

MarketView

Hong Kong Retail

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Third Quarter 2008

Quick Stats

		Y-o-Y change	Q-o-Q change
Inflation Rate	4.6% (Aug 08)	↑	↓
Unemployment Rate	3.2% (Jun-Aug 08)	↓	↓
Visitor Arrivals	19.6 million (Jan-Aug 08)	↑	N/A
Prime Retail Rental Value	HK\$426.55 psf	↑	↓

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

Hot Topics

- As the global financial turmoil threatens to bring layoffs to Hong Kong, consumers will cut their spending, dragging down economic growth over the near future.
- The perceived decline in consumer sentiment has not yet been fully reflected in retail sales growth in August, and should become more evident towards the end of the year.
- The gradual slowdown in local economy led to the first negative rental growth across-the-board in all the prime shopping districts under review since the SARS epidemic in 2003. However, the worst has yet to arrive in Hong Kong.
- Retail property market activity is expected to decline in the remaining months of 2008. The rental market could possibly find short-term support from local retailers instead of high-end international brands.

A perceptible decline in consumer sentiment began to surface in the third quarter, resulting from the global economic slowdown, the ongoing financial market turbulence and escalating fears of a local economic downturn. The Census and Statistics Department's latest release indicated that real GDP growth in the second quarter of 2008 was 4.2% higher than that of one year earlier, but significantly lower than the 7.3% growth in the first quarter. In particular, growth in private consumption declined to 3.1% from 7.9% over the same period, as the volatile stock market led to reduced consumer spending on financial services and rising inflation eroded purchasing power.

Retail sales growth remained firm in August with the total value up 10.4% on the same month last year to \$22.8 billion and volume up 3.9%. Despite the continued growth, both indicators generally experienced decelerating trends, probably influenced by the negative impact of both the local assets/stock market corrections and the fall-off in inbound tourism in August. It is likely that the perceived change in consumer sentiment has not yet been fully reflected in overall retail sales and should become more evident towards the end of the year.

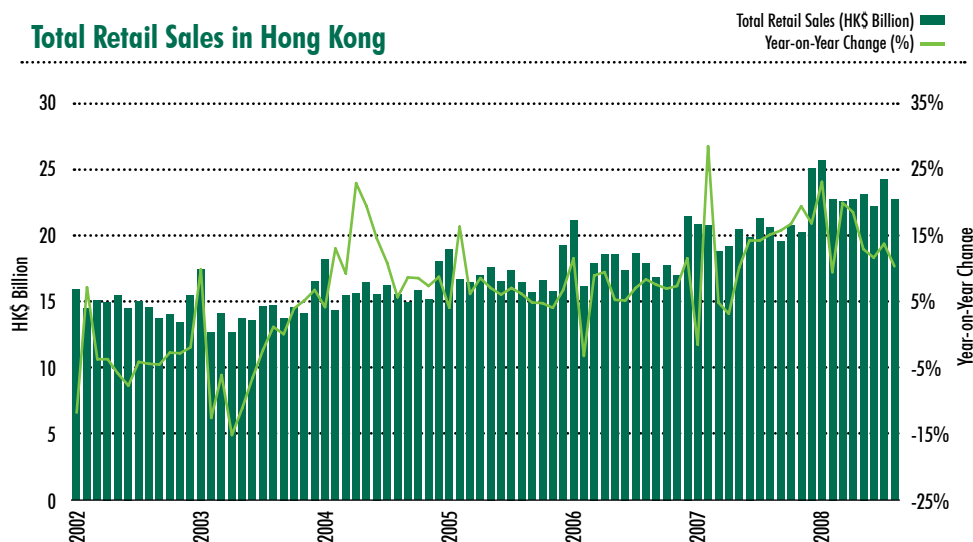
Although the labour market remained firm during the third quarter, overall market conditions took some unexpected turns as global financial woes heightened. Several recent occasions where the

services of provisional liquidators were required did not help shore up the already softened consumer mood. As the global financial turmoil threatens to bring layoffs to Hong Kong, consumers will cut their spending, dragging down economic growth over at least the next few quarters.

