BULGARIA

Quarterly Macroeconomic Review 2Q2025

Macroeconomic and Market Research

„Decline in political instability boosts sentiments, investments and consumption"

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This quarterly macroeconomic review of Bulgarian economy was published on 10 April 2025. It employs statistical data and information available as of 07 April 2025.

Outlook

Bulgaria's GDP growth outlook remains resilient on the back of strong domestic demand and private consumption in particular. Solid GDP growth performance in the period of the forecast will draw support from full entry into the border-free Schengen area and an assumed decline in political instability, which should boost sentiments, investments and spending appetite.

The announced US "reciprocal" tariff plan was more aggressive than we had anticipated. The impact will be concentrated in electrical equipment, chemicals and pharmaceutical products manufacturing. However, the positive impulse stemming from Germany's fiscal expansion and the plan to ramp up military spending in the EU will more than offset the negative impact of higher US tariffs.

Inflation is likely to have peaked in 1Q2025, before stabilizing at around 3% in the rest of 2025 and in 2026. Inflation increases should not pose a risk to completion of the euro zone entry from 1 January 2026, which remains part of our baseline. The country fulfills all Maastricht criterion including price stability criterion and is ready to adopt the euro. BNB and commercial banks are working hard to meet all remaining technical requirements related to payment, information, accounting, and statistical systems.

MACROECONOMIC DATA AND FORECASTS

	2022	2023	2024	2025F	2026F	2027F
GDP (EUR bn)	86.1	94.7	103.7	112.2	121.0	129.8
Population (mn)	6.4	6.4	6.4	6.3	6.2	6.2
GDP per capita (EUR)	13 351	14 694	16 323	17 914	19 482	21 066
Real economy, yoy change (%)						
GDP	4.0	1.9	2.8	3.1	3.3	2.7
Private Consumption	3.9	1.4	4.2	3.3	3.1	2.9
Public Consumption	8.0	1.1	4.5	6.5	4.2	3.5
Fixed Investment	6.5	10.2	-1.1	6.4	6.2	2.6
Exports	12.1	0.0	-0.8	1.3	4.7	4.7
Imports	15.3	-5.5	1.3	3.6	5.8	5.3
Labor market						
Monthly wage, nominal (EUR)	905	1 043	1 188	1 311	1 425	1 546
Real wage, change (%)	-1.9	5.6	11.4	6.8	5.7	5.4
Unemployment rate (%)	4.1	4.3	4.2	3.9	3.5	3.4
Fiscal accounts (% of GDP)						
Budget balance (ESA 2010)	-2.9	-1.9	-3.0	-3.0	-3.0	-2.7
Primary balance	-2.5	-1.5	-2.5	-2.2	-2.0	-1.6
Public debt	22.0	22.3	23.6	27.6	28.8	29.7
External accounts (% of GDP)						
Current account balance	-2.7	-0.9	-1.8	-0.9	-1.1	-1.0
Net FDI	4.1	4.2	2.2	3.2	3.7	3.4
Gross foreign debt	50.3	47.5	47.4	49.3	49.2	48.3
Prices stability, yoy change (%)						
Inflation (CPI), avg	15.3	9.6	2.4	3.5	3.0	3.0
Inflation (CPI), eop	7.8	4.7	2.2	3.3	3.2	2.9
Housing Price Index (HPI)	13.8	9.9	16.5	11.6	8.0	7.0
Monetary sector, yoy change (%)						
Loans to households	14.6	15.9	20.8	14.9	12.7	11.9
Loans to non-financial corporations	10.4	7.3	10.1	11.6	11.4	10.4
Deposits on households	8.3	11.0	11.8	12.9	8.2	8.3
Deposits on non-financial corporations	26.6	9.0	7.0	9.7	7.8	7.4

Source: National Statistical Institute, Bulgarian National Bank, Ministry of Finance, UniCredit Bulbank

PRIVATE CONSUMPTION SHOWS LITTLE SIGNS OF EASING

We expect moderate acceleration of GDP growth in 2025

Bulgaria's real GDP growth is likely to accelerate to 3.1% yoy in 2025, from 2.8% yoy in 2024 (see chart). The two main factors that will contribute to the projected GDP growth acceleration this year, according to our baseline macro scenario, are stronger investments and a stronger public consumption.

Stabilization of political environment will have far reaching positive implications

Stabilization of the political environment, after a pro-European government was formed in January, will help the country press ahead with the growth enhancing reforms envisaged in its Recovery and Resilience Plan (RRP). We expect Bulgaria to absorb two RRP tranches in 2025 and another two in 2026. However, the total funds absorption (for the whole envelope of funds the country is entitled to receive) is unlikely to exceed 55%, since part of the reforms will remain unfulfilled, also resulting in partial disbursement of tranches.

