

# Briefing Office and retail

March 2017



Image: Xinghai Square, Shahekou District

## SUMMARY

Average Grade A office rents in Dalian fell during 2H/2016. Average rents in the mid- to high-end retail market held stable during the same period.

- One new Grade A office project was completed in 2H/2016, contributing 40,000 sq m of office GFA to the market and expanding overall stock to 1,150,000 sq m.

- Despite a significant injection of new supply compared with the level seen in 1H/2016, steady demand from tenants saw city-wide vacancy rates decrease by 0.7 of a percentage point (ppt) half-on-half (HoH) to 10.1% during the period.

- Grade A office rents declined 1.1% HoH and 6.7% year-on-year (YoY) to an average of RMB108.8 per sq m per month (exclusive of property management fees) by the end of 2H/2016.

- No new retail projects launched onto the market in 2H/2016. The closure of the Jiuguang Department Store meant total retail stock shrank to approximately 2.92 million sq m.

- City-wide vacancy rates increased 1.4 ppts HoH to 11.0% by the end of 2H/2016. This was largely due to the poor performance of the economy and the impact of the closure of the Jiuguang Department Store.

- Average mid- to high-end shopping mall first-floor rents remained stable at RMB420.0 per sq m per month.

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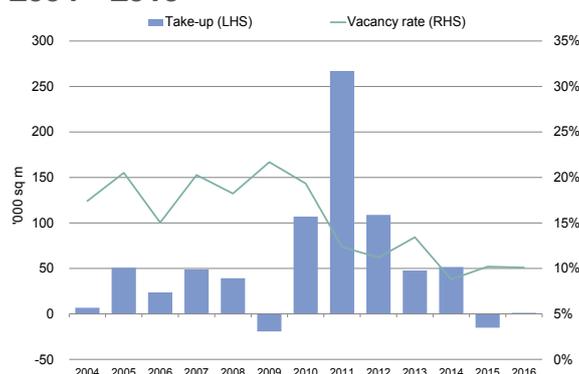
“Project delays have created a serious supply bottleneck that will see a large volume of new office space flood onto the market over the next three years. With demand already strained, vacancy rates are expected to rise.” Jack Xiong, Savills Research & Consultancy

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➔ **Economic overview**

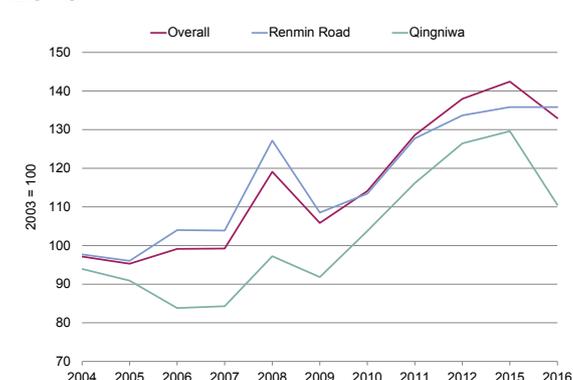
Dalian's GDP grew 6.5% YoY to RMB823.4 billion in 2H/2016. Fixed-asset investment (FAI) totalled RMB143.6 billion during the same period, down by 68.5% YoY. Urban disposable income per capita and retail sales grew by 6.0 YoY and 10.4% YoY, respectively.

GRAPH 1 **Supply, take-up and vacancy rates, 2004 – 2016**



Source: Savills Research

GRAPH 2 **Grade A office rental indices, 2004 – 2016**



Source: Savills Research

**Office market**

**Supply, take-up and vacancy rates**

One new project was handed over in 2H/2016, the Nova Centre located in the Qingniwa area, contributing approximately 40,000 sq m of office GFA to the market. As a result, city-wide Grade A office stock increased to 1.15 million sq m, of which the Xinghai Square and Renmin Road areas remained the largest submarkets, accounting for 32% and 27% of the total stock, respectively.

A generally weak economic environment saw investors and companies scale back their expansion plans, and consequently city-wide vacancy rates continued to face downwards pressure, declining 0.7 of a ppt HoH and 0.1% YoY to 10.1%. The majority of demand continued to stem from financial companies, which accounted for approximately 60% of all recorded transactions.

**Grade A office rents**

The enduring economic downturn continues to see the market face weak leasing demand, and consequently landlords remain under pressure to extend rental discounts and incentives in order to fill vacant space in their projects. As a result, Grade A office effective rents declined 1.1% to an average of RMB108.8 per sq m per month (exclusive of property management fees) by the end of 2H/2016, down 6.7% YoY.

**Submarket vacancy rates and rents**

Traditional business districts

Rents in the Renmin Road area remained stable at an average of RMB83.8 per sq m per month during the second half of 2016. As the majority of office buildings located in this area are under strata-title management, they tend to be older and offer lower-quality facilities than many other projects in the city; consequently, rents in this precinct are lower than other submarkets.

