



H1 2017 WAREHOUSE MARKET REPORT

Moscow

HIGHLIGHTS

The total warehouse stock delivered in H1 2017 fell by one half to 135,500 sq m year on year.

The Q2 vacancy rate came up to 11.7% – about 1.5 million sq m in absolute terms.

H1 2017 showed a 10-percent increase over the transaction volume recorded at the same period last year reaching 608,300 sq m. Retail operators were responsible for about 40% of the total amount.

The Class A average asking rental rate was 3,700 rub./sq m/year, down by 7.5% in 12 months.



Maxim Zagoruiko
Director,
Industrial, Warehouses and Land,
Knight Frank, Russia and CIS

"The warehouse real estate market demonstrates timid signs of demand recovery. Stagnation of the economy in Russia is perceived more likely in a positive way and encourages many market players to turn up the heat to cover their warehouse requirements resulting in the slow vacancy rate reduction. If this trend continues, rental rates in liquid warehouses with the most advantageous location near the Moscow Ring Road may slightly increase by the end of the year. Moreover, the stepped-up number of transactions for the acquisition of warehouse space by end users is an indicative trend for the market. In general, the number of lease and purchase requests has significantly exceeded the figures for the same period last year and, according to our projections, the market will stay at the level of previous years in 2017 in terms of the transaction volume – 1 million sq m. Many developers, seeing increased activity from potential consumers, began to actively restart their projects. For example, Terminal Borisovsky, Logistics Partner, PNK Group, Logopark Development and Infraströy Bykovo have begun the construction of speculative objects".

WAREHOUSE MARKET REPORT MOSCOW

Key indicators. Dynamics*

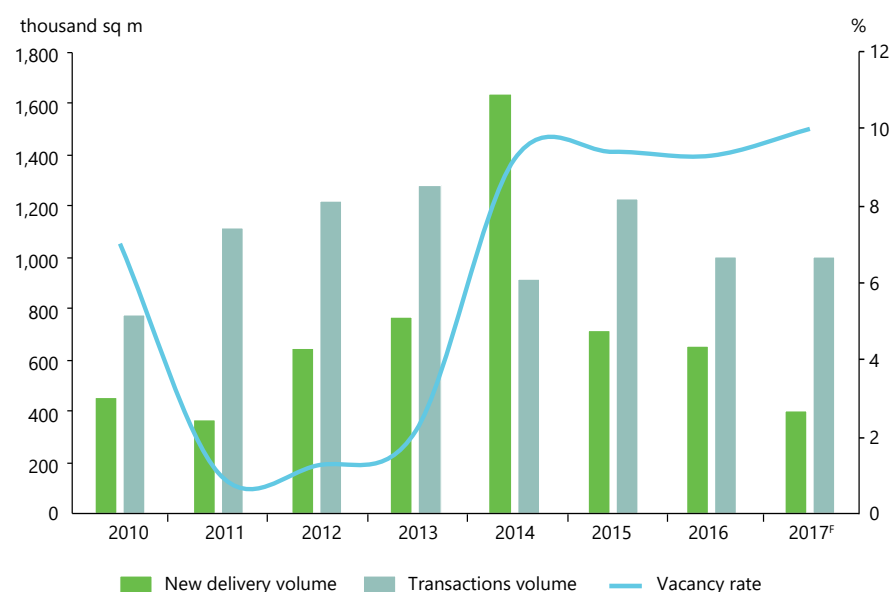
	Class A	Class B
Total quality supply volume, thousand sq m		12,801
including, thousand sq m	10,850	1,951
New delivery in H1 2017, thousand sq m		135.5
Lease and purchase transactions volume in H1 2017, thousand sq m		608.3
Vacancy rate, %		11.7 ▲
Asking rental rates**, rub./sq m/year	3,000–4,500 ▼	2,000–3,500 ▼
Operational expenses, rub./sq m/year	1,000–1,200 ►	700–900 ►

* Compared to Q4 2016

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

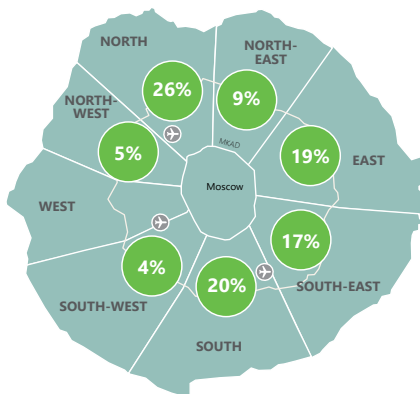
Source: Knight Frank Research, 2017

Dynamics of growth of quality warehouse space, the volume of lease and purchase transactions and the vacancy rate in the Moscow region



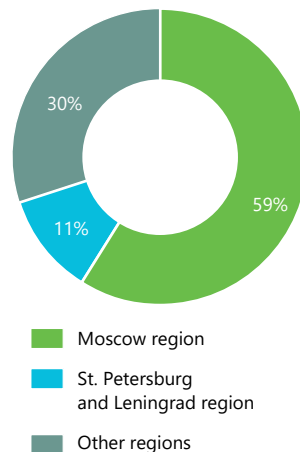
Source: Knight Frank Research, 2017

Breakdown of lease and purchase transactions of warehouse space by directions of the Moscow region



