
United Bulgarian Bank
Bulgaria: Macroeconomic Update
August 2022

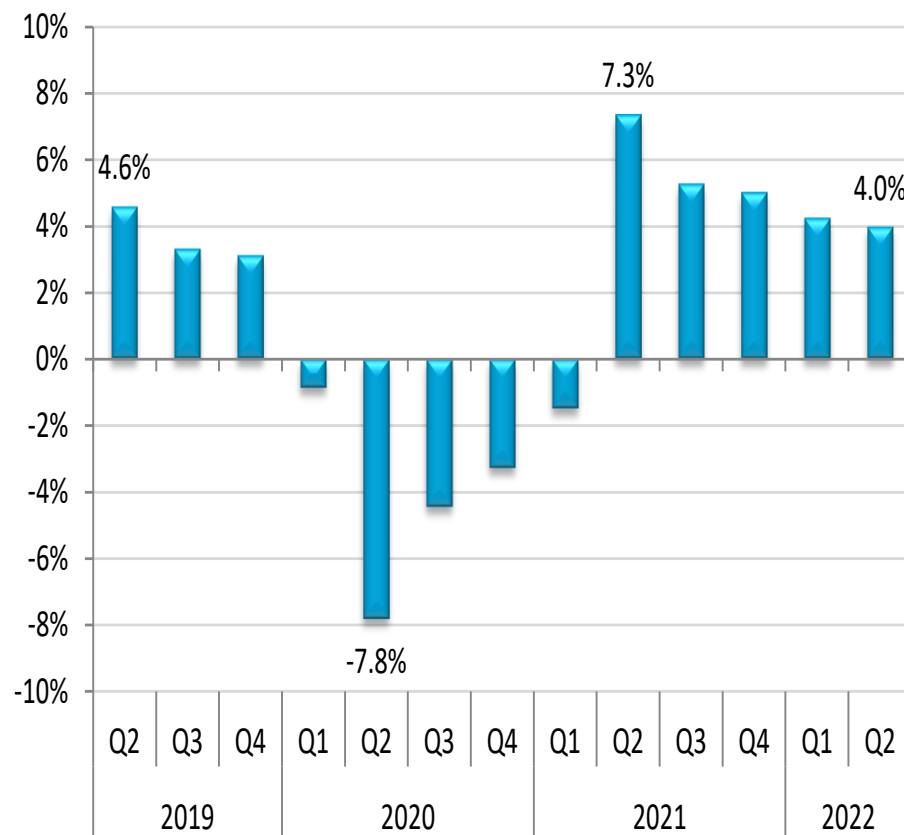
Chief Economist Department

- **Increasing geopolitical tensions, ongoing pandemic disruptions, the risk of energy shortages and a persistent, unfavourable macrofinancial context increasingly cast their shadows on the global economic outlook. Russia has scaled back drastically its gas exports to Europe by cutting supplies through the Nord Stream 1 pipeline to 20% of capacity. Against this backdrop, macroeconomic uncertainty is extremely high, and the global economic outlook deteriorates at a rapid pace.** The weakening of the global economy is becoming more and more apparent. The US economy recorded two consecutive quarters of negative growth in 2022 – i.e. a technical recession. The euro area economy showed strong(er) resilience in the first half of 2022. Reopening effects (e.g. tourism) and production backlogs supported growth, but forward looking indicators (PMIs) and economic confidence (ESIs) decreased strongly, indicating a (drastic) slowing of the economy in the quarters ahead. Moreover, energy-intensive (and dependent) European economies (e.g. Germany) already show strong signs of stagnation with (close to) zero growth.
- **Despite strong resilience so far, we expect most home markets to move towards a more stagflationary scenario.** Negative (energy) supply shocks and supply chain disruptions, as well as high (core) inflation and vanishing confidence, are expected to weigh on economic activity despite support from EU and RRF funding (for CEE markets). Most home markets are set for relatively weak growth in 2022 –Belgium (2.3%), Bulgaria (2.8%), Czechia (2.1%) and Slovakia (1.4%) – while growth in Hungary (5.7%) continues to beat expectations on the back of past fiscal stimulus. Statistical overhang effects hide the near stagnation of growth (or even a possible technical recession) in many home markets in the course of 2022.
- **Elevated and accelerating inflation remains a first-order problem in the near term.** Despite the strong commitment of central banks to rein in inflation, we expect near-term inflation in the US and the euro area to remain high. However, due to ongoing demand destruction and stabilising energy markets combined with strong base effects, we expect inflation to peak in the coming quarters before gradually converging towards the central banks' 2% inflation targets. We expect average inflation in 2022 to reach 7.8% in the euro area and 7.9% in the US before decreasing to 4.6% and 3.1%, respectively, in 2023. CEE home markets, with often double-digit inflation readings, however, face a significant risk of inflation de-anchoring, especially in light of strong(er) wage pressures..
- **The ECB ended an 8-year long period of negative interest rate policy by raising its policy rates 125 basis points.** Hence, we expect the ECB to continue its policy normalisation, gradually bringing the deposit rate to 2.25% by end-2022 and close to neutral (2.5%) by mid-2023. A severe European recession (as a consequence of critical energy deficits) may force the ECB to pause mid-way (winter 2022/2023) before resuming policy normalisation after the recession abates.

