

Market Trends

- Office space completion in Q1 2009 has decreased by more than 50%
- Vacancy rates are still high compared to Q1 2008
- Prime rents continue to fall and are now being quoted at ca. €15 per sq m per month

Market Dynamics

Supply	↓
Vacancy Rate	↑
Prime Rent	↓
Prime Yield	↑

OFFICE MARKET OVERVIEW

The high-speed growth of office rents has become a thing of the past. The dynamic environment on the Sofia office market that was observed during the last couple of years has now calmed down and is further compressed by the significant pipeline scheduled for completion within the next few years. We should point out that occupiers are increasingly focusing on the total cost of occupation (including annual running costs, service charges and rent-free periods), as opposed to rental cost alone.

The investment market has also slowed down considerably. The lack of buyers pushed yields further upwards in H2 2008 as negotiation strength fully moved onto the buyer side. The small number of transactions that actually occur are taking longer to close, and discrepancies between price expectations of buyers and sellers are making it very difficult to conclude investment deals.

As a result of the ongoing financial crisis, the falling rental levels and the considerable pipeline of modern office space, it is expected that office yields will decompress further in the short term, but then will return to the levels of 2007 once the recession slump has passed.

STOCK AND NEW SUPPLY

Office space completion has decreased in comparison to the record levels of 2008. Q4 2008 supply was more than double the Q1 2009 amount. Furthermore, all the office space delivered in Q1 2009 was Class B; most of the high-quality office space is scheduled for later in the year. This resulted in the share of Class A offices shrinking even further to less than 30%.

In line with recent trends most the new office completions are located in non-central location (NCL) and along Sofia's Entrance Boulevards (EB). As a consequence the share of CBD office stock decreased to ca. 23% of the total, while EB kept its share of ca. 50%. Another notable characteristic of the new supply is that it is 100% speculative – owner occupied space in the capital has fallen to under 20% of the total stock. The situation is similar when considering the entire 2009 pipeline – only ca. 10-15% of it has been announced as owner occupied.

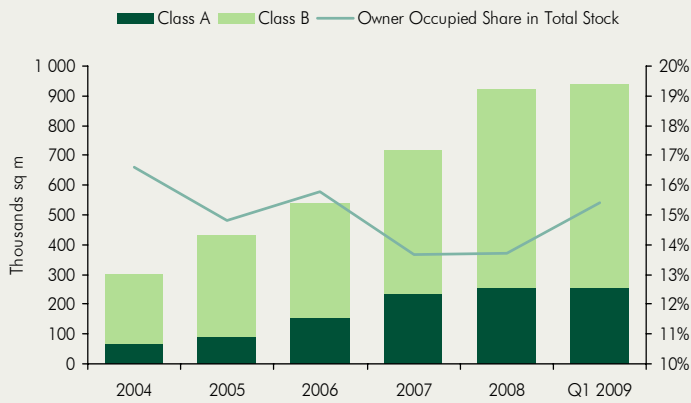
Key Economic Indicators 2005 – 2008

Macroeconomic Indicator	2005	2006	2007	2008*
GDP Growth (%)	6.2	6.3	6.2	6.0
Annual Inflation (%)	6.5	6.5	12.5	7.8
Foreign Direct Investments – FDI (€ bln)	3.15	6.16	8.49	6.16
Foreign Direct Investments – FDI (% of GDP)	14.4	24.4	29.4	18.1
Base Interest Rate (%)	2.04	2.69	3.93	5.12
Average Monthly Salary (€)	166	184	220	280
Final Consumption (€ bln)	19.3	22.0	24.6	28.8
Unemployment Rate (%)	10.7	9.1	6.9	6.3

Source: NSI, BNB

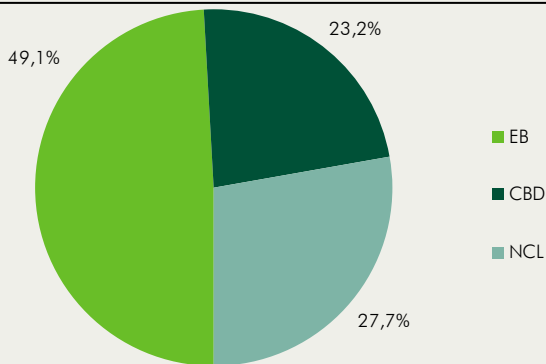
* preliminary data for 2008

Sofia Office Stock Class and Type Shares – 2004 to Q1 2009



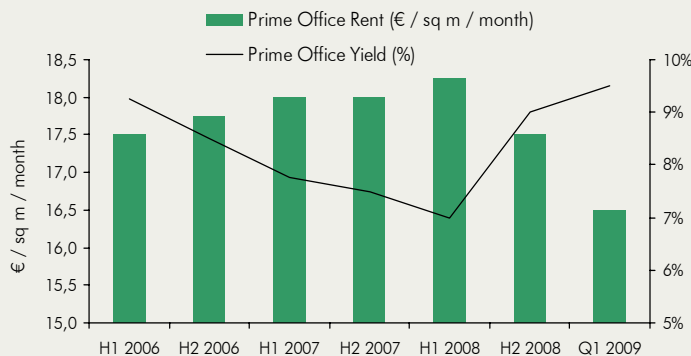
Source: Elta consult

Sofia Total Office Stock per Location in Q1 2009



Source: Elta consult

Sofia Prime Office Rents and Yields – 2006 to 2009



Source: Elta consult

Selected Projects in Pipeline for 2009

Name of Project	Office, sq m	Completed
Kambanite Business Centre	15,800	Q2 2009
Benchmark Office and Shopping Centre	17,000	Q2 2009
Bulgaria House	10,000	Q2 2009
Stella Park office complex	14,500	Q3 2009
Balkan News Corporation office building	22,000	Q4 2009

