March 3, 2004
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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 04/10-1

2:30 p.m., February 4, 2004

1. Bulgaria—Stand-By Arrangement—Review, Extension, and Waiver of Nonobservance of Performance Criterion and Applicability of Performance Criteria

Documents: Bulgaria—Fourth Review Under the Stand-By Arrangement, Requests for Waiver of Applicability of Performance Criteria and Waiver of Nonobservance of Performance Criterion, and Request for Extension of the Arrangement (EBS/04/6, 1/16/04; and Supplement 1; 2/2/04)

Staff: Schiff, EUR; Muniz, PDR

Length: 1 hour, 20 minutes

Executive Board Attendance

A. Krueger, Acting Chair

Executive Directors	**Alternate Executive Directors**
	A. Al Nassar (SA), Temporary
	C. Faircloth (CO), Temporary
	G. Meissner (GR)
	H. Jang (AU), Temporary
	O. Basdevant (FF), Temporary
	C. Sia (ST), Temporary
	T. Ross (NO), Temporary
	N. Epstein (UA), Temporary
	J. Sipko (BE), Temporary
	D. Vogel (AG), Temporary
	A. Monajemi (MD), Temporary
	Y. Lissovolik (RU), Temporary
	E. Menye (AF), Temporary
	M. Martinez (CE), Temporary
	L. Rizzotti (IT), Temporary
	A. Maciá (BR), Temporary
	D. Prasad (IN), Temporary
	P. Williams (UK), Temporary
	S. Bakhache (MI), Temporary
	J. Milton (AE), Temporary
	Y. Wu (CC), Temporary
	Y. Yakusha (NE)
	N. Watanabe (JA), Temporary
	S. Antic (SZ), Temporary

A.S. Linde, Acting Secretary
H. Mooney, Assistant

Also Present
IBRD: R. Quintanilla, Senior Country Economist. European Department: J. Fagjenbaum, Deputy Director; G. Anayiotos, C. Cottarelli, C. Duenwald, P. Egoume-Bossogo, H. Flickenschild, B. Joshi, J. Schiff. External Relations Department: C. Lotze. Legal Department: M. Milford. Office of the Managing Director: A. Kammer. Policy Development and Review Department: C. Muniz, A. Pitt. Secretary's Department: A. Blazejewski, P. Ramlogan. Senior Advisors to Executive Directors: L. Croitoru (NE). Advisors to Executive Directors: M. Abbing (NE), K. Nauphal (MI), V. Yotzov (NE). Advisors to Executive Directors: S. Wolff-Hamacher (GR).

1. BULGARIA—STAND-BY ARRANGEMENT—REVIEW, EXTENSION, AND WAIVER OF NONOBSERVANCE OF PERFORMANCE CRITERION AND APPLICABILITY OF PERFORMANCE CRITERIA

The staff representative from the European Department (Mr. Schiff) submitted the following statement:

> This statement provides information that has become available since the issuance of the staff paper for the fourth review under the Stand-By Arrangement for Bulgaria (EBS/04/6). This information does not change the staff's appraisal in that staff paper.
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> The second of two prior actions for Board consideration of this review was completed on January 22, 2003, when the Bulgarian National Bank (BNB) announced a reduction, effective April 1, 2004, in the test period for classifying loans as loss from 120 to 90 days. Minimum provisioning for loans 61 to 90 days overdue has also been raised from 30 percent to 50 percent.
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> Indications are that all performance criteria for end-December were observed, with the exception of the ceiling on tax arrears to the General Tax Directorate, for which a waiver has been requested. In particular, staff has confirmed that the following performance criteria were observed: ceilings on contracting and guaranteeing public sector debt; the floor on the Fiscal Reserve Account (FRA); the ceiling on use of FRA resources to acquire policy-related assets; and the ceiling on arrears to the National Social Security Institute. Preliminary data on the performance criteria for which waivers of applicability were requested—the general government deficit and wage bill of selected public enterprises—indicate that these have been observed as well.
>
> Macroeconomic data point to further robust growth but also continued external risks. Industrial production rose by 11 percent year-on-year and industrial sales by 14 percent in November. The twelve-month external current account deficit rose to 8.75 percent of estimated GDP in November, up from 8.5 percent in October, with FDI coverage at 80 percent for the same period, and reserves roughly unchanged, at 5.2 billion euros. Year-on-year growth in bank claims on the non-government sector decelerated slightly for the second consecutive month in December, reaching 40.5 percent in real terms. Owing to higher food and fuel prices, December inflation was significantly higher than expected—1.8 percent month-on-month compared with a projected 0.7 percent—leaving end-year inflation at 5.6 percent.
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> Preliminary fiscal data indicate that a very small general government surplus was achieved in 2003, in line with understandings reached during discussions for the review. Both revenues and expenditures were some .75 percentage point of GDP higher than expected (net of tax arrears clearance

