

Real Estate Investment Analysis

Bulgaria

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1. Key factors of the Bulgarian market: Overview

The Bulgarian market overview will provide general information in terms of incentives that investors need to assess in the process of the Real Estate investment decision making.

Bulgaria is the only EU state that has introduced a flat tax of 10% (Deloitte, 2009). The implementation of this policy has contributed to improvement in the local business performance and to attracting foreign companies looking for tax friendly business environment which as an effect will contribute to higher level of employment, improvement of living standards, and increasing government tax income

In addition, Bulgaria also had the lowest average labour cost within EU for 2008 which as a consequence facilitates companies' production efficiency by outsourcing low cost manpower (Eurostat, 2008). This automatically leads to economies of scale, a strategic advantage for companies competing with foreign EU incumbents.

Another important factor for foreign investors is that the Bulgarian currency is fixed to the Euro (1.9558 BGN per 1 EUR) (ECB, 2009). This means that there is no risk of currency exposure such as transaction or economic exposures that would affect value or yields of properties owned by Eurozone investors.

The strategic location of Bulgaria is another essential factor for Real Estate entrepreneurs. Macedonia and Turkey are EU candidates (EC, date unknown). Moreover, Macedonia, Serbia and Montenegro were offered EU visa-free travel from the next year.(Vucheva, E., 2009). These events will make Bulgaria a centre of trade in the Balkan region which will develop the logistics industry and will pick property prices up, thus higher levels of yields.

Image 1: Candidates for EU membership:



(BBC, date unknown)

http://news.bbc.co.uk/1/shared/spl/hi/europe/04/enlarging_europe/html/turkey.stm

According to the Finance Minister Simeon Djankov, Bulgaria will apply in November to join the EMU, the European Union’s two-year currency stability test before the country can change the lev and adopt the euro. That would take the Balkan country closer to the eurozone and the protection of the European Central Bank (Kostantinova, E., 2009).

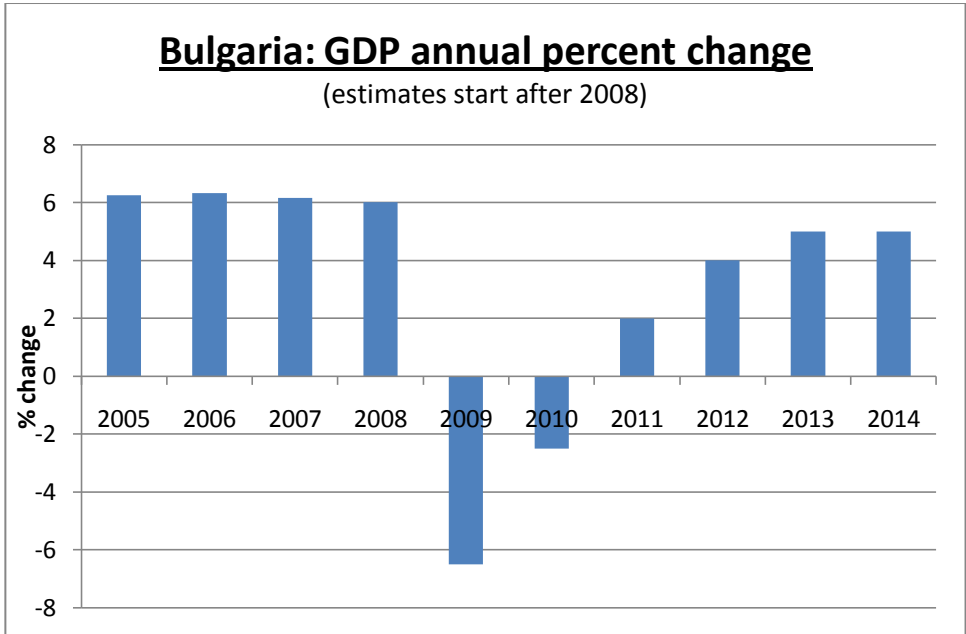
2. Key macroeconomic factors: Overview

Macroeconomics represents the fundamentals of all markets. Investments, no matter of the asset class, are highly dependent on their behavior. Some of main factors that Real Estate investors should assess before entering new markets are the the GDP, inflation, and unemployment figures.

2.1 GDP

The Bulgarian GDP performance was one of the strongest in Europe for the period from 2005 to 2008 as you can see below, mainly driven by FDI inflows which is a strong proof of the market’s investment attractiveness. FDI volumes increased from €3.5 billion in 2005 to their peak of more than €8 billion in 2007. The Real Estate sector accumulated the highest investments volumes of more than €2.5 billion in 2007 (Forton, 2009). However, the country’s wealth is highly dependent on Western Europe’s economies. Still, the latest publications show growth of 0.4% for the Eurozone for the Q3 of 2009 (BBC, 2009). This trend consequently will have a positive impact on the Bulgarian market, returning it to growth after 2 years of recession.

