

MarketView

Hong Kong Industrial

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Third Quarter 2008

Quick Stats

		Y-o-Y change	Q-o-Q change
Warehouse Rental Value	HK\$6.9 psf	↑	↓
Warehouse Capital Value	HK\$1,070 psf	↑	↔
Warehouse Vacancy Rate	1.6%	↓	↑
I/O Rental Value	HK\$11.8 psf	↑	↓
I/O Capital Value	HK\$2,906 psf	↑	↓
Factory Rental Value	HK\$7.6 psf	↑	↓
Factory Capital Value	HK\$1,354 psf	↑	↑

* The arrows are trend indicators over the specified time period and do not represent a positive or negative value.

Hot Topics

- The deteriorating growth of merchandise exports value reflected a broad-based import demand moderation from Hong Kong's major trading partners.
- Warehouse leasing activity sustained a somewhat stable performance. The persistently low vacancy and a lack of new supply have softened the downward pressure on rents.
- I/O properties are set to gradually lose their market appeal as the abundant supply of new quality office space in former industrial locations provides more available space at competitive rents.
- The overall factory property market was relatively active due to demand from users seeking large floor space for non-production uses.

Amid the slowdown of the world economy, in Hong Kong, the value of total exports of merchandise increased to \$247.9 billion while the value of re-exports grew to \$239.8 billion in August 2008. Concurrently, the total exports and re-exports of goods captured a y-o-y increase of 1.9% and 2.7%, respectively, according to the latest government figures. These performances moderated after the double-digit growth in July, a result of considerable fluctuations on exports over the past few months. For the first eight months of 2008, total exports grew by 8.3% y-o-y. Within this total, the value of re-exports increased by 9.1% y-o-y. Both performances were comparatively weaker than growth in the corresponding period of 2007 when they were 9.8% y-o-y and 12.1% y-o-y, respectively.

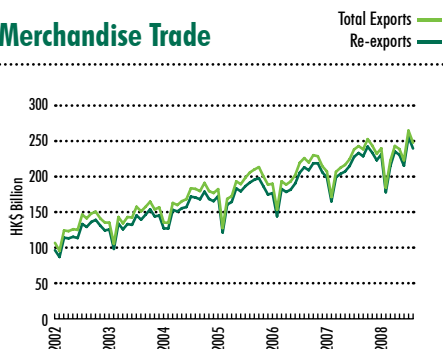
The apparent deteriorating growth of merchandise exports value reflected a broad-based moderation in external demand from Hong Kong's major trading partners. In particular, exports to European and emerging Asian economies started to decline while imports demand remained weak in the US and Japan. That said, the robust consumption and manufacturing activities on the Mainland comprised the only support to Hong Kong's re-export trade. Weakening demand in Western markets for Asian goods has effectively destroyed the idea that Asia can decouple from an economic downturn in these markets. Hong Kong's exports are set to slow for the rest of the year and possibly 2009 on the back of the ensuing impact on the export-dependent Asia, which will inevitably

affect China's relatively strong underlying business fundamentals.

Hong Kong's industrial property market remained on its consolidation course under the influence of the current financial woes. As many investors continue to fret about the broader economic impact and a possible global recession, they adopted a "wait-and-see" attitude towards investment in this sector. The industrial strata-title sales market was so static that despite the at least 5.5% - 6% yield which is now quite common in this sector, such high yielding properties failed to attract strong interest from investors. Leasing transactions in traditional industrial areas including Sha Tin, Yuen Long, and Fanling were relatively active. Both rents and prices had fair support from constant user demand as the supply of quality industrial properties was finite, limiting property value corrections to less than 1.3% q-o-q in general. Although the warehouse vacancy rate increased by 30 basis points to 1.6% in the third quarter, it was still 70 basis points lower than the record set 12 months ago.

