Accelerating the Success of Beijing’s CBD

How Beijing’s CBD can become a more dynamic submarket
After nearly 20 years, Beijing’s CBD has become the largest Grade A office submarket in the city, developing into the most popular destination for both multinational and domestic companies in all industries. Over the past two years, the CBD has entered a growth phase similar to the pace of GDP growth. Considering the abundant future supply in the next five years, we think occupiers in the market should use this opportunity to optimise their office location and cost. Landlords should regard it as an incentive to improve the quality of their properties and their services to tenants.

Executive Summary
How to respond to the rapidly growing Grade A supply in the upcoming years is the key question faced by all the office landlords in Beijing. However, through the seminar Colliers organised, we notice that many CBD developers are still confident about the future, especially those projects with good reputations and performances.

Retaining current quality tenants should be most important to landlords for existing projects. It is necessary to take action as early as possible for renewal or expansion; and to improve tenant mix to avoid uncertainty arising from the business cycles of different sectors. Meanwhile, the creation of a dynamic and harmonious relationship between landlord and tenant and with other tenants can effectively reduce the turnover rate of tenants in commercial buildings.

Good building facilities and large space availability are the key attractions of new projects. Landlords can utilise new projects to attract upgrade demands or demand from tenants with high space requirements. Starting the pre-leasing progress earlier and holding a flexible leasing strategy, especially for quality tenants, are key to a good foundation for future performance.

Referring to the development history of international CBDs such as the City of London and New York’s Manhattan district, we find that the success of a submarket can be accelerated if the government offers better service and support. Furthermore, landlords need to pay attention to trends among occupiers to expand their target tenant pool. For example, the most active industries in Manhattan were not only finance, but also real estate and TAMI (technology, advertising, media, and information) in 1H 2017. We see opportunities for Beijing’s CBD to attract new sectors, and to focus on mixed-use as well as purely office developments.

Figure 1 - New Supply, Net Absorption, Vacancy Rate for Grade A Office in CBD (2002-2021F)

Source: Colliers International Research
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Development of Beijing’s CBD

Development and Achievements

The core concept of the Central Business District (CBD) is built on the urban service industrial agglomeration effect. Its purpose is to create a healthy business environment for industries including finance, professional services, media, and commerce. Referring to the Beijing CBD, it was only a vision in the 1990s, and the Beijing municipal government accelerated its construction in 2000. As of now, Beijing CBD has developed into an industrial cluster dominated by finance, modern services and cultural media industries providing various functions.

According to the Beijing Central Business District Administration Committee’s introduction to the CBD in August 2016, the number of enterprises in Beijing CBD has reached 19,000 including 8,900 large enterprises. The CBD has gathered more than 200 international high-end service enterprises and approximately 50 regional headquarters of MNCs. Besides, more than 1,800 cultural medium enterprises are concentrated in the CBD, including 169 international media organisations, accounting for 90% of the total for the city. All of these enable Beijing CBD not only to promote the economic growth and social progress of the capital, but also to embody culture and communication values.

Figure 2 - Distribution Map of Grade A Office Submarket

Grade A Office Distribution

Beijing contains eight major submarkets for Grade A office with the total stock of Grade A office property reaching about 6.32 million sq metres (68.0 million sq ft) by the end of Q3 2017. The CBD is one of the most important submarkets in the city due to the high proportion of Grade A office space that it represents, complicated tenant mix, and strong demand.

The CBD covers 3.99 sq kilometres according to its primary planning, only accounting for 0.3% of the total area of the six urban districts of Beijing. However, the Grade A office stock in CBD was approximately 2.16 million sq metres (23.3 million sq ft) by end-3Q17, accounting for 34% of Beijing’s total stock and becoming the largest submarket. The second-ranking Lufthansa submarket has 15% of Grade A office stock, and has received much spill-over or relocation demand from the CBD area in recent years.
Macroeconomic Indicators

