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## OFFICE LEASING PACE SLOWED IN Q4

**Summary & Recommendations**

2018 new supply in the Xi'an Grade A office market was 301,100 sq m, while net absorption reached 273,100 sq m. Due to a drop in demand, the average rent declined 0.8% yoy, and the vacancy rate was 31.7%.

- > We predict 2019 new supply will soar to 595,700 sq m.
- > In 2019 the average rent will likely decline due to an influx of new supply, before rebounding with less new supply planned from 2020.
- > As a potential CBD, Hi-tech Zone would be competitive for tenants to expand and upgrade due to the relatively heavy new supply and low rent next to City North. For landlords, astute pricing considering location and the vacancy rate is the key to attract businesses.

	Q4 2018	Full year 2019	2018-23 Annual Average
 <b>Demand</b> <ul style="list-style-type: none"> <li>&gt; In Q4 the majority of demand came from the financial services and flexible workspace sectors. We predict in 2019 net absorption will increase 13.5% yoy due to a reviving economy.</li> </ul>	60,500 sq m	310,000 sq m	280,500 sq m
 <b>Supply</b> <ul style="list-style-type: none"> <li>&gt; According to developers' schedules, we predict new supply in 2019 will climb sharply to 595,700 sq m, a 98% yoy gain.</li> </ul>	100,300 sq m	595,700 sq m	307,300 sq m
	QOQ / End Q4	YOY / End 2019	Annual Average Growth 2018-23 / End 2023
 <b>Rent</b> <ul style="list-style-type: none"> <li>&gt; We forecast in 2019 average rent will decline by 0.5% yoy on the back of new supply, before rebounding in 2020 as the quantity of new supply tapers off.</li> </ul>	-1.2% RMB104.9	-0.5% RMB104.4	1.0% RMB110.2
 <b>Vacancy</b> <ul style="list-style-type: none"> <li>&gt; In 2019 a sharp increase in supply will probably push the vacancy rate up to 33.2%. After the peak in 2019, we expect the vacancy rate to decline sequentially due to lower supply, eventually falling to 17.1% by 2023 year-end.</li> </ul>	0.6pp 31.7%	+1.5pps 33.2%	-2.9pps 17.1%

Source: Colliers International  
Note: 1 sq m = 10.76 sq ft. USD1 = RMB6.85 at end Q4. "PP = percentage point".

# LEASING MARKETS AND RENTS

## Two projects were completed in Hi-tech Zone

In Q4, two new projects were recorded, adding a total of 100,300 sq metres (1,079,228 sq feet) of space to the market:

- > Huicheng International Tower located
- > ICI G

In Q4 2018, Xi'an's Grade A office market totalled 1,453,400 sq metres (15,638,500 sq feet), a 7.4% qoq increase.

## Vacancy rate edged up due to falling demand

### Falling demand

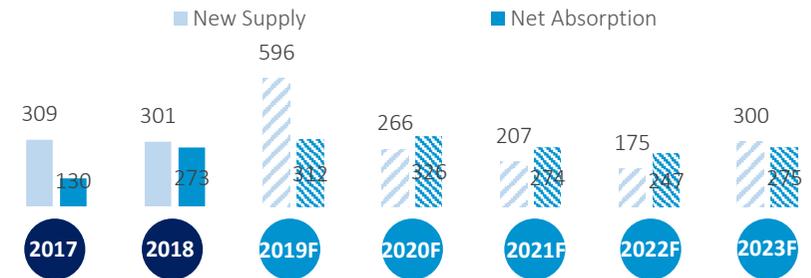
In 2018 new supply was 301,100 sq metres (3,239,840 sq feet), which was flat growth yoy. As Q4 is traditionally a slow season for office leasing in Xi'an, net absorption dropped by 3.8% qoq to 60,500 sq metres (650,980 sq feet). In 2018, total net absorption reached 273,100 sq metres (2,938,556 sq feet), a 8.5% yoy decline as demand softened amid concerns about a temporary economic slowdown. As a result, the vacancy rate rose 0.6pp qoq to 31.7%.

By submarket, the Hi-tech Zone accounted for the largest proportion of net absorption, recording a total of 46,400 sq metres (499,264 sq feet). This was due mainly to two major flexible workspace leasing transactions in Q4.