Full entry into the border-free Schengen area will help travel, trade and tourism to increase, while, at the same time, acceleration of growth will benefit from an assumed decline in the political instability, which should boost business and consumer sentiments thereby positively affecting investments and spending appetite.

Growth remains over reliant on private consumption

Private consumption will remain the primary growth driver. However, our forecast envisages real private consumption growth to moderate to 3.3% in 2025, from 4.2% in 2024, on the back of two main reasons. First, wage growth is likely to lose some momentum, despite persistently tight labor market conditions anticipated in the period of the forecast (see chart). This is because efforts to consolidate the fiscal position will include only a 5% rise in wages of most public sector institutions, providing a smaller spill over to incomes expansion in the private sector of the economy. Second, retail lending growth is likely to weaken, since BNB introduced borrower-based measures in order to constrain the supply of mortgage loans to overstretched borrowers.

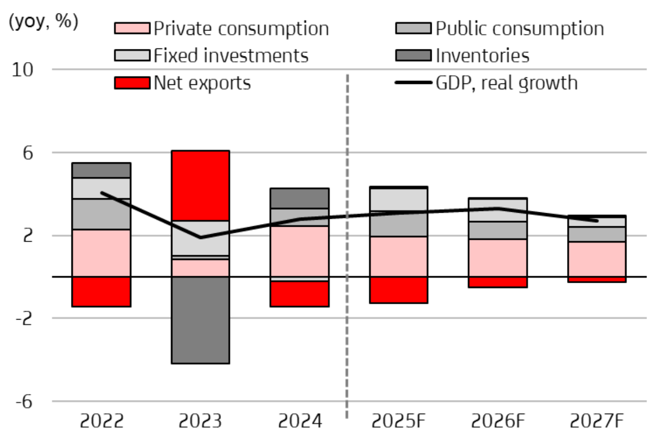
Headwinds on the external front are not over

Our baseline scenario envisages net export contribution to growth to remain negative in 2025, in proportions similar to those posted in 2024. The announced US "reciprocal" tariff plan was more aggressive than we had anticipated. Despite relatively low direct exposure to higher US tariffs, the indirect impact, via a hit to global trade and particularly to Eurozone growth, is likely to be more significant. On our estimate, the impact will be concentrated in electrical equipment, chemicals and pharmaceutical products manufacturing. However, the positive impulse stemming from the forthcoming Germany's fiscal expansion and the plan to ramp up military spending in the EU will more than offset the negative impact of higher US tariffs, in our view.

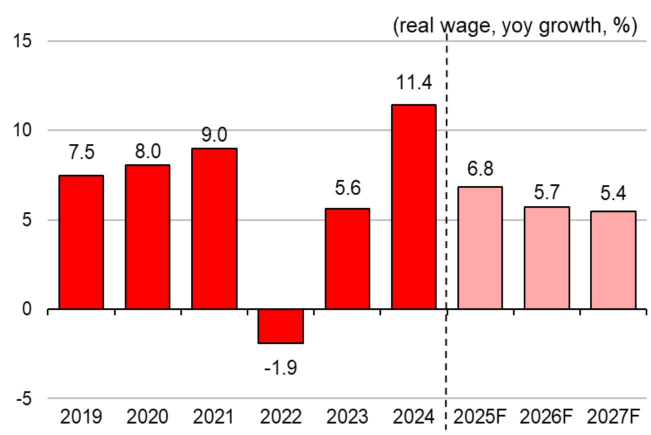
FISCAL POLICY WILL CONTINUE TO SUPPORT INCOMES GROWTH

Fiscal policy will continue to support incomes growth in 2025, though in a less pronounced way when compared to 2024. At the same time, the budget will provide additional fiscal space to increase public capex. This is positive, because infrastructure bottlenecks remain significant in many areas, including not only roads, but also networks for transfer of electricity, fuels, water and other key resources. Above all, an increase in public capex

GDP GROWTH IS PROJECTED TO REMAIN RESILIENT, DESPITE SIGNIFICANT CHALLENGES ON THE EXTERNAL FRONT



REAL WAGES GROWTH IS PROJECTED TO LOSE MOMENTUM IN THE PERIOD OF THE FORECAST



Source: National Statistical Institute, UniCredit Bulbank

is urgently needed because the lack of public infrastructure adequate to the needs of local businesses and households represents a major obstacle to boost country's international competiveness.

