REPUBLIC OF BULGARIA
Ministry of Finance

CONVERGENCE PROGRAMME

(2024–2027)

2024
Sofia, Bulgaria

CONVERGENCE PROGRAMME

OF THE REPUBLIC OF BULGARIA

2024–2027

Sofia, 2024,
Ministry of Finance

Contents

List of Abbreviations

BNB	Bulgarian National Bank
CP	Convergence Program
EC	European Commission
ECB	European Central Bank
ESA 2010	European System of Accounts 2010
EU	European Union
EUR	euro
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
HICP	Harmonized Index of Consumer Prices
IMF	International Monetary Fund
LCIP	Labour costs per unit of production
LCIT	Law on Corporate Income Taxation
LIBOR	London Interbank Offered Rate
LSBRB	Law on the state budget of the Republic of Bulgaria
MoF	Ministry of Finance
NHIF	National Health Insurance Fund
NII	National Insurance Institute
NSI	National Statistical Institute
OECD	Organization for Economic Cooperation and Development
PFL	Public Finances Law
PITL	Personal Income Tax Law
pps	percentage point
REER	Real effective exchange rate
SGP	Stability and Growth Pact
SIC	Social Insurance Code
USD	US dollar
VAT	Value Added Tax
VATL	Law on value added tax
WM	Workforce Monitoring

1. Overall Policy Framework and Objectives

The Convergence Programme (CP) of the Republic of Bulgaria is prepared annually in April on the basis of the rules of the Stability and Growth Pact (SGP) - the regulatory framework for the coordination of national fiscal policies of the Member States of the European Union (EU). The programme is prepared in accordance with the Code of Conduct[1], which contain guidelines for the implementation of the SGP and guidelines on the format and content of the Stability and Convergence Programmes.

This year's edition of the Convergence Programme is the last, as changes to the SGP are expected to enter into force in May 2024. According to the reform of the EU's economic governance framework, a medium-term fiscal structural plan covering a period of 4 or 7 years will replace the Stability/Convergence Programmes and National Reform Programmes that each Member State shall submit to the European Commission on an annual basis.

The first version of the Convergence Programme (2024-2027) was approved by Council of Ministers' Decision № 314 and sent to the European Commission (EC) on 30 April 2024.

The current update of the adopted in April programme makes changes to part of the data and texts relating to 2023 as a result of new, more up-to-date data received from the National Statistical Institute (NSI) for the previous year. This aligns the data in the programme with the data sent by the NSI to Eurostat.

The Convergence Programme of the Republic of Bulgaria (2024-2027) reflects the fiscal effects on the parameters of the budgetary framework under a no-policy-change scenario. The choice of this scenario is a consequence of a caretaker government, which should not determine policy developments in the medium term.

Preserving the sustainability of the budgetary framework in the context of Bulgaria's commitments, both under the SGP and in relation to its euro area membership target, remains a fiscal policy priority in the medium term.

The long-term sustainability of public finances remains a key policy aspect, including in terms of boosting confidence and creating a predictable investment and business environment. The medium-term budgetary objective for the structural balance on an annual basis is -1% of Gross Domestic Product (GDP).

On the basis of the envisaged debt financing and GDP projections, General Government debt is projected to increase both in nominal terms and as a ratio of General Government debt to GDP in the coming years.

In the context of preserving macroeconomic stability and participation in Exhange Rate Mechanism II, Bulgaria guarantees that it will maintain the currency board regime at the current level of the fixed exchange rate of BGN 1.95583 to EUR 1 until the country joins the euro area.

This Convergence Programme covers the period 2024-2027 and consists of seven parts.

[1] http://data.consilium.europa.eu/doc/document/ST-9344-2017-INIT/en/pdf

This first part contains the general framework of the government's economic policies and objectives.

The second part analyses the economic development of the country in terms of key macroeconomic indicators and presents a forecast of their development in the medium term.

The third part is a description of the strategic fiscal policy objectives in terms of budget balance and government debt. It sets out the current budgetary position and expected developments over the reference period, with an emphasis on the structural balance. The main directions for the evolution of the debt position over the programme period are outlined. The key highlights of the policies and the specific measures for their implementation are also presented, as well as an assessment of the expected quantitative impact of their implementation.

In the fourth part, a sensitivity analysis of the forecast parameters is carried out and an alternative scenario for the country's economic development in the medium term is developed. The effect of the alternative scenarios on the budgetary parameters is also discussed. The effects on government debt of changes in the assumptions of the baseline macroeconomic scenario are also presented.

Part five is devoted to the sustainability of public finances. The main focus is on the long-term budgetary outlook in view of the effects of ageing of population.

The sixth part elaborates on the quality of public finances. Here the government's policy strategy in this area, the composition of expenditure, and the structure and efficiency of revenue systems are presented.

The seventh part reviews the institutional features of public finances in Bulgaria - budgetary procedures and national fiscal rules. This part of the programme also focuses on key legislative changes related to public finances.

2. Economic Prospects

2.1 Assumptions for the development of the world economy

This Convergence Programme is based on the macroeconomic forecast for the period 2024-2027, which has been developed with the medium-term macroeconomic model of the Institute for Analysis and Forecasting (IAF), with assumptions for key indicators of the external environment, with cut-off date 13 March 2024.

The world economy has proved more resilient than expected in 2023, despite geopolitical uncertainty, still high inflation and tight monetary policy. Lower international energy and food prices have led to a slowdown in inflation among advanced and many of the developing countries. This allowed major central banks to end their policy of raising key interest rates at the end of the year. At the same time, GDP growth in the EU slowed significantly in 2023 as a result of weak household consumption and relatively low investment activity. The inflation rate has also declined, mainly driven by falling international commodity prices.

Table 2-1: Assumptions on key macroeconomic indicators

International environment	Historical data	Forecast			
	2023	**2024**	**2025**	**2026**	**2027**
World economy (real growth,%)	3.1	3.1	3.2	3.1	3.1
European economy – EU (real growth,%)	0.4	1.0	1.7	1.9	1.7
Annual average exchange rate USD / EUR	1.08	1.08	1.08	1.08	1.08
International commodity prices (in dollars, change in%)					
Crude oil, Brent	-17.2	-1.6	-6.7	-4.1	-2.6
Non-energy commodities	-9.8	-1.8	-0.8	-1.0	-0.5
Food	-9.2	-9.0	-1.5	-1.6	-0.8
Beverages	1.4	23.9	-0.5	-0.5	-0.5
Agricultural raw materials	-4.7	8.4	-0.4	-0.4	-0.4
Metals	-9.6	-4.3	-0.3	-0.7	0.1
EURIBOR 3m.	3.1	3.5	2.6	2.4	2.3

Source: WB, Eurostat, ECB, IMF, Bloomberg, own calculations

The international environment is expected to remain volatile over the forecast period, but without significant structural shocks and/or shortages of key commodities. The continued slowdown in inflation will contribute to a shift towards a policy of interest rate cuts by the ECB and a gradual improvement in financing conditions. Growth in the EU is expected to remain subdued in early 2024 and then accelerate, reaching 1% in the current year and 1.7% in 2025. Following the sustained GDP growth in the USA and some developing countries over the past year, the global economy is projected to continue growing at around 3.1-3.2% over the medium term. Both EU and global rates remain below average compared to the pre-pandemic period. The more moderate external demand, mainly from the EU, than in the previous forecast is a factor for the expected lower real export growth in Bulgaria in the current forecast.

2.2 Economic prospects and cyclical development

2.2.1 Economic growth

In 2023, Bulgaria's real GDP growth slowed to 1.8% from 3.9% in 2022. The weaker growth was mostly due to a decline in exports and investment. Weaker demand from trading partners was reflected in a 1.9% decline in exports of goods and services. Fixed investment grew by 3.3% supported by public capital spending, while private investment activity remained weak. At the same time, inventories in the economy declined substantially and this predetermined the 18.1% fall in total investment. The use of accumulated inventories led to a significant reduction in domestic imports of 6.3%. Against the backdrop of weaker external demand and investment activity, consumption growth remained robust. Household consumption growth accelerated to 5.4% due to higher real disposable income growth.

On the supply side, gross value added increased by 0.8%. Weaker growth was reported relative to 2022 in both services and industry, with the only sub-sectors with growth acceleration being the consumption-related trade; transport; accommodation and food service activities.

2.2.2 Cyclical development[2]

Potential GDP growth in 2023 reached 2.6%. For the period 2024-2027, growth is expected to be in the range of 2.9-3%, with an increase in investment leading to an increase in the contribution of the capital and a reduction in unemployment keeping the contribution of the labour positive. Total factor productivity will be the main contributor to growth throughout the forecast period.

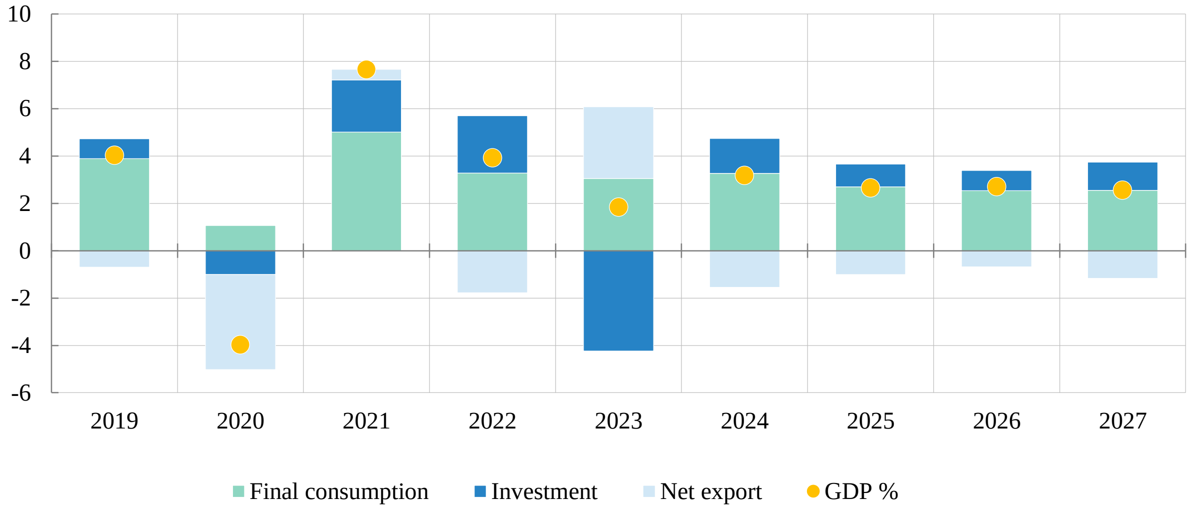
The output gap in 2023 was positive at 0.7%. For 2024, as output growth accelerates, the deviation is expected to widen to 0.8%. In the following years, the output gap will shrink and close at the end of the projection period.

2.3 Medium-term scenario

In 2024, real GDP growth is expected to accelerate to 3.2% due to higher growth in public investment and consumption expenditure. Private investment is expected to pick up in line with stronger external demand. The contribution of inventories to GDP growth will be neutral. Weaker employment growth and slowing consumer credit growth will be reflected in a slowdown in household consumption growth, which will continue to be supported by real disposable income growth. The improvement in the external environment will support export growth. Import growth, as a result of strong domestic demand, will be higher than export growth and the contribution of net exports to GDP growth will be negative.

[2] The cyclical development of the economy is measured by the output gap. It is calculated as the difference between actual and potential GDP relative to potential GDP. Potential GDP for the Bulgarian economy is calculated using a production function according to a methodology developed by the EC: Havik, K., & Kieran Mc Morrow, K., & Fabrice Orlandi, F., Christophe Planas, C., Rafal Raciborski, R., Werner Roeger, W., Alessandro Rossi, A., Anna Thum-Thysen, A. & Valerie Vandermeulen, V.,"The Production Function Methodology for Calculating Potential Growth Rates & Output Gaps," European Economy – Economic Papers 535, 2014.

Graph 2-1: Contributions by components to GDP growth (pps)



Source: NSI, IAF

Economic growth will slow down to 2.7% in 2025. The expected slowdown in income growth will lead to lower household consumption growth. At the same time, as uncertainty eases and demand picks up, private investment growth will accelerate. Export growth will accelerate as a result of stronger external demand in the EU, but the contribution of net exports will remain negative.

In 2026 and 2027, GDP will grow by 2.7% and 2.6%, respectively. Real income growth will support robust consumption growth. The increase in demand will have a positive impact on investment activity. External demand will remain robust and export growth will remain close to that in 2025. Import growth will be higher, reflecting the planned acquisition of military equipment.

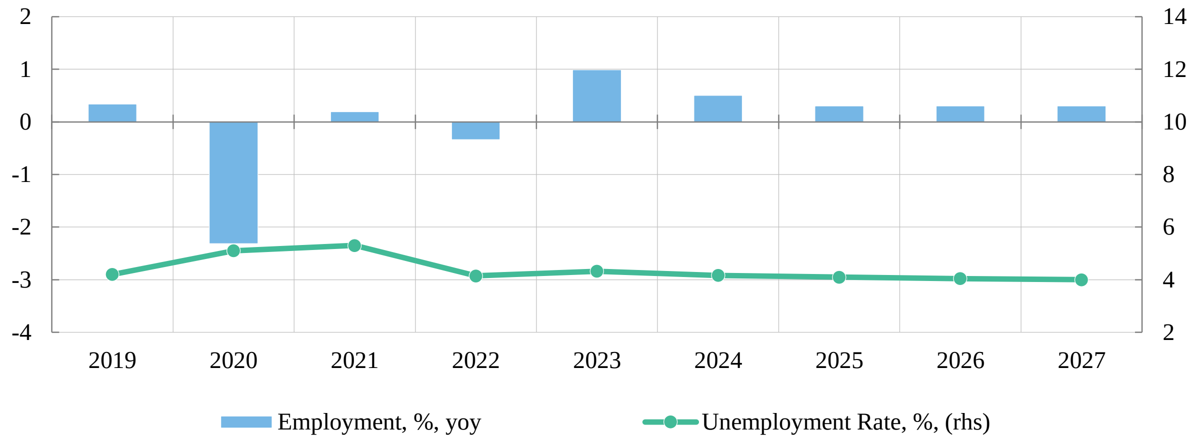
2.4 Sector balances

2.4.1 Labour market, income and productivity

Although the Bulgarian economy faced a number of challenges in 2023, mostly related to external factors, as a result of which its real growth rate slowed down, the employment recorded a relatively high annual growth rate of 1%. The average annual number of employed in the Bulgarian economy reached 3,480.7 thousand in 2023, with an increase in their number in the service and construction sectors. The main contributors to employment growth were the economic activities "Public administration; education; human health and social work activities", "Trade, transport, accommodation and food services" and "Information and creative industries; telecommunications". In construction, employment grew by 1.8%, driven mainly by high demand for housing. Demand for labour remained high and the share of entrepreneurs identifying labour shortages with the necessary qualifications and skills as a constraint to business expansion continued to increase. In industry and services, their share has now reached the figures recorded in 2019.

The economic activity rate of the population aged between 15 and 64 reached 73.9% in 2023 and the employment rate was 70.7%. There was a slight increase in the unemployment rate to 4.3%. The number of unemployed has reached relatively low levels and is increasingly being exhausted as a source of employment growth in the coming years.

Graph 2-2: Dynamics of employment and unemployment rate, %



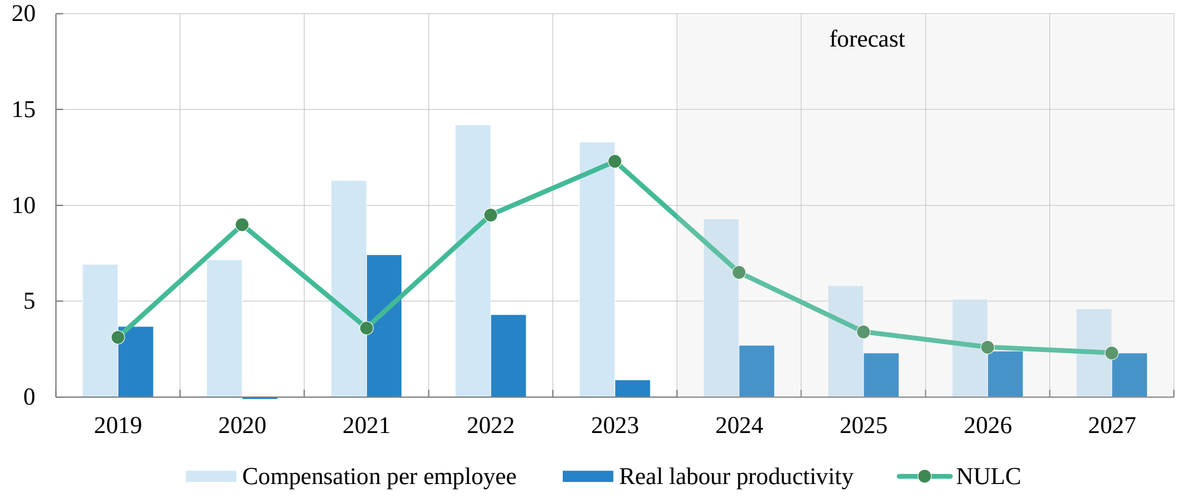
Source: NSI, IAF

The expectation that Bulgaria will follow a steady economic growth trajectory throughout the forecast period also determines the forecast for labour market dynamics in 2024-2027. In 2023 relatively high employment growth was observed, but in 2024 its pace is expected to slow down to 0.5%. The main argument for this dynamics is the negative demographic development in the country and the running out of opportunities to increase labour supply. Although we expect a steady upward trend in employment over the 2024-2027 period, changes in the unemployment rate are minimal, and the unemployment rate is expected to reach 4% in 2027. There are increasingly limited opportunities to transition from unemployment to employment, and our underlying assumption is that in the coming years, employment growth will occur predominantly by bringing some of the inactive back into the labour force or by attracting labour from other countries.

In 2023, the nominal growth of the compensation per employee was 13.3%. The rate still remains high, driven mainly by the increase in compensation per employee in the industry sector (22.6%) and the higher wage costs in the budgetary sector. In the service sector, growth in compensation per employee remained relatively lower (9.9%). Due to the higher increase in compensation per employee relative to labour productivity growth, the nominal unit labour costs (NULC) increased by 12.3% y-o-y. These developments reflected the reported high growth in labour income over labour productivity in the industry, agriculture, and construction sectors, contributing to increased labour cost pressures in these sectors. Real unit labour costs in the economy as a whole increased by 4.5%.

The preliminary data for the average wage growth in 2023 showed that the growth in the public sector (14.9%) exceeded that in the private sector (13.2%). For the economy as a whole, the average wage has risen by 13.7% in nominal terms and managed to offset the increase in consumer prices in the country, with real growth of the indicator remaining positive at 4.7% (deflated by HICP).

Graph 2-3: Dynamics of nominal ULCs and components (%)



Source: NSI, IAF

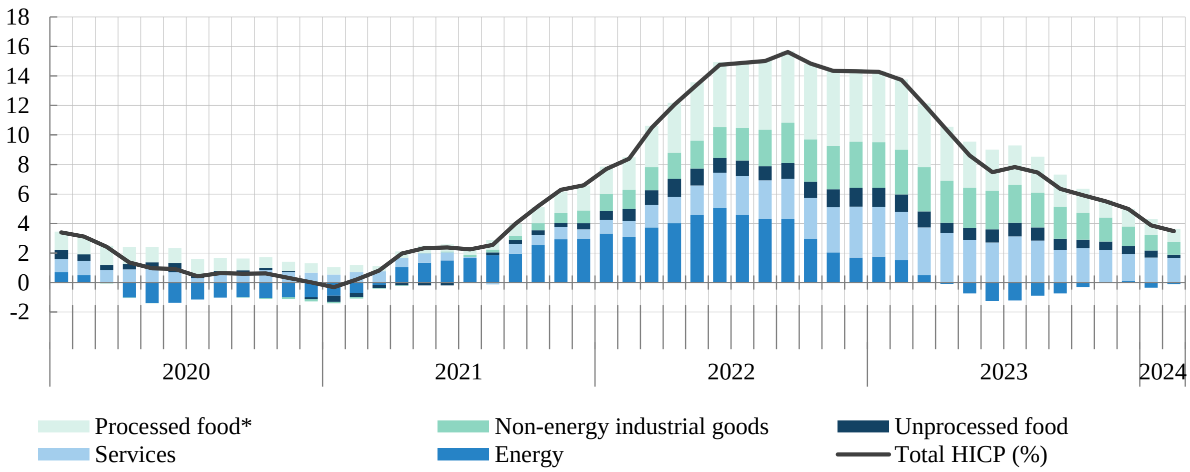
In 2024, the growth in compensation per employee is expected to ease off, following the slowdown in inflation, employment dynamics, and the acceleration in real labour productivity growth. In nominal terms, the growth rate of the indicator is estimated at 9.3%. A higher contribution is expected on the back of the tightening labour market conditions and growing labour shortages, as well as to the increase in the minimum wage in the country, in line with the adopted regulatory changes. Labour income growth will continue to decelerate until the end of the projection period as a result of the slowdown in inflationary developments and the lower contribution from the minimum wage adjustments.

A more substantial acceleration of real labour productivity of 2.7% is expected in 2024 due to the expected increase in real GDP growth. In the period 2025-2027, the estimated dynamics of the indicator is expected to maintain a relatively stable growth rate of around 2.3%. Together with lower nominal labour income growth, this will lead to a moderation of nominal unit labour cost growth to around 2.3% at the end of the projection period.

2.4.2 Inflation

The disinflationary trend in the country, which has been observed since the last quarter of 2022, persisted throughout 2023 and continued into early 2024. The annual HICP inflation rate in February 2024 decelerated to 3.5%. The slowdown is mostly attributable to the downward trend in international commodity prices as well as the base effect associated with the accelerated price increases in the previous year. In this context, all major HICP components reported a slowdown in their inflation rates, except for alcohol and tobacco, following the introduction of higher excise duties on cigarettes in March 2023 and January 2024.

Graph 2-4: Annual HICP inflation rate (%) and contributions by main components (pps)



* processed food including alcohol and tobacco

Source: Eurostat, own calculations

Services contributed the most to the headline inflation rate in February 2024, followed by non-energy industrial goods and food, while energy products contributed negatively. Core inflation[3] narrowed to 4.3% y-o-y on the back of a slowdown in the inflation rate of consumer goods, and consumer durables in particular, as well as catering and transport services.

Inflation at the end of 2024 is expected at 2.3% and the annual average - at 2.4%. Core inflation and services in particular will have the largest contribution to inflation at the end of 2024. Energy is also expected to have a small positive contribution of 0.1 pps. Among the factors for this is the expected increase in transport fuel prices in line with the crude oil futures dynamics at the end of the year. The forecast also includes three specific measures intended to reduce inflation. They are aimed at lowering the prices of firewood from state forestries, medicines for cardiovascular diseases in the positive drug list of the National Health Insurance Fund, as well as full coverage of the state-financed fees for university degrees. Their overall effect in average annual inflation is estimated at -1.0 pps.

