

Briefing Office and retail

August 2015



Image: Forum 66, Municipal Square

SUMMARY

Grade A office rents saw an overall downturn in 1H/2015 due to the entrance of new projects. City-wide vacancy rates rose 30 percentage points to 47.7% by the end of 1H/2015, the highest for a decade.

- With four projects, totalling 507,000 sq m, handed over to the market, Shenyang's Grade A market leasable stock increased to 1.4 million sq m.

- Grade A office vacancy rates increased 30 percentage points (ppts) year-on-year (YoY) to 47.7%.

- Shenyang's net take-up reached 113,000 sq m by the end of 1H/2015, up 169.4% YoY due to the influx of new supply.

- Grade A office effective rents fell 1.6% half-on-half (HoH) to RMB135.8

per sq m per month (including the property management fees).

- Only one retail project was launched onto the market in 1H/2015, replacing an existing space recently vacated by two department stores, leaving total retail stock at 5.73 million sq m.

- Prime shopping centre first-floor rents saw a decrease of 0.9% HoH to RMB367.0 per sq m per month.

- Shenyang is expected to receive three new projects in 2H/2015, adding more than 373,000 sq m of retail space to the market.

“As the retail market continues to show no significant signs of recovery, landlords continue to feel the pressure. Looking to attract tenants, landlords continued to offer rental incentives, resulting in prime shopping centre first-floor rents witnessing a decrease of 0.9% half-on-half to RMB367.0 per sq m per month.” Jack Xiong, Savills Research

→ Economic overview

China's GDP growth slowed to 7.0% in 1H/2015, while Shenyang's GDP growth rate also narrowed to 3.8%. Shenyang's total investment in fixed assets amounted to RMB319.2 billion, down 11.0 ppts YoY. Real estate investment amounted to RMB75.06 billion, falling 32.4% year-on-year (YoY). Boosted by the spring festival, retail sales totalled RMB183.26 billion in the first half of 2015, up 8.1% YoY.

Office market

Market commentary

The Shenyang Grade A office market welcomed a supply peak of 507,000 sq m in 1H/2015, sending a shockwave through the market. By the end of 1H/2015, city-wide vacancy rates had increased 18 ppts HoH to 47.7%. As the new projects were of Grade A standard, rents remained relatively flat despite the influx of supply.

Supply, net take-up and vacancy rate

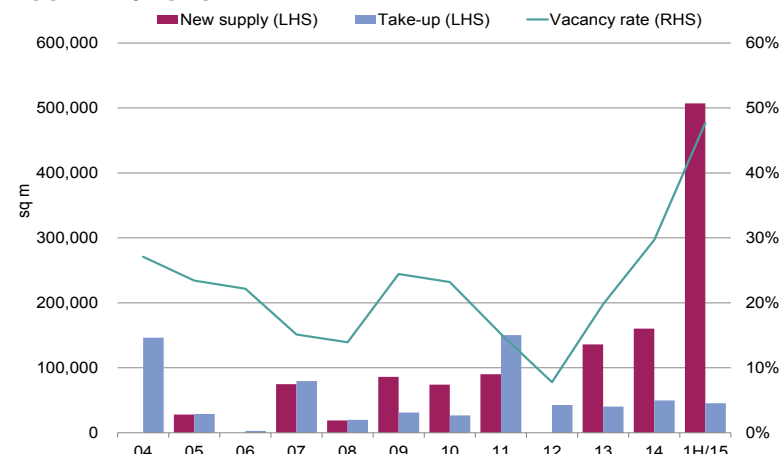
Supply

Four new projects - Sunnyworld Centre, Fortune Plaza Tower A, Tongfang Plaza and Forum 66 Ph I - entered the market in 1H/2015, contributing 507,000 sq m to the Grade A office market. As a result, stock reached 1.4 million sq m.

Sunnyworld Centre, located in North Station area, was handed over in January 2015. The project was developed by Sunny World Group. It is the first project in Shenyang to adopt an under-floor air distribution system, with a built-in PM2.5 cleaning system. Many well-known companies have taken-up space in Sunnyworld Centre, including Olympus and Threebond.

Fortune Plaza Tower A, also located in the North Station area, was developed by Yingtena Group - one of Shenyang's local companies. As a large portion of the project will be held by the landlord for lease, only a small section will be for sale, with most of the tenants expected to buy at least one whole floor. Tenants include China Securities and Aeon Life.