TABLE 1 **Key economic indicators, 2016**

Indicators	Units	Value	YoY growth rate (%)
GDP	RMB billion	823.4	5.0
FAI	RMB billion	143.6	-68.5
Retail sales	RMB billion	341.0	10.4
Disposable income per capita (urban)[1]	RMB	28,463	6.0
Consumer Price Index (CPI)	Previous year = 100	101.9	-

\* Annualised figure  
Source: Dalian Statistics Bureau, Savills Research

TABLE 2 **Notable office leasing transactions, 2H/2016**

Company	Project	Location	Office GFA (sq m)	New lease/renewal
Ship & Port Fund	Xiwang Tower	Qingniwa Area	900	New lease
CYY Food	Nuode Building	Xinghai Bay Area	6,000	New lease
BQ Investment	Wanda Centre	East Harbour Area	500	New lease
Sinochem LN	Xiwang Tower	Qingniwa Area	1,900	New lease

Source: Savills Research

→ However, given its central location, the area remains a popular office destination among domestic companies with lower rental budgets. As a result, the Renmin Road area maintains the lowest vacancy rate in the city, at 4.8%.

The Qingniwa area is host to a number of prime office projects, such as the Senmao Building and Xiwang Tower, and continues to attract interest from multi-national companies (MNCs). This precinct was the only one to receive new supply during the period, with the handing over of the Nova Centre adding approximately 40,000 sq m of leasable office GFA to the market. However, poor leasing performance in the new project caused the vacancy rate in the precinct to spike up 0.6 of a ppt HoH to 12.5%. Looking to attract more stable tenants, landlords have begun to extend rental discounts and incentives and as a result, rents in the area declined by 3.6% HoH to an average of RMB118.3 per sq m per month by the end of 2H/2016.

**Emerging markets**

The Xinghai Square area saw rents decline 2.7% YoY to an average of RMB123.3 per sq m per month. This was largely due to slowing demand and the anticipation of future supply, which has seen landlords lower asking rents. Strong leasing performance in the Nuode Building saw vacancy rates in the precinct decline by 4.6 ppts to 11.9% by the end of the period.

The East Harbour area witnessed a number of early lease terminations in key projects during the period, namely Wanda Centre and Shangfang Mansion, as the economic downturn causes more tenants to exit the market. As a result, vacancy rates in the area grew by 3.5 ppts to 11.6% during 2H/2016. Despite landlords slashing rents in the hope of attracting and retaining tenants, the area remained the most expensive in Dalian, averaging RMB135.0 sq m per month, although down 5.3% HoH.

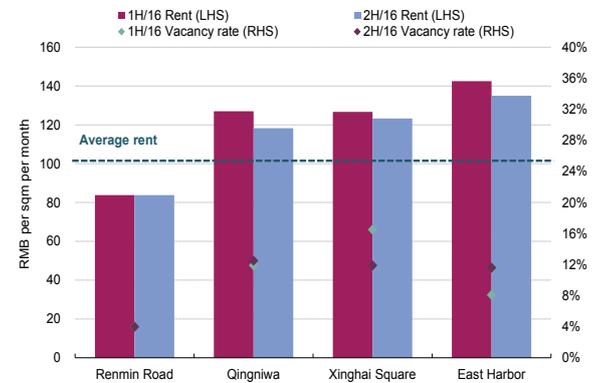
**Office market outlook**

The Grade A office market is expected to see an influx of supply in the first

half of 2017, with two new projects with a combined leasable office GFA of 130,000 sq m scheduled to be handed over. As all new supply is to be concentrated in the prime areas of Qingniwa and the Xi'an Road Commercial Zone, the market is expected to have difficulties absorbing the stock. As a result, both city-wide occupancy rates and average rents are expected to face downwards pressure in the short- to mid-term.

Following a series of delays in project delivery, the city's office market has accrued a bottleneck of supply, which is expected to flood the market over

**GRAPH 3**  
Grade A office submarket vacancy rates and rents, 1H/2016 vs 2H/2016



Source: Savills Research

**TABLE 3**  
Future project focus

Project name	Eton Centre - Dalian	Centre Avenue
		
Location	Qingniwa	Xi'an Road
Owner	Eton Properties	Yongjia Group
Office GFA (sq m)	89,726	39,749
Floor plate (sq m)	1,700-1,800	2000
PM Company	Eton	Yongjia
Asking Rent	RMB 130 / sq m / month	RMB 105 / sq m / month
Management Fee	RMB 1 / sq m / day	RMB 1 / sq m / day

Source: Savills Research

**TABLE 4**  
Future office supply, 1H/2017

Project (EN)	Projects (CN)	Office GFA (sq m)	Submarket
Central Avenue	中央大道	39,749	Xi'an Road
Eton Centre - Dalian	大连裕景中心	89,726	Qingniwa

Source: Savills Research



the next three years. With demand already strained, the oversupply of new office space is forecast to raise vacancy rates. However, landlords of new projects will be wary of their timing when it comes to entering the market, which is likely to result in more handover delays.

The Xinghai Square and East Harbour areas are scheduled to receive the majority of high quality supply, which should help them transition rapidly into mature business centres. However, the substantial level of new supply is expected to outstrip demand, causing landlords to extend rental discounts in order to attract and retain tenants. As a result, it can be expected that the market will experience a continuous decline in rents until the vacant space is absorbed.

