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**ANALYSIS OF HONG KONG'S  
REAL ESTATE PRICES IN 2018**

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# **Analysis of Hong Kong's Real Estate Prices in 2018**

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## **Resumen**

Este artículo tiene como objetivo analizar los precios del mercado inmobiliario de Hong Kong en 2018 teniendo en cuenta los principales problemas urbanísticos. Hong Kong tiene que afrontar grandes problemas respecto al precio inmobiliario que ha llegado a sus máximos niveles. Según el Índice Centa-City, los precios del mercado inmobiliario han aumentado casi un 300 por ciento entre 2003 y 2018. En este artículo se analizan los tres factores que predicen una burbuja inmobiliaria: la falta de terreno para construir, las insuficientes políticas gubernamentales y la constante globalización de los mercados financieros.

## **Palabras clave**

Hong Kong, Precios del mercado inmobiliario, Planificación urbanística, Urbanismo, Terrenos en construcción, Burbuja inmobiliaria, Centa-City Index, Políticas gubernamentales.

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## **Abstract**

The goal of this paper is to study the situation of Hong Kong's real estate prices in 2018, in connection with the major problems in the Urbanism of Hong Kong. Hong Kong has big issues regarding property prices, since they have never been higher. According to the Centa-City Index, real estate prices in Hong Kong have increased almost by 300 percent from 2003 to 2018. For me, there are three main factors that foretell a property bubble: the lack of building land, inadequate government policies, and the constant globalization of the financial markets.

## **Keywords**

Hong Kong, Real Estate Prices, Town Planning, Urbanism, Building Land, Property bubble, Zoning Laws, Centa-City Index, Government Policies.

# ANALYSIS OF HONG KONG'S REAL ESTATE PRICES IN 2018

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## **Introduction**

Hong Kong has a population of 7,486,400 inhabitants at the end of 2018, a population that lives in an area of land relatively small, which is even smaller due to the fact that more than a 40% of Hong Kong's land is officially considered as land not for building –due to several reasons, being the environmental one of the most important.

There is a potential property bubble considering the three-fold increase in property prices in the period 2003-2018. The UBS Global Real Estate Bubble Index Report (2017) stated that Hong Kong might be facing another financial bubble as current housing prices are seen as “fundamentally unjustified”, and benchmark metrics such as price-to-income and price-to-rent ratios have reached all-time highs.

In an era in which a strong academic debate is being held regarding the need or not for compact cities,<sup>1</sup> the study of the

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<sup>1</sup> On the one hand, a few authors have criticized the need for compact cities, defending the phenomenon known as sprawl –a low-density, automobile-oriented, usually suburban development–. Bruegmann stated that sprawl is “a natural result of affluence that occurs in all urbanized societies” (Bruegmann, 2005:18). Thus, he defends the *status quo* of most American suburbs –as his study is mainly focused on the United States– because of several reasons, namely: a) Sprawl is what people desire in the absence of government coercion; b)

Urbanism of Hong Kong has brought us to select three major problems because we consider that are the most relevant:

- Lack of building land
- Inadequate Government policies
- Property bubble in Hong Kong's real estate market

This paper will analyse all these issues, trying to offer possible solution to them.

### **Lack of building land**

Hong Kong has 7,486,400 residents<sup>2</sup> crammed into a relatively small territory of 1,104 km<sup>2</sup> total land area.<sup>3</sup> However, out of these 1,104 km<sup>2</sup>, a 38-odd % has been designated as country parks and special areas that provide statutory protection for the habitats, meaning that it is impossible to build in these lands. Therefore, as a starting, there is only a 60% of the total land available.

Sprawl is the result of free market at work; c) the harmful side effects of sprawl are overrated by critics of the *status quo* and, d) sprawl cannot be limited without government regulations that will artificially affect the house supply and thus raise housing prices. On the other hand, many authors have criticized sprawl and they are in favour of a compact cities' model, as the case of scholars adhered to the American New Urbanism doctrine. For these reserachres –for example, Duany, Plater-Zyberk and Speck (2001)–, sprawl is a dangerous phenomenon that must be reverted.

