CUSHMAN & WAKEFIELD | #MARKETBEAT

Q2 | 2018

Commercial Real Estate - Russia

#MARKETBEAT

Cushman & Wakefield Research Department

Jul '18

Macroreview | Capital Markets | Office

Retail | Warehouse & Industrial | Hospitality & Tourism

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Outlook

1 500 000 OF FAN IDs

were issued for the football fans visiting FIFA World Cup 2018 including 600 000 received by foreigners.

BRIEFING: FORGET ABOUT THE ECONOMY

Social and political events drove back the economy. Summer 2018 will be the most intensive in the history.

Despite lower business activity many noticeable events occurred during the spring and summer 2018.

FIFA World Cup 2018 was a strong driver for retail in general and street retail, in particular, in Moscow and other cities. After the Word Cup we will see decrease of retail sales, but positive impact on the consumer culture in large cities will be prolonged.

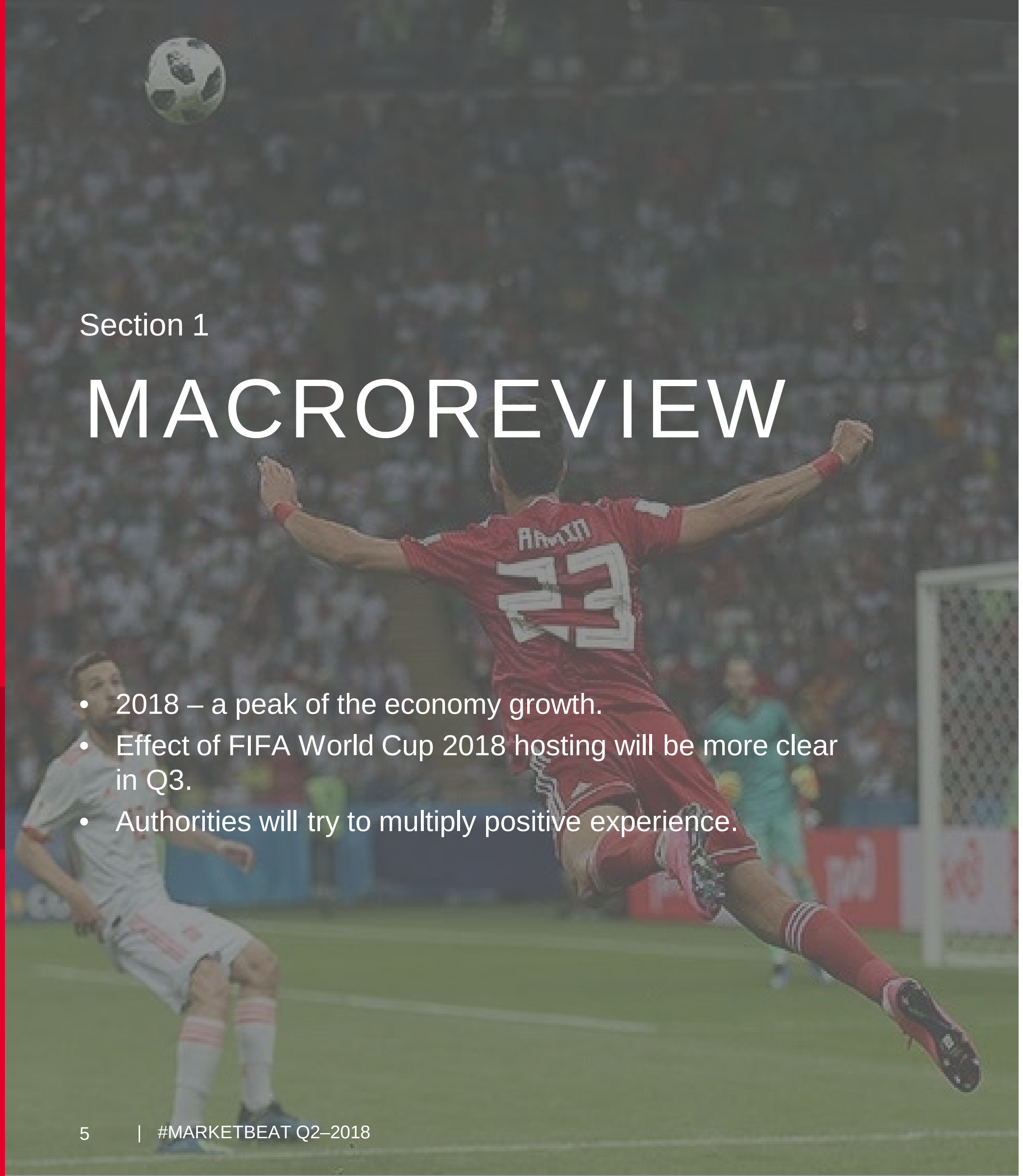
Recent macro indicators and forecasts are divergent. Against the background of relatively high real wages in 2018 we expect growth rate of disposable income to be close to zero next year. The Ministry of Economic Development predicts decrease of the economy growth rate in 2019-2020 after promising results of 2018. Consequently, start of a new real estate cycle is postponed to 2022-2024.

Optimistic forecasts of oil prices will prevent the economy recession, but are not enough for driving growth.

As we predicted a year ago, the tax pressure is increasing. VAT is raised up to 20%. This will not lead to immediate effect, but will counteract effects of the economy growth stimulating.

Potential increase of the retirement age should be considered as a form of taxation. Currently 40 mn of retirees receive guaranteed monthly income from the government and are considered one of target groups for modern retail. Drastic increase of the retirement age will lead to shrinkage of this group and radical changes on the consumer market. Mass market retail chains and discounters will have to change strategies.

14/06-15/07	World Cup FIFA 2018
17-22/07	Moscow Urban Forum
16/06	Draft law on VAT increase up to 20% (has passed the second reading on July,18)
16/06	Draft law on the retirement age increase (pending until autumn)
16/07	Putin and Trump meeting
9/08	Moscow mayoral election



Section 1

MACROREVIEW

- 2018 – a peak of the economy growth.
- Effect of FIFA World Cup 2018 hosting will be more clear in Q3.
- Authorities will try to multiply positive experience.

MACRO INDICATORS

	2017	2018	2019	2020	2021
GDP growth, %	1.6	**1.8**	1.3	1.2	1.2
RUB/USD	58.3	**60.5**	60.7	60.7	60.8
CPI, %	3.7	**2.9**	4.0	4.0	4.0
Interest rate	10.55	**8.75**	8.18	8.11	8.12
Current Balance, % of GDP	1.5	**0.8**	0.9	0.3	0.2
Private consumption, %	3.3	**3.2**	2.6	2.3	2.0
Government spending	0.4	**0.5**	0.5	0.7	0.8
Capital outflow, bn USD	12.28	**-121**	-122	-94	-81
Unemployment rate, %	5.20	**5.10**	5.21	5.14	5.09
BRENT crude oil price	54.2	**75.2**	77	-	-

Source: Oxford Economics 06/07/2018

2018 IS THE BEST YEAR OF THE PREVIOUS FIVE

Despite the negative background, 2018 demonstrates more optimistic indicators compared to the previous years and a short-term forecast. The effect of the FIFA World Cup 2018 will also influence the final figures. Most likely, 2019 is to be relatively worse.

1.8 %

GDP Growth forecast for 2018

Oxford Economics

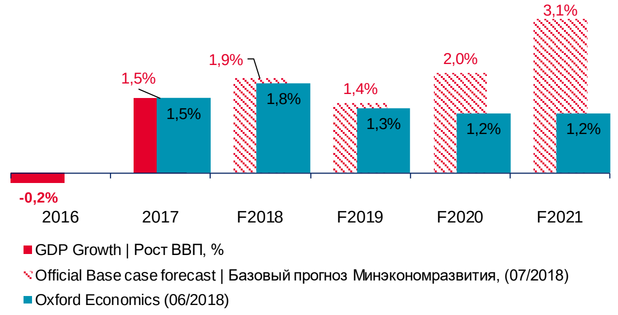
20 %

VAT

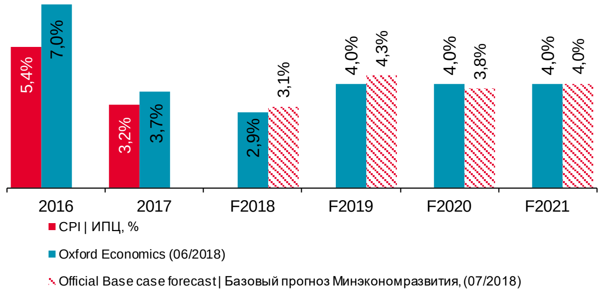
From January 2019

Rosstat

GDP Growth, %



The Consumer Price Index, %



A new release of the forecast of the Ministry of Economic Development in July 2018 demonstrates significant difference between official position of the ministry and the consensus opinions on the market. The ministry doesn't see a scenario for development of the Russian economy in the short-term (2018-2019), but it is expected that Russia will reach the growth rates exceeding the world average by 2021.

On the contrary, international experts tend towards the damping development trend of the Russian economy.

For the real estate market, it makes sense to take the positive forecast of the Ministry of Economic Development as a basic scenario. This will give the opportunity to be better prepared for changes.

In the scenario of sluggishly damping development trend in the economy, the real estate market will stay at the bottom of the cycle for unpredictably long period.

Outlook

RETIREMENT AGE INCREASE IS A NEW SOCIAL CONTRACT

Starting from the next year increase of the retirement age will start influencing consumer behavior.

CONSUMER MARKET BOOMING 2.0

In 2018, we see a rapid growth of households' debts. Most likely consumers are compensating decrease of real income by credits.

8.5 %

Growth of Russian Households Debt

Jan-May 2018

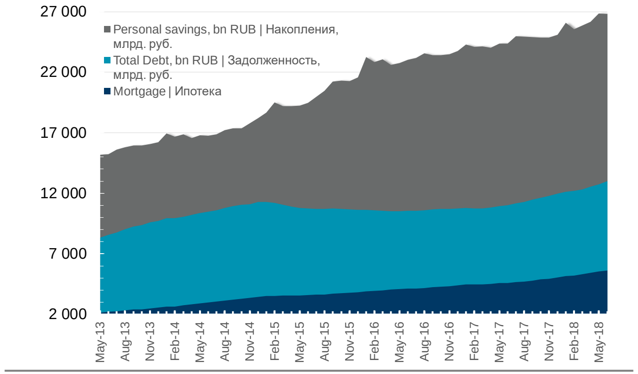
2.5 %

Growth of Consumer Credits

May 2018

Source: Central Bark, Cushman & Wakefield calculations

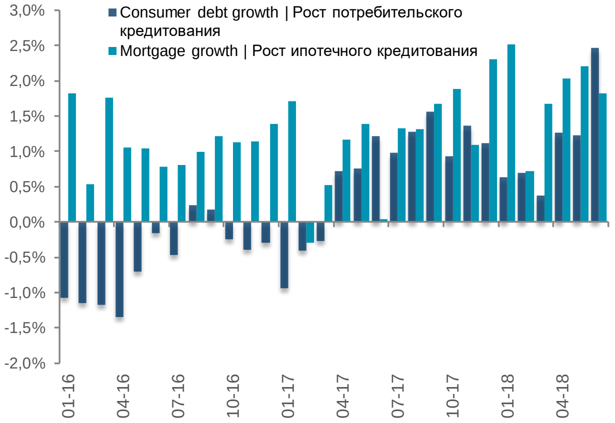
Shares and deposits (of physical persons), bn RUB



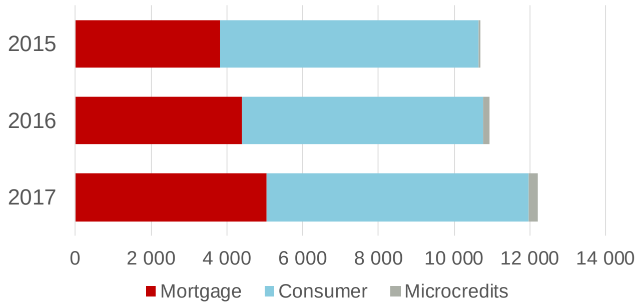
In May, household debts showed a rapid growth. Unlike previous periods, consumer credits demonstrated even higher growth rate than mortgage loans.

