

Chinese investments in Russian real estate Clear solutions for complex projects



September 2014



Market overview

China and Russia are one of the largest world economies, neighbors, and strategic partners

China and Russia, general facts

	 Russia	% of world	 China	% of world
Population, mln	146	2.0	1,360	18.7
GDP*, USD bln	2,093	2.8	9,468	12.8
GDP* per capita, USD bln	14,685		7,013	
Real GDP growth 2009-13, %	1.0		8.8	
Land area, mln sq. km	17.1	11.5	9.6	6.4

* market exchange rates

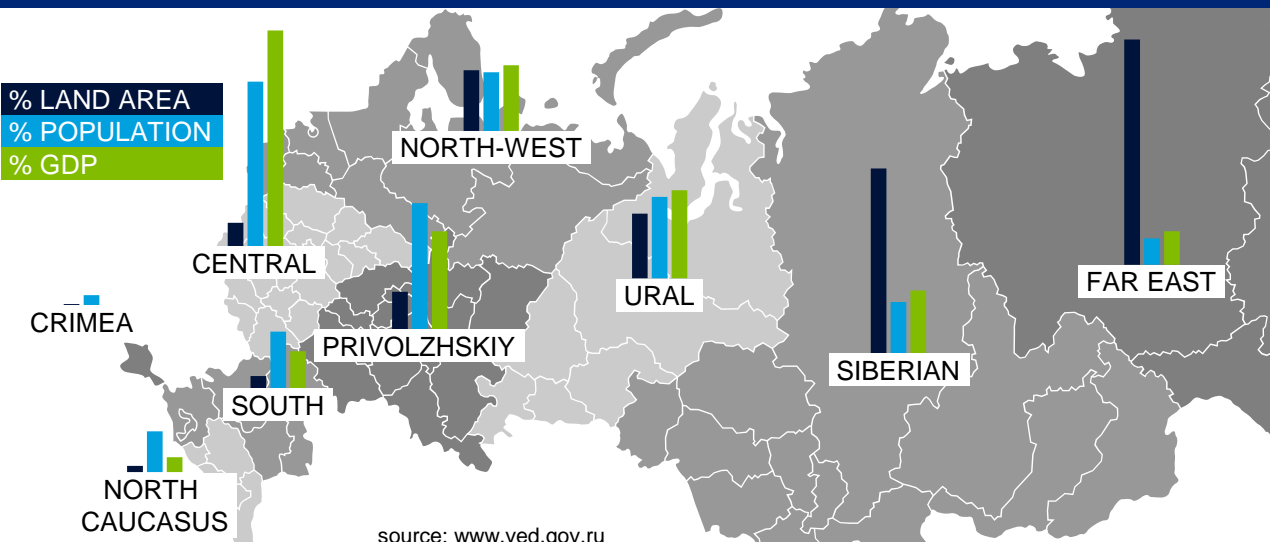
source: EIU

Russia-China trade and investments



China is the 2nd largest Russian export market (6.8% of export) and the number one supplier (16% of total import)

In May, 2014 the leaders of Russia and China agreed to set up an Investment Cooperation Commission consisting of high-profile representatives of public and private companies



Investment project	Industry	Investments, bln USD	Period	Participants
the Power of Siberia a unified gas transmission system	oil & gas	400	2013-2017 (1st stage)	Gazprom, CNPC
Huadian Teninskaya power station	energy	0.6	2013-2016	THK-2, China Huadian Corporation, ICBC
wide-body 400-seat passenger airliner	aviation	7.5	2015-2023	UAK, COMAC
ESPO pipeline	oil & gas	25	2006-2012	Rosneft, Transneft, China Development Bank