<sup>2</sup> Census and Statistics Department. The Government of the Hong Kong Special Administrative Region (2018). <<https://www.censtatd.gov.hk/hkstat/sub/so20.jsp>>.

<sup>3</sup> Lands Department of Hong Kong (2013). <[http://www.landsd.gov.hk/mapping/en/publications/hk\\_geographic\\_data\\_sheet.pdf](http://www.landsd.gov.hk/mapping/en/publications/hk_geographic_data_sheet.pdf)>

Besides, still according with the data provided by the Lands Department, only a 40% of Hong Kong's total land is flat. It is possible to build in not flat land –many neighbourhoods in Hong Kong Island, for example, are built in hilly lands–, but the fact of such a huge proportion of land not being flat makes it more difficult to carry on the process of land development.

In this sense, the Policy Address by the Government of Hong Kong (2015)<sup>4</sup> clearly identified and explained this problem the next way:

“72. What Hong Kong lacks is not land, but land that is developable. The difference lies in the need for land planning and development. The process of land planning and development takes time. (...) The Government scaled back the speed and scope of our planning and development of land, and did not foresee the huge demand for developable land as a result of the eventual economic recovery. A substantial amount of land was zoned for non-development uses such as country parks to improve the environment. We also lowered the development intensity of land newly planned for development. These are causes of the serious shortage of housing supply that we have been facing in recent years”.

Before explaining the lack of land, the Policy Address focuses on explaining the problems that this issue causes to many Hongkongers, namely:

“70. There is a serious mismatch between the supply of land and the needs of our society. The short supply of land and housing has led to rising property prices and rents.

71. High property prices and rents have prevented many young people from forming a family or starting their own business. This has also resulted in cramped living space for

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<sup>4</sup> 2015 Policy Address, Government of Hong Kong:  
<<http://www.policyaddress.gov.hk/2015/eng/p70.html>>

society as a whole and insufficient space for social welfare facilities such as kindergartens, elderly homes and residential care homes for persons with disabilities. We have an ever longer PRH waiting list, and an increasing number of people have seen their living environment deteriorate. Some have no alternative but to live in subdivided units in industrial buildings. Small and medium-sized enterprises face greater operating difficulties while overseas investors are disheartened by the difficulty in establishing a business base in Hong Kong. The root of many social and economic problems in Hong Kong lies in the shortage of land for development”.

The Government recognises that the price of housing in Hong Kong is so high because of the lack of building land, and also this lack of building land produces a shortage in housing supply, as well as high prices. This fact is the root of many social problems in Hong Kong.

The Centa-City Index (CCI),<sup>5</sup> compiled by the real estate agency Centaline and the City University of Hong Kong is

“a monthly index based on all transactions records as registered with the Land Registry to reflect property price movements in the previous 1-2 months. As land registration takes time, any index based on the Land Registry's sale and purchase data inevitably could not provide the most up-to-date information. On the other hand, index based on the current contract price data is a good indicator of the most recent price movements in property agent market share, thus the Centaline transaction data are able to reflect the market situation”.

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<sup>5</sup> Centa-City Index: < [http://www1.centadata.com/cci/cci\\_e.htm](http://www1.centadata.com/cci/cci_e.htm)>

This index is closely related to the problem analyzed in this paper, the lack of building land that causes that the prices of developable and developed land in Hong Kong become much more expensive. The Centa-City Index precisely shows the current situation and also the past evolution of these prices.

Nevertheless, it is necessary to make some remarks about the Index. July 1997 is used as the base period of the index, and this index, in the base period, equals 100. Besides, a property price index can be calculated by aggregating the prices of the constituent estates using the formula:

Figure 1. Formula of Centa-City Index (CCI) for a month

$$= \frac{\text{Total market value of the constituent estates in the month}}{\text{Total market value of the constituent estates in the previous month}} \times \text{CCI for the previous month}$$

Source: Centada, [http://www1.centadata.com/ci/notes\\_e.htm](http://www1.centadata.com/ci/notes_e.htm)

It is important to remark that an estate is only considered for inclusion as constituent estate if:

- it has a high transaction value
- it has a large number of transactions
- it has been in the market for at least 12 months after occupancy
- it is representative of the region.

