

<u>Recommendation</u>	<u>Previous</u>	<u>From date</u>	<u>52-week target</u>
Market Perform	-	-	BGN 9.73

Sopharma

Business Summary

Sopharma is the second largest Bulgarian pharmaceutical company in terms of sales and holds almost 10% of the Bulgarian pharmaceutical market. The company has the largest capacity for antipyretic production, modern ampoule production line and the only gamma sterilization laboratory in Bulgaria. Sopharma successfully fulfilled the GMP (Good Manufacturing Practice) requirements and received GMP certificates for all its production units in 2004. Export represents more than 50% of Sopharma's revenues, mainly from Russia, Ukraine, Poland and other ex-Soviet markets. Sopharma and its subsidiaries are vertically integrated structure which covers all aspects of production, export, wholesale trading and logistics.

Current Market Activity

Shares of Sopharma posted 48% increase for the last year. However, all gains for the period were made during late 2006 and January 2007. The performance afterward was weak as the price stayed in the tight range between BGN 7.00 and 8.00. The reason could be found in the already strong rise that created almost one billion BGN of market capitalization and the lag of fundamentals. Sopharma didn't manage to attract speculators in 2007 and remains in the focus of long-term investors. This also resulted to low liquidity in terms of number of deals as compared to other Bulgarian blue chips. Sopharma isn't offering the same return as fast growing new stocks or undervalued small and mid-caps. In addition, the company was overpriced for long period of time as compared to other sectors.



Financial Summary

Sales and profits improved in 2007 after the weakness noticed in 2006 due to lower currency exchange gains. Sales for the domestic market were hardly changed (3%) but revenues from exports in USD grew by 41% (30% in BGN) for the first eight month of 2007. The weaker US dollar had negative effect on revenues abroad, which was offset by higher end-prices. The sales of tablets in the domestic market shrank by 19% but were compensated by the strong increase of ampoules. The profit margin improved in first half of 2007 but the cash flow from operations is negative.

Valuation Ratios

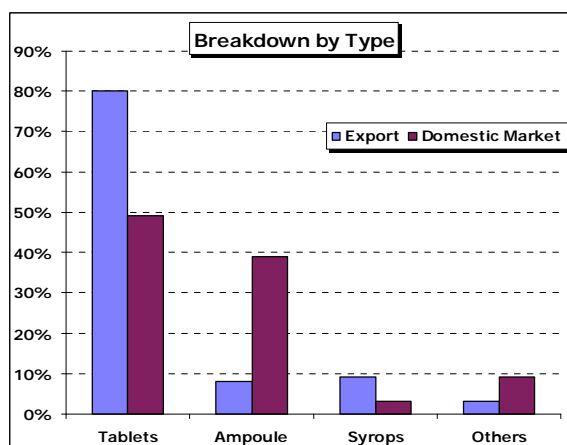
Enterprise Value	1 127 730 000
Dividend Yield - Gross	1.25%
Trailing P/E (ttm)	34.55
Forward P/E (2007)	26.59
PEG Ratio (5yr expected)	0.89
Price/Sales (ttm)	3.22
Price/Book (mrq)	5.08
Enterprise Value/Revenues (ttm)	3.47
Enterprise Value/EBITDA (ttm)	21.68

Profitability and Growth Ratios

Return on Capital	17.61%
Return on Equity	14.70%
Return on Assets	7.65%
EBITDA Margin	15.32%
Net Profit Margin	9.33%
Revenue Growth	33%
EPS Growth	25%
Capital Growth	13.95%
Assets Growth	14.13%

Production

Sopharma is producer of generic pharmaceutical products but maintains own development and innovation activities. The trade marks of Sopharma represent 81% of the export products in 2006 whereas generic products were 19%. Sopharma's tablet plant has the capacity to produce 2.5 billion tablets per year and its ampoule plant's annual production capacity amounts to 80 million ampoules. Moreover, the plant of Sopharma in Vrabevo, which was put in operation in end-2003, has the capacity to produce 1.5 billion tablets annually, as well as 20 million pieces of syrup forms and 30 million pieces of ointments per year. In 2004 the construction of another plant with capacity to produce 12 million pieces of suppositories was finished as well.



