



H1 2011

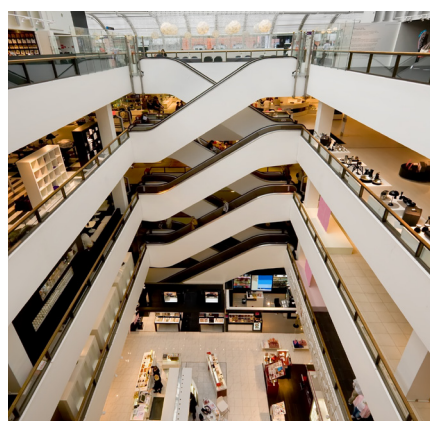
RETAIL REAL ESTATE MARKET

Moscow

Knight Frank

EXECUTIVE SUMMARY

- Current and future slowdown in growth of supply of retail space due to slower construction rates and suspension of retail projects during the crisis.
- Revival of development plans by retail operators, leading to greater competition for retail space and reappearance of waiting lists for properties most in demand.
- Increase of retail rents.

RETAIL REAL ESTATE MARKET.
MOSCOW

Julia Dalnova
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Strong growth of demand for premises from retail operators and slowdown in rates of supply growth make us expect intense competition for premises in the next two years, resulting in higher rent levels.

We also expect that the ban imposed by the Mayor of Moscow on construction of commercial property inside the Third Transport Ring will lead to rise in the value of functioning retail properties in the long term.

Key events

- Since autumn 2010 Moscow city hall has been reviewing current investment contracts. Some of them have already been annulled, and several major retail projects have been revised. Construction of large underground retail complexes on Pushkin square and Tverskoy Zastavy square have been cancelled. In the latter case the developer, AFI Development, was able to reach agreement with city hall on compensation of expenses already made for creation of the underground complex. The compensation may cover purchase by the developer of the city's 25%

Main indicators. Shopping centres*		Trend
Total area of high quality shopping centres (total space / GLA**), million sq m	7.77 / 4.18	
Total area of shopping centres commissioned in 1H 2011 (total space / GLA), million sq m	0.26 / 0.15	
Total area of shopping centres scheduled to open in 2H 2011 (total space / GLA), million sq m	0.31 / 0.17	
Vacancy rate, %	3	↓
Base rental rates, \$ per sq m per annum (not including operating expenses and VAT)		
anchor tenants	100-400	↑
retail gallery tenants	600-4,000***	→
Operational expenses, \$ per sq m per annum	80-255	→
Provision by quality retail area, sq m GLA per 1,000 residents	363	
<p>* The table only shows data for professional shopping centres (a professional shopping centre is defined as one building or a group of architecturally connected buildings with gross leasable space in excess of 5,000 sq m, united by a single concept and under single management)</p> <p>**Gross leasable area</p> <p>*** Rates for stores with space of about 100 sq m on the ground floor</p> <p>Source: Knight Frank Research, 2011</p>		

stake in the Afimall City retail project in Moscow City (the capital's new business district).

- Investments in the retail segment saw an upturn during the first half of 2011, and retail emerged as the leader among commercial property segments by number of transactions. The total amount of investments in retail projects increased by 10 times in comparison with 2010. Major transactions on the Moscow market included: purchase of the 57,000 sq m Kaluzhsky shopping centre from MCG (owned

by Pavel Fuks) by structures under the control of the businessmen Mikhail Gutseriev and Mikhail Shishkhanov for an estimated price of \$150-230 million; and purchase by Yuri and Alexei Khotin of the Gorbushkin Dvor and Filion retail centres from MTZ Rubin (the centres have 60,000 and 128,000 sq m of space, respectively, and total transaction value is estimated at \$400-500 million). It became known earlier that IMMOFINANZ had bought the remaining 25% of the Goodzone shopping centre, which is being built in the southern part of Moscow.



- There were two major takeovers of retail operators in the first half of 2011: the food retailer Diksy Group bought the Victoria retail chain; and Alexander Zanadvorov, owner of the retailer The Seventh Continent bought four Mosmart shopping centres in Moscow, which are to be rebranded as Nash Gipermarket.

Supply

Total space at quality shopping centres on the Moscow market* at the end of 1H 2011 was 7.77 million sq m, and GLA was 4.18 million sq m. Quality GLA per 1,000 population in Moscow is 363 sq m, which still leaves the Russian capital behind most large cities in Europe.