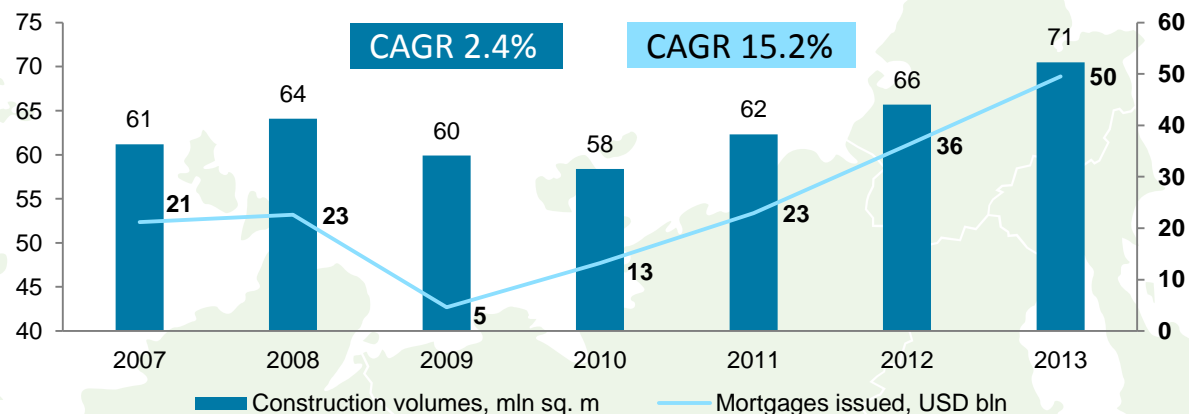
Residential construction is the biggest and most appealing real estate sector in Russia

Basic indicators of residential market

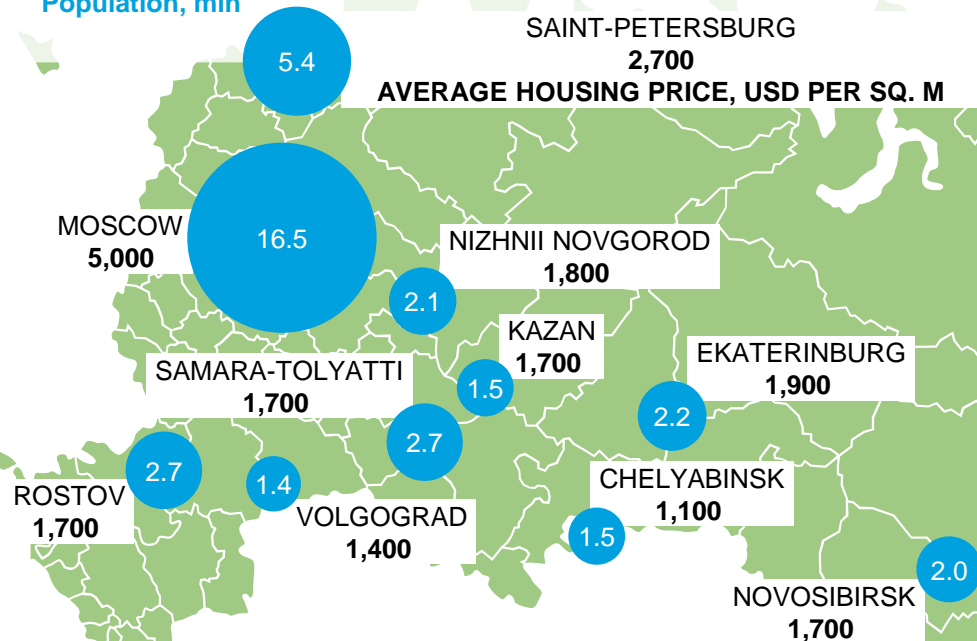
Housing stock, mln sq. m	3,400
Housing stock per head, sq. m	23
Housing stock built before 1970, %	50%

