FitchRatings

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Fitch Affirms Bulgaria at 'BBB'; Outlook Positive

Fitch Ratings - Frankfurt am Main - 11 Apr 2025: Fitch Ratings has affirmed Bulgaria's Long-Term Foreign-Currency Issuer Default Rating (IDR) at 'BBB' with a Positive Outlook.

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

Key Rating Drivers

Credit Fundamentals, Positive Outlook: Bulgaria's ratings are supported by its strong external and public finance balance sheets versus 'BBB' peers and credible policy framework, underpinned by EU membership and a long-standing currency board. This is balanced against low labour productivity and unfavourable demographics, which weigh on potential growth and government finances over the long term. There is a recent record of unstable coalition governments, which has affected reform implementation, and the perception of corruption is high. The Positive Outlook reflects the prospects for euro adoption, which would lead to further improvement in external metrics.

Euro Adoption: In February 2025, Bulgaria submitted a request to the European Commission and the ECB for an extraordinary convergence assessment after meeting all nominal Maastricht criteria, including the price stability criterion. The reports will likely be released in early June and, if the assessment is positive, allow the adoption of the euro from January 2026. Fitch does not expect significant difficulties with the formal approval, given strong political commitment at the EU level. Overall, we consider euro adoption as supportive of the rating.

Government Formation: Political parties GERB, BSP and TISP formed a minority government in January 2025, following the October 2024 snap elections (the seventh since 2021). The government's key objectives are euro adoption and implementation of necessary reforms under the Recovery and Resilience Facility (RRF). Longevity and stability of the coalition will be tested in the near term but successful eurozone entry and progress on RRF-linked reforms could support the government beyond end-2025.

Solid Economic Growth: Fitch has revised its 2025 growth forecast up to 3.1%, from 2.5% expected in October 2024, due to the stronger carry-over effect and improved domestic political situation. Strong nominal wage growth will continue to support private consumption. We remain cautious about the capacity and pace of reform implementation, but EU funds flows should increase and will support investment activity.

Planned maintenance works at oil and copper refineries will affect export performance, but we expect some positive spillovers from full Schengen entry as of January 2025. We forecast GDP growth at 2.8% in 2026, with upside risks related to euro adoption. Elevated trade uncertainty and global slowdown are the key downside risks to our forecast, mainly due to second-round effects, as direct trade exposure to the US is low.

Broadly Stable Inflation: HICP inflation inched up towards 4% at the beginning of 2025, following a low of 1.5% in September 2024, driven by changes in administered prices and withdrawal of lower VAT rates for certain products and services. We expect HICP inflation to average 3.9% in 2025, up from 2.6% in 2024, above the current peer median of 3%. The expected increase in inflation should not derail Bulgaria's eurozone entry. We expect inflation to ease to 3% in 2026. However, eurozone entry may accelerate price convergence to the EU average over the medium term.

Fiscal Deficits: Fitch estimates that the fiscal deficit widened to 2.8% of GDP in 2024, from 2% in 2023, on higher wage bill and social spending. We forecast the deficit at 2.7% in 2025 (versus 'BBB' median of 3.3%), reflecting further increase in public sector wages, deliveries of military equipment (0.5% of GDP) and some revenue-enhancing measures. We expect the deficit to narrow to 2.4% in 2026, above the government's target of 2.2%, due to our assumptions of higher defence spending and lower expected EU fund inflows.

Weak Fiscal Anchor: Bulgaria's fiscal position has weakened in recent years due to increased social spending, delays in reform implementation and a lack of credible medium-term fiscal planning. The new government adopted the updated medium-term budget forecast for 2025-2028, with a cash deficit of 3% of GDP planned in 2025-2026. Under the EU fiscal framework, the country is not obliged to implement any meaningful fiscal consolidation in 2025-2028, given its very low public debt level. The government is analysing the possibility of applying for the national escape clause under the Stability and Growth Pact to allow higher defence spending, further weakening the EU fiscal anchor.

Low Public Debt: Bulgaria's public debt ratio will remain very low compared with EU countries, and among the lowest in the 'BBB' category, despite the expected increase. We estimate public debt/GDP rose to 24.1% of GDP in 2024 and project it will reach 33.9% in 2029 due to plans to recapitalise certain state-owned enterprises in 2025 (3.3% of GDP), payment for military equipment in 2026 and Fitch's higher defence spending assumption over the medium term. General government interest payments will rise to 1.8% of revenue in 2026, from an estimated 1.2% in 2024, well below the 'BBB' median of 9.0% in 2026.

Strong External Finances: Fitch expects the current account deficit to widen to 2.4% of GDP in 2025 ('BBB' median: surplus of 0.4%) and to 2.9% in 2026, from 1.8% in 2024. We expect the capital account surplus to average 1.6% of GDP and net FDI inflows to remain below 1% in 2025-2026. Bulgaria's external position is supported by sizeable foreign reserves (9.1 months of current external payments in 2024). We project the net external creditor position to narrow to 28.1% of GDP in 2026, from 33.1% in 2024 (compared with the 'BBB' median of 0.5%), due to the expected increase in public sector external indebtedness.