The following shopping centres opened for business in Moscow during 1H 2011:

- A shopping centre as part of the MonArch mixed use complex at Bld. 1, 31 Leningradsky Ave (16,000 sq m total space, 10,700 sq m GLA);
- Planernaya Interchange (a public transport interchange with retail premises at Planernaya metro station with total space of 50,300 sq m and 11,000 sq m GLA).
- Afimall City shopping and leisure centre in Moscow City (179,400 sq m total space, 114,200 sq m GLA).
- Severnoye Siyaniye shopping and leisure centre in Northern Butovo (partially opened, 17,000 sq m total space and 10,000 sq m GLA).

Growth of shopping centre supply in H1 2011 was 263,000 sq m with 146,000 sq m GLA.

Effects of the freeze in retail centre construction during the crisis are being acutely felt in Moscow during 2011. About 300,000 sq m of new space with 167,000 sq m GLA is likely to open in the city during 2H 2011, so total growth of supply for the year will be no more than 560,000 sq m (313,000 sq m GLA), which is the lowest figure since 2003, when new GLA was about 230,000 sq m.

No major increase in the rate of retail space growth is expected in 2012, when about 800,000 sq m (350,000 sq m GLA) is likely to

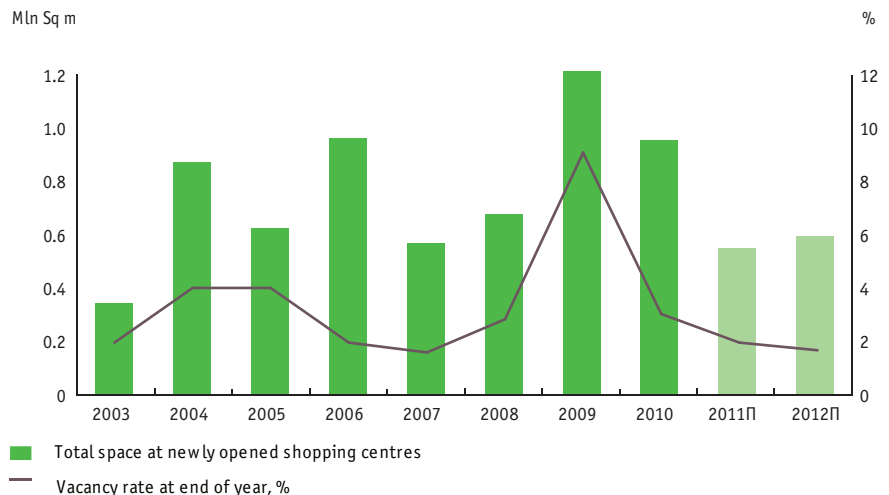
*We include large shopping centres located outside the capital but near the MKAD in the Moscow market because they are focused mainly on the capital's residents.

The central administrative district is the leader in Moscow by retail space per capita, and the eastern district is the last one by this indicator



Source: Knight Frank Research, 2011

We expect commissioning of new retail space in 2011 to be at their lowest level since 2003



Source: Knight Frank Research, 2011

open. A significant part of new supply next year will be at two large-scale projects in the capital's southern administrative district: River Mall (258,000 sq m with 88,500 sq m GLA) and Goodzone (123,000 sq m with 70,000 sq m GLA). Both projects were announced before the crisis and their opening will reinforce leadership of the southern administrative district by volume of retail centre supply (at the end of H1 2011 the district had 600,000 sq m, which

is 14% of total supply on the Moscow market). Despite this, the southern district takes a low sixth place among Moscow's nine districts by quality retail space per capita due to its high population, while first place is taken by the central administrative district, where the low number of residents entails nearly 760 sq m of space in quality shopping centres per 1,000 population (not including street retail).

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RETAIL REAL ESTATE MARKET

Moscow



Demand

Trends in visitor traffic at shopping centres match development of retail turnover. Figures from Rosstat show growth of retail turnover by 5.3% in 1H 2011 in comparison with the same period of 2010 (growth of retail turnover y-o-y in the first six months of 2010 was 4.6%). Several retail chains reported y-o-y revenue growth in the first half of 2011, as well as growth of the average check.

Demand for retail space has recovered, but shortage of new premises in Moscow is holding back development by retail operators. Record volumes of new supply, which came onto the Moscow market in the acute stage of the crisis

in 2009-2010, had been almost fully taken up by 2011. Successful shopping centres have waiting lists of would-be tenants and new centres have lease contracts for more than 80% of space before they open. Nevertheless, there are a number of shopping centres with high vacancy levels (above 15-20%). These are mostly projects built some time ago, with poor location and high levels of competition in their vicinity. Many of them need overhauls or full-scale reconstruction.

