



Conversion or redevelopment? Effects of revitalization of old industrial buildings on property values

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ABSTRACT

The revitalization programmes, which are meant to transform the neighbourhood community for better living, are presumed to bring positive value enhancements to the living environment of the city, while allocating limited land resources effectively to the highest and best use. By employing two hedonic price models and based on two sets of residential transaction data obtained from a former industrial-hub, *Kwun Tong*, in Hong Kong, the study investigated whether different modes of revitalization (*redevelopment* or *wholesale-conversion*) bring different externalities to the value of the neighbourhood properties in the city. Surprisingly, the findings suggest that revitalization programmes, irrespective of the mode, did not generate positive externalities to the property values in the vicinity. More precisely, neither redevelopment nor wholesale-conversion, in general, has brought significant positive value enhancements to the nearby properties. Though this finding is against the intuition that positive externalities generated by revitalization are capitalized into nearby property values, this also reinforces the intuition that the economic benefit of a single building revitalization is less apparent than an area based revitalization approach. Results, however, indicate that, although revitalization has not brought as much positive benefits expected, there are some positive indications that property values may be enhanced in the future. The results also revealed that the geographic scope of the influence for properties is apparent only within 200-m radius.

1. Introduction

The revitalization of older urban districts and dilapidated areas including contaminated and under-utilized land resources has gained political support across the world as an essential element of the urban regeneration process. Since revitalization is supported by strong economic forces vacant and contaminated land resources reduce the efficiency of the land market, causing inefficient allocation of scarce land resources in the real estate market. This has been proved a major reason for market failure due to negative externalities and information asymmetry (Hara Associates, 2003; Tonin & Turvani, 2014; USEPA, 2006). Another major argument supporting revitalization is the positive externalities that it brings to the neighbourhood. Revitalization helps improve the living environment in the city inhabitants, and enhances the quality of the city life, public safety and the image of the city. Proponents of urban revitalization claim that revitalization brings win-win propositions for all stakeholders involved, as it creates positive externalities beyond the boundaries of each project (Newell, 2009). The rationale for revitalization is “primarily” tied to employment and tax benefits at the project site, as well as “off-site” benefits. The theory of

spillover effects promotes development, simultaneously raising the tax base for the local authorities, while enhancing the financial and aesthetic wellbeing of the cities (Newell, 2009).

Nevertheless, a proper assessment of economic, social and environmental effects of such revitalization efforts is essential as authorities need to identify priorities in order to allocate limited financial resources efficiently among competing needs. One approach to measure the benefits of revitalization projects is to assess the value of revitalization projects and the associated contribution to the property tax base (De Sousa, 2005). Another method popularly used to measure the benefits of revitalization is to evaluate the impact of revitalization on the neighbourhood property values (Simons, 2005; Simons & Saginor, 2006). This approach is considered important as it helps capture spillover effects that revitalization and redevelopment projects often bring to the surrounding community (De Sousa et al., 2009). Not only does revitalization brings positive externalities to the neighbourhood in the form of land and building values improvement for property owners, but it also increases the tax base for authorities.

As revitalization projects benefit the surrounding property owners and the local governments through enhancement of neighbourhood

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property values, the land use implications of revitalization, to a certain extent, is a determining factor affecting the future location of various land uses in the vicinity. However, the degree and the nature of spillover effect or ripple effects of revitalization projects is dependent on the mode of revitalization. The purpose of this study is to measure and compare the effects of the wholesale conversion and redevelopment of industrial buildings projects in Kwun Tong, which was once an industrial hub in Hong Kong. More specifically, the study seeks answers to following questions:

- What is the impact of wholesale conversion of industrial buildings on nearby residential property values?
- What is the impact of redevelopment of industrial buildings on nearby residential property values?
- Do different modes of revitalization (conversion and redevelopment) affect nearby residential property values differently?

The study begins with a discussion of Hong Kong's industrial land use and the associated policies, followed by a brief review of the existing literature, with special reference to externalities related to revitalization. Then follows a theoretical explanation of a Hedonic Price Model (HPM) as applied to residential property development. The penultimate section analyzes the HPM empirical results obtained, while the last section concludes with the research findings and areas for future research. The contribution of the study is two-fold: (a) to the authors' knowledge this is the first study to compare the effects of a redevelopment and wholesale conversion with regard to their influence on nearby properties; (b) the findings of the study will help to reach a consensus among researchers regarding the effects of redevelopment on nearby property values. The findings would enrich the hedonic pricing literature on the effects of redevelopments on property values.

In the study, revitalization is defined as the whole-sale conversion and redevelopment of industrial buildings. Conversion is defined as a change in function or change of use of a building (e.g. convert an office block to a residential use). Redevelopment refers to the process of reconstruction of an existing premises by demolition of the existing structure and construction of a new building.

