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Savills World Research
Shenyang

Briefing
Office and retail sectors

March 2014

Image: Star Mall Shenyang Plaza, Tiexi district

SUMMARY

In reaction to slowing demand, Grade A office rents fell further in Q4, with yearly growth below 1% in 2013. Meanwhile, city-wide vacancy rose 12.0 ppts YoY due to the slow absorption of new projects.

- Grade A office leasable stock remained unchanged at 708,000 sq m as no new projects were handed over in the fourth quarter.
- City-wide vacancy rates fell 0.6 of a percentage point (ppt) quarter-on-quarter (QoQ) to 19.8%. Occupancy rates fell in most of the older projects, however, as some tenants relocated to recently launched projects.
- Grade A office rents dropped 1.1% QoQ to RMB134.8 per sq m per month (including property management fees), with year-on-year (YoY) rental growth constrained to just 0.5%, the lowest in the past four years.
- Five mid- to high-end retail projects were launched onto the market in Q4/2013, adding 630,000 sq m of retail GFA to the retail market and bringing total retail stock to 5.5 million sq m.
- Prime shopping mall vacancy rates fell to 11.0%, while prime shopping centre first-floor rents increased slightly for the third consecutive quarter to roughly RMB359.4 per sq m per month, representing YoY growth of 2.7%.
- Both the Grade A office and mid- to high-end retail markets are expected to see a substantial level of new supply in 2014, with ten office buildings and eight retail projects scheduled for completion.

"Supported by rising demand from F&B, lifestyle and entertainment retailers, the mid- to high-end retail market witnessed a decrease in vacancy rates, despite five new retail projects debuting in the fourth quarter."

Joan Wang, Savills Research

Economic overview

Echoing the general economic slowdown in China, Shenyang's GDP grew at a real rate of 8.3% YoY. The fixed-asset investment (FAI) YoY growth rate dropped from 26.9% in Q3/2012 to 19.4% in Q3/2013. Real estate investment (REI), however, increased by 16.9% YoY to RMB181.3 billion. Meanwhile, urban residents' disposable incomes per capita and retail sales grew by 10.1% and 13.3% respectively during the same period.

Office market

Market commentary

Shenyang's Grade A office market welcomed a supply peak of 136,000 sq m in 2013, despite no new projects being handed over in the fourth quarter and five projects being postponed to 2014. This large amount of supply, combined with slowing demand in reaction to economic uncertainties, pushed city-wide vacancy rates up by 12.0 ppts compared with 2012. Meanwhile, overall rental growth was less than 1% in 2013.

The oversupply issue is expected to intensify in the next two years, with 19 projects scheduled to be handed over to the market, bringing a total office GFA of 1.9 million sq m. As a result, both city-wide occupancy rates and overall rents are expected to decline due to fierce market competition.

TABLE 1

Macroeconomic indicators, Jan–Sep 2013

Indicators	Units	Value	YoY growth (%)
GDP	RMB billion	522.31	8.3
Foreign direct investment (FDI)	US$ million	4.03	-4.3
FAI	RMB billion	573.74	19.4
REI	RMB billion	181.3	16.9
Retail sales	RMB billion	229.79	13.3
Disposable income per capita (urban)*	RMB	22,090	10.1
Consumer product index (CPI)	PY = 100	102.7	-

Source: Shenyang Statistics Bureau, Savills Research
*Annualised figure.

TABLE 2

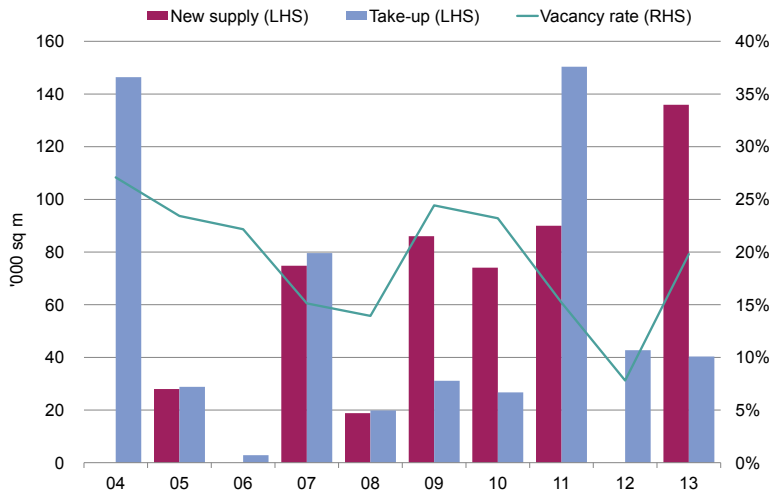
Grade A office market key indicators, Q4/2013

