

Market Report

Ukraine
Year-End 2009



NAI Pickard

Commercial Real Estate Services, Worldwide.



Best commercial property agency,
Ukraine- 2009

Macroeconomics

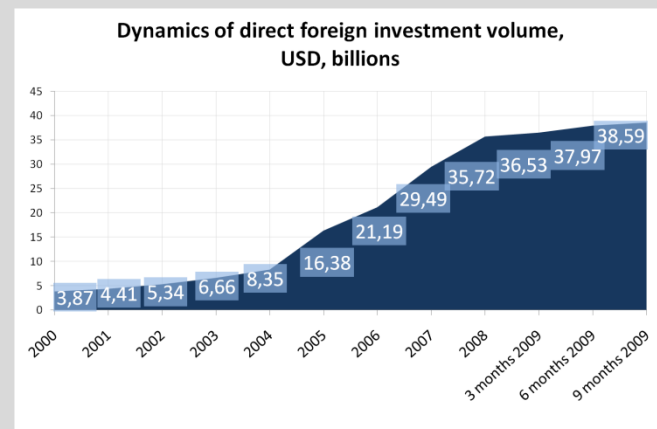
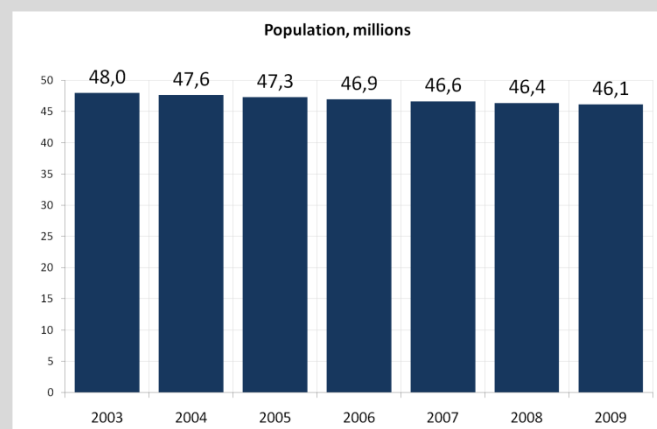
Year-End 2009

The year 2009 was overshadowed by the world economic crisis.

The crisis started in the autumn of 2008 and caused an immediate reduction in the investment funds available worldwide. Its impact on Ukraine was dramatic; from a high of up to \$8 billion of FDI it dropped to just over \$3 billion during 2009. Domestic investments also sharply reduced.

Also as Ukraine's exports were heavily reliant on metallurgy, chemical and heavy industrial products, primary products in the industrial processes Ukraine's exports were hit heavy and hard. More so than in most other European countries.

The consequences were that local and international companies that operate in Ukraine commenced cost cutting programmes with staff and/or salary cuts and in some cases salaries simply being delayed. White collar workers were affected mostly in major cities, but with less impact on blue collar workers. However a reduction of salaries and a decline in job security caused a consequent drop in consumer confidence and therefore reduced consumption. It had a similar effect on B2B and B2C.



Source: State Statistics Committee of Ukraine, IMF (Inflation and GDP forecasts)