GRAPH 1 **Grade A office supply, net take-up and vacancy rate, 2004-1H/2015**



Source: Savills Research

TABLE 1 **Macroeconomic indicators, 1H/2015**

Indicators	Unit	Value	YoY growth (%)
GDP	RMB billion	334.22	3.8
Foreign direct investment (FDI)	US\$ billion	0.54	-69.9
FAI	RMB billion	319.2	-11.0
REI	RMB billion	75.06	-32.4
Retail sales	RMB billion	183.26	8.1
Disposable income per capita (urban)	RMB	18290	6.5
Consumer product index (CPI)	PY = 100	100.9	-

Source: Shenyang Statistics Bureau, Savills Research

TABLE 2 **Northern China Grade A office market main indicators, 1H/2015**

	Beijing	Tianjin	Shenyang	Dalian	Qingdao
Stock (million sq m)	9.94	0.61	1.40	1.10	1.53
HoH change (%)	2%	-	57%	-	4%
YoY change (%)	5.8%	18.8%	88.7%	-	10%
New Supply (sq m)	150,000	-	510,000	-	58,000
HoH change (%)	-62.2%	-	237.8%	-	-27.8%
YoY change (%)	168.2%	-	1,460%	-	-
Vacancy	4.1%	24.0%	47.7%	8.3%	19.3%
HoH change (% ppts)	-0.7	-3.9	18.0	-0.5	1.5
YoY change (% ppts)	0.6	5.9	30	-1.6	1.9
Rents (RMB per sq m per month)	319.1	141.9	135.8	124.8	102.8
HoH change (%)	0.2%	-0.2%	-1.6%	-1.4%	-0.1%
YoY change (%)	1.7%	0.8%	-1.7%	0.5%	1.4%

Source: Savills Research

→ Tongfang Tower is located in the centre of Hunnan Olympic Central, a non-core area in Shenyang. It was also developed by a local company, Shenyang Tongfang Co. Harbor. The launch of this project has met the demand previously disappointed by the lack of Grade A projects in Hunnan area, attracting a number of famous companies such as Digital China and Turck.

Forum 66 was developed by Huanglung Properties, well-known for a number of high-quality properties in China. Forum 66 is 350 m high and is a representative landmark of Shenyang. Known for its high-quality, Forum 66 attracted a large amount of well-known companies, such as the Hokkaido Bank and Medtronic. It is the second project in Shenyang developed by Huanglung Properties, after Palace 66.

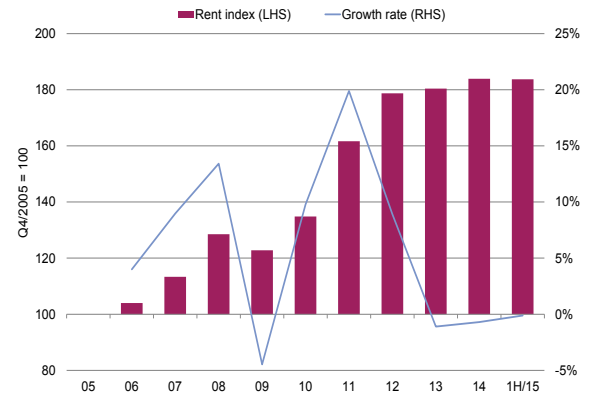
Vacancy Rate and Take-up

City-wide vacancy rates rose dramatically to 47.7% in 1H/2015, up 30 ppts YoY. Major business areas saw a similar trend, with Municipal Government area vacancy rates increasing 47 ppts YoY to 53%. This

rise can be attributed to, firstly, the influx of supply causing oversupply in the market as each project was over 100,000 sq m. Secondly, due to landlords handover strategies, some space within these projects was held back from the market, leaving a large amount of vacant space. As a result, the projects' vacancy rates are expected to remain elevated in the short term. Lastly, the tenant base was relatively limited, with most tenants relocating from older buildings.

