

Q3 2023

Office Market Overview

Russia | Moscow

Table 1
Key market indicators
Source: Nikoliers

	Q1-Q3 2021	Q1-Q3 2022	Q1-Q3 2023
Total office stock, million sq m	19.4	19.6	20.0
Class A	4.9	5.1	5.4
Class B+/-	14.5	14.5	14.6
Completions, thousand sq m	497.6	223.6	187.2
Class A	394.7	151	163.2
Class B+/-	102.9	72.6	24.0
Office take-up, thousand sq m	1,126	610	1,416
Vacancy rate, %	8.0	8.1	7.4
Class A	9.5	11.9	11.6
Class B+/-	7.5	6.8	5.8
Weighted average rental rate*, RUB/sq m/year	23,710	21,575	21,374
Class A	28,314	27,301	25,764
Class B+/-	19,876	18,371	17,832

*Excluding operational expenses, utility bills and VAT (20%).

Main results

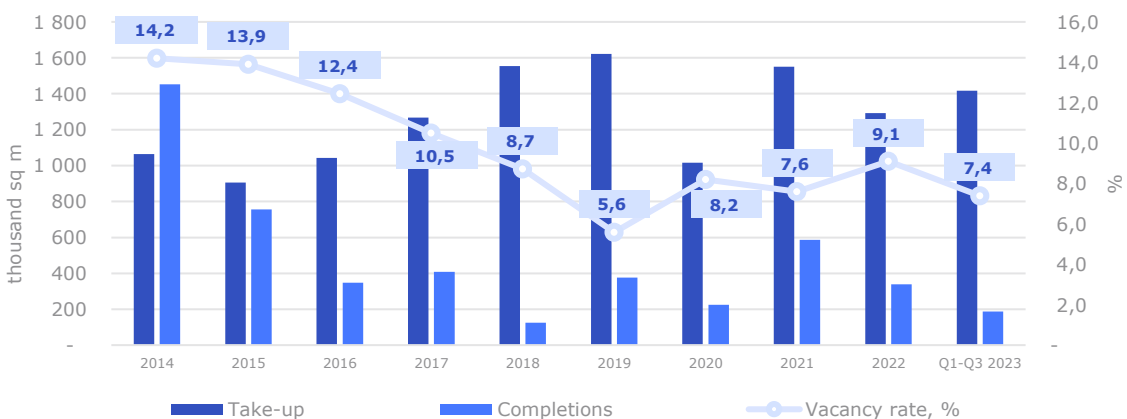
Changes in key market indicators signal a surge of interest in offices. The vacancy rate went down by 0.6 p.p. versus the previous quarter – to the lowest level for the two recent years. The adjustment of weighted average rental rates is mainly due to a high volume of transactions and withdrawal of liquid supply from the market. The average rate is still influenced by the decline in the prices in less sought-after facilities outside the Moscow Ring Road.

Based on the results for nine months of 2023, the commissioning of new quality offices amounted to 187,200 sq m, of which eight new projects were commissioned in Q3, which is still below the commissioned space in the same period of the two recent years.

During the current year we saw a number of large wholesale purchase transactions, which can be explained both by the fact that market participants are in need of buying large high-quality office assets in limited supply, and by the fulfillment of pent-up demand as well as the development of Russian business.

Thus, the level of demand for Q1-Q3 of 2023 amounted to 1,416 thousand sq m, which is a record-high demand for the entire history of the market reviews.

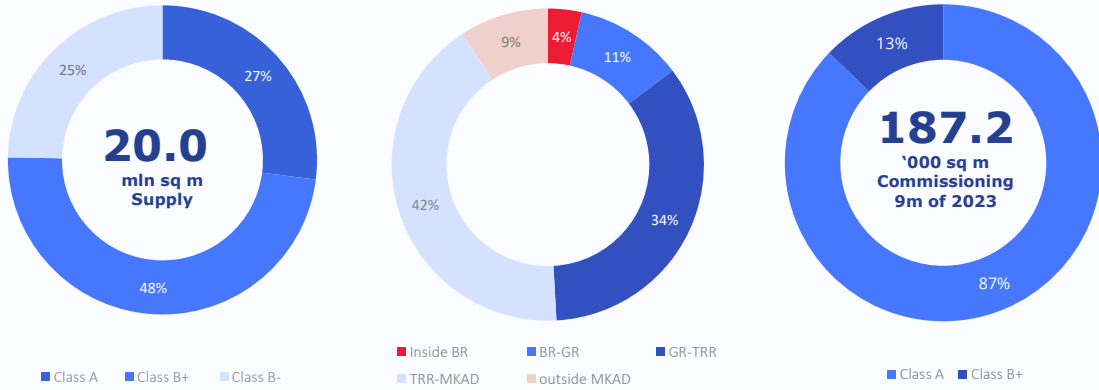
Chart 1
Key market indicators, Class A and B+/-
Source: Nikoliers



