HEADWINDS & OPPORTUNITIES

China Property Market 2018 Review and 2019 Outlook

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2018 proved to be a challenging year for China economically as the government got serious about tackling some of the imbalances in the economy that have persisted in recent years—chief among these was the financial de-risking by cracking down on informal lending channels while also restricting credit availability in order to deleverage the corporate world. This would have proved challenging and painful at the best of times, but it was exacerbated by the start of a trade war with the United States. In addition, the greater regulatory oversight of tech companies and weakness of the stock market and you would expect the economy to be in freefall; nevertheless, while there is continued weakness in a number of smaller cities, leading first- and second-tier cities have remained firm.

Office markets from Beijing to Guangzhou and Chengdu have seen vacancy rates falling and rents improving while others—seeing excess supply—have found it more difficult to increase rents.

Retail markets continue to struggle with rising competition from numerous online or omni-channel competitors, but the more experienced are reinventing their value proposition by continually changing their tenant mix, introducing hot new brands and experimenting with technologically advanced interactive displays and working with, rather than resisting, online platforms.

The logistics market continues to go from strength to strength, with a rise in parcel deliveries and increasing demand for quality and timeliness, as well as expansion to cross border ecommerce and cold chain logistics as FMCG sales are increasingly online.

Hotels have not only seen a renaissance in boutique experiential travel and wellness, outdoor and sports-related segments but also in city centres younger, more modern segments of leading cities like Shanghai where occupancy rates and ADRs are starting to rise.

The residential market continues to yoyo back and forth, not only on depending on the policy environment but also the availability and cost of mortgages. As pricing flatlines and volumes fall, overextended developers are finding themselves desperate for a white knight or a change in policy. The residential leasing market has overheated with too much money deployed into immature operational platforms to service a relatively new market that is still too small to accommodate the sudden surge in supply.

Investment was sluggish at the start of 2018 but picked up towards the end of the year as developers were rushing to meet sales targets and investors were desperate to deploy raised capital. Domestic insurers and foreign funds have a larger share as domestic funds find financing more challenging and returns fail to meet expectations. Should the real estate market continue to cool in 2019, many investors are hoping to pick up distressed opportunities or diamonds in the rough amongst the rising NPL portfolios.

Niche markets, especially the healthcare and data centre sectors continue to attract interest from investors seeking higher returns and less competition, though they come with higher risk profiles and a longer investment horizon more appropriate for PE, developers and insurance companies than funds.

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China’s economy has grown dramatically over the last twenty years from RMB325 billion in 1977 to RMB11.1 trillion just before China’s ascension to the WTO in 2001 and then up to RMB82.7 trillion in 2017. When China’s economy was relatively small, its impact on the global economy was commensurately small; however, with the increasing size and might of the Chinese economy, the impact of decisions made in China have on the global economy and country economies is likewise considerable. The international community—especially the United States—is imploring China to adhere to international norms of trade and market access. Also, given the reliance upon the Chinese economy that some countries have, there are concerns that China’s economic might could be weaponized to achieve economic or strategic goals and hence some countries are treating these issues as national security concerns.

With this all said, trade and economic relations between China and other countries are likely to continue to change as the balance of power shifts. There is likely to be increased and sustained pressure on China to open markets and increase transparency in its policymaking. International companies involved in cross-border trade should expect increased uncertainty and volatility as politics affects ongoing business concerns, while other sectors of the market may be increased to overseas competition. Nevertheless, China will end up doing what is in China’s best interests as all other nation states also do. Sectors of the economy will open at a time and manner of China’s choosing, either opening markets when local incumbents already have a dominant position or when local competitors need to hone their skills in preparation for international expansion.
Debt Burden

One of the modern era’s biggest systemic risks is debt. This is not specific to China but as in many China’s current circumstances have arisen faster and vaster than in many other countries. According to the Bank of International Settlements, China’s debt to GDP stood at 253.1% by June 2018 (US$33.1 trillion, RMB219 trillion) having stood at just 138.4% at the end of 2008 (US$6.5 trillion, RMB44 trillion). While 253% may seem like a lot, this is comparable to many developed countries UK (280%), US (249%), Australia (235%) and Japan (370%).