Source: Sopharma

Acquisition Policy

Sopharma is expanding its area of operations by acquiring smaller Bulgarian companies. In 2004 Sopharma acquired the majority stake in the capital of the former essential oils producer Bulgarska roza – Sevtopolis. The latter is currently producing predominantly two of the main tablet forms of Sopharma, which are exported abroad. Sopharma also owns several companies abroad, which carry out the exports.

The company acquired stakes in the capital of four of the larger distributors of its products on the Bulgarian market in order to ensure its positions on the domestic market and created its subsidiary Sopharma Trading.

STAKE AND ACQUISITION YEAR		
Rostbalkanpharm	51,00%	2001
Pharmachim Holding	100,00%	2002
Pharmalogistica	89,00%	2002
Sopharma Poland	60,00%	2003
Bulgarska roza - Sevtopolis	49,00%	2004
Electron Commerce	100,00%	2005
Sopharma Trading	99,62%	2006
Mineral Commerce	70,00%	2006
Biopharm Engineering	51,34%	2006
Doverie United Holding	5,07%	2007
Momina Krepost	34,08%	2007

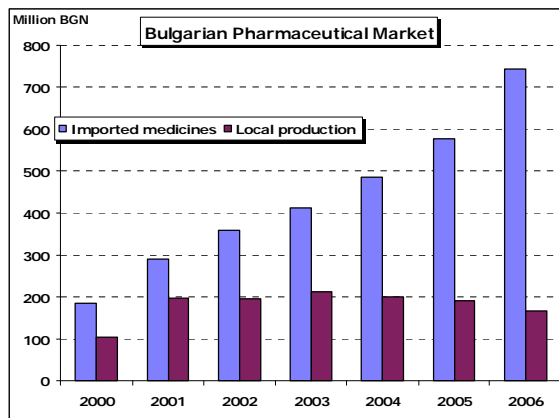
As of 30 June 2007;
Source: Sopharma

Intellectual Property

Sopharma has more than 350 trade marks and 60 patents, most of them registered in different countries. The company protect its intellectual property by the Bulgarian and foreign legislations in this field – patents, trademarks, industrial design. Sopharma is also interested in the possibilities to exercise its exclusive rights of them. However, popular products of Sopharma are subject of imitation drugs in the domestic and foreign markets, mainly by repackaging imported medicines from Asia.

Pharmaceutical Market

Sopharma is relying on export sales to compensate the volatile domestic market. The domestic production is under the severe pressure from imported medicines. Moreover, the local companies are threatened also by counterfeit production, mainly repacked imports from Asia, which is sold under the brands of leading Bulgarian producers. The estimations for the sales of fake drugs are for BGN 100 million annually. In terms of packages sold, imported drugs recently increased to the number of domestic production but their average prices are higher. Bulgarian pharmaceutical market will grow by the moderate 3 to 5%, according to the estimations of different sources in the sector.



Source:

Perspectives

The horizontal and vertical integration retained the position of Sopharma despite the challenges in Bulgarian pharmaceutical market. This is already bearing fruits as end-user prices carry the burden of multiple charges from retailers. Bulgarian government adopted new price regulations that imposed maximum charges for retail trade of 10% over the prices of medicines. Sopharma and its main Bulgarian peer Actavis decreased the discount to retailer from around 10% to 2-3%. The new regulations and lower discounts should decrease the end-prices of drugs and will boost the revenues and margins of both Bulgarian producers.

The health-care outlays in Bulgaria are among the lowest in EU. In addition, the GDP per capita also provide opportunities for the market to grow faster in years to come. Generic drugs are more popular in low income countries due to their better prices.

