

Kyiv & Regions Retail Market, H1 2020

Adverse Impact of COVID-19 on Sales Volume Results in Higher Demand for Turnover-Linked Leases



Demand

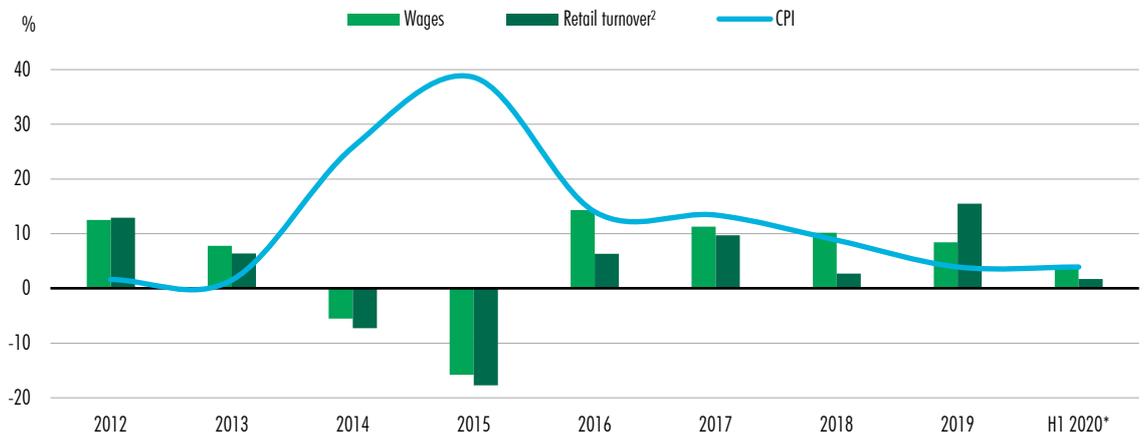
In the beginning of 2020, the overall sentiment of the retail market was quite sound up until February, with consumer demand continued to expand, thereby stimulating growth of retail turnover by +11.1% y-o-y in January-February. However, the COVID-19 pandemic weighed heavily on the national retail market starting from March, eventually resulting in the modest +1.7% YTD Kyiv retail turnover expansion by the end of H1, the lowest it has been since 2015. Real wage index shrank considerably by the end of H1, albeit still remaining positive (103.8) and roughly in line with the CPI (103.9), which has reached nearly historic lows due to sound monetary policy on the part of NBU over the last several years.

Bricks-and-mortar fashion segment saw modest development dynamics, with only a handful new brands entering the market this year to date. Most notable market entries were two Danish brands

b.young (Mid-Range Fashion brand) and *Fransa* (Value Denim brand), a Polish brand *4F* (Specialist Clothing) and a US brand *Vans* (Specialist Clothing). The long-awaited opening of Swedish DIY furniture brand *IKEA* was announced for H2 2020 after initial launch of online store in the beginning of the year. The retailer is expected to occupy approximately 5,000 sqm in the capital's Blockbuster Mall in the format of *IKEA* city store.

Before the lockdown necessitated by COVID-19, a few major trends were evident on the market. In food retailing, traditional grocery retailers were gradually substituted by modern retail chains. Modernization of existing stores was also an ongoing trend, with increasingly more stores providing self-service checkouts across the city.

Figure 1: Kyiv Wages, Retail Turnover and Consumer Price Index (% change, y-o-y)¹



¹ Excluding the temporarily occupied territories, the Autonomous Republic of Crimea, the city of Sevastopol and part of the anti-terrorist operation zone.

