Turner & Townsend

Hong Kong market intelligence

June 2024

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Contents

Overview

Moderate growth in 2024 anticipated for Hong Kong's construction sector, following economic improvement of 2023

Hong Kong is returning to a consistent yet cautious growth trajectory with a rise in consumer spending, real income levels and the removal of pandemic austerity measures. The construction industry is following suit, boosted by the government's focus on expanding major construction projects and increasing housing land supply. Data reports indicating an upward trajectory of economic growth for Mainland China in 2024 further eases concerns around Hong Kong's growth outlook.

The 2024-2025 Hong Kong Budget reaffirms the government's focus on developing Hong Kong as a strong regional business and commerce hub. Major infrastructure spending across housing, research and development, healthcare, tourism development and smart transit systems will strengthen Hong Kong's position as a destination for enterprise and talent - central to achieving its economic ambition.

Approximately 19 percent of recurring government expenditure has been allocated to healthcare infrastructure projects. The Digital Economy Development Committee (DEDC)'s report also reflects the government's policy push toward advancing the development of Hong Kong's digital economy and infrastructure. The administration's green agenda is an additional boost to the construction industry with new renewable energy projects and aspiration to position Hong Kong as an international maritime and logistic hub with a nationwide plan to make its ports smart and sustainable.

However, challenges continue to persist. Weakened construction demand from the Mainland, rising labour costs, the lack of skilled labour, and high construction costs continue to hamper growth. Hong Kong's construction sector is expected to face a labour shortage of 40,000 people in 2027. In response to this anticipated shortage, the government has allowed construction companies to apply for bigger quotas of workers from overseas to work on construction projects.

Given the government's current financial position and existing market uncertainties, Hong Kong's mega-projects are being reassessed for financing, cost-effectiveness and affordability. Despite positive indicators, like the uptick in tourism and improved government policies helping the industry, a cautious approach making strides to Hong Kong's mega infrastructure development is prudent, given domestic and international challenges.

All factors considered, the economy and Hong Kong's construction industry are poised for gradual but steady progress. With the government prioritising high-quality developments and a focused agenda on building capacity for economic development through various sector-specific strategies, an approach of doing the right project and doing the project right is key to setting the construction industry up for success.

Economy

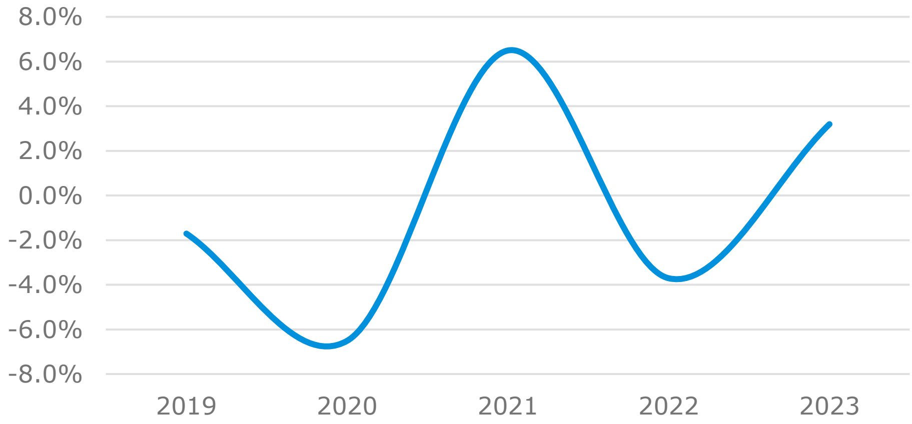
A considerable comeback for the economy in 2023

After a significant contraction of 3.7 percent in 2022, Hong Kong's economy made a notable recovery in 2023. Though lower than the government's forecast of 3.5 to 5.5 percent, the economy held its upward trajectory with an overall 3.2 percent growth over the previous year.

The consistent growth across all four fiscal quarters was driven by a resurgence in inbound tourism and strong domestic demand, fueled by the removal of pandemic prevention measures and the recommencing of normal travel. By December 2023, Hong Kong had welcomed 34 million visitors, with four million arriving in December alone. This momentum continues into 2024, with over 11 million visitors in the first three months.

