

Bulgaria

Baa1 stable/BBB positive/BBB positive*

Outlook

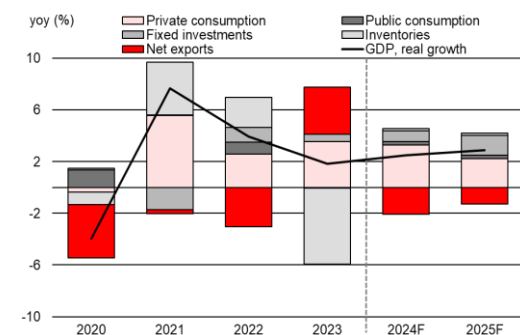
No major shifts in the approval ratings of the main parties have been registered in the month before Bulgaria's snap parliamentary vote. We see two scenarios as equally likely from here. In the positive one, which we assume as our baseline scenario, a pro-European government is formed, which will finalize Bulgaria's eurozone entry and press ahead with structural measures needed to speed up country's modernization. In response, GDP is likely to accelerate in 2025, also underpinned by stronger external demand. Inflation will go down enough for the BNB to request an extraordinary convergence report in February or March 2025, paving the way for eurozone entry on 1 January 2026. Under the negative scenario, a lack of compromise will lead to a new snap parliamentary vote in the beginning of 2025, while support for existing or newly emerged anti-establishment parties could increase. In a worst-case scenario, the new snap vote next year would produce a parliament in which populist and Eurosceptic parties have a majority and form a government. In response, euro adoption could be temporarily scrapped, because the main priority would be to shift the country's geopolitical orientation more toward Russia at the expense of cooperation with western Europe and Euro-Atlantic nations.

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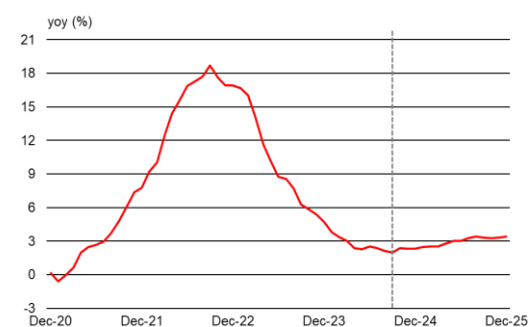
KEY DATES/EVENTS

- 15 October, 15 November, 16 December: CPI
- 18 October: sovereign-rating review by Fitch
- 27 October: parliamentary election
- 14 November, 6 December: 3Q24 GDP (flash, structure)

GDP-GROWTH FORECAST



INFLATION FORECAST



Source: NSI, UniCredit Group Investment Strategy

MACROECONOMIC DATA AND FORECASTS

	2021	2022	2023	2024F	2025F
GDP (EUR bn)	71.1	85.8	93.9	100.0	107.3
Population (mn)	6.5	6.4	6.4	6.4	6.3
GDP per capita (EUR)	10 962	13 307	14 576	15 742	17 139
Real economy, change (%)					
GDP	7.7	3.9	1.8	2.5	2.9
Private consumption	8.5	3.9	5.4	4.8	3.2
Fixed investment	-8.3	6.5	3.3	4.7	8.2
Public consumption	0.4	5.5	-0.4	1.5	1.6
Exports	11.2	11.6	-1.9	1.4	3.0
Imports	10.7	15.0	-6.3	4.1	4.5
Monthly wages, nominal (EUR)	798	905	1 029	1 176	1 279
Real wages, change (%)	9.0	-1.9	4.0	11.8	5.7
Unemployment rate (%)	5.2	4.1	4.3	4.4	4.0
Fiscal accounts (% of GDP)					
Budget balance	-3.9	-2.9	-1.9	-3.0	-3.0
Primary balance	-3.5	-2.5	-1.5	-2.5	-2.4
Public debt	23.4	22.1	22.5	24.6	25.8
External accounts					
Current-account balance (EUR bn)	-1.2	-1.2	-0.3	-0.2	0.6
Current-account balance/GDP (%)	-1.7	-1.4	-0.3	-0.1	0.6
Extended basic balance/GDP (%)	1.1	1.9	4.4	4.6	6.1
Net FDI (% of GDP)	1.8	2.4	3.3	3.2	3.5
Gross foreign debt (% of GDP)	58.1	51.6	48.3	46.1	43.6
FX reserves (EUR bn)	34.6	38.4	41.9	43.9	47.9
Months of imports, goods & services	9.4	7.4	8.8	9.0	9.0
Inflation/monetary/FX					
CPI (pavg.)	3.3	15.3	9.6	2.6	3.0
CPI (eop)	7.8	16.9	4.7	2.3	3.4
LEONIA (eop)	-0.53	1.82	3.80	3.15	2.16
USD-BGN (eop)	1.65	1.86	1.81	1.78	1.73
EUR-BGN (eop)	1.96	1.96	1.96	1.96	1.96
USD-BGN (pavg.)	1.73	1.85	1.80	1.81	1.75
EUR-BGN (pavg.)	1.96	1.96	1.96	1.96	1.96

