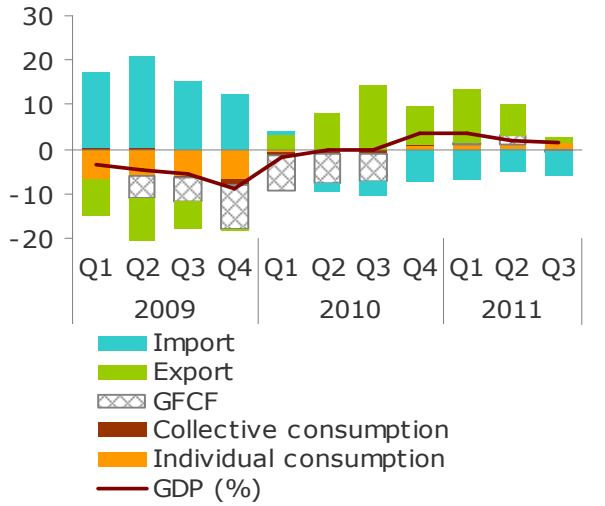
Macroeconomic environment and policies in brief

- Preliminary data on **Q3 2011 GDP has been revised up to 1.6% yoy** (s.a. data), as compared to the 1.3% flash estimate, thus Bulgarian growth came higher than the EU average (1.4% yoy). Better performance was a result of higher export growth and slower decline in investment. Imports also reported stronger growth, driven mainly by the ongoing recovery in households' consumption. However, the uncertain international juncture subdued economic activity in the country, resulting in a moderate 0.3% growth from the previous quarter.
- Seasonal recovery in the **labor market** continued in the third quarter, which was confirmed by the downward dynamics of the unemployment rate to 10.2%. In line with expectations annual **HICP inflation** moderated significantly starting Q2 and stabilized around 3% as of October amid easing agricultural and energy commodity prices. Weak labour market also kept inflation in check.
- **Current account balance** continued to improve, as the surplus for the first nine months of 2011 stood at 4% of GDP, reflecting positive dynamics in trade and services balance. Financial account remained negative in September, though FDI increased during the month, reaching EUR 534.5 mln in Jan-Sept. The overall balance of payments also came positive at EUR 21.3 mln, thus the accumulated deficit in January-September narrowed to EUR 102.5 mln. **International reserves** reached EUR 13.2 bn at end-November, up 0.9% over the month, being enough to cover 6.5 months of imports and 121.5% of the short-term external debt as of end-September.
- **Gross external debt** decreased to 93.5% of GDP (EUR 36.12 bn) at end-September. Maturity structure remained practically unchanged as the long- and short-term debt remained at 70 and 30% respectively.
- **Money supply growth** decelerated slightly as of end-October due to reduction in non-financial enterprises' deposits, caused probably by some private external debt repayments made by Bulgarian firms, while **private sector credit growth** remained broadly unchanged.
- **Fiscal consolidation continued in 2011 supported by stringent expenditure policies and gradual improvement on the revenue side**. General government deficit amounted to BGN 842.1 mln (1.1% of GDP) in Jan-Oct 2011, down by 1.6 pps compared to corresponding period in 2010.
- Bulgaria is the only EU Member State recording a **drop in long-term interest rate for a fourth month in a row**. The entire benchmark yield curve regarding Bulgarian government bonds has been shifting to lower yield levels in all maturity segments since August 2011. Bulgarian debt market sustainability to imported external shocks is also evident from renewed declining spread trend to German bunds. The absence of high volatility of the sovereign credit spread is largely due to the active and market-oriented policy on government debt management, as well as to the stability of the entire financial sector.

Recent Economic Developments

- Preliminary data on **Q3 2011 GDP has been revised up to 1.6% yoy** (s.a. data), as compared to the 1.3% flash estimate. The uncertain international juncture subdued economic activity in the country, resulting in a moderate 0.3% growth from the previous quarter.

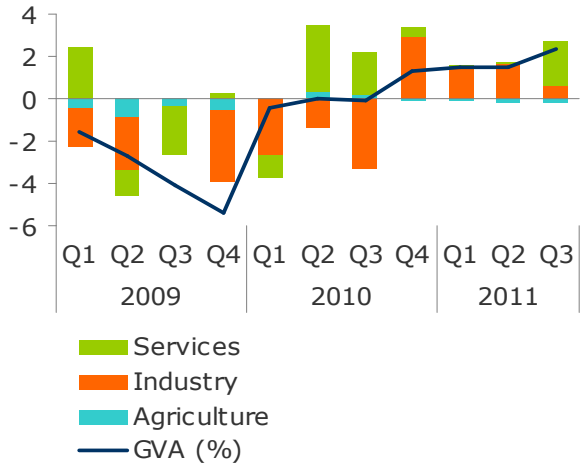
Contributions to GDP growth
(pps, yoy)



Source: NSI

- Individual **consumption** had the largest contribution for the registered annual growth, seeing that households' consumption continued to recover and reported a 1.9% yoy increase. For the first time since 2008, **external sector** contributed negatively to growth, as imports of goods and services kept expanding, up 8.1% yoy, while exports growth slowed sharply to 2% due to a decline in demand from major trading partners, as well as some base effects. **Investment activity** also moved to contraction territory, as gross fixed capital formation stood negative at 2.8% yoy.
- **Gross value added** expanded by 2.3% yoy with industry and services largely accounting for developments on the supply side. **Industrial sector** growth slowed to 2.2% yoy, being 5.9% in Q2, construction still in the red. Value added growth in **services** accelerated to 3.2%, signaling a slight revival in domestic demand, while **agriculture** value added decreased by 2.3%.