Market position

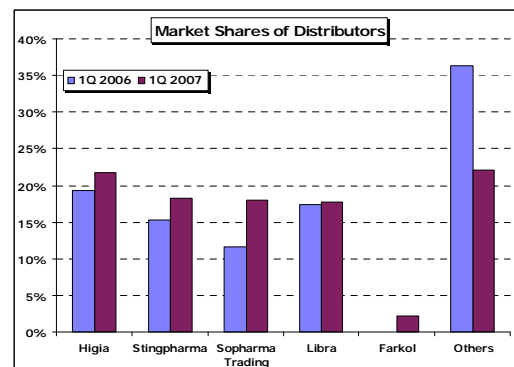
Sopharma and its main Bulgarian peer Actavis retain their leading market positions. The main reason is that they produce well-known medicines that could be bought without medical prescription. The two companies are also supplying hospitals with cheaper medicines than imported analogues. Sopharma has around 10% of Bulgarian pharmaceutical market but is aiming at specific niches like nutrition supplements that are the main source of growth for the market.

Positions of leading pharmaceutical companies in the Bulgarian Market

	1H 2007	2006	2005
Actavis	1	1	1
Sopharma	2	2	2
Novartis	3	3	3
Sanofi-Aventis	4	5	5
Roche	5	7	6
Servier	6	6	7
GlaxoSmithKline	7	4	4
Pfizer	8	8	8
Menarini	9	9	10
Novo Nordisk	10	10	9

Source: IMS Health

The market share of Sopharma Trading in wholesale trading grew to 18.3% and the company is the leading supplier for Bulgarian hospitals. Although this guarantees market share and more competitive prices for Sopharma's products, it carries several problems – low profit margins and delayed payments. The largest distributors are gaining positions as they are mostly vertically integrated with producers or have preferential services for the pharmacies.

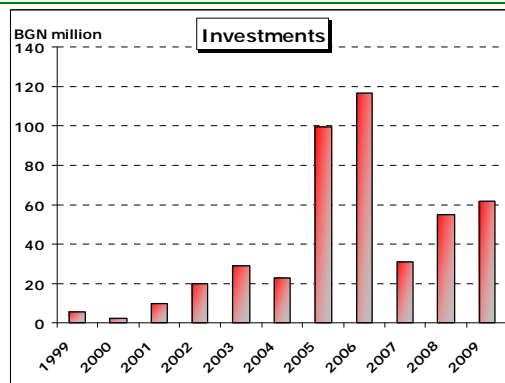


Source: Sopharma

Investment Program

Sopharma continued its large-scale investment program in 2005 and 2006. The building of new tablet plant was approved by the Bulgarian regulatory body in August 2007. The new facility should be finished within 3 years and will significantly increase the production capacity. Sopharma is in process of building new logistical centre.

The reconstruction of the ampoule plant began in the first half of 2007, which will double its production capacity.



Source: Sopharma

Ownership

The 67% of Sopharma was privatized in September 2000 by the specially created company for deal Elpharma by Electroimpex with 60% and Unipharm with 40%. The price for the stake was USD 24 million. Additional 15% were sold afterward to Elpharma, whereas the rest had been offered to individuals in the mass privatization.

After few changes in the ownership in 2006, Elpharma sold its stake to several companies. Gramercy Emerging Markets Funds also acquired minority stake.

SHAREHOLDER STRUCTURE	
Donev Investments (Sofia AD)	25,36%
Telso AD	23,77%
Telecomplex AD	20,42%
Gramercy Emerging Markets Fund	17,26%
Other Legal Entities	10,00%
Individuals	2,88%
State	0,31%

As of 30 June 2007
Source: Sopharma

Stock Information (BSE Ticker: SFARM; Bloomberg: SFARM BU; REUTERS: SFARM.BB)

Last Price	7.93	Market Cap	1 046 760 000	1Y Range	5.33 - 7.96	Average Volume (3m)	524 156
Beta	-	1Y Change	+48%	SOFIX Change	+93.31%	BG40 Change	200.17%

Valuation

The rising profits during the first half of the year are due to increased exports and the vertical integration of Sopharma. This managed to improve the valuation ratios to the average for Bulgarian stocks. Moreover, the stable sales growth and improving margins should provide long-term support for Sopharma to compensate the lag behind other fast developing Bulgarian stocks.

