MARKET IN MINUTES

Savills Research

Hong Kong – July 2019

Office and Retail Investment

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Investment sentiment subdued in Q2

Recent domestic and overseas uncertainties have hit transaction volumes hard.

- Investment sentiment was subdued by the US / China trade tensions as well as the controversial Extradition Bill and the social unrest which followed, with both transaction volumes and values falling by half over the first few months of the year.
- The few office transactions recorded over the quarter were driven by either bargain-hunting veteran investors or by end users entering the market for the first time with limited pricing information.
- Many office tenants who were actively looking to purchase their own premises a few months ago backed off from the sales market given the deteriorating sentiment, and many decided to renew their leases instead.
- The core retail investment market was particularly hard hit by declining retail sales, with suburban retail remaining relatively unscathed, therefore becoming the first choice for many retail investors.
- In a surprise move, Goldin Financial withdrew from the tender of a hotel / commercial site at Kai Tak pointing to 'social contradiction and economic instability'.
- With the reopening of trade negotiations between the US and China after the G20 Osaka Summit, more positive news is anticipated over the next few months, but the path to an ultimate trade resolution is not expected to be an easy one.
- With recent local events also causing capital outflows as evidenced by rising HIBOR and a declining aggregate balance, the investment market looks set to endure another bumpy ride over the next three to six months.

"The on-going US / China trade tensions, as well as the proposed Extradition Bill, have hit investment sentiment, with non-residential transaction volumes falling by half. Bargain hunting occurred in both the office and retail markets with cash-rich investors looking for distressed assets which proved hard to come by."

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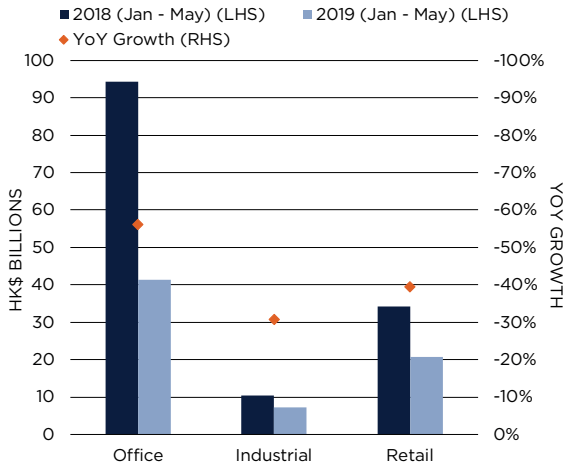
GRAPH 1: Major Non-residential Transaction Value (over HK$100 million), January to May 2019



Source RCA, Savills Research & Consultancy

BOTH TRANSACTION VOLUMES AND VALUES WERE HARD HIT GIVEN SUBDUED INVESTMENT SENTIMENT

Investment sentiment was subdued by the US / China trade tensions as well as the Extradition Bill and resulting unrest, with major non-residential transactions (over HK$100 million) falling by 50% y-o-y over the first five months of 2019, as many investors remained on the sidelines. Some southern China industrialists have seen their businesses severely impacted by the trade war, reducing their appetite for property investment in Hong Kong. Overall non-residential transaction volumes also declined significantly by 49% over the first four months of 2019, the worst start to a year since 2016, which saw the first interest rate hike by the US Fed.

OFFICE SECTOR SEES BARGAIN HUNTING

The office sector quietened with many investors driven to bargain hunting, but many landlords, who are experienced investors themselves with holding power, stood firm on asking prices. The few deals concluded were mainly purchases by end users who were determined to find their own space for occupation regardless of market conditions. Many office tenants who were active in looking to purchase their own premises a few months ago backed off from the sales market given the worsening sentiment, and many decided to renew their leases instead.

We saw similar trends on Kowloon side with many buyers turning cautious and some even abandoning purchasing processes given deteriorating business prospects. A

TABLE 1: Number Of Non-residential Transactions, Jan-Apr 2019 vs Jan-Apr 2018

NUMBER OF TRANSACTIONS	JAN-APR 2018	JAN-APR 2019	YOY GROWTH
Office	569	323	-43%
Commercial	742	475	-36%
Flatted Factories	2,047	927	-55%
Non-residential	3,358	1,725	-49%

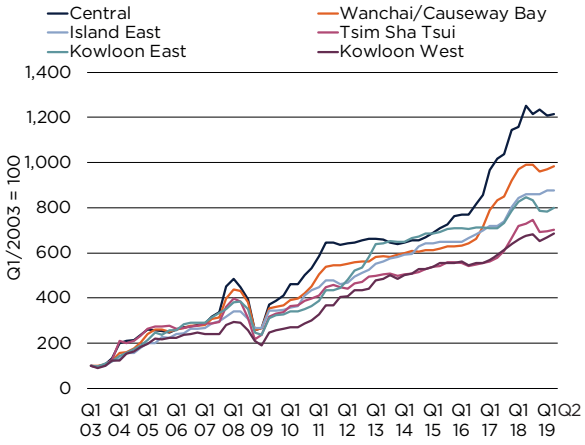
Source Rating and Valuation Department, Savills Research & Consultancy

