1/2014

AEB REAL ESTATE MONITOR

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Hot Topic:

Russian real estate market among most attractive in Europe in 2014



Contents

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The “AEB Real Estate Monitor” is registered with The Federal Service for Supervision of Legislation in Mass Communications and Protection of Cultural Heritage, Certificate registration ПИ № ФС77-24458/ СМИ “АССОЦИАЦИЯ ЕВРОПЕЙСКОГО БИЗНЕСА: Обозрение рынка недвижимости” зарегистрировано в Федеральной службе по надзору за соблюдением законодательства в сфере массовых коммуникаций и охране культурного наследия. Свидетельство о регистрации ПИ № ФС77-24458 от 23 мая 2006

Frank Schauff
Chief Executive Officer,
The Association of
European Businesses

Dear Reader,

Welcome to this year's first edition of Real Estate Monitor, the leading English-language supplier of commercial news about the Russian real estate market.

Real Estate Monitor analyses the retail, industrial, hospitality, residential, office and capital markets in Moscow, St. Petersburg and across Russia.

The Monitor offers a range of tools for real estate professionals. It gives you information about property values and should help you make better-informed decisions about the market. It is my hope that you will find this publication a useful resource, and that it will accelerate your business growth.

I would like to take this opportunity to thank those of our Real Estate Committee members who have been active in contributing to this publication and to the other activities of the Committees.

I look forward to seeing many of you at our upcoming Real Estate Committee events.

Sincerely yours,
Frank Schauff

Dear Reader,

Christophe Vicic
Chairman of the AEB Real Estate Committee

We have compiled another edition of the Real Estate Monitor covering the main trends and forecasts for the Russian real estate market. Below is a short summary of the key developments for the market as we move into the year.

Going into 2014 the government has acknowledged that reasons why the economy disappointed in 2013 are not a function of the global economy, rather than the result of domestic factors. We find this encouraging. Our forecast of GDP growth at 2.0% is hardly a selling point when US growth is forecast at 2.6%. However, the government's new focus on investment to support growth, rather than relying on consumption, will be an important theme in 2014. With growth forecasts universally conservative it is clear the market is unwilling to price in reform too soon, but we are encouraged that the Kremlin is looking in the right direction.

As for the real estate market, the weak economy has actually done little to impact volumes. 2013 volumes came in at USD 8.1bn, way above pre-crisis levels of USD 5.1bn in 2008 and we expect 2014 to be strong too at USD7bn. We forecast a slightly lower number largely due to the absence of the USD 1bn type deals that were a feature of the last few years. What is clear though is that there is considerable depth and volume of investment in the market which we expect to be reasonably well supported in 2014. Despite the robust investment market, we are not inclined to predict any compression in yields in 2014 and expect rates to remain flat for the foreseeable future. With economic predictions cautious, rental increases are unlikely, especially given the large amount of stock coming to the market in 2014, particularly in the retail and warehouse space. Indeed we would not be surprised to see a jump (from admittedly a very low base) in vacancy rates in both those sectors.

Policy issues are one of the big unknowns in the market going into 2014. Specifically the move to cadastral valuation of commercial real estate, combined with the changes in property tax. So far these changes have only been implemented in Moscow and Moscow region, but what is clear is that they have created considerable disquiet amongst owners, developers and occupiers.

Despite the slowdown in economic growth, the Russian real estate market still has considerable potential. Importantly, even though completions are expected to come in at record levels in 2014, there remain significant supply constraints overall. Moscow still has less than 10% of the class A office space per capita than San Diego; half the shopping centre space per capita of Warsaw and warehouse space per capita that is half that of Munich.

Sincerely yours,
Christophe Vicic

St. Petersburg Market Overview

Office

Completion level in Q4 2013 became one of the highest on record. In the last quarter of 2013 117,300 sq m in office buildings were completed, this volume is one of the highest quarterly results, only in Q4 2009 more spaces were completed. Two completed business centres refer to Class A buildings, their total leasable area is 56,250 sq m. Five buildings refer to Class B, their total area is 61,495 sq m. Two largest office centres completed in Q4 2013 are Nevskaya Ratusha BC, Phase I, on Degtyarnaya str., 3 (37,880 sq m GLA, Class A) and Leader Tower BC on Leninsky Ave., 153 (38,000 sq m, Class B). Total completion level in 2014 will be a bit below than in 2013. Before the end of 2014 210-220 thousand sq m may be delivered to the market, if all announced plans are realized. Share of Class A will be the same as in 2013 – around 60%. (**1** ▶)

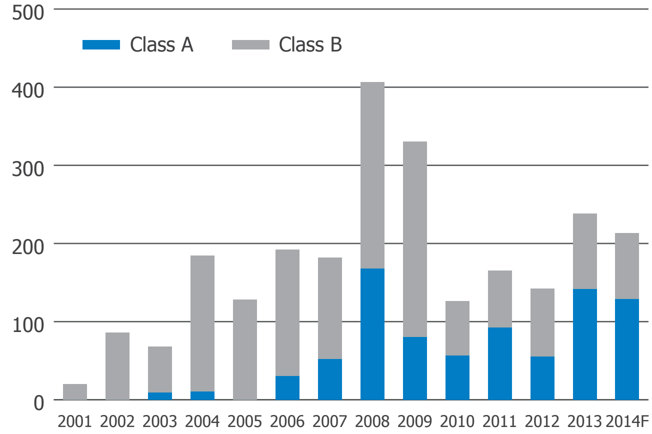
As result modern office stock (Classes A and B) in St. Petersburg increased by 238,640 sq m in 2013, which reflects a 68% YoY growth. This brought total modern office stock to 2.407m sq m, which corresponds to 479 sq m per 1,000 inhabitants. (**2** ▶)

1 ▶ Main New Office Buildings

Name	Class	GLA, sq m
Completed in 2013		
Nevskaya Ratusha, I оч.	A	37,880
Renaissance Pravda	A	19,260
Technopolis Pulkovo, II ph.	A	18,750
Senator on Prof.Popova, III ph.	A	18,370
Renaissance Premium	A	13,600
Sinop	A	12,020
Preobrazhenskiy	A	11,300
Leader Tower	B	38,000
Megapark	B	13,000
Zolotaya Dolina	B	10,000
Announced to be completes in 2014		
Trinity Place	A	27,300
Electro	A	15,700
Eightedges	A	13,200
Paradny Kvartal	A	10,000
SetlCenter	B	21,300
Pulkovo Star	B	16,000

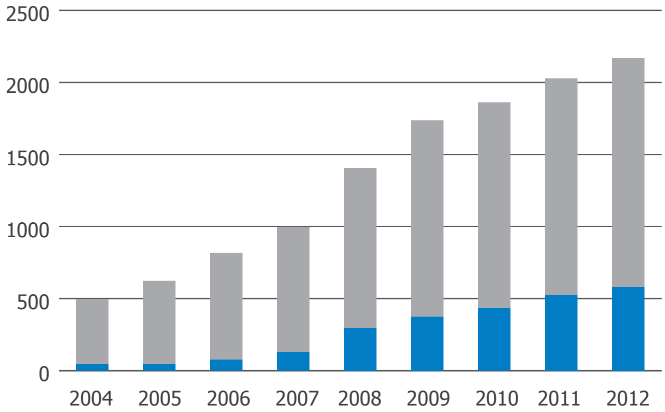
Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

2 ▶ Office Completions Dynamics



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

3 ▶ Office Stock Dynamics



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

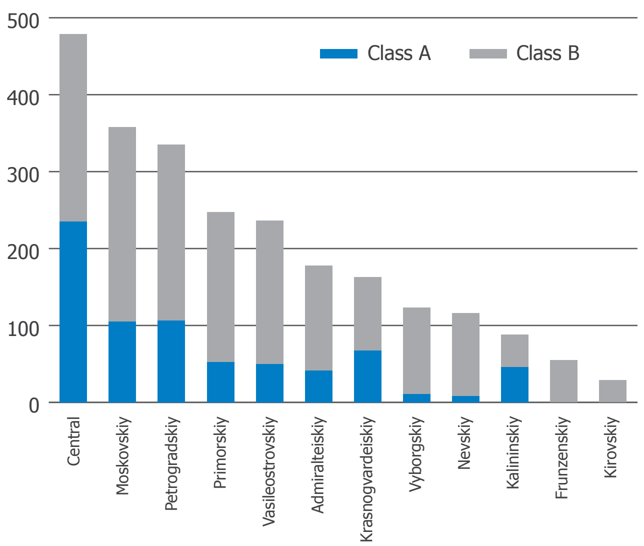
Share of new office buildings belong to Class A reached the highest value. 60% of new business centres are Class A office buildings. As result, completions in 2013 in Class A is comparable with total completions level in 2012. (3 ▶)

Moskovskiy District took the leading role in terms of new office space delivered to the market. As for the historical centre (Central, Admiralteiskiy, Petrogradskiy and Vasileostrovskiy District together) 47-50% of new office completion volume were commissioned both in Q4 2013 and in whole 2013. But 38% of new volume was delivered in Moskovskiy District – the highest result among administrative districts. Through to FY 2014 the trend of geographical distribution will be the same: more than 30% of new volume will be delivered in Moskovskiy District. As for the historical centre (Central, Admiralteiskiy, Petrogradskiy and Vasileostrovskiy District together), its share will slightly increase from 37% in 2014 to 47% among spaces that announced to be completed in 2014-2016. (4 ▶)

The transfer of Gazprom and its affiliate companies to St. Petersburg is the main reason for the leading role of Mining and Exploration in leasing deals structure. In just the last three years Gazprom and its affiliates have leased more than 70,000 sq m of office space. As example, the largest lease deal for office market happened in Q3 2013. Gazprom Export leased 12,300 sq m in Senator BC on Professora Popova street. The market situation that will be observed in 2014 is depended of decision of future of transfer of Gazprom to St. Petersburg. In the case of maintenance of previous administrative strategy, the Mining and Exploration sector will take a leading role in leasing deals structure. One can expect that IT companies will also be very active. (5 ▶)

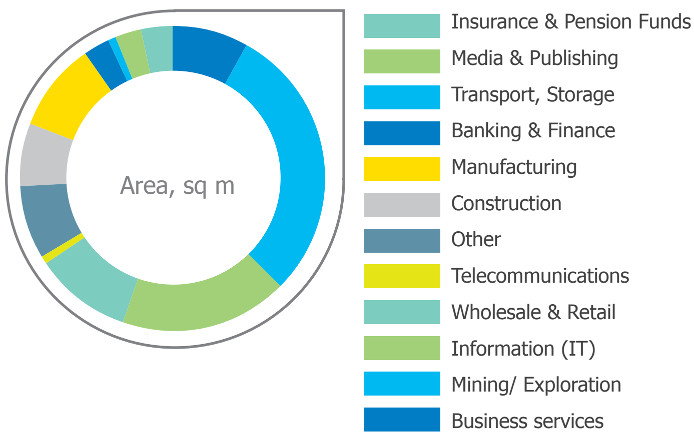
Net absorption level in 2013 became the lower since 2010. As for 2013 the annual level of net absorption reached 121,970 sq m. In Q4 2013 we fixed a negative net absorption in Central (first time since 2009), Vasileostrovsky and Nevsky districts. Moskovskiy District took

4 ▶ Office Stock, Geographical Distribution



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

5 ▶ Office Deals Breakdown by Business Sector, 2013



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

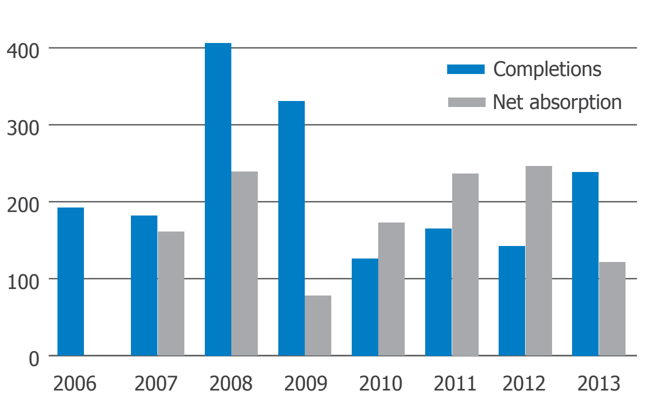
the 1st place in terms of absorbed office space — around 35,400 sq m. (6 ▶)

The average vacancy rate significantly increased in 2013 from 7.7% to 11.8%, mainly due to high completion and low net absorption in Q4. Vacancy rates have increased in Class A from 10.7% at the end of 2012 to 19.4% at the end of 2013, in Class B from 6.7% to 8.6%.

In 2013 rouble rents increased by 8% in Class A office buildings and by 5% in Class B. Due to weakness of rouble, rental rates growth in USD was less than in roubles, it was 3% in Class A and 1% in Class B. Currently, average rents are USD350–440/sq m/year for Class A and USD270–350/sq m/year for Class B office buildings (triple net). (7 ▶)

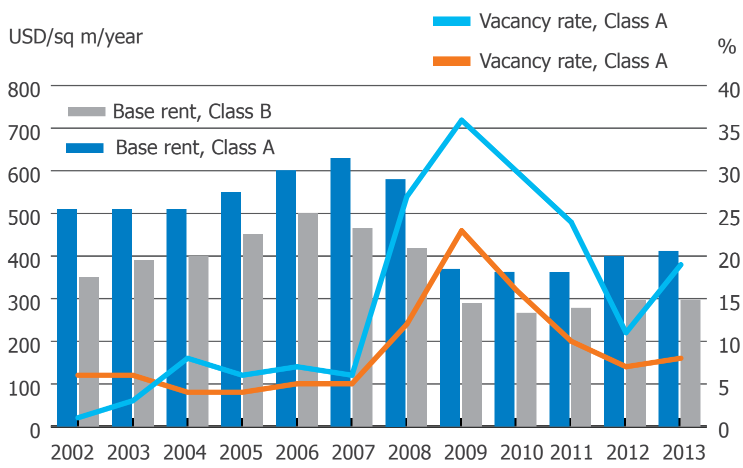
We don't expect an increasing of rental rates. Despite high quality of new business centres, the developers expectation about rental rates are often overestimate on the start of project marketing. Due to competition, a growth of average rental rates due to high rate in new objects is bounded by the marketing policy of the existing office centres.

6 ▶ Office Completions and Net Absorption



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

7 ▶ Office Market Balance



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

Shopping Centre

The total volume of retail market spaces reached 2.056 m sq m at the end of 2013. (8 ▶)

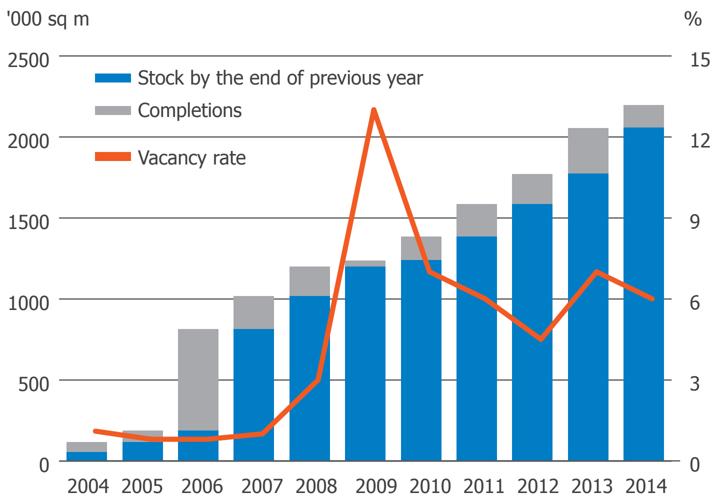
Seven shopping entertainment centres (SEC), with the total leasable area of 283,500 sq m, were delivered to the market in 2013, that is the highest volume since 2007. Two projects, 5 Ozer SEC (22,600 sq m) and Zanevskiy Kaskad SEC, Phase III (45,600 sq m) were delivered to the market in Q4 2013.

