

Lithuanian Commercial Real Estate

Q1 2012

MARKET COMMENTARY

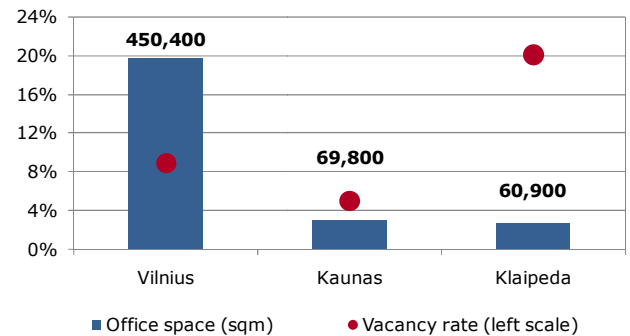


The start of 2012 did not bring any major changes to the Lithuanian commercial real estate market. Construction of commercial premises continued, new projects were introduced to the market, and attempts were made to lease or sell existing vacant premises. Movement in this sector was stronger in Vilnius after developers decided last year that it was time to revive the dormant commercial property market and to continue, as well as resume construction of new modern office buildings.

The development of business centres in Lithuania's capital has become the mainstay of the commercial sector. In 2010, rapidly decreasing vacancies in office premises and the suspension of construction projects in the commercial premises sector determined the rather bold decision by developers to revive or resume the construction of new business centres. Earlier this year, reconstruction of a small business centre (about 2,000 sqm usable office area) was completed in the Naujamiestis district, Vytenio Street. The opening of such a small project will not affect the Vilnius office market unlike other much larger projects currently being implemented, which will undoubtedly affect the performance of this sector. There are currently seven business centres under construction in the capital, with the consequent future availability of an additional **32,800 sqm** of modern office space. Despite the rapidly growing competition, plans launching the construction of at least three other large business centres in the near future have been announced (the largest of these is the Quadrum business centre on Konstitucijos Avenue). In view of these pending projects, the modern office market in Vilnius should theoretically be supplemented with over 80,000 sqm of usable office space over the next two years. The question naturally arises whether this planned investment is justified, and whether the capital needs this much office space in the near future?

The vacancy figures in Vilnius have not changed considerably over the last year and a half. Since Q3 2010, the office vacancy rate in Vilnius has been around 9-10%. The vacancy rate in Q1 2012 rose slightly in Vilnius, from 8.8% to **8.9%**, with a total vacant area of **39,900 sqm**. This means that the development of local companies is not that fast, whereas the arrival of larger international companies in the Lithuanian market is not as constant or plentiful as earlier anticipated. Furthermore, completion of the seven business centres is unlikely to lead to an overall reduction in vacant area. Given the current market situation, it can hardly be expected that these centres will be fully leased prior to their opening expected later this year.

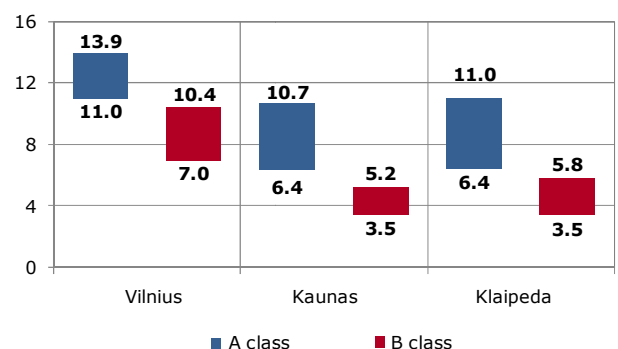
Modern office stock and vacancy rate



Source: Ober-Haus

Data: Q1 2012

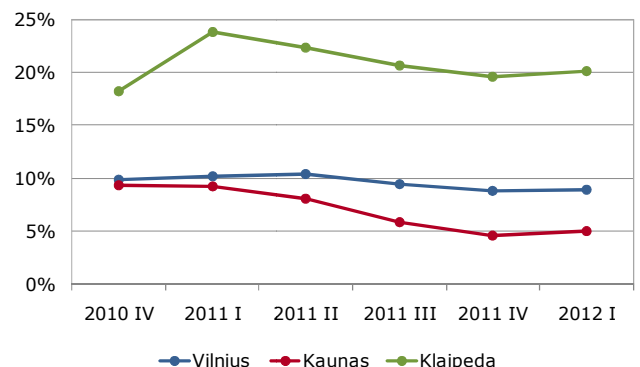
Modern office rents (EUR/sqm/month, without VAT)



Source: Ober-Haus

Data: Q1 2012

Modern office vacancy rate



Source: Ober-Haus

Data: 2010- 2012

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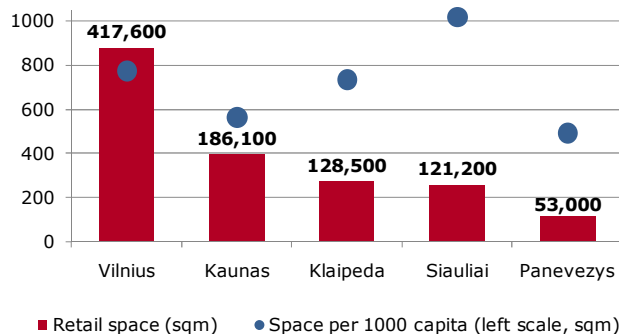
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From the theoretical perspective if these business centres are 50% occupied on the day they open (this would be an optimistic outcome given the current supply and demand), the overall vacancy rate of office space in Vilnius would increase from 8.9% to 11.6% and total area of vacant office space at the end of 2012 would be 56,300 sqm. In the event of such noticeable changes in the modern office premises market, landlords would be forced to compete not only with respect to the quality of the premises and ancillary services, but also with respect to their rents.

