

OFFICE

Cost conscious tenants prevalent across markets

Hong Kong Island

Despite the notable rebound in Hong Kong's equity market in recent months, global economic uncertainties have continued to dent leasing demand for Grade-A office space in Central. In March, demand was mainly for small floor plates of less than 10,000 sq ft in traditional Grade-A office buildings at a monthly rent of HK\$100-130 per sq ft.

In order to reduce rental costs, a number of large multinationals and corporates have planned to exit the CBD to decentralized areas. The Securities and Futures Commission's planned relocation from Cheung Kong Center in Central to One Island East in Quarry Bay in January 2020 is one example. Meanwhile, there will be around 1.9 million sq ft of new space available in Central and Admiralty in the coming 12 to 18 months, which is equivalent of 10% of existing stock. Given the hold-up of co-working space demand, it will significantly drive up the low Grade-A vacancy in Central and Admiralty, currently at 2%.

Because of this, we expect rents in the CBD to soften, as landlords of premium Grade-A office buildings will be under pressure. Meanwhile, some smaller MNCs may move in to fill the vacancies, provided that landlords are willing to cut their asking rents or divide each floor into smaller units to secure occupancy.

Kowloon

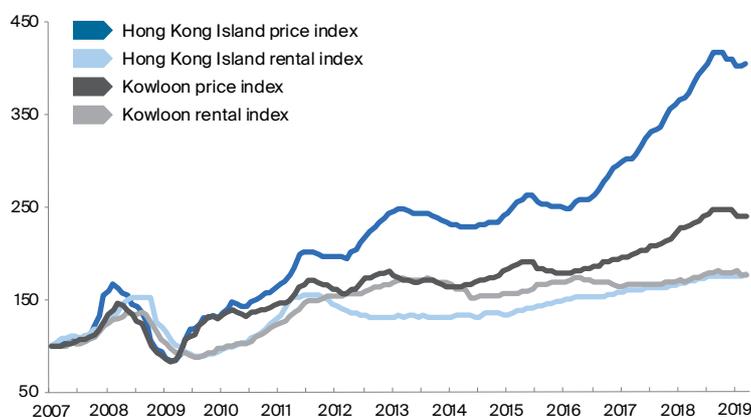
The Grade-A office leasing market in Kowloon was generally active in March, with around 120 sizeable transactions recorded, almost double the figure in February. Demand was fuelled mainly by the relocation and consolidation needs of sourcing, insurance and electronics companies.

One significant transaction during the month was WeWork's lease of the 150,000-sq-ft space between 26/F and 31/F in the Gateway Sun Life Tower Extension in Tsim Sha Tsui. The transaction was concluded after Sun Life's decision to leave the building.

Apart from this take-up, Kowloon office market is dominated by cost-conscious tenants amid economic uncertainties. Cost reduction has driven some companies to have either downsized their office space or moved to co-working space. For example, Prudential Assurance moved to World Finance Centre South Tower in Tsim Sha Tsui from Festival Walk in Kowloon Tong and reduced their total office area by more than half.

FIGURE 1
Grade-A office prices and rents

2007 = 100



Source: Knight Frank Research

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

District	Net effective rent			Price (Gross)		
	HK\$ psf / mth	MoM %	YoY %	HK\$ psf	MoM %	YoY %
Premium Central	193.2	-2.4	0.5	-	-	-
Traditional Central	144.6	-1.3	5.2	-	-	-
Overall Central	161.1	-1.7	3.2	43,119	1.3	3.0
Admiralty	115.8	-0.5	0.8	38,607	0.0	15.9
Sheung Wan	86.0	0.0	2.2	33,881	0.5	4.4
Wan Chai	78.2	-2.7	-0.6	30,031	0.0	3.5
Causeway Bay	83.6	-1.6	0.7	26,024	0.0	3.5
North Point	52.2	-3.3	-3.5	-	-	-
Quarry Bay	54.1	-0.5	1.8	-	-	-
Tsim Sha Tsui	71.6	0.0	7.3	18,142	-0.9	4.7
Cheung Sha Wan	32.9	0.3	2.6	-	-	-
Hung Hom	44.3	0.2	3.1	-	-	-
Kowloon East	32.0	-0.4	-0.7	13,429	0.2	2.3
Mong Kok / Yau Ma Tei	59.1	0.0	0.6	-	-	-

