



## Fitch Affirms Bulgaria at 'BBB'; Outlook Stable

Fitch Ratings - Frankfurt - 16 November 2018: Fitch Ratings has affirmed Bulgaria's Long-Term Foreign-Currency Issuer Default Rating (IDR) at 'BBB'. The Outlook is Stable.

Bulgaria's ratings are supported by its sound external and public finances, credible policy framework aimed towards gradual accession to eurozone membership and stable growth prospects. The ratings are constrained by lower income levels compared with the current 'BBB' median, and weak demographics which could constrain growth and weigh on government finances over the long term. Governance indicators are in line with peers.

### RATING ACTIONS

ENTITY	RATING	PRIOR
Bulgaria	LT IDR BBB ● Affirmed	BBB ●
	ST IDR F2 Affirmed	F2
	LC LT IDR BBB ● Affirmed	BBB ●
	LC ST IDR F2 Affirmed	F2
	Country Ceiling A- Affirmed	A-
senior unsecured	LT BBB Affirmed	BBB

### KEY RATING DRIVERS

Economic growth prospects are broadly in line with peers. Fitch expects real GDP growth to remain largely unchanged at 3.7% in 2018, before slowing to 3.5% in 2019 and 3.0% in 2020. Domestic demand should benefit from a scheduled 10% increase in public and minimum wages from January 2019; household consumption increased by 7.5% yoy in 1H18 (1H17: 4.0%). Investment growth is expected to increase from 3.2% in 2017 to 7.0% in 2018 and an average of 6.5% yoy in 2019-20, driven by higher capex, funded by the EU. These investments will be import-intensive, causing the net exports contribution to GDP to remain negative over the forecast horizon.

Inflation has surged to 3.6% as of 3Q18 from 2.8% at end-2017, in line with the closing of the output

gap (at end 2017) and boosted by high wage growth (2Q18: 8.2% yoy), low unemployment (2Q18: 5.5%), higher energy and food prices, and one-off factors in some services subcomponents. Fitch has revised upwards its forecasts for consumer prices (annual average) to 2.8% yoy in 2018 (from 1.9%), 3.0% in 2019 (from 2%) and 2.9% in 2020. However, this is only slightly above the forecast 'BBB' median and comes against a background of sustained deflation through 2016.

Monetary policy revolves around the operation of a credible currency board arrangement (CBA) against the euro. Bulgaria's sovereign net foreign assets (2018F: 33% of GDP) and external liquidity ratio (2018F: 343%) are high compared with the 'BBB' median of 5.3% and 143.7%, respectively, and will remain key credit strengths over the forecast period.

In July 2018, Bulgaria formally applied to the European Central Bank for 'close cooperation' with the aim of joining simultaneously the ECB's Single Supervisory Mechanism and ERM-2 (the two-year compulsory waiting period prior to joining the eurozone) by July 2019. Fitch views the European Commission's generally supportive stance towards Bulgaria's entry into ERM-2 (subject to meeting the banking union requirements) as an affirmation of Bulgaria's commitment to adherence to convergence criteria for eurozone accession (which include ceilings on inflation, general government debt, the long-term interest rate and the fiscal deficit).

Bulgaria's fiscal finances are strong relative to peers. Bulgaria's general government surplus was 2.5% of projected 2018 GDP (cash basis) as of 3Q18, driven by 10% yoy increase in taxes, as well as other revenues. However, Fitch expects the seasonal ramp up in spending in 4Q18 to reduce the surplus to 0.5% of GDP in 2018 (projected current 'BBB' median: -2.4%). Pension reforms, wage increases and other discretionary measures will contribute to a modest decline in the surplus to 0.3% of GDP by 2020.

Government debt levels (on both gross and net basis) remain far lower than both the 'BBB' median as well as most other EU member states. Bulgaria did not tap the debt markets in 2018, and no major debt redemptions are imminent until 2022. Fitch projects that the general government debt/GDP ratio will decline from an average of 27% in 2014-17 to just under 23% in 2018, 21.3% in 2019 and 19.5% in 2020. Although FX-denominated debt makes up nearly 80% of public debt currently, virtually all of the FX debt is euro-denominated, and the credibility of the CBA greatly reduces exchange rate risks.

