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Emerging City Winners

Profiles: China

Dalian

- *Home to one of China's largest seaports, Dalian serves as the gateway to North East China.*
- *A leading city in the government's programme to revitalise the old industrial base of North East China*
- *Strong linkages with Japan and Korea, and a high concentration of investment from both countries*
- *Important software hub, and the first city in China authorised as a business process outsourcing (BPO) base*
- *An emerging financial hub—home to one of China's three futures exchanges*
- *Business park sector offers dynamic prospects. Strong demand also exists in high-end residential*



CITY SUMMARY

- Dalian is home to China's seventh largest port and serves as a gateway city to North East China.
- A leading city in the government's programme to revitalise the old industrial base of North East China
- Well established linkages with Japan and Korea, and a high concentration of investment from those countries.
- Important software hub, and the first city authorised as a business process outsourcing (BPO) base in China
- Dynamic shipbuilding sector – expected to be world's largest shipbuilding centre by 2020
- An emerging financial hub and home to one of China's three futures exchanges
- Highly successful business park segment
- China's 'soccer city'

ECONOMIC DASHBOARD

Size	Population (million 2006)	5.7
	GDP (USD billion 2006)	32
	Employment (million 2006)	0.89
Growth	Population (% pa 2001–2006)	0.6
	GDP (% pa 2001–2006)	15.8
Infrastructure	Air Passengers ('000 2006)	6,351
	Freight Traffic (million tonnes 2006)	201
Openness	FDI (USD billion 2006)	2.2
	Exports (USD billion 2006)	17
Wealth	GDP/Capita (USD 2006)	5,342
	Disposable Income /Capita (USD 2006)	1,675
Education and Labour	Higher Education Institutions (2006)	21
	Total Enrolments ('000s 2006)	201
	Unemployment (% 2006)	2.9
	Average Wage Rates (USD 2006)	1,923
Business	Business Environment (Score)	B
Lifestyle	Quality of Life (Rank)	5*

ECONOMIC BACKGROUND

Shipbuilding and IT are Dalian's two fastest growing industries. Their growth reflects the government's twin ambitions to establish Dalian as North East Asia's main shipping hub, and transform the city into the "Bangalore of China".

An important shipping hub in North East Asia

The city's recent economic development has been largely underpinned by its port activities. Dalian is the largest seaport in North East China and the city's shipbuilding output accounts for 25% of China's total. More than 28,000 people are employed in the sector - its ships are now exported to over 40 countries. This booming industry has created a solid industrial base, enabling Dalian to take a leading role in the government's programme to revitalise North East China¹.

Two shipbuilding giants dominate the industry: Dalian Shipbuilding Industry Co. Ltd. (DSIC) and China Ocean Shipping Company (COSCO). DSIC is the market leader, with an output of 2.6 million tonnes in 2007, representing 20% of China's total shipping output, whilst COSCO, China's second largest shipbuilder, has announced plans to build the group's first ship building facility in Dalian in 2008.

The entry of world-class shipbuilding companies has also been central to the success of the industry in Dalian. STX (the sixth

¹ North East China refers to three provinces: Jilin, Liaoning and Heilongjiang Province..



largest shipbuilder in the world) initially invested USD 410 million in Dalian's Changxing Island port complex in Sept. 2006, followed by a second phase investment of USD 490 million in December. 2006. Japan's Kawasaki Heavy Industries Group (KHI) also teamed up with Dalian COSCO to build a shipbuilding facility in Dalian.

The entry of industry giants has triggered an increasing number of parts suppliers to expand into Dalian to capitalise on the city's strategic location and solid industrial base. There are now 15 shipbuilding firms in Dalian, together with 32 ship-maintenance firms and three maritime industry-focused universities. The clustering of firms throughout the shipbuilding supply chain has effectively boosted Dalian's shipbuilding capability and reduced shipbuilding costs.

The competitive edge of the shipbuilding industry is expected to strengthen further, with annual capacity anticipated to reach 10 million tonnes by 2020, which would make it the world's largest shipbuilding base.

The "Bangalore of China"



Dalian started to develop its software sector in the early 1990s as part of the central government's plan to revitalise the industrial base of North East China by moving up the value chain. To seize this opportunity, the software

sector has been designated to capitalise on Dalian's inherent advantages, notably an abundance of high quality human resources, a language edge, competitive operation costs and a pleasant living environment. With the help of powerful government support, the software sector in Dalian has witnessed dramatic growth from a turnover in 1998 of only USD 24 million to USD 1.24 billion in 2005, representing a 500-fold increase in less than ten years. Export volume rose from almost nothing in 1998 to USD 300 million in 2005 and is projected to reach USD 1.5 billion within the next three years.

