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STRONG DEMAND ENCOURAGES MARKET UPGRADES

Summary & Recommendations

Supported by summer vacation spending, the retail sales in Q3 2018 remained active.

- > Although one project entered the market, the average ground floor fixed rent in Beijing's mid to high-end shopping malls levelled off at RMB825 (USD119.9) per sq metre per month in Q3 2018.
- > Since most of the new supply in 2019 is scheduled to be located at suburban areas with lower rents, we project the overall rents to drop slightly in 2019.
- > We recommend landlords adjust their tenant mix and rearrange their space to provide more lifestyle, interactive art, technology or theme-branded shopping experiences.

	Q3 2018	Full Year 2018	2018-22 Annual Average
 <p>Demand</p> <p>> The F&B sector was active, and we expect it to remain so in the future, with the light meal market having the fastest expansion. Lifestyle brands are also increasing their market share.</p>	109,000 sq m	441,000 sq m	379,000 sq m
 <p>Supply</p> <p>> We expect supply of 224,000 sq metres (2.4 million sq ft) to enter the market in Q4 2018, followed by a peak of 630,000 sq metres (6.8 million sq ft) in 2019. 2020 will likely dip to 116,000 sq metres (1.2 million sq ft), before bouncing back to about 400,000 sq metres (4.3 million sq ft) annually in 2021 and 2022.</p>	101,000 sq m	375,000 sq m	383,000 sq m
 <p>Rent</p> <p>> In 2019, heavy new supply in suburban areas will probably drive down rents. However, rents are likely to increase by about 2.4% in 2020 due to limited new supply and strong market demand, staying steady over the following two years.</p>	End Q3/QOQ 0.1% RMB 825	End 2018/YOY 1.6% RMB 829	End 2022/ Annual Average Growth 2018-22 0.3% RMB 840
 <p>Vacancy</p> <p>> Except in 2019, when we expect the vacancy rate may rise to 4% temporarily, the vacancy rate should be pushed gradually lower to less than 2% in 2022 as new vacant space will probably be steadily absorbed.</p>	-0.2pp 2.5%	-1.3pp 1.8%	-0.1pp 2.0%

Source: Colliers International
Note: USD1 to RMB6.88 as of end-Q3. 1 sq m = 10.76 sq ft

Q3 2018 REVIEW

Summer vacation spending boosts retail sales

Beijing's retail market saw a boom in Q3 2018, mostly fueled by the summer vacation, which is the high season for travelling. Beijing's retail sales growth of commodities in Q3 2018 increased to 9% YOY from 8% YOY in Q2 2018. The turnover growth of the food service industry slightly decelerated but still reached 8.8% YOY. The rapid retail sales growth has provided a solid base for the retail leasing market.

SUPPLY AND DEMAND

One project opened in Q3

Fangshan Paradise Walk, developed by Longfor Group, was the only shopping mall that opened in Q3. This mall, with a GFA of 101,000 sq metres (1.1 million sq ft), has increased Beijing's prime retail stock to 5.8 million sq metres (62 million sq ft) during the quarter.

Fangshan Paradise Walk is the third mall in Beijing under Longfor Group's Paradise Walk series, which are one-stop experiential shopping malls. Achieving an occupancy rate of 100% upon opening, the mall has attracted more than 250 trendy brands of different kinds, including the fashion brands UR and Uniqlo; the lifestyle brand SiSYPHE Bookstore; the F&B brand Haidilao Hot Pot; and a Super Species supermarket. Its opening has filled the void of big shopping malls in Fangshan District.

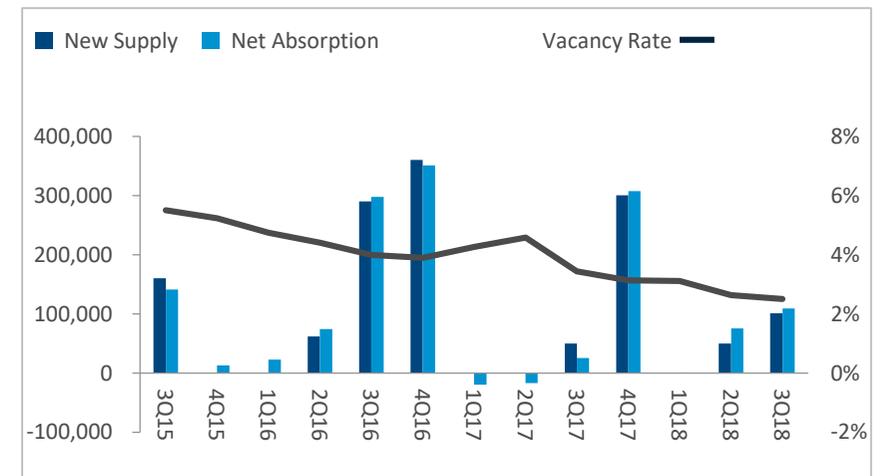
Innovative redesign of shopping mall space to reduce vacancy rate

