REPUBLIC OF BULGARIA
Ministry of Finance

CONVERGENCE PROGRAMME

(2023–2026)

2023
Sofia, Bulgaria

CONVERGENCE PROGRAMME

OF THE REPUBLIC OF BULGARIA 2023–2026

Sofia, 2023,
Ministry of Finance

Contents

List of Abbreviations

BNB	Bulgarian National Bank
CITL	Corporate Income Taxation Law
CP	Convergence Programme
SSC	Social Security Code
EC	European Commission
ECB	European Central Bank
EDTWL	Excise Duties and Tax Warehouses Law
ESA 2010	European System of Accounts 2010
ESSF	Electricity System Security Fund
EU	European Union
EUR	euro
FDI	Foreign direct investment
GDP	Gross Domestic Product
HICP	Harmonised Index of Consumer Prices
IMF	International Monetary Fund
LIBOR	London Interbank Offered Rate
MF	Ministry of Finance
NHIF	National Health Insurance Fund
NSSI	National Social Security Institute
NRA	National Revenue Agency
NRRP	National Recovery and Resilience Plan
NSI	National Statistical Institute
OECD	Organisation for Economic Development and Co-operation
PFL	Public Finance Law
pps.	percentage point
REER	Real effective exchange rate
RRF	Recovery and Resilience Facility
SGP	Stability and Growth Pact
TFP	Transitional and final provisions
ULC	Unit labour costs
VAT	value added tax
VATL	Value Added Tax Law

1. OVERALL POLICY FRAMEWORK AND OBJECTIVES

Bulgaria's Convergence Programme (CP) is prepared annually in April, based on the rules of the Stability and Growth Pact (SGP) – the regulatory framework for the coordination of national fiscal policies of European Union (EU) Member States. The Programme has been prepared in accordance with the Code of Conduct"[1], containing Specifications on the implementation of the SGP and Guidelines on the format and content of Stability and Convergence Programmes.

The Convergence Programme of the Republic of Bulgaria (2023–2026) reflects the fiscal effects on the parameters of the budgetary framework under a no-policy-change scenario. The choice of this scenario is a consequence of the limited mandate of the current caretaker government. The program is influenced by recent developments from the 2022 Budget and its subsequent update, as well as the political cycle related to the holding of early parliamentary elections in late 2022 and early 2023, respectively, and the fact that the current year budget was not adopted by the end of April 2023. This also led to the late submission to the National Assembly by the caretaker government of a draft Law on the State Budget of the Republic of Bulgaria for 2023 and the accompanying Updated Medium-Term Budget Forecast for the period 2023–2025, which constitutes the grounds for the draft law and reflects the macroeconomic and fiscal prospects and assumptions in the medium term based on current legislation, implying a significant deterioration of the deficit without the implementation of consolidation measures. There is a stated commitment by the leading political parties represented in the newly formed National Assembly to reduce the budget deficit to 3% of GDP at the final adoption of the 2023 budget. For this the caretaker government has also presented possible consolidation revenue and expenditure measures with estimated annual fiscal impact, the implementation of which requires political support. Bulgaria reserves the right to a subsequent update of the Convergence Programme to reflect the policies and priorities endorsed by a possible new government or by the majority of MPs in the National Assembly.

Maintaining the sustainability of the budgetary framework in the context of Bulgaria's commitments, both under the SGP and in relation to its status as a country under Title III of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union remains a fiscal policy priority in the medium term. Despite the estimates under the 2023–2026 budgetary framework for deviations from the previously outlined deficit targets, it is expected that with the adoption of Budget 2023 consolidation measures will be adopted to ensure that the budget balance in the medium term will be within the limits of national and European rules and constraints, which will be reflected in the 2023–2026 budget forecast.

The long-term sustainability of public finances remains a policy priority, including in terms of strengthening credibility and creating a predictable investment and business environment. Bulgaria maintains its medium-term budgetary objective of -1% of GDP for the structural balance on an annual basis.

Based on the projected debt financing and GDP forecasts, the general government debt is projected to increase in the coming years, both in nominal value and as a ratio of the consolidated

1 http://data.consilium.europa.eu/doc/document/ST-9344-2017-INIT/en/pdf

sector's debt-to-GDP, but to remain far below the maximum reference value of the Maastricht criterion of 60%.

In the context of maintaining macroeconomic stability and its participation in Exchange Rate Mechanism II, Bulgaria guarantees that it will maintain the currency board arrangement at the current level fixed exchange rate of BGN 1.95583 per 1 EUR until the country's accession to the euro area.

The current Convergence Programme covers the period 2023–2026 and consists of seven parts.

This first part contains the general framework of government economic policies and objectives.

The second part analyses the economic development of the country in terms of key macroeconomic indicators, and presents a forecast for their development in the medium term.

The third part is a description of the strategic objectives of fiscal policy in terms of budget balance and government debt. Here are the current state of the budget and the expected development during the reference period, with an emphasis on the structural balance. The main guidelines for the development of the debt position during the programming period are outlined. The main highlights of the policies and the specific measures for their implementation are also presented, as well as an assessment of the expected quantitative effect of their implementation.

In the fourth part, an analysis of the sensitivity of the forecast parameters is made, and an alternative scenario for economic development of the country in the medium term is developed. The effect of the implementation of the alternative scenarios on the budget parameters is also affected. The effects on government debt of changes in assumptions under the baseline macroeconomic scenario are also presented

Part five is dedicated to the sustainability of public finances. The main focus is on the long-term budgetary perspective in view of the effects of population aging.

The sixth part deals with the quality of public finances. Here are presented the strategy of government policy in this area, the composition of expenditures, as well as the structure and efficiency of revenue systems.

The seventh part reviews the institutional characteristics of public finances in Bulgaria – budget procedures and national fiscal rules. This part of the Programme also focuses on key legislative changes related to public finances.

The Convergence Programme takes into account measures and developments in the field of fiscal policy, reflecting the recommendation of the Council of July 2022, containing an opinion on the Convergence Programme for 2022 of Bulgaria:[2]

"In 2023, ensure that the growth of nationally financed primary current expenditure is in line with an overall neutral policy stance, taking into account continued temporary and targeted support to households and firms most vulnerable to energy price hikes and to people fleeing Ukraine. Stand ready to adjust current spending to the evolving situation. Expand public investment for the green and digital transitions, and for energy security taking into account the REPowerEU initiative, including by making use of the Recovery and Resilience Facility and other Union funds. For the period beyond 2023, pursue a fiscal policy aimed at achieving prudent medium-term fiscal positions."

[2] https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv%3AOJ.C_.2022.334.01.0011.01.ENG&toc=OJ%3AC%3A2022% 3A334%3ATOC

2. ECONOMIC PROSPECTS

2.1 Assumptions for the development of the world economy

This Convergence Programme is based on the macroeconomic forecast for the period 2023–2026, which was developed with the medium-term macroeconomic model of the Ministry of Finance (MF), based on assumptions for key external indicators, as of March 2023.

In 2022, global economic dynamics reflected the ongoing recovery from the crisis caused by the COVID-19 pandemic and new shocks from the Russian Federation's war in Ukraine and energy problems in Europe. The first half of the year reported strong economic growth both in the EU and globally, driven by some easing of supply chains, rising consumption and production. In the second half of 2022, the economic growth slowed down impacted by uncertainty due to the war, risks to energy stability in the EU, the shortage of basic raw materials that pushed up their prices and subsequently led to significant acceleration of inflation. In an effort to contain rising inflationary pressures, leading central banks started to implement a more restrictive monetary policy and have undertaken a series of increases in reference interest rates.

Table 2-1: Assumptions on key macroeconomic indicators

	Historical data	Forecast			
International environment	**2022**	**2023**	**2024**	**2025**	**2026**
World economy (real growth,%)	3.4	2.8	3.1	3.2	3.2
European economy – EU (real growth,%)	3.5	0.7	1.8	2.1	1.9
Annual average exchange rate USD / EUR	1.05	1.06	1.06	1.06	1.06
International commodity prices (in dollars, change in%)					
Crude oil, Brent	41.7	-17.7	-5.8	-5.3	-4.4
Non-energy commodities	8.7	-10.6	-2.1	-1.4	-0.6
Food	16.2	-6.9	-5.2	-3.1	-1.6
Beverages	7.3	5.1	-2.4	-0.5	-0.5
Agricultural raw materials	5.0	-35.0	1.4	-0.4	-0.4
Metals	-0.4	-5.0	-0.3	0.3	1.0
EURIBOR 3m.	0.3	3.3	3.3	2.8	2.3

Source: WB, Eurostat, ECB, IMF, Bloomberg, own calculations

Expectations for economic activity have improved in recent months, despite persistently high inflation. The presented macroeconomic forecast is based on the assumption that the international environment will remain unstable during the forecast period. The EU economy will remain relatively resilient to challenges in the energy sector. Potential disruptions in international trade and/or shortages of basic raw materials will not lead to a significant blocking of activity in economic sectors. In 2023, the still high inflation and increasing interest rates are expected to significantly reduce consumption and investment activity in the EU and other advanced economies, with GDP growth rates slowing to 0.7% in the EU and 2.8% globally. In 2024, economic activity will slightly accelerate, reflecting expectations for a stabilization of the environment. In 2025, slowing inflation will enable central banks to gradually ease monetary policy, will support increase in consumption and further acceleration of GDP. At the end of the forecast period, the growth rate in the EU will be slightly above the long-term average, and will be close to the long-term for the world.

2.2 Economic prospects and cyclical development

2.2.1 Economic growth

In 2022, Bulgaria's gross domestic product grew by 3.4% in real terms. Domestic demand had a positive contribution to growth (4.6 pps), while the contribution of net export was negative (-1.2 pps). The lower growth of the economy compared to that recorded in 2021 of 7.6% was due to a slowdown in the growth of all components.

Private consumption grew by 4.8%. Its growth was supported by the increase in real disposable income of households, employment and consumer credit. Nominal growth in disposable income offset the increase in inflation, however, the real growth of income was weaker than in 2021, contributing to a slowdown in the growth of household consumption. Government consumption reported growth of 6.5%. At the same time, investment in fixed capital fell by 4.3%, weak private investment activity contributing to this decline. The change in inventories offset the decline in gross fixed capital formation and contributed 1.3 pps. for GDP growth. Growth in exports of goods and services slowed to 8.3% and was outpaced by growth in import, which reached 10.5%.

On the supply side, gross value added rose by 3.4%. The growth was driven by industry without construction (14.4%) followed by services (1.1%) and more specifically *public administration and defence; compulsory social security; education; human health and social work activities*. The value added in construction decreased by 4.5%.

2.2.2 Cyclical development[3]

In 2022 the growth of the potential GDP reached 2.6%. This represents an acceleration compared to 2021 and is due to the increase in employment. In 2023, growth is expected to remain at 2.6%. For the period 2024-2025, the increase in investment will lead to an increase in the contribution of capital and an acceleration of the growth of potential GDP to 3%. In 2026, a slight slowdown in growth to 2.9% is expected, mainly due to a decrease in the positive contribution of labor as a factor for potential growth. Throughout the forecast period, total factor productivity will be with the highest contribution to growth.

The output gap in 2022 was positive reaching 0.9%. For 2023, as real GDP growth slows, the gap is expected to narrow to 0.2%. In the following years, until the end of the forecast period, the gap will increase and reach 0.9%.

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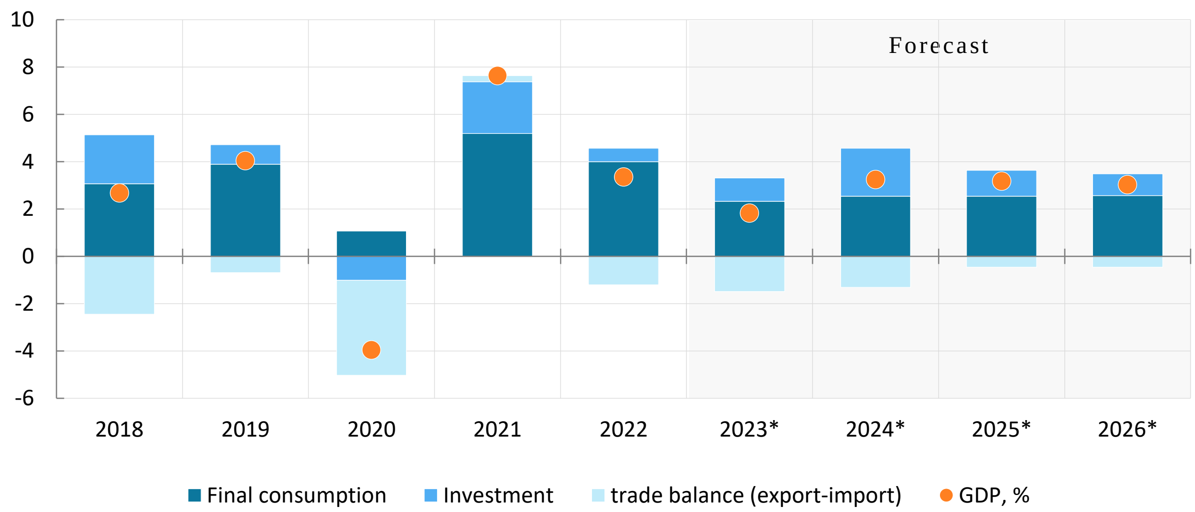
[3] The cyclical development of the economy is measured by output gap. It is calculated as the difference between actual and potential GDP in relation to potential. The potential GDP for the Bulgarian economy is calculated using a production function approach according to a methodology developed by the EC: Havik, K., & Kieran Mc Morrow, K., & Fabrice Orlandi, F., Christophe Planas, C., Rafal Raciborski, R., Werner Roeger, W., Alessandro Rossi, A., Anna Thum-Thysen, A. & Valerie Vandermeulen, V.,"The Production Function Methodology for Calculating Potential Growth Rates & Output Gaps," European Economy – Economic Papers 535, 2014.

2.3 Medium-term scenario

In 2023, GDP growth is expected to slow down to 1.8%, mainly attributable to consumption, export and change in inventories. Private consumption growth will be supported by growth in real disposable income, but will slow down as compared to 2022 in line with weaker growth in employment and consumer credit. Government consumption growth is also expected to be weaker than in 2022. At the same time, fixed capital investment will grow supported by public investment. Private investment will continue to be subdued due to high uncertainty and deteriorating financing conditions. The change in inventories had a positive contribution to GDP growth in the past two years, but its contribution is expected to be neutral in the forecast period. Export growth will slow down significantly due to weaker external demand. This will lead to a bigger negative contribution of net exports to the GDP growth.

Graph 2-1: Contributions by components to GDP growth (pps)



Source: NSI, MF

In 2024, GDP growth will accelerate to 3.3%. Easing inflationary pressures will stimulate the growth in household consumption. The increase in demand will also have a positive effect on private investment activity, and the growth of public investments will remain strong. Under the influence of the improving external environment, the growth in exports of goods and services will accelerate and the negative contribution of net exports to GDP growth will shrink compared to 2023.

In 2025–2026, GDP growth of 3.2% and 3% is expected, respectively. A slowdown in investment growth is expected due to public investment, while private investment will accelerate due to a reduction in uncertainty and an increase in demand. Private consumption will grow at a rate close to its long-term average. In line with the dynamics of the external environment, accelerated growth in exports of goods and services is forecast in 2025, followed by a slight slowdown in growth at the end of the period. The rate of import growth will remain higher, but the negative contribution of net export will shrink.

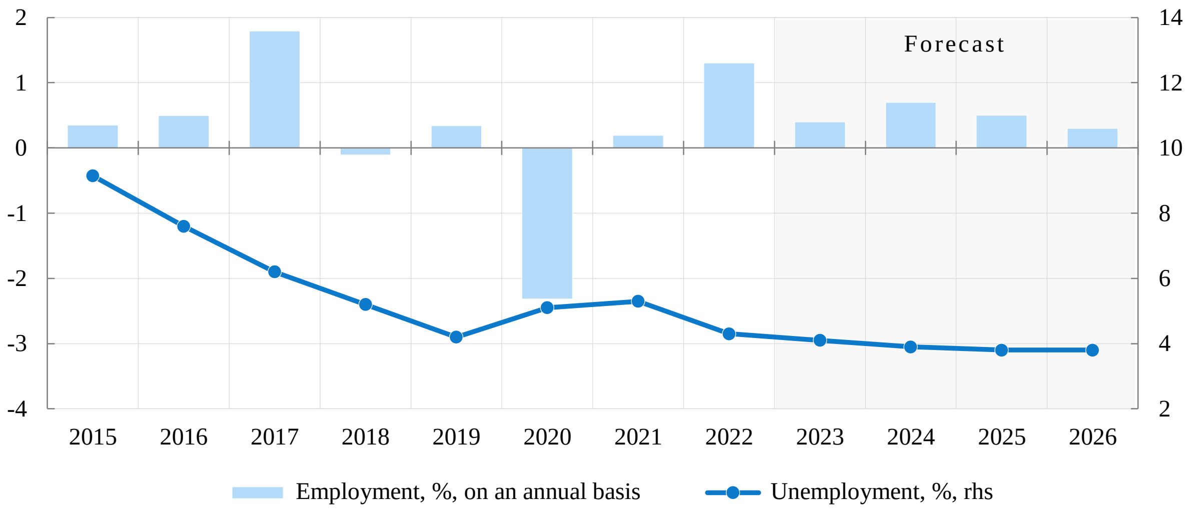
2.4 Sector balances

2.4.1 Labour market, income and productivity

In 2022, along with the lifting of all containment measures against the spread of COVID-19, there was a rapid recovery in employment in the Bulgarian economy. The labour demand increased in most economic sectors, and Bulgarian entrepreneurs have again begun to identify the insufficient supply of qualified labour as one of the main impediments for their business activity and development. The average annual number of employees in the Bulgarian economy reached 3502 thousand people in 2022 and increased by 1.3% compared to the previous year. This growth was due to the growth of employees in services and construction. All economic activities of services registered employment growth, some of which exceeded 5% ("Real estate operations", "Generation and dissemination of information and creative products; telecommunications"). In construction, employment grew by 1.2%, driven mostly by high demand for housing. The impact of the flow of Ukrainian refugees on the employment dynamics in Bulgaria was negligible. According to the monthly data of the Employment Agency, the number of Ukrainians working under an employment contract in the country was between 5,000 and 9,000 people in different months, most of them were employed in tourist activities (mostly related to summer sea tourism).

The activity rate of the population (15-64 age group) increased to 73.6% in 2022 and the employment rate was 70.4%. The unemployment rate decreased to 4.3%. The number of registered unemployed also had lower rates than in 2021 and at the end of June reached a historical low for the last 30 years.

Graph 2-2: Dynamics of employment and unemployment rate, %

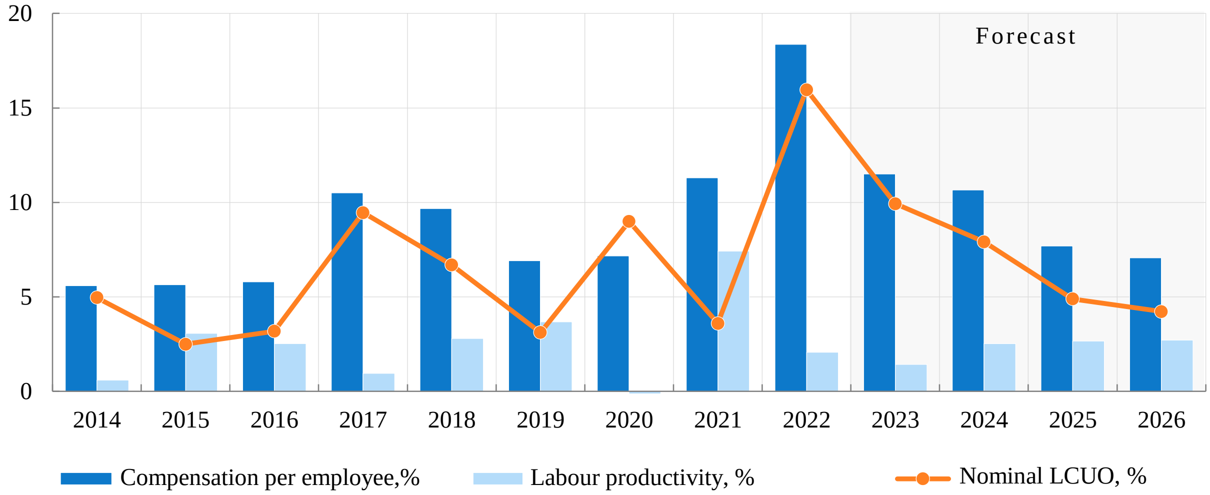


Source: NSI, MF

In terms of cumulative increase in consumer prices in the country and a high demand for labour, the compensation per employee rose nominally by 18.4% in 2022. The growth of the indicator in the industry excluding construction amounted to 31.8% and for manufacturing only – 24.7%. This rate more than doubled the value recorded in services (14. 8%) and exceeded about three times that in construction (9.9%). In the largest activity of services, “Trade, transport and hotels and restaurants”, the growth rate of the indicator reached 19.5%. The development during the year was determined by the private sector of the economy, in which the nominal increase in compensation per employee fully compensated the inflation in the country. In the general government, education and health sector, it was also characterized by a double-digit growth rate (10.8%), but overall the public sector reported lower growth compared to services and for the country as well, and the nominal increase in wages in it failed to compensate the overall annual average inflation. There was also a substantial increase in the bonuses and fringe benefits in addition to the salary[4], which suggests that employees were compensated for the high increase in prices by means of additional payments not fixed in the basic wage.

In 2022, real labour productivity growth slowed to 2.1%, but as with the dynamics of income, the industry sector without construction made a leading positive contribution (15%), and in manufacturing this rate reached 30.8%. In services[5], the indicator dynamics crossed into negative territory (-1.8%), due to the accelerated employment growth in the sector. Labour productivity in construction continued to decline for a second year in a row (-5.7%). The dynamics of income and labour productivity led to an accelerated increase in nominal unit labour costs for the economy to 16% as a whole, but in real terms, this rate was only 0.8%. In the manufacturing, which is most exposed to external competition, there was a significant decrease in the indicator considered both in nominal and real terms, by 4.6% and 17.3% respectively. This means that the wage dynamics in the sector has not put pressure on labour costs and are fully driven by increased production volumes and higher sales prices in it.

Graph 2-3: Dynamics of nominal ULCs and components, %



Source: NSI, MF

The expectation that Bulgaria will move along a constant trajectory of economic growth throughout the forecast period predetermines the forecast for the labour market dynamics in 2023–2026. After a rapid recovery in employment in 2022, annual employment growth is expected to slow down to 0.4% in 2023. The main argument for this development is the overall slowdown of Bulgarian economy. Ukrainian immigrants seeking asylum in the country are expected to have little impact on employment dynamics.

In the next year 2024, along with the acceleration of the growth in Bulgarian economy, the number of employed persons is expected to increase by 0.7%. During the year, the number of employees is also expected to exceed their level recorded in 2019, the last pre-COVID-19 year. In 2025 and 2026, the Bulgarian economy will continue to grow at a relatively high pace, but employment growth will slow down nonetheless. The labour demand will continue to be high, but the opportunities for extensive increase in labour supply will be increasingly limited (mainly due to the unfavorable demographic processes in the country). The employment rate of the population (15–64) is expected to reach around 75% towards the end of the projection period.

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4 According to data from short-term and annual statistics on employment and labor costs.

5 When calculating labour productivity in the services sector, the imputed rent of persons living in their own premises is not deducted.

In parallel with the increase in employment, unemployment in the country is expected to follow a steady downward trend. However, the rates of decrease are expected to be relatively low, as the opportunities for transition from unemployment to employment are increasingly limited without additional measures and programs to increase the probability of realization of the long-term unemployed, who are generally without qualification and even without a graduated level of education higher than the basic one. According to the forecast, the unemployment rate for 2023 will be 4.1% (0.2 percentage points lower than the previous year) and by the end of the forecast period it will have decreased to 3.8%. The relatively small decline in the unemployment rate over the period 2024-2026 means that the projected employment growth during this period will realize predominantly by attracting some of the people out-of-labour-forceback into the labour market or by attracting labour force from other countries.

The dynamics of compensation per employee is expected to slow down from 18.4% in 2022 to 11.5% in 2023 in nominal terms, following the containment of inflation, economic activity, employment, as well as the lower contribution of the public sector. Despite the expected slowdown, historically considered, this nominal rate remains high. In 2024, the nominal increase in compensation per employee is estimated at 10.6%. With the expected continued limitation of inflation, the dynamics of labour incomes will be determined primarily by the acceleration of the growth in real productivity, employees, as well as the increase in the minimum wage in the country. In the period 2025–2026, the nominal growth of compensation per employee will slow down more significantly to 7.7% and 7.1% respectively.

Within the forecast period, the average annual rate of real labour productivity growth is estimated at 2.3%. The recovery in labour productivity growth after 2023 combined with the expected slowdown in the wage dynamics will contribute to a gradual weakening of pressure on unit labour costs (ULC). At the end of the forecast period, nominal ULC growth will slow down to around 4%, while the real ULC growth is estimated to increase moderately at an annual average rate of 2%.

2.4.2 Inflation

The annual HICP inflation rate in the country accelerated until September 2022, when it reported its highest value of 15.6% yoy. The significant increase in international commodity prices, and especially those of energy, and their direct and indirect effects largely accounted for these dynamics. In addition to the supply-side factors, strong domestic demand also had a pro-inflationary impact. Since the last quarter of 2022, there has been a slowdown in inflationary processes in the country, with inflation at the end of the year decelerating to 14.3% and its annual average value being 13.0%.

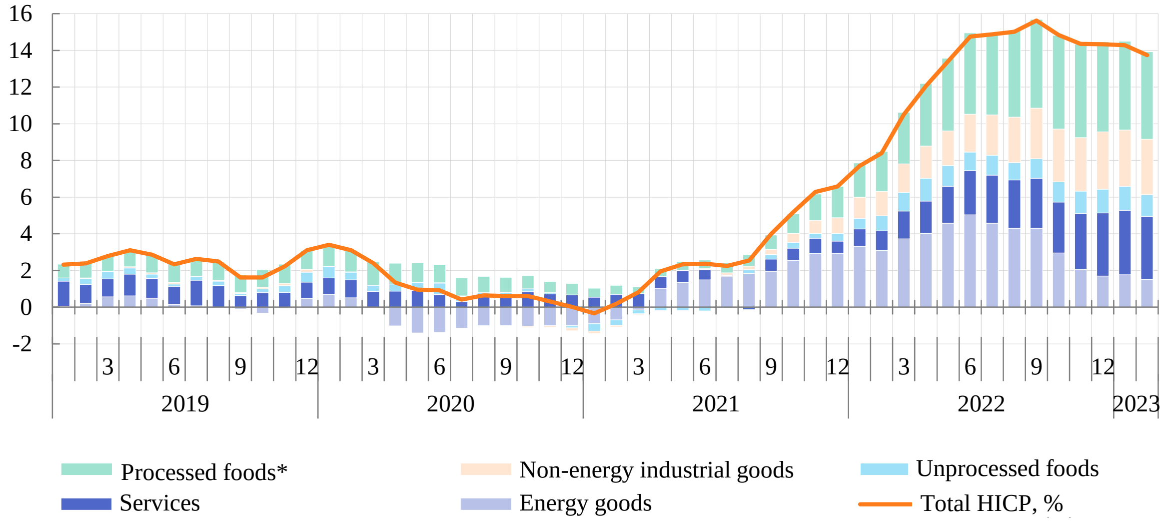
The rate of increase in consumer prices continued to slow down in the first two months of 2023 to 13.7% yoy in February. It was mainly due to the decrease in international prices of energy commodities and other raw materials, as well as the effect of the higher base in the previous year. Core inflation[6] edged marginally down to 10.9% yoy in February due particularly to lower inflation in transport services and consumer durables.

Inflation at the end of 2023 is expected to decrease to 5.6% and the annual average to be 8.7%. The slowdown will be largely due to a significant decrease in the contributions of food and energy components, with the prices of the latter expected to fall slightly at the end of the year. The assumed decrease in international prices of raw materials over the entire forecast period will keep the underlying inflation in check, namely the increase in prices of non-energy industrial goods and services. However, due to the projected increase in domestic demand as well as

6 The core inflation includes services and non-energy industrial commodities.

labour costs, the two consumer groups will form a significant contribution to the headline inflation in the country.

Graph 2-4: Annual inflation rate (%) and contributions by main components (pps)



* Processed foods incl. alcoholic beverages and tobacco

Source: Eurostat, own calculations

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Table 2-2: Forecast of HICP dynamics in the period 2023–2026

	2023	2024	2025	2026
Average annual inflation (in %)	8.7	3.8	2.8	2.2
End-of-period inflation (in %)	5.6	3.2	2.4	2.1

In 2024, inflation is expected to continue decelerating, reaching 3.2% at the end of the year and the average annual inflation to be 3.8%. Energy commodity prices will continue to decrease until the end of the forecast horizon. In 2025 and 2026, average annual inflation will continue to slow down to 2.8% and 2.2%, respectively.

[7] The core inflation includes services and non-energy industrial commodities.

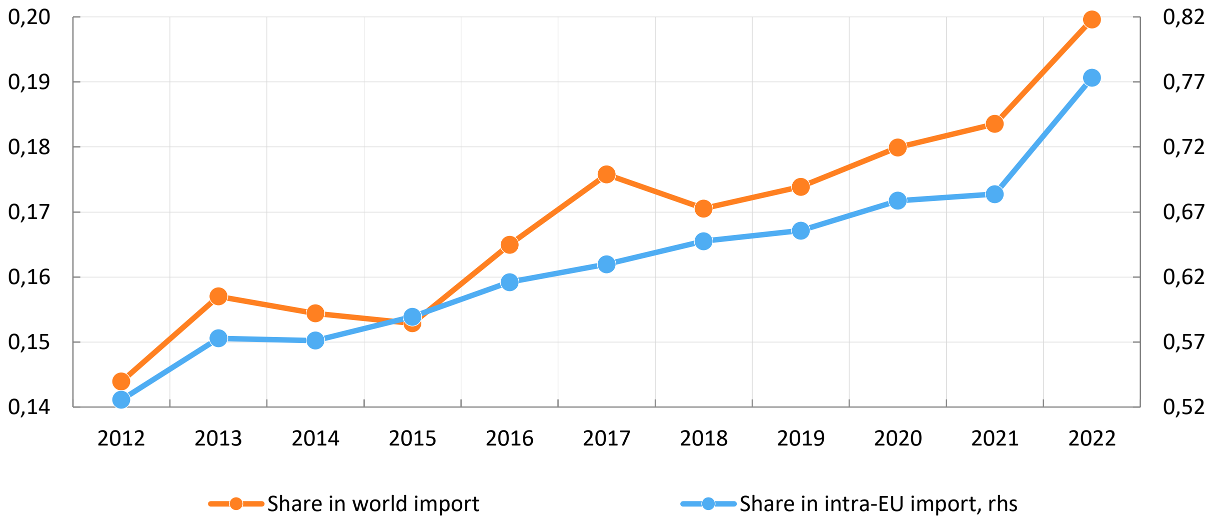
2.4.3 External sector[8]

In 2022 the current and capital account recorded a surplus of EUR 216 million (0.3% of GDP) against a negative balance in 2021.

The improvement reflected a favourable change in both the capital and all the current account sub-items except for the trade balance. In Bulgaria, export of goods increased by 33.5% and import – by 36.3%, which determined the increase in the trade deficit by 1.7 percentage points to 5.8% of GDP. Over the year, the trade balance was driven by the higher real growth of import than export. The real growth in import was driven by strong household consumption, while export growth was favoured by active trade in mineral fuels (oil and petroleum products and electricity), as well as metal raw materials and specialized production. The significant increase in the prices of mineral fuels and the increase in their share in the country's export also predetermined the formation of positive terms of trade (excess of the export deflator compared to that of the import).