Gross value added
(pps, yoy)

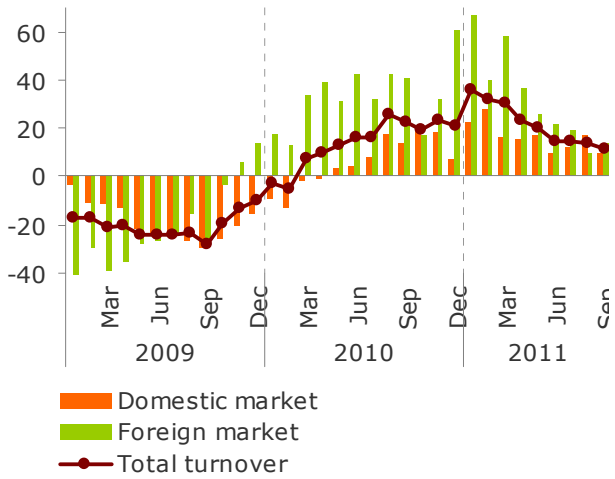


Source: NSI

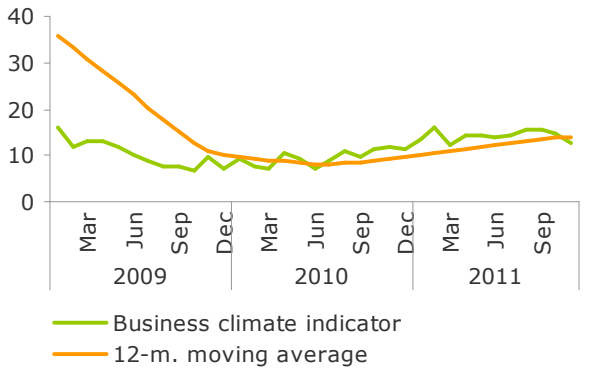
- **Industrial turnover** slowed its annual growth to 11.7% yoy in September. In contrast to its gradual downward tendency during last five months, foreign market sales accelerated to 14.2%, while positive trend in domestic turnover broke and domestic sales decelerated to 10.2%.
- Growth in **industrial production** also slowed to 1.6% in real terms. According to the production purpose, non-durable consumer goods had a negative contribution for the first time since the beginning of the year.
- **Retail sales** decreased by 3% yoy, led by the slump in retail sales of audio and video equipment, down 11.2% yoy.
- **Construction production index** decrease also amplified to 10.5% yoy, being 8.2% in August, as the decline in both building construction and civil

engineering deepened to 6 and 16.6% respectively.

Industrial turnover
(%, yoy)



Business climate
(balance)



Source: NSI

- **Business climate** in the country fell by 2.1 points in November. Future expectations worsened, as respondents in all sectors except for retail trade indicated an increase in problems arising from the uncertain economic environment. Business climate improved only in retail trade, still sale expectations in the latter also decreased.
- Seasonal activities supported the continuing **labour market revival**, however, negative annual trend carried on. Q3 employment number (LFS) increased by 2.9% qoq, mainly determined by construction, several processing industries and trade. It was accompanied by a rise in population participation rate - up 0.9 pps to 51.9%[1], and a decrease in unemployment rate to 10.2%. The ongoing economic restructuring, construction sector difficulties and slow domestic demand recovery continued impeding reversal in negative annual labour market tendency. Q3 employment number decreased by 2.8%, thus the unemployment rate stood 0.7 pps higher compared to Q3 2010.

Employment growth (%) **and Unemployment rate** (level)

Source: NSI

- The number of **registered unemployed people** stepped up by 1.3% mom to 314.1 K in October. Thus the jobless rate increased marginally to 9.6%, though it stood 4.9% lower compared to a year earlier. Unemployment inflow went up over the month, reflecting seasonal activities fall, as well as the expenditure consolidation in the government sector. The outflow of unemployed also stepped up, influenced strongly by the higher number of persons who started working in October – 21.1 K. Labour

[1] For the age group of 15 and over.

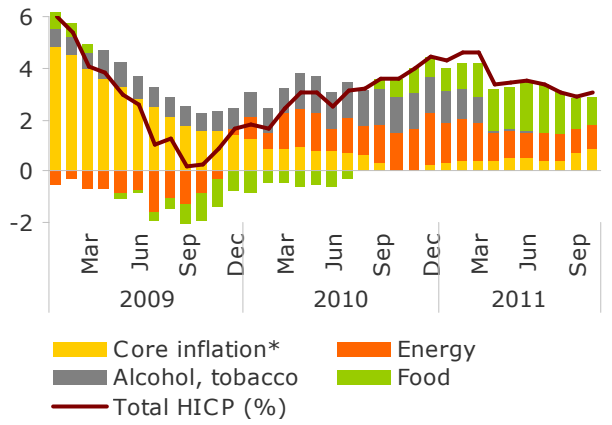
demand on the primary market traditionally decreased, however, subsidized employment programs were strengthened, with some 10.5 K new people who found jobs under programs and measures during the month.

Inflow, outflow and total number of unemployed people (in thousands)

Source: EA

- Consumer prices increased in line with the expectations, up 0.3% mom in October. The overall **inflation dynamics** was largely led by the upward seasonal pattern in domestic food prices, which increased by 1%, as well as the higher prices of clothing and footwear, up 3.7% mom. These price changes have been partially offset by the decline in automotive fuels and market services prices, down by 0.5 and 0.1% mom respectively. The **annual HICP inflation remained broadly stable**, standing at 3%. Turning to its structure, trends in inflation contributions by main components remained practically unchanged, as food prices inflation slowed further and energy prices contribution remained relatively constant compared to September. Despite the weak domestic demand, core inflation continued to pick up from the bottom and stood at 1.5% yoy. Non-energy industrial goods largely accounted for its dynamics, as their negative inflation rate narrowed to only 0.2% due to higher apparel and footwear prices during the month.