² Includes organized retail sales only; *Latest available data as of the end of June

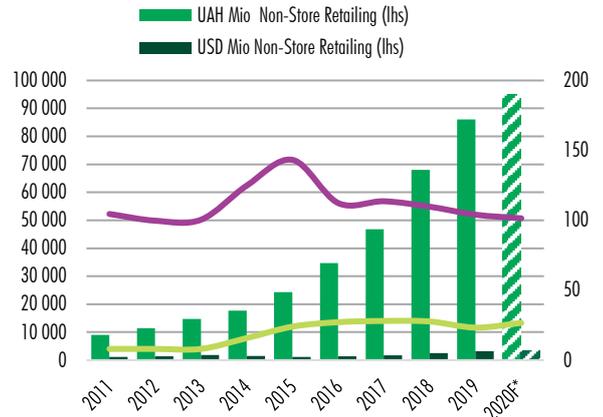
Source: Kyiv Statistics Office

In addition to faster payment turnover at cash registers, self-checkout areas resulted in optimization of space. Convenience store continued expansion galore throughout the country. With the improvement in accessibility of 4G mobile networks, performance of e-commerce sales increased considerably, where electronics and apparel products led in online sales structure. According to Euromonitor International data, compound annual growth rate of e-commerce sales in Ukraine over the past 5 years was averaging at ca. 27%. Noteworthy is the fact that the Kyiv retail market also saw the development of online-to-offline commerce strategies, also known as click-and-mortar. One of the largest online retailers in Ukraine *Rozetka* opened their first offline store in 2017 and now operates 10+ offline shops in Kyiv. Another large Ukrainian beauty e-commerce player *Makeup* announced plans to launch their first physical location in Kyiv, looking to take up ca. 270 sqm in Atmospha SC.

Supply

Over the last 6 months 80,700 sqm of GLA have been added to the shopping center stock with the single completion of Retroville SC in Kyiv, thereby increasing total shopping center volume to 1.4mio (+6.3% YTD). According to developers' statements, around 493,000 sqm of new shopping center premises are currently under construction and expected for delivery in 2020-2021. Meanwhile, only Phase II of April Mall (49,600 sqm) is planned to be completed in the second half of 2020. 2020 is thus set for a slowdown in new completions after record breaking 178,000 sqm delivered in 2019, the largest new volume supplied to the market over the past 10 years. The opening of River Mall SC in 2019 added a quality tenant mix to the shopping center stock of the left bank of the city, where only 23% of total competitive stock volume is located. Given such scarce competitive supply and a growing number of business class residential premises in Osokorky and Posniaky districts, River Mall raised the bar of shopping center competition in the area. Similarly, Piramida SC is currently undergoing expansion works designed to enlarge the food court and create an entertainment area.

Figure 2: Desktop and Mobile Retail Sales in Ukraine (excl Sales Tax) in Historic Nominal Prices (incl Inflation)



Source: CBRE Ukraine

Table 1: Cross-Border Market Entry in Kyiv Shopping Centers in H1 2020

| BRAND | RETAIL SECTOR | ENTRY LOCATION |
|---------|---------------------|----------------|
| b.young | Mid-Range Fashion | River Mall |
| Fransa | Value and Denim | River Mall |
| Vans | Specialist Clothing | River Mall |
| 4F | Specialist Clothing | Retroville |

Source: CBRE Ukraine

Table 2: Potential Cross-Border Market Entry in Kyiv Shopping Centers

| BRAND | RETAIL SECTOR | ENTRY LOCATION |
|--------------------|--------------------------------|----------------|
| IKEA | Homeware and Department Stores | Sweden |
| Kipling | Specialist Clothing | Belgium |
| The Kooples | Luxury and Business | France |
| FLO | Value and Denim | Turkey |
| Funday | Value and Denim | Russia |
| Elisabetta Franchi | Luxury and Business | Italy |
| The Athletes Foot | Specialist Clothing | United States |
| Stella McCartney | Luxury and Business | United Kingdom |
| Coach | Luxury and Business | United States |
| Home&You | Homeware and Department Stores | Poland |
| Versace | Luxury and Business | Italy |
| Miss Sixty | Mid-Range Fashion | Italy |
| Steve Madden | Mid-Range Fashion | United States |
| Eataly | Coffee and Restaurants | Italy |
| Sephora | Other | France |
| Debenhams | Homeware and Department Stores | United Kingdom |
| Deichmann | Specialist Clothing | Germany |

