

COMMERCIAL REAL ESTATE MARKET COMMENTARY

LITHUANIA / Q2 2017

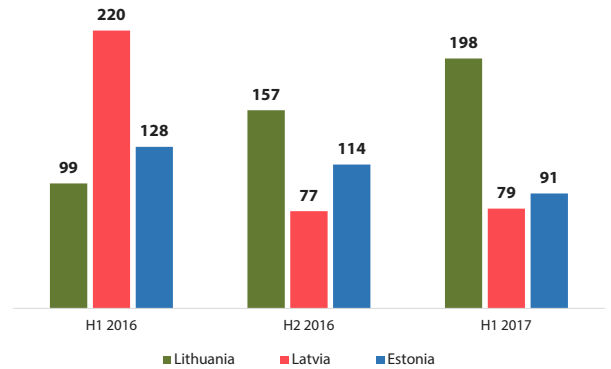
In the first half of 2017, investor activity in commercial real estate in the Baltic countries was not uncommon, but the recorded scope of investment showed an unfading interest in the modern commercial property. A total of 18 investment transactions were concluded in this period in Lithuania, Latvia and Estonia, which involved the purchase of over 312,000 sqm of cash flow commercial property (modern offices, retail, warehousing and industrial buildings and premises, at least EUR 1.5 million in value). The total value of the acquisitions was EUR 368 million, nearly 18% less compared to the first half of 2016.

One transaction concluded in mid-2017 had a major effect on this year's indicators. The transaction involved the acquisition of 80% ownership interest in the property investment company, Baltic Retail Properties, by CPA[®]:17 – Global of the US investment company W. P. Carey, and the Finnish Kesko Corporation. The property portfolio of Baltic Retail Properties comprises 18 retail stores in Lithuania, Estonia and Latvia, and a logistics centre in Lithuania. Following the acquisition, CPA[®]:17 – Global controlled by W. P. Carey Inc. became the main shareholder of Baltic Retail Properties paying EUR 127 million (including acquisition-related charges and costs) for its 70% share. Meanwhile Kesko acquired 10% of the shares of Baltic Retail Properties following Kesko's sale of its 7 retail stores in Latvia and Estonia to Baltic Retail Properties for EUR 64 million.

Lithuania shared the major portion of the investment in the first half of 2017, i.e. EUR 198 million or 54% of the overall investment in the Baltic countries. The largest investment transactions in Lithuania during the period were the said acquisition of the shares in Baltic Retail Properties and the acquisition of the Vertas and Pentagon office buildings in Vilnius. In June 2017, the Swedish investment company Eastnine (former East Capital Explorer) completed the acquisition of Vertas. The company paid EUR 29 million for the building, which, according to the buyer, at the time of the acquisition guaranteed about 6.5% yield. The Finnish property investment and management company Technopolis purchased an almost completed office building in Ozas Park from the ICOR Group. The transaction involved the purchase of both the office building and the parcel of land next to the building. The acquisition of the building was completed in April, and the acquisition of the land is scheduled for completion by the end of 2017. The total transaction value is about EUR 32 million. According to the official notice of Technopolis, the initial yield of 6.5% is forecast on completion.

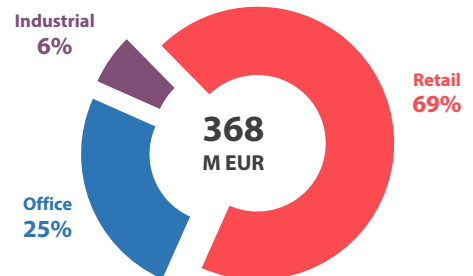
The value of investment transactions in Estonia in the first half of 2017 totalled EUR 91 million or 25% of the overall investment in the Baltic countries. The largest investment transactions in Estonia involved the sale of 3 retail centres managed by Kesko to Baltic Retail Properties, the acquisition of the shares in Baltic Retail Properties mentioned above, and the sale of the Prisma Shopping Centre in the city of Narva (the shopping centre was purchased by the French property management company CORUM for EUR 16.7 million from EFTEN Kinnisvarafond AS controlled by EFTEN Capital). Latvia saw the smallest share of investment over the period totalling EUR 79 million. The major portion of the investment in Latvia accounted for the sale of 4 retail centres managed by Kesko to Baltic Retail Properties and subsequent sale of the shares of Baltic Retail Properties to CPA[®]:17 - Global.

