According to flash estimates data of the National Statistical Institute, in Q2 2016, GDP growth in real terms was 3.0% yoy. The employment rate in Q2 increased by 0.8pp yoy reaching 49.5%. As a result, the unemployment rate decreased by 1.9pp to 8.0%. In July 2016, the consumer price index indicates a monthly inflation of 1.0%, breaking the deflationary trend. The coverage of the monetary base with FX reserves remained high in June (179.6%), which guarantees stability of the currency board. The current account balance was again positive in the second quarter of the year. The Netherlands was the leading foreign investor in Bulgaria for H1 2016, followed by Luxemburg and Great Britain. Lending continued declining in June 2016 in year-on-year terms, while deposits continued rising. Nevertheless, a month-on-month growth lending was observed in June.

**Higher GDP growth continued**

According to flash estimates data of the National Statistical Institute, in Q2 2016, GDP grew by 3.0% yoy in real terms, reaching the same growth rate as in Q1. The most significant component of GDP on the demand side - the final consumption (77.7% of GDP), increased by 2.0% yoy. The smaller GDP component - gross fixed capital formation (21.5% of GDP), dropped by 4.5%. The third component - the net export (0.8% of GDP) showed a positive value, supported by an increase in export and import by 2.0% and 2.2% yoy, respectively.
On the production side, in Q2, the output of industry went up by 1.1% yoy. By components, manufacturing industry rose by 2.3%, while mining industry and production of electricity, heat and gas each stepped down by 2.2%.

**Industry by sectors (% yoy)**

Unlike the industry, construction shrank by 11.7% yoy for the second consecutive quarter. Its decline was a result of a decline in buildings construction segment by 13.2% and a drop in the segment of civil and engineering construction by 10.0% yoy – mainly based on much weaker EU funds absorption for the period.

**Construction by components (% yoy)**

*Source: NSI*
Reflecting the positive dynamics of the GDP in Q2, the employment rate rose by 0.8pp yoy to a level at 49.5%. As a result, the unemployment rate decreased by 1.9pp to 8.0% eop. Both indicators showed positive dynamics of the GDP in Q2, as they are expected smoothly to improve.

Monthly inflation for July was 1.0% which broke the deflationary trend. It impacted the dynamics of the annual average deflation, which remained at its June level (-0.8%). On the other hand, the end-of-period deflation dropped to 0.1% in July (1.1% in June), due to increasing prices for food, alcohol and tobacco, restaurants and entertainment.

As of June 2016, the gross state budget not only remained positive but also accumulated a significant surplus of BGN 3.1 bn. The reason for that were accelerated revenue growth by 8.6% yoy and contraction of expenses by 4.5% yoy. The growth of total revenues was mainly due to rising tax revenues by BGN 1.2 bn yoy, as a result of increased consumption. On the expenses side, the drop was mainly caused by a contraction of capital expenditures by BGN 1.1 bn yoy.

Current account balance remained in positive territory in Q2 at EUR 381.7 mn, while for the same period last year the C/A balance was at EUR -205.6 mn. By components, trade balance deficit narrowed to EUR 320.6 mn in Q2 2016, which was by EUR 99.0 mn less than the deficit for the same period in 2015. As expected, the balance of services was positive, at EUR 462.6 mn, shrinking by EUR 68.5 mn yoy. The primary income continued to be negative with a balance of EUR 368.0 mn for Q2, which however was by EUR 396.6 mn less than the deficit for the period April - June 2015. In turn, the secondary income strongly supported the current account again by EUR 607.7 mn, i.e. by EUR 160.2 mn more than a year ago.

Foreign direct investment (FDI) in the country for Q2 totaled to EUR 410.9 mn, which was by EUR 39.1 mn more than the volume in Q1 2015. For H1 2016
the foreign direct investments in the country amounted to EUR 778.4 mn or by EUR 179.5 mn less than the level a year ago.

**Current account by components (EUR mn)**

![Chart](chart.png)

*Source: BNB*

Foreign direct investment (FDI) in the country for Q2 totaled to EUR 410.9 mn, which was by EUR 39.1 mn more than the volume in Q1 2015. For H1 2016 the foreign direct investments in the country amounted to EUR 778.4 mn or by EUR 179.5 mn less than the level a year ago. Within the geographical structure of the FDI, for H1, leading investors in the country were the Netherlands (EUR 189.8 mn), followed by Luxemburg (EUR 133.6 mn), Great Britain (EUR 110.8 mn) and Germany (EUR 80.1 mn).

**Positive signals for growth in lending**

In June, for the twentieth consecutive month, lending to businesses and individuals contracted by 1.2% yoy, reaching BGN 48.5 bn. Lending to non-financial enterprises registered a more significant drop by 1.5% yoy to BGN 30.3 bn, whereas lending to households decreased moderately by 0.7% yoy to BGN 18.2 bn. Against this background, a positive fact was the growth in total lending by 0.8% on a month-on-month basis in June, which was in a positive territory for the fourth consecutive month. If this tendency continues, which is
the most probable scenario; it will lead to a growth in lending also on an annual basis.

**Loans development (% yoy)**

![Graph of Loans development (% yoy)](image-url)

**Source: BNB**

Compared to the same period of 2015, lending in June 2016 was accomplished in the decreasing dynamics of the average nominal interest rates. Thus, the average nominal interest rate on loans to non-financial enterprises was 4.7% in June, which was 1.5pp less than the level a year ago. Interest rates on consumer and mortgage loans decreased by 0.8pp to 9.4% and 5.1%, respectively. The volume of deposits in June increased for the nineteenth consecutive month by 8.2% yoy, up to BGN 58.6 bn. By components, households’ deposits rose by 6.3% yoy reaching BGN 41.1 bn, while those of non-financial enterprises soared by 13.1% yoy up to BGN 17.5 bn. For the eighth consecutive month firms’ deposits registered a two-digit growth, which is a clear signal for a hindered investment process in the real economy, which also correspond with the decrease of investments in Q2. Moreover, in June, the average nominal interest rate on non-financial enterprise deposits lowered by 0.3pp to the minimum of 0.4% per annum. The rate on households deposits was 0.7% p.a. in June, a 0.7pp drop compared to June 2015.

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1 Average weighted value of nominal interest rates on loans (deposits) in BGN, EUR and USD.
Conclusions

In H1 2016, real GDP grew faster than anticipated, repeating the growth pace of 2015 (3.0%). Otherwise, main drivers were presently household consumption investments. Against this background, net export weakened. Indeed, the cheaper money, a consequence of the ongoing ECB’s QE policy, led to an increase in household consumption, which is pushing the GDP growth. Moreover, this tendency is considered to drive the GDP in H2 2016. Banking sector remained in a good condition finding the growth path in lending. Moreover, the results of AQR and stress testing demonstrated strong capital position of the sector. On the other hand, nearly all banks showed healthy capital positions also in adverse scenario simulations.

References

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