

An aerial photograph of a warehouse loading dock. Several white semi-trailers are parked at the bays. One trailer is yellow. The dock has a concrete floor with white and yellow markings. In the background, there are air conditioning units on a raised platform.

Q1 2017 WAREHOUSE MARKET REPORT

Moscow

HIGHLIGHTS

56 thousand sq m of quality warehouse space were put into operation in the Moscow region in Q1 2017.

The volume of lease and purchase transactions of warehouse space in the Moscow market was almost 60% lower than in the comparable period a year earlier and amounted to 98.1 thousand sq m.

Retail operators continue to be the main consumers of warehouses, but their share decreased year-on-year.

The average asking rental rate shows a slight reduction: the indicator dropped by 5% since the beginning of the year.



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

"The first quarter of this year brought a timid hope for all participants of the market that the demand for quality warehouse projects in the Moscow region will be restored. In my view, this is primarily due to positive changes in the economy of the country. Therefore, many companies that previously took a wait-and-see attitude and just estimated the terms and rates, decided to take advantage of the favorable moment and lease warehouse space. At the same time, the main driver of demand in 2016 was food retail operators, but by the results of the first quarter, companies of pharmaceutical distribution and online trade segment completed the major share of transactions. We also witness an increased number of requests for the acquisition of warehouse complexes.

As for the construction of new facilities, the scenario has not changed as a whole. Today, the level of rental rates and the amount of vacant space make the implementation of new projects economically unprofitable, which is confirmed by the minimum delivery volume. Therefore, the share of built-to-suit projects will not go down in 2017".

WAREHOUSE MARKET REPORT MOSCOW

Key indicators. Dynamics*

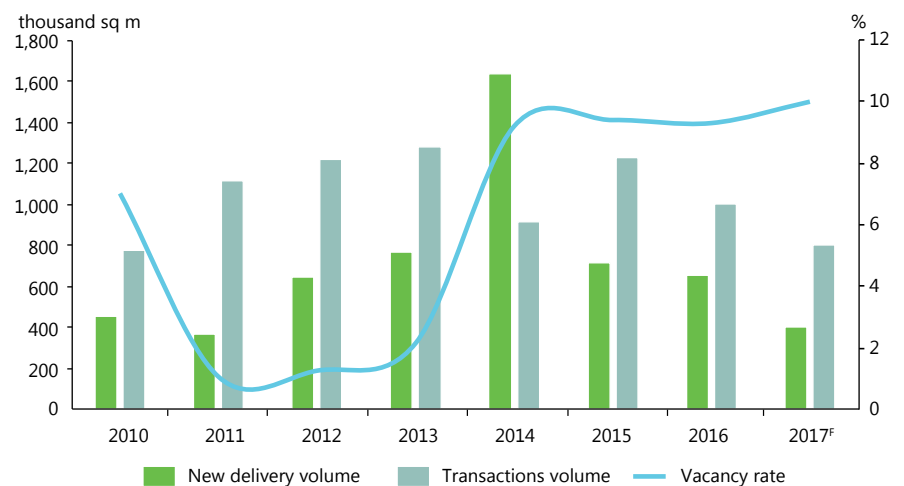
	Class A	Class B
Total quality supply volume, thousand sq m	12,722	
including, thousand sq m	10,771	1,951
New delivery in Q1 2017, thousand sq m	56	
Lease and purchase transactions volume in Q1 2017, thousand sq m	98.1	
Vacancy rate, %	12 ▲	
Asking rental rates**, rub./sq m/year	3,000–4,500 ▼	2,000–3,500 ▼
Operational expenses, rub./sq m/year	1,000–1,200 ▶	700–900 ▶

* Compared to the end of Q4 2016

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

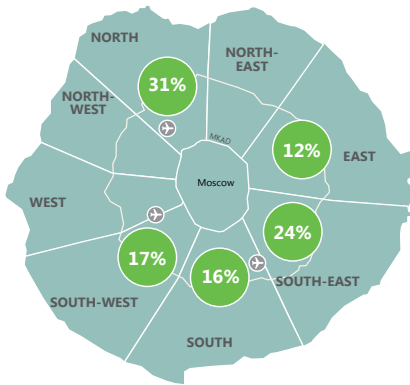
Source: Knight Frank Research, 2017

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

Supply

56 thousand sq m of quality warehouse space were put into operation in the Moscow region in Q1 2017, which was almost 60% lower than in the comparable period a year earlier. Significantly, all the delivered facilities were speculative.