Hong Kong's economy grew by 3.2% in 2023 - a significant increase over the 3.7% contraction in 2022

Figure 1:
Real GDP (year-on-year growth)



Source: *Census and Statistics Department, The Government of the Hong Kong Special Administrative Region*

In line with the overall economic upswing, nearly all components of Gross Domestic Product (GDP), measured by expenditure, witnessed growth in 2023. However, exceptions were noted in government consumption expenditure and expenditure on export and import of goods. Total exports declined by 10.3 percent in 2023, primarily due to weakened external demand, while total imports of goods saw a similar drop of 8.6 percent. Despite this, the general trend indicates a positive trajectory for the economy.

Moreover, with the removal of pandemic prevention measures in both Hong Kong and Mainland China in early 2023, consumer sentiment rebounded swiftly. Improved labour market conditions and rising household incomes further bolstered overall economic growth. A notable highlight was the 7.1 percent growth in expenditure on building and construction, driven by increased private sector spending, which effectively offset the decline in public sector expenditure.

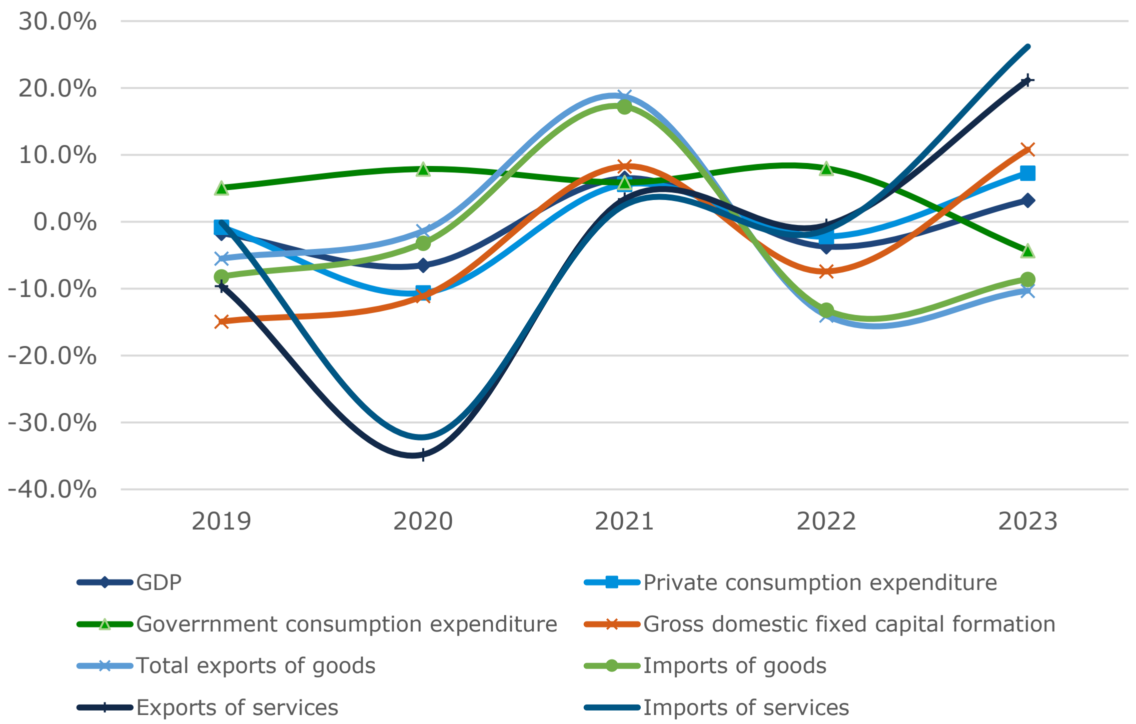


Figure 2:
GDP by Expenditure Components 2019 - 2023 (year-on-year % change)

Source: *Census and Statistics Department, The Government of the Hong Kong Special Administrative Region*

Cost pressures on domestic business remained mild in 2023 with wage growth staying moderate and a low ceiling maintained on commercial and housing rental rates. Consumer Price Inflation (CPI) also remained moderate despite an increase in electricity prices and the overall cost of living.

Composite CPI inflation rose from 1.9 percent in 2022 to 2.1 percent in 2023. A strong Hong Kong dollar played a significant role in capping inflation, particularly in comparison to Hong Kong's major trading partners. The strength of the Hong Kong dollar against many major currencies has helped to stabilise the economy against increased inflation pressures from its major trading partners.