The dynamic growth of the software sector is exemplified by the performance of Dalian Software Park, which was set up by a joint venture between the municipal government and Dalian Yida Group. Dalian Software Park has turned out to be one of the most successful software parks in China; indeed, it is China's largest software export base and has the highest level of foreign investment of any software park. Its turnover growth rate reached 68% in 2006, and there are now more than 300

firms operating in the park, of which 70 are Japanese companies.

Dalian Commodity Exchange Centre – China's Largest Futures Exchange

Dalian hosts the largest commodities futures exchange in the country, and is one of only three futures exchanges in China². Dalian has the world's second largest bean futures exchange (after CBOT in Chicago) and the world's largest non-transgenic bean futures exchange.

To tap into its strong market position, the Dalian municipal government aims to develop Dalian's commodity exchange into one of global significance within the next 15 years. In an effort to facilitate this, the futures market is being positioned as the core financial activity in the city. ABN AMRO has become the first foreign bank in the Chinese futures market by investing in a local futures brokerage.

The significant growth of the futures market in Dalian is expected to lead to further upgrading of the local shipping industry by driving the development of services covering the banking, insurance, transport and electronics sectors. Beneficial linkages between the futures market and the shipping industry will further consolidate Dalian's position as an important North East Asian shipping hub and one of the top financial cities in North East China.

The Financial Hub of North East China

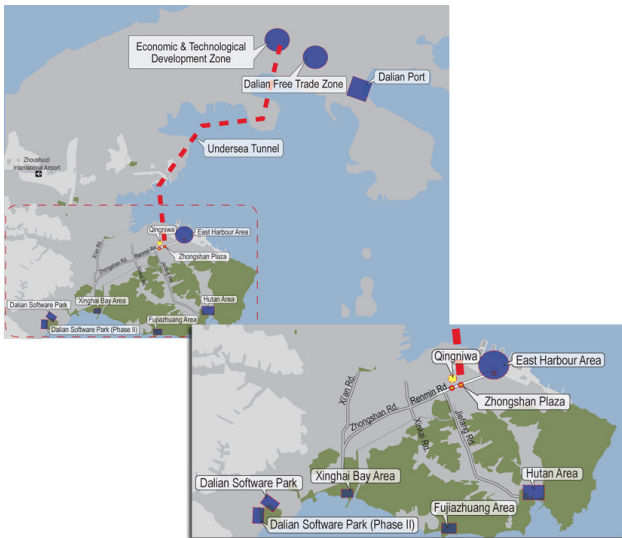
As the financial hub of North East China, Dalian boasts the most open and internationalised financial environment in the region. Two foreign insurance firms and eight foreign banks have set up branches in Dalian including Bank of East Asia, HSBC and Standard Chartered Bank. Three foreign banks have been approved to start renminbi business in the city. Citibank for example, has opened a branch in Dalian Jan 2008.

Additionally, the establishment of Dalian Bank, with its aim of providing easier access to financing for local firms, will further consolidate Dalian's role as the leading financial centre in North East China.

² The other two futures exchanges are in Shanghai and Zhengzhou



URBAN FORM AND INFRASTRUCTURE



Source: Jones Lang LaSalle Research

Dalian is located in the middle of the Liaodong Peninsula, which juts out into Bohai Bay. Most of the city's business activity is clustered in a small region covering five urban districts - Zhongshan, Shahekou, Xigang, Ganjingshi and Lvshun - with a land area of 1,100 sq km and a population of 1.2 million residents.

The urban districts of Dalian were originally designed by the Russians, who sought to replicate Parisian urban design, which is built around circular plazas with radial roads. There are more than 100 plazas remaining in the city, with one of the most central and historical being Zhongshan Square.

Xinghai Square, located south of the city, is a modern rendition of this traditional urban design complex and was redeveloped in 1996. As the biggest city plaza in Asia, the square covers a land area of 1.76 million sq m and is being developed into a luxury residential area.

Renmin Road and Zhongshan Square constitute the city's core CBD, accommodating high end business and financial activities. Meanwhile, retail facilities are clustered in Qingniwa Bridge and Xian Road.

Limited space in the traditional CBD has constrained the city's evolution. In order to accommodate the CBD growth, the East Port area, immediately next to Renmin Road, is planned as a CBD extension. The East Port area formerly played a pivotal role in the city's economy, but the area went into decline as port facilities were established elsewhere in the city region. The Dalian municipal government is now regenerating this

distressed area into a new business district specifically servicing shipping businesses, and leveraging its strategic location adjacent to the CBD. The planned area will cover 40 sq km and will be home to high quality office and hotel developments. The East Port area is expected to be fully developed in 20 years and it is rumoured that Wharf is planning to develop a five-star hotel in this emerging commercial district.

