OVERVIEW

2011

OFFICE REAL ESTATE MARKET REPORT

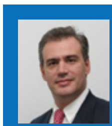
Moscow

Knight Frank

GENERAL TRENDS

- As of the end of 2011, total supply of the quality office premises virtually reached 12 million sq m. Supply of Class A and B premises has grown by 720 thousand sq m which is the lowest value over the past 7 years.
- By the end of 2011, absorption of Class A and B office premises totaled about 1 million sq m (excluding the extension of the existing agreements). This is slightly more than in 2010 but a positive trend could be noted as the absorption in 2010 was based primarily upon delayed demand.
- In 2011, rental rates for Class A and B offices rose by almost 10% and 6% respectively. This growth peaked in the first half of the year with fears of crisis starting to spread throughout Europe in autumn. Nonetheless, the fourth quarter appeared to be traditionally active accounting for some 40% of all the transactions made in 2011. We do not expect any significant reduction in demand, and consequently, rental rates will remain stable in the next half-year with some potential for a slight growth.

OFFICE REAL ESTATE MARKET REPORT



Mikhail Ioannesyants,
Associate Director,
Office Real Estate
Department

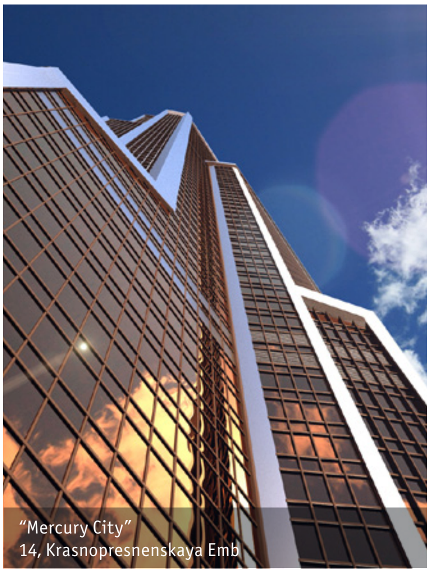
"In 2011, the office real estate market did not change a lot over 2010. A slight growth in supply and a steady demand from tenants and buyers of the office premises resulted in the decrease of the vacancy rate available (12.5% for Class A office premises). On the one hand, this is quite a low value to trigger the growth of the rental rates. On the other hand, this is sufficient to meet the demand coming from most tenants. Still, the range of large office blocks in the completed buildings is still highly scarce. Companies seeking for premises over 15 thousand sq m have no more than 5 options available. Today's demand is driven by the quality development of the market: a substantial share of the demand for Class A and B+ offices comes from companies leasing offices in the business centers of a lower class. In particular, major lease transactions made in 2011 involving "Kaspersky Lab", "Mail.ru", TEK "Mosenergo", "GroupM", "Renaissance Credit" appeared to be relocations to the office premises of a higher level. Also, major companies continue to consolidate their premises. Such examples would include transactions made by "GroupM", "Mail.ru" and "Credit Europe Bank".

We also note the better quality of the newly constructed office centers: property commissioned in 2010-2011 is of better quality than those completed in 2000-2005. However, the technical data disclosure process by owners leaves much to be desired; in this respect, we are well behind the western markets where the technical disclosure is more organized, thus making it easier for the tenants and buyers to make a decision".

Key indicators	Class A	Class B+	Class B-
The total volume of quality office space, thousand sq m		11,910	
including, thousand sq m	2,340 (+ 13%)*	6,410 (+ 5%)*	3,150 (+ 4%)*
Commissioned in 2011, thousand sq m		720	
including, thousand sq m	275	262	183
Vacancy rate,%	12,5 (-5 p.p.)*	17,2 (-3 p.p.)*	
Average rental rates **, $/ sq m / p.a.	830 (+9,2%)*	480 (+5,5%)*	
The range of rental rates **, $/sq m/ p.a.	650-1,200 (1,000 -1,300***)	350-650	260-400
Operating expenses, $/ sq m / p.a.	110-210	80 - 120	50-95

*Change compared to the end of 2010
** Excludes operating expenses and VAT (18%)
*** Range requested rents for premium space
Source: Knight Frank Research, 2012

BC "Citydel"
9 Zemlyanoy Val St



"Mercury City"
14, Krasnopresnenskaya Emb

Key Events

- In December 2011, the Federation Council of the Russian Parliament authorized the change of the borders between the city of Moscow and Moscow Region with effect from 1 July 2012. This initiative would mean a 2.4 times increase in the Russian capital's total area (up 148 thousand ha). The city of Moscow would take over an area spanning between the Warsaw and Kiev highways.