Supply

Chart 2

Breakdown of existing and new office supply, by classes and submarkets, %
Source: Nikoliers



In the first nine months of 2023, some 187,200 sq m of quality office space was commissioned, of which 87.2% were Class A offices.

Q3 2023 saw the commissioning of eight new office facilities, such as two buildings within Ostankino Business Park (buildings 4 and 5), BC Lucky (bld. 6), Alcon III (Alcon Tower), BC on 20A Zemledelchesky Alley, retail and office functions within the residential development at 25B Khoroshevskoe Highway, as well as the Innovation Centre of Moscow State University (an educational cluster with office space) and a completed renovation in the PANGAEA neighborhood.

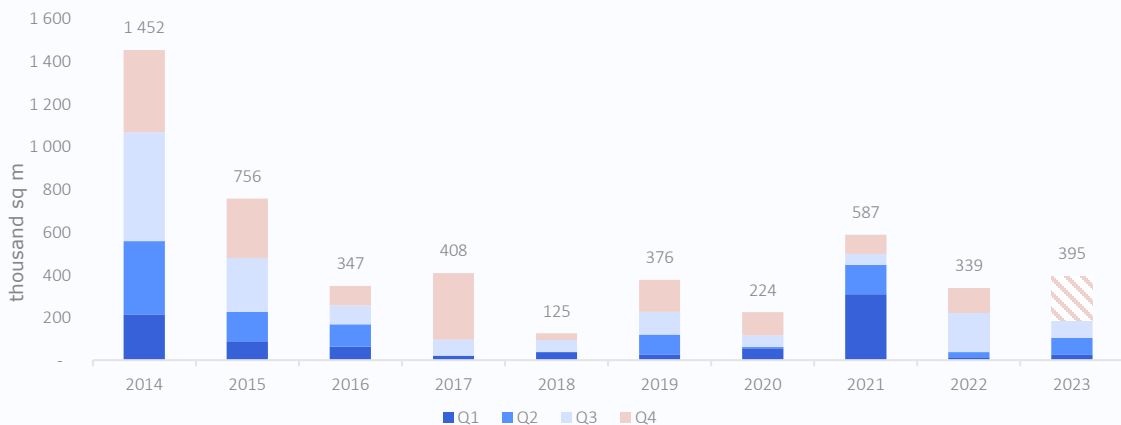
The office facilities commissioned in Q3 2023 are mainly concentrated outside the Third Ring Road (65.2%) and in the area between the Garden

Ring and the Third Ring Road (34.8%). New construction in the quarter under review falls mainly on the Suschevsky submarket due to the commissioning of 34,700 sq m in Ostankino business park. A remarkable thing is that both buildings had been sold prior to being commissioned, so there is no increase in vacancies in the given location.

Commissioning of newly built office space at the level of 395,000 sq m has been announced for 2023 (till the year's end), which is 16% more than the final figure for 2022. The commissioning deadlines for some projects can be pushed back to the next year, but no freezing of the projects already under construction is expected.