Beijing’s GDP and Tertiary Industry

The proportion of tertiary industry in Beijing’s GDP has increased steadily, from 76% in 2011 to 80% in 2016, showing that Beijing’s economy has transitioned to service-led growth. Beijing has the highest portion of tertiary industry among all cities in China, accounting for 82% of total GDP by end-H1 2017, compared to 70% in Shanghai and Guangzhou, and 61% in Shenzhen. At the same time, tertiary industry in Beijing has recorded a faster growth rate than overall GDP growth over the past three years. According to the Beijing Statistics Bureau, the city’s GDP grew by 6.7% YOY in 2016, while tertiary industry grew at 7.1%, 0.4 percentage points faster than GDP growth. Beijing’s economy continued to expand in 1H 2017, with GDP rising 6.8% YOY, up by 0.1 percentage points versus 2016. Tertiary industry continued to grow faster, at 7.2% YOY, over the same period.

Chaoyang District GDP and Tertiary Industry

Besides Beijing’s overall indicators, it is important to take a close look at the macroeconomic indicators for the Chaoyang district where the CBD is located. Chaoyang district’s GDP growth rate was slower than the city’s total GDP growth rate in 2016, at 6.5%. Nonetheless, the tertiary industry growth rate was in line with Beijing at 7.1% YOY, 0.6 percentage points faster than its GDP growth rate. The proportion of tertiary industry in Chaoyang district’s GDP has increased by 4 percentage points from 89% in 2011 to 93% in 2016, indicating that the growth momentum of the services sector was very strong. All these solid fundamentals underpinned sustained leasing demand in Grade A office market in the Chaoyang district.
Impacts of Recent Major Events and Politics

Since 2015, there have been seven major events and policies that should have a significant impact in both the short and the long term on the Beijing office market:

> In April 2015, an outline of the coordinated development of the Beijing-Tianjin-Hebei area was approved by the Political Bureau of the Communist Party of China Central Committee. The integration of Beijing, Tianjin and Hebei should stimulate infrastructure development and industrial upgrades.

> In July 2015, Beijing announced that it would speed up the construction of Tongzhou District, the city’s subsidiary administrative centre. The Beijing city government will relocate its functional offices out of central Beijing to Tongzhou by end-2017. We predict that Tongzhou will attract business related to local government’s functional offices.

> In August 2015, the Beijing city government announced a ban on new large-scale commercial developments within the central area of the six urban districts. This action should further restrain office property supply in the long term.

> In May 2016, China expanded its value-added-tax (VAT) regime to all industries and an 11% VAT (or a tax rate of 5% if acquired before 1 May 2016) rate is applied to the real estate industry. The reform is aimed at lowering tax burdens, tax-related costs and mitigating double taxation for certain businesses.

> In July 2016, the Beijing city government started to charge property tax at 12% of the rental income for leased space instead of charging 1.2% on the book value. The gains in property tax add more cost to landlords.

> In April 2017, China announced it will develop the Xiongan New Area in Hebei province to help phase out non-capital functions from Beijing. It is generally thought that the Xiongan New Area will attract central and state-owned enterprises. We expect the Beijing real estate market to suffer less impact in the short term, while the long-term impacts are difficult to predict.

> In September 2017, the Beijing Municipal Commission of Housing and Urban-Rural Development issued a strict order to tackle construction dust pollution, requiring six urban districts, ten new districts and the Yizhuang Economic and Technological Development Area to stop construction work and housing demolitions from 15 November to 15 March next year. In the short term, we expect that this action will cause the completion date of several future projects to be postponed. Considering that the purpose of the regulation is to reduce pollution during the winter, if the government implements this policy every year in the future, this will have a long-term impact on the office market.
Supply and Demand in CBD

Vacancy remains low in the CBD

As the Beijing municipal government has accelerated the construction of the CBD since 2000, quality office buildings have entered the market gradually. The supply of Grade A office properties in Beijing CBD reached its peak in 2007 mainly due to the 2008 Beijing Olympic Games, with 470,000 sq metres (5.1 million sq ft) of new completion. Then the market maintained rapid expansion till 2011. Subsequently the market entered a slow supply period till 2016 with average annual supply of only 40,000 sq metres (430,600 sq ft) per year.

