

CHAPTER 3 : DEVELOPMENTS IN SELECTED SECTORS

Summary

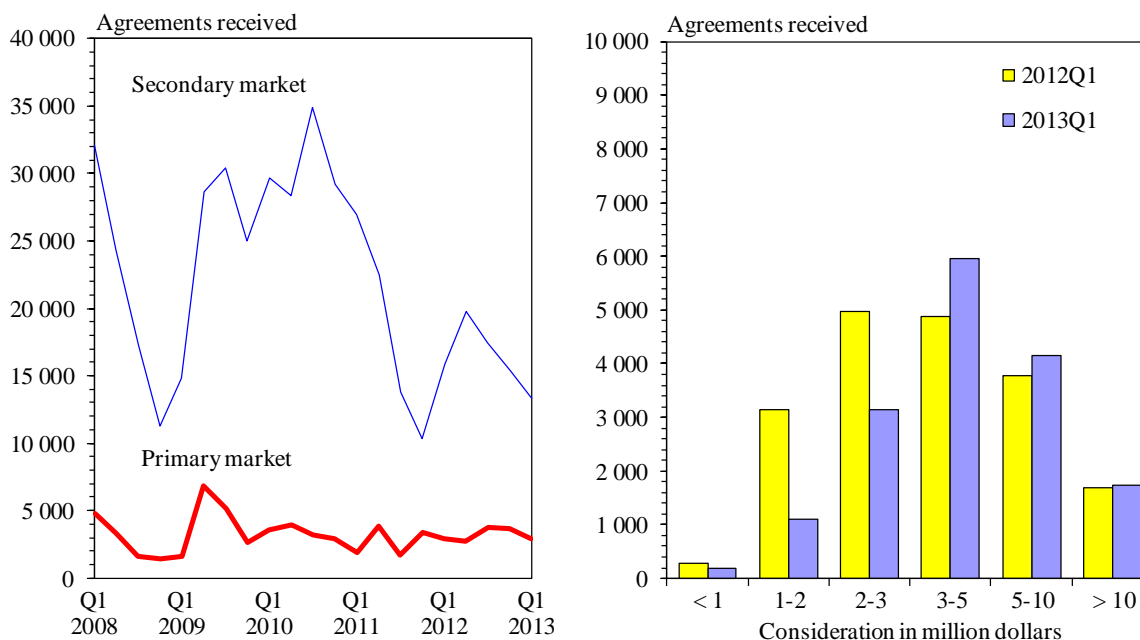
- *Amid the low interest rate environment and a tight demand-supply balance of flats, the residential property market re-gained momentum in the first two months of 2013. Yet the market softened after the announcement of the latest round of demand management measures by the Government in late February and the interest rate hike for new mortgages by the major local banks in mid-March. Overall flat prices rose by 5% between December 2012 and March 2013, but this was entirely due to the surge in the first two months. Trading activities slowed down markedly during the quarter.*
- *Raising flat supply through increasing land supply remains the Government's top policy priority in ensuring a healthy and stable property market. Reflecting the Government's sustained efforts, total flat supply in the coming few years increased to 67 000 units, the highest level since September 2007.*
- *The commercial and industrial property markets remained generally buoyant in the first two months of 2013, but cooled off in March under the effect of the new demand management measures.*
- *Inbound tourism maintained solid growth, with the Mainland market remaining the growth engine. Total visitor arrivals leapt by 13.5% over a year earlier to 12.7 million.*
- *As the external trade environment turned less steady, the logistics sector was subdued in the first quarter. Air freight throughput only recorded marginal expansion while container throughput fell further. The labour dispute at the Kwai Chung Container Terminals starting in late March could put a further drag on container throughput in the second quarter.*

Property

3.1 Amid the low interest rate environment and a tight demand-supply balance of flats, the *residential property market* re-gained momentum in the first two months of 2013. Yet market sentiment took an obvious turn following the announcement of the latest round of demand management measures by the Government in late February, and softened further after the major local banks raised the interest rates for new mortgages in mid-March.

3.2 Trading activities showed some pick-up in January and February, but then plunged to a very low level in March. Taking the first quarter as a whole, the total number of sale and purchase agreements for residential property received by the Land Registry fell to 16 271, 15% lower than the preceding quarter and 13% lower than a year earlier. Within the total, primary and secondary market transactions fell by 20% and 13% respectively from the preceding quarter. In parallel, total consideration shrank by 17% to \$94.3 billion.

