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COMMERCIAL REAL ESTATE MARKET  
OVERVIEW  
H1 2011



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## Summary

In H1 2011, the office real estate market of Moscow Region increased by 300 thous. sq.m. of high-quality areas. The volume of delivered new supply is much lower than the delivery paces of the previous years—the trend of the delivery slowdown, which began in 2010 is still relevant.

Therefore, the aggregate supply volume in the office real estate market amounted to approx 11.1 mln. sq.m.

The business activity was rather high during H1 2011—the demand on rent and sale of high-quality premises remained high, which caused the further reduction of the vacant supply level. The share of vacant premises in the “A” class constituted about 13-15%, in “B” class—14-17% as of the end of H1 2011.

In general, the beginning of the year was rather positive for the office real estate market, the market continued demonstrating rather stable indices, at the same time all the post-crisis trends remained relevant.

The demand on rent and sale of high-quality office premises remained rather high during H 1 2011. The trend of gradual growth of average rented area remains.

The price situation in the office real estate market is characterized by the uptrend: the aggregate growth of the average rental rates reached approximately 10-15% since the beginning of the year against the background of tenants' rather high activity.

During Q2 2011, no new professional retail center was opened in Moscow. Consequently, by the results of half a year the supply volume remained at the level reached in Q1: the total volume amounted to 5.98 mln. sq.m., rentable area—3.03 mln. sq.m. Therefore, the provision of Moscow population with high-quality retail areas remained at the level of 289 sq.m. per 1, 000 residents.

During H1 2011, retail operators' high activity, which contributed to the growth of deals number and the vacant premises level decrease both in the professional retail segment and in the street retail segment, was observed.

During H1 2011, the professional retail real estate market continued its development within the framework of trends, formed already at the end of 2010.

The vacant premises level decrease and the stabilization of rental rates were characteristic of both the professional retail segment and the street retail segment. At the same time the most sought-after retail centers and the most prestigious retail streets displayed the gradual growth of rates by 5-10% versus the end of 2010.

With regard of adopted by the Government of Moscow legislative acts about the prohibition of new construction in the central part of the city, as well as the decision about the reduction of retail function to the minimal indices in the projects at Tverskaya Zastava square and Paveletsky station square, the further growth of rental rates in the street retail segment may be expected.

During H1 2011, the supply in the hotel market of Moscow increased by 636 rooms at the expense of the opening of three hotels. As the majority of delivered in the recent years hotels, two of three opened properties are positioned in the upper segment of the market. This trend contributes to the deficit of high-quality hotels in the middle and lower segments of the market. Therefore, the hotel real estate market of Moscow still targets predominantly business tourists.

The delivery of new brand W Hotels took place at the end of H1 2011 in the Russian market: W Saint-Petersburg de luxe class hotel for 137 rooms was opened in Saint-Petersburg (Starwood Hotels&Resorts operator). The hotel has a number of competitive advantages (the location near the Saint Isaac's Cathedral, nonstandard style, etc.), which make it possible to expect that the hotel will be able to occupy its niche in the luxe class hotel market of St.-Petersburg.

During H1, 5 hotels under the international operators' management were opened in regional cities, the aggregate room stock of which constituted 834 rooms.

The preservation of low paces of new supply increase and almost total absence of new projects in the middle and lower segments may be noted among the main observed during the last years trends, which will contribute to the deficit of rooms in the nearest years, which will lead to the gradual growth of occupancy rate and sales prices as the demand recovers.

## Supply

The office real estate market of Moscow Region increased by 300 thous. sq.m. of high-quality areas for H1 of 2011. Delivered new supply volume is considerably lower than the indices of the previous years—the trend of the delivery paces slow-down, which began in 2010, is still relevant.

Therefore, the aggregate supply volume amounted to approx 11.1 mln. sq.m. in the office real estate market.

The business activity was rather high during the first half of 2011—the demand for rent and purchase of high-quality premises remained high, which caused the further reduction of the vacant supply level. The share of “A” class vacant premises constituted approx 13-15%, “B” class—14-17% as of the end of H1 2011. The office market within the Central business area is close to the complete recovery - here the level of “A” class vacant supply is lower than the average one in the market. The demand for the farther from the center districts is gradually growing and the growth paces will increase due to the rather strict restrictions of new construction within the TTR.

