

Briefing Office sector

August 2015



Image: Xi'an Center, High-tech Zone, Xi'an

SUMMARY

The Xi'an Grade A office market is currently going through a period of upgrade, with an influx of new, high-quality supply which is expected to change the distribution patterns of stock in the city.

- By the end of 1H/2015, Xi'an's Grade A office market total stock reached nearly 400,000 sq m.

- Grade A office rents in Xi'an reached an average of RMB116 per sq m per month, while vacancy rates were recorded at 8.5% – less than other major western cities such as Chengdu and Chongqing during the same period.

- Drivers of demand in the market include the financial services, manufacturing, real estate, professional services and retail industries.

- Over the next three years the Grade A office market is expected to receive 1.33 million sq m of supply, a supply peak in the market.

"The rapid development of Xi'an's economy has generated increasing demand within the office market. Although the lack of supply has created a tight market, the upcoming influx of supply is expected to create a new wave of pressure from increased competition."

Dave Law, Savills Research

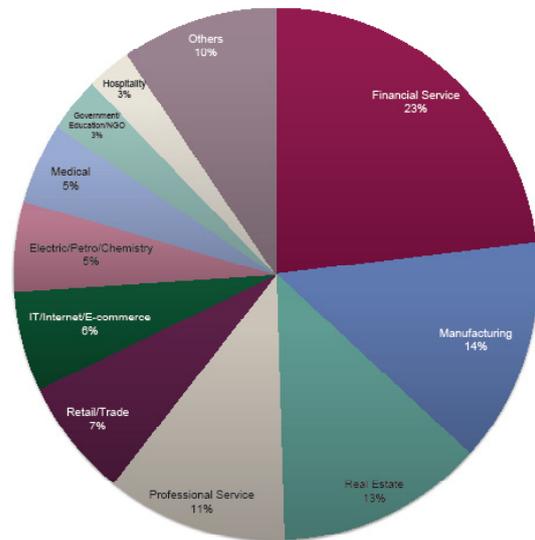
➔ **Market overview**

Xi'an, the capital of Shanxi Province, is a core city of the Guanzhong-Tianshui Economical Zone and the political, economic and cultural centre of the northwest region of China. Since the implementation of the Western Development Policies in 2000 due to the "One Belt and One Road" (OBAOR) strategy, Xi'an has seen a rapid development of its economy, which can be attributed to its prime location, and cultural, scientific and education-based focus. In the first half of 2015, its GDP grew 7.6% year-on-year (YoY), 0.6 of a percentage point (ppt) higher than the national average level.

Benefiting from continuous improvement to its infrastructure and the rapid development of the overall economy – especially tertiary industries – the Xi'an office market is constantly upgrading. Since 2000, nine Grade A office projects have entered the market, and by the start of 2015 Grade A office stock was 390,000 sq m, across 14 buildings. However, the total supply is relatively small, and is behind the supply of other main cities in the western region of China, such as Chengdu and Chongqing.

The lack of Grade A office supply in Xi'an has created much hype around high-quality projects in the area, leading to high rents and low vacancy rates. In the second quarter of 2015, Grade A office average rents reached RMB116 per sq m per month, similar to levels seen the same time last year. Vacancy rates were recorded at 8.5%, down 10.5 ppts YoY. In both of these factors, Xi'an performed better than other core western cities such as Chengdu and Chongqing. Similar to most of the other developing cities in China, dispersed ownership projects are the main part of the Xi'an Grade A office building market at 56%, and a total of 560,000 sq m.

GRAPH 1 **Xi'an Grade A office market tenant mix (1H/2015)**



Source: Savills Research

TABLE 1 **List of Prime office buildings in Xi'an, 1H/2015**

Project	Region	GFA (sq m)	Launch date
Zhongda International	Downtown	7,500	2000
High-tech International Business Center	High-tech Zone	48,000	2004
Chang'an International (A/B/C/D)	Downtown	46,660	2005
China Merchant Bank Building	High-tech Zone	63,960	2008
Gate of City (C/B)	High-tech Zone	112,000	2010 / 2013
Linkai International	High-tech Zone	46,000	2011
Northwest International Financial (E/F)	North	17,600	2012
China Overseas Building	Qujiang	20,440	2013
CapitaMall Office	2nd Ring Road & Xiaozhai	33,600	2013

Source: Savills Research

TABLE 2 **Comparison of the Grade A office market in Chengdu, Chongqing and Xi'an, 1H/2015**

City	Office GFA (sq m)	Rents (RMB per sq m per month)
Xi'an	390,000	116
Chengdu	2.21 million	99
Chongqing	1.35 million	107

Source: Savills Research

Xi'an is, of course, one of the most famous tourist cities in China, and as such, tertiary industries comprise over half of the whole economy. Tourism, retail and associated businesses are booming, whereas secondary industries and the manufacturing sector are already relatively developed. Office tenants are mainly financial services firms, companies from the manufacturing sector, and professional services providers.

