

Briefing Office and retail sectors

November 2013



Image: Wulihe area, Heping district

SUMMARY

Grade A office and mid- to high-end retail YTD rental growth slowed to below 3% as competition for tenants intensified with the addition of new supply.

■ One new project, the 43,000-sq m Shenyang Tiandi Tower B, entered the market in Q3/2013.

■ Grade A office city-wide vacancy rates rose by 2.7 percentage points (pps) in Q3/2013 to 20.4%, due to the launch of a new project.

■ Net take-up registered 16,000 sq m in Q3/2013, with year-to-date (YTD) net take-up reaching 36,000 sq m.

■ Grade A office rents rose by 0.8% quarter-on-quarter (QoQ) to an average of RMB136.3 per sq m per month (including management fees), with YTD growth constrained to just 1.6%.

■ Six Grade A office projects are expected to launch in Q4/2013, adding

375,000 sq m to the market and increasing current stock by 47%.

■ Shenyang's fourth Wanda Plaza debuted in Q3/2013, adding 170,000 sq m of retail GFA to the mid- to high-end retail market, while two department stores located in Taiyuanjie were closed, leaving total retail stock at 4.6 million sq m.

■ City-wide retail vacancy rates fell to 12.6%, with tenant mix adjustments having been completed in one shopping centre and high occupancy rates in the new Wanda Plaza.

■ Prime first-floor shopping mall rents ranged between RMB250 and RMB550 per sq m per month in Q3/2013, with YTD growth constrained to just 2.5%.

■ Seven retail projects are expected to debut in Q4/2013, adding a total retail GFA of 682,000 sq m to the market and enlarging total stock by 15%.

“Hunnan New District welcomed its second shopping centre, Wanda Plaza, in Q3, helping the area’s retail environment to mature.”

Joan Wang, Savills Research

➔ Economic overview

Echoing the country's sluggish economic growth, Shenyang's real GDP growth slowed to 9.0% in the first half of 2013, from a real compound annual growth rate (CAGR) of 14.6% from 2000 to 2012.

Shenyang's fixed asset investment (FAI) rose 21.7% year-on-year (YoY) reaching RMB318.5 billion in Q2/2013. However, the construction of many projects was suspended due to the 12th National Games being held in Shenyang, leading to the real estate investment (REI) growth rate to slow to 16.0%, down 11.9 ppts from Q1/2013.

TABLE 1
Macroeconomic indicators, Jan–Jun 2013

Indicators	Units	Value	YoY growth (%)
GDP	RMB billion	352.3	9.0
Foreign direct investment (FDI)	US\$ million	2.92	-5.9
FAI	RMB billion	318.47	21.7
REI	RMB billion	97.68	16.0
Retail sales	RMB billion	149.9	13.0
Disposable income per capita (urban)*	RMB	28,967	9.6
Consumer product index (CPI)	PY = 100	103.1	3.1

Source: Shenyang Statistics Bureau, Savills Research

*Annualised figure.

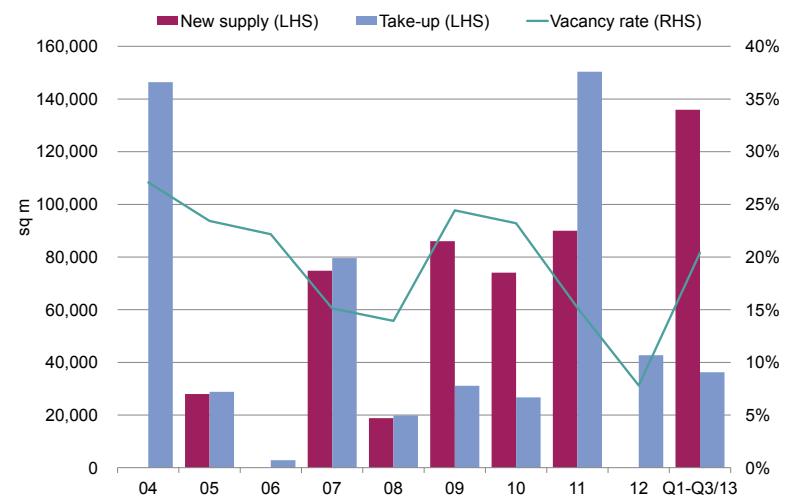
TABLE 2
Grade A office market key indicators, Q3/2013

	Stock (sq m)	Vacancy rate (%)	Net Take-up (sq m)	Supply (sq m)	Rent (RMB per sq m per month)
Q3/2013	708,000	20.4	16,000	43,000	136.3
QoQ change (%/ppts)	6.5	2.7	7.2	-	0.8
YoY change (%/ppts)	23.7	10.7	-	-	3.8

Source: Savills Research

GRAPH 1

Grade A office supply, take-up and vacancy rate, 2004–Q2/2013



Source: Savills Research

Office market

Market commentary

Shenyang's Grade A office market saw one new project launched in Q3/2013. With the limited pool of tenants, particularly those from the services sector, resulting in low occupancy rates in projects completed in the past six months, the city-wide vacancy rate was pushed up to over 20% by the end of Q3/2013. Domestic financial, energy and logistics companies were the major demand drivers in the quarter.