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

RESIDENTIAL

Vacancy tax weighs on market despite a sales rebound

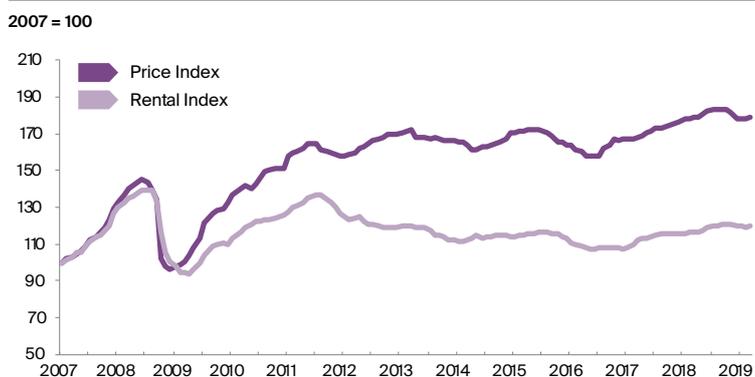
In March, total residential sales volume soared 27.9% MoM to 5,231 units, according to the Land Registry, making it the first month with over 5,000 monthly transactions since July 2018. The latest official data shows that overall property prices increased by 1.3% MoM in February led by a hefty overall price increase in small and medium-sized units.

In February 2019, the proportion of sales transactions involving Double Ad Valorem Stamp Duty (DSD) dropped to 5%, the lowest point since the revised DSD took effect in November 2016. The DSD cases in Q1 2019 accounted for only 8% of the total number of transactions. The proportion of sales transactions involving Buyer's Stamp Duty (BSD) also declined, accounting for only 3% of total transactions in Q1 2019, compared to 8% in Q4 2018. This indicates that both non-first-time buyers and overseas buyers are retreating as tax burdens kicked in.

Entering the traditional peak season in March, the luxury leasing market also saw a rebound in transactions. Some districts such as Mid-levels Central and Happy Valley recorded active leasing activity. Landlords have remained firm in their negotiations.

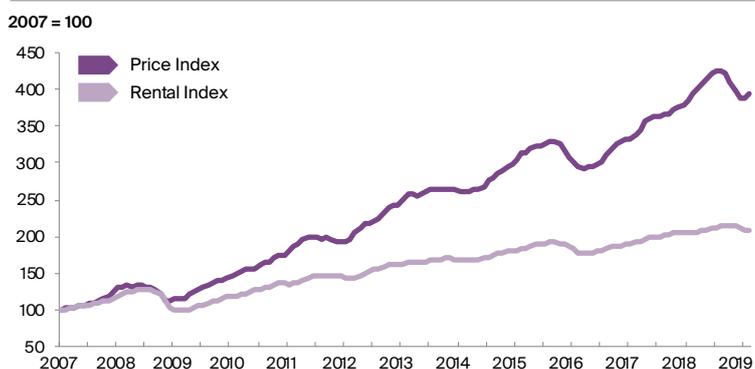
The government has tabled a proposal for a vacancy tax, officially known as "Special Rates", which will levy a tax equivalent to 200% of the rateable value of primary homes that have not been sold or leased for 6 months or more. Even as the issue being debated, consensus market view seems already suggest that it will have limited long term impact on supply and prices.

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 (Mar 2019)

District	Building	Tower / floor / unit	Saleable area (sq ft)	Price (HK\$ million)	Price (HK\$ per sq ft)
Island South	90 Repulse Bay Road	House	5,668	503.9	88,899
Happy Valley	23-39 Blue Pool Road	House	4,571	338.2	73,988
Island South	8 Deep Water Bay Drive	Tower 1 / low floor	3,641	221.4	60,800
The Peak	La Hacienda	House	2,800	153.8	54,929
Island South	Manderly Garden	House	3,160	170.0	53,797

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

TABLE 3
Selected residential lease transactions (Mar 2019)

