

Briefing Retail sector

January 2015



Image: Lujiazui, Pudong district

SUMMARY

2015 is likely to prove challenging for the Shanghai retail market. Stakeholders have to bring a fresh approach to the consumer market, adopting more innovative retail formats and experiences to keep shoppers' attention.

- Six new shopping malls were launched in Q4/2014, adding 403,600 sq m of supply to the market.

- First-floor shopping mall rents in prime retail areas remained unchanged in Q4/2014 at an average of RMB46.4 per sq m per day. Rents in non-prime areas fell 0.2% QoQ to an average of RMB16.7 per sq m per day.

- Shopping mall vacancy rates in prime retail locations increased 0.1 of

a percentage point (ppt) in Q4/2014 to 4.1%.

- Limited retail availability and Little Lujiazui landlords' tough selection criteria pushed retail tenants to the Nextage area, providing projects with the ability to update tenant mix.

- 16 shopping malls are expected to open in 2015, adding 1.1 million sq m of new space to the market.

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 "Last year was a testing time, but the situation is likely to get worse before it gets better. Landlords will have to focus on the mid-to long-term prospects."

James Macdonald, Savills Research

➔ Market commentary

2014 was a year of challenges for the brick and mortar retail market. Innovation and the evolution of online retail platforms gained significant traction with consumers, bringing more challenges to the physical market which was already struggling to attract satisfactory tenant mixes. This, combined with a continuous inflow of new supply and generally sluggish retail sales growth in Shanghai, is making the market much more challenging, complex and divergent.

Rents

Retail rental movement has been very modest in 2014, with the market believed to be at an inflexion point. In the fourth quarter, prime retail area rents remained unchanged, while non-prime areas fell 0.2%. For the full year, this represents a 0.1% and -0.7% change respectively.

Landlords have had to become more focused on long term goals in the last twelve months, and more accommodating to retailers' quite demanding requirements, as competition between landlords intensifies and retailers adopt more conservative and disciplined expansion strategies. The shift in negotiation power from landlords to retailers has led to lower starting rents and more favourable leasing terms, as well as landlords focusing more energy on marketing and asset management and readjusting expectations as to when they might start to make satisfactory returns.

Despite the downbeat sentiment, opportunities still exist. A number of projects in non-prime retail location have become local retail landmarks after around three years of operation – typically one lease cycle. Indeed in 2014, landmark projects in non-prime locations outperformed the rest of the market with an annual growth of 2.7%. Considering the lower starting base, these projects still pose better rental growth prospects in the coming years.

in the future. Although some merely provide project information, others are more actively promoting their project by providing news and updates on the retailers within their mall, aiming to establish superior customer loyalty through closer interaction.

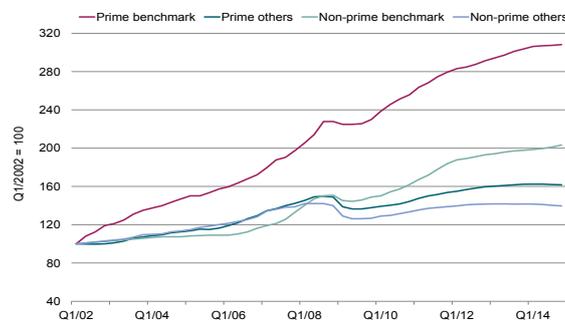
Vacancy

Overall vacancy rates in the nine key retail areas increased 1.2ppts in Q4/2014 to 5.4%. Both prime and non-prime areas have witnessed increases for the last consecutive three quarters.

Prime area vacancy rates increased by 0.1 ppt to 4.1%, mainly due to increased availability in Nanjing Road (E) and Nanjing Road (W). Nanjing Road (E) is Shanghai's leading tourist destination and one of the few pedestrian streets as such it is difficult to drive foot traffic into the mid- and high-zones of shopping malls (typically anything above the second floor). As a result, it is hard to lease these floors; landlords revert to leasing the high-zone to F&B but the mid-zone is much trickier. Nanjing Road (W) has been impacted by the slowing of luxury consumption. During the past year, most projects in these two areas have had a relatively stable tenant mix, with the exception of Raffles City. After the re-division of some retail units within the project, the mall now boasts over 100 fashion and accessories brands, with around 82% coming from overseas.