operations), with the additional expenditures largely in the social spheres and for arrears clearance.

The Bulgarian Privatization Agency has formally invited the winning bidder for the state telecommunications company, BTC, to sign the sales contract by February 20. Advent International has agreed to purchase 65 percent of BTC for 230 million euros and to invest a minimum of 400 million euros over the next five years.

Mr. Yakusha and Mr. Yotzov submitted the following statement:

The authorities wish to express their gratitude to the Fund for surveillance and assistance, which have been helping Bulgaria to make progress in its economic transformation as well as in preparation for EU accession. Over the last year Bulgaria has made further progress in placing the economy on market based principles. The overall implementation of the two-year Stand-By Arrangement supported program has been successful, macroeconomic performance has been good and the financial discipline has been maintained.

The authorities are well aware of the remaining challenges and risks and are strongly committed to continue the cautious policy they have embarked on. They are also deeply convinced that their efforts to preserve macroeconomic stability and sustainable growth will further success of the ongoing reforms in the run-up to EU accession.

Policy Framework and Recent Developments

The authorities' efforts continue to be focused on limiting the economy's vulnerability to risks and on achieving robust economic growth. The policy framework is based on (i) preservation of the currency board arrangement until EU entry and eventual euro adoption; (ii) implementation of a cautious and flexible fiscal policy, oriented toward sustainable economic growth and (iii) acceleration of structural reforms with a clear focus on European integration. The authorities are strongly committed to this policy framework, which allows them to address more effectively the still remaining problems.

Bulgaria's real GDP is expected to grow by about 4.5 percent in 2003, led by an increase in private consumption and fixed investment. A higher gross value added was generated in industry and service sectors, while the agricultural sector has contributed negatively to real growth mostly because of bad weather last year. Despite a hike in food prices at the end of the year, the annual average inflation has stayed under control supported mainly by a relatively large share of traded goods in the consumer basket and a neutral fiscal stance.

All end-September performance criteria under the program have been met with the exception of the criterion on tax arrears collection. This is due to the delay in privatizing a state-owned enterprise from which arrears payments are anticipated. Most structural benchmarks have been met as well, though some related to tax administration and expenditure management were not fully observed largely due to technical difficulties.

Bulgaria's progress towards EU membership received a broadly favorable assessment in the European Commission's annual report. Moreover, in December 2003 the European Council confirmed the draft declaration in support of Bulgaria's membership in the EU as of January 2007.

Fiscal Policy

The government's economic program has been underpinned by a sound fiscal policy, as it has been the case since the currency board implementation in mid-1997. Tax revenues were higher than projected. Non tax revenues have increased as well, supported by some reduction in discretionary and interest expenditure. In line with staff advice, the authorities agreed to address rising trade and current account deficits by saving a substantial portion of additional revenue, thus aiming at a balanced budget for the year, compared to the modest deficit that had been initially projected. Preliminary data indicate that a small general government budget surplus was achieved in 2003.

The 2004 budget continues the policy of gradually lowering the tax burden. The corporate tax rate has been reduced, minimum income exempted from taxation has been raised and the personal income tax rate for the lowest income bracket has been lowered. To offset these tax cuts, selected excise taxes (on tobacco, alcohol and gas) have been raised closer to EU average levels. In addition, the authorities committed themselves to further improve the tax administration, and to contain government subsidies. These measures are necessary to contain a rather small budget deficit, projected at 0.7 percent of GDP. Moreover, the authorities are ready to take additional measures, including further fiscal tightening, should the external conditions not improve. The fiscal stance is consistent with a modest decline in the external debt-to-GDP ratio as envisaged in the budget. In the last several years, the Bulgarian authorities have established a strong track record in responding flexibly to various shocks. They have also shown a consistent commitment to fiscal discipline.