Multiples Analysis

The strong gains in late 2006 and the lower profits made Sopharma overvalued as compared to the market. The stock performance confirmed it so far this year. The situation is different now as net profit is rising and P/E ratio with 2007 expected results is below 25. Sopharma is no longer expensive as P/E ratios of Bulgarian blue chips are above 30 and even 25 calculated with 2007 estimated profits. Revenues for the last twelve months are inflated by the solid increase during the fourth quarter of 2006 after the transformation of wholesaler Sopharma Trading. Excluding the consolidated data, P/S ratio should be twice higher.

Last Price	7,93
Number of Shares	132 000 000
Market Capitalization	1 046 760 000
Net Profit (ttm)	30 294 000
P/E	34,55
Revenues (ttm)	324 870 000
P/S	3,22
Equity	206 058 000
P/B	5,08
EV	1 127 730 000
EBITDA	49 773 000
EV/EBITDA	22,66
EV/Revenues	3,47

Source: Sopharma
Calculations: ELANA Trading

Peers Comparison - Valuation

Comparing Sopharma with similar companies in Central and Eastern Europe will make the Bulgarian company fair valued. The generic producers, with the exception of Lithuanian *Sanitas*, have average P/E of 30 and P/B of 4.82. This is close to the current valuation ratios of Sopharma. We included also companies with own research facilities in the region, classified in Pharmaceuticals – Diversified. This lowers the average P/E and P/B ratios to 25.12 and 3.73, respectively. The P/E and P/B ratios are under the influence of national price policies (like the Bulgarian pharmaceutical market, which is under the pressure of low income consumers and small health care costs) or the degree of leverage. The P/S ratio clears this – the average for generic producers is 4.45, whereas for all companies is 3.61 times revenues.

		P/E	P/B	P/S	EV/EBITDA	EV/Sales
Pharmaceuticals - Generic						
<i>Biofarm</i>	Romania	36,26	6,53	8,90	24,63	8,42
<i>Pliva</i>	Croatia	40,05	2,35	2,43	12,89	2,56
<i>Zentiva N.V.</i>	Czech Rep.	20,95	4,70	3,12	12,40	3,38
<i>Sanitas</i>	Lithuania	112,75	51,71	3,59	17,97	4,70
<i>Verofarm OAO</i>	Russia	23,02	5,69	4,21	15,59	4,39
Pharmaceuticals - Diversified						
<i>Antibiotice</i>	Romania	29,17	4,30	3,97	18,57	3,96
<i>EGIS Nyrt</i>	Hungary	21,98	1,70	1,52	10,40	1,43
<i>Richter Gedeon Vegyeszeti Gyar</i>	Hungary	17,95	2,40	3,18	9,91	2,98
<i>Grindeks</i>	Lithuania	11,58	2,17	1,58	8,33	1,73

Source: Reuters

Peers Comparison – Profitability Ratios

When comparing to Sopharma, the pharmaceutical companies in Central and Eastern Europe have better profit margins on average on ttm basis. 25% EBITDA margin is usual for generic producers. Sopharma is one step behind as the wholesale operations usually have lower margins. We can expect further improvement for Sopharma but slowly due to the low medicine prices in Bulgaria.

