

Quick Stats

	Change from	
	2009	2008
New supply	↓	↓
Rents	↑	↓
Vacancy	↓	↑

Hot Topics

- Retail sales demonstrated a positive dynamics in 2010 on the back of strengthening population purchasing power
- New supply amounted to mere 45,000 sq m, a four-year minimum
- Prime rents were growing throughout the year while secondary rents stabilized at the level 2009
- The recovery on regional markets is not so pronounced due to lower level of solvent demand

Retail property market of Ukraine proved the most resilient during recent economic downturn and from the beginning of 2010 has started showing signs of recovery.

DEMAND

Consumers. On the back of economic stabilization, population purchasing power displayed positive dynamics in 2010 for the first time since the end of 2008. Kyiv Statistics Office reported a 5% increase in real wages over the year after a sharp 12% drop in 2009. As a result, retails sales in fixed prices in 2010 grew 6.2% compared to the 2009 figure.

Improving consumer credit market also had a positive impact on retail turnover growth. In H2 2010 many retailers started offering short-term lending programs at their stores in order to stimulate demand. Consequently the volume of consumer loans with maturity of up to one year increased by 19% following a long period of continuous decline.

Key Retail Market Indicators Dynamics



* - real disposable income figure for January-September 2010

Source: Kyiv Statistics Office

Consumer sentiment in Ukraine demonstrated an overall positive trend in 2010, with Kyiv citizens being the most optimistic in their outlook. However, confidence is still fragile and displays short-term volatility which is indicating that consumers are sensitive to different governmental initiatives in economic and political sphere.

Retailers. On the back of retail sector recovery, international retailers are becoming increasingly interested in the Ukrainian market. According to the research carried out by CB Richard Ellis in the summer of 2010, Ukraine ranks 17th out of 38 countries targeted by international retailers seeking to expand in 2011, which implies significant potential of the Ukrainian retail market.

Growing retailers' interest was reflected in a number of market entries in 2010. The majority of new fashion retailers (Massimo Dutti, Topshop, New Look, Okaidi, Obaibi) became tenants in the newly delivered SC Sky Mall. New Yorker and Oysho announced the opening of their flagship stores in Sky Mall in the early 2011. In addition, British retailer River Island opened its first store in SC Dream Town in late 2010, while American shoe retailer Nine West entered Kyiv market by opening a store on Kreschatik Street. Moreover, DIY operator Leroy Merlin delivered its first Ukrainian hypermarket in Obolonkiy district of Kyiv in December 2010.

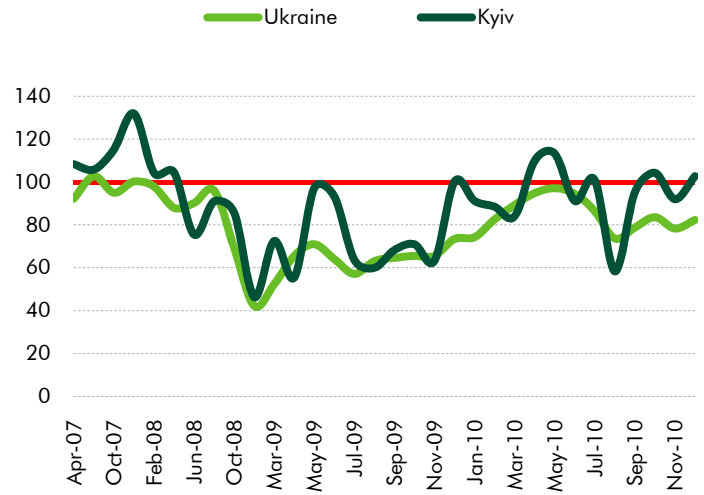
It is worth mentioning that when entering the Ukrainian market, international retailers still have a clear preference for the franchising model over own stores strategy due to the high existing country risks. Spanish Inditex Group present in Ukraine with its brands Zara, Pull&Bear, Bershka, Stradivarius, Massimo Dutti is one of the few retailers that operate their own stores on the market.

SUPPLY

Over 100,000 sq m of retail space was forecast to enter the Kyiv market in 2010. Despite developers' optimistic announcements, Kyiv has witnessed the opening of only one professional retail scheme – shopping center Sky Mall (GLA - 45,000 sq m). Thus, as of the end of 2010, total cumulative retail stock in Kyiv accounted for ca. 490,000 sq m of quality premises within shopping centers.

Thereby the provision of competitive retail stock in Kyiv remains far behind most Central and Eastern European (CEE) capitals. In Q4 2010 this number for Kyiv amounted to mere 174 sq m of quality retail premises per 1,000 people, while the average indicator in CEE capitals reaches 400-600 sq m per 1,000 residents.

