Bulgaria
Market Report 2010

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Dear Readers

We are pleased to introduce our first Bulgarian Real Estate Market Report, covering the office, retail, industrial and residential sectors

The past 12 months have certainly been a testing time for the Bulgarian market. We have witnessed a huge amount of new office stock brought to the Sofia market, whilst the retail market has suffered from a slowdown in leasing that has led to a number of projects in the key regional cities freezing construction.

That said, the industrial market is still under-supplied and we are also starting to witness stability and even some positive movement in values within the residential sector.

In terms of the investment market, 2009 was extremely quiet but we do expect to see things start moving in 2010. There is liquidity in the market and a number of funds have already announced large amounts of capital destined for South Eastern Europe.

On a more corporate note, 2009 was our first year in the Bulgarian market and we hope that 2010 will bring us even more success. We have already formed close ties with a number of key clients and we hope to expand on these in the years to come

We hope that you find this report useful and we look forward to working with you throughout 2010

Yours faithfully

Andrew Peirson

Executive summary

- During 2004–08, Bulgaria enjoyed a period of rapid economic growth guided by strong foreign international investment and buoyed by a vibrant export sector.
- Bulgaria became a full member of the EU in 2007 which further increased international interest and investment into the country.
- There was a delayed reaction to the global economic crisis but 2009 brought an end to years of positive growth, and the real estate market was hit hard.
- Many developments which were in the pipeline have been stopped or cancelled altogether. This is not solely due to the fall-out of the financial crisis, but also due to the realisation of an oversupply in a number of areas within Bulgaria
- Foreign Investment funds are still active, and although 2009 was a very quiet year on the investment front, we expect to see more activity in 2010.

Office market

- The total stock in Sofia reached 950,000 m2, with more than 70% located in suburban areas.
- Average vacancy rates reached 15% in Sofia in 2009 as new office buildings have struggled to secure tenants. We expect this to rise to 20% during 2010 due to the completion of a number of new schemes.
- New developments in Sofia are quoting between 13 – 16 EUR/m². In central Sofia the prime rents have stabilised at around 20 EUR/m².
- The regional office market is still at very early stages, with only Varna realising any good quality projects. Ruse will have its first business park by the end of 2010. The market in the regions is limited to mainly domestic occupiers with very few international occupiers looking beyond Sofia.
- The out of town market in Sofia is currently suffering from over-supply. Adversely, there is still an undersupply of international quality Grade A space within the city centre which is keeping prime rents high.
- The majority of the new developments are concentrated on the main boulevards of Sofia and the ring road. This trend is driven by the lack of (and the cost of) suitable land plots for large office projects in the CBD and Broad Center area.
- The market is generally witnessing an improvement in quality of new build schemes and the majority of activity is from tenants moving from older buildings to new speculative schemes.

Business Park, Sofia

Retail market

- Over recent years the Bulgarian retail market has been transformed and now most major towns and cities have some form of modern retail provision.
- Sofia has the largest retail offering with nearly 80,000m² of lettable area currently and over another 100,000m² to be completed in 2010.
- Whilst Sofia has managed to sustain good levels of performance the regional cities have generally suffered from over-development.
- Rents regionally are lower than the achieved rents in Sofia with new schemes expected to achieve an average weighted rents of between €16-18 m², while in Sofia they are still as high as €23 m².

- Many developments, in both Sofia and the regions, have been frozen or cancelled altogether. This a mixture of the levels of supply now in the market and the lack of financing now available to developers.

- The investment market is quiet and we did not witness an open market retail investment deal in 2009, despite a number of existing malls being openly marketed. We expect a similar story in 2010.

Hermes Park

Industrial market

- Rents have continued to fall across Bulgaria with a fall of 15% over the last year. Rents in Sofia however are largely unchanged with prime rents of €5.5 m² still being achieved.

- Very little speculative development occured in 2009 and we again do not see a different story in 2010. Developers looking for pre-leasing before committing to build out

- Market dominated by build to suit owner-occupied development. The majority of the supermarket operators have now developed their own build-to-suit facilities, and there is very little institutional stock available to the investment market

- There are key infrastructure improvements to be made before Bulgaria can establish itself as a logistics hub. This is possible given its strategic location between Turkey and Greece and the rest of Europe.

Residential market

- The supply of residential stock has slowed over 2009, with many projects planned or under construction now being on hold.

- Currently the market is seeing a slight uplift in the demand for residential property on a freehold basis, with new mortgages for Bulgarian nationals becoming more accessible.

- The coastal and ski resorts have been particularly affected and sale prices have fallen dramatically over the past 12 months. Mortgages in such locations are almost impossible to obtain and as such the market is only accessible to cash buyers

- The Sofia residential market has also experienced a downturn particularly in low cost housing. There is still however an under-supply of high end products for families and high net worth individuals, and we see this as a potential growth market in 2010

- We expect to see the market in 2010 being domestically driven with very little foreign investment expected.