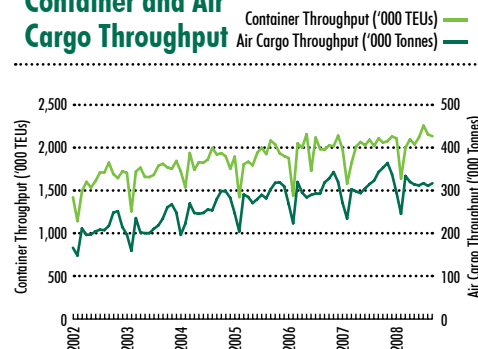
The much weaker global economy is envisaged to slash Hong Kong's merchandise trade growth to mid-single-digit rate at best in 2009. Should this much reduced growth combine with the negative impact on consumption from the sharp correction in asset markets, the combined force will bring 2008 GDP growth below the 10-year trend of 3.8% growth for the first time since the SARS epidemic of 2003.

Merchandise Trade



Source: Census & Statistics Department

Container and Air Cargo Throughput



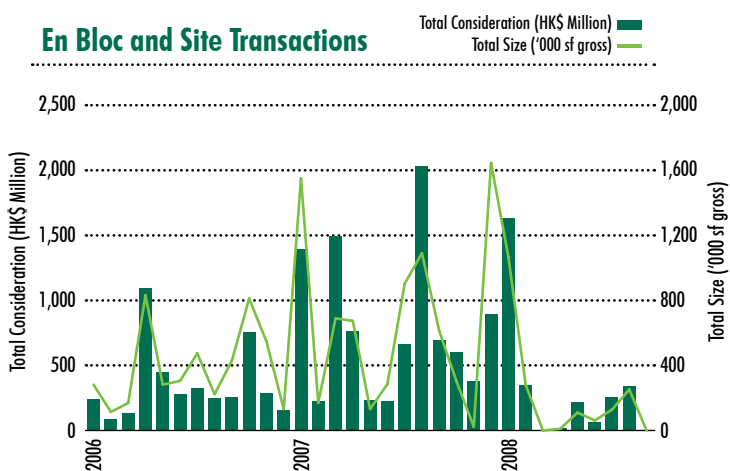
Source: Marine Department; Civil Aviation Department

Selected Leasing Transactions in Q3 2008

Property	Floor	Location	Type	Size (sf)	Gross Rental (HK\$ psf per month)
Tsuen Wan International Centre	15/F & 16/F	Tsuen Wan	Industrial	42,539	5.5
Wo Kee Hong Building	Units A-D, 14/F	Kwai Chung	Industrial	12,444	5.7
Sino Favour Centre	5/F	Chai Wan	I/O	12,687	9.0
Midas Plaza	3/F	San Po Kong	Industrial	10,710	15.5
Yiuga Factory Building	Units A-B, 2/F, 3/F & Unit B, 4/F	Kennedy Town	Industrial	11,709	6.7
Sea View Estate Block B	Unit 3, 3/F	North Point	Industrial	10,611	8.4

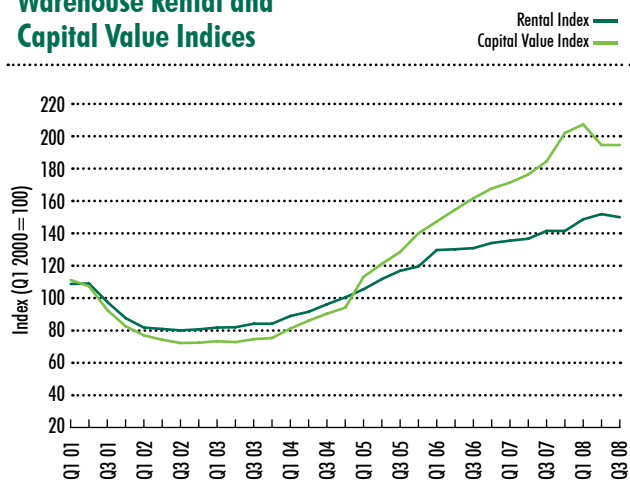
Selected Sales Transactions in Q3 2008

Property	Floor	Location	Type	Size (sf)	Price (HK\$ Million)	Price (HK\$ sf)
Wang Fai Industrial Building	3/F & 4/F	San Po Kong	Industrial	28,698	30.00	1,045
Regent Centre Tower B	6/F	Kwai Chung	Industrial	20,473	27.00	1,319
Safety Godown	11/F	Chai Wan	Warehouse	36,470	32.00	877
World Tech Centre	16/F	Kwun Tong	Industrial	23,818	52.40	2,200
Hing Wai Centre	24/F	Aberdeen	Industrial	27,999	39.20	1,400
Southeast Industrial Building	Units A-E, 6/F	Tsuen Wan	Industrial	26,573	25.97	977