COMMERCIAL PROPERTY INVESTMENT VOLUMES IN THE BALTICS
(million EUR)



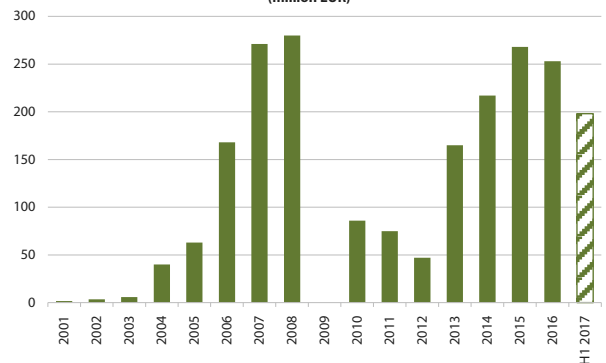
Source: Ober-Haus / 2016 - 2017

COMMERCIAL PROPERTY INVESTMENT VOLUMES BY SECTOR IN THE BALTICS



Source: Ober-Haus / H1 2017

COMMERCIAL PROPERTY INVESTMENT VOLUMES IN LITHUANIA
(million EUR)



Source: Ober-Haus / 2001 - 2017

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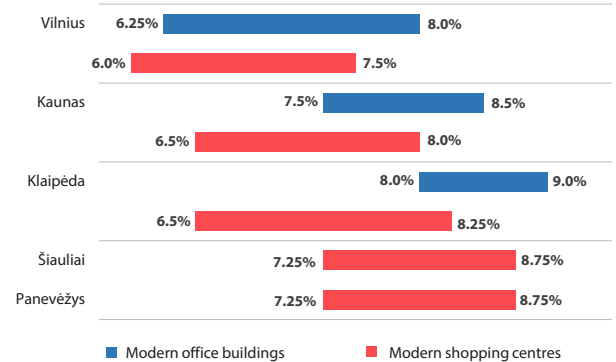
Transactions involving W. P. Carey Inc., Kesko and Baltic Retail Properties determined the distribution of investment by property segments in the first half of 2017. Of the total EUR 368 million invested in Lithuania, Latvia and Estonia 69% went to the retail property sector. A total of 25% investment was made in offices and the remaining smallest portion (6%) was traditionally invested in warehousing facilities. The largest transaction in the warehousing property segment was the purchase of 21,000 sqm logistics centre in Vievis (with Rimi as the anchor tenant) by the Estonian investment company United Partners Property from Sirin Development.

One large investment transaction determined that US investors (W. P. Carey Inc.) were the largest single investors in modern commercial property accounting for 33% of the total investment in the Baltic countries in the first half of 2017. Local investors from the Baltic countries accounted for another 33% of the total investment and investors of other countries (Denmark, Finland, France, Sweden, Russia, and the UK) accounted for the remaining 34% of the total investment. The geography of investors in the Baltic countries does not expand considerably – local, Scandinavian and private investors continue to take centre stage. However, new international investors in the Baltic market (e.g. W. P. Carey Inc.) tend to expand their portfolios; the market also attracts new market players (e.g. the French property management company CORUM, which has made its first acquisition in Estonia this year). Despite the new larger investors in the market, the geographic pattern of investment remains limited. For example, over the past 17 years, investors from 15 different countries have invested in the developed commercial property in Lithuania and this number has not changed since 2015.

In 2017, activity in the commercial real estate market reached record new levels countrywide. According to the data of the State Enterprise Centre of Registers, the first half of this year in **Lithuania** saw over **4% more** transactions on non-residential properties (buildings and premises) compared to the same period in 2016. In total, 9,159 non-residential buildings and premises were purchased over the first half of this year in Lithuania and this is the best first half year result in the country's history. According to Statistics Lithuania, construction works worth **EUR 404 million** were carried out in the non-residential buildings sector in the first half of 2017 or **15% more** than in the same period in 2016.