The increase in commodity export was also reflected in an improvement in the market positions of the country. In 2022 the shares of Bulgaria’s export in both the world and within the EU import have increased significantly.

Graph 2-5: Bulgaria's share in international trade (%)



Source: MF calculations based on WTO and BNB data

Real effective exchange rate dynamics have shown a significant acceleration since mid-2021. Due to the significant increase in inflation globally over the period, REER calculated with the consumer price index (CPI), reported a smaller increase, which was mainly due to the appreciation of the nominal effective exchange rate. However, the REER deflated by the ULC exhibited a more significant contribution from the deflator. In 2022, the nominal growth in LCUO accelerated at a significant rate of 16% Taken overall to the economy, this reflected the substantial increase in compensation per employee. It should be noted, however, that in the manufacturing industry, which is most exposed to competition from the external environment, there was a decline in LCUO, both in nominal and real terms, which means that the increase in labour income did not have a negative effect on the cost competitiveness of the export-oriented activities.

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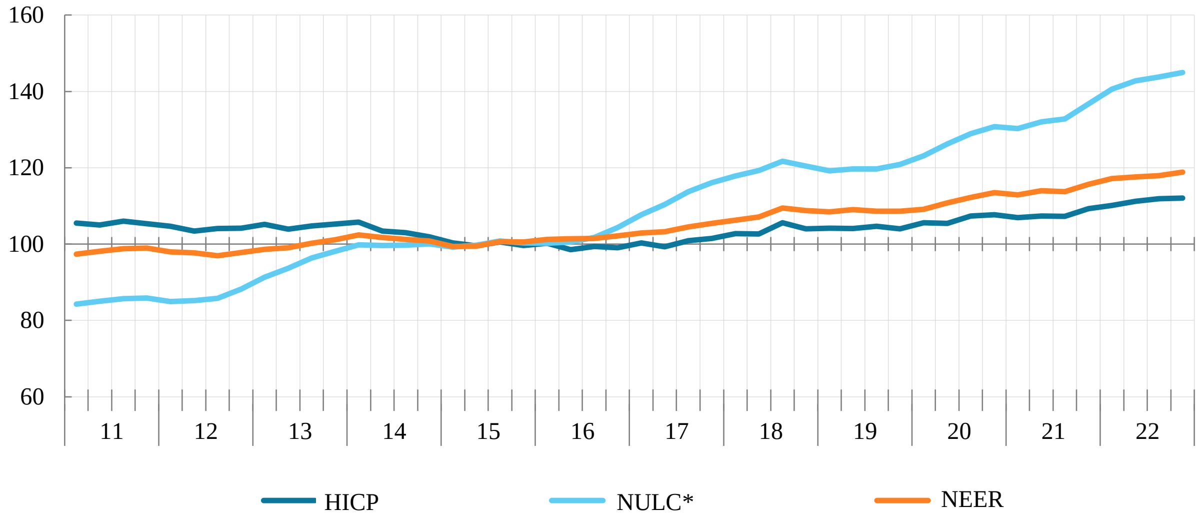
[8] The External Sector analysis is developed with Balance of Payments statistic data (analytical presentation), except graphs and data for which a different source is explicitly indicated.

Graph 2-6: REER of Bulgaria compared to 36 industrial countries, 2010 = 100



* Nominal labour costs per unit of output for the total economy

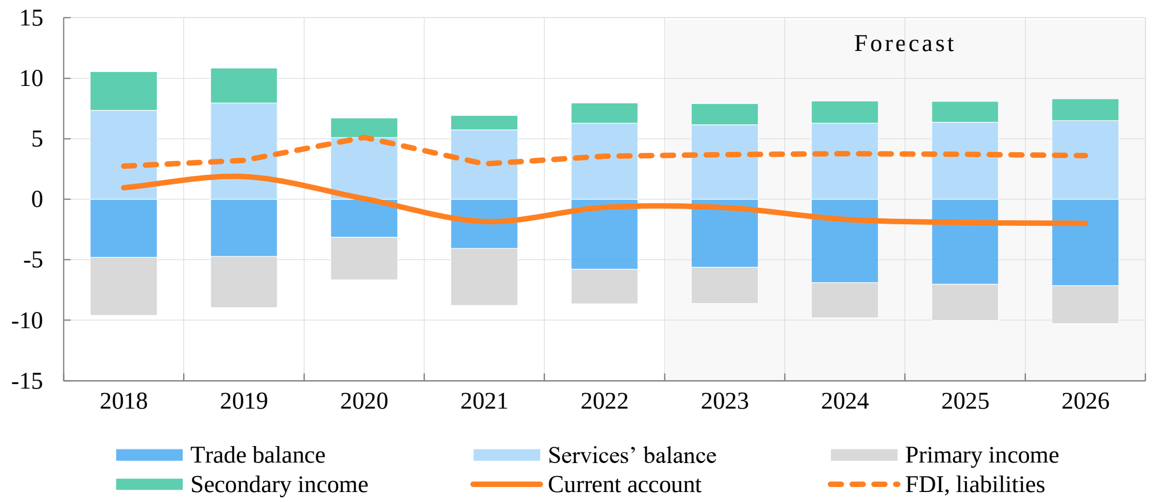
Source: EC

In 2022 the services surplus continued to grow, reaching 6.3% of GDP. A major contribution to the improvement of 0.6 percentage points were the revenues from trips of foreigners in the country, as well as services related to information technology and telecommunications. The balance of income items also improved, reflecting lower disbursed investment income to non-residents and the first inbound transfer under the Recovery and Resilience Plan. The current account deficit in 2022 decreased to 0. 7% of GDP, compared to 1.9% in 2021.

In the forecast period 2023–2026, the country's external position is expected to remain stable.

The current account balance will remain without significant changes in 2023. As regards trade in goods, the expected outpacing increase in real imports compared to exports will be offset by positive terms of trade. The trade deficit will increase in value terms, but there will be an improvement in the ratio to GDP due to the stronger nominal increase in the denominator. The expected slowdown in economic activity in our main partners and the downward dynamics in prices will also be reflected in lower growth of tourism and transport services receipts. The surplus on the Services will decrease slightly as a percentage of GDP and the total incomes balance will remain unchanged.

Graph 2-7: Current account (% of GDP)



Source: BNB, NSI, MF

In the remaining years of the forecast period, the negative current account balance will increase to around 2% of GDP. Stronger domestic demand will be the reason for outpacing nominal growth in import of goods compared to export, despite the favourable terms of trade. An increase in the trade deficit is expected, more substantially in 2024 and with minimal changes in 2025–2026. The surplus on Services will improve throughout the period, reflecting the full recovery of international travel after the COVID-19 crisis and the gradual improvement of the external environment.

In 2022, the flow of assets on the financial account[9] exceeded that of liabilities by EUR 689.2 million. Annual inflows of foreign direct investment (FDI) reached EUR 3 bn. or 3.6% of GDP. The predominant share of incoming FDI was in the form of reinvested profit from foreign parent companies.

Over the entire forecast period, FDI growth is expected, the pace will be close to overall economic activity and the FDI to GDP ratio will remain in the range of 3.6-3.8%.

2.4.4 Monetary and financial sector

The main goal of monetary policy in Bulgaria is to maintain price stability by ensuring the stability of the national currency. This goal is achieved in a currency board framework with a fixed exchange rate of the national currency to the euro.

At the end of December 2022, the market value of Bulgaria's international foreign exchange reserves – the assets on the balance sheet of the Issue Department[10] of the Bulgarian National Bank (BNB), amounted to EUR 38.4 billion (45.4% of GDP), increasing by EUR 3.8 billion on an annual basis. According to the principles of operation of the currency board, the dynamics of international foreign exchange reserves corresponded to the increase in the amount of the liabilities of the Issue Department. The increase in banknotes and coins in circulation, liabilities to banks and liabilities to the government and other budget organizations had the main contribution to the higher amount of the liabilities of the Issue Department at the end of 2022 compared to December 2021. At the end of December 2022, the foreign exchange reserves provided coverage of 8.0 months of imports of goods and non-factor services, while their ratio to the short-term external debt of the country amounted to 438.4%. At the end of February 2023, international foreign exchange reserves amounted to EUR 36.4 billion, posting an increase by EUR 5.4 billion compared to February 2022.

In 2022, the annual growth of deposits of the non-governmental sector followed upward dynamics, reaching 14.3% at the end of the year (9.1% in December 2021). The observed trend was driven by the deposits of non-financial corporations, which at the end of 2022 increased by 26.6% on an annual basis (8.5% at the end of 2021). The trade sector and the manufacturing industry had the main contribution to the growth of deposits of non-financial corporations at the end of the year. The increase in nominal turnover in the trade sector and in the nominal gross operating surplus in the manufacturing sector contributed to the strong growth of firms' deposits. An additional factor for the accelerated growth of deposits during the year was the weak investment activity, which was a prerequisite for storing the free resources of firms in the form of deposits. The slowdown trend in the growth of household deposits, observed at the end of 2021 and early 2022, was discontinued and their growth accelerated from the third quarter, reaching 8.3% at the end of the year. The discontinuation of the applied fee for maintaining

9 Analytical presentation of the balance of payments

10 The market value of international foreign exchange reserves includes changes in transactions, exchange rate differences and price revaluations.

cash holdings above a certain amount by large commercial banks from the third quarter of 2022 is a potential factor for the stronger growth rate of household deposits at the end of the year.

As of December 2022, broad monetary aggregate M3 grew annually by 13.2% (10.7% at the end of 2021), with overnight deposits having the largest contribution. Deposits with agreed maturity up to 2 years showed a gradual contraction in their negative contribution, more pronounced in the last quarter. As of February 2023, the annual growth rate of deposits of the non-government sector amounted to 14.3%, and that of broad money – to 13.1%.

The annual growth of credit to non-financial corporations and households remained high in 2022 against the background of strongly negative real interest rates, significant volume of attracted funds and high liquidity in the banking system. The growth of credit to non-financial corporations followed an accelerating trend in the first eight months of the year, fueled by strong demand for working capital funding and accumulation of inventory due to significant increase in commodity prices, supply chain disruptions and increased uncertainty in the economic environment. The reported decline in inventories in the economy, following the high levels reached in the first half of 2022, contributed to some deceleration of the growth of corporate loans toward the of end of the year, and it amounted at 10.4% in December (4.6% in December 2021). Higher growth of wages compared to that of inflation and negative real interest rates boosted consumer and housing loan demand, with housing loan growth remaining at high levels throughout the year and consumer loan growth decelerating slightly in late 2022. For the high growth of housing loans (17.8% as of December 2022 compared to 16.5% at the end of 2021) contributed the retained preferences of households for the purchase of real estate as an alternative form of savings or investment. In December 2022, consumer loans increased by 12.4% on an annual basis (12.2% at the end of 2021). As of February 2023, annual growth of credit to non-financial corporations slowed further to 8.7%, consumer credit growth remained at 12.3%, and housing credit growth accelerated to 18.1% year-on-year.

Under the conditions of the currency board in operation in the country, the increase in the main interest rates of the ECB in the second half of 2022 was quickly transferred to the interest rates on the interbank money market. At the same time, due to the continued significant inflow of attracted funds , high liquidity and competition in the banking sector, the transmission of ECB's monetary policy changes to interest rates on deposits and loans in Bulgaria was very limited. From the historically low levels reached, in the second half of 2022 interest rates on new[11] time deposits for households and non-financial enterprises began to rise slightly, reaching 0.94% and 1.05% respectively by December 2022 (from levels of 0.12% and -0.41% in June 2022). At the beginning of 2023, additional increase in the interest rate on newly contracted time deposits of non-financial corporations was reported in February to 1.29%, while the interest rate for households decreased to 0.69%. During the first eight months of 2022, a slight downward trend in interest rates on newly granted loans to non-financial corporations and households continued to be observed. In the September-December period, an increase in interest rates for corporate loans and consumer loans for households was observed, while the increase for housing loans was insignificant. As of February 2023 the interest rates on new corporate, consumer and housing loans amounted to 3.71%, 8.32% and 2.72% respectively (from levels of 2.30%, 8.22% and 2.51% in August 2022).

In 2022, an acceleration of the annual growth of credit and of total assets of the banking sector was recorded, while at the same time the reduction of non-performing loans and advances in the balance sheets of banks continued. The total amount of risk exposures increased, while the

[11] The terms "new" deposits and "new" loans refer to the statistical category "new business".

levels of the banking sector's capital ratios remained well above the minimum regulatory requirements and capital buffer requirements. The liquidity position of the banking sector remained stable.[12]

In 2022, the decrease in the amount of non-performing loans and advances and in their share in total loans and advances was driven both by the banks' operations on writing offs and sales of non-performing loans and the growth of the amount of loan portfolio. Gross non-performing loans and advances in the banking system decreased by 9.0%, amounting to BGN 4.4 billion at the end of the year. The gross amount of all non-performing exposures[13] was BGN 4.6 billion and its share – 3.1% of the total gross exposures (with an amount of BGN 4.9 billion and a share of 3.8% as of December 31, 2021). According to the "narrow scope" (applied since June 2020 with EU Regulation[14]), the amount of gross loans and advances in the banking system at the end of 2022 amounted to BGN 96.1 billion, and the ratio of non-performing loans calculated on this basis fell to 4.6% (5.9% at the end of 2021). According to the so-called "broad scope"[15] (including "cash balances with central banks and other demand deposits") the total amount of gross loans and advances at the end of 2022 amounted to BGN 125.3 billion, registering an increase of 16.2% on an annual basis. The calculated ratio of non-performing loans based on the "broad scope" decreased to 3.5% at the end of 2022 (4.5% at the end of December 2021). The net amount of non-performing loans and advances[16] at the end of December 2022 amounted to BGN 2.3 billion. This amount represents the potential residual credit risk in the balance sheet of the banking system, which remains fully covered by the excess of capital over capital requirements and applicable capital buffers. Compared to the end of 2021, the net amount of non-performing loans and advances according to the "narrow scope" decreased by 11.3%, and its ratio to net loans and advances at the end of December 2022 amounted to 2.4% (3.2% at the end of December 2021). According to the "broad scope", the ratio of net non-performing loans and advances at the end of 2022 decreased to 1.9% (2.4% at the end of 2021).

As a result of higher annual growth in the total amount of risk exposures compared to that of own capital, end-2022 capital adequacy ratios declined from the levels at end-2021, but remained significantly above regulatory requirements. As of December 31, 2022, Common Equity Tier 1 capital ratio, Tier 1 capital ratio and the total capital adequacy ratio amounted to 19.98%, 20.48% and 20.88% respectively (compared to 21.66%, 22.04% and 22.62% at the end of 2021). The profit of the banking system as of December 31, 2022 amounted to BGN 2.1 billion, with the main contribution for its increase with BGN 733 million compared to the reported profit for 2021 being the increase in net interest income. An additional contribution to the increase in profit had the higher amount of net income from fees and commissions and other

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12 The assessment of the state of the banking system is based on data from the supervisory reports on an individual basis as of the end of December 2021 and December 2022, received by 21 February 2023.

13 The exposures are determined on the basis of the broadest definition according to the methodology of the European Banking Authority (EBA), which includes both gross loans and advances, together with cash balances with central banks and other demand deposits, and debt securities other than "held for trading".

14 The changes are pursuant to Commission Implementing Regulation (EU) 2020/429 of 14 February 2020 amending Implementing Regulation (EU) № 680/2014 on the provision of information by the institutions to supervisors. According to the amendments, in contrast to the period June 2015 - March 2020, "cash balances with central banks and other demand deposits" should not be included in the scope of gross loans and advances, but should be reported separately.

15 The indicator used by EBA for the share of gross non-performing loans and advances is based on a broad definition covering all counterparties on loans and advances, including "central bank cash balances" and "other demand deposits".

16 The net value of non-performing loans and advances is calculated according to the EBA methodology, and their gross amount is reduced by the accumulated impairment. In calculating the share of net non-performing loans and advances, both their net value and that of total loans and advances are used.

net income, lower impairment costs, as well as the reversal of provisions. The higher reported profit contributed to the increase of the indicators for return on assets (ROA) and return on equity (ROE), with return on assets (ROA) amounting to 1.34% at the end of 2022 (0.99% as of 31 December 2021) and return on equity (ROE) increasing to 12.01% (8.11% as of December 31, 2021).

As of December 31, 2022, all banks complied with the capital requirements and the specified buffers[17]. The excess of capital over the regulatory minimum under Pillar 1 for the whole banking system amounted to BGN 9.6 billion, decreasing by 3.5% compared to the end of 2021. At the end of 2022, the capital exceeding the requirements under Pillar 1, Pillar 2 and the combined buffer requirement[18] decreased by BGN 1.9 billion to BGN 2.9 billion. The main factors for the reported decrease were the increased total amount of risk exposures during the period, as well as increased capital requirements and requirements for buffers.

As of 31.12.2022, the leverage[19] ratio aggregated for the banking system (with a fully implemented definition of Tier 1 capital) amounted to 9.41% (10.48% at the end of 2021) and shows a low level of indebtedness and a high capital coverage of total exposure (formed by banks' assets, off-balance sheet positions, derivatives, securities financing transactions and standard purchases and sales with forthcoming settlement). During the period, the total risk exposure of the banking system increased at a higher rate than that of Tier 1 capital. During the year, the leverage ratio reported by all banks in Bulgaria was above the minimum regulatory requirement of 3.0%.

In 2022, the liquidity of the banking system remained stable, with the liquidity coverage ratio (LCR[20]) of the banking system amounting to 235.0% at the end of the year (274.0% at the end of 2021). For all credit institutions the liquidity coverage ratio significantly exceeded the minimum regulatory requirement of 100%. At the end of December 2022, the aggregated level of the net stable funding[21] ratio (NSFR) for the banking system amounted to 162.4% (compared to 166.1% by December 2021), with all banks in Bulgaria complying with the minimum regulatory requirement of 100%.

The activity of banking supervision over credit institutions in 2022 continued to be focused on analysis and assessment of the financial condition of the banking system and of individual banks with the aim of identifying inherent and potential risks and taking timely supervisory measures. In February 2022, the BNB Governing Council, taking into account the stable state of the banking sector and the reduction of risks related to the COVID-19 pandemic, adopted a decision to discontinue the macroprudential measures imposed in March 2020 and confirmed in January 2021 related to the ban on banks' distribution of profit for 2019 and 2020 and the imposed limits on foreign exposures of the banks. The discontinuation of the ban on banks' profit distri-

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17 More information on the current levels of capital buffers can be found on the BNB website: http://www.bnb.bg/BankSupervision/BSCapitalBuffers/index.htm

18 The "Combined buffer requirement" is according to the definition in Art. 2, paragraph 3 of Regulation No. 8 of the BNB of April 27, 2021 on banks' capital buffers.

19 The regulatory requirement for leverage ratio (with a "fully implemented" definition of Tier 1 capital) was introduced in accordance with Regulation (EU) 2019/876 of the European Parliament and of the Council of 20 May 2019 amending Regulation (EU) №575/2013 and has been applied since 28 June 2021. The level of 3% is defined according to the value in the Basel III regulatory framework.

20 The liquidity coverage ratio for the banking system is calculated as the ratio between the liquidity buffer and the net cash outflows.

21 The regulatory requirement was introduced pursuant to Regulation (EU) 2019/876 of the European Parliament and of the Council dated 20 May 2019 amending Regulation (EU) № 575/2013 and has been applied since 28 June 2021.

bution is in compliance with the decision of the European Central Bank (ECB) and the European Systemic Risk Board (ESRB) not to extend the application of the ESRB's recommendation on the limits on profit distributions of the banks. The BNB, as the competent supervisory authority, requires so-called "less significant" banks which intend to pay a dividend or undertake buy-backs and other distributions, including from the profit for 2021, to submit distribution plans that are subject of supervisory dialogue. With the decision of the BNB Governing Council from February 2022, effective as of April 1, 2022, the measure to impose individual and aggregate limits on banks to foreign counterparties, aimed at limiting credit risk and the risk of concentration in their balance sheets, was suspended. The measure, imposed in March 2020 and extended in January 2021, contributed to the sustained improvement of the liquidity position of the banking system. The BNB took a decision to discontinue the measure, taking into account the achieved positive effect of its action on the stability of the banking system, while continuing to regularly analyze the relevant risks and remaining ready to implement an appropriate macroprudential measure, if necessary.

In accordance with the decisions of the BNB Governing Council taken in 2021 and announced 12 months before their entry into force, the countercyclical capital buffer rate was increased from 0.5% to 1.0% as of October 1, 2022 and to 1.5% from January 1, 2023. In March and June 2022, within the framework of the quarterly review of this buffer, the BNB Governing Council kept its level at 1.5% for the second and third quarters of 2023. Given the persistently high rates of credit growth and in view of the increased uncertainty in the economic environment, in September 2022 the BNB Governing Council decided to increase the countercyclical capital buffer rate to 2.0%, starting from October 1, 2023, and with a decision in December 2022, this level was also kept for the first quarter of 2024.

In 2022, the annual review of the identified as other systemically important institutions and the levels of capital buffer set for them was performed. Eight banks were identified in the review, with buffer levels set for them in 2023 between 0.50% and 1.00%.

The activity of the BNB in relation to the regulatory framework in 2022 was focused on the area of covered bonds. With the adoption of the Law on Covered Bonds, the requirements of Directive (EU) 2019/2162 of the European Parliament and of the Council dated 27 November 2019 on the issue of covered bonds and covered bond public supervision and for amending Directives 2009/65/EC and 2014/59/EU were implemented. In June 2022, the BNB Governing Council adopted Ordinance No. 42 on the terms and procedure for the issue of covered bonds, with the adoption of which the work on creating a comprehensive legal framework for the issuance of covered bonds by banks in the country in accordance with Directive (EU) 2019/2162 was completed.

According to the forecast of the Ministry of Finance, the growth rate of claims on the private sector will slow down until the end of 2023, both in corporate and household claims. This will be influenced by the slowdown in economic growth, the expected increase in the interest rates on loans as a result of the transmission of the ECB's monetary policy and, to a lesser extent, the entry into force of the higher levels of the countercyclical capital buffer set by the BNB. In total, claims on the non-government sector will grow by 9%. Claims on corporations will increase by 7.2% as their lower growth rate will be at the expense of a significant decrease in the growth of overdrafts and a slower increase in short-term loans. Claims on households will increase by 11.7%.

In 2024, the claims on non-government sector will accelerate to 9.3%, driven by higher growth of claims on corporations. It is envisaged that they will be positively influenced by the implementation of the National Recovery and Resilience Plan (NRRP), as well as by a positive growth of private investments. At the end of 2024, claims on corporations will grow by 7.9%.

from the growth of claims on households will slow down slightly to 11.2%, supported by higher growth in private consumption.

In the period 2025–2026, claims on households will continue to slow down and at the end of 2026 will grow by 8.9%. Claims on non-financial corporations will maintain a relatively stable growth rate until the end of the forecast period, which will then reach 7.7%. Total claims on the private sector will slow down smoothly until the end of the forecast period and at the end of 2026 their annual growth will reach 8.2%.

3. GOVERNMENT BALANCE AND DEBT

3.1 Policy strategy

Bulgaria will attempt to adhere to the prudent fiscal policy pursued in recent years, despite the increased economic uncertainty caused by the conflict in Ukraine and the inability to predict and assess the short-term and long-term its effects .

The preparation of budget 2023 and the updated medium-term budget outlook for the period 2023–2025 was affected by the late adoption of budget 2022 and its subsequent update, as well as by the political cycle involving two early parliamentary elections in late 2022 and early April 2023.

The implementation of Budget 2023 within the usual timeframe was hampered by the absence of a regular government to take an executive decision to submit the 2023 draft budget to Parliament with long-term assumptions for policy development included in compliance with the rules of the Public Finances Law (PFL), was the reason for the caretaker government to submit to the National Assembly the so-called "extending law" for 2022 with a term until the adoption of the 2023 Budget. Continuing political uncertainty has delayed the submission by the caretaker government to Parliament of the 2023 draft state budget law and the accompanying Updated Medium-Term Budget Outlook for the period 2023–2025, as well as the expected approval by the Council of Ministers of the Medium-Term Budget Outlook 2024-2026 as a follow-up to the previous documents.

The national budget documents (Budget 2023, the Updated Medium-term Budget Forecast for the period 2023–2025, as well as the Medium-term Budget Forecast for the period 2024-2026) and the current CP 2023–2026 were developed simultaneously and with the same parameters and assumptions.

It should be stressed that the draft state budget for 2023 and the Updated Medium-Term Budget Forecast for the period 2023–2025 reflect the fiscal effects on the parameters of the budgetary framework under a scenario based on the current legislation, the choice of this scenario being a consequence of the constraints of the current caretaker government to take long-term policy decisions beyond the horizon of its mandate. With the budget balance of the "General Government" sector for 2022 according to preliminary reporting data at -2.8% of GDP, the estimates under the 2023–2026 budgetary framework with the current legislation and reflecting the fiscal effects of enacted legislation that predetermines revenues and expenditures, show that the full-year effect for 2023 implies a significant deterioration of the general government budget balance, which reaches -6.1%, with the tendency of a slight improvement and stabilising between -4.7% and 5.0% of GDP for the period 2024-2026. This is the result of policy decisions and legislative changes adopted by the last National Assemblies related to changes in tax legislation concerning the introduction of tax exemptions and reduced tax rates with a negative impact on budget revenues, as well as an increase in expenditure of a permanent nature.

The caretaker government prepared and published for public consultation proposals for amendments in tax laws with measures to increase collection, improved fiscal control and changes in corporate taxation, which would have a consolidation effect and ensure that the deficit is brought within the limits of the SGP. The proposals, however, did not find political support and accordingly were not reflected in the estimates for the budgetary framework.

At the same time, possible revenue and expenditure measures with an estimated annual fiscal impact have been proposed, which could be considered by the National Assembly and, if given the necessary political support, could help to bring the deficit within the 3% limit. Overall, the political sentiment is for a budget for 2023 within the Maastricht criteria and the national fiscal rules. During the period 2023–2026, the long-term implementation of the debt criterion is maintained as a priority, resp. maintaining the level of the debt to GDP ratio below the limit of 60%. Among the individual components forming the "General Government" debt sector, the most significant contribution is made by the "Central Government" sub-sector debt and, in particular, the government debt as its main component. Sub-sector "Local Government" and sub-sector "Social Security Funds" retain their minimal influence on the sector debt, which predetermines the leading importance of the implemented debt policy.

The government debt management policy for the period under review follows the outlined objectives of the fiscal policy and will be aimed at fulfilling the strategic goal of providing the necessary resources for refinancing the outstanding debt, financing the planned levels of the state budget deficit and ensuring the liquidity position of the fiscal reserve.

In the state of global economic uncertainty, a complicated geopolitical situation, and in the process of tightening the monetary policy by the major central banks, the main challenges and goals for debt management will be focused in the direction of providing opportunities for market-oriented financing, both in the local and international capital markets. The volatility and fragmentation of the financial markets, as well as the continuing cycle of rising main interest rates, are among the determining factors for the rise in the price of debt financing and the risks accompanying its provision.

In order to implement the set goals, in the period 2023–2026 it is planned to use the issues of government securities both on the local and external debt market as the main instrument of debt financing. The determination of the specific characteristics of new debt will be in accordance with the prevailing market conditions, the investor base, the profile of the outstanding debt , the possibilities to reduce the refinancing risk and minimize liquidity risks to the state budget.

In addition, a legal possibility is foreseen to supplement the market-oriented financing of the state budget with new external government debt through loans under financial instruments from the EU and/or from international financial institutions. Regarding to the financing of new investment projects and specific programs with government and government-guaranteed loans, the adopted conservative approach will continue to be applied.

3.2 Medium-term objectives

In 2023, the budget balance is expected to be negative at 6.1% of GDP, and the forecast for the following years is for a deficit of the sector of 4.7% of GDP in 2024, 4.9% for 2025 and 5.0% of GDP for 2026. The presented forecast was developed on the basis of the latest macroeconomic forecast of the Ministry of Finance, as well as the measures and policies undertaken that have a fiscal impact during the forecast period.

Part of the “General government” deficit, which is reported on an accrual basis, is due to a time shift in the accounting of the expenditures for supplies of military equipment paid in previous years on a cash basis. According to the European System of Accounts 2010 (ESA 2010) methodology the government expenditure on military equipment is accounted for during the year of delivery. Therefore, the investment costs for the acquisition of a new type of combat aircraft, made in 2019 and 2020 in the amount of BGN 2,197.7 million, have an impact on the cost estimates for 2024-2026, which, together with the shifted reporting of other expenditures on military equipment, increase the deficit by 0.13% of GDP in 2024, 0.73% of GDP in 2025 and 0.17% of GDP in 2026, respectively, with the largest delivery of military equipment expected to take place in 2025. This impact is temporary and does not lead to permanent (structural) deterioration of the budgetary position and to the violation of fiscal sustainability in the long run.

The main contributor to the reduction of the budget deficit in the medium term are expenditures, which are expected to decrease by 2.3 percentage points in 2026 compared to their level in 2023 (reaching 39.4% of GDP). In terms of revenue, the ratio of total revenues to GDP will fall to 34.3% of GDP in 2026, compared to 35.5% at the beginning of the period, due to the outpacing GDP growth.

In the period 2023–2026, a nominal increase in all revenues is expected, which is due to an increase in revenues in the main elements. The largest increase is in tax and insurance revenues from direct taxes and social security contributions, which is a result of the increase in household incomes, the possibility to choose insurance and the increase in insurance length of service and retirement age. In the case of non-tax revenues, a more significant increase is observed in the capital transfers received in 2024, due to the increase in the revenues from the EU under the Recovery and Resilience Plan.

The largest contribution to the total expenditures growth of the General Government sector have interest expenditure and social transfers other than those in kind, which cover pension expenditures, as well as social security benefits and allowances and capital expenditures. Capital expenditures for gross fixed capital formation increase significantly as a share of GDP from 3.0% in 2022 to 4.0% in 2023, 4.6% in 2024 4.7% for 2025, and decreasing to 3.5% for 2026. The change in the indicator is due to the supply of military equipment and the accelerated pace of absorption of European funds and the Recovery and Resilience Plan.

Significant for the increase in social transfers are the increase in social benefits under the Law for Social Assistance and the Law on People with Disabilities, the planned change in the poverty line, the increase in the minimum wage when determining the hourly work rate to calculate the remuneration of personal assistants under the Law on Personal Assistance and foster family allowances under the Law on Child Protection, as well as the annual pension update from 1 July each year under the Swiss rule of the Social Security Code (SSC).

3.3 Actual balances and updated budgetary plans for the current year

3.3.1 Update of the 2022 budget framework

The economy of Bulgaria has fared relatively well during the years of the COVID-19 pandemic. After reporting a 4% drop in 2020, GDP rebounded strongly by 7.6% in 2021. In parallel, there was an increase in inflation in the second half of 2021, driven mainly by high electricity prices, prices of some energy sources, as well as rising food prices. Despite the unprecedented shocks caused by the outbreak of war in Ukraine, economic expansion continued in 2022 with GDP growth of 3.4%, amid high inflation and political uncertainty.

The focus of budgetary policies in 2022 quickly shifted from measures to combat the COVID-19 pandemic to measures to minimize the negative effects of the outbreak of the military conflict in Ukraine on the economy and vulnerable groups. Already in the middle of the year, the main part of the measures to combat the pandemic was dropped, and in the second half of the year expenditure measures only affecting the medical aspects of the pandemic (purchase of medicines, supplies, vaccines, etc.) continued to be financed. However, the sudden shock of the outbreak of war in Ukraine led to a sharp deterioration in the economic perspectives and created unprecedented risks, including in terms of the supply of fuels, energy commodities and raw materials in the region. Along with this, the humanitarian aspect of the crisis required immediate actions to control the refugee crisis and provide humanitarian aid to Ukraine, housing the refugees who wish to remain in the country and their support during their stay in Bulgaria.