HICP and contributions by main groups (pps, yoy)

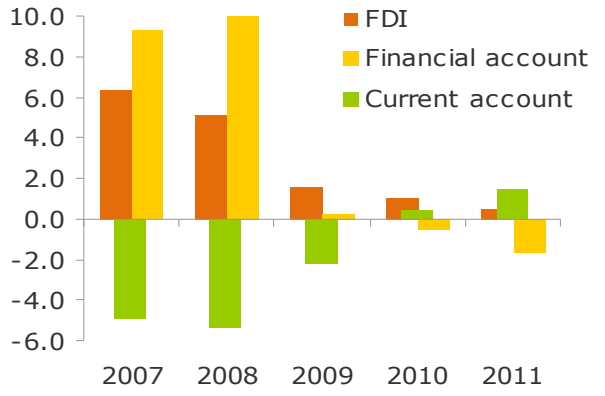


Source: NSI, MF

- **Current account surplus** amounted to EUR 119.7 mln in September, thus the accumulated surplus for the first nine months of the year stood at EUR 1.5 bn (4% of GDP). Trade balance improvement had the largest contribution, as its accumulated deficit for the first nine months dwindled to EUR 780.2 mln, being EUR 1.7 bn for the corresponding period a year earlier. Exports of goods rose by 18% during the month, while in Jan-Sept its growth amounted to 32% yoy. For the first nine months Bulgarian companies exported goods worth EUR 14.8 bn. As to imports, its growth rate accelerated to 20% yoy in September alone, being 12.6% a month earlier. Imported goods in Jan-Sept amounted to EUR 15.6 bn, up 20.4% compared to corresponding period in 2010.
- During September, the last month of the active summer tourist season in Bulgaria, "**Services" balance** increased by 3.7% yoy, reaching EUR 298.7 mln. Bulgarians continued spending less on other foreign services, these

expenditures stepping down 51.8% yoy. As a result, services sector surplus reached EUR 2.09 bn for the first nine months of 2011. For the same period the income deficit rose by 13.3% up to EUR 1.17 bn. August data on income deficit was revised upwards, thus the hypothesis for the possible change in trend has been denied. In Jan-Sept net current transfers increased by 9.3% yoy to EUR 1.36 bn, while registering a 45.4% drop in September alone.

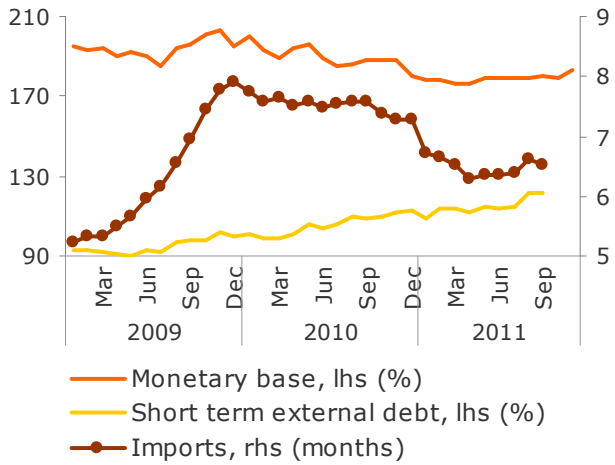
FDI, Current and Financial Account
(January - September, billion euro)



Source: BNB

- **Financial account** turned slightly negative in September and stood at EUR 7.1 mln. The accumulated deficit since January remained generally unchanged at EUR 1.67 bn. Foreign investments in the country amounted to EUR 193.4 mln in September alone, reaching EUR 534.5 mln in Jan-Sept. Yet the latter remained much lower compared to EUR 1.03 bn of FDI attracted during the same period in 2010. "Net other investments" article reported positive balance at EUR 63.3 mln, as Bulgarian banks withdrew deposits from abroad worth EUR 196.9 mln, thus their deficit from the beginning of the year narrowed marginally to EUR 1.66 bn.
- The **overall balance of payments** was positive again at EUR 21.3 mln, limiting the accumulated deficit to EUR 102.5 mln, which is an improvement compared to EUR 449.3 mln deficit for the same period of 2010.
- **Gross external debt** (GED) stood at 93.5% of GDP (EUR 36.12 bn) at end-September, down by 8.4 pps yoy and 0.1 pps mom. External debt stock of the banking system contracted further, as its rate of change accelerated to 13.2% yoy. At the end of the month banking sector foreign debt stood at 17.1% of GED (being 19.4% a year earlier). Other sectors foreign debt rose by 4.5% yoy, as the stock of short-term loans went up by 7.8%. Meanwhile, intercompany loans decreased to EUR 14.66 bn, being EUR 14.78 bn twelve months earlier, as local firms continued repaying outstanding debt to their mother-companies abroad. Maturity structure remained practically unchanged as the long- and short-term debt remained at 70 and 30% respectively.

Coverage with FX Reserves



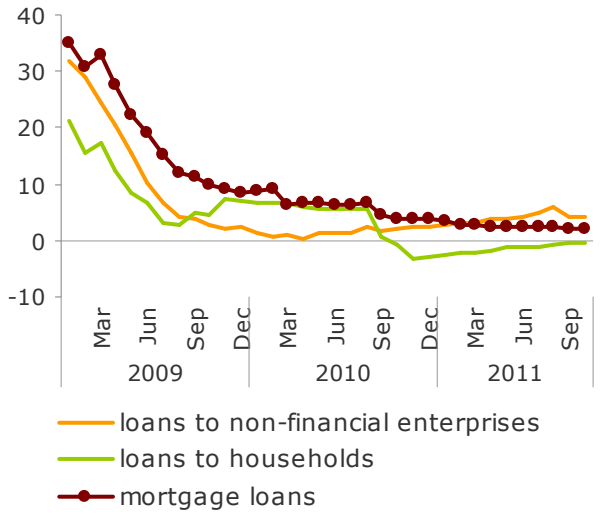
Source: BNB, MoF

- **International reserves** reached BGN 13.2 bn at end-November, up 0.9% over the month, largely due to a 7.7% mom increase in the Government deposit and to a smaller extent to Bank Department deposit increase by 1.1%. Bank reserves had a negative impact on total reserves, as they dropped 2% mom. Monetary

base coverage improved compared to October and stood at 183.3%. At the end of September BNB reserves were enough to cover 6.5 months of imports and 121.5% of the short-term external debt.