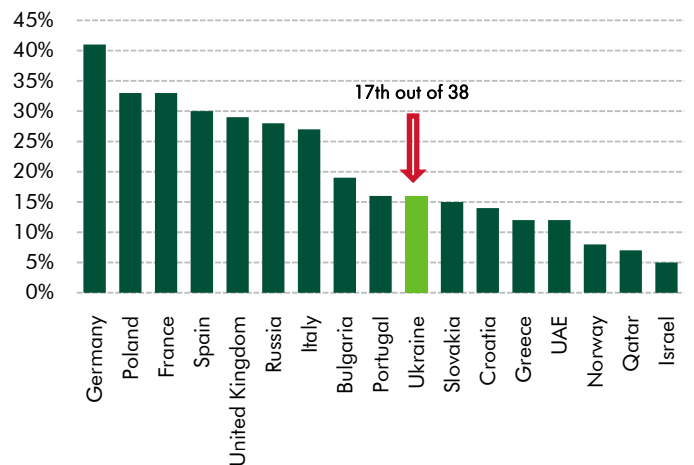
Consumer Confidence Index*



* - figures above 100-mark indicate that positive expectations outweigh negative ones

Source: GfK Ukraine

Select Target Countries For Retail Expansion in EMEA in 2011*

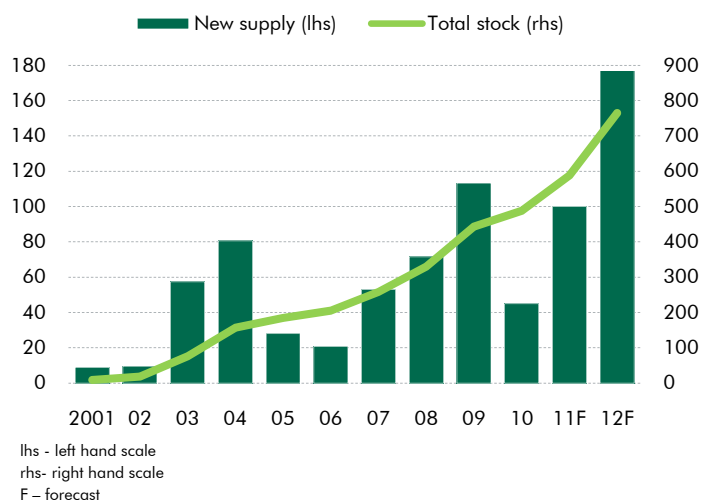


*- share of international retailers targeting country in 2011

Source: CB Richard Ellis

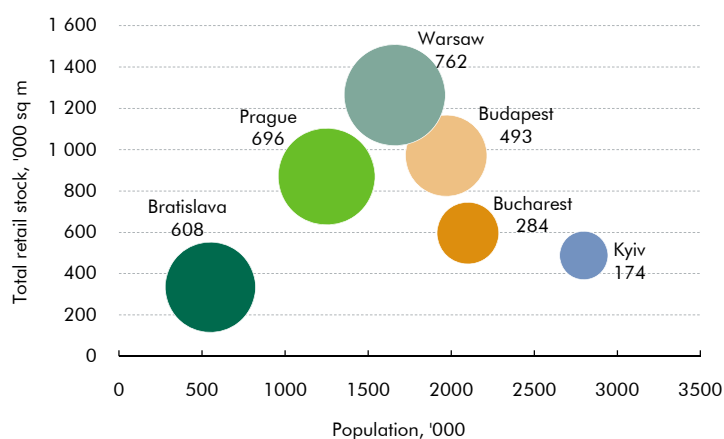
Low construction activity in 2009 caused by financing hurdles during economic recession resulted in tightening of development completions in 2010 (over 60% lower than in 2009). Many developers were forced to put off commissioning of their projects, among which most notable are the 2nd phase of SC Dream Town (GLA - 45,000 sq m) and SC Continental (GLA - 32,000 sq m). Thus, the pipeline for 2011 consists of only retail schemes with previously postponed delivery dates.

