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*The overall vacancy rate reached **9,5%***



MOSCOW RETAIL MARKET REPORT

Q3 2020

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"2020 has become a year of abysmal low in terms of the announced volumes of new shopping centres and the actual volume, which has already been commissioned and may still be commissioned by the end of the year. We note a dramatic drop in developers' activity against the ongoing recession and the deteriorating situation with the pandemic as well as restrictive measures taken by the authorities, which primarily negatively affect not only retailer business but also shopping centre owners. In current conditions, it is difficult to forecast the rate of market recovery, but we are sure that in the absence of serious restrictive measures both in Moscow and in other regions of Russia against the second wave of growth in new cases, our estimates for the future completion will not require adjustment and the main volume of the shopping centres unopened but announced for opening in 2020, will be commissioned in 2021."

Key conclusions

- ♦ Two neighbourhood shopping centres were opened in Moscow by ADG Group in Q3 2020: "Elbrus" (GLA 4.7k sq m) and "Budapest" (GLA 9.7k sq m).
- ♦ The vacant space in the Moscow shopping centres operating for more than two years increased by 1.8% (compared to 2019) and amounted to 5.3%. The vacancy rate in new facilities equals to 11%. The overall vacancy rate reached 9.5%, which is 2.9 p.p. more than in Q3 2019.
- ♦ Reduced activity of new international retailers: only 11 new brands entered the Russian market (while 17 new brands entered the Russian market in the same period of 2019).
- ♦ Rental rates for premises in shopping centres in Q3 2020 did not change significantly and remained the same compared to Q2 2020.
- ♦ Compared to the same period of the previous year, rental rates reduced affected by the recession and restrictive measures to prevent the pandemic.
- ♦ It is possible that the commissioning of about 30–40% of the facilities previously announced for opening in 2020 will be postponed.

Key indicators. Shopping centres*. Dynamics

Shopping centres stock (GBA / GLA), million sq m	13.58/6.75
Opened in 2020 (GBA / GLA), thousand sq m	476/166.9
Scheduled for opening in 2020 (GBA / GLA), thousand sq m	≈580.8/≈313.4
Vacancy rate, %	9.5 (+2.9 p.p.)**
Fixed rental rent:	
Retail gallery tenants, RUB/ sq m/year	0–100,000
Anchor tenants, RUB/ sq m/year	3,000–15,000
Operating expenses:	
Retail gallery tenants, RUB/ sq m/year	6,000–10,000
Anchor tenants, RUB/ sq m/year	1,500–3,000
GLA in quality shopping centres per 1,000 citizens	532.2

* The table refers only to high quality, professional retail properties. A professional shopping centre is a standalone building or a group of buildings sharing the same architectural style, concept and under common management, with a total area of more than 5,000 sq m