- Historically the British & Irish investors have been the main target buyers but they have now all but disappeared. What little foreign investment that does exist comes through Russia, Ukraine and nearby Greece and Romania.

Office market

Sofia

History

For years, the Sofia office market has witnessed poor quality development, but offices where build quality is of a higher standard have generally performed well. The Business Park Sofia scheme is a good example. The first, and currently only, business park in Sofia, BPS has successfully attracted international companies who have been drawn to the amenities on site and the standard of buildings that were, at the time, better than what was being developed elsewhere, and more in line with requirements.

Individual buildings such as East Park Trade Centre, Iztok Tower, Europark and the Landmark Centre in the city centre have also enjoyed success, hence higher rents. Again, such schemes have successfully attracted international tenants due to their standard of building and location.

Areas to the north of the city centre and on arterial routes in the west and south have witnessed an over-supply of poorly located and specified office schemes that have skewed the vacancy rate somewhat through their inability to attract tenants.

In terms of take-up, today's figures are higher than five years ago but the 75,000 m^2 transacted in 2009 is a reduction from the heights of 2007 and 2008 when record levels of above 125,000 m^2 was done.

The Current Situation

Sofia has around 950,000m^2 of office stock, although this comprises varying degrees of quality. Included in this figure are older buildings which are simply not in a state to be re-let. Therefore, modern office stock, i.e. offices completed within the last 10 years, is nearer 500,000m^2.

The office market in the capital suffers from a level of over-development following several years of poor quality development that has led to an increase in the vacancy rate for the city. Added to this the negative effects brought on by the financial crisis, there is increasing downward pressure on rents, and pressure on landlords to find ways to be more flexible in order to secure tenants.

In particular, the out-of-town office market continues to suffer from a high level of vacancy and a low level of activity, while the city centre and its periphery remains under-developed and demand for good quality accommodation is relatively high.

The majority of development is currently occurring along Tsarigradsko Shosse. This arterial route in and out of Sofia leads to the Trakia highway and provides direct access to the city centre, easy access to Sofia Airport and is close to major residential hubs, while also benefiting now and will continue to do so in the future from the metro extensions and retail developments that improve local amenities. The majority of current development is of a higher standard than has been developed in the past, and although most schemes are still largely vacant there is hope that the market will absorb this over the next 12-18 months.

The area around Tsarigradsko Shosse is quickly becoming the prime out-of-town office location, a shift away from the east of the city along the ring road near to Mladost, where development had been focussed. The main schemes completed or under construction on and around Tsarigradsko Shosse are shown in the table below:

Office schemes around Tsarigradsko Shosse

Scheme	Developer	Size (m^2)	Completion
Benchmark Business Centre	Benchmark	17,000	Completed Q1 2010
Iztok Tower	Landmark	13,000	Completed Q3 2009
Ellipse Centre	Ilpa	10,000	Estimated Q2 2011
European Trade Centre	ETC	73,000	Q2 2010
Mega Park	Soravia Group	50,000	Q3 2010
Polygraphia Centre	BLD/Northridge	15,500	Q3 2010
'Captain Ford' Business Centre	Fort Knox/Variant Sofia	75,000	2012

European Trade Centre

The area around Sofia Airport has also been the focus of large scale land buying in the past, and a host of speculative developments are now appearing. The most notable of these is the American developer Tishman's 'Sofia Airport Centre', a truly Class A office park development that also incorporates high quality logistics space. Other existing schemes and those under construction around the airport are shown in the table below.

Sofia Airport Centre

The Tsarigradsko Shosse area is not the only major arterial route in and out of the city centre to continue to witness office development. Main roads such as Boulevard Bulgaria, Cherni Vrah and Todor Aleksandrov have also proved attractive to developers for the siting of new office buildings. The schemes on Bulgaria Boulevard are generally of a better quality and have successfully attracted the likes of KPMG, ING Bank, Hypo Bank and First Investment Bank. Pro Credit Bank has recently moved into a build-to-suit headquarter building on Todor Aleksandov Boulevard, which is also the home to LukOil's Bulgarian headquarters.

Despite new development taking place in out of town locations, Sofia's city centre is still largely under-developed. Problems with the cost and ownership of land, along with planning restrictions meant developers have focussed their attention elsewhere. What little development land exists is invariably purchased for hotel or retail/leisure development. This has led to high levels of unsatisfied demand from city centre occupiers for good quality office space, with several companies having had to relocate out of the city centre in order satisfy their requirements.

There are a number of developments currently coming out of the ground that should help satisfy the pent up demand in the centre of Sofia and attract companies back to this area. The most notable of these is GEK Terna's 'City Tower' scheme on Macedonia Square. At over 34,000m² this building represents the largest ever city centre office development in the capital, and early demand has led the developer to speculatively start construction in a difficult financial period. Completion of City Tower is scheduled for 2012. Perform Business Centre will also be completed in mid 2010 and will bring a further 16,000m² to the market. Immorent is currently developing over 30,000m² above the Serdika shopping mall scheme on the western periphery of the city centre. Although not centrally located, the scheme represents the closest thing there is to an international standard central office building that is to be finished during 2010.