We expect high retail turnovers in June and July partly driven by FIFA World Cup.

Growth Rate of Household Debt



Household debt structure, bn RUB



#MARKETBEAT

CORPORATE DEBT

Lending started active recovery in March, however already in May this growth stopped, and within the retail market the lending began to shrink again. This was unexpectable since we assumed that retailers and distributors would prepare the stocks before the FIFA World Cup 2018.

7.25 %

Key Rate

No changes

21.6 %

Overdue Debt

In Real Estate sector

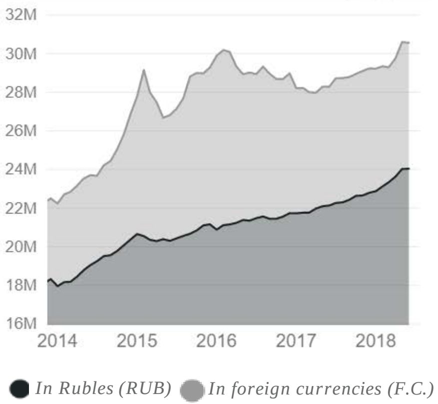
Source: The Central Bank of Russia

The spring was generally positive for lending. Overdue debt in the most problematic segments (construction and real estate) showed a slight decrease against the background of positive dynamics of corporate debt in March and April.

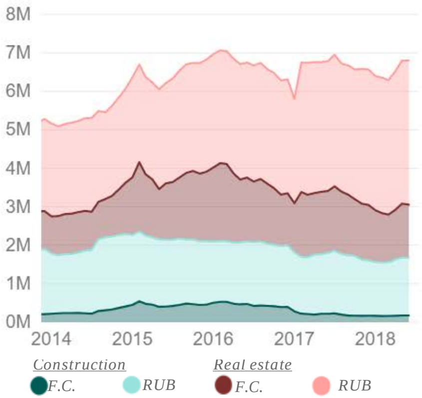
We expect that in summer the growth of lending to consumption sector will accelerate due to the influx of tourists. This will smooth the traditional summer downturn of consumer activity.

Corporate debt and overdue debt

Total debt, mn RUB



Construction and real estate, mn RUB



Overdue debt

PUBLIC RETAIL AND DEVELOPMENT COMPANIES

Stock Market Indicators from 10/04/18 to 10/07/2018 as compared to the MICEX index

+10.2 %

PIK

The growth leader over the past 90 days

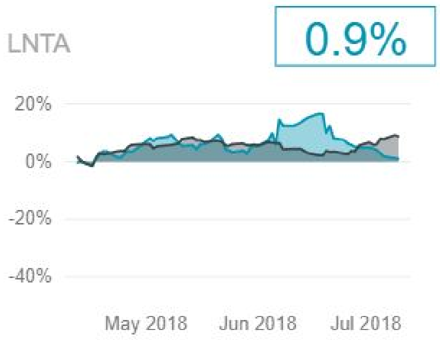
-21.6 %

Sistema Hals

The largest fall for the period of 90 days

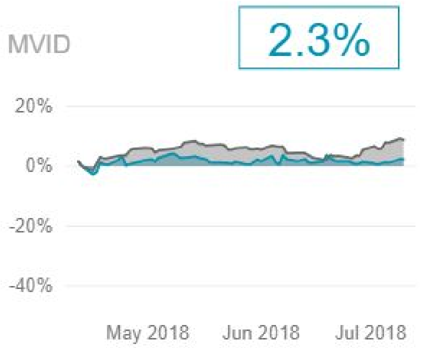
Source: MICEX, Yahoo Finance

Lenta



Magnit

M.video



PIK

Sistema Hals

LSR Group

Section 2

CAPITAL MARKETS

- A slow start in 2018.
- Decline of the capitalization rate will slowdown due to the weakening of the ruble.
- In 2018 we expect to see large transactions.

480 mn EUR
Total investment volume in Russia
In H1 2017

4.0 bn EUR
Total investment volume in Russia
Forecast for 2018

9.5 %
Capitalization rate, prime office segment
H1 2018

-11 %
Investment volume decline
In 2018

Capital Markets

THE CAPITALIZATION RATE REMAINED UNCHANGED, INVESTMENT VOLUME FORECAST DECREASED BY 11%

We except several large deals to be closed in H2 2018.

EASTERN EUROPEAN INVESTMENT IN COMMERCIAL REAL ESTATE

Poland retains its position as the strongest investment market in the region. In H1 2018, Poland's share of the total recorded investment accounted for 52% of all investments in the commercial real estate across Eastern Europe.

-24 %

Investments in Central and Eastern Europe

Decrease compared to H1 2017

3.7 bn EUR

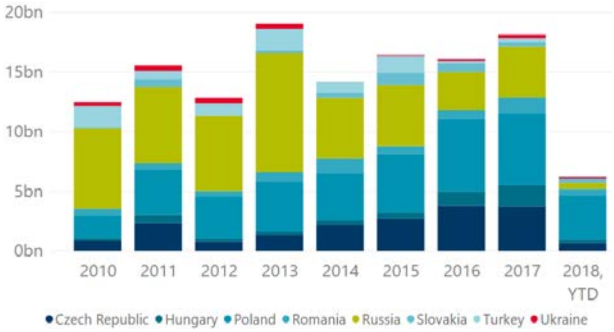
Investment volume in Poland

The largest investment market in CEE region in H1 2018

REAL CAPITAL ANALYTICS

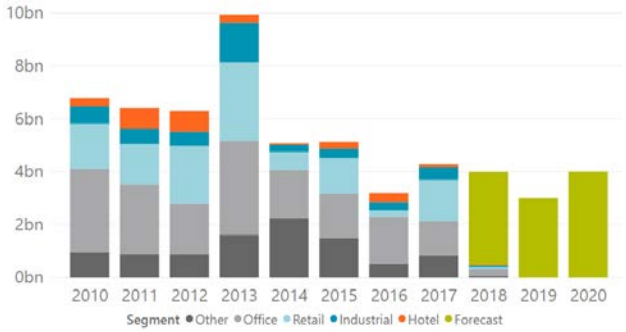
Source: Real Capital Analytics

Investments on the core CEE markets, bn EUR



In 2018 the investment market in Eastern Europe continues to show disappointingly low volumes. Total investment in the commercial real estate as of the end of H1 2018 was approximately seven billion euros. More than half of this volume are attributed to Poland that retained its position as the country with the largest investment market in the region.

Investments in Russia, bn EUR



The Russian investment market has experienced a slow year start. We revised the previous yearly investment forecast of 4.5 bn EUR.

Given that in the first half of the year the investment volume was less than 500 mn EUR and that currently there is series of large transactions in a preparation stage, we expect that the investment volume will reach 4 mn EUR by the end of the year.

CAPITALIZATION RATES

9.5 %

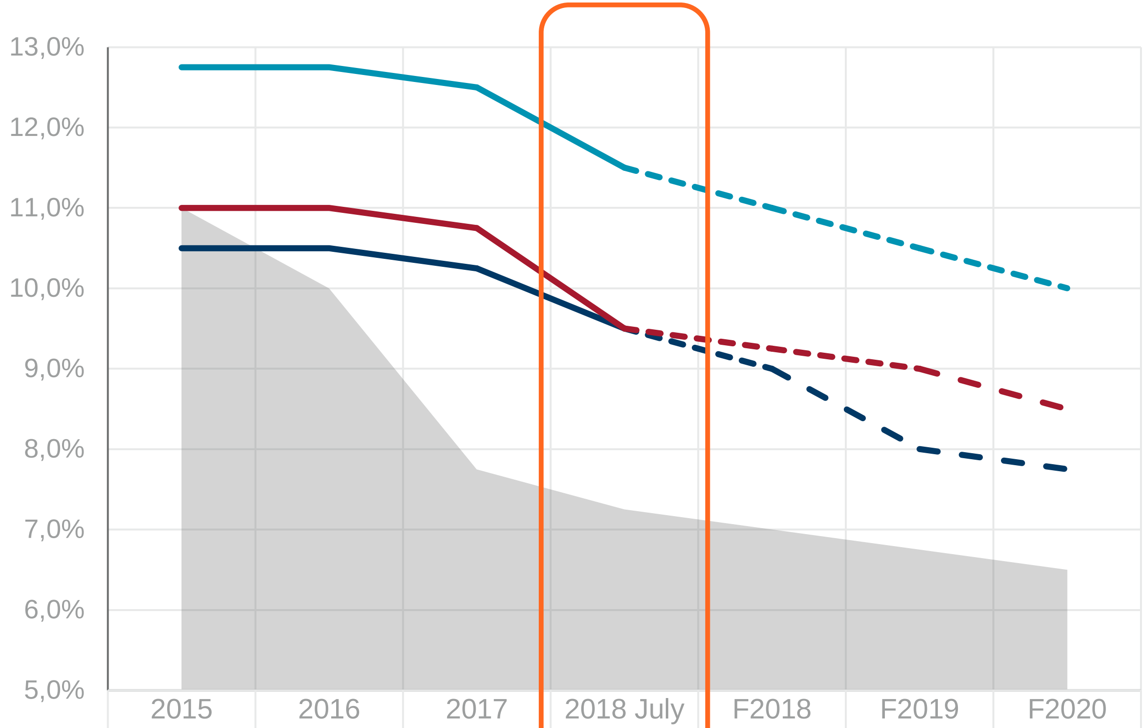
Office

Capitalization rate, Jul 18

7.25 %

The key rate

The Central Bank of Russia



	2015	2016	2017	2018 July	F2018	F2019	F2020
Central Bank Key Rate	11,00%	10,00%	7,75%	7,25%	7,00%	6,75%	6,50%
Office	10,50%	10,50%	10,25%	9,50%	9,00%	8,00%	7,75%
Shopping Centers	11,00%	11,00%	10,75%	9,50%	9,25%	9,00%	8,50%
Warehouse	12,75%	12,75%	12,50%	11,50%	11,00%	10,50%	10,00%

INVESTMENT STRUCTURE

Foreign investment continues to account for a relatively small share on the Russian market. This situation is expected to keep unchanged in the upcoming years.

