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# Leasing

## Market overview

The Grade A office market has been active in Q2 2008, thanks to a positive sentiment and a solid demand for office space. In particular, the average monthly effective rents in Central, the prestigious CBD area, rose to an all-time high of HK\$122 per sq ft. In the meantime, the vacancy rate also dropped to a record low of 1.1%. Consequently the adjacent Wanchai/Causeway Bay area, benefiting most from the decentralisation from Central, recorded a quarterly rise of 55.1% in office take-up and 12.5% rise in average effective rents.

High rent will definitely affect firms' relocation and expansion plans. Investors also became more cautious about making investment decisions due to the prolonged sub-prime crisis, oil price hike and tighter lending by local and foreign banks. It is anticipated that the office sector will undergo a consolidation period in the second half of 2008.

## Grade A office take-up, GFA (sq ft)

| District                | Q2 2007        | Q3 2007       | Q4 2007        | Q1 2008                | Q2 2008                      | Q2 2008<br>Vs Q1 2008 | Q2 2008<br>Vs Q2 2007 |
|-------------------------|----------------|---------------|----------------|------------------------|------------------------------|-----------------------|-----------------------|
| Sheung Wan              | 15,141         | 7,149         | 17,360         | 15,094                 | 8,914                        | -40.9%                | -41.1%                |
| Central                 | 184,131        | 22,244        | 257,931        | 166,860                | 13,851                       | -91.7%                | -92.5%                |
| Wanchai/CWB             | 26,421         | 12,042        | 20,580         | 107,447                | 166,647                      | +55.1%                | +530.7%               |
| Island East             | 28,369         | 1,735         | 76,198         | 88,468                 | 61,669 <sup>(1)</sup>        | -30.3%                | +117.4%               |
| <b>Hong Kong Island</b> | <b>254,062</b> | <b>43,170</b> | <b>372,069</b> | <b>337,869</b>         | <b>251,081<sup>(2)</sup></b> | <b>-33.6%</b>         | <b>-1.2%</b>          |
| Tsimshatsui             | 22,307         | -52,460       | 72,335         | 1,651                  | 7,930                        | +380.3%               | -64.5%                |
| Kowloon Station         |                |               |                | 910,000                |                              |                       |                       |
| Kowloon East            |                |               |                | 182,416 <sup>(3)</sup> | 141,186 <sup>(4)</sup>       | -22.6%                |                       |

(1) If One Island East is taken into account, the figure will be 1,391,479 sq ft (GFA)  
 (2) If One Island East is included, it will be 1,580,890 sq ft (GFA)  
 (3) If Kwun Tong 223 is added, it will become 282,416 sq ft (GFA)  
 (4) The figure will remain unchanged if Kwun Tong 223 has been taken into account.

## Major leasing transactions in Q2 2008

| District            | Property              | Area (sq ft) | Tenant                                 |
|---------------------|-----------------------|--------------|--|
| Sheung Wan          | Vicwood Plaza         | 11,000 (G)   | Hong Kong Securities Clearing Co. Ltd. |
| Central & Admiralty | Alexandra House       | 10,000 (L)   | Walkers (Asia) A Partnership           |
| Island East         | Cityplaza Four        | 16,000 (L)   | HSBC                                   |
|                     | Devon House           | 27,000 (L)   | HSBC                                   |
| Kowloon Station     | ICC                   | 350,000 (G)  | Deutsche Bank                          |
| Kowloon East        | Enterprise Square One | 28,100 (G)   | Baltrans Logistic                      |
|                     | Skyline Tower         | 26,000 (G)   | Schenker International (HK) Limited    |
|                     | Millennium City 6     | 17,000 (G)   | Longrow Shipping Ltd                   |

Notes:  
 G Gross (generally including all common areas plus lift shafts, mechanical rooms and staircases, etc.)  
 N Net (excluding all common areas)  
 L Lettable (generally including passenger lift lobby, corridors and lavatories, etc.)