As Chim and Wong state,

“The gap between housing prices and construction costs in Hong Kong was relatively narrow until the late 1980s. Hong Kong's economy boomed after China began to open up after



1979. Housing prices rose dramatically, because supply could not respond in the immediate short term. As a result, the gap between housing and construction prices began to widen” (Chim and Wong, 2015:154).

Figure 2. Centa-City Index CCI at 2018/10/26.



Source: Centadata (Centa-City Index) (2018).

The evolution of real estate prices in Hong Kong shows that average home sale prices have skyrocketed over 300 percent since 2003, even if, in 2016, prices dropped a little bit compared to 2015. Even though, prices remain very high indeed. The drop that took place in 2016 was not, however, dramatic, as analysts like Nishizawa (2016), point to several reasons why a crash is unlikely. After mid-February 2016, when they fell to the lowest level in 14 years, secondary transactions and major housing estates rebounded five-fold to a nine-month high in the week ended March 2016. Prices actually kept increasing after 2016, being much higher in 2017 compared to 2016, and in 2018 compared to 2017.

The lack of building land has impact to housing prices in Hong Kong, and so there is an affordability problem very complicated to solve: if housing prices are so high because of

the existing lack of building land, many citizens will not be able to afford to buy/rent a house. Nevertheless, Hong Kong has a large system of public housing, but it is not and will not be enough to cover all the needs of the citizens.

“Home seekers are facing increasing difficulty in the affordability of and accessibility to an owner-occupied flat owing to a frenetic (...) price increase in the past decade [s]” (Liu, 1994: i).

Factors affecting affordability are property price, tenure, prevailing interest rate, wealth of purchasers, household income, tax policy and state regulatory measures (Darke and Darke, 1988). Of all these factors, the first one is affected by the lack of building land. The affordability of owner-occupiers is showed by the Price-Income Ratio (PIR) though, sometimes, mortgage-repayment ratio is also used. This lack of affordability has important social consequences in Hong Kong, especially among young people.

Another index to take into consideration is the Housing Affordability Index,<sup>6</sup> which measures whether or not a typical family earns enough income to qualify for a mortgage loan on an average home based on the most recent price and income data.

Figure 3 shows how housing prices increased enormously from 2003 to 2011 –and they continued increasing until 2015–, but the affordability index has not increased in the same way that prices. In other words, houses are less affordable for Hong Kong citizens than in the past.

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<sup>6</sup> In a more technical way, the Affordability Index is the proportion of a household's income on mortgage outgoing assuming the household on the median income level who has bought a 400sq feet flat at average house price with a 20 years mortgage at the prevailing mortgage rate.

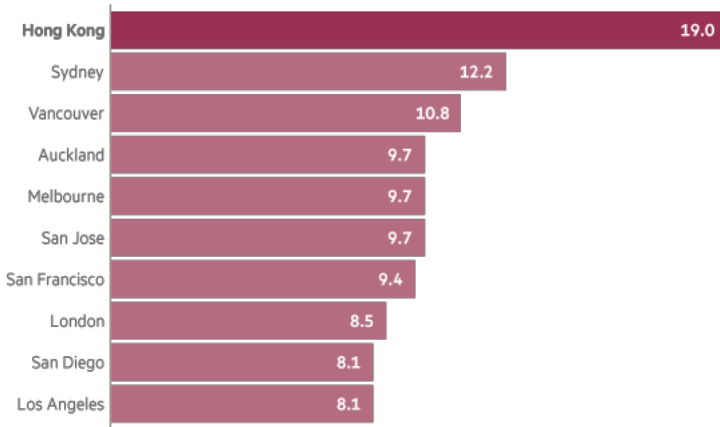
Figure 3. House Price and Affordability in Hong Kong. 1994-2011



