

## 20. BULGARIA

*Bulgaria's economy started to recover after a steep downturn in the second quarter and is expected to continue expanding. Domestic demand and exports are set to contribute to growth. After an initial surge, unemployment had stabilised, partially due to the publically financed employment retention measures. Budget deficits have returned after four years to support employment and incomes.*

### Sharp recession and a gradual recovery

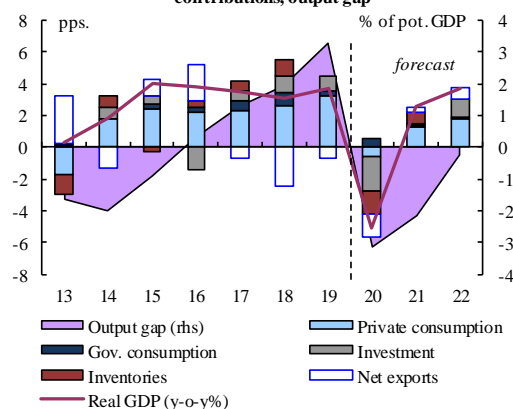
Economic developments in Bulgaria have been marked by the adverse impact of the COVID-19 pandemic. Containment measures negatively affected supply in sectors directly subject to them. The disposable income of households took a hit and the restrictions led to a higher saving rate. Nevertheless, the decline in consumer spending was curbed by continued wage increases and the relatively low weight in consumption of most affected services. Lower employment and subdued consumer confidence, related to the second wave the pandemic, are set to weigh on private consumption, while the government's anti-crisis measures are expected to support private income.

Investment activity declined markedly in the first half of 2020. The reduced actual and expected business activity, combined with higher uncertainty, prompted companies to postpone investment plans. As these factors are assumed to remain in place throughout 2020, subdued investment is likely to persist.

Goods exports began to fall sharply in March 2020. Signs of recovery in exports to EU markets have been registered since May 2020, but exports to third countries have not improved. Travel services came to a halt during the period April-June and the flows have improved only slightly since then. The second wave of the pandemic is set to weigh on the rebound of exports in 2020-Q4 and 2021-Q1.

The economic recovery is projected to bring the economy back to pre-crisis levels by the end of 2022. Both exports and consumption are set to contribute positively to the expansion in the next two years, in line with positive external demand and labour market developments. In 2021 investment activity is forecast to recover only gradually on account of still high uncertainty. With investment growing strongly in 2022 on the back of the improved cyclical position, economic growth is expected to be driven primarily by domestic demand.

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



The risks to the forecast are broadly balanced. As the it does not take into account the implementation of the Recovery and Resilience Plan, an upside risk to public investment emerges. On the downside, more depressed business sentiments could lead to lower investment in the next two years.

### Labour market continues to slowly stabilise

The unemployment rate has increased significantly since the onset of the COVID-19 pandemic. The government's job retention scheme has helped to limit job losses by enabling a downward adjustment in average hours worked. The largest share of job losses was recorded in the accommodation and food services sectors. As some dismissed workers did not start looking for a job immediately, inactivity rates went up. After a sharp increase in the first half of the year, the unemployment rate is expected to level off at 5.8% in 2020. A partial recovery in employment is projected to take place in 2021 and the unemployment rate is set to reach 5.6%. Despite worsened labour market conditions, compensation per employee is projected to remain on an upwards trajectory, albeit at a more moderate pace. This is in part driven by public sector wage increases, as well as increases in minimum wage and minimum insurance thresholds.

### Services prices to determine headline inflation

HICP inflation has been on a downward path since the beginning of the year due to lower fuel prices. Inflation is expected to fall to 1.2% in 2020 and then gradually increase to 1.4% in 2021 and 1.8% in 2022. In the next two years inflation will be driven mainly by services inflation, continuing the upward trend in recent years.