Chart 3

Office completions
Source: Nikoliers



Construction of office projects

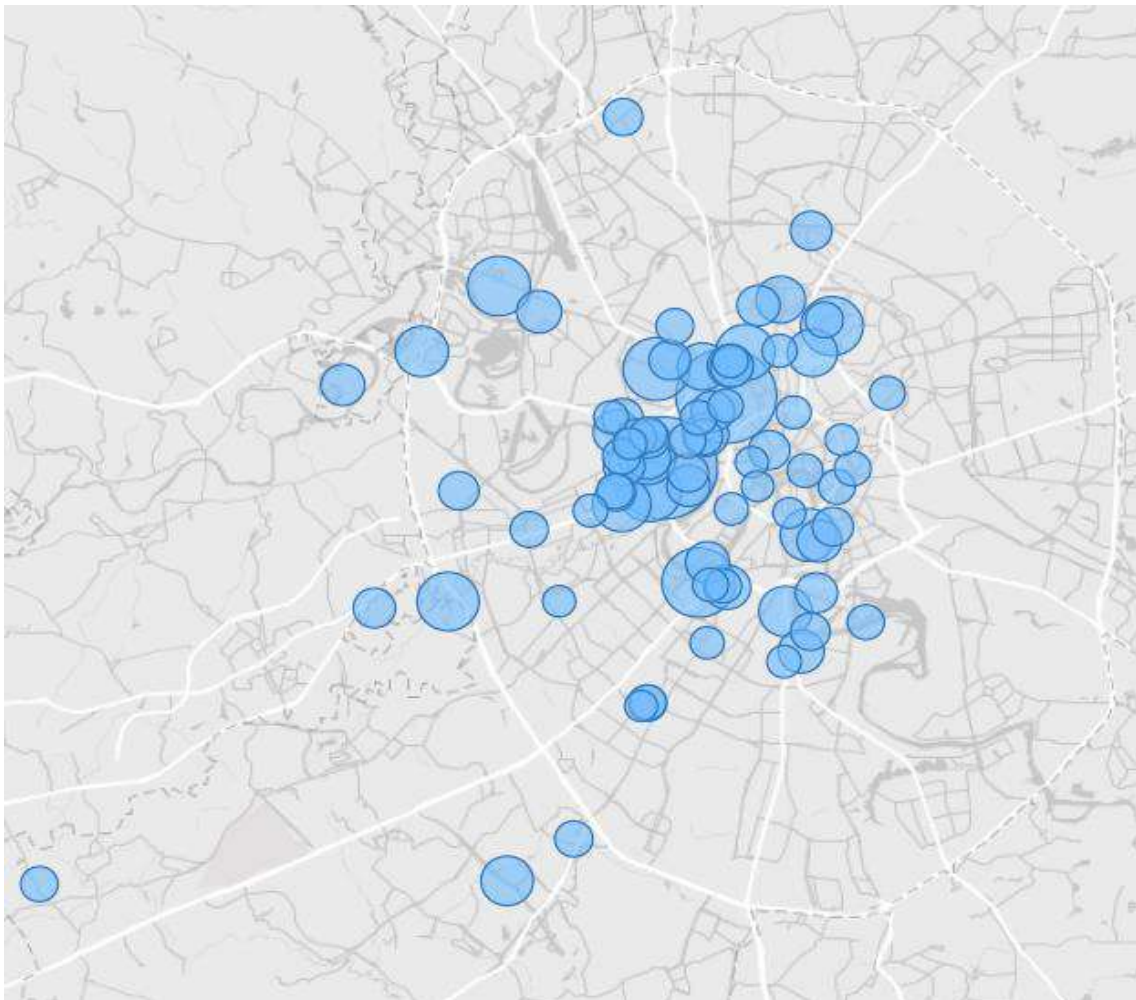
Development activity in 2023 started to recover after a slowdown last year amid the aggravation of geopolitical factors. Currently, developers are still cautious about entering new projects, although information about a number of interesting office locations is emerging. The growth of the key interest rate is a factor of decreasing attractiveness of construction in the midst of rising cost of financing, but the Moscow market's demand for quality offices stimulates the creation of highly liquid projects.

The TRR-MKAD zone accounted for 50% of total office construction activity. Location is still the most important factor in choosing an office. The development of the Moscow public transport system may become a new force of attraction for the facilities sitting not far from the key Moscow interchange (transfer) hubs.

Demand for the central zone still prevails, but given the scarcity of quality office supply for sale, there is an opportunity to attract the potential buyer with a unique offer at a radical discount in locations that are not obvious to customers. The program of integrated development of urban territories, which allows to create mixed-use clusters at the sites of inefficient industrial zones, could further spark the interest. Furthermore, preferences for projects creating new workplaces is an additional incentive for office project development.

Given the keen interest in the acquisition of ownership, sale is the preferred method of office asset divestiture (monetization). Purchase offers account for about 75% of the total office space in projects currently under construction.