Key office schemes close to Sofia Airport

Scheme	Developer	Size (m²)	Completion
Auto Union Centre	Landmark	9,400	2007
Porsche Building	Orchid	8,000	2007
Sofia Airport Centre	Tishman/GE	1st Phase 17,300	Q2 2010
Brussels Centre	IHM	12,000	2011
Astral Business Centre	ATRSAL	13,500	2011

Key city centre office schemes			
Scheme	**Developer**	**Size (m²)**	**Completion**
Landmark Centre	Soravia Group	6,300	2003
Mall of Sofia	RESB	10,400 (above mall)	2006
Platinum Centre	BP Group	10,000	2007
Perform Business Centre	Limoni/Perform	16,000	Q3 2010
Serdika Centre	Immorent	28,000	Q4 2010
City Tower	GEK Terna	30,200	Q2 2012
Millennium Centre	NIKMI	25,000	TBC

Other office schemes in the pipeline include the Millennium Centre in the southern part of Vitosha Boulevard close to the Ivan Vazov district. This well-located scheme will eventually deliver 25,000m² to the market amongst 110,000m² of hotel and residential accommodation. Completion dates are not yet known, with construction currently on hold.

The table above shows the key office schemes that have recently been completed or are currently under construction in and around the city centre.

City Tower

The future

The future of the office market in Sofia will depend largely on restricting poor quality developments and for international standard buildings to become more widely available. Bulgaria also needs to improve its attractiveness to companies outsourcing jobs abroad.

Following years of poorly designed and located buildings, resulting in downward pressure on rental levels, it is now time for the supply to be more in line with the levels of demand in the market.

In terms of rents, it has been hard to judge true rental levels in the past as they have shifted haphazardly for years. This is a result of tenants not being advised and an immature market attempting to adapt to western levels. Rents are expected to reach a sustainable level, with prime city centre rents settling at around €19-20/m²/month.

Due to the current difficulties in obtaining bank finance for office development the current level of over-supply in the out-of-town market should begin to reduce, and existing vacant buildings see an improvement in vacancy levels. With this reduction, rents should stabilise to a level of between €13–15/m², depending on location.

Public transport will be key. In the major cities across Europe, public transport is of utmost importance, and in the more established CEE cities such as Prague, Budapest and Warsaw there is heavy reliance on the public transport systems, particularly the metro. Despite the poor condition of the roads around Sofia, to date car transport has been the transport mode of choice. It remains to be seen what effect the improved and extended metro system will have on the main office locations across Sofia, and if the areas in areas such as Mladost will witness increased levels of demand as a consequence.

In terms of potential large scales moves, the majority of Government institutions have not relocated for years, remaining in poor quality office buildings in and around the centre. Many of the banks, both Bulgarian and foreign owned, are likewise in traditional central headquarters, and we expect to see both sectors start to relocate out of the centre over the next five years. This should free up space in the centre, while creating higher demand in the out-of-town market.

Many international companies now have a presence in Bulgaria, although this is often simply to cover their domestic operations in Bulgaria.

One of the driving forces for growth in CEE office markets over the last 10 years has been shared service centres, which have yet to become established in Bulgaria. To date, only Hewlett Packard is operating a shared service centre of any notable size, their centre being the largest training centre in the Balkan region.

Despite the favourable tax rates in Bulgaria, the low employment costs and high number of potential graduate employees, Bulgaria rarely features in shortlists of proposed relocations, with countries such as Czech Republic, Poland, Hungary and even nearby Romania being favoured. For the office market to grow, and for take up to increase above existing company relocations and expansions, this must be improved. With the new Government in place and improved inward investment agency, there is hope that international companies will start to view Bulgaria as a favourable location to relocate employment and services.

Mega Park

Retail market

Introduction

Prior to the global economic crisis Bulgaria enjoyed a period of rapid economic growth. This was generated by strong foreign international investment and buoyed by a vibrant export sector. As the economy grew so did GDP and demand for domestic goods rose.

This increase in disposable income and the subsequent increase in demand for domestic goods were serviced by a stark increase in the supply of retail space and is considered by many to be the most dynamic sector of commercial property in Bulgaria.

Developers responded by initiating a large number of new shopping centres and retail warehouse developments. International developers such as ECE, Plaza Centers and GTC have entered the market with significant projects in Sofia and the main regional cities.

The vast majority of the leading retail groups operating in Bulgaria are currently foreign-owned which has led to the local market quickly adopting the characteristics of Western markets. Consolidation in the market has already started and is gaining momentum, with developers and investors also turning to new formats of shopping schemes such as factory outlets and retail warehousing.

