

Commercial Real Estate - Russia

# #MARKETBEAT

Cushman &amp; Wakefield Research Department

Macroreview

Capital Markets

Offices

Retail

Warehouse &amp; Industrial

Hospitality &amp; Tourism

# Jul '20

# Q2 2020

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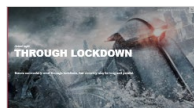
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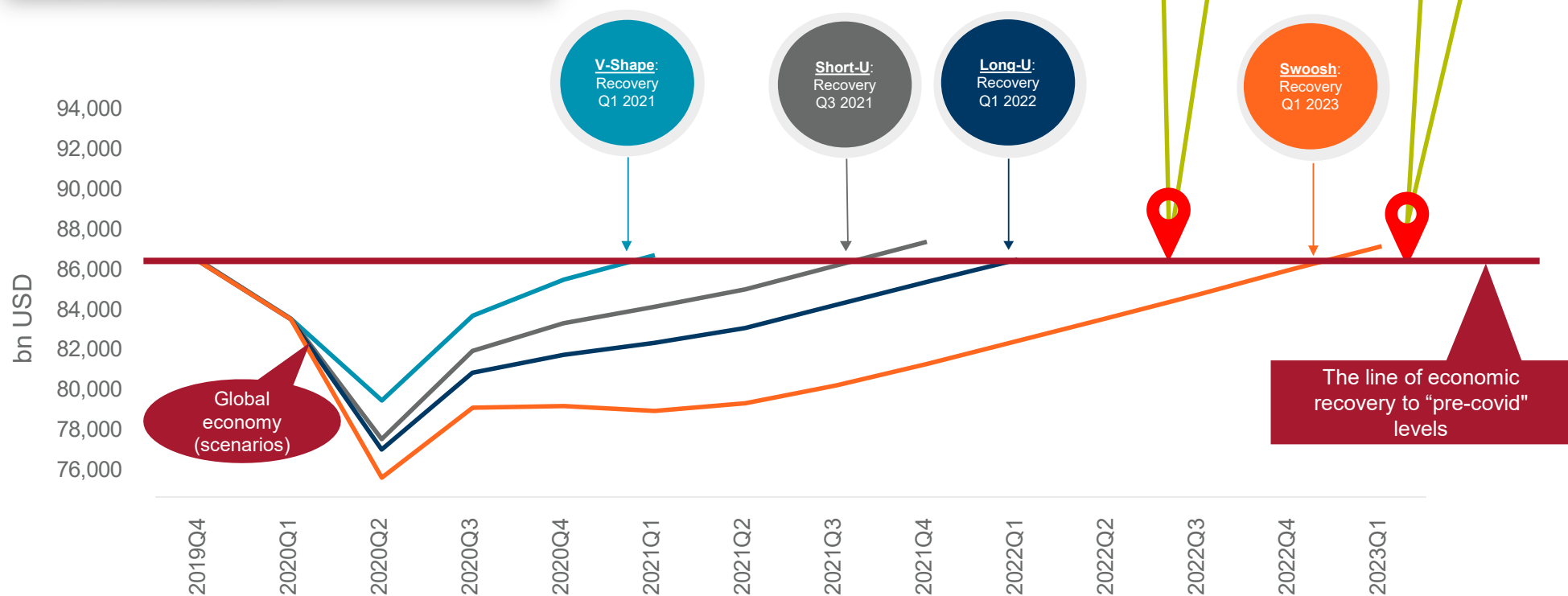
# GLOBAL CONTEXT

In spring and summer 2020 Russia is facing the same challenges as other countries. For the first time since sanctions Russia joined global trends.

# LONG WAY BACK

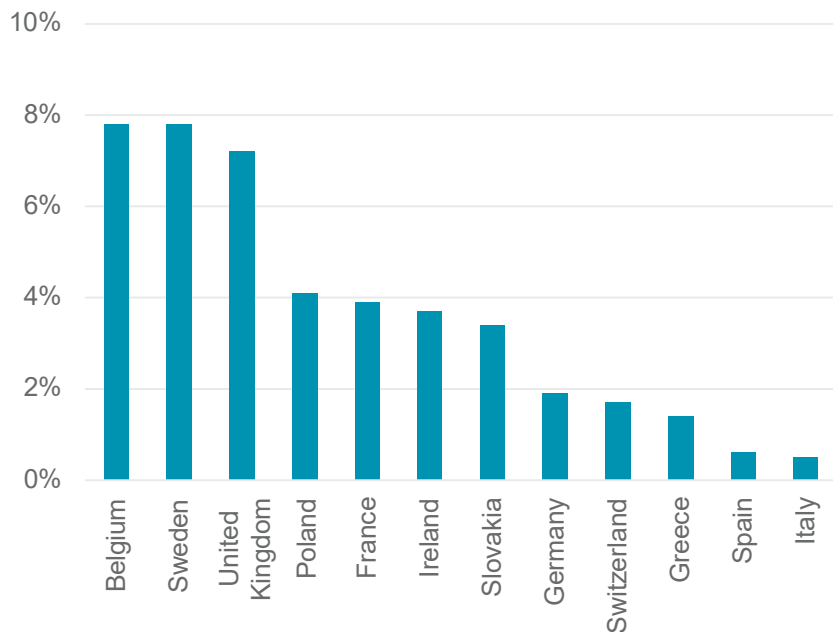
## Global GDP in real terms

Russia has been successful in mitigating the impacts of the pandemic. However, structural problems in the economy will restrict the speed of the post-COVID recovery.



# REMOTE WORK STATUS

% of employees working remotely in 2019  
(before the pandemic)



## BUSINESS BAROMETER

# 30%

believe that 100% of employees will return to the office after the restrictions are lifted

Remote work in Russia was extremely unusual before 2020 with less than 1% of employees working remotely, but the pandemic will change the game.

In May 50% of business barometer respondents were expecting that 50% of staff will stay at home offices.

# INVESTMENT ACTIVITY IN EASTERN EUROPE REMAINS STRONG

Russia is the third largest investment market in the region.

## -7%

Investment volume in CEE  
In H1 2020 compared to H1 2019

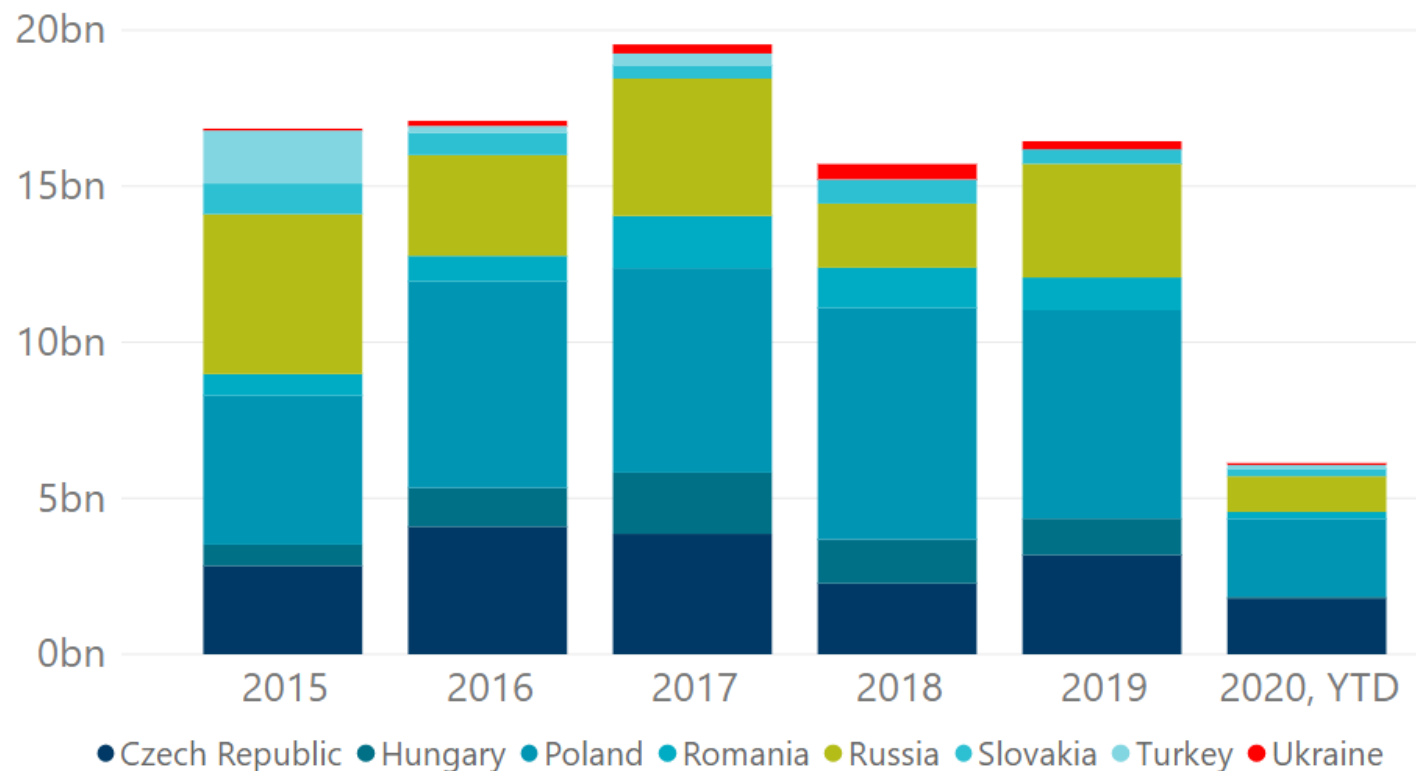
## 2.5

bn EUR  
Investment volume in Poland in H1  
2020

**REAL** CAPITAL ANALYTICS

Source: Real Capital Analytics

Investment volume in the core CEE markets, H1 2020, EUR



# HIGH INVESTMENT ACTIVITY IN RUSSIA IN H1 2020

The lockdown will lead to a slight decrease in activity in H2 2020. Annual investment forecast is decreased.