Table 2.1 Bulgaria: GDP annual percent change

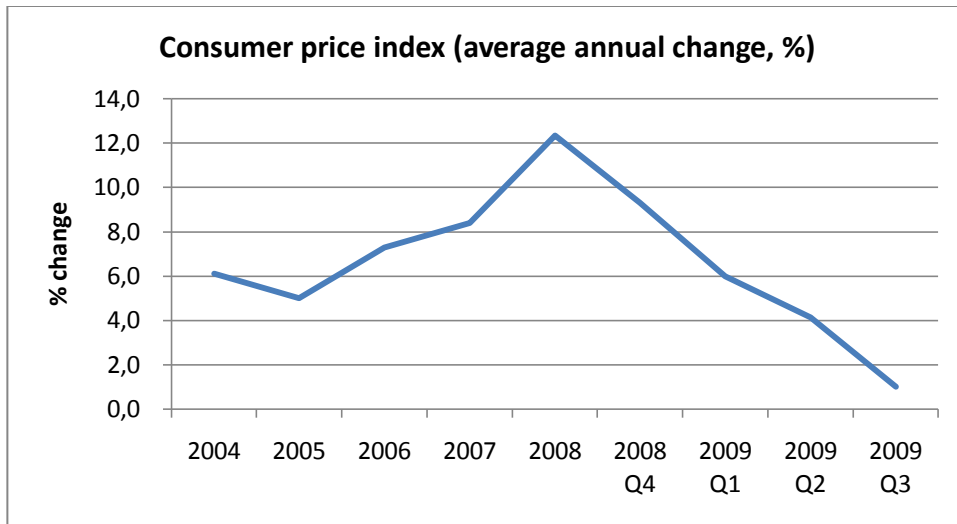


(IMF, 2009) <http://www.imf.org/external/pubs/ft/weo/2009/02/weodata/weoselgr.aspx>

2.2 Inflation

Another important factor for Real Estate investing is inflation. A high inflation rate in 2008 has triggered property prices up which have favoured 'flippers' looking for a quick turnover. Now, when spending is weak, inflation has bottomed to almost below 1% in Q3 of 2009 (BNB, 2009). That will suppress the flipping practices, and will limit speculations on property prices and will prevent future property bubbles.

Table 2.2: Consumer Price Index (Average Annual Change, %)

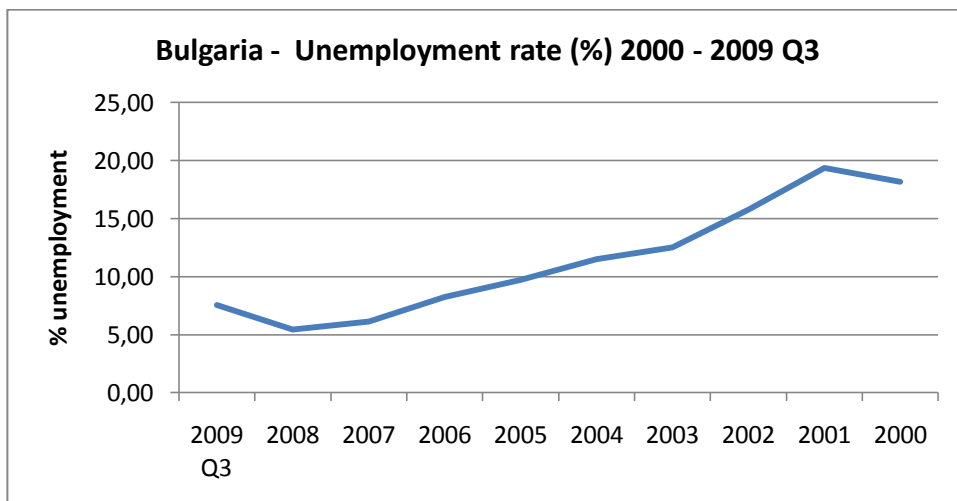


(BNB, 2009) <http://www.bnb.bg/bnb/home.nsf/fsWebIndex?OpenFrameset>

2.3 Unemployment

As you can see on the table below, the unemployment rate has decreased by approximately 15% for the last decade, a trend mainly driven by the sustainable economic growth for this period (ECB, 2009). However, again because of the global recession, the Bulgarian economy has shrunk by causing an increase in unemployment for 2009. Yet, that provides employers with higher choice of skilled labour available on the market

