Zeppelin's

Real Estate Tech

1Q 2008: A Real Estate Newsletter by Zeppelin Real Estate Analysis Limited
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A Happy New Year to all our readers and website visitors. We think it is very likely that 2008 will be an eventful year with increased market activities and risks. Markets or sectors which have been laggards in the past may catch up with the investment frenzy seen elsewhere in particular when investment products and opportunities appear harder to come by. As one Peanuts cartoon portraying Snoopy shaking the hands of Charlie Brown who later thought to himself that “it is Snoopy's [Good Luck, you are going to need it] handshake”, your humble author wishes all the same too.

In this Issue:

We would also like to hear from prospective readers / writers who wish to share their real estate experience with us.

This quarterly (generally published in January, April, July and October) newsletter is circulated freely via email to over thousands of readers comprising real estate developers, investors, fund managers, financiers, owners, users, top executives, senior managers, prominent academics and related professionals from Hong Kong and abroad. Our content is / has also been published in newspapers and web portals such as **China Daily**, **Hong Kong Economic Journal** (a Chinese daily), **21st Century Business Herald** (China), **The Standard** (a Hong Kong English Daily), **MITCRE Alumni Newsletter**, the **Surveying Newsletter** of the Hong Kong Institute of Surveyors, **Centanet.com, Netvigator.com, Hongkong.com, E-finet.com, Red-dots.com, Realtradex.com, FrogPondGroup.com, Icfox.com**, **PacificProperties.net**, **Soufun.com** and **House18.com**. We had also been quoted in the **Asian Wall Street Journal** and interviewed by **Radio Hong Kong**. We also publish monthly articles and analyses in the months in between. This newsletter is now into its **12th year** and **46th** issue.

We also operate a website **www.real-estate-tech.com** through which we intend to share some of our real estate knowledge and ideas with interested parties. There are close to 1,000 content items, in English or Chinese, including analyses, articles, charts, and tables, plus spreadsheets, tutorials, e-books, and the like, the majority of which is free with some requiring a token fee. The website is regularly visited by thousands from all over the world and should be of interest to people interested in China real estate markets.

Zeppelin Real Estate Analysis Limited is involved in real estate development, investment, and management with a focus on **independent real estate analysis**. Together with Zeppelin Property Development Consultants Limited, we offer services related to real estate asset management [analysis, investment strategy, and portfolio assessment], project management [architectural design, cost control, and contract administration], facility management [facility utility assessment, facility strategy, and building maintenance], and marketing management [campaign coordination, leasing, and sales]. We are part of the Zeppelin Group headquartered in Hong Kong with office operations in Beijing, Shanghai, and Shenzhen and we have access to networks covering China / Asia, North America, and Europe.

China Big 4 Real Estate: Relative Price Ratios and What They May Tell

Real Estate Tech, 1Q 2008

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Here Big 4 refers to the 4 major cities of Beijing, Shanghai, Guangzhou, and Shenzhen. Nowadays, real estate investors have left their footsteps in 2nd and 3rd tier cities, although the Big 4 may still collectively occupy a significant portion in any China real estate investment portfolio.

In this issue out of curiosity, we have done simple calculations to look at 2 things in order to see if there are any recognizable patterns:

1) How the office and retail sectors in each of the Big 4 compare to its residential sector

2) How the residential, office, and retail sectors in Shanghai, Guangzhou, and Shenzhen compare to the residential, office, and retail sectors in Beijing