The vacancy rate at the end of Q3 2018 was 2.5%, down 0.2 percentage points QOQ. Both robust consumption during summer vacation and an active adjustment of tenants by landlords contributed to the low vacancy rate, despite the new supply.

In addition to the improvement of tenant quality, an innovative redesign of internal space is also being undertaken by some shopping malls to make the most of retail space as well as attract customers, especially in emerging submarkets. An area of 1,400 sq metres (15,000 sq ft) on floor B1 of Joy City Chaoyang, formerly a childrens care retailer, has been redesigned and turned into WOODSTAGE. Unlike traditional retail entities, WOODSTAGE is a theme space that encourages events bringing consumers and brands together.

CapitaMall Wangjing has reshaped 4,400 sq metres (47,000 sq ft) of its fourth floor into an art-focused retail space, introducing lifestyle, internet sensation brands and brands incorporating technology.

Beijing mid- to high- end shopping centre new supply, net absorption & vacancy rate (sq metres)



Source: Colliers International Beijing Research

Light meal and lifestyle sectors see major expansion

In Q3 2018, in addition to fashion, F&B expanded as shopping malls adjusted their tenant mix. As a fast-paced lifestyle is increasingly common, stores that serve coffee, new style tea drinks and light meals are gaining more popularity among customers, thus encouraging this market to expand. KFC China launched K PRO in Joy City Chaoyang, a franchise that promotes healthy eating. In addition to opening its third store in Beijing in Zhongguancun, HEYTEA for the first time added two kinds of savoury pastries to its menu. A multi-level Starbucks flagship store opened in Beijing Fun, becoming the second largest flagship store globally. Luckin coffee, a major local rival of Starbucks in China, has announced the introduction of light meals to its menu, promoting this with 50% off until the end of 2018.

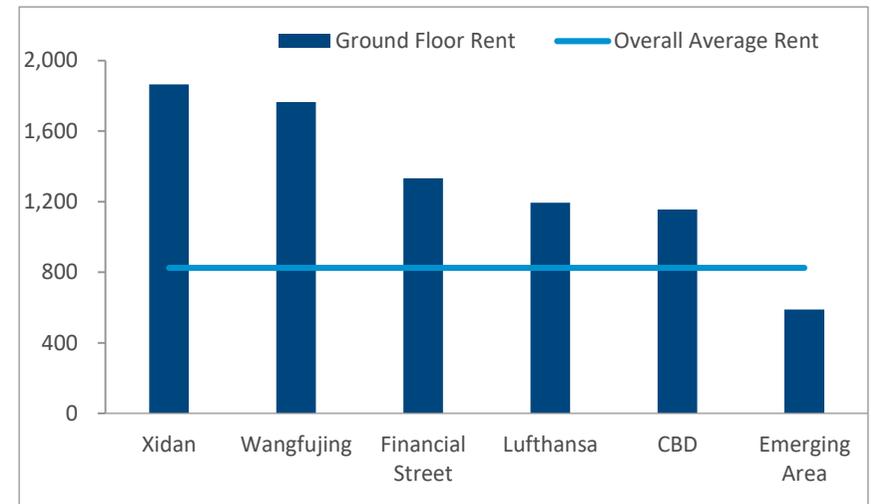
The lifestyle sector also expanded during Q3. HKTDC Design Gallery, established by the Hong Kong Trade Development Council, opened a store in Beijing APM. The brand features the promotion of products from Hong Kong designers and brand manufacturers. Experiential boutique bookstores Yanyouji and CITIC Books + Coffee each opened a store in WF Central and Daxing Paradise Walk respectively.

Rents remain stable

Landlords continued to adjust their tenant mix in Q3 2018, and rents in prime submarkets such as Wangfujing have declined to a level where high-quality tenants are willing to make commitments to large spaces. However, projects in emerging areas have seen their rents rising due to the increasing success of their tenants.

