Macroeconomic bulletin

Spring 2023

March
2023

dsk Research

Sovereign credit rating

Bulgaria

Moody's
Baa1 stable

S&P Global Ratings
BBB stable

FitchRatings
BBB positive

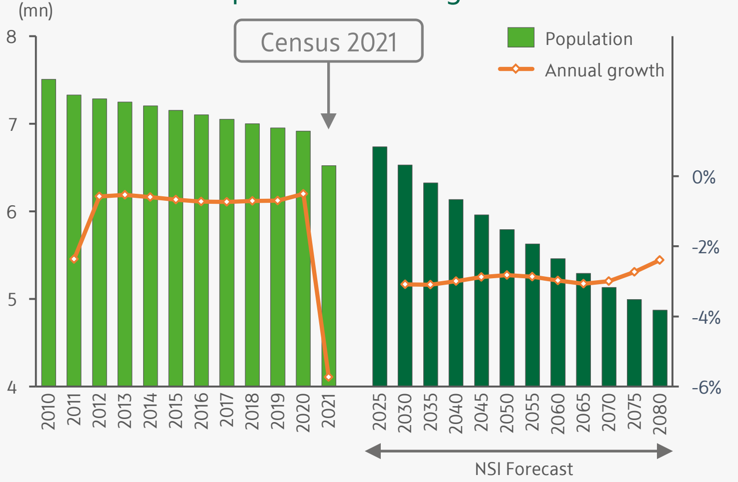
- The world is preparing for a year of weak growth, and in some regions even recession. Many factors indicate that the consequences of the shocks that impacted the global economy in the last few years have not passed and will persist in the current year 2023. COVID-19 first seriously shook the world, plunged the economies into a deep recession and after the sharp recovery came, contributed to disruptions in trade channels and supplies. As a result of these shocks, there were shortages of productive resources and this contributed to raising prices. The beginning of 2022 marked a new global factor, Russia's war in Ukraine, which further intensified the inflationary pressure that were already on the way.
- A new major economic world factor is also shaping up in early 2023 and that is the re-opening of China after the government waived COVID-19 zero. This will further put pressure on the global economy and central banks policies to deal with inflation and interest rates. After a serious increase in interest rates by central banks, the American bank Silicon Valley Bank (SVB) went bankrupt and this increased uncertainly in the financial sector.
- In addition, the second largest bank in Switzerland and with a century of history, Credit Suisse fell into a crisis of confidence on the part of its customers. Although the two events are unrelated, the financial sector is showing volatility that central banks are trying to contain through financial support and the facilitation of Europe's biggest banking deal since the financial crisis.

Demographics

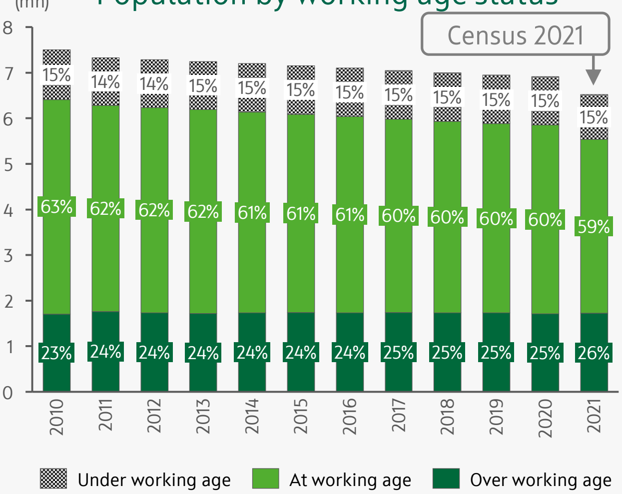
Without a radical demographic strategy, the population will continue to decline

The population of Bulgaria continues to decrease with dangerous trends for the economy in every aspect. Census 2021 final data has confirmed the negative demographic trend. In 10 years, the population shrank by 12% and reached 6.5 million people. More than 50% lives in the two most economically developed regions: Southwest & South Central.