TABLE 2: Major Office Transactions, Q2/2019

DATE	PREMISES	UNIT(S)	GROSS AREA (SQ FT)	CONSIDERATION (HK$ MIL)	AVERAGE PRICE (HK$ PER SQ FT)
May 2019	The Center	3908	3,140	$138.7	$44,168
May 2019	Shun Tak Centre – West Tower	2508 & 09	2,816	$110.0	$39,063
May 2019	The Center	3903	1,843	$87.5	$47,460
May 2019	Lippo Centre Tower 1	2407A	802	$35.7	$44,554
April 2019	COSCO Tower	2110, 11, 12 & 13	5,281	$147.9	$28,000
April 2019	Shun Tak Centre – West Tower	3007 & 08	3,881	$124.7	$32,131
April 2019	The Center	2211	3,184	$114.6	$35,990

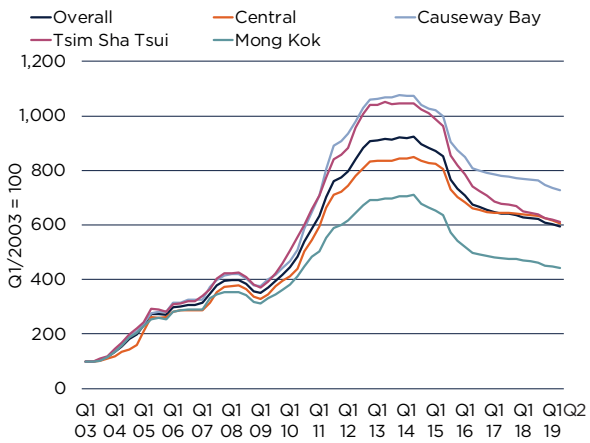
Source Savills Research & Consultancy

GRAPH 2: Grade A Office Price Indices By District, Q1/2003 to Q2/2019



Source Savills Research & Consultancy

GRAPH 3: Prime Street Shop Price Indices By District, Q1/2003 to Q2/2019



Source Savills Research & Consultancy

TABLE 3: Prime Street Shop Price Growth, Q1-Q2/2019, 2018 and 2017

	Q2/2019 (% QoQ)	Q1/2019 (% QoQ)	2018 (% YOY)	2017 (% YOY)
Central	-1.5	-1.3	-2.8	-1.0
Causeway Bay	-1.2	-1.2	-3.3	-2.4
Tsim Sha Tsui	-1.3	-1.0	-6.4	-5.6
Mong Kok	-1.2	-1.0	-5.1	-2.2

Source Savills Research & Consultancy

TABLE 4: Grade A Office Price Growth, Q1-Q2/2019, 2018 and 2017

DISTRICT	Q2/2019 (%QOQ)	Q1/2019 (% QOQ)	2018 (% YOY)	2017 (% YOY)
Central	+0.4	-2.2	+7.9	+34.0
Wanchai/ Causeway Bay	+1.5	+0.9	+4.3	+29.0
Island East	0.0	+1.9	7.2	+14.7
Tsim Sha Tsui	+1.1	+0.5	4.2	+19.7
Kowloon East	+2.2	-0.5	-0.1	+10.5
Kowloon West	+2.5	+2.3	2.1	+15.3

Source Savills Research & Consultancy

number of end users in the Kowloon market are industrialists with manufacturing bases in southern China. Investors were looking for bargains (typically at a 10% to 15% price discount) but very few landlords were prepared to entertain such discounts, leading to lower transaction volumes across the harbour.

CORE RETAIL HIT BY A DWINDLING RETAIL SALES PERFORMANCE

The decline in retail sales performance (-1.8% over the first five months of 2019), in particular key shopping items for tourists (Jewellery, watches and clocks -4.4%, Electric goods -16.6%), further dampened investment sentiment with many veteran retail investors happy to wait out the turbulence. Nevertheless, there were still adventurous investors looking for bargains, such as the prime shop at 151 Hollywood Road which sold for HK$595 million, with the vendor selling at a loss of HK$105 million within 3 months. The retail market focus was still firmly on suburban retail with sales holding up well, but for major transactions of over HK$100 million, purchasers showed greater interest elsewhere (such as industrial premises with redevelopment potential).

GOLDIN FINANCIAL'S WITHDRAWAL FROM ITS KAI TAK'S COMMERCIAL TENDER

In a surprise move, Goldin Financial withdrew from the tender of a hotel / commercial site at Kai Tak citing 'social contradiction and economic instability'. The site in question was Kai Tak Area 4C Site 4, with a site area of 115,088 sq ft and a maximum GFA of 863,158 sq ft. Goldin won the tender of the site for HK$11.1 billion or HK$12,888 per sq ft in May this year, the highest commercial AV for Kai Tak. The acquisition of the Land was thought to bring significant synergy to the development of the existing land parcel held by Goldin Financial located at Area 4B Site 4, Kai Tak for residential use.

MARKET OUTLOOK

With the reopening of trade negotiations between the US and China after the G20 Osaka Summit, more positive news is anticipated over the next few months, but the path to an ultimate trade resolution is not expected to be an easy one. With recent local events also causing capital outflows as evidenced by rising HIBOR (increasing from 1.66% at the end of March to 1.98% at the end of May) and a declining aggregate balance (declining from HK$64.8 billion at the end of March to HK$54.3 billion at the end of May), the investment market looks set for a bumpy ride over the next three to six months.