** Compared to Q3 2019

Source: Knight Frank Research, 2020

Supply

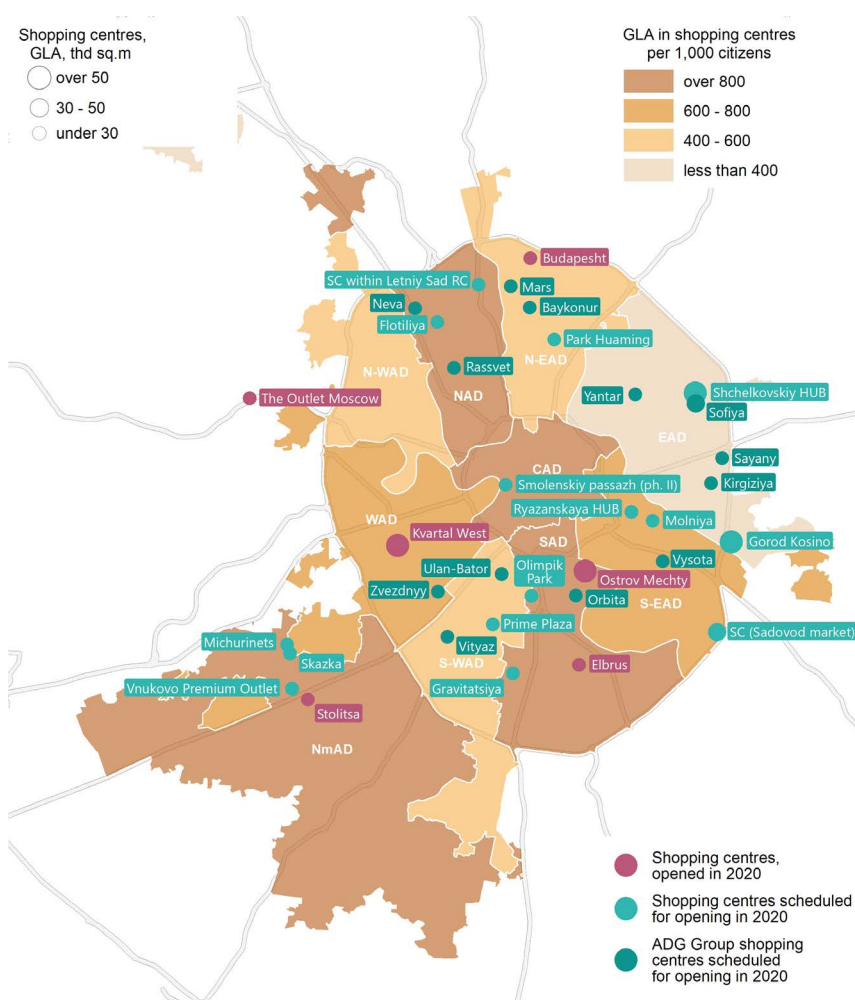
As of Q3 2020, the total supply of retail space increased by 14.4k sq m compared to H1 2020: two neighbourhood shopping centres of ADG Group were opened: “Elbrus” (GLA 4.7k sq m) and “Budapest” (GLA 9.7k sq m). Thus, the total supply of the Moscow retail real estate market is 13.58 mln sq m in Q3 2020 (GLA – 6.75 mln sq m).

In total, 166.9k sq m were commissioned in 2020, which is 12% more than in the same period of 2019, when 149k sq m of the leasable area was commissioned. The new supply increased due to the opening of a shopping centre which is a part of “Kvartal West” mixed-use complex, “Ostrov Mechty” shopping centre, “The Outlet Moscow” and “Stolitsa” shopping centre in H1 2020. Moreover, 49% of the announced annual commissioning was postponed in Q1-Q3 2020, which is 467.7k sq m of leasable retail area.

The previously announced openings of this year – Vnukovo Premium Outlet and the ADG Group neighbourhood centres – have been postponed to Q4 2020.

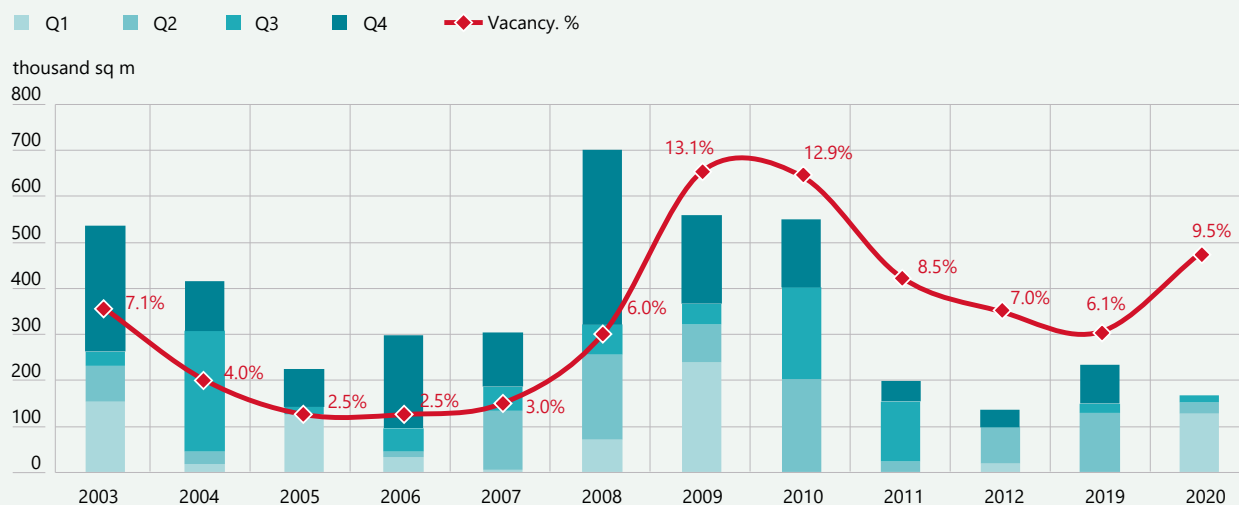
Considering the new commissioning volume, the high-quality retail density in Moscow amounted to 532.2 sq m per 1,000 people. Compared to Q2 2020, the figure increased by 0.2%. The growth against the similar period of the previous year was 3.7%.

