Shanghai Grade-A Office Market Report

Q3 2023

This report focuses on the Grade-A office market in Shanghai, with information about supply and demand, rents, vacancy rates and the office investment market

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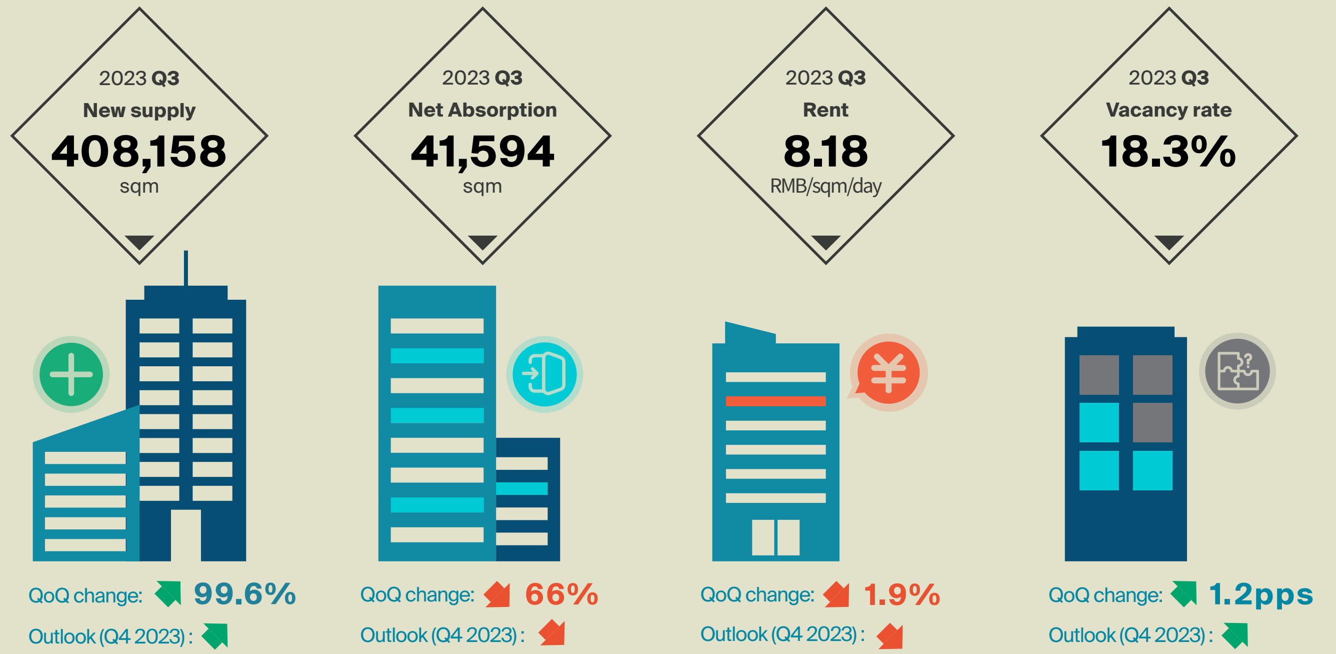
Overview and Outlook

Overall office market performance has yet to pick up

With the global economy growing slowly and more companies focusing on reducing costs, it will take more time for the office leasing market to pick up. In the third quarter (Q3), four new office projects were completed, adding a total of 408,158 sqm of office space to the market, an increase of 99.6% QoQ. Total new supply in the first three quarters of 2023 reached 930,000 sqm. The average market rent continued to decrease by 1.9% QoQ to RMB8.18 per sqm per day. The average vacancy rate continued to increase by 1.2 percentage points to 18.3% due to the concentration of new supply and limited leasing demand in the market. With several new projects entering the market, as well as a number of tenants seeking to surrender their leases and move out, the overall market saw a higher vacancy rate. In Q3, the market's net absorption was only 41,594 sqm, down 66% QoQ. Market leasing demand continued to come from sectors that were more active in the recent past, such as TMT, finance, professional services, and retail and trade. In the retail sector, the strongest office demand was from catering, apparel, cosmetics and media companies.

