

Intelligent Investment

# Commercial Real Estate in the Era of High-Quality Economic Development

REPORT

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CBRE  
CHINA RESEARCH

DECEMBER 2023

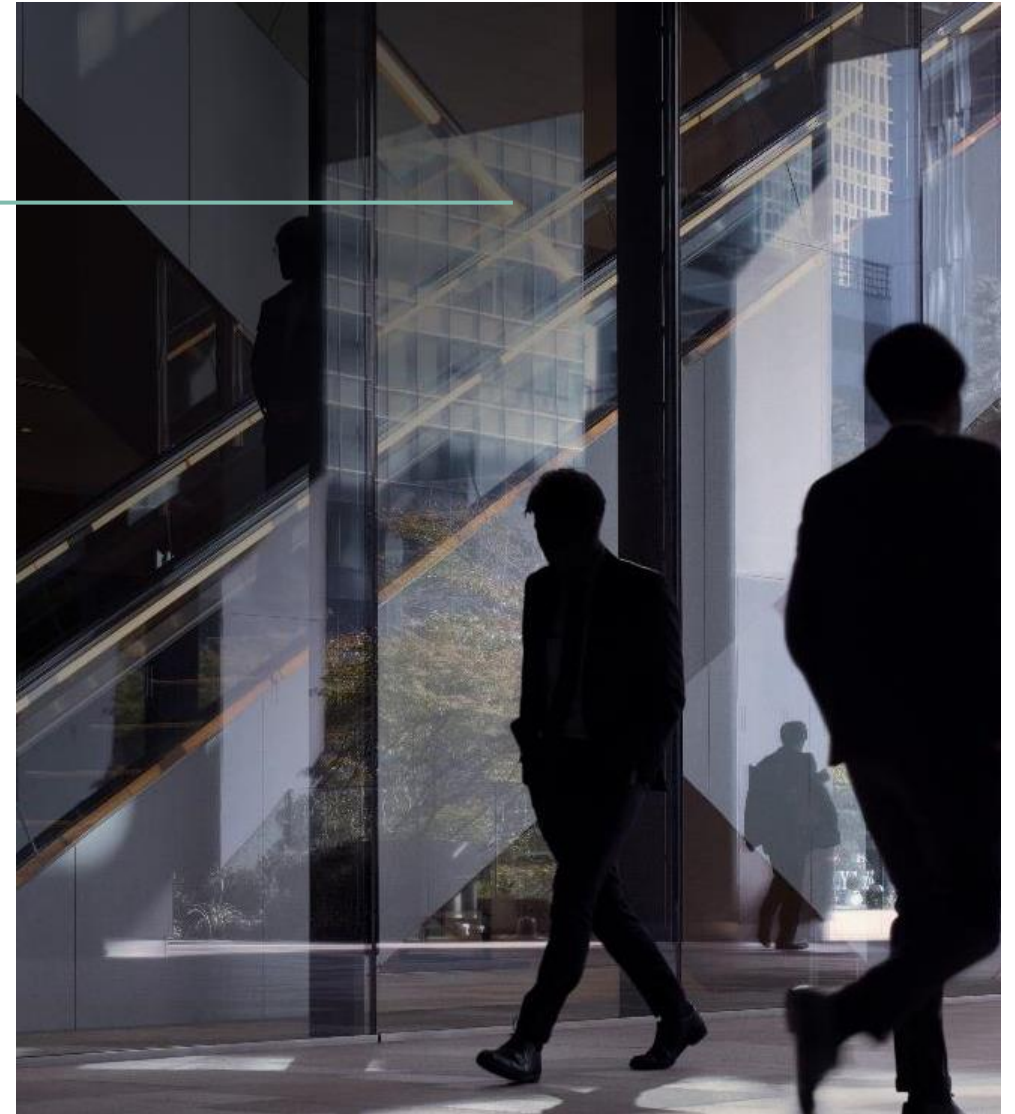
CBRE



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# 1

Shift in growth engines;  
Focus on high-quality  
development



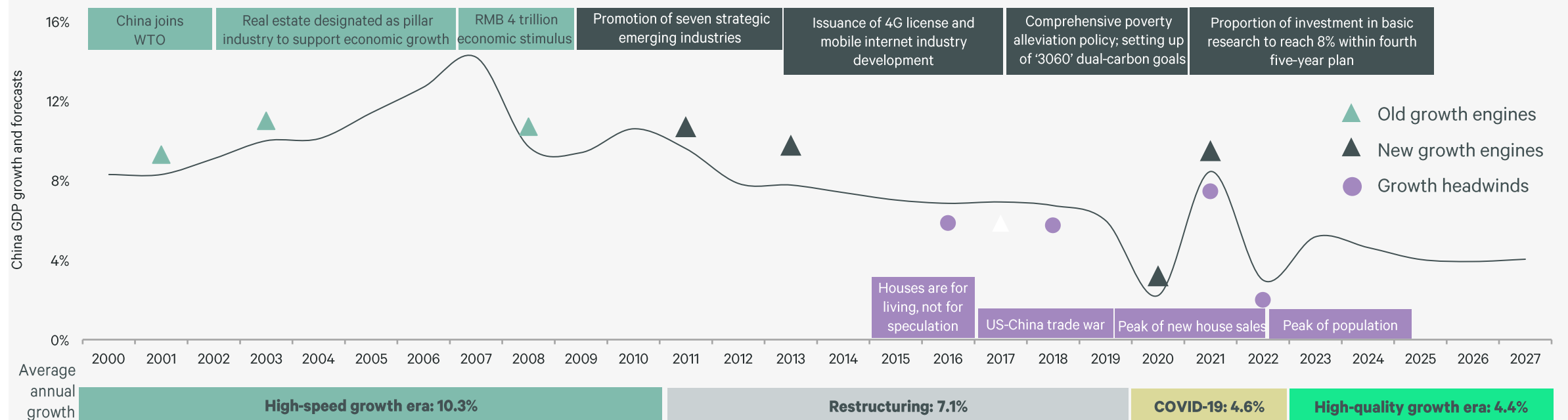
# New economic drivers to characterise high-quality growth period

Following the relaxation of pandemic-related controls at the end of 2022, China's GDP growth rebounded strongly, reaching 5.2% y-o-y in the first three quarters of 2023. China's short-term economic outlook nevertheless remains challenging due to volatile external economic and geopolitical conditions, along with still fragile business expectations and consumer confidence.

Medium and long-term economic indicators indicate that China is entering a new phase of economic growth. Exports, investment, and human capital, which have underpinned China's high-speed growth over the past 20 years, are gradually slowing. New home sales fell by 25% last year after peaking at 1.7 billion sq. m. in 2021, while the country's population declined for the first time in 60 years in 2022.

As new growth drivers emerge and propel China's economy into a new era of high-quality growth, the sustainability of economic development, economic structural adjustment and industrial upgrading, as well as improvements to the quality of life of the general population, will assume greater importance than ever before.

**Figure 1: China GDP growth rate and forecast**



Source: National Bureau of Statistics, CBRE Research, December 2023

## From Resource driven to Innovation driven

- Fixed-asset investment in China grew by 2.9% y-o-y in the first three quarters of 2023. While investment in real estate fell by 9.3% y-o-y, high-tech industries grew logged an increase of 11.1% y-o-y, indicating a shift in the composition of economic growth.
- The 2022 Global Innovation Index (GII) published by the World Intellectual Property Organisation (WIPO) ranked China 12th worldwide. A total of 24 of the world's top 100 scientific and technological innovation clusters were in China, the highest of any country.
- With China announcing in 2020 that it would aim to have CO2 emissions peak before 2030 and achieve carbon neutrality before 2060, the country's economic trajectory is now turning towards green and sustainable development.