Shopping centre development has primarily been the main area of development. Despite the high rents, the high street in Sofia (Vitosha Boulevard) does not attract many of the major international retailers due to poor tenant mix and inefficiency of buildings. The high street instead comprises of a mix of small local retailers and international brands but this has grown organically and as such little planning has gone into the tenant mix.

As a result, the majority of international retailers have entered the Bulgarian market with presence in the shopping centres.

In terms of shopping centre development in Sofia, this commenced in 2006 with the opening of City

Centre Sofia and Mall of Sofia, both located on the periphery of the city centre. Before this, the city centre department store TZUM was redeveloped in 1999 and was the only notable shopping centre development, mainly attracting high end fashion retailers

Mall of Sofia

This trend has continued as a number of shopping centres are under construction or are now currently in the pipeline in Sofia and in all major towns and cities across Bulgaria.

In terms of the regions, Bulgaria has witnessed a number of developments completed over the past 3 years, and there are several projects under construction. The below table illustrates the main purpose built shopping centres which are currently operating in Bulgaria:

Existing shopping centres		
Scheme	**City**	**Size (m^2)**
City Centre Sofia	Sofia	22,500
Mall of Sofia	Sofia	34,500
Mall Varna	Varna	33,000
Bourgas Plaza	Bourgas	27,000
Mall Plovdiv	Plovdiv	22,000
Park Mall	Stara Zagora	20,000

The current situation

The global crisis has certainly had its effect on retail performance in Bulgaria and sales volumes have generally fallen. As a result of this the rate of growth of new retail developments has also significantly slowed as retailers slow down on their expansion plans.

Adversely many of the discount retailers and hypermarkets have increased levels of demand, and the likes of Lidl and Penny Market have increased their land buying, and have now opened stores across Bulgaria, particularly in secondary cities. Carrefour has continued to expand since arriving in Bulgaria in 2008 in Burgas Plaza, Kaufland opened three new stores in 2009 (Bourgas, Stara Zagora and Kyustendil), and the most dynamic food retailer of all was Billa who opened 10 new stores in 2009 alone.

Rental reductions are now commonplace in the majority of shopping centres. With falling turnover retailers are requesting reductions to fall in line with reduced profit levels and as such this is having a negative impact on capital values.

Serdika Centre

The main shopping centres in Sofia appear to have been largely unaffected by such reductions. Here there is still an appetite from expanding retailers and new retailers to the market, and particularly the new retailers to Bulgaria aim to start with a presence in Sofia. Therefore rental levels, although not increased, have remained stable during this difficult period.

In terms of current development pipeline, we will see big changes in the markets in both Sofia and Varna this year. Sofia will see the opening of ECE's Serdika Centre and the Carrefour Tsaridgradsko Mall whilst two new shopping centres are due to open in Varna this year, with a further centre opening in 2011

See the table below for the schemes that are due to complete in 2010.

In terms of rental levels, shopping centre rents that are currently being achieved are on average 20% lower than the levels that were previously witnessed in June 2007. Rents regionally are lower than the achieved rents in Sofia, with new schemes expected to achieve an average weighted rent between depending on the competition within the city in question and the location of the property. There are instances where rents are above such levels but these have been the subject of the rent reductions that landlords have had to deal with.

In terms of retail rents in Sofia, this is generally between €22-24 m^2 in the shopping centres with rents as high as €55 m^2 for units up to 50 m^2 with reductions thereafter for larger units. The high street in Sofia is difficult to quantify, with so many types of tenants, and landlords, making it almost impossible to accurately state a single prime rental range. Rents range from as low as €40 m^2 up to €120 m^2, and much depends on the type of user, its location, and the strategy of the landlord. For a typical unit of between 50 – 100 m^2 in a prime pitch we would assume a prime rent to be around €90 - 100 m^2

The future

In Sofia, vacancy levels are currently low and rents stable. The existing centres are performing well and we expect the two new centres opening in 2010 to also perform strongly. Both Serdika and Tsarigradsko Mall are bringing much needed new operators to the market, with the likes of Peek & Cloppenburg and Zara opening, and this should help their performance and improve the general tenant mix and selection in the city.

Bulgaria Mall

In order for Sofia to continue its impressive retail performance there needs to be a period of saturation and for new development to be slowed. From mid 2010 the city will have four major shopping centres and there remains little room for further development. The eastern and central parts of the city in particular will have no real scope for future development and anything further will only result in oversupply that will lead to rents falling and a lack of confidence from both tenants and investors.

That said, the western part of the city is still under-developed and there is certainly scope for more. This should be met with London Sofia Property developing Bulgaria Mall, a 140,000 m^2 development that includes 33,000 m^2 of retail space which is located on Boulevard Bulgaria. Development should start in 2010 and expected completion date is 2012/2013.