Population* of Bulgaria



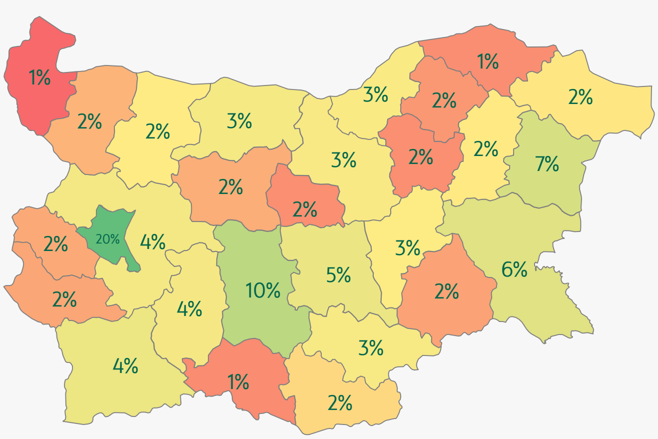
Population by working age status



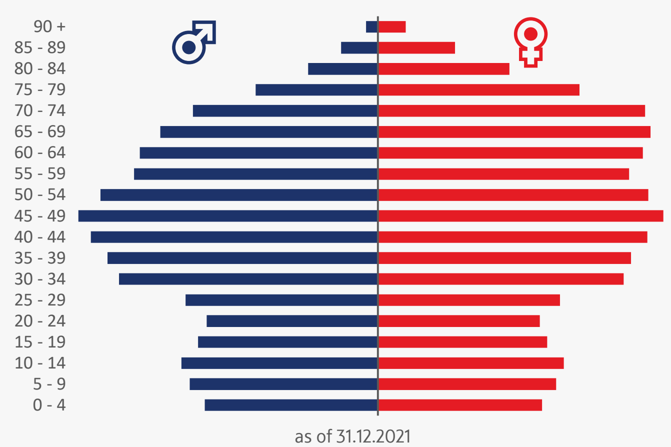
If urgent long-term social measures are not taken, the demographic trends will deteriorate in the long term. Bulgarian business is already feeling the consequences of the demographic crisis in the form of a labour shortage, especially affecting the high qualified personnel. The indicator measuring the business climate in the country shows this trend as being most tangibly felt in the "Construction" and "Industry" sectors, which are one of the most important sectors for strong and constant economic growth of the GDP.

Population by administrative regions

as of Census 2021



Population pyramid: The process of ageing continues



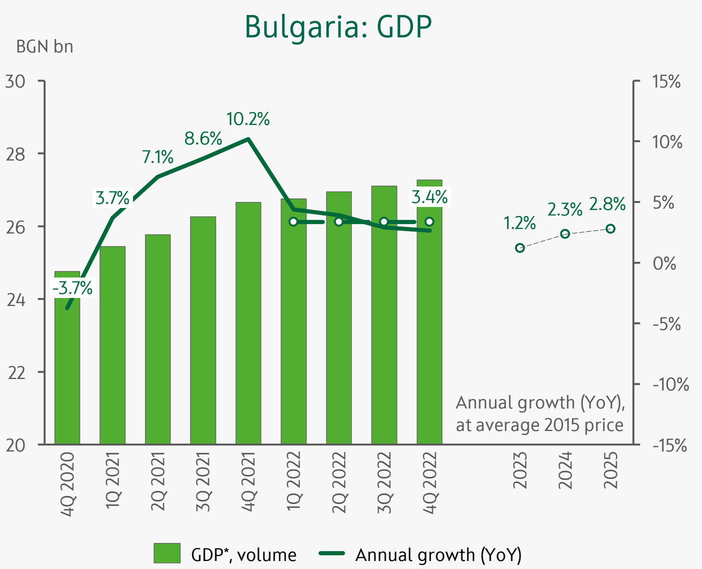
as of 31.12.2021

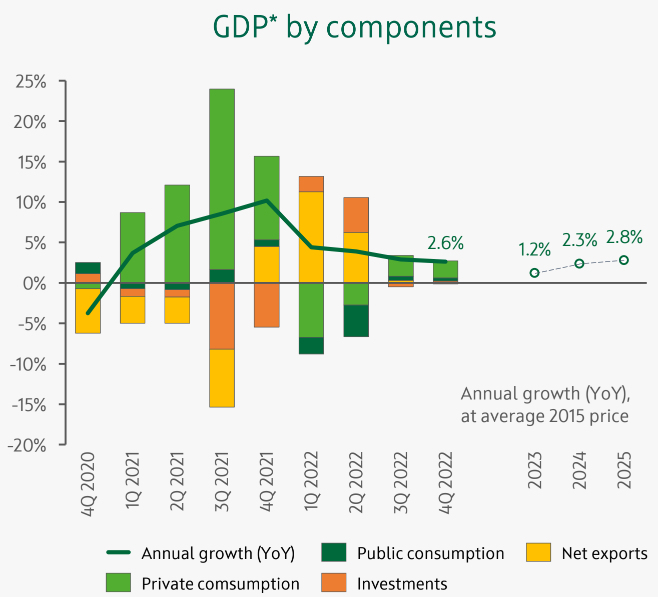
* *Population forecast to 2080 are based on the 2011 Census.*

Gross Domestic Product

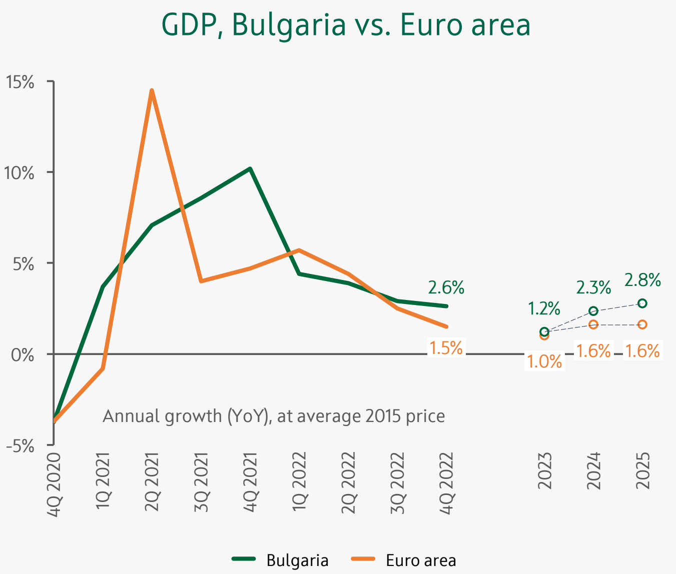
Recession seems an increasingly unlikely option

