

Kyiv Office Market

Prime rents remain largely unchanged amid scarce supply and growing demand

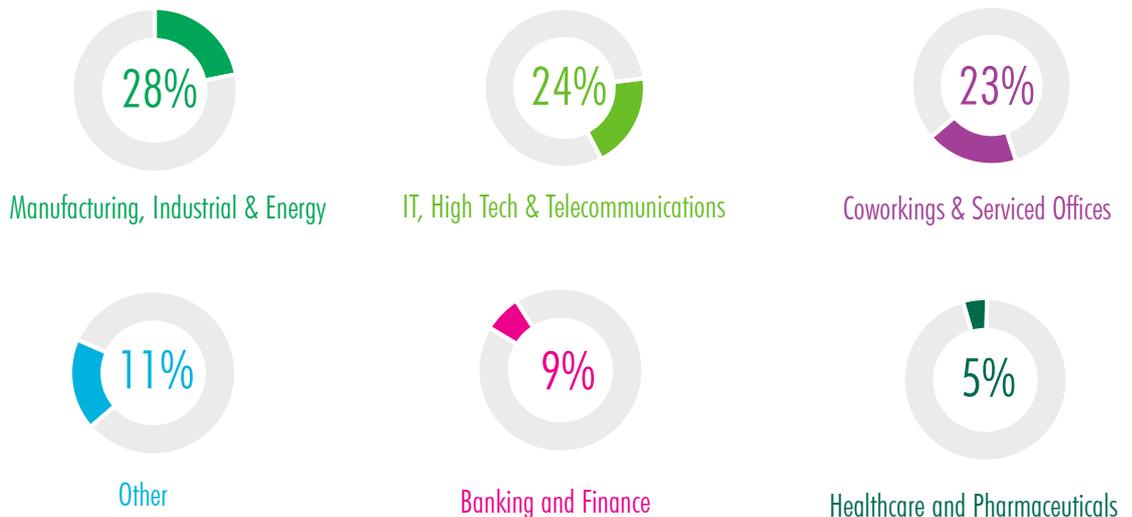


Demand

As of H12019, take-up in Kyiv office market was decreasing after a strong demand in 2017-2018, which, at the time, was a result of companies relocating on the back of positive business outlook and moderately growing economy. In H12019, resulting in a take-up of 65,800 sqm (-19% y-o-y), while total leasing activity, which includes the amount of renewals, amounted to 105,200 sqm (+4.2% y-o-y). As a result, take-up in H12019 decreased, as number of new entries and expansions has noticeably contracted. The market reached its peak in total leasing activity in H22017 when take-up amounted to 95,000 sqm. Since H22017, the take-up volume has been decreasing.

The most part of remaining vacant stock was leased in 2017-2018, producing scarcity of high quality office on the market. Despite the demand remaining strong in H12019, lack of high grade properties affected the amount of take-up. To mark a change in market dynamics, Manufacturing & Energy companies took the largest share of take-up in H12019 28% (+27 pp YTD). IT, High Tech & Telecommunication companies, however, still represented the highest number of transactions due to the fact that the average unit size for the segment was smaller. Overall, however, the trend of growing space requirements from IT,

Figure 1: Total Take-up Structure by Industry (% share)



Source: CBRE Ukraine

High Tech & Telecommunications companies decreased substantially in H12019, with the share of total space leased reaching ca. 24% (-16 pp YTD) in the total take-up. As a result of the significant growth of coworking companies in H12019, Business Services segment was divided into Coworkings & Serviced Offices and Business Services segment represented by all other companies in the industry (lawyers, auditors, consultants, etc.). In H12019, Coworkings & Serviced Offices accounted for 23%, whereas Business Services represented only 3% of take-up (-19pp YTD), followed by other industries,

including Healthcare & Pharmaceuticals, Mass Media & Advertising, Transport & Logistics, Wholesale & Retail, Banking & Finance and other sectors that made up the remaining 22%. The expansions in H12019 took the largest share in the total take-up structure representing 45% of total amount. The share of new entries rose to 12%, correlating with an improved business sentiment over the H12018-H12019 period. Relocations accounted for 17% in H12019, which can serve as evidence of depletion of value-added opportunities in a growing market. Relocation & Expansions represented 26% of take-up.