With the launch of a new project intensifying competition for tenants, the majority of landlords were forced to either maintain the same rental offerings as nine months ago or even provide rental incentives, narrowing Grade A office YTD rental growth to within 2%.

Supply, take-up and vacancy rates

One new project, Shenyang Tiandi Tower B, was handed over in Q3/2013, adding an office GFA of 43,000 sq m to the market and expanding the leasable stock to 708,000 sq m. Supply totalled 136,000 sq m in the first three quarters of 2013, an historical peak over the past decade.

Located in North Station area, Shenyang Tiandi Tower B was received favourably by several domestic financial and energy companies. This project had already achieved

an occupancy rate of over 30% by the end of Q3/2013, largely due to Sinopec's pre-commitment of 5,000 sq m. Other well-known tenants include China National Petroleum Corporation (CNPC) and New China Life Insurance (NCL).

Net take-up for the quarter reached 16,000 sq m, almost equivalent to the previous quarter. YTD net take-up was 36,000 sq m, compared with supply of 136,000 sq m and average annual take-up over the last five years of 54,000 sq m per annum, indicating slowing demand in the local market. The demand primarily came from the financial and energy firms, with domestic companies continuing to take a lead.

Vacancy rates in existing projects remained largely stable as demand for newly established offices and expansions remained weak. Consequently, the city-wide vacancy rate rose by 2.7 ppts QoQ and 10.7 ppts YoY to 20.4%, due to low take-up in this year's newly launched projects.

Grade A office rents

Most landlords, responding to weaker demand, maintained the same rental offerings as Q2/2013. As a result, Grade A office rents appreciated by just 0.8% QoQ to RMB136.3 per sq m per month (including property management fees), with YTD growth down to 1.6% from a CAGR of 15% over the past three years.

Submarket vacancy rates and rents

Wulihe area

Wulihe area continued to command the highest rents in Shenyang, largely stabilising at RMB157.0 per sq m per month (including property management fees), up 4.5% YoY. Meanwhile, vacancy rates fell by 1.4 ppts QoQ to 5.7%, down 4.8 ppts YoY, as vacant space in prime office buildings was absorbed.

North Station

North Station rents appreciated by 2.0% QoQ, leading to the city's second highest rents at an average of RMB141.0 per sq m per month (including property management fees). The launch of a new project pushed up the area's vacancy rate by 17.0 ppts QoQ to 21.5%, representing a YoY increase of 17.8 ppts.

Office market outlook

Six projects, with 375,000 sq m of office GFA, are scheduled to enter the market in Q4/2013, enlarging total stock by 47%. Competition between landlords for tenants is expected to be intense, resulting in rising city-wide vacancy rates while overall rents are expected to fall.

Retail market

Market commentary

Despite the launch of Wanda's fourth mall in Shenyang this quarter, the city-wide vacancy rate fell to its lowest level in recent years due to high occupancy in a new project and the improved performance of a recently repositioned shopping mall.

Vacant space in mature retail areas was rapidly taken up, following active expansions from a number

of fashion, F&B, and leisure and entertainment retailers. Despite this, YTD rental growth was further constrained to below 3%, as fierce competition between projects resulted in landlords focusing on tenant mix and occupancy rates instead of rental performance.

Supply and stock

Only one project, the 170,000-sq m Wanda Plaza (Hunnan store), opened in Q3/2013 – the first supply seen this year. Also in the third quarter, two department stores, namely ISETAN and New Mart (connected) both located in Taiyuanjie area and with a total retail GFA of 105,000 sq m, were closed, to be replaced by Happy Family Department Store in Q4/2013 when it reopens. As a result, Shenyang's mid- to high-end retail stock increased marginally to 4.6

TABLE 3
Selected office leasing transactions, Q3/2013

Company	Project	Location	GFA (sq m)	New lease/ renewal
Sinopec	Shenyang Tiandi Tower B	North Station	5,000	New lease
CNPC	Shenyang Tiandi Tower B	North Station	700	New lease
NCI	Shenyang Tiandi Tower B	North Station	500	New lease