Fig. 1
Distribution of construction volumes and office projects to be commissioned in 2023–2026
Source: Nikoliers



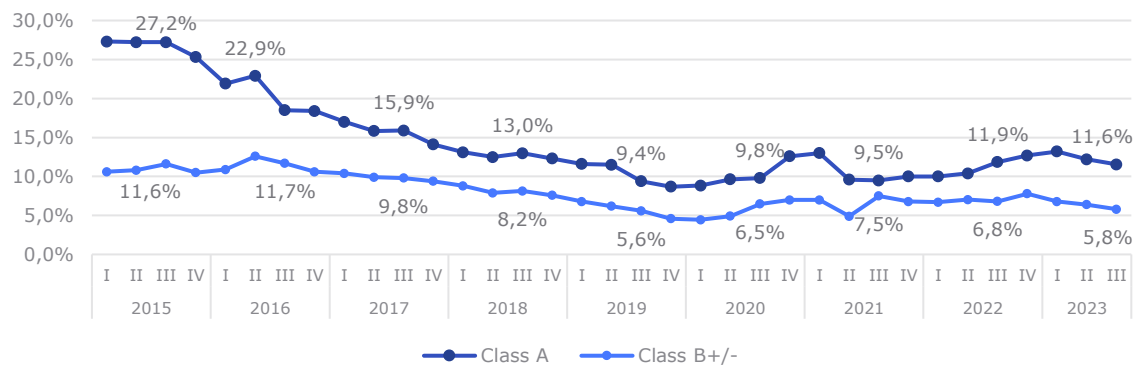
Vacancy rate

At the end of nine months of 2023 robust demand for office space reduced the vacancy rate to 7.4%, which is a record low for a similar period of the previous two years. The volume of net absorption demonstrates positive dynamics and as of the end of Q3 2023 amounts to 480,400 sq m.

The vacancy dynamics indicates the rapid occupation of offices, especially in the most attractive locations of Moscow. Thus, the vacancy rate in the Central Business District dropped by 1.3 p.p. as compared to the previous period, in premium locations – by 1.1 p.p., and in the Leningradsky Business Route – by 0.6 p.p.

That said, the average market vacancy rate in Class A and Class B+/- has dropped by 0.6 p.p. each, which indicates approximately the same activity of consumers in different price segments and in the office market across the board.

Chart 4
Vacancy rate by Class
Source: Nikoliers

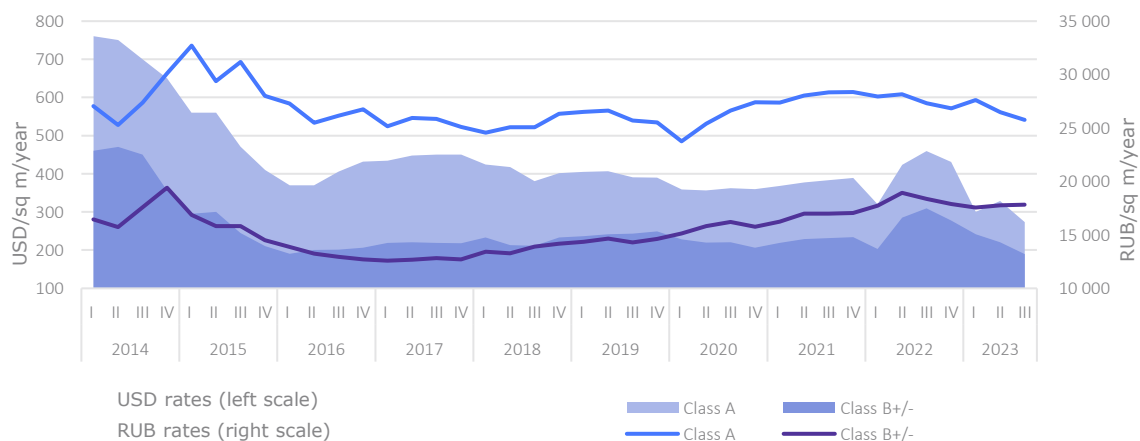


Rental rates

Weighted average rental rates are negatively affected by the dynamics in less popular locations and remote areas of Moscow outside the MKAD. Occupancy in the expensive price segment also drives down the average market rate, whereas prices do not go down in the existing facilities.

The rental cost in the Central Business District is stable, with a 2.1% quarter-on-quarter decrease in the Premium submarket due to the occupancy of some very expensive facilities. In Moscow-City MIBC the rental rate growth by 12.4% can be explained by the availability of new offers in the high price segment.

