Colliers Quarterly

HONG KONG | RESIDENTIAL

Q4 2017
1 February 2018

Residential market to stay resilient amid stability

Zac Tang Senior Analyst | Hong Kong

The Hong Kong residential market had a robust 2017 with price and transaction volume increasing 13% and 24% respectively from 2016. Demand in the primary market stayed strong with developers actively launching new projects, while the secondary market was driven by strong market sentiment. In 2018, we expect overall home price to increase 8-10%, with supply shortage to remain unsolved, and supported by persistent negative real interest rates.

Forecast at a glance

Supply
17,800 new private units were completed in 2017, up 22% YOY. We expect supply to increase further in 2018 to around 20,000 units

Demand
The US Federal Reserve has indicated that it will raise interest rates three times in 2018. Nevertheless, we do not expect real (i.e. inflation-adjusted) interest rates to turn positive again in Hong Kong before H2 2019 or early 2020.

Rent
We expect luxury residential rents to increase 4.2% from 2017 to 2019. A positive business outlook should continue to support leasing demand amid tight supply

Price
In 2018, the overall residential price should increase by 8-10%. Residential prices should increase moderately in 2019, and should go flat in 2020 as a result of increasing supply and interest rates.

A robust year for the residential market

The Hong Kong residential market had a robust 2017 with price and transaction volume increasing from the previous year. Demand in the primary market stayed strong with developers more actively launching new projects with aggressive financing schemes. Demand in the secondary market was driven by strong market sentiment despite the presence of high stamp duties.

In Q4, overall transaction volume in the private residential market increased 24% QOQ to 16,320 units, pushing up the whole year's transaction volume by 13% YOY despite high stamp duties and cooling measures constraining speculative activities. According to the latest figures from Land Registry, the two-month transaction volume of October and November for the primary and the secondary market had increased 35% and 50% from July and August respectively. The 40%/60% spilt of primary and secondary units sold in 2017 stayed the same as 2016.

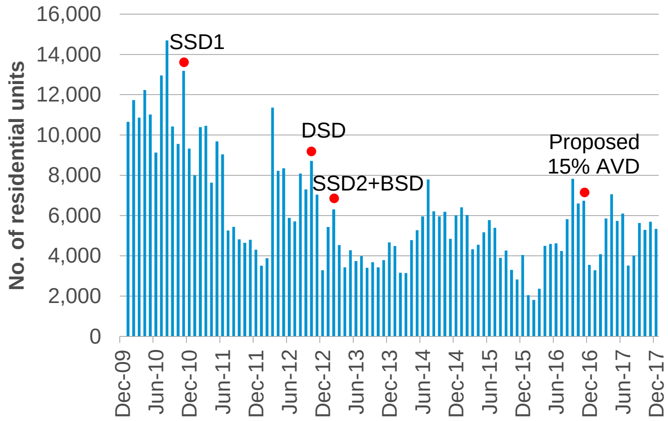
According to Transport and Housing Bureau, the completion of private residential units in 2017 reached 17,800 units, an increase of 22% YOY. This figure has reached the completion target set by the Rating and Valuation Department for 2017.

Despite increasing supply, the housing market shortage remained unsolved. The medium-term supply market should not be strong because the government had only sold nine residential development sites in 2017 for a total of 4.0 million sq ft (371,613 sq m) of space, which is lower than the 10 million sq ft (929,031 sq m) provided by the 24 residential sites sold in 2016. For the Government's tender, PRC developers have acquired 68% in terms of land value and 70% in terms of gross floor area. Hong Kong developers started to increase their residential land reserve by expediting farm land conversion into residential land. Sun Hung Kai Properties has completed the conversion process for agricultural land in Shap Sz Heung, Tai Po in the New Territories by paying HKD15.9 (USD2) billion or HKD3,319 (USD427) per sq ft land premium. After the change, the site will provide a buildable gross floor area of about 5 million sq ft (464,516 sq m) or about 4,700 residential units.

