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Emerging City Winners Profiles: China Qingdao

- *Qingdao is home to some of China's best-known brands*
- *Chosen as one of the venues for the 2008 Olympic Games*
- *Boasts the 3rd largest sea port in China*
- *Attracts 27% of South Korean investment in China*
- *One of China's most famous travel destinations*
- *Logistics offers the best short term real estate opportunities. Strong demand also exists for Grade A offices.*



CITY SUMMARY

- Qingdao is home to some of China's best-known brands, including Haier, Hisense, Tsingtao Beer and Aucma
- It has been chosen as the venue for the Sailing Regatta in the 2008 Olympic Games
- It boasts the 3rd largest sea port in China after Shanghai and Shenzhen
- Almost 50% of China's professional marine experts are located in Qingdao
- It is the Chinese city with the highest level of South Korean investment
- It is one of the most famous travel destinations in China
- The logistics sector offers the best short term real estate opportunities
- In the office sector, there is strong demand for Grade-A office buildings

ECONOMIC DASHBOARD

Size	Population (million 2006)	7.5
	GDP (USD billion 2006)	40.2
	Employment (million 2006)	2.4
Growth	Population (% pa 2000–2006)	1.01
	GDP (% pa 2000–2006)	19.6
Infrastructure	Air Passengers ('000 2006)	6,791
	Freight Traffic (million tons 2006)	224
Openness	FDI (USD billion 2006)	3.7
	Exports (USD billion 2006)	23
Wealth	GDP/Capita (USD 2006)	5,367
	Disposable Income /Capita (USD 2006)	1,923
Education and Labour	Higher Education Institutions (2006)	25
	Total Enrolments ('000s 2006)	245
	Unemployment (% 2006)	2.96
	Average Wage Rates (USD 2006)	2,330
Business	Business Environment (Score)	B
Lifestyle	Quality of Life (Rank)	7 th

- Please refer to Definition of Terms, Exchange Rate in 2006: 1US\$=7.9719RMB

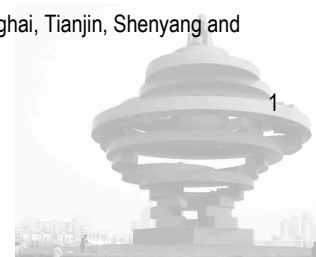
Qingdao is best known for its highly successful indigenous brands (such as Haier, Hisense, Tsingtao Brewery and Aucma) and as an area of outstanding natural beauty. More recently, this city on the banks of the Yellow Sea has caught investors' interest due to its role in the 2008 Olympics. It is one of the few cities in China co-hosting the 2008 Olympics with Beijing¹.

If the Olympics and well-known brands have been the external drivers of Qingdao's development, then its key asset has been its strategic location. Japan and South Korea are just an hour's flight from Qingdao, putting it firmly on the radar screen of Japanese and South Korean investors. Strong cooperation between Qingdao and South Korea has been a significant driver of the city's growth.

The city's port, which is the 3rd largest sea port in China after Shanghai and Shenzhen, has provided Qingdao with tremendous opportunities for developing the logistics and shipbuilding sectors. Qingdao attracts logistics and marine experts from all over the country. Indeed, almost 50% of total Chinese marine talent is today located in Qingdao.

Drawn by the city's strategic advantages and strong prospects, a growing number of international investors and developers are rushing to the scene. We believe that with the further opening of the city, Qingdao will quickly become a rising star in the Greater Bohai Rim region.

¹ Other cities include Hong Kong, Shanghai, Tianjin, Shenyang and Qinhuangdao.



ECONOMIC BACKGROUND

GDP is growing rapidly on the back of the strong marine and tourism industries

Qingdao boasts the fastest economic growth over the past 5 years out of China's 12 key secondary cities. Qingdao's GDP growth rate for 2000-2005 was 19.6%, almost 200 basis points higher than the group's average. The strong momentum is fostered by the marine and tourism industries, which benefit from Qingdao's strategic location on the Yellow Sea and long coastline (the longest in China). In 2006, the value added output of the marine industry amounted to USD 5.2 billion, accounting for 12% of the city's GDP. The tourism industry is also booming; its growth triggered by the 2008 Olympics. The tourism industry accounted for 10% of GDP in 2006, and the number of foreign tourists, currently 0.85 million, is expected to reach 1.3 million by 2010.

Economic cooperation with South Korea

Qingdao is the city in China with the highest level of South Korean investment. It is home to more than 8,000 South Korean firms and almost 60,000 South Korean nationals, with 10,000 additional South Koreans arriving every year. South Korea has become Qingdao's most important partner in terms of trade and foreign investment. In 2005, the trading volume between Qingdao and South Korea reached USD 7 billion, accounting for 23% of total trade. The actual utilised foreign direct investment from South Korea was USD 8.6 billion, 27% of total South Korean investment in China.

In contrast to many cities which are only on the receiving end of foreign direct investment, Qingdao also has interests in the South Korean market. Tsingsao Beer, Hai'er and most of the well-known state-owned firms have invested in South Korea.

