

## Quick Stats

	Change from	
	2010	2009
New supply	↓	↓
Rents	↑	↑
Vacancy	→	↓

## Hot Topics

- Retail sales increased by 14.2% y-o-y in December, bringing the annual turnover growth to 16.7% and spurring demand for retail space
- 45,000 sq m of new supply entered the market in 2011 with a record 251,000 sq m of retail space expected in 2012
- On average rents rose by 5-10% y-o-y, mainly thanks to the strong retailers' activity in the first half of the year

## FUNDAMENTALS

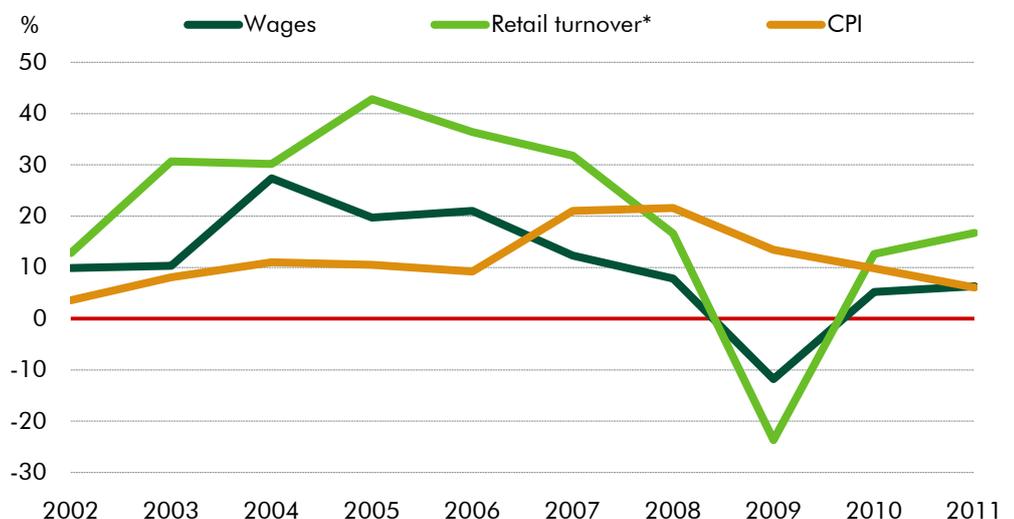
Driven by an upsurge in domestic consumption, the Ukrainian economy grew at a respectable 6.6% rate y-o-y in Q3 2011. Towards the final quarter, however, the growth began to slow amid brewing sovereign debt crisis in the euro zone and worsening global economic outlook, which led to a decline in external demand and brought about a noticeable slowdown in associated industries. At the same time, the negative impact on industrial production was offset by a strong growth in the agricultural sector, where output jumped by a whopping 17.5% y-o-y thanks to a record harvest of wheat. Real GDP growth rate in 2011 is estimated at 4.5 – 5.5%<sup>1</sup>. Forecasts for 2012 vary between 3.5% and 5%.

The official inflation level is recorded at 4.6% y-o-y (down from 9.1% in 2010), which is among the lowest indicators on record. The deceleration in prices is mostly due to contractionary monetary policy pursued by the National Bank, and price level regulation by the government. The expected rate of inflation for 2012 ranges between 7.6% and 10.5%.

Consumer confidence was fluctuating during the first eight months of the year, topping at 81.4 mark (7.3 pp increase since January 2011) in August. As the year drew to an end, pessimistic expectations began to prevail, dragging Consumer Confidence Index down by 6.1 pp in December (according to GfK Ukraine).

Kyiv retail sales grew in H1 2011 on the back of strong consumer demand, which, in turn, was driven by rising real wages, better economic sentiments and an expansion in consumer credit. In the second half of the year, however, as consumer confidence began to weaken, the growth in retail sales went down accordingly. Nevertheless, fuelled by positive trends in the H1 2011 annual retail turnover growth in Kyiv reached 16.6% y-o-y (+4 pp compared to 2010).

