APAC Regional Headquarters

Singapore on top, but competition to increase.
Outline

Our analysis of the location considerations of RHQs in Asia Pacific is split into four sections.

**Section 1:** We look at the economic backdrop and long-term themes for corporate profitability in the region against which global firms are choosing where to locate/relocate their headquarters to achieve the best competitive position.

**Section 2:** Focus on the key Asia Pacific hubs – Hong Kong, Singapore, Shanghai, Beijing, Sydney and Tokyo. We compare how the first three markets stack up against one another in the regional headquarters stakes.

**Section 3:** Relative strengths and characteristics of each office market – we look at the role of property in maintaining and increasing city competitiveness and business efficiency, and how being a location for RHQs has impacted real estate in these cities.

**Section 4:** Outlook on the changing nature of demand, and how real estate dynamics will help shape future changes in economic and spatial structure.

Competition between cities to attract major multi-national companies (MNCs) is already fierce. However, with long-term drivers of economic change continuing to shape the regional business environment, that competition is expected to further intensify. Singapore and Hong Kong continue to maintain a strong rivalry, while Tokyo and Sydney have long been key destinations for MNCs. The rapid economic development of China, and commensurate growing importance of its Tier 1 cities, have enabled Beijing and Shanghai to compete to host RHQs as well.

Generally, the main criteria that MNCs consider when selecting locations for regional headquarters (RHQs) include:

- Strategic geographical location – proximity to clients and markets.
- Rational and well-developed legal and regulatory framework.
- Globally competitive tax environment.
- Stable political environment.
- Favourable business environment, including incentives.
- Transparency and easy market access.
- Cost of operations.
- Availability of talent.
- Proximity to production facilities.
- Access to distribution channels.
- Good quality of life, including environment, schooling, housing, openness to foreigners etc.

While this list is comparatively long, the criteria vary in importance between companies. In essence, MNCs are seeking a strategic location that offers close proximity to clients and target markets as a top priority. Preferably, this location should also offer a well-developed and transparent regulatory framework, political stability and quality talent. Environmental quality is also a growing concern for companies locating their RHQs in Asia Pacific.

The role of property in city competitiveness

Commercial real estate is often seen as a derived demand, with the amount of floor space that needs to be provided stemming from the city’s economic attractiveness. However, it can also work in reverse such that the amount, quality and price of commercial real estate can actually be an attractor itself – companies move to cities because of their favourable supply or price dynamics. Hence the built environment is a key factor for cities and regions with respect to maintaining and growing their competitiveness on the regional or global stage.

In this report, we examine the key drivers of location strategy for RHQs in the Asia Pacific region. We then consider the key strengths and weaknesses of different property markets and how they can impact corporate real estate decisions. In line with this analysis of location strategy, we undertake a ranking exercise and score markets according to ten criteria – seven operational and three relating to real estate.

Competition between cities to intensify

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Section 1 - Location trends

Asia Pacific a critical battle ground for long-term growth

Asia Pacific’s ascension as a competitive and important economic region is a major pull for global businesses. Economic growth in Asia Pacific over the last decade has outpaced Europe and the US. Furthermore, although growth has slowed in some markets in recent years, Asia Pacific is forecast to increase its share of global GDP from 31% in 2015 to 36% by 2030 (Figure 1). Despite recent volatilities, economies in the region are still well positioned to offer rich long-term opportunities.

Importantly, the increase in economic diversity from the dominance of manufacturing and commodities to an increasing focus on service industries, has led to a clear trend towards companies opening new RHQs in the region. There are also signs of migratory shift within the region as companies reconfigure and relocate their operations to better leverage opportunities for operational excellence and reduced cost, whilst also identifying future opportunities for growth.

Established hubs vs. emerging markets

When making location decisions, Singapore and Hong Kong are often thought of as the most popular choices. However, Sydney and Tokyo are also established hubs which actively compete for RHQs. The changing economic geography of the Asia Pacific region though has seen a shift in spatial focus. The rise of the “Asian tiger economies” and rapid advancements in China and India have seen both Tokyo and Sydney somewhat marginalised to the geographic periphery of the region, while Singapore and Hong Kong remain at the core. In the case of Sydney, it takes 10 hours to fly to Shanghai, while Southeast Asia is at least a six-hour flight away.

