savills
第一太平戴维斯

Savills World Research
Beijing

Briefing
Office sector

July 2014

Image: SOHO Peaks, Wangjing, Chaoyang district

SUMMARY

Overall demand rebounded after a slowdown over the past five quarters, resulting in rents appreciating for the first time since Q2/2013 and vacancies compressing further.

- Only one new project was handed over in the second quarter of 2014, adding an office GFA of 56,000 sq m to the market and enlarging Grade A office leasable stock to 9.4 million sq m, still the largest in mainland China.

- Net take-up jumped to 87,000 sq m from 54,000 sq m in the previous quarter, the highest level over the past eight quarters, and accumulated to 141,000 sq m in the first half of 2014, nearly 2.5 times that of FY2013.

- Supported by the positive net absorption, city-wide vacancy rates dropped a further 0.4 of a percentage point (ppt) quarter-on-quarter (QoQ) to 3.5%, still the lowest level in the country, despite the new supply.

- After consecutive declines over the past four quarters, rents rose 1.1% QoQ to RMB314.7 per sq m per month by the end of Q2/2014.

- Six projects are scheduled for handover in the second half of 2014, offering a total leasable office GFA of 428,000 sq m to the market. City-wide vacancy rates, however, are expected to rise to around 5%. Overall rents are predicted to remain stable given promising pre-leasing rates in most new projects, combined with growing demand.

"Supported by an active leasing market and one new building launched this quarter, net take-up witnessed its highest level since Q2/2012." Joan Wang, Savills Research

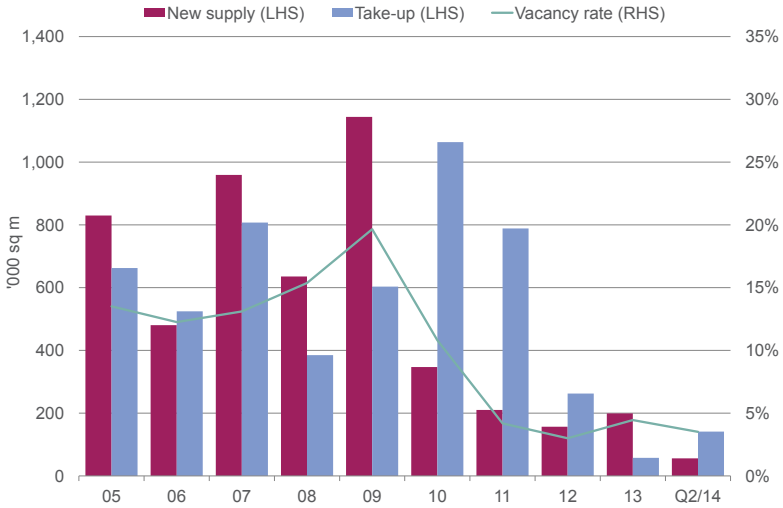
Supply, net take-up and vacancy rate

In the second quarter, the Grade A office market welcomed its first new supply of 2014, with the handover of the 56,000-sq m Ocean International Centre Phase II (Towers 1 and 2). As a result, leasable Grade A office space expanded to around 9.4 million sq m, still the largest market in mainland China.

Located in the CBD vicinity, Ocean International Centre II (Towers 1 and 2) was handed over at the end of June. This project also has an 18,000-sq m shopping mall component occupied by a series of fashion, F&B, lifestyle, healthy and beauty, and services retailers. By the end of this quarter, Ocean International Centre II had achieved a positive occupancy rate as one tower was entirely occupied by CGGC Group, a leased area of nearly 20,000 sq m.

GRAPH 1

Supply, net take-up and vacancy rate, 2005–Q2/2014



Source: Savills Research

TABLE 1

Grade A office leasing market key indicators, Q2/2014

	Stock (sq m)	Vacancy rate (%)	Take-up (sq m)	Supply (sq m)	Rent (RMB per sq m per month)
Q2/2014	9,391,000	3.5	87,000	56,000	314.7
QoQ change (%/ppts)	+0.6	-0.4	+62.5	-	+1.1
YoY change (%/ppts)	+2.8	+0.8	-	-	-0.7

Source: Savills Research

TABLE 2

New supply – 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: 34,000 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
Major tenants	CGGC Group, PPTV

Source: Savills Research

Evidenced by the pre-commitment levels of the aforementioned new supply, overall demand has rebounded this quarter, bringing both active leasing enquires and transactions. Net take-up rose significantly to 87,000 sq m, up from 54,000 sq m, to the highest level over the past eight quarters. Total take-up reached 141,000 sq m in the first half of 2014, nearly 2.5 times that of FY2013. Largely due to the absorbed space in Ocean International Centre II, the CBD vicinity registered the highest net take-up of 40,000 sq m, followed by the CBD with 20,000 sq m.