In the coming years, end-of-period inflation will continue to gradually decelerate, mostly in line the expected dynamics of international prices. It is projected to be 2.2%, 2.1% and 1.8% in 2025, 2026 and 2027, respectively. The contribution of core inflation components will continue to narrow but will be the leading driver behind the headline inflation in line with the projected increase in domestic demand, as well as labour costs.

The annual average inflation is forecast to accelerate slightly to 2.8% in 2025. This is associated with the planned return to the standard VAT rate for restaurant services in early 2025, as well as the waning of the base effects of the three measures described above to reduce the prices of firewood, medicines for cardiovascular diseases and state-financed fees for university degree. The average annual rate of inflation would slow to 2.0% in 2026 and 1.9% in 2027.

Table 2-2: Forecast of HICP dynamics in the period 2024–2027

	2024 г.	2025 г.	2026 г.	2027 г.
Average annual inflation (in %)	2.4	2.8	2.0	1.9
End-of-period inflation (in %)	2.3	2.2	2.1	1.8

[3] Core inflation includes services and non-energy industrial goods.

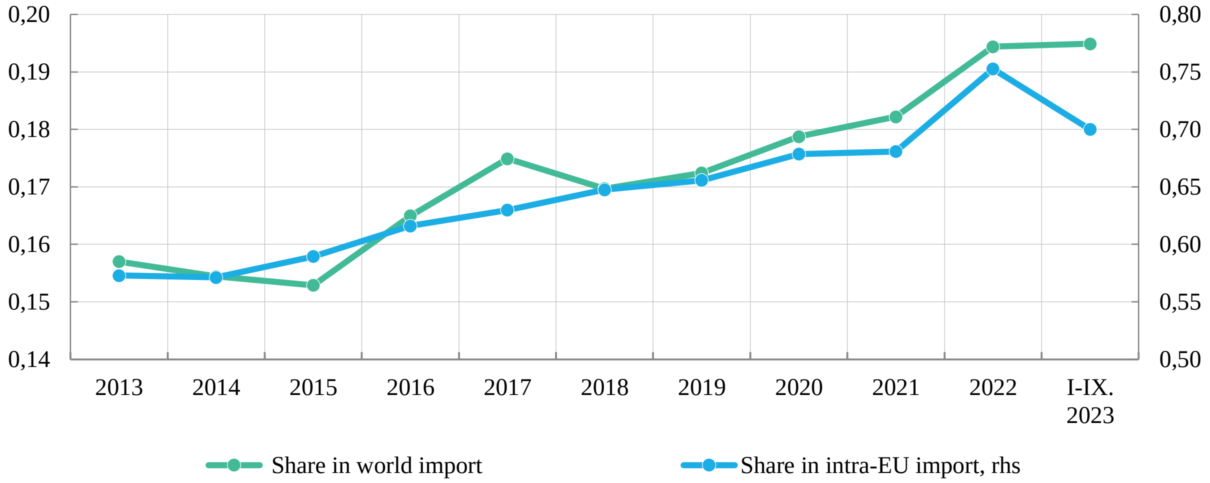
Source: IAF

2.4.3 External sector [4]

In 2023, the current and capital account balance was reported at a surplus of EUR 1.2 billion (1.3% of GDP), being negative in 2022.

An improvement in the balance was reported for both the capital account and trade in goods and services. Export of goods declined by 8.1% and import by 10.1%, which determined the narrowing of the trade deficit by 2.1 pps to 3.9% of GDP. The dynamics in foreign trade was due to fall in prices of internationally traded commodities as well as the decline in traded quantities. The decline in export in real terms was driven by weaker GDP growth dynamics in the EU, bottlenecks in supply chains due to conflicts in the Middle East and planned repairs of some of the country's largest enterprises. At the same time, the draw down on inventories has led to a more substantial decline in import relative to export and an improvement in the trade balance.

Graph 2-5: Bulgaria's share in international trade (%)

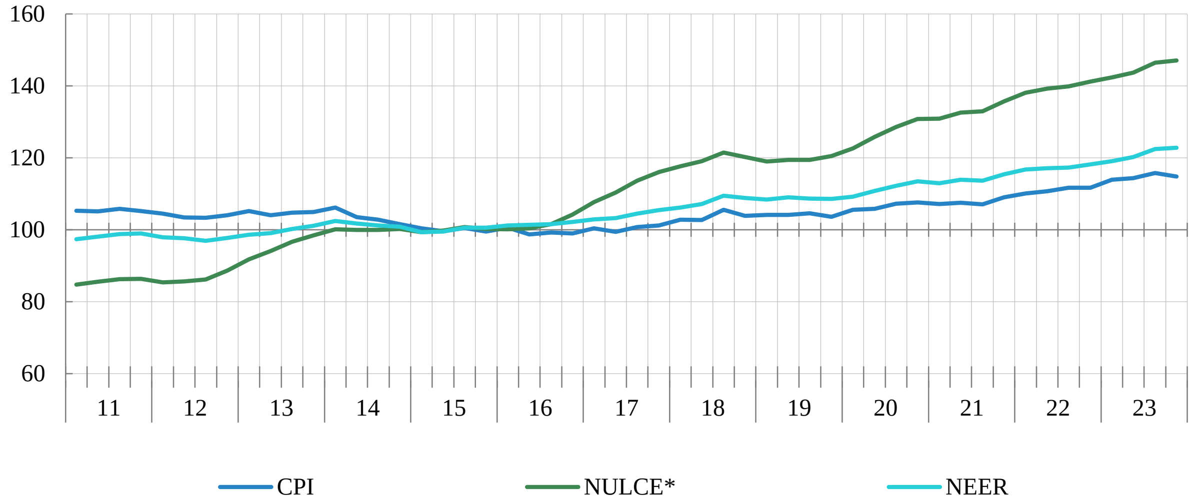


Source: IAF with data from WTO

In terms of the country's market position relative to the rest of the world, a slight improvement was reported in the first nine months of 2023. Within EU, the market share of Bulgarian export lowered compared to 2022, but remained higher compared to 2021.

4 The analysis for the External Sector is developed with statistical data for the Balance of Payments (analytical presentation), with the exception of graphs and data for which a different source is explicitly indicated.

Graph 2-6: REER of Bulgaria compared to 36 industrial countries, 2015=100



* Nominal labour costs per unit of output for the total economy

Source: EC

The dynamics of the real effective exchange rate have shown a substantial acceleration since mid-2021. Due to the significant increase in global inflation over the period, the REER calculated using the consumer price index (CPI) recorded a smaller increase, which was mainly due to the appreciation of the nominal effective exchange rate. However, in the case of the indicator with unit labour costs, the deflator had a more significant contribution. The real effective exchange rate dynamics in 2023 were mostly driven by the appreciation of the nominal effective exchange rate. This was true both for the indicator deflated by the CPI and the one deflated by unit labour costs in total economy.

In 2023, the services surplus continued to grow, reaching 7.1% of GDP, with the main contributors to the improvement coming from foreign travel to the country, as well as information technology and telecommunications services. The overall deficit on income items worsened, reflecting the larger amount of investment income paid to non-residents. The current account deficit declined to 0.3 percent of GDP in 2023, from 1.4 percent in 2022.

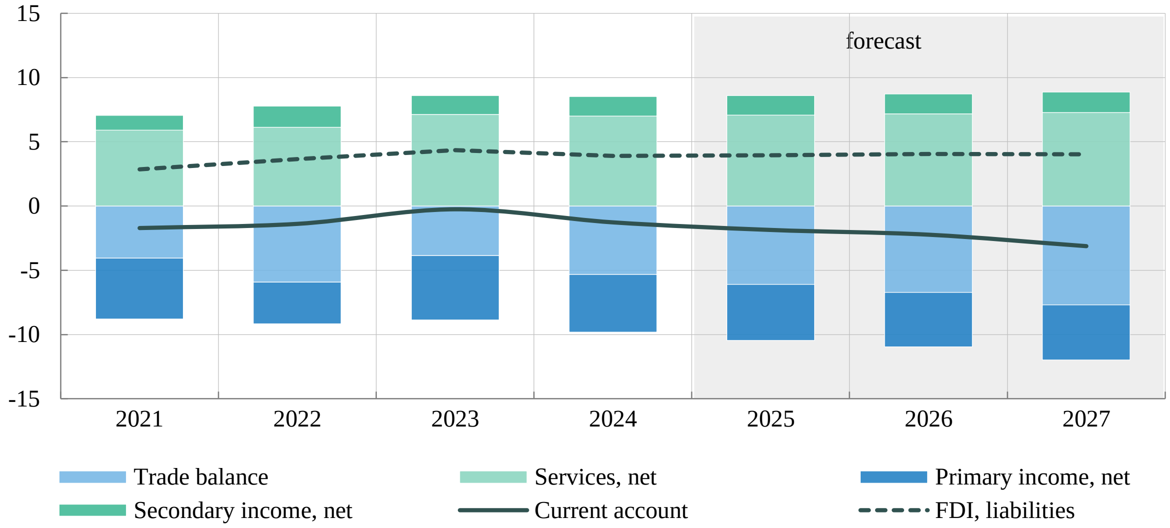
Over the 2024-2027 forecast period, the country's external position is expected to remain stable.

Sustained domestic demand growth, along with a more moderate recovery in the external environment, will predetermine a gradual widening of the trade deficit and a decline in the current account balance. A current account deficit of 1.3% of GDP is expected in 2024. The expected accelerated nominal increase in import relative to export of goods reflects not only changes in volume but import prices will surpass those of export as well. The latter is due to the assumption that the country's main refinery switches to importing crude oil other than Urals. Therefore, the price in the energy commodity group will accelerate compared to 2023, while price dynamics among the other groups is expected to be subdued. The surplus in the services article will be about 7% of GDP in 2024. A full recovery in international travel receipts is expected during the year, following the severe Covid-19 shock. The overall balance of income articles will remain negative at 2.9% of GDP.

In 2025-2027, the negative current account balance will widen to 3.1% of GDP at the end of the period. Despite the favourable terms of trade, nominal growth in merchandise import will outpace export due to stronger growth in consumption and investment, including the acquisition of military equipment. The surplus in services will widen slightly, supported by an increase in the positive balance in tourism and business services. The primary income deficit will be around 4.3-4.4% of GDP. Recovery and Resilience plan funds and incoming transfers over the 2021-

2027 programming period will support the secondary income surplus, but no significant change in the balance as a percentage of GDP is expected (1.5-1.6% of GDP).

Graph 2-7: Current account (% of GDP)



Source: BNB, NSI, IAF

In 2023, the inflows to the financial account[5] exceeded that of assets abroad. A major contributing factor was foreign direct investment (FDI) inflows, which reached EUR 4 billion or 4.3% of GDP. The bulk of inward FDI was in the form of reinvested earnings from parent companies to domestic companies.

Throughout the forecast period, FDI is expected to increase at a rate similar to overall economic activity and the FDI-to-GDP ratio will be around 4%.

2.4.4 Monetary and financial sector

The main objective of monetary policy in Bulgaria is to maintain price stability by ensuring the stability of the national currency. This objective is achieved through a currency board arrangement with a fixed exchange rate of the national currency against the euro.

As of end-December 2023, the market value of Bulgaria's international foreign exchange reserves, the assets on the balance sheet of the Bulgarian National Bank's (BNB) Issue Department, amounted to EUR 41.9 billion (44.6% of GDP), increasing by EUR 3.5 billion from end-2022. According to the principles of operation of the currency board, the amount of international foreign exchange reserves corresponds to the balance sheet value of the liabilities of the BNB's Issue Department[6]. The largest contribution to the increase in the liabilities of the Issue Department in 2023 was from the liabilities to banks, mainly as a result of the increase in the minimum required reserves (MRR), which was driven by the increase in the MRR rate to 12% from mid-2023. At the end-December 2023, foreign exchange reserves provided coverage of 9.3 months of imports of goods and non-factor services, while their ratio to the country’s short-term external debt amounted to 503%.

At the beginning of 2023, the banking system continued to be characterised by high liquidity, a slow and weak transmission of the ECB's monetary policy tightening to deposit and lending

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[5] Analytical presentation of the balance of payments.

[6] The liabilities of the Issue Department of the BNB include notes and coins in circulation, liabilities to banks, liabilities to the government and other budget institutions, liabilities to other depositors and the Banking Department deposit.

interest rates, especially in the households sector, and continued high household credit growth, supported by both demand-side factors and an active supply of credit by banks. Taking these developments into account, as well as the strong consumer demand and the high rate of consumer price increases, on 26 April 2023 the Governing Council of the BNB decided to increase the MRR rate on funds attracted by banks in two steps. Pursuant to the decision of the Governing Council of the BNB, as of 1 June 2023, the MRR rate on funds attracted by banks from non-residents was increased from 5% to 10%, and as of 1 July 2023, the MRR rate on funds attracted by banks from both residents and non-residents was increased from 10% to 12%.

The BNB's decision was aimed at tightening the monetary conditions in the country by withdrawing part of the excess liquidity in the banking system, thus reducing the banks' free resources and lending capacity and creating an incentive for faster and stronger transmission of the increased interest rates in the euro area to the interest rates in Bulgaria. As a result of this measure, liquidity in the amount of about BGN 3.3 billion was withdrawn from the banking system, which, however, did not contribute to slowing down the annual growth of credit to households (15.9% at the end of the year), as the increased MRR requirement was implemented by the banks by transforming mainly foreign liquid assets into minimum required reserves and, to a lesser extent, by transforming excess reserves into minimum required reserves. By the end of 2023, the effects of the increase in the MRR rate on deposit and lending rates to households as a whole for the banking system also remained limited due to the remaining ample liquidity.

In 2023, the banking sector capital ratios' levels remained well above minimum regulatory and capital buffer requirements. Non-performing loans and advances on banks' balance sheets and their share in total loans and advances continued to show a decline as a result of banks' write-off and sale operations of non-performing loans, as well as the growth in the amount of the loan portfolio. With the increase in the banking assets and the change in the interest rate cycle, higher net operating income was reported relative to the end of 2022, resulting in higher profit for the banking system in 2023. The liquidity position of the banking system remained stable throughout the year, with the ratios of liquidity coverage and of net stable funding maintained at levels well above the minimum regulatory requirements.

In fulfilling its macroprudential mandate, the BNB supervises the activities of credit institutions and the banking system on the basis of continuous monitoring, identification and assessment of systemic risks. The level of the combined buffer requirement in Bulgaria is the highest among the countries represented in the Single Supervisory Mechanism. As one of the macroprudential tools applied, the countercyclical capital buffer is aimed at preserving the ability of the banking system to cope with the adverse effects of cyclical risks related to the business and financial cycle by strengthening the capital position of banks. Effective as of 1 January 2023, the applicable level of the buffer is 1.5% for credit risk exposures in the Republic of Bulgaria, and in view of the sustained high credit growth rates and uncertainty in the economic environment, the BNB Governing Council decided to increase the level of the countercyclical capital buffer rate to 2.0%, effective as of 1 October 2023. The decisions to increase the level of the countercyclical buffer aim to strengthen the resilience of the banking system in case of profitability and capital position pressure, caused by a potential increase in non-performing loans and their impairment. Among the priorities of the macroprudential activity of the BNB in 2023 was the regular analysis of the risks arising from lending, where residential real estate is used as a collateral. With regard to risks of a structural nature, during the 2023 annual review of the buffer for other systemically important institutions, carried out by the Governing Council of the BNB, six institutions were identified as such and for them the buffer levels in 2024 will be in the range of 0.5% up to 1.0%. During the 2023 biennial review of the systemic risk buffer, its level was confirmed at 3% of local risk-weighted exposures.

According to the projections of the Institute for Analysis and Forecasting, the rate of growth of claims on the private sector will slow until the end of 2024, and this will happen both for the claims on enterprises and on households. However, the growth of households' claims will remain at relatively higher levels and will be around 12.1% y-o-y at the end of 2024, supported by still strong growth of nominal incomes. The annual growth of claims on enterprises[7] at the end of 2024 will be around 8.1%.

In the period 2025–2027, credit to households is expected to decelerate along with expected slowdown in households' consumption and lower nominal growth of compensation of employees. The expected rise in interest rates, as a result of strengthening the transmission of the ECB's monetary policy transmission, together with lower inflation rates, is also expected to contribute to a slowdown in households' credit. The growth of their claims will decline to 9% in 2025 and to around 7.2% at the end of 2027. In 2025–2026, annual growth of corporate claims is expected to accelerate in the context of stronger absorption of Recovery and Resilience Plan funds and in sync with the expected acceleration in private investment. It is expected that the growth of total claims on enterprises will be 8.7% at the end of 2025, and 8.9% at the end of 2027. Overall, claims on private sector's growth will slow from 9.7% in 2024 to 8.2% at the end of the forecast horizon.

[7] The data refer to non-financial and financial enterprises from the monetary statistics of the BNB.

3. Government Balance And Debt

3.1 Policy strategy

Adherence to a consistent and predictable fiscal policy remains a top priority to ensure fiscal and macroeconomic stability, as well as compliance with the rules and restrictions of European and national legislation, despite external and internal risks and challenges. The development of the parameters of the budgetary framework for the period 2025–2027 is in line with the deficit targets to ensure fiscal sustainability and predictability and compliance with the Maastricht criteria.

As the current Convergence Programme transitions to the upcoming development later in the year of the first medium-term fiscal-structural plan for Bulgaria, which should replace the current Stability Programmes/Convergence Programmes and National Reform Programmes, it reflects the parameters of the budget framework under the current national and European legislation.

In the current political situation, the caretaker government cannot commit to different fiscal perspectives in the absence of clarity on the horizon of policy development, reforms and investments, therefore the estimates for the parameters of the budget framework are prepared under a base scenario with no change in policies and objectives on the basis of the latest updated medium-term budget forecast for the period 2024-2026 approved by the government in January this year. The 2027 data is a continuation of 2026 with changes compared to the nominal values of the revenue and expenditure indicators only in relation to policies and programmes whose fiscal dimension is tied to assumptions for which automatic mechanisms are foreseen, to the implementation of multiannual programmes and projects and with other non-discretionary effects.

The government debt management policy for the forecast period follows the outlined objectives of the fiscal policy and will be aimed at fulfilling the strategic goal of providing the necessary resources for refinancing the debt outstanding, financing the planned levels of the state budget deficit and ensuring the liquidity position of the fiscal reserve.

Among the basic factors that are expected to be the focus of attention when conducting the debt policy are those related to the geopolitical security environment, economic activity and inflationary expectations of the key economies, the monetary policies of the main central banks, in the context above all of the influence, which the same have on the state of the markets, the expected risk premiums, etc.

In order to realize the set goals, in the period 2024-2027 it is planned to use the issues of government securities both on the domestic and on the international debt market as the main instrument for providing debt financing. The determination of the specific characteristics of the new debt will be in accordance with the characteristics of the debt repayment profile, domestic and international capital markets conditions, the size and price of financing, the diversification and preferences of the investor base, the possibilities of reducing the refinancing risk.

In addition, to the market-oriented financing of the state budget, it is planned to provide an opportunity to negotiate new external government debt through loans under financial instruments from the EU and/or from international financial institutions. With regard to the financing of new investment projects and specific programmes with government and government guaranteed loans, the approach applied so far will be followed, aimed at strict compliance with the legally defined rules and requirements, taking into account the government's priorities for supporting the development of strategic sectors in the economy.

3.2 Medium-term objectives

In 2024, the budget balance of the "General Government" sector is expected to be negative in the amount of 3.0% of GDP, and the forecast for the following years of the period is for a deficit of the sector in the amount of 3.0% for 2025; 2.8% for 2026 and 3.0% of GDP for 2027. The projections presented in this part were developed under no-policy-change scenario, based on the approved fiscal parameters and assumptions contained in the Law on the state budget of the Republic of Bulgaria for 2024 and the latest Updated Medium-term Budget Forecast.

Part of the deficit of the "General Government" sector, which is reported on an accrual basis, is due to the time shift in the reporting of the costs of supplies of military equipment, which were paid in previous years on a cash basis. According to the ESA 2010 methodology, government expenditures on military equipment are reported in the year of their delivery. Therefore, the investment costs for the acquisition of a new type of combat aircraft made in 2019 and 2020 in the amount of BGN 2,197.7 million have an impact on the costs for the period 2025–2027, as together with the shifted accounting and of other expenditures for military equipment worsen the deficit by 0.3 percentage points of GDP for 2025 and 1.3 pps of GDP for 2027 respectively, as the largest deliveries of military equipment during the period under consideration are expected to take place in 2025 and 2027. This impact is temporary and does not lead to a permanent deterioration of the budgetary position and the disruption of fiscal sustainability in the long term.

The main contribution to keeping the deficit at a relatively constant level as a share of GDP during the forecast period is expenditure, which is expected to remain constant at a level of around 40.2% of GDP for the period 2024–2026, with a decline planned for 2027 to 38.9% of GDP. Revenues are projected to be 37.1% of GDP in 2024–25 and to increase to 37.6% of GDP in 2026, with a slight decline as a share of GDP to 35.9% in 2027.

In the period 2025–2027, a nominal increase in all revenues is expected, which is due to a rise in receipts from the main revenue elements, with tax and insurance revenues having the largest increase in receipts from social security contributions and direct taxes, which is the result of the higher household incomes, the increase in the maximum insurance income, the possibility of choosing insurance and the increase in the insurance length of service at retirement. In indirect taxes, the highest positive impact is the planned gradual increase in the excise rate on cigars and cigarillos, on smoking tobacco, on heated tobacco products, on liquid for electronic cigarettes, as well as the change in the specific and proportional excise duty on cigarettes, which has an impact on revenues from VAT and excise taxes. In non-tax revenues, a more significant growth is observed in capital transfers received in 2025-2026 due to the expected increase in EU revenues under the Recovery and Resilience Plan, in dividend revenues from public enterprises, revenues from household waste charges due to the new mechanism of taxation of households and companies, coming into force from 01.01.2025.

In terms of expenditure, an increase in social transfers, personnel and interest costs is planned.

Social transfers, other than those in kind, which cover the costs of pensions, as well as social security benefits and allowances, are growing due to the annual pension indexation from 1 July under the Swiss rule of the Social Insurance Code, of the planned increase in the number of newly granted pensions in considering the periods of military service and the periods of repression suffered as actual seniority for the right to a pension and the increase in the amount of widow's supplements to pensions to 30% of the deceased spouse's pension. There is also a forecast growth in social benefits under the Social Assistance Law and the Persons with Disabilities Law, due to the planned change in the poverty line and the growth of the unemployment benefit, which have an impact on the calculation of the remuneration of personal assistants under the Law on Personal Assistance and the remuneration of foster families under the Child Protection Law.

In the case of health insurance payments, an annual increase is expected in the costs of hospital care, for medical products for home treatment, as well as for products for malignant diseases and for life-threatening and emergency interventions/cases.