The increasing trend is that most businesses are looking for locations that are geographically close to their target growth markets to facilitate speedier decision-making, better marketing and a more effective regional network and distribution strategy. This has seen emerging markets become more popular destinations. As China grows further in size and strategic importance, an increasing number of MNCs are considering the viability of basing their RHQs in China – this has been reflected in the increase in the number of MNCs in Shanghai, while numbers in other more established hubs have been much more stable.

To understand how locational factors change in tandem with changes in Asia’s economic landscape, it is helpful to consider some of the key longer-term drivers in the region. The rise of Asian consumerism

Although many markets in Asia are known for their manufacturing base, the expanding middle class and its growing spending power is a driving force behind consumerism in the region. Demand for consumer durables, education and healthcare has increased, but is expected to increase dramatically further. In 2009, Asia Pacific represented 28% of the global middle class; by 2020 this is forecast to increase to 54% and with it an increase of over one billion people.1

For obvious reasons China is a key market for many MNCs in consumer goods, with the likes of IKEA and Unilever moving their RHQs to Shanghai to better meet Chinese demand. Ford also decided to move its Asian headquarters from Thailand to Shanghai in 2009. As a two-way platform between China and the rest of the region, Hong Kong also has significant appeal. The 2015 business census identified that with 46% of RHQs in Hong Kong engaged in the import/export, wholesale and retail business, often as their parent company is manufacturing based (Figure 2). In fact, over 80% of all RHQs in Hong Kong included China in their target markets.

Meanwhile, the attempt of China to transform from low-end manufacturing to high-end value-add industries is changing the country from just a point of sale market to a place where MNCs can locate their research and development functions. In 2012 AstraZeneca relocated its Asia Pacific headquarters from Singapore to the Shanghai Zhangjiang high-tech park. In the same year, AstraZeneca relocated its Asia Pacific headquarters at Shanghai’s Technology Innovation Centre.

Nonetheless, Singapore remains the region’s most established healthcare hub. In 2005 the government invested SGD500m in the Biopolis business park, which has attracted more than 100 drug and biomedical companies, including Pfizer and Merck & Co. Companies remain attracted to the country with Royal Philips recently expanding their RHQ in Toa Payoh.

In China – this has been reflected in the increase in the number of MNCS located there. The number of MNCs in Shanghai has increased significantly from just a point of sale market to a place where MNCs can locate their research and development functions. In 2012 AstraZeneca relocated its Asia Pacific headquarters from Singapore to the Shanghai Zhangjiang high-tech park. In the same year, AstraZeneca relocated its Asia Pacific headquarters at Shanghai’s Technology Innovation Centre.

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Figure 1
Regional share of world GDP, constant prices and exchange rate

<table>
<thead>
<tr>
<th>Year</th>
<th>Region</th>
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<th>2020</th>
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<td>13%</td>
<td>14%</td>
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<tr>
<td></td>
<td>Other</td>
<td>8%</td>
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<td>8%</td>
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</tr>
</tbody>
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Source: Oxford Economics

Figure 2
Regional headquarters located in Hong Kong by sector, 2015

- Finance and banking: 46%
- Professional services: 19%
- Transportation & storage: 14%
- Other: 14%
- Import/export, wholesale & retail: 13%
- Retail: 8%
- Education & healthcare: 8%

Source: Hong Kong Census and Statistics Department

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Technological change fuels expansion
The growth of social media, cloud computing and the drive for greater internet speeds will drive activity in the TMT (Technology, Media, Telecommunications) sector. Furthermore, the digitalisation of consumption will play to the advantage of emerging internet players in Asia. The Asia Pacific region, therefore, is an integral part of TMT expansion and as such major TMT hubs are starting to emerge.