## +20%

Investment in Russia

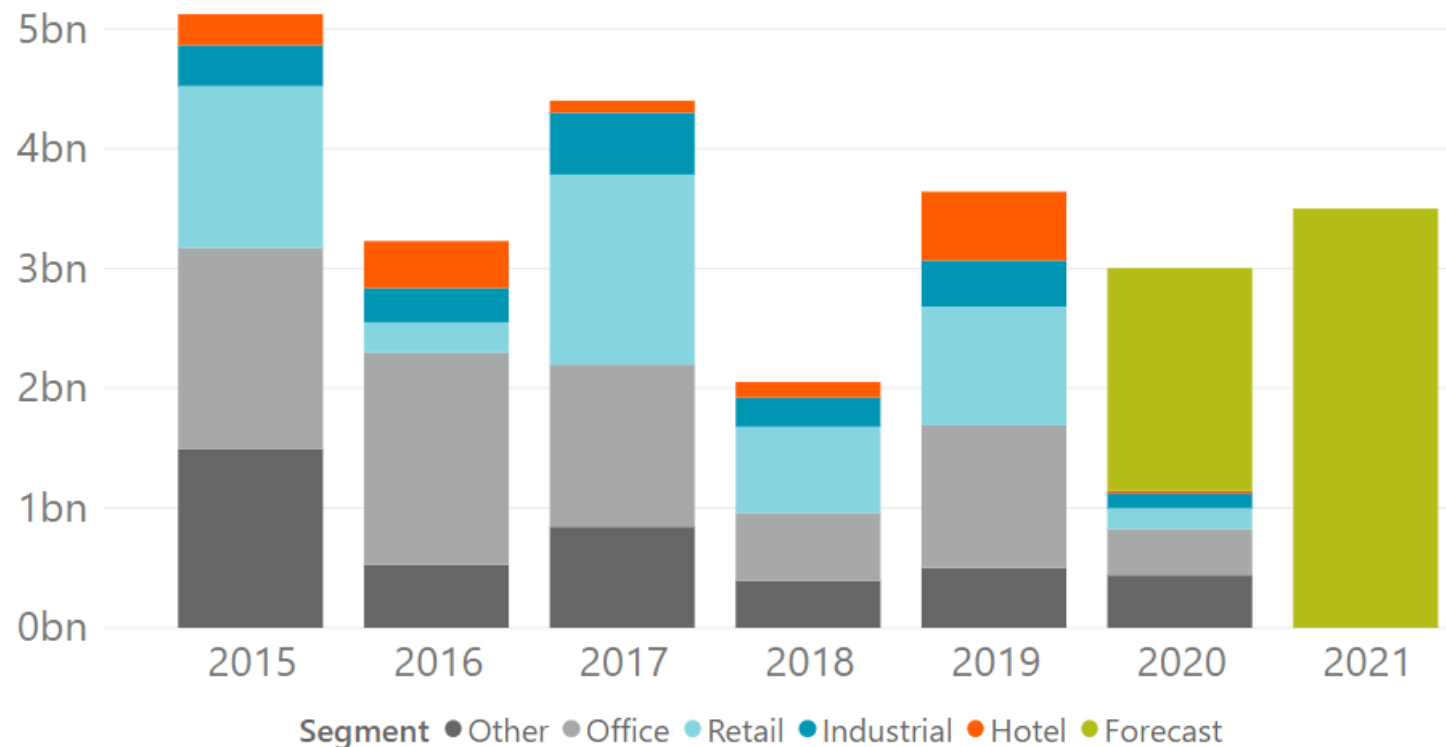
In H1 2020 compared to H1 2019

## 3

bn EUR

Investment in Russia, Forecast for 2020

Source: Real Capital Analytics, Cushman & Wakefield



# GLOBAL AND LOCAL TRENDS

Global trends and Russian realities

GLOBAL TREND	RUSSIAN REALITIES	COMMENTS
Death of weak business	Small and medium businesses are the most vulnerable	Large conglomerates will receive state support
Suburban revival	Citizens are moving out of city center	For the last 10 years urban development was focusing on central parts of big cities leaving suburban areas heavily underdeveloped. Now the demand for quality dwellings will shift to the outskirts.
On-shoring of production	Localization	Localization program runs for 5 years already
Gateway cities	Sub-million cities in Russia get their chance in the fight for talent	Remote work gives chance smaller cities, less costly to live in to successfully compete for talents with Mega-cities.
Datacenters boom	Strong shift towards “digital state” and additional demand driven by dataflow regulation.	There are likely to be datacenter network development projects across Russia.



# GLOBAL AND LOCAL TRENDS, PART 2

Global trends and Russian realities

GLOBAL TREND	RUSSIAN REALITIES	COMMENTS
Automatization	National Projects, State Corporations	This trend will be channeled through government programs.
Growth of state debt	In Russia the National Debt is low and RUB is underappreciated.	Limited support measures made Russia exempt from global trend for growing national debt.
End of open space	Open space was not yet common in all Russian companies	Maybe old style "corridor" offices will be transformed into modern shared space
Sectoral growth	State companies and natural resources monopolies will gain more power	State companies will benefit from multiple growth drivers.
Experience retail	Cold climate makes shopping malls an important part of urban structure	Shopping centers will need a new focus and most likely Russian retail formats will diverge from global standards as consumer behavior becomes more "domestic"



## NEW!

*For insights on global trends and changes on the real estate market watch IQ Interview with Andrew Phipps, Head of Business Development in EMEA and Local Markets and Global Futurist in Cushman & Wakefield. To watch please follow [the link](#).*



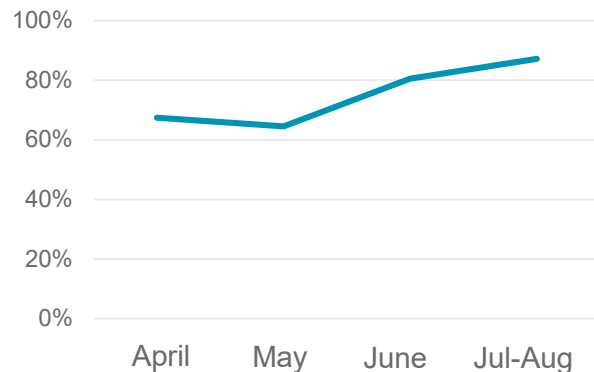
*Actual topic*

# THROUGH LOCKDOWN

Russia successfully went through lockdown, but recovery may be long and painful.

# CUSHMAN & WAKEFIELD BUSINESS BAROMETER

## Business activity index

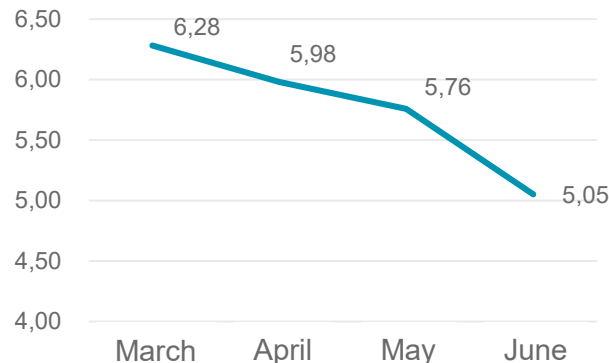


Activity index reflects evaluation of current business activity of the company as % of nominal

In June business activity accounted to 90% of nominal. May was the lowest month with 64% of business activity. However, May with its long holidays had always been the weakest month for Russian business.

Companies were successful in preparing themselves to lockdown.

## COVID pessimism index



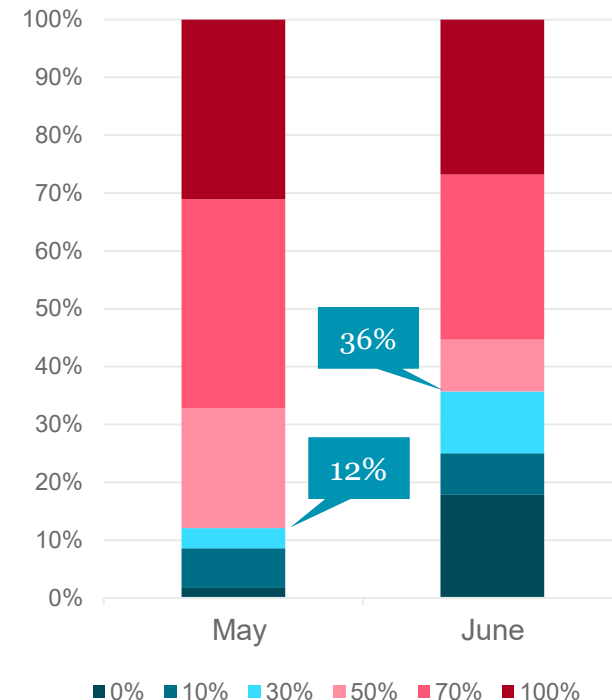
Covid pessimism index reflects the expectation of the pandemic impact on the business (the scale is from 1 (no impact) to 10 (catastrophic impact)).

In June pessimism evaporated as businesses started opening and activity increased.

## BUSINESS BAROMETER

Detailed report is [HERE](#).

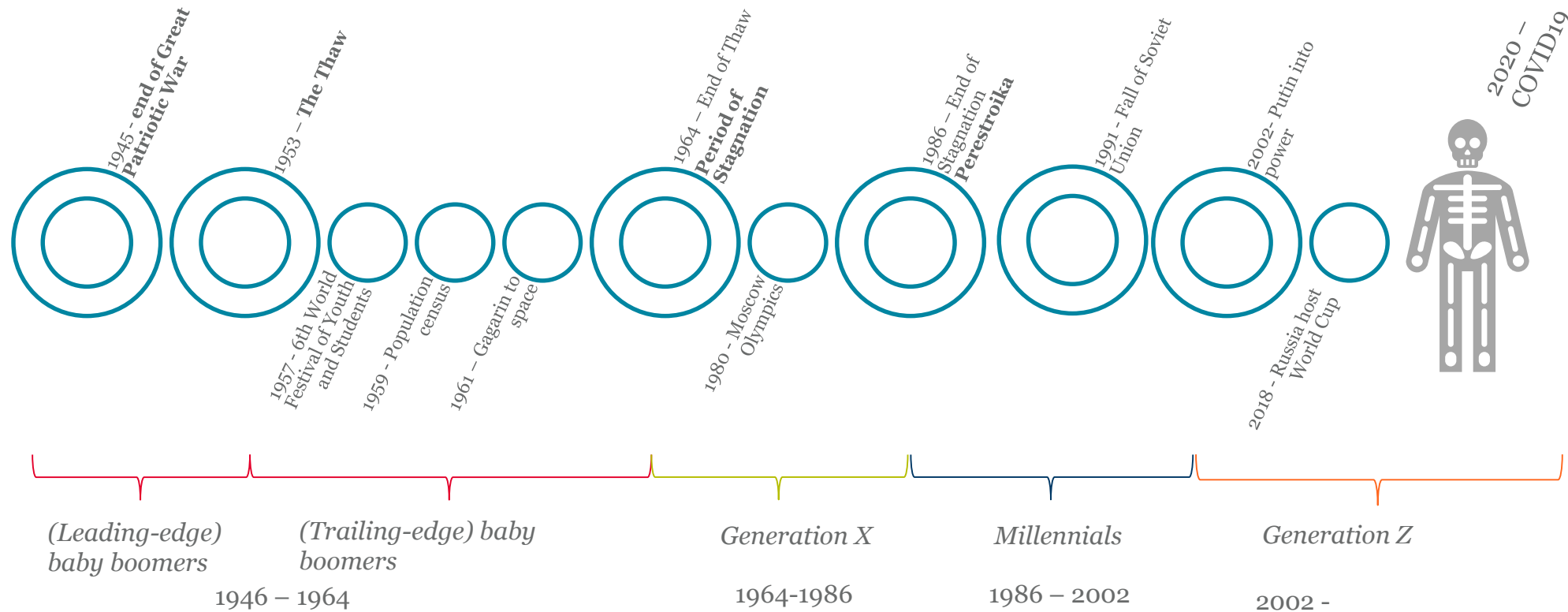
## What percentage of employees will return to the office?



Businesses re-evaluated their approach to remote work. In May only 12% were expecting that the majority of staff will work from home. In June 60% said that work from home will become dominating trend after pandemic.

# COVID GENERATION?

The key events that have helped to forge different generations in Russia.



# FUTURE = DEURBANIZATION + SUBURBANIZATION?



## Density

There is no evidence that infections are higher in dense areas. But affluent neighborhoods suffered less.



## Education and innovation will become new anchors

Suburban locations focused on science, innovation, education offering higher life standards are more attractive.



## Accessibility

Suburban life has to rely on private cars which contradicts global trends.



## Young talents prefer to work in downtown

C&W research shows that 80% of young professionals prefer downtown office locations.



Suburban living – new chance or trap for citizens [Marketbeat.Live](#)





# POST-COVID STRATEGY IS NOT A PLAN BUT A MUSCLE

Most advanced businesses used lockdown to train themselves for innovation and flexibility

## Section 1

# MACROREVIEW

- Russia is expected to fully recover by mid 2023.
- Conservative spending policy restricts government expenses from growth.
- Inflation target is set at 4% and most likely will be achieved.
- Shrinking demand together with growing costs along the whole supply chain will lead to stagnation in output.