Table 2.3: Bulgaria – Unemployment rate (%) 2000 – 2009 Q3



(ECB, 2009)

http://sdw.ecb.europa.eu/quickview.do?SERIES_KEY=132.STS.M.BG.S.UNEH.RTT000.4.000&

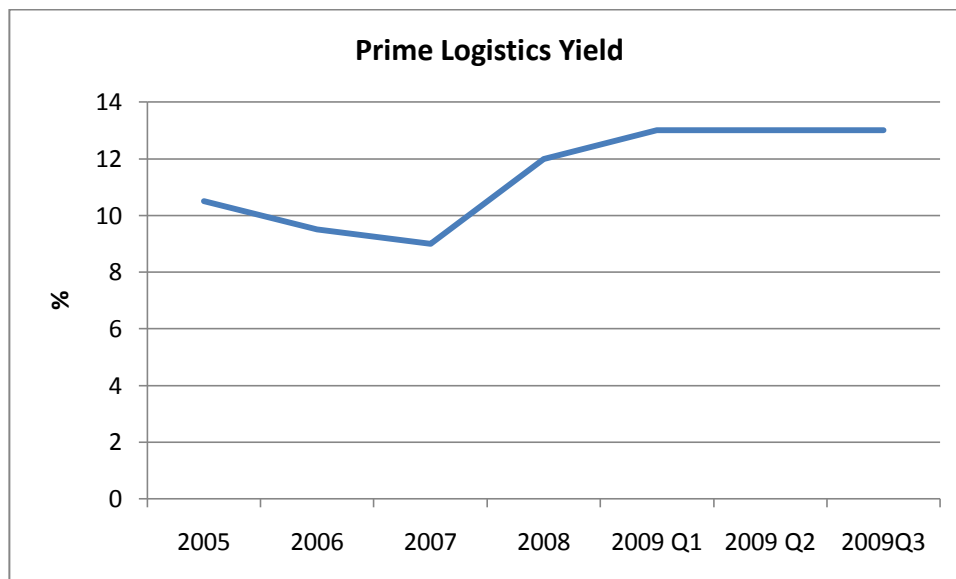
3. Property Overview (recent trends)

3.1 Industrial and logistics markets

The supply of logistics and industrial have been relatively unaffected by the recession. These segments have started their development later compared with the commercial real estate segment, thus remains undersupplied with relatively stable prices. Many projects have been delayed in the first part of 2009, mainly because of the weakened financial back up but it is strongly expected to be retouched in short-term (Colliers, 2009).

The demand in the beginning of the year was very weak but it has started picking up after the second part of 2009. This increase in demand was underpinned by super- and hypermarkets, establishing sound logistics networks, which have flourished in the current recession. Some of them are Lidl, Billa, Kaufland, and Carrefour (Colliers, 2009).

Table 3.1: Prime Logistics Yield



(Source: Forton, 2009) http://forton.bg/en/wp-content/Q3_2009_Logistics.pdf

3.2 Retail market

The fast growth in the retail sector that was witnessed last year has slowed down in the beginning of 2009 due to the worsened current economic situation in Bulgaria. Many retail businesses were forced to minimize costs as a result of the decrease in the sales volumes. Because of the weak performance of shopping malls, retail businesses were forced to make requests for renegotiations for lease terms. The restrictive lending practices of the banks have contributed to further financing issues (Colliers, 2009). A factor easing this sector is the financing provided by banks. They tend to provide loans to retail operators perceiving them as a low risk investment and healthy developers for the market