72 %

The share of foreign investments

The Central and Eastern Europe, H1 2018

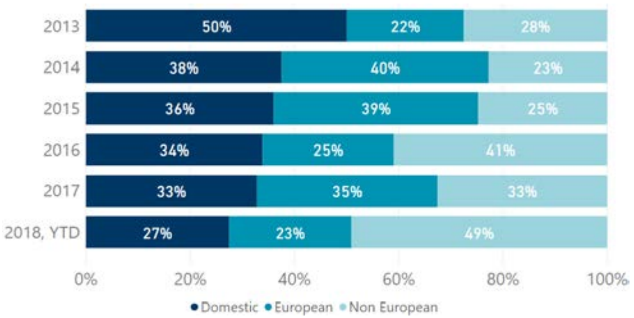
24 %

The share of foreign investments

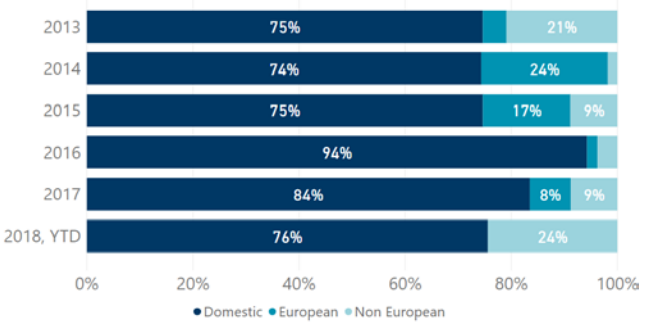
Russia, H1 2018

Source: Real Capital Analytics

The Central and Eastern Europe



Russia



Investments in Eastern Europe is relatively evenly distributed, with similarly-sized shares originating from within the domestic market, as well as from both regional (European) and external sources (The United States, Asia, Africa etc.). In 2018, the share of Non European investments increased. From a broader perspective, as the market continues to open itself up to new participants, it is the external investment market that shows the most positive signs of growth.

The Russian market continues to be dominated by domestic investors. This situation has been observed since 2009, whereas prior to 2009, particularly between the years of 2004 and 2007, European investors represented the majority of market players.

We predict that the share of international investment in the Russian market in the upcoming years will not exceed 20%, until the market becomes more open to international capital.

Section 2

OFFICES

- All indicators of the office market show positive dynamics despite the overall negative background.
- Despite the volatility of the economy, the market reached equilibrium and this year will show a slight increase.

Moscow H1 2018

Classes **A**, **B+** & **B-**

16.99 mn sq. m

Total stock of office buildings 09/07/2018

41 ‘000 sq. m

Construction

144 ‘000 sq. m

Net absorption

950 ‘000 sq. m

Take-up

Offices

MARKET RECOVERY

All indicators of the office real estate market are improving. Significant growth in demand and rental rates in Class A is evident.

NEW SUPPLY

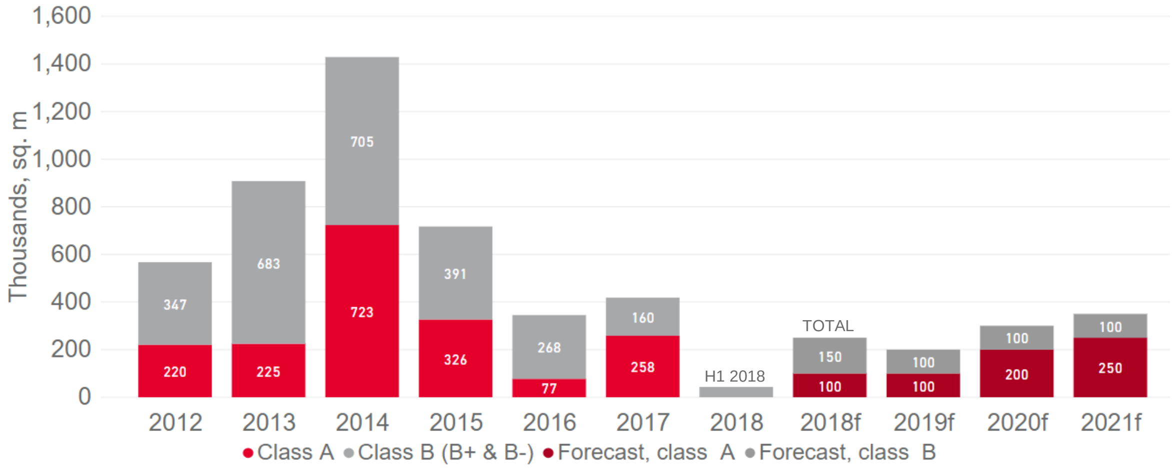
Delivery of the majority of new buildings is postponed by the end of the year. In 2018, 250,000 sq. m will be delivered to the market. In 2019, construction activity will remain low.

In Q2 2018 only one business center was delivered to the market - MFC Nikolin Park, which is located in the New Moscow area (2,310 sq. m).

Despite the fact that new construction in H1 2018 almost doubled the indicator of the last year (41,000 sq. m and 23,000 sq. m, respectively), by the end of 2018 new construction will reach only 250,000 sq. m, which is 40% lower than last year. Rentable area of almost all new buildings will not exceed 20,000 sq. m, except for one property with rentable area 70,000 sq. m.

In the period of 2019-2021, the share of class A in new supply will be growing, while new deliveries in Class B will be most likely properties after redevelopment / reconstruction.

New construction, class A and B



DEMAND

The activity of tenants is at a record high of 2017.

950

'000 sq. m

Take-up (lease and sale deals)

H1 2018

1,850

'000 sq. m

Take-up (lease and sale deals)

Forecast: 2018

Demand structure remains the same to previous quarter – 15% of take-up was carried out through lease of big blocks in business centers (>5,000 sq. m deals).
The most active industries in H1 2018 by number of deals were Banks and Finance (20%), Wholesale trade and Retail (14%), IT and Computers (13%), FMCG (10%).

Major deals in H1 2018

COMPANY	*AREA, SQ.M*	*PROPERTY*	*CLASS / SUBMARKET*
Aeroflot	*18 447 sq. m*	*Arbat 1*	*A / Downtown*
Transneft Technologies	*12 666 sq. m*	*VEB Arena*	*B+ / Central*
OZON	*11 221 sq. m*	*Towers on Naberezhnaya*	*A / CTY*
X5	*9 701 sq. m*	*Oasis*	*A / Central*
Lamoda	*7 061 sq. m*	*Zhukov 1*	*B+ / OTA*
School 42	*4 890 sq. m*	*Factoria*	*B+ / Central*

In recent years the demand for office space in Class A has grown. In 2011-2014 average annual take-up in this class was 350,000 sq. m, and in 2015-2017 - about 550,000 sq.m. Tenants have taken advantage of recent opportunities associated with loyal rental conditions for the most high-quality premises. In Q2 2018, the demand for the prime segment increased significantly. Many small blocks in the most expensive buildings of Moscow were leased out.

We expect a slight decline in demand in 2019 due to the governmental decisions to increase the tax burden on businesses and conservative forecasts of the economy in general. In 2020, demand will again reach the level of 2017.

ABSORPTION RETURNS TO THE POSITIVE ZONE

Absorption remains positive since the end of 2017. Against the background of low construction activity and high demand, additional premises are taken off the market.

144

'000 sq. m

Absorption in H1 2018

41

'000 sq. m

New construction in H1 2018

Source: Cushman & Wakefield

Absorption and new construction

Absorption by class

Absorption is an indicator that reflects the difference between the area occupied at the beginning and at the end of the period. *Positive absorption* means that additional vacant office premises are "selected" from the market. *Negative absorption* reflects the opposite - the release of additional office space, which together with new construction leads to vacancy.

VACANT OFFICE PREMISES

The vacancy rate (in Classes A, B + and B-) decreased by 0.3 percentage points to 11.6% and will remain at this level throughout the year.

11.6 %

Vacancy rate by the results of Q2 2018

Classes A and B (B+ & B-)

1.97 mn sq. m

Vacant premises by the results of Q2 2018

Classes A and B (B+ & B-)

Source: Cushman & Wakefield

Vacancy rates

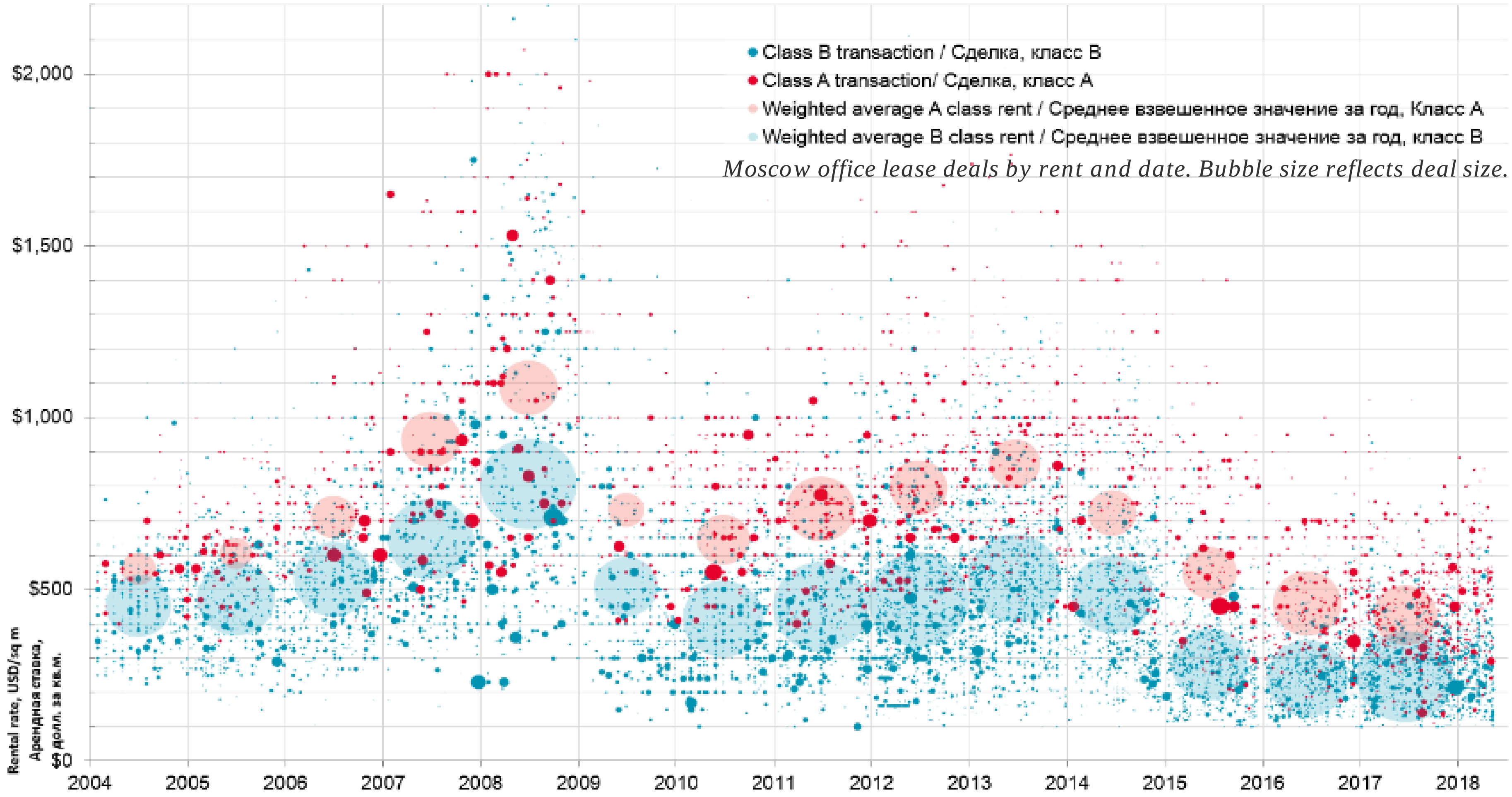
Due to a new record low figure in new construction and high take-up, the vacancy rate continued declining from the last year. At the end of H1 2018 the indicator amounted to 11.6% (12.2% in 2017).

