Zeppelin's Real Estate Tech

4Q 2013: A Real Estate Newsletter by Zeppelin Real Estate Analysis Limited

Phone (852) 2401 6613 Fax (852) 2401 3084 E-mail stephenchung@zeppelin.com.hk Web: www.Real–Estate-Tech.com

EU countries are in the economics talking mood again, the USA shuts down part of its government functions, Japan seeks to inflate the economy, and China appears to be trying out more liberalized economic arrangements via the Shanghai Free Trade Zone. Hong Kong tends to keep applying the various stamp duties imposed in the past year or so thus making life tough for sellers and agents of properties. In this issue:

- **Hong Kong Residential Real Estate: The Betting Ratios**
- **Nobody dies from not being a homeowner**
- **Invited Guest Author: Mr. Gary Carmell of CWS Capital Partners LLC on "The Renter Generation"**

"A real estate mogul is someone who has lost count of the real estate he or she owns."

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 the **South China Morning Post, China Daily**, **Hong Kong Economic Journal**, **21st Century Business Herald**, **Apple Daily**, **Sing Tao**, **Quamnet Magazine**, **The Standard**, **MITCRE Alumni Newsletter**, **Surveying Newsletter**, **Reidin.com, Centanet.com, Netvigator.com, Hongkong.com, E-finet.com, Red-dots.com, PacificProperties.net**, **Soufun.com** and **House18.com**. We had also been quoted in the **Asian Wall Street Journal** and interviewed by **USA Today**, **i-Money**, **Ming Pao, Radio Hong Kong**, **Cable TV (Money Café)** and **Commercial Radio**. We also publish monthly articles and analyses in the months in between. This newsletter is now into its **18th year** and **69th** 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 focuses on China / Hong Kong 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 allocation], project management [architectural design, cost control, and contract administration], and facility management [facility utility assessment, facility strategy, and building maintenance]. We are part of the Zeppelin Group headquartered in Hong Kong with office operations in Mainland China and we also have access to networks covering Asia, North America, and Europe.

Who? Me?

Stephen Chung
Managing Director, Zeppelin Real Estate Analysis Limited
Founder and Editor, Real Estate Tech Quarterly Newsletter
Real Estate Website Developer, www.Real-Estate-Tech.com

Stephen is an independent real estate analyst – number cruncher and chartered surveyor and has been involved in real estate development, investment, and management in Hong Kong / China / Asia and North America.

Stephen provides relevant real estate market insights and macro-micro assessments to real estate developers, investors, owners, financiers, funds, and civic organizations, and possesses many years of experience in building economics, project management, facility strategy, marketing, and research.

Stephen is also a regular real estate writer - columnist and his articles have been published in both English and Chinese media including the following:

- China Daily
- Hong Kong Economic Journal
- South China Morning Post
- Apple Daily
- Quamnet Magazine
- Real estate and finance websites such as Soufun.com, Finet.com etc
- Journals of professional institutes such as the Hong Kong Institute of Surveyors

Stephen is an honorary adjunct professor of the University of Hong Kong and the City University of Hong Kong and has been invited to speak to audiences from:

- Universities: such as the University of Hong Kong, City University of Hong Kong, York University
- Professional Institutes: such as the Hong Kong Institute of Surveyors, Canadian Institute of Quantity Surveyors, Royal Institute of Chartered Surveyors
- Business Associations: such as the Rotary Clubs

Stephen has 3 real estate books in Chinese published to date as follows:

Online book = Easy Real Estate Lectures

Hard copy = Real Estate Investment Know-How above 101

Most recent and hard copy = The Real Estate Market Turning Point

We welcome enquiries from interested parties and could be reached as follows:

Email: StephenChung@zeppelin.com.hk
Office Phone: 852-24016603
Office Fax: 825-24013084
Office Address: 7/F, 20-24 Kwai Wing Road, Kwai Chung, NT, Hong Kong
Website: www.Real-Estate-Tech.com

Our services can be obtained and delivered via a) tailor-made professional consultation; b) online report purchases; c) emailed discussions and advice; and / or d) phone discussions.

Hong Kong Residential Real Estate: The Betting Ratios

Real Estate Tech, 4Q 2013

Stephen Chung BS BBldg(HKU) MS in Real Estate(MIT) MRICS MHKIS FPFM PQS RPS(QS)
Zeppelin Real Estate Analysis Limited - Phone (852) 24016603 / Fax (852) 2401 3084 stephenchung@zeppelin.com.hk

To buy or not to buy? (No, this is not from Shakespeare's Hamlet)

A friend of your humble author has recently sold his home for a good price and wonders if he should jump back in or rent for a while…and wait. There is no standard answer and no one size fits all although the friend was informed of my bet on the market: down.