Numerous global TMT companies have set up RHQs in Singapore including Microsoft, LinkedIn and Cisco Systems, attracted by the country’s excellent network connectivity. More recently HubSpot, a leading inbound marketing and software company, also chose Singapore for its RHQ. Twitter, the popular microblogging social media site, set up its Asia Pacific headquarters in Singapore last year.

Alongside this, Hong Kong strives to be the prime location for data centres in Asia Pacific, and a hub for technological cooperation and trade. In this role it has benefited from government’s industrial revitalisation, advanced telecommunication infrastructures and a less regulated environment compared to mainland China.

ASEAN rising, and the end of ‘cheap’ China unlock opportunities in South & South East Asia
The ASEAN bloc, comprising of 10 countries, has been of interest to many due to its resilient and dynamic growth. The ASEAN Economic Community (AEC) has been immensely successful in working through its agenda, with the vast majority of targets having been met. While the ultimate goal of free trade barriers is unlikely to be achieved this year, there is still an expectation that “freer” trade and capital movement will be accomplished, resulting in a more conducive business environment. This will assist in increasing foreign investment and boost market attractiveness in these countries.

China has been the major recipient of foreign direct investment (FDI) among emerging economies in the last decade. Rising wages and the transformation of China’s economic structure, though, are altering its manufacturing functions in Singapore. Meanwhile, a growing number of Japanese companies have moved some of their key functions to Singapore, viewing the city-state as a strategic location from which they can oversee ASEAN countries in search of cheaper production costs. Similarly, major Indian companies such as Tata Consultancy Services and Mahindra have located their international or regional headquarters in Singapore.

Outbound FDI prefers Singapore as gateway
Outbound FDI is also an important theme, with investment boosting markets in Australia, Singapore, Myanmar and Thailand amongst others. Increasingly, we are seeing that Asian companies are using Singapore as their gateway to the world.

For example, Chinese companies like Trina Solar and Huawei have their RHQs in Singapore. Approximately 1,200 Chinese companies have offices in Singapore, 30% of which are in the high-tech sector reflecting a shift in focus towards South East Asia in search of cheaper production costs. Similarly, major Indian companies such as Tata Consultancy Services and Mahindra have located their international or regional headquarters in Singapore.

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By contrast, Hong Kong’s role is to serve as a gateway for outbound China investment capital and also as a platform for raising investment for China. According to Deloitte, mainland companies raised HK$195bn on the Hong Kong stock market in 2014, which accounted for almost 87% of the total raised and a huge jump from only 31% in 2010.

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Section 2 - Pros & cons of cities

Singapore, Hong Kong and Shanghai are Asia’s core RHQ locations, reflected in the number of companies which have chosen these cities for their RHQs. Competition among cities is intense, and all three cities need to remain innovative to attract capital and talent.

Shanghai provides access to China, but has regulatory obstacles
The established hubs of Singapore and Hong Kong are strong all-rounder as RHQ locations, whilst direct access to Asia Pacific’s largest market and economic titan drives Shanghai into the top three locations (Figure 4). This has been reflected in the rapid growth of RHQs in the city, estimated to have risen from 53 in 2003 to 470 in 2014 – an expansion rate of 21% per annum.

However, Shanghai does have weaknesses. The rising cost of land and the increasing occupancy cost of prime leased properties are concerns, as are rising salaries and mounting local business competition.

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Shanghai
Pros
Direct access to China
Commercial heart of China
Good distribution channels
Access to local talent
Land supply
Laboratory for Chinese business economic reform
Diverse economic base
Cons
Policy incentives
• Business subsidy for establishing a new RHQ
• Rental subsidy
• Simplified admin procedures and greater personnel mobility

Hong Kong
Pros
Open and free economy
Proximity to China
Favourable legal environment
Low tax regime
International talent
Good living conditions
Quality transport infrastructure
Cons
Infrastructure
Lack of diversity in space in core prime locations
Good living conditions
Lack of diversity in economic base

Pros
Shanghai is acknowledged as a key financial hub of China, with its high growth rate and large market size.