Source: Eurostat, BNB, NSI, UniCredit Group Investment Strategy

*long-term foreign-currency credit ratings as provided by Moody's, S&P and Fitch, respectively

COMMITMENT TO EUROZONE ENTRY TO FACE ONE MORE TEST

There has not been a major change in support for the main parties in the months leading up to elections on 27 October

The split in the MRF could boost its chances of being called upon to form a government, since the number of feasible coalitions would rise

Voters drifting away from mainstream parties is likely to lose momentum

Euro entry and boosting absorption of RRP funds will remain key priorities

Tax reform is unlikely to be among the immediate priorities

The center-right, pro-European Citizens for European Development of Bulgaria (GERB) is in the lead, according to recent public-opinion polls (see chart). The same polls suggest that the two leading pro-European parties, GERB and the centrist-liberal collation formed by We Continue the Change and Democratic Bulgaria (WCC-DB), are likely to control around 115 MPs in Bulgaria’s 240-seat parliament (see chart). This means that at least one more party is likely to be needed to form a ruling coalition. One possible candidate to join such a ruling collation would be the moderate, national-conservative There Is Such a People party. Another potential candidate would be one of the factions of the recently split, mostly ethnic Turkish party, the Movement for Rights and Freedoms (MRF), provided that both pass the four-percent barrier for parliamentary entry. Although it is less likely, we think it should not be ruled out that the Bulgarian Socialist Party (BSP) could also take part in such a pro-European ruling coalition, especially if it softens its long-held view that euro adoption is a key long-term priority, but Bulgaria is not yet ready to join the eurozone in the short-to-medium term.

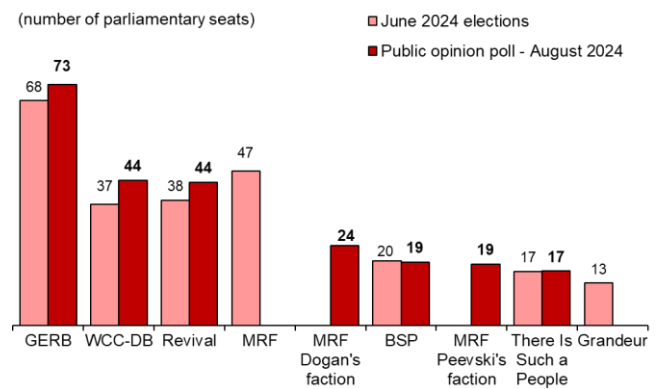
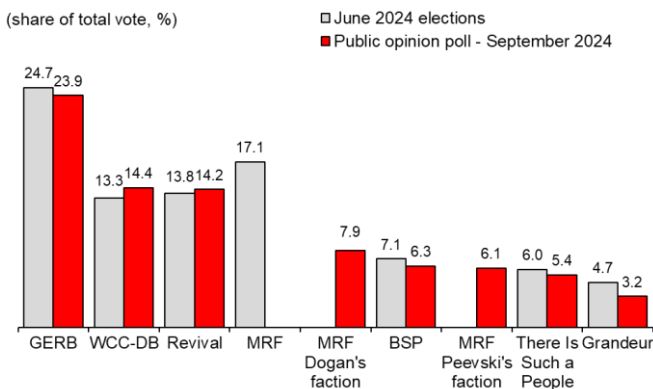
The protest vote is unlikely to rise by much. The far-right, pro-Russian Revival party is set to gain votes, but this will reflect the fall of another party with a similar profile (Grandeur) earlier this year, while the number of ultranationalist voters is likely to stay broadly static. However, Revival’s overtly pro-Putin stance towards the war in Ukraine and use of aggressive rhetoric against opponents are likely to mean that it will be excluded from any coalition talks and kept in isolation, similarly to what has happened since it first entered parliament in October 2022.