### Demand

The FIRE (finance, insurance, real estate and business services) sector remained the major player in the office market in Hong Kong although their activities were slower compared with last quarter. As Central is approaching its highest capacity, tenants are searching for alternatives in the non-core areas of Hong Kong Island such as Wanchai/Causeway Bay and Island East with lower rents. Those areas adjacent to the CBD, like Wanchai/Causeway Bay, have become the market focus and attracted a large part of the spillover demand from Central since the beginning of the year. Likewise, Island East was considered another hotspot thanks to its modern office premises and comprehensive supporting facilities.

### Take-up

In Q2 2008, the overall office take-up of Hong Kong Island amounted to 25,081 sq ft, down 33.6% quarter-on-quarter (QoQ) and 1.2% year-on-year (YoY). However, if including the 1,329,810 sq ft from One Island East, the overall take-up of Hong Kong Island will surge to 1,580,890 sq ft. Nevertheless, many of the floor plates in One Island East were pre-committed last year, therefore it should not be taken as a Q2 increase. In fact, the take-up in Island East (excluding One Island East) saw a quarterly plunge of 30.3% to 61,669 sq ft in Q2.

The high rental and tight availability of office space in Central/Admiralty are forcing more companies to relocate their workforce to nearby districts such as Wanchai/Causeway Bay. Wanchai/Causeway Bay's take-up of 166,647 sq ft in Q2 represents an increase of 55.1% QoQ and a five-fold jump YoY. Across the harbour, Tsimshatsui's office take-up rose to 7,930 sq ft or up 380.3% QoQ although there is still a drop of 64.5% YoY. The office

This decentralisation trend is also prompting companies to move across the harbour. Kowloon Station is becoming a favourable location for the FIRE sector to house their expanding workforce. After signing a 12-floor tenancy agreement, Deutsche Bank became the third global investment bank moving into the International Commerce Centre (ICC), following Morgan Stanley and Credit Suisse. It has pre-committed 420,000 sq ft of floor space and the right to lease up to 630,000 sq ft of area.

market in Tsimshatsui was bolstered by a stable local demand and its role as one of the main alternatives to companies in Central. On the other hand, Kowloon East's take-up dropped 22.6% quarterly to 141,186 sq ft due to the massive new supply in Q1 that was not being fully absorbed. Nevertheless, the market is expected to be stable in Kowloon East especially among existing buildings with additional tenants moving in from other districts.

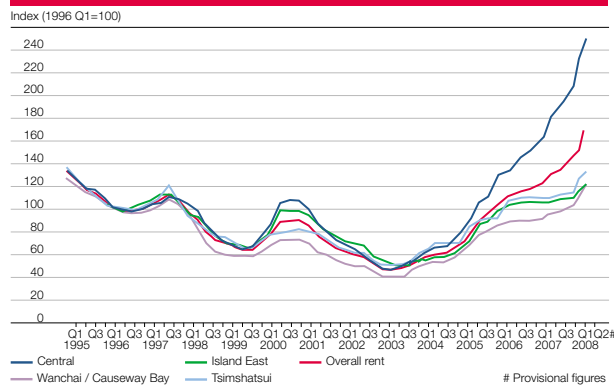
As a result of low availability of office spaces, Central's take-up showed a significant plunge of 91.7% QoQ from 166,860 sq ft to 13,851 sq ft in Q2. Similarly, the take-up in Sheung Wan decreased quarterly by 40.9%. In general, except for Wanchai/Causeway Bay and Tsimshatsui, all districts in Hong Kong saw lower take-ups in Q2.

## Rents

Rental of all districts continued an upward movement in Q2 2008 with Central's effective rent rising 5.2% QoQ to HK\$122 per sq ft per month. In the first 6 months of 2008 the average rental in the CBD soared by more than 15%, in line with our forecast at the beginning of the year. Benefited from the speeding up of the decentralisation process, rentals in non-core areas increased at a faster pace. The average rental in Wanchai/Causeway Bay witnessed the largest quarterly growth of 12.5%, reaching HK\$45 per sq ft per month. Rental in Island East (excluding One Island East) rose 7.1% QoQ to HK\$30 per sq ft per month.