- After several months of fluctuations, private consumption again shows a positive contribution to GDP dynamics. However, the annual growth of private consumption is expected to decrease mainly due to inflationary pressure, interest rate hikes and reduced real disposable income. Our expectations for investments are, in the mid-term, to grow at a higher pace compared to the general dynamics of GDP. That will be boosted mainly by a recovery in economic activity, together with the launch of NextGenerationEU. The fiscal measures taken by the government to compensate for high energy prices and inflation are expected to be withdrawn in 2023.





- In late 2021 and early 2022, net exports illustrated a significant positive contribution to GDP growth. This was influenced by the country's export, which registered high annual growth.



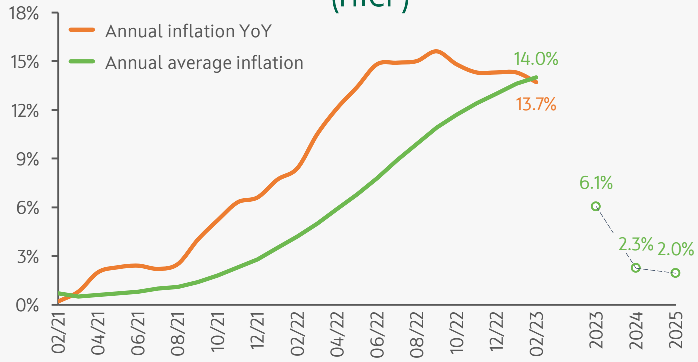
*Seasonally and calendar adjusted data

On the prices side, we assume lower prices for energy resources, which in turn implies lower prices for the amount of electricity exported from Bulgaria. In general, we expect the contribution of net exports to be negative in the medium term. Similar to Bulgaria's GDP dynamics, Euro Area has also stagnated over the past few quarters and is expected to prolong this trend until the first quarter of 2023, after which an economic recovery will begin, fueled by an improving supply channel environment, cooling inflation and tackling the uncertainty surrounding energy supplies.

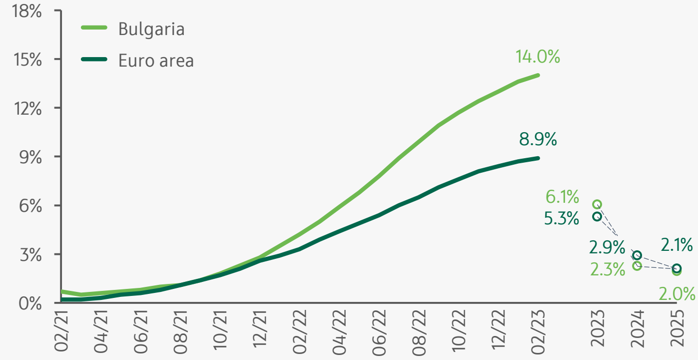
Inflation

Fuel, natural gas and electricity prices calm inflationary pressure

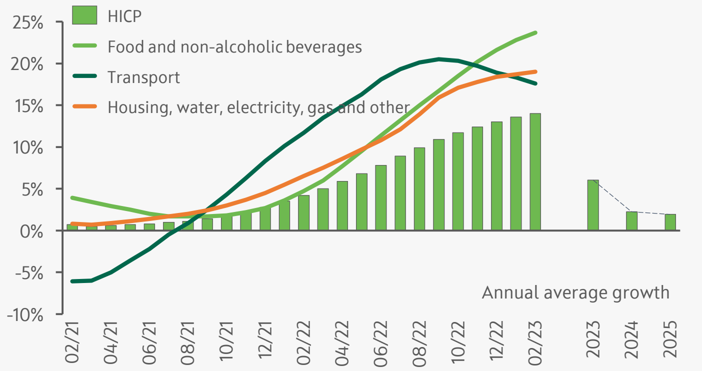
Harmonized Indices of Consumer Prices (HICP)



