

Bulgaria (/gws/en/esp/issr/80442251)



## Fitch Upgrades Bulgaria to 'BBB'; Outlook Stable

Fitch Ratings-London-01 December 2017: Fitch Ratings has upgraded Bulgaria's Long-Term Foreign- and Local-Currency Issuer Default Ratings (IDRs) to 'BBB' from 'BBB-'. The Outlooks are Stable.

A full list of rating actions is at the end of this rating action commentary.

### KEY RATING DRIVERS

The upgrade of Bulgaria's IDRs reflects the following key rating drivers and their relative weights:

#### High

A prolonged decline in external debt ratios has led Bulgaria's external finance metrics to outperform the majority of its 'BBB' peers. Including data revisions, Bulgaria's net external creditor position strengthened to 8.6% of GDP in 2016 from a net debtor position of 2.1% of GDP in 2015. Bulgaria's net creditor position is forecast to strengthen further, staying above the 'BBB' median net creditor position of 0.8% of GDP. Current account surpluses averaging 3.4% of GDP are also forecast for 2017-2019, supported by gains in export competitiveness and a diversifying export base. This compares with the 'BBB' median current account deficit of 1.2% of GDP.

Bulgaria's sovereign external buffer continues to strengthen as reserves climb. Foreign reserves represent 49.7% of GDP, equivalent to 10 months of imports. An external liquidity ratio of 215% (end-2016) provides more than adequate liquidity support for Bulgaria's long-standing and credible currency board regime.

#### Medium

Budget outturns are stronger than peers. Compared with the previous forecast for a deficit of 0.6% of GDP, Fitch now forecasts the general government budget to balance in 2017, as was the case in 2016. For 2018-2019, budget measures that will increase spending on pensions, salaries, defense and social welfare will result in small fiscal deficits, but primary fiscal surpluses will be maintained.

General government debt/GDP is low relative to peers and on a downward trajectory. Projected primary surpluses will contribute to further government debt reduction, with debt forecast to stay below 25% of GDP for 2017-2019, significantly lower than the 'BBB' category median of 41.2%. Public debt sustainability is supported by the sovereign's low level of interest payments to revenues (2.3% compared with a peer median of 7.3%) and relatively long average debt maturity.

Economic growth is strengthening. After average growth of 1.1% over 2010-14, Fitch forecasts average growth of 3.6% in 2017-19, an upward revision of 0.5pp from six months ago, and above the five-year median (3.2%) of its 'BBB' peers. Risks to Fitch's forecast are balanced and highly dependent on both private and public sector investment activity. Higher growth may come from better-than-forecast public expenditure of EU structural funds and/or resumption of credit growth. An underperformance of both factors would risk lower economic growth.

Bulgaria's 'BBB' IDRs also reflect the following key rating drivers:

Fitch views the risk of domestic banking sector contingent liabilities materialising on the sovereign's balance sheet to have reduced. This reflects banks' solid capital buffers, strong liquidity, stable deposit-based funding and moderate profitability. These factors mitigate the risks stemming from the high stock of legacy bad debts in banks' loan books. The ratio of NPLs to total loans (excluding exposure to banks) was 16.6% at end-3Q17 and is likely to remain the highest in the region. Authorities have begun to address regulatory gaps and improve bank supervision.

Bulgaria's GDP per capita still lags the median level of 'BBB' peers and higher rated sovereigns. Progress in income convergence will depend on how effectively authorities push ahead with structural reform. Labour market rigidities remain a key challenge in view of worsening demographics.

Bulgaria's governance indicators are in line with its 'BBB' category peers. There is broad-based political consensus in favour of integration with the rest of the EU, although progress in effective policy making is vulnerable to a changeable political environment, given the country's history of unstable governments. However, with Bulgaria's upcoming presidency of the EU council beginning 1 January 2018, Fitch's baseline is for the current GERB-United Patriots coalition under Prime Minister Boyko Borissov to remain stable.

### SOVEREIGN RATING MODEL (SRM) and QUALITATIVE OVERLAY (QO)

Fitch's proprietary SRM assigns Bulgaria a score equivalent to a rating of 'BBB+' on the Long-Term FC IDR scale.

Fitch's sovereign rating committee adjusted the output from the SRM to arrive at the final LT FC IDR by applying its QO, relative to rated peers, as follows:

-Macroeconomics: -1 notch, to reflect Fitch's view that the SRM is currently benefitting from a cyclical economic upswing, and that sustained and higher potential growth is limited by Bulgaria's structural economic competitiveness challenges, particularly labour market rigidities and adverse demographic trends.

Fitch's SRM is the agency's proprietary multiple regression rating model that employs 18 variables based on three year centred averages, including one year of forecasts, to produce a score equivalent to a LT FC IDR. Fitch's QO is a forward-looking qualitative framework designed to allow for adjustment to the SRM output to assign the final rating, reflecting factors within our criteria that are not fully quantifiable and/or not fully reflected in the SRM.

#### RATING SENSITIVITIES

The main factors that could, individually or collectively, could lead to positive rating action are:

- Stronger medium-term GDP growth potential.
- Progressive convergence towards income levels of higher rated peers.

The main factors that could, individually or collectively, could lead to negative rating action are:

- Re-emergence of external imbalances, for example from prolonged widening of the current account deficit and/or deterioration of external competitiveness.
- Higher fiscal deficits that result in deterioration of the public debt trajectory.
- Materialisation of contingent liabilities on the sovereign's balance sheet; for example, from state-owned enterprises.

#### KEY ASSUMPTIONS

- Fitch assumes the Bulgarian authorities will maintain continuity in economic, fiscal and policies, and in relations with the EU.
- The global economy performs in line with Fitch's Global Economic Outlook.

The full list of rating actions is as follows:

Long-Term Foreign-Currency IDR upgraded to 'BBB' from 'BBB-'; Outlook Stable  
Long-Term Local-Currency IDR upgraded to 'BBB' from 'BBB-'; Outlook Stable  
Short-Term Foreign-Currency IDR upgraded to 'F2' from 'F3'  
Short-Term Local-Currency IDR upgraded to 'F2' from 'F3'  
Country Ceiling upgraded to 'A-' from 'BBB+'  
Issue ratings on long-term senior unsecured debt upgraded to 'BBB' from 'BBB-'

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#### Applicable Criteria

Country Ceilings Criteria (pub. 21 Jul 2017) (<https://www.fitchratings.com/site/re/901393>)  
Sovereign Rating Criteria (pub. 21 Jul 2017) (<https://www.fitchratings.com/site/re/901261>)