- **Money supply growth** decelerated slightly to 9.6% yoy as of end-October, coming from 10.3% a month earlier. Despite the faster increase in liquid monetary aggregate M1, up 6.3% vs. 5.5% in September, the slowing annual growth rate of deposits with agreed maturity up to 2 years by almost 2 pps kept broad money increase subdued. Money supply decreased by 0.5% over the month due to a 0.2% drop in M1 and a 0.9% decline in the deposits with agreed maturity up to 2 years. The reduction in non-financial enterprises' deposits, caused probably by some private external debt repayments made by Bulgarian firms, largely accounted for these developments. Total deposits dropped by 0.4% in October, leading to a slowdown in their yoy growth to 10.5% at the end of the month.

Credit growth
(% change, yoy)

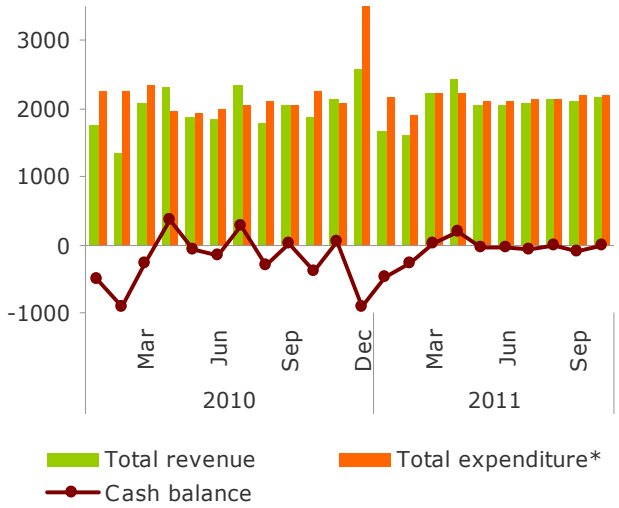


Source: BNB, MoF

- **Private sector credit growth** remained broadly unchanged at 2.3% as of end-October. Corporate credits annual rate of increase stood at 4.1%, showing practically no change from a month earlier, while loans to households limited their decrease to below 0.1% yoy. Consumer credits dropped 0.3% yoy, while mortgages continued growing by a marginally declining positive rate of 2.1%.
- **Bulgarian banking system operates smoothly** and continues maintaining high capital and liquidity buffers. The capital adequacy ratio at end-September reached 17.8%, while the ratio of liquid assets at end-October improved during last twelve months from 22.2% to 25.9%. Banks' stable positions are largely determined by the sustained high growth of funds attracted by households and corporations, up 14.1% and 10.3% yoy respectively. The banking system reported a net profit of EUR 514 mln, return on assets being 0.82% at end-October.
- **Interest rates** on short-term credits in all currencies declined in October. Nevertheless, a more significant volume increase in newly lent credits was seen only in euro denominated corporate loans. The cost of long-term credits slightly increased, though volumes remained at their September level. Deposit rates increased for BGN denominated deposits and declined for FX denominated ones. However, newly acquired deposits in both local and foreign currency decreased over the month.
- **Consolidated budget deficit** stood at BGN 842.1 mln (1.1% of GDP) on cash basis at the end of October, down by approximately 1.6 pps (a BGN 1060.6 mln decrease in nominal terms) as compared to deficit level a year earlier.
- **Total revenue** accounted for 78.3% of the 2011 annual plan, up 6.7% in

nominal terms compared to October 2010. Tax revenue collected during the first 10 months of the year stepped up by 11.6% yoy to 81.9% of the annual forecast, the 12.5% increase in indirect taxes having the largest positive contribution. VAT, excises and custom duties revenues increased as well, up by 13.4, 10.6 and 9.1% respectively in yoy terms. Total social and health insurance contributions accumulated in January-October came 11% higher compared to corresponding period in 2010[2]. Direct taxes also grew, up 9.3% yoy. Non-tax revenue remained broadly on their October 2010 level, while grants decreased.

Consolidated Budget
(monthly value, mln BGN)



** incl. contribution to EU budget*

Source: MoF

- **Total expenditure** amounted to 75.8% of the annual forecast, up 1.1% in nominal terms on a year earlier. It was mainly driven by the increase in social expenditures and maintenance.
- **Fiscal reserve** stood at BGN 5.3 bn at end-October.
- **General government debt**, including government guaranteed debt, accounted for 15.7% of GDP at end-September, of which 5.5% of GDP domestic debt, 8.6% of GDP external debt and 1.6% of GDP government guaranteed debt.

[2] The administratively determined rate of social contributions has been raised by 1.8 pps since January 2011.

