

# GOVERNMENT DEBT REVIEW 2011



Ministry of Finance  
Republic of Bulgaria



# **Government Debt Review • 2011**

Sofia, 2012

## Abbreviations

BDGA	Bank Deposit Guarantees Act
BIR	Base Interest Rate
BNB	Bulgarian National Bank
BPS	basis points
CPI	Consumer Price Index
EBRD	European Bank for Reconstruction and Development
EIB	European Investment Bank
EU	European Union
FDI	Foreign Direct Investments
GDP	Gross Domestic Product
GFCF	Gross Fixed Capital Formation
GVA	Gross Value Added
HICP	Harmonized Index of Consumer Prices
IMF	International Monetary Fund
JBIC	Japan Bank for International Cooperation
LEONIA	Lev OverNight Index Average
LFS	Labour Force Survey
LIBOR	London Interbank Base Offered Rate
LSPDACB	Law on State Protection of Deposits and Accounts with Commercial Banks, replaced by BDGA
MF	Ministry of Finance
NSI	National Statistics Institute
SDR	Special Drawing Rights
USD	US dollar

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# **The Bulgarian Economy in 2011**

In 2011, economic activity in Bulgaria felt a strong influence from the dynamic developments in the global economy. Revival came largely from export-oriented companies in manufacturing, and was accompanied by the continuing restructuring at the company level aimed at increasing labour productivity and labour efficiency. At the same time, the improvement of domestic demand is yet to be felt, with credit remaining tight and unemployment relatively high. The budget consolidation process helped ensure fiscal and macroeconomic stability.

### Gross Domestic Product

In 2011, Bulgaria's nominal gross domestic product (GDP) was BGN 75,265 million, a 1.7% increase in real terms from the previous year, as against a 0.4% growth in 2010. The dynamics in this indicator were powered by external demand, with the positive contribution of net exports reaching 2.3 p.p. Although at a slower rate, domestic demand continued to shrink and its negative contribution was 0.6 p.p., against 5.2 p.p. in 2010.

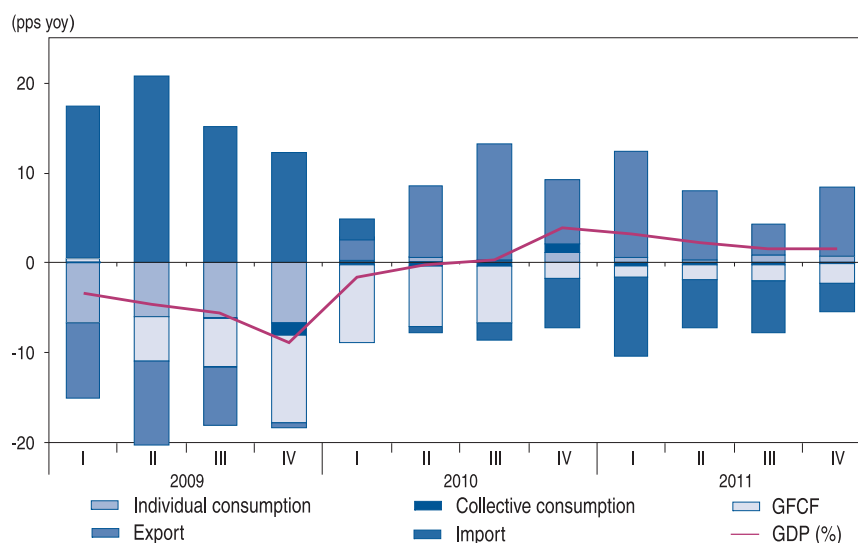
The favourable external economic environment in the first half of 2011 led to a faster increase in the export of goods and services which achieved a 12.8% growth rate in real terms for the year. A major contributor for this development was the increased export of goods, while services increased only slightly. The accelerated growth of exports drove up the demand for raw materials and supplies necessary for export-oriented production operations, as a result of which the import of goods grew by 10.5% in real terms. At the same time, the decline in the import of services persisted due to suppressed domestic demand, but the rate of decline slowed down to 3.3%.

Final consumption in 2011 shrunk by 0.3%, due mainly to lower individual consumption. High unemployment, limited credit availability and the still considerable degree of uncertainty in the economy were the main factors behind the continued decrease in household consumption expenditure which shrunk by 0.6% on an annual basis. Public consumption went up by 3% compared to 2010; however, its contribution was not sufficient to offset the lower consumer spending.

The gradual recovery of economic activity slowed down the decline in investments in Bulgaria to 1.6% from a drop of 19.2% in 2010 in comparative prices. Investments made in the economy were fully covered by national savings which reached 23.9% in GDP terms.



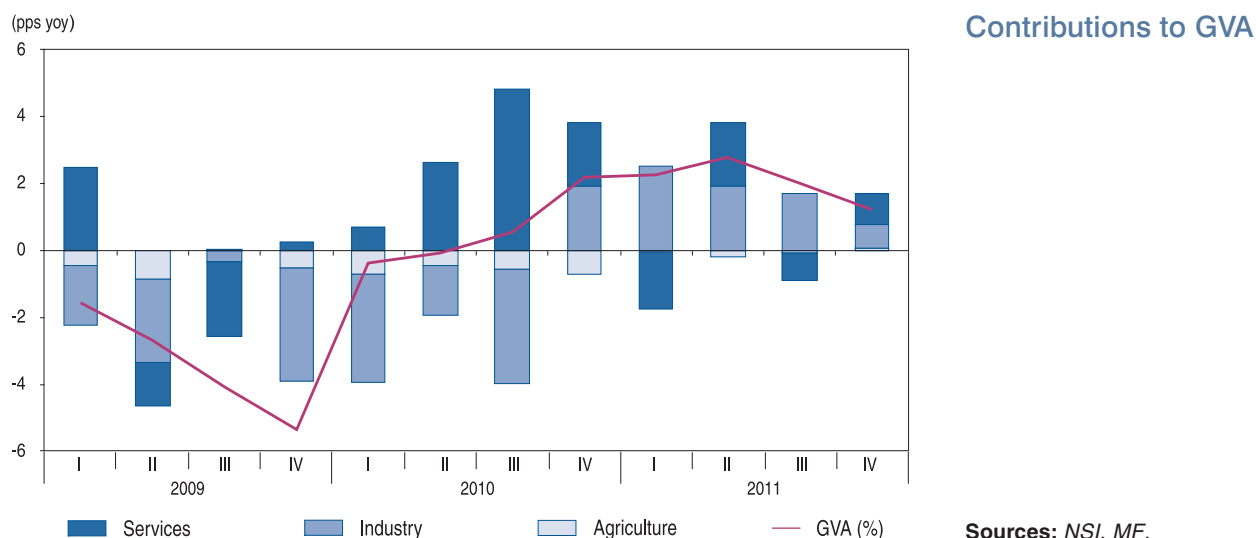
## Contributions to GDP Growth



Sources: NSI, MF.

On the supply side, Bulgaria's Gross Value Added (GVA) rose by 1.8%. As a result of stable external demand and the rise in international prices of commodities in the first half of the year, the volume of industrial products sold on external markets went up by 25.6% in 2011, which production increased by 5.8%. Value added in manufacturing rose by 9.1%, and the revival in the sector led to a general growth rate of 6.6% in real terms in the industrial sector. For the third year in a row, the construction sector reported a decline but the rate of that decline slowed down considerably, down to 1.1%, as against the shrink by 17.9% in 2010. Services did not exhibit any significant change from the previous year, with the gross value added in the sector down by 0.1%. In the agricultural sector, the reported decrease in gross value added in real terms reached 1.1%.

According to potential growth indicators, the economy slowed down to a growth rate of 0.7%. The drop in investments and the decline in the employment rate were factors contributing to that development.



## Labour Market and Income Levels

In 2011, economic growth fell short of helping turn around the negative trends in the labour market. Economic recovery came largely from exports, while domestic demand, which is also a determining factor in employment rate dynamics, exhibited signs of revival only as from the second quarter of the year.

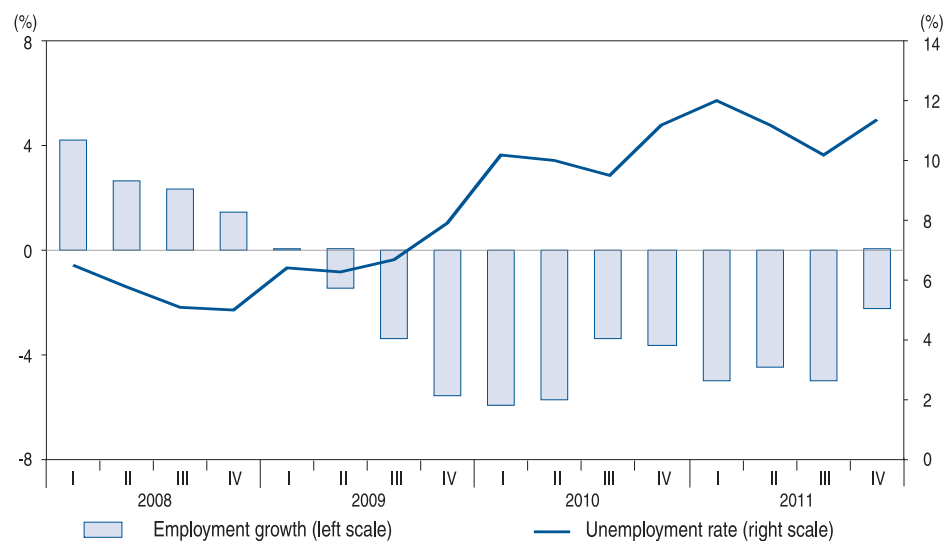
The annual decline in the employment rate registered a certain slowdown in 2011 compared to the previous year (to 4.2% from 4.7% in 2010<sup>1</sup>), which was due to the slowdown in the decrease in the employment rate in manufacturing, while in the service sector the pace of employment rate decline speeded up on an annual basis. The increased demand for labour force in some of the export-oriented industries (machine building and manufacturing of electrical equipment) was unable to offset the continuing decrease in the number of people employed in activities which are dependent mainly on domestic demand.

The unemployment rate went up 1 p.p. compared to 2010, reaching an annual average of 11.2%<sup>2</sup>. The demand for labour, weaker than in the previous year, and the more limited capacity to create jobs, were at the root of the drop in the economic activity rate of the population (aged over 15) to an average of 51.3% in 2011.

<sup>1</sup> According to data on persons employed from the System of National Accounts (SNA).

<sup>2</sup> According to data from the Labour Force Survey.

## Employment Growth and Unemployment Rate



Source: NSI.

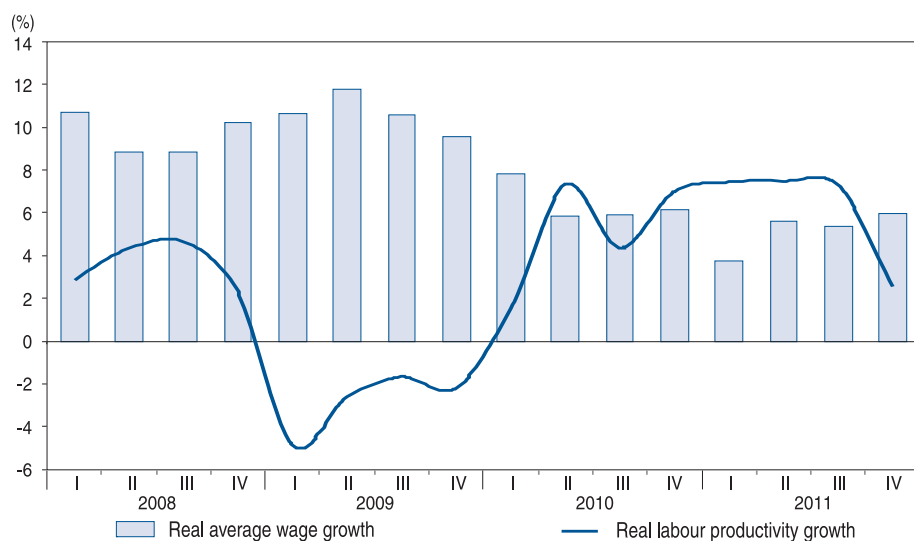
In 2011, the increase in the average monthly salary for the economy in general was 9.1% in nominal terms and 4.7%<sup>3</sup> in real terms. The efforts of the government to streamline public spending reflected in a considerable slowdown in this indicator for the public sector, where a nominal growth in salaries of 3.1% was registered, and in real terms that translated into a decrease of 1.1%. In the private sector, wages and salaries exhibited higher rates of increase, growing at 11.2% and 6.7% in nominal and in real terms, respectively. In a breakdown by economic activity, the highest contributions to the growth in income levels came from processing industries, trade and transport, which was due to the higher labour productivity in those sectors.

Continuing job cuts have had an effect, further improving labour productivity<sup>4</sup>: its increase in real terms stepped up to a rate of 6.2% in 2011. Growth was evident in almost every economic activity, yet its current dynamics was driven primarily by the tradable sector<sup>5</sup> (12%).

<sup>3</sup> HICP-deflated.

<sup>4</sup> Calculated as the ratio between GDP in constant prices and the number of employed persons, as defined in SNA.

<sup>5</sup> For the purposes of this analysis, the tradable sector is defined as industry excluding construction, which is due to the lack of more detailed data about GVA and employment levels.



Real Average Wage and Labour Productivity Growth

Sources: NSI, MF.

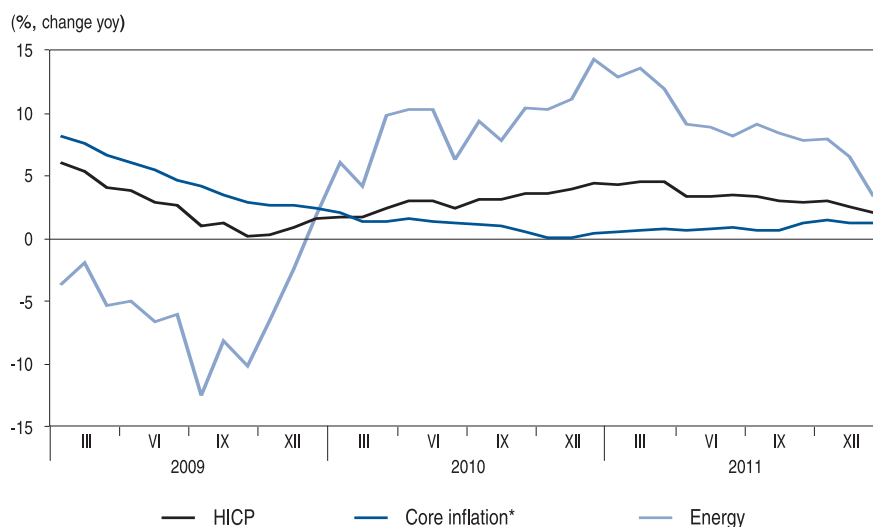
The upward trend in labour productivity had a favourable influence on the development of the real unit labour cost (ULC)<sup>6</sup>. In 2011, this indicator showed an average decrease of 3.7%, and accounted for the largest contribution in the tradables sector, with the services sector also exhibiting a downward ULC trend.

### Inflation

The 2011 dynamics in price levels in Bulgaria was largely a reflection of the fluctuations of international prices of food and energy goods. The rise in prices for major commodities in 2010 – 2011 as a result of the recovery of global demand and the various constraints on the supply side was the determining factor behind the increase in consumer prices in Bulgaria in the first half of the year. Prices on international markets plateaued in mid-2011, which helped the annual change in domestic consumer prices continue with its downward trend. A slowdown in the annual rate of increase was observed for both foodstuffs and energy goods. Unemployment was up and the pace of recovery of domestic demand remained sluggish, thus also held down the increase in consumer prices and contributed to maintaining a relatively low rate of core inflation (services, non-energy goods and non-foods).

<sup>6</sup> Calculated as the ratio between compensation per person employed to GDP per person employed in current prices.

## Harmonised Index of Consumer Prices



Sources: Eurostat, MF.

\* Services and non-energy non-food goods.

General inflation, measured through monthly HICP year-on-year basis, slowed down to 2% at the yearend, indicating a weakening inflationary pressure in Bulgaria, and the annual average inflation rate stood at 3.4%.

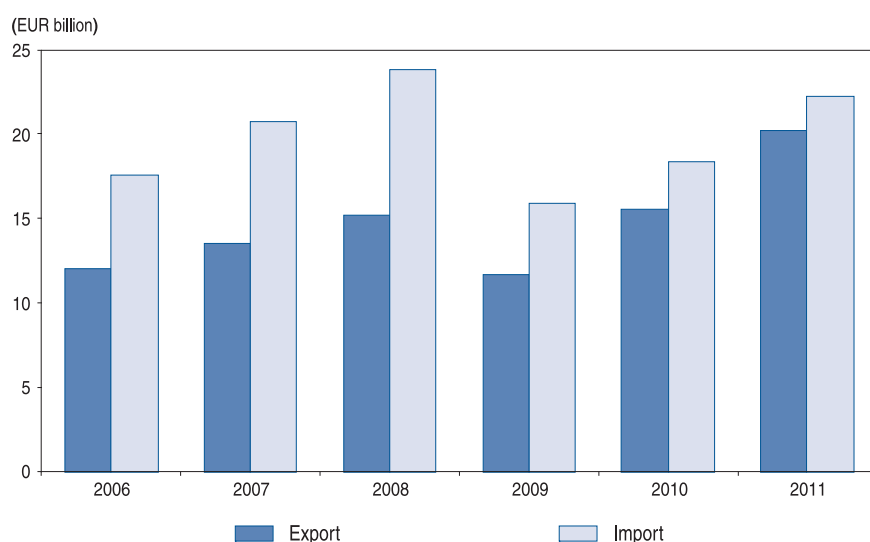
The annual change in administratively regulated prices was 4.5%, accounting for almost of the overall increase in consumer prices at the end of 2011. The main adjustments in controlled prices had to do with the raise in the minimum monthly wages in September and the resulting increase (by 34.3%) in the consumer fee charged on visits to a general practitioner, and in the prices of hospital care services (12.5%). More tangible prices increases were reported also for electricity and heating for households (2.1% and 2.4%, respectively), urban public transport (7.6%), and university tuition fees (4.6%).