## MACRO INDICATORS

	2019	2020	2021	2022	2023
GDP growth, %	1.3	-6.2	3.5	2.1	3.0
RUB/USD	64.7	69.2	67.6	68.1	68.5
CPI, %	4.5	3.5	4.1	3.6	3.9
GDP deflator, %	4.7	-7.1	4.8	8.8	5.6
Interest rate, %	8.84	7.0	6.4	7.4	7.7
Current Balance, % of GDP	1.9	-5.2	-4.1	-2.1	-1.4
Private consumption, %	2.5	-7.2	7.0	2.9	1.5
Government spending	2.1	-2.7	1.0	0.9	0.7
Capital outflow, bn USD	4.6	6.0	5.2	5.2	5.2
Unemployment rate, %	64.4	41.1	48.2	49.4	53.2
BRENT crude oil price	1.3	-6.2	3.5	2.1	3.0

Source: Oxford Economics 26.06.2020



## IT CAN TAKE A LONG TIME FOR RUSSIA TO GET OUT OF THE CRISIS

**-6.2%**

GDP fall in Russia

In 2020

**0.7%**

Average annual GDP growth

In the second decade of XXI

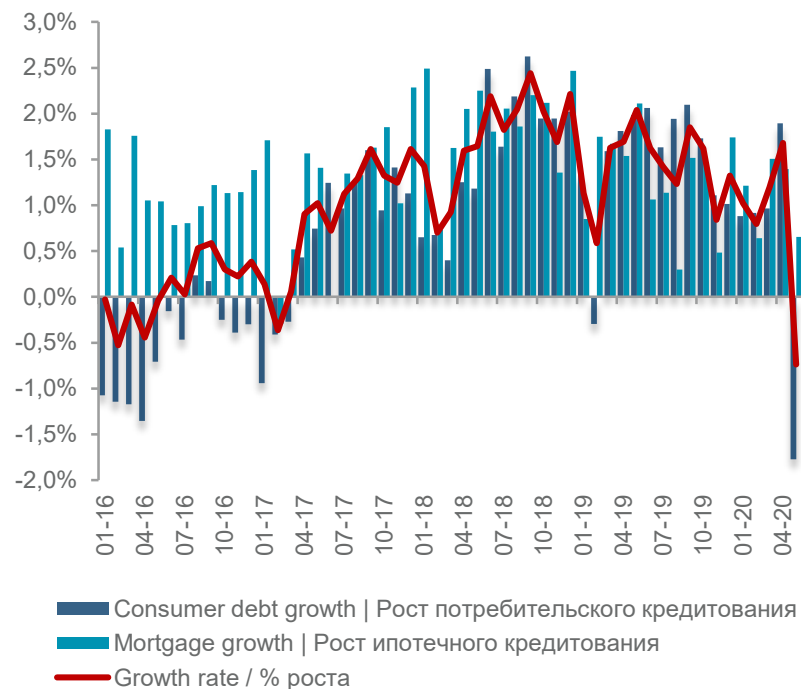


Source: Rosstat, Oxford Economics

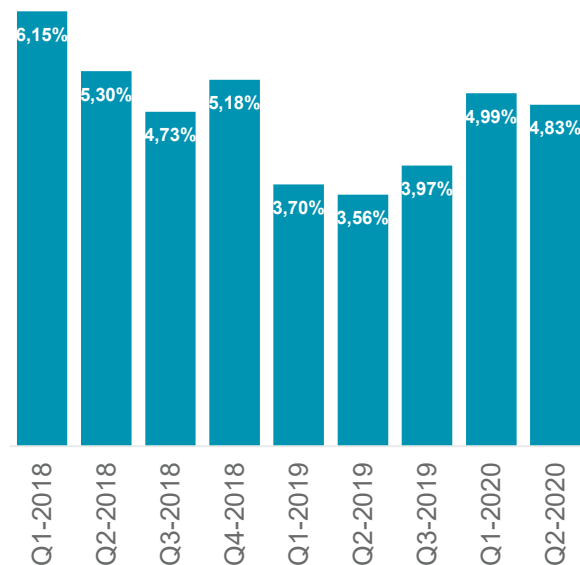
# RESIDENTIAL AS A NATIONAL IDEA AND PROJECT

Residential market remains strong. High rate of premature repayment of mortgage debt supports growth potential for mortgage market and residential construction.

## Monthly change in consumer and mortgage household debt



## Premature mortgage repayment, % of total debt



In April household consumer debt lost almost 2% due to retail stores lockdown. Also people had to cancel their vacation plans for summer 2020.

At the same time mortgage debt gained 0.7%.

Almost 5% of total mortgage debt is paid back prematurely each quarter which makes almost 20% annual premature repayment rate.

High repayment rate reflects healthy state of the market and relatively high quality of mortgage debt.

## Section 2

# OFFICES

- Vacancy rate increased by 2 p.p compared to 2019.
- The forced shutdown of construction sites and local lockdown led to low level of construction activity. In Q2 2020 only 2 buildings with total office area of 5,121 sq. m were delivered to the market.
- Office indicators forecast was corrected downward.
- In H1 2020 take-up decreased by 4.3% compared to H1 2019.

## MOSCOW Q1-2 2020

Classes A, B+ & B-

**18.4** mn sq. m

Total stock of office buildings

**94** '000 sq. m

New construction

**2.1** mn sq. m (11.6%)

Vacancy

**840** '000 sq. m

Take-up

**9%**

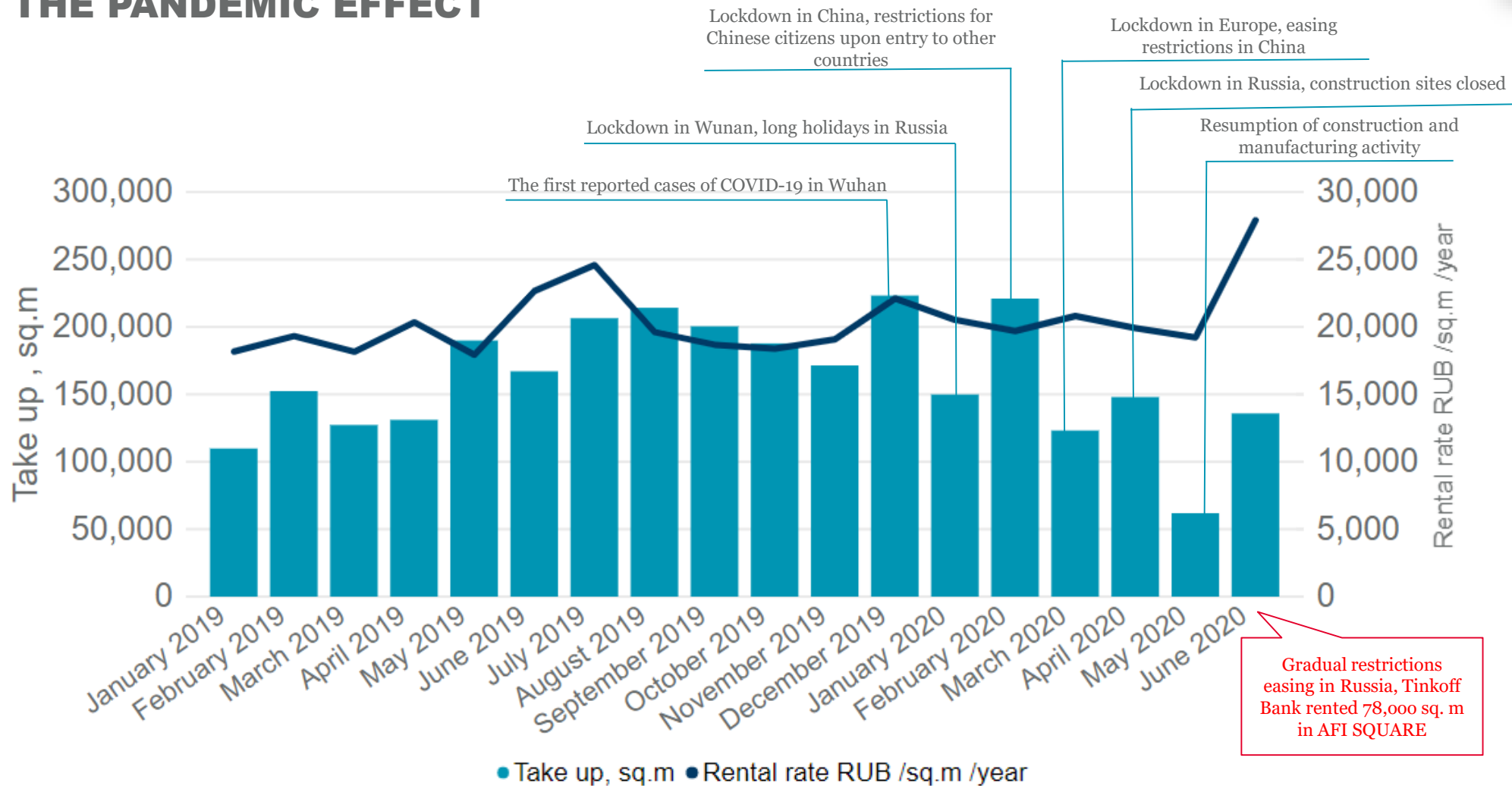
Capitalization rate, prime office segment

*Offices*

# OFFICE MARKET WILL SHOW POSTPONED RECOVERY IN Q3-4 2020

The pandemic effect was most noticeable in May. The market indicators will stabilize by the end of the year.

# THE PANDEMIC EFFECT





## THE PANDEMIC EFFECT: HOW QUICK WILL THE RECOVERY OCCUR?

Despite the negative dynamics of office indicators, demand for large offices is still noticeable.



Tinkoff Bank rented 78,000 sq. m in AFI SQUARE (Class A). That is one of the most outstanding deals in the office market history and it affected significantly the YTD average rental rate.



## NEW SUPPLY

New construction of Q2 2020 covered only 5% of H1 2020 new construction. Low level of construction activity is a result of forced shutdown of construction sites and local lockdown.

# 94

'000 sq. m

New construction

Jan-June 2020

# 195

'000 sq. m

New construction

2020F

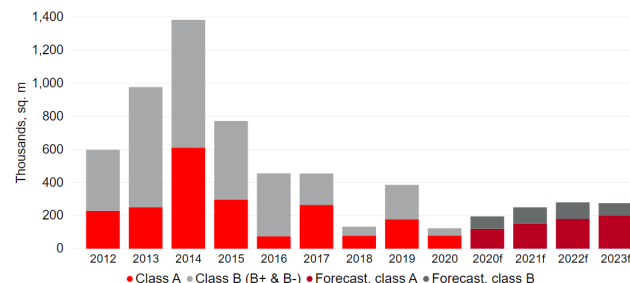
Source: Cushman & Wakefield



94,000 sq. m were completed in Jan-June 2020. All new properties are located in the South and South-West of Moscow. Suvorov Plaza, that is fully occupied by Sberbank, represents 36% of YTD new construction.

In Q2 2020 two office buildings of Class B were delivered and new construction amounted to 5,121 sq. m.

## New construction, Classes A and B



Quarantine measures and forced shutdown of construction sites led to the decrease in construction activity. Some completions will be postponed until the next year due to economic turbulence and business activity slowdown.

The new construction forecast was reduced. We expect 195,000 sq. m of new office space in 2020. Gradual recovery of construction activity will take place in 2021 - 2023.

## DEMAND

The dramatical decline in year-on-year take-up has not occurred while one of the most outstanding deals in the market history was signed.