Stable Banking Sector; Strong Credit Growth: The Bulgarian banking sector remains stable, with solid capitalisation (total capital ratio at 22.7% at end-2024) and improving asset quality. Loan growth increased across the major segments, with retail mortgage growth accelerating to 29.1% in 2024

(20.5% in 2023), partly driven by a methodology adjustment, robust consumer loan growth at 11.9% (12.3% in 2023) and resilient demand among corporates. The ratio of gross impaired loans decreased to 3.4% at end-2024, from 6.5% at end-2021, according to Fitch's estimates.

ESG - Governance: Bulgaria has an ESG Relevance Score of '5[+]' for both Political Stability and Rights and for the Rule of Law, Institutional and Regulatory Quality and Control of Corruption. These scores reflect the high weight that the World Bank Governance Indicators (WBGI) have in our proprietary Sovereign Rating Model (SRM). Bulgaria has a medium WBGI ranking at 56th percentile reflecting a history of unstable coalitions, relatively high perception of corruption and moderate institutional capacity versus a track record of peaceful transitions and above average regulatory quality.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/ Downgrade

- External Finances/ Structural: Lack of progress in eurozone accession due to renewed political instability or a failure in meeting convergence criteria.

- Macro/Structural: Weaker economic growth prospects, for example, as a result of adverse political developments that weigh on reform implementation.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

- External Finances: Further progress towards euro adoption, for example, through confirmation that Bulgaria has met convergence criteria and greater certainty regarding the likely timing of euro adoption.

- Macro: An improvement in growth potential, for example, via the implementation of structural and governance reforms to improve the business environment and/or effective use of EU funds.

Sovereign Rating Model (SRM) and Qualitative Overlay (QO)

Fitch's proprietary SRM assigns Bulgaria a score equivalent to a rating of 'BBB' on the Long-Term Foreign-Currency (LT FC) IDR scale.

Fitch's sovereign rating committee did not adjust the output from the SRM to arrive at the final LT FC IDR.

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

Country Ceiling

The Country Ceiling for Bulgaria is 'A-', two notches above the LTFC IDR. This reflects strong constraints and incentives, relative to the IDR, against capital or exchange controls being imposed that would prevent or significantly impede the private sector from converting local currency into foreign currency and transferring the proceeds to non-resident creditors to service debt payments.

Fitch's Country Ceiling Model produced a starting point uplift of +1 notch above the IDR. Fitch's rating committee applied a further +1 notch qualitative upward adjustment under the Long-Term Institutional Characteristics pillar, reflecting our view that trade and financial integration is stronger than the model outputs, supported by EU membership.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

Bulgaria has an ESG Relevance Score of '5[+]' for Political Stability and Rights as WBGIs have the highest weight in Fitch's SRM and are, therefore, highly relevant to the rating and a key rating driver with a high weight. As Bulgaria has a percentile rank above 50 for the respective governance indicator, this has a positive impact on the credit profile.

Bulgaria has an ESG Relevance Score of '5[+]' for Rule of Law, Institutional & Regulatory Quality and Control of Corruption as WBGIs have the highest weight in Fitch's SRM and are, therefore, highly relevant to the rating and are a key rating driver with a high weight. As Bulgaria has a percentile rank above 50 for the respective governance indicators, this has a positive impact on the credit profile.

Bulgaria has an ESG Relevance Score of '4[+]' for Human Rights and Political Freedoms as the Voice and Accountability pillar of the WBGIs is relevant to the rating and a rating driver. As Bulgaria has a percentile rank above 50 for the respective Governance Indicator, this has a positive impact on the credit profile.

Bulgaria has an ESG Relevance Score of '4[+]' for Creditor Rights as willingness to service and repay debt is relevant to the rating and is a rating driver for Bulgaria, as for all sovereigns. As Bulgaria has a track record of 20+ years without a restructuring of public debt as captured in our SRM variable, this has a positive impact on the credit profile.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/topics/esg/products#esg-relevance-scores.

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Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
Bulgaria	LT IDR	BBB ⊕	Affirmed		BBB ⊕
	ST IDR	F2	Affirmed		F2
	LC LT IDR	BBB ⊕	Affirmed		BBB ⊕
	LC ST IDR	F2	Affirmed		F2
	Country Ceiling	A-	Affirmed		A-
• senior unsecured	LT	BBB	Affirmed		BBB

ENTITY/DEBT	RATING			RECOVERY	PRIOR
• Senior Unsecured-Local currency	LT	BBB	Affirmed		BBB

RATINGS KEY	OUTLOOK	WATCH
POSITIVE		
NEGATIVE		
EVOLVING		
STABLE		

Applicable Criteria

Country Ceiling Criteria (pub.24 Jul 2023)

Sovereign Rating Criteria (pub.24 Oct 2024) (including rating assumption sensitivity)

Applicable Models

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Country Ceiling Model, v2.0.3 (1)

Debt Dynamics Model, v1.3.2 (1)

Macro-Prudential Indicator Model, v1.5.0 (1)

Sovereign Rating Model, v3.14.2 (1)

Additional Disclosures

Solicitation Status

Endorsement Status

Bulgaria	EU Issued, UK Endorsed

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Endorsement policy