## Balance of Payments

In 2011, adjustments to the balance of payments continued. The positive trend in exports not only brought trade deficit down but also generated a surplus in the current account. The current account balance in the balance of payments was a positive value of BGN 706.9 million, or 0.9% of the annual GDP, against a deficit of 1.0% a year earlier.

Following an accelerated increase in Q1 and a relative slowdown in the rate of increase in the second half of the year, the annual nominal growth in exports reached 30% in 2011. Its dynamics was linked to the upward trend in international prices, yet

the main contributor to that change was the increased volume of exports. A more detailed analysis of the structure of exports would reveal that its overall annual growth was due to the groups 'Base metals', 'Raw materials for the food and beverage industry', 'Mineral products and fuels' and 'Machinery, equipment and appliances'.



## Export/Import Dynamics

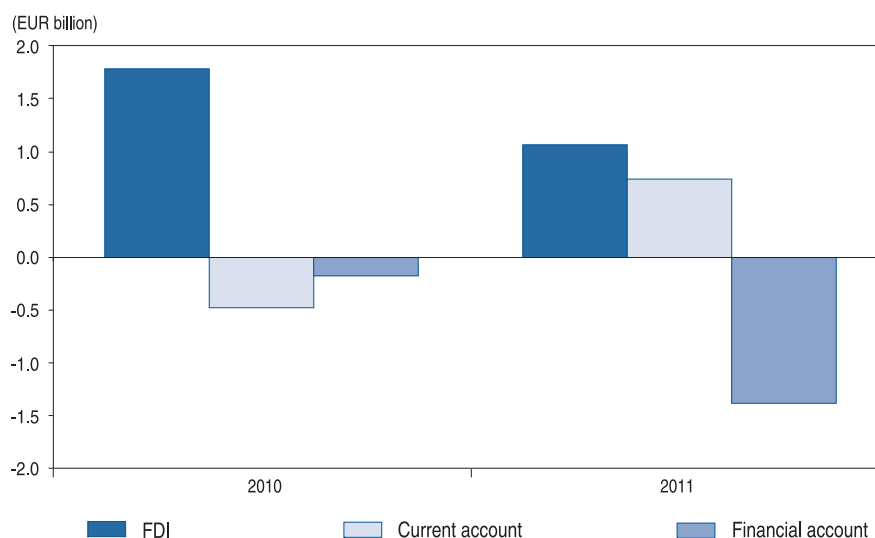
Sources: BNB, MF.

The dynamics in imports was determined mainly by the requirements of export-oriented production operations, and their annual rate of increase in nominal terms reached 21.2%. The primary factors behind increased imports, due mostly to higher international prices, were raw materials and supplies, and mineral products and fuels. The resulting trade deficit (5.1% in GDP terms) improved by BGN 1.5 billion compared to the previous year, reaching a record low compared to the years of the economic boom.

Surplus under services grew to BGN 4.5 billion in 2011, from BGN 3.9 billion in the previous year. Lower expenditure for the use of hired services, on the one hand, and higher income from transport and travel, on the other, were the main reasons for the improvement of the trade balance.

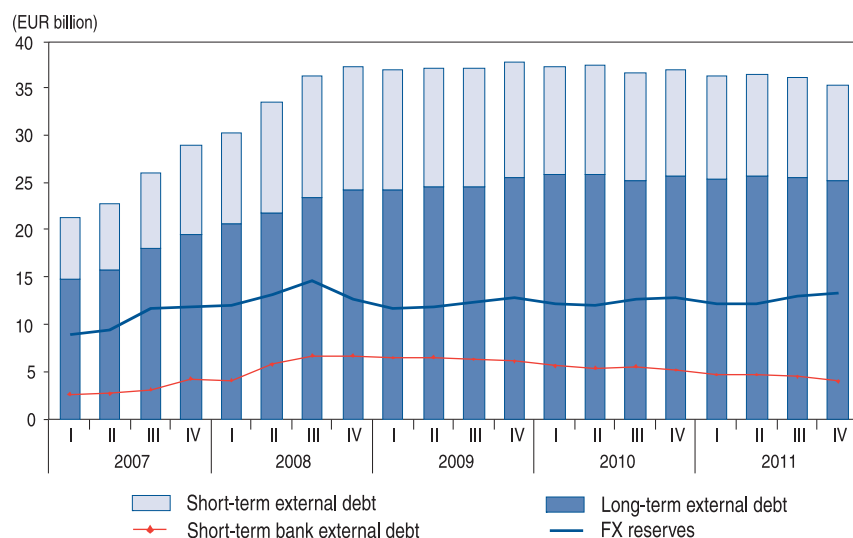
Payments to non-resident parent companies in the form of investment income increased the negative balance on the 'Income' line to BGN 3.2 billion in 2011. The increased amounts of in-coming transfers to the General Government sector (BGN 300 million higher than in 2010) increased the 2011 surplus in 'net current transfers' to BGN 3.3 billion and caused a higher positive contribution by that line item in improving the current account balance within the balance of payments.

## FDI, Current and Financial Account



In 2011, the negative balance in the financial account stood at BGN 2.3 billion. Cash flows were largely associated with the banking sector, representing redemption of liabilities due to the high liquidity of banks in Bulgaria. Over the year, deposits of non-residents in Bulgaria dipped by BGN 2.2 billion. At the same time, Bulgarian foreign assets held in deposits and foreign currency grew by BGN 1.1 billion. Investor risk-aversion, which grew as a result of the crisis globally, including towards developing markets, paired with the exacerbated debt problems of some of the countries in the region, held investment in-flows to Bulgaria at levels that were considerably below those in the pre-crisis period. In 2011, foreign direct investments amounted to BGN 2.6 billion, compared to BGN 2.4 billion (in adjusted data) in 2010.

Repayment of liabilities to non-residents had a positive effect on the country's gross external debt which, according to the latest statistics, went down to 91.9% of GDP at the end of 2011 from 102.8% in 2010. The debt maturity structure also improved, with the portion of short-term debt down to 28.2% of the gross external debt at the end of 2011, and a 133.8% cover by BNB reserves.



**Bulgaria's External Debt**

Sources: BNB, MF.

## Financial Sector

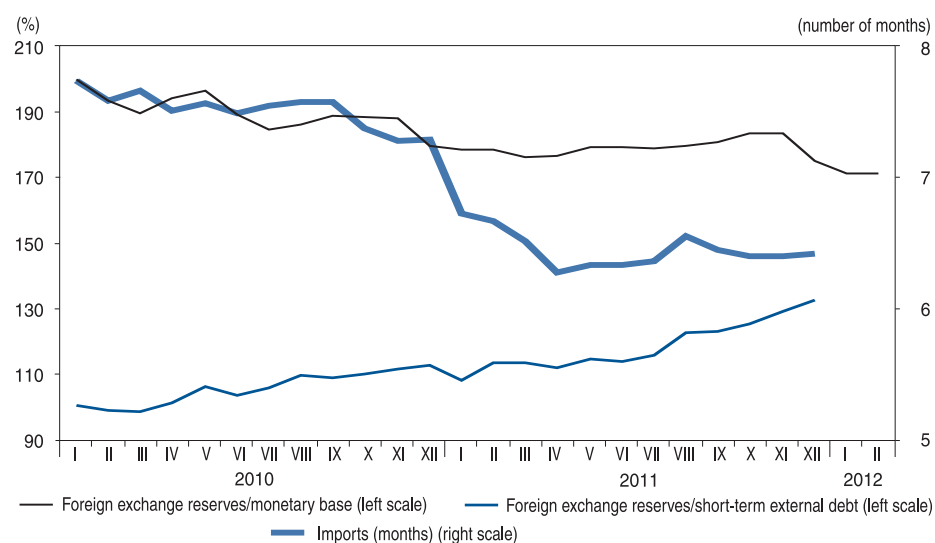
The financial sector remained stable in 2011. The international FX reserves of Bulgaria exhibited a downward trend until the middle of Q2, following which they began to recover and as of the end of December had climbed back to EUR 13.3 billion, reaching an annual rate of increase of 2.9%, against 0.4% for December the previous year. The international reserves to monetary base coverage ratio dipped slightly from 179.8% at the end of 2010 to 175.1% in December 2011. On its part, the gradual recovery of imports of goods and services brought about a slight deterioration of its coverage ratio on an annual basis, to 6.3 months from 7.3 months a year earlier.

The downturn in lending to the private sector was brought to an end in early 2011 and it embarked on a very slow recovery. Having reached its annual high in August (3.3%), the rate of growth of lending decelerated slightly in the subsequent months, to gain speed again in December and return back up to 3.3%. The key role in that positive growth was played by credit to non-financial undertakings which exhibited an acceleration in their annual increase from 2.4% in December 2010 to 5.7% at the end of 2011. The contribution of household credit was close to neutral, since consumer loans moved down at a decelerating rate throughout the year, while housing loans retained a positive, although decelerating rate of change.

The low rates of economic recovery and the time lag with which the labour market tends to respond to positive trends in the economy contributed to the continuing increase in bad debt. At the end of Q4, loans overdue for more than 90 days accounted for 14.9% of gross loans to non-financial undertakings and households; for comparison, their share at the end of 2010 was 11.3%.



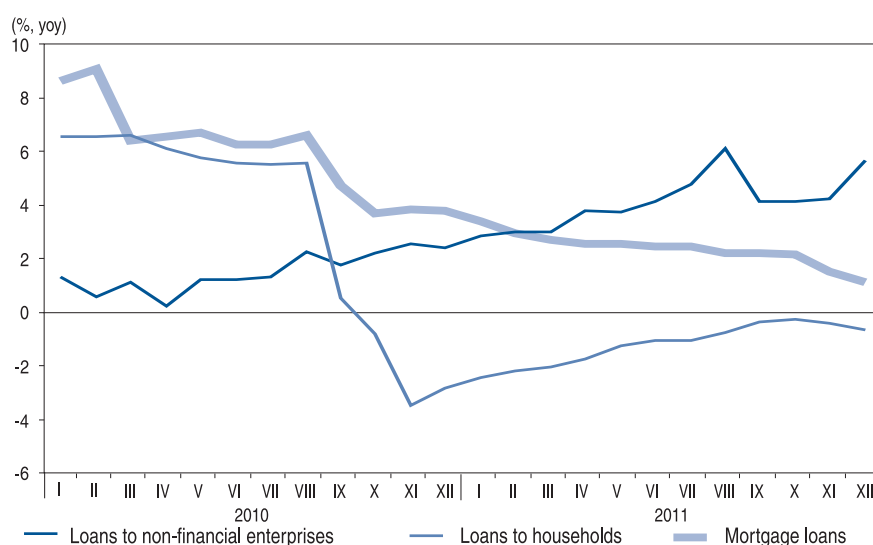
## Coverage with FX Reserves



Sources: BNB, MF.

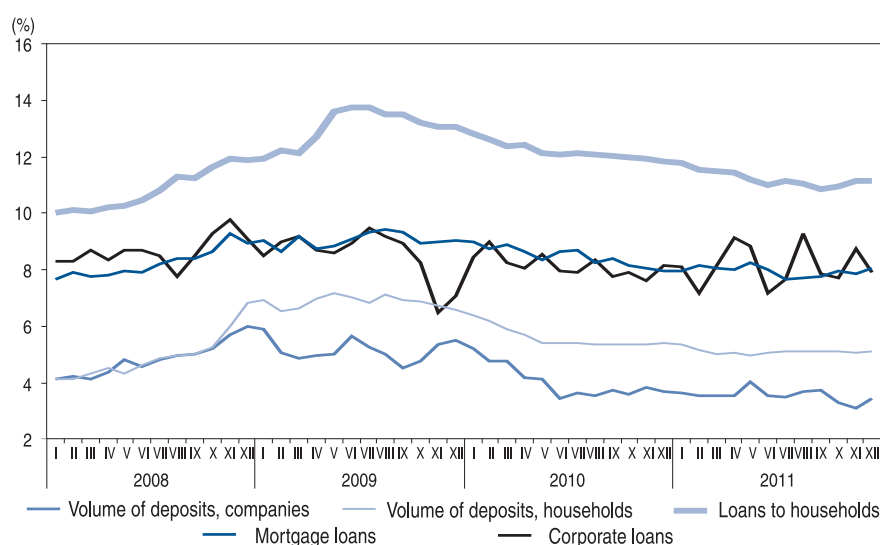
Domestic interest rates were among the important factors influencing the dynamics of lending. The downward trend of interest rate levels, which was more pronounced in 2010, wore out in 2011. As of the end of December, interest rates on housing loans were back up, gravitating towards their pre-crisis levels, with a minimal increase of 6 BPS from the end of 2010. At the same time, prices of loans to companies and, to a larger extent, consumer loans, remained relatively high, although on an annual basis they registered decreases of 0.2 and 0.7 p.p., respectively. Household deposits were

## Loans for Private Sector



Sources: BNB, MF.

the main source of financing for banks over the past year, which explains also why deposit rates remained relatively high. The trend can be explained with the desire of banks to turn primarily to their internal resources to meet their financing needs, since the option of attracting foreign capital, which was common practice earlier on, proved to be unsustainable in the long run. The total amount of deposits at the end of December increased by 13.2% on an annual basis, mostly due to non-financial undertakings and households. Both institutional sectors were net savers during the year and generally such a trend does not emerge in the sector of non-financial undertakings. The main factors enabling companies to accumulate savings included their improved financial conditions as a result of income earned from exports, and the turnaround in domestic demand. The increase in the net worth of households was supported by the almost zero annual growth in lending, while the high interest rates on loans served as a factor in the increase of assets, almost 93% of which were deposits.



**Weighted Average Interest Rate on Loans and Deposits**

Sources: BNB, MF.

Despite the adverse effect of a range of factors, by an adequate management of their balance sheets and cash flows, the Bulgarian banking system was one of the most highly capitalised in the European Union, and ranked relatively high in terms of liquidity and profitability. At the end of December, total capital adequacy was 17.5%, and it remained unchanged compared to December, 2010. The liquid assets ratio reached 25.6%, against 24.4% a year earlier. By maintaining a higher capital ratio, banks managed to set up an adequate capital buffer of BGN 2.9 billion. The banking system ended 2011 with a net profit of BGN 586.1 million.

# **Domestic Government Debt**

In 2011, the debt issuance policy of the Ministry of Finance was aligned both with the Government's policy in support of a stable economic development and maintaining Bulgaria's public finance at sustainable levels, and with the main strategic goals concerning government debt management for the period 2009 – 2011.

In an economic and financial environment marked by extremely high risk, Bulgaria's debt policy was focused on ensuring reliable, timely and efficient financing for the public budget through the active participation of the government as an issuer of government securities and strengthening the role of government securities as one of the main instruments for financing the borrowing needs of the state. One of the fundamental goals set for the Ministry's issuance policy in 2011 was to provide transparent and fair market-oriented financing at a minimum cost and an optimal level of risk by implementing an active, flexible issuance policy, adequate to the financial situation, aimed at extending the range of instruments offered, diversifying their maturity and currency structure, and employing innovative instruments, including repurchase and switch issue auctions, as part of its active policy of managing domestic debt. The achievement of that goal determined the market-oriented behaviour of MF in its capacity of government securities issuer and strengthened Bulgaria's positions as one of the most stable debt issuers in the region, which in its turn provided objective conditions for strengthening the positive trends in the market for Bulgarian government securities.

