

RESEARCH



H1 2015 WAREHOUSE MARKET REPORT

Moscow

HIGHLIGHTS

In H1 2015, the total area of new quality warehouse space has amounted to a record 570.1 thousand sq m.

The take-up of quality warehouse space in the Moscow region was 260.5 thousand sq m, which is 20% higher than the total volume of deals concluded in the same period previous year.

Asking rental rates during H1 2015 changed slightly and were around 3,800–4,600 rub/sq m/year for Class A properties.

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Key indicators. Dynamics*

	Class A	Class B
Total quality supply volume, thousand sq m	9,999.4	
including, thousand sq m	8,048.4	1,951
New delivery in H1 2015, thousand sq m	570.1	
Lease and sale transactions volume in H1 2015, thousand sq m	260.5	
Vacancy rate, %	10.4 ▲	
Asking rental rates**, rub/sq m/year	3,000–5,200 ▼	
Operational expenses, rub/sq m/year	1,000–1,300 ►	

* Compared to the end of Q4 2014

** Triple net – excluding VAT, operating expenses and utility bills

Source: Knight Frank Research, 2015

Supply

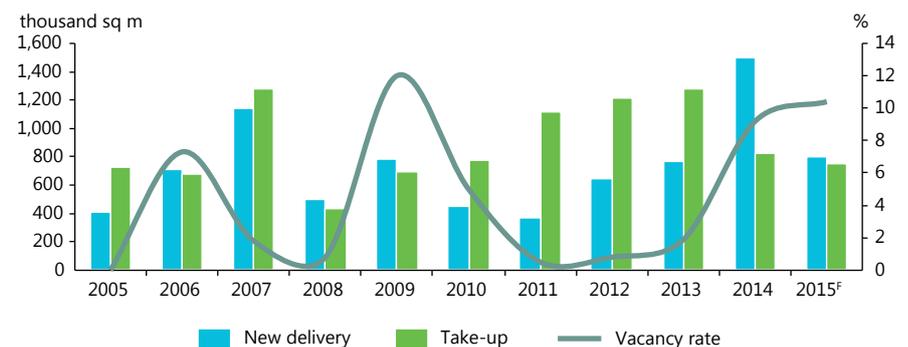
In H1 2015, about 570 thousand sq m of new quality warehouse space was added to the stock, which is a record high in the history of the market for quality warehouses. The large volume can be explained by the fact that delivery dates for a number of projects have been rescheduled from 2014.

It's worth mentioning that in the post-crisis period (between 2011 and 2013), the warehouse market has experienced an extremely low vacancy rate (0.5–1.9%), that

motivated developers for construction of new facilities; some volume was delivered only in late 2014 or early 2015. In H1 2015, the total area of warehouse space in the Moscow region has reached 9.9 million sq m.

We have been witnessing a slowdown in construction activity in 2015: with lack of debt financing and falling demand, developers are revising their plans for speculative projects and refocusing on built-to-suit facilities.

New delivery, take-up and vacancy rate dynamics



Source: Knight Frank Research, 2015



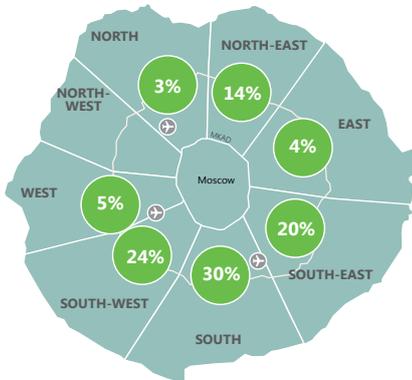
Viacheslav Kholopov

Partner, Director,
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"Despite the challenging economic environment, activity in the warehouse market remains high: companies are trying to take advantage of the market situation to get the best deals on rentals. However, we can expect a decrease in the vacancy rate in 2016, as well as rental rates correction.

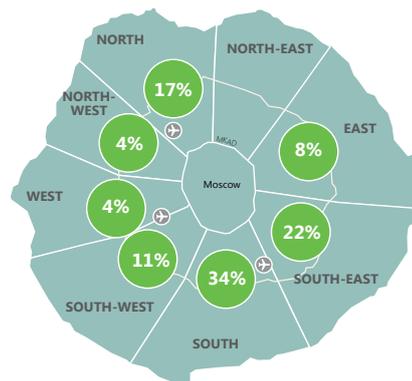
The current state of the economy makes warehouse development a low-margin business for the majority of the existing market players, so in 2015–2016 the market will be driven by a limited number of companies specialised in warehouse development. Potential supply reduction will not have any positive implications for tenants in the future: asking prices will rise, while the number of lease and purchase options will decline. At the same time, for companies planning development in terms of logistics a year before they move, a solution is already in place: most sites will continue to offer built-to-suit options".