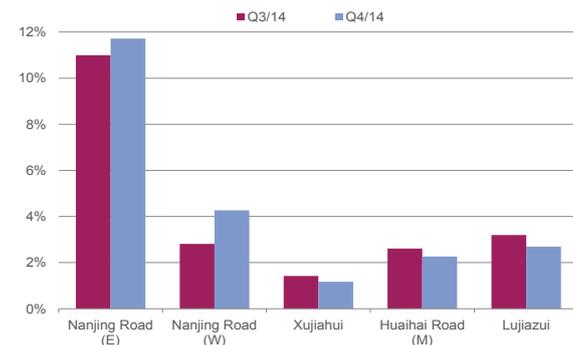
In Pudong, vacancy rates in Lujiazui fell 0.5 ppt to 2.7%. Limited retail availability and Little Lujiazui landlords' tough selection criteria pushed retail tenants to the Nextage area, providing projects with the ability to update their tenant mix.

GRAPH 1 Retail rental indices, Q1/2002–Q4/2014



Source: Savills Research
 Note: Benchmark means five to six market-leading projects based on a comprehensive assessment of reputation, management, design, business and developer experience.

GRAPH 2 Vacancy rates in prime areas, Q3/2014 vs. Q4/2014



Source: Savills Research

Supply

Six new malls opened in the fourth quarter, adding 403,600 sq m of space and bringing annual supply to 782,900 sq m, a 5% increase on 2013 levels.

The Zhangjiang area in Pudong saw two projects, Chamtime Plaza and Huizhi Life Center, opened next to Jinke Road station (metro line 2) adding 184,000 sq m of new supply. Chamtime Plaza focuses on F&B and fashion, introducing the first H&M and Uniqlo stores to the area. Huizhi Life Center focuses more on lifestyle, such as Auchan Supermarket and a handful of child-related stores.

Puxi saw 219,600 sq m of new supply, including Bailian Binjiang Shopping Mall, Arch Walk, SOHO Fuxing Plaza and MTR City Plaza (North Block) plus the reopening of The Place (Phase One & Two).

All seven projects launched official WeChat accounts as a way of promotion, which is a recent and rapidly growing trend; one that is likely to become more common for projects

Three projects in the area underwent renovation in 2014. Aside from Xinmei Union Square shopping mall, Plaza 721 (formerly Pacific Digital Plaza) and 1088 Plaza (formerly Zhongrong International Business City) are both attempting to reposition themselves with better facilities and new tenant mixes. I.T. expanded its leasing space in Xinmei Union Square to around 1,000 sq m, while Tao Heung took around 900 sq m in 1088 Plaza.

Performance of non-prime areas remains varied. Wujiaochang's vacancy rate was only 0.4%, while Hongqiao reached to 15.6% as a result of 167,700 sq m of new supply in the fourth quarter.

Outlook

16 projects are expected to launch in 2015, adding 1.1 million sq m of space to the market. Of these, five will launch partial launches i.e. individual phases of a bigger project. Prime areas are expected to see 158,000 sq m of shopping mall supply. The emerging areas of Hongqiao Transportation Hub, New Jiangwan Town and Zhenru will see their first sizeable retail projects opened in 2015.

Shanghai already has half a dozen factory outlet projects, from the relatively successful Bailian Outlets Plaza in Qingpu to the underperforming Global Outlets Park in Jinshan, all of which are located in Puxi. The city, however, is expected to see the completion of two new outlet projects in Pudong, namely Florentia Village and Shanghai Village, adding a total of 100,000 sq m in 2015. This will be the first time two outlet projects have been launched in the same year. Florentia Village, located between Disney Land Park and Shanghai Pudong Airport, is expected to open in Q1/2015. Shanghai Village, developed and operated by Value Retail, will be located adjacent to Disney Land Park and marks the development of their relationship which started in Paris 15 years ago with La Vallée Village.