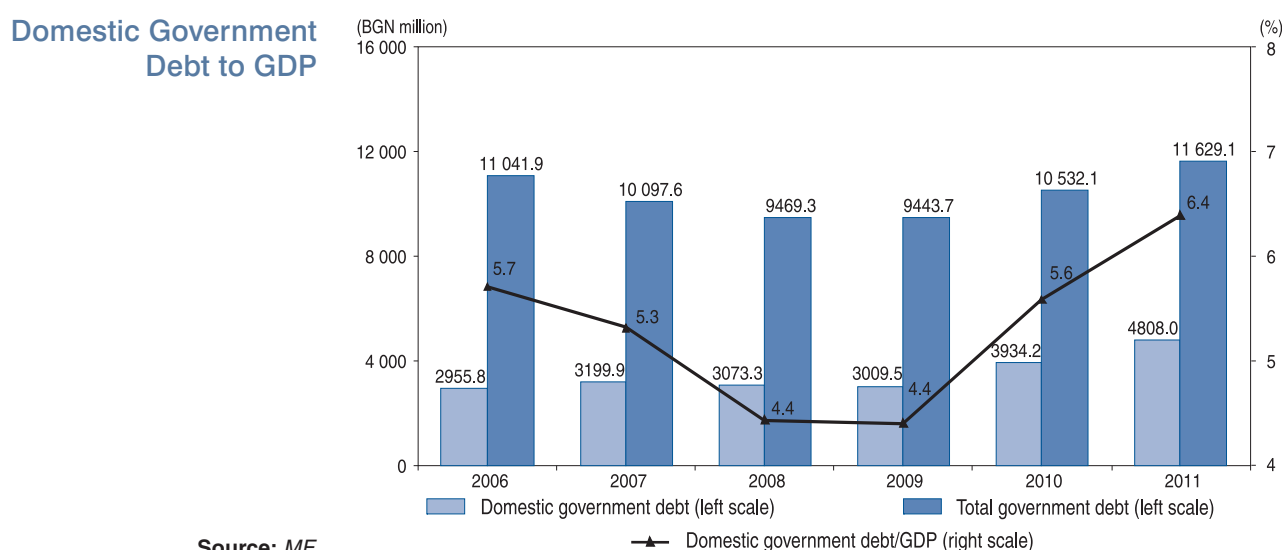
The Ministry of Finance continued its policy of issuing government securities for the domestic market as a matter of priority. Interest in the offerings of central government debt instruments grew over the year, and translated into the offering of benchmark issues along the entire range of the debt curve. The active issuance policy of the Ministry of Finance in the primary market aimed at diversifying the currency and maturity structures by offering issues denominated and payable in euros, and in the context of the well-established practice of reopening issues in circulation, this facilitated the improvement of market liquidity and domestic debt structure.

In 2011, the demand for government securities considerably exceeded supply. The annual averages for the various bid-to-cover ratios by type of security were the following: for 3-month treasury bills: 2.94, for 6-month treasury bills: 2.89, for government securities with a maturity of 3 years and 6 months: 2.12, for EUR-denominated government securities with a maturity of 5 years: 2.56, for 7-year government securities: 1.96<sup>1</sup>, for 10-year bonds: 0.62<sup>2</sup>, and for government securities with a maturity of 10 years and 6 months: 2.43. As a matter of priority, mid-term and long-term government securities with fixed-rate coupons were issued.

<sup>1</sup> The bid-to-cover ratio shown above for the 7-year issue includes the repurchase operation via a switch issue of government securities carried out on 24.10.2011.

<sup>2</sup> The bid-to-cover ratio shown above for the 10-year bonds is the result of the repurchase operation via a switch issue of government securities carried out on 28.11.2011.

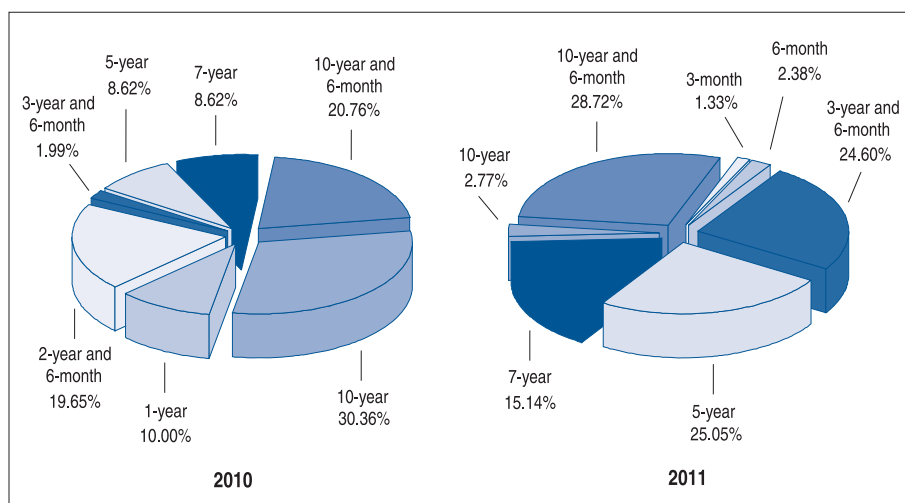
The nominal amount of domestic government debt at the end of 2011 stood at BGN 4808.0 million, which was 6.4% of GDP. Of that, debt under government securities issued by auction was BGN 4,220.5 million, government securities issued for the purposes of the structural reform amounted to BGN 252.5 million, and debt undertaken under the domestic government loan was BGN 335.0 million, respectively. In percentage, government securities issued by auction accounted for 87.8% of the total amount of domestic government debt, government securities issued for the purposes of the structural reform were 5.2%, and the domestic government loan was 7.0%.



In 2011, the Ministry of Finance continued to implement a flexible issuance policy adapted to the current market situation and responding to investor demand, and placed government securities with a variety of maturities on the domestic market. A total of 24 auctions for the sale of government securities, 2 auctions for repurchasing of government securities against payment, and 2 auctions for repurchasing of government securities against switch issues were held. The total nominal value of issued government securities was BGN 1,124.2 million.<sup>3</sup> Within the total amount of government securities issued in 2011, the relative share of short-term securities was 3.7%, the portion of mid-term government securities was 49.7%, and long-term GS accounted for 46.6%. During the year, the Ministry of Finance put in circulation one EUR-denominated issue as well, which triggered a lot of interest among the government securities market participants.

<sup>3</sup> This includes the value of government securities issued in 2011 by sale, in the amount of BGN 1067.9 million, and the total nominal value of government securities issued for repurchasing via a switch issue, in the amount of BGN 56.3 million.

As part of the active policy of government debt management, two operations for repurchasing debt in circulation by auction were held in 2011. At these two auctions for repurchasing government securities without any specified residual maturity, two 10-year bonds, issued in 2002 and 2003, respectively, were offered for repurchasing. The total volume of repurchased government securities was BGN 2.2 million. Domestic government debt in the same amount was respectively cancelled and the redemption profile of debt maturing in 2012 and 2013 was respectively smoothed out. In the second half of the year, two auctions were also held for repurchasing government securities without any specified residual maturity by replacing them with government securities from another issue (switch auctions). As a result of these two active operations, the repayment of debt maturing in 2012 of over BGN 56 million was rescheduled. An issue with original term of maturity of 5 years (source bond) maturing on 24.01.2012 was offered for repurchasing, and the total nominal value of bids placed and bids approved, respectively, at the two auctions was BGN 56.3 million, and the amount of domestic government debt payments falling due in 2012 was thus reduced by that amount. The high interest in government securities sale auctions is indicative of investor confidence in the Republic of Bulgaria as an issuer of sovereign debt.

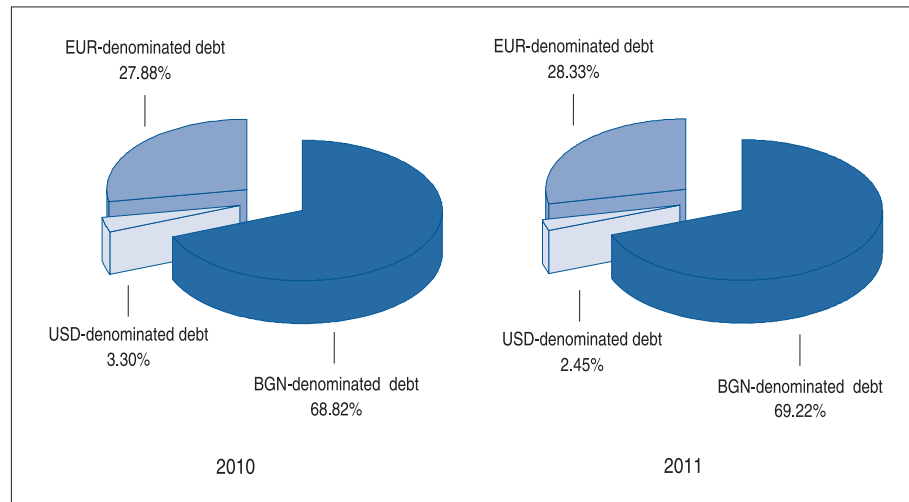


**Maturity Structure of Newly-issued GS**

Source: MF.

The currency structure of the domestic government debt exhibited a certain change from the previous year. The relative shares of BGN-denominated government securities and of EUR-denominated SG increased slightly, reaching 69.2% and 28.3%, respectively, while the share of USD-denominated debt dropped to 2.5%.

## Currency Structure of Domestic Government Debt

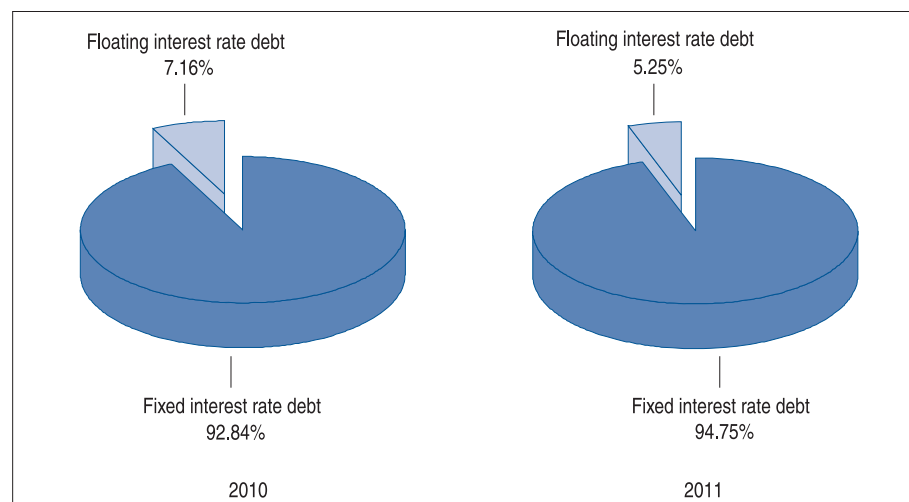


Source: MF.

In terms of the interest rate structure of debt, the trend of increasing the share of fixed-rate coupon debt continued into 2011, with that portion of the debt reaching 94.8%, from 92.8% at the end of 2010, at the expense of floating-rate coupon debt, which was reduced to 5.2%. The increase and decrease, respectively, amounted to about 2.0 p.p. compared to the previous year.

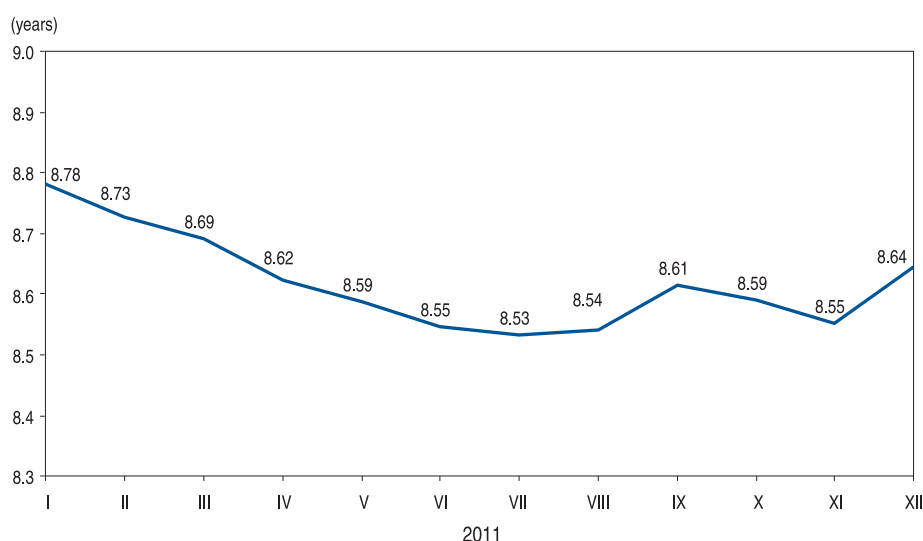
Treasury bonds newly issued during the year on the domestic market were all fixed-rate coupon debt.

## Interest Rate Structure of Domestic Government Debt



Source: MF.

In the review period, positive adjustments were made also in the average original maturity of government securities issued by auction. The average term of government securities went up from 8 years and 7 months to 8 years and 8 months, or by 1 month, compared to the value of that indicator at the end of the previous year.



**Average Primary Maturity of Auctioned GS in Circulation at the End of the Respective Month**

Source: MF.

## Domestic Financing

Net domestic financing through government securities during the year was a positive value, amounting to BGN 539.5 million.<sup>4</sup> Actual proceeds from government security issues in the period under review amounted to BGN 1,115.2 million, and government securities redemption payments stood at BGN 575.7 million, respectively. The nominal value of government securities issued on the domestic market in the year totalled BGN 1,124.2 million, with gross domestic financing through government securities in the following maturity segments: government securities with a maturity of 10 years and 6 months in the amount of BGN 322.9 million, 10-year bonds in the amount of BGN 31.1 million, 7-year bonds in the amount of BGN 170.2 million, and government securities with a maturity of 3 years and 6 months in the amount of BGN 276.5 million. Gross domestic financing also includes one mid-term issue of government securities with a maturity of 5 years (denominated and payable in euros) in the amount of EUR 144.0 million (BGN 281.6 million) released during the year. In the short-term segment, one treasury bill issue with a maturity of 3 months and one 6-month issue in the amount of BGN 15.0 million and BGN 26.8 million were put on the market.

<sup>4</sup> Based on principal amounts.



## Domestic Government Debt Dynamics

(BGN million)

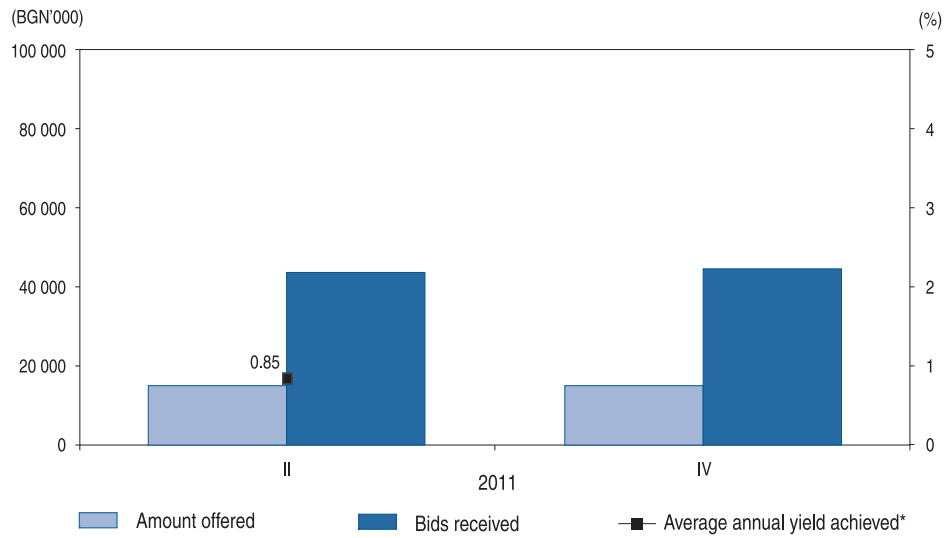
Structure	Amount as of 31 Dec. 2010	Increase	Decrease	Amount as of 31 Dec. 2011	Nominal increase (decrease)	Per cent increase (decrease)
<b>Domestic government debt</b>	<b>3 934.16</b>	<b>1 459.17</b>	<b>587.79</b>	<b>4 807.98</b>	<b>873.82</b>	<b>22.21</b>
<b>1. Government securities issues</b>	<b>3 652.45</b>	<b>1 124.17</b>	<b>556.16</b>	<b>4 220.46</b>	<b>568.01</b>	<b>15.55</b>
3-month	-	15.00	15.00	-	-	-
6-month	-	26.80	26.80	-	-	-
12-month	150.81	-	150.81	-	-150.81	-100.00
2-year and 6-month	296.36	-	-	296.36	-	-
3-year	-	-	-	-	-	-
3-year and 6-month	30.00	276.51	-	306.51	276.51	921.70
5-year	837.80	281.64	281.32	838.12	0.32	0.04
7-year	210.00	170.23	80.00	300.23	90.23	42.97
10-year	1 160.92	31.09	2.23	1 189.78	28.86	2.49
10-year and 6-month	313.11	322.90	-	636.01	322.90	103.13
15-year	653.45	-	-	653.45	-	-
<b>2. Government securities issued for structural reform</b>	<b>281.71</b>	<b>-</b>	<b>31.63</b>	<b>252.52</b>	<b>-29.19</b>	<b>-10.36</b>
19-year	0.28	-	0.28	0.00	-0.28	-100.00
20-year	147.03	-	16.34	130.70	-16.34	-11.11
24-year	0.89	-	0.13	0.76	-0.13	-14.29
25-year	133.51	-	14.89	121.05	-12.45	-9.33
<b>3. Domestic government loans (State Fund Agriculture)</b>	<b>-</b>	<b>335.00</b>	<b>-</b>	<b>335.00</b>	<b>335.00</b>	<b>-</b>

Note: Data at nominal value.

Source: MF.