Source: CBRE Ukraine

Vacancy & Rents

During the most turbulent months of lockdown between March and June, abatement requests from tenants ranged from rent holidays and rent reductions to adoption of OPEX-only payments for the duration of quarantine measures. Landlords, in turn, were looking into such occupier requests on a case-by-case basis depending on vulnerability of each individual tenant. Similarly, turnover-linked terms were pursued by retailers outside of the ‘essential’ sectors in anticipation of continued slow sales post quarantine. Shopping centers saw landlords agreeing to temporary 20%-30% reductions in rents resulting in the \$60-\$80/sqm/month range for prime locations and \$35-\$50/sqm/month range for secondary locations. As many consumers switched to local neighborhood alternatives for their everyday essentials during the lockdown, the most significant decreases in rents were noted in large shopping centers, in particular those located in the CBD.

Without consideration of temporary discounts for occupiers, rents in existing long-term agreements softened slightly by 5%-10% YTD. Rents in prime shopping centers ranged between \$80-\$110/sqm/month in H1 2020 vs \$85-\$115/sqm/month in H2 2019; and for secondary shopping centers – between \$40-\$60/sqm/month in H1 2020 vs \$44-\$63/sqm/month in H2 2019. Average vacancy on the market has increased to 6.6% (+2.1 pp YTD) primarily due to the slow take-up of new supply. The slow-going occupation pace of premises in Retroville SC is yet another reminder of the very large shopping center segment saturation in Kyiv. Lavina Mall SEC (127,500 sqm), Ukraine’s largest shopping centre to date, was faced with a similar challenge when it opened four years prior – modest occupation of ca. 40%. This similarity in occupiers’ behavior at different phases of the economic cycle may be indicative of the fact that a more balanced in-person shopping experience is on the cards. The leasing performance of another very large Blockbuster Mall (100,000 sqm), delivered in Q4 2019, will also influence the landscape of future retail development in Kyiv in particular and Ukraine at large.

Figure 3: Kyiv Shopping Center Stock and New Supply

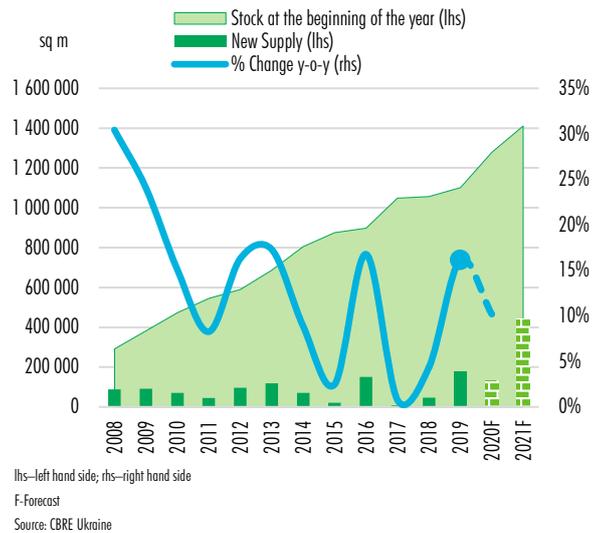
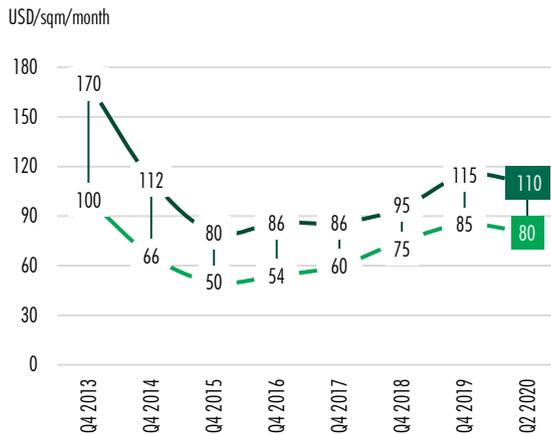


