

OFFICE

Rental growth in Central and Quarry Bay continues to polarise

Hong Kong Island

Affected by uncertainty in the US–China trade negotiations and slowing global economic growth, leasing demand for Grade-A offices in Central was softening. Premium Grade-A offices in this CBD area were particularly affected, as tenants' affordability was undermined. Buildings leased for less than HK\$100 per sq ft per month were less impacted because of the expansion of some financial and legal firms.

In Island East, demand for Quarry Bay offices was strong thanks to its maturing business infrastructure and the continuous influx of decentralisation tenants. However, with a low vacancy rate of only about 1%, sizeable office spaces of over 15,000 sq ft in the area were highly sought after, underpinning rental increases of 1.2% month on month (MoM) in June.

Due to different demand drivers and tenant expectations, rental growth in Central and Quarry Bay is expected to polarise for the rest of 2019.

Kowloon

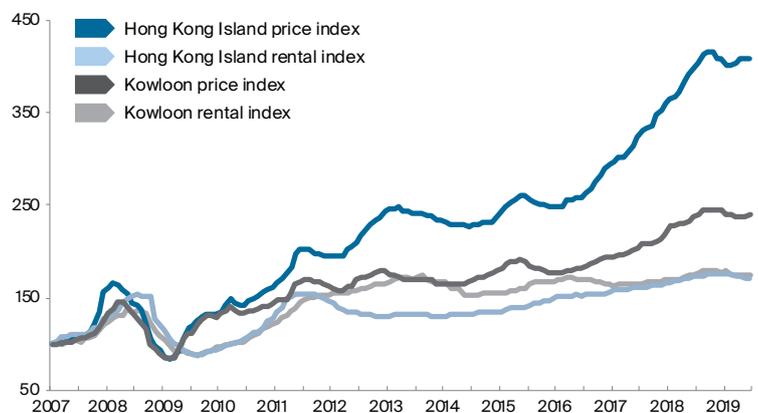
Leasing momentum in the Grade-A office market in Kowloon weakened in June amid the unclear market outlook, with the number of transactions falling around 30% MoM. Most of the deals were less than 3,000 sq ft and were recorded in Kowloon East.

Facing downbeat market sentiment, some companies relocated their offices to buildings with lower rents. For example, apparel brand Ralph Lauren, whose office of the sourcing division is currently in Kowloon Bay, will move to the sixth floor of Hong Kong Spinners Industrial Building, Phase 1 & 2 in Cheung Sha Wan, taking up an area of 69,000 sq ft. The relocation will enable the company to reduce its rental overhead from around HK\$30 per sq ft per month to HK\$21.5 per sq ft, a savings of around 30%.

Despite softening leasing demand, overall Grade-A office rents in Kowloon increased by 0.5% MoM. However, this was due to a few exceptional cases; rents are unlikely to go up much. We expect overall rents in Kowloon to increase only 1% to 3% for the whole year in 2019.

FIGURE 1
Grade-A office prices and rents

2007 = 100



Source: Knight Frank Research

TABLE 1
Grade-A office market indicators (June 2019)

District	Net effective rent			Price (Gross)		
	HK\$ psf / mth	MoM %	YoY %	HK\$ psf	MoM %	YoY %
Premium Central	189.7	0.0	-3.6	-	-	-
Traditional Central	144.0	0.0	2.2	-	-	-
Overall Central	159.5	0.0	-0.2	43,907	0.0	0.0
Admiralty	115.0	0.0	-1.1	39,184	0.0	5.7
Sheung Wan	85.1	0.0	-0.1	34,341	0.0	-1.2
Wan Chai	78.5	-0.5	-1.3	30,476	0.0	3.0
Causeway Bay	80.0	-1.2	-4.3	26,409	0.0	3.2
North Point	51.8	-0.8	-4.3	-	-	-
Quarry Bay	55.1	1.2	3.7	-	-	-
Tsim Sha Tsui	72.2	0.9	4.8	18,262	0.7	0.2
Cheung Sha Wan	33.3	0.0	1.9	-	-	-
Hung Hom	44.4	0.4	-1.3	-	-	-
Kowloon East	32.0	0.0	-1.9	13,313	-0.3	0.3
Mong Kok / Yau Ma Tei	60.1	-0.2	1.8	-	-	-

Source: Knight Frank Research

Note: Rents and prices are subject to revision.