		RoA	RoE	EBITDA margin	EBIT margin	Net margin	Estimate P/E
Pharmaceuticals - Generic							
<i>Biofarm</i>	Romania	16,90%	19,88%	34,18%	27,22%	24,53%	32,78
<i>Pliva</i>	Croatia	5,84%	8,08%	19,88%	11,91%	9,06%	n/a
<i>Zentiva N.V.</i>	Czech Rep.	8,94%	19,41%	27,26%	21,50%	15,74%	20,41
<i>Sanitas</i>	Lithuania	1,31%	2,80%	26,13%	11,64%	3,27%	n/a
<i>Verofarm OAO</i>	Russia	16,75%	24,56%	28,19%	25,16%	18,27%	16,48
Pharmaceuticals - Diversified							
<i>Antibiotice</i>	Romania	11,04%	16,31%	21,34%	16,66%	13,62%	35,77
<i>EGIS Nyrt</i>	Hungary	6,91%	7,94%	13,77%	7,74%	6,92%	22,19
<i>Richter Gedeon Vegyeszeti Gyar</i>	Hungary	12,26%	13,70%	30,02%	20,88%	17,98%	17,98
<i>Grindeks</i>	Lithuania	13,72%	20,42%	20,74%	17,41%	13,74%	10,74

Source: Reuters

5Y Projections

As a result of gradually improved margins, we expect solid improvement of net profits. Our estimations for sales are based on solid export growth, which is currently the driving force behind the increased revenues. However, domestic sales growth will speed up in later stage.

	2006	2007	2008	2009	2010	2011
Sales	223 393	301 581	361 897	416 182	478 609	526 470
Growth		35,00%	20,00%	15,00%	15,00%	10,00%
Net margin	11,75%	13,00%	14,00%	15,00%	16,00%	17,50%
Net Profit	26 259	39 206	50 666	62 427	76 577	92 132
Growth		49,31%	29,23%	23,21%	22,67%	20,31%

Estimated data for 2007-2011;
Calculations: ELANA Trading

Price Target

The one year target for Sopharma shares is BGN 9.73. We stick to P/E 30, which is close to the average for Bulgarian liquid stocks. However, the market tends to give additional premium for stocks with growing sales and profits. The P/S ratio is good indicator as peers are traded 3 to 4 times their revenues. We took the same for Sopharma, despite the turnover of Sopharma Trading. The P/B of 5 is showing a price that lag behind the other two ratios, mainly due to the dividends that Sopharma pays.

BGN'000	2007	2Q 2008	2008
Sales	301 581	358 882	416 182
Net Profit	39 206	44 936	50 666
Equity	218 451	249 754	281 056
Expected P/E	30	30	30
Price Target	8,91	10,21	11,52
Expected P/S	3,50	3,50	3,50
Price Target	8,00	9,52	11,04
Expected P/B	5,00	5,00	5,00
Price Target	8,27	9,46	10,65
Average Target	8,39	9,73	11,07

Calculations: ELANA Trading

Recommendation

We give *Market Perform* recommendation of Sopharma. The one year price target is BGN 9.73 but in the light of current market euphoria in Bulgaria it is more probable that investors will pursue higher price – P/E of 30 to 35 times the net profit for 2H 2007 and 1H 2008. This is the reason to expect prices at BGN 10.21, or possibly above BGN 11 in one year horizon. The expected return for the next 12 months is 22% (price target of BGN 9.73) or 28% (P/E 30).

Bulgarian stock market posted solid growth for the last twelve months due to the abundant liquidity. Although all reasons behind another 50-100% next year are present, we expect the increase to slow down to more reasonable pace. That's why the expected 25-30% gains of Sopharma should be consistent to the broad market performance. In addition, possible surprises are on the upside.