MNCs were the key market driver in the Grade A office market before the Global Financial Crisis of 2008-2009. However, after the Global Financial Crisis, domestic enterprises expanded rapidly and sought quality office space in core areas stimulated by Chinese government support at end-2009. As a result, demand outpaced supply between 2010 and 2012, contributing to a significant decline in the vacancy rate, from 27% in 2009 to 6% at end-2012. In 2014 and 2015, leasing demand came mainly from the domestic finance industry especially the P2P sector, and the vacancy rate reached its lowest point of 3.6% at the end of 2015.

Rent has fluctuated within a reasonable range

Shrinking demand during the 2008 Global Financial Crisis resulted in a rapid rental decline in 2008 and 2009. However, strong leasing demand from domestic companies in the CBD from the end of 2009 onwards led average rent to show an upward trend. The annual rental growth rate reached its highest point at 55% in 2011. Underpinned by continuous leasing demand and landlords’ strong position, the average rent of the Grade A office properties in the CBD soared to a high level of RMB366.5 per square metre (psm) per month in 2012 compared to RMB310.1 psm per month in 2011, although the pace was decelerating. In 2013, given economic uncertainties, demand for Grade A office property market was muted, resulting in less bargaining power for landlords. Average rent accordingly edged down for a while.

Over the past three years, the average rent in the CBD has been largely flat if one excludes the effect of new projects which had rents very different from the average. This is mainly for the following reasons:

- The slightly increased vacancy rate since 2016 has put pressure on certain landlords who were likely to adjust their rental rapidly based on the vacancy rate.
- Newly completed office buildings of high quality and with relatively low rents in surrounding submarkets such as Wangjing and Lufthansa have become attractive. With more tenants choosing relocation and decentralisation, certain landlords in the CBD became more flexible in rental negotiations in order to secure existing tenants.
- Certain existing landlords have lowered their rental expectations or improved incentives in order to fill vacant space because they are mindful of the coming wave of supply in the CBD core area.

Nevertheless, average rent in Beijing stood at RMB351.7 (USD53.3) psm per month by the end of Q3 2017, up by 0.9% YOY.

Figure 8 - New Supply, Net Absorption, Vacancy Rate for Grade A Office in CBD (2007-Q3 2017)

Source: Colliers International Research

The vacancy rate in the CBD has begun to edge up since 2016. Firstly, demand from the domestic finance industry has slowed down due to the stricter government supervision towards P2P companies. Certain landlords have also adopted stricter screening on the qualification of P2P companies given their potential higher risks of default. Secondly, more MNCs have downsized or relocated to lower rent office buildings given their tightening budgets amidst the global economic slowdown. Nevertheless, the vacancy rate in the CBD stood at about 4.8% at end-Q3 2017, a slight increase compared to end-2015, but remained at a relatively low level.
Complicated Leasing Demand

The CBD has a complicated tenant structure, which covers more than 10 different industries. Finance and professional service are the two major industries among Beijing CBD's existing tenants, accounting for 40% and 16% of the total office space respectively in Q2 2017. The IT and Trade sectors are the following two biggest industries, with portions of 8% and 6% respectively.

Based on our analysis of the new leasing transactions in Beijing's CBD Grade A office market, the finance sector was the most active industry, contributing the largest proportion at 40% of all new leases in 1H 2017; however, this represented a decline from 52% over the whole year of 2016. In the same period, leasing demand from professional service and IT was active: the proportion of leases from the two sectors increased to 22% and 13% respectively. The real estate industry also contributed 10% of total leasing transactions, up by 2 percentage points compared to 2016.