Optimistic outlook for 2024

Continued geopolitical conflicts and the residual effects of sharp fiscal tightening will continue to impact global economic growth, international trade and investment. According to the International Monetary Fund (IMF), global growth is projected to remain at 3.1 percent in 2024, consistent with 2023. Inflation is expected to soften globally in 2024 due to stricter monetary policies in developed economies. This constrained global financial environment may affect cross-border financial and business activities.

In line with other Asian economies, the Hong Kong economy is expected to grow in 2024 due to robust domestic demand and an additional uptick in tourism. However, weak demand from advanced economies and geopolitical factors will continue to impact Mainland China's export performance. Despite these challenges, Mainland China's pursuit of high-quality development projects through comprehensive reforms and the expansion of the economy promises a solid medium-term outlook for Hong Kong's economy. Strong economic fundamentals and additional export policy support will further help maintain Hong Kong's growth trajectory.

Hong Kong's GDP is expected to continue growing with an estimated forecast of 2.5 to 3.5 percent in 2024, following a 3.2 percent growth in 2023. CPI is expected to remain moderate, though there may be some inflation in domestic costs due to economic growth. With the government increasing capacities for further economic development via land development projects, expanding infrastructure, as well as positioning Hong Kong as an attractive destination for enterprises and top talent, growth is expected to maintain momentum in the long term.

Hong Kong Budget 2024-2025

This year's Budget showcases the government's determination to amplify economic growth using key strategic levers.

Under the banner of 'Advance with confidence. Seize opportunities. Strive for high-quality development', the focus of this year's Budget affirms the Hong Kong government's confidence in the economy's growth momentum.

With an increase of 3.2 percent over the previous year, the economy is forecasted to hold this growth rate from 2025 through to 2028.

A moderate inflation rate and real term growth in income levels of general consumers shore up the forecast of economic growth from 2.5 to 3.5 percent in this year, even as there is an estimated consolidated deficit of HK$101.6bn in 2023-2024. The government's focus on innovation and technology, fiscal consolidation strategy and 'One Country, Two Systems' approach offset some of the challenges in the Hong Kong market.

The construction industry is a key economic driver. Average annual expenditure has increased over the past five years to about HK$85bn in 2023-2024 due to governmental focus on infrastructure projects aimed at improving livelihoods and the environment. Land and housing supply is ramping up, with a target supply of 308,000 public housing units over the next ten years until 2033-2034.

The medium range forecast projects capital works expenditure could be up to HK$90bn, highlighting the government's strong commitment to infrastructure development. Underscoring this commitment is the railway initiative, which aims to enhance connectivity within the Greater Bay Area (GBA) and promote the 'GBA on the Rail' concept. Additionally, a steering committee under the Development Bureau (DEVB) will be established to advance the application of Modular Integrated Construction (MiC), in tandem with potential investments in the MiC supply chain by the government to increase innovation and overall productivity in the construction industry.

Key transportation initiatives have been earmarked to encourage economic productivity based on the planning principles of 'infrastructure led' and 'capacity creation'. These include collaboration between Airport Authority Hong Kong and Dongguan Port Group to develop a sea-air cargo transshipment mode and environmentally-friendly transit systems in the pipeline.

Tech is also a prime focus area for the government. Centres like the Hong Kong Microelectronics Research and Development Institute (HKMSRDI) and the development of the Cyberport 5 project are examples of the direct investment and co-investment in projects to be implemented, covering areas such as life technology, green technology and finance, semiconductors and chips.

Healthcare infrastructure, such as hospitals and testing institutes, is a major focus area, with approximately 19 percent of recurring government expenditure allocated to this sector.

Based on the Budget, we are encouraged by the construction industry's promise of consistent growth, supported by strengthened government financial fundamentals and focused investments in large-scale infrastructure projects.

Key economic levers in this year's Budget influencing the construction industry

The 2024 Budget introduces several strategic initiatives aimed at driving growth and innovation within Hong Kong's construction sector. These key levers encompass major infrastructure projects, housing developments, technological advancements, and sustainability efforts.

Northern metropolis

Site formation and infrastructure works in Shenzhen-Hong Kong Boundary Control Points Economic Belt, Yuen Long and North districts.

New residential, commercial and industrial areas in total land area of about 300 square kilometers.

Transport

Plans for smart and green mass transit systems in East Kowloon, Kai Tak and Hung Shui Kiu / Ha Tsuen.