In Q4, City North continued its strong performance, with net absorption of 12,800 sq metres (137,730 sq feet). As a result, City North saw the largest drop in vacancy among all submarkets in Q4, as vacancy dropped 5.4 pps qoq to 38.8%. In Q4, lower total stock and more net absorption compared to other submarkets led to the largest drop. At the same time, with the opening of Metro Line 4, the accessibility was improved, and it attracted enterprises into City North, which we expect to continue.

In Q4 flexible workspace expansion remained one of the bright spots for Xi'an's Grade A market, as highlighted by FUNWORK's lease of 4,300 sq metres (46,270 sq feet) at Huicheng International Tower. In 2019 flexible workspace operators will probably remain active as several operators are still searching for new space, alleviating some pressure from the new supply.

Supply, net absorption ('000 sq metres)



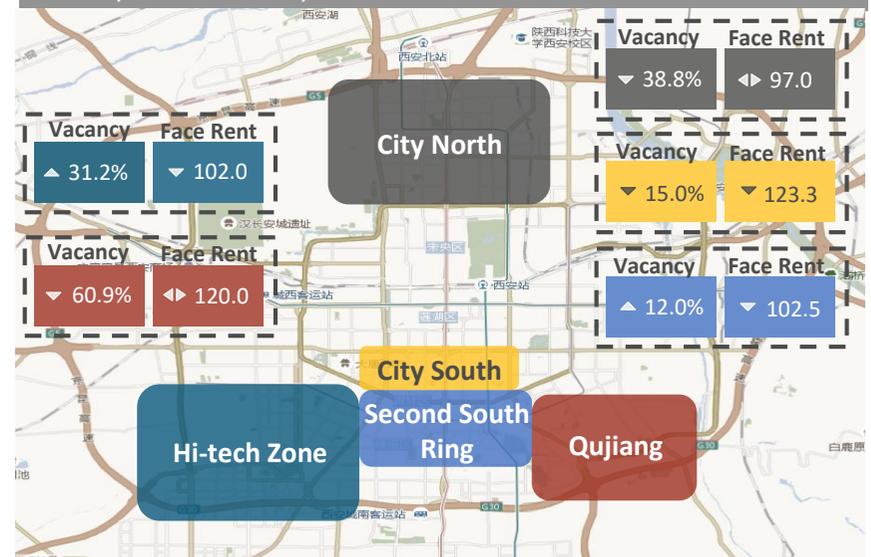
Source: Colliers International

Vacancy rate



Source: Colliers International

Vacancy rate & rents by submarket



Source: Colliers International

### Rents dropped slightly

In Q4 2018, the influx of new supply put pressure on rents in Xi'an, forcing landlords to cut prices to maintain their occupancy rates. Consequently, the average rent of Grade A offices dropped by 0.8% qoq to RMB104.9 (USD15.3) per sq metres per month.

By submarket, rent in Hi-tech Zone declined by 0.4% qoq to RMB102 (USD14.9) per sq metres per month. In addition, in Q4 South Second Ring witnessed the sharpest decline, dropping by 4.7% qoq, as rents in this area were negatively impacted by increasing competition from other submarkets.

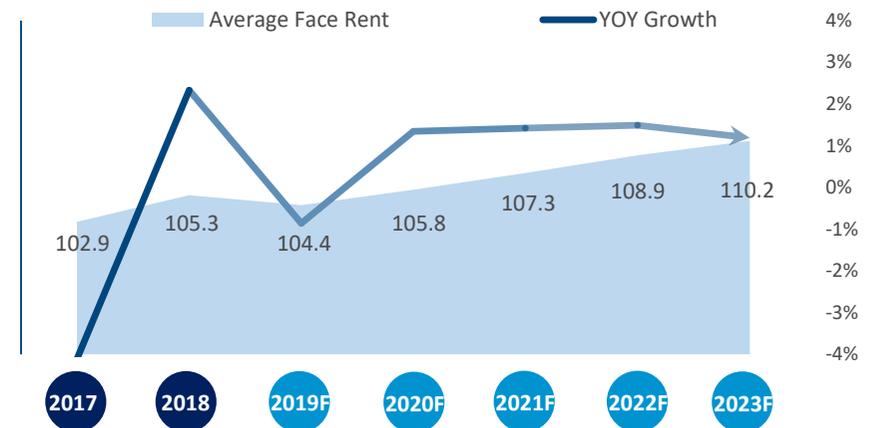
### Demand highlights

Television broadcast and media companies are now clustering in the Qujiang submarket, as local municipalities are offering cash incentives to companies whose television series win awards in film festivals at home and abroad. We expect more media and TMT related businesses to cluster in Qujiang in the future.