### Fiscal expansion to support incomes

Bulgaria is facing the COVID-19 pandemic from a strong fiscal position and the government has put in place measures such as higher remuneration for medical and security staff, subsidies and social support schemes, with an aggregate budgetary impact of around 2% of GDP. Despite the measures and the deteriorating economic outlook, the budget in cash terms remained in surplus for about two thirds of the year. The accrual general government balance is set to turn negative reaching around -3% of GDP by the end of 2020.

In 2021, the budget deficit is forecast at around 3% of GDP. The recovery will have a positive impact on revenues, but a number of expenditure measures to preserve jobs and support incomes through wage increases and social benefits will have a negative impact in 2021 deficit. Under a no-policy-change assumption, the budget deficit is set to drop to around 1½% of GDP in 2022, mainly due to the withdrawal of emergency measures. This forecast does not include any measures funded by the Recovery and Resilience Fund.

General government debt is expected to increase by more than 5 pps. and reach over 25¾% of GDP in 2020 and 26.5% of GDP in 2021, before returning to a downward trend in 2022. Except for the primary deficit and the contraction in GDP, debt increase also reflects some precautionary borrowing of the government according to the new debt ceilings established by the budget amendment last summer in view of the emergency situation.

Table II.20.1:

### Main features of country forecast - BULGARIA

	2019			Annual percentage change						
	bn BGN	Curr. prices	% GDP	01-16	2017	2018	2019	2020	2021	2022
GDP	119.8	100.0		3.6	3.5	3.1	3.7	-5.1	2.6	3.7
Private Consumption	70.5	58.9		4.3	3.8	4.4	5.5	-1.0	2.1	3.0
Public Consumption	20.1	16.8		1.4	4.3	5.3	2.0	3.2	0.4	0.3
Gross fixed capital formation	22.4	18.7		4.9	3.2	5.4	4.5	-11.5	0.5	7.0
of which: equipment	10.0	8.4		5.1	4.4	8.8	15.1	-12.8	0.0	8.1
Exports (goods and services)	76.9	64.2		7.3	5.8	1.7	3.9	-13.3	5.0	8.2
Imports (goods and services)	73.0	61.0		7.6	7.4	5.7	5.2	-11.6	4.5	7.3
GNI (GDP deflator)	120.9	101.0		3.7	5.1	2.7	3.7	-5.3	2.6	3.7
Contribution to GDP growth:										
Domestic demand				4.3	3.6	4.5	4.4	-2.2	1.5	3.0
Inventories				0.0	0.6	1.1	0.0	-1.4	0.8	0.0
Net exports				-0.7	-0.7	-2.5	-0.7	-1.5	0.3	0.7
Employment				0.4	1.8	-0.1	0.3	-2.9	0.5	1.0
Unemployment rate (a)				11.1	6.2	5.2	4.2	5.8	5.6	5.0
Compensation of employees / head				8.3	10.5	9.7	6.9	4.7	4.7	4.0
Unit labour costs whole economy				5.0	8.7	6.3	3.5	7.2	2.6	1.3
Real unit labour cost				0.7	4.6	2.2	-1.7	5.8	-0.2	-0.8
Saving rate of households (b)				-	-	-	-	-	-	-
GDP deflator				4.2	3.9	4.0	5.3	1.4	2.8	2.1
Harmonised index of consumer prices				3.8	1.2	2.6	2.5	1.2	1.4	1.8
Terms of trade goods				1.4	0.3	0.7	1.9	0.0	0.5	-0.4
Trade balance (goods) (c)				-14.1	-1.5	-4.8	-4.7	-2.9	-2.0	-2.2
Current-account balance (c)				-5.9	6.1	4.6	5.2	3.5	4.0	4.4
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-4.9	7.1	5.7	6.4	4.9	5.4	5.9
General government balance (c)				-0.6	1.1	2.0	1.9	-3.0	-3.0	-1.4
Cyclically-adjusted budget balance (d)				-0.6	0.7	1.4	1.0	-2.0	-2.4	-1.3
Structural budget balance (d)				-	0.7	1.4	1.0	-2.0	-2.4	-1.3
General government gross debt (c)				27.0	25.3	22.3	20.2	25.7	26.4	26.3

(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.