Key Economic Indicators

		2008	2009	2010	Q4 '10	Q1 '11	Q2 '11	Q3 '11	V '11	VI '11	VII '11	VIII '11	IX '11	X '11
GDP*														
Gross Domestic Product*	%, yoy	6.1	-5.5	0.2	3.7	3.3	2.0	1.6						
Consumption	%, yoy	2.5	-7.3	-1.1	0.5	1.2	1.4	1.6						
Gross fixed capital formation	%, yoy	16.3	-24.9	-14.0	-0.9	1.6	8.4	-2.8						
Export	%, yoy	3.0	-11.2	16.2	15.2	21.6	12.2	2.0						
Import	%, yoy	4.2	-21.0	4.5	10.7	10.0	7.5	8.1						
Agriculture	%, yoy	29.6	-6.1	3.9	-1.5	-1.4	-2.5	-2.3						
Idustry	%, yoy	4.4	-7.8	1.9	10.5	5.4	5.9	2.2						
Services	%, yoy	5.0	-0.8	-0.9	0.6	0.1	0.1	3.2						
Adjustments	%, yoy	5.7	-16.5	-0.2	5.2	7.9	5.3	2.6						
Short term business statistics														
Industrial production	%, yoy	0.7	-18.3	2.0	5.2	10.6	6.3	3.1	9.1	1.6	5.1	2.6	1.5	2.5
Industrial turnover	%, yoy	13.7	-20.2	14.1	21.1	32.6	19.1	13.5	20.2	14.5	15.0	14.1	11.7	10.8
Retail trade turnover	%, yoy	8.9	-8.9	-5.6	-4.3	0.4	0.4	-2.9	1.8	-0.9	-3.0	-2.7	-3.0	-5.2
Construction output	%, yoy	12.7	-14.5	-18.0	-8.5	-14.8	-14.4	-11.0	-16.9	-3.7	-14.2	-8.1	-10.8	-10.2
Total business climate	balance	38.0	10.2	9.6	11.5	13.8	14.1	15.2	14.2	13.8	14.5	15.6	15.5	14.8
Industrial confidence	balance	39.9	12.3	13.4	15.0	21.6	22.8	24.1	22.1	21.6	22.7	24.7	24.9	23.1
Retail trade confidence	balance	41.3	13.5	10.1	13.0	13.0	10.7	20.2	11.2	9.5	13.1	23.9	23.6	23.9
Construction confidence	balance	40.3	8.5	5.1	2.9	4.7	4.4	3.9	5.7	5.6	8.2	2.5	1.1	1.4
Services confidence	balance	28.7	5.1	5.6	11.8	8.1	10.1	3.8	9.8	10.7	5.7	2.5	3.1	2.4
Labour market														
Participation rate (15+)	level	53.8	53.0	52.0	52.1	50.8	51.0	51.9						
Employment rate (15+)	level	50.8	49.4	46.7	46.3	44.7	45.3	46.6						
Employment (LFS)	%, yoy	3.3	-3.2	-6.2	-4.7	-4.0	-4.5	-2.8						
Unemployment rate (LFS)	level	5.6	6.8	10.2	11.2	12.0	11.2	10.2						
Unemployment rate (EA)	level	6.3	7.6	9.5	9.1	10.9	10.1	9.5	10.0	9.7	9.6	9.6	9.4	9.6
Nominal wage	%, yoy	26.5	11.8	6.3	10.4	8.5	9.3		9.1	8.5				
Real wage**	%, yoy	13.0	9.1	3.2	6.1	3.8	5.7		5.5	4.8				
Labour productivity (GDP per employed)	%, yoy	3.5	-2.9	6.4	7.8	5.2	6.0							
Real ULC	%, yoy	3.7	8.1	-2.2	-6.7	-7.0	-3.4							
Prices														
Harmonized index of consumer prices	%, yoy	11.9	2.5	3.0	4.0	4.5	3.4	3.1	3.4	3.5	3.4	3.1	2.9	3.0
Domestic producer prices	%, yoy	13.3	-4.3	7.2	11.1	11.9	10.3	7.2	10.0	10.1	8.4	6.6	6.6	6.5
Consolidated fiscal program (cummulative)														
Revenue and grants	mln BGN	27313	25041	23933	23933	5530	12042	18354	9997	12042	14119	16242	18354	20519
Total expenses	mln BGN	25323	25667	26755	26755	6272	12692	19180	10595	12692	14839	16973	19180	21361
Contribution to EU budget	mln BGN	720	746	670	670	250	367	528	330	367	422	466	528	588
Cash deficit(-) / surplus(+)	mln BGN	1990	-626	-2823	-2823	-742	-651	-826	-598	-651	-721	-731	-826	-842
	% GDP	2.9	-0.9	-4.0	-4.0	-1.0	-0.9	-1.1	-0.8	-0.9	-0.9	-1.0	-1.1	-1.1
Government and gov. guaranteed debt	mln BGN	10710	10641	11778	11778	11447	11573	11944	11532	11573	11708	11763	11944	
	% GDP	15.5	15.6	16.7	16.7	15.1	15.3	15.7	15.1	15.2	15.4	15.4	15.7	
Fiscal reserve	mln BGN	8382	7673	6012	6012	4699	5154	5071	4986	5154	4881	4993	5071	5342
	%, yoy	12.5	-8.5	-21.6	-21.6	-26.1	-14.5	-24.4	-24.3	-14.5	-22.8	-19.0	-24.4	-16.5
Financial sector														
BNB International reserves	mln EUR	12713	12919	12977	12977	12209	12340	13051	12245	12340	12500	13079	13051	13176

