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Savills World Research
Beijing

Briefing
Office sector

April 2014

Image: Kerry Centre, CBD, Chaoyang district

SUMMARY

The rate of rental decline slowed to the lowest level in the past four quarters, supported by a shortage of new supply. Meanwhile, city-wide vacancy rates fell as space was digested in recently launched projects.

- Grade A office stock stabilised at 9.34 million sq m as no new projects were handed over in the first quarter. However, three projects have achieved relatively high pre-commitment rates and are scheduled to enter the market in the coming three months.

- Net take-up totalled 54,000 sq m in Q1/2014, almost equivalent to that in the previous quarter and the whole year of 2013, although demand is still focused on relocations and renewals.

- City-wide vacancy rates fell by 0.5 of a percentage point quarter-on-quarter (QoQ) to 3.9%, up 1.2 percentage points (ppts) year-on-year (YoY), as vacant space in two recently launched projects was further absorbed.

- Grade A office effective rents fell for the fourth consecutive quarter by 0.4% QoQ to an average of RMB311.5 per sq m per month, representing a YoY decline of 2.4%.

- The Grade A office market is expected to welcome eight projects this year, with a total leasable office GFA of 484,000 sq m, less than a half of which will be located in prime areas. Overall rents are predicted to dip by 0% to 2% by the end of 2014, with city-wide vacancy rates to rise to 5% to 7%.

"Grade A office rents are expected to largely remain stable in the short term, supported by relatively limited supply in prime areas." Joan Wang, Savills Research

Supply, net take-up and vacancy rate

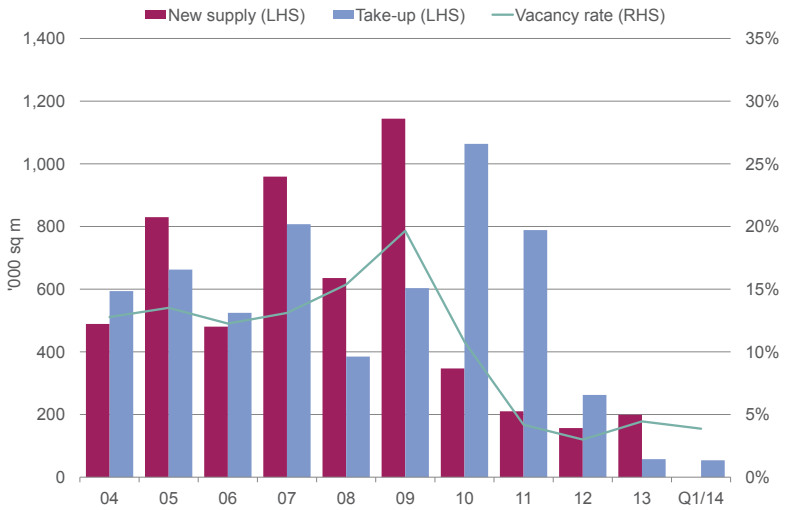
Beijing's Grade A office leasable stock stabilised at 9.34 million sq m by the end of Q1/2014, as no new projects were handed over in the first quarter. Three projects, namely ZGC Internet Financial Centre located in Zhongguancun area (ZGC) and Ocean International Centre Phase II (Towers 1 and 2) situated in the CBD vicinity, postponed their handover dates to the second quarter, despite having attracted several quality tenants from projects in the vicinity and consequently recording healthy pre-leasing rates.

Despite a relatively low level of enquires resulting from the traditional slow season around Chinese New Year, leasing transactions were largely stable, with several large-size leases concluded in the first quarter. As a result, net take-up reached 54,000 sq m in Q1/2014, almost equivalent to that in the previous quarter, when the market welcomed a sizable new project, and that of the whole year of 2013. Leasing activity is still focused on relocations and renewals, with relatively weak demand from new set-ups and expansions compared with that between 2010 and 2012.