source: www.rbc.ru, www.gks.ru

Construction and mortgage volumes



Population, mln

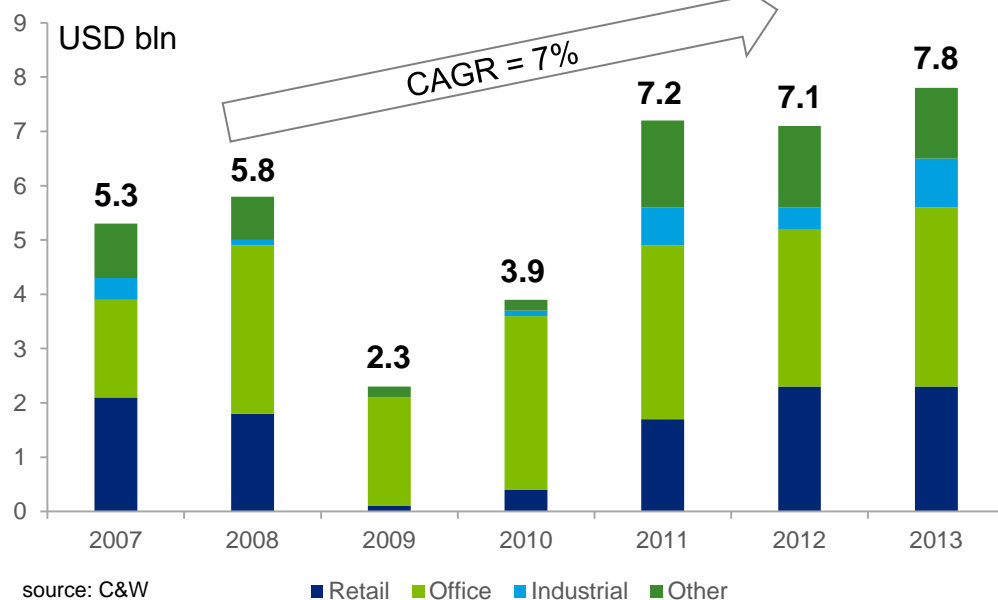


source: irn.ru, bn.ru

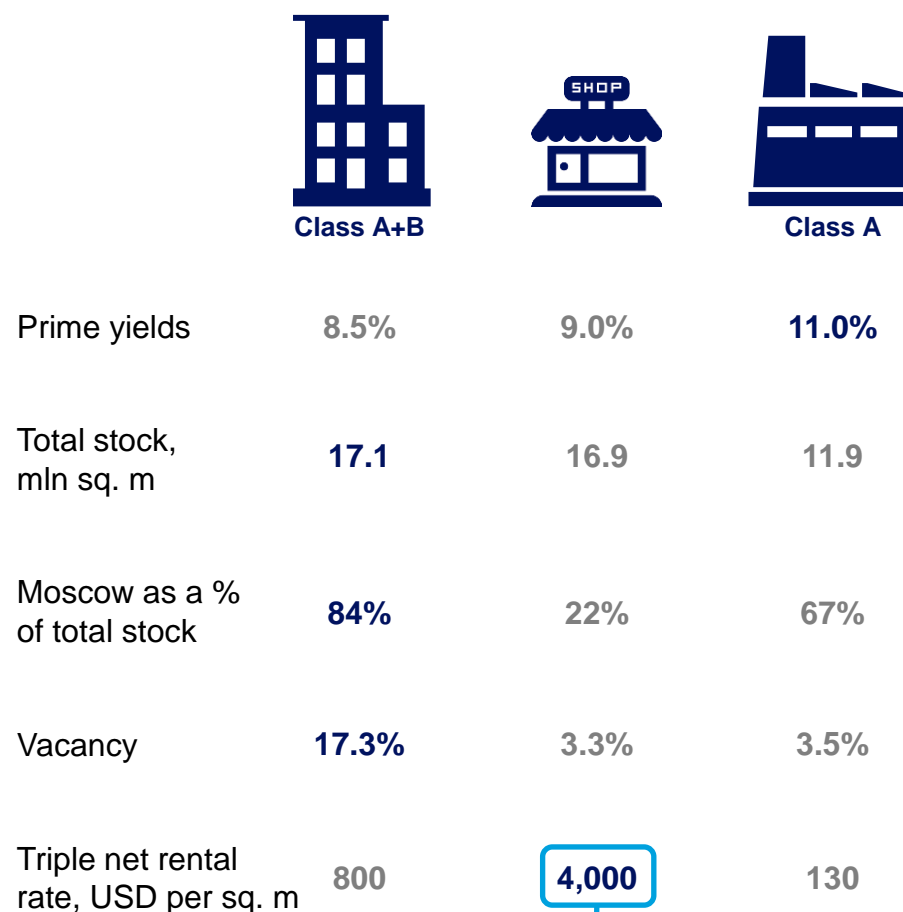
Investment project	Investments, bln USD	Period	Participants
Baltic Pearl, Saint-Petersburg (GBA 1.8 mln sq. m)	4.0	2005-2016	SII Co, Government of Saint-Petersburg
Satellite town "Yuzhniy", Saint-Petersburg (GBA 4.3 mln sq. m)	4.9	2012-2031	Dalian Wanda Group, Start Development
Housing units in Krasnodar (GBA 0.4 mln sq. m)	0.3	2015-2018	CMII, Industrial Techno-Park Kuban
Housing units in Khabarovsk (GBA 1.5 mln sq. m)	2.5	2014-2018	CSCEC, Government of Khabarovsk

