Shanghai – July 2024

MARKET IN MINUTES

Savills Research

Office

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Net take-up recovers

Despite growing demand, the citywide vacancy rate continues to rise and rental declines are accelerating.

- Six new projects totalling 374,000 sqm were handed over in Q2/2024, bringing the cumulative total for H1/2024 to 1mn sqm and the overall stock to 19.3mn sqm by the end of Q2/2024.

- Despite half of the submarkets experiencing vacancy rate decreases, the citywide vacancy rate increased by 0.6 ppt QoQ to 22.3% due to the influx of new supply. Significant take-up was recorded in North Bund, North Station, and Old Huangpu, reducing the non-prime area vacancy rate by 0.3 ppt.

- Net take-up was 186,000 sqm in Q2/2024, bringing H1/2024 net take-up to 486,000 sqm, equivalent to 75% of the total take-up for 2023.

- Landlords continue to offer rental discounts, leading to a 3.4% decline in Grade A office rents in Q2/2024, averaging RMB6.4 psm pday. Prime, non-prime, and decentralised market rents fell by 2.1%, 2.8%, and 4.9%, respectively.

- Despite previous restrictions on extra-curricular children's classes, several education and training organizations have opened new locations and expanded administrative functions, indicating a gradual recovery in demand.

- Landlords are adjusting leasing strategies to the market situation by lowering tenant thresholds and accepting third-party office operators to improve occupancy. Increased leasing activity from these companies is expected in the second half of the year.

"A challenging market environment persists, yet strategic government initiatives and adaptive landlord strategies signal a cautiously optimistic outlook for the Shanghai office property market."

JAMES MACDONALD, SAVILLS RESEARCH

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.

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

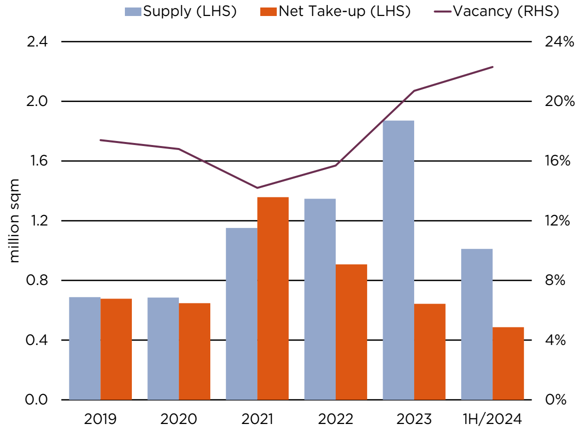
COMMERCIAL TENANT REPRESENTATION

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

TRANSACTION AND ADVISORY

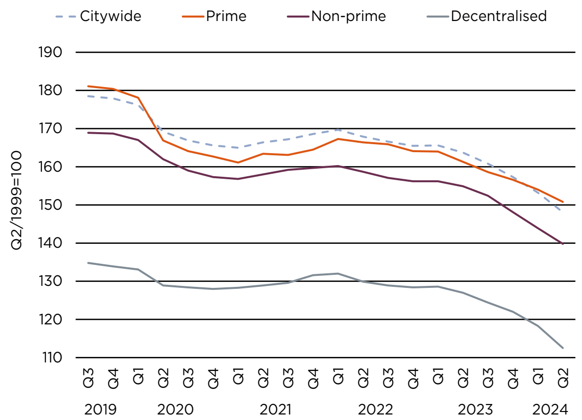
Joey Chio
Senior Director
China
+8621 6391 6688
joey.chio@savills.com.cn

GRAPH 1: Grade A Office Overall Supply, Take-up And Vacancy, 2019 To Q2/2024



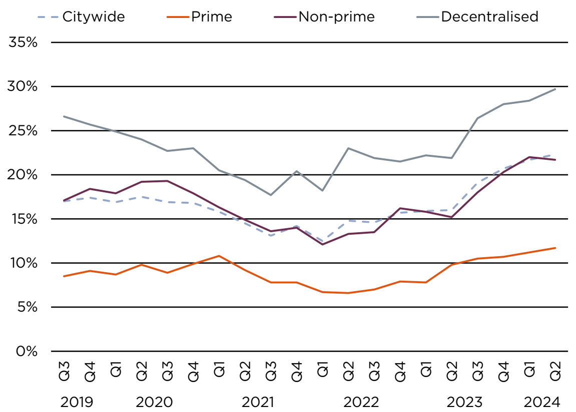
Source Savills Research

GRAPH 2: Grade A Office Rental Indices, Q3/2019 To Q2/2024



Source Savills Research

GRAPH 3: Grade A Office Vacancy, Q3/2019 To Q2/2024



Source Savills Research

MARKET OVERVIEW

Despite weak overall market sentiment, government agencies are actively attracting investment, supporting the growth of start-ups through industrial policies, and assisting enterprises with potential in upgrading their office spaces.