Macroeconomics

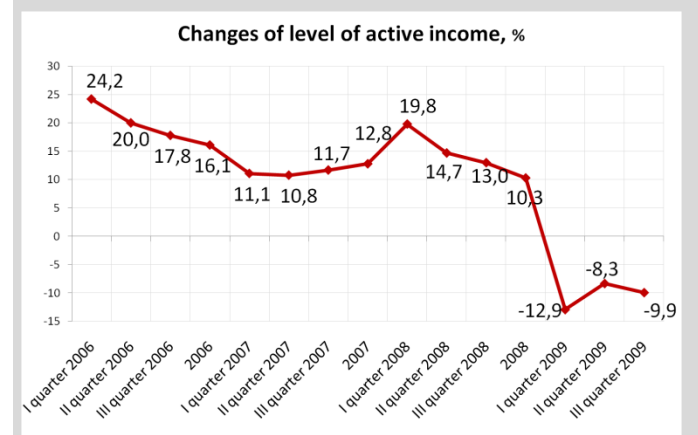
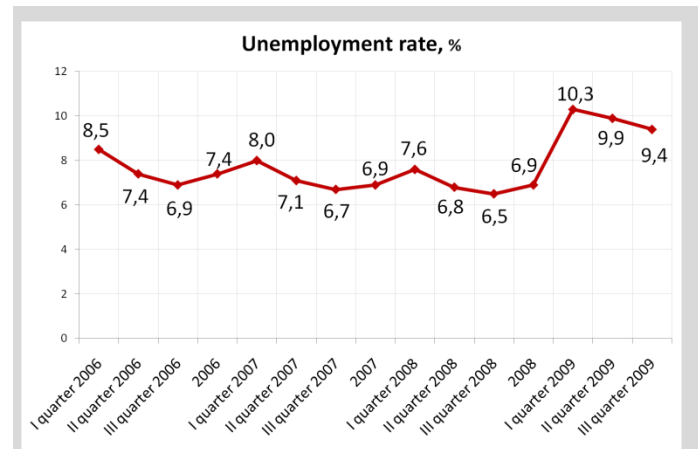
Year-End 2009

The ongoing political hiatus; presidential elections at the year end and continuous impasse between the then PM and President also made investors nervous and many put investment plans on hold.

Some these negative indicators slowed by the middle of 2009 and some positive trends started to appear.

Unemployment started to decline and according to Headhunter UA half of the companies they interviewed were planning to recruit by the year end.

Certainly the positive growth trends of India and China will increase the demand for Ukraine's primary products and provided positive trends in other world markets continue plus the end of the political hiatus the forecast for Ukraine in 2010 looks positive.



Source: State Statistics Committee of Ukraine

Hospitality market

Year-End 2009

General market situation

The hospitality market has fared better than other sectors and remains relatively stable due to the following factors: the perspective to host EURO 2012 (Kyiv, Lviv, Donetsk, Kharkiv; steady demand by foreign visitors for high-end hotels ; massive undersupply of quality hotel property, and a small number of international hotel chains.

Being optimistic about the EURO 2012 many owners expect to attract investments to their projects or, at least, make agreements with international hotel chains.

Projects of hotels and also mixed-use projects with hotels in their structures are starting to appear in greater number. This is done with the purpose to raise attractiveness of the project in general due to its hotel component.

Trends

A growth in hotel supply was observed, as the operators in this market segment became more active.

However this was not caused only by projects in city-participants of EURO 2012. New hotels were launched in Lviv, Kyiv, Truskavets, several cities in Crimea and in other regions.

Yet growth was mainly focused on Kyiv, where despite the crisis the growth in hotel rooms in 2009 was higher than in the previous years.

In 2009 in Kyiv 5* hotels with in total 553 rooms were launched. Among them there were 2 large projects: 5 star hotel Inter Continental and the 3 star Premier International Ltd. (national operator).

Hotels launched in 2009 (Kyiv)	Number of rooms	Class
InterContinental	277	5*
Visak	42	4*
City Hotel Management	23	3*
Royal Hotel de Paris	11	3*
Bakkara (Premier International Ltd.)	200	3*
Prospective projects (to be launched before 2012 r.)	Number of rooms	Class
Fairmont Raffles Hotels International , 1a Naberezhno-Khreschatytska St.	251	5*
Hilton, 28-30 Shevchenka St.	257	5*
24/39 Prorizna St.	180	4*
Holiday Inn, 79 Gorkogo St.	200	3*
34 Konstyantynivska St.	30	3*
Ibis (Accor Hospitality Group), 25 Shevchenko St.	213	3*
Prospective projects (to be launched after 2012 r.)	Number of rooms	Class
Sofitel, at the corner of Luteranska and Kruglouniversitetska	298	5*
Sheraton, 21 Naberezhno-Khreschatytska St.	239	5*
Crowne Plaza, Korolenkivska St.	225	4*
4* Hotel, 50-54 Antonovicha St (former Gor'kogo St.)	305	4*
Conference Hotel, 6 Sorokarichya Zhovtnya Av.	300	
Hilton Garden Inn, 29 Zhylianska St.	209	3*
Etap (Accor), Mechanizatoriv St.	202	2*
Hotel Holosiyvskiy, 93 Sorokarichya Zhovtnya Av.	280	2*

