

The industrial property market continued to register buoyant performance though the pace has moderated. Although Hong Kong's total export market has been sustained by robust intra-regional trade between the Mainland and other Asian countries, the continued weakening in the US economy and the prevailing global financial turmoil has inevitably impacted macro consumer sentiment. According to the latest government figures, the value of Hong Kong's total exports of goods increased 7.6% y-o-y to \$184.4 billion

Cross-strait links between China and Taiwan may pose challenges to Hong Kong's transit role, but industrial properties should remain popular for their redevelopment potential.

in February 2008; within this total, the value of re-exports increased by 7.8% y-o-y to \$178.1 billion. Despite the annual growth, the trade flows in both January and February showed considerable volatility due in part to seasonal factors but also to a certain extent by a combination of the sluggish US market and the severe winter storms that hit China in early 2008.

The slowdown in the US economy and its ripple effects on the global economy are starting to have an influence on China's exports. For instance, export growth to the US registered at 6.5% y-o-y in February, compared with 26.6% y-o-y in January, narrowing China's trade surplus for the month to US\$66.8 billion from US\$152.1 billion the previous month. The reduction in growth was generally due to the appreciation of RMB, increasing fuel prices and rising wages, which have driven up manufacturing costs. Portions of foreign purchasing orders have been diverted to other countries with lower costs such as Vietnam, India and even Cambodia. As merchandise trade related to the Mainland accounted for the major portion of the SAR's total exports (46.3% in

2007), logistics players in Hong Kong are expected to encounter some challenges due to the uncertain global outlook in 2008.

Another challenge to the Hong Kong industrial market would be the establishment of direct links between Mainland China and Taiwan proposed by the Taiwanese President-elect Ma Ying-jeou. These links could include direct flights, tourism, economy and trade; and Ma is proposing to have the first direct flight from Taiwan to the Mainland in this July.

Traditionally, Hong Kong has been the transit hub between the Mainland and Taiwan. If cross-strait links are established, resulting in direct economic, trade and transport activities between the two countries, Hong Kong's transit role would be subject to severe immediate challenge.

Nevertheless, the Hong Kong industrial market still has considerable support even amid the current uncertain global financial environment. For instance, exports to Asia registered considerable growth; India recording the strongest y-o-y growth of 126.6%, followed by Vietnam at 42.1%. Demand for industrial properties can be sustained by logistics players who are adding capacity to serve the strong growth from these emerging economies. Other support comes from developers seeking to acquire industrial properties with redevelopment potential as hotels, following the government's announcement of favourable policies towards the hotel industry and tourism promotion in February. As the supply of new industrial space will remain at a low level over the medium-term, the value of industrial properties is expected to remain stable.

QUICK STATS

	Change in Q4 07	Change in Q1 08
WAREHOUSE		
Demand	↑	↔
Supply	↔	↔
Rents	↔	↑
Vacancy Rate	↓	↑
INDUSTRIAL/OFFICE		
Demand	↑	↔
Supply	↔	↔
Rents	↑	↑
Capital Values	↑	↑
FACTORY		
Demand	↑	↔
Supply	↔	↔
Rents	↑	↓
Capital Values	↑	↓

SELECTED LEASING TRANSACTIONS IN 1Q 2008

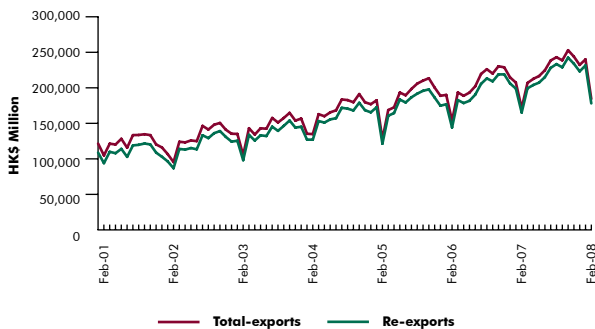
Property	Floor	Location	Type	Size (sf)	Gross Rental (HK\$ psf per month)
Safety Godown Industrial Building	2/F	Chai Wan	Industrial	41,500	7.7
QPL Industrial Building	Units 1-8, 11/F	Tsuen Wan	Industrial	21,083	4.2
Tsuen Wan International Centre	Unit E, 29/F	Tsuen Wan	Industrial	4,001	5.8
Remex Centre	17/F	Wong Chuk Hang	Industrial	10,543	5.3
Unison Industrial Centre	Units C & D, 15/F (including Carpark No. 35)	Sha Tin	Industrial	11,850	7.1
Wo Kee Hong Building	Unit B, 14/F	Kwai Chung	Industrial	3,440	4.2
Harbour Centre, Tower 1	Unit 1, 5/F	Hung Hom	Industrial	6,172	10.9

