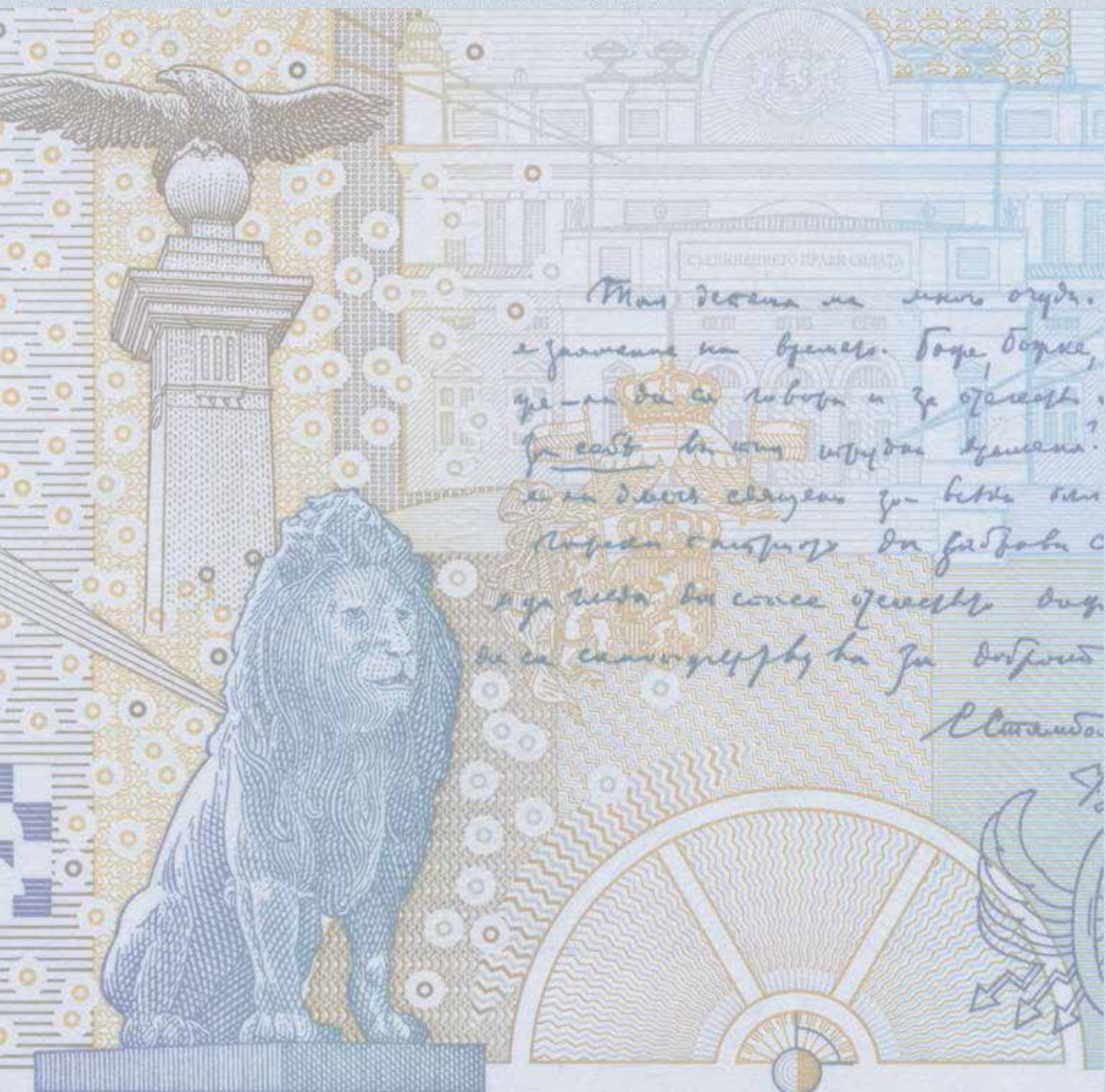


BULGARIAN NATIONAL BANK



ECONOMIC REVIEW

2/2021



ECONOMIC REVIEW

2/2021



BULGARIAN NATIONAL BANK

The BNB quarterly Economic Review presents information and analysis of balance of payments dynamics, monetary and credit aggregates, their link with the development of the real economy, and their bearing on price stability. External environment developments are also analysed since they directly affect the Bulgarian economy. The Review contains quantitative assessments of short-run developments in major macroeconomic indicators like inflation, economic growth, exports, imports, trade balance and the balance of payments current account, foreign direct investment, monetary and credit aggregates dynamics. Given the magnitude of the economic shock from the spread of COVID-19, the charts in this issue cover the period from the start of 2008, which allows to compare the changes in economic variables during the global financial and economic crisis of 2008–2009.

The Economic Review, issue 1/2021 was presented to the BNB Governing Council at its 14 May 2021 meeting. It employs statistical data published up to 19 April 2021. Expectations of economic trends in Bulgaria in the short term (until the third quarter of 2021), as described in this document, are based on the BNB macroeconomic forecast prepared as of 26 March 2021. These expectations are founded on the assumption that the measures imposed in the fourth quarter of 2020 to contain the spread of COVID-19 in other EU countries and Bulgaria would be extended until the end of the second quarter of 2021. The estimates and projections published in this issue should not be regarded as advice or recommendation. Exclusively the information user is liable for any consequences thereof.

The Economic Review is available on the BNB website, Research and Publications menu, Periodical Publications sub-menu. Please address notes, comments and suggestions to the BNB Economic Research and Projections Directorate at 1000 Sofia, 1, Knyaz Alexander I Square.

© Bulgarian National Bank, 2021

1, Knyaz Alexander I Square
1000 Sofia, Bulgaria

Tel.: (+359 2) 9145-1351, 1209, 1806, 1227

Website: www.bnb.bg

This issue includes materials and data received up to
9 August 2021.

The contents of the BNB Economic Review may be quoted
or reproduced without further permission.
Due acknowledgement is requested.

ISSN 2367 – 4962 (online)

CONTENT

SUMMARY	7
1. EXTERNAL ENVIRONMENT	9
Current Business Situation	9
International Commodity Prices	18
2. FINANCIAL FLOWS, MONEY AND CREDIT	20
External Financial Flows	20
Monetary and Credit Aggregates	24
Interest Rates	30
Financial Flows between the Consolidated Budget and Other Sectors of the Economy	33
3. ECONOMIC ACTIVITY	36
Current Economic Environment	36
Exports and Imports of Goods and Services	41
Behaviour of Firms and Competitiveness	45
Household Behaviour	51
Fiscal Policy Effects on the Economy	54
4. INFLATION	61

Charts

Global PMIs	9	Foreign Currency Purchases and Sales between the BNB and Banks (on a Monthly Basis)	26
Global Industrial Production.....	10	Annual Growth of Credit to Non-financial Corporations and Contributions of Individual Types of Loans	26
World Trade.....	10	New Loans to Non-financial Corporations (Monthly Volumes).....	27
Inflation Measured through CPI.....	10	Annual Growth of Household Credit and Contributions of Individual Types of Loans	27
Contribution to the Change in Real GDP in the United States by Component	11	New Loans to Households (Monthly Volumes)	28
US ISM-PMIs.....	11	Changes in Credit Standards.....	28
US Consumer Confidence Indices.....	12	Changes in Credit Demand	28
US Unemployment Rate and a Monthly Change in Number of New Employees in the US Non-Farm Sector	12	Overnight Interbank Money Market Rates (Average Monthly Value)	30
US Inflation Rate	12	Interest Rates on New Time Deposits	30
Manufacturing and Services PMIs and Change in China's Real GDP.....	13	Interest Rates on New Loans to Non-financial Corporations by Currency.....	31
China's Inflation Rate	14	Interest Rates and APRC on New Household Loans.....	31
Minimum Required Reserve Rates in China.....	14	Interest Rates on New Corporate and New Housing Loans: the Spread between Bulgaria and the Euro Area	31
Contribution to the Change in Real GDP in the Euro Area by Component	14	Long-term Interest Rates in the Primary and Secondary Markets of Government Securities	32
Contribution to the Change in Real GDP in the Euro Area by Country	15	Reference Government Securities Yield Curve in Bulgaria.....	32
PMIs in the Euro Area	15	Consolidated Budget Effect on Other Sectors' Liquidity (Monthly).....	33
Euro Area Unemployment Rate and Employment Growth.....	16	Contribution to GDP Growth by Final Use Component	36
Euro Area Inflation Rate	16	Business Climate and Consumer Confidence.....	37
Interest Rates of the ECB, EONIA, €STR and Excess Liquidity in the Euro Area Banking System	17	Business Climate Dynamics Indicator.....	37
EURIBOR Dynamics	17	Expectations about Future Economic Activity	38
Brent Crude Oil Price.....	18	Factors Hampering Activities of Corporations	38
Brent Crude Oil Futures Prices	18	Uncertainty Indicator in the Economy (Corporations and Households)	39
Price Indices of Major Raw Materials and Commodity Groups.....	19	Production Assured with Orders from Other Countries and Finished Goods Inventories	39
Current and Capital Account Flow Dynamics and Contributions of Individual Components	20	Dynamics of the Production Index in Industry, Construction and Services in 2020	39
Financial Account Flow Dynamics and Contributions of Individual Components.....	22	Dynamics of Nominal Exports and Imports of Goods	41
Direct Investment Liabilities by Type of Investment.....	23	Exports of Commodity Groups by Use.....	42
FDI by Sector as of the End of the Fourth Quarter of 2020	23	Exports of Goods: Geographical Breakdown.....	42
Gross External Debt	24	Imports of Commodity Groups by Use.....	43
Annual Growth of Non-government Sector Deposits and Contribution by Sector	24	Imports of Goods: Geographical Breakdown.....	44
Reserve Money	25	Dynamics of Exports and Imports of Services	44
Bank Deposits with the BNB	25	Annual Change of Services Exports and Contribution by Sub-component	44
Currency in Circulation	25	Annual Change of Services Imports and Contribution by Sub-component	45

Rate of Change in Real Value Added and Contribution by Sub-sector	45
Manufacturing Turnover Dynamics.....	46
Construction Production Dynamics and New Buildings Permits Issued	46
Services Value Added Rate of Change and Contribution by Sub-sector	46
Measures Taken by the Firms in Relation to Their Staff in April, December 2020 and February 2021	47
Changes in Firms' Revenue from Sales in April, December 2020 and February 2021	47
Contribution to Changes in the Number of Employed by Economic Sector.....	47
Changes in the Number of Unemployed Persons	48
Labour Productivity Dynamics (Value Added <i>per Employee</i>).....	48
Compensation <i>per Employee</i> at Current Prices	48
Unit Labour Costs	48
Gross Operating Surplus at Current Prices	49
Financing Sources	49
Contribution of the Change in Production Factors to GDP Growth.....	49
Contribution to the Change in Labour Force by Component	51
Economic Activity and Share of Discouraged Persons	51
Unemployment Rate	51
Employment and Nominal Wage Bill	52
Private Consumption and Consumer Confidence	52
Retail Trade Turnover	52
Household Propensity to Save (on a Quarterly Basis).....	52
Contributions of Major Groups of Revenue to Growth in Total Revenue and Grants, Cumulatively (on an Annual Basis).....	55
Contributions of Major Tax Groups to Tax Revenue Growth, Cumulatively (on an Annual Basis)	56
Contributions of Major Groups of Expenditure to Total Budget Expenditure Growth, Cumulatively (on an Annual Basis).....	57
Inflation and Contribution of Major Commodity and Services Groups to It	61
Annual Rate of Change in Brent Crude Oil and A95 Petrol Prices	62
Rate of Change of Food Price Index	62
Contribution of Major Sub-groups of Unprocessed Food to Overall Inflation	62

Contribution of Major Sub-groups of Processed Food to Overall Inflation	62
Core Inflation.....	63
Contribution of Inflation in Services and Major Services Sub-groups to Overall Inflation	63
Contribution of Inflation in Non-food Goods (Excluding Energy Products) and Major Services Sub-groups to Overall Inflation	63
Contribution of Tobacco Products and Major Sub-groups of Goods with Administratively Controlled Prices to Overall Inflation	64
Rate of Change in PPI on the Domestic Market and Contributions by Major Sub-sector	64
Rate of Change in Producer Prices on the Domestic Market by Major Industrial Groupings.....	64
Expectations of Selling Prices in Industry, Retail Trade and Services in the Following Three Months	64
Rate of Change of House Price Index.....	65
Actual and Equilibrium House Prices.....	65
Price-to-Rent Ratio (Percentage Deviation from Long-term Average Value)	66

Tables

Projections of the Annual Rate of Change of Euro Area Real GDP	17
Projections of Euro Area Annual Inflation Rate	17
Flows on Major Balance of Payments Accounts	21
Gross External Debt as of April 2021	24
Real GDP Growth by Final Use Component.....	40
Real GDP Growth by Final Use Component.....	40
Exports by Commodity Group, January–March 2021	42
Imports of Commodity Groups by Use, January–March 2021	43
Gross Value Added Change	50
Gross Value Added Change	50
Employment and Income Dynamics.....	53
Employment and Income Dynamics.....	53
Retail Trade Turnover	53
Retail Trade Turnover	54
Key Budget Indicators Performance for 2020 and 2021	59
Rates of Change in Commodities and Services Prices and Their Contribution to Inflation	66
Key Indicators of the Housing Market in Bulgaria	67

ABBREVIATIONS

ABSPP	Asset-Backed Securities Purchase Programme
APP	Asset Purchase Programme
APRC	Annual percentage rate of charge
BDB	Bulgarian Development Bank
BIR	Base interest rate
BOP	Balance of Payments
BTC	Bulgarian Telecommunications Company
b.p.	basis points
CBPP3	Covered Bond Purchase Programme
CEECs	Central and East European countries
CEFTA	Central European Free Trade Association
CFP	Consolidated Fiscal Programme
CIF	Cost, insurance, freight
CNY	Chinese Yuan
CPI	Consumer Price Index
DXY	an index measuring the exchange rate of the US dollar against the basket of six major currencies
EA	Employment Agency
EC	European Commission
ECB	European Central Bank
EIB	European Investment Bank
EMBI	Emerging Markets Bond Index
EONIA	Euro OverNight Index Average
ESA 2010	European System of National and Regional Accounts
EU	European Union
EURIBOR	Euro Interbank Offered Rate
EWRC	Energy and Water Regulatory Commission
FDI	Foreign Direct Investment
FOB	Free on Board
FRS	Federal Reserve System
GDP	Gross Domestic Product
GFMS	Gold Fields Mineral Services
HICP	Harmonized Index of Consumer Prices
HRW	Hard Red Wheat
HUF	Hungarian forint
IEA	International Energy Agency
IMF	International Monetary Fund
ISM	Institute for Supply Management
LEONIA	LEv OverNight Index Average
LIBOR	London Interbank Offered Rate
M1	narrow money
M2	M1 and quasi-money
M3	broad money
MF	Ministry of Finance
MFIs	Monetary Financial Institutions
mt	metric tons
NPISHs	Non-profit institutions serving households
NSI	National Statistical Institute
OPEC	Organization of Petroleum Exporting Countries
OTC	over-the-counter
PBoC	People's Bank of China
PEPP	Pandemic Emergency Purchase Programme
PELTRO	Pandemic Emergency Longer-Term Refinancing Operations
PMI	Purchasing Managers' Index
p.p.	percentage points
PPP	Purchasing Power Parity
PSPP	Public Sector Purchase Programme
RON	Romanian new leu
SITC	Standard International Trade Classification
WTI	West Texas Intermediate
€STR	Euro Short-Term Rate

SUMMARY

In the second quarter of 2021 global PMIs increased significantly, reflecting the lower economic uncertainty amid decreasing COVID-19 cases and progress in vaccinations, especially in developed countries. The pace of recovery continued to diverge across regions, with PMIs signalling acceleration of economic growth in developed economies and moderation in developing market countries. Global inflation rose significantly in the second quarter of 2021, reflecting both low base effects of 2020 and robust growth in demand for industrial goods and raw materials after the phase-out of anti-epidemic measures accompanied by serious disturbances in global supply chains. Over the period, the central banks of the US and the euro area left unchanged their accommodative monetary policies, providing favourable financing conditions for achieving a sustainable economic recovery after the health crisis caused by the COVID-19 spread. Both central banks continued to assess the reported acceleration of inflation as a transitory phenomenon, requiring no changes in their monetary policy stance. In line with the international environment and developments in Bulgaria's main trading partners, external demand for Bulgarian goods and services is expected to post significant year-on-year growth in the third and fourth quarters of 2021, with 2020 low base effects contributing essentially to this dynamics. The forecast is based on the assumption that the containment measures imposed in Bulgaria and other EU Member States will be phased out in the second half of 2021.

In the first four months of 2021 the total current and capital account surplus of Bulgaria decreased from the same period of 2020, reflecting mainly a higher deficit on the trade balance and decreased net revenue from travel and transport services. In the second half of 2021 the positive current and capital account balance is expected to increase on an annual basis from the end of 2020, driven mainly by a projected rise in net revenue from travel and transport services under an assumption of a phase-out of COVID-19 containment measures.

Over the first five months of 2021 the annual growth of non-government sector's deposits accelerated from the end of 2020 under the influence of still deferred household consumption of some goods and services, limited investment activity of corporations and maintenance of precautionary savings amid a persistent uncertainty surrounding the COVID-19 pandemic development. Since March the growth rate of credit to the private sector has gradually accelerated, more pronounced in the sector of households.

In the second half of the year the growth in deposits of the non-government sector is expected to slow down slightly in line with a projected gradual rise in economic activity and private consumption. Projected domestic demand growth, still low lending rates and positive housing market prospects will favour the growth of credit to the private sector over the projection horizon.

In the first quarter of 2021 the real GDP growth rate in Bulgaria accelerated to 2.5 per cent on a quarterly basis despite the extension of containment measures that were introduced at the end of 2020. Net exports and private consumption contributed most strongly to economic growth over the review period. The positive contribution of net exports was driven by services trade, where exports of services posted growth, and imports of services reported a fall, while private consumption growth was in line with increased real income of households, reflecting higher wages and net government transfers. Despite the growth rate of economic activity, employment declined by -0.7 per cent on a quarterly basis, because of a decrease of self-employed workers in agriculture. Employment in other sectors posted an increase. In the second quarter of 2021 short-term economic indicators in Bulgaria signalled continuous growth in the economic activity in line with easing of certain anti-epidemic measures in Bulgaria. Assuming a phase-out of all containment measures in Bulgaria and Bulgaria's major trading partners, in the second half of the year real GDP is expected to grow compared with the first half of the year. This will be accompanied by a certain weakening of the role of fiscal policy due to the assumption of a phase-out of some government anti-crisis measures related to the COVID-19 pandemic.

In June 2021 the annual inflation slightly accelerated compared to the end of 2020, reaching 2.4 per cent. This reflected mainly the higher prices of energy products as a result of the strong hike of international oil prices on an annual basis. Core inflation also accelerated from the end of the previous year amid easing of containment measures against COVID-19 and growth in final consumption expenditure of households. Concurrently, inflation in the food group slowed down somewhat from end-2020 due mainly to lower prices of unprocessed food. Administratively controlled prices continued to contribute positively to overall inflation driven by indirect effects of higher international natural gas prices. In the third and fourth quarters of 2021 the gradual acceleration of inflation is expected to be sustained, reflecting mostly the assumptions of upward developments in international food and petroleum product prices over this period compared with end-2020.

1. EXTERNAL ENVIRONMENT

In the second quarter of 2021 global PMIs increased significantly, reflecting the lower economic uncertainty amid decreasing COVID-19 cases and progress in vaccinations, especially in developed countries. The economic recovery was more pronounced in the services sector, while more moderate growth in industry was due to the deepening disturbances in global supply chains. The pace of recovery continued to diverge across regions, with PMIs signalling acceleration of economic growth in developed economies and moderation in developing market countries. Global inflation rose significantly in the second quarter of 2021, reflecting both low base effects of 2020 and robust growth in demand for industrial goods and raw materials after the phase-out of anti-epidemic measures accompanied by serious disturbances in global supply chains. Over the period, the central banks of the US and the euro area left unchanged their accommodative monetary policies, providing favourable financing conditions for governments, firms and households to achieve a sustainable economic recovery after the health crisis caused by the COVID-19. Both central banks continued to assess the reported acceleration of inflation as a transitory phenomenon, requiring no changes in their monetary policy stance.

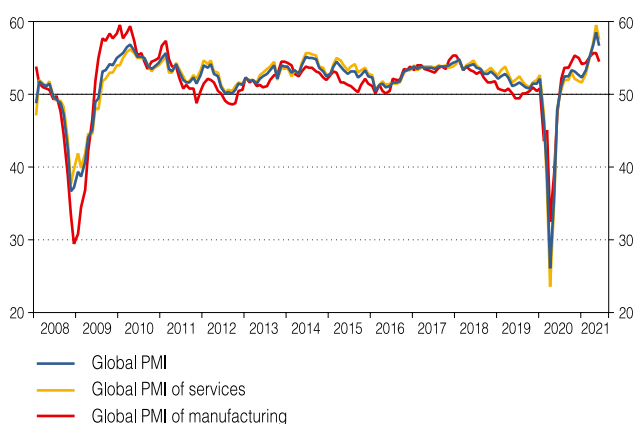
In line with the international environment and developments in Bulgaria's main trading partners, external demand for Bulgarian goods and services is expected to post significant year-on-year growth in the third and fourth quarters of 2021, with 2020 low base effects contributing essentially to this dynamics. The forecast is based on the assumption that the containment measures imposed in Bulgaria and other EU Member States will be phased out in the second half of 2021.

Current Business Situation

In the second quarter of 2021 global PMI dynamics indicated an accelerated recovery of the global economic activity. The PMI level increased significantly from the average values observed in the first quarter of 2021, reaching in May its highest value since 2006: 58.5 points. A higher economic recovery rate was reported in developed market economies, including the US and euro area Member States. In developing markets, the average value of the global PMI was also above the neutral 50 point limit, though recording a significantly smaller rise compared to the first quarter of 2021. Lower growth in developing market economies was mainly due to China and India, with the composite PMI in India declining below the neutral 50 point limit during the second quarter of 2021 as a result of the negative COVID-19 developments in the country.

Across economic sectors, PMIs in the second quarter of 2021 suggested a substantial recovery of the global economic activity in the services sector. Growth in industry was more moderate, with a significantly increased time of delivery in manufacturing due to difficulties in global supply chains, which contributed to higher commodity and producer prices.

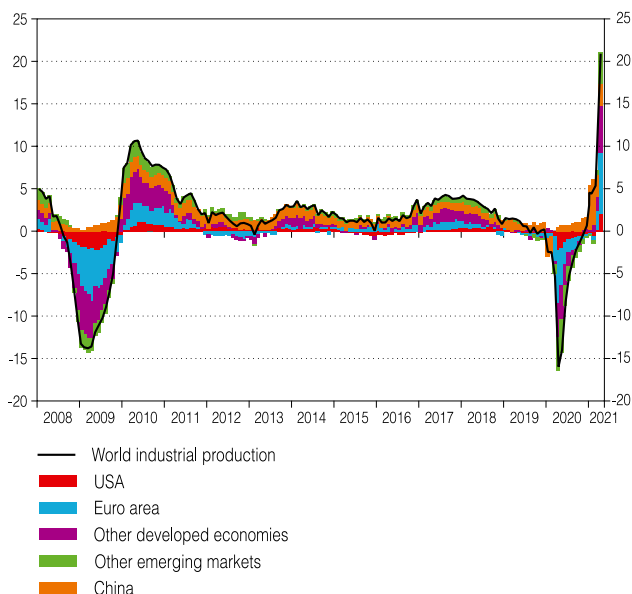
Global PMIs



Source: JP Morgan.

Global Industrial Production

(annual rate of volume change and contribution by region, per cent)



Source: CPB Netherlands Bureau for Economic Policy Analysis.

Between January and April 2021, a very large acceleration in the annual growth rate of world industrial output and world trade was reported,¹ reflecting largely the low base effect from the same period of 2020. This effect was more pronounced in April in all countries, excluding China which faced the first coronavirus wave in early 2020.

Over the second quarter of 2021 global inflation² accelerated significantly in both developed and emerging market economies. This acceleration was mainly due to the 2020 low base effect in energy prices, although core inflation has also increased somewhat. Deepening of disturbances in global supply chains were also a driving factor for price rises. Preliminary World Bank estimates show that global inflation as of June was 2.8 per cent on an annual basis, from 1.8 per cent in March 2021.

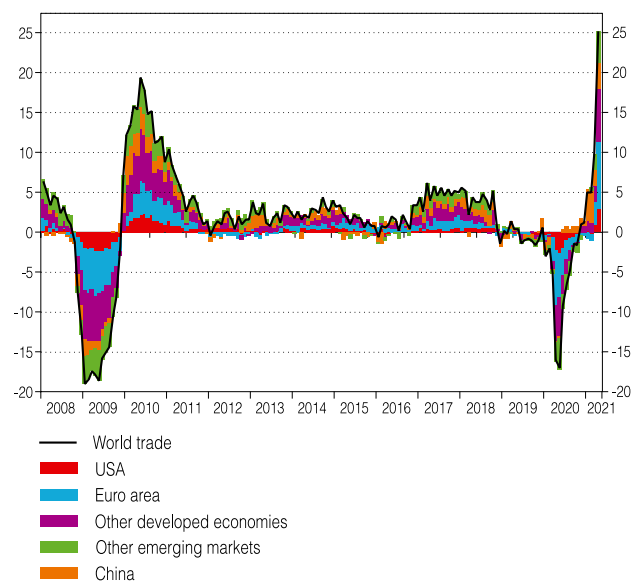
In the third and fourth quarters of 2021 external demand for Bulgarian goods and services is expected to grow considerably on an annual basis in line with indications of the international environment and the low base effect in 2020. This forecast is based on the assumption that the containment measures imposed in the fourth quarter of 2020 in other EU Member States and Bulgaria would be phased out in the second half of 2021.

¹ Based on CPB Netherlands Bureau for Economic Policy Analysis data as of 24 June 2021.

² Based on the World Bank data as of 16 July 2021.

World Trade

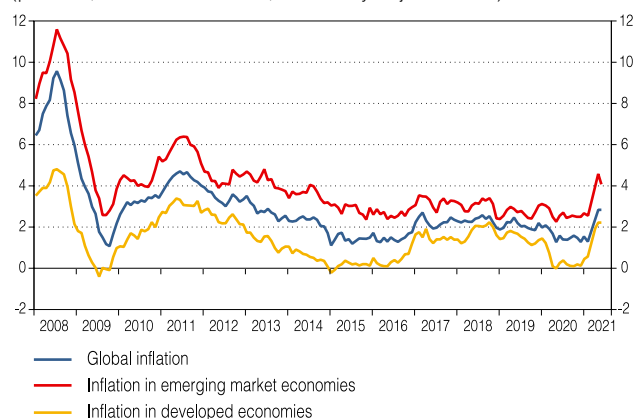
(annual rate of volume change and contribution by region, per cent)



Source: CPB Netherlands Bureau for Economic Policy Analysis.

Inflation Measured through CPI

(per cent, on an annual basis, seasonally adjusted data)



Notes: The World Bank measures the change of CPI in individual groups as a weighted average of CPI changes in the countries of the group. Real GDP based on purchasing power parity is used to calculate country weights. Groups include only World Bank Member States classified by the World Bank as emerging market economies and developed economies.

Source: the World Bank.

The United States

In the first quarter of 2021 US GDP growth accelerated to 1.6 per cent on a quarterly basis against 1.1 per cent in the fourth quarter of 2020, reflecting mainly growing household consumption and resumed growth in federal government consumption and investment. In the first quarter of 2021 business investment growth slowed down, while inventories posted quarter-on-quarter declines. Over the review quarter net exports continued to contribute negatively to real GDP growth.

Large-scale fiscal policy measures³ adopted in December 2020 and March 2021 were the major factor behind the higher household consumption. In Congressional Budget Office's forecasts, the federal budget deficit for the fiscal 2020 year⁴ will reach 13.4 per cent of GDP, making it the second largest since 1945.

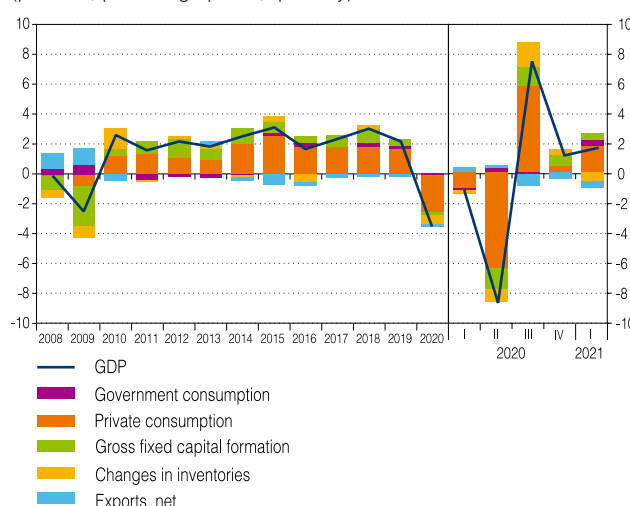
In the second quarter of 2021 leading economic indicators of the US economy witnessed tentative developments: though remaining historically high, by end-period most of them were lower than at the end of the first quarter. In June 2021 the ISM Manufacturing PMI fell to 60.6 points compared to 61.2 points in May and 61.4 points on average in the first quarter of this year. ISM-PMI services index decreased to 60.1 points against 64.0 points in May, which was its highest historical value. The average value of the indicator in the second quarter was 62.3 points against 59.2 points on average in the previous quarter. Labour and raw material shortage is probably the reason for the moderate deceleration in economic activity growth both in manufacturing and services at the end of the second quarter. Consumer confidence indicators showed mostly positive movements in the second quarter of 2021, remaining, however, below their pre-crisis

³ The new US government's Build Back Better Plan is a projected three-package fiscal stimulus, worth USD 7 trillion. The first USD 1.9 trillion package, called American Rescue Plan Act of 2021, passed by the US Congress on 10 March 2021 and included expenditure to counter the pandemic and direct financial support to households, small businesses and communities significantly affected by the pandemic. The second package, known as American Jobs Plan, is in the process of adoption by July 2021 and provides for infrastructure investments of USD 2.3 trillion. The third package, American Families Plan, envisages a number of packages in order to support households in spending on childcare, education and healthcare. Fiscal expenses on the second and third packages are projected to be funded by tax increases under the Made in America Tax Plan.

⁴ Fiscal years in the United States run from 1 October of the previous year to 30 September of the reference year.

Contribution to the Change in Real GDP in the United States by Component

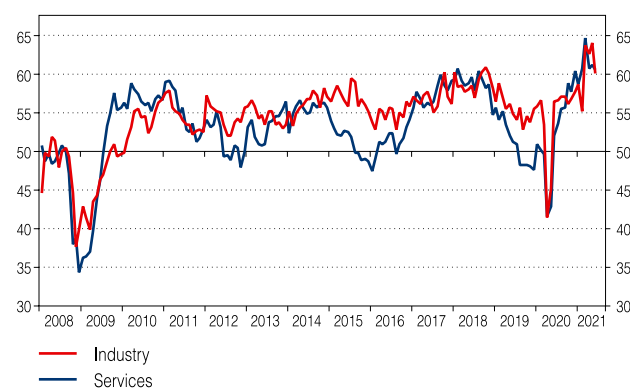
(per cent, percentage points; quarterly)



Source: Bureau of Economic Analysis.