## Treasury Bill Issues

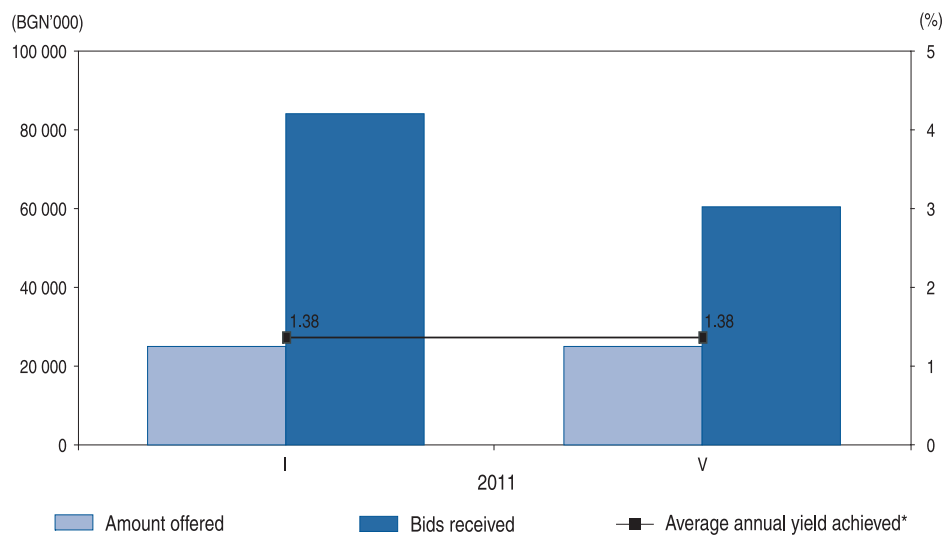
Short-term securities issued during the year included 3-month and 6-month discount government securities; their total nominal value amounted to BGN 41.8 million, with offers of BGN 80.0 million. The total nominal value of bids placed reached BGN 232.8 million. At the two auctions held for 3-month treasury bills, investors placed bids exceeding the government securities offered almost by a factor of three (average bid-to-cover ratio of 2.94). At the two auctions for 6-month treasury bills, the number of bids placed by investors was also almost three times more than the government securities on offer (average bid-to-cover ratio 2.89). The average annual yield achieved at the auctions for 3-month and 6-month treasury bills was 0.85% and 1.38%, respectively. A very high interest on the part of all primary dealers in government securities was noted at all auctions.



## 3-month Government Securities Auctions

\* Average annual yield is calculated on the basis of the yield to maturity.  
**Note:** Ministry of Finance did not approve bids received for auction held on 18 April 2011.

Source: MF.



## 6-month Government Securities Auctions

\* Average annual yield is calculated on the basis of the yield to maturity.

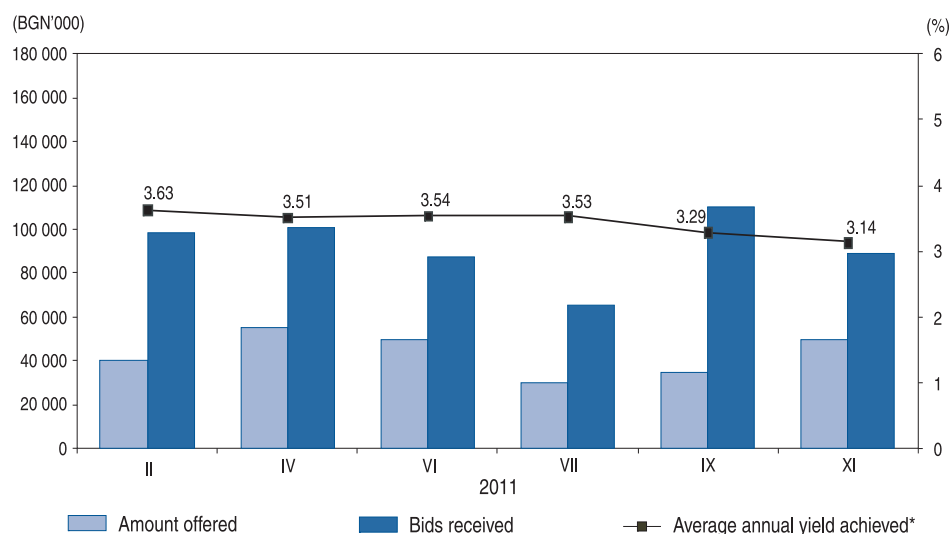
Source: MF.

## Treasury Bond Issues

The total nominal value of treasury bonds issued during the year amounted to BGN 1,082.4 million. In 2011, government securities with a maturity of 3 years and 6 months, 5-year EUR-denominated government securities, 7-year, 10-year, and government securities with a maturity of 10 years and 6 months were issued.

Issued government securities with a maturity of 3 years and 6 months were represented by one issue, with a total nominal value of BGN 276.5 million. Interest in securities with a maturity of 3 years and 6 months was high, with a total volume of bids of BGN 551.8 million, or a bid-to-cover ratio of 2.12. The yield achieved on the primary market for these government securities ranged between 3.14% and 3.63%.

### 3-year and 6-month Government Securities Auctions

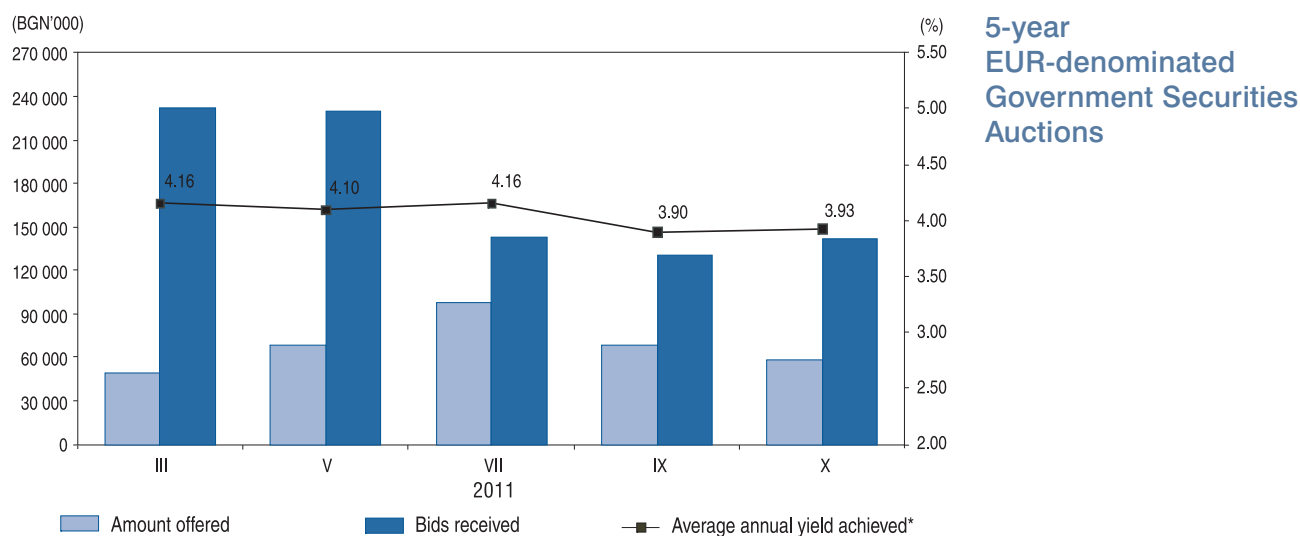


\* Calculated according to ISMA-International Yield (%).

Note: The original maturity of the issue is 3 years and 6 months but the residual term to maturity by 7 November 2011 is approximately 2 years and 7 months.

Source: MF.

In March 2011, an auction for the sale of EUR-denominated government securities with an original maturity of 5 years was held.



\* Calculated according to ISMA-International Yield (%).

**Note:** Ministry of Finance did not approve bids received for auction held on 5 December 2011.

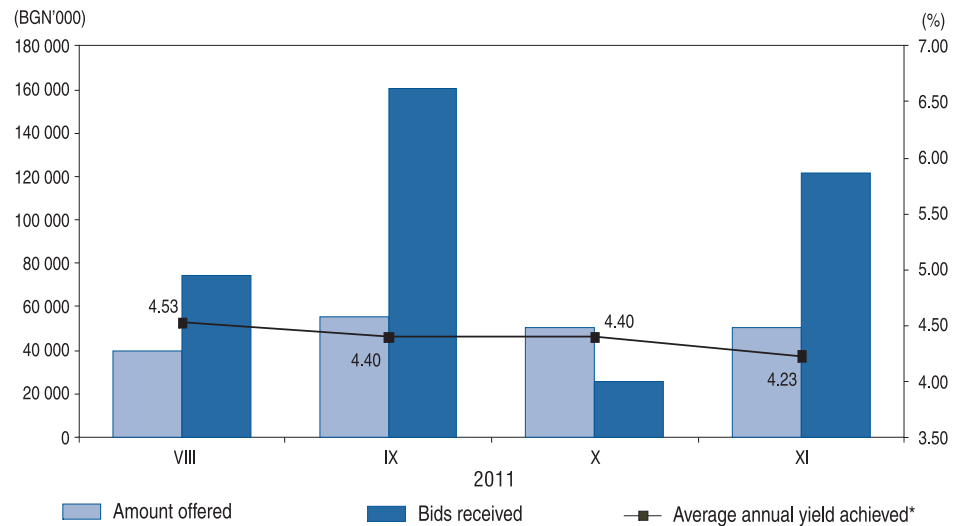
**Source:** MF.

Newly issued government securities with a maturity of 5 years were represented by one issue (2011) with a total nominal value of EUR 144.0 million (BGN 281.6 million) placed on six auctions in the course of the year. Interest in these securities was higher at the original issue and first reopening, and the total volume of bids at the six auctions was BGN 876.7 million, with a weighted average bid-to-cover ratio for the original issue and reopenings was 2.56. The yield achieved on the primary market for these government securities ranged between 3.90% and 4.16%.

During the year, one issue of 7-year bonds with a nominal value of BGN 170.2 million was put into circulation. It was released on four auctions, and these government securities typically met with high demand on the market. The total volume of bids was BGN 381.7 million, and the average bid-to-cover ratio was 1.96. The highest interest in that issue was registered in Q3, taking into account the bid-to-cover ratio of 2.91 achieved during the September reopening of the issue.

The yield on 7-year bonds achieved on the primary market ranged between 4.23% and 4.53%.

## 7-year Government Securities Auctions



\* Calculated according to ISMA-International Yield (%).

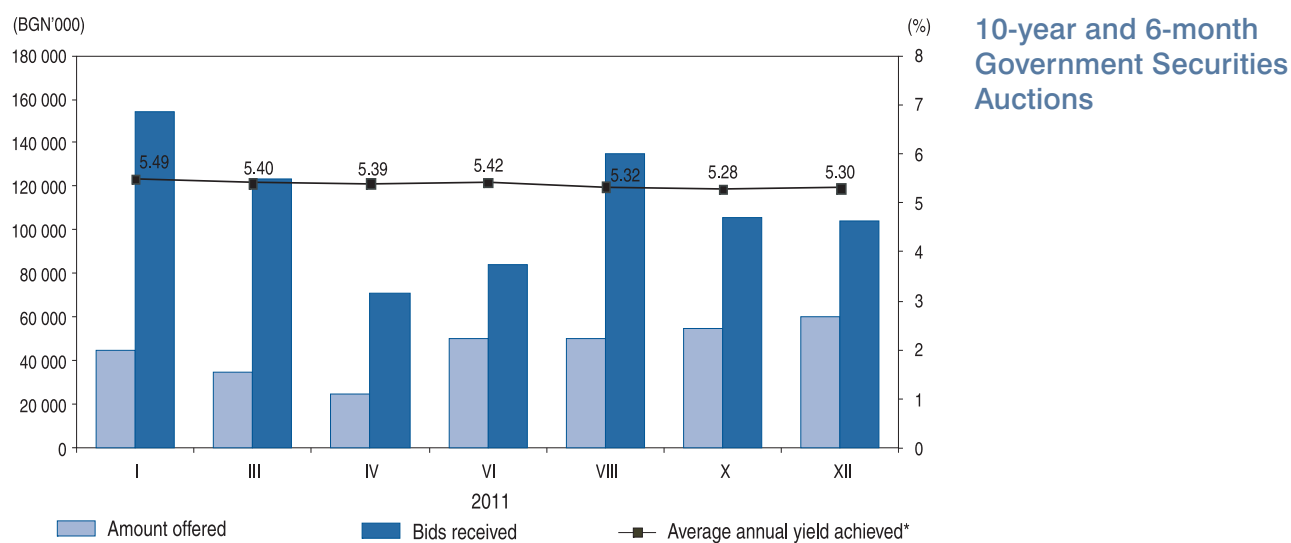
**Note:** The original maturity of the issue is 7 years but the residual term to maturity by 21 November 2011 is approximately 5 years and 3 months.

Source: MF.

The government securities with a maturity of 10 years (issue 2006) registered a total nominal value of BGN 31.1 million as a result of the auction held in November. Interest in these securities was not high, considering the bid-to-cover ratio of 0.62 achieved by the issue. The yield of 10-year bonds achieved on the primary market was 3.96%.

Government securities with a maturity of 10 years and 6 months were represented by one issue (2011), sold on seven auctions. The total nominal value was BGN 322.9 million, and the offering amounted to BGN 320.0 million. Interest in these bonds remains high and constant throughout the year. The volume of bids received was BGN 777.3 million, or an average bid-to-cover ratio of 2.43. The yield of the treasury bonds with a maturity of 10 years and 6 months ranged between 5.28% and 5.49%.

The April auction for government securities with a maturity of 3 months and the December auction for government securities with a maturity of 5 years (denominated in euros) were both cancelled, since the yield sought by the participants did not correspond to the targets set in the issuance policy. In consideration of the fact that the government has a sufficient array of financing options available, the Ministry of Finance decided to decline all bids received at those two auctions.



\* Calculated according to ISMA-International Yield (%).

Source: MF.

Overall, actions relating to government borrowing in the form of government securities from the domestic market in the review period were in line with the set objectives of implementing an anti-cyclical and restrictive fiscal policy aimed at achieving the main goal of the budget policy for the following year: to keep the deficit under the Consolidated Fiscal Programme below the threshold of 3% of GDP, in accordance with the Stability and Growth Pact.

## Domestic Government Debt Service

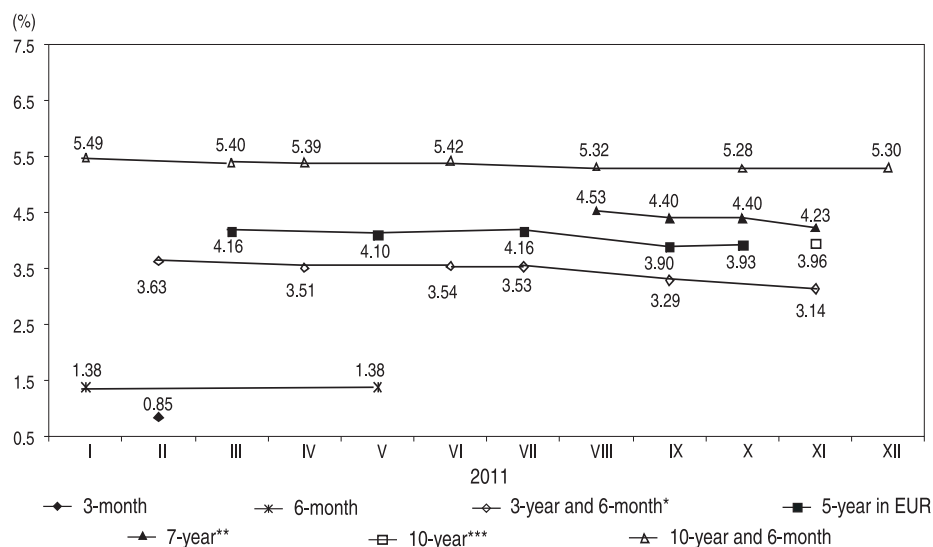
The total amount of debt amortisation payments made in 2011 was BGN 746.5 million, including BGN 575.7 million in redemptions of principal and BGN 170.8 million in interest payments. The largest relative share – 98.8%, or BGN 168.7 million, is that of interest payments on government securities issued to finance the public budget, followed by interest payments on government securities issued for the purposes of the structural reform – 1.2%, or BGN 2.1 million.