### Kyiv Wages, Retail Turnover and Consumer Price Index (% change, y-o-y)



\* - includes organized retail sales only  
Source: Kyiv Statistics Office

<sup>1</sup> - Latest forecasts provided by the following organizations: EBRD, Oxford Economics, Cabinet of Ministries of Ukraine, Ministry of Economic Development and Trade of Ukraine, Troika Dialog, Goldman Sachs, National Bank of Ukraine

Retail sector is heavily dependent on consumer credit availability. Owing to the stable recovery of the banking sector during 2011, credit loans stock has risen by UAH16 bn since the beginning of the year.

## DEMAND

Overall, 2011 was marked by solid retail sales growth spurring retailers' activity. However, starting from September retail operators adopted a more cautious approach towards expansion against the backdrop of worsening consumer sentiment and weaker sales.

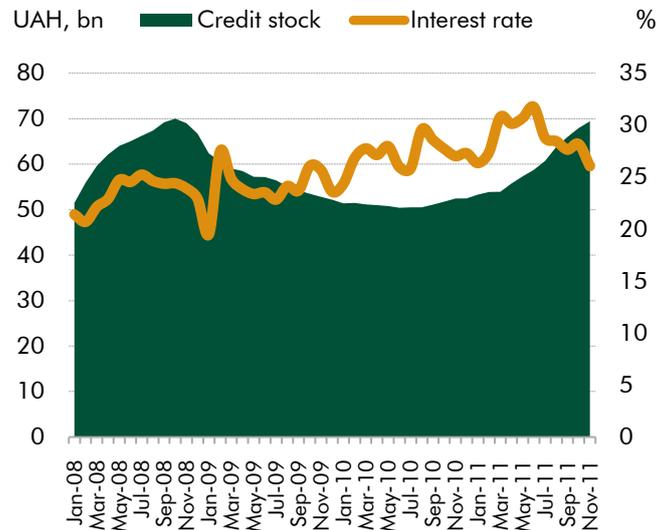
Food retailers expanded most rapidly as they encountered only marginal reductions in consumer demand given that food expenditures are more or less fixed. Major national food retailers (Fozzy, ATB, Novus, EKO, Kviza Treid) vigorously expanded their chains during the year. Moreover, retailers explored new formats: Kviza Treid introduced hypermarket *Velmart* and *VK Select*, a premium supermarket; Adventis opened two discounters *Topmart*.

Fashion retail is more sensitive to changes in consumer confidence; hence retailers of this segment had to deal with a more challenging market, especially in the second half of the year. The same is true for the consumer electronics retailers. They started the year in an optimistic mood and in the first half of 2011 retail sales were rising steadily. However, in H2 2011 concerns over economic instability caused consumers to reign back on their spending.

Despite weakening consumer confidence towards the year-end, 2011 on the whole was characterized by growing demand from retailers. Moreover, 2011 saw several market entries, mainly fashion brands such as *GAP*, *New Yorker*, *Oysho*, *FinnFlare*, *Noa Noa*, etc. in the mid-range segment; *Christian Dior*, *Tru Trussardi* and *Ermanno Scervino* in luxury&business segment.

After years of local chains monopoly in H&B sector, several new players began to surface in 2011. The majority of newcomers entered the market via acquisitions of local retailers. For example, Hong Kong based H&B chain *Watsons* acquired 100% stake in Ukrainian retailer *DC*. Russian H&B retailer *L'Etoile* entered the market with its own brand, but also purchased two local chains – *Brocard* and *Bonjour* - which so far continue to function under their original brands.

## Stock of Consumer Credit\* and Interest Rate in Ukraine



\* - for consumer loans issued in UAH, monthly average weighted rate per annum  
Source: National Bank of Ukraine

## Retail Market New Entries 2011

MID-RANGE FASHION	FOOTWEAR&ACCESSORIES
GAP	a.testoni
New Yorker	Vince Camuto
Oysho	CentrObuv, Centro
FinnFlare	Coccinelle
Noa Noa	Six
Alcott	I am
Ci Mi	Diva
LUXURY&BUSINESS	OTHERS
Christian Dior	Ralph Lauren Home
Tru Trussardi	L'Etoile
Ermanno Scervino	Watsons
	Crafttholic

Source: CBRE

Regarding plans for 2012, retailers still intend to expand albeit at a slower pace. They remain concerned about the impact of a potential crisis on consumer spending, sticking to what they know best and minimizing the risks. According to CBRE research 'How Active Are Retailers in EMEA?', Ukraine's position in the ranking of the countries with most potential for foreign retailers' expansion has dropped from 17<sup>th</sup> to 23<sup>rd</sup> with some players waiting for stability to return before committing to new stores, while others are deterred by the lack of suitable stock.