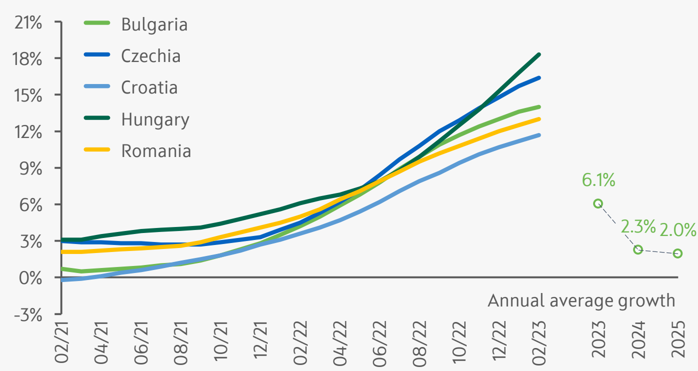
HICP, Bulgaria vs. Euro area



HICP by commodity group*

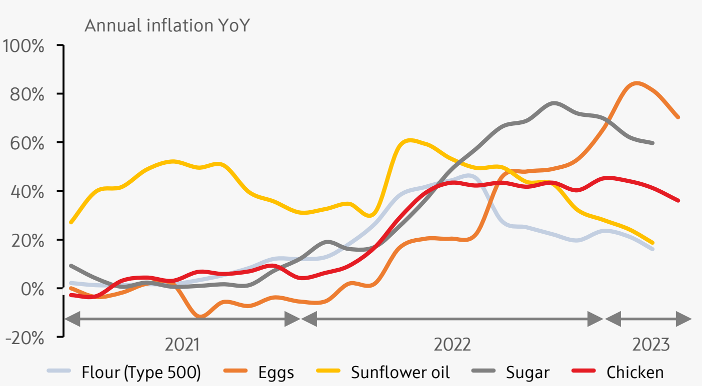


HICP, Bulgaria vs. CEE countries



- The recovery of international trade after COVID-19 and the war that started in Ukraine are the main drivers that accelerated the prices of energy sources, and from there, of all other goods and services. In many regions of the world, 2022 turned out to be a record year for the growth of consumer prices, which significantly undermined the purchasing power of the population. Governments and businesses try their best to compensate for the reduced purchasing power by increasing nominal wages and social benefits, but this further affects inflationary pressure. Per our expectation in the Autumn bulletin, inflation started to show signs of calming down even before the end of 2022 and the beginning of 2023. The recovery of relatively low transport fuel, natural gas and electricity prices contributed to a reversal of the inflation trend in European Union and Bulgaria in particular.
- We predict that this trend will continue throughout the year, with the average annual inflation at the end-2023 reaching a level of 6.1%.

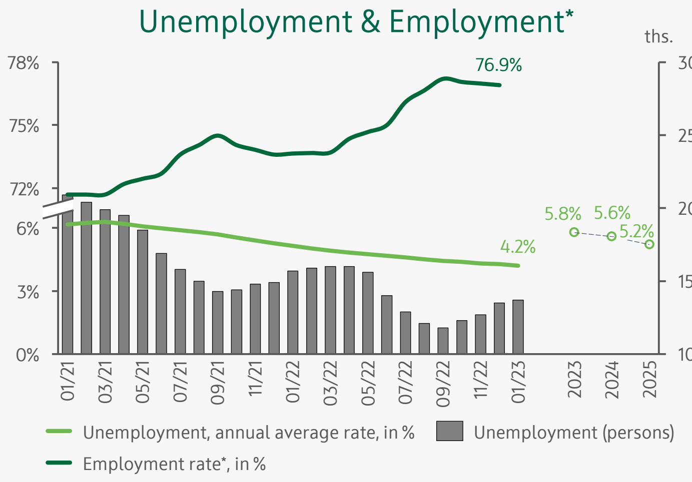
Basic food inflation

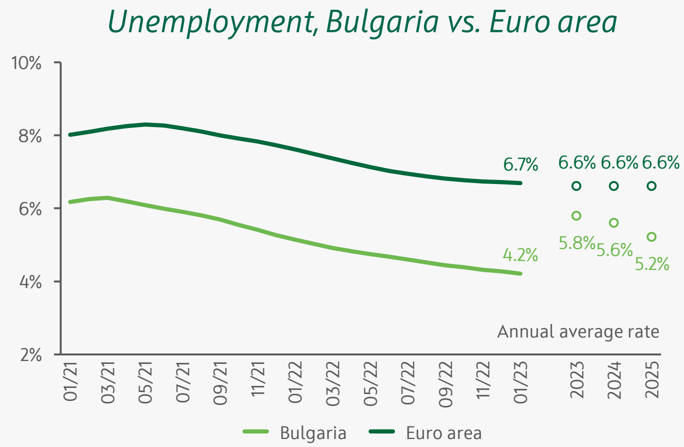


*Three consumer groups with the largest weights in the HICP general basket are presented.