On account of an increased take-up and a stable demand, office rental in Tsimshatsui increased by 6.7% QoQ to HK\$32 per sq ft. Similarly, office rents in Sheung Wan and Kowloon East rose 2% and 4% to HK\$52 per sq ft and HK\$26 per sq ft respectively compared with the previous quarter.

## DTZ index - office rent, Hong Kong



## Grade A office quarterly average effective rents (HK\$ per sq ft per month net)

| District             | Q1 2007 | Q2 2007 | Q3 2007 | Q4 2007 | Q1 2008 | Q2 2008 | Q2 2008    |            |
|----------------------|---------|---------|---------|---------|---------|---------|------------|------------|
|                      |         |         |         |         |         |         | Vs Q1 2008 | Vs Q2 2007 |
| Sheung Wan           | 43      | 43      | 44      | 45      | 51      | 52      | 2.0%       | 20.9%      |
| Central/Admiralty    | 83      | 89      | 97      | 106     | 116     | 122     | 5.2%       | 37.1%      |
| Wanchai/Causeway Bay | 34      | 34      | 36      | 38      | 40      | 45      | 12.5%      | 32.4%      |
| Island East          | 26      | 26      | 26      | 27      | 28      | 30*     | 7.1%       | 15.4%      |
| Tsimshatsui          | 27      | 27      | 27      | 28      | 30      | 32      | 6.7%       | 18.5%      |
| Kowloon East         | -       | -       | -       | 23      | 25      | 26      | 4.0%       |            |

\* If One Island East has been taken into account, the average net effective rent is HK\$31 per sq ft per month

# Sales and investment

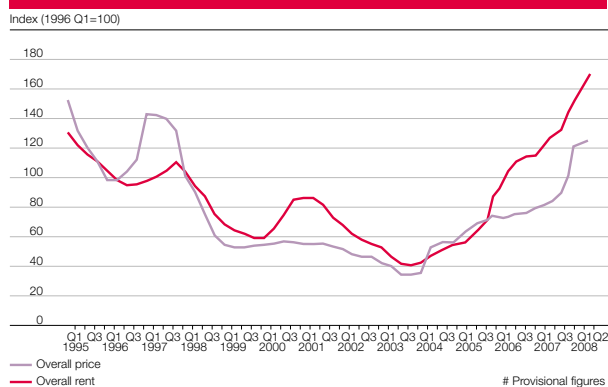
In Q2 2008, only 12 strata-title grade A and en-bloc grade B office sale transactions (over HK\$100 million) were registered, down 52% compared with last quarter. Likewise, the average prices of grade A office properties also recorded a quarterly drop of 27.1% in Q2. Although there was no great change in average price of our benchmark property, 9 Queen's Road Central in Q2, the properties in the surrounding non-core areas such as Cosco Tower in Sheung Wan witnessed a fall in average price from HK\$13,093 per sq ft in Q1 to HK\$10,622 in Q2, representing a dip of 18.9% QoQ.

In general, the investment demand for office premises remained strong thanks to a continuous rise in rental, but the tightened credit condition has forced many investors to postpone their investment decisions on account of a high borrowing cost. It is expected that the office investment market sentiment will remain cautious in the short term.