Small, but stable demand as well as the continuing optimization by tenants of their warehouse facilities have adjusted the vacancy rate despite the low delivery volume. The Q1 vacancy rate reached 12%, which was almost 3 p. p. higher than the final indicator of 2016. The largest amount of vacant space was concentrated in the north of the region, which was one of the leaders to deliver new warehouse complexes (including speculative properties) over the last few years.

Demand

98.1 thousand sq m were purchased and leased for Q1 2017 in the Moscow region, which was almost 2.5 times less against last year's figure, as Q1 2016 was record-breaking in the history of quality warehouse real estate market.

The total volume of transactions in Russia reached a total of 244 thousand sq m. The main difference in the regional structure of Q1 transactions was the decrease in the share of the Moscow region, which was historically much larger than the share of other Russian cities: it was equal to 40% in Q1 and was less than the share of transactions in regional cities of Russia (excluding Moscow and St. Petersburg).

As for the geographical distribution of transactions, their largest volume was recorded in the north and south-east – about 55%.

The downward trend of the share of retail companies in the total volume of transactions, which started in H2 2016, ran on in Q1 2017. These companies had been the driving force of the industry in the last 2 years. They were responsible for about 34% of the transactions for the first three months of 2017, that was still the highest value among other profiles, but significantly smaller than before. For comparison, the share of retail companies was about 50% in H1 2016. Almost all food retailers implemented their short-term lease programs with warehouse space in 2015–2016. Now distributors and manufacturing companies are stepping forward. A high proportion of companies from the online trade segment in Q1 2017 are rather related to a small aggregate volume of transactions, where each transaction can have a significant share. It is too early to say that online trade will be the new driving force of the warehouse industry.

The average size of Q1 transaction amounted to 10.5 thousand sq m, which was generally in line with the common practice, when major transactions did not occur at the beginning of the year, as well as with the fact that large players had already used the current market situation to lease or purchase the necessary space.

Commercial terms

3,700 rub./sq m/year is currently the average asking rental rate for Class A warehouses in the Moscow region, for Class B premises – 3,000 rub./sq m/year (triple net – excluding VAT, operating expenses and utilities). The knockdown in rates totaled 5% since the beginning of the year.

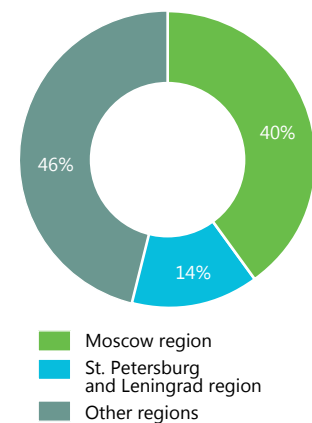
The lease agreements are primarily concluded for 3–5 years at rental rates denominated in Russian currency. Tenants insist on the condition of mandatory early termination if long-term agreements are concluded for 5–7 years. Developers demonstrate flexibility in commercial terms in order to keep existing tenants and to attract new ones: for example, they extend rent-free period or offer payment by installments.

The amount of vacant space rose up to 1.5 million sq m for the first three months of 2017 through not the most liquid projects: now tenants have the opportunity (and use it)

to move from depreciated warehouse complexes to modern facilities where attractive rental rates are offered on top of it.