Infrastructure: Greater Dalian Plan

In 2005, the government announced its plans to build a 6-km undersea tunnel connecting downtown Dalian with the city's development zone. The project is expected to be completed by 2010 with a total investment of USD 0.5 billion. Improving access to the city's development zone is expected to significantly boost the residential market in that area as it will become a realistic location for residents who need to commute into Dalian's CBD.

BUSINESS ENVIRONMENT

Aiming to develop Dalian into one of China's major IT hubs, the Dalian municipal government has endeavoured to improve the business environment specifically for the IT sector. It has focused on IPR (Intellectual Property Rights), which has been identified as the key concern of the IT sector.

In 1998, the Dalian municipal government teamed up with Microsoft to develop initiatives to protect original software. The government provided financial support to organise corporations in the city going for CMM valuation (Capability Maturity Model for Software). This model has since been replicated widely by other Chinese cities, and in 2005, the central government designated Dalian as a role model for protecting original software.

Also, to maintain the high quality of human resources, the government has offered generous financial incentives to IT experts in the city. A USD 1.3 million professional foundation has been set up by the government to attract IT talent into Dalian.

The continuous efforts to facilitate the growth of the IT sector positioned Dalian to be the first Chinese city designated by the Chinese government as an authorised BPO base (in 2006), subsequently followed by Shanghai, Shenzhen, Chengdu and Xi'an.



CORPORATE ACTIVITY

Logistics Players

As one of the largest seaports in North China, Dalian has long been home to various logistics and shipping companies. This includes Maersk, Itochu and KWE, all of which have been in the market for several years and are currently undergoing expansions in the city.

Logistics developers such as Prologis have moved into the city in order to secure their positions in an increasingly dynamic logistics market. ProLogis bought 120,000 sq m of existing facilities in the Bonded Port Area, the only bonded port in North East China. The main tenants are from Japan, Europe and the US, and include Canon, Sanyo, YKK, Santa Fe, Fuji Logistics and IDU.

IT gaining importance in the city

Corporate activity is most active and intensive in the IT sector, supporting Dalian's aim to be the "Bangalore of China".

More than 2,000 Japanese firms have expanded their technical support centres to Dalian - including Panasonic, Sony, Hitech and Toshiba. Total investment from Japan has reached USD 4.2 billion, which is roughly 10% of total Japanese investment in China.

HP, IBM, Accenture, SAP and GE are all present in Dalian Software Park. Five of the top ten global ITO (Information Technology Operations) and BPO service providers now have a presence in Dalian. The active presence of international players has effectively integrated Dalian into the global IT supply chain.

Oracle recently established a Global Support Centre in the city (one of 18 around the world). It will provide technical support to clients in mainland China, Taiwan and Korea.

Intel, the world's largest semiconductor manufacturer, is investing USD 2.5 billion in a production facility in Dalian, which will be the company's first wafer-fabrication plant in Asia and is expected to employ 1,500 people. Intel's investment represents one of China's largest single foreign-financed projects and is expected to greatly enhance the IT supply chain in the city.

To further boost the IT hardware sector, Dalian is now aggressively pursuing ASUS, TSMC and FOXCONN to invest in the city.

Growth of local IT companies

The growth and internationalisation of Dalian's indigenous IT companies is seen as critical to the city's sustainable

development as a leading-edge IT hub. Some local IT service giants have developed their market position through internationalisation - more than 150 local IT service firms have direct business links with Korea, Europe and the US, and ten have set up branches abroad.

Dalian Hi-Think Computer Technology Co. (DHC) and HiSoft Corporation, the local pioneers in the market, have received strategic investment from Intel and Microsoft. An example of a local IT success story, DHC won the Uzbekistan railway financing system programming project despite strong international competition from global leaders such as SAP.

LABOUR AND EDUCATION

Critical mass of IT specialists

	Tianjin	Beijing	Hangzhou	Wuhan	Chengdu	Dalian	Xian
Total Population(million people)	10.8	15	7	8	11	5.7	7.4
IT Professionals (people)	21,800	175,451	17,738	21,700	60,000	40,000	42,000
Percentage	0.20%	1.14%	0.27%	0.27%	0.55%	0.70%	0.57%

Source: Statistic Yearbook 2007

Dalian is home to a high number of IT professionals, totalling approximately 40,000 people (in 2005), which represents 0.7% of the total population - a proportion well above other tier II city IT bases in China. A total of 21 universities in Dalian graduate 65,000 students each year, and, typically, approximately 6,000 students major in IT-related studies. The IT sector in Dalian is attractive for new graduates due to its abundant opportunities and highly competitive salaries - often exceeding salaries in the financial sector.