Several main events influenced the development of budgetary parameters during the year. First, due to the political situation that has arisen – parliamentary elections in November 2021 and the formation of a regular government in the middle of December 2021 – the first two months of 2022 passed without an adopted regular annual Law on the State Budget and the action of the so-called "Extending Law" that regulates the implementation of some of the provisions of the Law on the State Budget for 2021, Law on the National Health Insurance Fund (NHIF) Budget for 2021 and Law on the State Social Security Budget for 2021 until the adoption of Law on the State Budget of the Republic of Bulgaria for 2022 by the National Assembly. In parallel, the procedure for adopting the regular Law on the State Budget for 2022 went on. This had a restraining effect on spending as overall consolidated fiscal program (CFP) spending for the first quarter of 2022 remaining nominally close to that reported for the same period of the previous year (nominal growth of only 0.9 percent). The Law on the State Budget of the Republic of Bulgaria for 2022 was adopted by the National Assembly at the end of February 2022 and published at the beginning of March.

Next, Russia's invasion of Ukraine in late February 2022 and the deepening of the military conflict in the following months should be noted. The presence of military actions in the vicinity of Bulgaria and the related sanctions imposed by the EU on Russia have led to significant negative consequences for the Bulgarian economy, including the unilateral termination of natural gas supplies from Russia to Bulgaria after April 2022. The shocks on the international markets of natural gas and energy commodities led to an unprecedented rise in prices – at the end of August, the price of natural gas on the Dutch TTF exchange exceeded 330 EUR/MWh, which accordingly led to a chain increase in the price of electricity and other energy commodities in a large part of Europe. Along with this, Bulgaria faced a situation where in extremely short deadlines it had to secure new sources and routes for the supply of natural gas, due to the unilateral termination of supplies by Gazprom. The increase in prices on regional electricity exchanges deepened, partly due to problems with natural gas supplies.

This, in turn, boosted the trend of rising of electricity prices on the free market in Bulgaria, which began in 2021, forcing the adoption of measures to mitigate the negative impact of expensive energy on economic entities in the country. The government had to extend and expand the programs for compensating non-domestic consumers of electricity and natural gas, which were in effect since the last quarter of 2021. The extension of the programs until July 2022 was within the spending limits of the annual budget law, and compensatory payments were made through expenditures from the "Electricity System Security Fund" (ESSF) budget, including at the expense of additional revenues.

In the beginning of June, the government prepared and submitted to the National Assembly a draft of the Law on Amendments and Supplements to the Law on the State Budget of the Republic of Bulgaria for 2022 (Law on Amendments and Supplements of the State Budget of the Republic of Bulgaria for 2022). An urgent package of anti-crisis measures aimed at overcoming the negative consequences of the growing inflationary pressure on the most affected groups of society and business was proposed. The goal was to support Bulgarian citizens and businesses in the conditions of an unprecedented crisis caused by the war in Ukraine and to mitigate the shocks caused by the high prices of energy commodities and raw materials for the vulnerable groups of society and for the economy of Bulgaria. The bill was finally approved by the National Assembly in the end of June and published in the beginning of July (State Gazette, no. No. 52 dated 07/05/2022), as the fiscal target for the year on a cash basis was kept at the level from the beginning of the year – a deficit of 4.1 percent of the estimated GDP.

The adopted anti-crisis measures in the field of tax policy have included the introduction from July 2022 of a reduced Value added tax (VAT) rate of 9% for central heating and natural gas, a zero rate for the supply of bread and flour, as well as exemption from excise duty on natural gas and liquefied petroleum gas (LPG) used as motor fuel and on electricity. According to preliminary estimates, the effect of the action of the mentioned measures for 2022 was estimated at about BGN 222.5 million less tax revenue. During the discussion of the budget update, another major problem facing businesses was also addressed – the high prices of electricity for consumers outside the regulated market for the period July-December 2022. During the procedure for voting on the draft law in the National Assembly a number of changes were made, which introduced a specific mechanism for the payment of compensations to non-domestic consumers of electricity at the expense of targeted contributions from public corporations from the energy sector with 100 percent state participation in the capital. The amount and the due date for making the targeted contributions was determined by the Council of Ministers on a monthly basis, with the funds coming from the FSES budget and serving to pay compensations to non-domestic consumers of electricity. The compensations paid by ESSF were in the amount of 100 percent of the difference between the average price of the "day-ahead" segment of the "Bulgarian Independent Energy Exchange" EAD for the relevant month and the base price of BGN 250/MWh. The mechanism was intended to apply for the period 01.07.2022 – 31.12.2022.

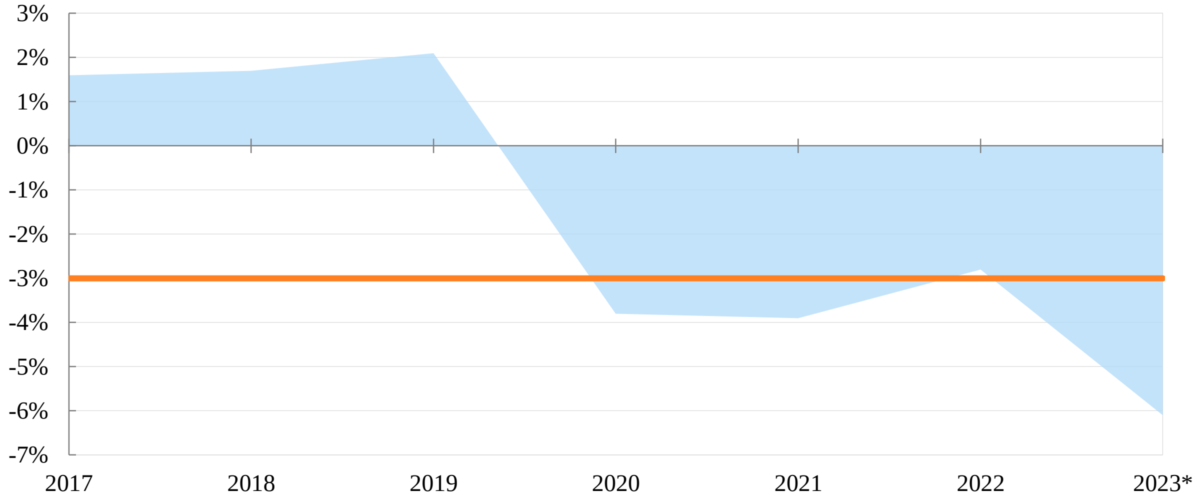
Regarding social expenses, in the second half of the year, all pensions were increased by 10% as of July 1, 2022, and the paid supplement in the amount of BGN 60 was added to the amount of pensions. As of October 1, 2022, a new recalculation of pensions was made depending on the year of their granting. These two increases, along with the increase on 12/25/2021, have resulted in a significant increase in the total amount of pension costs. During the year, in order to compensate for inflation, the salaries of some of the administrations in the budgetary sphere were also increased.

In June 2022, after a vote of no confidence in the National Assembly, the government resigned. The impossibility of forming a new elected government and the subsequent early parliamentary elections, as well as the complicated political situation after them, led to the failure to adopt a Law on the State Budget for 2023 within the time limits set by the law and to extending the validity of the Law on the State Budget for 2022 at the beginning of 2023.

3.3.2 Budget developments in 2022

A series of events had a mixed impact on the budgetary position in 2022. On one hand, the economic recovery that began in 2021 continued in 2022. This was reflected in a strong performance of industrial production, growth in consumption and exports, and the preservation of employment, which together with inflation favored budget revenues. On the other hand, a number of factors had a negative impact on the expenditure side of the budget. It was the extraordinary epidemic situation that lasted in the first quarter of 2022 and the related costs of combating COVID-19, as well as the shocks on the fuel and energy markets, that necessitated the immediate intervention of the state with measures to reduce the negative consequences on business and vulnerable groups of the population. Funds were also allocated to deal with the consequences of the military conflict in Ukraine. Social spending and compensation of employees rose significantly due to high price growth and double-digit inflation for most of the year. Despite the large fiscal effect of these adverse impacts, Bulgaria managed to maintain the level of the General Government sector's deficit for 2022 at the level of 2.8%, which corresponds to the requirement of the SGP, where the reference value is a deficit of 3%. At the same time, compared to the target set in the previous CP – a deficit of 5.3%, the data from the April Notification Tables for Deficit and Debt of Bulgaria reported an improvement in the budget balance in General Government sector by 2.5 percentage points which is due to an increase in the revenue part by 0.5 percentage points, while at the expenditure part a contraction of expenses by 2.0 percentage points was reported.

Graph 3-1: Budget balance (ESA 2010, % of GDP)



* Prognoses

Source Eurostat, MF

Revenues as a relative share in GDP reached 38.5% in 2022, which is an increase of 0.8 percentage points compared to the level in 2021. The growth of relative share of revenues in GDP is mostly due to the growth of taxes on production and imports (including one-off revenues from electricity producers used to pay compensation to non-residential electricity consumers) and the increase in sales revenue, property income and other current revenues, while in current taxes on income, wealth, etc. was observed remaining at the level compared to the previous year.

Taxes on production and imports recorded the largest growth both in nominal terms – by over BGN 5.5 billion and as a percentage of GDP – by 1 percentage point. Targeted contributions made in implementation of the provisions of the Law on the State Budget of the Republic of Bulgaria for 2022 by public corporations from the energy sector with 100 percent state participation in the capital, which financed the compensations for the high prices of electricity for non-domestic customers, are reflected here. An increase in revenues is observed for all taxes in the group, the most significant being VAT. This reflects both real consumption growth in 2022 and the acceleration of inflation. The significant growth in consumption is largely the result of the continued recovery in consumption after the initial shock of the COVID-19 pandemic and the imposed restrictions. The registered increase in the income of retirees and a large number of employees also contributes to the increased consumption and related tax revenues.

For current taxes on income, wealth, etc. there is an increase in revenues in nominal terms by BGN 1.7 billion, and as a share of GDP compared to the previous year the level remained at 6.4% of GDP. A nominal increase is reported for all taxes in the group, with the largest being for corporate taxes. The reasons are, on one hand, the increased volume of production in industry, and on the other, the increase in prices in many industries, such as energy, production of raw materials, foodstuffs, etc. This leads to increased profits, correspondingly to a higher profit tax. There is also a nominal increase in personal income tax, which is a result of the recorded growth in remuneration both in the private and public sectors. At the same time, the more substantial increase in tax receipts from this source of revenue is limited by the increased in 2022 volume of tax credit for children. It should also be noted that there is an increase in taxes on wealth (property taxes), which reflects the increased prices of properties in the country and the number of transactions for their acquisition, etc.

Revenues from social and health insurance contributions increased nominally by BGN 1.6 billion, while in terms of GDP they reported a decrease of 0.5 pps. compared to 2021. The main factor contributing to this is the increase of income, incl. of the minimum wage and the minimum insurance thresholds, etc.

Revenues from sales, property income and other current revenues increased nominally by BGN 2.5 billion and by 0.3 pps. as a share of GDP compared to 2021. The main reason here is the increased funds from the sale of greenhouse gas emissions quotas, dividends from state-owned enterprises and other revenues.

In 2022, the total expenditures of the "General Government" sector increased nominally by BGN 10.5 billion and amount to 41.3% of GDP, which is by 0.3 pps. lower than the level reported in 2021. Nominal increase is observed in almost all types of expenditure except for other current expenditure, the most significant being the increase in expenditure on subsidies and in social expenditure other than those in kind.

Expenses for employee compensation increased nominally by BGN 1.1 billion, although their level relative to GDP decreased by 1.1 pps. compared to 2021. The main reason for the nominal increase is the increase in remuneration in the public sector, incl. those of the teaching staff, with the aim to compensate to a certain extent the accumulated inflation. The payment by mid-2022 of additional amounts to the remuneration of doctors and medical specialists on the front line in the fight against the COVID-19 pandemic, etc., also has an impact.

The costs for intermediate consumption, the main part of which is maintenance, are growing nominally – by BGN 1.6 billion, and as a relative share in GDP – by 0.2 percentage points, the main reason being the increased prices of materials, fuels, energy, the prices of the services and the costs of current repairs.

The amount of social transfers as a relative share of GDP increased by 0.3 percentage points, and in nominal terms this is BGN 4.3 billion. In the case of social transfers in kind, where payments to medical care providers are reflected, the nominal increase is almost BGN 1.2 billion, and the share of spent funds in GDP increases by 0.3 percentage points compared to 2021. This reflects the continued payment until mid-2022 of additional amounts to medical professionals' remuneration and other costs to combat COVID-19. The other category of social transfers, other than those in kind, reflect the social payments made for pensions, support and benefits to households, where the nominal increase is BGN 3.8 billion compared to 2021, and their share in GDP increases by 0.5 pps. In 2022, pensions were increased in several steps: as of 25.12.2021, which practically affects the annual increase for 2022, the percentage for each year of insurance service increased by 12.5 percent in the pension formula, increased in the minimum and maximum pension; as of July 1, 2022, all pensions were increased by 10%, including as a permanent addition the "COVID" supplement paid until then, and the minimum and maximum pensions increased by 26.2 and 33.3%, respectively; as of October 1, 2022 there was a new increase in pensions granted until the end of 2021, the percentage of increase depending on the year the pension was granted. Also, during the months of January-June 2022, all pensioners also received a "COVID" supplement of BGN 60 and those vaccinated against COVID-19 also received one-time amount to the pension of BGN 75. The expenditures for social transfers and benefits for households; register an increase in benefits for temporary incapacity due to general illness; benefits for raising a small child; social assistance benefits, incl. of heating benefits, family benefits for children, etc.

Expenditures for subsidies marked the largest increase compared to 2021, both nominally – by BGN 3.1 billion, and as a share of GDP – by 1.3 pps. A major contribution have the subsidies to offset the costs of non-domestic end-users of electricity and to operators of the electricity transmission network for the purchase of amounts of electricity needed for technological costs, as well as subsidies under other programs to compensate for high energy and natural gas prices.

At the same time, payments to employers under the job preservation program (mainly the 60/40 program) during the epidemic situation caused by the COVID-19 pandemic were suspended in the second half of the year.

Capital expenditure as a share of GDP in 2022 increased both in the gross formation of fixed capital – by 0.4 pps, and in the other elements of capital expenditure – by 0.1 pps. The nominal increase is BGN 1.4 million and BGN 0.3 billion, respectively. The increase in gross fixed capital formation is mainly driven by expenditure incurred on infrastructure projects, mainly in the transport sector, both from the state budget and from EU-funded operational programmes. At the same time, the complicated political situation in the country and the change of governments slowed down the process of starting new projects, and accordingly, the larger capital expenditures foreseen in the previous CP were postponed to the following years. The delayed approval of the Recovery and Resilience Plan, as well as the necessary procedures for the initiation of projects under it, also limited the execution of capital expenditures. A delay is also reported for the projects under the operational programs of the new EU programming period 2021-2027.

In 2022, interest expenses keep their share of GDP unchanged compared to 2021 – 0.5%, and nominally increase by BGN 0.1 billion.

3.3.3 Measures to combat the COVID-19 pandemic in 2021, war in Ukraine and energy crisis

– COVID-19

The National Statistical Institute data for 2022 indicate that in the period in which the emergency epidemic situation was in effect – until March 31, 2022, and in the following months, the measures regarding revenues and expenses incurred from the national budget for the implementation of measures and fiscal incentives for controlling the COVID-19 pandemic and its consequences are in the amount of about BGN 3.3 billion, which represents 2% of GDP.

Revenue Measures

The measures adopted in previous years, related to the application of a reduced VAT rate on certain goods and services from 20% to 9%, and the increased amount of tax relief for children (Article 22c and Article 22d of the VAT Act) continued to be applied in 2022. By the end of the year, the measures related to changes in VAT continued to be applied for zero-rate taxation of supplies of vaccines against COVID-19 and services directly related to these vaccines, as well as medical devices for in vitro diagnostics of COVID-19 and the services directly related to these products, with a place of performance on the territory of the country. This tax treatment also applies to intra-Community acquisitions with a place of performance in the territory of the country of these goods. The exemption from customs duty and VAT on the import of medical goods and the reduced VAT rate on the supply of beer and wine, as part of restaurant and catering services, applied until 30.06.2022.

According to preliminary data of the revenue agencies, the effect of the mentioned measures for the whole of 2022 is estimated at nearly BGN 0.7 billion less tax revenue (0.4% of GDP).

Expenditure measures

According to preliminary data, the total amount of expenditures amounted to BGN 2.6 billion (1.6% of GDP). The main categories of expenditure measures almost all of which continue their effect from previous years and whose main objective remains limiting the negative socio-economic consequences of the pandemic, combating the spread of COVID-19 and treatment of COVID-19 patients in 2022 are as follows:

Measures to help households and vulnerable groups, most significant of which are:

- with the largest share also in 2022 continue to be the additional amounts paid to the pensions of all pensioners for the period January-June 2022. The total amount of funds under this measure is BGN 743.9 million;
- pensioners with a completed vaccination course by 31.12.2021 or a booster dose against COVID-19 in the period January 1 – June 30, 2022 received an additional amount to the pension in the amount of BGN 75. The total amount of funds under this measure is BGN 57.0 million;
- to compensate the income from pensions to the level of December 2021 after the changes made in the amount of pensions at the end of 2021 for the period until the end of June 2022, an amount of BGN 101.9 million was spent;
- funds in the amount of BGN 265.9 million were used to provide vaccines, medicinal products and rapid antigen tests in the fight against the COVID-19 pandemic;
- BGN 14.7 million were allocated to support families with children up to 14 years old, whose parents cannot work remotely from home and are not able to use paid leave.
- BGN 6.2 million were paid under the measure "Implementation of employment programmes and training measures to support the unemployed and employers".

Business support measures – of the most important are:

- The largest share belongs to the expenses incurred under the measure "60/40" in aid of employers to maintain the employment of their employees in the amount of BGN 823 million.
- additional expenses under the budget of the state fund "Agriculture" to support farmers affected by the negative effects of the pandemic – BGN 143.5 million;
- to support businesses in the field of tourism, including supporting the tourism sector with grants, assistance to tour operators for refunds to their clients for unrealized trips due to COVID-19 and one-time assistance for tour guides – the funds spent are in the amount of BGN 66.0 million;
- grants for air carriers with an operating license of the Community with a permit for the carriage of passengers, issued by DG "Civil Aviation Administration" pursuant to Art. 109 of the 2021 Law on State Budget– BGN 57.3 million;
- Aid for bus carriers that have a license for passenger transport – BGN 35.2 million;
- financial support in the field of culture and arts in the conditions of a declared emergency epidemic situation – BGN 35.8 million;
- subsidies for tour operators that use air carriers with a valid operating license for charter flights to the Republic of Bulgaria for tourism purposes – BGN 9.6 million.

Measures for the support of government bodies, charged with activities to control the pandemic and the consequences of COVID-19 – the most significant are:

- The costs for support of the personnel on the first line, directly engaged in activities for prevention of the spread of COVID-19, incl. for administering vaccines – costs in the amount of BGN 369.9 million;
- Supplements to the remuneration of the staff in the hospital establishments – BGN 74.8 million;

- costs for anti-epidemic measures in municipal administrations – BGN 63.3 million;
- costs for personal protective equipment (masks, gloves, overalls, protective clothing, protective glasses) for the needs of the state administration and medical institutions; for disinfectants, disinfection of working premises, thermometers for distance measurement, consumables, reagents, medicines, PCR tests, etc. for medical institutions; for rapid antigen tests for students from I to XII grades and for the purchase of air purifiers from educational institutions – BGN 33.4 million were spent;
- The NHIF budget funds financed medical care providers, dental care and medical-diagnostic activities for work under adverse conditions in connection with the declared epidemic situation and treatment of COVID-19 – BGN 216.2 million;
- Costs stemming from the implementation of the National Vaccination Plan against COVID-19 – BGN 1.3 million;
- Costs for the implementation of border health control activities – BGN 1.3 million.

As of April 1, 2022, the emergency epidemic situation on the territory of Bulgaria was terminated due to the low number of infected and the reduced pressure on the healthcare system.

– Costs related to the humanitarian crisis caused by the hostilities in Ukraine

As of 31.12.2022 reported expenses for financing activities to provide immediate humanitarian aid to Bulgarian citizens living in Ukraine and Bulgarians with Ukrainian citizenship, including if evacuation is necessary, to provide humanitarian aid to Ukraine, to provide humanitarian aid to Ukrainian refugees in Bulgaria, as well as the costs for dealing with the consequences of the military actions against Ukraine amount to BGN 580.1 million from the national budget (0.4% of GDP), incl. BGN 2.0 million are the reported expenses from the municipal budgets and BGN 142.0 million are funds from the EU (0.01% of GDP).

Humanitarian aid programs for persons with refugee status

At the beginning of March 2022, with Decision 145/2022 of the Council of Ministers was approved the "*Programme for the Use of Humanitarian Aid for Persons Seeking Temporary Protection in the Republic of Bulgaria as a result of the military actions in Ukraine"* with an initial term from 24.02.2022 to 31.05.2022. This program was later amended and supplemented by Decision No. 181, No. 239, No. 241, No. 298 and No. 423 dated 2022. The program is administered by the Ministry of Tourism, with costs financed by EU instruments and/or from the state budget. The funds reported by the ministry under this program for the period during which it was implemented for 2022 amount to BGN 161.8 million.

By Decision No. 317 of the Council of Ministers dated May 20, 2022, a new *"Program for humanitarian aid to displaced persons from Ukraine with temporary protection granted in the Republic of Bulgaria"* was approved, which was later amended and supplemented and the period of operation of the program was extended until 24.02.2023. The program is administered by the Ministry of Tourism (MT), and the aid is approved by an act of the Council of Ministers. With Decision of the Council of Ministers (DCM) No. 212 of 2023, the term of the Program was extended until April 30, 2023 in connection with the extension of the effect of temporary protection on the territory of the Republic of Bulgaria until March 4, 2024. According to DCM No. 484 dated December 21, 2022 in the budget of the Ministry of Tourism BGN 37 million have been provided at the expense of the state budget, to finance the payments under the Program until April 30, 2023. The funds spent under this program by MT as of 31.12.2022 amount to BGN 77.3 million.

As of 31.12.2022, according to the budget of the Ministry of Tourism, expenses in the total amount of BGN 239.1 million were reported for the two humanitarian aid programs in connection with the military actions in Ukraine, as part of the expenses in the amount of BGN 137.5 million were reimbursed by the operational programs of the European Union.

In the field of social protection – within the framework of the current regulations in the field of the social assistance system, Ukrainian citizens arriving in the country have the status of temporary protection. If after an assessment of each specific case it is established that the person needs support to meet his basic life needs, he has the right to social assistance and protection, including people with disabilities. In addition, those arriving from Ukraine have the right to work in Bulgaria without a permit to access the labor market, as well as to use simplified procedures for accessing the Bulgarian labor market. As of 31.12.2022, the Ministry of Labor and Social Policy reports expenses in the amount of BGN 16.3 million from its budget and BGN 4.5 million in EU funds. The one-time benefits granted are counted as social expenses in accordance with Art. 16 of the Regulations for the Implementation of the Law on Social Assistance to Persons Displaced from Ukraine with Provisional Protection, the amount being up to five times the amount of the guaranteed minimum income (BGN 375). For the period from 24.02.2022 to 31.12.2022, one-time benefits were paid to 43,483 persons granted temporary protection.

Under the "Solidarity" project, administered by the Ministry of Labor and Social Policy – the funds paid for subsidies in the amount of BGN 4.3 million include minimum aid in the sense of Regulation (EU) No. 1407/2013 and an integration supplement for accommodation of persons, Ukrainian citizens. The remuneration of 2,785 Ukrainian citizens amounts to BGN 2.71 million. 1,960 Ukrainian citizens have benefited from the integration supplement in the total amount of BGN 1.25 million. The remuneration of 633 mentors is in the amount of BGN 0.34 million. The project funds are provided in accordance with Regulation (EU) 2022/613 of the European Parliament and of the Council of 12 April 2022 amending Regulations (EU) No. 1303/2013 and (EU) No. 223/2014 regarding increased pre-financing with REACT-EU funds and to determine the cost per unit of product. Under the project, funds were paid to displaced persons from Ukraine and their families.

Compensation for Bulgarian farmers for the adverse consequences of the war in Ukraine

The DCM No. 247 dated 17.08.2022 grants the State Fund "Agriculture" to ensure liquidity to farmers and to support pig farmers and poultry farmers for animal welfare, as well as to provide support to farmers under national measures to compensate for the increased prices of energy commodities, feed, plant protection preparations, fuels and fertilizers. As of 31.12.2022, the State Fund "Agriculture" reports costs for subsidies in the total amount of BGN 444.0 million to ensure liquidity of farmers under the Temporary Framework in connection with the military actions in Ukraine and to support pig farmers and poultry farmers for humane treatment of animals, as well as to provide support to farmers under national measures to compensate for the increased prices of energy carriers, feed, plant protection preparations, fuels and fertilizers.

Other expenses

The Ministry of Interior reports expenses incurred in the amount of BGN 3.0 million for humanitarian aid, as well as for dealing with the consequences in connection with the military actions in Ukraine for the period 01.01 – 31.12.2022. The indicated data include expenses for overtime work and the due social security contributions on it, as well as salaries and corresponding social security contributions for the personnel in the holiday accommodations of the Ministry of the Interior, serving the accommodated members of families of employees of the

Ministry of the Interior of Ukraine. The amount also includes current expenses and capital expenses.

The expenses of the Council of Ministers in this direction are in the amount of BGN 5.4 million, of which BGN 5.2 million are reported for maintenance.

The expenses incurred by the Ministry of Defense for humanitarian aid, as well as for dealing with the consequences of the military actions in Ukraine, amount to BGN 2.6 million at the expense of the budget of the Ministry of Defense.

BGN 2.6 million are spent on the budget of the Ministry of Transport and Communications to cover the free transport of Ukrainian citizens on the territory of the country, is counted as subsidy costs.

In the field of health care – with the 2022 amendments to the Law on Health Insurance for Foreign Citizens with Temporary Protection adopted by the National Assembly, access to the full range of medical care paid by the NHIF was ensured, as the specific issues related to determining the amount and order for the payment of health insurance contributions, the persons who pay them, the moment of occurrence of payment obligations and the moment of occurrence of the rights of insured persons are determined by Resolution No. 69 of May 5, 2022 of the Council of Ministers for Health Insurance of Persons with Temporary Protection under Art. 1a, par. 3 of the Law on Asylum and Refugees and to persons under Art. 39, par. 6, item 2 and art. 40a, par. 3a of the Law on Health Insurance, for this purpose BGN 7.3 million were provided from the state budget in 2022 and BGN 10.0 million have been allocated in the draft law for 2023.

In the field of education – in relation to education, it should be borne in mind that the system is open to the reception and education of children and students of preschool and school age from Ukraine in Bulgarian state and municipal kindergartens and schools, which expands the scope of children and accordingly of the costs associated with them. In connection with the provision of activities aimed at persons seeking temporary protection in the Republic of Bulgaria as a result of the military actions in the Republic of Ukraine, the following acts of the Council of Ministers were adopted in 2022: DCM No. 144/2022 on granting temporary protection to displaced persons from Ukraine and amending the National Action Plan for Temporary Protection in the Republic of Bulgaria; DCM No. 105/2022 approving additional expenses under the budgets of the Council of Ministers and the Ministry of Health for 2022 for advance financing of expenses for persons seeking temporary protection in the Republic of Bulgaria as a result of the military actions in Ukraine (amended and supplemented with DCM No. 106/2022 and DCM No. 194/2022) and DCM No. 414/2022 for approving additional funds under the budget of the Ministry of Health and approving an additional transfer under the budget of the NHIF for 2022 for payment of the medical assistance and health insurance contributions of the persons granted temporary protection.

– Compensation programs for high electricity and natural gas prices

At the end of 2021, the *Program for compensating non-domestic end customers of electricity and the Program for compensating the costs of the operators of electricity transmission and distribution networks for the purchase of amounts of electricity needed for technological costs were approved* (DCM № 739/2021; DCM № 771/2021; DCM № 885/2021; DCM № 893/2021). Support under the programs is aimed at all non-domestic end customers in the sense of § 1, item 27d and 33a of the Additional Provisions of the Energy Act (EE). The programs provide a mechanism to support non-residential final customers through electricity traders, suppliers of last resort, electricity producers selling directly to non-residential final customers and the operator of an organized electricity exchange market The beneficiaries of this program are estimated to be around 633,000 non-residential electricity end customers. They are supported monthly by making compensation based on the quantities of active electrical energy, on which, in principle, a "duty to society" price should be charged, with a fixed amount of support per MWh. The operation of these programs was extended initially until the end of the first quarter, and subsequently until the end of the half-year of 2022, as they were repeatedly modified and further developed (DCM 15/2022; DCM No. 30/2022; DCM No. 92/2022; DCM No. 105/22022; DCM No. 202/2022; DCM No. 301/2022; DCM No. 356/2022). The total amount paid under the programs in the period January – July 2022 is BGN 1,647.6 million. (1% of GDP).

In addition to the compensations for non-domestic consumers of electricity and for the operators of the electricity transmission and distribution networks for the purchase of amounts of electricity needed for technological costs, the following were also approved:

- *Program for compensating residential customers of natural gas and district heating companies using natural gas as the main fuel, with support of a fixed amount per MWh (*DCM № *31/2022).* The program envisages a mechanism to assist household customers through the end suppliers of natural gas and through the public supplier in the sale of natural gas to persons who have been issued a license for the production and transmission of thermal energy, in their capacity as heat supply companies. About 137,951 domestic natural gas and district heating customers who use natural gas as their main fuel benefit from the program, and assistance was provided through compensation based on the quantities of natural gas consumed for the relevant month up to a fixed amount per MWh.
- *Compensation Program for the unforeseen expenses of the water supply companies for consumed electrical energy (*DCM № *40/2022).* The program aims to further minimize the negative effect for non-domestic users of the water supply sector from the increase in the price of electricity in international markets and to reflect the specific nature of the provision of water supply services by companies to consumers at prices regulated by a state body.
- *Program to support students and PhD students housed in student dormitories managed by state higher education institutions and "Student Canteens and Dormitories" EAD (SSO EAD) (DCM №162/2022).* The principle for calculating the compensations under the program is based on the need to compensate the excess costs of purchasing electricity at market prices, compared to the value of the same quantities of electricity at regulated prices for domestic end customers of the state universities and student halls and dormitories EAD. This need arises from the fact that the organizations running the dormitories buy electricity as non-domestic end customers, and the predominant amounts of it are consumed for domestic needs by the users of the dormitories. On the basis of the preliminary calculations, it is planned that about 30,000 students and PhD housed in student dormitories will benefit from the compensation on average per month.