The biggest concern is not how much debt there is, especially as most of it is domestically held and therefore less prone to currency fluctuation, but how quickly we have arrived here and the increasing reliance that companies place on increasing debt availability. Even if the total debt-to-GDP ratio doesn’t contract, the mere fact that it is not growing is in some cases is enough to create significant stress as we saw over the last 12 months. Other issues include a lack of transparency, oversight of the shadow banking sector (something that was actively addressed in 2018), an inability to properly asses risk and therefore price debt, policy-directed lending often overriding best market practices, the lack of a mature enough equity markets as a viable alternative for company fundraising and particularly high levels of debt for non-financial corporations.

These are all pressing concerns that the government is taking steps to address; however, the issues are large, interrelated and incredibly complex and resolving or just alleviating some of these situations will take time and patience and will cause significant discomfort, including but not limited to, slower economic growth, corporate bankruptcies, market consolidation and asset repricing. Progress is likely to prove slow as other issues impede the ability progress to be made; however, the long-term trend is likely to prove more constant.
Serviced offices have been around for decades, while co-working has been more recent. Both these have focused on the peripheries of the corporate world—either targeting representative offices, start-ups, freelancers, and in some cases, SMEs. Both platforms offer immediate occupation, flexible lease terms, minimal capex, as well as a range of services, events and shared amenities and sometimes a business community, mentorship and exposure to VCs.

In recent years, operators, emboldened by the acceptance of the business model and successful fundraising rounds, have expanded aggressively beyond their original scope of service, taking on larger premises, targeting larger corporate occupiers and offering tailor-made real estate solutions packages. As they continue to expand their scope, they are starting to encroach upon the core businesses of what once were their partners—landlords and brokers. Now, their partners are starting to push back. Landlords are beginning to offer an expanded range of services and amenities—like breakout areas—to tenants while others are establishing their own co-working spaces within their buildings that offer the flexibility of immediate occupation and flexible lease terms as well. Brokers are expanding their tenant targeted offerings by expanding from their traditional, lease-negotiation, lease portfolio management, project management and facility management services to include partnerships with landlords to provide flexible workspaces.

With more established operators adopting an increasing number of traits of flexible spaces, the impact of WaaS is likely to be more profound, broader and longer-lasting than previously envisaged. The adoption of WaaS comes at a time when economic growth is slowing but the pace of change in the corporate world is accelerating. In these cases of dynamism and uncertainty, to tie a corporate to a long-term lease with only limited opportunities for an expansion or contraction of headcount would be nonsensical.
Tech & Data

The property sector, long seen as the industry least touched or disrupted by technological innovations, is, at last, starting to embrace technology.

Online brokerage platforms such as Anjuke, Fang.com have matured over time from residential brokerages to commercial brokerage platforms while platforms such as Taobao are even marketing large-scale investment opportunities. These platforms have also expanded into the management of for-lease residential properties through platforms such as Ziroom and Yizu, providing the landlords not just with listings but full management and tenants can download an app that enables them to unlock their doors, pay rent and contact property management.

E-commerce platforms continue to capture market share and expand to new categories while making inroads into physical retail spaces. Technology is also automating consumer experiences from unmanned retail stores and drone deliveries to facial payments and VR retail stores. While the application of some of the initial tech might have left something to be desired in terms of consumer experience, as the tech and knowhow improve it should become less prominent and subtler, enhancing rather than replacing shop assistants. Meanwhile, tech adoption has recently focused more on consumer engagement and brand experience versus inexact automation.

As tech disrupts the retail market it creates opportunities and challenges for the logistics market with lower costs and improving efficiency and consistency.

Technology is making its way into our homes as smart home devices manufacturer Xiaomi continues to increase its range of offerings after its recent HK IPO and partnership with IKEA and other tech companies such as Alibaba and Baidu getting in on the smart speaker market pioneered by the likes of Apple, Google and Amazon. Similar companies are also beginning to cooperate with district and city government by leveraging the vast amounts of data from IoT sensors, mobile devices and a plethora of other sources to enhance security, regulate traffic and better distribute resources.