When looking at the breakdown by nationality of new leasing deals over the recent two years, we find that the Grade A office leasing market is dominated by domestic tenants. Furthermore, the portion of domestic new tenants has been rising: domestic companies signed 79% of the total leasing space in 2016, while the proportion increased by 1 percentage point to 80% in 1H 2017. Due to cost concerns, the market saw more consolidation and relocation activities by MNCs to lower rent areas, especially in the pharmaceutical and energy sectors. As a result, only 20% of the leasing space was taken by MNCs.
Future Trend in the CBD

More Than Half of New Supply to be Concentrated in CBD

We project that Beijing’s Grade A office market will enter a new period of heavy supply, with average annual new supply of about 600,000 sq metres (6.5 million sq ft) between 2017 and 2021. This would represent an increase of over 160% compared to the average annual new supply of 226,900 sq metres (2.4 million sq ft) between 2012 and 2016. We estimate that the total future supply in Beijing over 2017-2021 will be 2.97 million sq metres (32.0 million sq ft), and that 51% of the total future supply will be concentrated in CBD.

Ongoing Wave of Supply to Push Up the Vacancy

There should be rapid growth in new supply in the CBD from 2018 to 2021. A total office GFA of approximately 1.45 million sq metres (15.6 million sq ft) of new supply is scheduled to be completed, leading the CBD’s total stock to rise to over 3.6 million sq metres (38.8 million sq ft) by then end of 2021. Most of the future supply will be located in the CBD Zhongfu core zone with the first phase available to lease in 2018. However, we predict that over 30% of the area will be retained by the landlord for self-use.

Considering the strong economic growth rate of China compared to many other countries, we forecast that...
domestic enterprises will continue to dominate the Grade A office leasing market. Since finance, IT, and profession service account for the largest proportion of Beijing’s GDP, we predict that these three sectors will continue to be the major generators of demand.

Flexible workspace has been a rapidly developing new sector in the real estate industry over the past two years. We predict that both domestic and international flexible workspace operators will continuously seek opportunities to expand in Beijing. Although most operators normally choose non-Grade A office buildings, we have found that powerful flexible workspace operators have begun to locate their space in Grade A office properties in the core area in order to attract different clients who are more concerned about location and can accept premium rents. For example, WeWork opened a 4,000 sq m (43,055 sq ft) workspace at Office Park in 3Q 2017.

In addition, the financial technology (fintech) industry is growing rapidly and we believe that the development of fintech has implications for the office property market. We expect large existing fintech companies with local clients to search for space in the core area. As a result, landlords in the CBD should expect higher demand from these new sectors to occupy vacant space and to enrich tenant mix.

Despite the sustained demand, we expect growth in demand to lag behind growth in office supply in the short term. Considering the CBD’s ongoing wave of ample new supply, we expect the average vacancy rate to reach 19% at end-2021. Nevertheless, we believe that office space will be absorbed eventually as the new supply in the core area will be restrained over the long term, reflecting in particular the ban on new large-scale commercial developments within the central area of the six urban districts that came into effect in 2015.

Figure 14 - New Supply, Net Absorption, Vacancy Rate for Grade A Office in CBD (2013-2021F)

Rent to face moderate downward pressure
We expect heavy new supply to put pressure on both existing and future landlords in the CBD. Certain future landlords may lower their rental expectations to attract anchor tenants, while existing landlords will probably become more flexible in rental negotiations in order to compete with future projects. We predict that average rent in the CBD will face moderate downward pressure, resulting in an average annual rental decline of about 1% between 2017 and 2021.

Figure 15 - Average Rent and Vacancy Rate for Grade A Office in CBD (2013-2021F)

Source: Colliers International Research

CBD Prospects

Opportunities for occupiers
We expect the abundant new supply in the next five years to shift the current market situation which favours landlords. Tenants are likely to have more opportunities to build a better working environment at less cost in the future.

More choice of quality office space
The further increase of prime office space in Beijing’s CBD will provide more choices for existing tenants in terms of space expansion, upgrades, or consolidations. Furthermore, potential tenants considering relocating to the CBD may find it easier as new office buildings will ease the current tight market conditions given the low vacancy rate.

Source: Colliers International Research
**Stronger rental negotiation power**

We expect the office market to shift over the medium term towards favouring tenants, especially high-profile companies. Competition in the CBD office market looks set to intensify, considering the competition between existing old properties, new projects completed in recent years, and upcoming properties. Therefore, occupiers should have stronger bargaining power when negotiating new leases or contract renewals as usually landlords are willing to offer rent discounts and incentives to retain current tenants or attract anchor and large tenants.