SELECTED SALES TRANSACTIONS IN 1Q 2008

Property	Floor	Location	Type	Size (sf)	Price (HK\$ Million)	Price (HK\$ psf)
Wang Fai Industrial Building	16/F	San Po Kong	Industrial	10,642	11.00	1,034
Tuen Mun Industrial Centre, Block F	Unit F2, 3/F	Tuen Mun	Industrial	11,026	4.98	452
Yau Lee Centre	7/F	Kwun Tong	Industrial	14,980	24.72	1,650
Trans Asia Centre	Units 3-10, 2/F	Kwai Chung	Industrial	11,369	10.50	924
CCT Telecom Building	Units 1-3 & 5-10, 15/F	Sha Tin	I/O	14,427	36.06	2,500

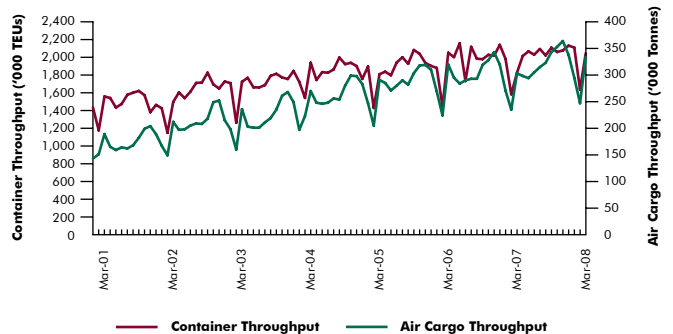
ECONOMIC INDICATORS

Merchandise Trade



Source: Census & Statistics Department

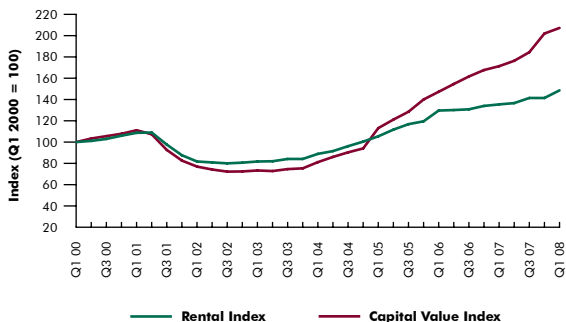
The Container and Air Cargo Throughput



Source: Marine Department; Civil Aviation Department

WAREHOUSE

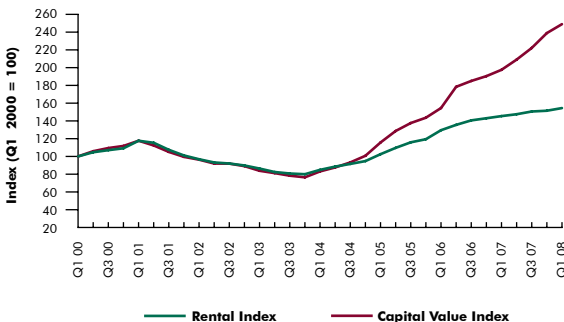
Warehouse Rental and Capital Value Indices



Warehouse leasing activities in the first quarter remained stable, as a wide spectrum of industries were impacted to varying degrees by the unusually severe winter storms that crippled transportation networks in much of China in early 2008. Mainland exports to the US were affected by slowing demand as well as these temporary seasonal factors, impacting Hong Kong’s re-exports performance. Though the value of re-exports rose 12.5% y-o-y in the first two months of 2008, the performance was almost 100 basis points below the y-o-y growth registered in the same two-month period in 2007. Slowing re-exports could be among the factors driving a slight increase in overall warehouse vacancy, which rose 0.1% q-o-q to 1.7%, notwithstanding stable demand. Nevertheless, both rents and capital values registered reasonable gain in the quarter, rising 5.1% and 2.6% q-o-q, respectively.