Dalian's booming software industry is expected to generate demand for approximately 80,000 to 100,000 new IT specialists annually. As the local labour pool can no longer satisfy such demand from the IT sector, Mayor Xia Deren has organised a recruitment drive in other main cities in China, as well as abroad, to attract IT professionals and to ease labour supply shortages.

Fluent Japanese speakers

The city's strategic location (within one-hour flying distance from Japan), its frequent economic co-operation with Japan and its strong historical linkages have all contributed to the creation of a sizeable community of 100,000 fluent Japanese speakers. The city's language skills have contributed to the success of its BPO activities. HP, Fidelity International and IBM have all set up call centres and data-processing centres in Dalian to capitalise on the diverse language skills.

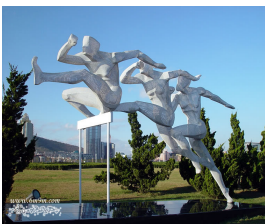


QUALITY OF LIFE

Dalian is renowned as one of China's most environmentally friendly cities. The ratio of green space reached 43% in 2006, significantly higher than the national urban average of 32.5%. These quality surroundings have helped to position Dalian as one of the most liveable cities in China. The Dalian municipal government recognizes this important differentiator and continues to drive efforts to further improve the city's environment. As a result, Dalian has gained recognition from the Chinese central government as the 'National Sanitary City' and the 'National Garden City'.

In addition, various large-scale international events including the annual Dalian International Fashion Festival, Acacia Flowers Festival, Spring Festival of Fireworks and Dalian Import and Export Commodities Fairs attract businessmen, artists and fashion designers from all over the world.

In sport, Dalian is an important "soccer city" with a dedicated fan base and one of the top teams in the Chinese domestic soccer league.



The attractive living environment, various international-level events, and special culture and historic connections with Japan and Russia act as incentives to retaining local talent and serve to make Dalian one of China's most

popular travel destinations.



REAL ESTATE DASHBOARD

Market Size/Stock	
Offices Grade A (000s sq m, 2Q07)	189
Retail (000s sq m, 2007)	2,206
Five-Star Hotels (2007)	6
Market Activity	
Office Construction Grade A (000s sq m, by 2009)	na
Office Vacancy Grade A (% , 3Q07)	24.7
Benchmark Values	
Grade A Office – Rents (USD psm pa)	285
Retail – Rents* (USD psm pa)	640-960
Industrial – Rents (USD psm pa)	34-54
Hotels – Room Rates (Five-Star, USD)	78.8
Residential Sales Prices (USD psm)	1,067
Grade A Offices – Indicative Yields (%)	9.5

Source: Jones Lang LaSalle Research

REAL ESTATE TRENDS

Of Dalian's main real estate sectors, the business park sector offers the best investment opportunities in the short to medium term thanks to the well-established market and continuing strong occupier demand.

The residential sector is amongst the most advanced due to solid demand generated from local residents upgrading and additional requirements of new migrants into the city. The active participation of large Chinese developers such as Vanke, China Overseas and China Resources has contributed to improving market transparency and increasing building quality. We foresee sales prices will see steady growth in the medium term.

The office market is in an earlier stage of development and is dominated by local developers. A two tier market has emerged, with significant rental differentials emerging between locally developed offices and international grade offices (of which there is very limited supply). Going forward, international grade offices are expected to record strong absorption, supporting rising rents. Rents on Grade B offices are likely to maintain their current levels, with vacancy rates gradually declining.

The retail market is facing the challenge of oversupply due to high levels of construction in 2003, when the municipal government began to regenerate downtown Dalian. 1.55 million sq m of retail space was added to the market between 2003 and

2005. The government has since responded by significantly decreasing the amount of land available for retail development. Therefore, there is only a small number of upcoming retail projects. However, there is substantial pent-up demand for wholly-owned and professionally managed developments.

INVESTMENT TRENDS

In the investment market, the most notable deal is Xiwang Tower, which was originally developed by Hyundai Motor Company ten years ago but was suspended in 1997 due to the financial crisis. Only in 2007 did three groups - Yida, JP Morgan Chase and Shui On Group - team up to acquire the distressed building and successfully regenerate it into a Grade A office building. Both STX Group and the China Securities Regulatory Commission secured more than 1,000 sq m of space in this building in Q1 07, when Xiwang Tower was first available for leasing.

In the retail sector, Itokin department store was closed due to bad performance and was finally taken over by Lifestyle Holdings, a Hong Kong developer. Intime was forced out of the market and was purchased by Dashang Group, while C-mall was closed due to poor performance.

INDUSTRIAL/BUSINESS PARK

There are three state-level industrial zones in Dalian: Dalian Free Trade Zone, Dalian Economic & Technological Development Zone and Dalian High-Tech Industrial Zone.