Commercial segment attracts billions of dollars from local and foreign investors, Moscow takes the lead

Total investments by sector



Major commercial real estate indicators



Investment project	Investments, bln USD	Period	Participants
Park Huaming - mixed-use development with GBA of more than 200,000 sq. m located North-West Moscow	0.8	2014-2018	Russian-Chinese Center for trade and economic cooperation
Greenwood office and retail center with GBA of 130,000 sq. m located in Putilkovo, Moscow Region	0.4	2010-2011	Chengtun Group Cooperation, Government of Moscow

Prime retail indicator—base asking rental rate for a 100-200 sq. m gallery unit on the ground floor of prime shopping centers

Our service offerings to Chinese
investors in real estate

Tax and legal

Preliminary stage: formation and acquisition

Problem: Which form of entity to choose when entering Russian real estate market?

- **Response:** Russian legal entity vs. foreign company (with a branch or no presence in Russia), based on the specifics of your business
- **Solution:** Deloitte CIS can carry out an entity choice analysis and provide you with an expert advice in respect of options most suitable for your business in Russia

Operations services

Problem: How to finance Russian real estate business? What would the tax impact be?

- **Response:** Various options are available. Each of them has its own tax implications that under certain circumstances can adversely affect your business
- **Solution:** Deloitte CIS offers services in designing tax efficient financing structures tailored to real estate projects in Russia. In doing so, we always provide a comprehensive advice on how to minimize potential tax implications and risks

Problem: Which taxes are applicable to business operations involving Russian real estate?

- **Response:** Depending on various factors, your business activities may be subject to Russian profit tax, VAT, property tax and land tax
- **Solution:** Deloitte CIS will identify tax saving opportunities for your business (e.g. tax effective structuring of business operations, application of government tax incentives) and explain whether and how you can take advantage of them.

Problem: How difficult is it to transfer employees from China to Russia and structure payments of their salary? Which problems are expected?

- **Response:** Russian legislation in this area is quite complex. You are most likely to deal with at least labor and civil law issues, immigration regulations, tax aspects of employing foreign individuals
- **Solution:** Deloitte CIS has an extensive expertise in dealing with foreign employees. We can provide you with a comprehensive legal and tax advice which would cover, among others, issues such as visas and work permits, structuring of cost recharges and salary payments

Disposition of assets and exit strategies

Problem: What are the most tax effective ways to repatriate Russian earnings back to China? How to exit from Russia in a tax efficient manner upon project completion?