- Developers plan completion of the Moscow City project by 2015. The area to be rented there will account for nearly a half of all Class A area scheduled for commissioning in 2013-2015. The following projects are currently approaching completion: Mercury City, Central Yadro, Vostok Tower of the Federation complex, Evolution Tower as well as the multifunctional facility (sites 15 and 16). The Empire Tower was commissioned in 2011.

- As part of the effort undertaken by the Moscow Department of Cultural Heritage (Mosgornaslediye) to limit new construction in the centre of Moscow, over 200 investment contracts were cancelled for a total of some 2 million sq. m, including 1 million sq m of office premises. Permits to break buildings in the centre of Moscow issued earlier were checked with 224 of them suspended.

- Investments in commercial real property grew by 86% in 2011 to \$8.2 billion compared to \$4.4 billion in 2010. Office real property accounted for some U.S.\$3 billion.

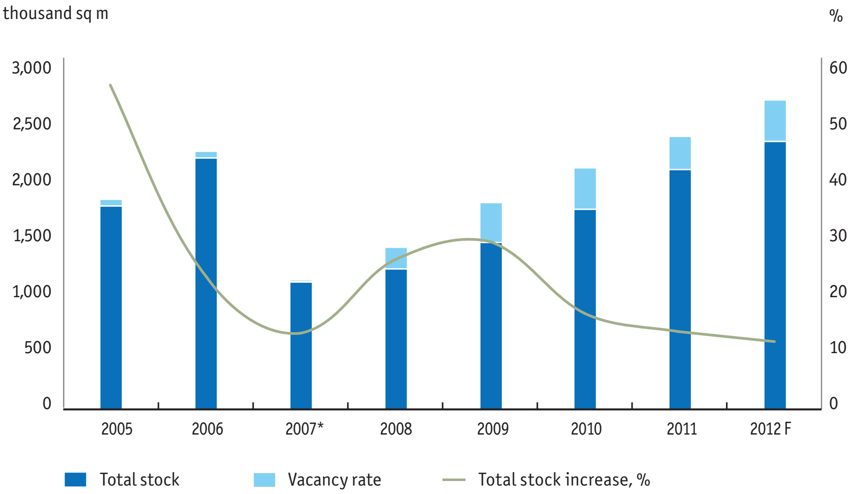
Supply

As of the end of 2011, total supply of Class A and B office premises in Moscow stood at 2.3 million sq m and 9.53 million sq m respectively. The supply growth rates have been decreasing over the past three years. In 2007, supply grew by 20-25% as compared to only 13% and 5% (275 thousand sq m and 445 thousand sq m) in 2011 for Class A and B respectively.

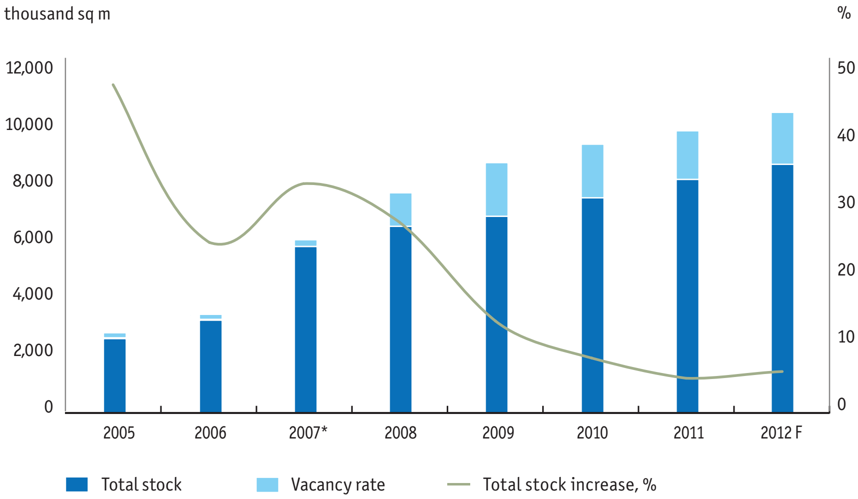
The two key drivers for the reduction of new construction volumes are the decrease in the activity coming from developers in 2008 (as it takes 3-4 years to complete an office centre, this is the key driver for the low growth rate in supply in 2011-2012) and the new policy of Moscow government. Revision and cancellation of a number of investment projects, an initiative to change the terms of lease of land for development, a ban on construction within the Third Transport Ring Road, the change of the borders between the city of Moscow and Moscow Region, and potential relocation of the authorities from the centre of Moscow – all those arrangements caused revision of existing plans and delays of new projects.