Financial Data

Consol. Statement of Income (in thousand BGN)	2002	2003	2004	2005	2006
Sales	121 725	100 429	107 492	131 993	223 393
Production expenses	72 500	53 161	61 363	64 784	156 793
Personnel expenses	14 749	14 941	16 462	20 162	25 005
Net income from financial activities	(2 505)	(3 002)	5 101	6 652	3 309
Other revenues and expenses	0	0	0	0	0
EBITDA	31 971	29 325	34 768	53 699	44 904
Depreciation	9 649	6 953	5 739	6 379	7 705
EBIT	22 322	22 372	29 029	47 320	37 199
Interest expense	(3 038)	(2 606)	(2 758)	(2 959)	(5 511)
Pretax income	19 284	19 766	26 271	44 361	31 688
Taxes	5 477	4 125	5 410	8 363	4 552
After-tax income	13 807	15 641	20 861	35 998	27 136
Minority interest	1 665	123	529	830	877
Net income	12 142	15 518	20 332	35 168	26 259
Earnings per share in BGN	2,02	0,24	0,31	0,53	0,20

Consol. Balance Sheet (in thousand BGN)	2002	2003	2004	2005	2006
Total Assets	194 183	197 514	246 649	317 521	371 515
Equity subscriptions receivable	0	0	0	0	0
Fixed assets	104 131	109 436	127 934	160 520	142 093
Tangible fixed assets	40 563	48 222	71 508	88 003	115 484
Financial investments	1 258	9	9	9	4 659
Current assets	90 052	88 078	118 715	157 001	229 422
Inventory	31 192	36 078	33 591	39 225	85 742
Receivables	44 552	48 297	78 366	104 968	129 617
Financial assets and cash	10 572	3 703	6 758	12 808	13 822
Total liabilities + equity	194 183	197 514	246 649	317 521	371 515
Equity	142 112	142 898	160 799	183 790	199 245
Registered capital	6 000	66 000	66 000	66 000	132 000
Capital funds	118 820	20 713	27 933	29 940	36 748
Earnings	17 292	56 185	66 866	87 850	30 497
Liabilities	52 071	53 935	84 121	133 370	171 909
Long-term payables	17 765	8 612	7 672	17 414	6 314
Long-term bank loans	16 688	19 167	41 690	48 980	33 929
Short-term bank debt	1 732	6 280	6 348	32 994	50 128
Short-term payables	15 886	19 876	28 411	33 982	76 581
Other liabilities	0	0	0	0	0
Working capital	72 434	61 922	83 956	90 025	102 713

Consol. Cash Flow Statement (in thousand BGN)	2002	2003	2004	2005	2006
Net income	12 142	15 518	20 332	35 168	26 259
Depreciation	9 649	6 953	5 739	6 379	7 705
Changes in Working capital	10 683	(10 512)	22 034	6 069	12 688
Other operating cash flow items	(19 788)	6 562	(52 567)	(52 377)	(18 697)
Net cash from operating activities	12 686	18 521	(4 462)	(4 761)	27 955
Capital expenditures	(20 346)	(11 324)	(15 467)	(12 200)	(20 379)
Other investing cash flow items	430	(17 224)	5 702	(17 695)	16 805
Net cash from investing activities	(19 916)	(28 548)	(9 765)	(29 895)	(3 574)
Issuance/ Retirement of Stock, Net	0	11	0	1 461	4 615
Issuance/ Retirement of Debt, Net	5 911	5 969	25 198	42 612	18 508
Dividends paid	0	0	(5 804)	(407)	(4 686)
Other financing cash flow items	(3 038)	(3 375)	(2 137)	(2 960)	(40 370)
Net cash from financing activities	2 873	2 605	17 257	40 706	(21 933)
Net change in cash	(4 357)	(7 422)	3 030	6 050	2 448
Beginning-of-period cash	15 482	11 125	3 728	6 758	12 808
End-of-period cash	11 125	3 703	6 758	12 808	15 256
Cash per share	1,85	0,06	0,10	0,19	0,12

Number of shares:	6 000 000	66 000 000	66 000 000	66 000 000	132 000 000
Price in BGN - period end:	12,04	3,33	4,62	7,50	6,90
Market cap in BGN (period end)	72 240 000	219 780 000	304 920 000	495 000 000	910 800 000