Nonetheless, since 2006 Qingdao has seen increasingly diversified sources of foreign investment, with a growing number of investors from North America, Europe, Latin America, Africa and Oceania becoming active in the market. This diversification will further unlock Qingdao's potential.

Moving up the value chain

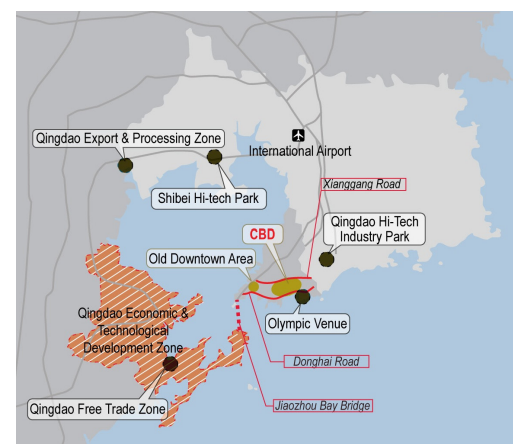
The performance of industries such as electronics and home appliances, petrochemicals, automobiles and shipbuilding has endowed Qingdao with a solid industrial base. However, the focus to date has been on low value added parts in the supply chain. To improve the city's future economic prospects, the Qingdao municipal government is keen to move up the value

chain. IT has been one of the main sectors to be targeted, with Qingdao being named a "National Software Industrial Base" by the central government in 2002. This has facilitated the creation of a sound business environment for IT corporations. Lucent Technology (now Alcatel-Lucent), for example, has set up its R&D centre in the Qingdao Software Park. This is one of its 9 global R&D facilities.

Qingdao going forward

Going forward, Qingdao is seeking to position itself as the "International Shipping Centre, Regional Logistics Centre, Service Centre, Financial Centre and Hi-tech Industry Centre" of northern China.

URBAN FORM & INFRASTRUCTURE



Planned as a leading city in Shandong Province

The newly released 'Overall Urban Plan for the Shandong Peninsula City Cluster' has confirmed Qingdao's leading role in Shandong Province. This region is an increasingly popular destination for industries relocating from both South Korea and Japan, as well as for capital from southern China.

According to this plan, Shandong province will develop into a pole able to compete with the Yangtze River Delta and the Pearl River Delta, the most successful city clusters in China. It covers 8 cities in Shandong including Qingdao, Jinan, Yantai, Zibo, Weihai, Weifang, Dongying and Rizhao, whose combined population amounts to 42.4 million inhabitants and combined GDP accounts for 67% of the total Shandong GDP. Qingdao and Jinan have been highlighted as the two core cities in this region, with Qingdao foreseen to play a key role equivalent to that of Shanghai in the Yangtze River Delta and Guangzhou/Shenzhen in the Pearl River Delta.

An Evolving Urban Form: From West to East

The central urban area in Qingdao covers four administrative districts, namely Shinan, Shibei, Sifang and Licang with a land area of 189 sq km and urban population of 2.7 million. In all the Qingdao municipality city consists of seven administrative districts and five satellite cities with a combined population of 7.4 million.



The city has undergone dramatic urban transition with the municipal government relocating from west Zhongshan Road, the old downtown area,

to East Hong Kong Road in 1992. Since then, Hong Kong Road has emerged as the key CBD area and now hosts most of the Grade-A offices and prime retail space, as well as high-end residential projects. In contrast, the old downtown has gradually decayed and its business activities are now limited to residential projects and middle-end department stores. Nevertheless, the old downtown's suburban area (named Badaguan) remains a prime area for high-end residential projects and travel resorts given its historic German buildings and beautiful beaches and scenery.

Around the urban area, three industrial regions have emerged, forming "Big Qingdao". This includes, in the west, Huangdao, an industrial centre driven by the port-related industry; in the north, Chengyang, a Japanese and South Korean manufacturing base; and, in the east, Laoshan, a hi-tech industrial centre.

CBD: The Shinan CBD core, with a land area of 1.5 sq km, nestles around the new City Hall. Shandong Road and Hong Kong Central Road, the most bustling and modern areas, host most of the Grade-A offices such as the Qingdao International Finance Centre, Cyberport, Crowne Plaza and TOP Yi He International, as well as the modern retail space in the city including Carrefour, Jusco and Sunshine department store.



Olympics venue: The Olympics sailing venue, located in Fushan Bay near the City Hall, will be turned into an attractive entertainment centre. This will include a water sports centre with

first-class sailing facilities, a yacht club, an international liner terminal, a conference centre, a five-star hotel, an upscale shopping centre and public parks. It will become a landmark in Qingdao upon completion, and several high-end residential

projects have already been built nearby to capitalize on its impact.