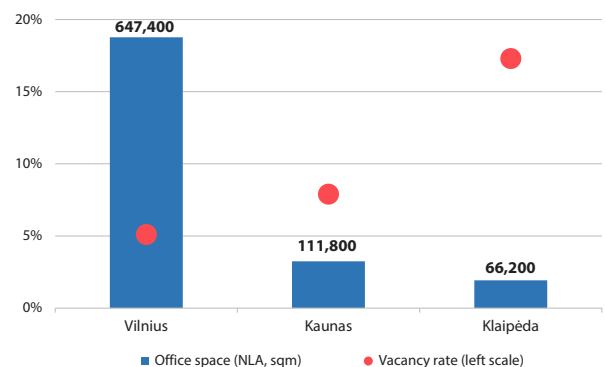
In Q2 2017, the fastest expansion of new offices was recorded in Kaunas city. Developers and other companies actively developed buildings of different purpose which provided new area for offices both for own needs and for the market. All in all, five different purpose construction projects were completed. All five projects offered a total of 14,700 sqm useful office area (A and B blocks in Prospekto Verslo Parkas, Sitis, Žaliakalnio Terasos, B66 and the newly completed headquarter of the consulting company SDG). Due to these projects the modern office premises market in **Kaunas** grew by as much as 15% over the second quarter of this year and the total office supply reached **111,800 sqm**. This sharp growth in supply affected the vacancy rate in Kaunas – over the second quarter of this year it increased from 2.4% to **7.9%**. The largest area of office premises was offered by YIT Kausta, the construction and development company which has completed construction of the office building B66 on K. Baršausko Street offering about 4,900 sqm of office area to the market.

COMMERCIAL PROPERTY INVESTMENT YIELDS



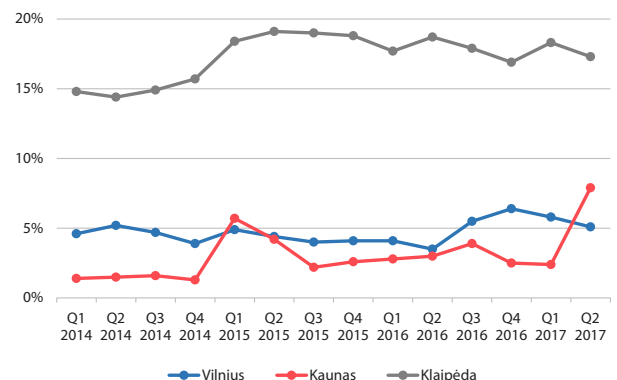
Source: Ober-Haus / Q2 2017

MODERN OFFICE STOCK AND VACANCY RATE



Source: Ober-Haus / Q2 2017

MODERN OFFICE VACANCY RATE



Source: Ober-Haus / 2014 - 2017

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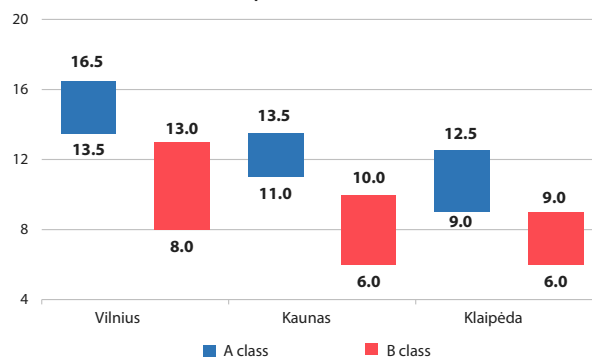
LITHUANIA / Q2 2017

On completion of the development, about 70% of its premises were already rented. The biggest tenants are the IT companies Teltonika and Virtustream. Since there is no longer any shortage of administrative premises projects in Kaunas and the market will gradually be supplemented with new projects in 2017–2018, it is inevitable that there will be an increase in the number of vacant premises. However, the wider choice also makes the demand more active since companies can plan their expansion very realistically or consider establishing their business in Lithuania's second biggest city. Kaunas is still very attractive for larger companies where rents are on average 20% lower than in Vilnius. Recently the office rents in Kaunas has stabilised and it is unlikely that it will increase significantly in the existing competitive environment. Over 2017 alone, the modern office market in Kaunas city will be supplemented with a useful office area of 30,000–40,000 sqm, i.e. this year the total modern office premises market in Kaunas might increase by as much as 30–40%. At the end of the second quarter this year, the rents for A class offices in Kaunas was **11.0–13.5 EUR/sqm**, B class – to **6.0–10.0 EUR/sqm**.

