

Will Hong Kong Real Estate Regain its Former Peak Price Levels ?

Real Estate Tech, October 1998.

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The answer is **Yes** but we do not know when. It could be short enabling the present generation who invested in it to recoup their investment (or even more) or it could be long. The following mathematical illustrations will give a rough sense of what sort of price increase percentage performances are required to bring back the previous peak price levels based on the assumption that prices have by and large dropped 50% (used for ease of calculation) overall since last year - please note the average increase percentage for the past 30 years is around 17% per annum for the residential sector :

Within 2 Years = approximately 41% per annum
Within 3 Years = approximately 26% per annum
Within 4 Years = approximately 19% per annum
Within 5 Years = approximately 15% per annum
Within 6 Years = approximately 12% per annum
Within 7 Years = approximately 10% per annum

Hence, using the 17% as demarkation, the probability of recouping the lost ground is higher if the timeframe allowed is close to 5 years or more. Any timeframe shorter than that will probably not be sufficient though real estate increase or decrease patterns seldom follow a straight line up or down. That is to say a timeframe shorter than the 5 years (or close to it) will require a more volatile increase pattern with sharper fluctuations.

Now we need to **review the possibility of the 17% benchmark**. The fact that it was achieved before does not necessarily mean it can be attained in future. As the Hong Kong economy is increasingly tied to that of China, and assuming Shanghai to be the economic barometer, *Shanghai (future) real estate price levels (which reflect its economy) will have some implications for Hong Kong based on a pure mathematical approach (while a mass private housing market has yet to be realized, Shanghai [middle class and up] residents may now afford a HK\$225,000 home based on reported / observed information using the official HK\$ to RMB exchange rate. The Hong Kong Home is taken to be around HK\$2M):

Appreciation Rate p.a. for 25 years	Shanghai HomeHK\$ in 25 years
5%	\$ 762,000
10%	\$ 2,438,000
15%	\$ 7,407,000
17%	\$ 11,398,000
20%	\$ 21,464,000
25%	\$ 59,557,000

Shanghai Appreciation Rate p.a. Shanghai	Hong Kong (HK) requires an appreciation rate p.a. of :		
	HK\$ 2x Shanghai	HK\$=Shanghai	HK\$ 0.5x
5%	-1.1%	-3.8%	-6.4%
10%	3.6%	0.8%	-1.9%
15%	8.3%	5.4%	2.5%
17%	10.2%	7.2%	4.3%
20%	13.0%	10.0%	7.0%
25%	17.8%	14.5%	11.4%

Hence, from the above, it can be seen that for Hong Kong to see a 17% p.a. rise in price for the next 25 years, its price level will have to be twice as expensive as those of Shanghai even after 25 years AND having Shanghai prices appreciating by 25% p.a. at the same time. This at least seems a tough call for the moment. From the numbers above, the future average appreciation rate (IF there is appreciation) for Hong Kong real estate may probably be 10% or less over the next 25 years. Again, please note we have been assuming straight line price appreciation / depreciation for ease of calculation yet in reality, prices move in cyclical patterns, sometimes with very volatile fluctuations. This means that while a 17% or more price appreciation is mathematically possible during certain times in the next 25 years, to maintain such a rate over the full 25 years requires some extraordinary circumstances.

Please also note we are not saying that prices will only go up in China / Hong Kong and the above should not be viewed as predictions. Moreover, the estimated price level which Shanghai residents may afford now is just an educated guess and should this be lower, the rates of return for Hong Kong in the table above will also be lower. These are just projections to help interested parties analyse the possibilities of making successful real estate investment from a mathematical angle. Needless to say, other methods and information should also be considered / used to form a more comprehensive analysis.

Extra Note : Recently there were suggestions that residential prices in Hong Kong may have stabilized. While this may be the case, it is felt that further price drops are still quite likely and may even surpass the imagination of most. Part of the reason is that the more dominating factors today are the American economy (slow down?), the Japanese financial surgery and the like. These have yet to act out their full impact (if ever).

*Readers may also refer to our previous article "A Tale of Two Cities - Hong Kong & Shanghai" published in April 1998. Readers may contact us for a copy.