

Briefing Office and retail sector

July 2018



Image: Hangzhou Tower Central Plaza

SUMMARY

Hangzhou Tower Central Plaza, located under Wulin Plaza, launched in 1H/2018 with a total GFA of 94,000 sq m and is the first retail project launched in a prime area in the last 12 months.

- Two Grade A office projects entered the market in 1H/2018, adding 103,000 sq m.
- The city-wide Grade A office vacancy rate was 14.2% in 1H/2018, down by 0.8 of a ppt.
- Grade A office rents increased 1.6% half-on-half (HoH) to RMB5.4 per sq m per day.
- Four new retail projects were launched in 1H/2018, adding 398,000 sq m to the city's downtown retail market.
- Vacancy rates in shopping malls increased 2.7 ppts HoH to 11.0% mainly due to the new supply.
- City-wide first-floor shopping mall rents increased 1.0% HoH to RMB18.9 per sq m per day.

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 "The Hangzhou office market has started to see demand from co-working operators. Co-working brands are moving from Grade B office buildings to Grade A buildings, helping absorb Grade A space, while also putting upward pressure on market rents."
 James Macdonald, Savills Research

➔ **Office market**

Hangzhou's GDP achieved an 8% real growth rate in 2017 totalling RMB1.256 trillion, the tenth largest city economy in China. Tertiary GDP increased by 14% in 2017, accounting for 63% of the total GDP. The municipal government remains committed to developing Hangzhou into a value-added, service-based and technologically-advanced economy.

Supply and demand

Two projects were handed over in 1H/2018, one located in Qianjiang New City (QJNC) and the other in the Huanglong submarket, adding 103,000 sq m of total Grade A office space.

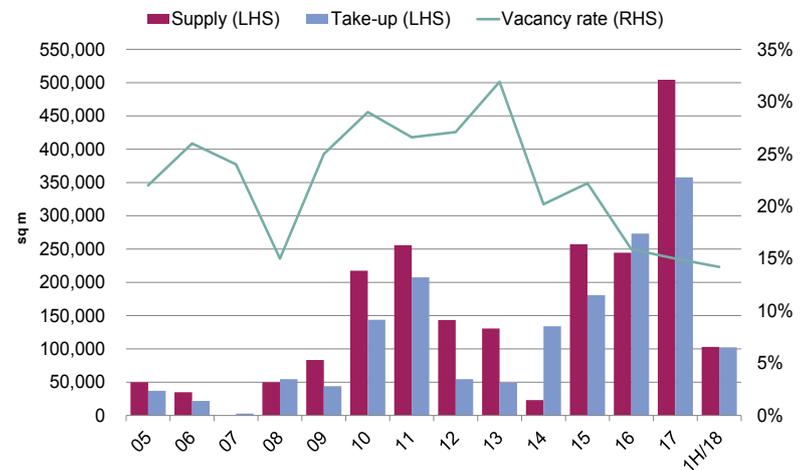
GT Land Plaza ICON Office is located in QJNC with a total office GFA of 60,000 sq m. ICON Office is part of a 400,000 sq m mixed-use complex developed by GT Land that is also comprised of ICON Residence, Jumeirah Hotel, a high-end club, an art gallery and a 100,000 sq m shopping centre, which is expected to open in 2H/2018.

Huanglong Vanke Centre Buildings A and B were also launched in 1H/2018, adding a total office GFA of 43,000 sq m. The two buildings are part of the Huanglong Vanke Centre project, which is comprised of nine Grade A office buildings with a total GFA of around 220,000 sq m and an 80,000 sq m shopping mall called Knowledge Mall. Phase 1 of the project - Building G/H/I - was launched in 2015, and is currently close to fully leased. Major tenants include Baidu Qianbao (百度钱包) and Zhong'an Insurance (众安保险). Building C/D and Building E/F are expected to launch in 2019 and 2020, respectively.

In terms of the demand side for Grade A office space in Hangzhou, financial, information technology and professional services sectors remain the key demand drivers. There has also been a notable uptick in leasing activity in recent years among real estate and architecture companies. In addition, the market saw increasing demand from co-working brands. For example, naked Hub opened its first space in the Euro America Centre in Huanglong. SOHO 3Q leased around 6,000 sq m in Zhejiang Fortune

GRAPH 1

Grade A office supply, demand and vacancy rate, 2005-1H/2018



Source: Savills Research

GRAPH 2

Grade A office rents*, 2009-1H/2018



Source: Savills Research

* Rents of new projects are included in the basket six months after launch

Finance Centre, and WeWork will set up its first location in Hangzhou in Gonglian Plaza, taking up around 10,000 sq m in Q4/2018. Many other co-working operators are expected to expand to the Hangzhou market in the near future.

