

Hong Kong Luxury Residential

FIRST QUARTER 2006

Following a year of fast economic growth in 2005, there is general consensus that Hong Kong's economy, underpinned by continued robust growth in the trade and exports sectors, the tourism and conferencing markets and an expanding financial services industry, should continue to sustain its broad-based expansion in 2006. The upbeat economic outlook, which is already acting to bolster salaries and employment in the SAR, provides solid support on the demand side in the luxury residential market. Meanwhile, as supply is generally limited in this sector over the next several years, we do not anticipate any significant negative pressure on market rents or prices over the short to medium term.

Whilst the steady influx of expatriate employees to Hong Kong is a driving force behind the continued growth of the luxury residential leasing market, the upward revision by corporate end-users of their housing budgets in anticipation of further rise in rentals over the medium term is acting to fuel the acceleration of incremental rise in rental rates. The positive growth of the Consumer Price Index should provide a favourable environment for rentals to pick up further growth momentum in 2006. Indeed, several keynote leasing projects, for

example 2 Barker Road, 29 Severn Road, 8 Severn Road and 1 Barker Road, have either come on stream or are reportedly in the pipeline. Market-sensitive developers appear intend on releasing their projects within this period of positive conditions in the luxury residential leasing market.

The upward revision by corporate end-users of their housing budgets in anticipation of hardening rentals over the medium term would accelerate the rate of luxury residential rental increments.

Yet, despite the upbeat conditions in the leasing market, the same buoyancy has not been observed in the luxury residential sales market. On one hand, sales activities in

the secondary market continue to lag behind the primary market as investors refrain from making financial commitments on the back of the uncertainty which arose as a result of those earlier occasions that saw local banks outpace the US Fed's interest rate hikes by 25 basis points. On the other hand, developers have opted to delay the launch of their respective luxury residential developments as it is expected that market sentiment will improve should signals emerge indicating an end to the interest rate upcycle over the near term. On the positive side, however, it is expected that a further revaluation of the RMB will boost investment sentiment, acting to further drive the luxury residential sales market. Moreover, as Hong Kong has entered into an inflationary period, the role of real estate as a hedge against the uptrend in inflation will become more apparent.

QUICK STATS

	Change in Q4 05	Change in Q1 06
New Supply	↔	↔
Demand	↑	↑
Vacancy Rate	↓	↓
Prime Rents	↔	↑

SELECTED LEASING TRANSACTIONS IN 1Q 2006

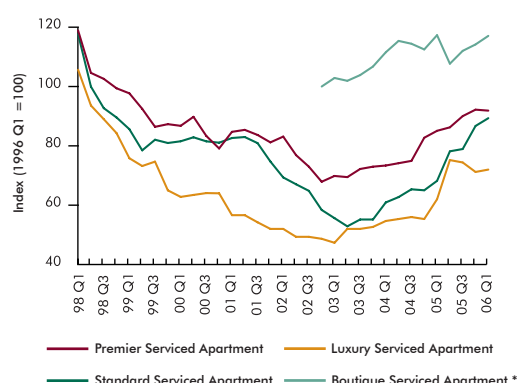
Month	Property	Floor	Location	Size (sf)	Gross Rental (HK\$ per month)	Gross Rental (HK\$ psf per month)
Jan-06	Century Tower 1	Low	Mid-Levels	2,565	68,000	26.51
	The Repulse Bay	High	Island South	2,140	83,500	39.02
	Hongkong Parkview	High	Island South	2,620	105,000	40.08
Feb-06	Dynasty Court	High	Mid-Levels	1,962	65,000	33.13
	Lily Court	Mid	Mid-Levels	720	24,000	33.33
	150 Kennedy Road	High	Mid-Levels East	1,237	50,000	40.42
Mar-06	Bamboo Grove	High	Mid-Levels	1,772	60,000	33.86
	Hillsborough Court	Mid	Mid-Levels	931	35,000	37.59
	Grand Garden	High	Island South	3,054	78,500	25.70

SELECTED SALES TRANSACTIONS IN 1Q 2006

Month	Property	Location	Size (sf)	Price (HK\$ Million)	Price (HK\$ psf)
Jan-06	Unit A, 30/F, Tavistock II	Mid-Levels	2,030	28.53	14,054
	House H, Sunshine Villa	The Peak	2,300	33.80	14,696
	Unit C, 12/F, Celestial Garden	Island South	2,363	28.80	12,188
Feb-06	House C, Wing On Villas	The Peak	2,000	51.50	25,750
	Unit A, 10/F, Block 1, Clovelly Court	Mid-Levels	2,809	31.00	11,036
	Unit 45, 56 Repulse Bay Road	Island South	4,089	57.00	13,940
Mar-06	House 3A, Residence Bel-Air	Island South	4,654	61.22	13,154
	House 8, Severn Hill	The Peak	3,000	58.50	19,500
	Unit B, 36/F, Tower 6, Leighton Hill	Happy Valley	2,167	31.58	14,573

