CUSHMAN & WAKEFIELD | #MARKETBEAT

Q3 | 2018

Commercial Real Estate - Russia

#MARKETBEAT

Cushman & Wakefield Research Department

Macroreview

Capital Markets

Office

Retail

Warehouse & Industrial

Hospitality & Tourism

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Outlook

GROWING MORTGAGE LOANS AND A NEED FOR ACCUMULATION OF PERSONAL PENSION SAVINGS WILL RESULT IN DECREASED CONSUMPTION CAPACITY FOR THE MIDDLE CLASS.

Pensionary reform will result in a labor force increase of about 5-10 mn people.
The unemployment rate will grow in the period of 10 years.

BRIEFING: CONSUMER MARKET IS UNDER PRESSURE

A dull fall after a warm and vibrant summer

In September Sergey Sobyanin started his next 5 year term as the Mayor of Moscow. This means that heavy transport infrastructure investments will continue and the city will be improving public spaces and will focus on the quality of life.

Vladimir Putin had signed a pension reform that extends the retirement age by 5 years. This move has already escalated social tension and will also have a long term impact on the labor force and unemployment. Russian citizens will begin to prepare for retirement themselves, primarily by allotting less money to consumption, and dedicating more funds to pension accounts.

The Central Bank raised the Key Rate by ,25 p.p. as a reaction to 10% Ruble devaluation.

The Central Bank also revised the target for 2019 inflation from 4% to 5.5%.

In Q3 the consumer optimism index fell significantly, particularly among Millennial generation, whose optimism fell from -4 to -10 points. Pension reform could be one of the reasons as this generation understands now that they will have to save for retirement themselves.

Another reason for the recession in the consumer market, especially in larger cities, is growing mortgage debt.

We expect consumer activity to remain low in Q4 2018. As a result consumer inflation will not escalate as rapidly as it was expected.

Trends of Q4:

- High leasing activity in office and W&I markets.
- Consumer activity is decreasing.
- Rising CPI is a threat.
- Additional pack of sanctions.

SANCTIONS

Section 1

MACROREVIEW

- Growth rate will slow down in Q4 2108.
- High GDP deflator in 2018 will lead to CPI escalation in 2019.
- The consumer market in 2018 will perform worse than expected originally, due to an income recession in H2 2018.
- Mortgage growth and residential construction are driving the economies of major Russian cities.

MACRO INDICATORS

	2017	2018	2019	2020	2021
GDP growth, %	1.6	**1.9**	1.3	1.2	1.2
RUB/USD	58.3	**62.9**	65.3	65.5	65.5
CPI, %	3.7	**2.9**	5.1	4.1	4.0
GDP deflator,%	7.6	**10.2**	5.1	3.7	3.7
Interest rate, %	10.55	**9.1**	9.6	9.4	8.6
Current Balance, % of GDP	1.5	**0.8**	0.9	0.3	0.2
Private consumption, %	3.3	**2.6**	2.8	2.6	2.3
Government spending	0.4	**0.6**	0.6	0.6	0.8
Capital outflow, bn USD	12.28	**-34**	-125	-113	-107
Unemployment rate, %	5.20	**4.8**	4.8	4.9	5.0
BRENT crude oil price	54.2	**74.1**	76.5	73.0	73.5

Source: Oxford Economics 12/10/2018

2018 IS THE BEST YEAR OF THE PREVIOUS FIVE

After good results in 2018 growth will slow down.

1.9 %

GDP Growth forecast for 2018

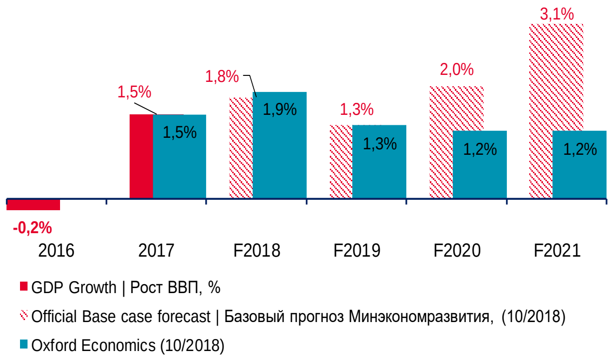
Oxford Economics

5.5 %

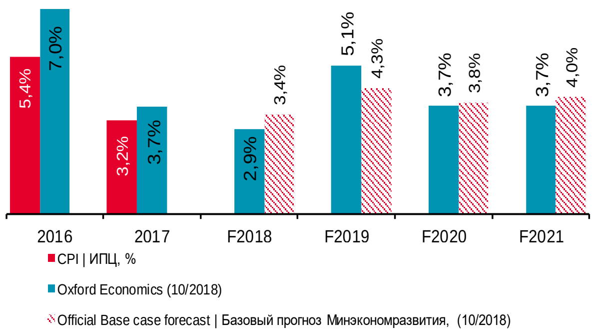
CPI target

By the Central Bank

GDP Growth, %



The Consumer Price Index, %



The Russian government is rather pessimistic about its 2019 outlook as it revised GDP forecast down to 1,3%.

Higher numbers for 2020-2021 reflect the task assigned by Vladimir Putin to ensure an economic growth rate above the world average. As of yet there is no official plan as to how this can be achieved.

Tightening sanctions, accelerated inflation and weak consumer market will be major challenges for the Regulator in 2019.

Also VAT increase from 18% to 20% will drive prices and inflation in 2019.

Fundamentals

CONSUMER MARKET BOOMING

The August 2018 increase of household debts is the highest in 5 years – 2,7%. Consumer credits are growing faster than mortgage loans.

15 %

Growth of Mortgage Households' Debt

Jan-Aug 2018

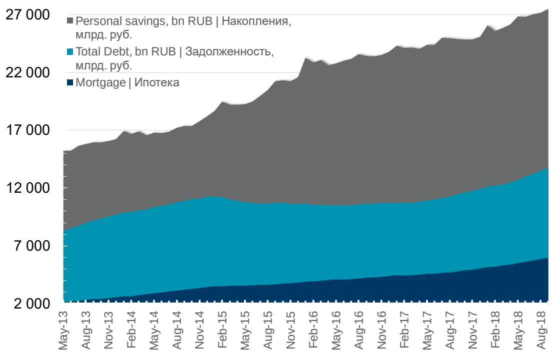
6 %

Share in GDP

Of the mortgage debt

Source: Central Bark, Cushman & Wakefield calculations

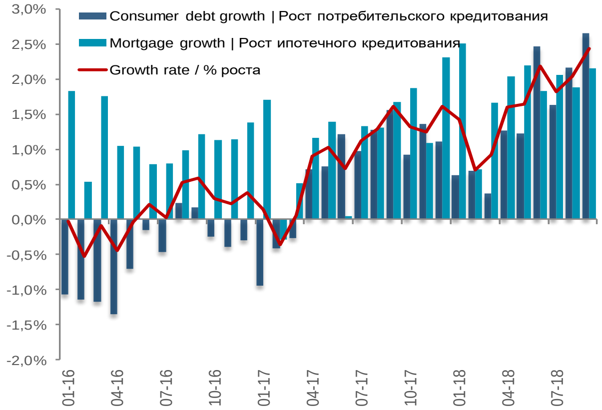
Shares and deposits (of physical persons), bn RUB



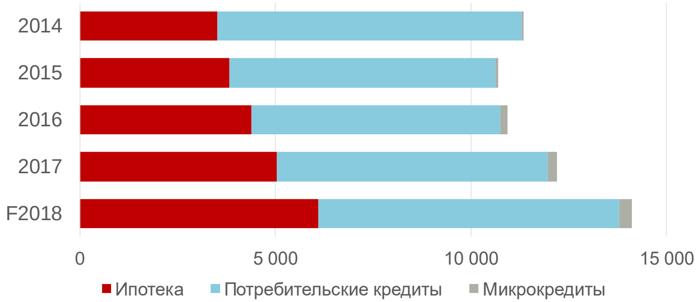
From Jan-Sept 2018 the household debt increased by 14%, the highest growth rate in the last 5 years.

Despite rapid growth, mortgage loans are still low volume relative to GDP, with Russia showing the lowest rate in Europe. In Central and Eastern Europe, mortgage loans account for 15-20% of GDP, with the indicator in Western Europe closer to 70-100%

Growth Rate of Household Debt



Household debt structure, bn RUB



CORPORATE DEBT

Corporate debt was actively growing throughout Q3 2018. Wholesale and retail are the most dynamic segments. Construction and real estate are stagnating.