Infrastructure Improvements

Infrastructure improvements have been a major challenge for the government due to the mountainous topography and the position of Jiaozhou Bay, which separates downtown Qingdao from the new port and western industrial zones. However, to cater for the needs of the aggressive city expansion plan, USD 10 billion will be invested in infrastructure over the next 5 years. The most ambitious plans are to build an undersea tunnel and a bridge connecting Huangdao and the CBD. The Qingdao Jiaozhou Bay Bridge, with a length of 35.4 km and minimum cost of RMB 9.94 billion, is due to be completed around the 2008 Olympics; the tunnel is expected to be completed by 2010. These two projects will help connect different parts of the city, turning Qingdao into a true metropolitan area.

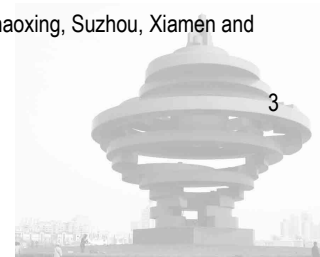
BUSINESS ENVIRONMENT

As a city opened up early in the 19th century, Qingdao has been regarded as one of the five main foreign trade ports together with Shanghai, Guangzhou, Tianjin and Dalian. Its long history in dealing with foreign investors has taught the government how to treat new entrants in the market. Indeed, the government's effectiveness and efficiency was praised by the World Bank, which nominated Qingdao as one of the six "Golden Medal Cities"² in China in terms of business environment in 2006.

The Mayor of Qingdao, Mr. Xiageng who has a PhD in Economics, has paid much attention to property rights. The local government has also focused on improving its level of service, using high-level planning and fiscal powers to increase the attractiveness of the market. Interestingly, Mr. Xiageng has at the same time sought to liberalize political governance, opening direct lines of communication with more than 300 local citizens through television, the most innovative idea in China.

The sound investment environment was the cradle for many indigenous brands. Back in 1984, Qingdao brought out the "Brand Economy" concept to stimulate the growth of domestic companies and encourage cooperation. The municipal government created incentives targeting everything from local companies' investment decisions and financial operations to marketing issues. Ten years later, the result has been that the

² The other five cities are Hangzhou, Shaoxing, Suzhou, Xiamen and Yantai.



10 largest enterprises account for more than 50% of Qingdao's total economy. This is known as the "Qingdao phenomenon".

CORPORATE ACTIVITY

Qingdao attracts 40% of all FDI heading to Shandong province, and is home to some of China's leading brands - most famously Tsingtao Beer, but also consumer electronics giants Haier and its rival Hisense. The city provides a convenient export-processing base for foreign manufacturers, particularly firms from South Korea and Japan.

Local Giants

Qingdao now is home to more than 10 prominent Chinese brands in sectors ranging from hi-tech and beer to white goods. The top 10 companies currently account for almost 50% of total industrial output in the city. The best-known and most popular among them are Haier, Hisense and Tsingtao Beer.

Haier, set up in 1984, grew from an ailing township enterprise with USD 178,000 in debts into the 4th largest white goods manufacturer worldwide. It now has 50,000 employees and 13 factories overseas, notably in the US, Malaysia, the Philippines, and the Middle East. Haier's fame is largely attributable to the CEO, Mr. Zhangrui Min, who has driven the company's innovation and international expansion. The continuous flow of innovative ideas, such as creating a vegetable washing machine for peasants in rural China, a washing machine designed to make goats' milk cheese, and a fold-out table which enables coolers to double as desks, has greatly raised Haier's reputation nationally and even worldwide.



Haier and rival Hisense have helped to create an electronic home appliance kingdom in Qingdao.

These two companies, which today hold 38% of the market share in

China, have attracted firms in the home appliance supply chain who are keen to capitalize on the agglomeration effect.

Tsingtao Beer, a symbol for Qingdao or even for China, has a history of more than a century. It was originally set up by a German investor in 1903, and was awarded the "Golden Prize" in the Munich World Exhibition in 1906. Time hasn't erased Tsingtao Beer's reputation. On the contrary, it has become a leader of the beer industry. Moreover, the Tsingtao beer festival held in Qingdao every year since 1991 has become not only a popular entertainment festival, but also an important

international event enhancing economic cooperation at a national and international level.

Foreign Firms' Presence

The major overseas firms with a presence in Qingdao include Japanese manufacturers, such as the trading arm of Mitsubishi which operates a food-processing joint venture (JV) in Jiaonan County, west of the city's Economic Development Trade Zone (ETDZ). South Korean and Singaporean companies have also chosen the area as a base for mainland operations, and western investors are increasingly visible. AT&T of the US has a telecom equipment manufacturing JV, Coca-Cola a bottling JV, and Swiss-based Ciba-Geigy has several pharmaceutical JVs in the city. Maersk, Ikea, Nike, Emerson, Durex, Bombardier, etc are also some of the recognizable brand names that have a notable presence in the city.

In the petrochemical industry, the entrance of big players, and stimulus provided by government initiatives aimed at boosting cooperation, has significantly raised the profile of the industry.

Lidong Chemical, founded by LG group and Qingdao Kailian Group, is the world's leading petroleum production company. It invested USD 540 million in Qingdao, enabling it to produce one million tons of petroleum annually and making it the largest foreign investment project in Shandong province.