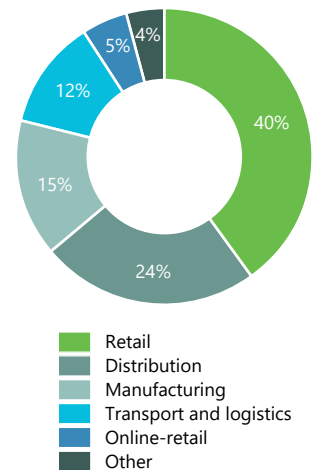
Source: Knight Frank Research, 2017

Breakdown of lease and purchase transactions of warehouse space depending on the region



Source: Knight Frank Research, 2017

Breakdown of lease and purchase transactions of warehouse space in the Moscow region by tenant profile



Source: Knight Frank Research, 2017

Supply

The 2015 trend was extended in H1 2017 when the new construction volume in the Moscow region had been reduced. Only 135,500 sq m were put into operation, which was almost two times less against H1 2016 (245,000 sq m). The total quality warehouse stock got to 12.8 million sq m in the Moscow region in H1.

The total delivery volume of new quality warehouse facilities in the Moscow region is expected to run up to 400,000–450,000 sq m by the end of the year.

The bulk of quality warehouse space (about 60%) commissioned in 6 months has been located in the north of the Moscow region. The remaining facilities have been in the east and south-west of the Moscow region.

Developers do not risk building speculative properties given the current general economic situation in the country and also taking into account the current warehouse market environment. Therefore, only one project of that kind was put into operation in the first half of 2017. The remaining warehouse premises were constructed according to the built-to-suit scheme.

Class A facilities have been still the most liquid on the market; therefore all the com-

plexes delivered in the first six months of 2017 belonged to Class A warehouses.

The Q2 vacancy rate eased insignificantly to 11.7% (by 0.3 p. p.) from Q1 2017. The vacancy rate for the first half of 2017 was 2.4 p. p. higher than the similar index for 2016 due to a significant jump of vacant space in the market of quality warehouse real estate of the Moscow region, which occurred in early 2017.

Demand

608,300 sq m of quality warehouse space were purchased and leased on the Russian market according to H1 results, which was 10% higher against last year's figure. The share of the Moscow region shrank by 16 p. p. – up to 58% of the total volume of transactions in Russia (356,000 sq m in absolute terms). The drawdown of the Moscow region share can be explained by the growth in the volume of transactions in other regions of Russia amounting to 184,000 sq m in H1 2017 (30% of the total volume of transactions).

In the first half of 2017, the downward trend of the share of retail operators in the total volume of transactions continued and now it is 40%. At the same time, they are still holding a leading position among tenants

and buyers of warehouse space. The decline of this index was primarily due to the share gains of distribution companies and a small increase in the share of manufacturing companies.

The average transaction size of H1 2017 in the Moscow region got to 13,200 sq m which was 1,500 sq m less than the same value in 2016, which had hit record highs of the first half of the year in the history of the market.

Traditionally, the largest transaction volume is registered in the north and south of the Moscow region, where 46% of all transactions were concluded by the end of the first half of 2017 owing to the large supply volume in these directions and the developed transport infrastructure. The share of transactions increased from 6% to 19% in the east of the region compared to H1 2016. This growth was ensured by several major transactions happened here during the reporting period. However, it is not the reason to say that demand is shifting to the east of the Moscow region.

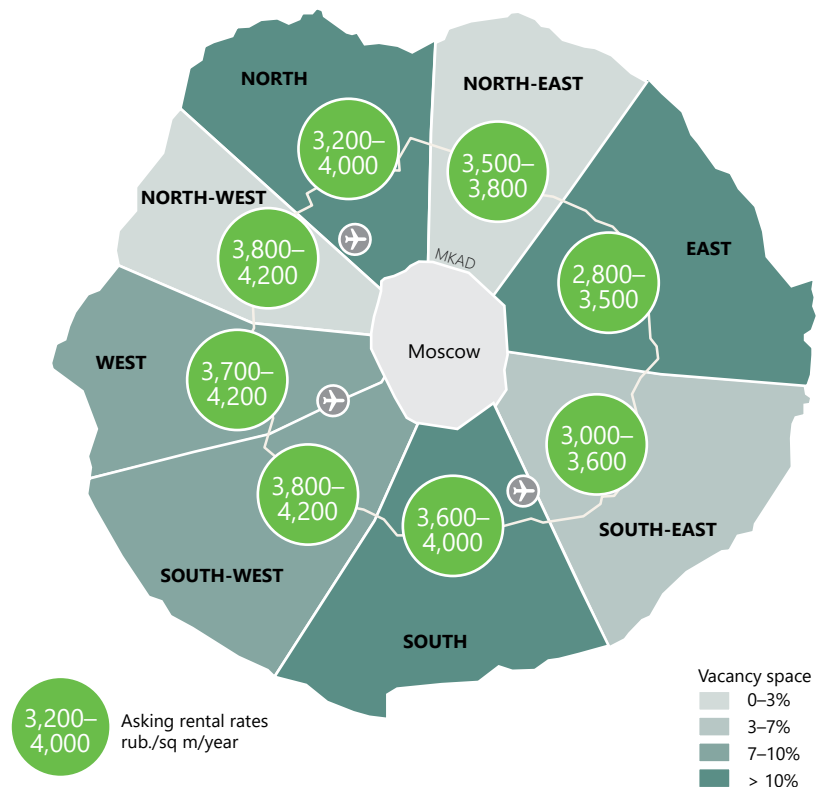
The share of purchase transactions completed by end users still remains low: about 7% in the total volume of H1 transactions. Of note, the share of such transactions was only 2.5% in the same period last year.