Office premises continue to grow moderately

Class A



Class B



*In 2007, office premises underwent a reclassification process, and about 1.8 million sq m of Class A property were degraded to Class B. The growth rate for 2007 does not take into account those premises.

Source: Knight Frank Research, 2012

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In the next three years, we expect a number of large Class A office centers to be delivered to the market. Developers plan completion of new Class A premises to be completed within the Third Transport Ring in 2014-2015 (with some rare exceptions).

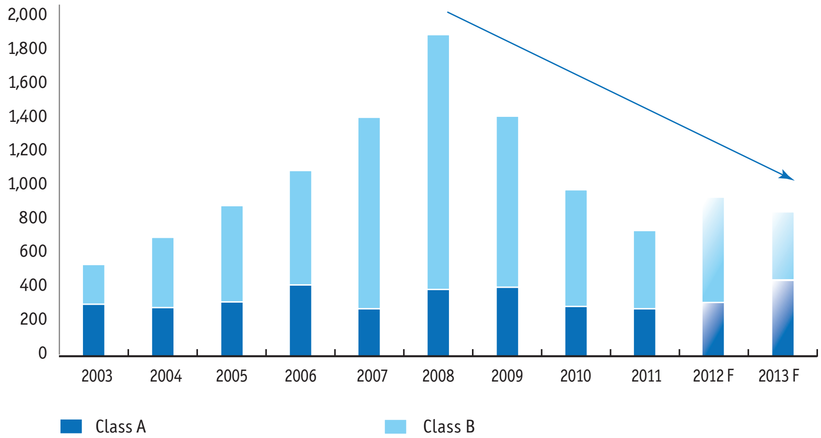
Demand

Demand for Class A and B office property remained strong throughout 2011. In autumn 2011, fears emerged that a second wave of the global economic crisis was expected but those hardly affected the demand. A traditionally high level of business activity was observed: the fourth quarter accounted for about 40% of all the transactions made during the year. Absorption totaled about 1 million sq m in 2011 (this does not include extension of existing agreements). This is comparable to the 2010 value when the bulk of all the absorption came from deferred demand originating from 2008-2009. In 2011, the deferred demand was hardly in place meaning that actual growth of current demand took place.

As office premises are leased in Moscow for 5 years on average, most of the tenants who entered into lease agreements in 2007 (when a record level of absorption was registered) used the year of 2011 for considering other rental opportunities. Alongside with that, most tenants extended their current agreements, partially due to no more appropriate options available. In particular, agreements were extended by the tenants of the office premises at such milestone business centres as "Krylatskiye Hills", "Dukat III", "Lesnaya Plaza" and "Aurora Business Park".

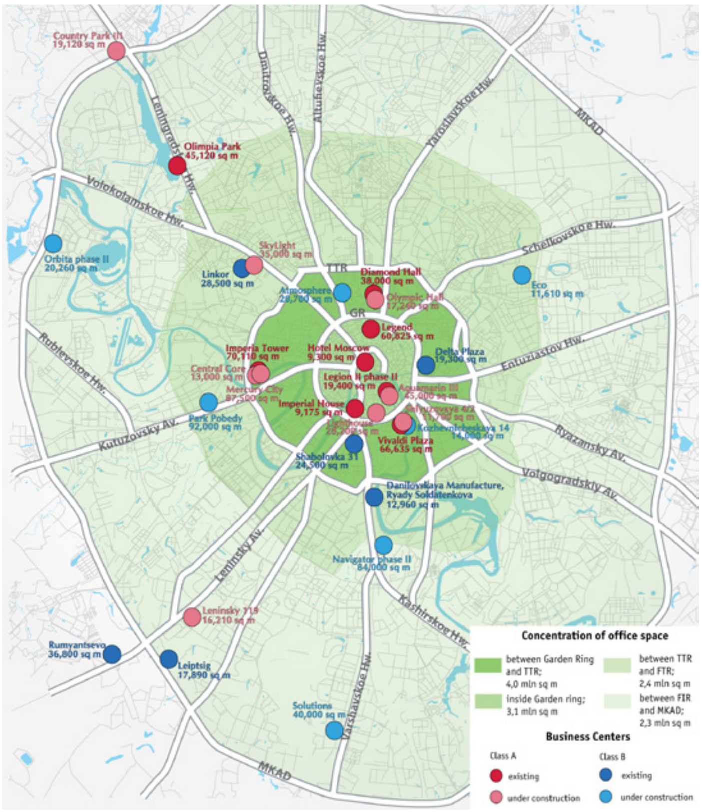
The delivery of the office premises is expected to remain on the low levels, but in 2012-2013 it will be higher over 2011