LABOUR AND EDUCATION

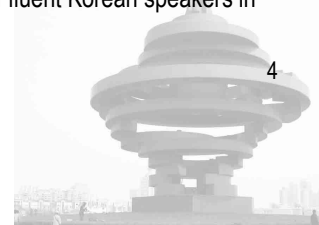
Abundant marine experts are a key asset

Benefiting from its strategic location and a vibrant marine industry, Qingdao has become the leader in marine research. Located in the city is the Ocean University of China, renowned as the best university in the field, as well as 30% of China's independent marine research institutions. A national level marine science and technology lab was also set up there at the end of last year; this is the first such lab in the country.

The abundance of human resources in the marine industry has enabled Qingdao to move up the value chain, so that it no longer relies solely on low value-added sectors such as pure fishing, tourism and trading based on the marine industry. It has now developed hi-tech sectors including oceanic chemicals and marine medicine.

Advantage of foreign language speakers

The ongoing economic cooperation with South Korea has led to the emergence of a large number of fluent Korean speakers in



Qingdao. This factor helped Qingdao attract USD 90 million of South Korean investment in 2005, almost as much as the combined total investment from Hong Kong, Japan, the USA and Taiwan, the top 5 investors in the city.

Low cost vs. lack of supply

Although rich in marine experts, Qingdao is short of labour in general, especially highly skilled labour with management skills. The labour pool provided by universities and colleges amounts to 245,000 graduates annually, only one third of that in education bases such as Chengdu and Wuhan. However, this shortage is to some extent compensated for by the low cost of labour in the city. The average annual wage in 2006 was USD 2,330, even lower than that in Chongqing, a city regarded as having a large low-cost labour pool.

With the limited supply of land and fierce competition in southern China, more and more foreign firms are seeking cost effective locations in northern China; Qingdao, with its low costs, is an obvious choice. To alleviate the labour shortage problem in the city, the Qingdao municipal government has adopted initiatives designed to attract immigrants. According to the overall plan for the Shandong peninsula city cluster, the urbanization rate will reach 60% by 2010 and 70% by 2020, up from the current 57%. This increase will encourage an influx of millions of new workers.

QUALITY OF LIFE

A place where the mountains meet the sea



Qingdao, renowned for its carefully preserved Teutonic architecture and 580 m beach, has become one of the top travel destinations in China. In 2006 Qingdao welcomed 29 million

tourists, a 14.7% increase on the previous year.

Various fairs and festivals take place throughout the year, taking advantage of the year-round mild climate. One of the most famous events is the annual Qingdao International Beer Festival which takes place in the last 2 weeks of August. It attracts millions of people every year from other parts of China and over 20 different countries, helping to raise Qingdao's profile internationally.

Qingdao, with its clean air and quick and easy access to core Chinese cities such as Beijing and Shanghai, is attracting not

only foreigners with businesses in China, but also Chinese people from all over the country. The strong demand for holiday homes has brought about a boom in the residential market.



REAL ESTATE DASHBOARD

Market Size/Stock	
Offices Grade A (000s sq m, Q2 2007)	500
Retail ('000s sq m, 2006)	912
Number of Five Star Hotels (2006)	6
Market Activity	
Office Construction Grade A* (000s sq m by 2009)	110.2
Retail Construction (000s sq m by 2009)	520
Office Vacancy Grade A (%Q2 2007)	9.6%
Benchmark Values	
Offices Grade A – Net Effective Rents (USD per sq m pa)	167
Retail – Rents* (USD per sq m pa)	700
Warehouse – Rents (USD per sq m pa)	26-48
Hotels – Room Rates (Five Star, USD)	132
Residential Prices (USD per sq m)	1,600-3,800
Grade A Offices – Indicative Yields (%)	9%-10%

Source: Jones Lang LaSalle Research

REAL ESTATE TRENDS

The property market in Qingdao is still in its growing phase, with rents in every sector on the rise and supply still limited. Capital values also show strong potential for further growth.

However, the market is still very much domestically driven, with international players having a limited presence in the city due to the central government's protectionism.

We foresee that over the next 2-3 years the market will experience a dramatic change in terms of quality and quantity. In the short-term, logistics will be the sector enjoying the best investment opportunities given the expansion of the market and increasing capacity of the port and airport facilities.

The office sector will also boast ample investment opportunities. The limited supply of high-quality office space and strong demand has made the office market the second most dynamic market in Qingdao. In 2006 prime yields were as high as 9-10% compared to 7-8% in other secondary cities.

The retail sector still needs some time to mature in many aspects, e.g. developers' development rationale, shopping centre management as well as international brands' penetration. In contrast, the residential sector enjoyed a boom in sale prices and rents from 2002 to 2005, but the market is more volatile and

is mostly driven by local developers, with an increasing price gap between different areas.