US ISM-PMIs

(per cent)



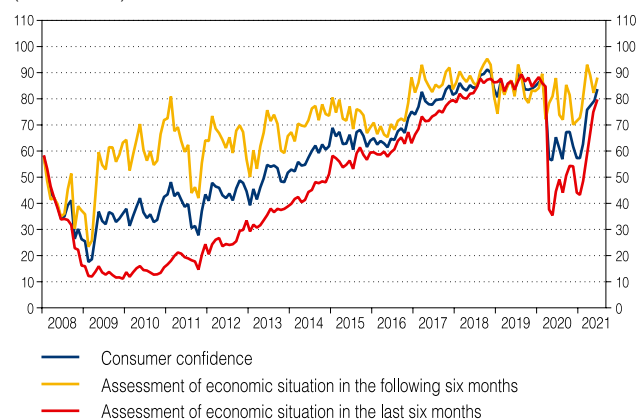
Sources: Institute for Supply Management, Bureau of Economic Analysis.

level driven by the COVID-19 pandemic. In the second quarter of 2021, US labour market conditions improved further, remaining, however, significantly worse than their pre-pandemic status. Over the review period total employment in the US non-agricultural sector rose by 1.7 million jobs against an increase by around 1.6 million jobs over the first quarter 2021. In June the unemployment rate went down slightly to 5.9 per cent, from 6.0 per cent at the end of the first quarter. The US participation rate rose to 61.6 per cent by June against 61.5 per cent at the end of the first quarter of 2021. Overall, data available in July 2021 indicated a slowdown in quarterly growth of real GDP over the second quarter of 2021.

Over the second quarter of 2021 US inflation increased significantly, the annual rate of change in the price index of personal consumer expenditure (PCE) observed by the Federal Reserve exceeding the target of 2 per cent. In May the annual rate of change in this index was 3.9 per cent against an average of 1.8 per cent in the first quarter of 2021. However, part of this growth was driven by the base effect in 2020 when a large decline in most goods was reported due to demand contraction as a result of the COVID-19 pandemic. Another substantial part of the increase reflected mainly the pass-through of oil price increases in consumer prices of energy products. Beside the effects referred to above, consumer prices rose due to higher demand in the process of a recovery of economy's normal functioning accompanied by considerable difficulties in supply of certain goods. The annual growth rate of the core personal consumption expenditure price index (PCE), excluding food and fuel, reached 3.4 per cent in May, from 1.6 per cent on average in the first quarter of 2021. June CPI data (the other key US inflation indicator) also showed an accelerated annual rate of inflation to 5.4 per cent compared to 1.9 per cent on average in the first quarter. The annual growth rate of the core CPI index, excluding food and fuel, accelerated to 4.5 per cent in June, from 1.4 per cent on average in the first quarter. The significant increase of the core CPI index over the second quarter of 2021 was mainly driven by price rises in automobiles (second hand), hotel services, car rentals, air tickets, clothing and vehicle insurance.

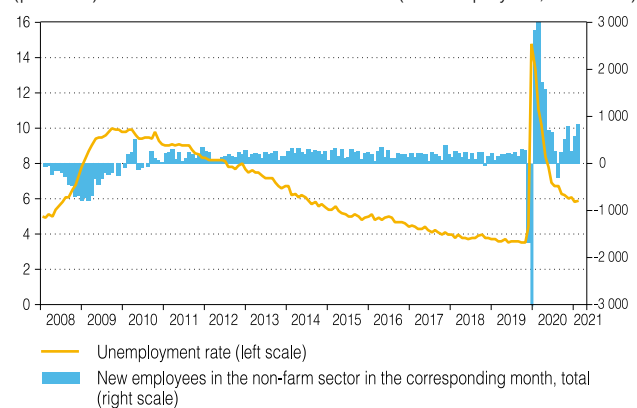
US Consumer Confidence Indices

(2000 = 100)



Source: The Conference Board.

US Unemployment Rate and a Monthly Change in Number of New Employees in the US Non-Farm Sector

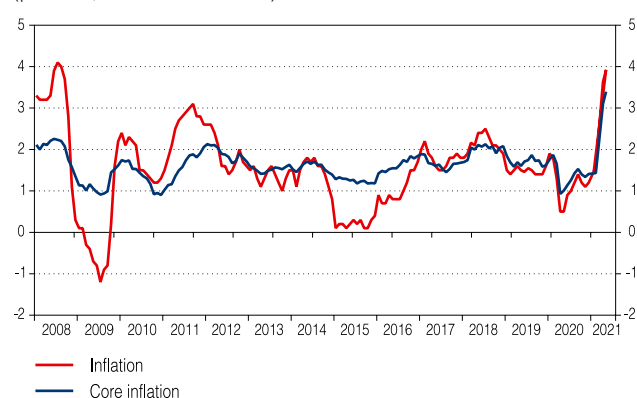


Notes: The values of monthly changes in the number of new employees in the non-farm sector for April and June 2020 are not evident in the chart, coming to -20.7 and 4.8 million employees.

Source: Bureau of Labour Statistics.

US Inflation Rate

(per cent, on an annual basis)



Notes: Inflation is measured by personal consumption expenditure index. Core inflation is measured by personal consumption expenditure index, excluding food and energy expenditure.

Source: Bureau of Economic Analysis.

In the second quarter of 2021, the US Federal Open Market Committee (FOMC) maintained its target range for the federal funds rate at 0.00–0.25 per cent and continued to implement its asset purchase programme. Concurrently, the Committee's discussions on the future process of reducing the asset purchase programme were launched. In addition, the FOMC decided to raise the interest rates on required reserves and banks' excess reserves by 5 basis points each to 0.15 per cent.

At the June meeting a significant strengthening of confidence among FOMC members in the resilience of the economic recovery and positive economic effect of the US vaccination programme was reported. Members' individual forecasts were revised upwards, with the strongest revision made to the expectations for 2021, while changes in projections for 2022 and 2023 were relatively minor. Expectations about the process of monetary policy normalisation were also revised. The median of members' individual forecasts for the level of federal funds rate showed an expected first rise by 50 basis points in 2023⁵. FOMC long-term equilibrium value assessments of all economic indicators were left unchanged, including the long-run equilibrium level of federal funds rate (2.5 per cent).

In the second quarter of 2021 total assets in the US Federal Reserve balance sheet rose by USD 390 billion⁶ to USD 8.08 trillion (38.6 per cent of GDP in 2020).

China

In the second quarter of 2021 the real GDP growth rate in China accelerated to 1.3 per cent on a quarterly basis, from 0.4 per cent in the first quarter.

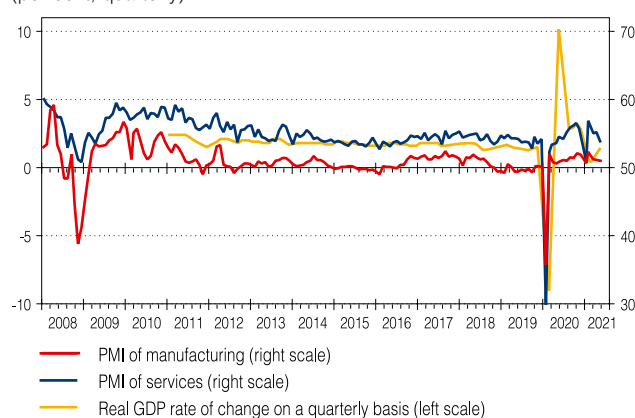
In the second quarter of 2021 PMIs went up on the first quarter of the year, though reporting a downward dynamics in May and June and signalling an economic activity slowdown in both industrial production and services sectors. Growth deceleration in manufacturing in May and June was largely attributable to the decline in current production due to disturbances in the supply of some high technology components, such as chips, higher prices and interruptions

⁵ In March 2021 the median of FOMC members' individual forecasts did not indicate an increase until 2024 inclusive.

⁶ Referred to as the US dollar below.

Manufacturing and Services PMIs and Change in China's Real GDP

(per cent, quarterly)



Sources: National Bureau of Statistics of China and China Federation of Logistics and Purchasing.

in electricity and coal supply in several Chinese regions. PMI indices suggested a stronger decline in services than in industry due to the strong increase in COVID-19 cases in some south provinces of China and subsequent local anti-epidemic measures.

In the second quarter of 2021 inflation in China accelerated to 1.1 per cent on an annual basis in June from 0.4 per cent in March 2021. This increase was mainly driven by price rises in non-food goods and services, while food prices reported a deflation. Concurrently, production price inflation in the second quarter accelerated further, reaching 8.8 per cent on an annual basis in June against 4.4 per cent in March. The accelerated growth rate of producer prices reflected surging commodity prices due to a rapid economic recovery both in China and globally.

In the second quarter of 2021 the People's Bank of China did not initiate new monetary policy measures, but in early July it cut minimum required reserve rates of commercial banks⁷ by 50 basis points, which is expected to release liquidity of approximately CNY 1 trillion. A portion of the released liquidity would be used for refinancing medium-term operations of commercial banks to the central bank maturing over the next months. The central bank announced it would develop policies in support of micro-, small- and medium-sized enterprises with a view to expenditure increases related to higher commodity prices.

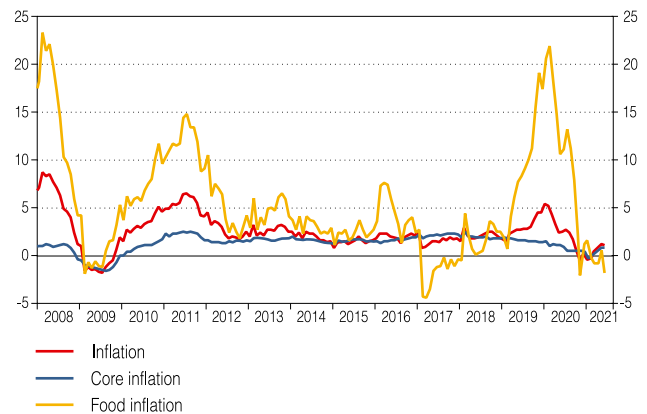
Euro Area

The imposed anti-epidemic measures in relation to the increase in COVID-19 cases in Europe in the first quarter of 2021 were the main factor behind the 0.3 per cent decline in euro area real GDP on a quarterly basis over the period under review. As in the previous quarter, the quarterly GDP decline was largely driven by weaker private consumption, which was partly offset by the positive contribution of changes in inventories and investment. The four largest euro area economies reported divergent changes in real GDP on a quarterly basis: a strong decline in Germany and weaker in France and Spain, and slight growth in Italy.

⁷ Excluding those that already had a rate of 5.0 per cent (mainly micro-, small-, regional, municipal and other banks).

China's Inflation Rate

(per cent, on an annual basis)

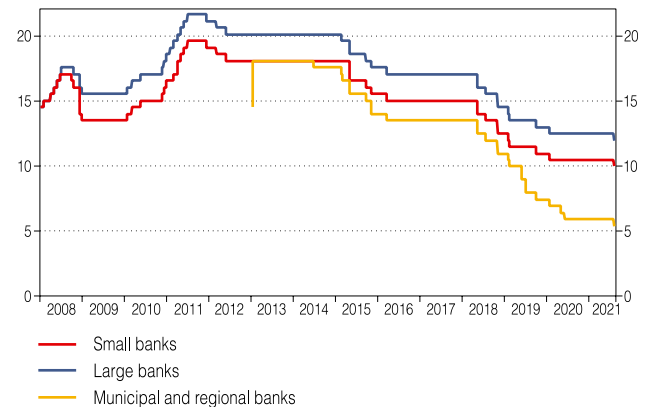


Notes: Inflation is measured by consumer price index. Core inflation is measured by consumer price index, excluding food and energy expenditure.

Source: National Bureau of Statistics of China.

Minimum Required Reserve Rates in China

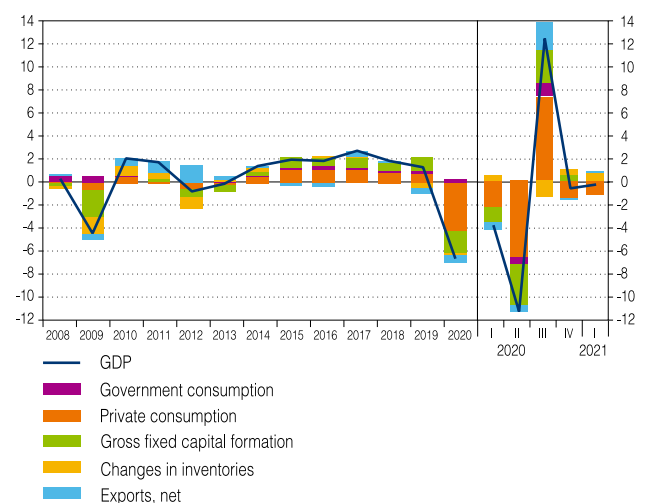
(per cent)



Source: the PBoC.

Contribution to the Change in Real GDP in the Euro Area by Component

(per cent, percentage points; quarterly)



Source: Eurostat.

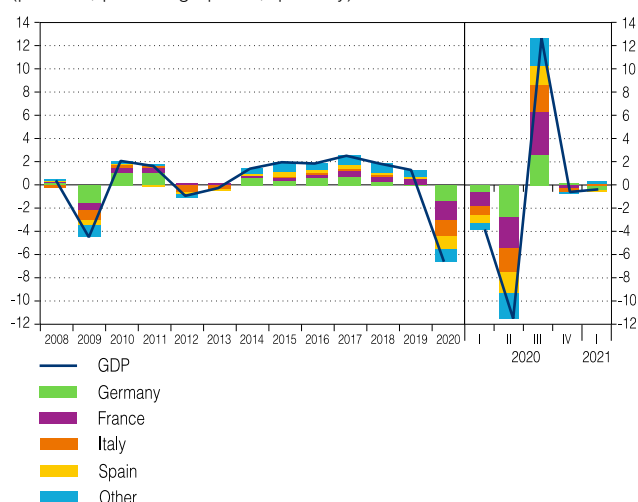
Euro area economic indicators rose significantly in the second quarter of 2021, reaching very high historical levels. In June 2021 the composite PMI in the euro area was 59.5 points (the highest value since June 2006), signalling significant growth in the economic activity both in manufacturing and services. This reflected the increased demand and firms' positive expectations to overcome the COVID-19 health crisis, given the progress of the vaccination process in Europe. In June manufacturing PMI reached its highest value since its publication and services PMI its highest value since July 2007. Household confidence also rose over the second quarter, with the EC indicator reaching its peak since the beginning of 2018. Labour market conditions in the euro area improved in the second quarter. The unemployment rate fell to 7.9 per cent in May, from 8.1 per cent in March 2021. Concurrently, consumer expectations of the unemployment rate over the following twelve months measured by the EC consumer confidence index improved considerably in the second quarter of 2021, reaching its pre-crisis levels. Overall, data available in mid-July 2021 indicated an acceleration in quarterly growth of real GDP over the second quarter of 2021.

Consumer price inflation in the euro area increased substantially in the second quarter of 2021, reaching 1.9 per cent on an annual basis in June compared to 1.1 per cent on average in the first quarter of 2021. Higher inflation reflected the 2020 low base effect in energy prices and, to a lesser extent, price increases in industrial goods. Core inflation, excluding food and energy product prices, fell in the second quarter of 2021 to 0.9 per cent on an annual basis in June against 1.2 per cent on average in the first quarter of 2021.

In June the ECB revised its economic growth forecast for the period 2021–2022 upwards, leaving unchanged its forecast for 2023. The Bank expects euro area real GDP growth to reach 4.6 per cent in 2021, 4.7 per cent in 2022 and to slow down to 2.1 per cent in 2023. The upward revision is driven by the assumption that the pandemic will have a weaker economic effect due to the progress of the vaccination campaign, significant additional fiscal policy measures partially financed by NextGenerationEU and improved expectations about external demand, reflecting the US supportive fiscal policy. The upward revision

Contribution to the Change in Real GDP in the Euro Area by Country

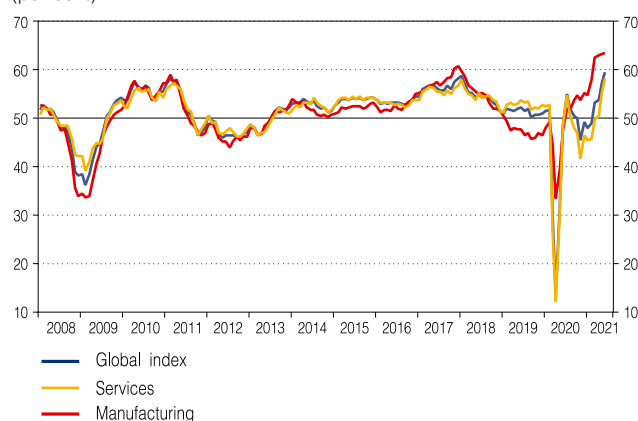
(per cent, percentage points; quarterly)



Sources: Eurostat and BNB calculations.

PMIs in the Euro Area

(per cent)



Sources: Eurostat, Markit.

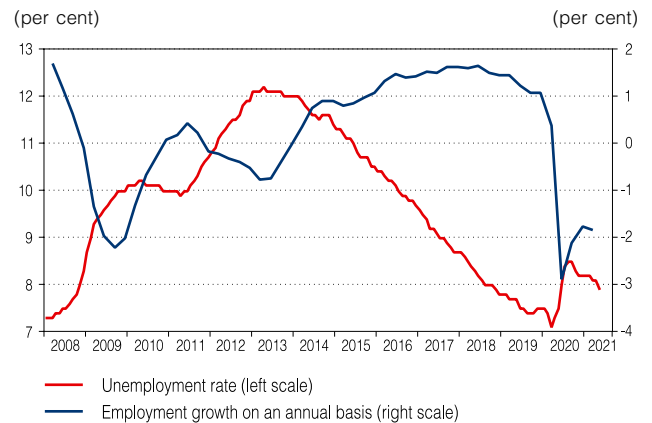
sion of inflation projection for 2021 and 2022 was attributable to the faster economic recovery and higher commodity prices.

The ECB Governing Council left unchanged the reference interest rates and the forward guidance for their future path in the second quarter of 2021. No changes were made to asset purchase programmes: net purchases under the Asset Purchase Programme (APP) continued at a monthly pace of EUR 20 billion, while purchases under the Pandemic Emergency Purchase Programme (PEPP) would continue to be conducted at a significantly higher pace than during the first months of the year. The ECB Governing Council noted that PEPP with a balance of EUR 665 billion of a total of EUR 1850 billion by end-June would be used flexibly with a view to preventing a tightening of financial conditions in the euro area. The Governing Council of the ECB expected net purchases under the PEPP to continue to at least the end of March 2022, or until the ECB Governing Council judges that the COVID-19 crisis phase is over.

On 8 July the ECB Governing Council announced the results of its monetary policy strategy review. In the new strategy the quantitative definition of price stability was changed from 'close to, but below two per cent' to symmetric two per cent inflation target, meaning positive and negative deviations from the target would be equally undesirable. The ECB Governing Council confirmed that HICP remains the appropriate measure for assessing price stability. The ECB Governing Council recommended the inclusion of the costs related to owner-occupied housing in the HICP, which would better represent the inflation rate. In the meantime, the ECB Governing Council in its monetary policy assessments will take into account inflation measures that include initial estimates of the cost of owner-occupied housing to supplement its set of broader inflation measures. The ECB Governing Council announced also an action plan to better account for climate change considerations within its monetary policy framework. The design of these measures will be consistent with the price stability objective.

At the end of June 2021 the cumulative amount of purchases under the Eurosystem's extended Asset Purchase Programme (APP) totalled

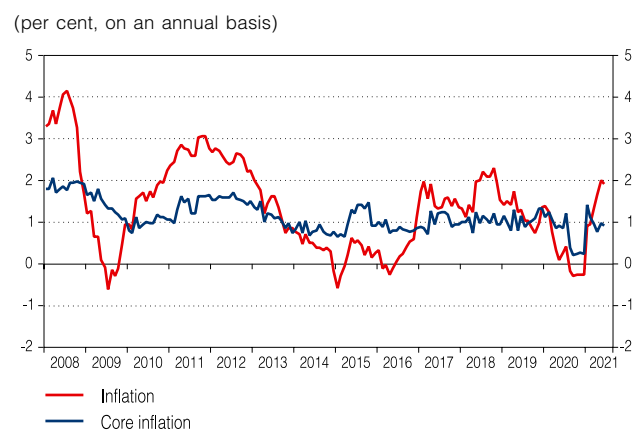
Euro Area Unemployment Rate and Employment Growth



Note: Unemployment data are up to May 2021.

Source: Eurostat.

Euro Area Inflation Rate



Notes: The inflation is measured by HICP. Core inflation is measured by HICP, excluding energy products, food, alcohol and tobacco products.

Source: Eurostat.

Projections of the Annual Rate of Change of Euro Area Real GDP

(per cent)

Institution	Date of release	2021		2022		2023	
		latest	previous	latest	previous	latest	previous
the ECB	VI.2021	4.6	4.0	4.7	4.1	2.1	2.1
the EC	VII.2021	4.8	4.3	4.5	4.4	-	-

Sources: the ECB, the EC.

Projections of Euro Area Annual Inflation Rate

(per cent)

Institution	Date of release	2021		2022		2023	
		latest	previous	latest	previous	latest	previous
the ECB	VI.2021	1.9	1.5	1.5	1.2	1.4	1.4
the EC	VII.2021	1.9	1.7	1.4	1.3	-	-

Sources: the ECB, the EC.

EUR 3017 billion, up EUR 54 billion compared with the end of the first quarter of 2021. Concurrently, the cumulative amount of the temporary asset purchase programme of private and public sector securities (PEPP) totalled EUR 1185 billion as of the end of June (against EUR 938 billion as of the end of March).

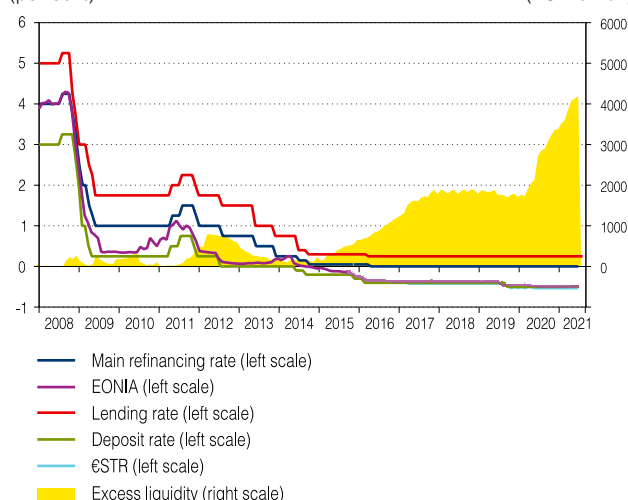
As of 2 July 2021 the Eurosystem balance sheet figure rose to EUR 7908 billion (69.8 per cent of GDP in 2020) compared with EUR 7494 billion (66.2 per cent of GDP in 2020) on 2 April 2021. Asset purchases under the APP and PEPP (EUR 292 billion) and long-term refinancing operations (EUR 110 billion) contributed most to the higher ECB balance sheet figure over the period. The excess liquidity in the euro area banking system continued to grow, reaching EUR 4209 billion as of the end of June, up EUR 302 billion compared with the end of March.

The increased excess liquidity in the euro area banking system over the quarter was the main factor behind the maintained low levels of the euro short-term rate in the euro area money market (€STR), and the interest rates on unsecured deposits in the interbank market. Over the review period the average value of the €STR fell to -0.57 per cent against -0.56 per cent in the first quarter of 2021. The trade volume of overnight deposits in the unsecured euro area money market rose in the second quarter of 2021, with its daily average over the period coming to EUR 44.1 billion, against EUR 43.4 billion in the first quarter of 2021. Over the quarter EURIBOR unsecured deposit rates did not change significantly.

Interest Rates of the ECB, EONIA, €STR and Excess Liquidity in the Euro Area Banking System

(per cent)

(EUR billion)

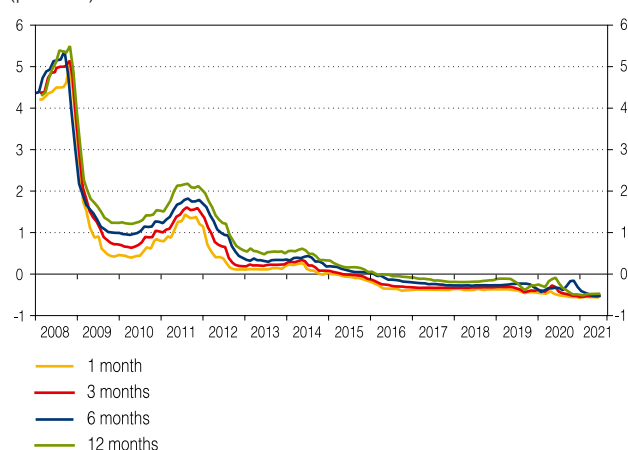


Notes: EONIA and €STR data are average for the month. Between 15 March 2017 and 30 September 2019 €STR data are on the preliminary €STR interest rate (pre-€STR).

Source: the ECB.

EURIBOR Dynamics

(per cent)



Source: the ECB.

International Commodity Prices

Crude Oil

In the second quarter of 2021 the Brent crude oil price rose significantly on an annual basis in both US dollars (118.3 per cent) and euro (99.9 per cent). In June 2021 the crude oil price stood at USD 73.1 *per barrel* (EUR 60.7 *per barrel*). High annual growth reflected to a large degree the low base in the second quarter of 2020, when global fuel consumption fell considerably due to COVID-19 containment measures. Global economic activity continued to recover, contributing also to the higher demand for oil in the second quarter of 2021. The strict fulfilment of output cuts agreed between the OPEC+ countries was another important precondition for strong price increases.⁸

Considering the progress of the vaccination process in developed countries and economic indicators signalling a continuing recovery of global economic activity in July 2021, market participants' expectations concerning the oil price in the second quarter of 2021 increased significantly compared to those in March 2021. In the first two weeks of July 2021 futures prices for the next six months fluctuated between USD 71.1–74.5 *per barrel*. This increase was largely due to the difficulties in negotiating the gradual reduction of the OPEC+ output cuts in early July 2021⁹.

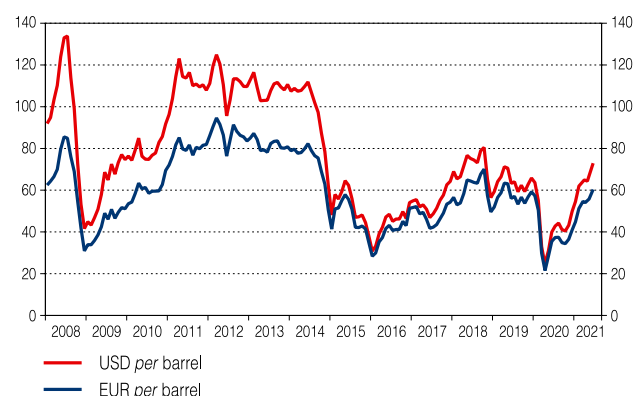
Basic Metals and Food Prices

In the second quarter of 2021 metal prices in US dollars posted significant annual growth of 79.2 per cent (63.6 per cent in euro), retaining the upward trend observed in the last three quarters. The major factor behind higher metal prices was the enhanced demand, reflecting the rebound in global economic activity in the second quarter. The base effect in 2020 added to strong growth in metal prices. By index sub-component, copper and aluminium prices had the major contribution to annual growth of the metal price index over the second

⁸ On 3 December 2021 OPEC, Russia and other leading oil-producing countries revised their schedule for a gradual reduction of the supply constraints, deciding on 7.2 million barrels *per day* in January 2021 and on holding additional OPEC+ meetings in the following months, at which supply changes will be discussed in the course of 2021.

⁹ The UAE did not support all OPEC+ decisions in early July, expressing its disagreement with the low base oil production quota in 2022.

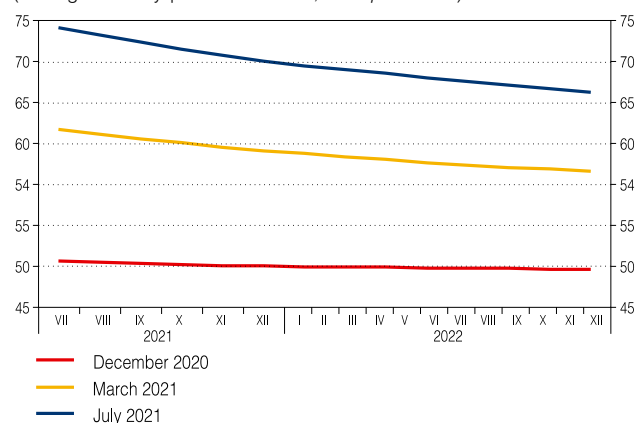
Brent Crude Oil Price



Source: the World Bank, the ECB and BNB calculations.

Brent Crude Oil Futures Prices

(average monthly price of contract, USD *per barrel*)



Source: JP Morgan.

quarter of 2021. The price of copper, which is of key importance to Bulgarian exports of goods, rose significantly in the review period. This was mainly due to global industrial output growth and low base effects in the corresponding period of 2020. At the end of the quarter, the increase in metal prices was partially limited by the plans announced by Chinese authorities to release copper, aluminium and zinc from the national reserves. Metal prices in the third and fourth quarters of 2021 are expected to increase year on year both in US dollars and euro. Their growth rate is anticipated to slow down at the end of the year.

Over the second quarter of 2021 the food price index in US dollars posted an annual increase of 32.4 per cent (20.8 per cent in euro). As in the previous quarter, most index sub-components increased, with soyabean and maize having the largest positive contribution to annual growth of the food price index. This reflected the higher global demand, particularly from China, and the low base effect over the same period of the prior year. The price of wheat, which is essential for Bulgarian exports of goods, also reported a significant increase on an annual basis in the second quarter of 2021, reflecting to a large extent the higher global demand for wheat used in animal husbandry. Rises in the price of maize may be explained by China's enhanced demand and expectations for restrictions on the supply side due to unfavourable weather conditions in some of the main producers of maize.

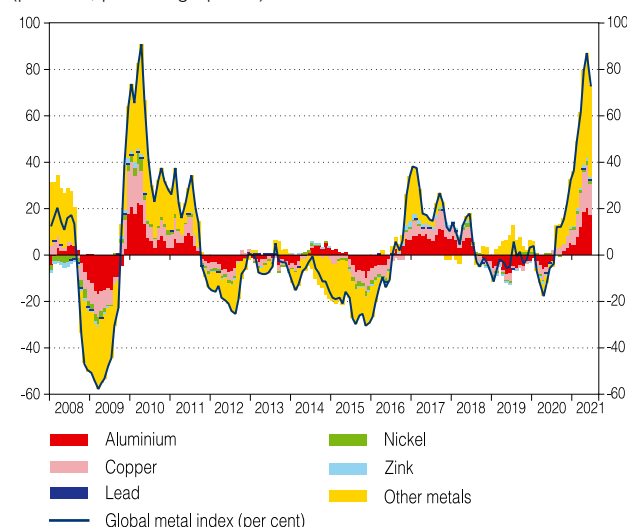
Market participants' expectations of food prices in the third and fourth quarters of 2021 point to an increase on an annual basis both in US dollars and euro, which will moderate by end-year.