GRAPH 1

Supply, net take-up and vacancy rate, 2004–Q1/2014

Net take-up was almost equivalent to last year's total.



Source: Savills Research

TABLE 1

Grade A office leasing market key indicators, Q1/2014

	Stock (sq m)	Vacancy rate (%)	Take-up (sq m)	Supply (sq m)	Rent (RMB per sq m per month)
Q1/2014	9,335,000	3.9	54,000	-	311.5
QoQ change (%/ppts)	-	-0.5	-	-	-0.4
YoY change (%/ppts)	+2.2	+1.2	+80.9	-	-2.4

Source: Savills Research

TABLE 2

Major leasing transactions, Q1/2014

Company	Building	Location	GFA (sq m)	GFA (sq m)
Construction Investment Bank	Minsheng Financial Centre	East Chang'an Avenue	20,000	New lease
Qualcomm	Global Trade Centre	North Third Ring Road	18,000	New lease
Samsung Electronics	Fortune Financial Centre	CBD	17,000	New lease
Xinhuanet.com	China Overseas Property Plaza	South Second Ring Road	16,000	New lease
MoMo	SOHO Peaks Tower 2	Wangjing	5,700	New lease
BMW	Ping'an International Financial Centre	Lufthansa	4,000	New lease
Acer	ECO Plaza	Wangjing	4,000	Renewal
AIA	International Financial Centre	CBD	3,200	Renewal
SHEISEIDO	Landgent Centre	CBD vicinity	2,600	New lease
CFLD	Gateway Plaza	Lufthansa	2,200	New lease

Source: Savills Research

In Q1, financial, IT and high-tech, professional services, conglomerates, and media and cultural companies were the major demand drivers, collectively accounting for over 70% of recorded transactions. Domestic enterprises continued to take the lion's share of demand, accounting for 70% of recorded transactions. In contrast, demand from overseas companies was relatively weak due to their tightened rental budgets combined with conservative expansion plans with regards to headcount and office space.

The city-wide vacancy rate decreased by 0.5 of a ppt QoQ to 3.9%, representing YoY growth of 1.2 ppts, still the lowest level nationwide. This was largely due to vacant space in projects launched in the last 12 months, including Fortune Financial Centre and World Profit Centre, being

gradually digested. Over 80% of Grade A office buildings currently boast high occupancies of over 95%.

Rent

Grade A office effective rents fell for the fourth consecutive quarter to RMB311.5 per sq m per month by the end of Q1/2014, representing QoQ and YoY declines of 0.4% and 2.4% respectively, still the highest level in mainland China. However, rental decline was further compressed by 0.2 of a ppt, with overall demand tending to stabilise after landlords' rental adjustments over the past few quarters, combined with limited leasable space across the board.

Eastern markets[1] continued to witness moderate rental declines in every submarket, with the two oldest business districts in the locality, namely East Chang'an Avenue and Lufthansa, recording the largest falls of 2.3% and 0.8% respectively. This was largely due to most landlords having to offer rental discounts to secure high occupancies by retaining existing tenants and competing for new clients. In contrast, western market[2] rents remained stable, with Beijing Financial Street (BFS) and ZGC registering rental growth of 0.1% and 0.3% respectively.

1 Eastern markets include the CBD, CBD vicinity, Lufthansa, East Second Ring Road and East Chang'an Avenue.

Submarket rents and vacancy rates

Traditional business districts

Given that vacant space was absorbed in Fortune Financial Centre, which was handed over in the previous quarter, CBD vacancy rates fell by 1.4 ppts QoQ to 5.6%, representing a YoY increase of 3.5 ppts. Meanwhile, CBD rents continued to drop by 0.6% QoQ to RMB353.2 per sq m per month, the smallest decline over the past five quarters. With Guanghualu SOHO 2, located in the CBD area, and Ocean International Centre Phase II (Towers 1 and 2), situated in the CBD vicinity, scheduled for handover within the coming nine months, the majority of landlords of existing projects in the CBD either maintained the same rental offerings as the previous quarter or lowered rents to retain and compete for tenants.