Prior to this year, Shenyang's Grade A office market stock was limited, with high occupancy rates in Grade A office projects. To some extent, this situation

GRAPH 2 **Grade A office rental index, 2005 – 1H/2015**



Source: Savills Research

TABLE 4 **Selected office leasing transactions, 1H/2015**

Company	Project	Location	GFA (sq m)	New lease/renewal
Medtronic	Forum 66	Municipal Square	400	New lease
Hengchang	Sunnyworld Centre	North Station	500	New lease
Sumitomo Mitsui Banking Corporation	Forum 66	Municipal Square	1,000	New lease

Source: Savills Research

TABLE 3 **New supply, 1H/2015**

	Sunnyworld Centre	Fortune Plaza Tower A	Forum 66	Tongfang Plaza
Location	North Station	North Station	Municipal Government Square	Municipal Government Square
Landlord	Sunny World Group.	Yingtena Group.	Huanglung Properties	Tongfang Co. Harbor
Grade	Grade A	Grade A	Grade A	Grade A
Leasable office GFA (sq m)	100,000	100,000	190,000	117,000
Floor plate (sq m)	2,000	2,000	2,000-3,000	2,000
Asking rent (RMB per sq m per year)	1,240	1,640	1,640	1,036
PM Fee (RMB per sq m per month)	30	30	30	22

Source: Savills Research

→ had suppressed the leasing market demand. However, as new projects entered the market, this problem was solved. Moreover, to attract high-quality tenants, some of the landlords opted for competitive leasing plans, stimulating leasing demand. Therefore, city-wide net take-up reached 113,000 sq m in 1H/2015, up 169.4% YoY. Demand drivers of the market included companies from the financial sector, which is still relatively active in terms of expansion plans.

Grade A office rents

Due to the large amount of supply in 1H/2015, competition between landlords intensified. A continued influx of supply is expected to enter the market over the next three years, likely to result in many landlords losing bargaining power with tenants, making it more difficult to apply rental increments. As a result, Grade A office effective rents fell 1.6% HoH, to RMB135.8 per sq m per month (including the property management fees).

Submarket vacancy rates and rents

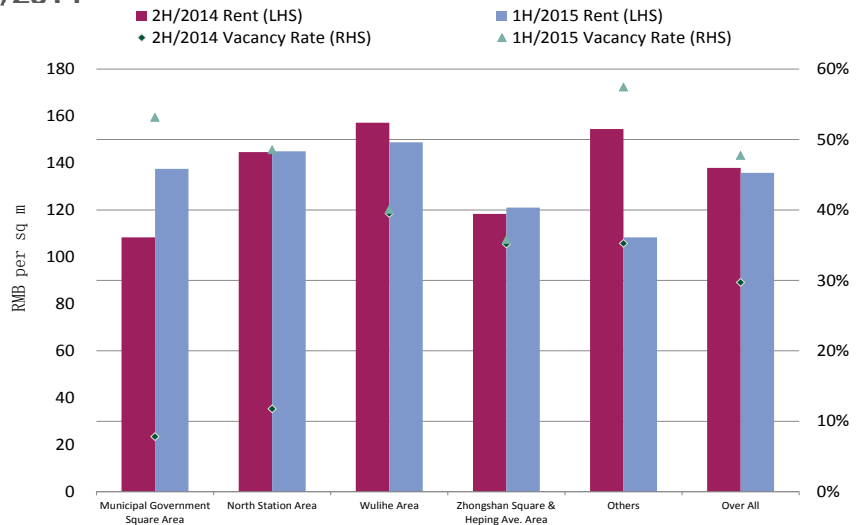
- Wulihe area
Wulihe area continued to command the highest rents in Shenyang in 1H//2015, due to the amount of high-quality projects in the area. By the end of 1H//2015, Wulihe area rents were recorded at RMB148.8 per sq m per month (including management fees). Vacancy rates remained high, increasing 0.6 of a ppt HoH to 40.1%.

- Municipal Government Square area
The Municipal Government Square area witnessed a period of adjustment in 1H/2015. The launch of Forum 66 increased both overall rents and vacancy rates in the area. By the end of 1H/2015, Municipal Government Square area rents were recorded at RMB137.5 per sq m per month (including management fees). Vacancy rates also rose dramatically, by 47 ppts YoY to 53%.

Office market outlook

Shenyang's Grade A office market is expected to welcome a peak supply in 2H/2015, with six new projects

GRAPH 3 **Grade A office submarket vacancy rates and rents, 1H/2015 VS 2H/2014**



Source: Savills Research

TABLE 5 **Future project focus**

	New World K11	Forum 66 Ph II
Location	Wulihe	Municipal Square
Completion date	2017	2017
Landlord	New World Properties	Hanglung Properties
Grade	Grade A	Grade A
Leasable office GFA (sq m)	320,000(total GFA)	470,000
Floor plate (sq m)	2,000	2,000-3,000
Asking rent (RMB per sq m per month)	TBC	TBC
PM Fee (RMB per sq m per month)	TBC	TBC