Bulgaria – GDP growth

The Bulgarian economy advanced **4.0% year-on-year** in the second quarter of 2022, compared with the second quarter of the previous year and by **0.8% compared with the first quarter of 2022**, preliminary data showed. Final consumption registered an increase of 5.2%, while gross fixed capital formation decreased by -7.3% in the second quarter of 2022, compared to the second quarter of the previous year at seasonally adjusted data. Exports of goods and services increased by 10.4% and imports of goods and services increased by 16.7%.

GDP Growth rate, compared to the same quarter previous year, seasonally adjusted data



Bulgaria – Outlook 2022 - 2024

The current forecast has two scenarios - basic and pessimistic. In the base scenario, the stagflationary tendencies are moderate. In the pessimistic scenario, after the cut of gas for EU from Gazprom in Q4 2022 the main trading partner euro area would go into recession in 2023. This would have long-term implications for both curbing domestic demand and investments and increasing negative net exports.

| Bulgaria | Base scenario | | | | | Pessimistic scenario | | | | |
|---|---------------|------|------|------|------|----------------------|------|------|------|------|
| September 12, 2022 | 2020 | 2021 | 2022 | 2023 | 2024 | 2020 | 2021 | 2022 | 2023 | 2024 |
| Real GDP growth (in %) | -4 | 4 | 2.8 | 1.6 | 3.5 | -4 | 4 | 1.1 | -1.3 | 2 |
| Inflation (in %, harmonised CPI, average) | 1.2 | 2.8 | 13.0 | 6.8 | 3.6 | 1.2 | 2.8 | 15.5 | 9.1 | 3.4 |
| Unemployment rate (% , end of year, Eurostat definition) | 6.3 | 4.6 | 5.3 | 6 | 4.8 | 6.3 | 4.6 | 6.5 | 7 | 6 |
| Government budget balance (in % of GDP) | -4 | -4.1 | -4.5 | -3 | -2 | -4 | -4.1 | -5 | -6 | -1.7 |
| Gross public debt (in % of GDP) | 24.7 | 25.1 | 27 | 29.8 | 30 | 24.7 | 25.1 | 29.8 | 34 | 35 |
| Current account balance (in % of GDP) | 0.1 | -0.2 | -2.5 | -2.8 | -1.5 | 0.1 | -0.2 | -3.5 | -3.1 | -2 |
| Long-term interest rate, 10Y Government Bond Yield | 0.40 | 0.70 | 3.40 | 3.70 | 3.60 | 0.4 | 0.70 | 2.70 | 3.00 | 3.10 |
| House prices (annual %-change, existing and new dwellings, Eurostat def.) | 5.4 | 8.7 | 9.5 | 5 | 3.5 | 5.4 | 8.7 | 3.5 | 2.0 | 0 |