Personnel costs are increasing due to the planned annual growth of the minimum wage in accordance with Art. 244 of the Labour Code, the planned increase in funds for the delegated activities in education in connection with the policy to increase teachers' salaries until reaching an average salary of not less than 125% of the national average salary, a growth in funds for wages and salaries of staff in elective positions and those employed in the judicial system, as well as a result of increases in staff costs in connection with the policy of overcoming disparities in staff remuneration in budget organizations.

Capital expenditure on gross fixed capital formation rises in 2024 to 4.0% of GDP, then ranges from 3.1% to 3.6% of GDP towards the end of the period. The change in the indicator is related to the dynamics of supplies of combat equipment during the forecast period, as well as to the accelerated rate of absorption of funds from European funds and under the National Plan for Recovery and Resilience.

3.3 Actual balances and updated budgetary plans for the current year

3.3.1 Update of the 2023 budget framework

2023 began in the absence of adopted by the National Assembly annual laws on the state budget, on the budget of Public Social Insurance and on the budget of the NHIF. Taking into account the political situation, in order to ensure stability and the ability to finance the institutional systems and the implementation of their state and public functions until the election of a regular government, at the end of 2022 the so-called "extension law" was adopted by the Parliament.

At the beginning of June 2023, with the support of the two leading political formations in the National Assembly, a regular government was formed, which put the focus of its policy on developing the Budget 2023 as quickly as possible, and until its adoption, the parliament extended the deadline, and subsequently adopted an additional extension law until the final adoption of the budget framework for the period 2023-2025, subject to compliance with the country's commitments in the context of joining the Eurozone.

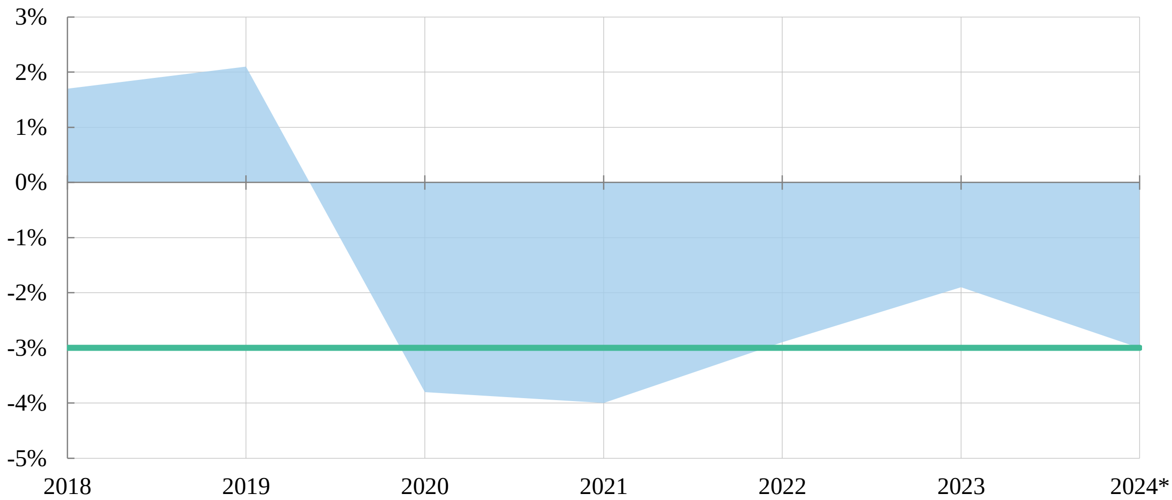
A draft State Budget for 2023 and an Updated Medium-Term Budget Forecast for the period 2023-2025 were developed and approved by the regular government with Government Decision No. 459 of July 5, 2023. With the said decision, the Council of Ministers withdrew the previous draft Law on the State Budget of Republic of Bulgaria for 2023 (Decision No. 331/28.04.2023), submitted for consideration in the National Assembly by the caretaker government.

Budget developments in 2023

Compared to the previous three years, when the fiscal shocks of the COVID-19 pandemic and the outbreak of the war in Ukraine manifested themselves, in 2023 the country's fiscal situation can be defined as balanced. The lack of significant external shocks on the economy can be assessed as a positive factor. This allowed a reorientation of fiscal policies from supporting various entities affected by the series of shocks on households and the economy to the implementation of a more intensive capital programme.

In this situation, Bulgaria achieved a level of the balance of the "General Government" sector in the amount of -1.9% of GDP, which is the lowest deficit for the last four years, and for another year it remained below the reference value for the deficit in the SGP. Compared to the stated goal in the previous Convergence Programme – a deficit of 6.1% (prepared by the caretaker government in the absence of an adopted Budget 2023), the data from the April Notification Tables on the Deficit and Debt of Bulgaria report an improvement in the budget balance by 4.2% which is due to an increase in the revenue part by 1.9 pps while in the expenditure part there is a contraction of expenses by 2.3 pps compared to initial forecasts. Compared with the forecast to the October Notification Tables on the Deficit and Debt of Bulgaria for a deficit for 2023 in the amount of about 3.0% of GDP, an improvement of 1.1 pps is reported, mostly on the expenditure line, as the revenue part also has a contribution, mainly through tax revenues. Realized expenses remained lower than the plan, including due to the late adoption of the 2023 Budget and the correspondingly significantly shortened deadlines for the implementation of policies and programmes.

Graph 3-1: Budget balance (ESA 2010, % of GDP)



* Forecast

Source Eurostat, MF

Revenue as a share of GDP reached 37.9% in 2023, down from 0.5 pps compared to the level in 2022. At the same time, in nominal terms, revenues increased by BGN 5.2 billion. The main reason for the contraction of revenues as a share of GDP is the reported decline as a relative share of GDP in taxes on production and imports, while in nominal terms the volume of these taxes is retained. In most of the other types of income, with the exception of other incomes, where the received capital transfers are also included, an increase in the relative share in GDP is observed. It should be noted that in 2022 a base effect is taken into account from introduced measures to tax the excessively high revenues of electricity producers, which were used to pay compensations for the high prices of electricity to consumers outside the regulated market. In 2023, the effect of these temporary measures is significantly weaker due to the normalization of energy prices on international and regional energy exchanges.

Taxes on production and imports account for 14.8% of GDP in 2023, down from 1.3 pps compared to the previous year, and in nominal terms there is an increase of BGN 0.1 billion. As already indicated, the receipts from targeted contributions from electricity producers in 2023 report a huge decline, which is due to the normalization of electricity prices on the Bulgarian Independent Energy Exchange. With the exception of the first quarter, the average monthly price of electricity in the "day-ahead" segment remained below or very close to the legally regulated compensation payment threshold of BGN 200 per MWh, which is why for most of the year compensations to end-customers of electricity outside the regulated market were not paid. This accordingly led to a drop in the collected revenue from targeted contributions in 2023 compared to the previous year. In parallel, two diverging trends were observed in VAT. In the case of VAT receipts for transactions in the country and intra-community acquisitions, a steady growth is observed, which reflects the growing consumption and economic activity in the country. At the same time, there is a decrease in VAT revenues on imports due to the decline in the volumes and prices of imported goods (mainly raw materials), given the disrupted supply chains as a result of the events in the Red Sea, as well as the effect of restrictive measures against Russia and liberalized trade with Ukraine. This, together with the increasingly liberal trade policy of the EU, as a result of which there are numerous agreements concluded or preferential tariffs granted on an autonomous basis, also led to a decrease in customs revenues. In the case of excise taxes, there is an increase in revenue as a result of the recovery in consumption and the increased rates for tobacco products.

At current taxes on income, wealth, etc. an increase in revenues is observed - by 0.2 pps, which in nominal terms is close to BGN 1.3 billion. A nominal increase is reported for all taxes in the group, with the largest being for the personal income tax (PIT). The main reasons for the increased PIT receipts are the recorded stable salary growth, including the compensation for the inflation of the previous year, both in the public sector and in the private sector, where employers seek to retain and attract quality employees, and in a number of areas to deal with staff shortages. Corporate tax revenues are also rising, with the largest increase in corporate tax on financial institutions. Revenues from taxes on capital retain their level as a percentage of GDP compared to the previous year.

Revenues from social and health insurance contributions increased nominally by nearly BGN 1.9 billion, and related to GDP they reported an increase of 0.3 pps compared to 2022. The main factor contributing to this, as with the PIT, is the sensitive growth of incomes, incl. the minimum wage and the minimum insurance thresholds, etc.

Nominal growth of BGN 1.2 billion and an increase in the share of GDP by 0.6 pps is accounted for in property income. This is largely due to the significant dividend received by state-owned enterprises (including an interim dividend for the financial result for 2023), mainly from the energy sector, as a consequence of the large profits in the previous and current years. Also the contribution of interest income as a result of increased interest rates in the banking sector is significant.

The received capital transfers reduce their share in GDP by 0.8 pps compared to the previous year, which is nominally BGN 1.1 billion. This reflects the funds received under EU programmes and funds.

In 2023, the total expenses of the "General Government" sector will increase nominally by BGN 3.7 billion and amount to 39.8% of GDP, which is 1.5 pps lower than the level reported in 2022. An increase as a share of GDP compared to the level in 2022 is reported for compensation of employees, social payments and gross fixed capital formation, while for intermediate consumption, subsidies and other expenses there is a decrease in the ratio to GDP.

Expenses for compensation of employed persons increased nominally by BGN 2.2 billion, with their level compared to GDP increasing by 0.3 pps compared to 2022. The main reason for this is the increase in remuneration in the public sector, including the implementation of the policy of maintaining the salaries of the staff in the school education sector at the level of 125% of the average salary and increasing the remuneration of those employed in a number of areas of the budget sector, incl. the increase of the minimum wage.

The costs for intermediate consumption, which mainly include the costs of maintenance, decreased nominally - by BGN 0.6 billion, and as a relative share in GDP - by 0.8 pps. This is mainly influenced by units from the "General Government" sector, outside of the budgetary authorities under national legislation, whose balance sheets show an improvement.

The amount of social transfers as a relative share of GDP increased by 1.6 percentage points, and in nominal terms this represented BGN 5.3 billion. In the case of social transfers in kind, where payments to medical care providers are reflected, the nominal increase is by BGN 2.5 billion, and the share of spent funds in GDP increases by 1.1 pps compared to 2022. This reflects the increase in prices of clinical pathways and payments to other providers of medical care. The other category of social transfers, other than those in kind, reflect the social payments made for pensions, benefits and benefits to households, where the nominal increase is BGN 2.8 billion compared to 2022, and their share in GDP increases by 0.5 pps. In 2023, pension costs increased due to: payment of increased pensions from July 1, 2022 and from October 1, 2022, incl. the increase of the minimum and maximum pensions; update by 12% from July 1, 2023 of all pensions, except for the maximum; as well as the additional one-off payments of BGN 70 to the pensions of all pensioners with pensions up to the poverty line in April 2023.

In the expenses for social transfers and benefits for households, an increase in the sums for benefits is reported for the following categories - temporary incapacity due to general illness; unemployment benefits; benefits for pregnancy and childbirth, and raising a small child; benefits for people with disabilities that are linked to the poverty line; social assistance benefits, incl. heating subsidies; family benefits for children.

Expenditures for subsidies marked the largest decrease compared to 2022, both nominally - by nearly BGN 4.2 billion, and as a share of GDP - by 2.7 pps. The main reason is the normalization of the price of electricity on the free market, which also led to a drastic drop in compensation costs.

Capital expenditure is one of the elements of expenditure where the most significant increase is reported in 2023. In terms of gross fixed capital formation, the nominal increase is nearly BGN 2.6 billion, and as a share of GDP – by 1.2 pps, while capital transfers have a minimal drop of BGN 0.1 billion or 0.1 pps of GDP. The high growth of capital expenditure on the accounts for funds from the EU, supported by the growth of investment expenditure on the state budget and the budgets of municipalities, is the reason for the overall increase in the gross fixed capital formation. According to regulations of the European Parliament and the Council of the EU, 31.12.2023 was the deadline in which the beneficiaries of the operational programmes financed by the European Structural and Investment Funds for the programme period 2014-2020 could pay the costs of the projects they implemented. This determines the significant growth of capital expenditure in 2023, which is reported on the accounts for EU funds, and which represents the final stage of payments in connection with the completion of the projects for the programming period 2014-2020. The main direction of the expenditure incurred on infrastructure projects is in the transport, environment and regional development sectors. At the same time, the complicated political situation in the country in 2023 and the change of governments led to a certain delay in the process of starting new projects, including the Recovery and Resilience Plan, and accordingly larger capital expenditures foreseen in the previous Convergence Programme were postponed for the following years.

In 2023, interest expenditures keep their share of GDP unchanged compared to 2022 – 0.4%.

3.3.2 Measures to combat the COVID-19 pandemic in 2023, war in Ukraine and energy crisis

– COVID-19

The summarized data on the amount of expenditure incurred under the national budget by the first-level spending units and municipalities in connection with measures to combat COVID-19 and overcome the socio-economic consequences of the pandemic in 2023 amounts to BGN 160.6 million. (0.1% of GDP).

BGN 126.7 million from the national budget was spent on household support measures. The largest share is reported by the Ministry of Health in the amount of BGN 122.9 million for the purchase of vaccines and medicinal products.

For business support measures, (BGN -0.3 million) was recorded, which is a compensated difference between the non-reimbursed financial assistance paid in 2023 and reimbursed amounts representing illegally received funds.

A total of BGN 34.2 million has been provided from the national budget for measures for the state government bodies charged with activities to control the pandemic and the consequences of COVID-19. The costs of support to frontline staff directly involved in activities to prevent the spread of COVID-19 have the largest share of BGN 25.0 million.

– Costs for humanitarian aid as well as for dealing with the consequences related to the military actions in Ukraine

The expenses reported by the first-level spending units and municipalities in 2023 for financing activities for the provision of immediate humanitarian aid to Bulgarian citizens living in Ukraine and Bulgarians with Ukrainian citizenship, including if evacuation is necessary, for the provision of humanitarian aid to Ukraine, as well and for spending on dealing with the consequences of the military actions against Ukraine amount to BGN 489.5 million at the expense of the national budget and BGN 27.6 million at the expense of EU funds (a total of 0.3% of GDP). The main directions of assistance are as follows:

Under humanitarian aid programmes for persons seeking temporary protection

The costs for humanitarian aid and for dealing with the consequences of the military actions in Ukraine in 2023 under the "Programme for Humanitarian Assistance to Displaced Persons from Ukraine with Temporary Protection in the Republic of Bulgaria" amount to BGN 56.2 million.

Funds disbursed under the State aid "Aid to support the liquidity of farmers to overcome the negative economic impact of the Russian aggression against Ukraine", developed in compliance with the rules of the Temporary Framework for State aid measures in crises to support the economy after the aggression of Russia against Ukraine, amounting to BGN 426.2 million.

Extraordinary temporary assistance for small and medium-sized enterprises affected by the consequences of the Russian invasion of Ukraine. Pursuant to Ordinance No. 2 of 28.02.2023 of the Ministry of Agriculture and Food, for the implementation of Art. 39c of Regulation (EU) No. 1305/2013, BGN 16.8 million were paid on account of the funds from the European Union to the State Fund "Agriculture".

In the field of social protection - within the framework of the current regulations in the field of the social assistance system, persons arriving in the country with the status of temporary protection, for whom, after an assessment of each specific case, it is found that they need support to satisfy the basic vital needs, have the right to social assistance and protection, including people with disabilities. In addition, those arriving from Ukraine have the right to work in our country without a permit to access the labour market, as well as to use simplified procedures for accessing the Bulgarian labour market. In 2023, expenses in the amount of BGN 1.5 million were reported at the expense of the national budget and BGN 10.8 million of funds from the EU.

– Compensation programmes for high electricity and natural gas prices

In 2023, to compensate for the high energy prices under programmes approved by the Council of Ministers(with Council of Ministers Decision (CMD) No. 534 and CMD No. 710 of 2022 and with CMD No. 104 and CMD No. 688 of 2023), more precisely to compensate the costs of non-household final customers for electric energy and the operators of the electric transmission and electric distribution networks for the purchase of the quantities of electric energy needed for technological costs spent BGN 588.8 million (0.3% of GDP).

3.3.3 Budget highlights for 2024

The fiscal framework for 2024 projects the deficit on a cash basis to be 3.0% of GDP, which is within national fiscal rules. At the same time, the deficit of the "General Government" sector this year is forecast to be 3.0% of the forecast GDP[8], which is in line with the requirements of the SGP and will maintain the stability of the country's fiscal position as a necessary condition for the adoption of the country as a full member of the Eurozone.

In 2024, there is a change in the focus of budget policy from measures to deal with crises to those aimed at stimulating economic growth, investment in the public capital programme, improving business conditions and increasing the income of the population. The main spending priorities laid down in the government programme are with an emphasis on social policies, investment programmes and reforms, financed both by the national budget and by EU funds and programmes.

In the next part, the main priorities of the revenue policy and the main expenditure directions laid down in the law on the budget for 2024 are examined.

The revenue policy is oriented towards achieving macroeconomic and budget stability in the medium and long term and providing the necessary financial resources to implement the government's expenditure policies.

– Administrative measures in the area of revenue

- Maintaining low tax rates for corporate tax and personal income tax, as well as the basic rate of VAT, as an important incentive for investment, consumption, economic growth and employment. Maintaining tax incentives for certain sectors and activities.
- The amounts and ratios of insurer/insured of insurance contributions for the state social insurance funds and of the health insurance contribution remain unchanged in 2024 compared to 2023.
- The most significant effect for the budget is also the package of measures to increase revenue collection, incl. measures in the field of fiscal control of goods with a high fiscal risk, which aim at more effective prevention and countermeasures against tax fraud and tax evasion and non-payment - the expected additional revenues from VAT and corporate tax amount to BGN 740.0 million in 2024 (0.37% of estimated GDP).
- The increase in the maximum insurance income from January 1, 2024 to BGN 3,750 has a major budgetary effect. The additional income from health insurance and pension insurance contributions, as a result of the increase in maximum insurance income, amounts to BGN 302.5 million for 2024 (0.15% of projected GDP).
- The overall positive effect on the revenues from VAT and excise taxes as a result of the increase in the excise rate on cigarettes, cigars and cigarillos, smoking tobacco, heated tobacco products, electronic cigarette liquid, introduced from 01.03.2023, and from the inclusion of liquids for electronic cigarettes, not containing nicotine, and tobacco substitutes containing nicotine (from 01.08.2023) and heated products with content other than tobacco (from 01.01.2024) in the scope of excise goods, in accordance with the proposed schedule for increasing the excise duty rates for these products, is estimated at BGN 140.9 million for 2024 (0.07% of estimated GDP).
- The reduced rate of VAT to 9% for natural gas and central heating was in force until the end of June 2023, with the return of the rate to the standard level of 20% for most goods

[8] The estimated GDP is based on the spring macroeconomic forecast 2024 - https://www.minfin.bg/bg/866

and services having a positive effect on revenues in 2024, which is estimated at a total of BGN 189.8 million (0.1% of estimated GDP).

- The abolition of the reduced rate of 9% of VAT for the supply of a general tourist service and of services for the use of sports facilities (from 01.07.2024) and the extension of the period of validity of the reduced rate of 9% of VAT for the supply of restaurant and catering services (until 31.12.2024) have a total budget effect of BGN 5.0 million additional revenues.

- The abolition of the zero VAT rate for the supply of bread and flour after June 30, 2024 is expected to have a positive budgetary effect of BGN 32.4 million for 2024 (0.02% of estimated GDP).

- The introduction of a domestic top-up tax in accordance with Council Directive (EU) 2022/2523 to ensure a global minimum level of taxation for groups of multinational enterprises and large local groups in the Union (in effective from 01.01.2024) is expected to generate additional revenues of BGN 220.0 million for 2024 on an accrued basis (0.11% of estimated GDP).

- The abolition of the measure for exemption from excise duty on electricity, natural gas and liquefied petroleum gas, which was in effect until 31.07.2023, is expected to lead to additional revenues from VAT and excise duties in the amount of BGN 90.1 million in 2024 (0.05% of estimated GDP).

- The effect of the legislative amendments in the field of gambling, related to the taxation of this type of activity, which came into force on 01.01.2024, is additional revenues in the amount of BGN 75.0 million (0.04% of the estimated GDP).

- The additional expected revenues related to the operation of the toll system are in the amount of BGN 23.2 million for 2024 (0.01% of the estimated GDP).

- The increase in the threshold for turnover when applying patent tax from BGN 50 to 100 thousand, as well as the introduction of patent tax for legal entities operating as mass-catering and entertainment establishments, has a net positive effect of BGN 1.0 million. for 2024

- The introduction from 01.01.2024 of legally recognized expenses under the Personal Income Tax Law (PIT Law) - in the amount of 10%, when determining the taxable income from the sale or exchange of financial assets, including and virtual currencies, as well as from trading in foreign currency and the exemption from taxation of income (from waste) under the Personal Income Tax Law - from the sale or exchange of movable property transferred to persons who have the right to collect, transport, recover or dispose of waste in accordance with the Law on Waste Management (as of 01.01.2024) is expected to lead to a decrease in annual PIT revenues by BGN 17.5 million (0.01% of estimated GDP).

- The abolition of the obligation for insurers to pay compensation to insured persons for the third working day of temporary incapacity, starting from 01.01.2024, is forecast to lead to a drop in revenues of BGN 15.0 million in 2024 (0.01% of estimated GDP).

- The termination in 2024 of the measure to make the Temporary Solidarity Contribution under Council Regulation (EU) 2022/1854 of 6 October 2022 on emergency intervention to tackle high energy prices is projected to lead to a reduction in revenues of BGN 375.9 million (0.19% of estimated GDP).

- The change in the parameters of the dividend policy of state-owned enterprises is expected to lead to a decrease in revenues by BGN 482.5 million (0.24% of estimated GDP) in 2024.

The energy measures and programmes to mitigate the economic consequences of the volatility of electricity and natural gas prices that started in 2021 were until the end of 2023. Therefore, no revenue and no incurring costs associated with these programs are expected in 2024. Given the fact that the programmes were designed in such a way that expenditures equalled revenues, the effect on the budget balance would be neutral.

The parameters of the spending policies for 2024 are consistent with the abilities of the budget for financing state activities, the prospects for the development of the public spheres, the acceleration of economic growth, including the implementation of the planned investment projects at the national and municipal level.

— Income policy

With regard to the income policy, from January 1, 2024, an increase was made in the amount of the minimum wage - from BGN 780 to BGN 933, which is in accordance with the provisions of Art. 244 of the Labour Code (introduction of an automatic mechanism for determining the minimum wage - 50 percent of the average salary for the previous 12-month period).

For 2024, an increase in the funds for salaries and remuneration of the personnel for the elected positions and for those employed in the system of judicial power, for which a mechanism for the formation of the remuneration is regulated by law, has been calculated.

Full-year funding is provided for 2024 and subsequent years as a result of personnel cost increases made in 2023 in some spending units.