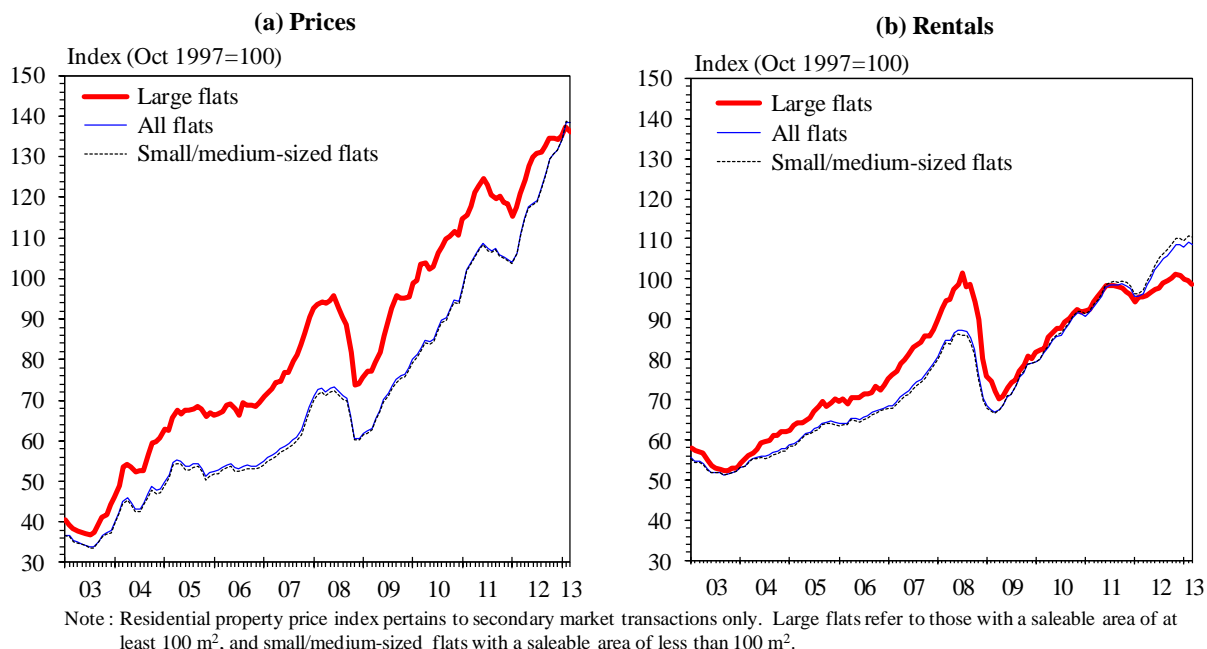
Diagram 3.1 : After some pick-up in January and February, trading activities plunged to a very low level in March



3.3 Overall flat prices rallied by 5% between December 2012 and March 2013. Yet this was entirely due to the surge in the first two months, and flat prices in fact reverted to a mild decline in March in tandem with the shift in market expectation. Prices of small/medium-sized flats soared by 5% while prices of large flats edged up by 1% during the first quarter. Following the general uptrend since 2009, overall flat prices have surpassed the 1997 peak by a rampant 38%.

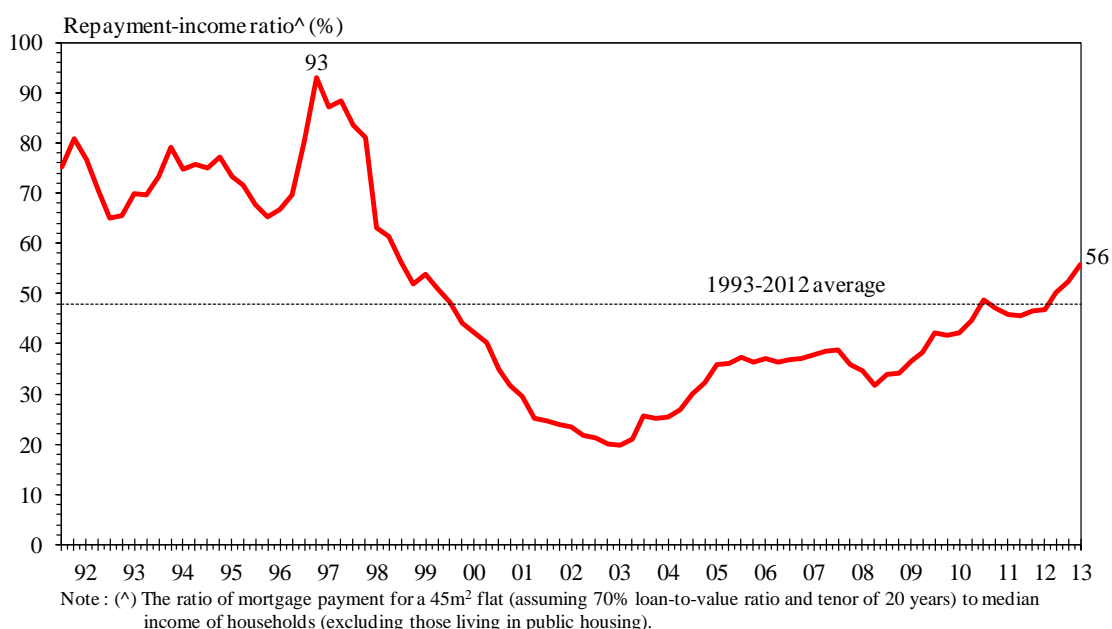
3.4 Meanwhile, the leasing market has shown signs of softening since late 2012. Between December 2012 and March 2013, overall flat rentals showed little change. Analysed by class, rentals of small/medium-sized flats edged up by 0.5% while those of large flats declined by 2%. The average rental yield for residential property edged down further from 3.0% in December 2012 to 2.9% in March 2013.