The regional market will be tested in 2010. The main cities of Varna and Plovdiv will see new

Shopping centres due to complete during 2010

Scheme	City	Developer/Investor	Size (m^2)	Completion
Serdika Shopping Centre	Sofia	ECE	58,000	Q2 2010
Carrefour Tsarigradsko Mall	Sofia	ASSOS Capital	66,000	Q3 2010
Grand Mall Varna	Varna	Orchid Development Group	52,000	Q3 2010
Varna Towers	Varna	Densi	52,000	Q3 2010
Mall Rousse	Rousse	RESB	38,500	Q3 2010
Mall Markovo Tepe	Plovdiv	Melina	16,000	Q3 2010
Galeria Plovdiv	Plovdiv	Sienit/Charlemagne	51,000	Q2 2010

centres opening that will put pressure on the existing shopping centres. Varna in particular will see two further shopping centres opening, with Varna Towers and Grand Mall Varna both expected to open their door for trading in the 3rd quarter of 2010. The main existing centres in both cities, namely Mall Varna and Galeria Plovdiv do however have a strong tenant mix, and have actively been managed through 2009, and this must continue through 2010 in order to continue recovery.

Retail Park, Plovdiv

We would not expect any new retail development to occur during 2010 in the regional cities, with construction only occurring on developments that have managed to reach necessary pre-leasing levels for financing to continue. This freeze of development should provide the much needed respite that existing centres and those soon to open will need in order to stabilise rents and to look at improving income and maximise value.

We do expect the discount food retailers to continue their aggressive expansion strategy, particularly in the secondary towns across Bulgaria.

Furthermore 'big box' retail parks that offer lower rents should begin to arrive and will cater for the growing DIY market that so far has been dominated by the large international operators such as Praktiker and Bricolage. Last year Baumax opened in both Bourgas and Sofia and together with smaller home furnishing stores such as Jysk we expect to see speculative retail parks appear.

In general the Bulgarian market has simply grown too quickly. Organic growth from the high street to the shopping centres has not been allowed to occur, and as a result we now have instances of over-supply. Whilst the global economic crisis has obviously had its huge negative effects on the real estate market, it could be argued that it has saved Bulgaria from over-supplying its retail market from an unrecoverable position.

Freezing of developments both before and mid-way through construction has meant that the existing centres and those soon opening have had a chance to stabilise their position, and it would appear that 2009 was the low point and that 2010 is bringing renewed optimism.

The retail market in Sofia is expected to cope well with the new developments opening and there is genuine hope that they will improve the market in the city. The regions similarly should benefit from new centre openings and the tenants they bring, but owners of existing centres will need to work harder in order to maintain their position. As the country rises from the global economic crisis it is expected that unemployment will fall and GDP will rise and therefore we expect more expendable income.

Key message

Whilst the Bulgarian market offers significant potential for new "modern" shopping centres, a slowdown in development after 2010 would enable these newly built schemes to become more established within the local retail hierarchy.

Mall Varna

Industrial market

Location

Sofia

Sofia is acknowledged to be the largest logistic and industrial centre within Bulgaria, with total stock currently exceeding 1.25 million m^2.

New supply within the capital's ring road increased by 58,000m^2 in H1 2009, with a large proportion of this (16,200m^2) attributed to Sofia Airport Centre being developed by Tishman. Speculative space continued to be delivered over the course of 2009, predominantly through projects that had overrun from H2 2008, bringing the total stock of space for the city to just over 220,000m^2.

Indeed, Sofia experienced greater levels of speculative building than in the rest of the country. Only 25% of new developments that were in the planning or under construction stages in H1 2009 were designed for speculative purposes. By the end of 2009 this figure had increased as Universal completed 15,600 m^2 of logistics space on the Trakia highway, on the outskirts of Sofia close to the ring road.

Forecasts predict that speculative space within Sofia will increase further in 2010 and 2011 as a number of new schemes are in the planning or construction stages such as the Industrial Park Sofia East.

Plovdiv

Plovdiv is Bulgaria's second city. The locations of the industrial areas within Plovdiv are quite separate, since 32% is situated in Trakia (the South Industrial area) and a larger proportion is situated to the north of the city. The total amount of industrial and logistical space within Plovdiv increased by 8% in 2009, predominantly due to Kaufland building a 20,000m^2 distribution scheme in the Rakovski Industrial Zone.

Plovdiv was considered the most rapidly developing industrial and logistic area in Bulgaria. During 2009 almost no new projects have commenced at all. Some projects were delayed or stopped, and the construction of 10,000m^2 in the Central Distribution Park Plovdiv has been postponed.

There are, however, projects under construction despite the pipeline appearing to be in decline. Plovdiv industrial Park is currently being developed and on completion will provide 80,000m^2 of logistic and industrial space. This scheme is not being built speculatively, but on the back of pre-leases, which is typical of the market today as banks have become more conservative in terms of real estate financing.

