Ministry of Finance of the Republic of Bulgaria

BULGARIAN ECONOMY

MONTHLY REPORT

Based on statistical data published up to September 17, 2019

#7/2019

Gross domestic product

In Q2 GDP has continued to increase, supported by net export. The growth reached 3.7% yoy (non-seasonally adjusted data) and slowed down from 4.8% in Q1, due to the almost neutral contribution of domestic demand because of a decline in the change in inventories. Fixed investments increased by 1.3%, up from 0.6% in Q1. The acceleration reflected higher public capital expenditures. At the same time, both private and public consumption growth was weaker than in Q1. These developments, along with lower export growth, led to a decrease in import.

On the supply side, Gross Value Added growth accelerated. The rate reached 3.9% yoy with the highest contribution coming from *public administration* and *real estate activities*. The value added in construction increased by 6.6% yoy after a decrease in Q1.

Short-term business statistics

After the reported weak performance in June, short-term indicators had positive development in July. Industrial production and turnover returned to growth supported by both domestic and foreign industrial sales. Manufacture of *food products* and *electricity, gas, steam and air conditioning supply* had major contribution to the rise in domestic turnover, while manufacture of *chemical products* supported the growth in foreign sales. Construction production also followed an upward trend mainly due to higher building construction. Meanwhile, *sales of computers, peripheral units and software* and *of audio and video equipment* posted the largest increase in retail trade.

In August, the overall business climate indicator continued to decline, but remained above its long term average. The monthly value was 3.1 points lower than in July, as the assessment of the present business situation in all sectors was less favourable, and expectations deteriorated. Households' more negative expectations also led to a decrease in the consumer confidence indicator in August.

Labour market

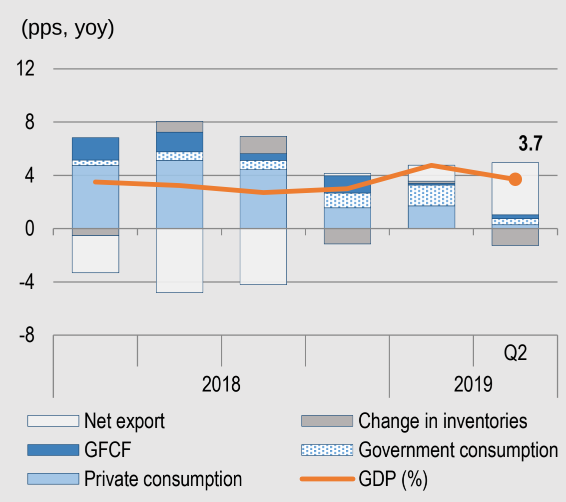
In Q2 the labour force participation increased further due to activation, while working-age population was declining. The labour force (15-64) went up 1.4% yoy driving upwards the activity rate to 73.8%. Employment numbers increased across all 10-year age groups, as the increase in 15-24 and 25-34, was the first since early 2018. Given the unfavourable demographic trends this broad employment improvement reflected higher labour market participation. Higher job opportunities resulted in a further decrease in the unemployment rate to a historical low of 4.2% (LFS).

The overall employment growth (ESA 2010) slightly accelerated in Q2, up by 0.2%, mainly due to services. *Agricultural* employment continued to decrease, while employment growth in *industry* was sustained by *construction* but restrained by the negative dynamics in *industry excl. construction*. Job creation in services was broadly supported by all sub–activities.

Productivity

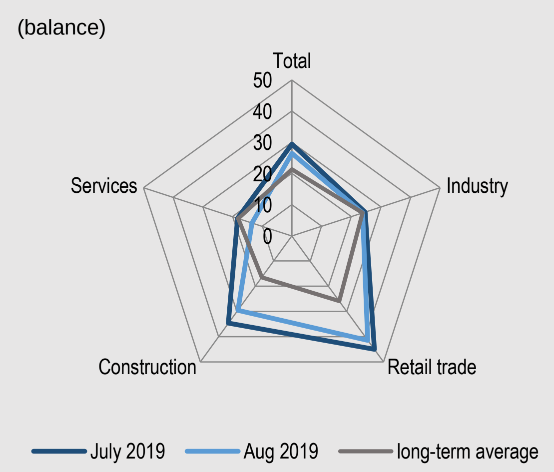
Productivity growth accelerated to 3.6% yoy in Q2, up from 2.8% in Q1, supported by higher real GVA in all economic sectors. The largest contribution came from services. Although industrial

