



Research department  
and market analysis

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Moscow, 1 quarter 2017

# Office market report

# Main indicators of the office market

Moscow, 1 quarter 2017

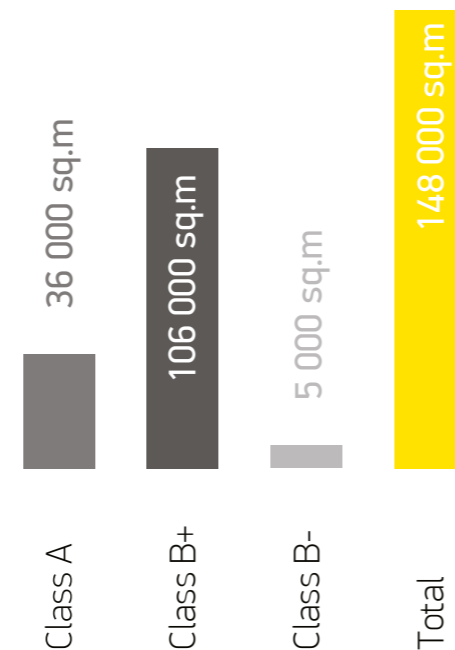
## The first 3 months have seen zero supply,

which is the record lowest supply for the last 10 years

The first quarter of 2017 has seen zero new supply, which has become an anti record for the last 10 years of collecting and tracking down market data. The total number of square meters of new office space in 2017 is expected to be the lowest and will not exceed 450,000 square meters as announced by the developers. The largest projects, however, will continue to be pushed back, and the new supply may actually turn out to be even lower. Property owners remain pessimistic further delaying new projects to avoid exposure to the property taxes once a project is commissioned. The delivery of new projects may also depend on signing up large tenants. The majority of the new supply for the coming 24 months will derive from the projects that were scheduled to be rolled out in 2015-2016.

Total net absorption for Q1 of 2017 has made up 148,000 square meters. The market is still characterized by migration of the occupiers to quality projects, now mostly to Class B+ office buildings. Due to numerous transactions, total net absorption made up 106,000 square meters by the end of March comprising 36,000 square meters in Class A office buildings. After the slowdown of freeing up office space in Class B- properties at the end of 2016,

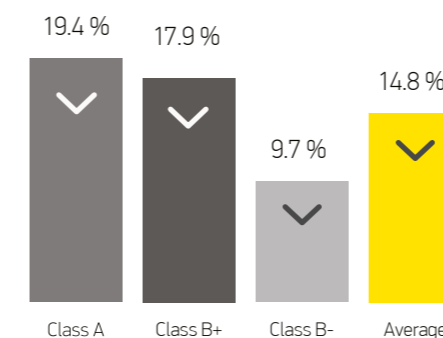
Net absorption of office space  
Q1 2017



## By 1.1 points

The vacancy rate of office sq.m has decreased by 1.1 points

Vacancy rate\*



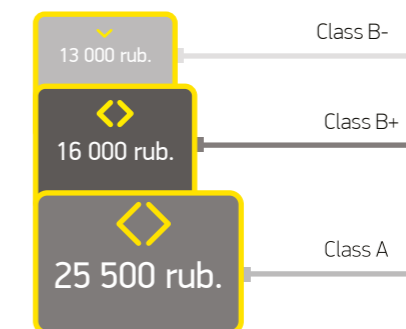
the total net absorption became positive and reached 5,000 square meters in Q1 of 2017.

The decrease of the new space delivery continues to impact the market calibrating the balance between demand and supply. In the beginning of the year vacancy rates have dropped by 0.9 points averaging 14.8% in the office market. In Q1 of 2017 the decrease of vacancy rates affected all building classes. Despite of constantly decreasing delivery of new office space and a zero supply in the first quarter about 2,900,000 square meters remain vacant. Thus, every 6th square meter is vacant at the moment. Nevertheless it's worth noting that the allocation of new delivered office space is uneven throughout Moscow districts.