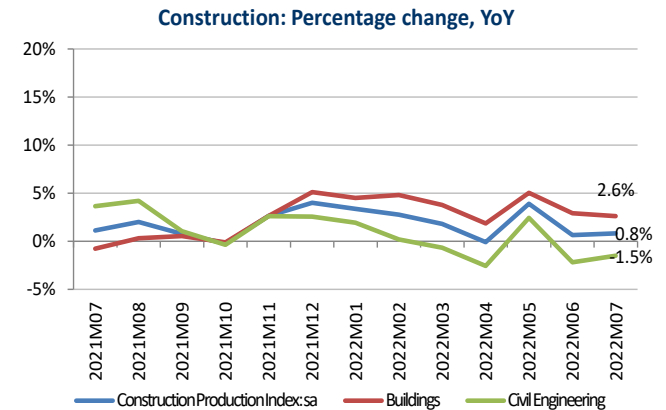
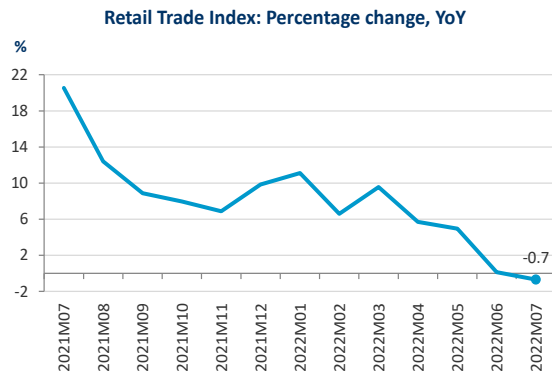
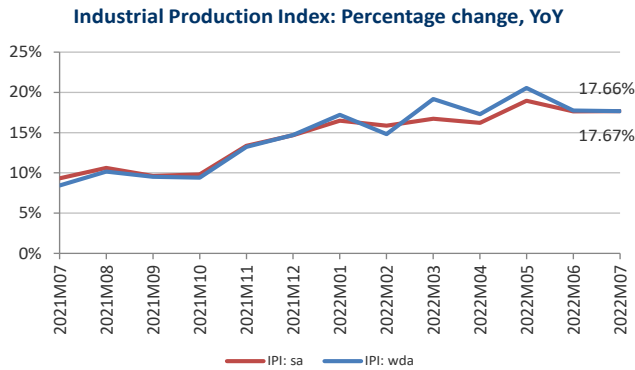
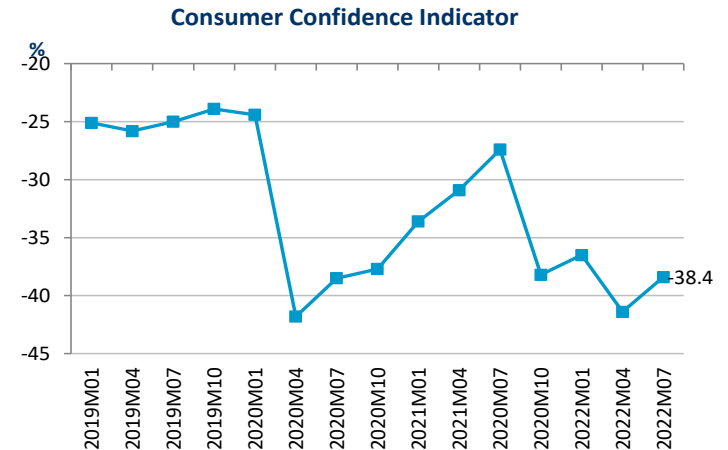
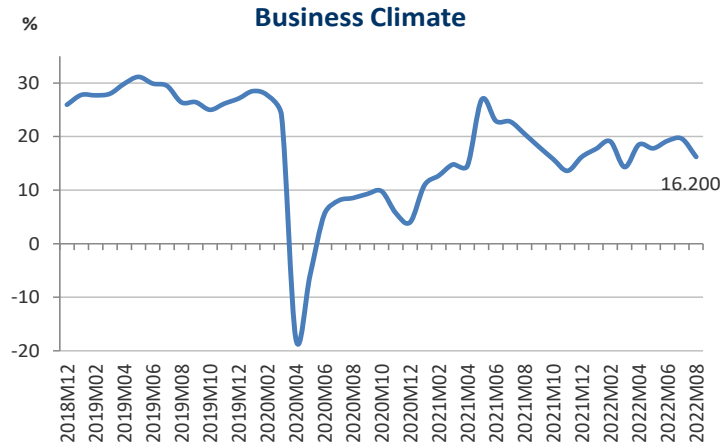
Source: KBC, UBB

| BULGARIA: Real GDP Growth (%) | 2022 | 2023 | 2024 |
|-------------------------------|------|------|------|
| KBC /UBB (September 2022) | 2.8 | 1.6 | 3.5 |
| World Bank (April 2022) | 2.6 | 4.3 | 3.7 |
| EC (July 2022) | 2.8 | 2.3 | n.a. |
| OECD (June 2022) | 2.5 | 2.3 | n.a. |
| IMF (June 2022) | 2.8 | 4.0 | 4.1 |
| MF (April 2022) | 2.6 | 2.8 | 3.6 |
| BNB (July 2022) | 1.9 | 1.7 | 3.7 |
| UniCreditBulbank (June 2022) | 2.7 | 2.0 | n.a. |