Local developers without large farmland reserves have had to bid for smaller residential sites, redevelopment sites owned by the Urban Renewal Authority, or form JVs with other developers to compete for prime sites. In November, for example, the government sold the 987,803 sq ft (91,770 sq m) (gross floor area) site in Cheung Sha Wan, the biggest residential site sold in the year, to a consortium of five developers led by Sino Land for HKD17.3 (USD2.2) billion.

In 2017, US Fed Fund rate target was increased three times or by 0.75%. Yet, Hong Kong's prime rate did not follow suit and stayed at 5%. The three-month Hong Kong Interbank offered rate (HIBOR) had stayed low at 1.3% at the end of 2017, up by 0.5 percentage points from one year previously. Hong Kong home buyers continued to enjoy a very low financing cost. The property market was further supported by a buoyant stock market with the Hang Shang Index ending 2017 at 29,919.2, an annual increase of 36%.

Residential Sales and Purchase Agreements



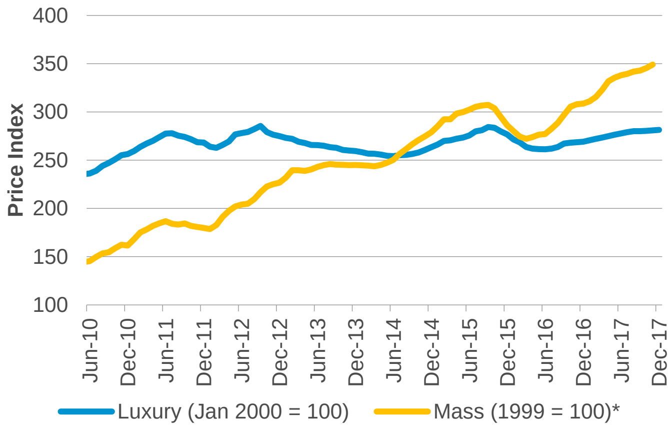
Source: The Land Registry

The strong growth maintained

According to the latest figures published by the Rating and Valuation Department, the overall private residential price increased 1.8% since September, or 12.9% over the first eleven months. Price for mass market increased at the same rate since September, and 13.1% over the first eleven months. We estimate that prices for the luxury market to increase by about 0.5% QOQ.

A strong user demand filled vacancies quickly. Being supported by a wealth effect and strong interests from mainland Chinese buyers, ultra-luxury units achieved new record prices. Unit 12C and 12D in Mount Nicholson, a luxury apartment on The Peak, were sold at HKD1.16 billion (USD149 million) or HKD132,060 (USD16,974) per sq ft. The unit price was an all-time high record for a residential strata title transaction. A unit in Victoria Harbour, a luxury apartment in North Point developed by Sun Hung Kai Properties, was sold at a record of HKD102.8 million (USD13.2 million) or HKD64,887 (USD8,340) per sq ft, marking a new benchmark of luxury apartments for the district.

Hong Kong Residential Price Index



Source: Colliers; Rating and Valuation Department
*refers to the units smaller than 1,076 sq ft

Leasing market picked up steadily

The residential leasing market has regained momentum in Q4 2017. An increasing number of new expatriates to Hong Kong continued to contribute to new leasing demand in Mid-levels, Southside, and the Peak, but we also saw that more expatriates are leasing outside the traditional districts, due to changing corporate policies favouring personal leases and increasing rents in traditional areas.

