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Savills World Research
Beijing

Briefing
Office sector

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Image: The Genesis, Lufthansa, Chaoyang district

SUMMARY

Faced with slowing demand, landlords have been under increasing pressure to offer more competitive rents and discounts in order to retain high quality tenants and achieve healthy occupancy rates.

- Four new projects entered the Grade A office market in the second quarter of 2016, contributing a total office GFA of 306,000 sq m.
- The overall vacancy rate increased by 1.2 percentage points (ppts) to 4.4% during the period (including self-use office space).
- Grade A office rents were down 0.7% quarter-on-quarter (QoQ) to RMB337.8 per sq m per month by the end of Q2/2016.
- The remainder of 2016 will see the Grade A office market receive six new projects, with a combined office GFA of approximately 350,000 sq m. The distribution of new supply, combined with slowing demand, is expected to place downward pressure on occupancy rates in the short term.

"With several high-quality projects entering the non-prime market, the gap between traditional business districts and non-prime areas is expected to continue to narrow. Lower rents and more flexibility in rental agreements will see non-prime areas continue to grow in attractiveness." Jack Xiong, Savills Research & Consultancy

Supply, net take-up and vacancy rate

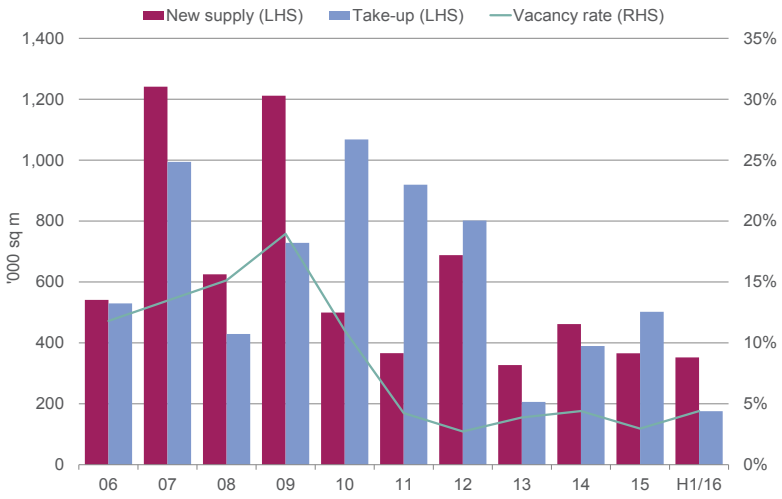
Four new projects entered the Grade A office market in the second quarter of 2016, contributing a total office GFA of 306,000 sq m. This pushed Grade A office stock up to approximately 9.5 million sq m (including self-use office GFA) by the end of Q2/2016.

The overall vacancy rate increased by 1.2 ppts to 4.4% during the period (including self-use office GFA). This was largely the result of a significant influx of supply combined with slowing demand which placed downward pressure on absorption levels. This was further exacerbated by the majority of new supply during the quarter entering the leasing market, with only Alibaba Headquarters positioned for self-use. In addition to this, the leasing market continues to be battered by the instability of financial companies, where early lease terminations continue to see falling occupancy rates in some projects.

Demand from newly developing industries such as the niche financial, 'internet plus' and co-working space sectors remains strong, albeit instable. In response to this, landlords have looked to mitigate their risk by requesting higher rents and deposits, or by simply refusing to lease space out to these companies.

GRAPH 1

Supply, net take-up and vacancy rate, 2006–Q2/2016



Source: Savills Research & Consultancy

TABLE 1

New supply, Q2/2016

Project Name EN	Project Name CN	Location	Grade	Office GFA (sq m)
Alibaba Headquarter	阿里巴巴总部大厦	Wangjing	Grade A	54,000
LSH Centre - Tower A	利星行中心A座	Wangjing	Grade A	92,000
The Genesis	启皓北京	Lufthansa	Grade A	100,000
Tianyuan Xiangtai Plaza	天圆祥泰大厦	Asia-Olympic	Grade A	60,000

Source: Savills Research & Consultancy

TABLE 2

Major leasing transactions, Q2/2016

Company	Industry	Nationality	Project	Location	GFA (sq m)
Polycom	IT& High-tech	Overseas	Ping An IFC	Lufthansa	6,800
Stago	Bio-tech & Pharmaceutical	Overseas	Guancheng Building	Lufthansa	2,700
Credit Harmony	Finance	Domestic	Tsinghua Tongfang Square	ZGC	2,500
ACIFI	Other	Domestic	IFC	CBD	1,100
Linktop Technology	IT & High-tech	Domestic	Parkview Green	CBD	1,100

Source: Savills Research & Consultancy

By comparison, demand from bio-tech and pharmaceutical and cultural companies remains relatively stable.

Rents

Grade A office rents were down 0.7% QoQ to RMB337.8 per sq m per month by the end of Q2/2016. In the face of slowing demand, landlords have been pressured to offer more competitive rental discounts to achieve healthy occupancy rates. A general hesitance towards accepting newly launched financial companies into their projects has seen landlords increasingly view tenants of traditional industries in a favourable light and extend rental discounts accordingly.