Particularly strong competition is expected among B class business centres in Vilnius, where the vacancy rate in Q1 2012 was 10.5%, while in A class business centres this rate was significantly lower with a figure of 6.4%. Considering the fact that two-thirds of the office space currently under construction consists of B class premises, as mentioned above, competition will be even stronger in this segment during the year. However, owners of A class office premises should not be complacent, as construction of Lithuania's largest business centre Quadrum is planned for the right bank of the River Neris. Schage, the Norwegian developer of this centre with a total area of over 70,000 sqm, plans to fill the shortage of A class office space in Vilnius by offering up to 40,000 sqm of top class space with BREEAM certification (one of the most famous standards for environmental performance of buildings) in the new Vilnius business district. Market participants should pay particular attention to the demolition of old buildings and the construction of new buildings in their place. The object of such scope and class (if it is developed all at once rather than in stages) not only leaves no room for new projects in the near future, but also becomes the biggest competitor for other buildings of the same class, forcing owners to make concessions to existing tenants in order to keep them.

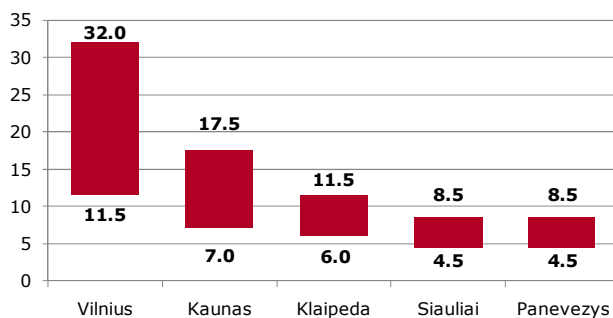
The situation is different in the modern office sector in the other major Lithuanian cities. In Klaipėda, modern office space vacancy at the end of Q1 2012 was as high as 20.1%. It is unlikely that there will be any significant developments in this sector in the near future. In Kaunas, the vacancy rate is lower than in Vilnius and Klaipėda, with a rate of 5.0%, while the total area of vacant space is only 3,500 sqm. With such little supply, larger companies find it almost impossible to find suitable premises. It comes as no surprise that an office building is being built next to the Mega shopping centre by Senukai to provide office space for its administrative staff. Meanwhile, the British company Callcredit Information Group has leased 2,000 sqm of newly built facilities at Žalgiris Arena for its information technology centre. The recently opened financial services centre of the Danish company Nielsen & Nielsen Holding A/S plans to employ about 40 highly skilled finance and accounting professionals. It would seem that Kaunas has not been considered seriously by those developers who are capable of directing investment to this city, but who are restrained from their more active development plans due to rising construction costs and the low level of rents.

Shopping centre stock
(over 5,000 sqm GLA and over 10 tenants)



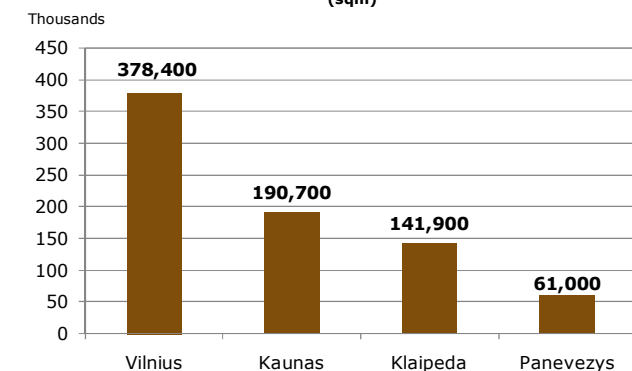
Source: Ober-Haus Data: Q1 2012

Main retail streets rents
(for 100 - 300 sqm, EUR/sqm/month, without VAT)



Source: Ober-Haus Data: Q1 2012

Modern warehouse stock
(sqm)



Source: Ober-Haus Data: Q1 2012

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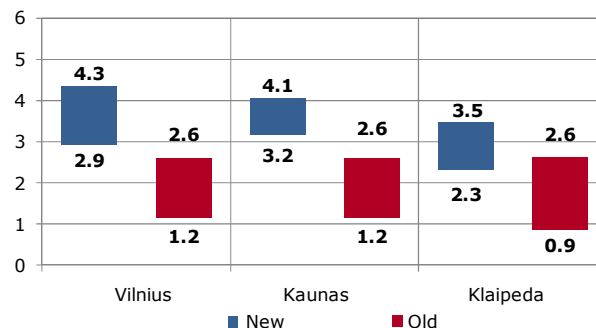
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After slight increase in rents in 2011, no major changes have been recorded in Q1 2012. Prices remain the same as at the end of 2011: **11.0–13.9 EUR/sqm** for A class and **7.0–10.4 EUR/sqm** for B class office premises in Vilnius. In Kaunas and Klaipėda, rents are **6.4–11.0 EUR/sqm** for A class and **3.5–6.4 EUR/sqm** for B class premises. Rents for offices in Kaunas and Klaipėda are at an all-time low with few or no new projects planned, it is unlikely that this year will see any major changes in the prices in any of the cities.