7.5 %

Key Rate

Increased by 0,25 in Sept 2018

23 %

Overdue Debt

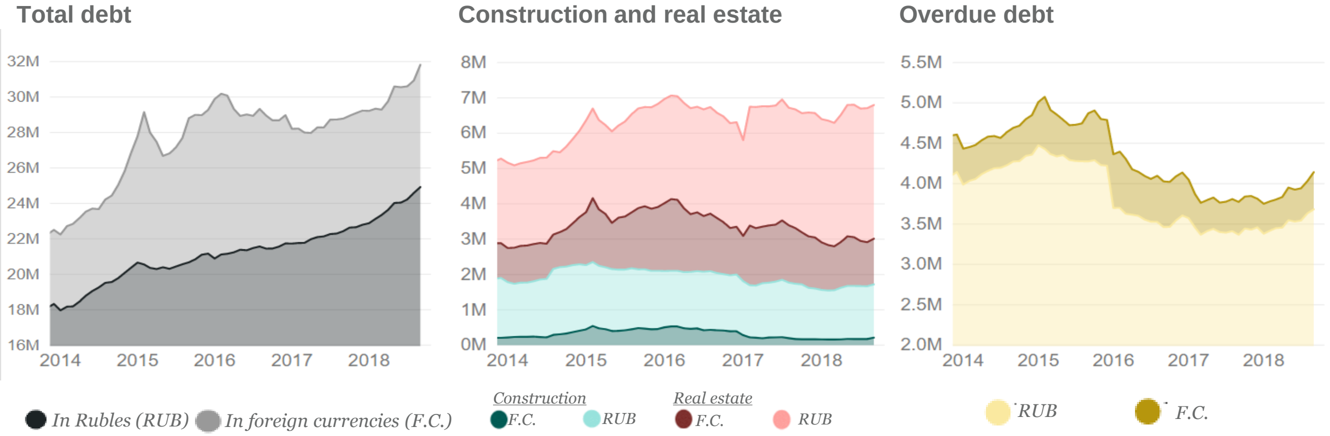
In Real Estate sector

Source: The Central Bank of Russia

Corporate debt continues growing. Wholesale and retail sectors showed an expansion of the assortment and credits due to growing consumer optimism in Q3 2018. However, the negative trend of consumer confidence will most likely lead to termination of the sector growth.

Credits in construction and real sectors have not grown since 2015. The share of overdue debts in these sectors are still relatively high: 23% for real estate and 18% for construction.

Corporate debt and overdue debt, mn RUB



PUBLIC RETAIL AND DEVELOPMENT COMPANIES

Stock Market Indicators from 12/08/18 to 12/10/2018 as compared to the MICEX index

+2.6 %

PIK

The growth leader over the past 90 days

-31.1 %

Lenta

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

- Slow start for 2018.
- Decrease of capitalization rate stopped due to the weakening ruble and increase of the key rate.

732 mn EUR

Total investment volume in Russia

In Jan-Sept 2018

1.2 bn EUR

Total investment volume in Russia

Forecast for 2018

9.5 %

Capitalization rate, prime office segment

October 2018

-9 mn EUR

Foreign investments outflow

In 2018

Capital Markets

TOTAL INVESTMENTS DROPPED SIGNIFICANTLY, WHILE FOREIGN INVESTMENT OUTFLOWS SHOW LOW FIGURES.

We expect investment activity to increase in 2019-2020.

EASTERN EUROPEAN INVESTMENT IN COMMERCIAL REAL ESTATE

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

8%

The share of Russia in CEE

By the total investment in the commercial real estate

4.8 bn EUR

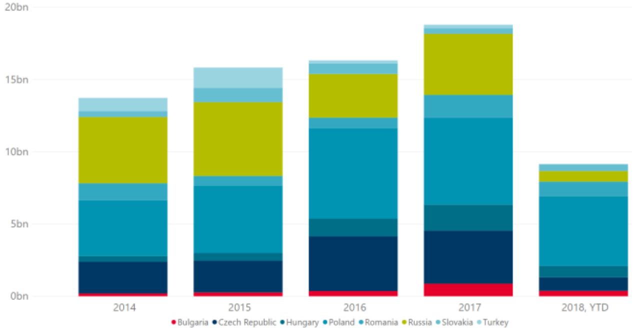
Investment volume in Poland

The largest investment market in CEE region in Jan-Sept 2018

REAL CAPITAL ANALYTICS

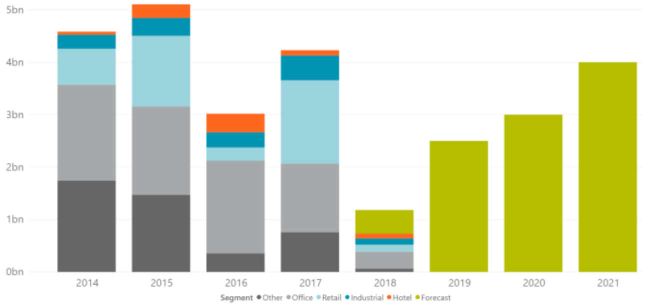
Source: Real Capital Analytics

Investments on the core CEE markets, bn EUR



Poland maintained a leading position in the regional investment market. In Jan-Sept 2018 only Poland and Slovakia showed higher levels of investment activity compared to the last year. Investment volumes in Hungary, Czech Republic, Romania, Russia and Bulgaria are behind indicators of 2017. However, results for 2018 will be comparable to the previous year.

Investments in Russia, bn EUR



The Russian investment market is in the weakest position in the history of the real estate market. We expect only 1.2 bn EUR of investments in 2018.

The foreign investment outflow was 800 mn EUR last year while it is only 9 mn EUR in Jan-Sept 2018. The exit of foreign investment from the Russian market is almost completed. We expect an increase in investment activity in 2019-2020.

CAPITALIZATION RATES

9.5 %

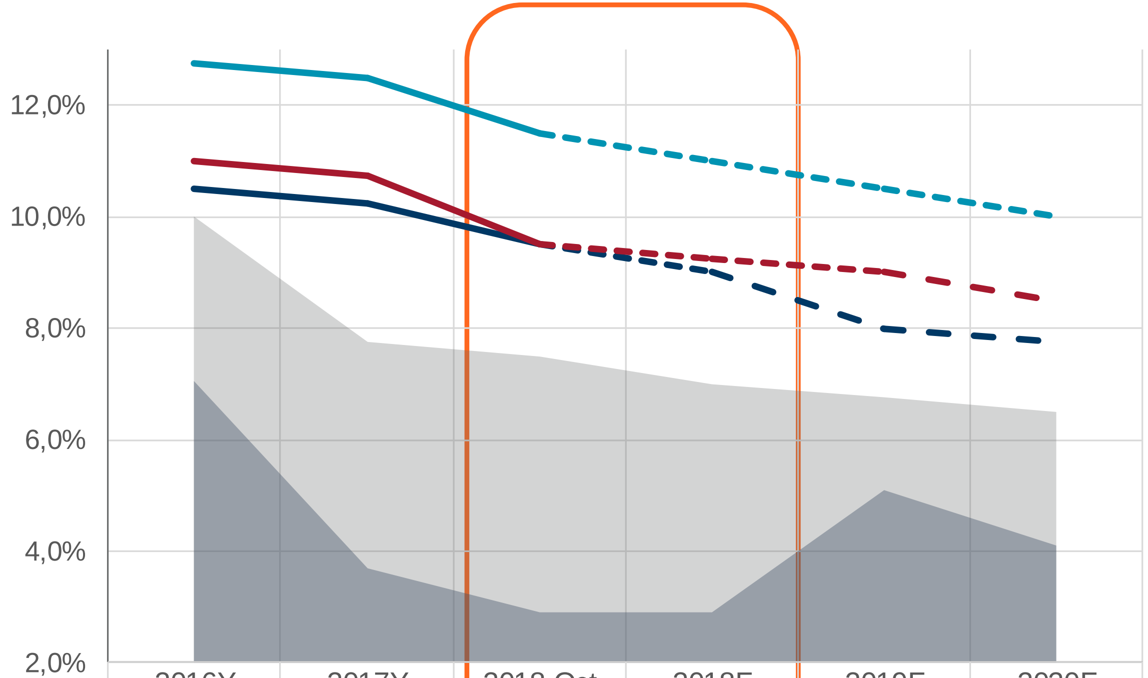
Office

Capitalization rate, October'18

7.5 %

The key rate

The Central Bank of Russia



	2016Y	2017Y	2018 Oct	2018F	2019F	2020F
Central Bank Key Rate	10,00%	7,75%	7,50%	7,00%	6,75%	6,50%
Inflation	7,04%	3,70%	2,90%	2,90%	5,10%	4,10%
Office	10,50%	10,25%	9,50%	9,00%	8,00%	7,75%
Shopping Centers	11,00%	10,75%	9,50%	9,25%	9,00%	8,50%
Warehouse	12,75%	12,50%	11,50%	11,00%	10,50%	10,00%

Capital Markets

#MARKETBEAT

INVESTMENT STRUCTURE

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

73 %

The share of foreign investments

The Central and Eastern Europe, Jan-Sept 2018

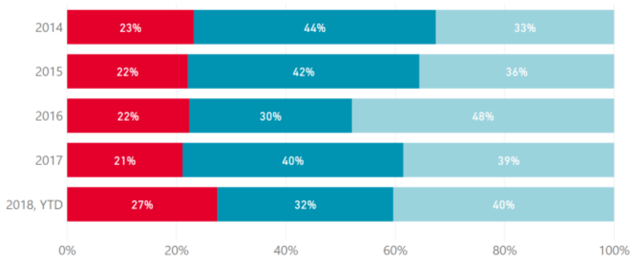
20 %

The share of foreign investments

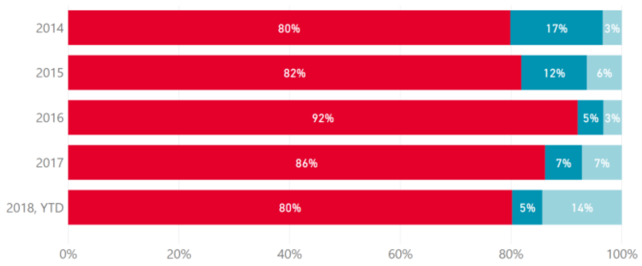
Russia, Jan-Sept 2018

Source: Real Capital Analytics

Central and Eastern Europe



Russia



Investments in Eastern Europe are 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

- Despite the volatility of the economy, the market shows a slight improvement of all the indicators each quarter.
- Vacancy is going down due to low construction activity and take-up close to the high level of the last year.
- Take-up remains on the level of 1,8-2,0 mn sq. m annually.

