MARKET IN MINUTES

Savills Research

Residential Sales

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Luxury prices slip by 2%

Both local and external uncertainties are dampening luxury residential market sentiment as volumes hit new lows and values begin to weaken.

- External events including Russia's invasion of the Ukraine, tougher US regulation of China tech stocks have hit the local stock market hard and dampened property investment sentiment in general, while the recent Omicron outbreak poses a further threat to the local luxury residential market
- Luxury volumes (over HK$50 million) declined dramatically in Q1/2022 to 91, the lowest since the social unrest of Q3/2019, with the lower price bracket enduring the largest drop. Luxury prices softened by between 1.5% and 2.7% as a result.
- Luxury sites in traditional luxury enclaves are still in demand with a South Bay Road site tendered for a record high average price of HK$62,355 per sq ft. Only a handful of luxury sites are to be put up for tender by the Government in 2022/2023, with a Cape Road site the most eye-catching.
- Stretched affordability and weak market sentiment all contributed to mass price adjustments in Q1/2022, which declined by 2.4% across the board.
- While the local COVID situation is largely contained, the lockdown of major Chinese cities may increasingly impact China's economy and Mainland HNWIs appetite for luxury properties in Hong Kong.
- With the US Fed likely to increase interest rates more aggressively, the local negative real interest rate environment could be put to the test, though there is still some way to go before reverting to positive territory.

"While the local COVID situation is largely contained, the lockdown of major Chinese cities will impact China's economy and Mainland HNWIs appetite for luxury properties in Hong Kong. Even with the US Fed likely to increase interest rates more aggressively given that US inflation is at a 40-year high, local real interest rates should remain in negative territory."

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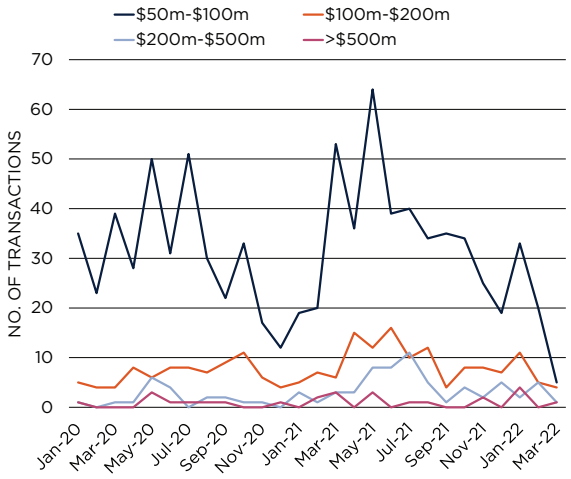
TABLE 1: Residential Price Growth by Segment, Q2/2021 to Q1/2022

	Q1/2022	Q4/2021	Q3/2021	Q2/2021
Townhouse	-1.5%	-0.2%	0.0%	+3.2%
Hong Kong Island Luxury Apartment	-2.1%	+1.2%	+0.7%	+4.0%
Kowloon Luxury Apartment	-2.1%	0.0%	-0.3%	+2.9%
New Territories Luxury Apartment	-2.7%	+1.7%	0.0%	+2.4%

Source Savills Research & Consultancy

GRAPH 1: Luxury Transaction Volumes by Price Range, January 2000 to March 2022



Source Land Registry, Savills Research & Consultancy

LUXURY SENTIMENT DAMPENED BY BOTH EXTERNAL AND LOCAL UNCERTAINTIES

External events such as the Russian invasion of the Ukraine and tougher US regulation of China tech stocks have hit the local stock market hard, with the Hang Seng Index plunging to a six-year low of 18,415 in mid-March, before rebounding slightly towards the end of the first quarter. Meanwhile, the Omicron outbreak in Q1/2022, when daily cases surged to over 50,000 in mid-March before gradually receding to below 10,000 towards the end of March, posed further threats to the local luxury residential market. The ongoing border closure with the Mainland and highly restrictive COVID measures have deterred both Mainland and local buyers from making purchasing decisions.