Diagram 3.2 : Flat prices reverted to a mild decline in March, while rental increase has slowed down since late 2012



3.5 As the increase in flat prices outpaced the growth in income, the home purchase affordability (i.e. the ratio of mortgage payment for a 45-square metre flat to median income of households, excluding those living in public housing) surged from 52% in the preceding quarter to 56% in the first quarter of 2013, far exceeding the long-term average of 47.9% over 1993-2012. The risks of a housing market bubble thus have risen further, especially so in face of the ongoing accommodative monetary measures of the major central banks and the resulting low interest rate environment.

Diagram 3.3 : The mortgage payment to income ratio worsened further



3.6 Raising flat supply through increasing land supply is the Government's top policy priority in ensuring a healthy and stable development of the property market. The Government has effectively resumed the lead in supplying government land since resuming the Government-initiated Sale Mechanism while retaining the Application Mechanism in 2010. However, in order to address lingering concerns in the community over government land supply should developers choose not to trigger sites for sale under the Application Mechanism, the Government has decided to abolish the Application Mechanism from 2013-14 onwards. Taking together the 2013-14 Land Sale Programme, railway property development projects, projects of Urban Renewal Authority, projects subject to lease modification/land exchange and private redevelopment projects not subject to lease modification/land exchange, the total housing land supply in 2013-14 is estimated to have the capacity to produce about 28 700 flats. As a result of the Government's sustained efforts, the *total supply of flats* in the coming few years (comprising unsold completed flats, flats already under construction but not yet sold and flats on disposed sites where construction has yet to commence) increased from 64 000 units as estimated at end-March 2012 to 67 000 units as estimated at end-March 2013, the highest since September 2007. In addition, another 9 000 units could be added to the supply through conversion of a number of residential sites into "disposed sites" and the completions of auction/tendering of some sites in the months ahead.

3.7 As it will take time to increase flat supply, the Government has also put in significant efforts to manage demand and reduce the possible risks to financial stability arising from an exuberant property market⁽¹⁾. In February the Government doubled the rates of existing ad valorem stamp duty (AVD) for transactions of all types of properties and advanced the charging of AVD on non-residential property transactions. The Hong Kong Monetary Authority (HKMA) also required banks to assume a higher mortgage rate increase for stress-testing in mortgage loan application for all types of properties, and further tightened the maximum loan-to-value ratios of mortgage loans for non-residential properties (**Box 3.1**). The Residential Properties (First-hand Sales) Ordinance, which aims at enhancing the transparency and fairness of the sales arrangements of first-hand residential properties, took effect in April 2013.

Box 3.1

Latest Government measures on the property market (February 2013)

In view of the renewed exuberance in the property market on entering 2013, the Government introduced another round of demand management measures for both residential and non-residential properties in late February. The Hong Kong Monetary Authority (HKMA) also launched a new round of macro-prudential measures, the sixth since October 2009, to strengthen the risk management of the banking sector's mortgage lending business. These measures are summarised below.

(1) Increase the ad valorem stamp duty (AVD) rates for residential and non-residential property transactions

To increase the cost of transactions, the AVD rates applicable to both residential and non-residential property transactions were doubled. For transactions valued at \$2 million or below, the AVD was raised from \$100 to 1.5% of the consideration or value of the property (whichever is higher). The new AVD rates do not apply to Hong Kong Permanent Resident buyers acting on their own behalf and who are not beneficial owners of any other residential property in Hong Kong at the time of acquisition of a residential property.

(2) Advance the charging of AVD on non-residential property transactions

To increase the transaction costs for the non-residential market and forestall any possible shift in exuberance from the residential market to the non-residential market, the AVD will be charged on an agreement for sale and purchase of a non-residential property, instead of when a conveyance on sale of non-residential property is executed. This standardised the stamp duty regime for both residential and non-residential property transactions.

(3) Tighten the terms of mortgage lending

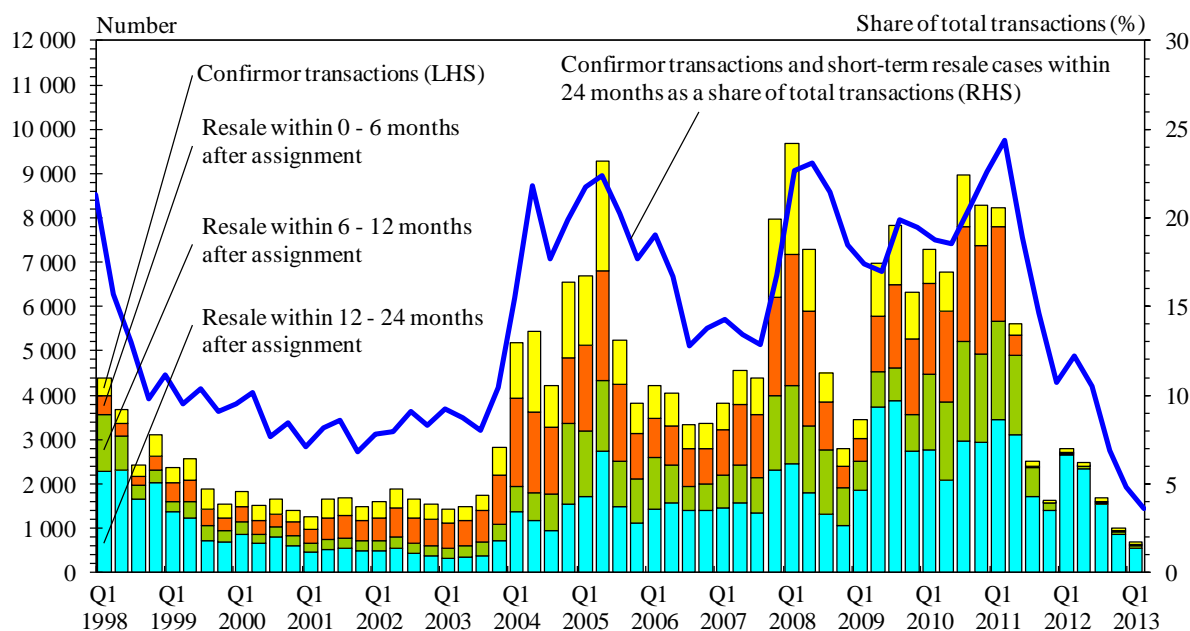
The HKMA's new round of measures is as follows:

