2. BULGARIA
Strong growth ahead

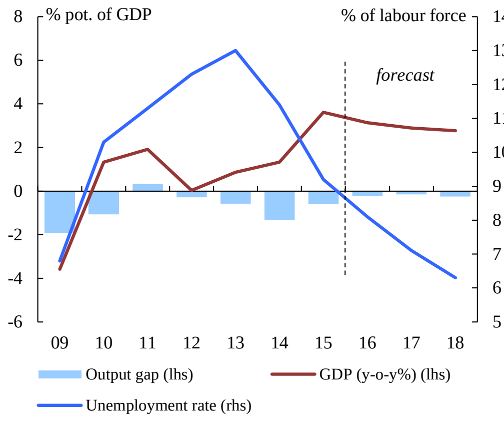
After a strong performance in 2015 and in the first half of this year, real GDP growth is forecast to reach 3.1% in 2016 and then just slightly less over the forecast horizon. Private consumption is expected to be the key growth driver. While remaining negative in 2016, inflation is forecast to move into positive territory in 2017. Unemployment is expected to continue decreasing in the coming years. The fiscal deficit for 2016 is projected at 0.9% of GDP, but is forecast to marginally increase in 2017.

Strong performance of private consumption

A substantial revision of national accounts data lifted real GDP growth figures from 3.0% to 3.6% in 2015. Private consumption growth, driven by rising consumer confidence, was particularly buoyant in 2015 at 4.5%.

GDP growth is projected at 3.1% in 2016 followed by a slight decrease to 2.9% and 2.8% in 2017 and 2018, respectively. For 2016, domestic demand is expected to contribute 2 pps. to real GDP growth with net exports contributing 1.1pps. While private consumption growth is forecast to remain robust at 3.2% in 2016, investment is expected to contract by 0.8% due to the slowdown in EU funds absorption following the completion of the 2007-2013 programming period. Investment is forecast to pick up momentum with growth of 3.2% in 2017, as more projects co-financed by the EU under the new, 2014-2020 programme, are likely to be implemented in 2017.

Graph II.2.1: **Bulgaria - Real GDP growth, output gap and unemployment**



The overall strength of GDP growth in Bulgaria is expected to further reduce the economy's output gap from -0.6% in 2015 to -0.2% in 2016. However, the output gap is projected not to fully close over the forecast horizon.

Overall, risks to the growth outlook appear balanced. Upside risks on the domestic front include better-than-expected private consumption growth. However, as a domestic downside risk, a significantly slower absorption of EU funds could dent investment and growth in 2017. Given the openness of the economy, weak import demand from the main trading partners, especially in Europe, and surging oil prices would pose external downside risks.

Positive but declining current account balance

Driven by stable demand from EU trading partners as well as a strong tourism season, Bulgaria's exports have been performing well in 2016. The current account balance is forecast at 2% of GDP this year and is expected to decline to 1% in 2017 and 0.6% in 2018, mainly due to higher import growth fuelled by a strong domestic demand and by the expected rise in energy import costs.

The end of deflation in 2017

While annual HIPC inflation is forecast to be negative in 2016 at -0.9%, it is expected to pick up pace to reach 1% in 2017, mainly driven by buoyant domestic demand as well as recovering energy prices.

Further improvement of the unemployment and labour market conditions

Employment growth is projected to increase from 0.4% in 2015 to 0.8% in 2016 and to slightly slow down to 0.7% in 2018. Together with the expected decrease in the labour force due to population ageing and emigration, this is likely to further reduce the unemployment rate to 8.1% in 2016, 7.1% in 2017 and 6.3% in 2018.

Fiscal consolidation likely to continue but contingent liabilities could pose a risk

The public deficit is expected to decrease from 1.7% in 2015 to 0.9% of GDP in 2016 and is forecast to gradually decrease to 0.8% and 0.7% in 2017 and 2018, respectively. The adjustment in 2016 is due to a better-than-expected performance of both revenue and expenditure. Budget revenue benefited from better macroeconomic conditions and some revenue enhancing measures such as increases in excise duties for energy and improvements in the tax control and collection systems, together with some signs of improving tax compliance. On the expenditure side, the improvement is mainly due to lower capital and other current expenditure, as the implementation of the new EU funds programmes has yet to gain momentum.

