Property - High Times

By Christopher Dillon

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After plunging two-thirds in the wake of the 1997 Asian financial crisis, Hong Kong's property market is booming. Fuelled by low interest rates, an open door to foreign investors and a buoyant Chinese economy, the University of Hong Kong All Residential Price Index rose 28.4 per cent during the 12 months ended August 31, 2010.

The Hong Kong Special Administrative Region (SAR) continues to benefit from China's rapid economic expansion. And while the infrastructure in Mainland cities is improving steadily, Hong Kong's transport links, business services and rule of law make it a popular beachhead for multinationals operating in China. That role has sparked increases in the price of commercial real estate and in residential rents. "The rent for a flat suitable for an expatriate family of four can easily top HK$80,000 ($10,300; £6,400) per month," notes Diana Lilauwala, an estate agent specialising in expat rentals.

But it's not only expatriates who are driving Hong Kong's residential property market. In the first half of 2010, Mainland residents reportedly bought one-third of the new homes sold in the SAR. These properties are purchased as investments; as an alternative to a hotel room during shopping or business trips; and, until the rules governing the Capital Investment Entrant Scheme were changed last month, as a way to obtain residency in the SAR. Expensive "trophy" homes are popular with Mainland buyers, and concerns that foreigners are pricing Hong Kong people out of the market are prompting demands for government intervention.

Despite its reputation as one of the world's freest economies, the Hong Kong government plays a large role in the SAR's real estate market. About half the population lives in government-owned or -subsidised housing and — with the exception of the ground under St John's Cathedral — all land in Hong Kong is owned by the government and made available to users through long-term leases. This ownership structure lets the government expand or restrict the availability of land to meet changing conditions. However, this is a blunt policy tool: It takes years for homes to be built on newly released land, by which time an overheated market can become depressed.

Government land policies and high prices have concentrated power in the hands of a few large developers. Controlled by some of Hong Kong's most prominent families, Cheung Kong, Henderson Land, New World Development and Sun Hung Kai Properties time their land purchases and home sales for maximum profitability, contributing to market volatility.

In addition, Hong Kong cannot calm or stimulate the property market by raising or lowering interest rates. As a result of the currency board system through which the Hong Kong dollar is pegged to the United States dollar, the SAR's interest rates are effectively set in Washington. However, the Hong Kong government can provide guidance on lending policy. In August 2010, the Hong Kong Monetary Authority reduced the maximum loan-to-value ratio for mortgages on residential properties valued over HK$12 million from 70 per cent to 60 per cent. To date, the authority's decision has not dampened buyers' enthusiasm.

The government also faces conflicting demands from first-time buyers, who want affordable flats, and existing home owners, who want steadily rising prices. Until 2003, the government built and sold subsidised flats for low-income families through the Home Ownership Scheme (HOS). The recent spike in property prices has sparked calls for the construction of new HOS flats, which the government has resisted. In his October 13 policy address, Hong Kong's Chief Executive, Donald Tsang, announced plans to build 5,000 small- and medium-sized flats under a new programme, called My Home Purchase Plan. Under the plan, tenants will receive a subsidy equal to half the rent that they have paid, which they can use as a down payment on a flat. A senior government official, who asked not to be named, said the new scheme was launched because, "We knew we needed to do something — today — to help people." The first 1,000 flats to be built under the programme will be completed by 2014.

Some observers worry that Hong Kong is in the midst of a property bubble that will collapse when interest rates begin rising. But this view is not universal. "Despite property prices in Hong Kong rising significantly from the trough in 1998, we expect mass residential prices to increase by 11 per cent in 2011," says Buggle Lau, chief analyst at Midland Realty.

Christopher Dillon is the author of *Landed: The expatriate's guide to buying and renovating property in Hong Kong* (www.landedbook.com).