

Hong Kong Luxury Residential

FIRST QUARTER 2008

Local economic performance remained strong on the back of a consistently falling unemployment rate and rising wages, but the luxury residential property market seemed unlikely to maintain the same pace of growth from the previous quarter. The fluctuating external economic environment triggered by the global credit crunch has been clouding the outlook of the investment market worldwide, and it has become clear that the US will experience a recessionary period in 2008 which could continue well into 2009.

Investors were less aggressive in their efforts to acquire luxury residential properties this quarter amid the threat of US economic slowdown.

Market sentiment has been cooling during the first three months of 2008. The average capital value of luxury residential properties on Hong Kong Island registered quarterly growth of only 8.5%, which, though respectable, appeared moderate in comparison to the 15.5% surge in the fourth quarter of 2007. According to the Land Registry, both transaction volume and prices for residential premises fell sharply this quarter, registering q-o-q reductions of 8.9% and 17.3%, respectively.

Local investors were less aggressive in acquiring luxury residential properties this quarter amid the threat of US economic slowdown. The new labour law, along with surging labour costs, the appreciating RMB and restrictive environmental measures in Mainland China could lead to a wave of factory closures. This would both negatively affect Hong Kong's re-exports and raise Hong Kong industrialists' concerns over their business prospects, leading both local traders and

industrialists to adopt a "wait-and-see" attitude on property investments with a view to preserving the flexibility of their capital flows. Meanwhile, some developers are now taking advantage of the current high capital values of Hong Kong luxury residential properties, opting to sell their leasing portfolios on a strata-title basis. The most notable example was Sun Hung Kai Properties' Tower 4 of Hillsborough Court, The Royal Tower, in Mid-Levels, which has achieved a reported unit rate of around \$20,000 psf.

Despite the widespread difficulties in the financial services sector, to date there have been few indications in the market that institutions would forego incentive compensation in Hong Kong. Fortunately, supported by strong underlying fundamentals in terms of continued supply constraints and low borrowing costs, the purchasing power of Hong Kong residents should remain robust. It is believed that the cooling of the property market is a short-term concern, and savvy players are seeking to time the inevitable rebound of market confidence. The performance of Hong Kong's luxury residential property market should regain momentum when the local economy emerges from the shadow of the US subprime debt crisis. The highest acquisition rate ever offered by the Urban Renewal Authority, \$9,986 psf, for 24 old buildings located along Staunton Street and Wing Lee Street in Central has signalled that the prospects for Hong Kong's luxury residential properties are still positive in the long-run.

QUICK STATS

	Change in Q4 07	Change in Q1 08
New Supply	↑	↓
Demand	↑	↔
Vacancy Rate	↓	↔
Prime Rents	↑	↑

SELECTED LEASING TRANSACTIONS IN 1Q 2008

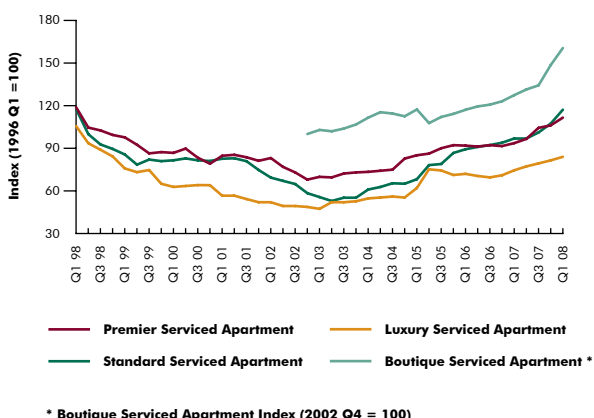
Month	Property	Floor	Location	Size (sf)	Gross Rental (HK\$ per month)	Gross Rental (HK\$ psf per month)
Jan-08	Flat A, 17/F, Celestial Gardens	High	Island South	2,375	115,000	48.42
	Flat A, 46/F, Aigburth	High	Mid-Levels	3,080	175,500	56.98
Feb-08	House B, 59 Mt. Kellett Road	House	The Peak	3,286	220,000	66.95
	Flat B, 18/F, 127 Repulse Bay Road	High	Island South	3,008	168,000	55.85
	House 26, 61-63 Deep Water Bay	House	Island South	3,362	220,000	65.44
Mar-08	Flat B, 2/F, Falconridge	Low	The Peak	3,300	108,000	32.73
	House 8, Stanley Court	House	Island South	2,669	150,000	56.20
	Flat A, 23/F, Grand Garden	High	Island South	3,054	125,000	40.93
	House F, Mt. Austin Estate	House	The Peak	3,773	230,000	60.96