We think there are two equally likely scenarios from here. In the positive one, which we assume as our baseline, a pro-European coalition government is formed, and this will end prolonged political instability. Eurozone entry and fulfilling the requirements stipulated in the country’s Recovery and Resilience Plan (RRP) will remain high on the policy agenda of the government. A compromise will have to be reached regarding the next steps to improve public trust in the legal system, including by giving judges and prosecutors a bigger say in the rulings issued by the judiciary. Continuing support for Ukraine in its war against Russia and the push for full membership in the EU’s Schengen free-border zone will be key foreign-policy priorities. More public capex is likely under this scenario, especially in the water-management sector, as water shortage has become an important issue in the ongoing election campaign. However, reforming the tax system is unlikely to be among the immediate priorities of the new government, despite that there is a pressing need to reduce inequality and to permanently raise tax revenues in order to meet higher pension, health-care and social costs related to an aging population.

We have kept our forecast for 2.5% real GDP growth in 2024. Under the positive scenario, we expect GDP growth to accelerate to 2.9% in 2025, as improved EU-fund absorption (we think

NO MAJOR SURGE IN SUPPORT FOR EXTREME POPULISTS

MAINSTREAM PARTIES ARE LIKELY TO BE IN CONTROL



Source: Central Electoral Commission, Alpha Research Agency (the public-opinion poll was conducted in the period 18 Sep – 24 Sep 2024), UniCredit Group Investment Strategy

Moderate acceleration of growth is anticipated under the positive scenario, which is also our baseline

We think Bulgaria could enter the eurozone by 1 January 2026

Personal antipathy between the leaders of GERB and WCC-DB might lead to a new snap vote

GDP growth remains little changed next year under the negative scenario

A political price will have to be paid if Bulgaria misses the chance to complete the euro-adoption process

Bulgaria will receive two tranches from its RRP next year) and stronger external demand should help boost exports and investment growth. Private-consumption growth is set to moderate, in our view, since both real-wages growth (see chart) and retail credit growth are expected to lose momentum in throughout the next few months and further into next year.

We now expect Bulgaria’s consumer price inflation, calculated according to the national methodology, to bottom out at 2.0% yoy in September 2024, mostly driven by huge base effects. However, the country’s 12-month average inflation rate, which is used for convergence assessment purposes, is expected to bottom out half a year later, at 2.3% in March 2025 (see chart). Only then, if our projection is right, will inflation have gone down enough for the BNB to request an extraordinary convergence report. If the report is positive and the political environment is supportive (if Bulgaria has a stable government backed by a ruling coalition committed to completing eurozone entry), then the European Council will formally approve Bulgaria’s accession to the euro area in May or June next year. If so, we think a realistic time for euro introduction in Bulgaria is likely to be 1 January 2026, rather than 1 July 2025.

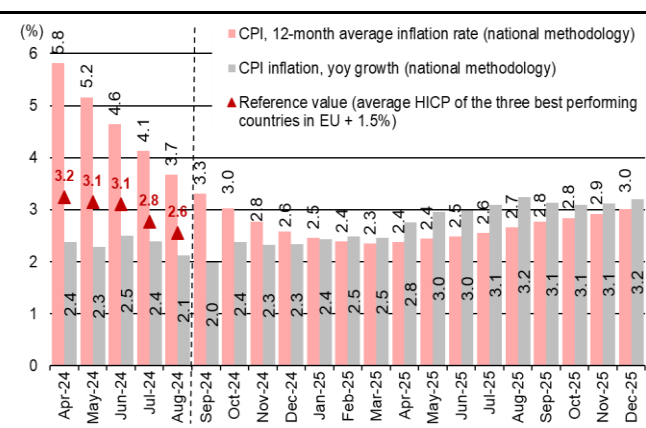
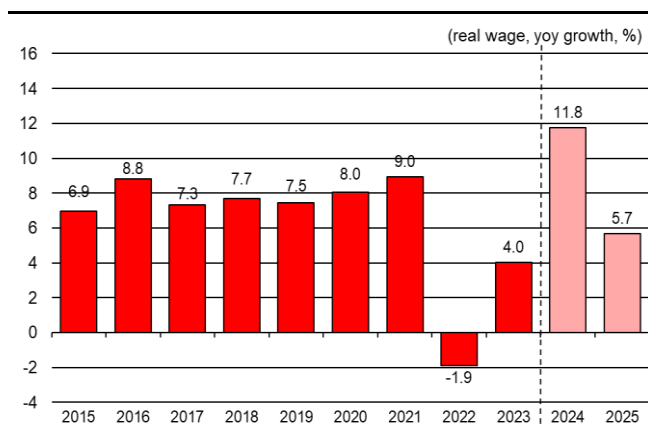
Under the negative scenario, limited desire to end political confrontation and seek compromise leads to a new snap vote at the beginning of next year. Such an outcome would deepen the country’s political crisis and lead to erosion of support for mainstream parties at the expense of votes for existing or newly emerged anti-establishment parties. A large proportion of political power will remain in the hands of the country’s president, whose role in decision-making might rise further. Under a worst-case scenario, support for Ukraine would be at risk, thereby complicating the country’s relations with its allies from NATO and the EU. Structural reforms are likely to stall further, crippling plans to modernize the economy and boost living standards.