## Auctions for Government Securities Issued in 2011

Auction date	Issue date	Issue number	Currency	Maturity (in months)	Maturity date	Interest rate	Amount offered	Bids received	Bids approved at nominal value	Bids approved at sell price	Average price per 100 units of nominal	Min price approved per 100 units of nominal	Average annual yield (%)*	Max yield approved (%)
10.01.2011	12.01.2011	BG3010011008	BGN	6	12.07.2011	0.00	25 000 000.00	84 050 000.00	25 000 000.00	24 826 500.00	99.31	99.25	1.38	1.50
17.01.2011	19.01.2011	BG2040011210	BGN	126	19.07.2021	5.00	45 000 000.00	154 220 000.00	45 000 000.00	43 510 425.01	96.69	96.52	5.49	5.51
07.02.2011	09.02.2011	BG301011006	BGN	3	09.05.2011	0.00	15 000 000.00	43 500 000.00	15 000 000.00	14 967 884.99	99.79	99.76	0.85	0.97
21.02.2011	23.02.2011	BG203011013	BGN	42	22.06.2014	3.45	40 000 000.00	98 450 000.00	40 000 000.00	39 812 020.00	99.53	99.22	3.63	3.73
07.03.2011	09.03.2011	BG2040011210	BGN	126	19.07.2021	5.00	35 000 000.00	123 750 000.00	35 000 000.00	34 075 369.98	97.36	97.08	5.40	5.44
28.03.2011	30.03.2011	BG2030011113	EUR	60	30.03.2016	4.00	25 000 000.00	118 670 000.00	25 000 000.00	24 880 515.01	99.52	99.42	4.16	4.18
Translated into levs														
04.04.2011	06.04.2011	BG2030110113	BGN	42	22.06.2014	3.45	48 895 750.00	232 098 346.10	48 895 750.00	48 662 057.67	99.90	99.61	3.51	3.61
18.04.2011	20.04.2011	BG3010211004	BGN	3	20.07.2011	0.00	15 000 000.00	44 700 000.00	0.00	0.00	0.00	0.00	0.00	0.00
27.04.2011	29.04.2011	BG2040011210	BGN	126	19.07.2021	5.00	25 000 000.00	70 950 000.00	22 900 000.00	22 318 625.00	97.46	97.19	5.39	5.43
09.05.2011	11.05.2011	BG301031002	BGN	6	11.11.2011	0.00	25 000 000.00	60 550 000.00	1 800 000.00	1 787 380.00	99.30	99.29	1.38	1.40
16.05.2011	18.05.2011	BG2030011113	EUR	60	30.03.2016	4.00	35 000 000.00	117 520 000.00	35 000 000.00	34 923 940.00	99.78	99.68	4.10	4.12
Translated into levs														
06.06.2011	08.06.2011	BG2030110113	BGN	42	22.06.2014	3.45	50 000 000.00	229 849 141.60	68 454 050.00	68 305 289.57	99.86	99.76	3.53	3.57
20.06.2011	22.06.2011	BG2040011210	BGN	126	19.07.2021	5.00	50 000 000.00	83 950 000.00	50 000 000.00	49 912 885.00	98.83	96.96	5.42	5.47
04.07.2011	06.07.2011	BG2030011113	EUR	60	30.03.2016	4.00	50 000 000.00	72 800 000.00	14 000 000.00	13 934 165.00	99.53	99.44	4.16	4.18
Translated into levs														
25.07.2011	27.07.2011	BG2030110113	BGN	42	22.06.2014	3.45	30 000 000.00	142 384 424.00	27 381 620.00	27 252 857.93	99.86	99.76	3.53	3.57
08.08.2011	10.08.2011	BG2040011210	BGN	126	19.07.2021	5.00	50 000 000.00	134 800 000.00	50 000 000.00	49 045 800.00	98.09	97.92	5.32	5.34
15.08.2011	17.08.2011	BG2040110210	BGN	84	17.02.2017	4.50	40 000 000.00	74 585 600.00	40 000 000.00	39 999 988.56	100.13	99.95	4.53	4.57
12.09.2011	14.09.2011	BG2030110113	BGN	42	22.06.2014	3.45	35 000 000.00	110 260 011.00	51 510 011.00	51 510 011.00	100.50	100.39	3.29	3.33
19.09.2011	21.09.2011	BG2040110210	BGN	84	17.02.2017	4.50	55 000 000.00	160 050 000.00	55 000 000.00	55 000 000.00	100.72	100.57	4.40	4.44
26.09.2011	28.09.2011	BG2030011113	EUR	60	30.03.2016	4.00	35 000 000.00	66 850 000.00	35 000 000.00	35 000 000.00	100.58	100.16	3.90	4.01
Translated into levs														
03.10.2011	05.10.2011	BG2040011210	BGN	126	19.07.2021	5.00	55 000 000.00	130 747 235.50	68 454 050.00	68 454 050.00	98.35	97.85	5.28	5.35
17.10.2011	19.10.2011	BG2030011113	EUR	60	30.03.2016	4.00	30 000 000.00	72 404 000.00	35 000 000.00	35 000 000.00	100.48	100.28	3.93	3.98
Translated into levs														
24.10.2011	26.10.2011	BG2040110210	BGN	84	17.02.2017	4.50	50 000 000.00	141 609 915.32	68 454 050.00	68 454 050.00	100.75	0.00	4.40	0.00
07.11.2011	09.11.2011	BG2030110113	BGN	42	22.06.2014	3.45	50 000 000.00	25 232 208.00	25 232 308.00	25 232 308.00	100.84	100.72	3.14	3.19
21.11.2011	23.11.2011	BG2040110210	BGN	84	17.02.2017	4.50	50 000 000.00	121 875 000.00	50 000 000.00	50 000 000.00	101.48	101.33	4.23	4.27
28.11.2011	30.11.2011	BG2040006210	BGN	120	04.01.2016	3.50	50 000 000.00	31 090 000.00	31 090 000.00	30 592 560.00	98.40	0.00	3.96	0.00
05.12.2011	07.12.2011	BG2030011113	EUR	60	30.03.2016	4.00	35 000 000.00	32 550 000.00	0.00	0.00	0.00	0.00	0.00	0.00
Translated into levs														
12.12.2011	14.12.2011	BG2040011210	BGN	126	19.07.2021	5.00	60 000 000.00	104 015 000.00	65 000 000.00	63 881 151.00	98.28	97.61	5.30	5.39
<b>Total for 2011</b>							<b>1 315 724 300.00</b>	<b>2 915 129 148.02</b>	<b>1 124 171 839.00</b>	<b>1 115 239 673.70</b>				

\* Yield of treasury bonds is calculated according to the methodology applied by the MF and the interest convention (ACT/ACT) adopted as of 1.01.2001, using the ISMA-International Yield (%) formula.

Source: MF.



**Yield of GS Achieved at Primary Market**

\* The original maturity of the issue is 3 years and 6 months but the residual term to maturity by 7 November 2011 is approximately 2 years and 7 months.

\*\* The original maturity of the issue is 7 years but the residual term to maturity by 21 November 2011 is approximately 5 years and 3 months.

\*\*\* The original maturity of the issue is 10 years but the residual term to maturity by 28 November 2011 is approximately 4 years and 1 month.

Source: MF.

## Government Securities Issued for the Purposes of the Structural Reform

The nominal value of government securities outstanding issued for the purposes of the structural reform amounted to BGN 252.5 million at the end of 2011. The debt reduction by BGN 29.2 million from the previous year was the result of regular amortisation payments and foreign exchange differences.

Redemptions of principal amounts of government securities issued for the purposes of the structural reform amounted to BGN 31.6 million during the year.

Interest expenditure on government securities issued for the purposes of the structural reform amounted to BGN 2.1 million at the end of 2011.



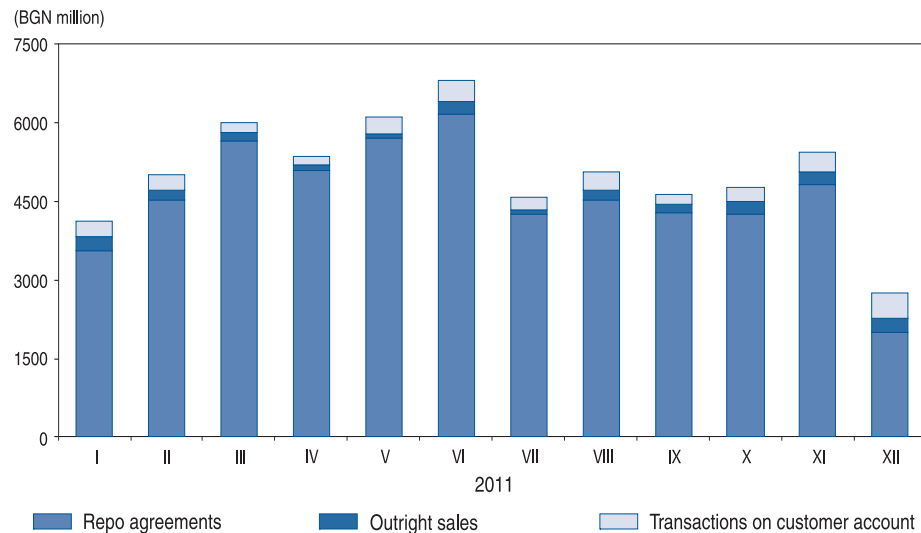
# **Secondary Market of Government Securities Overview**

In 2011, the secondary market of government securities was marked by brisk activity, which led to an increase in the number and volume of trades compared to the previous year. This was due to a stronger investment interest in the Bulgarian government debt instruments issued on the domestic market, such as low-risk financial instruments providing a good yield. Trading was influenced by the deepening crisis in the Eurozone as a result of the growing problems with the government debts of Portugal, Spain, Ireland and Greece, and the lack of suitable investment alternatives on the Bulgarian capital market.

The total amount of trades registered during the year reached BGN 77,557.9 million in nominal value, with the segment of repo transactions continuing to prevail (70.7%), followed by freeze/unfreeze of government securities (21.7%), transactions with and between clients of the participants in ESROT, the electronic system for registration and support of trading in dematerialised government securities (4.8%) and final buy/sell transactions (2.8%). Compared to the previous year, the volume of bond trades on the secondary market grew at 20%, unlike freeze/unfreeze transactions, which dropped by 34%. As a result of the increased activity, the liquidity ratio of the secondary market for government securities for the year reached 13.6%, from 12.9% in 2010. The market was considerably more dynamic in the first half of the year, with peaks of trading volumes in May and June. In the second half of the year, trading volumes dropped slightly and remained at that level. As usual, trading tended to be most active on the days of acquiring newly-issued government securities, and when principal and interest payments were made on maturing securities. On the interbank market, the predominant type of transactions were repos DVP on payment accounts (82.1% of their total volume), the most popular being overnight trades (56.5%) for the purposes of ensuring daily liquidity. Although the volume of final buy/sell transactions and transactions with and between clients of the participants in ESROT went up by 40.3% and 19.0%, respectively, compared to 2010, their share remained considerably smaller. Trading included government securities along the entire yield curve, with a clear prevalence of long-term government securities. The average annual yield of the the long-term benchmark issue with a maturity of 10 years and 6 months declined gradually on the secondary market from 5.56% in January to 5.23% in December, which is yet another proof that securities issued on the domestic market are viewed positively by investors. At the same time, trading in government securities, denominated and payable in euros, was weak and remained at a relatively constant level, between 5% and 8% of total volume, despite the pronounced interest in those debt instruments in the primary market.

## Secondary Market of Government Securities Overview

### Volume of Transactions in Tradeable Government Securities



**Notes:** 1. Volume of repo agreements include reverse repo agreements and those concluded during the current day.

2. Transactions in government securities denominated in foreign currency are in BGN at BNB exchange rate of the respective currency on the day of transaction.

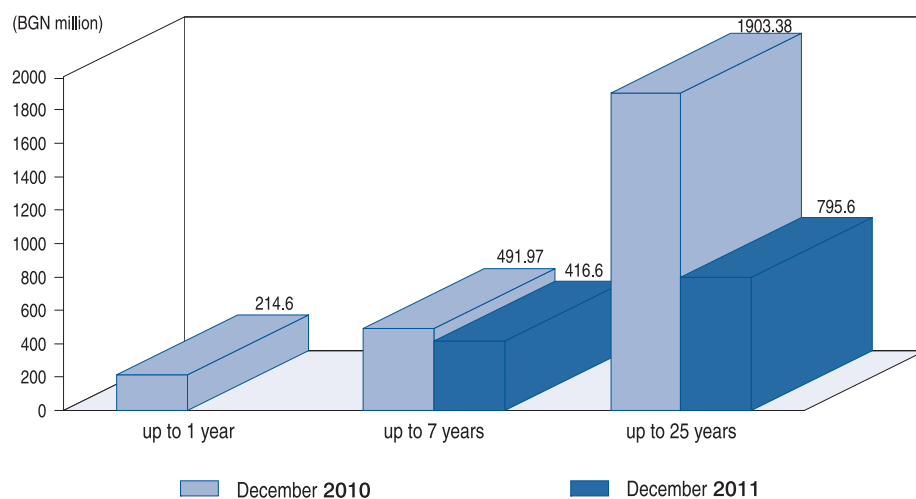
**Source:** BNB.

In 2011, as in previous years, there were no refusals due to unavailability of funds in the payment accounts of market participants with the Government Securities Depository, and the number of refusals due to unavailability of government securities was negligible, only 0.13% of the total number of trades. At the end of the year, government securities in the amount of USD 400 thousand issued under ZUNK<sup>1</sup> were cancelled, for ZUNKs accepted by the MF for repayment of liabilities to the government that had arisen under the said Act.

In 2011, as a result of MF's issuance policy and the brisk trading on the secondary market, investments in government securities showed an increase for all government security holders, and exposures in government securities in the various categories remained relatively stable. At the end of 2011, government securities in holder portfolios were distributed as follows:

- For government securities issued for the purposes of financing the public budget deficit, the largest market segment belonged to banks (53.6%), followed by insurance companies and pension funds (25.8%), resident non-banking financial institutions, companies and individuals (19.7%) and foreign investors (0.9%);
- For government securities issued for the purposes of the structural reform, the largest share was again that of banks (53.6%), followed by resident non-banking financial institutions, companies and individuals (37.5%), insurance companies and pension funds (9.0%), and foreign investors (0.01%).

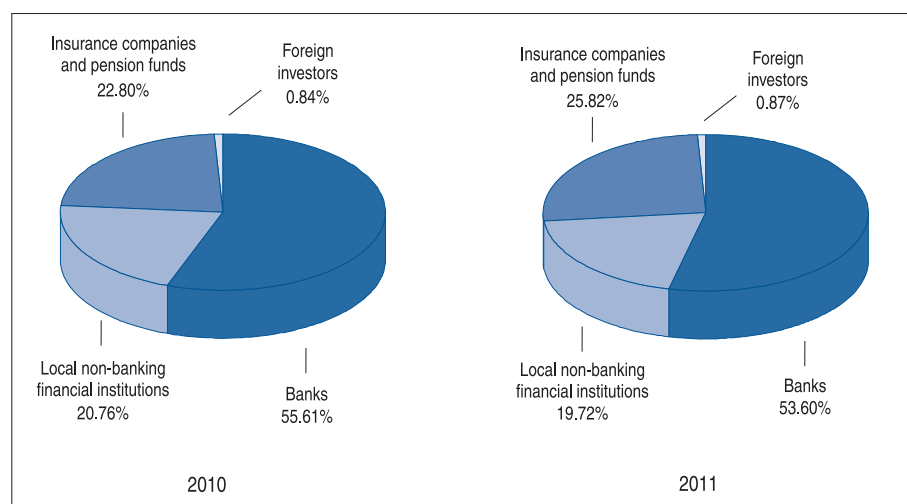
<sup>1</sup> Law on Settlement of Non performing Credits Negotiated prior to 31 December 1990.



**Maturity Structure of Government Securities Transactions on the Interbank Market**

**Notes:** 1. Transactions in government securities denominated in foreign currency are in BGN at BNB exchange rate for the last business day of corresponding period.  
2. Volume of repo agreements do not include reverse repo agreements.

**Source:** BNB.



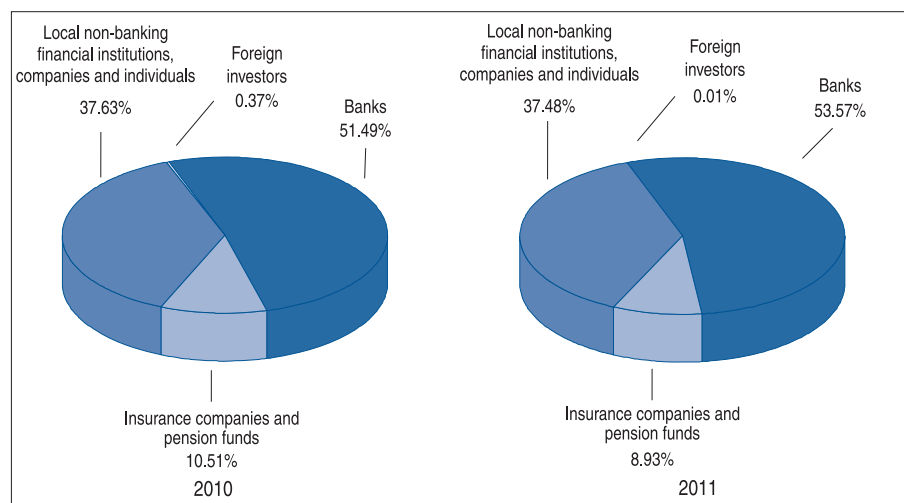
**Holders of Government Securities Issued for Financing the Budget Deficit**

**Notes:** 1. Frozen by holders Government Securities are included.  
2. Based on data of the BNB and ESROT participants.  
3. The lev equivalent of government securities denominated in foreign currency is based on BNB exchange rate quoted for 31 December of corresponding year.

**Source:** BNB.

# Secondary Market of Government Securities Overview

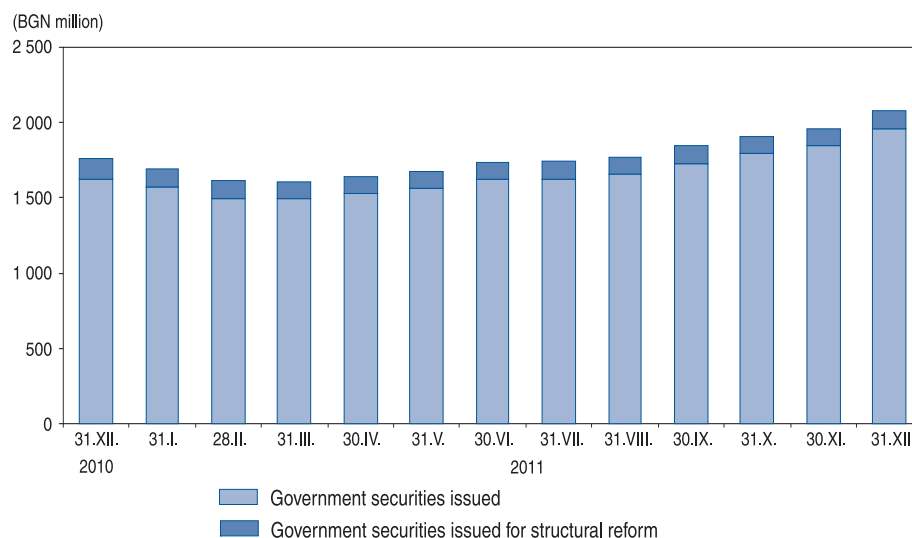
## Holders of Structural Reform Government Securities



- Notes:**
1. Frozen by holders Government Securities are included.
  2. The lev equivalent is based on BNB exchange rate quoted for 31 December of corresponding year.
  3. Based on data of the BNB and ESROT participants.