The mentioned three programs were supplemented several times (DCM №93/2022, DCM № 105/2022, DCM No. 202/2022, DCM № 301/2022, DCM № 356/2022, DCM № 734/2022), and the total amounts paid under them in 2022 amounted to BGN 208.8 million. (0.1% of GDP)

With the entry into force of the Law for amending and complementing of the Law on State Budget for 2022 (State Gazette, volume 52 of 07.05.2022) provisions were approved in §23 and §24 of the Transitional and Final Provisions of the Law, which regulated a new mechanism for financing compensations for non-domestic end customers of electricity through the budget of the ESSF. The final text of the regulations provides that public enterprises from the energy sector with 100 percent state participation in the capital will make targeted contributions to the

ESSF, which will be used to cover the costs of compensating non-residential end customers of electricity. It was decided that the compensation should be in the amount of 100 percent of the difference between the real average monthly exchange price of the "day-ahead" segment of the Bulgarian Independent Energy Exchange EAD (BIEE) for the relevant month and the base price in the amount of BGN 250/MWh. It is planned that this mechanism will be applied for the period from July 1, 2022 to December 31, 2022, and upon the proposal of the Minister of Energy, the Council of Ministers will determine the amount and deadlines for making the targeted contributions. The total amount of revenue from the targeted contributions received under the ESSF budget, in implementation of DCM № 490/2022, DCM № 587/2022, DCM № 648/2022, DCM № 735/2022, DCM № 920/2022 and DCM № 1035 /2022 for the period July-December 2022 is in the amount of BGN 3,181.0 million (1.9% of GDP). By its decision the Council of Ministers approved a new *Program for compensating the costs of non-domestic end customers for electric energy and the operators of the electric transmission network for the purchase of quantities of electric energy needed for technological costs for the period from July 1, 2022 to September 30, 2022.* (DCM No. 534/29.07.2022), which was also extended for the period from October 1, 2022 to December 31, 2022 (DCM No. 710/29.07.2022). The program combines the previously existing Program for the compensation of non-residential final customers of electricity and the Program for the compensation of the costs of electricity transmission and distribution network operators for the purchase of quantities of electricity required for technological costs, targeting the same group of affected non-residential final customers consumers of electric energy and uses the compensation mechanism, regulated by the provisions of the effective Law for amending and complementing of the Law on State Budget 2022. Cost under the program until the end of 2022 are in the amount of BGN 2,712.2 million (1.6% of GDP).

The Law for amending and complementing of the Law on State Budget for 2022 provided the amount of BGN 150 million to compensate individuals, end users of motor fuels for the period July-December 2022. The compensation was provided by reducing the amount owed by the individual for payment of the final distributor in the amount of BGN 0.25 per liter/kilogram of fuel when directly filling into a fuel tank. Compensation was provided when paid in cash, by bank debit or credit card.

3.3.4 Budget highlights for 2023

– Revenues policy

The estimates for the period 2023–2026 reflect the increase in the amount of the minimum wage from January 1, 2023 – from BGN 710 to BGN 780, while the effects of the amount of the estimated minimum wage for the period 2024-2026 are calculated in an indicative amount, in accordance with Art. 244 of the Labor Code.

An increase in funds for the delegated activities in education for the period 2023–2026 is foreseen in connection with the continuation of the policy of increasing the salaries of education specialists to reach an average salary of not less than 125 percent of the average salary for the country in order to stimulate the entry of young and qualified teachers into the preschool and school education system.

For 2023, an increase in the funds for salaries and remuneration has been calculated for the personnel in the elected positions and for those employed in the judicial system, for which a mechanism for the formation of the remuneration is regulated by law.

Funds are provided in full for 2023 and subsequent years as a result of increases made in personnel costs in 2022 to individual budget officers.

A 10% increase in personnel costs is envisaged for structures that did not receive another increase in 2022.

— Social policy

With regard to the policy related to social support and benefits paid from the budget of the State Social Security, the updated medium-term budget forecast for the period 2023–2026, in accordance with the requirements of the SSC, provides:

- The minimum daily amount of the unemployment compensation (BGN 18.00) and the maximum daily amount (BGN 85.71) are maintained for the entire period up to and including 2026;
- The period of payment of cash compensation for pregnancy and childbirth is maintained (410 days), as well as the amount of compensation for raising a child up to two years of age and for raising a child up to 8 years of age by the father (adoptive parent) – BGN 710 for the entire period up to and including 2026;
- Maintaining the regime of payment of cash compensation for temporary incapacity for work according to Art. 40, par. 5 of SSC – the first three working days are paid by the insurer, and from the 4th day of the onset of incapacity – by the State Social Security for the entire period up to and including 2026;
- Maintaining the period from which short-term compensations are calculated in case of temporary incapacity for work is kept – 18 calendar months, pregnancy and childbirth and unemployment – 24 months, for the entire period up to and including 2026;
- The amount of the one-time compensations in the event of the death of an insured person is retained – BGN 540 for the entire forecast period;
- For the period 2023–2026, the provision of Art. 22, par. 2 of the Law on Factory and Office Workers' Claims Guaranteed in the Event of Their Employer's Bankruptcy, regarding the maximum monthly amount of the guaranteed receivable, which cannot be less than 2.5 minimum wages is kept.
- As a result of these assumptions, the costs of compensations and benefits under the budget of the State Social Security in 2023 will increase by BGN 180.6 million compared to the 2022 Law.
- According to the budget of the Ministry of Labor and Social Policy for 2023, additional costs for benefits and benefits are envisaged, including:
    - BGN 111.1 million in connection with the determined new amount of BGN 504 of the poverty line for 2023, when determining the financial support under the Law for Persons with Disabilities;
    - BGN 131.0 million under the Personal Assistance Mechanism under the Personal Assistance Law, taking into account the reached scope of users and personal assistants, as well as the increase of the minimum wage from BGN 710 to BGN 780 for remuneration of personal assistants;
    - BGN 50.1 million, taking into account the phased implementation of the transition from the current mechanism for linking monthly social benefits under the Social Assistance Law to the poverty line, as well as the determined new amount of BGN 504 for the poverty line for 2023.;
    - BGN 50.0 million under the Law on Family Allowances to ensure a year-round increase from 01.04.2022 of the income criterion from BGN 410 to BGN 510 for monthly family allowances for raising a child until the completion of secondary education, but no more than 20 years of age (Article 7 of the Law on Family Allowances), as well as the differentiated increase in the amount of this type of benefits;

- BGN 23.4 million regarding the newly introduced one-off assistance for second, third and fourth grade students without an income test, regardless of the type of school under the Law on Family Allowances for the first term of the 2023/2024 school year.

─ Health care policies

The health care policy for the period 2023–2026 is aimed at improving the efficiency and the citizens’ satisfaction of the functioning of the sector.

The identified policy priorities of the Ministry of Health for the period 2023–2026 are as follows:

- Protecting citizens' health as a state of physical, mental and social well-being;
- Ensuring financial stability and security of the health system through a long-term, sustainable and predictable funding mechanism based on health outcomes;
- Increasing the quality and accessibility of health services with a focus on prevention and treatment of socially significant diseases;
- Providing health protection for children, pregnant women and persons with physical disabilities and mental disorders;
- Development of capacity for emergency assistance and emergency response;
- Better planning and motivation of the health care workforce;
- Development of electronic health care and digitization of the health care system.

In the field of health care, additional funds have been provided for the period 2023–2026 as follows:

- BGN 267.0 million to purchase additional quantities of vaccines against COVID-19, with a view to creating maximum opportunities for vaccination of the population, especially in population groups with a proven increased risk of severe course of the disease, hospitalization and death;
- BGN 142.6 million – in order to strengthen the personnel capacity and financial sustainability of the reached salary level of the personnel directly involved in activities to prevent the spread of COVID-19 in the Regional Health Inspectorates and the Centers for Emergency Medical Assistance – second-level spenders to the Minister of Health, as well and for financial provision of the minimum basic salary levels agreed in the Collective Labor Agreement in the Health care sector 2022 for the medical staff employed in the health and treatment facilities, whose heads are second-level spenders to the Minister of Health, and in the health offices in state and municipal kindergartens and schools, in nurseries and nursery groups for kindergartens;
- BGN 5.1 million to provide for the establishment of a new Air Emergency Medical Centre, comprising 5 bases in Sofia, Dolna Mitropolia, Varna, Plovdiv and Bezmer, as well as the opening of Emergency Medical Care Branches in Primorsko and Sarnitsa, in order to provide emergency medical care by air, as well as to improve access to emergency care for citizens during the tourist seasons;
- BGN 35.0 million to ensure an increase in the number of persons who need treatment and to expand the scope of activities related to the treatment of persons under 18 and over 18 years of age in the country or abroad, for whom no other mechanisms for financing are

envisaged with funds from the state budget, municipal budgets and the budget of the NHIF or which cannot be provided in the country;

- BGN 4.0 million to expand the scope of persons, incl. to carry out prophylactic immunization of newborns against rotavirus gastroenteritis under the National Program for the Prevention of Rotavirus Gastroenteritis in the Republic of Bulgaria 2022–2025;
- BGN 7.7 million to increase the immunization coverage against seasonal flu of the target group under the National Program for Improving Vaccination Prevention of Seasonal Flu and Pneumococcal Infections in Persons 65 and Over 2023–2026.

In order to improve the efficiency of costs and the satisfaction of citizens with the functioning of the health sector, an additional BGN 849.6 million were provided for health insurance payments in the budget of the NHIF in 2023.

The approved funds are aimed at several main priority areas in the health care system:

- policy in the field of promotion, prevention and control of public health, the purpose of which is to ensure quality and effective meeting of the health needs of citizens by implementing primary prevention, health promotion and integrated prevention of infectious diseases, including surveillance of infectious diseases and effective government health control over environmental factors. The policy includes: implementation of national programs in terms of limiting morbidity and mortality from infectious diseases; central supply of vaccines for mandatory and targeted immunizations and of vaccines and drugs for the treatment of COVID-19, etc.
- policy in the field of diagnosis and treatment, which is aimed at improving the health status and quality of life of Bulgarian citizens and reducing health inequalities through activities in the field of diagnosis and treatment of diseases and the organization of medical assistance. The priority investment projects planned for implementation in the field of diagnostics and treatment are related to the development of electronic health care and improvement of the material base and access to health services for all citizens.
- the main scope of the policy in the field of medicinal products and medical devices is to provide medicinal products that meet the standards of quality, safety and efficacy to meet the needs of the population.

The provisions of the Law on Health Insurance, which introduce a gradual increase in the part of the minimum insurance income on which health insurance contributions are determined for persons who are insured at the expense of the state budget, continue to apply – from 55 percent in 2016 to 90 percent of the minimum insurance income for self-insured persons from January 1, 2023, with each subsequent year the ratio increases by 5 percent. until reaching the minimum insurance income for self-insured persons. At the same time, with the increase in the minimum wage, the minimum insurance income, on which the state makes contributions, also increases. The total amount as a result of the changes will increase in 2023 by 145.4 million. The total amount as a result of the changes will increase in 2023 by BGN 145.4 million. The effect on the balance on a consolidated basis is neutral because income and expenses will increase by the same amount.

– Policies in the field of education and science

Policies in preschool and school education are aimed at effective socialization of children from early childhood, ensuring equal access to quality education, personal development of children and students, promotion of innovation, qualification of pedagogical specialists, modernization of educational institutions, digitalization of education. An increase in funds for the delegated activities in education is foreseen in connection with the continuation of the policy of increasing the salaries of pedagogical specialists to reach an average salary of not less than 125 percent of the average salary for the country, in order to stimulate the entry of young and qualified teachers in the system of preschool and school education. Measures aimed at reducing inequalities and promoting social inclusion, motivation of children and students for education and acquisition of key competences are also implemented. Educational policies/measures are included in Priority 1 "Education and Skills" of the National Development Programme Bulgaria 2030. They are enshrined in the Strategic Framework for the Development of Education, Training and Learning in the Republic of Bulgaria (2021-2030).

The provision of conditions for quality education for all will also be supported through the implementation of a complex of measures laid down in the investment projects and procedures of the Ministry of Education and Culture under the NRRP. The investment project "STEM centers and innovations in education" aims to increase digital literacy and motivation to learn, promote interest and develop students' skills in the field of natural and engineering sciences, artificial intelligence, robotics, IT, innovation and entrepreneurship for their practical application. The investment project "Modernization of educational infrastructure" aims to create a material base that guarantees healthy and high-quality conditions for learning and the achievement of an overall renewed appearance of educational institutions, supported by investments in the construction of a safe, ecological, attractive and healthy environment for learning, development, upbringing and socialization.

For preschool and school education for 2023, additional funds are provided as follows:

- BGN 465.0 million – to continue the policy of increasing the salaries of pedagogic specialists to reach an average salary of not less than 125 percent of the average salary for the country in order to stimulate the entry of young and qualified teachers into the system of preschool and school education;
- BGN 18.0 million – to continue the step-by-step expansion of access and inclusion in compulsory preschool education for 4-year-old children;
- BGN 44.4 million – to increase the interest and increase the extracurricular activities guaranteed for each student through additional support for sports, recreation and culture to ensure wide access to them and for outstanding high achievements;
- BGN 4.8 million – for the development of Bulgarian studies abroad, by providing better conditions for seconded teachers in secondary and higher schools abroad and for additional financing of Sunday schools abroad.

In the field of higher education, the policy with the aim of promoting the efforts of autonomous higher education institutions for continuous development of the quality of the higher education offered, assisting them in the introduction, development and improvement of internal systems for evaluating and maintaining the quality of education and academic staff, in period 2023–2026, additional funds are provided, distributed as follows:

- BGN 40.0 million – year-round effect of the increased in 2022 remuneration of academic staff in state higher education institutions;
- BGN 20.00 million – for the maintenance of the education of the state higher schools in accordance with the order of art. 91, par. 2 of the Law on Higher Education by increasing the weight of the allocation based on a comprehensive assessment of the quality of education and its compliance with the needs of the labor market;
- BGN 24.4 million – for social and household expenses of students and doctoral students;

Funds for the period 2023–2026 are planned for the increased remuneration of the scientists of the Bulgarian Academy of Sciences in 2022 in the amount of BGN 26.7 million.

Every year, the central budget calculates and spends funds for the National Strategy for Development of Scientific Research in the Republic of Bulgaria 2017–2030 and the National Road Map for Scientific Infrastructure and National Scientific Programs.

According to the National Strategy for Development of Scientific Research in the Republic of Bulgaria 2017-2030, the planned public funding of R&D for 2023 should amount to 0.80% of GDP.

The adoption of a single normative act for the promotion of research and innovation will set a framework and establish a clear coordination and funding mechanism. Improving the regulatory framework and the coordination and funding mechanisms will allow for a more efficient use of financial resources and increase the levels of private sector investment and improve the links between science and business.

During the period of implementation of the CP 2023–2026, "Programme to Power up Economic Recovery and Transformation through Science and Innovation" will be implemented, which is expected to leverage funds under the National Recovery and Resilience Plan.

The envisaged investments are in two main pillars:

- Pillar One: Strengthening research and innovation capacity and accelerating the internationalization of the national innovation ecosystem. The first pillar includes two operations: 1) the implementation of project proposals of innovative small and medium-sized enterprises (SMEs) awarded the Seal of Excellence in the European Innovation Council competitions and 2) the implementation of project proposals in the "Widening participation and strengthening ERA" part of the Horizon Europe FP to strengthen the research and innovation capacity of Bulgarian public universities and research organizations. The two operations provide synergies with the European Union's Horizon Europe Framework Programme for Research and Innovation (2021-2027).
- Pillar 2: Establishing a network of research universities in Bulgaria. The objective of this pillar is to create and promote a national model for the development of research universities, which allows universities to move to a next stage of their development and become full participants in the research and innovation ecosystem.

The established network of research universities includes 9 universities. The programme aims to develop this model and encourage more universities to stimulate and fund in research to not only improve the quality of education and training, but also to provide innovative developments to the Industry and in particular to small and medium business and industry.

Under Project Fiche 5 of "Programme to Power up Economic Recovery and Transformation through Science and Innovation", it is expected that a total of BGN 401 million will be leveraged over the entire period of implementation of the NREAP as follows: for the period 2021-2023 – BGN 256 million, for 2024 – BGN 72.5 million, and for 2025 – BGN 72.5 million.

In 2023, the implementation of the measures of the Operational Plan for the implementation of the first stage (2017-2022) of the National Strategy for Development of Scientific Research in the Republic of Bulgaria 2017-2030 will be reported and an Operational Plan for the implementation of its second stage (2023–2025) will be developed and adopted. From 2024, the focus will be on the development of existing infrastructures and regular evaluation of their effectiveness in terms of the services offered. The strategic programmes of the Centers of Excellence and Centers of Competence under the Research, Innovation and Digitalization for Smart Transformation Programme 2021-2027 will also be supported.

— Defense policy

The 2023 draft budget law and the budget forecast for the period 2024-2026 provide funds for the maintenance and development of national defense capabilities and capabilities, related to collective defense. Defense costs, according to the NATO classification, also include the costs of pensions for retired servicemen, reduced by contributions for servicemen to pension funds, the costs of military courts and military prosecutors' offices, the costs of maintaining the Permanent Delegation of the Republic of Bulgaria to NATO, the contribution of the Republic of Bulgaria to the civilian budget of NATO and to the European Peace Support Mechanism, paid from the budget of the Ministry of Foreign Affairs (MFA) and the contribution of the Republic of Bulgaria to the NATO Innovation Fund, paid from the budget of the Ministry of Innovation and Growth (MIG). Thus planned, defense spending in total amounts to 1.85 percent of GDP for 2023, for the period 2024-2025 – 2 percent of GDP for each year, for 2026 2.15% of GDP, in accordance with the National Plan for increasing defense spending to 2 percent of the GDP of the Republic of Bulgaria by 2024, approved by Decision of the Council of Ministers №3 of 2018.

Funds are provided for the rearmament and modernization of the three types of armed forces and the increase of the defense capabilities of the Bulgarian Army, and funds are provided for the implementation of the investment projects approved by the National Assembly for the modernization of the Bulgarian Army, namely: the acquisition of a multi-functional modular patrol ship for the Navy, a new type of combat aircraft – II stage, including for associated costs in two stages (MIDS terminals, transport, VAT and customs duties) and basic combat equipment for the construction of battalion combat groups from the composition of a mechanized brigade. In addition, funds are provided for the acquisition of ammunition and fuel for combat training, as well as for the acquisition, modernization, maintenance and repair of armaments, rockets, torpedoes and technique, and repair and building infrastructure.

— Energy measures

In order to mitigate the economic consequences of the sudden instability of electricity and natural gas prices in 2021, 2022 and 2023, measures have been taken through the adoption and implementation of programs to compensate for the increase in the prices of energy carriers, including:

- Program for compensation of non-domestic end customers of electric energy – compensation period 01.10.2021–31.03.2023, which is likely to be extended in view of the Decision of the 48th National Assembly of the Republic of Bulgaria, which assigns The Council of Ministers to adopt a program for providing compensation to non-domestic end customers of electricity from 01.01.2023 to 31.12.2023;
- Program for compensating the costs of the operators of the electricity transmission and distribution networks for the purchase of the quantities of electrical energy needed for technological costs – compensation period 01.07.2021–31.03.2023;
- Program for compensation of domestic customers of natural gas and heating companies using natural gas as the main fuel with support with a fixed amount per MWh – compensation period 01.12.2021–31.05.2022;
- Program for compensating the unforeseen expenses of the water and sanitation industry companies for the consumed electricity for 2021 – compensation period 01.01.2021–30.06.2022;
- Program to support students and PhDs accommodated in student dormitories managed by state universities and "Student Chairs and Dormitories" EAD for the compensation period from 01.10.2021 to 30.04.2022.

To ensure the implementation of the Government's programs for mitigating the economic consequences of the instability of electricity and natural gas prices, funds are provided as follows:

- Additional expenses granted under the budget of the Ministry of Energy (BGN 1 310 million with resolutions of the Council of Ministers No. 355, No. 475 and No. 476 of 2021.);
- Revenues of the Power System Security Fund, incl. own revenues for 2022 in the amount of BGN 1 244.5 million (with Decisions No.C-10 and No.C-15 of 2022 of the Commission for Energy and Water Regulation), revenues received on the basis of §24 of the Transitional and Final Provisions (TFP) of the Law on the State Budget of the Republic of Bulgaria for 2022 (BGN 3 181 million for the period from July 2022 to December 2022) and incoming revenues (from January 2023 to June 30, 2023) on the basis of §8 of the TFP provisions of the Law on the Implementation of provisions of the Law on the State Budget of the Republic of Bulgaria for 2022, the Law on the State Public Insurance Budget for 2022 and the Law on the Budget of the NHIF for 2022 (BGN 446.1 million as of 28.02.2023).

– Transport, communications and e-government policy

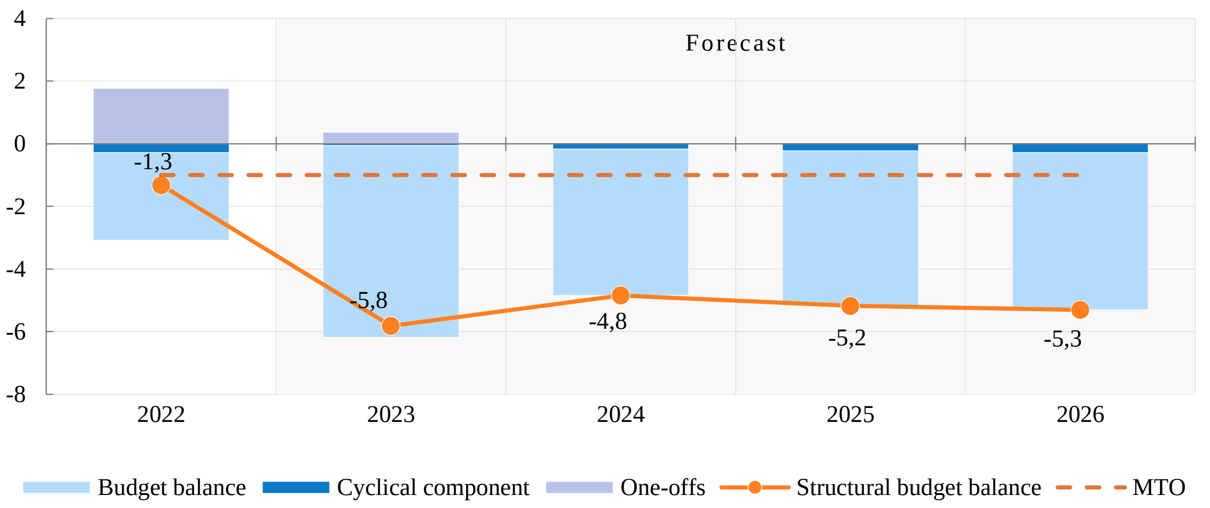
From January 1, 2019, the phased introduction of the toll system began with the introduction of the so-called "electronic vignette" for passenger cars, and from March 2020, the phased introduction of TOL segments in the scope of the paid road network based on distance traveled began, which also started the charging of trucks over 3.5 tons. In 2022, a change was made amending the scope of the republican road network and updating the toll rate. In this regard, for the period 2023–2026, a change in revenues from toll fees is expected, with an increase in revenues of BGN 189.3 million for 2023, an increase of BGN 66.26 million is planned for 2024, and for 2025 and 2026, it is planned to maintain the revenues up to the amounts of 2024, in which the amount of revenues from toll fees on an annual basis of BGN 520.0 million is reached. The funds will be directed to the effective maintenance, modernization and development of the transport infrastructure, construction of highways and integration of the national road infrastructure into the European transport network.

3.4 Structural balance (cyclical components of the balance, one-off and temporary measures) and fiscal position, including the expenditure benchmark

The structural budget balance in 2023 is estimated at a deficit of 5.8% of GDP. In its calculation, the negative General government balance is adjusted for one-off measures. Their size, presented as a percentage of GDP, is decreasing compared to recent years, and as one-off revenues are planned to decrease significantly, the adjustment is towards a slightly higher structural budget deficit. At the same time, the cyclical component, which reflects, the positive output gap and the sensitivity of the budgetary position to the economic cycle, is reflected in a downward adjustment of the structural budget balance.

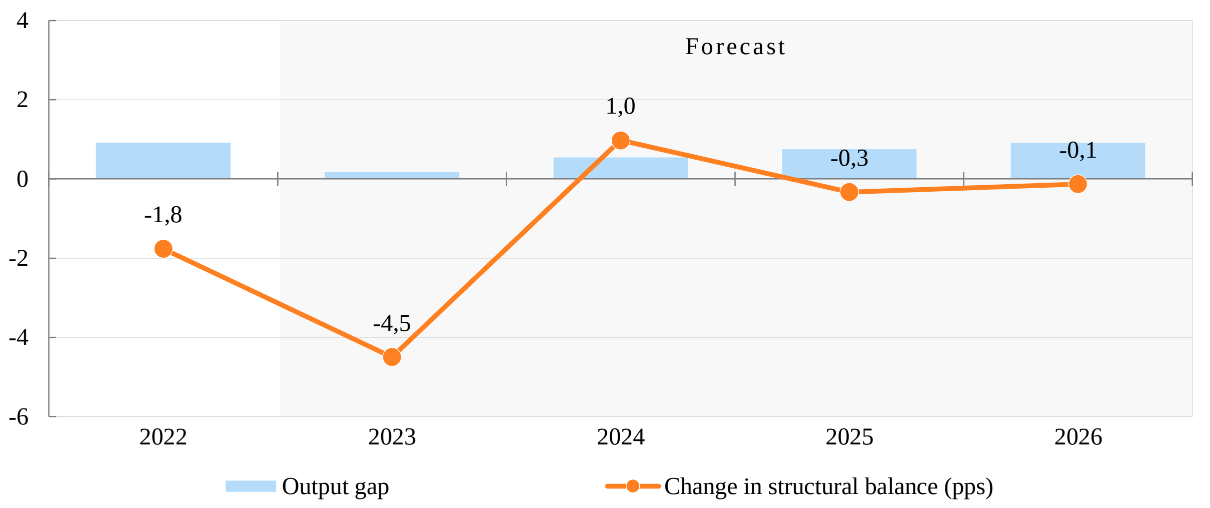
In 2024, a reduction in the deficit of the "General government" sector is planned, as a result of expected higher revenues. No one-off expenditures (or revenues) are foreseen, so there will be no effect on the structural budget balance. The economy will be slightly above its potential and the cyclical component will have a slight negative effect on the structural balance. As a result, the structural budget deficit will shrink to 4.8% of GDP in 2024.

Graph 3-2: Structural budget balance



Source: MF, own calculations

Graph 3-3: Fiscal position



Source: MF, own calculations

In the last two years of the forecast period, the General Government deficit is forecast at 4.9 and 5% of GDP, respectively, and no one-off are foreseen. The output gap will remain positive and will slightly increase, which will be reflected in an adjustment to a lower structural balance compared to the planned actual budget deficit in both years. The structural budget deficit will reach 5.2% of GDP in 2025 and 5.3% at the end of the forecast period.

The medium-term budget target for the structural balance of the "General Government" sector is a deficit of 1% of GDP. This objective is in accordance with the requirements of Art. 23, par. 2 of the PFL, taking into account the relatively low amount of the Consolidated General Government debt, as well as the low risks to the long-term sustainability of public finances. According to Art. 24 of the LPF, the non-fulfillment of the medium-term budget objective for the structural deficit is allowed in exceptional circumstances. Due to the crisis triggered by COVID-19, the General Escape Clause of the SGP was activated in 2020, allowing Member States to deviate from the step to achieve the medium-term budgetary objective in 2020 and 2021. Subsequently, a decision of the European Commission (EC) extended the application of the EU escape clause for 2022 and 2023, but the general escape clause will not apply for 2024.

The assessment of compliance with the requirements under the SGP and the LPF regarding the growth of budgetary expenditure is based on the EC's common methodology for the so-called expenditure benchmark, taking into account the difference between nationally and EU-funded public investment. The expenditure benchmark is compared to the level of the potential medium-term GDP growth calculated by the EC.

Based on calculations made by the Ministry of Finance, the change in real terms of the expenditure indicator used for fiscal governance purposes in the EU is estimated at -3% for 2022, 5.4% for 2023, -1% for 2024, 0.5% for 2025 and 2% for 2026, respectively.

The expenditure benchmark is part of the indicators monitored in the assessment of compliance with the rules in the preventive part of the SGP and as such falls under the general escape clause, which was activated in the 2020-2021 period and will continue to operate in the current year 2023.

3.5 Debt levels and developments, below-the-line operations

Based on the data from the April Notification tables on the deficit/surplus and debt of Bulgaria, by the end of 2022, the amount of the "General Government" sector debt is increasing compared to the level of the previous year. In nominal terms, the debt level increases by about BGN 4.6 billion from BGN 33.3 billion in 2021 to BGN 37.8 billion in 2022. As a ratio to GDP, the indicator decreases by 1 pps. to 22.9% (at 23.9% at the end of 2021), remaining far below the Maastricht convergence criterion threshold of 60%. Among the individual components forming the sector debt, the "Central Government" sub-sector debt shows the most significant growth, as the main contribution to this is the government debt.

In 2022, debt financing of the "Central Government" sub-sector was received in the total amount of BGN 7.7 billion, the main part of which is in the form of government securities placed on both the domestic and international capital markets. Government securities with a total nominal value of BGN 2.6 billion were issued on the domestic debt market during the year, divided into four issues denominated in BGN: 3.5-year government securities (issued in November 2021, with maturity date 17.05.2025) with a total placed amount of BGN 1,300.0 million, 5.5-year government securities (issued in September 2022, with maturity date 28.03.2028) with a total placed volume of BGN 330.5 million, 7.5-year government securities (issued in November 2021, with maturity date 24.05.2029) with an amount of BGN 500.0 million and 10.5-year (issued in January 2016, with maturity date 27.07.2026) with a total placed amount of BGN 502.75 million. In line with the Global Medium-Term Note Programme for issuing debt on the international capital markets in September 2022, the Republic of Bulgaria is placing two tranches of Eurobonds with a total nominal volume of BGN 4.4 billion. (2.25 billion euros), incl. with a maturity of 7 years, an amount of 1.5 billion euros and with a maturity of 12 years, a volume of 750 million euros. Funds in the amount of BGN 899.7 million were also disbursed (EUR 460.0 million) under the second government loan under the European Instrument for Temporary Support to Mitigate Unemployment Risks in an Emergency (SURE) following the COVID-19 outbreak (15-year tranche).

For the same period, the debt repayments of the subsector amounted to BGN 3.3 billion, of which BGN 2.7 billion are maturities of bonds issued on the foreign and domestic debt markets (BGN 2.4 billion are maturities of Eurobonds issued on the international capital markets in 2015 and BGN 0.3 billion maturities of government securities) and BGN 0.6 billion in loans, incl. government loans and loans to institutional units included in the scope of the sub-sector.

The currency and interest rate structure of the "General Government" sector debt at the end of 2022 is characterized by a dominant share of debt denominated in euros – 69.7% and in BGN – 30.1%, as well as liabilities with a fixed interest rate – 98.3%. At the end of 2022 the part of the debt denominated in other currencies is 0.2%, and that with floating interest rates – 1.7% as of 31.12.2022. This structure of the debt portfolio is preserved throughout the period 2023–2026, as the relevant portion of the debt in leva and euro and the debt with floating interest rates as of 31.12.2026 are eexpected to be around 99.9% and 0.2%.

The interest payments for 2022 on an accrued basis to the estimated GDP are expected to reach a level of about 0.4%, and compared to the previous years in the period 2023–2026 higher levels are forecasted: 0.6% in 2023 to 1.3% at the end of 2026. The more negative dynamics of debt service costs in the medium term is determined by the increased levels of regulatory interest rates and expectations this trend to continue.

As of December 31, 2022, the average residual maturity of the General Government sector debt was 7.7 years, and at the end of 2026 it is expected to gradually extend to 9 years.

For the current 2023, the expectations for an upward trend in the debt level of the "General Government" sector are maintained. In nominal terms, its value is expected to reach BGN 49.1 billion, and the ratio of debt to GDP – at the level of 26.6%.