Source: Elta consult

DEMAND

Demand for quality, class A office space in Sofia remains stable despite the negative effects of the financial crisis – the harshest impact has been on the lower class office space in poor locations. At any rate, the slowdown of the economy has resulted in weakened occupier demand, increased vacancy levels, and a downward correction of rents across all office types and classes, although to a different degree. The trend towards rent adjustments and growing incentives on the part of landlords, which appeared in the last quarter of 2008, has become even more obvious in the first months of 2009.

Nevertheless, take-up level in Q1 2009 is still high due mostly to several large pre-lease transactions:

- Bulgarian Telecommunication Company (BTC) signed a 20-year lease agreement for 23,000 sq m office space in European Trade Center (ETC) on Tzarigradsko Shosse blvd. (scheduled to open in January 2010) at an average monthly rate of ca. €12.6 per sq m;
- Carrefour has also leased 7,500 sq m office space in ETC, next to their first Sofia hypermarket;
- Germanos Telecom Bulgaria has signed a lease agreement for 2,300 sq m of office and logistics space in Sofia Airport Center (SAC) – the first two buildings of the center are already completed, while the third is scheduled for May 2009, making the total area 27,000 sq m;
- Honeywell Bulgaria has also rented ca. 3,000 sq m office and logistics space in Sofia Airport Center (SAC);
- 2Be telecommunications retail chain has leased ca. 2,600 sq m office space in Vassilev Business City (Business Town Sofia) in January 2009;
- Hewlett & Packard (HP) signed a 10-year lease agreement for ca. 8,000 sq m of office space in Kambanite Business Center (KBC) on Sofia's Ring Road across from Business Park Sofia; (KBC should be completed in Q2 2009).

RENTS

Office rents in Sofia continue experiencing a downward pressure as a result of a mixture of factors, the major ones being the global crisis (and the slowing down of the economy as a result), the weakened occupier demand, and the large number of office completions over the last couple of years. Currently, headline monthly rents for class A office space are in the range of €12.5 – 15 per sq m, while for class B they are between €8.5 and €12 per sq m, depending on location, amount of leased space, and lease duration. There are higher offers, but we have no evidence of any deals concluded on these levels.

Rents in the CBD are closest to the prime rental values, due to the limited availability of good quality office space and very limited supply in the pipeline; we expect that CBD rents will be least affected by the overall decrease that has started in Q4 2008, and might even witness some growth towards the end of 2009.

Sofia Sub Markets Map



Source: Elta consult

DEFINITIONS

Floor space areas: Figures relate to gross areas. Availability records all space which is being formally marketed. Take-up records all space which is let and sold for occupation.

Development areas: These include new buildings, redevelopments behind existing facades and buildings undergoing substantial refurbishment to provide high quality accommodation. All figures refer to gross lettable areas.

Prime yield: Represents the yield, which an investor would need to pay now to buy space in a prime location, which is fully let at its current rental value.

Pre-Let: New space leased prior to or during construction.

Rents: An average of the rental values applicable to the highest quality buildings in prime locations is taken to give a top rental value norm figure.

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VACANCY RATES

Despite the significant amount of pre-leased office space, take-up in Q4 2008 and Q1 2009 could not keep up with the amount of office space completions, and as a consequence, vacancy level increased to ca. 8% on average. It is still lower for class A office space (ca. 7.3%), while CBD vacancy rate remained stable at around 3.5 – 5%.

PIPELINE

There is more than 100,000 sq m of office space scheduled for completion in Q2 2009, of which around 43% are announced as class A. Less than 10% of the pipeline is located in the CBD, while 42% is in non-central locations (NCL). Another 150,000 sq m should be completed in the second half of 2009, thus expanding the total office stock in Sofia to over 1.2 million sq m at the end of the year.

Among the largest projects to be completed in 2009 are BenchMark Center on Tsarigradsko Shosse blvd. (17,000 sq m), Kambanite Business Center (15,800 sq m) and Alfa Business Center (7,800 sq m) near BPS, and Stella Park office complex (14,500 sq m) also on Tsarigradsko Shosse blvd.

OUTLOOK

Although pre-lease agreements and build-to-suit solutions, boosted by banks' financing requirements as well, will continue to account for a large share of the annual take-up in the short run, we expect office completions in 2009 to exceed take-up and thus increase the availability of office space in the capital. This in turn will inflate vacancy rates and depress rental levels further for all but the best located properties.

In the long run, we expect that with economic recovery take-up will start expanding at a faster rate and cause rental rates to return to the levels of mid-2008. Because of the huge pipeline, however, not all projects and office premises will be successful, and the gap in rents and vacancy levels between prime, high-quality office space and secondary one will widen.