The share of vacant premises in Class A declined from 17.3% in H1 2017 to 14.0% in H1 2018. At the same time, the vacancy rate in Class B remains almost unchanged, during the last year only a slight decrease occurred from 11.3% to 10.9%.

Vacant premises

The vacancy rate in the center of Moscow (within the boundaries of the TTR) remains stable over the last year - about 10%, while the average vacancy rate outside the TTR remains at the level of 15%. The vacancy rate in New Moscow is 30%.

LEASE DEALS IN MOSCOW



Moscow office lease deals by rent and date. Bubble size reflects deal size.

RENTAL RATES

Forecast: gradual increase of rental rates.

324

USD / sq. m annum

July 2018

Dollar equivalent (all deals in classes A and B)

19,408

RUB / sq. m annum

July 2018

Ruble equivalent (all deals in classes A and B)

Source: Cushman & Wakefield

Rental rates in US dollars

The average dollar equivalent of rental rates in Class A in H1 2018 is 486 USD/ sq. m/year (29,117 Rubles/ sq. m/year).

The average dollar equivalent of rental rates in Class B is 15,537 Rubles/ sq. m/year (259 USD/ sq. m/year).

Rental rates in Russian rubles

Despite the volatility of the economy and geopolitical factors, we expect that the average rental rate will continue to increase in the coming years, mainly through Class A, due to taking off the market high-quality supply and low pace of new construction.

RENTAL RATES

The share of deals in buildings with USD nominated rental rates in H1 2018 is about 10% on average, which slightly exceeded the indicator of 2017 - 7%. In Class A, this share is higher and in 2017 – 2018 is amounted to 20-25%.

10.0 %

Share of USD deals

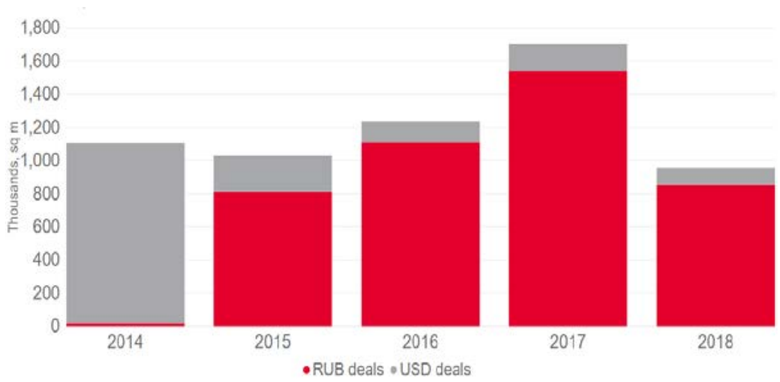
Classes A and B (B+ & B-)

Source: Cushman & Wakefield

Leasing demand and rental rates

Class	Deal currency	Deals volume, sq. m	Rate
A	USD	89,082	$602
	RUB	177,809	25,942 rubles
B+ & B-	USD	7,450	$476
	RUB	664,491	15,338 rubles

Leasing demand and rental rates



Section 2

RETAIL

- The consumer market recovery is slower than expected. Long-term forecast for indicators of the consumer market was revised downwards. Further corrections can be expected in 2019.
- New construction reached the minimum. The development cycle is getting longer.
- Half of the retail space planned for delivery in 2018-2019 in Russia is located in Moscow and other cities with population of more than one million people.

5.2 mn sq. m

Total quality stock in Moscow

In quality shopping centers, mixed-use buildings, outlets, and retail parks

90 ‘000 sq. m

New construction, Moscow, H1 2018

Retail properties with GLA of more than 15,000 sq. m

9.5 %

Vacancy rate

Quality shopping centers, Moscow

155 ‘000 RUB / sq. m

Prime rental rate indicator

Base asking rental rate for a 100 sq. m gallery unit on the ground floor of a prime shopping center

INFLUENCE OF LEGISLATIVE INITIATIVES

New legislative initiatives will have a negative influence on retail and consumer market.

VAT

20%

The rise of VAT from 18% to 20% will lead to increase of prices. Considering low pace of household income growth, in the mid-term this will lead to review of a structure of spending, consumers will come back to the saving pattern. Spending volume will remain the same while number of purchased goods will be smaller, consumers will be looking for the most favorable offers and discounts. In addition, it is possible that the demand for unauthorized trading will increase. Currently, retail chains are one third of the total retail turnover. It is likely that this share will be decreasing.

Retiring age

63-65 years

The draft law which caused a stormy reaction of the society, will affect the retail market in several years. Currently, retired people are the target audience of the modern retail. They are a socially active group which has a small but stable and guaranteed income, and access to credit resources. Also, they receive an additional income - many retirees work a few years after retirement and get a salary. If the law is adopted, by the time of retirement, people will have less opportunities to continue working. On the other side, they will lose governmental support in the previous years and won't be active consumers.

Cross-border online purchases

€200

Restrictions for Russian people on purchases in foreign online-shops have been actively discussed for several years. Several aspects were discussed: maximum duty-free cost of purchase, possible taxes on all purchases and timing of new rules' implementation. In April 2018, the Ministry of Finance initiated the public discussion of a new version of the draft law. According to this document, maximum tax-free purchase is 200 EUR per month (will be decreasing gradually).

The main purpose of this initiative is to support domestic producers and retailers. But the effect of these measures to stimulate the economy growth and retail segment will be insignificant – currently the volume of purchases in foreign online-shops is not more than 2% of the total retail turnover in Russia.

CONSUMER MARKET IS UNDER PRESSURE

Despite the positive forecast of the main indicators of the consumer market for 2018, next year consumer activity will decrease because of significant slowdown of disposable income growth, prices increase after VAT rate rise, and general downturn of economic growth.

Forecast for 2018

2.0 %

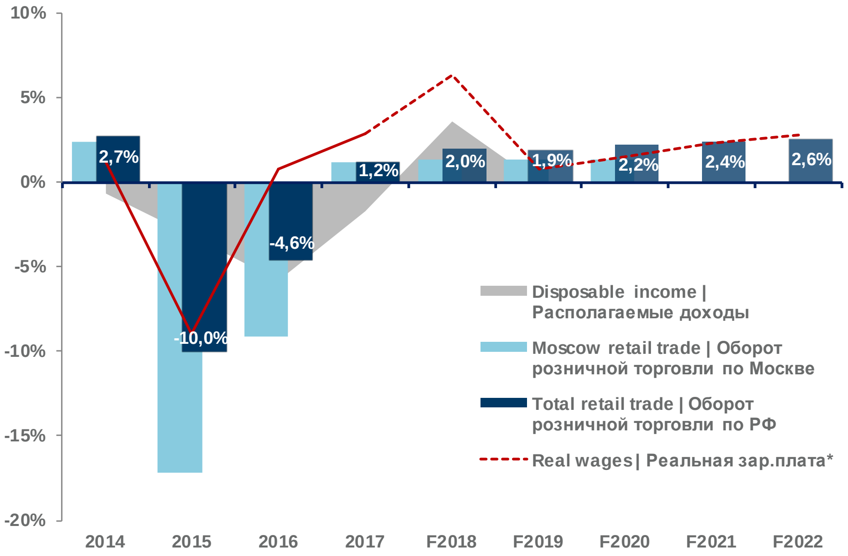
Retail turnover growth

3.4-3.9 %

Disposable income growth

Source: The Ministry of Economic Development

Consumer market indicators



Source: The Ministry of Economic Development

* In the revised forecast as of July 2018, the Ministry of Economic Development introduced a new indicator – “Real wages” instead of “Disposable Income” that was published before.

According to the latest edition of the forecast of the Ministry of Economic Development, as well as to the report of Maxim Oreshkin, real disposable income forecast was revised upwards in 2018. Mainly due to pre-election programs of indexing of the wages of government workers and military service (for instance, average nominal wage in public sector is to grow by 13% year-on-year in 2018) the level of real disposable income will show increase for the first time in the last 5 years. This growth will be noticeable, however not prolonged. In 2019, we will see a failure in real wages and therefore in disposable income.

New revised forecast of the retail turnover is more conservative. Considering the forecast of the real wages, it is likely that the figures will be lowered in the next revision in Autumn 2018.

Retail

DEVELOPMENT CYCLE IS GETTING LONGER

Almost half of the projects that are planned for delivery next year, have been in the development process for more than 5 years. Not all of them will be completed on schedule and will be postponed again.

THE MARKET IS IN THE PROCESS OF SELF-ADJUSTMENT

Three years of the consumer market compression together with lack of credit financing to retail segment and shrinkage of expansion plans of retailers have resulted in a new record low volume of new construction.

173

‘000 sq. m

New construction, H1 2018

Russia (including Moscow)

350

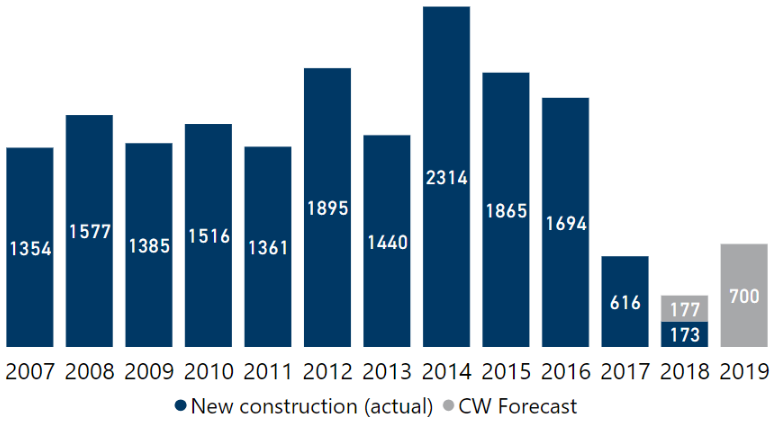
‘000 sq. m

New construction, 2018F

Russia (including Moscow)

Source: Cushman & Wakefield

New construction in Russia (including Moscow), ‘000 sq. m



Source: Cushman & Wakefield

In H1 2018, 6 shopping centers with total GLA of 173,000 sq. m were opened in Russia.

Many projects that were planned for delivery in 2018 were moved to the next year, so the new construction forecast was revised downwards. In 2018, we expect around 350,000 sq. m of quality retail space to be delivered to the market instead of 500,000 sq. m in the previous forecast.

The largest shopping center of 2018 is Kashirskaya Plaza (GLA 71,000 sq. m) that was opened in Moscow in Q2. No other large-scale retail schemes are expected this year.

