



RESEARCH



2017 OFFICE MARKET REPORT

Saint Petersburg

HIGHLIGHTS

The level of vacant office space remained within 7-8% during the year 2017, going down less than 1 p. p. by the end of the year if compared to 2016.

The average asking rental rates demonstrated a steady increase. Class A business centres recorded the rental increase of 9%, Class B - 5% in the national currency at the end of 2017.

The take-up rates slowed down. The net take-up volume of 2017 amounted to 154,000 sq m - 29% less than in the previous year.

The total volume of lease transactions reached 120,000 sq m. The main demand for office space in 2017 was formed by IT and telecommunications spheres. This sector made a breakthrough by 25 p. p. in the share of premises leased for the year.

112,000 sq m of leasable premises were purchased for investment purposes and for the company's own needs during 2017. The figure was comparable to the results of the office real estate market in 2016.



Marina Puzanova
Head of Commercial Department
Knight Frank St. Petersburg

«The shortfall of quality office space became more and more apparent by the end of 2017 - there were cases when several clients put a claim for vacated premises and the landlord could choose the most interesting tenant for himself. The situation became more difficult for large customers: landlords of vacated space preferred not to wait for large tenants with their long-standing decision-making and approval processes, but divided the premises into smaller units and quickly let them. In this context, there was no significant rents increase observed, as tenants were still optimizing their costs, and the rent size was the main parameter in choosing an office. In 2018, we do not expect major changes: the rotation of tenants will continue, low delivery volume of new facilities will only partially meet the pent-up demand. Herewith, the choice will be very modest for discerning tenants wishing to move to the property of the highest quality: most of the newly constructed facilities intended for the lease market belong to Class B properties according to their characteristics.».

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Key Indicators. Dynamics*

	Class A	Class B
Total leasable area, thousand sq m	3,041	
including, thousand sq m	1,005	2,036
Changes against the end of 2016, %	6 ▲	4 ▲
New delivery in 2017, thousand sq m	143	
including, thousand sq m	58	85
Total vacant stock, thousand sq m	231 ▼	
including, thousand sq m	57	174
Vacancy rate, %	5.7 ▲	8.5 ▼
Asking rental rates in operating business centres, \$/sq m/year, incl. OPEX, net of VAT (18%)	242–380	121–311
Average asset-by-asset change of the rent in rubles in operating business centres, %	11 ▲	6 ▲

*Comparison with Q4 2016 results

Source: Knight Frank St. Petersburg Research, 2018

Supply

The total leasable area of quality offices in St. Petersburg exceeded the figure of 3 million sq m following the results of 2017. Its 5% increase was ensured by the delivery of more than 20 business centres in 2017, with about half of all facilities being built from scratch, while the rest approached the market after reconstruction.

The volume of offices entering the market in 2017 reached 143,000 sq m - an all-time low figure for 10 years, less by 41% than in 2016. A similar decrease occurred in 2010 due to developers' activity drop in 2008-2009 and

the excess of supply that existed for some time. However, more than 85% of new quality offices replenished the open lease market, and a third of new business centres enjoyed an occupancy rate of over 80% for the year.

The maximum quality supply volume in functioning business centres was concentrated in Moskovsky and Central districts. Whereas, Frunzensky, Kirovsky and Pushkinsky districts were least supplied with offices. Their total share did not exceed 6% of the total volume of premises for lease in St. Petersburg.

Key Events

The most notable event in the office market of St. Petersburg in 2017 was the trend of investment activity renewal, which was outlined in 2016. More than 10 purchase transactions of business centres were concluded over the year. The largest acquired business centres were Kellermann Center and Premium, which Raven Russia investment fund added to its asset portfolio; Aeroplaza, bought by Jensen Group; and Senator at 36, Moyka River Emb, which expanded the office real estate chain of Imperia Financial and Holding Company.

IT companies demonstrated the highest activity - the share of IT and telecommunications transactions in the overall structure of lease transactions in 2017 was 53%, while the share of oil and gas sector was significantly reduced till the level of 17% for the first time since 2013.

All transactions with an area of more than 5,000 sq m were completed either with the participation of IT companies or oil and gas companies. The Russian company Peter-Service, which developed solutions for the telecommunications business, leased 9,300 sq m in Smolensky business centre on Vasilievsky island and two IT companies were also accommodated in Megapark at 22, Zastavskaya St.

The purchase of the buildings of Lotos Tower multifunctional complex on Primorsky Avenue confirmed the high activity of IT and telecommunications sector on the office real estate market. The international company JetBrains, which created professional software development tools, bought two buildings to reconstruct them for office use and accommodation of its employees, which would expand the company's presence in St. Petersburg.