Shanghai's recent urban renewal plan lays out a clear roadmap for enhancing the office market. Grade A buildings should focus on their core strengths, expanding investments and attracting top-tier enterprises to maintain their competitive edge. For Grade B landlords, the emphasis should be on integrating B2C clients, such as medical clinics and training centers, or converting part of the building into hotels to diversify their offerings and enhance the overall value proposition. Meanwhile, Grade C buildings should target startups and incubators, offering affordable premises in central locations to foster innovation and entrepreneurial activity.

SUPPLY AND DEMAND

A total of 374,000 sqm of new supply was delivered through six new projects in Q2/2024, with non-core markets accounting for 60% of this. The new projects include CPIC Xintiandi Commercial Centre T2 (Huaihai Rd (M)), CCB Life Building (Old Huangpu), Lujiazui Financial Holding Plaza Ph2 (Zhuyuan), CCCC Riverside Plaza (East Bund), The Summit T3 (Huamu), and Origin Plaza (Xuhui Binjiang). By the end of the quarter, the total stock of Grade A office buildings in the city reached approximately 19.37mn sqm.

Notable transactions exceeding 10,000 sqm, including single-tenant leases, have bolstered market confidence. The city's net absorption for the quarter was 186,000 sqm, a positive shift compared to the same period last year. Secondary business areas contributed 96,000 sqm to net absorption, showing significant improvement from Q1/2024, indicating resilience. It is noteworthy that the net absorption of Grade A office buildings in the first half of 2024 reached 486,000 sqm, accounting for 75% of the total absorption in 2023, and similar to H1/2022. Traditional industries remained the primary source of demand, with financial and retail trading companies particularly active, comprising one-third of known transactions. Domestic demand accounted for 76%, while foreign enterprises were less active than before. However, recent openings such as Allianz Fund Management indicate continued interest.

VACANCY AND RENTS

The average vacancy rate for Grade A office buildings increased by 0.3 ppts QoQ to 22.3%. Due to the supply influx and slow absorption of new projects, some submarkets saw notable increases in vacancy rates, such as East Bund (+14.5 ppt) and Huamu (+7.3 ppt). However, more than half of the 26 submarkets experienced improved occupancy rates, with secondary business areas seeing a 0.3 ppt QoQ decrease in vacancy rates.

Given the persistently high vacancy rates and ongoing rent declines, rents decreased by 3.4% QoQ to RMB 6.4 psm pday. Prime, non-prime, and decentralised markets saw decreases of 2.1%, 2.8%, and 4.9%, respectively. Landlords are enhancing rental discounts and making other concessions to attract and retain tenants, such as providing shuttle buses, dining facilities, and gyms. Some non-core projects have seen rent declines of 20-30% compared to previous contracts.

MARKET OUTLOOK

The market will continue to see ample supply in the second half of the year, with approximately 794,000 sqm scheduled for delivery, 70% of which will be in decentralised business areas. If delivered as planned, the total stock of Grade A office buildings in Shanghai will reach 20.17 mn sqm by the end of 2024.

Landlords are adjusting leasing strategies in response to market conditions, such as lowering tenant thresholds and accepting third-party office operators to improve occupancy. More active leasing activity from these operators is expected in the second half of the year.

Despite the currently weak absorption levels, traditional industries remain relatively strong. Landlord incentives continue to favour tenants, allowing enterprises to upgrade office spaces while reducing costs. The influx of new projects also provides tenants with more options. Additionally, government policies on talent training and support for emerging industries, such as AI and computer science, are sending positive signals for future demand.

TABLE 1: Notable Leasing Transactions, Q2/2024

TENANT	TENANT INDUSTRY	PROJECT	BUSINESS DISTRICT	LEASED AREA (SQ M)
Only Education	Consumer Services	Lumina Shanghai Ph1	Xuhui Binjiang	13,900
Lianjia	Real Estate	New Bund Square City	New Bund	13,000
Manulife sinochem	Finance	Lee Garden	Nanjing Rd(W)	10,000
Beigene	Healthcare	CPIC Xintiandi Commercial Centre	Huaihai Rd (E)	10,000
Jike Office	Business Centres & Co-working Spaces	Foresea Life Building	North Bund	4,800

Source Savills Research