## SUPPLY

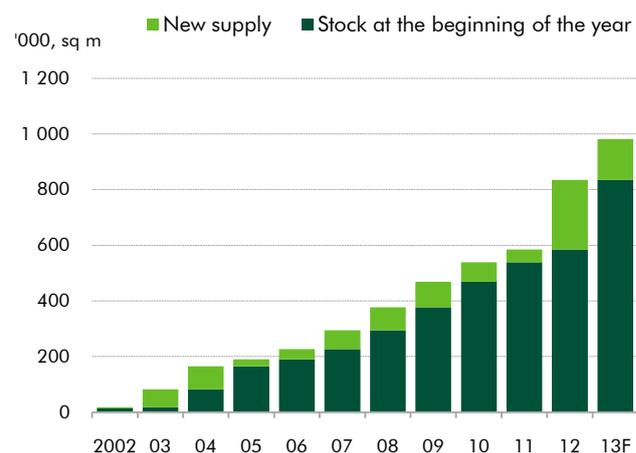
Indeed 2011 provided retailers with little opportunities to expand in Kyiv. The only professional retail scheme delivered in the market during the year is a theme-oriented Phase II of Dreamtown shopping centre (GLA – 45,000 sq m). Thus, Kyiv shopping center<sup>2</sup> stock now numbers some 584,000 sq m of quality retail space. Still, Kyiv market remains one of the least saturated among CEE capitals with only around 208 sq m of quality retail premises per 1,000 people. And even in the unlikely case that all of the ambitious delivery plans for 2012 get realized, the saturation picture will improve only slightly. Should all 251,000 sq m of retail space enter the market as planned, Kyiv provision rate will reach about 300 sq m per 1,000 people, which is still twice below the level of the developed CEE markets, like Warsaw or Prague.

Over the next couple of years the market is expected to expand and undergo a structural change. The average size of a professional shopping centre in Kyiv increased remarkably over the last 3 years. While in 2008 it stood at 17,000 sq m, in 2011 the average GLA of a quality scheme has reached 24,000 sq m, whereas the same indicator for the shopping centers currently under construction is almost twice higher – i.e., 40,000 sq m of GLA. Furthermore, the historical imbalance between Left and Right Bank in terms of retail space provision has started to change. Thus, almost half of the retail space currently under construction is located on the Left bank of the Dnieper River. This shift in developers' preferences can be explained by lower competition and broad target audience living in the immediate proximity - factors that are also driving retailers' interest in that part of the city. Overall, although construction activity increased in 2011, economic uncertainty and tightening of lending terms have led to no development starts recorded in the second half of the year.

Despite the announcements made by some developers throughout the year as to their intention to explore new formats (outlet centers, retail park, etc.), Kyiv E-95 Outlet Center (GLA – 26,000 sq m), was the only project in the segment whose construction began in 2011.

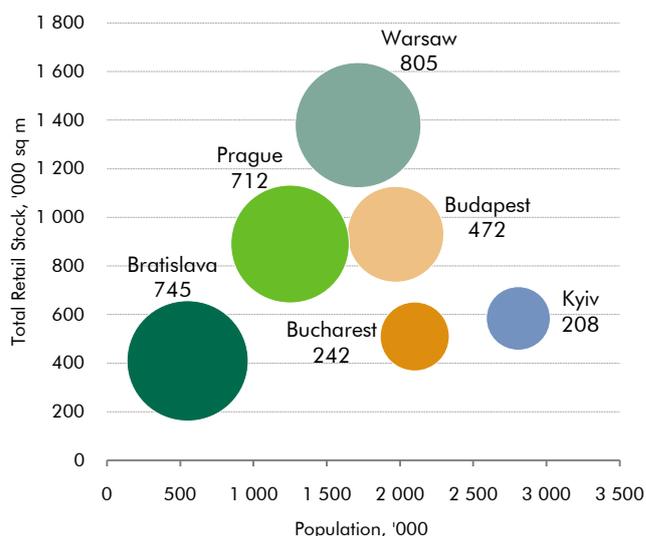
The absolute majority of the schemes under construction are of traditional regional format with about 251,000 sq m scheduled for delivery in 2012,