By the end of 2013 vacancy rate increased up to 7.0%. Shopping centres with low occupancy at the time of opening were delivered to the market at the end of 2013, that was the reason for vacancy rate increasing. New supply of 138,950 sq m will be delivered to the market by the end of 2014, vacancy rate will decrease to 5.5 - 6%. (9 ▶)

Outlet-centres format (not represented yet in St. Petersburg) continued its development in 2013. Hines started construction of Outlet Village Pulkovo (24,000 sq m). Fashion House Group obtained a building permission for Fashion House outlet-centre construction in the south of St. Petersburg. One more outlet-centre — Vaalimaa Shopping Center Oy will be built in Finland in Vaalimaa near the Russian border. The opening of all outlet-centres is scheduled for 2015.

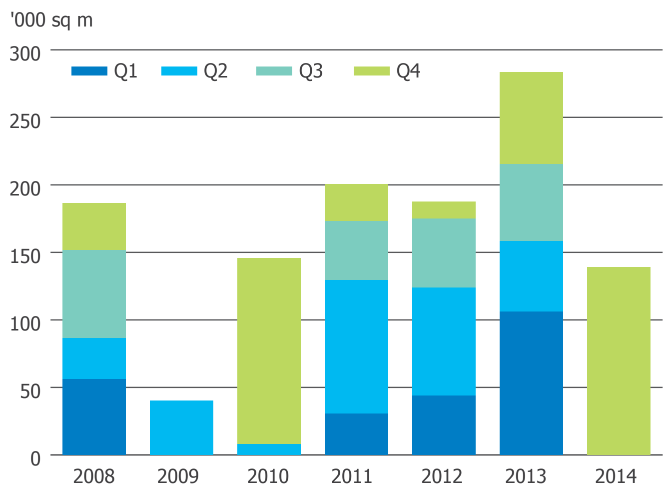
The leader in terms of new retail spaces delivered to the market in 2013 was Frunzenskiy District with two shopping entertainment centres total leasable area of 102,300 sq m. However, according to the results of 2013, Primorskiy District is the leader in terms of total existing shopping stock. Kalininskiy and Primorskiy Districts are the most popular in terms of the future supply. Leading position in terms of quality shopping centre stock per capita is held by Moskovskiy District. We do not expect significant changes in the districts ranking in 2014 (10 ▶, 11 ▶)

8 ▶ Shopping Centre Stock and Vacancy Rate Dynamics



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

9 ▶ Shopping Centre Quarterly Completions Dynamics



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

New brands continue entering St. Petersburg retail market. As for example some new openings in 2013: Michael Kors (Galleria SEC), ELC (London Mall SEC), Funday (Leto SEC), Reima (Mega Dybenko SEC), Takko Fashion in several shopping entertainment centres.

Premium supermarkets are increasing their presence in St. Petersburg. The premium brand convenience chain Azbuka Vkusa entered the market in 2013, four supermarkets of the chain were opened during the year. The supermarket chain Land increased the number of the stores up to ten (three new openings in 2013).
Prime (maximum) base rents are stable at USD2,000/ sq m, but rental rates for some tenants increased in 2013. Main increasing was observed for the premises for entertainment and for goods for children. This is due to the high growth of demand for these categories. Also rents increasing for the premises for hypermarket and supermarket, sports goods were observed, a bit less - for fashion tenants. (**12** ▶)

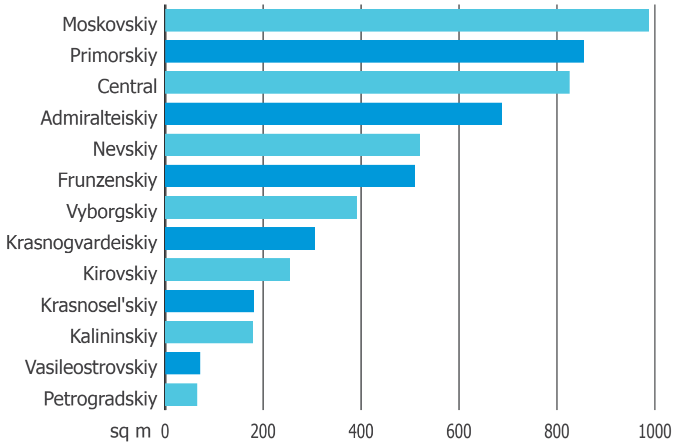
There is intense competition amongst shopping centres for customers. Currently we are seeing developers working hard to make the tenant mix reflect the demands of the target audience. This may include a specific tenant (entertainment centres and cinemas are the most popular), or be reflected by the positioning of the project.

For example Galeria SEC's tenant mix is reflected by a large number of flagship stores, such as Michael Kors, Reiss, Lee Cooper. If all announced projects are completed, quality shopping centre stock per capita will reach 430 sq m per 1,000 inhabitants in 2014. Considering the circumstances developers have to pay more and more attention to shopping centre concept and also to create a unique component for each shopping centre, that can allocate the centre from other city projects. This may include a specific tenant (entertainment centres and cinemas are the most popular), or be reflected by the positioning of the project.

Shopping centres with outdated concept are looking for new ways of market positioning. In 2013 reconception was made for Felichita SEC (new name of the complex is London Mall). Tenant mix was changed in Baltiyskiy SEC. Kapitoliy SEC, Smile SEC and Kosmopolis SEC are at the stage of reconception now.

Large shopping entertainment centres becoming a destination point for families to spend their weekends. Diversity and fullness of services became one of the most important factors for regional and superregional projects. So, besides the tenant mix in retail gallery, quality entertainment component (including children entertainment) becoming increasingly important as well as varied food court and restaurant area.

10 Shopping Centre Stock per 1,000 Inhabitants



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

11 Shopping Entertainment Centres (SEC) Completed 2013 and to be Completed 2014

SEC, completed in 2013		
Name	**GLA, sq m**	**Developer**
Balkaniya Nova, Phase II	50,000	Adamant
Kontinent (Zvezdnaya)	56,000	Adamant
Kontinent (Bukharestskaya)	52,300	Adamant
Pearl Plaza	48,000	SRV Group
Velikan Park	9,000	Interkom
Zanevskiy Kaskad, Phase III	45,600	Adamant
5 Ozer	22,600	Fort Group
London Moll (reconception)	61,300	Fort Group
Future SEC, 2014		
Yevropolis	60,500	Fort Group
Monpasye	30,500	Fonika
Torgovy Dvor	16,750	Torgovy Dvor
Admiral	14,000	Sovetnik

12 Base Rent in Shopping Centres

Profile	Area (sq m)	Rental rate (USD/sq m/ year)
Hypermarket	>5,000	130-170
Supermarket	1,000-2,500	350-500
DIY	8,000-15,000	110-160
Fitness clubs	2,500-5,000	120-180
Household goods	<2,000	140-180
White & Brown	2,000-3,000	200-350
Sport goods	>4,000	130-150
	800-1,500	180-220
Cinema	>3,000	130-180
Entertainment	2,000-3,500	140-200
	1,000-2,000	160-220
Perfume and cosmetics	300-500	800-1,500
	50-100	1,200-2,000
Goods for children	>1,000	280-340
	<150	700-1,200
Food courts	40-150	1,100-2,200
Restaurants	250-600	450-700
Fashion and apparel	1,500-2,500	220-350
	600-1,200	270-400
	400-600	400-600
	200-300	600-900
	100-200	900-1,500
	<100	1,000-2,000

Warehouse

Quality warehouse stock in St. Petersburg in 2013 reached 1.98m sq m. In Q4 2013, three new warehouse complexes: Nordway, Phase II (40,000 sq m GLA), Orion, Phase II and Phase III (22,000 sq m and 15,000 sq m respectively) were delivered to the market. All these warehouses belong to Class A. Total quality warehouse stock increased by 122,000 sq m in 2013.

The total area of 356,000 sq m of new quality warehouse space is planned to be delivered to the market in 2014. If all announced projects are completed, this volume will be the highest for the last five years. It should be noted that warehouse complex STC, Phase I (54,000 GLA) that is currently operates, but not commissioned, is included in pipeline. (**13** ▶)

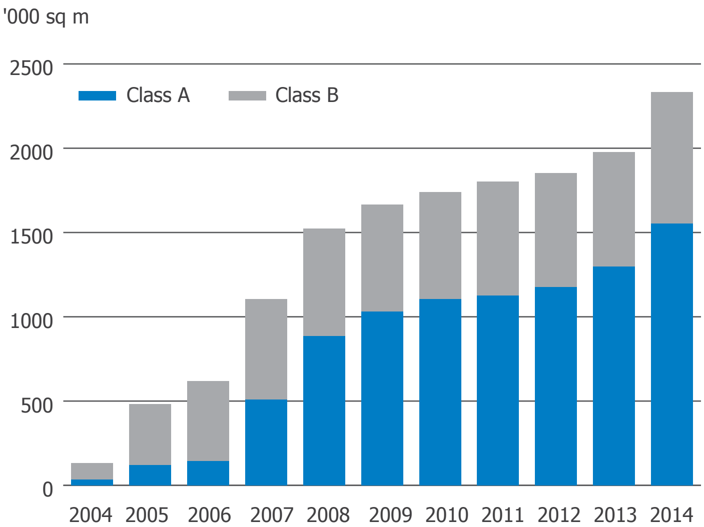
Warehouse distribution by type in the mid-term perspective will reflect speculative supply growth. By the end of 2014 the volume of speculative warehouse complex will increase by 30% (1,338,000 sq m by the end of 2014 vs. 1,040,000 sq m in the end of 2013).

The majority of future projects are either the next phases of the existing warehouses, or built-to-suit projects. As for example Ruslan Warehouse, Phase II (30,000 sq m), PNK-KAD (68,000 sq m), Logopark Osinovaya Roscha, Phase II (45,000 sq m).

In Q1–Q4 2013 net absorption reached around 128,900 sq m, with the share of Q4 2013 absorbed volume around 53,000 sq m. Vacancy rate has increased up to 1.7% at the end of 2013. Currently, the total volume of available space in quality warehouse complexes is still at low level (33,600 sq m). (**14** ▶)

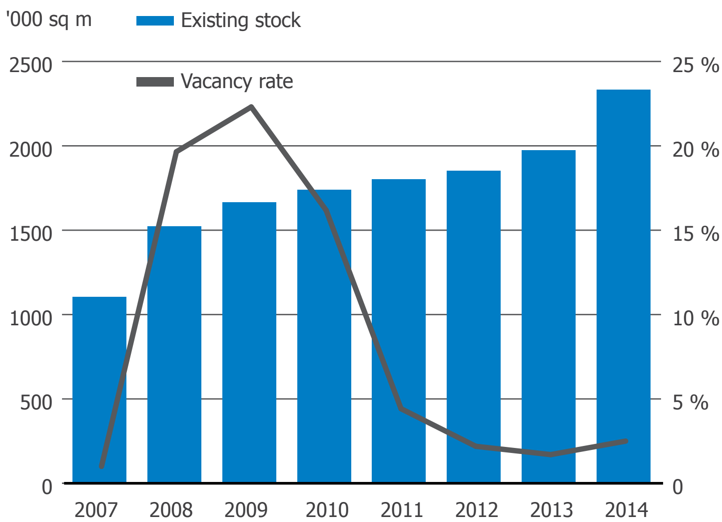
The total take-up in 2013 was the highest since the pre-crises years — 303,000 sq m (75,000 sq m in Q4 2013), most of which are pre-let deals. (**15** ▶)

13 ▶ Warehouse Quality Stock Supply Dynamics



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

14 ▶ Supply and Vacancy Rate Dynamics



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

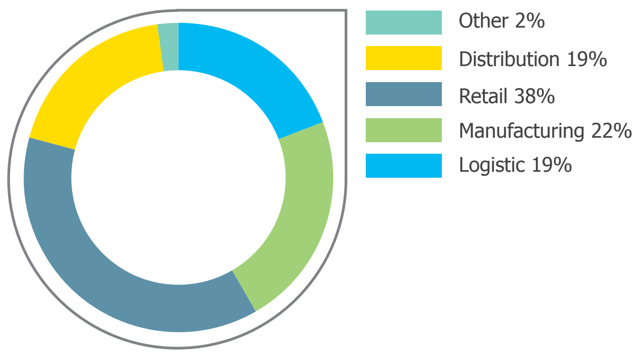
In the last quarter, as well as for entire 2013, retail companies showed the highest activity on the St. Petersburg warehouse market — 38% of the total leased volume in 2013 (62% in Q4 2013). Manufacturing companies took the second place — 22% in 2013 (38% in Q4 2013). Share each of logistic and distribution companies is equal to 19% in 2013. There were no deals in these sectors in Q4 2013. (**16** ▶)

In 2013 rental rates increased up to USD125—135/sq m/year (without OpEx and VAT). As a rule, rental indexation at 3–4% is fixed in leasing agreements. Operating expenses for Class A warehouse properties equal to USD35–40/sq m/year. In Class B projects operating expenses are not included in the basic rent. Typical lease length for quality warehouse projects is 5–7 years. Short-term leases (11 months) are available for Class B complexes. We do not expect a rental rents increasing in 2014. (**17** ▶)

15 ▶ Main Deal on Warehouse Market in 2013

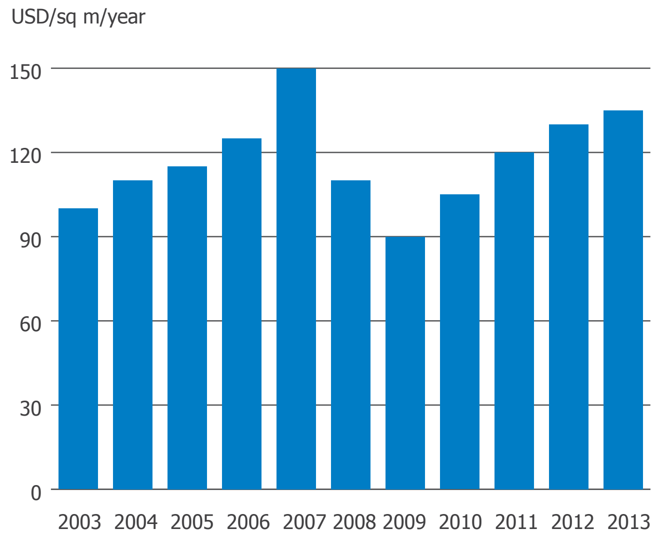
Company	Area	Warehouse complex
Rent		
Major	27,000	STC, Phase II
Conf.	20,000	Nordway, Phase II
O'Key	15,000	Logopark Osinovaya Roscha
BAT Russia	12,000	Logopark Osinovaya Roscha
Automotive	12,000	Orion
Autotrading	8,700	PNK-Shushary
Sale		
Verny	34,900	PNK-KAD
Intertorg	20,000	Sofiyskaya St., 60