Cons
Increasing land acquisition cost
Rising occupancy cost of prime leased properties
Growing cost of living
Increasing employee salaries
‘War for talent’
Mounting local business competition

Policy Incentives
• Incentive I/RHQ Programmes including tax incentives (15% concessionary for RHQs for 3+ years on income from abroad)

Other main RHQ locations – Tokyo, Sydney and Beijing
Tokyo
Japan is a highly mature and sophisticated economy. There are acknowledged benefits of locating RHQs in Tokyo, including the size of Japan’s economy, extensive infrastructure, cutting-edge technology and high quality of living. However, given the mature status, exclusivity and distinctiveness of the Japanese market, foreign companies in Tokyo focus overwhelmingly on the Japanese market alone. The number of foreign firms using Tokyo as a location for their Asia Pacific RHQ is relatively small. Distance from other countries is one drawback, as well as the language barrier. In addition the effective corporate tax rate is high, and labour costs are the most expensive in the region. Although the Tokyo Metropolitan Government has launched a Special Zone for Asian Headquarters, providing preferential tax treatments and subsidies to foreign companies establishing Asian HQs in the designated areas, the cost of doing business remains considerable. The recent sharp deterioration in the yen, though, to a certain extent has eased some of this cost burden.

Sydney
Similar to Tokyo, Sydney is very much a longstanding choice of locating RHQs. The city boasts many positives including the ease of doing business with a western-friendly culture and highly skilled, English-speaking workforce. Its resilient economy, political stability, mature legal and regulatory systems, as well as excellent quality of life all make it an attractive choice. However, similar to Tokyo, geographically Sydney is at the periphery of the Asia Pacific region rather than at the centre. Recent depreciation in the Australian dollar has helped lessen business costs, though they still remain among the most expensive markets in the region. Consequently on broad metrics, Singapore and Hong Kong are often seen as better alternatives, offering western-friendly environments and English-speaking staff, in a more central location.

Beijing
Like Shanghai, Beijing has also seen costs rise, including the cost of acquiring land, occupancy cost and the cost of employing someone locally, all of which hits the bottom line of any business. Being the political centre of China, the city has its fair share of state-owned enterprises. It is, however, a city which is quite entrepreneurial, with many successful start-ups being born within the bounds of the city, and in Zhongguancun in particular. Today, Zhongguancun is popularly known as the ‘Silicon Valley of China’ and is largely responsible for making Beijing the country’s single largest hub of both mature TMT industries and also an incubator for related start-ups.

Singapore offers economic diversity and a gateway to ASEAN
Similar to Hong Kong, Singapore has lured foreign investors with its tax friendly incentives, transparent and legal framework, skilled workforce and excellent infrastructure. However, Singapore is the only economy in Asia and one of two in Asia Pacific, along with Australia, that currently retain a AAA credit rating from all three ratings agencies.

Being in the same time zone as key Asian markets, such as China and Malaysia, has also been a major factor, as well as the fact that many of its residents are bilingual in English and Mandarin/Malay. In the past, the main challenge for Singapore as an RHQ location has been its distance from China. This is balanced out by Singapore’s status as gateway to the growing South East Asia region and its emerging position as bridge between India and China.

Indeed, the city state has set its sights on becoming a centre for wealth management, education and healthcare by exploiting its position as a link between China, India and also the Middle East. Singapore also scores highly for quality of life and was ranked as the top destination globally for expats in ECA’s 2015 survey.

Where Singapore once trailed Hong Kong in terms of economic diversification, it has made great progress toward becoming a vibrant and varied financial and commercial hub. Beyond the existing attractive tax system, the government has introduced tax incentive policies to attract different MNCs to establish their RHQs. Providing multinationals promise to hire a certain number of people and fulfil other business criteria, RHQs can get a 15% concessionary tax rate.

In terms of negative aspects, Singapore has comparatively few. The main negative is cost, although in the latest cost-of-living ranking by Mercer (2015) Hong Kong is back at the top of the list as most expensive after briefly being supplanted by Singapore. Although it is still very early in the process, as ASEAN countries continue to develop and expand, in the long run, Singapore could find itself in a similar position to Hong Kong sometimes being bypassed for Shanghai. However this is not considered a near-term concern.