**Better services and amenities**

Occupiers should be able to enjoy more advanced amenities and superior services in the Beijing CBD, boosted by the new supply and improving infrastructure. Facilities and specifications of future supply in the CBD are much higher than the current market level, incorporating the latest technology, trendy designs, and greener and healthier systems. The new high-quality projects should also force landlords of existing properties to refurbish them and upgrade their amenities in order to catch up with rising market standards.

In order to differentiate themselves from other properties, many landlords try to provide more unique and customised services for occupiers, such as exclusive events and art galleries. Apart from rent and building specifications, occupiers may choose a property with suitable tenant mix and services, fitting their business strategy, brand image and employees’ needs.

The new subway lines proposed and the underground paths connecting many buildings which are under construction will continue to improve the CBD’s accessibility in the future. The influx of co-working space, openings of new hotels, boutique shops and restaurants will provide more sophisticated and comprehensive environment and services to occupiers in the submarket.

**Challenges for landlords**

We expect the combination of more diverse sources of demand and growing supply to increase competitive challenges for landlords.

**Abundant future supply**

We expect approximately 1.45 million sq metres (15.6 million sq feet) of new supply to be launched into the CBD market between 2018-2021. The direct impact of this huge volume of future supply is likely to be an increasing vacancy rate and downward pressure on rent, as demand is not likely to grow so fast in short term.

Landlords will have to make a balance between maintaining high occupancy rates and achieving satisfactory rental growth.

**Tenant relocation and decentralisation**

Relocation and decentralisation by tenants continuously cause demand to spill over to the fringe CBD and emerging areas. Cost concern is the biggest factor as rent in the CBD has become too high for cost-sensitive industries, such as manufacturing and MNCs with tighter budgets but recruitment expansion plans. On the other hand, for large companies which plan to consolidate multiple offices under one roof, newly completed properties in emerging areas provide sufficient space at reasonable cost. Many companies are relocating back offices to the fringe CBD or decentralised locations in order to optimise leasing costs. This trend is also squeezing market demand in the CBD.

**Dated building facilities**

In the CBD submarket, 54% of grade A office buildings were completed before 2007, which means that over 50% of the office buildings have aging facilities and outdated designs. Maintenance and upgrading of facilities in response to tenants’ changing tastes and new properties’ higher specifications has become a major challenge for landlords of existing properties.

**Regional functions**

According to the Beijing municipal government’s master urban plan released recently, Beijing is positioned as a national political centre, national cultural centre, international commutation centre and technological innovation centre. All the other functions beyond the above four are described as “non-capital” functions. Obviously, neither economic nor financial centre is mentioned. Beijing aims to establish an economic structure oriented towards high technology and to optimise regional development by relocating non-capital functions from core areas to suburban areas or surrounding areas in neighbouring provinces, such as Tongzhou district in eastern Beijing and Xiong’An New Area in Hebei Province.

The plan is projected to reshape Beijing’s industry distribution in the future as resources and support will be focused on key industries, such as high-end technology and IT, whereas certain industries will not be encouraged or even not allowed to be developed in the city. As a result, the demand structure of office space may change accordingly, requiring CBD landlords to...
anticipate the changing dynamics and adjust their leasing strategies.

International CBD case studies

London and New York, the two leading global financial centres for hundreds of years, have experienced peaks and troughs in their history. As the CBDs of London and New York, the development histories of the City of London and Manhattan and recent market momentum in these two areas can be a good reference for Beijing CBD’s development.

The City of London

London has thousands of years of history, and has been an economic and financial centre for at least 250 years. The following timeline describes the positioning change of London:

> Before 1750: London was a harbour city, and the UK’s capital, political and trade centre

> Late 18th Century: London became an economic and financial centre for the UK and one of the world’s leading cities

> After Second World War: London saw a slight downturn, especially after the booming of New York

> 1980-1990s: London strengthened its position as a global financial hub following after its first great financial boom in the late 1980s and a second boom in the 1990s

> 2016: The UK’s vote for Brexit brought some uncertainty to London, although clear signs of a downturn have not been noticed so far

The City of London and the West End are the two chief CBD areas in London. However, the City of London is still the principal financial centre, even though Canary Wharf has emerged as a new financial district in London in recent years.