In 2017, it was reported that the construction project of a multifunctional office and shopping complex Sky City on the embankment of Obvodny Channel was sold to Chinese investors. A new permit for the construction of the complex was issued in November of last year.

Key Business Centres commissioned in 2017

Property	Business District	Class	Leasable office area, thousand sq m	Developer
Renaissance Business Park	Embankments with views	A	20.9	Renaissance Development
Reforma	North-Western	B	14.4	Euroauto
GRAFFITI (Kondrat'evsky Business Quarter)	Embankments with views	B	14	Splav Group of companies
Senator at Chapaeva (2nd phase)	Petrogradsky	A	13.4	Imperia Financial and Holding Company
Polis	South-Eastern	B	13.2	Polis Group of companies
Chkalovsky, 50	Petrogradsky	B	11.7	Tellus Group
Ponomarev Center	Central-1	A	8.5	Concern Piter
Business Centre at 10, Oktyabr'skaya Emb.	Eastern	B	6.4	Sinergia
Senator at Bolshaya Morskaya	Central-1	A	3.9	Imperia Financial and Holding Company

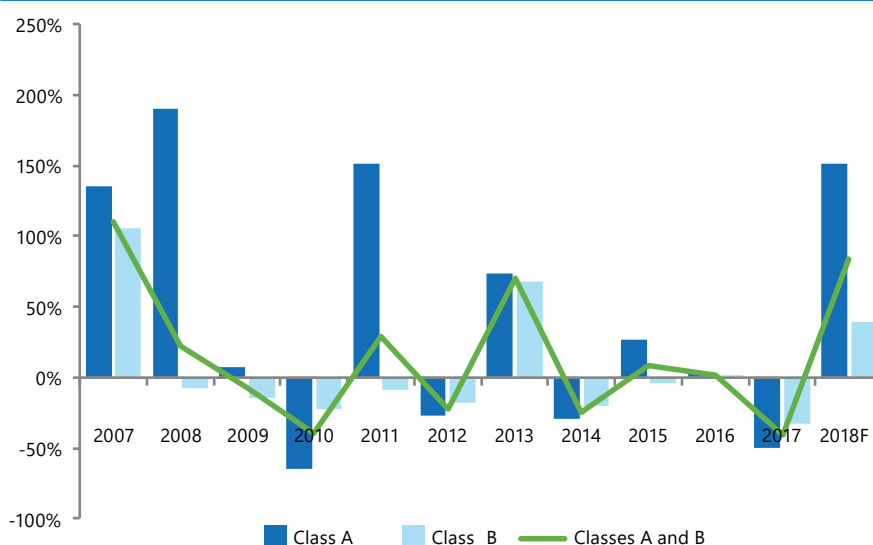
Source: Knight Frank St. Petersburg Research, 2018

Demand

The total net take-up amounted to 154,000 sq m by the end of the year - 29% lower than the similar level last year. It distributed in the districts the following way: Embankments with views business district strengthened its leadership position, which

was adopted already in H1 2017. This was due to the high occupancy level of several facilities that rose during the year, as well as the commissioning of a new business centre Renaissance Business Park, fully leased by Gazprom-pererabotka already at the construction stage.

Delivery dynamics by classes against the previous period, %



Source: Knight Frank St. Petersburg Research, 2018

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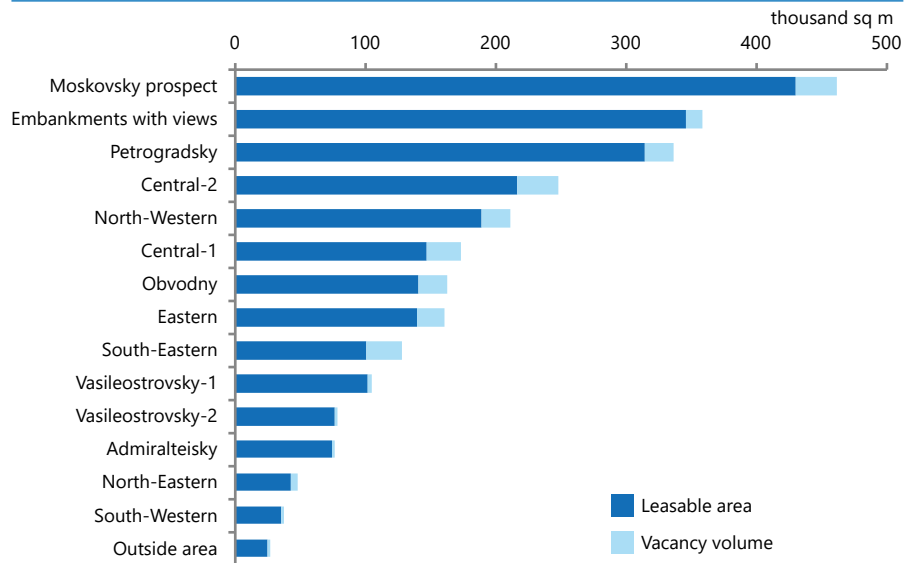
Remarkably, North-Western business district (district where Lakhta Center was to be accommodated) was also gradually gaining popularity: the take-up rate grew by 19.3 p. p. during the year.