More relevant, though, are the recent government initiatives to calibrate the inflow of foreign labour into Singapore and prioritise hiring local workers over foreigners which could prevent RHQs from setting up shop there.
Data and Methodology

We assess and rank the attractiveness of each city in the RHQ stakes across seven operational categories and three real estate categories:

Operational
1. Proximity to clients and markets: distance from the rest of the region, in particular China and ASEAN.
2. Favourable legal and regulatory environment: rule of law, government effectiveness.
4. Human capital: quality of education, labour market efficiency, innovation, attractiveness to expat talents.
5. Transparency: level of openness and clarity across the economy, government and regulation.
6. Freedom of information: ready access to required quantity and quality of data.

Real estate
10. Prime workstation cost: cost in USD per sq m per annum in 2015.

Source: Data used is based on sources from OECD, Economist Intelligence Unit, World Bank, MoE, Oxford Economics and Cushman & Wakefield Research.

Section 3 - Real estate perspective

Asia Pacific a critical battle ground for long-term growth

From a corporate real estate perspective, a city’s competitiveness also relates to its ability to provide appropriate space to accommodate demand and respond to a changing business environment. A city may perform well against all of the operational selection criteria, however it also needs to be able to provide suitable office accommodation of an appropriate quality, in the right location and at the right cost (Figure 4). Low market volatility in respect to all three of these criteria in this respect is a positive, allowing for corporates to appropriately plan and budget for their office occupational needs. Accordingly, the property market has an important role in maintaining and growing a city’s competitiveness.

Accessibility and availability

Along with cost, discussed subsequently, the quantity and quality of office stock is a key differentiator and a headline concern for corporate real estate decision makers. In broad terms, the larger a market’s stock, the greater number of companies (and workers) that can be accommodated, which in turn affords greater economies of scale that can be derived from agglomeration.

Hong Kong is decentralising to overcome scarcity of space

Hong Kong and Singapore are facing the greatest pressure with regard to accommodating future expansion. Firstly, considering Hong Kong, its vacancy rate is currently at only 5% (Figure 5) which presents a barrier to entry for those requiring large amounts of contiguous space. Lack of office supply is a prevailing issue in the tightly packed city, with supply of top-quality space remaining more or less constant for the last decade, and vacancy remaining stubbornly low even during the financial crisis. At the same time, the sheer compactness of Hong Kong is one of its plus points and makes the city incredibly efficient.
Figure 6 Office occupiers in Singapore by sector, 2015

Outside of the Raffles Place and Marina Bay CBD/Financial district area, there are also a range of accommodation options from business parks to campus style office accommodation. Permissible uses within business parks, though, may not be suitable for all companies. Notwithstanding, high-profile companies such as Nike moving out of their downtown space (Plaza 66) and into leased suburban (leased) campus-style offices have completed or are underway in the past three years. This is very much a demand-led decentralization initiative, rather than one that is supply-led, with high-profile companies choosing to occupy campus-style offices in their home market to struggle to find a similar product in Shanghai. In doing so, prime waterfront land of the current port site has been reserved list. The Government Land Sales Programme, which is for a supply response through developers submitting an acceptable bid price (in the case of the reserved list). For a long time, diversity of space in Shanghai has not been as high as in Singapore. In the past, companies choosing to occupy campus-style offices in their home market have struggled to find a similar product in Shanghai. Consequently, they resorted to leasing CBD grade A office space. The situation, though, is fast changing as several suburban (leased) campus-style offices have completed over the past two years and many more are in the pipeline for the next three years. This is very much a demand-led decentralization initiative, rather than one that is supply-led, with high-profile companies such as Nike moving out of their downtown space (Plaza 66) and into leased campus style office space (in the Yangpu district).