Grade A office rents and vacancy rates

City-wide Grade A office rents increased to an average of RMB5.4 per sq m per day, up by 1.6% HoH in 1H/2018. Non-prime markets saw rents increase 2.5% HoH on the back of a strong performance by QJNC. With the business environment maturing in QJNC, there is increasing

demand for office space in the area, which has allowed landlords to raise rents. Meanwhile, landlords in traditional business areas were pressured to give rental discounts to attract tenants, which drove rents in prime markets down by 0.4% HoH.

The city-wide Grade A office market vacancy rate remained stable at 14.2%. Without considering the impact of newly released projects this quarter, the city-wide vacancy rate decreased by 3.4 ppts HoH. The vacancy rate in the prime market was 16.5%, up by 5.8 ppts HoH, and 13.5% in the non-prime market, down by 2.7 ppts HoH.

QNJC witnessed a 3.2 ppts vacancy rate decrease HoH to 13.8%. Companies are interested in setting up offices or relocating to the area because of the maturing business environment and strong amenities. In addition, rent in QNJC is also 10%-20% lower than that in prime areas, and could be 20%-30% lower on a like-to-like basis. On the other hand, the rents in QJNC—while still lower than rents in prime markets—have been on the rise in the past three years and averaged RMB4.99 per sq m per day in 1H/2018, up by 3.1% HoH.

Vacancy rates in Huanglong were 17.5% in 1H/2018, up by 11.2 ppts HoH. The increase was due to the new supply on offer in Huanglong Vanke Centre Buildings A and B. Removing the impact of new supply, the vacancy rate remained stable in the area. Vacancy rates in Wulin also stayed stable at 15.2%. Huanglong and Wulin submarkets have been strict with tenant selection since the nationwide crackdown on P2P financing companies.

Strata-title sales market

Growth of the strata-title office market was slow in 1H/2018; the total area transacted was 380,607 sq m at an average of RMB20,830 per sq m for the first five months of 2018. Projects in Xihu and Gongshu districts, including Zheshang Chuangtou Centre (浙商创投中心) and Sunac Blue Peacock (融信蓝孔雀), recorded higher transaction prices—over RMB30,000 per sq m.

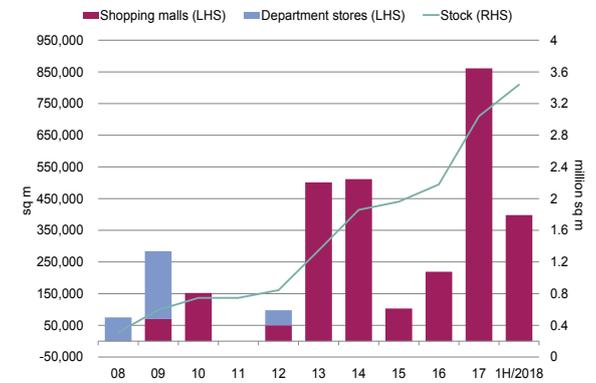
Office market outlook

Five Grade A office projects are expected to launch in 2H/2018, adding a total office GFA of 290,000 sq m. Only one project will be in a prime submarket—the GDA Plaza

in Wulin. QJNC market is expected to receive three more projects including Zhejiang International Trade Headquarter Building (planned for self-use), Dikai Chengxing Buildings A and B (迪凯城星国际大厦A、B座 with Building B planned for self-use), and World Shibao International Centre West Tower (世包国际中心 西塔). Both Dikai Chengxing Building A and Shibao International Centre West Tower are expected to be for-sale projects. Though the new supply seems large in 2H/2018, it will create little pressure on the leasing market as most of the projects are either planned for self-use or for-sale. It is expected that QJNC will see only China Life Building being launched in the next three years for lease. With the submarket absorbing vacant space in the next several years, QJNC is forecast to experience continuing growth in rents till demand and supply shift to Qianjiang Century City (QJCC).