- Require banks to assume a mortgage rate increase of 300 basis points, instead of the existing 200 basis points, in stress-testing the repayment ability of mortgage loan applicants for both residential and non-residential properties.
- Lower the maximum loan-to-value (LTV) ratios of mortgage loans for all non-residential properties, whether or not for self-use, from the existing applicable levels by 10 percentage points.
- Set the maximum LTV ratio of mortgage loans for standalone car park spaces at 40% and the maximum loan tenor at 15 years. Other requirements on maximum LTV ratio and debt-servicing ratio applicable to non-residential property mortgage loans also apply to standalone car park space mortgage loans.
- Introduce a risk-weight floor of 15% for all new residential mortgages granted by banks using the internal ratings-based approach.

These measures would help ensure a healthy and stable development of the property market and maintain the overall macroeconomic and financial stability. The Government will closely monitor the market situation and introduce further measures when necessary.

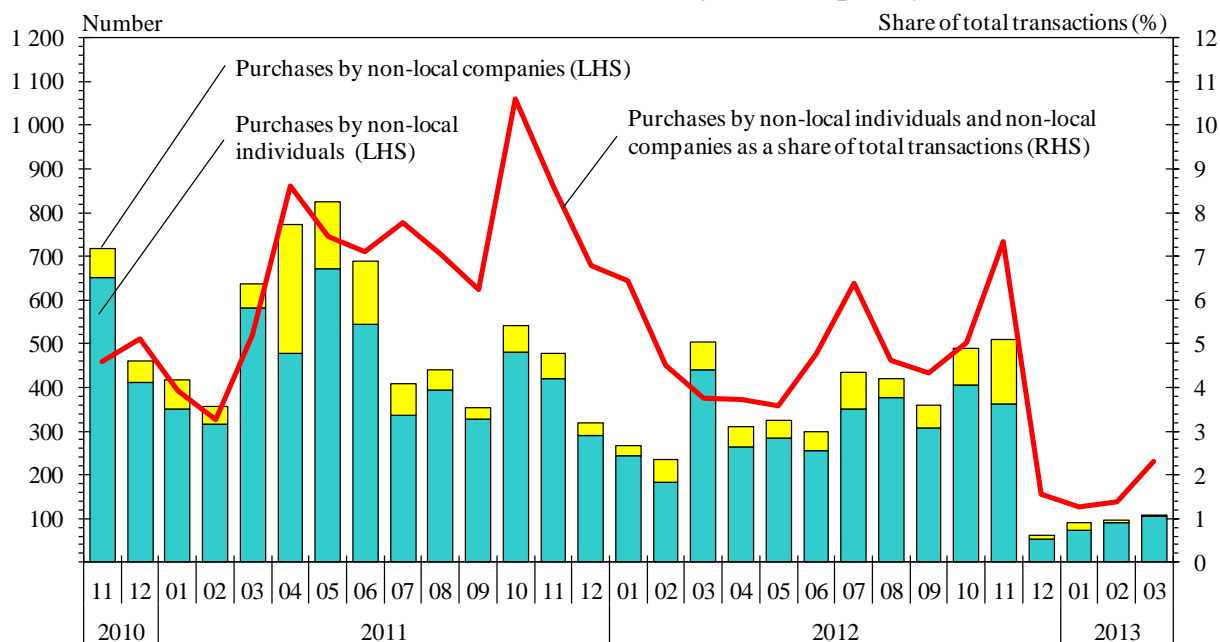
3.8 These measures have yielded noticeable results. On *speculative activities*, there were on average only 227 cases of short-term resale (comprising confirmor transactions and resale within 24 months after assignment) per month or 3.6% of total transactions in the first quarter, markedly below the monthly average of 2 661 cases or 20.0% in January to November 2010 (i.e. the period before the introduction of the Special Stamp Duty). Reflecting the effects of the Buyer's Stamp Duty, *purchases by non-local individuals and non-local companies* plunged to an average of 98 cases per month or 1.6% of total transactions in the first quarter, markedly lower than the monthly average of 365 cases or 4.5% in January to October 2012. As to *mortgage lending*, the average loan-to-value ratio of new mortgages was 55% in the first quarter, much lower than the average of 64% in January to October 2009 before the first round of macro-prudential measures for residential property mortgage lending was introduced by the HKMA.

Diagram 3.4 : Speculative activities were sharply reduced



Note : Confirmor transactions refer to resale before assignment.

