit D	2,888	140	48,476
Aberdeen	Larvotto	High floor / unit A	2,608	110	42,178
Kowloon Tong	62 Begonia Road	House	3,273	128	39,108

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

TABLE 3
Selected residential lease transactions (Nov 2019)

District	Building	Tower / floor / unit	Lettable area (sq ft)	Monthly rent (HK\$)	Monthly rent (HK\$ per sq ft)
Mid-Levels Central	Dynasty Court	Tower 1 / high floor / unit B	1,548	107,500	69
Mid-Levels West	Azura	High floor / unit B	1,589	108,000	68
Island South	The Lily	Tower 3 / low floor	2,534	165,000	65
Island South	12 Shouson Hill Road	House	3,559	151,000	42
Island South	12A South Bay Road	House	3,084	110,100	36

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

RETAIL

Social unrest fostered sales of community shops

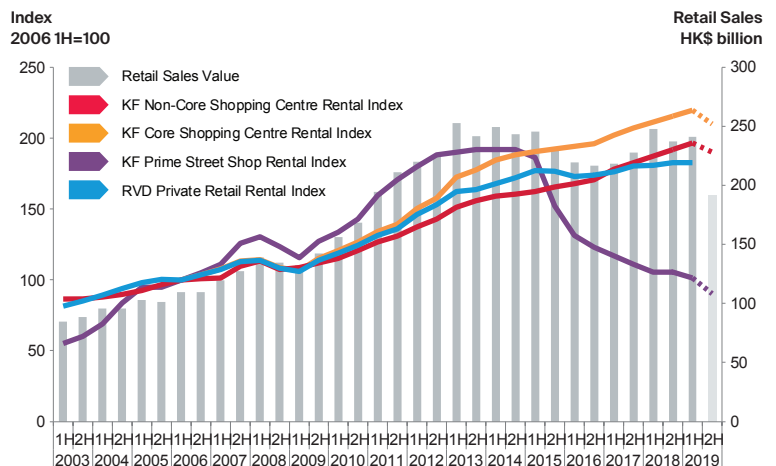
The ongoing social unrest, coupled with poor macro-economic conditions, have dealt a heavy blow to Hong Kong's retail market. The National Day Golden Week is typically a peak selling season for retailers, but that vanished this year because of depressed consumption sentiment and severely disrupted tourism. Total retail sales value dropped by 24.3% YoY in October; the luxury sector suffered the most severely, with sales plummeting 42.9% YoY. This is the worst slump on record. Total visitor arrivals plunged 43.7% YoY in October, with Mainland arrivals dropping 45.9% YoY.

To weather the storm, some retail chains have adopted consolidation strategies by shutting down outlets in the areas worst hit by protests and focusing on neighbourhood malls. Others have taken measures to reduce costs, such as asking employees to take unpaid leave and freezing hiring. Falling sales have also prompted retailers to seek rental reductions and concessions from landlords, both temporarily and for lease renewals and new leases.

As people have chosen to stay in their local communities and avoided going to key shopping districts because of the unpredictable conditions, such as traffic congestion and social events, stores in non-core retail areas have been somewhat buttressed by more local consumption in the past few months. Therefore, we believe under the current circumstances, the role of neighbourhood malls will be strengthened, resulting in the development of 'local community hubs'.

Faced with the difficult operating environment, retailers are generally pessimistic about sales in the Christmas season and Lunar New Year. Many are looking for rental relief from their landlords. In the meantime, the latest government relief measures are a welcome sign for the market. However, looking ahead, given the severity of the situation, we forecast that the prime street shop rents will drop by at least another 15% in 2020.

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 (Oct 2019)

Outlet	Value (HK\$ billion)	Share of total %	Change MoM %	Change QoQ %	Change YoY %
Jewellery, watches and clocks, and valuable gifts	3.9	13.0	6.4	-28.9	-42.9
Clothing, footwear and allied products	3.0	9.9	1.1	-32.7	-36.9
Department stores	2.9	9.5	0.9	-19.4	-31.0
Fuel	0.9	3.1	1.1	7.3	4.4
Food, alcoholic drinks and tobacco (excluding supermarkets)	3.3	10.8	-15.0	5.8	-11.6
Consumer durable goods	5.8	19.2	6.5	23.9	-16.2
Supermarkets	4.5	14.9	-0.7	-0.6	0.5
Others	5.9	19.6	2.7	-24.2	-27.1
All retail outlets	30.1	100.0	0.7	-12.4	-24.3

Source: Census and Statistics Department / Knight Frank Research

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