Overall, while the market transactions have been trending downwards, prices are still holding up quite nicely notwithstanding some price cut deals here and there. Furthermore, many recent market opinions tend toward painting a not so rosy picture compared to reports made 12 months ago, and many commentators expect some price corrections ranging mostly from 10% to 20%, with a few opting for 30% or more. As for your humble author, let's say he will not be surprised at all if prices were to dive 50% within a 2 or 3 year period.

Now, assuming my friend finds the down market bet being more likely than an up market bet, then he may do the following math to ascertain his betting ratios:

A) We shall use a simple example = assume a residential property is worth HK$10M and based on the typical 3% rental yield, this would mean the landlord can expect to fetch HK$300K per year or HK$25K per month.

B) Now this HK$25K per month rental includes the apartment management fee, ground rents where applicable, and property rates (to the uninitiated, these are similar to municipal taxes), and assume these items cost the owner on average HK$4,000 per month, then the net rental before taxes would be (HK$25,000 - $4,000) x 12 months = HK$ 252,000 per year.

We use the net rental figure for comparison between the buy and rent options because even if my friend decides to buy and live in his own home, he would still have to pay this HK$4,000 per month. In short, the net rental reflects the actual extra recurrent cost the renter needs to dish out over owning the property.

For simplicity, we also assume 1) the renter does not get any return on his cash saved from not buying; 2) no mortgages are used in buying and owning; 3) a firm 2 year rental contract; 4) the various special stamp duty taxes do not affect our scenario.

We shall on the other hand treat the net rental offered by the renter to be a total write-off, i.e. no value is assigned to the possession and enjoyment of the rented property.

C) Here is the chart:

Price $	Annual Rent	Annual NET Rent	2 year NET Rent
10,000,000	300,000	252,000	504,000
Price Drops:		Divided by:	2 year NET Rent
5%	500,000		0.99
10%	1,000,000		1.98
15%	1,500,000		2.98
20%	2,000,000		3.97
25%	2,500,000		4.96
30%	3,000,000		5.95
35%	3,500,000		6.94
40%	4,000,000		7.94
45%	4,500,000		8.93
50%	5,000,000		9.92

As can be observed, even just a 5% price drop renders a close breakeven with the 2-year renting budget. And with each decrease of HK$500K from the price, the price drop / net rental budget ratio goes up more or less by 1. In short, the betting ratios get better with each drop.

As to at which ratio should start to entice the renter to switch back to owning, this depends on the ascertainment, even if only a guess, of the market condition and price trend. If one thinks prices have yet to stabilize, by all means wait further. If not, then a switch may be called for.

However, as to what minimum ratio deemed probable is sufficient to entice someone to take the renting and waiting route, there is again no cast-in-stone type answer, although your humble author would suggest a minimum of 2. That is, for every probable dollar loss, there is a similar probability to gain two dollars. This means one at least has to anticipate a 10% price drop, and more if what one intends to purchase would lead to hefty stamp duties.

Consider probabilities too

Expecting what $ amount of real estate price gain or loss is one thing, considering their probabilities of occurrence is another. For instance, using the same $10M property in the example above, say there is an 80% for the price to drop $1M (10% of the current price), and say another investor thinks there is a 10% for the property to gain $5M (50% of current price), which expectation is worth more? Here's one way to calculate it:

80% x $1M (price drop) = $800,000 and 10% x $5M (price gain) = $500,000. The drop expectation is worth more.

All in all, if one is inclined to expect prices to drop more than to rise, then renting and waiting is also an investment tactic.