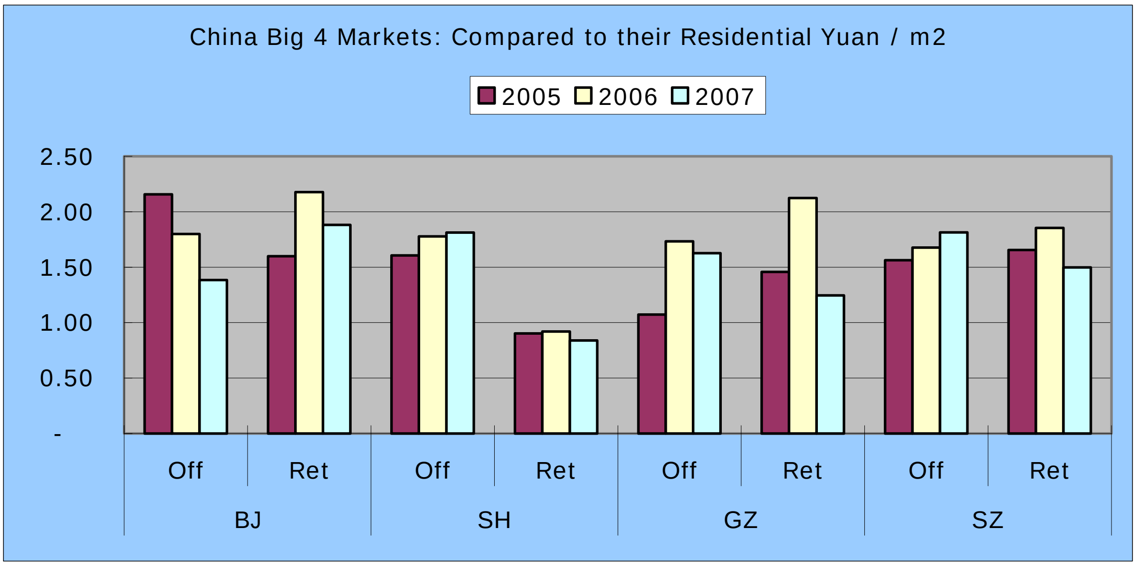
To the meticulous-minded, he or she may wonder why residential and Beijing are used respectively as the benchmark (=1.00). There is no particular reason. One could have used office or retail and any of the other 3 cities as benchmarks. Irrespective of what are eventually selected, one has to start somewhere. Here are a few points to bear in mind when reviewing the content here:

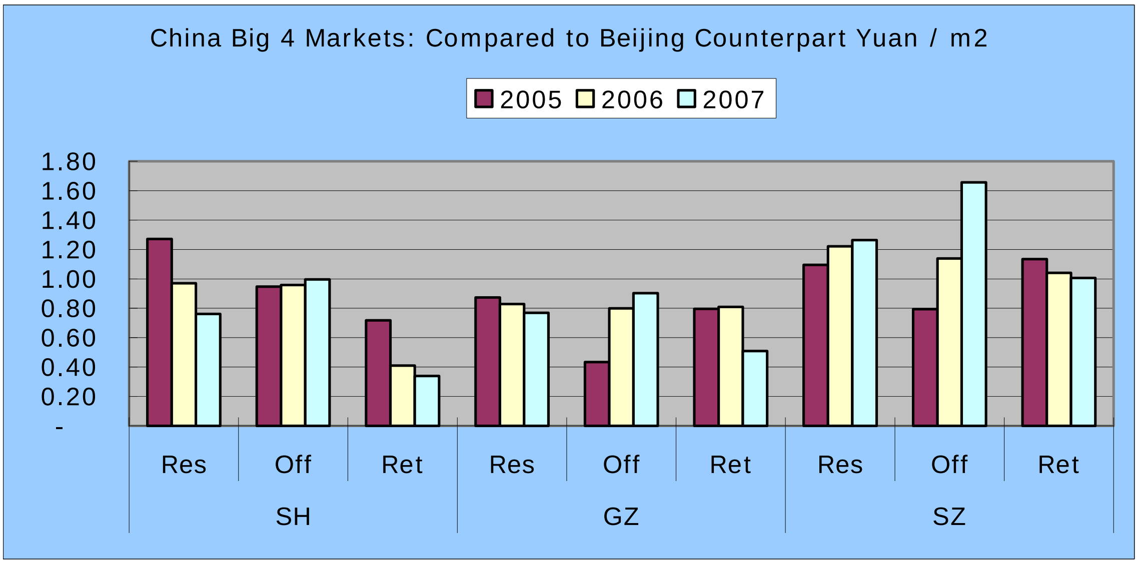
a) **Data source** = we have referred to the data contained in the www.soufun.com database and basically the monthly-published price per floor area i.e. Yuan / m2 figures on each city and its various sectors of residential, office, and retail are used. As the latest figures we have are good up to September 2007, we have looked at the September figures of 2005 and 2006 to gauge for patterns, if any. Note that such figures are cumulative for the year.