Bulgaria's external finance metrics outperform the majority of its 'BBB' peers. Gains in export market shares, sustained export competitiveness, anchored by real effective exchange rate stability have enabled Bulgaria to run current account surpluses. A weakening of growth in some of EU export markets and stronger domestic demand will lead to a decline in the trade balance, pulling the current account surplus down from 6.5% of GDP in 2017 to 1.1% in 2018 and an average of 0.8% in 2019-20.

Bulgaria's net external creditor position, at a projected 17% of GDP in 2018 is stronger than the current 'BBB' median of -6.7%. Fitch expects a further improvement to 19% of GDP in 2019 and 20.4% in 2020. While gross external debt has also declined from a peak of nearly 100% of GDP in 2010 to a projected 70.6% in 2018, the build-up of external assets has been significant in boosting Bulgaria's overall external position. External assets are estimated to increase by nearly 90% from 2010 levels to USD58.5 billion (83% of GDP by 2020).

Bulgaria's demographics are among the worst in the EU, due to a combination of a low birth rate and negative net migration. By some estimates, the working age population could shrink by 12% by 2025 (from 2015 levels), and by over 21% by 2047. This poses a constraint to potential growth in the medium term, and could raise fiscal costs associated with social expenditures and a declining tax base for the government in the long term.

## **DERIVATION SUMMARY**

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 structural bottlenecks, particularly adverse demographic trends, constrain potential growth compared with peers.

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.

## **KEY ASSUMPTIONS**

-Fitch assumes the Bulgarian authorities will maintain continuity in economic and fiscal policies, and in relations with the EU.

-The global economy performs in line with Fitch's Global Economic Outlook.

## **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.

-Progress towards eurozone accession.

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.

-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.

## **DATE OF RELEVANT COMMITTEE**

12 November 2018

Additional information is available on [www.fitchratings.com](http://www.fitchratings.com)

## **FITCH RATINGS ANALYSTS**

Primary Rating Analyst

Arvind Ramakrishnan

Director

+49 69 768076 271

Fitch Deutschland GmbH

Neue Mainzer Strasse 46 - 50

Frankfurt am Main D-60311

Secondary Rating Analyst

Gergely Kiss

Director

+44 20 3530 1425

Committee Chairperson

Charles Seville

Senior Director

+1 212 908 0277

## **MEDIA CONTACTS**

Peter Fitzpatrick  
London  
+44 20 3530 1103  
peter.fitzpatrick@thefitchgroup.com

## **Applicable Criteria**

Sovereign Rating Criteria (pub. 19 Jul 2018) (/site/re/10037181)

Country Ceilings Criteria (pub. 19 Jul 2018) (/site/re/10037793)

## **Additional Disclosures**

Dodd-Frank Rating Information Disclosure Form (/site/dodd-frank-disclosure/10052146)

Solicitation Status

Endorsement Policy (/site/regulatory)

## **DISCLAIMER**

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: [HTTPS://WWW.FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](https://www.fitchratings.com/understandingcreditratings) ([HTTPS://WWW.FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](https://www.fitchratings.com/understandingcreditratings)). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEB SITE AT [WWW.FITCHRATINGS.COM](http://WWW.FITCHRATINGS.COM) (<https://www.fitchratings.com/site/home>). PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. DIRECTORS AND SHAREHOLDERS RELEVANT INTERESTS ARE AVAILABLE AT [HTTPS://WWW.FITCHRATINGS.COM/SITE/REGULATORY](https://www.fitchratings.com/site/regulatory) (<https://www.fitchratings.com/site/regulatory>). FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH WEBSITE.

## **COPYRIGHT**

Copyright © 2018 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an

enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001

Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see <https://www.fitchratings.com/site/regulatory> (<https://www.fitchratings.com/site/regulatory>)), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

## **SOLICITATION STATUS**

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

## Endorsement Policy

Fitch's approach to ratings endorsement so that ratings produced outside the EU may be used by regulated entities within the EU for regulatory purposes, pursuant to the terms of the EU Regulation with respect to credit rating agencies, can be found on the EU Regulatory Disclosures (<https://www.fitchratings.com/regulatory>) page. The endorsement status of all International ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for all structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.

## Fitch Updates Terms of Use & Privacy Policy

We have updated our Terms of Use and Privacy Policies which cover all of Fitch Group's websites. Learn more (<https://www.thefitchgroup.com/site/policies>).