Dalian Free Trade Zone (FTZ): Founded in May 1992, Dalian Free Trade Zone is the only FTZ in North East China. In 2004, Dalian FTZ expanded to 64 sq km from 1.9 sq km. Positioned close to Dalian port, Dalian FTZ is the location of the majority of high-quality logistics facilities in the city, with target clients including foreign trade, manufacturing and shipping companies.

Most existing and future warehousing stock is situated in three major areas: the Auto Logistics Park, the old Free Trade Zone and the Bonded Logistics Park. Prologis has completed circa 48,000 sq m of international-standard warehouses in the FTZ, with rentals of around RMB 1 per sq m per day³. Another 73,000 sq m of warehouses are due for completion within the next two years.

³ Rents in industrial parks are quoted as RMB



In August 2006, Dayao Bay Bonded Port (within the Dalian FTZ) was approved by the State Council and is now the third bonded port in China after Shanghai and Tianjin. The total planning area is 6.9 sq km, with phase I covering 2.8 sq km. The bonded port enables both bonded logistics and export processing activity.

Dalian Economic & Technological Development Zone: As one of China's first state-level economic and technological zones, Dalian Development Zone was founded in 1984 with a planned area of 330 sq km. Its pillar industries are electrical and telecommunications, food processing, garment and textiles and mechanical equipment as well as pharmaceutical production. Presently, there are over 2,000 foreign manufacturing and logistics enterprises in the zone, mainly from Japan, the US and Europe, which include Canon, Konica, Mitsubishi, West Pacific Petrochemical and YKK. Rentals for high-quality warehouses range from RMB 0.7 to RMB 1.1 per sq m per day, while asking rents on manufacturing facilities are RMB 0.9 per sq m per day. Land prices in the zone are approximately USD 34 per sq m.

Dalian High-tech Industrial Zone (DHTIZ): DHTIZ was authorised by the State Council in 1991, with a site area of 35.6 sq km. It has successfully attracted around 2,300 companies, over 30% of which are foreign. Currently, DHTIZ mainly consists of two parts—Dalian High-tech Industry Belt (DHTIB), including Dalian Software Park to the south west of the downtown area and Dalian Digital and DNA Port (DD Port) to the north east of the downtown area.

Dalian Software Park (DLSP): Founded in 1998 by Yida Group, a local developer, DLSP covers a planned area of 11.6 sq km. It is the largest professional software park in China and is one of the country's 11 software industry bases. The properties in the park are a mix of small buildings and mid-rise towers. A total of 15 buildings are for lease only, including several built-to-suit premises, with nearly full occupancy and an average rental level of about USD 6.6 per sq m per month. Currently, 375 companies have invested in DLSP, including 30 "Fortune 500" firms, among which 42% are foreign firms. Renowned tenants include Accenture, Ericsson, Microsoft, Oracle and Intel. Singapore developer Ascendas has been heavily involved in DLSP and is a key investor in Dalian Software Park Phase II.

RESIDENTIAL

The high end residential market in Dalian has expanded from the traditional downtown and Hutun areas into four designated areas, which include Xinghai Bay and Fujiazuang.



Due to the efforts of former Mayor Bo Xilai (China's current Minister of Commerce), the Xinghai Bay area has successfully emerged as Dalian's premium residential location. The average sales price in Xinghai Bay reached over USD 1,467 per sq m in

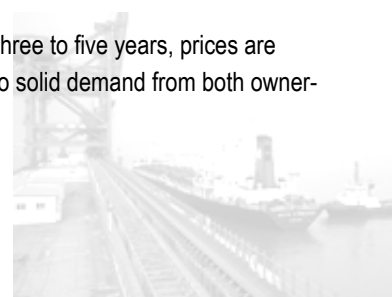
2007, significantly above the average price in the downtown area of USD 1,067 per sq m. 90% of prime residential projects in the city are located in the Xinghai Bay area, with most projects being large, high-rise developments. Xinghai National Treasure, for example, one of the most prestigious projects in the city, has recorded sales prices in the secondary market of over USD 2,667 per sq m, while rents range from USD 2,000 to USD 2,667 per month per unit. The high rental yield of 9% attracted not only owner-occupiers from local residents and other parts of Liaoning Province, but also some national celebrities to invest in this project.

The Hutun area benefits from excellent sea views, mature amenities and close proximity to downtown Dalian. It continues to play a key role in Dalian's high-end residential market, and average sales prices are second only to Xinghai Bay.

In the mass market, limited land supply and surging residential prices in downtown Dalian have pushed local residents to move to the northern and western parts of the city, two areas that have witnessed significant infrastructure improvements since 2001.

