

Briefing Residential leasing

August 2016



Image: Four Seasons Place, Pudong

SUMMARY

The leasing market remained strong in Q2/2016, with rents continuing to rise despite vacancy rates creeping up in the serviced apartment and villa markets.

- Two new serviced apartment projects, Parkside Serviced Suites by Lanson Place, and Diamond Court, were launched in Q2/2016, adding 182 and 280 units to the market, respectively.
- Serviced apartment rents averaged RMB229.3 per sq m per month, up 4.6% year-on-year (YoY). This is RMB48.6 per sq m per month, or approximately 30%, higher than rents of strata-title apartments.
- Strata-title apartment rents were up 8.4% YoY, to an average of RMB180.7 per sq m per month; this is the largest increase since 2012 when rents grew by 9.3% YoY.
- Villa rents increased 0.5% quarter-on-quarter (QoQ) to an average of RMB153.0 per sq m per month. This market saw the lowest vacancy rates this quarter at 5%, up 1.2 percentage points (ppts) QoQ. Serviced apartments and strata-title apartments' vacancy rates were 9.0% and 11.4% respectively.
- There is growing demand for affordable, short-term, managed residences as more tenants search for alternate, hassle-free options to strata-title apartments.

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 “The lines between serviced apartments and strata apartments are becoming increasingly blurred with the introduction of ‘selected service’ residences and managed strata apartments.” James Macdonald, Savills Research

➔ **Market overview**

Two serviced apartment projects were launched in Q2/2016, the 182-unit Parkside Serviced Suites by Lanson Place, and the renovated 280-unit Diamond Court.

Both rents and vacancy rates increased in the overall residential leasing market in the second quarter. Rents rose 0.9% to an average of RMB187.3 per sq m per month, up 3.8% YoY, while vacancy rates increased 0.4 of a ppt QoQ to 8.5%, down 2.5 ppts YoY.

The residential leasing market remained relatively stable in the second quarter, with a handful of leading residential compounds continuing to outperform the rest of the market, most notably in the Pudong markets of Lujiazui and Jinqiao. The city is still experiencing a decrease in the number of mid- and senior-level expatriate managers; however, the increase in wealthy Chinese entrepreneurs and business people looking to rent high-end units is helping offset the weakening demand from expatriates.

Rental overview

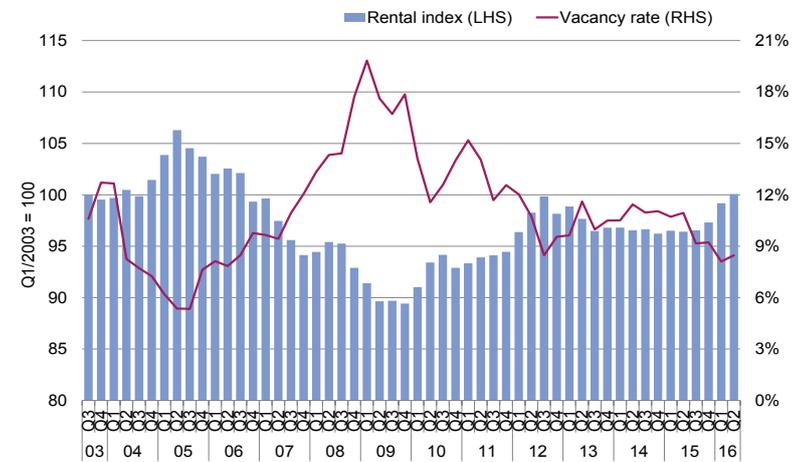
Rents increased across the board this quarter, continuing a trend in rental growth that began last year. Serviced and strata-title apartment rents increased by 1.1% QoQ to an average of RMB229.3 and RMB180.7 per sq m, respectively. Villa rents saw an increase of 0.5% QoQ to an average of RMB153 per sq m.

Vacancy rate overview

Both the serviced apartment and villa markets saw an increase in vacancy rates this quarter, by 0.5 of a ppt (9%) and 1.2 ppts (5%), respectively. Compared to the same period last year, vacancy rates in both markets have decreased 2.7 ppts.