Diagram 3.5 : Purchases by non-local buyers stayed subdued after the introduction of the Buyer's Stamp Duty

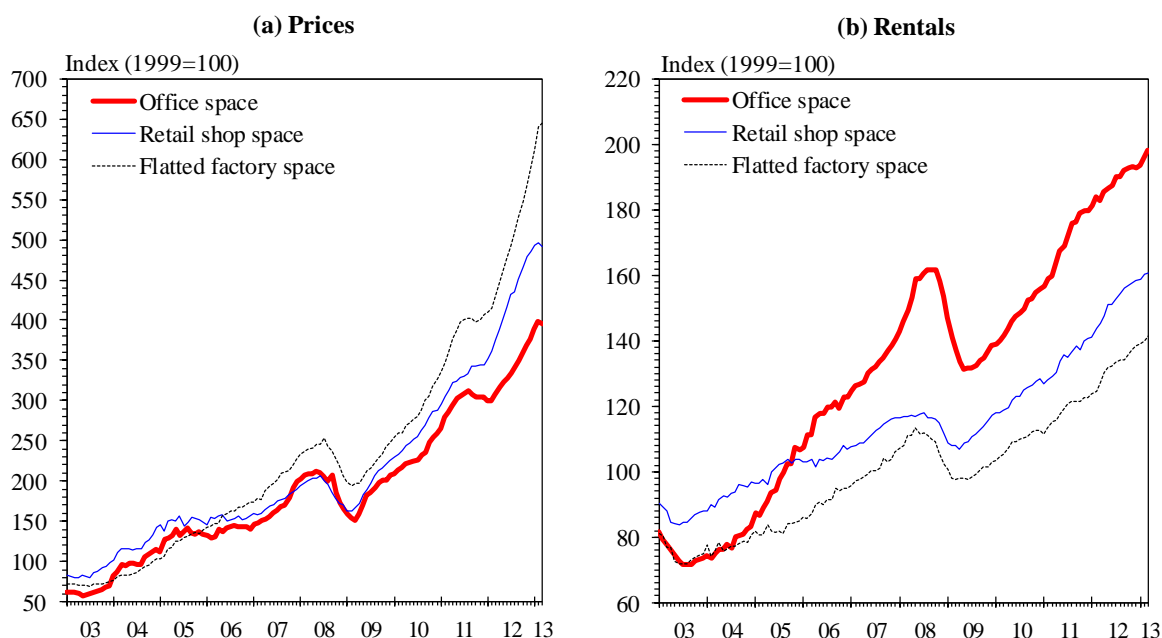


3.9 The *commercial* and *industrial property markets* remained generally buoyant in the first two months of 2013, but showed some cool-off in March following the announcement of the latest demand management measures (**Box 3.1**). Sale prices of *retail shop space* rose by 2% between December 2012 and March 2013, with the gains in January and February partially offset by the decline in March. Meanwhile, rentals increased by 1%. The average rental yield for retail shop space was 2.4% in March 2013, same as in December 2012. Transactions for retail shop space edged down by 1% from the preceding quarter to an average of 800 cases per month in the first quarter⁽²⁾. This was however still 24% higher than the monthly average in January to November 2010.

3.10 Sale prices of *office space* rose by 5% between December 2012 and March 2013, but a monthly decline was in fact recorded in March. Within the total, the prices of Grade A, B and C office space increased by 5%, 4% and 7% respectively. Meanwhile, overall office rentals recorded a gain of 3%. The gains for Grade A, B and C office space were 3%, 3%, and 2% respectively. The average rental yields for Grade A and B office space remained at 2.9% in March 2013, same as in December 2012, while that for Grade C office space edged down from 2.9% to 2.8%. Trading activities were largely sustained in January and February, but plunged to a very low level in March. For the quarter as a whole, transactions for office space fell by 16% from the preceding quarter to a monthly average of 310 cases. Yet this was still 4% above the monthly average in January to November 2010.

3.11 For *flatted factory space*, sale prices surged by 10% between December 2012 and March 2013 notwithstanding the decelerated increase recorded in March. Meanwhile, rentals increased by 2%. The average rental yield declined further from 2.9% in December 2012 to 2.7% in March 2013. Transactions for flatted factory space plunged by 34% from the high base in the preceding quarter to a monthly average of 810 cases in the first quarter. This was however still 19% higher than the monthly average in January to November 2010.

Diagram 3.6 : The market for non-residential properties also slowed down in March