16 ▶ Warehouse Demand Breakdown by Company Type, 2013



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

17 ▶ Prime Rent Dynamics in St. Petersburg



Source: AEB North-Western Regional Committee (Jones Lang LaSalle)

Capital Markets

Despite the disappointing macro backdrop real estate investment volumes remain robust and Russia's real estate investment market showed good results in 2013 with investment volumes firmly above pre-crisis levels. Investment into Russian real estate reached USD8.1bn in 2013, which is close to the results of the previous two years, down a mere of 7.5% YoY from 2012 levels. (**18** ▶)

Thanks to a number of key deals foreign capital significantly exceed 2012 levels. We expect this to recede slightly in 2014. Foreign capital amounted to USD3.7bn in 2013, or 45% of total volume, compared to USD1.5bn in 2012 (17% of total investment volume in 2012. The Metropolis and White Gardens acquisitions account for a large part of this. We expect foreign capital to account for 40% of investment volumes in 2014. (**19** ▶)

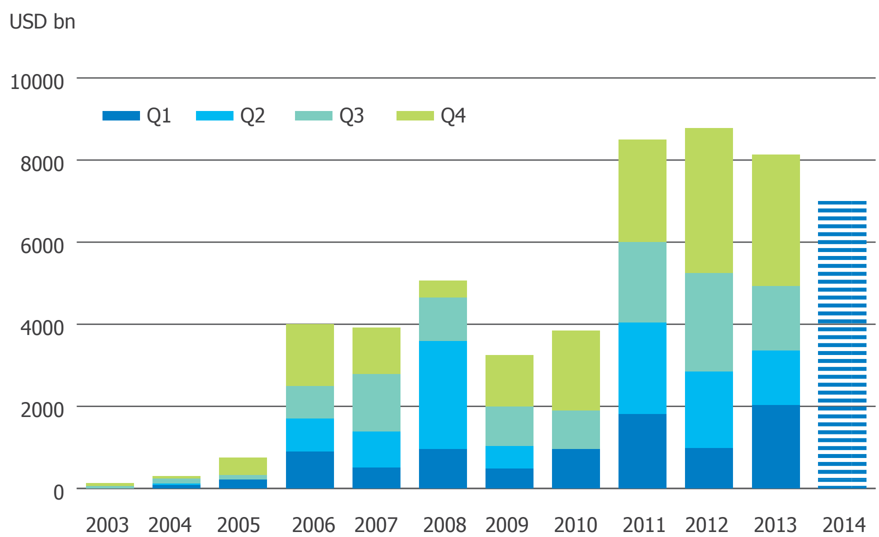
Q4 2013 capitalization rates in Moscow remained unchanged at 8.75% for offices, at 9% for shopping centres and at 11.0% for warehouse sector. The uncertain economic situation in Russia is unlikely to alter this 2014 and we expect capitalization rates to remain flat. (**20** ▶)

2014 investment volumes into Russian real estate market will again exceed pre-crisis results. We expect volumes to reach USD7.0bn. However this doesn't necessarily reflect declining activity on the market, it merely shows that the market does not expect the $bn deals that were a feature of 2011 – 2013.

Yields and capitalization rates likely to remain flat in 2014. The uncertain economic situation in Russia is unlikely to change prime yields and we expect capitalization rates to remain flat in 2014. Although we do not rule out the possibility of yields increase in case of US Fed tapering intensifies suddenly

In 2013 investor interest was still focused on office and retail market segments and their share accounted to around 37% each. Increased investment volume into retail sector (compared to 21% in 2012) is the result of the sale of Metropolis shopping centre. Investment into under-developed retail assets reached USD635m and increased by 127% YoY in 2013. Volumes in the warehouse sector were strong too. The Increased investment volumes into warehouse segment (from 7% in 2012) became possible thanks to the MLP transaction and several built-to-suit deals. (**21** ▶)

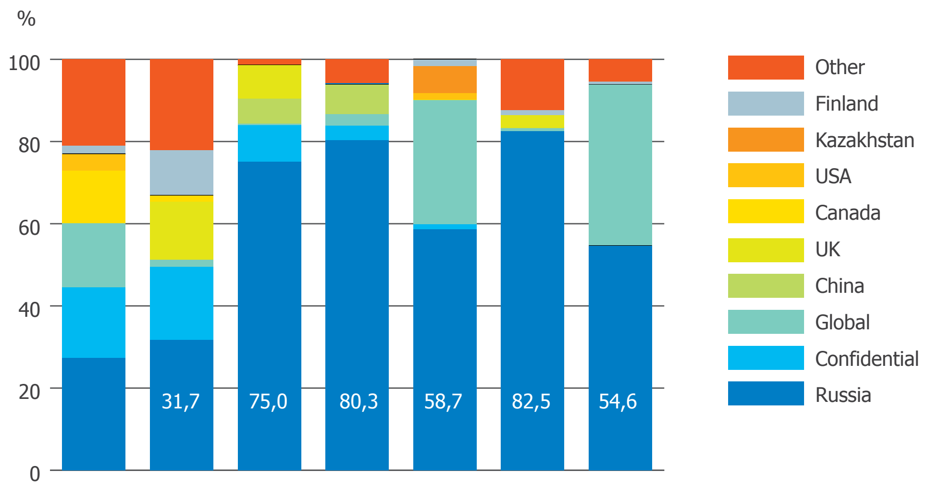
18 ▶ Russia Investment Volume Dynamics



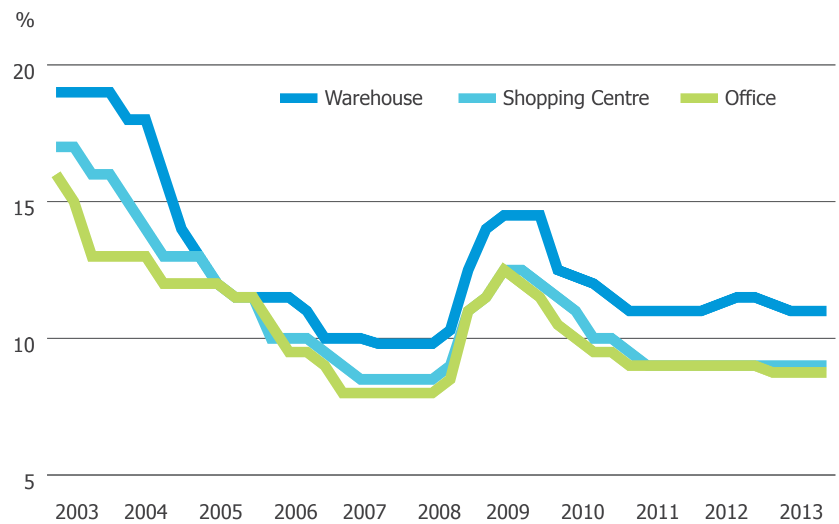
The office market will attract the bulk of investments in 2014. We expect that investors will continue to be interested in office and retail sector in 2014, but the office market segment will dominate. Russian regional shopping centres have great potential with steadily increasing investor interest, although somewhat constrained by the lack of high quality assets.

Investments into warehouses will exceed 10% of total investment volume in 2014, this will be possible because of several deals at the active negotiation stage (for example, Logopark Sever is at the stage of due diligence) as well as elevated demand for built-to-suit projects. Also Russian regional shopping centres have great potential with steadily increasing investor interest, although somewhat constrained by the lack of high quality assets.

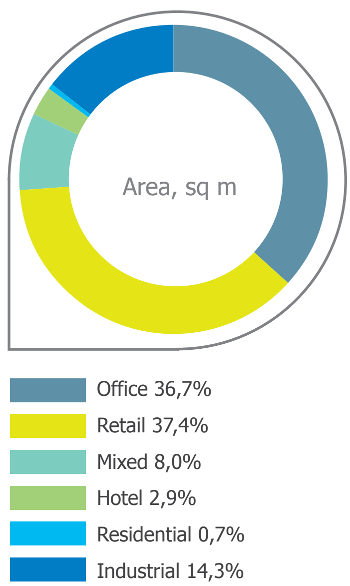
19 ▶ Investors by Source of Capital



20 ▶ Prime Yields Moscow



21 ▶ Investment Volumes Breakdown by Sector



The market was far too optimistic going into 2013. Whilst economists were not predicting growth to reach anything like pre-crisis levels, there was optimism that the 2012 level of 3.5% could be defended in 2013. As it happened, through the year economists were consistently downgrading their forecasts and in the end 2013 growth closed at less than half the IMF's original estimate of 3.7% due largely to stagnant investment and weakening consumption dynamics. (22 ▶)

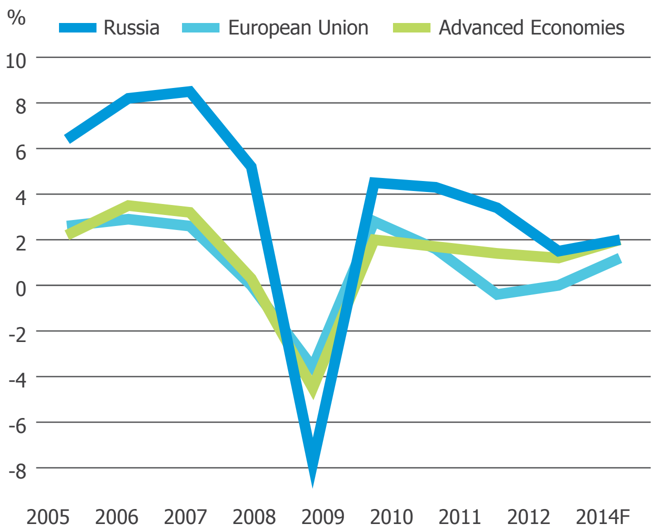
Expectations for 2014 are more realistic. Amid this evidence of slowing growth what gives us some optimism going into 2014 is that the Kremlin has markedly adjusted expectations for future growth with the Economics Ministry's forecast of 2.2% coming comfortably between a wide range of consensus (VTB Capital forecast 1.3% and IMF forecast 3%). Putin has acknowledged that the main drivers for the poor results in 2013 were internal rather than external. That is to say, a lack of Kremlin sponsored initiatives to drive investment. He acknowledged for the first time that Russia's long term growth forecasts will lag other leading emerging economies unless the government targets investment.

Retail sales growth will moderate in 2014. The primary transmission point for the real estate market is through retail sales which we believe will be significantly affected in 2014. Consumption growth in 2013 was largely supported by wage increases (public sector rather than private sector) and as this cools so too will consumer demand (23 ▶)

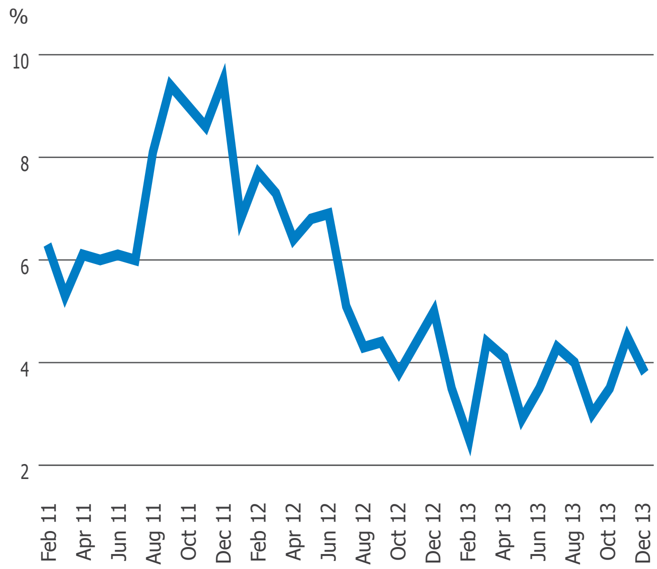
Nonetheless, the spending power of the Russian consumer is still very strong. Retail spending is still relatively strong at c$700bn in 2013. 55% of Russian households are defined by the OECD as middle class and 15% of Russian households earn more than $50k pa. Surprisingly, wealth distribution is actually better than the US (GINI coefficient = 41.7).

Budget constrains will define the switch from consumption to investment led economy. Whereas the budget balanced at $95/bbl in 2008 it now requires $101/bbl to balance and with the budget so stretched, there is little room for the Kremlin to spend, consequently we believe that the it will be forced to focus in 2014 on indirect ways to encourage investment. Efficiency within SOEs, CBR policy and engag-

22 ▶ Real GDP Growth, YoY



23 ▶ Retail Sales Growth, YoY

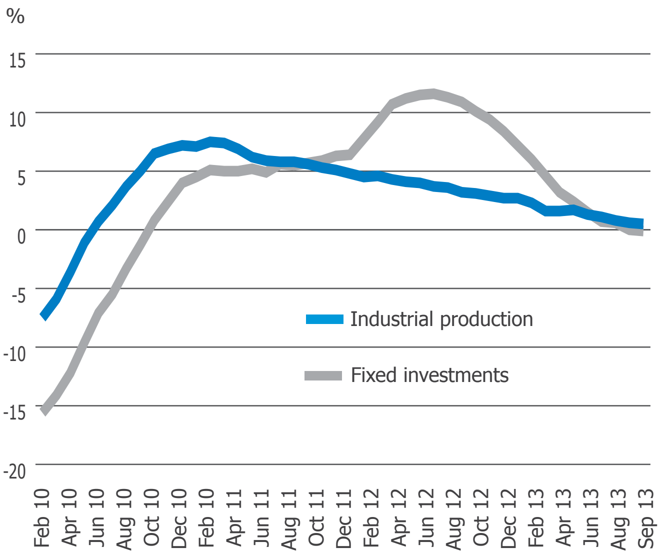


ing foreign capital markets will be the dominant themes through 2014 as the government switches from policies that focus on domestic stability and instead focuses on riskier policies that favour growth. (24 ▶)

The Kremlin will continue to try to improve business sentiment. Kremlin has waged an offensive over recent years to engage foreign capital markets to support investment. Though the Kremlin continues to struggle with its rhetoric it has made quantifiable progress in the last few years bringing the country's business infrastructure closer to developed market standards.

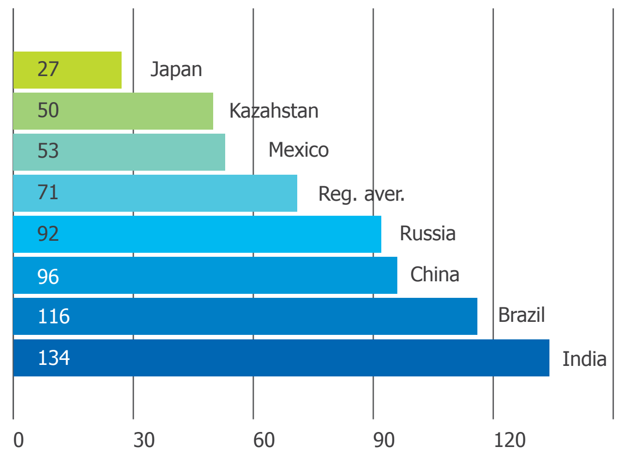
Russia's financial services infrastructure is improving. The merger of MICEX and RTS and MICEX' subsequent IPO, Euroclearability for domestic bonds and equities, T+2 settlement and a Central Depository that is Rule 17f-17 compliant (enabling US pension funds to access local stocks) are important steps in bringing Russia's financial services infrastructure to European levels.