Shopping Centres Opened in Q1-Q3 2020 and Planned for Opening by the End of 2020



Source: Knight Frank Research, 2020

Volume of commissioned shopping centres and vacancy rate dynamic



Source: Knight Frank Research, 2020

In terms of the “old Moscow” administrative districts, Central, South, and North districts are the most saturated. Novomoskovsky district is the leader in terms of retail density (1,453 sq m / 1,000 people), which is due to the small population (274,170 people). A significant increase in the population is expected in the next 3-5 years due to the commissioning of a large volume of housing against the background of commissioning of shopping centres and, therefore, a reduction in the density to 750–850 sq m / 1,000 people. Troitsky administrative district is less saturated by high-quality retail space with a zero value.

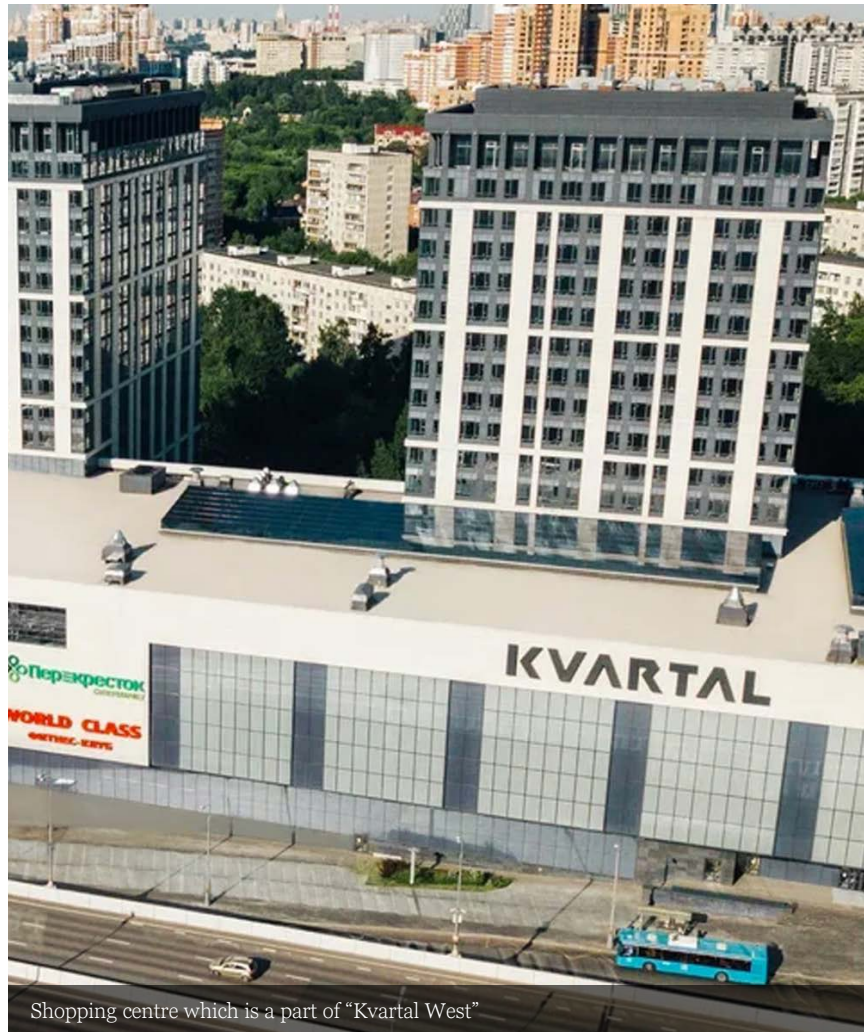
Vacancy rate

At the end of Q3 2020, the vacancy rate in Moscow shopping centres commissioned over two years ago increased by 1.8% (compared to 2019) and amounted to 5.3%. No changes were recorded compared to Q2 2020. The vacancy rate in new facilities decreased by 3 p.p. compared