At the end of the year, 231,000 sq m of office space remained vacant at the market, and most of them belonged to Class B (75%). During the year, the number of vacant Class A premises increased by 10%, which was the result of the entry of several quality properties to the market. This entry did not result in the reduction of the existing shortage of Class A premises. The office market responded to the lack of Class A offices by the decrease in vacant Class B premises by 7.8% compared to the same period in 2016. However, this decrease was not as large as it could have been expected: new supply in quite attractive locations for tenants had a chance to be fully or partially taken up, but there were a number of Class B facilities that had problems with occupancy due to the peripheral location or inappropriate lease terms. The total volume of lease transactions came up to 120,000 sq m, which was 45% less than in the same period last year. In general, there was a decrease in the average leased area by 39% in 2017 against 2016 results, the drop mainly occurred in Class A properties, where the average transaction size was the lowest for the last 5 years. The sphere of IT and telecommunications became the leader of tenants' activity in terms of the volume of leased space - 53%. In quantitative terms, about 30% of transactions were completed by the participants of this profile, while the average area of offices leased by IT companies was 73% higher than the market average. In 2017, oil and gas companies stopped dominating in the lease transactions - their share was reduced by 39 p. p.

Class B transactions prevailed in the structure of lease transactions - 76% of the total volume of implemented premises. Thus, the office market of St. Petersburg faced a high demand for quality Class A premises, which were in short supply, and partial replacement of the needs at the expense of lower-class premises.

Most of the tenants, who approached Knight Frank St. Petersburg in 2017, wanted to change their location and searched the fitted out premises in Central, Petrogradsky and Moskovsky districts. Interestingly, 66% of Class A and B office space was leased in these business districts in total according to the results of 2017. The main budget of requests varied between 1,100-1,200 RUB/sq m/month. The size of the rental rate, location, transport accessibility and parking availability were still the determining factors when choosing an office.

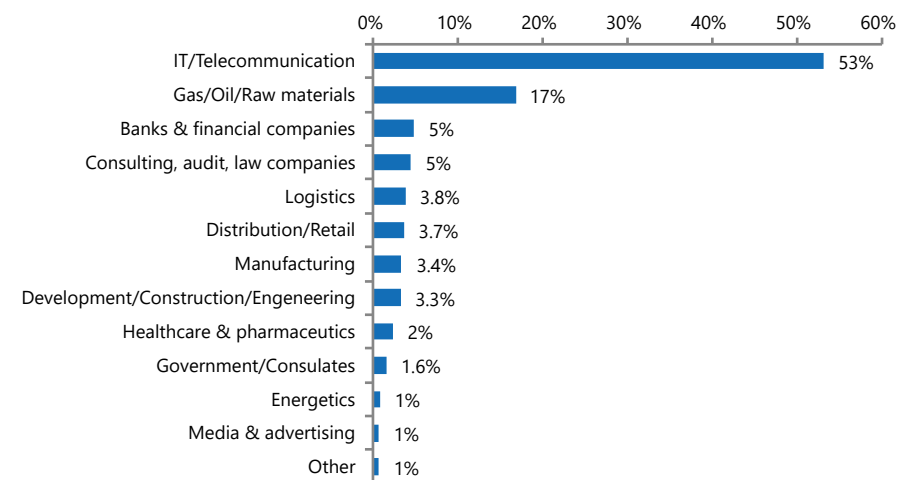
Distribution of the total volume and vacant office space by business districts in 2017, %*