Qingdao has been performing well in both sectors, its position however, as a leading city in the Yellow Sea economic region is not yet strong enough. Furthermore, its catchment area is not as vast as that of Chengdu or Hangzhou, two cities in which the catchment area has been the main driver for both the retail and residential sectors. We expect a growing number of opportunities to arise for retailers in the retail sector and developers for residential sector over the next 5 years.

INVESTMENT TRENDS

Due to the relatively opaque market transparency and a constrained supply of quality space, transactions undertaken by international institutional investors are still very limited. Nevertheless, some international institutional investors and overseas Chinese developers, most of which are from Hong Kong, have established their presence in the market (e.g. the Carlyle Group and Sun Hung Kai. Most of the transactions to date in the office and retail sectors have been by local or domestic market players.

Shui On Property, for example, acquired a 100% interest in Blocks A and C, phase III of Central International Plaza, in Q1 2007 (now it has B as well). This project comprises an office tower, a mid-range residential block, and a three-storey retail podium with a total GFA of over 62,000 sq m. Shui On, which holds 50%, has completed this previously stalled development project at the end of 2007. The Printemps department store operator took over the 44,000 sq m Hisense Plaza in early 2007. These two major deals have contributed to the increased transparency of the real estate sector.

However, due to the limited supply, there are not enough high-quality projects available for investors. We believe, however, that with the further opening up of Qingdao and with the appearance of big international corporations, more investment class buildings will come on the market.

INDUSTRIAL/ LOGISTICS

Qingdao has all four types of economic development zones, namely the Qingdao Economic & Technological Development Zone (QDZ) in Huangdao, the Hi-Tech Industry Park based in Laoshan, the comparatively small Free Trade Zone (FTZ) within the QDZ, and the Export Processing Zone (EPZ) in Chengyang.

The Hi-Tech Industry Park has attracted many hi-tech and software companies such as the Lucent Global R&D centre which is one of Lucent's 9 main global R&D centres. The Export Processing Zone specializes in new material and mechanics industries and is now home to Tyco's second Qingdao facility.

Given that Qingdao relies heavily on the port for its development, it is not surprising that the QDZ, home to the Free Trade Zone, has become the focus of the government's industrial strategy. The port in the Free Trade Zone is China's largest ore terminal and crude oil port. A number of world-renowned shipping and logistics companies are operating their dock and logistics businesses along the coast. These include P&O, China Merchants Group, Maersk, Universal Container, Pan Asia and COSCO. Logistics relying on the port has been the most competitive sector in Qingdao.

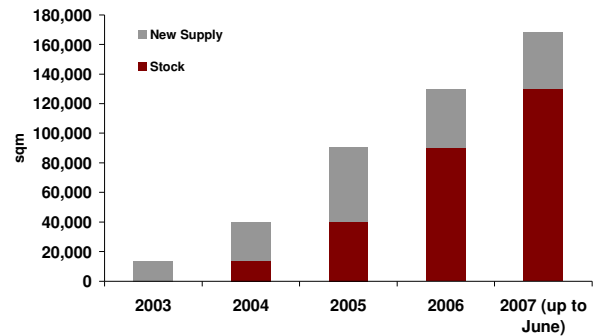
The city currently has a total of 168,300 sq m of high quality logistics space, of which 88% is located in the Free Trade Zone and 12% in the airport area.

Developers in the Free Trade Zone are mostly local companies such as China Merchants, Jinan Steel and Jin An Bang - all major developers of for-lease spaces. ProLogis is planning a 65,954 sq m project adjacent to the south bank of the port. Upon its completion in 2008 the project, comprising four warehouse buildings, will be the largest facility in the port area and also the first investment by a foreign developer. ProLogis has already developed another project in the Chengyang District, adjacent to the airport.

Currently, the occupancy rate in the port and airport areas is 91% and 100% respectively, indicating strong demand for transportation hubs. Tenants in the two areas are mainly logistics operators, including Kerry Logistics, Pantos Logistics, and Expeditors Logistics. A local cotton trader, Sai'er'ka, occupying over 30,000 sq m, is the largest tenant in the Free Trade Zone; Qingdao is in fact one of the largest textile export bases in China.

Looking forward, we believe that continuous growth in export volumes will keep demand for logistics space in Qingdao at a strong level, thus maintaining a stable volume of take-up over the next five years. Considering the tight supply in both the Free Trade Zone and airport area, rents will remain robust over the next 2-3 years.

Logistics Supply



Source: Jones Lang LaSalle Research

OFFICES



Qingdao's local Grade-A office market in the CBD is currently characterized by a basket of roughly 10 mature buildings, most of which are "strata titled". Indeed, all five buildings released in 2006 are strata-titled. By 2009, two international standard buildings, namely the IMC and Shangri-La Phase II, will have come on

the market. The IMC will be the tallest building in Shandong Province, and will set a new benchmark in Qingdao. Most importantly, it will be the first building in Qingdao with single ownership.

The limited supply over the next 2 years will put upward pressure on rents in Qingdao. It is noteworthy that the net effective rent in the market grew for 6 consecutive quarters, reaching USD 167/year in Q2 2007, a 14% increase on Q1 2007.