Source: Yip (2013: 328), after data from Centaline

The organisation Demographia, in his 12th Annual International Housing Affordability Survey, 2016, stated that Hong Kong is the world's least affordable city, being the city's median multiple nearly four times the threshold at which prices are considered "severely unaffordable". Moreover, Hong Kong's Median Multiple of 19.0 was the highest recorded – least affordable– in the 12 years of the Demographia International Housing Affordability Survey. In accordance with Figure 4 by far, Hong Kong is the world's least affordable city indeed:

Figure 4. World's Least Affordable Cities



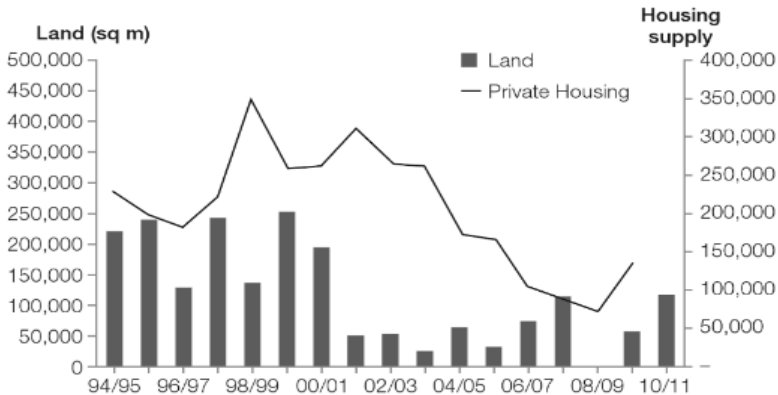
Source: Demographia (2016).

Besides, the Figure 5 shows a clear shortage in housing supply –which also affects the private rental market– when compared to the available land.

“The private rental sector, which has been in decline since the 1970s, has stabilised in the last decade and accommodates around 14% to 15% of the households in Hong Kong. It has also been transformed, from a tenure for the poorest before the 1980s, to a polarised tenure which lodges both the high pay expatriates in multi-national companies at the high end of the market, and single people and poor households (and students as well) at the other extreme end” (Yip, 2013: 331).

In any case, the main consequence is precisely the fact that there is a clear shortage in housing supply in Hong Kong; shortage which, far from decreasing, is currently increasing.

Figure 5. Land and Private Housing Supply, 1994-2011.



Source: Yip (2013: 331), after the data provided by the Census and Statistics Department of Hong Kong.

Being this the case, that the lack of building land provokes a clear increase of the land prices which reduces the housing affordability for most citizens, there is another topic –related to the lack and building land as well as to land reclamation– to take into account: where will Hong Kong grow to? This is an important question, Hong Kong needs to grow, but to grow where?

Hong Kong's total land area is 1,104 km<sup>2</sup>, however, a 38-odd% of it has been designated as country parks and special areas which provide statutory protection for the habitats, meaning that it is impossible to build in these lands. Besides, of this 60% of the land which is theoretically available, most of it is not flat, being thus more complicated to build in it.

Being this the case, Hong Kong has almost no land to grow. One option for the Government would be to continue reclaiming land from the sea, but most major land reclamation projects are currently stopped, except for the projects in the Outlying Islands. Also environmental concerns have been an accompaniment to Hong Kong reclamation projects. Many environmentalist associations criticise these projects, but some authors consider that it is necessary to find a balance between protecting the environment and urban development in Hong Kong.

Even so, an option to grow in Hong Kong Island would be to reclaim land towards the west, to the west of Kennedy Town, even if politicians, because of the popular pressure, do not seem to be willing to do so.

There is a small green belt around some Hong Kong cities. The green belt areas are not yet classified as country park and allows new cities to be built there (Liu, 2014). However, even if new towns were created in all the existing green belts in Hong Kong, this would not be enough to meet all the needs for housing supply.

Besides, there is a problem which must be added: the price of public transportation in Hong Kong. Most of citizens who work downtown are reluctant to move in new towns created in new belts, as the costs of transportation are too high when compared to their salaries.

There is a certain margin to grow within New Development Areas in Rural Towns mainly in the northern part of Hong Kong, but, it will not be enough, having a net inflow of population bigger than the outflow. If the Government of Hong Kong cannot really touch mountains, most reclamation projects are stopped. It becomes difficult to forecast what will happen.