Hospitality market

Year-End 2009

Demand

The demand for hotel services has contracted with the weakening of business tourism, as budgets for business trips were substantially reduced because of the crisis.

As a result, the occupancy rate in Kyiv hotels has reduced 20% compared to 2008.

Yet even after such fall in demand the hotel property segment remained relatively stable.

Occupancy rate of high-end hotels, managed by international hotel operators, has always been higher than others (up to 70%), which has secured a steady demand.

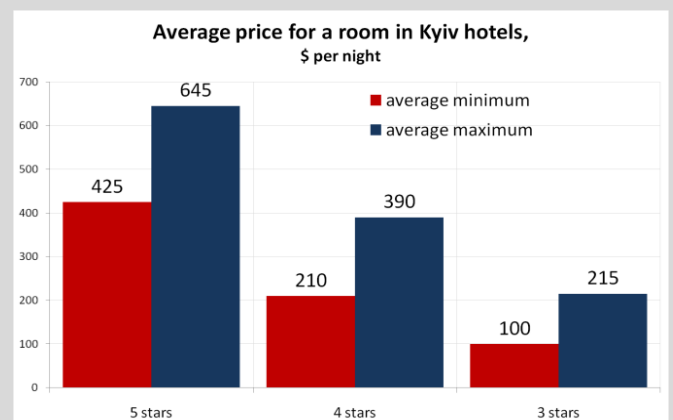
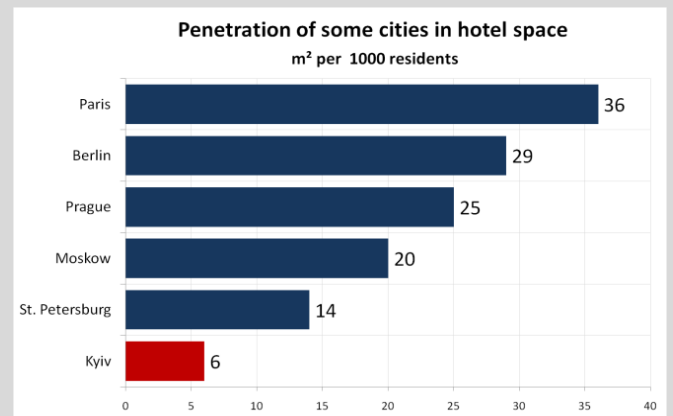
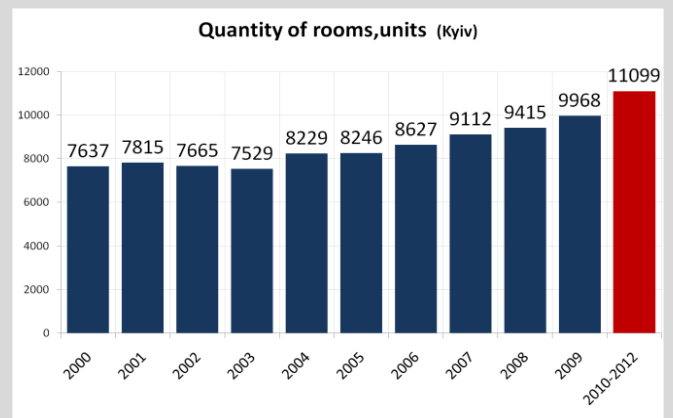
In 2008 occupancy rates were very high during Monday-Friday, up to 98%, but were very low at weekends due to no tourism. Therefore occupancy rates compared to other major cities for the week remained low.