| BULGARIA: Harmonised CPI (%) | 2022 | 2023 | 2024 |
|------------------------------|------|------|------|
| KBC /UBB (September 2022) | 13.0 | 6.8 | 3.6 |
| World Bank (April 2022) | 9.3 | 3.4 | 2 |
| EC (July 2022) | 12.5 | 6.8 | n.a. |
| OECD (June 2022) | 14.1 | 8.5 | n.a. |
| IMF (June 2022) | 12.2 | 4.1 | 1.8 |
| MF (April 2022) | 10.4 | 5.1 | 2.7 |
| BNB (July 2022) | 14.7 | 3.8 | 3.1 |
| UniCreditBulbank (June 2022) | 13.7 | 7.8 | n.a. |

Bulgaria: Main Frequency Indicators

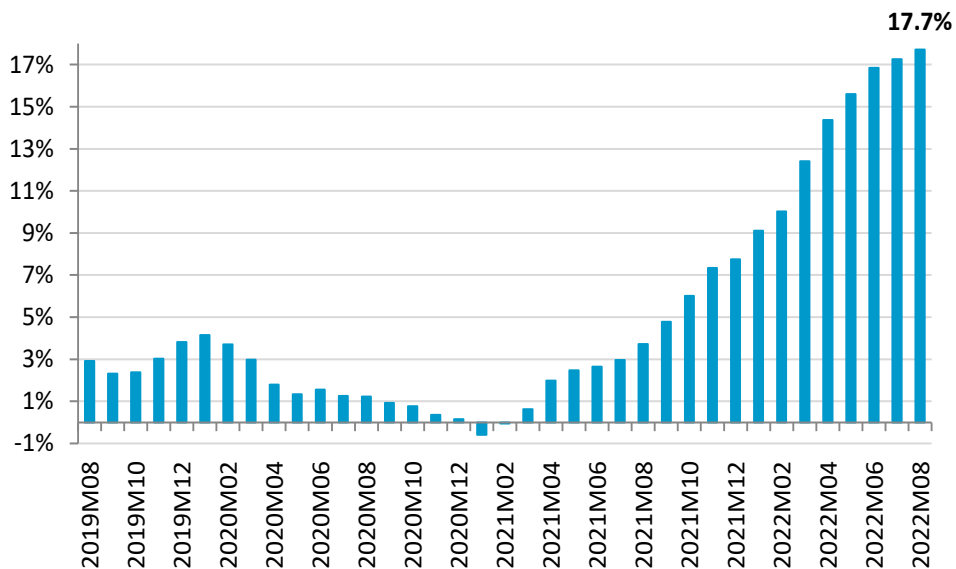
The most of high frequency indicators are decreasing in August. Industrial production decreased from 19 in May to 17.66 in August and construction decreased from 3.9 in May to 0.8 in August, mainly for civil engineering. Business climate indicator decreased at the end of August from 19.6 to 16.2. Consumer confidence increased from -41.4 to -38.4. Retail trade decreased from 5.0 in May to -0.7 in August.



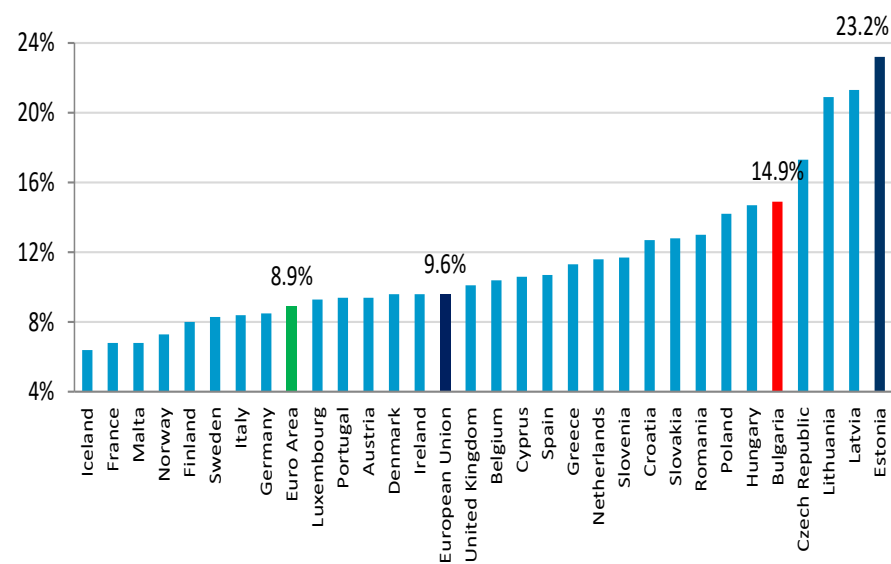
Bulgaria – Inflation (1)

Inflation in August increased to 15.0% yoy HICP and 17.7% CPI. This is the highest value in 24 years. **Our current forecast is average annual inflation of 13.0% HICP for 2022 and 6.8% for 2023.** We suppose that we will see double-digit inflation rates throughout the year. Our forecast for the inflation at end of 2022 year-on-year is 15.3% CPI and 14.4% HICP.