The engineering and architectural design industries are now gaining local government support, as highlighted by Xi'an's 2018 Construction Land Supply Plan proposal<sup>1</sup>, which plans to release 908 pieces of construction land with a total area of 54 million sq metres (581,251,160 sq feet) to relevant industries. Colliers expects demand from the engineering and architectural design industries to grow in the next few years in Xi'an, which should help boost the demand for Grade A office buildings.

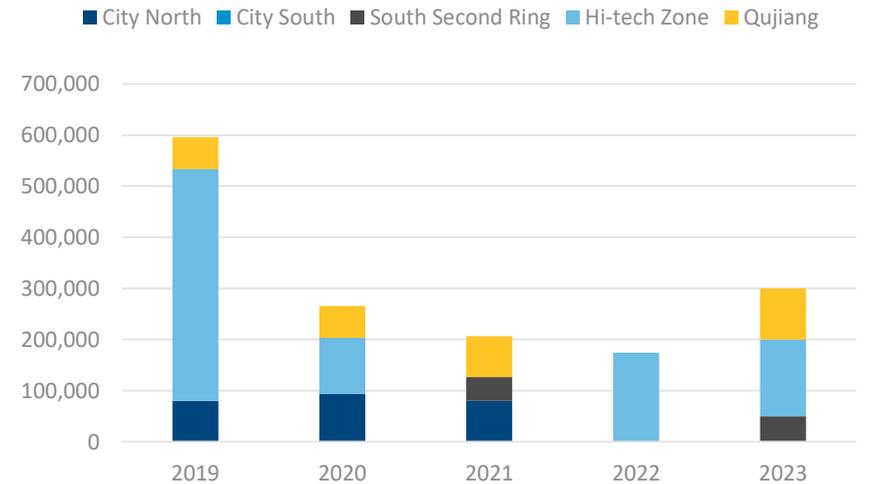
<sup>1</sup> [http://gtzy.xa.gov.cn/ptl/def/def/index\\_954\\_6034\\_ci\\_trid\\_2947474.html](http://gtzy.xa.gov.cn/ptl/def/def/index_954_6034_ci_trid_2947474.html)

Rents (RMB per sq metres per month)



Source: Colliers International

Future supply by submarket (sq metres)



Source: Colliers International

## OUTLOOK

### Future supply is concentrated in Hi-tech Zone

From 2019 to 2023, about 1,088,000 sq metres (11,706,880 sq feet) of Grade A office space is planned in the Hi-tech Zone submarket, which represents 75% of total future supply in the city. By 2023, the total Grade A stock in Xi'an should increase by nearly 100% from 2018 levels to 2,896,000 sq metres (31.2 million sq feet).

Given the volume of new supply that we predict in 2019, Colliers expects the vacancy rate to increase 1.5 pps to 33.2% in 2019, but then to decline steadily to 17.1% by 2023 year-end. In 2019, rents are at risk of falling due to heavy supply, but in 2021 to 2023 we expect a rebound due to lower new supply and vacant space. We believe that average annual rental growth will be 1.0% yoy over the period 2018-2023.

### Incentives driving investment demand

In order to attract investment and talent, Xi'an has promulgated ten preferential policies covering various sectors including high-tech, advanced manufacturing, civil-military integration and financial services. For high-tech companies that meet the requirements, Xi'an has set up a RMB100 billion (USD14.6 billion) Science and Technology Industry Development Fund that will provide incentives of up to RMB5.0 million (USD739,645). Preferential subsidies bringing the tax rate down to 15% are also available. In addition, incentives and subsidies are also provided to individuals as part of the talent retention programme.

As a regional hub, Xi'an should attract more enterprises to incorporate, thanks largely to government support policies, a build-out of its transportation system, excellent educational resources, and investment subsidies. Colliers expects Xi'an to see rapid development of high-end manufacturing, science and technology, finance and professional services in the future.

### Major leasing transactions in Q4

Property	Tenant	Industry	Sq metres
Efin International	Tongjia Auto	Automobile & Components	5,200
Huicheng International	FUNWORK	Co-working	4,300
Enterprise Headquarters Building	Haier	Wholesale/ Retail	2,500
Huicheng International	Cendes	Professional Services	1,400

Source: Colliers International

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