However, projections for the hospitality segment are optimistic, and the main market players expect its full recovery in a year or two.

Prices

The drop off in demand for hospitality services caused hotel operators to lower their prices. As the demand reduced by 20%, prices also went down by 20%.

However it should be noted that typically quality hotel room prices in Kyiv remain high compared to their European counterparts. Prices in 3-5 star hotels are often 1.5 to 2 times higher even during the crisis. Consequently yields on hotel projects remain attractive.



Hospitality market

Year-End 2009

Prognosis

It is expected, that new hotel projects will be developed in the cities, where EURO 2012 matches will be held (Kharkiv, Donetsk, Kyiv, Lviv), and also in the most popular resorts in Crimea and the Carpathian Mountains.

It is forecasted, that during the next year or two the hospitality service will develop mainly in the highest category (4-5 stars), since there is currently a major shortage in this segment.

Following the high-end hotel operators, economy chain hotel brands also started to look closely at the Ukrainian market.

Any development activity will most likely take place with the involvement of international hotel operators. Already now they are showing strong interest in Ukraine.

International hotel operators, which have expressed intention to develop in Ukraine	Class
Hilton	5*
Fairmont Hotel Kiev	5*
Sofitel (Accor Group)	5*
Reikartz Hotels & Resorts	4*
Park Inn (IHG)	4*
Sheraton (Starwood)	4*
Crowne Plaza (IHG)	4*
Novotel (Accor Group)	4*
Holiday Inn (IHG)	3-4*
Ibis (Accor Group)	3*
Regent	3*
Ramada Encore (Wyndham Hotel Group)	3*
Etap (Accor Group)	2*

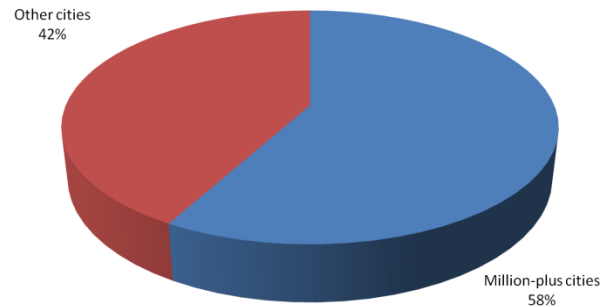
Retail Market

Year-End 2009

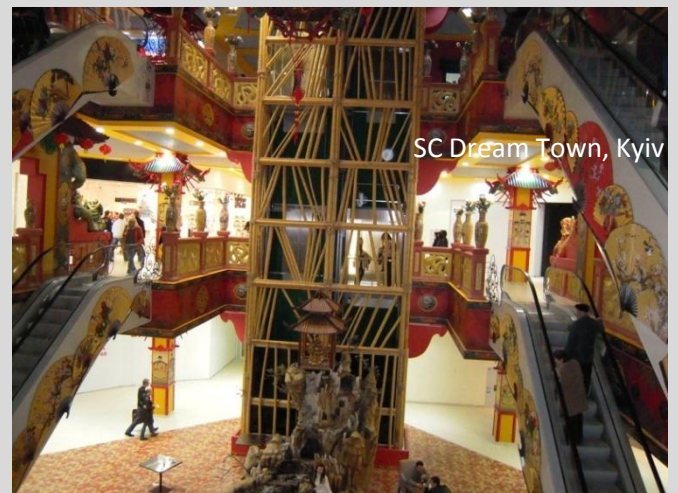
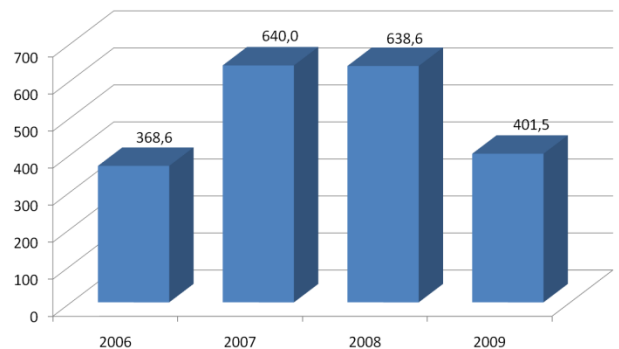
Market situation