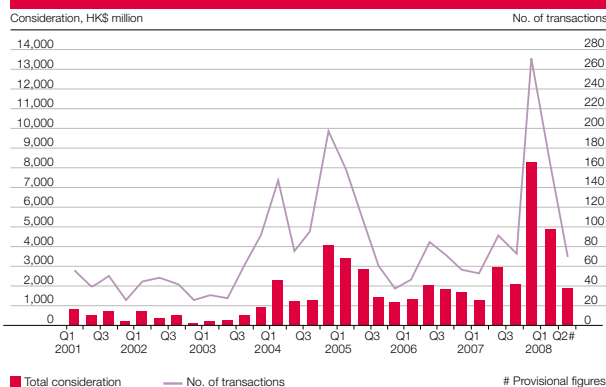
## Major sales and investment transactions in Q2 2008

| District            | Property  | Gross floor area (sq ft) | Total consideration (HK\$m) | Unit rate (HK\$ per sq ft) |
|---------------------|---|--------------------------|-----------------------------|----------------------------|
| Sheung Wan          | 22/F & 23/F, Cosco Tower, 183 Queen's Road Central      | 39,492                   | 446.26                      | 11,300                     |
| Central & Admiralty | BOCG Insurance building, 134-136 Des Voeux Road Central | 75,149                   | 800                         | 10,646                     |
|                     | 23/F, Tower 1, Lippo Centre, 89 Queensway               | 157,00                   | 250                         | 15,924                     |
|                     | 41/F, Tower 1, Lippo Centre, 89 Queensway               | 12,108                   | 228                         | 18,831                     |
| Tsimshatsui         | Isa Tower, 5 Minden Avenue                              | 13,355                   | 132.8                       | 9,944                      |

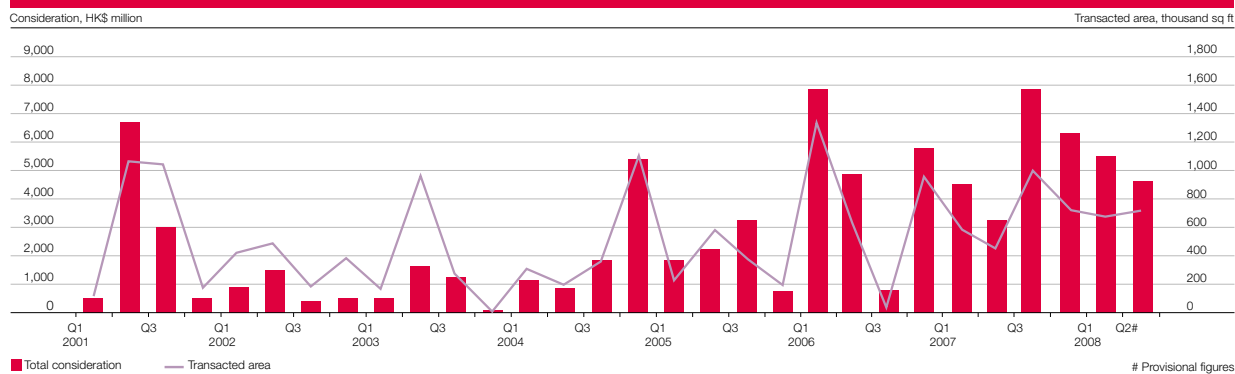
## DTZ index - office rent & price, Hong Kong



## Strata-title grade A office transactions



## Major en-bloc and strata-title transactions (grade A & B, over 10,000 sq ft gross)



# Vacancy

Despite a volatile stock market and the economic slowdown in the US, the stable business outlook of Hong Kong helped reduce the vacancy in Q2. The overall vacancy rate in Hong Kong Island (excluding One Island East) decreased from 2.1% to 1.7% this quarter, representing a drop of 1.9 percentage points from the previous year.

Central continued to be the business area in the city with the tightest supply. Its vacancy rate dropped from 1.2% to 1.1% in Q2, leading to a low take-up during the quarter. Not surprisingly, Wanchai/Causeway Bay recorded the biggest fall in vacancy in

