

The Republic of Bulgaria

Rating on Foreign Currency Long-term Senior Debts: BBB-/Stable

Rating on Local Currency Long-term Senior Debts: BBB/Stable

(Latest rating review released on July 2, 2003)

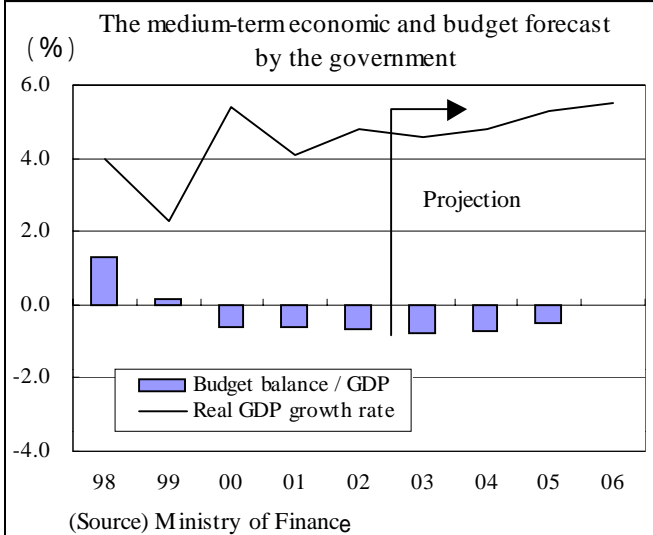
Main Factors for the Ratings

Positive Factors

- An emerging virtuous circle of the economy due to the progress of economic and budgetary reforms in anticipation of the EU accession in 2007.
- Rising exports boosted by the expansion in the production capacity through inflows of foreign direct investment.
- Constraint on budget deficits and significant reduction in government debts.

Negative Factors

- Early stage in transforming the industrial structure.
- High level of external debt due to the increase in that of the private sector.
- Inflexible labor market.



Updated: from June 2003 to August 2003

Positive Factors

- The budget balance for the first half of 2003 recorded a large surplus due mainly to increasing tax revenues.
- The government released a medium-term economic and budgetary projection, targeting fairly high economic growths and a balanced budget.
- The IMF completed the third review under Stand-by Arrangement and approved the disbursement.

Negative Factors

- Finance Minister submitted his resignation to Prime Minister (later he withdrew the resignation).
- The current account deficit for the first 6 months of 2003 doubled on a year-on-year basis due to the sharp growth in imports.
- The economic growth rate decelerated slightly to 3.8% (year-on-year) in the first quarter of 2003 following the fourth quarter of 2002.

<Prospects and Noticeable Points>

Upgrading of the rating on the foreign currency long-term debts

On July 2, 2003, JCR upgraded the rating on the foreign currency long-term debts to “BBB-” and newly assigned the “BBB” rating to the local currency long-term debts. The upgrading of the rating reflects the following: political, economic and budgetary reforms have progressed in pursuit of the EU entry in 2007; and a sustainable economic growth is in prospect in the medium-term perspective in view of the virtuous cycle emerged in the economy owing to proper economic and fiscal policies implemented by the government and the central bank, including tight fiscal policy, the reduction in public debt, the maintenance of the currency board regime and the stable financial system.

The budgetary balance recorded a large surplus despite the slight economic slowdown

The real economic growth rate decelerated slightly to 3.8% in the first quarter of 2003 over the same period of 2002, because while domestic demand continued to grow rapidly, widened negative net external demand

contributed adversely to the growth. Meanwhile, the inflation and unemployment rates continued to improve; the July CPI was up a low 2.0% (year-on-year) and the June unemployment rate fell to lower than 14%. According to the Ministry of Finance, the budgetary balance for the first half of 2003 recorded the large surplus of leva 627 million due mainly to the increase in tax revenues. Judging from the budgetary surplus equivalent to nearly 2 % of GDP for 2002, most probably the government will be able to achieve its projected budgetary deficit of 0.8 % of GDP for the whole year. At end-May, the government debt rose slightly in terms of US dollar, but the ratio of its debt to GDP declined to lower than 50% from 55.6% at the end of 2002, reflecting the appreciation of the Bulgarian currency against the US dollar.

The government's medium-term economic and budgetary projection

The government released the medium-term economic and budgetary projection for the period 2004 to 2006. The real economy is projected to grow annually at over 5 %, and inflation to be stable at around 3 % during the period. It is also projected that although the budgetary balance will be in deficit for both 2004 and 2005, it will be in equilibrium in 2006 (the projection incorporated a reduction in the corporate income tax rate). As JCR estimates the potential economic growth rate to be at around 5%, the government would probably be able to achieve the projected economic and budgetary targets, given that it implements the economic reform as it has done to date.

The focal point of the current coalition government is its fiscal policy

The focal point for the moment would be the fiscal policy of the coalition government led by Mr. Simeon whose political power base has been weakening. Although the government retains the parliamentary majority securing more than 120 seats, members of parliament have defected from the coalition parties one after another, besides, its popularity has dropped to the lowest level ever recorded. The sharp drop in the popularity was derived from the failure to deliver on its election promises to 'improve living standards of the people', as exemplified by the persistently high unemployment rate. Prime Minister reshuffled his cabinet this July, sacking 4 ministers in order to go through the current political difficulty. In the following month, Finance Minister who led the economic reforms submitted his resignation to Prime Minister for lack of support for his conservative fiscal policy. Later, Finance Minister withdrew the resignation because he received enough support for his fiscal policies. JCR expects that reforms will continue to proceed, but closely monitor the political development and the stance of fiscal policy. As there will be plenty of time before the next general election to be held in 2005, an early election could be called depending on the outcome of a local election this October.

Main Economic Indicators: The Republic of Bulgaria

		1999	2000	2001	2002	2003 (f)	2004 (f)
Real GDP growth rate	(%)	2.3	5.4	4.0	4.8	4.6	5.0
CPI (annual average)	(%)	2.6	10.3	7.4	5.8	3.5	3.7
Unemployment rate (year-end)	(%)	16.0	17.9	17.9	16.3	15.5	15.1
General government balance/GDP	(%)	-1.0	-1.1	-0.9	-0.6	-0.5	-0.8
General government debt/GDP	(%)	84.7	80.6	69.9	60.7	50.3	46.1
Current account balance/GDP	(%)	-5.0	-5.6	-6.2	-4.3	-5.2	-4.7
Trade balance/GDP	(%)	-8.3	-9.3	-11.7	-10.2	-10.5	-8.9
Foreign Direct Investment/GDP	(%)	6.2	8.0	5.9	2.8	5.0	3.7
Import coverage	(months)	5.9	5.4	5.0	6.1	6.6	6.2
External debt/GDP	(%)	84.2	88.9	77.0	70.3	59.8	53.2
External debt/ exports (G&S)	(%)	188.3	160.0	138.4	132.2	119.8	117.0
Foreign exchange reserves/ short term external debt	(times)	2.5	2.4	2.9	3.1	3.3	3.1
Debt service ratio	(%)	18.0	16.7	20.1	15.8	15.3	16.3

Note: figures for 2003 and 2004 are JCR forecast.

Sources: Central bank, Ministry of Finance, IMF and EIU

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