Some controversial tax exemptions were removed

There are no increases in the main taxes. At the same time, some cases of preferential tax treatment were removed (in the form of lower VAT rate for some goods and services), which will help fiscal revenues to increase by an amount equivalent to 0.2% of GDP, while also making tax administration easier.

Improving tax collection will be crucial

Improving tax collection is set to be an important policy priority. The latter should be welcomed, in our view, as room to improve tax collection seems significant, given the size of the grey sector, which according to different measurement methods varies between one-fourth and one-third of the total economy.

Budget execution risk seems limited

We see no major risks for the budget execution. We think Bulgaria has a reliable fiscal plan, which highlights the country's commitment to fiscal prudence needed to complete the euro adoption process and to keep public debt-to-GDP ratio on a sustainable trajectory. The center-right, pro-European GERB party, who leads the government, have a very strong track record in pursuing prudent fiscal policy and we see no reasons to believe that the latter has changed. In case plans for curtailing the grey economy fail to materialize in full, the public capex will be downsized, to ensure there are no risks for meeting the budget deficit target.

INFLATION RISES SHOULD NOT POSE RISKS TO SUCCESSFUL COMPLETION OF THE EUROZONE ENTRY

Average consumer price inflation, calculated according to the national methodology, is likely to have peaked in 1Q2025, before stabilizing at around 3% in the rest of 2025 and in 2026 (see chart).

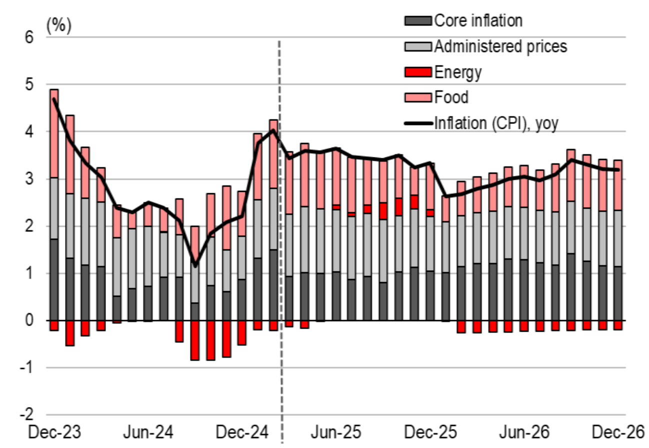
Inflation spike in January was mostly driven by one-offs

Administratively regulated prices are likely to have the largest contribution to the higher inflation in 2025. However, large part of the projected price increases have already materialized in January, when administratively regulated prices posted a sharp 3.6% mom spike, which was the highest mom rise posted since October 2014 (see chart). We think that elevated political instability over the past four years have made the regulators reluctant to allow higher cost of inputs to fully translate into higher prices for electricity, water and other utilities. Only after a stable pro-European government was formed in January, the administratively regulated prices started to catch up the lost ground that was amassed in the period of political instability.

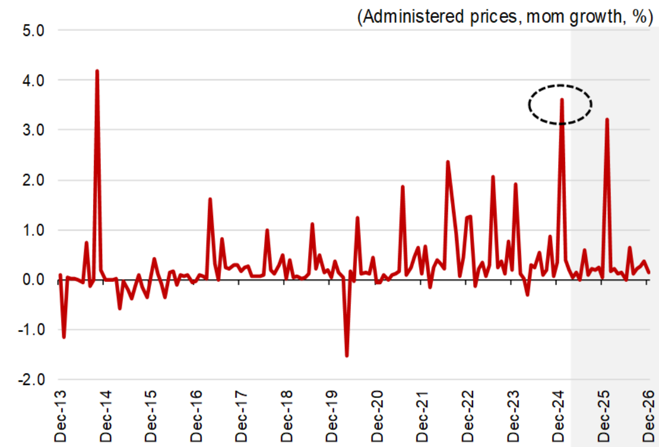
Food inflation to rise due to both domestic and external factors

The second largest contributor to higher inflation in 2025 will be food prices. Food prices already posted sharp increase in the start of the current year, when reduced VAT rates on bread and bread products as well as catering services were removed by the Parliament as part of the passing of the new budget. On top of that, in the preparation of our forecast, we have used technical assumptions envisaging an increase in the global prices of some categories of agricultural commodities such as sugar, chicken meat, eggs, beef and some sea products, which would further exercise pressure on food prices in the rest of the current year.