Source: BNB.

## GS Investments by Non-banking Financial Institutions, Companies and Individuals



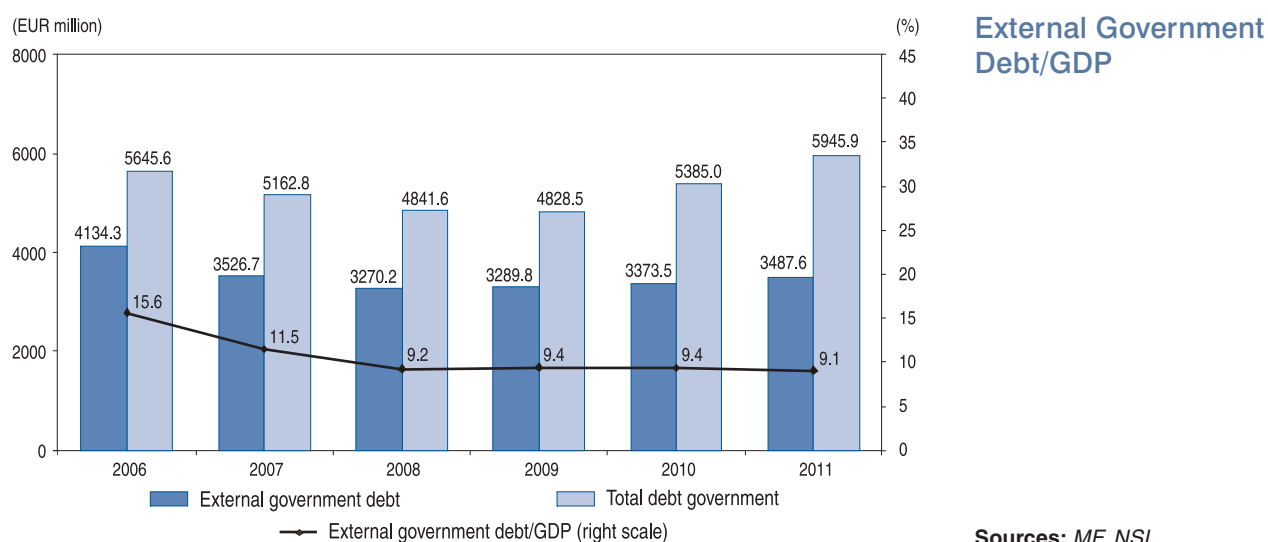
Source: BNB.

**Note:** The lev equivalent of government securities denominated in foreign currency is based on BNB exchange rate for the last business day of corresponding period.



# **External Government Debt**

External government debt at the end of 2011 stood at EUR 3,487.6 million. In nominal terms, it increased by EUR 114.1 million in comparison to its level at the end of the previous year. The rise in external government debt was due primarily to the positive net external financing in the amount of EUR 76.8 million. Compared to the previous year, the external government debt/GDP ratio showed a decrease and stood at 9.1%.

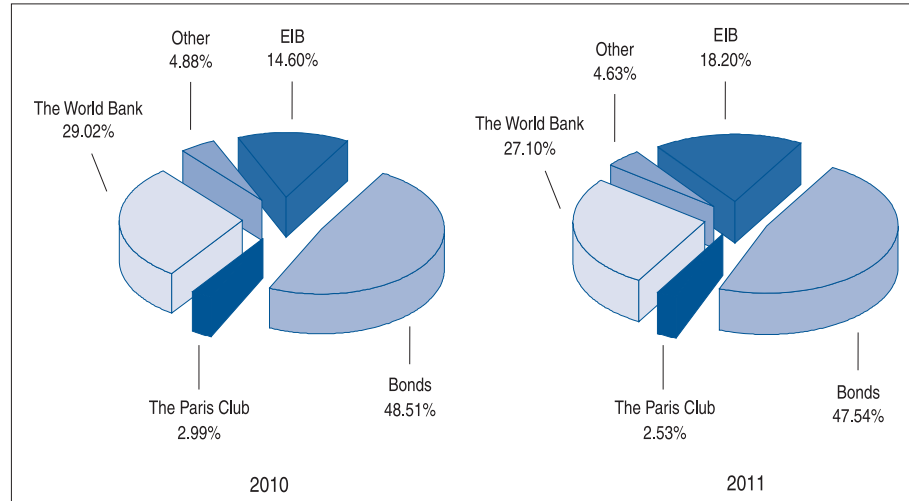


Compared to the end of 2010, certain changes can be observed in the external debt structure by type of instrument and by creditor. The loan disbursements from the European Investment Bank (EIB) during the year, in the amount of BGN 350.0 million, brought an increase of 3.6 p.p. to the relative share of debt to EIB in the total amount of external government debt, taking it up to 18.2%. The purpose of those loan disbursements was to implement investment projects in areas of strategic importance for the economy. A decrease was observed for loans from the World Bank (by 1.9 p.p.) which account for 27.1% of the total amount of external government debt. The decrease is due to the regular amortisation payments made during the year. As of the end of 2011, the relative share of liabilities to other creditors dropped, and amounted to 4.6%.

As of the end of 2011, the largest share in the structure of external government debt was that of bonds issued on the international capital markets (47.5%), and debt to the World Bank (27.1%). The share of debt to the rest of creditors was 25.4%.



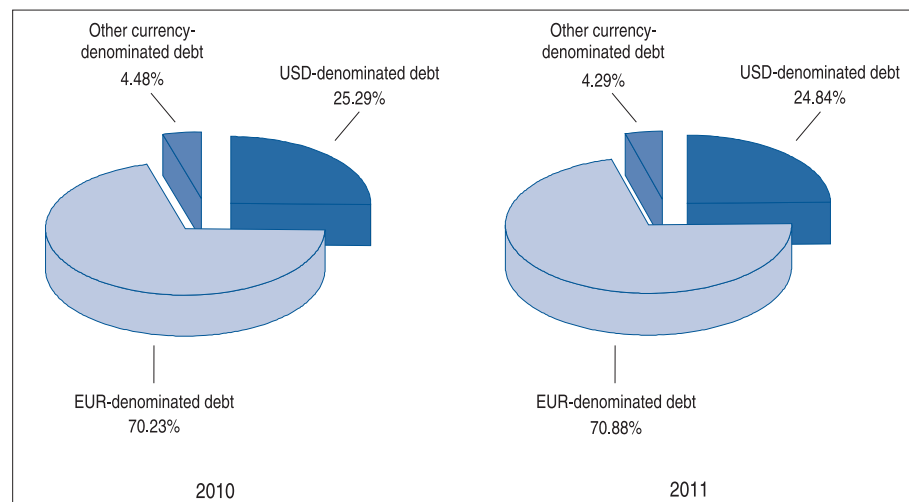
## External Government Debt by Creditors



Source: MF.

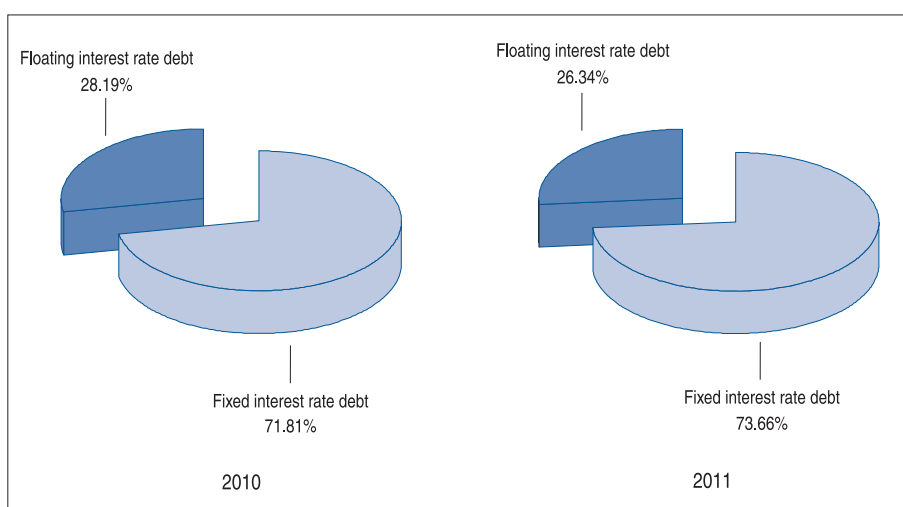
The currency structure of debt experienced certain changes during the year as a result of the implemented policy of borrowing funds primarily in euros, and the payments made in US dollars, Japanese yens and Kuwaiti dinars. The USD-denominated debt, and debt denominated in other foreign currencies declined slightly, compared to the end of 2010, reaching 24.8% and 4.3%, respectively. The EUR-denominated portion of the debt was still predominant (70.9%). The 2011 increase was due largely to the positive net financing in euros.

## Currency Structure of External Government Debt



Source: MF.

The interest rate structure of external government debt in recent years has been dominated by fixed rate debt, and it retained its high relative share in 2011 as well. Fixed-rate coupon debt grew by 1.9 p.p., reaching 73.7%, while floating interest debt went down to 26.3%.



**Interest Rate Structure of External Government Debt**

Source: MF.

## Loans Received

New external financing received in 2011 amounted to BGN 410.5 million, including funding in the amount of BGN 161.1 million under the Structural Programme Loan from the European Investment Bank, and BGN 249.4 million in government investment loans. During the year, the highest rates of absorption of government investment loans were registered for EIB loans.

Net external financing for the year was a positive value, and amounted to BGN 150.2 million.

## External Government Debt

### New External Financing and External Debt Repayments in 2011

(BGN million)

Structure	Loans Received (tranches)	Repayments, including		
		principal	interest	total
<b>External government debt</b>	<b>410.5</b>	<b>260.3</b>	<b>335.8</b>	<b>596.1</b>
I. Bonds	-	-	247.4	247.4
1. EUR-denominated global bonds (2013)	-	-	120.1	120.1
2. USD-denominated global bonds (2015)	-	-	127.4	127.4
II. Credit facilities	410.5	260.27	88.4	348.7
1. Paris Club	-	24.6	6.5	31.1
2. World Bank	-	90.0	24.1	114.0
2.1. World Bank	-	82.5	22.8	105.3
2.2. JBIC	-	7.4	1.3	8.7
3. European Union	161.1	-	3.5	3.5
3.1. European Union	-	-	-	-
3.2. EIB	161.1	-	3.5	3.5
4. Other	-	-	-	-
5. Government investment loans	249.4	128.0	54.1	182.1
5.1. World Bank	59.8	31.2	7.3	38.5
5.2. EIB	188.9	72.7	37.3	109.9
5.3. EBRD	-	-	0.0	0.0
5.4. Other	0.7	24.2	9.5	33.7
6. Government guarantees called	-	17.7	0.3	14.7
6.1. World Bank	-	20.6	0.3	20.9
6.2. EBRD	-	3.0	-	3.0

**Note:** The lev equivalents of new external financing and repayments are based on the BNB central rate for the respective foreign currency to the Bulgarian lev valid until 4 pm on the day of the respective payment.

Source: MF.

### External Government Debt Service

The debt policy implemented over the past several years, and the resulting currency and interest rate structure of external government debt have minimised risks associated with interest- and exchange rate fluctuations in international markets, and reduced debt servicing costs.

Repayments made during the year in connection with external government debt amounted to BGN 596.1 million, of which BGN 260.3 million in principal redemptions, and BGN 335.8 million in interest payments.

Of the total principal amounts repaid under external debt, repayments towards government investment loans amounted to BGN 128.0 million, or 49.2%. Repayments towards government loans during the year amounted to BGN 114.6 million, and repayments on government guarantees called were BGN 17.7 million. Their respective shares in the total amount of annual amortisation payments on external debt were 44.0% and 6.8%. In interest paid, the breakdown was as follows: 73.7%, or BGN 247.4 million on global bonds; 16.1%, or BGN 54.1 million on government investment loans; 10.1%, or BGN 34.0 million on government loans, and 0.1%, or BGN 0.3 million on government guarantees called.

In terms of the agreed repayment schedules, the largest share of 2011 repayments in the structure by creditor belonged to repayments on debt to the World Bank, with BGN 141.8 million, followed by payments on loans from the European Investment Bank, with BGN 72.7 million, and on debt to other countries, with BGN 48.8 million.

In the total amount of interest payments, the largest portion was that of bonds issued on international capital markets, with BGN 247.4 million, or 73.7% of external interest payments. This was due to the fact that global bonds account for 47.5% of total external government debt. Next came interest paid on loans from the European Investment Bank, in the amount of BGN 40.8 million, the World Bank, with BGN 31.7 million, and other countries, with BGN 16.0 million (including payments to Germany as one of the Paris Club lenders).

All payments were made regularly and in line with the agreed repayment schedules and the terms of the respective credit facilities.

## External Government Debt

(EUR million)

Structure	as of 31.12.2010	as of 31.12.2011
<b>External government debt</b>	<b>3 373.5</b>	<b>3 487.6</b>
I. Bonds	1 636.5	1 658.1
1. EUR-denominated global bonds (2013)	818.5	818.5
2. USD-denominated global bonds (2015)	818.0	839.6
II. Credit facilities	1 737.0	1 829.5
1. Paris Club	100.7	88.1
2. World Bank	758.7	714.7
2.1. World Bank	730.3	688.1
2.2. JBIC	28.4	26.6
3. European Union	52.4	134.8
3.1. European Union	-	-
3.2. EIB	52.4	134.8
4. Other	-	-
5. Government investment loans	815.7	887.0
5.1. World Bank	210.6	225.4
5.2. EIB	440.2	500.0
5.3. EBRD	-	-
5.4. Other	164.8	161.6
6. Government guarantees called	9.5	4.9
6.1. World Bank	9.5	4.9

**Notes:** 1. Debt data based on nominal value.

2. Currency revaluation of debt into euros is based on BNB central rates for the respective foreign currencies to the Bulgarian lev quoted for the last business day of the period.

Source: MF.



# Government Debt

The government debt management policy implemented in 2011 was in line with the goals set in the Government Debt Management Strategy for the period 2009 – 2011 and the implementation tools specified, and was aimed at implementing a prudent and effective policy in terms of assuming new central government debt, in order to prevent any uncontrollable debt increase and any adverse effect on Bulgaria's fiscal and macroeconomic stability.

The main goal of this stable policy of debt management was to ensure the funding necessary for financing the Government's priorities, and refinancing for debt outstanding which keeping the level of government debt at reasonable levels and achieving a sustainable financial position.

The nominal government debt at the end of 2011 amounted to EUR 5,945.9 million, of which EUR 3,487.6 million in external debt, and EUR 2,458.3 million in domestic debt. In nominal terms, government debt registered an increase of EUR 560.9 million compared to its level as at the end of 2010. The main factors behind the government debt increase were the new domestic and external financing obtained during the year, and foreign exchange differences resulting from the currency revaluation of debt, in the amount of EUR 34.5 million. At the end of 2011, government debt in GDP terms was 15.5%, which is an increase by 0.6 p.p. from the level reported at the end of 2010 (14.9%). Despite the increase, performance under this indicator remains considerably below the 25% limit set in the Government Debt Management Strategy effective for the period.

The negative effects of the economic crisis on the balance of payments continued into 2011, and for the third year in a row, a budget deficit was reported. In 2011, it amounted to BGN 1,487.4 million, representing a reduction, under the indicator of budget balance / GDP (cash basis), to 2.0%.

The fiscal reserve as of the end of 2011 was BGN 5.0 billion, or EUR 2.6 billion.