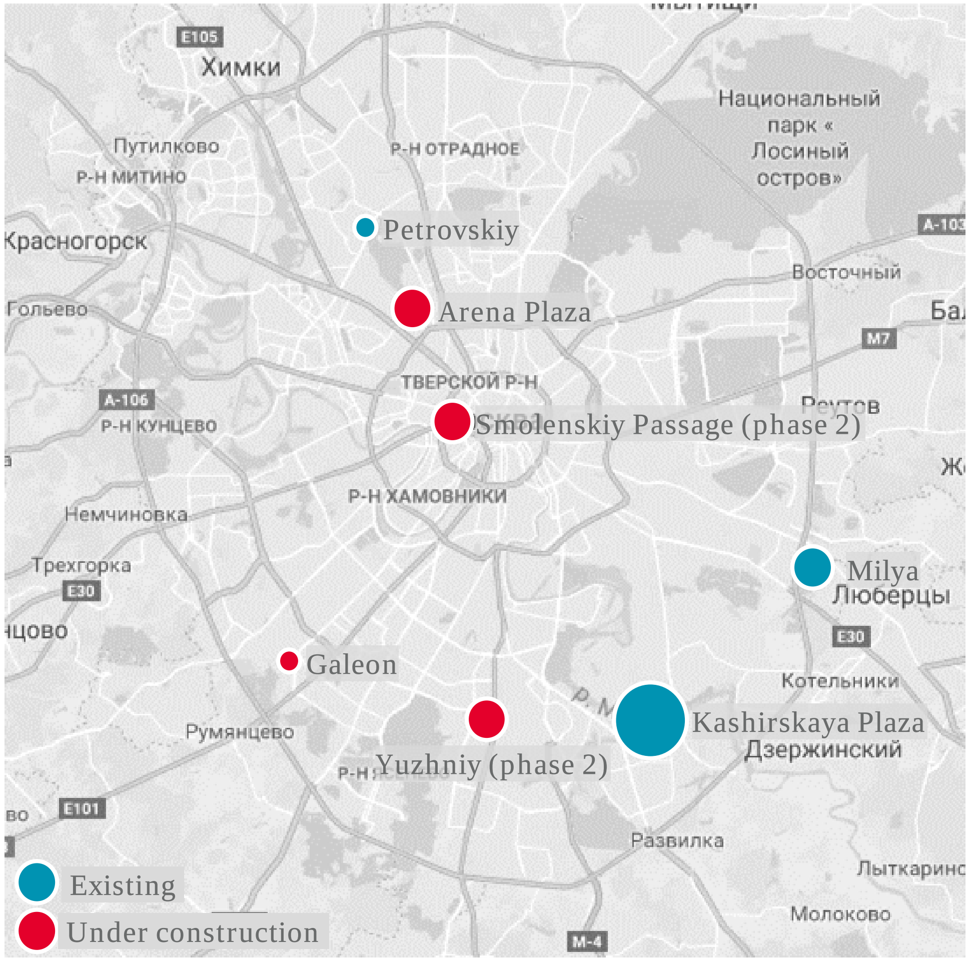
The revival of construction activity to the level of the last year is expected in 2019 – several large-scale projects are planned for opening both in Moscow and other cities.

ALMOST HALF OF RETAIL SPACE UNDER CONSTRUCTION IS LOCATED IN THE CITIES WITH 1+ MN INHABITANTS

Traditionally, the highest construction activity is concentrated in Moscow – 43% of the retail space planned for delivery in 2018-2019 among cities with population of more than one million inhabitants.

Names of the cities with new construction volume of more than 100,000 sq. m of retail space are highlighted on the map.

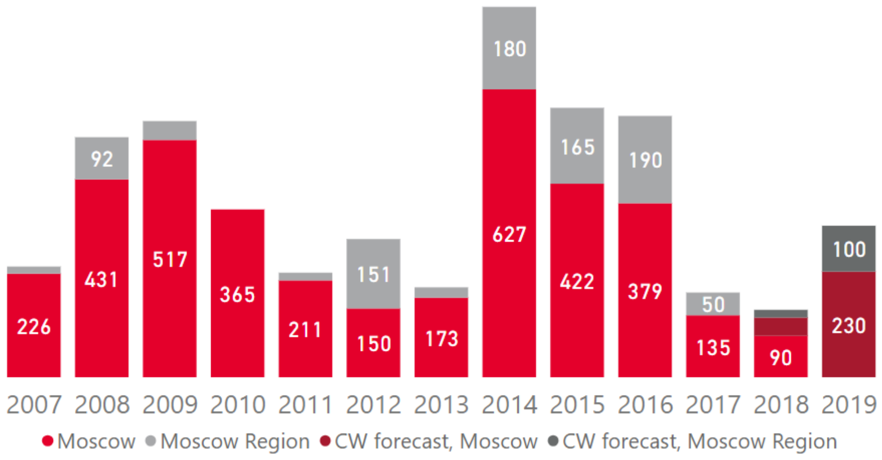
Shopping centers opened in H1 2018 and planned for delivery in 2018 in Moscow



Retail

NEW CONSTRUCTION IN MOSCOW

New construction in Moscow and Moscow region, ‘000 sq. m



Construction activity in Moscow remains low and can be compared to the level of the last year – around 130,000 sq. m of quality retail space is expected to be delivered to the market in 2018.

Next year, together with the opening of such large-scale properties as Salaris (GLA 105,000 sq. m) and retail part of Ostrov Mechty entertainment park (GLA 70,000 sq. m) new construction will reach 230,000 sq. m.

CHANGING CONSUMER STIMULATES THE DEVELOPMENT OF NEW RETAIL FORMATS

Shopping centers and operators are targeted to the generation of millennials which are focused on getting new emotions and experience.

NEWCOMMERS, H1 2018

COACH

KARL KARL LAGERFELD

LIU•JO MILANO

COCCODRILLO

ADOLFO DOMINGUEZ

Dino Zoo TAVA TERITORIJA

Both shopping centers and retailers are in search of new unique concepts to increase their efficiency –a creative leisure area was opened in MEGA Teply Stan shopping center, Meeting Point co-working is planned to be located in Vegas Crocus City, MARK eat food hall was launched in Aviapark.

Food halls are developing and expanding the geography – Zenden opened a food court in Pyatigorsk on a place of Verhkny Rynok, Ginza Project plans to develop a chain of Green Market gastronomic centers in residential districts in Moscow, Gremm Group announced the launch of a gastronomic market at Maroseyka Str.

Market consolidation continues – M.Video and Eldorado will be opened instead of Media Markt stores, Euroset and Svyaznoy agreed on the merge under Svyaznoy brand.

NEW MARKETPLACES

беру!

ГдеМатериал

ozon.ru выбирайте

одноклассники

Билайн

ВСЕ АПТЕКИ

Ecommerce keeps growing – in 2017 it grew by 17% (according to AKIT), in the previous years – by 20-30%. Existing online-operators are developing omni-channel operations and new formats – large ecommerce players are launching marketplaces (Yandex and Sberbank, Ozon, Mail.ru), Lamoda plans to open offline stores, Rambler and Sberbank are launching a new service for preliminary orders in restaurants and paying bills online.

COMMERCIAL TERMS

In general, commercial terms remained at the level of the last year. However, the prime segment showed first signs of growth, reflecting the growing confidence of market players.

155 '000

RUB / sq. m / year

Prime rental rate indicator - base asking rental rate for a 100 sq. m gallery unit on the ground floor of prime shopping centers

12-15 %

of turnover

Average rental payment for an operator in retail gallery

Rental rates in prime shopping centers *

Tenant type	Average rental rate, Rub./ Sq. m / year	
	Min	Max
Hypermarket	-	8 000
DIY	-	10 000
Entertainment center	-	14 000
Cinema	6 000	12 000
Fashion (anchor)	-	15 000
Retail gallery unit	20 000	250 000
Fitness center	6 500	10 000
Restaurant, café, coffee shop	20 000	150 000
Food court	75 000	170 000

Source: Cushman & Wakefield

*Average rental rates for successful shopping centers in Moscow. The data can be used only for estimation of the level of rental payments.

The most common structure of rental payments is a compound rental rate – either a minimum fixed rent or a percentage of the turnover of the tenant (whichever is higher) is used as a rental payment. "Net" percentage of turnover (without fixed payment) is almost never used as a method of payment, it is sometimes used for large anchor tenants (hypermarkets, entertainment, cinema). However, different payment schemes are used in different shopping centers – in some properties these types of tenants also pay fixed rent.

Average percentages vary from 12 to 15% for retail gallery operators, from 3 to 5% for large anchor tenants.

Section 2

WAREHOUSE AND INDUSTRIAL

- The demand for warehouse space in the Moscow region remains high. The vacancy is decreasing.
- Developers prefer built-to-suit approach to speculative construction.
- Some of the developers are increasing asking rental rates in prime locations due to the lack of high-quality premises which are ready to move-in.

MOSCOW, CLASS A

	H1 2018	2018 (forecast)
Stock (‘000 sq. m)	10,059	10,613
New construction (‘000 sq. m)	148	702
Vacancy rate (%)	9	8.5
Rental rate * (RUB / sq. m / year)	3,300-3,600	3,300-3,600
Take up (‘000 sq. m)	625	1,300

REGIONS, CLASS A

	H1 2018	2018 (forecast)
Stock (‘000 sq. m)	6,782	7,075
New construction (‘000 sq. m)	139	422
Take up (‘000 sq. m)	166	550

** Average rent excluding OPEX, utilities and VAT*

DEMAND FOR WAREHOUSE SPACE IS STABLE

Trends. Moscow and Regions

148
‘000 sq. m
New construction, class A
Moscow and the regions, H1 2018

625
‘000 sq. m
Take up, class A
Moscow and the regions, H1 2018

Source: Cushman & Wakefield

The demand for warehouse space in the Moscow region remains high, take up is growing.

Vacancy rate is decreasing - there is a lack of “ready to move-in” premises with total area of more than 20,000 sq. m in prime location. Taking advantage of this shortage, some developers are increasing asking rental rates in prime properties.

However, speculative construction is still not increasing. In the context of low economic growth, the tenants are ready to wait 6-9 months until a new building that meets all their requirements is completed.

The demand for warehouses in the regions is lower than in Moscow. In H1 2018, the take up decreased by 10% compared to the average indicator of the last 5 years.

The situation with speculative construction in the regions is the same as in Moscow. Developers prefer to start construction after signing of preliminary lease or purchase agreement. In the majority of regions there is a lack of speculative warehouse premises.

Warehouse & Industrial

MOSCOW REGION

The share of vacant space is decreasing, development activity is increasing.

THE VACANCY RATE IS DECREASING

Rental rate and vacancy rate. Moscow region

9 %

Vacancy rate, class A

H1 2018

3.3-3.6

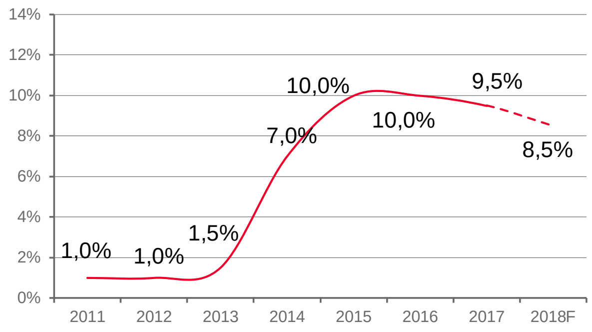
‘000 RUB / sq. m / year

Rental rate, class A

H1 2018

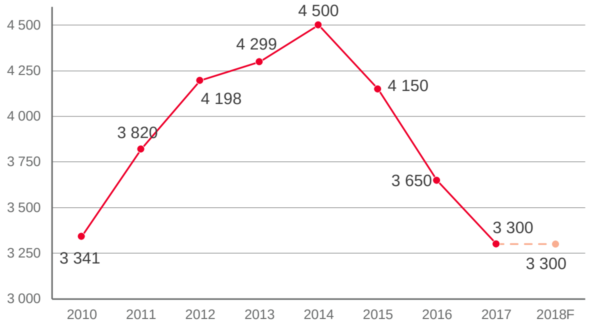
Source: Cushman & Wakefield

Vacancy rate, class A



Vacancy rate continues to decrease. At least half of the warehouse space planned for delivery in 2018 is under preliminary lease or purchase agreements. Developers are still cautious and prefer build-to-suit projects to speculative construction.

