News Release

JLL 仲量聯行

Office rents stable despite considerable new supply; foreign investors became more active in Shanghai's investment market

According to JLL Shanghai Second Quarter Property Review

Shanghai, July 06, 2017 – Leasing momentum remained strong in the fringe CBDs and rents in these areas continued to outperform. "Investor interest in the Shanghai office market stayed strong as buyer profile continued to diversify," said **Eddie Ng**, Managing Director for JLL East China. In the residential market, low inventory and limited new supply allowed prices to keep stable despite authorities' tight policy stance. Retail rents grew for the second consecutive quarter where experienced operators have capitalised on a rebound in retail sales volume. Vacancy in the logistics market fell back down into single-digits as pent-up demand from the Chinese New Year holiday produced strong leasing activity in last quarter's completions.

Office

Space availability releases upgrade and consolidation demand. CBD recorded a net absorption close to 100,000 sqm in 2Q17, supported mainly by domestic financial services and professional services, retail, and TMT companies. "Manufacturing & trading companies in the CBD continued to seek cost effective space in the decentralised market" said **Anny Zhang**, Head of Markets for JLL Shanghai. Upgrade demand from Grade B occupiers also helped drive leasing demand in the new projects.

Supply wave takes a breather in the CBD. New Supply in the CBD reached 101,900 sqm, down 80% q-o-q. Two projects, ITC Phase 1 and China Overseas International Center, reached completion. CBD vacancy still decreased slightly by 0.1 ppt q-o-q to 12.4%. In the decentralised market, ten projects with a combined GFA of around 504,000 sqm reached completion. Despite large supply volume, decentralised vacancy only increased by 3.2 percentage points q-o-q to 25.7%.

Rents remain flat as owners compete with new projects. While the leasing market remained active, owners of stabilized projects in the CBD stayed conservative as they compete with new projects. CBD recorded flat rent growth in 2Q17. Strong leasing demand contributed to the 0.8% q-o-q rental growth in the decentralised market.

Strata-titled Office

Capital values rose given limited supply. No new supply launched this quarter. Sales volume decreased by 32% q-o-q to 131,330 sqm, however purchase inquiries remained large in number. Besides large corporate buyers who sought space for self-use or investment purposes, several cash-rich leasing tenants opted to buy space. Robust demand and limited supply drove up capital values to around RMB 44,614 per sqm, an increase of 2.3% y-o-y in 2Q17. Moving forward, strong demand in the CBD market and the low supply level expects to generate spillover demand into the decentralised market. However, overall price growth is expected to decelerate over the next 12 months given a large upcoming supply wave in the decentralised market and potential for tighter financing conditions.

Business Parks

Diversified demand sources drive net absorption in the core business park market. Stable demand continued to support rental appreciation as rents grew 1.0% q-o-q in 2Q17. In terms of demand, tenants in business parks became increasingly diversified: architectural design, film production and hi-tech manufacturing firms were active in 2Q17. High-quality projects in core business parks were particularly favored. For example, Kehui, SBP, and Headquarter Ph3 in Caohejing as well as Carey Tower and Innov Star in Zhangjiang, all recorded large-sized lease transactions during the quarter.

Meanwhile, high-quality assets in top locations also became highly sought-after by institutional investors. Investment activity kept active in business parks this quarter. Caohejing recorded two en-bloc transactions during 2Q17: H88 and Innov Tower.

Capital Markets

Total 2Q17 investment volume in Shanghai reached RMB 19.4 billion, which was a 2.8% q-o-q decline and a 47.2% y-o-y gain. In terms of asset types, office continues to dominate the investment market in Shanghai in 2Q17 with a total of RMB 17.9 billion, which represents 92.1% of total. Retail space came in second with a total of RMB 600 million transacted, or 3.1% of the total, and industrial investments reached RMB 400 million, or 2.1% of total.

In 1H17, total transactions in China reached RMB 85.4 billion, or a 53.0% y-o-y gain, and Shanghai represented 46.1% of total investments in the market.

Despite high prices and lower transaction volume, investors remained upbeat on Shanghai. Johnny Shao, Head of Capital Markets for Shanghai and East China, said: "One of the key reasons for a slowdown in 2Q17 is the limited availability of quality assets for sale in the market, especially after the frantic buying spree witnessed in 4Q16. Another reason is the sellers' pricing strategy of offering limited discounts to buyers, which likely prolonged the decision making of potential deals. "

Foreign investors became more active in Shanghai's investment market. Overseas buyers were responsible for two of the largest transactions this quarter. CapitaLand purchased Guozheng Centre for RMB 2.64 billion in May while Keppel Land China bought SOHO Hongkou for RMB 3.57 billion in June.

JLL responsible for one major deal in the quarter. In 2Q17, JLL was responsible for the sale of H88 Tower in Caohejing Shanghai. The office building had a total GFA of 55,879 sqm was sold to a domestic fund.