to the previous period and amounted to 11%. The overall vacancy rate reached 9.5%, which is 2.9 p.p. more than in Q3 2019. The overall vacancy rate decreased by 0.5 p.p. compared to Q2 2020.

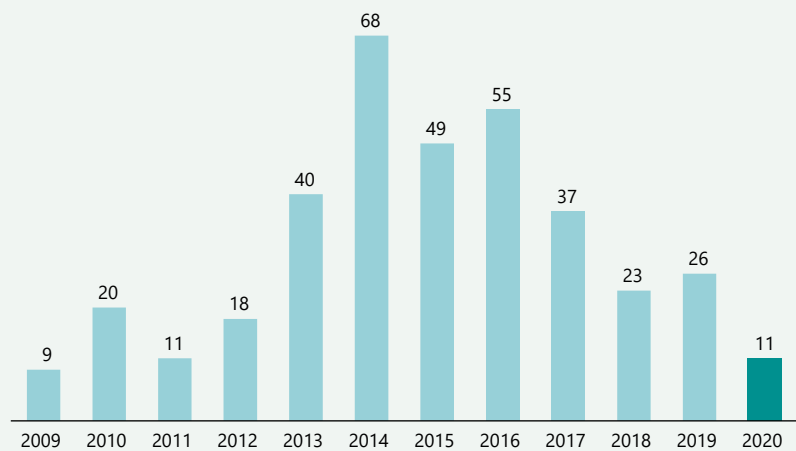
The vacancy rate in the facilities opened in Q3 2020 is high (up to 50%), which complies with the recent years' tendency, i.e. the completion of shopping centres with a large volume of vacant space and its active occupancy during the first year of operation.

Brands

11 new brands entered the Russian market this year (while 17 newcomers entered the Russian market in the same period of 2019). Half of the new retailers are represented by the “Apparel, Footwear, Underwear” profile. Regarding the price segment, as of Q3 2020, the prevailing share of new brands (55%) is the “upper middle / premium” segment. This segment was also the leader (88%) in the same period last year. It should be noted that the “premium” segment in Russia is more resistant to crises and volatility of purchasing power.

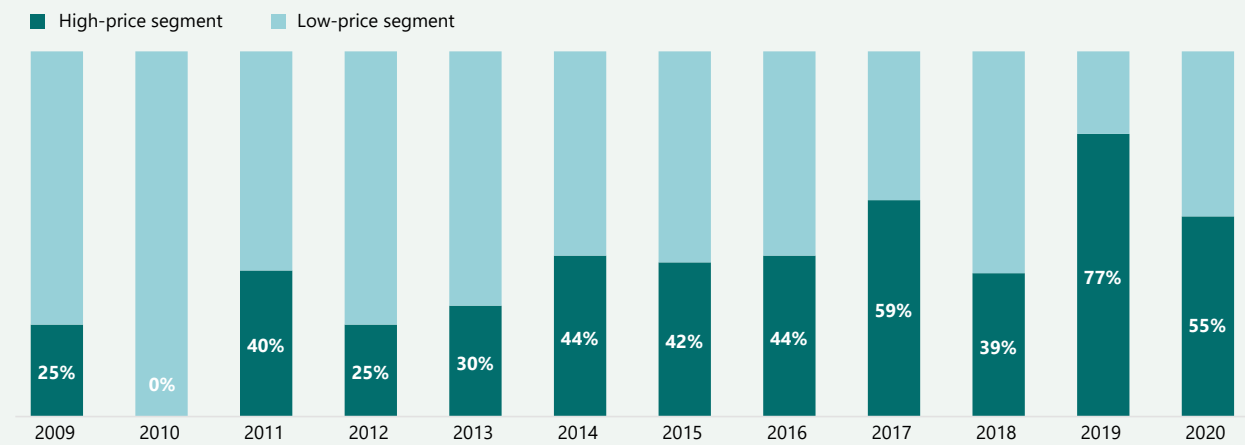


Dynamics of new international operators entering the Russian market over the past 12 years