Commercial terms

The average Class A rents decreased by 7.5% on H1 2016 and reached a value of 3,700 rub./sq m/year (triple net – excluding VAT, operating expenses and utility payments). Class B rents remained unchanged for the last 12 months and stayed at the level of 3,000 rub./sq m/year.

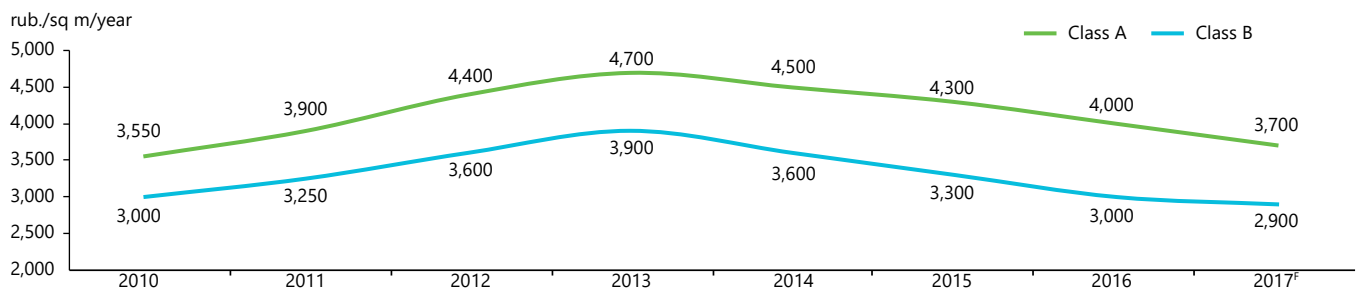
1.5 million of vacant sq m have exercised a significant impact on the rental rates dynamics, constraining their growth. Landlords are forced to conclude lease contracts for 5–7 years with the possibility of early termination after 3–4 years in order to attract tenants. In addition to the early termination of contracts, developers are flexible with other commercial terms: rent-free period increase, payments by installments.

The asking rental rates and breakdown of Class A vacant space by the directions of the Moscow region



* Triple net – excluding VAT, operating expenses and utility bills
 Source: Knight Frank Research, 2017

Dynamics of average ruble rental rates* for warehouses of the Moscow region



* Triple net – excluding VAT, operating expenses and utility bills
 Source: Knight Frank Research, 2017





Forecast

We expect that the total delivery volume in the market of the Moscow region may reach about 400,000 sq m by the end of the year. The development is economically impractical thanks to the heavy volume of vacant space and low rental rates leading to the implementation delay of new projects.

The volume of transactions in the Moscow region will approach circa 1 million sq m in 2017, which corresponds to the 2016 level. Retail operators – the driving force of demand in the Moscow region in 2014–2016, completed the optimization of their warehouse facilities in Moscow and are now actively developing warehouse space in the regions. However, the activity of companies from other sectors (production, distribution) has boosted allowing to maintain the market

demand at a level comparable to the previous years.

In our opinion, the low delivery volume of new facilities and the ongoing demand for quality warehouse property in the Moscow region will give the vacancy rate an opportunity to drop to 11% by the end of 2017. The facilities commissioned before the end of 2017 will not have a sizable effect on the vacant space growth, since most of them are implemented according to the built-to-suit scheme.

Large vacant stock still has a strong impact on asking rental rates, despite the fact that they have hit bottom values, thus probably reflecting in 3–5% decrease of the rates until the end of 2017, according to our projections.

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Key indicators of warehouse market of Moscow region

Indicator	2013	2014	2015	2016	2017 ^F
Total quality supply volume at the end of Q4, thousand sq m	9,603	11,240	11,957	12,666	13,066
New delivery in Q1–Q4, thousand sq m	763	1 637	717	709	400
Lease and purchase transactions volume, thousand sq m	1,280	911	1,231	1,099	1,000
Vacancy rate, %	1.9%	9.2%	9.4%	9.3%	10%
Asking rental rates, rub./sq m/year	4,700*	4,500	4,300	4,000	3,700

* Ruble rental rates has calculated based on the annual average dollar rate for the period under review.

Source: Knight Frank Research, 2017



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