Generally, the beginning of the year was rather positive for the office real estate market, the market continued to demonstrate rather stable indices, at the same time all the post-crisis trends remained relevant. Despite the fact that the correction of developers' plans and the optimization of portfolios were still taking place, the construction of a number of large projects was resumed in H1 2011, besides, the implementation of new projects were announced. Thus, Sistema Hals company offered for sale 2 buildings of B+ business center “Danilovsky fort” at Novodanilovskaya embankment measuring 30 thous. sq.m.

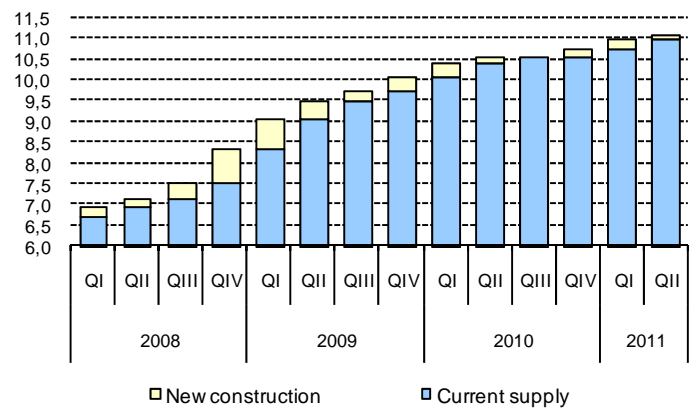
The same Sistema-Hals intends to enter another project – a

### Some of the projects announced for the reconception/construction in H1 2011

Developer/Investor	Name and class of the property	Address	Area, sq. m
<i>Unfreezing / Reconception</i>			
“STT-development”	MFC (“Russia” tower)	Moscow-City, sites 17-18	250 000
MR Group	MFC (MR Group )	5, Golovinskoe highway	166 300 (offices 61 570)
“Snegiri development”	Evolutsiya (City Palace)	Moscow City, sites 2,3	169 000
“Sistema-Hals”	SkyLight (Siemens towers-“Sistema-Hals”)	39, Leningradsky prosp.	111 000
Midland Development/Sberbank	“Tsarev Sad”	36, Sofiyskaya – 10, Bolotnaya	80 000
n/a	Parliament center (“Rossiya” hotel)	Moscvoetskaya emb	n/a
<i>New construction</i>			
Bosch	Bosch office	Khimki	57 000
n/a	MFC “Zvezdny”	Korolev	34 000
“Renova-stroygroup”	MFC on the territory of ZIL factory	23, Avtozavodskaya	500-700 thous.
“Ak bars development”	“Smolenska”	12, Smolensky boul.	21 000

Source: Blackwood company data

### Supply volume dynamics, mln.sq. m



Source: Blackwood Company data

transport terminal in the structure of “Moscow-City”, acquiring 50%+1 share of the Holland company Citer Invest B.V. Besides transport infrastructure, the project presupposes the construction of high-quality office and hotel real estate. The planned term of the project implementation is 2015.

And Sberbank, planning the change of its headquarter, re-oriented from the purchase of the property to its construction and now it is looking for an appropriate for this purpose site.

**Demand**

Demand for the rent and purchase of high-quality office premises stayed rather high during H1 2011. The trend of gradual growth of the average rented area remains.

As far as the demand structure by the incoming requests to Blackwood Company is concerned, it turned out to be the following by the results of H1 2011: requests for rent constituted 61% of all the requests, 39% fell at the purchase of office premises.

“B-” class remains the most requested for rent class, however, the share of requests for it is in the process of falling due to the growth of demand for the more high-quality properties of “A” and “B+” classes.

The blocks measuring up to 200 sq.m. (38%) constitute the largest share in the demand structure of the office premises rent – this segment is still the most sought-after.

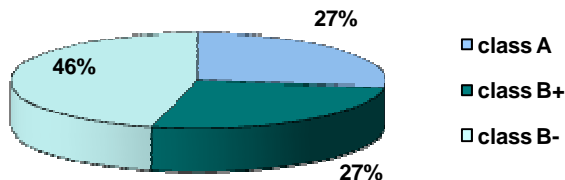
There is a gradual redistribution of demand towards the most high-quality “A” class properties in the purchase and sale segment of high-quality office premises – the share of requests for it increased from 18% to 24% versus the corresponding period of last year.