Logistics Park, Varna

Varna

Varna has a smaller provision of industrial and logistic space than Sofia and Plovdiv. Varna has not suffered to the same extent as Sofia and Plovdiv, since the industrial market has not grown at the same pace.

Modern logistic space in Varna is available to lease, and this supply should be able to service the demand from occupiers. Logistics Park Varna is being constructed in three parts and is available to let. Planning for the project Industrial Zone Varna-West has been approved and construction works are due to begin in H2 2010.

Bourgas

The supply of modern industrial and logistic stock increased by 23,000m^2 in 2009, representing an increase of 14% on the level delivered in 2008. Total stock of modern industrial and logistic space in Bourgas stands, therefore, at 160,000m^2. With the pipeline for future industrial and logistic development almost exhausted, the Municipality of Bourgas has prepared master plans for two new industrial zones. The two schemes are to be built in the northern part of the city near the village of Bulgarevo, with areas covering 30,000m^2 and 10,000m^2. These two projects will be developed by the municipality under the Phare Programme provided for by the European Union.

Supply

The industrial market is still embryonic in comparison to other commercial property sectors, and therefore has not been as greatly affected. The majority of units are built for owner occupation, thus creating an undersupply of speculative industrial space.

Projects such as the Central Distribution Park Plovdiv were postponed in 2009 due to the leasing risk that speculative developments provide, with banks preferring projects that have large elements of pre-leasing and build- to-suit units. Only 25% of projects that began in the first half of 2009 were built purely for speculative purposes. In the first half of 2009 barely any projects began construction in Plovdiv, Varna or Bourgas.

The majority of the new stock in Bulgaria is currently being built to the north and east of Sofia in the industrial districts of Druzbha and Gara Iskar with the total supply for the area planned to reach in excess of 1.35 million m².

Demand

Demand for speculative modern industrial units has traditionally been low as the majority of companies have preferred to design and build their own units. Demand for logistic space was very low in the first half of 2009, but picked up during H2 as occupiers became more active. Demand for units continues to be driven by third party logistic providers and companies involved with fast moving consumer goods. During the recent economic downturn low cost supermarkets and hypermarkets have thrived, with Lidl, Picadilly and Billa choosing build to suit schemes while Kaufland has established a large distribution centre in Plovdiv.

Primarily, demand has focussed on Sofia, with the recently completed Sofia Airport Centre attracting interest from larger international firms such as Honeywell, Germanos and Hilti.

In terms of investment, logistic and industrial property has yet to establish itself as an attractive asset class to investors. There has, to date, been relatively little speculative space offered for sale and leases to institutional tenants are rare.

Vacancy

During 2009 the vacancy rates for industrial and logistic space have remained relatively stable. As supply of speculative office space has been so minimal for such a long period of time vacancy rates have generally remained relatively low. Within Sofia's industrial market, vacancy is currently estimated to be as low as 1%. The regional centres of Bourgas, Varna and Plovdiv have been subjected to higher vacancy rates which are generally considered to be circa 3-4%.

Rents

Rental levels for modern logistics space in prime locations remained relatively stable throughout 2009, with rents for modern logistic space currently at €5.50/m²/month in prime areas such as the north and east industrial districts of Sofia. Recycled stock is leasing at circa €3/m²/month, reflecting the position of supply of older stock exceeding demand. Prime rents in the regional industrial centres are lower and are averaging €4.50/m²/month, although a number of modern schemes are available to let at lower rents.

Sofia Airport Centre, Logistics Centre

Residential market

History

Bulgaria has a long history of its people owning their own homes rather than renting. Statistics indicate that only 10% of the Bulgarian population is in rented accommodation, which is low compared to Western Europe.

The quality of residential units has generally improved in recent years, although there is an abundance of poorly designed buildings, and due to the current economic downturn half finished developments across Sofia.

Traditionally, the Lozonets and Iztok quarters in the capital have been home to higher quality apartment buildings, while the villages below the Vitosha Mountains range in the south and west of the city remain the most desirable for family homes.

Many high-rise council estates were built during the former communist era, particularly in Lyulin in the north of the city , and Mladost in the south. These areas currently have the highest residential population. The life expectancy of buildings in both areas is coming to an end, therefore lower cost building in these areas should be in demand over the next 5 years.

Locations

Sofia

The residential market in Sofia is the largest in Bulgaria. As with most large cities, the city centre generally commands the highest prices, together with peripheral locations, in this case the suburbs of Doctors Garden, Ivan Vazov and Lozenets.

Values for apartments in and around the city centre have not been particularly adversely affected by the financial crisis due to continued demand, and a lack of available space keeping levels of supply down.

Outside of the centre, the areas to the west of the city, along Boulevard Bulgaria and Manastirski Livadi, have seen a large supply of new apartment buildings developed over the past three years, although a number of these have been left vacant or had development frozen. Despite values in this area having dropped it is still seen as one of the more desirable residential locations within the city due to its accessibility and nearby amenities.