The demand of the overall retail market is still growing. Although there was one new project entering the market in Q3 2018, the average ground floor fixed rent in Beijing's mid to high-end shopping malls stayed steady at RMB825 (USD119.9) per sq metre per month in Q3 2018.

Beijing mid- to high- end shopping centre average ground floor fixed rent by submarket (RMB psm per month)



Source: Colliers International Beijing Research

Major new leases and openings Q3 2018

Property	Brand	TRADE
Beijing APM	sandro	Fashion
Beijing APM	HKDTC Design Gallery	Lifestyle
Livat Xihongmen	Victoria's Secrets	Fashion
Joy City Chaoyang	K PRO	F&B
Beijing Fun	Starbucks Flagship Store	F&B

Source: Colliers International Beijing Research

RETAIL FORECAST

Landlords are improving tenant mix

Landlords are tending to revise their tenant mix especially by bringing in experiential sectors to meet the growing and diverse demands of young consumers. According to the future plan of Joy City – Chaoyang, nearly 10,000 sq metres (1.1 million sq ft) of the mall area will be upgraded, including a fashion space on the fourth floor, and a multi-sectional area incorporating fitness, fashion, F&B and a Joint Publishing bookstore on the ninth floor. Since 2016, flexible workspace operators have been increasingly taking space in shopping malls, supporting the trend of shopping malls looking to drive more retail traffic. Longfor Group has launched its own flexible workspace brand EASYWORK in its Changying Paradise Walk mall in November 2016. CapitalLand has set up URWork in Capital Mall Wangjing in June 2017. WeWork entered Beijing Fun in August 2018, and is slated to open in Joy City – Chaoyang. We foresee the border between retail and other types of property continuing to blur, as increased diversity of tenants can help to drive foot traffic and retail sales.

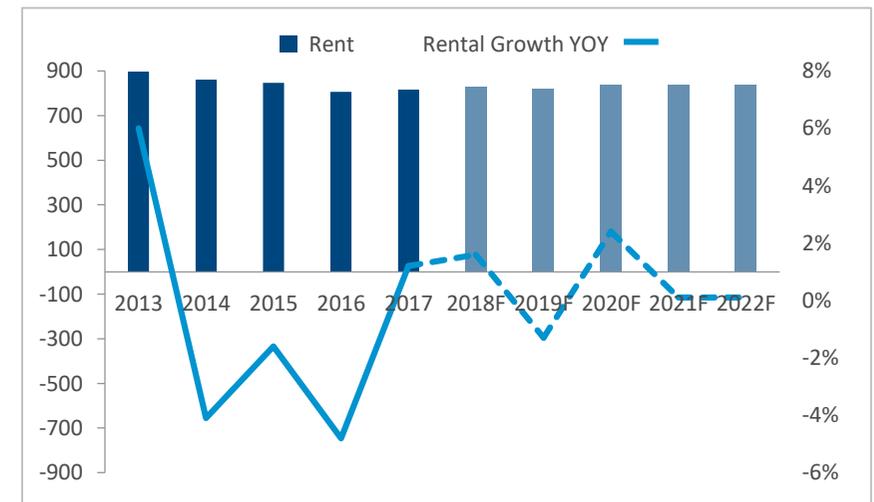
Rents will gradually pick up as prime area stock increases

We expect the new supply in Q4 2018 to be about 224,000 sq metres (2.4 million sq ft). This new supply will probably be absorbed quickly due to the strong retail market demand along with the fact that this new supply is managed by large, well established landlords. As a result, the overall vacancy rate should continue to decline 0.2 percentage points to 2.3%, pushing the rent slightly upward to RMB829.4 (USD120.60) in Q4 2018.

In 2019, we predict a peak in new supply of 630,000 sq metres (6.8 million), thus raising the overall vacancy rate to 4%. Since more than 90% of the new stock in 2019 is scheduled to be located in suburban areas outside the Fifth Ring Road, overall rents will probably decrease by 1% YOY to RMB818.5 (USD119.0) psm per month.

We predict that 2020 will experience a low point in new supply, bringing down the overall vacancy rate. New supply as scheduled should rebound and continue increasing in 2021 and 2022, especially in prime submarkets, where rents are much more expensive. Therefore, overall rents should pick up gradually during 2021 and 2022.

Beijing mid- to high- end shopping centre average ground floor fixed rent forecast (RMB psm per month)



Source: Colliers International Beijing Research

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