INDUSTRIAL/OFFICE (I/O)

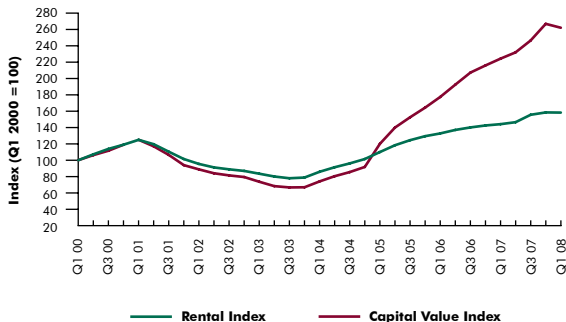
Industrial/Office Rental and Capital Value Indices



I/O properties continued to be welcome by professional investors in the industrial property sector on the back of the dual purposes of these premises, which offers flexibility in utilising the space. A notable transaction was the acquisition of 14,427 sf of floor space in CCT Telecom Building in Sha Tin by a local individual investor for \$36.06 million. Notwithstanding the mixed-use nature of I/O buildings, developers holding industrial land bank with redevelopment potential are likely to opt to realise such potential through other property types, and therefore no new I/O property is anticipated to be available in the market. For instance, Billion Development paid a \$1 billion premium for the rights to develop a 30-storey commercial building on the site of the former Sing Tao Building in Kowloon Bay. The rental value of I/O properties recorded growth of 2% q-o-q while capital value registered quarterly growth of 4.2% in the first quarter.

FACTORY

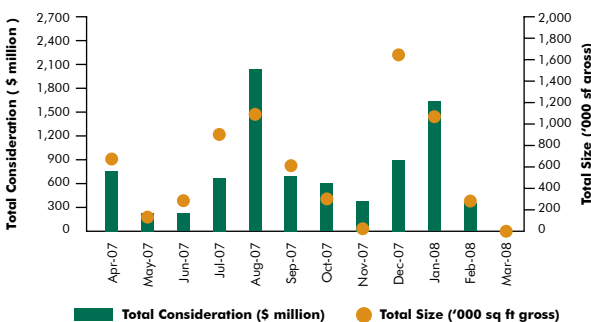
Factory Rental and Capital Value Indices



Factory became the first industrial property type to experience a consolidation in the first quarter of 2008 after recording continued robust growth since 2004. During the period under review, factory premises posted a slight drop in both rental and capital values, which fell 0.1% and 1.8%, respectively. Due to the mild adjustment in both rents and prices, the yield of factory properties edged upward, rising from 6.6% to 6.7%. As the global economy is full of uncertainties that may dampen demand in the industrial property market, potential buyers tended to adopt a “wait-and-see” attitude, resulting in a relatively mild level of activity in the market. A notable transaction involved the acquisition of 14,980 sf of space in Yau Lee Centre in Kwun Tong by a local company for \$24.72 million.

EN BLOC & SITE TRANSACTIONS

En Bloc and Site Transactions



The total consideration and total size involved in industrial en bloc transactions in the first quarter were \$1.98 billion and 1.35 million sf, respectively. Compared with the figures from the final quarter of 2007, the total consideration increased 5.7% although total transacted floor size dropped almost 32%. Local buyers continued to dominate the industrial en bloc market. Notable en bloc transactions saw the 408,000-sf Piazza Industrial Building in Kwun Tong change hands for \$600 million, or \$1,470 psf; and the 311,704-sf Oriental News Building in Kowloon Bay sold for \$525 million, or \$1,684 psf. Demand from developers for sites with re-development potential is likely to provide the dominant support to transacted values in the short- to medium-term, particularly since the government is now quite keen to encourage all kinds of hotel development, including business hotels in certain former industrial districts where land use is being changed to non-industrial uses.



