Hong Kong's property problem

Kate Farr and Rachel Read explore Hong Kong's property market, one of the world's most expensive

Holding the dubious distinction of being one of the world's most expensive cities in which to live and own property, entering the Hong Kong market is challenging for even the most experienced of buyers. But although the city's property bubble has long since been forecast to burst, the market continues to go from strength to strength, despite concerns about affordability, coupled with recent government-led cooling measures.

While the Central business district has traditionally been the beating heart of commerce in Asia's World City, there is an increasing trend amongst businesses faced with the city's notoriously punishing commercial rents to diversify from these locations to keep costs competitive. "Causeway Bay, Central and Tsim Sha Tsui remain the focus for luxury retail brands, but there are many small-to-medium scale retail podiums and shopping malls being developed alongside new residential projects in decentralised areas such as Yuen Long, North Point and Tseung Kwan O," says Tom Gaffney, managing director of CBRE Hong Kong. "These residential developments will attract upper-middle class consumers, and therefore affordable luxury brands, to the area."

Although much has been made of Hong Kong's recent slump in retail sales, Gaffney explains that, far from dragging the market down, it has created new opportunities within the commercial sector. "Increased vacancy on prime streets has pulled prime retail rents down by 30 per cent. More prudent tourist spending has caused a double-digit drop in sales at major shopping malls since 2014. On the one hand, luxury retailers have been suffering from weaker tourist consumer buying power, but on the other hand, this has created opportunities for international brands and mid-range retailers to expand in Hong Kong." In fact, according to CBRE Research, Hong Kong had the world's most new market entrants in 2015 and 2016, supporting the suggestion that, far from being in decline, Hong Kong's retail market remains extremely buoyant.

Nigel Smith, managing director of commercial real estate firm Colliers International, holds a similar view. "With retail sales expected to be hitting the bottom, institutional investors have been actively pursuing retail properties in urban fringe and decentralised areas with potential value-add opportunities," he says. "Investment sentiment for office properties stayed robust, especially in core-CBD areas, following a recent record sales price for the Murray Road Car Park site," adds Reeves Yan, Colliers' executive director of capital markets and investment services.

$3bn
Amount paid for a 460,000sqft car park in the centre of Hong Kong

This unassuming-sounding plot is now the most expensive piece of land ever sold in Hong Kong. Bought by developer Henderson Land, who outbid eight other developers to seal the deal for $3 billion, this 460,000 square foot site sits in the heart of the Central CBD and is slated to become a landmark mixed-use retail and office building by 2022. Early forecasts suggest that, once complete, Henderson will sell units at approximately $7,700 per square foot – far surpassing the current record of $5,100 at the existing 9 Queen's Road Central site.

Meanwhile, on the residential side of the market, Hong Kong's traditional upscale locations

"Prices are 16 times the average household median income, one of the worst ratios in the world"

remain popular with homeowners, while once again, investors look further afield for improved returns.

"Prestigious locations like The Peak and South Side are dominated by wealthy family end users, where investors mainly focus on new hotspots like South Horizons or Kennedy Town – districts recently covered by MTR lines," says Clara Chu, senior director of residential services at Colliers International.

"We rarely see investors buying prestigious locations for leasing, as the yields are lower than the smaller units in those hotspot areas, which can be easily rented out."

And what of Hong Kong's most visible external investors, once renowned for big-ticket property purchases? "Even gigantic PRC [mainland Chinese] investors who own residential properties in those prestigious areas treat them as a holiday house or leave them empty rather than leasing them out," says Chu. "This is why the capital value and rent remain popular and stable in these prestigious locations among the wealthy end user."

"The luxury market in general commands very low yields, as low as 1.5 per cent, as the investment play is mostly from a capital appreciation perspective," agrees Stella Abraham, head of residential leasing and relocation services at Jones Lang LaSalle.

Panorama view of Kennedy Town, Hong Kong. The background is Kowloon West

Despite prices that remain unaffordable for the majority, appetite for property continues to remain high across all residential market sectors. "Property prices have reached record high levels. From an affordability perspective, prices are already at 16 times the average household median income level – one of the worst ratios in the world," adds Abraham.

A number of government demand-side management measures have been rolled out in recent years in an attempt to address this issue and cool the overheated property market. Applicable taxes now include a stamp duty of between 1.5 and 8.5 per cent for permanent residents and 15 per cent for non-permanent residents, along with a further 15 per cent buyer's stamp duty for non-PRs; investors looking to flip homes for a quick profit are also subject to a 10 to 20 per cent duty if they have owned a property for less than 24 months.

Yet despite the implementation of these additional fees, Hong Kong's ever-keen buyers remain undeterred. "Since the demand side measures were implemented in 2009, prices have already close to doubled, suggesting that the measures had limited impact on the upward price trend," says Abraham. "There are still many buyers willing to enter the market at this price point – once again, suggesting there is still a demand-supply imbalance in the market."

The statistics back up this supposition, as she forecasts another record year, despite overall stagnant salaries. "The overall market's residential property prices have risen 7.1 per cent through the first four months of 2017. Given the still-upbeat sentiment, we expect prices to rise between 10 and 15 per cent for the full year."

So with prices remaining buoyant, what are the options for would-be homeowners and investors looking to get the best value and choice at the upper end of the market? Adrian To, Swire Properties' director of residential, suggests that diversification could be the answer. "While properties in prime urban locations are constantly sought-after, there is a segment of buyers who look for unique properties found in non-traditional locations," he says. Although located in a rural coastal location that is considered far-flung by most Hong Kongers' standards, Swire Properties' new Whitesands development taps into this demand for higher-end properties in unusual settings. "Located in South Lantau, the buyers of these properties are willing to make a lifestyle investment," To says. The low-density development of 28 detached houses launched in 2016, and with six homes already sold, is spearheading the trend for wealthy buyers frustrated by low supply in more established locations.

And what of those who are looking to purchase property strictly as an investment? Are there quick gains to be made for strategic purchasers? Ryan Jenkins, associate partner at wealth management advisory firm St James' Place, advises a cautious approach. "We generally take a long-term view on investments and would not want to speculate on short-term price movements," he says. "We suggest that any purchase decision should be considered on an individual basis, taking into account an investor's financial position and objectives.

"Investors who are already highly exposed to local properties as a percentage of their asset base and who may employ substantial leverage, for example, mortgages, may be best advised to consider deleveraging and diversifying across other asset classes and geographic exposures to reduce risk."

With the Hong Kong property scene looking unlikely to experience any dramatic changes in the near future, informed research, diversification and a long-term view seem like the way forward for anyone looking to dabble in this most dizzying of markets. P

SHENZHEN PROPERTY
Shenzhen, the Chinese city of nearly 12 million across the border from Hong Kong, has also seen a dramatic rise in prices in recent years. Prices rose more than 70 per cent in the past two years, partly due to the city's reinvention as a Chinese 'Silicon Valley'. With more than 90 per cent of the city's population non-locals, many of them with high-paying jobs, the property market saw huge rises.