Grade A office tenants are typically private enterprises, accounting for over 50% of the total. Foreign-related firms (including multinational companies, foreign governments and Sino-foreign joint ventures) account for about 30%, indicating the city has a long history as the first choice for foreign firms in northwest China.

Regional Characteristics

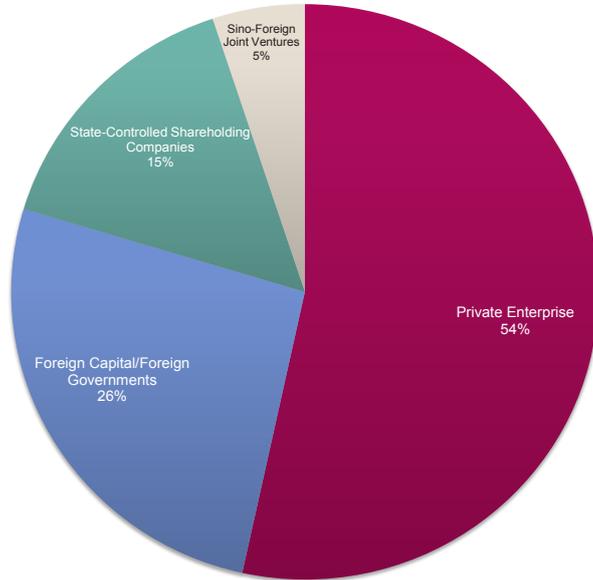
The Grade A office market is centralised in five regions: Downtown; High-tech Zone; 2nd Ring Road South and Xiaozhai; North; and Qujiang. The High-tech Zone is the most significant in terms of Xi'an's industrial development strategy.

Downtown

As the earliest developed area of Grade A office buildings in Xi'an, current stock now stands at approximately 45,000 sq m. Key projects include Zhongda International and the Chang'an International Center.

Benefiting from the advantageous location and high-quality surrounding amenities, the area records the highest rents and lowest vacancy rates, at RMB150 per sq m per month and 3.7%, respectively. Key tenants include companies from the financial, retail and high-tech manufacturing industries. However, due to aging facilities within older buildings and traffic congestion in the downtown area, tenants have begun to relocate to other areas,

GRAPH 2 Capital Source Structure of Tenants in the Xi'an Grade A office market (1H/2015)



Source: Savills Research

MAP 1 Distribution of Grade A office buildings in Xi'an



Source: Savills Research

causing a 1.6% YoY decline in rents and vacancy rates to rise 3.7 ppts YoY. Additionally, limited land supply and strict protection policy of properties with a long history has restricted the supply of Grade A office buildings in this area. As a result, no new Grade A office

projects are expected to be launched in the next three years.

High-tech Zone

As one of the first national-level high-tech zones, this area has attracted a large number of multinational

corporations, including Huawei, IBM, ZTE and Samsung, to set up their production and R&D centres.

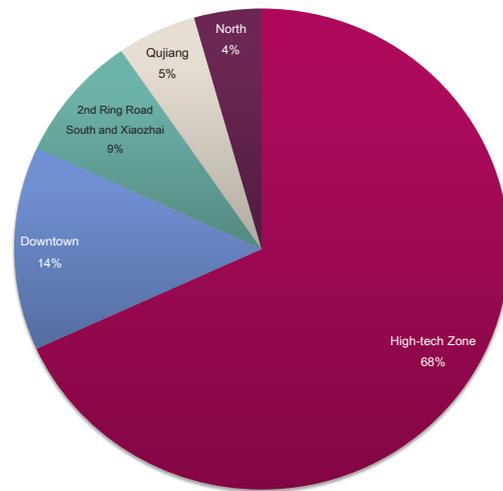
The High-tech Zone area can be divided into two phases. Phase 1 is centred around Tangyan Road and Tech Road. As the government continuously accelerates the development of the high-tech industry, land supply within Phase 1 is becoming more limited. The economical and regional development of the whole high-tech zone is expanding to the south (Phase 2), with a number of projects totalling 700,000 sq m. This is equal to half the future supply expected to enter the overall market before 2019. Key projects within Phase 2 include Greenland Center Plaza, with Greenland Center A and B, the Yongli International Financial Center, the Maike International Center and Xi'an Center.