Source: Savills Research

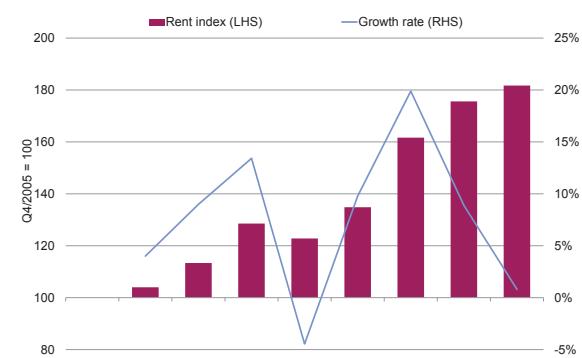
TABLE 4
Future office supply, Q4/2013

Project	Business district	Office GFA (sq m)
Huachen Zhongji Mansion (华晨中际大厦)	North Station area	51,000
Zhongtie Mansion (中铁大厦)	Zhongshan Square and Heping Avenue area	40,000
Lang Qin Tae-won Center (朗勤泰元中心)	Zhongshan Square and Heping Avenue area	33,000
Maoye Centre (茂业中心)	Wulihe area	100,000
Dongda International Center (东大国际中心)	Zhongshan Square and Heping Avenue area	116,000
Global International Plaza (Phase 2) (环球国际大厦(二期))	North Station area	35,000

Source: Savills Research

GRAPH 2

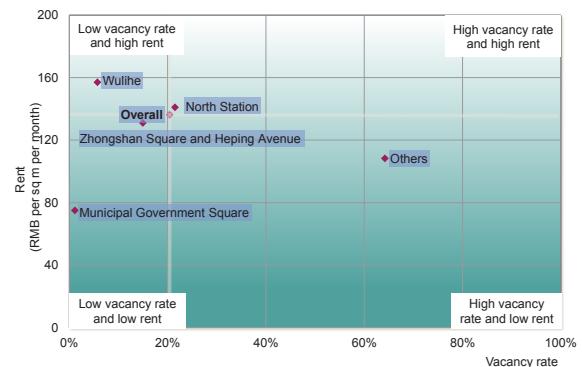
Grade A office rental index, 2005–Q2/2013



Source: Savills Research

GRAPH 3

Grade A office submarket vacancy rates and rents, Q2/2013



Source: Savills Research

million sq m, one of the largest retail markets among second-tier cities.

Located in Hunnan New District, Wanda Plaza (Hunnan store) is Wanda Group's fourth Wanda Plaza in Shenyang. The shopping centre is anchored by Wanda Department Store, Wanda Cinemas, Vanguard supermarket and D House gym. It also includes a number of fashion, F&B, leisure and entertainment, and household and lifestyle retailers such as Uniqlo, Pizza Hut, Music Star KTV and MUJI. The project is the second shopping centre in Hunnan New District, following the opening of Pan-China Shopping Centre in 2010.

Demand and vacancy rates

Fashion, F&B, and leisure and entertainment retailers showed the greatest appetite in the local market in the third quarter. A number of retailers including CK Jeans, Uniqlo, Ochirly, Basic House, Yahui Food Court and Yunhaiyao Restaurant took space previously used by the now-closed Zen department stores in Joy City – Shenyang. Meanwhile, H&M, Sephora, Shanghai Min and Pacific Coffee pre-leased in the second phase of Rich Gate Shopping Centre, which is scheduled for debut in 2014.

Largely due to the improved performance of Joy City – Shenyang, combined with full occupancy in the newly completed project, the city-wide vacancy rate fell by 3.1 ppts QoQ to 12.6%, down 1.6 ppts YoY.

Rent

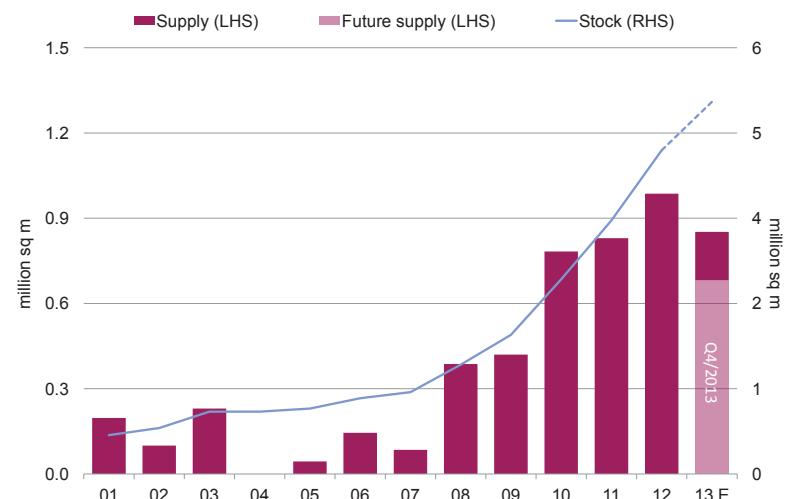
Prime shopping centre first-floor rents remained largely unchanged at RMB250 to RMB550 per sq m per month, while YTD rental growth was limited to just 2.5%, down from a CAGR of 8.4% over the last three years. This was due to landlords increasing rental discounts to attract suitable tenants, given the current amount of supply.

