

# Briefing Office and retail

February 2018



Image: Pavilion, Qingniwa Area, Zhongshan District

## SUMMARY

The prolonged economic downturn continues to see the office market face weak leasing demand. Landlords are unable to raise asking rents, and as a result Grade A office rents remained stable at an average of RMB106.2 per sq m per month at the end of 2H/2017.

- Two new projects were handed over in the Grade A office market in 2H/2017. As a result, overall stock increased to 1.24 million sq m.
- Weak leasing demand, coupled with the entrance of new supply, saw the city-wide vacancy rate increase by 4.3 percentage points (ppts) half-on-half (HoH) to 16.7% in 2H/2017.
- Grade A office rents remained stable at an average of RMB106.2 per sq m per month (exclusive of property management fees) in 2H/2017.
- Two new retail projects were launched into the market in 2H/2017. As a result, overall stock increased to 3.31 million sq m.
- Retail city-wide vacancy rates held stable at 12.2% in 2H/2017.
- Average mid- to high-end shopping mall first-floor rents fell to RMB406.5 per sq m per month, representing a decline of 0.2% HoH and 0.6% year-on-year (YoY).

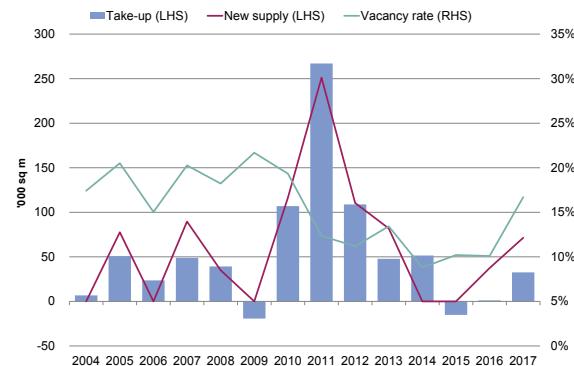
“Due to delays in project launches in 2H/2017, the Dalian office market is expected to face an influx of new supply in the next two years.” Jack Xiong, Savills Research & Consultancy

## → Economic overview

Dalian's GDP grew 7.1% YoY to RMB 736.3 billion in 2017. Fixed-asset investment (FAI) totalled RMB165.3 billion during the same period, up by 3.3% YoY. Urban disposable income per capita and retail sales grew by 6.7% YoY and 9.2% YoY.

GRAPH 1

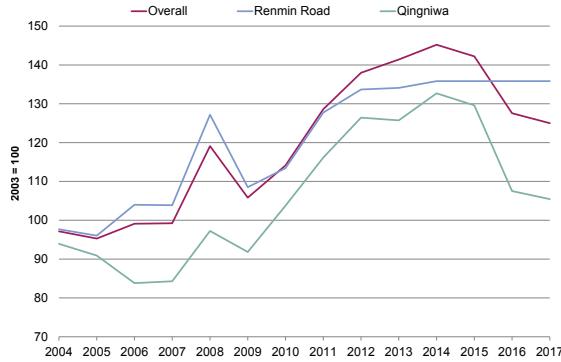
### Supply, Take-up and Vacancy Rates, 2004 – 2017



Source: Savills Research

GRAPH 2

### Grade A Office Rental Indices, 2004 – 2017



Source: Savills Research

## Office market

### Supply, take-up and vacancy rates

Two new projects were handed over in 2H/2017, contributing a total GFA of 90,100 sq m to the city's Grade A office market. The new supply included: Xinxing Centre (新星星海中心), located in Xinghai Square district, contributing 71,400 sq m; and Eton Centre (裕景中心), located in Qingniwa district, partially opened bringing an additional 18,700 sq m to the market. A delay in receiving fire control certification saw the project only partially opened. Upon full opening the project should total 90,000 sq m GFA. By the end of 2H/2017 city-wide Grade A office stock increased to 1.24 million sq m. Xinghai Square and Qingniwa Area continued to reign as the largest submarkets, accounting for 38% and 27% of the total stock, respectively.

A generally weak economic environment saw investors and companies scale back their expansion plans. Consequently city-wide

vacancy rates continued to face upwards pressure, up 4.3 ppts HoH and 4.7 ppts YoY to 16.7%. The majority of demand continued to stem from insurance companies, which accounted for approximately 30% of all recorded transactions in 2H/2017.