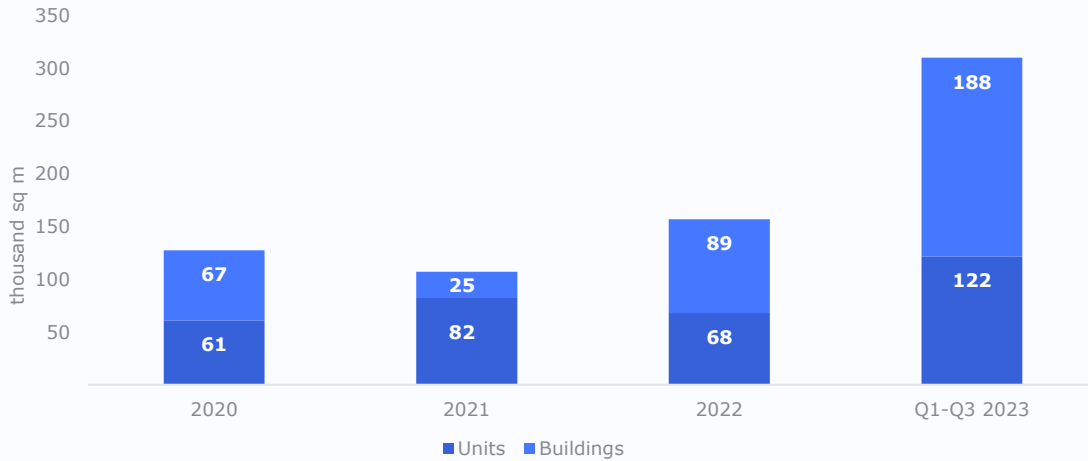
Chart 5
Rental rate by class
Source: Nikoliers



Office sales market

Chart 6

Breakdown of office purchase and sale transactions
Source: Nikoliers



Sales of office properties keep on breaking new records. In Q3 2023 there were a number of large transactions completed in the sales market in favor of IT and telecom companies, state corporations as well as construction and development concerns.

Approximately 22% of transactions in terms of office space are represented by sale and purchase deals in 2023. Such a high level of purchases by end users in the office segment was recorded for the first time. On average, the share of purchase transactions previously did not exceed 14% of the total demand for office space.

This growing transactional activity can be explained by market conditions, when acquisition

of the ownership title is seen as a valuable and liquid asset as well as a viable money saving alternative with a prospect of the office asset value to grow further.

The interest in buying whole buildings is still very high: based on the results for the nine months of 2023, such transactions account for 61% of total office space purchases. New business centres that meet modern-day requirements are always an attractive option for stakeholders. In the meantime, the availability of free finances at the disposal of companies acts as an additional impetus for the growth of cash investments in property.

Table 2

Key sale transactions in the Moscow office market, Q1-Q3 2023
Source: Nikoliers

Occupier	Size, sq m	Deal type	Property name	Address	Class
Moscow Mayor's	47,000	Sale	iCity Time Tower	37 Shmitovsky drive	A
VK	30,487	Sale	SkyLight, bld. A	39 bld. A Leningradsky Ave.	A
Natsproyektstroy	27,271	Sale	Orbital	10 Third Magistralnaya str.	A
Astra Group	22,250	Sale	Ostankino Business Park, phase II	16 Ogorodny drive	A
Rosselkhozbank	13,396	Sale	Oko, Phase II	19 First Krasnogvardeisky drive	B+

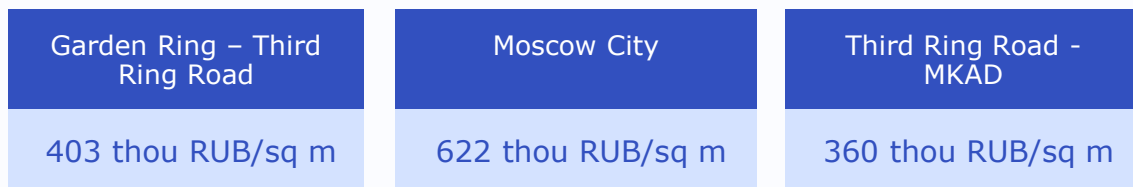


Office space supply in buildings under construction

Fig. 2

Weighted average asked wholesale prices (per unit purchases)

Source: Nikoliers



The purchase of buildings at an early stage of their construction is a good chance to select an attractive option at a reasonable price. Given the depreciation of existing buildings and the need for contemporary spaces, the acquisition of a new business centre is a rather attractive option for the placement of business structures.