Table 3: Key Shopping Centers in the Pipeline, as of H1 2020

| ANNOUNCED FOR DELIVERY | GLA, SQ M | DEVELOPER |
|---------------------------------|----------------|------------------------------------|
| Delivered in H1 2020 | 80,700 | |
| Retroville | 80,700 | Stolitsa Group |
| H2 2020 | 49,600 | |
| April Mall (Phase II) | 49,600 | Kyivproekt Development |
| 2021 | 443,400 | |
| Lavina Mall (Phase II) | 20,000 | Mandarin Plaza/Megaline |
| Lukianivka Mall | 47,000 | Arriano Real Estate |
| New Ray | 34,500 | Build Commerce Group |
| Ocean Mall | 100,000 | Mandarin Plaza/Megaline |
| Piramida (Phase II) | 11,000 | Dragon Capital Property Management |
| Respublika | 135,000 | K.A.N. Development |
| Retail Park Petrivka (Phase II) | 7,100 | CEETRUS |
| Rive Gauche (Phase II) | 56,800 | CEETRUS |
| White Lines | 32,000 | A Development |
| Project | 840,200 | |
| Blockbuster Mall (Phase II) | 75,000 | Mandarin Plaza/Megaline |
| Hippodrome Mall | 293,000 | Mandarin Plaza/Megaline |
| Kyiv Mall | 65,200 | Delice |
| Lisova Mall | 220,000 | Mandarin Plaza/Megaline |
| Peremoha Mall | 150,000 | Mandarin Plaza/Megaline |
| Sky Mall (Phase III) | 37,000 | Prizma Beta |

Source: CBRE Ukraine

Figure 4: Base Rents Range in Kyiv Prime Schemes



Source: CBRE Ukraine

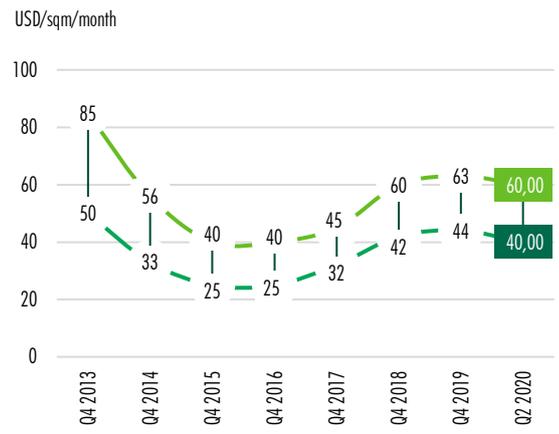
Investment

It was very quiet in the retail investment sector in H1 2020 and unsurprisingly so. Whereas development processes take years to initiate and are very hard to halt once fully underway, investment transactions can be halted at a snap of two fingers – even after long months of preparations and negotiations. While footfall may have begun to slowly recover after reopening, the lull in investment activity is expected to continue until the end of 2020, as traditional retail sector was hardest hit by the anti-pandemic measures, with retail migrating online at unprecedented scale and tempo. Most investors are thus expected to maintain the wait-and-see attitude for the medium-term future, as increased uncertainty is hovering over long term performance of traditional shopping centers. On the back of low investment activity on the market, prime yields weakened by +0.75pp standing at 12.5%.

Regions

The overall country retail turnover posted a modest 3.7% y-o-y increase in H1 2020 vs 11.4% achieved in H1 2019. The highest growth indicators were registered in Volyn (+10.9% y-o-y), Zaporizhzhia (+10.0% y-o-y), and Khmelnytskyi regions (+9.2% y-o-y), excluding temporarily occupied territories of Crimea and Donetsk & Luhansk regions. Ever since the beginning of COVID-19 outbreak, consumers became notably more price-sensitive. The development of e-commerce took a prominent place in the retail market in H1 2020 and is transforming to a new level. For instance, brands

Figure 5: Base Rents Range in Kyiv Secondary Schemes



Source: CBRE Ukraine

such as *Colin's*, *IKEA* and *Miniso* took advantage of the lockdown and launched their online stores during H1 2020. *Fora* food chain of *Fozzy* Group introduced collaboration with the *EVO's* marketplaces *Prom.ua* and *Bigl.ua* by offering delivery services. *Rozetka*, *Nova Poshta*, and *ATB* launched deliveries in all regions of Ukraine, *Metro Cash&Carry* added *Poltava* to its e-commerce reach, and *Silpo* commenced deliveries across the majority of regional centers, including *Dnipro*, *Kyiv*, *Kharkiv*, *Lviv*, and *Odesa*, among others.