	Stock (sq m)	Vacancy rate (%)	Net Take-up (sq m)	Supply (sq m)	Rent (RMB per sq m per month)
Q4/2013	708,000	19.8	4,000	-	134.8
QoQ change (%/ppts)	-	-0.6	-74.9	-	-1.1
YoY change (%/ppts)	23.7	12.0	-60.9	-	0.5

Source: Savills Research

GRAPH 1

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



Source: Savills Research

Supply, take-up and vacancy rates

No new projects entered Shenyang's Grade A office market in Q4/2013, as five projects, namely Huachen Zhongji Mansion (华晨中际大厦), Lang Qin Tae-won Centre (朗勤泰元中心), Global International Plaza II (环球国际大厦二期), Zhongtie Mansion (中铁大厦) and Maoye Centre (茂业中心), postponed their handover dates to 2014. As a result, Grade A office leasable stock remained unchanged at 708,000 sq m. However, annual supply in 2013 reached 136,000 sq m, an historical high over the past decade.

Net take-up decreased to 4,000 sq m in Q4/2013 from an average of 12,000 sq m in the previous three quarters, largely a result of cautious corporate expansion plans. Demand was mainly seen from the finance (particularly banking and insurance), professional services, IT and high-tech, and bio-tech and pharmaceutical sectors, with domestic companies taking the lead.

Net take-up accumulated to 40,000 sq m in 2013, almost equivalent to that in 2012, but only accounting for 30% of annual supply, leading to an increase in overall vacancy rates.

City-wide vacancy rates fell 0.6 of a ppt QoQ to 19.8%, up 12.0 ppts YoY, although occupancy rates in most of the older projects (buildings older than five years) declined as some tenants relocated to recently launched projects with relatively high-standard building specifications and rental discounts.

Grade A office rents

Given the intensifying market competition due to the large amount of new supply launched onto the market during the first three quarters, landlords of most existing projects maintained the same rental rates as previous quarters or even provided rental incentives to compete for new tenants and to retain existing tenants. Furthermore, some landlords intended to offer rental discounts to facilitate the completion of deals before Chinese New Year, given the slowing demand. Grade A office rents consequently dropped by 1.1% QoQ to RMB134.8 per sq m per month (including property management fees), with YoY rental growth at just 0.5%, the lowest during the past four years.

Submarket vacancy rates and rents

Wulihe

Although it continued to command the highest rents in Shenyang with its cluster of high-quality projects, rents in Wulihe dropped 0.8% QoQ to RMB155.8 per sq m per month (including property management fees), representing a YoY decline of 0.8%. This was largely a result of some landlords offering discounts to retain their quality tenants, given the slowing demand in the locality and new projects being launched in the past few quarters. As a result, Wulihe's vacancy rate was stable at 6.2%, representing a YoY decline of 1.0 ppt.

North Station

North Station, recognised as Shenyang's original CBD, saw rents appreciate by 3.2% YoY to RMB141.8 per sq m per month (including property management fees), still the city's second highest. Vacancy rates rose, however, by 19.0 ppts YoY to 21.5% by the end of Q4/2013 due to the low occupancy at Ping'an Fortune Centre (previously Shenyang Tiandi Tower B), a high-end project handed over in the third quarter.

Office market outlook

Due to the five aforementioned projects postponing their completion dates to 2014, a total of ten projects are scheduled to be handed over this year, injecting a total office GFA of 687,000 sq m into the market, nearly half of which will be clustered in the North Station area. As a result, stock will increase by 97% to around 1.4 million sq m. Additionally, another nine projects with a total office GFA of nearly 1.2 million sq m are expected to be handed over in 2015, increasing current stock by 260%.

Given this substantial level of new supply being released onto a market which is already suffering from oversupply, city-wide vacancy rates are expected to increase significantly. Landlords may have to offer more rental incentives to compete for a limited pool of tenants under fierce competition or may have to consider selling part of their projects to support cash flow, as in the case of Kerry Centre.