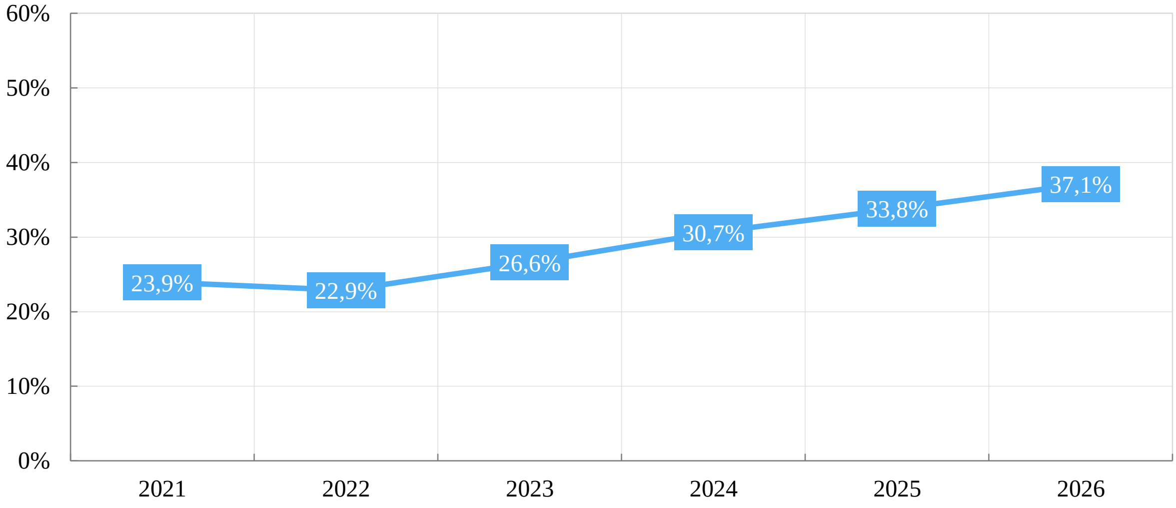
In 2023, until the adoption of the State Budget Law of the Republic of Bulgaria for 2023 by the National Assembly, but for a period not longer than three months (this period ceases to run from the day of dissolution of the National Assembly to the day of constitution of the next National Assembly), based on the provisions of the Law on the Application of Provisions the 2022 State Budget of the Republic of Bulgaria Act , the 2022 Public Social Insurance Budget Act and 2022 NHIF Budget Act (published, State Gazette, volume 104 of 30.12.2022, in force from 1.01.2023) and in accordance with Art. 87, par. 2 of the Public Finances Act, the Council of Ministers may issue government debt only to refinance the debt outstanding up to the amount of annual repayments on the government debt issued until the beginning of 2023 (BGN 3.0 billion). In this context, on 17.01.2023 the Republic of Bulgaria issued on the international capital markets 10-year Eurobonds with a nominal volume of EUR 1.5 billion (2.9 billion BGN) and an annual interest coupon of 4.5% within the Global Medium-Term Note Program for issuing debt on the International Capital Markets (GMTN) framework, with which the possibility of issuing of government debt until the adoption of the 2023 State Budget Act is used. The proceeds were used to cover the maturity in March 2023 of Eurobonds issued on the international capital markets.

At the moment, the debt financing needs for the 2023 state budget is projected to be in the total amount of BGN 13.7 billion. (including a BGN 2.9 billion issue of Eurobonds placed on the ICM in January 2023), which is planned to be secured through tradable debt instruments, both on the domestic and foreign markets.

In 2024, debt financing in the amount of BGN 15.2 billion is planned, in 2025 and 2026, BGN 14.6 billion per year, with the outstanding debt to be refinanced amounting to BGN 3.5 billion for 2024 (incl. BGN 2.9 billion upcoming maturity of Eurobonds), to BGN 3.6 billion for 2025 (incl. BGN 3.3 billion for maturity of domestic government securities) and BGN 2.8 billion for 2026 (incl. BGN 2.5 billion for maturity of domestic government securities). The remaining part of the planned debt financing is justified by the need to finance the planned state budget deficits and ensure the liquidity position of the fiscal reserve.

Based on the assumptions for the main indicators of the budget framework and the outlined need to secure larger volumes of new debt financing, over the next three years the level of consolidated "General Government" sector debt in nominal terms is projected to continue to grow to 60.6 billion BGN at the end of 2024, BGN 71.1 billion at the end of 2025 and BGN 82.6 billion at the end of 2026. A similar trend is expected for debt-to-GDP ratio, reaching 30.7% in 2024, 33.8% in 2025 and 37,1% in 2026. Taking into account these developments, the estimated values of the indicator of the general government sector debt/GDP remain below the maximum permissible reference threshold of the Maastricht convergence criterion of 60%.

Graph 3-4: General government sector debt/GDP ratio



Source: MF

The "Central Government" sub-sector debt continue to have a leading influence on forecasts for the growth of the consolidated "General Government" sector debt, and in particular the government debt as its main component. The contribution of the debt of the other two sub-sectors forming the debt of the "General Government" sector: "Local Government" sub-sector and "Social Security Funds" sub-sector is minimal. This trend is maintained throughout the considered period. An additional impact could be a possible expansion of the scope of the sector upon reclassification of institutional units in compliance with the requirements of Eurostat and the ESA 2010.

During the period 2023–2026, preliminary estimates show that the "Local Government" sub-sector debt will not expect significant changes compared to the level reported at the end of 2022 of about BGN 1.4 billion. In 2023, the sub-sector debt is forecast to grow to around BGN 1.9 billion, and this level will be maintained until the end of 2026. Flexible financing schemes for municipalities during the new program period will keep its share of GDP within approx. 1.0% – 1.2%. The restrictions laid down in the Public Finances Act and the Municipal Debt Act stipulate that the annual amount of municipal debt payments for each municipality in each individual year cannot exceed 15 percent of the average annual amount of own revenues and the total equalization subsidy for the last three years, calculated on the basis of data from the annual reports on the implementation of the municipality's budget.

The "Social Security Funds" sub-sector has no debt obligations and is not expected to take on new ones in the coming years. The accumulated financial assets in the form of government securities issued by the "Central Government" sub-sector participate in the netting (consolidation) of the sector. By the end of 2022, these assets amount to about BGN 365.3 million.

Table 3-1: Revenues from privatization and post-privatization control of the central budget, BGN million

Report 2022	Law on the State Budget of the Republic of Bulgaria project 2023	Forecast 2024	Forecast 2025	Forecast 2026
2.1	0.8	0.5	0.5	0.4

The values set in the table are based on a revenue forecast from privatization and post-privatization control for the period 2024-2026, prepared in February 2023 by the Agency for Public Enterprises and Control.

The main revenues by year are expected from the sale of:

- 2024: properties – private state property (BGN 0.4 million), separate parts of companies (BGN 0.1 million);
- 2025: properties-private state property (BGN 0.4 million), separate parts of companies (BGN 0.1 million);
- 2026: properties-private state property (BGN 0.2 million), separate parts of companies (BGN 0.2 million).

Proceeds from the implementation of post-privatization control under concluded privatization contracts are also expected.

3.6 Budgetary implications of major structural reforms

3.6.1 Effects on the expenditure side of the budget

— Pension policy:

The pension policy in the coming years aims to ensure the stability of income in the pension insurance system, as well as to achieve a greater adequacy of pensions in view of the demographic challenges facing the country.

The pension cost forecast for the period 2023–2026 was developed taking into account the provisions of Part One of the SSC, the updated 2022 Law on the State Social Insurance Budget and the assumptions made in the Spring Macroeconomic Forecast of the Ministry of Finance, dated March 24, 2023, including:

- Art. 68, par. 1-2 of SSC – From January 1 of each calendar year, the increase in the age for acquiring the right to a pension by 2 months for women and by 1 month for men continues for those who worked under the conditions of the third labor category. The required length of service to qualify for a pension for both sexes continues to increase by 2 months until reaching 36 years and 10 months for women and 39 years and 10 months for men in 2026.

The necessary conditions for retirement in the period 2023 – 2026 are listed in the table below:

Table 3.2: Conditions for retirement under Art. 68, para. 1-2 of the SSC, 2023–2026

Year	WOMEN		MEN	
	age	Length of service	age	Length of service
2023	62	36 y. and 4 m.	64 y. and 6 m.	39 y. and 4 m.
2024	62 y. and 2 m.	36 y. and 6 m.	64 y. and 7 m.	39 y. and 6 m.
2025	62 y. and 4 m.	36 y. and 8 m.	64 y. and 8 m.	39 y. and 8 m.
2026	62 y. and 6 m.	36 y. and 10 m.	64 y. and 9 m.	39 y. and 10 m.

Source: National Social Security Institute: MF

- Art. 68, par. 3 of SSC – the minimum retirement age for part-time work for the third category of work continues to increase by 2 months until reaching 67 years in 2023. In the period 2024 – 2026, the retirement age remains at the level reached in 2023.
- Art. 69, par. 1, 2, 3, 5, 5a and 6 of SSC- the minimum retirement age for those working in the "Security" sector continues to increase by 2 months each until reaching 54 years and 6 months in 2026.
- Art. 69b – the minimum retirement age for persons who worked under the conditions of the first and second category of work, who do not meet the conditions for retirement from an occupational pension fund under Art. 168 of SSC or have changed their insurance under Art. 4c of SSC, continues to increase by 4 months for women and 2 months for men until reaching in 2026 51 years and 4 months for women and 54 years and 6 months for men of the first labour category and 56 years and 4 months for women and 59 years and 6 months for men of the second labor category.
- In the period 2023–2026, the pensions for labour activity, granted until 31 December of the previous year, shall be updated from 1 July each year, under Art. 100 of the SSC (the so-called "Swiss rule") with a percentage defined as the sum of 50 percent of the increase in insurance income and 50 percent of the consumer price index in the previous calendar year. The amounts of the minimum pension for length of service and age and the social pension for old age, as well as the related pensions and supplements, are increased by the same percentages from July 1 of the respective year.

The expected effect on pension costs is as follows:

- for 2023 – employment pensions granted until December 31, 2022, as well as pensions not related to employment, are scheduled to be updated from July 1, 2023 by 12.0 percent (percentage determined under Art. 100 from SSC), with the necessary funds amounting to BGN 1 147.2 million;
- For 2024 – employment pensions granted until December 31, 2023, as well as pensions not related to employment, are scheduled to be updated from July 1, 2024 by 9.6 percent (percentage determined under Art. 100 from SSC), with the necessary funds amounting to BGN 1 010.7 million;
- for 2025 – pensions for employment, granted until December 31, 2024, as well as pensions not related to employment, are scheduled to be updated from July 1, 2025 by 7.6 percent (percentage determined under Art. 100 from SSC), with the necessary funds amounting to BGN 816.0 million;
- for 2026 – employment pensions granted until December 31, 2025, as well as non-employment pensions, are scheduled to be updated from July 1, 2026 by 5.4 percent (percentage determined under Art. 100 from SSC), with the necessary funds amounting to BGN 681.3 million.
- The maximum amount of one or more pensions received for the period 2023–2026 remains at BGN 3,400. (in force from 1 October 2022), applying to all pensions, regardless of the starting date of their granting.
- In the period 2023–2026, it is planned that the amounts of the minimum old age pension, as well as the related pensions and supplements, will increase by the percentages under Art. 100 per SSC as of July 1;
- Within the reference medium-term program, expenditure on pensions and supplements remains at levels between 10.4% and 11.0% of GDP.

As a result of the above-mentioned assumptions for 2023, the pension costs under the State Social Insurance Budget increase by BGN 3 657.4 million compared to the law for 2022.

In 2024, 2025 and 2026, the increases in pension costs under the budget of the Income tax compared to the previous year are BGN 2 145.9 million, BGN 1 812.3 million and BGN 1 481.7 million respectively.

Table 3-3: Estimated expenditure on pensions and allowances, 2023–2026

Year	Pension expenditure	
	million BGN	% of GDP
2023 (draft SSI Budget Law)	19 163.2	10.4
2024	21 309.0	10.8
2025	23 121.3	11.0
2026	24 603.1	11.0

Source: National Social Security Institute

3.6.2 Effects on the revenue side of the budget

Estimates of the amount of tax revenues for the period 2023–2026 are based on the forecasts of the Ministry of Finance for the main macroeconomic indicators and the impact of the measures implemented by the revenue agencies to improve collection and compliance with legislation. The priorities in the tax policy in the medium term are taken into account and the effects of the changes in the tax legislation, related to the implementation of measures for improving the collection, stimulating the economic recovery and development, reducing the administrative burden and introduction in the national legislation of provisions of European tax law are taken into account. The effects of the continued implementation of some measures related to the COVID-19 pandemic, as well as anti-crisis measures in response to the challenges of high energy and basic food prices, are reported.

– Corporate taxes

The reported financial results (taxable profit/loss) and the amount of advance payments made by persons liable to tax under the Corporate Income Tax Law (CITL) who generated a taxable profit for the previous year have a major impact on corporate tax revenues during the period.

Since 2021, the date of submission of the annual tax declarations under CITL and the date of payment of the corporate tax has been moved from March 1 to June 30 of the following year. The provisions of the CITL regarding the period for declaring advance payments (according to Art. 87a, paragraph 1 of the CITL within the period from March 1 to April 15 of the same year) and for submitting the declaration of changes to advance payments for corporate tax under Art. 88 of the CITL have been changed. The deadlines for monthly and quarterly payments have not changed, with the exception of the deadline for paying advance corporate tax for the month of December and for the third quarter of the current year, which changes from December 15 to December 1 of the year.

The forecast for the period 2023 – 2026 takes into account the effect of the application of the new scheme of tax relief, representing state aid for regional development, for which a positive decision of the EC is expected in 2023 regarding compliance with the Guidelines for regional state aid (2021/C 153/01).

When planning the receipts from other taxes under the CITL, the reduction from 2022 of the rate from 10% to 3% of the tax on expenses in kind according to Art. 204, para. 1, item 4 of the CITL.

— Personal income taxes

The forecast for the period 2023–2026 has been prepared while maintaining the single tax rate of 10% (without a tax-free minimum) for all income of taxpayers, with the exception of the income from business activities of persons carrying out business activities as traders within the meaning of the Commercial Law, including sole traders or natural persons registered as farmers, who chose to have the income from their economic activity taxed on such an annual tax base. The amount of revenues from personal income taxation does not include revenues to local budgets from patent tax and tax on taxi transport of passengers.

The amount of tax revenues from personal income tax is mainly influenced by the development of labour market parameters and the legislative and administrative measures taken in the field of labour, social and tax legislation. Influenced by the size of the average salary, the level of unemployment in the country, the results declared with the annual tax return (ATR) of individuals, the amount of dividends paid and liquidation shares, the level of interest rates on deposits of citizens and the volume of deposits.

The effect of the accepted increase in the amount of legally recognized expenses from 25 percent to 40 percent for the income from the activities of lawyers is reported, as well as the available information about the effects of the permanent measures of the National Revenue Agency to comply with tax legislation and improve the collection of income.

In forecasting PIT revenues, the expected negative annual budget effect of applying an increased amount of tax relief for children for the incomes acquired in 2022 and 2023 was taken into account.

— Value added tax

When forecasting the revenues from the VAT for the period 2023–2026, the assumptions about the changes in the economic activity in the country, the dynamics of consumption, imports, exports, the impact of the adopted legislative changes and the impact of factors due to changes in the external environment are taken into account. Both the forecasts for the macroeconomic indicators and the effects of the changes in the legislation have been taken into account.

The forecast is made on the assumption that the measures to reduce the VAT rate for restaurant and catering services, general tourist services and sports facilities will no longer apply from 01.01.2024. At the same time, the reduced rate of VAT on books, on food suitable for babies or young children and on baby nappies and similar hygiene articles remains a permanent measure of tax policy.

The effect of the reduced VAT rate of 9% for supplies of natural gas and central heating until 01.07.2023 and the application of a zero VAT rate for supplies of bread and flour until 31.12.2023 is taken into account.

— Excise duties

In the preparation of the forecasts for revenues from excise taxes, in addition to macroeconomic indicators, the positive effect of measures to improve control over trade in excise goods was also aligned, taking into account the legislative changes made. An assumption was made to preserve throughout the period of relative stability of the structure of the consumption of excise products within the various groups of excise goods.

The effects of an increase in excise rates for all tobacco products with the introduction of an excise calendar for a period of four years ahead, starting from March 1, 2023, are reported, with the aim of a balanced increase in the minimum excise tax on cigarettes and other categories of tobacco products. The forecast is based on the presumption of maintaining the excise duty rates on alcoholic beverages, beer and fuels (excluding natural gas, electricity and liquefied petroleum gas).

With regard to the revenue from excise duty on electricity, natural gas and liquefied petroleum gas used as motor fuel, it is considered that the exemption from taxation of these products will apply until 30.06.2025.

For 2023, the amount of the amount under the state aid scheme "Aid in the form of a discount on the value of the excise duty on gas oil used in primary agricultural production" is unchanged at BGN 100 million.

– Other taxes

In the preparation of the tax revenue forecasts, proceeds from the temporary solidarity contribution adopted under Council Regulation (EU) 2022/1854 of 6 October 2022 on emergency intervention to tackle high energy prices with effect from 1 October 2022 have been included. The temporary solidarity contribution shall be paid for the tax profits for 2022 and for 2023, the tax profit being determined according to the rules regulated in the CITL (§ 9. of the TFP of the CITL in force from 8.10.2022 – SG 99 of 2022). In view of the possibility provided for in the law, the obliged persons may make advance payments under this contribution.

Table 3-5: Estimated budgetary effects of discretionary revenue measures on an accrued basis for the period 2023–2026, incremental change compared to the previous year in BGN million

	2023	2024	2025	2026
Revenues from social security contributions as a result of changes in the income policy (incl. increase in the minimum wage, minimum social security thresholds and the minimum social security income of self-employed persons and the minimum social security income of farmers and tobacco farmers, increase in the maximum social security income, increase in salaries of teaching staff)	332.0	519.3	430.6	421.2
Temporary solidarity contribution under Council Regulation (EU) 2022/1854 of 6 October 2022 for emergency intervention to tackle high energy prices by companies in the oil, gas and coal extraction and refining activities.	288.0	-375.9		
Revenue from the operation of the tolling system	189.3	66.3		
Effect on VAT and excise revenue as a result of the increase in the excise duty rate on cigars and cigarillos, smoking tobacco, heated tobacco products, e-cigarette liquids (from 1.03.2023).	97.1	209.6	187.8	179.2
Personal Income Tax revenue as a result of the increase in the minimum wage, minimum social security thresholds and minimum social security income	34.4	86.0	68.0	74.0
Revenue from insurance choice	7.0	7.7	7.4	7.0
Revenues from social security contributions as a result of the increase of the length of service required for retirement	0.5	0.5	0.5	0.5
Reduced VAT rate of 9% for central heating (until 30.06.2023)		15.0		
Reduced VAT rate of 9% for natural gas (until 30.06.2023)		46.0		
Increased rate of 40 per cent of the statutory income tax allowance for lawyers	-6.0			

	2023	2024	2025	2026
State aid for regional development – tax relief for corporation tax	-11.0			
Abolition of fees for the use of kindergartens and nurseries	-11.5			
Amendment of dividend policy parameters	-15.4			
Reduced VAT rate of 0% on bread and flour (until 31.12.2023)	-82.7	165.4		
Effect on VAT and excise revenue as a result of exemption from excise duty on electricity, natural gas and LPG – until 01.07.2025	-92.6		92.6	
Increase of the registration threshold from BGN 50 to BGN 100 thousand turnover under the VAT Act	-110.0			
Reduced VAT rate of 9% for restaurant, catering and tourist services, sports facilities (until 30.12.2023), as well as books, baby food, diapers and hygiene products (after 31.12.2023 as a permanent measure)	-243.2	211.5		
Negative effect on import VAT revenues as a result of the adoption of a law to control the implementation of restrictive measures in view of Russia's actions destabilising the situation in Ukraine	-520.0			
Measures in the field of energy	-3 767.8	-692.5		
Total:	**-3 912.0**	**258.9**	**786.9**	**681.9**

Source: MF

4. Sensitivity Analysis and Comparison with the Previous Update

4.1 Alternative scenario

More than a year after the start of the Russian Federation's war in Ukraine, the international economic situation remains uncertain and hard to predict. In the alternative macroeconomic scenario, a possibility of a more unfavorable dynamic of the external demand and a greater drop in prices of international raw materials compared to the baseline scenario is considered. The growth shock to the European and global economies is evident in the second half of 2023, and the trend will carry over into 2024. In the last two years of the forecast period, both EU and global GDP will see higher growth relative to the baseline scenario, but its level at constant prices will remain lower until the end of the forecast horizon. In the considered scenario, the negative effect on the EU economy is stronger, which implies a certain depreciation of the euro against the dollar. Weaker global demand will also lead to relatively lower international commodity prices until the end of 2026. As a result of lower economic activity in the EU and a larger fall in international prices, the ECB is expected to gradually decrease the main interest rate in the second half of 2024. The probability of such a downside scenario to materialize is dictated by the strong increase in interest rates in 2022. High indebtedness and the rising cost of debt service increase the risk of defaulting on current payments to creditors and deterioration of financial stability. This would have a negative impact on the real estate market, construction activity and household consumption.

Table 4-1: Summary of assumptions used in the alternative scenario (deviation from baseline) for the period 2023–2026.

INTERNATIONAL ENVIRONMENT	2023	2024	2025	2026
World economy [real growth, %.]	-0.4	-0.6	0.4	0.1
European economy – EU (real growth,%)	-0.7	-1.1	0.7	0.1
Annual average exchange rate USD / EUR	-4.0%	-2.0%	0.0%	0.0%
Crude oil, Brent/barrel [%]	-2.9%	-8.7%	-2.5%	-2.0%
Metals prices	-0.5%	-1.0%	-0.5%	-0.5%
Agricultural raw materials prices [in USD %]	-0.5%	-6.1%	-0.5%	-0.5%
Food prices [in USD %]	-2.6%	-3.4%	-1.2%	-1.2%
Non-energy raw materials prices [in USD ,%]	-5.4	-2.6	-0.3	2.1
EURIBOR 3m. %	0.0	-0.3	0.0	0.0

Source: MF

Weaker demand in our main trading partners will lower Bulgaria's real GDP growth in 2023 and 2024. In the next two years of the forecast period, economic growth will be slightly higher compared to the baseline scenario. Behind these developments in 2025 will be the stronger external demand, which will have a positive effect on the growth of export of goods and services, while higher investments in fixed capital will account for the most at the end of the period. However, the GDP at current prices will remain below the baseline scenario, partly due to the lower GDP deflator. The weaker growth of companies' revenues from export will have a negative impact on employment and incomes in the country, and hence on consumption. Investments will also be negatively impacted by weaker demand and high uncertainty, especially in real estate and construction. The depreciation of the euro against the dollar in 2023 will raise the prices of imported raw materials and translate into slightly higher inflation compared to the baseline scenario. Over the rest of the period, inflation will be lower in the alternative scenario, due to the expected larger decline in international commodity prices. As a result of the deteriorating terms of trade, the GDP deflator will be lower compared to the baseline scenario throughout 2023–2026. The current account deficit will widen relative to the baseline scenario, following foreign trade dynamics.

A summary of the expected changes in key macroeconomic indicators, as a result of the changes made in the assumptions, are presented in the following table.

Table 4-2: Changes in key macroeconomic indicators (deviation from baseline)

Main macroeconomic indicators	2023	2024	2025	2026
GROSS DOMESTIC PRODUCT				
GDP level at current prices [%]	-0.5%	-1.2%	-1.1%	-1.1%
GDP [real growth, percentage points]	-0.1	-0.5	0.1	0.2
Consumption	0.0	-0.1	0.1	0.0
Gross fixed capital formation	0.5	-1.1	-1.1	1.1
Export of goods and services	-0.7	-1.0	1.0	0.0
Import of goods and services	-0.3	-0.6	0.4	0.0
LABOR AND PRICES MARKET				
Employment (SNA) [%]	0.0%	-0.2%	-0.2%	-0.1%
Unemployment rate [pps]	0.0	0.1	0.1	0.1
Compensation of employees [pps]	-0.1%	-0.3%	-0.4%	-0.5%
GDP deflator [pps]	-0.3	-0.2	-0.1	-0.2
Annual average inflation (HICP) [pps]	0.3	-0.4	-0.3	-0.2
BALANCE OF PAYMENT				
Current account % of GDP [pps]	-0.6	-0.8	-0.5	-0.6
BUDGET SECTOR				
Budget revenues (%)	-0.2	-0.6	-0.5	-0.5
Budget balance % of GDP (%)	-0.1	-0.3	-0.3	-0.3
State debt % of GDP (%)	0.2	0.7	0.9	1.2

Source: MF

4.2 Sensitivity of budget forecasts in different scenarios

The sensitivity analysis presents the change in basic budget parameters that would occur upon realization of the alternative macroeconomic scenario.

In the alternative scenario, GDP at current prices is lower over the period 2023–2026, which has a negative effect on tax revenues and, accordingly, total budget revenues. Lower personal income tax revenues, as well as social security and health insurance contributions, are the main contributors, due to the lower level of compensation of employees in the alternative scenario. Total revenues would decline relative to the baseline scenario by 0.2% in 2023 and 0.6% in 2024. As a result of the change in revenues and the lower level of nominal GDP, the budget balance would worsen by 0.1 percentage points in the current year and 0.3 percentage points for the remainder of the period.

The change in assumptions, the higher budget deficits and the lower level of GDP at current prices will be reflected in an increase in government debt as a percentage of GDP by between 0.2 and 1.2 percentage points.

4.3 Comparison with the previous programme

In 2022, the Bulgarian economy grew by 3.4% with an expected growth of 2.6% in the previous CP. The higher growth was due to stronger-than-expected consumption. Expectations were that weaker growth in real disposable income and increased uncertainty would lead to a more substantial slowdown in household consumption growth.

In the current CP, lower economic growth is expected for the period 2023–2025. The high levels of inflation and the rise in interest rates led to a worsening of the expectations for the growth of the EU economy and, respectively, this also affected the forecasts for the Bulgarian economy.

Employment growth in 2022 was 0.4 pps. lower compared to what was presented in the previous CP. The reason is the significantly weaker integration of the flow of Ukrainian refugees into the Bulgarian economy and their lower participation in employment. At the same time, the unemployment rate for 2022 is 0.7 pps. lower than the value of the indicator in the CP 2022. The high demand for labor in 2022 was met to a much higher extent by unemployed persons than by persons outside the labor force or coming from external labor markets compared to prior expectations.

In the current CP, lower employment growth is predicted in 2023, which is mainly due to the expected lower growth of the Bulgarian economy. The same applies to the growth of employment in 2025, where expectations are underestimated both for the growth of the Bulgarian economy in general and for employment in particular. For employment dynamics in 2025, there are no significant differences between the two convergence programmes.

The unemployment rate for 2023 is lower compared to its value in the previous CP, and its new value reflects the reported values of the indicator in 2022. The same applies to 2024-2025, although in these years the differences in the forecast for the value of the indicator to decrease.

Table 4-3: Main macroeconomic indicators

	2022			2023			2024			2025		
	CP 2023	CP 2022	Difference (pps)	CP 2023	CP 2022	Difference (pps)	CP 2023	CP 2022	Difference (pps)	CP 2023	CP 2022	Difference (pps)
GDP, real growth, incl:	3.4	2.6	0.8	1.8	2.8	-1.0	3.3	3.6	-0.3	3.2	3.4	-0.2
Final consumption	5.2	2.6	2.6	3.0	3.3	-0.4	3.3	3.6	-0.4	3.3	3.7	-0.4
Gross fixed capital formation	-4.3	7.6	-11.9	6.3	9.0	-2.7	12.6	6.0	6.6	6.5	9.9	-3.4
Export of goods and services	8.3	4.1	4.1	1.7	4.0	-2.3	4.3	5.8	-1.5	4.7	4.6	0.1
Import of goods and services	10.5	5.4	5.1	3.9	6.1	-2.2	6.4	6.5	-0.1	5.4	6.8	-1.5
Average annual inflation (HICP)	13.0	10.4	2.7	8.7	5.1	3.5	3.8	2.7	1.1	2.8	2.3	0.5
Employed	1.3	1.7	-0.4	0.4	0.8	-0.4	0.7	1.0	-0.3	0.5	0.6	-0.1
Unemployment rate	4.3	5.0	-0.7	4.1	4.8	-0.7	3.9	4.4	-0.5	3.8	4.2	-0.3

Source: MF, NSSI

The difference with the previous update of the CP regarding inflation dynamics in the country stems mainly from the war in Ukraine, which significantly changed medium term expectations for the international commodity prices. In addition, the euro depreciated against the US dollar by an average of 11% in 2022, against an expected decline of 6.8%, and further strengthened the impact of the rise in international commodity prices in USD on domestic producer and consumer prices. Subsequently, inflation accelerated above expectations in 2022 and the forecast for consumer prices was revised upwards. At the moment, expectations are for a greater increase in food prices, as well as for higher core inflation, which will have a more significant contribution to the overall HICP, especially in 2023.

5. Sustainability of Public Finances

5.1 Policy strategy

This section examines the sustainability of the fiscal position by assessing the current state of public finances in terms of future increases in public spending related to population aging. For this purpose, the sustainability indicators S1 and S2, calculated according to a methodology developed by the EC[22], are used.

The Medium-Term Fiscal Sustainability Indicator (S1) shows the necessary adjustment in the structural primary budget balance within five years after the end of the forecast period (2026 in the case of the MF forecast) to ensure that government debt over a period of t + 15 (2038) does not exceed the reference value of 60%.

The Long-Term Fiscal Sustainability Indicator (S2) shows the necessary adjustment in the primary balance to meet the budgetary time constraint (the discounted value of future structural primary balances to cover the current level of debt) for an infinitely long period of time, including additional aging-related costs.

A positive value of the indicators denotes the need for fiscal consolidation or structural reforms to reduce the burden of aging on public finances, while a negative value indicates the presence of fiscal space.

Table 5-1: Sustainability indicators

	MF		EC	
	S1	**S2**	**S1**	**S2**
Value, of which:	0.1	2.9	-1.4	3.4
Initial budgetary position	3.1	3.8	1.1	2.1
Debt requirement	-2.0		-2.5	
Future changes in the budgetary position	-1.0	-0.9	0	1.3

Source: MF, Fiscal Sustainability Report 2021

The table presents the MF's assessments of sustainability indicators and those of the EC from the Fiscal Sustainability Report of the EC[23], published in April 2022. The differences in the values of indicators S1 and S2 between the two institutions are largely due to different expectations for economic growth, debt and the budget balance in the medium term, as the Commission's estimates are based on forecasts from the autumn of 2021. In addition, the assessment of fiscal sustainability is highly dependent on long-term economic prospects. The differences in S1 and S2 indicators between the two institutions is also due to different expectations for future changes in the budget position, which are related to expenditures on pensions, health care and

22 European Commission (2022). "Fiscal Sustainability Report 2021-Vol1". Institutional Paper 171. - ANNEX A5 Fiscal sustainability indicators

23 European Commission (2022). "Fiscal Sustainability Report 2021-Vol2". Institutional Paper 171.

education. In preparing its long-term macroeconomic forecast and relevant estimates of age-related expenditures, the MF uses updated assumptions set out in the 2021 Aging Report, a forecast of pension expenditure submitted by the National Social Security Institute and estimates of health and education expenditures derived from the MF's long-term model.

Estimates show that debt growth over the forecast period until 2026 could become a risk for the country's fiscal sustainability. The S1 indicator is positive, which according to the EC[24] reference values means moderate risk in the medium term and implies actions for improving the primary structural balance in order to maintain the debt level below 60% of GDP in the medium-term. The value of indicator S2 also indicates moderate risk for fiscal sustainability in the long-term.

