MARKET IN MINUTES
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Residential Sales

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Luxury market sentiment weakens

Rare fund activity in the super luxury sector may reflect contrasting views on the future market direction.

- The stock market correction and the first increase in the prime rate since 2018 have dampened luxury residential sentiment, with heaviest post-GFC quarter-on-quarter price falls registered in Q3.
- Some eye-catching deals, such as the sale of House 3B of Gough Hill Residences for HK$500 million suggests that super luxury products are still highly sought after.
- Luxury sites and en-bloc buildings are still in demand, and with two sites on Hong Kong Island to be tendered in Q4, we expect both to attract market attention when launched
- Luxury volumes remained thin in Q3 across all price brackets due to subdued sentiment. With economic recession looming and rising geopolitical tensions in mind, many ultra-high net worths in Hong Kong may opt to diversify their local portfolios globally to mitigate such risks.
- Given the negative outlook, we expect the luxury residential market outlook to be clouded over the next nine to 12 months, with values likely to correct by 10% over 2022, and to decline by a further 5% to 10% over 2023.

"Despite a drifting luxury market and extremely low volumes, luxury sites are still in demand. While interest rates look set to continue to rise over the next three to six months, rising inflation and the possibility of recession remain key concerns among Hong Kong's ultra-high net worths, many of whom plan to realign their global investment portfolios to mitigate such risks."

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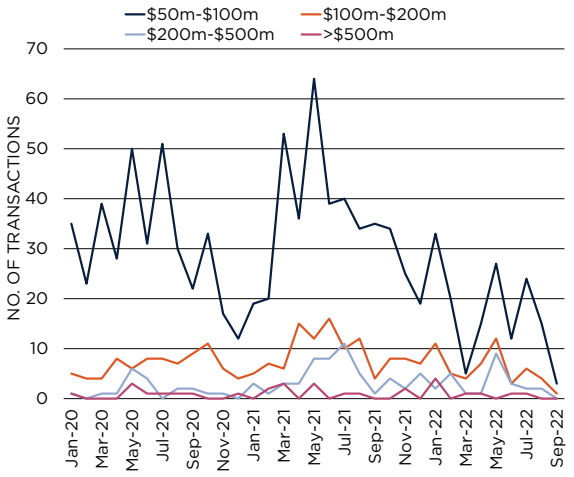
TABLE 1: Residential Price Growth by Segment, Q4/2021 to Q3/2022

	Q4/2021	Q1/2022	Q2/2022	Q3/2022
Townhouse	-0.2%	-1.5%	-4.1%	-4.5%
Hong Kong Island Luxury Apartment	+1.2%	-1.7%	-2.9%	-4.7%
Kowloon Luxury Apartment	0.0%	-2.1%	-2.7%	-4.2%
New Territories Luxury Apartment	+1.7%	-2.7%	-2.5%	-5.1%

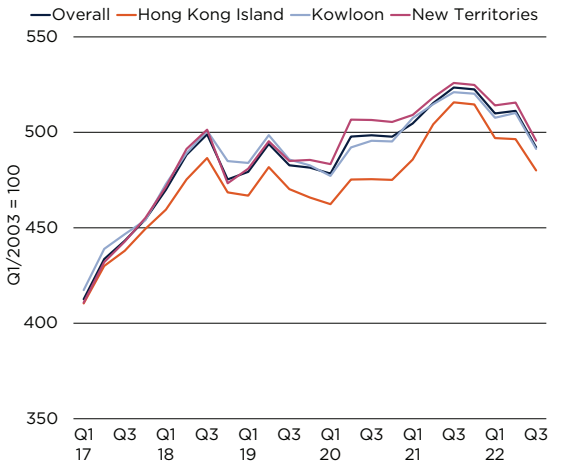
Source Savills Research & Consultancy

GRAPH 1: Luxury Transaction Volumes by Price Range, January 2020 to September 2022



Source Land Registry, Savills Research & Consultancy

GRAPH 2: Mass Market Price Indices by District, Q1/2017 to Q3/2022



Source Savills Research & Consultancy

STOCK MARKET CORRECTION AND FIRST PRIME RATE INCREASE SINCE 2018 WEAKENS LUXURY SENTIMENT FURTHER

The dismal performance of the IPO market, weak business sentiment both locally and in China, as well as continued strict quarantine controls (just relaxed to 0+3 in September) and China's firm 'COVID zero' policy, all contributed to a stock market correction in Q3 with a 26% decline from a recent high at the end of June to below 17,000 by October 11th, an 11-year low.

On top of this worrying economic and financial situation, the US Fed has persisted in increasing rates to fight inflation at home (another 1.75 percentage point increment in September) and this has finally led to a prime rate increase of 0.125% by major local banks, the first increase since 2018. Both have exerted negative pressure on the luxury residential market, with luxury prices recording their heaviest quarter-on-quarter decline since the GFC across all districts in Q3/2022.

In some rare positive market news, LC Vision Capital, a Singaporean fund, bought all the remaining 152 units (with 242 car parking spaces and 31 motorcycle parking spaces) at 21 Borrett Road, Mid-Levels for a total consideration of HK$20.766 billion, representing an average price of around HK$62,000 per sq ft. The move was a very rare foray by fund investors into the luxury residential sector, with the extremely low yield on offer (luxury yields at around 1.9% in Q3) not typically appealing to yield-driven investment funds.

