

A low-angle, upward-looking photograph of a modern glass skyscraper against a clear blue sky. The building's facade is composed of a grid of dark blue glass panels, reflecting the sky and surrounding environment. The perspective creates a strong sense of height and architectural scale.

# Q1 2014 OFFICE MARKET REPORT

Moscow

## HIGHLIGHTS

- 209 thousand sq m of Class A and B office space have been delivered in Q1 2014, which is almost 20% lower than for the same period last year.
- The transactions volume on lease and purchase of high-quality office space in Q1 2014 has dropped compared to the previous year by almost 35% amounting to roughly 100 thousand sq m.
- The vacancy rate has slightly grown compared to the end of 2013, amounting to 16.3% for Class A and 12.3% for Class B office buildings in Q1 2014.
- The average lease rate for Class A offices has dropped by 3%, amounting to 776 \$/sq m/year, while for Class B, over the same period, it has dropped by almost 7% to the figure of 457 \$/sq m/year

## OFFICE MARKET REPORT



**Konstantin Losiukov,**  
Director  
Office Department,  
Knight Frank

*"The office market of today is "the tenant's market". The vacancy rates growth coupled with a drop in average lease rates enabled companies to choose premises in buildings of any size and at any stage of readiness. Landlords, in turn, are willing to discuss provision of office blocks of various sizes, reduced lease rates and carry out finishing works at their own expense. However, I would not characterize current market state as that of recession, but rather as a "cool-down" after a period of strong growth of 2011–2012".*

### Key indicators. Dynamics\*

Key indicators	Class A	Class B
Total stock, thousand sq m	13,545	
including, thousand sq m	2,814	10,731
Delivered in Q1 2014, thousand sq m	209	
including, thousand sq m	130	79
Vacancy rate, %	16.3	12.3
	+0.1 p. p.	+0.8 p. p.
Average asking rental rate**, \$/sq m/year	776	457
	-3.0%	-6.9%
Rental rates range**, \$/sq m/year	360–1,200 (1,000–1,300***)	250–1,000
Average OPEX rate, \$/sq m/year	150	100
* Compared to Q4 2013		
** Excluding Operational Expenses and VAT (18%). The operational expenses do not include changes associated with an increase in property tax		
*** Range of asking rents for premium fitted-out space		
Source: Knight Frank Research, 2014		

### Supply

By the end of Q1 2014, the total supply of high-quality office space in Moscow has exceeded 13.5 million sq m, comprised of 2.8 million sq m of Class A and 10.8 million sq m of Class B offices.

Following the post-recession decline, since 2012, office space delivery volume began to grow. This year, in comparison with 2013, the expected growth will amount to almost 15%. However, despite the large amount of high-quality office space planned for delivery until the end of 2014, only 209 thousand sq m of Class A and B offices were delivered in Q1, which is almost 20% lower than for the same period last year. The reason for this is postponement of planned delivery dates for a number of objects.