## From abundant human capital to Abundant educated human capital

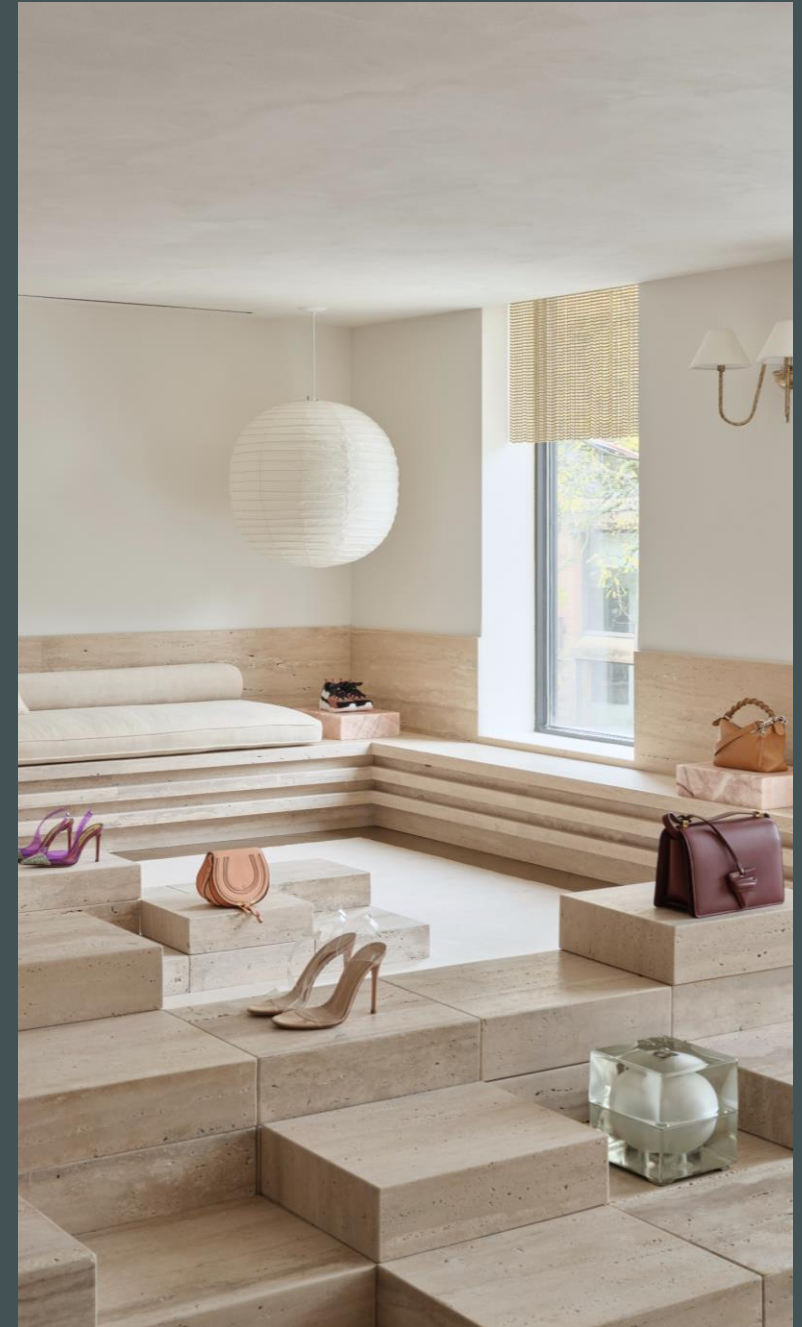
- China's birth rate has stood at below 10 per 1,000 since 2020, with the country's total population dropping by 850,000 in 2022. The proportion of the elderly population aged 60 and above is expected to reach 25% by 2030.
- At the same time, the country's supply of educated human capital is increasing. There was a total pool of over 240 million university graduates in 2022, with the number of graduates expected to exceed 10 million per year from 2023 to 2025.
- According to the China ICT Talent Ecology White Paper jointly released by Huawei and Ernst & Young in 2022, China is suffering from a lack of talent in emerging fields such as cloud computing, big data, IoT, AI and 5G. It is predicted that the ICT talent gap will continue to widen, reaching over 20 million by 2025.

## From export oriented to Consumption oriented

- As the shift in China's demographic and income structures continues, households in big cities and middle- to high-income households will become key to consumption upgrading.
- The country's population continues to flow into big cities, with the number of permanent residents of China's top 20 GDP cities increasing by 3.99 million in 2022, contrasting with the decline of 30,000 in the number of people residing in all cities nationwide.
- According to McKinsey's China Consumer Report 2023, China was home to 138 million households with annual incomes of over RMB 160,000 in 2021. Another 71 million households are forecasted to join this income bracket by 2025.

# 2

Shifting gears and  
improving quality;  
New leasing trends



# Shifting gears and improving quality: five new business and consumer trends

As technological innovation and consumption upgrading emerge as new engines of economic growth, corporate strategic decision-making and residents' consumption behaviour will change accordingly.

These qualitative changes will drive the structural evolution of China's commercial real estate demand in four areas - **quantity, quality, efficiency and sustainability** – and creating a multitude of new investment opportunities.



## New consumer demand

Rising incomes will elevate consumers' expectations for goods and services, resulting in higher quality and wider range of choices. Consumption environment and experience will also become more important.



## Emerging business engines

Strategic emerging industries<sup>1</sup> will continue to flourish and become a crucial pillar of economic upgrading and transformation, driving corporate investment in R&D and talent.



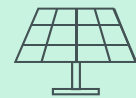
## Higher quality real estate

As China's population demands improved living, consumption and working conditions, this will drive demand for higher quality residential, retail and office real estate.



## Improving efficiency

With enhancing efficiency set to be a core objective of future business development, companies will seek efficiency-enhancing solutions such as digitalisation and artificial intelligence to optimise business operations.



## Embracing sustainability

China's 3060 dual-carbon target will accelerate green development and encourage corporations to factor in sustainability criteria into business behaviour and corporate decision-making.

Note 1: According to the 'Classification of Strategic Emerging Industries (2018)' issued by the National Bureau of Statistics, strategic emerging industries include advanced technology, high-end equipment manufacturing, new materials, biotechnology, new energy & new energy vehicles, environmental protection and digital creative industries.

# Office

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- Strategic emerging industries typically have a high concentration of talent and technology and have therefore become a major source of demand for quality office space and R&D facilities. CBRE expects tier I and tier II cities with sufficient talent availability to be a priority for corporate site-selection and expansion.
- With 81% of China-based respondents to CBRE's 2022 Global Live-Work-Shop survey believing that the quality of working environment is more important compared to the period before the onset of the COVID-19 pandemic, flight-to-quality occupier demand will continue to grow.
- Abundant new Grade A office supply scheduled to come on stream in the emerging business districts of China's major cities over the next three years will provide favourable conditions for occupier expansion while ensuring real estate expenditure remains under control.



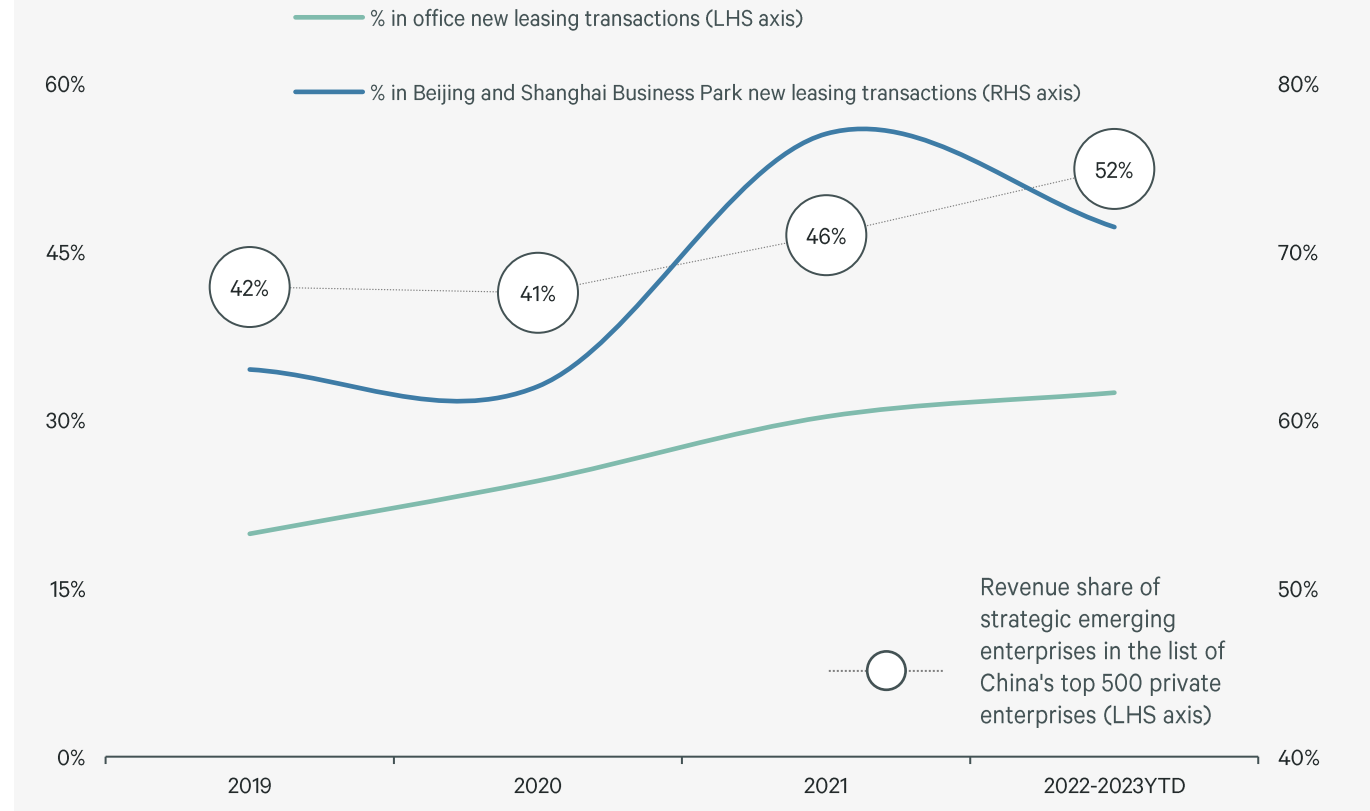
# Strategic emerging industries to drive demand for quality office and R&D space

