MARKET IN MINUTES
Savills Research

Office

savills 第一太平戴维斯

Vacancy rates continue their rise to 19.1%

Supply spike pushes vacancy up to new highs, while demand remains lacklustre.

- Nine new Grade A projects, or a total of 1.07 million sqm of office space, were handed over in Q3/2023, driving the city's total stock to 17.9 mn sqm by the end of the quarter.
- New supply and weak demand pushed the citywide vacancy rate up 3.1 ppts QoQ to 19.1%, up 6.6 ppts from a recent low seen in Q1/2022.
- Net take-up totalled 351, 700 sqm in Q3/2023, in large part due to self-use developments and pre-leasing. Excluding owner occupied projects, non-prime areas contributed 70% of total net take-up.
- Renewals and cost saving remain top priorities for many companies. Some renewals were temporary extensions, as companies considered future office needs.
- Grade A office rental decrease (1.8%) accelerated with rents averaging RMB6.9 psm pday. Prime, non-prime and decentralized rents fell by 1.7%, 1.6%, and 2.1%, respectively.
- Nine out of 26 key submarkets saw space being handed back to the market, with reasons including POEs struggling to grow/IPO, startups going bankrupt, a few MNCs reducing capacity or relocating operations.
- Leasing transaction volumes were limited in Q3/2023 however the co-working and IT sectors remained relatively active.

Definitions
Core prime: Nanjing Road (W), Huaihai Road (M), Lujiazui
Core non-prime: Old Huangpu, South Huangpu, Hongqiao, North Station, North Bund, Zhuyuan and Xujiahui.
Decentralised markets: All areas outside of the core markets including East Bund, Changfeng, Hongqiao Transportation Hub, Xuhui Riverside, Xinzhuang, Zhenru, Wujiaochang, Former Expo, Qiantan, Houtan and Huamu.

"The vast majority of tenants continue to hunker down, unable to financially commit themselves to new premises in the current environment. Nonetheless, the time will come when businesses must make a choice, and the competitive rates in certain new projects are increasingly difficult to overlook."

JAMES MACDONALD, SAVILLS RESEARCH

Savills team

Please contact us for further information

RESEARCH

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

COMMERCIAL

Cary Zheng
Senior Director
Central China
+8621 6391 6688
cary.zheng@savills.com.cn

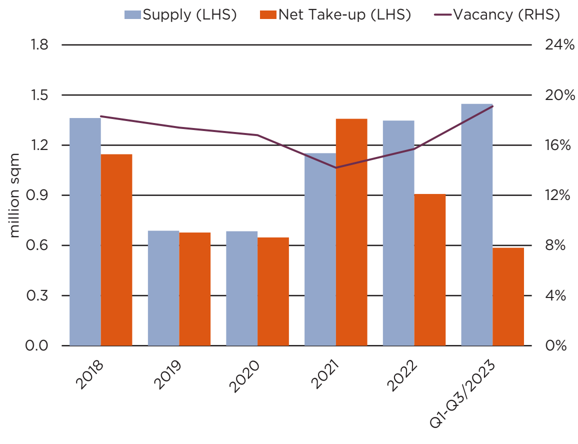
COMMERCIAL TENANT REPRESENTATION

Peter Sheng
Senior Director
Shanghai
+8621 6391 6688
peter.sheng@savills.com.cn

TRANSACTION AND ADVISORY

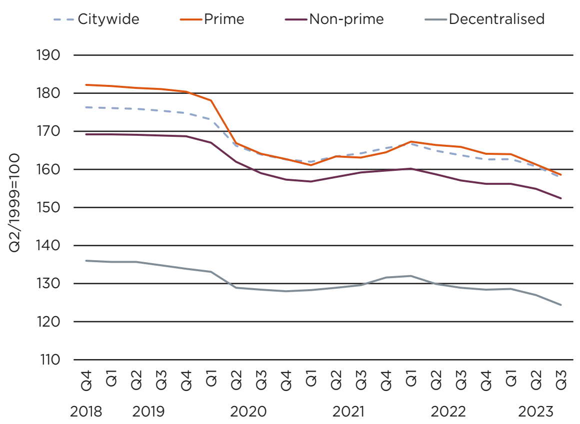
Joey Chio
Senior Director
China
+8621 6391 6688
joey.chio@savills.com.cn

