RESEARCH

Knight Frank

HI 2013

INVESTMENT MARKET

Moscow

HIGHLIGHTS

- The total investment transactions volume in the first half of 2013 amounted to approximately $ 3.4 bln, which is only slightly (5%) more than the figure for the same period last year.
- The largest share in the total investment transactions volume fell with the segment of commercial real estate (almost 50%). Transactions with office facilities amounted to approximately 30%. Favorable situation on the warehouse market boosts investor interest in this segment, however, its share for the moment is in the range of 5%.
- Since the beginning of 2013, there have been no significant changes to the capitalization rates, which remain high as compared with the more developed European markets. We do not expect their significant reduction in their near future.

INVESTMENT MARKET

The main parameters of commercial real estate segments in the 1st half of 2013. Dynamics*

Segment	Offices		Shopping Centres	Warehouses		Hotels cat. 3 - 5★
Object Class	A	B		A	B	
New delivery, thousand sq m Change, %	96.3 +3.8** ▲	244.7 +2.4 ▲	231 / 147*** (+3.3%) / (+3.9%) ▲	260 +3.5 ▲	–	570 +1.8 ▲
Vacancy rate, % Change, ppt	14.7 +2.1 ▲	12.8 -1.7 ▼	3.0 =	1.0 +0.2 ▲	2.0 =	60% ▼
Rates, $/sq m/year Change, %	830 -0.5 ▼	490 +1.4 ▲	700 - 4000 =	135 - 145 +3.0 ▲	115 - 120 +3.0 ▲	178 =
Yield , % Change, ppt	8.5 - 10.0 +1.0 ▲	10.5 - 11.5 +0.5 ▲	9.0 - 10.0 =	11.0 - 11.5 =	12.0 - 13.0 =	–
Average selling price, $/sq m	6,000 - 8,000	4,000 - 6,000	3,500 - 7,500	1,250 - 1,400	600 - 800	200 - 1,000

* Compared to the end of 2012.
** The total volume of Class A space for the first half of the year has been recalculated in accordance with the new version of commercial real estate classification adopted in 2013.
*** The total area of the building / total leasable area
For hotels the respective rows show: number of new rooms; room occupancy (%); average daily rate ($ per room per day); and average selling price per room (thousand $ per room)
Source: Knight Frank Research, 2013

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«The first half of 2013 was characterized by a relatively high activity on the real estate investment market, and our expectations for 2013 are optimistic. The total investment volume for the year can reach $7 bln, but due to the introduction of new high-quality assets, an even higher figure is possible.

Project financing is still available, but is limited. Although no new players appear on the market, the largest Russian representatives of private capital exhibit a growing interest in investing not only in commercial and office buildings, but also in the warehouse properties. In this case, there is a shortage of high-quality investment-attractive assets».

Supply and demand

Investment activity on the real estate market was quite high in the first half of 2013. Compared to the same period last year, the volume of investment transactions has slightly increased (by about 5%). However, the real estate investment market in Russia still remains rather closed, it is difficult to compare figures this narrow in value: an average amount of investment transaction is approximately $120 - 130 million, that is, actually the difference of indicators can be explained by a single transaction.

Total volume of investment transactions on the real estate market in the first half of the year amounted to about $ 3.4 bln.

The investors are traditionally focusing on premium-quality office and retail properties in Moscow, however, a major acquisition of a shopping center in Novosibirsk has changed the customary geographical distribution of investments: if earlier the share of transactions with regional projects did not exceed 5%, by the end of the first half of 2013, it amounted to about 27%.

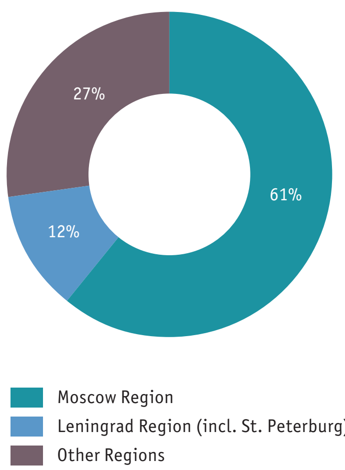
Almost half of the total investment transactions volume fell with retail properties. In particular, such transactions were closed as the purchase of 50% of the project Metropolis by Hines CaIPERS Russia Long Term Hold Fund and the acquisition of SEC Aura (Novosibirsk). It is worth noting, that vacancy rate on the real estate market of Moscow remains low as the trade operators are active — about 3%. The rental rates in the first half of 2013 did not change significantly. No substantial growth of high-quality shopping centers supply stock is expected in 2013. However, new formats (such as outlet centers, eco-markets) are going through a rather active development phase, unusual concepts of shopping centers are being considered.