SELECTED SALES TRANSACTIONS IN 1Q 2008

Month	Property	Location	Size (sf)	Price (HK\$ Million)	Price (HK\$ psf)
Jan-08	House A1, Rosecliff	Island South	3,980	91.80	23,065
	Unit A, 37/F, Tower 1, Clovelly Court	Mid-Levels	2,809	70.00	24,920
	House 8, 8 Severn Road	The Peak	4,650	210.00	45,161
Feb-08	10/F, Grosvenor Place	Island South	2,809	68.00	24,208
	Unit D, 51/F, Tower 3, Tregunter	Mid-Levels	3,688	85.00	23,048
	House 41, Strawberry Hill	The Peak	3,200	106.30	33,219
Mar-08	House 19, Stella Maris	Island South	4,186	60.50	14,453
	Unit B, 42/F, Estoril Court	Mid-Levels	3,347	60.00	17,927
	House L15, La Hacienda	The Peak	3,200	98.00	30,625

SERVICED APARTMENTS

Serviced Apartment Rental Indices

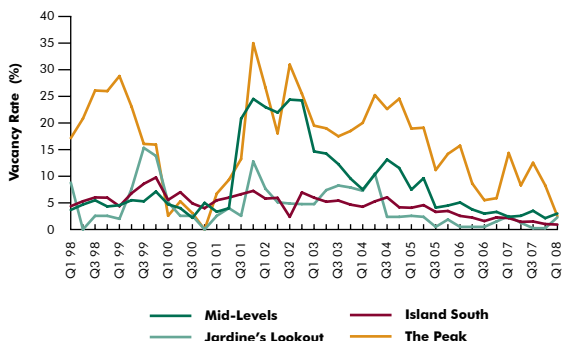


Serviced apartments are still in high demand as the widespread interest in quality serviced accommodations remains strong. The sustained shortage of supply and high rental values of luxury residential properties also give the market a forceful boost. In the first quarter of 2008, the occupancy rate of all four serviced apartment types ranged from 99.5% to 100%, with boutique serviced apartments remaining the most attractive type due to their trendy style and convenient locations. Although the rental values of boutique serviced apartments performed well, with 8.1% quarterly growth, standard serviced apartments put up the highest rental growth figure at 9.2% q-o-q. Premier and luxury serviced apartments soared 5.1% and 3.1% q-o-q in rents, respectively.

Serviced accommodations have become popular in the market. Developers continued to increase their investment on serviced apartments in hopes of achieving higher returns. One of the most aggressive serviced apartment players, VCC Land, actively acquired properties such as 25-27 Tung Lo Wan Road in Causeway Bay and 535 Canton Road near Kowloon Station in West Kowloon for business expansion. Along with Shama Tsim Sha Tsui (87 units) opened in January, The HarbourView Place (266 units) atop Kowloon Station is also ready for lease at over \$60 psf per month. In addition to these new serviced apartment projects, another 700 new units or so are expected to enter the market this year to meet the surging demand.

VACANCY

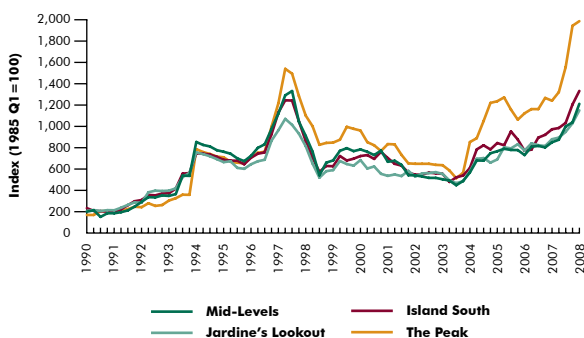
Luxury Residential Vacancy Rate



According to the Buildings Department, no properties obtained occupation permits on Hong Kong Island during the first two months of 2008. As a result, limited supply kept the overall vacancy rate very tight. Even in the face of an unclear economic situation, the overall luxury residential vacancy rate on Hong Kong Island remained very stable, edging upward less than 0.4 percentage points to 1.9% during the period under review. Amongst the four traditional luxury residential districts, The Peak registered the highest quarterly vacancy drop of 5.8 percentage points in the first quarter, highlighting strong demand. Jardine's Lookout, in contrast, registered a relatively high quarterly vacancy appreciation of about two percentage points, possibly suggesting landlords' firm stance on rentals in newer properties in the area, for example The Legend, that the market has been slow in absorbing. Other districts, meanwhile, registered relatively stable vacancy rates.

SALES MARKET

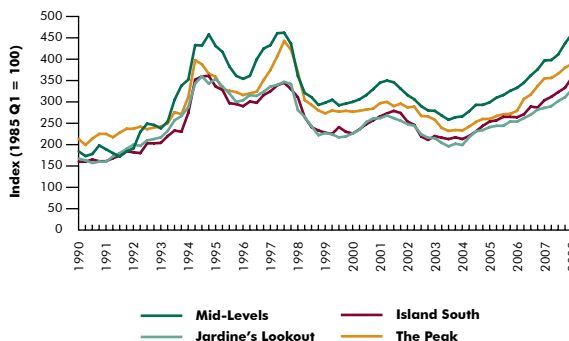
Luxury Residential Capital Value Indices



Both local players and foreign investors were obviously becoming more conservative in acquiring properties in the midst of the weakened stock market and international economic uncertainties. The extended holiday from Christmas through Lunar New Year in Hong Kong further contained market growth in the first quarter. The average capital value of luxury residential properties on Hong Kong Island reached \$15,888 psf, registering a moderate q-o-q growth of 8.5% in comparison to 15.5% q-o-q growth in the previous quarter. Mid-Levels became the market focus, registering a quarterly surge of 16.8% stimulated by the sale of The Royal Court, Tower 4 of Hillsborough Court by Sun Hung Kai Properties. The Peak registered a quarterly gain of 2.2%, ranking the lowest amongst the four traditional luxury residential districts due to a lack of transactions as landlords in the district preferred to hold on to their properties.