2 Western markets include BFS and ZGC.

BFS continued to witness the highest rents and occupancy rates in the city, due to stable demand from domestic financial companies as well as a continuous shortage of supply. Considering that Q1 is the traditional slow season in the leasing market, combined with the majority of landlords maintaining rents and with Jinshifang Street No. 7 Project (BFS E9) kicking off pre-leasing activity before its handover in the third quarter, BFS rents largely

TABLE 3

Future supply, 2014

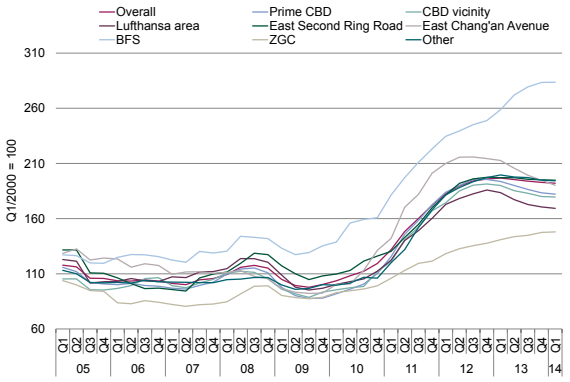
Project	Completion	Submarket	Leasable office space (sq m)	Self-use space (sq m)
ZGC Internet Financial Centre 中关村互联网金融中心	Q2	ZGC	51,000	-
Ocean International Centre II Tower 1 远洋国际中心二期1座	Q2	CBD vicinity	33,000	-
Ocean International Centre II Tower 2 远洋国际中心二期2座	Q2	CBD vicinity	22,000	-
Jinshifang Street No. 7 Project (BFS E9) 锦什坊街柒号项目(金融街E9)	Q3	BFS	59,000	
Posco Centre 浦项中心	Q4	Wangjing	74,000	15,000
Raycom Infotech Park – Tower B 融科资讯中心B座	Q4	ZGC	58,000	
SOHO Peaks Tower 3 银峰SOHO3座	Q4	Wangjing	124,000	
Guanghualu SOHO II 光华路SOHO2号	Q4	CBD	63,000	

Source: Savills Research

GRAPH 2

Grade A office rental indices, Q1/2005–Q1/2014

Rents continued to fall, although the rate of decline slowed.

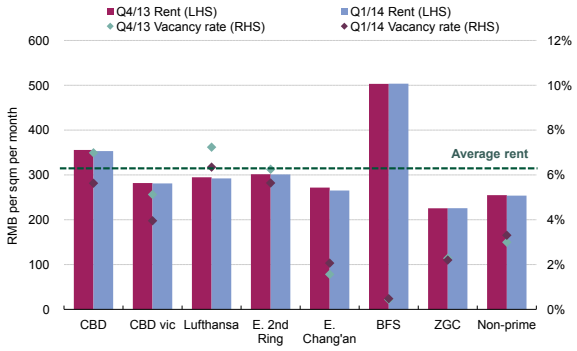


Source: Savills Research

GRAPH 3

Submarket rents and vacancy rates, Q4/2013 vs Q1/2014

Most submarkets witnessed stable or improved occupancies.



Source: Savills Research

stabilised at RMB503.6 per sq m per month, up 9.7% YoY, while vacancy rates rose by 0.1 of a ppt to 0.5%.

ZGC rents surpassed Wangjing rents, growing by 0.3% QoQ to an average of RMB225.7 per sq m per month, representing a YoY appreciation of 5.0%. This was largely supported by the positive performance of the IT and high-tech sector, and the recently booming internet-finance industries. Meanwhile, vacancy rates fell by 0.1 ppt QoQ to 2.2%, the third lowest in the city following BFS and East Chang'an Avenue.