The areas to the north are predominantly social housing, with the largest district of Sofia, Lyulin, now home to over 250,000 residents, making up almost 20% of the cities total population of 1.25 million inhabitants. It is a similar story in nearby districts of Mladost and Nadejda where the majority of housing is low cost and values are low. That said, the life expectancy of a large number of buildings in these areas are coming to an end and as such we expect to see demand for further low cost housing in these areas in the coming years.

The city of Sofia and its surroundings have not yet witnessed speculative development of 'higher end' housing schemes that are now beginning to appear in many CEE towns and cities. As well as high quality apartments in central Sofia, there is also demand for high quality housing on the outskirts from both high net worth foreigners and Bulgarians. Family housing is predominantly one-off developments, many of which are in need of repair, and this is another sector where we expect growth in supply as demand increases.

The problem is the lack of supply catered to the higher end sector, with developers still choosing to build cheaply, despite a customer base being there that is capable of securing mortgages or even cash purchasing.

Capital values Sofia

Sales prices Sofia

Area/Location	Average price per m²
Doctors Gardens	1550
Ivan Vazov	1300
Lozenets	1250
Iztok	1250
Geo Milev	1100
Blvd. Bulgaria	1000
Boyana	980
Dragalevci	950
Simeonovo	950
Mladost	870
Manastirski Livadi	850
Student Town	790
Ovcha Kupel	780
Vitosha	750
Zapaden Park	750
Lulin	700

Rents Sofia

Headline rents in EUR per calendar month (Sofia)				
Area/Location	**1 bed**	**2 bed**	**3 bed**	**houses**
Doctors Gardens	450	900	1700	N/A
Lozenets	350	500	900	N/A
Iztok	350	550	1200	N/A
Ivan Vazov	250	650	1200	N/A
Blvd. Bulgaria	300	500	800	N/A
Lyulin	180	230	300	N/A
Mladost	200	250	320	N/A
Student Town	220	270	360	N/A
Geo Milev	300	420	490	N/A
Vitosha	250	350	450	N/A
Zapaden Park	200	280	340	N/A
Manastirski Livadi	280	350	500	N/A
Ovcha Kupel	210	320	350	N/A
Boyana	300	500	900	2500
Dragalevci	280	450	600	1900
Simeonovo	280	450	600	1700

Regional Cities

Bulgaria's regional cities also saw a slump in house prices in 2009. Major cities such as Varna, Plovdiv, Bourgas, Rousse and Stara Zagora showed decline of between 20-25%.

With the exception of Varna, most regional cities have much lower average price levels than Sofia and this is shown in the table below.

The earning potential in regional cities is the main reason for the reduction, and as such the majority of supply is low cost. That said, Varna and Burgas are still showing healthy levels of value, down to the ports and the industry and employment brought by the Black Sea

Average price levels	
City	**Avarage prices per m²**
Varna	900
Plovdiv	650
Rouse	550
Bourgas	850
Stara Zagora	600

Holiday Homes

The holiday homes market includes the Black Sea coastal resorts such as Sunny Beach and Golden Sands and also the ski resort towns south of Sofia of Bansko and Borovets.

Both have seen huge changes over the past five years, with extensive development catering for the 1/2 bed apartment market. The vast majority of buyers were foreign, mostly from the UK and Ireland, and the market was seen as a key investment product in a growing economy.

Due to mass over-supply in Black Sea and ski resorts, a result of a lack of any clear planning restrictions, there has been large reductions in value across the board.

Likewise as in most of Bulgaria, mortgages are very difficult to obtain. The main problem in the main towns and cities is the interest rate and level of equity required, whereas the majority of leading banks are currently unwilling to lend for holiday home purchases. Therefore, the only buyers are cash buyers, and as such values reflect this. The majority of buyers today are either Bulgarians or from Russia and the Baltic states.

In terms of values, the table below shows the extent of the fall in values in recent years:

Location	2006 Price €/m²	2007	2008	2009/10
Sunny Beach	1350	1350	850	550
Golden Sands	1250	1250	750	500
Bansko	1350	1400	1000	600
Borovets	1400	1500	950	650

Overview

During 2009 the residential property market in Bulgaria showed decreasing pricing. The reasons for this are two-fold. Firstly, as with most markets, the Bulgarian market suffered from the fall-out of the worldwide economic crisis. Secondly, the level of demand was never going to reach the vast supply levels and this in turn had a further negative impact on values.

Sales prices for dwellings in Sofia slipped on average by 25-30 %. In terms of the regions, the highest decreases were registered in the northern cities of Bulgaria: Montana and Vidin, and Shumen in the east.

Banks were very conservative when lending to new buyers having some of the highest interest rates in the EU of nearly 10%. Bulgaria is still under the currency board and even though the National Bank of Bulgaria's base rate is 0.39% interest rates are dictated by the Banks recourses, which are increasing deposit rates to very high levels to obtain more cash to operate.