b) **For item 1** = the September 2005-2007 office and retail figures on each city are divided respectively by the corresponding September 2005-2007 residential figures for that city

c) **For item 2** = the September 2005-2007 residential, office, and retail figures on Shanghai, Guangzhou, and Shenzhen are compared one after another with the corresponding figures of Beijing

Here are the rough results:





And these are the initial observations:

A) **There are no overall recognizable patterns** = by recognizable we mean e.g. City A-Retail is always more or less x times City A-Residential, or for that matter, City C sectors harbor very close relative price ratios to City A sectors year after year. We have done simple correlations between the years of the above 2 charts and find little or insignificant correlations among them (save for those between 2006 and 2007 in the 2nd chart).

Correlation between		R	R2
2005	2006	0.56	0.31
2006	2007	0.63	0.39
2005	2007	0.39	0.15
Imply =	City-Sector to City-Residential Fluctuate		

Correlations between		R	R2
2005	2006	0.52	0.27
2006	2007	0.84	0.71
2005	2007	0.14	0.02
Imply =	City to BJ Fluctuate		

B) **Relative ratios which change drastically** = may imply comparative dangers and / or investment opportunities. Assuming all other factors being equal, when the relative ratios for a City-Sector are on an increasing trend, see if the City-Sector being benchmarked to is worth a look. On the other hand, if the relative ratios for a City-Sector are on a decreasing trend, see if this City-Sector is worth a look. If such relative ratios for a City-Sector are fluctuating, this could mean high volatility and thus risk. Note however that relative ratios are only one element to investigate among many, and investment relying solely on comparing such relative ratios could be risky and even misleading.

C) **Relative ratios which appear consistent are rare** = e.g. these are seen in Shanghai-Retail when compared to its own Residential (Chart 1), and Shanghai-Office, Guangzhou-Residential, and Shenzhen-Retail when these are compared to their Beijing counterparts (Chart 2). Note that such consistent ratios do not automatically mean little nominal price changes in the cities and sectors involved, just that their relativity changes little.

D) **Shanghai appears to be a better RELATIVE bargain to Beijing** = as its residential, office, and retail are all below or no higher than those of Beijing. Yet, given their similar metropolitan scales and that Shanghai is more likely to become a global financial center than Beijing, Shanghai seems a better bet. Guangzhou-Retail also deserves some attention.

In summary, the use of relative price ratios does NOT in itself spare an investor from investigating other ratios, reviewing from other angles, and / or making fewer calculations. Rather, it is one more tool to help with refining or fine-tuning investment decisions.

Hong Kong REIT: Allow Some Participation into Development Projects

Real Estate Tech, 1Q 2008

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REIT stands for Real Estate Investment Trusts and Hong Kong started to have its first REIT, which is the famous LINK REIT, in 2005, thereafter followed by another 6. When the REIT Code was first published in 2003, non-Hong Kong properties were not allowed. Your humble author and his contemporaries had had our share of urging geographical relaxation which materialized in 2005. Of the 7 REIT now in operation, 2 involve non-Hong Kong real estate portfolios.

Your humble author now wishes to encourage further relaxation: allow REIT to participate in real estate development projects. This restriction is understandable; real estate developments do come with more risks assuming all else being the same, and one intent of having REIT is to let the public own and share in the benefits of certain larger scale (existing and already income generating) real estate which are usually out of reach of most individual investors. To allow real estate development projects would mean no immediate rental income from such projects.