RESIDENTIAL

Sales volume plunged amid concern about the worsening economy

Hong Kong's monthly residential sales volume tumbled over 43% in June to a four-month low of 4,627 units, according to the Land Registry. Primary sales in June dropped to the lowest level in 2019, totalling just 1,111 units.

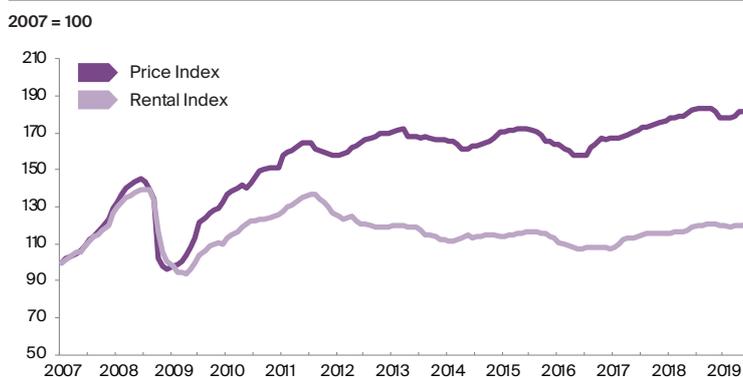
The latest official data shows that overall residential prices increased 10.4% from January to May. However, Knight Frank's earlier study on the correlation between house prices and the Hang Seng Index, a barometer of the city's economy, found that mass home price movements closely followed the HSI trend with a time lag of up to three months. So with the HSI having dropped close to 10% at a point since May, there is a possibility for mass home prices to undergo some corresponding adjustment.

The luxury home market is another story. Despite recent market turbulence, high net worth individuals were not afraid of paying top dollar for luxury properties here. For instance, an investor dished out HK\$581 million for a 7,008 sq ft house in Mount Nicholson, while an Indian entrepreneur paid HK\$250 million for a 3,641 sq ft apartment unit in 8 Deep Water Bay Drive.

The residential leasing market entered the traditional peak season in June. Families are actively looking for new homes before the new school year starts. Rents for both mass and luxury homes grew steadily in the first half of the year.

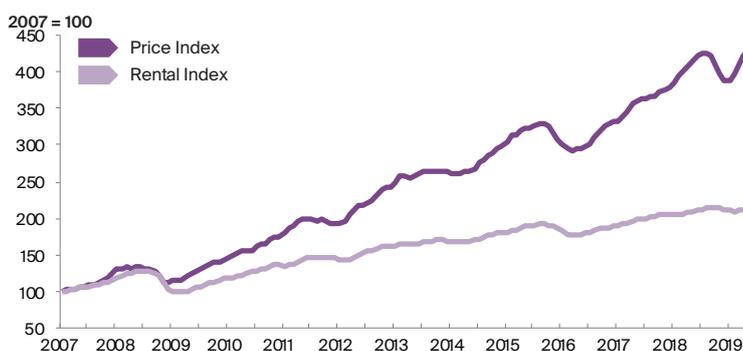
Despite the worsening economic outlook and the potential for capital to out of the region, we expect the Hong Kong residential markets to remain resilient.

FIGURE 2
Luxury residential prices and rents



Source: Knight Frank Research

FIGURE 3
Mass residential prices and rents



Source: Knight Frank Research

TABLE 2
Selected residential sales transactions (June 2019)

District	Building	Tower / floor / unit	Saleable area (sq ft)	Price (HK\$ million)	Price (HK\$ per sq ft)
Tsim Sha Tsui	The Arch	Sky Tower / high floor / unit A	2,014	180	89,374
The Peak	Mount Nicholson	House	7,008	580.9	82,889
Island South	8 Deep Water Bay Drive	Tower 1 / mid floor / unit B	3,641	251.2	69,000
Tin Hau	The Pavilia Hill	Tower 2 / top floor / unit A	3,365	185.2	55,034
Island South	Tai Tam Road 12-16	House	3,350	180	53,731

Source: Knight Frank Research
Note: All transactions are subject to confirmation.