*Excluding business centres for sale and own needs of companies

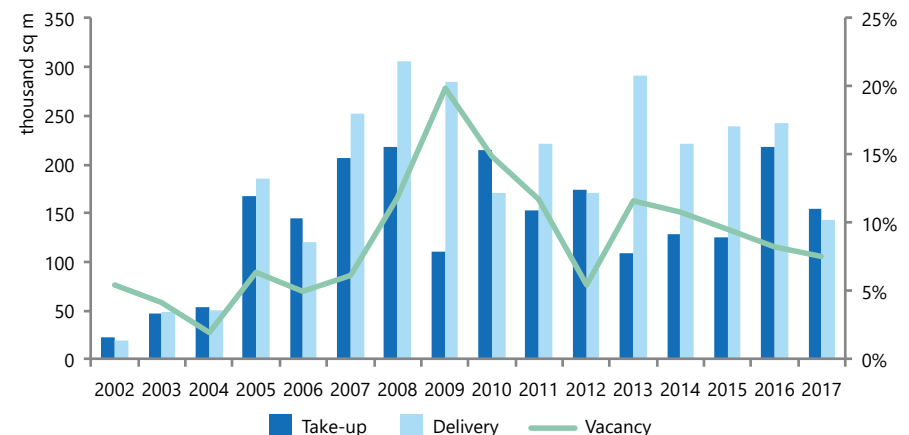
Source: Knight Frank St. Petersburg Research, 2018

Distribution of lease transactions by area depending on tenant profile, %



Source: Knight Frank St. Petersburg Research, 2018

Dynamics of delivery volume, take-up and vacancy share



Source: Knight Frank St. Petersburg Research, 2018

Commercial terms

The upward trend of rental rates was observed both in 2016 and 2017. The average rental rate for vacant space in Class A business centres was 1,835 RUB/sq m/month, in Class B business centres - 1,171 RUB/sq m/month, including VAT and OPEX. Compared to the end of 2016, the asset-by-asset increase of rents was 11% and 6% for both classes in rubles, respectively, such a growth in Class A properties was caused by the rental increase in 6 business centres of Vasileostrovsky district. Such reaction of landlords can be connected with the opening of the central part of ZSD (Western High-Speed Diameter), which improved the transport situation of the district.

The average Class A rental rate was registered at the level 317 \$/sq m/year and 203 \$/sq m/year including OPEX, net of VAT, increasing by 13,1% in Class A and 9% in Class B due to declining of US dollar against the ruble.

The declared average cost of an open parking lot was 5,301 RUB/parking lot/month and 8,018 RUB/parking lot/month for indoor parking by the end of 2017. The average rental rate for a parking lot rose by 8% in Class A business centres and went down by 6% in Class B properties, if compared with the results of previous year.

Rental rates dynamics from 2007*



*Incl. OPEX, net of VAT

Source: Knight Frank St. Petersburg Research, 2018



Ligovsky 266 Business Centre

Forecast

According to our estimates, about 263,000 sq m of office space for lease shall be added to the office real estate market in 2018. If so, the results of 2018 will be 84% higher than the results of 2017. Nevertheless, the office space in the multifunctional cultural and business complex Lakhta Center, designed for Gazprom's own needs, will hold a significant share of the delivery. Therefore, it is worth noting that, without taking into account this office

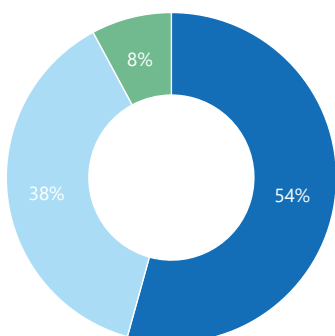
space, only 50% of the declared volume of new supply will be intended for the lease market. Moreover, the completion of all projects on schedule is unlikely due to a long period of implementation or zero construction stages, so the actual amount of new supply will hardly provide tenants with enough office space in 2018.

The downward trend of the vacancy rate by 1-1.5 p. p. will be strengthened on the

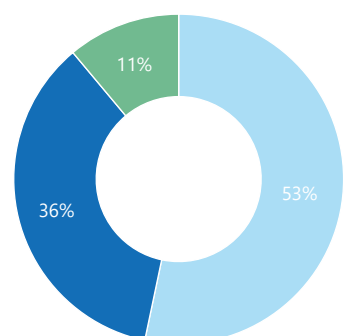
market in connection with the rotation of tenants as well as with slowing pace of construction and commissioning of new quality business centres in 2018. The shortage of quality supply and removal of large office units from the market in the short term will serve as prerequisites for further rental increase by 7-10%, since the vacation of office space, leased by Gazprom's structures and contractors, should be expected no earlier than 2019.