Rental rate, class A, RUB / sq. m / year



At the end of Q2 2018, some of developers started to increase asking rental rates in quality warehouses in prime location.

DEMAND FOR WAREHOUSE SPACE IS STABLE

Supply and Demand. Moscow region

227

‘000 sq. m

New construction, class A and B

H1 2018

739

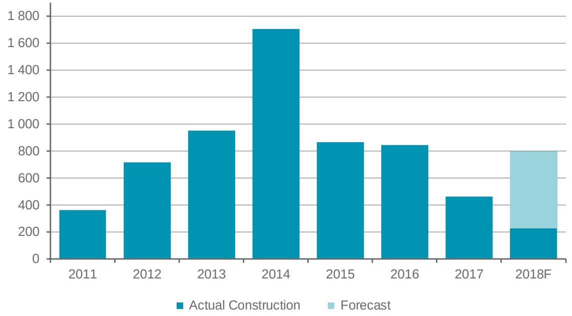
‘000 sq. m

Take up, class A and B

H1 2018

Source: Cushman & Wakefield

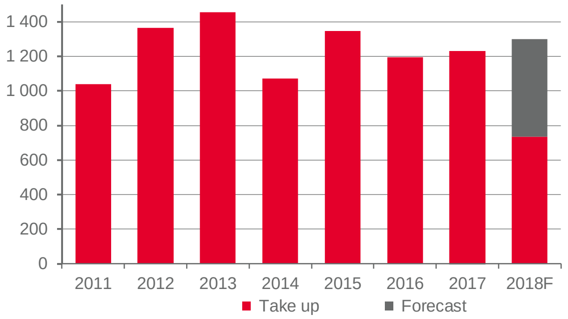
New construction, classes A and B, ‘000 sq. m



The supply of warehouse space increased by 227,000 sq. m during the first half of 2018, which is two times higher than in the same period of 2017.

We predict that in 2018 around 800,000 sq. m of new warehouse space will be constructed, representing 70% increase to 2017.

Take up, classes A and B, ‘000 sq. m



In Q2 2018, 325,000 sq. m of warehouse space was leased and purchased, which is 25% higher than the average indicator for the last 5 years. Against the background of the first signs of the market recovery - vacancy rate decrease, prime rental rate increase – we note the growth of tenants’ activity.

RETAILERS ARE THE MAIN TENANTS

Demand. Moscow region

50%

Share of retail segment

In take up structure of the last 12 months

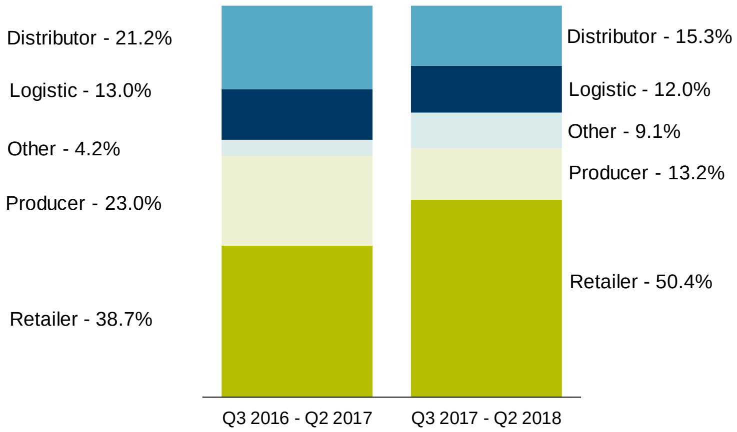
22%

Share of fashion retailers

In take up structure of the last 12 months

Source: Cushman & Wakefield

Take up structure



Traditionally, retail segment is the main driver of demand for quality warehouse premises. After a slight decrease of demand from retailers in 2016-2017, we note that their share increased from 38.7% to 50.4%. This increase compensated decrease of demand from manufacturing companies and distributors.

As of take up structure by profile, fashion segment has the biggest share – 22%. Followed by food and beverage and logistic segments– 15% and 12% of take up, respectively.

Warehouse & Industrial

REGIONS OF RUSSIA

The demand for warehouse space decreased. Developers prefer built-to-suit projects to speculative construction.

SEVERAL REGIONS HAVE RECORDED A DEFICIT

Supply and Demand. Regions

154

‘000 sq. m

New construction, class A and B

H1 2018

175

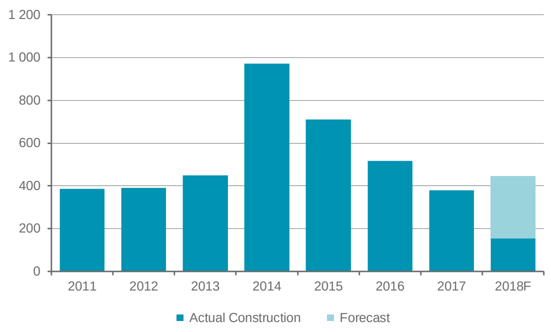
‘000 sq. m

Take up, class A and B

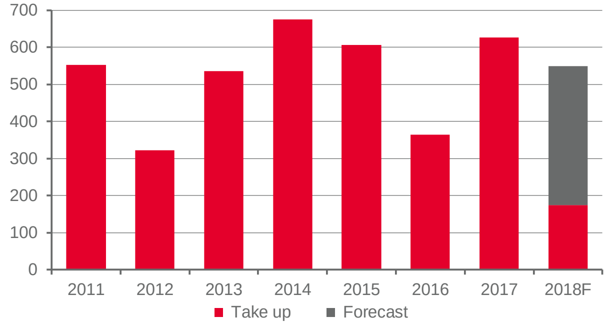
H1 2018

Source: Cushman & Wakefield

New construction, classes A and B, ‘000 sq. m



Take up, classes A and B, ‘000 sq. m



In Q2 2018, 49,000 sq. m of new warehouse space was constructed, which is relative to the same period of 2017. Based on the preliminary results, approximately 450,000 sq. m of space will be constructed by the end of the year – a 20% increase over the previous year. In a number of regions there is a deficit of quality warehouse space, which may stimulate the growth of speculative construction.

In H1 2018, the tenants’ activity on the regional markets decreased. In Q2 2018, 132,000 sq. m of warehouse space was leased or purchased, which is 10% less than the amount recorded from the previous year. Based on the preliminary results, the yearly take up will reach 550,000 sq. m, representing a 15% decrease to 2017.

THE HIGHEST DEMAND IS FROM RETAILERS

Demand. Regions

46%

Share of retail segment

In take up structure of the last 12 months

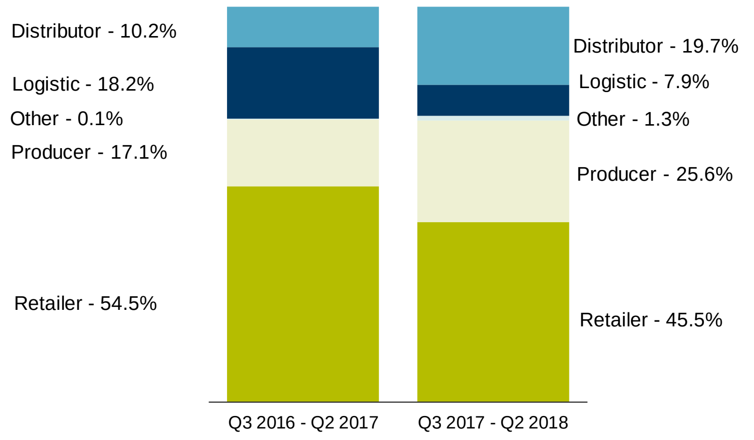
21%

Share of F&B segment

In take up structure of the last 12 months

Source: Cushman & Wakefield

Take up structure



Traditionally, around 50% of warehouse space in the regions is leased or purchased by retailers, however in the last 12 months the share was slightly lower than usual and comprised 45.5%. It is too early to declare a new trend as the number of transactions in the regions is insignificant, and take up structure is very volatile from period to period.

Food and Beverage segment has the largest share in take up structure – 21% of the total volume of transactions.

KEY PROPERTIES

Supply and demand. Moscow and regions

Key warehouse properties opened in H1 2018, and planned for delivery by the end of 2018

Property	Highway	Region	Distance from city, km	Total area, 000 sq. m	Delivery
Vnukovo - 2	Kievskoe	Moscow	17	38,6	Q1
Wildberries	Simfelopolskoe	Moscow	20	95	Q3, Q4
IKEA Yesipovo	Leningradskoe	Moscow	33	90	Q4
Mikhaylovskaya Sloboda	Novoryazanskoe	Moscow	20	46,9	Q2, Q4
PNK Park Sofyino	Novoryazanskoe	Moscow	32	34,8	Q2
Logopark Sigma		Ufa		24,5	Q1
A Plus Park Kazan		Kazan		58,7	Q1, Q3
Monetka		Khanty-Mansiysk		25,7	Q3
Oktavian	Toksovskoe	St. Petersburg	11	28,5	Q2, Q4
A2 Logistic Krasnodar		Krasnodar		10	Q3

Section 2

HOSPITALITY

- Operating results of H1 2018 were very much affected by the 2018 FIFA World Cup over which, according to the official statistics, Moscow was visited by 3 million tourists, including 1.2 million foreigners (if one doesn't count the CIS countries).
- Supply growth in H1 2018 was registered, mostly, in the airport hotel segment (776 new hotel rooms in Domodedovo, Sheremetyevo, and Vnukovo), with only 171 new rooms opened in the city.
- Preliminary operating results for June 2018 demonstrate a substantial (200-300%) growth in RevPAR across all price segments compared to the same period in 2017, with revenue growth mainly driven by a rise in the room rates. Other types of revenue in city hotels were much less pronounced.

~60 `000 keys

Overall estimated classified room stock (net of hostels and serviced apts)

City of Moscow's and Cushman & Wakefield's estimates, June 2018

19.5 `000 keys

Modern quality room stock

Cushman & Wakefield's estimates, H1, 2018

171 keys

In 1 new hotel

Net room stock increase over H1 2018

776 keys

In 3 new airport hotels

Net room stock increase in H1 2018

THE MORE AIRPORT HOTELS, THE MERRIER

Main supply increase – in the airport submarket.

