OVERVIEW

Q3 2011

INVESTMENT MARKET

Moscow

Knight Frank

EXECUTIVE SUMMARY

- There was moderate positive trend in terms of lending to the construction sector in Q3 2011.
- Investment activity remained at the high levels observed since the beginning of 2011. International investors' activity rose significantly - foreign capital accounted for 44% of total transactions on the commercial real estate market in nine months of 2011.
- Retail kept its leadership among commercial real estate segments by levels of investment, mainly it was due to large volume of transactions typical for the segment.

INVESTMENT MARKET OVERVIEW

Main indicators

Segment	Office		Shopping centres	Warehouse		Hotels[1] 3-5★
Class	A	B		A	B	
New supply, thousand sq m,	51.1	141.2	—	91.5	—	—
Change, %	↑ (+2.2%)	↑ (+1.5%)	=	↑ (+2.1%)	=	=
Vacancy rate, %;	13.3%	18.3%	2.5%	0.6%	4.5%	66.7%
Change from Q2, p.p	↓ (-1.2 p.p.)	↓ (-0.9 p.p.)	↓ (-1.0 p.p.)	↓ (-2.4 p.p.)	↓ (-1.5 p.p.)	↓ (-1.3 p.p.)
Rates, $ per sq m per annum;	835	480	100-500 / 700-4,000[2]	130-135	100-120	167
Change from Q2, %	↑ (+2.4%)	↑ (+2.0%)	↑ (+5.0%)	↑ (+2.2%)	↑ (+4.8%)	↑ (+11.8%)
Yield[3] , %;	8.5-9.0%	10.5-11.0%	9.0–10.0%	10.0-11.0%	11.5-12.5%	12.0-13.0%
Change from Q2, p.p.	=	=	=	=	=	=
Average sale price, $ per sq m	6,500-8,000	4,500-6,500	3,000-7,000	1,200-1,400	600-800	200-1,000

[1] 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)
[2] Figures for anchor tenants and retail gallery operators
[3] Estimated cap rate
Source: Knight Frank Research, 2011

Evgeny Semyonov
Director of Investment and Sales

The third quarter of 2011 saw heightened interest of many commercial real estate market players in regional projects. Investors have been drawn to regional projects by a lack of investment-quality projects in Moscow, while developers have been motivated to seek opportunities outside the capital due to Moscow government policies, which have limited construction in the city.
Foreign investors are more conservative in their choice of investment projects, so their interest has stayed focused mainly on the Moscow and St. Petersburg markets.

Main events

- Moscow government plans to offer more than 700 lots (modestly-sized real estate assets and shares in investment contracts) for sale by the end of the year as part of its programme of municipal asset sales. The first lots for auction will be a part of Gostiny Dvor the Oktaybr cinema on Novy Arbat street and municipal stakes in the International Trade Centre and the Novinsky Passazh mixed-use complex.
- A number of transactions involving western investors were closed in Q3. The most significant were as follows:

*As of 10 October 2011 the 24.99% municipal stake in OJSC Novinsky Bulvar, 31, which owns the Novinsky Passazh shopping and office centre, had been sold

Heitman European Property Partners fund acquired a building at the Metropolis mixed-use complex. This was the first transaction by the fund since it entered the Russian market in 2007.

Capital Group continued sale of various assets to amass cash for implementation of large projects. UFG Real Estate bought the Pushkinsky Dom ("Pushkin House") business centre as well as the Concord business centre and Metromarket shopping centre (both located in the same building), all from Capital Group.

One of the largest transaction on the Russian commercial real estate market promise to be the acquisition of SC Galereya in St. Petersburg by American bank Morgan Stanley. The deal is estimated at the level of $1.1 bln.

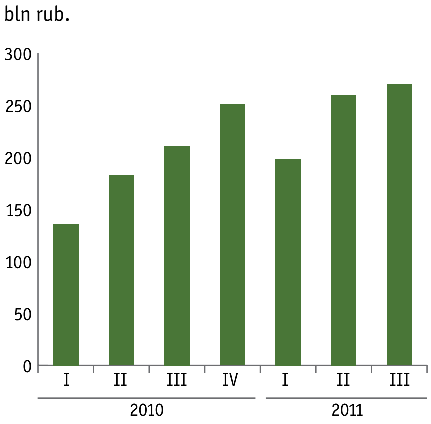
Financing

The first nine months of 2011 saw an upturn in lending. Total lending to the real sector of the economy in Q3 was 6475 bln rubles, which is 43% more than in the same period of 2010. The construction sector accounted for 5-6% of total lending to legal entities and to self-employed individuals in 2010-2011.