The crisis has noticeably negatively influenced the development of the shopping centre market in Ukraine. The foot flow to shopping centres has declined, vacancy rates have increased, and average rental rates have come down. The supermarket brand Okey has left the market, and the DIY network Karavan has reduced its presence in the Ukrainian market to just one store. But there are also positive trends. Auchan is continuing to expand with new hypermarkets as is Metro Cash & Carry. Real and Novus opened their first stores in 2009 and OBI maintains its presence in the market. There are other international retailers considering entering the Ukrainian market on the first significant signs of recovery. Also despite the decrease in retail turnover in Ukraine, according to the A.T. Kearney Global Retail Attractiveness Year List Ukraine ranks 17th as in the previous year. However during 2009 the focus remained on cities with a million plus inhabitants. There was also a trend towards reconceptualization of operating shopping centres: SC Europort (Kyiv) reconsidered its tenant mix and made a re-launch in a renewed format.

Retail space of shopping centres put into operation in 2009



Increase in retail space in SC of Ukraine, thousands m²



Retail Market

Year-End 2009

Trends

Despite the negative economics in 2009 24 shopping centres were opened (instead of 57 announced), and 3 shopping centres expanded their retail space. Most of the shopping centres, 7 in total, were opened in Kyiv. The largest of these were Dream Town (Kyiv), Riviera (Odesa) and Kiev (Poltava). Today there are about 330 retail property units which can be considered as shopping centre and their combined total area is 3.1 mln m².

The growth of retail space during last year was 401, 500 m², which is 1.6 times less than in the previous year.

Percentage growth of retail space was 15% compared to 21% in 2008.

The growth was focused on the million-plus cities.

Currently the average m² of retail space in Ukraine is 68 m² per 1000 inhabitants compared to 163 m² in Poland.

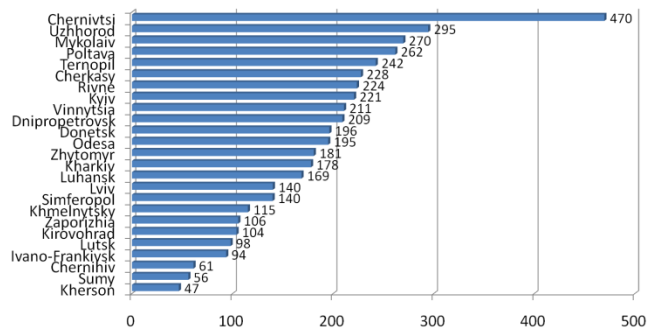
Demand

Chain retailers indicated in a survey that they would be ready to expand at first in Kyiv, then in the million-plus cities and lastly in the smaller regional centres. A similar tendency was observed concerning the occupancy of shopping centres. By the end of 2009 the vacancy rate for shopping centres had increased by about 65%. Hence, vacancy rates in shopping centres at the end of 2009 were slightly more than 2% in Kyiv, 6-10% in the million-plus cities, and on average 15-20% in the smaller regional centres.

In Kyiv and the million-plus cities the vacancy rate of shopping centres is acceptable.