One of the biggest gains from the adoption of new technology is the digitization of the human physical experience and the generation of copious amounts of information which, if properly stored, categorized and analyzed, can inform our understanding of how individuals interact with the physical environment and therefore how the physical world can be better redesigned to meet the needs of society. This may be in the form of closed loop systems, AI optimisation and human design.
Housing

The residential market is incredibly important in China with some estimates stating that it accounts for one-fifth to one-third of economic growth and roughly two-thirds of a family’s assets. However, China has been trying to cool the market and wean itself off the reliance on the residential property market in recent years. This comes with the now standard range of policy tools including restricting mortgage availability, house purchase restrictions, control over pre-sale permit pricing and tightening up land auction processes and requirements. The hope is to cool price appreciation and therefore maintain or improve housing affordability as incomes continue to rise while avoiding a price correction which would see household wealth shrink. While price appreciation is controlled, transaction volumes are still supported to enable developers to monetise their investments and either pay down debt or reinvest and generate continued economic growth and employment.

The latest iteration of property cooling measures has taken an extra turn with the support of the development of the residential leasing market, which while started in 2016 and gained significant momentum in 2018. The leasing market is expected to improve affordability, increase mobility and encourage individuals to invest in alternative asset classes which contribute to the real economy—like equity markets or business startups—and, at the same time, create employment and make more efficient use/absorb current vacant residential stock. As the leasing market matures, there is the potential for a more diverse, multifaceted leasing market that caters to specific communities such as student housing or senior housing.
As wages continue to rise and returns on fixed investment diminish, it was hoped that the consumer market would usher in a new era of economic growth for China, moving towards more international norms where household consumption accounts for roughly 50-70% of the economy from its current level of 35-40%.

There are now concerns that, despite household debt levels remaining relatively low at 50.3% of GDP by June 2018, this figure has risen too quickly on the back of the increasing mortgage issuances and little consumer debt and it is starting to have a drag on expenditure. This is especially true as Chinese interest rates remain amongst the highest out of developed economies, and debt servicing is taking up an increasing amount of households’ disposable income, limiting their ability to consume products and services.

There is also the issue of financial deleveraging, greater regulation of the consumer financing internet platforms and a collapse of the P2P market while the ongoing trade war with the United States, a slowing domestic economy, flat lining residential market and weak equity markets have all weighed heavily on consumer sentiment.

The real retail sales growth rate has slowed from 13.0% at the end of 2012 to 7.8% at the end of 2017 and by November 2018 had reached just 5.8%. While part of this as a result of comparing against a larger base, the slowdown in retail sales has been faster than the slowdown in the economy—a poor omen for the retail sector.

Despite slowing retail sales growth rates, new opportunities continue to emerge, and domestic brands are meeting changing consumer needs, especially in the affordable range with the likes of many specialty coffee brands and electronic brands such as Huawei and Xiaomi. New business models are created that offer comparable quality to existing brands but with significant cost saving.
CITIES

Performance of Office and Retail Property Market in 2018

WUHAN
- Office:
  - Supply: 389,700 sq m
  - Rental Growth: 2.0%
  - Vacancy: 32.9%
- Retail:
  - Supply: 137,000 sq m
  - Rental Growth: 2.8%
  - Vacancy: 6.8%

XI’AN
- Office:
  - Supply: 112,000 sq m
  - Rental Growth: -2.2%
  - Vacancy: 30.1%
- Retail:
  - Supply: 1,228,000 sq m
  - Rental Growth: 1.5%
  - Vacancy: 3.8%

CHENGDU
- Office:
  - Supply: 216,700 sq m
  - Rental Growth: 4.1%
  - Vacancy: 21.0%
- Retail:
  - Supply: 489,300 sq m
  - Rental Growth: 1.5%
  - Vacancy: 4.5%

CHONGQING
- Office:
  - Supply: 41,400 sq m
  - Rental Growth: -2.4%
  - Vacancy: 35.9%
- Retail:
  - Supply: 615,000 sq m
  - Rental Growth: -0.2%
  - Vacancy: 12.4%
BEIJING
Office
Supply 520,037 sq m
Rental Growth 10.9%
Vacancy 7.0%
Retail
Supply 500,000 sq m
Rental Growth 2.9%
Vacancy 7.7%

GUANGZHOU
Office
Supply 207,400 sq m
Rental Growth 11.2%
Vacancy 4.3%
Retail
Supply 418,000 sq m
Rental Growth 1.2%
Vacancy 11.5%

TIANJIN
Office
Supply 357,500 sq m
Rental Growth 0.2%
Vacancy 33.8%
Retail
Supply 418,000 sq m
Rental Growth 1.2%
Vacancy 11.5%