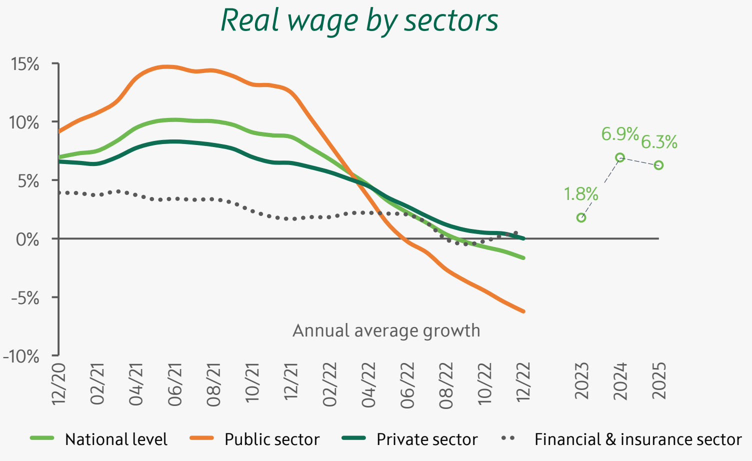
Labour market

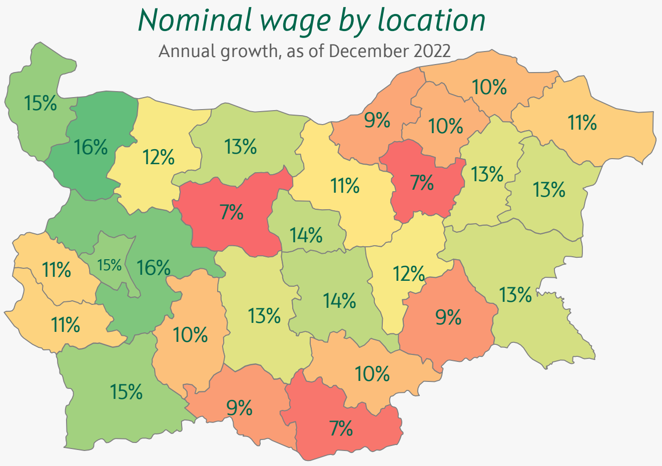
Competition for employees is growing among companies in an environment of decreasing labour force





Labour market remains resilient and the unemployment rate remains at historic lows in line with labour supply shortages, particularly in "Services" and "Restaurants and hotels" sectors. The demand for employees continues to exceed the supply in the economy, as a result of which number of companies hire employees from Non-EU countries, such as Ukraine, Moldova, Turkey, Kazakhstan, Kyrgyzstan, Uzbekistan, etc. This fact determines the labour market to be less sensitive to GDP growth dynamics.



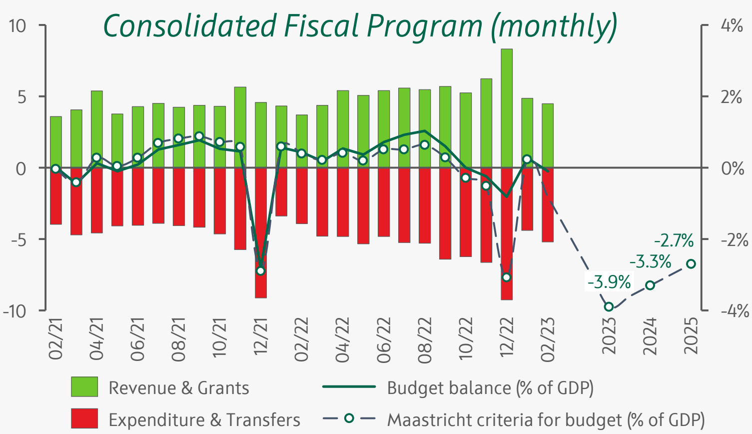


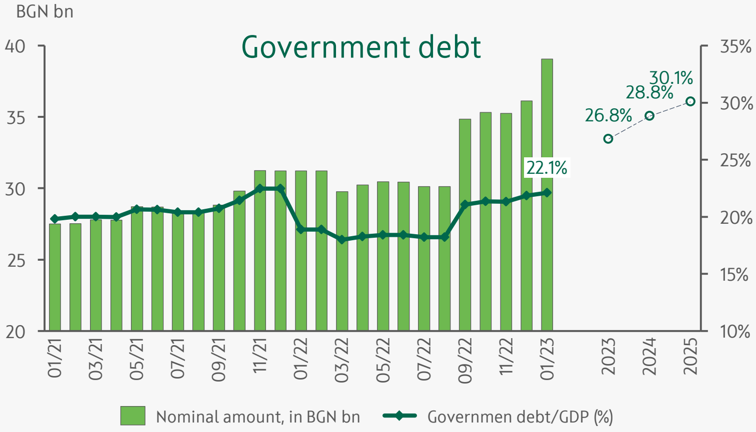
The relatively higher employment is mainly attributed to the observed reduction in the risk of a recession in 2023, i.e. possible increase in layoffs. Even on the contrary, there is a trend of "employee stocking" in an environment with a shrinking labour force and economically active population. As a result, the nominal wage continues showing serious growth rates and is expected to increase in the medium term by 10% annual growth. However, real wage growth in 2022 contracted by 2%, mainly due to high inflation rates. In some regions of Bulgaria, wage growth in real terms was seriously undermined last year. Our expectations are for the dynamics of real wage growth are to be in the positive area over the projection horizon.