Moscow Q1-3 2018

Classes A, B+ & B-

17.12 mn sq. m

Total stock of office buildings
12/10/2018

93 '000 sq. m

Construction

201 '000 sq. m

Net absorption

1.36 mn sq. m

Take-up

Offices

MARKET NEEDS FOR QUALITY CONSOLIDATED OFFICE LOTS

High activity of tenants leads to the formation of local shortage of office space while maintaining a high vacancy rate.

NEW SUPPLY

2018 beats the 15-year-old anti-record by deliveries of new office space. In 2019, the figure will remain at 2018.

VTB Arena

Novion

Gallery 76

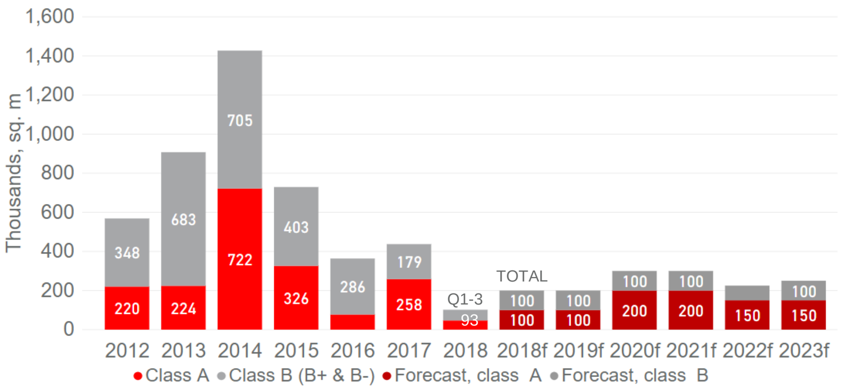
Source: Cushman & Wakefield

In Q3, 4 office buildings of class A (3 phases of VTB Arena and Novion Business Center) and 1 small business center Gallery 76 of class B+ were delivered into the market. Thus, new construction of Q3 amounted to 47,000 sq. m, which is similar to the first half of the year.

Despite the fact that new construction in Q1-3 2018 turned out to be approximately equal to the same period of last year (93,000 sq. m and 115,000 sq. m, respectively), by the end of the year new construction will reach only 200,000 sq. m. Due to the fact that owners are aware of making decisions about the construction of large office buildings, office 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 most likely be properties after redevelopment / reconstruction.

New construction, class A and B



DEMAND

The activity of tenants is not as strong as in 2017, but nevertheless take-up remains at the natural Moscow level of 1.8-2 mn sq.m per year.

1,360

'000 sq. m

Take-up (lease and sale deals)

Q1-3 2018

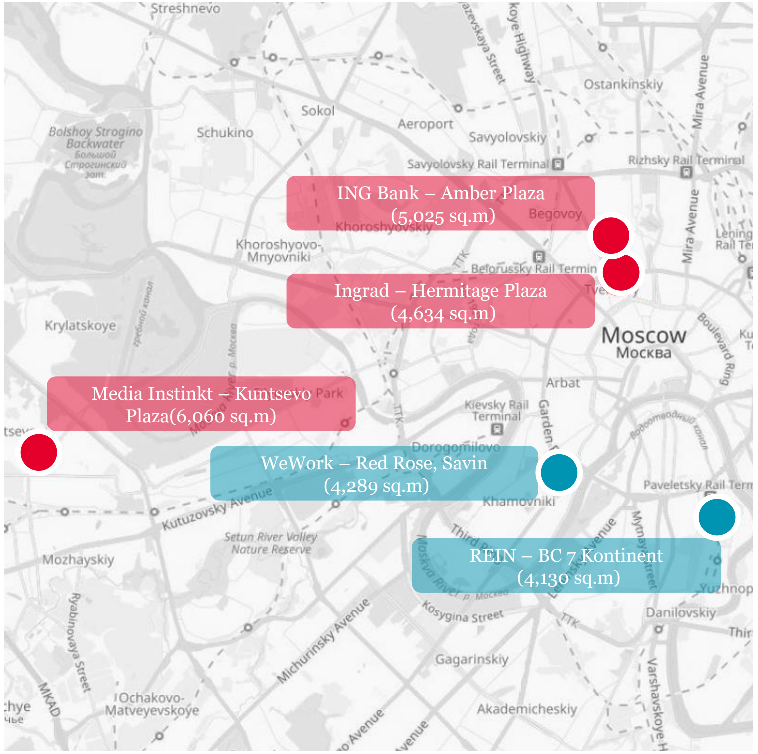
1,800

'000 sq. m

Take-up (lease and sale deals)

Forecast: 2018

Major deals in Q3 2018



In Q3, take-up amounted to 410,000 sq. m which is 20% lower than in Q1 and Q2. The decline was due to a decrease in demand in class B, while demand for class A continues to grow moderately. Tenants have taken advantage of recent opportunities associated with loyal rental conditions for the most high-quality premises.

The most active industries in Q3 2018 by number of deals were Banks and Finance (20%), Real Estate (16%), Equipment (10%).

In Q3, only 5 deals of more than 4,000 sq.m were carried out (on the map). Thus, the main demand by closed deals comes from blocks of less than 2,000 sq.m, only 25% of demand accounted for bigger blocks. Despite this, we are registering a local shortage in large consolidated blocks in the central area.

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.

POSITIVE ABSORPTION ESTABLISHED A FOOTHOLD

During 2018, some of the best vacant premises were taken off the market and more are expected to follow. Against the background of low construction activity and high demand, absorption will be growing.

201

‘000 sq. m

Absorption in Q1-3 2018

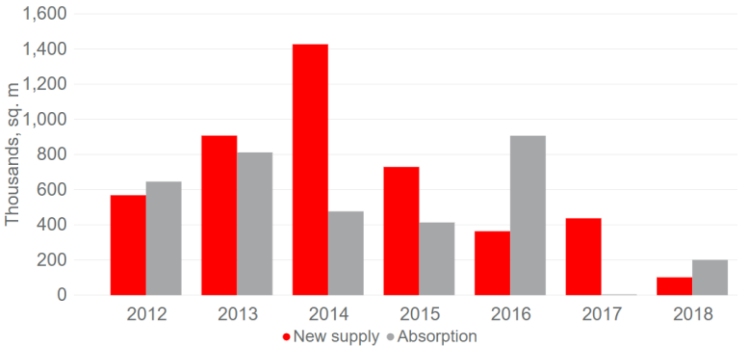
93

‘000 sq. m

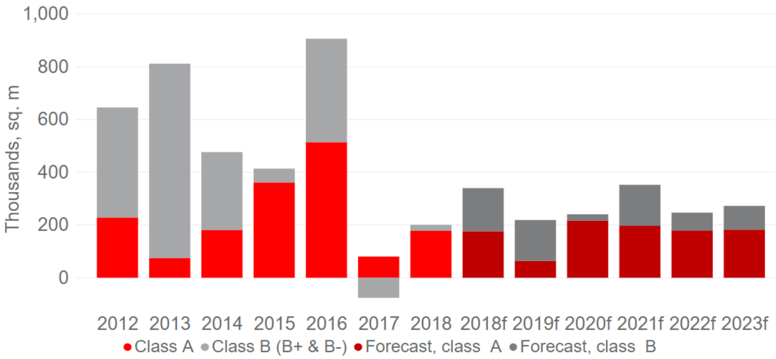
New construction in Q1-3 2018

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 SUPPLY

Since the beginning of 2017, the vacancy rate has been decreasing by 0.1–0.4 percentage points quarterly. At the end of Q3 the vacancy rate amounted for 11.7% (in class A, B + and B-) and will remain at this level until the end of the year.

11.7 %

Vacancy rate by the results of Q1-3 2018

Classes A and B (B+ & B-)

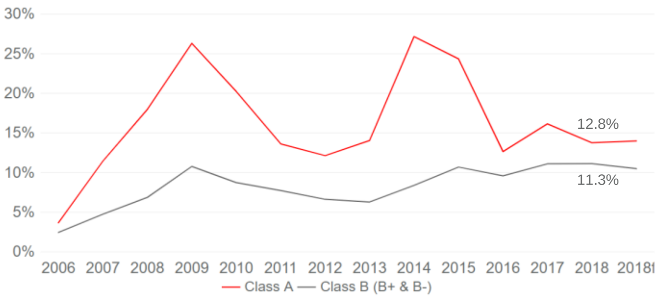
1.99 mn sq. m

Vacant premises by the results of Q1-3 2018

Classes A and B (B+ & B-)

Source: Cushman & Wakefield

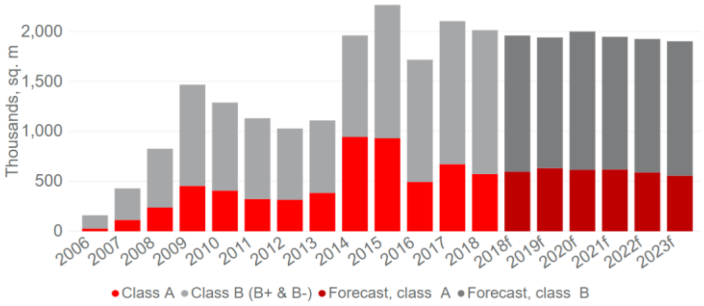
Vacancy rates



Due to a new record low figure in new construction and high take-up, the vacancy rate continued declining from the middle of last year. At the end of Q3 2018 the indicator amounted to 11.7% (12.3% in 2017).

