OVERVIEW

2011

INVESTMENT MARKET

Moscow

Knight Frank

EXECUTIVE SUMMARY

- In 2011 recovery of the debt capital market was observed: loans to legal entities grew by 25% for the twelve months of the year.
- Total commercial real estate acquisitions almost doubled over last year and reached $8 billion.
- Major characteristics of the market in 2011 was high level of investments' differentiation by segments with the retail and office segments accounting for 40% each.
- An undoubtedly positive trend was foreign investors' returning to the Russian market. The share of foreign capital transactions exceeded 33%.

INVESTMENT MARKET

Main indicators

Segment	Office		Shopping centres	Warehouses		Hotels* 3-5★
Class	A	B		A	B	
New supply, thousand sq m,	275.0	445.0	320.0	328.9	37.3	1,150
Change, %	↑ (+13.0%)	↑ +4.9%	↑ +4.3%	↑ +7.7%	↑ +2.0%	↑ +3.7%
Vacancy rate, %	12.5%	18.3%	2.5%	0.2%	2.0%	62.3%
Change from the beginning of the year, persentage points (p.p.)	↓ -5.0 p.p.	↓ -3.0 p.p.	↓ -1.5 p.p.	↓ -4.8 p.p.	↓ -9.5 p.p.	↑ +0.3 p.p.
Rates, $ per sq m per annum	830	480	100-500 / 700–4,000 **	130–140	105–125	171
Change from the beginning of the year, %	↑ +9.2%	↑ +5.5%	↑ +12.0%	↑ +11.0%	↑ +18.0%	↑ +9.0%
Yield***, %	8.5–9.5%	10.0–11.0%	9.0–10.0%	10.0–10.5%	11.0–12.0%	-
Change from the beginning of the year, p.p.	↓ -1.0 p.p.	↓ -1.0 p.p.	↓ -1.5 p.p.	↓ -0.5 p.p.	→	-
Average selling price, $ per sq m	6,500 – 8,000	4,500–6,500	3,000–7,000	1,100–1,400	600–800	200–1,000

* For hotels the respective lines show: number of new rooms; room occupancy (%); average daily rate ($ per room per day); and average selling price per room (thousand $ per room)

** Figures for anchor tenants and retail gallery operators

*** Estimated cap rate

Source: Knight Frank Research, 2012

Evgeniy Semyonov
Director of Investments and Sales, Knight Frank

"The past year set a record for the Russian real property market in terms of the volume of investment transactions made. However, one third of all major transactions were made with foreign investors involved. Positive dynamics was primarily attained by strengthening of debt capital market. At the same time, towards the end of 2011, we noted spreading destabilization fears among market players against the background of debt problems in Europe and political transition period in Russia in connection with the parliamentary and presidential elections".

The global economic situation was quite unstable throughout 2011. Debt problems in Europe contributed a lot to uncertainties on the global financial markets causing withdrawal of capital from the risky assets in emerging countries. In particular, the Russian market suffered a total capital outflow of $80 bln as against $30 bln projected in early 2011.

Main Events

- In late 2011, it was announced that by the end of January 2012, Morgan Stanley would close the deal for acquisition of Galleria shopping and leisure centre, the largest one in St. Petersburg (30A Ligovsky Ave). The estimated value of this transaction is $1.1 billion making it the largest one at the Russian commercial real estate market.
- In spring 2011, a decision was taken “to limit, but practically ban, any construction in the centre of Moscow”. Also, at the end of 2011 new borders of Moscow were maintained. The so-called Greater Moscow will officially be established on 1 July 2012.
- Mirax Group, one of Russia’s largest developers, ceased to exist in March 2011.

Financing

The debt capital market started to recover in 2011. Loans to legal entities grew by 25% over 2010 with an even greater increase (38%) in construction financing. This growth came from lower interest rates at the back of better liquidity in the bank sector over 2009-2010.