Source: Knight Frank Research, 2020

The structure of brands entered the Russian market over the past 12 years, by price segment



Source: Knight Frank Research, 2020

Four international operators opened their first outlets in Russia in Q3 2020: a Weekday fashion brand of the H&M group in Aviapark SEC, Paulig Café & Store in Myasnikskaya Street, Patrick Roger elite chocolate boutique in The Outlet Moscow, and Adidas Terrex outdoor outfit store in Metropolis SEC.

The opening of the first two & Other Stories brand stores of the H&M Group was announced by the end of the current year in Metropolis and Vegas Crocus City shopping centres.

The opening of the first corner of a new brand of Russian designers Post Post Scriptum was announced.

In turn, the French accessory brand Longchamp announced its exit from the Russian market. According to Longchamp CEO, the store closings are mainly due to the pandemic crisis. Brands of Russian designers and large federal chains have also experienced the negative economic impact of the pandemic restrictions and the recession. Most brands have revised their development plans for 2020.

International operators that entered the Russian market in Q1-Q3 2020

Nº	Brand	Country	Profile	Price segment
1	UFC Gyms	USA	Sport	Upper middle
2	Filorga	France	Cosmetics / Perfumery	Upper middle
3	Suitsupply Woman	Netherlands	Apparel / Footwear / Lingerie	Upper middle
4	The North Face	USA	Apparel / Footwear / Lingerie	Middle
5	Ereda	Italy	Apparel / Footwear / Lingerie	Upper middle
6	Jysk	Denmark	Household goods	Low middle
7	Boss Woman	Germany	Apparel / Footwear / Lingerie	Upper middle
8	Weekday	Sweden	Apparel / Footwear / Lingerie	Middle
9	Paulig Café&Store	Finland	Food & Beverage	Middle
10	Patrick Roger	France	Grocery stores	Upper middle
11	Adidas Terrex	Germany	Apparel / Footwear / Lingerie	Middle

Source: Knight Frank Research, 2020

Commercial terms

In Q3 2020, the rental rates for retail premises in shopping centres remained unchanged. Compared to the same period of the previous year, rental rates reduced affected by the restrictive measures against the pandemic and the recession. The boundaries of the base rental rate for anchor tenants and small-sized operators of a retail gallery reduced by 25% in Q2 2020 compared to Q1 2020 and the previous year. Despite the reduction, maximum base rental rates relate to premises within the food court area and pop-up retail for existing projects with high traffic and can reach 120,000 rubles / sq m / year. The minimum rental rates are established for premises over 2,000 sq m for anchor tenants.

Trends

The keynote of the first half of 2020 was the unprecedented measures aimed at preventing the spread of Covid-19. The preventive policy, which started in mid-March, included increased protection measures (additional disinfection of premises, promotion of antiseptic hygiene, social distancing) and progressed to complete self-isolation of people and the closure of most retail, entertainment, and sports facilities. About 80% of retailers were closed within the period from 28 March to 1 June 2020, which stopped the work of most shopping and entertainment centres. Peak downtime weeks were characterized by a dramatic drop in turnover for fashion, catering, and entertainment tenants (over 90%). The problem of the relationship between landlords and tenants regarding the lease terms has become more crucial. Attempts have been made to resolve the issue at the legislative level. Agreements with 80% of the shopping and entertainment centres owners have been reached by the end of April 2020.