To overcome disparities in remuneration of staff in budget organizations (to smooth out observed significant imbalances/inequalities in the level of pay for the same positions in different administrative units and structures in the sectors providing public services), including to increase the remuneration of personnel for 2024, without structures for which the remuneration is determined by particular mechanism, additional funds in the total amount of BGN 352.9 million (0.18% of the estimated GDP), incl. BGN 32.0 million for municipal administration - state activities, for which it is planned that the funds will be distributed in accordance with the order and conditions determined by an act of the Council of Ministers. Within the defined general resource for increasing the remuneration of the staff for 2024, funds are also provided for increasing the remuneration of the academic staff, including BGN 39.0 million for state universities, BGN 10.0 million for the Bulgarian Academy of Sciences and BGN 3.0 million for the Agricultural Academy.

An increase in funds for the delegated activities in education is foreseen in connection with the continuation of the policy of increasing the salaries of pedagogical specialists to reach an average salary of not less than 125 percent of the average salary for the country in order to stimulate the entry of young and qualified teachers in the system of preschool and school education. The estimated amount for 2024 is BGN 289.9 million (0.15% of estimated GDP).

The increase of the maximum insurance income for 2024 to BGN 3,750 is associated with additional costs for insurance contributions in the amount of BGN 35.9 million (0.02% of estimated GDP).

— Measures regarding pensions, social benefits and benefits, and social assistance

In the area of pension policy, the costs are influenced by the following measures:

- The legal provisions continue to be in effect, according to which the required retirement age and insurance length of service for those working under the conditions of the three labour categories are increased, as well as the minimum retirement age for persons under Art. 69, Art. 69a and Art. 69b (persons from the "Defence and Security" sector and professionals engaged in dance arts) of the Social Insurance Code (SIC).

- Pensions for employment, granted until December 31, 2023 will be indexed from July 1, 2024 by decision of the Supervisory Board of the National Social Security Institute (NSSI) with a percentage determined according to the rule of Art. 100 from SIC – 50 percent from the increase in insurance income and 50 percent from the consumer price index for the previous calendar year. The specified growth rate in 2024 is 11 percent. From July 1, 2024, the minimum amount of the pension for length of service and age and the related minimum amounts of pensions for labour activity, as well as the amount of the social pension for old age and related pensions and supplements are also increased by 11 percent (the number determined under Article 100 of the SIC).
- In 2024, the maximum amount of one or more pensions received remains at BGN 3,400.
- From July 1, 2024, the amount of the so-called "widow's" supplements under Art. 84 of the SIC is increased from 26.5 to 30 percent of the amount of the deceased spouse's pension.
- In 2024, an increase in the number of newly granted pensions is expected, since the period of conscription or peacetime alternative service, as well as the periods of repression under Art. 7 of the Law on Political and Civil Rehabilitation of Repressed Persons are accepted as length of service. In addition, with changes in the Methodology for determining permanently reduced working capacity, the determined percentages of permanently reduced working capacity/type and degree of disability are expanded, which contributes to the increase in the number of newly granted disability pensions.

The overall effect of the action of the described measures, the year-round payment of pensions increased from July 1, 2023, as well as the natural growth of the newly awarded, compared to the terminated pensions, is expected to lead to an increase in pension costs by 2,482.9 million BGN (1.24% of estimated GDP) compared to those reported in 2023.

The main features of the policy in the field of social benefits and benefits paid by the state social insurance in 2024 continue to be sustainability of support, predictability for the affected persons and steps towards expanding the coverage of social risks. This is expressed in: preservation of the minimum daily amount of the unemployment benefit; preservation of the period of payment of cash compensation for pregnancy and childbirth and the amount of compensation for raising a child up to two years of age; preservation of the period of two months of payment of the monetary benefit for raising a child up to the age of 8 by the father (adoptive); preservation of the period from which short-term benefits are calculated in case of temporary incapacity for work, pregnancy and childbirth and unemployment; preservation of the amount of the one-time benefit upon the death of an insured person and preservation of the provision of art. 22, para. 2 of the Law on Guaranteed Receivables of Workers and Employees in the Event of the Employer's Bankruptcy, regarding the maximum monthly amount of the guaranteed receivable, which cannot be less than 2.5 minimum wages. The maximum daily amount of unemployment benefit is increased from BGN 85.71 to BGN 107.14. The payment regime for cash compensation for temporary incapacity is changed from January 1, 2024, according to Art. 40, para. 5 of SIC - the first two working days are paid by the insurer, and from the 3rd day of the onset of incapacity - by the Public Social Insurance. As a result of the described policy, the expenses for benefits and benefits under the budget of Public Social Security Budget in 2024 will increase by BGN 79.7 million (0.04% of the estimated GDP).

– Social policy

Social policy covers a number of aspects related to the standard of living and the labour market in the country. It is realized in several main directions.

- The active policy of the labour market is aimed at ensuring more and more qualified labour force and integrating the unemployed and inactive persons of working age into the labour market.

- Social assistance policy is aimed at ensuring the satisfaction of the basic vital needs of people in critical situations, applying clear, accurate and objectively justified mechanisms. With the legislative change that entered into force in June 2023, it went from tying social benefits to the guaranteed minimum income to tying them to the poverty line determined by the Eurostat methodology. This introduces a mechanism for regularly updating access to assistance and updating the amount of assistance.
- The policy for the rights of people with disabilities has a main focus on creating conditions and opportunities for social inclusion and providing vulnerable groups of people with disabilities with targeted, supportive and encouraging measures.
- An essential part of the social inclusion policy is the provision of material support for families with children and families caring for children at risk. In 2024, the income criterion for determining the right to access monthly family allowances for raising a child until the completion of secondary education, but no more than 20 years of age, is increased, according to the Family Allowances for Children Law, as follows: for receiving the full amount of assistance from BGN 510 to BGN 710, respectively, and for receiving 80 percent of the full amount of assistance, the change in the income range is from BGN 510.01 to BGN 610 to BGN 710.01 up to BGN 810. The income criterion for determining the right to access the remaining two family allowances for children, which are provided with an income test - the one-off allowance for pregnancy and the monthly allowance for raising a child up to the age of one year, respectively, is increased from BGN 610 to BGN 810. In 2024, the amounts of some family allowances for children under Family Allowances for Children Law are also changing: the amount of the one-time birth allowance is increasing from BGN 250 to BGN 375 for the first child, from BGN 600 to BGN 900 for the second child, from BGN 300 to BGN 450 for the third child and from BGN 200 to BGN 300 for the fourth and each subsequent child, and this increase also affects the one-time adoption allowance; the one-time pregnancy allowance is increased from BGN 150 to BGN 225; the monthly benefits for raising a child with a permanent disability are increased, differentiated according to the degree of disability.
- Policies in the area of living standards, demographic development and social investments are aimed at creating modern measures that are harmonized with the applied policies of the European Union to reduce working poverty, achieve social cohesion and create equal opportunities for full-fledged social and productive life for all social groups of the population.

The planned funds for the implementation of the measures in the various directions of the social policy amount to BGN 426.1 million (0.21% of the estimated GDP) and are as follows:

- BGN 104.3 million for social payments in connection with the determined new amount of BGN 526 on the poverty line for 2024, including the costs of benefits under the Social Assistance Law – BGN 75.6 million, additional costs when determining the financial support under the Law for Persons with Disabilities – BGN 27.6 million and BGN 1.1 million for the benefits under the Child Protection Law;
- BGN 230.3 million in connection with the effect of a change in the minimum wage from BGN 780 to BGN 933, incl. BGN 224.6 million for determining the remuneration of personal assistants under the Personal Assistance Law and BGN 5.7 million for remuneration for professional foster families under the Child Protection Law;
- BGN 23.4 million in connection with the year-round provision of the one-off aid introduced in 2023 for students of the second, third and fourth grades without an income test, regardless of the type of school under the Family Allowances for Children Law;
- BGN 40.6 million for an increase in the amount of monthly allowances for raising a child with a permanent disability according to the Family Allowances for Children Law;

- BGN 12.5 million for an increase in the amounts of one-off benefits for pregnancy and childbirth under the Family Allowances for Children Law;
- BGN 15.0 million additional funds for active labour market policies.

Additional costs of BGN 258.4 million (0.13% of the estimated GDP) are planned for the activities in the field of social services, financed through the municipal budgets.

– Healthcare policy

The main financed directions of the health policy are: protection of citizens' health as a state of physical, mental and social well-being; ensuring financial stability and security of the health system through a long-term, sustainable and predictable funding mechanism based on health outcomes; increasing the quality and accessibility of health services with an emphasis on the prevention and treatment of socially significant diseases; ensuring health protection for children, pregnant women and persons with physical disabilities and mental disorders; development of emergency aid and emergency response capacity; better planning and motivating the health care workforce; development of electronic healthcare and digitization of the healthcare system.

The total amount of estimated healthcare costs for 2024 is BGN 10,024.2 million, which represents 5.02% of GDP. Within this amount, an additional BGN 1,110.6 million is provided for health insurance payments under the NHIF budget. It is planned to implement a number of activities related to prevention and early detection of diseases, as well as activities related to monitoring the treatment of patients and determining cost effectiveness.

Additional funds are provided for a number of specific directions in the field of health care: to provide an annual amount of the increased remuneration of the personnel in the centers for emergency medical assistance and regional health inspections; for organizational and financial support of Bulgarian citizens for carrying out assisted reproduction activities for persons with infertility; for additional subsidies for medical facilities for hospital assistance for the implementation of state policy in emergency situations, accidents and catastrophes; to provide medicinal products intended for the treatment of infectious diseases; to provide vaccines for mandatory immunizations and reimmunizations; to support training to acquire a specialty in the healthcare system; for organizing and conducting screening of diseases related to children's health and women's reproductive health; for aids, devices, equipment and medical devices for people with disabilities, etc. In total, the additional funds provided for these activities amount to BGN 203.1 million (0.10% of the estimated GDP). In addition, an additional BGN 21.5 million (0.01% of estimated GDP) has been earmarked for health care activities at the municipal level.

– Policies in the field of education

Policies in education are focused on improving the educational process, the personal development of students, promoting innovation, qualification of pedagogical specialists, modernizing educational institutions and increasing the quality of higher education. The total amount of estimated expenses for education for 2024 is BGN 8,396.1 million, which represents 4.2% of GDP.

Policies in <u>preschool and school education</u> are aimed at effective socialization of children from early childhood, ensuring equal access to quality education, personal development of children and students, promotion of innovation, qualification of pedagogical specialists, modernization of educational institutions, digitalization of education.

In 2024, additional funding is planned in the field of preschool and school education, with the overall effect of the planned measures being an increase in costs by BGN 590.8 million (0.30% of estimated GDP).

<u>Policy in the field of higher education</u>

To ensure sustainable development policies and expand access to higher education for 2024, additional funds have been provided, distributed as follows: for the state to cover the tuition fees of students and doctoral students, a state order from the second semester of the academic year 2023/2024 year – BGN 136.0 million; to ensure the increase in the remuneration of the academic staff from 2023 in a full-year amount - BGN 39.0 million; to ensure the updated amount of student scholarships from July 1, 2023 – BGN 6.0 million; for an increase in the amount of funds for food and accommodation in student halls and dormitories at state higher education institutions - BGN 4.5 million; for renovation, repair and furnishing of student dormitories - BGN 50.0 million; for financing the construction of a computing center for artificial intelligence by the Institute for Scientific Research in the Field of Computer Sciences at Sofia University "St. Kliment Ohridski" (INSAIT) - BGN 100.0 million.

— Policies in the field of science

Increasing the amount and efficiency of public research and development (R&D) spending is aimed at increasing the quality, exploitation and commercialization of research results; raising the level of scientific research institutions and modernization of equipment for carrying out R&D; the development of regional and local technology testing laboratories, promoting entrepreneurship in research organizations, maintaining successful clusters, addressing gaps in research infrastructure and optimal use of shared infrastructure capacity; capacity building and development of human resources in the R&D system; stimulating cooperation between universities, scientific institutes and businesses with the aim of effectively orienting scientific developments to the needs of the market and society. BGN 721.4 million (0.36% of estimated GDP) has been allocated for science in the 2024 budget.

— Defence policy

Defence policy is concerned with maintaining modern, combat-capable and interoperable armed forces. The Republic of Bulgaria will continue its participation in the decision-making process, as well as in the process of building defence capabilities of NATO and the EU. Defence expenditure for 2024 amounts to 2.05% of GDP (0.05% more than the reference rate), which fulfils the National Plan to increase defence expenditure to 2% of GDP of the Republic of Bulgaria by 2024 and the commitments made to NATO. Funds are provided for maintaining and developing national defence capabilities and capabilities related to collective defence, including funds for the implementation of the investment projects approved by the National Assembly for the modernization of the Bulgarian Army, as follows:

- BGN 174.0 million for costs associated with the acquisition of the new type of combat aircraft - Stage I (transportation, VAT, customs duties and other costs related to the implementation of international contracts);
- BGN 82.3 million for the acquisition of a new type of combat aircraft - II stage, including for accompanying costs (transportation, VAT and customs duties);
- BGN 161.0 million for the acquisition of a multifunctional modular patrol ship for the Navy;
- BGN 546.0 million for the acquisition of basic combat equipment for the construction of battalion combat groups from the composition of a mechanized brigade.

In addition, funds are provided for the acquisition of ammunition and fuels for combat training, for the acquisition, modernization, maintenance and repair of armaments, missiles, torpedoes and equipment, and for the repair and construction of infrastructure, as well as for the implementation of other policies.

— Energy measures

The policy in the field of energy is aimed at sustainable energy development of the country, efficient use of energy and energy resources, meeting society's needs for electricity and thermal energy, natural gas and fuels, establishing cleaner and more efficient energy production through rational use of conventional and renewable energy sources, minimizing the impact of production, transmission and use of energy on the environment, improving the management of natural resources. Energy efficiency is a key goal and is particularly important to achieving our long-term energy strategy and climate goals. Development of electric mobility and energy storage systems is ahead.

Programmes to mitigate the economic impact of electricity and natural gas price volatility began in 2021 and peaked in spending in 2022, with spending declining in 2023. At the moment, the effect of these programmes is until the end of 2023, which is why their effect on costs is negative in 2024. As indicated in the review of revenues, the amount of reduction in revenues and expenses is identical - 982.8 million BGN, which is why the impact on the budget balance is neutral.

— Investment policy

In 2024, the government foresees the implementation of the capital budget under national programmes, under programmes and mechanisms of the European Union and under other international programmes and agreements. For this purpose, the capital expenditures under the separate budgets of the first-level spending units under the state budget are shown in a separate resource in the central budget. The goal is to achieve better planning and spending of capital expenditures, as well as higher efficiency and transparency in the implementation of investment programmes. In this regard, it is envisaged that during the implementation of the budget for 2024, the funds for capital expenditures of the ministries and departments will be provided by acts of the Council of Ministers in accordance with Art. 109, para. 3 of the Public Finance Law (PFL). The proposed approach will enable timely allocation of funds from the central budget for expenditures on projects and programmes of the ministries and departments for which there is readiness for their immediate implementation. In this way, the long-standing practice of capital expenditures at the end of the year being redirected to other types of expenditures or remaining unrealized in the budgets of ministries and departments, which does not achieve the annually set goals for the level of investments in the public sector, will be overcome.

Within the framework of the capital budget, the implementation of an investment programme for the municipalities is foreseen, through which priority infrastructure projects of the local communities will be realized, which will contribute to the improvement of the infrastructural development of the regions. In the provisions of the 2024 National Development Plan, it is possible for the National Assembly to prioritize and change the objects in need of funding, taking into account the interests of the local community and the public significance of the objects at the proposal of the Council of Ministers, based on the proposal of mayors of municipalities.

The maximum amount of planned capital expenditure at the consolidated level for 2024 is BGN 9,994.0 million (5.0% of forecast GDP).

— Policies in the field of culture, youth and sport

In order to increase interest in Bulgarian culture and actively support the creation and distribution of art and cultural products, and for the implementation of the goals and activities in connection with the realization of the priorities of the implemented policies in the field of youth and sports, additional funds have been provided in the amount of BGN 155.9 million for activities in the field of culture and BGN 14.0 million for sports activities and events.

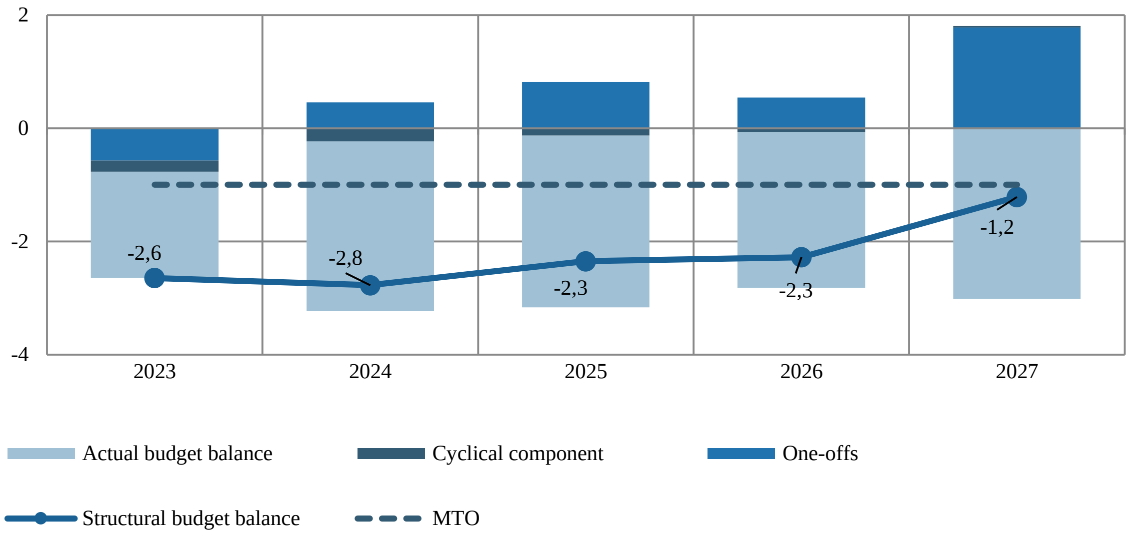
3.4 Structural balance (cyclical components of the balance, one-off and temporary measures) and fiscal position, including the expenditure benchmark

The structural budget balance in 2024 is estimated at a deficit of 2.8% of GDP. During the forecast period, one-off expenditures on military equipment is expected. In 2024, their consideration leads to a positive change (0.5 pps) of the structural vs. planned General Government budget deficit. On the other hand, the positive output gap and the sensitivity of the budget position to the economic cycle suggest a negative correction (0.2 pps).

In 2025, it is planned to maintain the actual deficit of General Government sector at 3% of GDP. Spending on one-off measures will continue to be reflected in a lower structural budget deficit, while the adjustment to the phase of the economic cycle will be small and in the opposite direction. As a result, the structural budget deficit is estimated at 2.3% of GDP in 2025.

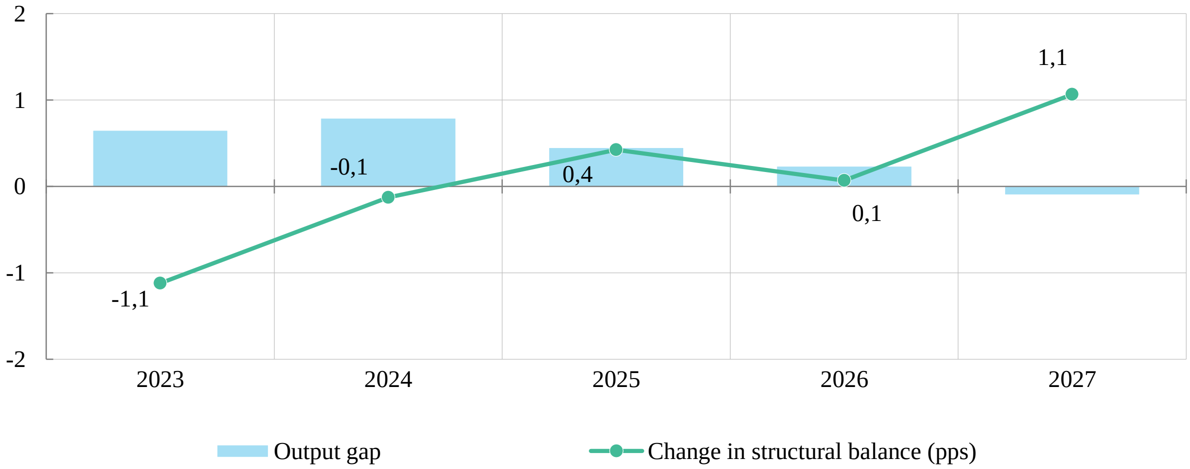
In the last two years of the forecast period, the actual General Government deficit is expected to amount to 2.8 and 3% of GDP, respectively. The deviation from potential growth will be minimal (changing from slightly positive in 2026 to slightly negative in 2027), thus not leading to an adjustment to the headline balance. Reflecting one-off spending, the structural budget deficit is estimated at 2.3 and 1.2% of GDP in 2026 and 2027, respectively.

Graph 3-2: Structural budget balance (% of GDP)



Source: MF, IAF

Graph 3-3: Fiscal position



Source: MF, IAF

The medium-term budget target for the structural balance of the General Government is a deficit of 1% of GDP. This purpose is in accordance with the requirements of Art. 23, para. 2 of the PFL, taking into account the relatively low amount of the consolidated debt of the "General Government" sector, as well as the low risks to the long-term sustainability of public finances. According to Art. 24 of the PFL, the non-fulfilment of the medium-term budget target for the structural deficit on an annual basis is allowed in exceptional circumstances. Due to the crisis caused by COVID-19, the General escape clause of the SGP was activated in 2020, which allowed Member States to deviate from the step towards the medium-term budgetary objective in 2020 and 2021. Subsequently, an EC decision extended the application of the derogation clause in the EU for 2022 and 2023, but the general derogation clause will not apply for 2024.

The assessment of compliance with the requirements of the SGP and the PFL with regard to the growth of budget expenditures is based on the common methodology of the European Commission for the so-called expenditure benchmark, taking into account the division between public investments financed with national funds and with EU funds. The expenditure benchmark is compared to the level of potential medium-term GDP growth as calculated by the EC.

Based on calculations made by the Ministry of Finance, the change in real terms of the expenditure indicator used for the purposes of fiscal management in the EU is estimated at -3.7% for 2023, 3.1% for 2024, 1.6% for 2025, respectively 4% for 2026 and -2% for 2027. According to EC calculations, the reference growth level is estimated at an average of 2.2% for the period 2023-2027.

3.5 Debt levels and developments, below-the-line operations

Based on the data from the April Notification tables on the deficit/surplus and debt, at the end of 2023 the nominal amount of the "General Government" sector debt amounted to BGN 42.4 billion, marking an increase of about BGN 4.5 billion compared to the level of the end of 2022 (BGN 37.9 billion as of 12/31/2022). As a share of GDP sector's debt increased slightly by 0.5 p.p. compared to the previous year to a level of 23.1% (at 22.6% at the end of 2022).