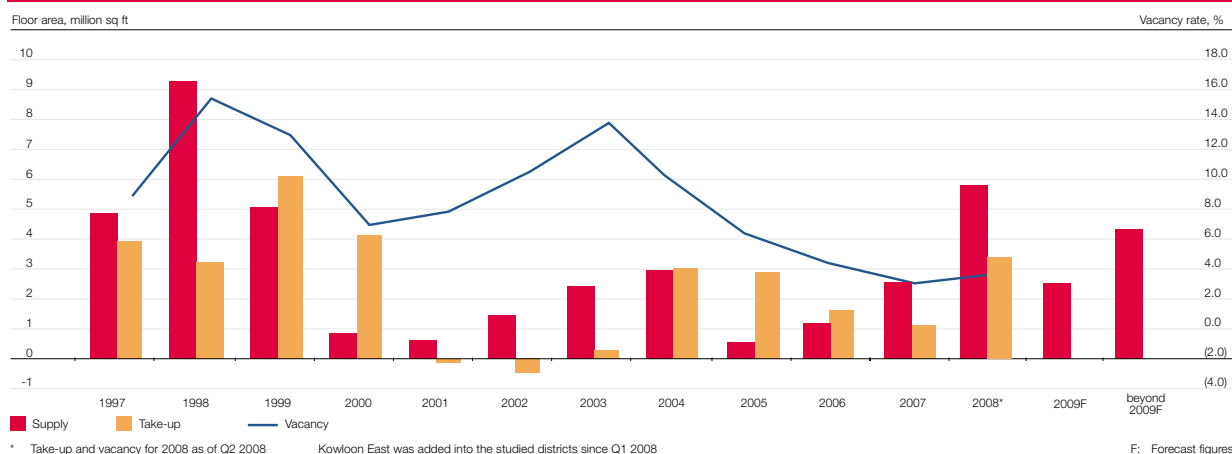
Q2, down 1 percentage point to 2.3% as the spillover demand from Central took up office spaces there. With its modern office premises and comprehensive supporting facilities, vacancy rate in Island East dipped to 1.3%, if One Island East was excluded.

On the Kowloon side, the vacancy rate in Tsimshatsui dropped slightly from 3.5% to 3.4% in Q2. In Kowloon East, the market was active with a low vacancy rate of 3.7%. However, a huge supply coming on stream by the end of 2008 (including Kwun Tong 223, a major new completion in 1H 08) is set to increase the vacancy.

## Grade A office vacancy

| District                                    | Q1 2007 | Q2 2007 | Q3 2007 | Q4 2007 | Q1 2008         | Q2 2008         |
|---|---------|---------|---------|---------|-----------------|-----------------|
| Central/Admiralty                           | 3.7%    | 3.0%    | 2.9%    | 1.9%    | 1.2%            | 1.1%            |
| Sheung Wan                                  | 5.5%    | 5.1%    | 4.8%    | 4.3%    | 3.8%            | 3.6%            |
| Wanchai/Causeway Bay                        | 4.2%    | 4.0%    | 3.9%    | 3.9%    | 3.3%            | 2.3%            |
| Island East<br>(incl. One Island East)      | 4.2%    | 3.9%    | 3.8%    | 3.0%    | 2.0%<br>(3.7%)  | 1.3<br>(2.8%)   |
| Hong Kong Island<br>(incl. One Island East) | 4.1%    | 3.6%    | 3.5%    | 2.8%    | 2.1%<br>(2.5%)  | 1.7%<br>(1.9%)  |
| Tsimshatsui                                 | 3.4%    | 3.2%    | 3.8%    | 3.5%    | 3.5%            | 3.4%            |
| Kowloon Station                             |         |         |         |         | 0%              | 0.0%            |
| Kowloon East<br>(incl. Kwun Kong 223)       |         |         |         | 10.7%   | 5.6%<br>(16.4%) | 3.7%<br>(14.8%) |

## Supply, take-up and vacancy (1997 – 2008 & beyond)



# Supply

As the majority of new office supply between 2007 and 2009 lies in Kowloon East (over 6.2 million sq ft in Kwun Tong and Kowloon Bay), the district presents ample expansion options to FIRE sector companies seeking to relocate their back office operation to a relatively lower rental district (approximately 1/5 of Central's rents). With abundant supply and improving infrastructure in Kowloon East, it is expected that landlords of prime buildings can keep rents competitive and offer more incentives to tenants.