External Sector

In spite of the economic slowdown in the EU, Bulgaria's main trade partner, exports have continued to perform well. The estimates show they

have increased by an impressive 9 percent in euro terms over the past year. This increase has been accompanied by a further shift of the geographical structure of exports towards EU countries, which also testifies to Bulgaria's sound competitiveness. The recent appreciation of the euro is likely to have only a moderate impact on external competitiveness and a mixed effect on the economy as a whole. Over the program period, imports have been driven mostly by the rise of investment imports, reflecting strong green field foreign direct investments. Net inflow of FDI in 2003 rose to a record high level since the beginning of the economic transformation up to about 7 percent of GDP. Broadly similar trends have been observed and addressed in a number of other transition countries (including those with a currency board). Bulgaria's foreign reserves have grown for the sixth year in a row in 2003. The debt burden continues to lessen, and, sustainability analyses show that in virtually all scenarios external debt-to-GDP ratios would further decline, implying that the medium-term current account is sustainable.

Financial Sector

The large role played by foreign banks (they represent about 90 percent of banking system capital) along with the tight banking supervision has secured financial stability in times of rapid credit growth. Although the increased banking sector intermediation is generally welcomed and has been long awaited, authorities have agreed on the need to slow credit growth to a more modest pace. The central bank has undertaken intensive surveillance of aggressive banks, tightened the definition of bad loans, and expanded the coverage of the credit register. It has also put off the discussion on lowering the minimum reserve requirements. If, contrary to the expectations and despite the already implemented measures, credit growth does not continue to decline, the monetary authorities will increase the frequency and the scope of reviews, and will implement additional measures. The government will also remain cognizant (in their asset management) of the need to contain credit growth within sustainable levels.

Structural Reforms

Overall progress on structural reforms has been good. With the privatization of the second largest bank in May 2003, the banking sector has been fully privatized. The restructuring and privatization of non-infrastructural state owned enterprises are approaching completion as well. A relatively small number of mostly large infrastructure enterprises, like energy and railway enterprises, remain in state ownership. The government had to delay the privatization of the telecommunication company (BTC) and tobacco holding (Bulgartabac). While the sale of the BTC is at the final stage, Bulgartabac is taking considerably longer, reflecting changes in the privatization strategy recently approved by the Parliament. The new strategy allows the sale of separate entities of the company after running a product-

orientated restructuring. The government believes this approach will secure strong investor interest.

On December 1, Bulgaria became the 55th subscriber to the SDDS, marking a major step forward in the development of the country's statistical system. Bulgaria now meets the specifications for coverage, periodicity, and timeliness of the SDDS data categories, and for dissemination of advance release calendars. Bulgaria was among the first group of countries who participated in the IMF's GDDS, and it is the third country to graduate from the GDDS to SDDS subscription.

Bulgaria has a vast growth potential ahead of accession and thereafter. However, the comparative advantages of low unit labor costs and high productivity gains can materialize only in a reasonable time frame, which would also require a substantial inflow of both direct and indirect foreign investment, as well as increased domestic confidence. The authorities had firmly adhered to the policy framework under the current program and they believe the implementation of this program provides a solid basis for a successor, precautionary Stand-By Arrangement.

Finally, the authorities consent to the publication of the staff paper.

Mr. Mozhin and Mr. Lissovolik submitted the following statement:

We thank the staff for a concise and insightful staff paper on Bulgaria. At the outset, we would like to state our support for the completion of the review as well as the proposed decisions. Our position is dictated by the strong performance of Bulgaria under the program, which improves Bulgaria’s track-record in Fund program implementation and raises the prospects of moving to a precautionary arrangement with the Fund in the future. Turning to the issues pertaining to the last review under the Stand-by arrangement, we continue to stress the overarching importance of fiscal prudence for the sustainability of the program. The case for keeping the fiscal stance in order is further accentuated by the high level of the current account deficit.

