CHAPTER 4 : DEVELOPMENTS IN SELECTED SECTORS

Summary

- *Following the brief consolidation in late 2015 and early 2016, the residential property market rebounded in the second quarter and turned exuberant in the third quarter amid a still tight demand-supply situation. Yet the market cooled down visibly after the Government introduced the latest round of demand-side management measure in early November, with trading activities turning very quiet and the upward momentum in flat prices moderating noticeably. Overall flat prices rose by a cumulative 8% during the full-year 2016.*

- *The Government's sustained efforts to increase land and flat supply have yielded results. Total flat supply in the coming three to four years rose to a new record high of 94 000 units. Meanwhile, as the various demand-side management measures yielded the intended results, speculative activities remained subdued and non-local demand stayed low in 2016, while investment activities also quietened down markedly towards the end of the year.*

- *The commercial and industrial property markets remained lacklustre in 2016, despite some relative firm-up in the latter part of the year. Trading activities were very quiet, while prices and rentals generally showed modest performance.*

- *Inbound tourism remained in a consolidation mode during most of 2016, but there was some relative improvement since the second quarter as the effect of the "one trip per week" Individual Visit Endorsements gradually faded. Overall visitor arrivals reverted to a marginal year-on-year increase in the fourth quarter, though for 2016 as a whole they still fell by 4.5% to 56.7 million, representing the second consecutive year of annual decline.*

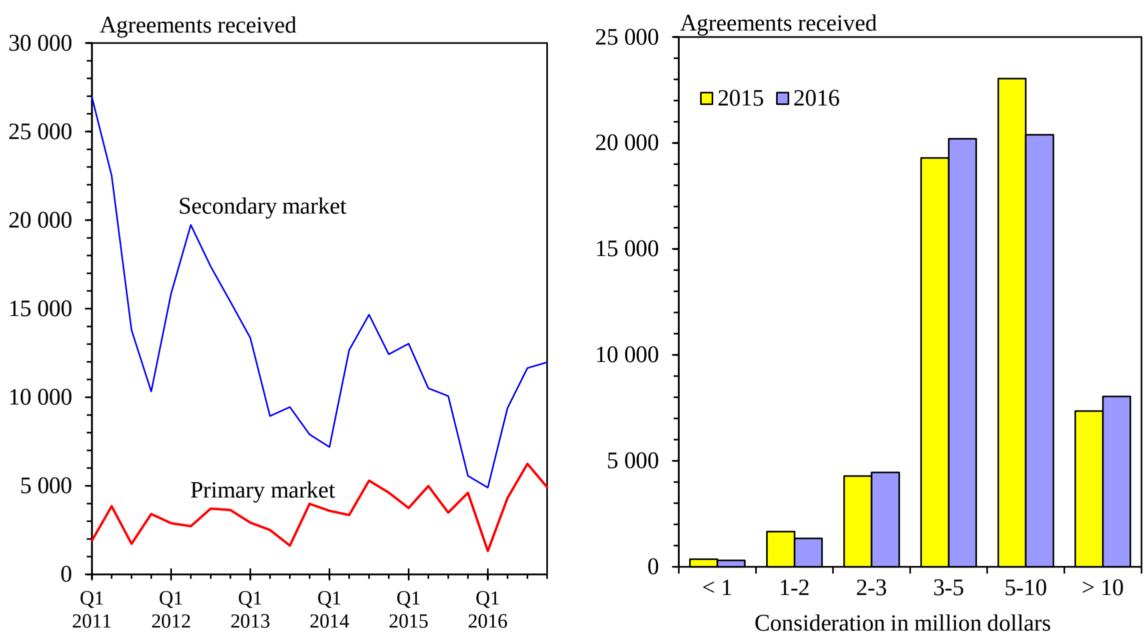
- *The logistics sector showed some pick-up over the course of 2016 along with the gradual improvement of the external trade environment. Total container throughput declined by a narrowed 2.5% to 19.6 million twenty-foot equivalent units, while air freight throughput rose by 3.2%.*

Property

4.1 Following the brief consolidation in late 2015 and early 2016, the *residential property market* rebounded in the second quarter and turned exuberant in the third quarter amid a still tight demand-supply balance of flats. With a view to forestalling a further build-up of housing bubble risks, the Government raised the ad valorem stamp duty on residential property transactions to a flat rate of 15% in early November(1). The market cooled down visibly thereafter, also aided by the US interest rate hike later in mid-December. Trading activities turned very subdued, while the upward momentum in flat prices was arrested.

4.2 The total number of sale and purchase agreements for residential property received by the Land Registry fell by 2% to 54 701 in 2016, sharply below the long-term average of 91 878 from 1996 to 2015. There were however sharp fluctuations through the year, rebounding from a low of 1 807 in February to a high of 6 739 in November, before slowing down markedly to 3 550 in December when both buyers and sellers adopted a "wait-and-see" attitude following the introduction of the latest demand-side management measure. Within the total, secondary market transactions declined by 3% to a record low of 37 908 in 2016, while primary market transaction level was almost the same at 16 793. Total consideration went up slightly by 3% to $428.0 billion in 2016.