Against the backdrop of China's shift to higher quality economic growth, the development of strategic emerging industries including advanced technology, biotechnology, and high-end equipment manufacturing is accelerating. The revenue share of strategic emerging enterprises reached 52% in the list of China's top 500 private enterprises in 2023, an increase of 10-pps compared to 2019.

In comparison to traditional manufacturing industries, strategic emerging industries are very talent-and technology-capital-intensive. High quality office and R&D space is therefore crucial to their daily operations. CBRE data show that **strategic emerging enterprises' share of new office leasing transactions nationwide increased from 24.6% in 2019 to 32.5% in the first three quarters of 2023**. Firms from these industries accounted for more than 70% of new leasing transaction volume in Beijing and Shanghai business parks between January-September of this year.

China's 14th Five-Year Plan proposes that "the average annual growth rate of society-wide R&D expenditure will achieve more than 7% during the period of 2021-2025, and the added value of strategic emerging industries will account for more than 17% of GDP by 2025 (compared to 13% in 2022). This will ensure steady demand for related office and R&D properties in the coming years.

Figure 2: Revenue share of strategic emerging enterprises in the list of China's top 500 private enterprises along with their historical share of office and business park leasing transactions in Beijing and Shanghai.



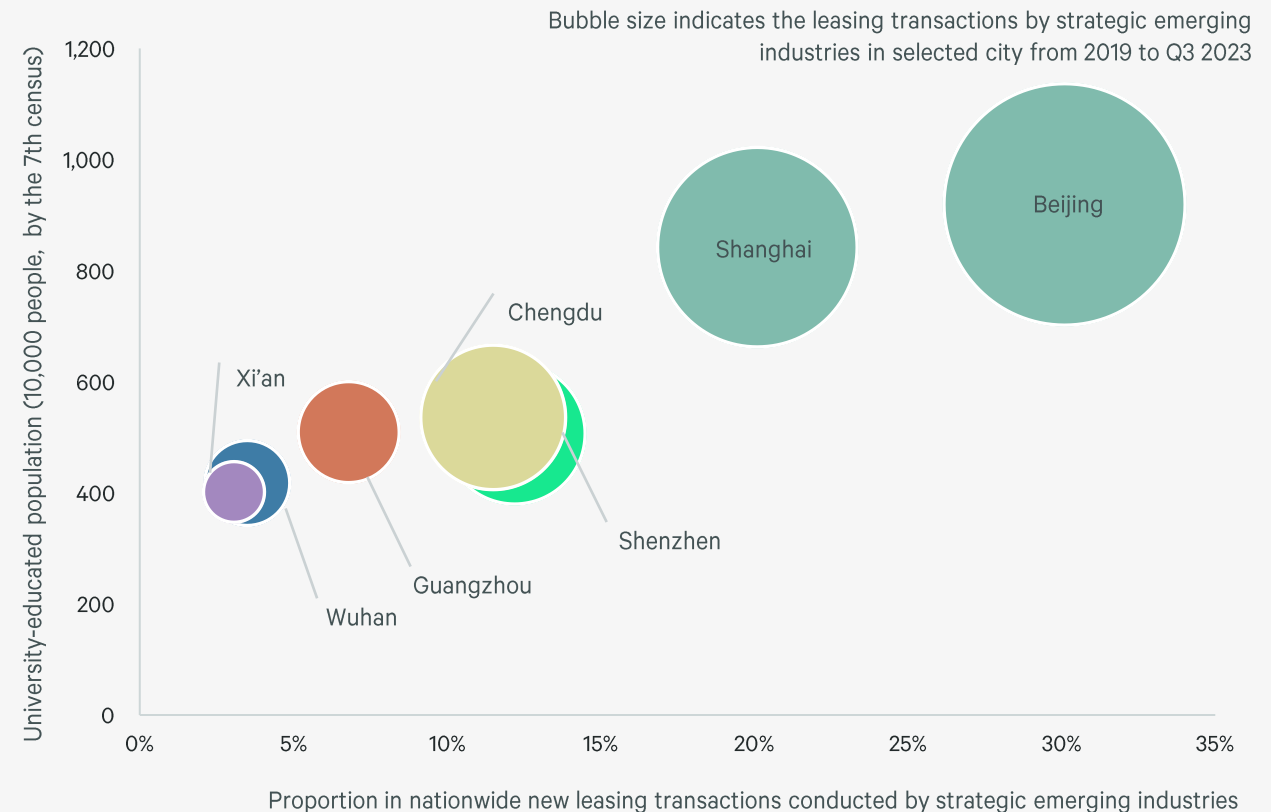
Source: All-China Federation of Industry and Commerce, financial reports of listed companies, CBRE Research, December 2023

# Talent-rich tier I and tier II cities to be priority for site-selection and expansion

Talent availability is a necessary precondition for the development of strategic emerging industries. Beijing, Shanghai, Chengdu, Shenzhen, Guangzhou, Wuhan and Xi'an are among the top 10 cities in China in terms of the size of their university-educated population. These cities collectively host around half of the country's 985 universities and are therefore assured of a continuous inflow of talent.

Office selection by firms operating in strategic emerging industries is highly correlated with the distribution of talent. CBRE data show that **between the beginning of 2019 and September 2023, 84% of new office leases signed by strategic emerging industries were in the above seven major cities**. Beijing and Shanghai were the two most popular destinations, accounting for over 50% of new leasing transactions.

Figure 3: Talent and office leasing demand of strategic emerging industries in key cities



