

Bulgaria Business Forecast Report Q3 2014

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Abstracts

Core Views

Political risk in Bulgaria is on the rise, amid legislative deadlock. High unemployment and political disillusionment will leave social tensions elevated, while traditionally peripheral political parties could grow in influence. Bulgaria's economic recovery will be weak in 2014 as domestic demand remains elusive. Deflation and political uncertainty compound already weak confidence levels among businesses and mean that a sharp bounce-back for the economy is unlikely.

Bulgaria's economic rebalancing will continue to play out over the coming years, keeping the current account in surplus until 2018. Although the surplus is set to shrink, weak domestic demand conditions will preclude a more rapid return to a deficit. **Major Forecast Changes** We have made no **Major Forecast Changes** this quarter.

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Political risk in Bulgaria is on the rise, amid legislative deadlock. High unemployment and political disillusionment will leave social tensions elevated, while traditionally peripheral political parties could grow in influence.

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Challenges Remain Despite EU Membership

We expect EU membership to remain key to Bulgaria's long-term political outlook, helping underpin investor sentiment in the country and steady economic growth. However, we note that despite having already joined the bloc, Bulgaria has a number of challenges it must yet tackle to improve its business environment and help ensure a more stable economic and political situation over the next ten years.

Below we outline these challenges and possible scenarios for political change.

CHAPTER 2: ECONOMIC OUTLOOK

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Weak Domestic Demand Conditions To Persist

Bulgaria's economic recovery will be weak in 2014 as domestic demand remains elusive. Deflation and political uncertainty compound already weak confidence levels among businesses and mean that a sharp bounce back for the economy is unlikely despite exports of goods and services offering a silver lining for the economy in light of the eurozone recovery.

Table: GDP**Fiscal Policy****Expansionary Fiscal Policy On A Sustainable Path**

Economic and political dynamics in Bulgaria strongly suggest that the recent departure from fiscal austerity will remain in place, leading to a gradual widening of the nominal fiscal deficit over the coming years. Nevertheless, we do not envision major fiscal slippage or a deteriorating credit profile for the sovereign, as Bulgaria will continue to have among the lowest fiscal deficits and public debt stocks in the region.

Table: Fiscal Policy**Balance Of Payments****No Rapid Return To Current Account Deficit**

Bulgaria's economic rebalancing will continue to play out over the coming years, keeping the current account in surplus until 2018.

Although the surplus is set to shrink, weak domestic demand conditions will preclude a more rapid return to a deficit. We note, however, that rising geopolitical tensions could affect Bulgaria's trade outlook over the coming years, given the country's high dependence on fuel imports from Russia.

Table: Current Account**Monetary Policy****Deflationary Spiral Risks Loom Large**

Prolonged deflation threatens to jeopardise Bulgaria's nascent economic recovery, potentially delaying improvement in domestic demand. With limited policy options available to the central bank, we note considerable downside risks to our 1.4% real GDP growth forecast this year.

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