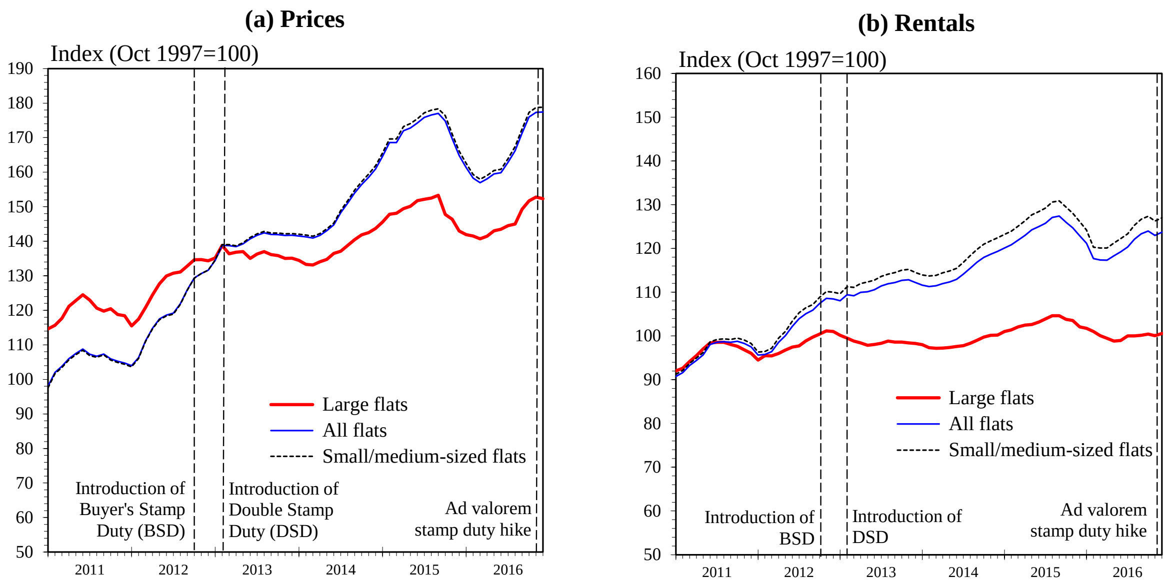
Diagram 4.1 : Trading activities picked up through most of the year before moderating after November



4.3 Flat prices also exhibited sharp volatilities over the course of the year. Overall flat prices switched from a fall of 5% during the first quarter to an increase of 2% during the second quarter and 7% during the third quarter, but the increase moderated to 4% during the fourth quarter reflecting the sharp deceleration after the latest hike in ad valorem stamp duty. For the year as a whole, overall flat prices in December 2016 still went up by 8% over December 2015. Analysed by size, prices of small/medium-sized flats and large flats leaped by 8% and 7% respectively.

4.4 In parallel, the leasing market also revived since the second quarter before cooling down again in the fourth quarter. Overall flat rentals in December 2016 inched up by 1% over December 2015, but were still 3% below the peak in September 2015. Analysed by size, rentals of small/medium-sized flats rose by 1% during 2016, while rentals of large flats declined by 1%. Reflecting the relative movements of flat prices and rentals, the average rental yield for residential property edged down from 2.8% in December 2015 to 2.6% in December 2016.

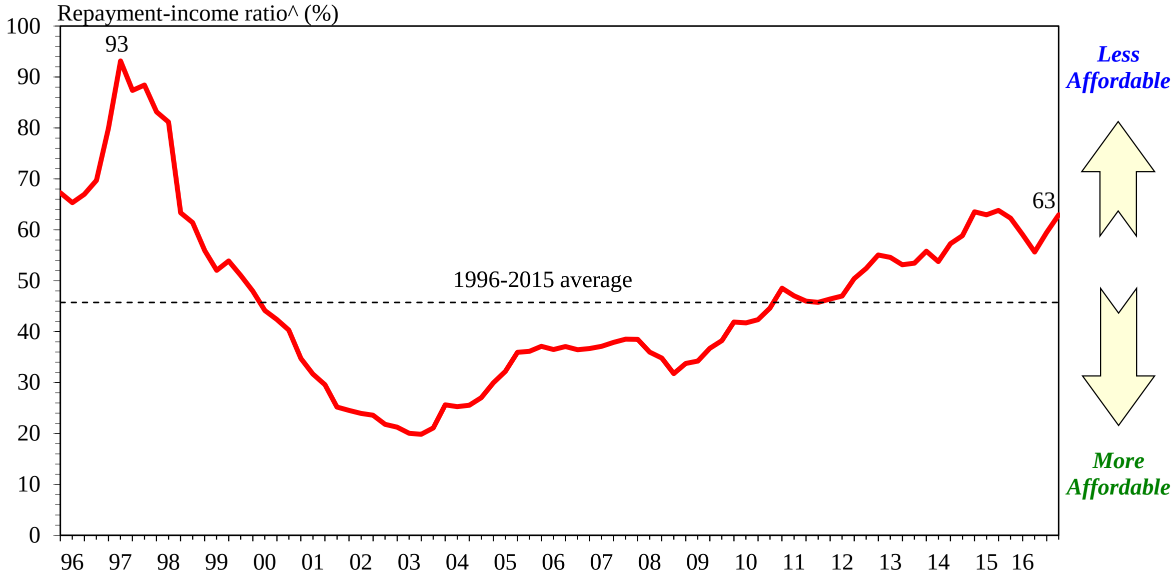
Diagram 4.2 : Flat prices and rentals showed decelerated growth in the fourth quarter



Note : Residential property price index pertains to secondary market transactions only. Large flats refer to those with a saleable area of at least 100 m^2, and small/medium-sized flats with a saleable area of less than 100 m^2.

4.5 As a result of the surge over the past several years, overall flat prices in December 2016 exceeded the 1997 peak by 77%. 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) worsened to around 63% in the fourth quarter, significantly above the long-term average of 46% over 1996-2015. Should interest rates rise by three percentage points to a more normal level, the ratio would soar to 82%.