The retail property market appeared to show early signs of consolidation, in that the first negative rental growth across-the-board in all the prime shopping districts under review was registered since the SARS epidemic in 2003. Despite the weakened economy and dampened spending sentiment, the quarterly rental declines ranged only from 0.4% to 1.5% lower than the previous quarter. Indeed, the overall rental growth still captured a positive increase of 10% y-o-y, reflecting the resilience of the retail market amid the current financial downturn to date.

With the stock market still volatile and the credit crunch showing no sign of calming, consumers are expected to be more cautious in spending for the remainder of the year, and the local economy is likely to head for a gradual slowdown. Retail players will have to be prepared to overcome the tougher operational environment in Hong Kong. Retail property market activity is therefore expected to decline in the remaining months of 2008; the rental market could possibly find support from local retailers instead of high-end international brands in the near future.

Total Retail Sales in Hong Kong



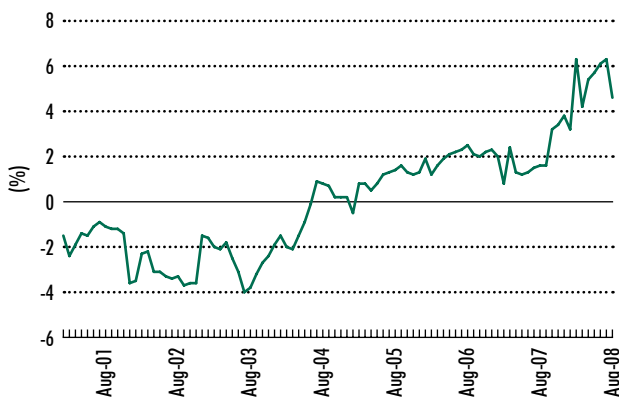
Source: Census & Statistics Department

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Selected Leasing Transactions in Q3 2008

District	Property	Size (sf)	Tenant
Central	Shop B, G/F, 50 Wellington Street	2,019 (lettable)	Feva Group
Central	B/M, G/F, M/F, 15C Wellington Street	2,400 (gross)	JDC Fashion
Central	G/F, C/L, 56-58 Wellington Street	2,000 (gross)	EQ:IQ
Central	Shop C, G/F, Entertainment Building, 30 Queen's Road Central	4,371 (lettable)	Club 21
Central	B/M, Manning House, 48-52 Queen's Road Central	7,429 (gross)	G2000
Central	Shops 1 & 2, G/F, 1/F, Nexus Building, 41 Connaught Road Central	7,467 (gross)	Halwinner
Tsim Sha Tsui	G/F-3/F, Yue Hwa International Building, 7 Ashley Road	26,816 (gross)	Esprit
Tsim Sha Tsui	Shop 8, G/F, Silvercord, 30 Canton Road	1,093 (gross)	Calvin Klein Underwear
Mong Kok	G/F, B/M, Hollywood Plaza, 610 Nathan Road	5,600 (gross)	Sephora
Mong Kok	Shop C, G/F, M/F, 617-619 Nathan Road	2,400 (gross)	Tung Hing Watch

Hong Kong Inflation Rate



Source: Census & Statistics Department

Hong Kong's headline inflation was 4.6% in August, down 1.7 percentage points from July. The reduction was mainly due to the implementation of two one-off measures by the government, including a three-month waiver of public housing rentals and a two-year suspension of the Employees Retraining Levy as from August 2008. Excluding these measures, the underlying inflation rate in August was level with that in July. However, inflation is likely to have peaked for the year, as the stabilisation of food prices on the Mainland is expected to alleviate the rise in prices of foodstuffs in Hong Kong, and energy prices should continue to decline for the remainder of 2008. The potential moderation in domestic demand and employment growth on the back of the prolonged global financial turbulence is increasingly likely to become factors containing Hong Kong's inflation.