Luxury prices registered downward adjustments in Q1/2022 across most districts as a result, with townhouse prices falling by 1.5%, while luxury prices on Hong Kong Island, Kowloon and the New Territories declined by 1.7%, 2.1% and 2.7% respectively.

Luxury volumes (over HK$50 million) declined dramatically in Q1/2022 to 91, the lowest since the outbreak of social unrest in Q3/2019, which was a 20% QoQ drop from an already quiet Q4/2021. Similar to last quarter, less affluent buyers are affected the most, with volumes in the price bracket between HK$50 and HK$100 million declining by 25%. The super-rich were less affected, as volumes over HK$100 million registered only a 9% QoQ decline.

The most noticeable super luxury deal over the quarter was the sale of two residential blocks at 1 & 1A Kotewall Road in Mid-Levels to Lai Sun Development for HK$1.3 billion (A.V. of HK$22,628 per sq ft), which Lai Sun intends to redevelop into 20 large luxury units with a saleable area of 1,250 to 2,500 sq ft for sale in 2025 at the earliest.

RECORD HIGH PRICE FOR SOUTH BAY ROAD TENDER REFLECTS DEVELOPER'S APPETITE FOR LUXURY SITES

Luxury sites in traditional luxury enclaves are still in demand with a South Bay Road site tendered for a record high average price of HK$62,355 per sq ft., beating the previous record for a government tender of HK$50,010 per sq ft, the A.V. of the 9-11 Mansfield Road site on the Peak tendered a year ago. The winning bid went to SEA Holdings, which intends to develop two to four detached houses on the site with a construction cost of over HK$500 million. The record price reflected developers' continued interest in exclusive super luxury sites, and their general confidence in the super luxury market in the medium term.

Looking at the Land Sale Programme from April 2022 to March 2023, there are only a handful of luxury sites up for tender by the Government, namely a site on Hospital Road in Mid-Levels, a site on Sai Ning Street and Victoria Road in Kennedy Town, and a site on Cape Road in Stanley. Among the three, the Cape Road site is the largest (526,000 sq ft) and has the highest potential to be developed into super luxury accommodation and should attract plenty of market attention when being made available in the second half of 2022-2023.

TABLE 2: Tender Result of South Bay Road Site

SITE	Rural Building Lot No. 1203 at South Bay Road, Repulse Bay
DATE	Feb 2022
CONSIDERATION (HK$)	$1,188,181,800
SITE AREA (SQ FT)	21,173
MAXIMUM GFA (SQ FT)	19,055
AV (HK$ PER SQ FT)	$62,355
SUCCESSFUL BIDDER	SEA Holdings
ESTIMATED PRODUCT	2-4 detached houses
ESTIMATED COMPLETION	2025 - 2027
ESTIMATED STATUS AFTER COMPLETION	Long term investment holding

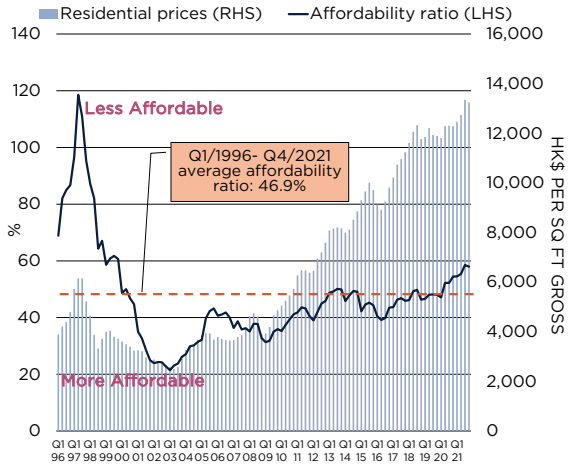
Source Lands Department, Newspaper

TABLE 3: Major Super Luxury Transactions (over HK$200 million), Q1/2022

DATE	PROPERTY	FLOOR AREA (SQ FT)	CONSIDERATION (HK$ MILLION)	AVERAGE PRICE (HK$ PSF)
Jan	1 & 1A Kotewall Road, Mid-Levels	57,450 (max GFA)	$1,300	$22,628
Jan	15/F, Mount Nicholson Phase III Tower C, the Peak	4,230 (saleable)	$583.19	$137,870 (saleable)
Jan	House 6, Twelve Peaks, Southside	4,241 (saleable)	$387.0	$91,252 (saleable)
Jan	Unit 22A, St. George's Mansions Tower 3, Ho Man Tin	3,325 (saleable)	$218.0	$65,564 (saleable)
Feb	House 33A, Cadenza Phase 1, Sheung Shui	6,906 (saleable)	$202.0	$29,250 (saleable)