District	Building	Tower / floor / unit	Lettable area (sq ft)	Monthly rent (HK\$)	Monthly rent (HK\$ per sq ft)
Happy Valley	The Leighton Hill	Tower 6 / high floor / unit A	1,674	115,000	69
Tsim Sha Tsui	The Masterpiece	Low floor / unit C	1,466	89,000	61
Mid-Level East	The Altitude	Low floor / unit A	1,509	79,000	52
Mid-Level East	Evergreen Villa	Block A / high floor	2,330	110,000	47
Mid-Level Central	Estoril Court	Block 2 / high floor / unit C	2,888	130,000	45

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

RETAIL

Retail sales disappointing, but overall trends positive

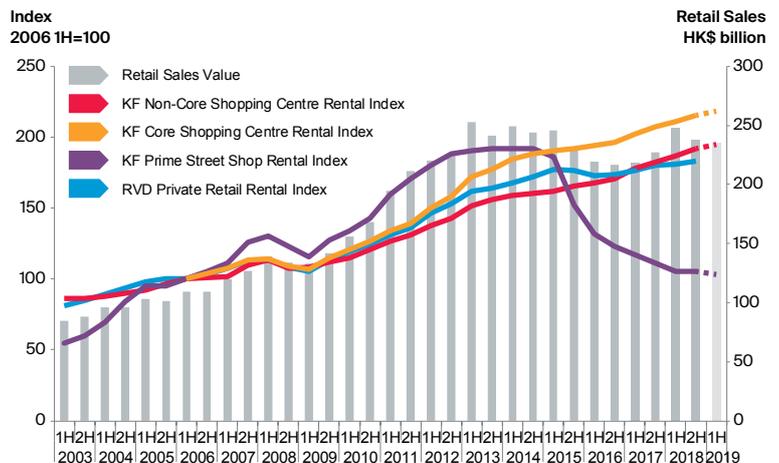
Hong Kong's retail sales in February slumped 10.1% YoY in value, ending the growth trend since March 2017 and registering the biggest decline since August 2016. In January and February 2019 combined, sales value registered a mild drop of 1.6% YoY. The weak retail sales continued to reflect a cautious consumer sentiment caused by external uncertainties, which also exerted downward pressure on rents in core retail areas. In contrast, Mainland visitor arrivals in the first two months of the year recorded a growth of 18.7% YoY. We believe that the new cross-boundary transportation links that have enhanced travel convenience from multiple Mainland destinations to Hong Kong will continue to boost visitor arrivals, offering long-term support for the retail sector.

Landlords have been adjusting their leasing strategies to target local consumers and same-day visitors by embracing more mid-tier brands. We see more affordable lifestyle brands taking up space in core shopping areas and in premium shopping centres. Examples include Japanese discount megastore Don Don Donki upcoming 15,000 sq ft-flagship store in Mira Place Two, Sephora's upcoming 4,000 sq ft-store in ifc mall, and Muji's new store in Pacific Place.

Looking ahead, the retail market is likely to register flat growth or even a mild drop in the first quarter of this year. Nevertheless, consumer sentiment is likely to be underpinned by favourable employment figures and an improving stock market. Together with rising tourist arrivals and new retail potential, we expect both retail sentiment and sales to improve in the second half of the year, albeit at a slow pace.

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 (Feb 2019)

Outlet	Value (HK\$ billion)	Share of total %	Change MoM %	Change QoQ %	Change YoY %
Jewellery, watches and clocks, and valuable gifts	7.2	17.8	-14.0	22.6	-9.7
Clothing, footwear and allied products	5.8	14.4	-7.1	22.5	-11.0
Department stores	4.2	10.4	-12.7	-23.7	-6.1
Fuel	0.7	1.7	-11.1	-14.0	-2.0
Food, alcoholic drinks and tobacco (excluding supermarkets)	3.9	9.7	-16.5	10.3	-13.7
Consumer durable goods	5.5	13.5	-16.5	-17.1	-18.4
Supermarkets	4.3	10.5	-10.7	2.0	-5.5
Others	8.9	22.0	-23.3	14.4	-7.0
All retail outlets	40.7	100.0	-15.4	3.6	-10.1

Source: Census and Statistics Department / Knight Frank Research

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