Some changes took place in the demand structure for the purchase of office premises by area as well: the growth of the number of requests for small blocks measuring up to 200 sq.m. was observed during H1 2011.

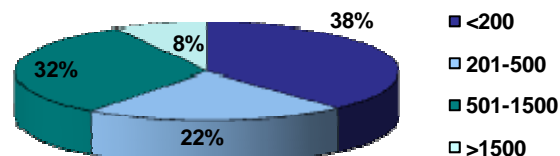
The general trends in demand in the high-quality office real estate market in H1 2011 were the following:

- Demand for the rent and purchase of premises remains rather high, however, it is still highly differentiated: high-quality premises of high class located in prime areas are of the highest demand;
- The average rented area and the term of conclusion of lease contracts are growing;
- Demand for the purchase of premises still stays rather high, including on the part of banks.

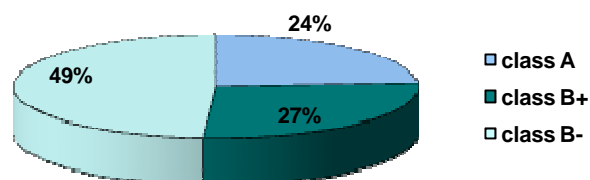
**Demand structure for office premises rent by class**



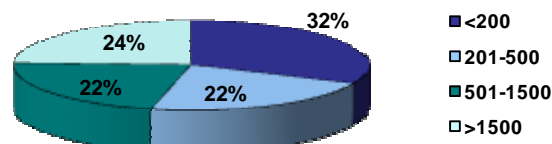
**Demand structure for office premises rent by metric area**



**Demand structure for office premises purchase by class**



**Demand structure for office premises purchase by metric area**



Source: requests to Blackwood, in H1 2011

### Rental rates

During H1 2011, the professional retail real estate market was in the process of development within the framework of trends, formed already at the end of 2010. The vacant area level decrease and the rental rates stabilization were characteristic of both the professional retail segment and the street retail segment. At the same time the most in-demand among tenants retail centers and the most prestigious retail streets displayed gradual growth of rates by 5-10% versus the end of 2010.

The situation when no decrease of rental rates took place during May-June (months for which seasonal decrease of business activity is characteristic) in the market is indicative of the fact that the growth observed in 2010 was not the result of a single burst of demand on the part of retail operators, but became the beginning of the market recovery process.

There were no important changes in the retail real estate market during Q3 2011.

The further growth of rental rates is possible not earlier than Q4, when the market will begin to recover after the summer slack.

Taking into account adopted by the Government of Moscow legislative acts at the beginning of 2011 about the prohibition of new construction in the central part of the city, as well as the decision about the reduction of retail function to the minimal indices in the projects at Tverskoy Zastavi square and the square of Paveletsky station, the further growth of rental rates in the street retail segment may in all likelihood be expected.

Besides, the growth of rental rates is expected in the segment of professional retail centers: by the results of H1 2011, the new supply increase paces slowdown, which in the nearest future will cause the deficit of high-quality areas, was outlined. This, in its turn, will contribute to the growth of rental rates as retail operators' development policy is resumed.

### The level of vacant areas and rental rates in retail corridors of Moscow as of the end of Q2 2011 and in comparison with Q2 2010

Retail corridor	The share of vacant areas, %	Rental rate, \$ per sq.m.	Rental rate, \$ per sq.m. as of the end of Q2 2011
Tverskaya	1,7	3 900 – 8 300	2 650 – 5 000
1st Tverskaya-Yamskaya	1,8	2 700 – 3 900	1 200 – 2 250
Arbat	2,0	2 100 – 3 500	1 500 – 4 050
Novy Arbat	7,9	600 – 2 800	1 450 – 2 500
Pyatnitskaya	4,1	1 800 – 3 700	1 350 – 3 550
Petrovka	1,0	2 000 – 3 150	1 800 – 2 250
Garden Ring	4,1	900 – 2 400	950 – 2 700
Kutuzovsky prospect	3,1	700 – 2 600	900 – 2 750

Source: Company data

### Forecast

It may be forecasted by the results of H1 2011 that in the nearest 1-2 years the new supply increase paces in the professional retail real estate market will slowdown considerably: projects, which were launched before the crisis, enter the market in low paces, the number of new announced projects is small and there is high probability that the paces of their implementation will be much lower than they may have been before the crisis.

