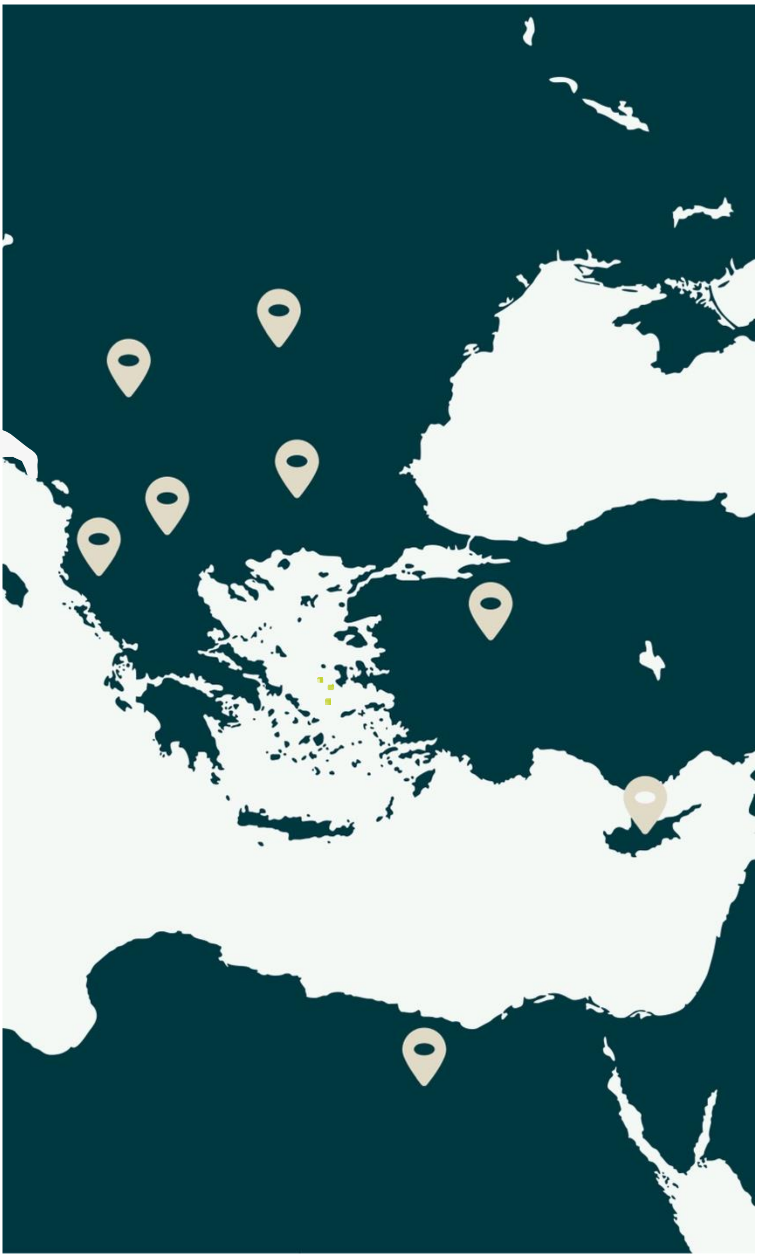
Bi-WEEKLY REPORT

Emerging Markets Analysis

20 February – 4 March 2024



COUNTRIES IN FOCUS:

Bulgaria & North Macedonia

Strong (EU-funded) investment activity and resilient private consumption should underpin economic growth in the period ahead

Political stability is key to economic growth

Euro adoption to be delayed at least until 2025

Monetary policy should remain cautious, given inflation risks

Fiscal balances are set to embark on gradual consolidation path, helping to safeguard public finances

APPENDIX:

NATIONAL BANK OF GREECE

NBG – Economic Analysis Division
https://www.nbg.gr/en/group/studies-and-economic-analysis