Under the negative scenario, 2.6% GDP growth is expected in 2025. Bulgaria receives only one tranche from its RRP, as ongoing political confrontation will make it hard to implement the structural measures needed to unlock EU funds. Private capex will suffer as well since elevated uncertainty will prompt firms to retain a wait-and-see approach. On the positive side, Bulgaria’s accession to the euro area is unlikely to suffer much under this scenario. If the next snap vote is held in March 2025, it would not be too late for Bulgaria to request an extraordinary convergence report shortly after a new government is formed in April or early May at the latest, provided that commitment to euro adoption remains intact after the vote and Bulgaria has already met the inflation criterion, as our inflation projection envisages.

If Bulgaria misses this opportunity because it has no regular government to steer it through the final stages of the euro-adoption process, then it is not clear when the next chance will present itself. Importantly, meeting the inflation criterion later may prove more complicated, in our view, because it is likely to require moderate tightening of the fiscal policy, including more-stringent control of income growth for at least several consecutive quarters.

REAL-WAGE GROWTH TO LOSE MOMENTUM NEXT YEAR

BULGARIA TO MEET INFLATION CRITERION EARLY NEXT YEAR



Source: Eurostat, NSI, UniCredit Bulbank

Note: UniCredit Bulbank does not forecast harmonized inflation, while the latter would be used to assess Bulgaria’s convergence in terms of price stability.

GROSS GOVERNMENTAL FINANCING REQUIREMENTS

EUR bn	2023	2024F	2025F
Gross financing requirement	4.3	5.0	5.6
Budget deficit	2.9	3.0	3.2
Amortization of public debt	1.4	2.0	2.4
Domestic	0.0	0.3	2.2
Bonds	0.0	0.3	2.2
Bills	0.0	0.0	0.0
Loans/other	0.0	0.0	0.0
External	1.4	1.7	0.2
Bonds and loans	1.2	1.5	0.0
IMF/EU/other IFIs	0.2	0.2	0.2
Financing	4.3	5.0	5.6
Domestic borrowing	0.0	0.9	1.1
Bonds	0.0	0.9	1.1
Bills	0.0	0.0	0.0
Loans/other	0.0	0.0	0.0
External borrowing	4.3	4.4	4.3
Bonds and loans	3.8	4.4	4.3
IMF/EU/other IFIs	0.5	0.0	0.0
Privatization/other	0.0	0.0	0.0
Change in fiscal reserves (- =increase)	0.0	-0.2	0.2

GROSS EXTERNAL FINANCING REQUIREMENTS

EUR bn	2023	2024F	2025F
Gross financing requirement	23.8	23.1	20.8
C/A deficit	0.3	0.2	-0.6
Amortization of medium- and long-term debt	6.1	5.9	4.1
Government/central bank	1.4	1.7	0.2
Banks	1.1	1.4	1.4
Corporates/other	3.6	2.8	2.5
Amortization of short-term debt	17.4	17.0	17.3
Financing	23.8	23.1	20.8
FDI (net)	3.1	3.2	3.8
Portfolio equity, net	-1.2	-2.3	-2.0
Medium and long-term borrowing	8.7	6.0	4.8
Government/central bank	4.3	4.4	4.3
Banks	1.6	1.4	1.4
Corporates/other	2.8	0.2	-0.9
Short-term borrowing	17.0	17.3	17.6
EU structural and cohesion funds	1.3	1.5	2.2
Other	-1.6	-0.8	-1.6
Change in FX reserves (- = increase)	-3.5	-2.0	-3.9
Memorandums:			
Nonresident purchases of LC gov't bonds	0.0	0.0	0.0
International bond issuance, net	2.6	2.9	4.3

Source: BNB, Bulgarian Ministry of Finance, UniCredit Group Investment Strategy

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