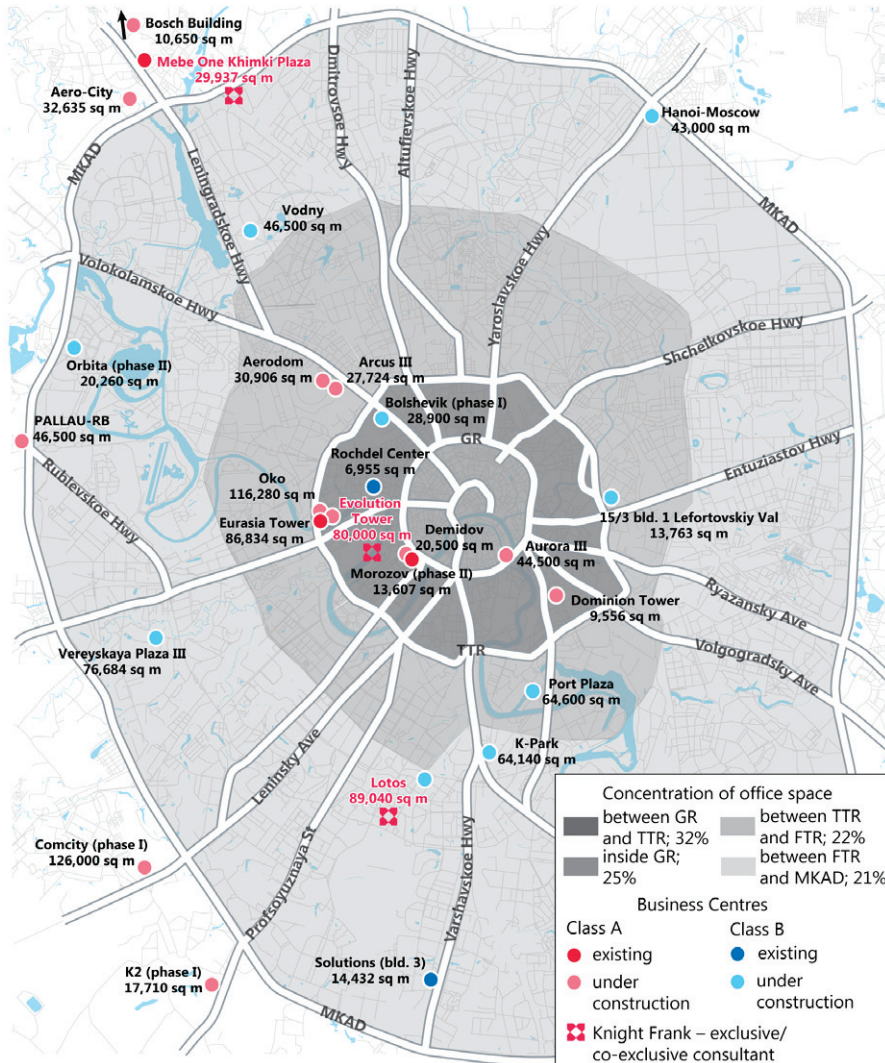
Formation of decentralized business districts continues on the office market of Moscow. In the first three months of 2014, considering the total amount of new supply, only 18% of office space in Class A and B was delivered within the Garden Ring. This figure will continue to decline, and by



BC ALCON  
72 Leningradskiy Ave

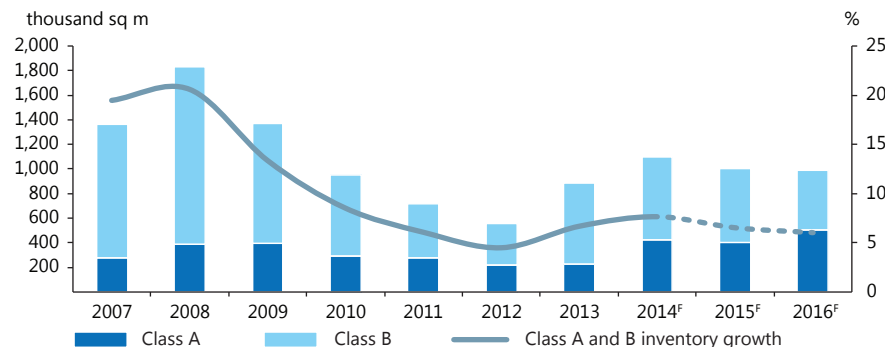


## Key office projects delivered in Q1 2014 and due to be completed by the end of 2014

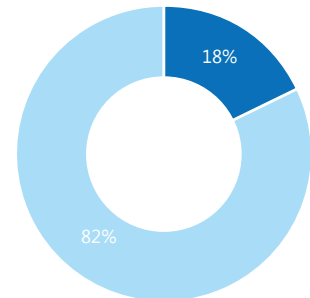


\* Office properties that received the delivery act in Q1 2014  
The buildings class is indicated according to the Moscow Research Forum Office Classification of 2013  
Source: Knight Frank Research, 2014

## Delivery of almost 3 million sq m of high-quality office space is planned for by 2016



## Dynamic decentralization continues of the office market of Moscow



Source: Knight Frank Research, 2014

2016, more than 90% of high-quality office space will be delivered outside the Garden Ring. The largest volume will fall with the business districts formed in the areas located along the Leningradskoe direction, as well as in the MIBC Moscow-City and on the New Moscow territory near the MKAD.

## Demand

The volume of demand in Q1, traditionally the least active period, in 2014, showed the lowest value since mid-2009. High-quality office space lease and purchase transactions volume for 3 months in 2014 dropped by almost 35% compared to Q1 of the previous year and amounted to about 100 thousand sq m.

In 2013, we observed a drop in demand caused by the companies' wariness due to the economic situation in the country and the world, as well as their desire to optimize the office space in order to reduce lease costs. In 2014, against the backdrop of uncertainty, the tenants' mood will also be determined by the geopolitical and economic situation in the country. In Q1 2014, significant currency fluctuations took place. This has led to the situation where a number of companies refused to move or postponed signing lease contracts for an indefinite period. Those who decide to move, try to reduce the risks associated with currency by fixing the exchange rate corridor.