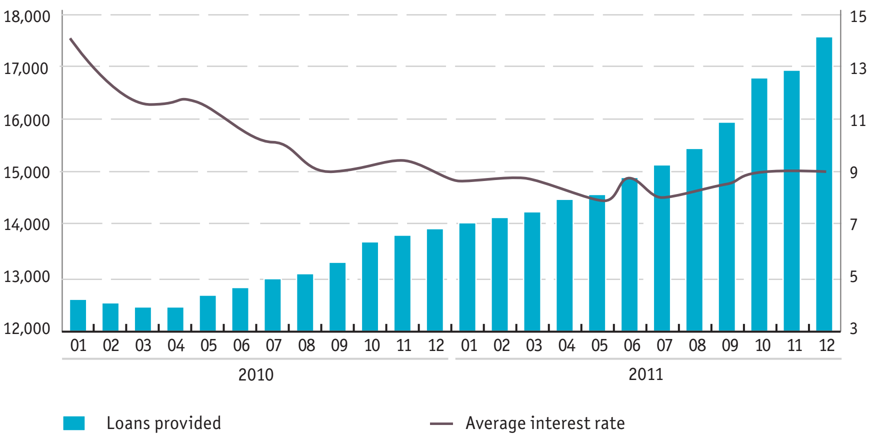
Being in the position to raise cash on quite favorable terms and conditions, Russian state banks continued to drive financing of commercial real property construction. In particular, Sberbank opened a $394-million credit line for Mezhdunarodniy Centr Development to support construction of Mirax Plaza mixed-use centre, and Gazprombank granted $375 million to City Palace to finance construction of Evolution Tower mixed-use centre. Most of the loans were spent on completion of construction, erection of second stages and refinancing.

Foreign banks became more active. For example, Nordea Bank lent funds to AFI Development and Snegiri Development to refinance their loan for construction of Four Winds mixed-use centre. Raiffeisen Bank granted a loan to Immofinanz Group or Pyataya Avenue shopping centre. Most non-Russian banks followed a more conservative credit portfolio strategy and were hardly involved in any development projects because of high risks.

At the same time, projects lending growth resulted primarily from the need for high-yield fund raising at the back of relatively high funding costs for Russian privately-held banks. For example, Russkiy Capital provided funds for Vnukovo Outlet Village construction.

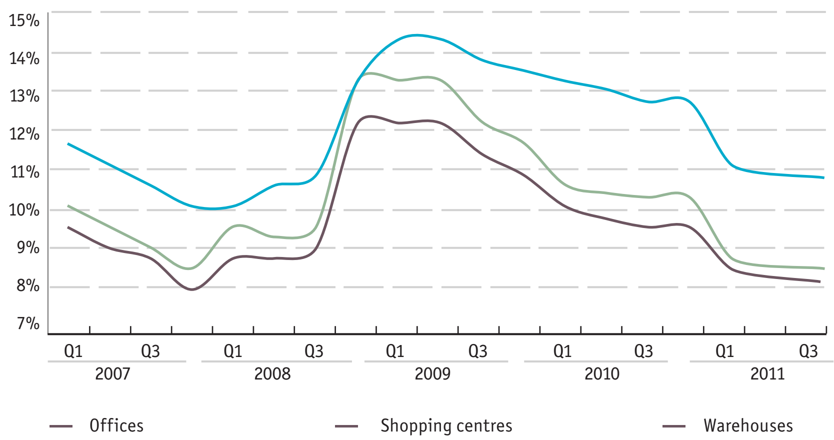
Most banks currently follow a strategy of capping loans by 50-60% of the estimated collateral value. This allows creditors to get their money back in full even in case the market situation goes worse. Stricter terms and conditions were partially caused by a substantial number of non-core assets accumulated in 2009-2010 on the banks' balance sheet as repayment of overdue debt.