The case of Hong Kong is different nowadays than, for example, Macau. The Government in Macau is very active

reclaiming new land. Actually most forecasts establish that more than a 40% of new land will be gained in the next 10-20 years. But in Hong Kong it is not possible, as it seems that the days in which reclaiming new land was the answer to the lack of building land are gone.

Hong Kong's case is often compared with Singapore, even if this comparison is not actually fair. Although Hong Kong's land is bigger than Singapore's, in Singapore more than 60% of the land is flat, while in Hong Kong, it is just a 40%.

Some experts, as a possible solution, suggest a reutilization of existing spaces. In this sense, Paul Zimmerman (2016) states that the so-called "brownfield" sites are the solution:

"The key is to use the space that we do have in a more efficient way. A lot of the industrial properties in the New Territories, for example, are totally space-inefficient" (Zimmermann, 2016).

Thus, a possible solution could be to turn some of the not efficient semi abandoned industrial properties in the New Territories into actual building land. Nevertheless, this is, once again, a temporary solution.

In this sense, the document *Long Term Housing Strategy: Implementation Milestones* (2014)<sup>7</sup> provides some clues on these issues when talking about measures to increase housing land supply. The Annex B of the *Implementation Milestones* document states that on the one hand, the Government need to meet the targets for public housing, as it is a social need, but, on the other hand, any development project will imply a

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<sup>7</sup> Transport and Housing Bureau, the Government of Hong Kong: "Long Term Housing Strategy: Implementation Milestones as at December 2014" <<http://www.thb.gov.hk/eng/policy/housing/policy/lths/ImplementationMilestones201412.pdf>>

consequence on the community as a whole: “there is simply no magic solution that can increase land supply without impacting on the local community”. In other words, if the Government decided to reclaim land massively again, it would have a clear and immediate consequence on the environment, for example, but nevertheless more land is needed to meet the housing need of Hong Kong inhabitants.

For instance, a 1% of the Green Belt areas must be developed according to this document. Otherwise, the Government has absolutely no way of being able to provide the necessary housing. So, the situation is actually really complicated, and a way out, any way out, is not easy to be determined.

### **The existence of a property bubble in Hong Kong**

A property or real estate bubble may be defined as

“A temporary situation where asset prices become elevated beyond any realistic fundamental valuations because the general public believes current pricing is justified by probable future price increases” (Roberts, 2008:1).

The problem is, if this belief is sufficiently important to make a large number of people to purchase the asset –in this case, real estate assets–, then prices will continue to rise. Thus, more people will be convinced to buy. This gives birth to a self-sustaining reaction, until the pool of buyers is exhausted and the volume of buying declines.

Consequently, prices will stop rising and they will even fall, as the buyers no longer believe that future prices will increase. And, at the end, it becomes possible that this bubble bursts:

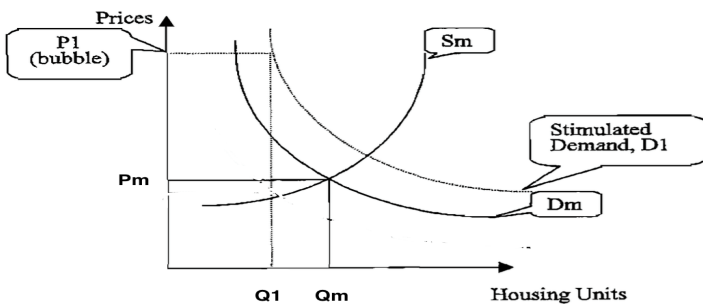
“Once prices begin to fall, the fear of being priced ‘out’ forever changes to a fear of being priced ‘in’ forever. A buyer who overpaid and over-borrowed will be in a circumstance where they owe more on their mortgage than



the property is worth on the open market. They cannot sell because they cannot pay off the mortgage. They become trapped in their homes until prices increase enough to allow a breakeven sale. This puts the conditions in place to reverse the cycle and causes prices to drop precipitously” (Roberts, 2008: 3).