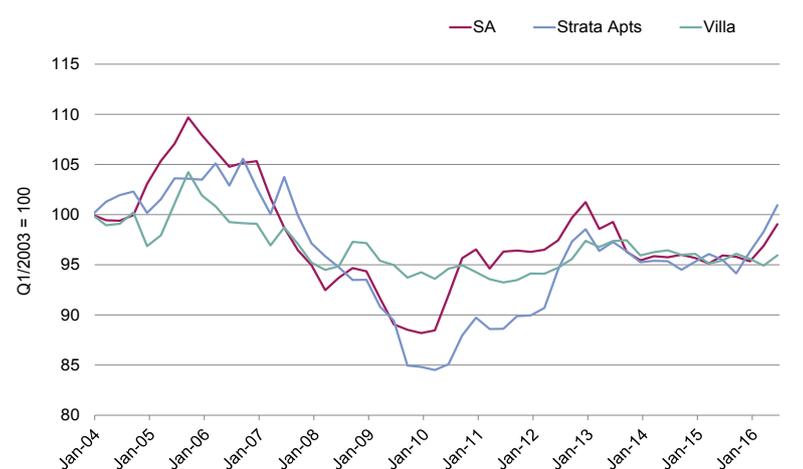
Serviced apartments have the flexibility to position themselves in the market to target tenants with both long- and short-term

GRAPH 1 **Residential leasing market rental index and vacancy rate**



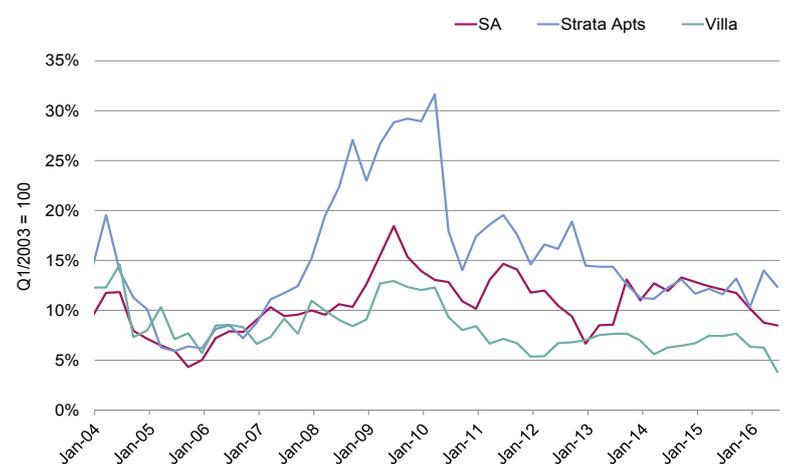
Source: Savills Research

GRAPH 2 **Residential leasing market rental index**



Source: Savills Research

GRAPH 3 **Residential market vacancy rate**



Source: Savills Research

→ leasing requirements, though many projects will start off by signing predominantly short-term leases in order to obtain better occupancy rates, before gravitating towards longer-lease contracts. Some serviced apartments may lean more towards short-term leases, catering to business people on shorter postings or even tourists. While rents are higher for shorter stays, the turnover is also greater, especially in off-peak periods. This strategy has blurred the line between serviced apartments and hotels. Projects that adopt this approach do incur greater costs as they must often partner with online travel agents (OTA) to advertise units. These agents take anywhere from 10-18% (depending on the unit's web page ranking) each time a unit is leased. This, combined

GRAPH 4 Residential leasing market rent and vacancy rate, Q2/2016



Source: Savills Research

TABLE 1 Strata-title apartment, serviced apartment and villa indicators, Q2/2016

	Rent (RMB per sq m per month)			Vacancy (%)		
	Q2/2016	QoQ change (%)	YoY change (%)	Q2/2016	QoQ change (ppts)	YoY change (ppts)
Serviced apartments	229.3	+1.1	+4.6	9.0	+0.5	-2.7
Strata-title apartments	180.7	+1.1	+8.4	11.4	-1.0	-1.8
Villas	153.0	+0.5	+0.3	5.0	+1.2	-2.7
Overall	187.3	+0.9	+3.8	8.5	+0.4	-2.5

Source: Savills Research

TABLE 2 Selected strata-title apartment, serviced apartment and villa transactions, Q2/2016

Project name	Type	Area	Gross unit size (sq m)	Unit price (RMB per month)	Transaction date
Shimao Riviera Garden	Strata-title apartment	Lujiazui	329	38,000	Apr
Stanford Residences	Serviced apartment	Jing'an	237	56,000	Apr
Central Residence	Serviced apartment	Xuhui	204	41,000	Apr
Ambassy Court	Strata-title apartment	Xuhui	118	30,000	May
Elite Residence	Serviced apartment	Changning	125	22,000	Jun
Green Villas	Villa	Jinqiao	340	62,000	Jun

Source: Savills Research

with additional costs of labour and management, has reduced profit margins for operators.