MAJOR HONG KONG INDUSTRIAL AREAS

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

ASIA OFFICES

Hong Kong
34/F Central Plaza
18 Harbour Road, Wanchai
Hong Kong
Telephone: (852) 2820 2800
Facsimile: (852) 2810 0830

Suite 2109-12, 21/F
Sun Life Tower, The Gateway
15 Canton Road, Tsimshatsui
Kowloon, Hong Kong
Telephone: (852) 2820 8100
Facsimile: (852) 2521 9517

Beijing
Suite 1203-1205, 12/F, Tower A
Beijing Fortune Plaza
7 Dong San Huan Middle Road
Chaoyang District
Beijing 100020
People's Republic of China
Telephone: (86) 10 5820 9288
Facsimile: (86) 10 5820 9088/9188

Shanghai
Suite 3201, 3203-3206
32/F, K. Wah Center
1010 Huai Hai Middle Road
Shanghai 200031
People's Republic of China
Telephone: (86) 21 2401 1200
Facsimile: (86) 21 5403 7519

Suite 1004, 10/F
Azia Center
1233 Lu Jia Zui Ring Road
Shanghai 200120
People's Republic of China
Telephone: (86) 21 2401 1200
Facsimile: (86) 21 5047 1171

Guangzhou
Suite 1401-1402, Guangzhou
International Electronics Tower
403 Huan Shi East Road
Guangzhou 510095
People's Republic of China
Telephone: (86) 20 2883 9200
Facsimile: (86) 20 2883 9248

Shenzhen
Suite 2404-05
Excellence Times Square Building
Yi Tian Road, Futian District
Shenzhen 518048
People's Republic of China
Telephone: (86) 755 3395 3700
Facsimile: (86) 755 2399 5370

Hangzhou
Suite 1201, 12/F, North Tower
Anno Domini Plaza, 8 Qiu Shi Road
Hangzhou 310013
People's Republic of China
Telephone: (86) 571 2880 6818
Facsimile: (86) 571 2880 8018

Chengdu
Suite 704A-706, Office Tower at
Shangri-La Centre Chengdu, Block B
9 Bin Jiang East Road, Chengdu 610021
People's Republic of China
Telephone: (86) 28 8447 0022
Facsimile: (86) 28 8447 3311

Tianjin
Suite 903, Tower A, The Exchange
189 Nan Jing Road, Heping District
Tianjin 300051
People's Republic of China
Telephone: (86) 22 8319 2178
Facsimile: (86) 22 8319 2180

Dalian
Suite 2104, 21/F
Tian An International Tower
88 Zhong Shan Road, Zhongshan District
Dalian 116001
People's Republic of China
Telephone: (86) 411 3980 5855
Facsimile: (86) 411 3980 5866

Qingdao
Units 401-404, Crowne Plaza
76 Hong Kong Middle Road
Shinan District, Qingdao 266071
People's Republic of China
Telephone: (86) 532 8077 7286
Facsimile: (86) 532 8077 7267

Wuhan
Suite 3915, 39/F, Wuhan New World
International Trade Centre, Tower 1
568 Jian She Avenue, Wuhan 430022
People's Republic of China
Telephone: (86) 27 8555 8277
Facsimile: (86) 27 6885 0506

Taipei
13F/A, Hung Tai Center
170 Tun Hua North Road
Taipei 105, Taiwan
Telephone: (886) 2 2713 2266
Facsimile: (886) 2 2712 3065

Singapore
6 Battery Road #32-01
Singapore 049909
Telephone: (65) 6224 8181
Facsimile: (65) 6225 1987

Tokyo, Japan
5/F Shuwa Daiichi Hamamatsucho Building
2-2-12 Hamamatsucho, Minato-ku
Tokyo 105-0013, Japan
Telephone: (81) 3 5470 8711
Facsimile: (81) 3 5470 8715