Strengthened ruble and migration of the tenants to quality projects in previous quarters have somehow stabilized commercial terms on the market of commercial real estate. Average asking base rents in ruble terms remained the same as compared to the end of 2016.

\*As compared to the end of Q1 2016

Average asking base rents



**148  
thousand sq.m**

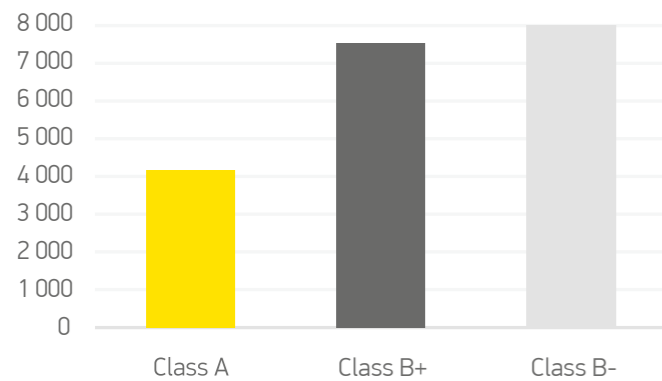
by the end of Q1 net absorption has made up 148 thousand sq.m

**25 500  
RUB/sq.m/year**

average asking base rents for class A office space makes up RUB 25 500

# Supply

Total stock, Q1 2017, thousand sq. m



As of Q1 of 2017 the total number of square meters of office space has made up 19.9 million sq.m comprising 4.2 million sq.m (21%) of Class A, 7.5 million sq.m (38%) of Class B+ , 8.2 million sq.m (41%) of Class B- office premises.

The first three months of 2017 have seen zero new supply, which is the record lowest supply for the last 10 years. The majority of the new supply planned for the first three months will be delivered in Q2-Q3 of 2017.

Nevertheless, the total number of square meters of new office space planned for delivery in 2017 is expected to be the lowest and will not exceed 450,000 square meters. The largest projects, however, will continue to be pushed back, and the new supply may actually turn out to be even lower. Property owners continue to postpone the delivery of new projects to avoid exposure to the property taxes once a project is commissioned. The delivery of new projects may also depend on signing up large tenants. In the next 24 months the office market will be saturated by those projects that were planned for delivery in 2015-2016.

Besides, it's worth noting that the structure of new office space delivery will change according to the classes in comparison with 2016. Class A office buildings will prevail. Last year the number of new Class A office buildings made up 26% of the total supply, this year it won't exceed 80%.

**19.9 million sq.m**

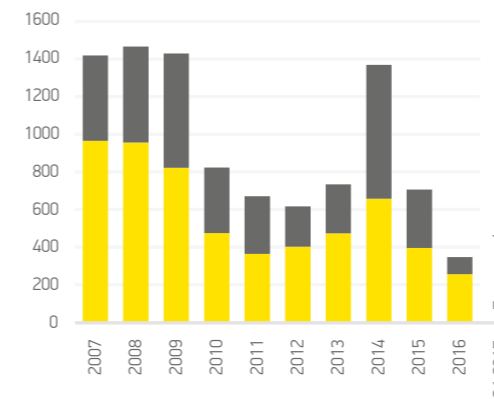
Total stock of office space has made up 19,9 million sq.m as of Q1 2017