Graph 1 Contributions to GDP growth



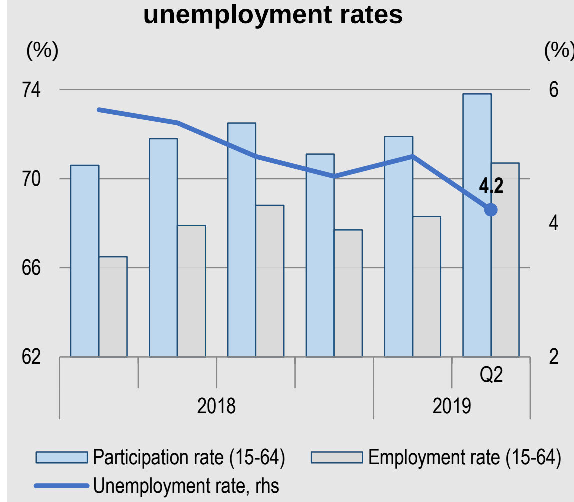
Source: NSI

Graph 2 Business climate by sectors



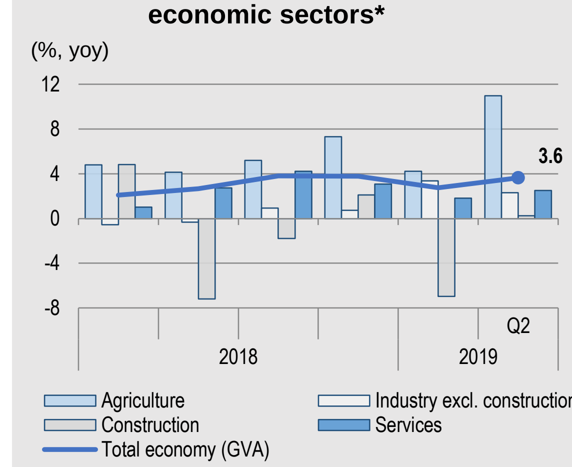
Source: NSI

Graph 3 Activity, employment and unemployment rates



Source: NSI

Graph 4 Real productivity growth by economic sectors*



* GVA in services is not corrected for the imputed rent

Source: NSI, MF

productivity growth lowered, the rate of increase in manufacturing, which is mainly exposed to external competition, remained significant at 8.8% yoy. Compensation per employee grew by 11.5% yoy (close to the Q1 reading of 11.2%). The upward trend was mostly driven by positive base effect in *services* (up by 13% yoy), and the indicator in *industry* was up by 8.8%. Reflecting productivity and compensation per employee dynamics in Q2, the overall nominal unit labour costs (NULC) went up by 7.7% yoy. Still, NULC in *manufacturing* continued decreasing, pointing to a lower labour costs pressure in the export-oriented activities.

Inflation

Food and services prices determined the annual inflation dynamics in July and August. After accelerating to 2.6% in July, the inflation rate edged down to 2.5% yoy in August. The contribution of *energy goods* to the overall price dynamics was very low. At the same time *food prices* increased by 5.1% and *services* – by 3.6% yoy in August. The acceleration in food inflation, observed since the beginning of the year, together with the increase in wages, pushed up the prices in some services such as catering, up by 5.6% in August.

Core inflation, which excludes *energy goods* and *unprocessed foods*, accelerated to 2.9% in July and slowed down to 2.7% in August.

External sector

Current account balance improved on a year earlier in June, supported by all sub-accounts. The accumulated surplus since the beginning of the year reached 3% of projected GDP. In June, the upward trends in trade turned into a decline in export and import on a year earlier. Still the decrease in import outpaced that in export for both goods and services. Commodity export went down by 2.7% yoy, import – by 11.2% and both dynamics reflected lower trade in intra and extra-EU trade. Export of services, down by 3%, were driven by a decline in travel and transport receipts. Import of transport services decreased for a second consecutive month and was the main factor for the lower services import (-9%). EU-related payments to the General government kept increasing.

Gross external debt decreased to 57.7% of projected GDP at end-June with positive contribution from all institutional sectors.

Financial sector

Credit to the private sector growth slowed down in July affected by a strong decline in bad and restructured loans. Its annual rate declined to 6.5% yoy, coming from 6.8% a month earlier driven by lower increase in corporate credit (4.3% yoy vs 4.6% as at end-June). Credit to households continued to accelerate, up by 8.7% yoy, due to higher growth in consumer loans and mortgages.

Weighted average lending rate slightly increased in July due to higher average rate on consumer loans, while the average price of corporate credit and mortgages declined on a month earlier.