Land

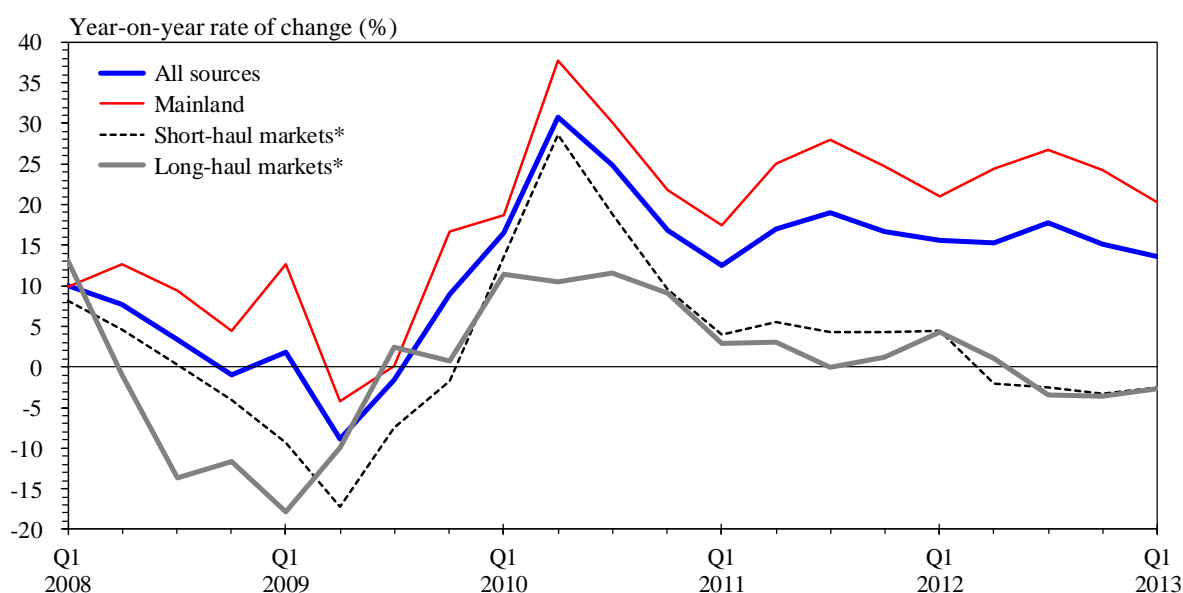
3.12 Reflecting the Government’s ongoing efforts to increase land supply, eight land sites with a total area of about 12.6 hectares were sold by public tender in the first quarter of 2013, fetching a land premium of \$24.2 billion. Within the total, there were five residential sites, one commercial site, one hotel site and one site for hospital development. The tender exercises for four residential sites also commenced in March, including one in Tsueng Kwan O, one in Tuen Mun, and two in Kai Tak on which the “Hong Kong Property for Hong Kong People” conditions would apply.

3.13 Regarding exchange of land, one industrial/godown site with an area of about 0.08 hectare was approved in the first quarter. As to lease modifications, seven sites were approved.

Tourism

3.14 The inbound tourism sector maintained solid growth in the first quarter of 2013, though performance was mixed among different markets. Overall *visitor arrivals* leapt by another 13.5% over a year earlier to 12.7 million, as the strong growth in the Mainland market more than offset the declines in other markets. Visitor arrivals from the Mainland surged by 20.3% to 9.5 million and constituted 74.6% of all visitors. Meanwhile, visitors from the short-haul and long-haul markets declined further by 2.5% and 2.7% respectively⁽³⁾. Analysed by the length of stay, the increase in same-day visitors, at 19.5%, was much faster than that in overnight visitors, at 7.4%. As a result, the share of same-day visitors expanded from 50.5% a year earlier to 53.1% in the first quarter, while that of overnight visitors declined from 49.5% to 46.9%.

Diagram 3.7 : Inbound tourism maintained solid growth on the back of sustained surge in Mainland visitors



Note: (*) See note (3) at the end of this chapter for the definition of short-haul and long-haul markets.

3.15 Supported by the solid growth in visitor arrivals, hotel room occupancy rate was at a high 87% in the first quarter, same as a year earlier. The average achieved hotel room rate edged down by 0.7% to \$1,470⁽⁴⁾. Underpinned by the strong growth in visitor arrivals and also a higher per capita visitor spending (**Box 3.2**), total tourism expenditure associated to inbound tourism surged by 14.6% to \$296.5 billion in 2012.

Box 3.2

Per capita spending of incoming visitors

Expenditure of incoming visitors in Hong Kong recorded spectacular growth in the past decade. According to the Hong Kong Tourism Board (HKTB), total tourism expenditure associated to inbound tourism⁽¹⁾ reached a record high of \$296.5 billion in 2012. This represented a cumulative surge of 286% over 2002, or a notable average annual growth of 14.5% during the period. Apart from a sustained influx of incoming visitors, the surge in total tourism expenditure was also driven by rising per capita spending of visitors.

For same-day in-town visitors, their per capita spending⁽²⁾ grew by a sturdy 13.1% per annum in the past decade to \$2,121 in 2012. Within the total, per-capita spending of such visitors from the Mainland, in terms of both the level in 2012 and the ten-year average annual growth rate, at \$2,489 and 10.0% respectively, was distinctly above their non-Mainland counterparts, at \$665 and 4.4%⁽³⁾. This was possibly due to the fact that around half of the non-Mainland same-day in-town visitors were en-route to other places⁽⁴⁾ and thus had limited time for spending in Hong Kong.

By comparison, per-capita spending of overnight visitors grew at a more moderate pace of 4.9% per annum over the past ten years to \$7,818 in 2012. Within this total, per capita spending of Mainland and non-Mainland overnight visitors grew by 4.6% and 4.2% per annum respectively⁽³⁾. Per capita spending of Mainland overnight visitors has exceeded that of non-Mainland visitors since 2007. At \$8,565 in 2012, per capita spending of Mainland overnight visitors was 31% above that of the non-Mainland counterparts.