**21%**  
Class A

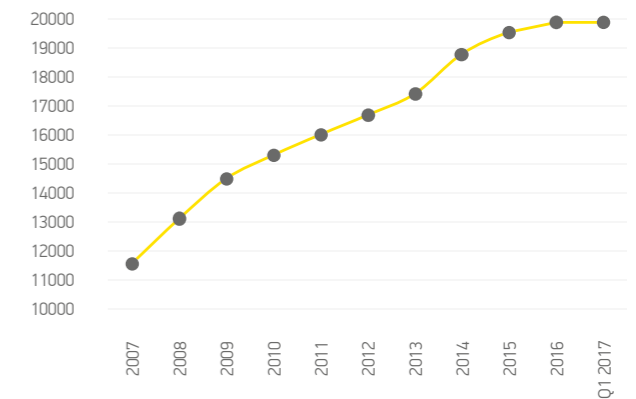
**38%**  
Class B+

**41%**  
Class B-

Increase in supply, thousand sq.m



Total stock trend, thousand sq.m



Since 2014 the greater part of developers has frozen the delivery of some projects. Some projects were frozen at the planning stage or its zoning was changed from office to apartments. Such changes can result in further decrease in new office delivery, while the supply will get minimal.



**Victor Reshetnikov** | Director, Office agency department

**Low vacancy rate boosts tenants' activity on the commercial real estate market**

We observe a resumed demand on Class A and B+ office buildings in all sectors. The biggest number of inquiries comes from government institutions. We expect that due to low vacancy rates and zero supply tenants' activity on the commercial real estate market will only pick up stream.

## Main properties expected to be delivered in 2017

Property	Address	Developer	Class	Office space, sq.m
MFK "IQ-quarter"	11 Presnenskaya Embankment	Hals-Development	A	108 623
Federation Tower -I "Vostok"	12 Presnenskaya Embankment	AEON-Development	A	82 000
Neopolice	Kievskoye Shosse, 3 km MKAD	A-Store Estate	A	56 700
Stratos Lab	10D Nametkina Street	Vysota	A	32 000
Oasis	3 Koroviy Val Street	BIN	A	28 775
MFC Fili-grad, Phase I	5 Beregovoy Proyezd	MR Group	A	26 500
Smolensky Passage, Phase II	7-9 Smolenskaya Square	BIN	A	21 000
Novion	1 Samarskaya Street	BIN	A	21 000
Tverskaya Residence	2nd Brestskaya Street Bld.2	Tekhnokom	A	18 976
SKY House	40 Mytnaya Street	Mos City Group	A	17 500
20 Nagornaya Street Bld. 7	20 Nagornaya Street Bld. 7	Souzprominvest	B+	14 836
Bernikov	11 Nikoloyalamskaya Street Bld.2	BIN	B+	13 000
Arena Park Bld. 4, 5	36 Leningradsky prospect, Bld. 4,5	UK Dinamo	A	12 938



# Demand

Total net absorption for Q1 of 2017 has made up 148,000 square meters. The market is characterized by migration of the occupiers to quality projects, now mostly to Class B+ office buildings. Due to numerous transactions, total net absorption made up 106,000 square meters by the end of March comprising 36,000 square meters in Class A office buildings. After the slowdown of freeing up office space in Class B- properties at the end of 2016, the total net absorption became positive and reached 5,000 square meters in Q1 of 2017.

Net absorption in Q1 this year is thus 29% lower than in Q1 of 2016. However it's worth noting that about 40% of net absorption last year was determined by one large transaction in Q1.

It is obvious that net absorption is still characterized by migration of the occupiers to high-quality office buildings. More and more companies continue consolidating offices to reduce their rental and logistics expenses leaving lower quality offices unoccupied. Some tenants prefer to move to new office buildings and benefit from better technical conditions as soon as possible, even without coming to an agreement with their current landlords. That's why the number of vacant office square meters continues to decrease mostly in Class A and B+ office premises.

Therefore, the largest transactions are settled in shell & core offices. As a result, some tenants will move to their new offices later which will negatively affect the total net absorption.

As of Q1 2017 the number of inquiries is almost equal in all sectors. The biggest number of inquiries still comes from the consumer section and makes up about 14% of all inquiries. During the first 3 months the number of inquiries from trading companies reduced by 2 points to 12%. By the end of the year financial sector got more active and the number of inquiries increased by 2 points and made up 7% from all inquiries as compared to the end of 2016.