The main factor for the increase in the debt is the growth of the "Central management" subsector debt by about BGN 4.3 billion. During the year, government securities of the International capital markets were issued and were disbursed funds for loans of the units classified in the sub-sector in the amount of BGN 7.5 billion. The repayments have been made for a total amount of BGN 3.4 billion, of which BGN 2.2 billion maturity of Eurobonds issued to the International capital markets in 2016, BGN 0.4 billion payments on government securities, issued on the domestic debt market and BGN 0.8 billion in loans.

Eurobonds with a nominal value of BGN 7.4 billion were issued in 2023 as part of the Global Medium-Term Note Issuance Programme on the International Capital Markets (GMTN programme). On January 17, 2023, 10-year Eurobonds were issued in the nominal amount of EUR 1.5 billion (BGN 2.9 billion), annual interest coupon of 4.5% and a yield of 4.78%, and on November 6, 2023 – a dual tranche of Eurobonds with total aggregate amount of EUR 2.3 billion (BGN 4.5 billion). The transaction includes a 7.5-years tranche of EUR 1.3 billion, annual interest coupon of 4.375% and a yield of 4.673%, and 12.5-years tranche of EUR 1.0 billion, annual interest coupon 4.875% and a yield of 5.13%.

In the currency and interest rate structure of the "General Government" sector debt at the end of 2023, the tendency for increasing of relative share of debt instruments denominated in euros - 73.1% and in BGN - 26.8%, is maintained as well as and dominant position of debt with fixed interest rates – 98.7%. The share of debt denominated in other currencies is 0.1% at the end of 2023, and that with floating rates – 1.3% as of 31/12/2023. This structure of the debt portfolio is expected to be maintained throughout whole the period 2024–2027, as the corresponding ratios of the debt in BGN and in Euro, and of the one with floating interest rates as of 31.12.2027 are projected to be almost 100% (0.02% debt in other currencies) and 1.3%.

Interest payments on an accrual basis to the projected GDP for 2023 are expected to be around 0.4%, and compared to the previous years in the period 2024-2027 higher levels are projected of 0.7% in 2024 to 1.2% at the end of 2027. The expected increase in debt service costs in the medium term is determined by the projected debt growth and regulatory interest rates dynamics.

As of December 31, 2023, the average residual maturity of the "General Government" sector debt marked a level of 7 years and 8 months, and at the end of 2027 it is expected to gradually extend to 8 years and 5 months.

For the current 2024, the expectations for an upward trend in the "General Government" sector debt level are maintained. In nominal terms, its size is expected to increase BGN 49.9 billion, and the debt-to-GDP ratio - at the level of 25.0%.

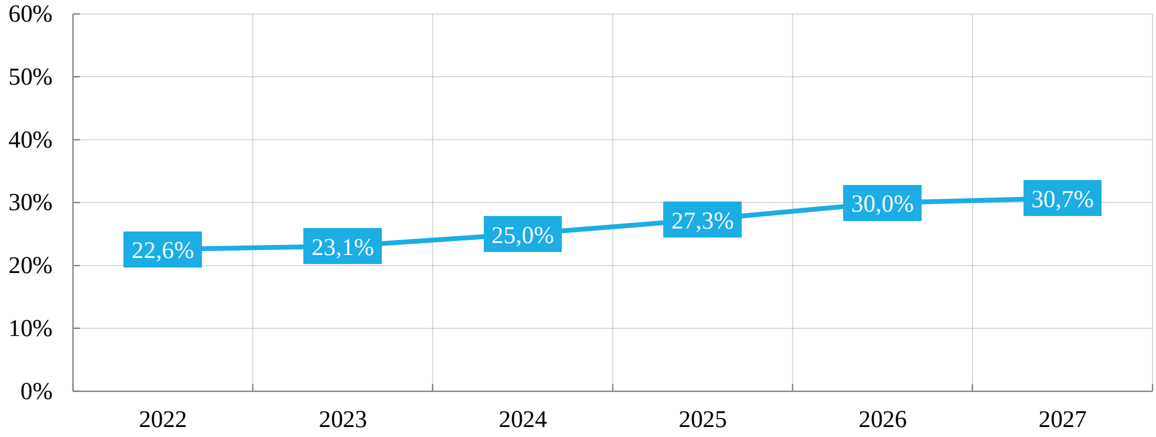
In 2024, a new government debt in the maximum amount of BGN 11.7 billion is planned, which provides an opportunity both for issuing government securities on the domestic debt market and on the international capital markets, as well as for concluding structural programme loans of up to EUR 500 million with the EIB (European Investment Bank) and CEB (Council of Europe Development Bank) for co-financing of projects implemented with resources from the European funds during the programme period 2021-2027.

By the end of April 2024, debt financing in the amount of BGN 200 million was realised, and a new issue of 3-year government securities, denominated in BGN, on the domestic debt market were placed, with a maturity date of April 17, 2027 and an annual interest coupon of 3%. At the auction held on 04/15/2024, a weighted average annual yield of 3.01% was achieved. With this, the Ministry of Finance resumed its issuance activity after more than a year's absence from the domestic government securities market. The auction is in implementation of the 2024 issuance policy and according to the issuance calendar for government securities for April 2024 published in March.

During the period 2025–2027, new debt financing is planned in the amount of BGN 11.6 billion, BGN 11.7 billion and BGN 9.0 billion per year respectively, as the upcoming debt repayments, which should be refinanced amounts to BGN 3.6 billion for 2025 (including BGN 3.3 billion for government securities issued on the domestic market), to BGN 2.8 billion for 2026 (including BGN 2.5 billion for government securities issued on the domestic market) and BGN 3.6 billion for 2027 (including BGN 1.9 billion for government securities issued on the foreign market market). The remaining part of the planned debt financing is justified by the need to finance the planned state budget deficits and ensure liquidity buffers.

Under these assumptions and the outlined need to secure larger volumes of new debt financing, an increase in the General Government sector debt level is projected over the next three years, both in nominal level and as a ratio of GDP. Projections show an increase in absolute amount to BGN 57.7 billion at the end of 2025, BGN 66.8 billion at the end of 2026 and BGN 72.0 billion at the end of 2027 or average annual growth for the forecast period of about BGN 7.4 billion. The General Government debt-to-GDP ratio is projected to reach 27.3% in 2025, 30.0% in 2026 and 30.7% in 2027, with an average annual growth rate for the period 2025–2027 of 1.9 pps.

Graph 3-4: General Government consolidated gross debt/GDP ratio



Source: MF

The "Central Government" sub-sector debt continue to have a leading influence on forecasts for the growth of the consolidated "General Government" sector debt, and in particular the government debt as its main component. The debt contribution of the other two sub-sectors forming the "General Government" sector debt: the "Local Government" sub-sector and the "Social Security Funds" sub-sector is minimal. This trend is maintained throughout the whole period. An additional impact could be a possible expansion of the scope of the sector upon reclassification of institutional units in compliance with the requirements of Eurostat and the implementation of the ESA 2010.

In the period 2024–2027, preliminary estimates show that the "Local Government" sub-sector debt will not expect significant changes compared to the level of about BGN 1.7 billion reported at the end of 2023. A slight increase is projected in 2024 of the sub-sector debt to about BGN 1.9 billion, gradually decreasing in the following years to about BGN 1.7 billion at the end of 2027. Flexible financing schemes for municipalities in the new programme period will keep its share of GDP within about 1.0% – 0.7%. The restrictions laid down in the Public Finances Law and the Municipal Debt Law stipulate that the annual amount of municipal debt payments for each municipality in each individual year cannot exceed 15 percent of the average annual amount of own revenues and the total equalization subsidy for the last three years, calculated on the basis of data from the annual reports on the implementation of the municipality's budget.

The "Social Security Funds" sub-sector has no debt obligations and is not expected to take on new ones in the coming years. The accumulated financial assets in the form of government securities issued by the "Central Government" sub-sector participate in the netting (consolidation) of the sector's debt. By the end of 2023, these assets amount to about BGN 338.2 million.

3.6 Budgetary implications of major structural reforms

3.6.1 Effects on the expenditure side of the budget

— Pension policy

The pension policy in the coming years aims to ensure the stability of income in the social insurance system, as well as to achieve a greater adequacy of pensions in view of the demographic challenges facing the country.

When developing the forecast for pension costs for the period 2024 - 2027, the provisions of part one of the Social Insurance Code and the 2023 Public Social Insurance Budget Law taken into account, as well as the assumptions laid down in the spring macroeconomic forecast of the Ministry of Finance from March 15, 2024, including:

- Art. 68, para. 1-2 of SIC - from January 1 of each calendar year, the age for acquiring the right to a pension continues to increase for those working under the conditions of the third labour category, increasing by 2 months for women and by 1 month for men. The required length of service to qualify for a pension for both sexes continues to increase by 2 months until reaching 37 years for women and 40 years for men in 2027.

The necessary conditions for retirement in the period 2024 - 2027 are indicated in the table below:

Table 3-1: Conditions for retirement under Art. 68, para. 1-2 of the SIC, 2024 – 2027

Year	WOMEN		MEN	
	Age	Length of service	Age	Length of service
2024	62 y and 2 months	36 y and 6 months	64 y and 7 months	39 y and 6 months
2025	62 y and 4 months	36 y and 8 months	64 y and 8 months	39 y and 8 months
2026	62 y and 6 months	36 y and 10 months	64 y and 9 months	39 y and 10 months
2027	62 y and 8 months	37 years	64 y and 10 months	40 years

Source: National Social Security Institute: MF

- Art. 68, para. 3 of SIC - the required retirement age for part-time service is 67 years (reached in 2023), with 15 years of actual length of service;
- Art. 69, para. 1, 2, 3, 5, 5a and 6 of SIC - the minimum retirement age for those working in the "Security" sector continues to increase by 2 months each until reaching 54 years and 8 months in 2027.
- Art. 69b – the minimum retirement age for persons who worked under the conditions of the first and second labour category, who do not meet the conditions for retirement from an occupational pension fund under Art. 168 of SIC or have changed their insurance under Art. 4c of SIC, continues to increase by 4 months for women and by 2 months for men until reaching in 2027 51 years and 8 months for women and 54 years and 8 months for men of the first category and 56 years and 8 months for women and 59 years and 8 months for men of the second labour category.
- From July 1, 2024, the amount of "widow's" supplements under Art. 84 of the SIC are increased from 26.5 to 30 percent of the amount of the deceased spouse's pension.
- In the period 2024 - 2027, it is planned that pensions for labour activity, granted until December 31 of the previous year, will be indexed from July 1 of the respective year according to Art. 100 of the SIC (so-called "Swiss rule") with a percentage equal to the sum of 50 percent of the increase in the insurance income and 50 percent of the Consumer Price Index for the previous calendar year. The amounts of the minimum pension for length of service and age and the social pension for old age, as well as the related pensions and supplements will be updated by the same percentages from July 1 of the respective year.

The expected effect on pension costs is as follows:

- For 2024 - pensions for labour activity granted until December 31, 2023, as well as pensions not related to labour activity, are scheduled to be indexed from July 1, 2024 by 11.0 percent (percentage determined by Article 100 of SIC), with the necessary funds amounting to BGN 1,100.7 million;
- For 2025 - pensions for labour activity granted until December 31, 2024, as well as pensions not related to labour activity, are scheduled to be indexed from July 1, 2025 by 6.6 percent (percentage determined by Art. 100 of SIC);

- For 2026 - pensions for labour activity granted until December 31, 2025, as well as pensions not related to labour activity, are scheduled to be indexed from July 1, 2026 by 4.6 percent (percentage determined by Art. 100 of SIC);
- For 2027 - pensions for labour activity granted until December 31, 2026, as well as pensions not related to labour activity, are scheduled to be indexed from July 1, 2023 by 3.8 percent (percentage determined by Art. 100 of SIC).
- The maximum amount of one or more pensions received for the period 2024 - 2027 remains at BGN 3,400 (effective from October 1, 2022), applying to all pensions, regardless of the start date of the pension;
- In the period 2024–2027, it is planned that the amounts of the minimum pension for length of service and age and the social pension for old age, as well as the related pensions and supplements, will increase by the percentages under Art. 100 per SIC as of July 1;
- Within the reference medium-term programme, cash expenditures for pensions and supplements remain at levels between 10.8% and 11.3% of GDP.

As a result of the above-mentioned assumptions for 2024, the expenses for pensions under the 2024 Public Social Insurance Budget Law increase by BGN 2,482.9 million compared to the report for 2023.

Table 3-2: Estimated expenditure on pensions and allowances, 2024–2027

Year	Pension expenditure	
	BGN mln.	% of GDP
2024 (draft PSI Budget Law)	21 604.0	10.8
2025	23 792.7	11.2
2026	25 226.3	11.3
2027	26 357.2	11.2

Source: National Social Security Institute

3.6.2 Effects on the revenue side of the budget

Estimates of the amount of tax revenues for the period 2024-2027 are made on the basis of the forecasts of the Ministry of Finance for the main macroeconomic indicators and the impact of the measures applied by the revenue agencies to improve the collection and compliance with the legislation.

— Corporate taxes

The reported financial results (taxable profit/loss) and the amount of advance payments made by persons liable to tax under the Corporate Income Tax Law (CIT) who generated a taxable profit for the previous year have the main influence on the income from corporate tax during the period.

The forecast for corporate tax revenue in 2024-2027 is based on keeping the basic tax rate at 10%. The forecast for the period 2024-2027 also takes into account the impact of the introduction of a domestic top-up tax for companies from multinational groups of enterprises in connection with Council Directive (EU) 2022/2523 of 14 December 2022 to guarantee a global minimum level of taxation of multinational enterprise groups and large national groups in the Union, as well as the effect of implementing the new tax relief scheme representing regional development aid, for which a positive decision was received in 2023 of the European Commission regarding compliance with the Regional State Aid Guidelines (2021/C 153/01), as well as the effect of the adopted new state aid scheme in the form of a tax relief, representing state aid for farmers engaged in primary agricultural production under the order of LCIT (art. 189b of LCIT and art. 48, paragraph 6 of PITL).

When forecasting corporate tax revenues, a positive effect of the proposed package of measures to increase revenue collection is included, including in the field of fiscal control of goods with a high fiscal risk, which aim at more effective prevention and countermeasures against tax fraud and tax evasion and non-payment.

— Personal income taxes

The forecast for the period 2024-2027 has been prepared while maintaining the single tax rate of 10% (without a tax-free minimum) for all income of taxpayers, with the exception of the income from business activities of persons carrying out business activities as traders within the meaning of the Commercial Law (including sole traders) and to natural persons registered as farmers, who chose to have the income from their economic activity taxed on such an annual tax base. In the amount of income from personal income taxation, the receipts in the local budgets from patent tax and tax on taxi transportation of passengers are also included.

The development of the parameters of the labour market and the legislative and administrative measures taken in the field of labour, social and tax legislation have a major influence on the amount of tax revenues from the PITL.

The impact on revenue growth during the forecast period of the increased amount of tax benefits for children under Art. 22c and Art. 22 of the Personal Income Tax Law, as well as the available information regarding the effects of the adopted legal changes and the effects of the permanent measures of the National Revenue Agency to comply with tax legislation and improve revenue collection is included.

— Value Added Tax

When forecasting VAT revenues for the period 2024-2027, assumptions regarding changes in economic activity in the country, the dynamics of consumption, imports, exports, available information on the physical volumes of goods from which VAT is generated, the impact of adopted legislative amendments and the impact of factors determined by changes in the external environment are taken into account. Both the forecasts for macroeconomic indicators and the effects of changes in legislation are included.

The forecast was made assuming the temporary anti-crisis measures to reduce the VAT rate in the terms adopted as of 01.01.2023, including the positive effect of the proposed package of measures to increase revenue collection, incl. in the field of fiscal control of goods with a high fiscal risk, which aim at more effective prevention and countermeasures against tax fraud and tax evasion and non-payment.

— Excise duties

In the preparation of the forecasts for revenues from excise taxes, in addition to the dynamics of macroeconomic indicators, the positive effect of measures to improve control over trade in excise goods was also taken into account, taking into consideration the legislative changes made. An assumption has been made to maintain the relative stability of the consumption structure of excise products within the various groups of excise goods throughout the entire period.

The effects of an increase in excise rates for all tobacco products with the introduction of an excise calendar for a period of four years ahead, starting from March 1, 2023, with the aim of a balanced increase in the minimum excise tax on cigarettes and other categories of tobacco products, are reported. The nicotine-free e-cigarette liquids and nicotine-containing tobacco substitutes are included in the scope of excise goods along with a timetable for increasing the excise duty rates on these products.

The withdrawal of the temporary measure of exemption from excise duty on electricity, liquefied petroleum gas and natural gas used as motor fuel, pursuant to Article 15 of Council Directive 2003/96/EC of 27 October 2003 on the restructuring of the legal framework of the Community on the taxation of energy products and electricity has been taken into account. The exemption applied during the period from July 9, 2022 to July 31, 2023. In view of this, the forecast is made on the basis of the presumption of maintaining the excise rates of alcoholic beverages, beer and fuels.

For 2024, the amount under the state aid scheme "Aid in the form of a discount on the value of the excise duty on gas oil used in primary agricultural production" is unchanged at BGN 100 million.

Table 3-5: Estimated budgetary effects of discretionary revenue measures on an accrued basis for the period 2024–2027, incremental change compared to the previous year in BGN million

	2024	2025	2026
Income from social security contributions from the change in the income policy (incl. increase in social security, minimum insurance thresholds and minimum insurance income of self-insured persons and minimum insurance income of farmers and tobacco producers, increase in maximum insurance income, increase in salaries of pedagogics staff)	302.5	278.7	192.9
A package of measures to increase the collection of VAT and corporate tax revenues	740.0		

	2024	2025	2026
Effect on revenues from VAT and excise taxes as a result of an increase in the excise rate on cigars and cigarillos, on smoking tobacco, on heated tobacco products, on e-cigarette liquid (from 1.03.2023)	140.1	168.5	162.0
Effect on VAT and excise revenues as a result of the inclusion of nicotine-free e-cigarette liquids and nicotine-containing tobacco substitutes in the scope of excise goods, together with the proposed schedule for increasing excise rates for these products (from 01.08.2023 d.)	0.8	0.4	0.4
Extending the period of validity of the reduced rate of 9% VAT for the supply of tourist services and for the use of sports facilities (until 30.06.2024) and for the supply of restaurant and catering services (until 31.12.2024)	5.0	304.0	
Reduced rate of 9% VAT for natural gas (until 30.06.2023)	175.0		
Reduced rate of 9% VAT for central heating (until 30.06.2023)	14.8		
Reduced rate of 0% VAT for bread and flour (until 30.06.2024)	32.4	32.4	
Excise duty effect of exemption from excise duty on electricity, natural gas and liquefied petroleum gas (LPG), incl. from the change of the period of application (until 31.07.2023)	75.1		
VAT effect of exemption from excise duty on electricity, natural gas and liquefied petroleum gas (LPG), incl. from the change of the period of application (until 31.07.2023)	15.0		
Introduction of a domestic top-up tax in accordance with Council Directive (EU) 2022/2523 on ensuring a global minimum level of taxation for groups of multinational enterprises and large local groups in the Union (in force from 01.01.2024)	220.0		
Legislative amendments in the field of gambling related to the taxation of this type of activity (from 01.01.2024)	75.0		
Revenues from the operation of the toll system	23.2	43.0	
Increased threshold of the turnover condition when applying patent tax and extending the scope of the patent tax to mass-catering and entertainment establishments	1.0		
Introduction of legally recognized expenses under PITL - deduction of 10 percent of legally recognized expenses when determining the taxable income from the sale or exchange of financial assets, incl. virtual currencies, as well as from foreign currency trading (from 01.01.2024)	-8.0		
Exemption from taxation of income (from waste) under the Personal Income Tax Law - from the sale or exchange of movable property transferred to persons who have the right to collect, transport, recover or dispose of waste in accordance with the Law on Waste Management (from 01.01. 2024)	-9.5		
Waiver of the obligation for insurers to pay compensation to insured persons for the third working day of temporary incapacity (from 01.01.2024)	-15.0		
Proposed increase in the threshold of turnover for registration under the VAT Law from BGN 100 to BGN 166 thousand		-215.0	
Temporary solidarity contribution under Council Regulation (EU) 2022/1854 of 6 October 2022 for emergency intervention to address high energy prices by companies in oil, natural gas and coal mining and oil refining activities.	-375.9		
Programmes to mitigate the economic effects of electricity and natural gas price volatility	-982.8		
Change in the parameters of the dividend policy	-482.5		
Total:	**-53.6**	**612.0**	**355.3**

4. Sensitivity Analysis and Comparison with the Previous Update

4.1 Alternative scenario

The international geopolitical situation was characterized by a high degree of uncertainty in 2023 as well. The Middle East region remains at particularly high risk, where a new escalation of the conflict would make it difficult for supply chains to function globally. In the developed alternative macroeconomic scenario, a variant of a more unfavourable dynamic of external demand and higher prices of tradable goods is considered. The shock to the growth of the European and world economies will be felt in 2024 and 2025, but the EU economy will also have a negative impact in 2026 due to its greater proximity to the region and dependence on trade. Some depreciation of the euro against the dollar is also expected.

Table 4-1: Summary of assumptions used in the alternative scenario (deviation from baseline) for the period 2024–2027

INTERNATIONAL ENVIRONMENT	2024	2025	2026	2027
World economy [real growth, %.]	-1.1	-0.5	0.1	0.0
European economy – EU (real growth,%)	-1.3	-0.8	-0.2	0.0
Annual average exchange rate USD / EUR	-5.0%	-2.5%	0.0%	0.0%
Crude oil, Brent/barrel [%]	21.1%	12.3%	0.0%	0.0%
Metals prices	11.4%	6.5%	0.0%	0.0%
Agricultural raw materials prices [in USD %]	17.3%	11.3%	0.0%	0.0%
Food prices [in USD %]	19.6%	12.8%	0.0%	0.0%
Non-energy raw materials prices [in USD,%]	0.0	0.0	0.0	0.0

Source: IAF

As a result of the simulation, inflation in the country will be higher compared to the baseline scenario, by 0.8 pps respectively. in 2024 and by 0.3 pps in 2025. The higher price increase in the alternative scenario will be followed by a period of slower domestic inflation compared to the baseline in 2026 and 2027. At the same time, the increase in international prices of crude oil, metals, agricultural raw materials, and food affect the import price index more substantially than the export price index, leading to a deterioration in the terms of trade and a correspondingly lower GDP deflator in 2024 compared to the baseline scenario. Given the very tight monetary conditions in the Euro area, the ECB is not expected to undertake another increase in key interest rates.

The increased cost of living will reduce purchasing power, which will translate into slightly lower household consumption over the entire forecast period. Investment activity will be limited by uncertainty, and higher costs for raw materials, and the effect will be somewhat delayed compared to other components of GDP. Weaker investment activity will lead to weaker labour demand and a slowdown in income growth relative to the baseline scenario, which in turn will also harm household consumption.