Diagram 4.3 : The mortgage payment to income ratio rose further



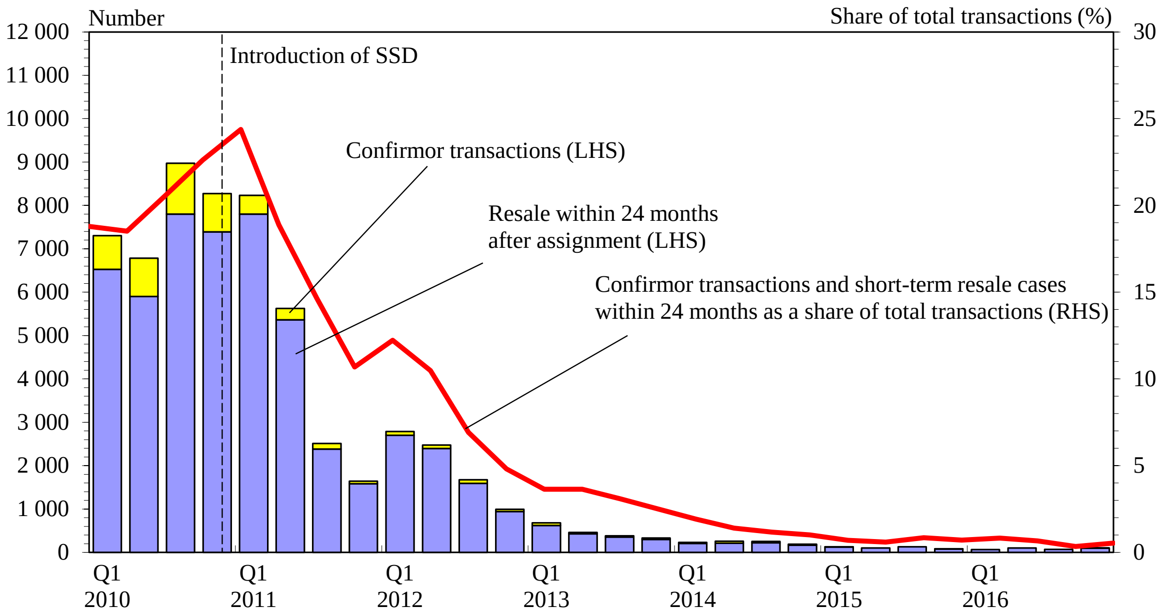
Note : (^) The ratio of mortgage payment for a 45m^2 flat (assuming 70% loan-to-value ratio and tenor of 20 years) to median income of households (excluding those living in public housing).

4.6 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. As at mid-January 2017, more than 20 residential sites, capable of providing more than 14 500 flats, have been sold or would be put up for sale in 2016-17 by the Government under the Land Sale Programme. This is the highest flat production capacity of government land sale sites since the Government-initiated Sale Mechanism was introduced in 2010-11. Combining other sources (including railway property development projects, the Urban Renewal Authority's projects, and private development and redevelopment projects), the aggregate private housing land supply in 2016-17 was estimated to have the capacity of producing over 19 000 flats, exceeding the annual supply target for the third consecutive year.

4.7 While the demand-supply balance of flats is still tight for the time being, it is set to ease in the years ahead. Gross completions of private flats surged by 29% to 14 600 units in 2016. After netting off demolition of 1 100 units, the net completions of 13 500 units were higher than the take-up of 11 900 units(2), and the vacancy rate thus edged up from 3.7% at end-2015 to 3.8% at end-2016. The Rating and Valuation Department forecasts that completions will rise to 17 100 units and 19 500 units respectively(3) in 2017 and 2018, comparable to the average of 18 000 units per annum over 1996-2015. Reflecting the Government's sustained efforts in raising land supply, the number of private domestic units commencing work jumped by 15% to 20 800 in 2016. The *total supply of flats* in the coming three to four years (comprising unsold flats of completed projects, flats under construction but not yet sold and flats on disposed sites where construction can start any time) rose to a new record high of 94 000 units as estimated at end-2016. An additional 7 300 units could also be added to the total supply after the conversion of a number of residential sites into "disposed sites".

4.8 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[(4)]. These measures have yielded notable results. On *speculative activities*, the number of short-term resale (comprising confirmor transactions and resale within 24 months after assignment) remained subdued at an average of 28 cases per month or 0.5% of total transactions in 2016, well 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* also stayed low at 94 cases per month or 1.8% of total transactions in 2016, much lower than the monthly average of 365 cases or 4.5% in January to October 2012 (i.e. the period before the introduction of the Buyer's Stamp Duty). As an indicator of *investment activities*, purchases by Hong Kong Permanent Residents (HKPRs) who owned at least one residential property plunged to 225 cases or 6.3% of total transactions in December 2016, sharply below the monthly average of 1 181 cases or 22.1% in January to November 2016 before the latest hike in ad valorem stamp duty. For *mortgage lending*, the average loan-to-value ratio of new mortgages was 52% in 2016, likewise considerably below 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 Hong Kong Monetary Authority.

Diagram 4.4 : Speculative activities stayed subdued



Note : Confirmor transactions refer to resale before assignment.