The slowdown in the commissioning of newly built quality offices in the midst of burgeoning demand

from buyers leads to the fast reduction of offers available.

Meanwhile, MIBC Moscow City remains the most expensive location. Yet this business district is still in high demand even in the backdrop of cheaper offers in other less attractive projects.

Table 3

Off-plan supply

Source: Nikoliers

Ring zone/Unit size	<150	150 - 500	500 - 1 000	1 000 - 2 000	2 000 - 5 000	>5000	Buildings
Supply, sq m							
GR-TRR	1,232	3,739	3,824	19,871	10,325	15,600	55,784
Moscow City	-	7,900	2,107	21,765	2,242	-	-
TRR-MKAD	7,989	15,552	14,455	64,877	2,092	17,624	34,012
Average prices, thousand RUB/sq m							
GR-TRR	427	407	422	457	382	340	278
Moscow City	-	610	613	631	590	-	-
TRR-MKAD	376	365	342	359	495	349	311

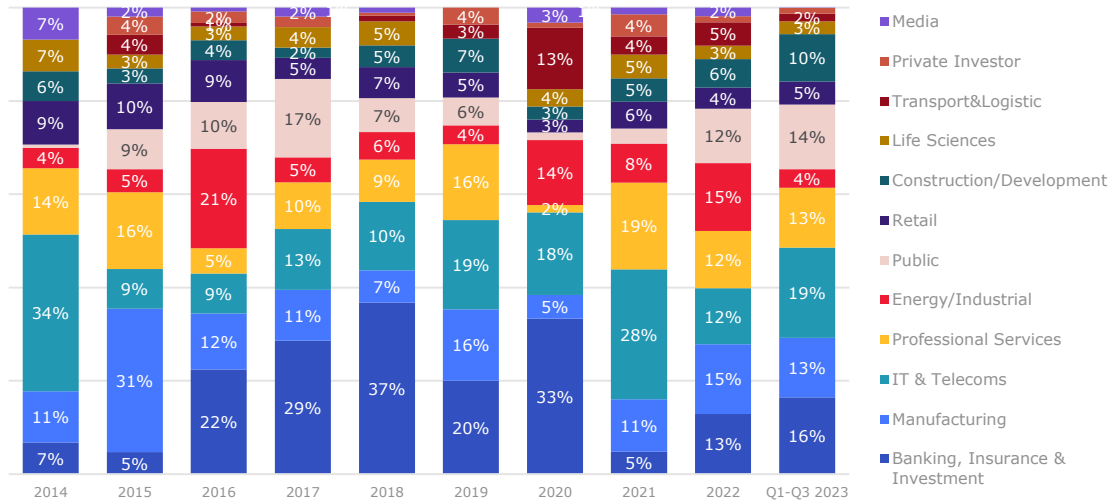
The prices include VAT except for co-investment projects.

Take-up

The demand in the nine months of 2023 totaled to 1,416,000 sq m, which is 4.2% higher than in the third quarters of the pre-pandemic period. This is more than double as high versus a similar period of the previous year and 25.7% higher than in Q3 2021. The market is currently at the stage of high business activity driven by the earlier unsatisfied demand of Russian companies and the general stabilization of economic relations inside the market.

Chart 7

Take up distribution by business sector, %
Source: Nikoliers



During the first to third quarters of 2023, the demand for office space was mainly generated by industries, such as IT and telecommunications (19%), banks and financial companies (16%), state-owned companies and non-profit organizations (14%) as well as professional services (13%) and manufacturing (13%).

Class A offices account for 42.3% of the total office space leased during the nine months, whereas 47.2% of demand fell to the share of Class B+ offices. As the offices in use become antiquated, the interest in top-quality facilities is not only bolstered by business structure development and the desire to place the whole team in one location, but also by the aspiration to improve the existing space.