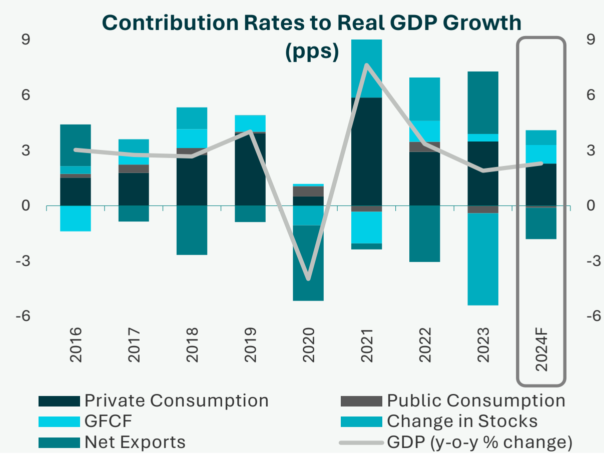
Emerging Markets Analysis

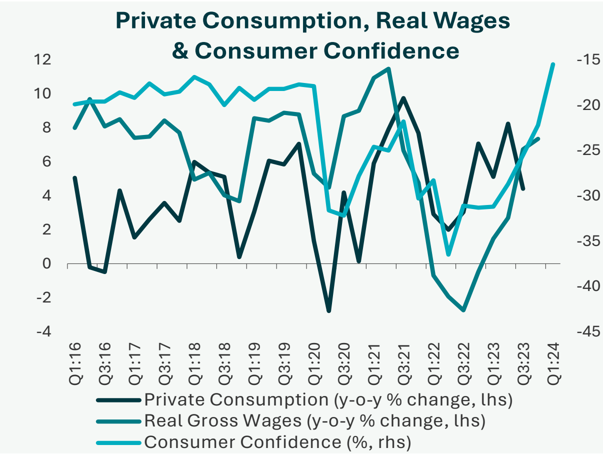
Head:
Konstantinos Romanos-Louizos
+30 210 33 41 225
romanos.louizos.k@nbg.gr

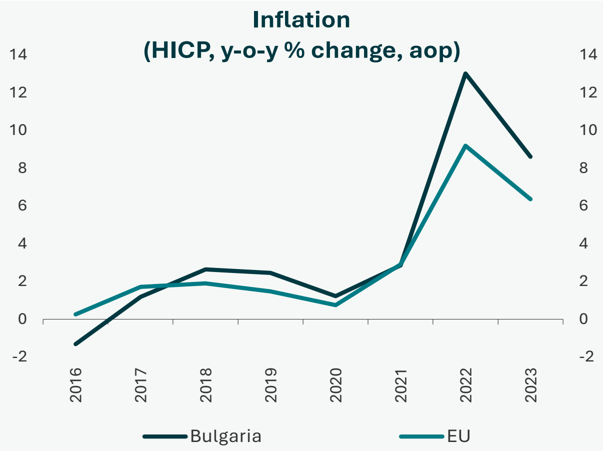
Georgios Ntinenis
+30 210 33 41 434
ntinenis.georgios@nbg.gr

Bulgaria

BBB / Baa2 / BBB (S&P / Moody's / Fitch)







	4 Mar	3-M F	6-M F	12-M F
Base Interest Rate (%)	3.8	3.7	3.4	3.0
BGN/EUR	1.96	1.96	1.96	1.96
Sov. Spread (2027, bps)	63	70	68	65

	4 Mar	1-W %	YTD %	2-Y %
SOFIX	793	1.0	3.7	38.1

	2021	2022	2023E	2024F	2025F
Real GDP Growth (%)	7.7	3.9	1.8	2.2	3.3
Inflation (eop, %)	7.8	16.9	4.7	3.5	3.0
Cur. Acct. Bal. (% GDP)	-1.7	-1.4	0.3	0.6	0.6
Fiscal Bal. (% GDP)	-2.8	-0.8	-3.1	-3.2	-2.6

Sources: Reuters, NSI, Eurostat & NBG estimates

Strong (EU-funded) investment activity and resilient private consumption should underpin economic growth in the period ahead. The deployment of the Recovery & Resilience Plan and other EU funding (with total available EU loans & grants under the 2014-20 and 2021-27 Multiannual Financial Frameworks and the Next Generation EU programme amounting to more than 30% of the Bulgaria's FY:23 GDP), should boost gradually investment activity, despite restrictive financing conditions. Note that the investment-to-GDP ratio has dropped markedly (to c. 18.0%, well below the EU average of 22.0%), highlighting not only the role of political stability (with significant delays on key reforms having led so far to poor absorption of EU funds), but also the need to enhance further the business environment.

Private consumption growth, the economy's traditional expansion driver, should remain resilient in FY:24, albeit moderating from the high rates observed in FY:23, reflecting fading support from: i) tight labour market conditions (with unemployment currently hovering slightly above record-low levels and real ex-post wages posting high single-digit growth); ii) subsiding inflation (projected at 3.4% on average in FY:23, down from 9.6% in FY:22, but still above the past decade's average of c. 1.5%); and iii) improving consumer confidence.

At the same time, net exports are unlikely to add to GDP growth, in view of sluggish economic expansion in the EU, on the one hand, and relatively strong domestic absorption and envisaged normalization in the level of inventories, on the other hand.