## Companies in the services sector

remain the main consumer of high-quality office space

The structure of demand according to the branch of business activity, Q1 2017



- Consumer services
- Trading companies
- IT, telecommunication and media companies
- Other
- Developers
- Manufacturing companies
- Banks and finance companies
- Professional services
- FMCG and pharmaceutical companies
- Logistics and transport companies
- Energetics
- Industrial sector
- Government institutions

\*The analysis is based on the total number of applications received by ILM in Q1 2017

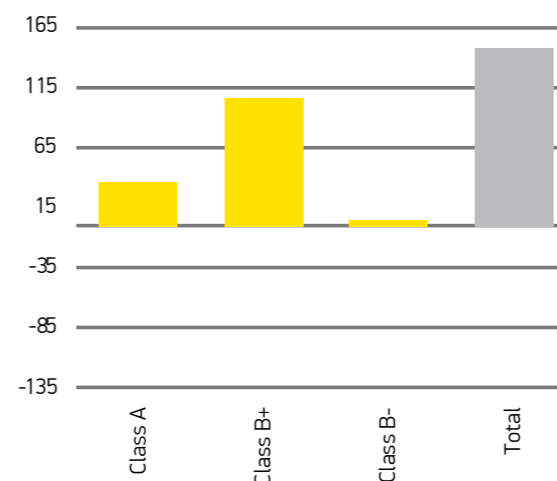


Sergey Kruzhilin | Director, Office agency department

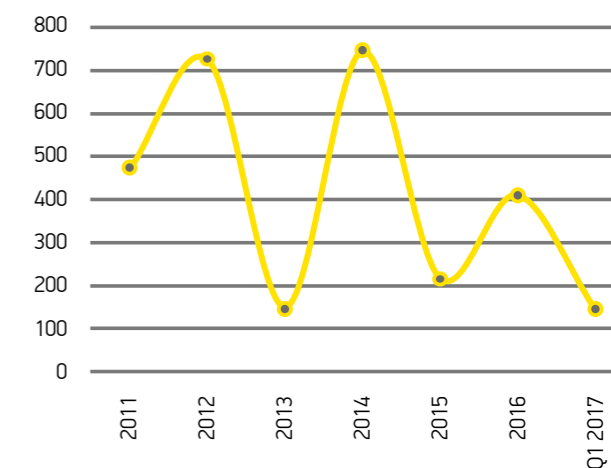
## Companies continue moving to quality projects

We are watching the increased tenants' activity in cutting their lease expenses in current location on relatively stabilizing commercial real estate market. It provides an opportunity to companies that prefer optimizing their lease expenses without turning to consulting agencies to avoid regular indexation of base rents and/ or reduce their current expenses. Those companies that have managed to estimate their perspectives on the real estate market correctly move to quality projects and reduce their lease expenses at the same time.

Net absorption as of Q1 2017, thousand sq.m



Net absorption trend, thousand sq.m\*



Net absorption on the market of high-quality office space at the end of Q1 2017, thousand sq.m

District	Class A	Class B+	Class B-
Central District	6,6	-18,2	2,4
Moscow City	13,8	4,2	-*
NED before FRR	0,9	3,3	-11,7
NED after FRR	-*	8,6	-*
ED before FRR	-9,5	1,7	-5,2
ED after FRR	-*	-0,2	-4,6
SED before FRR	-*	-11,5	6,7
SED after FRR	-*	0,9	2,8
SD before FRR	0,3	48,5	0,4
SD after FRR	-*	1,8	-3,9
SWD before FRR	-*	-2,4	-5,2
SWD after FRR	6,0	-14,9	11,0
WD before FRR	0,2	39,7	-0,1
WD after FRR	0,4	15,5	13,8
NWD before FRR	-*	-*	-0,1
NWD after FRR	-12,8	16,3	0,9
ND before FRR	-7,7	8,7	-3,4
ND after FRR	37,9	-0,8	1,7

