RESIDENTIAL RESEARCH

Knight Frank

ASIA-PACIFIC RESIDENTIAL REVIEW

December 2012

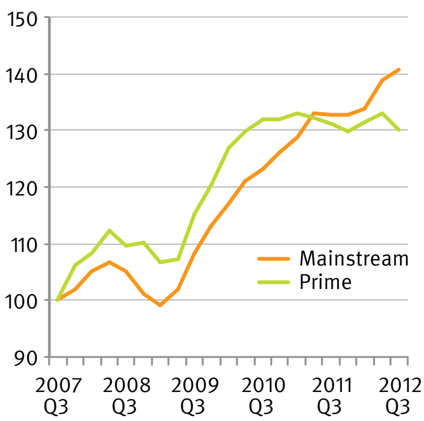
INTRODUCTION

MAINSTREAM MARKETS OUTPERFORM PRIME IN ASIA PACIFIC

"While Asia is undergoing huge economic changes, and we see prices in the mainstream markets reflect this, the more internationalised prime markets have not always benefited as much as we may have expected."

Nicholas Holt
Research Director,
Asia Pacific

Figure 1
Mainstream vs. prime market performance in Asia (Q3 2007 = 100)



Source: Knight Frank Research

Push and pull factors combine to encourage a number of prime Asian buyers to look abroad for luxury residential property. Knight Frank's prime forecasts show that this is likely to continue in 2013. Nicholas Holt looks into the numbers and provides the narrative.

When analysing 2012 Asia Pacific residential market data, one startling trend that jumps out is the fact that prime markets have seemingly underperformed when compared with mainstream markets across much of the region (see Figure 1). In this edition of the Asia-Pacific Residential Review, we will explore some of the explanations for this, and provide an in-depth analysis of the historic price performance of the region's prime and mainstream markets. Some of our conclusions will in turn provide a platform for our 2013 prime forecasts, a comprehensive regional complement to Knight Frank's Prime Global Forecast.

This paper will provide a roundup of the latest trends affecting mainstream markets (see pg. 3), followed by an in-depth analysis of how the mainstream and prime markets (i.e. the top 5% of the market) have fared against each other (see pg. 4), concluding with our prime forecasts for 2013 (see pg. 5).

One of the key narratives that emerges, is that while prices rebounded strongly in 2009 after the global financial crisis, the increasing intervention of policymakers in some countries has "pushed" some buyers out of the prime residential markets. At the same time, given the favourable investment and lifestyle opportunities abroad, some prime buyers have been "pulled" towards prime residential markets outside of their domestic markets.

One thing is certain, and that is the demand and supply drivers at the top end of the market are different to the mainstream. While Asia is undergoing huge economic changes, and we see prices in the mainstream markets reflect this, the more internationalised prime markets have not always benefited as much as we may have expected.

There are of course many other narratives and explanations in each market and sub-market, and with our research teams in each country, we have identified some of the key factors that have influenced prime residential market performance to date and the risks going forward into 2013.

The biggest concern for the region's markets remain macroeconomic, with a domestic slowdown viewed as the largest threat for prime market performance in 2013. The possibility of further government intervention to reduce house price inflation in these times of low interest rates is likely to remain, posing a risk to several residential markets over the next 12 months.

If we take a slightly longer time horizon, given the huge increases in economic activity and wealth in the Asia-Pacific region, the medium term forecast for prime residential property remains unanimously positive.

ASIA-PACIFIC MAINSTREAM MARKETS IN Q3 2012 DOMINATED BY STRONG PRICE PERFORMANCE IN HONG KONG AND CHINA

Perhaps the biggest headline in the Asia-Pacific residential markets over the last quarter has been the introduction in October of a 15% stamp duty for foreign buyers of residential property in Hong Kong.

Despite the large number of cooling measures introduced over the last three years, prices have continued to soar in **Hong Kong**, nearly doubling since the beginning of 2009. The government has followed the example of Singapore, who introduced a similar stamp duty in December 2011.

Singapore itself has seen record volumes transacted in 2012, as low interest rates have continued to fuel demand despite the continuing stream of cooling measures. With the residential market a serious concern for the government, many commentators have noted that further intervention in 2013 cannot be ruled out.

Reflecting the improving sentiment in the **Chinese** economy, the country's housing markets have continued to see strong demand. The price falls in Beijing and Shanghai in the last half of 2011 now look more like a blip in the strong upward trajectory. Mainstream prices in Beijing and Shanghai have risen 12.82% over the last six months, second only to Hong Kong in the region.

