Market activity picks up

A flurry of portfolio deals was announced in the final weeks of the first half of 2021.

- 15 deals were concluded in Q2/2021 with a total consideration of RMB13.4 billion, down by 21% YoY. Adding the consideration from assets from portfolio transactions will bring the total consideration to RMB42.3 billion.

- Several big-ticket portfolio transactions were announced towards the end of June, including Blackstone’s purchase of 55% of SOHO China for around RMB19.5 billion, Brookfield’s purchase of a five-retail property portfolio from Macquarie for RMB8.9 billion and Ping’an Insurance’s purchase of partial stakes in six Raffles City developments for RMB33.0 bn.

- Despite compressed yields and fierce competition, investors remain confident in the growing logistics/data centre market. CapitaLand made its first mainland data centre acquisition with the purchase of a project in Minhang for RMB3.66 billion.

- Nine China Infrastructure REITs (I-REITs) started trading on the Shanghai (SSE) and Shenzhen (SZSE) Stock Exchanges on June 21, raising RMB360 billion. A key milestone for China real estate market, the launch of REITs is expected to bring new sources of capital and clarity to the market.

- Shanghai held its first batch sale for residential-titled land in June. 56 land plots were transacted with no plot recording a premium higher than 10%.

“Though transaction volumes remain limited, investors are exploring opportunities in the multifamily market as the sector matures, regulations provide guardrails and the product receives greater acceptance from local renters.”

JAMES MACDONALD, SAVILLS RESEARCH
MARKET COMMENTARY

15 deals were concluded in Q2/2021 with a total consideration of RMB13.4 billion, down by 2% YoY. Adding the consideration for the assets from portfolio transactions brings the total consideration to RMB42.3 billion. Several big-ticket portfolio transactions were announced towards the end of June, including Blackstone's purchase of 5% of SOHO China for around RMB19.5 billion, Brookfield’s purchase of a five-retail property portfolio from Macquarie for RMB8.9 billion and Ping’an Insurance’s purchase of partial stakes in six Raffles City developments for RMB33.0 bn. All the deals include one or more core or core-plus assets in Shanghai. The market is seeing a rise in interest from institutional buyers looking to capitalise on the attractive pricing environment, access to sizeable portfolios and the recovery in market fundamentals.

The rental housing market is also seeing an increase in interest from investors. They recognise the market potential given government support and the need for affordable housing for young professionals. There is also an increasing willingness to pay extra for additional services, hassle-free experience and dependability that is offered from an institutional landlord compared to a private individual. Rental apartment transactions tend to be value-add rather than stabilised deals, though there are also cases of hotels converted to serviced apartments, and serviced apartments acquired and subsequently sold strata-tile. Jingrui Holding, for example, purchased Hongqiao Hongyi Plaza in Q2/2021; the mixed-use project is to see its hotel (7,887 sq m) and part of its retail (45,083 sq m) sections converted into serviced apartments and operated as Jingrui Yuetang (锦瑞悦庭).

The long-anticipated China I-REITs were finally launched on June 21. The nine I-REITs were warmly received by both institutional and retail investors. Insurance companies took around 10% of total equity, second only to the REIT sponsors. Ping’an Insurance and Taikang insurance were among the top buyers in this category. The I-REITs allow investors to buy shares in mutual funds that invest in asset-backed securities holding ownership (such as warehouses and business park projects) or management rights (such as toll roads and sewage). Insurance companies seem to prefer REITs with ownership rights that focus on warehouses, while mutual funds preferred REITs with management rights. Despite the early success of China’s I-REITs, their long-term performance against other REIT markets remains to be seen; there is still no clear timeline for when more traditional commercial asset classes or multifamily developments might be included.

OFFICE MARKET

Four new projects were launched onto the market in Q2/2021, adding a total office GFA of 258,300 sq m. Net office take-up more than doubled in Q2/2021 to 410,900 sq m, the highest quarterly level over the past three years. With demand outstripping supply, the citywide vacancy rate fell 1.3 percentage points (ppts) in Q2/2021 to 14.5%. Landlords have regained their confidence and have started to adjust up rates and/or reduce incentives. Grade A office rents recovered 0.8% on an index basis in Q2/2021 with rates averaging RMB7.3 pem pdy.