LEASING MARKET

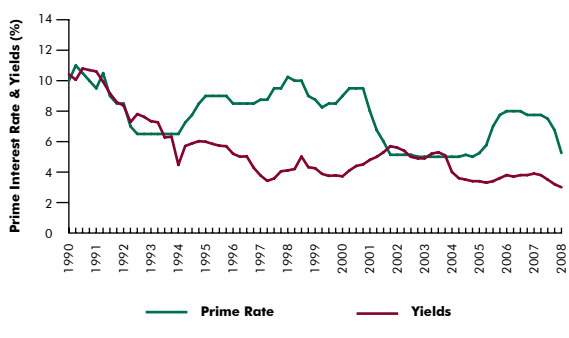
Luxury Residential Rental Indices



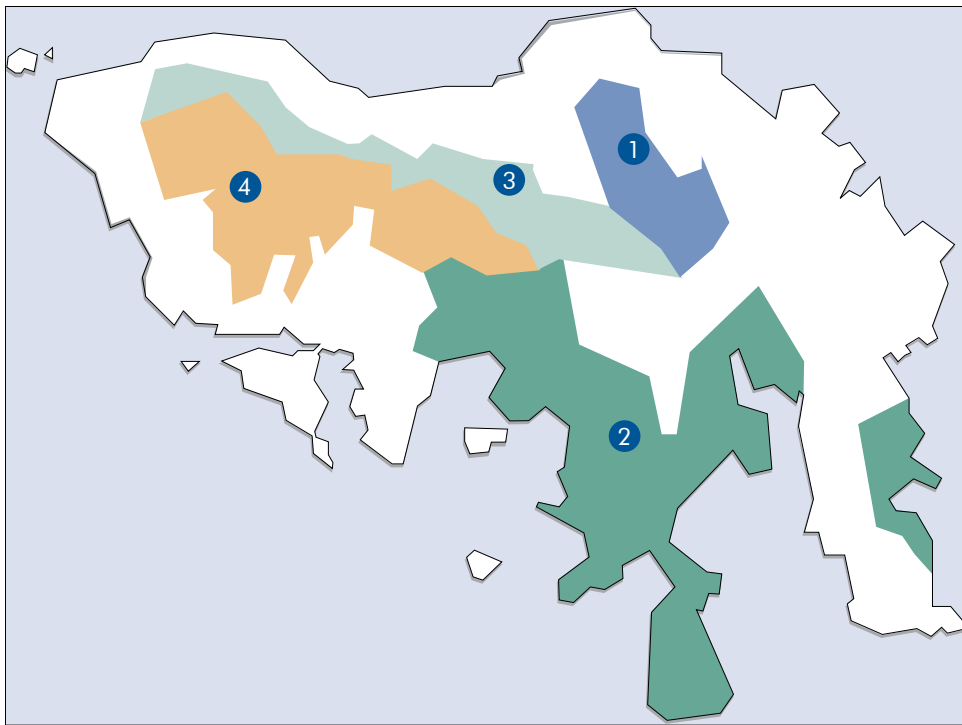
Landlords opted to sell rather than lease out their properties as market yields continuously compressed. Potential buyers adopted a cautious acquisition strategy for luxury residential properties to avoid high investment risk arising from the fluctuating global economic environment. As such, increasingly hesitant users prefer to take advantage of leasing periods to wait for a desirable buying moment to arrive. Thus, the luxury residential leasing market continued to sustain considerable demand and rental values remained strong, with 14% yearly growth in average against a backdrop of shrinking supply of leasing stock. The overall rents of luxury residential properties on Hong Kong Island registered quarterly growth of 4.8%. Island South surged 7% q-o-q, the strongest performance amongst the four districts, while Mid-Levels recorded the most moderate quarterly growth, with a 2.3% gain in the quarter.

YIELDS

Luxury Residential Yields



The overall yield of luxury residential premises on Hong Kong Island continued to fall, dropping another 0.2 percentage points to 3%, the lowest level in past two decades. Although the local prime lending and mortgage rates were further reduced to 5.25% and about 2.5% respectively, further reduction room is limited according to major local banks. The marginal spread between the yield and mortgage rate may dampen investment interest in luxury residential properties in the near-term. Yet, given that the cost of borrowing remains stable and rental gains are expected to outpace price appreciation in the longer-term, the spread should improve as 2008 progresses. With real mortgage rates lower than the prevailing inflation rate, Hong Kong has entered into a negative real interest rate environment and interest in acquiring luxury residential properties ought to recover quickly once market sentiment stabilises.



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.