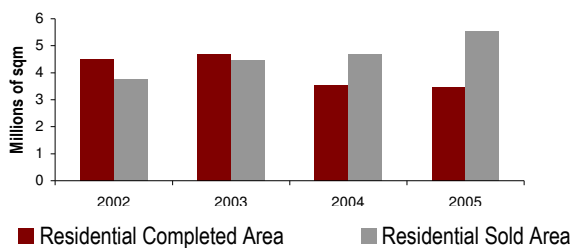
Demand for residential property took off in 2003 – a result of government-led urban regeneration programs as well as a widespread desire on the part of local residents to upgrade their living conditions. Since 2004, the amount of residential space sold in the city has exceeded space completed, which has driven sales prices upwards. The supply shortages combined with strong demand have attracted large domestic developers (such as Vanke) who are keen to capitalize on these potentially lucrative market conditions. The active involvement of these players has helped to create more market transparency and improve building quality.

We foresee that over the next three to five years, prices are likely to increase steadily due to solid demand from both owner-



occupiers and investors. More new projects will be seen in the northern and western parts of the city where land has been released in recent years. The entry of developers such as Wharf, New World Properties and Ascott will further push the upgrading of Dalian's residential market.

Housing Supply and Demand



Source: Dalian Statistics Yearbook

OFFICES



Office space in downtown Dalian clusters in three areas - Renmin, Zhongshan and Xinkai Roads. The market in Renmin Road is led by top quality buildings such as the Asia Pacific Finance Centre and Pingan Building; Zhongshan Road is home to

the only two Grade A office buildings in the city - Senmao Building and Xiwang Tower - whilst Xinkai Road hosts the Pearl River International Building. Occupiers in high quality office buildings in Dalian are mostly from the shipping and trading sectors. Average occupancy is between 300–500 sq m.

A two tier office market has emerged with the highest rents and lowest vacancy rates achieved in Grade A office buildings. Top rents of USD 285 per sq m pa (excluding management fees) are achieved on Grade A offices in Zhongshan Road. Vacancies in the Senmao Building, for example, are only 5%, and current MNC tenants are interested in expanding in this building, even though the building was completed almost ten years ago. One reason for Senmao's success has been the quality of its property management – an important detail that some local developers overlook.

Rents for Grade B level buildings are significantly lower and vacancy rates are in the region of 20%. In Renmin Road, where most of the grade B level buildings are located, rents reach up to USD 146 per sq m pa. In Xinkai Road, where most of the older high quality buildings were constructed, rents are USD 109.5 per sq m pa reflecting the older stock.

Dalian has witnessed office market decentralisation in recent years due to the limited high quality space in downtown Dalian and the increasingly important position of Dalian High-Tech Industrial Zone (DHTIZ), which hosts the majority of Dalian's new office supply.

The limited high-quality space in downtown Dalian has pushed some software development tenants to relocate to DHTIZ, where office buildings are developed to cater specifically for software companies and have better property management. Rents can reach USD 91 per sq m pa in DHTIZ, similar to the levels in buildings on Xinkai Road.

The city is now aggressively developing as a major 'shipping centre' and financial centre in North East China, and a key national BPO centre. As a result, we expect future office demand will be boosted as more shipping, software firms and financial institutions move into the city.

Nonetheless, we estimate that it will take several years for newly created demand to absorb the current vacant space. Rents for Grade B office space are expected to remain stable, with vacancy rates gradually declining over the next two years. Rents for Grade-A offices will see steady growth due to the limited supply and expanding demand.

HOTELS

Dalian's hotel market is underpinned by increasing corporate demand, the booming MICE (meetings, incentives, conventions and exhibitions) business and Dalian's position as a popular leisure destination.

Benefiting from the policy to revitalise North East China, Dalian has emerged as a logistics and finance hub in North East China. This in turn has made the city one of the most attractive places in mainland China for MNC expansion. According to our survey in 2006, Dalian is one of the preferred locations for expansion, together with Chongqing, Chengdu and Tier I cities.

MICE business has always been the most important demand driver for Dalian's hotel market. In 2006, Dalian hosted 119 conferences and exhibitions that drew more than 4.7 million visitors to the city. Hosting the 'World Economic Forum on Growth' in September 2007 further consolidated the city's position as a conference hub. Business visitors account for the main component of demand for five-star hotels.

Dalian is a key leisure destination and was awarded 'China's best tourist city' by the National Tourism Administration and the



World Tourism Organization (UNWTO) in 2006, together with Hangzhou and Chengdu. The UNWTO, recognizing how proactively the municipal government is promoting the city internationally, feels that Dalian is well on its way to becoming a key destination for tourism.