24 ▶ Industrial Production / Fixed Investment Growth, YoY

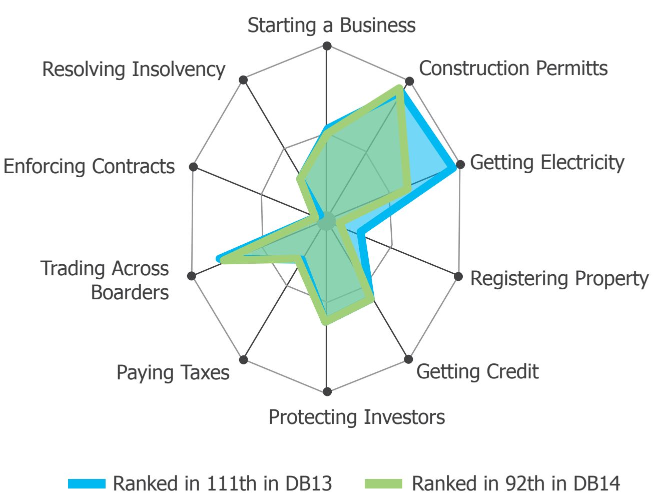


Doing business in Russia appears to be getting easier. Russia will target 2013 was also the year that saw a marked improvement in Russia's ranking on the World Bank Ease of Doing Business Survey (though we note that difficulty in obtaining construction permits and getting electricity remains a burden for the Real Estate industry). In addition, having secured WTO membership in 2012 Russia remains committed to OECD accession which would further integrate Russia with global markets. (25 ▶, 26 ▶)

25 ▶ World Bank Ease of Doing Business 2014 Ranking



26 ▶ World Bank Ease of Doing Business 2014 Ranking



Retail

BRIEF SUMMARY

In 2013 the volume of new construction of retail space in Russia was high, 63 new retail complexes have been constructed and delivered in 40 Russian cities. A reduction in the cconstruction of new quality retail premises in Moscow for 2012-2013 is going to be compensated by large-scale and expected projects in 2014. Retailers are expanding and are interested in new space both in Moscow and all Russia's regions. Despite the growing negative consumer expectations retail turnover growth is positive and most of retailers reported the income growth. During the 2013 rental rents remained stable, as it was in 2012. (27 ▶)

CONSUMERS

According to Rosstat, real income of the Russian population in November 2013 grew up by 1.5%, comparing to November 2012. Moreover, it increased by 3.6% in January-Nove mber 2013 relatively to the same period of time last year. The average monthly salary was 30,670 rubles in August 2013 and increased by 11.6% comparing to the past year. Total retail trade growth for January-November was 3.9%. (28 ▶)

RETAILERS

Retailer demand has remained relatively strong in Russia, with limited new market entrants but existing retailers looking to expand and experiment with new format types. Several brands started operating directly (Montcler, Tommy Hilfiger), others are expanding through franchising (McDonalds Starbucks, Disney Store). There were a number of monobrand flagship openings for popular in Russia brands, such as Reima, Ticcurila, Chicco, Harman, The North Face and some others.

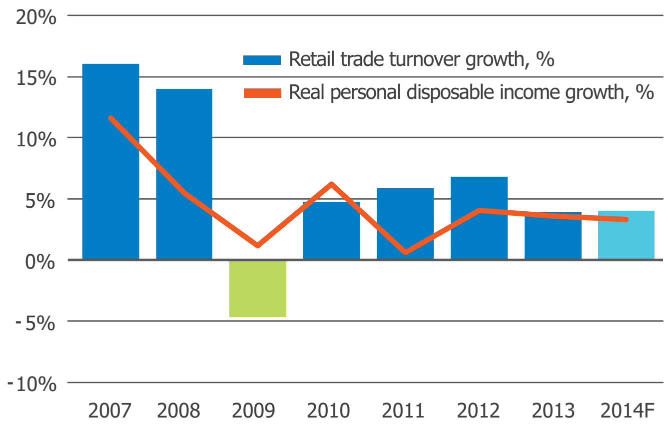
Vacancy rates in prime shopping centres in Moscow are at extremely low levels, with occupiers now transferring interest to the high street as shopping centre space cannot meet the demand.

Those brands already present in Russia are actively looking to expand into the regions. (29 ▶)

RETAIL SPACE

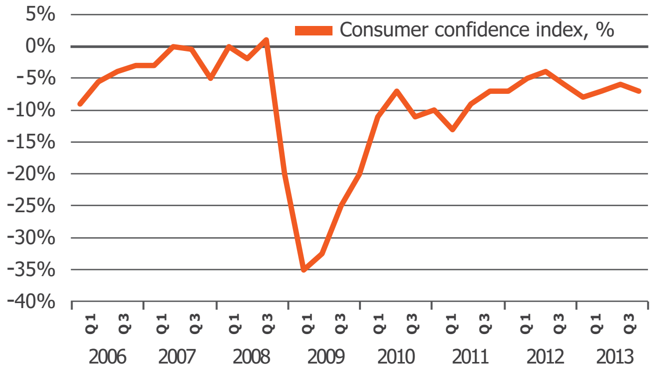
In Q4, the visiting rate of the retail centers was at the higher level than it used to be in several last years. Buyers

27 ▶ **Ratail Trade Turnover and Real Disposable Income, Russia, YOY**



Source: Rosstat

28 ▶ **Consumer Confidence Index, %**



Source: Rosstat

share (amount of people who made a purchase compared to total number of visitors) stood still at respectively low level of 30.6%. It might indicate that consumer's activity is decreasing.

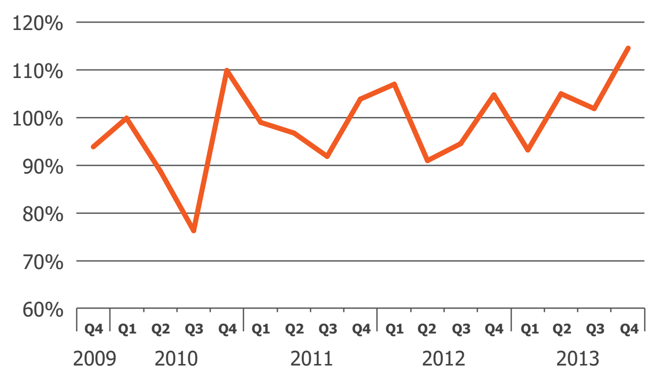
The level of vacant space in the quality retail centers is at the lowest level. During the year 2013 the quality shopping mall vacancy rate was in the range from 1.0% to 1.5%. The low availability was supported by low level of new construction in Moscow in the last years and Moscow government prohibitive policy for commercial development in Moscow.

In general, there is a lack of supply in the quality retail centers in Moscow. (30 ▶, 31 ▶)

NEW CONSTRUCTION: RUSSIA

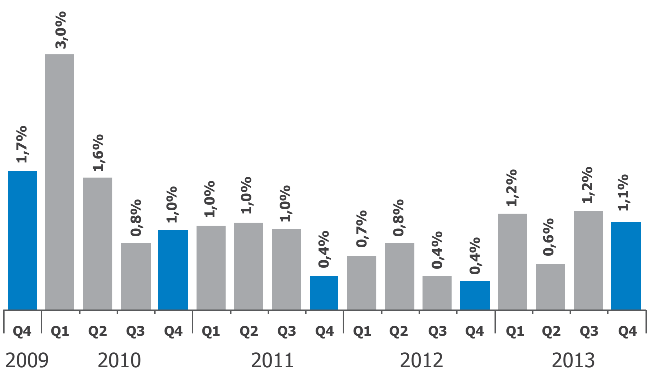
90 quality retail schemes (shopping malls, outlets, retail parks) with total area of 2.8 mn sq m were planned for delivery in 2013. By the end of the year 63 new retail centers were delivered in Russia with a total area of more than 1.6 mn sq m. The new construction volume in Russia is stable at the level of 1.4-1.8 mn sq m annually. In Q4 22 new shopping malls with total GLA 742,000 sq m have been opened outside Moscow. (32 ▶)

29 ▶ Footfall



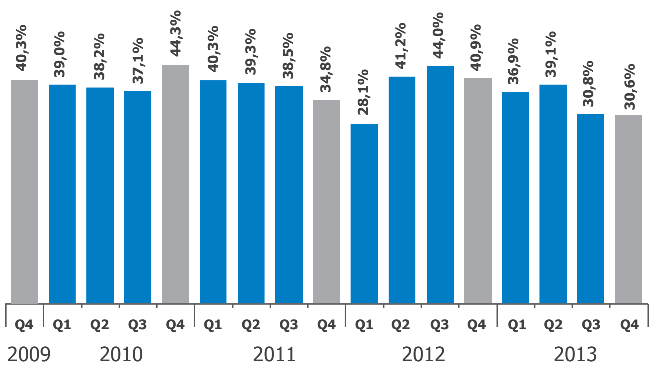
Source: Cushman & Wakefield

31 ▶ Vacancy Rate



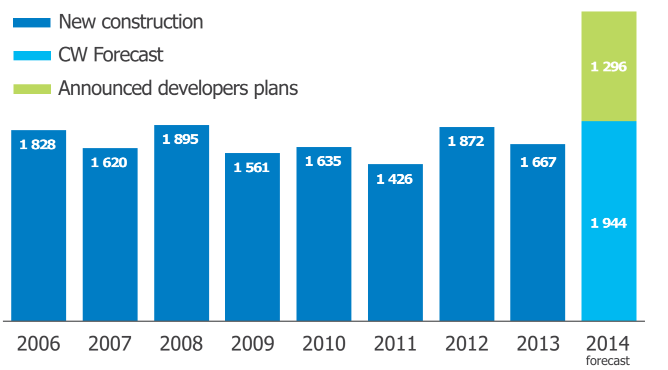
Source: Cushman & Wakefield

30 ▶ "Successful Shopers"



Source: Cushman & Wakefield

32 ▶ Quality Retail Construction, '000 SQ M, Russia



Source: Cushman & Wakefield

Average area of newly constructed shopping centers is decreasing, in 2013 it averaged 24,000 sq m and this is 30% lower than it was in 2011. The development in cities with population less than 1 mn shopping malls (32 from 63) has been delivered in small Russian cities, for example Aero Park City in Bryansk (GLA 91,000 sq m) and Kristall in Tymen (GLA 75,000 sq m).

According to developers' plans 3.2 bn sq m of new quality retail space might be delivered the next year in Russia, most likely around 60-70% will be opened.

NEW CONSTRUCTION: MOSCOW

Five quality retail centers opened in Moscow in 2013. The largest of them was Rio on Leninsky (GLA 57,000 sq m). In Q4 just several neighborhood malls opened (Izmailovsky, SC VDNH) as well as specialized furniture store Roomer.

There are 1.2 mn sq m of quality retail space which is under construction in Moscow at the moment planned for delivery in 2014-2015: Aviapark, that is going to become the largest shopping mall in Europe (GLA 235,000 sq m), Columbus (GLA 140,000 sq m), Vegas Crocus City (GLA 95,000 sq m), River Mall (GLA 91,200 sq m), Mosaika (GLA 67,000 sq m).

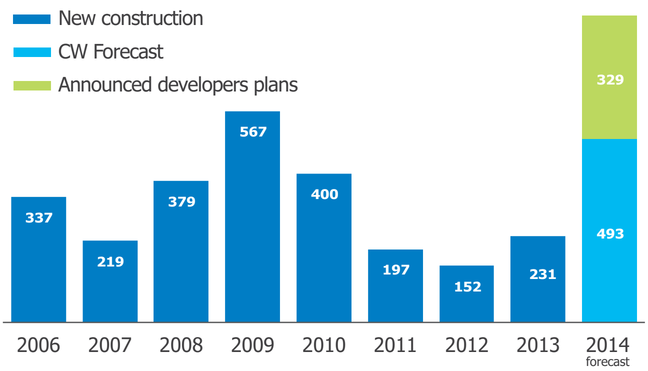
Moscow region construction level was also moderate (comparing with several previous years) – just 4 new shopping malls with total GLA less than 100,000 sq m have been opened. Besides Moscow region excelled by two new fashion outlets, which are still rare in Russia: Fashion House Outlet-Mall (TSUM, Reserved, Samsonite, Reebok, Tom Tailor, Adidas, Kanzler) and Vnukovo Outlet Village (Adidas, Levi's, Ecco, Kanzler, Lacoste). Angry Birds Park became the unique center of attraction for young shoppers in Vnukovo Outlet Village. In 2014 Bella Vita retail park (GLA 36,000 sq m), another new retail format in Russia, might open in Moscow region. (33 ▶, 34 ▶)

COMMERCIAL RATES IN SHOPPING MALLS

Moscow retail gallery rental rates are in the range of US$ 500- 4,000 (per sq m annually before VAT and other expenses) depending on the size of the retail unit and the type of retailer. Throughout Q1-Q3, and the whole of 2012, rental rates were stable across all sub-sectors.

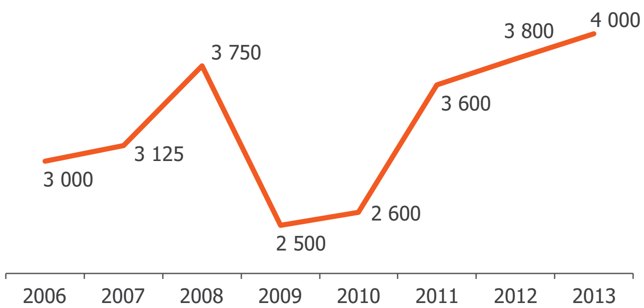
Moscow's prime retail indicator* is US$ 4,000 per sq m per annum, as a base rate. However, a tendency towards rate increases was observed in 2013 and near future growth may be higher than 5% (our current conservative estimate).

33 ▶ Quality Retail Construction, '000 SQ M, Moscow



Source: Cushman & Wakefield

34 ▶ Prime Retail Indicator*, Moscow



* Prime retail indicator — base asking rental rate for the 100-00 sq m gallery unit at the ground floor of the prime shopping centers US$ per sq m per annum, triple net

Source: Cushman & Wakefield

In other cities, rental rates in shopping malls are typically 30% to 60% below Moscow levels.

Additionally, among other payments there are operational expenses (US$ 150-250 per sq m annually for units smaller than 500 sq m), marketing (US$ 10-25 per sq m annually), and others depending on the project. (35 ▶)

HIGH STREETS

The analysis of the retail spaces on the most passable areas in the city centre shows that the most popular categories of tenants are catering (cafe, restaurants) and clothing shops. They occupy 29% and 21% of all premises respectively. Significant tenants are those who offer the following services: spa, hairdressers, medical services, communications companies, photography and legal services – all of them occupy 10% of retail premises on the main streets of the city, banks, jewelry stores, cosmetic stores and accessories occupy 5%.

As before retailers prefer central locations – Okhotny Ryad, Tverskaya, Kyznetsky Most areas.

The important trend of 2013 is the Moscow government strategy to expand the Moscow pedestrian areas. The new pedestrian streets might increase the quality supply and the retailers' interest to them is strong.

The other new street retail premises are supporting retail in large office buildings, hotels and mix-use complexes. These locations are generating the predictable paying capacity and foot flow.