The average vacancy rate on the market is about 3%, and there is no free space for rent in successful shopping centres. Retail operators which announced large-scale development plans in the Moscow area at the end of 2010

have been forced to readjust their strategy towards regional expansion due to shortage of available premises in Moscow.

Commercial terms

Rental rates at Moscow retail centres has been increasing since the middle of 2010, but rates of growth have been modest despite the shortage of retail space: increase of rental rates from the start of 2011 has only slightly outpaced inflation (5-7% in rubles). Average rent growth in US\$ has been 8-10%.

Lease contracts usually include annual indexation of 10-12% and a step-rent method is increasingly used, by which a relatively low rent is set for the period of launch and leasing of premises to tenants, and the rate is increased at the end of an agreed period or when the shopping centre achieves a specific level of traffic.

The range of operating expenses has not seen major change since the start of 2011 and remains in the region of \$70-255 per sq m per annum.

Rental rates at Moscow shopping centres, H1 2011

Type of premises	Area, thousand sq m	Retail profile	Rate, \$ per sq m per annum*
Anchor tenant premises	>5,000	Food hypermarkets	100-200
		Other retailers	100-250
	1,500-5,000	Food hypermarkets and other retailers	200-400
	500-1,500	Food supermarkets and retailers	200-500
Retail gallery premises	100	Children's goods	300-1,000
		Clothes, footwear (ground and first floors)	700-2,000
	50	Leather accessories, bijouterie, gifts, jewellery, mobile telephones (ground floor)	1,300-4,500

*Not including operating expenses and VAT (18%)

Source: Knight Frank Research, 2011



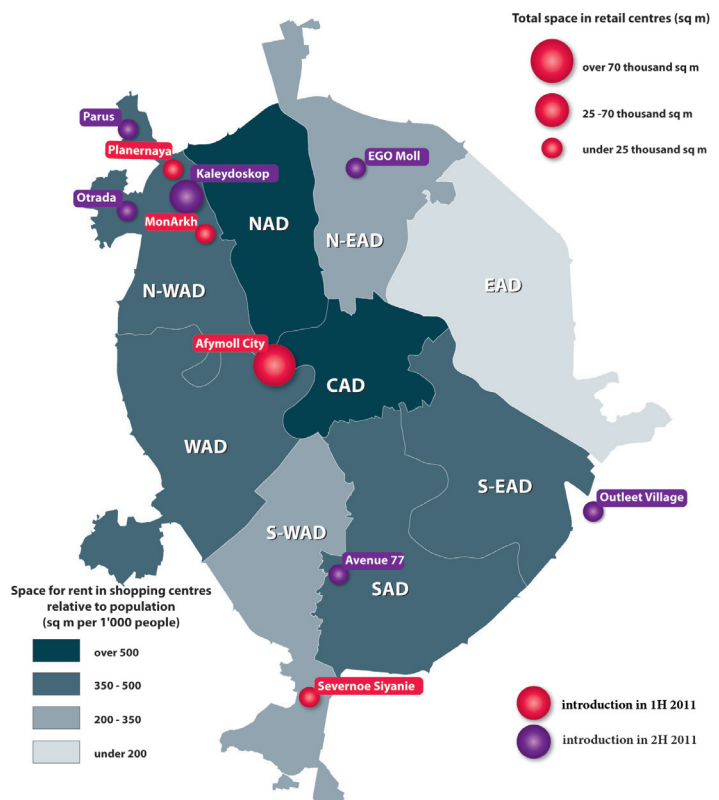
Forecasts

Significant increase of rental rates in the second half of 2011 is very probable in view of imminent shortage of retail space on the Moscow market. We predict rise of asking rates in US\$ by more than 20% in the whole of 2011.

We expect that developers activity on the Moscow retail real estate market will recover in the immediate future following sharp declines caused by the crisis and then by initiatives of the new team at Moscow city hall. New projects will be seen outside the Third Transport Ring, in the form of both stand-alone shopping centres and retail projects as part of new residential districts and mixed-use complexes. Intensive construction of retail centres is also likely in towns in Moscow Region, which still have an acute shortage of modern retail space.

Assuming further positive trends in the economy, the best opportunities for development of retail chains in the next few years are in regional cities with populations of 300-500,000. Regional expansion by retailers will encourage a reorientation of developer activity away from Moscow.

Shopping centres opened in H1 2011 and main openings scheduled in 2H 2011. GLA per 1,000 population by Moscow districts in H1 2011.



Source: Knight Frank Research, 2011

OVERVIEW



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