

## Bulgaria: Snap election fails to end political uncertainty

- The main antiestablishment party There is Such a People (ITN) won the snap elections held last Sunday
- Former ruling party, GERB (Citizens for European Development of Bulgaria), came second but are likely to go into opposition
- With 112 seats in the 240 strong parliament, the protest parties fell short of what was needed to form a governing majority
- Limited time to prepare for the use of machines in the election process led to very low voter turnout
- The likeliest scenario is a minority government with a limited mandate for reforms
- The second-likeliest scenario is another snap election held in parallel with the presidential election later this year
- We keep our central macroeconomic scenario unchanged for the time being

### Support for protest parties increased but fell short of what was needed to form a governing majority

The main antiestablishment party, ITN, led by the popular folk-rock singer and late-night TV host Slavi Trifonov, won Sunday's snap election. The ITN garnered 24.1% of the vote and will have 65 seats in the 240 strong parliament (see charts), according to the final election results published on the website of the central electoral commission. Mr. Trifonov remained faithful to his unconventional approach to the election campaign. His campaign was very quiet, resembling that of Mr. Simeon Saxe-Coburg Gotha, who achieved a resounding victory in the parliamentary election held in 2001 after making just two pre-arranged TV appearances.

GERB fell to second place with 23.5% of the vote and will have 63 MPs in the new parliament. GERB has seen its approval rating slowly eroded, as the party and its leader, long-term Prime Minister Boyko Borisov, struggled to respond to the widespread allegations of corruption and electoral malfeasance. GERB acknowledged that its chances of taking part in the next coalition government are slim and the party will most likely go into opposition.

The Bulgarian Socialist party (BSP) finished third with 13.4% of the vote, failing to win the protest vote of the young people, who flocked to support newer parties.

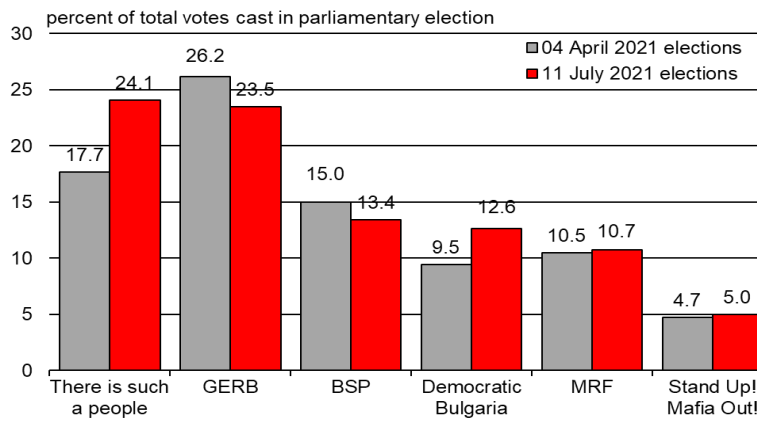
Democratic Bulgaria (DB), an alliance of three right-wing formations, which was among the most vocal critics of Mr. Borisov and GERB, garnered 12.6% of the vote and will have 34 seats in the new National Assembly (see charts).

The Movement for Rights and Freedoms (MRF), an ethnic Turkish party, received 10.7% of the vote, less than had been anticipated, after limitations on the number of voting sections set abroad was removed as part of the last-minute amendments to the electoral code that passed the National Assembly in May.

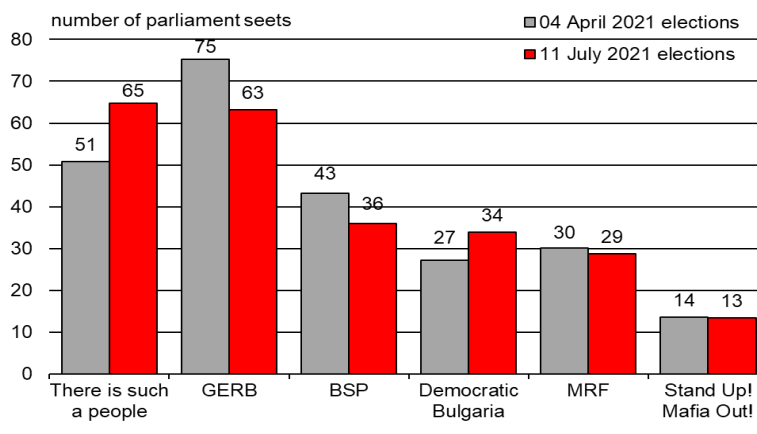
Another antiestablishment party, Stand UP! Mafia OUT! (IMV), was the last to make it into the new parliament.

When combined, the three parties that benefited mostly from the protests against Mr. Borisov and GERB will have 112 seats in the 240-strong parliament. This is an improvement compared to the 92 seats the same combination of three parties won in April's election, but still fell short of what is needed to form a stand-alone government.

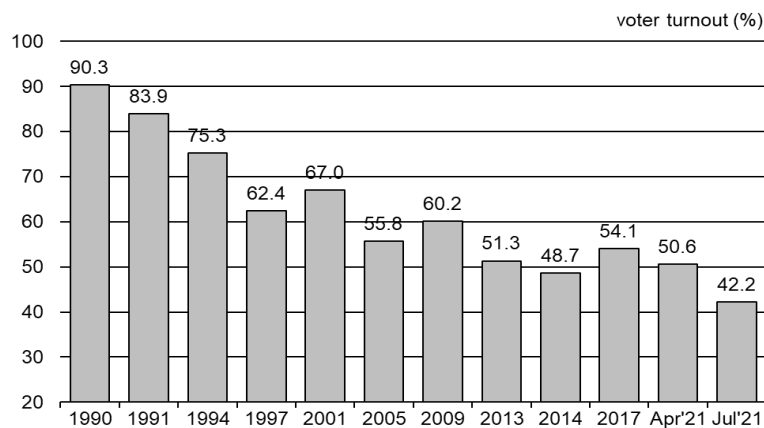
**CHART 1: SUPPORT FOR PROTEST PARTIES INCREASED**



**CHART 2: ALLOCATION OF MPS IN THE NEW PARLIAMENT**



**CHART 3: INTRODUCTION OF MACHINES IN THE VOTING PROCESS RESULTED IN VERY LOW TURNOUT**



Source: Central Election Commission (based on 100% of processed data), UniCredit Research

### **Limited time to prepare for the use of voting machines led to a very low voter turnout**

At 42.2%, Sunday's election produced Bulgaria's lowest turnout in modern history (see Chart 3), also lower than the 50.6% turnout in April. This largely reflects the limited time for preparation for the use of machines in the voting process.