Diagram 4.5 : Purchases by non-local buyers remained low

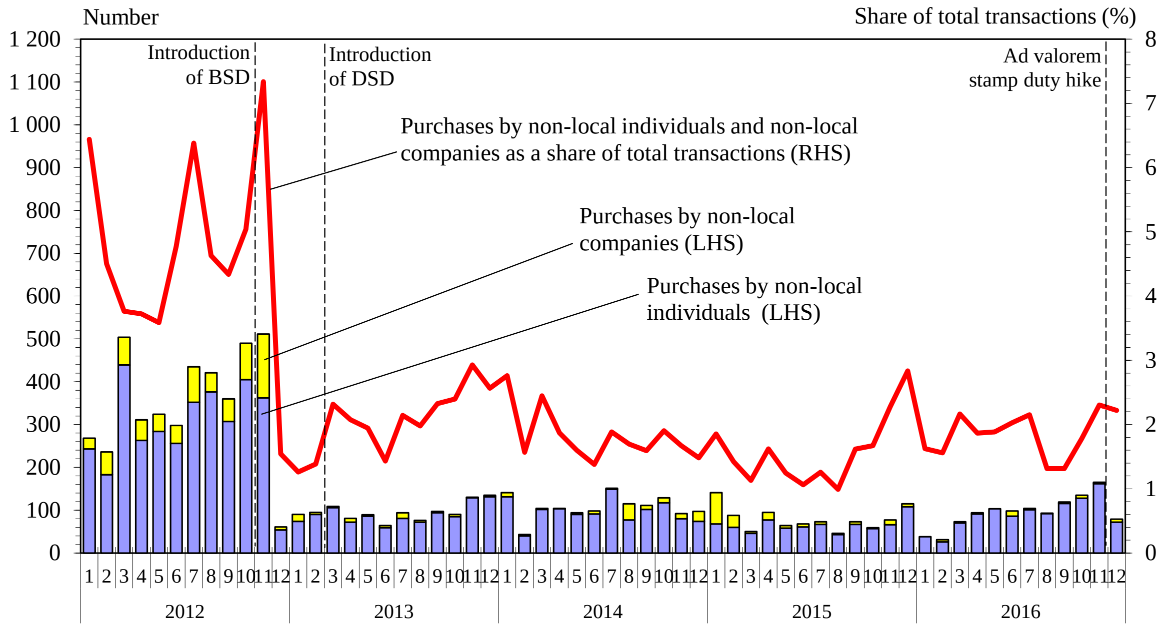
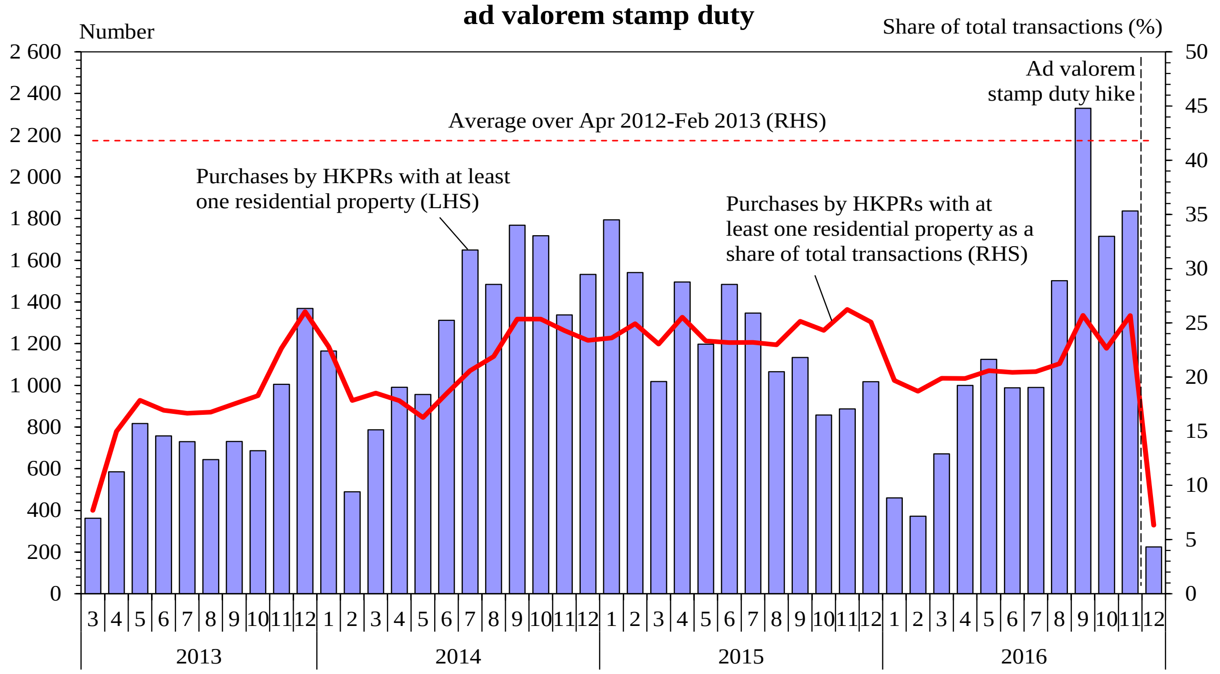


Diagram 4.6 : Investment activities quietened down after the latest hike in ad valorem stamp duty



4.9 Looking forward, the uncertain global and local economic conditions as well as the pace of US interest rate normalisation will continue to be the major factors affecting the residential property market this year. In the medium term, as and when the increased land supply over the past few years turns into actual production of flats, the demand-supply balance of flats will gradually ease thereby leading to a more stable and healthy market.

4.10 The *commercial* and *industrial property markets* remained lacklustre in 2016, despite some relative firm-up in the latter part of the year. Trading activities were very quiet, while prices and rentals generally showed modest performance.

4.11 Overall prices of *office space* fell by 2% between December 2015 and December 2016. Within the total, prices of Grade A office space stayed virtually unchanged, while prices of Grade B and C office space fell by 3% and 4% respectively. Over the period, overall rentals rose by 3%, with those of Grade A, B and C office space rising by 3%, 2% and 2% respectively. As a result, the average rental yield of Grade A, B and C office space rose to 3.0%, 3.1% and 3.1% respectively in December 2016, from 2.9%, 3.0% and 2.9% a year earlier. Transactions plunged by 25% to a historic low of 1 100 cases in 2016. As the take-up of 98 100 m^2 was lower than the completion of 153 100 m^2, the vacancy rate edged up from 8.0% at end-2015 to 8.2% at end-2016, but was still below the long-term average of 10.0% over 1996-2015.