The City of London has experienced at least two downturns in its recent history. The first started in the period after the Second World War and arguably lasted till the early 1980s. The second took place in the early 1990s, when a new financial centre in the eastern part of London, Canary Wharf, emerged as a rival to the City. However, the City of London had already strengthened its position as a consequence of the so-called “Big Bang” reforms of financial regulations, policies, and systems in the mid-1980s. These reforms attracted more international financial institutions and other related industries, such as professional services and media groups, to enter the City. The City continued its financial reforms in the 1990s, and started to construct more new properties including residential projects to weaken the impact from Canary Wharf.

Landmark buildings in the City of London

Source: Colliers International Research
The City of London remains the most dynamic financial hub in the UK. Though the City of London only covers one square mile, it contributed around GBP48 billion in Gross Value Added (GVA) in 2016, accounting for 13% of London’s or 3% of the UK’s output. The City of London’s financial services contributed 2.6% of the UK’s GVA in 2016.

In addition, the business environment in the City of London is very active. According to the statistics of the City of London Corporation, there were 18,000 businesses in the City of London in 2015, with nearly 99% small firms with less than 250 employees. About 1,200 firms move into the City each year and around 1,000 new start-ups are established, of which 55% are from the professional service sector.

Supported by the dynamic economy, employment in the City of London increased by 28% over the five years to 2015. In 2016, there were 455,000 workers in the City of London, accounting for 9% of London’s total workforce. The financial, professional and business services sectors provide the greatest number of jobs and drive jobs growth.

Figure 16 - Job categories in the City of London

For the office market, there were around 9 million sq metres (97 million sq ft) of office space in the City of London at end-Q2 2017. Net take-up in 1H 2017 reached 240,000 sq metres. However, Canary Wharf only recorded 2,400 sq metres of net absorption during the same period, demonstrating the continuing strong appeal of office space in the City of London. We noticed that media and technology was the largest demand driver in 1H 2017 and accounted for 34% of total new leasing areas. Notable transactions included Framstore’s lease of 9,100 sq metres (98,000 sq ft). Next came the legal, financial and insurance sectors, which together accounted for 16%. Notable transactions included Deutsche Bank’s pre-lease of 46,450 sq metres (500,000 sq ft). Over the past two years, coworking operators such as WeWork have expanded rapidly and taken around 55,740 sq metres (600,000 sq ft) of office space per year. The vacancy rate stood at 5.2% at end-2Q17.

The UK’s vote for Brexit, i.e. exit from the European Union, in June 2016 has brought about potential uncertainties. This has contributed to a decline of average rent. In Q2 2017, average rent in the City core area dropped, by 7% YOY to GBP62.8 (RMB549.1 per sq metre) per month according to the data from Colliers International UK research. However, the rent in Canary Wharf was stable at GBP40.4 (RMB355.8) per sq metre per month.

The changing political environment combined with the fast-changing business conditions has resulted in a shortening of lease terms to around six years from a typical original period of around 10 years.

Figure 17 – New Leases by Industry in 1H 2017

Source: Colliers International UK

Manhattan, New York

Manhattan, regarded as the CBD of New York, has a shorter history than the City of London, but it developed rapidly in the twentieth century and now ranks equally with the City of London as a global financial hub. The development of Manhattan can be divided into the following six phases:

- Late 1800s: The maritime industry stimulated banking and insurance industries in Downtown
- After 1898: Manhattan became an independent borough
1930s: Manhattan became NYC’s economic centre with the completion of many well-known skyscrapers.