Debt sensitivity is also assessed, which presents a set of possible scenarios for the development of the consolidated debt of the General Government sector (referred to as government debt for short in the present analysis) as a percentage of GDP. Based on the sensitivity, the sustainability of the debt is assessed according to criteria developed by EC[25]

Four alternative scenarios are considered, which present the possible effects on the government debt-to-GDP ratio under the following assumptions:

- Historical structural primary balance – it is assumed that after the last year of the medium-term budget forecast (2026), the structural primary balance converges in four years to the average reported in the last 15 years. The aim is to assess whether the baseline scenario is realistic taking into account past fiscal performance;
- Shock on the interest rate and GDP growth – a permanent increase in the implicit[26] interest rate by 0.5 pps. is considered. and a decrease in nominal GDP growth by 0.5 pps. Lower nominal GDP growth could occur both along the lines of lower real growth and along the lines of a lower deflator, i.e. lower inflation.;
- Financial stress – the scenario includes a temporary increase in the implicit interest rate by 1 pp. in the first estimated year;
- Deterioration of the primary budget balance – the scenario considers a higher deficit (or lower surplus) on the primary budget balance by 0.5 pps. of GDP in the first two years of the forecast, after which the resulting balance is retained.

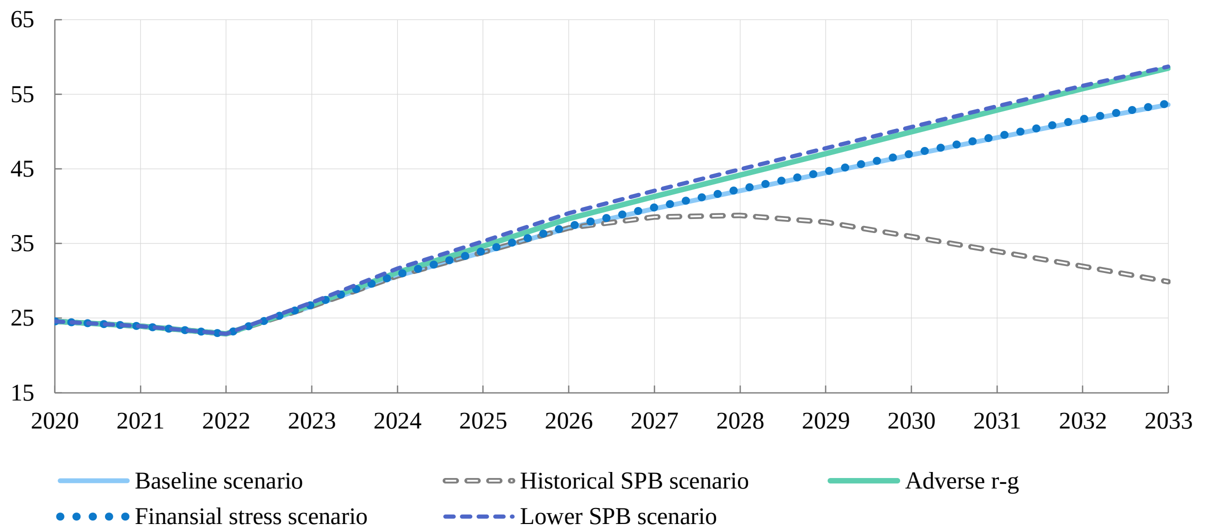
Fan charts are also presented, from which information can be obtained about the uncertainty around the baseline scenario. Historical data on GDP growth, the interest rate and the primary budget balance are used to construct the graphs. Means and the variance-covariance matrix are calculated, which describe the joint normal distribution for these variables. For each of the variables, shocks are generated based on the joint distribution, which are added to the baseline forecasts and used to calculate the distribution of the forecasted debt dynamics. By design, the joint normal distribution of shocks generates a symmetrical fan chart, with risks in the positive direction matching those in the negative direction. Additionally, an adjustment is made by restricting positive shocks to construct an asymmetric fan chart and trace the debt-to-GDP dynamics under a higher probability of negative shocks.

24 $S1<0$ – low risk; $0<S1<2,5$ – moderate risk; $S1>2,5$ – high risk;
$S2<2$ – low risk; $2<S2<6$ – moderate risk; $S2>6$ – high risk.

25 European Commission (2022). “Fiscal Sustainability Report 2021-Vol1”. Institutional Paper 171. - ANNEX A1 Fiscal sustainability analysis: the Commission’s framework

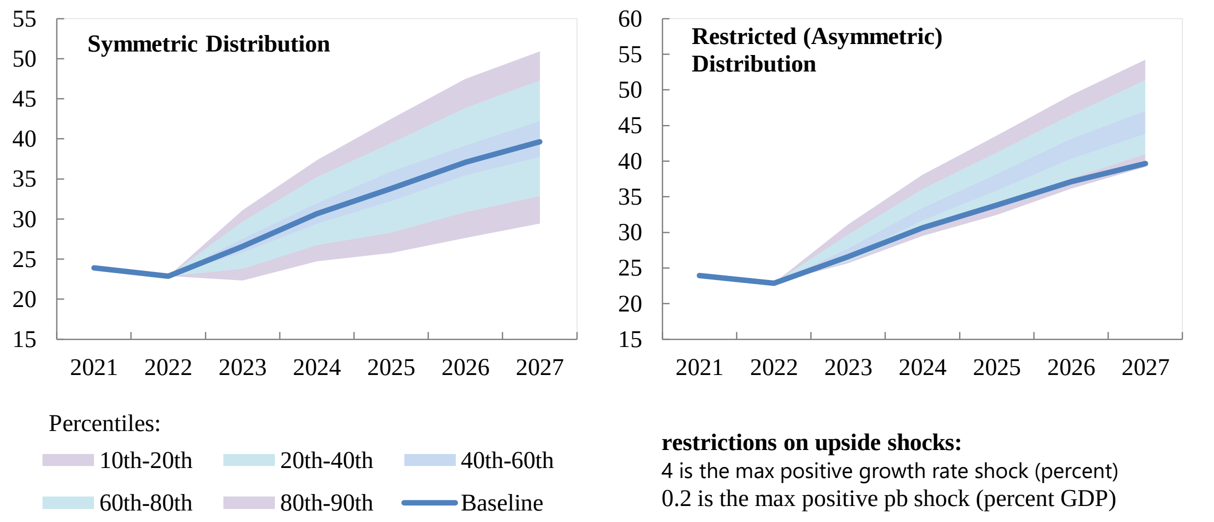
26 An implicit interest rate is calculated as interest expense divided by the previous year's debt level.

Graph 5-1: Government debt % of GDP (four alternative scenarios)



Source: MF

Graph 5-2: Fan-shaped graph for expected Government Debt % of GDP



Source: MF

In the baseline scenario of no policy change[27] the debt-to-GDP ratio continues to rise until 2033, but remains below the 60% mark, furthermore historically in 94.7% of the cases the structural primary balance has been higher than expected on average over the 2027 period -2033, which means that the country should be able to improve its fiscal position. If fiscal policy were to return to historically observed levels, the debt-to-GDP ratio would stabilize over the forecast period and in 2033 it would be 23.7 pps. under the baseline scenario. In the event of a shock to the interest rate and nominal GDP, the ratio at the end of the period will be 4.9 pps. above the baseline scenario. A temporary increase in the interest rate for one year minimally affects the debt to GDP ratio at the end of the period, namely by 0.2 pps. At the same time, a shock to the primary balance would have the most adverse effect and raise the debt-to-GDP ratio in 2033 by 9.2 pps.

[27] In the baseline scenario, the assumption is that the structurally adjusted primary balance before cost of aging remains at the value of the last year of the medium-term budget forecast (2026) for the remainder of the period to 2033

The symmetrical fan-shaped graph shows that there is a 10% probability that the government debt-to-GDP ratio by 2027 will be below 29%, a 60% probability that it will be below 42%, and a 90% probability that it will be below 51%. When adjusted by restrictions on positive shocks, the probability that the government debt at the end of the forecast period will fall below 39% of GDP is 10%, and with a 90% probability it will be below 54%. Overall, with an 95% certainty, debt in 2027 will be higher than in 2022.

5.2 Long-term budgetary perspectives, incl. the impact of the aging of the population

5.2.1 Social security

The long-term budget forecast for the development of the state pension system was developed under the parameters of the legislation in the field of pensions in force as of April 1, 2023 and the provisions of the SSC, in accordance with the assumptions of the spring macroeconomic forecast of the Ministry of Finance of March 24, 2023.

The forecast reflects the changes in the pension sphere adopted by the Law on amending the Law on the State Social Security Budget for 2022 (published in State Gazette volume 51 dated 2022), which have a significant impact on the amounts of pensions both in 2022 and in the long term, including:

- The continued monthly payment of an additional BGN 60 in the first half of 2022. In the period January-June 2022, pensioners for whom the income from a pension in January 2022 (with the "COVID supplement" of BGN 60 included) was less than that in December 2021 (with the "COVID supplement" included " of BGN 120), were compensated by being paid an amount representing the difference between their income in December 2021 and their income in January 2022.
- As of 01.04.2022, according to an amendment in Art. 90a, par. 2 of the SSC, the amount of the social pension for disability is determined in the following percentages of the social pension for old age:
    - for persons with permanently reduced working capacity/type and degree of disability 100 percent with certain foreign assistance – 160 percent;
    - for persons with permanently reduced working capacity/type and degree of disability from 91 percent to 100 percent – 140 percent;
    - for persons with permanently reduced working capacity/type and degree of disability from 71 percent to 90 percent – 130 percent.
- As of July 1, 2022, all work-related pensions granted until December 31, 2021 were updated with 10 percent instead of 6.1 percent (the percentage determined under the rule of Article 100 of the SSC). Additional amounts of BGN 60 paid as of June 30 (the so-called ‘COVID supplements') and individual compensatory amounts representing the difference between their pension income in December 2021 and their pension income from January 2022 were included in the basic amount of the work-related pension received after applying the 10 per percent.
- The minimum old-age pension amount increased from BGN 370.00 to BGN 467.00 as of July 1, 2022 (by 26.2 percent).
- The amount of the social pension for old age increased from BGN 170.00 to BGN 247.00 from July 1, 2022 (by 45.3 percent).
- The maximum amount of one or more pensions received, without considering supplements, increased from BGN 1,500.00 to BGN 2,000.00. (with 33.0 percent) from 01.07.2022, and from October 1, 2022 to BGN 3,400.00. (with 70.0 percent).

- From 1 October 2022, pensions awarded until 31 December 2021 were recalculated on the basis of the average monthly insurance income of the country from which the pension was first granted and the percentage per year of service (accrual rate) set out in the legislation in force at the date of award of the pension. For the period from the grant to the time of the recalculation, a new annual update rule was implemented from July 1 – instead of the sum of 50% of the increase in insurable income and 50% of the consumer price index in the previous year, the higher of the two percentages was applied. When the recalculated amount turned out to be different from the amount as of September 30, 2022, the pension was determined at the higher amount.

In the long term, the following factors will have the strongest influence on the financial condition of the state pension system in Bulgaria:

- Demographic changes represented by the age dependence coefficient;
- Retirement conditions represented by the intra-system dependency ratio;
- The 'generosity' of the public pension scheme represented by the income replacement rate.

Demographically, the Bulgarian pension system is facing serious challenges. The NSI and Eurostat forecasts show that the country's population will continue to decrease, while at the same time its age structure will deteriorate. This will lead to a significant increase in the age dependency ratio. If in 2021, 100 persons between the ages of 15 and 64 corresponded to 34 persons over the age of 65, then in 2070 their number will increase to 54 per 100 persons. The population of working age will decrease and its share of the total population in Bulgaria will shrink from about 64% to about 57%. In turn, the share of the elderly population (65+) will grow from about 22% in 2021 to 30% in 2070.

In the long term, the ratio between the number of pensioners and the number of insured persons will increase. The ratio between the number of pensioners and the number of insured persons, also called the (systemic) dependency ratio, is a key indicator of the financial status of defined benefit pension schemes. The aging of the population and the increase in the average life expectancy on the one hand, and the reduction of the working-age population on the other, have a significant impact on the state insurance system in the long term.

In the long term, the number of insured persons follows the trend in the number of employed, with an increase expected until 2027, followed by a decreasing trend until 2070, which is the result of the decrease in the working-age population, leading in turn to shrinking workforce.

The total number of pensioners with employment pensions paid by the state social insurance (SSI) will decrease in the long term as a result of the increase in legal requirements for access to a pension, as well as due to the negative demographic trends in the country. As a result of the negative natural population growth in the country, however, the relative share of pensioners in the total population of the country will increase from about 29% in 2021 to 35% in 2070.

At the end of 2022, the number of pensioners with a work-related pension was 1,977.4 thousand persons. By 2070, it is expected to decrease to about 1,748 thousand persons.

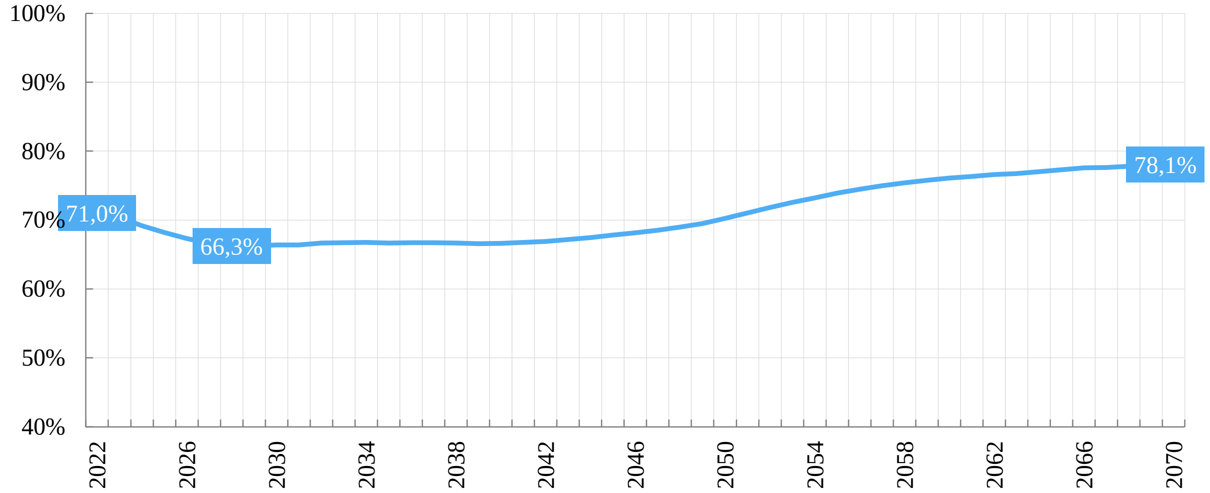
While disability pensioners are expected to continue their decline throughout the period under consideration, retirement pensioners with long-term and old-age pensions will experience a decline until 2040, after which their numbers will begin to steadily increase and increase the demographic pressure on the state pension system. The increase is the result of the influx of the generations born in the 1970s and 1980s into the population of pensioners. Demographic pressure after 2040 will also intensify due to two additional circumstances:

- Firstly, in 2027, the required length of service to acquire the right to an old-age pension ceases to increase. At that point it will reach 37 years for women and 40 years for men.

- Secondly, in 2029 the age of eligibility for the old-age pension for men will reach 65. The age continues to rise only for women (until 2037), when both men and women will retire at 65. At this stage, there is no legally defined mechanism regarding the implementation of the legislation (Article 68, paragraph 5 of the CSO) linking the retirement age to changes in the average life expectancy after 2037, which is why the forecast was developed on the assumption that after 2037, the retirement age remains 65 for both sexes.

These circumstances will lead to a deterioration of the ratio between the number of pensioners and the number of insured persons in the long term.

Graph 5-3: Pensioners with work-related pensions to insured persons (2022–2070)



In 2022, 71 pensioners with work-related pensions corresponded to 100 insured persons. Graph 5-3 shows that the so-called intra-system dependency ratio[28] will decrease, so that in the period between 2027 and 2037, when the retirement age for women and men will equal 65 years, the ratio between the number of pensioners and the number of insured persons will be around 66-67 % This reduction is the result of the projected lower number of newly granted pensions in these years, due to the increase in the retirement age, the limitation of early retirement, as well as the presence of incentives for older workers to stay longer in the labor market. After 2040, under the influence of factors such as population aging, increasing average life expectancy and decreasing number of employed persons, the ratio between the number of pensioners and the number of insured persons will begin to increase, reaching 78.1% in 2070.

The pension policies carried out in recent years contributed to increasing the adequacy of pensions.

In the period 2022-2026, pension amounts will grow significantly. In 2022, the gross income replacement rate[29] reached 51.9%. As a result of the pension policies implemented in 2022, in the next few years the gross income replacement rate is expected to reach around 56-57%, and these are also its highest values for the entire period under consideration.

[28] The ratio between the number of pensioners with work-related pensions and the number of insured persons.

[29] The rate of the average pension for employment to the average insurance income of the insured persons for the relevant calendar year.

In the long run, the average value of the income replacement rate will decrease to about 37.0%. The most significant influence on this process is the legislative requirement for the reduction of the individual coefficient of pensioners who will be granted a pension from both the State social security fund (first pillar) and the universal pension fund (second pillar)[30]. The income replacement rate by State social security fund will be lower for pensioners who are insured in both pillars. Their pensions will be reduced according to the percentage of the insurance contribution that was transferred to the second pillar, taking into account the number of months during which the person was insured in a universal pension fund in relation to the total length of his insurance service. These persons will receive an additional old-age pension from a universal pension fund. The reduction in the amount of first-pillar pensions granted to women born at the beginning of 1960 who become entitled to a pension for length of service and age in 2023 is about 10.0 percent. This percentage will increase to around 25 per cent for pensions granted after 2050, as the entire pensionable service of those who will then retire will cover periods after 2001 with provision in a universal pension fund. It is important to note that the value of the reduction is different for each individual pensioner and depends on the specific period that covers his insurance experience.

The rule for updating pensions under Art. 100 of the SSC, according to which the modernization is carried out at a rate equal to the sum of 50% of the increase in the insurance income and 50% of the harmonized index of consumer prices in the previous calendar year, also contributes to the reduction of the income replacement rate.

The dynamics in pension costs are directly dependent on the dynamics in the system dependency ratio and the income replacement rate.

In 2022, pension expenditures reached 9.5% of GDP without the additional amounts to pensions and 10.0% of GDP with additional amounts included[31], which were not foreseen in the 2022 Law on the Budget of the State social insurance. In 2023 and 2024, the expenditures for pensions will exceed 10.0% of GDP, and in 2025 and 2026 they will reach their highest value for the entire forecast period of 11.0%. After 2026, pension expenditure as a share of GDP will begin to gradually decline, reaching its lowest value of 9.1% in the period 2042-2050, after which it is expected to rise to 9.5% at the end of the forecast period. The reasons for the reduction in pension costs as a percentage of GDP in the period 2027-2050 are complex and can be summarized in two groups: 1) reducing the number of pensioners and keeping the ratio between the number of pensioners and insured persons at relatively low levels – mainly due to demographic reasons and the stricter conditions for acquiring the right to a pension; 2) anticipatory growth of the average insurance income compared to the average pension, due to the applied mechanism for updating pensions and the reduction of the pension of persons who were insured in both pillars at the time of their retirement.

Long-term pension costs will also be affected by the opportunity granted to insured persons born after 1959, who until August 2015 were mandatorily insured in the state social insurance (I pillar) and in a universal pension fund (II pillar), to change their insurance and switch to insurance only in the first pillar with an increased insurance contribution. At the end of 2022, 93,543 insured persons have transferred entirely to the first pillar, of which 36,721 persons have

[30] Since 2002, persons born after 1959 are insured for a second pension in universal pension funds, and for them 5% of the pension insurance contribution is redirected to the second pillar.

[31] These are the amounts paid to pensions in the first half of 2022, the funds for which were transferred to a foreign funds account of the NSSI and reported as an expense for 2021:

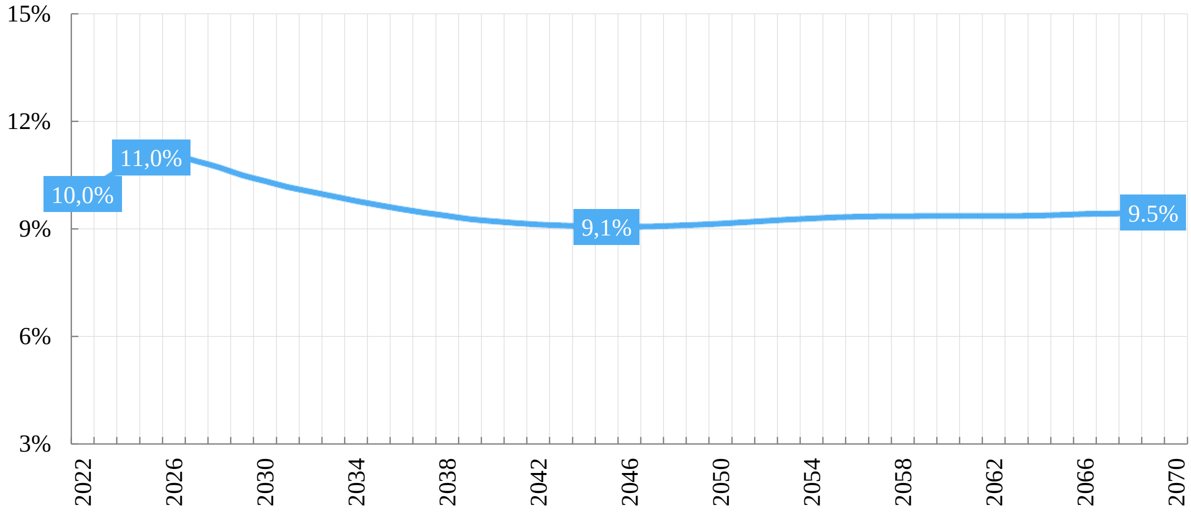
– BGN 750.0 million for the payment of additional amounts of BGN 60. to the pensions of all pensioners for the period January-June;

– BGN 100.0 million for the payment of a lump sum of BGN 75 for pensioners vaccinated against COVID-19.

already received a pension in full amount from the Social security insurance (1.8% of all pensioners with pensions granted at the end of 2022), and the remaining 56,822 persons (2.2% of all persons insured by the end of 2022) continue to be insured and accumulate pension rights.

The following graph shows the results of the long-term forecast for the costs of pensions paid by the state social insurance for the period 2022-2070.

Graph 5-4: Pension expenditure as % of GDP (2022-2070)



Fiscal pressure on the state pension system is strongest at the beginning of the period as a result of the changes in pension amounts adopted by the Law on Amendments to the Law on the Budget of the State Social Insurance for 2022, which lead to a significant improvement in their adequacy. In the long run, the effect of population aging and higher life expectancy will be largely offset by lower first-pillar income replacement rates for those who were insured in both pillars. Since these persons will also receive a second pension from the universal pension fund, the future adequacy of pensions will depend largely on the replacement rate that will be achieved by the second pillar.

5.2.2 Health care

In the long run, the share of total health expenditure is expected to reach 5.1% of GDP in 2050 and then slightly decrease to 5% in 2070. A similar trend is expected in the 2021 Aging Report. Long-term health care costs are based solely on the population forecast. Such a scenario is very restrictive. It does not imply a change in the policy of public spending on health in the context of expanding budget-funded health services. Also, according to many econometric stud- is, technical progress and other non-demographic factors are among the main reasons for rising health care costs in developed countries. For this reason, in addition to the baseline report, the 2021 Aging Report examines 11 other scenarios for the development of health care expenditures related to different demographic and economic dynamics. Their expenditures in Bulgaria in the period 2019–2070 increased by 0.2 percentage points to 2.2 percentage points, with the largest increase in a scenario involving factors other than demographic such as innovations in medical technology.

Table 5-3: Health expenditure[32] % of GDP

	2019	2030	2040	2050	2060	2070
MF	4.6	4.8	5.0	5.1	5.0	5.0
Report 2021	4.9	5.1	5.3	5.5	5.4	5.4

Source: MF, Aging report 2021

5.2.3 Education

Table 5-4: Education expenses % of GDP

	2019	2030	2040	2050	2060	2070
MF[33]	3.8	4.1	4.0	4.2	4.4	4.2
Report 2021	2.9	3.1	3.0	3.2	3.4	3.3

Source: MF, Aging report 2021

The MF forecast of public expenditure on education is based on the long-term demographic forecast and the assumption that expenditure will be indexed with the growth of nominal labor productivity. In the period after 2040, the stabilization of the demographic dynamics of the under-18 populations is expected to lead to a smooth increase in total education expenditure.

5.3 Contingent liabilities

Guaranteed debt of the “General Government” sector at the end of 2022 is expected to amount to BGN 590.2 million or 0.4% of GDP, marking an increase in nominal terms compared to the level reported at the end of 2021 (BGN 556.1 million or 0.4% of GDP). The increase is a consequence of the regular operations performed on the guaranteed loans.

The guaranteed debt of the "General Government" sector is mainly formed by the guarantees issued by the "Central Government" sub-sector with a share of 99.9%. Subsector "Local Government" takes about 0.1%, and units from the subsector "Social Security Funds" cannot issue guarantees.

In 2023, until the adoption of the State Budget Law of the Republic of Bulgaria for 2023 by the National Assembly and assumption of the issuance of the new government guarantees provided for in the Law on the Application of Provisions of the 2022 State Budget of the Republic of Bulgaria Act , the 2022 Public Social Insurance Budget Act and the 2022 NHIF Budget Act[34] intended to support strategic projects in the energy sector, for energy efficiency and the green transition of SMEs and in line with EU instruments, as well as disbursements from the loans in full in 2023, the nominal amount of the "General Government" guaranteed debt is expected to increase, reaching in nominal terms up to BGN 2.4 billion, and as a ratio to the estimated GDP to amount to about 1.3%.

At the end of 2023, the dominant share with 53% in guaranteed debt structure by sectors is expected to be occupied by the guarantees of the "Energy" sector, followed by the guarantees under new loan agreements of the Bulgarian Development Bank EAD in the amount of up to

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32 The values from the aging reports are the sum of health care costs and long-term care costs. The Report's forecasts are based on data from the System of Health Accounts, while the MF's forecasts are based on COFOG expenditure data.

33 Classification of the functions of government (COFOG)

34 Published in State Gazette, volume 104 dated 30.12.2022 г., entered into force on 1.01.2023 г.

BGN 700.0 million with share of 30%. Guarantees issued under the EU instruments created as a result of the outbreak of COVID-19 – SURE and the Pan-European Guarantee Fund, as well as in connection with the proposal of the EC on the provision of EU macro-financial assistance to Ukraine in the form of grants and loans, take a share from 14%. The remaining 3% take the guarantees provided in accordance with the Law on Students and Doctoral-candidate Loans Act, under other implemented international agreements and issued municipal guarantees.

In the following years of the forecast period, their gradual reduction to 1.1% of GDP by the end of 2026 is assumed, as a result of the expected improvement in 2025–2026 of economic activity, both in Bulgaria and in the EU, the assumptions for GDP growth in nominal terms, as well as the planned service of the guaranteed loans, in accordance with the agreed repayment schedules.

In accordance with item 1.7 of Decision No. 70/ January 27, 2023 of the Council of Ministers for the budget procedure for 2024 and in connection with Art. 73, item 8 of the PFL, all state and municipal enterprises with a total amount of liabilities as of 31.12.2021 exceeding 0.1% of the country's Gross Domestic Product, which are not part of the consolidated fiscal program, are subject to monitoring and do not fall under the scope of the "General Government" sector. They should present information and an assessment of the forecasts for income and expenses and for assets and liabilities with reporting data for 2021 and 2022, an estimate for 2023 and a forecast for the period 2024–2026.

Based on the information received, for the four-year period 2023–2026, a reduction of the liabilities of the state-owned companies from the non-financial sector, subject to monitoring, by 21.84% is predicted. The reported amount of long-term and short-term liabilities of these companies as of 31.12.2022 is a total of BGN 11.4 billion, and as of 31.12.2026, the forecasts for the same amount to BGN 8.9 billion.

The total indebtedness ratio decreases from 0.75 as of 31.12.2022 to 0.48 at the end of the period. The combined debt-to-asset ratio of these companies decreased by 0.10 over the forecast period to 0.32. The liquidity ratio remains stable at a level of over 1.7 throughout the period 2021–2026.

6. QUALITY OF PUBLIC FINANCE

6.1 Policy strategy

The strategy of the policy in the field of the quality of public finances follows the consistent actions for institutional, legislative and methodological changes in the direction of improving the management of public finances.

The achievement of a sustainable medium-term fiscal framework and its implementation are related to the implementation of a number of measures to increase the quality of public finances, expressed in the improvement of the budget process, improvement of budget documents, confirmation of the application of good budget practices and monitoring of the effects of the conducted sectoral policies by monitoring the key indicators to measure progress in terms of the implementation of the strategic goals of the policies and the achievement of the expected benefits/effects for society.

Despite the challenges on a global scale and the lack of a regular government at the moment, efforts continue to achieve a better connection between the financing of the implemented policies and the achieved results of their implementation.

In recent years, the practice of including information on key indicators for measuring the degree of achievement of the goals of the policies carried out by the executive authorities in the medium-term budget forecast and in its update has been established.

In the medium term, it is expected that the accumulation of information on the defined key performance indicators will contribute to the creation of a sustainable basis for monitoring and tracking trends, as well as for assessing the relationship between the strategic objectives of budget organizations and the policies/budget programs implemented by them.

Regardless of the established permanent regulation of the budget framework with the adoption of the PFL in 2013, efforts continue to improve the regulatory framework in the area of the budget, which are accompanied by monitoring and analysis of the implementation of budget legislation and budget practices, as well as and compliance with fiscal rules.

The legal framework for program budgeting requires the government to maintain an up-to-date program classification, approved by the Council of Ministers, that corresponds to the functions of the central administration and the portfolios of the executive authorities that carry out policies, therefore the program classification was updated according to the current statutory arrangement.

The quality of public finances is built on the basis of the developed macroeconomic and budget forecasts in support of the prudent fiscal policy pursued by the government, and for this purpose a corrective is necessary – an independent body which, through its functions, promotes the sustainability of the budget framework, and also monitors the compliance with fiscal rules, as well as the availability of corrective mechanisms in case of deviations from the set goals.

The strengthened framework for fiscal governance within the EU expanded the role and formalized the tasks of national independent fiscal institutions, which found a place in national legislation. The effective interaction of the Ministry of Finance with the Fiscal Council in the preparation of the main budgetary documents contributes to increasing the quality and reliability of information and data based on the Fiscal Council's analyses, assessments and recommendations. The Council also contributes to increasing accountability and improving fiscal transparency by monitoring compliance with numerical fiscal rules and by indicating the presence of potential risks to the budget.

The accession of the Republic of Bulgaria to the Organisation for Economic Development and Co-operation (OECD) is a cause of great importance for the country, since the scope of this organization covers almost all aspects of socio-economic life.

On 10 June 2022. The OECD formally launched accession talks with Bulgaria by approving a Roadmap with the parameters, stages and conditions of the accession process in the framework of the annual OECD Council meeting at ministerial level. Given the need for our country to assess the compliance of its laws, policies and practices with the OECD best standards and subsequently to work out ways to improve them in line with the recommendations made by the individual Committees, the participation of lead and/or partner institutions on the OECD legal instruments was identified. The prepared self-assessments were sent to the Inter-Ministerial Coordination Mechanism for the organisation and coordination of the process of talks and preparatory activities for the accession of the Republic of Bulgaria to the OECD and were included in the Initial Memorandum. Preparations were also made for the participation of the various institutions in OECD committees/working bodies in relation to the technical reviews in the framework of the accession process.