Fiscal Policy

On the whole, fiscal policy in Bulgaria has been strong, as evidenced by significant overperformance with respect to the level of the budget deficit. At the same time, while we understand the rationale for some flexibility in setting and attaining fiscal goals, clearly the first-best case is that of a transparent, rules-based budgetary framework. In Box 2 the staff suggests that the actual fiscal stance may be weaker, if below-the-line (B-T-L) items are taken into account. In this respect we wonder what the exact composition of these B-T-L items is, for their weight in the all-important fiscal indicator is

not insignificant. Also, is the inclusion of such items into the budget deficit dictated by the Fund's GFS methodology? If not, the information in Box 2 (even if accompanied by a detailed list of the B-T-L items) may engender needless uncertainty with respect to the actual fiscal stance in Bulgaria as well as its comparative standing versus other economies.

We welcome Bulgaria's steps aimed at reducing tax rates and curtailing subsidies in the railways and energy sectors. At the same time, the pattern of implementation of the fiscal parameters in the Fund program attests to the intrinsic difficulties in bringing down tax arrears, whose unwieldy character has been a veritable *bête noire* of the CIS economies in the past. As we noted during our previous interventions, the problem of arrears should be given major consideration on the part of the Bulgarian authorities in order to improve the payment discipline. Finally, our concerns pertaining to the use of FRA resources that had been raised on previous occasions remain valid with respect to the possibility of inefficient use of these resources in investment projects. The implications of the negative signal for the financial markets regarding the credibility and transparency of fiscal policy (which are so paramount for the sustainability of the program) will far outweigh any considerations associated with allocative inefficiency.

Structural Reforms

On the whole we agree with staff's assessment that structural reforms in Bulgaria have proceeded at a rather good clip. We are encouraged by the fact that banking intermediation in Bulgaria is accompanied by strong prudential supervision. We also welcome the transfer of government deposits from commercial banks to the BNB, which among other things should serve to contain bank lending. With regard to the developments in the labor market, the decline in unemployment is encouraging, though complacency needs to be avoided, for the sustainability of further declines in unemployment is not assured. The government will need to continue to promote active labor market policies alongside with measures aimed at advancing labor market flexibility. With respect to the pace of privatization we are encouraged by the recent break in the deadlock over the privatization of BTC. Further action to expedite the sale of Bulgartabac and other enterprises slated for privatization would serve to reinforce investor confidence in Bulgaria's economy and bring the country the long-awaited investment grade rating.

External Position

The sustainability of the country's external position largely hinges on the ability of the country to continue to attract FDI and in this regard the issue of the interaction between FDI inflows and the trade balance as well as the sustainability of FDI flows appears to be of relevance, particularly in the medium term. Firstly, the increase in profit remittances appears to have

outpaced the growth in FDI in the past 3 years, which raises questions about the nature and the sustainability of these FDI flows. Secondly, the reservoir of privatization proceeds is likely to be considerably depleted, particularly after the completion of the sales of BTC and Bulgartabac (in Table 10 the staff projects that privatization receipts will start to decline after 2003). Also, regional factors, including the accession of the CECs and the Baltic states to the EU ahead of Bulgaria, may disadvantage Bulgaria compared to the CECs in terms of exports and FDI vis-à-vis the EU. Furthermore, in case external factors delay Bulgaria's EU membership, this may adversely affect both FDI and exports. Finally, as trade liberalization forges ahead in Bulgaria, FDI as a mode of by-passing trade barriers may increasingly give way to direct imports from abroad, while FDI itself may become more import-intensive. Does the staff have any estimates of the export and import elasticities of FDI in Bulgaria and are there signs of increasing complementarity between FDI and exports?

Conclusion

The commendable reform efforts of Bulgaria's authorities have not been expended in vain, for macroeconomic stability has been largely attained, whilst growth continues to perform strongly. It is also encouraging that luck appears to be on the side of Bulgaria, whose reforms were rewarded by the recent discoveries of gold in Bulgaria's Rhodopes Mountains. However, neither good macroeconomic figures, nor even gold ounces will suffice in turning Bulgaria into a veritable success story, unless the authorities manage to translate the progress in economic reforms into a sustained rise in living standards. Indeed, while thus far economic performance has been strong and the commitment to economic reform on the part of the Bulgarian authorities is beyond any doubt, the sustainability of the reforms through strong ownership is not assured. The year 2004 will be the last respite before the parliamentary elections scheduled for 2005, presidential elections in 2006 and a push to join the EU in 2007. As the country braces itself for the challenges in the political domain, it will be important to approach these deadlines with a sufficient reservoir of economic strength and stability. We wish the Bulgarian authorities every success in meeting these challenges in the years ahead.