## Kyiv Shopping Center Stock\*



\* – Shopping center stock was reviewed in 2011. Moreover, retail schemes featuring a hypermarket and a small retail gallery that were previously left out of the stock, have been included into calculations. Annual development completion figures were adjusted accordingly.  
F – forecast  
Source: CBRE

## Retail Premises per 1,000 Inhabitants in Selected CEE Capitals in 2011



Source: CBRE

and another 146,000 sq m forecast to enter the market in 2013. Furthermore, several large projects, such as SC on Zlatoustivska St., Park Gorkogo, Panda Park, Prospect, Kvadrat on Vyrlitysa, etc., are in the process of obtaining all the necessary documents and permits to start construction. Should the delivery of those projects (ca. 450,000 sq m) take place within mid-term perspective (3-4 years), Kyiv market might reach saturation level in terms of traditional retail schemes. However, the chances of the timely delivery of such a massive amount of space are very slim given the established practice of delays in completions.

<sup>2</sup> – [shopping center is] a retail property that is planned, built and managed as a single entity, comprising units and “communal” areas with a minimum gross leasable area (GLA) of 5,000 sq m; the quality of tenant-mix, 50% of which should consist of chain retailers.

## VACANCY AND RENTS

In 2011, the demand for quality properties remained strong, resulting in an average 5-10% growth y-o-y in both prime and secondary rents. That increase was achieved in H1 2011, while in the second half of the year rents remained largely flat amid worsening sales outlook. As of today, prime rents vary between \$100 and \$170/sq m/month (triple net), while secondary rents are within the range of \$55-85/sq m/month for typical gallery units.

Vacancy in prime properties remained close 0% throughout the year, while the average secondary vacancy increased slightly (now stands at 6%) due to slow absorption of space within the newly delivered Dream Town (Phase II). Low demand for premises within the scheme can be attributed to its specialized format - few brand name retailers of the segment present on the market.

## REGIONS

Retail market in the regions has revived in 2011 with developers turning their attention even to smaller cities in response to the growing demand from retailers. The real breakthrough was the opening of three Inditex brands within Magicentr in Vinnytsya (ca. 370,000 ppl). Since the presence of Inditex brands serves as an indication of the scheme/city potential for the majority of other retailers, the Inditex expansion into smaller cities paves the way for quality improvements of the market.

Still, when it comes to new completions of quality schemes large cities remain in the lead, with Kharkiv being in the first rank with over 50,000 sq m delivered in three schemes. Nonetheless, it is worth mentioning that large schemes now operate in the market of smaller cities, such as Zaporizhya, Mariupol and Kremenchuk.

### Typical Lease Terms in Kyiv Shopping Centers

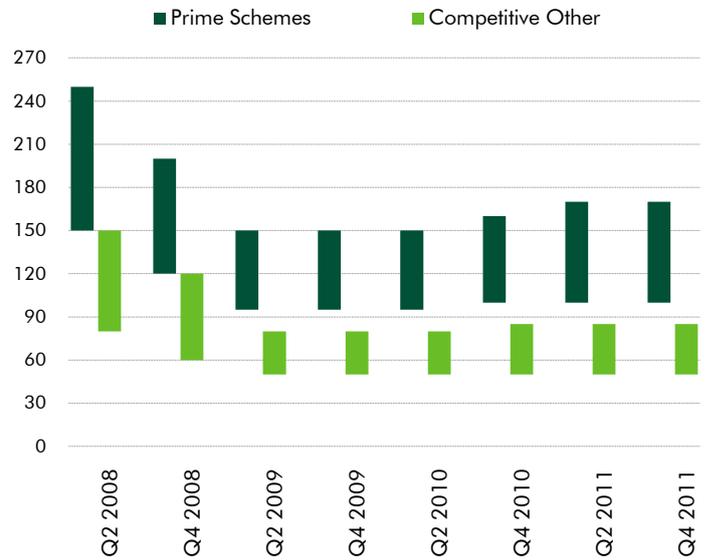
<b>Rent Payment</b>	Rent is paid in advance, on a monthly basis and is quoted exclusive of 20% VAT and service charges. Fixed rent payments per sq m per month of leasable area is a common market practice, but for anchor tenants/major international retailers with significant market power – a turnover rent or mixed type rent (base or % of turnover, whichever is higher) can be applied.
<b>Rent escalation/Rent review</b>	Rents are usually denominated in USD, but payable in Hryvnia at the official USD/UAH exchange rate (according to the National Bank) with monthly adjustments. The rent is typically annually indexed for USD inflation (CPI).
<b>Tenants covenant</b>	Tenant has to provide either a rent deposit or a bank guarantee, typically equivalent to 1-2 months of rent.
<b>Service charge</b>	Service charges generally cover the repair and cleaning of the common areas, management fee, and technical maintenance. Utility costs such as water, heating and electricity are not included and are paid separately per meter. Service charges amount to \$1-2/sq m/month for anchor tenants and \$3-5/sq m/month for other tenants.
<b>Incentives</b>	Tenants are usually given a rent free period of one to two months for the fit-out works. Other incentives such as capital contributions and a longer rent-free period are rare.
<b>Lease length and term</b>	Parties are obliged to notarize rental agreements with duration of over 3 years; therefore leases of gallery tenants are usually signed for 2 years and 11 months. Anchor tenants sign leases for longer periods – up to 10 years.
<b>Repairing liability</b>	A landlord usually undertakes repairs of the structure, common areas and roof. All internal maintenance/repairs is tenant's responsibility.