In recent years, Bulgaria joined a number of OECD legal instruments and intensified its participation in an increasing number of OECD committees and working groups, with our country's efforts aimed at maintaining an active position and bringing added value to their work. At the moment, Bulgaria participates with the status of "member"/"associate member" in the activities of 13 working bodies, in 6 other bodies it has the status of "participant", and in 19 other bodies it is a "guest"/"observer" Our country has joined to 32 legal instruments and has requested accession to 6 more.

In terms of public financial management, one of the key recommendations of the OECD Council is in terms of the principles of budgetary governance "OECD Council Recommendation on Budgetary Governance (2015)", which is also enshrined in the relevant legal instrument, to which Bulgaria has acceded, has prepared a self-assessment of the compliance of legislation, policies and practices.

It should be noted that Bulgaria's 2019 Budgeting in Bulgaria review, which was published on the official OECD website in Issue 2 for 2021 of the OECD Journal on Budgeting, was also based on an assessment of the degree of compliance with the OECD Council Guidelines on Budgetary Governance, which represents a comparison with established international standards and best practices in the budgeting and fiscal management process.

Bulgaria has participated in the "Open Budget Survey" of the International Budget Partnership since 2006, when it scored 47 points, and over time our country has seen a significant improvement in its score, reaching 71 points in 2019 and 2021, which is also the average value for OECD member countries. The country thus remains in the second group of countries in the index scoring between 60 and 80 (out of a maximum of 100), considered to provide "significant information" about the budget.

The Open Budget Index is the only international independent comparative study of budget transparency that assesses the extent to which governments in 117 countries around the world provide the public with timely and detailed budget information. The index covers the procedures for drawing up, adopting, implementing and reporting the budget and the responsibilities of other institutions such as the Court of Auditors and the legislature in the budget process.

In general, the Government of Bulgaria provides a significant amount of information through the eight types of key budgetary documents that are the subject of the evaluation. Undoubtedly essential to the progress made in recent years is the preparation and publication of a "Budget for Citizens" at various stages of the budget process.

The assessment for budget supervision is 61 points (out of a maximum of 100), and the indicator assesses the functions of the legislative and supreme audit institutions to ensure monitoring in relation to the budget.

Regarding public participation in the budget process, our country achieved a score of 26 points (out of a maximum of 100), where this indicator assesses the formal opportunities provided to the public to participate in various budget initiatives.

6.2 Composition, effectiveness and cost efficiency – COFOG

Table 6-1: Budget expenses by functions

	% of GDP		% of total budget expenses	
	2021	2026	2021	2026
1. Total state services	3.5	4.2	8.6	10.7
2. Defence	1.6	1.7	4.0	4.4
3. Public order and security	2.7	2.1	6.6	5.3
4. Economic Activities	6.7	5.9	16.5	15.0
5. Environment Protection	0.8	0.5	1.9	1.2
6. Residential construction, improvement and communal economy	1.0	0.7	2.4	1.9
7. Health care	5.8	5.4	14.4	13.7
8. Recreation, culture and religion	0.9	0.6	2.2	1.4
9. Education	4.3	3.9	10.6	9.9
10. Social Defense	13.4	14.4	32.9	36.5
11. Total expenses	40.6	39.4	100.0	100.0

For the period 2021–2026, a decrease of 1.2 percentage points is expected in the total expenses of the "State Government" sector of GDP. This is largely due to the drop in spending undertaken in 2021 to prevent the spread of COVID-19, for its treatment, measures to support businesses and to reduce the negative effects of the pandemic, which led to an increase in spending on the functions " Health care' and 'Economic Activities' in 2021.

For the period 2021–2026, expenditure under the function "**General government services"** is expected to grow from 3.5% of GDP in 2021 to 4.2% in 2026. The increase is related to the increase in interest expenses of the sector "General government", which according to the COFOG methodology are reported in this function.

Defense spending increased as a share of GDP from 1.6% to 1.7%. This includes the means for maintaining and developing national defense capabilities and capabilities related to collective defense, including funds for the implementation of the investment projects approved by the National Assembly for the modernization of the Bulgarian Army, namely: the acquisition of a multi-functional modular patrol ship for the Navy, a new type of combat aircraft – II stage, plus associated costs in the two stages of implementation (transportation, VAT and customs duties) and basic combat equipment for the construction of battalion combat groups from the composition of a mechanized brigade. Additionally, funds are provided for the acquisition of ammunition and fuel for combat training, as well as for the acquisition, modernization, maintenance and repair of armaments, rockets, torpedoes and equipment, and the repair and construction of infrastructure.

Expenditures under the function "**Public order and security**" decrease as a share of GDP from 2.7% in 2021 to 2.1% in 2026. This functional group includes expenditures for activities to counter serious crimes against the person and property of citizens, border control and protection of the state border, combating illegal migration on the territory of the Republic of Bulgaria and strengthening control over the establishment of illegally staying citizens on the territory of the country, ensuring fire safety and protection of the population in the event of fires, disasters and other emergency situations, etc.

Expenditure under the “**Economic Activities”** function decreases from 6.7% of GDP in 2021 to 5.9% of GDP in 2026. The function includes state-owned enterprises that are part of the General Government sector and eliminates expenditure related to European funds, including the resources for the implementation of the National Recovery and Resilience Plan, which, according to the ESS 2010 methodology, have no impact on the revenues and expenses of the "State Government" sector.

Expenditures under the "**Environmental protection**" function fell from 0.8% to 0.5% of GDP during the period under review. The costs of the function include measures in the field of protection and use of the components of the environment; the national system for environmental monitoring and information security; to improve the investment process, maintain, modernize and build the technical infrastructure related to the implementation of geoprotective measures and activities to limit landslides, erosion processes along the Danube coast and abrasion processes along the Black Sea coast and to prevent accidents and damage, as well as the activities on the registration and monitoring of landslide areas.

Expenditures under the function "**Housing construction, improvement and communal economy"** decrease from 1.0% of GDP for 2021 to 0.7% for 2026. This function includes the costs of management, control and regulation of housing construction and territorial development activities. The costs for the implementation of the National Program for energy efficiency of multi-family residential buildings are also included within the scope of this function. Another priority area includes activities for the management, maintenance and construction of the water infrastructure in the country, as well as activities related to the design, construction, operation and maintenance of national roads.

Expenditures under the "**Health care**" function decrease from 5.8% of GDP in 2021 to 5.4% of GDP in 2026. Expenditures under the function include measures to protect citizens' health; ensuring financial stability and security of the health system through a long-term, sustainable and predictable funding mechanism based on health outcomes; increasing the quality and accessibility of health services; ensuring health protection for children, pregnant women and persons with physical disabilities and mental disorders; development of emergency aid and emergency response capacity; better planning and motivating the health care workforce; development of electronic healthcare and digitization of the healthcare system.

For the period 2023–2026, additional funds in the amount of BGN 142.6 million per year have been allocated to the function to strengthen the personnel capacity and financial sustainability of the reached level of pay for the staff in the Regional Health Inspections and Emergency Medical Assistance Centers, as well as for the financial provision of the minimum basic salaries for the medical staff agreed in 2022 in the collective labor agreement for the "Healthcare" sector.

According to the municipal budgets for the period 2023–2026, additional funds in the amount of BGN 119.8 million have been allocated for the activities delegated by the state under the "Healthcare" function, in order to ensure the introduction of free nurseries from April 1, 2022 and the taking over of their support from the state and in connection with the increase in the amount of the minimum wage. Additional funds are also provided for an increase in the remuneration of the pedagogical staff in the nurseries and the related increase in the insurance contributions at the expense of the employer.

Expenditure under the "**Recreation, Culture and Religion function**" decreases from 0.9% of GDP in 2021 to 0.6% of GDP in 2026. This function includes measures in the area of protection of movable and immovable cultural heritage, where main priorities are preservation and socialization of cultural heritage and stimulation of its connection with tourist products, attraction of project financing in the field of culture under various programs and donors, development and technical improvement of the museum network, attraction of funds from European programs and bilateral agreements to support culture and establishing Bulgaria as a destination for the implementation of international cultural projects. This spending function also includes policies in the field of sports for students and sports in free time, as well as in the field of bringing sports sites and facilities into a state that meets modern international requirements and standards.

Expenditures under the "**Education**" function fell from 4.3% to 3.9% of GDP during the period under review, including measures aimed at implementing policies in preschool and school education, effective socialization of children from early childhood, ensuring equal access to quality education, personal development of children and students, promotion of innovations, qualification of pedagogical specialists, modernization of educational institutions, digitization of education. Under this function, additional costs are foreseen for increasing the salaries of pedagogical specialists in connection with the policy of increasing their incomes up to a level of 125 percent of the average salary for the country, as well as costs for the gradual expansion of access and coverage in compulsory preschool education of 4-year-old children; to increase interest and increase extracurricular activities; to compensate for the costs of raising and educating children who are not accepted due to lack of places in state and municipal kindergartens and schools; for an increase in the remuneration of academic staff in state higher education institutions, etc.

Expenditure under the "**Social Protection**" function increase significantly – from 13.4% of GDP in 2021 to 14.4% of GDP in 2026. The increase in spending on this function is associated with an increase in pension and social assistance costs. In the case of pensions, the increase is mainly due to the annual indexation from July 1 of the relevant year according to the Swiss rule, as well as the 10% increase in pensions implemented in 2022 from the first of July, recalculation of pensions for work-related activity and an increase in the maximum pension from first of October, which have an impact on costs in the following years as well. The increase in terms of benefits and benefits for households is chiefly a result of the increase in social benefits under the Social Assistance Act and the Disability Act, due to the increase in the poverty line for the country, as well as the projected increase in the unemployment benefit, which accordingly leads to an increase in the hourly rate for work done to calculate personal assistants' allowances under the Personal Assistance Act and foster families' allowances under the Child Protection Act.

6.3 Structure and efficiency of revenue systems

6.3.1 Tax policy and legislation

The tax policy of the Republic of Bulgaria is oriented towards ensuring macroeconomic and budgetary stability in the medium and long term, as well as the necessary financial resources for the implementation of the government's expenditure policies. Tax policy is characterized by predictability, while encouraging business development, investment activity, stimulating innovation, energy efficiency and employment. At the international aspect, the country's tax policy is aimed at supporting the functioning of the European Union's single market, the successful implementation of the digital transformation of the European society and economy in, as well as the activities to address climate and environmental issues.

The 2023 fiscal discretionary measures include emergency legislative changes to support citizens, businesses and employment in response to the spread of the COVID-19 pandemic. Some of these measures, such as the extended period for declaration under the CITL and the reduced VAT rate for certain goods, were made permanent through changes in the relevant tax laws. In response to the challenges related to the high prices of energy and basic food products, a package of anti-crisis measures was introduced in 2022, some of which continue to operate in the period 2023–2025. It is assumed that the economic recovery in Bulgaria is taking place simultaneously with the same processes internationally.

Adhering to the principles of fairness and efficiency, the tax system is developed in a way that favors growth and ensures a budget revenue increase. In this regard, the objectives and measures of the tax policy to limit tax fraud, to prevent tax evasion, to deal with the shadow economy and to reduce the administrative burden and costs for businesses and citizens play an important role.

For the period 2023–2026, tax policy will continue to adhere to the principles and guidelines established in recent years, with its main objectives again aimed at maintaining economic growth, improving the business environment, combating tax abuse, as well as improving fiscal sustainability in the long term. The main priorities related to the improvement of revenue collection, the prevention of opportunities for evasion and non-payment of taxes and insurances and the reduction of the administrative burden and costs for businesses and citizens are maintained.

During the period 2023–2026, the Ministry of Finance will continue to actively participate in the EU structures and activities and in OECD initiatives in the field of taxes and administrative cooperation. Work continues with regards to the participation of the Republic of Bulgaria in the activities for the introduction of the four minimum standards already agreed by the OECD. The same could be said with regards to other elements of the package of measures under the "Shrinking the tax base and the transfer of profits" (Base Erosion and Profit Shifting – BEPS) Project, in connection with the Republic of Bulgaria's accession to the OECD's Inclusive Framework for the introduction of measures under the project for narrowing the tax base and the transfer of profits (Protocol No. 13.37 of the meeting of the Council of Ministers on March 30, 2016). The introduction of the minimum standards is also related to the fulfillment of Bulgaria's obligations as an EU Member State.

Throughout the period, Bulgarian experts will continue to participate in the activities related to the discussion, analysis and impact assessment of the measures planned by the OECD to deal with the tax challenges caused by the digitalization of the economy and unresolved problems related to the transfer of profits: Pillar 1 (redistribution of tax rights) and Pillar 2 (minimum taxation of the profits of multinational enterprises). The reform is expected to provide an increase in corporate tax revenues, a significant reduction in profit shifting and an increase in tax certainty.

The leading priority actions of the EC to address the challenges related to the climate and the environment implies Bulgaria committing itself to take measures in the tax legislation to achieve the goals set by the European Union in areas such as the taxation of energy products and promoting the use of environmentally friendly vehicles.

Throughout the period 2023–2026, the implementation of a policy aimed at increasing revenue collection and achieving the set budget goals remain primary goals. In order to fulfill the priority objectives of the tax policy, regulatory changes and actions of the revenue administrations in the field of collection and control are carried out. Many of the measures to improve revenue collection in the area of tax policy are of a permanent nature, they are included in the strategic documents that each of the responsible institutions develops and implements and will continue to be implemented throughout. The main tools for minimizing losses from tax revenues not received in the budget are the interaction of institutions and the exchange of information on a national and international scale, as well as the reduction of the administrative burden and costs for businesses and citizens.

The main measures of a permanent nature include: VAT refund mechanism for supplies of goods and services; Implementation of fiscal control over the movement of goods with a high fiscal risk (SVFR); Mechanism for repayment of public obligations of persons with receivables from municipalities, other departments or state-owned enterprises under public procurement contracts and those awarded in implementation of EU operational programs; Constant monitoring of debtors with arrears above a certain amount; Encouraging voluntary compliance with legislation; Control over the supply and movement of liquid fuels; Reducing the administrative burden.

– Legislative changes

In order to increase budget revenues and combat tax fraud, measures are undertaken to improve compliance with legislation, prevention and countermeasures against tax fraud and tax evasion.

In order to solve the problem of VAT fraud in e-commerce by strengthening cooperation between tax authorities and payment service providers, as well as in relation to the provisions introduced by Council Directive (EU) 2020/284 of 18 February 2020 on the requirements for payment service providers, relevant amendments have also been made to the Value Added Tax Law (VATL) (Law amending and supplementing the VATL, promulgated, SG volume 102 of 23.12.2022, in force from 1.01.2023).

Regarding excise taxation of tobacco and tobacco products, an excise calendar for a gradual increase in rates over a period of four years has been introduced in the Law on Excises and Tax Warehouses – effective from March 1, 2023.

A temporary solidarity contribution has been introduced. The changes in the TFP of the CITL regulate the order and manner of implementation of Chapter III of Council Regulation (EU) 2022/1854 of October 6, 2022 on emergency intervention to address high energy prices. The adopted provision regulates the rules for the temporary solidarity contribution, which should be paid for the surplus profits generated by the companies and places of business from the Union, operating in the crude oil, natural gas, coal and oil refining industries.

Increased is the range of incomes for which information is provided with the reference under Art. 73, para. 1 of the Personal Income Tax with certain non-taxable incomes (Law amending and supplementing of the Personal Income Tax Law, promulgated, SG volume 102 of 23.12.2022, in force from 1.01.2023). Added, regardless of their size, are the incomes from supplementary pension insurance, business trip money and other income, which, although they are exempt from taxation, are regularly received by individuals and are important for the correct determination of disposable income. The threshold above which the obligation to provide arises has been changed (from BGN 5,000 to BGN 500), in relation to gambling income, as well as income from interest on deposits and bonds. Added are the various benefits of social assistance, state and national awards, scholarships (except for scholarships that are provided by schools for the benefit of students and pupils), annuities and consumer dividends.

Local individuals are given the opportunity to declare in the annual tax return the income acquired during the year that is exempt from taxation by virtue of the law, the acquired income taxable with a final tax, the property received by inheritance, bequest and donation, as well as the property received with a refund right of ownership according to the order of a normative act. Until the change, incomes subject to final tax were not included in the annual tax return under Art. 50 of the VATL, regardless of the wishes of the persons.

Changes have been made to remove existing deficiencies in Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and to clarify in this regard the national laws of the Member States in an unambiguous manner, which in turn guarantee legal certainty and clarity of rules in the field of administrative cooperation and exchange of information. At the same time, the digitalization of the economy and the development of possibilities of hiding income, especially in cases where the activity is carried out through digital platforms established in other jurisdictions, motivates the expansion of the scope of the automatic exchange of information for tax purposes in relation to income realized through such platforms, and their recipients. In connection with this and in accordance with the requirements of Directive (EU) 2021/514, the adopted changes in the Law amending and supplementing the Tax and Social Insurance Procedural Code (promulgated, SG volume 100, dated 16.12.2022, effective from 1.01.2023) improve the overall regulation of information exchange and administrative cooperation and expand the scope of automatic information exchange, including the information provided by the operators of digital platforms for sellers conducting business through those platforms.

Other changes in the area of administrative cooperation include the creation of the possibility of the presence of officials of a Member State during administrative proceedings in another Member State, as well as the clarification of the current provision on parallel checks, providing for a 60-day deadline for answering by the questioned authority when a proposal is made to carry out a parallel inspection. Rules have been established regarding joint audits and inspections between two or more Member States. The provisions of Art. 143 and the created new art. 143l "Joint revisions and inspections" of the Tax and Social Insurance Procedural Code shall enter into force on January 1, 2024.

To improve the business environment and reduce the administrative burden and costs for businesses and citizens:

The amount of the threshold for mandatory VAT registration has been increased from BGN 50,000 to BGN 100,000 with the amendment to Art. 96, para. 1 of VATL (Law amending and supplementing the VATL, promulgated, SG volume 58 of 23.07.2022). The change is effective from 01.01.2023. The EU decision to allow the Republic of Bulgaria to introduce a derogation from Council Directive 2006/112/EC of November 28, 2006 on the common system of VAT was adopted by the EU Council on November 14, 2022 and was published in the Official EU Journal of 17.11.2022 (L 297/69).

In accordance with the decisions of the Court of the European Union, changes have been made to VATL to reduce the tax base of the supply in case of full or partial non-payment, which may become uncollectible, in view of the possibility provided for in the provision of Art. 90, paragraph 1 of Council Directive 2006/112/EC of 28 November 2006 on the common system of VAT (VAT Directive). The change in VATL was introduced with the Law amending and supplementing the law, promulgated, SG volume 102 of 23.12.2022, in force from 1.01.2023.

The range of VAT-exempt supplies has been expanded with the addition of the activity of managing alternative investment funds. The new provision introduced in Art. 46, para. 1 of the VATL treats the management of alternative investment funds, defined as special investment funds, in accordance with the criteria established by the EU law, as an exempt supply.

Pursuant to the adopted § 5 of the Law amending and supplementing the VATL amending Art. 66a of VATL (SG, volume 102, dated 23.12.2022, in force from 1 January 2023), reduced tax rates (from 20% to 9%) for the supply of books (including textbooks, reference books and study sets, children's illustrated, drawing or coloring books, printed or manuscript sheet music publications), other than publications which are wholly or mainly intended for advertising and other than publications which consist wholly or mainly of video content or audio-musical content), of food suitable for babies or young children and baby diapers and similar hygiene articles under Annex No. 4 of the Law are established as a permanent measure. The period of validity for the reduced tax rate for restaurant and catering services and for the supply of a service for the use of sports facilities has been extended until 31.12.2023. The same is applicable to the period of validity of the zero VAT rate for supplies of bread and flour (§ 38 of the Law amending and supplementing the VATL for the amendment of § 15e of the TFP of VATL).

In order to reduce the administrative burden in relation to taxable persons who are declared in liquidation, it is proposed that if these persons have chosen to remain registered for VAT until the date of their deletion from the commercial register, they should not submit an application for deregistration on the date of their deletion. The termination of the VAT registration of these persons is already carried out ex officio by the revenue authorities.

A change has been made to the term for the provision of collateral for trading in liquid fuels. The amendment enables persons to promptly report the change in the price of fuel on the internal market, influenced by: stock quotes on world exchanges; market changes in the price conditions of producers and importers, leading to a redistribution of the volumes of end customers, consequences of accidents and natural disasters, leading to a temporary redistribution of the customers of a given producer/importer, etc.

Part of the changes made in the Excise Duties and Tax Warehouses Law (EDTWL) (Law amending and supplementing the EDTWL, promulgated, SG volume102 of 23.12.2022 in force from 1.01.2023) are aimed at reducing the administrative burden and creating easier conditions for economic operators, including removing potential obstacles for taxable persons in the application of the new regimes in the EDTWL, which are in force from February 13, 2023. A new provision was introduced to eliminate a gap in the EDTWL, since the persons who receive excise goods on the territory of the country, which are not subject to excise duty in the Member State of dispatch, were not among those expressly defined as taxable persons. It is accepted that when importing or introducing into the territory of the country products of the type of oils from vegetable fats, methanol, etc., the persons who import or introduce these goods should declare to the customs authorities the purpose of the goods (whether they will be used and/ or offered for sale as motor fuel and heating fuel). A legal framework has been created in which the certified recipients will submit a monthly excise declaration for the tax period, and not, as before, for individuals to declare and pay the excise tax for each receipt of excise goods released for consumption in the territory of another member state.

The obligation under EDTWL to register persons who consume their own electricity produced from energy from renewable sources for their own needs from a plant with a total installed community of up to 1 MW has been abolished. The change fulfils a commitment made in the Recovery and Resilience Plan of the Republic of Bulgaria in reform C4.R6 "Stimulation of the production of electricity from renewable sources". The hypotheses of mandatory registration (in Article 57a of EDTWL) are supplemented with the persons who import or bring into the country compressed natural gas transported by specialized vessels. This change aims to increase control under excise legislation and avoid deviation or avoidance of payment of the corresponding excise duty due depending on consumption. It is expressly stipulated that activities in which the user of an energy product enables its reuse in his enterprise are not considered to be production of energy products, provided that the excise duty already paid for this product is not less than the amount of the excise duty, which would be payable when re-excise is to be levied on the re-used product.

In 2023, a positive decision of the EC is expected on compliance with the Regional State Aid Guidelines (2021/C 153/01) for the application of a new scheme of tax relief representing state aid for regional development, which will start the devolution of corporate tax according to Art. 184 in connection with Art. 189 of the CITL, to be applied until December 31, 2027. The tax preference is provided with the aim of encouraging economic activity for SMEs by stimulating them to invest in tangible and intangible assets in enterprises located in municipalities with unemployment higher than the national average, expecting to maintain or increase employment levels in these municipalities.

The conditions regarding the general requirements for the assignment of corporate tax under Art. 167 of the CITL have been changed. It is explicitly stated that there are no enforceable public obligations and obligations under sanctions under criminal decrees that have entered into force, related to the violation of the normative acts regarding public obligations, as well as the corresponding interest related to their non-payment, when as of December 31 of in the corresponding year, the same are not reflected in the tax-insurance account or are not reflected as submitted for enforcement at the National Revenue Agency.

With the amendment in Art. 29, par. 1, item 2, letter "d" (new – SG volume 52 of 2022) of the Personal Income Tax Law, the legally recognized expenses for income from exercising a profession as a lawyer are increased (from 25% to 40%), which in turn reduce the taxable income from exercising the specific activity. The change applies from January 1, 2023.

With legislative amendments made (§ 7 of the of the TFP of Law on State Budget for 2022, Law on the State Public Insurance Budget 2022 and Law on NHIF Budget for 2022 – SG volume 104 of 30.12.2022) the period of use of the tax benefits under Art. 22c and 22d of the Personal Income Tax Law (for children and for children with disabilities) has been extended in 2023. The possibility of advance use in the current year is preserved. It is expressly regulated that the amounts refunded on the basis of these tax reliefs are not subject to enforcement. It is also possible to use the tax relief by submitting an annual tax return for a deceased person by the heirs by law or by will, as well as the testators or their legal representatives, when there are no other possibilities for the relief to be applied.

— National Revenue Agency (NRA)

In order to increase the share of voluntary compliance with obligations and improve the collection of tax and insurance obligations, the NRA continues the implementation of the following measures:

- Assisting citizens and companies in exercising their rights and obligations:
    - Ensuring fast and quality assistance to NRA clients.
    - Improvement of existing and development of new electronic services.
    - Reducing the administrative burden, expanding communication channels and increasing the share of electronic interaction and exchange of information with customers and with other administrations with regards to the: provision of administrative services, determination, declaration and payment of public obligations.
    - Customer service when accepting tax and insurance declarations and issuing certificates regardless of territorial competence.
    - Active communication and expansion of preventive measures towards citizens and businesses – notification letters, electronic messages, meetings, information campaigns and other activities to stimulate the fulfillment of obligations.

    - Ensuring transparency in the activities of the NRA and expanding the scope of open data.

- Control for compliance with legislation and reduction of tax fraud and enhanced administrative cooperation:
    - Constant monitoring and communication with obliged entities that form a significant share of the country's economy, incl. strengthening their awareness of the mechanisms and indications of tax fraud in order to avoid it.
    - Improvement of control, based on analysis of risk and risk behavior and development of a communication strategy with a view to providing an unlimited circle of clients of the administration with information for a general prevention against involvement in tax and insurance fraud.
    - Developing the capacity of the NRA for control over electronic commerce and control in a digital environment (e-audits).
    - Development of the NRA's capacity to control online gambling.
    - Implementation of effective and efficient fiscal control in relation to the movement /transportation/ of goods with a high fiscal risk on the territory of Bulgaria, with the aim of preventing tax evasion and tax fraud.
    - Achieving better transparency and efficiency of control-related activities, incl. the effectiveness of interdepartmental cooperation in countering and uncovering tax and/or insurance fraud and crimes.
    - Improving the quality of audit proceedings.
    - Dialogue with the business with the purpose of prevention in relation to compliance with tax and insurance legislation. Organization of meetings with branch organizations and the Advisory Board in relation to compliance with tax and insurance legislation.
    - Research and consultations with stakeholders on opportunities to implement the Standard Audit File for Tax (SAF-T) in accordance with the OECD Guidelines.
- Effective and efficient collection of arrears
    - Active communication and early implementation of methods stimulating the voluntary payment of arrears in order to avoid the need to apply coercive actions.
    - Application of a unified and individualized approach based on the evaluation of the customer's behavior, by means of data mining models.
    - Constant monitoring and communication with persons who have obligations with a high fiscal effect.
    - Improving communication, incl. electronically, with debtors, public debt collectors and interested parties.
    - Active communication and use of legal opportunities to facilitate the payment of debt by persons with temporary difficulties.
    - Increasing the effectiveness of mutual assistance in collection by using data from the automatic exchange of tax information.
    - Preparation for and conclusion of agreements with third countries on the implementation of the "Convention on Mutual Administrative Cooperation in Tax Matters" in the "Assistance in Collection" part.

- Development of the system for managing the risk of non-compliance with tax and insurance legislation in the NRA
  - Improvement of control based on risk analysis and risk behavior, incl. broad communication to create general prevention against involvement in tax and insurance fraud;
  - Continuing the implementation of the "Segmentation and behavioral profiling of NRA customers in the context of risk management" project;
  - Implementation of the activities under the "Strengthening compliance by introducing in the National Revenue Agency models for studying the external context and influencing the behavior of taxpayers" project;
  - Implementation of the activities under the "Development and implementation of a model of "Horizontal Monitoring" by the Bulgarian Revenue Administration" project;
- Assessment of VAT tax gaps at a high level.

– Customs Agency

Excise legislation

With the amendments and additions made in 2022 to the Law on EDTWL, effective from 2023, the persons registered under Art. 57a, para. 1(3b) of the EDTWL, are obliged to submit an excise duty declaration at the end of the tax period, which is one year. It is also provided that e-cigarette liquid containing nicotine is considered to be a tobacco product.

- In Article 29, para. 3, the taxable amount for a heated tobacco product and e-cigarette liquid is amended;
- Article 37 amends the excise tax rate for cigars and cigarillos;
- Article 38 amends the excise rate for smoking tobacco (for pipe and cigarettes) heated tobacco products, e-cigarette liquid containing nicotine;
- Article 39 amends the excise duty rate for cigarettes;
- Art. 3, para. 1, a new point 11 shall be inserted, related to the removal of a gap in the law, as currently persons who receive excise goods on the territory of the country which are not subject to excise duty in the Member State of dispatch are not explicitly defined as taxable persons. As of 13 February 2023, the new regimes for the receipt of excise goods from and to the territory of the country which are not subject to excise duty in the Member State of dispatch or receipt enter into force.
- In order to facilitate the activities of certified consignees, an addition has been made to Art. 44, para. 1(3) and a change to Article 87 of the EDTWL concerning the declaration and payment of excise duty due. This establishes a legal framework under which certified consignees will submit a monthly excise duty declaration for the tax period, rather than, as before, declaring and paying the excise duty for each receipt of excise goods released for consumption on the territory of another Member State.
- The amendment to Article 53, para. 6 creates a statutory possibility, by introducing a ground for payment of the statutory interest in addition to the excise duty due, for persons who are the owners of the goods and are depositors in the tax warehouse to remove the goods from the tax warehouse upon termination of the tax warehouse management license.

- An addition has been made to Article 57, para. 3(7), relating to the new definitions of 'independent small wine producer' and 'independent small wine producer's wine establishment' and their obligation to submit a declaration that they meet the requirements of Article 4(8), (8a) and (9) of the EDTWL.
- The amendment of Art. 57b para. 3(2) refines the provision and brings it into line with Art. 57a, para. 1(4), according to which persons registered for VAT purposes in another Member State who bring excise goods into the territory of the country for the purpose of making supplies under the conditions of distance selling within the meaning of the VATL shall register through a tax representative.

The new par. 7 in Article 59 is in line with the provision of Article 21, para. 6b of Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity. The purpose is to remedy a shortcoming in the transposition of the Directive by explicitly providing that activities where the user of an energy product makes it possible to re-use it in his undertaking are not to be regarded as the production of energy products, provided that the excise duty already paid on that product is not less than the amount of excise duty that would be payable if the re-used product were to be subject to a second excise duty.

- Paragraph 32 of the TFP of the EDTWL provides that: 'The provisions on the procedure for the movement of excise goods under Articles 76a, 76b and 76c shall apply until 12 February 2023 inclusive, and movements of excise goods commenced before that date shall be completed in the same manner.“

Amendments and additions to the Regulations on the Implementation of the Law on Excises and Tax Warehouses in 2022 have been prepared in connection with the amendments and supplementations to the EDTWL.

Proposals for the inclusion of bills in the Legislative Program of the Council of Ministers for the first six months of 2023

In the period until 30.06.2023, as part of the Legislative Program of the Council of Ministers for the first six months of 2023, the Customs Agency has made proposals for the inclusion of the following bills: A Law amending and supplementing the EDTWL, a Law amending and supplementing the Customs Law, a Law amending and supplementing the Civil Servant Law and a Law amending and supplementing the Law on Electronic Government. Along with them, currently the Customs Agency has submitted for consideration to the Ministry of Finance a package of materials for amending the Roads Law. The project was prepared in connection with the need to create conditions for a more efficient use of the personnel resources of the state administration in carrying out the control functions assigned to the executive power, and it provides for relevant amendments to the Road Traffic Law and the Customs Law.

In order to increase the collection of the public state receivables established in the normative act and in accordance with the powers granted to it, the Customs Agency analyzes and applies various tools to increase the efficiency of the functions performed by the customs administration within the available financial, administrative and human resources. In this regard, the Customs Agency has carried out an analysis of the collectability of public state receivables, established by acts of the customs authorities, when the same are not subject to voluntary implementation, a package of materials has been imported.