International and domestic arrivals are increasing sharply. In 2006, Dalian's international arrivals totalled 700,000, up 16.7% on 2005. Japan remains the largest source market due to investment inflows and a series of tourism promotions aimed at improving Sino-Japanese relations. A total of 344,000 Japanese tourists visited Dalian in 2006, accounting for half of all foreign arrivals. Domestic arrivals in 2006 recorded a 25% increase over 2005.

This strong momentum has been reflected in the strong performance of the hotel sector. There were 159 star-rated hotels by end-2006, of which six are five-star. The average daily rates of the five-star segment reached USD 78.8, up 3% from 2005, and the occupancy rate reached 64.4%.

According to the plan released by the Dalian Tourism Bureau, Dalian will have 205 star-rated hotels by 2010. Also, we estimate that 1,254 new rooms will be added to the four- to five-star hotel market by 2009.

Source: Jones Lang LaSalle Hotels

RETAIL

The retail market in Dalian is smaller than most other tourism cities in China in terms of retail sales value. The city's relatively low wealth levels have constrained high-end retail market development. However, consumerism and brand recognition are relatively high in Dalian due to the long development history in retail sector. Therefore, well positioned, high quality shopping centres will likely do well in short to medium term.

	Nanjing	Chengdu	Qingdao	Dalian	Hangzhou	Shenyang
GDP Growth in 2000-2005 (%)	18.8	12.5	18.6	15.6	16.1	13.3
Retail Sales Growth in 2000-2005 (%)	19	12.5	21.4	10.1	18.2	11.2
Total Retail Sales in 2006 (USD million)	14,641	14,496	12,631	10,531	13,957	13,158
Disposable Income in 2006 (USD)	2,201	1,605	1,923	1,675	2,387	1,462

Source: Statistic Yearbook 2007

Currently, the two main retail areas catering for local residents are Qingniwa and Xian Road, which are both already fairly saturated with retail amenities.

The Qingniwa area is home to the most popular department stores such as Mykal Department Store and shopping malls such as ParkLand. Rents for shopping malls in this area outstrip other sub-markets, reaching USD 657-949 per sq m pa.

As Qingniwa is the retail hub serving eastern Dalian, the Xian Road area has emerged as the prime retail hub for the western part of the city. The Xian Road retail area covers about 6 sq km, stretching from Xian Road to Olympic Square and Peace Square. Compared with Qingniwa, the Xian Road retail area is more geared towards the local mass market and mostly attracts residents of western Dalian. It benefits from a convenient transportation system, backed by a number of public bus routes and parking facilities.

Luxury brands are mostly concentrated on the ground floor of the Shangri-La Hotel and Furama Hotel along Renmin Road. Some luxury brands can also be found in ParkLand, one of the highest-end shopping malls in Qingniwa.



Shopping malls dominate Dalian's retail market, accounting for 45% of the total prime retail stock, followed by department stores (at 26%) and retail podium formats (at 21%). However, most shopping malls in the city are struggling with poor performance. This largely reflects low differentiation, poor management, and a lack of uniform practices.

The above factors, combined with a massive increase in supply between 2003 and 2005 have translated into a significant adjustment of the Dalian retail market. A number of players have been forced out of the market due to poor performance, such as Itokin and Intime. Other retailers have re-positioned through brand adjustment and upgrading. For example, China Resources took over the unused VIVO Department Store along Tianjin Road in 2006 to refurbish it into an equivalent of MIXC⁴.

Looking forward, it will be high quality and clearly positioned shopping malls that will be successful in this saturated market.

⁴ The MIXC is a shopping mall developed by China Resources in Shenzhen. It has achieved huge success due to its clear position and professional mall management. The MIXC is considered as a role model for the shopping mall sector.



It is possible that, with the increasingly important position Dalian is playing in North East China, more high profile retailers will enter the market, pushing rentals to a higher level. This trend has been evidenced by Mont Blanc leasing 120 sq m and Hugo Boss leasing 200 sq m in the ParkLand Shopping Centre in Q3 2007. The improving wealth levels of Dalian residents will also be a major draw for retailers. Metro is planning to open at least one more store in Dalian before 2008 and IKEA is expected to open a store in 2008.

CLOSING THOUGHTS

Dalian is gradually transforming into an 'IT City' in China, and, ultimately, the "Chinese Bangalore", as referred to by Thomas L. Friedman in *The World is Flat*. Government support and the development of the business park segment have helped the city establish solid fundamentals in the software industry. The city's human resources advantages include a wealth of IT specialists as well as a high number of fluent Japanese language speakers. Currently, six of the top ten global BPO firms have operations in Dalian. However, fierce competition from cities such as Xi'an, Chengdu and Hangzhou, combined with rising labour costs, will make for a more challenging business environment.

