Briefing
Office sector

June 2016

Image: Chang'an International Center, Downtown, Xi'an

SUMMARY

Since the second half of 2015, three projects, including High Tech Zone No.9, have been handed over, adding 95,000 sq m and increasing total stock to 477,000 sq m. The economic downturn has turned net absorption negative, increasing vacancy rates and driving rents down.

- Since Q2/2015, the Xi'an Grade A office market has received 95,000 sq m of space; total stock stands at approximately 477,000 sq m.
- Net absorption has declined to -20,000 sq m as a result of the current economic situation and a rising trend of companies purchasing office space for self-use.
- City-wide vacancy rates rose 18.6 percentage points (ppts) year-on-year (YoY) to 27.1%.
- Average rents continued to decline, falling 3% YoY, to RMB108.25 per sq m per month.
- In the coming year, the Xi'an Grade A office market is expected to receive 400,000 sq m of new supply.

"Compared to Chengdu, Chongqing, or even Kunming, Grade A office stock in Xi'an is relatively sparse, making the vacancy rate relatively stable. However, a forecast supply surge is expected to significantly increase stock, leading to imbalances between supply and demand."
Dave Law, Savills Research & Consultancy

Market overview

In Q1/2016, Xi'an's GDP reached RMB116.64 million, a growth of 8.1% YoY. This is 1.4 ppts above the national average and 0.5 ppts higher than the provincial rate. The tertiary industry achieved the highest annual growth rate of 8.6%, adding RMB75.71 billion to the economy. City-wide fixed asset investment growth turned positive in Q1, reaching RMB58.11 billion, up 0.8% YoY, including RMB23.21 billion worth of real estate investment, a 1.2% increase YoY.

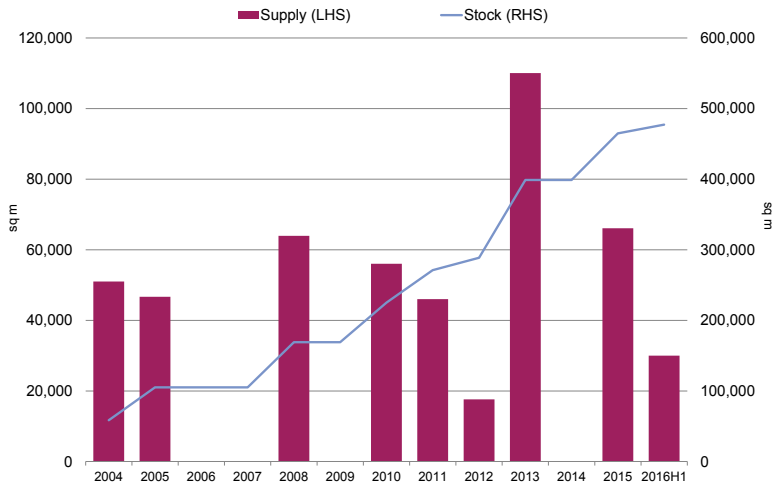
Since the second half of 2015, 95,000 sq m of space has been handed over across three projects, including High Tech Zone No. 9, which raised city-wide Grade A office stock to 477,000 sq m. A myriad of factors, namely slowing economic growth and office space purchases by end-users, has pushed net absorption into the negative, to -20,000 sq m. The average vacancy rate increased 18.6 ppts YoY, to 27.1%.

City-wide rents continued to fall, declining 3% YoY, to RMB108.25 per sq m per month. Rents in the High Tech Zone declined the steepest, by 5.4% in the same period.

Financial services and management and consulting firms remain the main sources of new demand, although IT, internet, and e-commerce companies also remain active in the office market. Industries that have been hit hardest by the economic slowdown – architecture, manufacturing and construction – make up the greatest percentage of tenants leaving Grade A office spaces.

GRAPH 1

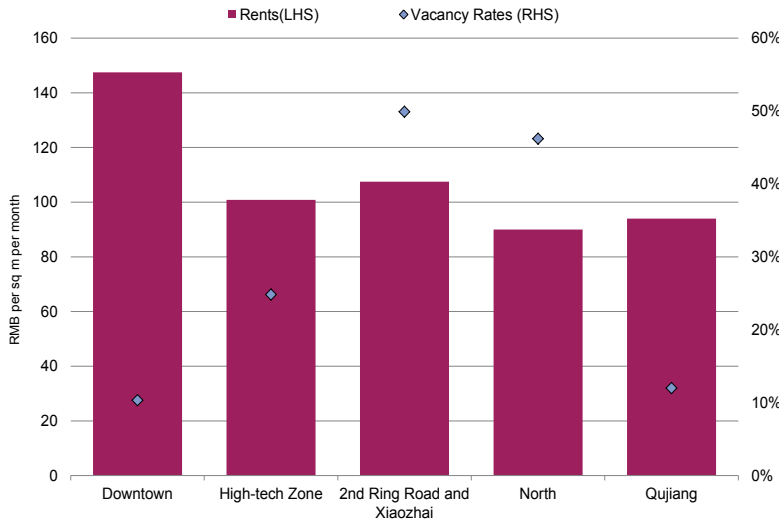
Xi'an Grade A office supply and stock, 2004-1H/2016