Projects related to the development and improvement of the integrated information systems of the Customs Agency

In the period from 2023 to 2026, the Customs Agency will continue to implement a number of projects in accordance with the Roadmap for the implementation of the "e-Customs" (2021-

2027) Sector Strategy, which aims to increase the quality of administrative services of citizens and businesses, to reduce the administrative burden, to produce timely reflection of changes in the regulatory framework, to improve the processes of transition to a paperless environment, etc.

During the period, the implementation is planned of 26 measures out of a total of 46 measures from the Roadmap to the "Sector strategy for the development of electronic management in the Customs Agency – "e-Customs" 2021–2027", adopted by Decision No. 951 of 25.11.2022 of the Council of Ministers.

As a priority at the national level for the modernization of border crossings, the Customs Agency launched a project to build a single integrated information system "Control of means of transport in real time" (CMTRT). The project is aimed at increasing the throughput of the border crossing, improving the results of countering attempts to violate customs and excise legislation, expanding the possibilities of automated risk analysis, facilitating the commercial operations of legitimate businesses, increasing the competitiveness of the economy, as well as improving the performance of the functions of CA in protecting the people's lives and health.

In connection with the construction of the CMTRT, in the period 2023 – 2025, the following projects will be launched in the agency:

- "Construction of a video data center of the Customs Agency – stage 1";
- "Development and introduction of Institutional Architecture of CA in relation to the: "Construction of a Centralized Information System for the Control of Means of Transport in Real Time (CIS CMTRT) – stage 1 on Cloud architecture" project;
- "Development and implementation of the Institutional Architecture of the Customs Agency (CA) in relation to the "Building a Border Control Traffic Management System on Cloud Architecture" project;
- "Development and implementation of the Institutional Architecture of the Customs Agency in relation to the "Building a Queue Management System on Cloud Architecture" project.

During the period, the implementation will be completed of 11 projects from the work program regarding the development and introduction of the electronic systems provided for in the Customs Code of the Union, included in the Customs Agency's National Plan for the development of information systems 2020-2025. In the period, the construction of a Bulgarian Integrated X-ray information system for the analysis and exchange of images and data from the X-ray equipment of the Customs Agency is also planned.

In 2023, the agency continues to implement projects under the "Good Governance" Operational Program (OPGG):

- "Upgrading the main systems of the Customs Agency for the provision of data and services – BIMIS (phase 2)" under Contract No BG05SFOP001-1.007-0001-C01/15.04.2019 for the provision of grant financial assistance, with an implementation period from 01.03.2019 to 30.09.2023 and a total value of BGN 13 377 145,60 including VAT. The project includes 5 activities.
- "Upgrading the main systems of the Customs Agency for the provision of data and services – BIMIS (phase 3)" under Contract No BG05SFOP001-1.025-0001-C01 of 29.11.2021 for the provision of grant financial assistance under the OPGG, with an implementation period from 01.09.2021 to 31.12.2023 and a total value of BGN 17 784 495,00 including VAT. The project includes 7 activities.

In 2023, CA will apply under Procedure BG16BARA001-1.001 for the direct provision of a grant entitled "Financing of adjustment measures in connection with the consequences of Brexit".

7. INSTITUTIONAL CHARACTERISTICS OF PUBLIC FINANCE

7.1 National fiscal rules

The existence of a legal framework defining budgetary rules, restrictions and procedures in the event of deviations from the targets for a given indicator is a prerequisite for in- creasing the predictability of fiscal policy, compliance with budgetary and financial discipline, and ensuring the sustainability of public finances. Fiscal rules should be of a permanent nature, to be relevant for a significant indicator (in the most general case for budget balance, debt, expenditure and revenue) and set numerical limits or targets. Legal requirements and procedures are also required for corrective mechanisms and measures to return to the target or to the restriction set by the rule and cases of deviation from the target/the restriction.

In terms of scope, we distinguish between rules for indicators both according to the national methodology – for the budget balance and expenditures under the consolidated fiscal programme (on a cash basis) and for government debt, as well as indicators according to the European methodology – for the general government sector (for some rules – and for its relevant sub- sectors) – for the medium-term budgetary objective (MTO), for the structural deficit, for the budget balance, for expenditure growth relative to potential GDP growth and for consolidated debt for the General Government sector.

With the adoption of the Public Finance Act (PFA) and the Fiscal Council and Automatic Corrective Mechanisms Act and their subsequent amendments related to achieving full compliance with European legislation, Bulgaria has fully met the requirements for strengthening economic governance in the EU. The rules meet internationally accepted definitions and criteria and the requirements for aligning national fiscal planning with the preventive and corrective arms of the EU Stability and Growth Pact.

Concentration of fiscal rules and their permanent regulation within the PFA has a positive impact not only on improving coordination in the implementation of various policies, but also on better planning, development and implementation of fiscal policy, as it ensures their long-term sustainability.

An important condition for the proper functioning of fiscal rules are the bodies that monitor the compliance, as well as the existence of corrective mechanisms in case of deviation from the set goals. Their monitoring is based on universal criteria for assessing fiscal policy. Fiscal rules generally impose restrictions on fiscal policy at the national level, but some of them also impose numerical restrictions on budget indicators of individual budgets, such as those for municipalities.

Since the adoption of the PFA in 2013, three significant amendments to the PFA have been adopted so far (in 2016, 2017 and 2020), which were related to the refinement and further development of the regulation in order to improve the governance processes of public finances and achieving full compliance with the requirements of Council Directive 2011/85/EU of 8 November 2011 on the requirements for budgetary frameworks of the Member States, creating the conditions for implementing the relevant regulations adopted at the end of 2011, as well as with regard to fiscal rules and restrictions in order to ensure an adequate response to the challenges and extraordinary situation borne out of the COVID-19 crisis.

Compliance with fiscal rules and budgetary discipline are the responsibilities of different authorities. The government is responsible for complying with fiscal rules at the national level (for the CFP and the General Government sector) with limited opportunities to influence subsectors (local authorities, social security funds and autonomous budgets), and can compensate for existing deviations only within the scope of the central government. Deviations from the set restrictions are possible when they are the result of imposed one-off measures and they do not lead to lasting negative trends for the development of fiscal policy in the medium term.

At the level of individual budgets, the legal commitments of the first-level spending units require within governance responsibilities to observe budgetary discipline, incl. the rules applicable to them. This also applies to stand-alone budgets, which are not part of the state budget, as they affect the parameters of the budgetary framework at the national level.

In addition to the basic principles, rules and procedures applicable to all spending units, the accumulated budget imbalances of local authorities and the inability to comply with the rules for municipalities are the reason for legal regulation of procedures for identifying municipalities in financial difficulties and establishing financial recovery mechanisms.

During the implementation period of the amendments in the PFA, with regard to the established mechanism for financial recovery of municipalities, the number of municipalities defined as municipalities with financial difficulties decreased.

In 2023, the practice introduced by the Minister of Finance for coordination of the draft budgets of the municipalities, where the term of the procedure for financial recovery has expired in 2022, continues in order to fulfil their commitments to repay interest-free loans granted under Art. 130g, para. 1 of the PFA.

Both national and European resources have been mobilized in response to the global challenges of containing and overcoming the consequences of the COVID-19 pandemic. The smooth implementation of these proactive counter-cyclical measures was not to be impeded, which is why the possibility of a temporary deviation from the restrictions in the conditions of extraordinary circumstances was provided for in national legislation – this was the reason for the adoption of amendments to the Public Finances Act at the end of 2020. The changes provided greater flexibility to national fiscal rules in the presence of exceptional circumstances by introducing norms for temporary deviation from the requirements in accordance with the dynamic and rapidly changing reality needs and removing the preconditions for pro-cyclical impact; clear definition of limitations and tolerances; ensuring the implementation of measures to limit and overcome the consequences of emergency situations and the unhindered absorption of funds from European funds and programs, including and the implementation of relevant recovery plans. By adopting these changes, it has been ensured that the restrictions are in line with the dynamic challenges of complying with the requirements of European legislation.

7.2 Budgetary procedures

Budgeting is an ongoing process, but the stages and steps for its implementation are evolving depending on many factors – organizational, economic, political, legal and others, which predetermine the need to develop a schedule to organize the process of planning and drafting budget documents

The PFA states that the budget procedure includes the stages, deadlines, distribution of responsibilities and requirements for compiling both the medium-term budget forecast and the draft state budget. The constant strife to improve the quality of budget documents as an expression of good public finance management implies that the budget procedure takes into account both the changing requirements for all responsible institutions and the requirements for Bulgaria as a member state within the European Semester – the timetable for the coherence of national economic and budgetary policies within the European Union.

The budget procedure for 2024 (approved by Decision No 70 of the Council of Ministers of 27 January 2023) was prepared in accordance with the rules of the PFA, and its preparation reflected the set requirements for the structure and content of key budget documents and deadlines for their preparation.

The 2024 budget procedure was planned to ensure a return to the standard stages in the budget preparation and adoption process, after the budget procedures in recent years were carried out in the context of an ongoing epidemic emergency, as well as political challenges and uncertainty, which accordingly affected the timing of the prepared budget documents.

However, the implementation of the steps and timelines of the first stage of the procedure has been delayed by the absence of a Budget 2023 adopted within the usual timeframe and incorporating long-term policy development assumptions.

The deadlines for the first stage of the 2024 budgetary procedure coincided with the preparation of the draft of the 2023 Budget, including the preparation of the updated Medium-Term Budget Forecast 2023–2025 (approved by Decision No 331 of the Council of Ministers of 28 April 2023 and submitted to the National Assembly for consideration), which are the basis for the development of the current CP, the Medium-Term Budget Forecast 2024-2026 and other related acts of the Government.

According to preliminary planning, in June 2023, the Council of Ministers will consider and approve the draft decision prepared by the Minister of Education and Science on approving the maximum amount of new state guarantees that can be issued in 2024 under the Student Loans Act and doctoral students, as well as the draft decision prepared by the Minister of Finance for approving the projects that will be financed with state and/or state-guaranteed loans in 2024. The first stage ends in July with the adaptation by first-level spending units of their budget forecasts for the period 2024 – 2026 with the decisions adopted by the Council of Ministers and with the publication of the budget forecasts in a program format on its websites in compliance with the requirements of the Law on the Protection of Classified Information.

In the second stage of the procedure, the main processes and budget documents are related to the preparation of the bill of the state budget of the Republic of Bulgaria for 2024 and updated medium-term budget estimates for the period 2024-2026.

The coordination with the National Association of Municipalities in the Republic of Bulgaria of the mechanism for distributing the general equalization subsidy and the targeted subsidy for capital expenditures by municipalities and the holding of consultations on the proposals of the association for the total amount of the main budgetary relationships of the municipal budgets with the central budget and others proposals for the draft state budget for 2024 in its part for municipalities is also part of the second stage.

By the end of October 2023, the Council of Ministers examines and approves the drafts prepared by the Minister of Finance of the Law on the State Budget of the Republic of Bulgaria for 2024 and of the updated medium-term budget forecast for the period 2024-2026, and if necessary, approves changes and in the other related acts of the government. In the same period, the Council of Ministers examines and approves the drafts of the Law on the Budget of the NHIF for 2024 and the Law on the Budget of the State Social Insurance for 2024.

Within one month of the promulgation in the "State Gazette" of the Law on the State Budget of the Republic of Bulgaria for 2024, the Council of Ministers adopts, on the proposal of the Minister of Finance, a Decree on the implementation of the State Budget of the Republic of Bulgaria for 2024.

If necessary, within one week of the approval of the changes in the updated medium-term budget forecast for the period 2024-2026, the first-level spending units of the budgets of the budget organizations, which are determined to implement the program format of the budget, update the program formats of their budgets, send them to the Ministry of Finance, the Audit Office and the National Assembly and publish them on their websites, which ends the budget procedure for 2024.

The budget procedure for 2024 currently follows the set deadlines for the preparation of the main budget documents, which creates conditions for transparency and predictability and represents an element of the good governance of public finances in the country. The conscientious participation in the budget process of all budget organizations is a condition for the overall success of the procedure and a prerequisite for achieving the desired final results of its implementation.

7.3 Other institutional developments in relation to public finance

Although Bulgaria will not join the euro area on January 1, 2024, the caretaker government continues the work on the practical preparation for membership at the same accelerated pace.

In this regard, a new Law on the Bulgarian National Bank was prepared to regulate the functioning of our national bank within the euro area.

A draft Law on the Introduction of the Euro in the Republic of Bulgaria (Euro Act) is also being prepared. It is being drafted by a specially formed interdepartmental working group to the Coordination Council for the Preparation of the Republic of Bulgaria for Euro Area Membership. At this stage, work on the bill is in an advanced phase. According to the indicative schedule adopted by the working group, after the Euro Act has been drafted, it will be sent to the EC and the ECB for their comments. The bill will be finalised by June after which it will be submitted for adoption by the National Assembly.

A wide-ranging communication campaign is about to be launched, which will inform and explain to the Bulgarian society and businesses the process of our country's accession to the euro area.

Bulgaria's goal is to submit a request for the preparation of Convergence Reports by the EC and the ECB immediately after the fulfillment of the Maastricht criteria on the one hand, and on the other – adoption of the necessary regulatory and other commitments agreed upon when the lev joined the Exchange Rate Mechanism II, and in fulfillment of the Convergence Reports' recommendations.

8. Annex A

Table 1a: Macroeconomic prospects

	ESA 2010 code	2022	2022	2023	2024	2025	2026
		Level (MBGN)	Rate of change	Rate of change	Rate of change	Rate of change	Rate of change
Real GDP	B1*g	108 296	3.4	1.8	3.3	3.2	3.0
Nominal GDP	B1*g	165 384	19.0	11.6	7.1	6.4	5.9
Components of real GDP							
Private consumption expenditure	P.3	72 520	4.8	3.2	4.3	4.0	3.8
Government consumption expenditure	P.3	19 107	6.5	2.4	-0.2	0.9	1.7
Gross fixed capital formation	P.51	17 502	-4.3	6.3	12.6	6.5	4.8
Change in inventories and net acquisition of valuables (% of GDP)	P.52+ P.53	5 021	5.4	5.3	5.2	5.0	4.9
Export of goods and services	P.6	74 824	8.3	1.7	4.3	4.7	4.3
Import of goods and services	P.7	83 076	10.5	3.9	6.4	5.4	5.0
Contributions to real GDP growth (In percentage points)							
Final domestic demand		-	3.3	3.3	4.5	3.7	3.4
Change in inventories and net acquisition of valuables	P.52+P.53	-	1.3	0.0	0.0	0.0	0.0
External balance of goods and services	B.11	-	-1.2	-1.5	-1.3	-0.5	-0.5

Table 1b: Price developments

	ESA 2010 code	2022	2022	2023	2024	2025	2026
		Level	Rate of Change[35]	Rate of Change	Rate of Change	Rate of Change	Rate of Change
GDP deflator		100	15.1	9.5	3.7	3.1	2.8
Private consumption deflator		100	16.6	8.1	3.2	2.7	2.5
HICP[36]		100	13.0	8.7	3.8	2.8	2.2
Public consumption deflator		100	9.8	8.0	3.3	2.7	2.2
Investments deflator		100	14.0	8.8	4.7	2.7	2.3
Export price deflator (goods and services)		100	22.8	-0.8	2.4	1.7	1.2
Import price deflator (goods and services)		100	22.2	-2.6	2.1	1.1	0.6

35 Percentage change as compared to the previous year.

36 Optional for Stability Programmes.

Table 1c: Labour market developments

	ESA 2010 code	2022	2022	2023	2024	2025	2026
		Level	Rate of Change	Rate of Change	Rate of Change	Rate of Change	Rate of Change
Employment (thousand persons)[37]		3 502	1.3	0.4	0.7	0.5	0.3
Employment (millions of hours worked)[38]		5 669	1.2	0.8	1.1	1.0	0.5
Unemployment rate[39]		4.3	4.3	4.1	3.9	3.8	3.8
Labour productivity (BGN per person employed)[40]		30 923	2.1	1.4	2.5	2.7	2.7
Labour Productivity (BGN per hour worked)[41]		19	2.1	1.0	2.2	2.2	2.5
Compensation of employees (MBGN)[42]	D.1	73 153	19.3	11.9	11.6	8.5	7.5
Compensation per employee		27 940	18.4	11.5	10.6	7.7	7.1

Table 1d: Sectorial balances

% of GDP	ESA 2010 code	2022	2023	2024	2025	2026
Net lending/borrowing vis-à-vis the rest of the world	B.9	0.3	1.0	0.9	-0.3	0.0
of which: –balance of goods and services		0.5	0.5	-0.6	-0.6	-0.6
–balance of primary incomes and transfers		-1.2	-1.2	-1.1	-1.3	-1.4
–capital account		0.9	1.7	2.6	1.7	2.0
Net lending/borrowing of the private sector	B.9	3.1	7.1	5.6	4.7	5.1
Net lending/borrowing of the general government	EDP B.9	-2.8	-6.1	-4.7	-4.9	-5.0
Statistical discrepancy						

37 Occupied population, national accounts definition.

38 National accounts definition.

39 Harmonised definition, Eurostat; levels.

40 Real GDP per one person employed.

41 Real GDP per one hour worked.

42 In MBGN.

Table 2a: General government budgetary prospects

	ECC 2010	2022 Level	2022 % of GDP	2023 % of GDP	2024 % of GDP	2025 % of GDP	2026 % of GDP
Net lending (EDP B.9) by sub-sector							
1. General government	S.13	-4 647.6	-2.8	-6.1	-4.7	-4.9	-5.0
2. Central government	S.1311	-4 457.0	-2.7	-6.4	-5.2	-5.5	-5.5
3. State government	S.1312						
4. Local government	S.1313	423.5	0.3	0.3	0.5	0.5	0.5
5. Social security funds	S.1314	-614.2	-0.4	0.0	0.0	0.0	0.0
6. Total revenue	TR	63 711.2	38.5	35.5	36.2	35.4	34.3
7. Total expenditure	TE	68 358.8	41.3	41.6	40.9	40.4	39.4
8. Net lending / borrowing	EDP B.9	-4 647.6	-2.8	-6.1	-4.7	-4.9	-5.0
9. Interest expenditure	EDP D.41	770.4	0.5	0.6	1.0	1.3	1.7
10. Primary balance		-3 877.2	-2.3	-5.5	-3.6	-3.7	-3.4
11. One-off and other temporary measures		-2 917.7	-1.8	-0.4	0.0	0.0	0.0
12. Total taxes (12=12a+12b+12c)		37 314.3	22.6	21.1	21.1	20.9	20.7
12a. Taxes on production and import	D.2	26 164.0	15.8	14.5	14.3	14.1	13.9
12b. Current taxes on income, wealth, etc.	D.5	10 615.1	6.4	6.3	6.6	6.6	6.5
12c. Capital taxes	D.91	535.2	0.3	0.3	0.3	0.3	0.3
13. Social contributions	D.61	13 890.5	8.4	8.4	8.6	8.6	8.8
14. Property income	D.4	1 743.8	1.1	0.9	0.9	1.0	1.0
15. Other		10 762.6	6.5	5.1	5.6	4.8	3.9
16=6. Total revenue	TR	63 711.2	38.5	35.5	36.2	35.4	34.3
Tax burden (D.2+D.5+D.61+D.91-D.995)		51 204.8	31.0	29.5	29.7	29.6	29.4
17. Compensation of employees + intermediate consumption	D.1+P.2	25 346.2	15.3	15.8	14.5	13.7	13.5
17a. Compensation of employees	D.1	16 543.9	10.0	9.9	9.7	9.5	9.3
17b. Intermediate consumption	P.2	8 802.3	5.3	5.9	4.8	4.2	4.3
18. Total social transfers (18=18a+18b)		24 689.3	14.9	15.7	16.3	16.6	16.7
of which Unemployment benefits	D.621, D.624	412.6	0.2	0.3	0.2	0.2	0.2
18a. Social transfers in kind	D.6311. D.63121. D.63131	4 671.2	2.8	2.9	3.1	3.2	3.3
18b. Social transfers other than in kind	D.62	20 018.1	12.1	12.8	13.2	13.3	13.4
19=9. Interest expenditure	EDP D.41	770.4	0.5	0.6	1.0	1.3	1.7
20. Subsidies	D.3	8 362.8	5.1	3.2	2.0	1.9	1.8
21. Gross fixed capital formation	P.51	5 035.8	3.0	4.0	4.6	4.7	3.5
22. Capital transfers	D.9	817.3	0.5	0.6	0.7	0.6	0.6
23. Other		3 337.0	2.0	1.7	1.9	1.6	1.6
24=7. Total expenditure	TE1	68 358.8	41.3	41.6	40.9	40.4	39.4
Government consumption (nominal))	P.3	30 796.3	18.6	18.5	17.8	17.3	17.0

Table 2b: No-policy change projections

	2022	2022	2023	2024	2025	2026
	Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. Total revenue at unchanged policies	63 711.2	36.75	37.27	36.08	35.04	34.02
2. Total expenditure at unchanged policies	68 358.8	38.71	42.43	40.52	38.96	38.59

Table 2c: Amounts to be excluded from the expenditure benchmark

	2022	2022	2023	2024	2025	2026
	Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
1. Expenditure on EU programmes fully matched by EU funds revenue	1 432,2	0,9	1,3	2,3	1,9	1,1
1a. Investments fully matched by EU funds revenue	739,1	0,4	0,7	1,9	1,4	0,7
2. Cyclical unemployment benefit expenditure	412,6	0,2	0,3	0,2	0,2	0,2
3. Effect of discretionary revenue measures	3 012,4	1,8	-2,1	0,1	0,4	0,3
4. Revenue increases mandated by law	0.0	0.0	0.0	0.0	0.0	0.0

Table 3: General government expenditure by function

% of GDP	ESA 2010 code	2021	2026
1. General public services	1	3,5	4,2
2. Defence	2	1,6	1,7
3. Public order and safety	3	2,7	2,1
4. Economic affairs	4	6,7	5,9
5. Environmental protection	5	0,8	0,5
6. Housing and community amenities	6	1,0	0,7
7. Healthcare	7	5,8	5,4
8. Recreation, culture and religion	8	0,9	0,6
9. Education	9	4,3	3,9
10. Social protection	10	13,4	14,4
11. Total expenditure (= item 7 = 24 of Table 2)	TE1	**40,6**	**39,4**

Table 4: General government debt developments

% of GDP	ESA code	2022	2023	2024	2025	2026
1. Gross debt[43]		22.9	26.6	30.7	33.8	37.1
2. Change in gross debt level		- 1.0	3.7	4.1	3.1	3.3
Contributions to changes in the gross debt to GDP ratio						
3. Primary balance[44]						
4. Interest expenditure[45]	EDP D.41	0.4	0.6	1.0	1.3	1.6
5. Stock-flow adjustment						
of which:						
Differences between cash and accruals[46]						
Net accumulation of financial assets[47]						
of which: privatisation proceeds						
Valuation effects and other[48]						
Implicit interest rate on debt[49]		1.9	2.8	4.0	4.3	5.1
Other relevant variables						
6. Liquid financial assets[50]						
7. Net financial debt (7=1-6)						
8. Debt amortization since the end of the previous year		9.9	8.9	7.7	6.6	4.2
9. Percentage of debt denominated in foreign currency		69.8	72.1	72.8	76.0	78.8
10. Average maturity		7.7	8.8	8.8	8.7	9.0

43 As defined in Regulation 479/2009 (not an ESA concept).

44 Cf. item 10 in Table 2.

45 Cf. item 9 in Table.

46 The differences concerning interest expenditure, other expenditure and revenue could be distinguished when relevant or in case the debt-to-GDP ratio is above the reference value.

47 Including liquid assets, government securities, assets in third countries, government controlled enterprises and the difference between quoted and non-quoted assets could be distinguished when relevant or in case the debt-to-GDP ratio is above the reference value.

48 Changes due to exchange rate movements, and operation in secondary market could be distinguished when relevant or in case the debt-to-GDP ratio is above the reference value.

49 Approximately calculated as interest expenditure divided by the debt level of the previous year.

50 AF1, AF2, AF3 (consolidated at market value), AF5 (if quoted in stock exchange; including mutual fund shares).

Table 5: Cyclical developments

% of GDP	ESA 2010 code	2022	2023	2024	2025	2026
1. GDP growth (%)		3.4	1.8	3.3	3.2	3.0
2. Net lending of general government	EDP B.9	-2.8	-6.1	-4.7	-4.9	-5.0
3. Interest expenditure	EDP D.41	0.4	0.6	1.0	1.3	1.6
4. One-off and other temporary measures		-1.8	-0.4	0.0	0.0	0.0
5. Potential GDP growth (%)		2.6	2.6	2.9	3.0	2.9
Contributions:						
labour		0.2	0.2	0.3	0.3	0.2
capital		0.5	0.6	0.8	1.0	1.0
total factor productivity		1.9	1.8	1.8	1.7	1.6
6. Output gap		0.9	0.2	0.5	0.8	0.9
7. Cyclical budgetary component		0.3	0.1	0.2	0.2	0.3
8. Cyclically-adjusted balance (2-7)		-3.1	-6.2	-4.8	-5.2	-5.3
9. Cyclically-adjusted primary balance (8+3)		-2.6	-5.6	-3.8	-3.9	-3.7
10. Structural balance (8-4)		-1.3	-5.8	-4.8	-5.2	-5.3

Table 6: Divergence from previous update

	ESA 2010 code	2022	2023	2024	2025	2026
Real GDP growth (%)						
Previous update		2.6	2.8	3.6	3.4	-
Current update		3.4	1.8	3.3	3.2	3.0
Difference (pps)		0.8	-1.0	-0.3	-0.2	-
General government net lending (% of GDP)	EDP B.9					
Previous update		-5.3	-2.8	-2.8	-2.4	-
Current update		-2.8	-6.1	-4.7	-4.9	-5.0
Difference (pps)		2,5	-3,3	-1,9	-2,5	-
General government gross debt (% of GDP)						
Previous update		25.5	27.7	29.1	30.4	-
Current update		22.9	26.6	30.7	33.8	37.1
Difference (pps)		-2.6	-1.1	1.6	3.4	-

Table 7: Long-term sustainability of public finances

% of GDP	2007	2010	2020	2030	2040	2050	2060	2070
Total expenditure	37.7	36.1	41.5					
Of which: age-related expenditures	15.0	17.3	18.9	19.2	18.2	18.4	18.8	18.7
Pension expenditures	7.4	9.3	9.2	10.3	9.2	9.1	9.4	9.5
Social security pension				10.1	9.0	8.9	9.1	9.2
Old-age and early pensions				8.0	7.1	7.2	7.6	7.5
Other pensions (disability, survivors)				2.1	1.9	1.7	1.5	1.7
Occupational pensions (if in general government)								
Health care	4.0	4.4	5.8	4.8	5.0	5.1	5.0	5.0
Long-term care								
Education expenditure	3.6	3.6	3.9	4.1	4.0	4.2	4.4	4.2
Other age-related expenditures								
Interest expenditure								
Total revenue	37.7	32.5	37.7					
Of which: property income								
Of which: from pensions contributions (or social contributions if appropriate)								
Pension reserve fund assets								
Of which: consolidated public pension fund assets (assets other than government bonds)								
Social contributions diverted to mandatory additional pension scheme[51]								
Pension expenditure paid by mandatory additional pension scheme[52]								
Labour productivity growth	1.9	8.2	-0.5	3.0	2.3	2.2	1.8	1.5
Real GDP growth	6.6	1.5	-4.0	1.8	1.2	1.0	1.3	1.3
Participation rate, males (aged 20-64)	78.3	76.8	82.2	86.8	86.2	87.2	88.6	87.9
Participation rate, females (aged 20-64)	68.4	67.0	72.4	77.7	77.7	77.8	79.4	78.7
Participation rate, total (aged 20-64)	73.3	71.9	77.3	82.3	82.1	82.6	84.1	83.4
Unemployment rate (%, aged15-64)	6.9	10.3	5.1	4.8	5.3	5.3	5.3	5.3
Population aged 65+ over total population	17.8	18.2	21.6	23.1	26.3	30.1	32.4	30.9

51 Revenue from social security contributions or other revenue for the mandatory additional pension insurance, with which the accounts payable can be covered.

52 Pension expenditure or other social benefits paid by the mandatory additional pension insurance.

Table 7a: Contingent Liabilities

% of GDP	2023	2024
Government guaranteed debt	1.3	1.2
Of which: linked to the financial sector	0.4	0.4

Table 8: Basic assumptions

	2022	2023	2024	2025	2026
Short-term interest rate (annual average) 6-month LIBOR in EUR, %	0.34	3.30	3.30	2.80	2.30
Short-term interest rate (annual average) 6-month LIBOR in USD, %					
Long-term interest rate (annual average), %					
USD/EUR exchange rate (annual average)	1.05	1.06	1.06	1.06	1.06
Nominal effective exchange rate. percentage change. previous year = 100[53]					
EUR/BGN exchange rate (annual average)	1.95583	1.95583	1.95583	1.95583	1.95583
World economy (excluding EU). GDP growth, %	3.4	2.8	3.1	3.2	3.2
EU GDP growth, %	3.5	0.7	1.8	2.1	1.9
Growth of relevant foreign markets. %					
World import volumes, excluding EU, %					
Crude Oil, Brent (USD/barrel)	99.8	82.2	77.4	73.3	70.0
International prices of non-energy commodities, %	8.7	-10.6	-2.1	-1.4	-0.6
International prices of food products, %	16.2	-6.9	-5.2	-3.1	-1.6
International prices of agricultural raw materials, %	5.0	-35.0	1.4	-0.4	-0.4
International prices of metals, %	-0.4	-5.0	-0.3	0.3	1.0

[53] The positive values reflect appreciation, the negative – depreciation.

9. ANNEX B

Table 1: Table of the RRF impact on programme's projections – GRANTS

Revenue from RRF grants (% of GDP)							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
RRF GRANTS as included in the revenue projections			*0.02*	*0.28*	*1.34*	*1.10*	*0.46*
Cash disbursements of RRF GRANTS from EU			*1.62*	*0.00*	*1.46*	*1.67*	*1.43*
Expenditure financed by RRF grants (% of GDP)							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Compensation of employees D.1			0.00	0.01	0.01	0.02	0.01
Intermediate consumption P.2			0.00	0.03	0.08	0.07	0.02
Social payments D.62+D.632							
Interest expenditure D.41							
Subsidies, payable D.3							
Current transfers D.7							
TOTAL CURRENT EXPENDITURE			***0.00***	***0.03***	***0.10***	***0.08***	***0.03***
Gross fixed capital formation P.51g			***0.02***	***0.25***	***1.24***	***1.02***	***0.43***
Capital transfers D.9							
TOTAL CAPITAL EXPENDITURE			***0.02***	***0.25***	***1.24***	***1.02***	***0.43***
Other costs financed by RRF grants (% of GDP)*							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Reduction in tax revenue							
Other costs with impact on revenue							
Financial transactions							

* This covers costs that are not recorded as expenditure in national accounts.
Bold: required information.

Table 2: Table on the RRF impact on programme's projections – LOANS

Cash flow from RRF loans projected in the programme (% of GDP)							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Disbursements of RRF LOANS from EU	0	0					
Repayments of RRF LOANS to EU							
Expenditure financed by RRF loans (% of GDP)							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Compensation of employees D.1							
Intermediate consumption P.2							
Social payments D.62+D.632							
Interest expenditure D.41							
Subsidies, payable D.3							
Current transfers D.7							
TOTAL CURRENT EXPENDITURE							
Gross fixed capital formation P.51g							
Capital transfers D.9							
TOTAL CAPITAL EXPENDITURE							
Other costs financed by RRF loans (% of GDP)[1]							
	2020	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Reduction in tax revenue							
Other costs with impact on revenue							
Financial transactions							

* This covers costs that are not recorded as expenditure in national accounts.
Bold: required information.