Mr. Shaalan submitted the following statement:

In spite of, and in contrast to, the economic slowdown in the European Union for the past three years, the Bulgarian economy continues to reap the benefits of generally sound macroeconomic policies and steady progress in introducing key structural reforms. The most notable accomplishments in the latter area are reflected in what appears to be a successful privatization program until recently and with it a number of policy actions promoting a market friendly business environment, which was supported by a meaningful beginning at reforming the judiciary. Economic activity has for the past

several years registered healthy growth in a low-inflationary environment and reduced the unemployment level. Notwithstanding these commendable accomplishments, we share the staff's concerns regarding the potential risks emanating from the high and increasing current account deficits and the related high level of private sector credit expansion, which again, following several years of sharp increases has reached extremely uncomfortable levels in the year just ended. The rest of our remarks will focus on these two issues.

The current account deficit, which now stands at some 8 percent of GDP, is reminiscent of the levels in a number of Asian countries at the outbreak of the crisis in the later part of the nineties. In fact, data from Bulgaria stands at the high end of the range observed for the Asian countries. At that time, the staff flagged these deficits as a major cause for the vulnerabilities that we are all too familiar with. However, the vulnerability analysis carried out by the staff for Bulgaria appears to show that the high current account deficit is not, at this time, raising any red flags. A variety of studies have shown that the predictive value of vulnerability indicators is low. We, therefore, have reservation on the value of this tool in assessing vulnerabilities. It would have been useful for the staff to look into the differences between the Bulgarian situation and that of the crisis ridden Asian countries of the nineties.

Undoubtedly, the high level of reserves and the fact that the current account deficit has been almost totally financed by non-debt creating capital inflows have been important factors in containing negative impulses from the external sector. However, it is important to note that these factors should not be relied upon to sustain these high current account deficits, particularly as the currency board arrangement limits the policy options open to the country to deal with a potential crisis. The staff's comments on these views as well as the comparability with Asian countries would be appreciated.

The high level of private credit, which has fuelled the healthy growth of the economy in recent years and contributed in no small way to the growth in the current account deficit, is a source of concern in at least two respects. First is the likely impact of this credit expansion on the current account deficit, and in the event that non-debt creating inflows were to decline significantly, on the country's foreign exchange reserves. Any sharp decline in these reserves could have a negative impact on confidence in the currency board arrangement. The second concern relates to the health of the banking system arising from the risks attached to an increase in non-performing loans (NPLs) associated with this high level of credit growth.

The above consideration would clearly suggest that priority needs to be accorded to the pursuit of a more active fiscal policy in the period immediately ahead. In this connection, tighter financial policies are called for. Generally, as noted in Mr. Yakusha and Mr. Yotzov statement, fiscal

management in Bulgaria has been prudent and flexible. This is most encouraging. We hope that the authorities will monitor fiscal developments during the current year with the aim of curtailing the current account deficit. In this connection, we concur with the staff's view that the budget for 2004 is somewhat expansionary, and in view of the projected increase in the rate of growth it would be prudent to target a small surplus for 2004. While the built-in flexibility in the conduct of fiscal policy provides room for the authorities to contain spending if revenue generation falls short of projections, we would appreciate some elaboration from the staff on whether this flexibility is adequate to allow the government to prevent a repeat of the experience of the past few years when revenue overperformance was spent in the last quarter of the year.

Efforts in the fiscal area should also aim at avoiding the emergence of off-budgetary operations and strengthening spending discipline. The potential for using Fiscal Reserve Account resources to capitalize a state highway enterprise in 2004, in addition to being inadequate from a cyclical point of view, could undermine the transparency of the budget and possibly create large government contingent liabilities. In this regard, while we welcome the authorities' decision to postpone this plan, we also encourage them to consider other, more transparent, means of supporting the country's infrastructure.