INFLATION IS LIKELY TO HAVE PEAKED IN 1Q2025, BEFORE STABILIZING AT AROUND 3% IN THE REST OF THIS YEAR AND NEXT



COST INCREASES HAS TRANSLATED INTO A HIGHER ADMINISTRATIVELY REGULATED UNFLATION ONLY WITH A SIGNIFICANT DELAY



Source: National Statistical Institute, UniCredit Bulbank

Services prices inflation to go down in 2H2025 and in 2026

Only on a third place, we expect inflation to accelerate in 2025 on the back of higher services prices. After reaching relatively elevated proportions in the 1H2025, we anticipate deceleration of real wages growth, which is part of our baseline macro scenario, to help services price inflation to recede in the 2H2025.

Acceleration of inflation in proportions envisaged in our forecast should not pose a risk for Bulgaria's efforts to meet inflation criterion and adopt the euro from 1 January 2026. Moreover, when assessing country's performance regarding inflation one should take into account the significant part of the inflationary pressure, which was attributable to one-offs, such as the higher taxes on foods and catering services on top of the impact that too low administratively regulated prices increases in prior years had in January 2025.

BNB and commercial banks are working very hard to complete the preparation for the euro adoption

Bulgaria is ready to adopt the euro. The country fulfills all Maastricht criterion including the price stability criterion. Preparation for euro entry is in full swing and goes in line with the schedule. The technical infrastructure necessary for the euro adoption is practically finished. As result of that, the country's payment systems are fully in line with those in the euro area. The same applies to the information, accounting, and statistical systems. Large-scale preparations are going on in every relevant aspect that the changeover process depends on. The cash centers in Sofia, Plovdiv, Varna, Burgas and Pleven are fully ready, while the BNB has already made a very good progress is testing production of the Bulgarian euro coins.

ACCELERATION OF CREDIT GROWTH HAS CONTRIBUTED TO HOUSING PRICES INFLATION

BNB is carefully monitoring the situation

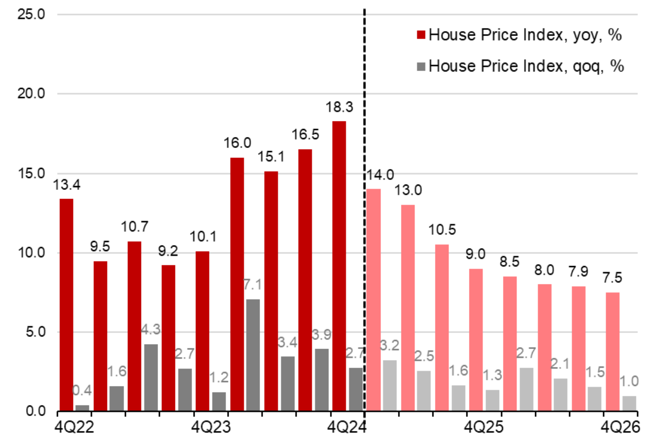
Acceleration of credit growth has contributed to both consumer price inflation and particularly to housing prices inflation (see chart). In addition, there has been some spillover effect to other assets classes. However, it is important to highlight that acceleration of retail credit growth (see chart) took place against the backdrop of a very weak external demand. Last year, acceleration of retail credit growth provided a boost to private consumption and residential construction and from here to GDP growth, thus helping to compensate for the negative impact that weak external demand had on the pace of the country's economic expansion.

Meanwhile, BNB activated all the instruments that it has at its disposal, both in terms of monetary policy and macroprudential policy, after borrower based measures were put in place for a first time in October 2024.

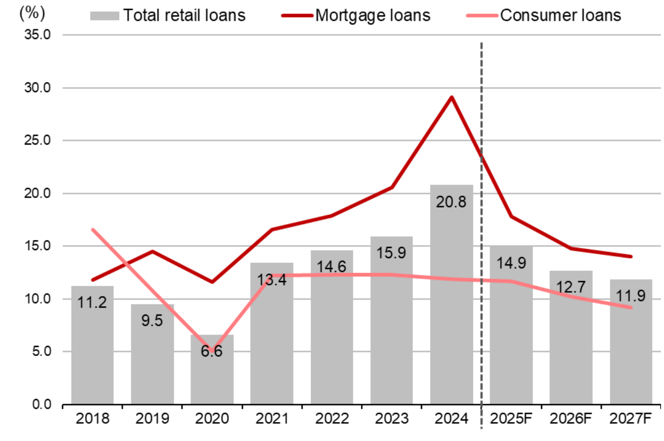
If needed, BNB sees room to further tighten borrowers-based measures

BNB wants to strike the right balance between two main goals. To control the accumulation of risks associated with rapid retail credit growth, on one side, while, on the other, make sure that the regulatory measures in place do not suppress GDP growth, because crucial part of the latter comes from the credit-financed residential construction and consumption. BNB assessment is that minimum required reserves and capital requirements are already strict enough. At the same time, the BNB is of the view that the borrowers based measures are in the neutral territory. We think, BNB will continue their comprehensive quarterly reviews of the mortgage market and, if necessary, will tighten existing borrower-based requirements even further.