The main indicators of shopping centre market in Ukraine in 2009	Ukraine	Kyiv
Quantity of SC	332	42
Retail area in SC, millions m ²	3,12	0,61
Vacancy rate of retail space in SC, %	13	2
Average rental rate for vacant spaces, \$ /m ² per year	264	683

Penetration of regional centres of Ukraine in retail space in shopping centres as of 01.01.2010, m² per 1000 residents



Major shopping centres opened in 2009	GBA, thousand m ²	GLA, thousand m ²
Dream-Town (Kyiv)	80,0	40,9
Riviera Shopping City (Odesa)	60,0	48,0
4Room (Kyiv)	40,0	23,4
Appolo (Dnipropetrovsk)	30,0	19,5
Domosfera	30,5	20,2

Retail Market

Year-End 2009

This success of the big city centres compared to the regional centres appeared to be primarily due to a better design concept and management. Often the good centres remain full while the poorer centres suffer the brunt of the decline of the retail space demand.

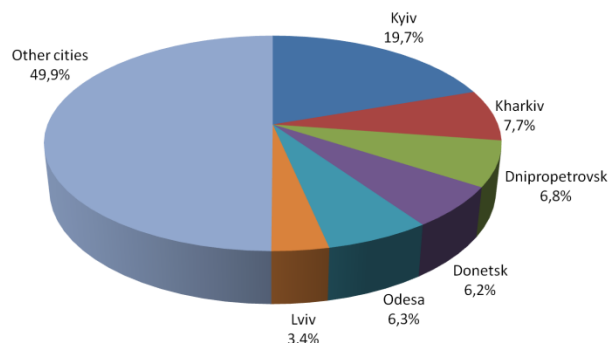
Rental rates

Rental rates from the end of 2008 considerably decreased in all shopping centres. In \$ terms the average rental rate decreased by 50% and more and by the end of the year it was \$57 per m² per month for shopping centres in Kyiv and in the million-plus cities the base rate was approximately \$20 m² per month (including VAT). After the drop in rental rates from the beginning of 2009 a number of shopping centres started to significantly increase their rates since autumn 2009.

Prognosis

Very few new shopping centres are expected to open during 2010. Probably only those that were in the final stages of commissioning in 2009, with virtually no newbuild projects. With the fundamental low density of retail space in Ukraine compared to its immediate neighbouring countries as the market returns there will once again be a great shortage of retail space with consequent rapid increase in rental rates. Also poorly conceived regional centres will need to reconceptualize and/or change management style or close.

Allocation of operating shopping centres as of 01.01.2010



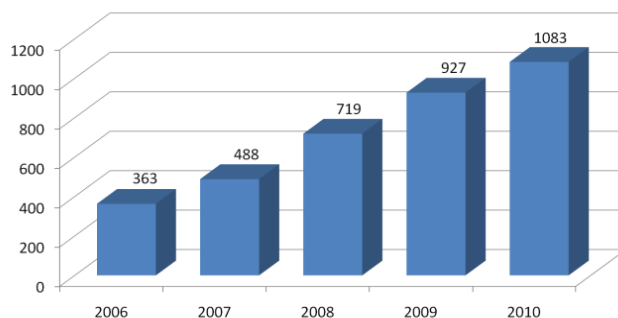
Office market

Year-End 2009

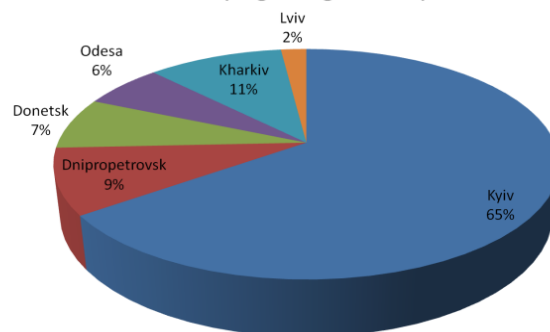
Market situation

The primary activity for tenants and landlords alike during 2009 was the adjustment of their office space and/or cost to the new market conditions. Some needed less office space due to a reduction in their business activity and consequent staff reduction; others needed to reduce office costs due to the new economic environment. Up to 2008 rents had generally been set in \$ paid in UAH but when the ROE changed from 5 to 8 to the \$ (a 60% increase) tenants started demanding a rent reduction combined with the rent being fixed in UAH only. Other actions taken was to sublease unneeded space often at drastically reduced rates from the primary lease rate, to trade down in quality and size or even more drastically to close down and leave the country. Landlords had little choice but to comply with their tenants' demands because vacancy rates had gone from 2% to as high as 15% and they could be left with vacant space and zero income as there were virtually no new tenants entering the market. Towards the end of 2009 the market was stabilizing albeit a low level. However it is worth noting that generally rental rates per m² in Ukraine still remain higher than their European counterparts.