Real estate bubbles normally occur following a land boom. In order to identify bubbles before they burst, economists have developed several financial ratios and economic indicators that are used to evaluate whether homes in an area are fairly valued. If current levels are compared to previous levels that have been unsustainable in the past –i.e. led to crashes, for example–, a guess can be made as to whether a given real estate market is experiencing a bubble. In this sense, these indicators describe two related aspects of a housing bubble: the valuation component, which measures how expensive houses are compared to what most people can afford, and the debt component, which measures how indebted households become in buying them for home or profit, and also how much exposure the banks accumulate by lending for them.

Figure 6: Causes of the Property Price Bubble in Hong Kong



Source: Lai (2016).

Among the authors who claim that there is a real estate bubble in Hong Kong, Eugene Lai (2016) considers that there exists a property bubble in Hong Kong which has been induced due to an increasing demand and an insufficient supply for housing (Figure 6).

Lai (2016) makes reference to a report by the Real Estate Research of the bank UBS in which it was stated that Hong Kong might be facing another financial bubble as current housing prices are seen as “fundamentally unjustified”, meaning this that benchmark metrics such as the previously quoted price-to-income ratio and price-to-rent ratios have reached all-time highs.

In fact, Lai (2016) quotes four reasons that, in his opinion, explain why there is a property bubble in Hong Kong:

1. The lack of building land. This is indeed a big problem in Hong Kong's real estate system. There is a mismatch between the demand of the society and the supply of land.
2. Low percentage share of GDP of the construction industry and real estate services. Lai points out that, comparing Hong Kong and similar economies such as Singapore, Hong Kong has an average ratio of approximately 8% while that of Singapore is approximately 14% annually. Such little amounts of investment would lower gross living space of Hong Kong, resulting in a mismatch between gross living space and the Hong Kong population.

“the living space per capita recorded in 2015 is approximately 161 square feet while that of Singapore is approximately 323 square feet. If the average living space in Hong Kong were to increase to the level same as Singapore, it is believed that the property price would undoubtedly decrease substantially” (Lai, 2016).

3. Government policies. These last few years, “the Government has tried to implement different policies to

curb property prices by trying to eliminate speculators from the market” (Lai, 2016). An example of this policy is the Double Stamp Duty, which targets non-first-time buyers, and which is the doubling of stamp duty in property purchase valued at HK\$2 million or above to 8.5% from previous 4.25%, as well as Buyer’s Stamp Duty (BSD), which is a 15% tax levied specifically on companies and non-permanent residents who buy properties in the city.

“even if it is true that these policies have reduced the sale volume by eliminating speculators from the market, it is also true that there might be a psychological effect on the supply side, as policies might affect the property developer’s perspective on the projected weakening demand and prospects of the market due to increase in transaction costs, thus the willingness for producers to supply more properties would decrease. Therefore, in the long run, the supply of properties decreases, which will undoubtedly push up the property price” (Lai, 2016).

4. Globalised financial markets. In the past, homebuyers were mainly local people, while currently foreign investors are entering the Hong Kong real estate market. Being this the case, the continuous capital inflow into Hong Kong has kept home prices high and made home ownership increasingly unaffordable.

However, even if there seems to be property bubble in Hong Kong, we can consider that it is extremely unlikely that it bursts. There is a property bubble in Hong Kong in the sense that real estate prices are extremely elevated beyond objective justifications. Consequently, at first sight, it would appear that Hong Kong’s –and Mainland China’s– current situation is similar to that existing in Spain before the outburst of the financial crisis in 2008. However, the situation in Hong Kong and China is different from that in Spain before 2008 because this bubble will not burst. And the bubble will not burst because, even if property prices are extremely high, there is

liquidity in both systems. Liquidity is beyond any doubt the main key in this point: there will be no burst of the bubble in Hong Kong and China, but corrections of the prices, corrections like the ones that took place in Shenzhen the last two years and like the one that is taking place in 2016 in Hong Kong. In 2016, prices have dropped a little bit when compared to 2015 (around a 12%). But this decrease of the prices is not the burst of the bubble, just a simple cyclic correction.