GRAPH 1: Grade A Office Overall Supply, Take-up And Vacancy, 2018 To Q3/2023



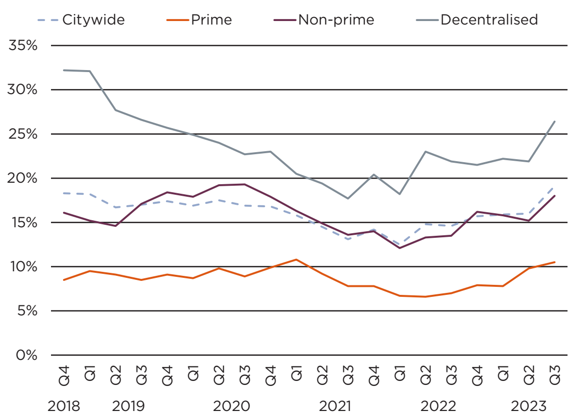
Source Savills Research

GRAPH 2: Grade A Office Rental Indices, Q4/2018 To Q3/2023



Source Savills Research

GRAPH 3: Grade A Office Vacancy, Q4/2018 To Q3/2023



Source Savills Research

MARKET OVERVIEW

New supply in the third quarter is expected to push full-year figures to a new record. Lease inquiries and site inspections remain relatively limited and there remains a lag with leasing activities. In the past, many renewals were direct transactions, but now, more property owners are willing to pay brokerage firms renewal commissions while also offering increased tenant incentives. Larger firms are also working closely with relevant authorities to explore potential office upgrade solutions, with a preference for leasing/purchasing space in the same region or developing HQ spaces.

SUPPLY AND DEMAND

Nine new projects were delivered to the market in Q3/2023, totalling of 1.07 mn sqm of office space, driving the city's total stock to 17.9 mn sqm. Launched projects with anchor tenants:

- LuOne, South Huangpu (Xiaohongshu, Ipsos)
- Joy Centre, North Station (China Mobile, Industrial Bank)
- Hongqiao United Tower, Hongqiao
- Hong Shou Fang Corporate Avenue, Caojiadu (Mega Gravity)
- Guohua Financial Centre, North Bund (Guohua Life)
- China Overseas Centre, Zhenru (Yuanlong Yato)
- Pingjin Centre, Xinzhuang
- New Bund Square, Qiantan (Siemens Energy)
- Green Valley Expo, Expo (Self-use)

Office leasing activity remained relatively limited in Q3/2023, nevertheless net take up totalled 351,700 sqm in large part due to self-use developments and pre-leasing. That said, pre-leasing rates remain below historical norms at roughly 20-30%. West Nanjing Rd was the only prime submarket to record positive take-up in the third quarter, with the majority of demand focused on the newly built, decentralized and emerging markets with lower cost.

With the rapid development of emerging sectors, industry reshuffling and consolidation are also intensifying. Some companies are returning unused spaces, while startups are shutting down, increasing pressure on property owners. Net take-up in the first three quarters of 2023 is 586,000 sqm, lower than the same period of the previous two years, while supply for the same period was 1.45 mn sqm.

Leasing activity has primarily centered around the North Station and Xuhui Binjiang largely because of recently completed projects. Financial and professional services firms continue to account for the majority of space leased, meanwhile energy companies have been more active though individual units tend to be relatively small (average 800 sqm).

VACANCY AND RENTS

Due to the supply influx and weak demand, the citywide vacancy rate increased 3.1 ppt QoQ to 19.1, up 4.5 ppt YoY. Almost two thirds of Shanghai's submarkets recorded vacancy rate increases.

Landlords continue to offer rental discounts while other projects have started reducing face rent and offering more flexible lease terms, especially when some owners see tenants downsize their requirements. Grade A office rents fell 1.8% in Q3/20023 to an average of RMB6.9 psm pday, down 3.5% YoY.

Some landlords have started linking rental costs to tenants' corporate tax contributions. For SOE landlords this means that if tenants meet specific tax contribution hurdles in the preceding 12-month period, the landlord will be able to reduce rents starting from the second year of the lease term. POE landlords on the other hand prefer to offer tenant incentives directly (usually 3-6 months' rent free). If their projects can contribute a significant tax amount, they can apply for a subsidy from the district government.

MARKET OUTLOOK

Another half a million sqm of new supply is scheduled to launch in Q4/2023, located in non-prime and decentralized areas. Should the current absorption level persist, and projects stick to completion schedules, the citywide vacancy rate will exceed 20% by year end.

It seems likely there is not enough momentum for a significant rebound in the short term. That said, authorities continue to actively court new investment and support businesses where they can. Tenants could seize their opportunity to secure future HQ premises in case of rebound.

TABLE 1: Notable Leasing Transactions, Q3/2023

TENANT	TENANT INDUSTRY	PROJECT	BUSINESS DISTRICT	LEASED AREA (SQ M)
CIMIC Logistics	Transportation	Sinar Mas Centre	North Bund	7 000
Zhong Guang Yun	Information Technology	T Centre	Zhenru	5 000
Fuder Finn Consulting	Professional Services	Grand Gateway T1	Xujiahui	3 300
Novo Nordisk	Healthcare	New Bund Centre	Qiantan	3, 000
Bokura	Media & Entertainment	Lumina Shanghai Phase 2	Xuhui Binjiang	2, 500

Source Savills Research