Increasing variety of space options in Shanghai

In contrast, Shanghai enjoys the advantage of a wide hinterland. In 2006-07, when vacancy rates were around 23%, securing large tranches of contiguous office space was difficult. Since then the prime vacancy rate has now eased to around 9% and is expected to increase further. In total, 6 million sq m of office space is scheduled to complete by 2018 which is forecast to drive vacancy to 18%. Such a considerable amount of development pipeline provides good options across a variety of grades to RHQs in the city. However, as many new developments will be in the city’s non-core areas (Map 1), proximity to amenities will need to improve in order to attract major firms. In this respect, Shanghai is distinctly lacking not only Singapore but also Hong Kong.

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For a long time, diversity of space in Shanghai has not been as high as in Singapore. In the past, companies choosing to occupy campus-style offices in their home market have struggled to find a similar product in Shanghai. Consequently, they resorted to leasing CBD grade A office space. The situation, though, is fast changing as several suburban (leased) campus-style offices have completed over the past two years and many more are in the pipeline for the next three years. This is very much a demand-led decentralization initiative, rather than one that is supply-led, with high-profile companies such as Nike moving out of their downtown space (Plaza 66) and into leased campus style office space (in the Yangpu district).

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Occupancy costs

While cost has always been an important factor for occupiers, it has come under closer scrutiny since the Global Financial Crisis. To a certain extent, these costs will be set against the benefits of locating in a particular market and the quality of space on offer. However, higher costs require higher corporate returns or at least greater perceived benefits. Hence we define occupancy costs as the average total cost of leasing prime net usable space. This includes rents and outgoings, such as maintenance costs and property tax, if they are normally payable by the occupier. However operational costs such as electricity, waste and HVAC are excluded.

Hong Kong’s central business district is still one of the most expensive places in the world to do business, ranking as the most expensive market in Asia Pacific. Total occupancy costs in Hong Kong stood at USD1,924 per sq m per annum in 2015, practically double those of Singapore and Shanghai.

Following a decline in Hong Kong occupancy costs in 2013, they swiftly returned to growth in 2014 and are forecast to continue to increase over the period to 2018. Nonetheless, the rental gap between core and non-core areas is expected to narrow. This reflects a general trend of consolidation of the financial sector in Hong Kong and expansion of the TMT sector into non-prime locations.

Shanghai offers more affordable real estate than Hong Kong. However, despite rental decline in 2012 and 2013, Jing’an is now more expensive than Singapore – mainly as a result of recent rental decline in the latter. Demand in Shanghai is strong, but with ample supply only modest rental growth of less than 1.5% per annum is expected in Pudong, while rents are forecast to remain largely flat.

Lack of grade A/premium supply drove significant cost increases in 2007 in Singapore. Tight supply has now been relieved and coupled with a lacklustre leasing market has resulted in rental decline over 2015. Further new supply in 2016 is expected to drive double-digit vacancy and further rental decline and therefore provide a more attractive leasing environment for occupiers.

Considering the ways different organisations occupy and use space (i.e. space allocation per worker, or space efficiency) provides interesting differences a different picture. Not only does Singapore currently have lower occupancy costs on a per sq m basis compared to Shanghai, this is further exacerbated by better space efficiency.

Of course, if market convention in Shanghai were to move to greater space efficiency, which is approximately 20% worse than Singapore, this would make Shanghai a more affordable market. Interestingly, space efficiency is worst in Hong Kong, exacerbating its already higher rent per sq m. In a world of cost cutting and space optimisation, this is an important factor to consider.

Table 1 Office occupancy costs, 2015

<table>
<thead>
<tr>
<th></th>
<th>Base rent (USD per sq m pa)</th>
<th>Outgoings (USD per sq m pa)</th>
<th>Total occupancy costs (USD per sq m pa)</th>
<th>Total occupancy costs (USD per workstation)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hong Kong</td>
<td>1,654</td>
<td>269</td>
<td>1,924</td>
<td>21,110</td>
</tr>
<tr>
<td>Shanghai</td>
<td>900</td>
<td>129</td>
<td>1,029</td>
<td>9,050</td>
</tr>
<tr>
<td>Singapore</td>
<td>832</td>
<td>98</td>
<td>930</td>
<td>8,850</td>
</tr>
</tbody>
</table>

Total occupancy costs can be reduced through improving space efficiency

Section 4 - Outlook

Migratory shift within cities

It is commonplace for companies to geographically reposition themselves to take advantage of economic growth, cost efficiencies and competencies. These migratory shifts not only occur between cities, but also within cities as local real estate market dynamics change.

