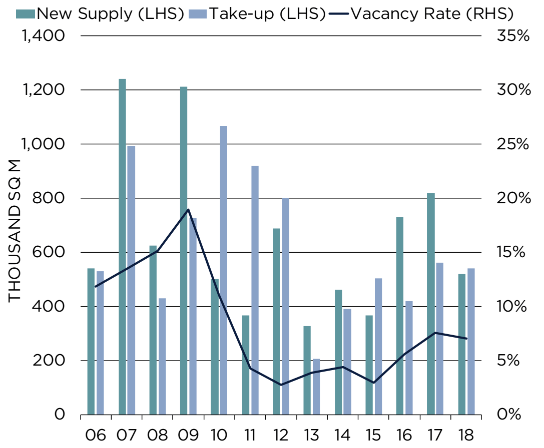
Asian Cities Report – 1H 2019

REPORT
Savills Research

Beijing Office

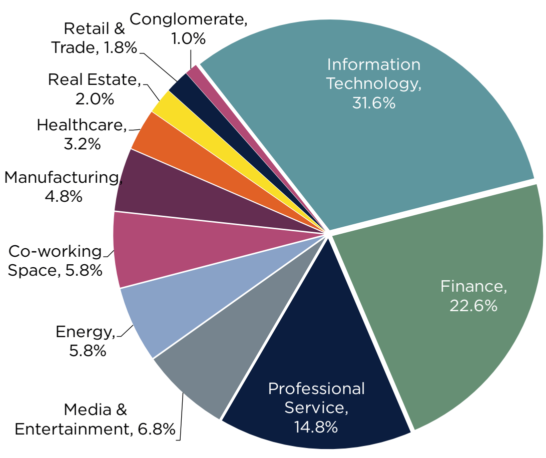
Beijing office market remains active

GRAPH 1: Supply, Net Absorption And Vacancy Rates, 2006 to 2018



Source Savills Research & Consultancy

GRAPH 2: Absorption By Tenant Category, 2018



Source Savills Research & Consultancy

MARKET OVERVIEW

The overall performance of Beijing's office market remained largely stable in 2018. Despite a slowdown in the domestic economy, the office market maintained an upward trend, underpinned by Beijing's strong economic fundamentals as well as steady demand.

A total of 520,037 sq m of new supply was launched during the year, increasing total Grade A office stock by 2.6% year-on-year (YoY) to 11.02 million sq m by the end of 2018.

Information technology, finance and professional services companies were the top three demand drivers for office space, collectively accounting for 69% of total leased area in 2018. Meanwhile, annual net absorption outstripped annual supply, reaching 541,327 sq m , and consequently the city-wide vacancy rate contracted by 0.5 of a percentage point (ppt) YoY to 7.0% by the end of 2018.

SUPPLY

A total of nine new projects were launched during the year, contributing a combined Grade A office supply of 520,037 sq m. Mainly due to postponements in the CBD core plot area, new supply in prime submarkets was absent during the year. All of the city's new projects launched in non-prime submarkets, reflecting the growing trend of decentralisation in the market.

An influx of projects in the CBD core plot area were scheduled to debut in 2018, however these were met with further delays, and opening times have once again been rescheduled. As a result, all prime submarkets experienced an absence of new supply for the entire year. Tenant demand for new leases and expansion requirements were not able to be realised and many companies' leasing strategies remained unfulfilled.

DEMAND

Non-prime business districts, including Wangjing and other areas (including Sanyuanqiao, Andingmen, Chongwenmen and Caishikou), led the largest proportion of annual net absorption in 2018, accounting for 187,000 sq m and 233,000 sq m, respectively. Meanwhile, the emerging market of Lize has started to attract companies, absorbing 8.7% of total leased area during the year. In contrast, prime submarkets—including CBD and its vicinity, BFS and Zhongguancun—were less active and accounted for a mere 2.6%, 1.4% and 1.7% of total absorption, respectively.

The major driving force for office leasing shifted from traditional industries to a variety of burgeoning sectors during 2018. Companies from the information technology sector were the top demand drivers, accounting for 31.6% of annual leased area. The finance and professional services sectors followed in second and third place, accounting for 22.6% and 14.8%, respectively.

TABLE 1: Major Leasing Transactions in Grade A Office Market, 2018

NAME	INDUSTRY	DOMICILE	PROJECT	LOCATION	GFA (SQ M)
Volkswagen	Manufacturing	Foreign	ZRT Plaza	Other (Sanyuanqiao)	34,000
Miss Fresh	Retail & Trade	Domestic	Ronsin Technology Centre	Wangjing	15,000
SenseTime	Information Technology	Domestic	Ideal International Plaza	ZGC	10,500
AIA	Finance	Foreign	Merchant Tower	CBD	10,000
China Bohai Bank	Finance	Domestic	Minsheng Financial Centre	East Chang'an Avenue	8,000
Fun Work	Co-working Space	Domestic	Pangu Plaza	Asia-Olympic	7,500
Renrendai	Finance	Domestic	Phoenix Place	Lufthansa	5,700
Everbright Fund	Finance	Domestic	Fortune Resource International Centre	BFS	4,000
Thyssen Krupp	Manufacturing	Foreign	China Life Tower	East 2nd Ring Road	3,100

Source Savills Research & Consultancy

Traditional industries such as manufacturing, energy and real estate no longer lead the demand race in the market, with their collective demand declining to less than 10% during the year. Meanwhile, the co-working sector continued to show why it cannot be ignored, expanding its market share to 5.8% in 2018.