Table 1: Key Office Lease Transactions in H12019

| OCCUPIER | INDUSTRY | PROPERTY | ADDRESS | TRANSACTION TYPE | GLA SQ M |
|---------------------------|------------------------------------|-------------------------|----------------------------|----------------------|----------|
| Confidential | Manufacturing, Industrial & Energy | Office Scheme | 22-24 Hoholivska St. | Relocation&Expansion | 9,000 |
| EPAM | IT, High Tech & Telecommunications | Europassage | 58/10 Simyi Prakhovykh St. | Expansion | 7,100 |
| DTEK Academy | Manufacturing, Industrial & Energy | Unit City Business Park | 3 Dorogozhytska St. | Relocation&Expansion | 4,400 |
| Confidential | Coworkings & Serviced Offices | Paladis | 25 Sichovykh Striltsiv St. | New entry | 4,000 |
| Confidential | Banking and Finance | Astarta | 58 Yaroslavska St. | Expansion | 3,900 |
| Platforma | Coworkings & Serviced Offices | Office Scheme | 35 Borychev Tok | Expansion | 3,900 |
| Metinvest | Manufacturing, Industrial & Energy | Unit City Business Park | 3 Dorogozhytska St. | Relocation&Expansion | 2,500 |
| Creative States | Coworkings & Serviced Offices | Gulliver | 1A Spartyvna Sq | Expansion | 1,800 |
| Regus | Coworkings & Serviced Offices | IQ | 13-15 Bolsunovska St. | Expansion | 1,800 |
| Mangrove Capital Partners | Banking and Finance | Gulliver | 1A Spartyvna Sq | Expansion | 1,800 |
| Grammarly | IT, High Tech & Telecommunications | Gulliver | 1A Spartyvna Sq | Expansion | 1,400 |
| SoftServe | IT, High Tech & Telecommunications | Forum West Side | 6 Oleny Telihy St. | Relocation&Expansion | 1,300 |

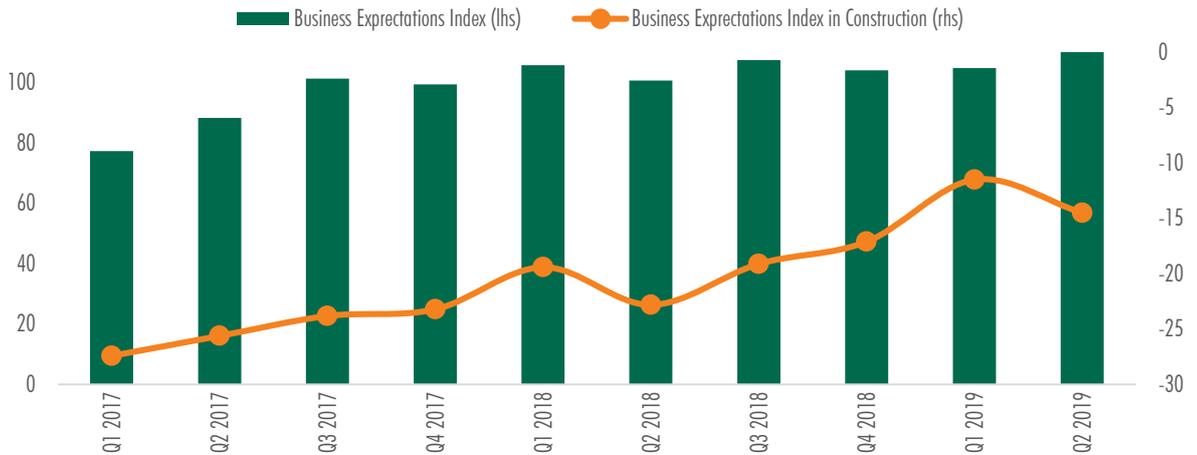
Source: CBRE Ukraine

Supply

The business expectations index and the business expectations index in the construction posted positive dynamics over the 2017-2019 period. In H12019 business expectations index increased by 6.6 pp YTD to 110.7%. Looking at the business expectations index in construction, it improved to -14.5% (+2.6 pp YTD) in H12019, albeit the sentiment remained broadly negative and the index decreased slightly in Q22019 (-3 pp q-o-q). According to Ukraine State Statistics Committee, the major factors negatively impacting business

expectations in construction were financial constraints (44% of surveyed companies), insufficient demand (26% of surveyed companies), and weather conditions (18% of surveyed companies). Furthermore, the share of construction companies that considered financial constraints as the major factor restraining construction, slightly decreased (-4% YTD), as well as the number of those who considered demand insufficient also declined (-4% YTD).