Dalian is making significant efforts to move up the value chain and incorporate into the global supply chain. Growth of indigenous IT companies has been witnessed in recent years, with local IT giants gradually gaining a global platform. The entry of Intel and its massive investment will also be a big draw for the city to develop its hardware sector. It is estimated that around USD 2.5 billion of relevant investment will be diverted into Dalian, owing to Intel's investment.

The recent detailed policy from the central government on revitalising North East China has pushed Dalian to an even higher level. Dalian will be clearly positioned as the 'shipping centre for North East Asia' and also an important futures market in China. The aggressive development of the service industry in the city will finally benefit its office market, which is in its early stage, and lead to a more transparent and vibrant investment environment.



DEFINITION OF TERMS

ECONOMIC DASHBOARD

Population: Population refers to the total population as of 31 December.

There are two definitions of population:

- Registered population – those officially registered with the police.
- Permanent residence population – those who actually reside permanently in a location, usually longer than one and a half years.

Dalian's population refers to the total population.

GDP: Refers to the gross domestic (i.e. regional) product of a location.

Employment: Refers to the number of persons engaged in labour and receiving remuneration payment or earning business income, including fully employed staff and workers in state-owned, collective-owned or other kinds of economic sectors and otherwise employed persons.

Population Growth: Refers to the compound annual growth rate over the five-year period from 2001 to 2006.

GDP Growth: Refers to the annual GDP growth rate over the five-year period from 2001 to 2006.

Freight Traffic: Refers to the volume of freight transported by various means, measured in millions of tonnes.

FDI: Foreign direct investment refers to investment made inside China by foreign enterprises and economic organisations or individuals (including overseas Chinese, compatriots in Hong Kong, Macau and Chinese enterprises registered abroad).

GDP per Capita: Refers to the total gross domestic product divided by the registered population.

Disposable Income: Refers to the actual income at the disposal of a household that can be used for final consumption, other non-compulsory expenditure and savings, which is part of the urban households' income that can be disposed by the urban households themselves.

High Education Institutions: Refer to higher education institutions that provide higher education courses and training for senior professionals. They include full-time universities, colleges, high-professional schools, high-professional vocational schools and others. High education institutions are set up according to the central government evaluation and approval procedures.

Unemployment Rate: The registered urban unemployment rate refers to the ratio of the number of registered unemployed to the sum of the number of persons employed and registered unemployment in a location.

Average Wage Rates: Average wage rate refers to the average wage of fully employed staff and workers. It is calculated as follows:

Average wage of fully employed staff and workers = total wages of fully employed staff and workers/average number of fully employed staff and workers.

Business Environment: Jones Lang LaSalle's grading is measured by an assessment of a location's macroeconomic environment, its policy towards private enterprise and foreign investment and its labour market and tax regimes. A location's business environment is graded from A (highest) to C (lowest), with Shanghai providing the benchmark.

Quality of Life: Jones Lang LaSalle's grading refers to the quality of health, culture and environment in each city. A city is ranked among 15 cities (Shanghai, Beijing, Guangzhou, Shenzhen, Chongqing, Chengdu, Tianjin, Wuhan, Xi'an, Qingdao, Hangzhou, Suzhou, Nanjing, Dalian and Xiamen).

REAL ESTATE DASHBOARD

Offices Grade A Stock: Refers to the total completed Grade A office space (occupied and vacant). Grade A reflects an above-average property in the market, with quality criteria being at the upper end of the scale.

Retail Stock: Represents the total stock of all the department stores and shopping malls in Dalian.

Number of Hotels: Refer to the number of five-star hotels.

Office Construction Grade A: Refers to the total amount of Grade A office space in properties where construction has commenced and completion is expected in 2008 or 2009.

Office Vacancy Grade A: Refers to Grade A office floor space (as a percentage of the total Grade A stock) in existing properties that are physically vacant, ready for occupation today and are being actively marketed.

Benchmark Rents: Refer to the typical open-market rentals (within a range) that could be expected for a unit of the highest quality and specification in the best location expressed in US dollar per square metre per year.

Grade A Office Rents: Refer to the net rentals.

Industrial Rents: Refer to the rentals of warehouses mainly in Dalian Economic & Technological Development Zone, Dalian Hi-tech Zone and Dalian Free Trade Zone.

Residential Prices: Refer to typical prices (within a range) for high-end residential projects in US dollar per square metre.

Grade A Offices – Indicative Yields: Refer to the best (i.e. lowest) yield estimated to be achievable for a notional office property of the highest quality and specification. Indicative yields represent Jones Lang LaSalle's 'market view', based on a combination of market evidence where available and a survey of expert opinion.





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