Meanwhile, the country's capital welcomed the second quarter of this year in a more modest manner since the construction of an office building of P. Baublio Street had been completed just before Q2 2017. This building, Santariškes Medical Business Center, with an area of around 2,000 sqm was rented to one tenant (private clinic). The total area of the modern office premises grew to **647,400 sqm** at the end of the second quarter in Vilnius. Meanwhile, tenants of office premises were particularly active and continued to reduce the amount of vacant premises in already operating office buildings. The area of rented modern office premises amounted to over 11,000 sqm in the second quarter of this year in Vilnius and reduced the total vacancy rate from 5.8% to **5.1%**. The vacancy rate of A class offices accounted for 2.7%, and of B class – for 6.3%. It could be said that the speedy development of modern office premises that has taken place over the last few years in Vilnius has been successful. Taking a look at the projects that have been completed in 2017 and that are nearing completion, it can be seen that new projects have definitely received a considerable amount of interest on the part of tenants. Most of the latest projects do not face any major problems in relation to finding tenants. Even some lease agreements are signed beforehand, though construction has not even started, and this fact signals a sufficiently fast business development. If all the planned projects will completed this year, the market of modern offices in Vilnius city will be replenished with up to 15 different projects or their stages with a total useful area of 84,000 sqm. The well-balanced supply and demand continues to maintain stable office rents in Vilnius which, in principle, have not changed since the end of 2015. Currently, B class offices are renting at **8.0–13.0 EUR/sqm**, A class – at **13.5–16.5 EUR/sqm**.

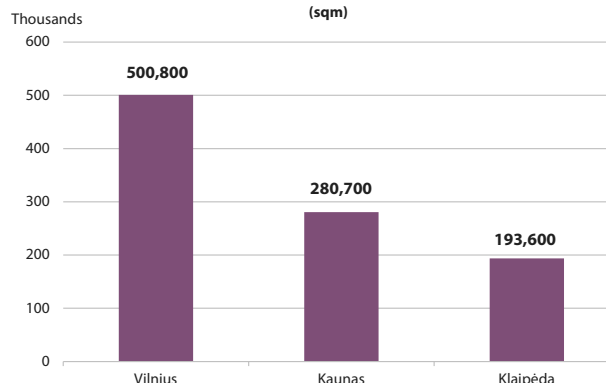
Meanwhile the office market in Klaipėda city continues to be stable. The port city has long failed to demonstrate any abundance of new projects. Nevertheless, lately, the development of some small projects can be noticed. In the third quarter this year, the construction of a new 1,000 sqm area building on S. Nėries Street should be completed. It is planned to rent the building to companies in the medical services industry. No other major office development plans are anticipated in Klaipėda in the near future. The previously announced and already launched development of the industrial territory on Liepų Street, which is being carried out by Viremidos Investicijos and which planned to build the office building Kamino Biurai during the first stage, is now being adjusted.

MODERN OFFICE RENTS (EUR/sqm/month, without VAT)



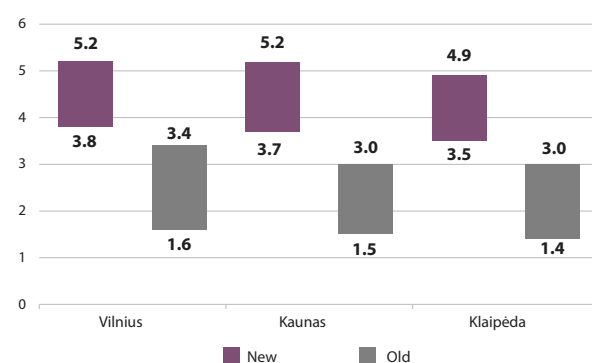
Source: Ober-Haus / Q2 2017

MODERN WAREHOUSE STOCK (sqm)



Source: Ober-Haus / Q2 2017

WAREHOUSE RENTS (EUR/sqm/month, without VAT)



Source: Ober-Haus / Q2 2017

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This territory will now be used for the development of the technology park Inovacijų ir Verslo Slėnis which should house institutions and agencies training IT, digital design and other innovative field specialists. The sluggish expansion of companies that need modern and more expensive office premises continues to maintain a fairly high level of vacant premises in Klaipėda city. Although the vacancy rate of modern office premises reduced from 18.3% to **17.3%** over the second quarter of this year, this indicator has remained within the range of 15–20% since the end of 2011. Meanwhile, investors in new and bigger scope projects are deterred by relatively low office rents whose growth potential is limited due to too small demand. For example, recently only the administration of Klaipėda city municipality has considering acquiring or renting larger premises. For this reason, office rents have remained the same: they are **6.0–9.0 EUR/sqm** in B class buildings, and **9.0–12.5 EUR/sqm** in A class buildings.