The vacancy rate has slightly grown compared to the end of 2013; amounting to 16.3% (0.1 percentage points growth) in Class A offices and 12.3% (0.8 percentage points growth) in Class B office buildings

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Moscow

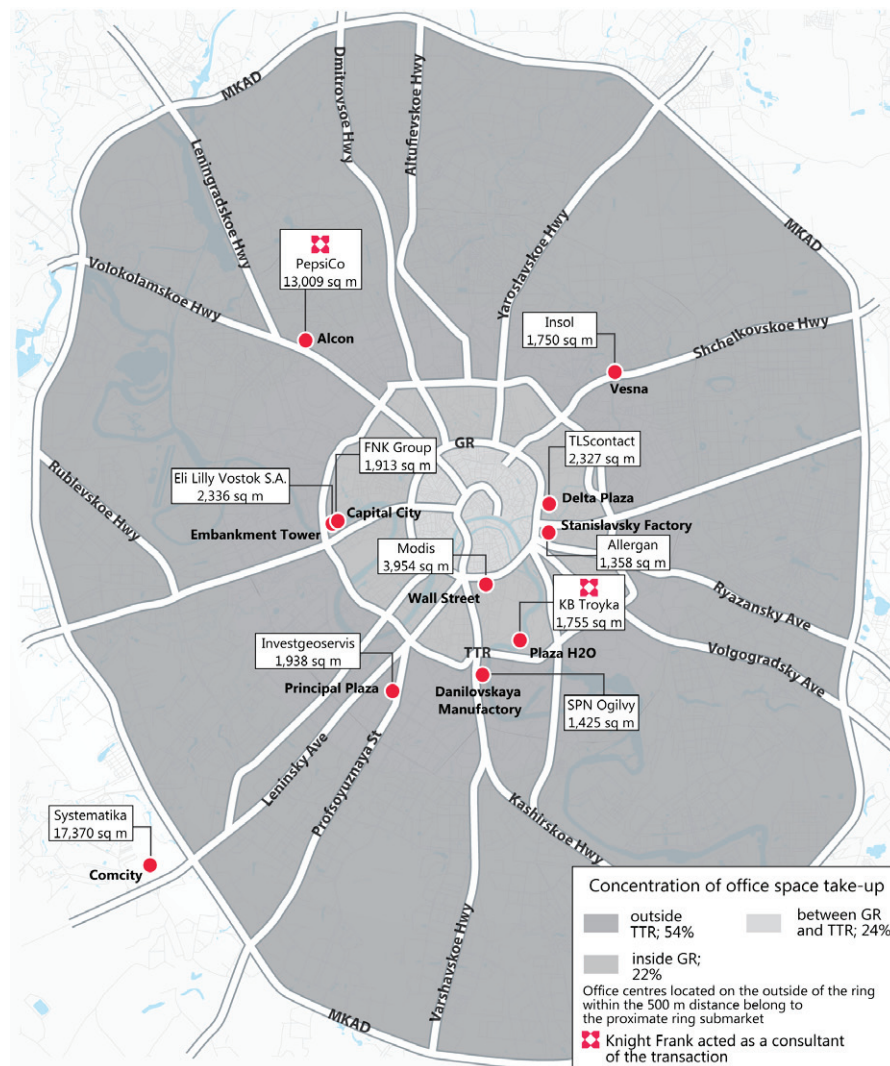
by the end of Q1 2014. Although, according to our forecasts, the growth figures could have been more significant, this did not happen since for the considered period the delivered premises were either built "for the client" or almost completely leased out on the construction stage.

The tenants' queries structure has also changed: Class B office buildings were in greater demand. This resulted from two main reasons: the first one being the growth in the number of requests for the purchase of office space, as the supply stock is available precisely in the segment of Class B business centers; the second one is the companies' desire to reduce the lease cost. Consequently, the number of requests for office lease offered at a lower rate continues to grow.

The average deal size in Q1 2014 has dropped to 1.2 thousand sq m (1.6 thousand sq m in Q1 2013 and 1.4 thousand sq m at the end of 2013), as only two office lease deals with the size exceeding 5 thousand sq m were closed.