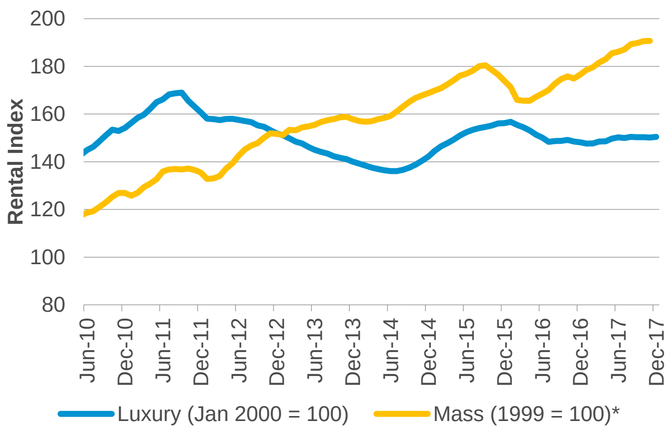
The overall luxury residential rent was stable in Q4 compared to Q3. Mid-levels was the most active market with rents increasing the fastest at a rate of 0.6% QOQ. Southside and The Peak remained flat, vacancies were low but demand was relatively stagnant. We observed that demand for houses increased, probably because asking rents have become more negotiable, especially for houses which have been vacant for several months. However, housing budgets for expatriates will remain tight, limiting the growth of demand for the top segment of the luxury market.

The increasing demand for new locations and the availability of more affordable units have driven rents to rise faster outside traditional districts. For example, the rental difference between Island East and traditional luxury residential areas has narrowed from 37% in 2012 to 15% in 2017.

We expect the overall luxury residential rent to increase by 4.2% from 2017 to 2019 over the two-year period amid the positive business cycle. It is unlikely that MNCs will increase expatriates' housing budgets in the coming few years. However, a positive business outlook should continue to support leasing demand amid a tight supply. As leasing demand for ultra-luxury units and townhouses remains relatively soft, we expect the rental outlook for luxury apartments in Mid-levels to be the most resilient. Southside will be supported by the growth of apartments, while the Peak should see the most moderate growth.

With new international school campuses coming to Kowloon and the New Territories, and the overall living amenities and conveniences continuing to improve sub-urban areas should become more popular with expatriates in the coming years.

Hong Kong Residential Rental Index



Source: Colliers; Rating and Valuation Department
*refers to units smaller than 1,076 sq ft

Prices should rise in 2018, despite approaching the peak level

We believe the growth momentum to persist in 2018 amid low interest rates and supply shortage. However, there are factors that can have negative impacts on the local property market, especially concerning the tightening of local market liquidity.

The US Federal Reserve started a scheme to gradually reduce its balance sheet in 2017. The combined balance sheets of major central banks have increased from roughly USD7 trillion to USD18 trillion over the last decade, data from Citi Research showed. However, we expect that the balance sheet normalisation will be very gradual.

The US Federal Reserve has indicated that it will raise interest rates three times in 2018. Hong Kong interest rates will rise gradually in response, because of the territory's currency peg. Nevertheless, we do not expect real (i.e. inflation-adjusted) interest rates to turn positive again in Hong Kong before H2 2019 or early 2020. We expect new completions to reach an annual average of 20,000 units in the private residential market from 2018 to 2020, of which 16% will be in Tseung Kwan O — over 10,000 new units. Despite the new supply in the coming four years, 96% of these units will be smaller than 100 sq m (1,076 sq ft). However, the prolonged supply shortage should persistent as pent-up demand has not been fully digested.

The Stamp Duty Amendment Bill allows home owners to hold two flats for a total of 12 months, up from the original six months proposed, to offload their first property to avoid paying the tax. The amendment will increase the flexibility for owner-occupiers and is likely to stimulate more activities in the secondary market. We expect the 30%/70% spread of transactions between primary units and secondary units to widen in 2018, with the secondary market regaining momentum.

The residential market should stay resilient amid a positive global economic outlook. In 2018, prices for the mass market should increase by 8-10%, and the luxury market should grow by 3-5%. Residential prices should increase moderately in 2019, and should go flat in 2020 as a result of increasing supply and interest rates.

For more information:

Nigel Smith
Managing Director | Hong Kong
+852 2822 0508
nigel.smith@colliers.com
Individual Licence: E-111570

Letizia Garcia Casalino
Senior Director | Residential Services
+852 2822 0709
Letizia.GC@colliers.com
Individual Licence: E-361726

Daniel Shih
Director | Research
+852 2822 0654
daniel.shih@colliers.com