Beginning in 2015, the vacancy rate in class A is gradually decreasing from the first quarter to the last, generally decreasing over the past 4 years at a similar pace. 2018 will be the next year with the lowest figures. In class B, the vacancy rate has been stable for the last 2 years.

Vacant premises



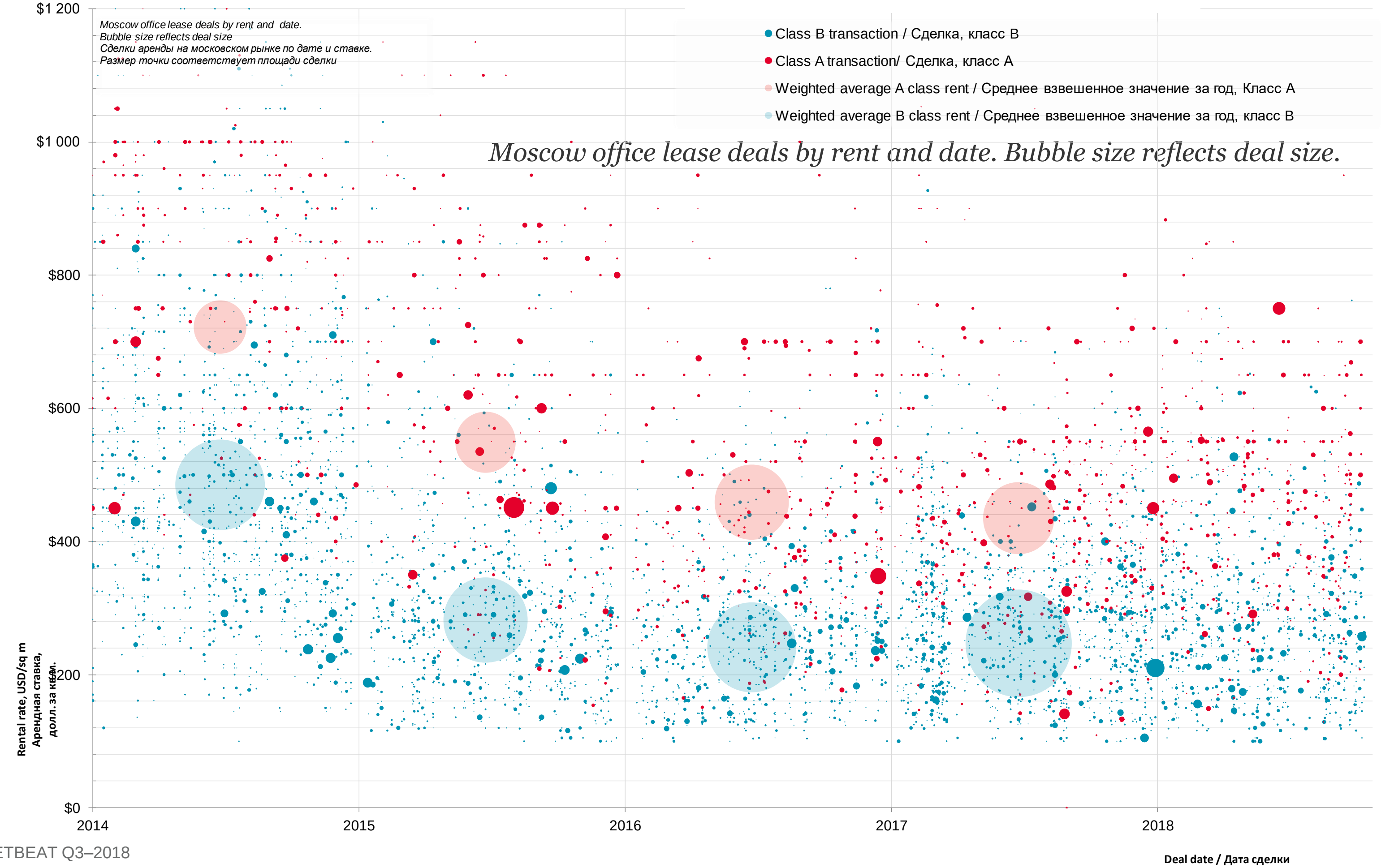
The vacancy rate in the center of Moscow (within the boundaries of the TTR) remains stable over the last year - about 10%, while the average vacancy rate outside the TTR has been decreasing since the beginning of 2017 (16.4% at the beginning of 2017 and 13.3% in Q3 2018). Due to the lack of big vacant blocks in the center, tenants pay more attention to location between the TTR and the MKAD. The vacancy rate in New Moscow is 30%.

LEASE DEALS IN MOSCOW

CUSHMAN & WAKEFIELD

45000

MOSCOW OFFICE MARKET DEALS
СДЕЛОК НА ОФИСНОМ РЫНКЕ МОСКВЫ



RENTAL RATES

Forecast: gradual increase of rental rates despite the volatility of the economy and geopolitical factors.

306

USD / sq. m annum

YTD 2018

Dollar equivalent (all deals in classes A and B)

18,829

RUB / sq. m annum

YTD 2018

Ruble equivalent (all deals in classes A and B)

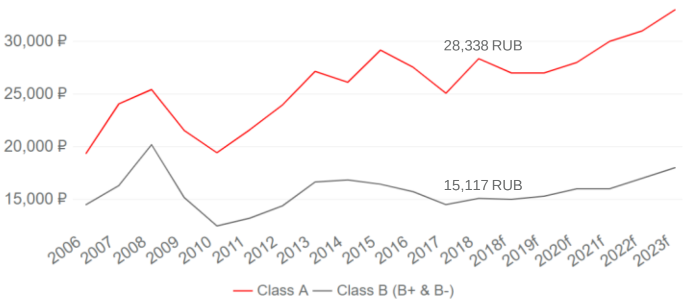
Source: Cushman & Wakefield

Rental rates in US dollars

The average dollar equivalent of rental rates in Class A (YTD 2018) is 466 USD/ sq. m/year (28,338 Rubles/ sq. m/year).

The average dollar equivalent of rental rates in Class B is 15,117 Rubles/ sq. m/year (244 USD/ sq. m/year).

Rental rates in Russian rubles



According to the results of the first 9 months, the average rental rate has increased. In Q3 rental rate grew due to the rise in class B, while in class A the average rental rate decreased slightly. In the coming years the average rental rate will continue to grow by 2-4 percentage points per year.

RENTAL RATES. DEALS CURRENCY

The share of deals in buildings with USD nominated rental rates in Q1-3 2018 is about 7% on average, which is still slightly higher than in the same period of 2017 (6.5%).

8.5 %

Share of USD deals (all lease and sale deals)

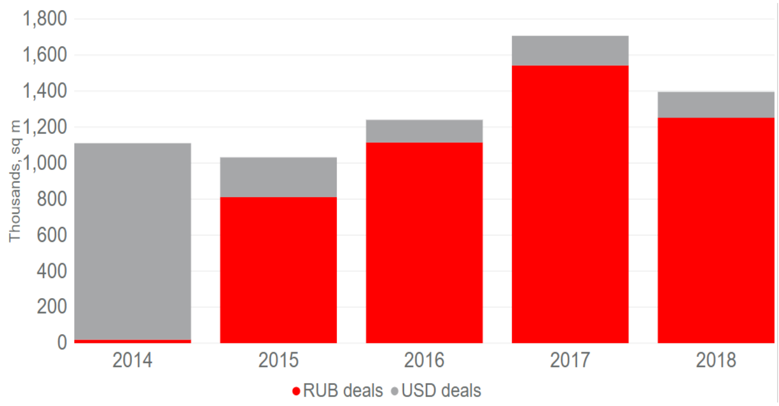
Classes A and B (B+ & B-)

Source: Cushman & Wakefield

Leasing demand and rental rates

Class	Deal currency	Deals volume, sq. m	Rate
A	USD	30,229	$543
	RUB	92,605	20,456 rubles
B+ & B-	USD	2,534	$570
	RUB	271,225	16,802 rubles

Leasing demand and rental rates



Section 2

RETAIL

- Active growth of the consumer market and optimistic forecast of the 2018 results are now turning to a slowdown next year.
- New sanctions at the end of this year, VAT increase and the following rise in prices from January 2019, and a rapidly growing consumer credit load will result in the decline of consumer confidence.
- New construction remains low.