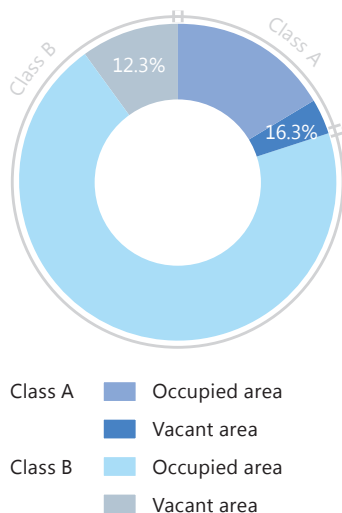
The largest volume of leased and purchased office space in Q1 2014 fell with the FMCG and TMT sector companies. In total, these companies have leased and purchased more than a half of high-quality office space in the total volume of Q1 2014. However, it is worth noting that such ratio has been achieved through two major transactions. Furthermore, steady demand was noticeable with oil and gas mining and delivery companies, pharmaceutical companies and B2B companies. The share of financial sector, which traditionally owns

## Key office space lease and purchase transactions closed in Q1 2014



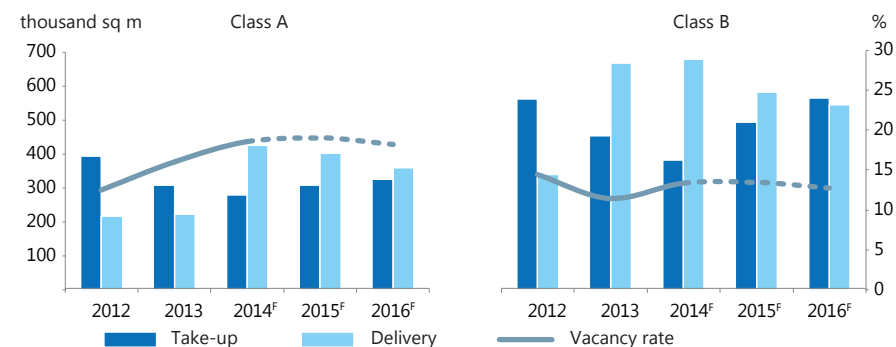
Source: Knight Frank Research, 2014

## Total supply volume and vacancy rate by class



Source: Knight Frank Research, 2014

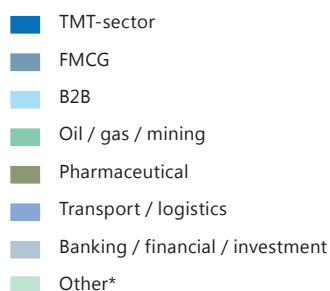
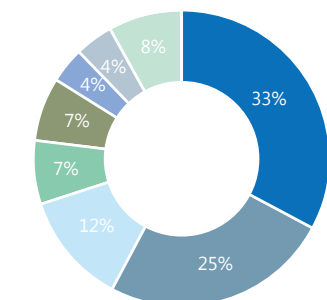
## In 2014–2015 the growth of vacancy rates in Class A and B office facilities will continue



Source: Knight Frank Research, 2014

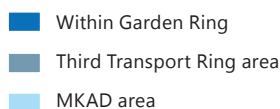
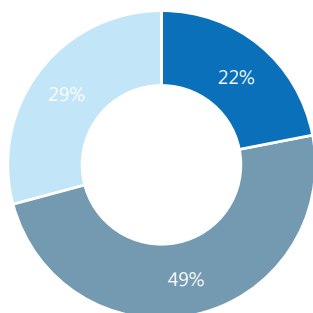


**Over a half of office space in Q1 2014 was leased or purchased by the IT and telecommunication companies and FMCG sector representatives**



\* Other: manufacturing and construction companies  
Source: Knight Frank Research, 2014

**In Q1 2013, almost a third of office space was leased and purchased in the business centers located in and around MKAD**