Reflecting this dynamics of the international commodity prices on an annual basis and if exchange rates are assumed to remain unchanged, we expect the positive terms of trade for Bulgaria to cease in the second quarter of 2021. The expected rise in oil prices on an annual basis is assumed to contribute to the discontinuation of the positive terms of trade as Bulgaria is a net importer of oil. Assuming that COVID-19 containment measures will be phased out by the end of 2021, a shift to positive terms of trade for Bulgaria is projected over the third quarter of the year. This will be mainly driven by projected higher prices in the services sector. In the last quarter of 2021 favourable terms of trade for Bulgaria are likely to change.

Price Indices of Major Raw Materials and Commodity Groups

Metals

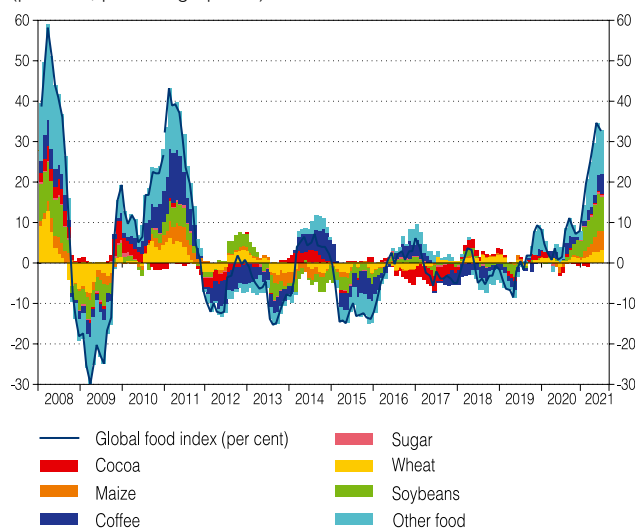
(per cent; percentage points)



Sources: the ECB and BNB calculations.

Food

(per cent; percentage points)



Note: Annual rate of change (per cent) and contribution (percentage points) by sub-component of relevant price indices measured in US dollars).

Sources: the ECB and BNB calculations.

2. FINANCIAL FLOWS, MONEY AND CREDIT

In the first four months of 2021 the total current and capital account surplus of Bulgaria decreased compared to the same period of 2020, reflecting mainly a higher deficit on the trade balance and decreased net revenue from travel and transport services. In the second half of 2021 the positive current and capital account balance is expected to increase on an annual basis from the end of 2020, driven mainly by a projected rise in net revenue from travel and transport services under an assumption of a gradual phase-out of COVID-19 containment measures.

Over the first five months of 2021 the annual growth of non-government sector's deposits accelerated from the end of 2020 under the influence of still deferred household consumption of some goods and services, limited investment activity of corporations and maintenance of precautionary savings amid a persistent uncertainty surrounding the COVID-19 pandemic development. Since March the growth rate of credit to the private sector has gradually accelerated, more pronounced in the sector of households.

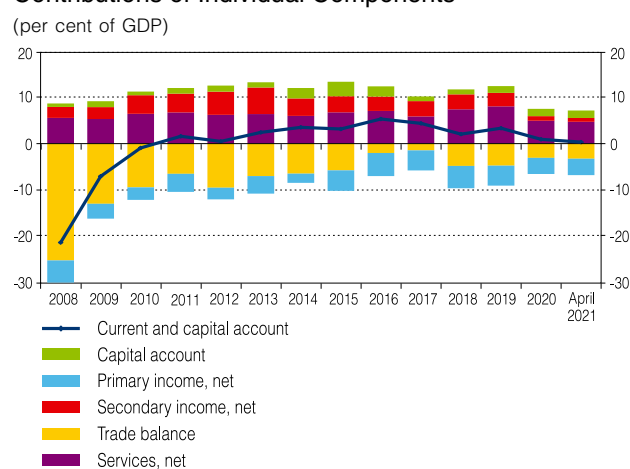
In the second half of the year the growth in deposits of the non-government sector is expected to slow down slightly in line with a projected gradual rise in economic activity and private consumption. Projected domestic demand growth, still low lending rates and positive housing market prospects will favour the growth of credit to the private sector over the projection horizon.

External Financial Flows

In the first four months of 2021 a deficit was reported on the BOP current account¹⁰ of Bulgaria compared to a surplus in the same period of 2020, reflecting mainly an increased negative trade balance and decreased services trade surplus. As of April, BOP current account balance for the last 12 months was negative at -1.3 per cent of GDP (-0.7 per cent of GDP at the end of 2020).

Higher trade balance deficit in January–April 2021 compared to the same period of 2020 reflected a larger increase in nominal goods imports than in nominal exports. In the context of the COVID-19 containment measures in force over the first four months of 2021 in Bulgaria and its major trading partners, an annual growth rate of 19.1 per cent was reported in goods imports and 17.3 per cent in goods exports. The increased trade balance deficit was mainly driven by rising real volumes of goods imports (by 6.0 per cent on an annual basis during the first quarter), while real goods exports declined on an annual basis (-2.3 per cent in the first

Current and Capital Account Flow Dynamics and Contributions of Individual Components



Notes: April 2021 data on the current and capital account flows are accumulated for the last 12 months.

Nominal GDP data for the last four quarters, including the first quarter of 2021, are used in calculating the GDP ratio for April 2021.

Sources: the BNB, the NSI, BNB calculations.

¹⁰ The analysis of balance of payments flows employs information from its analytical reporting. Preliminary data.

quarter of the year).¹¹ A significant price rise of crude oil, of which the country is a net importer, was also a factor for the increased trade balance deficit.

The reduced surplus in net services during the first four months of 2021 compared to the same period of 2020 was a result of the stronger rate of decline in nominal services exports than in services imports, largely reflecting the fact that Bulgaria is a net exporter of tourist and transport services, which were strongly affected by the containment measures. For January–April 2021 services exports dropped by 13.1 per cent on an annual basis, with the rate of decline slowing significantly from the annual decline of 30.4 per cent in 2020. This decrease was most pronounced in travel-related services which were impacted by the declining number of foreign nationals' visits to Bulgaria (NSI data for January–April 2021 show that this decline was -30.1 per cent annually compared to a -60.4 per cent year-on-year decrease for the entire year of 2020). For January–April 2021, services imports fell by 11.8 per cent on an annual basis, with imports of travel-related and other services reporting a significant decline, and those related to transport increasing over the period.

Net primary income deficit decreased marginally on an annual basis, mainly due to higher revenue from direct and portfolio investment¹² in Bulgaria. Lower dividends and distributed profits on the debit side of the item, reflecting largely other sectors,¹³ had an additional contribution to this. At the same time, banks did not distribute dividends, as in 2020, in line with the BNB decision of January 2021 on the macroprudential measure for capitalising all banking system profits for 2020.¹⁴

In the first four months of the year, net secondary income surplus declined from a year earlier, primarily driven by lower remittances from Bulgarian citizens working abroad. The balance of payments capital account surplus rose slightly

Flows on Major Balance of Payments Accounts

(EUR million)

	January–April 2020	January–April 2021	Change, January–April 2020 vis-à-vis January–April 2021
Current account	315.8	-103.0	-418.7
Trade balance	-389.4	-625.2	-235.8
Services, net	943.2	801.3	-141.8
Primary income, net	-673.2	-638.8	34.4
Secondary income, net	435.3	359.7	-75.6
Capital account	286.9	356.6	69.7
Financial account	-1,726.9	5,144.0	6,870.9
Change in reserves	2,354.1	-3,488.3	

Sources: the BNB, the NSI, BNB calculations.

¹¹ Non-seasonally adjusted national account GDP data.

¹² Preliminary data subject to revisions, which usually show an increase in outflows to non-residents.

¹³ It should read sectors other than general government, banks and central bank.

¹⁴ For further details, see the BNB [press release](#) of 28 January 2021.

on an annual basis, mainly as a result of lower outflows under this item.

As a result of flow dynamics on individual current and capital account items, as of April the surplus on the overall balance of the two accounts for the last 12 months declined from the end of 2020, with a rising trade balance deficit, a contracting net services surplus and a lower net secondary income surplus contributing most substantially. Total current and capital account balance as of April 2021 was 0.3 per cent of GDP (0.9 per cent of GDP at the end of 2020).

The forecast of current account flow developments is based on the assumption that a large part of the COVID-19 containment measures in force in the fourth quarter of 2020 and early 2021 in other EU countries and Bulgaria would be phased out in the second half of the year. As a result, the negative trade balance is expected to swing to a surplus on an annual basis¹⁵ over the third and fourth quarters of 2021. This will reflect mainly a projected rise in the positive balance of net services and, to a lesser extent, of net secondary income. In the second half of 2021, revenue from travel and transport services is anticipated to rise from the same period of 2020, which would push up the net services surplus. Net secondary income surplus is expected to increase more significantly in the second half of the year due both to projected higher current transfers to the government under EU programmes and increased remittances from Bulgarian emigrants. In the second half of 2021 capital account surplus is expected to grow slightly on an annual basis.¹⁶

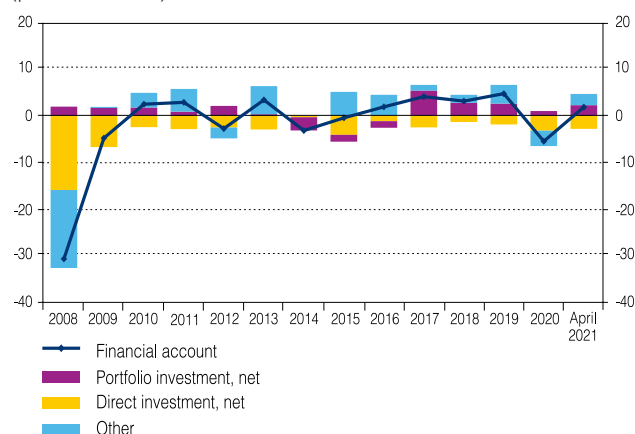
In January–April 2021, a net outflow from Bulgaria's financial account to the amount of EUR 5.1 billion (8.4 per cent of GDP) was reported. The positive financial account balance in the first four months of 2021 was formed as a result of a significantly larger increase in Bulgarian residents' foreign assets compared to their foreign liabilities. The rise in foreign assets was mainly due to increased short-term assets of banks. Measures announced by the BNB in March 2020

¹⁵ It should read current account balance for the last four quarters.

¹⁶ It should read capital account balance for the last four quarters.

Financial Account Flow Dynamics and Contributions of Individual Components

(per cent of GDP)



Notes: The Other item includes Other investments, net, and Financial derivatives (other than reserves) and Employee stock options, net. April 2021 data on financial account flows are accumulated for the last 12 months. Nominal GDP data for the last four quarters, including the first quarter of this year, are used in calculating the GDP ratio for April 2021.

Sources: the BNB, the NSI, BNB calculations.

to further strengthen the capital and liquidity position of banks, including by imposing limits on their foreign exposures in order to reduce credit and concentration risks in bank balance sheets, remained in force during 2021 as well.¹⁷ An increase in assets outside Bulgaria of other sectors¹⁸ was reported, which also contributed, though to a lesser extent, to net outflows from Bulgaria. As of April 2021, the financial account balance for the last 12 months turned to a surplus of 1.9 per cent of GDP (a -5.5 per cent deficit as of end-2020), mainly driven by the increase in foreign short-term assets in the form of bank institutions' foreign currency and deposits as compared to their level at end-2020.

In the first four months of 2021 direct investment liabilities (reporting FDI inflows into Bulgaria) increased on an annual basis to EUR 513.7 million (EUR 454.9 million in January–April 2020).¹⁹ This growth was due to the increase in liabilities from reinvested profits for which the banking sector contributed substantially. Banking reinvested profits reflected BNB decisions as of 2020 and 2021 on the capitalisation of all profits. Proceeds from Sofia airport concession were reflected as an additional inflow of direct investments into Bulgaria. At the end of the first quarter, total FDI amounted to 78.8 per cent of GDP. Breakdown by economic sector shows that real estate activities, manufacturing and financial and insurance activities registered the highest FDI amounts.

As a result of net flows on the balance of payments current, capital and financial accounts, gross international reserves in April 2021²⁰ declined from the end of 2020, according to BOP data for the last 12 months, with increased foreign assets of the banking sector contributing mainly to this between January and April 2021. As of April the international reserve coverage of the average nominal imports of goods and non-factor services retained its high level of 9.4 months for the last 12 months (11.1 months in December 2020). The ratio of Bulgaria's inter-

¹⁷ For further details, see the BNB [press release](#) of 28 January 2021.

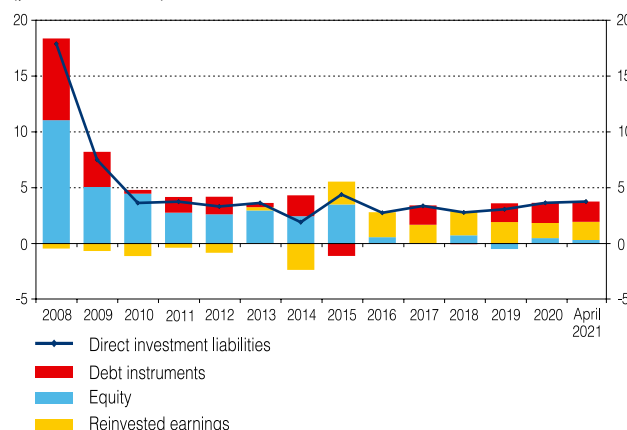
¹⁸ It should read sectors other than general government, banks and central bank.

¹⁹ Preliminary data subject to revision.

²⁰ Valuation adjustments and price revaluation excluded.

Direct Investment Liabilities by Type of Investment

(per cent of GDP)



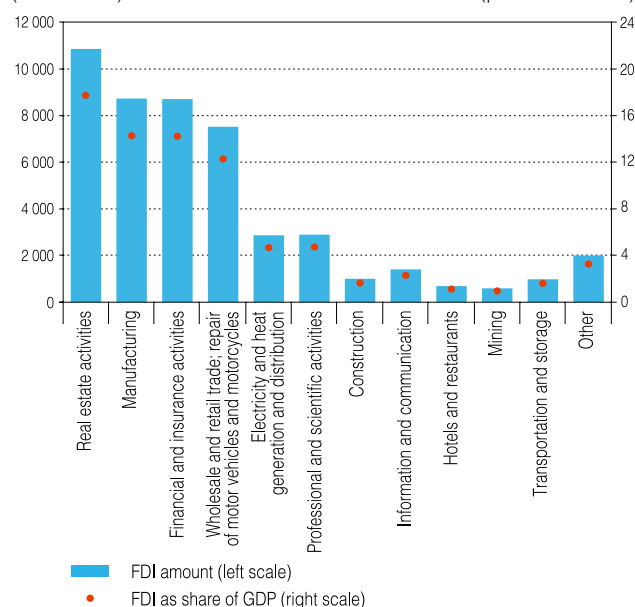
Notes: April 2021 data on direct investment liabilities flows are accumulated for the last 12 months. Nominal GDP data for the last four quarters, including the first quarter of 2021, are used in calculating the GDP ratio for April 2021.

Sources: the BNB, the NSI, BNB calculations.

FDI by Sector as of the End of the Fourth Quarter of 2020

(EUR million)

(per cent of GDP)



Note: Nominal GDP data for the last 12 months, including the first quarter of 2021, are used in the FDI to GDP ratio denominator.

Sources: the BNB, the NSI, BNB calculations.

Gross External Debt as of April 2021

(EUR million)

	Amount	Change	
		Since December 2020	For the last 12 months
General government	7,399.6	-20.0	1,613.6
Central bank	0.0	0.0	0.0
Banks	5,015.7	-310.2	307.8
Other sectors	10,875.1	-168.8	-549.0
FDI – intercompany loans	14,310.9	-345.6	257.2
Total	37,601.3	-844.6	1,629.6

Note: Further details on individual institutional sectors are available on the BNB website, Statistics, External Sector/Gross External Debt.

Source: the BNB.

national reserves²¹ to short-term external debt remained also high, reaching 308.6 per cent in April against 336.4 per cent in December 2020.

In April 2021 Bulgaria's gross external debt came to EUR 37.6 billion (61.5 per cent of GDP), marking a drop of EUR 844.6 million from December 2020 (63.4 per cent of GDP). This drop was mainly driven by a lower amount of intercompany loans and decreased short-term liabilities of banks from a year earlier. In April 2021 long-term debt as a share of Bulgaria's gross external debt occupied 76.5 per cent (77.4 per cent in December 2020). Concurrently, based on debt interest payments data, it may be concluded that the terms for servicing external obligations by Bulgarian residents remain favourable.

Monetary and Credit Aggregates

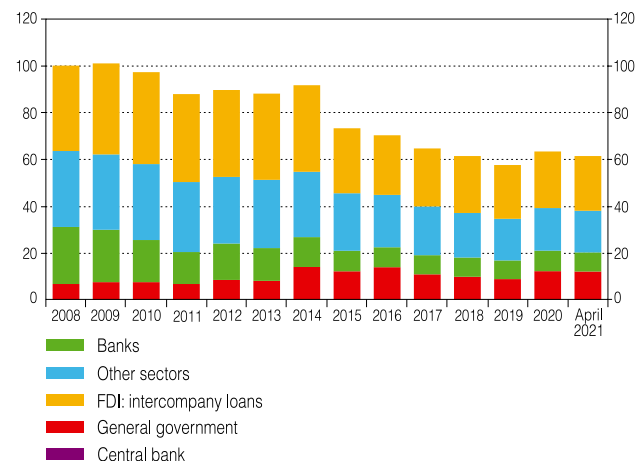
Over the first five months of 2021 the annual growth of non-government sector's deposits²² accelerated from the end of 2020, reaching 11.7 per cent in May (9.7 per cent in December 2020). This dynamics was largely driven by increased household savings and, to a lesser extent, by growth in non-financial corporations' deposits. Over the first several months of 2021 deposit dynamics was affected by still deferred household consumption of some goods and

²¹ The analysis is based on gross international reserves on the BNB Issue Department balance sheet. The market value of international reserves includes changes stemming from transactions, valuation adjustments and price revaluation.

²² Non-government sector's deposits include deposits of households, non-financial corporations and financial corporations. Deposits of households and non-financial corporations comprise the largest share of all non-government sector's deposits (96.4 per cent on average for the last 12 months as of May 2021) and, therefore, the analysis is focused on these two sectors.

Gross External Debt

(per cent of GDP)

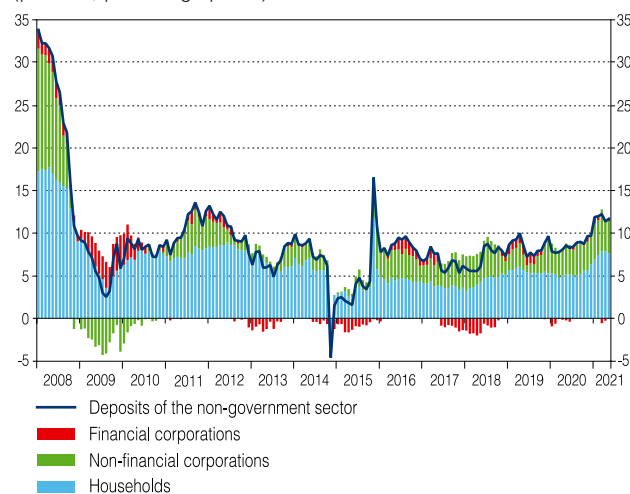


Notes: Further details on individual institutional sectors are available on the BNB website, Statistics, External Sector/Gross External Debt. Nominal GDP for the last four quarters, including the first quarter of 2021, is used in calculating the gross external debt to GDP ratio for April 2021.

Sources: the BNB, the NSI, BNB calculations.

Annual Growth of Non-government Sector Deposits and Contribution by Sector

(per cent, percentage points)



Note: The annual growth rate of non-government sector's deposits in November 2015 reflects the exhausted base effect of KTB removal as a reporting unit from the monetary statistics in November 2014.

Source: the BNB.

services, also due to limited possibilities to make certain expenses related mostly to tourism and travel, limited investment activity of corporations and maintenance of precautionary savings amid a persistent uncertainty surrounding the COVID-19 pandemic development. Despite the gradual relaxation in internal containment measures and very low deposit interest rates, households continued to save for precautionary motives. The bulk of total non-government sector's deposits was still made up of overnight deposits. A factor likely to affect the continuous rise in overnight deposits is the practice applied by some banks to transform time into demand deposits and to stop offering new time deposits. In terms of the currency structure, households and firms continued to save primarily in national currency.

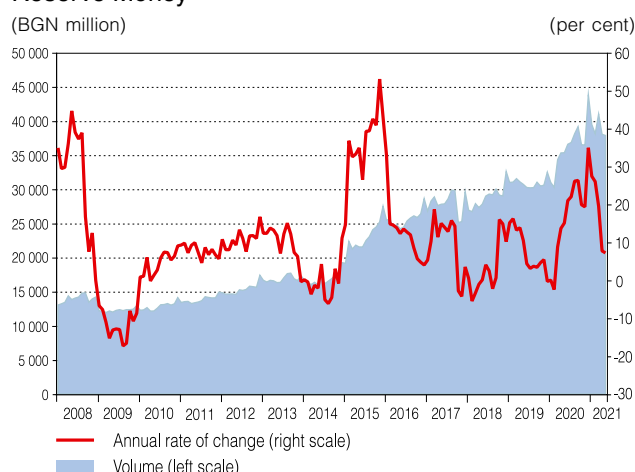
The effective implicit rate of minimum required reserves²³ remained at levels close to the previous year's levels, reflecting high inflows of attracted funds from residents in the banking system during the first five months of 2021. In May this rate was 9.37 per cent (9.43 per cent in December 2020), with banks' deposits at the BNB comprising 8.27 percentage points in the fulfilment of minimum required reserves, and the remaining 1.10 percentage points forming recognised cash balances.

Annual growth in reserve money followed a downward trend, its rate reaching 7.2 per cent in May (34.9 per cent at end-2020) driven by decreased banks' deposits at the BNB, in particular excess reserves. In May 2021 excess funds on banks' minimum reserve accounts over the required minimum of reserve assets under Ordinance No 21 was 50.2 per cent on an average daily basis, from 81.1 per cent in December 2020.²⁴ At the same time, minimum required reserves continued growing under the influence of the rising deposit base. During the first five months of 2021 bank funds in TARGET2 remained close to their level of the end of 2020.

²³ Under Article 3 of BNB Ordinance No 21 on the Minimum Required Reserves Maintained with the Bulgarian National Bank by Banks, the rate of minimum required reserves on funds attracted from residents is 10 per cent of the deposit base, from non-residents 5 per cent and from the state and local government budgets 0 per cent.

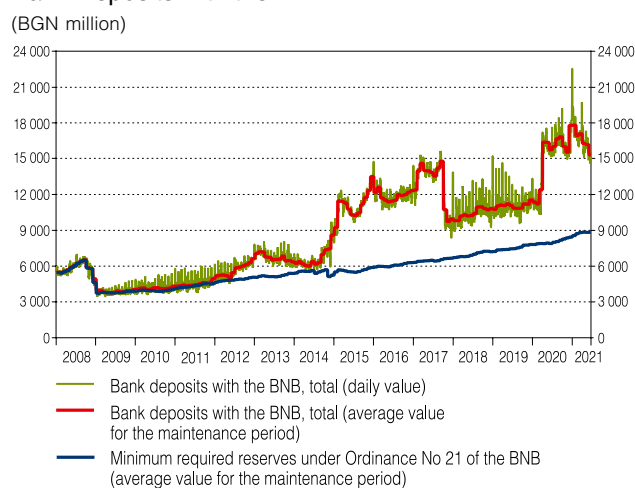
²⁴ In 2021 the excess reserve interest rate remains unchanged from 2020 at -0.70 per cent.

Reserve Money



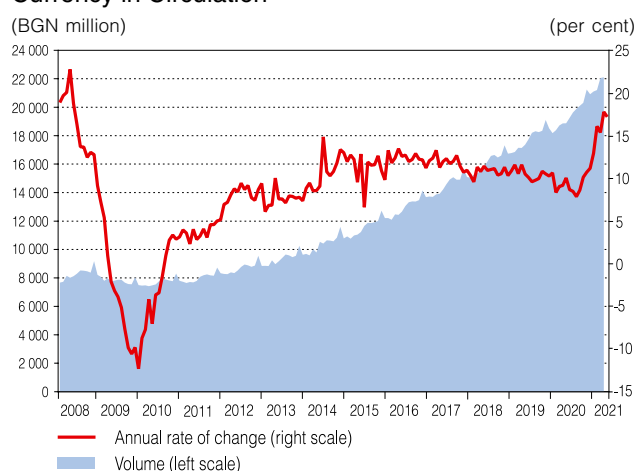
Source: the BNB.

Bank Deposits with the BNB



Source: the BNB.

Currency in Circulation



Source: the BNB.

The annual growth rate of currency in circulation retained its upward trend which started in September, reaching in May 17.2 per cent (11.2 per cent by end-2020). High growth rates of currency in circulation could be explained by demand for liquidity for transaction purposes, given the gradual recovery in the economic activity and private consumption, on the one hand, and by demand for cash for the purpose of accumulation in the context of historically low interest rates on deposits. An additional factor fostering demand for cash was the increased deposit service expenses under the current policy of certain banks to charge fees on large deposits, transform time into demand deposits and stop opening new time deposits.

Reserve currency (euro) trading with the BNB is the main lev liquidity management instrument of banks under currency board arrangements. In the first five months of 2021 net BNB sales of euro to banks were EUR 575 million.

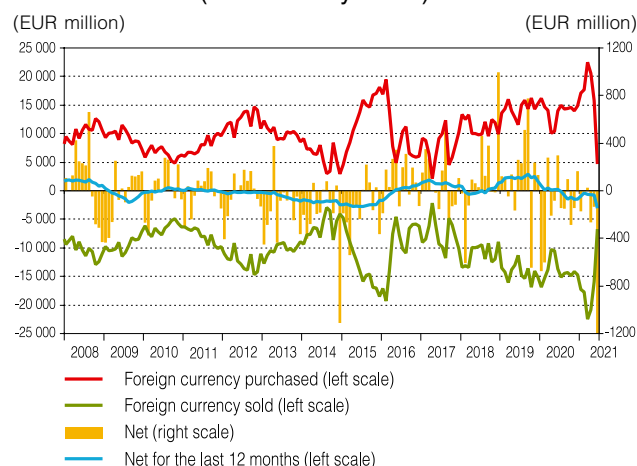
As of May 2021 bank assets grew by 11.0 per cent year on year.²⁵ Bank assets growth in the first five months of the year was largely driven by foreign assets of banks, with a significant decrease reported in their excess reserves with the BNB. This dynamics could be explained by banks' demand for higher earning opportunities for investing free liquid funds, while observing the BNB limits on bank foreign exposures. Increases in claims on the non-government sector and in Bulgarian government bond portfolios contributed also to total assets growth, albeit to a lesser extent. Compared with the end of 2020, a slight decline in foreign liabilities of banks was reported, which resulted in a BGN 9.5 billion increase in net foreign assets to BGN 17.3 billion as of May.

Since March the growth rate of credit to non-financial corporations and households²⁶

²⁵ Data from sectoral monthly reporting of other monetary financial institutions were used.

²⁶ Loans represent the bulk of bank claims on the non-government sector with a share of 97.1 per cent on average for the last 12 months as of May 2021, and the analysis was therefore focused on them. In addition to loans, claims include also repurchase agreements, securities other than shares, and shares and other equity instruments. Non-government sector's loans, in turn, include loans to households, non-financial corporations and financial corporations. The share of loans to households and non-financial corporations in total loans to the non-government sector accounted for 93.3 per cent on average in the last 12 months as of May 2021 and, therefore, developments in these two sectors are analysed.

Foreign Currency Purchases and Sales between the BNB and Banks (on a Monthly Basis)

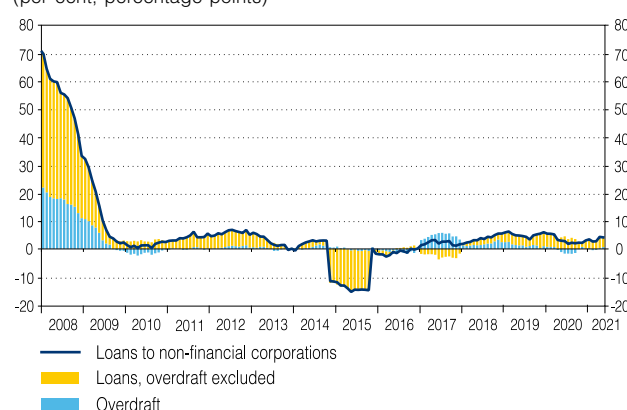


Notes: Net means currency purchased by the BNB minus currency sold by the BNB. Data refer to all bank transactions in foreign currency, including liquidity management operations related to the transfer of own funds from lev accounts with the BNB to own accounts with the BNB in euro and vice versa.

Source: the BNB.

Annual Growth of Credit to Non-financial Corporations and Contributions of Individual Types of Loans

(per cent, percentage points)



Note: The annual growth rate of loans to non-financial corporations in November 2015 reflects the exhausted base effect of KTB removal as a reporting unit from the monetary statistics in November 2014.

Source: the BNB.

has gradually accelerated, reaching in May 6.4 per cent (4.5 per cent by end-2020), the acceleration being more pronounced in the sector of households. Both demand and supply side factors continued to affect credit growth acceleration. Lending survey results for the first quarter of 2021 show a significant rise in demand for loans by households, especially for housing loans. In the sector of non-financial corporations, demand remained at the previous quarter's levels, though banks report that almost all factors have contributed to the enhanced demand for corporate loans. On the supply side, banks have a significant amount of liquidity as a result of progressively rising attracted funds from residents and BNB March 2020 measures to strengthen banking system capital and liquidity, in force during 2021 as well. Lending survey data for the first quarter of 2021 suggest eased standards in approving credit applications by corporations and households, most pronounced in housing loans. An important survey outcome is that over the first quarter of 2021 the overall state of the macroeconomic environment influenced the easing of the credit policy for the first time since early 2020. Most likely, these trends in credit demand and supply would persist in the second quarter as well. Commercial banks continued to disburse loans guaranteed by the Bulgarian Development Bank (BDB) under a government's measure in support of vulnerable firms and households, which was a factor, though with a limited relevance, supporting credit growth.