Developing two cross-boundary projects – Hong Kong-Shenzhen Western Rail Link and Northern Link Spur Line.

Land and housing Supply

The Land Sale Programme will cover a total of eight residential sites, two commercial sites and one industrial site.

Railway property developments, private development and redevelopment projects as well as Urban Renewal Authority project will contribute to private housing land supply in 2024-25.

Technology

Establish the Hong Kong Microelectronics Research and Development Institute (HKMSRDI) this year.

Science Park Expansion Programme and Cyberport 5 Expansion will add 79,000 gross floor area to existing technology infrastructure.

Healthcare

Construction of the Chinese Medicine Hospital and the Government Chinese Medicines Testing Institute.

Establishing the Hong Kong Centre for Medical Products Regulation (CMPR).

Green infrastructure

Develop Hong Kong as a green maritime fuel-bunkering centre and Hong Kong International Airport into a green airport.

Apply renewable energy in government buildings and facilities.

Tourism and culture

West Kowloon Cultural District continued development of facilities including new museums, performance venues and public spaces.

Financing

Expanding the scope of the Government Green Bond Programme to cover sustainable finance projects and take forward the Infrastructure Bond Scheme to raise capital for infrastructure projects.

Issue bonds of about HK$95-135bn per annum in the next five years to drive projects delivery.

Construction output

Sector expenditure is set to experience steady growth despite increasing housing land supply, amongst other factors, driven by government support.

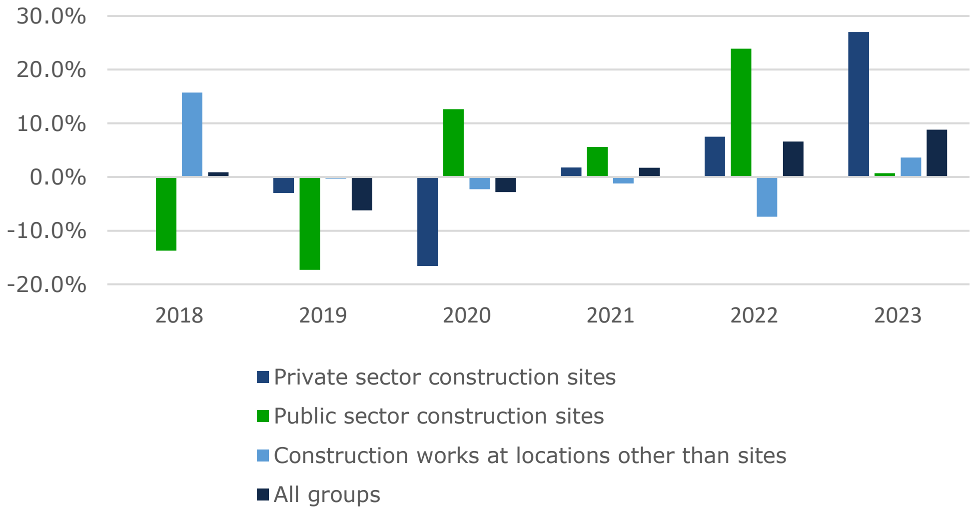
Construction Industry Council (CIC) data forecasts an annual rise in construction expenditure between 2.0 to 3.0 percent in following year (2024-2025). Additionally, data from the Census and Statistics Department shows the total gross value of construction works (GVCW) increased over 2023.

Private sector sites demonstrated a strong increase of 25.4 percent in real terms through 2023 while public sector sites grew by 1.3 percent in the same period.

Figure 3:

Gross Value of Construction Works (GVCW) in nominal terms

(year-on-year % change)