Current stock in the High-tech Zone has reached 270,000 sq m, making it the largest market in terms of stock in Xi'an. Due to regional policy advantages and the industry clustering effect, the area performs quite well, with average rents reaching RMB114 per sq m per month – up 4.6% YoY – while vacancy rates are 7.8%, down 2 ppts YoY. Main tenants include companies from the financial and professional services sectors, as well as high-tech manufacturing industries.

In the second half of 2015, Xi'an Center is expected to enter the market, adding 130,000 sq m.

2nd Ring Rd South & Xiaozhai
 Located between Downtown and the High-tech Zone, this is one of the earliest developed business areas in Xi'an. Currently this area benefits from convenient transportation systems and a mature business atmosphere. However, this area mainly consists of Grade B office buildings, with a shortage of Grade A office buildings. Capital Square is the only

GRAPH 3 Supply of Grade A office building in Xi'an (1H/2015)



Source: Savills Research

MAP 2 Business Area Expansion in the High-tech Zone



Source: Savills Research

GRAPH 4 Rents and Vacancy Rates by district in Xi'an (1H/2015)



Source: Savills Research

Grade A office project in the area, at approximately 34,000 sq m. However, CapitaMall Office Phase 2, Momopark and the Xi'an International Center are all expected to enter the market in 2016, 2017 and 2018 respectively, adding 320,000 sq m of supply, which equals more than a quarter of total future supply expected to enter the overall market.

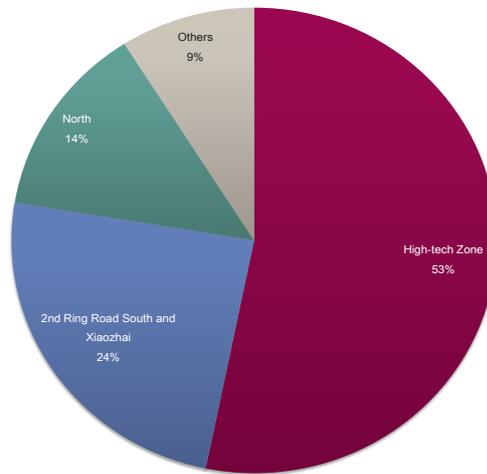
North

The North is a national-level economic and technological development area, benefiting from access to transportation links such as the high-speed railway line, metro (line 2) and the Xi'an Xianyang International Airport. As a result, this area has become a new hub for office space, also attracting many government organisations that have relocated to the area. Key projects include the Northwest International Financial Center E&F, which has attracted a large number of state-owned corporations and multinational corporations.

Although the area continues to have prestige as being a national-level economic and technological development area, many tenants are starting to relocate as other areas of the city begin to offer a more fast-paced, incentive-driven atmosphere; rents and occupancy rates have begun to decline. In the second quarter of 2015, rents fell 5.3% YoY to RMB90 per sq m per month, while occupancy rates were recorded at 14%, down 4.4 ppts YoY.

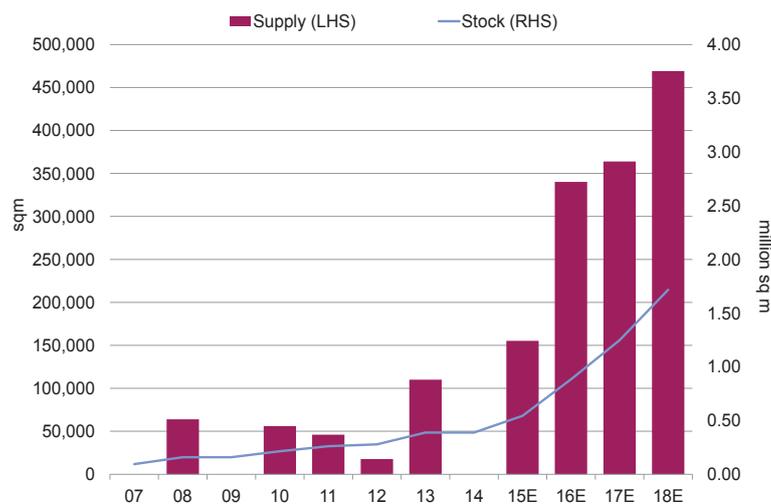
With support from government planning, the North area will be one of the most concentrated supply regions. At least 180,000 sq m will enter the market before 2019, including Vanke Baldur, the Zhengshang International Financial Center and Haiyue Plaza. Northwest International Financial Center Building D is expected to enter the market in the second half of 2015, adding 25,200 sq m. As a result of a