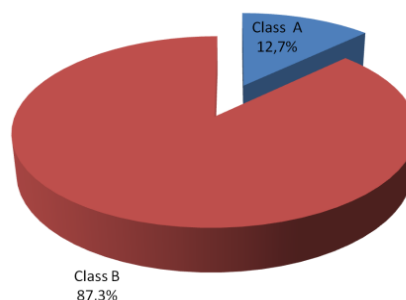
Volume of supply of office space in class A and B business centres
as of beginning of the year, thousand m²



Allocation of office space in business centres in the cities (beginning of 2010)



Allocation of office space in business centres according to class, beginning of 2010



Office market

Year-End 2009

Trends

The penetration of quality office space in Kyiv, not to mention other Ukrainian cities, continues to lag considerably behind that of other European cities. The capital of Ukraine has only 253 m² of A and B Class office space per 1, 000 population, compared to 1450 m² of the same class of space in Warsaw.

Also the crisis has significantly changed developers' plans regarding the commissioning of new quality office space. Out of 300 thousand m², which were announced at the end of 2008 for 2009, only 156 thousand m² (about half of the projects) were actually commissioned. Thus the growth of office space in 2009 was 16.8%, which is the smallest growth for the last 4 years.

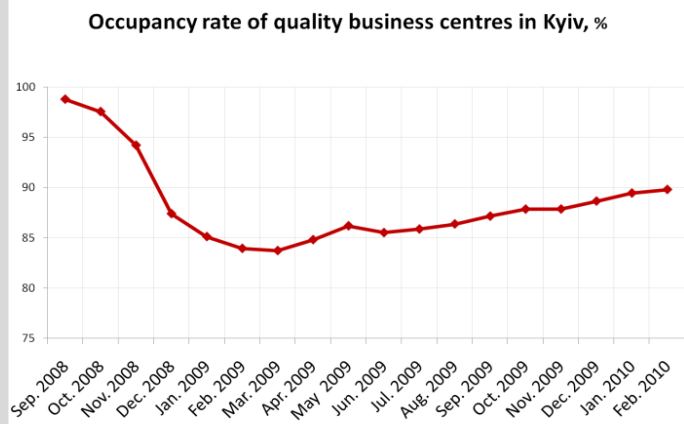
By the end of 2009 the market share of class A business centres was 12,7%.