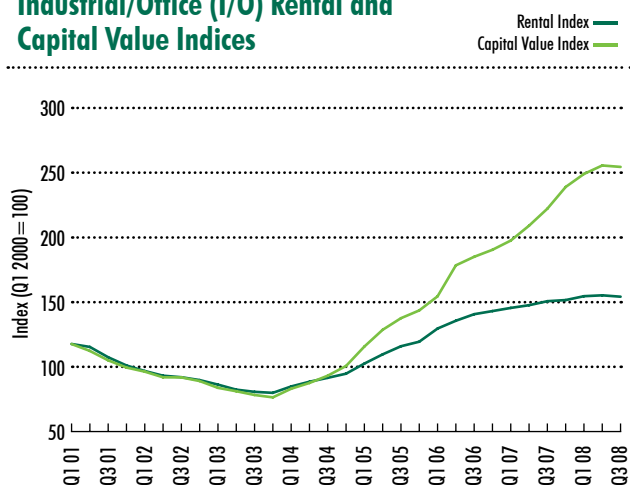
The total consideration involved in industrial en bloc transactions in the third quarter amounted to about \$604 million. Although this almost doubled the total transacted values concluded in the previous quarter, the overall performance on a year-to-date basis was indeed 62.6% below that over the same period last year. Concurrently, a similar year-to-date contraction of 68.7% was also noted in terms of total size involved in industrial en bloc transactions. The gloomy international trade prospects prompted many investors to become more conservative towards industrial en bloc acquisitions as did the banks' appetite to fund these acquisitions. The tightened credit controls had effectively limited market activity to fiscally sound local buyers only, regardless of their intention to acquire these premises for either redevelopment or long-term investment purposes.

Warehouse Rental and Capital Value Indices



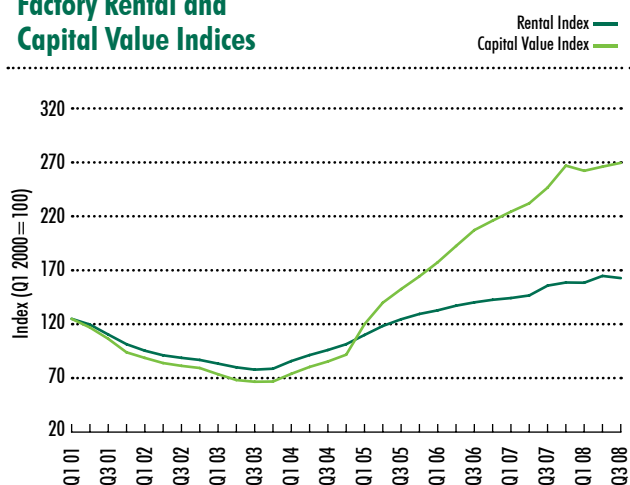
Warehouse leasing activity in the review period sustained a somewhat stable performance amid the deteriorating trade flows. Vacancy in warehouses with advanced support facilities remained low, and a lack of new supply has thus far helped to soften the downward pressure on rents despite the fact that landlords have allowed more room for negotiation. Warehouse rents consolidated slightly at 1.3% q-o-q while prices flat-lined in the third quarter. Although the overall warehouse market sentiment has become subdued, some positive aspects persist in the longer run: the relatively softened energy prices, minimal new supply at least until 2010 and the government's supportive measures in funding the construction of infrastructure projects. These positive factors should combine to provide a certain degree of optimism to this user-driven market.