Lujiazui is expected to continue to be one of the strongest performing prime areas in 2015. At the start of the year, Lujiazui will see the opening of largest Disney store in the world beside Oriental Pearl Tower, the precursor for the opening of Disneyland Park later in the year. Shanghai Tower is also expected to open in late 2015, with a number of new retailers such as Eslite Bookstore. These new retail options will bring a new wave of consumers and tourists to the area, supporting rental growth in the coming years.

The overall retail market, however, will continue to see a period of consolidation and weaker demand

Selected leasing transactions



Repetto

Repetto is renovating its new store in Grand Gateway. The ballet shoe company made its first foray into the China market in early 2014. This new store represents the brand's third store in Shanghai.



Victoria's Secret

Victoria's Secret will unveil its first store in Shanghai in early 2015. The store is located on the first floor of Raffles City with a net area of around 150 sq m, focusing on perfumes, accessories and their lingerie line.



Zara

Zara has been very conservative in 2014, but still opened two new stores towards the end of this year. One is a street store in the central section of Nanjing Road (E) pedestrian street, while the other is in the newly opened The Place along with its sister brands Oysho, Massimo Dutti and Zara Home.



Outback Steakhouse

After two years in Shanghai, the American restaurant chain will open another two stores in Shanghai in The Place, Changning district and SOHO Fuxing Plaza, Huangpu district.



Nice Meeting You

Nice Meeting You is one of the most rapidly expanding restaurant chains of 2014. The restaurant has secured spaces in at least six shopping malls in Q4/2014, focusing on higher footfall projects including SML Center, and key projects in decentralised locations such as Minhang Plaza and Zhoupu Wanda Plaza. The retailer also opened an "Express" store during the soft opening period of Crystal Galleria.

which could last for up to three to four years. The hope is that not only will international brands continue to grow their presence, but that new retailers will continue to establish footholds in the China market via Shanghai, as well as domestic brands finding their

own space in the market. At the same time, the hope is that developers and landlords adopt more innovative retail formats and consumer experiences, bringing a fresh approach to the brick and mortar retail market. ■

Project focus

Bauhinia Square

■ Bauhinia Square, expected to open to the public in 2015, is located on Kongjiang Road in the Yangpu district, connected to Jiangpu Road Metro Station (Line 8 and future Line 18). The project has a total retail GFA of 69,200 sq m over 12 floors (B1-11F), making it the largest retail development along the road.

■ Kongjiang Road used to be one of the most popular retail streets in the Yangpu district, but has seen its popularity waning in recent years compared to Wujiaochang and Daning. The core section of the road has seen no new retail supply since 2000

and the majority of retail stock is street stores or retail podiums, which appear outdated.

■ 2015 will hopefully bring a breath of fresh air to the road as three projects are scheduled to open with a total retail GFA of 129,400 sq m, including Bauhinia Square, Wenfeng Shopping Mall and Ocean Plaza. As the new projects are all small- to mid-size developments, Kongjiang Road is expected to continue to see shoppers hopping from one mall to another in a way that is rarely seen in other parts of the city where larger retail developments ensnare consumers.



Please contact us for further information

Savills Research



James Macdonald
 Director, China
 +8621 6391 6688
 james.macdonald@savills.com.cn

Savills Retail



Siu Wing Chu
 Deputy Managing Director
 +8621 6391 6688
 siuwing.chu@savills.com.cn



Aileen Zhong
 Director
 +8621 6391 6688
 aileen.zhong@savills.com.cn



Nicky Zhu
 Senior Associate Director
 +8621 6391 6688
 nicky.zhu@savills.com.cn

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