

RESEARCH REPORT

Kyiv Industrial Big Box

CBRE | Ukraine

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H1 2014

HOT TOPICS

- Fading development activity: 81,500 sq m of new space entered the market, a 35% y-o-y decrease
- Lean demand: take-up shrunk threefold in view of weak economic background
- Increasing vacancy rate: by the end of Q2 2014 vacancy rate reached 13.8% (+1.5 pp from Q4 2013)
- Relative stability of prime rents: base rents for top quality premises remained generally flat at \$6.25/sq m/month

DEMAND

Over the first six months of 2014 the recovery trend in demand has reversed, with transactional activity largely driven by relocation and optimization strategies, as majority of large occupiers, who are predominant from the retail sector, satisfied their requirements for warehouse premises in the course of 2011-2013. At the same time, precarious economic background does not contribute to the segment's development. As a result, take-up dropped threefold compared to the same period in 2013 and reached approximately 54,000 sq m. Another notable fact is that due to instability in Eastern region of Ukraine some companies relocate their stocks to the Central part of the country, thereby boosting demand for warehouse space in the Kyiv region in particular. One of such examples is Konti, a Donetsk based candy producer.

KEY TRANSACTIONS IN H1 2014

OCCUPIER	INDUSTRY	PROPERTY	DIRECTION	sq m
Ekol	3PLs, Transportation	WWM Center	Kyiv city	10,000
Zammerl	3PLs, Transportation	V-log	M-01, E-95	10,000
CAT Kargo	3PLs, Transportation	MLP-Chaika	M-06, E-40	7,500
Eurotek	Wholesale and retail trade	Technopolis warehouse	M-01, E-95	7,000
Ekol	3PLs, Transportation	VVS	M-05, E-95	6,000
Omega Avtopastavka	Wholesale and retail trade	MLP-Chaika	M-06, E-40	5,000
AVK	Wholesale and retail trade	Technopolis warehouse	M-01, E-95	3,500
DSV	3PLs, Transportation	SAN factory II	Kyiv city	3,500

Source: CBRE Ukraine

In terms of take-up structure, the largest share of warehouse space (62% of all transaction volume) was leased on the Right (West) Bank, a 9 pp y-o-y increase. At the same time, contribution of the Moscow direction (M-01, E-95) on the Left (East) Bank is still significant despite a slight easing up of demand in that direction. The share of the Left bank submarket mentioned above accounted for 38% of take-up, having decreased by 7 pp and 27 pp compared to H1 2013 and H1 2012, respectively.

SUPPLY

In total, the modern warehouse stock witnessed around 81,500 sq m of new completions in the first six months of 2014. The lion's share of new space concentrated on the Left (East) Bank accounting for 90% of the total volume of new premises (80% in 2013).

KEY WAREHOUSE SCHEMES IN H1 2014

NAME	DEVELOPER	WAREHOUSE PREMISES, sq m	HIGHWAY	COMPLETION
RLC (Refrigerated logistics center)	RLC	60,000	M-01,E-95	H1 2014
Vagatable&Food storage	Local	10,400	M-01,E-95	H1 2014
SAN factory (Phase II)	Sky Development	7,000	Kyiv city	H1 2014
Warehouse complex	Local	4,000	M-03,E-40	H1 2014

Source: CBRE Ukraine

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At the same time, by the end of June the Right (West) Bank saw a minor increase in ambient space of 7,000 sq m in the second phase of SAN Factory in Kyiv. As 2014 is progressing, no new notable properties are expected for delivery later in the year. Therefore the new supply in 2014 is expected to be 35% less compared to 2013 results.

VACANCY

As of the end of Q2, the average vacancy rate reached 13.8% compared to 8.1% six months ago (+5.7 pp). The reason for the sharp increase in vacancy is twofold. Firstly the market saw a significant input of space in the specialized RLC multi temperature complex in Q1. Secondly, the annual volume of organized retail turnover, one of the main drivers of demand for warehouse premises, weakened markedly over January – May 2014 for the first time since 2009, having decreased by 5.7% y-o-y in Kyiv. At the same time, as occupiers are facing space redundancies, a sublease trend is gaining momentum, which takes away volume from the main market, as sublease market is noticeably more flexible.

