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MARKET OVERVIEW

# OFFICE SPACE

SOFIA | Q4 2010

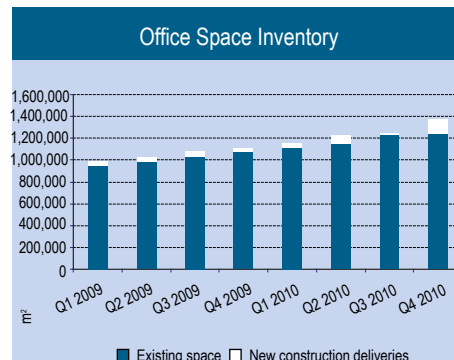
### Office Market Highlights

- » The office space inventory reached 1,378,200 m<sup>2</sup>
- » 361,700 m<sup>2</sup> are actively under construction
- » The overall market vacancy for class A and B office space increased to 24.3%
- » The net absorption in Q4 2010 was 35,700 m<sup>2</sup>, while the annual figure is estimated just over 105,000 m<sup>2</sup>, which represents almost a 50% increase from the 2009 level
- » The average rental rates continued to decrease further in all submarkets



### Inventory

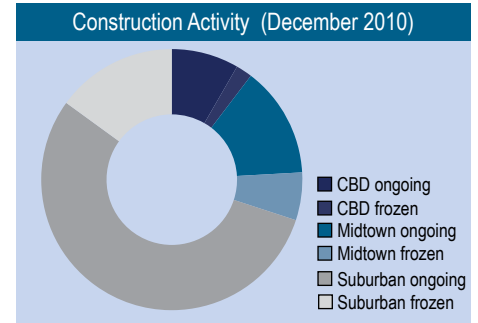
2010 turned out to be a record year in new office space deliveries amounting to 265,500 m<sup>2</sup>. It was capped by a record fourth quarter with 132,000 m<sup>2</sup> of newly constructed offices. Several big projects, which started during the construction boom 3-4 years ago, were completed and now increased significantly the supply of modern office space. By the end of the year the total inventory in Sofia reached 1,378,200 m<sup>2</sup> of which 45% represent class A properties. Some of the major projects, delivered this year include Megapark, ETC, and Serdika Center.



### Construction Activity

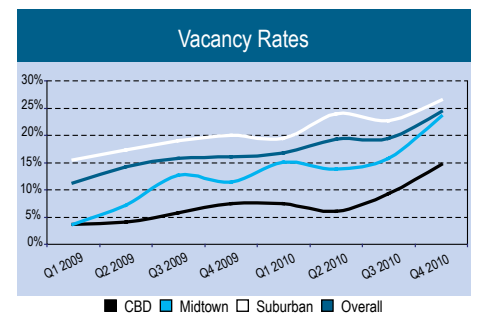
The overall construction activity declined in 2010 in terms of issued construction permits and new construction starts. Some investors made additional efforts to complete the ongoing projects in time, while others delayed the construction process due to lack of prospect occupiers and the associated restricted debt financing.

By the end of December 361,700 m<sup>2</sup> were under active construction and approximately 168,800 m<sup>2</sup> were frozen or delayed. Tzarigradsko Shousse Corridor remains the submarket with the highest volume of office space under construction accounting for 18% of the market total. There are 250,000 m<sup>2</sup> are scheduled for delivery in 2011.



### Vacancy

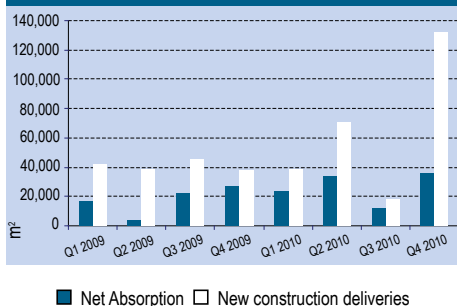
The year-end witnessed a significant increase in the volume of vacant office space following the delivery of several big projects with considerable vacancy. By the end of December the vacant space amounted to 335,000 m<sup>2</sup> or 24.3% from the overall class A and B inventory. Interestingly, for the first time ever the CBD vacancy reached double digits in the fourth quarter rising to 14.6% from 9.3% three months earlier. The overall suburban vacancy reached 26.5% and the overall midtown vacancy 23.5%.



### Absorption

The leasing activity has picked up in 2010 with the improving economic environment. As a result, the cumulative annual net absorption in class A and B properties was 50% up from 2009, amounting to 105,000 m<sup>2</sup>. With 35,700 m<sup>2</sup> the fourth quarter marked the highest quarterly result in 2010. Companies in the IT and BPO sectors continued to expand and remained the most active on the market. We have also witnessed several notable relocations and consolidations, but their net effect on the absorption level was only

### Absorption & Deliveries



marginal, since tenants were moving from one property to another within the upper property grades. The big contributor for the positive result in the class A and B office segments were relocations from class C properties as many tenants capitalized on the falling rents.