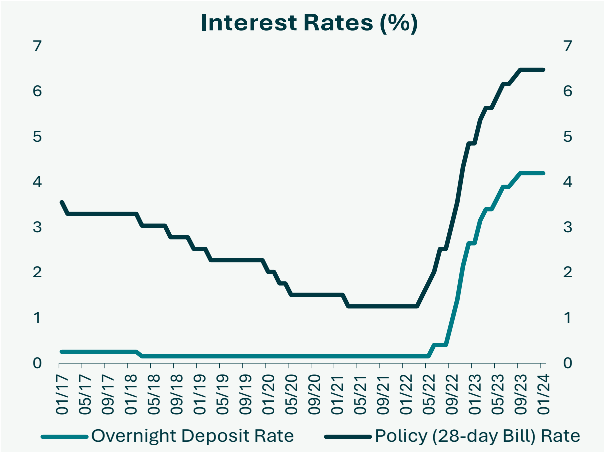
All said, we see GDP growth firming to 2.2% in FY:24 from 1.8% in FY:23, overperforming compared with the EU average (up c. 0.9%), but still below its long-term potential of c. 3.5%.

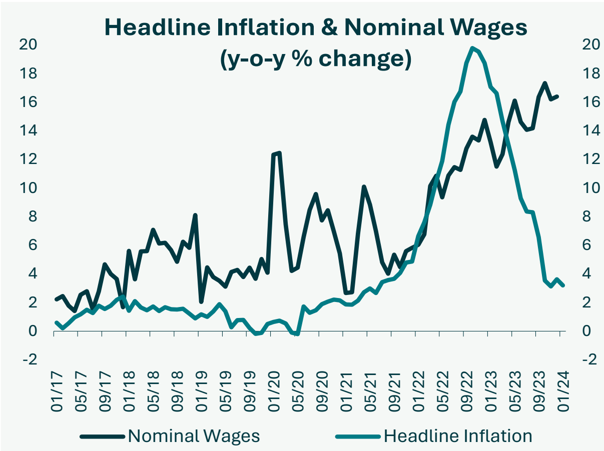
Political stability is key to economic growth. Recall that in June 2023, nearly 2 months after the April election, the 5th held over the past 2 years, the Parliament voted in a rotational coalition Government, backed by the country's largest political forces and former political feuds, the GERB and the "We Continue the Change" (WCC, in collaboration with "Democratic Bulgaria") parties. However, ongoing tensions over the allocation of ministerial portfolios among partners in the Cabinet to be led by M. Gabriel of the GERB, which is due to succeed that of N. Denkov of the WCC, has exposed cracks in the unity of the coalition. Although we cannot rule out the scenario of early elections, we still expect the cabinet switch to eventually completed. In the event, however, we recognise that the coalition would have a hard time staying together, something that could affect policy implementation. Importantly, however, the anchor offered by EU membership and the prospect of euro adoption, limit the risk of a serious policy slippage.

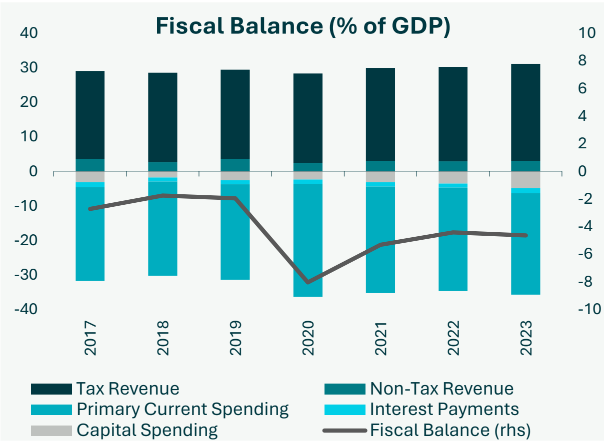
Euro adoption to be delayed at least until 2025. Delays in the adoption of necessary legislation, mainly due to political instability, and elevated inflation has prompted authorities to defer the target date for euro adoption by 1 year to 2025. Although inflation has eased, it remains significantly above the EU average, with Bulgaria unlikely to meet the relevant criterion (i.e. an upward deviation of no more than 1.5 pps from that of the 3 best performing EU states) by the deadline of mid-2024 so as to ensure accession in 2025. More worryingly, there are serious concerns over the prospect of sustainable inflation convergence. Indeed, any improvement in productivity under a fixed exchange rate regime (recall that Bulgaria has been successfully running a currency board since 1997) should be translated into higher inflation (Balassa-Samuelson effect). Weak demographics also pose a challenge. Note that prices in Bulgaria currently stand at c. 60% of the EU average, confirming the significant upside potential for inflation. However, we recognise that competent authorities could show some compromise on ultimate accession, as it was the case with Croatia.