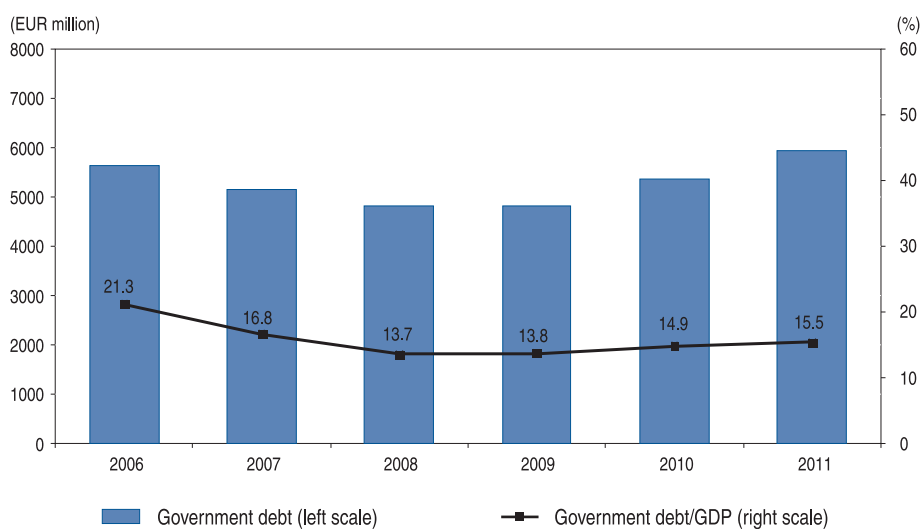


## Government Debt Dynamics

Structure	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
	(EUR million)												
<b>Domestic government debt</b>	<b>1 060.3</b>	<b>906.2</b>	<b>951.7</b>	<b>1 086.1</b>	<b>1 153.8</b>	<b>1 370.6</b>	<b>1 453.5</b>	<b>1 511.3</b>	<b>1 636.1</b>	<b>1 571.3</b>	<b>1 538.7</b>	<b>2 011.5</b>	<b>2 458.3</b>
Government securities issued for financing the public budget	450.9	491.4	554.6	754.9	879.2	1 130.5	1 214.3	1 300.7	1 451.2	1 398.8	1 383.2	1 867.5	2 157.9
Government securities issued for the structural reform	495.5	389.9	382.4	321.7	270.4	240.0	239.1	210.5	184.9	172.5	155.5	144.0	129.1
Government securities issued under LSPDAB/1996	113.9	24.9	14.6	9.4	4.2	-	-	-	-	-	-	-	-
Internal loans	-	-	-	-	-	-	-	-	-	-	-	-	171.3
<b>External government debt</b>	<b>8 587.1</b>	<b>9 159.5</b>	<b>9 096.6</b>	<b>7 685.9</b>	<b>6 961.1</b>	<b>6 140.6</b>	<b>4 876.8</b>	<b>4 134.3</b>	<b>3 526.7</b>	<b>3 270.2</b>	<b>3 289.8</b>	<b>3 373.5</b>	<b>3 487.6</b>
Brady bonds	4 954.6	5 347.7	5 400.0	2 398.7	1 890.1	1 164.1	-	-	-	-	-	-	-
Other bonds	-	-	250.0	2 310.0	2 091.4	2 018.3	2 162.5	2 050.2	1 700.3	1 736.7	1 576.1	1 636.5	1 658.1
Paris Club	811.1	645.3	433.5	284.5	218.9	176.3	163.7	151.1	138.5	125.9	113.3	100.7	88.1
World Bank	820.5	889.6	941.1	836.1	870.0	930.6	1 020.0	877.0	870.5	574.2	793.6	758.7	714.7
G-24	70.9	60.8	53.8	48.9	42.0	34.6	36.9	14.3	-	-	-	-	-
European Union	400.0	460.0	390.0	390.0	350.0	350.0	287.5	215.0	127.5	40.0	15.0	52.4	134.8
IMF	1 126.5	1 309.4	1 183.4	990.9	940.2	868.7	559.5	258.9	-	-	-	-	-
Other	147.7	136.6	136.6	129.2	125.2	125.2	62.3	44.2	31.6	19.0	6.3	0.0	0.0
Government investment loans	207.8	251.0	240.3	236.7	383.0	428.8	549.2	588.6	637.4	756.9	771.9	815.7	887.0
Government guarantees called	48.1	59.2	67.8	61.0	50.2	43.9	35.2	25.0	21.0	17.5	13.6	9.5	4.9
<b>Total government debt</b>	<b>9 647.4</b>	<b>10 065.7</b>	<b>10 048.3</b>	<b>8 771.9</b>	<b>8 114.9</b>	<b>7 511.2</b>	<b>6 330.2</b>	<b>5 645.6</b>	<b>5 162.8</b>	<b>4 841.6</b>	<b>4 828.5</b>	<b>5 385.0</b>	<b>5 945.9</b>
<b>GDP (BGN million)</b>	<b>24 309</b>	<b>27 399</b>	<b>30 299</b>	<b>33 189</b>	<b>35 812</b>	<b>39 824</b>	<b>45 484</b>	<b>51 783</b>	<b>60 185</b>	<b>69 295</b>	<b>68 322</b>	<b>70 511</b>	<b>75 265</b>
<b>GDP (EUR million)</b>	<b>12 429</b>	<b>14 009</b>	<b>15 492</b>	<b>16 969</b>	<b>18 310</b>	<b>20 362</b>	<b>23 256</b>	<b>26 476</b>	<b>30 772</b>	<b>35 430</b>	<b>34 932</b>	<b>36 052</b>	<b>38 482</b>
<b>Total government debt/GDP (%)</b>	<b>77.6</b>	<b>71.9</b>	<b>64.9</b>	<b>51.7</b>	<b>44.3</b>	<b>36.9</b>	<b>27.2</b>	<b>21.3</b>	<b>16.8</b>	<b>13.7</b>	<b>13.8</b>	<b>14.9</b>	<b>15.5</b>

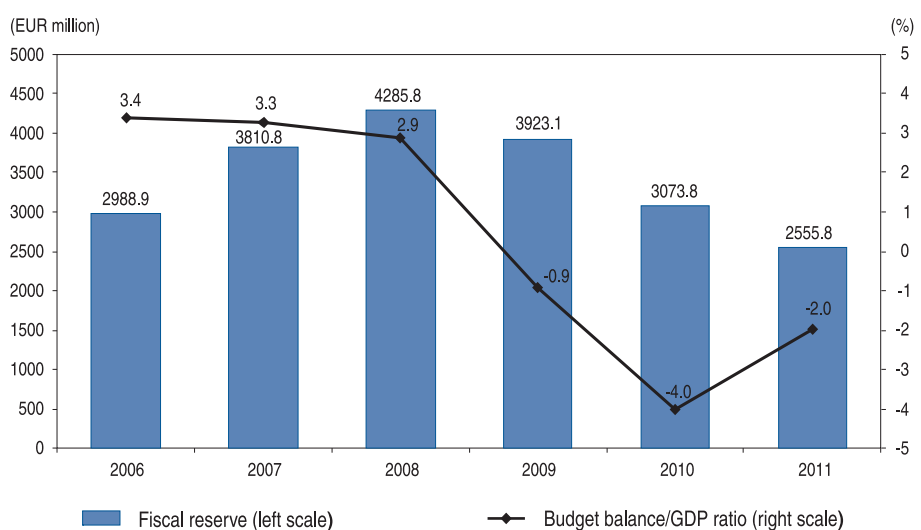
Notes: 1. Debt data based on nominal value.  
 2. Currency revaluation of debt into euros is based on BNB central rates for the respective foreign currencies to the Bulgarian lev quoted for the last business day of the period.  
 3. GDP data from the National Statistics Institute.

Sources: MF, NSI.



## Government Debt Dynamics

Source: MF.



## Budget Balance and Fiscal Reserve

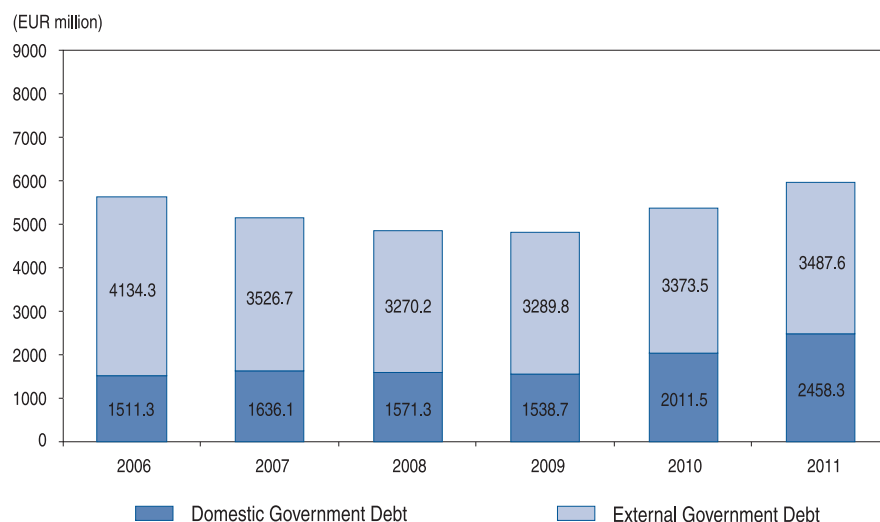
Source: MF.

The nominal domestic government debt amounted to EUR 2,458.3 million, representing 6.4% of GDP, or an increase by about 0.8 p.p. compared to 2010. In nominal terms, domestic government debt went up by EUR 446.8 million as a result of the positive net financing achieved through government securities issued during the year on the domestic market.

External government debt at the end of the year stood at EUR 3,487.6 million, reporting an increase of EUR 114.1 million from its level at the end of 2010. The increase in external government debt was largely the result of obtaining new external financing during the year. The external government debt/GDP ratio decreased compared to 2010, and stood at 9.1%.

Within the structure of government debt, the relative share of domestic government debt was 41.3%, and external government debt was 58.7%, against 37.4% and 62.6%, respectively, in 2010.

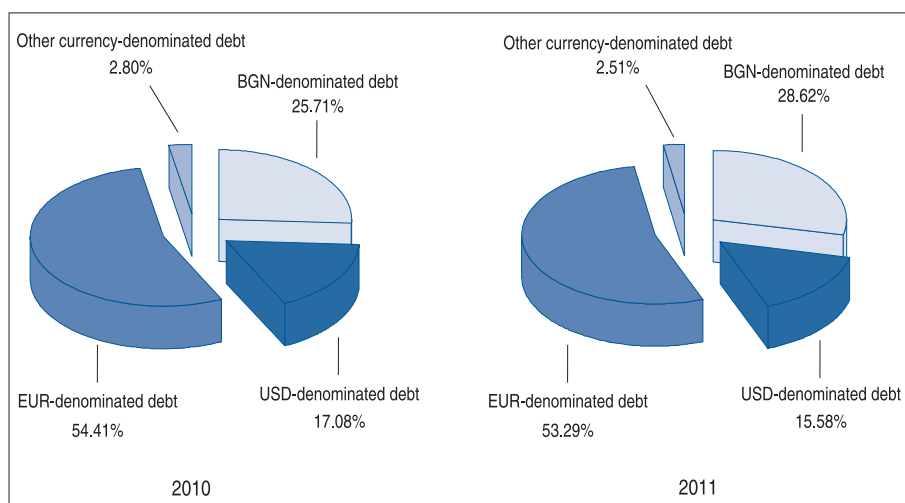
## Dynamics of Domestic and External Government Debt 2006 – 2011



Source: MF.

In the currency structure of government debt, the relative share of BGN-denominated debt instruments continued to rise, thus helping minimise risks associated with exchange rate fluctuations on international capital markets. Compared to the end of 2010, the lev portion of the debt grew from 25.7% to 28.6% at the end of 2011, and the share of USD-denominated debt declined from 17.1% to 15.6%. Over the year, the share of EUR-denominated debt stabilized at a level of about 53.3%, and debt denominated in other foreign currencies settled at about 2.5% of total debt.

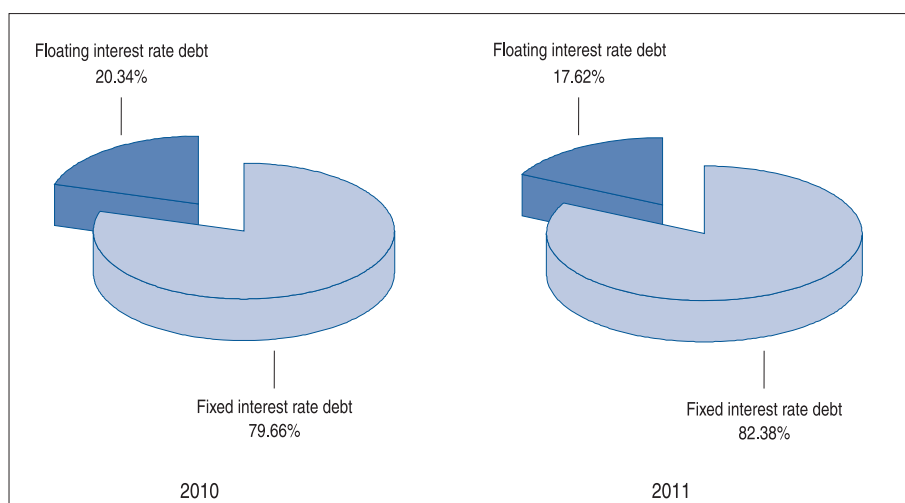
The trend reported for the above indicators was largely due to the placement of BGN- and EUR-denominated government securities during the year, the focus on EUR-denominated external financing as a matter of priority, and the regular amortisation payments made in servicing debt.



**Currency Structure of Government Debt**

Source: MF.

In the year under review, the interest rate structure of government debt continued to be dominated by fixed rate debt (82.4% in 2011, from 79.7% in 2010), which enables an adequate predictability of public budget funds necessary to service government debt. The reported increase of 2.7 p.p. compared to the end of the previous year was largely due to the large volume of government securities issued at fixed interest rates (BGN 1,124.2 million) and the disbursements of funds from official external creditors, also at a fixed rate. This, in turn, brought down the relative share of floating rate debt from 20.3% as of the end of 2010 to 17.6% in 2011.



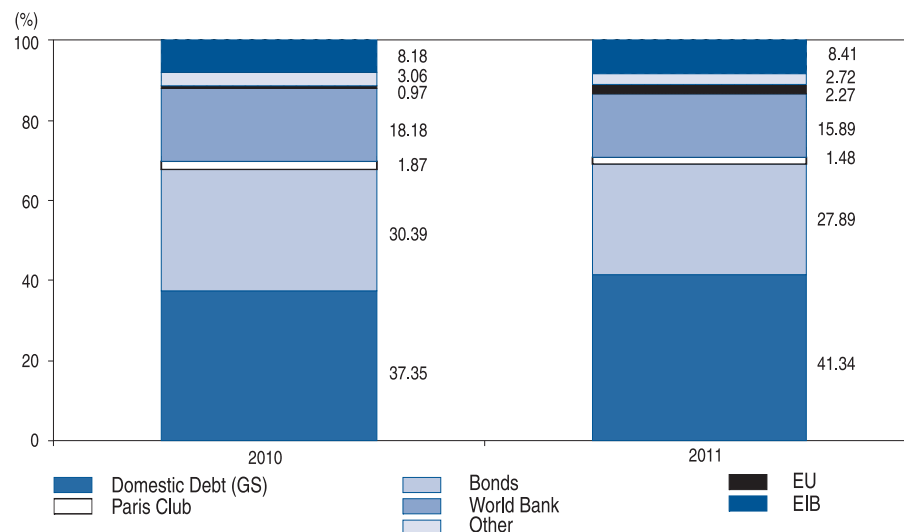
**Interest Rate Structure of Government Debt**

Source: MF.

In the structure of government debt by type of instrument and by creditor, the largest relative share was that of liabilities associated with government securities, accounting for 69.2% of the total amount of government debt (including government securities issued on the domestic market, with 41.3%, and government securities issued on international capital markets, with 27.9%). The increase by 1.5 p.p. compared to the end of 2010 was the result of the positive financing through government securities issued on the domestic market.

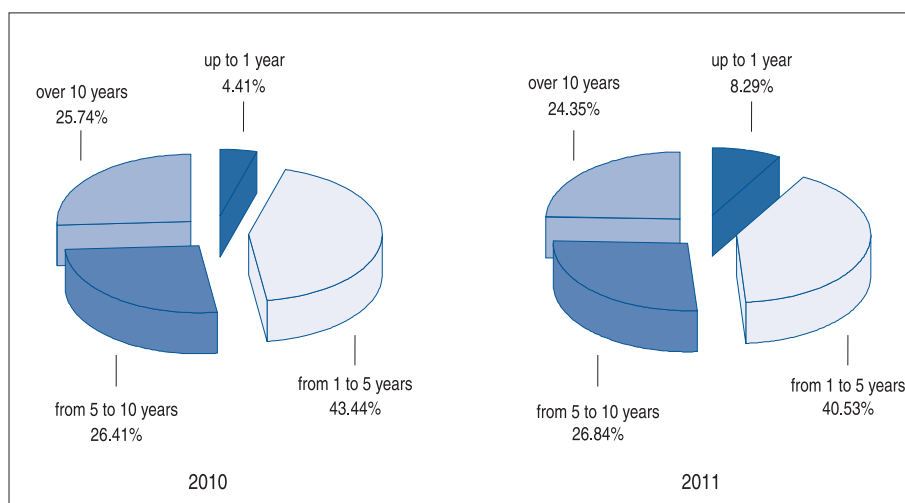
The share of government loans was 30.8% with a largest portion of that being liabilities to the World Bank, 15.9%, followed by EIB with 10.7%, other creditors with 2.7%, and the Paris Club with 1.5%.

## Debt Structure by Instruments and Creditors



Source: MF.

Compared to the previous year, there were several key factors at play behind the change in the maturity structure of debt. Changes in the residual maturity of debt were due to the issuance policy implemented in 2011 which set itself the priority task of increasing the share of mid-term government securities (an issue of government securities with a maturity of 3 years and 6 months, and a 5-year EUR-denominated issue of government securities). This mid-term government securities accounted for 49.7% of all securities issued during the year, followed by long-term government securities (government securities issues with a maturity of 7 years, 10 years, and 10 years and 6 months), with 46.6% in the total securities issued during the year. Compared to the previous year, the volume of debt with residual maturities from 1 to 5 years decreased from 43.4% to 40.5%, at the expense of debt with residual maturity of up to 1 year, which went up from 4.4% to 8.3%. An increase of 0.4 p.p. was registered for terms to maturity between 5 and 10 years – 26.8%, while debt with terms to maturity over 10 years went down by 1.3 p.p., reaching 24.4%.



