Asian Cities Report – 1H 2019

Shanghai Business Park

REPORT
Savills Research

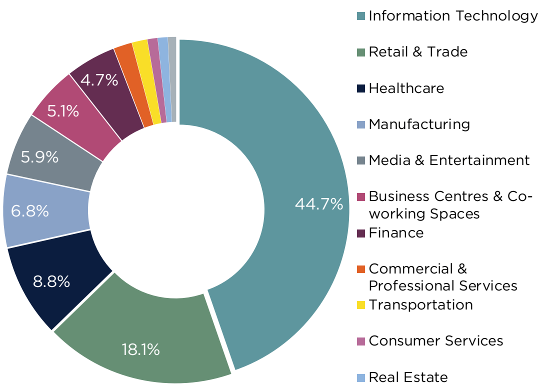
savills 第一太平戴維斯

Rental growth is expected to moderate in 2019

MAP 1: Shanghai Commercial Area

Source Savills Research

GRAPH 1: Shanghai Business Park Take-up By Industry, 2018



Source Savills Research

INTRODUCTION

Shanghai has supported a business park market for 30 years, since the first park, Caohejing, was established as a state-level economic and technological development zone in 1988. The majority of projects developed in Caohejing's first phase were for industrial-related use, and when Jinqiao business park was set up in 1990 and Zhangjiang in 1992, they also focused on industrial properties.

While initially intended for industrial use, business parks started to convert their existing premises and build traditional office buildings in the early 2000s. This move coincided with limited supply and low vacancy rates in the city core Grade A office market (2003-2008), which pushed up rents to a high of RMB8.7 per sq m per day by Q1/2008. At that time, just prior to the GFC, rents in the high zones of better projects reached as high as RMB18 per sq m per day. Limited availability and higher overheads in the core markets forced companies to consider alternative, more affordable locations, whilst infrastructure and amenity improvements, a suburbanising population and lower rents made business parks more attractive.

DEMAND DRIVERS

Rising core rents vs. lower cost business parks: The city's core Grade A office rents stood at RMB9.0 per sq m per day by the end of 2018, whilst business parks were close to half that price at RMB4.8 per sq m per day. Companies seeking to reduce overheads have been tempted to relocate their premises to areas with more affordable rates.

Improving infrastructure: As Shanghai's local government continues to pour money into improving infrastructure (highways and Metro), business parks have become much more connected and accessible than in the past. Key infrastructure has also encouraged the development of decentralised, commercial, transit-oriented developments (TODs).

Improved management: As yields in city centre office stock have reached all-time lows, investors have turned their attention to decentralised assets and business parks, which offer higher returns. The investors also bring in new money to upgrade older facilities and contribute a greater level of professional asset management expertise.

Lower real estate and land costs in these areas have also encouraged development of the social infrastructure — schools, hospitals and rental apartments — compared to some city centre locations. This in turn supports residential communities and complements business parks and commercial TODs.

Bifurcation: As companies continue to grow so do their real estate costs. Some companies that have reached a large scale may decide to relocate back office and non-client-facing functions to more affordable locations, e.g. business parks.

Compared to more centrally located business areas, Shanghai business parks typically offer larger floor plates and built-to-suit options and often have significant industry clustering.

TABLE 1: Selected Investment Deals, 2018

PROJECT	BUSINESS PARK	TOTAL VALUE (RMB MILLION)	ABOVE GROUND GFA (SQ M)	BUYER
L6&L8, City of Elite	Jinqiao	512	24,800	World Union
49% Vi-Hub	Jinqiao	800	79,900	BOCGI
Block 5&7, Caohejing Pujiang Hi-Tech Plaza	Caohejing Pujiang	722	40,100	Phoenix Property
80% Pujiang Yunchuang	Caohejing Pujiang	360	33,100	GLP
Zhangjiang Pharma Valley	Zhangjiang	755	25,600	Starcrest Capital

Source Savills Research & Consultancy

Leasing demand in 2018 was driven mainly by domestic companies, with the information technology, retail and trade sectors accounting for the majority (62.8%) of recorded leases. Demand from co-working operators has been increasing, with notable deals including: WeWork taking up 7,000 sq m of office space in Zhangjiang; and Yoho Space leasing 10,000 sq m in Bay Valley in Yangpu district.