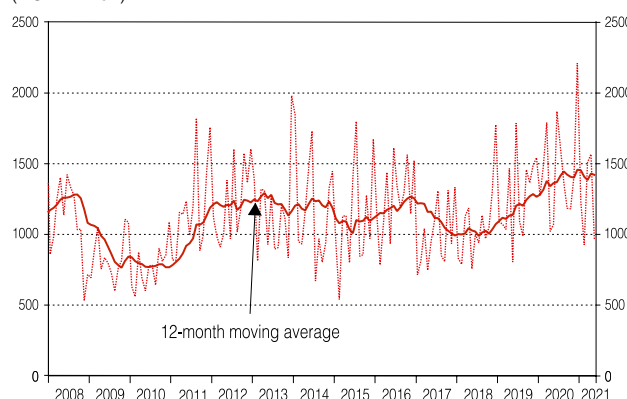
As of May the annual growth rate of non-financial corporations' credit accelerated to 4.1 per cent (3.0 per cent by end-2020), with the main contribution of loans excluding overdraft and, to a lesser extent, overdrafts. In the first five months of the year newly extended²⁷ corporate loans remained at close to end-2020 levels. In terms of the currency structure, an increase was registered in the share of newly extended corporate loans in euro at the expense of lev and dollar-denominated loans. As of May loans in national currency comprised 52.1 per cent of total new corporate loans, while euro-denominated ones occupied 47.1 per cent and dollar-denominated 0.8 per cent.²⁸

²⁷ The terms 'new' and 'newly extended' hereinafter referred to as the statistical category 'new business'.

²⁸ The share of loans in national currency and euro for the last 12 months as of May 2021.

New Loans to Non-financial Corporations (Monthly Volumes)

(BGN million)

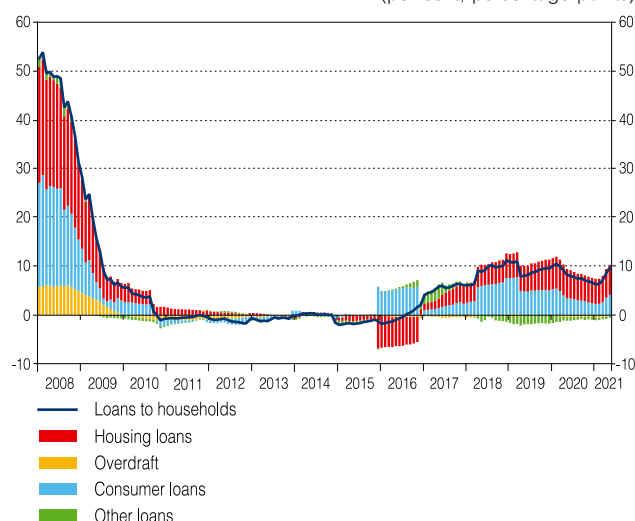


Note: For data characterised by a significant volatility, additionally moving averages computed for suitably selected periods are provided, in order to smooth the fluctuations in corresponding time series and present the trends in their development.

Source: the BNB.

Annual Growth of Household Credit and Contributions of Individual Types of Loans

(per cent, percentage points)



Note: Based on additional information received from reporting units, a revision of household loans was carried out according to their purpose of use in the period December 2015 – August 2019.

Source: the BNB.

Household credit accelerated strongly to 9.7 per cent on an annual basis in May (6.6 per cent at the end of 2020). More essential growth acceleration was observed in consumer loans, their annual rate reaching 8.7 per cent in May (5.0 per cent in December 2020). Growth in credit for house purchase increased to 13.4 per cent in May, from 11.6 per cent at end-2020. Newly extended household loans recorded a rise in volumes during the first five months of 2021²⁹ compared to the end of the prior year, due largely to the higher amount of new consumer loans.

Summarised weighted results of the bank lending survey³⁰ for the first quarter of 2021 suggest easing of credit standards³¹ in approving credit applications of corporations and households, most significantly for housing loans. Major factors contributing to easing of the banks' lending policy (credit standards and conditions)³² to corporations were the competition and high liquidity in the banking sector, significant volumes and low costs of attracted funds and the overall state of the macroeconomic environment. In addition, the easing of bank policies with regard to households was also driven by favourable prospects of the housing market and increased assessments of borrower solvency. The decreased risk appetite of banks has further contributed to the credit policy tightening with regard to corporate and consumer loans, while the higher risk appetite has favoured their policy on housing loans. Bank expectations for the second quarter of 2021 are for keeping corporate lending standards and continuous easing of household credit standards.

Over the first quarter of 2021 banks reported retention of demand for corporate loans and a significant increase in household demand,

²⁹ Based on 12-month moving average.

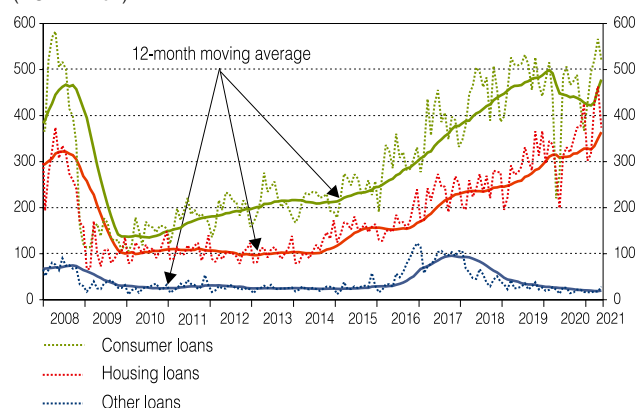
³⁰ Bank lending survey in Bulgaria is carried out by the BNB on a quarterly basis. Summarised results of the survey are presented through weighting bank responses by their market share in the relevant credit segment.

³¹ Credit standards are understood as internal bank guidelines or criteria for loan approvals established prior to negotiating the terms of extended loans. Credit standards determine the type of the loan and collateral considered admissible by banks, taking into account specific priorities by sector, etc. Credit standards specify also all relevant conditions to be met by a borrower.

³² Credit conditions typically involve the reference interest rate surcharge, the loan amount, conditions for its utilisation and other conditions, fees and commissions, collateral or guarantees to be provided by a borrower.

New Loans to Households (Monthly Volumes)

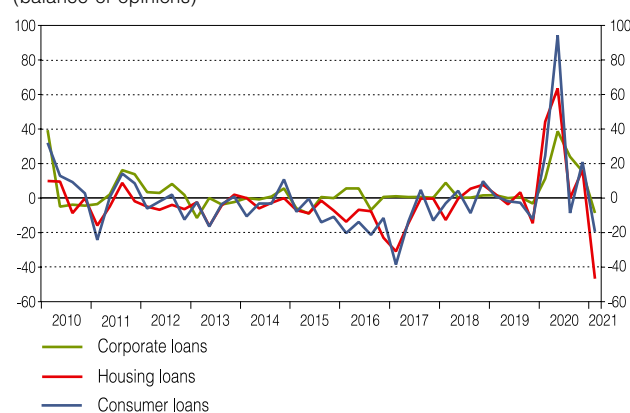
(BGN million)



Source: the BNB.

Changes in Credit Standards

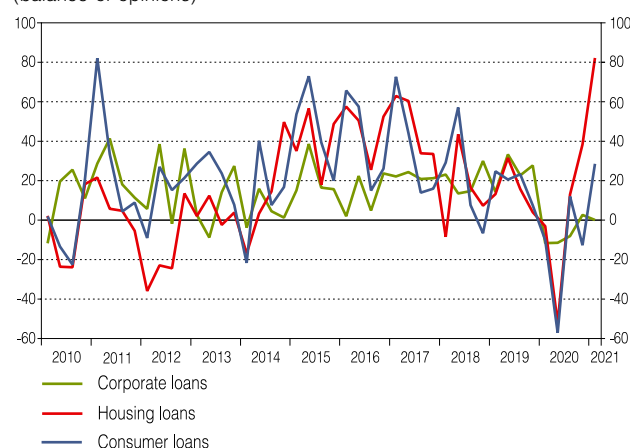
(balance of opinions)



Source: the BNB.

Changes in Credit Demand

(balance of opinions)



Source: the BNB.

Notes: As regards credit standards, charts present banks' balance of opinions defined as a difference in percentage points between the percentage of banks responding 'tightened' ('considerably' and 'somewhat'), and the percentage of banks responding 'eased' ('considerably' and 'somewhat'). As regards credit demand, the balance of opinions is defined in percentage points as a difference between the percentage of banks responding 'increased' ('considerably' and 'somewhat') and the percentage of banks responding 'reduced' ('considerably' and 'somewhat'). All opinions are weighted by the bank's market share in the relevant credit segment. Data presented in the charts show the change from the previous quarter.

most pronounced in loans for house purchase. Historically, from the moment when questions on households were included in the survey (2010), no such increase in demand for housing loans was observed. Although weighted results show that corporate credit demand remained unchanged from the last quarter of 2020, bank responses point to almost all factors pushing up credit demand. The main factors continued to be corporations' needs for working capital and inventories, low interest rates, and the need of funds for refinancing and renegotiating debt. Unlike the previous three quarters, demand for investment purpose funds had also a slight positive contribution. The most important drivers for the enhanced demand for consumer loans in the first quarter of 2021 involved demand for financial resources by households for purchasing current consumption and durable goods, the overall state of the macroeconomic environment and low interest rates. Higher demand for housing loans over the quarter was mainly driven by households' needs of funds for purchasing first and especially additional residence, as well as favourable housing market prospects. In the second quarter of 2021 banks expect an increase in demand for loans by both households and corporations.

In the second half of the year growth in deposits of the non-government sector is expected to slow down slightly in line with a projected gradual rise in the economic activity and private consumption. The expected increase in the share of non-performing loans in bank portfolios and the projected moderate rise in interest rates on new loans in the second half of 2021 due to the expiry of the extended private moratorium on bank loan repayments are anticipated to have only a slight moderating effect on credit growth. Concurrently, projected domestic demand growth, still low lending rates and positive housing market prospects will favour growth of credit to the private sector over the projected horizon. The newly launched Recovery programme in support of the business through guarantees from the Fund of the Funds aimed at overcoming the effects of the COVID-19 pandemic may also be expected to have a stimulating effect on credit dynamics.

Interest Rates

In the first half of 2021 no unsecured overnight deposit transactions in levs were concluded in the interbank money market. These developments reflected the lack of an incentive for trading in this market amid ample banking system liquidity, partially due to the continued strong increase in deposits and BNB measures of March 2020 remaining in force during 2021 to strengthen banks' capital and liquidity. As no transactions were concluded over the period, LEONIA Plus index was not available.

Deposit interest rates recorded a further decline from achieved historically low levels under the influence of an increasing inflow of attracted funds and high banking system liquidity. As of May 2021 the average weighted interest rate on new time deposits of non-financial corporations and households was 0.01 per cent (down 9 basis points from the end of 2020), while the average interest rate on household deposits remained slightly positive at 0.09 per cent as of May (down 6 basis points from the end of 2020). The negative value of non-financial corporations' deposit rate rose to -0.18 per cent in May (-0.02 per cent in December 2020). Downward dynamics of new corporate deposit rates was driven by the increase in the negative lev deposit rate (from -0.10 per cent in December to -0.27 per cent in May), which pushed the overall average weighted rate on lev deposits of households and corporations into a negative territory.

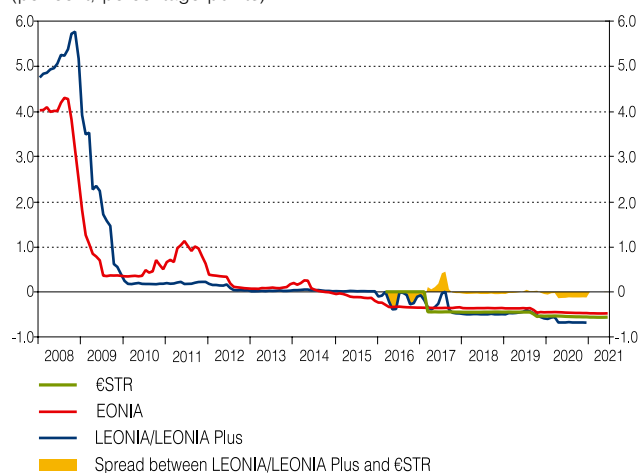
Interest rates on new loans continued to follow a slight downward tendency under the influence of decreasing costs and increasing volumes of attracted funds and lacking high-yield alternatives for using free resources by credit institutions. Banks continued to disburse loans under the two government anti-crisis programmes in response to the COVID-19 pandemic, appearing to be a favourable factor for downward developments in interest rates on new loans.³³

As of May 2021 the interest rate on new corporate loans in levs fell by 22 basis points from end-2020 to 2.6 per cent, and in dollars

³³ These programmes provide for guaranteeing loans to corporations under reduced collateral requirements and lower interest rates along with interest-free loans to natural persons, where certain conditions are met. The above programmes are set to expire by the end of June 2021.

Overnight Interbank Money Market Rates (Average Monthly Value)

(per cent, percentage points)



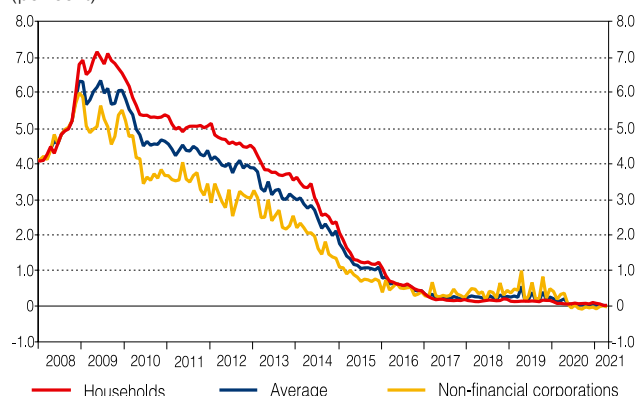
Notes: €STR replaced EONIA on 2 October 2019. EONIA (euro overnight index average) will further be computed and published until the end of 2021 by applying a fixed spread to €STR.

LEONIA Plus replaced LEONIA on 1 July 2017. Monthly LEONIA Plus values are calculated as an arithmetic average for days when overnight unsecured lending transactions are concluded in the interbank market in levs.

Sources: the BNB, the ECB.

Interest Rates on New Time Deposits

(per cent)



Notes: The average interest rate is calculated for all sectors, maturities and currencies weighted by the relevant volumes of new deposits. Average deposit rates for non-financial corporations and households are based on interest rates for all maturities and currencies weighted by relevant volumes of new business.

Source: the BNB.

by 119 basis points to 2.2 per cent. A slight increase was observed in new euro lending rates (by 36 basis points to 2.5 per cent in May).³⁴ In the sector of households, a stronger drop in the annual percentage rate of charge (APRC) was registered in newly extended consumer loans, its value reaching as of May 8.6 per cent. This dynamics was due to a much larger degree to the decline in the implicit rate of non-interest expenses. The APRC on new housing loans posted a 8 basis point decrease from the end of 2020 to 3.1 per cent in May, reflecting almost entirely lower interest rates.

As a consequence of a larger drop of interest rates in Bulgaria compared to the euro area, spreads between interest rates on new loans to corporations and households contracted slightly from the end-2020 levels.³⁵

Over the second half of 2021 new deposit rates for both non-financial corporations and households are expected to remain close to zero, reflecting continuous strong inflows of attracted funds and ample banking system liquidity. New lending rates are expected to rise slightly under the influence of a projected increase in the share of non-performing loans in bank portfolios after the expiry of the deadline for deferring obligations of bank clients.

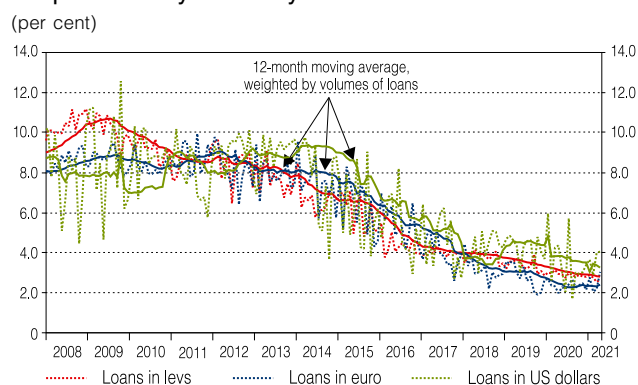
In the second quarter of 2021 no government securities auctions were held in the primary market. Given the lack of new primary market issues and strongly limited trade volumes in the secondary government bond market during the review period, as of end-June the long-term interest rate used for assessing the degree of convergence remained unchanged from March at 0.14 per cent.

At the same time, the upward trend observed since early 2021 in the yield of Bulgarian government bonds issued in international capital markets was sustained, with June increases more pronounced in the long end of the sov-

³⁴ Indicated values of interest rates on loans to non-financial corporations and households are weighted averages on a 12-month basis.

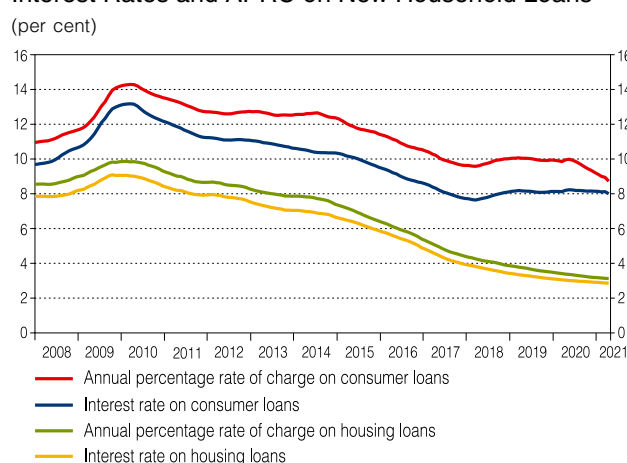
³⁵ Spreads are calculated as a difference between average interest rates in Bulgaria and the euro area across all maturities for the relevant type of credit, overall in national currency and euro, weighted by relevant volumes of new loans for a 12-month period.

Interest Rates on New Loans to Non-financial Corporations by Currency



Source: the BNB.

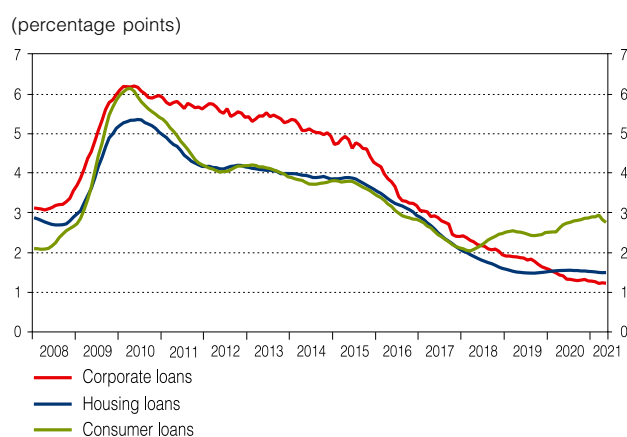
Interest Rates and APRC on New Household Loans



Notes: Interest rates in all maturities and currencies are weighted by the relevant volumes of new loans for a 12-month period. The difference between the APRC and relevant interest rates reflects the approximate share of all non-interest service charges on loans (including fees and commissions).

Source: the BNB.

Interest Rates on New Corporate and New Housing Loans: the Spread between Bulgaria and the Euro Area



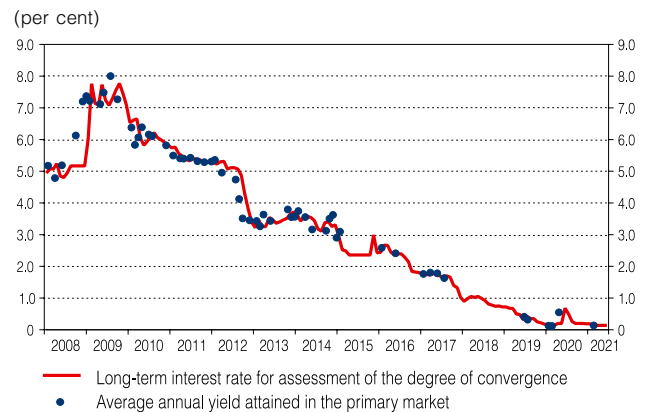
Sources: the BNB, the ECB.

foreign yield curve. A marginal yield drop was reported only in the short end of the yield curve.

Increased yields of domestic government bonds were affected by both internal and external factors, with upward trends observed in euro area countries as well. Rising government bond yields in the euro area reflected optimistic expectations of market participants about the economic recovery after accelerated vaccination campaign and increased inflation expectations on the back of favourable macroeconomic prospects, including the implementation of the large US fiscal stimulus package. In addition, expected positive effects of the Recovery and Resilience Facility on the euro area economic activity are likely to have an additional influence on the improving macroeconomic outlook over medium to long-term horizons, contributing to the decrease of the financial market uncertainty and, hence, demand for lower risk assets. The political uncertainty in Bulgaria after parliamentary elections in April was an internal factor likely to push up Bulgarian government bond yields. Concurrently, the decrease of Bulgarian bond yields in the short end of the yield curve in the second quarter of 2021 led to narrowing in spreads between Bulgarian and German government securities. Widening spreads were reported in the long-term end of the curve.

In the third and fourth quarters of 2021 Bulgarian government bond yields would further reflect both external and internal factors. Maintenance of external factors driving the current upward trend in government bond yields may also contribute to yield increases of domestic government bonds. The political uncertainty arising after the parliamentary elections in April and July 2021 remains an internal factor likely to exert an upward pressure on Bulgarian government bond yields over the projection horizon. At the same time, a potential COVID-19 resurgence in the euro area could result in an increase of the financial market uncertainty, investors' reorientation to lower risk assets and declines in government bond yields, including in Bulgaria.

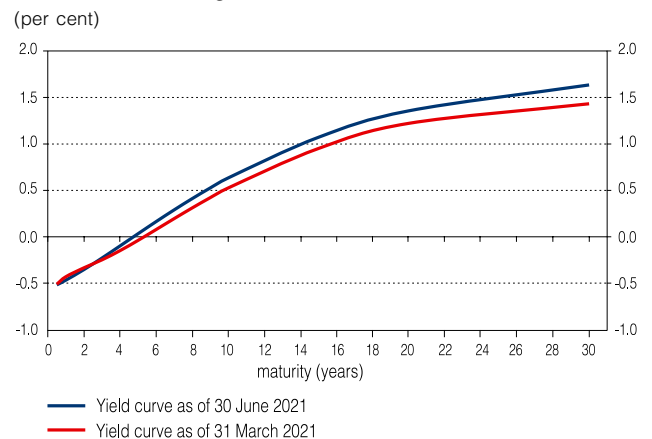
Long-term Interest Rates in the Primary and Secondary Markets of Government Securities



Notes: The chart shows the yields reported in the primary and secondary markets of government bonds with ten-year-and-six-month original maturity. The frequency of auctions for issues with this maturity corresponds to the number of observations marked in blue.

Source: the BNB.

Reference Government Securities Yield Curve in Bulgaria



Notes: The reference yield curve of Bulgarian government securities is based on BNB own calculations under the extended version of the Nelson–Siegel–Svensson model (1994). The yield change refers to the previous quarter.

The chart employs daily yield data on Bulgarian government securities issued and traded in international capital markets, published in the MF Central Government Debt and Guarantees Monthly Bulletin.

Sources: the MF, BNB calculations.

Financial Flows between Consolidated Budget and Other Sectors of the Economy

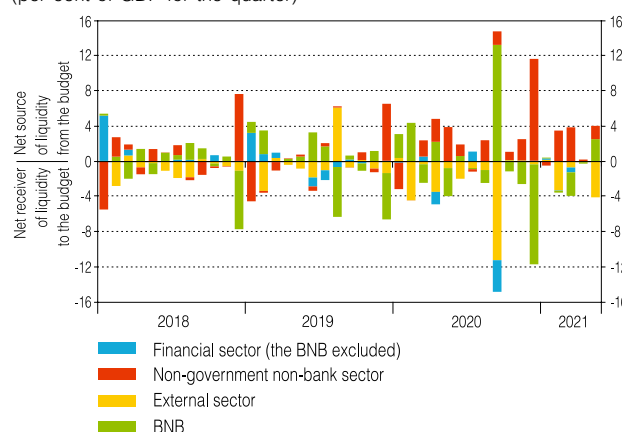
Government revenue and expenditure policies and budget financing operations affect the allocation of liquidity across economic sectors.³⁶

In the first quarter of 2021 the non-government non-bank sector remained a net beneficiary of liquidity from the budget as a result of the excess of non-interest budget expenditure over tax and non-tax revenue. The main factor behind positive net financial flows to this sector was the implementation of government's discretionary measures under the State Budget Law³⁷ for 2021. Concurrently, the external sector was a net source of liquidity to the budget due to the excess of reimbursed funds under the EU Common Agricultural Policy and grants under EU programmes over the amount of budget expenditure on Bulgaria's contribution to the EU budget and interest payments on external loans. During the same period, the excess of newly issued government securities in the domestic market over maturing government bonds was a factor for rechanneling liquidity from the budget to the financial sector (excluding the BNB). Net inflows of liquid funds from the budget to the non-government sector (BGN 1886 million) and the financial sector (BGN 121 million) was higher than the positive net flows from the external sector (BGN 1011 million) in the first quarter of 2021. Hence, the government deposit with the BNB decreased from December 2020 by BGN 754 million to reach BGN 7267 million as of end-March.

CFP performance data for April and May 2021 show that the government continued to support non-government non-bank sector's liquidity under the influence of the extended duration of the measures in support of households and corporations. Nevertheless, BNB estimates show that the net effect of the budget on the liquidity of the non-government sector shrank to as high as BGN 531 million, which was due to increased

Consolidated Budget Effect on Other Sectors' Liquidity (Monthly)

(per cent of GDP for the quarter)



Notes: This chart is based on monthly data of CFP implementation by including also information obtained from MF monthly bulletins on state budget performance and major CFP indicators and MF Central Government Debt and Guarantees monthly bulletins. GDP data for the second quarter of 2021 from the BNB macroeconomic forecast of June 2021 are used to assess liquid flows in April and May 2021.

Sources: the MF, the BNB.

³⁶ Allocation across economic sectors in this Section of the Economic Review is based on available information from monthly reports under the Consolidated Fiscal Programme and does not therefore coincide with the sector classification used in the National System of Accounts.

³⁷ For further information, see Main Parameters of the 2021–2023 Budgetary Framework, BNB Economic Review, 4/2020.

tax and non-tax revenue over the period.³⁸ In line with our expectations for the second quarter of 2021, in May Bulgaria received EUR 511 million under the EC instrument – Support to Mitigate Unemployment Risks in an Emergency, SURE – whereby the external sector became a net source of liquidity to the budget in April and May. No new government bond issues and maturing government securities appeared in the domestic market, so as the effect of the financial sector (the BNB excluded) to the budget was neutral.

In the third and fourth quarters of 2021 there is some uncertainty about consolidated budget's effect on non-government non-bank sector's and other sectors' liquidity, stemming mainly from the political uncertainty in Bulgaria. This uncertainty poses a risk that some effective fiscal measures would be extended or new ones would be announced. Maturing government securities in the domestic market (to the amount of BGN 323 million) over the third quarter of 2021 would be a factor for rechanneling liquidity from the budget to the financial sector (excluding the BNB), with a net budget effect on this sector's liquidity driven also by the implementation of the MF issuing policy over the projection horizon. An expected finalisation of the National Recovery and Resilience Plan, its consideration by the EC and a follow-up approval appear to be a potential factor for the disbursement of advance payments under it, presupposing a net inflow of liquid funds from the external sector to the budget until the end of the year.

Developments in financial flows generated in the process of external and internal economic factor interaction contributed to the decrease in Bulgaria's international reserves. By the end of June 2021 their market value (including valuation adjustments and price revaluations) – an asset on the BNB Issue Department balance sheet – was EUR 29.7 billion (BGN 58.1 billion), posting a decrease by EUR 1.1 billion (BGN 2.2 billion) from end-2020. According to the currency board principles, the decline in international reserves corresponds to the drop in the balance sheet value of the Issue Department liabilities. Lower reserves of banks with the BNB, in particular their excess reserves, contributed most

³⁸ For details, see the Fiscal Policy Effects on the Economy Section in Chapter 3.

substantially to the decreased liabilities of the BNB Issue Department in the first half of 2021 *vis-à-vis* December 2020. In the Issue Department liability side, currency in circulation posted a rise from the end of 2020, and the government deposit with the BNB also increased, albeit to a lesser degree.

In the second half of 2021 an additional drop is expected in excess reserves maintained by banks on their accounts with the BNB. This dynamics would be driven by banks' demand for higher earning opportunities for investing free liquid funds. At the same time, over the projection horizon minimum required reserves are anticipated to continue growing due to the rising deposit base. With regard to currency in circulation, we envisage that their annual growth rates will slightly moderate. Over the forecast horizon, developments in the government deposit with the BNB are expected to reflect mainly the realised budget balance and the MF issuing policy. A potential external source of liquidity to the budget would be an expected advance payment by the EC under the National Recovery and Resilience Plan.

3. ECONOMIC ACTIVITY

In the first quarter of 2021 the real GDP growth rate in Bulgaria accelerated to 2.5 per cent on a quarterly basis despite the extension of containment measures that were introduced at the end of 2020. Net exports and private consumption contributed most strongly to economic growth over the review period. The positive contribution of net exports was driven by services trade, where exports of services posted growth and imports of services reported a fall, while private consumption growth was in line with increased real income of households, reflecting higher wages and net government transfers. Despite the growth rate of economic activity, employment declined by -0.7 per cent on a quarterly basis, because of a decrease of self-employed workers in agriculture. Employment in other sectors posted an increase.

In the second quarter of 2021 short-term economic indicators in Bulgaria signalled continuous growth in the economic activity in line with easing of certain anti-epidemic measures in Bulgaria. Assuming a phase-out of all containment measures in Bulgaria and Bulgaria's major trading partners, in the second half of the year real GDP is expected to grow compared with the first half of the year. This will be accompanied by a certain weakening of the role of fiscal policy due to the assumption of a phase-out of some government anti-crisis measures related to the COVID-19 pandemic.

Current Economic Environment

Despite the extension of containment measures introduced against the spread of COVID-19 in the last quarter of 2020, the real GDP growth rate accelerated to 2.5 per cent in the first quarter of 2021 according to seasonally adjusted NSI national account data. Enhanced economic activity was driven by the private sector. In terms of growth structure, the main positive contribution was made by net exports and the transition to growth in domestic demand. Concurrently, government consumption and fixed capital investments declined on a quarterly basis³⁹. Notwithstanding, in the first quarter of 2021 government net transfers to households and corporations continued to strongly support disposable income of economic agents under the projected in the 2021 State Budget Law allowances to pensions, measures on subsidised employment⁴⁰ and public sector wage rises.