A transaction of sale & lease back kind (a transaction where the property owner sells it to an investor and then makes a long-term lease of this property) was closed in the segment of the retail real estate in the first half of 2013. Such deals are common in USA, Canada and some European countries, but in Russia there are still only singular cases. Such arrangement is suitable for large-scale retail operators who prefer stand-alone format hypermarkets. On the one hand, it enables them to construct or adapt the building to their needs, on the other — releases a significant amount of funds for the development of their own business. Such transactions are mainly observed in the segment of retail and warehouse real estate, and a stable market is an important external condition for their success.

No significant changes occurred on the office market during the first half of 2013. The new construction volume is rising, and with it — the quality of the constructed office centers: developers are paying attention to advancement of related infrastructure, environmental friendliness and energetic efficiency of the facilities. Presently, the demand is rather limited due to the uncertainty of both the Russian and the global economies. The rental rates for Class A and B office centers over the past six months have not changed. Relative transparency and stability of cash flows and the high-quality pool of tenants for office buildings continue to attract investors: about a third of the total volume of investment transactions closed in the first 6 months of 2013 falls with office real estate. Among the major transactions worth noting are the repurchase of the 50% partner's share in the project Aquamarine III by AFI Development, the acquisition of business center Four Winds by the Millhouse Capital agencies and the sale of the business center Hermitage Plaza.

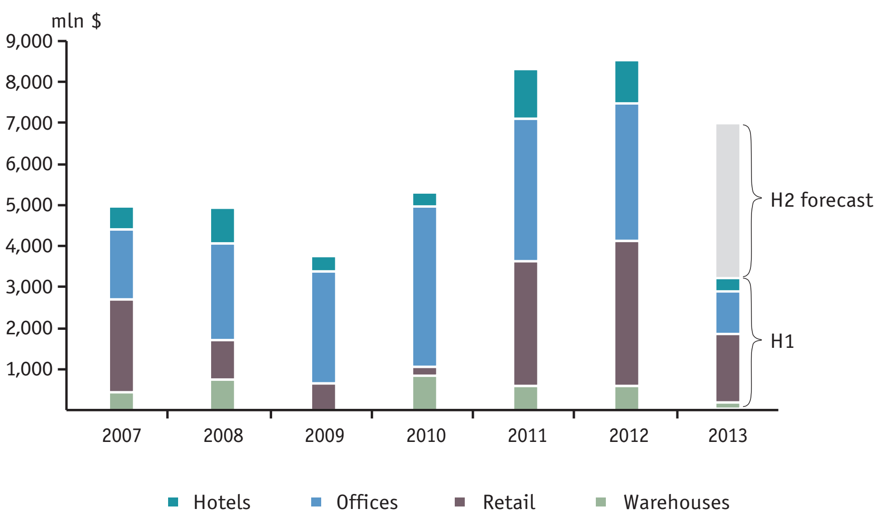
Investors grow more interested in the warehouse segment against the background of a stable situation on the traditionally attractive commercial and retail real estate markets. The record-high take-up, ready-to-move-in facilities deficit, improvement in construction quality, as well as a steady growth in rental rates are making warehouse facilities an increasingly more attractive investment option. A number of investment transactions was closed in the first half of 2013: the acquisition of Tinkoff factory by the A + Development Company, the purchase of a warehouse facility in Tomilino by the Bin Group, as well as the acquisition of a storage building in the complex PNK-Chekhov by the RB Invest Company. The total amount of investment transactions in the warehouse segment amounted to approximately $210 million (about 6% of the total volume of investment transactions closed in January-June 2013). It is also worth noting that the transfer of assets of Eurasia Logistics Company (warehouse complex Tolmachevo in Novosibirsk, Biek Tau in Kazan, Pyshma in Yekaterinburg) in the structure IQ Property Management, controlled by the BIN