The restrictions on the operation of shopping and entertainment centres in Moscow were first lifted on 1 June 2020 and the strict self-isolation regime was cancelled on 9 June 2020. During the first week of the SCs operation after the restrictions, the traffic was at the level of 45-50% of last year on weekdays (at weekends, it amounted to 55-60% of last

Rental rates in Moscow shopping centres

Profile	Fixed rental rate, RUB/sq m/year*	The share paid based on turnover, %
Hypermarket (>7,000 sq m)	0–8,000	1.5–4
DIY (>5,000 sq m)	0–6,000	4–6
Supermarket (1,000-2,000 sq m)	8,000–18,000	4–6
Supermarket (450-900 sq m)	18,000–35,000	6–6
Household goods (<1,500 sq m)	0–10,000	6–10
Household appliances and electronics (1,200-1,800 sq m)	6,000–15,000	2.5–5
Sports goods (1,200-1,800 sq m)	6,000–12,000	6–8
Children's goods (1,200-2,000 sq m)	6,000–12,000	7–9
Operators of the shopping gallery:		
Anchors 1,000 sq m	0–12,000	4–12
Mini-anchors 700-1,000 sq m	0–14,000	6–12
Mini-anchors 500-700 sq m	0–16,000	6–12
300-500 sq m	0–25,000	5–12
150-300 sq m	8,000–18,000	6–14
100-150 sq m	16,000–36,000	10–14
50-100 sq m	25,000–80,000	12–14
0-50 sq m	45,000–100,000	12–14
Leisure concepts:		
Entertainment centres (2,000-4,000 sq m)	4,000–8,000	10–14
Cinemas (2,500-5,000 sq m)	0–6,000	8–12
Public catering:		
Food-court	45,000–120,000	12–15
Cafes	15,000–90,000	12–14
Restaurants	0–25,000	10–14

* Negotiated commercial terms

Rental rates are listed excluding VAT and operating expenses

Source: Knight Frank Research, 2020

year traffic). Traffic in the stores of large chain tenants has averaged 50–70% of the last year's indicators since the beginning of June.

By the end of Q3, traffic stabilized at 80–85% of the figures for the same period last year. However, due to the increase in morbidity, restrictive measures (lockdown for certain groups, recommendations to reduce visits to public places, etc.) are partially returning by early October, which directly affects traffic rates.

Most retailers switched to optimizing the number of outlets and started developing e-commerce: their online stores, marketplaces, and sales through social media. The online channel had been a strong sales driver in the retail market

before the pandemic, while the lockdown stimulated further development of the market digitalization.

The H&M Group has decided to launch in Russia online stores of Arket, & Other Stories, COS, Weekday and Monki, while offline stores of the first two brands are scheduled for opening.

Stockmann has opened an online outlet and does not plan the opening of an offline store shortly.

The shift towards e-commerce has taken place even in traditional offline segments such as luxury brands. Although 72% of premium segment customers preferred to shop offline before the pandemic, luxury brands moved online during the quarantine, adding elements of "premium" service to the shopping

process. For example, Gucci Live provides the opportunity to advise customers when buying online. Specialized marketplaces are being created, such as Alibaba's launch of an outlet featuring Luxury Soho luxury brands, and Amazon's launch of Common Threads: Vogue x Amazon Fashion, featuring exclusive items from independent designers.

Live commerce model is actively developing against the background of the streaming services growth: this is a new way of online interaction between a seller and a buyer, combining a seller or influencer and the ability to buy online by direct inclusion (the leaders are TaoBao of the Alibaba Group and Amazon Influencer of the Amazon Group).

The growth of online channels does not mean that offline stores will disappear. Offline commerce will transform, creating new store formats and services for customers, as well as areas for socialization, education, cultural and entertainment events.

In turn, the retail market is greatly influenced by global processes: consumer behaviour and preferences are changing almost at lightning speed in comparison with previous decades. The list of basic requirements of the modern buyer is diverse and is influenced by digitalization, demographic changes, and a responsible attitude to the environment. Technological development also influences consumer behaviour and makes retailers look

for more flexible ways of cooperation with customers: from choosing new communication points (leaving to social media) to developing omnichannel behaviour. Such a transformation affects the "behaviour" of the brands themselves, most of which work according to the 3R rule (reduce, reuse, recycle). They reject the use of animal materials, actively work to introduce recycled materials, and reduce the use of natural resources when producing new ones. Ethical issues also come to the fore: cultures and nations diversity, conditions for workers and the legitimacy of transactions for the materials purchasing.