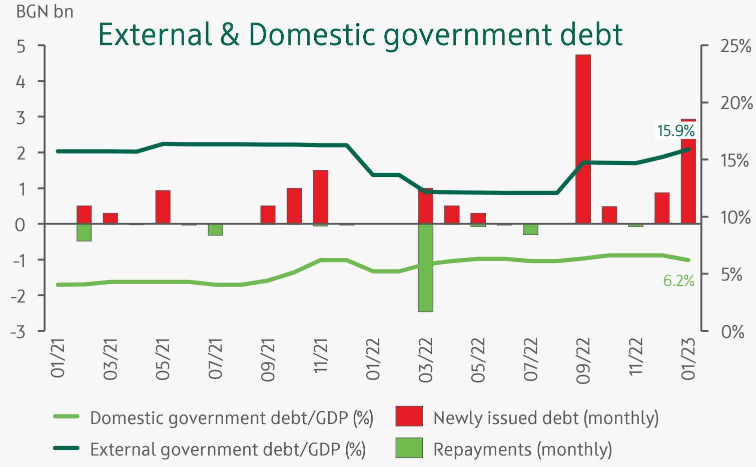
Unemployment rate is for the age range of 20 – 64 years of age.

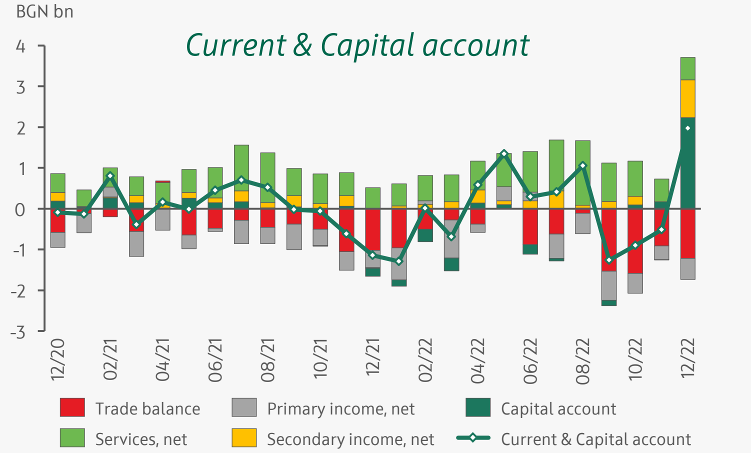
State budget

Not expecting a regular government even after the SPRING 2023 election









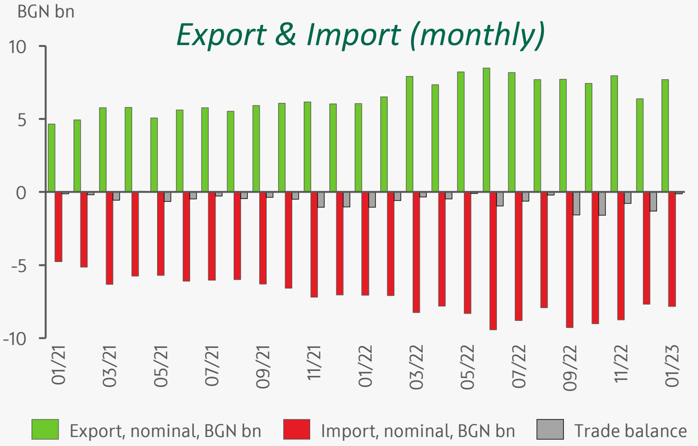
- In the last few years, political parties are in constant populism due to frequent early elections, and this has weighed mostly on government finances. The government deficit was met in 2022, despite the expected slowdown in economic growth, and 2022 ended at minus 2.9% of GDP. Due to the sharp increase in expenditures (in particular pension & subsidy costs) and the lack of revenue growth, the expected government deficit for 2023 is 6-7% of GDP, which does not meet the Maastricht criteria for joining. The current budget is a continuation of last year's budget 2022, and with a delay in forming a regular government and continuing this budget, the deficit at the end of the year will be excessive. The interim government will most likely try to push through an "solidarity contribution" on companies in order to balance the budget deficit.
- Our expectations are for an increasing government debt in nominal terms and as a ratio to GDP and reaching 26.8% by the end of 2023. We do not expect forming a regular government after Spring 2023 vote, rather the focus turns to the Autumn 2023 elections when the local elections are, most likely 2-in-1 (local & new early parliamentary elections).

Trade & Investment

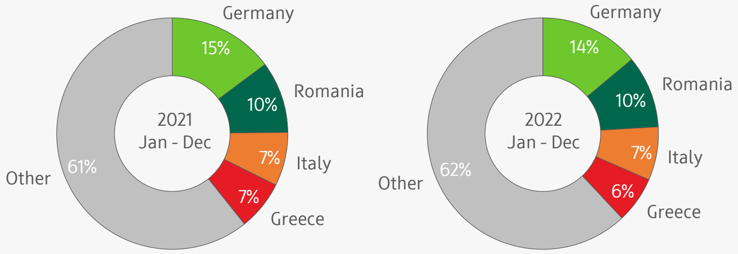
Energy resource prices are a major factor in the significant annual growth of net exports

- Country's exports and imports illustrated impressive growth in 2022, being at the top position in the EU in terms of growth, which for the entire year is close to 40%. This confirms the openness of the economy to foreign markets and sensitivity to the external environment.