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, Q1-3 2018

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

9.1 %

Vacancy rate

Quality shopping centers, Moscow

160 ‘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

#MARKETBEAT

SLOWDOWN OF THE CONSUMER MARKET GROWTH BY 2019

Starting from the middle of the last year, the retail turnover in Russia continues to grow. However, the consumer market growth will slow down in the next two years.

Forecast for 2018

2.9%

Retail sales growth

1.7% - Forecast for 2019

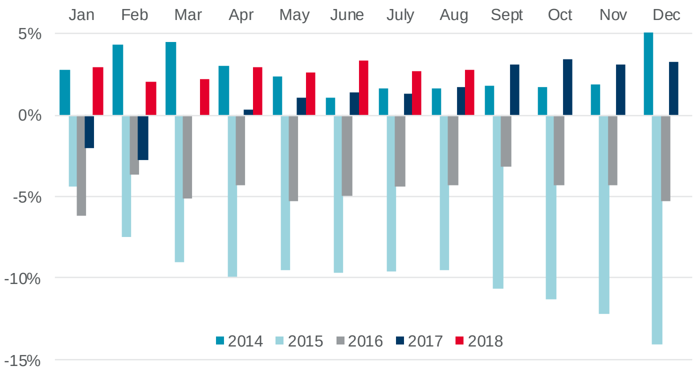
3.4%

Real disposable income

1.0% - Forecast for 2019

Source: The Ministry of Economic Development, October 2018 (base forecast), Rosstat

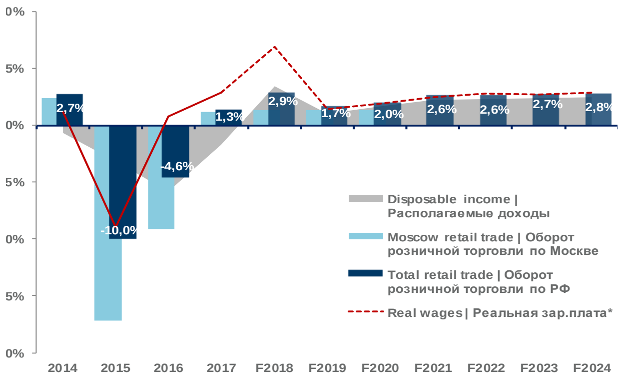
Retail Turnover in Russia



** Monthly change compared to the same period of the last year*

Starting from May 2017, retail turnover shows a positive trend. Against the background of a noticeable growth of real wages and growing consumer lending, average monthly growth of the retail turnover for Jan-Aug, 2018 is 2.7%. This allowed the Ministry of Economic Development to review the forecast upwards (from 2.0% to 2.9%).

Consumer Market



However, population surveys show declining consumer optimism caused by rising prices, taxes and more pessimistic expectations for short-term economic development. In 2019-2020, we will notice a slowdown of consumer activity growth.

Retail

WEAK CONSUMER MARKET WILL KEEP NEW CONSTRUCTION LOW

Around 2 mn sq. m of retail space is currently under construction. However, the opening of these projects will depend on the consumer market's activity. We expect that 700,000 sq. m will be delivered to the market in 2019.

IN 2018 NEW CONSTRUCTION WILL REACH A 10-YEAR MINIMUM

Construction activity will slightly grow in 2019, however against the background of slow consumer market growth there will be no return to the pre-crisis levels of construction.

264

'000 sq. m

New construction, Q1-3 2018

Russia (including Moscow)

450

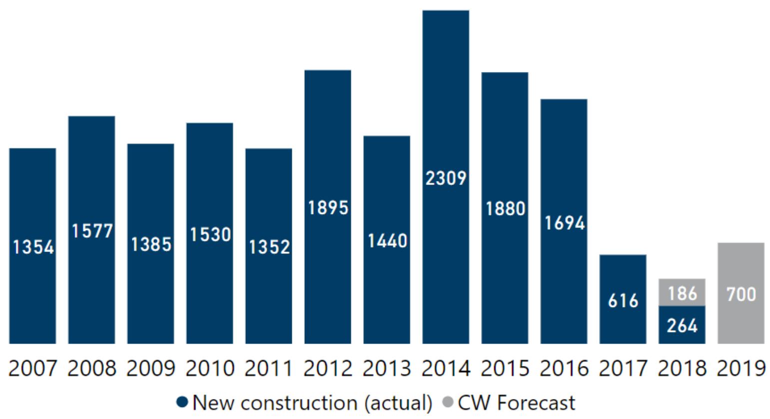
'000 sq. m

New construction, 2018F

Russia (including Moscow)

Source: Cushman & Wakefield

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

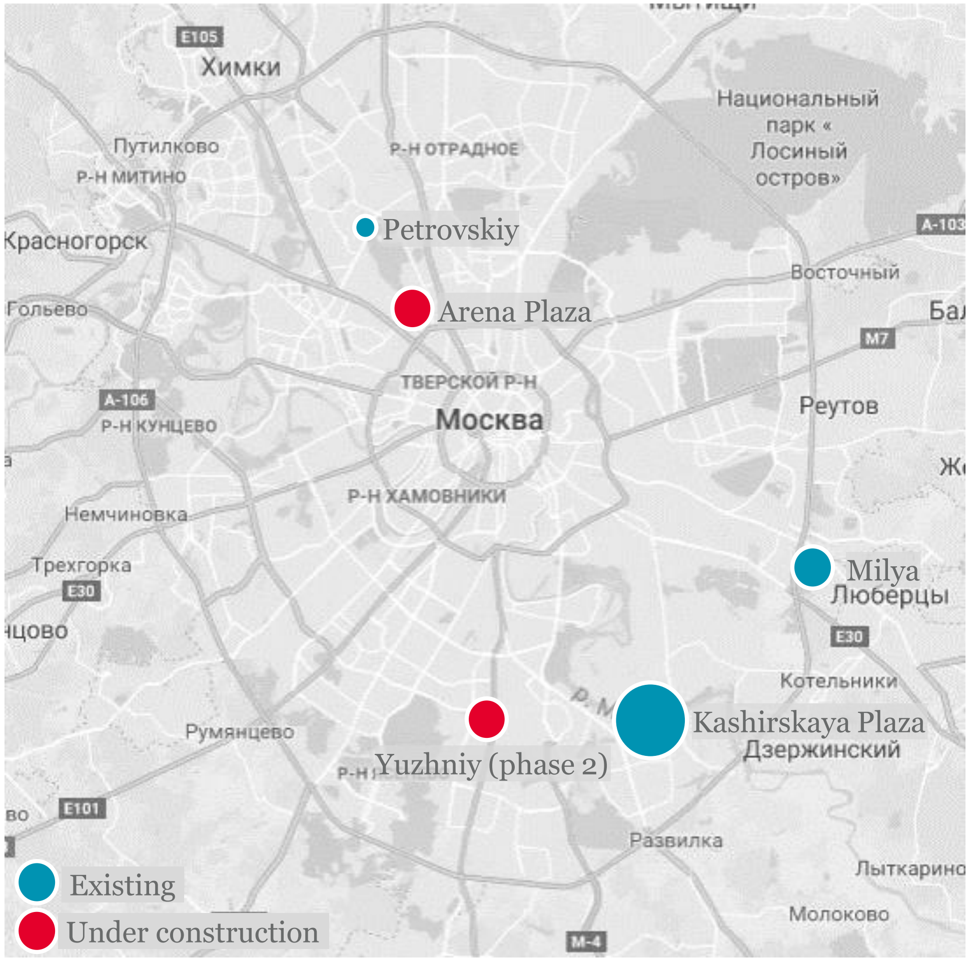


Source: Cushman & Wakefield

In Q3 2018, 3 shopping centers with total GLA of 91,000 sq. m were opened in Russia. Armada Capital (GLA – 60,000 sq. m) has the most significant share of this construction volume. In the regions, it is the largest opening in 2018.

The market is turning from quantity to quality growth. Many shopping centers are in the process of concept upgrade, outlet format which is relatively new for the market is actively developing. In Q3 2018, the second phase of Outlet Village Pulkovo (GLA – 6,700 sq. m) was delivered to the market; Brands' Stories in Ekaterinburg (GLA 10,000 sq. m) - the first outlet outside Moscow and St. Petersburg is expected to be opened by the end of the year. Two new outlets in Moscow and one in Perm were announced to be constructed.

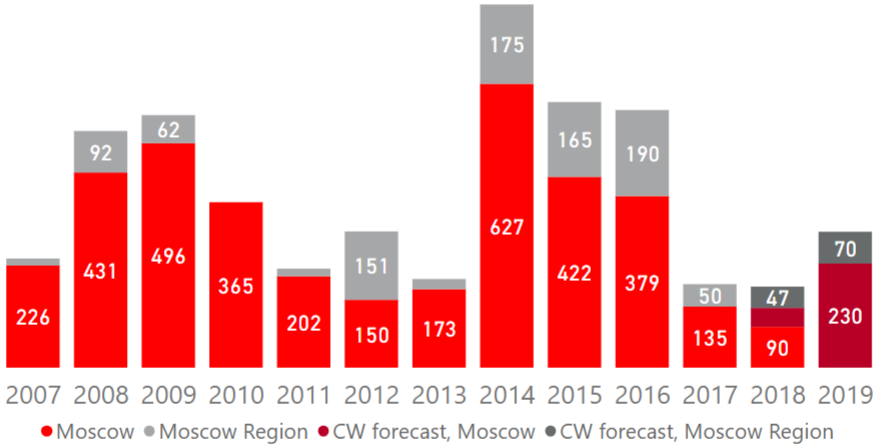
Shopping centers opened and planned for delivery in 2018 in Moscow



Retail

NEW CONSTRUCTION IN MOSCOW

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



No new quality retail scheme was opened in Moscow in Q3 2018. By the end of the year we don’t expect any large-scale shopping centers to be delivered to the market – only two small projects are planned for opening.