On the other hand, Vilnius, the leader both in the terms of prices and supply, may face temporary difficulties at the end of this year, when the newly-opened business centres will flood the market. To put it in the context of other countries in Europe, the current modern office vacancy rate (8.9%) in Vilnius is not bad. For example, at the end of 2011, the figure for the office vacancy rate in Europe (24 cities) was 9.9%, but if we take only Central and Eastern Europe (10 cities) this indicator stood at 15.0%.

The 10% office vacancy rate in Europe therefore is quite normal and acceptable considering the overall economic situation in this region. However, it is very likely that with the arrival of the new supply this year, Vilnius will join most of the other European cities, with a vacancy rate in excess of 11-12%. For the vast majority of existing business centres, such change in the vacancy rate will have no significant effect, but the owners of currently developed buildings will face the biggest challenge: they will have to decide how to attract tenants and how to realise the projects they develop. In turn, tenants will be able to enjoy even greater choice and more attractive rents over the course of the year.

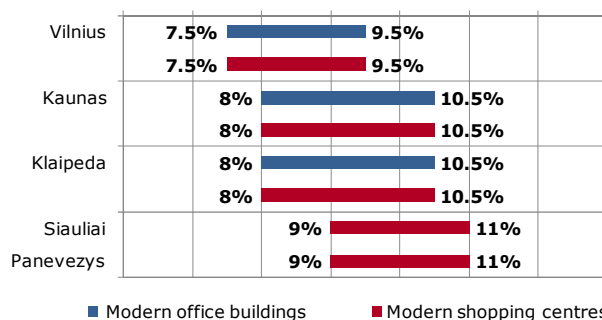
Warehouse rents
(EUR/sqm/month, without VAT)



Source: Ober-Haus

Data: Q1 2012

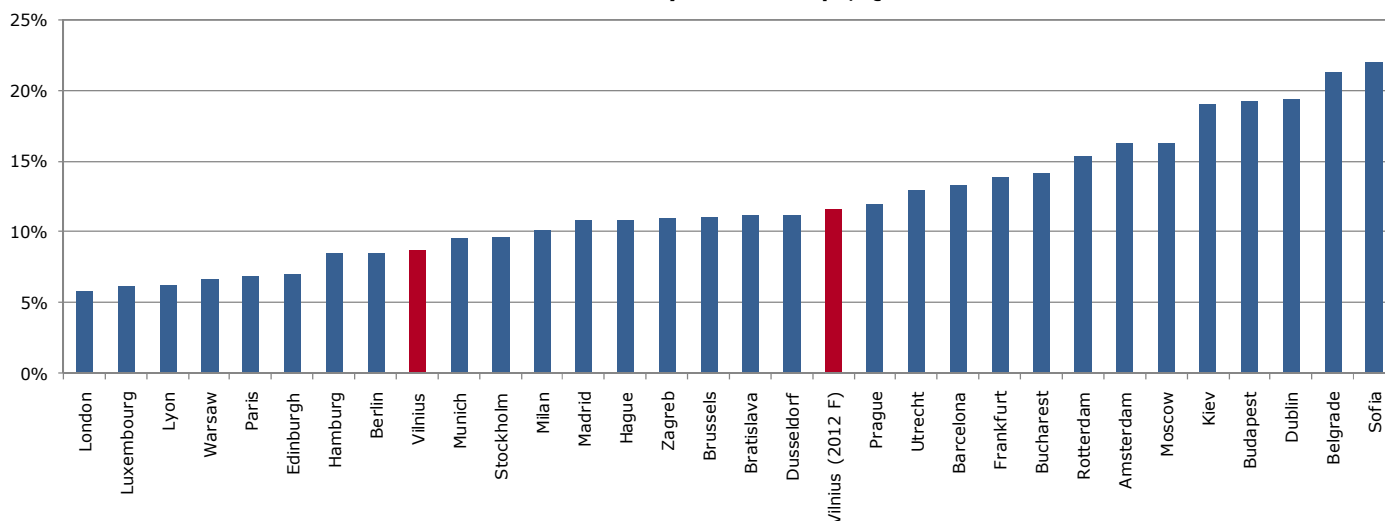
Commercial property yields



Source: Ober-Haus

Data: Q1 2012

Modern office vacancy rate in Europe, Q4 2011



Source: Ober-Haus, Jones Lang LaSalle, CBRE

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 and Poland; 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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