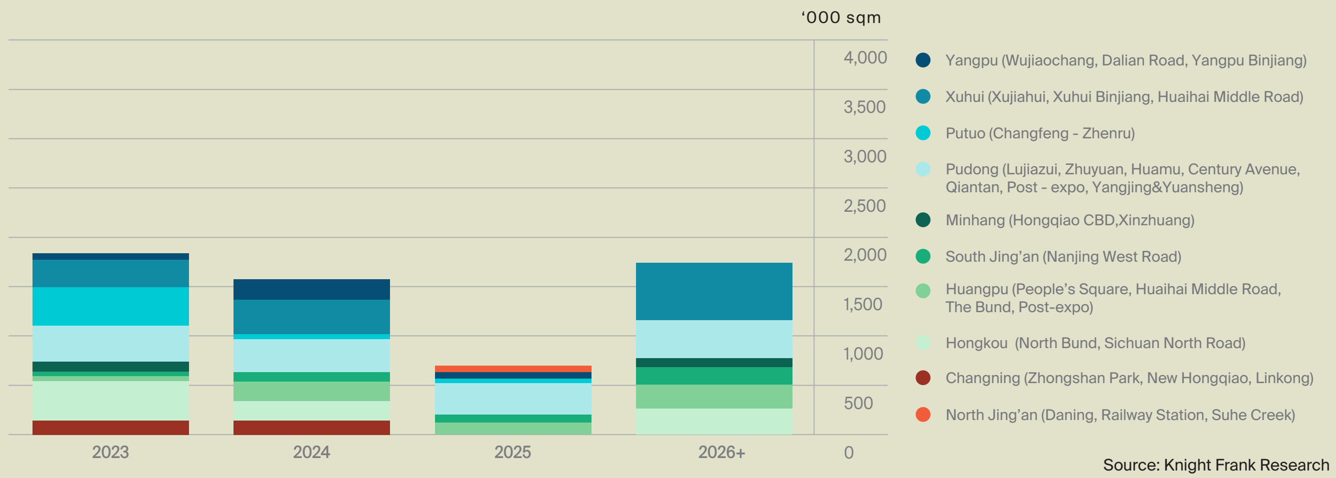
As the leasing market did not show the expected signs of a pick-up in demand, it is doubtful whether the nearly 850,000 sqm of projects in Q4 will be released on schedule. Cost-control decisions have led to an inevitable trend of tenants surrendering leases, downgrading or moving out. We believe that given the economic uncertainty and corporate cost-cutting, the office market still faces a possible further decline in market rents and a rising vacancy rate.

Fig 1: Shanghai Grade-A office market indicators[1]



Source: Knight Frank Research
[1] Rent refers to average effective rent

Fig 2: Shanghai office development pipeline by district, 2023-2026+



Source: Knight Frank Research

Supply and Demand

An increasing number of cost-oriented companies moved out of the CBDs

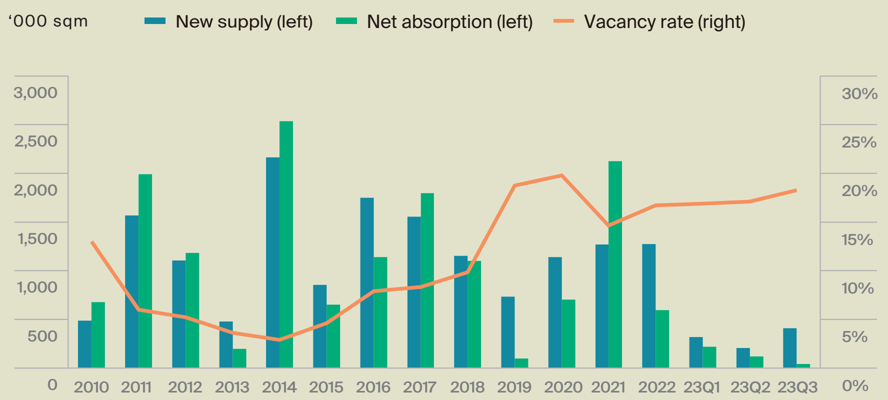
New completions in Q3 added a total of 408,158 sqm of new supply to the market. The Summit, in Pudong Huamu, added 210,000 sqm of office space to the market. Guohua Financial Centre, in the North Bund of Hongkou, and Hong Shou Fang, on Changshou Road in Putuo, added 91,420 sqm and 47,597 sqm of office space, respectively, to the market. In addition, the PJ Centre, in the Xinzhuang area of Minhang, released 59,141 sqm of office space to the market.