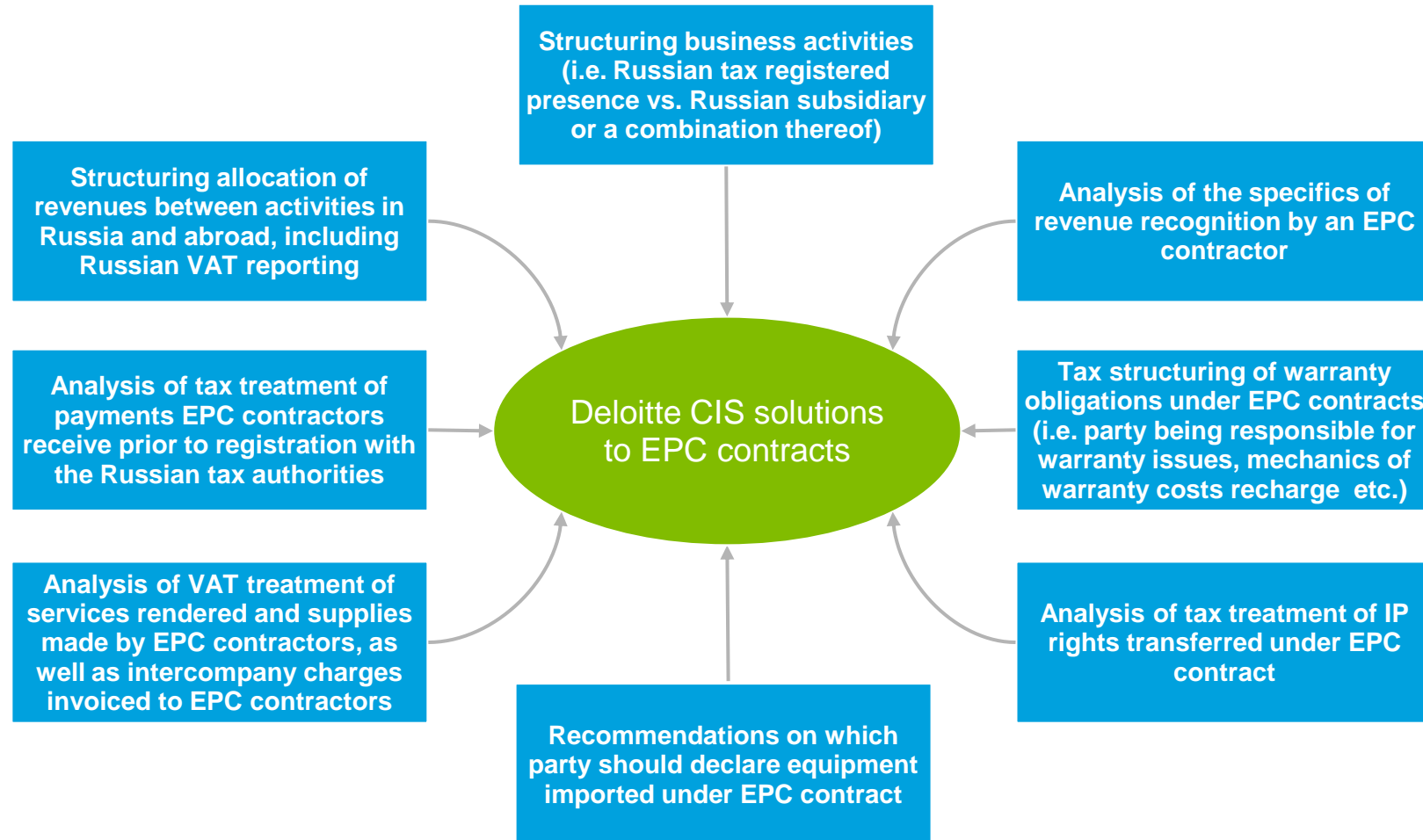
- **Response:** This would depend on the ownership structure of your business, which should be properly designed to minimize the tax impact. Many factors have to be considered and no universal way exists.
- **Solution:** Deloitte CIS offers services in designing tax efficient ownership structures tailored to business activities and client preferences. In doing so, we carry out an in-depth analysis of various tax factors and risks and present to the clients personalized solutions that in many cases are unique

Other services

- Tax compliance for federal, regional and local tax returns
- Assistance in preparation of financial statements
- Structuring of corporate mergers and acquisitions
- Application of special vehicles provided by Russian legislation (e.g. real estate investment trusts etc.)
- Support during tax audits and litigations with the tax authorities