4.12 The *retail shop space* market remained lacklustre in 2016, constrained by the weak retail sales. Between December 2015 and December 2016, prices stayed little changed, while rentals fell by 2%. The average rental yield stayed unchanged at 2.5% over the period. Trading activities plummeted further by 27% to a historic low of 1 510 cases in 2016[(5)]. The take-up was a negative 42 000 m^2, while the completion was 123 100 m^2. As a result, the vacancy rate rose from 7.7% at end-2015 to 9.0% at end-2016, slightly above the long-term average of 8.8% over 1996-2015.

4.13 Prices and rentals of *flatted factory space* rose by 3% and 4% respectively between December 2015 and December 2016. The average rental yield thus rose from 3.0% to 3.1% over the period. Transactions fell by 21% to a very low level of 2 690 cases in 2016. As to the demand-supply balance, there was a negative take-up of 189 300 m^2 against a completion of 4 500 m^2. The vacancy rate therefore rose from 5.0% at end-2015 to 5.8% at end-2016, but was still markedly below the long-term average of 8.0% over 1996-2015.

Diagram 4.7 : Prices and rentals of non-residential properties generally showed modest performance in 2016

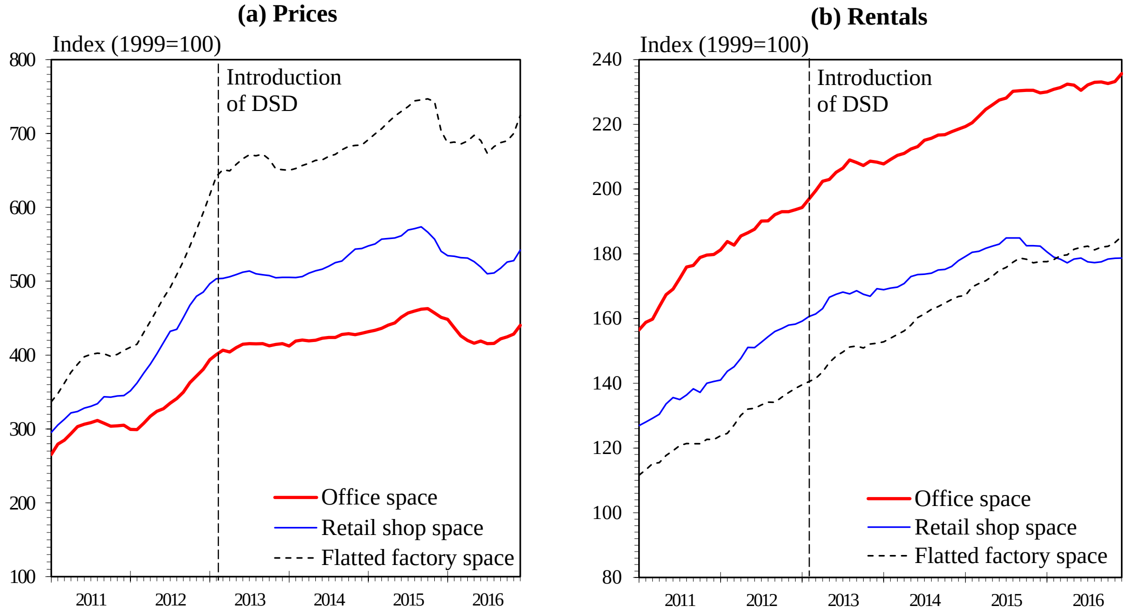
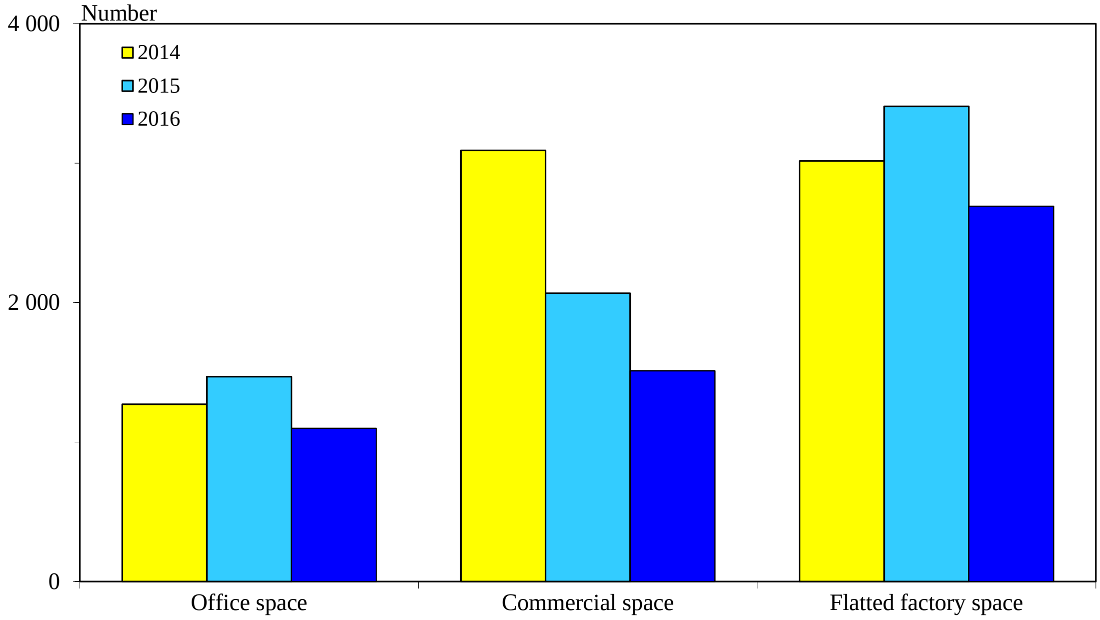