The share of investment transactions in the Moscow region is still high



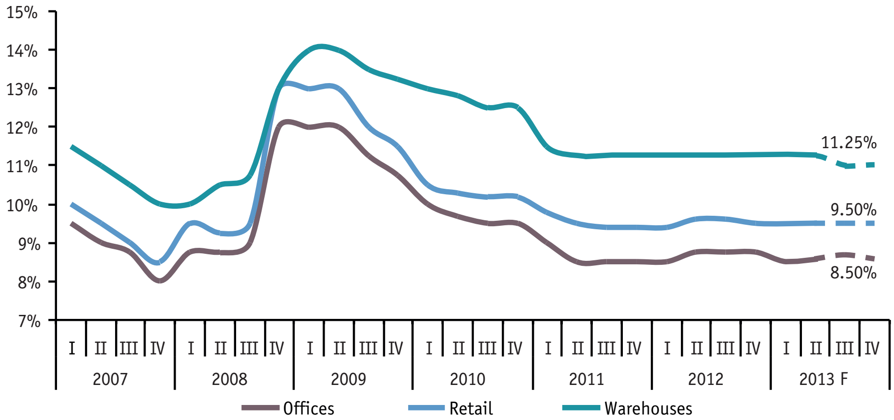
Source: Knight Frank Research, 2013

Traditionally, office and retail properties interest investors the most

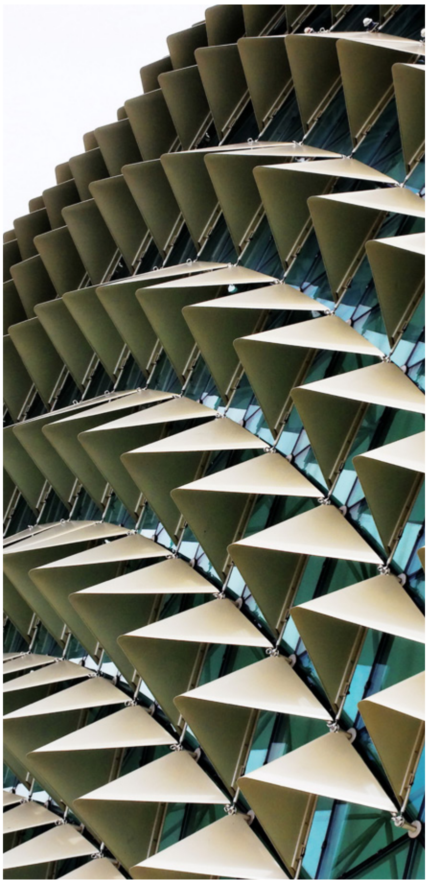


Source: Knight Frank Research, 2013

Dynamics of capitalization rates by segments of commercial real estate



Source: Knight Frank Research, 2013



Group, completed in the first half of the year. The total value of these assets, according to our estimates, could reach $800 million.

For the past two years, the main indicators on the Moscow commercial real estate market are not subject to major changes: the new supply and demand volumes remain at comparable level, the rental rates remain virtually unchanged. The average yield remains at mid-2011 level. We believe that persistence of a stable situation on the occupier market will result in a slight downward pressure on capitalization rates, which will be adjusted by no more than 1%.

The commercial real estate investment market is dominated by Russian investors, but due to a few large transactions with foreign funds, the share of foreign capital in the first half of 2013 accounted for about 25% of the total transactions. At the same time, the participation of foreign investors in the Russian real estate market is still fragmented: there appear practically no new players. The capitalization rates on the Moscow commercial real estate market remain attractive comparing to most of the European markets, however, high risks, lack of the market transparency and the taxation aspects of "expensive" financing, limit emergence of new foreign players.

The major investment purchase and sale transactions of commercial real estate in the first half of 2013

Buyer	Seller	Assets	Transaction value (estimation)
RosEuroDevelopment	Ronesans Holding	SEC Aura Novosibirsk	$784 mln
CalPERS JV Hines	Morgan Stanley (MSREF)	TC Metropolis Moscow	$600 mln
Millhouse Capital	AFI Development JV Snegiri Development	BC Four Winds Plaza Moscow	$370 mln
–	CJSC Forum Properties	BC Hermitage Plaza Moscow	$240 mln
AFI Development	Super Passion Limited	BC Aquamarine III* Moscow	$230 mln
Azimut Hotels chain owner	JSC Magnitogorskiy metallurgic factory	Renaissance Moscow Hotel Moscow	$170 mln
Orient Express Hotels	–	Grand Hotel Europe St. Petersburg	$135 mln
BIN GC	–	Tomilino warehouse complex Moscow	$100 mln

* A share in the project

Source: Knight Frank Research based on open sources information, 2013

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Established in London more than a century ago, Knight Frank is the renowned leader of the international real estate market. Together with Newmark Company, Knight Frank's strategic partner, the company encompasses 370 offices in 48 countries across six continents.

Knight Frank has been a symbol of professionalism for tens of thousands of clients all over the world for 117 years. After 17 years, Knight Frank has become the leading company in the commercial, warehouse, retail and residential real estate segments of the Russian real estate market. More than 500 large Russian and international companies in Russia have already made use of the company's services.

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