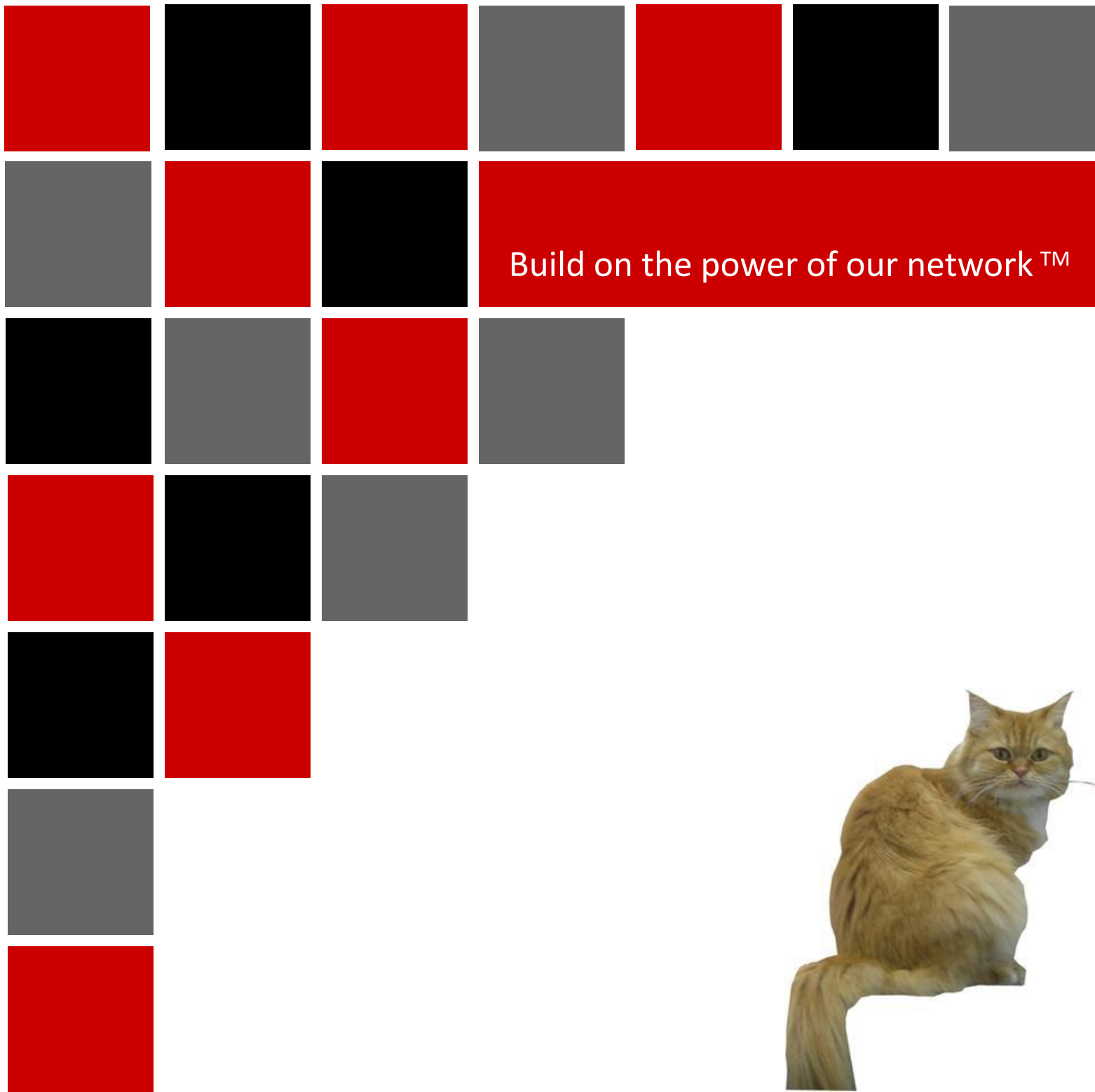
It's worth pointing out, that in 2009 class A business centres were launched only in Kyiv and Dnipropetrovsk with the majority in Kyiv. There was going to be a project in Donetsk but it was changed to a hotel and retail project.

Prognosis

Due to this very low level of m² of office space compared to other European counterparts there is a strong argument that as the market economy starts to grow again vacant space will quickly be absorbed and rental rates will start to climb again. Some pundits put this in the 2nd half of of 2010, some in the 1st quarter of 2011. There appears little doubt that this will happen, the only question is when. At NAI Pickard we believe the most likely scenario is the 2nd-half of 2010.

The main indexes for BC market in 2009	Total area of BC, thousand m ²	Vacancy rate, %	Rental rate, \$ per month per 1m ²
Kyiv	704.3	11-12	22-25 (class A – 35)
Kharkiv	112.2	18-25	12-13
Donetsk	78.4	15-18	16-18
Dnipropetrovsk	100.1	15-20	14-15 (class A – 20)
Odesa	66.8	14-16	15-17
Lviv	21.0	14-16	10





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