Business and industrial parks are still drawing both end-user and investor attention. However, with project values in mature areas, including Zhangjiang, Caohongjia and Jinjiang rising and core asset opportunities scarce, investors are focusing on value-add opportunities as well as those with lease-up risks. One private equity recently purchased Zhangjiaji 368 for RMB33 million with plans to renovate the asset. End-user buyers and long-term

TABLE 1: Yields And Capital Values By Sector1, Q2/2021

<table>
<thead>
<tr>
<th>GRADE A OFFICE</th>
<th>BUSINESS PARK</th>
<th>PRIME SHOPPING MALL</th>
<th>PRIME RETAIL STREET STORE</th>
<th>HIGH-END SERVICED APARTMENTS</th>
<th>HIGH-END STRAT APARTMENTS</th>
<th>5-STAR HOTEL</th>
<th>LOGISTICS</th>
</tr>
</thead>
<tbody>
<tr>
<td>APPROX. GROSS TO NET RATIO 2</td>
<td>70-80%</td>
<td>80-90%</td>
<td>55-65%</td>
<td>70-80%</td>
<td>60-70%</td>
<td>80-90%</td>
<td>35-45%</td>
</tr>
<tr>
<td>NOI</td>
<td>4.0-4.5%</td>
<td>4.5-5.0%</td>
<td>4.0-4.5%</td>
<td>3.5-4.0%</td>
<td>2.5-3.0%</td>
<td>2.0-2.5%</td>
<td>1.5-2.0%</td>
</tr>
<tr>
<td>APPROX. VALUE (RMB PER SQ M)</td>
<td>50-90,000</td>
<td>20,000-40,000</td>
<td>60-100,000</td>
<td>100-200,000</td>
<td>55-70,000</td>
<td>100-200,000</td>
<td>40-50,000</td>
</tr>
</tbody>
</table>

1 Yields refer to stabilised assets in downtown locations free of any impediments with a clean holding structure owning 100% of the building, and assuming 100% occupancy. Capital values refers to the average for the building on an aboveground GFA basis – retail assets will have higher capital values for lower floors.
2 Assumes consideration losses, including taxes, fees, and other miscellaneous.

Source: Savills Research
capital remain the principal purchasers of office assets. Nevertheless, there remains a divide between buyer and seller pricing expectations, which has led to some assets sales processes being protracted or failing.

**RETAIL MARKET**
Four new projects were launched onto the market in Q2/2021, bringing a total GFA of 320,000 sq m. Overall shopping mall vacancy rates fell 0.4 of a ppt in Q2/2021 to 9.2%, down 2.5 ppts YoY. First-floor rents increased 0.3% in Q2/2021 to an average of RMB16.3 per sq m per day, up 0.2% YoY.

The effective pandemic controls and rising vaccination rates have improved consumer sentiment, though it remains below pre-pandemic levels. Investor sentiment has likewise improved in recent quarters, and more retail transactions are likely to close in the second half of 2021, some of which were postponed from last year. Typical buyers are private equity firms with strong retail management teams who have faith in the long-term growth prospects and have a keen awareness that retail markets have a range of projects whose performance is only somewhat related to market-wide trends. From this perspective, a sector-wide sell-off represents a rare buying opportunity. Sellers, on the other hand, may be looking to trim their exposure to China's retail sector to recycle capital and reweight portfolios or are shifting to asset-light holdings and management strategies.

**LOGISTICS**
More capital from various sources continues to pour into the logistics sector despite compressing yields as investors search for diversification and higher yields and growing market potential driven by China’s burgeoning e-commerce sector. GLP announced the closing of its newly established GLP China Income Fund II in Q2/2021, with capital commitments totalling RMB8.8 billion. JD Logistics successfully IPO’ed on the Hong Kong Exchange market in late May and raised US$3.2 billion.

Meanwhile, China’s cold chain network is gaining increased importance with the rise of e-commerce and online groceries. BlackRock will provide support for the development of Metcold Opportunity Funds I and II, which encompasses a portfolio of 15 cold chain facilities, five of which are now in operation. Macquarie Infrastructure and Real Assets became a major investor and shareholder of Metcold’s platform in 2018.