Even though the macroeconomic environment was quite unfavorable and loan interest rates were high in Q4 2011, lendings continued to grow rapidly



Source: Knight Frank Research based on the Russian Central Bank's data, 2012

Cap rates for all commercial real estate segments stabilized in 2011 after an almost two-year downturn



Source: Knight Frank Research, 2012

Standard terms and conditions for bank financing in 2011

Terms and conditions	Russian banks		Foreign banks	
	Project financing	Refinancing	Project financing	Refinancing
Rate	12 - 15%	9 - 11%	LIBOR + 800 - 1,200 b.p.	LIBOR + 550 - 700 b.p.
LTV*	50 - 60%	60 - 70%	55%	75%

* The loan-to-value (LTV) ratio expresses the amount of a first mortgagelien as a percentage of the total appraised value of real property

Source: Knight Frank Research, 2012

Major transactions to finance/refinance commercial real estate projects in 2011

Lender	Borrower	Purpose	Transaction details
Sberbank	Dekmos	completion of construction at Moscow hotel	10 bln rubles
	Renova Stroygroup	regional projects	5 bln rubles
	RGI International Limited	refinancing of Tsvetnoy Central Market shopping centre construction in Moscow	$150 mln
	Mezhdunarodniy Centr Development	completion of Mirax Plaza mixed-use centre in Moscow	$394 mln credit line
	Stroitel'naya Kompaniya Arban	construction of an office and hotel centre in Krasnoyarsk	1.24 bln rubles non-revolving credit line
	ALCON	construction of Alcon business centre at Leningradskiy Ave in Moscow	$110 mln 7-year credit line
	Tashir	acquisition and development of Raikin shopping and leisure centre	$220 mln
	Podolsk MLP	construction (phase II) of Podolsk MLP class A warehouse	$143.8 mln credit line
VTB	Gals-Development	project lending, debt refinancing for Gals-Development	credit line increased to 23.5 bln rubles
	Adamant	construction (phase II) of Continent shopping and leisure centre in St. Petersburg	44 mln euro non-revolving credit line
Gazprombank	City-Palace	construction of Evolution Tower mixed-use centre	$345 mln credit line
	Mirland Development	construction of Vernissage shopping centre in Yaroslavl'	$29.1 mln
	Stroitel	erection of Stroitel's objects	4.2 bln rubles credit line
KIT Finance	DVI Holding	completion of KomsoMALL shopping and leisure centre in Volgograd	1.65 bln rubles
Rosbank	Immofinanz Group	a loan for Shushary logistic centre	
Russkiy Capital	Dmitry Kulkov, Vladimir Razumnov, Vyacheslav Shikulov	partial financing of Vnukovo Outlet Village construction	$20 mln
Nordea Bank	AFI Development and Snegiri Development	refinancing of the $143-million credit line from MDM Bank to finance construction of Four Winds business centre	$170 mln
Nordea Bank jointly with Marfin Popular Bank	Finstroy	refinancing of completed shopping centres in Ufa and Lipetsk	1.1 bln rubles
UniCredit Bank	Hines	Dukat Place III business centre	$205 mln
Aareal Bank	Raven Russia	refinancing of logistic centre construction in Noginsk	$34 mln
Raiffeisen Bank	Immofinanz Group	refinancing of Fifth Avenue shopping centre	$55 mln
	Raven Russia	construction of class A warehouses in the towns of Klimovsk and Lobnya	$68 mln
	Tushino Complex	refinancing of Prazdnik mixed-use centre	$30 mln
	Gamma Invest Group	construction (phase II) of Europa shopping and leisure centre in Kaliningrad	$59.5 mln 10-year credit line

Source: Knight Frank Research based on data from open-access sources, 2012

Additionally, the banks started to study more closely their potential borrowers for their creditworthiness as well as to consider opportunities for the loan-based projects to generate cash flows supporting debt repayment. For example, if a project is for renting (a shopping mall or a office building), one of the requirements imposed by a creditor could be presence of preliminary rental agreements for a part of premises.