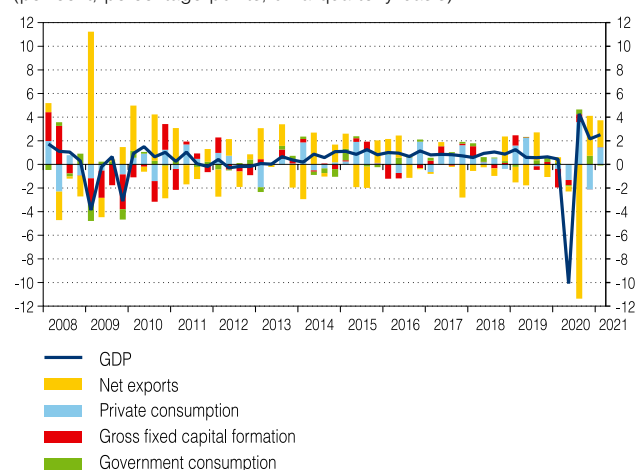
Private consumption had the largest positive contribution to the quarter-on-quarter change in domestic demand over the first quarter of 2021. It increased by 2.2 per cent from the fourth

³⁹ According to BNB calculations published by the NSI, for which quarterly non-financial accounts of the general government sector are used.

⁴⁰ Including the programmes such as '60/40', 'Short-term support for employment in response to the COVID-19 pandemic', 'Employment for you' and 'Save me'.

Contribution to GDP Growth by Final Use Component

(per cent, percentage points; on a quarterly basis)



Notes: Non-additive data due to direct chain-linking and seasonal adjustment of GDP and its components. The contribution of the change in inventories has not been included.

Sources: the NSI, BNB calculations.

quarter of 2020 in line with increased income of households, improved consumer confidence indicator and lower rate of household savings.⁴¹ The EC consumer survey shows that in the first quarter of 2021 households' financial position in all income groups improved, including those with the lowest income (first quartile), which generally have a higher propensity to consume. Higher household income was underpinned by quarter-on-quarter growth of employees, the increased minimum wage⁴² since the beginning of the year and higher public sector remunerations⁴³. In terms of final consumer expenditure structure, a stronger rise was reported in expenditure on services, non-durable and semi-durable goods, while durable goods exhibited lower growth. This points to a broad-based and sustainable increase in household consumption.

In the first quarter of 2021 government consumption fell by 0.5 per cent in real terms compared to the previous quarter. Data from quarterly non-financial accounts of the general government sector indicate that this dynamics was a result of a quarter-on-quarter fall in intermediate consumption and government's health-care costs.⁴⁴

Between January and March 2021 investment in fixed capital rose by 0.1 per cent on a quarterly basis in real terms. BNB estimates⁴⁵ show that this was entirely driven by growth in private investment, while public investment reported a fall on a quarterly basis. Quarter-on-quarter private investment growth is in line with the lower uncertainty in the economy compared with the high values recorded in the past year⁴⁶, available spare capacity, increased external demand for Bulgarian goods and services on a quarterly basis and improved managers' expectations about future production activity. Lower investment of the general government sector in the

⁴¹ According to seasonally adjusted data. For details, see the Household Behaviour Section in Chapter 3.

⁴² From the beginning of 2021 the minimum wage was raised from BGN 610 to BGN 650.

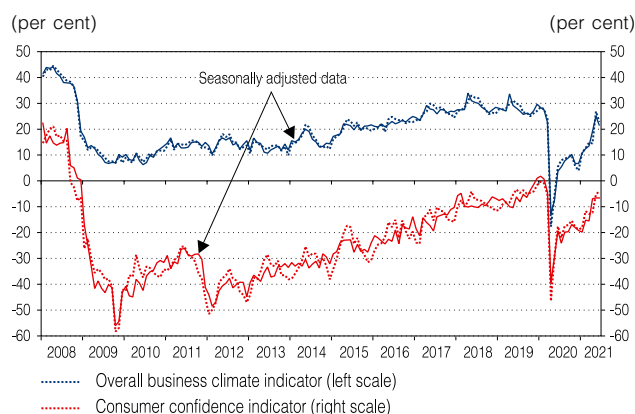
⁴³ For details see the Fiscal Policy Effects on the Economy Section in Chapter 3.

⁴⁴ NSI preliminary data, seasonally adjusted by the BNB, are used.

⁴⁵ The estimate employs data derived from quarterly non-financial accounts of the general government sector, published by the NSI.

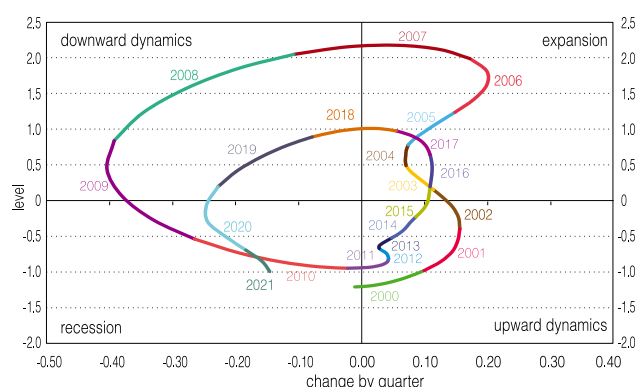
⁴⁶ According to the uncertainty indicator calculated by the BNB.

Business Climate and Consumer Confidence



Sources: the NSI, Eurostat, BNB calculations.

Business Climate Dynamics Indicator



Notes: The chart compares the business climate level (the vertical axis) and its quarterly change (the horizontal axis). The business climate series has been transformed using the HP filter (with a parameter $\lambda = 100$) in order to eliminate short-term fluctuations, after which it has been standardised. The four chart grids allow to distinguish the four phases of the business cycle.

Sources: the NSI, BNB calculations.

first quarter of the year compared with the fourth quarter of 2020 is likely to reflect the exhausted effect of one-off investments at the end of 2020.

Net exports had the largest positive contribution to quarterly growth of real GDP in the first quarter of 2021 driven by services trade, where a rise in exports and a fall in imports of services were reported. As regards goods, imports continued to grow buoyantly underpinned by increased consumption and investment spending of corporations and households. Exports of goods also grew quarter on quarter but at a much slower pace than imports, constrained by not yet recovered external demand from EU Member States.

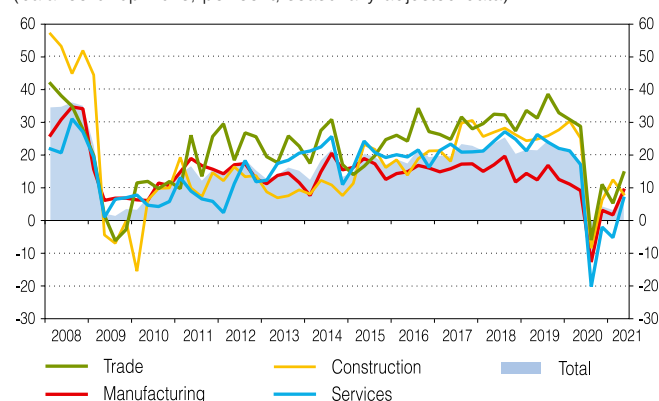
Economic indicators in Bulgaria for the second quarter of 2021 provide signals of continuous quarterly growth in the economic activity amid easing of the anti-epidemic measures in Bulgaria. Seasonally adjusted data⁴⁷ show that in the second quarter of 2021 the overall business climate indicator rose from the previous quarter, reflecting the more optimistic sentiment of managers in all sectors. Regarding the indicator of the future production activity, an improvement in expectations was reported in the sectors of manufacturing, trade and services, which corresponded to the reported increase in production assured with orders from both Bulgaria and abroad. The uncertain economic environment and insufficient demand continued to be among the main factors hampering business activities, although the share of firms pointing to these factors as constraints decreased somewhat. Concurrently, the economic uncertainty indicator calculated by the BNB reported a significant decline for both corporations and households. In line with the construction of the indicator, this is a sign that economic agents' expectations about economic environment developments are similar.

According to Eurostat's seasonally adjusted data on consumer confidence, in the second quarter of 2021 consumer sentiment improved on a quarterly basis, reflecting mainly the more optimistic consumer expectations about the economic situation and their financial position. The improved household sentiment is a precondition for further private consumption growth in the second quarter of 2021. These expectations are

⁴⁷ BNB seasonally adjusted data.

Expectations about Future Economic Activity

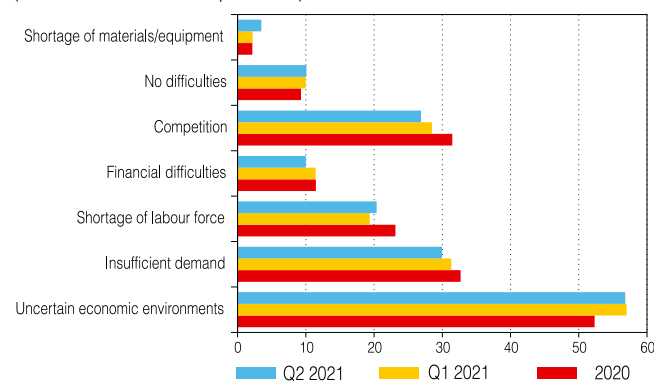
(balance of opinions, per cent; seasonally adjusted data)



Sources: the NSI, BNB calculations.

Factors Hampering Activities of Corporations

(relative share of all corporations)



Note: Average for the period calculated as sector-weighted (industry, construction, trade and services).

Sources: the NSI, BNB calculations.

supported by the increased number and nominal amount of card payments⁴⁸, and the rise in quarter-on-quarter retail trade turnover in real terms in April and May 2021⁴⁹.

In April–May 2021 the industrial production index also posted growth compared with the first quarter of 2021, albeit at a slower rate than in the first quarter of 2021. An increase in production was reported in all major sectors: mining and quarrying, manufacturing and production and distribution of electricity and heating and gas. The dynamics in the structure of nominal industrial turnover indicates that slowing growth of industrial production was due to a slower increase of corporate sales in domestic market, whereas turnover growth in external markets accelerated significantly from the first quarter 2021. This is a precondition for accelerated growth of exports in the second quarter of 2021 compared with the beginning of the year.

Construction production also rose in April and May 2021 compared to the first quarter of 2021, which reflected growth both in building and civil engineering construction. This gives grounds to expect an increase in investment activity in Bulgaria in the following months.

Data on the services production index⁵⁰ show that the economic activity in April increased in all major sub-sectors compared with the first quarter of 2021. These developments are in line with the easing of most containment measures in Bulgaria in April. Between January and March 2021 the highest increase was reported in services related to information and communication, accommodation and food services activities, and trade.

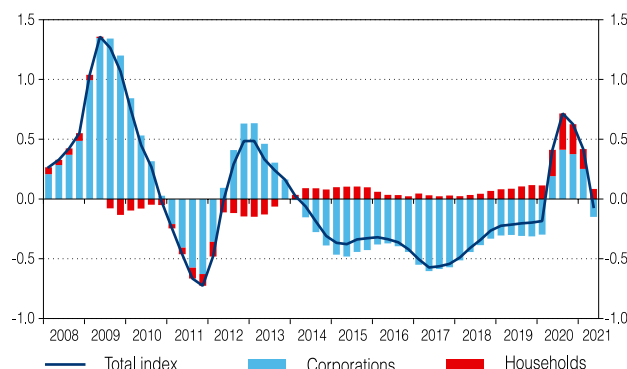
Assuming a phase-out of containment measures in Bulgaria and abroad, the economic activity in Bulgaria is projected to grow in the second half of 2021 compared with the first six months of the year. Private consumption and investment in fixed capital are expected to further support real GDP growth against the background of projected employment growth, lower uncertainty and increased external and domestic demand for goods and services. Net exports will also

⁴⁸ Borica AD non-public data are used.

⁴⁹ NSI seasonally adjusted data.

⁵⁰ Eurostat seasonally adjusted data are used.

Uncertainty Indicator in the Economy (Corporations and Households)

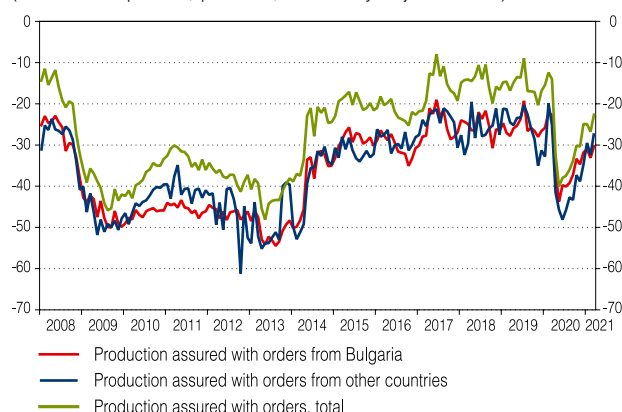


Notes: Higher values of this indicator should be interpreted as an increase in uncertainty. Positive/negative values of the global indicator show that the uncertainty in the economy is above/below its long-run level. This indicator is constructed under a methodology presented in: Ivanov, E. 'Constructing an Uncertainty Indicator for Bulgaria', BNB Discussion Papers 109/2018, and corresponds to the indicator U1 constructed in the paper.

Sources: the EC, BNB calculations.

Production Assured with Orders from Other Countries and Finished Goods Inventories

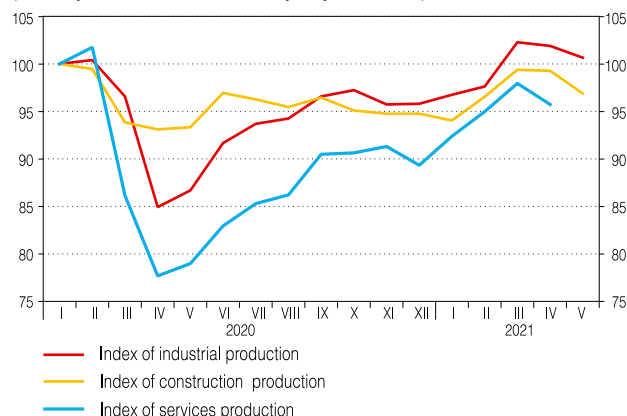
(balance of opinions, per cent; seasonally adjusted data)



Sources: the NSI, BNB calculations.

Dynamics of the Production Index in Industry, Construction and Services in 2020

(January 2020 = 100; seasonally adjusted data)



Sources: the NSI, Eurostat, BNB calculations.

Real GDP Growth by Final Use Component

(per cent, on a quarterly basis; seasonally adjusted data)

	2016				2017				2018				2019				2020				2021
	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	I
Consumption	1.3	-0.1	0.7	2.1	-0.1	1.5	1.3	1.7	1.3	0.6	1.1	0.1	1.5	2.4	0.1	0.5	0.0	-1.0	3.2	-1.2	2.1
incl.																					
Household consumption	1.4	-1.2	0.9	3.2	-1.1	1.4	1.5	2.7	1.0	0.2	0.8	-0.6	2.6	3.6	-0.3	-0.1	-0.5	-2.2	5.3	-0.9	2.2
Government final consumption expenditure	-0.8	2.5	0.2	1.9	0.8	-0.7	1.4	0.6	2.7	1.4	1.1	-0.5	1.4	0.2	0.6	1.9	-1.0	0.8	2.4	4.5	-1.1
Collective consumption	-0.7	2.6	1.5	1.2	1.9	0.5	1.3	1.1	0.4	2.5	-0.1	2.1	-2.0	0.8	2.7	0.6	3.4	0.0	1.1	2.0	0.4
Gross fixed capital formation	-5.7	-2.3	0.1	-1.7	1.7	3.8	-0.6	0.8	4.7	0.1	-1.7	0.6	4.6	0.2	-1.5	1.1	-8.2	-2.5	3.5	-0.1	0.1
Exports of goods and non-factor services	3.0	4.6	0.1	1.2	1.8	2.0	1.7	-2.2	0.4	1.1	-0.4	4.3	-0.2	-2.0	5.1	-0.8	0.6	-22.2	2.0	11.2	6.7
Imports of goods and non-factor services	1.0	1.7	1.9	1.4	2.1	1.5	1.9	1.9	1.2	1.4	0.5	1.2	1.7	0.7	1.4	0.7	0.0	-21.3	20.8	4.4	2.7
GDP	1.0	1.0	0.7	1.1	0.8	0.8	0.8	0.7	0.6	0.9	1.0	0.9	1.3	0.6	0.6	0.6	0.4	-10.1	4.3	2.2	2.5

Source: the NSI.

Real GDP Growth by Final Use Component

(per cent, on an annual basis)

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Consumption	2.7	-3.8	0.5	2.0	1.8	-1.6	1.8	2.7	2.5	3.0	3.5	3.6	1.4
incl.													
Household consumption	2.3	-2.8	0.1	1.7	2.0	-1.7	1.8	2.2	2.1	2.2	2.6	3.2	0.1
Government final consumption expenditure	1.0	-0.8	-0.2	0.3	-0.3	0.0	0.1	0.0	0.1	0.2	0.5	0.2	0.5
Collective consumption	-0.7	-0.2	0.6	0.1	0.0	0.1	-0.1	0.3	0.2	0.4	0.4	0.1	0.8
Gross fixed capital formation	6.2	-5.8	-4.9	-1.0	0.4	0.1	0.7	0.6	-1.4	0.6	1.0	0.9	-1.0
Exports of goods and non-factor services	1.3	-6.2	4.7	6.3	1.2	5.8	2.0	4.2	5.5	3.7	1.1	2.5	-7.3
Imports of goods and non-factor services	-3.5	15.5	0.5	-5.3	-3.3	-2.8	-3.4	-3.1	-3.3	-4.4	-3.6	-3.3	4.0
GDP	6.1	-3.4	0.6	2.4	0.4	0.3	1.9	4.0	3.8	3.5	3.1	3.7	-4.2

Source: the NSI.

contribute positively to economic growth over the half-year in line with the expected partial recovery of the economic activity in Bulgaria's major trading partners. Real GDP growth in the second half of 2021 will be limited by the assumption included in the forecast of phasing out some of the COVID-19 anti-crisis measures of the government in support of corporations and households. The main risk to lower than projected economic growth over the second half of the year is associated with the possible retightening of containment measures worldwide in case of insufficient progress toward herd immunity at global level or the spread of virus variants against which vaccines are less effective. Risk to lower growth arises also from the political uncertainty in Bulgaria after the parliamentary elections in July and the probability to postpone the implementation of some of the investment projects included in the forecast.

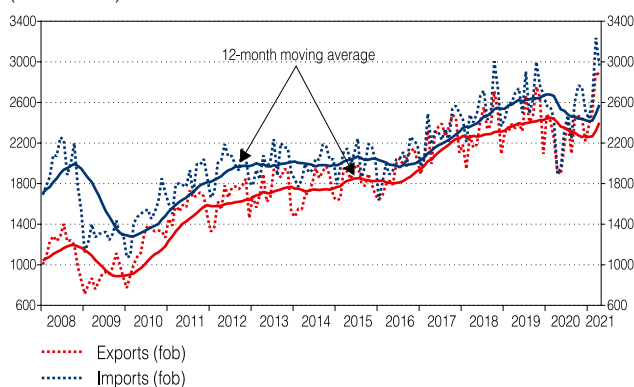
Exports and Imports of Goods and Services

Foreign trade data for the first quarter of 2021 show that Bulgarian exports and imports of goods rose considerably on an annual basis in nominal terms: by 8.1 and 9.5 per cent, irrespective of the extension of the containment measures against the spread of COVID-19 in Bulgaria and Bulgaria's major trading partners. Both in imports and exports the price component had a significant positive contribution to nominal growth. According to non-seasonally adjusted national account GDP data, in January–March 2021 real exports of goods fell by -2.3 per cent on an annual basis, while real imports rose by 6.0 per cent on an annual basis.

Foreign trade data for January–March 2021 show that the base metals group⁵¹ contributed most substantially to annual growth of exported goods in nominal terms, followed by the group of machines⁵². The year-on-year price rise was of key significance for the group of base metals, while nominal growth in machines reflected both real volumes and the price component.⁵³ Chemical products⁵⁴ also contributed substantially to growth in exports of goods driven mainly by the price rise on an annual basis.⁵⁵ The only commodity groups posting a nominal decline on an annual basis were the groups of mineral products⁵⁶ and textile and leather⁵⁷. Similar to 2020 mineral products had the largest negative contribution to the change in exports of goods in nominal terms. This was attributable to the annu-

Dynamics of Nominal Exports and Imports of Goods

(EUR million)



Source: the BNB.

⁵¹ In this chapter, it should read the group of base metals and their products under the Combined Nomenclature.

⁵² In this chapter, it should read the group of machines, vehicles, appliances, instruments and weapons under the Combined Nomenclature.

⁵³ Real volumes of exports in the groups of base metals and machines have been constructed by using NSI data on export prices and nominal values of exports in the respective commodity group under the Standard International Trade Classification (SITC).

⁵⁴ In this chapter, it should read the group of chemical products, plastics and rubber under the Combined Nomenclature.

⁵⁵ Real volumes of exports in the group of mineral products have been constructed by using NSI data on export prices and nominal values of exports in the respective commodity group under the SITC.

⁵⁶ In this chapter it should read the group of mineral products and fuels under the Combined Nomenclature.

⁵⁷ In this chapter it should read the group of textiles, leather, clothing, footwear and other consumer goods under the Combined Nomenclature.

Exports by Commodity Group, January–March 2021

	Value (EUR million)	Change* (EUR million)	Growth** (per cent)	Contribution** (percentage points)
Wood products, paper, ceramics and glass	364.7	24.5	7.2	0.3
Machines, vehicles, appliances, instruments and weapons	2,273.4	270.1	13.5	3.7
Mineral products and fuels	673.3	-102.9	-13.3	-1.4
Base metals and related products	1,454.8	318.6	28.0	4.3
Animal and vegetable products, food, drinks and tobacco	1,246.5	22.7	1.9	0.3
Textiles, leather, clothing, footwear and other consumer goods	834.4	-27.0	-3.1	-0.4
Chemical products, plastics and rubber	1,080.8	88.6	8.9	1.2
Total exports	7,928.1	594.6	8.1	-

* Change on the corresponding period of the previous year.

** Growth/contribution to growth of total exports over the period on an annual basis.

Source: the BNB.

al fall in real volumes⁵⁸, while the price component⁵⁹ of the commodity group rose significantly, reflecting the enhanced global demand for crude oil and constraints in its production.

Between January and March 2021 exports of goods to EU countries⁶⁰ rose by 11.7 per cent year on year, which was mainly due to the groups of machines and base metals. Exports to Germany, Italy and Belgium contributed most markedly to growth. Exports to non-EU countries grew by 1.6 per cent on an annual basis in the first quarter of 2021 again driven mainly by the groups of metals and machines. Exports to China and Turkey had the largest positive contribution. Reflecting this dynamics, the share of exports to the EU in total Bulgaria's goods exports increased to 67 per cent in the first quarter 2021 (65 per cent a year earlier).

Balance of payments data in April 2021 indicate an accelerated annual rate of growth in exports of goods in nominal terms compared with the first quarter of 2021. Assuming a global phase-out of most containment measures over the second half-year of 2021, real exports of goods are projected to continue growing buoyantly on an annual basis in the third and fourth quarters of 2021. Export prices in the third and fourth

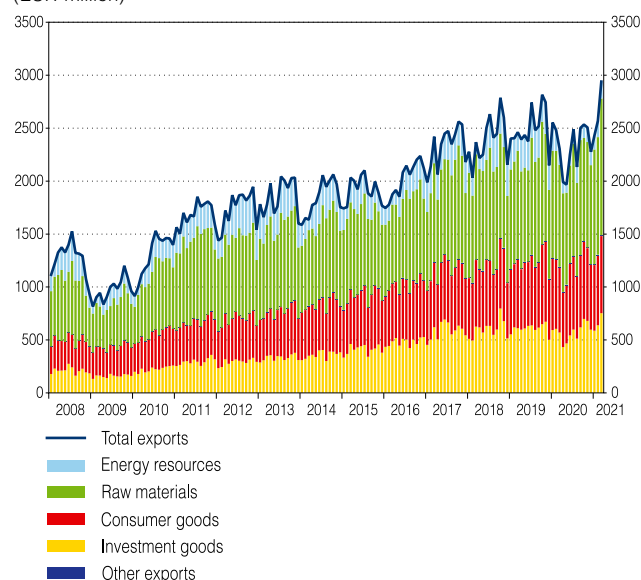
⁵⁸ Real volumes of exports in the group of mineral products have been constructed by using NSI data on export prices and nominal values of exports in the respective commodity group under the SITC.

⁵⁹ The quarterly export deflators for the oil and refined petroleum products group under the SITC were used to estimate the price effect in the first quarter of 2021.

⁶⁰ In this chapter the EU group should read the 27 states of the European Union. In January 2021 the United Kingdom ended its membership in the EU.

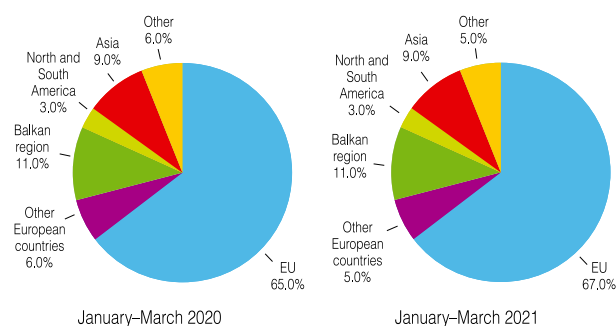
Exports of Commodity Groups by Use

(EUR million)



Source: the BNB.

Exports of Goods: Geographical Breakdown



Source: the BNB.

quarters of 2021 are expected to increase on an annual basis, which will also have a positive effect on the change of exports.

In the first quarter of 2021 imports of goods increased by 9.5 per cent on an annual basis⁶¹ driven by both higher import prices and increased real volumes⁶². Annual growth of goods imports in nominal terms was attributable to all groups by use, with the exception of the energy resources group. The groups of raw materials and investment goods had the largest positive contribution to growth of nominal imports. Nominal growth in these two groups was ascribable to the combination of higher real volumes and higher prices compared with the corresponding period of 2020.⁶³ BNB calculations⁶⁴ show that real volumes in the group of energy resources reported a strong decline on an annual basis, while import prices rose.

In the first quarter of 2021 the share of imported goods in Bulgaria from EU Member States remained unchanged from a year earlier at 51 per cent. Imports from EU Member States rose by 9.2 per cent year on year. Machines and chemical products contributed most substantially by commodity group and Germany by country. Imports from non-EU countries grew by 9.9 per cent on an annual basis, with machines and energy resources making the largest positive contribution by commodity group and imports from Turkey and China by country.

The balance of payments data in April 2021 show an accelerated growth rate in nominal imports of goods compared with the first quarter. Real imports of goods are projected to grow strongly on an annual basis in the third and fourth quarters of 2021. This dynamics will largely follow the expectations of domestic demand and exports developments. Import prices are

⁶¹ NSI foreign trade data.

⁶² Non-seasonally adjusted national account GDP data.

⁶³ Real volumes of imports of the raw materials group have been constructed, which includes the commodity groups under the SITC of manufactured goods classified chiefly by materials, inedible (crude) materials (excluding fuels), chemicals and chemical products and imports of the group of investment goods, which includes the group of machines, equipment and vehicles under the SITC. NSI data on import prices of the relevant commodity group and nominal values of imports of the commodity group under the SITC are used.

⁶⁴ Real volumes of imports of mineral fuels, oils and related products have been constructed by using NSI data on import prices of the commodity group and nominal values of imports of the commodity group under the SITC.

Imports of Commodity Groups by Use, January–March 2021

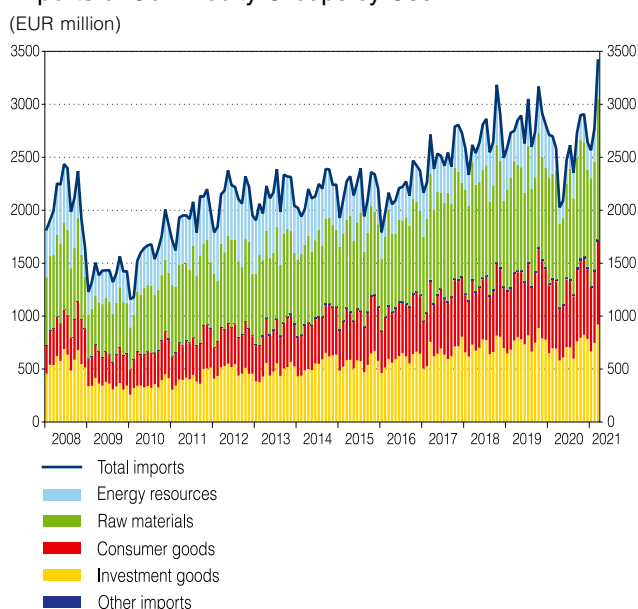
	Value (EUR million)	Change* (EUR million)	Growth** (per cent)	Contribution** (percentage points)
Consumer goods	2048.2	120.7	6.3	1.5
Raw materials	3374.3	363.5	12.1	4.5
Investment goods	2334.5	298.5	14.7	3.7
Energy resources	938.0	-29.9	-3.1	-0.4
Other imports	59.6	9.3	18.4	0.1
Total imports (cif)	8754.6	762.0	9.5	-

* Change on the corresponding period of previous year.

** Growth/contribution to total import growth over the period on an annual basis.

Source: the BNB.

Imports of Commodity Groups by Use



Source: the BNB.

also projected to increase on an annual basis in the third and fourth quarters of 2021, which will also support the nominal change in imports of goods.

Based on balance of payments data for the first four months of 2021, exports and imports of services declined on an annual basis but the rates of decline were much slower than those in 2020. Non-seasonally adjusted national account data for the first quarter of 2021 show that both real and price components contributed negatively to the year-on-year nominal change in exports and imports of services.

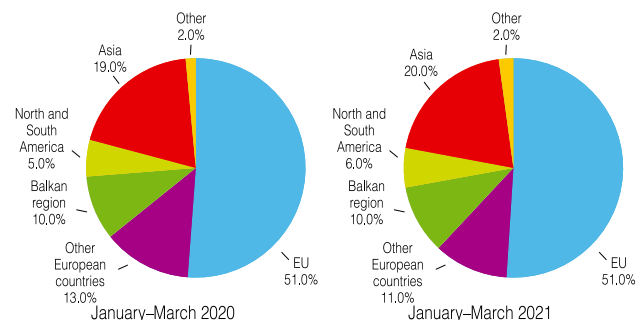
Between January and April services exports declined nominally by 13.1 per cent compared with the corresponding period of 2020 (against a fall of 30.4 per cent in 2020). Lower revenue from travel (-32.1 per cent) and other services⁶⁵ (-9.1 per cent) contributed most strongly to the annual fall, while transport services reported a slight increase. Since the containment measures against the spread of COVID-19 remained effective in Bulgaria and in a number of Bulgaria's trading partners in the first four months of the year, the operation of accommodation establishments remained subdued. The number of foreign nationals' visits to Bulgaria based on NSI data for January–April 2021 fell by 30.1 per cent on an annual basis (against -60.4 per cent for 2020). A faster partial recovery to 2019 levels was recorded in foreign nationals' visits whose purpose is other than holidays or excursions.

In the first four months of 2021 imports of services fell nominally by 11.8 per cent on an annual basis (against a decline of -22.5 per cent for 2020). Other services, falling by -23.7 per cent, and reduced expenditure of Bulgarian nationals on travel (-16.3 per cent) contributed most strongly to this fall. NSI data indicate that the total number of Bulgarians' visits abroad dropped by 7.8 per cent year on year against an annual decline of 43.3 per cent for 2020.