North Macedonia

BB- / NR / BB+ (S&P / Moody's / Fitch)







	4 Mar	3-M F	6-M F	12-M F
1-m SKIBOR (%)	4.4	4.2	4.1	3.7
MKD/EUR	61.6	61.6	61.6	61.6
Sov. Spread (2028, bps)	304	310	300	280

	4 Mar	1-W %	YTD %	2-Y %
MBI 100	6,781	-0.4	10.9	16.2

	2021	2022	2023E	2024F	2025F
Real GDP Growth (%)	4.5	2.2	1.0	2.1	3.3
Inflation (eop, %)	4.9	18.7	3.6	3.2	2.4
Cur. Acct. Bal. (% GDP)	-2.8	-6.1	0.7	-0.7	-1.3
Fiscal Bal. (% GDP)	-5.3	-4.4	-4.9	-3.9	-3.3

Sources: Reuters, NBRNM, MAKSTAT, Ministry of Finance & NBG estimates

Monetary policy should remain cautious, given inflation risks. The massive hike in interest rates (with the NBRNM's key 28-day bill rate having gone up 505 bps since April 2022, to 6.3%, and the overnight deposit rate, which appears more relevant in the context of the system's large liquidity surplus, having increased by somewhat less -- up 405 bps, to 4.2%), combined with favourable global energy price developments and state's intervention to freeze the price of over 50 basic food products, have helped in bringing inflation down. The latter currently stands at slightly over 3.0% y-o-y, significantly down from its peak of c. 20.0% at end-2022, but still above its pre-pandemic average of c. 1.0%.

Nevertheless, strong nominal wage growth (up 14.7% on average in FY:23, reflecting structural issues in the labour market as well as a loose incomes policy and its spillover to the private sector) and high uncertainty (over the expiry of state measures in March and potential repercussions from ongoing geopolitical tensions) suggest that risks to the inflation outlook are clearly tilted to the upside, prompting the NBRNM to remain cautious in the short-term, despite the relative slow pace of economic growth (projected at 2.1% in FY:24, below its long-term potential of 3¼% and the growth rate of its regional peers, up c. 3.0%) and broadly anchored inflation expectations.

Assuming authorities stick to the provisions of the latest General Collective Agreement (CGA, see below), allowing wage growth to subside gradually to levels more consistent with observed (modest) productivity gains, we see the NBRNM remaining on hold at least until mid-year, when inflation is expected to have been entrenched at current levels. Note that although the shallow domestic financial market provides the central bank with some monetary flexibility, it is crucial to avoid maintaining significant price differentials between the country and the euro area, given the need to safeguard the MKD's longstanding peg with the EUR. Importantly, at current levels (EUR 4.5bn), FX reserves cover more than 5 times the monetary base (M0) and 4½ months of GNFS imports, suggesting capacity to absorb any (temporarily) increased FX needs, without jeopardizing financial stability.

Fiscal balances are set to embark on gradual consolidation path, helping to safeguard public finances. The FY:23 budget deficit widened to 4.9% of GDP from 4.4% in FY:22, on higher capital spending. The latter was largely channeled to the Corridor 8/10d highway project, whose construction was initiated in mid-2023. Adjusted for capital spending and (higher) interest payments, the primary current surplus widened further to 1.8% of GDP in FY:23 from 0.3% in FY:22, in line with lower discretionary spending (especially on goods & services and energy subsidies), which more than offset the cost of the hike in public sector wages. The adoption of measures streamlining preferential treatments in PIT, CIT and VAT, as well as the levy of a one-off solidarity tax (all effective as of September '23) also provided a small, yet critical, contribution to tax revenue, compensating for the impact of weak demand and easing inflation.

For FY:24, we expect the budget deficit to narrow to 3.9% of GDP, falling behind the target of 3.4%, with the phasing-out of energy subsidies accounting for the bulk of consolidation. The full impact of the recently adopted tax reforms should also help. Note that the public wage bill is due to rise further this year, albeit modestly, as agreed under the latest GCA (with the latter, however, providing for a streamline in the wage-setting process as of 2025, by capping public wage increases by nominal GDP growth). Risks to our forecast are tilted to the downside, reflecting relaxed fiscal discipline ahead of the double election in spring and/or cost overruns related to the Corridor 8/10d project.

In fact, the budget deficit is projected to fall below the 3.0% of GDP threshold provided under the Budget Law only in FY:26. Importantly, gross public debt should continue hovering below 55.0% of GDP (or slightly over 60.0%, when considering guaranteed debt) over the forecast horizon. High gross financing needs (c. 15.0% of GDP), due to Eurobond amortizations, remain, however, a vulnerability.