Inflation, y/y: 2019 - 2022

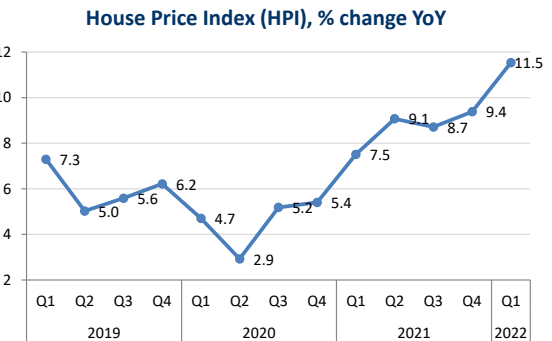
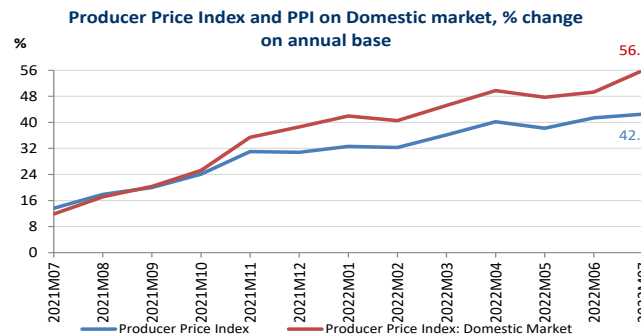
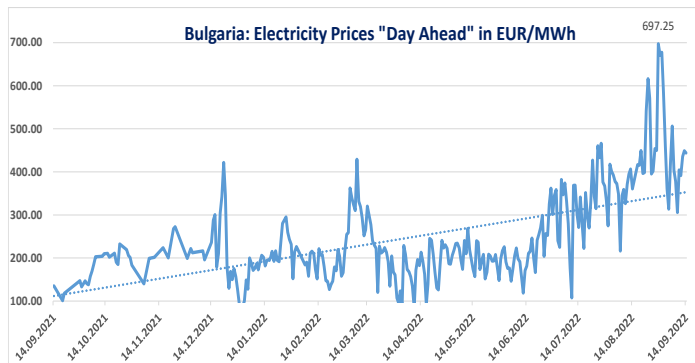
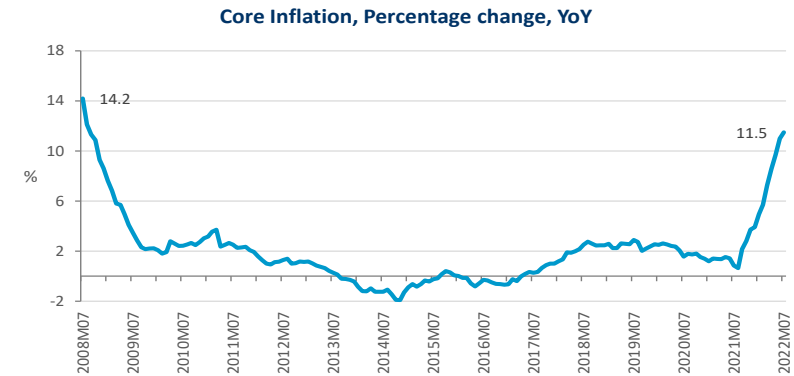
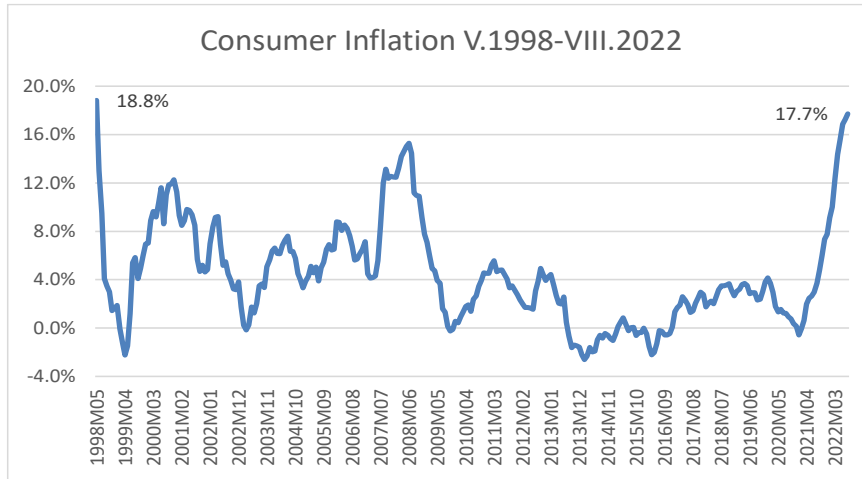


