Ministry of Finance of the Republic of Bulgaria

BULGARIAN ECONOMY

MONTHLY REPORT

Based on statistical data up to June 16, 2020

In March COVID-19 containment measures were widely introduced by all EU Member States, posing a significant impact on economic development. In Bulgaria a State of emergency was introduced on 13 March and lifted in mid-May, while certain anti-epidemiological measures still remain relevant. The effects of the containment measures are evident through different economic indicators in March–May.

Gross Domestic Product

In Q1 GDP increased by 1.2% yoy compared to a growth of 2.9% in Q4. The slowdown resulted from lower domestic demand, while the higher exports, up by 1.8%, led to positive net exports contribution. Household consumption increased at a slower pace, due to a decrease in expenditures on durable goods and slower growth in consumption of other goods and services, because of the imposed restrictive measures and higher uncertainty. Gross fixed capital formation went down led mostly by the drop in construction investment.

Growth in Gross Value Added decelerated to 1.1% as value added in industry decreased. Services were up by 1.3% with biggest positive contribution from *public administration; education; health* and *information and communication*.

Short-term indicators

Short term indicators showed a sharp deterioration in April as a result of the containment measures related to Covid-19. Industrial production declined at a double-digit rate of 15.7% yoy, due to a reduction in all economic activities, except for *mining and quarrying*. The decrease in turnover also accelerated to a double-digit rate and was equally attributable to diminished sales on both domestic and international market. The fall in construction speeded up, owing to a greater extent to lower building construction. In retail trade, a record decline was reported of 20% yoy. The decrease was broad based, as *automotive fuels; textiles, clothing and footwear*; *computers and software* and *food, beverages and tobacco* had the highest negative contributions.

In May sentiment indicators started recovering. Business climate was up 11.8 points mom after a drop of 47.1 points in April. Companies' expectations for the business situation improved in all sectors. However current situation and demand in services were still assessed as unfavourable. Consumer confidence also rose, up by 7.5 points mom, on the back of better expectations for the households' financial situation and the economy in the coming months.

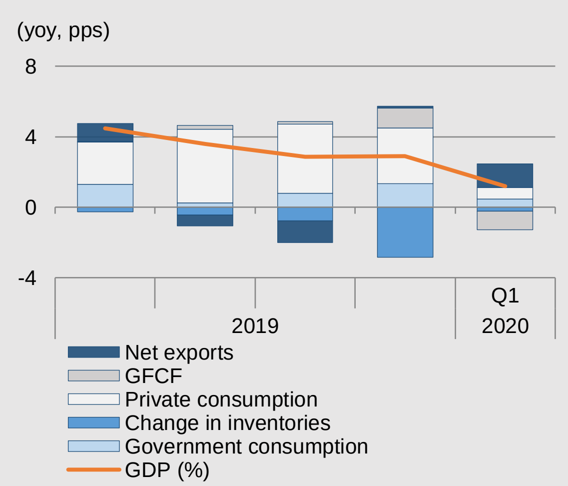
Labour market and Productivity

In Q1 the number of employed declined to 3 398.2 thousand (according to ESA), down by 1.3% yoy, mainly because of the reduced economic activities in many sectors due to the COVID-19 containment measures. The largest decline was observed in *agriculture*, *industry (except construction)* and *wholesale and retail trade*; *repair of motor vehicles and motorcycles*; *transportation and storage*; *accommodation and food service activities*. The decrease was due to the lower number of self-employed, while the number of employees was still growing marginally on an annual basis.

As employment declined, labour productivity increased in all sectors and was the main driver for the increase in GVA in the quarter. The highest productivity growth rate was observed in *agriculture*, up by 5.2% yoy, but there was also improvement in *industry*, up by 1.6%, and *services* - up by 2.1%.

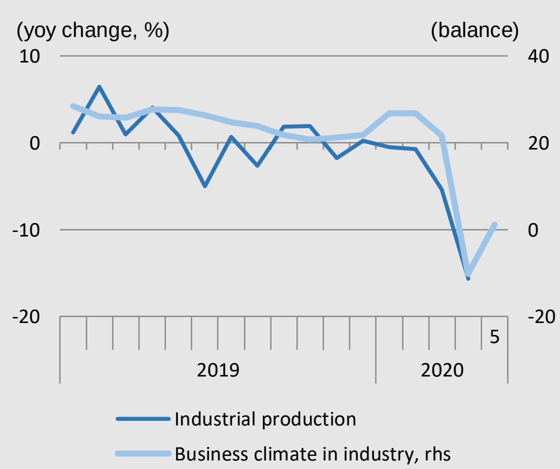
In Q1 the overall compensation per employee went up by 7.3% yoy and along with real labour productivity growth of 2.5% contributed to an increase in nominal unit labour cost (NULC) of 4.7%. The quarterly figures do not suggest any significant negative impact from the pandemic containment measures yet. Both compensation per employee and productivity dynamics remained close to the rates, reported an year ago. In *services*, the increase in compensation per employee accelerated to 7.6% yoy, following a yoy decrease in predominant part of the activities in 2019. The increase in income growth in *services* resulted in nominal