Retail market

Market commentary

Shenyang's mid- to high-end retail market welcomed a second historical supply peak in 2013, with five projects debuting in the fourth quarter, bringing a total retail GFA of 630,000 sq m. Despite this, city-

TABLE 3

Selected office leasing transactions, Q4/2013

Company	Project	Location	GFA (sq m)	New lease/ renewal
US Consulate	Maoye City	Wulihe	3,500	New lease
Consulate General of the Federal Republic of Germany in Shenyang	CR Building	Wulihe	2,200	New lease
Daxin Fortune	Shenyang Tiandi	North Station	750	New lease

Source: Savills Research

TABLE 4

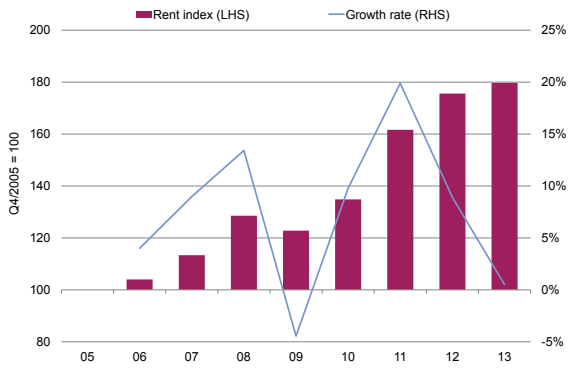
Future office supply, 2014

Project	Business district	Office GFA (sq m)
Huachen Zhongji Mansion (华晨中际大厦)	North Station	51,000
Lang Qin Tae-won Center (朗勤泰元中心)	Zhongshan Square and Heping Avenue	32,500
Global International Plaza II (环球国际大厦二期)	North Station	35,200
Zhongtie Mansion (中铁大厦)	Zhongshan Square and Heping Avenue	40,000
Maoye City (茂业中心)	Wulihe	100,000
Dongda International Center (东大国际中心)	Zhongshan Square and Heping Avenue	116,000
Kerry Center (嘉里中心)	Wulihe	70,000
Shenyang Tiandi Tower A (沈阳天地A塔)	North Station	22,000
Sunnyworld Centre (新地中心)	North Station	120,000
Fortune Plaza II (财富中心二期)	North Station	100,000

Source: Savills Research

GRAPH 2

Grade A office rental index, 2005–2013



Source: Savills Research

GRAPH 3

Grade A office submarket vacancy rates and rents, Q3/2013 vs Q4/2013

Source: Savills Research

wide vacancy rates decreased to 11.0% by the end of 2013, as F&B, lifestyle and entertainment retailers accelerated their expansion plans due to the eagerness of landlords to attract them in order to increase footfall in their projects.

Meanwhile, unlike older department stores, new department stores tend to be built as larger projects to improve trade mix in an attempt to attract customers in a market dominated by shopping malls. This was evidenced by the three new department stores launched this quarter, all of which have retail GFAs of over 100,000 sq m.

Supply and stock

In the fourth quarter of 2013, the oversupply problem in Shenyang intensified as five more mid- to high-end retail developments, including three department stores and two shopping centres, held their grand openings, bringing a total retail GFA of 630,000 sq m onto the market and increasing total stock by nearly 13%. As a result, annual supply in 2013 reached a second historical high of 976,000 sq m, bringing Shenyang's mid- to high-end retail stock to 5.53 million sq m by the end of 2013, 55% of which is shopping centres.

The five new projects are:

Jiu-Guang Department Store

Located in Zhongjie area, Jiu-Guang Department Store was developed by Lifestyle International Holdings Limited, a Hong Kong retail operator. The 120,000-sq m project is positioned as a mid- to high-end department store and held its opening in October 2013. The project is anchored by Fresh Mart (鲜品馆) and has also introduced a series of second-tier luxury and designer brands, many of them new entrants to the local market, including Michael Kors, Kate Spade, Anne Klein and Joan&David. The project also includes a wide range of tenants primarily consisting of fashion, jewellery and F&B retailers. This marks the opening of the second Jiu-Guang Department Store in northeast China and the fourth nationwide following those in Shanghai, Suzhou and Dalian.