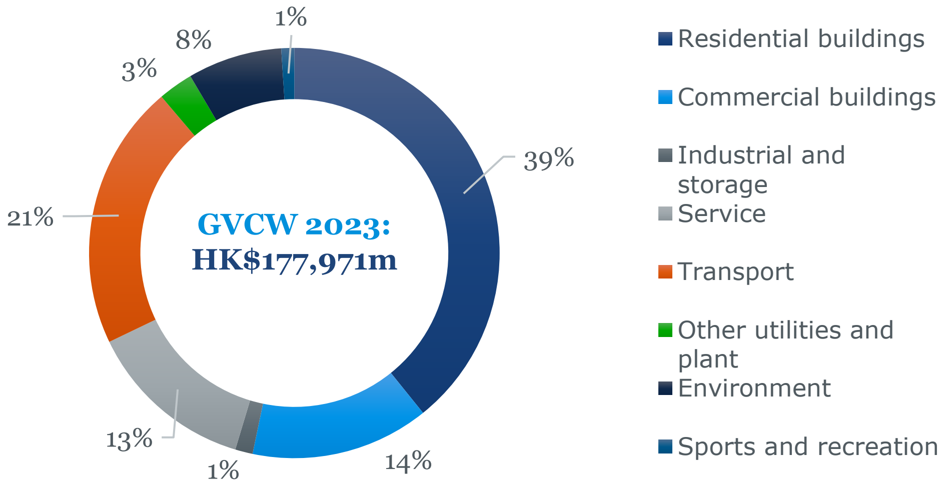
Source: *Census and Statistics Department, The Government of the Hong Kong Special Administrative Region*

Residential buildings remained the largest contributor to GCVW, registering a 49.8 percent nominal increase from the previous year. Transport projects also remained consistent, contributing the second-largest share of GCVW with an increase of 7.2 percent in nominal terms.

Figure 4:

Gross Value of Construction Works (GVCW)

(analysis at construction sites by end-user group)



Source: *Census and Statistics Department, The Government of the Hong Kong Special Administrative Region*

The government's 'Long Term Housing Strategy Annual Progress Report 2023' highlights land and housing supply as a priority. With a 70:30 split between public and private housing, the target is approximately 440,000 units over the next decade. For 2024-2025, the private housing target is 13,200 units, potentially surpassing this by 15 percent to reach 15,500 units. Key developers like the MTR Corporation Limited (MTRCL) and the Urban Renewal Authority (URA) will contribute an estimated 5,400 flats.

The Land Sale Programme will cover eight residential sites, providing 5,690 units, with the government taking a cautious approach to land sales given current market conditions. These sites, along with two newly identified sites, will enhance mature neighbourhoods and prime real estate properties. Residential housing projects, both public and private, will account for the largest share within the Gross Construction Value of Works (GCVW) in 2024.

Industrial development will also add significantly to industry output. The announced government sale of a site up for redevelopment near Yuen Long INNOPark will add 16,000 square metres of GFA for commercial use. Other government policies such as providing land supply for 80,000 private housing units in the next five years, focus on healthcare and transit infrastructure development are also poised to provide continued growth for the sector.

8.8%

Growth in GVCW during 2023

49.8%

Growth in GVCW for residential building projects in 2023

308,000

Public housing units over the next decade

Tender price escalation forecast

Tender prices are expected to rise by about 2.0 percent in 2024, with construction activity due to take a dip in the private sector and spending on public projects tipped to reduce marginally.

Tender prices increased by 4.0 percent in 2023, as predicted our earlier forecast for 2023 in our previous Hong Kong market intelligence report. Price escalations have gradually slowed throughout the year due to global economic headwinds, high interest rates and lower than forecasted actual land sales.

Domestic challenges include tenders on hold for the sale of private residential sites over the past two years, reduced actual expenditure on public sector projects and prolonged project timeline for major infrastructure projects impacting the progress of mega projects and construction costs. A muted Chinese property market facing oversupply and strict measures to regulate borrowing by developers have further dampened demand in Hong Kong's real estate.

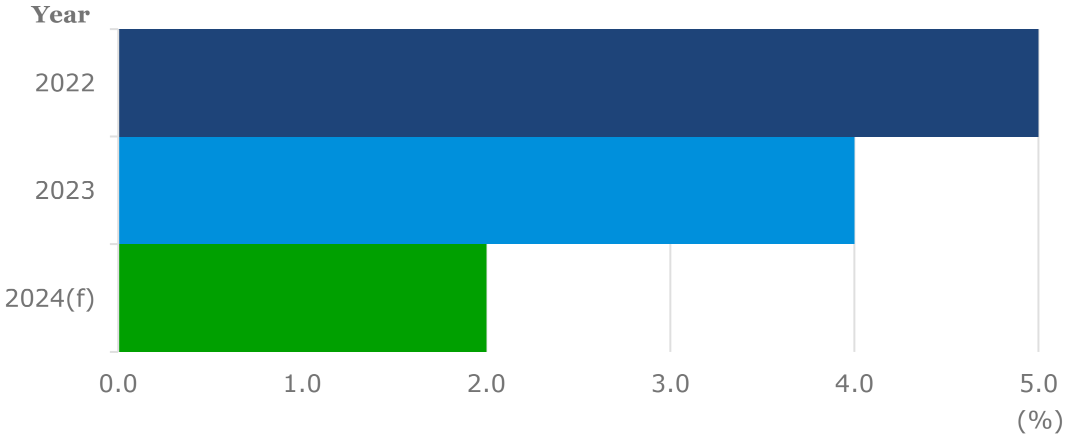
Input costs for construction are fluctuating. A stronger Hong Kong dollar and reduced demand for construction materials from Mainland China will likely reduce material costs this year. A shortage of skilled workers, coupled with an aging existing workforce remain one of the industry's key challenges driving labour costs upward. However, this may be offset through reduced material costs as the slowdown in large-scale construction projects means prices for key construction materials such as sand, concrete and equipment are likely to fall.