Table 4

Key lease transactions in the Moscow office market for Q1-Q3 2023
Source: Nikoliers

Occupier	Size, sq m	Deal type	Property name	Address	Class
Central University (Tinkoff)	14,249	Lease	Ducat Place II	7 Gasheka str., bld. 1	B+
Promsvyazbank	13,916	Lease	Baltschug Plaza	7 Baltschug str.	A
Confidential	9,583	Lease	Legion II, Phase I	9 Bol. Tatarskaya str.	A
Confidential	9,519	Lease	Mokhovaya, Phase II	4-7, Vozdvizhenka str. bld. 1	A
Renaissance Insurance	9,500	Lease	Krylatsky hills business park	17 bld. 1, Krylatskaya str.	A



Trends in and forecasts for the office market

The facilities vacated after a wave of company relocations in 2022 are being rapidly occupied again.

Tenants do not miss on the opportunity to fill attractive office spaces, so quality assets are quickly absorbed, leaving the market. The growing lease transaction volumes clearly show that the adaptation to the new balance of demand and supply has completed in the market. The pent-up demand and Russian business development continue to be the main driving force behind the high demand for office space.

High office sale rates persist

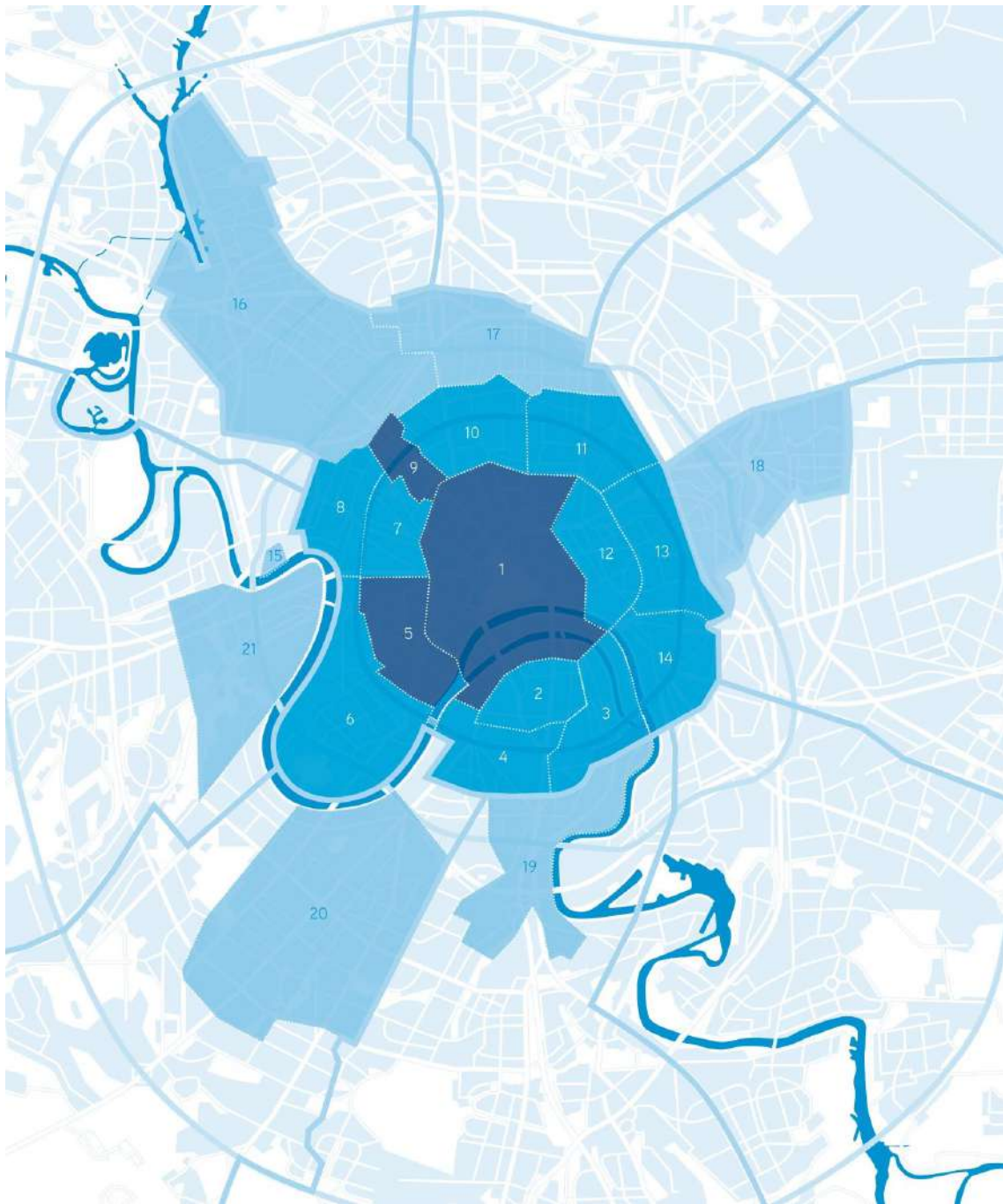
The record volume of sale transactions during the nine months of 2023 is the best evidence that the corporate sector has ample funds to finance business in the current market situation, being willing to save money by investing it in a stable high-quality asset. This means that the surging cost of debt financing will hardly trigger a drop in the level of purchase and sale transactions. The opportunity to bring the entire team together in one locus is an important factor for business right now, and so the possibility of buying a large office unit is quite important now. The obsolescence of existing office centres further whips up the interest in the acquisition of off-plan office facilities.