In the Moscow region, the biggest retail space increase is expected in Pushkino, where two shopping centers are planned for delivery in 2019-2020 – Pushkino Park (GLA – 30,000 sq. m) and Aquarelle (51,500 sq. m).

RETAILERS CONTINUE MODERATE EXPANSION

New brands are entering the market, both international and Russian

NEWCOMMERS, Q1-3 2018

Food retail is the most actively developing market segment. For instance, Vkusvill (originated from Moscow) is rapidly expanding – the chain increases its presence in St. Petersburg, installs vending machines at MCC stations, and started cooperation with Lavkalavka.

In order to optimize business and reach a wider audience, retailers are modifying the formats of their stores, also through space reduction. For example, IKEA is opening small design studios (150-200 sq. m) and Zamania is launching a small format of entertainment parks (900-1200 sq. m).

Large federal operators are introducing new brands – Sportmaster opened private label stores – Demix, Detskiy Mir plans to launch a chain of pet stores, Chitay Gorod opened a new shop of unusual things – Gogol Mogol.

CLOSURES, Q1-3 2018

New operators also appear in F&B segment – DoubleB opened a low-budget coffee shop - White by Double B, co-owner of Coffee Mania plans to launch a new brand – Hello People, and Azbuka Vkusa opened a café – AV Bistrot.

Besides newcomers, some international retailers returned to the Russian market (Orsay, Sephora). Mexx also announced its re-entry.

COMMERCIAL TERMS

In general, commercial terms remained at the level of the last year. The prime segment shows moderate growth.

160 '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 is at a stable high.
- Vacancy rate in the Moscow region is decreasing, asking rental rate is increasing.
- By the end of the year we expect record high take up in the Moscow region.
- Developers prefer built-to-suit projects to speculative construction.

MOSCOW, CLASS A

	Q1-Q3 2018	2018 (forecast)
Stock (‘000 sq. m)	10,250	10,639
New construction (‘000 sq. m)	340	728
Vacancy rate (%)	9	8.5
Rental rate * (RUB / sq. m / year)	3,600	3,600
Take up (‘000 sq. m)	1,126	1,500

REGIONS, CLASS A

	Q1-Q3 2018	2018 (forecast)
Stock (‘000 sq. m)	6,928	7,075
New construction (‘000 sq. m)	276	422
Take up (‘000 sq. m)	308	450

** Average rent excluding OPEX, utilities and VAT*

DEMAND FOR WAREHOUSE SPACE IS STABLE

Trends. Moscow and Regions

616

‘000 sq. m

New construction, class A

Moscow and the regions, Q1-3 2018

1,434

‘000 sq. m

Take up, class A

Moscow and the regions, Q1-3 2018

Source: Cushman & Wakefield

The demand for warehouse space in the Moscow region remains high. Throughout 2018, we see a growing take-up. This growth is caused by the increasing number of deals, while the average deal size decreased by 20% in Q3 2018 compared to the same period in 2017.

Against the background of high demand we see the asking rents increase – 10% in the last 3 months.

In the Moscow region, the vacancy rate is gradually decreasing. New tenants prefer built-to-suit to ready-to-move warehouses. After the decrease of the land prices, developers are offering to construct warehouses with good transport accessibility on land plots closer to MKAD.

Tenants have the beneficial option to move to more suitable and modern warehouse complexes.

The demand for warehouses in the regions is lower than in Moscow. In Q1-3 2018, take up decreased by 30% compared to the same period from the last year.

The situation with speculative construction in the regions is the same as in Moscow - developers prefer built-to-suit projects.

Large-scale warehouse complexes outside of Moscow were delivered in Kazan, Ufa, Khanty-Mansiysk, St. Petersburg.

Oktavian, class A (St. Petersburg)

Warehouse & Industrial

MOSCOW REGION

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

MARKET IS GROWING

In the Moscow region, rental rate is growing, vacancy rate is decreasing.

9 %

Vacancy rate, class A

October 2018

3 600

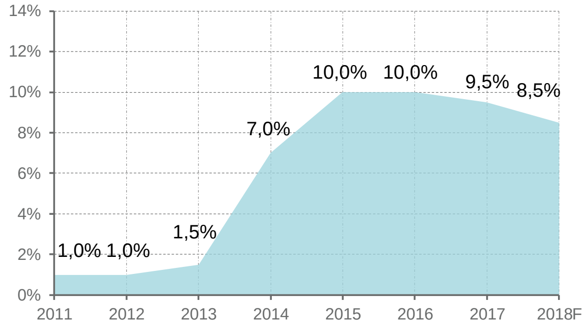
RUB / sq. m / year

Rental rate, class A

October 2018

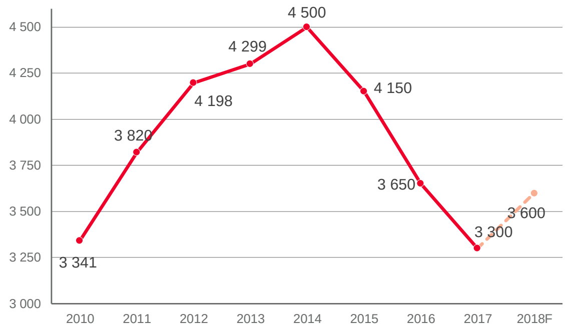
Source: Cushman & Wakefield

Vacancy rate, class A



The vacancy rate continues to decrease. At least half of the warehouse space planned for delivery in 2018 is under preliminary lease or purchase agreements. Tenants prefer to move into a new warehouse built according to their requirements, in a suitable location, rather than rent space in an existing warehouse complex. Therefore, the pace of vacancy rate decrease is slow.

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



Starting from the end of Q2 2018, we see an increase in asking rental rates – 10% in Q3 2018.

We expect rental rates to remain 3,600 RUB per sq. m per year by the end of 2018.

RECORD HIGH DEMAND FOR WAREHOUSES IN THE MOSCOW REGION

Supply and Demand. Moscow region

417

'000 sq. m

New construction, class A and B

Q1-3 2018

1,276

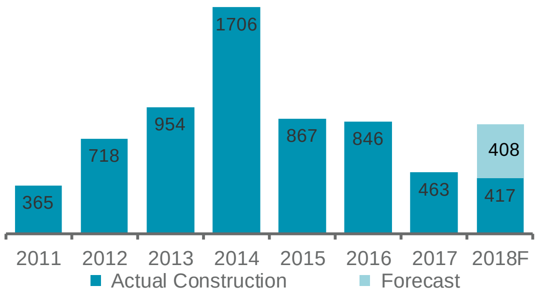
'000 sq. m

Take up, class A and B

Q1-3 2018

Source: Cushman & Wakefield

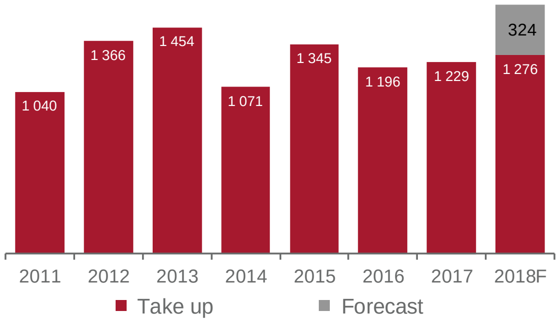
New construction, classes A and B, '000 sq. m



In Q1-3 2018, the supply of warehouse space increased by 417,000 sq. m. We expect 408,000 sq. m to be delivered to the market in Q4.

We predict that 826,000 sq. m of new warehouse space will be constructed in 2018 , which is almost two times higher than in 2017.

Take up, classes A and B, '000 sq. m



In Q1-3 2018, 1.3 mn sq. m of warehouse space was leased and purchased, which is 40% higher than the indicator in the same period of 2017. Take up has already been growing for 3 quarters.

We expect take up to comprise around 1.6 mn sq. m in total by the end of 2018 - the highest indicator for the last 10 years.