On monetary policy, we commend the authorities for their prudent management and the strengthening of prudential and supervisory regulations, including in particular the actions taken to limit risks arising from insider lending, but encourage them to be vigilant in monitoring credit growth developments. The increase in credit to the private sector in recent years does not appear of a cyclical nature, but seems to be associated with the reemergence of the banking sector as a viable financial intermediary in the country and may well have a large catching-up component. As noted above, the rate of growth has, however, reached levels that raise concerns regarding the potential deterioration in the quality of the banking sector assets in addition to the pressures it adds to domestic demand. In this context, we believe the measures agreed to by the authorities to tighten regulation, while stringent, are appropriate particularly given the limited policy options available to the authorities to influence credit. Moving forward, it is not all too convincing that the factors presented in Box 1 of the staff paper are likely to significantly reduce credit growth in 2004. The authorities are therefore encouraged to closely monitor these developments and, if necessary, increase liquidity requirements on a bank-to-bank basis.

With these remarks we again commend the authorities for their successful transition to a market economy and wish them continued progress.

Mr. Zurbrügg and Mr. Antic submitted the following statement:

Key Points

We support the completion of the fourth review given the sound macroeconomic results and the strong track record. However, risks have increased with the rapid credit growth and widening current account deficit.

Fiscal policy should not add to the external vulnerabilities and should continue to provide a solid foundation for the currency board. Structural reforms need to support the adjustment, while financial sector policies should be more proactive.

The finalization of the BTC sale sends a positive message to the investor community. We hope that the new strategy to sell Bulgartabac in individual units will produce similar results.

The efforts pursued by the authorities have yielded tangible macroeconomic results despite the prolonged economic slowdown in the EU. FDI inflows have been strong, reserves are still on the rise and the debt burden is decreasing. For the first time after 1997, some positive results were recorded in lowering unemployment. On the basis of the strong performance under the program, we support the completion of the fourth review, as well as the extension of the program.

While the progress achieved so far is commendable, the majority of the population has not substantially benefited from the reforms. The impatience is growing, the government has a very low rate of approval and there are voices within the government for raising public expenditures. Increasing expenditures can have some positive short-term effects for the government, but will pose significant medium and long-term costs. The only way to achieve higher living standards is by accelerating structural reforms while maintaining sound macroeconomic policies.

The growing external imbalance and rapid credit growth pose a serious risk for the Bulgarian economy. In order to limit these vulnerabilities, we concur with the measures proposed by the staff, namely (i) adapting fiscal policy to the macroeconomic environment, and (ii) strengthening structural reforms. Special attention should be given to financial sector policies to deal with unsustainable credit growth. In this context, we are concerned by what appears to be a wait-and-see attitude.

Fiscal policy provides a solid foundation for Bulgaria's currency board (CBA). The authorities should pursue a fiscal deficit target for 2004 that will help contain pressures on the external position and will also allow the government to meet its objective of a balanced budget by 2005. We regret the significant rise in the wage bill and the planned increase in public

employment. This decision is not consistent with the authorities' vision of a small and well-trained civil service.

Spending some of the fiscal reserve account (FRA) on capital projects might not be ideal in the situation of a growing current account deficit. We welcome the fact that the authorities will carefully analyze such an issue in collaboration with the IFIs and put this option on hold until the risks surrounding the macroeconomic environment are under control.

Financial sector policies are important in limiting external as well as internal macroeconomic risks. The BNB has strengthened its oversight and has made loan classification stricter. The government also intends to return the remaining deposits at commercial banks back to the BNB, and not to transfer new deposits to commercial banks. Although those measures will alleviate the situation, we think they are not sufficient to constrain credit growth that is projected to rise significantly in 2004. Credit in foreign currency is also rising and we are worried about the growing risks on the borrower side, because the currency composition of their revenues can impose significant problems for the banking sector. Can the staff elaborate on the risks stemming from excessive credit growth?