Retail market outlook

Seven projects, four shopping centres and three department stores, are scheduled to debut in Q4/2013, adding a total retail GFA of 682,000

GRAPH 4

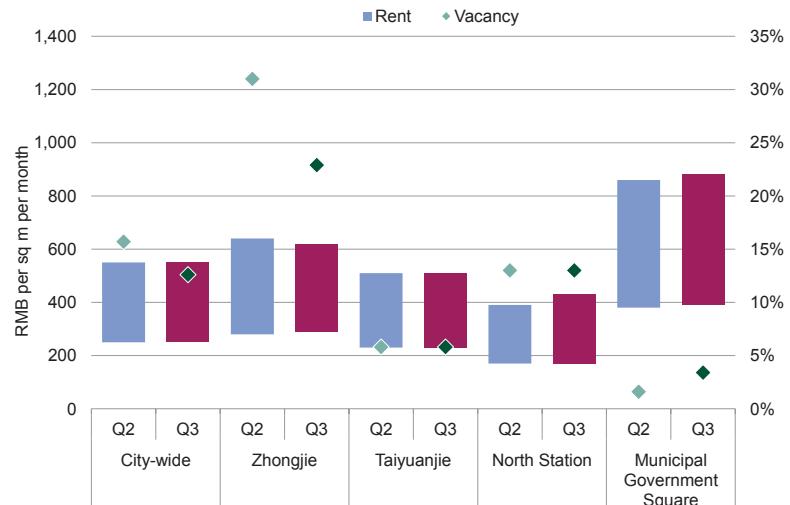
Mid- to high-end retail supply and stock, 2001–2014E



Source: Savills Research

GRAPH 5

Rental ranges and vacancy rates for major retail areas, Q2/2013 vs Q3/2013



Source: Savills Research

sq m to the mid- to high-end retail market, and enlarging total stock by 15%. Compounded by the fact that half of this new supply will be located in emerging retail areas such as Hunnan and non-prime areas such as Tiexi and Beixing, this substantial level of supply is

expected to put downward pressure on city-wide occupancy rates and rents. Landlords will need to become more flexible on leasing terms and rents in order to compete for suitable tenants, particularly considering the amount of oversupply that already exists within the market. ■

TABLE 5

Mid- to high-end retail market key indicators, Q3/2013

	Stock (million sq m)	Vacancy rate (%)	Supply (sq m)	Rental range (RMB per sq m per month)
Q3/2013	4.62	12.6	170,000	250-550
QoQ change (%/ppts)	1.4	-3.1	-	-0.4
YoY change (%/ppts)	3.8	-1.6	-	4.3

Source: Savills Research

TABLE 6

Selected retail leasing transactions, Q3/2013

Tenant	Trade	Project	Location	NLA (sq m)
Tongdelai	F&B	Wanda Plaza	Tiexi	400
Xiyouji	Child-related	Longemont Shopping Mall	Zhongjie	350
AU Hers	Fashion	Joy City	Zhongjie	240
Casio	Watch	Palace 66	Taiyuanjie	200

Source: Savills Research

TABLE 7

Future retail projects, Q4/2013

Project	Retail area	Retail type	Retail GFA (sq m)
Star Mall Shenyang Plaza (星摩尔购物中心)	Tiexi	Shopping centre	150,000
Shenyang Tiandi (沈阳天地)	Municipal Government Square	Shopping centre	62,000
Sunnyworld Centre (阳光百货)	North Station	Department store	100,000
UNI-Mall (中海环宇城)	Beixing	Shopping centre	70,000
Happy Family Mall (兴隆大都会)	Hunnan New District	Department store	105,000
Sunwah IFC (新华国际金融中心)	Municipal Government Square	Shopping centre	90,000
Happy Family (兴隆大家庭)	Taiyuanjie	Shopping centre	105,000

Source: Savills Research

Please contact us for further information**Savills Research****James Macdonald**

Associate Director, China
+8621 6391 6688

james.macdonald@savills.com.cn

Savills Beijing Research & Consultancy**Joan Wang**

Director
+8610 5925 2042

joan.wang@savills.com.cn

**Anthony McQuade**

Senior Director
+8610 5925 2002

anthony.mcquade@savills.com.cn

**Yi Liu**

Associate Director
+8624 8398 5087

yi.liu@savills.com.cn

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