Warehouse & Industrial

RUSSIAN REGIONS

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

SEVERAL REGIONS EXPERIENCING DEFICITS

Supply and Demand. Regions

302

‘000 sq. m

New construction, class A and B

Q1-3 2018

324

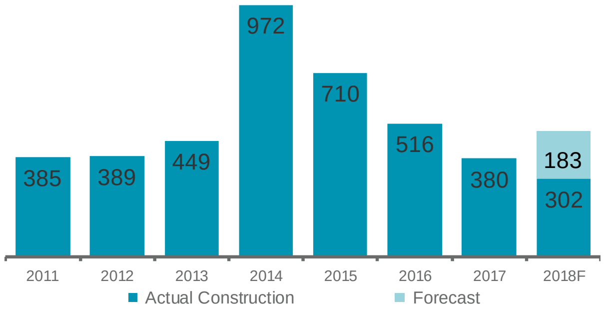
‘000 sq. m

Take up, class A and B

Q1-3 2018

Source: Cushman & Wakefield

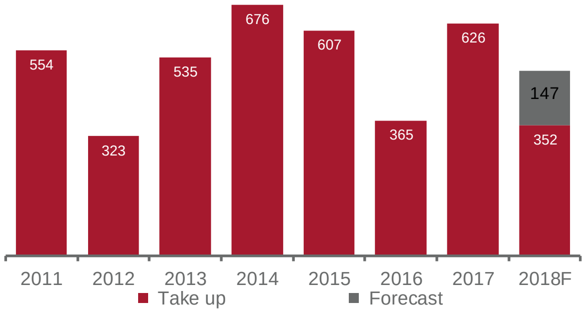
New construction, classes A and B, ‘000 sq. m



In Q1-3 2018, 302,000 sq. m of new warehouse space was constructed, which is 68% higher than in the same period of 2017. 70% of this space are built-to-suit warehouses that were constructed for large retailers.

Around 480,000 sq. m of space will be constructed in total by the end of the year – a 20% increase over the previous year.

Take up, classes A and B, ‘000 sq. m



In Q1-3 2018, 352,000 sq. m of warehouse space was leased or purchased, which is 30% less than the amount recorded from the previous year.

In Q3 2018, for the first time since the end of 2017, take up was higher than the same indicator from the previous year. However, we expect the yearly take up to be 25% less than in 2017.

KEY PROPERTIES

Supply and demand. Moscow and regions

Key warehouse properties opened and planned for delivery in 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	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

- Upon successful completion of the 2018 FIFA World Cup, over which , according to official reports, Moscow was visited by 3 million tourists, including 1.2 million foreigners (net of the CIS countries), lodging demand continued to grow – as demonstrated by the confident increase in Occupancy registered by Moscow hotels in July-September.
- Supply growth over 9 months of 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.
- YTD Sept 2018 results show continued growth both in Occupancy and ADR for the Wider market year-on-year. All this confirms city hoteliers' positive expectations for full-year results.

~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

19 500 keys

Modern quality room stock

Cushman & Wakefield's estimates, 9 months 2018

171 keys

In 1 new hotel

Net room stock increase over 9 months 2018

776 keys

In 3 new airport hotels

Net room stock increase over 9 months 2018

THE MORE AIRPORT HOTELS, THE MERRIER

Main supply increase – in the airport submarket.

171 keys

New supply in Moscow over 9 months 2018

1 new hotel

776 keys

New supply at Moscow airports over 9 months 2018

3 new hotels

Source: Cushman & Wakefield

New supply in Moscow in 2018

Hotel 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

Hotel 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**	

Hospitality

HOTEL SUPPLY GROWTH IS SLOWING DOWN - TEMPORARILY

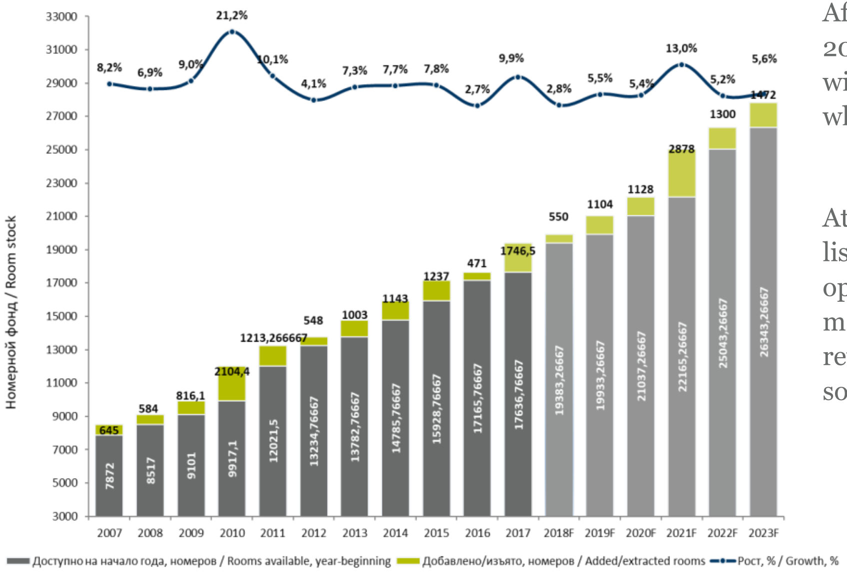
Growth rates are lower than in 2017 – but there is no reason to worry yet.

2.8 %

Year-to-year growth in 2018

Expected market growth rate vs. 2017

Supply growth dynamics – actual and projected



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 1,100 keys per annum as soon as in 2019.

Source: Cushman & Wakefield

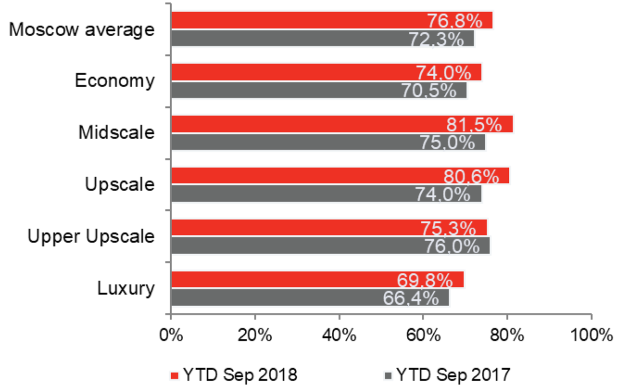
NO LOSERS IN SIGHT

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

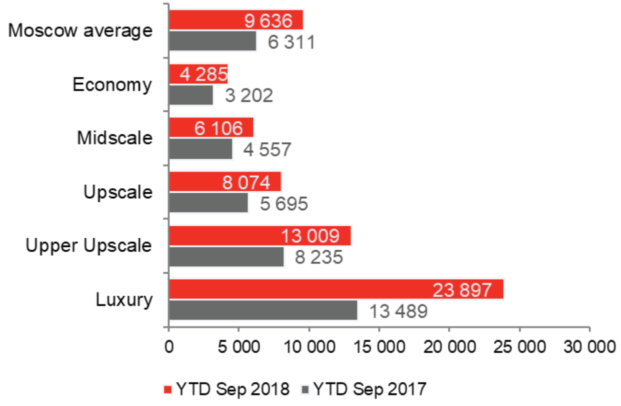
76.8 % Occ, YTD Sept 2018
Wider market

52.7 % Change in ADR (RUB), YTD Sept 2018
Wider market

Occ, YTD Sept 2018, by segment



ADR (RUB), YTD Sept 2018, by segment



The average Occ level for the Wider market over the first 9 months of the year reached 76.8%, which is 4.4 percentage points higher than a year ago. The most popular hotels with the highest levels of Occupancy were Upscale and Midscale properties, registering 81.5% and 80.6%, respectively. The only hotel segment which had a decline in Occupancy levels were Upper-Upscale properties (-0.7 pp.), although such a minor adjustment is hardly a loss.

The “Championship effect” continued to affect ADR levels across all price segments, with the average growth rate for the Wider market reaching 52.7% (from 6,311RUB in 2017 to 9,636RUB in 2018), with the highest increase attributable to the Luxury segment (+77.2%, to 23,897RUB).

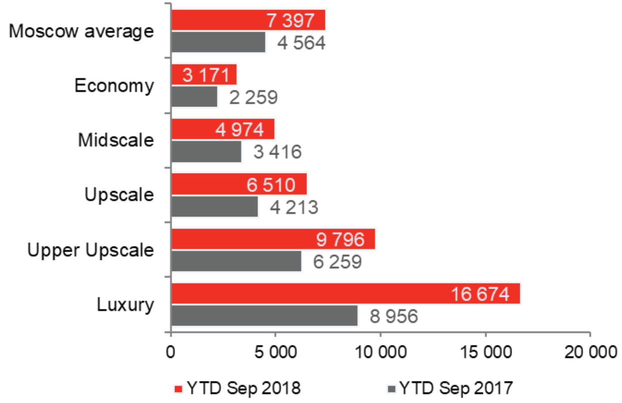
Source: Cushman & Wakefield

EXCELLENT GROWTH OF ROOM YIELD

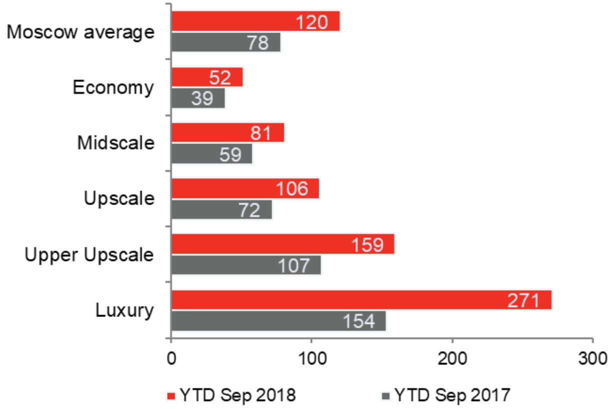
62.1 % **Change in RevPAR (RUB),YTD Sept 2018**
Wider market

53.9 % **Change in RevPAR USD), YTD Sept 2018**
Wider market

RevPAR (RUB), YTD Sept 2018, by segment



RevPAR (USD), YTD Sept 2018, by segment



Moscow hotels were very 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 room nights.