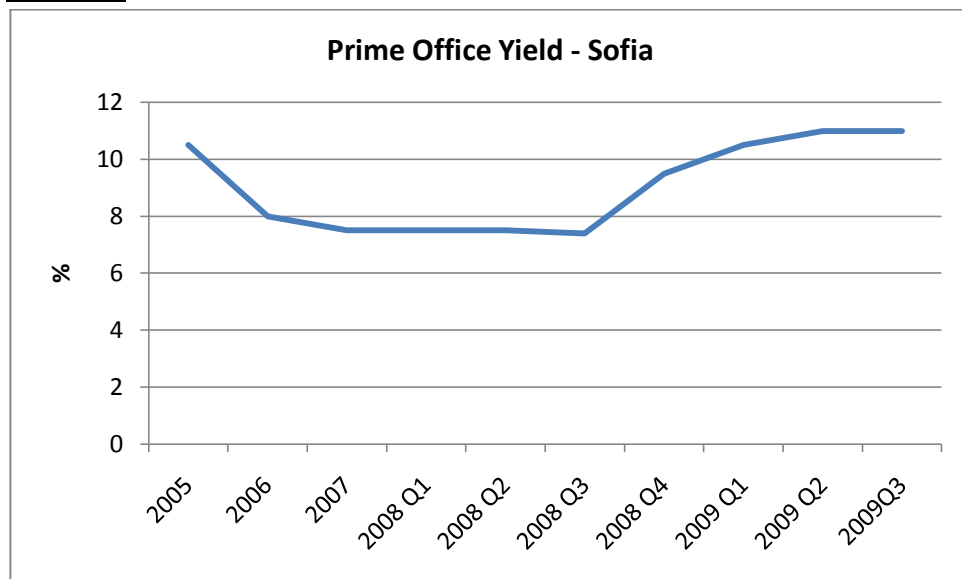
The demand in the retail sectors has considerably decreased. Many businesses in this sector have reestablished their expansion strategies by taking a wait-and see positions because of uncertainty in future revenues. (Colliers, 2009)

3.3 Office market

The office market, particularly in the capital of Bulgaria, Sofia, continues of the most affected commercial market from the economic recession which started in the beginning of 2009. Most companies limited their expansion and some of them even closed down, leaving vacant space. This market remains highly oversupplied because of the weakening demand from tenants which led to fall in renting prices with more than 30% (Forton, 2009)

On the other side, falling office prices and the cheap labour have attracted international outsourcing companies. That makes Bulgaria a leading market for outsourcing on the region of Central and Eastern Europe. According to a research made by Forton, Bulgaria is holding 13th place among the world premium outsourcing destination (Forton, 2009)

Table 3.3: Prime Office Yields - Sofia



(Source: Forton, 2009) http://forton.bg/en/wp-content/Q3_2009_Office.pdf

4. Conclusion and recommendations

To sum up, the Bulgarian market has an attractive framework of incentives for investors as already mentioned in the country's overview. In terms of macroeconomics the country is performing poorly, mainly because of the global recession and its impact on emerging markets. However, this trend will be temporary until developed nations return to growth, as the Euro zone has already achieved that, and reestablish foreign investment practices, returning the Bulgarian market to growth again. When it comes to the Real Estate environment, many entrepreneurs have suffered losses mainly because of the outflow of foreign investors. This consequently led to property bubble

burst which has dropped prices down. In addition, the higher unemployment rate contributed to weak consumption which had a negative impact on the retail and residential property sectors.

The economic recession and the downturn of the property market in Bulgaria, however provides lucrative opportunities. Property prices have reached their bottom. Investors now have the bargaining power to purchase properties below their market value. Forecasts for the Bulgarian economy are positive with average 4% growth in the next 5 years (Goldman Sachs, 2008). That will reduce unemployment and will return investors confidence. Such a trend will push property prices up again. Therefore, at the moment investors have the opportunity to purchase properties on their lowest rate, below the market value, and to reap the benefits of future pickups in property prices and consumers' spending.

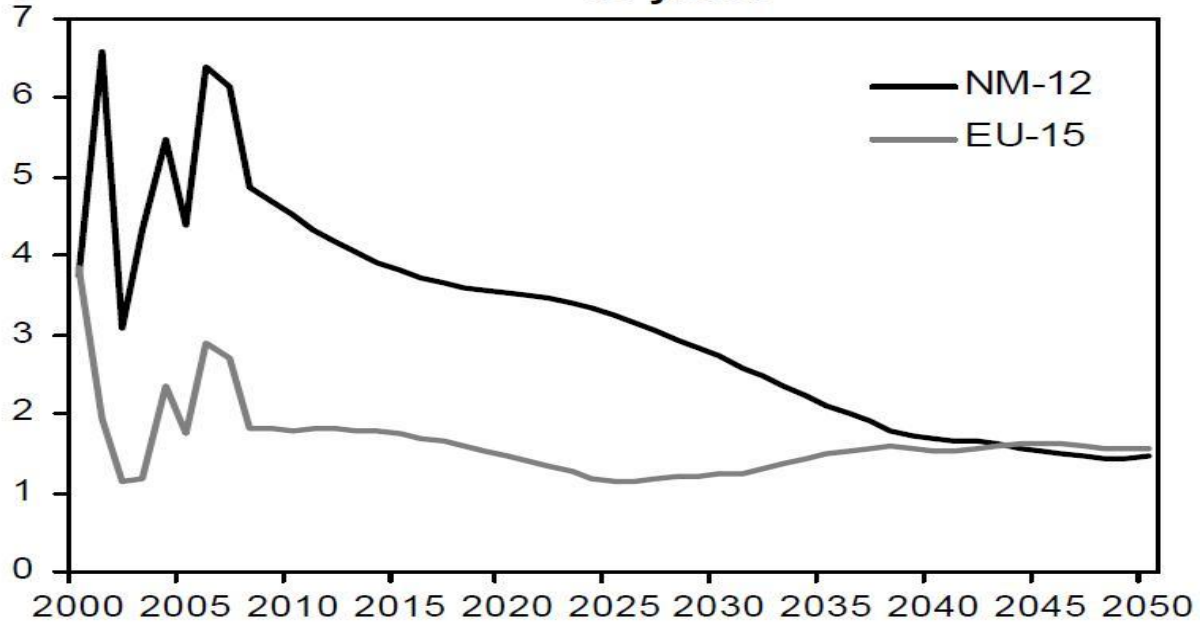
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Appendices:

