Briefing
Retail sector

July 2016

Image: Disney Town

SUMMARY

The closure of a number of fashion stores and lower pre-commitment among some new projects increased overall vacancy levels.

- Retail sales grew by 7.1% year-on-year (YoY) in the first five months of 2016, 0.9 of a percentage point (ppt) lower than the same period in 2015.
- Three projects launched soft openings, with a total retail GFA of 162,000 sq m.
- First-floor shopping mall rents in prime retail areas increased by 0.2% quarter-on-quarter (QoQ) to an average of RMB48.9 per sq m per day, while non-prime areas increased by 0.1% QoQ at RMB16.8 per sq m per day.
- Vacancy rates in both prime and non-prime areas increased by 0.5 of a ppt in Q2/2016 to 6.2% and 9.5%, respectively.
- The opening of Disneyland is expected to bring new dynamism to the city's prime retail areas.

"Citywide rents trended down in Q2 as more new projects provided incentives to attract the right tenants during the first lease cycle. However, the rental index remains stable, supported by the healthy performance of mature projects."

James Macdonald, Savills Research

Market commentary

It is becoming increasingly difficult for landlords and market observers to gauge suitable rental levels and assess the best ways to increase the overall performance of a retail centre.

F&B tenants, typically occupying the basement levels and upper floors of a project, have seen their rents continue to increase in recent years. At the same time, apparel and accessories retailers, typically occupying the first and second floor of a shopping centre, have had to scale back their expansion plans in response to decreasing sales numbers. Landlords, still eager to sign leading apparel tenants to high-visibility, first-floor spaces in flagship stores, are providing significant incentives and offering lower rates to attract the best retailers. This has lowered the rental difference between lower and upper floors to such an extent that first floors are now no longer the most expensive real estate in certain malls.

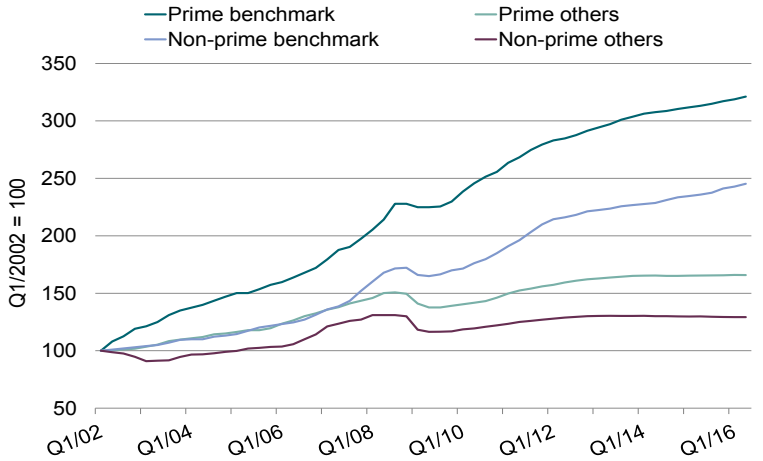
First-floor shopping mall rents in prime retail areas increased by 0.2% quarter-on-quarter (QoQ) in the second quarter to an average of RMB48.9 per sq m per day, while those in non-prime areas increased by 0.1% QoQ to RMB16.8 per sq m per day.

Prime areas

Vacancy rates in prime retail areas increased by 0.5 of a ppt QoQ to 6.2%, the highest level in the past 24 months. Four of the five prime retail areas recorded increases with the only exception being Huaihai Road (M).

GRAPH 1

Retail rental indices, Q1/2002–Q2/2016



Source: Savills Research
Note: 1)Benchmark refers to five to six market-leading projects based on a comprehensive assessment of reputation, management, business and design. 2) Rent is based on affordable rents of fashion and accessories tenants on the first floor.

Huaihai Road (M) is a distinguished, upscale retail location focusing on street, leisure and lifestyle retail. It has a diversified format: open and enclosed retail areas, and a number of various-sized projects. The area maintains the lowest proportion (25%) of fashion and accessories tenants and the highest percentage (40%) of F&B tenants among all prime areas. Moreover, a majority of the retail buildings, even many of those under 10,000 sq m, are operated by reputable developers, funds or local SOEs with strong retail backgrounds, making possible an orderly tenant mix reconfiguration and positioning. With the opening of a new metro line (Line 13) that intersects the middle section of the road and the introduction of more new stores such as Gentle Monster and Line Cafe, footfall should become more balanced along different sections of the road as more choices become available to consumers.