Table : Per-capita spending of incoming visitors in 2012

	Same-day <u>in-town visitors</u>	Overnight <u>visitors</u>
Per capita spending	\$2,121	\$7,818
(Average annual growth in 2003-2012)	(13.1%)	(4.9%)
<i>Within which :</i>		
(i) <i>Mainland visitors</i>	\$2,489	\$8,565
<i>(Average annual growth in 2003-2012)</i>	<i>(10.0%)</i>	<i>(4.6%)</i>
(ii) <i>Non-Mainland visitors</i>	\$665	\$6,516
<i>(Average annual growth in 2003-2012)</i>	<i>(4.4%)</i>	<i>(4.2%)</i>

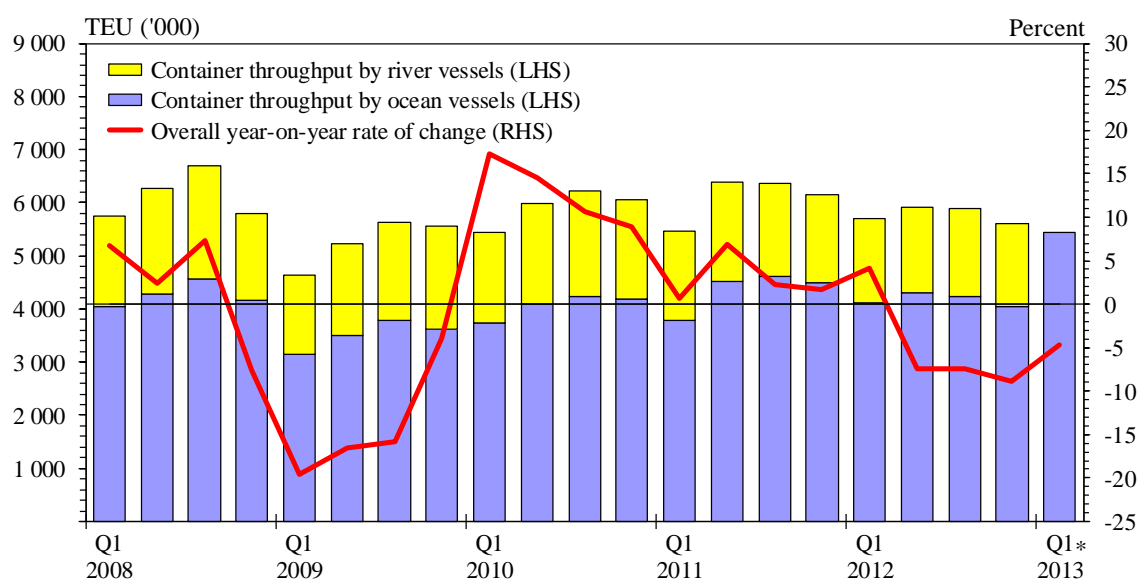
- (1) Tourism expenditure associated to inbound tourism comprises destination consumption expenditure by overnight and same-day in-town visitors, cruise passengers, servicemen, aircrew members and transit/transfer passengers, and international transportation expenditure.
- (2) Per capita spending is calculated based on destination consumption expenditure only.
- (3) The average annual growth for all same-day in-town visitors (at 13.1%) exceeded that for Mainland and non-Mainland visitors (at 10.0% and 4.4% respectively), as it has included the compositional effect of a higher share of Mainland visitors, who had a higher per capita spending. This is also the case for the growth rate of per capita spending of overnight visitors.
- (4) According to HKTB, 51% of the non-Mainland same-day in-town visitors in 2012 indicated “en-route” as their purpose of visiting Hong Kong, sharply higher than the share of 11% for the Mainland counterparts.

Logistics

3.16 As the external trade environment turned less steady, performance of the logistics sector was subdued in the first quarter. *Total container throughput* fell further by 4.6% from a year earlier to 5.4 million TEUs. In parallel, the value of trade handled at the Hong Kong Port decreased by 1.7%, and its share in overall trade value declined further from 25.0% a year earlier to 23.5%.

3.17 A labour dispute started at the Kwai Chung Container Terminals on 28 March as a few hundred container terminal workers went on strike for higher pay and improvement in working conditions. The strike has caused some impact on the operation of the container terminals and could have more visible impact on the overall throughput in the second quarter. The Government has taken active steps in conciliating the dispute.