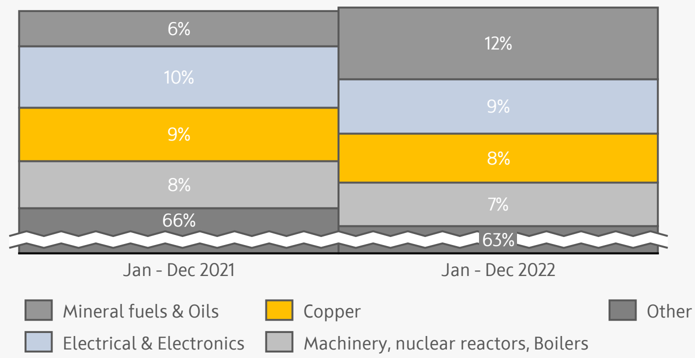
Export & Import (monthly)



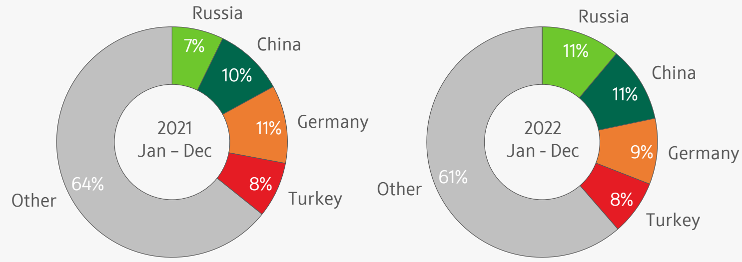
Export, main trade partners



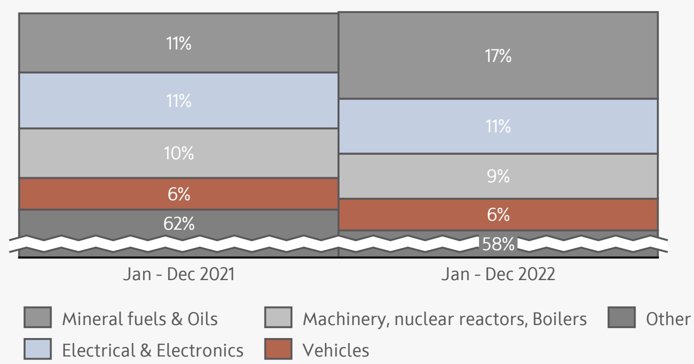
Export by category



Import, main trade partners

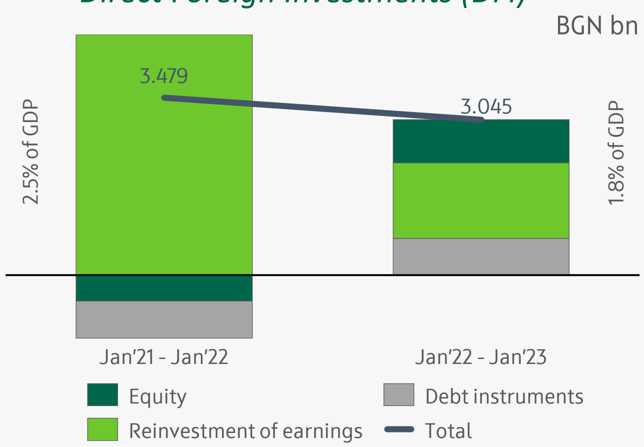


Import by category



- The main drivers of the impressive growth are the high prices of fuels, electricity, food, machinery and metals. In 2023, net exports are expected to cool slightly due to consumption of the effects that boosted trade in the past year.
- Investments: The expectations remain the same compared to the last macroeconomic bulletin: falling down and the trend will continue in the long-term.

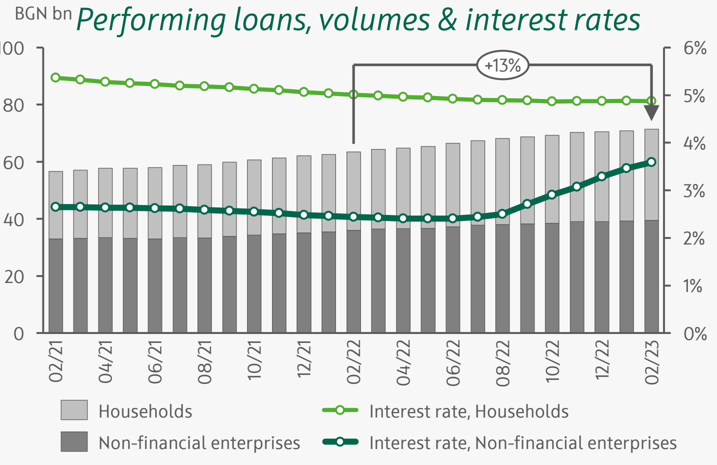
Direct Foreign Investments (DFI)