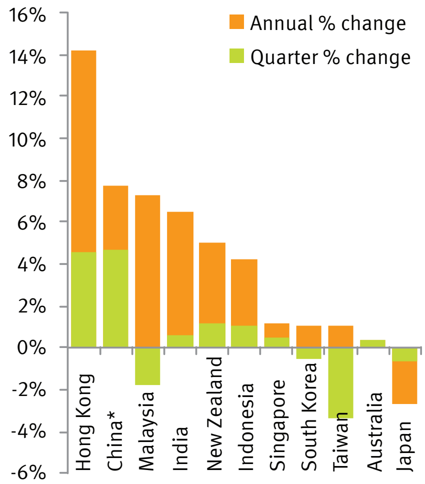
In **Malaysia**, nationwide prices slipped 1.81% in the third quarter, due to a more challenging overall market sentiment. The effects of cooling measures, and perhaps most importantly the impending General Election, has encouraged a wait-and-see attitude amongst market participants.

Further down the archipelago, **Indonesia's** house prices continued to grow strongly. The loan-to-value ratio cap of 70% which was introduced in July for properties below 70 sq m seems to have had little impact to date. Instead, the economy's robust growth is being translated into strong housing demand.

In **India**, across the 15 cities surveyed, ten saw price increases over the third quarter, while five saw price drops. Despite the relatively weaker economic performance of the Indian economy, the strong underlying fundamentals have ensured that the market as a whole remains on an upward trajectory.

Finally, in the Pacific region, **Australia's** housing markets have stabilised following price falls in 2011 and the first half of 2012. **New Zealand's** residential markets have continued to enjoy solid growth, notably in the key cities of Auckland, Wellington and Christchurch which have been buoyed by low interest rates.

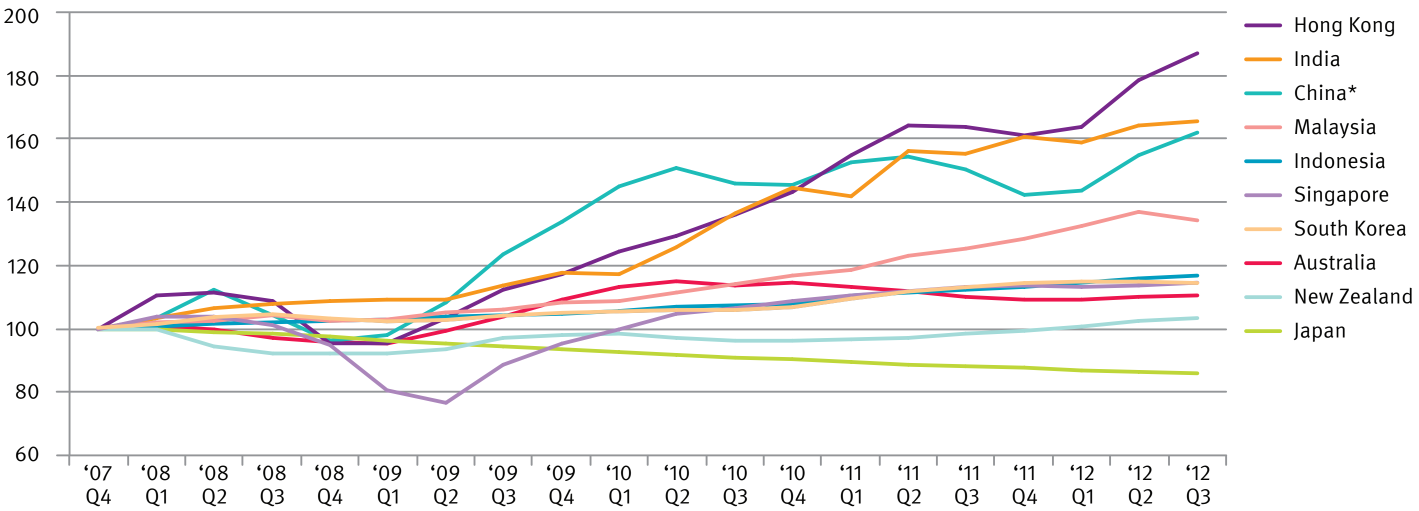
Figure 2
Global House Price Index Q3 2012



*Based on Beijing and Shanghai

Source: Knight Frank Research

Figure 3
Global House Price Index (Q4 2007 = 100)



Source: Knight Frank Research

MAINSTREAM VS. PRIME

The huge increases in incomes and wealth that we have seen across Asia have lifted residential prices significantly over the last decade. However, when analysing price performance, notably over the last couple of years, mainstream markets across Asia (excluding Japan) have outperformed the prime end of the market. This is in contrast to many other regions of the world.