A growing number of wealthy mainland Chinese are renting serviced apartments before purchasing a strata-title apartment in the same area, in order to get a feel for the neighbourhood.

Vacancy rates in the strata-title apartment market decreased by 1.0 ppt QoQ to 11.4%, remaining down 1.8 ppts YoY. This market is the most viable option for many as rents are more affordable than serviced apartments. Due to cost cutting measures implemented by a number of MNC's, many employees are allocated smaller housing budgets or are provided with no budget at all. This has resulted in many serviced apartment tenants turning to strata-title leases.

This quarter saw serviced apartment rents reach RMB229.3 per sq m, RMB48.6 per sq m higher than strata-title apartment rents. Taking this into consideration, the launch of cost-effective, 'selected service' residences are starting to narrow the divide between traditional serviced apartments and strata-title apartments.

There are a number of advantages to renting a 'selected service' residence. 'Selected service' residences are able to offer tenants a convenient, flexible accommodation solution. Particularly aimed at white-collar workers, these apartments provide the assurance of a set lease term (one month to one year) including centralised ownership and management, terms which many multinational companies require for their employees.

Tenants in strata-title apartments are vulnerable to landlords cancelling or refusing to renew leases – a familiar situation for many strata-title apartment tenants.

These 'selected service' residences also remove everyday pressures for expats by providing assistance with administrative needs, such as registering with the police, providing housekeeping and solving any maintenance issues.

Waigaoqiao Sunland

The China (Shanghai) Pilot Free Trade Zone (FTZ) launched in 2013 and is located in the Pudong New Area.

Sunland is a comprehensive development area located five minutes' drive from the Waigaoqiao Free Trade Zone (part of the FTZ). It includes apartments, shopping malls, hotels, and a golf club. The area is being developed in phases, with the last handover expected for 2020. Sunland will cater predominantly to the needs of companies and employees based in the FTZ.

Background of the FTZ

The FTZ is looking to build a system that encourages innovation, abides by international rules of investment and trade, promotes the continued growth of the finance and trade sectors, and provides a properly regulated environment with a sound legal system.

Serviced apartment supply currently planned for Sunland

One Sunland Place Serviced Suites by Lanson Place will be handed over in Q3/2016. There are two further projects expected to launch in 2017 – Kinghouse Serviced Apartments and Somerset Sunland. More launches are expected for 2018, including Savills Residence Waigaoqiao.

Accessibility

Sunland is currently serviced by the Zhouhai Road station (metro line 6), which is one stop away from the South Waigaoqiao Free Trade Zone station. The area is a 30 minutes' drive to Pudong International Airport, and 50 minutes from Hongqiao International Airport in Puxi.

Outlook

The success of the development will depend on whether retail offerings in the surrounding area appeal to the targeted tenants (western grocery stores, international brands, etc.). Inclusion of a lake and park area will certainly attract the attention of expats looking to live in a more natural environment than downtown Shanghai. This development plan for the area mirrors aspects of Jinqiao, a popular residential area for expats and families.

Market news

Nord Anglia International Chinese School opens in September 2016
Nord Anglia International Chinese School is expected to open in September this year. Situated in the Minhang district, the school will be accepting both foreign and Chinese passport holders from ages 6 to 18.

Historically, international schools in China only accepted students who were foreign passport holders (due to local regulations) and catered chiefly to the expat communities. The growing number of expats leaving China, combined with the growing trend among middle-class Chinese families to send their children abroad for education, has increased the number of international schools attempting to open their doors to more local students.

Other international schools in Shanghai with bilingual or dual-language curriculum programmes include Wellington Bilingual College, Shanghai United International School and Yew Wah.

Government supports the residential leasing market

The State Council announced a new policy statement on 3 June 2016, aimed at further developing the property leasing markets. Multiple supportive measures will be put in place, including:

1. Allowing commercial-use property be re-designated for residential leasing use. Under the same land use period and plot ratio, the utilities charges (water, electricity) will all be based on the residential scale (lower than commercial).
2. Tax relief with the VAT rate levy on individual's rental income will be lowered to 1.5% from 5%. For monthly income less than RMB30kpsm, the VAT will be exempted before end-2017.
3. More city-specific policies, including rental payment with housing provident fund.
4. Property units to be added into the city's housing supply plan.
5. Develop professional leasing companies and agencies.
6. Consider the potential of tax reductions for tenant's rental expenses.
7. Support for the financial sector and REITs.