Sunnyworld Department Store

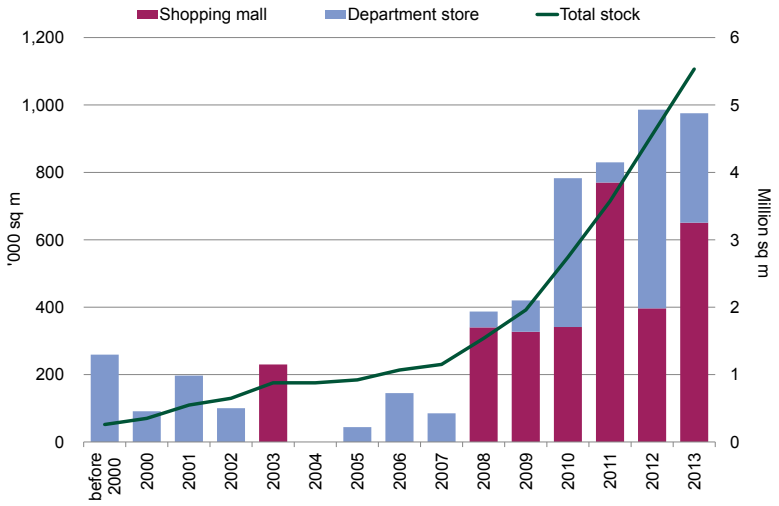
Sunnyworld Department Store is located in the North Station area and opened in November 2013, with a total retail GFA of 100,000 sq m. This project is positioned as a mid-end department store and offers a lifestyle shopping experience by introducing Zhongying International Cinema, EuroJoy Ice Park, a boutique supermarket and an art gallery as its anchor tenants.

Rich Gate Shopping Centre Phase II

Situated in the North Station area, Rich Gate Shopping Center Phase II is the second phase of Rich Gate Shopping Centre, developed by the SRE Group (上海置业集团) and Shenyang Harves Century Group (沈阳华锐世纪集团). The 155,000-sq m project is positioned as a mid-end shopping mall and introduced a number of fast-fashion brands and F&B retailers, such as Gap, H&M, SHANGHAI MIN and Ocean Music Harbon, with CGV and Bile KTV as the anchor tenants. By the end of 2013, this project had achieved a

GRAPH 4

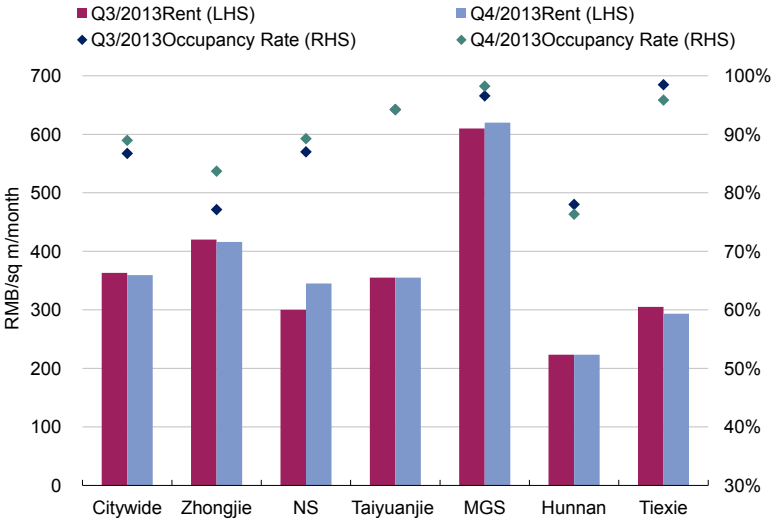
Mid- to high-end retail supply and stock, pre-2000–2013



Source: Savills Research

GRAPH 5

Rental ranges and occupancy rates of major retail areas, Q3/2013 vs Q4/2013



Source: Savills Research
NS = North Station
MSG = Municipal Government Square

pre-leasing rate of approximately 85%.

Star Mall Shenyang Plaza
Star Mall Shenyang Plaza was developed by FIBA Group and Turkmall, with a total retail GFA of 150,000 sq m. This project is positioned as a mid-end mall mainly serving the surrounding residents. Star Mall Shenyang Plaza is anchored by Robbinz Department Stores, Auchan Supermarket, Huayi Brothers Movie and DuoDuo World, and has introduced a cluster of fast-fashion, children's, entertainment and F&B brands, such as Zara, H&M, Gap and South Beauty. By the end of 2013, the pre-leasing rate of Star Mall Shenyang Plaza was as high as 90%.