# 840

## '000 sq. m

Take-up (lease and sale deals)

Jan-June 2020

# 1.53

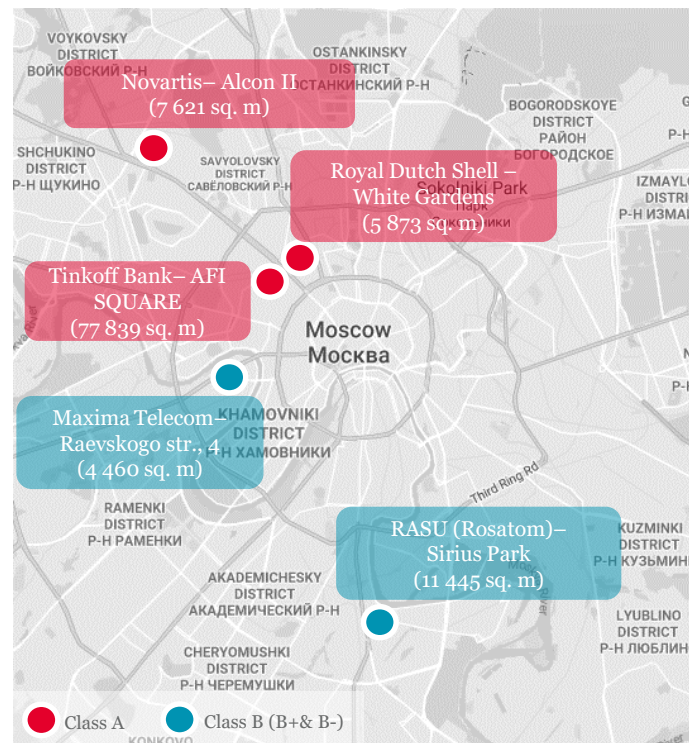
## mn sq. m

Take-up (lease and sale deals)

2020F

Source: Cushman & Wakefield

### Major new lease deals in H1 2020



In Jan-June 2020, take-up decreased by 4.3% compared to the last year and amounted to 840,000 sq. m. The business activity was higher in the pre-quarantine period. In Q1 2020 take-up exceeded Q2 2020 by 30% and amounted to 494,000 sq. m. In April-May leasing activity was lower by 35% compared to the same period of 2019. Deals that formed take-up in April-May had been negotiated before the lockdown.

Despite the business activity slowdown Tinkoff Bank rented 78,000 sq. m in AFI SQUARE. This prime business center is now under construction. One more major pre-lease deal took place in Q1 2020 - Novartis rented more than 7,500 sq. m in Alcon II.

In H1 2019 the pre-lease deals share in take-up was 9.5%, while in H1 2020 the indicator increased by 5.5 p.p. and amounted to 15%. The quality office supply is still very tight.



## FLEXIBLE WORKSPACE AS A PART OF NEW WORKPLACE ECOSYSTEM

Flexible workspace is one of a few segments that effectively adapted to new normal and offered products that meet the needs of potential tenants.

**206**  
‘000 sq. m

**Total stock of flexible workspace**  
July 2020

**76%**

**Chain operators share**  
July 2020

*Source: Cushman & Wakefield*

### Major deals with flexible workspace, Q1-2 2020

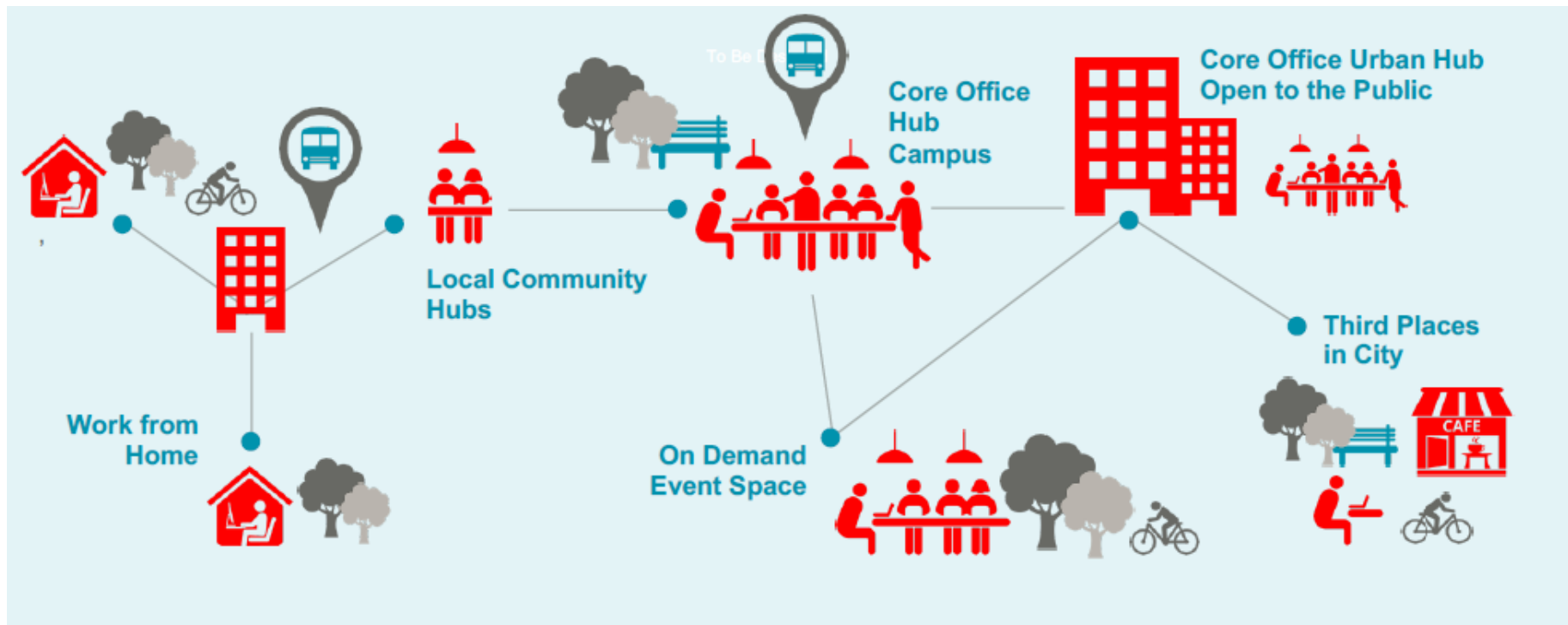
No	Coworking name	Area rented, sq. m	Tenant	Quarter
1	WeWork Arcus III	3 457	Citymobil	Q2
2	Workki Neo Geo	2 584	Gazpromneft-SM	Q1
3	Deworkacy	1 369	Sbermarket	Q2
4	Space 1 Stanislavsky Factory	950	Brown-Forman	Q2
5	Space 1 Kompozitorskaya	800	Confidential Client	Q1

In terms of the new normal, flexible workplace became a great option for those companies that either were interested in expansion or were forced to optimize the occupied space. The majority of organizations were not ready to reduce the staff while their costs should have been reorganized. In that case, a company can rent a certain number of hotdesks in flexible workspace. Employees will reserve a table for a time required, and the company will not pay extra money for the rent of a whole office.

After the implementation of work-from-home more and more people are changing their perception of offices. Soon traditional office will be associated with a hub, where people collaborate and meet clients and colleagues, while their home or flexible office will be more suitable for daily work.

# A TOTAL WORKPLACE ECOSYSTEM

Work-from-home experience accelerated development of a workplace ecosystem. While people will shift to balancing office, home and third places, the office will remain a critical driver of culture, learning and personal connections.



## VACANT OFFICE PREMISES

Despite the low level of new construction activity in Q2 2020, vacancy rate increased. In case of pent-up demand realization the indicator will stabilize at 11.7% by the end of the year.

# 11.6 %

Vacancy rate, June 2020

Classes A and B (B+ & B-)

# 2.1 mn sq. m

Vacant premises, June 2020

Classes A and B (B+ & B-)

# 173

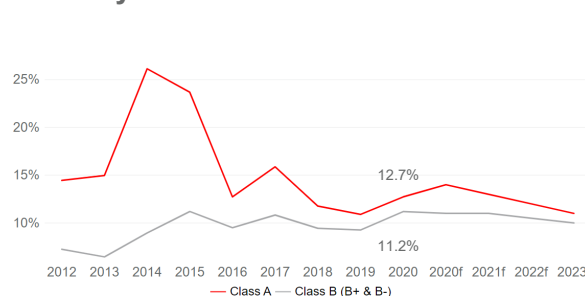
# '000 sq. m

Vacant premises with exposition period more than 1 year

Classes A and B (B+ & B-)

Source: Cushman & Wakefield

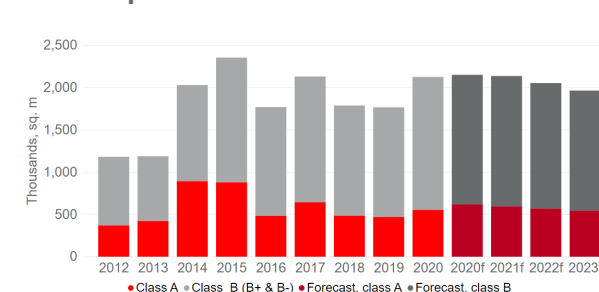
Vacancy rates



At the end of Q2 2020, the vacancy rate amounted to 11.6% which indicates growth by 2 p.p. from the last year. Such growth is a consequence of space optimization and new vacancies entering the market during a slowdown of negotiation processes with potential clients during the lockdown.

Vacancy rate in Class A increased by 1.8 p.p. y-o-y, in Class B – by 3.4 p.p. Further indicator growth is possible in Q3 2020. However, we expect vacancy rate to be at the level of 11.7% in 2020 due to business activity recovery in the end of the year.

Vacant premises



The total vacant premises exceeded by 17% compared to 2019 and amounted to 2.1 mn sq. m. At the same time, the share of premises with exposition period more than 1 year decreased by almost 50% compared to H1 2019. Companies are now focused on cost-effective options, and premises that previously didn't meet tenant's expectations increase in their attractiveness

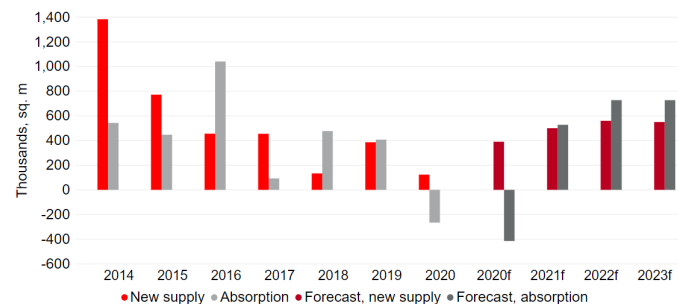
# ABSORPTION

Absorption remained negative due to vacancy rate increase.