The purchase of goods and services is becoming a way of self-expression and self-definition for a modern consumer. Consumers are looking for "their" brand. They are now interested not in advertising, but in the history of a brand or product: "tell me your story: if we have similar life principles, I will like you". At the same time, they are interested in the speed of selection, service, and transaction. Time spent shopping is critical today, with value for money becoming increasingly important. The consumer strives to buy reliable and quality brands at reasonable prices.

Buyer behaviour data with demographic trends and the economic situation suggest that there was a steady shift towards more deliberate and targeted shopping due to the recent-years'

recession. Demonstrative consumption is giving way to a more conscious or practical one. The product consideration is characterized by greater selectivity of a product or service and the use of modern technologies. The pragmatic approach is noted everywhere while selecting clothing, food and/or durable goods. Preliminary monitoring of brand websites, quality to price comparison, search for optimal buying conditions (bonuses, promotions, delivery) – the buyer strives to consciously take every step. It triggers the development of new tools and technologies, i.e. the resources that allow you to compare the cost of goods, evaluate quality, and search for the best offer on the market (Trivago, Yandex.Market, Yula, Avito, etc.).

New consumer behaviour is focused on obtaining new experiences, developing cultural traditions, maintaining youth, being active, and striving for a healthy lifestyle. Shopping centres are increasing their entertainment and sports components: the share of entertainment operators has increased from 8% to 15% in the leasable area of shopping centres (compared to facilities commissioned before 2014), the share of the sports component has increased from 1% to 4% (compared to facilities commissioned before 2014). It is worth noting the increase in the number of niche concepts such as martial arts, yoga and pilates, dance studios, cycling, and cross-fit.



The Outlet Moscow

Forecast

According to the announced developers plans, the volume of new completions in Moscow will amount to 313.4k sq m of retail space by the end of 2020. Thus, the annual volume of new supply of shopping centres will be 480.3k sq m, which is twice as much as last year. Record completions of shopping centres for the last five years (about 950,000 sq m) was announced for 2020, 49% of announced volume has already been postponed to next year. Such large retail facilities as the shopping centre at “Seligerskaya” HUB (GLA 145,000 sq m), the shopping centre in Mytishchi (GLA 144,000 sq m) and the shopping centre on the site of “Sadovod” market (GLA 50,000 sq m) were announced for opening by the end of 2020. However, as of the end of Q3 2020, construction of these projects was suspended.

There is a possibility of adjusting the commissioning date of 30–40% of new shopping centres announced for opening in 2020–2021. However, the reduction in completions will not be significant since certain facilities are already at the final stage and it is unprofitable for developers to postpone the completion date of the project at this stage. There is a possibility of adjusting the commissioning date of certain facilities, but in any case, all the announced shopping centres will enter the market in the next five years.

With limited demand and reduced purchasing power, neighbourhood shopping centres will continue to gain popularity among both developers and consumers, thereby creating competition for larger shopping centres with an ageing shopping-only concept. Due to consumers choice of retail facilities close to their living places to save time, and the economic attractiveness of the format, i.e. a faster payback period for small SC projects than large retail facilities, the format is becoming more popular. The concept of a small shopping centre, focused on meeting the needs of the walking distance target audience, can offer a mixed-use comfortable environment for leisure, shopping, and entertainment. Neighbourhood shopping centres are scheduled for commissioning in 2020–2021: ADG Group projects, a shopping centre in Aviakonstruktor Milya Street with the total area of 11,000 sq m and a shopping centre in the “Leninsky, 38” residential complex with a leasable area of 10,000 sq m.

Major shopping centres which will be opened by the end of 2020

Name	Address	GBA	GLA
Prime Plaza	Kahovka St., 29A	40,470	25,000
Flotiliya	Flotskaya St., 7, bld. 1	28,000	23,000
Smolenskiy passazh (phase II)	Smolenskaya Sq., 7-9	58,437	19,647
Rasskazovka HUB (Skazka)	Borovskoye Hwy. / Korneya Chukovskogo St.	29,000	18,608
Gravitatsiya	Chertanovskaya St.	30,000	18,500
Molniya	Ryazanskiy Ave. within Kvartaly 21/19 RC	18,450	14,020
Ryazanskaya HUB	Nizhegorodskaya St.	20,000	14,000
Vnukovo Premium Outlet	Lapshinka Village	17,000	11,900
Olimpik Park	Elektrolitnyy Passage, 3B	20,000	11,000
SC on Aviakonstruktor Milya St.	Aviakonstruktor Milya St.	11,000	7,700