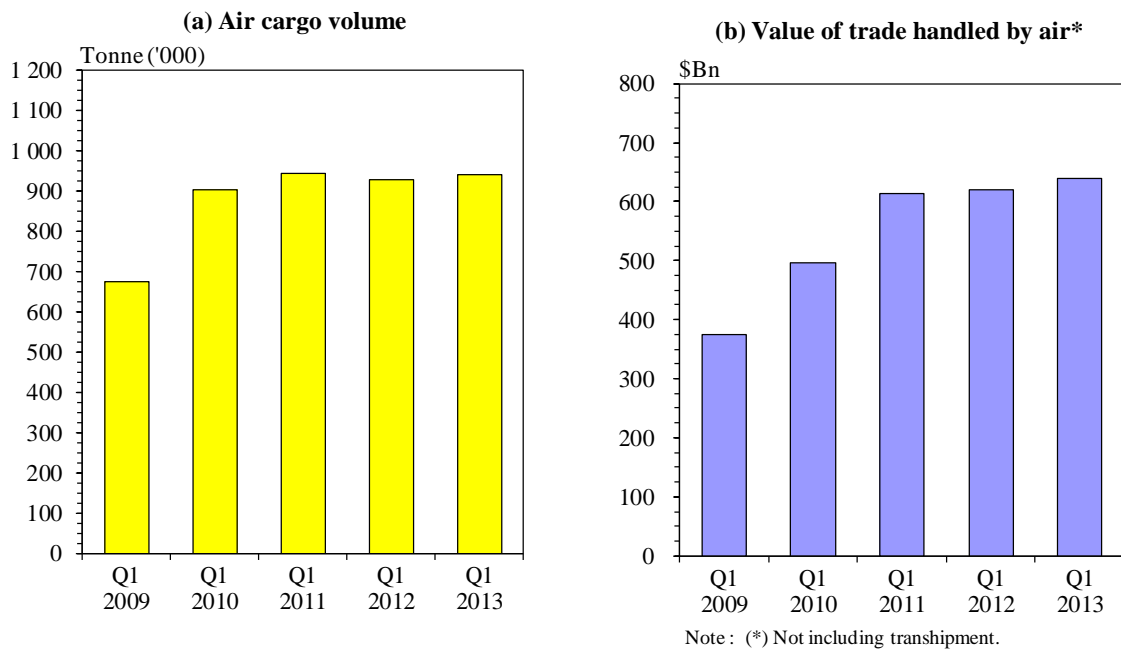
Diagram 3.8 : Container throughput fell further



Note: (*) The container throughput figure for the latest quarter is the preliminary estimate by the Hong Kong Port Development Council, for which a breakdown by ocean and river vessels is not yet available.

3.18 *Air freight throughput* was also modest, edging up by a mere 1.3% over a year earlier to 942 000 tonnes in the first quarter. The total value of trade by air increased by 3.1%, while its share in overall trade value decreased from a record high of 37.3% a year earlier to 36.9%.

Diagram 3.9 : Air cargo throughput and value of trade handled by air showed modest performance



Transport

3.19 Traffic flows for most major modes of transport improved in general. Air passenger traffic rose by 5.2% over a year earlier to 14.3 million in the first quarter, and water-borne passenger trips by 4.4% to 6.8 million. As to land-based cross-boundary traffic movements, average daily passenger trips increased by 7.4% to 572 800 while average daily vehicular movements dropped by 2.4% to 39 900.

3.20 In February the Government launched a three-month public consultation on the proposed measures to improve traffic distribution among the road harbour crossings. Three options involving toll adjustment of different degrees at the Eastern Harbour Crossing (EHC) and the Cross Harbour Tunnel (CHT) were put forward with a view to diverting some traffic from the CHT to the EHC, thereby alleviating the traffic congestion at the CHT. If there is sufficient support in the community, the Government will negotiate with the tunnel franchisee concerned, seek funding from the Finance Committee of the Legislative Council, and take forward the necessary legislative procedures for conducting a 12-month trial of the preferred option in the second half of 2014 to test its effectiveness.

Creativity and Innovation

3.21 In February the Government announced the way forward for the development of the patent system in Hong Kong. The key plans include

introducing an “original grant” patent system with substantive examination outsourced to other patent office(s) while retaining the current re-registration system, retaining the short-term patent system with suitable refinements, and developing a full-fledged regulatory regime on patent agency services in the long run. The Government will work out the details of the implementation plan in the next phase.

Environment

3.22 In March the Environment Bureau unveiled “A Clean Air Plan for Hong Kong”. The Plan outlines comprehensively the challenges that Hong Kong is facing with regard to air quality and gives a detailed account of the air quality management system in Hong Kong, as well as the measures to tackle air pollution from different sources such as transport and power plants. The Plan also sets the target of largely achieving the new Air Quality Objectives by 2020.

Notes :

- (1) For details of the measures promulgated in 2010, see Box 3.1 in the First Quarter Economic Report 2010, Box 3.1 in the Third Quarter Economic Report 2010 and note (2) at the end of Chapter 4 in the 2010 Economic Background and 2011 Prospects. For details of the measures promulgated in 2011, see note (2) at the end of Chapter 3 in the Half-yearly Economic Report 2011, Box 3.1 in the Third Quarter Economic Report 2011. For details of the measures promulgated in 2012, see Box 3.1 in the Third Quarter Economic Report 2012 and Box 4.1 of 2012 Economic Background and 2013 Prospects. For details of the measures promulgated in 2013, see Box 4.2 of 2012 Economic Background and 2013 Prospects and Box 3.1 of this report.
- (2) The figures on transaction refer to commercial space, which comprises retail premises and other premises designed or adapted for commercial use but excludes purpose-built office space.
- (3) Short-haul markets refer to North Asia, South & Southeast Asia, Taiwan and Macao, but excluding the Mainland, while long-haul markets refer to the Americas, Europe, Africa, the Middle East, Australia, New Zealand and South Pacific. In the first quarter of 2013, visitor arrivals from the Mainland, short-haul and long-haul markets accounted for respective shares of 75%, 17% and 9% of total visitors.
- (4) The figures on hotel room occupancy and achieved room rate do not include tourist guesthouses.