Financial, IT and high-tech, and media and cultural companies maintained steady demand in the city, collectively responsible for nearly 60% of the recorded transactions, of which insurance, investment companies and funds were the strongest demand drivers. Meanwhile, echoing a promising market performance, e-commerce enterprises showed greater appetite in expansion by completing 16% of the recorded transactions, with representative deals including JD.com's commitment of approximately 20,000 sq m in Zhaolin Plaza, located in BDA.

Domestic enterprises continued to dominate market demand, responsible for 87% of the recorded transactions, while demand from overseas companies has been rather fragile in the past few quarters due to their tightened budgets for both office rents and headcount.

Despite the new supply, positive net absorption led to city-wide vacancy rates declining by a further 0.4 of a ppt QoQ to 3.5%, still the lowest level in the country. Overall, 80% of Grade A office buildings boasted occupancy rates of over 95% in Q2/2014. Lufthansa witnessed the largest fall in vacancy rates, dropping 1.2 ppts to 5.1%, largely a result of World Profit Centre, which launched in Q3/2013, welcoming new anchor tenants with large office space requirements. Additionally, CBD vacancy rates fell by 0.8 of a ppt QoQ to 4.8%.

Rents

After consecutive declines over the past four quarters, rents rose 1.1% QoQ to RMB314.7 per sq m per month by the end of Q2/2014. Rising demand combined with limited leasable area in the majority of projects reinforced landlords' bargaining power, allowing overall rents to grow as a result.

East Chang'An Avenue registered the largest rental appreciation of 3.0%, largely due to the improved performance of one project – Oriental Plaza. Meanwhile, remaining a priority location for the relocation, renewal or first offices of many overseas and domestic enterprises, CBD rents rose by 1.4% QoQ after consecutive declines in the past five quarters. The Lufthansa area was the only exception, and saw a 1.1% drop despite improved occupancy rates. This was mainly the result of overseas companies with tightened rental budgets accounting for a larger share of tenant profile than any other submarket.

Submarket rents and vacancy rates

Traditional business districts

In the second quarter, the CBD performed well in all three key indicators: rental growth, vacancy rate and net take-up, as this is still the priority location for many enterprises, particularly overseas companies and private companies planning to expand or upgrade their office premises. This submarket witnessed active demand, allowing rental rates to appreciate by 1.4% QoQ to RMB358.5 per sq m per month, the first growth in the past six quarters, and net take-up to record 20,000 sq m, the second highest of all submarkets. Additionally, with the vacant space of one recently launched project further digested and occupancy rates of other projects largely remaining stable, CBD vacancy rates dropped by a further 0.8 of ppt to 4.8%. Domestic financial and overseas professional services companies were the strongest demand drivers in the CBD area.

Beijing Financial Street (BFS) continued to outperform in the overall market by commanding the highest rents and occupancy rates in the city. Despite one new project, Dreamsfount 35th (BFS E9 project), kicking off pre-leasing activities and scheduled for handover in the fourth quarter, current landlords were still able to maintain their negotiation power, with strong demand