Source: Knight Frank Research, 2020

ADG Group

Name	Address	GBA	GLA
Sofiya	Sirenevyy Blvd., 31	62,070	35,513
Kirgiziya	Zelenyy Ave., 81	26,147	13,592
Baykonur	Dekabristov St., 17	13,454	9,541
Rassvet	Zoi i Aleksandra Kosmode-myanskikh, 23	9,365	6,460
Mars	Inzhenernaya St., 1	8,072	6,184
Ekran	Novocherkasskiy Blvd, 21A	8,863	6,167
Vysota	Yunyk Lenintsev St., 52	8,944	6,139
Neva	Belomorskaya St., 16A	8,664	5,890
Biryusinka	Bulatnikovskaya St., 9A	7,032	4,644
Almaz	Shabolovka St., 56	5,591	3,878
Sayany	Sayanskaya St., 9	5,260	3,026

Source: Knight Frank Research, 2020

In addition to community centres, the new retail supply in Moscow for the coming years will be based on Transport Interchange Hubs. The city attracts investors through tenders for certain projects and is ready to work by itself on others. Investors have joined the projects of 15 transport interchange hubs, most of which comprise a retail purpose. The construction of shopping centres was announced as part of “Vykhino” (GLA 70,000 sq m), “Seligerskaya” (GBA 145,000 sq m) and “Park Pobedy” (GBA 237,000 sq m) by Tashir, “Shchelkovskaya” HUB by “Kievskaya Ploschad”, “Botanika Mall” SC at “Botanichesky Sad” HUB (GLA 27,000 sq m), and “Discovery” SC at “Khovrino” Transport Interchange Hub (GBA of 25,000 sq m). The affiliate of “Kievskaya Ploschad” developer applied for an investment package for “Nagatinskaya” Transport Interchange Hub; 3S Development acquired the rights to 99% of “Nekrasovka” and “Klenovy Bulvar” Hubs, which will include the construction of the mixed-use complex. The implementation of the announced projects is scheduled for 2021–2024.

The following shopping centre projects have been announced: “Paveletskaya

Plaza” shopping and entertainment centre (GLA / GBA 35,000 / 73,000 sq m) with the announced completion at the end of 2021; Estate Mall (GBA 10,400 sq m) in Novorizhskoe Highway, a permit for the construction of “Gorod Kosino” shopping and entertainment centre (GLA / GBA 72,000 sq m / 127,000 sq m) was issued; the start of construction in 2020 was announced for “Prokshino” mixed-use complex of the Safmar Group (GBA 332,000 sq m). A shopping centre with an area of about 13,000 sq m will be built in Kommunarka with parking on the accessible roof.

The recovery of the SCs traffic in Russia to the pre-crisis level can be expected no earlier than mid-2021, and in some segments, for example, entertainment centres and cinemas, no earlier than the end of 2021. Firstly, certain restrictions associated with the virus containment will physically reduce the capacity of the facilities. Secondly, consumers behaviour will change by natural caution following the past months, incomes reduction, and a switch to e-commerce.

In conditions of the current epidemic and economic situation, the vacancy rate is forecast to grow up to 11% by the end of the year, provided the lifting of

restrictions on the operation of retail real estate was final, and no measures will be re-imposed.

The rental rates reduction recorded in H1 2020 is temporary and will return to the previous level in the next 1.5–2 years with the recovery of the retail real estate market.

Further development of the retail real estate market will be formed due to the following factors:

- ♦ New construction slowdown.
- ♦ Further changes in the areas and formats of retail facilities.
- ♦ Increased share of social, cultural, educational, sports and recreational functions in the SCs tenant mix.
- ♦ Greater integration of online and offline retail. Using new technologies as well as new sales and promotion channels.
- ♦ Decreasing the retail space areas.
- ♦ Increased supply of services and new customer care tools.
- ♦ Change in consumer behaviour.



Paveletskaya Plaza



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