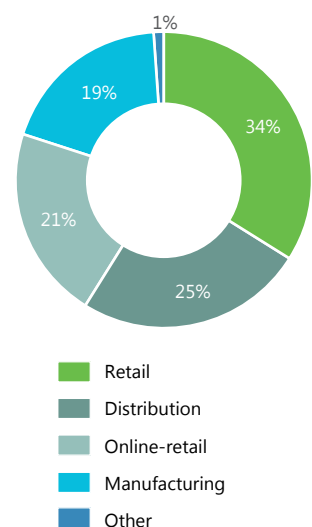
The driving factor of most tenants when choosing new premises is the rental cost owing to the current difficult economic conditions. The quality of the building and its location are still secondary factors.

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



Source: Knight Frank Research, 2017

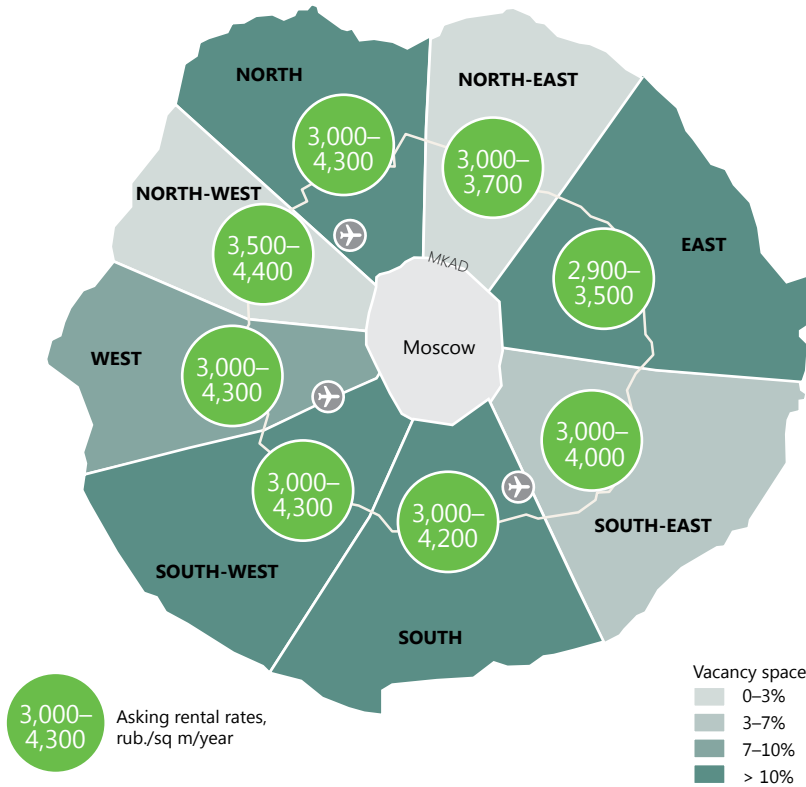
Breakdown of lease and purchase transactions of warehouse space in the Moscow region by tenant profile



Source: Knight Frank Research, 2017

WAREHOUSE MARKET REPORT. MOSCOW

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

Forecast

We witness the restrained optimism from developers and tenants, as well as from investment funds as a result Q1 2017. Many of them have optimized their costs, adjusted to external conditions and are thinking about further development. Thus, we expect the current demand for quality warehouse complexes to be strong until the end of 2017. Developers can even announce the launch of new projects.

There are practically no warehouse complexes vacant where landlords used to purposefully follow the dumping policy in relation to rates to attract tenants. However, a significant amount of vacant space continues to affect the rates. We expect the rates will continue falling by 3-5% during 2017.

In 2017, the profile of tenants will go on changing: companies from the retail sector are likely to remain among the leaders in terms of the leased space, but their share will hardly exceed 30% in the total volume of transactions. Manufacturing companies and distributors will actively develop, becoming one of the most active tenants of the year.

Low expected delivery and stable demand will have a positive impact on the vacancy rate. We expect it to fall down to 10% by the end of 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

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