The unfavourable development of the external environment in 2024 and 2025 will also harm the growth of export of goods and services. Import of goods and services will also be lower than the baseline scenario, as a result of weaker domestic demand and export. The negative contribution of net export to GDP growth will increase in 2024, but will be more favourable in the last two years of the forecast period compared to the baseline scenario. The current account balance will follow trends in foreign trade and the dynamics of import and export prices, leading to its deterioration.

GDP growth will be lower by 0.6–0.7 pps compared to the baseline scenario at the beginning of the period. The level of GDP at both constant and current prices in the alternative scenario will remain permanently below that in the baseline until the end of the period.

A summary of the expected changes in key macroeconomic indicators, as a result of the changes made in the assumptions, is presented in the following table.

Table 4-2: Changes in key macroeconomic indicators (deviation from baseline)

Main macroeconomic indicators	2024	2025	2026	2027
GROSS DOMESTIC PRODUCT				
GDP level at current prices [%]	-2.1	-2.4	-2.5	-2.8
GDP [real growth, pps]	-0.7	-0.6	-0.1	0.0
Consumption	-0.1	-0.3	-0.3	-0.1
Gross fixed capital formation	0.3	-1.8	-1.0	0.4
Export of goods and services	-2.5	-1.1	0.0	-0.1
Import of goods and services	-1.3	-1.1	-0.5	-0.2
LABOR AND PRICES MARKET				
Employment (SNA) [%]	-0.2	-0.4	-0.5	-0.4
Unemployment rate [pps]	0.1	0.2	0.2	0.2
Compensation of employees [pps]	-0.8	-0.9	-1.0	-1.3
GDP deflator [pps]	-1.4	0.3	0.1	-0.4
Annual average inflation (HICP) [pps]	0.8	0.3	-0.4	-0.5
BALANCE OF PAYMENT				
Current account % of GDP [pps]	-2.6	-2.4	-1.8	-1.8
BUDGET SECTOR				
Budget revenues (%)	-0.8	-0.8	-1.0	-1.2
Budget balance % of GDP (%)	-0.3	-0.4	-0.5	-0.7
State debt % of GDP (%)	0.7	1.2	1.7	2.5

Source: IAF

4.2 Sensitivity of budget forecasts in different scenarios

The sensitivity analysis presents the change in basic budget parameters that would occur upon realization of the alternative macroeconomic scenario.

In the alternative scenario, GDP at current prices is lower over the period 2024–2027, which harms tax revenues and, accordingly, total budget revenues. Lower personal income tax revenues, as well as social security and health insurance contributions, are the main contributors, due to the lower level of compensation of employees in the alternative scenario. Total revenue would be lower than the baseline scenario by 0.8% in 2024 and 2025, after which the gap would begin to widen. As a result of lower revenues, the budget balance will begin to deteriorate by between 0.3 pps in 2024 and 0.7 pps towards the end of the period.

The change in assumptions and higher budget deficits will be reflected in an increase in government debt, as a percentage of GDP, by between 0.7 and 2.5 pps.

4.3 Comparison with the previous programme

The growth of the Bulgarian economy in 2023 was in line with the expectations in the previous Convergence Programme. There was a difference in components, which on the one hand is explained by a revision of the data for 2022, and on the other by a difference between the report and expectations for the external assumptions. Fixed capital investment in 2022 was revised decrease to growth and this had an effect on the dynamics in 2023. In addition, private investment activity during the year was weaker than expected. The slowdown in EU growth in 2023 was stronger than expected and this was reflected in a decline in export of goods. When preparing the forecast for 2023, a neutral contribution of the change in inventories was assumed, but the reported data show a strong negative contribution. The decrease in inventories was accompanied by a decrease in the import of goods.

Table 4-3: Main macroeconomic indicators

	2023			2024			2025			2026		
	CP 2023	CP 2022	Difference (pps)	CP 2023	CP 2022	Difference (pps)	CP 2023	CP 2022	Difference (pps)	CP 2023	CP 2022	Difference (pps)
GDP, real growth, incl:	1.8	1.8	0.0	3.2	3.3	-0.1	2.7	3.2	-0.5	2.7	3.0	-0.3
Final consumption	4.0	3.0	1.0	4.2	3.3	0.9	3.4	3.3	0.2	3.2	3.3	-0.1
Gross fixed capital formation	3.3	6.3	-3.0	8.5	12.6	-4.1	5.1	6.5	-1.4	4.4	4.8	-0.5
Export of goods and services	-1.9	1.7	-3.6	2.2	4.3	-2.1	3.7	4.7	-1.0	4.1	4.3	-0.2
Import of goods and services	-6.3	3.9	-10.2	5.0	6.4	-1.4	5.6	5.4	0.2	5.4	5.0	0.4
Average annual inflation (HICP)	8.6	8.7	-0.1	2.4	3.8	-1.4	2.8	2.8	0.0	2.0	2.2	-0.3
Employed	1.0	0.4	0.6	0.5	0.7	-0.2	0.3	0.5	-0.2	0.3	0.3	0.0
Unemployment rate	4.3	4.1	0.2	4.2	3.9	0.2	4.1	3.8	0.2	4.0	3.8	0.2

Source: IAF, NSSI

In the current Convergence Programme, lower GDP growth is expected for the period 2024-2026. International institutions have lowered their forecasts for EU growth and this has led to a downward adjustment in expectations for exports of goods and services. Weaker demand has also been reflected in a reduction in the forecast for investment growth over the forecast period. At the same time, a bigger increase in public consumption is expected in 2024 compared to the previous Convergence Programme.

In 2023, several indicators related to the labour market were updated, including of the number of people employed by the SNA, as well as the workforce and all its components from the LFS. This update was determined by the results on the number and composition of the population of the census conducted in the second half of 2021. The data of the relevant indicators for 2022 were updated, which in some cases led to dramatic changes related not only to the magnitude, but even to the direction of change of some indicators. For example, according to the previous data, employment in 2022 had increased by 1.3%, while according to the revised data, it decreased by 0.3%.

The relatively large differences in the 2023 forecast from the previous Convergence Programme and the 2023 reported data are largely due to these updates. According to the forecast, employment growth for 2023 was supposed to be 0.4%, while according to NSI data at the moment, employment in 2023 increased by 1% or by 0.6 pps more than forecast. At the same time, if we compare not the growth, but the number of employed, according to the forecast in the CP 2023, they were 3 516 thousand, while according to the reported number, they were 3 481 thousand. In other words, although employment growth is lower than reported, the number of employed people in the forecast is higher than reported to date by about 35 thousand. The lower number of employed people is almost entirely due to the lower number of self-employed persons, which is largely based on population estimates that have been updated as a result of published census data.

Secondly, it should be noted that in CP 2023 it was expected that the unemployment rate would reach a "plateau" in 2025-2026, while data from the LFS show that this phase in the dynamics of the indicator (which was also affected by the population update) probably occurred as early as 2023. This also explains the observed differences in the unemployment rate between CP 2023 and CP 2024 for both 2023 and 2024 projections. Downward population updates (as a result of census data) are also the reason for lower expectations for employment growth in 2024–2025 compared to CP 2023. In practice, we are moving forward one or two years more the severe limitation of employment growth caused by unfavourable demographic dynamics.

Compared to the previous update of the Convergence Programme, the inflation forecast for 2023 is very close to the reported value for the annual average HICP inflation in the country. Currently, the expectations for 2024 are for a smaller price increase, which is mostly associated with the effect of the measures to reduce inflation, which is estimated at -1 pps in average annual inflation. The expected larger declines in the international prices of some major commodity groups such as natural gas, food and metals also played a role in this direction.

5. Sustainability of Public Finances

5.1 Policy strategy

This section examines the long-term sustainability of the fiscal position, assessing the current state of public finances from the perspective of future increases in public spending related to population ageing. For this purpose, the sustainability indicators S1 and S2, calculated according to a methodology developed by the EC[9], are used.

Indicator S1 shows the necessary adjustment in the structural primary budget balance in the first projection year (2024) to keep the government debt-to-GDP ratio below 60% by 2070. Indicator S2 shows the adjustment in the structural primary balance in the first projection year, which is required to stabilize government debt in the long term.

A positive value of the indicators means a need for fiscal consolidation or structural reforms to reduce the burden of population aging on public finances, while a negative value indicates the presence of fiscal space.

Table 5-1: Sustainability indicators

	IAF		EC	
	S1	**S2**	**S1**	**S2**
Value, of which:	0.7	1.9	1.6	2.4
Initial budgetary position	2.5	2.7	2.7	2.9
Debt requirement	-0.7		-0.7	
Future changes in the budgetary position	-1.1	-0.7	-0.4	-0.5
Required structural primary balance in the first forecast year	-1.8	-0.6	-1	-0.3

Source: IAF,Debt Sustainability Monitor 2023

The table presents the IAF's estimates of the fiscal sustainability indicators and those of the EC from the EC's Debt Sustainability Monitor published in March 2024. The existence of differences in the values of the S1 and S2 indicators between the two institutions is largely due to different expectations for economic growth, debt and budget balance in the medium term. The Commission's estimates are based on forecasts from Autumn 2023. Moreover, the assessment of the sustainability of fiscal policy is highly dependent on the prospects for long-term economic development. The existence of differences in the values of indicators S1 and S2 between the two institutions is also due to differences in expectations for future changes in the budget

[9] European Commission (2024). "Debt Sustainability Monitor 2023". Institutional Paper 271

position, which are related to the costs of pensions, healthcare and education. In preparing its long-term macroeconomic forecast and the corresponding estimates of costs related to population aging, the IAF uses assumptions that are embedded in the 2024 Ageing Report, a forecast of pension expenditures submitted by the NSSI, and projections of health and education costs derived from the long-run model used[10].

According to the estimates of the IAF, the two indicators S1 and S2 are below 2%, which, according to the reference values of the EC[11], indicate a low risk for fiscal sustainability in the long term. However, to keep the debt level below 60% of GDP by 2070 a correction in the structural primary deficit is needed. The EC's 2023 Debt Sustainability Monitor assesses the risk to Bulgaria's public finances in the long term as moderate. The reason is the S2 indicator and more specifically the unfavourable initial budget position associated with a primary deficit.

5.2 Long-term budgetary perspectives, incl. the impact of the aging of the population

5.2.1 Social security

The long-term budget forecast for the development of the state pension system was developed under the parameters of the legislation in the field of pensions in force as of April 1, 2024 and the provisions of the Social Insurance Code, in accordance with the assumptions of the spring macroeconomic forecast of the Ministry of Finance of March 15, 2024.

In the long term, the following factors will have the strongest influence on the financial condition of the state pension system in Bulgaria:

- Demographic changes, represented by the coefficient of age dependence;
- Retirement conditions represented by the intra-system dependency ratio;
- The "generosity" of the public pension scheme, represented by the income replacement ratio.

Demographically, the Bulgarian pension system faces serious challenges. Eurostat forecasts show that the country's population will continue to decrease, while at the same time its age structure will deteriorate. This will lead to a significant increase in the age dependency ratio. If in 2023, 100 persons between the ages of 15 and 64 corresponded to 34 persons over the age of 65, then in 2070 their number will increase to 54 per 100 persons. The population of working age will decrease and its share of the total population in Bulgaria will shrink from about 64% to about 57%. In turn, the share of the elderly population (65+) will grow from around 22% in 2023 to 30% in 2070.

In the long term, the ratio between the number of pensioners and the number of insured persons will increase.

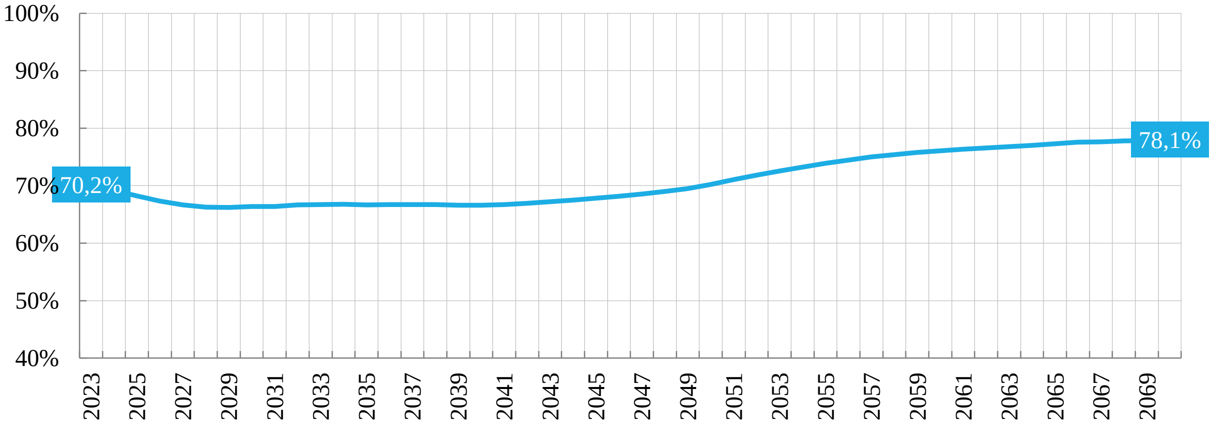
The ratio between the number of pensioners and the number of insured persons, also called the (systemic) dependency ratio, is a key indicator of the financial status of defined benefit pension schemes. The aging of the population and the increase in the average life expectancy on the one hand, and the reduction of the working-age population on the other, have a significant impact on the state insurance system in the long term.

[10] http://www.minfin.bg/upload/9114/D.E.2008.pdf

[11] S1<2 – low risk; 2<S1<6 – moderate risk; S1>6 – high risk;
S2<2 – low risk; 2<S2<6 – moderate risk; S2>6 – high risk.

In 2023, 70 pensioners with work pensions corresponded to 100 insured persons. As a result of the negative demographic changes, both the number of insured persons and the number of pensioners are expected to decrease in the long term. In view of the fact that in 2037 the legislative increase in the retirement age[12] will end, as well as due to the increase in the average life expectancy, the number of pensioners will decrease more slowly than that of insured persons. This will lead to a worsening of the system dependency ratio and it will reach 78.1 percent from 70.2 percent in 2023.

Graph 5-1: Pensioners with work-related pensions to insured persons (2023–2070)



The pension policies carried out in recent years contributed to increasing the adequacy of pensions.

The gross income replacement rate[13], which in 2019 was 38.8%, reached 54.3% in 2023. As a result of the pension policies implemented in 2022, in the next few years the gross income replacement ratio is expected to reach around 56-57%, and these are also the highest values for the entire period under consideration.

In the long run, the average value of the income replacement rate will decrease to about 40.0%. The most significant influence on this process is the legislative requirement for the reduction of the individual coefficient of pensioners who are granted a pension from both the State Social Security and the universal pension fund (second pillar)[14]. The rate of replacement by State Social Security will be lower for pensioners who were insured in both pillars. Their pensions will be reduced according to the percentage of the insurance contribution that was transferred to the second pillar, taking into account the number of months during which the person was insured in a universal pension fund in relation to the total length of his insurance service. These persons will receive an additional old-age pension from a universal pension fund. The reduction in the amount of first-pillar pensions granted to women born at the beginning of 1960 who become entitled to a pension for length of service and age in 2023 is about 10.0 per cent. This percentage will rise to around 25 per cent for pensions granted after 2050, as the entire insurance period of those who will retire then will cover periods after 2001 with provision in a universal pension fund. It is important to note that the value of the reduction is different for each individual pensioner and depends on the specific period that covers his insurance experience.

[12] The forecast does not take into account the linking of the retirement age to changes in the average life expectancy after 2037, since the legislation does not specify a mechanism by which this linking will be carried out.

[13] The ratio of the average pension for employment to the average insurance income of the insured persons for the relevant calendar year.

[14] Since 2002, persons born after 1959 are insured for a second pension in universal pension funds, and for them 5% of the pension insurance contribution is redirected to the second pillar.

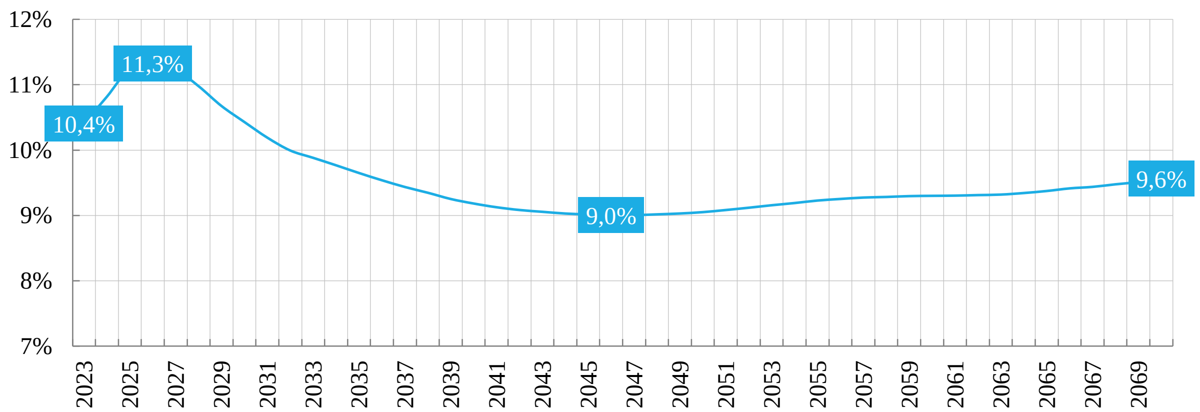
The rule for updating pensions under Art. 100 of the SIC, according to which modernization is carried out at a rate equal to the sum of 50% of the increase in insurable income and 50% of the harmonized index of consumer prices in the previous calendar year, also contributes to the downward trend in the income replacement ratio.

The dynamics in pension costs are directly dependent on the dynamics in the system dependency ratio and the income replacement ratio.

In 2023, total pension expenditure, including non-work-related pensions, reached 10.4% of GDP. Over the next few years, pension costs as a percentage of GDP will increase and in 2025 and 2026 will reach their highest value for the entire forecast period at 11.3%. After 2026, pension expenditure as a share of GDP will begin to gradually decline, reaching its lowest value of 9.0% in the period 2042-2050, after which it is expected to rise to 9.6% at the end of the forecast period. The reasons for the decrease in pension costs as a percentage of GDP in the period 2027-2050 are complex and can be summarized in two groups: 1) decrease in the number of pensioners and keeping the ratio between the number of pensioners and insured persons at relatively low levels – mainly due to demographic reasons and the stricter conditions for acquiring the right to a pension; 2) anticipatory growth of the average insurance income compared to the average pension, due to the applied mechanism for updating pensions and the reduction of the pension of persons who were insured in both pillars at the time of their retirement.

The following graph shows the results of the long-term forecast for the cost of pensions paid by the State Social Security for the period 2023–2070.

Graph 5-2: Pension expenditure as % of GDP (2023-2070)



Long-term pension costs will also be affected by the opportunity granted to insured persons born after 1959, who until August 2015 were mandatorily insured in the State Social Security (I pillar) and in a universal pension fund (II pillar), to change their insurance and switch to insurance only in the first pillar with an increased insurance contribution. As of March 2024, there are a total of about 107,000 persons with insurance transferred entirely to the first pillar, of which 59,479 already have a pension granted by the State Social Security in full, and the remaining 47,521 persons continue to be insured and accumulate pension rights.

In conclusion, the results of the long-term budget forecast show that, under current legislation, the fiscal pressure on the state pension system is strongest at the beginning of the forecast period, which is a result of the measures taken in 2022 to increase the adequacy of pensions. Then pension costs, measured as a share of GDP, will be the largest.

In the long run, the effect of an aging population and higher life expectancy will be largely offset by lower first pillar income replacement rates for those who have been insured in both pillars of the pension system. As these persons will also receive a second pension from the universal pension fund, the future adequacy of pensions will largely depend on the replacement rate that will be achieved by the second pillar.

5.2.2 Healthcare

In the long term, the share of total health expenditure is expected to reach 5.2% of GDP in 2050 and then slightly decrease to 5% in 2070. Similar dynamics are expected in the Ageing Report 2024. The forecast for long-term health care spending is based solely on population projections. Such a scenario is highly restrictive. It does not imply a change in public health spending policy in the context of expanding budget-funded health services. Also, according to a number of econometric studies, technological progress and other non-demographic factors are among the main causes of rising health care costs in developed countries. For this reason, in addition to the basic scenario, the Ageing Report examines 6 more scenarios for the development of health care costs related to different demographic and economic dynamics. The largest increase (1.2 pps) in Bulgaria's spending in the period 2022–2070 is forecast in the so-called risk scenario, in which factors other than demographics such as innovations in medical technologies are included.

Table 5-2: Health expenditure [15] % of GDP

	2022	2030	2040	2050	2060	2070	2070-2022
IAF	4.6	4.8	5.0	5.2	5.1	5.0	0.4
Ageing report 2024	5.1	5.2	5.4	5.6	5.6	5.4	0.4
Ageing report 2021	4.9	5.1	5.3	5.5	5.4	5.4	0.4

Source: IAF, Ageing report 2021, Ageing report 2024

5.2.3 Education

The IAF's forecast of public expenditure on education is based on the long-term demographic forecast and the assumption that expenditure will be indexed with the growth of nominal labour productivity. In the period after 2040, the stabilization of the demographic dynamics of the population up to 18 years of age is expected to lead to a smooth increase in total education expenditure until 2060. The EC forecasts expect a minimum increase in education expenditure as a % of GDP of 0.1 pps for the period 2022-2070, and in a scenario with an increase in the enrolment ratio in the education system, costs increase by 1.1 pps.

Table 5-3: Education expenses % of GDP

	2022	2030	2040	2050	2060	2070	2070-2022
IAF[16]	3.9	3.8	3.7	3.8	4.0	3.9	0.0
Report 2024	3.7	3.7	3.6	3.8	4.0	3.8	0.1
Report 2021	2.9	3.1	3.0	3.2	3.4	3.3	0.3

Source: IAF, Ageing report 2021, Ageing report 2024

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15 The values from the aging reports represent the sum of health care spending and long-term care spending. The Report's projections are based on data from the System of Health Accounts, while the IAF's projections are based on data from the General Government by Functions (COFOG) sector. For the purposes of the forecast, health expenditure as a % of GDP for the period 2020-2022 is kept at the 2019 level.

16 Classification of the functions of government (COFOG)

5.3 Contingent liabilities

The General Government guaranteed debt at the end of 2023 amounted to BGN 696.3 million or 0.4% of GDP, marking an increase in nominal terms compared to the level reported at the end of 2022 (603.9 BGN million or 0.4% of GDP). The increase is a consequence of the regular operations performed on the guaranteed loans.

The General Government guaranteed debt is mainly formed by the guarantees issued by the "Central Government" sub-sector with a share of 99.9%. Sub-sector "Local government" occupies about 0.1%, and according to the provisions of the PFL, social security funds cannot issue guarantees.