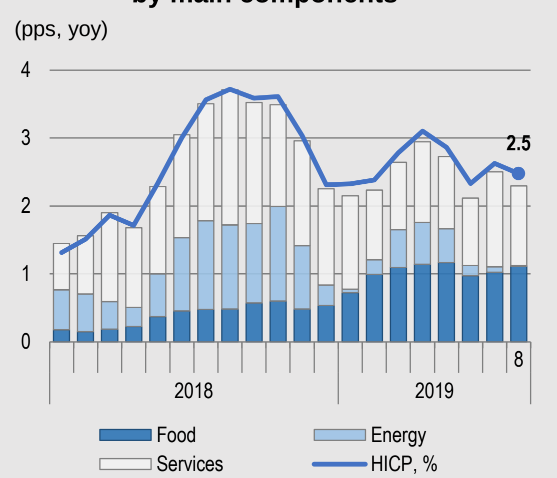
BNB's international reserves declined in August, as part of the Government deposit was used for payments on the contract for acquisition of new fighter jets from the USA. The reserves went down by 2.9% mom to EUR 24.8 bn, as the Government deposit decreased by 15.8% mom following a transfer to the Ministry of Defense.

Fiscal sector

The accumulated budget surplus continued to improve on a yoy basis and at end-July stood at 2.8% of projected GDP, equaling the ratio a month ago. Revenues increased at a double digit pace, up by 15.2% yoy, backed by higher tax receipts – mainly indirect tax revenue and social and health insurance contributions. Due to a positive base effect following legislative amendments, non-tax proceeds, up by 38.4% yoy, continued to have strong contribution to the revenue growth. The growth in expenditure, up by 10.8% yoy, was mainly driven by subsidies (8.6% of total expenditure) and personnel cost (24% of total). The latter rose as a result of a 10-percent increase in wages in the budgetary sector and teachers' salaries.

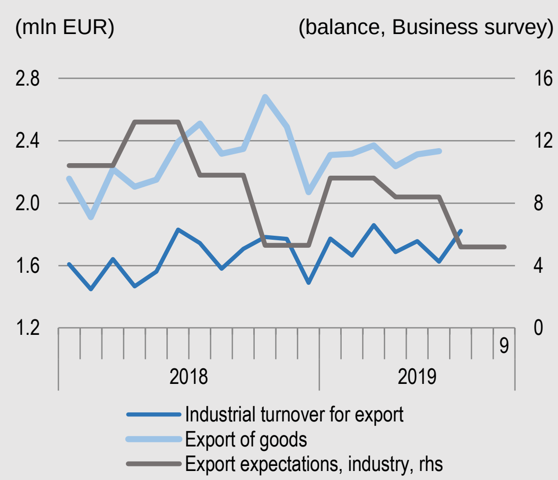
Government debt-to-GDP ratio edged up on a month earlier to 20.3%, but was lower than its level at end-July 2018 (22.5%).

Graph 5 HICP dynamics and contributions by main components



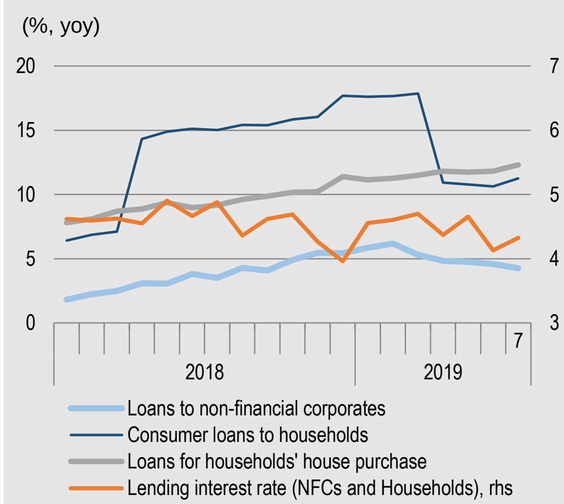
Source: NSI, MF

Graph 6 Export, export turnover and expectations



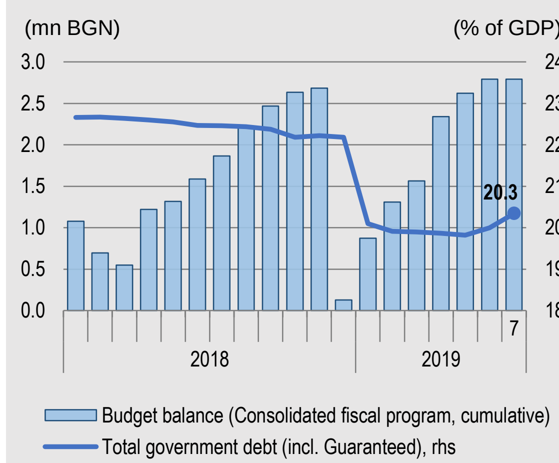
Source: BNB, NSI

Graph 7 Private sector credit growth



Source: BNB, MF

Graph 8 Budget balance and government debt



Source: MF