Industrial/Office (I/O) Rental and Capital Value Indices



Although the flexible use of I/O properties, especially as a practical alternative to office properties, attracted some foreign investors and local buyers in previous quarters, both prices and rents came under pressure in the third quarter, particularly in the Kowloon East and Cheung Sha Wan areas where Grade A office rents have now begun to soften. Their abundant supply of new quality office space also warrants the availability of space at competitive rents. I/O properties are set to lose their market appeal as a result. A brand new I/O development in Kwun Tong obtained its Occupation Permit in August, adding some 71,000 sf to Hong Kong's overall I/O stock of about 6.6 million sf. The third quarter saw both rents and prices of I/O properties drop slightly by 0.7% q-o-q and 0.4% q-o-q, respectively.

Factory Rental and Capital Value Indices



The overall factory property market was relatively active during the review period as compared with previous quarters. The demand for space continued to emerge mainly from users seeking large floor space for non-production uses. That said, the uncertainties stemming from the current global financial strain remained a concern to many, and the worries kept factory property values in consolidation despite improved market activity. A mild rental retreat of 1.2% q-o-q was registered in the third quarter. Yet, the average prices of factory properties increased slightly by 1.3% q-o-q, likely reflecting the solid demand from users seeking to hold large floor space assets for their own use.

Major Hong Kong Industrial Areas



— Hong Kong Island — South East Kowloon — Western Kowloon — The New Territories

Major Industrial Districts in Hong Kong

Kwun Tong

A former industrial precinct gradually transforming to a decentralised office node. Still, the area holds considerable share of Hong Kong's industrial stock, particularly in the I/O sector (36.9%) given their industrial cum commercial nature. Meanwhile, the area is also home to about 7.9% of warehouse space and 19.2% of factory stock, in Hong Kong.

Kwai Tsing/Tsuen Wan

As the area is in close proximity to the Container Terminals in Kwai Chung and Tsing Yi while strategically linked to the Hong Kong International Airport by the Tsing Ma Bridge, many logistics players opt to cluster in the area for its convenient access to these facilities. As a result, over 52% of Hong Kong's warehouse space is found in the Kwai Tsing and Tsuen Wan districts. In addition, about 18.3% of Hong Kong's I/O space and 32.2% of factory stock are located in these districts.

Tuen Mun

As the River Trade Terminal is near the area, this traditional industrial district is also popular among Hong Kong's logistics players. Currently, the district holds about 4.2% of Hong Kong's warehouse space while some 8.1% of the SAR's factory stock is in the area.

Yuen Long

Yuen Long's share of industrial property stock within Hong Kong is limited to about 3.4% of warehouse stock and 1.2% of factory space, respectively. Yet, the area is gaining wider market acceptance from logistics users who value its easy access to the Hong Kong landing point of the Deep Bay Link. The Deep Bay Link, opened in July 2007, is the fourth vehicular access connecting Hong Kong to Shenzhen within the Pearl River Delta.

Sha Tin

The area has traditionally been an important logistics hub in terms of rail-based cargo shipment in addition to its role as Hong Kong's major precinct of manufacturing activities. Currently, about 13.3% of warehouse stock, 6.3% of I/O stock and 6.5% of factory stock are located in Sha Tin.

Industrial Property Definitions

Warehouse:

This category comprises premises designed or adapted for use as godowns or cold stores and includes ancillary offices. Premises located within the container terminals are also included. About 80% of the stock is located in the New Territories, with Kwai Tsing/Tsuen Wan alone accounting for over 52 per cent.

Industrial/Office (I/O):

This category comprises floor space in developments with planning permission and lease modification for industrial/office use and certified for occupation as such. The stock is distributed in 11 districts throughout the territory, with Kwun Tong, Shum Shui Po and Kwai Tsing, accounting for more than 70 per cent of the total floor space.

Factory:

This category comprises flatted factories and ancillary office accommodations. It includes flatted factory space that has received planning permission for industrial/office use but has not yet completed the government lease modification. Also included in this category is strata-title floor space with temporary planning permission for industrial/office use and short-term waivers of government lease restrictions. It should be noted that much of the flatted factory space completed in recent years has been built to a high standard with good finishes. Although many factory buildings are occupied as offices, showrooms, or a mixture of these uses and light industrial purposes, they should be distinguished from buildings with proper industrial/office status. The majority of the stock is found in four districts of Hong Kong, namely Kwun Tong, Tsuen Wan, Kwai Tsing and Tuen Mun, which account for 60 per cent of the total supply.

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