Revenue performance in 2017 is forecast to continue improving on the back of the positive macroeconomic developments. Under a no-policy-change assumption, expenditure is forecast to increase mainly due to higher capital expenditure most of which would be matched by EU funds. The same trends are expected to drive budget components in 2018.

Contingent liabilities of public and other entities, including the envisaged state aid to the national energy company, pose downside risks to public finances over the entire forecast horizon. Additional risks on the expenditure side include announced plans to increase wages in the public sector. Upside risks may stem from continued improvements in tax collection.

General government debt is expected to increase to 29.4% of GDP in 2016, mainly driven by the decision to temporarily increase cash buffers. It is then forecast to decline to 26.3% of GDP in 2017 and to further reduce to 25.9% of GDP in 2018 as a result of the relatively low primary balance and the improving debt financing conditions. The structural deficit is expected to drop to ¾% of GDP in 2016 and remain below 1% of GDP in both 2017 and 2018.

Table II.2.1:

Main features of country forecast - BULGARIA

	2015			Annual percentage change						
bn BGN	**Curr. prices**	**% GDP**	**97-12**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**
GDP	88.6	100.0	3.0	0.9	1.3	3.6	**3.1**	**2.9**	**2.8**
Private Consumption	55.4	62.5	3.5	-2.5	2.7	4.5	**3.2**	**2.9**	**2.8**
Public Consumption	14.3	16.1	2.9	0.6	0.1	1.4	**1.1**	**1.4**	**1.6**
Gross fixed capital formation	18.6	21.0	12.4	0.3	3.4	2.7	**-0.8**	**3.2**	**3.6**
of which: equipment	8.1	9.2	-	1.2	13.9	9.8	**-0.5**	**5.0**	**3.5**
Exports (goods and services)	56.8	64.1	2.3	9.6	3.1	5.7	**5.0**	**4.5**	**4.6**
Imports (goods and services)	56.6	64.0	6.5	4.3	5.2	5.4	**3.3**	**4.3**	**4.6**
GNI (GDP deflator)	86.8	98.0	3.8	0.0	2.7	2.4	**3.6**	**2.2**	**2.3**
Contribution to GDP growth: Domestic demand			4.7	-1.5	2.5	3.6	**2.0**	**2.7**	**2.7**
Inventories			0.5	-0.8	0.2	-0.1	**0.0**	**0.0**	**0.0**
Net exports			-2.2	3.1	-1.3	0.1	**1.1**	**0.2**	**0.0**
Employment			-0.3	-0.4	0.4	0.4	**0.8**	**0.8**	**0.7**
Unemployment rate (a)			11.7	13.0	11.4	9.2	**8.1**	**7.1**	**6.3**
Compensation of employees / head			27.6	8.8	5.6	5.6	**5.4**	**4.8**	**4.2**
Unit labour costs whole economy			23.5	7.4	4.6	2.3	**3.0**	**2.7**	**2.1**
Real unit labour cost			0.2	8.2	4.1	0.1	**3.2**	**1.6**	**0.6**
Saving rate of households (b)			-	-	-	-	**-**	**-**	**-**
GDP deflator			23.3	-0.7	0.5	2.2	**-0.1**	**1.1**	**1.4**
Harmonised index of consumer prices			-	0.4	-1.6	-1.1	**-0.9**	**1.0**	**1.2**
Terms of trade goods			1.0	-0.8	0.7	0.6	**0.5**	**-0.5**	**0.2**
Trade balance (goods) (c)			-13.7	-7.0	-6.5	-5.8	**-4.7**	**-5.1**	**-5.3**
Current-account balance (c)			-6.1	1.2	0.0	0.4	**2.0**	**1.0**	**0.6**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)			-5.7	2.3	2.2	-1.5	**0.3**	**-0.5**	**-0.8**
General government balance (c)			-0.1	-0.4	-5.5	-1.7	**-0.9**	**-0.8**	**-0.7**
Cyclically-adjusted budget balance (d)			-0.1	-0.2	-5.0	-1.5	**-0.8**	**-0.8**	**-0.6**
Structural budget balance (d)			-	-0.2	-1.8	-1.4	**-0.8**	**-0.8**	**-0.6**
General government gross debt (c)			40.5	17.0	27.0	26.0	**29.4**	**26.3**	**25.9**

(a) as % of total labour force. (b) gross saving divided by 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.