As a result, the Wider market RevPAR over first 9 months of the year grew both in RUB and in USD.

Source: Cushman & Wakefield

AND WHAT IF 2018 FIFA WORLD CUP IS PUT ASIDE?

Stunning success for Moscow hotels during the group matches.

85.9 %

Sept 2018 Occ, year-on-year

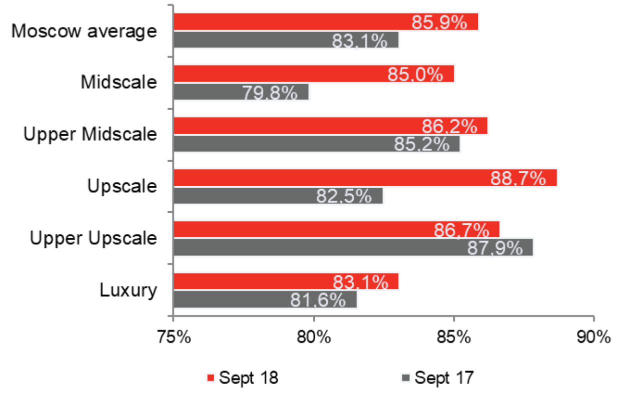
Wider market

6.8 %

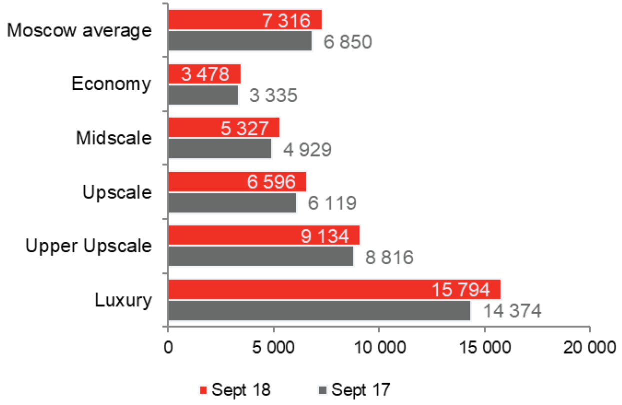
ADR (RUB) change, Sept 2018, year-on-year

Wider market

Occ, Sept 2018, by segment



ADR (RUB), Sept 2018, by segment



Any concerns over the market's slow path of bottoming out after the fantastic success of the 2018 FIFA World Cup proved wrong – as soon as September, the Wider market boasted impressive growth rates both in Occ as well as ADR levels.

The absolute champions were the Upscale hotels which managed to have a 15.9% increase in RevPAR by pushing both Occ (6.2 pp) and ADR (7.8%). They were closely followed by Luxury and Economy hotels (11.9% and 11.1%, respectively).

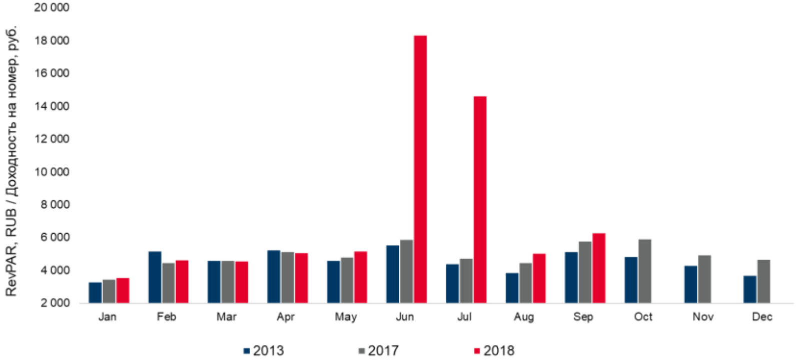
The worst change in RevPAR was recorded in the Upper-Upscale segment where properties had a negative dynamics in Occ (-1.2 pp) on the back of a rather weak ADR growth (3.6%), resulting in a disappointing 2.2% increase of Room Yield.

Source: Cushman & Wakefield

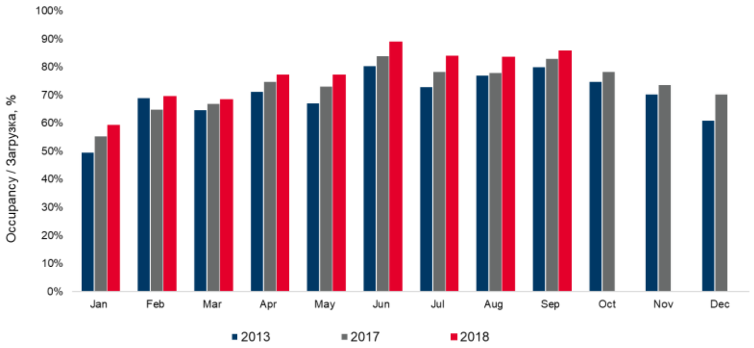
IS THERE LIFE AFTER A MEGA-SPORTING EVENT?

Should the market expect positive trends to continue after 2018?

Occupancy dynamics, %, by month



RevPAR dynamics (in RUB), by month



Despite the widely expressed concerns of a drop in Occ between the end of the 2018 FIFA World Cup and the normal course of business, the operating results of the Moscow hotels showed that accommodation demand in July-September remained strong. Instead of a loss of room nights, the market kept gaining room nights sold over the remainder of the summer season as well as in September – a clear gain not only vis-à-vis 2017 but also against 2013, widely seen as the benchmark year. Stability of demand enabled the hotels to continue pushing room rates which resulted in RevPAR growth beyond the 2018 FIFA World Cup period. Clearly, 2018 has all the chances of turning into one of the most successful years in the modern development period of Moscow. So, what's next?

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%

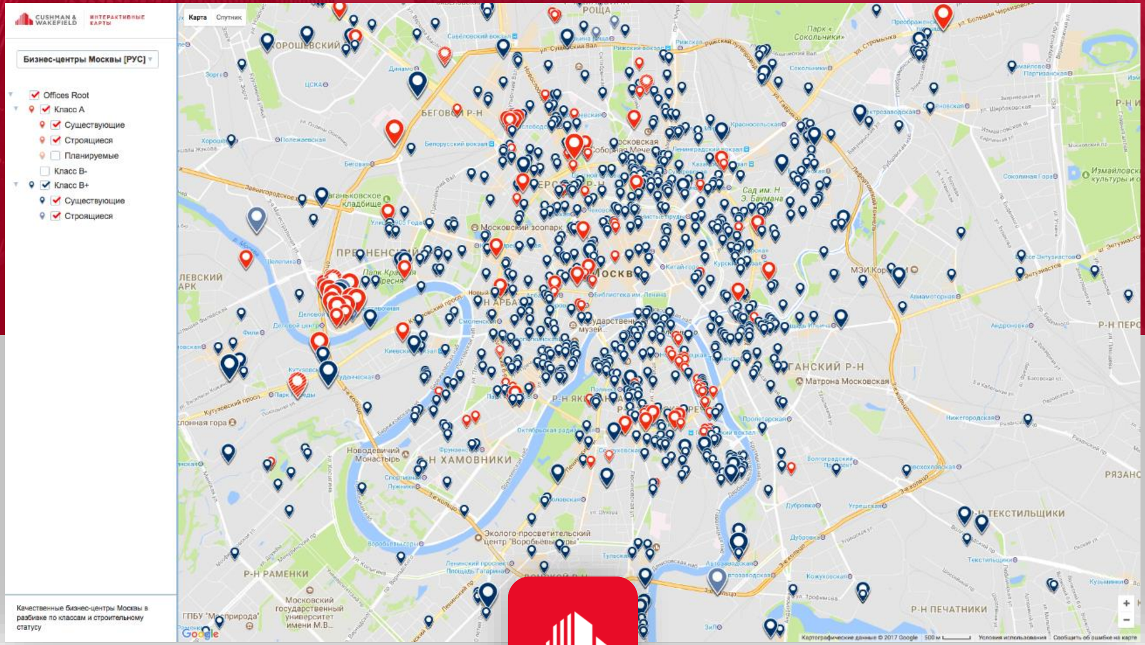
Cushman & Wakefield in Russia

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

CUSHMAN & WAKEFIELD IN RUSSIA

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About the company

CUSHMAN & WAKEFIELD IN RUSSIA

Cushman & Wakefield has been successfully operating in Russia since 1995, with employees more than 150 experienced and highly qualified experts. The Moscow office implements projects in all major cities in Russia and the CIS, forming transnational teams for solving complex tasks when necessary. There are 12 key areas of company activity, covering all the sectors of commercial real estate: offices, retail, warehouses, hospitality and tourism, land. The range of services provided includes the leasing of spaces, asset management, investment consulting, real estate operation, services for corporate clients, project management, development consultancy, representing tenant's interests, valuation, hospitality and tourism. Cushman & Wakefield is one of the largest companies in the global commercial real estate market, with a turnover of $6.9 billion and a team of more than 48,000 specialists in more than 400 offices in 70 different countries. For more information, visit our websites – www.cwrussia.ru and www.cushmanwakefield.ru

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