Delivery of the new warehouse premises in Moscow in terms of direction



Source: Knight Frank Research, 2015

Take-up of warehouse premises in Moscow in terms of direction



Source: Knight Frank Research, 2015

Lease and purchase transactions volume in the regional cities of Russia



Source: Knight Frank Research, 2015

According to our estimates, about 70% of the total new warehouse space planned for 2015 was delivered in the first six months of the year.

Southern part of Moscow region is currently experiencing high development activity, a trend that has continued in H1 2015: South, South-East and South-West accounted for over 70% of the delivery in the first six months of 2015. It's worth highlighting that almost all of them were new phases of existing warehouse complexes.

With a large number of new warehouses delivered and the demand declining, the vacancy rate rose by 1.2 p. p. in H1 2015 to 10.4%. This figure comprises both new warehouses and freed up space. Also, some companies offer subleases of unoccupied space in order to cut costs.

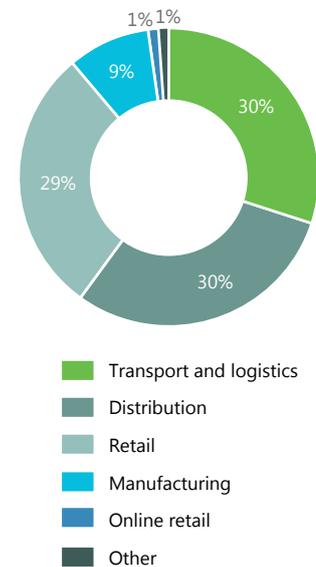
Demand

In H1 2015, lease transactions and purchases of quality warehouse property in Russia totalled around 410 thousand sq m, which represents a 20% decrease from the first six months of 2014 and is almost half the record high seen in H1 2013. It's worth mentioning that while the number of transactions decreased, businesses showed continued interest in warehouse space offered for rent in the Moscow region. However, this demand may transfer into deals only in H2 2015 since the negotiation period now lasts longer. It's also worth saying that there have been no major deals closed on the sale market in 2015: a number of transactions are now going through the bargaining stage and will be completed by the end of 2015. And still, this year the sales volume will be far from the 2013 or 2014 levels.

The current economic context has provided some important changes in inquiries from tenants in H1 2015. Commercial terms have become one of the key factors when choosing a warehouse space for rent, property location and class less important. Also, with production shrinking and consumption and freight going down, some of the lease transactions were represented by tenants moving from one warehouse complex to another in search of better lease terms. Some of them have reduced the warehouse area leased.

If we look at the geographical distribution of transactions, we'll see that the Moscow region accounted for about 63% of the total number of deals across the country; St. Petersburg and other large cities, 18% and 19%, respectively. For the first time since 2012, the share of the cities other than Moscow and St. Petersburg in warehouse take-up has decreased.

Take-up of warehouse premises in Moscow in terms of company profile



Source: Knight Frank Research, 2015

Given the general distribution of newly built warehouses across the Moscow region, it's not surprising that about 70% of quality warehouse take-up was in its southern part.

The average transaction size in the Moscow region changed only slightly: 9.5 thousand sq m in H1 2015 versus 9.9 thousand sq m in the same period of 2014. About 65% of the total number of deals involved warehouse space of less than 10 thousand sq m, which is also comparable to H1 2014 levels.

In the first six months of 2015, retail businesses and distributors made up around 60% of the total number of lease transactions. About 30% was represented by transport and logistics companies; the number of deals with them increased from 2013 and 2014 but failed to reach 50%, as it happened in Q1 2015. The share of manufacturing companies and online retailers shrank to 9% and 1%, respectively. It's worth mentioning that a significant share of retailers can be explained by a high level of activity seen among DIY stores and grocery chains, the retail sectors that feel the most secure in their positions in the current environment and announce expansion plans in Russia.

Commercial terms

Ruble-denominated asking rental rates dropped by about 10–15% in the past 12 months. Today, asking rates range 3,800–4,600 rub/sq m/year for Class A warehouses

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and 2,800–3,500 rub/sq m/year for Class B facilities (triple net: excluding VAT, operating expenses and utility bills). The largest drop in rates for quality warehouse space was seen between October 2014 and March 2015, when economic uncertainty and high vacancy rates forced many landlords to revise their commercial terms. Also by the end of H1 2015, a number of offers appeared with rates much lower than the market average, indicating that price competition was rather intense and some developers were ready to offer tenants major concessions to avoid having vacant space.

Most lease contracts are signed for a short period of time (three to five years) and have rates denominated in rubles. While there are still some offers fixed in foreign currencies, we believe that in the next 1–2 years most lease rates will be denominated in rubles.