Tax and legal

Engineering, procurement and construction (EPC) contracts



Financial advisory

Transaction Support

Our **Real Estate Transaction Support team** carries out due diligence in reviewing target companies trading performance, cash flows, debt structures, and major contracts. As the Russian market evolves, sale and purchase agreements are becoming more sophisticated, with increasing use of “completion accounts” mechanisms. We can assist with SPA drafting and review completion accounts to help you achieve maximum value from the transaction

Problem: *What sources of financial information prepared by the Russian real estate companies are appropriate to look when considering an investment?*

- **Response:** Statutory accounts prepared under the Russian Accounting Principles do not often reflect fair financial performance and financial position of the Target due to not recorded or incorrectly recorded transactions (such as transactions with related parties, tax optimization schemes, service, management, facilitation and other similar transactions)
- **Solution:** Deloitte CIS can prepare an adjusted pro-forma of financial statements reflecting fair (“IFRS-like”) financial performance and financial position of the Target

Problem: *Which unrecorded liabilities may exist in Russian companies operating in real estate business?*

- **Response:** Russian real estate companies generally have significant contingent and other unrecorded liabilities (e.g. commitments to construct and infrastructure items for local authorities free of charge, “golden parachutes”, committed CAPEX, long-term lease liabilities generally unrecorded in RAS, contracts retention, litigations, etc.)

Solution: Deloitte CIS can identify all potential unrecorded liabilities and estimate actual amount of the Target’s net debt

Problem: *How can financial risks be covered in the Sale Purchase Agreement?*

- **Response:** This can be reached via appropriate pricing mechanism, sufficient warranties and indemnities, explicit description of completion statement and completion price adjustments
- **Solution:** Deloitte CIS provides full SPA support from a financial point of view. Together with you and your legal advisors we will work out the most appropriate financial terms and formulas, participate in negotiations with the seller and check of completion statement

Real Estate Valuation

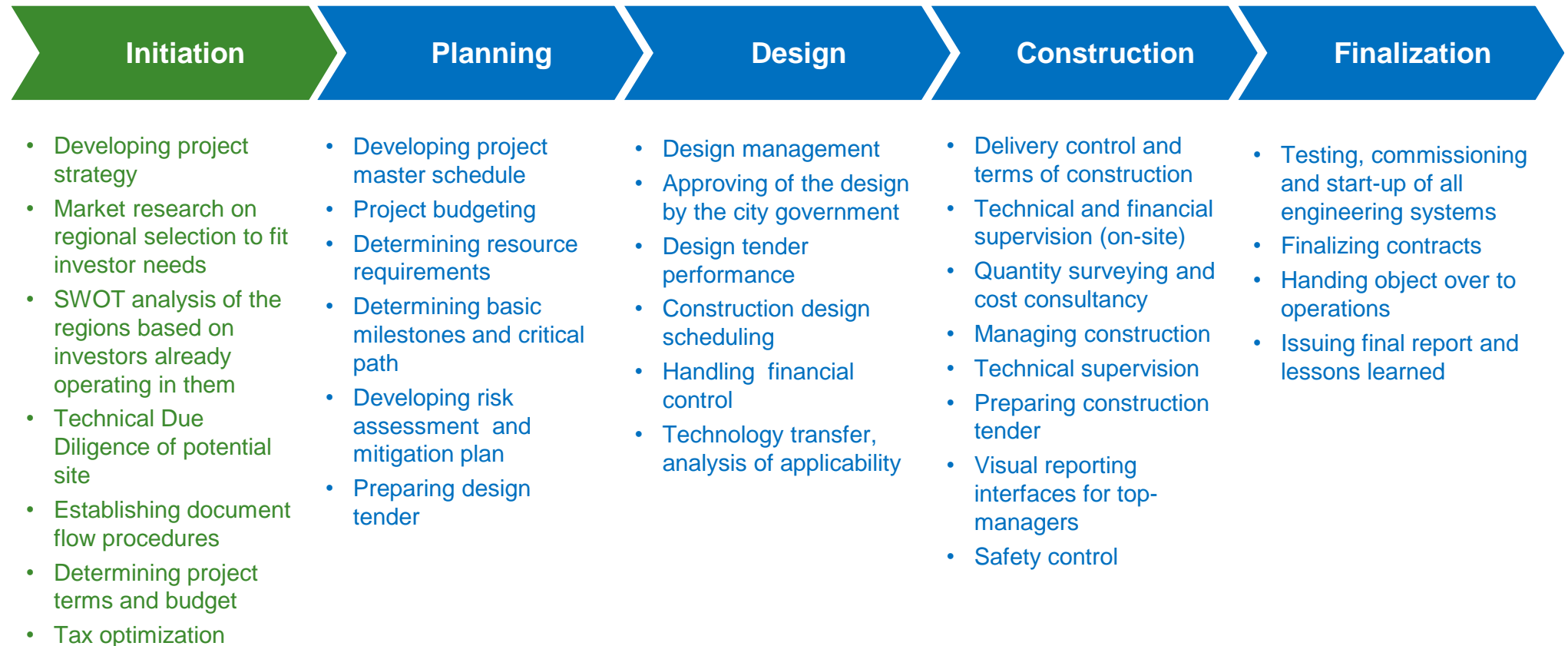
Our **Real Estate Valuation team** covers a full spectrum of real estate valuation services, ranging from evaluating large and diverse portfolios to performing single property analyses. In addition, our team is proficient in preparation of feasibility studies and investment memorandums, highest and best use analysis, financial modeling, location analysis and market research