Non-prime markets[3]

With the majority of landlords of projects located in traditional business districts in eastern markets lowering rents to combat slowing demand, non-prime markets saw rents decline by 0.2% QoQ to an average of RMB253.7 per sq m per month, down 2.6% YoY. Meanwhile, non-prime market vacancy rates rose by 0.3 of a ppt QoQ to 3.3%, representing YoY growth of 0.8 of a ppt. However, non-prime areas continued to attract companies, particularly those from the IT and high-tech, telecom, and media and cultural sectors, to relocate, considering a 4% to 28% rental discount from traditional business districts in eastern markets. This was evidenced by American telecom giant Qualcomm relocating to North Third Ring Road from the CBD by committing to 18,000 sq m in Global Trade Centre.

Two projects, namely SOHO Peaks Towers 1 to 3 (with Towers 1 and 2 on the strata-title market and Tower 3 held by the landlord) and Posco Centre located in Wangjing area have kicked off pre-leasing activities and are expected to be handed over within the next three quarters, bringing total leasable office GFA of over 400,000 sq m to the market. This large amount of new supply in the pipeline, combined with decreased rents in traditional business districts such as the CBD and Lufthansa over the past four quarters, forced the majority of landlords in Wangjing to offer rental discounts in face rents, as well as provide longer rent-free periods to retain tenants and compete for new clients.

As a result, Wangjing witnessed declines in both rents and occupancy rates in the first quarter. Rents decreased for the second consecutive quarter by a further 1.8% QoQ to RMB224.6 per sq m per month, representing a YoY decline of 1.6%. Meanwhile, vacancy rates rose by 1.1 ppts QoQ to 2.6%, representing YoY growth of 2.1 ppts, the highest level over the past seven quarters.

3 Non-prime markets include Wangjing, Asian Games Village, North Third Ring Road, South Second Ring Road, etc.

TABLE 4

Ocean International Centre Phase II (Towers 1 and 2)

Location	East Fourth Ring Middle Road 58, Chaoyang district
Owner	Sino-Ocean Land Limited
Office GFA (sq m)	Tower 1: 33,000 Tower 2: 22,000
No. of storeys	Tower 1: 24 Tower 2: 11
Floorplate (sq m)	Tower 1: 1,392 Tower 2: 2,032
Whole-floor efficiency	70%
Ceiling height (m)	2.8
Raised floor (mm)	100
Passenger lifts	12
Car park	412
Asking rent	RMB400 per sq m per month
Management fee	RMB30 per sq m per month

Source: Savills Research & Consultancy

OUTLOOK

Western market rents are expected to stabilise, while eastern market rents will continue to fall due to predicted rising vacancies.

■ In the next three quarters, Beijing's Grade A office market is expected to see a pick-up in supply, with eight projects scheduled to be handed over, with total leasable office GFA of 484,000 sq m, enlarging total stock by 5.2%. Two of the new projects, namely Raycom Infotech Park – Tower B located in ZGC and Posco Centre located in Wangjing area, are positioned as international Grade A office buildings and are expected to further upgrade the ZGC and Wangjing office markets by completion. Just 48% of the new supply will be located in prime business areas including the CBD, BFS and ZGC.

■ The limited space situation in Beijing's western markets should ease, as approximately one-third of new supply will be located in BFS and ZGC, enabling stable rents and low vacancy rates of less than 5%. However, eastern market rents are expected to further decrease by 1% to 2%, as rising vacancies intensify market competition, given the weak demand in terms of expansions and new set-ups. As a result, overall Grade A effective rents are predicted to drop by 0% to 2% by the end of 2014, with city-wide vacancy rates rising to 5% to 7%.

■ Given the high level of net take-up of nearly 0.8 million sq m in 2011, when the market witnessed strong demand, many leases will expire successively in 2014 under a typical three-year lease-term. However, as most leases were signed with relatively high rents in 2011 (compared with those signed in between 2009 and 2010), a smaller gap between renewal and new-lease rents is expected, leading to a further slowing in the rate of rental decline in the coming three quarters.

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