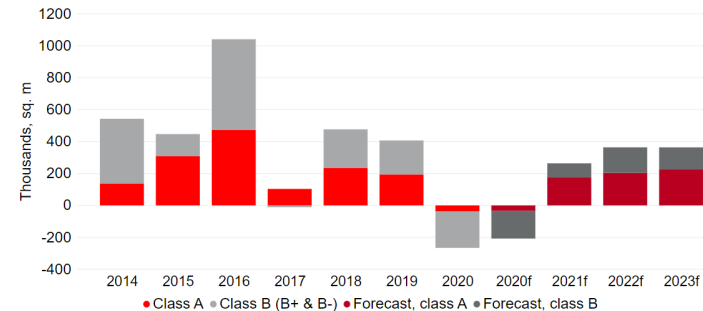
**-186**  
‘000 sq. m

Absorption in Jan-June 2020

### Absorption and new construction



### Absorption by classes

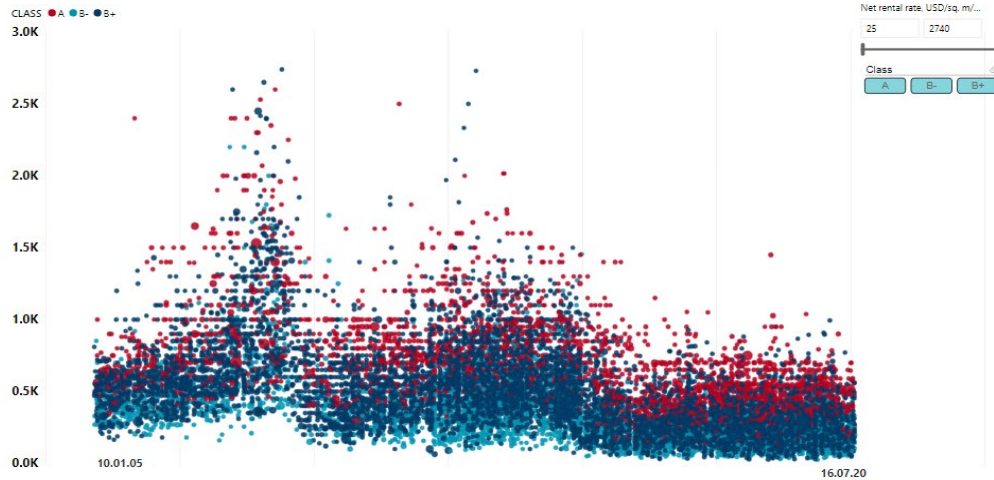


**Absorption** is an indicator that reflects the difference between the area occupied at the beginning and at the end of the period. *Positive absorption* means that additional vacant office premises are “absorbed” from the market. *Negative absorption* reflects the opposite - release of additional office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

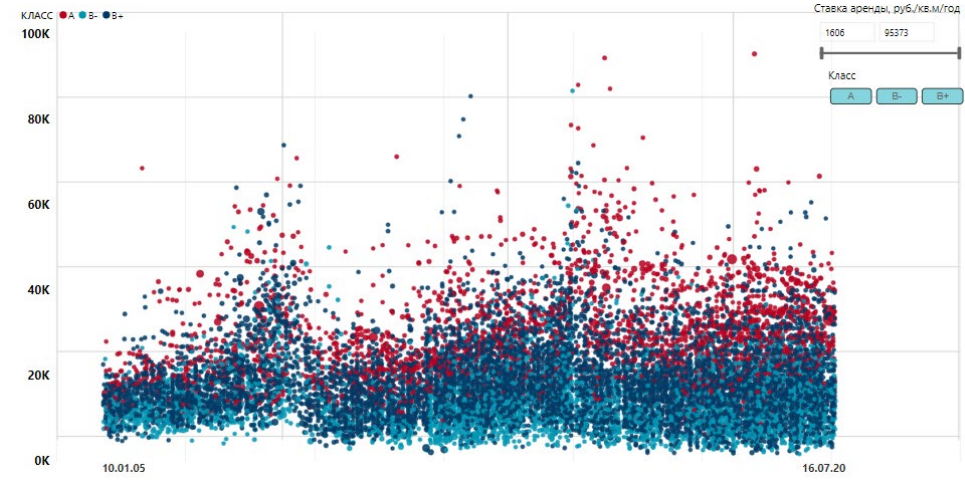
Source: Cushman & Wakefield

# LEASE DEALS IN MOSCOW

## Rental rates in USD equivalent



## Rental rates in RUB equivalent



- The dots on the chart are office lease deals. The horizontal axis represents the date of the deal, and the vertical axis shows the rental rate in USD or RUB equivalent.
- Using the link or QR code, you can access an interactive graphic that displays the details of each transaction.



## RENTAL RATES

Pre-lease in Prime Class business center has a significant impact on YTD average rental rates. By the end of the year the indicator will stabilize at the level of 2019.

# 316

**USD / sq. m annum**

January – July 2020

US Dollar equivalent (all deals in classes A and B)

# 21 560

**RUB / sq. m annum**

January – July 2020

Ruble equivalent (all deals in classes A and B)

Source: Cushman & Wakefield

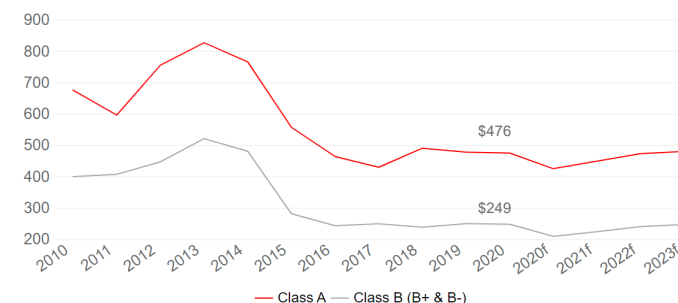
In H1 2020, rental rates increased by 8% compared to 2019. Rental rates in Class A increased by 6.3%, in Class B – by 3.7%.

Such increase is a result of the major pre-lease deal of Tinkoff Bank in AFI SQUARE, a prime class business center. That deal represents 23% of take-up in Q2 2020 and rental rates in AFI SQUARE are higher than the market average.

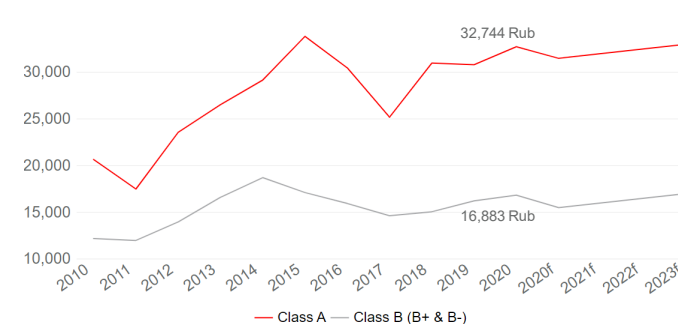
The average US Dollar equivalent of rental rate in Class A in 2019 is 476 USD/ sq. m/year (32,744 Rubles/ sq. m/year). The average US Dollar equivalent of rental rates in Class B is 249 USD/ sq. m/year (16,883 Rubles/ sq. m/year).

We expect average rental rate to keep the level of 2019 (~20 000 Rubles/ sq. m/year) by the end of 2020.

Rental rates in US Dollars



Rental rates in Russian Rubles



## EXPERTS' OPINION

For more insights on the office market watch [\*\*IQ Interview\*\*](#) from Cushman and Wakefield with Vadim Subbotin, Deputy Director General, The World Trade Center



## NEW!

*Experts share opinion on:*

- *how the WTC operate in the new normal,*
- *what safety measures are taken in the WTC,*
- *how to reach compromise between tenants and landlords,*
- *which companies are the WTC's tenants for 40 years,*
- *how accommodation of medical staff was organized during COVID-19.*



## Section 2

# RETAIL

- The consumer market, which was under pressure long before the pandemic, will increasingly decline this year. Retail sales and real disposable income will be in the negative zone in 2020.
- Delivery dates of the projects are moved until the market recovers – only the projects that are on the latest stage of development will be opened. More than 55% of new retail space will be concentrated in Moscow.
- Some retailers announced business optimization programs and shutdown of some stores. During the year, we will see the rotation of tenants in shopping centers and average vacancy rate growth up to 13-15% in Moscow by the end of 2020.

## 5.5 mn sq. m

**Total quality stock in Moscow**

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

## 134 '000 sq. m

**New construction, Moscow, H1 2020**

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

## 230 '000 sq. m

**New construction, Moscow, 2020F**

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

## 9.5 %

**Capitalization rate**

Prime shopping centers, Moscow



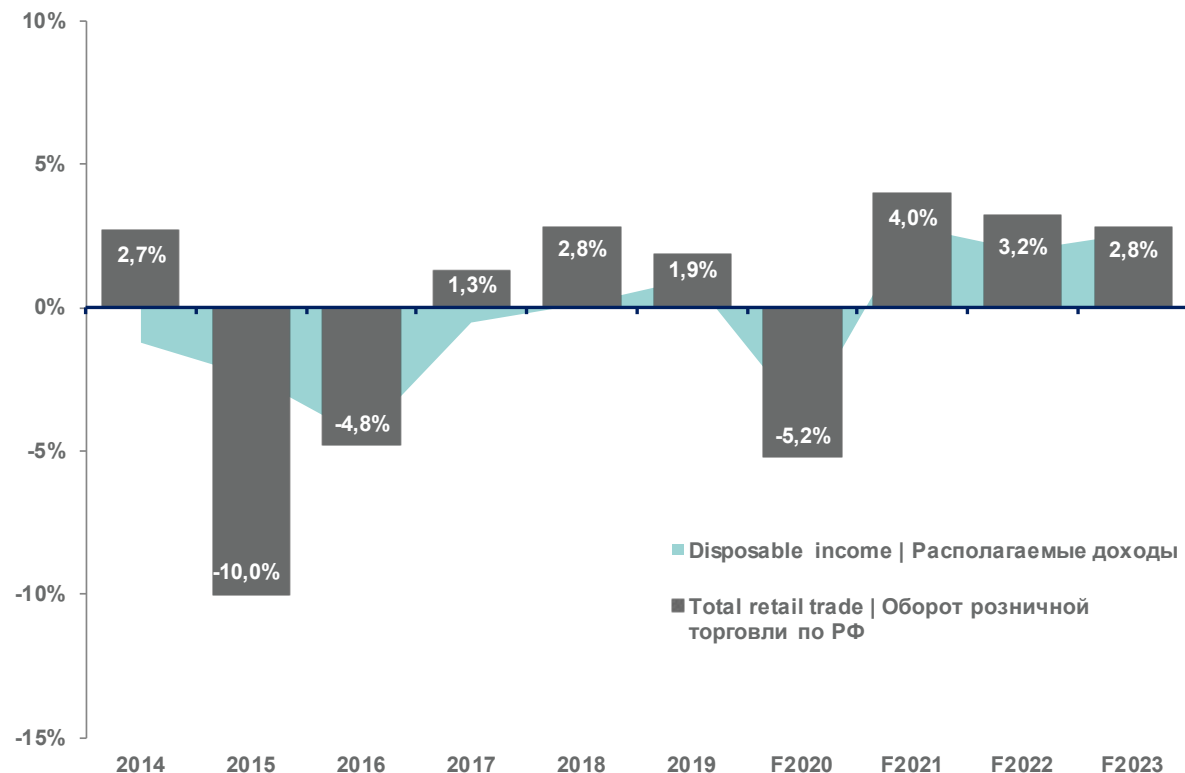
*Retail*

# FOOTFALL AND VACANCY RATE IN SHOPPING CENTERS WILL STABILIZE NOT EARLIER THAN THE NEXT YEAR

After shopping centers reopening pent-up demand won't last long. Shrinking incomes and coronavirus concerns will hold back the consumer activity.

# CONSUMER MARKET IS UNDER PRESSURE

## Consumer market in Russia



Due to the lockdown, retail sales declined significantly in April and May compared to the last year (by -23.3% and -19.2, respectively according to Rosstat). In total, from January to May the drop comprised -6.1%. In early summer, the lockdown measures have started to be lifted gradually, so probably the decline of retail sales in June won't be so deep. According to the official forecast, this year the retail turnover will drop by 5.2%.

Limited personal financial resources also have a negative impact on the consumer market. According to the Romir's survey, which was held in March-May 2020, half of population in Russia reported income decrease. According to official forecast, real disposable income will decline by 3.8% this year. The indicator will be back to the level of 2019 only in 2022.

Source: Rosstat, The Ministry of Economic Development, May 2020

## SHOPPING CENTERS - THE MOST AFFECTED SEGMENT

A significant share of the space in shopping centers is occupied by entertainment and fashion operators, which will feel a drop in consumer footfall. Falling incomes will force people to spend less on these categories.