Nevertheless, many projects available on the market do not comply with standard requirements imposed by the banks. In particular, insufficiency of collateral for borrowing enough funds, interest grace period or nonstandard repayment schedule, rescheduling of earlier raised loans etc. would require that a creditor assumes higher risks and that a nonstandard approach is applied to transactions.

Such projects facilitated development of such credit instruments as mezzanine financing that are quite new for the Russian market. This approach helps organize lendings for risky investment projects and, as a rule, involves creditors sharing profit coming from the project financed, inter alia, via call options for a share in the project etc. For example, Mezhdunarodniy finansoviy club bank is increasing the share of mezzanine loans as one of its strategic initiatives for the next 5 years.

As to geographical distribution of financing in 2011, regional projects increased their share in total loans. This trend was primarily driven by the expansion of developers to the regions due to limited opportunities in Moscow.

In late 2011, the great degree of uncertainty on the global financial markets adjusted to the Russian capital market. Creditors were afraid of potential turbulence in global economy due to a number of open debt issues in Europe. Debt financing started to be offered to developers under stricter terms and conditions. In the reporting year, the cost of loans grew in the range of 100 basis points.

Supply and demand

Throughout 2011, strong investment activity on the commercial real estate market was observed. As a result, total volume of commercial real estate acquisition transactions nearly doubled over 2010 and exceed $8 bln. The average transaction value also grew with an almost 50% share of more than $100 mln transactions (against 30% in 2010). More available financing contributed a lot to this growth.

An undoubtedly positive trend was that foreign investors returned to the Russian market. The post-crisis period of 2009-2010 only witnessed incidental involvement of non-Russian companies but in 2011 foreign capital was involved in over 33% of all the transactions made. Foreign investors' increased activity was partially caused by a lot of deferred demand that was previously accumulated.

What is worth mentioning is that major institutional investors prevailed. In particular, Hines closed its transaction to purchase a number of objects: a warehouse in Khimky and Gogolevsky business centre.

Investment -attractive objects are still in short supply in all market segments. As a result, now investors are more focused on development projects and lower quality assets.

Major characteristic of the market in 2011 was high level of investments' differentiation by segments. . Investments were equally split between the retail and office segments with each of them accounting for 40%. Investors were traditionally less focused on hotels and warehouses (13% and 7% respectively). As to the Moscow market, the office segment maintained its championship in terms of total volume of transactions. This deviation came from a wide range of supply of investment-attractive retail objects on the regional markets.

Office real estate

Traditionally high attractiveness of office real estate for investments largely comes from its greater transparency and predictability in comparison to other market segments. It is worth mentioning that unlike crisis period when objects were sold by great discount, in 2011 developers are selling their objects at market prices. Some of developers plan to reinvest funds to new projects.

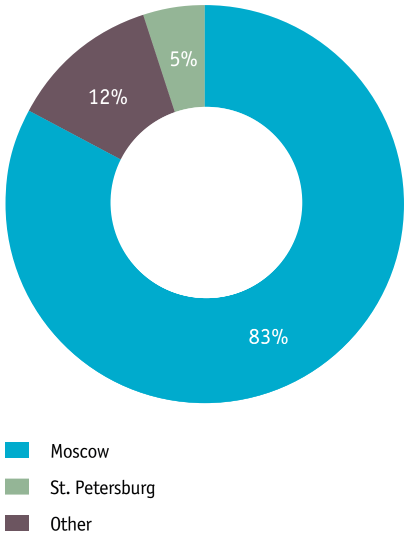
Most notable transactions are: acquisition of Coalco share by VTB Capital (some 47%) in two business centres: Belaya Ploschad' and Beliye Sady.

Construction activity and a steady renters demand contributed to rental rates growth throughout 2011. By the end of the year, office rental rates stabilized averaging $825 and $480 per sq m per annum (up 10% and 6% year-on-year) for classes A & B respectively.