Borrowing increased in Q3 compared with Q2, but the rate of growth was much slower. This was primarily due to reduction of the money mass in Russia and also to stabilization of average bank interest rates at 8% following a period of steady decline.

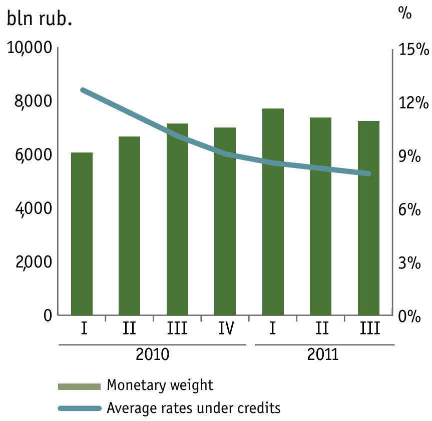
As before, large Russian and foreign banks are mainly financing projects that are already at an advanced stage of completion. A large share of lending is for completion of existing objects,

Lending to the construction sector continued to grow in Q3 2011, but the rate of growth was slower



Source: Knight Frank Research based on Central Bank data, 2011

Money mass and interest rates



Source: Knight Frank Research based on Central Bank data, 2011

Main transactions for financing/refinancing of commercial real estate projects in Q3 2011

Lender	Borrower	Purpose	Transaction details
Sberbank	Arban Construction Company LLC	Non-renewable credit line for construction of an office and hotel complex in Krasnoyarsk	1.24 bln rubles
	RGI	Refinancing of a loan for construction of the Tsvetnoy Central Market shopping centre in Moscow	$150 mln
	Tashir	Loan for purchase and development of the Raikin shopping and entertainment centre	$220 mln
	MLP Podolsk LLC	Credit line for construction of the 2nd phase of the class-A MLP Podolsk warehouse complex	$143.8 mln
VTB	Adamant	Non-renewable credit line for construction of 2 phase of Kontinent shopping centre	44 mln euro
Gazprombank	City Palace LLC	Credit line for construction of Evolution Tower mixed-use complex	$345 mln
	Stroitel	Credit line for financing and refinancing of construction projects Stroitel	4.2 bln rubles
KIT Finance Rosbank	DVI Holding Immofinanz	Credit for completion of onstruction work at the KomsoMALL shopping centre in Volgograd	1.65 bln rubles $70-72 mln
Russky Kapital	Dmitry Kulkov, Vladimir Razumnov, Vyacheslav Shikulov	Partial financing for construction of Vnukovo Outlet Village	$20 mln
UniCredit Bank	Hines	Credit line for the Ducat Place III business centre	$205 mln
Nordea Bank with Marfin Popular Bank	Finstroy	Refinancing of completed shopping centres in Ufa and Lipetsk	1.1 bln rubles
Nordea Bank	AFI Development and Snegiri Development	Refinancing of a $143 million credit line at MDM Bank for construction of the Four Winds business centre	$170 mln

Source: Knight Frank Research based on open-access sources, 2011 construction of second phases and project refinancing. New and small-scale companies, development projects had to attract funding on less favourable terms, which consecuently reduce the business profitability. Some of them don't sustain the competition and leave the market. sThis led to the exclusion from the market of weak players and consolidation of the construction sector among the major real estate developers and banks.

As for the territorial distribution of financing, there has been an increase in the share of regional projects in total lending. This is because many developers have reacted to limited opportunities in Moscow by expanding their business in regional cities.

Supply and demand

Investment activity remained at high levels in Q3 and total investments in the first nine months of 2011 were nearly double their level in the same period of 2010.

Increased activity by international investors was a defining feature of commercial real estate investments in Q3. A number of transactions involving foreign capital were closed in the third quarter, including purchase by Heitman European Property Partners of a building in the Metropolis multi-use complex in Moscow from Capital Partners.

Foreign capital represented 44% of the value of transactions in the first three quarters of 2011. In view of the traditionally conservative approach of western investors, this points to lowering of risks on the Russian commercial real estate market and its increasing attractiveness on global capital markets.

During the first nine months of 2011 the share of the Russian capital sank to 63% in total transaction volume, while in 2009-2010 more than 90% of investments were in Moscow.This was accompanied by substantial growth in the share of St. Petersburg, which accounted for 34% of total commercial real estate investments in the first three quarters of 2011. Investors also showed interest in other regional cities (acquisition by DVI Group of the project for construction of the KomsoMALL shopping centre in Irkutsk is one example).

