Free trade zones and Yangtze River Delta integration policies help spur demand

GRAPH 1: Suzhou Grade A Office Market New Supply, Net Take-up and Vacancy Rate, 2014 to 2019

Free-trade zones and Yangtze River Delta integration policies continue to spur demand for Grade A office space in the Suzhou market, bringing new office projects to the market. In 2019, a total of 392,000 sq m of new supply was completed across the city, a significant increase from 2018, when 291,000 sq m was completed. The office vacancy rate in the city fell to 6.0% in 2019, down from 10.6% in 2018. The city’s Grade A office market continues to be one of the most vibrant in China, as new projects bring more opportunities for office operators to establish themselves in the market.

SUPPLY AND DEMAND

Five Grade A office projects—Suzhou Centre Tower B located in West SIP, Pacific Finance Building, Suzhou New Building and GCL Plaza in East SIP, and Core of the World Tower C in the Moon Bay area—with a total GFA of 296,200 sq m were completed during 2019, pushing Suzhou’s Grade A office stock to 3.1 million sq m. Leasing activity was muted in Suzhou in the first half of 2019 in response to the slowing economy and the ongoing financial de-risking campaign that started in 2017. New financial enterprises such as P2P and microlenders were prohibited from entering the market, while the majority of demand continued to come from tech firms. Third-party office operators such as co-working, makerspaces and incubators are still growing in 2019 after aggressive expansion in 2018. Two notable deals were WeWork’s lease of about 8,640 sq m in Suzhou Centre Tower B and domestic brand Chunian’s (中产) lease of 12,000 sq m in Hong Long City Centre. The first sizable office deal in almost seven years was concluded in March when China Overseas acquired Suzhou International Fortune Plaza in West SIP for RMB4.4 billion, with a GFA of roughly 332,000 sq m, equating to RMB135,000 per sq m. The project has since been renamed China Overseas Fortune Centre. Additionally, the establishment of the China (Jiangsu) Pilot Free Trade Zone (FTZ) in August helped increase interest in the SIP in all of 2019, attracting both domestic and foreign enterprises. The FTZ consists of three areas totaling 320 sq km: Suzhou (60 sq km, including the 5.9 sq km Suzhou comprehensive bonded zone in SIP), Nanjing (20 sq km) and Lianyungang (20 sq km). The Suzhou component will look to establish itself as a world-class, high-tech industrial park with a focus on driving innovation with an international dimension, developing high-end industries, implementing modern management systems and opening up the economy on all fronts.

RENTS AND VACANCY RATES

The SIPFTZ and YRD integration policies led to the gradual recovery of the office market demand with net absorption for the year totalling 393,000 sq m. Nevertheless, demand was not enough to absorb all the new supply, and consequently, the citywide Grade A office vacancy rate increased by 1.6 ppt a year-on-year (YoY) to 33.4% by the end of 2019. Grade A office rents fell 3.7% YoY to an average of RMB137.0 per sq m per month. While the overall market conditions weighed upon all landlords, those that have been more heavily exposed to fintech firms and saw space being vacated by tenants, were more aggressive in their discounts to attract new tenants to take up vacant space.

OFFICE MARKET OUTLOOK

Four Grade A office projects totaling 331,000 sq m of space will be delivered to the market in 2020, roughly on par with 2019. 2020 supply includes delayed projects that were originally scheduled for 2019, such as What’s International Financial Centre. New high-quality projects will continue to intensify competition, especially for older developments. While Suzhou has one of the highest vacancy rates outside of the YRD Tier 1 cities, it also has the most to gain from a closer relationship with Shanghai, where city-centre rents are close to three times the value. As companies look to cost control and tap into new talent pools, Suzhou will certainly be one of the first cities on their list.

Popular F&B brands expand aggressively, while the growth of mass-market fashion brands slowed

SUPPLY AND DEMAND

Suzhou’s retail sales grew by 6.3% YoY in the first eleven months of 2019 to RMB3.4 trillion. The growth was 1.4 ppt lower than the same period in 2018. Nine new projects launched onto the market in 2019, contributing a total retail GFA of 771,000 sq m. Projects included Oriental City in Gaoyi district, Magic Holiday Plaza in Xiangning district, GCL Plaza and Zhujiajiao Lane Neighbourhood Centre in East SIP, 3D Park in Wuhu district, and four projects located in Wujiang district—Suzhou Plaza, The Mixc One Wujiang, Angel Place Wujiang and Garden Li. The city’s stock reached 8.5 million sq m, with shopping malls accounting for more than 80% of the total, a transformation from the original Singapore model of neighbourhood centres into larger-scale shopping malls which are more common now in cities like Shanghai.

Suzhou Centre and Longjiang Shuishan Paradise Walk, two landmark projects, attracted many new brands to enter the Suzhou market for the first time, stimulating both footfall and consumption through these new brands and creative shopping experiences. The most aggressive brands were high-end outlets and specifically milk tea brands, such as Hey Tea, Lelecha (乐乐茶) and Naruw. At the same time, domestic chain restaurants such as Guanmanzi (观曼滋), Tanyu Hot Pot (谭渔热) and Bumi Hot Pot ( бум伊热) also entered major shopping malls.

Luxury brands continued to focus on traditional department stores such as Suzhou Tower, Matteo and Juquang Department Store, though as the sector recovers some brands are considering opening additional stores in high-end shopping malls. Fast fashion and mass-market brands have found the market more challenging, and there have been a number of international brands that have relinquished spaces while other brands are adjusting their store networks. Shopping centres that continue to rely on these brands to anchor their space and drive footfall will have to adjust strategies to better appeal to rapidly changing consumer tastes.

RENTS AND VACANCY RATES

Citywide vacancy rates increased by 1.4 ppt YoY to 9.7% in Q2/2019. As new landmarks’ projects launched onto the market, they may not have a direct impact on the market vacancy rate as pre-commitment rates will tend to be relatively high. However, these projects do attract a lot of the attention and footfall from the surrounding area and, eventually, tenants, resulting in the rise of vacancy rates in existing developments. Suzhou Centre’s launch onto the market has had a significant impact on projects in West SIP and even the wider area. Impacted projects are taking this opportunity to adjust tenant mixes and positioning to fill space and better compete in the changing retail market.

First-floor rents fell just 0.4% YoY to an average of RMB137.0 per sq m per month, influenced by the increasing vacant rates. Shopping malls in Suzhou New District were less impacted by new supply or rising vacancy rates and recorded an increase of 1.8% YoY.

RETAIL MARKET OUTLOOK

New supply has focused on non-prime areas, especially Wujiang and Wujiang, in recent years, but the retail atmosphere is still lacking. Projects have found it difficult to attract quality brands and shoppers and occupancy rates of some projects have even fallen after project openings. While these projects are likely to find 2020 still challenging, it is hoped that a growing surrounding population and improving the business environment will allow development to gradually increase occupancy rates.

¥990,000 worth of new projects are expected to open in 2020, including Longfor Single Paradise Walk, Hong Dong Shopping Mall and Joy Tremor. This represents a smaller increase in stock and will continue to increase competition within Suzhou. Better-quality developments with more adventurous tenant mixes and engaging spaces could improve the retail atmosphere and encourage consumers to part with more of their hard-earned cash.

RESEARCH

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