

# 2018 Moscow

## Office market report 2018 results and 2019 forecasts



### General trends and events

- High demand for offices has remained. During 2018 there were bought and leased 768,000 sqm. The decrease of 13% in comparison with the last year was due to the high market absorption rate of demanded areas and the lack of premises supplied in central locations (GR and BR zones).
- The minimum supply in 2018 (128,000 sqm) led to the vacancy's decrease and the increase in rental rates.
- For the first time in the recent 10 years, the vacancy rate (average for A, B+ and B) decreased below 10% and amounted to 9% at the end of 2018. The vacancy rate decreased most intensively in classes A and B+ (more than 5 pp).
- The weighted average rental rate (average for A, B+ and B) increased by 3% to 18,000 rub/sqm/year in 2018. The growth driver was class A where new supply made 7%, whereas in class B, by contrast, the rate decreased by 2%.
- According to developers, the supply will amount to 400,000 sqm of new office areas in 2019. The implementation of these plans will be reflected in a gradual movement of the office market towards a new cycle. The pace of the vacancy rate will decrease, however, the restrained growth of the rate will be remaining.

#### Indicator of 2018

#### Class A

#### Class B+

#### Class B

Total supply, mln sqm

6

5.8

4

New supply, thousand sqm

108

20

—

Volume of deals, thousand sqm

420

271

77

Vacancy rate

11%

9%

6.5%

Rental rates\*, rub/sqm/year

24,800

13,100

11,900

*\*the rates are indicated for shell & core premises, excluding VAT and operating expenses*

## Investment market

■ In Russia the volume of investments in commercial real estate has been decreasing for the third consecutive year, in particular, in the office segment. In 2018, the volume of investments in office facilities decreased by 39% amounting to \$1.1 bln (\$1.8 bln in 2017). For the first time in 3 years the volume of investments in office real estate is sidelined by the retail segment.

■ About 91% of investments were implemented in Moscow (\$996 m). The relevance investors' demand among the investors in St. Petersburg for office properties has also decreased to \$93 m, which was 37% less than in 2017 (\$147 m).

■ About 89% of investments (\$980 m) belong to the national investors. The foreign investments have totaled up to \$116 m.

■ Following the results of 2018, the capitalization rate for office properties: 10–11.5%.

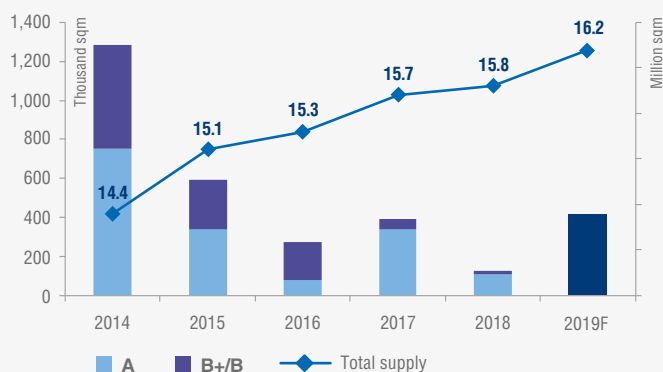
## Supply

■ Following the results of 2018, the new supply has reached 128,000 sqm being minimum over the recent 5 years. The downtrend resulted from the oversupply of office areas and the unfavorable economic conditions (sanctions, capital outflow, ruble's volatility, inflation, etc.). All these led to the cancellation of construction or building freeze of new office premises and reconception of office projects to apartments.

■ In 2018 the volume of the new office supply was 67% below the 2017 figure (392,000 sqm) and nearly 10 times smaller than in 2014 (1.2 m sqm).

■ The total volume of office properties has increased by 0.8% and amounted to 15.8M sqm at the end of 2018.