Appendix A: New EU Member States—A Fifth BRIC?

Real GDP growth, % **NMS can grow faster than EU-15 for the next 30 years**

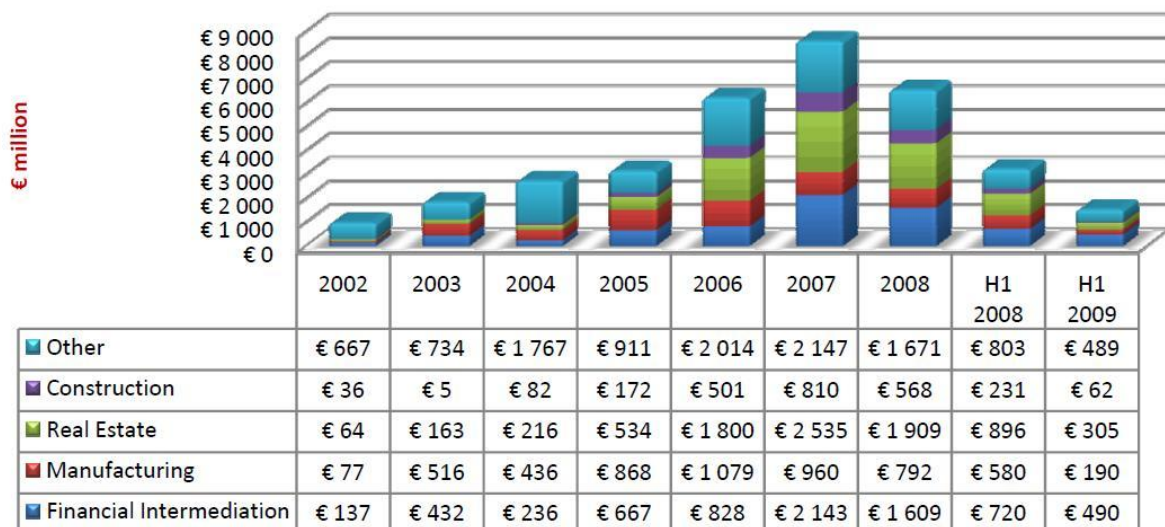


Worldbank, Eurostat, GS projections

(Source, Goldman Sachs) <http://www2.goldmansachs.com/ideas/global-economic-outlook/new-eu-member-states-pdf.pdf>

Appendix B: Bulgaria – FDI by Sector

FDI by Sectors



(Source: Forton) http://forton.bg/en/wp-content/Q3_2009_Economic.pdf

Appendix C: Retail Market Overview – 2009 – High Street (by City)

HIGH STREET

SOFIA – ON ANNUAL BASE		
	m2	Percentage
Total stock	38,161	100%
Vacant	958	2,5%
Replacements	6,036	15,8%

Source: Colliers` research

VARNA – ON ANNUAL BASE		
	m2	Percentage
Total stock	16,315	100%
Vacant	452	2,8%
Replacements	2,228	13,7%

Source: Colliers` research

BURGAS – ON SIX MONTHS BASE		
	m2	Percentage
Total stock	10,872	-
Vacant	90	0,8%
Replacements	1,428	13,1%

Source: Colliers` research

PLOVDIV – ON SIX MONTHS BASE		
	m2	Percentage
Total stock	28,233	-
Vacant	16	0.1%
Replacements	618	2.2%

Source: Colliers` research

(Source: Colliers)

http://www.colliers.com/Content/Repositories/Base/Markets/Bulgaria/English/Market_Report/PDFs/Retail_H2_2009_ENG.pdf