SERVICED APARTMENTS

Serviced Apartment Rental Index



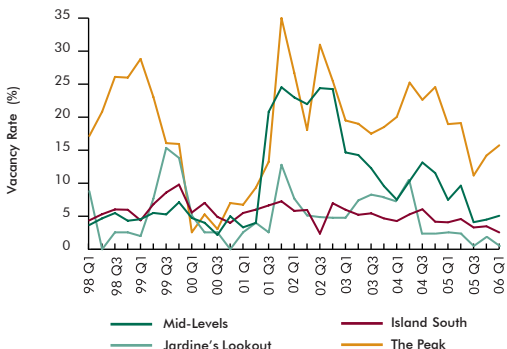
* Boutique Serviced Apartment Index (2002 Q4 = 100)

As a result of the close clustering together as the holiday seasons in year-end 2005 and the Lunar New Year of 2006, some overseas executives of MNCs opted to take their annual leave during the first quarter. This phenomenon acted to release a number of units back to the premier serviced apartment market, as indicated in this sub-segment's q-o-q rise of vacancy from 15.6% to 21.4% and the co-occurring rental slide of 0.4% registered within the same period, the first rental correction since the midst of the SARS outbreak in 2003. Otherwise, broad-based rental rises of 1.1% in luxury, 2.5% in boutique and 3% in standard serviced apartments were registered.

Whilst top-end luxury residential leasing properties are generally resistant to competition from high-end serviced apartments, others are indeed vulnerable to such a challenge. Surveys by CBRE Research indicated an all-inclusive rental difference of less than \$2 psf exists between luxury residential properties and their top-end serviced counterparts. Hence, it is clear that top-tier serviced apartments, offering world-class service and comfort as well as a high degree of flexibility and hassle-free lifestyle, will continue to act as a big draw for new overseas arrivals.

VACANCY

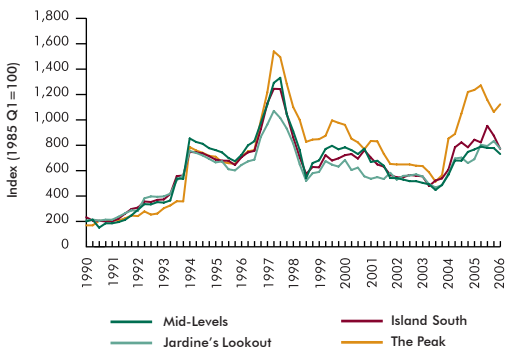
Luxury Residential Vacancy Rate



The overall vacancy rate amongst Hong Kong Island's luxury residential districts in the year's first quarter dropped back down to 3.6% after ticking up in the final quarter of last year, following the similarly low vacancy level of 3.5% registered in the third quarter of 2005. On a district-by-district basis, the vacancy rates at Jardine's Lookout, Island South, Mid-Levels and The Peak at the end of the first quarter stood at 0.5%, 2.6%, 5.1% and 15.7%, respectively. Jardine's Lookout saw the biggest q-o-q compression in vacancy with a drop of 1.4 percentage points, whilst The Peak saw its rate tick up by the largest amount, with vacancy rising by 1.6 percentage points.

SALES MARKET

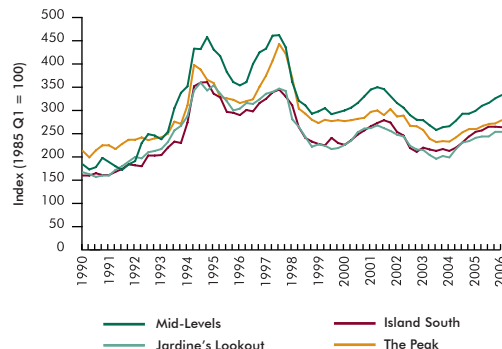
Luxury Residential Capital Value Index



While the stronger financial position of buyers of luxury residences made them less vulnerable to present hikes in mortgage interest rates, potential investors have nevertheless remained on the sidelines awaiting signals that might indicate a winding down of the prevailing interest rate upcycle. Meanwhile, the real estate market was dominated by the marketing of mass residential projects in the first quarter. The confluence of these factors resulted in relative inactivity in the luxury residential sales market within the period, leading to a further correction of 3.9% in average capital values across Hong Kong Island. While retreats in price of between 6.1% and 12.2% were recorded in Mid-Levels, Jardine's Lookout and Island South, prices in The Peak rose by 5.6%, q-o-q.