Fashion and accessories brands make up a larger percentage of tenants in prime areas than in non-prime areas (34% vs 19%). As the category hit hardest by the rise of e-commerce, even some leading projects are beginning to feel the pressure of finding the right tenants to fill their space. For example, the vacancy rate in Xujiahui increased 3.3 ppts in the second quarter, of which 89% of the vacant space was previously owned by fashion and accessories tenants.

Non-prime areas

Three projects opened in non-prime areas in the second quarter, including Daning Music Plaza, Bingo (East Building) and U Fun, with an aggregate retail GFA of 162,000 sq m. The opening of new projects pushed the average citywide vacancy rate up 0.5 of a ppt QoQ to 9.5%. However, if the new projects are excluded, the vacancy rate actually decreased 0.7 of a ppt QoQ to 8.3%.

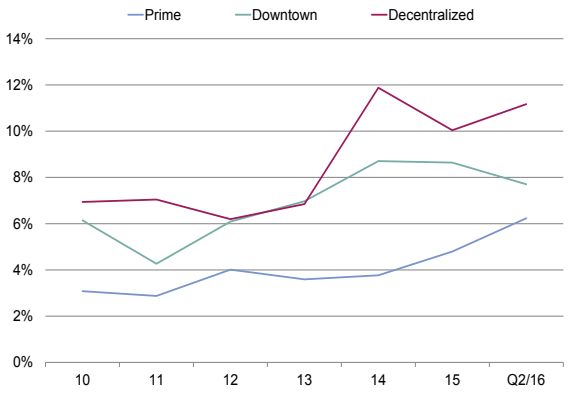
Higher rental prices have pushed more families and cost-conscious companies to suburban locations, increasing the population density in decentralised areas. On the back of this trend, there is now greater demand for F&B, services and children's retail options in non-prime locations. Retailers are becoming increasingly drawn to these areas, including newcomers to the local market. Vanilla will open its first restaurant in Shanghai at Sky Mall, Fratelli La Bufala will open in Hopson One, while Burger King opened the first BK Café in Daning Music Plaza.

The Disney effect

After five years of construction, Disney held its grand opening for the first phase of the Shanghai Disney Resort in June 2016. The 3.9 sq km of Phase

GRAPH 2

Vacancy rates, 2010–Q2/2016



Source: Savills Research

one is part of the 7.0 sq km core area of the Shanghai International Tourism Resort Zone, which is slated to become a key new driver of Shanghai's future development.

Aside from the theme park, the core area currently has two retail facilities: Disney Town, a 46,000 sq m open-plan project adjacent to the park operated by Disney and Shendi, and Shanghai Village, a 50,000 sq m outlet mall operated by Value Retail.

The opening of Disney represents a new era of development for the theme park and tourism industry in Shanghai and across China. It is believed that the tourism industry will catalyse new growth of the services industry, providing an added boost to the economy. Visitors to Disney from further afield will likely aid the hospitality sector as they combine a visit to Disney with a city stopover, increasing sales figures in key tourist locations, such as Xintiandi and Nanjing Road (E).

All true international cities boast vibrant and well-developed tourism markets which in turn help to boost sales, footfall and visibility in the main tourist-focused retail precincts. The completion of the Shanghai Disney Resort and the continued development of the tourism industry in Shanghai will help take the city's retail market to the next level.

Project focus

189 Lane

189 Lane is CITIC Capital's first retail project in Shanghai. The project is located in the Putuo district, within a few minutes' walk of Metro Line 7/13 (Changshou Road). It is a mature residential and commercial area, housing over 100,000 residents as well as a decent number of office buildings.

With retail GFA of around 30,000 sq m, the project aims to provide more retail options to the surrounding communities and office staff, complementing the neighbouring project Hong Kong New World Department Store (Shaanxi Road Branch).

The project is currently under leasing and is expected to open at the end of 2016.

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