NANJING
Office
Supply 61,800 sq m
Rental Growth 1.4%
Vacancy 11.0%
Retail
Supply 636,100 sq m
Rental Growth 3.9%
Vacancy 5.5%

SHANGHAI
Office
Supply 1,411,000 sq m
Rental Growth 0.3%
Vacancy 18.6%
Retail
Supply 900,400 sq m
Rental Growth 1.3%
Vacancy 6.8%

HANGZHOU
Office
Supply 310,000 sq m
Rental Growth 2.1%
Vacancy 19.5%
Retail
Supply 739,000 sq m
Rental Growth 0.2%
Vacancy 9.3%

SHENZHEN
Office
Supply 620,000 sq m
Rental Growth 0.7%
Vacancy 10.3%
Retail
Supply 530,000 sq m
Rental Growth 0.2%
Vacancy 1.2%
Shanghai likes to think big, really big. Not happy with the largest office market in China, having sailed past Hong Kong and usurped Beijing in recent years, Shanghai is setting its eyes on more than doubling the size of its office market by 2035.

This may seem counterintuitive when looking at the 2035 City Plan that was launched in 2018, which looks to limit Shanghai’s new construction land and constrain population growth to 25 million people. Nevertheless, the city is exploring a more effective way of using its existing land resources with urban rejuvenation a key focus of city development.

Despite the growing presence of TMT, finance and consumer focused companies, advanced manufacturing is still very important to Shanghai. Industrial land currently accounts for roughly 27% of the city’s construction land and 30% of the transacted land between 2016 and 2018, nevertheless while a few leading companies such as Tesla, Pepsi and SAIC enjoy 50 years land usage rights, most only have 20 years with renewals subject to negotiation.

Industrial parks are also evolving to better reflect and meet the new needs of the advanced manufacturing and business community. Two mature industrial areas: Zhangjiang and Jinqiao, which historically have had a number of office/campus/headquarter/R&D facilities are now positioned as city sub-centres more akin to Wujiaochang and Huamu, than their erstwhile peers. Indeed, landmark buildings over 250m high are planned in the two industrial parks challenging the market’s conventional wisdom.

With more modern planning concepts, industrial parks will gradually evolve into more mixed and dynamic spaces for work, life and leisure.

The reimagining of industrial parks will contribute to the continuing expansion of more traditional businesses enabling the city to reach its unofficial goal of having 25-30 million sq m of Grade A office space by the end of 2035 up from 13.6 million sq m in 2018. This would catapult it to comparable scale to some of the largest markets in world at the moment, namely New York and other leading global cities.

Some may be concerned about Shanghai’s ability to absorb all the new supply, given stronger competition for corporate headquarters from some of China’s other first-tier cities as well as the city becoming less attractive to new talent given hukou related restrictions and rising residential costs. Nevertheless, as the integration of the Yangtze River Delta is elevated to a national strategy, Shanghai has the potential to increase the competitiveness of the whole metropolitan area through closer connection with neighbouring cities. More importantly, Shanghai must establish as a leading platform for global resources to enter China despite increased trade protectionism around the world.
Since 2011, Beijing has replaced Shanghai as the most expensive office market in Mainland China. Grade A office rents in Beijing Financial Street—the heart of China’s financial system—are now higher than Chuo Ward in Tokyo and Marina Bay in Singapore.

Financial and tech companies continue to flock to Beijing. By the end of 2018, financial institutions’ deposit in Beijing is 34% higher than Shanghai, accounting for 9% national total. From 2012 to 2018, a total of 29 unicorn companies were born in Beijing, including Xiaomi (US$30bn) and Didi (US$80 bn) significantly more than its peers in Asia. The capital’s influence is magnified through its marriage of financial power with rapid technological innovation.

The tertiary sector’s contribution to GDP is the highest in the country at 82%, providing a strong base of demand for the office market. Net absorption totalled 540,000 sq m in 2018, higher than annual supply, pushing down vacancy rates (some of the lowest in the country) even further. Grade A office rents have responded to market conditions, increasing for seven consecutive quarters as landlords maintain the upper hand in negotiations.