1970-1980s: Emergence of finance and services

2000s: Emergence of Downtown, Midtown and Midtown South

After 2006: A new development era commenced with the Manhattan West Redevelopment and the completion of the New World Trade Centre

Manhattan attained equal importance to London as a financial centre after the First World War, although its position suffered badly following the Great Wall Street Crash of 1929 and subsequent Great Depression. After the Second World War, Manhattan surpassed the City of London and became the world’s most important economic and financial centre. However, industrial restructuring caused New York City including Manhattan to suffer from economic problems in 1970s. A resurgence in the finance industry through government reforms greatly improved the city’s economic health in the 1980s at about the same time as City of London was benefiting from its Big Bang. As a result, the two centres have been roughly equal in importance since then.

Manhattan is the smallest and most sophisticated and borough among New York City’s five boroughs. It consists of Uptown, Midtown and Downtown with major commercial centres located in Midtown, Midtown South Downtown. The total stock of Class A and B Office was around 47 million sq metres (506 million sq ft) at end-2Q 2017. The stock in Midtown and Midtown South accounts for 46% and 33% of total stock, respectively.

**Figure 18 - Manhattan Demographic Indicators**

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<thead>
<tr>
<th>Indicators</th>
<th>Figures</th>
<th>Remark</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population</td>
<td>1.6 million</td>
<td>19% of New York’s total population (2016)</td>
</tr>
<tr>
<td>Population Density</td>
<td>69,467.5 per sq mile</td>
<td>2.6 times of NYC (2010)</td>
</tr>
<tr>
<td>Median Household Income</td>
<td>USD 72,871 per year</td>
<td>1.4 times of NYC (2015)</td>
</tr>
<tr>
<td>Per Capita Income</td>
<td>USD 64,993 per year</td>
<td>2 times of NYC (2015)</td>
</tr>
<tr>
<td>Percentage of high education</td>
<td>59.9%</td>
<td>Population with age above 25 years and holding bachelor’s degree (2015)</td>
</tr>
<tr>
<td>population</td>
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Source: US Census

Buoyant business in New York City has led to a low unemployment rate and active tenant demand in recent years. Take-up in 1H 2017 in Manhattan reached 1.7 million sq metres (18.3 million sq ft) and the vacancy was 6.2% at end-Q2 2017. In 1H 2017, financial services, insurance, and real estate (FIRE) and technology, advertising, media, and information services (TAMI) were the top demand generators in Manhattan’s office market. Notable transactions included BlackRock’s new

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**Landmark buildings in Manhattan**

- Chrysler Building (1931)
- Empire State Building (1931)
- Rockefeller Center (1933-1952)
- Celanese Building (1973)
- Development of Manhattan West (2006)
- Redevelopment of Lower Manhattan (2011)

Source: Colliers International Research
lease of 79,000 sq metres (846,990 sq ft) and 21st Century Fox’s renewal and expansion of 72,000 sq metres (777,000 sq ft). The average rent of Class A office in Q2 2017 was USD70.5 (RMB472.6) per sq metre per month, up by 0.2% YOY based according to Colliers International US research.

In recent years, borderless evolution has continued in Midtown, Midtown South and Downtown. More new supply in Manhattan West and Lower Manhattan has created increasing relocation and consolidation. However, the intensifying competition is also leading to rising concession packages from landlords. The weighted average rental free period increased by 2.2% YOY to around 9.1 months in terms of a ten-year leasing term in 2016 according to Colliers International US research.

**Figure 19 – New Leases by Industry in 1H 2017**

![New Leases by Industry in 1H 2017](image)

Source: Colliers International US

From the above analysis, we find that both the City of London and Manhattan have experienced considerable fluctuations over their history. However, they have succeeded in becoming the leading global financial centres through reforms and adjustments to development strategies. They can provide useful models for the Beijing CBD’s future development.

### Strategies and solutions

Considering the ban on new large scale commercial developments within the six urban districts issued in 2015, we expect that the new supply in the CBD over the next five years will be the last wave of supply in prime locations in Beijing on a long-term view. As a result, the landlords have shown their confidence about the future of Grade A office in the CBD submarket.

However, there are still several sectors that can be improved by both government and landlords to create a better office environment, so as to ensure that Beijing’s CBD can develop along the lines of the top international business centres to become a more attractive CBD.