Throughout 2008, the new office supply in Kowloon East is expected to be around 3.6 million sq ft of office area. In light of the total supply in Hong Kong, the overall completion of office space will be up to 5.86 million sq ft for the whole year.

## Major new office supply

| District           | Development  | Total GFA (sq ft) | Developer(s)            |
|--------------------|--|-------------------|-------------------------|
| <b>2007</b>        |  |                   |                         |
| North Point        | 633 King's Road                                      | 300,000           | Shun Ho                 |
| Kowloon Bay        | Enterprise Square 5 (office portion)                 | 500,000           | Kerry                   |
| Kwun Tong          | Millennium City 6                                    | 400,000           | Sun Hung Kai            |
| Kowloon Station    | International Commerce Centre (Phase 1)              | 910,000           | Sun Hung Kai            |
| Kwun Tong          | 83 Hung To Road                                      | 240,000           | Billion Development     |
| Cheung Sha Wan     | 909 Cheung Sha Wan Road                              | 200,000           | Sun Hung Kai            |
|                    | Sub-total  | 2,550,000         |                         |
| <b>2008</b>        |  |                   |                         |
| Central            | Nexus Building                                       | 260,000           | Morgan Stanley          |
| Quarry Bay         | One Island East                                      | 1,500,000         | Swire                   |
| Kwun Tong          | Landmark East  | 1,100,000         | Windsor Properties      |
| Kwun Tong          | Kwun Tong 223  | 1,100,000         | Henderson               |
| Kowloon Bay        | Exchange Tower                                       | 700,000           | Sino                    |
| Kowloon Bay        | Manhattan Place                                      | 700,000           | Manhattan Realty        |
| Kwai Chung         | KCTL215 (Phase 1)                                    | 500,000           | Sun Hung Kai            |
|                    | Sub-total  | 5,860,000         |                         |
| <b>2009</b>        |  |                   |                         |
| Kwai Chung         | KCTL215 (Phase 2)                                    | 502,000           | Sun Hung Kai            |
| Kowloon Station    | International Commerce Centre (Phase 2)              | 560,000           | Sun Hung Kai            |
| Kowloon Bay        | Po Hing Building Redevelopment                       | 400,000           | Sino                    |
| Kowloon Bay        | Sing Tao Building Redevelopment                      | 520,000           | Billion Development     |
| Kwun Tong          | Crocodile Centre                                     | 250,000           | Crocodile               |
| Kwun Tong          | 120 Hoi Bun Road/ 114 Wai Yip Street                 | 312,000           | Sun Hung Kai            |
|                    | Sub-total  | 2,544,000         |                         |
| <b>Beyond 2009</b> |  |                   |                         |
| Causeway Bay       | Hennessy Centre Redevelopment                        | 700,000           | Hysan                   |
| Quarry Bay         | HK Tobacco Redevelopment                             | 510,000           | Kerry                   |
| Kowloon Station    | International Commerce Centre (Phase 3)              | 800,000           | Sun Hung Kai            |
| Kwun Tong          | 181 Hoi Bun Road                                     | 240,000           | Sun Hung Kai            |
| Central            | Crocodile House 1 & 2 and Ananda Tower Redevelopment | 180,000           | Citigroup               |
| Kwun Tong          | Kwun Tong Town Centre Redevelopment                  | 2,300,000         | Urban Renewal Authority |
|                    | Sub-total  | 4,730,000         |                         |

# Market outlook

Hong Kong's office market is so far less affected by the global economic downturn. International firms with sufficient liquidity and who were not seriously affected by the credit crunch will continue to create a strong demand for Hong Kong offices.

Looking ahead, investors are increasingly concerned about the oil price hike and tightening credit control, which will add to inflation pressure and occupiers' operating cost as well. However, the outlook of the office market remains optimistic in the short term and the rental in the CBD should remain stable in the second half of the year.



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