### Expectations for spending by the Russian consumers across sales channels for the next 6 months



The footfall in shopping centers in Moscow is gradually recovering. According to Watcom, during the first week after reopening the footfall index was 40-50% behind the same indicator of the last year. By the end of June the lag was already about 30%.

In the Eastern European countries, where the shopping centers were launched earlier than in Moscow (in the first half of May), the footfall rates reach 70-80% from the indicators of last year.

Most likely, in Russia we will see the footfall to recover to 80-90% with the opening of entertainment operators in August-September.

Until the end of the year we are unlikely to see pre-crisis levels of footfall – this is caused not only by people's concerns about epidemiological situation, but also due to limited financial resources of population. According to Romir, 2/3 of people assess their financial situation as unstable. F&B and entertainment are the first categories to save money on. Consumers are also planning to cut spending on clothes and shoes.

Source: Consumer Trends Research by Romir and BCG, April 2020

# CHANGES IN CONSUMER DEMAND BY CATEGORY

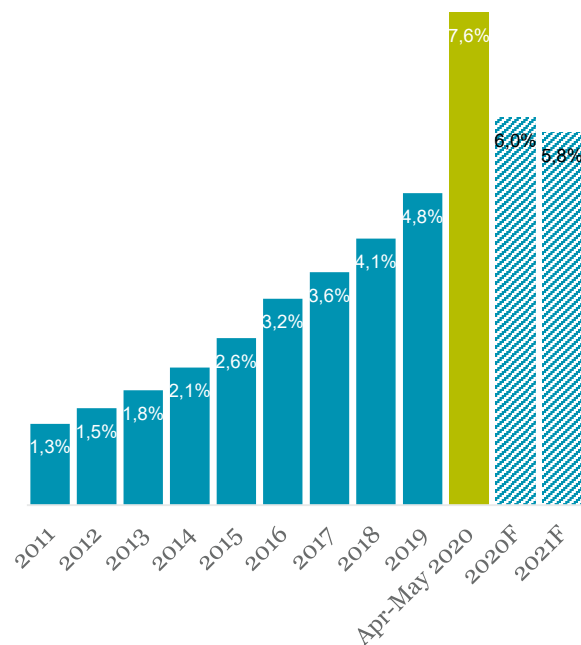


Source: Consumer Trends Research by Romir and BCG, April 2020

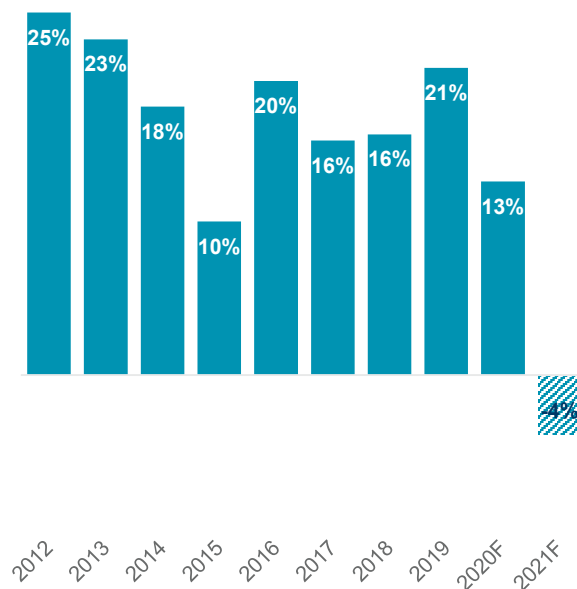
# E-COMMERCE

Investments in the platform will allow online trade to reach a 10%-share in total retail turnover.

Share of online in total retail sales in Russia



Online sales growth in **real terms**

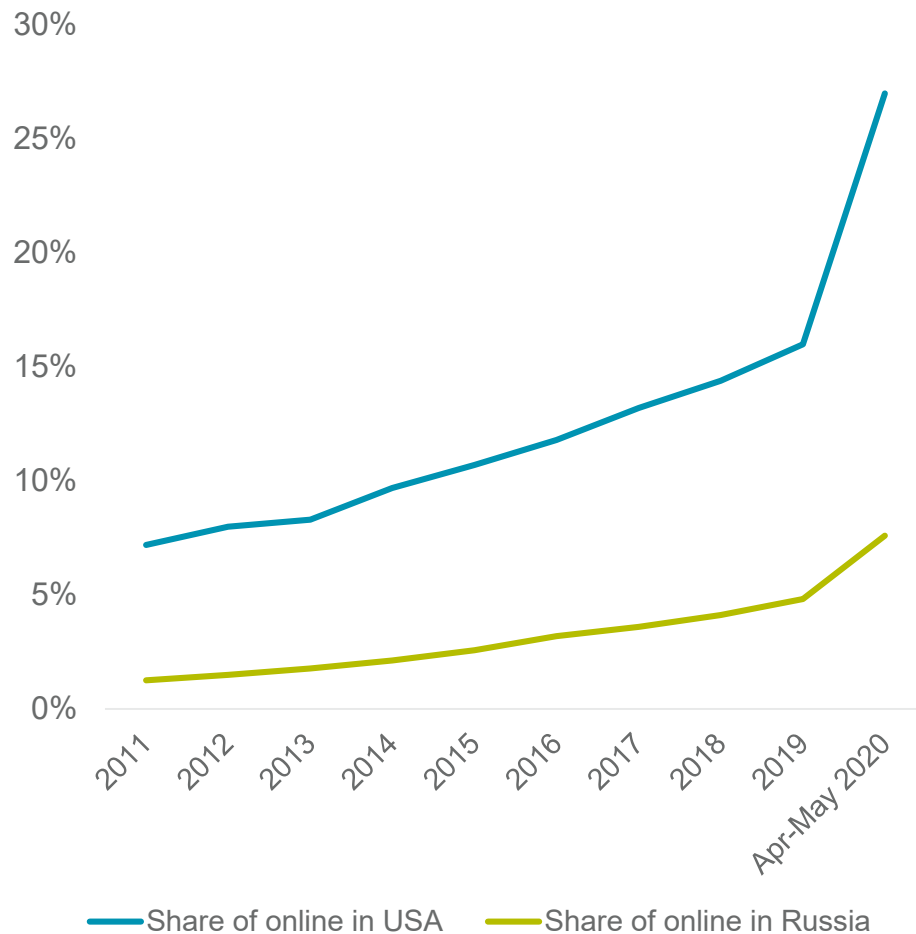


In Spring 2020, e-commerce had a strong impetus for development. Companies were able to expand the assortment, invest in logistic chains, so the share of online retail “broke through” 6% in total retail turnover.

It is possible that we will see a slight decrease of online retail turnover in 2021 in real terms due to the higher base of 2020 and general decline of household income, especially in middle class. Traditional offline retail will also try to win back the position which they lost during the lockdown.

However, the infrastructure created in 2020 will allow online trade to pick up a 10%-share in total retail turnover.

In April-May 2020 the share of online retail in Russia was equal to the level of USA in 2011



Retail

## BIG LEAP IN ONLINE RETAIL

Will e-commerce in Russia be able to secure a 7%-share in total retail turnover?

The volume of global e-commerce has grown significantly due to the huge investments made in infrastructure and urban logistics.

The growth rate of online retail in Russia is still lagging behind. However, if Russian marketplaces will be able to consolidate the success achieved during the pandemic and to keep its share in retail turnover after lifting the restrictions, there will be a new stage of development for online trade.

## DELIVERY DATES OF SHOPPING CENTERS ARE POSTPONED

Due to the pandemic retailers had to rethink their development plans and are now cautious about opening in new projects. Moving the opening dates of retail schemes until market stabilization seems to be the best solution for developers.

**400**  
**'000 sq. m**

New construction in Russia, incl. Moscow

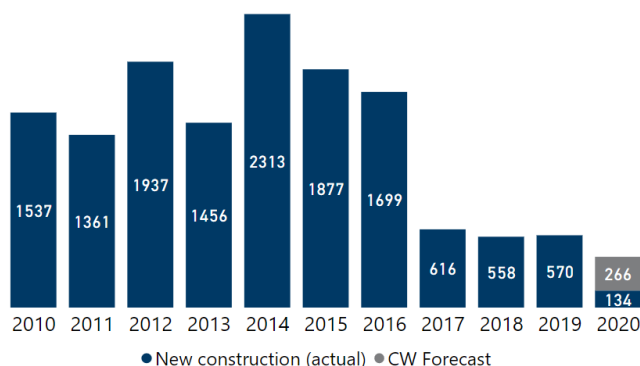
Forecast for 2020

**230**  
**'000 sq. m**

New construction in Moscow

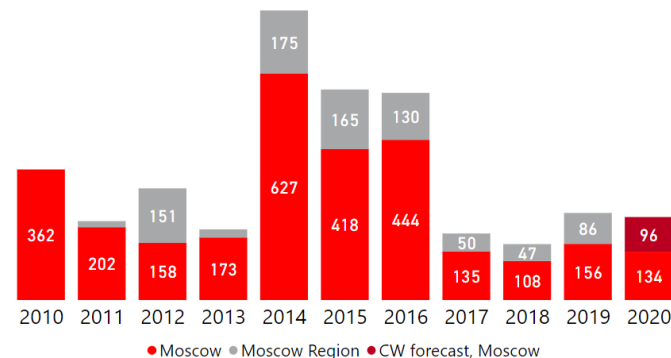
Forecast for 2020

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



In Jan-June 2020, 3 new quality retail schemes were opened in Russia with total GLA of 131,000 sq. m. This construction volume was concentrated in Moscow, there were no new shopping centers with GLA of more than 15,000 sq. m delivered to the market in the regions of Russia. The opening of all quality shopping centers in the regions was postponed.

New construction in Moscow, '000 sq. m



Two shopping centers were opened in Moscow just right after the restrictions were lifted – Kvartal West (GLA 44,000 sq. m) and The Outlet (GLA 20,000 sq. m). Both projects were on the final stage of construction.

Despite the pandemic, the volume of new construction in Moscow in H1 2020 was 25% higher than the same indicator in 2019 due to the delivery of two large retail schemes with GLA of more than 40,000 sq. m.

## RETAILERS ARE IN THE PROCESS OF OPTIMIZATION

A pause in operations, drop in footfall and decrease in household incomes will negatively affect the turnover of retailers. Some operators have to optimize their business and shut down the least profitable stores.

### NEWCOMERS IN 2020 (OPEN AND PLANNED)

**BOSS**  
HUGO BOSS

(BOSS WOMAN)

**EREDA**  
100% MADE IN ITALY

LABORATOIRES  
**FILORGA**  
PARIS

**SUITSUPPLY**  
(WOMEN)



**WEEKDAY**

*& other Stories*

Despite the fact that a significant share of retailers are now facing financial difficulties and adjusting development programs, some operators continue to open new stores and even announce international expansion plans. For instance, Detsky Mir announced openings of new stores even during the pandemic, Home market discounter plans to open 50 new shops in Moscow and Moscow region in 2020, Wildberries entered the markets of Slovakia and Poland, Vkusvill launched its first store in Amsterdam, and Cofix announced expansion plans in Europe and Americas (the first location was already opened in Poland).

The number of new openings from international retailers has decreased significantly, however new brands keep showing interest to the Russian market.



# EXPERT OPINION



## NEW!

*For more insights on the retail market watch IQ Interview with Tatyana Divina, Deputy Head of Research and Insight Department in Cushman & Wakefield. To watch please follow [the link](#).*

## Section 2

# WAREHOUSE AND INDUSTRIAL

- As compared to other commercial real estate segments, warehouse segment was less affected by the shock brought by the pandemic.
- In H1 2020, slowdown of construction activity was registered.
- Lack of quality warehouse spaces and slowdown of construction activity in the Moscow region keep the rental rates and level of vacant spaces on the level of the end of 2019.