Source: Knight Frank Research, 2014



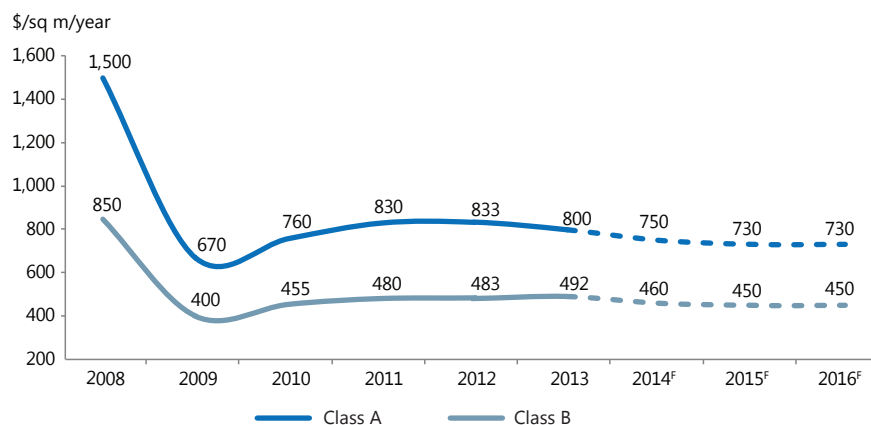
a big part in the total transactions volume did not exceed 5% in Q1 2014.

Although the center of Moscow is historically the focal point of business activity, almost a half (49%) of office space leased and purchased in Q1 2014 fell with objects located near the Third Ring Road. While the figure for the business centers located within the Garden Ring, was more than 2 times lower (22%).

## Commercial terms

In Q1 2014, the average weighted lease rates for high-quality office space in Moscow have dropped relative to those of the end of last year. For Class A offices, the average lease rate has dropped by 3% amounting to 776 \$/sq m/year, while in Class B this figure has dropped by almost 7% to the level of 457 \$/sq m/year

## Rental rates decline will continue for the coming two years



Source: Knight Frank Research, 2014

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Moscow



Mebe One Khimki Plaza  
25 Leningradskaya St. Khimki

A decline in the average lease rates for Class A and B office space is a consequence of changes in the balance of supply and demand. A larger volume of delivered office buildings against the backdrop of decline in demand is forcing landlords to offer more attractive commercial terms, to fill the vacant premises.

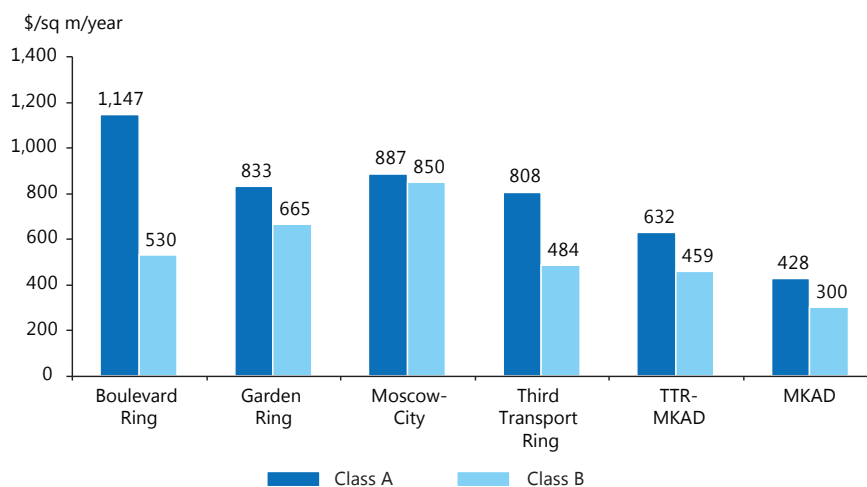
It is curious that in developed business districts, which are characterized by a large volume of supply and strong competition in attracting tenants, the difference in lease rates for Class A and B office space may be minimal.

## Forecast

The situation on commercial real estate market, as well as in the economy of the country as a whole are characterized by a high degree of uncertainty, which undoubtedly causes a negative impact on the investment climate and demand volumes.

Given the preservation of current macro-economic situation, we do not expect major

## Average asking rental rate for Class A and B offices depending on location



Source: Knight Frank Research, 2014

changes on the lease and purchase market of office real estate in the coming year. The planned office space delivery volumes in Class A and B segments in 2014–2016 will

amount to almost 3 million sq m, which will lead to further growth of vacancy rates and decline in lease rates considering low volume of demand.

## Europe

Austria  
Belgium  
Czech Republic  
France  
Germany  
Ireland  
Italy  
Monaco  
Poland  
Portugal  
Romania  
Russia  
Spain  
Switzerland  
The Netherlands  
UK  
Ukraine

## Africa

Botswana  
Kenya  
Malawi  
Nigeria  
Tanzania  
Uganda  
Zimbabwe  
Zambia  
South Africa

## Middle East

Bahrain  
UAE

## Asia Pacific

Australia  
Cambodia  
China  
India  
Indonesia  
Malaysia  
New Zealand  
Singapore  
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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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