

## 20. BULGARIA

### Moderate growth ahead

*Economic growth in Bulgaria is set to slow and remain close to potential. Despite weak external demand and elevated uncertainty abroad, domestic demand dynamics should underpin growth. Exports are forecast to grow at a modest rate, in line with foreign demand prospects. Inflation is set to decline, as temporary factors fade away and oil prices decline further. The government balance is set to remain in surplus and public debt to continue falling.*

#### Moderate GDP growth ahead

Following real GDP growth of just over 3% in 2018, growth dynamics remained strong in the first half of 2019, registering 1.1% in the first quarter and 0.9% in the second (q-o-q). Private consumption contributed strongly to the overall expansion on the back of rapid wage growth and high employment. Investment in machinery and equipment performed strongly, supported by favourable financing conditions and buoyant public investment activity. Aggregate investment, however, grew more moderately due to underperformance of other investment components.

Exports maintained positive annual growth in the first quarter, continuing the favourable trend from the second half of 2018. However, as external demand has continued to falter, exports declined in the second quarter and became more volatile. Imports contracted sharply in the second quarter due to an abrupt drop in imports of crude oil, as inventories were run down.

Real GDP growth is forecast to reach 3.6% in 2019, and then slow down to 3% in 2020 and 2.9% in 2021. Exports are set to register small negative growth in 2019 and regain modest growth rates ahead, in line with foreign demand developments. Domestic demand is expected to continue to lose some growth momentum, but remain the main growth driver. A limited room for further improvement in employment is set to weigh on household consumption dynamics while real wage increases support private spending. In 2019 aggregate investment should posit only modest expansion due to the relatively subdued performance in the first half of the year. In the next two years investment is expected to regain some momentum but grow at a moderate pace, against the backdrop of elevated economic uncertainty abroad and somewhat worsened growth prospects.

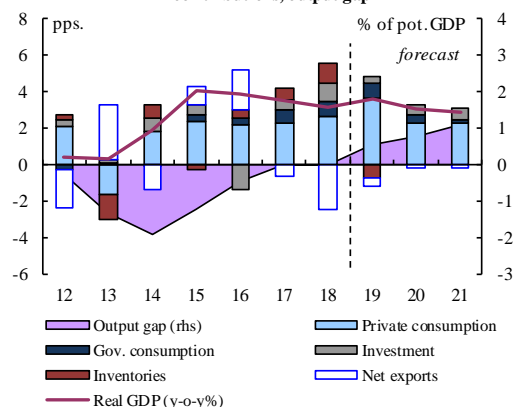
Risks to the forecast are mainly on the downside, associated with a potential sharp and protracted

deterioration of external demand from the major trading partners and second-round effects through higher unemployment and lower domestic demand.

#### Temporary factors influence inflation

Annual headline inflation is forecast at 2.4% in 2019. Price dynamics have been volatile since the beginning of the year, accelerating to 3.1% in April and declining to 1.6% in September. Food prices have contributed strongly to inflation, influenced by the poor harvest in 2018 and the spread of African swine fever beginning in May 2019. Energy inflation was influenced upwards by electricity price hikes in the middle of the year and downwards by lower petrol prices in the second half of the year. Services inflation outpaced that of total goods on the back of strong wage growth and factors specific to catering services, such as more pronounced seasonality and higher prices of food. Owing to the gradual fading of temporary factors and the further decline in oil prices, inflation is set to decrease to 1.6% in 2020 and increase again to 2.1% in 2021.

Graph II.20.1: Bulgaria - Real GDP growth and contributions, output gap



#### Unemployment falls to historic lows

The unemployment rate is expected to fall to 4.4% in 2019, down from 5.2% in 2018. Over the following two years it is set to drop further to 4.1% and 4.0%, respectively. The employment gains

forecast for 2019 are likely to stall in 2020 and to turn negative in 2021 due to Bulgaria's shrinking labour force. Real wages are forecast to increase strongly in 2019, owing to the historically low unemployment turnout and planned minimum and public sector wage increases. Wage growth is expected to remain strong in 2020 and 2021, although likely to moderate compared to this year.

### Sustained budget surpluses

The general government surplus, is forecast at 1.1% of GDP in 2019, lower than in 2018. Budget revenue is set to strengthen further this year mainly thanks to strong social contributions and revenues from electricity fees. Government expenditure, however, seems to be rising faster than revenues. This is mainly due to increases in some current expenditure categories such as wages and social expenditure, as well as an expected pickup in public investment.