Source: CBRE

Page 4

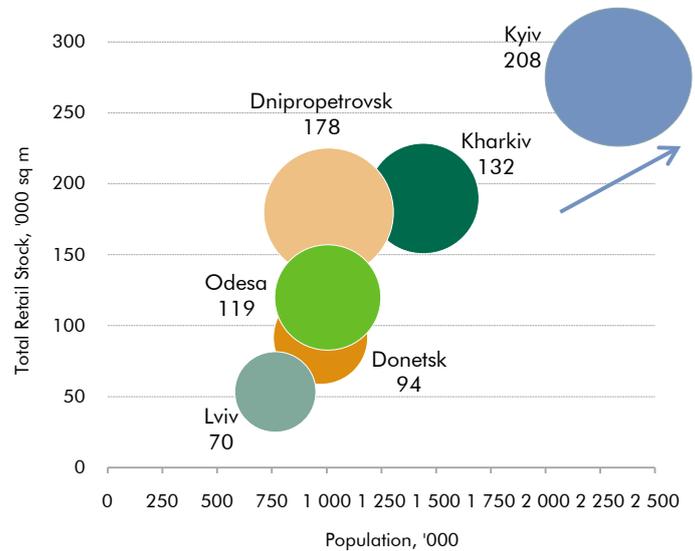
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### Base Rents in Kyiv (USD/sq m/month)



Source: CBRE

### Retail Premises per 1,000 Inhabitants in Ukrainian Largest Cities in 2011



Source: CBRE

## Key Retail Schemes in 2011-2012 in Ukraine

Retail Schemes Delivered in 2011				
NAME	CITY	DEVELOPER	GLA, sq m	COMPLETION/ ANNOUNCED DELIVERY
Magelan (Phase I)	Kharkiv	Kray Property	34,600	2011
Ave Plaza	Kharkiv	AVEC/Uniqa	9,070	2011
Dafi (Phase III)	Kharkiv	Dafi	7,500	2011
Donetsk City (Phase II)	Donetsk	Domus	29,700	2011
Passage	Dnipropetrovsk	Akselrod Estate	13,000	2011
City Mall (Phase II)	Zaporizhyya	Arricano Real Estate	25,000	2011
Ukraina	Mariupol	Local developer	13,300	2011
Galaktyka	Kremenchuk	Local developer	7,000	2011
Future Retail Schemes Under Construction				
City Center (Phase I)	Odesa	GMG Development	30,000	2012
Frantsuzkyi Bulvar (Phase III)	Kharkiv	Aksioma	34,200	2012
Magelan (Phase II)	Kharkiv	Kray Property	27,900	2012
Cascade Plaza (Phase I)	Dnipropetrovsk	Alef Estate	13,000	2012
Karavan (Phase III)	Dnipropetrovsk	Lex Holding	9,800	2012
SC on Evpatoriyske Highway (Phase I)	Simferopol	Krymska Developerska Compania	20,000	2012
Fabryka	Kherson	Bud House Group	65,000	2012
Suvorovskiy	Kherson	Local developer	32,000	2012
Lubava	Cherkasy	Bud House Group	18,000	2012