thousand sq m



Source: Knight Frank Research, 2012

Map of projects commissioned* in 2011 and scheduled for commissioning in 2012. Office premises concentration in Moscow



*Office centres having their Commissioning Certificates received in 2011. Buildings are classified according to the model adopted by the Moscow Research Forum.

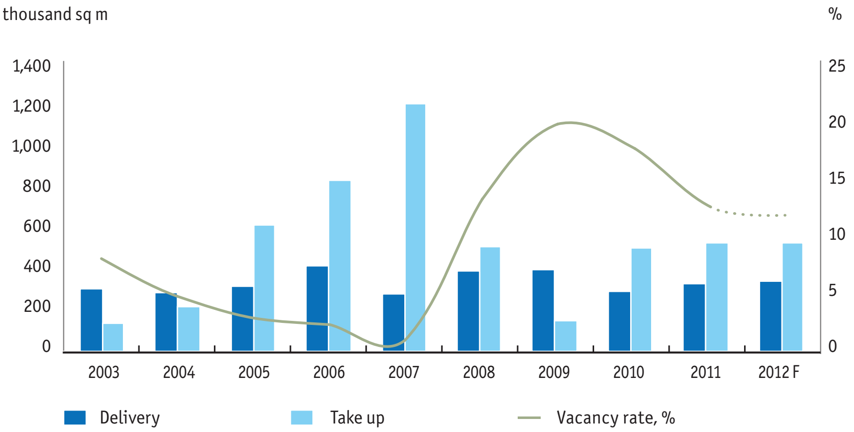
Source: Knight Frank Research, 2012

There has been a steady decline in the share of vacant area with 12.5% and 18.3% for Class A and B premises respectively. However, should no economic turbulence takes place and in terms of the low delivery, there will be a potential in the nearest future for a substantial growth in the rates.

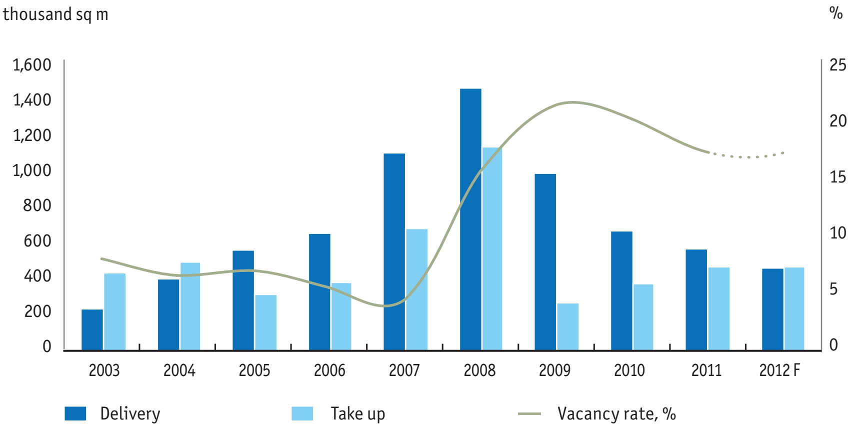
The office premises tenants' profile changed in 2011: oil and gas companies reduced their share, and demand from financial institutions as well as IT and telecommunication companies became stronger.

As compared to December 2010, the share of vacant area dropped from 17.4% to 12.5% for Class A and from 20.1% to 17.5% for Class B due to robust demand and insignificant volumes of new construction