2. Background: Hong Kong context

Hong Kong's economic structure has undergone remarkable changes since the 1980's due to the relocation of manufacturing industry to Mainland China, which brought significant changes to the Hong Kong's urban spatial structure. This structural change from manufacturing oriented to service oriented has left many industrial buildings vacant or under-utilized. It is reported that 6% of all flatted factories were vacant at the end of 2011 (Rating and Valuation Department, 2012), which is about 1.04 million m² of industrial building (flatted factories).

Recognizing these vacant or under-utilized industrial premises as a waste of limited land resources, the HKSAR government, from time to time, has introduced various policy measures to encourage owners to ensure their efficient utilization. For example, in 2001, with the intention of encouraging revitalization of areas with old industrial buildings, the government introduced a rezoning policy measure. It aimed to rezone around 250 ha of surplus and suitable industrial land for "Other Specified Uses (Business)" (OU(B)) and broaden the permissible uses for industrial buildings compared with the previous decade. Approximately 70% of existing industrial premises are positioned in non-industrial zones, with a majority in "Other Specified Uses" (OU(B)) zones. During 2001-2009, 37 cases of completed lease modifications for change of use were in OU(B) zones. Three of them are in the category of "wholesale conversion". The government introduced another policy in October 2009 (which came into operation on 1 April 2010), known as "*Revitalizing Industrial Buildings Policy*" (RIBP) to further promote and enhance the revitalization of industrial premises. In relation to these premises, this is the most important policy that the

government has introduced. Owing to the land shortage for residential and commercial property developments, as a solution the government expected to increase the supply of suitable land and premises for other uses through this policy. Another important goal of the policy was to make the city brighter and prosperous by creating positive externalities by transforming aged industrial premises into modern sustainable premises (urban regenerating process).

The concept behind the RIBP is that it promotes redevelopment as well as wholesale conversion: it encourages redevelopment in non-industrial zones and wholesale conversion within 'industrial' zones, 'Other Specified Uses (Business)' (OU(B)) and Commercial Zones (Development Bureau, 2010). Under this policy, there are 5 eligibility conditions relating to the wholesale conversion of old industrial premises: (i) industrial buildings have to be 15 years old or more, and situated in "Industrial", "Commercial" or "OU(B)" zones; (ii) an application has to be made with the consent of the owners of all premises in the building; (iii) there should be no increase in the total GFA and no excessive site coverage after the conversion, but continuation of the building height restriction under the planning regime; (iv) the building is not allowed to revert to industrial use during the waiver period; and (v) the full market premium is only payable once the building is fully redeveloped.

All in all, these measures aim at enhancing the revitalization potential (through redevelopment as well as wholesale conversion) in the main non-industrial districts as well as industrial districts (such as Kwun Tong), which in turn are expected to bring significant changes to land use and the urban spatial structure through externalities in the vicinity. These externalities are reflected through the market value of the neighbourhood properties. Generally, it is expected that revitalization brings positive externalities to the nearby properties. It is thus of great importance to examine the externalities (in terms of property prices) due to different types of revitalization project (redevelopment or wholesale conversion) to see if they differ or not. This is the threshold for the study. It has been observed that housing property prices in Kwun Tong increased by more than 100% between April 2009 and January 2013 (Midland Realty, 2013). It is worth examining if this is due to the revitalization of old industrial premises in Kwun Tong.

Although few studies have investigated the effects of redevelopment on nearby property prices (e.g., Chau & Wong, 2012; De Sousa et al., 2009; Weber, Bhatta, & Merriman, 2007), to the authors' knowledge, no comprehensive studies have analyzed and compared the effects of different modes of revitalization, in particular (a) redevelopment, and (b) wholesale conversion, on property values in the neighbourhood. It is important to understand neighbourhood upgrading and value enhancement effects, brought by different modes of revitalization, since one of the main goals of revitalization is to make the city brighter and prosperous by creating positive externalities to society. The findings and tangible benefits identified in this study will help to further refine and motivate the revitalization programme, in general, to bring maximum benefits to society.

2.1. Review of redevelopment and wholesale conversion related to property values

Real property, which is an inherently dynamic, stochastic, multi-dimensional and interdependent entity, is different from other commodities, as its value is not only determined by its own structural features but also the externalities in the vicinity of the property. Hence, revitalization projects can bring important value to the nearby properties even though the definition of revitalization may be different from country to country. Revitalization of aged industrial premises comprises redevelopment and wholesale conversion, according to the Hong Kong Government (HKSAR, 2009). Studies that focus on wholesale conversion are really rare in the literature. The literature review thus primarily aimed at reviewing studies on the effects of redevelopment and their influence on property values.

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