

After full year 2007 Moscow construction inflation of 26.14% for Class A fit-out projects and 21.22% for base build construction, first quarter numbers indicate that 2008 promises a slight slowdown in the rate of increase.

While the London market slows in terms of labour costs and demand-related price inflation, Moscow and Kiev markets continue to see real price pressure in the new-build and fit-out sectors. Leading the rises in overall costs are materials, led in particular by cement, but closely followed by manufactured goods. Raw material price increases affecting metals and oil-based products are pushing prices ever higher, with little hope of relief during 2008, despite the rate of growth slowing over the past two quarters.

Demand-based price inflation is mainly evident in the services – particularly the fees of international architects and engineers – reflecting the buoyancy at least of the Moscow and Kiev markets. As local vendors focus on the demands of international and demanding new local clients we expect to see these increases reflected in domestic service provision too.

London prices over the first quarter, excepting the price increases of raw materials, proved roughly stable – with fears for the health of the sector leading service providers to dig-in, focusing on client retention rather than growth in one of the worst bear markets for many years in our sector.

Notable also is the increase in construction labour costs in Kiev which outstrip Moscow in the first quarter. This can partially be put down to the shortage of skilled construction labour in that market and the comparative influx into the Moscow market over the same period of labourers from surrounding republics, including the Ukraine.

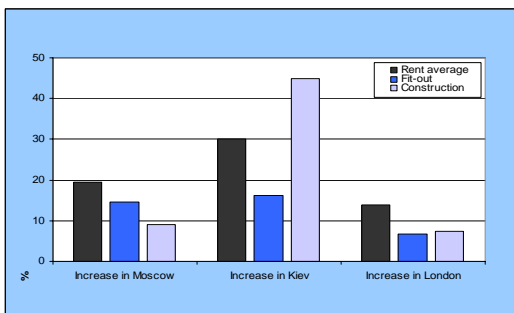
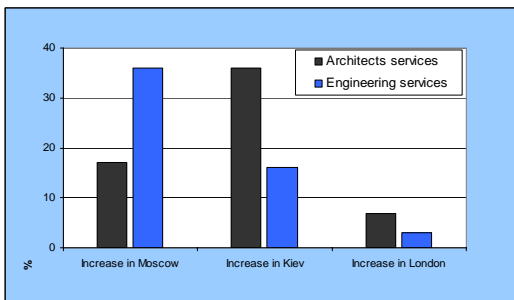
The fit-out numbers relate both to Class A and Class B completion work.

The current fit-out inflation rate in Moscow, for the first quarter of 2008 is running at an annualised 14.58%, against 16.26% for Kiev and 6.7% for London. Base-build construction shows the same trend, with annualised inflation rates, based on first quarter figures, of 9%, 45% and 7.3% respectively. While the fit-out market average total cost depends largely on the business sector of the tenant, with financial services leading the pack, the average Class A fit-out cost in Moscow has now for the first time breached the \$1000/m<sup>2</sup> faultline, reaching \$1035/m<sup>2</sup>, with Kiev at \$731/m<sup>2</sup> and London at \$898/m<sup>2</sup>. Kiev and Moscow prices were also affected over the first quarter of 2008 by the weakness of the US currency.

Our predictions for the remainder of 2008 are that fit-out costs in the Russian market will exceed \$1200/m<sup>2</sup> for Class A tenants, with figures of \$860/m<sup>2</sup> for Kiev and London marking a modest increase to \$960/m<sup>2</sup> based on material price increases.

Key Fit-out Construction Materials	Increase in Moscow, %	Increase in Kiev, %	Increase in London, %
Raised floor	4.7	14.7	6.7
Carpet	4.3	20.7	3.1
Cement	44.2	71.4	30.4
Ceramic tiles	15.7	2.2	4.9
Double layers gypsum board partitions with insulation	15.2	3.6	6.8
Aluminium framed double glazed partitions	22.5	17.4	9.9
Double leaf wood door	14.3	7.7	5.2
Suspended ceiling	8.0	8.5	3.0
Lights Lighting Technologies	12.4	4.2	7.8
Floor boxes	1.4	3.1	6.1
<b>Average Increase</b>	<b>14.3</b>	<b>15.3</b>	<b>8.4</b>

General Contractor Fit-out Works Description	Increase in Moscow, %	Increase in Kiev, %	Increase in London, %
Installation of raised floor	29.7	14.7	3.1
Installation of carpet tiles	9.6	14.7	2.6
Installation of ceramic tiles	5.3	11.1	4.3
Installation of double layers gypsum board partitions with insulation	11.6	45.9	6.1
Installation of glazed partitions	34.2	15.0	7.0
Surface preparation and painting	13.1	15.5	3.5
Installation of suspended ceiling Armstrong	9.6	20.0	3.3
Installation of lighting fixtures	9.4	11.1	3.6
Installation of floor boxes	11.9	14.7	3.1
Installation of sockets	15.1	14.7	4.4
<b>Average Increase</b>	<b>15.0</b>	<b>17.7</b>	<b>4.1</b>



The relative paucity in the Moscow market of quality engineering design companies compared to architectural practices was reflected in large demand-led first quarter increases in the cost of those services in Moscow. In Kiev we found the reverse to be the case, as the large number of mooted projects going through concept design kept demand, and therefore the fees, of locally experienced architects rising sharply. We expect this difference to level off as many of the proposed large-scale Kiev developments fall off the radar and those that continue move into scheme design and beyond.

An interesting feature of Q1 concerns the relatively modest increase in Moscow of new bid base build construction, especially given the material and labour cost increases that feed this metric. It has been widely speculated that the slowdown in Moscow base build cost rate of increase is a direct consequence of the sheer number of new build contractors on the market and the relative slowdown in mooted projects averaged out across industrial, commercial and residential sectors. We remain unconvinced and will be watching this number for growth in the coming half year.

*London is included for the first time in this regional bulletin purely for purposes of comparison. All figures relate to annualized percentage increases in the specified market segments during the first quarter of 2008. All figures are based on vendor quotations received from a mix of international and local vendors during this time period for completion during 2008. We have not discounted contractor hedging for this time period. All figures relate to contractor bid prices, not manufacturers list prices, and therefore represent the real end-user cost. Due to currency volatility, Sunbury Heights is changing the tracking currency for its European cost bulletins to Euros with effect from August 2008.*