		2008	2009	2010	Q4 '10	Q1 '11	Q2 '11	Q3 '11	V '11	VI '11	VII '11	VIII '11	IX '11	X '11
Monetary base coverage	%	175.3	195.2	179.8	179.8	176.3	179.2	180.7	179.3	179.2	178.9	179.7	180.7	179.7
Coverage of import with FX reserves	months	5.4	8.0	7.3	7.3	6.5	6.4	6.5	6.3	6.3	6.4	6.6	6.5	
Coverage of short-term external debt	%	96.5	100.2	112.8	112.8	112.4	113.6	121.5	114.7	113.6	115.1	121.3	121.5	
Money M1 (Narrow money)	%, yoy	-4.1	-8.8	0.8	0.8	4.9	3.7	5.5	3.5	3.7	5.2	6.8	5.5	6.3
Money M3 (Broad money)	%, yoy	8.8	4.2	6.2	6.2	7.4	8.0	10.3	7.9	8.0	9.4	9.4	10.3	9.6
Deposits	%, yoy	8.8	7.6	6.6	6.6	8.2	8.8	11.3	8.6	8.8	10.3	10.4	11.3	10.5
Credit to private sector	%, yoy	32.9	3.8	1.1	1.1	1.6	2.1	2.2	2.2	2.1	2.5	3.3	2.2	2.3
Credit to non-financial enterprises	%, yoy	33.1	2.3	2.4	2.4	3.0	4.1	4.1	3.7	4.1	4.8	6.1	4.1	4.1
Credit to households	%, yoy	31.4	5.8	-0.8	-0.8	-0.7	-0.6	-0.2	-0.6	-0.6	-0.5	-0.4	-0.2	-0.1
Interest rate on short-term loans	%	10.9	10.5	8.5	8.0	6.4	7.3	7.3	8.3	7.3	7.6	7.9	7.3	7.0
Interest rate on time deposits	%	5.6	7.0	5.4	5.1	5.1	4.9	4.7	5.0	4.9	5.0	4.8	4.7	4.8
Exchange rate BGN/USD	eop	1.39	1.36	1.47	1.47	1.38	1.35	1.45	1.36	1.35	1.37	1.35	1.45	1.40
	per. av.	1.34	1.41	1.48	1.44	1.43	1.36	1.42	1.36	1.36	1.37	1.36	1.42	1.43
Gross External Debt														
Gross external debt	% GDP	104.9	108.0	101.8	101.8	93.9	94.0	93.5	93.8	94.0	93.8	93.6	93.5	
Short term external debt	% GED	35.4	32.7	31.4	31.4	30.0	29.9	29.7	29.4	29.9	30.0	29.8	29.7	
Intercompany lending	% GED	36.4	38.5	40.2	40.2	40.0	40.0	40.6	40.3	40.0	40.4	40.5	40.6	
Balance of payments														
Current account	mln EUR	-8162	-3118	-356	-871	147	97	1255	127	50	614	521	120	
Current account, % GDP moving average		-23.4	-8.7	-1.0	-1.3	0.7	1.8	0.0	1.6	1.8	2.0	2.1	1.6	
Trade balance	mln EUR	-8597	-4174	-2412	-1040	-11	-630	-139	-219	-208	43	3	-185	
Trade balance, % GDP moving average		-24.6	-11.6	-6.7	-7.7	-5.8	-5.0	-4.7	-4.8	-4.9	-4.6	-4.5	-4.7	
Export, f.o.b.	mln EUR	15204	11699	15588	4313	4777	4862	5208	1660	1596	1841	1673	1694	
	%, yoy	12.5	-23.1	33.2	32.8	57.5	28.0	17.9	37.0	12.9	20.5	15.1	18.1	
Import, f.o.b.	mln EUR	-23801	-15873	-18001	-5352	-4788	-5492	-5347	-1879	-1804	-1799	-1669	-1879	
	%, yoy	14.7	-33.3	13.4	28.9	30.2	17.4	15.8	20.0	13.7	12.8	13.8	20.8	
Capital account	mln EUR	277	477	291	140	16	45	120	-1	45	40	31	48	
Financial account	mln EUR	11473	1190	-1	358	-743	-273	-652	-80	-302	-149	-156	-95	
Net Foreign Direct Investments	mln EUR	6212	2498	1459	693	-120	176	398	54	12	66	149	182	
Net Portfolio Investments	mln EUR	-731	-570	-661	-150	-189	-18	-210	-148	-40	-13	51	-248	
Other Investments - net	mln EUR	5980	-719	-774	-185	-424	-424	-811	44	1	-729	-145	63	
Change in BNB reserve assets	mln EUR	-674	650	384	-65	665	-92	-470	-220	-131	-38	-411	-21	

** Reference year 2005, seasonally and working day adjusted data.*
*** HICP deflated.*

Recent Developments and Government Debt Review

The medium term yield on Bulgarian government debt has set at sustainably low levels

On November 7, the Ministry of Finance (MoF) conducted the last planned for this year reopening of the medium term BGN denominated benchmark bond with original maturity of 3.5 years, its newly tapped volume being BGN 50 mln. A clear tendency for yield reduction was observed as the average weighted yield on the auction reached 3.14%, which is the lowest rate so far. This happens notwithstanding the increased risk expectations of investors on the European sovereign debt markets related to their negative assumptions as to the exit from the debt crisis in the Euro area and the significant increase of the premium on the structured products for protection against credit risk of a number of issuers.

The issue was launched in December 2010, at a peak yield rate of 3.69%, and after the auction on November 7 the total nominal value of the issue reached BGN 306.5 mln. Thus high liquidity on the secondary market has been ensured and the benchmark status of the bond has been affirmed.

The average weighted yield on approved bids during the action of 3.14% is below the secondary market yield on the EUR denominated Eurobonds with similar residual maturity of such countries as Lithuania (3.66%), Turkey (4.18%), Croatia (4.72%), Hungary (6.15%) and Romania (5.36%).

The reopening of the 3.5-year GS issue, together with the decision of the MoF to also reopen the 7-year issue with residual maturity of 5.5 years, has contributed to meeting the higher demand for investment alternatives in the medium term segment of the debt curve. The excellent results from the auction are an evidence of the positive attitude of the local investment community towards the consistent fiscal policy pursued by the government. The sustainably high demand on the GS primary market and the yield reduction, respectively, is preconditioned mostly by the active involvement of banks and leading institutional investors.