Q3 saw a significant increase in corporate relocation activity, with over 60% of the leasing activity coming from corporate relocations. Mainstream leasing demand included cost-oriented companies surrendering their leases and moving out after their lease expired to cheaper or more favourably discounted office buildings. The professional services sector, represented mainly by law firms, was one of the few sectors looking for office upgrades.

In terms of new leasing transactions, the TMT, financial, professional services, retail and trade sectors continued to be the main sources of demand. Newly completed office buildings in the past two years with good accessibility and suitable rents have been well received by TMT companies, especially media companies.

In Q3, the vacancy rate in Little Lujiazui increased by 1.5 percentage points QoQ to 7.0% as a result of an increase in vacant space from an increase in the number of companies relocating out of the area. However, high-quality buildings in good locations are still sought after by financial companies. While overall market demand continued to weaken, one highlight in the market was steady growth in leasing demand from foreign retail brands and trading companies. In Q3, leasing demand in Nanjing West Road came mainly from foreign retail and trading companies. The growing potential of the domestic retail market has enhanced the confidence of foreign brands to expand their business and increase investment.

Fig 3: Grade-A office supply, net absorption and vacancy rate



Source: Knight Frank Research

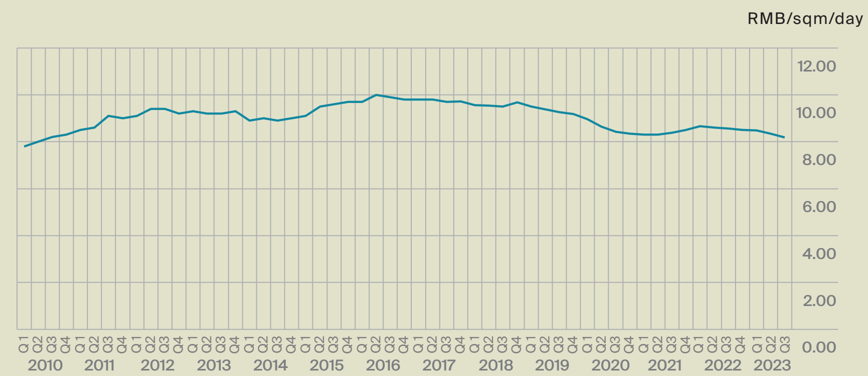
Rents

Corporate budget cuts and rent reductions by landlords were the main reasons for continued low rents

In Q3, the average Grade-A office rent continued to drop to RMB8.18 per sqm per day, a decrease of 1.9% QoQ. Corporate budget cuts and rent reductions by landlords were the main reasons for the continued decrease in rents.

In submarkets with more new projects entering the market, many landlords chose to adjust rents to obtain better market absorption due to the increase in vacant office space and stronger competition among landlords in the area, resulting in a continued downward trend in market rents. In Q3, the average rent in the North Bund market dropped by 4.7%

Fig 4: Grade-A office rental trend



Source: Knight Frank Research

QoQ to RMB7.70 per sqm per day, one of several submarkets with a large decline.

