Q3 2010
OFFICE REAL ESTATE MARKET
Moscow
Knight Frank

EXECUTIVE SUMMARY

- The total volume of quality office space is still increasing at slow rates, new projects are almost not announced, however there is a number of properties under construction are on the market.

- The demand for quality office space shows a positive trend for already a year. Class A office space takes a major share in the take-up (looms large) structure (about 80%), as are premises located within or close to the Garden Ring.

- Rental rates stabilized at the level achieved in the past quarter and there’s no sense for their decrease.
OFFICE REAL ESTATE MARKET

Key indicators

<table>
<thead>
<tr>
<th>Class A Premium**</th>
<th>Class A</th>
<th>Class B+</th>
<th>Class B-</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total volume of quality premises, million sq m</td>
<td>10.9</td>
<td>1.9</td>
<td>6.0</td>
</tr>
<tr>
<td>Including, million sq m</td>
<td>10.9</td>
<td>1.9</td>
<td>6.0</td>
</tr>
<tr>
<td>Commissioned in Q3 2010, thousand sq m</td>
<td>182</td>
<td>134</td>
<td>48</td>
</tr>
<tr>
<td>Including, thousand sq m</td>
<td>182</td>
<td>134</td>
<td>48</td>
</tr>
<tr>
<td>Vacancy rate, %</td>
<td>15.1</td>
<td>17.7</td>
<td>20.9</td>
</tr>
<tr>
<td>Base rental rate*, $ per sq m per annum</td>
<td>780-1,000</td>
<td>500-750</td>
<td>300-550</td>
</tr>
<tr>
<td>OPEX, $ per sq m per annum</td>
<td>90-200</td>
<td>80-100</td>
<td>50-80</td>
</tr>
</tbody>
</table>

* Excluding operating expenses and VAT (18%)
** Range of asking rents and sale prices for premises with premium locations

Source: Knight Frank Research, 2010

“Supply

About 182,000 sq m of quality office space were commissioned during the last 3 months, and the increase in office space for this year is being maintained on a low level – about 2% for the quarter. Since March 2010 no one Class A business center was commissioned, however many projects in this segment are currently under construction, and some of them are close to completion. This situation may be caused by the higher construction costs for Class A office space.

Only projects that have been at the higher stage of development before the crisis are now delivered to the market. The political situation in Moscow is also not so favorable for starting new projects. Its influence on the commercial real estate sector is not so significant, however, the processes of distributing land plots for construction, project documentation accommodation, possible government investment support, and commissioning all depend on political force. Changes in the political situation in Moscow, including the assignment of new officials in charge of the above-noted questions, might unpredictably influence on the terms of receiving agreements and of development for a series of projects.

By the end of the year an increase in quality office space slightly more than 300,000 sq m is expected, the most part comes from Class A. Such projects as “Vivaldi Plaza”, “Summit”, “Diamond Hall”, “Marr Plaza”, “Imperia Tower”, “Legenda Tsvetnogo”, “Impersky Dom”, and the business center on Shepkina St, 61-2, are all preparing...”

Key projects commissioned in Q3 2010

<table>
<thead>
<tr>
<th>Property Name</th>
<th>Location</th>
<th>Total area, sq m</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Class B+</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nagatino i-Land*</td>
<td>Bld 1-3, 18 Andropova Ave</td>
<td>37,387</td>
</tr>
<tr>
<td>Bld 1-1-B, 18 Andropova Ave</td>
<td>23,440</td>
<td></td>
</tr>
<tr>
<td>Bld 1-1-V, 18 Andropova Ave</td>
<td>22,070</td>
<td></td>
</tr>
<tr>
<td>Mirax Plaza, Bld D</td>
<td>36 Kutuzovskiy Ave</td>
<td>31,120</td>
</tr>
<tr>
<td>AFI on Paveletskaia*</td>
<td>Bld 1, 8 Paveletskaia Emb</td>
<td>17,000</td>
</tr>
<tr>
<td><strong>Class B-</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>East Gate</td>
<td>Bld 7-20, 100 Shelkovskoe Hwy</td>
<td>12,500</td>
</tr>
<tr>
<td>BC Perovo</td>
<td>Bld 1-9, 9 1st Perova Polya Passage</td>
<td>19,500</td>
</tr>
</tbody>
</table>

* Knight Frank is a consultant on the project
Source: Knight Frank Research, 2010

“The third quarter was a crossover period for the office market: For the first time since the beginning of the crisis, the size of absorption surpassed the volume of commissioned space, according to the quarter’s results. This situation is caused with the increase in the volume of deals on the one hand – Q3 results surpassed Q2 results twofold. And on the other hand the increase of supply remains on the low levels.

At the same time, rental rates have not changed compared with May. A significant increase in rates occurred in spring, facilitated by the developers’ anticipations of the growth in demand but in fact before the actual increase. Thus, the growth in market activity, that landlords counted on in spring, showed itself in Q3 and balanced the spring growth in rental rates.”

Mikhail Ioannesyants
Deputy Director,
Office Real Estate Department

“...”

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to enter the market. The situation, when the majority of the office area was leased before the official commissioning of the project, was usual on the pre-crisis market. Moreover, these projects are already almost halfway filled even now, when there’s a comparatively low demand for office space under construction.

**Demand**

Due to the economic recovery observed in the beginning of the year, a growing demand for quality office space is mentioned: for the past three months the volume of take up was about 385,000 sq m, which is 10% more than the volume of absorption for the entire H1, and for already a year the level of take-up shows a positive dynamics.