Source: Savills Research

GRAPH 2

Xi'an Grade A office Rents and Vacancy Rates by district, 1H/2016



Source: Savills Research

Downtown

In addition to the traffic congestion and the relatively older age of projects generally found in the Downtown area, the implementation of regional industrial policies and better availability of new, high-quality projects in neighbouring business districts have quickened the relocation of many tenants from the Downtown area to emerging districts. In the last year, the net absorption of this area was -3,620 sq m, while vacancy rates rose 6.6 ppts YoY, to 10.3%. Rents declined slightly to RMB147.5 per sq m per month, down 1.8 ppts YoY.

Due to limited land supply, the Downtown area is not expected to receive any new supply in the next year.

High Tech Zone

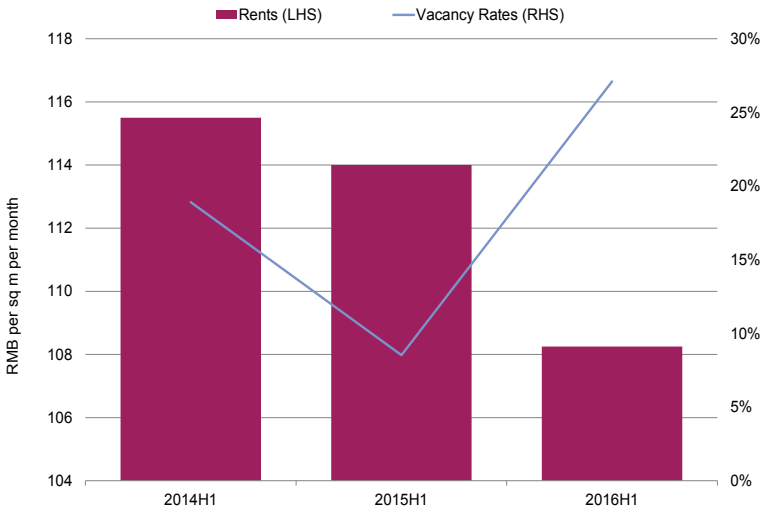
The largest of the city's submarkets market has been adversely affected by the economic slowdown. Net absorption now rests at -16,000 sq m, while vacancy rates rose 17 ppts YoY, to 24.8%. Rents in the area fell 5.4 ppts YoY, to RMB100.83 per sq m per month.

2nd Ring Rd South& Xiaozhai

In Q2/2016, CapitalMall Office II entered the market, bringing 30,000 sq m of new supply, nearly doubling the submarket's total stock to 64,000 sq m. As a result, vacancy rates skyrocketed to 49.9%. However, with no supply expected in the coming year and occupancy rates on the rise, rents are expected to remain stable, around RMB107.5 per sq m per month.

GRAPH 3

Rents and Vacancy Rates of Xi'an Grade A office market, 2004-1H/2016



Source: Savills Research

The High Tech Zone is expected to receive a large supply influx of over 400,000 sq m in the coming year, which is expected to decrease rents further.

North

In Q3/2015, Northwest International Financial Center D entered the market, with roughly 25,000 sq m of office space. The current vacancy rate is 46.2%, and rents average RMB90 per sq m per month

In the next year, the handover of Lafonce is expected to bring another 50,000 sq m onto the market. Faced with the lack of potential for regional industrial development, absorption rates in this area are expected to come under greater pressure.

Qujiang

The China Overseas Building was handed over in Qujiang last quarter. However, due to the scarcity of supply, vacancy rates decreased 10.2 ppts, to 12%. Simultaneously, the average rent rose 4.4 ppts, to RMB94 per sq m per month, making Qujiang the only area to see rental appreciation in the current market environment.

In the next year, Daxia International Center will enter the market, adding about 46,000 sq m of space.

Market outlook

As a key city in the Silk Road Economic Zone, Xi'an is expected to undergo a new wave of economic and industrial development which will ultimately benefit the development of the local office market. However, a supply influx of more than 1,400,000 sq m, roughly 294% of current stock, over the next three years will increase pressure on the office leasing market in the short term.

Growing competition will force property owners to adopt more efficient operating strategies and fully utilise resources from multiple channels, which will improve the overall quality and attractiveness of projects.

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