Thus, what prevents Hong Kong and China's property bubble from exploding? Liquidity. And this liquidity exists because there are billionaires, both in China and Hong Kong, with enough money to hold the system. In other words, even if from a structural point of view the situation of the property bubble in Mainland China and Hong Kong right now is not very different from the situation existing in Spain before 2008, the truth is that in Hong Kong and China this bubble will not explode because there are plenty of billionaires with enough liquidity to hold the system and prevent it from exploding, from bursting.

## **Conclusions**

The system of Town Planning in Hong Kong, which is the result of a socialist-like land tenure system within the world's most capitalistic economy –and is also the result of a very small administration which leaves a big margin for a private negotiation with developers and the rest of stakeholders–, as well as the geographic nature of Hong Kong, carries a series of problems, which we have analysed in our paper.

“Hong Kong [has] a unique position of being internationally acclaimed as one of the best, if not the very best example of a functioning capitalist economy which ironically is founded on what is fundamentally a socialist land tenure system” (Nissim, 2011: preface).

Hong Kong has big issues regarding property prices: They have never been higher. According to the Centa-City Index, real estate prices in Hong Kong have increased almost by 300 percent from 2003 to 2018.

There is undoubtedly a potential property bubble considering the three-fold increase in property prices in the period 2003-18. The *UBS Global Real Estate Bubble Index Report* (2017) stated that Hong Kong might be facing another financial bubble as current housing prices are seen as “fundamentally unjustified”, that benchmark metrics such as the previously quoted price-to-income and price-to-rent ratios have reached all-time highs.

In sum there are three main factors that foretell a property bubble: the lack of building land, inadequate government policies, and the globalization of the financial markets.

Regarding the lack of building land, there is a big mismatch between the demands of society and the supply of land. Hong Kong has more than 7.4 million residents crammed into a relatively small land mass of 1,104 square kilometers. The problem resides in the fact that almost 40 percent of the total land has been designated as country parks and special areas, which prohibits any construction on those areas. Consequently, construction is permitted only on 60 percent of Hong Kong’s land area.

This issue could be solved in several ways, but none of them seems to please everyone. It is critical for the long-term well-being of Hong Kong that solutions –even partial solutions– are found to make land available for housing. The government could find a way to stop land hoarding by the developers, a way to reclaim more land, or a way to reduce the size of some country parks.

In the last few years the government has tried to implement different policies to curb property prices by trying to eliminate speculators from the market. An example of this policy is the

Double Stamp Duty. Even if these policies have reduced the sale volume by eliminating speculators from the market, it is also true that there might be a psychological effect on the supply side, as policies might affect the property developers' perspective on the projected weakening demand and prospects of the market due to increase in transaction costs, thus the willingness for producers to supply more properties would decrease. Therefore, in the long run, the supply of properties decreases, which will undoubtedly push up the property price.

As to the globalization of financial markets, homebuyers in the past were mainly local people, while currently investors from outside the city are entering the Hong Kong real estate market. This being the case, the continuous capital inflow into Hong Kong has kept home prices high and made homeownership increasingly unaffordable.

So will this bubble burst any time soon? Our answer is no. Hong Kong's property bubble will not burst, at least not in the near future, unless it is triggered by some unforeseen disaster. Property crashes in Hong Kong have occurred only during the SARS (Severe Acute Respiratory Syndrome) outbreak in 2003 and the global financial crisis in 2008. It was not precipitated by an overheated property market. Even if property prices are extremely high, there is liquidity in Hong Kong. Liquidity is the main safety valve obviating a property bubble burst either in Hong Kong or on the Chinese mainland. Moreover, the bubble will not burst because developers will keep on raising prices while finding ways to attract people to buy. In this case, what goes up may not necessarily come down.

To sum up, there is no magic bullet to overcome Hong Kong's property issues in one go. It will require a multipronged approach because the community hasn't been able to reach a consensus. The opposing sectors would have to compromise by adopting land reclamation, using the fringes of country parks, converting industrial land and buildings for residential use,

even requesting the central government to apportion land near the border for our use. It is time for everyone to think outside the box and think creatively for solutions.

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