EU: HCPI Inflation (% y/y) by country July 2022



Bulgaria: Inflation (2).

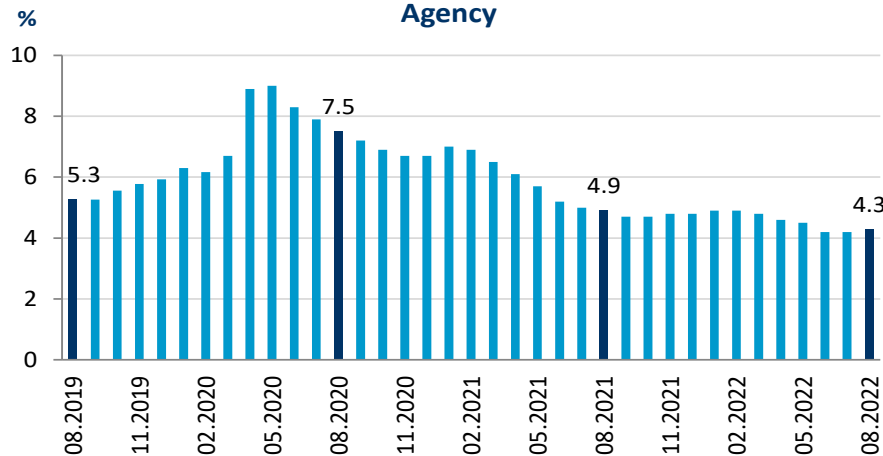
Both Bulgarian CPI and harmonized inflation has the highest record since May 1998. The core inflation is lower than the overall inflation (11.5% vs 14.9% in 07.2022). This reflects the impact of high commodity prices and especially energy prices. The big increase in the Producers Price Index 42.5% yoy is also evidence for this process. Low interest rates on bank deposits has led to increase in demand for housing and house prices.



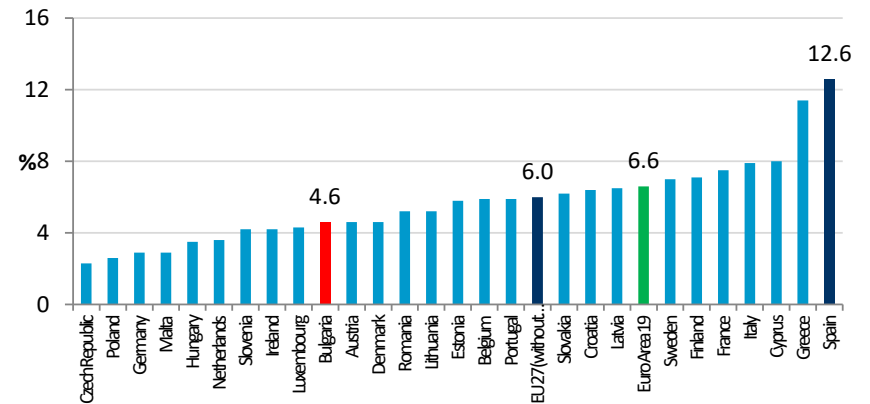
Bulgaria: Labor market

The labor market situation is assessed as tight as a result of the economic recovery and employment retention measures. According to Agency of employment in August 2022 the rate of registered unemployment is 4.3%, hitting another all time record low. In July 2022 the harmonized unemployment rate in Bulgaria is 4.6% and is well below the average of EU. **We expect moderate increase of unemployment of 5.3% for this year and 6.0% for the next year.**

Unemployment Rate Bulgaria: National Employment Agency



EU: Unemployment rate seasonally adjusted by country, July 2022



Note:

According to the definition of the NSI, unemployed are persons aged 15 - 74 years who: 1) do not have a job during the observed period; 2) actively looking for work for a period of four weeks, incl. observed week, or have already found a job that they expect to start within three months after the end of the observation period, 3) have the opportunity to start work within two weeks after the end of the observed period.