New supply distribution depending on the purpose, %

including Lakhta Center's leasable area



excluding Lakhta Center's leasable area



■ Intended for own needs of companies
■ Intended for lease
■ Intended for sale

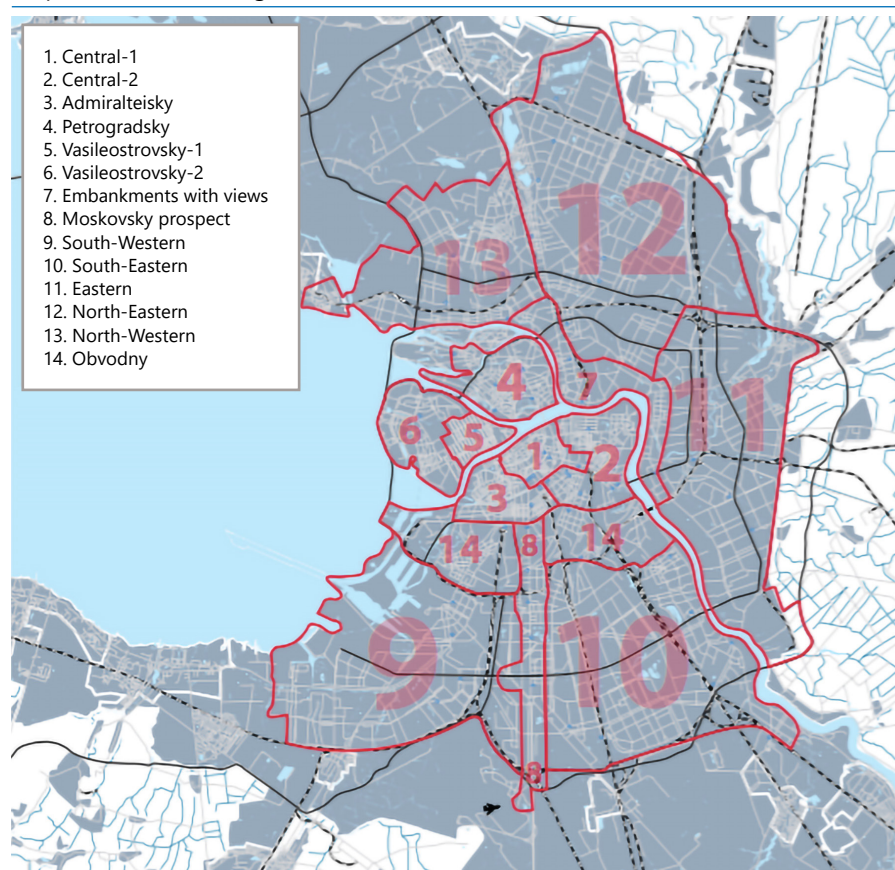
Source: Knight Frank St. Petersburg Research, 2018

Key properties to be commissioned in 2018

Property	Business district	Developer	Class	Leasable office area, thousand sq m
Lakhta Center (tower)	North-Western	Gazpromneft-Invest	A	75.3
Lakhta Center (multifunctional building)	North-Western	Gazpromneft-Invest	A	27.9
Ligovsky 266 (3rd phase)	Moskovsky Prospect	Stroitelnye mashiny	B	16.5
Business Centre at Nalichnaya	Vasileostrovsky-2	Dal'piterstroy	B	15
Atlas City	Moskovsky Prospect	Promyshlennaya Innovacionnaya Companiya	B	13
Multifunctional Complex Riverside (building D)	Embankments with views	SetlGroup	B	11.2
Dom Pushniny	Moskovsky Prospect	Pushnoy Dom	B	10
Aura	Outside area	Best'b	A	8.2
GRANI	Petrogradsky	Stroitelny trest	B	7
Senator at Malyi Avenue P. S.	Petrogradsky	Imperia Financial and Holding Company	A	6.7
Pythagor	Vasileostrovsky-2	Kompleksnye Stroitelnye Technologii	B	3.6
Obvodny 28	Obvodny	Torgtrans-servis	B	3.6
Renaissance Fontanka	Admiralteisky	Renaissance Development	A	3.4

Source: Knight Frank St. Petersburg Research, 2018

Map of Saint Petersburg business districts



Source: Knight Frank St. Petersburg Research, 2018

RESEARCH

Svetlana Moskovchenko

Head of Research Department

svetlana.moskovchenko@ru.knightfrank.com

OFFICE MARKET

Marina Puzanova

Head of Commercial Department

marina.puzanova@ru.knightfrank.com

+7 (812) 363 2222



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