Diagram 4.8 : Trading activities for commercial and industrial properties were very quiet in 2016



Land and planning

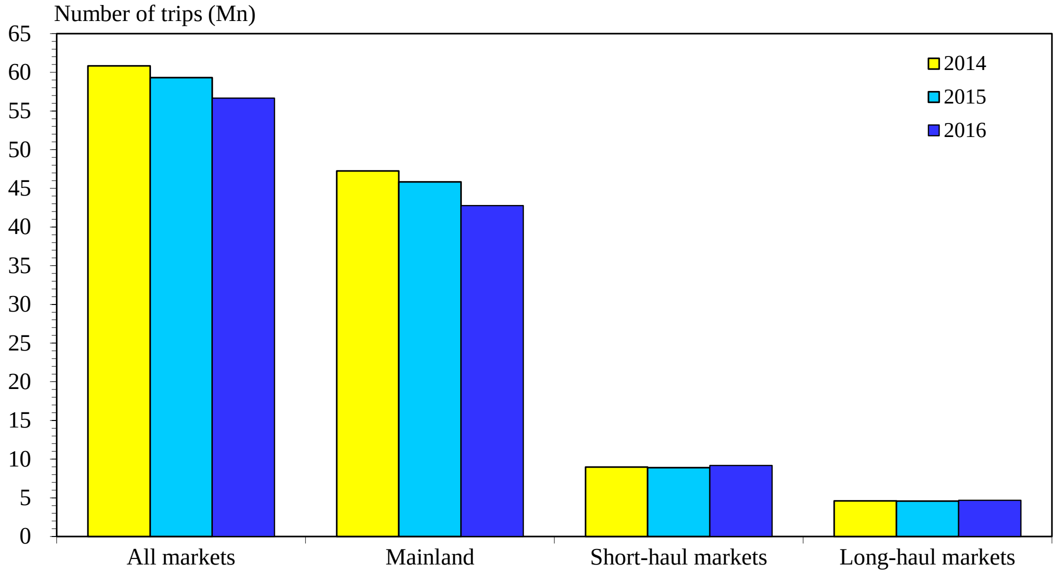
4.14 Thirty two sites with a total area of about 36.6 hectares were disposed of in 2016, fetching a land premium of $84.8 billion. Among these sites, there were 23 residential sites, two business sites, two commercial sites, one industrial site and four sites for petrol filling station. In addition, the tender exercises for one residential site in Kai Tak and one business site in Cheung Sha Wan commenced in the last quarter of the year. Regarding exchange of land, two sites with a total area of about 27.1 hectares were approved in 2016. As to lease modifications, a total of 67 sites were approved.

4.15 In October 2016, the Government launched a six-month public engagement exercise for “Hong Kong 2030+: Towards a Planning Vision and Strategy Transcending 2030” to collect views from the public on the updated territorial development strategy for Hong Kong. “Hong Kong 2030+” is a vision-driven, pragmatic and action-oriented strategic plan to guide planning, land and infrastructure development and shape the built environment of Hong Kong beyond 2030. The vision is for Hong Kong to become a more liveable, competitive and sustainable Asia’s world city.

Tourism

4.16 Inbound tourism remained in a consolidation mode during most of 2016, but there was some relative improvement since the second quarter as the effect of the “one trip per week” Individual Visit Endorsements[(6)] gradually faded. In the fourth quarter, overall *visitor arrivals* reverted to a marginal year-on-year increase of 0.4%, though for 2016 as a whole they still fell by 4.5% to 56.7 million, representing the second consecutive year of annual decline. Mainland visitors, which accounted for 75.5% of the total, fell by 6.7% to 42.8 million. Meanwhile, visitor arrivals from the short-haul and long-haul markets reverted to increases of 3.4% and 2.3% respectively[(7)] in 2016.

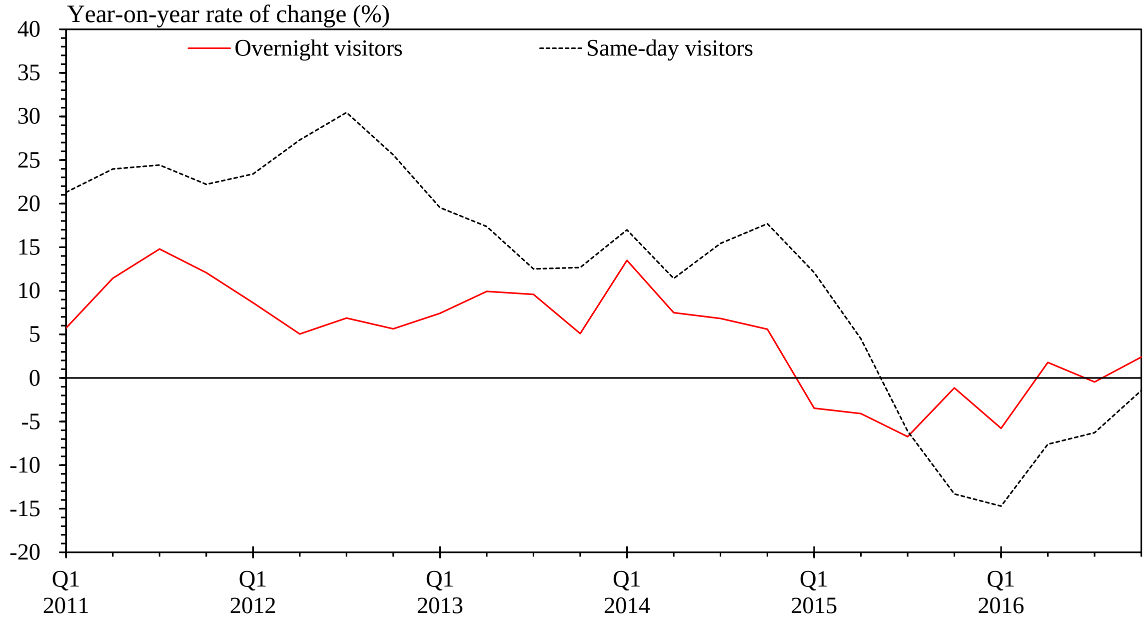
Diagram 4.9 : Inbound tourism remained in a consolidation mode during most of 2016