Nevertheless, uncertainty is growing. Future office supply will focus on the core area of the CBD and Lize Business District, but development progress has been slower than expected and tenants are reticent to move to new locations which lack supporting amenities, infrastructure and services while being surrounded by construction sites. Should new supply continue to be postponed, leasing activity in the prime markets is expected to slow as tenants stay put.

Softening demand could also rain on Beijing’s parade. Finance, IT and professional services are Beijing’s three key pillars of office demand, accounting for 69% of total leasing transactions in 2018. As the economy slows, market access and trade frictions persist and stricter financial regulation abound a number of companies are becoming more fiscally conservative—indicating a potential decrease of affordability.

Should market fundamentals continue to deteriorate in 2019, the office market may no longer be able to defy gravity as it has done so successfully in the last couple of years. Both tenants and landlords need to be prepared for the changing market.
Shenzhen is home to mainland China’s most expensive residential market, having attained this title in 2015 after seeing prices rise by almost 40% in just one year. The market however has remained remarkably robust and threatened to begin rising again in 2018 amid increasing focus on the greater bay area and the potential economic windfall it could bring. In order to forestall further potential price hikes the government issued a number of preventative measures to cool the warming market.

Despite pre-existing property restrictions, strong end-user and pent-up investment demand pushed up transaction volumes through the first three quarters of 2018, reaching 650,000 sq m, 840,000 sq m, and 980,000 sq m, respectively for the three quarters. However, since the release of the “731 policy” in July which restricts the ability for individuals to flip properties within three years of purchase or to use corporate shell structures, more potential home buyers adopted a wait-and-see attitude leading to a decline of transaction volume in Q4/2018. Total residential transaction volume reached 3.0 million sq m in the first eleven months of 2018, down 0.4% YoY while average transaction prices remained stable at RMB57,000 per sq m, down 0.7% YoY.

In the serviced apartment market, occupancy rates fell by 2.6 ppts YoY to an average of 80.3% by the end of 2018. Long-stay serviced apartment tenants tend to be expatriates and senior executives of MNCs, especially IT and trading companies. Additionally, many of the 98 Fortune 500 companies registered in Shenzhen are American and Japanese. Given deteriorating ties between China and the US, highlighted by the trade war, working visa issues and rising economic uncertainties, a number of expatriates and senior executives are reassessing their accommodation needs, leading to a decrease in serviced apartment demand.

While it might be expected that as the economy slows, so the prospects for the housing market would dim, though the weakened economic environment may in fact spur the government to move to a more relaxed policy environment for the market in the hope that it would lead to a stable performance of the property market. Future policies are likely to focus on maintaining stable growth in the property market and building a more robust housing and leasing market, while the serviced apartment market will likely see two new projects launching in 2019, bringing more quality stock to the market.
Guangzhou’s office market recorded one of its best years in 2018 both in terms of leasing and investment, made even more remarkable by the weakening of many other markets in China in response to oversupply and weakening demand. Guangzhou has now recorded two consecutive years in which demand has exceeded supply and hence dragged down vacancy rates. Net take-up reached 412,000 sq m in 2018, largely thanks to several notable new leases and space consolidations. Citywide vacancy rates responded by falling 4.3 ppts YoY to 4.3%, the lowest level in over a decade.

Leasing demand came from a wide array of industries, led by TMT, financial, professional services, manufacturing, biomedical, and IT sectors. In addition, co-working space operators also demonstrated a strong appetite for office space. Rents increased 11.2% in 2018 to an average of RMB190.9 per sq m per month. Zhujiang New Town outperformed other submarkets with its rents surging by 14.3% YoY. Pazhou also witnessed rapid rental growth as a result of strong demand triggered by some sizeable leasing deals.

The office investment market was also more active compared to the previous two years as the city’s office market entered the investment radar of many overseas and domestic institutional investors. Enquiry volume and investment and divestment activities increased throughout the year, with three en bloc investment deals concluded in 2018. More deals could have been concluded; however, there still remains a significant price difference between sellers and potential buyers. Despite strong investment demand and capital value growth investment yields have been pushed out in recent quarters as rental growth outpaced that of capital values.

The outlook for Guangzhou’s office market remains positive for the foreseeable future, underpinned by the formation of the Greater Bay Area and the long term economic benefits it is expected to achieve. These gains are in large part expected to flow from the continued investment in fixed assets, particularly infrastructure, that will be needed to integrate the city markets together (such as the Guangzhou-Shenzhen-Hong Kong High-Speed Railway), but also increased business activities that will result from increased connectivity among all major cities within the GBA.