In the third and fourth quarters of 2021 both exports and imports of service in real terms are projected to increase significantly on an annual

⁶⁵ The group of other services includes the sub-groups of construction; insurance and pension services; financial services; telecommunications, computer and information services; other business services; personal services, cultural, recreational and entertainment services; goods and services of the general government not included elsewhere.

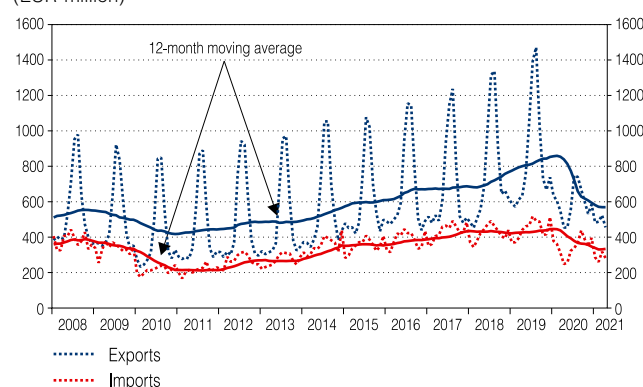
Imports of Goods: Geographical Breakdown



Source: the BNB.

Dynamics of Exports and Imports of Services

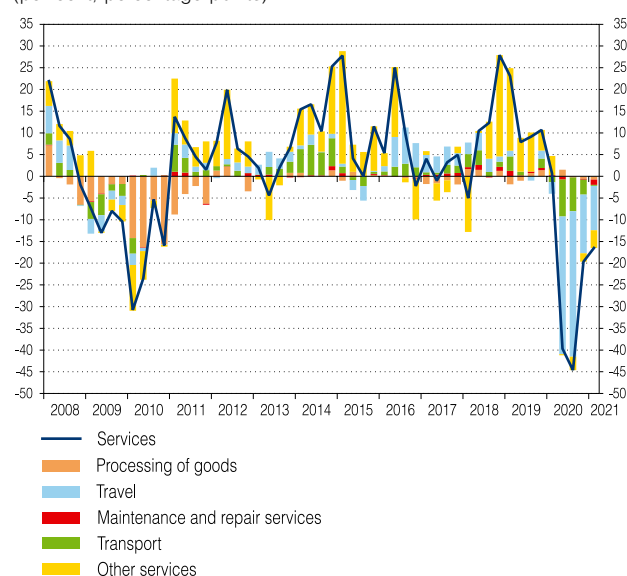
(EUR million)



Source: the BNB.

Annual Change of Services Exports and Contribution by Sub-component

(per cent, percentage points)



Source: the BNB.

basis. The assumption of the removal of most of the containment measures against COVID-19 in Bulgaria and in most of Bulgaria's trading partners in the second half of 2021, and our expectations of domestic and external demand developments in Bulgaria are of key importance for this dynamics.

Behaviour of Firms and Competitiveness

In the first quarter of 2021 the quarterly growth rate of gross value added in Bulgaria accelerated to 2.6 per cent, from 1.4 per cent in the previous quarter. The services sector continued to make the major positive contribution to value added growth, followed by agriculture, while industry contributed negatively.

Real value added in industry went down by -1.1 per cent on a quarterly basis in the first quarter (a trend observed from the second half of 2019) driven by the downturn in the economic activity both in manufacturing and construction. Despite the downward dynamics in gross value added of manufacturing, in the first three months of 2021 the industrial production index (in real terms) and the index of real turnover in manufacturing (both in domestic and external markets) exhibited a rise. The construction production index obtained from the NSI's short-term business statistics also reported quarterly growth between January and March 2021, reflecting the positive contribution of both the civil/engineering and building construction.⁶⁶ These inconsistencies between short-term business statistics data and national accounts are likely to reflect differences in the scope and sources of information, as well as the preliminary nature of national accounts data⁶⁷. The information available for this period could be interpreted as a sign of an uneven recovery of the economic activity in industry amid the extension of the measures against the spread of COVID-19.

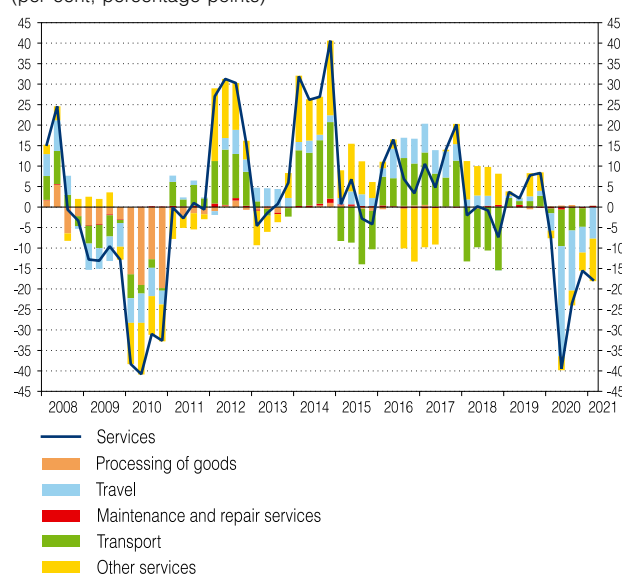
Services value added rose by 2.2 per cent quarter on quarter in the first quarter of 2021 (against 0.9 per cent in the previous quarter).

⁶⁶ Building construction include construction of residential and non-residential buildings. Civil engineering construction covers infrastructure construction of roads, bridges, pipes, power lines, telecommunications and other construction works.

⁶⁷ According to the NSI data dissemination calendar, revised data on GDP and its components for 2020 and for the first nine months of 2021 is expected to be published in October 2021, containing new or updated statistical information.

Annual Change of Services Imports and Contribution by Sub-component

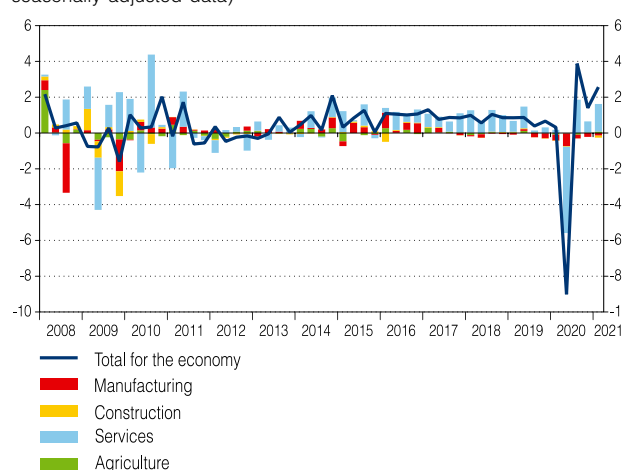
(per cent, percentage points)



Source: the BNB.

Rate of Change in Real Value Added and Contribution by Sub-sector

(per cent, percentage points, quarter on quarter; seasonally adjusted data)



Note: Non-additive data on contributions due to direct seasonal adjustment of value added and its components.

Sources: the NSI, BNB calculations.

The main contributor to this was the sub-sector of trade, transport, hotels and restaurants which continued to gradually recover after the shock in 2020 caused by the measures against the COVID-19 pandemic⁶⁸. Data on the services production index⁶⁹ providing a more detailed breakdown for the trade, transport, hotels and restaurants sub-sector suggest that in the first quarter the containment measures affected adversely only restaurants, while the economic activity in other sub-sectors improved compared with the previous quarter in line with growth in final consumption expenditure of households.

NSI data on short-term business statistics on production and turnover in manufacturing, trade and construction production for April–May 2021 give grounds to expect a quarterly rise in gross value added in the respective sectors over the second quarter of the year. Nominal manufacturing turnover in April and May increased from the previous quarter owing mainly to the real component (higher volume of sales in external and domestic markets). Seasonally adjusted industrial production index on average for April–May 2021 also increased from the first quarter of 2021 driven by positive developments in all main sub-sectors: mining and quarrying, manufacturing, and production and distribution of electricity and heating and gas. On average, the construction production index for April–May 2021 went up compared with the first quarter. NSI Business Situation Survey data show that this trend is stable and reflects increased assuring of firms' production with orders from Bulgaria and abroad. In April and May retail trade turnover increased further at both constant and current prices on a quarterly basis.

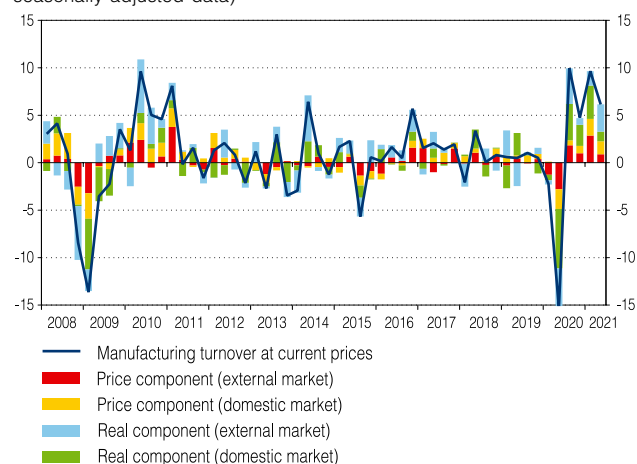
According to seasonally adjusted NSI national account data employment in the total economy fell by -0.7 per cent quarter on quarter in the first quarter of 2021. Agriculture contributed negatively to the change in employment over the quarter (due to fewer self-employed), while services and the two industry sub-sectors (manufacturing and construction) reported growth. Employment growth in the export-oriented sector of industry and in the services sector could be

⁶⁸ In the first quarter of 2021 value added in the sub-sector of trade, transport, hotels and restaurants remained 8.5 per cent lower than that in the first quarter of 2020 at constant prices.

⁶⁹ Eurostat seasonally adjusted data are used.

Manufacturing Turnover Dynamics

(per cent, percentage points, quarter on quarter; seasonally adjusted data)



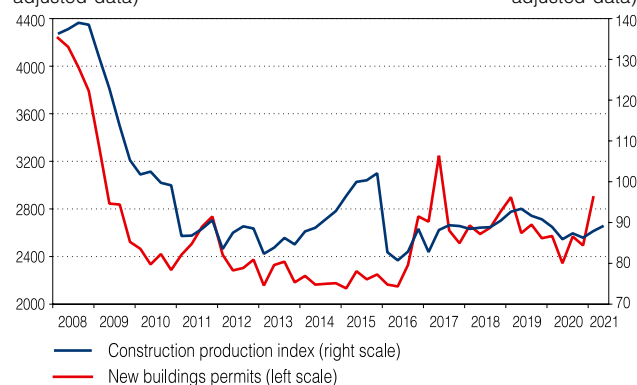
Note: Data for the second quarter are until May 2021.

Sources: the NSI, BNB calculations.

Construction Production Dynamics and New Buildings Permits Issued

(number of buildings; seasonally adjusted data)

(2015 = 100; seasonally adjusted data)

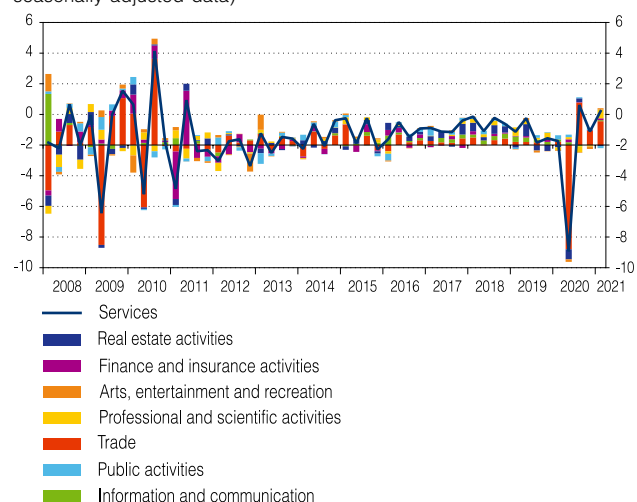


Note: Data on construction production index are until May 2021.

Sources: the NSI, BNB calculations.

Services Value Added Rate of Change and Contribution by Sub-sector

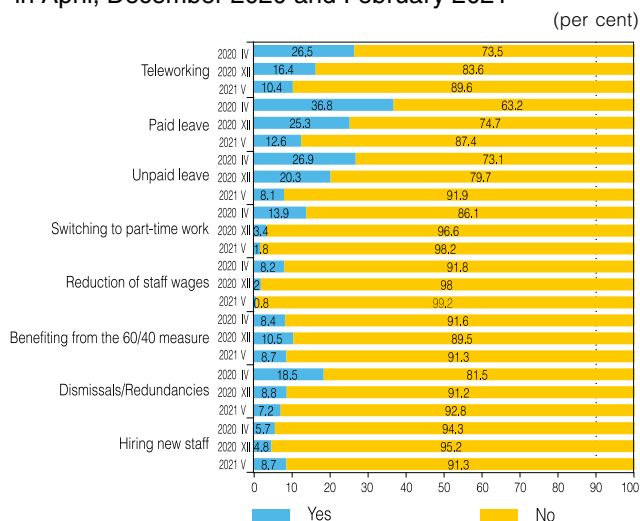
(per cent, percentage points, quarter on quarter; seasonally adjusted data)



Note: Non-additive data on contributions due to direct seasonal adjustment of value added and its components.

Sources: the NSI, BNB calculations.

Measures Taken by the Firms in Relation to Their Staff in April, December 2020 and February 2021



Note: Based on NSI targeted survey data on the activity and position of non-financial corporations amid an epidemic situation.

Source: the NSI.

explained by increased external and domestic demand for goods and services in the first quarter of the year⁷⁰. The increase in employment in the services sector was largely driven by the sub-sectors of information and communication⁷¹ and general government⁷².

In the first quarter of 2021 the total number of worked man-hours fell by 0.2 per cent on a quarterly basis. The slower decline compared with employment reflected an increase in worked man-hours *per* employee in all sectors of the economy. The upward dynamics in worked man-hours can be possibly explained by the return of some of the employees to full-time work in the sectors which continue to recover from the negative effects of the pandemic.⁷³ According to the Employment Agency data seasonally adjusted by the BNB, in April–June 2021 the total number of registered unemployed declined from the first quarter of 2021, which was attributable to the fall in newly registered unemployed and to the rise in the number of recruited unemployed persons. These developments and the projected increase in the economic activity in the second half-year of 2021 compared with the first one will

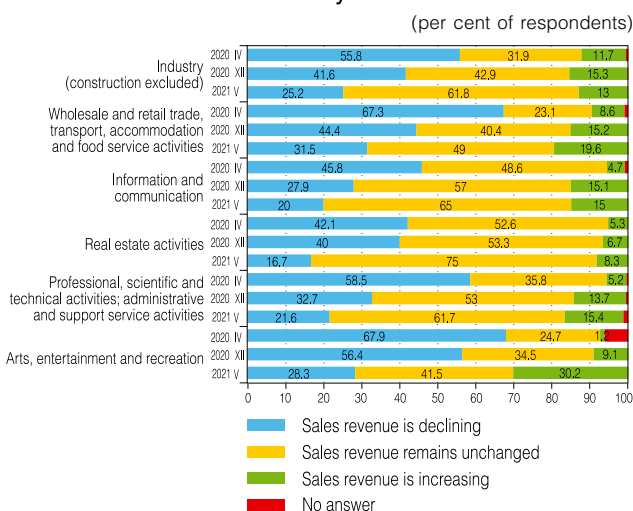
⁷⁰ For details, see the Current Economic Environment Section in Chapter 3.

⁷¹ This refers to the sub-sector of information and communication.

⁷² This refers to the sub-sector of general government, education, and human health and social work activities.

⁷³ Based on NSI survey data on the effects of the state of emergency on the business. For details, see [survey results](#) on the NSI website.

Changes in Firms' Revenue from Sales in April, December 2020 and February 2021

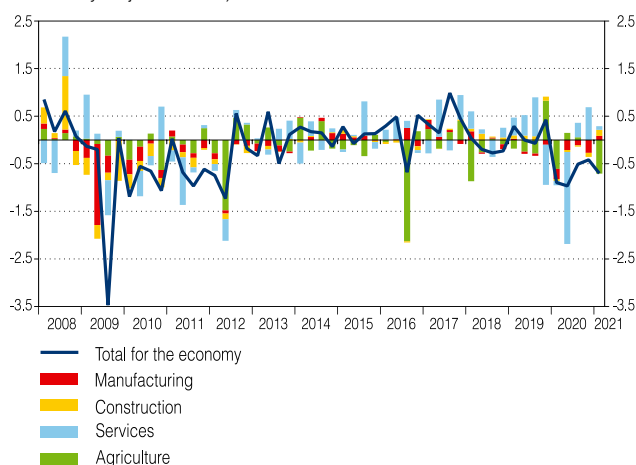


Note: Based on NSI targeted survey data on the activity and position of non-financial corporations amid an epidemic situation.

Source: the NSI.

Contribution to Changes in the Number of Employed by Economic Sector

(per cent, percentage points, quarter on quarter; seasonally adjusted data)

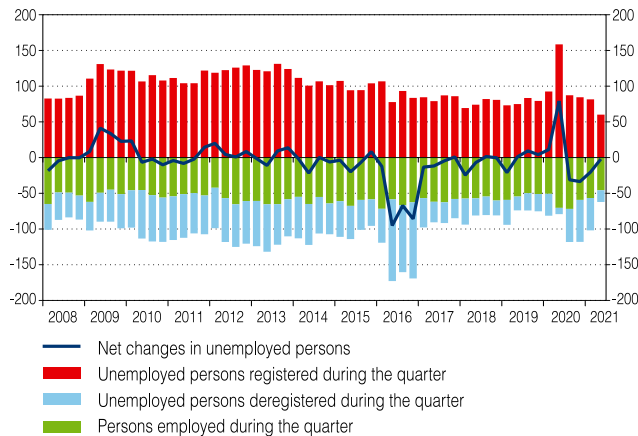


Note: Non-additive data on contributions due to direct seasonal adjustment of the total amount and its components.

Sources: the NSI, BNB calculations.

Changes in the Number of Unemployed Persons

(number of persons (thousand); seasonally adjusted data)



Sources: Employment Agency, BNB calculations.

be a precondition for moderate quarterly growth of employment in the following months combined with a gradually decreasing unemployment rate.

An increase in value added amid decreasing employment was the major reason behind the 3.3 quarterly rise of labour productivity⁷⁴ in the total economy over the first quarter of 2021 driven mainly by the services sector. Assuming a persistent easing of containment measures, improvement of the economic activity and continued switching of employees from part-time to full-time work, labour productivity is expected to grow further on a quarterly basis in the third and fourth quarters of 2021.

In line with increased labour productivity the quarterly growth rate of compensation *per* employee in nominal terms accelerated to 3.7 per cent in the first quarter of 2021 compared with 0.5 per cent in the previous quarter. In addition to higher labour productivity, other factors supporting wage growth in the total economy involved the increase in the minimum wage by 6.6 per cent⁷⁵ from the beginning of the year, enhanced economic activity over the period and the return of part of employees from part-time to full-time work⁷⁶. All main sectors contributed to the quarter-on-quarter increase in remunerations in the total economy over the first quarter, with the strongest rise registered in the sector of industry, followed by that of services.

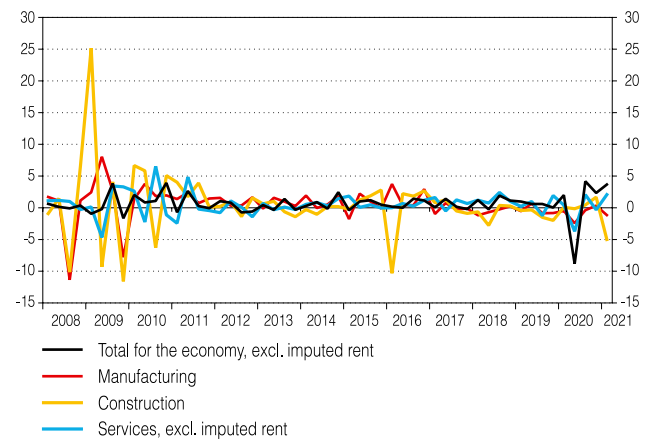
⁷⁴ Labour productivity is calculated after adjusting gross value added for imputed rent.

⁷⁵ From the beginning of 2021 the minimum wage was raised from BGN 610 to BGN 650.

⁷⁶ According to NSI surveys.

Labour Productivity Dynamics (Value Added *per* Employee)

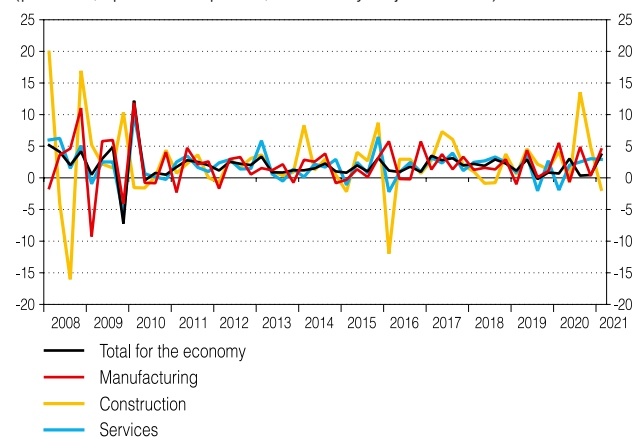
(per cent, quarter on quarter; seasonally adjusted data)



Source: the NSI.

Compensation *per* Employee at Current Prices

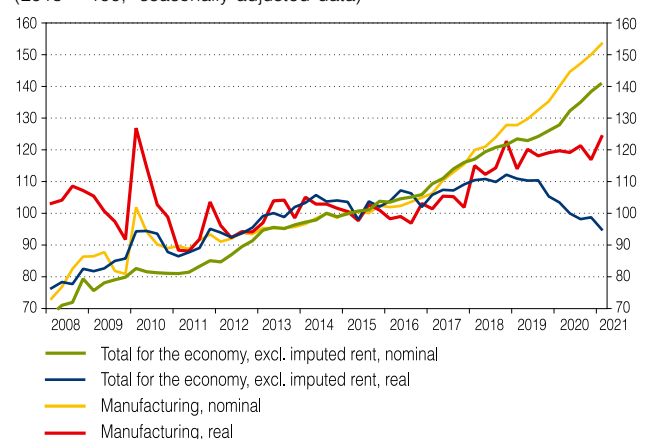
(per cent, quarter on quarter; seasonally adjusted data)



Sources: the NSI, BNB calculations.

Unit Labour Costs

(2015 = 100; seasonally adjusted data)



Sources: the NSI, BNB calculations.

Corporations' positive expectations of hiring new employees in the following three months and the projected improvement of the economic activity in the second half of 2021 are a precondition for the compensation *per* employee to increase further on a quarterly basis in the following months.

According to seasonally adjusted data, developments in compensation *per* employee and labour productivity in the first quarter of 2021 led to an increase in unit labour costs⁷⁷ in nominal terms. The increase in nominal unit labour costs compared with the previous quarter was most strongly pronounced in the industry sub-sector of construction, followed by the services sub-sectors of general government and information and communication.

In the first quarter of 2021 gross operating surplus remained close to its previous quarter's level according to seasonally adjusted data. However, developments across sub-sectors were divergent. In line with value added developments the services sector had the main positive contribution to the change in the operating surplus, in particular the sub-sector of trade, transport, hotels and restaurants. An improvement in financial performance from the previous quarter was reported in agriculture, while the gross operating surplus in industry posted a fall.

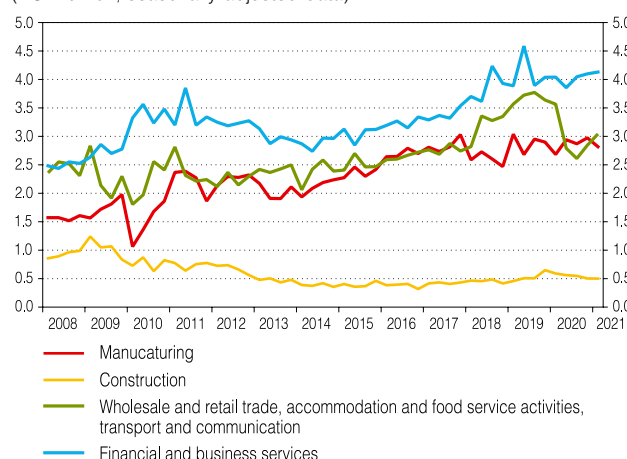
In the first quarter of 2021 external sources of financing used by corporations posted a decline. Across economic sectors manufacturing exhibited a stronger contraction of attracted funds between January and March 2021, while the amount of external financing of corporations from the services sector rose. From the perspective of the type of sources, attracted foreign funds for the total economy (FDI and other foreign liabilities) posted a decline, which was partly compensated by increased bank loans and financial leasing.

GDP growth decomposition by production factor suggests that higher total factor productivity was the main contributor to quarterly growth of the economic activity in the first quarter. Capital had a low positive contribution in line with slow growth of investment activity in January–March 2021. Concurrently, the decrease in hours worked *per* person was the reason for labour to

⁷⁷ Unit labour costs are calculated after adjusting gross value added for imputed rent.

Gross Operating Surplus at Current Prices

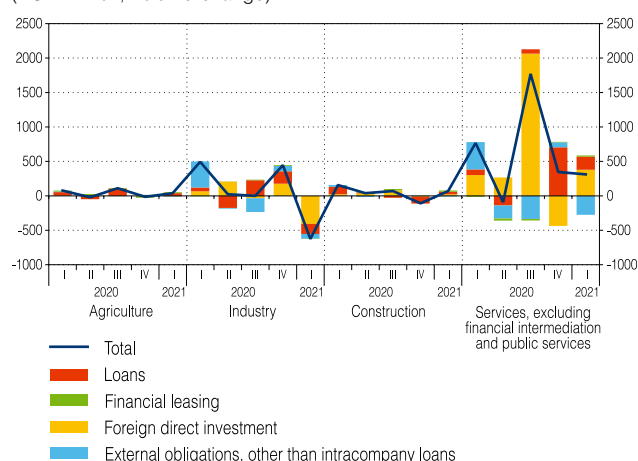
(BGN billion; seasonally adjusted data)



Sources: the NSI, BNB calculations.

Financing Sources*

(BGN million, volume change)



* Sources of financing other than gross operating surplus.

Source: the BNB.

Contribution of the Change in Production Factors to GDP Growth

(per cent, percentage points, quarter on quarter; seasonally adjusted data)



Sources: the NSI, BNB calculations.

Gross Value Added Change

(per cent, on a quarterly basis; real rate, seasonally adjusted data)

	2017				2018				2019				2020				2021
	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	I
Agriculture, forestry and fishing	6.0	0.5	1.4	0.7	-2.4	-1.5	0.9	0.1	0.7	2.5	0.6	-0.4	-1.9	-0.5	-1.9	0.4	1.7
Mining and quarrying; manufacturing; electricity, gas, steam and air conditioning supply; water supply; sewerage, waste management and remediation activities	0.0	1.1	-0.1	-0.5	-0.3	-0.8	-0.2	-0.3	-0.4	0.4	-1.1	-1.3	-1.6	-3.4	-0.9	-1.0	-0.7
Construction	1.1	1.1	0.0	-0.3	0.5	-0.3	0.8	1.3	0.9	1.3	-0.1	-0.5	-0.6	-0.9	0.0	0.1	-2.9
Wholesale and retail trade; repair of motor vehicles and motorcycles; transportation and storage; accommodation and food service activities	0.8	0.6	0.4	1.4	1.5	0.1	1.0	1.3	0.7	0.6	0.6	0.1	0.7	-21.8	10.6	3.4	5.4
Information and communication	-0.4	3.3	2.7	2.8	2.1	2.9	2.9	3.5	3.7	2.9	1.8	1.8	1.4	1.8	-0.8	-0.1	0.7
Financial and insurance activities	-0.9	-0.4	2.0	-1.8	2.2	0.0	1.5	0.7	0.4	1.0	-0.2	2.6	-0.1	2.0	0.2	0.0	1.1
Real estate activities	2.1	2.5	-0.7	4.6	3.6	1.3	3.5	2.5	-1.0	4.8	-2.0	-2.4	-0.9	-4.2	1.6	0.3	-0.4
Professional, scientific and technical activities; administrative and support service activities	0.4	0.1	1.0	2.2	2.6	2.0	3.2	0.1	6.0	2.3	1.2	3.6	-1.9	1.4	-3.5	-0.9	5.6
Public administration, education, human health and social work activities	2.7	0.2	0.9	0.9	0.6	1.1	0.7	0.8	-0.4	-0.1	0.9	0.2	1.4	0.8	0.3	0.7	-0.7
Culture, sport and entertainment; other activities; activities of households as employers; non-identified activities of households producing goods and services for own use; activities of extraterritorial organisations and bodies	2.3	0.7	2.7	0.3	1.0	-0.6	1.0	-0.4	-0.8	5.0	-3.7	-0.7	-1.3	-4.8	-0.9	-4.8	3.2
Gross value added, total for the economy	1.3	0.8	0.9	0.8	1.0	0.6	1.0	0.9	0.8	0.9	0.4	0.7	0.3	-9.0	3.9	1.4	2.6

Source: the NSI.

Gross Value Added Change

(per cent, on an annual basis)

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Agriculture, forestry and fishing	31.8	-8.9	-11.9	5.9	-11.1	3.5	7.0	-7.9	7.7	9.0	-2.0	4.1	-5.3
Mining and quarrying; manufacturing; electricity, gas, steam and air conditioning supply; water supply; sewerage, waste management and remediation activities	2.3	-7.4	-4.9	7.7	3.0	0.1	3.8	3.2	7.3	3.3	-1.5	-1.2	-5.2
Construction	15.1	6.8	-18.7	-4.0	-4.5	0.3	-3.4	4.3	-7.3	4.5	1.4	3.6	-1.0
Wholesale and retail trade; repair of motor vehicles and motorcycles; transportation and storage; accommodation and food service activities	-2.9	-4.3	13.6	3.1	-0.2	3.7	0.7	7.1	1.0	2.8	3.9	3.1	-11.9
Information and communication	74.2	-2.5	0.3	12.4	-3.2	2.1	0.7	2.2	16.5	6.1	10.6	13.1	0.6
Financial and insurance activities	10.5	13.2	24.7	-3.3	-4.7	-7.5	0.0	-0.9	6.9	1.0	2.7	3.0	2.5
Real estate activities	-5.0	1.2	3.6	0.0	2.9	-2.2	2.2	2.4	5.9	7.2	11.4	4.9	-3.5
Professional, scientific and technical activities; administrative and support service activities	-7.8	7.7	-7.1	2.6	-3.8	3.3	1.0	9.8	1.7	1.3	9.0	12.7	-6.6
Public administration, education, human health and social work activities	1.0	0.9	2.8	-2.6	3.0	-5.1	4.1	2.2	-3.1	5.8	3.1	0.3	5.9
Culture, sport and entertainment; other activities; activities of households as employers; non-identified activities of households producing goods and services for own use; activities of extraterritorial organisations and bodies	33.9	7.1	-15.2	15.6	-6.1	1.7	2.4	8.7	-0.2	5.5	2.6	1.1	-15.6
Gross value added, total for the economy	6.2	-1.0	0.8	2.6	-0.4	-0.2	2.2	3.5	3.5	4.2	3.5	3.3	-4.3

Source: the NSI.

make a slightly negative contribution to the quarterly rate of change in real GDP.