TABLE 3
Selected residential lease transactions (June 2019)

District	Building	Tower / floor / unit	Lettable area (sq ft)	Monthly rent (HK\$)	Monthly rent (HK\$ per sq ft)
Island South	The Lily	Tower 2 / high floor	2,625	181,000	69
Mid-Level Central	Bamboo Grove	Block 80 / high floor	1,650	113,500	69
Mid-Level Central	Dynasty Court	Low floor / unit B	1,520	85,000	56
Island South	Hong Kong Parkview	Tower 12 / high floor	2,308	120,000	52
Island South	Bel-Air	Phase 2 / tower 1 / low floor / unit A	1,956	100,000	51

Source: Knight Frank Research
Note: All transactions are subject to confirmation.

RETAIL

No silver lining in sight

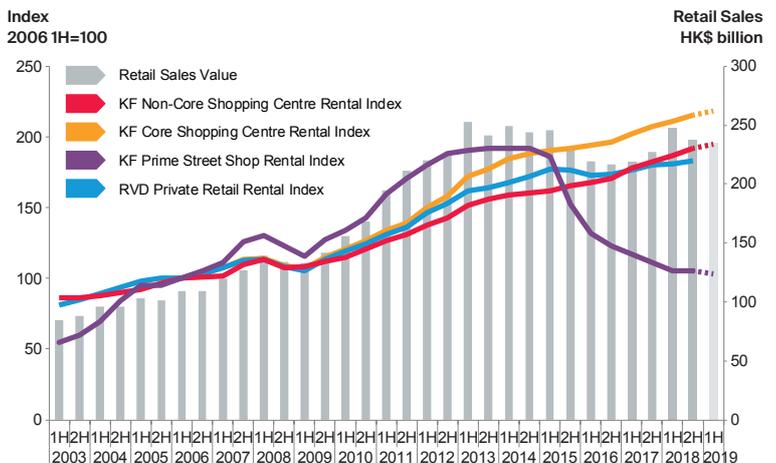
Hong Kong's retail sales had been falling since February this year, with retail sales for May dropping 1.3% YoY in value. The retail sales performance of the luxury sector also remained weak, down 2.7% YoY.

Deteriorating luxury retail sales have made the recovery of the retail leasing market more challenging, especially for prime street shops. With vacant shops remaining unfilled, rents continued to fall. For example, a 4,000 sq ft street-front shop at Yu To San Building on Queens Road Central, previously occupied by a luxury jewellery company, was recently leased to a sports brand for a monthly rent of HK\$1.4 million, or HK\$350 per sq ft, which was reportedly about 30% lower than the peak level rent.

With most of the luxury sector's physical expansion slowing down, some non-luxury retailers are seizing the opportunity to take up space in the core areas outside Central. For instance, in July, Japanese eyewear brand Onwndays will open its first two stores on Hong Kong Island, at Hysan Place in Causeway Bay and Lee Tung Avenue in Wan Chai. New York's Museum of Modern Art will open its largest design store outside Japan at K11 Musea in Tsim Sha Tsui, taking up about 6,000 sq ft.

Retail business performance is expected to remain weak amid external economic uncertainties and local political upheaval. We expect rents for prime street shops to decrease 5-10% in 2019, while rents for shopping malls should remain relatively stable.

FIGURE 4
Retail sales and rents



Source: Knight Frank Research / Rating and Valuation Department / Census and Statistics Department

TABLE 4
Retail sales by outlet type (May 2019)

Outlet	Value (HK\$ billion)	Share of total %	Change MoM %	Change QoQ %	Change YoY %
Jewellery, watches and clocks, and valuable gifts	6.7	16.8	14.8	-7.6	-2.7
Clothing, footwear and allied products	5.0	12.4	-4.8	-15.5	-3.7
Department stores	5.8	14.5	52.7	36.6	0.3
Fuel	0.9	2.2	4.6	25.8	-5.2
Food, alcoholic drinks and tobacco (excluding supermarkets)	3.5	8.7	-0.2	-11.5	3.1
Consumer durable goods	4.8	11.9	-7.2	-12.7	-9.3
Supermarkets	4.4	11.1	6.0	3.9	-0.8
Others	9.0	22.5	-3.0	0.8	3.3
All retail outlets	40.0	100.0	6.0	-1.6	-1.3

Source: Census and Statistics Department / Knight Frank Research

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