Graph 1 Contributions to GDP growth



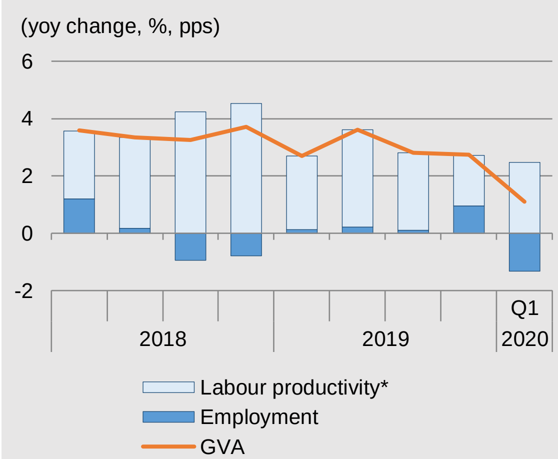
Source: NSI

Graph 2 Industry and business climate



Source: NSI

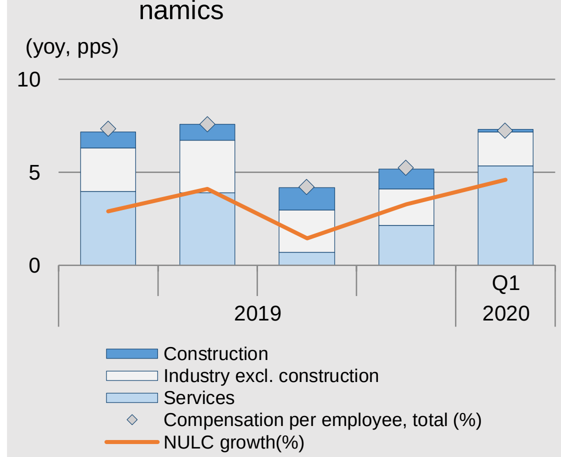
Graph 3 GVA growth by labour factors



*Imputed rent is not subtracted from the GVA

Source: NSI, MF

Graph 4 Compensation per employee growth by economic sectors and NULC dynamics



Source: NSI, MF

NULC growth of 5.3% yoy. Meanwhile, a marked slowdown in compensation per employee was observed in *industry*. The growth of 6.8% yoy was almost twice lower than in the first quarter of 2019. Nonetheless it outstripped the rise in productivity and contributed to a NULC increase in the industrial sector of 6.1%.

Inflation

The drop in energy prices caused an overall decrease in consumer prices of 0.3% mom in May. Energy prices went down by 2.3% due to lower prices of gas, heating and fuels for personal transport equipment. On the international market, energy commodity prices jumped, led by higher crude oil prices, up by more than 30% in USD terms. Food prices in Bulgaria increased by 0.2% in May, due to the increase in processed foods prices of 0.6%.

Annual inflation continued to decline for a fourth consecutive month in May, as core inflation also slightly decelerated. Inflation slowed down to 1% yoy compared to 1.3% yoy in April. Energy goods had the highest contribution, as the price decrease accelerated. Food prices followed different dynamics. Unprocessed food inflation accelerated, while the slowdown in the growth of processed food prices continued in May. The latter also resulted in lower core inflation, which edged down to 2.4% yoy in May, from 2.5% yoy in April.

External sector

In March, current account balance deteriorated on a year earlier for the first time since August 2019. The monthly deficit widened due to a larger trade deficit. The decline in exports of goods, down by 5.9% yoy, outpaced that of imports, down by 4.2% yoy. The decrease in trade was more pronounced with EU countries. By contrast, surplus in services increased by 6.7% yoy. Both export and import of services decreased by 19.3% yoy and 27.3% yoy, respectively, driven mainly by a decline in travel. Remittances from abroad went down by 66.4% yoy or almost EUR 80 mln. However, the favorable developments in the first two months of the year supported the doubling of the current account surplus in Q1 to EUR 501.6 mln or 0.8% of projected GDP. The withdrawal of part of the banks' deposits in parent companies abroad resulted in lower assets of the financial account under foreign currency and deposits in Q1.

In March Gross external debt declined by 0.6 pps yoy to 55.8% of projected GDP. All sectors contributed to the improvement.

Financial sector

COVID-19 pandemic and related containment measures and reduced economic activity seem to have affected the demand for loans in April. The growth of credit to the private sector decelerated to 7.6% yoy from 9.1% at end-March. Credit to non-financial corporations had the highest negative contribution, as its growth slowed down from 5.2% to 3.2% yoy with probably negative impact from the lockdown and worsened expectations. New loans to NFC lowered by 30% yoy in line with significant drop in business climate and most short term indicators in April. On the back of consumer confidence slump, in April households' consumer credit growth decelerated, for a second month in a raw, to 8.4%, down from 10.4% in March. These developments were in line with the lower domestic demand and decreased employment in Q1 as well as with the slowdown in wage dynamics in March. At the same time, dynamics of loans for house purchases still do not suggest any significant negative impact. The rate of growth in the segment edged down from 14.8% in March to 14.5% yoy at end-April and the monthly flow was positive. Although bad and restructured loans have kept a constant share of 8.8% in total households and NFC credit, in April the stock increased for the first time since October 2014, up by 0.9% yoy, led by corporate loans.