New supply Dynamic on Moscow Office Market

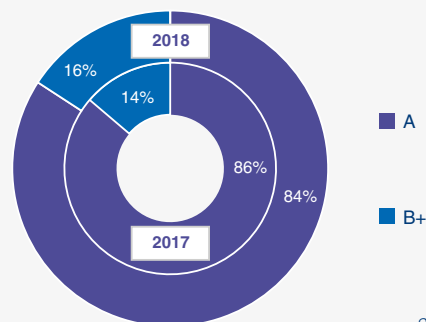


Source: S.A. Ricci

■ The new supply structure is consistently dominated by high-quality class A properties. Following the results of 2018 the share has reached 84% of the total volume (108,000 sqm). The new supply of class B+ amounted to 20,000 sqm (16% of the total volume). In 2017 the supply proportion was comparable, however, the absolute figures were higher: the supply of new class A and B+ office properties was 338,000 sqm and 54,000 sqm respectively.

Supply class structure

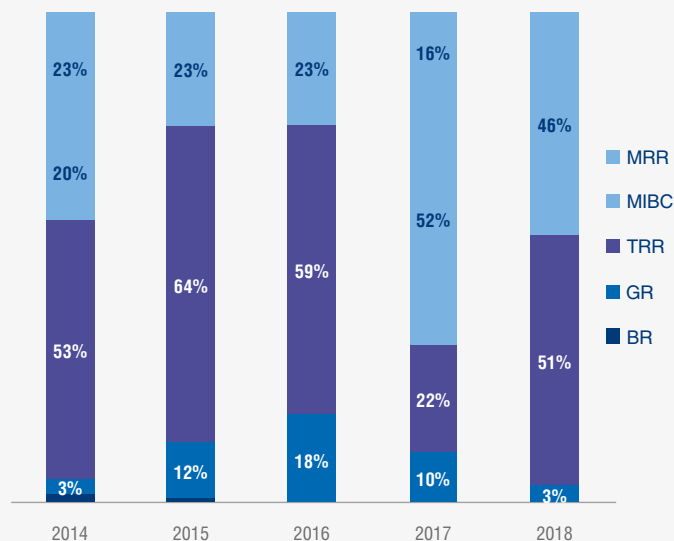
External circle: new supply of 2018  
Internal circle: new supply of 2017



Source: S.A. Ricci

■ By territory, TRR (51% and 65,000 sqm) and MRR (46% and 58,500 sqm) dominated. In 2017 the MIBC district was the leader accounting for over one half of all supplied areas (over 200,000 sqm). There were 85,000 sqm and 41,000 sqm supplied in 2017 in TRR and GR zones respectively.

New supply distribution by ring zones



Source: S.A. Ricci

### Examples of office buildings supplied in 2018

Name	Address	GLA, sqm	Class
Amaltea	Skolkovo, Bolshoy blvd. 40	31,000	A
VTB Arena Park	Leningraskiy avenue 36, bld. 9	27,500	A
Novion	Samarskaya st., 1	22,000	A
Krunit	Nagornaya st., 3, bld. 1	9,000	B+

■ We expect that the developer activities will grow in 2019. The developers plan to supply around 415,000 sqm of office properties. About one half of the new buildings – large projects, over 20,000 sqm. However, all of them will be located out of GR zones, therefore, the deficit of large high-quality blocks in Moscow center will accumulate.

■ In 2019 developers plan to supply more than a half of new properties in the TRR area representing making about approximately 220,000 sqm.

■ The share of high-quality class A will continue to dominate, however, it will decrease to 73% of the total volume accounting for around 300,000 sqm.

We forecast that in 2019 the total supply may increase by 1.5–2%. Not all of the buildings will be supplied as planned, however, it might be stated that the developer activities will be revived.