Household Behaviour

In the first quarter of 2021 household consumption rose on a quarterly basis, underpinned by the improved consumer sentiment and stronger income growth combined with a lower savings rate.

The NSI Labour Force Survey shows that labour force fell both on a quarterly and annual basis in the first quarter of 2021⁷⁸ as a result of a continuous decrease in the number of employed. Concurrently, the decline in labour force reflected in a slight decrease in the labour force participation rate⁷⁹.

The Labour Force Survey shows that the seasonally adjusted unemployment rate⁸⁰ rose to 6 per cent in the first quarter of 2021, from 5.7 per cent in the fourth quarter 2020 (according to non-seasonally adjusted data the unemployment rate increased to 6.3 per cent against 5.2 per cent in the fourth quarter), which was probably due to methodological changes. Concurrently, administrative statistics data of the Employment Agency has reported a fall in the unemployment rate⁸¹ to an average of 6.3 per cent in the first quarter of 2021, from 7.0 per cent in the fourth quarter of 2020. Since early 2021 the NSI made changes to Labour Force Survey methodology concerning mainly the definitions of employed and unemployed persons⁸². Concurrently, the changes made were not reflected in data for previous periods. As a result Labour Force Sur-

⁷⁸ Quarterly growth is calculated based on BNB seasonally adjusted data.

⁷⁹ The labour force participation rate is the proportion between economically active persons (labour force) and the population of the respective age.

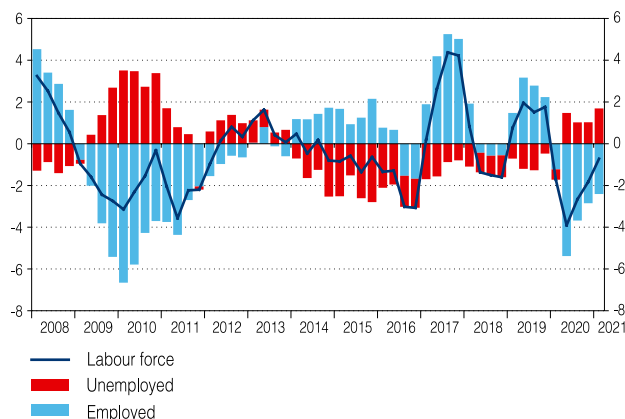
⁸⁰ The unemployment rate is the proportion between the number of unemployed and the labour force based on Labour Force Survey data. The series is seasonally adjusted by the BNB.

⁸¹ The definition of unemployment rate according to Employment Agency data corresponds to that referred to in note 79, but using a constant rate of labour force, comprising the number of persons in the respective age group since the last census of the population. Employment Agency data on the unemployment rate are not directly comparable to NSI Labour Force Survey data on the unemployment rate. The series is seasonally adjusted by the BNB.

⁸² For further information, see the methodological notes in the NSI's [press release](#).

Contribution to the Change in Labour Force by Component

(per cent, percentage points; on an annual basis)

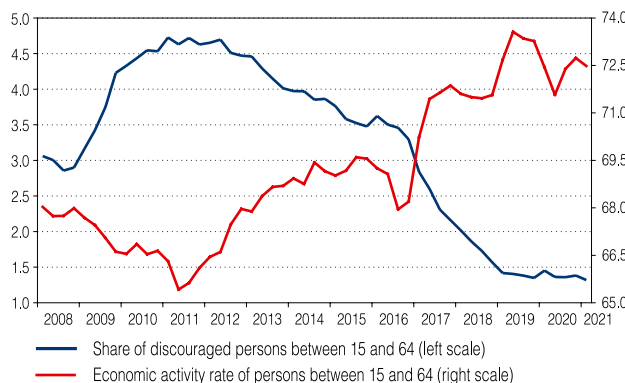


Sources: the NSI, BNB calculations.

Economic Activity and Share of Discouraged Persons

(per cent, seasonally adjusted data)

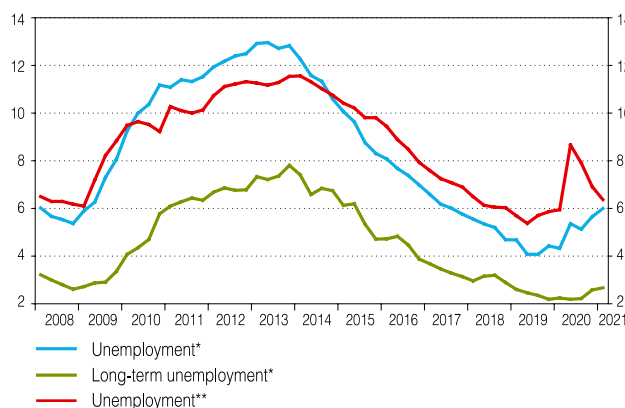
(per cent, seasonally adjusted data)



Sources: NSI Labour Force Survey, BNB calculations.

Unemployment Rate

(per cent, share of labour force; seasonally adjusted data)

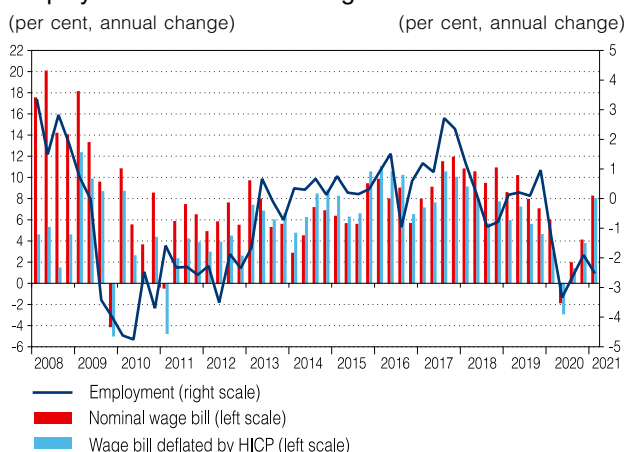


* NSI data.

** Employment Agency data.

Sources: NSI Labour Force Survey, the Employment Agency, BNB calculations.

Employment and Nominal Wage Bill



Sources: the NSI – SNA, BNB calculations.

vey data for the first quarter of 2021 are not directly comparable to those for 2020.

In the first quarter of 2021 labour income of employed accelerated both in nominal and real terms and on a quarterly and annual basis according to the NSI national account wage bill data. The wage⁸³ per employee also grew on an annual basis in line with the slower decline in employees, increased minimum wage from the beginning of the year and higher public sector remunerations. Concurrently, the decline in employment deepened on an annual basis due mainly to the reported decrease in the number of self-employed persons in agriculture.

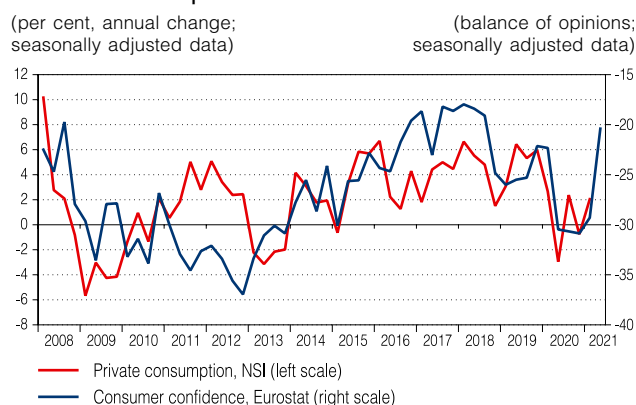
Higher income and increased consumer confidence led to 2 per cent real growth on an annual basis of private consumption in the first quarter of 2021. Retail trade turnover also posted a quarter-on-quarter increase in real terms, with food and non-food goods contributing to growth. Despite the slower rise in retail trade turnover in April and May 2021, the continuous decline in the unemployment rate (to 5.8 per cent in the second quarter of 2021 according to Employment Agency data), increased consumer confidence and easing of containment measures against the spread of COVID-19 in Bulgaria from the second quarter of the year gave signs of growth in private consumption.

The NSI Household Budget Survey shows that household savings as a share of income⁸⁴ (seasonally adjusted data) decreased in the

⁸³ According to the NSI national account wage bill data.

⁸⁴ Income is the gross income less taxes and social security contributions.

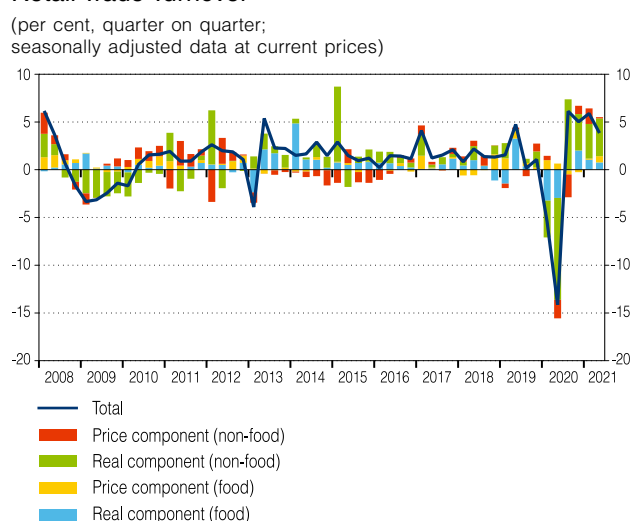
Private Consumption and Consumer Confidence



Note: Quarterly data on consumer confidence represent the average monthly values of Eurostat consumer confidence indicator.

Sources: the NSI, Eurostat, BNB calculations.

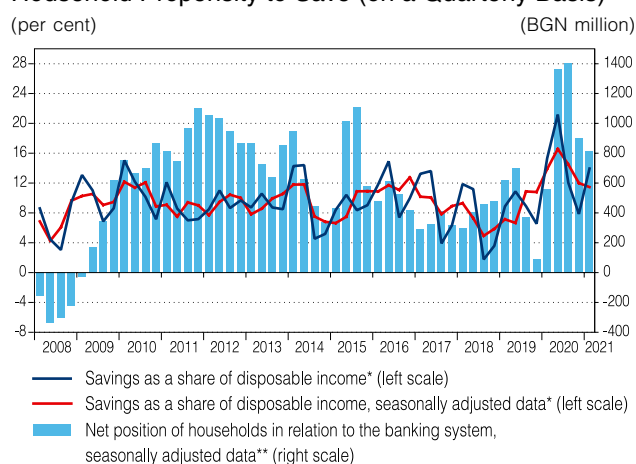
Retail Trade Turnover



Notes: Non-additive data on contributions due to direct seasonal adjustment of the total amount and its components. Data for the second quarter of 2021 represent the quarterly change of the average value of the indicator for April and May compared to the first quarter of 2021.

Sources: the NSI, BNB calculations.

Household Propensity to Save (on a Quarterly Basis)



* BNB data.

** NSI data.

Sources: NSI Household Budget Survey, the BNB.

Employment and Income Dynamics

	2017				2018				2019				2020				2021
	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	I
(per cent, quarter on quarter; seasonally adjusted data)																	
Employed persons	0.3	0.1	1.0	0.4	0.0	-0.2	-0.3	-0.2	0.3	0.0	-0.1	0.4	-0.9	-1.0	-0.5	-0.4	-0.7
Nominal wage <i>per employee</i> *	3.1	2.8	3.0	2.0	2.2	1.8	3.0	2.2	1.1	2.9	-0.5	0.8	0.8	3.5	0.7	0.4	3.7
Real wage <i>per employee</i> **	2.5	2.5	2.9	1.1	1.6	1.1	1.9	1.7	0.7	2.0	-1.3	0.6	0.1	4.6	1.0	0.6	1.8
Wage bill, nominal terms	3.1	2.5	3.2	2.2	2.8	2.0	2.5	2.6	1.3	3.7	0.2	0.6	0.5	-1.2	1.8	1.4	4.4
Wage bill, real terms**	2.5	2.2	3.2	1.3	2.2	1.3	1.5	2.1	1.0	2.7	-0.5	0.4	-0.2	-0.2	2.2	1.6	2.4
(per cent, on corresponding quarter of previous year, non-seasonally adjusted data)																	
Employed persons	1.2	0.9	2.7	2.4	1.2	0.2	-0.9	-0.8	0.1	0.2	0.1	1.0	-1.3	-3.3	-2.6	-1.9	-2.5
Nominal wage <i>per employee</i> *	6.9	9.3	11.3	11.7	9.4	9.0	9.5	10.3	8.0	8.5	5.1	5.7	5.9	2.9	6.1	6.8	10.3
Real wage <i>per employee</i> **	6.1	7.8	10.4	9.8	7.7	6.5	5.6	7.1	5.4	5.6	2.8	3.3	2.9	1.8	5.5	6.5	10.1
Wage bill, nominal terms	8.0	9.1	11.5	12.0	10.9	10.6	9.5	10.9	8.6	10.2	8.0	7.1	6.0	-1.9	2.0	4.1	8.3
Wage bill, real terms**	7.2	7.6	10.6	10.1	9.1	8.0	5.7	7.7	6.0	7.3	5.6	4.7	2.9	-2.9	1.4	3.8	8.0

Employment and Income Dynamics

(per cent, on an annual basis)

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Employed persons	2.4	-1.7	-3.9	-2.2	-2.5	-0.4	0.4	0.4	0.5	1.8	-0.1	0.3	-2.3
Nominal wage <i>per employee</i> *	13.5	10.6	12.0	6.5	8.0	8.3	5.6	5.8	6.2	9.9	9.6	6.8	5.4
Real wage <i>per employee</i> **	1.6	8.1	8.7	3.0	5.4	8.0	7.4	6.9	7.6	8.6	6.7	4.2	4.2
Wage bill, nominal terms	16.3	8.3	7.1	4.9	6.0	7.1	5.4	6.8	8.1	10.2	10.5	8.4	2.5
Wage bill, real terms**	4.0	5.8	4.0	1.4	3.5	6.7	7.2	8.0	9.5	8.9	7.6	5.8	1.3

* The wage is calculated according to NSI data (SNA), with social security contributions paid by the employer deducted from the compensation *per employee* and the difference divided by the number of employees.

** Data deflated by HICP.

Sources: NSI – SNA, BNB calculations, Eurostat.

Retail Trade Turnover

(per cent, quarter on quarter; seasonally adjusted data at constant prices)

	2017				2018				2019				2020				2021	
	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II
Retail trade, excluding motor vehicles and motorcycles	2.4	0.5	1.4	1.1	0.1	1.5	0.2	1.0	2.1	1.5	0.4	2.1	-6.6	-11.6	4.5	4.8	5.6	3.7
incl.																		
Food, drinks and tobacco products	0.2	0.4	1.5	3.2	1.2	2.7	1.0	-3.0	-4.0	8.8	1.0	0.0	-8.8	-8.0	-0.2	5.4	2.9	2.1
Textile, clothing, footwear and leather	12.6	-2.7	-5.3	0.5	3.9	6.4	1.8	4.9	-1.2	-4.2	3.1	4.1	-18.5	-43.0	62.6	-6.6	25.9	-1.0
Household appliances, furniture and other household goods	1.0	2.9	1.5	1.2	1.3	3.2	1.5	0.9	4.1	2.4	2.7	4.2	-8.5	-6.7	14.8	5.2	0.7	-2.2
Computer and communication equipment, etc.	-1.8	0.5	0.5	2.1	6.6	1.9	-1.9	-4.0	4.9	0.9	2.1	0.2	-13.6	-14.0	18.3	9.4	6.2	-1.2
Pharmaceutical and medical goods, cosmetics and toiletries	0.9	2.4	1.3	1.3	-1.6	2.0	1.6	2.3	-17.3	0.7	1.5	1.9	5.5	-19.4	9.0	7.9	3.0	11.5
Unspecialised shops with different kinds of goods	4.2	2.0	2.1	0.3	4.2	2.9	0.3	0.1	9.6	2.4	0.0	-0.4	-2.7	-4.1	-1.0	11.4	-2.4	13.3
Automobile fuels and lubricants	6.8	-2.3	1.2	-1.1	-7.6	3.5	-0.9	6.0	7.0	-1.8	-0.9	0.2	-10.5	-24.0	18.3	-0.7	3.7	5.8

* Data for the second quarter of 2021 are for April and May.

Source: the NSI: short-term business statistics.

Retail Trade Turnover

(per cent, on an annual basis)

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Retail trade, excluding motor vehicles and motorcycles incl.	8.9	-7.7	-8.4	0.6	5.3	3.8	10.2	11.8	6.1	5.4	3.3	5.6	-10.6
Food, drinks and tobacco products	1.6	8.7	2.0	2.5	4.8	1.5	21.9	7.2	7.3	3.7	2.6	5.2	-10.9
Textile, clothing, footwear and leather	19.7	-9.0	6.9	3.0	7.2	10.9	7.8	4.1	9.7	9.1	8.2	4.6	-29.8
Household appliances, furniture and other household goods	6.8	-23.3	-16.5	-4.8	10.0	4.3	1.9	3.0	5.1	7.1	6.5	10.7	-0.8
Computer and communication equipment, etc.	17.3	-24.7	-1.6	-0.4	-4.8	5.9	-3.8	10.1	2.2	6.8	7.8	3.2	-12.6
Pharmaceutical and medical goods, cosmetics and toiletries	21.8	13.6	7.9	7.6	8.9	11.3	12.2	9.7	10.7	6.7	3.8	-13.3	-2.0
Unspecialised shops with different kinds of goods	31.0	59.0	21.1	6.5	5.7	5.6	5.7	4.3	5.0	11.2	7.7	12.6	-4.0
Automobile fuels and lubricants	5.3	-8.5	-29.6	-2.7	6.2	-1.6	6.7	34.6	2.5	1.9	-5.3	10.4	-21.2

Source: the NSI: short-term business statistics.

first quarter of 2021 in line with the increased consumer expenditure. Over the same period the household net position *vis-à-vis* the banking system also posted a fall from the previous quarter.

The gradually improving external environment and strengthening economic activity in Bulgaria are expected to reflect in higher labour demand and supply, and to underpin growth in household consumption in the third and fourth quarters of 2021.

Fiscal Policy Effects on the Economy

In the first quarter of 2021 the fiscal policy effects on the economic activity in Bulgaria reflected largely the transfers to households and subsidies to corporations under subsidised employment programmes in the context of the crisis caused by the spread of COVID-19. At the same time, general government sector's consumption and investment⁸⁵ declined on a quarterly basis over the first quarter of the year.

Monthly data on consolidated fiscal programme (CFP) performance for January–May 2020 indicate a strong positive effect of the fiscal policy on the economic activity at the end of the first five months of 2021. This reflects mainly the sizeable increase in social and health insurance expenditure, higher expenditure on wages and subsidies, and growth in capital expenditure funded by the national budget. Social expenditure, significantly increased public sector wages

⁸⁵ BNB calculations on the quarterly rate of change in government investment, for which quarterly non-financial accounts of the general government sector, published by the NSI, are used.

and government subsidised employment programmes support household disposable income having a potential positive effect on the economic activity through stronger private consumption.

At the end-May 2021 the CFP budget balance was negative at BGN -140.6 million. Compared with the first five months of the previous year the balance on the consolidated fiscal programme fell by BGN 1454 million⁸⁶, reflecting growth in total budget expenditure by 26.3 per cent and an increase in total budget revenue by 16.1 per cent in May 2021. The budget deficit reflected mainly the expenditure made under the 2021 State Budget Law and expenditure associated with the extension of discretionary measures related to the pandemic, such as monthly supplement payments to pensions in the amount of BGN 50 for each pensioner.

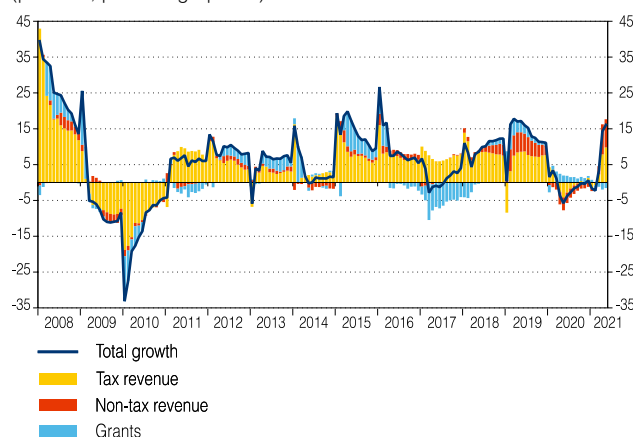
After a fall of -2.3 per cent in February, total CFP revenue posted a 3.4 per cent rise in March, which accelerated to 16.1 per cent in May. These developments followed largely the dynamics of tax revenue, which from a low annual decline in early year exhibited an increase, accelerating to 12.3 per cent in May. Non-tax revenue also contributed to growth in total budget revenue, posting a strongly accelerating rise to 60.6 per cent in May. The strong increase in tax and non-tax revenue reflected the concession remuneration for Sofia airport received in April 2021 in the amount of BGN 660 million (VAT inclusive). The upward dynamics in tax revenue was also influenced by the base effect of the containment measures and extended deadlines for payment of particular direct taxes in the previous year. Revenue from grants declined by -20.1 per cent on an annual basis in May, with the fall accelerating compared to that in March (-15.7 per cent).

Growth in tax revenue was mainly driven by strongly accelerated annual growth of VAT revenue to 19.0 per cent in May, with the tax received from the Sofia airport concession payment and relatively low base in the corresponding period of 2020 contributing to this effect. Nominal annual growth in private consumption in the first quarter of the year also favoured

⁸⁶ Based on Ministry of Finance Monthly Bulletins on state budget performance and major CFP indicators for 2020 and 2021. BNB calculations.

Contributions of Major Groups of Revenue to Growth in Total Revenue and Grants, Cumulatively (on an Annual Basis)

(per cent; percentage points)



Sources: the MF, BNB calculations.

the increase in VAT revenue. VAT receipts from domestic and intra-Community acquisitions (net), accelerating their growth to 23.3 per cent in May (from 12.8 per cent in March), contributed most strongly to VAT revenue growth.⁸⁷ Concurrently, the fall of VAT revenue from imports turned to growth of 10.5 per cent in May⁸⁸ driven by the strong rise in oil prices.

From the beginning of the year the annual growth rate of social and health insurance revenue gradually accelerated, reaching 9.6 per cent in May⁸⁹. Personal income tax revenue also posted growth (13.6 per cent) year on year in May. Government measures in support of employment, higher public sector wages and increased minimum wage and minimum insurance threshold of self-employed persons since early year had a positive effect on the dynamics of revenue from social and health insurance, and personal income tax. Accelerated growth in private sector wages in the first quarter of the year also contributed to this dynamics. The contribution of corporate tax revenue to the rise in total budget revenue in May was minimal.

Following the downward trend in the rate of decline from the beginning of the year excise revenue grew by 1.6 per cent on an annual basis at the end of May. Tobacco excise revenue posted a lower decline to -2.3 per cent, while fuel excise revenue rose by 6.5 per cent, with higher oil prices acting as a main driver.

In the first five months of 2021 annual growth of total CFP expenditure accounted for 26.3 per cent, remaining close to that reported at the

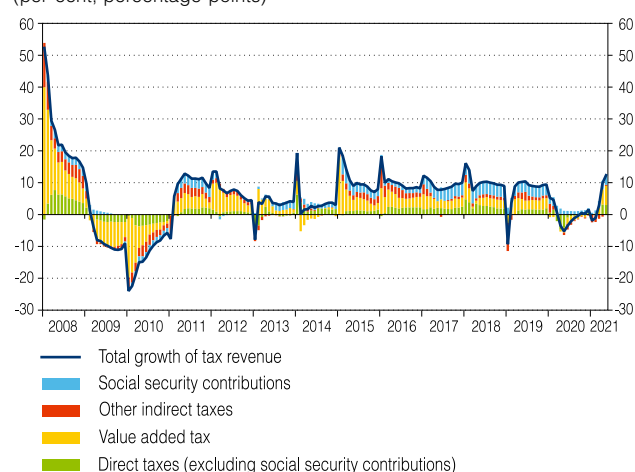
⁸⁷ Based on MF Monthly Bulletin on Budget Performance and Major Indicators under the Consolidated Fiscal Programme for May 2021, VAT revenue growth from domestic and intra-Community acquisitions was reported despite the expected negative budget effects as a result of lowered tax rates from 20 to 9 per cent on particular goods and services, effective for the period from the beginning of July 2020 to the end of 2021, in the context of a relatively low level of non-refunded tax credit amounting to BGN 99.9 million as of 31 May 2021.

⁸⁸ These developments were reported despite the changes made in July 2019 to VAT accrual on imports of particular raw materials from third countries. Based on MF Monthly Bulletin on Budget Performance and Major Indicators under the Consolidated Fiscal Programme for May 2021, the effect of applying this policy in January–May 2021 resulted in VAT not charged on imports, worth BGN 532.7 million, up 110.9 million compared with the same period of 2020.

⁸⁹ Revenue growth from social and health insurance in May 2021 was driven largely by higher revenue from social security contributions (6.8 percentage points) and, to a lesser extent, by revenue from health insurance contributions (2.8 percentage points).

Contributions of Major Tax Groups to Tax Revenue Growth, Cumulatively (on an Annual Basis)

(per cent; percentage points)



Sources: the MF, BNB calculations.

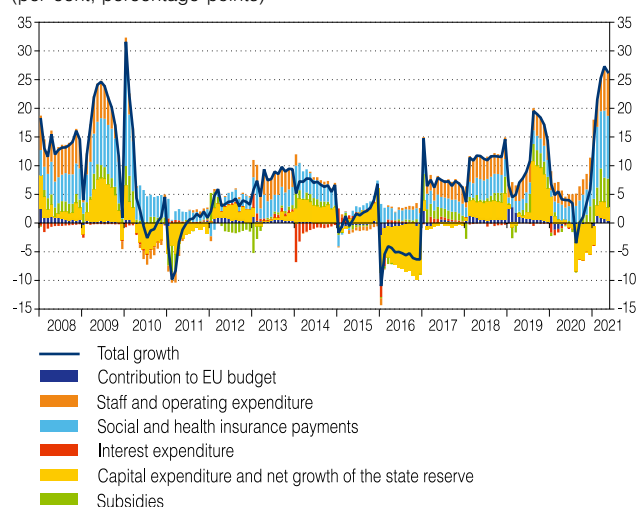
end of the first quarter. Social expenditure contributed most strongly to growth of total budget expenditure (10.9 percentage points), exhibiting an annual increase of 24.6 per cent in May.

Growth in social costs was driven by increased spending on pensions and social benefits under the Social Security Code (by 23.6 per cent on an annual basis in May), and higher expenditure on health insurance payments (by 30.4 per cent on an annual basis in May). Increased social payments reflected mainly the higher minimum and maximum amount of pensions, temporary monthly supplement payments of BGN 50 to pensions, the base effect of increased pensions from July 2020, the one-off payment of BGN 120 on food products for pensioners whose pension amount is less than BGN 369, as well as higher spending on unemployment benefits.⁹⁰ Increased transfers to households support their disposable income and private consumption, accordingly. The increase in health insurance payments was ascribable to expenses incurred to address the COVID-19 pandemic, which based on the Ministry of Finance information include expenditure on drugs, tests, consumables and protective equipment, as well as payment of additional remuneration to the medical staff. Taking into account the data on the acceleration of the annual growth rate of healthcare costs in May compared to March, it can be expected that this expenditure will contribute positively to the increase in government consumption on a quarterly basis in the second quarter of 2021.

Subsidy expenditure followed social costs in terms of a positive contribution to growth of total budget expenditure, increasing by 77.9 per cent at the end of May 2021. Its growth was mainly driven by higher subsidy costs financed by EU funds and, to a lesser extent, by costs incurred on subsidies under the so-called '60/40' measure. According to NSSI data between 1 January 2021 and 31 May 2021, BGN 332.7 million

Contributions of Major Groups of Expenditure to Total Budget Expenditure Growth, Cumulatively (on an Annual Basis)

(per cent; percentage points)



Notes: In Consolidated Fiscal Programme reports of January 2016, staff costs include wage, insurance and other remuneration expenditure, while in the reports for past periods the latter was included in operating expenditure. To avoid data inconsistencies prior to and after January 2016 resulting from the methodological change, staff and operating expenses are presented aggregately in the chart and separately in the 'Key Budget Indicators Performance for 2020 and 2021' table.

Sources: the MF, BNB calculations.

⁹⁰ As of 1 October 2020 the increase in the minimum amount of the unemployment benefit from BGN 9 to BGN 12 *per* day and the extension of its term from four to seven months became effective.

was paid to preserve jobs in Bulgaria under the '60/40' measure.⁹¹

Staff expenditure rose by 18.5 per cent on an annual basis in May, reflecting the increased wage costs in the budget sector under the State Budget Law for 2021.⁹² Operating expenditure also had a positive contribution to growth in total budget expenditure, which showed a significant acceleration in growth from the end of the first quarter, coming to 28.2 per cent at the end of May 2021.

According to preliminary data from quarterly non-financial accounts of the general government sector, in the first quarter intermediate consumption and healthcare expenditure posted a quarter-on-quarter fall in the government consumption sub-components.⁹³ Relatively high growth rates of the components of government consumption on a cash basis as of May 2021 indicate a turnaround of government consumption from a fall to growth on a quarterly basis at the end of the second quarter of the year.

Quarterly non-financial accounts of the general government sector, seasonally adjusted by the BNB, suggest that gross fixed capital formation declined quarter on quarter in the first quarter of 2021 due probably to one-off investment reported in the previous quarter. Concurrently, the increased CFP capital expenditure by 33.7 per cent on an annual basis at the end of the January–May period is indicative of gradual discontinuation of the recorded fall in government fixed capital investments and their positive impact on the economic activity in the second quarter of 2021. Annual growth of CFP capital expenditure in May was almost entirely driven by the increased capital expenditure under the national budget, which according to the Ministry of Finance information⁹⁴ includes investment payments for road infrastructure and investment projects of the Bulgarian Army.

⁹¹ Other subsidised employment programmes include the '80/20' and 'Save me' measures. According to the MF information the costs incurred under the 'Working capital support for SMEs affected by temporary anti-epidemic measures' programme, which is implemented under the 'Innovation and Competitiveness' Operational Program and is administered by the NRA, also contributed to growth of subsidy expenditure.

⁹² This included the 10 per cent rise in budget sector wages from the beginning of 2021 and increased wages of teachers.

⁹³ BNB seasonally adjusted data.

⁹⁴ According to information from the website of the Ministry of Finance on [CFP implementation as of 31 May 2021](#).