Land market

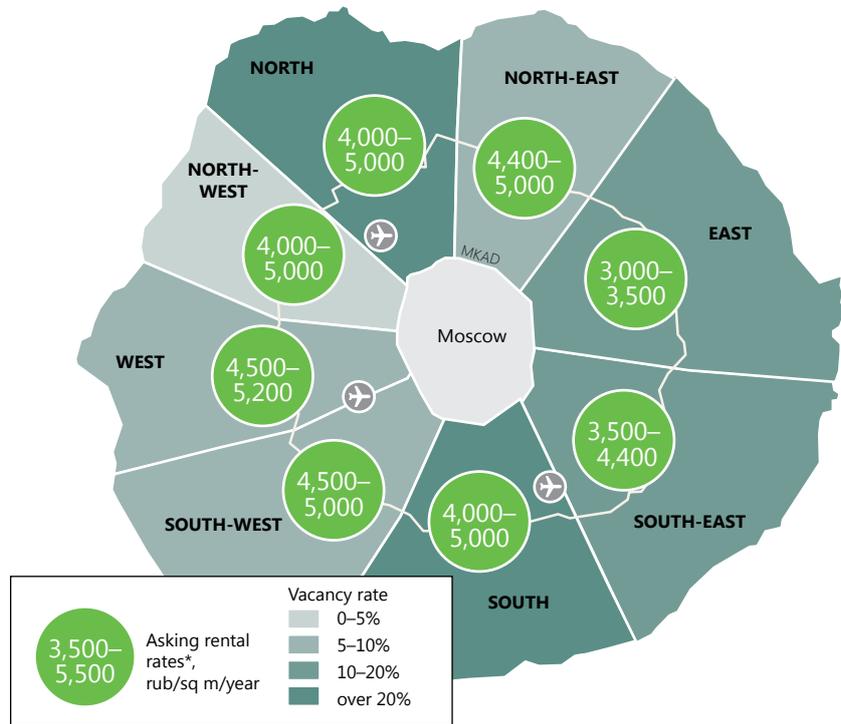
The overall downturn in the commercial real estate market affected the land market. A large number of companies have changed their plans to buy land, while others suspended the bargaining process. However, some market players are still looking at available offers. The stronger interest is shown for the southern and northern parts of the Moscow region. Another sought-after area is the west (Minskoye, Mozhayskoye and Novorizhskoye Highways), but the number of offers here is very limited. We have recently started getting more inquiries about land lots in the East, mostly for warehouse development and industrial projects.

If we look at the distribution of interest by distance from the Moscow Ring Road, we'll see that the most attractive locations are at 10–15 km from the city; however, more distant locations are becoming increasingly popular as well.

The number of players willing to buy land for residential development has plunged since the limited access to debt financing has forced small and medium-sized businesses to cancel expansion plans; the bulk of demand is represented by 10–15 large developers.

The Russian land market, which has always had prices denominated in foreign currencies, has partially switched to rubles due to high exchange rate volatility and economic uncertainty. Today the market is very diverse: some players (who typically own one or two assets) are offering overpriced land, while others have good deals with discounts for both commercial and housing development.

Vacant space and asking rental rates in terms of location



Source: Knight Frank Research, 2015

Average asking rental rates* dynamics for warehouse premises denominated in RUB



Source: Knight Frank Research, 2015

Average asking rental rates* dynamics for warehouse premises denominated in USD



* Triple net – excluding VAT, operating expenses and utility bills

Source: Knight Frank Research, 2015

Forecast

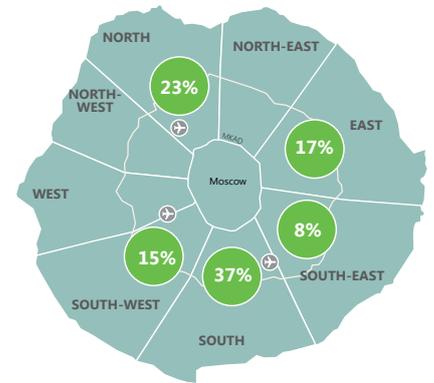
We expect the total area of quality warehouse space delivered in 2015 not to exceed 800 thousand sq m, which is half the record high seen in 2014.

Analysis of activity in the Moscow warehouse market shows that take-up may reach 700 thousand to 800 thousand sq m by the end of the year, which is comparable to last year's levels (or even higher). Availability of good deals will enable more options for tenants whose contracts have expired. The bulk of the deals will again be made up by retailers (mostly grocery chains and DIY stores).

With the delivery of new warehouse space declining and tenant activity remaining the same level, we can expect the vacancy rate to fall to 9% by the end of 2015. In our opinion, rental rates will be kept unchanged.

In 2016, if the economic situation improves and the sanctions are lifted, demand for quality warehouses may rise. Together with small supply of new speculative developments, this may lead to a significant reduction in the vacancy rate and an increase in rents. It is worth mentioning that a similar situation was observed during the previous crisis, when during 2009–2011, the vacancy rate fell by 11 p. p., to below 1%.

Warehouse space under construction in terms of location



Source: Knight Frank Research, 2015



PNK-Severnoe Sheremetyevo, Moscow region, Rogachevskoye hwy, 27 km from MKAD



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