Figure 2: Kyiv Business Expectations and Business Expectations in Construction Over the Next 12 Months



lhs – left hand side; rhs – right hand side

Source: Ukraine State Statistics Committee

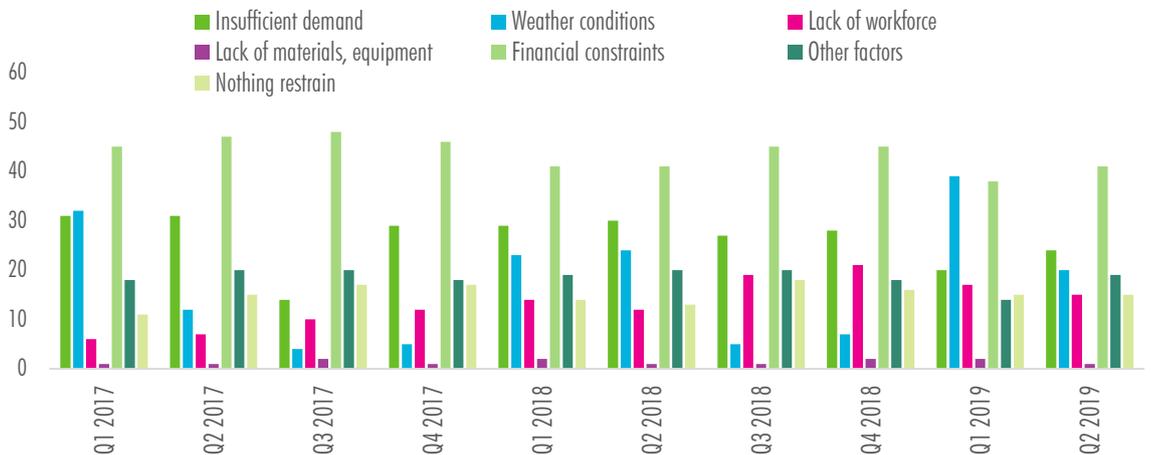
Surprisingly enough, the major negative factor that significantly added to negative construction sentiment was adverse weather conditions (+20% YTD). The share of construction companies, which responded that “no restraints” affected their business remained broadly the same at 15% (-1% YTD).

New supply of H12019 amounted to meager 30,600 sqm, with total competitive stock remaining largely unchanged at 1.76 mio sqm (+1.7% YTD), taking into account that some properties became owner-occupied (64,400 sqm over 2007-H12019). Among new additions to the stock were only small size properties in Palo Alto (5,000 sqm) at 10 Starokyivska St., Zitadelle BC (3,800 sqm) at 3 Tsyadelnna St., Amarcord BC (6,700 sqm) at 30 Holosiivskyi Ave., Unit.City (B10)

(10,400 sqm) at 3, Dorohozhytska St., and two office schemes of 2,200 sqm at 14A Lypkivskoho St. and 2,500 sqm at 28 Dniprovskna Naberezhna). Although new supply in H12018 was scarce (only 2,200 sqm were delivered), it rose substantially to 57,800 sqm in H22018 totaling 60,000 sqm of new completions as of the end of the year. Overall, new supply was insufficient to meet a healthy demand alongside decreasing vacancy and growing rental rates over the last 18 months in terms of the whole market.

Looking at projects in the pipeline, 12 office projects are set for completion in H22019 with a total area of ca. 118,400 sqm. Some projects are expected for delivery at the end of Q32019 including Avenue 53 BC (18,500 sqm) at 53, Peremohy Ave., where 12,000 sqm has been

Figure 3: Business Expectations in Construction by Factors of Influence, 2017-2019