Against this background, the outlined growth of the main retail operators' activity and the resumption of development programs in the nearest years may cause a new cycle of rental rates growth both in the segment of professional retail centers and in the street retail segment.

**Supply**

During Q2 2011 no new professional retail center has been opened. As a result the supply volume remained at the level reached in Q1: the total area constituted 5.98 mln. sq.m., the rentable area—3.03 mln. sq.m. Therefore, the provision of Moscow residents with high-quality retail areas remains at the level of 289 sq.m. per 1,000 residents.

The results of H1 2011 are indicative of the outlined slow-down of the new supply delivery paces. An expected pause took place after the hasty delivery of new projects in 2009-2010, which had reached a high stage of construction readiness before the crisis. The projects under construction still undergo hardship in fund-raising and attraction of tenants, that is why the terms of their delivery to the market are gradually shifted. Thus, the opening of such large projects as “River Mall” and “Gudzon” will by all appearances be shifted to 2012.

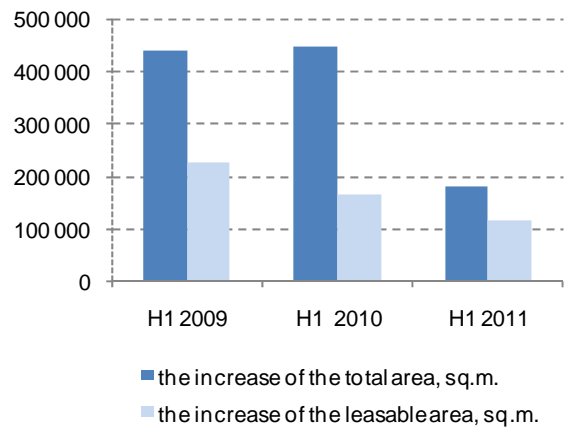
As far as new projects are concerned, in addition to the announced in Q1 2011 project of REC at the crossing of MKAD and the Altufievskoe highway (Finstroy developer), large-scale plans of Enka company on the redevelopment of “Kapitoly” retail centers were also announced.

The first property falling under the redevelopment will be RC in Yartsevskaya street (the first retail center of the group in Russia), a multifunctional complex measuring 235, 000 sq.m. (the area of retail component is 58, 900 sq.m.) will be built instead of it. In the aggregate, 5 retail centers, operating from

1900-beginning of 2000, are planned for reconstruction.

The necessity of redevelopment is determined by the growth of competition in the professional retail real estate market, complicity of the projects concepts, tenants' and potential visitors' raised requirements to properties and is indicative of the switch to the brand new stage of the market development.

**The increase of new supply in the professional retail real estate market, Moscow, 2009-2011**



Source: Blackwood Company data

**Professional retail centers delivered to the market in H1 2011**

Name	Total area/ Retail area, sq. m	Developer	The main tenants
Afimall City	179 000 / 114 000	AFI Development	“Zeleny Perekrestok” supermarket, “Eldorado” appliance store, “Sportmaster” sports goods store

Source: Blackwood Company data

**Demand**

During H1 2011, retail operators' high activity, which contributed to the growth of deals number and the decrease of vacant areas level both in the professional retail segment and in the street retail segment, was observed.

In H1, 4 international retail operators entered the Moscow market:

- Chili's Grill & Bar chain of restaurants (USA);
- Petit Patapon chain of children's clothing stores (Portugal, the first Russian store of the chain was opened at the end of 2010 in Krasnodar);
- Wendy's chain of fast food restaurants (USA);
- American Eagle chain of clothing stores (USA).

- All the mentioned retail operators develop in Russia according to the franchising scheme.