Shipping and logistics firms are the main occupiers in the market thanks to Qingdao's outstanding performance in the port and logistics sectors. Almost every big logistics and port player has a presence in the market and newcomers continue to arrive. One recent example is Toll Asia from Singapore, one of the leading integrated logistics companies in the Asia Pacific region.

With Qingdao gaining a leading role in the Shandong Province and even in the Bohai Bay Rim region, a growing number of financial and professional services firms have been keen to enter the market. E&Y, KPMG and PWC have set up operations as well as foreign banks such as BEA, HSBC, Mizuho Bank, and Standard & Chartered. Office demand has thus been generated by the aggressive expansion of banks, accounting firms, and management consultants who have been in the market for a while and are seeking to increase their presence in

high quality buildings with large blocks of space with potential expansion options.

The strong demand and limited supply of quality buildings has driven the vacancy rate down to 9.6% in the higher end buildings. Although some big tenants are not satisfied with the quality of the buildings and with the level of property management in particular, they are nevertheless choosing to occupy space early in this emerging hot city.

Looking forward, we are confident that demand in Qingdao is going to rise, particularly since the Qingdao municipal government is taking great pains to move up the value chain by developing the financial sector. Bank of East Asia, China Development Bank, Minsheng Bank, Mizuho Bank and Standard Chartered Bank and were all granted permission to set up Qingdao branches recently, meaning that more quality office building space will be taken up. The port expansion and dynamic logistics market will be other major drivers for Grade-A office demand.

With a small number of quality office buildings coming on the market by 2009, we estimate that some of the pent-up demand will be satisfied and that prestigious tenants will move to Shangri-La Phase II and the IMC Centre. This will put pressure on some of the relatively low quality buildings, although rents will remain stable due to the limited choice in the market. High quality office buildings will be seen to perform better than average.

The top 5 buildings currently on the market are:

Project Name	Asking Rent
QD Int'l Finance Centre	3.3 RMB/sqm/day gross
Crowne Plaza	8.0 RMB/sqm/day net inclusive
Cyberport	3.8 RMB/sqm/day gross
TOP Yi He International	4.0 RMB/sqm/day gross
Inter Royal	3.5 RMB/sqm/day gross

* Except for Crowne Plaza, all of these buildings are at least partially strata titled

HOTELS

The hotel sector, driven by tourism, exhibitions and the 2008 Olympics, is also booming.

At the end of last year, there were 6 five star hotels, 15 four star hotels and 63 three star hotels in Qingdao. In total, Qingdao has 17,000 rooms, making it the top city in Shandong province. Contrary to what one might expect, the size of the hotel market hasn't put pressure on the occupancy rate. This has been far higher than in other cities, averaging at 74%.

The strong performance of the sector is attributable to the vibrant tourism industry and prosperous exhibition activity in Qingdao.

The forthcoming 2008 Olympics, as well as the regeneration of the old downtown and creation of green spaces, has made Qingdao one of the most popular travel destinations in China. The number of domestic tourists grew by more than 10% y-o-y over the last 2 years, while that of foreign tourists grew by 25% y-o-y (15% above the national average). South Koreans form the largest group of tourists, accounting for 50%, followed by Japanese, Europeans and Americans. Not only is the number of tourists growing, the average length of their stay is also increasing. This was 3.6 days in 2006, up from only 2 days in 2002. Moreover, the government has plans aimed at increasing the average length of stay to 4 days by 2008, which should generate new demand.

International Arrivals in Qingdao 2006

Country	Number	y-o-y Growth rate (2005-2006)
Total International Arrivals	854,000	24.9%
Korea	374,000	26.1%
Japan	221,000	25.8%
Europe & America	98,800	44.5%

Source: Qingdao Statistics Website

In the exhibition sector, the best-known event is the China International Consumer Electronics Show (SINOCES). This is the most prominent international consumer electronics fair in the Asia-Pacific region, and is sponsored by the Ministry of Commerce, Ministry of Information Industry, Ministry of Science and Technology and the Shandong Provincial People's Government. In 2006, the prominent Consumer Electronics Show (CES), which is held annually in Las Vegas, selected SINOCES as its global strategic partner. This collaboration will attract more businessmen to Qingdao and will further raise the city's profile internationally.

The bright prospects have stimulated construction in the hotel sector. There are 11 five-star hotels and 5 four-star hotels under construction with total investment of USD 0.95 billion, a record in the hotel history of Qingdao. More than 3000 rooms will be added to the market in two years time.

Moreover, the arrival of new international hotel brands such as Hilton, Holiday Inn, InterContinental (at the site of the Olympics Sailing Marina), Kempinski and Sheraton will add fresh blood to the Qingdao hotel market, thus helping to enhance operational



standards and consolidating Qingdao's reputation as an international travel destination.

The booming market has also triggered the explosion of the budget hotel sector where the occupancy rate is 90% (20% above the national average). Jinjiang Inn, IBIS and Super 8 have all secured a market place in Qingdao.