As has been highlighted above, the Hong Kong government has made extensive efforts to mitigate office shortage by consolidating the existing CBD to enhance its supply of offices in terms of both quantity and quality, and at the same time exploring opportunities for the development of a second prime-grade office node to facilitate decentralisation, Kowloon East, or CBDE, is forecast to further accommodate almost 1 million sq m of space. In addition, there are plans to redevelop government offices in Wanchai to provide grade A space to the private sector, which could add 177,000 sq m in the city core. Migratory shift is already underway, with some big name firms relocating their RHQs out of Central, the traditionally prestigious location for businesses, to West Kowloon and Kowloon East, including Morgan Stanley and Manulife International.

Similar efforts have also been seen in Singapore, where the government is further encouraging the development of commercial space outside the CBD to relieve congestion and bring the workplace closer to homes. Some growing decentralised nodes include Jurong Gateway, Changi Business Park and Paya Lebar Central. The Government has spearheaded some of these moves, such as some agencies associated with the Ministry of National Development relocating to Jurong.

As Shanghai evolves to become a more mature, multi-tiered office market, facilitated by new development in non-core areas, similar relocations are expected to occur. An industry-specific hub has been developed in the Shanghai North Zone to attract major IT companies, while part of the Puxi Xuhui Binjiang area is intended to be transformed into West Bank Media Port to attract major media companies. However, relocating within Shanghai is not necessarily straightforward. Variations in district taxation can make strategic location decision-making more difficult as districts compete with one another for inward investment and corporate income tax.

Diversity to drive the rise of divisional headquarters

In recognition of the region’s importance and unique diversity in terms of culture, language and customs, many companies are abandoning the “one-size-fits-all” approach to the Asia Pacific region, and are instead creating multiple strategic nodes, or divisional headquarters, across the region. Of course, some of this is also being driven by changes in international tax policies, with OECD countries seeking to prevent MNCs from channelling all their regional profits through one low tax country.

Divisional headquarters are often divided along the lines of business units, which are then located in markets that are most suited to their needs. The most common of these is to have client-facing operations in prime locations, with back-office functions in secondary locations. Off-shoring, or BPO, is also highly common. There are, however, more functional drivers. Microsoft has its official RHQ in Singapore, but has located its R&D Group HQ in Beijing Zhongguancun, regarding China as a key growth market and location for future innovation. On this premise, Beijing could become more important as a divisional headquarters location given its political-relationship focused market.

As the region continues to develop and advance, opportunities in emerging markets will also begin to appear. The rise of ASEAN economies is likely to offer substantial opportunities in the manufacturing sector. Again, the shift to a divisional headquarters structure would allow sites in an established market, likely Singapore, but have the manufacturing division sited elsewhere in South East Asia to overlook operations. These markets also offer significant cost efficiencies with regard to office space. Occupancy costs in Bangkok and Kuala Lumpur, for example, are less than a third of those in Singapore (Figure 7).

Figure 7 Total office occupancy costs per workstation p.a. 2015 (USD)

Source: Cushman Wakefield Research

<table>
<thead>
<tr>
<th>City</th>
<th>Total Office Occupancy Costs (USD per workstation)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hyderabad</td>
<td>177</td>
</tr>
<tr>
<td>Chennai</td>
<td>192</td>
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<tr>
<td>Pune</td>
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<td>Manila</td>
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<tr>
<td>Chongqing</td>
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<td>Bangkok</td>
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<td>Qingdao</td>
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<td>Hangzhou</td>
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<td>Wuhan</td>
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<td>Jakarta</td>
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<td>Dalian</td>
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<td>Shenyang</td>
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<td>Ho Chi Minh City</td>
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<td>Hangzhou</td>
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<td>Mumbai</td>
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<td>Melbourne</td>
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<td>Dallas</td>
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<td>Brisbane</td>
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<td>Tokyo</td>
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<tr>
<td>Hong Kong</td>
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</table>