35 ▶ Quality Retail Lease Structure

Item	Comments
Lease Terms	Standard lease terms for gallery tenants are between 3-5 years, break options are rare. For anchor tenants (including fashion anchors) lease terms are up to 20 -25 years and break options are becoming popular.
Rental Payment	Rents are typically payable monthly in advance. Turnover / percentage rents are increasingly seen in shopping centres. Rental rates are generally calculated in USD, Eur or commercial units are used. In less quality shopping centres rental rates are calculated in RUR.
Rent Deposit	The rent deposit required in quality shopping centres is typically between 1 – 3 months rent equitant.
Indexation	Annual indexation is typical between 3-10% or at a level of USD / EU CPI. The practice of premium / key money payments is seldom seen in Russia. Rent reviews are rare on the market.
Service Charges	Service charge is payable by tenants at either an "open book" basis or more common as a fixed cost. Utilities payments are charged on consumption. Building insurance is normally charged back to tenant via service charge.
Other costs	VAT 18% Local property taxes are not payed separately, they are generally included in the service charges.

Source: Cushman & Wakefield

The establishment of obligatory paid parking in downtown might shift some tenants to the new streets with high traffic, for example, the new life could enjoy the Garden Ring. Rental rates in the trade corridors are stable. Nevertheless there were a few expensive deals in prime streets with deal rates above average by 15-20%. There is a tendency for increasing lease terms in the last few years. As an example, three years ago contracts used to be short-term mostly (11 months) and now agreements for the 3 and 5 years period become more and more widespread. (36 ▶)

HIGH STREETS – PEDESTRIAN AREA

The most important event for the high streets became the development of pedestrian zones in Moscow, which is actively supported by the city government. There is a change of visitor flows (from passengers to pedestrians) on those streets, where the driving was cancelled (it concerns Bolshaya Dmitrovka street first of all). There is a huge potential for retail activity talking about pedestrian streets and retailers show great interest in developing of those areas. The expansion of pedestrian zones will significantly increase the supply of the quality retail premises in Moscow.

36 ▶ High street rental rates

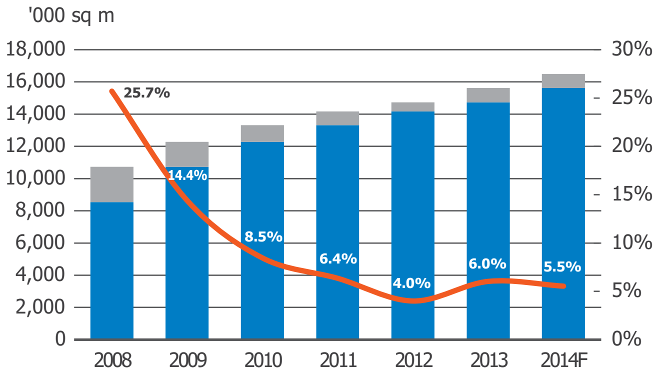
HIGH STREET	USD / sq m / annum	2013 TREND
1st Tverskaya Yamskaya	$2,500 - $3,000	stable
Arbat	$2,000 - $4,000	stable
Garden Ring	$1,500 - $3,000	stable
Kutuzovsky Prospekt	$1,500 - $3,000	stable
Kuznetsky Most	$2,000 - $4,000	stable
Leningradsky Prospekt	$1,200 - $2,200	stable
Leninsky prospect	$1,500 - $3.000	stable
Prospect Mira	$1,200 - $2,500	stable
Novy Arbat	$1,500 - $3,000	stable
Petrovka	$2,500 - $5,000	stable
Pyatnitskaya	$1,200 - $2,800	stable
Tverskaya	$3,000 - $6,000	stable
Stoleshnikov per.	$4,000 - $6,000	stable

Source: Cushman & Wakefield

Moscow Office Market in 2013: Solid Results, with Cautious Outlook

Moscow, 30 January 2013 – 302,641 sq m of new office space was delivered in Q4 2013 in Moscow. As a result, the total level of completions in 2013 proved to be 57% higher on a YoY basis and equaled to 888,269 sq. m, bringing the total volumes of office stock in Moscow to a record 15,620,980 sq m. This year, we anticipate another 865,027 sq m of new supply coming to the market, which translates into a 5.5% YoY growth in the volume of total office stock in Moscow. (37 ▶)

37 ▶ Moscow Total Office Stock (Dynamics and Outlook)



Source: Jones Lang LaSalle

In Q4 2013 seventeen new buildings were delivered most of which belong to Class B+. In terms of location of new supply, about 75% of all Q4 deliveries were in the areas outside the Third Transportation Ring (TTR) compared to the Central Business District which accounted just for 7% of all deliveries. (38 ▶)

As far as the annual supply is concerned, around 60% of it was commissioned in decentralized areas. We believe that this trend is likely to continue in the near term – about 74% of total office space expected be delivered by the end of 2014 will be located outside the TTR while in terms of classes, the majority of total completions will likely be seen in Class B+. The key reasons for these developments is the intention of the city authorities to restrict office construction in the areas inside TTR, particularly in the historical center of Moscow Combined with this areare lower rents and more options for tenants outside TTR in terms of available office space. (39 ▶, 40 ▶)

38 ▶ Main deliveries in Q4 2013

Property	Office Area, sq m	Location	Class	Status
Park Pobedy	92,000	Outside TTR	B+	New
Riga Land (Phase II, Block A)	33,924	Outside TTR	B+	New
RTS BC	33,000	Outside TTR	B+	Refurbishment
Golden Gate	20,825	Between Garden Ring and TTR	B+	New
Premium West	18,868	Outside TTR	B+	New
Arma	14,362	Between GR and TTR	B+	Refurbishment
Melnikoff House	14,104	Between GR and TTR	B+	New
Inchcape City	13,099	Outside TTR	B+	Refurbishment
Khameleon	12,000	Outside TTR	B-	Refurbishment

Source: Jones Lang LaSalle

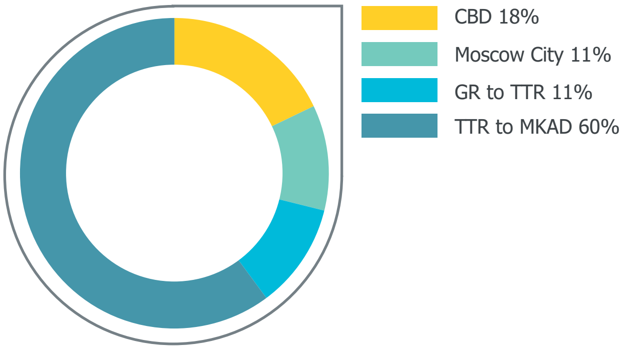
In terms of leasing activity, the market was solid in Q4 with take-up volumes being 18% higher on a quarterly basis at 381,252 sq m. Nonetheless, the annual result was 4.4% lower YoY with the volume of transaction totaling 1.43 m sq m compared to 1.49 m sq m seen for 2012. The amount of transacted space within the decentralized submarkets accounted for 50% of total take-up in 2013 and domestic tenants were slightly dominant, accounting for 60% of all transactions in 2013.

Gyunay Guseynova, Analyst of Office and Occupier Research, Jones Lang LaSalle, Russia and CIS, commented: In terms of deal type, the share of sales has decreased from 29% 2012 to 10% in 2013 which could be a signal that market participants became more cautious when deciding whether to buy or to rent real estate assets in the current price environment. (**41** ▶)

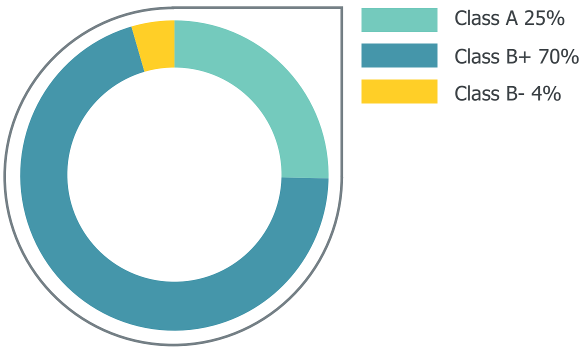
Among the largest transactions in 2013 there were leases of an additional 20,000 sq m of office space by Yandex in Krasnaya Roza BC, the lease of 14,000 sq m of office space by Norilsk Nickel in Mercury City Tower, the purchase of 10,000 sq m in Mercury City Tower by Japan Tobacco International and the renewal of around 8,700 sq m in Naberezhnaya Tower by IBM. The main drivers were companies from the Business Services sector, accounting for 33% across all deals recorded in 2013. Three other sectors: Manufacturing, Banking & Finance, Construction, Mining & Exploration accounted for a considerable share of activity with 23%, 14% and 12% respectively. (**42** ▶, **43** ▶)

Despite the considerable volumes of new supply seen in Q4, the overall vacancy rate ticked up slightly over the quarter and stood at 13.7%. At the same time, vacancy levels for Class A offices turned to be a little lower compared to the levels of the previous quarter with the overall figure of 18.2% in Q4 vs 18.9% seen in Q3. By the end of 2013, a noticeable increase in vacancies was seen in Class B+ due to the large volume of new office space delivered to the market in Q4 2013.

39 ▶ Completions by Location (2013)

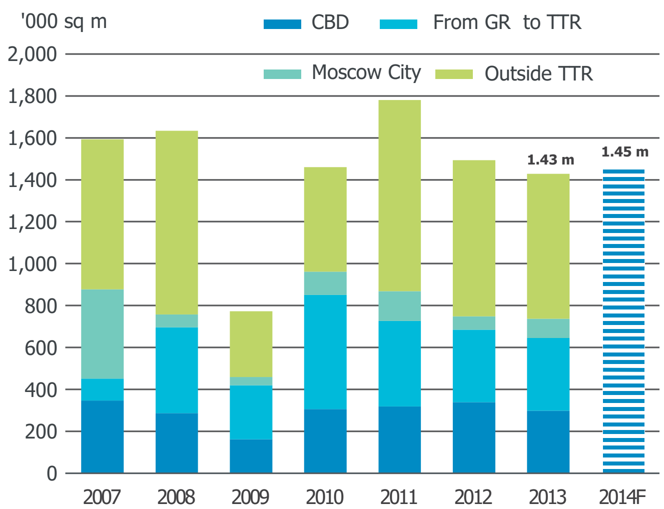


40 ▶ Completions by Class (2013)



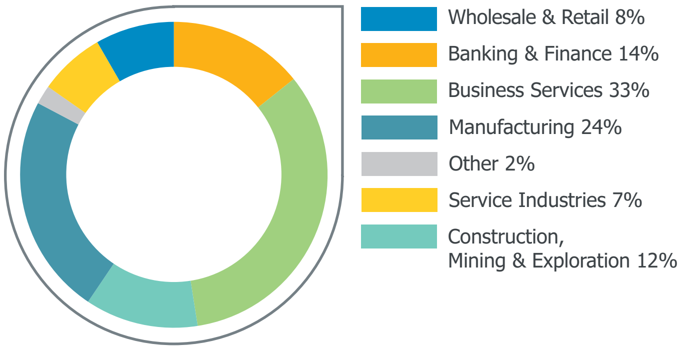
Source: Jones Lang LaSalle

41 ▶ Moscow Total Take-up (Dynamics and Outlook)



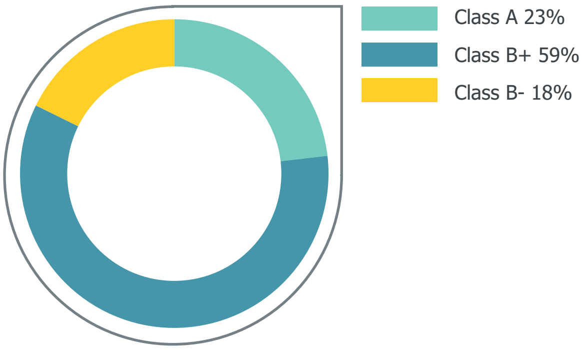
Source: Jones Lang LaSalle

42 ▶ **Demand by Business Sectors (2013)**



Source: Jones Lang LaSalle

43 ▶ **Demand by Class (2013)**



Source: Jones Lang LaSalle

Warehouse and Industrial

SUMMARY 2013

Moscow region

- 850,000 sq m of quality warehouse space were put into operation in 2013.
- The volume of leased and purchased warehouse space amounted to 1.3 mn sq m
- Average rental rates at year-end over $135 per sq m per year in Class A without VAT, operating expenses and utility costs.
- The sale price is $1200 – $1300 per sq m in typical projects of class A build to suite projects.
- The vacancy rate in Class A warehouses 1.5%.

Russia except Moscow region:

- New construction in the regions was more than 310,000 sq m.
- The volume of leased and purchased warehouse space in 2013 amounted to 410 sq m.
- In 2013, rental rates have increased, there is a tendency to reduce the vacancy rate. (44 ▶)

SUPPLY

Moscow region

In the past 2013 supply increased to 850,000 sq m, which is 16% higher than in 2012. It is a new record since 2008. In the Q4 2013 there was built about 196,000 sq m.

In 2013 there were built only 70% of the warehouse space announced by developers. There is a lack of ready- to-move storage space on the market. The vacancy rate in Class A warehouses over the past year remained unchanged at 1.5%.

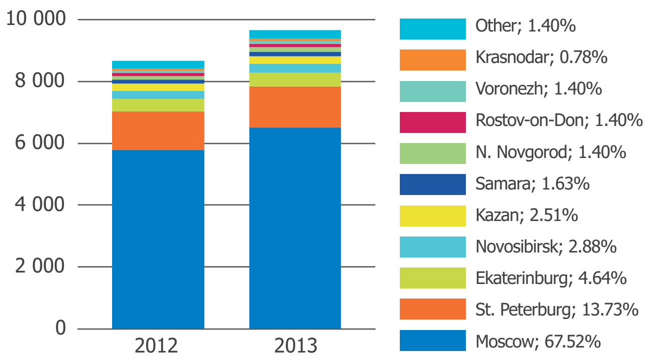
In 2014 the developers announced for delivery more than 1.8 million sq m of warehouse spaces, but according to our estimations they will built about 1.2 million sq m of announced volume. Most space will be located on the north and north-west of Moscow region. (45 ▶)

Russia (except Moscow region)

Over the past 2013 in Russian regions, except the Moscow region were built more than 310,000 sq m of new high quality warehouse space, which is 5% less than in 2012. More than 110,000 sq m (40%) was built in the Leningrad region and St. Petersburg. More 75,000 sq m (25%) was built in the Krasnodar. New warehouse space were constructed in Novosibirsk, Samara, Saratov and Sverdlovsk regions.

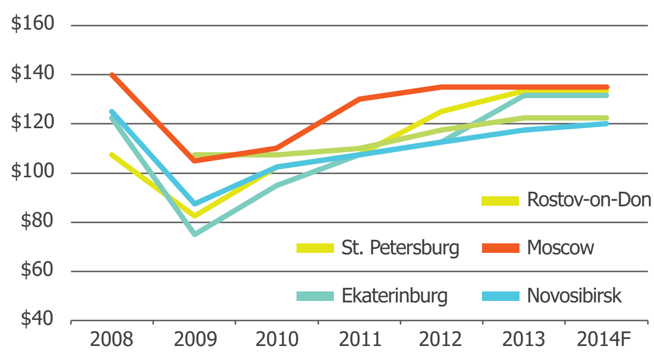
According to preliminary estimates, the volume of new construction in 2014 will increase by 1.5 times. Leader of the new construction will still be St. Petersburg, where will be build more than 30% of the total supply in the regions. (46 ▶)

44 ▶ Existig Stock, Class A (1,000 SQ M)



Source: Cushman & Wakefield

45 ▶ Rental Rates in Major Russian Cities, Class A



Source: Cushman & Wakefield

DEMAND

Moscow region

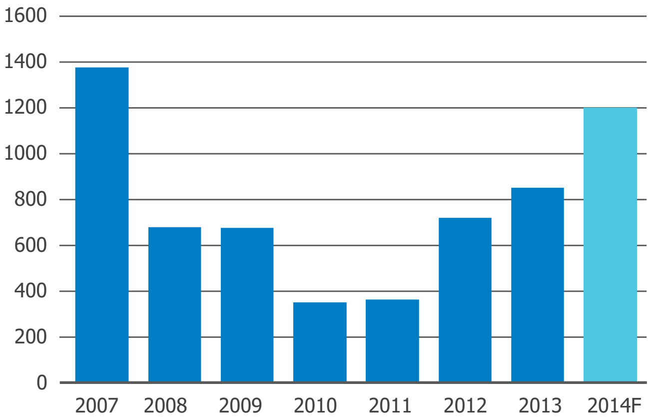
Since 2009, the volume of transactions on the market is growing. In 2013 the volume of transactions amounted to more than 1.3 million sq m, which is an absolute record on the market.