The NSI assessment is based on a sample "Labor Force Survey", in which Bulgarian households are interviewed on a rotating basis. The labor force survey is performed on a two-stage nesting sample, including about 19.6 thousand households each quarter (about 0.65% of the households in the country). The definition of unemployment of the NSI is according to Regulation of the European Commission (EC) № 1897/2000.

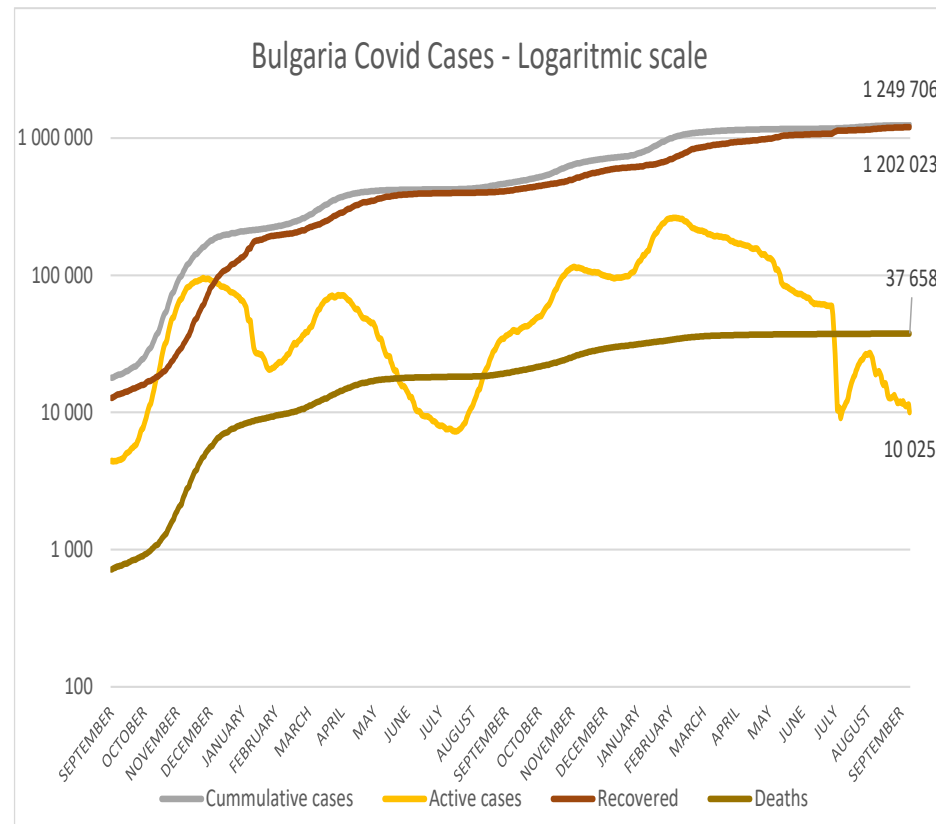
The Employment Agency considers unemployed only persons who have registered with the labor offices.