Taking price performance following the collapse of Lehman Brothers in September 2008, when a number of markets saw a slight price correction, national mainstream markets have outperformed the region's prime city markets, with the exception of Jakarta (see Figure 4). We have identified three key reasons for this Asian phenomenon.

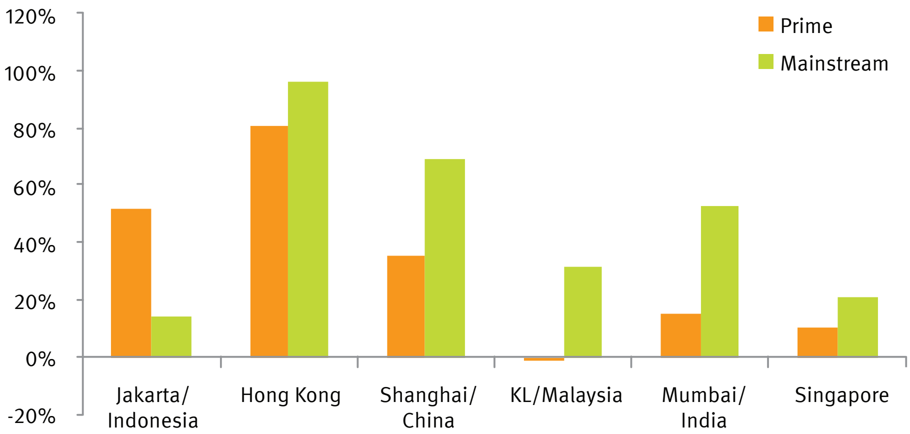
Firstly, and perhaps most importantly, although we are seeing growth in incomes across all income brackets, the absolute growth in the number of middle class, first home buyers in developing Asia is staggering (see Figure 5). It is the emergence of this property-buying class - reinforced by historic levels of urbanisation and a movement towards smaller family units - that has brought about significant new levels of demand. The reality is that even though we are seeing a large number of prime buyers emerging, this number pales in comparison to the number of new entrants into the mainstream market.

Across many of these markets, supply has found it hard to keep up with demand with planning, infrastructure and land use issues often holding up development activity. This is sometimes in contrast to the high end, where we have seen developers eager to enter the smaller and potentially more lucrative prime segment of the market.

Secondly, across much of Asia, 2012 has seen continued government interventions, aimed at mitigating the risk of asset bubbles and addressing concerns of affordability. These cooling measures have, however, dented demand for prime residential product in some markets through a range of measures; limiting financing, introducing extra taxes for foreign buyers and penalties for disposing of the property within a certain time period. Many of these measures have targeted the high end residential market (loan-to-value ratios in Hong Kong are limited to 50% for properties over HK$10 million), but more often they have been introduced to penalise multiple home owners at the expense of first time buyers, which disproportionally impacts the prime residential markets.

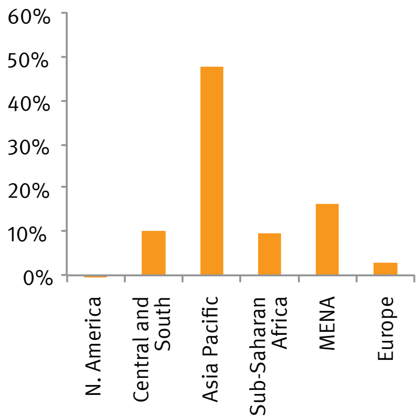
Finally, while the market has become more difficult for some buyers, the attraction of 'global' prime property markets outside their domestic arena has continued to provide incentives to move their money abroad. With an increasingly mobile, educated and well-travelled class of property owners in the Asian region, the lifestyle choice of having a second home abroad, for personal or for children's educational use is proving to be one of the key narratives for HNW Asian buyers. Purely from an investment point of view, as a diversifier away from the steamy and controlled Asian markets, it has been seen as a sensible strategy for their wealth portfolios. Domestic currencies that have strengthened against destination market currencies have also provided a currency play, which has made some purchases relatively cheaper.

Figure 4
Price growth across key Asian markets from Q4 2008



Source: Knight Frank Research

Figure 5
Projected growth in middle classes 2007-2012 by region



Source: OECD

THE PRIME ASIA PACIFIC FORECAST

As a complement to Knight Frank's Prime Global Forecast, we have carried out in-depth surveys in respect to an additional six Asian prime city markets, to provide a comprehensive picture of the regional outlook for prime markets in 2013. Of all the markets we monitor, taking into account past year performance, supply and demand dynamics and potential risks, our forecasts predict that 2013 will look fairly similar to 2012. We forecast modest price growth across most markets, with a couple of significant exceptions.