Source: CBRE

## YIELDS

Despite the fact that retail property market was one of the most dynamically growing real estate segments in 2011, there were no pure investment deals in professional segment. Prime yields declined by 1 pp to 13% during the first half of the year, but stayed broadly stable throughout the rest of 2011 on the back of weakening economic outlook. It should be noted that in the absence of investment deals, the specified yield is only theoretical. Even as there were no investment transactions, the market still witnessed a few development deals as well as acquisitions of land intended for retail use, mainly completed in H1 2011.

## OUTLOOK

Growing retail sales provided a strong background for retailers' expansion plans and resulted in a number of market entries in 2011. Closer to the year-end, however, retailers became increasingly careful about their expansion plans. Occupiers remain firmly focused on prime retail space, and there is little chance that this will spread out into more secondary locations while economic uncertainty persists.

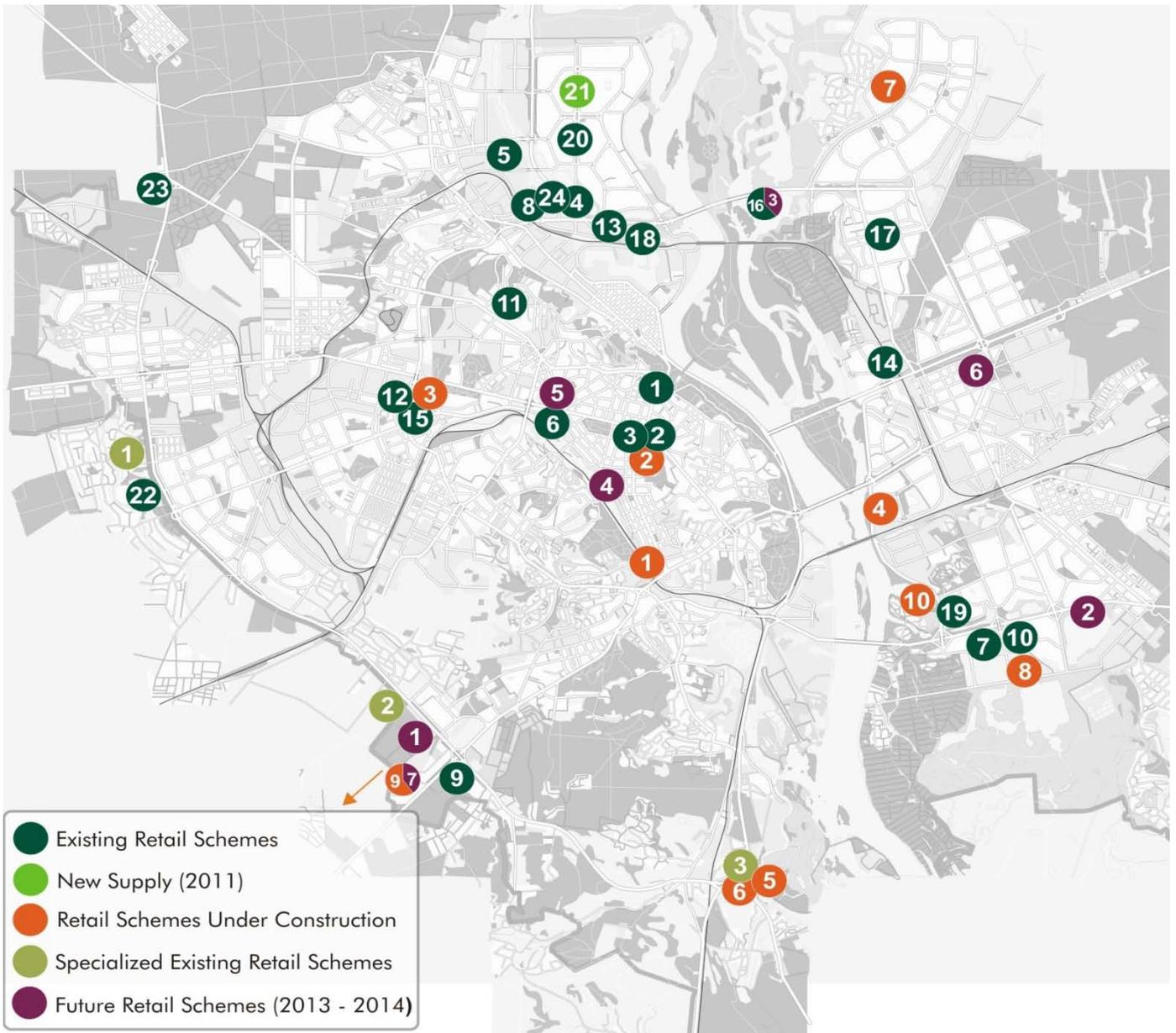
Forecast competitive retail space completions for 2012 hit the record height of 251,000 sq m. Should the cautious approach currently used by retailers