#### Government support

Despite the improvement of hard facilities such as infrastructure and the availability of preferential policies and incentives, we believe that provision of a competitive business and living environment will be a more important factor in attracting good companies and retaining talent in the CBD. It would be better if the government could strengthen the interaction between different buildings in the CBD through some event such as an industries forum. This would help the CBD to create a harmonious environment and good reputation to attract potential tenants.

In addition, balancing the representation of different property segments is a long-term strategy for the development of the CBD. For example, the City of London Corporation changed its development strategy from purely office development to mixed-used development in the early 1990s when construction of Canary Wharf commenced. Several hotels and the first department store opened in the 2000s. There were some small office buildings that shifted from office usage to residential usage, and several new residential buildings have been developed in recent years.

#### Leasing strategies

Leasing strategies are significant to landlords of both existing and future projects. We therefore suggest the following four major leasing strategies:

- **Early planning**: retaining current high-profile companies is one of the most important strategies for landlords of existing properties. As a result, preparing earlier contract renewals, e.g. one year before the expiry of the contract, to secure tenants
is necessary, especially for those tenants who occupy large amounts of space. For new projects, how to attract high-quality tenants is a vital task. Therefore, we expect landlords to start promotion activities in advance.

> **Adaptable leasing terms**: as the Beijing office market is still undergoing rapid growth, it is not practical to set long lease terms such as six to ten years as in the City of London or New York. As a result, it is reasonable to apply different lease term for diversified industries. For example, applying longer lease terms for large, mature tenants should help secure their occupancy. For start-up companies or companies from emerging industries, shorter lease terms are more acceptable to both landlords and tenants.

> **Flexible rental package**: we recommend landlords to offer more flexible packages to different types of tenants. Traditional market practice usually considers MNCs as the highest-quality tenants and offers them lower rents, while domestic financial companies need to pay higher rents, especially small companies. However, considering that domestic companies are the key market driver, landlords need to strengthen their background checking procedure and adopt suitable rent levels for different tenants.

> **Optimize tenant mix**: different tenants have different characters and this is the same for office buildings. As a result, it is important to find well-matched tenants for a building and retain the tenants for longer period. In addition, diversifying tenant mixes is an appropriate method to reduce risk considering many industries have their own business cycles. Tenants also expect that their neighbours in the same building or surrounding buildings can offer business or cooperation opportunities. Therefore, creating a friendly business eco-system can be considered as a long-term strategy for an office building. Landlords also need to pay attention to emerging sectors for Grade A office buildings, such as coworking space, fintech, and technology and media.

> Also suggest that landlords build smart office operation and service systems to meet the demands of business clients. For the supporting facilities, apart from the necessary and traditional facilities, we expect buildings to diversify configurations by blending in art, health, social, leisure and other functions, such as fitness, leisure clubs and themed restaurants.

In addition, landlords can offer value-added services to the tenants as methods to retain tenants. The following ideas are examples:

> If the landlords own several office buildings in different cities, it is helpful if the tenants can use these office facilities including meeting rooms at discounted rents.

> For those projects far away from the subway station or bus station, landlords can offer shuttle buses to reduce the commuting time for tenants.

> Adding canteens in the office building is also a good method to give a sense of belonging to the tenants.

> Organising social gatherings in the building regularly can improve the relationship of the tenants in the same building.

**New concepts**

Integrating new concepts including art, humanities, green health and technology into property design and operation helps to retain tenants and attract new occupiers. We expect buildings to integrate art decorations and themed marketing such as arts corridors, exhibition halls and other art space to create a unique building culture and eco-system.

In view of the expansion of the flexible workspace sector, we believe landlords also have an opportunity to cooperate with flexible workspace operators. We believe that flexible workspace not only boosts the occupancy rate in properties and enriches the tenant mix of buildings, but also offers a creative work mode conducive to future office needs.

**Building facilities and services**

Both existing and future projects should provide superior facilities and customised services to secure tenants, which are also important factors for the CBD’s prospective tenants. Buildings could improve clients’ experience through superior facilities such as VAV+ ventilation systems, PM2.5 prevention and breathing curtain walls to improve the efficiency in resources usage and the quality of the indoor environment. We
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