Financial and Performance Indicators	2002	2003	2004	2005	2006
Valuation Ratios					
Price/Earnings (P/E)	5,95	14,16	15,00	14,08	34,69
Book Value	23,69	2,17	2,44	2,78	1,51
Price/Book (P/B)	0,51	1,54	1,90	2,69	4,57
Sales Per Share	20,29	1,52	1,63	2,00	1,69
Price/Sales (P/S)	0,59	2,19	2,84	3,75	4,08
Price/Cash flow	3,32	9,78	11,70	11,91	26,82
EV (in thousand BGN)	85 789	247 662	359 518	591 579	1 006 365
EV/Sales	0,70	2,47	3,34	4,48	4,50
EV/EBITDA	2,68	8,45	10,34	11,02	22,41
EV/EBIT	3,84	11,07	12,38	12,50	27,05
Liquidity					
Current ratio	5,11	3,37	3,42	2,34	1,81
Quick ratio	3,34	1,99	2,45	1,76	1,13
Debt Management					
Debt to total assets	26,8%	27,3%	34,1%	42,0%	46,3%
Interest coverage	7,35	8,58	10,53	15,99	6,75
LT Debt/Equity	24,2%	19,4%	30,7%	36,1%	20,2%
Total Debt/Equity	36,6%	37,7%	52,3%	72,6%	86,3%
Asset Management					
Inventory turnover	3,90	2,78	3,20	3,37	2,61
Days sales outstanding	132	173	262	286	209
Fixed asset turnover	1,17	0,92	0,84	0,82	1,57
Total asset turnover	0,63	0,51	0,44	0,42	0,60
Profitability					
Profit margin on sales	10,0%	15,5%	18,9%	26,6%	11,8%
EBITDA Margin	26,3%	29,2%	32,3%	40,7%	20,1%
Basic earning power	11,5%	11,3%	11,8%	14,9%	10,0%
Return on assets	6,3%	7,9%	8,2%	11,1%	7,1%
Return on equity	8,5%	10,9%	12,6%	19,1%	13,2%
Return on investments	6,9%	9,1%	9,7%	14,1%	11,0%
Dividend Information					
Dividend Yield	n/a	2,7%	3,9%	3,9%	1,4%
Dividend per share (in BGN)	0,00	0,09	0,18	0,29	0,10
<i>* Valuation and profitability ratios are calculated on ttm basis. Other ratios are estimate for the most recent quarter.</i>					
Number of shares:	6 000 000	66 000 000	66 000 000	66 000 000	132 000 000
Price in BGN - period end:	12,04	3,33	4,62	7,50	6,90
Market cap in BGN (period end)	72 240 000	219 780 000	304 920 000	495 000 000	910 800 000

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Valuation Methods: Company valuations are based on the following methods: multiple-based (P/E, P/B, EV/EBITDA), historical valuation approaches, peer comparisons, discount models (DCF, DDM) or asset-based evaluation methods. Valuation models are dependent on macroeconomic factors, including interest rates, foreign exchange rates, prices of raw materials, and any expectations about the economy, the market sentiment. The valuation is based on expectations that might change rapidly and without notice, depending on developments specific to individual industries and countries. Recommendations and target prices derived from the models might therefore change accordingly. The application of models depends on forecasts of a range of economic variables, thus there is a range of reasonable variations within models. Any valuation is dependent upon inputs that are based on the subjective opinion of the analysts carrying out this valuation.

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Positive	More than 5% higher as compared to SOFIX and BG40 performance
Neutral	Market performance, +/-5% as compared to SOFIX and BG40
Negative	More than 5% lower as compared to SOFIX and BG40 performance

Frequency of Recommendations: No schedule of recommendations is available. The frequency of recommendations depends on specific factors to individual companies and the opinion of the analyst(s) for the necessity of minor or major changes.