Source EPRC, Newspapers

GRAPH 2: Affordability Ratio and Residential Prices, Q1/1996 to Q4/2021



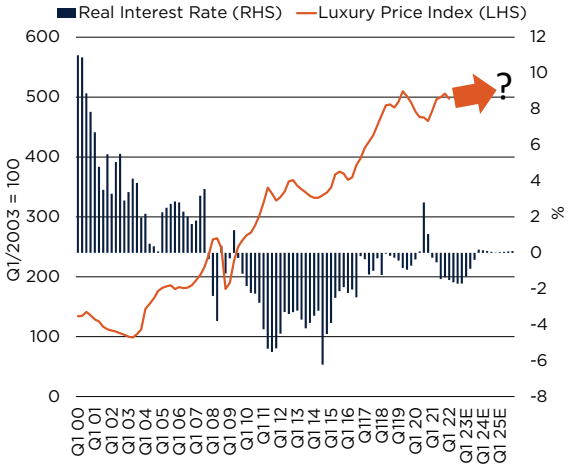
Source Savills Research & Consultancy

TABLE 4: Luxury Sites in the Land Sales Programme, 2022 to 2023

LOT NO.	LOCATION	SITE AREA (SQ FT)	APPROX. GFA (SQ FT)
IL 8872	Hospital Road, Mid-Levels	5,371	48,341
IL 9069	Sai Ning Street and Victoria Road, Kennedy Town	5,780	52,022
RBL 1204	Cape Road, Stanley	260,486	526,000

Source Lands Department

GRAPH 3: Luxury Prices vs Real Interest Rates, Q1/2000 to Q4/2025E



Source Census and Statistics Department, Oxford Economics, Savills Research & Consultancy

THE MASS MARKET ALSO STRUGGLED IN Q1 WITH STRETCHED AFFORDABILITY IMPACTING MARKETABILITY OF HOMES

The mass market also saw prices enduring a drop of 2.4% in Q1/2022, with Hong Kong Island experiencing the most severe decline (3.4%) among all districts as more professionals, both locals and expats, left the territory. Stretched affordability, which saw affordability at 58% in Q4/2021, has hindered the sales of many second homes with many potential homebuyers struggling to pass the stress tests of bank mortgage lenders. This shortcoming could not be overcome even with the further relaxation of price caps of 80% and 90% LTVs under the Mortgage Insurance Programme to HK$12 million and HK$10 million respectively.

MARKET OUTLOOK

While the local COVID situation is largely contained, the lockdown of major Chinese cities may increasingly impact China's economy with implications for Hong Kong. Due to a surging number of confirmed Omicron cases, since March, 23 cities in China have been fully or partially locked down, including major financial hubs such as Shanghai, which account for around 14% of China's population and 22% of the country's GDP. Many more cities are undergoing mass testing. The World Bank slashed China's 2022 GDP growth to 5%, lower than the country's 5.5% official target. All these factors will weigh on sentiment and further diminish HNWIs' appetite for luxury properties in Hong Kong.

The US inflation rate climbed to 8.1% in March 2022, the highest in 40 years. As such, the US Fed will have no choice but to increase interest rates more aggressively over the next few months to try to curb rising prices. While local banks still have abundant liquidity and did not react to the first rate hike in 2022, sequential hikes over the coming months will inevitably force banks to follow suit, increasing the cost of capital for property investors. Nevertheless, as Hong Kong is expected to see mild inflation of 2% to 2.5% over the next couple of years, the negative real interest rate environment, which has helped to propel the city's longest residential price rally over the past decade, is likely to persist at least for the next two years.

With all these challenging factors combined, we expect luxury residential prices to decline further by 5% to 7% over the remainder of the year.