In 2024, assuming the issuance of the new state guarantees provided in the State Budget Law of the Republic of Bulgaria for 2024 and full utilization of the funds from the loans, the nominal amount of the General Government guaranteed debt is expected to increased significantly, reaching in nominal terms up to BGN 4.5 billion, and as a ratio to the estimated GDP, it amounted to about 2.3%. Under these assumptions and due to the fact that new loans are mostly intended to support strategic projects in the energy sector, at the end of 2024 a dominant share of 90% in the sectoral structure of guaranteed debt is expected to be taken by the guarantees of "Energy" sector, followed by the guarantees created as a result of the outbreak of COVID-19 - SURE and the Pan-European Guarantee Fund, as well as in connection with the participation of the Republic of Bulgaria in the instruments of the European Commission regarding the provision of macro-financial assistance, support for the economic and social sustainability of Ukraine, financing of its infrastructure in the form of grants and loans with a share of 7%. The remaining 3% represent the guarantees provided in accordance with the Student and Doctoral-Candidate Loans Law, under loan agreements of the Bulgarian Development Bank EAD, intended for energy efficiency and the green transition of SMEs, under other implemented international agreements and issued municipal guarantees.

In subsequent years of the forecast period, as a percentage of GDP, guaranteed debt is expected to gradually decrease to 2% at the end of 2027, mainly due to current assumptions for GDP growth in nominal terms and the planned servicing of guaranteed loans in line with agreed repayment plans.

6. QUALITY OF PUBLIC FINANCES

6.1 Policy strategy

The strategy of the policy in the field of the quality of public finances follows the consistent actions for institutional, normative and methodological changes in the direction of improving the management of public finances.

Achieving a sustainable medium-term fiscal framework is related to the implementation of a number of measures to increase the quality of public finances, expressed in improving the budget process, improving budget documents, confirming the application of good budget practices and tracking the effects of implemented sector policies through monitoring of the key indicators for measuring progress regarding the implementation of the strategic goals of the policies and the achievement of the expected benefits/effects for society.

The legal regulation of the budget framework is accompanied by constant monitoring and analysis of the application of budget legislation and budget practices, as well as compliance with fiscal rules. With the expected adoption of the revised economic governance framework (a new regulation on the preventive arm of the SGP and an amendment to the regulation on the corrective arm of the SGP, as well as a Council Directive amending Directive 2011/85/EU on requirements for Member States' budgetary frameworks) an organization is underway to prepare relevant changes in national budgetary legislation with a view to full transposition. The introduction of a new unified national document called the "medium-term fiscal-structural plan" for each member state of the European Union also implies the adaptation of the national budget documents both in terms of time scope and content, as well as in terms of the observed fiscal rules, as far as this is applicable. Setting a horizon of at least 4 years for policies, reforms and investments is challenging, but will also strengthen the sustainability of the budget framework in political and economic terms.

The legal framework for programme budgeting requires the government to maintain an up-to-date programme classification, approved by the Council of Ministers, that corresponds to the functions of the central administration and the portfolios of the executive authorities that carry out policies, therefore the programme classification is updated according to the currently valid normative arrangement. The introduction of the approach of program and result-oriented budgeting for the bodies of the judicial power from 2025 is legally regulated.

The quality of public finances is built on the basis of the developed macroeconomic and budget forecasts in support of the prudent fiscal policy pursued by the government, and for this purpose a corrective is necessary - an independent body that, with its functions, promotes the sustainability of the budget framework, including and by expressing opinions and making recommendations on macroeconomic and budgetary parameters contained in the main budget documents and monitoring compliance with fiscal rules.

Within the framework of the talks and preparatory activities for the accession of the Republic of Bulgaria to the OECD, a self-assessment of the compliance of legislation, policies and practices with the best OECD standards has been prepared, and discussions and recommendations are forthcoming within the framework of the technical reviews by the individual OECD Committees for subsequent steps to improve the legal framework and practices of the legal instruments of the OECD, which are related to the budget and public administration.

Bulgaria continues its participation in the periodic "Open Budget Survey" of the International Budget Partnership, noting over time a significant improvement in its assessment of budget transparency, which is at the level of the average value for the countries - OECD members with an index for the group of countries deemed to provide "significant information" on the budget.

6.2 Composition, effectiveness and cost efficiency – COFOG

From 2024, a capital program at the national and municipal level was included in the budget and began to be implemented, including expenses under programmes and mechanisms of the European Union and under other international programmes and treaties. For this purpose, the capital expenditures under the separate budgets of the first-level spending units with a budget under the state budget and part of the capital expenditures of the municipalities were allocated as a separate resource under the central budget. The capital programme during the forecast years is listed in full under the Economic Affairs function. Therefore, the 2027 cost breakdown by function cannot be compared to the reported performance for 2022.

Table 6-1: Budget spending by functions – COFOG

	% of GDP		% of Total spending	
	2022	2027	2022	2027
1. General Public Services	3.7	3.7	8.9	9.6
2. Defence	1.5	2.2	3.7	5.6
3. Public Order and Safety	2.5	2.2	6.1	5.6
4. Economic Activities	8.6	5.8	20.8	14.9
5. Environment Protection	0.7	0.5	1.8	1.4
6. Housing and Community Amenities	0.9	0.4	2.2	1.0
7. Health	5.6	5.4	13.4	13.8
8. Recreation, Culture and Religion	0.6	0.6	1.5	1.5
9. Education	3.9	3.7	9.4	9.6
10. Social Protection	13.3	14.5	32.2	37.1
11. Total spending	41.4	38.9	100.0	100.0

Expenditures under the "**General Public Services**" function will reach 3.7% of GDP in 2027. This functional group includes the costs of executive bodies of the central, regional and municipal administrations, legislative bodies and other general services of the administration, the contribution to the budget of EU, the reserve of budget organizations in the state budget, interest expenses of the "General Government" sector, etc.

Expenditure on the "**Defence**" function reaches the level of 2.2% of GDP. The costs include the resources for maintaining and developing the national defence capabilities and the capabilities related to the collective defence, including resource for the implementation of the investment projects approved by the National Assembly for the modernization of the Bulgarian Army, namely: the acquisition of a multifunctional modular patrol ship for the Navy, a new type of combat aircraft, including for accompanying costs (transportation, VAT and customs duties) and basic combat equipment for construction of battalion combat groups from the composition of a mechanized brigade. Additionally, funds are provided for the acquisition of ammunition and fuel for combat training, as well as for the acquisition, modernization, maintenance and repair of armaments and equipment, and for the accompanying construction of adjacent infrastructure.

Spending under the function "**Public Order and Safety**" is also expected to reach the level of 2.2% of GDP in 2027. This functional group includes spending on activities to counter serious crimes against the person and property of citizens, border control and guarding the state border, countering illegal migration on the territory of the Republic of Bulgaria and strengthening control over the establishment of illegally staying citizens on the territory of the country, ensuring fire safety and protecting the population in the event of fires, disasters and other emergency situations, and others.

Expenditure under the "**Economic Affairs**" function reaches 5.8% as a share of GDP. In addition to state expenditures under the Consolidated Fiscal Programme, the function also includes state enterprises that are part of the "General Government" sector and eliminated the expenditures related to European funds, which according to the ESA 2010 methodology have no impact on the revenues and expenditures of the sector "General Government" sector.

Expenditures under the "**Environmental Protection**" function are planned at the level of 0.5% of GDP. Under this function, measures in the field of protection and use of the components of the environment are financed; the national system for environmental monitoring and information security; to improve the investment process, maintain, modernize and build the technical infrastructure related to the implementation of geoprotection measures, etc.

Expenditures under the "**Housing and community amenities**" function will be at the level of 0.4% for 2027. This function includes the funds for management, control and regulation of housing construction and territorial development activities. Also included are the costs of implementing the National Programme for Energy Efficiency of Multifamily Residential Buildings. Another priority area includes activities for the management, maintenance and construction of the water supply infrastructure and activities related to the design, construction, operation and maintenance of the republican roads outside the cities.

Expenditures under the "**Health**" function are planned at the level of 5.4% of GDP. The function includes measures to protect the health of citizens; ensuring financial stability and security of the health system through a long-term, sustainable and predictable funding mechanism based on health outcomes; providing more resources for prevention, drugs and research in outpatient care; increasing the quality and accessibility of health services; ensuring health protection for children, pregnant women and persons with physical disabilities and mental disorders; development of emergency aid and emergency response capacity; better planning and motivating the health care workforce; development of electronic healthcare and digitization of the healthcare system.

Expenditures under the function "**Recreation, culture and religion**" will be 0.6% of GDP in 2027. This function includes measures in the field of protection of movable and immovable cultural heritage, where the main priorities are preservation and socialization of cultural heritage and stimulating its connection with tourist products, attracting project funding in the field of culture under various programmes and donors, development and technical improvement of the museum network, attracting funds from European programmes and bilateral agreements for the support of culture and establishing Bulgaria as a destination for the implementation of international cultural projects. This also function includes policies in the field of sports for students and sports in free time, as well as in the field of bringing the sports sites and facilities into a form that meets modern international standards.

Expenditures under the "**Education**" function will reach the level of 3.7% of GDP, including measures aimed at implementing policies in preschool and school education, effective socialization of children from early childhood, ensuring equal access to quality education, personal development of children and students, promotion of innovations, qualification and improvement of the pay of pedagogical specialists, modernization of educational institutions, digitization of education.

Expenditure under the function "**Social Protection**" is expected to reach the level of 14.5% of GDP in 2027. The growth of this function is associated with an increase in the expenditure on pensions and social benefits. The greatest budgetary effect is from the annual indexation of pensions according to the Swiss rule, as there is also an effect from the increase in the amount of supplements to pensions under Art. 84 of the SIC (so-called "widow's supplements") of 30.0% of the deceased spouse's pension, starting from July 1, 2024 and the increase in the number of newly granted pensions, taking into account the actual length of service of the periods of conscription or peacetime alternative service and the periods of repression suffered.

6.3 Structure and efficiency of revenue systems

6.3.1 Tax policy and legislation

During the period 2024-2027, the goal remains to implement a policy aimed at increasing revenue collection and achieving the set budget goals.

Many of the measures to improve revenue collection in the area of tax policy are of a permanent nature, are included in the strategic documents that each of the responsible institutions develops and implements and will continue to be implemented in the period 2024-2027. At the same time, to fulfil the priority objectives of the tax policy, legislative changes and actions of the revenue administrations in the field of collection and control are carried out.

– Legislative changes

<u>To increase budget revenues and combat tax fraud - measures to improve compliance with legislation, prevention and countermeasures against tax fraud and tax evasion.</u>

The measure for implementation of fiscal control over the movement of goods with a high fiscal risk (GHFR) has been upgraded with the introduction of mandatory preliminary declaration of data for the transport of GHFR on the territory of the Republic of Bulgaria (State Gazette, No. 66 of 2023, in force from 1.10.2023).

From 01.01.2024, the adopted changes in the Tax and Social Insurance Procedure Code (promulgation, SG No. 100 of 2022) are in force, which improve the overall regulation of the exchange of information and administrative cooperation and expand the scope of the automatic exchange of information, including the information provided by the operators of digital platforms about sellers operating through those platforms. The changes are in line with the requirements of Council Directive (EU) 2021/514 of 22 March 2021 amending Directive 2011/16/EU on administrative cooperation in the field of taxation.

From the beginning of 2024, the amendments made to the Value Added Tax (VAT) Law (promulgated, SG No. 102 of 2022, effective from 01.01.2024) are also in force in order to allow the problem of VAT fraud in e-commerce, by strengthening cooperation between tax authorities and payment service providers, in relation to the requirements for payment service providers introduced by the provisions of Council Directive (EU) 2020/284 of 18 February 2020 amending Directive 2006/112/EC regarding the introduction of certain requirements for payment service providers (Directive (EU) 2020/284).

As a measure aimed at clarifying the shadow economy, a legal norm has been adopted, which enables a delivery recipient to withhold payment of the value of the purchase, in cases where the supplier is obliged, but has not issued a receipt (Law amending and supplementing the VAT Law, SG, No. 106 of 2023, effective from 01.01.2024).

An obligation has been introduced (Art. 123 para. 10 of the VAT Law) to declare data from the current accounting records for the cash available, as well as the amount of receivables (including from granted loans) from natural persons, workers, employees, persons, employed under a management and control contract, and accountable persons, provided that at the end of a calendar quarter, the total amount of assets and receivables exceeds BGN 50,000.

The excise calendar introduced in the Law on Excise Taxes and Tax Warehouses for the gradual increase of rates over a period of four years in relation to excise taxation of tobacco and tobacco products is being implemented - effective from March 1, 2023.

In accordance with Council Directive (EU) 2022/2523 of 14 December 2022 to ensure a global minimum level of 15 percent taxation at the EU level of multinational enterprise groups and large national groups in the Union, an additional tax to achieve minimum effective corporate taxation of multinational enterprise groups and of large national enterprise groups is introduced. A national additional tax has been introduced in the country, according to which the constituent entities of a multinational group of enterprises located in the Republic of Bulgaria, or of a large national group of enterprises, are subject to taxation with a national additional tax.

The provisions of the LCIT, introducing the regime of taxation upon leaving according to Art. 5 of Council Directive (EU) 2016/1164 of 12 July 2016 establishing rules against tax avoidance practices that directly affect the functioning of the internal market. The change concerns the transfer of assets/activity to another part of the enterprise located outside the country, which are part of the general regime for tax regulation in the case of a transfer between a part of an enterprise located in the country and another part of the same enterprise located outside the country.

In order to ensure a more effective countermeasure against tax evasion by paying a part of the remuneration in the form of "tax-free income", a change was made in the Personal Income Tax Law, expanding the scope for providing information by payers of income concerning non-taxable income incomes.

It is adopted that the payment of labour remuneration is carried out only by transfer or deposit to a bank payment account in the country specified by the worker or employee, when it is paid by an employer with 100 or more employed persons (except for persons with whom an employment contract for short-term seasonal agricultural work has been concluded) - Art. 3, para. 1, item 3 of the Law on Restriction of Cash Payments (SG, No. 66 of 2023).

<u>To improve the business environment and reduce the administrative burden and costs for businesses and citizens</u>

After the increase in the threshold for mandatory VAT registration from BGN 50,000 to BGN 100,000 in 2023, the amount of this threshold was increased again to BGN 160,000 (SG, No. 106 of 2023). The change will become effective from the beginning of 2025.

In connection with the implementation in the Customs Information System for the import of the functionality for centralized import clearance at the end of October 2023, a deferred payment of VAT has been introduced for centralized import clearance. Deferred payment means that the payment of VAT on import to customs is postponed and the tax is paid until the 16th of the month following the month of acceptance of the customs declaration. This regime is within the scope of Art. 211, para. 1 of Directive 2006/112/EC of November 28, 2006 on the general system of value added tax (Directive 2006/112/EC) - SG No. 106 of 2023, in force from 01.01.2024.

In view of the principles of legal certainty, proportionality and neutrality of VAT, the cases where a taxable person has not fulfilled his obligation to submit an application for registration under the law have been settled in a new way. The purpose of the changes made is to enable persons who have not submitted or have not submitted an application for VAT registration in due time, due to which they are registered later, to be able to issue tax documents in which they charge the VAT due for the taxable supplies made by them for the periods for which they should have been registered. Accordingly, the possibility of exercising the right to deduction of input VAT in a correctly issued VAT tax document by a registered person - the consignee of the relevant delivery, is also regulated.

A new scheme of state aid for farmers has been developed, related to the amendment of the legal framework for the implementation of state aid for farmers in the form of tax relief under Art. 189b of the LCIT and Art. 48, para. 6 of the PITL, in accordance with the terms of Regulation (EU) No. 2022/2472 of the Commission of 14 December 2022 regarding the declaration of certain categories of aid in the agriculture and forestry sectors and in rural areas as compatible with the internal market in application of Articles 107 and 108 of the TFEU (Regulation (EU) No. 2022/2472).

A new preference for natural persons registered as farmers has been introduced in the Personal Income Tax Law (Art. 22h of the PITL - SG No. 106 of 2023, effective from 01.01.2024), according to which individuals registered as farmers, who have received a subsidy or other support from the European Agricultural Guarantee Fund and the European Rural Development Fund, can use tax relief by reducing the amount of the annual tax bases by the amount of the subsidy received during the year, respectively support from the two funds, up to the amount of the annual tax bases before the reduction, but with no more than BGN 100,000. The tax relief applies from January 1 of the year in which the European Commission ruled that the measure is not state aid or is compatible state aid. If the European Commission decides by April 30, 2024, the tax relief may also apply for 2023.

From 1 January 2024, electronic food vouchers have been introduced with the aim of reducing the administrative burden through digitization and ensuring a more competitive environment for all persons involved in the scheme for the provision and use of food vouchers - food voucher operators, employers, employees and others. There is a six-month transition period during which both paper food vouchers and electronic food vouchers will be operational. From July 1, 2024, it is planned to completely switch to food vouchers on electronic media (Art. 59 of the LSBRB, SG No. 108 of 2023). The current tax relief for providing employees with social expenses in the form of food vouchers (on paper and electronic media) in a non-taxable amount of up to BGN 200 per month is maintained. With the changes adopted in the 2024 LSBRB, the total annual quota for providing food vouchers under Art. 209, para. 7 of LCIT is increased from BGN 1.4 billion to BGN 1.6 billion for 2024.

The increased amount of the tax benefits under Art. 22c and 22d of the Personal Income Tax Law (for children and for children with disabilities) is maintained in 2024, as follows: BGN 6,000 per year for one minor child, BGN 12,000 for two minor children, BGN 18,000 - for three and more minor children and, accordingly, for children with disabilities in the amount of BGN 12,000 per year, with the possibility of advance use during the year.

The application period of the zero VAT rate for supplies of bread and flour with a place of supply on the territory of the country, for imports and for taxable intra-community acquisitions, has been extended until 30.06.2024. Until the same date, the reduced tax rate of 9% VAT will also apply for the supply of a service for the use of sports facilities and a general tourist service.

The application period of the reduced rate of 9% VAT for the supply of restaurant and catering services has been extended until the end of 2024.

Changes have been adopted in the Personal Income Tax Law to introduce legally recognized expenses in the amount of 10 percent when determining the taxable income from the sale or exchange of financial assets and foreign currency. Virtual currencies are explicitly defined as a financial asset.

Income from the sale or exchange of movable property transferred to persons who have the right to collect, transport, recover or dispose of waste in accordance with the Waste Management Law are exempt from taxation.

The introduced short-term anti-inflationary measures to exempt electricity, liquefied petroleum gas and natural gas from excise duty pursuant to Article 15 of Council Directive 2003/96/EC of October 27, 2003 on the restructuring the Community legal framework for the taxation of energy products and electricity has been prematurely terminated. The initially adopted term of until 30.06.2025. In response to the Council's recommendation from 2023 for the gradual termination of the current emergency measures for energy support, the measure was terminated with the adoption of the Law on the State Budget of the Republic of Bulgaria for 2023 promulgated on 01.08.2023.

7. Institutional Characteristics of Public Finances

7.1 National fiscal rules

The permanent arrangement of fiscal rules in the PFL has a positive impact not only for improving coordination in the implementation of various policies, but also for better planning, development and implementation of fiscal policy, as their long-term sustainability and the sustainability of public finances are guaranteed.

Another prerequisite for achieving sustainability in terms of public finances and the parameters of the budget framework is the existence of a legal framework and procedures for corrective mechanisms and measures to return to the target or to the limitation determined by the rule in case of deviation from the target/limitation.

In terms of scope, we distinguish between fiscal rules for indicators according to the national methodology - for the budget balance and expenditures under the consolidated fiscal programme (on a cash basis) and for the government debt, and indicators according to the European methodology - for the "General Government" sector (for some rules - and for its respective subsectors) - for the medium-term budget objective for the structural deficit, for the budget balance, for the growth of expenditure relative to the growth of potential GDP and for the consolidated debt for the "General Government" sector.

With the adoption of the PFL and the Law on Fiscal Council and Automatic Corrective Mechanisms and their subsequent amendments related to achieving full compliance with European legislation, Bulgaria fully covered the requirements for strengthening economic governance in the EU. In this way, the rules meet the internationally accepted definitions and criteria and the requirements for harmonizing national fiscal planning with the preventive and corrective part of the EU's SGP.

From the adoption of the PFL in 2013 to the present moment, three (in 2016, 2017 and 2020) significant amendments to the PFL were adopted, which were related to the refinement and further development of the regulation in order to improve the processes of the governance of public finances and achieving full compliance with the requirements of Council Directive 2011/85/EU of November 8, 2011 on the requirements for the budgetary frameworks of the Member States, the creation of conditions for the implementation of the relevant regulations adopted at the end of 2011, as well as in terms of fiscal rules and restrictions with a view to ensuring an adequate response to the challenges of the COVID-19 crisis and the created emergency situation, for which the derogation clause was activated within the European Union, which allowed during emergency circumstances for a certain period of time that the costs directly related to the consequences of overcoming the pandemic are excluded from the scope when assessing compliance with the relevant fiscal rules and restrictions. With the adoption of these changes, it has been ensured that the restrictions are flexible in relation to the dynamic global challenges to the economy and the budget while complying with the requirements of European legislation.

With the upcoming adoption of the reformed economic governance framework (a new regulation on the preventive arm of the SGP and amendment to the regulation on the corrective arm of the SGP, as well as the Council Directive amending Directive 2011/85/EU on the requirements for the budget frameworks of the member states), in addition to the introduction of completely new documents (a national medium-term fiscal-structural plan and an annual progress report on its implementation), a change of the fiscal rules is also foreseen, which implies, in addition to their immediate application within the national medium-term fiscal-structural plan this year, respective transposition into national legislation of the new requirements resulting from the amendment of Directive 2011/85/EU. These innovations will require changes to the provisions in Chapter Two "Fiscal Rules" of the PFL in the part of the rules on the deficit, debt and expenditure of the "General Government" sector, including in relation to escape clauses.

In addition to the PFL, changes will also be necessary in the Law on Fiscal Council and automatic corrective mechanisms in relation to the new rules, requirements, procedures and documents, respectively functions of the national independent fiscal institution.

7.2 Budgetary procedures

According to the PFL, the budget procedure includes stages, terms, distribution of responsibilities and requirements for the preparation of the medium-term budget forecast and the draft state budget for the relevant period. As the main schedule for organizing the process of planning and drawing up the main budget documents, the budget procedure takes into account both the changing requirements for all responsible institutions and the requirements for Bulgaria as a Member State within the so-called European semester, through which national economic and budgetary policies are harmonized within the framework of the European Union.

The budget procedure for 2025 (approved by Decision No. 71 of the Council of Ministers of February 1, 2024) was prepared according to the rules of the Law on Public Finances, and during its preparation the set requirements for the structure and content of key budget documents and deadlines were reflected for their preparation.

The purpose of the budget procedure for 2025 is to create the necessary organization and coordination between the individual spending units in the process of budget planning and drawing up the main budget documents (the medium-term budget forecast for the period 2025-2027 and its update as reasons for the draft law of the state budget of the Republic of Bulgaria for 2025). In view of this, it covers all budgetary organizations, as well as legal entities controlled by the state and/or by the municipalities, which are not part of the consolidated fiscal programme, but fall within the scope of the "General Government" sector.