Residential

Mass market supply rises while high-end launches remain limited. In the mass market, developers accelerated new launches in 2Q17, resulting in a 47% q-o-q rise in new supply. Strict controls on pre-sales of high-end projects, however, meant that 2Q17 saw only two projects - Yanlord On the Park and Star River Pudong - launched a total of 256 units in the high-end segment.

High-end sales constrained by limited supply. Following subdued sales in the first quarter, mass market buying demand gradually picked up in 2Q17 as supply increased. As a result, sales volumes in the mass market rose 38% q-o-q in 2Q17, though still down 36% from a year ago when a price rally spurred strong buying activity. In the high-end segment, limited new supply constrained sales volume even as upgrade demand remained solid. As a result, only 498 units of high-end housing were sold in 2Q17, down 9% q-o-q. In the leasing market, demand strengthened slightly in 2Q17.

Developers firm on pricing. Despite low sales volumes, high-end prices remained largely stable in due to low inventory and limited new supply. Average primary sales prices edged up 0.7% q-o-q. Stronger leasing demand led rents to rise by a moderate 0.7% q-o-q.

New policies expected to benefit residential market. In May, Shanghai's authorities announced new restrictions on the sale of commercial-titled apartments. "We expect these restrictions will result in some demand spilling over into the traditional residential-titled leasing and sales market, mainly over the medium and long term," said Stephenie Zhou, Head of Project Sales for JLL Shanghai. Over the near term, the continued tight policy stance means that high-end sales will likely remain subdued in 2H2017. However, developers are expected to remain firm on their pricing due to a limited upcoming supply pipeline. Rents are expected to grow moderately on the back of solid leasing demand.

<u>Retail</u>

Sportswear and domestic brands active as retailer sentiment improves. International sportswear and casual wear brands continued to expand in Shanghai, as did domestic fashion designers, who extended their presence in key decentralized malls. "Sentiment improved further this quarter as sales for many brands in China continued to rebound from a soft period in 2016," said James Hawkey, head of Retail for JLL China. Mass-market F&B chains such as themed noodle shops continued to expand, having gained traction with affordable prices, quick turnover, and collaboration with China's app-enabled food delivery services. Co-working providers and conference centers took advantage of spaces in prime malls that had proved challenging for traditional retailers.

Four projects open with combined GFA of 368,000 sqm. HKRI Taikoo Hui opened in the competitive Nanjing West Road submarket. Raffles City opened near Zhongshan Park, where it faces stiff competition from the popular Cloud Nine mall. After many delays, Shanghai Tower's retail portion opened with an F&B focus. Vacancy rose to 10.3% in prime areas as the new malls together opened with above average vacancy, and several existing projects in Lujiazui and West Nanjing Road underwent repositioning. In the decentralized market, Vivo City added a one-stop shopping option targeting local residents in Minhang. Decentralized vacancy decreased to 9.7% as occupancy edged up in Huamu and Hongkou.

Rental growth continues moderate rebound. In the prime market, open-market ground floor base rents increased by 3.2% y-o-y (2.1% q-o-q) to RMB 52.6 per sqm per day. Decentralized rents rose 4.2% y-o-y (1.8% q-o-q) to RMB 21.1 per sqm per day. Rental growth was driven in particular by the Huaihai Road and Huamu submarkets, where leading projects with experienced operators continued to outperform.

<u>Logistics</u>

Net-absorption rebounds after sluggish first quarter. Following a period of negative absorption in the first quarter, net take-up accelerated to 170,000 sqm in 2Q17. "This proved our expectation that strong inquiry levels in the first quarter would translate into a rebound in leasing activity," said Stuart Ross, Head of Industrial for JLL China. Most leasing took place in projects that had been completed in the first quarter without pre-commitments. 3PLs and e-commerce firms continued to drive leasing demand. A lack of space in traditionally-popular West Shanghai submarkets meant that leasing activity was strongest in emerging areas, like Baoshan, Fengxian, and Lingang.

Vacancy falls on lack of new supply and strong demand. No new supply was completed this quarter, leaving total non-bonded stock in Shanghai at 5.1 million sqm. We do not anticipate any new supply until 2018. Given limited supply and strong leasing demand, non-bonded vacancy declined 3.0 ppts to 9.1%. Vacancy in the emerging submarket Jinshan declined from 56% to 28% as LIM Jinshan Fengjing leased out approximately half of its space. Western Shanghai vacancy remained near zero with only pockets of space available.

Rents continue to grow at a moderate pace. Rents edged up 0.5% q-o-q to RMB 1.31 per sqm per day in 2Q17, accelerating slightly from the previous quarter. Landlords had more confidence raising rents in light of the quarter's stronger leasing momentum.

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