It is very likely that the strong competition in the five-star sector will put downward pressure on room rents. This will however not happen until new supply comes on to the market around the time of the 2008 Olympics. The hotel sector in Qingdao is going to become increasingly specialised, with those able to capture a particular niche emerging as winners.

5* Hotel and International Arrivals Comparison

City	5* Hotel	No. of International Arrivals (000s)
Qingdao	6	850
Chengdu	8	580
Dalian	6	700
Hangzhou	10	1820

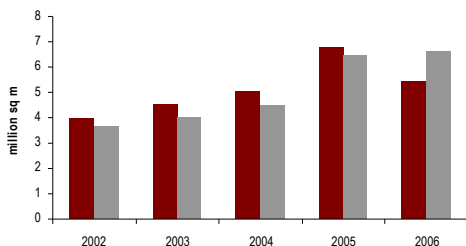
Source: Statistic Yearbook

Source: Jones Lang LaSalle Hotels

RESIDENTIAL

The residential market in Qingdao has seen healthy growth since 2002, with supply well matched to demand for four consecutive years. In 2006, however, supply decreased by about 20% while demand escalated and surpassed supply due to large-scale city regeneration. Demand is mainly driven by local inhabitants, accounting for 65-70% of total demand. Wealthy individuals from other parts of Shandong province are also important buyers and both parties buy mainly for their own use. Like other cities in China, capital appreciation has been significant with the average price rising from USD 258/sq m in 2002 to USD 920/sq m in 2007, i.e. at an annual rate of 20%.

Housing Supply and Demand



Source: Statistics Yearbook

However, in contrast to other secondary cities where numerous big-name Hong Kong and mainland Chinese developers are actively involved in the market, the residential market in Qingdao is dominated by famous local corporations. Haier, Hisense, Yizhong and Luneng, for example, all have extensive real estate arms.

The only big names in the market from outside Qingdao are Vanke and Hutchison Whampoa. Vanke entered the market in 2006 and developed a 400,000 sq m project in the Chengyang district, which benefits from Japanese and South Korean investments. Hutchison Whampoa became involved in a city-regeneration project in Xiao Gang Wan in early 2007. It is a complex project involving modern shopping and entertainment facilities as well as high-rise residential blocks with a total GFA of 1.1 million sq m. This project will transform Xiao Gang Wan into Qingdao's "Victoria Bay".



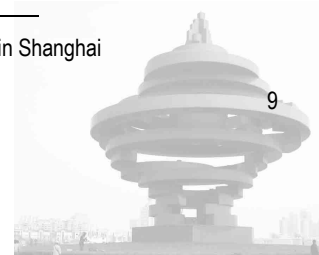
Donghai Road, parallel to Hong Kong Road in the Shinan District, has been the traditional middle-to-high-end residential area and continues to be the preferred residential location given its sea views and

proximity to the Olympics sailing venue. As stated above, local developers are the most active in the market and are involved in several high-end projects. Hisense, the largest among them, is currently working on two luxury apartment projects and one villa project.

The Laoshan District, with its stunning views, has always been the "She Mountain"³ of Qingdao, hosting many luxury villas. The average sales price in Laoshan recorded USD 1,580/ sq m at the end of 2006, with the investment yield hitting 10% in the peak tourist season. The favourable yield has induced numerous private investors to purchase villas in Laoshan.

Another feature of the Qingdao market is the price gap. The average price of projects along Donghai Road is about USD 1,580/ sq m, 200% higher than the average price. In No.9 Shandong Road, due to be completed by 2008, for example, the average sale price is expected to reach USD 3,550/ sq m. Even among the four urban districts, the price gap is obvious; in Shinan the average sales price is USD 1,400/ sq m whereas it is only USD 500/ sq m in Licang.

³ The most prestigious residential area in Shanghai

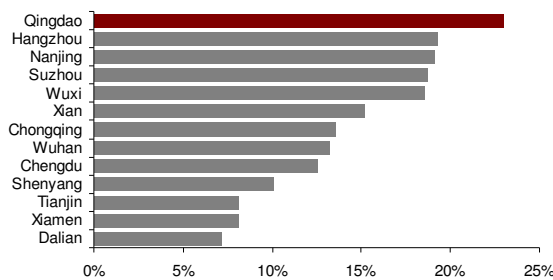


The market will continue to see price increases for high-end residential projects given the limited supply in the market and solid demand from wealthy individuals both locally and from across the country. Suburban areas will also witness rising prices as the city's regeneration process continues and as infrastructure improves.

RETAIL

The retail market is also booming despite its small size. The average growth rate of retail sales over the past 5 years has been 23%, far exceeding that in neighbouring city Dalian (7.3%).

Retail Sales Compounded Growth Rate Comparison (2000-2005)



Source: Jones Lang LaSalle Research

The lucrative market has been attracting a growing number of foreign players since 1998, when Jusco from Japan opened its first store in east Qingdao. Jusco was followed by Carrefour in 1999, also opening its first store in east Qingdao. The following 4-5 years saw the arrival of a number of foreign retailers including Metro and Wal-Mart, as well as the expansion of Jusco and Carrefour to additional locations. The overwhelming response of local residents contributed to the success of all these market players. Carrefour's first store in east Qingdao, for example, is hailed as the top store in China in terms of turnover.

