Growth slows in Grade A office market

Demand for new leases, expansions and relocations exhibited a declining trend.

- Two new projects – China RE Centre and Orient Financial Centre – entered Beijing’s Grade A office market in Q4/2018.

- The new projects contributed a combined GFA of 117,199 sq m and increased total Grade A office stock to 11.02 million sq m (including self-use GFA).

- Affected by the new supply, the city-wide vacancy rate increased by 0.3 of a percentage point (ppt) quarter-on-quarter (QoQ) to 7.0%, although it was down by 0.5 of a ppt year-on-year (YoY).

- A softening in demand for office space resulted in a slowdown in rental growth during the quarter. City-wide average rent was up by only 0.9% QoQ to RMB369 per sq m per month in Q4/2018, although it was up 10.9% YoY.

- The Grade A office market is scheduled to welcome one new project in Q1/2019, which will increase city-wide stock by 47,000 sq m GFA.

- Total net absorption outstripped annual supply in 2018, reaching 541,327 sq m.

“Uncertainty surrounding the economy and ongoing trade war has seen some companies adjust their leasing strategies. Consequently, there has been a decline in activity in the Beijing office market.”

JACK XIONG, SAVILLS RESEARCH & CONSULTANCY
SUPPLY AND DEMAND

Two new projects entered the Grade A office market in Q4/2018: China RE Centre located in Caishikou and Oriental Financial Centre in Wangjing. The new projects contributed a combined GFA of 117,199 sq m and increased total Grade A office stock to 11.02 million sq m (including self-use GFA).

The general economic slowdown resulted in the Grade A office market exhibiting less activity in Q4/2018 than in previous quarters. A number of companies have begun to adjust their leasing strategies, showing increased caution towards expansion, renewal and relocation plans. Meanwhile, some companies elected to downsize their current office space and others chose to move away from prime business districts in order to reduce costs.

Traditionally a key driver of leasing activity, demand from the financial sector was largely flat in Q4/2018. The downturn in appetite was attributed to heightened industry regulatory control on a national level and uncertainty surrounding the ongoing trade war conflict.

In contrast with the financial sector, tenants from the rapidly developing IT & high-tech sector continued to fuel demand for office space in the city, with some tenants actively expanding their footprints during the quarter. The IT & high-tech sector has gradually taken over the financial sector as the key driver of leasing demand for office space in the city. The majority of new leasing activity was concentrated in Zhongguancun (ZGC) and Wangjing districts.

RENTS AND VACANCY RATES

A softening in demand for office space has resulted in a slowdown in rental growth during the quarter. City-wide average rent was up by only 0.6% QoQ to RMB369 per sq m per month in Q4/2018, although it was up 10.9% YoY. The city-wide average vacancy rate increased by 0.3 of a ppt to 7.0%, although it was down by 0.5 of a ppt YoY.

Affected by the economic slowdown and a softening in tenant demand, the average vacancy rate in the CBD increased by 0.7 of a ppt QoQ to 3.4% in Q4/2018. Meanwhile, average rent in the precinct continued increased by 1.2% QoQ to RMB388.4 per sq m per month.

The average vacancy rate in Beijing Financial Street (BFS) decreased by 0.1 of a ppt to 1.3%. Meanwhile, average rent in the precinct continued to edge up, rising 0.2% QoQ to RMB635.9 per sq m per month. A clustering of mature financial companies in the precinct continues to make it an attractive choice for tenants from this industry, and consequently BFS has been able to maintain a stable performance over the years.

The average vacancy rate in ZGC increased by 0.9 of a ppt to 15% in Q4/2018. Despite this, average rents were able to edge up by 1.6% QoQ to RMB696.9 per sq m per month. Rapid rental growth in the precinct has resulted in a number of tenants finding ZGC increasingly unaffordable, and consequently there has been a reduction in demand for new leases and expansions.

OFFICE MARKET OUTLOOK

The majority of future supply in 2019 will be concentrated in the CBD Core Plot Area and Lize Financial Business District. The master-planned projects on the horizon are expected to have a significant influence on the structure and supply-demand dynamic of Beijing’s office market.

Meanwhile, a slowdown in economic growth and a softening in leasing demand will see rental growth struggle to achieve the increases registered in previous years. It is anticipated that city-wide average rent will remain largely stable throughout 2019.

<table>
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<tr>
<th>COMPANY</th>
<th>INDUSTRY</th>
<th>ORIGIN</th>
<th>PROJECT</th>
<th>LOCATION</th>
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