## MOSCOW Q1-2 2020

**18.64** mn sq. m

Total stock of warehouses, classes A and B

**140** '000 sq. m

New construction, classes A and B

**3.2%**

Vacancy rate, class A

**521** '000 sq. m

Take-up, classes A and B

**11%**

Capitalization rate, prime warehouse segment

*Warehouse & Industrial. Moscow region*

# GROWING DEMAND FROM E-COMMERCE AND FOOD RETAILERS REPLACES THE SHARE OF SMEs LEAVING THE MARKET

The effect of the pandemic crisis will be visible until the end of 2020 – some SMEs companies will leave the market. In terms of the lockdown and increased demand online operators faced the limitations of the existing infrastructure and business scaling. This will lead to the increase of retailers' demand for warehouses. On the other hand, limited construction activity supports supply-demand balance.

## RECOVERY OF NEW CONSTRUCTION ACTIVITY IS EXPECTED IN H2 2020

The Moscow region is suffering from a dearth of large quality warehouse spaces. As a result, even in the economy recession, 48% of new projects will be built speculatively.

# 140

'000 sq. m

New construction, classes A&B

Jan-June 2020

# 560

'000 sq. m

New construction, classes A&B

Forecast for 2020

Source: Cushman & Wakefield

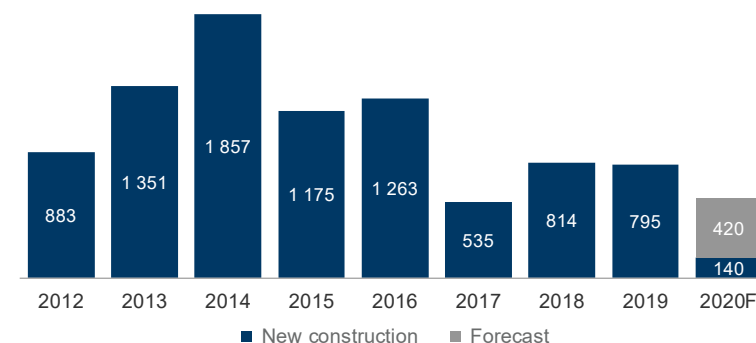
Lack of quality space, growing rental rates and decreasing vacancy determines a growth of warehouse segment in 2020. However, negative macroeconomic effects of H1 2020 cooled down the rapid market growth.

At the end of Q2 2020 the total volume of new warehouse spaces in the Moscow region reached 140,000 sq. m.

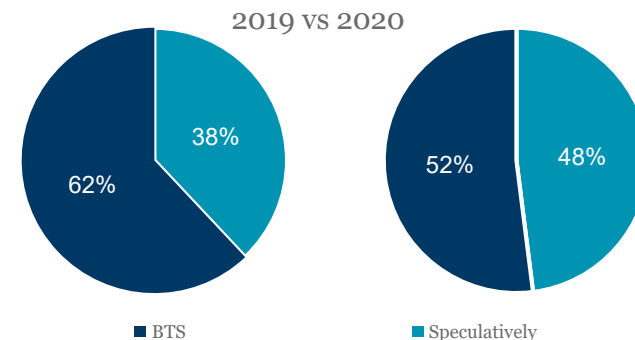
Despite the fact that speculative construction is more sensitive sector for any market changes, 48% of new projects will be build speculatively.

South direction is still the most demanded in the Moscow region. 20% of the new warehouse space will be built in this direction. In 2021, construction of two large projects with total area of more than 1 mn sq. m will start in the South of the Moscow region - PNK Park M-4 and Rusich industrial park.

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



New construction, classes A&B, type of project



## SLOWDOWN OF BUSINESS ACTIVITY IN THE PANDEMIC DECELERATED A DECREASE OF VACANCY RATE

In H1 2020 vacancy rate decreased by 0.4 p.p. and the average rental rate for class A increased by 1.3% compared to the end of 2019.

# 3.2%

Vacancy rate, class A

July 2020

# 3,950

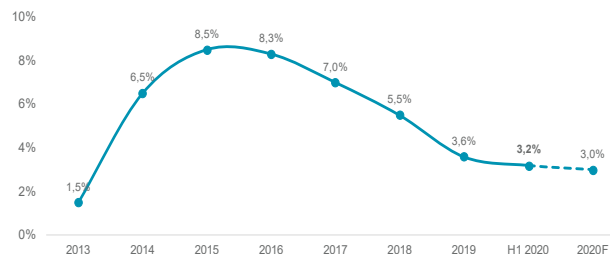
RUB / sq. m / year

Rental rate, class A

July 2020

Source: Cushman & Wakefield

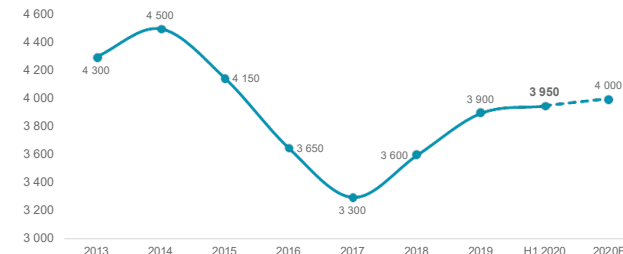
Vacancy rate, class A



In H1 2020 the vacancy rate reached 3.2%. The largest share of vacant space in the H1 2020 was recorded in the west of the Moscow region – 5% of the total stock in this area. The lowest share of vacant spaces was recorded in the North-West of the Moscow region – less than 1% of the total stock in this direction.

One of the most significant factor having an affect on supply and demand balance - new construction remains on a low level. Due to this we expect the vacancy rate will reach the level 3.0 p.p. by the end of 2020.

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



The average rental rate for class A is 3,950 RUB per sq. m per year.

As a result of new construction slowdown, we expect a moderate growth of the average rental rate for class A by the end of the year. It will reach 4,000 RUB per sq. m per annum.

In the South, the most demanded direction, the average rental rate is 4,200 RUB per sq. m per year. The lowest level of the rental rate for class A is in the South-East - 3,700 RUB per sq. m per year.

All data is presented at the end of periods

\* Average rental rate excluding OPEX, utilities and VAT

## INCREASED DEMAND FROM FOOD AND ONLINE RETAILERS SUPPORTED THE WAREHOUSE SEGMENT

# 521

'000 sq. m

Take-up, classes A&B

Jan-June 2020

# 900

'000 sq. m

Take-up, classes A&B

2020 Forecast

Source: Cushman & Wakefield

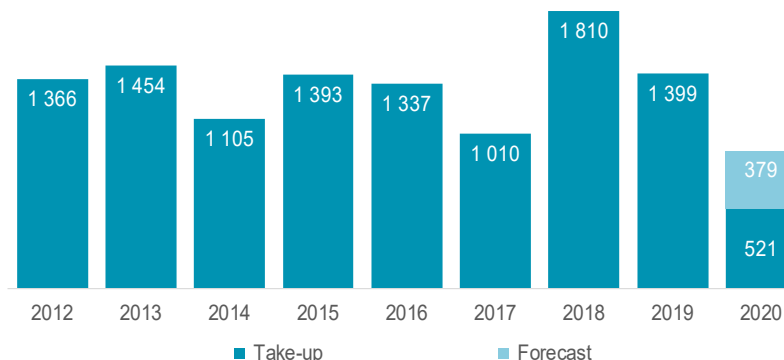
In Jan-June 2020, take-up in the Moscow region reached 521,000 sq. m which is 1.7 times less than in the first half of 2019. It is one of the lowest levels over the last 5 years. We expect take-up to reach 900,000 sq. m by the end of 2020. It will be the lowest figure since 2011.

Take-up in Q2 2020 was 2.4 times higher than in Q1 2020 and reached 368,239 sq. m. Take-up was driven by increased demand from online and food retailers as well as transport companies during the lockdown. Businesses efficiently adapted to new market conditions.

In H1 2020 e-commerce companies occupy the biggest share (32%) in the structure of buy and lease transactions. During the lockdown several companies signed short-term agreements for additional spaces.

For instance, online retailer Wildberries signed two short-term agreements for additional space in Klimovsk and Krekshino logistic parks - 35,000 sq. m in total.

Take-up, classes A&B, sq. m



In Q3-4 2020 we expect demand recovery from other business sectors, additionally to food and online retailers. In the middle of Q2 2020 we noted the growth of demand from logistic companies and producers. However, in 2020 food and online retailers are the main drivers of warehouse market growth.



## OUTLOOK: WAREHOUSE SEGMENT AFTER COVID-19

Investors and developers are concentrating on data centers and urban logistic.

The post-coronavirus period was marked by a revision of some forms of commercial real estate businesses.

Self-isolation and high-demand for online purchases made it obvious that the online retail segment has issues with the scaling of business and turnaround time for orders. Soon it will have an impact on urban logistics development.

Last mile warehouse is the most expensive stage of the e-commerce logistics that refers to the end of supply chain when the parcel is delivered to the customer. A general rule for the segment is to be located within a 30-minute drive time to client. For this reason, this facility should be constructed within the city borders.

In the future, we see the opportunity of redevelopment of some retail spaces for urban logistics, especially those shopping centers that located far away from major streams of people. However, nowadays there are no ready solutions for such redevelopment. Additionally some shopping centers cannot offer premises for urban logistic due to specific technical parameters.

Intensive growth of e-commerce requires large investments in the development of digital infrastructure. Since, most likely, the data center market of the Russian Federation expects a certain booming (the law on the storage and processing of personal data of Russians using servers located on the territory of Russia limits the opportunities for companies operating in the territory of the Russian Federation to use global resources), then given the market prospects, nowadays there are more and more large-scale projects for the development of data centers.

The main factor that determines the demand for a particular product and determines its success will be cost of services (undoubtedly, together with their quality). Therefore, in the next few years, the companies that will be able to optimize the cost of the services will determine the price and win the competition.

Nowadays, a number of large world companies are discussing the merger of their research centers to improve technical equipment for data centers. And here it is obvious that large companies are more flexible in cost management and have the advantages over the other market players. Data center chain as a business model is more sustainable and profitable than one standalone project.

## Section 2

# HOSPITALITY

- A buoyant start of the year experienced by the Moscow hotels in Jan-Feb was interrupted in mid-March by the urgent measures adopted by the federal government to prevent spread of COVID-19.
- As a result, Wider quality market Occ for the first 6 months of 2020 dropped by 36.8 ppt vs. last year – to 36.2%. However, thanks to the low price elasticity of remaining demand ADR's reduction was limited to 7.0%.
- As the hotel industry remained almost paralyzed in Q2, all planned hotel openings were moved to H2 2020.

## ~57.6k keys

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

Cushman & Wakefield's estimates based upon data in the Federal roster of classified tourist objects, Q2 2020

## 20.2k keys

**Modern quality room stock**

Cushman & Wakefield's estimates, Q2 2020

# COVID-19 DELAYED HOTEL OPENINGS IN H1 2020

New hotel openings scheduled for H1 2020 got postponed till H2 2020.

## 0 keys

### Modern quality supply increase in Q1-2 2020

All hotel openings moved to end of 2020

### New modern quality supply in Moscow\* in 2020

Project	Keys	Planned opening
Mövenpick	156	Q3
NOVA Hotel	155	Q4
Marriott Imperial Plaza	268	Q4
Hampton by Hilton Rogozhskiy val 12	147	Q4
<b>Total</b>	<b>726</b>	

\* Net of the New Moscow areas

Source: Cushman & Wakefield

# NEW OPENINGS MAY BE DELAYED

New quality supply gain may reach 726 keys in 2020.