DETAILED MACROECONOMIC DATA

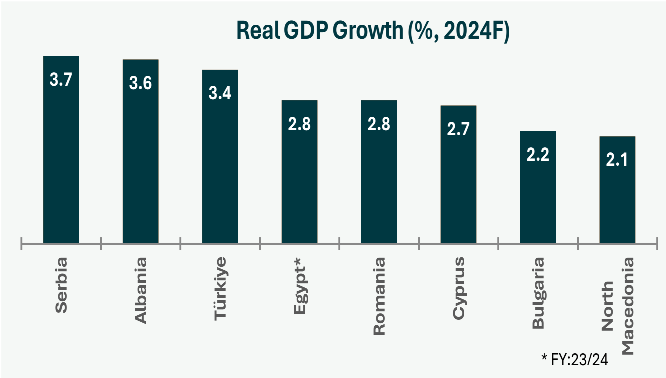
BULGARIA					
	2021	2022	2023e	2024f	2025f
Real Sector					
Nominal GDP (EUR million)	71,059	85,799	93,947	99,182	105,849
GDP per capita (EUR)	10,390	12,621	13,094	14,766	15,855
GDP growth (real, %)	7.7	3.9	1.8	2.2	3.3
Unemployment rate (ILO definition, %, aop)	5.3	4.2	4.3	4.3	4.2
Prices and Banking					
Inflation (%, eop)	7.8	16.9	4.7	3.5	3.0
Inflation (%, aop)	3.3	15.2	9.6	3.3	3.3
Loans to the Private Sector (% change, eop)	8.3	12.2	10.9		
Customer Deposits (% change, eop)	9.0	14.4	9.6		
Loans to the Private Sector (% of GDP)	47.6	44.3	44.0		
Retail Loans (% of GDP)	20.5	19.5	20.3		
Corporate Loans (% of GDP)	27.1	24.8	23.7		
Customer Deposits (% of GDP)	69.1	65.5	64.3		
Loans to Private Sector (% of Deposits)	69.0	67.6	68.4		
Foreign Currency Loans (% of Total Loans)	28.7	25.7	23.3		
External Accounts					
Merchandise exports (EUR million)	34,405	47,145	43,439	45,716	47,793
Merchandise imports (EUR million)	37,291	52,219	46,990	49,545	52,102
Trade balance (EUR million)	-2,887	-5,074	-3,551	-3,829	-4,309
Trade balance (% of GDP)	-4.1	-5.9	-3.8	-3.9	-4.1
Current account balance (EUR million)	-1,225	-1,200	0,274	0,593	0.679
Current account balance (% of GDP)	-1.7	-1.4	0.3	0.6	0.6
Net FDI (EUR million)	1,249	2,098	2,902	3,018	3,169
Net FDI (% of GDP)	1.8	2.4	3.1	3.0	3.0
International reserves (EUR million)	34,597	38,424	41,706	43,846	46,224
International reserves (Months[a])	9.8	7.8	9.2	9.2	9.2
Public Finance					
Primary balance (% of GDP)	-2.4	-0.4	-2.6	-2.8	-2.0
Fiscal balance (% of GDP)	-2.8	-0.8	-3.1	-3.2	-2.6
Gross public debt [b] (% of GDP)	23.9	22.6	23.2	25.1	26.1
External Debt					
Gross external debt (EUR million)	41,317	44,249	45,069	45,128	45,197
Gross external debt (% of GDP)	58.1	51.6	48.0	45.5	42.7
External debt service (EUR million)	7,000	8,200	7,100	7,250	7,500
External debt service (% of reserves)	20.2	21.3	17.0	16.5	16.2
External debt service (% of exports)	16.0	13.8	12.4	12.0	11.8
Financial Markets					
Base Interest Rate (%, eop)	0.0	1.3	3.8	3.2	2.6
Base Interest Rate (%, aop)	0.0	0.2	2.9	3.5	2.9
10-Y Bond Yield (%, eop)	0.7	6.0	4.5	4.2	3.9
Exchange rate: EUR (eop)	1.956	1.956	1.956	1.956	1.956
Exchange rate: EUR (aop)	1.956	1.956	1.956	1.956	1.956

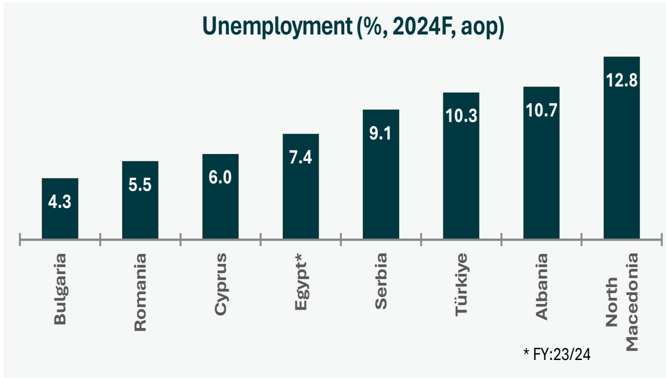
f: NBG forecasts; a: months of imports of GNFS; b: ESA 2010

