Bulgaria

Country note, June 2017

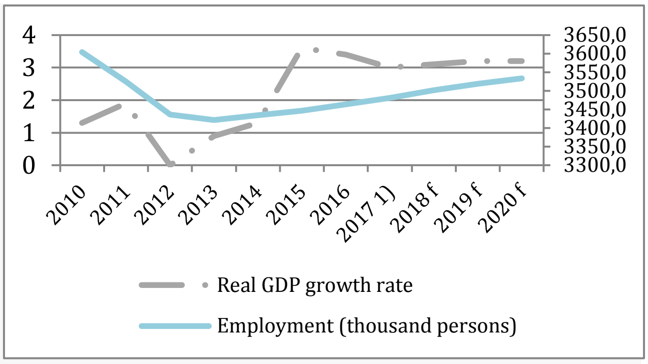
Fiscal Council of Bulgaria

Key messages:

- **The Bulgarian economy is recovering, and the GDP growth in 3.1% in 2017 is achievable, after having in first quarter a 3.5% .**
- **The Budget was balanced for 2016, for the first time after 2008, due to very good revenue performance, and low absorption of capital expenditures**
- **Because of some structural issues and economic cycle, surplus in 1% of GDP as target in middle run will be very welcomed**
- **The Structural reforms, absorption of EU funds and improving the efficiency of expenditures are crucial for the next years, for achieving the government fiscal targets and longrun sustainability**

Macroeconomic outlook

The economic recovery observed since 2014 has resulted in economic growth of 3,6 % of GDP in 2015 and 3,4 % of GDP in 2016. While the recovery in 2015 was largely driven by the growth of the government investments backed up by the export, the marked economic growth in 2016 was mainly due to the stable export supported by recovering labor market. The GDP growth for the first quarter of 2017 amounted to 3,5% and validates the expected over the three-percentage growth of GDP on an annual basis. Employment is recovering slowly, despite the significant demand for skilled labor. There are signs of "overheating" on the labor market at an unconventionally low level of employment of around 66-67%. Wage growth is above a two-digit figure despite deflation of the past 2 years. Inflation (CPI) since the beginning of the year has amounted to 1.2%. The mid-term risks and challenges to the economy remain the labor market, the attracting of more direct foreign investments and the development of the economies of the major economic partners.

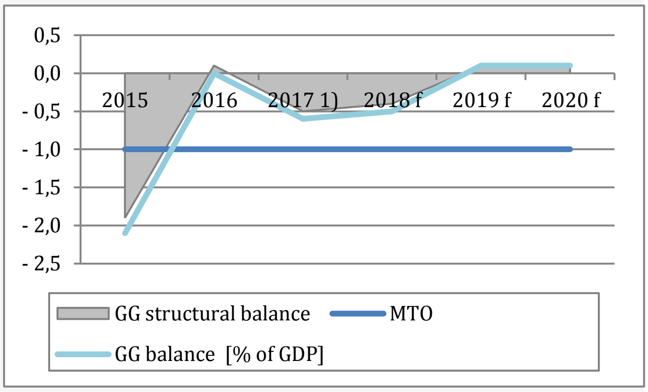


Short-term fiscal outlook

After a balanced general government budget in 2016, in 2017 the Government set on loose fiscal policy with expected budget deficit amounted to -0.6% of GDP as a result of higher social spending and higher investments. For the first 4 months of the year, the general government budget is running in surplus, following the same budget implementation profile in 2016. Tax revenues grew by nearly 9% over the same period of the previous year and total revenues are at the same level, following the poor absorption and re-allocation of European funds. Regarding the expenditures, an increase estimated at 7% was marked, compared to the same month of the previous year as well as almost 10% lower absorption of the capital expenditures. This trend is not disturbing, and the expected fiscal target for 2017 is easily achievable.

Medium-term fiscal outlook

The Medium Term Objective is a budget balance surplus, which the Government expects to achieve in 2019 and 2020. Despite the high expectations of better implementation, the revenue forecast is relatively conservative. The main risk is related to the EU funds revenues, which represent a significant part of the revenue and expenditure side of the consolidated budget. The main budget challenges are related to the expenditures, where the Government has introduced new social and income policies. An improvement of the cost efficiency and capital cost planning need to be presented, which could be a major issue in the medium term outlook. Despite the flexibility reduction of the budgetary expenditures, compared to prior period, they continue providing confidence in achieving the main fiscal aims. The low public debt ratio, estimated under 30% of GDP, provides comfort for manoeuvrability in managing the budget.
BFC is of the opinion, that the fiscal framework could be more ambitious, achieving the GG balance of 1% of GDP in 2020, considering the geopolitical challenges as well as the development of the economic cycle where hopes are towards closing the output gap by 2020.



Fiscal framework and national fiscal rules

In 2016 for the first time since 2009, Budget has met the MTO target, with GG structural balance amounted to 0.1% of GDP. Despite the weak loosening of fiscal policy in 2017, the structural deficit remains below the MTO's target and continues to improve in the years to come. Following the changes in the methodology, the expenditure benchmark is positive and Bulgaria does not violate the rule. Given the projections of reducing the public debt ratio from 29,5% of GDP to 24% in 2020, the Government expects to cover that rule as well.

Key indicator forecast

		2015	2016	2017 1)	2018 f	2019 f	2020 f
Real GDP growth rate	[% y-to-y]	3,60	3,40	3,00	3,10	3,20	3,20
Output Gap	[% of GDP]	-0,40	-0,30	-0,30	-0,20	-0,10	0,10
GG balance	[% of GDP]	-2,10	0,00	-0,60	-0,50	0,10	0,10
GG debt	[% of GDP]	26,70	29,50	26,40	25,60	25,10	23,80
GG structural balance	[% of GDP]	-1,90	0,10	-0,50	-0,40	0,10	0,10
MTO	[% of GDP]	-1,00	-1,00	-1,00	-1,00	-1,00	-1,00
Discretionary revenue measures	[% of GDP]	0,20	0,30	0,60	0,60	0,20	0,20

Sources: National Statistical Institute

Convergency programme of the Ministry of finance 2017-2020

f - forecast

1) estimates base on 1 qtr.