## Retail market

### Supply and stock

No new retail projects launched onto the market in 2H/2016. The closure of the Jiuguang Department Store saw total retail stock shrink to approximately 2.92 million sq m, of which shopping malls account for 80%.

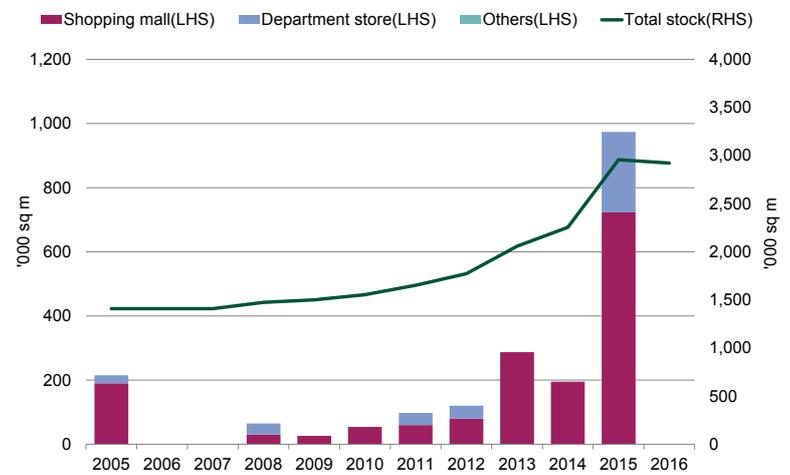
### Demand and vacancy rates

Luxury retailers continued to scale back expansion plans, given the slowing national economy and the government's ongoing anti-graft campaign. Fast-fashion and F&B retailers expanded aggressively. Major leasing transactions of the period included:

- Adidas leased approximately 2,000 sq m in Roosevelt.
- Rice Flour leased approximately 500 sq m in Roosevelt.
- GANT leased approximately 500 sq m in Yihe City.

Competition from the growth of the e-commerce sector, and ongoing tenant adjustment strategies in some projects, saw city-wide vacancy rates increase by 1.4 of a ppt HoH and 3.1 ppts YoY to 11% during 2H/2016. The Xinghai Bay area, one of the oldest

GRAPH 4  
**Mid- to high-end retail supply and stock, 2005 – 2016**



Source: Savills Research

GRAPH 5  
**Rental ranges and vacancy rates of major retail areas, 1H/2016 vs 2H/2016**



Source: Savills Research

TABLE 5  
**Selected retail leasing transactions, 2H/2016**

Tenant	Trade	Project	Location	GLA (sq m)
Youk Shim Won	Fashion	The Pavilion	Others	300
KH Design	Fashion	Yihe City	Others	300
RAPIDO	Fashion	Yihe City	Others	300

Source: Savills Research

prime retail locations, maintained the lowest vacancy rate of just 2.0% at the end of the period.

The Qingniwa area, a traditional business district, is host to a number of prime shopping mall and department store projects, such as New-Mart, Mykal, Parkland and Victory Plaza. However, the recent closure of the Jiuguang Department Store and an ongoing tenant adjustment strategy in Victory Plaza, has seen the average vacancy rate in the area rise by 5.2 ppts HoH and 7.4 ppts YoY to 14.2% during 2H/2016.

The Renmin Road area is host to a number of well-known mid- to high-end shopping malls, such as Friendship Shopping Center, Times Square and Galleria. Due to escalating anti-corruption efforts by the local government, average vacancy rates in the precinct have increased 1.4 of a ppt HoH and 2.1 ppts YoY to 7.4% during the period. The Xi'an Road area, billed as the second largest commercial centre in

Dalian, is host to a number of prime shopping mall projects, most notably Roosevelt Plaza and Fujia Plaza. Average vacancy rates in the area increased 2.8 ppts HoH and 4 ppts YoY to 6.3% by the end of 2H/2016.

**Rents**

Dalian's mid- to high-end shopping mall first-floor rents remained stable at RMB420 per sq m per month (excluding property management fees) in 2H/2016.

**Retail market outlook**

Retail supply is expected to increase in 1H/2017, with one new project scheduled to enter the market, contributing a total retail GFA of 240,000 sq m. Given the large volume of new supply and existing competition, city-wide occupancy rates are expected to decrease over the remainder of the year. Despite rising vacancy rates, established landlords in traditional retail areas are expected to increase rents as there is no shortage of demand in these areas.

TABLE 6

**Future retail project focus**

	<b>Central Avenue</b>
	
<b>Location</b>	Xi'an Road
<b>Retail GFA (sq m)</b>	240,000
<b>Retail type</b>	Shopping mall
<b>Opening date</b>	Q2/2017
<b>Major tenants</b>	TBC

Source: Savills Research & Consultancy

However, newer developments in non-prime locations will have to offer rental incentives in order to attract tenants. As a result, overall city-wide rental growth is expected to remain flat. ■

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