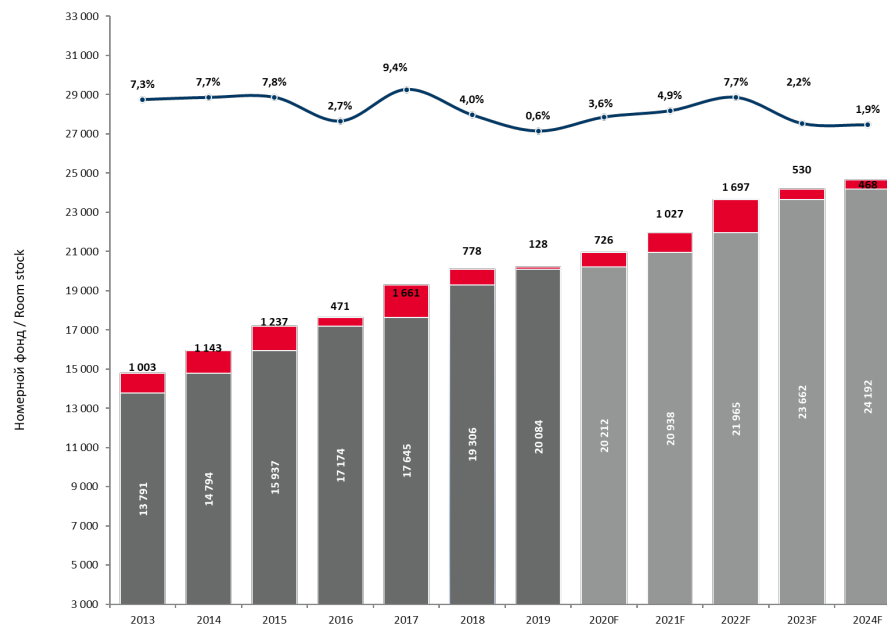
## 3.6 %

Year-on-year growth in 2020

Expected quality market growth in 2020

Source: Cushman & Wakefield

## Supply growth dynamics – actual and projected



■ Доступно на начало года, номеров / Rooms available, year-beginning ■ Добавлено/изъято, номеров / Added/extracted rooms — Рост, % / Growth, %

Temporary freeze of economic activity as well as travel restrictions imposed by the government in March 2020 made hotel development projects ready for completion push their opening dates to the second half of the year. Total new quality supply is still expected to reach 726 new keys in 4 new projects, translating into a year-on-year market growth of 3.6%.

This forecast, however, may prove to be overly optimistic if some investors, concerned over the slow recovery of hotel-related demand, may choose to delay opening till 2021.

# START OF HOTEL DEMAND RECOVERY EXPECTED LATER THIS YEAR

Moscow quality hotel market is yet to feel demand recoup.

## 36.2%

Occ (%)

YTD June 2020

Wider market

## -36.8 ppt

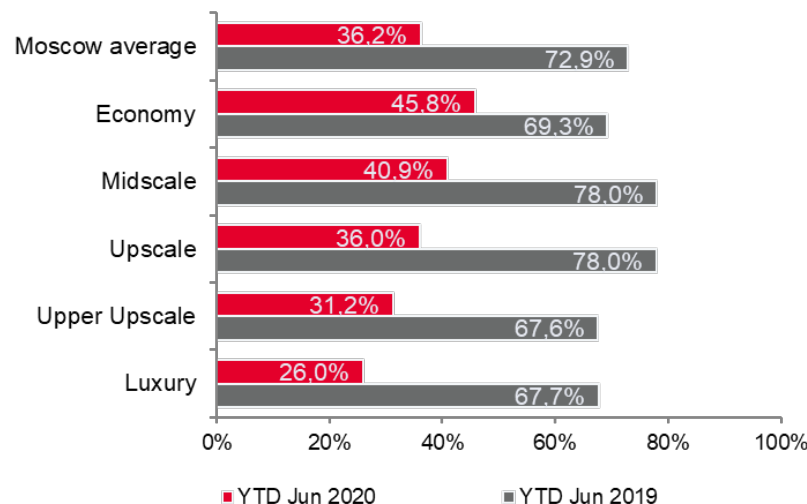
Occ change

YTD June 2020 vs. June 2019

Wider market

Источник: Cushman & Wakefield

Wider market Occ (%) by segment,  
YTD June 2020 vs. YTD June 2019



Extraordinary restrictive measures to fight coronavirus infection in Russia adopted by the federal government in mid-March temporarily placed market mechanisms on hold, resulting in a dramatic decline of hotel demand.

Almost complete depletion of traditional demand for hotel services was partially replaced by quasi-governmental demand (accommodation of medics in-between COVID shifts – at fixed rates). This allowed Midscale and Economy hotels to show better Occ results than hotels of other grades.

# COVID FACTOR AND ITS EFFECT ON HOTEL RATES

ADR fluctuations were not affected by supply/demand balance.

# 6 074

ADR (RUB), YTD June 2020

Wider market

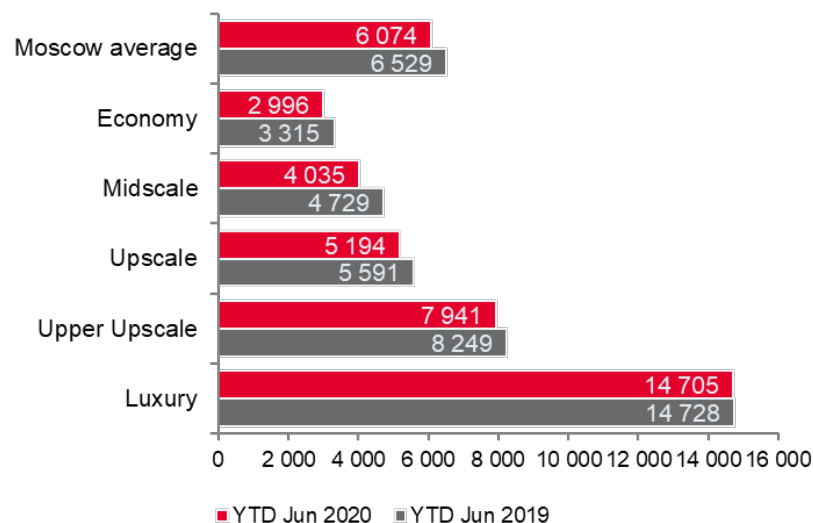
# -7.0%

year-on-year change  
YTD June 2020

Wider market

Источник: Cushman & Wakefield

Wider market ADR (RUB) by segment,  
YTD June 2020 vs. YTD June 2019



Due to low elasticity of demand (and non-market principles of tariff-setting) in Q2, higher-grade hotels chose to keep their rates rather than offer discounts. As a result, Luxury and Upper-Upscale hotels showed nominal year-on-year ADR changes of 0.2% and 3.7%, respectively.

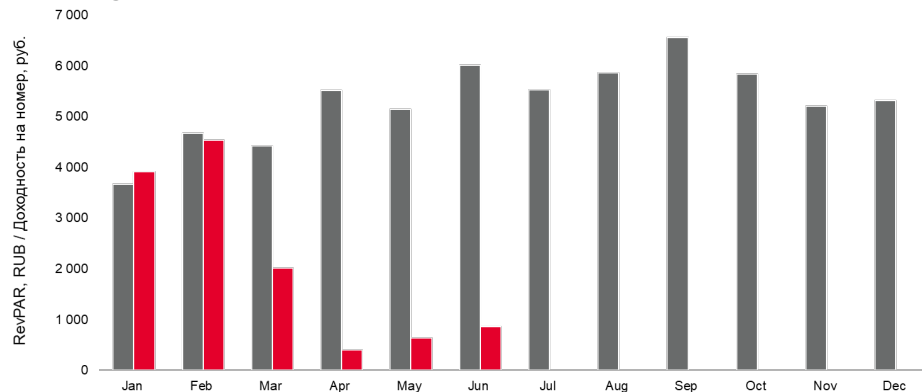
Hotels of other categories chose to accommodate governmental business (medics) at fixed rates (RUB2200-2500) which reduced their year-on-year ADR indicators by 7-15%.



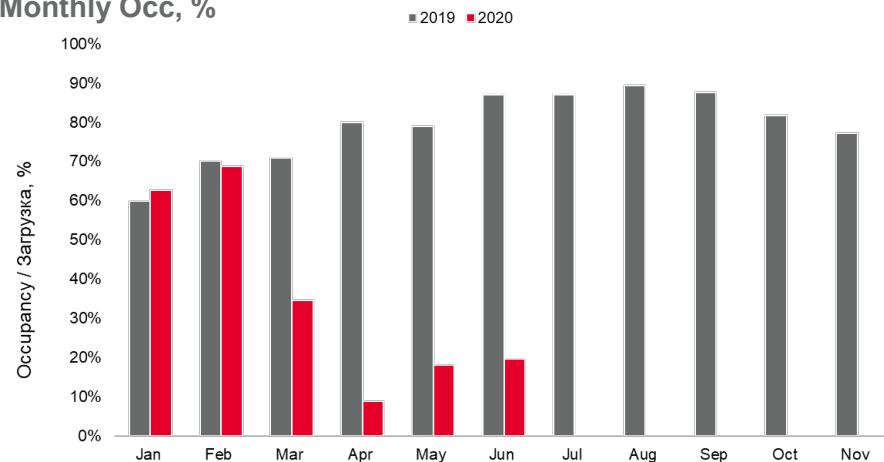
# DEMAND RECOVERY - WHEN AND HOW?

What can Moscow quality hotels expect in H2 2020?

## Monthly ADR, RUB



## Monthly Occ, %



Base hotel demand (Business, mostly Individual) recovery may be expected only with the start of the business season (Autumn/Winter) of 2020, driven by domestic clients. Business group (MICE) segment is likely to recover longer due to the official restrictions to hold mass meetings and events as well as because of widely expressed concerns of the “new coronavirus wave”.

Since state borders still remain closed and international travel is restricted, the number of foreign visitors arriving to Moscow both on business and leisure will be minimal. This will have a direct negative impact on operating results of the Moscow quality hotels whose share of foreign business has traditionally reached 40-60% of room nights.

Thus, 2020 is likely to become one of the most challenging years for the Moscow hotel industry. Even after domestic demand shows signs of recovery in the second half of the year, quality hotels are unlikely to see previous volumes of operating revenue soon. A great deal of uncertainty over speed and volumes of demand recovery will have a direct impact upon profitability of hotels, forcing owners and operators to re-think their business models, including staffing and operating costs.

# STANDARD COMMERCIAL 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 penalty. After crisis became very popular. Notice period is 6-12 months. 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.

## FEES

Agent service fees:

**Offices:** depends on the type of service and type of deal, **Retail:** 8-12% of the annual lease payment, **W&I:** lease - 1-2 months of lease payment, acquisition – 2-3%.

**Land:** acquisition- 3-5% depending on the land plot size.

## 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:** 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:** at the level of Russian CPI or 4-7% for RUB agreements; 2.5-4% or at the level of USA / EU CPI for agreements in foreign currency.

**Retail:** 5-10% or CPI in Russia for RUB agreements, 2-5% 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% for fashion, 1-3% for 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 not included into 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 tax depends on the region. In Moscow amounts to 1.7% in 2020 (1.8% in 2021).

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

VAT: 20% (from January, 1 2019)

# #MARKETBEAT

Section 3

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[www.cwrussia.ru](http://www.cwrussia.ru)



About the company

## **CUSHMAN & WAKEFIELD IN RUSSIA**

Cushman & Wakefield has been successfully operating in Russia since 1995, with more than 150 experienced and highly qualified expert employees. 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](http://www.cwrussia.ru) and [www.cushmanwakefield.ru](http://www.cushmanwakefield.ru)

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