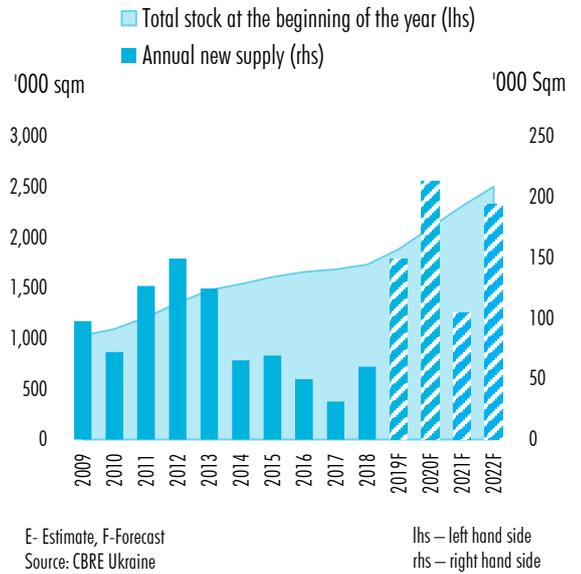
Source: Ukraine State Statistics Committee

already pre-leased by a potential tenant, the Office Scheme at 22-24 Hoholivska St. (9,000 sqm), which is fully pre-leased by a Manufacturing, Industrial & Energy company, and Office Scheme at 10, Myhailivska St. (3,500 sqm). The total new supply projected for 2020 amounts to ca. 213,300 sqm and the additional ca. 300,000 sqm are planned for completion in 2021-2022, which, if delivered, will slow down general rental growth and should keep the market at a healthy state of supply-demand equilibrium. However, the amount of new supply, which will be actually delivered on the market, might be lower, taking into account that the average percentage of actual completions in the new supply planned for the particular period was below 50% during last two years.

Vacancy and Rents

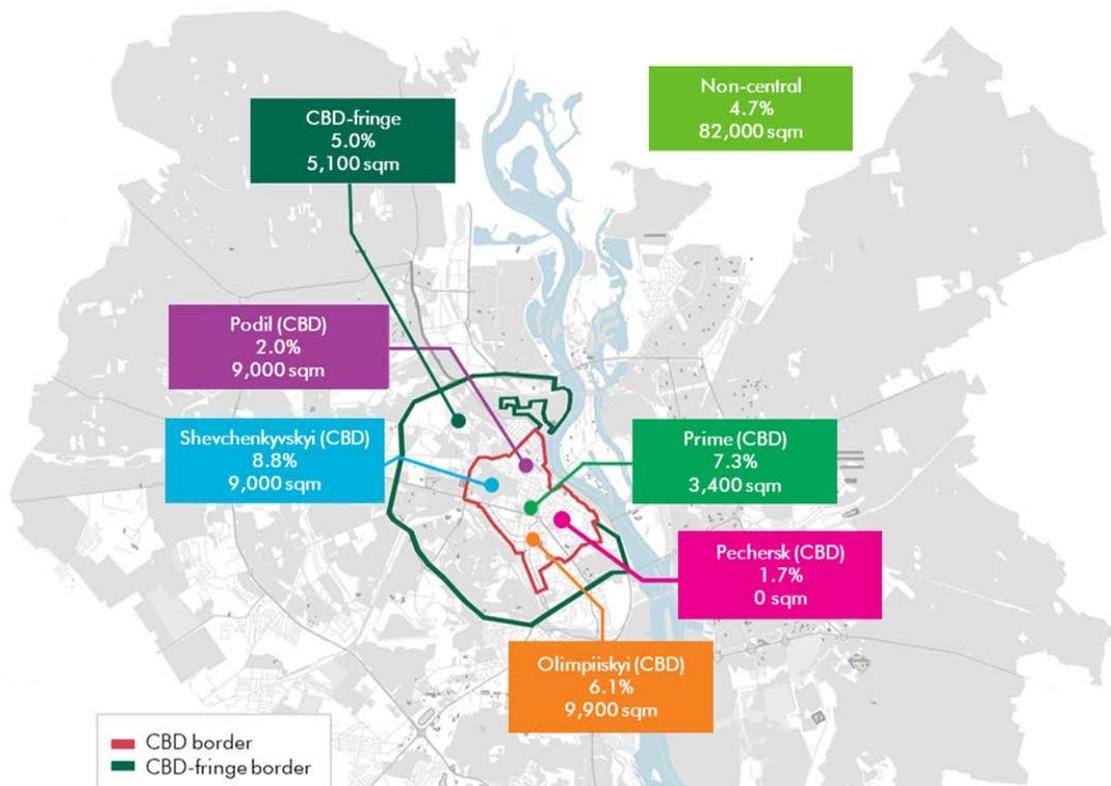
As of H12019, CBRE Ukraine recalculated vacancies retrospectively based on a new methodology. Starting from H12019, vacancy in office market is calculated based on an 80% sample of office centers in Kyiv, which is constantly updated and accounts for new competitive deliveries. Prior methodology, which allowed for more weight being given to a