Guangzhou will continue to be a landlord market as vacancy rates are expected to remain relatively low, and possibly below 10% for the next four to five years at least. 2019 is expected to see 536,000 sq m of new supply completed in 2019. Should all the supply hand over as scheduled it should offer some relief for tenants; however, it is unlikely to dramatically alter the market conditions in the short term. Rents are still expected to grow steadily, albeit at a slightly slower pace, in 2019, which should lend further support to the growth in capital values.
Chengdu has undergone extraordinary transformation since 2008 with the compound annual GDP growth rate over the last decade reaching 11.2%. Heavy investment into infrastructure over this period helped to drastically improve the city's road and metro network and enabled the city to expand into virgin territories.

The city is now seeking more quality and sustainable growth. In 2018, Chengdu launched the “Garden City” strategy, becoming one of the first cities in China to emphasize greenways and liveability in a planning document. By the first half of 2018, the city has built 1,585 km of greenways, around 10% of the total planned length. Greenways not only link urban life and parks but also introduced cultural, sports, entertainment and tourism facilities, in order to bring social and environmental benefits in a more sustainable and meaningful way.

As a key part of the Garden City planning, Longquan Mountain is positioned as the Central Greenland of Chengdu, which is expected to help drive the development of the city’s eastern areas.

More meticulous development of the land along metro lines has also been brought to the agenda. Chengdu is the city with the longest metro length under construction and is expected to operate a total of 13 metro lines—650 km—by 2020. The Garden City strategy encourages TOD (Transit-oriented Development) to optimise land use, incorporating mixed-used functions into the development projects.

The future property market will also need to focus on the development of higher quality and standard projects. In the retail market we are already starting to witness several small boutique projects coming to the market, differentiating from the traditional large-scale shopping malls and providing more diversified options to shoppers. Through closer connection with adjacent public spaces and communities, boutique projects hope to provide an alternative future direction for retail development and property management.
Chongqing’s economy reached RMB1.5 trillion in the first nine months of 2018, up 6.3% in real terms but a pace that was 3.9 ppts lower than the same period in 2017. The secondary industry saw growth slow 6.3 ppts to just 3.7% over the same period, but the tertiary industry (accounting for over half the economy) grew by 8.9%. Fixed asset investment and manufacturing, the previous drivers of Chongqing’s economy, are now faced with increasing challenges and are dragging down the growth of the whole economy.

With the growth formula for the previous decade broken, Chongqing now stands at a crossroads, looking for drivers, such as artificial intelligence and big data, to take the economy forwards over the next decade and beyond.

Varying paces of development for different industries have already started to have an impact on the office market. TMT and professional service companies replaced manufacturing as the key driver of demand for office space in 2018, while the fintech sector is shrinking as a result of stricter governance and co-working and sublease operators aggressively expand into Grade A office buildings. With vacancy rates remaining stubbornly high at 35.9% and intensifying competition from operators, a number of landlords have become more cautious when selecting co-working operators.

The retail market, meanwhile, is focused on absorbing vacant stock that increased after the market received 900,000 sq m of retail space in 2017. While supply moderated to just 615,000 sq m in 2018, the city remains over retailed and highly fragmented with competition between decentralised locations rising. Even prime locations, such as Jiefangbei, are struggling with increasing vacancy rates and stagnant rental growth.

The good news is that Chongqing is quickly developing its tourism industry. There have been 11 billion clicks on Chongqing related videos on Douyin/Tik Tok by mid-2018, 27% higher than Xi’an (one of the country’s key tourist cities). Chongqing also attracted a total of 410 million tourists in the first nine months of 2018, up 10.8% YoY. The question now is how to translate this boom in tourism into increased retail sales, something that all market practitioners should be thinking about.
Nanjing has in the past had one of the most competitive land markets in China. Nanjing recorded the first and third highest land sales revenues figures among all Chinese cities in 2016 and 2017 respectively, with several areas witnessing record high transaction prices. However, as the economy started to slow and access to debt became more challenging in 2018, land premiums began to slide. Developers are now faced with the dilemma of either selling at a lower price than they previously envisaged or waiting for the market to recover which requires a significant financial commitment and is still full of uncertainties.