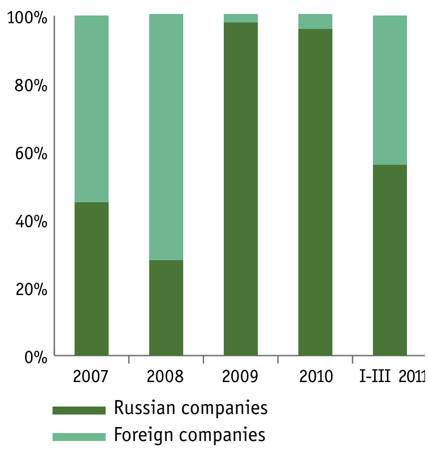
Retail remained the most attractive commercial real estate segment in Q3: its share increased by 7 p.p. in comparison with the first quarter and reached 50% of total investments in commercial real estate.

Office real estate

Relatively low volume of investment transactions in the office segment was mainly due to shortage of quality projects capable of attracting investors, although foreign funds showed some interest in the segment. Heitman European Properties closed acquisition of a building at the Metropolis business centre and UFG Real Estate bought two business centres (Concord and Pushkinsky Dom) from Capital Group.

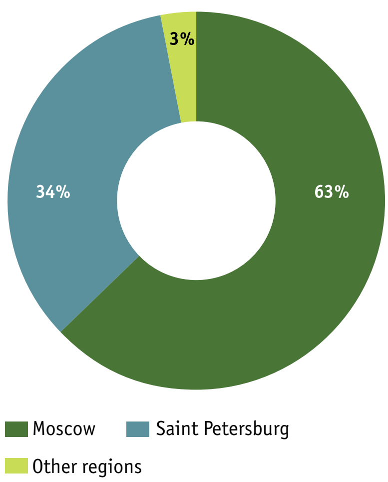
Growth of supply remained sluggish: about 620,000 sq m of new quality office space came onto the market in nine months of 2011. Demand was relatively strong at about 650,000 sq m, according to preliminary estimates. We expect some slowdown in growth of demand and stabilization of rental rates if the current economic uncertainty continues to prevail.

The market is moving back to the situation in 2007-2008, when more than half of transactions represented foreign capital



Source: Knight Frank Research, 2011

The share of Moscow in total commercial real estate investments declined significantly in the first nine months of 2011



Source: Knight Frank Research, 2011

Retail real estate was in first place by level of investments in nine months of 2011

Source: Knight Frank Research, 2011

Retail real estate

Transaction volumes in the retail segment exceeded $3 bln in the first nine months of 2011, representing about 50% of the total value of commercial real estate transactions in the period. The largest transaction for three years was closed in the third quarter of 2011 when Morgan Stanley investment bank bought the Galereya retail and leisure complex in St. Petersburg. Investor activity on the Moscow market was also intense: Tashir Group bought the Raikin shopping and leisure centre in Marina Roshcha district and UFG Real Estate acquired the Metromarket shopping centre. A number of other large transactions are also being finalized at present, several of which concern street retail.

The retail property market in Moscow is still experiencing very low levels of new supply. No shopping centres were opened in Q3 2011. Rapid expansion by retail operators has therefore led to a shortage of retail space in Moscow, which is confirmed by lowering of the vacancy rate to 2.5%.

Hotel real estate

Investor interest in the hotel segment was significantly greater during the first nine months of 2011 than in the same period of 2010. Market development has been supported by the policy of Moscow city hall, which is selling off its non-core assets. City hall's share stake in OJSC Dekmos, which is rebuilding the Moskva hotel, was sold in Q3 2011 and city stakes in various hotels – the National, Radisson SAS Slavyanskaya, 30% of shares in the Hilton Leningradskaya, and other assets – will be offered for sale in the near future.

Hotels continued to show strong operating indicators in Q3. Total supply grew by 770 rooms in nine months of 2011 despite postponement of several scheduled openings. This is a relatively high rate of growth for the Moscow market, although it is below the rates achieved in 2010. We expect the positive trends to be continued in coming months, although some slowdown is possible.