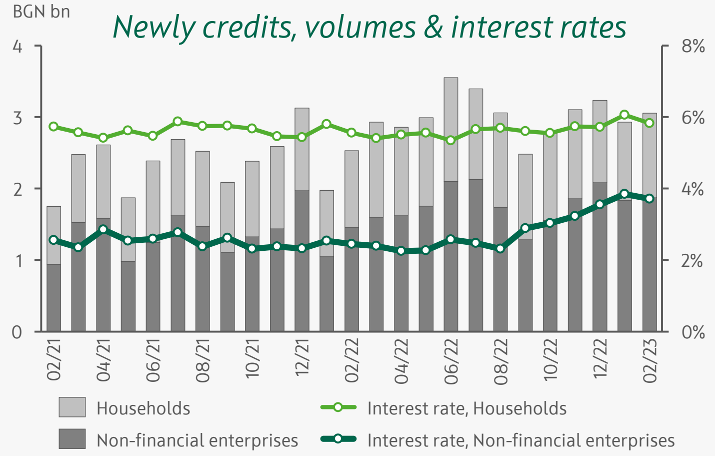


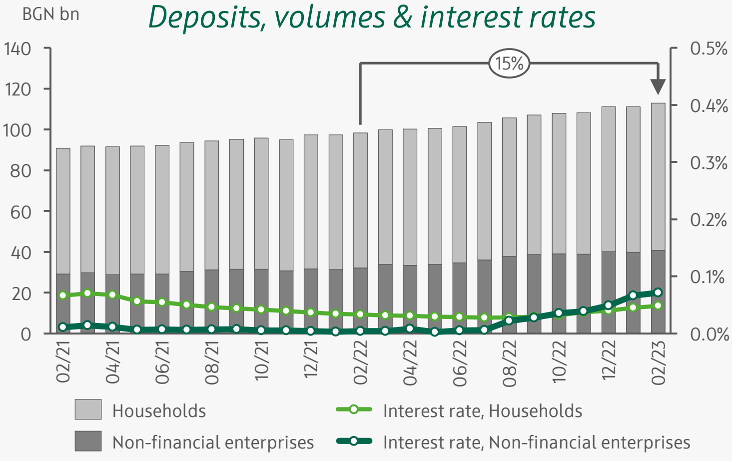
Banking system

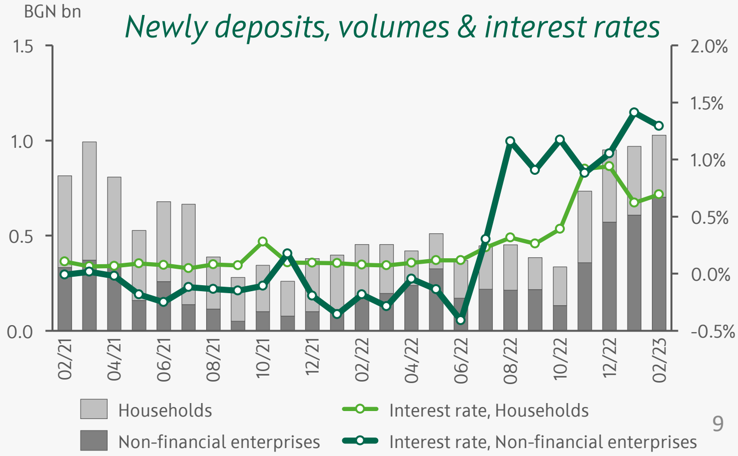
Non-financial enterprises are already feeling the monetary spillover effect

- Banking sector profit in Bulgaria marked a significant improvement in 2022 compared to 2021. Deposit growth remained strong during the year, especially insofar as deposits of non-financial enterprises are concerned. Household deposits growth eased notably in the same period, which we consider in large part reflects the negative impact of inflation on household finances, but also a natural rebound in consumption, following a period of various pandemic restrictions in 2020 and 2021, which depressed consumer spending.
- The monetary policy of the central banks still maintains high interest rates and, with unabated inflation, they seem ready to increase the rates even more. Expectations for a faster handling of inflation did not materialize and interest rates compared to the previous forecast were revised upwards (mainly Euribor).
- However, interest rates for the real economy have not yet exerted the expected dampening of lending and deposit inflows. On the contrary, there is no increase in interest rates on new production in household lending, resulting in continued high annual growth in the segment. In non-financial enterprises lending, interest rates are









Sources

Actual data

NATIONAL STATISTICAL INSTITUTE

MINISTRY OF FINANCE, BULGARIA

BULGARIAN NATIONAL BANK

STATISTICAL OFFICE OF THE EU

MINISTRY OF AGRICULTURE, BULGARIA

Forecasts

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