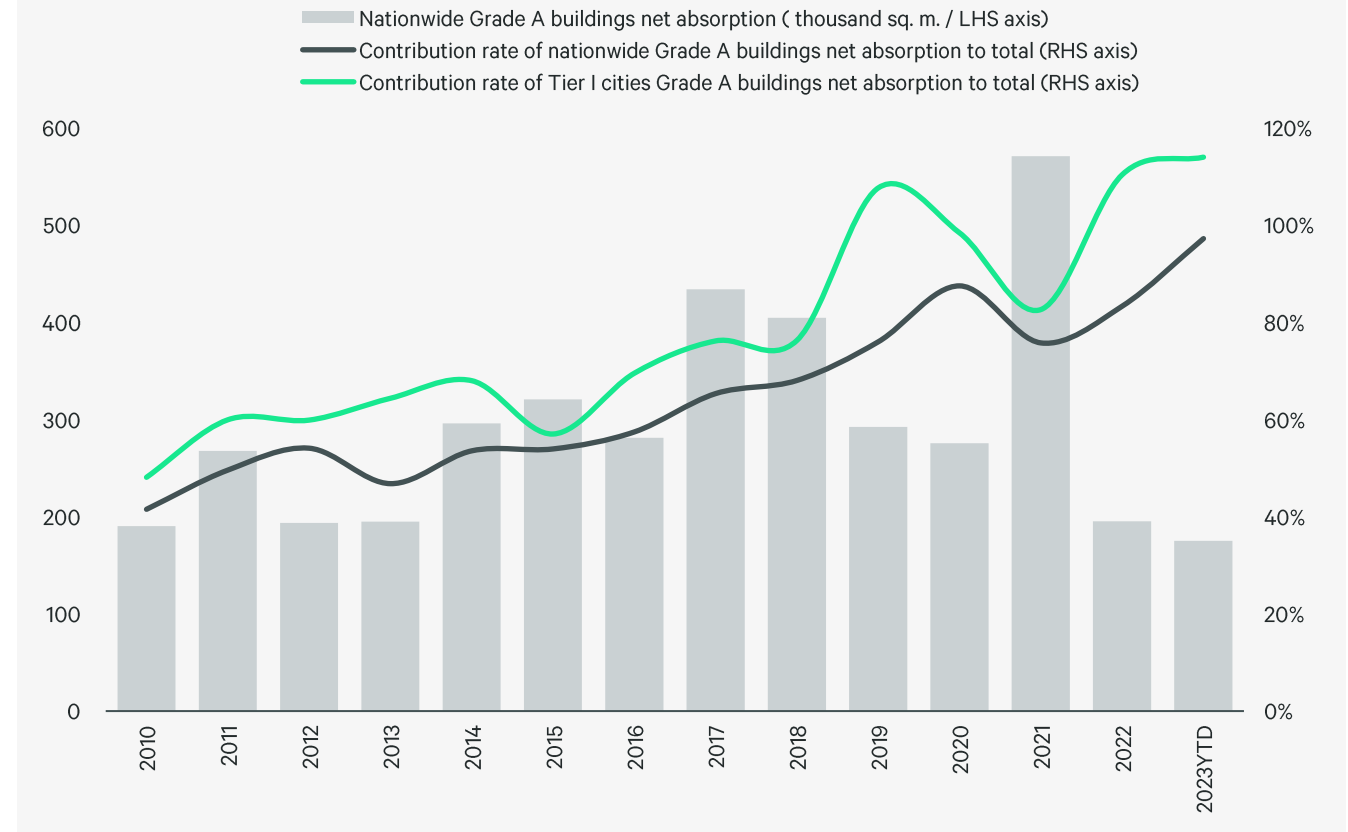
Source: National Bureau of Statistics, CBRE Research, December 2023

# Growing flight-to-quality demand for corporate office space

In addition to new demand created by the emergence of new economic engines, occupiers' growing emphasis on the quality office space is set to result in a substantial volume of new office requirements. Grade A buildings in 18 major Chinese cities tracked by CBRE accounted for 97% of office net absorption in first three quarters of 2023 as Grade B buildings continued to lose favour.

Respondents to CBRE's 2023 China Office Occupier Survey **named flight-to-quality as one of their top three preferred real estate strategies for a third consecutive year**. On the supply side, average annual new supply of Grade A office stock in major cities is expected to exceed 7 million sq. m. over the next three years, of which 63% will be in emerging business districts and greater CBDs. Abundant new supply will provide favourable conditions for occupiers to expand and upgrade their office space while keeping real estate expenditure in check.

Figure 4: Grade A offices' share of nationwide and tier I city net absorption



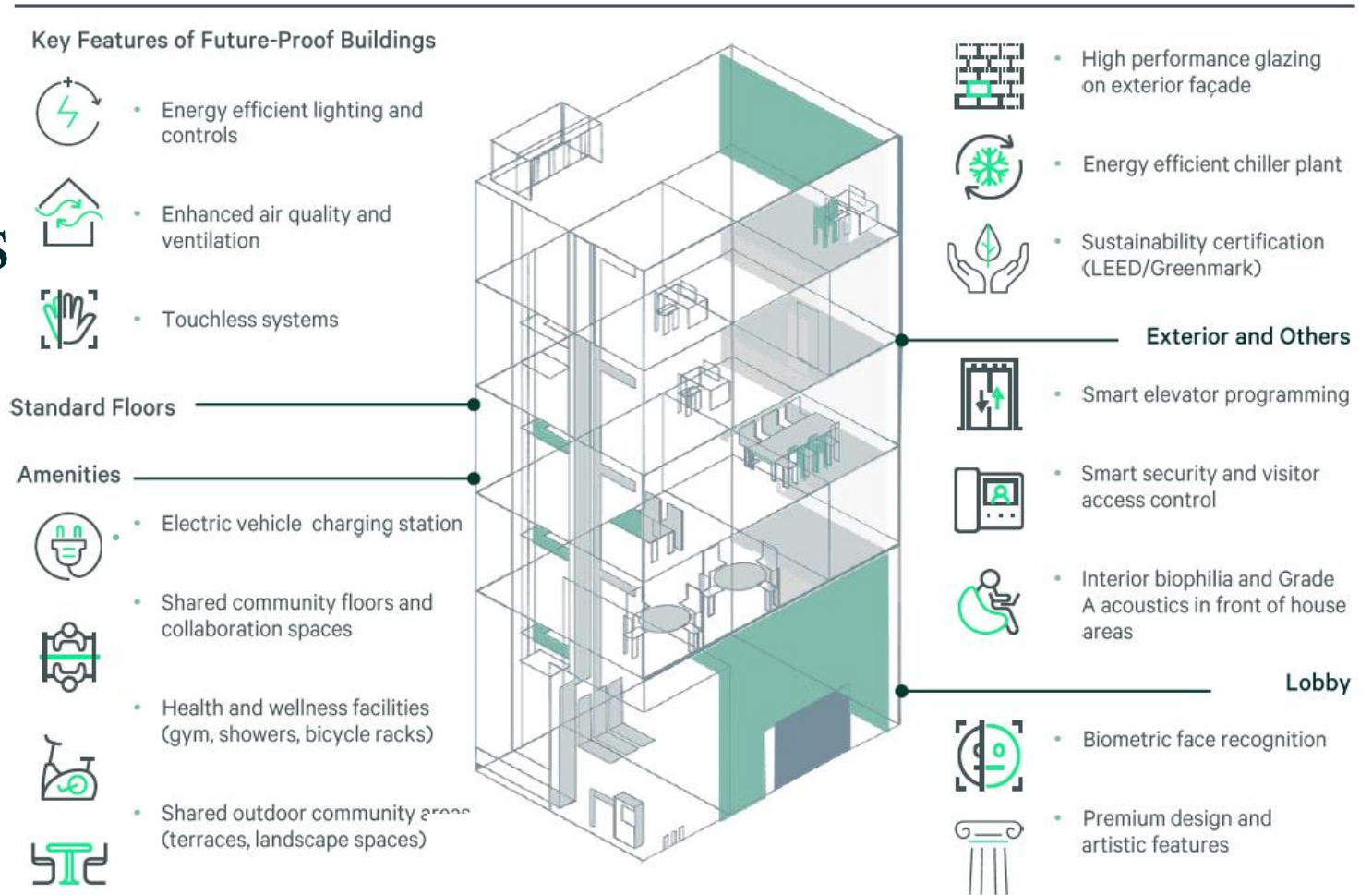
Source: CBRE Research, December 2023

# Employees' need for quality to drive demand for future-proof buildings

Occupiers' flight-to-quality demand is a direct result of employees' calls for more attractive workplaces. Some 81% of China-based respondents to CBRE's 2022 Global Live-Work-Shop Survey said they believe the quality of the working environment is more important now than it was before the pandemic, the highest such rate globally. In particular, employees require higher quality physical environments, spatial layouts and smart offices; a trend CBRE expects to drive demand for advanced future-proof buildings.

Figure 5: Key workplace features required by employees and proportion of respondents

- **85%** Environmental features (natural daylight, better air quality, acoustics etc.)
- **85%** living space within the office building
- **82%** Availability of car parking
- **81%** Availability of focus space for concentrated work
- **79%** Improve technology in the office



Source: 'Why Asia Pacific Offices are different and now is the time to invest', CBRE Research, December 2023

# Logistics

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- Amid a raft of headwinds including economic uncertainty, rising costs and geopolitical tension, logistics tenants are optimising operations by upgrading warehouse specifications and automation to strengthen supply chain efficiency and resilience.
- A recent CBRE survey of China-based logistics tenants identified rooftop solar electricity panels, known as photovoltaics (PV), and new energy charging piles as the most important facilities logistics tenants wish to see added or upgraded in future warehouses. These technologies can also help tenants reduce carbon emissions in the supply chain.



# Enhancing supply chain efficiency through warehouse location, specification, and automation

For companies to participate in China's coming period of high-quality development, improving operational efficiency will be essential. With the COVID-19 pandemic and recent geopolitical conflict having underlined the fragility of supply chains, enhancing resilience is a key focus throughout the logistics industry. Mirroring these concerns, CBRE's 2023 China Logistics Occupier Survey found that respondents were more worried about operational challenges such as economic volatility, rising costs and geopolitics compared to two years ago. In response, logistics occupiers are adopting a range of strategies to reduce costs and increase efficiency including network optimisation, warehouse upgrading and automation.