Positive are the results of the analysis of the entire benchmark yield curve as regarding Bulgarian government bonds, which has been shifting to lower yield levels in all maturity segments since August 2011. The sustainability of the Bulgarian debt market to imported external shocks is also evident from the renewed trend of lowering spread as compared to German bunds. The absence of high volatility of the sovereign credit spread is largely due to the active and market-oriented policy on government debt management, as well as to the stability of the entire financial sector.

Bulgaria is the only EU Member State recording a drop in its long-term interest rate for a

Bulgaria is the only EU Member State recording a drop in its long-term interest rate for a fourth month in a row. According to the harmonized long-term interest rate published by ECB on November 11 on the basis of the 10-year government bond yield, it has dropped from 5.39% down to 5.27% in the period June-October 2011. According to ECB data, nine EU Member States have a figure higher than that of the Bulgarian long-term interest rate,

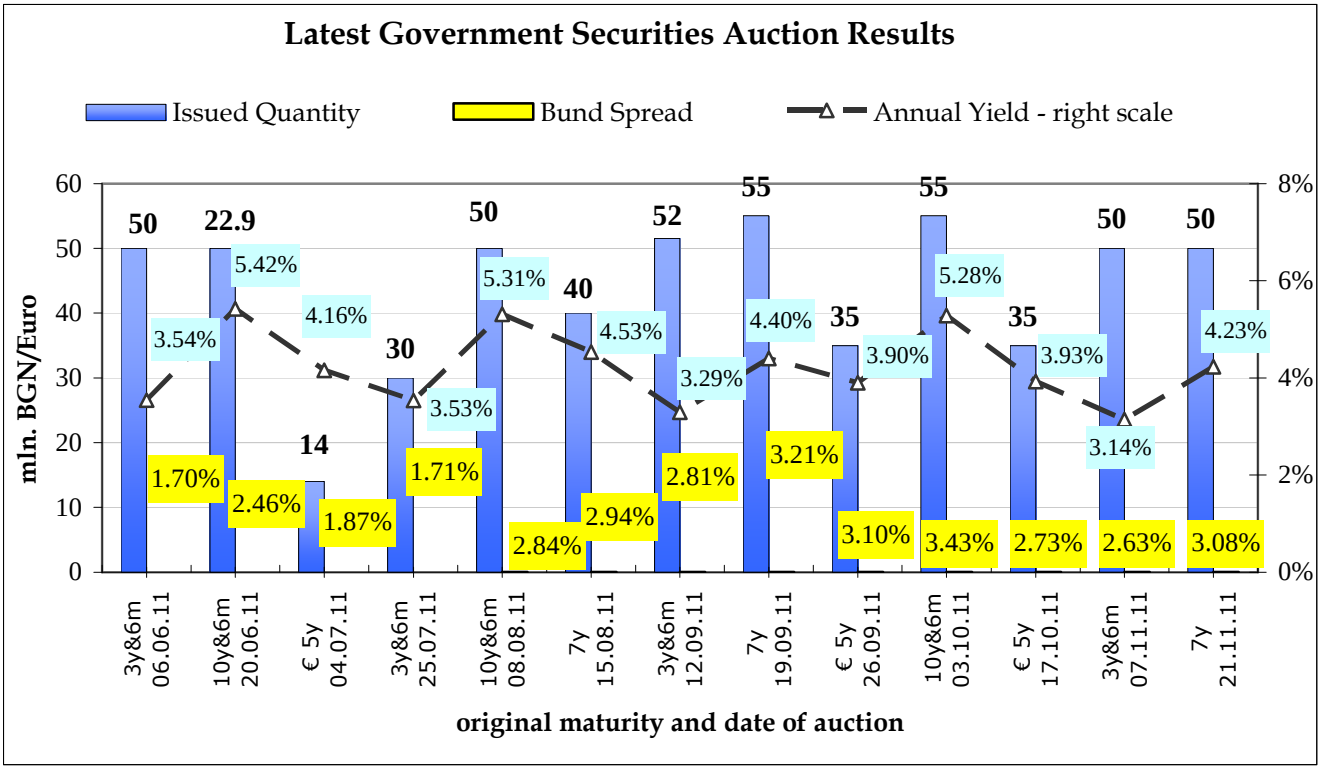
fourth month in a row

while two of the Member States have an interest rate very close to Bulgarian reading. Three more Member States only enjoy a reduction in the interest rate as against the previous reporting period.

The outcome of the auction held on November 21 to sell the 7-year bond issued in 2010 is in unison with the steady stabilization of Bulgaria's long-term debt dynamics and the dropping yield on the secondary market. The residual period of the issue as of the date of reopening is 5 years and 3 months, which explains the higher demand of investment alternatives in the medium-term segment of the debt curve in recent months.

The trend of reducing the yield on the primary market has been preserved, which resulted in a record drop in the weighted average annual yield of this issue. A yield of 4.23% was registered for the approved volume of BGN 50 mln as against 4.40% in the transitional reopening of the issue in September. The highest yield of this issue is 6.09%. This yield is better than the current yield of EUR denominated Eurobonds of similar residual maturity of Hungary (7.96%) and Turkey (4.86%).

The nominal value of the submitted bids on the auction amounted to BGN 121.9 mln, thus the issue was almost twice and a half oversubscribed. There was a very strong interest by the banks that are primary GS dealers, having made orders on their behalf and at their expense, as well at the expense of clients of theirs. The investor base assessment shows that in addition to the banks having acquired 43.1% of the total approved face value, there was a strong interest by institutional investors such as pension funds (35.13%), insurance and life insurance companies (11.9%) and other investors (9.87%).