Despite such economic headwinds, the tender price escalation in Hong Kong has shown a positive trend ranging from 3.0 to 5.0 percent over the past three years.

Assuming conditions remain largely stable, we expect to see a moderate increase of tender prices by about 2.0 percent in 2024.

Figure 5:

Tender price escalation forecast



Key construction material market prices

Materials	December 2022	December 2023	% Change
High tensile steel bars (10mm to 40mm) (HK$/tonne)	6,456.0	5,979.0	-7.3%
Portland cement (HK$/tonne)	931.0	940.0	+0.9%
Aggregates (HK$/tonne)	108.0	99.0	-8.3%
Sand (HK$/tonne)	313.0	300.0	-4.2%
Sawn hardwood (50mm x 75mm column) (HK$/m³)	6,939.0	6,939.0	No change
Galvanised mild steel plate (HK$/tonne)	23,241.0	18,977.0	-18.3%

Source: Census and Statistics Department, the Government of Hong Kong Special Administrative Region

Looking to the future

Hong Kong's construction sector is embracing alternative project delivery models as its portfolio of construction projects become larger and more complex.

The focus on the construction industry as a key pillar of Hong Kong's growth continues, underscored by ongoing government commitment to spending. A dedicated Budget outlook focused on infrastructure spending reaffirms the government's growth ambitions. Hong Kong's construction output remains steady and strong, and we expect the tender price to escalate at a moderate rate.

Upcoming mega projects, such as the proposed Northern Metropolis and transport infrastructure expansions, are being reviewed, with new funding and delivery models being deployed. Hong Kong's supportive government policies position the construction industry for growth, albeit in a measured and cautious manner. In this business environment, complex and mega projects can be procured and delivered more efficiently by adopting alternative models such as public-private partnership (PPP), framework contracting, delivery partner approach, digital programme management office (PMO) and integrated project controls.

These alternative models have been adopted by global organisations in both private and public sectors. Delivering mega projects require considerable amount of supply-chain preparation. Critical to an effective programme with a suitable project delivery model and strategic cost management measures is leveraging volume to secure considerable procurement savings.

Overall, the construction market has moved toward a steady growth yet cautious outlook given the current macro-economic factors. Financial prudence and project governance is at the forefront in the various project delivery models currently being implemented, whether through traditional or alternative approaches.

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Hong Kong is not alone in facing global economic headwinds, high construction costs and skilled labour shortage among other domestic challenges, as it embarks on massive land and infrastructure developments.

We see value in prioritising the right projects that will act as future growth engines in Hong Kong and strengthen its position as a regional economic hub. To ensure successful outcomes, complex and mega developments will require strong programme leadership, early assessment and adoption of a suitable project delivery model, with a digital-first approach.

Daniel Cheung
Director – Strategic Lead, Hong Kong & Macau at Turner & Townsend

About Turner & Townsend

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We are majority-owned by CBRE Group, Inc., the world's largest commercial real estate services and investment firm, with our partners holding a significant minority interest. Turner & Townsend and CBRE work together to provide clients with the premier programme, project and cost management offering in markets around the world.

We are passionate about making the difference, transforming performance for a green, inclusive and productive world.

Our team

Daniel Cheung
Strategic Lead
Hong Kong & Macau
Daniel.Cheung@turntown.com

Ollie Sneath
Head of Real Estate
Hong Kong & Macau
Oliver.Sneath@turntown.com

www.turnerandtownsend.com