Kyiv Shopping Center Stock



Source: CB Richard Ellis

Retail Premises Provision per 1,000 People in Select CEE Capitals in 2010



Source: CB Richard Ellis

Major Retail Schemes in 2011-2012 in Kyiv

NAME	SUBMARKET	GBA*, sq m	GLA**, sq m	DEVELOPER	DELIVERY
Promenada Park	Out of town	40,000	23,000	Promenada Center	Q1 2011
Dream Town	Residential district	82,000	45,000	Vita-Veritas	Q2 2011
Continental	Central district	41,000	32,000	Tri - O	Q3 2011
Ocean Plaza (1 st phase)	Transitional district	167,000	75,000	KAN Development	Q2 2012
Marmelad	Transitional district	52,000	34,000	Local developer	Q3 2012
SC in 26 th micro district	Residential district	47,000	22,000	Panorama Group	Q3 2012
Aquapark	Residential district	160,000	46,000	Prestige	Q4 2012

* GBA - gross building area
**GLA - gross leasable area

Source: CB Richard Ellis

At the same time Kyiv retail property market has seen a substantial improvement in construction activity in 2010. Among the most prominent events was the start of construction works of SC Ocean Plaza (75,000 sq m GLA of the 1st phase) in the central part of the city and SC Aquapark (GLA - 46,000 sq m) on the left bank. However, development financing remained generally unattainable and therefore only developers with own equity managed to keep construction works going in 2010.

Delivery of several large shopping centers in recent years (e.g. Sky Mall, Dream Town) and further extension of the existing ones (Bilshovyk, Karavan, etc) set the trend for growth of average shopping center size. Thus, by the end of 2010 average GLA of retail schemes in Kyiv reached 21,000 sq m compared to 17,000 sq m in 2008.

In addition, developers are demonstrating a growing interest to new formats of retail centers not yet present on the market. For example, the development starts of first two retail parks Panda Park (Kyiv) and Volodymyrskiy (Dnipropetrovsk) are scheduled for H1 2011 while outlet centers by Fashion House Group and Chameleon Retail Centraleurope are at the initial planning stage.

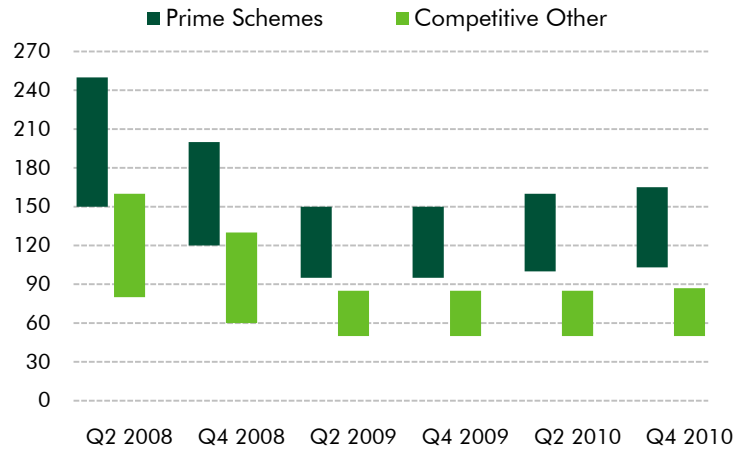
VACANCY AND RENTS

Throughout 2010 occupiers continued to target the best locations thereby exacerbating the polarization in the market between the best and the rest. Therefore vacancy in Kyiv shopping centers varied significantly depending on concept quality and location. Over 2010 vacancy levels returned to pre-crisis 0-2% in prime retail schemes, while vacancy in secondary locations showed only slight decrease after a dramatic surge in 2009 and currently standing at 3-5%.

Prime rents grew by some 10% in 2010 on the back of strong occupiers demand for quality space coupled with acute deficit of prime locations. By the year-end, rents in most successful shopping centers varied between \$100 and \$160 per sq m per month (triple net) for a typical gallery unit of 100-200 sq m. As a contrast rents in secondary locations stabilized at the level of the end of 2009 - \$50-80/sq m/month for typical gallery units and remained mostly unchanged during 2010.

Growing volumes of retail sales strengthened landlords' position on the market in 2010. Over the course of the year landlords ceased to offer various concessions which were ubiquitous in 2009 under the conditions of low demand (rent free periods, fit-out compensation or contributions, fixed exchange rate, lowering of deposit payments, etc).

Rents*



* - USD/sq m/month, triple net

Source: CB Richard Ellis

In the past two years retailers have been favoring floating rental rate (fixed below-market rate combined with certain percentage of retail turnover). This percentage for anchor tenants is usually the lowest – 1-2% of retail sales, while for mall tenants it varies within 4-8%. However, in contrast to the developed markets, the implementation of this practice in Ukraine entails difficulties, especially when it comes to controlling the actual turnover of a given retailer.

