

Briefing Retail sector

February 2014



Image: Causeway Bay

SUMMARY

Rental growth is showing clear signs of moderating while declines have been recorded in some secondary locations.

- Leasing market activity slowed in the run up to Christmas and Chinese New Year, as retailers focused on the peak season for sales.

- Market sentiment remained generally positive, but retailers are becoming more cautious regarding occupation costs and selective in terms of locations for their next expansion or relocation.

- Rental adjustment in the prime street shop segment continued in Q4/2013, with rents falling slightly by 0.3% after a 2.5% decline in the

previous quarter, largely driven by the rental decline in some secondary locations.

- After years of fast growth and speculative expansions, some secondary and tertiary locations disappointed their tenants in terms of footfall and popularity, and thus higher vacancy rates were noted in these areas.

- Base rents in major shopping centres grew by another 0.9% quarter-on-quarter (QoQ) in the last quarter of 2013.

- We forecast prime street shop rents to fall by 0% to 5% in 2014, mainly due to the rental correction in less prime locations.

- Shopping centre rents are projected to increase by 5% to 10% in 2014.

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 "While we remain broadly positive on market outlook, some adjustment in rents is inevitable in 2014." Simon Smith, Savills Research

➔ **Market commentary**

Activity in Hong Kong's retail leasing market slowed at the end of 2013 and the beginning of 2014, as retailers focused on the traditional peak season for sales over Christmas and Chinese New Year. The low level of transaction activity was also attributed to the lack of availability in first-tier locations.

Despite a slower market, sentiment remained generally positive. Overall retail sales registered a 5.7% growth in December and a sustained growth of 9.7% over 2013, higher than the 8.9% growth recorded in 2012. Retailers

from different sectors registered healthy sales growth over the holiday periods, with the exception of the Electrical Goods and Photographic Equipment, and the Furniture and Fixtures sectors, which may be attributed to slower home sales. The super luxury watch and jewellery sector remains subdued due to the decrease in gifting and the changing visitor profile of mainland Chinese tourists.

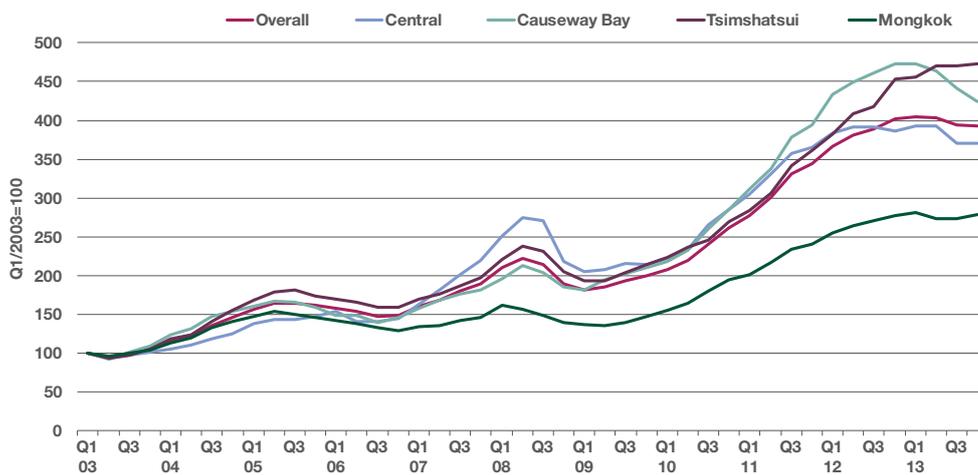
Meanwhile, prime street shop rents in first-tier locations remained flat over Q4/2013, as a result of a quiet

quarter in the leasing market. A few exceptions were noted in various sub-markets; Russell Street and Percival Street in Causeway Bay registered 5% to 10% rental declines from September to December 2013, the former owing to lower shopper traffic and the latter to its record-breaking rents, which challenged retailer affordability. The most sought-after location, Canton Road in Tsim Sha Tsui, continued to see growth of 2.4% following a number of noticeable deals, including Chow Tai Fook's leases at 86-98 Canton Road and 54 Canton Road (formerly Armani Exchange) for monthly rents of HK\$4.52 million (HK\$1,795 per sq ft gross) and HK\$6.65 million (HK\$1,900 per sq ft gross) respectively. As a popular location for goldsmiths and mid-market retailers, Nathan Road and Sai Yeung Choi Street South in Mong Kok also recorded an average growth of 4% over the same period.

In the shopping centre segment, base rents in major shopping centres saw sustained growth and recorded a 0.9% QoQ increase over Q4/2013. Overall, major shopping centre rents grew by 9.1% in 2013. On the back of the robust retail market seen over the past few years, many shopping centre landlords have been able to strengthen their position by upgrading their tenant and trade mix profiles. However, the challenges over the coming years will be avoiding cookie-cutter type developments and creating a point of difference from their counterparts.

We remain positive on the outlook of Hong Kong's retail market in 2014. We believe the recent and short-term rental adjustments should lead to the more sustainable long-term development of the market. Most of the retailers are still in an expansion mode but they are becoming more cautious with respect to occupation costs and selective in terms of locations for expansion or relocation. Moreover, after years of fast growth and speculative expansions, secondary and tertiary locations have disappointed their tenants in terms of footfall and popularity. Therefore, we believe there will be a polarisation in the prime street shop leasing market over the short to medium term. While first-tier locations, which have proven popular among mainlanders, will

GRAPH 1 **Savills prime street shop rental indices by district, Q1/2003-Q4/2013**



Source: Savills Research & Consultancy

GRAPH 2 **Savills prime street shop and major shopping centre rental indices, Q1/2006-Q4/2013**



Source: Savills Research & Consultancy

continue to see strong demand and sustained rental levels, more vacancy and steeper rental adjustments might be recorded in secondary and tertiary locations.

We project that street shop rents could well drift down this year, while we still see some headroom for rents in the shopping centre segment. Same-day visitors will outnumber overnights again in 2014 and this will continue to benefit centres in the New Territories and sales of convenience goods. Although this suburban retail story has been played out over the past few years, hazards are present

in this persistently buoyant sector, as infrastructure constraints – road, rail, air, cross border as well as hotel room numbers – could all impede growth. However, none of these factors is intractable. Dizzying projections from the government suggest that Hong Kong could receive 70 million tourists annually within three years and 100 million within a decade, mostly mainlanders. It is time for the government, landlords and retailers to look for new initiatives or opportunities to cater to this growing demand. Last year Hong Kong hosted 40.8 million mainland Chinese tourists. ■

TABLE 1
Rental changes and forecasts, 2013–2014F

	2013 (%)	2014F (%)
Prime street shops	-2.2	0 to -5
Shopping centres	+9.1	+5 to 10

Source: Savills Research & Consultancy

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