The recovering transport and logistics services sector has finally provided a stimulus for the development of warehousing premises in the country's biggest regions. According to the data of Statistics Lithuania, sales revenue of transport and warehousing companies in Lithuania grew by 17.8% in Q1 2017 compared to the same quarter last year. Meanwhile, the sales revenue of warehousing and storage companies (excl. VAT) was EUR 33.4 million over the same period or 12.5% and 23.7% more compared to the same periods in 2016 and 2015 respectively.

The revival in the development of warehousing premises can be felt in Vilnius and Kaunas regions where development projects are taken up not only by companies which build for their own needs but also by property developers. Some projects have even been launched without prior lease agreements. As many as three new warehousing and logistics premises projects were implemented over the first half-year in **Vilnius and Kaunas regions**; the total area of warehousing premises from these projects amounts to about **20,400 sqm**. The two biggest projects have been implemented in Vilnius: the logistics and transport company Ad Rem has built a warehouse in the territory managed by it in Kirtimai district, and a Norwegian company, Baltic Sea Properties, has completed the construction of a logistics centre not far from the Vilnius–Druskininkai road (a logistics centre with an area of 13,400 sqm has been leased along with administrative premises to a logistics company Rhenus Svoris). Following the implementation of these projects at the end of the second quarter of 2017, the total area of warehousing premises in Vilnius city and its surroundings increased to **500,800 sqm**.

Over this period, a small project was implemented in Kaunas district as well: Vetmarket built a modern veterinary pharmacy warehouse for its own needs. Further projects are currently being developed in Kaunas city and its surroundings and these should increase the area of warehouse premises noticeably this year. Over the second half-year of this year, construction of the Aibė logistics centre should be completed, as should the Epro group warehousing and administrative premises near the Islandijos road. Analizė, a company specialising in sales of odontological and other medical measures is building a new medicines warehouse with administrative premises in Ringaudai district. Meanwhile, Petrašiūnai district is seeing the approaching completion of a warehousing building with an area of almost 4,000 sqm. In total, these projects should implement the modern warehousing premises market of Kaunas with a further 34,700 sqm of warehousing premises. Presently the total area of modern warehousing premises in Kaunas city and its surroundings is **280,700 sqm**.

Over the second half of 2017, Vilnius should record completion of four more warehousing projects (or their stages), with a total area would of 39,100 sqm. These projects are being developed by Sirin Development, Arvydo Paslaugos, Woodline, and MG Valda. Taking into account all these projects, in 2017 alone, Vilnius and Kaunas regions will have almost 74,000 sqm of new warehousing premises, which means an almost 10% annual growth in supply in these regions. Taking a look at next year, it can be seen that developers and companies are not going to stop and that there are plans to invest in the modernisation of available premises, in their expansion and in construction of new projects for rent in Vilnius and Kaunas regions.

Moderate growth in rents of warehousing premises has been recorded in the last few years. This growth has continued this year as well. The remaining demand for modern premises contributed to the development of this sector and to the growth of property prices. Over the first half 2017, rents of new and old warehousing premises in **Vilnius region increased** by **3–4%**, meanwhile, the rents of warehousing premises in **Kaunas and Klaipėda regions** grew by **1–2%**. Currently, new warehousing premises in **Vilnius** are offered for rent at **3.8–5.2 EUR/sqm**, and old premises are available for **1.6–3.4 EUR/sqm**. In **Kaunas**, new warehouses can be rented for **3.7–5.2 EUR/sqm**, and old ones for **1.5–3.0 EUR/sqm**. In **Klaipėda**, new warehouses are available for **3.5–4.9 EUR/sqm**, and old – for **1.4–3.0 EUR/sqm**. The growing financial capacity of tenants, increasing prices for land and increasing construction costs might determine further moderate rents growth in the near future.

When using the survey data, a reference to **Ober-Haus Real Estate Advisors** is required.

If you wish to receive any additional information about development of the real estate market in Lithuania, Latvia, Estonia or you would like to order a special report on the part of the market relevant to you or the market of the project in progress, please contact Ober-Haus real estate market analysts.

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