There is generally a high level of caution from the buyers side due to the uncertainty over pricing and where the pricing will shift over the next 12 months.

Borovets Gardens

Mortgages

During the first half of the year financing was difficult to secure, but in Q3 mortgages were available at some of the highest levels of 10.5%. By the end of 2009 mortgages were available at slightly lower levels of 9.5%. Banks were lending no more than 70% of the loan value, showing a level of constraint compared to previous years when mortgages of over 90% loan to value were not uncommon.

Bulgaria's conservative lending has therefore resulted in a large reduction of buyers capable of investing the necessary level of equity. Further interest rate cuts are expected in the first quarter of 2010 which is a positive sign for buyers and existing mortgages. The good news is that the amount of overdue loans is only 3%.

Supply

Supply of newly build residential properties continued to grow in 2009, but at a reduced pace compared to 2008 and with many developments frozen due to lack of finance.

According to the preliminary data of the National Statistical Institute, in the first quarter of 2009 there were 547 completed residential buildings across Bulgaria, and a marked decrease of 10.6 % compared to the first quarter of 2008. The number of the new units within new buildings decreased by 12.9% compared to the first quarter of 2008 and reached 3 897.

In comparison with the previous quarter the number of the newly built residential buildings decreased by 432 and the number of the dwellings in them decreased by 42.8 %.

Summary

The following 12 months are certain to be a testing time for the Bulgarian residential market.

In Sofia we expect very little new development to come out of the ground and instead there is likely to be a recommencement of frozen projects as the market situation starts to improve. This will be the year for saturation, where existing vacant units and those under development start to sell and for the levels of supply to move more in line with market demand.

In terms of values, both Sofia and the main regional cities should see slight increases in the prime markets, i.e. city centre apartments and higher end product, and values stabilising for the secondary market.

It will be a similar story in the Holiday Homes market. Little, if any, new development is anticipated and much will depend on mortgage lending if the existing vacant and half built stock will witness any take up. If the banks continue to turn away from lending in the holiday homes market then there is likely to be another 12 months of limited activity and falling values.

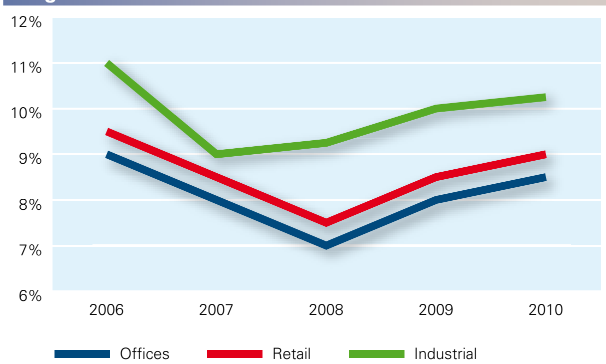
Another year of little foreign investment is in prospect, with the majority of activity coming from domestic buyers. As stated, much will depend on mortgage lending, and for interest rates on mortgages to reduce more in line with EU levels.

Investment market

Avto Union Centre

The volume of investment activity in 2009 was extremely low, with only one open market deal occurring in Sofia in the whole year. Despite a number of schemes being openly marketed, the number of buyers, particularly from abroad, has steadily fallen.

Bulgaria investment



Source: King Sturge

Currently the vast majority of active buyers in the market are of an 'opportunistic' nature, with their yield target rates reflecting this. Hence, there were few actual transactions in 2009, and 2010 is expected to be another quiet year on the investment front. The gap between what vendors are willing to sell at and purchasers are willing to buy at is currently around 100 basis points.

In terms of demand in 2010 and beyond, prime assets in Sofia will realistically be the focus for foreign investors. In particular, prime shopping centres and office buildings will be of interest, and any transactions that do take place in 2010 are likely to be for these asset classes. The regional markets suffer from an over-supply in the retail sector, while very little office or industrial stock is available. Investors have, therefore, tended to shy away from these markets.

In terms of yield movement, it is safe to assume that the only direction for yields to move is back down. The following table shows current prime yields in each sector:

Sector	Sofia	Regional
Office	8.5%	9.5%
Retail	9%	9.75%
Industrial	10.25%	11%

The lack of activity means there is currently little evidence to back up true yield shifts and therefore one can only assume where yields are judged to have moved to by also looking at nearby countries across Central & Eastern Europe.

The volume of investment activity in 2009 was extremely low, with only one open market deal occurring in Sofia in the whole year. This was the purchase of the Avto Union Centre by Greek private equity fund Bluehouse Capital, for a deal reported to reflect a yield of 10.14%

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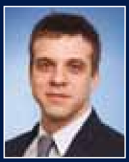

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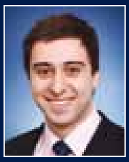

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