Some 82% of respondents intend to expand their logistics real estate footprint in tier I clusters. With regard to specific locations, CBRE expects respondents to prioritise sites close to transportation, consumers or manufacturers and suppliers, rather than facilities offering lower rents. This indicates that enterprises now consider warehouses as part of logistics networks in terms of total cost. According to CBRE's cost analysis of large logistics companies, reducing transportation and labour expenses by 1% can offset an 8%-9% increase in warehouse leasing costs.

Around 76% of logistics occupiers intend to increase in-city modern logistics warehouse space in the next three years, while just 20% of occupiers (mostly 3PLs) plan to increase their in-city traditional warehouse space. CBRE expects the drive towards efficiency and supply chain safety to spur increased demand for modern logistics warehouses, as warehouse automation and intelligent management tools can only be accommodated within newer, higher specification facilities.

Figure 6: '2023 China Logistics Survey', respondents' selection of locations and facilities, as well as adoption of warehouse automation over the next three years

What are the top factors you consider when deciding where to locate your logistics facilities?

94%

Of respondents wish to be proximity to public transportation, markets and customers, and point of production and suppliers.

Which of the following types of logistics facilities do you expect to use more?

76%

Of respondents prefer in-city modern logistics warehouse

Has your company already adopted or does it plan to adopt warehouse automation system?

60%

Of respondents has adopted or plan to adopt warehouse automation system

Source: '2023 China Logistics Occupier Survey', CBRE Research, December 2023

# Reducing carbon in the supply chain through green energy hardware

The government's "3060" pledge to have CO2 emissions peak before 2030 and achieve carbon neutrality before 2060 have placed sustainable development and low carbon front and centre of China's economic transformation. According to the UN's Net Zero Tracker 2023 Global Stocktake report, 149 countries and regions globally have set net zero targets. These markets represent 88% of the world's greenhouse gas emissions and 92% of the global economy. Forbes Global 2000 Companies report found that the number of listed companies that have set net zero targets reached 929 in 2020, more than double the previous year's total.

As a transportation node, green warehouses play an important role in reducing carbon emissions for manufacturers, traders, and transporters. Respondents to CBRE 2023 China Logistics Survey expressed a strong belief that the coming years will see significant demand for upgrading green energy facilities, **with roof top solar power (45%) and electric vehicle charging (44%) named as the most popular options.**

Warehouse roofs are large and flat, making it easier to install solar electricity panels, known as photovoltaics (PV), which capture the sun's energy and convert it into electricity. As warehouses are typically located in the suburbs where there are fewer tall buildings, they can capture abundant sunshine and therefore possess higher power generation efficiency. Enterprises with large real estate portfolios can obtain green power certificates to use surplus green energy produced by their warehouses and offset the carbon emissions of other types of real estate such as offices and shopping malls.

Figure 7: '2023 China Logistics Survey', How do you expect your building specifications and service requirements to change in future?



45%

**Roof top solar power**



44%

**NEV charging power**

Source: '2023 China Logistics Occupier Survey', CBRE Research, December 2023

# Retail

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- With the rapid rebound of offline consumer traffic after the lift on epidemic prevention and control measures, physical stores still play an irreplaceable role in the omnichannel retail chain.
- Physical stores are accelerating their evolution to a comprehensive place with the attributes of consumption, service, experience and socialization, and "quality" over "quantity", experience-driven sales and community creation will be the important direction for retail brands to strengthen their physical store networks in the future.



# Brick-and-mortar stores are irreplaceable, but functionally positioned to accelerate transformation

Retail footfall has staged a strong recovery this year as the country exited zero-covid controls. Data from China's State Ministry of Commerce show that passenger traffic in key shopping areas in 36 large and medium-sized cities across the country increased 164% y-o-y in the first seven days of the 2023 Golden Week holidays in October.

The rapid rebound in offline consumer traffic following the lifting of pandemic prevention and control measures underscores physical stores' essential role in China's omnichannel retail chain. Even brands that began life online are now aggressively expanding their brick-and-mortar store networks, with Shanghai Online Shopping Chamber of Commerce data showing that over 90% of the top 50 new consumer brands in the city added to their offline footprint this year. These include brands such as Maia Active, Neiwai, To Summer, and Babycare, all of which have recently opened new stores in high-quality shopping centres in Shanghai.

CBRE expects the coming years to see brick-and-mortar stores evolve into venues providing a comprehensive consumption, service, experience and social offering. While the growing maturity of omnichannel retailing will prompt retail brands to optimise synergies between online and offline resources; rising incomes will encourage consumers to demand higher quality shopping environments and services. This trend will be especially prominent in tier I and II cities, which are home to a high concentration middle- and high-income consumers.

Figure 8: Reasons for preferring in-store or online shopping (Mainland China)



Source: 2022 Mainland China Pacific Live-Work-Shop Survey, CBRE Research, December 2023

# Enriching and optimising offline store networks to achieve growth

Using a rapidly expanding international sportswear brand as an example, its number of stores in Shanghai stores increased from just five in 2019 to 21 as of September 2023.

Along with increasing its number of stores, the rationale behind this retailers' expansion lies in establishing a multi-tiered, multifunctional store network covering strategic locations. The group in question is also focusing on upgrading conventional stores in core business districts to flagship stores; adding community experience stores in regional shopping centres in submarkets; and opening outlets/airport stores targeting specific consumption scenarios.

CBRE believes that quality over quantity, experience-driven sales and community building will be important considerations for retail brands seeking to strengthen their physical store networks in future.

Figure 9: Expansion footprint of an international sportswear brand



Source: Open news, CBRE Research, December 2023

# Multifamily

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- China's population consider health and safety aspects of property management as more important since the onset of the pandemic.
- The development of institutionalised rental apartments is accelerating, with this asset class set to become a preferred option for China's 150 million renters who are seeking to improve their living quality.

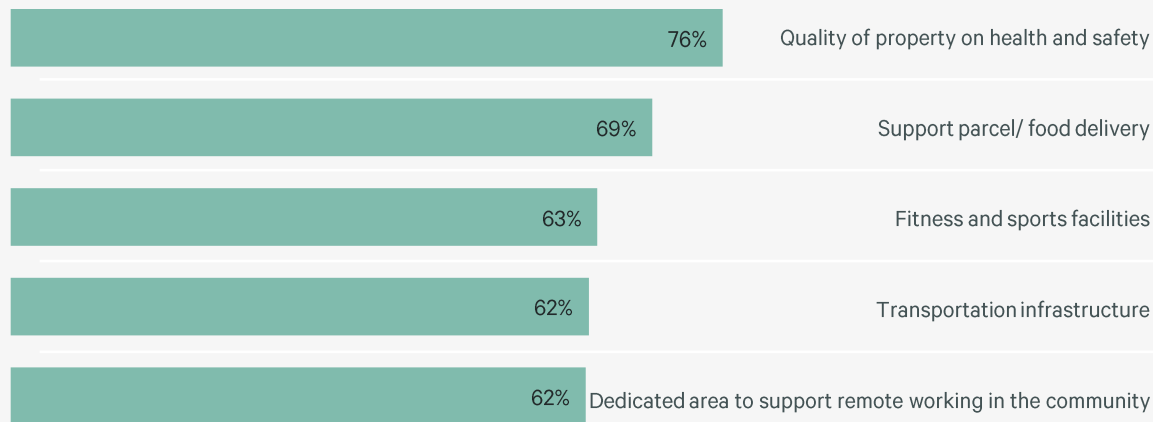


# High quality services and amenities underpin popularity of rental apartments

Consumption upgrading is also being reflected in demand for living conditions. CBRE’s 2022 Global Live-Work-Shop Survey found that 76% of China-based respondents consider health and safety aspects of property management to be more important since the pandemic’s onset. Supporting services including parcel and food delivery and fitness and sports facilities were also seen as key.

Driven by a combination of favourable land, financial, fiscal, and social security policies, as well as demographic trends such as urbanisation and smaller family sizes, China’s rental apartment market is expanding rapidly. Thanks to their ability to provide better living environments, more functional design, comprehensive community amenities and high quality management services, institutionalised rental apartments will become the preferred option for China’s 150 million renters.