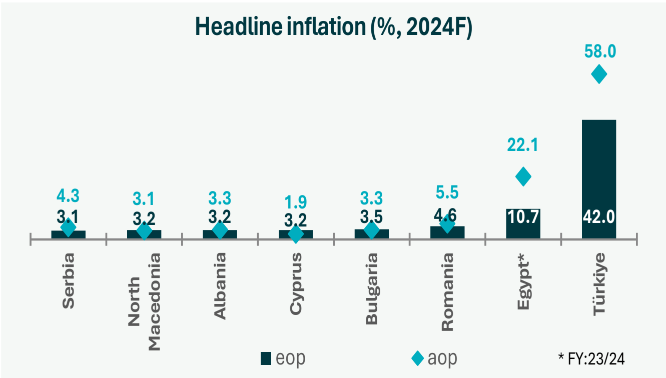
NORTH MACEDONIA	2021	2022	2023e	2024f	2025f
Real Sector					
Nominal GDP (EUR million)	11,855	13,053	13,667	14,376	15,252
GDP per capita (EUR)	6,454	7,135	7,501	7,922	8,438
GDP growth (real, %)	4.5	2.2	1.0	2.1	3.3
Unemployment rate (%, aop)	15.4	14.4	13.0	12.8	12.5
Prices and Banking					
Inflation (%, eop)	4.9	18.7	3.6	3.2	2.4
Inflation (%, aop)	3.2	14.0	9.5	3.1	2.7
Loans to the Private Sector (% change, eop)	8.0	8.8	5.2		
Customer Deposits (% change, eop)	8.5	5.1	9.5		
Loans to the Private Sector (% of GDP)	52.5	51.9	49.2		
Retail Loans (% of GDP)	27.5	26.4	25.4		
Corporate Loans (% of GDP)	25.0	25.3	23.6		
Customer Deposits (% of GDP)	60.7	58.0	57.3		
Loans to Private Sector (% of Deposits)	86.5	89.5	85.9		
Foreign Currency Loans (% of Total Loans)	40.7	42.6	42.0		
External Accounts					
Merchandise exports (EUR million)	6,041	7,320	7,292	7,640	7,952
Merchandise imports (EUR million)	8,378	10,801	9,868	10,518	11,084
Trade balance (EUR million)	-2,337	-3,481	-2,576	-2,879	-3,132
Trade balance (% of GDP)	-19.7	-26.7	-18.9	-20.0	-20.5
Current account balance (EUR million)	-0,329	-0,797	-0,095	-0,099	-0,204
Current account balance (% of GDP)	-2.8	-6.1	0.7	-0.7	-1.3
Net FDI (EUR million)	0,388	0,654	0,523	0,471	0.499
Net FDI (% of GDP)	3.3	5.0	3.8	3.3	3.3
International reserves (EUR million)	3,643	3,863	4,538	4,788	4.963
International reserves (Months[a])	4.5	3.7	4.6	4.6	4.5
Public Finance					
Primary balance (% of GDP)	-4.1	-3.3	-3.4	-2.5	-2.0
Fiscal balance (% of GDP)	-5.3	-4.4	-4.9	-3.9	-3.3
Gross public debt [b] (% of GDP)	59.8	58.5	61.5	62.8	62.7
External Debt					
Gross external debt (EUR million)	9,577	10,856	11,453	12,004	12,507
Gross external debt (% of GDP)	80.8	83.2	83.8	83.5	82.0
External debt service (EUR million)	2,689	2,558	4,043	3,761	4,342
External debt service (% of reserves)	73.8	66.2	89.1	78.5	87.5
External debt service (% of exports)	34.5	26.5	40.7	35.9	39.5
Financial Markets					
28-d CB bill rate (%, eop)	1.3	4.8	6.3	5.3	4.5
28-d CB bill rate (%, aop)	1.3	2.5	5.8	6.0	4.7
1-Y T-bill rate [c] (%, eop)	0.7	3.5	4.3	3.7	3.2
Exchange rate: EUR (eop)	61.6	61.6	61.6	61.6	61.6
Exchange rate: EUR (aop)	61.5	61.5	61.5	61.6	61.6