Key Budget Indicators Performance for 2020 and 2021

Consolidated Fiscal Programme	2020 January – May ¹		2021 January – May ¹	
	BGN million	per cent ²	BGN million	per cent ²
Total revenue and grants	17,637	-5.8	20,476	16.1
Tax revenue	13,997	-5.3	15,726	12.3
incl. social security and health insurance contributions	4,410	4.1	4,833	9.6
Non-tax revenue	2,282	-22.7	3,666	60.6
Grants	1,357	37.1	1,084	-20.1
Total expenditure (incl. the contribution to EU budget)	16,323	4.0	20,616	26.3
Staff	4,352	10.1	5,157	18.5
Operating expenditure	1,551	-5.9	1,989	28.2
Interest	346	-14.1	349	0.8
Social expenditure, scholarships	7,264	4.9	9,049	24.6
Subsidies	1,068	-3.1	1,900	77.9
Current and capital transfers to abroad	12	4.8	11	-2.4
Capital expenditure and government reserve growth	1,116	6.3	1,478	32.4
incl. capital expenditure	1,122	6.6	1,500	33.7
Contribution to the general budget of the European Union	615	2.7	683	11.0
	BGN million	difference ³ (BGN million)	BGN million	difference ³ (BGN million)
Budget balance, on a cash basis	1,313	-1,713	-141	-1,454
Tax revenue under the state budget	2020 January – May ⁴		2021 January – May ⁴	
	BGN million	per cent ²	BGN million	per cent ²
Tax revenue	9,168	-8.4	10,264	12.0
Corporate tax	698	-43.2	717	2.8
Personal income tax	1,753	3.4	1,992	13.6
Value added tax	4,425	-4.8	5,264	19.0
Excise duties	2,097	-4.9	2,130	1.6
Customs duties and taxes	87	-10.2	98	12.8
Insurance premia tax	23	8.9	24	4.1
Other taxes	85	-26.5	39	-54.2

Note: The difference between the sum of individual components and total sum is due to rounding.

¹ Based on monthly reports on cash-based performance of the Consolidated Fiscal Programme.

² The annual rate of change on the same period of previous year.

³ The change of the budget balance on the same period of previous year.

⁴ Based on monthly reports on cash-based implementation of the state budget.

Source: the MF.

The effect of fiscal policy on the economic activity through transfers to households and public investment is expected to be positive in the third and fourth quarters of 2021. Household disposable income is anticipated to be supported by the increase in expenditure for social payments, including pension indexation by 5 per cent as of 1 July 2021, and the increase in expenditure on public sector wages, incorporated in the 2021 state budget, as well as by the extension until July 2021 of the monthly supplement payments of BGN 50 to pensions. The assumption⁹⁵ of a phase out of some of the COVID-19 anti-crisis

⁹⁵ Based on the information available as of 25 June 2021 on the validity of the COVID-19 anti-crisis measures (the '60/40' program and pension allowances).

measures intended to support companies and households after July 2021 (such as payments under the so-called 60/40 program and the supplements to pensions) would have some limiting effect on Bulgaria's economic activity compared to the fiscal policy effect in the first half of the year. A possible reduction in healthcare expenditure based on the assumption that the COVID-19 pandemic will be gradually curbed and most of containment measures phased out, could have a further limiting effect.

The implementation of investment projects funded by the national budget and by EU funds in the context of the last phase of the 2014–2020 programme period is expected to continue contributing positively to the economic activity in the second half of 2021. Potential delays in the implementation of investment projects due to the political cycle in Bulgaria could reduce the projected positive effect of public investment on the economic activity in the third and fourth quarters of the year. The political uncertainty after the July parliamentary elections remains a factor posing potential risks to any possible changes in the amount, time frame and scope of current fiscal measures, and the announcement of new ones.

4. INFLATION

In June 2021 the annual inflation slightly accelerated compared to the end of 2020, reaching 2.4 per cent. This reflected mainly the higher prices of energy products as a result of the strong hike of international oil prices on an annual basis. Core inflation also accelerated from the end of the previous year amid easing of containment measures against COVID-19 and growth in final consumption expenditure of households. Concurrently, inflation in the food group slowed down somewhat from end-2020 due mainly to lower prices of unprocessed food. Administratively controlled prices continued to contribute positively to overall inflation driven by indirect effects of higher international natural gas prices.

In the third and fourth quarters of 2021 the gradual acceleration of inflation is expected to be sustained, reflecting mostly the assumptions of upward developments in international food and petroleum product prices over this period compared with end-2020.

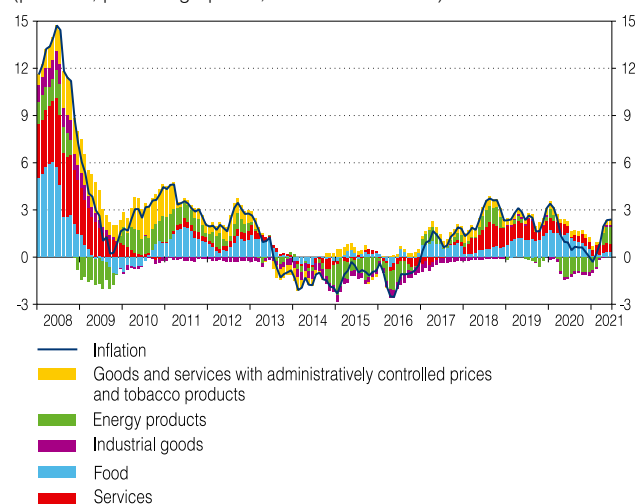
In the first half of 2021 the annual inflation followed an upward trend, reaching 2.4 per cent⁹⁶ in June against 0.0 per cent in December 2020. In June price increases were reported in each of the main groups, largely driven by the upward dynamics of international commodity prices in euro and growth in final consumption expenditure of households.

June inflation was pushed up mainly by the group of energy products, reflecting the rise in international oil prices in euro by 71.0 per cent in June 2021 compared to June 2020. Higher prices of petroleum products due to enhanced global demand were rapidly transmitted through the supply chain on producer prices and consumer prices of transport fuels. This was the reason behind the shift from annual deflation in the group of transport fuels at end-2020 (-17.3 per cent) to a price increase of 24.0 per cent in June 2021.

Food inflation in June 2021 came to 1.0 per cent compared with 2.0 per cent at the end of 2020, reflecting the positive contribution of processed food, while prices of unprocessed food posted a year-on-year decline of -2.8 per cent, from -0.8 in December 2020. Deflation in unprocessed food was mainly underpinned by the meat and meat products sub-group in the context of an annual decline in both import prices of these products and producer prices in Bulgaria. In June the group of fruit and vegetables, which

Inflation and Contribution of Major Commodity and Services Groups to It

(per cent; percentage points; on an annual basis)



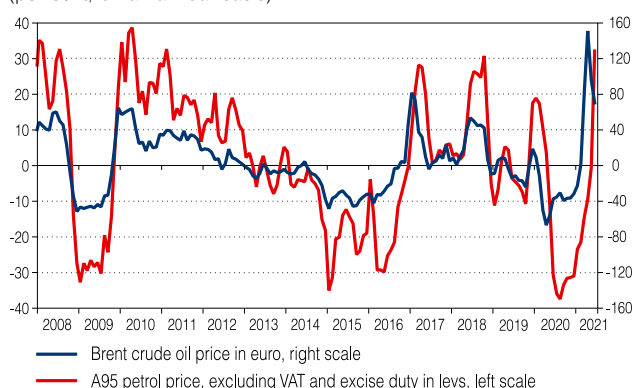
Notes: This structure corresponds to the Eurostat classification; tobacco products and goods and services with administratively controlled prices are presented separately. The price index of goods and services with administratively controlled prices is calculated through the elementary aggregates level in the consumer basket.

Sources: the NSI, BNB calculations.

⁹⁶ The analysis in this section employs NSI data on HICP.

Annual Rate of Change in Brent Crude Oil and A95 Petrol Prices

(per cent, on an annual basis)



Sources: the ECB, the NSI, BNB calculations.

are strongly affected by the weather conditions⁹⁷ during that period of the year, also had a significant negative contribution to the overall inflation.

Processed food inflation was 3.0 per cent in June (3.5 per cent by end-2020). The bread and cereals, and animal and vegetable oil and fats groups continued to contribute most to the price hike which was in line with the upward dynamics of producer prices⁹⁸. These developments were likely to reflect the upward trend in international wheat and other commodity prices in euro along with higher price indices of goods and services intended for current consumption in agriculture in Bulgaria.

In June 2021 core inflation (including services and non-food prices) accelerated to 1.4 per cent from the end of 2020 (0.5 per cent), reflecting the positive contribution of both sub-components of core prices.

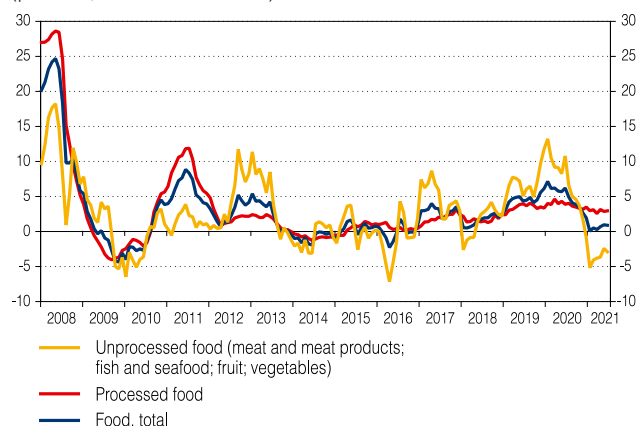
Annual inflation in services rose to 2.0 per cent in June 2021, from 1.8 per cent by end-2020 which was consistent with growth in final consumption expenditure of households following the easing of COVID-19 containment measures. Inflation in this group accelerated due to the higher prices of package holidays and insurance services. Catering, transport services (where the accelerated inflation reflected the upward

⁹⁷ The analysis employs Commodity Exchange and Wholesale Markets State Commission Monthly Bulletin data.

⁹⁸ According to producer price index (PPI) prices related to the manufacture of oils and fats rose by 43.9 per cent on an annual basis as of April 2021, while prices related to the manufacture of bakery and farinaceous products increased by 4.2 per cent.

Rate of Change of Food Price Index

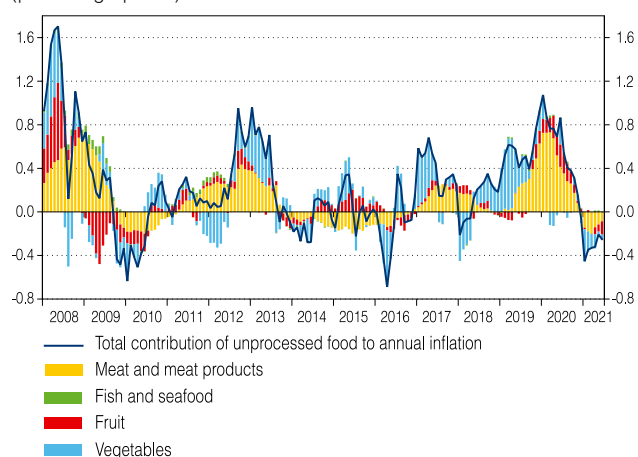
(per cent, on an annual basis)



Sources: the NSI, BNB calculations.

Contribution of Major Sub-groups of Unprocessed Food to Overall Inflation

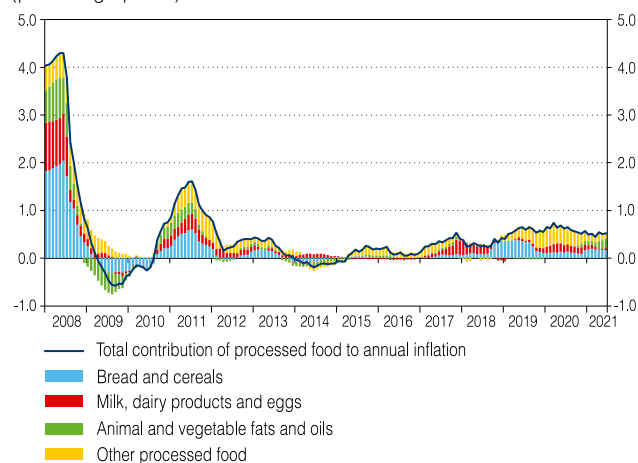
(percentage points)



Sources: the NSI, BNB calculations.

Contribution of Major Sub-groups of Processed Food to Overall Inflation

(percentage points)



Sources: the NSI, BNB calculations.

dynamics of food and fuel prices), including financial services, were the other components having a relatively high positive contribution to the inflation in the services group.

The deflation observed in non-food goods in 2020 was reversed in early 2021 and in June annual inflation in this group was 0.4 per cent (-1.1 per cent in 2020). These developments resulted from the easing of containment measures in Bulgaria and the exhausted negative effects of subdued demand in 2020⁹⁹. Dynamics of inflation in non-food goods was largely driven by the price growth in furniture and furnishings, coupled with the moderated rate of decline in prices of clothing and footwear and motor vehicle sub-groups. Developments in nominal retail trade volumes in May 2021 indicate steadily increasing demand of non-food goods, which is a precondition to preserve the trend to a gradual acceleration in annual growth of their prices in the following months.

Inflation in goods and services with administratively controlled prices and tobacco products increased to 1.7 per cent in June, from 1.2 per cent by end-2020. Electricity prices, reflecting the rise in the regulated price by 2.8 per cent in July 2020 for a year ahead, had the main positive contribution to the inflation in this group. Natural gas prices in June confirmed by the Energy and Water Regulatory Commission (EWRC) that were higher by 71.4 per cent compared to the same month of 2020¹⁰⁰, along with the price increase in heating also played a significant role in price rises in the group compared to December 2020. Other groups of goods and services with administratively controlled prices contributing more substantially to inflation were educational services, followed by medicines and pharmaceuticals.

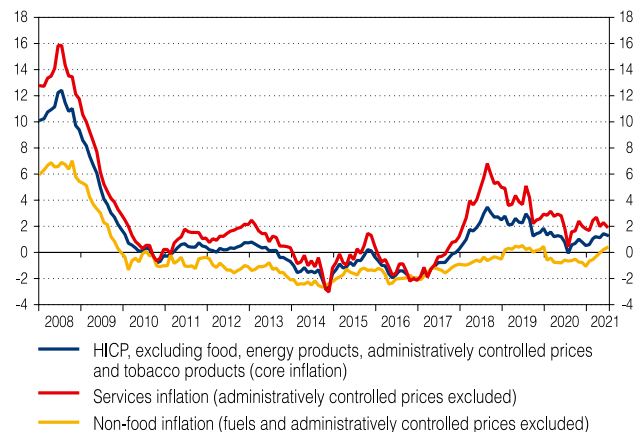
Accelerating inflation in the first six months of the year reflected the upward dynamics of producer prices. In April the total producer price

⁹⁹ According to the NSI Household Budget Survey in the first three months of 2021 real monetary consumption expenditure reported an increase of 9.6 per cent on average *per* household on an annual basis. The highest rate of change was seen in clothing and footwear (57.4 per cent), home furnishing and maintenance (41.9 per cent) and personal and cultural recreation services and education (32.4 per cent), with the expenditure only in the first group remaining slightly above its pre-pandemic level.

¹⁰⁰ The increase concerns the price at which the public supplier Bulgargas sells natural gas to final suppliers.

Core Inflation

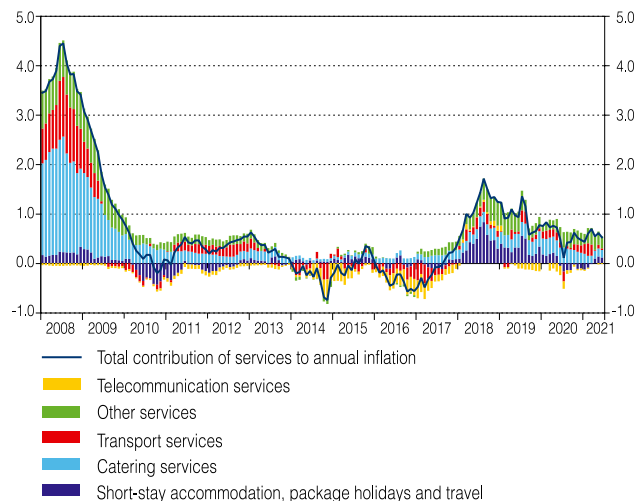
(per cent, on an annual basis)



Sources: the NSI, BNB calculations.

Contribution of Inflation in Services and Major Services Sub-groups to Overall Inflation

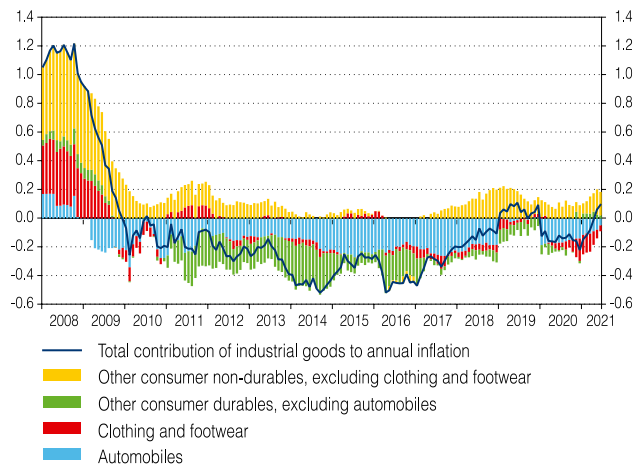
(percentage points)



Sources: the NSI, BNB calculations.

Contribution of Inflation in Non-food Goods (Excluding Energy Products) and Major Services Sub-groups to Overall Inflation

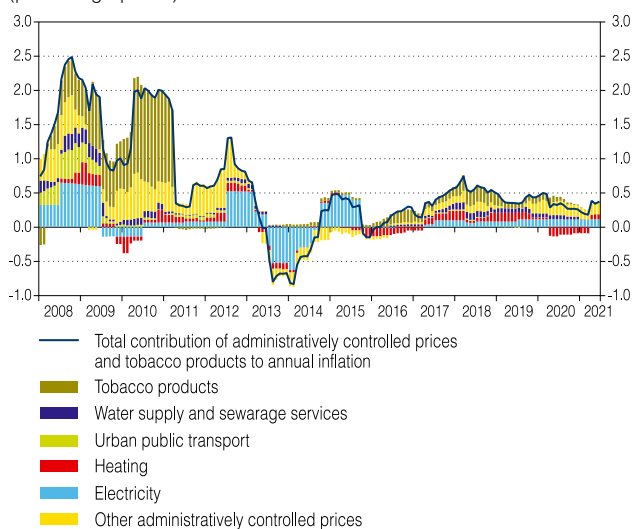
(percentage points)



Sources: the NSI, BNB calculations.

Contribution of Tobacco Products and Major Sub-groups of Goods with Administratively Controlled Prices to Overall Inflation

(percentage points)



Sources: the NSI, BNB calculations.

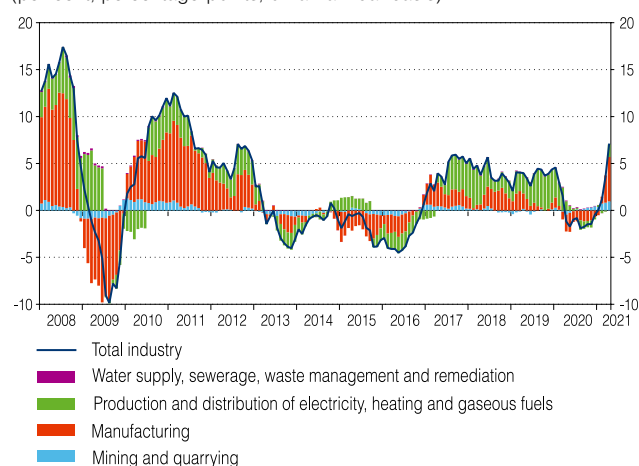
index (PPI) rose by 6.8 per cent compared with a fall of -0.5 per cent in December 2020. By economic sector, manufacturing contributed most to PPI dynamics, while the end-use classification shows a more significant price increase in intermediate consumption products and energy products. These processes coupled with higher metal prices reflected the increase in producer prices of food, refined petroleum products, production of electricity, heating and gas. The retained upward dynamics in the prices of these groups is a prerequisite for a further increasing pressure on final consumer prices in the following months.

According to the NSI business surveys, in June 2021 some of the firms that expected selling prices to remain unchanged, now foresee these prices to increase. This trend was more pronounced in manufacturing and retail trade sectors. In addition, the share of retail trade managers who expect prices to rise faster in the following three months than those observed previously is increasing. These developments imply a continued rising inflation in non-food goods over the following months.

In the first quarter of 2021 the annual growth rate in the house price index accelerated to 7.5 per cent, from 5.4 per cent at the end of the previous quarter, which was also accompanied by an increase in the volume of sale

Rate of Change in PPI on the Domestic Market and Contributions by Major Sub-sector

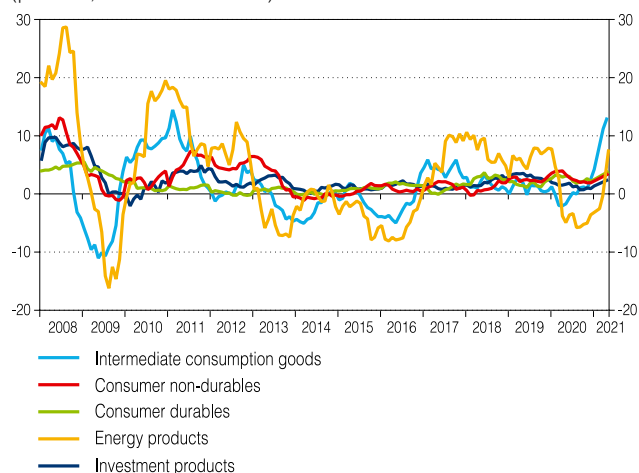
(per cent; percentage points; on an annual basis)



Source: the NSI.

Rate of Change in Producer Prices on the Domestic Market by Major Industrial Grouping

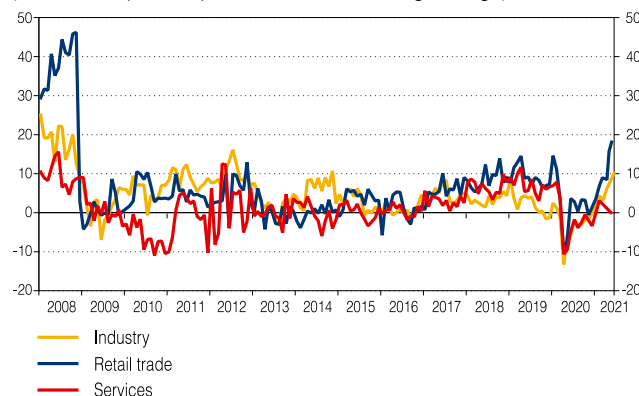
(per cent; on an annual basis)



Source: the NSI.

Expectations of Selling Prices in Industry, Retail Trade and Services in the Following Three Months

(balance of opinions, per cent, 6-month moving average)



Source: the NSI.

and purchase transactions.¹⁰¹ Higher house prices were reported in five of the sixth largest cities, with Sofia recording the most significant price increase (11.6 per cent). By HPI sub-component, prices of existing houses increased more (8.9 per cent) than new ones (6.7 per cent). Factors supporting housing demand and thereby contributing to higher house prices included the increased labour income, improved household sentiment for home purchase along with enhanced lending activity in the context of a continuously falling annual percentage rate of charge (APRC) on new housing loans. Accumulated savings in the economy and the lack of alternatives for their investment amid low interest rates were other possible factors with a pro-inflationary effect on house prices. In the first quarter of 2021 house prices in Bulgaria were 5.3 per cent lower than the maximum values in the third quarter of 2008. Estimates based on the BNB macroeconomic model¹⁰² suggest that in the first quarter of 2021 the output gap of current residential property prices in Bulgaria from their long-term equilibrium value remained slightly positive at about 2.7 per cent dependent on fundamental factors, such as income and interest rates on housing loans. Over the first quarter of 2021 the price-to-rent ratio, which represents an alternative indicator of undervaluation/overvaluation of houses, continued to deviate positively from its long-term (historical) value. In the third and fourth quarters of 2021 the house price index is expected to increase further on an annual basis. This will be attributable to the enhanced housing demand in line with the projected improvement of the economic activity in the country and the observed increased propensity of households to buy homes since the year's start as the NSI Consumer Survey shows.

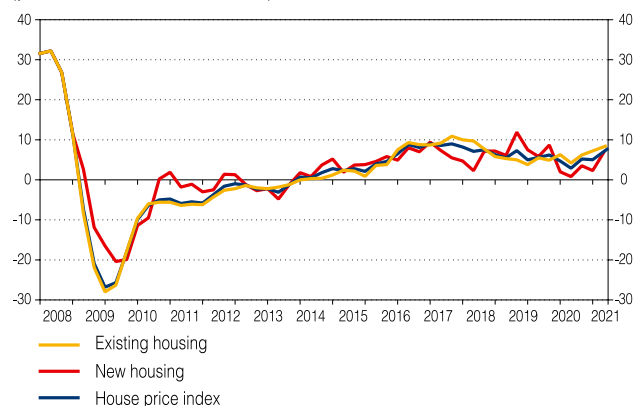
The overall inflation is projected to accelerate in the second half of 2021 and to reach about 3.5 per cent at year's end. Energy and food products are projected to continue to make a significant positive contribution mainly on the account of the expected increase in international oil and food prices in euro on an annual basis. As regards core HICP components, a simultaneous rise in services and non-food goods inflation

¹⁰¹ Eurostat data are used.

¹⁰² For more information on this model, see the research topic on Dynamics of House Prices in Bulgaria between 2000 and 2016, Economic Review, 1/2017.

Rate of Change of House Price Index

(per cent; on an annual basis)

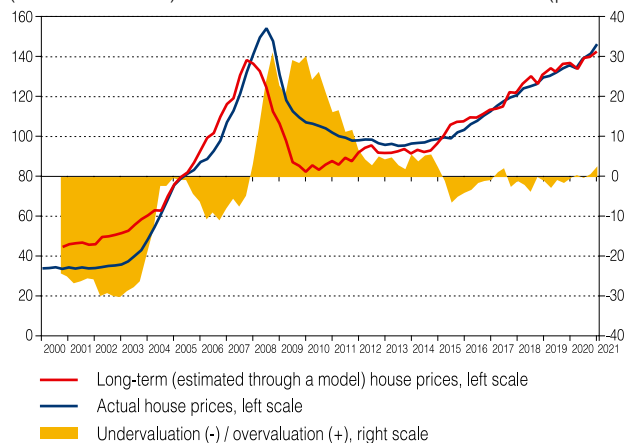


Source: the NSI.

Actual and Equilibrium House Prices

(index 2015 = 100)

(per cent)



Sources: the NSI, BNB calculations.

Rates of Change in Commodities and Services Prices and Their Contribution to Inflation

	Inflation accumulated as of June 2020 (December 2019 = 100)		Inflation accumulated as of June 2021 (December 2020 = 100)		Annual rate of inflation as of June 2021 (December 2020 = 100)	
Inflation (per cent)	-0.7		1.7		2.4	
	inflation rate by group (per cent)	contribution (percentage points)	inflation rate by group (per cent)	contribution (percentage points)	inflation rate by group (per cent)	contribution (percentage points)
Food	3.0	0.7	1.9	0.5	1.0	0.3
Processed food	2.4	0.4	1.9	0.3	3.0	0.5
Unprocessed food	4.1	0.4	2.0	0.2	-2.8	-0.2
Services	-0.1	0.0	0.1	0.0	2.0	0.5
Catering	2.6	0.1	2.0	0.1	3.1	0.2
Transport services	1.7	0.1	-3.7	-0.1	-0.7	0.0
Telecommunication services	-1.5	-0.1	-4.9	-0.2	-3.9	-0.2
Other services	-1.2	-0.2	2.4	0.2	4.7	0.5
Energy products	-17.3	-1.3	12.4	0.8	17.6	1.1
Transport fuels	-22.1	-1.3	17.3	0.8	24.0	1.1
Industrial goods	-0.5	-0.1	1.0	0.2	0.4	0.1
Goods and services with administratively controlled prices*	-0.2	0.0	0.4	0.1	2.1	0.4
Tobacco products	0.2	0.0	0.0	0.0	0.0	0.0

* The index of goods and services with administratively controlled prices is calculated through weighting the relevant elementary aggregates in the consumer basket.

Sources: the NSI, BNB calculations.

is expected mainly due to indirect effects of higher international prices and growth in final consumption expenditure of households. Projected growth of unit labour costs will be another factor of pro-inflationary effect in the services group. Electricity and heating price increases by 4.40 per cent and 16.2 per cent as of July 2021 for a period of one year is a reason to expect administratively controlled prices to continue to contribute positively to overall inflation in the third and fourth quarters of 2021.

Risks to the inflation forecast are assessed as balanced. Higher than projected inflation could be seen in energy products and administratively controlled prices in case of a stronger than expected rise in international oil prices. Concurrently, lower than expected inflation over the following months could be seen in core HICP components in case of more unfavourable than projected private consumption dynamics in the event of possible extension or tightening of anti-epidemic measures in Bulgaria.

Price-to-Rent Ratio (Percentage Deviation from Long-term Average Value)



Sources: the NSI, BNB calculations.

Key Indicators of the Housing Market in Bulgaria

(per cent; year-on-year change)

Indicators	2016	2017	2018	2019	2020	2020			2021
						II	III	IV	I
Price developments									
House price index, total	7.0	8.7	6.6	6.0	4.6	2.9	5.2	5.4	7.5
New dwellings	6.4	6.7	5.7	8.5	2.2	0.8	3.5	2.3	6.7
Existing dwellings	7.3	9.7	7.0	4.8	6.0	4.2	6.2	7.2	8.0
Inflation (HICP)	-1.3	1.2	2.6	2.5	1.2	1.1	0.6	0.3	0.2
House rentals, paid by tenants (HICP)	0.6	1.0	1.9	3.3	2.5	2.4	2.3	2.3	1.7
Lending									
New housing loans	7.4	32.7	14.9	12.4	18.1	20.0	15.5	12.3	39.2
Annual percentage rate of charge on new housing loans (per cent, at the end of the period)	5.4	4.4	3.9	3.5	3.2	3.3	3.3	3.2	3.1
Housing loans balances	-15.3	12.6	18.4	-1.4	-14.4	13.3	12.3	11.6	11.9
Construction and investment									
Permits issued for the construction of new residential buildings (square meters)	4.8	32.5	39.0	-7.9	-9.0	-23.6	-13.2	27.5	26.1
Value added in construction (at average annual prices for 2015)	-7.3	4.5	1.4	3.6	-1.0	-7.4	0.7	1.7	-12.6
Construction production index, building construction	-16.1	10.9	2.6	8.4	-8.3	-12.3	-6.9	-8.1	-3.9
Fixed investment; residential buildings	102.1	19.2	-2.2	6.6	-6.4	-13.1	-2.8	-0.6	0.7
Construction cost index for new buildings	0.8	2.5	2.9	5.1	2.1	1.8	1.0	2.4	5.2

Note: Values indicating the amount of the APRC on housing loans to households are averages weighted by the relevant volumes of new loans for a 12-month period.

Sources: the NSI, the BNB, Eurostat.

ISSN 2367-4962

ELEMENTS OF THE 20 LEV BANKNOTE, ISSUES 1999 AND 2007, ARE USED IN COVER DESIGN.