### Examples of business centres to be supplied in 2019

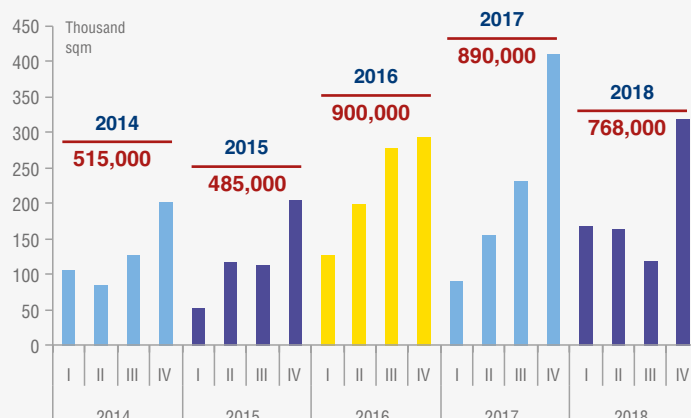
Name	Address	GLA, sqm	Class
Iskra Park	Leningraskiy avenue, 35	58,200	A
Stratos	Skolkovo	32,100	A
Park Legend	Avtozavodskaya st., bld., 23	31,800	B+
Park Khuamin	Vilgelma Pika st., bld., 14	24,800	A
Orbion	Skolkovo	22,600	A

## Demand

■ Following the results of 2018, the volume of new deals in the office market amounted to 768,000<sup>1</sup> sqm being 13% below the 2017 figure when the volume of deals totaled of 890,000 sqm.

■ In 2018 the share of lease agreement renegotiation deals accounted for 30% (325,000 sqm) of the total volume of all closed deals. In 2017 the volume of such renegotiation deals was higher (366,000 sqm), however, the share in the total volume also was 30%.

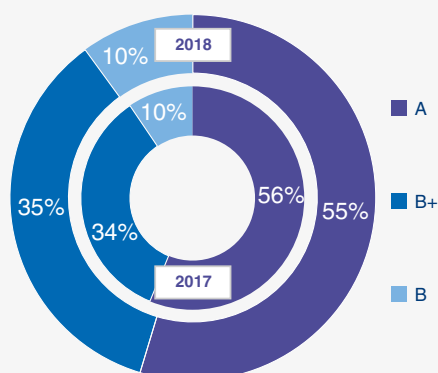
### Demand dynamic



<sup>1</sup>excl. Suvorov Plaza deal

■ As for class proportions, the demand structure remained similar to the 2017 relative indicators. Class A continues dominating in the demand structure. In 2018 the share of class A accounted for more than a half of purchased and leased areas (420,000 sqm). In 2017 the class A new deals figure made a comparable proportion, however, it was higher in absolute terms (498,000 sqm).

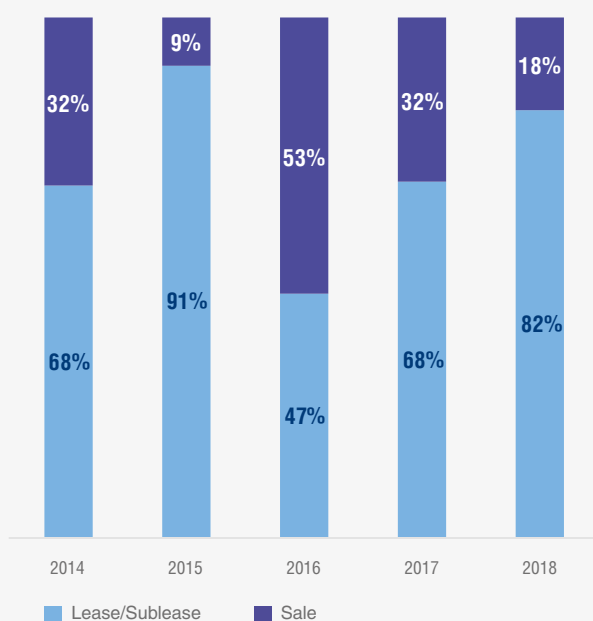
Demand by classes



Source: S.A. Ricci

■ The share of lease deals continues to increase against sales for the second consecutive year reaching 82%. In absolute terms, about 632,000 sqm were leased, which was 4% higher against the previous year (607,000 sqm). The volume of purchased areas decreased nearly twice making 136,000 sqm at the end of 2018 (against 279,000 sqm in 2017).