Source: Savills Research

TABLE 6 **Future office supply, 2H/2015**

Project	Business district	Office GFA (sq m)
Youyi Times Plaza (大连友谊)	Wulihe Area	54,000
Zhongtie Mansion (中铁大厦)	Zhongshan Square & Heping Ave. Area	40,000
Orchard Summer Place (夏宫城市广场)	Wulihe Area	60,000
North Yorker Plaza (北约克置地广场)	Zhongshan Square & Heping Ave. Area	100,000
Maoye City (茂业中心)	Wulihe Area	100,000
Rich Gate Phase II (华府天地二期)	North Station Area	200,000

Source: Savills Research

entering the market and adding a total office GFA of 554,000 sq m, enlarging stock by 40%.

Over the next two years (2016-2017), nearly 1.2 million sq m of new supply will be handed over to the market, intensifying the oversupply problem. As a result, both the city-wide occupancy rates and rents are likely to face downward pressure in the short-term. In response to the heightening competition, landlords will likely have to offer more rental incentives to compete for the limited tenant base, with some even considering selling part of the projects to boost cash-flow.

Retail market

Market commentary

Due to the lack of supply entering the market in 2014, Shenyang's mid- to high-end retail market has remained flat. Due to brand homogeneity and competition from O2O, competition within the retail market intensified, causing some projects to postpone completion dates.

Supply and stock

Only one project, Xinglong 100, was officially handed over to the market in 1H/2015, adding 105,000 sq m to the market and bringing Shenyang's mid to high-end retail GFA to 5.73 million sq m.

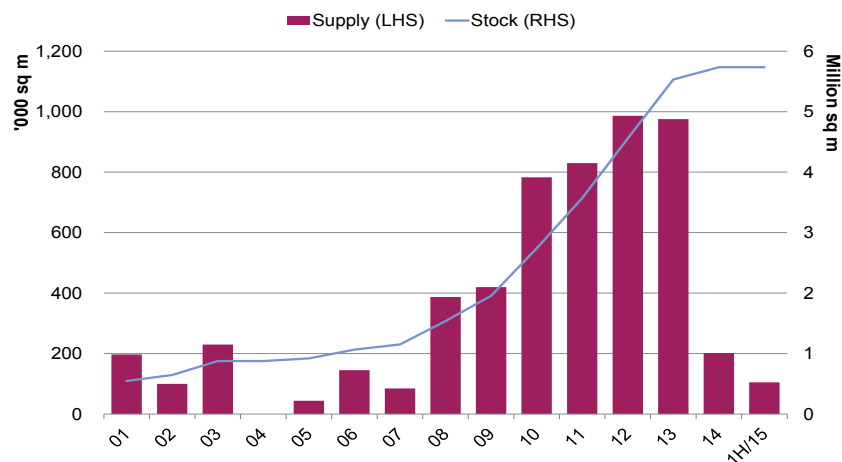
- Xinglong 100

Xinglong 100, located in Taiyuanjie, is Happy Family Mall's sixth department store in Shenyang. The project has taken over the space vacated by New Mart and ISETAN Department Store. Positioned as a mid-end department store, the 105,000-sq m project is anchored by its supermarket and introduces a number of fashion, accessory and entertainment retailers.

Demand and vacancy rates

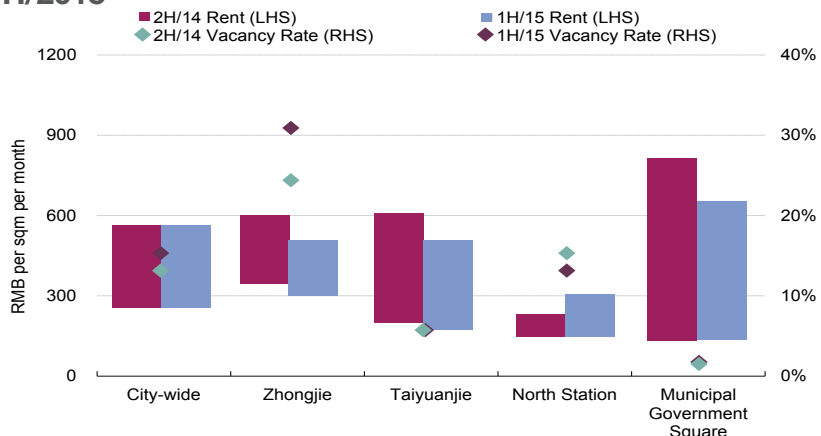
Demand from traditional fashion brands (even fast-fashion brands) has begun to weaken. However, as landlords push to attract higher footfall to their projects, F&B, child-related, entertainment (including theme cinema, KTV etc.) and lifestyle