In May, legislators introduced the compulsory use of machines in the election process in an attempt to reduce the opportunity for electoral malfeasance. However, this move was made only two months before the election, which significantly limited the time available to prepare the voters for the new rules. With so little preparation, it is perhaps not surprising that some elderly voters and other people with limited computer literacy were dissuaded from taking part in Sunday's vote.

### **Minority government with a limited mandate for reforms looks likely**

We see two likely scenarios from here.

Under the first, the antiestablishment parties ITN and IMV join forces with the right-wing DB and form a minority government, with some support in parliament from the BSP or the MRF. Such a scenario would require all participating parties to put aside their disagreements and ideological differences and to agree on a limited list of priorities. The main priorities would be to accelerate the vaccination process, to agree on the fiscal support measures that have to remain in force in a limited number of sectors where the recovery needs more time to materialize, as well as to finally agree on the list of projects included in the country's recovery and resilience plan.

In addition to these three priorities, the parties in the new ruling majority should try to agree on the necessary next steps to improve public trust in the legal system.

The previous parliament already passed the first reading of an amendment to a law aimed at closing down the specialized prosecution and the specialized court that deal with organized crime and high-profile corruption cases. In addition, the protest parties want the chief prosecutor to resign. The leader of ITN Mr. Trifonov even went so far as to propose sweeping changes to the constitution that would enable voters to directly elect the chief prosecutor.

Instead of insisting on these seemingly controversial proposals, the reform process could start with some proposals that already have broadly based support from political parties, representatives of the civil society, and the main professional organizations representing judges and the prosecutors in the country. One such proposal is to split the Supreme Judiciary Council into two colleges – one for judges and one for prosecutors. Another is to reduce the parliamentary quota in electing Supreme Judiciary Council members, while giving judges and prosecutors a bigger say. A third proposal is to consider undertaking specific steps to help ensure effective accountability and criminal liability of the chief prosecutor.

### **The second likeliest scenario is another snap election held in parallel with the presidential election later this year**

Under this scenario, which is probably about as likely as the first, the parliament fails to form a new government and is dissolved soon afterwards. Political power would remain in the hands of Bulgarian President Rumen Radev, whose caretaker government would continue to run the country until the end of October, when the second snap parliamentary election this year could be held in parallel with the presidential election.

### **We keep our baseline macroeconomic scenario unchanged for the time being**

We have decided to keep our baseline macroeconomic scenario unchanged as we await further details about potential economic policies to be implemented by the new government.

So far, ITN seems to prefer fiscal hawks at the helm of the government, while the IVM and especially the BSP, whose support in backing the new government in the parliament is considered very important, expressed deep disagreement with the proposed shift back to more conservative fiscal policy, which would contradict their election pledges.

We continue to think that aggregate demand will recover very rapidly this year and next. More precisely, we see GDP up by 4.4% this year and 4.1% next year, which should help the economy reach its pre-pandemic output level in 4Q21. There are two main reasons why we expect such a strong recovery in aggregate demand to materialize in 2021 and 2022.

First, growth in the period leading up to the recession caused by the COVID-19 pandemic was not driven by wider macroeconomic imbalances. Real estate prices were broadly in line with the fundamentals, while both household and corporate indebtedness were at healthy levels. This means that there will be no need for households and companies to cut back spending when the health crisis is over, which stands in sharp contrast to the period after the global financial crisis more than a decade ago when households and firms had to cut back spending to repair their overstretched balance sheets.

Second, and perhaps more importantly, the policymakers' response to the recent recession was very different. We have seen unprecedented fiscal stimulus. In Bulgaria, fiscal stimulus was slightly below 3% of GDP last year. Another 4% of GDP is likely to be deployed this year. When public-sector wages and pension increases are added to the picture, cumulative fiscal policy support deployed in 2020 and 2021 increases to around 10% of GDP. What's more, starting from 2021, the EU will provide access to its recovery and investment funds, from which Bulgaria is entitled to receive grants equivalent to more than 12% of last year's GDP.

Thus, over a period of around seven years, Bulgaria will receive total fiscal support equivalent to more than 20% of the country's GDP. Importantly, more than half of this will be investment, which will predominantly go to support the country's transition to the green economy as well as automation and digitalization, which should help boost the capacity of the economy to produce more goods and services in the long-run by addressing some of the main factors holding back the country's potential.

No matter what the exact formation of the next government is, Bulgaria will continue to have stable public finances. The next government is likely to raise pensions for a second time this year and perhaps introduce a tax-free allowance on personal income, which is positive for growth because it will leave more money in the hands of low-income households. Education and health care spending are also likely to see some increases in the years to come. All of this spending will be financed through a somewhat higher budget deficit. However, given where the country's public debt is now (at 25.2% of GDP in May), it is likely to remain at manageable levels for an extended period of time even if the country runs larger budget deficits than it has in the past.

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This report was completed and first published on 15 July 2021 at 16:05.

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