Residential supply increased 96% YoY in the first 11 months of 2018 while transactions only increased 1%. The average selling ratio of properties is 64%, significantly lower than the 79% recorded in 2017. While transaction prices are remaining stable for the time being, market sentiment tends to be less positive. More developers are partnering up to bid for new land plots in order to lower their development risk and reduce financial pressure.

2019 is expected to be a big year for Nanjing’s office market with a total of 452,000 sq m of new supply scheduled to be added to the market including IFC and Golden Eagle World. Nanjing Financial City’s handover in 2019 is expected to lead to the further improvement of the business environment in Hexi. The quality of co-working space on offer in Nanjing is also set to improve as more mature operators enter the market, such as Shui On’s InnoSpace, while Baisitting project has started construction.

The continued development of the co-working market should help stimulate or at least facilitate the growth of the city’s innovative spirit, the entry of leading hi-tech companies such as Alibaba and Xiaomi will also likely attract more talent to the city. As China seeks to grow domestic consumption and innovation, Nanjing’s future remains bright, backed by rich educational resources and a well-developed industrial infrastructure.
Despite being one of the most popular tourist destinations in mainland China, Hangzhou is increasingly recognized as a tech-savvy city. Over the last decade tourism's contribution to GDP fell from 15% to 8% while the information-related economy increased to 25%. The output from the e-commerce industry has consistently grown by over 20% for the last eight years.

As the home town of Alibaba, Hangzhou has witnessed the rise of numerous companies that feed off the business empire that is Alibaba. These companies are either start-ups that are invested in or have at some point spun off from one of the world's largest internet companies. Strong relationships with the local government and Chinese willingness to experiment with new technologies mean that many new gadgets are popping up around the city, especially internet-related tech such as autonomous convenience stores, mobile payment, mobile tax payments or hospital appointment booking systems.

Technology is seen as a catalyst for the growth of Hangzhou's economy and is shaping the city's office and retail market in a very particular way. Start-ups, entrepreneurs and technology companies' desire for campus-style office space has led to the development of several low-rise business parks in decentralised areas while quality office supply in the city centre remains rather limited. Nevertheless, the growth of the tech sector has led to increasing demand from other companies looking to provide services to these tech companies, such as real estate brokerage firms, though more likely to be located in more traditional city centre locations. Hangzhou's office vacancy rate despite recording one of the lowest rates among second-tier cities at 16% by the end of 2018, has seen vacancy rates rise in recent quarters with rising distress and closures of P2P companies of which Hangzhou was home to quite a few.

While companies such as Alibaba grew out of the boom of the e-commerce industry, technological innovations are finding their way back into the bricks and mortar world while many online players amongst others are keen to establish a foothold in the birthplace of Alibaba. Nevertheless, overall rental growth in Hangzhou remains tepid with the city having a lack of experienced international developers until recently, potentially indicating that there might be room for improvement.

With many technology companies, Hangzhou is a mecca for investment capital. Tech in Hangzhou is not just limited to Alibaba and a handful of tech start-ups—indeed many have survived the VC stages and have gone on to receive significant capital injections. Often when tech companies reach a certain scale, valuation or maturity they transit from leasing office space to acquiring headquarter buildings. Hangzhou was home to 20 unicorns (companies valued over USD1.0 billion) by the end of 2018. As these and others make the transition from renting to owning there could be a significant rise in investment for self-use.
Wuhan became the first city in central China to have an economy larger than RMB1.0 trillion in 2014. By 2017 Wuhan’s economy had grown to RMB1.34 trillion and in the first three quarters of 2018 reached RMB1.1 trillion, up 8.3% YoY.

Wuhan gained its fame as Big Wuhan through merging different smaller cities back in 1927. Big now not only refers to the city’s significant geographical size of 8,494 sq km (larger than Shanghai’s 6,340 sq km), but also the size of its economy, education resources and road network. The city is often referred to as the fifth biggest city in China, a national transportation hub, and the shipping centre of the mid-reaches of the Yangtze River.

Construction sites are seen almost everywhere in the city. By 2020, the city’s office and retail stock is expected to reach to 3.5 and 7.0 million sq m respectively, up 80% and 50% from the existing stock. This new supply will bring challenges to existing projects with some shopping malls already suffering from competition and shrinking footfall.