### Grade A Office Rents

Prolonged economic downturn continued to see the market face weak leasing demand, and consequently landlords remained unable to raise asking rents when looking to fill vacant space in their projects. As a result, Grade A office effective rents remained stable at an average of RMB106.2 per sq m per month (exclusive of property management fees) in 2H/2017, down 0.2 % 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

TABLE 1

### Key Economic Indicators, Jan – Dec 2017

Indicators	Units	Value	YoY growth rate (%)
GDP	RMB billion	736.3	7.1
FAI	RMB billion	165.2	3.3
Retail sales	RMB billion	372.3	9.2
Disposable income per	RMB	40,587	6.7
Consumer Price Index (CPI)	Previous year = 100	102.1	-

Source: Dalian Statistics Bureau, Savills Research

TABLE 2

### Notable Office Leasing Transactions, 2H/2017

Company	Project	Location	Office GFA (sq m)	New lease/renewal
XDF School	Xiwang Tower	Qingniwa Area	1,918	New lease
CHINA TAIPING	Nova Centre	Qingniwa Area	3,000	New lease
PING AN	Nova Centre	Qingniwa Area	1,900	New lease
Hanya Capital	Xinxing Centre	Xinghai Square	500	New lease

Source: Savills Research

2H/2017. 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. 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 6.3%.

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. Near full occupancy in the newly opened Eton Centre (裕景中心) and a strong improvement in performance in the recently opened Nova Centre (新星国际中心) saw the average vacancy rate in Qingniwa district decrease by 7.4 ppts HoH to 13.7%. The rental in Qingniwa area remained stable at an average of RMB114.3 per sq m per month in 2H/2017.

#### Emerging Markets

The Xinghai Square area received one new office project during 2H/2017, with Xinghai Centre contributing approximately 71,400 sq m. As a result, total stock in the area increased to 438,900 sq m and remained the largest business district in Dalian. Slow demand and the anticipation of future supply has seen a number of landlords lower their asking rents, consequently rents in the area declined by 5.3% YoY to an average of RMB113.8 per sq m per month. Poor leasing performance in the recently opened Xinxing Centre saw the average vacancy rate in the precinct rise by 13.4 ppts HoH to 26.8%.

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 caused more tenants to exit the market. As a result, vacancy rates in the area grew by 3.9 ppts HoH to 16.1% during 2H/2017. Despite landlords slashing rents in the hope of

attracting and retaining tenants, the area remained the most expensive in Dalian, averaging RMB130 sq m per month.

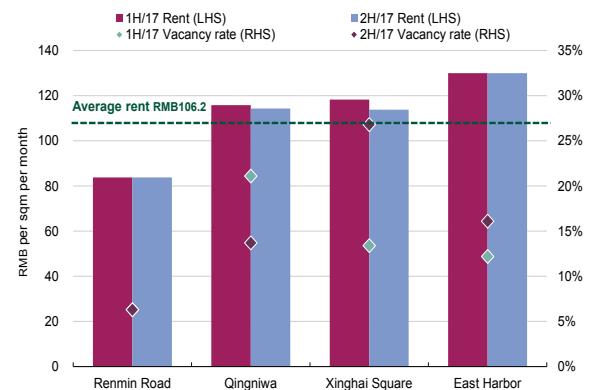
#### Office Market Outlook

The Grade A office market is expected to see an influx of supply in the 1H/2018 with two new projects – Central Avenue and Dingsen Tower, scheduled to be handed over, contributing a combined leasable GFA of approximately 112,000 sq m. As all new supply is to be concentrated in the prime areas of Renmin Road 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 further 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 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

GRAPH 3

#### Grade A Office Submarket Vacancy Rates and Rents, 1H/2017 vs 2H/2017



Source: Savills Research

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

TABLE 3  
Future project focus

Project name	Central Avenue	Dingsen Tower
Location	Xi'an Road	Renmin Road
Owner	Yongjia Group	Dingsen Group
Office GFA (sq m)	39,749	72,000
Floor plate (sq m)	2,000	2000
Asking Rent	RMB 105 per sq m per month	TBD
Management Fee	RMB 30 per sq m per month	TBD

Source: Savills Research

rental discounts in order to attract and retain tenants. As a result, it is expected that the market will experience a continuous decline in rents until the vacant space is absorbed.

## Retail Market

### Supply and Stock

Two new shopping malls were launched into the market in 2H/2017, contributing a total of 393,000 sq m of GFA. As a result, total retail stock increased to 3.32 million sq m, of which shopping malls accounted for approximately 80%. The new supply included:

#### Central Avenue

Central Avenue in Xi'an Road area, contributed 240,000 sq m of GFA, and is now the largest shopping mall in the precinct. The shopping mall is just one component of a larger complex which also offers tourism, culture and business facilities. Notable leases include BONA Cinema, YY sports, Youth Wharf KTV, Haizixiang Japanese Restaurant and Dinglong Gym.