Class A

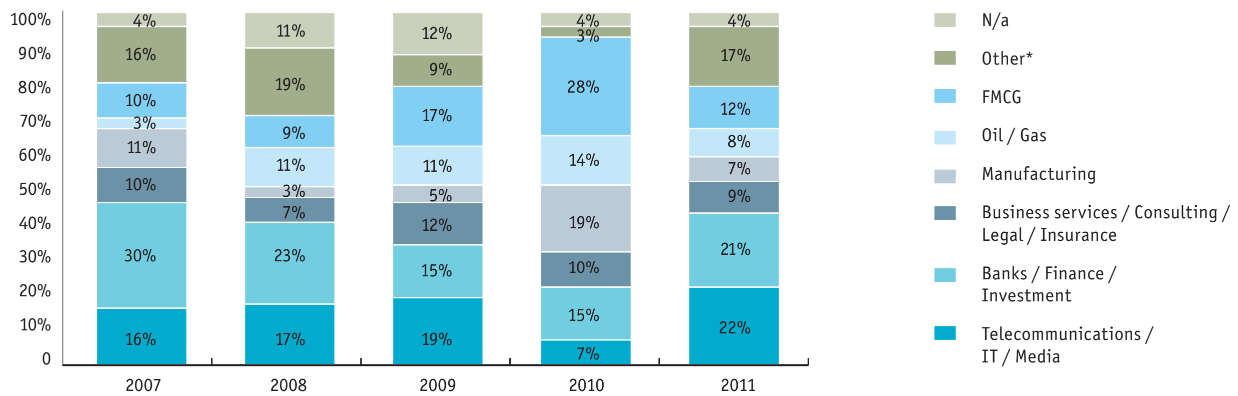


Class B



Source: Knight Frank Research, 2012

Financial institutions as well as IT and telecom providers are expanding their share in total absorption volumes; the share of consumer goods producers and manufacturers is reducing



*marketing, construction, retail, automotive, logistics

Source: Knight Frank Research, 2012, according to the data on transactions closed by the major consulting companies: CBRE, Colliers International, Cushman & Wakefield, JonesLang LaSalle, Knight Frank

Ключевые сделки 2011 г.

Tenant / buyer	Volume of the deal, sq m	Property Address	Property Name
Lease			
Mail.ru	29,930	39 Leningradsky Ave	SkyLight
Kaspersky Lab	29,840	39 Leningradsloe Hwy	Olimpia Park
Russian Argicultural Bank*	27,500	1 Arbat St	Alpha Arbat Centre
Sberbank	19,900	8 Novodanilovskaya Emb	Danilovsky Fort
Grinatom	13,500	8 Paveletskaya Emb	AFI na Paveletskoy
Morton	11,520	8 Preobrazhenskaya Sq	Preo 8
Group M LLC*	10,800	2 Tsvetnoy blvd	Legend
Renaissance Credit*	10,680	12 bld 1A Dvintsev St	Dvitsev
		8 bld. 1 Presnenskaya Emb.	Capital City
Schneider Electric	8,680	12 bld 1 Dvintsev St	Dvitsev
Credit Europe Bank*	7,620	12/16 Olimpiyskiy Ave	Diamond Hall
MRSK	7,600	4 2nd Yamskaya St	Nevskiy Dom
"Bud' Zdorov» (Ingosstrakh medical chain)*	7,400	12 Suschevskiy Val	Ocean Plaza
End-use purchase			
Federal Grid Company	40,000	4 Belovezhskaya St	Western Gate
Rusal	28,120	1 Vasilisy Kozhinoi St	Park Pobedy
VTB	about 16,000	13 bld 1 Krasnopresnenskaya Emb	Federation tower East
Unicreditbank	11,680	18 bld 1 Andropova Ave	Nagatino i-Land
Investment purchase			
Marnis Group	70,000	22 Andropova Ave	Nagatinskiy
O1 Properties	about 50,000	4 4th Lesnoy passage	Lesnaya Plaza
UFG Real Estate	about 40,000	9 Strastnoy Blvd	Pushkinskiy Dom
		10 Shabolovka St	Concord
PSN Group	37,000**	1 Arbat St	Alpha Arbat Centre
Aliv M	12,200	50A/8 bld 2 Zemlyanoy Val	Sadko
VTB Capital	project stock	5 Lesnaya St	White Square
TPG Capital		27 Lesnaya St	White Gardens

*Knight Frank acts as a consultant of the deal
**Total area
Source: Knight Frank Research, 2012

Commercial Terms

During 2011, average rental rates for Class A and B office premises rose by almost 10% and 6% respectively up to $830 and $480 per sq m p.a. (triple net) respectively. The rates grew primarily due to the shortage of the premium properties in the central part of the city.

As it is now prohibited to construct new offices in the centre of Moscow, rental rates now start to vary more depending on the proximity to the Boulevard Ring.