Figure 4: Kyiv Annual Development Completions and Total Competitive Stock ('000 sqm)



qualitative opinion, has thus been replaced with a more scientific approach appropriate for a more developed market which Kyiv is gradually becoming. According to the new methodology, in H12019 the average vacancy increased slightly from 4.3% to 4.9% (+0.6 pp YTD) as a result of migration of smaller companies from more to less professional properties due to a higher rental

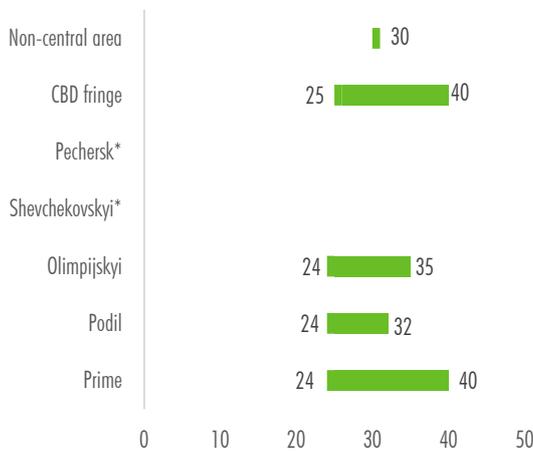
Vacancy Rate (%) and Projected New Supply for H22019 (sqm) on the Map of Kyiv Office Submarkets



growth in higher grade properties. The vacancy reported under prior methodology accounted for 9.8% as of the end of 2018, whereas the vacancy recalculated under new approach accounted for 4.9%. Delivery of several small office schemes in H12019 did not significantly contribute to growth of average market vacancy, as majority of new space was pre-leased. Despite rental appreciation demand for A-class properties across two CBD submarkets remained strong. The average vacancy for A class premises was slightly higher at 5.1% compared with vacancy for B class offices at 5% as of H12019. The lowest vacancy was registered in Pechersk 1.7% (+1.3 pp YTD), and Podil 2% (+0.6 pp YTD), whereas the highest vacancy was in Prime submarket 7.3% (+1.9 pp YTD) and Shevchenkyvskyi submarket 8.8% (-1.2 pp YTD).

Prime effective rent for A-class properties remained stable at \$25/sqm/month. The lower bound of the asking rental range of A-class and B-class properties grew by +41% YTD (\$17/sqm/month in H22018) and +17% YTD (\$12/sqm/month in H12018) respectively. As such, asking rents for class A properties stood in the \$24-\$40/sqm/month range, with B class properties averaging \$14-\$27/sqm/month. Significant gap between the lower and the upper bounds of the ranges is determined by characteristics of the leased unit, with fit-out condition and location of the property being the determining factors for noticeably higher rates.

Figure 6: Kyiv A-class Asking Base Rental Range¹ by Submarket of H12019 (USD/sqm/month)



¹Range includes office space for lease in different fit-out conditions

*No vacant premises as of research date

Source: CBRE Ukraine

Figure 5: Vacancy in Kyiv Office Market, 2011-H12019 (data revised retrospectively)



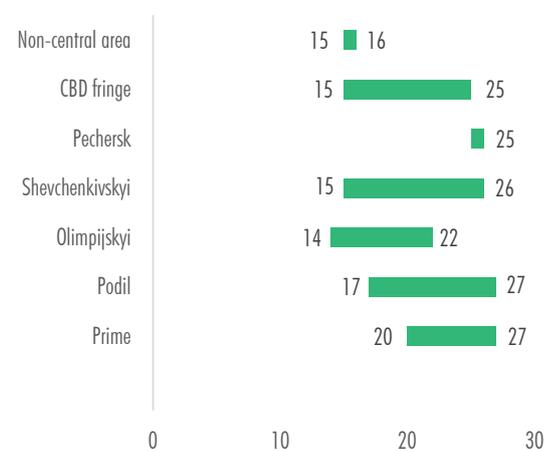
lhs – left hand side; rhs – right hand side

Source: CBRE Ukraine

Investment

In H12019, the volume of investment transactions decreased substantially to reflect political uncertainty in the country and amounted to meager \$15 mio (purchase of Incom BC by Merx Group in Q2019). Nonetheless, despite the fact that there was only one investment transaction in H12019, four development investments in the amount of \$57 mio were also made in H12019. One of them was represented by Block 4 of Arsenal Plant, purchased with a view for reconstruction into a mixed-use property containing office, retail, and residential space.