Figure 10: More important home selection criteria since the pandemic’s onset



Source: 2022 Mainland China Pacific Live-Work-Shop Survey, CBRE Research, December 2023

Figure 11: Supporting facilities and services for institutionalised rental apartments



3

Building high-  
quality portfolios



# Building high-quality portfolios

## Economic transition supports emergence of new asset classes

**Life science parks:** One type of industrial real estate that is most aligned with China's focus on high-quality economic development. CBRE advises investors to focus on acquiring R&D properties in biomedical parks in Beijing and Shanghai.

**Multifamily:** Consumption upgrading and the low penetration rate of multifamily rental apartments will create opportunities to purchase, convert, upgrade or develop properties in core tier I and tier II cities in major city clusters such as the Yangtze River Delta Area, Pearl River Delta Area and Beijing-Tianjin-Hebei Region.

## Capture flight-to-quality demand

**Office:** With just 7% of new office supply in China's tier I cities in the next three years located in the prime CBD; core investors are poised to benefit.

**Logistics:** Although new stock is peaking, the supply-demand balance will improve in the next two years. Investors are advised to focus on greenfield development and projects providing stable cashflow in tier I cities and satellite cities such as Suzhou, Foshan and Dongguan.

**Retail:** The leasing market is now entering another upward cycle, and REITs' underlying asset types has expanded to include retail. Investors are recommended to focus on retail assets in core CBDs in tier I and tier II cities with sustained population inflows along with large-scale regional shopping centres. Institutional investors are advised to co-operate with leading retail property management companies with extensive operational capability.



# Life sciences parks

Owing to China's ageing population, consumption upgrading, and domestic industrial innovation, life sciences parks are among the formats of industrial real estate set to benefit most from the country's growing focus on high-quality economic development.

Despite the cyclical downturn in global and domestic biopharmaceutical investment since 2022, leading pharmaceutical companies continue to pursue the development of new drugs. In H1 2023, R&D expenditure of A-share listed pharmaceutical companies increased by 18% y-o-y, maintaining a Compound Annual Growth Rate (CAGR) of nearly 20% over the past five years<sup>2</sup>.

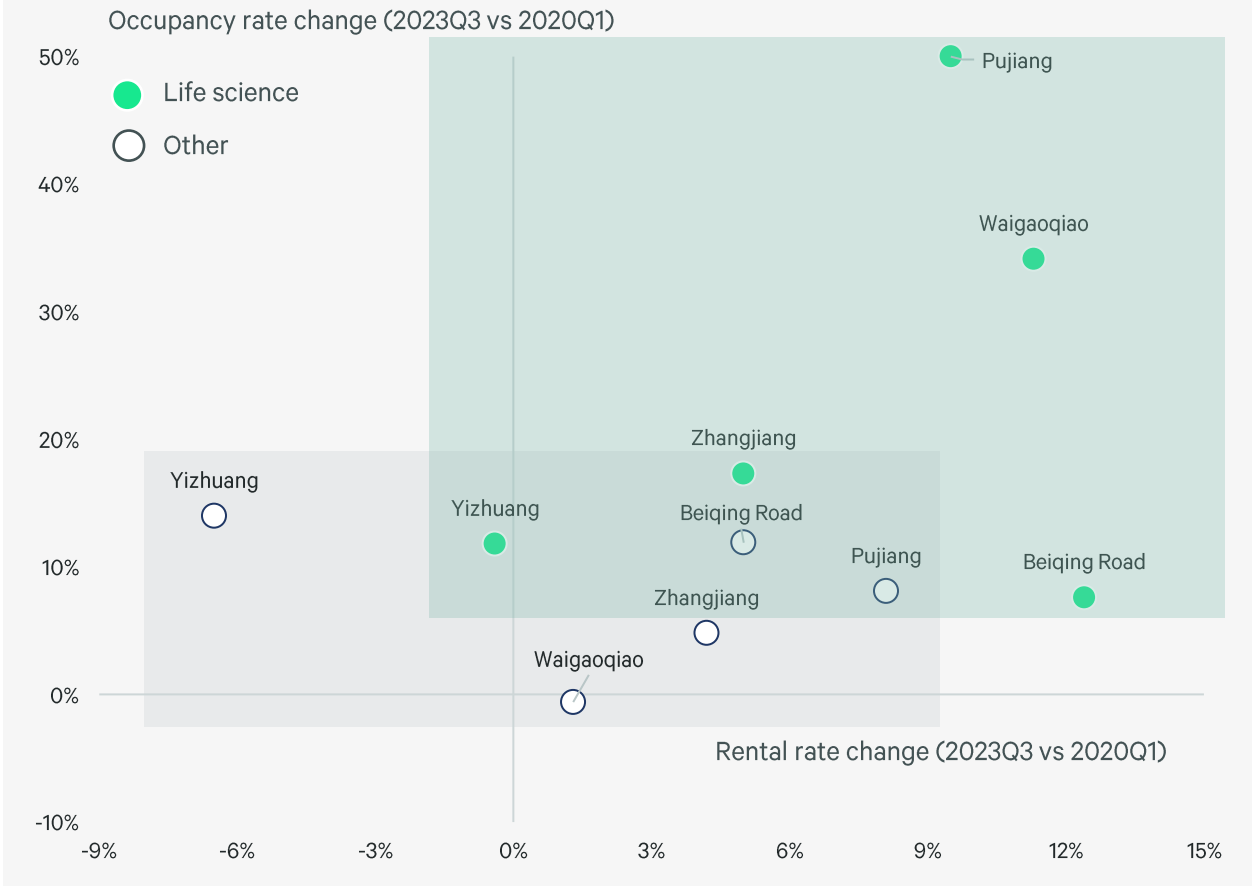
The continuous expansion of R&D spending has boosted demand for R&D property. CBRE's analysis of the performance of life science R&D facilities in Beijing and Shanghai with other R&D facilities since 2020 reveals that the former possess a clear advantage in terms of rental growth and occupancy. In addition to strong fundamentals, life sciences R&D facilities have a high threshold in terms of building standards; environmental assessment; industry regulations; and equipment investment, making their tenants more likely to commit to longer lease periods.

CBRE recommends investors with an interest in life sciences parks to focus on Shanghai and Beijing, which are home to the country's highest concentration of biopharmaceutical R&D industry chains and talent. In Shanghai, for example, around 278,000 people were employed in the biopharmaceutical industry in 20223. Government data show that the projected shortfall in talent will reach more than 400,000 by the end of the 14th Five-Year Plan. Assuming that 20% of this number are R&D staff and R&D area per capita is 30 sq. m., **demand for biopharmaceutical R&D facilities in Shanghai in the coming years will exceed 2.5 million sq. m., well below current known new supply of about 1.2 million sq. m.**

Note 2: Wind, CBRE Research, December 2023

Note 3: The White Paper on Talent Development of Shanghai Biomedical Industry, Shanghai Biomedical Industry Promotion Center, 2022

Figure 12: Change in rental rate and occupancy rate of business parks in Beijing and Shanghai since 2020: life science vs other



Source: CBRE Research, December 2023

# Multifamily

Looking beyond industrial innovation, better living conditions will be another key outcome of high-quality development. Investment in multifamily is already picking up, with total of 19 deals worth a combined RMB 11.0 billion completed in China's residential sector in the first three quarters of 2023, exceeding the past two years' combined total.

CBRE's 2022 Investing in China Multifamily Real Estate report forecasted that nationwide demand for residential rental apartments would reach 97 million units by 2030, a 56% increase from 2020. However, the country's penetration rate of multifamily rental apartments remains low, at under 3%, or 10% if affordable rental houses are included.

With around three-quarters of China's target multifamily users located in Guangdong, Shanghai, Beijing, Zhejiang and Jiangsu, investors are recommended to focus on these cities as well as nearby markets such as Suzhou, Nanjing, Hangzhou, Ningbo, Foshan and Dongguan.

## Urban renewal facilitates market entry for investors

CBRE data show that since 2015, a total of 35 transactions in the office, retail and hotel sectors involved a change of use. Of these properties, 22 were transformed or planned to be converted into rental housing apartments, with hotels and low-grade office buildings most involved.

CBRE's analysis of rental rates per sq. m. of Grade B office buildings and multifamily apartments in typical submarkets of Shanghai reveals that multifamily apartments command a premium in most districts, particularly outside the inner ring road. Opportunities to boost rental income through renovations along with local government policy support for urban renewal will continue to provide a solid foundation for investment in multifamily apartments.