RENTS

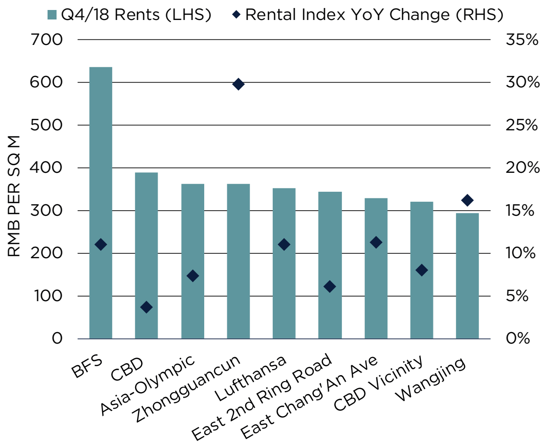
Average rent in the Beijing Grade A office market maintained its position as the most expensive in the nation. Steady demand and quality supply have seen Grade A office average rents increase for six consecutive quarters. The rental index was up 10.9% YoY to RMB369 per sq m per month by the end of 2018.

Prime submarkets such as BFS and ZGC performed positively during the year. Solid demand combined with a limited availability of leasable area in most projects in these precincts saw average rents surge upward by 11.0% and 29.8% YoY, respectively.

An abundance of new supply amid a period of decentralisation in the market has seen Wangjing and Asia-Olympic precincts experience a rapid pace of development in recent years. Robust leasing activity in these precincts pushed up rents by 16.2% and 7.4% YoY, respectively.

The rate of rental growth in CBD slowed in 2018, recording an increase of only 3.7% YoY. This phenomenon can be attributed to a variety of reasons, including a tenant reduction in leasing budgets, growing preference to relocate to non-prime submarkets and leasing strategy uncertainty due to the continued postponement of the CBD core plot area.

GRAPH 3: Beijing Grade A Office Rents And Growth Rates, Q4/2018



Source Savills Research & Consultancyy

> The core tenant base in Beijing's office market has shifted away from traditional sectors to the new tech frontier.

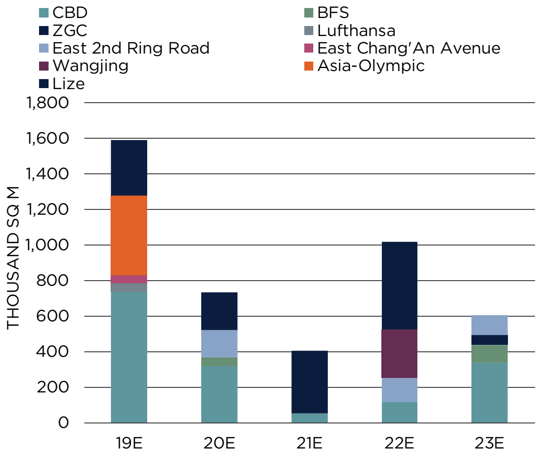
MARKET OUTLOOK

Eleven new office projects are forecast to enter the market in 2019, contributing a combined office GFA of 1.59 million sq m. Most of the future supply will be concentrated in the CBD core area and the Lize financial business district. However, it should be noted that the exact launch time of supply in the CBD core area remains hard to determine. Lize remains in a state of immaturity with ongoing construction, a lack of infrastructure and poor transportation amenities, leaving it still unprepared to welcome the relocation of new companies. The uncertainty of new supply will be the biggest challenge faced by Beijing's office market in 2019.

The finance, information technology and professional services sectors have been the leading drivers for demand for office space in Beijing, accounting for 69% of total leased area in 2018. However, a number of negative influences, such as the global economic slowdown, the US-China trade dispute and a tightening of financial supervision, have seen some companies experience a decline in rental affordability. As a result, it is expected that rental budgets will be reduced in 2019 and overall demand from these sectors will begin to recede in the future.

Both tenants and landlords are increasingly concerned about the slowdown of the economy as well as a softening in market demand. After years of steady growth, Beijing's office market could potentially face a turning point in 2019—overall rental growth is expected to slow down and the willingness of companies to upgrade and relocate their working space will begin to weaken. The rapidly changing market will require both landlords and tenants to be increasingly prepared and responsive in order to deal with the fluctuations and challenges they will face in 2019.

GRAPH 4: Beijing Grade A Office Future Supply, 2019 to 2023



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