COVID-19 Status

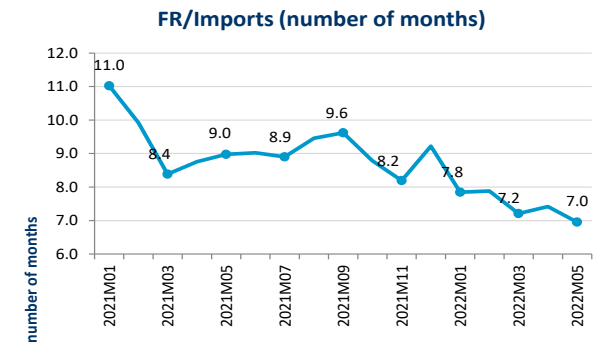
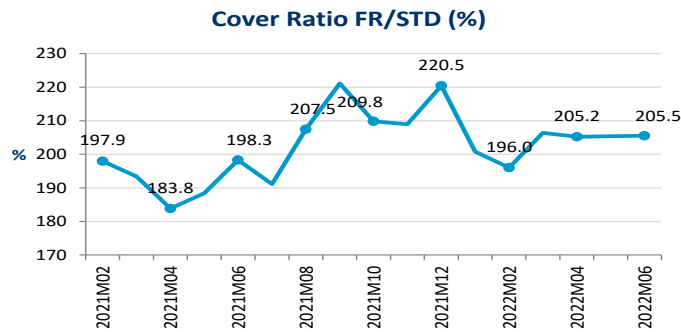
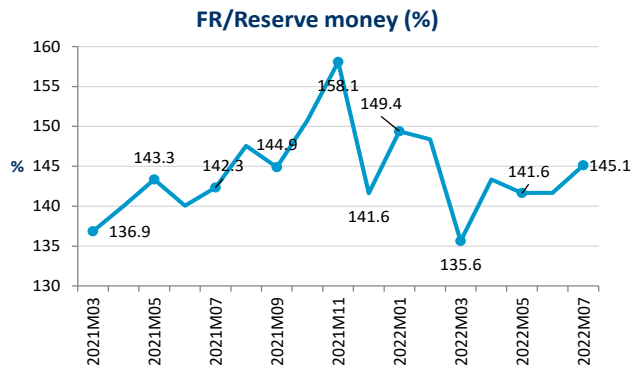
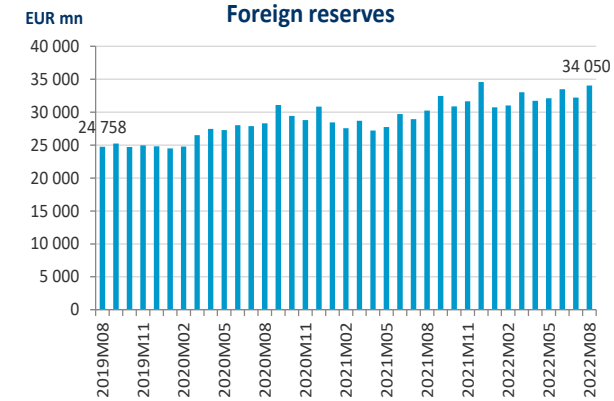
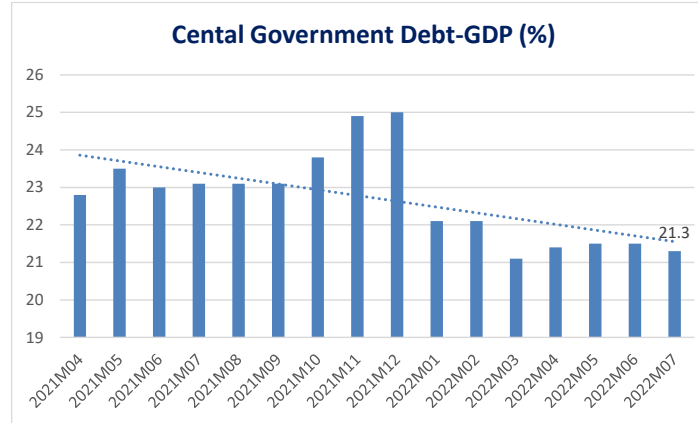
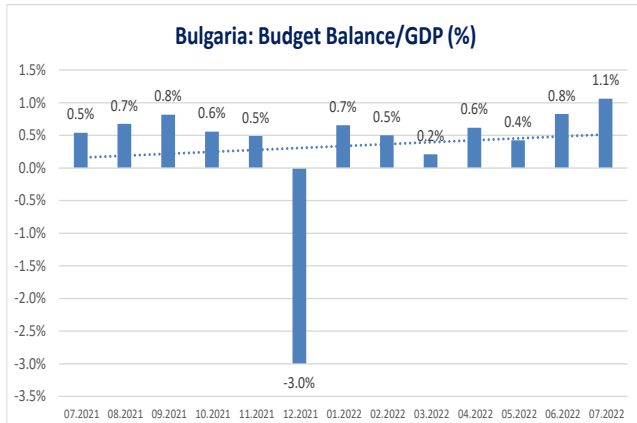
In mid-August, the new wave of Covid 19 Omicron subvariant began to fall . The active cases decreased from 25 157 on August 02, 2022 to 10 025 active cases on September 14, 2022. Mortality is still very small 37 658 on September 14, 2022.

The vaccination process has practically stopped. The fully vaccinated as of September 14, 2022 are 30% of population and 13% are with buster. The percentage of fully vaccinated was the same five months ago.

We don't expect a new emergency epidemiological situation to be imposed in the summer, but it is possible in the autumn. At this stage we don't expect the pandemic to be a significant obstacle to economic growth.



Bulgaria: Currency board indicators are stable.



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