Typical Lease Terms

Rent Payment	Rent is paid monthly in advance and is quoted inclusive 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/known international retailers with significant market power – turnover rent or mixed type (base+% of turnover) rent can be applied.
Rent escalation/rent review	Rents are usually denominated in USD, but payable in Hryvnia at the official USD/UAH exchange rate (quoted by National Bank) with monthly adjustments. The rent is typically annually indexed for USD inflation (CPI).
Service charge	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.
Tenants covenant	Tenant has to provide either a rent deposit or a bank guarantee, typically equivalent to 1-2 months' rent.
Incentives	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.
Lease length and term	Parties are obliged to notarize rental agreements with duration of over 3 years; therefore leases are usually signed for 2 years and 11 month. Anchor tenants sign leases for longer periods – up to 10 years. According to the Ukrainian law, lease length should not exceed 15 years.
Repairing liabilities	Landlord usually undertakes repairs of the structure, common areas and roof. All internal maintenance/repairs is tenant's responsibility.

Source: CB Richard Ellis

REGIONS

By and large regional property markets remained static due to a moderate level of solvent demand and established shopping habits¹ of population. In addition, strong deficit of development financing kept construction activity at a low level.

The only regional completion in 2010 was the opening of the biggest shopping center in Western Ukraine - SC King Cross Leopold (GLA - 45,000 sq m) in Lviv. This allowed some international brands including Zara, Pull&Bear, Stradivarius, Bershka (Inditex group) together with Marks&Spencer, Tom Tailor, Motivi, Frank Walder to enter the Lviv retail market.

Compared to 2009, retailers showed more interest in regional markets; however, expansion plans were still cautious. Food retailers (ATB, Fozzy Group, Furshet, Billa, Novus) and consumer electronics operators (Comfy, Foxtrot, Eldorado, Foxmart) were the most active and continued expansion in the regions by opening a number of new stores in 2010. Additionally, some DIY chains including Epicenter and Nova Liniya benefited from decreased land prices and managed to secure several new sites across the country.

Residents of regional cities are less prone to do their shopping in professional retail formats compared to Kyiv inhabitants. It is evident from the fact that in 2010 organized retail accounted for 52% of total retail turnover nationwide whereas in Kyiv this indicator stood at 73%.

In general, in Ukraine consumer demand showed strong growth dynamics in 2010. According to the State Statistics Committee, real wages increased by 10.2% over the year while retail turnover grew by 7.8%.

However, rents in regions remained mostly flat in 2010 stabilized at the level of \$30-60/sq m/month for a typical mall section. Looking ahead, any upward movement is not expected in the short term as the drop in demand was much more pronounced in regional markets than in Kyiv.

Rents* by retail formats in 2010

	Food hypermarkets/ supermarkets	Gallery		Consumer electronics	Entertainment
		Prime	Other competitive		
Kyiv	18-22	100-160	50-85	15-25	10-12
Megacities** and Lviv	12-16	40-60	20-40	12-18	8-10
Other regional cities	8-13	30-40	15-25	10-15	6-9

* - USD/sq m/month, triple net

** - Cities with population over 1,000,000 people

Source: CB Richard Ellis

OUTLOOK

The retail sector growth in Ukraine was solid in 2010 due to an impressive rebound of the consumer demand. According to Oxford Economics these positive trends are forecast to accelerate with private consumption growing on average at 6.5% annually over 2011-2014.

Following the recent squeeze of development completions, the announced pipeline for 2011-2012 in Kyiv amounts to ca. 270,000 sq m of modern retail space, which should add more than 50% to the existing stock. However, the probability of timely delivery of the entire announced volume is low due to the common practice of commissioning delays in Ukraine. Despite a growing interest from global retail we do not expect a great number of new market entries in the upcoming year due to the continuing shortage of quality space, as well as a projected shortage of new supply.

At the same time we expect the increase in the number of development starts in 2011 as banks are ready to start financing construction of the projects with quality concept. Meanwhile, international developers are showing interest in entering the projects under construction and even greenfield. However, taking into account the average market construction timeline, the development pipeline is likely to remain subdued in the short term.

¹ - Residents of regional cities are less prone to do their shopping in professional retail formats compared to Kyiv inhabitants. It is evident from the fact that in 2010 organized retail accounted for 52% of total retail turnover nationwide whereas in Kyiv this indicator stood at 73%.

The limited pipeline of quality retail space in 2011-2012 will spur further increase in the prime rents on average 10-15% per annum, provided economy stays on its current recovery path. We expect more conservative growth of secondary rents in the short term due to a weaker demand from retailers.

In terms of market recovery we expect the regions to lag behind the capital at least by 1.5-2 years due to more profound effect of the recent economic downturn. The construction activity in the regions is expected to gradually revive in 2011, primarily in Dnipropetrovsk, Odesa, Kharkiv and Lviv, as retailers are still mainly focused on large cities. However, we do not expect any significant increase in the modern retail stock at least until mid 2012. The average rents will remain largely unchanged in the short term with a possible sluggish upward correction after 2011.

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