171 keys

New supply in Moscow in H1 2018

1 new hotel

776 keys

New supply at Moscow airports in H1 2018

3 new hotels

Source: Cushman & Wakefield

New supply in Moscow in 2018

Project	Keys	Opening
Holiday Inn Express Khovrino (ex-Sozyuz)	171	Q2
Radisson Blu Olympiysky	379	Q4
Total	**550**	

New supply at Moscow airports in 2018

Project	Keys	Opening
Ibis Moscow Domodedovo Airport	152	Q1
Holiday Inn Express Moscow - Sheremetyevo Airport	192	Q1
DoubleTree by Hilton Moscow – Vnukovo Airport	432	Q2
Total	**776**	

HOTEL SUPPLY GROWTH IS SLOWING DOWN - TEMPORARILY

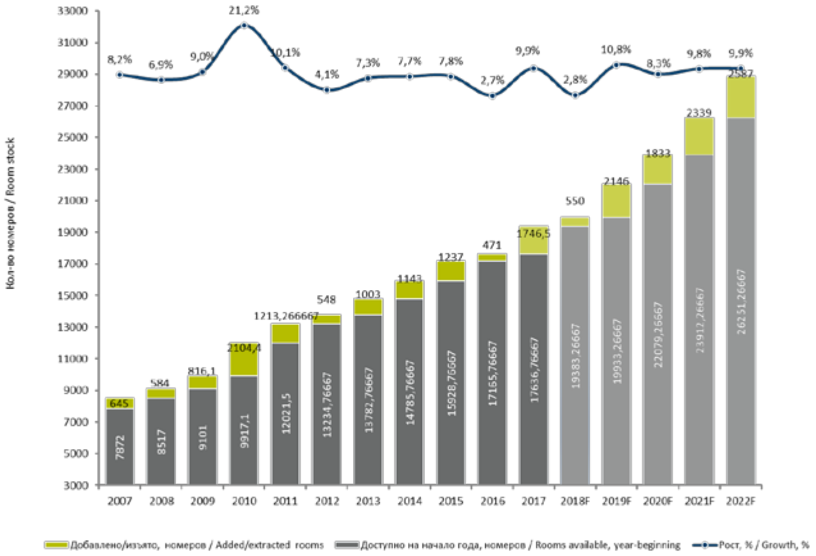
Growth rates are lower than in 2017 – but there is no reason to worry yet.

2.8 %

Year-to-year growth in 2018

Expected market growth rate vs. 2017

Supply growth dynamics – actual and projected



Source: Cushman & Wakefield

After a substantial growth of room stock in 2017, 2018 is expected to see a lower number of openings, with the total number of new keys limited to 550, of which 171 rooms are already opened.

At the same time, should all hotel projects currently listed in the development pipeline for 2019-2023 open on schedule, this slowdown of supply growth may prove to be short-lived, and growth rates will return to levels exceeding 8% per annum as soon as in 2019.

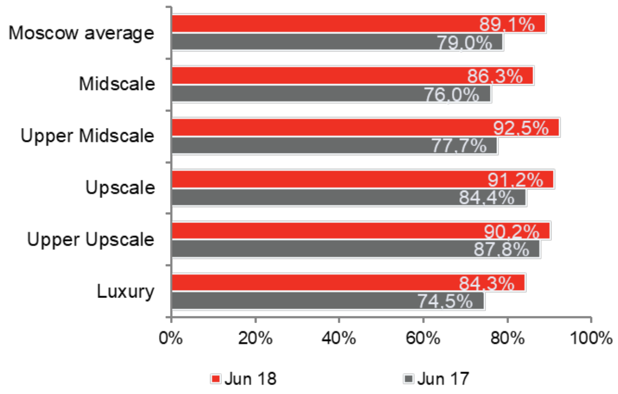
2018 FIFA WORLD CUP – HOW DID IT ALL START?

Stunning success for Moscow hotels during the group matches.

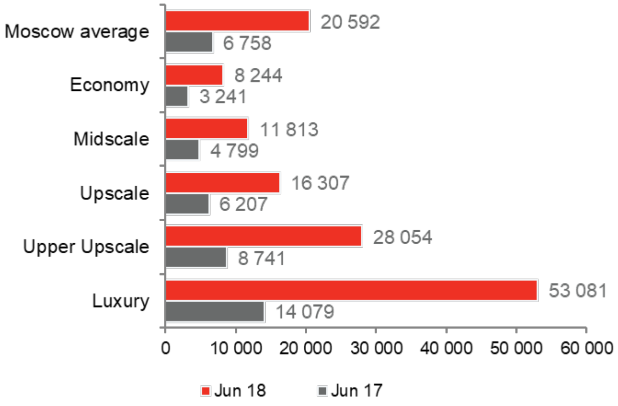
89.1 % **Jun 2018 Occ, year-on-year**
Wider market

204.7 % **ADR (RUB) change, Jun 2018, year-on-year**
Wider market

Occ, Jun 2018, by segment



ADR (RUB), Jun 2018, by segment



Any skepticism and low faith in the ultimate success of the “event of the year” displayed by the market players ahead of the 2018 FIFA World Cup were put to shame. Over the month of June, the Moscow hotels performed spectacularly well and managed not only to push room rates but also increased occupancies by some 10.1 basis points (12.8%), to 89.1% across all segments.

The main winners of the contest – Luxury hotels which housed FIFA officials, some football teams (and their families and friends) as well as high-paying guests. Their year-on-year increase in ADR reached 277% - from RUB14,097 in 2017 to RUB53,081 in 2018. On top of this, Luxury hotels’ Occ increased 13.1%, resulting in a 326.5% growth in RevPAR, to reach RUB44,745

Source: Cushman & Wakefield

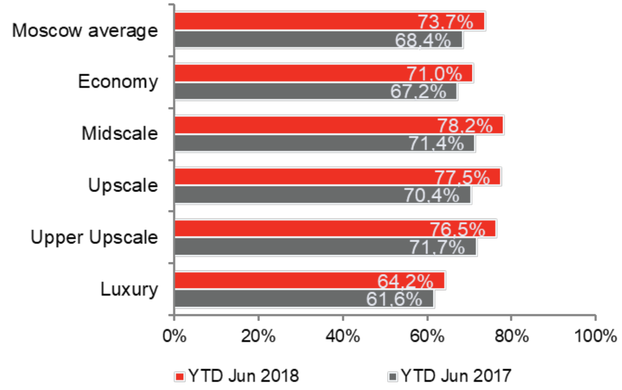
NO LOSERS IN SIGHT

All Moscow hotels scored big during the 2018 FIFA World Cup.

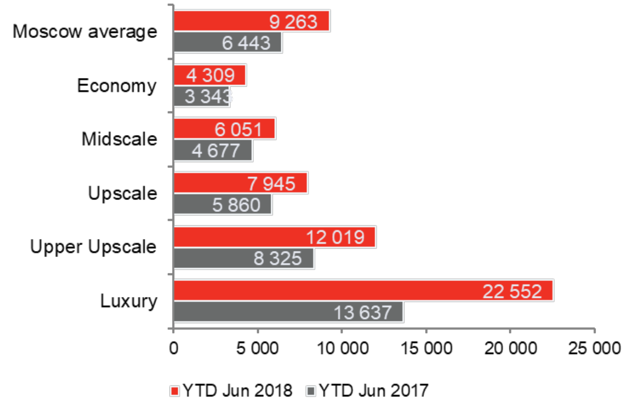
73.7 % **Occ, YTD Jun 2018**
Wider market

43.8 % **ADR (RUB), YTD Jun 2018**
Wider market

Occ, YTD Jun 2018, by segment



ADR (RUB), YTD Jun 2018, by segment



The average Occ level for the Wider market over the first 6 months of the year reached 73.7%, which is 5.2 p.p. higher than a year ago. The most popular hotels with the highest levels of Occupancy were Upper-Upscale, Midscale, and Upscale properties, registering 76.5%, 78.2%, and 77.5%, respectively.

Due to the “Championship effect”, ADR increased across all price segments, with the average growth rate in the order of 40% (from RUB6,443 in 2017 to RUB9,263 in 2018), with the highest increase attributable to the Luxury segment (+65.4%, to RUB22,552).

Source: Cushman & Wakefield

EXCELLENT GROWTH OF REVPAR

54.8 %

H1, 2018 RevPAR change (in RUB)

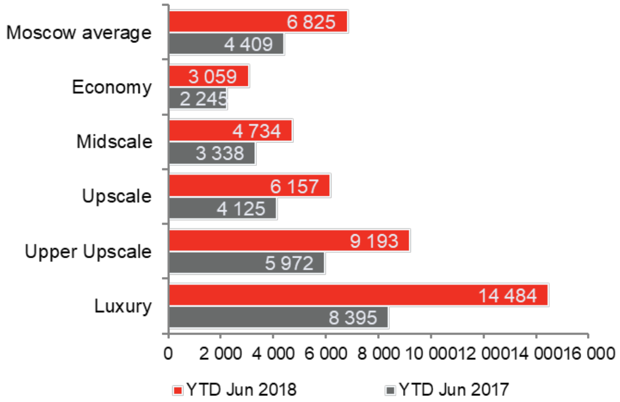
Wider market

72.5 %

Highest RevPAR growth in H1, 2018

Luxury segment

RevPAR (RUB), H1 2018, by segment



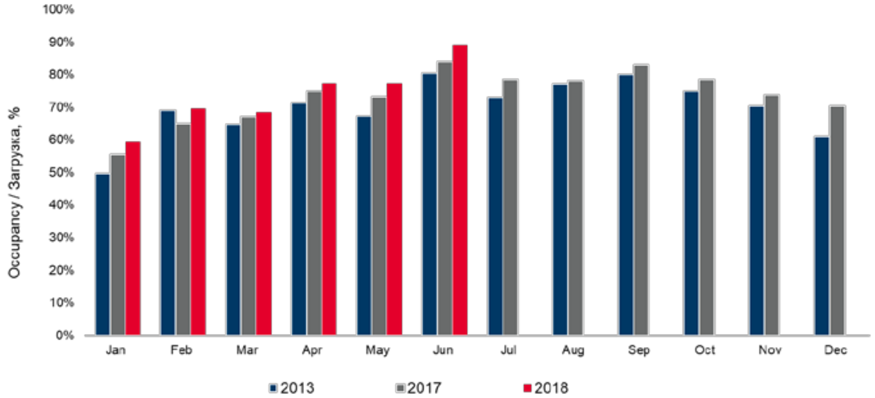
Source: Cushman & Wakefield

Moscow hotels were successful in converting extraordinary demand for accommodation during the first weeks of the 2018 FIFA World Cup (and a few weeks immediately preceding it) to higher rates – without losing the roomnights. As a result, the Wider market RevPAR during the first 6 months of the year grew almost 55%.

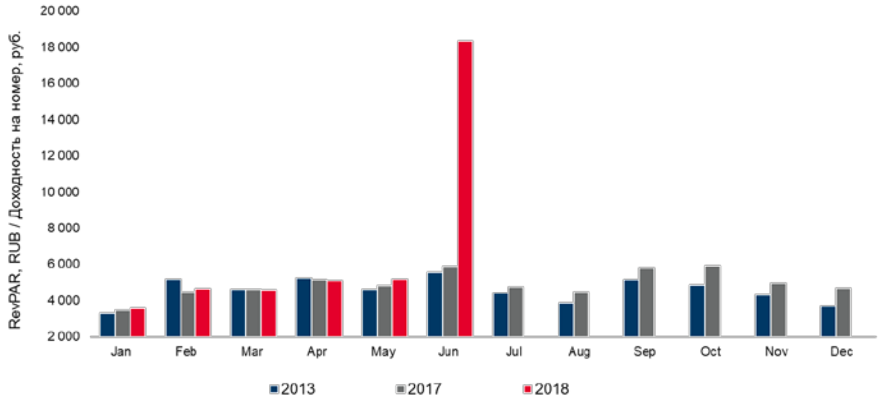
IS THERE LIFE AFTER A MEGA-SPORTING EVENT?