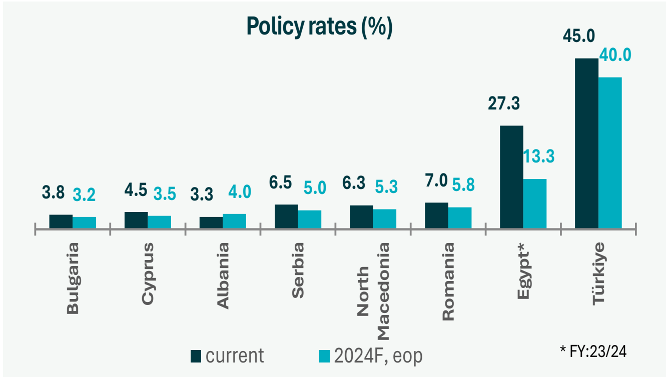
f: NBG forecasts; a: months of imports of GNFS; b: incl. guaranteed debt; c: primary market

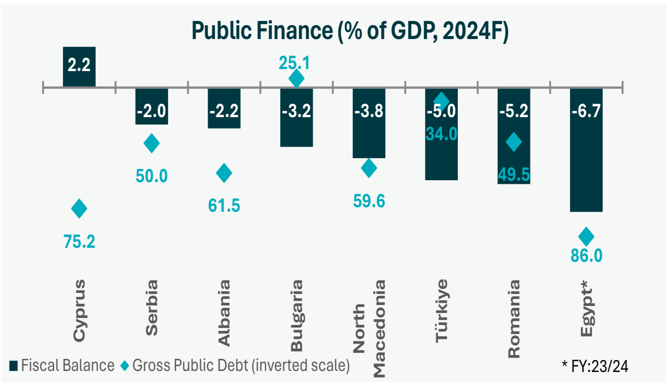
REGIONAL SNAPSHOT: MACROECONOMIC INDICATORS