The move may on one hand reflect the confidence of foreign funds in the local property sector, on the other hand, it may reflect some developers' cautious outlook for the luxury market, at least in the short term.

LUXURY HOMES AND SITES STILL IN DEMAND, DESPITE SLOWING VOLUMES

Some eye-catching deals over the quarter suggest that there is still demand for super luxury homes. Take for example House 3B (saleable area 4,299 sq ft) of Gough Hill Residences on the Peak, which was sold for HK$500 million (HK$116,306 per sq ft saleable), while the detached house at 8 Kent Road in Kowloon Tong (6,460 sq ft saleable) was sold for HK$538 million (HK$83,282 per sq ft saleable). The sales of these two prestige homes suggests that super luxury products are still highly sought after.

En-bloc buildings are still in demand, with the en-bloc at 68 Robinson Road sold to Weave Living and LaSalle Investment Management for HK$275 million. The property is expected to provide 25 two-bedroom units upon refurbishment.

Another luxury site on Hospital Road was sold for HK$551 million via Government tender to K. Wah, with the site having a GFA of around 42,978 sq ft, the deal represented an AV of around HK$12,820 per sq ft. The development is estimated to be completed between 2025 and 2027 and is earmarked for sales.

Two more luxury sites were scheduled for tender from the Lands Department in Q4/2022, and with the ongoing developer interest in developable sites, we would expect the eventual launch of these two sites to attract market attention.

Luxury volumes (over HK$50 million) plummeted in Q3 with only 58 transactions registered, a marked 36% decline when compared to Q2, mainly due to subdued sentiment. The decline was across all price brackets except at the very top end (>HK$500 million) where volumes remained unchanged.

TABLE 2: Luxury Sites to be Launched for Tender in Q4/2022

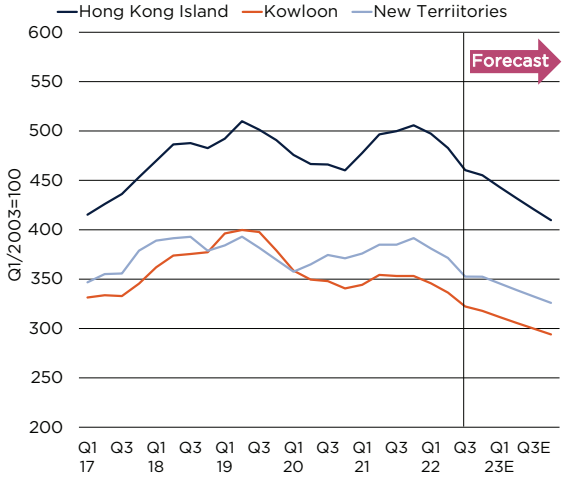
LOT NO.	LOCATION	SITE AREA (SQ FT)	APPROX. GFA (SQ FT)
IL 9069	Sai Ning Street and Victoria Road, Kennedy Town	5,780	46,243*
RBL 1204	Cape Road, Stanley	255,104	480,231**

Source Lands Department

* For pure residential use, a specific formula would apply for the calculation of total GFA for any potential retail podium

** According to the maximum GFA as stipulated in the latest OZP under R(B) Zone

GRAPH 3: Luxury Apartment Price Indices by District, Q1/2017 to Q4/2023E



Source Savills Research & Consultancy

TABLE 3 : Key Economic Forecasts, Q4/2022 to Q4/2023

	2022	2023			
	Q4	Q1	Q2	Q3	Q4
HK GDP	+4.0%	+6.4%	+4.8%	+2.8%	+2.1%
HK Inflation	+2.5%	+2.4%	+2.6%	+2.5%	+2.2%
HK 3-month HIBOR	3.52%	3.58%	3.56%	3.46%	3.27%
China GDP	+4.2%	+4.0%	+6.7%	+4.8%	+4.3%

Source FocusEconomics, Savills Research & Consultancy

THE MASS MARKET DECLINES WITH NEW LAUNCHES AT LOW PRICES ATTRACTING ATTENTION

The mass market was equally hard hit in Q3, as interest rate hikes have had a more profound impact on average homeowners. The primary sales market also suffered, as only launches in the New Territories with average prices under HK$15,000 per sq ft saleable sold well, with most launches in urban areas for HK$20,000 per sq ft saleable and above struggling to find buyers. Mass prices declined by 3.7% in Q3 as a result.

MARKET OUTLOOK

While interest rate hikes remain the key concern for many homeowners and potential home buyers in Hong Kong, among the ultra-high net worth community, inflationary risks, prospects of economic recession as well as geopolitical tensions are major worries for the moment, according to a recent survey by Swiss private bank Lombard Odier. As these negative factors are not going to be resolved in the near future, many billionaires in town may, or have already realigned their local investment portfolios to other global markets to mitigate such risks.

With interest rates looking set to rise through the remainder of this year and early next, real interest rates could turn positive as early as the middle of 2023, prompting cash rich investors to be more cautious when making large capital investment decisions such as buying luxury properties. Coupled with the slow recovery of both the local and China economies, the COVID-zero policy in China and persistent inflationary threats, we expect luxury prices to decline by 10% for the full year 2022 and adjust downwards by another 5% to 10% in 2023. The downside risks to our forecasts include prolonged COVID-zero beyond Spring next year and heightened geo-political tensions while upside risks include the potential for government to unpick previous cooling measures such as Special Stamp Duty (2010), Buyer's Stamp Duty (2012) and Doubled Ad Valorem Stamp Duty (2013).