Changes in the structure of take-up by deal type, 2018



Source: S.A. Ricci

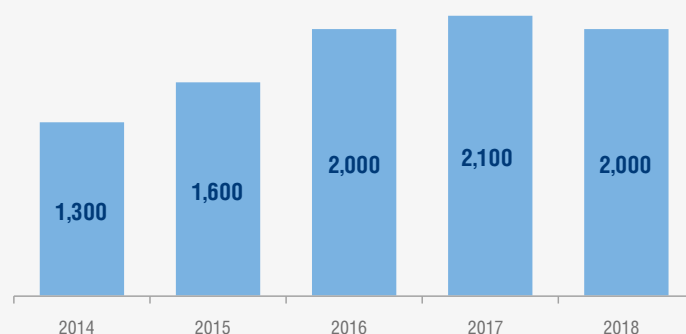
■ In 2018 the average deal size decreased by 5% to 2,000 sqm against the similar 2017 indicator (2,100 sqm).

■ For 5 years there can be noticed the trend of the average deal growth reflecting the increased demand for large blocks. The decrease in 2018 is due to the minimum supply of properties and no large high-quality blocks in interesting locations. As a result, the lack of new supply discourage the large deals.

■ The share of leases/purchases of areas up to 3,000 sqm in the total volume accounted for 80%. Deals with the areas of 3,000 to 10,000 sqm amounted to 18%. Deals with areas over 10,000 sqm accounted for 2% of the total amount.

We forecast that the average deal will be growing along with the developer activities' growth, especially in the central part of the city. In 2019 we expect that the average deal size will make 2,000–2,200 sqm.

Average deal size for 5 years, sqm



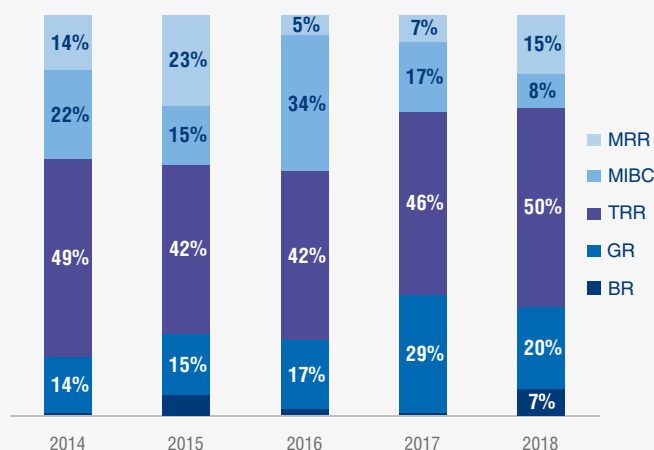
Source: S.A. Ricci

■ Following the results of 2018, the demand was concentrated within TRR. The share of closed deals in this area increased to 50% (46% in 2017), however, in absolute terms the volume decreased from 405,000 to 367,000 sqm. The second place in terms of new deals was within the Garden Ring with 150,000 sqm making 20% from the total amount. In absolute terms the figure decreased by 40% (260,000 sqm in 2017). Despite extremely limited supply, the volume of deals in the BR zone exceeded 50,000 sqm (7% from the total volume), in particular, due to the large deal at BC Arbat 1 (Aeroflot leased 18,400 sqm).

■ Following the results of 2018 the volume of new deals in properties located in the MRR zone increased by 78% against 2017 reaching 110,000 sqm against 62,000 sqm.

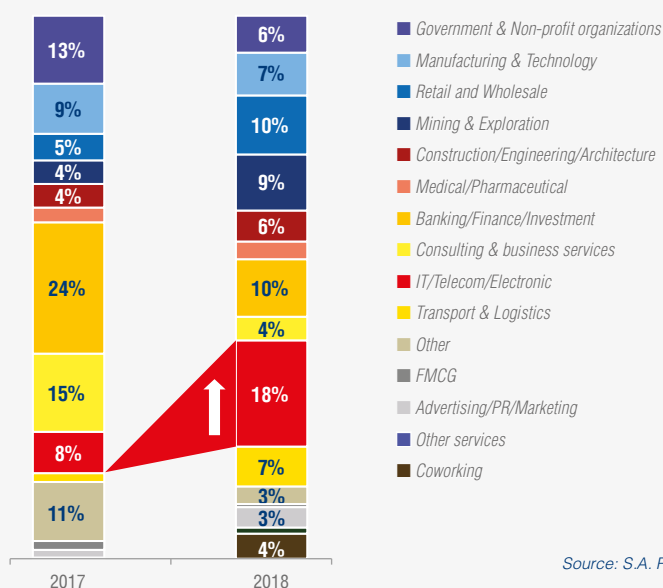
■ Owing to the supply deficit in Moscow City, especially the deficit of the large blocks, the volume of new deals in this zone decreased almost by 60% from 152,000 to 61,000 sqm.