**KEY DEALS**
- Noah Holdings purchased Hongqiao Sunnyworld Centre for RMB2.1 billion and started using the building as their headquarters from late June. The building has a total GFA of 63,138 sq m and is located in the centre of Hongqiao Business Area.
- CapitaLand purchased a Data Centre Campus from AVIC Trust for RMB3.66 billion. The 75,000 sq m project is located in Minhang district and has four buildings with a 55-megawatt capacity. The data centre campus currently serves both China Mobile and China Telecom and is managed by China data centre operator Daily-Tech. This is the first time that CapitaLand has bought any data centre facilities in China. The firm plans to expand its data centre portfolio in cities including Shanghai, Beijing and Shenzhen in line with its “CapitaLand 3.0” restructuring plan.

**LAND MARKET**
- Primary land sales totalled RMB183 billion in 1H/2021, up by 40% YoY. Commodity residential and commercial sectors accounted for 49% and 45%, respectively. Residential for-sale and for-rent land plot AVs averaged RMB14,960 and RMB4,506 per sq m, respectively. Commercial land plot AVs averaged RMB17,296 per sq m. Shanghai held its first batch of concentrated land auctions in June, selling 56 residential titled land plots. A new raft of regulations was established to curb the growth in accommodation values and ensure an even playing field between big and small developers. No land plots recorded a premium higher than 10%; this is compared to Q1/2021, when five land plots recorded premiums higher than 10%, with the largest premium being 36%. Developers were particularly keen on land plots in the “five new towns”, namely Jiading, Qingpu, Songjiang, Fengxian and Nanhui.

Logistics land supply in Shanghai remains limited, with investors forced to seek opportunities in second-hand land, industrial land and JV structures with companies that have idle land resources.

**OUTLOOK**
Shanghai's investment market is expected to be more active into the second half of 2021 as international buyers return to the market and prioritise transparent, liquid markets like Shanghai and Beijing.

As the government publishes policies to promote the growth of the rental housing sector by allowing land usage change and including rental housing into eligible underlying assets type in REITs, it is expected to see more investors get into the sector and take advantage of the policy benefits.

### TABLE 2: Key Land Deals, Q2/2021

<table>
<thead>
<tr>
<th>PLOT</th>
<th>DISTRICT</th>
<th>USE</th>
<th>GFA (SQ M)</th>
<th>CONSIDERATION (Million RMB)</th>
<th>AV (RMB PER SQ M)</th>
<th>BUYER</th>
</tr>
</thead>
<tbody>
<tr>
<td>Plot 095a-02, 095b-01, Unit N070403, Lingshi Community</td>
<td>Jing'an</td>
<td>Mixed-use</td>
<td>203,320</td>
<td>10,513</td>
<td>51,707</td>
<td>Poly</td>
</tr>
<tr>
<td>Plot X101-01, X102-02, X103-01 (237 Subdivision Plot), Unit W060701, Wanli Community</td>
<td>Putuo</td>
<td>Mixed-use</td>
<td>322,864</td>
<td>9,910</td>
<td>30,694</td>
<td>Excellence Group</td>
</tr>
<tr>
<td>Plot xh128E-03, Unit W53, Extension Section of Huangpu Jiangnan</td>
<td>Xuhui</td>
<td>Mixed-use</td>
<td>119,920</td>
<td>5,171</td>
<td>43,116</td>
<td>Forte</td>
</tr>
<tr>
<td>Plot 11-12, Unit MHSB0001, Huacao Town</td>
<td>Minhang</td>
<td>Residential</td>
<td>118,424</td>
<td>3,729</td>
<td>31,484</td>
<td>Country Garden</td>
</tr>
<tr>
<td>Plot A3-01A, Unit N091101, Xinjiangwan Community</td>
<td>Baoshan</td>
<td>Residential</td>
<td>67,848</td>
<td>3,328</td>
<td>49,046</td>
<td>Country Garden</td>
</tr>
<tr>
<td>Plots 04-02, 05-02, Unit JDC2-0201, JDC2-0202, Nanxiang Town</td>
<td>Jiading</td>
<td>Residential</td>
<td>78,742</td>
<td>2,457</td>
<td>31,200</td>
<td>Country Garden</td>
</tr>
</tbody>
</table>

*Source: Savills Research*