#### Ganjingzi Wanda Plaza

Ganjingzi Wanda Plaza contributed a total of 153,000 sq m of GFA. The project is now the fifth Wanda Plaza in Dalian. The project achieved full occupancy upon its opening. Looking to fill the consumption gap of the rapidly maturing residential community and surrounding student population, the project has introduced a variety of children's educational and F&B retailers, as well as some experiential stores.

### Demand and Vacancy Rates

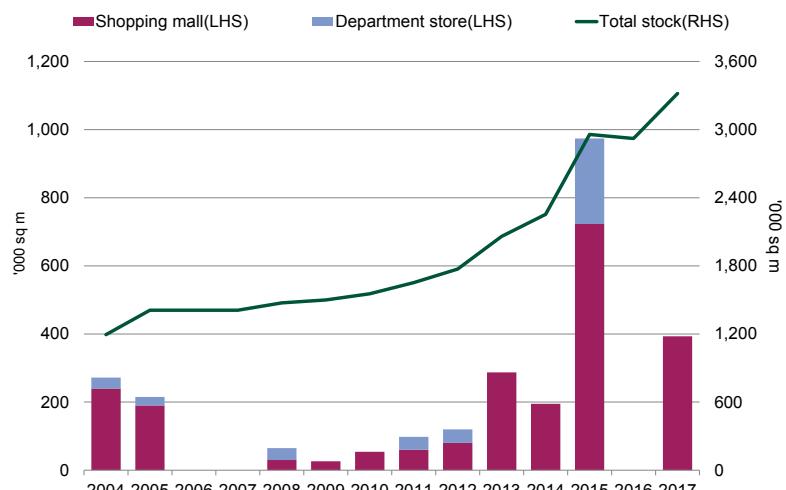
Looking to drive footfall to their projects, astute landlords focussed on introducing retailers that offer experiences for consumers. F&B retailers and experiential stores continued to expand in the city. Major leasing transactions of the period included:

- Xiaomi Experience Store leased 1,000 sq m in Ganjingzi Wanda Plaza.

- Hexiehao Buffet launched a 1,300 sq m store in Central Avenue.

GRAPH 4

### Mid-to High-end Retail Supply and Stock, 2004 – 2017



Source: Savills Research

GRAPH 5

### Submarket Rents and Vacancy Rates, 1H/2017 vs 2H/2017



Source: Savills Research

TABLE 5

### Selected retail leasing transactions, 2H/2017

Tenant	Trade	Project	Location	GLA (sq m)
Starbucks Coffee	F&B	Ganjingzi Wanda Plaza	Ganjingzi	300
BONA Cinema	Culture	Centre Avenue	Xi'an Road	8,000
Dinglong GYM	Lifestyle	Centre Avenue	Xi'an Road	3,000

Source: Savills Research

- The Sweet Dynasty from Hong Kong leased approximately 600 sq m in Pavilion.

Competition from the growth of the e-commerce sector and ongoing tenant adjustment strategies in some projects saw city-wide vacancy rates increase by 1.2 ppts YoY to 12.2% during 2H/2017.

The Xinghai Bay area, one of the oldest prime retail locations, maintained the lowest vacancy rate of just 6% in 2H/2017.

The Qingniwa area, a traditional business district, is host to a number of prime shopping malls and department stores, such as New-Mart, Mykal, Parkland and Pavilion. However, the ongoing tenant adjustment strategy in Victory Plaza and Parkland, has seen the average vacancy rate in the area rise by 2 ppts HoH and 2.4 ppts YoY to 16.6% during 2H/2017.

The Renmin Road area is host to a number of well-known mid- to high-end shopping malls, such as Friendship Shopping Centre, Times Square and Galleria. Poor performance of Galleria saw average vacancy rates in the precinct increase 3.5 ppts HoH and 4.2 ppts YoY to 11.6% during 2H/2017.

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. Strong performance of the recently opened Central Avenue, saw the average vacancy rate in the area decrease by 1.5 ppts HoH to 7.5% in 2H/2017.

#### Rents

Both new projects extended comparatively cheap rents. Consequently, mid- to high-end shopping mall first-floor average rent declined by 0.2% HoH to RMB406.5 per sq m per month (excluding

property management fees) in 2H/2017, down 0.6% YoY.

#### Retail Market Outlook

With no new supply scheduled to enter Dalian's retail market in 2018, total stock will remain unchanged at approximately 3.3 million sq m. The lack of supply is expected to see city-wide vacancy rates fall in 2018. Established landlords in traditional retail areas are expected to increase rents as there is no shortage of demand in these areas. 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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