Moreover, in Q2 the level of demand increased by 20% compared to Q1, and for the last 3 months it increased twofold compared with the past quarter. As in the past quarter, the share of Class A office space in the total structure of absorption was about 80%, while before the crisis tenants and buyers distributed their interests for Class A and Class B offices approximately in equal proportions. Moreover, in the end of 2008 the share of Class A space was at a level of 12% and over following 2 years it roused to a level of 20-50%. The fact that for already 6 months 80% of leased and purchased space is in Class A segment confirms the activation of deferred demand and the migration of tenants to the higher quality offices.

As the result of this the vacancy rate for Class A premises decreased to 15%, that is a significant reduction, but that is still far from the level reached in 2008. For Class B the vacancy rate reduces slowly, though this process is caused more by the low volumes of delivery, than by a significant growth of demand.

For the first time for two years the volume of take-up surpassed the volume of delivery of new space, yet it is still too early to talk about significant growth on the market. The main volume of take-up is filled by postponed unsatisfied deferred demand from tenants. In addition, 40% of the total volume of transactions for Q3 was comprised by two large freehold deals of office premises: the purchase of “Western Gate” business park, and the acquisition of “Domnikov” business center, by RZD. Such big-sized deals are single on the market, nevertheless, even without their consideration,
the level of take-up shows a stable positive dynamics. According to the general positive trends, there is no prerequisites for a decrease in demand and a traditional pre-New Year buoyancy of the office real estate market is expected by the end of the year.

A decrease in the share of renegotiation deals continues: the majority of tenants have already completed this process; moreover, commercial terms renegotiation is becoming more and more difficult on gaining market.

Commercial terms

An increase in business activity and positive expectations of market players facilitated a significant growth of rental rates for H1 2010. For the past quarter, rates stabilized at the previously achieved level, which provides a good background for their growth considering the market activation forecasted by the end of the year.

The market process of “chain reaction”, when rental rates increase together with increased demand, is especially characteristic for developing markets. In Moscow a phase of stabilizing rates on a new level is found right now, which was a result of gradually growing demand, on the one hand, the summer season of clients’ activity decreasing on the other hand.

The share of deals with office space within the Garden Ring insignificantly increased for 5% compared to the previous quarter and about 45% of Class A and Class B of leased and purchased office space is located in the center of the capital. The share of the central areas in the total volume of deals was slightly more than 30% last year, which might mean the end of the trend towards a decentralization of demand on the Moscow office market, which started to form in 2008. This is one of the reasons that properties with premium locations, which are acting as drivers of growth, sustain the highest rental rates.

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The share of leasehold and freehold deals for new office space has been gradually returning to the level of the beginning of 2008

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**Key deals in Q3 2010**

<table>
<thead>
<tr>
<th>Company</th>
<th>Volume of transaction, sq m</th>
<th>Address</th>
<th>Property Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lease</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>MosCommerceBank</td>
<td>5,570</td>
<td>Bld 1, 3 Begovaya St</td>
<td>NordStar Tower</td>
</tr>
<tr>
<td>Otkritie</td>
<td>5,550</td>
<td>12/1 Yakovoapostolsky Lane</td>
<td>Yakovoapostolsky Business Centre</td>
</tr>
<tr>
<td>Eldorado</td>
<td>5,270</td>
<td>14 Smolnaya St</td>
<td>Smolny Business Centre</td>
</tr>
<tr>
<td>Nycomed</td>
<td>4,750</td>
<td>Bld 1, 2 Usacheva St</td>
<td>Fusion Park</td>
</tr>
<tr>
<td>Mocrohen*</td>
<td>3,890</td>
<td>10 2d Volkonsky Lane</td>
<td>Volkonsky Business Centre</td>
</tr>
<tr>
<td>NTK</td>
<td>2,800</td>
<td>19 Leniniskaya Sloboda St</td>
<td>Omega Plaza</td>
</tr>
<tr>
<td>Transneft</td>
<td>2,530</td>
<td>69 Pyatnitskaya St</td>
<td>Pyatnitskaya Plaza</td>
</tr>
<tr>
<td>Russkiy Produkt*</td>
<td>2,380</td>
<td>21 1st Tverskaya-Yamskaya St</td>
<td>Chetire Vetra</td>
</tr>
<tr>
<td>Progress</td>
<td>2,150</td>
<td>21 Goncharnaya St, / Bld 1, 14</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>V. Radischevskaya St</td>
<td></td>
</tr>
<tr>
<td>Dibold Self Service</td>
<td>1,800</td>
<td>14 Dvintsev St</td>
<td>Dvintsev Business Centre, Bld C</td>
</tr>
<tr>
<td>InterLabService</td>
<td>1,600</td>
<td>Bld 1, 8 Olsufievsky Lane</td>
<td></td>
</tr>
<tr>
<td>Bio-Rad Laboratories</td>
<td>1,530</td>
<td>Bld 1, 9 Novodanilovskaya Emb</td>
<td>Danilovskaya Manufacture</td>
</tr>
<tr>
<td>Russian Caramel</td>
<td>1,420</td>
<td>Bld 2, Leningradskoe Hwy</td>
<td>Metropolis</td>
</tr>
<tr>
<td>Restaurants LLC</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Amgen</td>
<td>1,350</td>
<td>8 Presnenskaya Emb</td>
<td>Capital City</td>
</tr>
<tr>
<td>Purchase</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>RWM Capital</td>
<td>84,550</td>
<td>34 Mashi Porivaevoy St</td>
<td>Domnikov BC</td>
</tr>
<tr>
<td>confidential</td>
<td>60,407</td>
<td>21 Belovezhskaya St</td>
<td>Western Gate</td>
</tr>
<tr>
<td>May</td>
<td>6,000</td>
<td>7 Dmitriya Ulianova St</td>
<td></td>
</tr>
</tbody>
</table>

* Knight Frank is a consultant of the deal

Source: Knight Frank Research, 2010
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