Briefing
Office sector

February 2015

Image: Offices in Central

SUMMARY

After a broadly positive 2014, we expect modest rental growth in 2015.

- Rents in most districts were flat over 2014.
- The Shanghai-Hong Kong Stock Connect offset the negative effect brought by the Occupy Central Movement in Q4.
- PRC firms are taking up the vacant space returned by some large, multiple-floor MNC tenants.
- We believe that there will be increasing leasing activity in Kowloon East this year due to greater availability and a significant rental difference compared with other core districts.
- The potential Shenzhen-Hong Kong Stock Connect may further strengthen demand for office space from investment and securities firms.

"PRC firms continue to take up the slack left by MNCs, driven by IPOs and the Stock Connect programme."
Simon Smith, Savills Research

Market commentary

Grade A office rents were stable in Q4/2014, rising only by 0.8%. The Shanghai-Hong Kong Stock Connect which started in Q4 offset the negative impact brought by the Occupy Central Movement (OCM). On the back of moderate economic growth, a healthy employment situation and tight availability of quality office space in Hong Kong, Grade A office rents in 2014 rose by 1.5%.

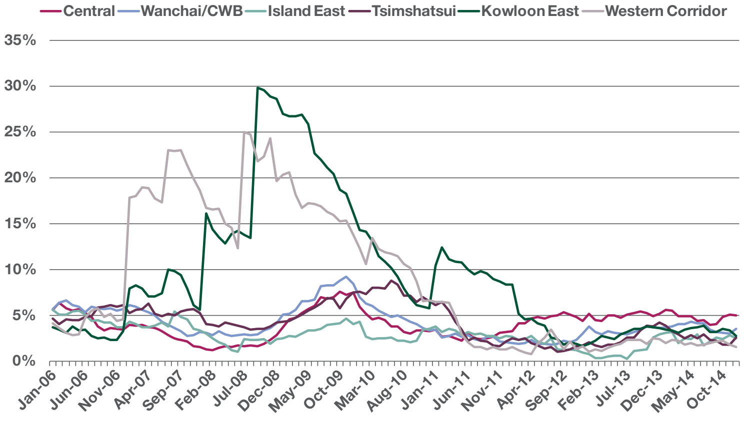
Firms are resuming their expansion plans gradually, especially in Central as the OCM ended. Over 30% of the transactions over 10,000 sq ft were in Central, with half of them being new lets. PRC firms are filling up the vacant space returned by some large, multiple-floor MNC tenants, stabilising the vacancy rate in Central. Central Grade A office rents rose by 0.8% in Q4 but fell by 0.4% over the year as a whole. Meanwhile, the occupancy rate stood at 5.0%, 0.1 percentage point (ppt) below the end December 2014.

Wanchai/Causeway Bay and Mong Kok, the other two districts affected by the OCM, witnessed rental growth of 1.0% and 6.6% respectively. The full letting of Langham Place in Mong Kok was the main rent driver in the district. We witnessed demand from banks and insurance companies which further squeezed availability in Tsim Sha Tsui, driving rents up by 1.2% over the quarter.

Rents in Island East, Kowloon East and Kowloon West were relatively stable, with quarterly rental growth of less than 1%. We believe there will be increasing leasing activity in Kowloon East due to more availability and a monthly rental difference of over HK$10 per sq ft compared with other core districts.

GRAPH 1

Savills Grade A office vacancy rates by district, Jan 2006–Dec 2014



Source: Savills Research & Consultancy

TABLE 1

Savills Grade A office rental growth, Q4/2014 and 2014

	Q4/2014 (%)	2014 (%)
Central	+0.8	-0.4
Wanchai/Causeway Bay	+1.0	+1.1
Island East	+0.1	+1.5
Tsim Sha Tsui	+1.2	+4.1
Kowloon East	-0.4	-0.6
Kowloon West	+0.4	-0.6

Source: Savills Research & Consultancy

TABLE 2

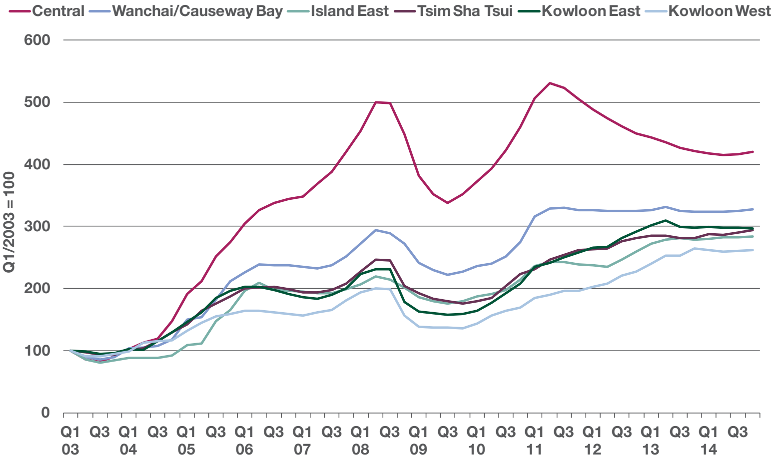
Major new leasing deals, Q4/2014

Tenant	Building	Size (sq ft)
The Economist	Cityplaza 4	16,400
Regus	181 Queen's Road Central	15,500
BNP	PCCW Tower	14,100
South Horizons Baptist Church	Global Trade Square	9,800
Hua Jun International Limited	Citibank Plaza	15,700
Athena Financial Group	Berkshire House	10,900

Source: Savills Research & Consultancy

GRAPH 2

Savills Grade A office rental indices by district, Q1/2003–Q4/2014



Source: Savills Research & Consultancy

OUTLOOK

The prospects for the market

In 2015, a steady pipeline of IPOs from PRC firms and the potential launch of Shenzhen-Hong Kong Stock Connect will maintain demand for Hong Kong Grade A office space, especially in Central. We believe demand from private banks and asset management firms will continue to be in focus; the latest paper published by the Hong Kong Financial Services Development Council suggested that the asset management industry is "expected to grow due to government's promotion of the industry and as institutional pension assets continue to grow" and the financial industry "is shifting from broker oriented to wealth management". A strengthening dollar this year will increase costs for some tenants, however, particularly European and Asian firms. On the back of limited availability and supply in the year, we expect a 0 to 5% increase in overall Grade A office rents, with 5% expected in Central itself.

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