Moscow hotels returning to the “business-as-usual” mode.

Occupancy dynamics, %, by month



RevPAR dynamics (in RUB), by month



Having finalized the 2018 FIFA World Cup with great success, the Moscow hotels now have to go back to the normal course of business. And the widely expected slowdown of business for the remainder of the summer season is a standard “pause”, caused by a sharp reduction in hotel accommodation demand after the end of a mega-sporting event. However, even this temporary slowdown is unlikely to greatly affect the yearly results – if one takes into account the upcoming start of the H2 business season (Sept-Nov). Presently, the market consensus expects the 2018 Total Revenue to be 10-15% higher than in 2017.

Numerous compliments to Russia as the host country for its flawless management of the main global sporting event as well as the real positive impact (financial and image-wise) from the increased numbers of foreign tourists prompted the authorities to address the visa regime issue and consider its liberalization. Specialists estimate that such a move might grow the number of visitors, at least to such traditional tourist destinations as Moscow and St. Petersburg, by 10-20% per year, further improving occupancies and increasing hotel revenues, particularly outside the summer months.

Source: Cushman & Wakefield

#MARKETBEAT

Section 3

APPENDIX

Information and interactive maps

STANDARD COMMERCIAL LEASE TERMS

LEASE TERMS

DURATION OF LEASE

Offices: 3-7 years
Industrial: either short-term (1-3 years) or long-term (5+ years)
Retail: 3-5 years, anchor tenants - 7-10 years.

BREAK OPTION

Offices: Possible after 3 years with deposit withdrawal as penalty. After crisis became very popular. Notice period is 6-12 months. When there is an option to review the rent after the third year, contract can be terminated from both sides.
Retail: Possible after 2-3 years, subject to negotiation with landlord.

DISPOSAL OF LEASES

ASSIGNMENT AND SUB-LETTING

Offices & Industrial: Usually possible, but subject to negotiation.
Retail: Not common, in some cases subject to negotiation.

MEASUREMENT PRACTICE

Space is measured generally on the BOMA system. Some Landlords apply BTI (Bureau of Technical Inventory) measurements.

RENTAL PAYMENTS

RENT PAYMENT AND FREQUENCY

Offices and retail: RUB or US$ per square meter per year, payable due monthly or quarterly in advance.
Industrial: Rubles.

RENT DEPOSIT

Offices: 1-3 months rent equivalent (bank guarantee optional, very seldom as landlords prefer the deposit).
Retail: 1-2 months rent equivalent (bank guarantee optional).
Industrial: 1-3 months rent equivalent (bank guarantee optional, very seldom as landlords prefer the deposit)

RENT REVIEWS

After crisis have become more popular, negotiable.

INDEXATION

Offices: 5-10% for RUB agreements; 2,5-4% or at the level of USA / EU CPI for agreements in foreign currency.
Retail: 8-10% or CPI in Russia for RUB agreements, 5% or US CPI for agreements in USD.
Industrial: 4-8% (for agreements longer than 5 years not more than 5-6%).

TURNOVER RENTS (only in **Retail**):

Compound rental rates (minimum fixed rent + a percentage of turnover) are almost always used in shopping centers. Normally, the percentage of turnover varies between 12-15% (fashion), 1-3% for large anchor tenants.

SERVICE CHARGES, REPAIR AND INSURANCE

REPAIR

Tenant: Internal repairs and maintenance.
Landlord: Structural repairs, common areas.

INSURANCE

Tenant: Contents insurance.
Landlord: Building insurance which is normally charged back to tenant via the service charge.

SERVICE CHARGES

Service charge is payable by the tenant at either an ‘open book’ basis or as a fixed cost.

UTILITY EXPENSES

Often included to service charges, but depends on landlord and different types of projects.

Retail: in some cases, service expenses can be increased due to the regular growth of utility expenses after provision of supporting documents.
Industrial: usually paid separately on the basis of actual consumption.

TAXATION

REAL ESTATE TAX

Landlord: the amount of tax depends on the region. In Moscow for office and retail: 1,4% in 2017, 1,5% in 2018 of cadastral value (1.2% of in 2015, 1.3% in 2016).

Tenant: can be partly or fully included to service charges paid by tenant.

VAT: 20%

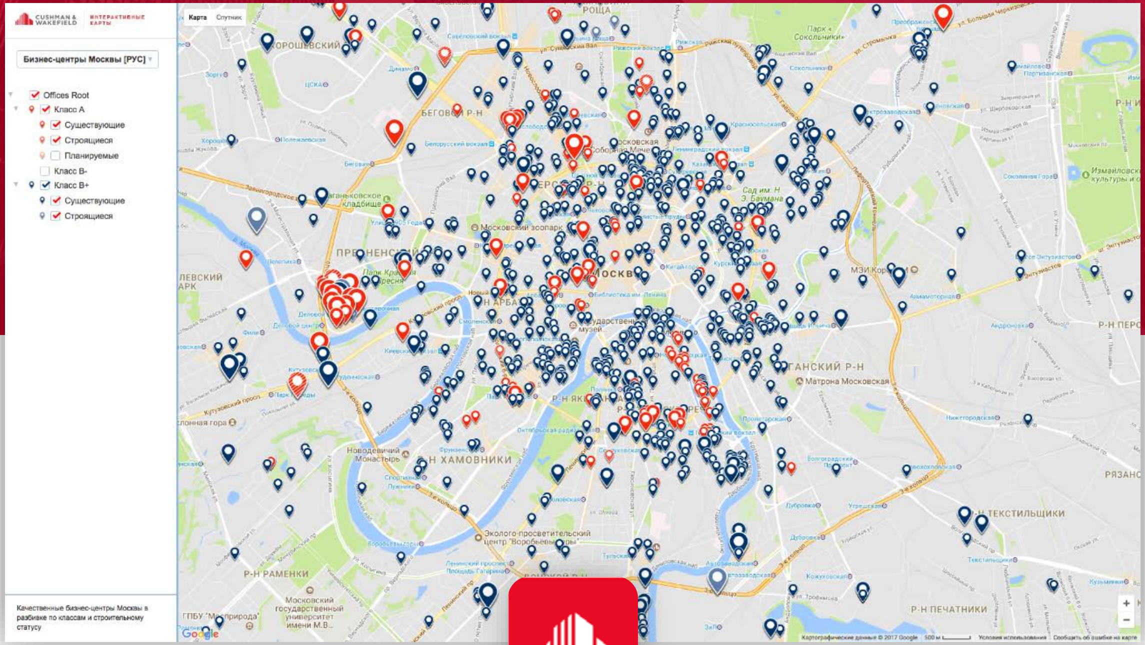
Cushman & Wakefield in Russia

INTERACTIVE MAPS

PROPERTY SEARCH

www.interactivemaps.ru

- Moscow offices
- Shopping centers in Russia
- Warehouses in Russia
- Hotels
- Infrastructure development



COMMERCIAL REAL ESTATE AND INFRASTRUCTURE INTERACTIVE MAPS

Research Department

CUSHMAN & WAKEFIELD IN RUSSIA

Denis Sokolov
Partner,
Head of Research & Insight
Denis.Sokolov@cushwake.com

Tatyana Divina
Associate Director,
Deputy Head of Research & Insight
Tatyana.Divina@cushwake.com

Marina Smirnova
Partner,
Head of Hospitality and Tourism
Marina.Smirnova@cushwake.com

Alexander Kuntsevich
Senior Analyst
Warehouse & Industrial
Research
Alexander.Kuntsevich@cushwake.com

Maria Logutenko
Junior Analyst
Office Research
Maria.Logutenko@cushwake.com

Evgeniya Safonova
Analyst
Retail Research
Evgenia.Safonova@cushwake.com

For more information and contacts please visit
www.cwrussia.ru

About the company

CUSHMAN & WAKEFIELD IN RUSSIA

Cushman & Wakefield is a global leader in commercial real estate services, helping clients transform the way people work, shop, and live. The firm’s 43,000 employees in more than 60 countries provide deep local and global insights that create significant value for occupiers and investors around the world. Cushman & Wakefield is among the largest commercial real estate services firms with revenues of $5 billion across core services of agency leasing, asset services, capital markets, facility services (branded C&W Services), global occupier services, investment management (branded DTZ Investors), project & development services, tenant representation and valuation & advisory.

Key contacts

CUSHMAN & WAKEFIELD IN RUSSIA

MANAGEMENT

Sergey Riabokobylko
Executive Partner, CEO
M +7 985 764 6436
sergey.riabokobylko@cushwake.com

Mikhail Mindlin
International Partner, COO
M +7 985 763 5803
mikhail.mindlin@cushwake.com

Pavel Ivashin
Partner, CFO
M +7 985 924 1671
pavel.ivashin@cushwake.com

AGENCY

Pavel Baranov
Partner, Head of Occupier Services
M +7 985 364 6253
pavel.baranov@cushwake.com

Evgeny Popov
Partner, Head of Strategy & Sales
M +7 916 590 6805
evgeny.popov@cushwake.com

Diana Mirzoyan
Partner, Land
M +7 985 764 7314
diana.mirzoyan@cushwake.com

Egor Dorofeev
Partner, Head of Warehouse & Industrial
M +7 985 923 6563
egor.dorofeev@cushwake.com

Oxana Mostyaeva
Head of Retail
M +7 916 181 7429
oxana.mostyaeva@cushwake.com

Andrey Shuvalov
Associate, Retail
M +7 903 256 2174
andrey.shuvalov@cushwake.com

Dmitry Tarasov
Head of Office Agency
M +7 926 833 66 93
dmitry.tarasov@cushwake.com

Ilya Kouznetsov
Head of Russian Regions: Corporate Services
M +7 916 501 4217
ilya.kouznetsov@cushwake.com

CONSULTING

Marina Smirnova
Partner, Head of Hospitality & Tourism
M +7 985 410 7237
marina.smirnova@cushwake.com

Marina Usenko
Partner, Hospitality & Tourism
M +7 916 173 6656
marina.usenko@cushwake.com

Julia Tokareva
Head of Development Consultancy
M +7 985 222 7247
julia.tokareva@cushwake.com

Konstantin Lebedev
Partner, Head of Valuation & Advisory
M +7 985 784 4705
konstantin.lebedev@cushwake.com

Denis Sokolov
Partner, Head of Research & Insight
M +7 916 901 0377
denis.sokolov@cushwake.com

Oleg Takoev
Partner, Valuation & Advisory
M +7 910 463 4278
oleg.takoev@cushwake.com

PROJECT MANAGEMENT

Semyon Yurchenko
Partner, Head of Asset Services
M +7 919 967 2568
semyon.yurchenko@cushwake.com

Andrey Chertischev
Partner, Head of Project & Development Services
M +7 916 557 2838
andrey.chertischev@cushwake.com

CAPITAL MARKETS

Alan Baloev
Partner, Capital Markets
M +7 916 740 2417
alan.baloev@cushwake.com