Xinglong Daduhui
Located in Tiexi district, Xinglong Daduhui is Happy Family Mall's fifth department store in Shenyang. The 105,000-sq m project, which is positioned as a mid-end department store, held its grand opening in Q4/2013. The development is anchored by Carrefour, Decathlon and Worlding Cinema, and has attracted a number of fashion, jewellery and entertainment retailers.

Demand and vacancy rates
Demand from F&B, children's, entertainment (including cinemas, KTVs, ice parks and so on) and lifestyle retailers strengthened as landlords attempted to introduce these tenants with the intention of attracting footfall to their projects. Meanwhile, secondary luxury and designer label retailers also showed interest in prime projects located in traditional retail catchments. Fashion and fast-fashion retailers, however, remained conservative on their expansions, considering the fierce competition between projects and the saturated market.

Although two shopping centres entered the market bringing a large amount of supply, both boasted high occupancies of over 85% due to their prime locations and the extensive retailer relationships of their landlords/operators. As a result, city-wide prime shopping mall vacancy rates fell 2.3 ppts QoQ to 11.0% by the end of Q4/2013, representing a YoY decline of 1.3 ppts.

Rent
Given the increasing competition between projects in the oversupplied retail market, many landlords made compromises on rental rates to secure healthy occupancies. Meanwhile, landlords attempted to introduce F&B, children's, entertainment and lifestyle retailers in order to offer a better experience to local shoppers. In contrast, fashion retailers, which usually have higher affordability, became rather cautious on expansions in the local market.

Consequently, Shenyang's prime shopping centre first-floor rents witnessed stagnant rental growth for the third consecutive quarter, up to an average of RMB359.4 per sq m per month, representing YoY growth of just 2.7%.

Retail market outlook
Shenyang's retail market is expected to experience a substantial level of new supply over the next three years, at an average of 652,000 sq m per annum, consequently enlarging total stock by 35% by the end of 2016. The majority of this new supply is expected to be retail components of mixed-use projects and will be clustered along the Golden Corridor in the Wulihe and Municipal Government Square areas.

Given this large amount of new supply being injected into an already saturated market, Shenyang's mid- to high-end shopping mall rents are expected to further decline as landlords either offer rental incentives to attract suitable tenants, particularly fashion retailers, or commit more retail space to F&B, lifestyle, children's and entertainment retailers, despite their weak rental affordability compared with fashion and accessory brands, to encourage more footfall.

TABLE 5

Mid- to high-end retail market key indicators, Q4/2013

	Stock (million sq m)	Vacancy rate (%)	Supply (sq m)	Rental range (RMB per sq m per month)
Q4/2013	5.53	11.0	630,000	359.4
QoQ change (%/ppts)	12.8	-2.3	82.0	0.9
YoY change (%/ppts)	21.4	-1.3	170.4	2.7

Source: Savills Research

TABLE 6

Selected retail leasing transactions, Q4/2013

Tenant	Trade	Project	Location	NLA (sq m)
DuoDuo World	Children	Star Mall Shenyang Plaza	Tiexi	10,000
H&M	Fashion	Palace 66	North Station	500
Coach	Fashion	Jiu-Guang Department Store	Zhongjie	400
SHANGHAI MIN	F&B	Rich Gate Phase II	North Station	400

Source: Savills Research

TABLE 7

Future retail projects, Q4/2014

Project	Retail area	Retail type	Retail GFA (sq m)
Happy Family Mall (兴隆大家庭（太原街店）)	Taiyuanjie	Department store	105,000
UNI-Mall (中海环宇城)	Beihang	Shopping centre	70,000
Sunwah IFC (新华国际金融中心)	Municipal Government Square	Shopping centre	90,000
Lotte Shopping Center (乐天世界购物中心)	North Station	Shopping centre	300,000
Kerry Center (嘉里中心)	Wulihe	Shopping centre	60,000
Orchard Summer Place (新夏宫购物中心)	Wulihe	Shopping centre	30,000
New World K11 Shopping Center (新世界K11百货)	Wulihe	Shopping centre	300,000
Yifang Plaza (一方广场)	Municipal Government Square	Shopping centre	140,000

Source: Savills Research

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