### Distribution of deals in Moscow's ring zones



Source: S.A. Ricci

### Structure of take-up



Source: S.A. Ricci

■ According to the results of 2018, the structure of tenants and buyers by industry adjusted relatively to 2017:

- ✓ The share of IT/ Technology/ Communications representatives increased from 8% to 18% (nearly 140,000 sqm).
- ✓ Retailers and wholesalers purchased/leased approximately 80,000 sqm. In the total structure the share increased from 5% to 10%.
- ✓ The share of financial organizations also accounted for approximately 10% of the total volume (less than 80,000 sqm). However, the decrease against 2017 was serious significant in both absolute and relative terms.

For the recent 3 years the demand has been high. The downward trend in 2018 was the result of the high market absorption rate of the demanded premises. If the planned properties are supplied to the market on time, in 2019 the demand will remain at 800,000–900,000 sqm. The volume of deals will be mainly formed by the companies of IT, retailers and wholesalers, finance sectors and systemically important players of the Russian economy.

### Examples of deals in 2018

Name	Address	Class	GLA, sqm	Client	Type of deal	Quarter
Arbat 1	Arbat st., 1	A	18,440	Aeroflot	Lease	2Q
VEB Arena	3-d Peschanaya st., 2A	B+	12,660	Transneft-Technology	Lease	2Q
Efremova, 10	Efremova st.,10	B+	11,360	Transmashholding	Lease	2Q
Naberezhnaya Tower	Presnenskaya emb.,10	A	11,220	Ozon.ru	Lease	2Q
VTB Arena	Leningradskaya sq., 36, bld. 10	A	9,170	Etalon Invest	Lease	4Q
1Zhukov	Marshal Zhukov av., 1	B	7,060	Lamoda	Lease	2Q
Kuntsevo Plaza	Yarcevskaya st.,19	A	6,060	Media Instinct	Lease*	3Q
White Square	Butirskiy val st., 10	A	5,880	WeWork	Lease	4Q
Factoria	Viatskaya st., 27	B	4,890	School 42	Lease*	2Q

\* S.A. Ricci Deals

## Vacancy

■ The average vacancy of areas in Moscow's office market (classes A, B+ and B) has decreased below 10% for the first time in the most recent 10 years making 9% at the end of 2018. The greatest decrease for the year (by 5 pp) was in A and B+ classes being most demanded in recent years:

- ✓ 11% vacant areas in class A properties.
- ✓ 9% vacant areas in class B+ properties.
- ✓ 6.5% vacant areas in class B properties.

We expect that the trend towards lower vacancy will remain, however, the pace will slow down if all new properties planned for supply in 2019.

## Rates

■ Following the results of 2018, the weighted average rental rate (classes A, B+ and B) increased by 3% amounting to 18,000 rub/sqm/year (17,500 rub/sqm/year at the end of 2017).

■ The growth driver was class A. The average rental rate increased by 7% to 24,800 rub/sqm/year.

■ In classes B+ and B rates, conversely, have decreased by 0.5% and 2% respectively. The weighted average rental rate in class B+ amounted to 13,100 rub/sqm/year. In class B this was 11,900 rub/sqm/year.

The significant growth of class A price figures and a decrease in class B prove the fact that high-quality areas are most demanded. New buildings which are planned on 2019 will be unable to fully satisfy the demand. The trend towards the increasing rental rate for the high-quality areas will remain, especially in the central zones.



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