Note : See note (7) at the end of this chapter for the definition of short-haul and long-haul markets.

4.17 Analysed by the length of stay, same-day visitor arrivals declined by another 7.7% in 2016, but the year-on-year decline has narrowed visibly since the second quarter. Overnight visitor arrivals also stabilised gradually and only edged down by 0.5% for the year as a whole. Reflecting these movements, the share of same-day visitors dropped from 55.0% in 2015 to 53.1% in 2016, while that of overnight visitors rose from 45.0% to 46.9%.

Diagram 4.10 : Both overnight and same-day visitors declined in 2016, but there has been some relative improvement since the second quarter



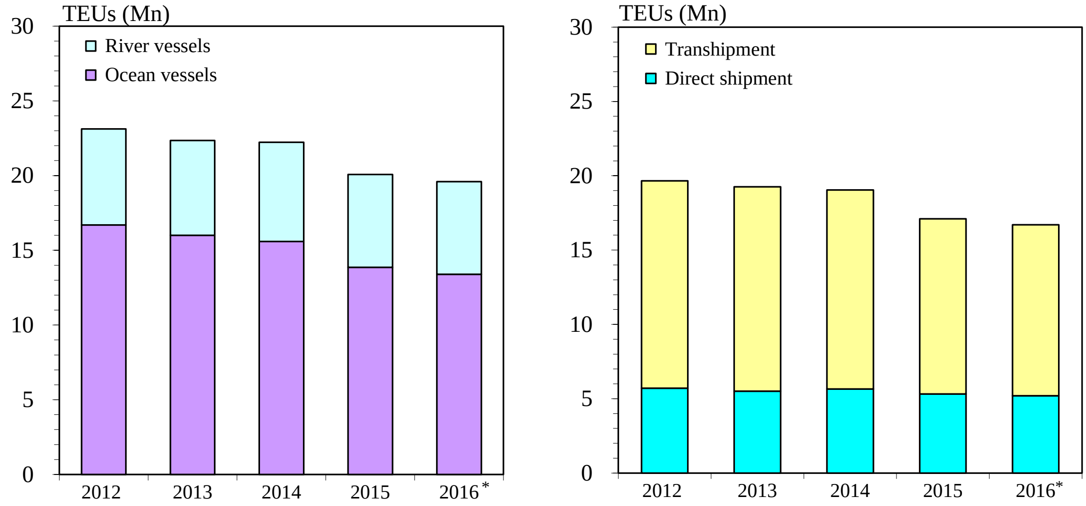
4.18 Supported by the stabilisation of overnight visitor arrivals, the average hotel room occupancy rate edged up from 86% in 2015 to 87% in 2016. The average achieved hotel room rate also declined by a less rapid 3.7%, to $1,287[(8)].

Logistics

4.19 The logistics sector showed some pick-up over the course of 2016 along with the gradual improvement of the external trade environment. *Total container throughput* declined at a narrowed rate of 2.5% to 19.6 million twenty-foot equivalent units (TEUs) for the year as a whole, with the year-on-year change improving steadily from a drop of 12.1% in the first quarter to a gain of 12.7% in the fourth quarter. Within the laden container throughput, the declines in both direct shipment and transhipment narrowed, to 1.5% and 2.3% respectively. In parallel, the value of trade handled at the Hong Kong port fell by 8.7%, and its share in total trade shrank further from 20.5% in 2015 to 18.8% in 2016.

Diagram 4.11 : Container throughput showed some pick-up over the course of 2016

(a) Total container throughput by mode of transport **(b) Laden container throughput by mode of shipment**