The market was then quiet for several years, until 2007 when the Printemps department store took over Hisense department store, one of the two high-end department stores in Qingdao.

Despite the active penetration of foreign retailers in early years, the retail market remains dominated by Chinese players due to the government's protectionism. Out of the top 10 retailers in Qingdao in 2006, 7 were local players.



MyKal, owned by Dashang Group, the biggest retailer in Dalian, opened an 80,000 sq m shopping centre in east Qingdao in 2007. It targets white-collar workers in the Shinan district and provides an array of entertainment facilities

including a cinema on its top floor. Sunshine Department Store, another high-end department store in Qingdao, was developed by Sunshine Group from Jiangsu province.

In terms of new retail developments, Hisense, which has now become the biggest real estate developer in Qingdao, is planning to open the 60,000 sq m Hisense Olympic Plaza in 2008. Just to the south of Hisense Olympic Plaza, Marina City is now being constructed and will be complete by 2008. It is another trendy mid to high end and mixed-used project with a large scale retail component (retail GFA 100,000 sq m) surrounding the Olympics Sailing Marina. Looking down to Hong Kong Road, a 27,000 sq m and 16,000 sq m retail podium is also being developed by a JV between IMC (Qingdao) Development Co. and Qingdao Chengji Property Development Co, and Capland Property Group Ltd. and the Carlyle Group, respectively. This high level of retail development activity will further enhance east Qingdao's reputation as a business district and higher-positioned retail catchment.

With the different market positioning of its department stores, the increasing spending power of local residents and Qingdao's influence on the nearby cities, Qingdao's retail future is bright.

Top Ten Retailers' Retail Sales in 2006

Rank	Retailers	Retail Sales (Million RMB)	Local or Foreign
1	Li Qun Group	602	Local
2	Weekly Group	258	Local
3	Jusco	194	Foreign
4	North Trade	145	Local
5	Li Ke Lai	130	Local
6	Carrefour	111	Foreign
7	Guo Mao	102	Local
8	Parkson	80	Foreign
9	Hisense	55	Local
10	Hualian	46	Local

Source: Statistics Book



CLOSING THOUGHTS

Qingdao is regarded as:

- A 'Gold Medal City' for its business environment (World Bank, 2006)
- One of China's 'Top 10 Business Destinations' (Fortune Magazine –Chinese version, 2004 and 2005)
- One of China's 'Top 10 Economically Dynamic Cities' (China Central Television, 2004)
- The city with best 'Entrepreneur Satisfaction' (China Central Television, 2004)
- One of China's 'Top 10 Habitable Cities' (Horizon Group, 2006)
- One of Asia's Most Efficient and Least Costly Cities to Do Export Business (World Bank, 2006)

The city stands for much more than just beer and beaches. Its strategic location and solid industrial base has been a major draw for investors, with the 2008 Olympics further enhancing the city's image. Investors are increasingly rushing to the market, hoping to capture their share of the booming economy and real estate sector. However, it still remains unclear which direction Qingdao will go after the 2008 Olympics. Will it maintain its strong position as a bustling and vibrant city, or will the growth rate decrease because of the intensive investment that took place before 2008?

Jones Lang LaSalle believes that, with its solid industrial base and inherent locational advantage, and benefiting from the far-reaching urban planning in Shandong Province, Qingdao will emerge as the key city in the Bohai Bay region. As long as the Qingdao municipal government stays committed to moving up the value chain, improving market transparency, and accepting international players' involvement in the market, Qingdao has great potential for competing with other cities in Bohai Bay, and should quickly become an increasingly important pole in the region.

Moreover, in the real estate sector, the logistics sector will continue to see rapid increases after 2008, benefiting from the maturing of the market mechanism and economies of scale. The office and retail sectors are also on a fast track, driven by the growing presence of international players. As for the residential sector, this will see some price adjustment in the future.



DEFINITION OF TERMS

ECONOMIC DASHBOARD

Population: Population refers to the total population as at 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-half year.

Chongqing's population refers to 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 2000–2006

GDP Growth: Refers to the annual GDP growth rate over the five-year period from 2000 to 2006.

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

FDI: Foreign direct investment refers to investments 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/Capita: Refers to 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: Refers to the number of higher education institutions providing 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 the 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 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, 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 department stores in Qingdao.

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

Office Construction Grade A: Include IMC 87,500 sq m office and 22,700 sq m office space from Shangri-La phase II. Both of the above two buildings are scheduled to complete Q1-Q2 2009, and is single-ownership building.

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

Benchmark Rents: Refer to the typical open-market rents (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: Refers to net effective rents excluding management fees.

Industrial Rents: Refer to rents of pre-built business parks

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. 9%-10% is calculated by Grade-A offices in Shinan CBD.





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