## Rental Rates

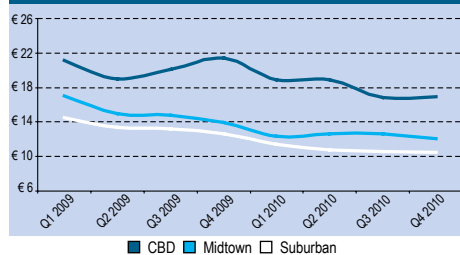
Rents continued to fall throughout the year reaching record low levels in many buildings. The average levels declined for

both, class A and B offices in all submarkets as a result of the increasing oversupply and the intensifying competition for tenants among landlords.

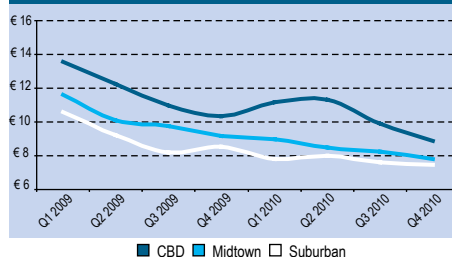
For class A space the average net asking rent in the CBD fell by 21.2% on an annual basis, followed by 16.8% in suburban submarkets and 13.4% in midtown. On a quarterly basis for the last three months, the change was the most significant for midtown submarkets as the average level dropped by 4.5% followed by suburban submarkets with 0.8%, while the CBD figure remained unchanged. Overall, the asking class A rents range between €7 and €25 m<sup>2</sup>.

In the class B segment the average net asking rents fell down for the year by 14.9% in midtown locations, 14% in the CBD, and 13% in suburban submarkets. The decline in Q4 2010 quarter was 5.5%, 10%, and 2.4% respectively. Class B rents ranged between €4 and €12 per m<sup>2</sup>.

### Average Asking Class A Rental Rates



### Average Asking Class B Rental Rates



### Selected Lease Transactions in Q4 2010

Tenant	Building	Size (m <sup>2</sup> )
Ernst & Young	Polygraphia Office Center	2,500
Pfizer	ETC	1,800
LiveNews	Megapark	1,250
Renault Nissan	Iztok Tower	1,100



## Economic Highlights

- The foreseen economic recovery is slowly taking place. The recession in 2009 (-4.95% real GDP growth) and Q1 2010 (-3.97%) gave way to the positive GDP growth rates in Q2 (0.51%) and Q3 2010 (1%). For 2010 the IMF is expecting a real GDP growth in the range 0% -0.4%
- As of November 2010 the year-on-year inflation rate (based on the Consumer Price Index) is 4.6%, while the accumulated inflation since the beginning of 2010 is 4.1%. The 12-month average rate for the period November 2009–November 2010 is 2.1%
- Based on preliminary data the FDI flows in Bulgaria for the period January – October 2010 amount to €844.9 million (or 2.3% of GDP) compared to €2526.3 million (or 7.2% of GDP) for the same period of 2009, showing a drop of 67%
- The Base Interest Rate for January 2011 is 0.18%, remaining almost unchanged for the last two quarters
- The country average unemployment rate (as given by NEA), has fallen by about 1 percentage point since the beginning of the year and as of October 2010 is 8.92%

## Market Outlook

The leasing activity will remain stable in 2011, but rental rates will stay under the pressure of the increasing oversupply and vacancy. According to initial data, approximately 250,000 m<sup>2</sup> of new office space are scheduled for completion in the next 12 months.

## Investment activity

The investor sentiment has moderately improved in the end of 2010. The Bulgarian commercial property market witnessed an increased level of investment activity during Q4 2010. There were no investment transactions closed during the year, but buyers and sellers moved closer to price consensus and it is a matter of time to see completed deals during 2011. Prime yields for office buildings in Sofia and secondary

cities were 9.0/10.0% and 10.5/11.0% respectively. Compared to 2009 bank financing also showed signs of recovery with interest rates on new business loans going slightly down and volumes going up during 2010. Provided there is a further improvement of the macroeconomic indicators in 2011 and the government conducts a correct fiscal policy, we expect to see an increased investment interest on Bulgarian real estate market.



Selected Office Projects Scheduled for Delivery in 2011

Bldg Name	Market	Office Area (m <sup>2</sup> )
Sofia One	Suburban	26,000
Vertigo	Suburban	17,000
Polygraphia Office Center	Midtown	16,500

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