HOUSING PRICES INFLATION SEEMS TO HAVE REACHED ITS PEAK IN 4Q2024, BEFORE SOME MODERATION PROJECTED IN THE NEXT TWO YEARS



MORTGAGE LENDING DREW SUPPORT FROM VERY LOW INTEREST RATES FOR BGN DENOMINATED OPERATIONS



Source: National Statistical Institute, Bulgarian National Bank, UniCredit Bulbank

GDP AND INFLATION FORECAST REVISIONS

	Forecast as of April 2025				Forecast as of January 2025				Revision (percentage change)			
	2024	2025F	2026F	2027F	2024	2025F	2026F	2027F	2024	2025F	2026F	2027F
Real yoy growth (%)												
GDP	**2.8**	**3.1**	**3.3**	**2.7**	**2.3**	**2.8**	**3.3**	**2.8**	**0.5**	**0.3**	**0.0**	**-0.1**
Private Consumption	4.2	3.3	3.1	2.9	4.8	3.5	3.2	3.1	-0.6	-0.2	-0.1	-0.2
Public Consumption	4.5	6.5	4.2	3.5	3.8	1.5	2.6	1.9	0.7	5.0	1.6	1.5
Fixed Investment	-1.1	6.4	6.2	2.6	-3.6	7.4	6.1	4.8	2.5	-1.0	0.1	-2.1
Exports	-0.8	1.3	4.7	4.7	1.0	2.9	4.5	5.6	-1.8	-1.6	0.2	-0.9
Imports	1.3	3.6	5.8	5.3	2.5	4.7	5.1	6.4	-1.2	-1.1	0.7	-1.1
Contribution to growth												
GDP	**2.8**	**3.1**	**3.3**	**2.7**	**2.3**	**2.8**	**3.3**	**2.8**	**0.5**	**0.3**	**0.0**	**-0.1**
Private Consumption	2.5	1.9	1.8	1.7	2.8	2.1	1.9	1.9	-0.3	-0.1	-0.1	-0.2
Public Consumption	0.8	1.2	0.8	0.7	0.7	0.3	0.5	0.4	0.1	1.0	0.3	0.3
Fixed Investment	-0.2	1.1	1.1	0.5	-0.6	1.2	1.1	0.9	0.4	-0.1	0.0	-0.4
Exports	-0.5	0.8	2.8	2.8	0.6	1.8	2.7	3.5	-1.1	-1.0	0.0	-0.7
Imports	-0.7	-2.0	-3.3	-3.0	-1.4	-2.7	-3.0	-3.8	0.7	0.6	-0.3	0.7
YoY, in %												
CPI inflation, total	**2.4**	**3.5**	**3.0**	**-**	**2.5**	**2.9**	**3.0**	**-**	**0.0**	**0.6**	**0.0**	**-**
Foods	2.6	3.4	2.7	-	2.7	2.9	3.3	-	-0.1	0.5	-0.6	-
Energy	-4.3	0.8	-2.4	-	-4.5	-2.3	-2.6	-	0.2	3.1	0.2	-
Administered prices	5.4	6.2	5.4	-	5.4	6.3	5.6	-	0.1	-0.1	-0.2	-
Core inflation	2.7	3.4	3.2	-	2.7	2.7	2.5	-	0.0	0.7	0.7	-
Contribution to growth, in %												
CPI inflation, total	**2.4**	**3.5**	**3.0**	**-**	**2.5**	**2.9**	**3.0**	**-**	**0.0**	**0.6**	**0.0**	**-**
Foods	0.9	1.1	0.9	-	0.9	0.9	1.1	-	0.0	0.2	-0.2	-
Energy	-0.4	0.1	-0.2	-	-0.4	-0.2	-0.2	-	0.0	0.3	0.0	-
Administered prices	1.1	1.3	1.1	-	1.1	1.3	1.2	-	0.0	0.0	0.0	-
Core inflation	0.8	1.0	1.0	-	0.8	0.9	0.9	-	0.0	0.2	0.2	-

Source: National Statistical Institute, UniCredit Bulbank

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