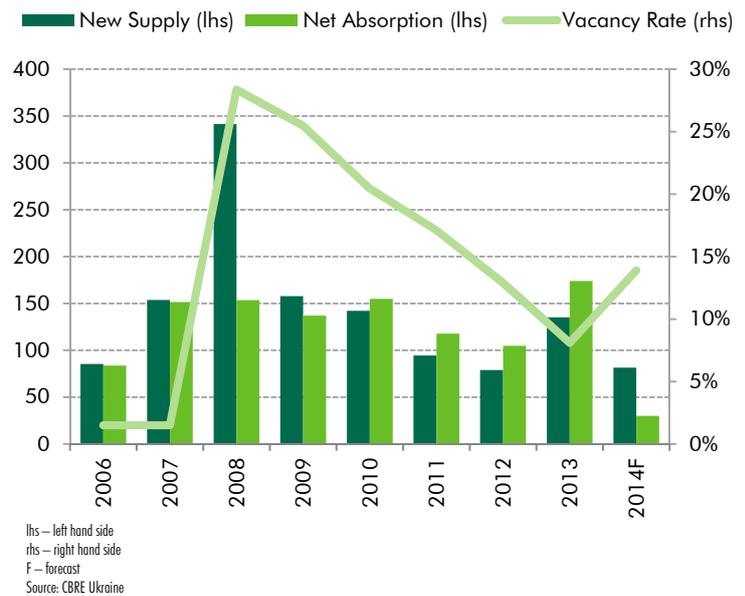
RENTS

The average base rent for prime space for lot size of around 5,000 sq m amounted to \$6.25/sq m/month by the end of 2013. With national currency plummeting over the first six months of 2014 (by ca. 50%), tenants pressured landlords to achieve temporary compromise exchange rates, as most rental contracts are dollar based. Effective 10-25% rent reductions followed for periods of 3 to 6 months. Without accounting for this interim dent in the effective going rents, prime asking rents remained broadly unchanged, with secondary rents going down by 10-20% and ranging between \$4.0 and \$5.5/sq m/month by the end of June.

YIELDS

After three years of relative stability during 2011-2013, the notional prime yield in the warehouse segment increased from 15% to 16% over the first six months of 2014. By the end of Q1, the indicator grew by 0.5 pp, reflecting increased risks of the country.

NEW SUPPLY, NET ABSORPTION AND VACANCY RATE



The following three months of strengthening tension in the economic and political fundamentals added an additional 0.5 pp to the notional prime yield. By the end of 2014 the indicator is likely to remain flat, provided things do not deteriorate further. In the long term, should the situation in the East stabilize, swift compression will be expected.

OUTLOOK

Tensions in Eastern Ukraine have dimmed growth prospects in Ukraine. Therefore, as 2014 is progressing, demand for warehouse premises is likely to remain modest. Due to the increased vacancy rate and weak economic background, rental growth will probably not be apparent in 2014 as it was expected six months ago. Moreover, no new ambient warehouse complexes are expected to enter the market until the end of the current year. At the same time, prime rent is likely to stay level in view of a limited volume of vacant professional warehouse units in sought-after locations, while secondary rents may falter somewhat. Looking ahead, shortage of large modern units for speculative purpose in the medium term is likely to be well felt when recovery begins. However, due to a very short time needed to construct a warehouse, no wild swings in the market should be expected when the economy in general and real estate market starting improving.

DEFINITIONS

(in alphabetical order)

Development Completions (new supply) – represents the total rentable area of completed new and significantly refurbished/renovated (stripped back to shell and core) floor space that has reached practical completion and is occupied, ready for occupation or an occupancy permit, where required, has been issued during the survey period. **Development completion** data includes properties dependant on **total competitive stock** definition or **total stock** definition (see below).

Leasing Activity – represents the total floorspace known to have been let or pre-let, sold or pre-sold to tenants or owner-occupiers during the survey period. Unlike **take-up** (see definition below) it includes sales and leasebacks, renewals, regears, as well as subleases.

Net Absorption (occupancy growth) represents the change in occupied stock within a market during the survey period.

Prime Rent – represents the top open-market tier of rent that could be expected for a unit of standard size commensurate with demand, of highest quality and specification and in the best location in a market at the survey date. **Prime Rent** reflects the level at which relevant transactions are being completed in the market at the time but need not be exactly identical to any of them, particularly if transaction flow is very limited or made up of unusual one-off transactions. If there are no relevant transactions during the survey period, the quoted figure is more hypothetical, based on expert opinion of market conditions, but the same criteria on building size and specification will still apply.

Take-up (gross absorption) – represents the total floorspace known to have been let or pre-let, sold or pre-sold to tenants or owner-occupiers during the survey period. A property is deemed to be taken-up only when contracts are signed or a binding agreement exists. Pre-let refers to **take-up** that was signed either in the planning or construction stage. All transactions (including pre-lets and pre-sales) are recorded in the period that they were signed. Exclusions include space that is under offer, sales and leasebacks (as there has been no change in occupation), contract renewals and renegotiations (unless the occupier took additional space, when only the additional space is included) and subleases.

Total Competitive Stock (speculative stock) – represents the total completed space (occupied and vacant) in the private sector at the survey date, recorded as gross rentable area. Includes purpose-built, space converted from other uses and independent space forming part of a mixed-use development. **Total competitive stock** excludes any buildings that are not considered to be 'competitive' or active in the marketplace. Exclusions include; government and public buildings, where the public sector space is purpose built and owner occupied and the public sector does not engage in the open market; singly occupied properties, occupied by a tenant as the owner or on a long-term lease agreement; properties that are not considered to be actively competitive due to a size threshold, age, use or class. **Total competitive stock = total stock** (see below) - owner-occupied properties.

Total Stock – represents the total completed space (occupied and vacant) in the private sector at the survey date, recorded as gross rentable area. Includes purpose-built, space converted from other uses and independent space forming part of a mixed-use development. **Total Stock** excludes any buildings that are not considered to be 'competitive' or active in the marketplace. Exclusions include; government and public buildings, where the public sector space is purpose built and owner occupied and the public sector does not engage in the open market and properties that are not considered to be actively competitive due to a size threshold, age, use or class.

Vacant Space – represents the total gross lettable (or rentable) floor space in existing properties, which is physically vacant and being actively marketed at the survey date. Space that is physically vacant, but not being marketed or is not available for occupation is excluded from **vacancy**. Space that is **under construction** is also excluded from **vacant space**

Vacant Space Rate represents the percentage ratio of total **vacant space** to **competitive stock**

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