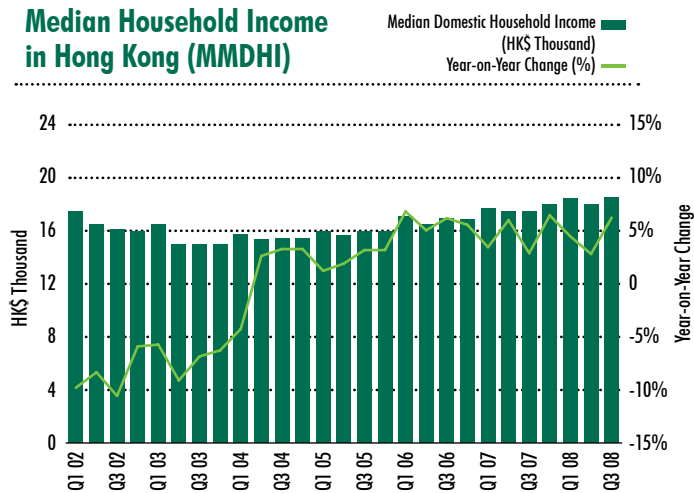
Hong Kong Unemployment Rate



Source: Census & Statistics Department

Labour market conditions remained firm during the third quarter. The total labour force continued to expand from June to August 2008, hitting a record high of 3.68 million according to government figures. The unemployment rate has remained stable at 3.2% during the period, notwithstanding the expansion in labour supply, being the lowest level since early 1998. Yet, there are no grounds for optimism in regard to the global financial turmoil. With further downside risks to the already challenging external environment, the uncertainties clouding Hong Kong's near-term economic outlook have increased, especially in light of the recent string of bankruptcies in Hong Kong from companies failing to manage their debt loads. The possible rise in unemployment may cause purchases to slump once the worsening market conditions eventually make their way to Hong Kong.

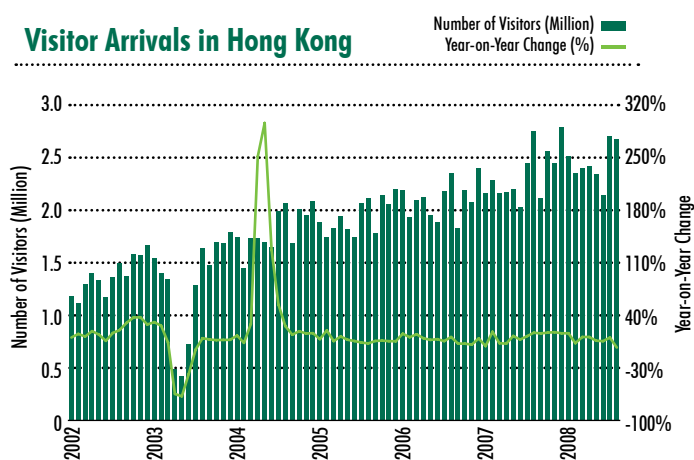
Median Household Income in Hong Kong (MMDHI)



Source: Census & Statistics Department

MMDHI was recorded at \$18,600 from May to July 2008, up slightly from the \$18,000 registered in the preceding period between March and May. This raise was mainly led by the high inflation rate captured in the first half of the year. However, the headline inflation rate in August still outpaced growth in the latest MMDHI figure by at least one percentage point. Market uncertainties from the current global economic chaos put pressure on any further growth in MMDHI. Together with the negative wealth effect caused by the stock market declines, the purchasing power of local residents could be decreased further and the will to spend diminished.