In 2013, the share of acquired property increased and amounted to 37% of total absorption. (47 ▶, 48 ▶)

About 30% of the total absorption was provided by retail segment companies. The average deal size in the sector decreased by 15% and amounted to 17,000 sq m.

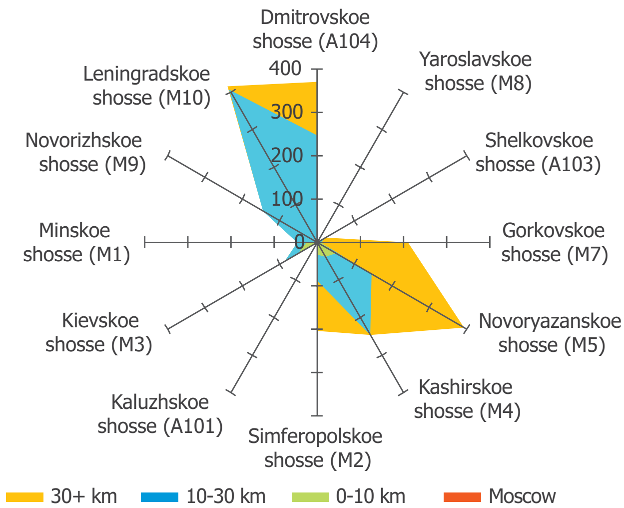
The proportion of manufacturing companies is greatly increased from 14% in 2012 to 25% in 2013. An increase was caused by a double growth of the transactions size, but the number of transactions were decreased. In the segment of distribution and logistics observed 50% reduction in the number of transactions, while increasing transaction size by 20-30%. In general, the market size of the deal in 2013 increased by almost 40% from 13,000 to 18,000 sq m.

46 ▶ New Construction in Moscow Region (1,000 SQ M)



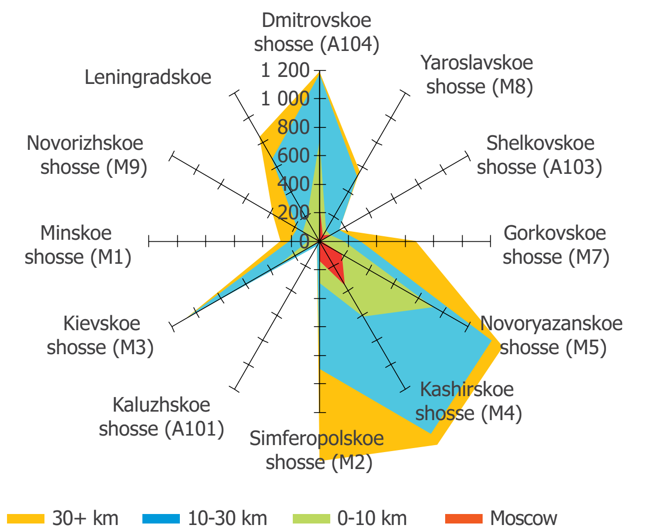
Source: Cushman & Wakefield

47 ▶ Distribution of Quality Development Geographical Pipeline for 2014 ('000 sq m)



Source: Cushman & Wakefield

48 ▶ Distribution of Warehouse Space in the Moscow Region, ('000 sq m)



Source: Cushman & Wakefield

Russia (except Moscow region)

In 2013, the amount of absorption was about 410,000 sq m, 62% more than in 2012. This is a record of absorption since 2008, but unlike the Moscow region, in this market there is no steady growth in volume of transactions, moreover since the beginning of 2012 until mid-2013 there was decrease of absorption volume.

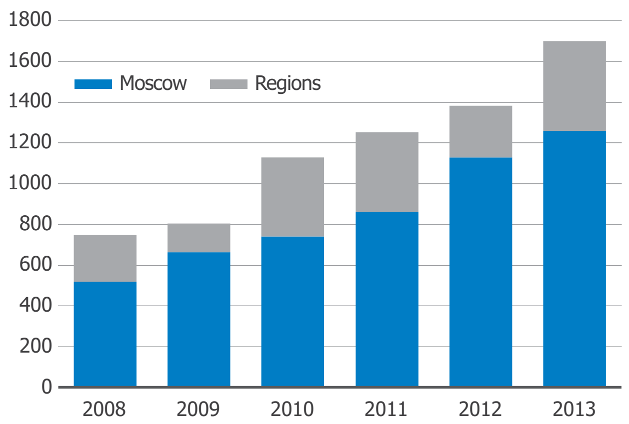
Absorption increase in 2013 was due to retail and logistics companies, in both cases increased in the number of transactions and the size of the transaction.

Market share of retail companies has increased from 29% to 59%, the number of transactions by 63%, average transaction size by 70%.

In 2013, the share of transactions for the purchase of warehouse space was 34%.

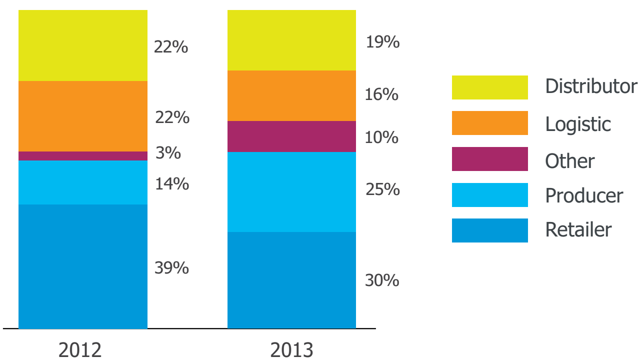
Most space was leased or purchased in St. Petersburg (39%), Novosibirsk (28%) and Rostov-on-Don (11%) regions. (49 ▶)

49 ▶ Take Up, '000 sq m



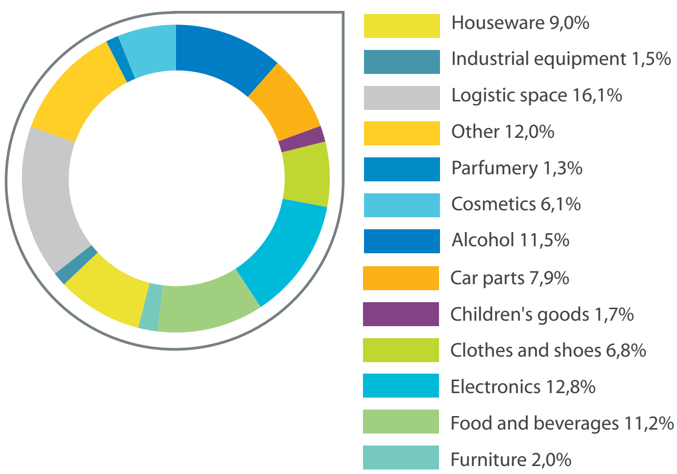
Source: Cushman & Wakefield

50 ▶ Structure of Demand, Moscow



Source: Cushman & Wakefield

51 ▶ Structure of Demand, Moscow



Source: Cushman & Wakefield

RENTAL RATES

Moscow region

For 2013 the average rental rates have not changed and were $135 per sq m per year, excluding VAT and operating expenses and utility costs. At the same time, we note an increase in rental rates which depends on the distance from MKAD and on direction. Highway traffic is an important factor.

Russia (except Moscow region)

In St. Petersburg and Yekaterinburg rental rates rose to the level of Moscow in 2013 and reached $130-$135 per sq m per year.

In general, during the 2013 rental rates growth for quality warehouse facilities was observed in Nizhny Novgorod, Rostov-on-Don, Krasnodar, Novosibirsk and Ufa regions. In these cities rental rates at year-end were close to around $120-$125 per sq m per year. (**50 ▶**, **51 ▶**)

TRENDS

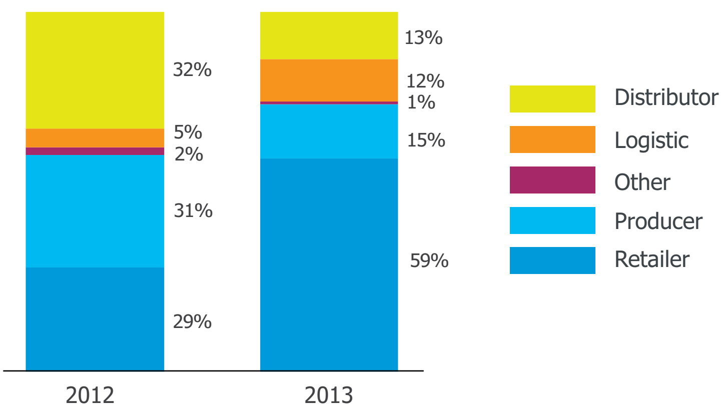
Demand for quality warehouse space in the warehouse segment was consistently high, with a tendency to geography expansion. In general, this segment is the most stable commercial real estate market for several years. Basis of demand in this segment in Russia are traditionally the retail segment companies.

Together with expanding the demand geography, the geography of development is also expanding. In regions the volume of new construction increases due to the entry of new players in the federal and local level, and due to the resumption of the construction of previously suspended warehouse projects.

In 2014 in Moscow and the Moscow region, we expect the increase in construction, and the increase of speculative construction share. According to our forecasts, rental rates do not change. Volume of absorption will be at 2013 figures level, there is an upward trend in vacancy rates.

In Russia, except for Moscow and the Moscow region, we expecting growth of the new construction volume and the supply will not keep up with demand, then the vacancy rate will continue to reduce. This may form the delay demand. In some regions the rental rates growth will slow down. (**52 ▶**)

52 ▶ Structure of demand, Regions



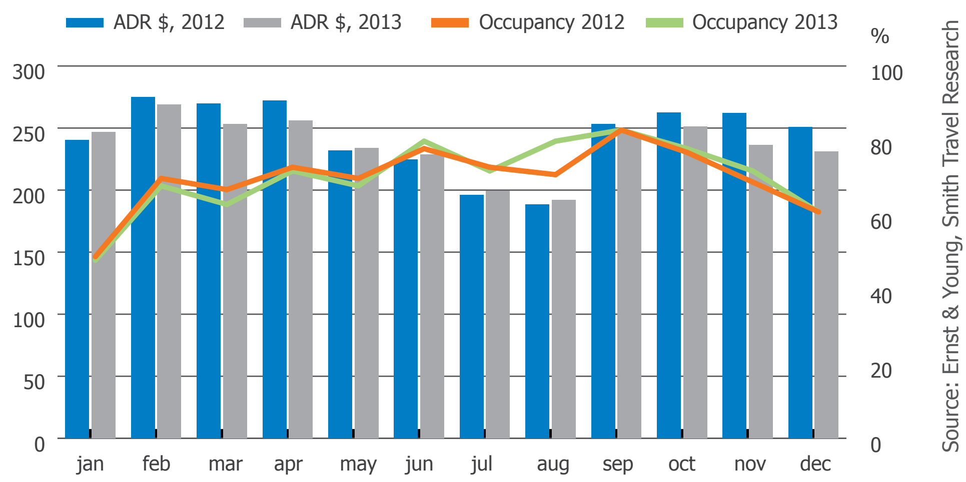
Source: Cushman & Wakefield

Hospitality – Moscow Hotels in Q4 2013

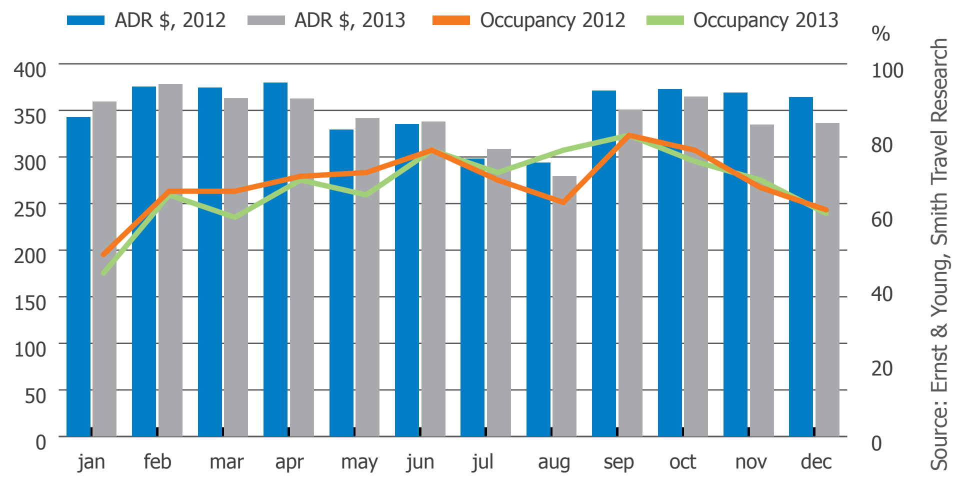
Operational indicators, such as average daily rate (ADR) and RevPAR (revenue per available room), across all segments of Moscow hotels for the period from January to December 2013 demonstrated a 3% decrease as compared to 2012. Thus, ADR amounted to 237 US Dollars and RevPAR - to 165 US Dollars. Average occupancy across all market segments of Moscow hotels remained unchanged and comprised 70%. (53 ▶)

ADR and RevPAR of upscale hotels demonstrated a negative trend compared to 2012: ADR decreased by 2% amounting to 343 US Dollars and RevPAR droped by 3% amounting to 231 US Dollars. The overall occupancy remained unchanged and comprised 68%. (54 ▶)

53 ▶ Average Market ADR ($) and Occupancy Dynamics, 2013 vs. 2012



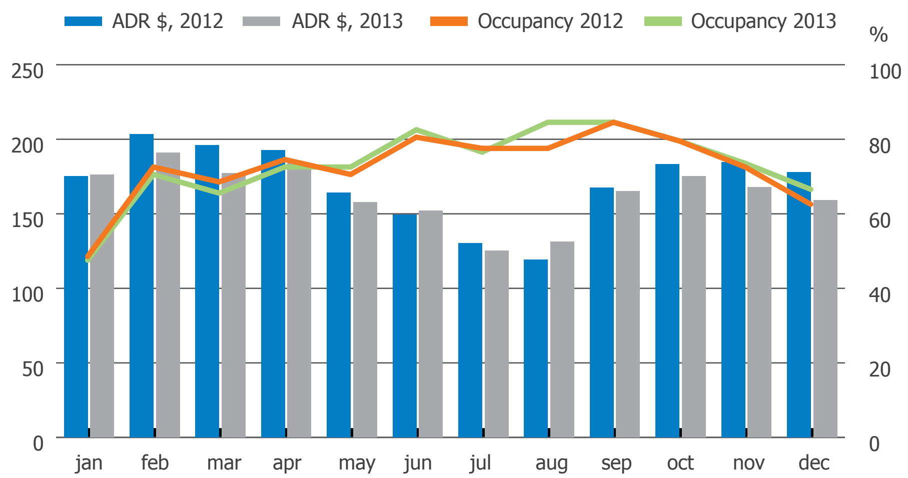
54 ▶ 5-star Hotels: ADR ($) and Occupancy Dynamics, 2013 vs. 2012