Figure 7: Kyiv B-class Asking Base Rental Range¹ by Submarket of H12019 (USD/sqm/month)



The transaction was made between Ukrgazbank and IntergalBud for the amount of ca. \$21 mio. Another notable development transaction in H12019 was the sale by VTB Bank of unfinished Sigma BC at 6 Vatslava Havela Blvd to Merx Group for the reported amount of ca. \$13.2 mio. Prime yields remained broadly unchanged despite political uncertainty, standing at 11.75%. The major factors impacting investment sentiment in H12019 were political risks associated with the Presidential elections and ensuing Parliamentary elections, along with the imminent change of government. An additional factor restricting investment is lack of new supply and continued absence of international players on the Ukrainian real estate commercial market. Whereas some of the first steps undertaken by the new President have been interpreted as positive for the market, potential investors mostly remain in the wait-and-see mode until the new Parliament and Government become operational and start making decisions. Summing up the results of H12019, it should be noted that new development on office market becomes more justified, particularly under conditions of a growing new supply and increasing rental rates.

Outlook

In the second half of 2019 the demand from occupiers is expected to continue growing due to a strengthening business sentiment and continued expansion of mainly IT, High Tech & Telecommunications sector. Supply-wise, the long-awaited new deliveries of ca. 118,400 sqm are expected to enter the market by the end of 2019. Despite these new additions to supply, prime rents

are likely to post a modest increase by the end of 2019 in the face of low vacancy, new supply being of predominantly A/B location and quality, as well as existence of a substantial volume of delayed demand due to an extended period of near no new supply.

Given the fact that both of this year's elections have not produced a shake-up to the economy, with the Ukrainian currency demonstrating unexpected strength, we forecast the delivery of most of the projects currently under construction in a timely manner. The investment volume in 2019 is likely to remain subdued, with only few high quality investment opportunities available for sale at the moment and investors unlikely to commit funds until early 2020. At the same time, the gap in asking and actual prices paid by investors remains significant. Building on the trend of stable economic environment, investment market is expected to grow over the 2020-2021, as new construction projects become available and new players enter the market – both on investment and development side. The average vacancy is likely to see moderate growth in H22019, attributed to new deliveries. As such, the indicator can potentially drift upwards to the level of 6%-7% by the end of 2019, which will not produce any noticeable effect on broad market trends.

Key Office Market Indicators Summary and Outlook



NEW SUPPLY

| | |
|---------|-----------------|
| H1 2018 | 2.2 ('000 sqm) |
| H1 2019 | 30.6 ('000 sqm) |
| H2 2019 | Upward Trend |



AVERAGE VACANCY

| | |
|---------|--------------|
| H1 2018 | 12% |
| H1 2019 | 4.9% |
| H2 2019 | Upward Trend |



TAKE-UP

| | |
|---------|-----------------|
| H1 2018 | 81.0 ('000 sqm) |
| H1 2019 | 65.8 ('000 sqm) |
| H2 2019 | Upward Trend |



PRIME RENT

| | |
|---------|------------------|
| H1 2018 | \$23 (sqm/month) |
| H1 2019 | \$25 (sqm/month) |
| H2 2019 | Upward Trend |