The local government has also planned to develop other areas for commercial use including QJCC, Future Sci-tech City and the Binjiang area. The majority of new developments in QJCC will be completed in 2021 and 2022, with developers such as Greenland, China Resources, Vanke, Shimao and Cinda leading the way. The premium-quality projects will take time to absorb tenants and will place pressure on surrounding areas. Home to the campus for Alibaba's Taobao Town, Future Sci-tech City is expected to see the launch of several Grade A projects in the coming years including EFC, Wantong Centre, AUX Future Centre and Fuli Centre. Supply will be met by the demand from high-tech companies under the "Alibaba impact" in the area. Binjiang is also expected to welcome several

GRAPH 3 Downtown retail supply and stock, 2008-1H/2018



Source: Savills Research

Grade A projects in the near future including Shimao Intelligent Gate (世茂智慧之门) which opens at the end of 2018.

Retail market

City-wide retail sales in 2017 increased 10.5% to RMB571.7 billion. As a major tourist city, tourism spending contributes to a large amount of retail sales in Hangzhou. The city received 162.87 million tourists in 2017, up by 15.8% year-on-year (YoY), and tourism revenue reached RMB304.1 billion, up by 18.3% YoY.

Supply and stock

Four retail projects were launched in 1H/2018 in downtown Hangzhou, adding a total retail GFA of 398,000 sq m, including Hangzhou Tower Central Plaza in Wulin, City Mall Phase 2 in North City, and Yuhang Life Hub and Intime City (Linping) in West City. One other project - Huarun Wanxiang Hui (华润万象汇) - launched in the suburban Xiaoshan area.

TABLE 1 Selected first-hand, strata-title sales transactions, Jan-May 2018

Project (EN)	Project (CN)	District	Transaction area (sq m)	Average transaction price (RMB per sq m)
Zheshang Chuangtou Centre	浙商创投中心	Xihu	1,585	30,916
Huace Centre	华策中心	Xihu	2,635	28,498
Hangzhou Vantong Centre	杭州万通中心	Gongshu	2,121	27,065

Source: Savills Research

As the first project launched in a prime area in the last 12 months, Hangzhou Tower Central Plaza—with a total retail GFA of 94,000 sq m—has attracted a lot of attention. The mall is in the underground area of Wulin Square with two retail floors conveniently connected to Wulin Square metro station (Line 1). The mall positioned itself as a fashionable place for young people—with a number of trendy shops on offer, such as the first Kaola offline shop in Hangzhou, the first Adidas Running shop in China as well as Zukka, Super Species (超级物种) and MOOGAN (摩根家居).

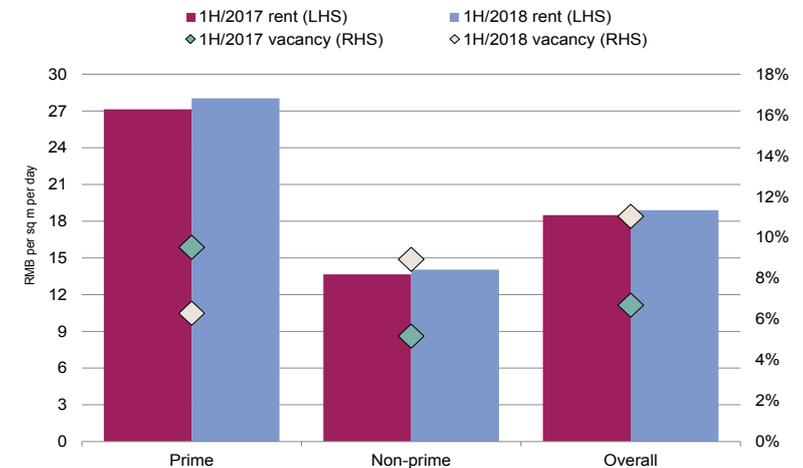
City Mall Phase 2, with a total retail GFA of 80,000 sq m, is located in the North City submarket. The mall has introduced a number of experiential retail outlets including car racing tracks, a swimming pool on the rooftop and other sports facilities. The indoor fountain on the first floor is the highlight of the shopping mall and creates a unique park experience for visitors. City Mall Phase 1 was launched in Jun 2013.

Yuhang Life Hub has a total GFA of 110,000 sq m and is located above the Nanyuan metro station (南苑站) (Line 1). The shopping mall was developed by Chongbang Group, and highlights of the mall include a rooftop landscaped garden designed by a Taiwan art studio, and a performance stage whose first performer will be a well-known Canadian shadow magician. The mall also includes an ice rink, an indoor swimming pool and a premium KTV. Ucommune set up its co-working space on the fourth floor of the mall and takes up around 380 seats.