Figure 13: Rental rates per sq. m.<sup>4</sup> of Grade B office/BP buildings and multifamily apartments in typical submarkets of Shanghai (2023Q3)



Note 4: Rental rate = effective rent \* occupancy rate. Rental rate of multifamily apartments is based on a single room.  
Source: Ke, Port Apartment, Mofang, CBRE Research, December 2023

# Office

While the abundant supply pipeline in China’s major cities will continue to challenge the supply-demand balance and weigh on rental growth in the next one to two years, rising long-term occupier demand for high quality office space and nuances in the supply-demand conditions of different locations will provide opportunities for institutional investors.

CBRE data show that in China’s four tier I cities, the vacancy rates in most core CBDs stood below 10% as of the end of Q3 2023. More importantly, **just 7% of new office supply due to be completed in tier I cities during 2024-2026 will be located in core CBDs. A recent CBRE found that employee satisfaction with transportation and amenities in core CBDs stood at 90%, well above the rates for decentralised locations.**

After several years’ price adjustments, along with the continuous decline of domestic policy rates, Grade A office assets in tier I cities have begun to enjoy positive carry. CBRE recommends that medium- to long-term institutional investors prioritise the acquisition of Super Grade A and Grade A office assets in core locations in tier I cities, particularly properties providing stable cash flow. With CBRE data showing that yield performance of office assets in China has displayed a low or negative correlation with more than 90% of the world’s major markets over the last decade, global investors will also be able to avail of diversification benefits.

Figure 14: Supply-demand conditions of different locations in tier I cities

	Vacancy rate	Share of supply during 2024-2026	Employee satisfaction with transportation and amenities
Core CBDs	12%	7%	90%
Other districts	24%	93%	74% <sup>5</sup>

Figure 15: China tier-1 cities Grade A office average NOI yield relative to borrowing cost



Note 5: Emerging districts.

Source: 2022 Mainland China Live-Work-Shop Report, CBRE Research, December 2023

# Logistics

Warehouse net absorption in China's major cities reached 5.3 million sq. m. in the first three quarters of 2023. This marked a significant increase of 45% y-o-y, equivalent to 150% of the average level of the same period in the three years prior to the onset of the pandemic.

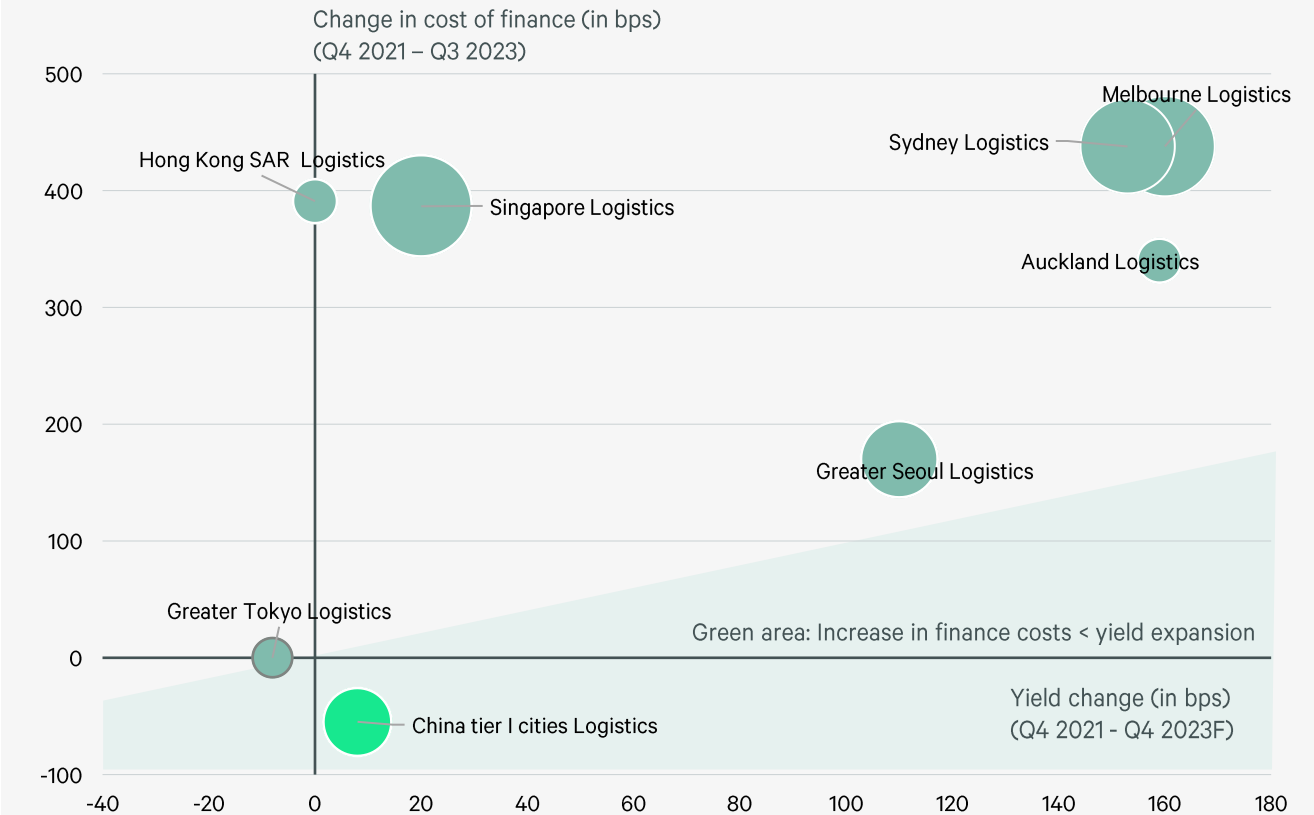
China's warehouse market is currently in the midst of a supply peak, with new supply expected to exceed 12 million sq. m. in 2023. However, new supply is projected to fall back to a more manageable level of around 6-6.5 million sq. m. per annum over the next two years. Considering the resilience of leasing demand, the supply-demand balance will gradually improve from H2 2024 to 2025. Tier I cities and surrounding satellite markets, which remain preferred locations for tenants seeking expansion, are expected to be among the first locations to witness stabilised rental growth.

In addition, continued interest rate cuts by the People's Bank of China (PBoC) means China is one of the few markets in Asia Pacific where financing costs have risen at a lower rate than cap rate expansion. In the short term, however, asset price and rental volatility will remain a challenge for investors. CBRE recommends that buyers focus on through-the-cycle opportunities such as greenfield development and core assets in tier I clusters.

In the long term, China will continue witness a structural scarcity of modern warehouse facilities. CBRE data show that while the volume of full-grade warehouse facilities in China and the U.S. stands at around 1.2 billion sq. m. apiece, **the scale of high-quality warehouses in China is only about 120 million sq. m., less than one-third of that in the U.S.** In contrast, China's demand fundamentals are much stronger, with both markets having a similar sized e-commerce market but China's freight turnover being 3.5x that of the U.S.<sup>6</sup>. Thanks to China's huge consumer market and manufacturing supply chain upgrades, demand for high-standard warehouses has significant growth potential.

Note 6: Sizes of e-commerce market in China and the U.S. are based on 2022 data from Euromonitor. Freight turnovers in China and the U.S. are based on 2021 data from the two governments (excluding pipeline transport).

Figure 16: Change in cost of finance and sector yields, and rental forecast<sup>7</sup>



Note 7: Size of the bubble refers to the forecast rental growth in 2024. Negative rental growth in Greater Tokyo logistics.