The budget balance is expected to remain positive during the forecast period. Revenue collection is projected to remain strong, in line with macroeconomic and labour market developments.

Wage increases in the public sector, which have been announced for 2020 and high public investment as a result of both national and EU-financed projects will fuel an increase in total spending. The budget surplus is thus expected to reduce to 0.9% of GDP in 2020 and remain at the same level in 2021.

The budgetary forecast is subject to upside risks. The public investment plans remain ambitious. At the same time, revenue collection seems to have gained some momentum and may continue to exceed expectations in the coming years.

In structural terms, the budget surplus is set to drop from 1<sup>2</sup>/<sub>3</sub>% of GDP in 2018 to around 1% of GDP in 2019 and further reduce during 2020 and 2021, reflecting the changes in the headline balance and the positive and increasing output gap. Interest spending is decreasing. On the other hand, the government plans some pre-financing of its medium term debt, so the pace at which Bulgaria's public debt is set to fall is likely to slow despite the primary surplus. The public debt-to-GDP ratio is projected to fall from 22.3% in 2018, to 21.1% in 2019, 19.9% in 2020 and 18.6% in 2021.

Table II.20.1:

### Main features of country forecast - BULGARIA

	2018			Annual percentage change						
	bn BGN	Curr. prices	% GDP	00-15	2016	2017	2018	2019	2020	2021
GDP	109.7	100.0		3.6	3.8	3.5	3.1	3.6	3.0	2.9
Private Consumption	65.5	59.7		4.6	3.5	3.8	4.4	6.1	3.8	3.7
Public Consumption	18.0	16.5		1.4	2.2	4.3	5.3	4.8	2.6	1.4
Gross fixed capital formation	20.6	18.8		6.4	-6.6	3.2	5.4	1.8	3.0	3.3
of which: equipment	8.5	7.7		7.1	-14.8	4.4	8.8	13.5	3.1	3.1
Exports (goods and services)	72.2	65.9		5.5	8.6	5.8	1.7	-0.2	3.2	3.2
Imports (goods and services)	69.4	63.3		6.6	5.2	7.4	5.7	0.5	3.8	3.7
GNI (GDP deflator)	110.6	100.9		3.6	5.6	5.1	2.6	3.5	3.0	2.7
Contribution to GDP growth:		Domestic demand		4.8	1.1	3.6	4.4	4.8	3.2	3.0
		Inventories		-0.1	0.4	0.6	1.1	-0.7	0.0	0.0
		Net exports		-1.0	2.2	-0.7	-2.4	-0.5	-0.2	-0.2
Employment				0.2	0.5	1.8	-0.1	0.6	0.0	-0.2
Unemployment rate (a)				11.6	7.6	6.2	5.2	4.4	4.1	4.0
Compensation of employees / head				8.5	5.8	10.5	9.7	7.8	6.6	5.4
Unit labour costs whole economy				5.0	2.4	8.7	6.3	4.7	3.5	2.3
Real unit labour cost				0.4	-0.1	4.5	2.2	0.1	0.5	-0.3
Saving rate of households (b)				-	-	-	-	-	-	-
GDP deflator				4.5	2.5	3.9	4.0	4.5	3.0	2.6
Harmonised index of consumer prices				4.6	-1.3	1.2	2.6	2.4	1.6	2.1
Terms of trade goods				-0.4	3.9	0.3	0.7	1.9	0.7	0.5
Trade balance (goods) (c)				-15.0	-2.1	-1.5	-3.3	-2.9	-2.9	-2.9
Current-account balance (c)				-6.5	5.3	6.1	4.6	5.5	5.5	5.4
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-5.7	7.3	7.1	5.7	6.7	6.8	6.7
General government balance (c)				-0.7	0.1	1.1	1.8	1.1	0.9	0.9
Cyclically-adjusted budget balance (d)				-0.6	0.2	1.1	1.8	1.0	0.6	0.6
Structural budget balance (d)				-	0.2	1.1	1.8	1.0	0.6	0.6
General government gross debt (c)				29.6	29.3	25.3	22.3	21.1	19.9	18.6

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.

Note: Contributions to GDP growth may not add up due to statistical discrepancies.