Source: CBRE Ukraine

Table 2: Office Pipeline for 2019-2023

| NAME | CLASS (QUALITY & LOCATION) | ADDRESS | GLA, SQM | STATUS |
|--|----------------------------|---------------------------------------|----------|----------------|
| H22019 | | | | |
| Avenue 53 (Phase I) | AC | 53 Peremohy Ave. | 18,500 | U/C |
| New Wave | BC | 98 Stepana Bandery Ave. | 15,000 | U/C |
| BC Saha | AA | 1B P. Sahaidachnoho St. | 9,000 | U/C |
| Office Scheme (Merx Group) | BA | 22-24 Hoholivska St. | 9,000 | Reconstruction |
| Forum Amurska Phase I | BC | 6 Amurska St. | 12,000 | U/C |
| Office scheme | BC | 10-14 Dniprovska Naberezhna St. | 3,500 | U/C |
| Azor | BC | 8 M.Maksymovycha St. | 5,400 | Reconstruction |
| Office scheme | BA | 10 Myhailivska St. | 3,400 | U/C |
| Sigma BC | BC | 6 Vatslava Havela Blvd. | 18,600 | U/C |
| Office scheme | AC | 7A Parkovo-Syretska St. | 9,000 | U/C |
| Kooperator BC | AA | 53/80 Saksahanskoho St. | 9,900 | Reconstruction |
| UNIT.City (B11) | AB | 3 Dorohozhytska St. | 5,100 | U/C |
| 2020 | | | | |
| UNIT.City (B14) | AB | 3 Dorohozhytska St. | 8,900 | U/C |
| UNIT.City (B15) | AB | 3 Dorohozhytska St. | 7,700 | U/C |
| UNIT.City (B16) | AB | 3 Dorohozhytska St. | 9,100 | U/C |
| UNIT.City (B17) | AB | 3 Dorohozhytska St. | 12,400 | U/C |
| K/MOST BC | AB | 5A Zoolohichna St. | 5,500 | U/C |
| Office scheme Phase I | AA | 4-6 Korolenkivska St. | 20,000 | U/C |
| Retroville | BC | 47 Pravdy Ave. | 11,100 | U/C |
| Office scheme | AA | 12 Myhailivska St. | 8,600 | U/C |
| Office scheme (former Voronin factory) | BA | 3 Korolenkivska St. | 19,500 | Reconstruction |
| Office scheme | AB | Dehtiarivska St./Zoolohichna ST., 21G | 11,000 | U/C |
| Arsenal Plaza | BA | 8 Moskovska St. | 50,000 | Reconstruction |
| Office scheme (former Arsenal plant block) | BA | 8B Moskovska St. | 11,700 | Project |
| Arsenal K 14 | BA | 8 Moskovska St. | 7,900 | Project |
| Zoranyi | BA | 31/33 Moskovska St. | 7,800 | Reconstruction |
| BC Lukyanivskyi | BB | 2/10 Yu.Illienka St. | 22,000 | U/C |
| 2021 | | | | |
| UNIT.City (B0) | AB | 3 Dorohozhytska St. | 7,600 | U/C |
| UNIT.City (B18) | AB | 3 Dorohozhytska St. | 18,900 | U/C |
| The Magnett BC Phase I | AB | 139 Velyka Vasylkivska St. | 33,000 | U/C |
| Office scheme Phase II | AA | 4-6 Korolenkivska St. | 40,000 | U/C |
| Office scheme | BA | 36 Volodymyrivska St. | 5,200 | Reconstruction |
| 2022 | | | | |
| UNIT.City (B1) | AB | 3 Dorohozhytska St. | 12,000 | U/C |
| UNIT.City (B2) | AB | 3 Dorohozhytska St. | 7,800 | U/C |
| UNIT.City (B3) | AB | 3 Dorohozhytska St. | 9,600 | U/C |
| The Magnett BC Phase II | AB | 139 Velyka Vasylkivska St. | 10,000 | U/C |
| Office Scheme | BA | 24 Zhylyanska St. | 25,000 | Project |
| SkyTowers | AB | 13 Peremohy Ave. | 130,000 | Project |

Source: CBRE Ukraine

DEFINITIONS (in alphabetical order)

CBD – central business district

Leasing Activity – represents the total floor space 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. For offices, the **prime rent** should represent the typical “achievable” open market headline rent which a blue chip occupier would be expected to pay for:

- an office unit of standard size commensurate with demand in each location, typically 500 sqm
- an office unit of highest quality and specification within the local market
- an office unit within the prime location (CBD, for example) of a market

Take-up (gross absorption) – represents the total floor space 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 (unless the occupier took additional space, when only the additional space is included).

Total Competitive Stock – represents the total completed space (occupied and vacant) in the private sector at the survey date, recorded as gross leasable 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.

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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