The operating indicators of business hotels demonstrated the following results: both ADR and RevPAR dropped by 3% compared to 2012 and comprised 205 US Dollars and 145 US Dollars respectively. The overall occupancy remained unchanged comprising 71%. (55 ▶)

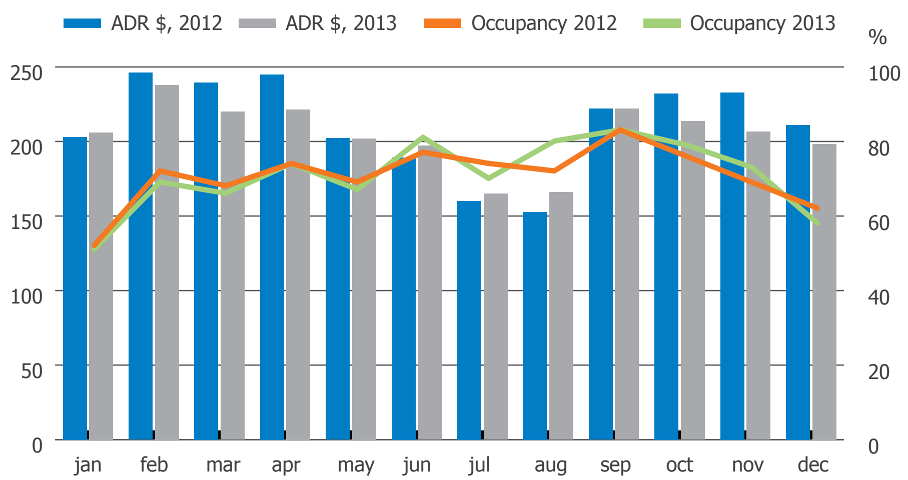
ADR and RevPAR of midscale hotels also showed decrease: ADR dropped by 4% (164 US Dollars) and RevPAR – by 3% (118 US Dollars). The overall occupancy demonstrated a slight increase comprising 73%. (56 ▶)

55 ▶ 4-star Hotels: ADR ($) and Occupancy Dynamics, 2013 vs. 2012



Source: Ernst & Young, Smith Travel Research

56 ▶ 3-star Hotels: ADR ($) and Occupancy Dynamics, 2013 vs. 2012



Source: Ernst & Young, Smith Travel Research

An absolute gap in RevPAR between the segments in January –December 2013 had slight changes compared to 2012 and demonstrated the following results:

- The variation between the upscale and midscale segment comprised 113 US Dollars (116 US Dollars in January – December 2012).
- The variation between upscale and business hotels comprised 86 US Dollars (89 US Dollars in January – December 2012).

During 2013 six hotels opened in Moscow:

- The five-star Nikolskaya Kempinski hotel on Nikolskaya Street, 12/1 opened in May. The hotel comprises 211 rooms, three restaurants, two bars, a lobby bar, a SPA and five conference rooms.
- The four-star Novotel Moscow City hotel located at Presnenskaya Embankment, 2 (Moscow City) opened in February. The hotel comprises 360 rooms, a restaurant, a bar, eight meeting rooms and a fitness center.

57 ▶ Operational Indices Dynamics

	January – December 2013 (US Dollars)	**January – December 2012** (US Dollars)	**January – December 2013 / January – December 2012,** %
5 stars			
Occupancy	68%	68%	0%
Average daily rate (ADR)	343 $	350 $	-2%
Revenue per available room (RevPAR)	231 $	238 $	-3%
4 stars			
Occupancy	71%	71%	0%
ADR	205 $	211 $	-3%
RevPAR	145 $	149 $	-3%
3 stars			
Occupancy	73%	72%	1%
ADR	164 $	170 $	-4%
RevPAR	118 $	122 $	-3%
Average			
Occupancy	70%	70%	0%
ADR	237 $	244 $	-3%
RevPAR	165 $	170 $	-3%

Source: Ernst & Young, Smith Travel Research

- At the end of July Starwood Hotels & Resorts opened a new Sheraton Moscow Sheremetyevo Airport hotel located 700 m away from terminal D of the international Sheremetyevo airport. The 342-room hotel features more than 1 000 sq. m of meeting space, two restaurants, a fitness-center and a SPA.
- A new Accor hotel complex opened in mid-December. The complex comprises three hotels: Mercure Moscow Paveletskaya (149 rooms), Ibis Moscow Centre Bakhrushina (190 rooms) and aparthotel Adagio Moscow Centre Paveletskaya (94 rooms). The complex offers a restaurant, a bar, a fitness center, a wellness center, eight conference rooms and underground parking.

Overall, the performance of Moscow hotels in 4Q 2013 confirmed the stabilization of hotel market. In 2014 we expect further continuation of positive trends, as well as increase of existing hotel supply and resumption of postponed construction works on hotel projects. (53 ▶)

58 ▶ Future Hotels Announced for Opening in Moscow and Moscow Region in 2014

Name	Room number	Address	Class
Four Seasons Hotel Moscow	180	Okhotny Ryad Street, 2	5 stars
Astrum Hotel Shelkovo	184	Shelkovo, Promenade Serafima Sarovskogo, 2	5 stars
Moscow Marriott Novy Arbat Hotel	230	Novy Arbat, 32	5 stars
DoubleTree by Hilton Moscow Leningradsky Riverside	270	Leningradskoye Highway, 39/7	4 stars
DoubleTree by Hilton Moscow Vnukovo Airport	432	Vnukovo Airport	4 stars
Hilton Garden Inn Moscow New Riga	162	New Riga Highway (45 km from MKAD)	3 stars
Mercure Moscow Baumanskaya	44	Baumanskaya Street, 54/1	3 stars
Radisson Sheremetyevo Airport	379	Sheremetyevo Airport	3 stars
Ibis Oktyabrskoye Pole	200	Marshal Rybalko Street, 2	3 stars
Ibis Stupino	120	Stupino, Pobedy Avenue	3 stars
Hampton by Hilton Moscow Strogino	214	Kulakova Street	2 stars

Residential

2013 overall was characterized by reduced demand with slightly higher average budgets. The increase in the average budget is most likely due to an increase by a few large companies of the number of expatriate top-managers. (**59** ▶)

LOCATION

The center of the city remains the most popular location for higher-end rentals in Moscow with 60% of all requests falling in this area. Within the center, "Patriarchy Ponds", "Chysty Prudy, Kitay Gorod" and "Arbat, Kropotkinskaya", areas remained the top requested locations throughout 2013. (**60** ▶)

On the supply side the top three areas are identical to the demand, albeit in a different order. Also, there remain some areas with excess supply. For example, Kutuzovsky prospect area accounts for less than 3% of all demand, but for over 5% of supply. (**61** ▶)

APARTMENT SIZE

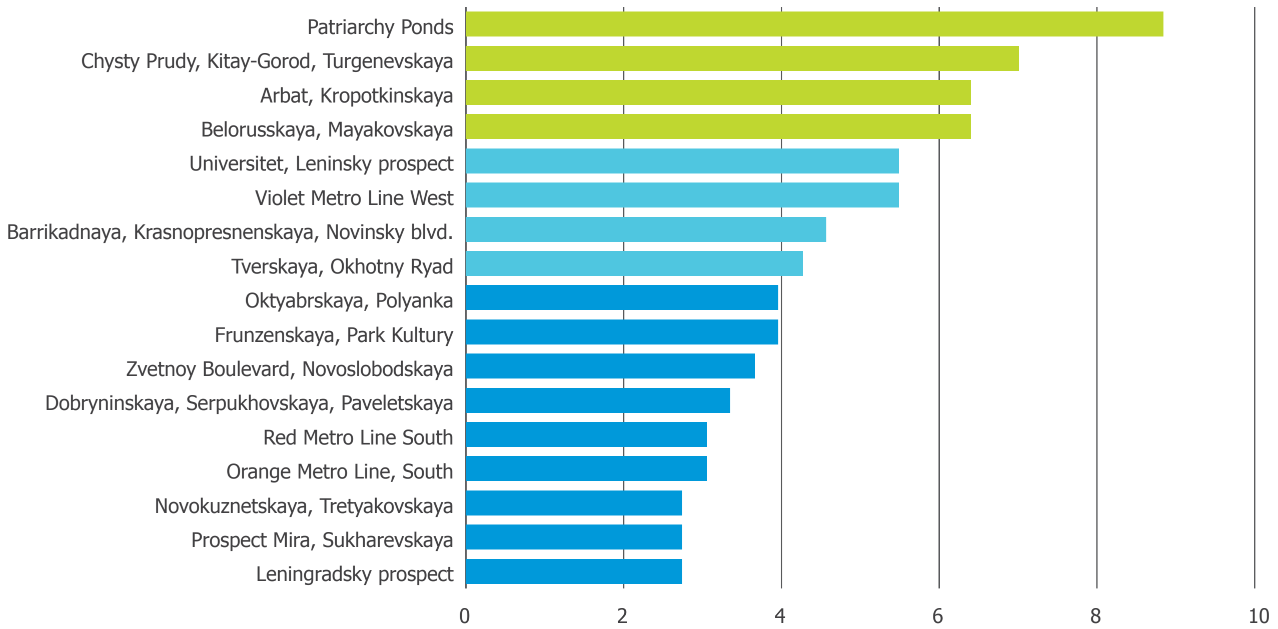
In 2013 demand for 2-room (1-bedroom) apartments surpassed the demand for 3-room (2-bedroom) apartments, which were most demanded in 2012. While there was a slight increase in the number of expatriate upper-management moving to Moscow, the number of families with children was lower than in 2012. As a result, the smaller, 1-bedroom, apartments are becoming more and more popular. (**62** ▶)

While 3-room apartments represented over 36% of all apartments offered on the market, 2-room apartments accounted for only slightly over 28%. This is almost a mirror image of the demand side. As a result finding a good 2-room apartment at a decent budget has become more difficult over the last 12 months. However, those looking for larger accommodations were also facing issues as the asking price for larger apartments, suitable for families with children, are often above the accommodation budget allocated to expatriates. (**63** ▶)

59 ▶ Changes in Number of Requests

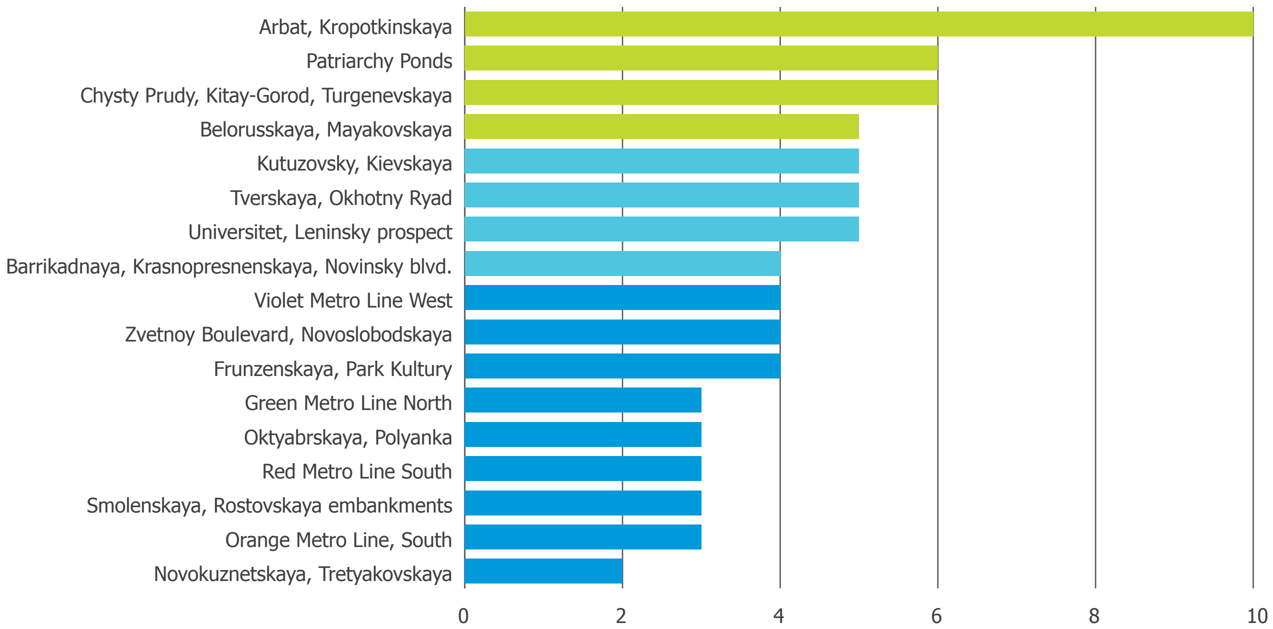
Source: Evans Property Services

60 ▶ Rental Requests by Area



Source: Evans Property Services

61 ▶ Apartments Offered for Rent by Area



Source: Evans Property Services

BUDGET

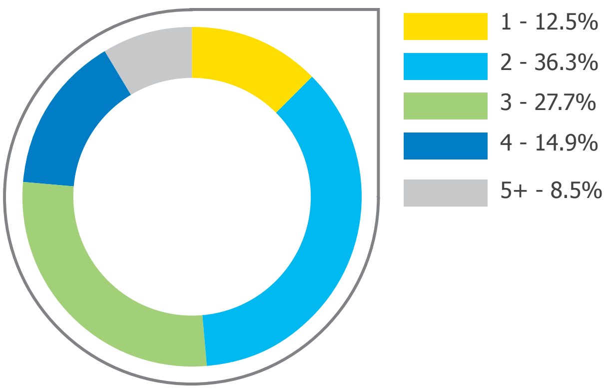
Overall, the average budget for all requests in 2013 increased slightly to $4 500 per month, from $4 360 in 2012. However, this increase came from the "$4 000 - $8 000 per month" segment, as the higher segments showed a slight decrease. (64 ▶)

Almost 70% of all apartments offered for rent on the Moscow market in 2013 were priced at, or below $8000 per month. While the supply of apartments in upper segments is considerable very often the asking price is not in line with the type or quality of the property that is being offered. As a result, finding a quality apartment without any "caveats" is still difficult in any budget. As always, regardless of the budget, finding an apartment for families with small children or pets is even more difficult. (65 ▶)

EXPECTATIONS

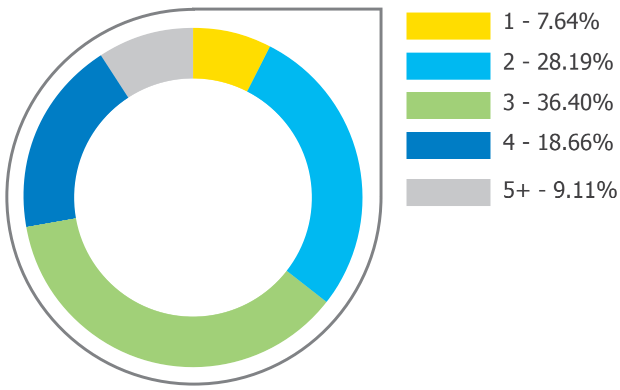
Given the situation on the market throughout the previous year we do not expect any significant changes in 2014. Absent any significant, unexpected changes in the economy overall, both average budgets and demand should stay the same. However, sharp fluctuations of the Russian Ruble, are likely to force some landlords to try to renegotiate agreements denominated in the local currency. In the last several years many companies have changed their housing budgets into Rubles and as a result very few rental agreements are signed in Dollars or Euros, a practice prevalent just a few years ago. As such, tenants whose rental agreements are coming up for renegotiation should expect a change in currency or other concessions, such as increased rental rates.