MARKET CONDITIONS

Shanghai had six key business parks, totalling 10.6 million sq m of stock, by the end of 2018. Zhangjiang, the largest submarket, accounts for 26% of stock, followed by Caohejing (24%) and Jinqiao (21%). Together the three business parks are the most mature in the city. Lujiazui Software Park is the only business park located downtown, just south of Zhuyuan, with Lujiazui Properties as the primary developer and landlord. Linkong and Caohejing Pujiang are emerging submarkets with less-developed infrastructure and facilities.

The six business parks received 540,300 sq m of new office supply in 2018, primarily located in Caohejing and Zhangjiang. Despite new projects, the strong net take-up of 497,100 sq m in 2018, especially from the IT and trading sectors, meant that the business park vacancy rate in 2018 fell 0.1 of a percentage point (ppt) to 10.1%. Apart from new leases, existing tenants, especially domestic companies, are also looking to expand their offices—a prime example being Huawei. However, continued economic uncertainties and the ongoing trade dispute with the United States meant that some tenants, especially foreign companies in the manufacturing and trading industries, were more cautious with relocations and expansions.

Rents for the six business parks increased by 0.6% in 2018, averaging RMB4.8 per sq m per day, almost half of the average city core office market rate (RMB9.0 per sq m per day). As the most expensive business park, Lujiazui Software Park's rents stood over 40% higher than the average for the six submarkets. Nevertheless, its central location has limited its development scope to 710,000 sq m.

Capital values for Shanghai's Grade A business park properties are estimated to have increased 2.4% in 2018 to an average of RMB31,900 per sq m. Gross yields fell ten basis points in 2018 to 5.4% (versus 3.23% of ten-year government bond yields), thanks to the strong investment appetite from both domestic and foreign investors.

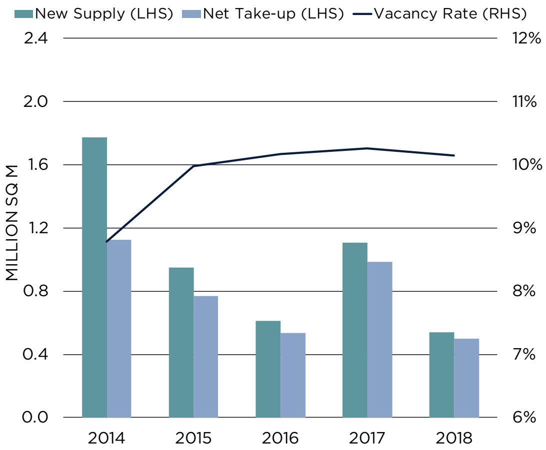
OUTLOOK

The city's six leading business parks are expected to receive 665,000 sq m of new supply in 2019, with the result being vacancy rates are forecast to rise while rental growth is expected to moderate. Professionally managed properties with good accessibility will continue to outperform, recording high occupancy rates and lower tenant turnover.

Whilst the strongest demand will still come from domestic firms, China has eased foreign-ownership restrictions and encouraged foreign direct investment in order to offset the slowing domestic economy. These steps will lend some support to China's office market as well as the business park market in Shanghai.

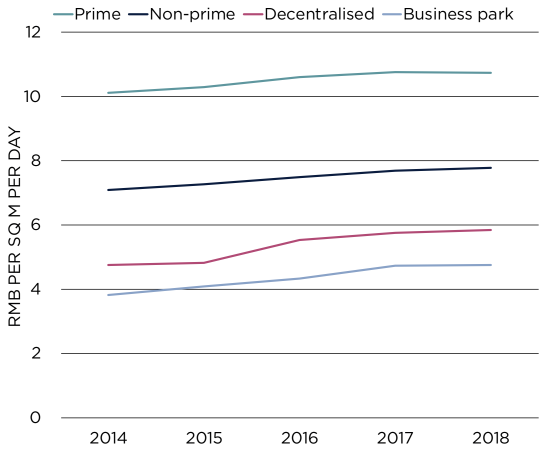
"Shanghai business parks witness rising demand from co-working operators."

GRAPH 2: Supply, Net Take-up And Vacancy, 2014 to 2018



Source Savills Research

GRAPH 3: Shanghai Office Rental Comparison, 2014 to 2018



Source Savills Research

Savills Shanghai
25/F Two ICC
No. 288 South Shaanxi Road
Shanghai 200031, China
+86 21 6391 6688