In Q3, the average rent in core CBDs continued to drop to RMB11.19 per sqm per day, a QoQ decrease of 1.3%. Affected by the outward relocation of cost-oriented companies in the Little Lujiazui and Huaihai Middle Road areas, the market rents in these two areas dropped to RMB11.72 and RMB9.89 per sqm per day, with QoQ decreases of 1.5% and 2.2%, respectively.

Nanjing West Road was one of the few submarkets where rents rose during the quarter, with the average market rent edging up to RMB11.40 per sqm per day. The area is favored by foreign retail and trading companies with higher rental payment capacity, which is an important reason for the slight increase in rents on Nanjing West Road.

Table 1: Major Grade-A office leasing transactions, Q3 2023

Submarket	Building	Tenant	Area (sqm)	Type
Little Lujiazui	Jinmao Tower	JT&N Law Firm	5,700	Relocation
Zhenru-Changfeng	T Centre Building One	ZhongGuangYun	5,000	Relocation
Xuhui Binjiang	The Lumina	Yuepu	3,000	Relocation
Nanjing West Road	Park Place	Sisley	1,700	Relocation
Little Lujiazui	DBS Tower	China Asset Management	1,548	Renewal
Qiantan	New Bund World Trade Centre Phase 4	Sandoz	1,200	New Lease

Source: Knight Frank Research

Note: All transactions are subject to confirmation

Investment Market

Owner-occupier buyers continued to dominate the market

In Q3 2023, the Shanghai office market recorded a total of 19 en-bloc transactions in the Shanghai office market, involving a total value of over RMB9.5 billion. 12 of the transactions were for Grade-A office buildings and 7 transactions were for standard office buildings in business parks. In Q3, owner-occupier buyers continued to dominate the market.

On 1 August, Yuanlong Yato announced plans to acquire office units and parking spaces of 7,459.44 sqm located on Floors 6-9, Building E, Zhonghai Centre in Putuo District, from China Overseas for approximately RMB307 million.

On 11 August, Seacon Shipping Group announced that it had entered into an agreement with Shanghai Lingang New Area Jingang Shengyuan Real Estate for a total consideration of approximately RMB240 million to acquire an office building under construction located at Unit 01–01, Block U2, PDC1-0105, PDC1-0202 in the Shanghai Pilot Trade Zone Lingang New Area. The property has a planned gross floor area of approximately 6,800 sqm and is intended to be used for the establishment of Seacon's new ship management office in Shanghai.

On 4 September, Swire Properties issued an announcement that it would acquire 40% equity stakes each in Dongmao Company and Yaolong Company, held by Lujiazui Group and Qiantan Investment (a subsidiary of Lujiazui Group), for a total consideration of RMB9.71 billion through its two wholly-owned subsidiary companies, and then develop the Yangjing Project and Qiantan Plot 21 Project with Lujiazui Group.

Shanghai Grade-A office market dashboard Q3 2023

Shanghai Grade-A office inventory, rents and vacancy rates of major business districts

