

Hong Kong Property

Key takeaways from call with Moody's on Hong Kong property sector outlook

Industry Overview

High rates & economic uncertainty to be headwinds

We hosted a call on Jan 31st with Stephanie Lau from Moody's to discuss the HK property sector outlook for 2024. (1) Moody's believes high interest rates and economic uncertainty in China may continue to be key headwinds. It has a negative outlook on ratings of China and Hong Kong. (2) In Moody's view, office and residential markets may remain under pressure, but the retail market may be relatively resilient. (3) Moody's thinks the challenging operating environment has weakened rated developers' credit fundamentals and reduced their financial buffers. Our views are similar to Moody's. We expect HK developers to see a mild deterioration in their fundamentals amid the city's cyclical downturn. But we believe the deterioration may be mitigated by their prudent investments and/or dividend cuts. We think HK companies' ratings will remain largely stable, given their adequate rating headroom. But if the cyclical downturn turns out to be longer/ more significant than expected, select BBB-rated companies (esp. those which have large exposure to the HK office market or which have invested heavily in new businesses/ taken on large projects in recent years) may see negative rating actions.

Office & residential markets to remain under pressure

Moody's expects office and residential markets to remain difficult in the near term. Office rents declined by more than 30% cumulatively in the past 4 years. Moody's continues to see downside potential in office rents due to oversupply, Chinese companies' weak demand for office space, and high vacancy rate. Moody's expects rated developers' rental income from their offices to see a mid-to-high single digit decline in the next 12-18 months. Negative rental reversion may continue but narrow from the level in '23. In Moody's view, due to weak market sentiment and a looming supply glut, residential prices may decline by 5%-10% in '24. Although interest rates may drop later this year, they may still remain high relative to historical levels.

Retail sales growth to taper off due to high base

Moody's believes the retail market may stay more resilient in '24, with retail sales to see a low-to-mid single digit YoY growth (vs. around 15% YoY growth in '23 when the HK-China border reopened). According to Moody's, tourist arrivals remain well below the level in '18, while a change in tourists' spending pattern and China's economic slowdown may negatively affect the recovery in the retail market. Also, a daily average of around 180k HK residents crossed the border to China in '23. Moody's think more frequent northbound travels by HK people may deter local consumption.

'24E: flat EBITDA, stable leverage & lower int. coverage

In Moody's view, weak office & residential markets may cap rated HK companies' earnings growth. Their aggregate EBITDA may be stable YoY in '24 & rise moderately in '25. Their leverage may be stable YoY in '24 but remain meaningfully higher than pre-pandemic levels. High interest rates have eroded their interest coverage headroom.

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Sirius Chan
Research Analyst
Merrill Lynch (Hong Kong)
+852 3508 3100
sirius.chan@bofa.com

Suyang Lu
Research Analyst
Merrill Lynch (Hong Kong)
+852 3508 5066
suyang.lu@bofa.com

Xiang Gao, CFA
Research Analyst
Merrill Lynch (Hong Kong)
+852 3508 6962
xiang.gao@bofa.com

Jing Peng
Research Analyst
Merrill Lynch (Hong Kong)
+852 3508 3105
jing.peng2@bofa.com

HK: Hong Kong

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