Additional data on the auction results can be viewed on the site of the Bulgarian National Bank, that is a fiscal agent to the government www.bnb.bg

Stable nominal extent of government debt is of primary significance to government finance

By end-October, public debt amounted to EUR 5 516.8 mln, consisting of EUR 2 217.2 mln internal debt and EUR 3 299.6 mln external one. Debt rose by approximately EUR 16.7 mln in nominal terms over the previous month mainly due to the increase in domestic government debt as a result of the new internal financing, accomplished by means of GS issues. Government debt-to-GDP ratio was 14.3%.

Government Debt Amount

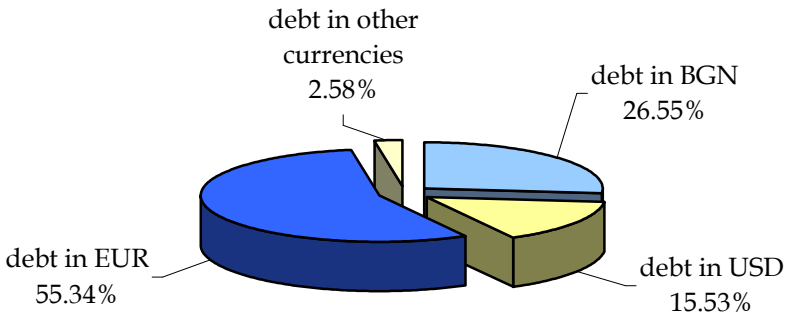
(million EUR)

Structure	31.12.2010	31.3.2011	30.6.2011	30.9.2011	31.10.2011
Domestic government debt	2 011.5	1 941.5	2 059.8	2 156.4	2 217.2
External government debt	3 373.5	3 319.5	3 272.1	3 343.7	3 299.6
Government Debt, total	5 385.0	5 261.0	5 331.9	5 500.1	5 516.8
Government Debt /GDP (%)	14.9	13.6	13.8	14.2	14.3

Government debt currency structure does not generate risks associated with its servicing

The currency structure of debt underwent again some positive change as both EUR and BGN denominated debt increased. Debt denominated in euro reached 55.3%, being 55% in September, while debt in BGN reached 26.6% up from 26.1% in September. Debt denominated in USD and other currencies decreased and reached 15.5% and 2.6% respectively.

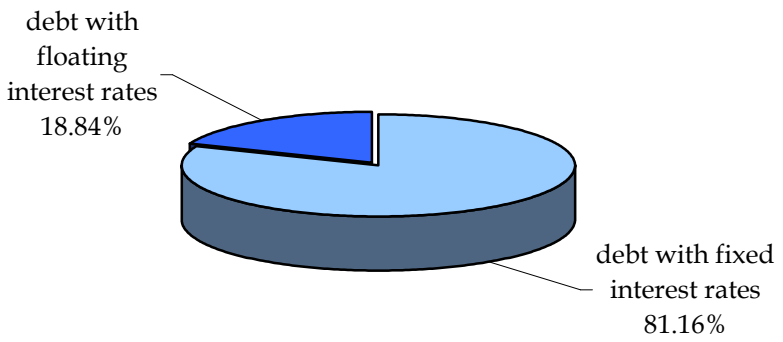
Government Debt Currency Structure as of 31 October



Debt interest rate structure provides predictability of the resources required for its servicing

Positive developments in debt interest rate structure continued in October, as the share of fixed interest rates debt increased somewhat to 81.2% following new internal financing during the month. Debt with floating interest rates narrowed to 18.8% (compared to 19.1% in September).

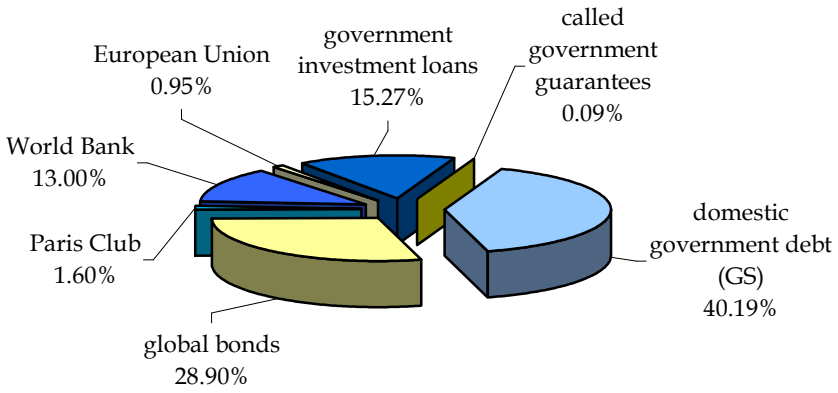
Government Debt Interest Rate Structure as of 31 October



Government debt portfolio structure is another key indicator for successful debt management policy

Debt structure by types of instruments and creditors in October showed no significant change, the largest relative share belonging to liabilities related to GS, issued on the domestic market - 40.2%, followed by global bonds - 28.9%, government investment loans - 15.3%, commitments to the World Bank - 13%, obligations to the Paris Club - 1.6%, the European Union - 1% and called state guarantees - 0.1%.

Government Debt Structure by Creditor as of 31 October



Comprehensive information on Bulgarian Government Debt, including monthly bulletins and annual reviews, cou be found at the website of Bulgarian Ministry of Finance.
http://www.minfin.bg/en/statistics/?cat=2&from=0&fyear=0&to=0&tyear=0&dq=&pokaz=0

For any further questions or comments, please contact Mrs. Milena Boikova, Director of Government Debt a Financial Markets Directorate, Ministry of Finance: email: M.Boikova@minfin.bg , tel. +359 2 9859 2450.