Source: Cushman Wakefield Research
“Hong Kong vs Shanghai’ becomes ‘Hong Kong plus Shanghai’

Competition between Hong Kong and Shanghai has significantly increased in recent years, almost to the extent that it receives similar attention to the rivalry between Hong Kong and Singapore. With recent announcements on establishing China’s first free-trade zone (FTZ) in Shanghai, companies are re-examining the future value proposition of the two cities and restructuring long-term business plans accordingly.

Covering approximately 121 sq km, the Shanghai FTZ is a major testing ground, not only for the liberalisation of trade in goods, but also for the services trade, especially financial services (involving interest rate liberalisation, future experiments with free RMB convertibility in the capital account, opening up of the financial industry, financial service innovation and some other offshore financial services). If implemented successfully it will go a long way to fulfil Shanghai’s aim of being a major financial, trade and shipping centre by 2020.

In addition to Shanghai, major financial firms will also evaluate Qianhai - the new Hong Kong-Shenzhen co-operation zone. Officials see significant potential for this zone, promoting it as “the Manhattan of the Pearl River Delta”. The 15-sq km special economic zone on the west side of Shenzhen is expected to initially provide 3.5m sq m of Grade A office facilities in a location only 10 minutes from Hong Kong airport and 7 minutes from Shenzhen airport. The zone is expected to attract major financial and service industries that have strong ties with the Mainland.

Notwithstanding the increased competition between Hong Kong and Shanghai, our view remains that the two can co-exist as complementary RHQs serving different roles. Like New York and Chicago, Hong Kong and Shanghai are very different cities. Shanghai lacks the regional and global presence of Hong Kong. As the commercial heart of China, Shanghai provides direct access to the Chinese market – particularly North and North East China - and is an optimal location from which foreign and domestic companies can raise capital in RMB denominations for business expansion in China. Hong Kong, meanwhile, remains a reliable option for regional and mainland Chinese companies to raise foreign currency for business expansion plans in the wider Asia Pacific region.

Summary

Singapore and Hong Kong are still the most prominent locations for RHQs in the Asia Pacific region. The two have enacted laws to specifically make them attractive destinations for MNCs to set up regional operations. In addition, these two cities have enacted strong legal and regulatory frameworks, tax incentives, high quality education and healthcare systems and a high standard of living for expatriate workers.

While these factors are still important to MNCs, it is clear that the decision-making landscape has begun to change. Singapore and Hong Kong are facing increased competition and not just from each other. Currently, the strongest competition is coming from Shanghai, which can offer quality local talent, a diverse economy and abundant office space at a cheaper rate. More importantly, though, the city is a gateway into the large, lucrative China market.

As the region continues to evolve, competition will come from other locations as well. Emerging markets will continue to grow in size, raise their regulatory, educational and infrastructure standards and subsequently become more attractive to MNCs. In this way we expect cities in ASEAN countries to rise to prominence within South East Asia and for Tier II cities in China to become more attractive as companies spread beyond Hong Kong, Shanghai and Beijing. It is noted that attempts to attract MNCs are already being made in some of these markets such as Malaysia’s “InvestKL” initiative as part of its Economic Transformation Programme (ETP).

Furthermore, it is already evident that with such diversity across Asia Pacific, and a move to clamp down on tax-minimisation practices of MNCs, there is a conscious move to establish strategic nodes in the region rather than a single RHQ. No individual city can offer a company everything that it needs, especially if that company has a diverse array of business units and requirements. Rather we expect to see smaller RHQs set up in established markets and for there to be numerous divisional headquarters across the region taking advantage of each city’s strengths. Again this plays to the strength of emerging markets.

In all instances, though, an in depth understanding of each city across the political, economic, demographic and real estate landscape is required, in order to maximise any opportunities that are presented.
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