1/F Shuwa Daiichi Hamamatsucho Building
2-2-12 Hamamatsucho, Minato-ku
Tokyo 105-0013, Japan
Telephone: (81) 3 5470 8800
Facsimile: (81) 3 5470 8801

*18 offices throughout Japan

Seoul, Korea
12/F, SC First Bank Building
100 Gongpyeong-dong, Jongno-gu
Seoul, Korea 110-702
Telephone: (822) 2170 5800
Facsimile: (822) 2170 5899

New Delhi, India
G/F RTI Building
4 Parliament Street
New Delhi 110 001, India
Telephone: (91) 11 4239 0200
Facsimile: (91) 11 2331 7670

Mumbai, India
#5, 3/F Tower C, Laxmi Towers
G-block, Bandra Kuria Complex
Bandra (E), Mumbai 400 051, India
Telephone: (91) 22 4069 0100
Facsimile: (91) 22 2652 7655

Bangalore, India
3/F The Hulkul
81/37, Lavelle Road
Bangalore 560 001, India
Telephone: (91) 80 4112 1240-49
Facsimile: (91) 80 4112 1239

Chennai (Madras), India
2H, 2/F Gee Gee Emerald 2C & 2D
151 Village Road, Nungambakkam
Chennai 600 034, India
Telephone: (91) 44 2821 4599/4571
Facsimile: (91) 44 2821 4607

Hyderabad, India
211, Maximus 2B, Mindspace Cyberabad
Survey No: 64 (Part)
APPLIC Software Layout, Madhapur
Hyderabad 500 081, India
Telephone: (91) 40 4033 5000
Facsimile: (91) 40 4033 5050

Pune, India
705-706, 7/F Nucleus
Church Road
Pune 411 001, India
Telephone: (91) 20 2605 5437/5367
Facsimile: (91) 20 2605 5405

Jakarta, Indonesia
7/F Permata Bank Tower I
Jalan Jenderal Sudirman Kav. 27
Jakarta 12920, Indonesia
Telephone: (62) 21 523 7337
Facsimile: (62) 21 523 7227

Manila, Philippines
Suite 1002-1005,
10/F Ayala Tower One &
Exchange Plaza
Ayala Avenue, Makati City
Metro Manila 1226, Philippines
Telephone: (632) 752 2580
Facsimile: (632) 752 2571

Cebu, Philippines
3/F, 12 Building
Asiatown I.T. Park, Lahug
Cebu City, Philippines 6000
Telephone: (632) 238 4211

Bangkok, Thailand
46/F CRC Tower
All Seasons Place
87/2 Wireless Road
Lumpini, Pathumwan
Bangkok 10330, Thailand
Telephone: (66) 2 654 1111
Facsimile: (66) 2 685 3300-1

Phuket, Thailand
12/9 Moo 4, Thepkrasattri Road
Kohkaew, Muang
Phuket 83000, Thailand
Telephone: (66) 76 239 967
Facsimile: (66) 76 239 970

Samui, Thailand
3/6 Moo 1, Baan Bophut -
Plaiqaem Road
Bophut, Koh Samui
Surat Thani 84920, Thailand
Telephone: (66) 77 430 737
Facsimile: (66) 77 430 740

Pattaya, Thailand
306/96-97 Moo 12 Thapraya Road,
Nongpaire, Banglamung
Chonburi 20150, Thailand
Telephone: (66) 77 430 737
Facsimile: (66) 77 430 740

Ho Chi Minh City, Vietnam
Suite 1301, Me Linh Point Tower
2 Ngo Duc Ke Street, District 1
Ho Chi Minh City, Vietnam
Telephone: (848) 824 6125
Facsimile: (848) 823 8418

Hanoi, Vietnam
Floor 12A, Vincom City Tower B
191 Ba Trieu Street
Hanoi, Vietnam
Telephone: (844) 220 0220
Facsimile: (844) 220 0210

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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 alone accounting for 40 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.