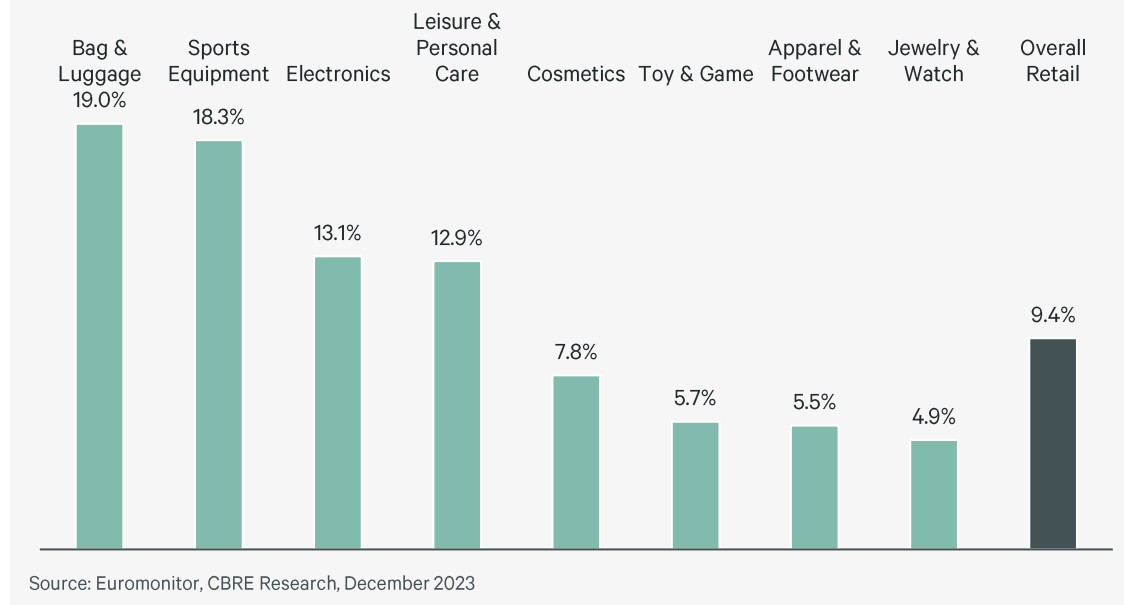
Source: CBRE Research, December 2023

# Retail

With face-to-face consumption staging a strong recovery since the relaxation of anti-pandemic controls, retailers in China are poised to accelerate the expansion of physical store networks. Euromonitor forecasts that the overall cumulative change in brick-and-mortar space in China will reach 9.4% over 2023-2027, with quality-living related retailers such as bags and luggage, sports equipment, leisure and personal care exhibiting especially strong growth.

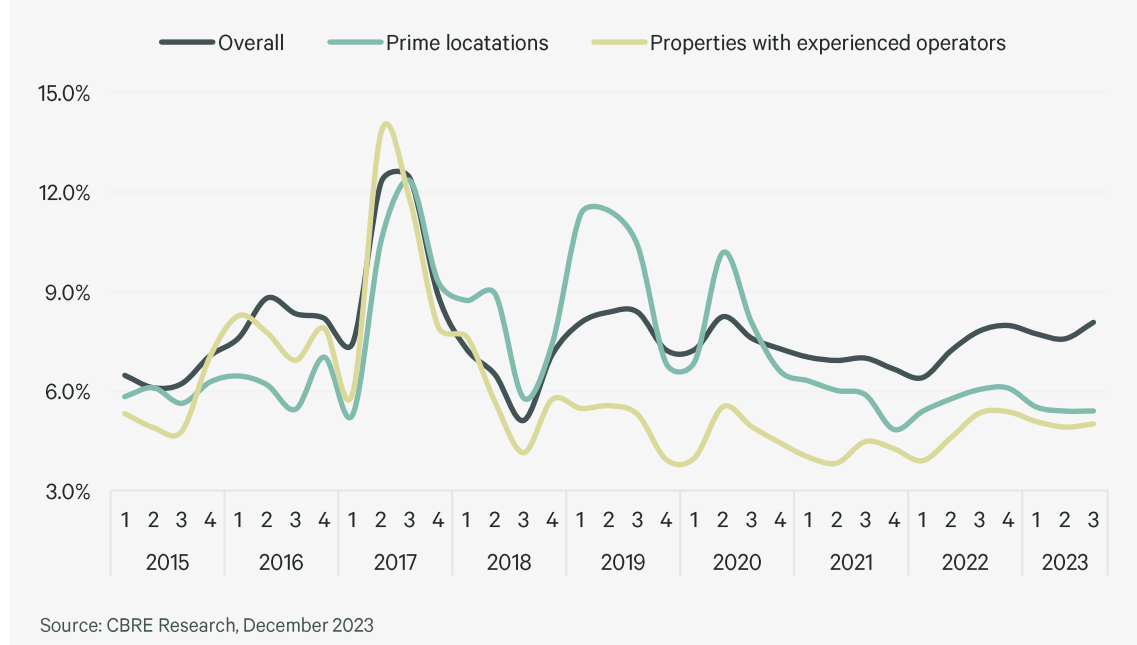
Although the retail sector will offer a range of cyclical investment opportunities, not all properties will benefit from the market recovery. Operational capability will be an important determinant of success. CBRE's analysis of the Shanghai retail market shows that shopping mall management has a more significant impact on occupancy than location; a trend that has become even more prominent since the onset of the pandemic.

**Figure 17: Forecast on cumulative change of total brick-and-mortar space taken by various retail categories in China (2023-2027)**



CBRE recommends that investors focus on retail investment opportunities in tier I and tier II cities with sustained population inflows. Given the scarcity of leasable space in core CBDs and retailers' strong intentions to expand, retail properties in core CBDs are expected to outperform the broader market. For institutional investors with limited operational experience or capacity, partnering with leading retail operators or locking in future cash flow returns through reasonable pricing at the bottom of the cycle through transaction structure arrangements will be among the most viable strategies.

**Figure 18: Vacancy rate of prime retail properties in Shanghai**



# Formation of retail REITs set to boost investment activity

In March 2023, China's public REIT regime expanded underlying asset types to include retail properties such as shopping centres, department stores, and farmer's markets. As of December 2023, four retail REIT had either been formally approved or were going through the approval process.

Based on the details of the four new retail REITs, they are likely to target shopping centres in tier II cities along with properties with short land tenure. Investors are recommended to closely monitor related PRE-REIT investment opportunities.

Figure 19: Major indicators of China's first batch of retail REITs

REIT	China Resources	Jinmao	SCPG	Wumart
<b>Underlying Assets</b>	Qingdao Mixc mall	Changsha Mall of Splendors	Hangzhou Xixi InCity mall	4 Wumart stores in Beijing
<b>Location</b>	Tier II	Tier II	Tier II	Tier I
<b>Asset Type</b>	Shopping mall	Shopping mall	Shopping mall	Neighbourhood centre
<b>GFA (thousand sq.m.)</b>	301	103	144	78
<b>Remaining land tenure (year)</b>	28	29	25	19-21
<b>Occupancy Rate<sup>8</sup></b>	98.5%	98.4%	98.1%	88.7%
<b>Rental Rate (RMB/sq. m./month)<sup>9</sup></b>	295.5	194.8	190.5	77.3
<b>Discount Rate<sup>10</sup></b>	7.00%	7.25%	7.00%	6.50%
<b>2024 Estimated Dividend Yield</b>	4.90%	4.83%	4.85%	6.40%

Note 8: Occupancy rates of China Resources REIT and SCPG REIT refer to average occupancy rates of 2023H1. Occupancy rates of Jinmao REIT and Wumart REIT refer to occupancy rates as of June 30th, 2023.

Note 9: Rental rates refer to average rental rates of 2023H1.

Note 10: Discount rates are as of June 30th, 2023.

Source: Prospectus, CBRE Research, December 2023

# Conclusion

The coming years will see China's economy undergo a transition from a rapid growth phase driven by exports, investment and a demographic dividend towards a period of slower but higher quality growth characterised by sustainable development, economic restructuring and industrial upgrading, as well as improvements to quality of life. CBRE expects China's economy to maintain a medium to high growth rate of 4.4% per annum in the period from 2023 to 2027.

CBRE expects the trends identified in this report to spur new commercial real estate leasing demand, with an emphasis on quantity, quality, efficiency and sustainability. Investment is also set to benefit, with life sciences parks, rental apartments and high-quality office, retail and logistics set to become more sought after than ever before.



# Contacts

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## China Research

### Sam Xie

Head of Research, China  
sam.xie@cbre.com

### Molly Hu

Associate Director, China Research  
molly.hu@cbre.com

### Joey Wu

Senior Analyst, China Research  
joey.wu@cbre.com

### Shirley Hu

Senior Director, China Research  
shirley.hu@cbre.com

### Tracy Chen

Senior Manager, China Research  
tracy.chen@cbre.com

### Ezra Liu

Analyst, China Research  
ezra.liu@cbre.com

## Global Research

### Richard Barkham, Ph.D., MRICS

Global Head of Research,  
richard.barkham@cbre.com

### Neil Blake, Ph.D.

Global Head of Forecasting and Analytics,  
EMEA Chief Economist  
neil.blake@cbre.com

### Henry Chin, Ph.D.

Global Head of Investor Thought Leadership,  
Head of Research, APAC  
henry.chin@cbre.com.hk

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