FRR – Fourth Ring Road

\* Buildings not applicable in the indicated district

Key deals in Q1 2017

Company	Number sq.m	Type of transaction	Property	Address
Glavgosexpertiza	13 600	lease	42 Bol. Yakimanka St.	42 Bol. Yakimanka St.
Rosselkhozbank	9 639	purchase	1st Krasnogvardeisky pr-d, 7, Bld. 1	1st Krasnogvardeisky pr-d, 7, Bld. 1
Detsky Mir	5 000	lease	3rd Nizhnelikhoborsky pr-d 3	3rd Nizhnelikhoborsky pr-d 3
Loco Bank	4 500	purchase	Sky Light	39 Leningradsky pr-t
UK Buket	3 000	lease	White Stone	4th Lesnoy per. 4
KupiVip	3 000	lease	Mikhailovsky	1 Mikhailovsky pr-d, Bld. 1
CM-Klinika	2 779	lease	22 Simferopolsky blvd.	22 Simferopolsky blvd.
LCM Group*	2 600	lease	38 Berezhkovskaya Emb.	38 Berezhkovskaya Emb.
BIN Engineering	2 300	lease	7/9 Bol. Drovyanoy per., Bld. 1	7/9 Bol. Drovyanoy per., Bld. 1
Match TV*	2 097	lease	Smena	16 Dokukina St., Bld. 1
Mamsy*	1 700	lease	Donskoy	11 Ordzhonikidze, Bld. 10
Shire Rus	1 700	lease	Krasnaya Roza, Morozov	16 Lva Tolstogo St.
Project 101	1 400	lease	Golden Gate	2 Entuziastov blvd.
Linkprofit*	1 395	lease	Lotos	2 Odesskaya St.
PromSvyazMontazh*	1 238	lease	8 Dokuchaev per.	8 Dokuchaev per.

\* in this transaction ILM acted as a consultant

# Vacancy rates

The decrease of the new space delivery continues to impact the market calibrating the balance between demand and supply. In the beginning of the year vacancy rates have dropped by 0.9 points averaging 14.8% in the office market. In Q1 of 2017 the decrease of vacancy rates touched all building classes.

The greatest decrease of vacancy rates is noticed in Class B+ office buildings. As a result of growing net absorption in this class the number of unoccupied office space has decreased by 1.5 points.

We watch the same tendency in Class A office buildings. The vacancy rates in this class have decreased by 0.9 points and reached 19.4% which now makes up 810,000 sq.m. At the same time the number of big office blocks in Class A buildings continues to decrease and big companies are now struggling while searching for new high-quality office space. Office space totaling more than 15,000 square meters is currently available only in 10 Class A office developments.

In the context of positive net absorption in Class B- in Q1 the vacancy rate has decreased by 0.1 points and reached 9.7% by the end of March.

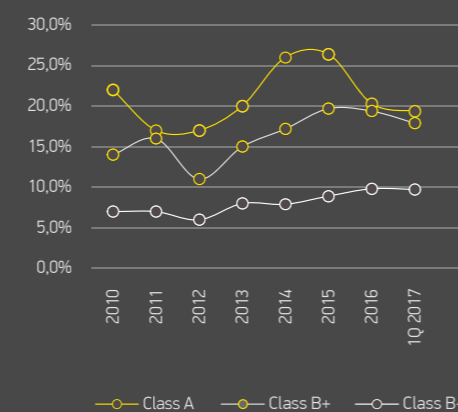
Despite of constantly decreasing delivery of new office space and a zero supply in the first quarter about 2,900,000 square meters remain vacant. Thus, every 6th square meter is vacant at that moment, nevertheless it's worth noting that the allocation of new delivered office space is uneven throughout Moscow districts.