Notwithstanding the above, your humble author is not seeking to liberalize the full development restriction. Instead, REIT can be restricted to having only a certain % of its overall portfolio value e.g. 25% in development projects and perhaps a maximum % e.g. 10% per development project too. Furthermore, REIT can only invest through a pre-sale arrangement i.e. only a portion of the agreed price can be involved prior to building completion and such portion of monies can only be treated as deposits, probably held in escrow somewhere, prior to building completion (evidenced by an occupancy permit etc).

Would the REIT make an investment mistake in development projects? Certainly yet the same can happen even with existing property acquisitions. Would the risks be higher? Definitely yet these would probably be within reasonable ranges or harbor a justifiable return to risk ratio.

Regardless, letting REIT the freedom to invest some portions of capital into development projects enables the shareholders to benefit from shrewd REIT managers. It would also enhance the investment appeal of REIT, placing them between publicly listed real estate developers on the high end and bonds on the lower end.

The current REIT market in Hong Kong cannot be described as vibrant. Yet, with a graying population, a “dividend” economy will arise. REIT SHOULD BE a good investment and income generating choice.

USA Real Estate: Worth Start Monitoring

Real Estate Tech, 1Q 2008

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This is not to see if the current USA home prices would impact its economy (though it very likely will) or to gauge the impact of sub-prime mortgages. But this is done with a view to monitor if, or more importantly when, the USA residential real estate market is ripe for investment again. Now is generally not a favorable time as not only prices appear to be falling still, the US$ compared to most currencies is still in the doldrums. That is, if you were to buy now, you are likely to lose both in terms of prices and currency exchanges.

In US$ terms, the residential market in the USA has not gone down too much and a sampling of states from the west coast via the middle and south to the east coast appears to suggest the prices range from having a tiny growth to no more than 10% down. Naturally, if one focuses on individual cities or residential neighborhoods, the story could have been different. In any event, please refer to the chart below:

Adj 1yr % change in USA Res RE$ based on Euro:

States	Pre Euro-x	Euro adj	Post Euro-x	+/- %
California	-8%	-15%	78%	-22%
Nevada	-9%	-15%	77%	-23%
Colorado	0%	-15%	85%	-15%
Oklahoma	4%	-15%	89%	-11%
Texas	4%	-15%	89%	-11%
Illinois	-2%	-15%	84%	-16%
Florida	-10%	-15%	77%	-23%
South Carolina	-4%	-15%	82%	-18%
New York	1%	-15%	86%	-14%
Massachusetts	-2%	-15%	83%	-17%

Briefly in the above sample, states such as California, Nevada, and Florida have their average prices reduced by around or close to 10% while a few states in the east appear to be holding steady. Nonetheless, if one factors into the equation the loss in value of the US$ when compared to other currencies (Euro in this instance), the losses become more significant with most being above 15%.

As to what level would start to have significant investment appeal? Your humble author does not know though he may be tempted to say 50% off the current price level, including drops in the US$ currency value. One of the reasons is that in real terms, the home has only in the last 15 years or so, i.e. since around the mid 1990s, grown in prices. That is to say, from 1890 to 1994, though homes have increased multiple times in nominal terms, they could only be exchanged for similar quantities of (other) goods and products. In short, the home on average has doubled since the mid 1990s its relative worth to other asset types. Your humble author wonders if that has anything to do with China being a supportive low-cost goods producer, yet would leave this to the experts. [Read previous article on this: http://www.real-estate-tech.com/gb2312articles/hkej440_S.htm in Chinese].

Also, the previous late 1980s to early 1990s real estate bubble in the USA / North America had more to do with non-residential assets than residential ones, though this time the situation has been reversed. The USA now faces bubble in some residential markets though the non-residential sectors appear fine overall. The recent residential sub-prime mortgage crisis has benefited the multi-housing rental market as homeowners give up owning and start renting again.

In summary, the residential price per floor area (US$ / ft2 net) in the major metropolitans is not inexpensive. YET, even for very prime assets, sometimes HK$10,000 / ft2 (or US$1,200 / ft2 net) can buy an investor some of the prime locations in say a NYC or Boston, and still has changes left.