Business cluster development

In the midst of booming office construction business locations keep expanding with new clusters being shaped. Besides the central and prime locations, the northern and western ends of Moscow still rouse keen interest. The rent reduction is possible outside the key business districts, but in the most popular locations no negative dynamics can be expected.

Stable market development

We forecast that around 180,000 sq m of new office space will be built and commissioned in the fourth quarter of 2023. Given that Class A offices prevail in the announced construction projects, we can expect the demand being gradually shifted to this segment as vacant Class B+ premises are occupied. Vacancies will most likely stabilize at the current level, while the low occupancy of quality facilities outside the Moscow Ring Road will continue putting certain pressure on the average market rental rate which will hardly grow in the months to come. In the meantime, growing prices in the business districts boasting high demand will insignificantly drive the rates upwards within the precincts of "old" Moscow.



Submarket	Vacancy rate			Base rent*, RUB/sq m/year		
	A	B+	B-	A	B+	B-
1, 5, 9 Premium	16.7%	4.9%	4.0%	41,331	29,192	25,112
1-14 CBD (excl. Premium)	5.0%	5.5%	4.1%	31,559	23,083	22,886
15 Moscow City	5.0%	9.0%	-	42,193	37,369	-
16 Leningradsky	12.5%	11.5%	2.5%	34,964	23,466	15,802
17 Sushevsky	2.7%	3.0%	4.7%	21,218	16,307	13,491
18 Elektroavodsky	33.2%	6.9%	6.6%	15,371	12,649	11,605
19 Tulsy	18.0%	5.1%	4.8%	21,047	20,083	16,475
20 Leninsky	4.3%	4.7%	10.3%	18,593	17,990	21,292
21 Kutuzovskiy	-	6.2%	4.8%	-	18,666	17,333

*Excluding operational expenses, utility bills and VAT (20%).

Range of Moscow rings	Vacancy rate			Base rent*, RUB/sq m/year		
	A	B+	B-	A	B+	B-
Inside the Boulevard Ring	4.3%	3.4%	0.8%	49,345	33,602	33,098
Boulevard-Garden Ring	6.2%	2.9%	4.1%	37,703	29,676	23,616
Garden Ring - Ring-Third Ring Road (TRR)	8.0%	6.0%	5.2%	38,374	23,187	18,032
TRR-MKAD	6.7%	6.4%	5.8%	26,945	17,150	13,974
Outside MKAD	40.1%	12.1%	1.5%	13,412	8,700	6,821

Contacts

Igor Temnyshev

Partner

Igor.Temnyshev@nikoliers.ru

Office Agency Department

Victoriya Goryacheva

Associate Head

Victoriya.Goryacheva@nikoliers.ru

Tenant Representation

Francois Nonnenmacher

Director

Francois.Nonnenmacher@nikoliers.ru

Anastasia Romanova

Director

Anastasia.Romanova@nikoliers.ru

Office Sales

Andrey Kukhar, MRICS

Director

Andrey.Kukhar@nikoliers.ru

Kirill Kutyavin

Director

Kirill.Kutyavin@nikoliers.ru

Business Support Block

Olga Bakulina, MCIM

Business Support Head

Olga.Bakulina@nikoliers.ru

Research

Veronika Lezhneva

Director

Veronika.Lezhneva@nikoliers.ru

Mariya Kotelnikova

Analyst

Mariya.Kotelnikova@nikoliers.ru

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 **Nikoliers**

123112 Moscow
10 Presnenskaya Embankment
BC Naberezhnaya Tower
Block C, 52 floor