LEASING MARKET

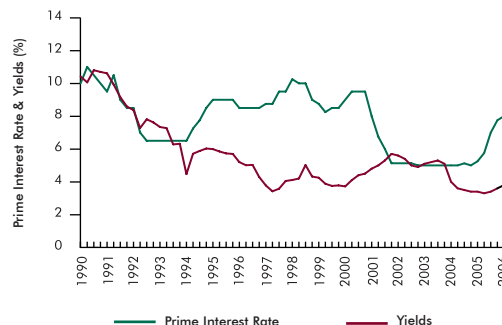
Luxury Residential Rental Index



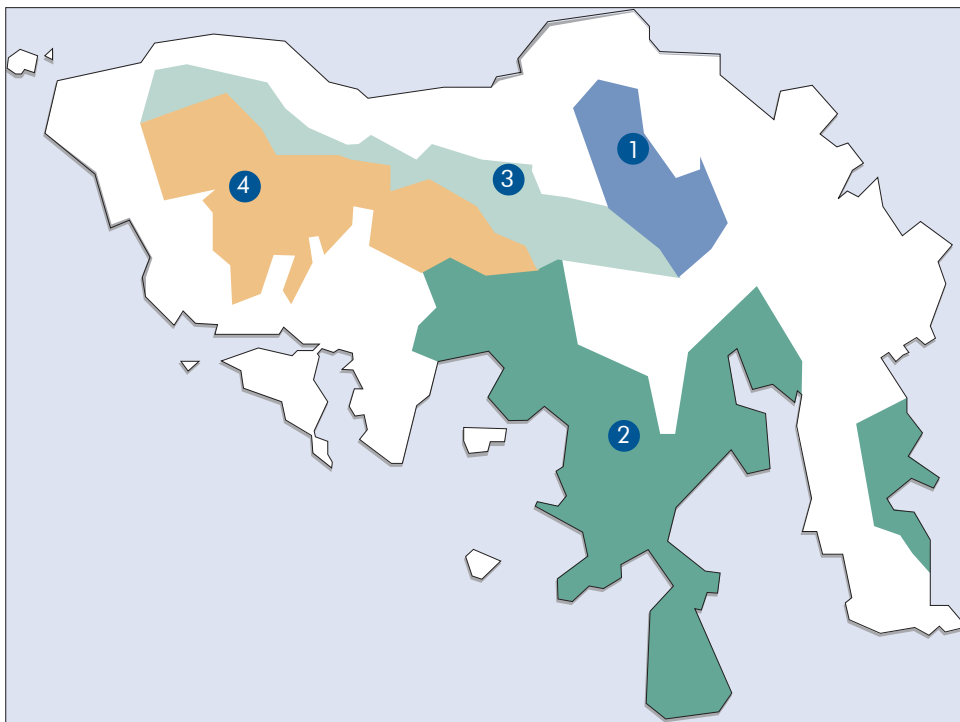
The first quarter is not generally the year's peak season for luxury residential leasing, as a number of landlords often have other priorities between the end of the calendar year in 2005 and the Lunar New Year in 2006. Meanwhile, a large number of MNCs prefer to relocate their expatriate staff to Hong Kong towards the end of the first quarter or early in the second quarter as part of their plans for the new financial year. Therefore, a mild q-o-q rental rise of 1.2% was registered on Hong Kong Island overall during the first quarter. Whilst The Peak and Mid-Levels registered growth of 2.5% and 2.1%, respectively, achieved rentals in Jardine's Lookout and Island South remained relatively unchanged.

YIELDS

Luxury Residential Yields



The prime interest rate increased by just 25 basis points during the first quarter, the smallest quarterly increment witnessed since the onset of the current interest rate hike cycle a year ago. While luxury residential property buyers are generally less reliant on mortgage borrowing, the persisting interest rate hike cycle is nevertheless expected to continue to dampen capital value performance. At the same time, rental growth of luxury residential properties is set to accelerate remarkably on the back of the broadening economic upswing, which, in turn, will prompt upward growth in yields in 2006. The uptrending yield of 3.8% registered in the first quarter was the highest achieved since the first quarter of 2004.



HONG KONG LUXURY RESIDENTIAL SUBMARKET DESCRIPTIONS

- 1. JARDINE'S LOOKOUT/TAI HANG** Medium low-rise, Medium low density
- 2. ISLAND SOUTH** Low-rise, low density
- 3. MID-LEVELS** High-rise, high density
- 4. THE PEAK** Low-rise, low density

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USEFUL INFORMATION WHEN LEASING RESIDENTIAL PROPERTY

RENTAL:

This is always referred to as monthly rental, and is payable monthly, in advance, by the tenant to the landlord.

RATES:

This is a tax charged by the Hong Kong Government and is usually paid by the tenant, unless the landlord has leased the property on inclusive rental terms. The charge is paid as a percentage of the 'rateable value' of the property, which is fixed by the Hong Kong Government.

MANAGEMENT FEES:

Unless paying an inclusive rental, this is charged to the tenant and usually covers building maintenance and cleaning services.

STAMP DUTY:

On leasing, this is divided equally between the tenant and the landlord, but on sale this is paid totally by the purchaser.

LEGAL FEES:

Each party bears its own legal costs.

DEPOSIT:

This usually takes the following form, but may vary between landlords:

- An initial one month's rental deposit immediately upon terms being agreed;
- two further months' deposit upon signing of the Tenancy Agreement.

Amounts required when signing the Tenancy Agreement:

1. First month's rental
2. First month's rates and management fees
3. Two months' rental as deposit
4. Electricity / Gas / Telephone deposit
5. Agent's fee
6. Stamp Duty

NB: The above can vary depending on the landlord and the lease terms agreed.