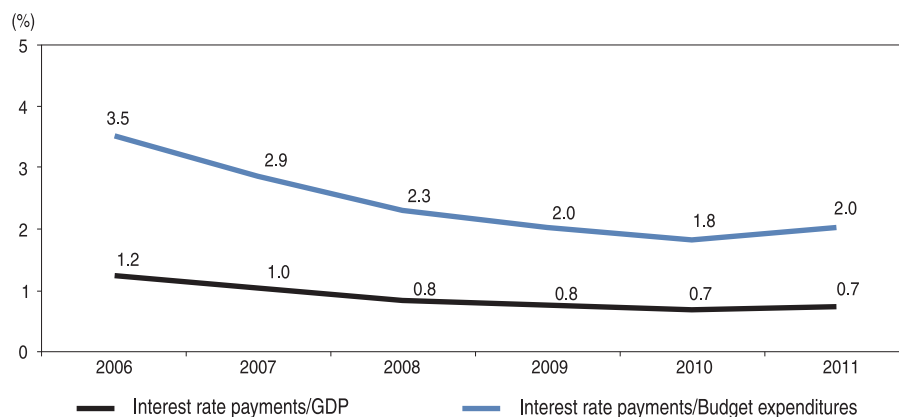
**Residual Maturity of Government Debt**

Source: MF.

Government debt repayments during the year totalled million 1,342.6 BGN, or BGN 6.8 million higher than in the previous year. Redemptions of principal amounted to BGN 835.9 million, or BGN 45.2 million less, and interest paid amounted to BGN 506.7 million, or BGN 52.0 million more than in 2010.

Net debt financing in 2011 was a positive value and stood at BGN 1,060.3 million.

The interest expenditure/GDP ratio remained unchanged from 2010, and was 0.7%. For the same period, interest expenditure accounted for 2.0% of total public expenditure, which is an increase of 0.2 p.p. compared to 2010. This was largely due to the higher absolute volume of interest payments on government debt in 2011, the level of public expenditure, which was kept similar to that in the previous year, and to the change in GDP reported as of the end of 2011 compared to the end of 2010.



**Interest Rate Expenses**

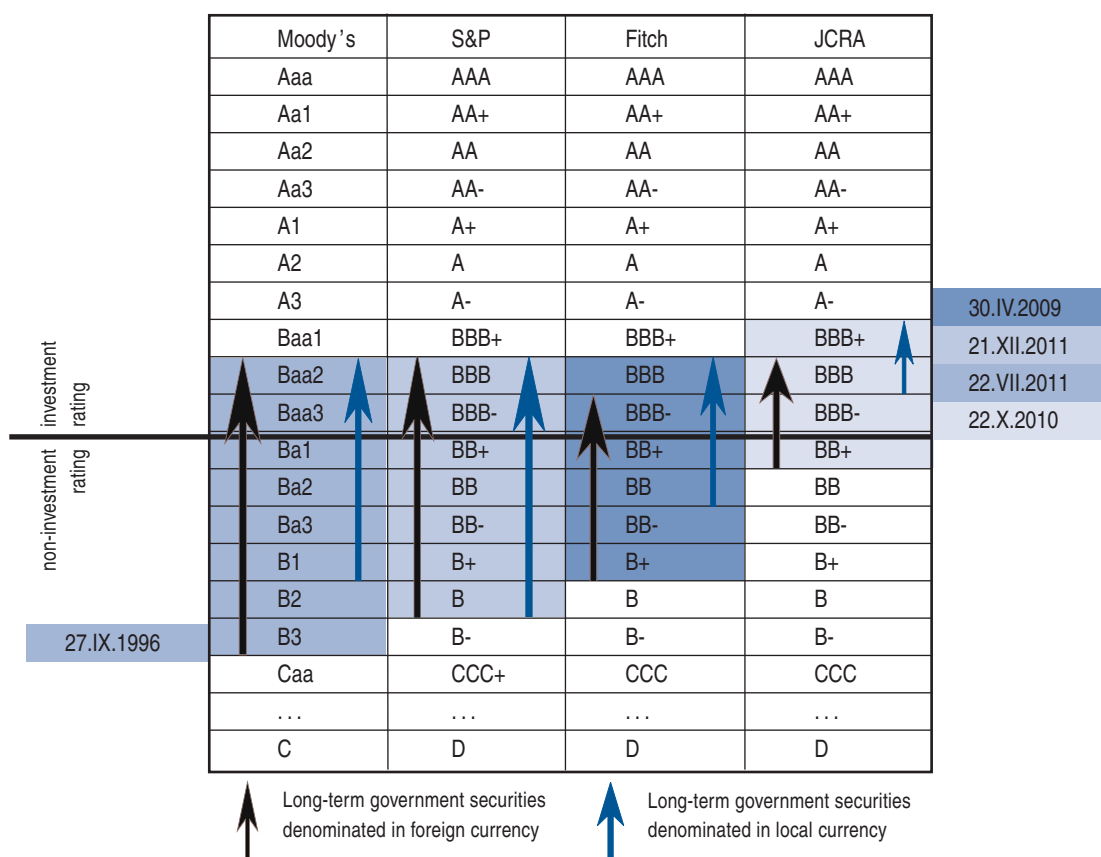
Note: Data based on Consolidated Fiscal Programme.

Sources: MF, NSI.

In 2011, the regular annual meetings were held with representatives of the two rating agencies contracted by Bulgaria – Standard and Poor’s (S&P) and Moody’s Investors Service, in connection with the on-going credit rating reviews of Bulgaria

The positive assessment of the dynamics of macroeconomic fundamentals and the stable debt indicators was reflected in an upgrade of Bulgaria’s rating – from Baa3 to Baa2, stable outlook, by Moody’s Investors Service on 22 July 2011. At the end of 2011, Standard and Poor’s retained the country’s earlier rating of BBB, stable outlook. Ratings are public and are used by rating recipients, and by others (investors, analysts, etc.) on the market, which explains their strong influence on financial markets globally.

**Credit Rating Grid per Agency  
and Ratings Awarded to Bulgaria**



Source: MF.

## Consolidated Government Debt Amount

(EUR million)

Structure	2006	2007	2008	2009	2010	2011
<b>Consolidated government debt</b>	<b>5 800.4</b>	<b>5 380.7</b>	<b>5 079.8</b>	<b>5 168.8</b>	<b>5 823.4</b>	<b>6 431.5</b>
1. Central government debt	5 645.6	5 162.8	4 841.6	4 828.5	5 385.0	5 945.9
2. Debt of social security funds	0.0	0.0	0.0	0.0	0.0	0.0
3. Municipal debt	154.8	217.9	238.2	340.3	438.4	485.6
<b>Consolidated government debt/GDP (%)</b>	<b>21.9</b>	<b>17.5</b>	<b>14.3</b>	<b>14.8</b>	<b>16.2</b>	<b>16.7</b>

**Notes:** 1. Government debt is reported at nominal value and does not include government-guaranteed loans.

2. Calculations are based on the following GDP values: for 2011 – BGN 75 265 million, for 2010 – BGN 70 511 million, for 2009 – BGN 68 322 million, for 2008 – BGN 69 295 million, for BGN 2007 – 60 185 million, and for 2006 – BGN 51 783 million.

3. Currency revaluation of debt into euros is based on BNB central rates for the respective foreign currencies to the Bulgarian lev quoted for the last business day of the period.

Source: MF.

At the end of 2011, consolidated government debt amounted to EUR 6,431.5 million, against EUR 5,823.4 million at the end of the previous year. Within the consolidated government debt, central government debt increased by EUR 560.9 million, and municipal debt grew from EUR 438.4 million to EUR 485.6 million. From 16.2% in 2010, the consolidated government debt/GDP ratio reached 16.7% at the end of 2011.



# **Government Guaranteed Debt**

As of the end of 2011, government guaranteed debt amounted to EUR 612.1 million, including EUR 606.0 million in external, and EUR 6.1 million in domestic government guaranteed debt. In nominal terms, it registered a decrease of approximately EUR 25.0 million from its level at the end of the previous year. This was due both to the smaller amount of disbursements made during the year under credit agreements signed earlier, and to repayments of government guaranteed loans, which were EUR 4.5 million higher than in 2010.

The government guaranteed debt/GDP ratio was 1.6%, showing a decrease by 0.2 p.p. from the previous year.

## Government Guaranteed Debt

(EUR million)						
Structure	2006	2007	2008	2009	2010	2011
<b>Government guaranteed debt</b>	<b>551.2</b>	<b>547.0</b>	<b>634.3</b>	<b>612.1</b>	<b>637.1</b>	<b>612.1</b>
I. Domestic government guaranteed debt	-	-	-	-	1.4	6.1
1. Guarantees under the Student Loans Act	-	-	-	-	1.4	6.1
II. External government guaranteed debt	551.2	547.0	634.3	612.1	635.7	606.0
1. World Bank	91.6	82.3	74.4	60.9	52.0	44.5
2. EIB	7.0	5.9	4.8	3.8	2.9	2.3
3. EBRD	49.0	42.4	41.4	32.0	23.8	18.8
4. Other	403.6	416.4	513.7	515.4	557.0	540.5
<b>Government guaranteed debt/GDP (%)</b>	<b>2.1</b>	<b>1.8</b>	<b>1.8</b>	<b>1.8</b>	<b>1.8</b>	<b>1.6</b>

Notes: 1. Debt amount shown at nominal value.

2. Debt revaluation in euros is based on BNB central rates for the respective foreign currencies to the Bulgarian lev as of the end of the period.

Source: MF.

In the structure of government guaranteed debt by creditor, no significant changes can be observed. The group of 'Other' increased its share from 87.4% to 88.3% at the expense of the decrease in government guaranteed debt to the World Bank, EIB and EBRD. The share of domestic government guarantees went up to 1.0% of total government guaranteed debt.

New external financing under government guaranteed debt was BGN 14.1 million, or BGN 21.3 million less than in 2010. Repayments amounted to BGN 129.6 million, with BGN 101.9 million of that in redemptions of principal and BGN 27.7 million in interest payments. Repayments in 2011 were BGN 8.7 million more, compared to the previous year.

In 2011, the government guarantees issued for credit facility agreements signed by the Bulgarian State Railways EAD (BDZ EAD) with IBRD were partially called. The principal due on the loan, in the amount of BGN 11.4 million, was repaid using funds from the the reserve for covering the risk of government guarantees being called, which had been planned in the central government budget.

In early 2011, the government claim relating to the redemption payments made by the Ministry of Finance to EBRD in 2010 in connection with a called government guaranteed loan to BDZ EAD was partially repaid, and about BGN 3 million of the repayments made from the central government budget to the external creditor were refunded by BDZ EAD.

During the year, the rest of the government guaranteed loans were serviced in compliance with their respective terms.

### New Financing and Repayments under Government Guaranteed Debt as of the end of 2011

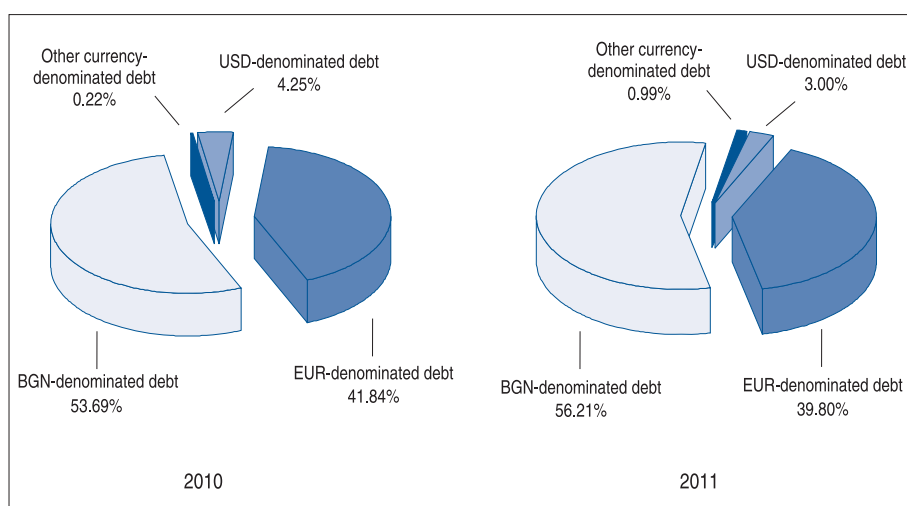
(BGN million)

Structure	Credit facilities received (tranches)	Repayments, including principal interest	
<b>I. Domestic government guaranteed debt</b>	<b>9.2</b>	<b>0.2</b>	<b>-</b>
1. Guarantees under the Student Loans Act	9.2	0.2	-
<b>II. External government guaranteed debt</b>	<b>4.9</b>	<b>101.7</b>	<b>27.7</b>
1. World Bank	-	5.0	2.1
2. EIB	0.6	1.9	0.1
3. EBRD	-	9.7	1.0
4. Other	4.3	85.1	24.5
<b>Government guaranteed debt</b>	<b>14.1</b>	<b>101.9</b>	<b>27.7</b>

**Note:** The lev equivalents of new external financing and repayments are based on the BNB central rates for the respective foreign currencies to the Bulgarian lev valid until 4 pm on the day of the respective payment.

Source: MF.

In the currency structure of government guaranteed debt, last year's trend of increasing liabilities denominated in other foreign currencies (Japanese yens) continued. A comparison with the end of 2010 reveals that their share increased by almost 2.5 p.p. to 56.2%. The share of liabilities in the domestic currency also grew, to 1.0%, respectively. The change is primarily due to the fact that 65.3% of all disbursements under government guaranteed debt made during the year were denominated in levs, and 30.3% were in Japanese yens. Liabilities in euros and in US dollars were both down, at 39.8% and 3.0%, respectively.

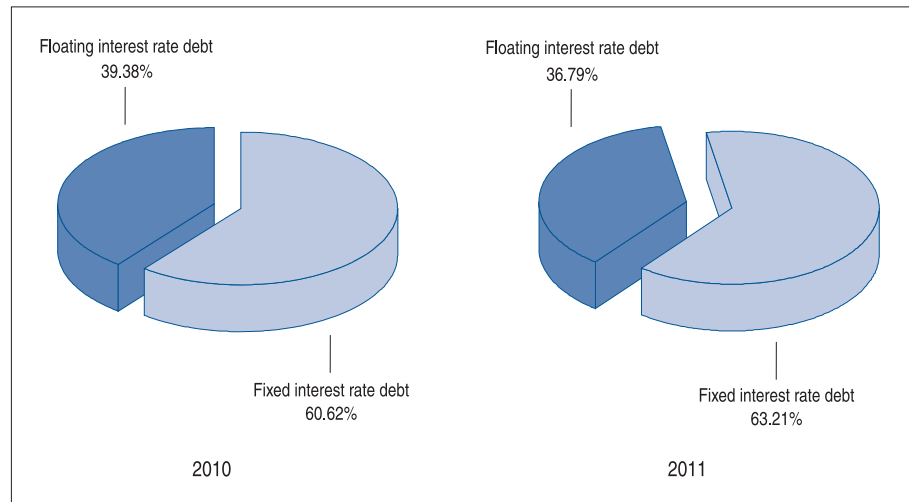


**Currency Structure of Government Guaranteed Debt**

Source: MF.

In terms of the interest rate structure of government guaranteed debt, a gradual increase in fixed interest rate debt was registered in 2011, from 60.6% to 63.2%. The change is due to the disbursements during the year, largely under fixed interest rate government guaranteed loans.

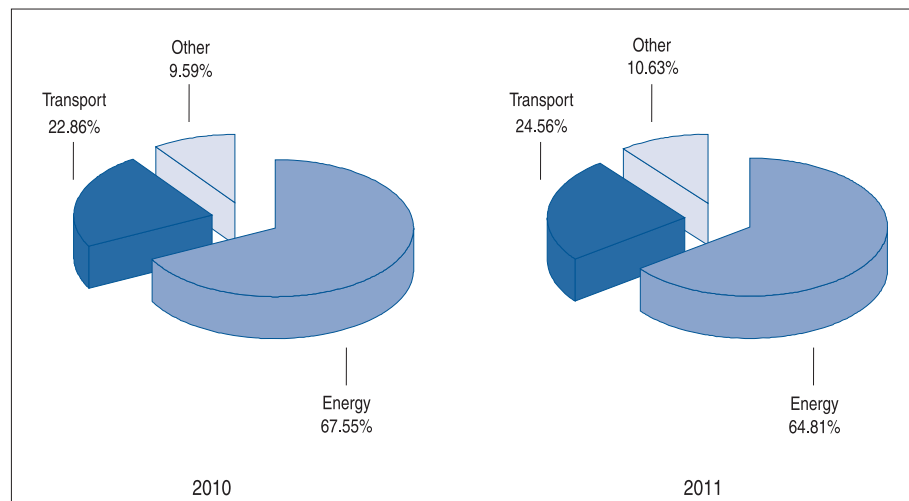
## Interest Rate Structure of Government Guaranteed Debt



Source: MF.

In the structure of government guaranteed debt by industry, the largest relative share belonged to loans to the energy sector (64.8%), followed by loans to transport (24.6%), and 'other' (10.6%).

## Government Guaranteed Debt by Sectors



Source: MF.