Main office real estate transactions in Q3 2011

Seller	Buyer	Assets	Transaction value (estimate)
UFG Real Estate	Capital Group	Pushkinsky Dom and Concord business centres	$243 mln
Orco property	Radishchevsky BC	—	
Sutton Holdings Limited	Moscow city Hall	25% of shares in Novinsky Passage	$47 mln
01 Properties	—	Evokom Plaza	$25 mln

Source: Knight Frank Research based on data from open-access sources, 2011

Main retail real estate transactions in Q3 2011

Buyer	Seller	Assets	Transaction value (estimate)
Romanov Property Holdings Fund	—	Dream House	—
Morgan Stanley	—	Galereya S&EC	$1.1 bln
DVI Group	Retail quarter - Irkutsk	Project for construction of the KomsoMALL SC	$80 mln
Tashir	Opin	Raikin shopping and entertainment centre	$100 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, 2011

Main hotel real estate transactions in Q3 2011

Buyer	Seller	Assets	Transaction value (estimate)
Mirtek Group	Rosatom	Baikal hotel	$13.8 mln
Individual buyer	Moscow city hall	Moskva hotel (49% of OJSC Dekmos)	$150 mln
Individual buyer	-	Rus hotel in Svetlogorsk	$8 mln
Regional hotel chain	Izhevsk Hotel LLC	Park Inn hotel in Izhevsk	$23 mln

Source: Knight Frank Research based on data from open-access sources, 2011

Warehouse real estate

Investors in a large number of transactions in the third quarter of 2011 were end-users. Two transactions were closed involving large Russian retail companies, which invested their own money in construction of warehouses designed and built to meet their specific needs (build-to-suit). PNK Group was the developer in both cases.

Foreign investment funds are studying investment projects. Raven Russia plans to invest in construction or purchase of warehouses, and the American fund Hines Global REIT has announced its intention to acquire the PNK-Chekhov warehouse complex . Value of the complex is estimated at $450 miln.

Warehouse property is currently in short supply: vacancy in the class-A segment had fallen to 0.5-1% by the end of Q3. About 770,000 sq m of new space is scheduled to open in 2012, but new properties are already 70% let to tenants before opening.

Forecast

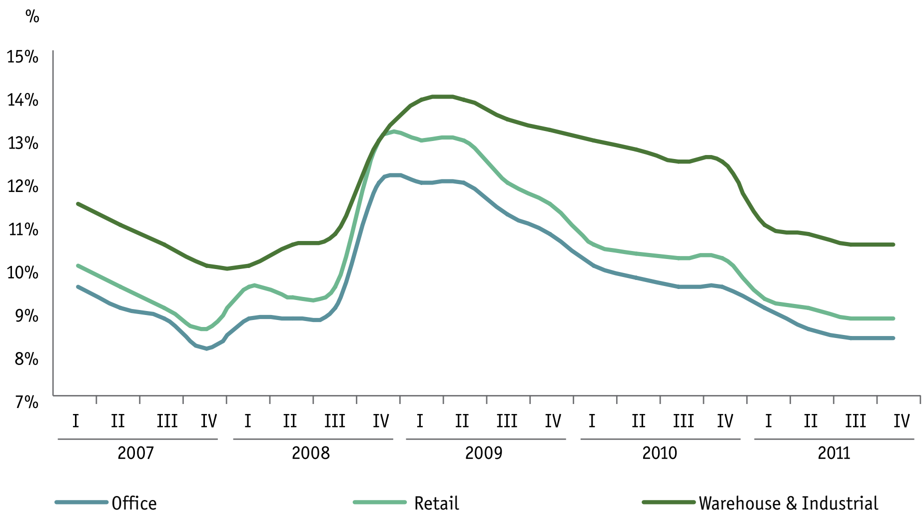
We expect commercial real estate investments to exceed $7 bln 2011, which will be a record level for the Russian market. If various transactions now at the negotiation stage are completed in Q4, the share of foreign capital could rise above 50% of the value all transactions in 2011. However, the uncertain economic climate and high levels of volatility on world financial markets can inhibit expansion of investment market in 3-6 months term.

Main warehouse real estate transactions in Q3 2011

Buyer	Seller	Assets	Transaction value (estimate)
Dixy	PNK Group	Multifunctional warehouse (44,000 sq m total space)	$83 mln
Large retailer	PNK Group	Warehouse complex (50,000 sq m total space)	—

Source: Knight Frank Research based on data from open-access sources, 2011

Cap rates in commercial real estate segments will remain at 3Q levels until the end of 2011



Source: Knight Frank Research 2011

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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 243 offices in 43 countries across six continents.

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