

2. BULGARIA

A balanced budget amid robust growth

Real GDP is expected to grow by 2.9% in 2017 and is forecast to marginally decline in 2018. Domestic demand continues to be the main growth driver over the forecast horizon. Inflation is forecast to turn positive in 2017. Unemployment is expected to continue decreasing in the coming years. A balanced budget was achieved in 2016 mainly due to higher tax revenues and reduced public investment, but a deficit of 0.4% of GDP is forecast in 2017. Risks to the growth outlook are broadly balanced.

Strong domestic demand growth

Real GDP growth remained robust in 2016 at 3.4%, driven by buoyant net exports and private consumption. In contrast, investment growth was significantly negative at -4% in 2016, mainly due to a low absorption of EU funds. Inventories contributed a sizable 1 pp. to growth in 2016.

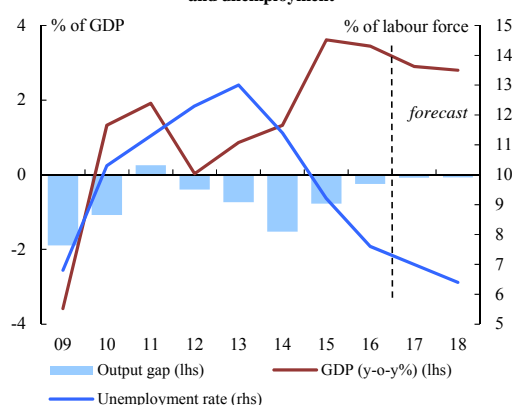
In 2017, real GDP growth is projected to reach 2.9%, as in the winter forecast, and then slightly taper off to 2.8% in 2018. Domestic demand is expected to be the main growth engine, driven in particular by private consumption and investment following the acceleration in EU funds absorption under the 2014-2020 EU programming period. Strong growth has led to a narrowing of the negative output gap in 2016, which is projected at -0.1% in 2017.

Risks to the growth outlook are broadly balanced. As a domestic downside risk, a significantly slower than expected implementation of EU funds could dent investment and growth. Given the openness of the economy, weaker import demand from the main trading partners, especially in Europe, and surging oil prices would pose external downside risks. On the upside, stronger-than-expected consumer confidence and faster progress with reforms could lift real growth rates.

Strong but declining current account balance

Driven by stable demand from its EU trading partners, as well as strong tourism due to favourable geopolitical factors, Bulgaria's exports continued to perform well in 2016. As a result, the current account balance reached 4.2% of GDP in 2016. It is projected to steadily fall to 2.4% in 2017 and 1.8% in 2018, as strong domestic demand and the expected rise in energy prices fuel import growth. In addition, the primary balance is projected to deteriorate in 2017 and 2018, driven by higher dividend payments.

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



Inflation to turn positive in 2017

Bulgaria has experienced deflation since 2013. Following negative annual HIPC inflation also in 2016, inflation is expected to reach 1.3% in 2017 due to strong domestic demand, higher administrative prices for utilities and recovering energy prices.

Unemployment and labour market conditions continue to improve

Employment is projected to rise by 0.6% in 2017 and 2018, mainly supported by the recovery in domestic demand. The gradual increase in employment, together with an expected stagnation in the labour force are likely to reduce the unemployment rate to 7% in 2017.

Balanced budget achieved in 2016

Fiscal consolidation continued at a faster-than-planned pace, outperforming budgetary targets. Following a deficit of 1.6% of GDP in 2015, the general government budget is estimated to have balanced in 2016. In structural terms, this corresponds to an adjustment of 1.5 pps. of GDP.

Fiscal consolidation in 2016 was the result of both revenue increases and expenditure reductions. Public revenue was better than expected as a result of improved tax collection and of revenue enhancing measures such as increases in the rates of excise duties for liquid heating fuels. The good performance of tax revenue partly offset the lower revenue from EU funds. On the expenditure side, the gradual transition to the new cycle of EU fund programming is reflected in lower-than-expected capital and current spending.

The general government deficit is forecast at 0.4% of GDP in 2017. On the revenue side, a positive contribution is expected from the increase in social security contributions, which kicked in at the start of this year, and the expected recovery in the use of EU funds. Total expenditure, however, is projected to grow by a higher rate than revenue, mainly as a result of increases in the public wage bill and public investment. Under a

no-policy-change assumption, a headline deficit of 0.3% of GDP is forecast in 2018. The structural deficit is forecast to remain below ½% of GDP in both 2017 and 2018.

General government debt is estimated to have reached 29.5% of GDP in 2016 due to a temporary increase in cash buffers, which will partly cover debt repayments in 2017. As a result of this prefinancing and the continuous primary surplus, general government debt is forecast to decline in 2017 and to reach 26% of GDP in 2018.

Downside risks to public finances stem from the contingent liabilities of state-owned enterprises (SOEs). An additional positive impact could be expected from ongoing efforts to improve tax collection. The fiscal forecast is subject to uncertainties related to the programme of the newly elected government, which has not been finalised yet.

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	3.4	2.9	2.8
Private Consumption	55.4	62.5		3.5	-2.5	2.7	4.5	2.1	2.7	2.7
Public Consumption	14.3	16.1		2.9	0.6	0.1	1.4	0.6	2.0	2.2
Gross fixed capital formation	18.6	21.0		12.4	0.3	3.4	2.7	-4.0	4.3	3.8
of which: equipment	8.1	9.2		-	1.2	13.9	9.8	-2.0	6.0	4.0
Exports (goods and services)	56.8	64.1		2.3	9.6	3.1	5.7	5.7	4.6	4.8
Imports (goods and services)	56.6	64.0		6.5	4.3	5.2	5.4	2.8	4.7	4.9
GNI (GDP deflator)	86.8	98.0		3.8	0.0	2.7	2.4	4.6	1.9	2.3
Contribution to GDP growth:		Domestic demand		4.7	-1.5	2.5	3.6	0.6	2.8	2.7
		Inventories		0.5	-0.8	0.2	-0.1	1.0	0.0	0.0
		Net exports		-2.2	3.1	-1.3	0.1	1.8	0.1	0.1
Employment				-0.3	-0.4	0.4	0.4	0.5	0.6	0.6
Unemployment rate (a)				11.7	13.0	11.4	9.2	7.6	7.0	6.4
Compensation of employees / head				27.6	8.8	5.6	5.6	3.1	4.9	4.5
Unit labour costs whole economy				23.5	7.4	4.6	2.3	0.2	2.6	2.3
Real unit labour cost				0.2	8.2	4.1	0.1	-0.9	1.6	0.8
Saving rate of households (b)				-	-	-	-	-	-	-
GDP deflator				23.3	-0.7	0.5	2.2	1.1	1.0	1.5
Harmonised index of consumer prices				-	0.4	-1.6	-1.1	-1.3	1.3	1.5
Terms of trade goods				1.0	-0.8	0.7	0.6	1.4	-1.0	0.2
Trade balance (goods) (c)				-13.7	-7.0	-6.5	-5.8	-3.6	-4.2	-4.2
Current-account balance (c)				-6.1	1.2	0.0	0.4	4.2	2.4	1.8
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-5.7	2.3	2.2	2.4	6.1	4.1	3.4
General government balance (c)				-0.1	-0.4	-5.5	-1.6	0.0	-0.4	-0.3
Cyclically-adjusted budget balance (d)				-0.1	-0.1	-5.0	-1.4	0.1	-0.4	-0.3
Structural budget balance (d)				-	-0.1	-1.8	-1.4	0.1	-0.4	-0.3
General government gross debt (c)				40.5	17.0	27.0	26.0	29.5	26.8	26.0

(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.