Key advantages that differentiate us from other services providers are:

- An in-depth understanding of the market and unique professional background
- A comprehensive set of financial modeling tools for development projects and operating properties
- Long-standing relations with major financial institutions that help ensure effective communication in the fund raising process

Construction group

Deloitte Construction Group is a team of top engineers and experts with extensive experience in construction of real estate and infrastructure projects. Our engineers use best world practices and methods to prevent delays in construction schedule and budget overruns



Our priority and objective are to minimize the risks to our clients on all steps in construction projects

Why Deloitte?

Why Deloitte?

Our industry specialization: tailored solutions to comprehensive problems

Our task is not to prepare a standard product, but rather to provide real support to our clients. We implement the projects together with the clients.

Deloitte CIS has extensive experience in providing different kinds of services to companies in the real estate industry.

Deloitte CIS has accumulated a wealth of experience in providing audit, tax, consulting and legal services to real estate and construction companies in Russia and abroad

As the provision of services to real estate and construction companies is one of our strategic priorities, we have created a group of specialists which focuses on providing quality and tailored solutions to companies operating in the industry

The group consists of highly qualified experts with a long-standing real estate experience in different kinds of real estate engagements, including, but not limited to, the below

Examples of what we can do:

- ✓ M&A transaction services
- ✓ Audit and assurance services
- ✓ Financial statements and internal control audits
- ✓ Financial accounting and reporting advisory
- ✓ Accounting support
- ✓ Legal support in real estate transactions
- ✓ Valuation services (Federal Valuation Standards, IVS, RICS)
- ✓ Forensic services (risk assessment, identification of fraudulent actions)
- ✓ Transition sourcing, advisory and due diligence
- ✓ Capital raising and capital market strategies
- ✓ Finance transformation
- ✓ Investment advisory
- ✓ Targeted market research
- ✓ Highest and best use analysis
- ✓ Taxation – international, domestic, regional
- ✓ Tax structuring, optimization and modeling
- ✓ Tax opinions
- ✓ Diagnosis of tax risks
- ✓ Ongoing tax consulting
- ✓ Analysis of special investment structures
- ✓ Express analysis of property portfolio
- ✓ Integration and restructuring
- ✓ IT systems strategy, selection and implementation
- ✓ Feasibility studies



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