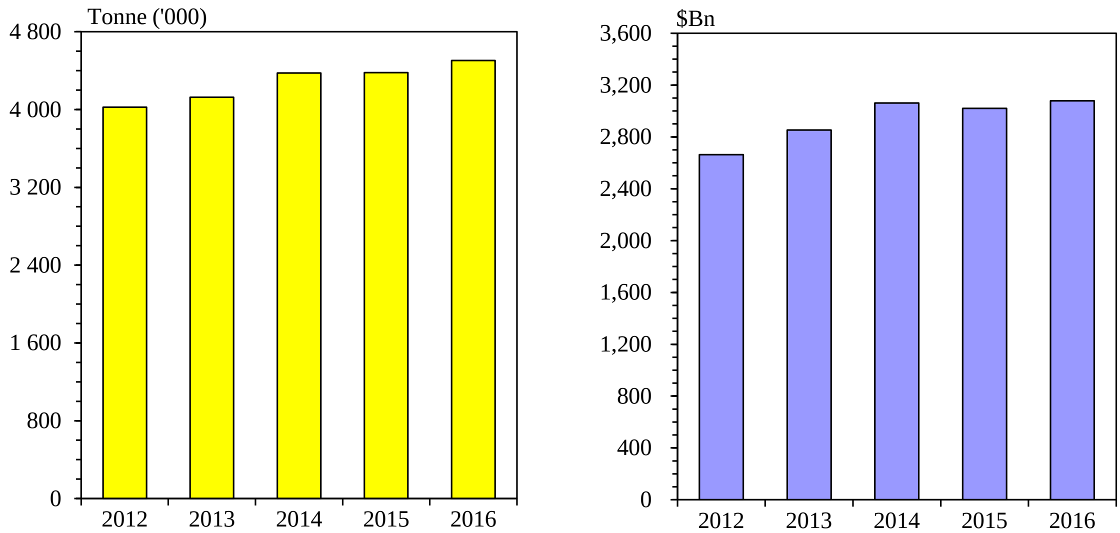


Note : (*) Total container throughput for 2016 is the preliminary estimate by Hong Kong Port Development Council. Its breakdown by mode of transport and the laden container throughput by mode of shipment are crudely estimated from the profile in the first ten months of 2016.

4.20 *Air freight throughput* fared better and rose by 3.2% to 4.5 million tonnes in 2016. Likewise, the value of trade by air rose by 1.9%, with its share in total trade increasing from 39.5% to 40.5%.

Diagram 4.12 : Air cargo throughput and the value of trade handled by air rose in 2016

(a) Air cargo volume **(b) Value of trade handled by air***



Note : (*) Not including transhipment.

Transport

4.21 Traffic flows for the different major modes of transport showed mixed performances in 2016. Air passenger traffic increased further, by 2.9% to

70.5 million, while water-borne passenger trips fell by another 3.4% to 26.7 million. As to land-based cross-boundary traffic, passenger trips edged down by 0.6% to 221.3 million, while average daily vehicle movements rose slightly by 2.0% to 42 328.

4.22 The extension of the Kwun Tong Line and the South Island Line of the Mass Transit Railway (MTR) commenced operation in October and December 2016 respectively. With the addition of six new stations (namely Ho Man Tin station, Whampoa station, Ocean Park station, Wong Chuk Hang station, Lei Tung station and South Horizons station), the extended MTR network now reaches all 18 districts of Hong Kong. The extension would reduce travelling time for commuters and further strengthen the efficiency and connectivity of the public transport network of Hong Kong.

Innovation and technology

4.23 In January 2017, the HKSAR Government and the Shenzhen Municipal Government signed a memorandum of understanding on the development of a Hong Kong/Shenzhen Innovation and Technology Park in the Lok Ma Chau Loop in Hong Kong. The park, with a site area quadruple that of the Science Park, will be a key base for co-operation between Hong Kong and the Mainland in innovation and technology research.

Environment

4.24 In the 2017 Policy Address, the Chief Executive announced that he accepted the proposals recommended by the Steering Committee on Climate Change, to reduce carbon intensity from the 2005 level by 65% to 70% by 2030. On air quality, the HKSAR Government signed an agreement with the Mainland to jointly promote the establishment of a domestic emission control area in the Pearl River Delta waters to regulate emissions from marine vessels. Separately, the Government also plans to introduce the bill for implementing quantity-based municipal solid waste charging in the current legislative year.

Notes :

(1) On 4 November 2016, the Government announced to increase the ad valorem stamp duty rates for residential property transactions to a flat rate of 15% with effect from 5 November 2016, in lieu of the ad valorem stamp duty rates at Scale 1 (commonly known as "doubled ad valorem stamp duty"). The exemptions and exceptions introduced through the Stamp Duty (Amendment) (No. 2) Ordinance 2014 will not be affected. Thus, a Hong Kong Permanent Resident acquiring a residential property where he/she is acting on his/her own behalf and does not own any other residential property in Hong Kong at the time of acquisition will continue to be subject to the existing ad valorem stamp duty rates at Scale 2.

(2) Take-up figures represent the net increase in the number of units occupied. The figures are arrived at by adding the completions in that year to the vacancy figures at the beginning of the year, then subtracting the year's demolition and the year-end vacancy figures. Take-up should not be confused with the sales of new developments, and it bears no direct relationship to the number of units sold by developers. Negative take-up means that there is a decrease in the number of units occupied (i.e. property previously occupied was released during the year and remained vacant at the year-end). Also, take-up, demolition, completion and vacancy figures on residential and non-residential properties are preliminary figures from the Rating and Valuation Department, and are subject to revision.

(3) Forecast completions in 2017 and 2018 are preliminary figures only, and are subject to revision upon the availability of more data.

(4) 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 and 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 in the 2012 Economic Background and 2013 Prospects. For details of the measures promulgated in 2013, see Box 4.2 in the 2012 Economic Background and 2013 Prospects and Box 3.1 in the First Quarter Economic Report 2013. For details of the measures promulgated in 2014, see Box 4.1 in the 2013 Economic Background and 2014 Prospects. For details of the measures promulgated in 2015, see Box 3.1 of the First Quarter Economic Report 2015.

(5) The figures on transaction and vacancy rate refer to commercial space, which comprises retail premises and other premises designed or adapted for commercial use but excludes purpose-built office space.

(6) For details of the change in Individual Visit Endorsements policy in April 2015, see paragraph 3.17 in the Half-yearly Economic Report 2015.

(7) Short-haul markets refer to North Asia, South and 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 2016, visitor arrivals from the Mainland, short-haul and long-haul markets accounted for respective shares of 76%, 16% and 8% of total visitors.

(8) The figures on hotel room occupancy and achieved room rate do not include guesthouses.