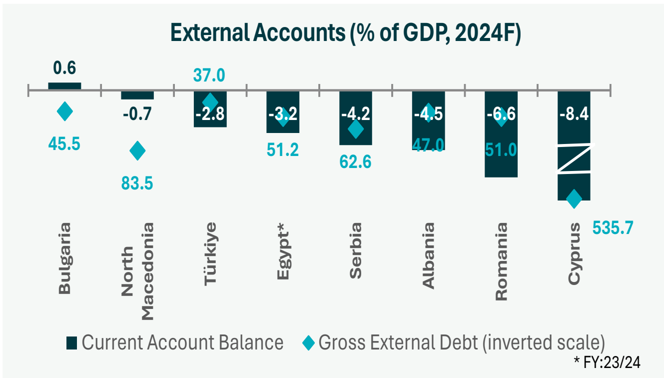


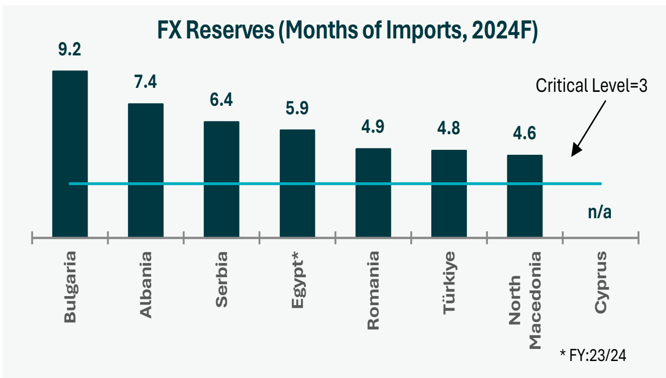






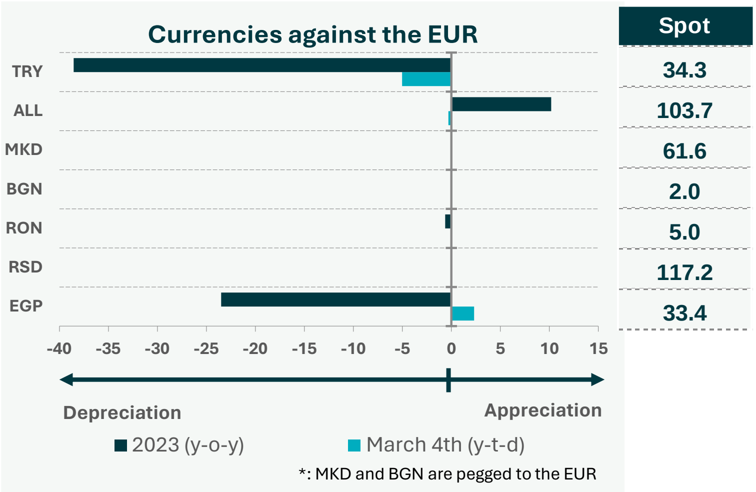


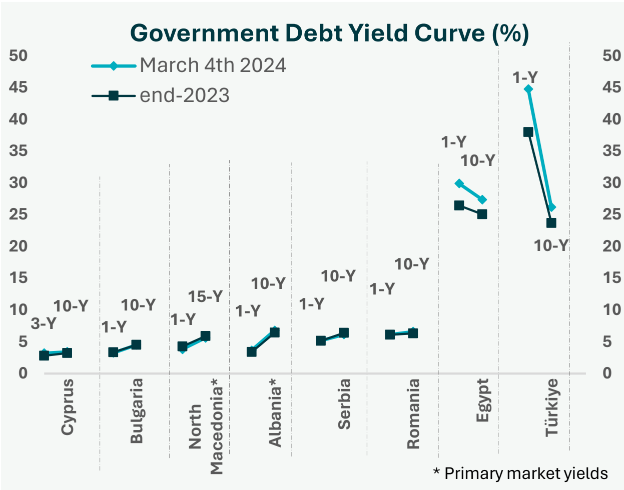


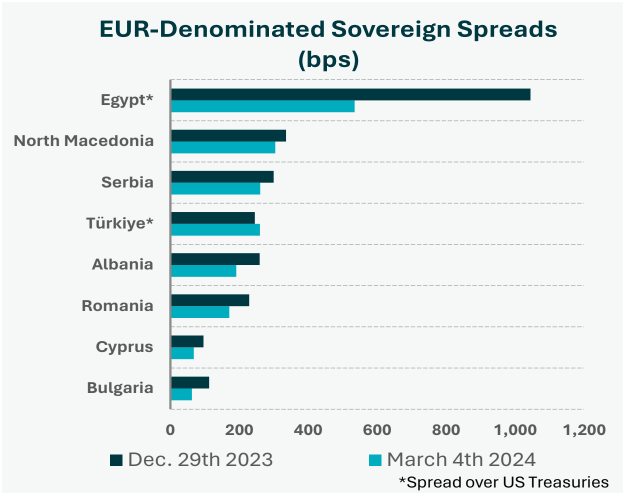


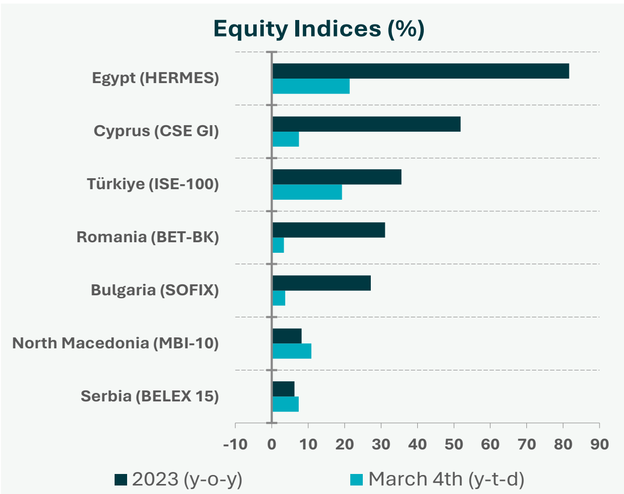
Sources: National Sources & NBG estimates

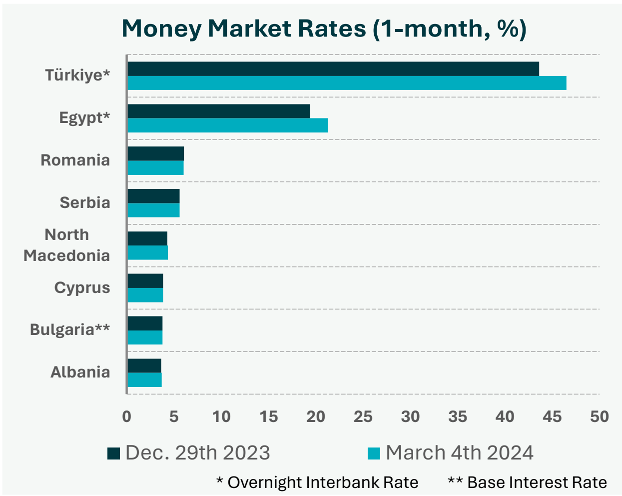
REGIONAL SNAPSHOT: FINANCIAL MARKETS











Sources: Reuters & NBG estimates


FOCUS
ECONOMICS
Analyst Forecast Awards
2023
NATIONAL BANK
OF GREECE
FOCUS
ECONOMICS
ANALYST FORECAST
AWARDS
2023
NBG Economic Analysis - Best Forecaster
among Greek banks for Greece and South Eastern Europe