In the CD vacancy rate is probably the lowest. By the end of March it has made up 10.8%, though in absolute terms it makes up about 700,000 square meters or 1/4 of

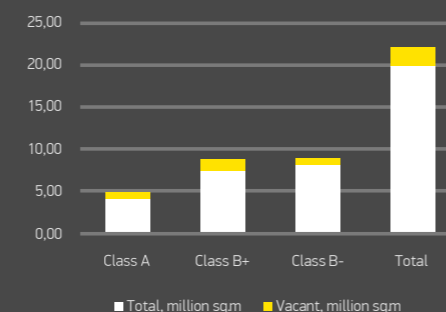
## 2,9 million sq.m

are vacant right now

Vacancy rate trend, %



Volume of vacant space, Q1 2017, million sq.m



all vacant office space in Moscow.

The highest vacancy rate remains in Class A office buildings located in SED before FRR (65.4%) and ED before FRR (60.8%). Several big Class A office projects are located here and are still unoccupied. In the CD vacancy rate in Class A office premises reduced by 0.4 points and by the end of the quarter reached 16.5%.

The number of vacant office space in MIBC Moscow City has made up about 179,000 square meters. Vacancy rate in this district is now 18.2%.

Analyzing vacancy rates in Class B+ office buildings, we came to the conclusion that the highest vacancy rate remains in NWD before FRR (100%, represented by only one office development), SWD after FRR (31.2%) and SED after FRR (31%). In CD vacancy rate has made up 9.3% and in the period of 3 months increased by 0.6 points.



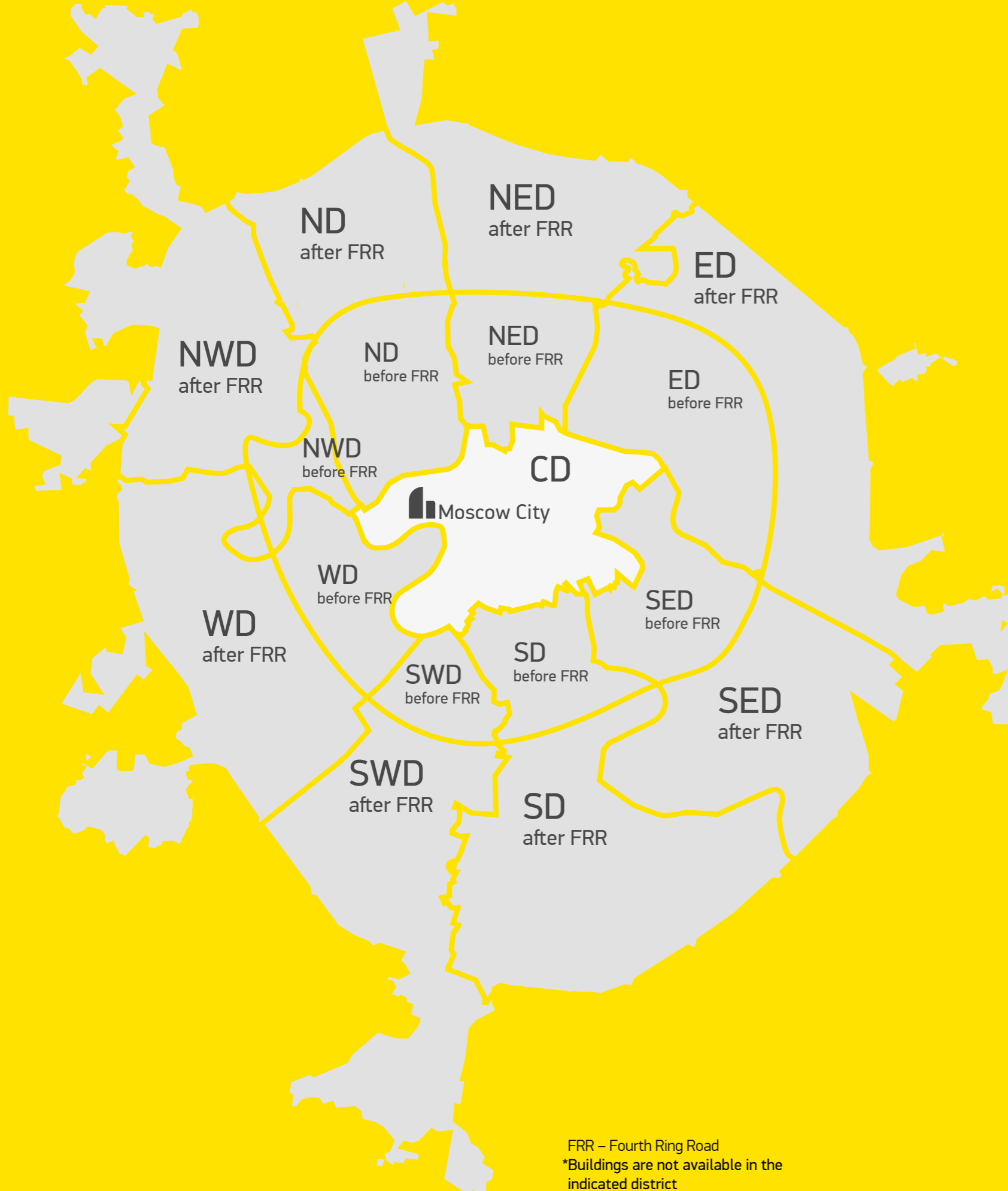
Yuri Yudakov | Director, Occupier services