The retail market used to be dominated by local players. Wushang Group enjoys the largest market share of retail space in the prime Wuguang area, including Wuhan International Square—currently the highest end project in the city with a retail GFA of 320,000 sq m. The situation is likely to change in coming years as more leading national and international developers launch their projects. A total of around 3.0 million sq m of retail space is expected to launch over the next five years which will further increase competition and more likely than not put the under-performers out of business.

As a key strategic city, Wuhan is hoping to become the economic engine of China’s central regions. Rapid growth however has brought new challenges for the city. Residential prices in Wuhan are some of the highest of any city in central and western China, approximately 15% to 40% higher than comparable cities such as Xi’an and Chengdu. High housing prices decrease affordability for individuals and, combined with higher pollution levels as result of economic activity and construction, could be one reason why the inflow of people from other parts of the country was lower compared to comparable cities. Nevertheless, several leading companies have moved or set up a second headquarter in Wuhan in recent years including Xiaomi, CMIC and PSA, an indication that the city is still extremely popular for corporations. Big Wuhan will definitely be better, it is just a matter of time.
Tianjin’s real estate market continues to extend its reach. During the past five years, over 90% of land transactions were of sites located outside the city’s Outer Ring Road, in 2018 there was one land plot sold within the Middle Ring Road. With more residential communities being established outside the city centre, demand for retail facilities in these locations is continuing to grow. Developers are consequently looking to identify opportunities for retail development in these new emerging locations with under-retailed residents.

Four shopping malls, totalling 315,000 sq m, were launched onto the market in 2018, all positioned as regional malls in decentralised locations, with regional malls now accounting for roughly one third of retail stock. The four projects opened with average occupancy rates of 85% pushing down the city-wide figures by 1.5 ppts YoY to 10.6%. Decentralised rents also outperformed the citywide average, increasing 1.6% YoY.

Compared to projects in prime locations, regional malls focus more on the daily demand of the surrounding consumers and communities. F&B and child-related tenants are usually allocated a relatively larger share. Indeed by end of 2018, F&B accounted for 41% of space in decentralised malls but only 28% in prime malls. New projects also tended to incorporate various art installations and cultural venues, constantly rolling out exhibitions and events to attract more visitors such as L+ Art Centre within L+ Mall and hannou Louvre Museum within MCC World. Well-arranged exhibitions or performances not only generate revenue by selling tickets but also help boost retail sales through engagement with other tenants within the mall as well as shoppers.

With the general quality of retail offering continuing to improve in newer completions, these decentralised locations who are recording the lion’s share of new developments, are seeing a significant improvement of their retail environment helping to anchor some of these new residential communities. Over 500,000 sq m of new supply is expected to open in decentralised areas in 2019, most of which will be in districts outside the main urban areas of Xiqing and Beichen. Better quality retail centres will give leading retailers more confidence to enter these emerging areas.
Xi'an is the political, economic and cultural centre in northwest China, and is also the shopping mecca of the region. The retail market has long been dominated by traditional department stores with very few alternative retail options available to consumers. Shopping malls share of the total retail stock remained below 50% until 2015.

The city’s retail market underwent dramatic changes in 2018 with retail supply reaching 1.2 million sq m. This represents not only the highest annual supply in the city’s history but it is also more than double the average annual supply of the last five years. Xi'an was also the city with the largest retail supply in 2018 of any city in China.

The opening of landmark shopping malls such as Xi'an SKP and Xi'an Joy City has convinced leading international brands to open their first stores in northwest China, such as Hermes, Celine, Victoria’s Secret and Lululemon. In 2018, nearly 30% of newly opened luxury brand stores in China were located in Xi'an. The improved quality of the projects on offer has also helped the city to enhance its retail attractiveness to both retailers and consumers through innovative architectural design and strong asset management capability.

In 2017, Xi’an’s permanent population increased by 800,000 and it is forecast to attract another 750,000 people in 2018. The rapidly growing population and strong residential demand also helped to boost the development of community malls. Residents in decentralised locations have more retail and entertainment choices than they have had before. With more retailers growing their presence in the city, expansion rates of both key F&B and fashion brands reached over 20% in 2018, which made the city one of the most attractive destinations for retailers in 2018.

It is expected that another 894,000 sq m of new supply could enter the market in 2019, representing another leap forward is yet to come.