A new point in the 2025 budget procedure is the proposal that the budget forecast for the period 2025-2027, the draft budget for 2025 and the updated budget forecast for 2026 and 2027 of the judiciary are also developed in a programme format in accordance with § 7 and 10 of the transitional and final provisions of the Law on the State Budget of the Republic of Bulgaria for 2024, where it is stated that a programme budget format will be applied to the budget of the judiciary according to the Methodology for Programme Budget in the Judiciary adopted by the Plenum of the Supreme Judicial Council, corresponding to the applicable general requirements for the structure and content of budget programme formats under the Public Finance Act. With the introduction of results-oriented budgeting in the judicial system as well, the process of covering all first-level spending units, whose budgets are included in the state budget, ends.

The first stage of the 2025 budget procedure covers the development and approval of the medium-term budget forecast for the period 2025-2027; adoption of standards for activities delegated by the state with natural and value indicators in 2025; approval of norms for an hour programme for preparation, creation and distribution of national and regional programmes of Bulgarian National Radio and Bulgarian National Television in 2025; approval of the Convergence Programme (2024-2027) and the 2024 update of the National Reform Programme; approving the maximum amount of new state guarantees that may be issued in 2025 under the

Student and Doctoral Loan Law and approving the projects to be financed with state and/or state-guaranteed loans in 2025.

The current European and national legislation requires in the spring of each year the government to develop a medium-term budget forecast, a Convergence Programme and a National Reform Programme under the same macroeconomic and fiscal forecasts and assumptions.

In the current situation, in the absence of a regular government with an appropriate governance programme and clear prospects for the budgetary framework and for the development of policies and reforms in the coming years, as well as with the expected final adoption of the revised economic governance framework and the requirement to prepare a new unified national document (medium-term fiscal-structural plan), some changes are required in terms of the structure and content of the budget documents prepared at the first stage of the budget procedure for 2025. Currently, the possibility of a one-time settlement of the procedure for the preparation and approval by the Council of Ministers of basic budget documents such as the Convergence Programme and the medium-term budget forecast for the period 2025-2027, which is related to overcoming the political challenge and ensuring a transition to the preparation of the first medium-term fiscal structural plan for Bulgaria, namely with the adoption of the current Convergence Programme the Medium-term budget forecast for the period 2025-2027 to be also considered approved.

In the second stage of the procedure, the main processes and budget documents are related to the preparation of the Law on the state budget of the Republic of Bulgaria for 2025 and an updated medium-term budget forecast for the period 2025-2027 as reasons for it, as well as the related conciliation procedures with interested institutions and organizations, including and with the National Association of Municipalities in the Republic of Bulgaria on the mechanism for allocating the general equalization subsidy and the targeted subsidy for capital expenditures by municipalities and conducting consultations on the association's proposals for the total amount of the main budgetary relationships of the municipal budgets with the central budget and others proposals on the draft state budget for 2025 in its part for municipalities.

As defined in the PFL, the procedure envisages that by the end of October 2024 the Council of Ministers will consider and approve the prepared by the Minister of Finance drafts of the Law on the State Budget of the Republic of Bulgaria for 2025 and of the updated medium-term budget forecast for the period 2025- 2027, and if necessary to approve and amend other related acts of the government. In the same period, the Council of Ministers examines and approves the drafts of the National Health Insurance Fund Budget Law for 2025.

Within one month of the promulgation in the "State Gazette" of the Law on the State Budget of the Republic of Bulgaria for 2025, the Council of Ministers adopts, on the proposal of the Minister of Finance, a Decree on the implementation of the State Budget of the Republic of Bulgaria for 2025.

The procedure foresees, if necessary, approval of changes to the updated medium-term budget forecast for the period 2025-2027, respectively, and the resulting need to update and publish the programme formats of the budgets of the first-level spending units, with which the budget procedure for 2025 ends.

The final results and the overall success of the 2025 budget procedure depend both on the management decisions of the government and on the good faith participation in the budget process of all budget organizations.

The 2025 budget procedure was developed under current European and national legislation, but after the final adoption of the revised economic governance framework, a transition will be made to ensure, within the second stage of the procedure, the development of a national medium-term fiscal-structural plan for Bulgaria.

The period for the preparation of the first medium-term fiscal-structural plan for Bulgaria should, after the holding of the upcoming extraordinary parliamentary elections, coincide with the beginning of the mandate of a regular government. The priorities from the new government's programme, including in terms of fiscal objectives, policies, planned reforms and investments, should be reflected in the plan. Insofar as the new rules stipulate that the plans should be submitted to the European Commission by September 20, 2024, with the possibility of an exception, given the current political situation, Bulgaria would benefit from the exception, and plan to submit its plan at the end of October.

8. ANNEX A

Table 1a: Macroeconomic prospects

	ESA 2010 Code	2023	2023	2024	2025	2026	2027
		Level (MBGN)	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change
Real GDP (2015 prices)	B1*g	110,859	1.8	3.2	2.7	2.7	2.6
Nominal GDP	B1*g	183,743	9.5	8.7	5.9	5.4	5.2
Components of real GDP							
Private consumption expenditure	P.3	75,526	5.4	4.1	3.9	3.5	3.5
Government consumption expenditure	P.3	18,846	-0.4	4.5	1.8	2.2	2.2
Gross fixed capital formation	P.51	20,134	3.3	8.5	5.1	4.4	6.1
Change in inventories and net acquisition of valuables (% of GDP)	P.52+ P.53	1,224	1.5	1.5	1.5	1.5	1.5
Export of goods and services	P.6	75,778	-1.9	2.2	3.7	4.1	3.8
Import of goods and services	P.7	80,863	-6.3	5.0	5.6	5.4	5.9
Contributions to real GDP growth (In percentage points)							
Final domestic demand			3.6	4.7	3.6	3.3	3.7
Change in inventories and net acquisition of valuables	P.52+P .53		-4.8	0.0	0.0	0.0	0.0
External balance of goods and services	B.11		3.0	-1.5	-1.0	-0.7	-1.2

Table 1b: Price developments

	ESA 2010 code	2023	2023	2024	2025	2026	2027
		Level	Rate of Change[17]	Rate of Change	Rate of Change	Rate of Change	Rate of Change
GDP deflator		100	7.5	5.4	3.2	2.6	2.6
Private consumption deflator		100	6.9	5.1	3.0	2.4	2.3
HICP[18]		100	8.6	2.4	2.8	2.0	1.9
Public consumption deflator		100	9.1	5.2	2.5	3.1	2.8
Investments deflator		100	7.8	5.7	2.7	2.2	2.1
Export price deflator (goods and services)		100	-1.8	1.5	1.1	1.2	1.1
Import price deflator (goods and services)		100	-2.3	1.2	0.5	0.9	0.7

Table 1c: Labour market developments

	ESA 2010 code	2023	2023	2024	2025	2026	2027
		Level	Rate of Change	Rate of Change	Rate of Change	Rate of Change	Rate of Change
Employment (thousand persons)[19]		3,481	1.0	0.5	0.3	0.3	0.3
Employment (millions of hours worked)[20]		5,631	1.0	0.6	0.8	0.5	0.7
Unemployment rate[21]		4.3	4.3	4.2	4.1	4.0	4.0
Labour productivity (BGN per person employed)[22]		31,849	0.9	2.7	2.3	2.4	2.3
Labour Productivity (BGN per hour worked)[23]		19.7	0.8	2.6	1.9	2.2	1.9
Compensation of employees (MBGN)[24]	D.1	80,811	14.9	9.9	6.1	5.4	5.2
Compensation per employee		30,526	13.3	9.3	5.8	5.1	4.6

17 Percentage change as compared to the previous year.
18 Optional for Stability Programmes.
19 Occupied population, national accounts definition.
20 National accounts definition.
21 Harmonised definition, Eurostat; levels.
22 Real GDP per one person employed.
23 Real GDP per one hour worked.
24 In BGN million.

Table 1d: Sectorial balances

% of GDP	ESA 2010 code	2023	2024	2025	2026	2027
Net lending/borrowing vis-à-vis the rest of the world	B.9	1.7	1.8	-0.1	-0.9	-2.3
of which: –balance of goods and services		3.2	1.7	1.0	0.5	-0.4
–balance of primary incomes and transfers		-2.9	-2.9	-2.9	-2.7	-2.7
–capital account		1.4	3.1	1.8	1.4	0.8
Net lending/borrowing of the private sector	B.9	3.5	4.8	2.9	1.9	0.6
Net lending/borrowing of the General Government	EDP B.9	-1.9	-3.0	-3.0	-2.8	-3.0
Statistical discrepancy						

Table 2a: General government budget prospects

	ESA 2010 code	2023	2023	2024	2025	2026	2027
		Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. General government	S.13	-3 454.5	-1.9	-3.0	-3.0	-2.8	-3.0
2. Central government	S.1311	-3 374.7	-1.8	-3.8	-3.9	-3.6	-3.8
3. State government	S.1312						
4. Local government	S.1313	-200.5	-0.1	0.8	0.8	0.8	0.8
5. Social security funds	S.1314	120.8	0.1	0.0	0.0	0.0	0.0
6. Total revenue	TR	69 696.6	37.9	37.2	37.1	37.6	35.9
7. Total expenditure	TE	73 151.1	39.8	40.2	40.2	40.3	38.9
8. Net lending / borrowing	EDP B.9	-3 454.5	-1.9	-3.0	-3.0	-2.8	-3.0
9. Interest expenditure	EDP D.41	803.9	0.4	0.7	1.0	1.2	1.2
10. Primary balance		-2 650.5	-1.4	-2.3	-2.1	-1.5	-1.8
11. One-off and other temporary measures		1 053.5	0.6	-0.5	-0.8	-0.5	-1.8
12. Total taxes (12=12a+12b+12c)		39,325.0	21.4	21.7	21.5	21.8	21.4
12a. Taxes on production and import	D.2	27,139.8	14.8	14.7	14.4	14.6	14.4

	ESA 2010 code	2023	2023	2024	2025	2026	2027
		Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
12b. Current taxes on income, wealth, etc.	D.5	11,651.9	6.3	6.7	6.8	6.9	6.8
12c. Capital taxes	D.91	533.2	0.3	0.3	0.3	0.3	0.3
13. Social contributions	D.61	15,755.0	8.6	8.9	9.2	9.4	9.0
14. Property income	D.4	2 622.1	1.4	1.1	1.4	1.7	1.6
15. Other		11 994.5	6.5	5.5	5.0	4.8	3.9
16=6. Total revenue	TR	69 696.6	37.9	37.2	37.1	37.6	35.9
Tax burden (D.2+D.5+D.61+D.91-D.995)		55,080.0	30.0	30.7	30.7	31.2	30.4
17. Compensation of employees + intermediate consumption	D.1+P.2	27,159.3	14.8	15.5	14.9	14.8	14.2
17a. Compensation of employees	D.1	19,124.7	10.4	10.6	10.6	10.5	10.1
17b. Intermediate consumption	P.2	8,034.6	4.4	4.8	4.4	4.4	4.1
18. Total social transfers (18=18a+18b)		29 908.5	16.3	16.3	16.9	17.1	16.7
of which Unemployment benefits	D.621, D.624	479.1	0.3	0.3	0.2	0.2	0.2
18a. Social transfers in kind	D.6311. D.63121. D.63131	6 899.2	3.8	-13.4	13.3	9.0	-0.8
18b. Social transfers other than in kind	D.62	23,009.3	12.5	16.7	9.0	6.1	3.2
19=9. Interest expenditure	EDP D.41	803.9	0.4	0.7	1.0	1.2	1.2
20. Subsidies	D.3	4,758.2	2.6	2.2	2.0	2.3	2.0
21. Gross fixed capital formation	P.51	6,429.1	3.5	4.0	3.8	3.1	3.6
22. Capital transfers	D.9	694.4	0.4	0.1	0.3	0.4	0.0
23. Other		3 397.6	1.8	1.4	1.2	1.4	1.3
24=7. Total expenditure	TE1	73 151.1	39.8	40.2	40.2	40.3	38.9
Government consumption (nominal))	P.3	33 409.8	18.2	18.4	18.1	18.1	18.1

Table 2b: No-policy change projections

	2023	2023	2024	2025	2026	2027
	Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. Total revenue at unchanged policies	69 696,6	37.93	37.23	36.79	37.43	35.92
2. Total expenditure at unchanged policies	73 151,1	39.81	40.51	39.69	40,79	36,85

Table 2c: Amounts to be excluded from the expenditure benchmark

	2023	2023	2024	2025	2026	2027
	Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. Expenditure on EU programmes fully matched by EU funds revenue	2,642.9	1.4	1.7	1.7	1.6	0.8
1a. Investments fully matched by EU funds revenue	1,041.6	0.6	0.4	0.3	0.3	0.4
2. Cyclical unemployment benefit expenditure	1,601.3	0.9	1.3	1.4	1.3	0.4
3. Effect of discretionary revenue measures	479.1	0.3	0.3	0.2	0.2	0.2
4. Revenue increases mandated by law	-1,200.2	-0.7	0.0	0.3	0.2	0.0

Table 3: General government expenditure by function

% of GDP	ESA 2010 code	2022	2027
1. General public services	1	3.7	3.7
2. Defence	2	1.5	2.2
3. Public order and safety	3	2.5	2.2
4. Economic affairs	4	8.6	5.8
5. Environmental protection	5	0.7	0.5
6. Housing and community amenities	6	0.9	0.4
7. Health	7	5.6	5.4
8. Recreation, culture and religion	8	0.6	0.6
9. Education	9	3.9	3.7
10. Social protection	10	13.3	14.5
11. Total expenditure (= item 7 = 24 of Table 2)	TE1	41.4	38.9

Table 4: General government debt developments

% of GDP	ESA code	2023	2024	2025	2026	2027
1. Gross debt[25]		23.1	25.0	27.3	30.0	30.7
2. Change in gross debt level		0.5	1.9	2.3	2.7	0.8
3. Primary balance[26]						
4. Interest expenditure[27]	EDP D.41	0.4	0.7	1.0	1,2	1.2
5. Stock-flow adjustment						
of which:						
Differences between cash and accruals[28]						
Net accumulation of financial assets[29]						
of which: privatisation proceeds						
Valuation effects and other[30]						
Implicit interest rate on debt[31]		2.1	3.3	4.0	4.7	4.2
6. Liquid financial assets[32]						
7. Net financial debt (7=1-6)						
8. Debt amortization since the end of the previous year		8.5	9.5	8.0	5.2	5.4
9. Percentage of debt denominated in foreign currency		73.2	71.6	74.5	77.2	75.5
10. Average maturity		7.7	7.8	8.2	8.6	8.4

25 As defined in Regulation 479/2009 (not an ESA concept).

26 Cf. item 10 in Table 2.

27 Cf. item 9 in Table.

28 The differences concerning interest expenditure, other expenditure and revenue could be distinguished when relevant or in case the debt-to-GDP ratio is above the reference value.

29 Including liquid assets, government securities, assets in third countries, government controlled enterprises and the difference between quoted and non-quoted assets could be distinguished when relevant or in case the debt-to-GDP ratio is above the reference value.

30 Changes due to exchange rate movements, and operation in secondary market could be distinguished when relevant or in case the debt-to-GDP ratio is above the reference value.

31 Approximately calculated as interest expenditure divided by the debt level of the previous year.

32 AF1, AF2, AF3 (consolidated at market value), AF5 (if quoted in stock exchange; including mutual fund shares).

Table 5: Cyclical developments

% of GDP	ESA 2010 code	2023	2024	2025	2026	2027
1. GDP growth (%)		1.8	3.2	2.7	2.7	2.6
2. Net lending of general government	EDP B.9	-1.9	-3.0	-3.0	-2.8	-3.0
3. Interest expenditure	EDP D.41	0.4	0.7	1.0	1.2	1.2
4. One-off and other temporary measures		0.6	-0.5	-0.8	-0.5	-1.8
5. Potential GDP growth (%)		2.6	3.0	3.0	2.9	2.9
Contributions:						
labour		-0.1	0.4	0.4	0.4	0.3
capital		0.8	0.9	1.0	1.0	1.1
total factor productivity		1.9	1.8	1.6	1.5	1.5
6. Output gap		0.7	0.8	0.4	0.2	-0.1
7. Cyclical budget component		0.2	0.2	0.1	0.1	0.0
8. Cyclically-adjusted balance (2-7)		-2.1	-3.2	-3.2	-2.8	-3.0
9. Cyclically-adjusted primary balance (8+3)		-1.6	-2.5	-2.2	-1.6	-1.8
10. Structural balance (8-4)		-2.6	-2.8	-2.3	-2.3	-1.2

Table 6: Divergence from previous update

	ESA 2010 code	2023	2024	2025	2026	2027
Real GDP growth (%)						
Previous update		1.8	3.3	3.2	3.0	
Current update		1.8	3.2	2.7	2.7	2.6
Difference (pps)		0.0	-0.1	-0.5	-0.3	
General Government net lending (% of GDP)	EDP B.9					
Previous update		-6.1	-4.7	-4.9	-5.0	
Current update		-1.9	-3.0	-3.0	-2.8	-3.0
Difference (pps)		4.2	1.7	1.9	2.2	
General Government gross debt (% of GDP)						
Previous update		26.6	30.7	33.8	37.1	
Current update		23.1	25.0	27.3	30.0	30.7
Difference (pps)		-3.5	-5.7	-6.5	-7.1	

Table 7: Long-term sustainability of public finances

% of GDP	2007	2010	2020	2030	2040	2050	2060	2070
Total expenditure	37.7	36.1	41.5					
Of which: age-related expenditures	15.0	17.3	18.9	19.0	17.9	18.0	18.4	18.4
Pension expenditures	7.4	9.3	9.2	10.4	9.2	9.0	9.3	9.6
Social security pension				10.2	8.9	8.8	9.0	9.3
Old-age and early pensions				7.9	7.0	7.1	7.5	7.6
Other pensions (disability, survivors)				2.3	1.9	1.7	1.5	1.7
Occupational pensions (if in general government)								
Health care	4.0	4.4	5.8	4.8	5.0	5.2	5.1	5.0
Long-term care								
Education expenditure	3.6	3.6	3.9	3.8	3.7	3.8	4.0	3.9
Other age-related expenditures								
Interest expenditure								
Total revenue	37.7	32.5	37.7					
Of which: property income								
Of which: from pensions contributions (or social contributions if appropriate)								
Pension reserve fund assets								
Of which: consolidated public pension fund assets (assets other than government bonds)								
Social contributions diverted to mandatory additional pension scheme[33]								
Pension expenditure paid by mandatory additional pension scheme[34]								
Labour productivity growth[35]	2.0	8.2	-0.5	2.6	2.4	2.2	1.7	1.2
Real GDP growth	6.7	1.6	-4.0	1.8	1.4	1.1	1.3	1.0
Participation rate, males (aged 20-64)	78.3	76.8	82.2	89.9	90.3	91.6	93.4	92.9
Participation rate, females (aged 20-64)	68.4	67.0	72.4	80.9	81.2	82.0	83.6	83.2
Participation rate, total (aged 20-64)	73.3	71.9	77.3	85.4	85.8	86.9	88.7	88.2
Unemployment rate (%, aged15-64)	6.9	10.3	5.2	4.4	4.9	4.9	4.9	4.9
Population aged 65+ over total population	17.8	18.2	21.6	25.1	28.4	32.4	34.9	33.2

33 Revenue from social security contributions or other revenue for the mandatory additional pension insurance, with which the accounts payable can be covered.

34 Pension expenditure or other social benefits paid by the mandatory additional pension insurance.

35 GDP (at 2015 prices) per employed person.

Table 7a: Contingent Liabilities

% of GDP	2024	2025
Government guaranteed debt	2.3	2.2
Of which: linked to the financial sector	1.2	3.4

Table 8: Basic assumptions

	2023	2024	2025	2026	2027
Short-term interest rate (annual average) 6-month LIBOR in EUR, %	3.14	3.53	2.57	2.36	2.27
Short-term interest rate (annual average) 6-month LIBOR in USD, %					
Long-term interest rate (annual average), %					
USD/EUR exchange rate (annual average)	1.0813	1.0846	1.0845	1.0845	1.0845
Nominal effective exchange rate. percentage change. previous year = 100[36]					
EUR/BGN exchange rate (annual average)	1.95583	1.95583	1.95583	1.95583	1.95583
World economy (excluding EU), GDP growth, %	3.1	3.1	3.2	3.1	3.1
EU GDP growth, %	0.4	1.0	1.7	1.9	1.7
Growth of relevant foreign markets. %					
World import volumes, excluding EU, %					
Crude Oil, Brent (USD/barrel)	82.6	81.3	75.8	72.7	70.8
International prices of non-energy commodities, %	-9.8	-1.8	-0.8	-1.0	-0.5
International prices of food products, %	-9.2	-9.0	-1.5	-1.6	-0.8
International prices of agricultural raw materials, %	-4.7	8.4	-0.4	-0.4	-0.4
International prices of metals, %	-9.6	-4.3	-0.3	-0.7	0.1

[36] The positive values reflect appreciation, the negative – depreciation.

9. ANNEX B

Table 1: Table of the RRF impact on programme's projections – GRANTS

Revenue from RRF grants (% of GDP)							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
RRF GRANTS as included in the revenue projections				0.32	0.98	1.25	1.63
Cash disbursements of RRF GRANTS from EU			1.60	0.00	1.44	1.66	1.35

Expenditure financed by RRF grants (% of GDP)							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Compensation of employees D.1				0.01	0.01	0.02	0.02
Intermediate consumption P.2				0.03	0.06	0.06	0.08
Social payments D.62+D.632							
Interest expenditure D.41							
Subsidies, payable D.3				0.01	0.05	0.06	0.18
Current transfers D.7							
TOTAL CURRENT EXPENDITURE				0.05	0.12	0.14	0.28
Gross fixed capital formation P.51g			0.02	0.27	0.86	1.12	1.35
Capital transfers D.9				0.01	0.11	0.23	0.27
TOTAL CAPITAL EXPENDITURE			0.02	0.27	0.97	1.34	1.62

Other costs financed by RRF grants (% of GDP)*							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Reduction in tax revenue							
Other costs with impact on revenue							
Financial transactions							

* This covers costs that are not recorded as expenditure in national accounts.
Bold: required information.

Table 2: Table on the RRF impact on programme's projections – LOANS

Cash flow from RRF loans projected in the programme (% of GDP)							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Disbursements of RRF LOANS from EU	0	0					
Repayments of RRF LOANS to EU							
Expenditure financed by RRF loans (% of GDP)							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Compensation of employees D.1							
Intermediate consumption P.2							
Social payments D.62+D.632							
Interest expenditure D.41							
Subsidies, payable D.3							
Current transfers D.7							
TOTAL CURRENT EXPENDITURE							
Gross fixed capital formation P.51g							
Capital transfers D.9							
TOTAL CAPITAL EXPENDITURE							
Other costs financed by RRF loans (% of GDP)[1]							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Reduction in tax revenue							
Other costs with impact on revenue							
Financial transactions							

* This covers costs that are not recorded as expenditure in national accounts.
Bold: required information.