Despite such substantial growth of online trade, the main proportion of all retail transactions remains in store. According to the official data collected by *Euromonitor International*, ca. 90% of all retail sales of 2019 in Ukraine came from store-based retailing. In the apparel and DIY segments, international brands *JYSK*, *LC Waikiki*, *Respect*, and *U.S. Polo Assn*, were among those most actively expanding on the Ukrainian market. In food retailing, the largest Ukrainian grocery discounter *ATB* grew its chain in the regions by opening 61 new supermarkets, which contributed to a 19% growth of *ATB* retail turnover.

In H1 2020, only 10,000 sqm of GLA were added to the regional shopping center stock with a single completion of Phase II of *APPOLO SC* in *Dnipro*. However, according to the official announcements of developers, the number of new deliveries in the pipeline have not been

affected by economic slowdown just yet. Over the course of H2 2020 and 2021, a total of ca. 176,000 sqm is expected for delivery in the cities of Dnipro, Ivano-Frankivsk, Kharkiv, Lviv, Odessa, Ternopil, Uzhgorod, Vinnytsia, and Zaporizhzhia. The density of retail area per 1,000 habitants in the biggest cities thus stayed broadly the same this year: 252 sqm in Lviv, 232 sqm in Dnipro, 210 sqm in Odesa, and 157 sqm in Kharkiv.

Table 5: Key Shopping Centers in the Regional Pipeline, as of H1 2020

| ANNOUNCED FOR DELIVERY | GLA, SQ M | CITY | DEVELOPER |
|-------------------------------|-----------|-----------------|-------------------------|
| DELIVERED IN H1 2020 | | | |
| APPOLO (Phase II) | 10,000 | Dnipro | Kontyent/UM K/Principal |
| H2 2020 | | | |
| Nikolsky | 53,000 | Kharkiv | Budhouse Group |
| Ostriv (Phase II) | 18,000 | Odesa | OTD |
| MegaMall (Phase II) | 10,000 | Vinnytsia | Tradeland |
| Atrium | 5,000 | Uzhhorod | UK Investment |
| Planeta Mall (Phase II) | 28,500 | Kharkiv | Local developer |
| Podoliany (Phase II) | 15,000 | Ternopil | Terkurii 2 |
| 2021 | | | |
| Veles (Phase II) | 21,500 | Ivano-Frankivsk | 555-IF |
| Spartak (Phase II) | 15,000 | Lviv | Lvivbudmaks-Invest |
| S)mall (ex.Dastor) | 9,500 | Vinnytsia | Local developer |
| Project | | | |
| Alexander Plaza | 48,000 | Zaporizhzhia | Land Development |
| Perehrestia (former Kubometr) | 3,000 | Dnipro | Alef Estate |

Source: CBRE Ukraine

Outlook

With majority of businesses reopened, the retail market and the consumers are gradually adapting to the “new temporary normal”. The dramatic effect the lockdown has had on occupiers resulted in an increased interest in turnover rent provisions. Such terms are likely to become more common in the segment as a safeguard against unpredictable sales under conditions of the ongoing COVID-19 crisis. No drastic increases in vacancy are expected over the course of the year, as landlords remain