Besides, during H1 2011, a number of international retail operators announced their planned entry to the Russian market :

- Jimmy Choo premium class chain of boutiques;
- Banana Republic chain of clothing stores;
- Kesko Food chain of hypermarkets;
- Berghaus chain of clothing stores and shoes

During Q3 2011, the decrease of the market main players' activity, traditional for the summer months is expected.

### Rental rates

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There were no important changes in the retail real estate market during Q3 2011.

The further growth of rental rates is possible not earlier than Q4, when the market will begin to recover after the summer slack.

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Source: Company data

### Forecast

It may be forecasted by the results of H1 2011 that in the nearest 1-2 years the new supply increase paces in the professional retail real estate market will slowdown considerably: projects, which were launched before the crisis, enter the market in low paces, the number of new announced projects is small and there is high probability that the paces of their implementation will be much lower than they may have been before the crisis.

Against this background, the outlined growth of the main retail operators' activity and the resumption of development programs in the nearest years may cause a new cycle of rental rates growth both in the segment of professional retail centers and in the street retail segment.



## Supply

During H1 2011, the supply in the hotel real estate market of Moscow increased by 636 rooms due to the opening of three hotels (see Spreadsheet). As the majority of delivered to the market in the recent years hotels, two of three opened properties are positioned in the upper segment of the market. This trend contributes to the preservation of the deficit of high-quality hotels in the middle and lower segments. Therefore, the hotel real estate market of Moscow still targets predominantly at business tourists.

The delivery of at least 2 large hotel properties to the Moscow market is expected by the end of 2011: the InterContinental Moscow Tverskaya hotel (5\*, 205 rooms) and Courtyard by Marriott Paveletskaya (4\*, 170 rooms). Therefore, the increase of new supply by the results of 2011 may amount to approx 1000 rooms, which corresponds to the results of the recent years and makes it possible to expect that as the demand for accommodation services is recovering against the background of the new supply increase paces slowdown, gradual growth of occupancy rate and sales prices will take place.

### The increase of new supply of hotel rooms, H1 2011, Moscow

Name	Address	Class	Number of rooms
Crowne Plaza Moscow World Trade Centre	12, Krasnopresnenskaya emb.	5*	149
Aminievskaya	5, Aminievskoe highway	2-3*	223
Radisson Blu Belorusskaya	26, 3rd Yamskaya str.	4*	264
<b>TOTAL</b>			<b>636</b>

Source: Blackwood Company data

### International operators' activity

The delivery of a new brand W Hotels to the Russian market took place at the end of H1 2011: the luxe class hotel W Saint-Petersburg for 137 rooms (Starwood Hotels&Resorts operator) was opened. The hotel has a number of competitive advantages (location near Saint Isaac's Cathedral, unusual style, etc.), which make it possible to expect that the hotel will be able to occupy its niche in the luxe class hotel market of St.-Petersburg.

On the whole, 5 hotels under international operators' management, the aggregate hotel room capacity of which

amounted to 834 rooms were opened during H1 (W Saint-Petersburg, Courtyard by Marriott in Kazan, Ibis in Nizhny Novgorod, Crowne Plaza in St-Petersburg and Park Inn in Astrakhan).

The preservation of international hotel operators' considerable interest to regional cities reflected not only in the statistics of delivered to the market properties, but also in the announced new projects (see Spreadsheet): only 40% of planned for delivery rooms are found in Moscow.

### New projects of hotels under international operators' management, announced in Q2 2011

Name	City	Class	Number of rooms	Delivery to the market
Kempinski Nikolskaya	Moscow	5*	210	2012
Hilton	Moscow	5*	142	2014
Park Inn	Novosibirsk	3*	150	2014
Swissotel Kamelia Sochi	Sochi	5*	200	2014
Pullman	Sochi	5*	150	2013
Mercury	Nizhny Novgorod	5*	n/a	2013
<b>TOTAL</b>			<b>852</b>	

Source: Blackwood Company data

### Trends and forecast

Among the main observed in the Moscow hotel market during the last years trends, the preservation of the new supply increase low paces and practically total lack of new projects in the middle and low segments may be singled out,

which will in the nearest years contribute to the rooms deficit preservation, which in its turn will cause the gradual growth of occupancy rate and sales prices as the demand is recovering.