**The decrease of the new space continues to impact the market calibrating the balance between demand and supply**

The decrease of the new space continues to impact the market calibrating the balance between demand and supply. In the context of zero supply and increasing net absorption in Class A and B+ office buildings we notice a pickup on the market including the inquiries about 10,000 square meters for lease of office space and even bigger number of square meters.

## 14,8 %

Average vacancy rate makes up 14,8% as of Q1 2017



FRR – Fourth Ring Road  
 \*Buildings are not available in the indicated district

Vacancy rate of high-quality office space as of the end of Q1 2017

District	Class A	Class B+	Class B-
Central District	16,5%	9,3%	8,3%
Moscow City	19,9%	12,7%	-*
NED before FRR	14,5%	17,0%	12,0%
NED after FRR	-*	24,6%	7,6%
ED before FRR	48,1%	22,5%	10,1%
ED before FRR	-*	1,4%	6,7%
SED before FRR	65,4%	18,7%	4,8%
SED before FRR	-*	31,0%	12,4%
SD before FRR	4,4%	19,0%	11,7%
SD after FRR	-*	30,6%	7,5%
SWD before FRR	34,8%	21,7%	32,1%
SWD before FRR	31,1%	31,2%	11,6%
WD before FRR	29,3%	28,5%	3,4%
WD after FRR	17,4%	29,3%	21,5%
NWD before FRR	-*	99,9%*	16,9%
NWD after FRR	47,7%	14,6%	5,4%
ND before FRR	11,7%	21,3%	8,7%
ND after FRR	14,2%	25,6%	6,5%



# Rental rates

Strengthened ruble and migration of the tenants to quality projects in previous quarters have somehow stabilized commercial terms on the market of commercial real estate. Average asking base rents in ruble terms remained the same as compared to the end of 2016.

By the end of Q1 average asking base rents in Class A office premises have made up RUB 25,000/ USD 450 per sq.m per year and in Class B+ office buildings RUB 16,000/ USD 285 per sq.m per year.

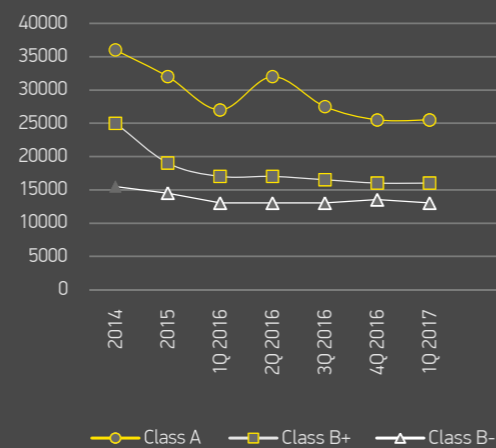
Little decrease in average asking base rents is noticed in Class B- office buildings. The decrease made up about 4% and by the end of Q1 base rents reached RUB 13,000 per sq.m per year.