Hongqiao CBD
Inventory: 1,422
Rent: 5.33 ▼
VR: 21.8% ▼

Zhongshan Park
Inventory: 459
Rent: 7.31 ▼
VR: 10.2% ▼

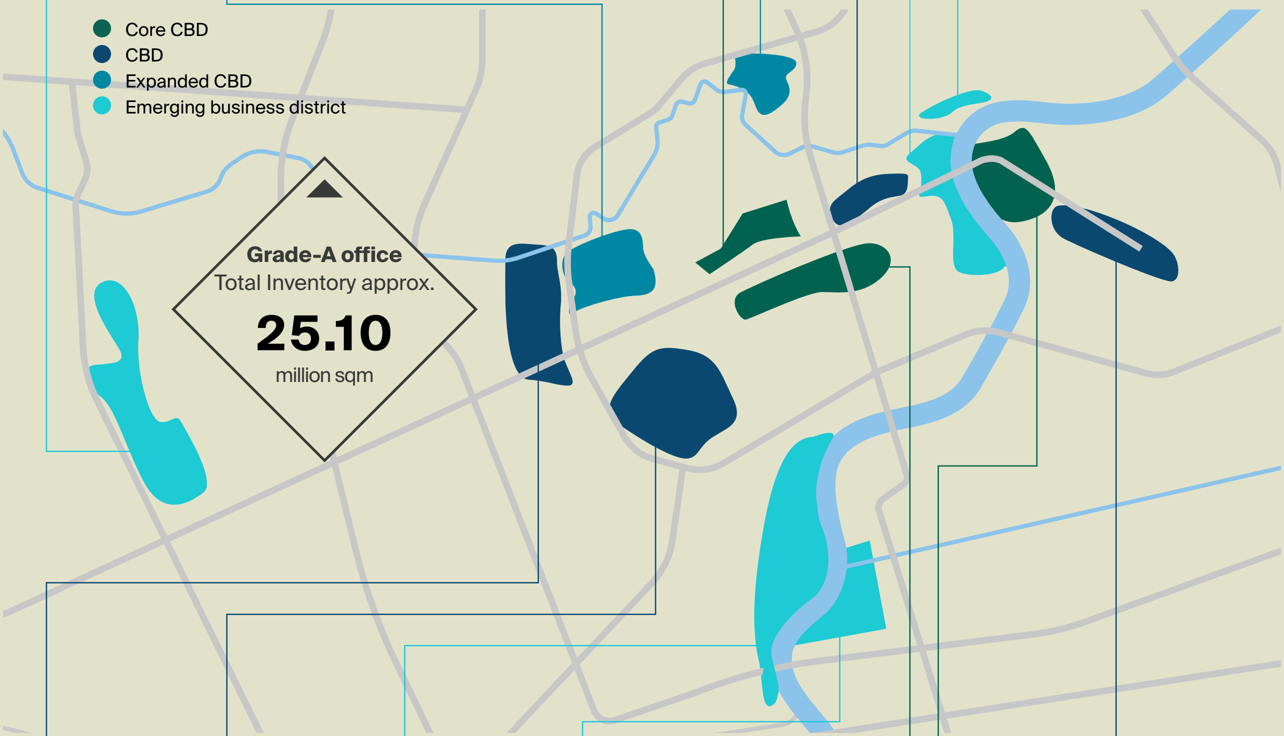
Nanjing West Road
Inventory: 1,435
Rent: 11.40 ▲
VR: 9.3% —

Railway Station
Inventory: 784
Rent: 7.14 ▼
VR: 20.4% ▼

People's Square
Inventory: 887
Rent: 8.19 ▼
VR: 11.4% ▲

The Bund
Inventory: 700
Rent: 9.91 —
VR: 10.9% —

North Bund
Inventory: 861
Rent: 7.70 ▼
VR: 29.1% ▲



New Honqiao
Inventory: 1,506
Rent: 6.98 ▼
VR: 12.2% ▲

Xujiahui
Inventory: 601
Rent: 8.25 ▲
VR: 23.3% ▼

Xuhui Binjiang
Inventory: 1,019
Rent: 6.00 ▼
VR: 32.1% ▲

Qiantan
Inventory: 833
Rent: 8.21 ▼
VR: 3.5% ▲

Huaihai Middle Road
Inventory: 1,069
Rent: 9.89 ▼
VR: 11.1% ▲

Little Lujiazui
Inventory: 2,787
Rent: 11.72 ▼
VR: 7.0% ▲

Century Avenue
Inventory: 943
Rent: 8.65 ▼
VR: 7.4% ▲

Source: Knight Frank Research

Note: unit for market inventory – 1,000 sqm; rents using average effective rent at RMB/sqm/month; VR refers to average vacancy rate.

We like questions, if you've got one about our research, or would like some property advice, we would love to hear from you.

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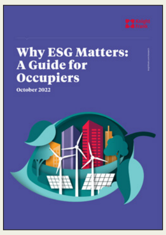

Why ESG Matters for Occupiers

Quantifying ESG in Real Estate