TABLE 3

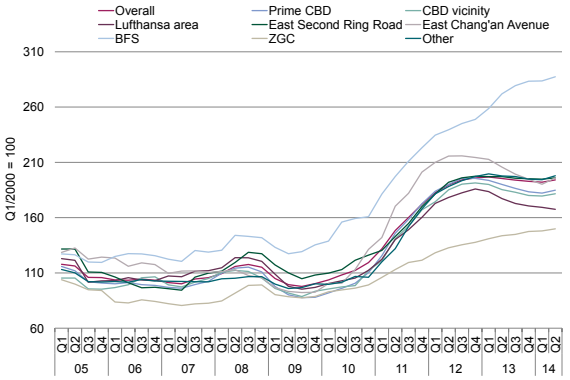
Major leasing transactions, Q2/2014

Company	Building	Location	GFA (sq m)	New lease/ renewal
Chukong Technology	SOHO Peaks Tower 3	Wangjing	24,000	New lease
JD.com	Zhaolin Plaza	Other	20,000	New lease
Creditease	Fosun International Center	CBD vicinity	8,600	New lease
IDG Capital Partners	COFCO Plaza	East Chang'An Avenue	5,000	Renewal
Sunshine Insurance Group	World Finance Centre	CBD	4,400	New lease
Focus Media	The Marchant Tower	CBD	4,000	Renewal
BSB	Eagle Run Plaza	Lufthansa	3,600	New lease
58.com	Guancheng Plaza	Lufthansa	2,700	Renewal
PPTV	Ocean International Centre II	CBD vicinity	2,700	New lease
Eisai	SK Tower	CBD	1,700	Renewal

Source: Savills Research

GRAPH 2

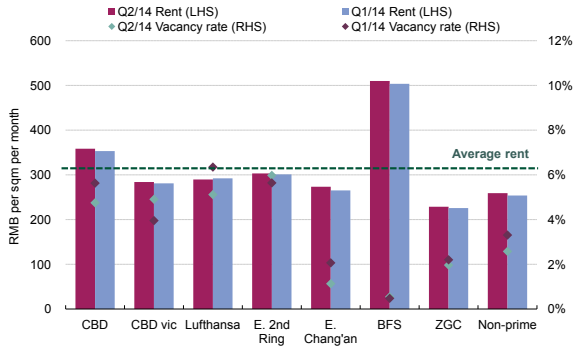
Grade A office rental indices, Q1/2005–Q2/2014



Source: Savills Research

GRAPH 3

Submarket rents and vacancy rates, Q1/2014 vs Q2/2014



Source: Savills Research

TABLE 4

Future project focus

Project name	Raycom Infotech Park (Tower B)	Dreamsfount 35th (BFS E9 project)
		
Location	2 Kexueyuan South Road, Haidian district	West Second Road, Xicheng district
Owner	Raycom	Sasac
Office GFA (sq m)	58,000	58,500
No. of storeys	18	12
Floorplate (sq m)	3,150	5,000
Whole-floor efficiency (%)	72	70
Ceiling height (m)	2.8	2.8
Raised floor (mm)	144	150
Passenger lifts	18	12 +2 VIP
Car park	400	270
Asking rent	RMB480 per sq m per month	RMB650–700 per sq m per month
Management fee	RMB33 per sq m per month	RMB34 per sq m per month

Source: Savills Research & Consultancy

TABLE 5

Future supply, 2H/2014

Project	Completion	Submarket	Leasable office space (sq m)	Self-use space
Dreamsfount 35th 锦什坊街叁拾伍号	Q4	BFS	58,000	-
ZGC Internet Financial Centre 中关村互联网金融中心	Q4	ZGC	51,000	-
Raycom Infotech Park – Tower B 融科资讯中心B座	Q4	ZGC	58,000	-
Posco Centre 浦项中心	Q4	Wangjing	74,000	15,000
SOHO Peaks Tower 3 锦银峰SOHO3座	Q4	Wangjing	123,000	-
Guanghualu SOHO II 光华路SOHO2号	Q4	CBD	63,000	-

Source: Savills Research

for new leases and long waiting lists for renewals. As a result, rents continued to appreciate by 1.3% QoQ to RMB510.0 per sq m per month, up 5.7% year-on-year (YoY). Average vacancy rates for the area hovered at 0.5%, the lowest among any submarket.

Supported by strong demand from the flourishing IT and high-tech industry, combined with no new supply during the past four and a half years, Zhongguancun (ZGC) rents appreciated by 1.3% QoQ and 4.4% YoY to RMB228.8 per sq m per month. Vacancy rates, however, continued to fall by 0.2 of a ppt to 2.0%. ZGC rental rates were the lowest of any submarket mostly due to the clustering of IT companies and education institutes, all of which have much lower affordability compared with financial and professional services companies. Some prime projects in this area are keen to introduce finance-related enterprises, especially given the synergy between finance, internet and professional services companies in relation to technology solutions. Additionally, this submarket is expected to welcome its first batch of new supply since 2010 in the coming six months, with the completion of ZGC Internet Financial Centre and Raycom Infotech Park – Tower B.