GRAPH 4 Mid- to high-end retail supply and stock, 2001-1H/2015



Source: Savills Research

GRAPH 5 Rental ranges and vacancy rates for major retail areas, 2H/2014 vs 1H/2015



Source: Savills Research

TABLE 7 Northern China mid- to high-end retail market indicators, 1H/2015

	Beijing	Tianjin	Shenyang	Dalian	Qingdao
Stock (million sq m)	10.10	3.30	5.70	2.40	3.05
HoH change (%)	1%	6%	2%	6%	18%
YoY change (%)	12%	4.2%	2%	16%	22%
New Supply (sq m)	140,000	200,000	110,000	130,000	460,000
HoH change (%)	-84.7%	33.3%	-	-33.3%	247.7%
YoY change (%)	208.7%	124.2%	-48.0%	-	-
Vacancy rate	5.6%	17.2%	18.4%	4.1%	22.2%
HoH change (%ppts)	1.1	1.4	1.6	-0.3	0.8
YoY change (%ppts)	0.4	0.5	1.5	1.2	1.3
Rents (RMB per sq m per month)	902.4	398.6	367.0	407.9	431.3
HoH change (%)	-0.5%	-1.1%	-0.9%	1.7%	1.6%
YoY change (%)	0.3%	-5.9%	1.0%	6.0%	1.9%

Source: Savills Research

retailers are becoming the market drivers.

Vacancy rates of the prime shopping malls increasing by 1.5 ppts YoY to 18.4%. However, due to an anchor tenant in Rainmaker Plaza terminating their contract, Zhongjie area vacancy rates rose by 5.4 ppts HoH to 20.4%.

Rent


Due to increased competition in the retail market in recent years, landlords have begun to lose bargaining power. By the end of 1H/2015, Shenyang's prime shopping centre first-floor rents witnessed stagnant rental growth, decreasing 0.9% HoH to RMB367.0 per sq m per month.

Retail market outlook

In 2H/2015, Shenyang is expected to receive three new projects, adding more than 373,000 sq m of retail space to the market. A large portion of the supply expected in the second half of 2015 is located in prime retail areas such as Zhongjie and the Golden Corridor. In decentralised areas such as Tiexi Square, the 120,000-sq m MixC will be launched onto the market in 2H/2015, upgrading the overall retail ambience in the area.

In the next two years (2016-2017), eight projects are expected to be completed, adding nearly 900,000 sq m to the market. Most of the new supply will be located along the Golden Corridor. Additionally, due to such a substantial level of future supply, city-wide shopping mall vacancy rates are expected to climb. In order to compete in an increasingly hot market, landlords are expected to begin offering more incentives in order to attract suitable tenants and may also allocate more space to F&B, lifestyle, children-related and entertainment retailers in order to generate more footfall. ■

TABLE 8 **New retail supply, 1H/2015**

Xinglong 100	
	
Location	Taiyuanjie
Opening date	Q1/2015
Retail GFA (sq m)	105,000
Retail type	Department Store
Floor	B2-8F
Tenant mix	Fashion, F&B, child-related, supermarket and lifestyle retailers.
Major tenants	Nike, Adidas, Puma



Source: Savills Research

TABLE 9 **Selected retail leasing transactions, 1H/2015**

Tenant	Trade	Project	Location	GLA (sq m)
MCM	Fashion	Dun an One Mall	Zhongjie	400
Luyu	F&B	Palace 66	Zhongjie	300
YoYoTo	Children	Palace 66	Zhongjie	600

Source: Savills Research

TABLE 10 **Future retail project focus**

	New World K11 Shopping Center	Lotte Shopping Center
		
Location	Wulihe	North Station
Retail GFA(sq m)	320,000 (total GFA)	178,000
Retail type	Shopping mall	Shopping mall
Opening date	2017	2017

Source: Savills Research

TABLE 11
Future retail projects, 2H/2015

Project	Location	Retail type	Retail GFA (sq m)
Yifang Plaza (一方广场)	Wulihe	Shopping centre	140,000
MixC City (华润万象汇)	Tiexi Square	Shopping centre	120,000
Avenue of Stars (星汇广场)	Zhongjie	Shopping centre	113,000

Source: Savills Research

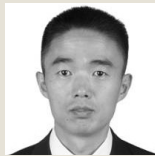
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