Jakarta and Bangkok tipped to be top Asian performers through 2013

Our forecasts show that we are more bullish in 2013 about the markets that have solid fundamentals and little or no cooling measures. Jakarta and Bangkok notably, are two markets that are well positioned to benefit from strong economic growth and a growing affluent and aspirational property owning class. Both of these markets have been the star performers over the past year, and we expect this to continue.

Safe haven and lifestyle destinations of Singapore and Hong Kong to remain stable

Over the last 12 months, Singapore and Hong Kong, considered the Asian safe haven and lifestyle markets, have erected protectionist measures that have and will continue to curb demand at the prime end of the market. In Singapore, while robust demand remains for prime landed property or good class bungalows (GCB); demand for luxury condominiums has proved weaker. Despite this, we expect the attractiveness of Singapore, with its transparent legal systems and stable political environment, will ensure that prices do not fall. Meanwhile in Hong Kong, where the new stamp duties for foreign buyers are likely to curtail some mainland Chinese demand that makes up a significant proportion of buyers, we expect prices to rise, but at a slower pace than the previous 12 months.

Differing drivers of demand to bring about contrasting performance in Beijing and Shanghai

In China, we are more bullish about the stronger domestic "establishment"

Figure 6
Prime city residential price performance and forecasts

City	% change to Q3 '12	Forecast '13
1. Jakarta	↑ >20%	↑ >20%
2. Bangkok	↑ >20%	↑ 10%-20%
3. Beijing	↓ <5%	↑ 5%-10%
4. Hong Kong	↑ 5%-10%	↑ <5%
5. Mumbai	↑ <5%	↑ <5%
6. Sydney	↓ <5%	↑ <5%
7. Hanoi	↓ 10%-20%	→ no change
8. Kuala Lumpur	↓ <5%	→ no change
9. Singapore	↑ <5%	→ no change
10. Tokyo	↑ 5%-10%	→ no change
11. Shanghai	↓ <5%	↓ <5%
12. Ho Chi Minh City	↓ 10%-20%	↓ 5-10%

Source: Knight Frank Research

market of Beijing than the Shanghai market, which is more linked to the business performance of the financial capital of the country. While the Shanghai market is probably more sensitive to the economic and financial markets, Beijing, which will see the opening of a number of new metro lines in 2013, is expected to see strong price performance over the next 12 months.

Mumbai's lack of liquidity to keep prices steady

Mumbai, whose prime residential market is closely correlated to the economic performance of the country, has seen prices stagnate over the last year. With uncertainty over the strength of the economy and an election on the horizon in 2014, we forecast prices to edge up slightly in 2013.

Tokyo prices to remain stagnant

At the top end of the market, prices are expected to remain relatively flat as weak demand is met with little new supply in Tokyo. In general, prices have been on a gentle downward trajectory as land prices continue to lose value and the economy struggles to regain the high levels of growth of the past.

Vietnam continues its downward trajectory amid economic uncertainty

Vietnam is passing through an extremely difficult economic period and this is being reflected in the price falls in both Hanoi and Ho Chi Minh City during 2012. With ongoing macro-economic issues, we expect another tough year in 2013, which will continue to impact the prime end of the housing market, although the feeling is that most of the price corrections have already taken place.

Sydney still an attractive lifestyle and investment choice

Finally, Sydney, which is closed off to foreign buyers except in the primary market, is expected to recover after a decrease in the number of motivated vendors, with a stable market forecast for 2013. Sydney has and will continue to be a target for Asian buyers, and could benefit if the Australian dollar weakens against key Asian currencies in 2013.

MEASURING RISK

While the forecasts we have presented represent what we believe to be the most likely outcome for 2013, there remains a number of derailing factors which have the potential to knock our forecasts off course.

With much uncertainty in the world economy, it is no surprise that both global and domestic economic factors remain the biggest risk to property prices in Asia Pacific in 2013.