Submarket rents and vacancy rates

Traditional business districts

Supported by stable demand, vacancy rates in western areas remained low by the end of Q2/2016, with those in Beijing Financial Street (BFS) and Zhongguancun (ZGC) falling to 1.0% and 1.8%, respectively. Meanwhile, average rents in these areas increased to RMB544.1 and RMB274.8 per sq m, respectively.

Due to slow demand and an influx of supply in non-prime markets, vacancy rates in eastern areas increased in the second quarter. The change was particularly prominent in the Lufthansa area, with new supply pushing vacancy rates up by 4.9 ppts to 7.7%.

Non-prime markets

The opening of Tianyuan Xiangtai Plaza this quarter, combined with the imminent launch of New Times Square, has seen the Asia-Olympic area continue to mature. However, the area will still require time to digest the new supply.

In recent years, Wangjing has continued to emerge as an attractive location for IT and high-tech, high-end manufacturing and e-commerce companies. This growth has been largely fuelled by an influx of high quality buildings, a rich business environment and competitive rental levels. Alibaba opened Alibaba Headquarters in Q2, a move which is expected to help the market further mature. LSH Centre – Tower A also came onto the leasing market. The project achieved a high occupancy rate and secured noteworthy tenants, including Mercedes Benz and Hewlett-Packard.

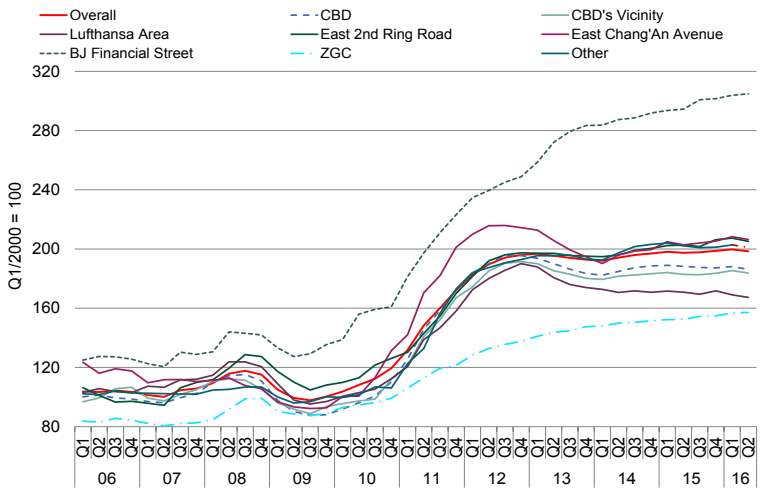
Market outlook

The remainder of 2016 will see the Grade A office market receive six new projects, with a combined office GFA of approximately 350,000 sq m. As a result, the market is expected to come under greater pressure to digest the new stock.

The gap between traditional business districts and non-prime areas is expected to continue to narrow, as non-prime areas grow

GRAPH 2

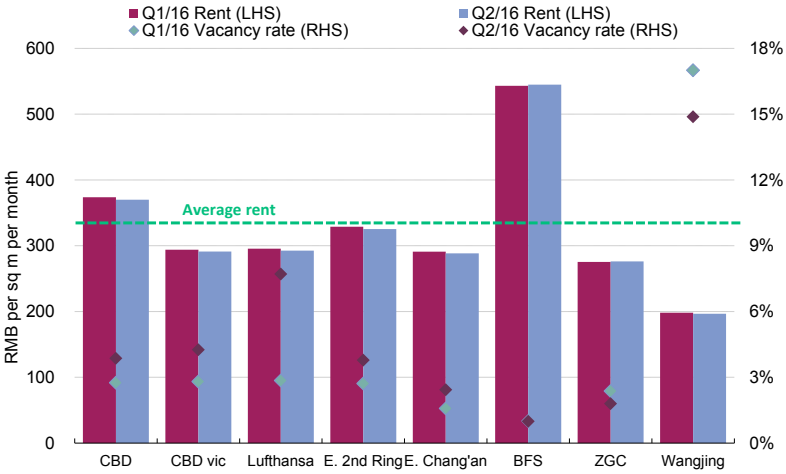
Grade A office rental indices, Q1/2006–Q2/2016



Source: Savills Research & Consultancy

GRAPH 3

Submarket rents and vacancy rates, Q1/2016 VS Q2/2016



Source: Savills Research & Consultancy

in attractiveness due to lower rents and more flexibility in rental agreements. Competition among landlords to attract and retain high quality tenants will increase as more supply and subsequently rental options become available to tenants. Landlords will likely have to adjust their rents and offer more discounts in order to remain competitive. As a result, average rental growth is expected to shrink in the mid to short term.

TABLE 3

Future supply focus, 2H/2016

Project name	Emperor Group Centre (英皇集团中心)
	
Location	CBD's Vicinity
Owner	Emperor Group
Office GFA	47,000 sq m
Typical Floor plate	2,239 sq m
Typical Clear ceiling height	3.1m
Office stories	F5 – F25
Completion date	Q4/2016

Source: Savills Research & Consultancy

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