Nobody dies from not being a homeowner

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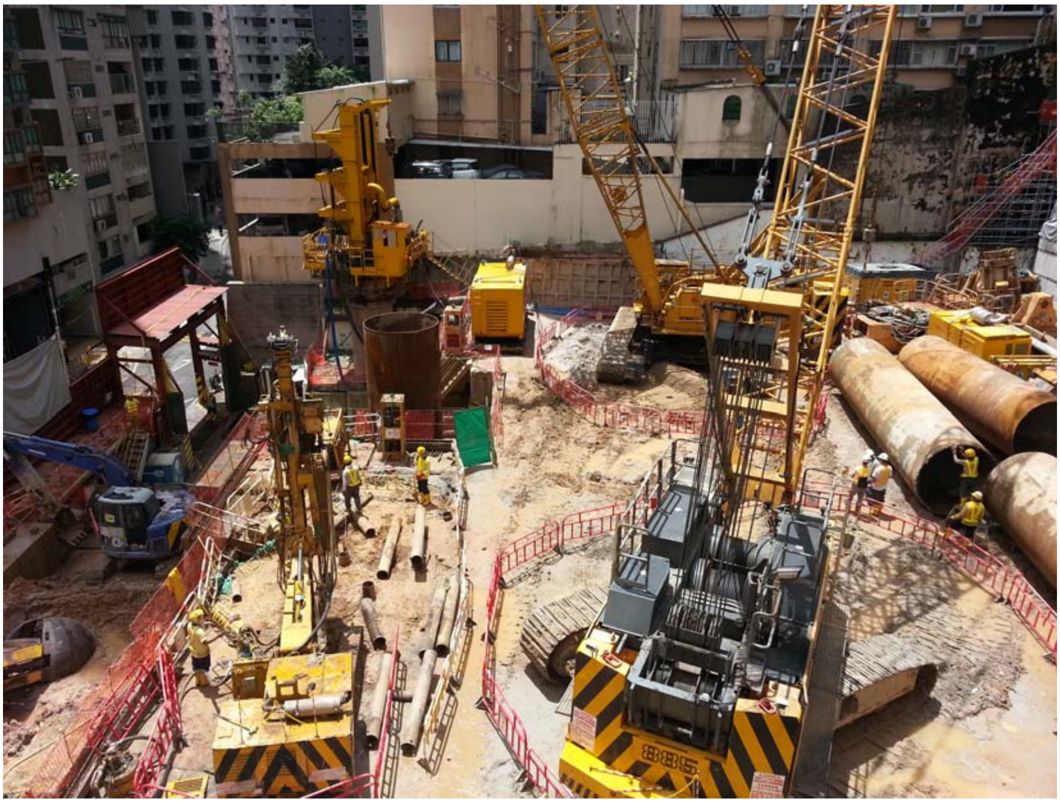
Stephen Chung BS BBldg(HKU) MS in Real Estate(MIT) MRICS MHKIS FPFM PQS RPS(QS)
Zeppelin Real Estate Analysis Limited - Phone (852) 24016603 / Fax (852) 2401 3084 stephenchung@zeppelin.com.hk



Built for shelter alone?

Humans can't last long without water and perhaps only a few weeks at best without food. Naturally we also need shelter from the weather elements. Today's young generation may add the smart phone, GPS, apps, i-pads, and the internet to the list too.

However, your humble author has yet to witness a case in which someone dies because he or she is not and cannot be a homeowner. Conversely, he had only heard of cases where someone overpaid for and over-borrowed on the real estate, thus ending up in bankruptcy and in a few instances, and regrettably, ending life as well. The fact we need shelter does not equate we need to own the shelter too.

While your humble author believes owning one's home could be a viable investment option for many households, at least one gets a roof over one's head comes old age, he does not see the need to be overly worked up about homeownership, financially, emotionally, or philosophically. Or for that matter seeing homeownership as being suited to everybody.

Being a homeowner does not automatically imply greater virtue over someone who is not. Nor does homeownership automatically lead to greater social stability – at least one Harvard study which your humble author had read does not support this common view in its entirety. On the other hand, homeownership sometimes reduces societal and labor mobility; imagine a real estate market with falling prices and contemplate who can relocate faster (to another city where there are jobs): a renter or a homeowner.

An owner-occupied home differs somewhat from an investment property in that the owner derives satisfaction and enjoyment from living in it, apart from the potential financial return or even perceived prestige. In short, there is a utility aspect which worth is more or less reflected by the net rental which the specific property can fetch.

As for the investment portion of a home, a few points to ponder:

A) Timing is of the essence = we had compared years ago the investment outcomes of different real estate investment tactics and those who have either the skill or luck to acquire and dispose of property in a timely manner will beat the other tacticians by a mile. Here is the article:

http://www.real-estate-tech.com/articles/SRS071001.htm

B) "Location, location, and location" sucks = we are not saying location is not important, it is. We are just opposed to saying it 3 times in a phrase giving people a wrong impression that this is the only factor to consider when investing in real estate. The phrase might have worked in the 14^{th}C when the world was not as connected; what happened in Venice barely affected Xian and vice versa. Not today.

C) Hong Kong real estate market cycle = based on the past 30 years or so, a cycle appears (from high to high, or low to low) to last around 16 years plus or minus 1. As such, adding 16 to 1997 price peak is 2013. Naturally, what had happened or seen in the past might or might not occur again. Make your own bet.