China's economic performance and the possibility of a significant slowdown is perhaps one of the most

Figure 7
Risk analysis

Risk	Ranking: Asia Pacific	Ranking: Global	Downside scenario and impact
A slowing domestic economy	1 (Highest)	3	The potential for a domestic slowdown, with the ensuing negative impact on employment and earnings growth, would have a substantial direct and domestic impact on housing markets, although the main effect would be felt in the mainstream rather than prime markets.
A slowing global economy	2	1	The global economy has essentially stalled since the second quarter of 2012. Consumers, businesses and investors are awaiting clear global signals as to how key risks play out, from the US's fiscal cliff to the Eurozone debt crisis. A weakening global economy would limit economy wealth creation and dampen confidence. The pull of 'safe-haven' investments would lessen the impact in some markets.
High inflation & low household income growth	3	7	High inflation in parts of Asia has already pushed interest rates higher. This, together with lower incomes would have the effect of & low household stifling demand but it would be more of a concern for mainstream than prime markets which are less exposed to credit availability.
Political/security issues	4	6	Those cities with a high degree of transparency, a strong legal system and relative political stability frequently see demand strengthen security at times of geo-political risk around the globe.
Government cooling measures	5	2	The efforts on the part of mainly Asian governments to improve domestic affordability and avert a housing bubble have become cooling increasingly wide-ranging and targeted at high-end properties. Regulatory measures such as higher stamp duty rates in Singapore have already had a direct impact on the number of foreign buyers, a similar trend may now be seen in Hong Kong given its 15% Stamp Duty rate for foreign buyers.
Eurozone crisis	6	4	If the Eurozone were to collapse all bets would be off and the global economy would enter a period of unchartered territory. Bank crisis lending would be severely restricted and volatility would return to the world's financial markets would return. But some investors may view the tangible asset of luxury bricks and mortar as safe an investment as any at a time of immense turbulence.
Interest rate rises	7 (Lowest)	6	With interest rates in much of Asia at historical lows, this availability of credit has helped push prime prices higher. Rate rises could dampen demand to some extent.

Source: Knight Frank Research

Figure 8
Government Intervention
Which cooling measures pose the greatest risk to prime residential markets?

Asia	Global	
1 (Highest)	2	Restrictions on multiple ownership
2	1	Shrinking mortgage availability
3	5	Stamp Duty increases
4	4	Large-scale housebuilding programmes
5 (Lowest)	3	Changes to CGT rules

Source: Knight Frank Research

important threats to the global and regional economy. With fears of a "hard landing" seemingly receding, the risk of a slowdown remains, as the world's second largest economy continues its transition under new leadership.

Although the Eurozone crisis did not rank as high a risk as elsewhere, there is no doubt that indirectly, a serious economic shock caused by the region's ongoing problems could impact prime markets, even in Asia Pacific. Certainly the more international markets of Singapore, Hong Kong and Sydney would be susceptible to a global economic slowdown.

There are however more insular concerns surrounding the health of domestic economies in the region, most notably in India and Vietnam, who have both seen significant slowdowns in 2012 from the strong growth of previous years. How these countries manage with some of the structural issues and whether they successfully implement reform in 2013 will have an impact on the property markets.

Further cooling measures are understandably seen as a significant risk to the prime markets, with Singapore notably ranking this as the highest risk going into 2013. Somewhat surprisingly, government intervention is ranked lower in Asia Pacific than globally. This is due to the increasing risk of interventions in mature real estate markets, such as London and Paris. Figure 8 provides a ranking of the degree of risk posed by the main cooling measures.

We have ranked interest rates, which are at historic lows across much of the region as a low risk. High inflation is seen as a risk in Asia Pacific, although the negative real interest rates that inflation generates could actually prove beneficial to property as an asset class, as buyers look for a store of wealth.

Beyond the core risks examined above, there are countless factors such as currency fluctuations, tax changes and political events which could change the patterns of demand and supply in the region's prime markets. But the fundamentals are likely to remain unaltered; the supply of luxury homes is fairly tight in most cities, with wealth growth and concentrations increasing across the region. While the feeling is that 2013 could look similar to 2012, the longer term outlook is extremely positive.

Figure 9
Asia Pacific Hotspots
Luxury housing markets are an amalgam of numerous sub-markets, some often amounting to only a few key streets or developments. We asked our network of Asia-Pacific research teams for their view as to which areas or price brackets they think will be their strongest performers in 2013.

City	Submarket
Bangkok	Central Lumpini
Beijing	CBD
Hanoi	Tay Ho District
Ho Chi Minh City	Villas in District 2
Hong Kong	Landed property on The Peak and Island South
Jakarta	Downtown CBD
Kuala Lumpur	Fringe locations with easy accessibility and good connectivity
Mumbai	Worli
Shanghai	Little Lujiazui area of Pudong
Singapore	District 9
Sydney	Inner city (15km radius) apartment market
Tokyo	Roppongi, Azabu and Akasaka

Source: Knight Frank Research

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