prevail throughout 2012 it might take up to 12-18 months for the new supply to be absorbed. Forecast new supply, however, is unlikely to be delivered onto the market in its totality, taking into account the history of chronic delays in completions.

The vacancy in prime segment is expected to remain close to zero since retailers are concentrating on the best locations; however with expansions on hold, we do not see grounds for rapid growth of prime rental rates either. Small upward movement is possible, but is likely to stay within 3-5% range in sought-after locations. We expect secondary vacancy to go up on the back of large new additions to the market, with rents stabilizing on the level seen in 2011 provided there are no shocks to the economy.

Although Kyiv market is still perceived by developers as one of priority destinations for development, regional markets provide more opportunities for growth given their low saturation with professional retail schemes. Following the developers' strong last year's activity in smaller cities we expect to see a growing number of completions in Tier 2 and 3 cities.

# KYIV SHOPPING CENTERS



Existing Retail Schemes			
#	NAME	GLA, sq m	COMPLETION/ANNOUNCED DELIVERY
1	Globus	18,600	2001-2002
2	Mandarin Plaza	9,400	2003
3	Arena City	8,000	2005
4	Gorodok	10,000	2003
5	Karavan (Phase I, II, III, IV)	37,900	2003-2008
6	Ukraina	24,000	2003
7	Aladdin (Phase I, II)	10,200	2004-2005
8	Alta-Center	17,000	2004
9	Magelan	22,400	2004
10	Piramida	12,000	2004

Existing Retail Schemes			
#	NAME	GLA, sq m	COMPLETION/ANNOUNCED DELIVERY
11	Promenada Center (Phase I,II)	22,000	2003-2004
12	Bilshovyk (Phase I,II,III)	65,000	2006-2009
13	Plazma	8,800	2006
14	Komod	10,000	2007
15	Arcadia 1	15,800	2007
16	Sky Mall (Phase I,II)	67,000	2007-2010
17	Kvadrat on Perova	19,100	2008
18	Blokbaster	25,500	2008
19	Arcadia 2	18,400	2008
20	Dream Town (Phase I)	41,000	2009
21	Dream Town (Phase II)	45,000	2011
22	Promenada Park (Phase I, II)	43,000	2009-2010
23	Auchan Belichi	17,400	2009
24	Auchan Petrivka	16,800	2008
Specialized Existing Retail Schemes			
1	4Room	22,230	2009
2	Araks	28,000	2009
3	Domosphaera (Phase I)	22,300	2009
Retail Schemes Under Construction			
1	Ocean Plaza (Phase I)	72,000	H1 2012
2	Gulliver (Continental/Esplanada)	38,000	H1 2012
3	Marmelad	38,700	H1 2012
4	Silver Breeze	21,000	H1 2012
5	Domosphaera (Phase II)	30,000	H2 2012
6	Alacor City	28,400	H2 2012
7	RayON	22,700	H2 2012
8	Kyiv Mall	75,400	H1 2013
9	Kiev E95 Outlet Centre (Phase I)	15,800	H1 2013
10	River Mall	55,000	H2 2013
Future Retail Schemes			
1	Panda Park	139,000	n/a
2	Kvadrat on Vyrlytsya	80,400	n/a
3	Sky Mall (Phase III)	46,500	n/a
4	Park Gorkogo	64,500	n/a
5	SC on Zlatoustivska	71,600	n/a
6	Prospect	41,000	n/a
7	Kiev E95 Outlet Centre (Phase II)	10,220	n/a

Source: CBRE

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