62 ▶ Rental Requests by Number of Rooms



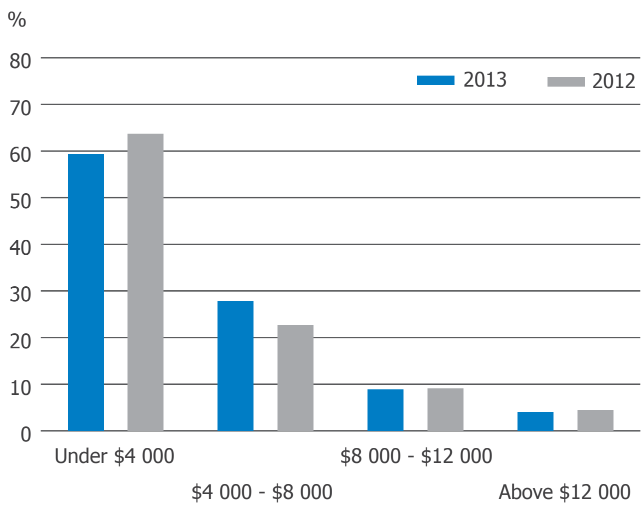
Source: Evans Property Services

63 ▶ Apartments Offered for Rent by Number of Rooms



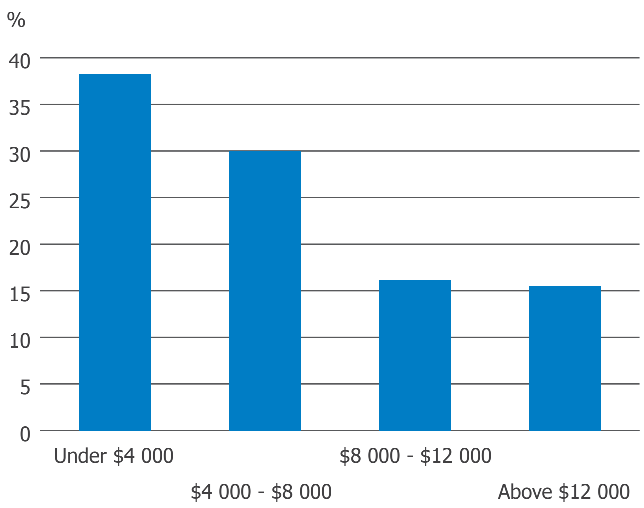
Source: Evans Property Services

64 ▶ Rental Requests by Budget



Source: Evans Property Services

65 ▶ Apartments Offered for Rent by Budget



Source: Evans Property Services

Hot Topic:

Investors anticipate the Russian real estate market to become one of the most attractive investment destinations in Europe in 2014.

By **Olga Arkhangelskaya**, Partner, Head of the Real Estate, Transportation, Infrastructure and Government & Public Sector in the CIS, EY

According to EY's annual Real Estate Assets Investment Trend Indicator Russia is among the most attractive European real estate investment markets in 2014. In particular an increased investment focus on residential property in Moscow and the Moscow region is anticipated by investors.

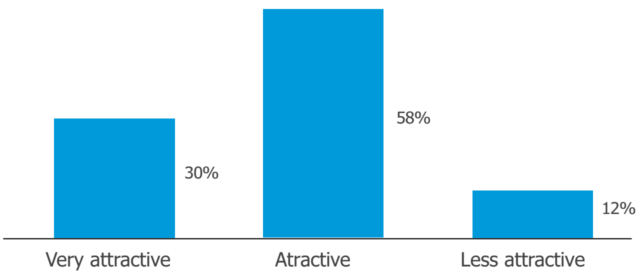
The trend indicator is based on a survey of 500 real estate investors from 15 European countries. For the Russian issue of the study, 33 companies that have been active in the Russian property market in recent years were surveyed. The vast majority of them (88%) view Russia as an attractive or very attractive location for real estate investments in 2014, and this positive trend has been maintained over the past couple of years. (66 ▶)

Compared with other European countries the trend has even further improved: 90% of the respondents rate Russia as an attractive or very attractive investment location in 2014. In last year's survey, 83% of the respondents shared this option. With regard to the 2014 European context, only participants from Germany, the UK, Austria, Turkey and Sweden rank their respective home markets higher. As a consequence of this optimistic outlook, the transaction volume in Russia is expected to rise with 73% of participants stating that it will exceed the level observed in 2013. (67 ▶)

In contrast to last year's results, residential real estate is anticipated to be very popular among investors in 2014. (68 ▶) 72% of the participants plan to invest in the Russian residential real estate, while in 2013 this share was only at 23%.

66 ▶ Russia's Attractiveness as a Location for Real Estate Investments

Original question:
"How do you rate Russia's overall attractiveness as a location for real estate investments in 2014?"



Source: EY

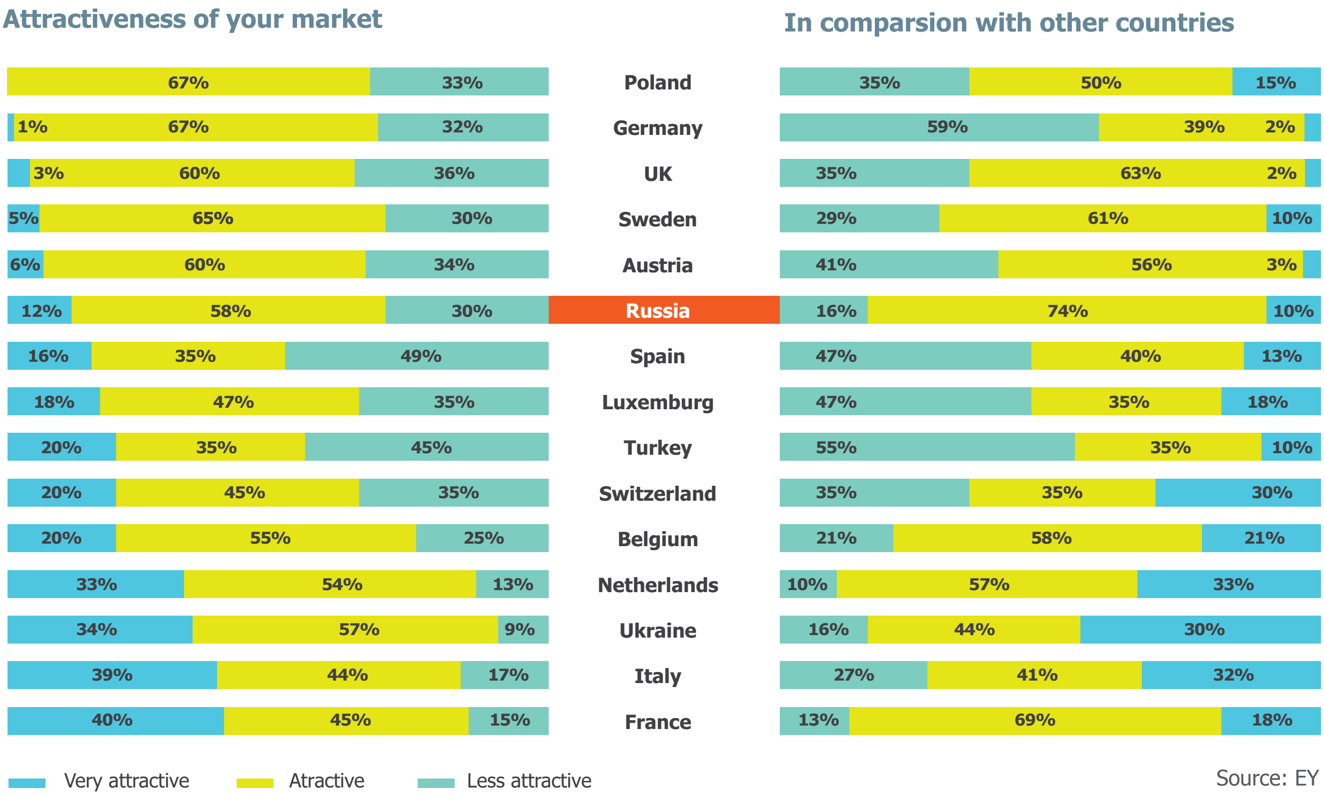
According to the survey, the strongest regional focus for residential investments will lie on Moscow. More than half of the participants (55%) plan to invest in Moscow prime locations. Also, other Moscow locations and the Moscow Region are attractive: 46% of the participants report plans to invest in residential real estate here.

With 77% of respondents agreeing that alternative debt providers with continue to become more important in 2014, a vast majority (85%) of participants also anticipate an increased number of portfolio deals in the commercial real estate sector. In 2014 investors are significantly more likely to adapt riskier strategies, such as value-add or opportunistic investments (79% agree against 50% in 2013). There is an anticipation for a rise in transaction volume in 2014 (73% agree), partly due to the expected increase in investment activity by international real estate investors (75% agree). Likewise, the average deal size on the Russian real estate market is predicted to increase with 76% of respondents agreeing.

67 ▶ Attractiveness of your market

Original question:

"How do you rate the countries' overall attractiveness as a location for real estate investments in 2014? / How do you rate the country's overall attractiveness as a location for real estate investments in 2014, compared with other locations in Europe?"



Source: EY

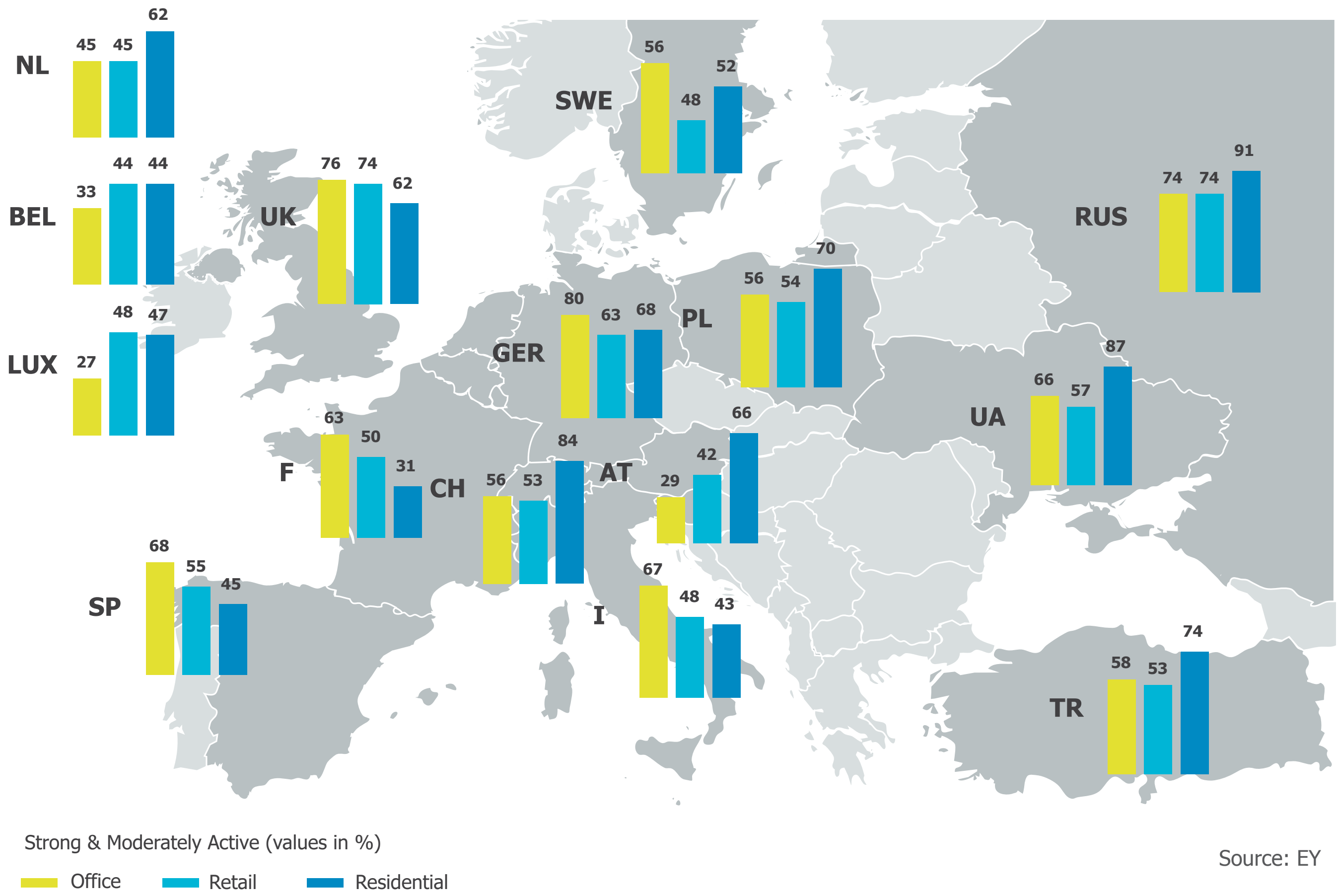
As far as the price expectation go, the prices for office buildings in prime locations are predominantly expected to remain stable (46% agree) or to increase (29%). However, the percentage of investors expecting these prices to increase has reduced, compared to the 50% in 2013. 75% of investors expect for office properties in secondary and peripheral locations to drop in price. For retail buildings in superior locations the prices are expected to increase by 40% of respondents and to remain stable by 33%. Retail property is peripheral areas are deemed attractive for investment by 50% of respondents, who anticipate an increase in price for such properties in 2014, while similar properties in secondary locations are most likely to drop in price, with 92% of respondents agreeing.

Overall the investment forecast for Russia on 2014 is optimistic, although the extent of this positive outlook will largely depends on the economic conditions and developments in the tax and legal framework.

68 ▶ Investment focus: residential properties

Original question:

"Compared with 2013, what level of focus do you intend to give to the following real estate use types in your investment strategy for 2014?"



Source: EY

Association of European Businesses

AEB REAL ESTATE COMMITTEE

The AEB Real Estate Committee was founded in 2003 and brings together real estate professionals from a variety of areas including developers, investors, financiers, consultants, project and facilities managers, and other service providers.

The Real Estate Committee has three primary objectives around which its activities are structured: to facilitate the exchange of information regarding real estate and development issues in Russia; to influence existing procedures in order to increase the attractiveness of foreign and domestic investment; and to establish a "bridge" between the AEB, the Moscow Government, State Duma and other relevant governmental bodies.

The Real Estate Committee is currently organised into 4 working groups: Finance and Investment, Industry Sub-sectors, Project Management & Ancillary Services and Office and Administration Managers. These working groups meet regularly to update on current developments in the real estate sector in Russia and regularly organise open and other events that are focused on topical subject matter and intended to fulfill the core objectives of the Committee.

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