The new policy sets out to improve the variety of leasing options, increase worker mobility and encourage investment in the market.

The new policy is unlikely to directly affect the serviced apartment and luxury residential leasing market, as tenants will remain from the same select demographics: expats, returnees and mainland Chinese entrepreneurs or business people.

Mercer's Cost of Living Survey
Shanghai is becoming ever more costly to live in. According to Mercer's 2016 Cost of Living Survey, Shanghai is currently the 7th most expensive city in the world to live in as an expat, trailing behind Hong Kong (1st) but ahead of Beijing (10th).

Market outlook

New supply for this year was concentrated in the previous quarter, and only one serviced apartment, One Sunland Serviced Apartments, is expected to launch in Q3/2016. This will give the market time to digest stock over the remainder of the year.

The next wave of serviced apartments is expected next year and will be split evenly between Puxi and Pudong based projects. Pudong supply is focused in the Waigaoqiao and Qiantan areas where a lot of development is currently underway.

With cost cutting measures being implemented even more in today's economy, the rise of 'selected service' apartments is a trend to watch. Following the explosion of co-working spaces, such as Naked Hub or WeWork, the move towards cost saving, flexible, communal space-focused residential solutions is already underway, as witnessed in the US with WeWork to WeLiving which sees a diversification of offerings.

The trend of senior expats leaving China for other parts of Asia or relocating back to their home countries is unlikely to reverse. However, demand from wealthy Chinese entrepreneurs is expected to continue increasing, filling the gap left by the number of expats leaving the city. ■

TABLE 3 **Serviced apartment supply forecast, 2016 – 2017E**

Project name	District	Area	No. of unit	Operator	Operator
One Sunland Serviced Suites by Lanson Place	Pudong	Waigaoqiao	Q3/2016	188	Lanson Place
Capella Residences Shanghai	Puxi	Xuhui	1H/2017	40	Capella Hotel Group
Da Zhong Li (Taikoo Hui)	Puxi	Jing'an	1H/2017	200	TBC
Kinghouse - Sunland Serviced Apartment	Pudong	Waigaoqiao	Q1/2017	336	Golden Wing Hotel Management
Qiantan 39-01	Pudong	Qiantan	2H/2017	212	Lujiazui Group
Shama Caojiadu	Puxi	Putuo	2H/2017	168	Shama
Somerset Sunland	Pudong	Waigaoqiao	1H/2017	342	Ascott
Stanford Residence Xuhui	Puxi	Xuhui	Q1/2017	119	TBC

Source: Savills Research

Project focus

Four Seasons Place*

Located in Pudong’s Lujiazui area, Four Seasons Place is an existing luxury serviced apartment project owned by BM Holdings. The project enjoys an open view of the Huangpu River and is a five-minute walk to Lujiazui metro station (line 2).

The serviced apartment units are located in the high zone of the 21st Century Tower, which comprises Grade A offices (3-26F), Four Seasons Hotel (30-41F) and serviced apartments (42-55F). The serviced apartment part offers 35 units, made up of one-bedroom to three-bedroom (144-369 sq m) types. Asking rents started from RMB100,000 per month in Q2/2016.

A clubhouse, shared with the Four Seasons Hotel, is provided for the serviced apartments’ tenants, with full facilities including a gym, an indoor swimming pool and a massage pool.

TABLE 4
Four Seasons Place*

Location	210 Century Avenue, Pudong	
Owner	BM Holdings	
No. of units	35	
Unit size	1 bedroom: 144 sq m 2 bedroom: 213-237 sq m 3 bedroom: 323-369 sq m	
Service	- 24 hour security - Bilingual concierge - 3 times/week basic housekeeping - One international telephone installation fee - Broadband & Wi-Fi - Management fee - Clubhouse	
Transport links	- 5 minutes’ walk to Lujiazui metro station (line 2) - 30 minutes’ drive to Hongqiao Airport - 45 minutes’ drive to Pudong Airport	

Source: Savills China Research
* Savills sole agency project.

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