Non-prime markets

Despite financial and professional services companies remaining keen on traditional business districts, many manufacturing, IT and high-tech, e-commerce, and media and cultural enterprises with weaker affordability and stronger consolidation demand continued to look for cost-advantageous office premises in non-prime markets, such as the Asian & Olympics, North Third Ring Road and Wangjing areas, consequently leading to a rebound in performance for non-prime markets this quarter. By the end Q2/2014, after consecutive declines over the past four quarters, non-prime market rents rose 1.9% QoQ to an average of RMB259.0 per sq m per month while vacancy rates decreased by 0.7 of a ppt QoQ to 2.6%, the lowest level since Q1/2013.

Except for limited prime projects such as Pangu Plaza in Asian & Olympics and Global Trade Centre in the North Third Ring Road area, office buildings located in Wangjing were the most sought-after. Stand-out deals this quarter include Tesla, an American luxury electric automobile manufacturing company, which leased approximately 2,100 sq m in UBP and Chukong Technology, which committed to 24,000 sq m in SOHO Peaks (Tower 3). As a result, Wangjing rents rose 1.7% QoQ to RMB228.7 per sq m per month, remaining down 2.2% YoY, while vacancy rates dropped by 0.2 of a ppt QoQ to 2.4%.

Wangjing will welcome its first international Grade A office building – Posco Centre – in the second half of the year. Additionally, a total of around 0.6 million sq m of new supply (including Grade B projects) is scheduled to be launched over the next year and a half, more than current stock. Although overall rents and occupancy rates are expected to decline in the short term due to the difficulty of absorbing such a substantial amount of supply, Wangjing will accelerate its transition into a mature/Grade A business district from emerging/Grade B market with the completion of these projects. The outlook for this area in the mid to long term, however, looks optimistic due to its easy access to the airport and the government's plan to make it another CBD. This plan is hoping to attract several international enterprises, including companies in the IT, high-tech and manufacturing related industries, to set up headquarters in the area.

Market outlook

In the second half of 2014, the Grade A office market is expected to see a surge in supply, with six projects scheduled for handover, adding a total leasable office GFA of 428,000 sq m to the market. This should ease the undersupply situation the city has witnessed over the past three years when supply averaged only 189,000 sq m. Additionally, the market is expected to welcome another upgrade with the completion of two international Grade A office buildings, namely Raycom Infotech Park – Tower B located in ZGC and Posco Centre situated in Wangjing.

New supply in core business districts including the CBD, ZGC and BFS, however, continues to be limited as only around half of the new supply, 230,000 sq m, will be located in such areas. Considering that core business areas are still the priority locations for expected growing demand, the new supply should be quickly absorbed, leading to vacancy rates in these areas remaining stable. As a result, landlords of prime business districts are expected to continue to hold a stronger bargaining power than tenants, allowing rents to largely stabilise in the second half of the year.

Growing demand (although not as strong as that between 2010 and 2012) was reflected in the pre-leasing activities at the majority of new supply in the 2014 pipeline, such as ZGC Internet Financial Centre and Raycom Infotech Park – Tower B located in ZGC and SOHO Peaks Tower in Wangjing. Pre-commitment rates for these projects range from 20% to 50%. Consequently, city-wide vacancy rates are expected to witness only a moderate rise to around 5%, still the lowest level in mainland China. Overall rents are expected to remain flat at the current high level until the market witnesses another supply peak after 2015.

Please contact us for further information

Savills Research

James Macdonald
Director, China
+8621 6391 6688
james.macdonald@savills.com.cn

Savills Beijing Research & Consultancy

Joan Wang
Director
+8610 5925 2042
joan.wang@savills.com.cn

Savills Commerical

Anthony McQuade
Senior Director
+8610 5925 2002
anthony.mcquade@savills.com.cn

Gary Wen
Senior Director
+8610 5925 2064
gary.wen@savills.com.cn