GRAPH 5 **Distribution of future supply by district (2015 - 2018E)**



Source: Savills Research

GRAPH 6 **Xi'an Grade A office building supply (2007 - 2018E)**



Source: Savills Research

slowing economy, and in turn lower demands for office buildings, new projects in this area have delayed their launches, leading to a slower overall development of the area.

Qujiang

Qujiang is a new business district designed to be led by the tourism and cultural industry, due to the famous historical sites in the area. As many developers are attracted by policies offered by the government, the office market in this area has developed

rapidly. However, most buildings in the area are of Grade B standards. The demand-drivers of the area, including not only tourism and cultural-related companies but also business incubators and start-ups, do not typically have high requirements for office space. The only Grade A office project in the area is the Zhonghai Building, totalling 20,000 sq m. Main tenants are architecture companies and transportation and financial services companies. Average rents in the area reached RMB90 per sq m per month,

while vacancy rates now stand at 22.2% – the highest vacancy rates in Xi'an. Over the next three years, no new Grade A supply is expected to enter the area, leading to less competition and, therefore, vacancy rates are expected to decrease further.

Market outlook

The Grade A office market is expected to receive three new projects totalling approximately 290,000 sq m in Q3/2015. The increased supply is expected to prompt developers to not only provide preferential measures such as extending rent-free periods and lower rents, but also other value-added services to differentiate themselves. This shift in focus to meeting changing supply pressures may also provide inspiration to developers for Grade A office building operations.

As a very important city along the Silk Road, alongside the presentation and action of the OBAOR strategy, Xi'an has a huge advantage over other cities in the area, and will drive the upgrade of the overall economy, and in turn, the overall office market. During the next three years, the supply of Grade A office space is expected to reach over 1.33 million sq m. Of this supply, the High-tech Zone region will receive the largest portion – comprising over 50% of the total – while the Downtown district will suffer a shortage. However, the distribution of new supply will be more concentrated after 2016. A significant upgrade of supporting facilities and management of properties is expected to heighten the experience of office tenants and push up the quality of the overall market. This will create fierce competition for existing stock.

In the second half of 2015, two projects are expected to enter the market totalling 155,000 sq m – including Northwest International Financial Center D and China Railway Xi'an Center. Northwest International Financial Center D, though only 25,000 sq m, is expected to see a longer period of absorption due to the slowing growth of the economy. Xi'an Center has a total office GFA of 130,000 sq m, which is equal to half of the area's current stock. As a result of the scale of the project and the fact that High-tech Zone Phase 2 is still in its infancy, vacancy rates are expected to remain high in the area. ■

Please contact us for further information

Savills Research

Savills Project Development & Consultancy Savills Agency



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



Dave Law
 Senior Associate Director
 +8628 8665 7375
 dave.law@savills.com.cn



Eric Wo
 Managing Director
 +8628 8658 7828
 eric.wo@savills.com.cn



Backy Fung
 Director
 +8628 8658 7841
 backy.fung@savills.com.cn

Savills plc

Savills is a leading global real estate service provider listed on the London Stock Exchange. The company established in 1855, has a rich heritage with unrivalled growth. It is a company that leads rather than follows, and now has over 600 offices and associates throughout the Americas, Europe, Asia Pacific, Africa and the Middle East.

This report is for general informative purposes only. It may not be published, reproduced or quoted in part or in whole, nor may it be used as a basis for any contract, prospectus, agreement or other document without prior consent. Whilst every effort has been made to ensure its accuracy, Savills accepts no liability whatsoever for any direct or consequential loss arising from its use. The content is strictly copyright and reproduction of the whole or part of it in any form is prohibited without written permission from Savills Research.