Retail real estate

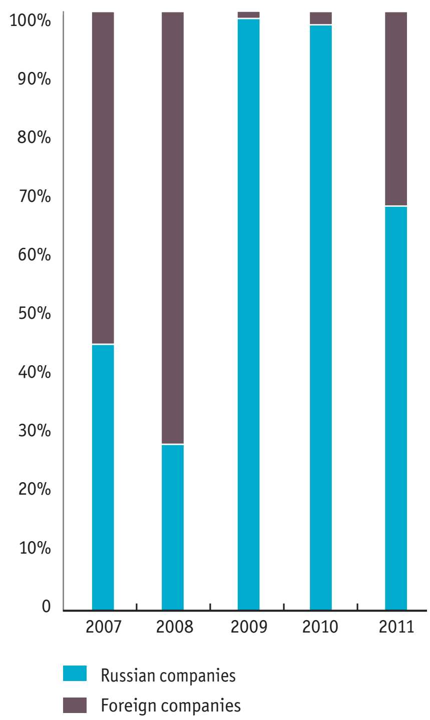
Total investments in retail real estate increased tenfold with the number of deals growing threefold only. This great difference between the greater transaction volume and total number of transactions made indicates that the average value of transactions grew substantially in 2011.

Moscow and St. Petersburg traditionally accounted for virtually all of the investments (95%)



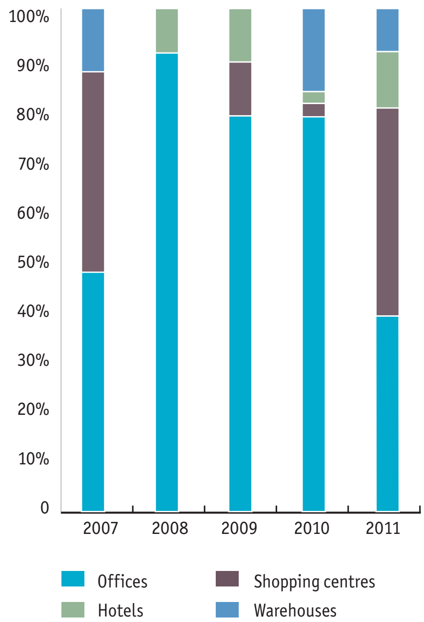
Source: Knight Frank Research, 2012

Foreign investors started to return to Russia in 2011



Source: Knight Frank Research, 2012

2011 witnessed a virtually equal split of investments in the office and retail segments



Source: Knight Frank Research, 2012

The largest deal at the Moscow market was acquisition by Kompleksnie Investicii of Gorbushkin Dvor and Filion shopping centres.

High investment activity in the segment was contributed by a number of factors: a lot of deferred demand accumulated during the post-crisis period, on the one hand, and quite a wide range of premises offered at the Moscow and regional markets, on the other hand. In particular, a number of St. Petersburg's milestone shopping centres changed their owners in 2011. For example, Jensen Group acquire one of the city's oldest shopping centres – Nevsky Passage. It's worth mentioning the imminent transaction involving sale of Gallerie shopping and leisure centre by Morgan Stanley that could become the largest deal in Russia.

However, Russian investors demonstrated greatest activity in the retail property segment in 2011. This came primarily from flexible profitability management of retail objects in comparison to other commercial real estate segments.

The decade's lowest figure for the supply growth of retail premises in Moscow in 2011 at the back of strong activity by retailers resulted reduction of vacancy rate to 2.5% and growth of rental rates by 12-14% on average.

Major office real estate transactions made in 2011

Buyer	Seller	Assets	Estimated Value
UFG Real Estate	Capital Group	Pushkinskiy Dom business centre, Concord business centre	$243 mln
VTB Capital	Coalco	share in Belaya Ploschad' and Beliye Sady business centres	$675 mln
Heitman European Property Partners	Capital Partners	A building at Metropolis mixed-use centre	$200 mln
Hines Global REIT	Fleming Family	Gogolevsky business centre	$96 mln
O1 Properties	VTB Capital	Capital Plaza	$210 mln