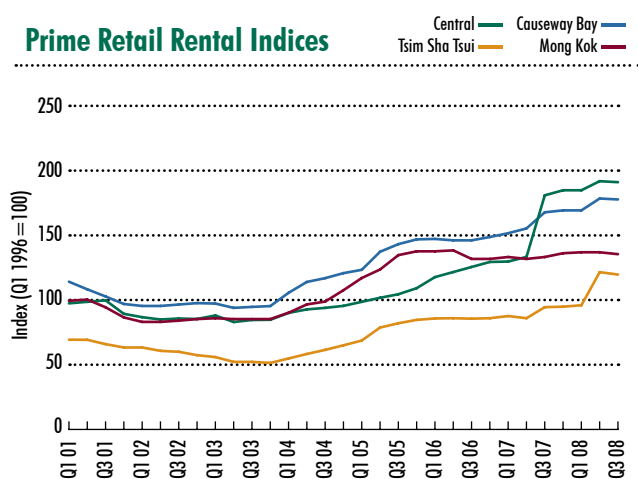
Visitor Arrivals in Hong Kong



Source: Hong Kong Tourism Board

In August, Hong Kong saw a 2.9% y-o-y drop in visitors to about 2.7 million, representing the first negative y-o-y growth in the last 19 months. This brought the cumulative arrivals for the year since January to almost 20 million — up 7.3% on the same period last year according to the Hong Kong Tourism Board. Although there was only a mild 0.8% y-o-y growth of Mainland arrivals to 1.7 million in August, probably attributed to China’s adjustment in visa policy, the Mainland market had already outperformed all other long- and short-haul market regions. Continually affected by a combination of factors in the macro environment triggered by the widespread economic downturn, these markets recorded drops of various degrees in arrivals in August.

Prime Retail Rental Indices



Source: Census & Statistics Department

The weakened economy and market turbulence triggered by the global financial tsunami will inevitably force consumers to hold off on spending, and retailers know it. The risk-averse approach from the formerly aggressive retailers has somewhat calmed the growth momentum in the retail property market during the quarter. The overall rents in prime shopping districts dropped a mild 0.8% q-o-q in the review period, with Tsim Sha Tsui registering the deepest quarterly rental drop of merely 1.5% after a substantial surge in the last quarter. While the re-emergence of the broad-based contraction in rental growth — the first since the second quarter of 2003 — seems to suggest that a long-awaited retail market consolidation may finally be in sight, it is noteworthy that the overall rents in prime shopping districts still captured some 10% y-o-y growth in the third quarter, thus the worst moment may be yet to arrive in Hong Kong.

Prime Shopping Districts in Hong Kong



- Kwun Tong Line
- Tsuen Wan Line
- Island Line
- Airport Express
- Tseung Kwan O Line

Prime Shopping Districts in Hong Kong

Central

This traditional banking and financial centre of Hong Kong is also a popular shopping hub for middle to upper class shoppers. Strategically linked with the Airport Railway and MTR, and supported by a number of Grade A office buildings, 5-star hotels and prestigious shopping centres in the area, Central has a large catchment area and attracts a broad spectrum of shoppers including tourists, expatriates, office workers, singles and families.

Causeway Bay

This area attracts a broad mix of international tourists, local shoppers, including office workers from commercial buildings within the area, young shoppers and family shoppers. The area has a comprehensive mix of retailers and restaurateurs catering to young, rich, budget minded and family clientele.

Tsim Sha Tsui

This area has the largest concentration of hotels and attracts tourists, affluent young shoppers predominantly from Kowloon, and office workers from commercial buildings within the area. There is a wide array of retailers ranging from necessity to luxury goods, restaurants, tailors and entertainment venues such as discos and karaoke bars.

Mong Kok

Strategically located along both MTR and KCR lines, Mong Kok also attracts a wide spectrum of shoppers, mainly local residents and Chinese tourists. The area consists of a number of modern fashion and accessories boutique stores catering to the young and hip crowd.

TERMINOLOGY

Inflation Rate:

This refers to the Composite Consumer Price Index (CPI) compiled by the Census and Statistics Department to provide an indicator of overall price movements affecting households. A weighting system is used to represent the relative importance, in terms of expenditure, of individual items in the basket of goods and services consumed by households. The weight of each item represents the importance of the item in the total expenditure of households.

Saleable Area:

The saleable area of a shop unit is measured up to the centre line of the wall separating adjoining units. The full thickness of the external walls and walls separating the units from the common areas, staircases, etc. are included.

Gross Floor Area:

The gross floor area of a shop unit is measured by adding the proportionate share of the common area to the saleable area of the unit.

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