Table 4: Major Food Retailers & Their Brands Operating on the Ukrainian Market

| RETAILER | SUPERMARKET FORMAT | HYPERMARKET FORMAT | CONVENIENCE STORE FORMAT |
|---------------|----------------------------|--------------------|---------------------------------|
| ATB | ATB | - | ATB Express |
| Fozzy Group | Le Silpo, Favore, Silpo | Fozzy C&C | Fora, Thrash! |
| Auchan Group | - | Auchan | My Auchan |
| Metro C&C | - | METRO | - |
| Tavria V | Cosmos, Tavria V | - | - |
| Novus | NOVUS | - | NOVUS Express |
| Retail Group | Velyka Kyshenia, VK Select | Velmart | VK Express |
| VolWest Group | SPAR, Nash Kraj, Eurospar | - | Nash Kraj Express, SPAR Express |
| Furshet Group | Gurman Furshet, Furshet | - | - |
| EKO Market | EKO Market | EKO Market | EKO Market |
| Omega | Varus | - | Varus-Express |
| Billa Ukraine | Billa | - | - |
| OPTTORH-15 | - | - | Delvi |
| Aretail | | | Kolo |
| LK-Trans | | | LotOK |
| Modern Trade | Kopyyka, Santim | | Kopyyka minimarket |
| Lvivkholod | Rukavychka | - | Rukavychka |

Source: CBRE Ukraine

generally flexibility with short term lease adjustments with a view to retain tenants. Investment activity is forecast to gradually resume in 2021, as vaccines become available and post-COVID patterns of traditional shopping become more predictable. In the meantime, the rental income in physical retail will remain volatile in conjunction with the dynamics of local infections, as authorities may choose to re-impose periodic curbs on traditional in-person shopping – whether of necessity or political expedience.



CONTACTS

For more information regarding this Market Report, please contact:

Sergiy Sergiyenko

Managing Partner

e: sergiy.sergiyenko@cbre-expandia.com

Radomyr Tsurkan

Managing Partner

e: radomyr.tsurkan@cbre-expandia.com

Diana Starunchak

Head of Marketing and Research

e: diana.starunchak@cbre-expandia.com

Anzhelika Arzumanian

Senior Analyst

e: anzhelika.arzumanian@cbre-expandia.com

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RETAILER SECTOR DEFINITIONS (in alphabetical order)

- **Coffee & Restaurants:** includes fast food, restaurants, confectionary retailers and coffee shops; otherwise known as Food & Beverage (F&B)
- **Consumer Electronics:** includes computing, phones, other electronics and electrical retailers
- **Health and Beauty:** includes cosmetics, skin care, chemists and healthcare retailers
- **Homeware & Department Stores:** includes DIY, department stores and furniture retailers
- **Luxury & Business Fashion:** includes any luxury retailer from all areas of retailing, including men's and women's luxury clothing/footwear, jewelry and business clothing retailers
- **Mid-Range Fashion:** includes men's and women's mid-market and casual fashion retailers
- **Other:** includes all other types of retailers including pet stores, books, music and DVD retailers
- **Specialist Clothing:** includes general (as opposed to luxury) footwear, underwear, sportswear, children's clothing and accessories retailers
- **Supermarket:** includes multiple grocery/convenience stores, supermarkets and hypermarkets
- **Value & Denim:** includes value and discount clothing, and denim retailers

DEFINITIONS (in alphabetical order)

Prime Rent - represents the typical "achievable" open market headline rent which an international retail chain would be expected to pay for a ground floor retail unit of up to 200 sqm commensurate with demand in each location. It is assumed that the occupier will also be agreeing to a package of incentives that is typical of the market at the time.

Prime Yield – represents the yield which an investor would receive when acquiring prime property in a prime location (CBD or major urban intersection, for example), which is fully let at current market value rents. Prime Yield should reflect 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 a hypothetical yield is quoted and is not a calculation based on particular transactions, but it is an expert opinion formed in light of market conditions, but the same criteria on building location and specifications still apply.

Shopping center - 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 sqm and offering good quality tenant-mix, at least 50% of which should consist of chain retailers.

Under Construction - represents the total amount of gross leasable area of properties where construction has commenced on a new development or in existing properties where a major refurbishment/renovation is ongoing at the survey date. This is where site works (foundation works) have begun or the ground has been broken (excavation works). It does NOT include demolition, sites being cleared for possible development in the future, or site preparation works where no specific development plans have been approved.

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