Rental rates have been mostly affected by economic trends. Nomination of asking base rents in ruble terms will continue. In case of stable economic conditions we expect that current base rents will remain on the same level as compared to the end of 2016. The average level can vary depending on the offer terms and conditions or on some landlords' behavior that will gradually increase base rent due to market stabilization.

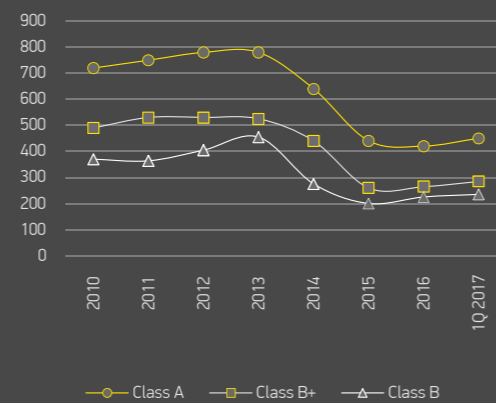
**29%**

As of 2016 and 2017 the decrease of asking base rent has made up 29%

Average asking base rents in ruble terms



Dynamics of average asking base rents in dollar terms



Andrei Protasov | Director, Investment and asset management

**Number of asset purchase and sale transaction may increase**

The highlight of Q1 of 2017 is a strengthening of the ruble rate. If the ruble rate fixes at 1 USD = 55 RUB, it may affect the debt load and the income from assets in ruble terms. It will dramatically change the situation for many property owners as their assets will generate a positive flow of money and the market value of their assets will exceed the debt load. This will boost the number asset purchase and sale transactions unless it doesn't bring about an increase in the asking price.



FRR – Fourth Ring Road  
 Rental rates VAT (18%) net of and OPEX.  
 \*Office space is not available in the indicated district

Average asking base rents for high-quality offices, Q1 2017

District	Class A	Class B+	Class B-
Central District	32 400 rub.	23 300 rub.	17 200 rub.
Moscow City	28 800 rub.	23 000 rub.	-*
NED before FRR	21 300 rub.	13 900 rub.	11 900 rub.
NED after FRR	-*	9 500 rub.	10 600 rub.
ED before FRR	20 100 rub.	16 800 rub.	11 300 rub.
ED after FRR	-*	16 200 rub.	9 700 rub.
SED before FRR	20 700 rub.	14 000 rub.	7 200p.
SED after FRR	-*	11 600 rub.	11 700 rub.
SD before FRR	32 100 rub.	14 200 rub.	12 300 rub.
SD after FRR	-*	13 000 rub.	12 000 rub.
SWD before FRR	17 500 rub.	26 500 rub.	13 800 rub.
SWD before FRR	15 700 rub.	14 000 rub.	16 100 rub.
WD before FRR	27 200 rub.	21 800 rub.	14 800 rub.
WD after FRR	17 500 rub.	10 500 rub.	9 800 rub.
NWD before FRR	-*	16 500 rub.	14 100 rub.
NWD after FRR	11 500 rub.*	10 500p.	12 300 rub.
ND before FRR	29 000 rub.	16 400 rub.	13 600 rub.
ND after FRR	11 800 rub.	11 300 rub.	11 700 rub.

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**772**  
deals

**680 140**  
sq. m marketed

**2009**  
year of foundation

**139**  
employees

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- Investment and asset management
- Property search
- Real estate brokerage
- Cadastral value revaluation
- Estimation of the real estate portfolio
- Reduction of occupancy costs

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