Source: Knight Frank Research based on data from open-access sources, 2012

Major retail real estate transactions made in 2011

Buyer	Seller	Assets	Estimated Value
Tashir	Opin	Raikin shopping and leisure centre	$220 mln
Fort Group	-	Macromir and all of its assets	$650 mln
Kompleksnie Investicii	MTZ Rubin	Gorbushkin Dvor shopping centre, Filion shopping centre	$450 mln
BIN	MCG and Z-Build	Kaluga shopping centre	$190 mln
Romanov Property Holdings Fund	-	Dream house	$100 mln
Jensen Group	VTB Capital	Nevsky Passage shopping centre	$80 mln
RMB Invest	Capital Group	3 Metromarket shopping centre	$117 mln
UFG Real Estate	Capital Group	Metromarket shopping centre	$57 mln

Source: Knight Frank Research based on data from open-access sources, 2012

Warehouse real estate

Total volume of investment transactions covering warehouses is substantially lower than in other segments of the commercial real estate market. Nonetheless, foreign investors appear to be highly interested in warehouse objects: over 80% of all the transactions were made with foreign capital involved. No other segment can boast similar performance. For example, in the first half of 2011, minority shareholders of Giffels – Van Riet Capital and Latidge Investments Limited – acquired Yuzhniye Vrata logistic centre.

The warehouse market witnessed a number of records set in 2011: the lowest volume of new warehouse area commissioned (370,000 sq m in Moscow and Moscow Region) and the highest absorption volumes (1 mln sq m) over the past 5 years. As a result, vacant area available dropped dramatically with 0.2% for class A premises, and rental rates (triple net) achieved $130-135 per sq m per annum.

Major characteristics of 2011 is activization of demand for design & build (build-to-suit) warehouse objects (Knight Frank consulted the largest transaction of this kind ever made – over 50,000 sq m of total area).

Major warehouse real estate transactions made in 2011

Buyer	Seller	Assets	Estimated Value
Hines Global REIT	AIG European Real Estate Partners	Warehouse object in the town of Khimky	$80 mln
Minority owners of Giffels Management Russia	Karta Realty Limited	Yuzhniye Vrata	$90 mln
Raven Russia	Espro	Vostochniy	$148 mln
Raven Russia	Espro	Kulon Pulkovo	$43 mln
Dixi	PNK Group	Multifunctional warehouse	$83 mln
Centre Obuv	PNK Group	Warehouse object	$68 mln

Source: Knight Frank Research based on data from open-access sources, 2012

Major hotel real estate transactions made in 2011

Buyer	Seller	Assets	Estimated Value
Gals-Development	Intourist	Pekin	$70 mln
Mikail Shishkhanov	Moscow Government	Moscow hotel (49% Dekmos)	$150 mln
Smart Finance Group	Moscow Government	National	$150 mln
Verniy Capital	Capital Partners	Ritz Carlton	$600 mln
Regional Hotel Network	Izhevsk Hotel	Park Inn Hotel in Izhevsk	$23 mln

Source: Knight Frank Research based on data from open-access sources, 2012

Hotel real estate

The Moscow Government played a significant role for investments on the hotel market in 2011. As part of the plan to privatize non-core assets, a number of the city's milestone hotels were sold, including Moscow and National hotels.

In 2011, total supply grew by 1,150 rooms via commissioning of 8 hotels. However, room rates grew throughout the reporting year (in the range of 7-15% in various segments) contributing to room profitability (in the range of 9-16% in various segments). As a result, the average room rate amounted to $320, $200 and $120 for 5-, 4- and 3-star hotels respectively.

OVERVIEW

Europe
Austria
Belgium
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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

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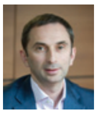

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Established in London more than a century ago, Knight Frank is the renowned leader of the international real estate market. Together with Newmark Company, Knight Frank's strategic partner, the company encompasses 244 offices in 43 countries across six continents.

Knight Frank has been a symbol of professionalism for tens of thousands of clients all over the world for 116 years. After 16 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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