Intime City (Linping), with a total GFA of 114,000 sq m, launched in mid-June. The shopping mall is located above Linping metro station (临平站) (Line 1), and is part of a 680,000 sq m mixed-use complex that also offers residential, street retail, Grade A office, serviced apartments and a five-star hotel. The shopping mall has introduced a series of well-known brands to the local market including H&M, Gap, Tommy Hilfiger and CK Jeans.

Huarun Wanxiang Hui (华润万象汇) is located in a key area in Xiaoshan District with direct access

GRAPH 4
Retail rents and vacancy rates, 1H/2017 vs 1H/2018



Source: Savills Research

to People Square station (人民广场站) (Line 2 and Line 5 which is under construction). The shopping mall has a total GFA of 104,000 sq m and is part of a 320,000 sq m mixed-use complex. With Huarun's brand reputation and good location, Huarun Wanxiang Hui has enjoyed an occupancy rate of around 95% since opening and expects to see rental growth in the future. Currently the shopping mall houses a number of famous brands including the first Hema Supermarket (盒马鲜生) in Xiaoshan District, Armani Exchange, Lego and Dyson.

Besides the five shopping malls, Alibaba opened its first offline mall - Qin Cheng Li (亲橙里) - in Future Sci-Tech City. The shopping mall, with a total retail GFA of 40,000 sq m, meets the daily needs of Alibaba employees as F&B takes up 40% of the whole area. The shopping mall is also an experimental site for Alibaba's new retail technologies, for example its AR mall guide, VR fitting room and targeted ads digital display. In addition, 亲橙里 mall offers Taobao Xinxuan (淘宝心选), which sells popular products on Tmall, the Tmall Future Store (天猫精灵未来馆) showcasing the latest tech products, and Hema Supermarket (盒马鲜生), which has 440 seats for dining. Though all these technologies created by Alibaba are still in their experimental stages and have some teething issues, they are expected

to be at the forefront of the retail revolution in the future.

Rents and vacancy rates

City-wide first-floor rents increased by 1% HoH to RMB18.9 per sq m per day mainly due to annual rental growth of certain existing projects. QJNC had the highest HoH rental growth among all submarkets at 1.7% to RMB26.7 per sq m per day thanks to the strong leasing performance of the landmark project Raffles City.

Growth in retail sales and in the tourism industry has enabled Hangzhou to absorb the large amount of new supply, keeping the city's overall vacancy rate around 10%. The average vacancy rate of shopping malls increased by 2.7 ppts HoH to 11% mainly due to new supply. Lakeside saw a decrease in vacancy of 1.7 ppts HoH due to strong leasing performances in a couple of leading projects including Hubin Yintai Phase Four. The vacancy rate in West City and Wulin increased by 5.4 ppts HoH and 4.0 ppts HoH respectively due to three new projects. With strong consumption power, Hangzhou has been the city that many brands choose for their first stores in Eastern China outside of Shanghai. Victoria's Secret opened a full-line store in In77 D (Hubin Intime Phase 3) in late June. Household appliance brands are a comparatively large presence in

the Hangzhou retail market as local consumers are enthusiastic about purchasing properties.

In the F&B sector, local Hangzhou food still dominates the market followed by specialities such as hot pot, Japanese/Korean food and Sichuan food. Guangzhou cuisine finds it comparatively hard to break into the Hangzhou market.

Retail market outlook

Looking forward, the market is expected to welcome 731,400 sq m of new supply in the second half of 2018 with several landmark projects set to open, including Joy City, Knowledge Mall and In77 E (Hubin Yintai Phase 5). The large amount of new supply will put vacancy pressure on the market. Meanwhile, as international developers continue

to launch and operate high-end retail projects such as Kerry Centre, Joy City and Raffles City in the city, Hangzhou's retail market is forecast to experience a gradual improvement of retail stock. ■

TABLE 2 **Upcoming downtown retail projects, 2H/2018**

Project (EN)	Project (CN)	Retail GFA (sq m)	Area	Retail type
Joy City	大悦城	200,000	North City	Shopping mall
G.T. Land Plaza	高德置地广场	100,000	QJNC	Shopping mall
Knowledge Mall	黄龙万科中心	80,000	HuangLong	Shopping mall
Xixi Incity Plaza Phase 2	西溪印象城二期	70,000	West City	Shopping mall
In77 E (Hubin Yintai Phase 5)	湖滨银泰五期(E区)	26,400	Lakeside	Shopping mall

Source: Savills Research

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