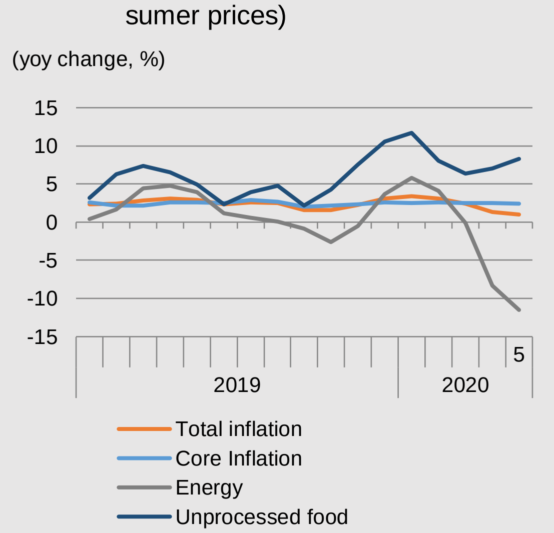
Fiscal sector

Despite a decrease in revenues, budget balance remained at a surplus for a fourth consecutive month and at end-April reached 1.4% of projected GDP. For the first time since the beginning of the year accumulated budget proceeds decreased, down by 3.6% yoy. It resulted from a drop in tax and non-tax revenue, while grants and donations almost doubled. Nearly all tax revenue's subgroups decreased, except for social and health insurance contributions, up by 6.2% yoy. A 20.7% fall was reported in non-tax revenue. Expenditures' growth decelerated to 4.1% yoy, being 5.5% a month ago. Social and personnel costs remained the main growth contributors, while a decrease was reported in subsidies, contribution to the EU budget, interest payments and current maintenance expenditures.

Government debt reached 21.3% of projected GDP.

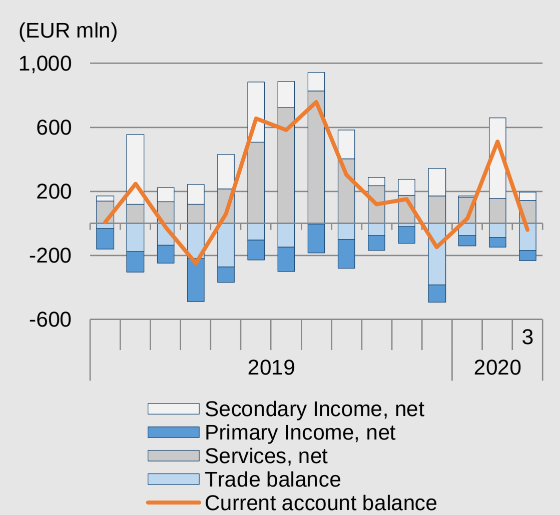
Table: Key Macroeconomic Indicators

Graph 5 Inflation (Harmonised index of consumer prices)



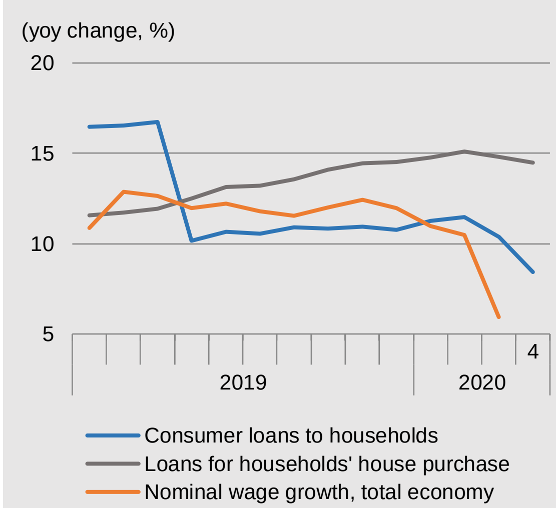
Source: Eurostat

Graph 6 Current account components



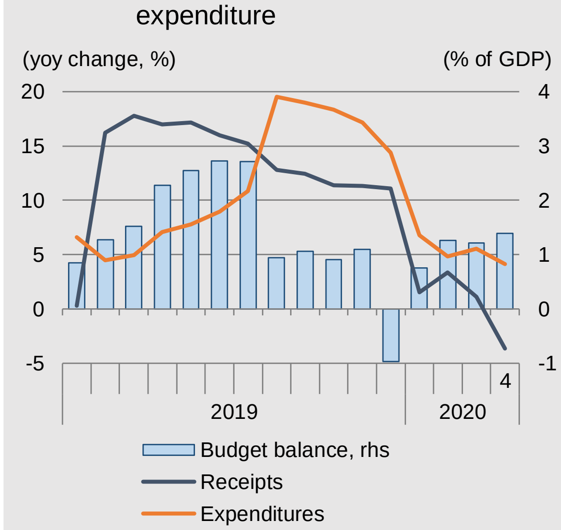
Source: BNB

Graph 7 Households incomes and loans



Source: BNB, NSI

Graph 8 Budget balance, receipts and expenditure



Source: MF

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