D) Population and demographics changes = vendors of real estate always like to point out that across the globe, property prices have been on an uptrend despite hiccups along the way. However, the phenomena might have been made possible via a variety of factors, planned or coincidental. And rising income and population are / were two such factors. If so, the income factor has been stagnant recently for at least some developed economies, and world population is expected to start declining some 20 years from now (peaking at 9B or so), not to mention the graying trend in many. Need we start contemplating better utilization of land and property under such probable scenarios? What do you think such trends, if realized, will have on prices?

E) Comparing real estate with stocks (equities) is pointless = many like comparing real estate to stocks and bonds and arguing over which asset class is better overall etc. Your humble author thinks this is unnecessary. Both asset classes harbor pros and cons, and unless one is buying all the real estate in any one market or all the stocks in any one exchange, and assuming point (A) above being equal, successful investing in real estate or stocks requires picking the proper items (individual properties or stocks) at the right time and for the right price. In fact, your humble author suspects most investors own both asset classes albeit in differing portions.

Real estate can be a very good investment asset given proper selecting, pricing, and timing. Learn to master it and not let it master you.

The Renter Generation: by Invited Guest Author Mr. Gary Carmell of CWS Capital Partners LLC

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Zeppelin Real Estate Analysis Limited - Phone (852) 24016603 / Fax (852) 2401 3084 stephenchung@zeppelin.com.hk

Sunshine, clean air, greenery, sizable properties, all for a fraction of a Hong Kong home

Note to readers: we had read the analytical article "The Renter Generation" written last year by Mr. Gary Carmell, President of CWS Capital Partners LLC, an apartment investment and management group in the USA, and thought its content would benefit our subscribers and readers immensely, especially those looking to invest in USA properties. As such, we asked Gary for permission to include it in our newsletter and he kindly agreed.

Executive summary: The rental apartment sector has good prospects because a) a sizable cohort of the 18 to 29 year olds – who form a strong tenant pool - is forthcoming; b) steady employment, rising income, and married households – supports needed for a strong homeowner strata - are getting weaker and fewer; c) renting facilitates the increasingly mobile job market; d) more stringent mortgage requirements imply many will seek to rent than to buy; just to name a few. No substitute though to reading the full analysis "The Renter Generation":

http://www.cwscapital.com/UserFiles/file/qu/CWS_April2012_Lead.pdf

Hope you would enjoy reading it as we had.

Do you need our services? You DO when…

- **In Real Estate Development:** you encounter overestimated proceeds, cost overruns, underestimated time schedules, design and quality issues, construction contractual disputes, joint venture conflicts, or the like…you need an experienced project manager like us

- **In Real Estate Investment:** you encounter challenges in 1) Selecting which markets (cities), sectors (residential, office, retail etc), and properties-projects to invest; 2) Striving for the best possible risk-adjusted portfolio return; or 3) Sensing the volatility of a market or sector; 4) Deciding which corporate strategies, tactics, priorities, properties, and projects to pursue; 5) Getting a INDEPENDENT SECOND OPINION on which you can trust…you need an independent real estate analyst like us

- **In Real Estate Management:** you encounter questions on 1) if it is more economical to buy or rent the real estate facilities and assets, and if so where and what; 2) how best to manage and maintain such facilities and assets; 3) what level of human resources are required, all with a view to maximize their utility to help achieve the corporate objectives… you need a seasoned facility strategist like us

- **Contact us:**

Hong Kong Office: Mr. Stephen Chung stephenchung@zeppelin.com.hk
Address: 7/F, 20-24 Kwai Wing Road, Kwai Chung, NT, Hong Kong
Phone: 852-24016603 Fax: 852-24013084 Web: www.Real-Estate-Tech.com

Shenzhen Office: Mr. K K Wong kkwong@zeppelin.com.hk
Address: Unit 1203, Shenhua Commercial Building, 2018 Jia Bin Road, Shenzhen
Phone: 755-28627707 Fax: 755-28687727

Beijing Office: Mr. Tomman Kwan tommankwan@zeppelin.com.hk
Address: Suite 2001, Tower G, City One, No. 48 Wang Jing Xi Road, Chaoyang District, Beijing 100102
Phone: 10-65011565 Fax: 10-65527129

For details: please download our group introduction at http://www.real-estate-tech.com/ZPG-Group%20Introduction-sOct07.pdf

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Zeppelin **Property Development Consultants Limited**

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