Rental rates for the premium premises are in the range of $1,000-1,300 per sq m p.a. with even more expensive options available. Those could be found in the historical centre of Moscow as well the business area that emerged along Tverskaya St. London's West End is the only location in Europe where the rental rates are higher – about $1,530 per sq m p.a.

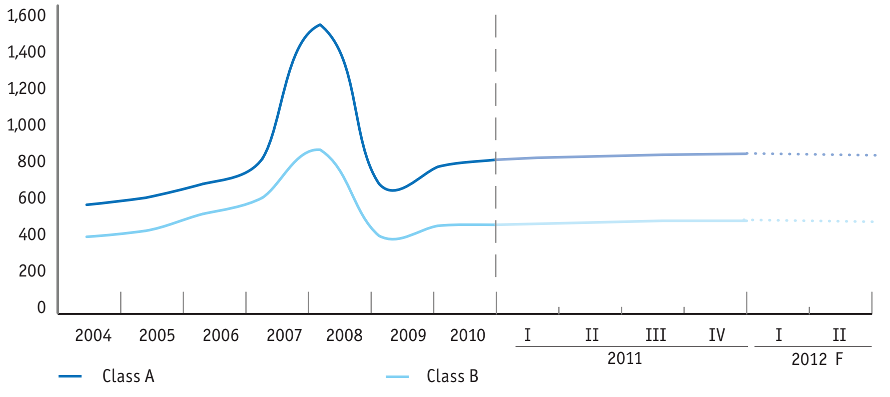
Rental rates for the mid-level office premises stood at $750-1,000 per sq m p.a. The low segment of Class A office premises ($650-800 per sq m p.a.) is represented by remote options as well as a number of sites commissioned recently with a high share of vacant area available.

In spite of the Moscow Government's initiative to relocate administrative centres to the so-called "new Moscow", most of the market players still tend to believe that infrastructural decentralization has a horizon of 20-25 years. In this connection, demand for premises in the central part of the city will remain traditionally high as long as the whole decentralization plan becomes clear and transparent.

As the office real estate market is greatly affected by the economic environment, many market players were concerned that demand and rental rates could drop by the end of the year. But that trend was only observed in a number of cases with the average level remaining flat.

Rental rate forecast, conservative scenario (as based on the forecast of the major economic indicators): the rates are expected to remain stable in the next six months

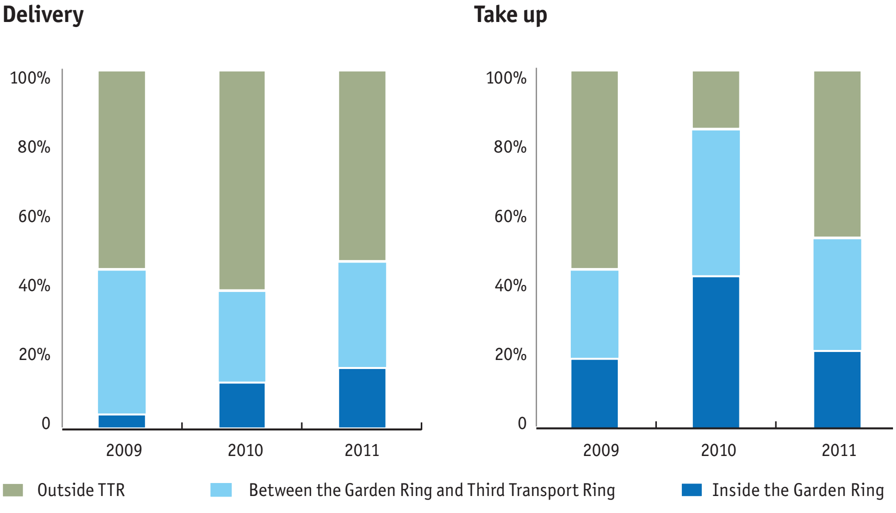
$ / sq m / p.a.



Source: Knight Frank Research, 2012

Office premises in the downtown are traditionally in a high demand while the new construction only available beyond the Third Transport Ring.
As it was not enough affordable supply in the centre of Moscow in 2011, the share of transactions beyond the Third Transport Ring Road grew

%



Office centres located on the outer side of the ring road belong to the submarket of the respective ring

Source: Knight Frank Research, 2012

OVERVIEW

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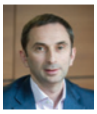

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Established in London more than a century ago, Knight Frank is the renowned leader of the international real estate market. Together with Newmark Company, Knight Frank's strategic partner, the company encompasses 243 offices in 43 countries across six continents.

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