Another area that needs to contribute to reducing external vulnerability is debt management. That is the area, in which the authorities have already shown their competency that resulted in a decreasing debt burden. We welcome the authorities' intention to further increase the share of domestic debt in overall public debt and agree that it would be helpful to use a portion of the assets accumulated in the FRA to repay external debt. However, some projections do not bode well for the overall strategy of decreasing the debt burden. First, significant government investment based on borrowing from abroad is projected in 2004 (286 million euros), which is the opposite of the experience over the last five years. Second, short term debt is on the rise as a percentage of total debt. Third, we are puzzled by the projected financing of the fiscal deficit in 2004. Staff comments on these issues would be appreciated.

Structural reforms in several areas are still needed to reduce the pressure on the budget, to improve the business climate and attract future FDI, and to reduce the vulnerability of the economy in general. The agreement on privatization of BTC sends a positive message to the investor community and will strengthen investor confidence. We hope that the new strategy to sell Bulgartabac in individual units will produce results as anticipated. Work also needs to continue regarding the reform of the energy and the railway sectors as well as regarding the reform of the judiciary.

Finally, we welcome that Bulgaria has recently moved from GDDS participation to SDDS subscription.

Mr. Le Fort and Mr. Vogel submitted the following statement:

Key Points

Bulgaria has shown remarkable progress in its macroeconomic performance. However, the trend of the external current account is an increasing source of concern.

A further strengthening of the euro against the dollar could deepen the imbalance. We wonder to what extent the higher shares in the EU market represent a creation of trade rather than a deviation from other regions.

While we welcome the fiscal performance in 2003, we believe that the 2004 budget can raise some reasons for concerns.

Financial sector policies, and more specifically, limiting the credit expansion by commercial banks will play a crucial role in the adjustment.

We are encouraged by the progress in the structural area. However, much remains to be done, particularly in governance and in the effectiveness of the judicial system.

At the outset, we support the proposed decision. Bulgaria has shown remarkable progress in its macroeconomic performance, with strong GDP growth, and falling inflation and unemployment rates. However, vulnerabilities seem to have increased as the external current account deficit has widened about 8 percent of GDP, according to recent estimates. Moreover, political constraints prompted by the government's low popularity may delay further progress of much needed structural reforms and eventually deteriorate macroeconomic performance.

The widening trend of the current account deficit is an important source of concern. We are aware that FDI inflows have financed a substantial portion of the external deficit and that the continued decline in the spread of the Bulgarian component of the EMBI+ index reflects the market's strengthening confidence in the country and, thus, financing the external deficit does not appear currently to be a problem. Nonetheless, a further strengthening of the euro against the dollar could deepen the imbalance even more, and an increase in interest rates in advanced economies may prompt a widening of spreads and deteriorate confidence. The staff paper underscores that higher market shares for Bulgaria exports in the EU market suggest that the country has maintained its competitiveness. Indeed, Figure 9 of the staff paper shows that Bulgaria, like other transition countries, has gained an increasing share of EU imports. But we believe that an assessment of competitiveness should consider the evolution of shares in all markets, and not

only the euro zone, particularly considering that the latter is likely the only one against which Bulgaria's currency is not appreciating. We wonder to what extent the higher shares in the EU market represent a creation of trade rather than a deviation from other regions. Moreover, according to the Economist Intelligence Unit, whereas in the first quarter of 2003 investment goods were the fastest growing category of Bulgaria's imports, consumer goods have taken the lead in the second half of the year, which could constitute another worrying signal of lower competitiveness of local production. Maybe staff can elaborate more about recent trends of private consumption and investment, and to what extent they could be signaling competitiveness problems.

Given the constraints that the currency board arrangement imposes, fiscal policy should assume part of the burden in containing the external current account deficit. In this regard, we welcome the fiscal overperformance that generated a balanced budget in 2003. Staff underscore that the response on fiscal policy to these risks has been adequate, though not ideal. We understand the benefits of a tighter fiscal policy under current conditions to prevent higher external vulnerabilities. However, there are other constraints that need to be overcome. A program with good chances of being successful may be put at risk when the adjustment goes beyond what is politically feasible. The authorities should make a significant effort to explain the nature of the problem and the role that fiscal policy should play under the currency board system, and stand ready for a flexible use of the fiscal tools at their disposal. In particular, the rate of expansion of public outlays should be controlled. We welcome the authorities' commitment to maintain sufficient flexibility to achieve a balanced budget if external conditions warrant, as Mr. Yakusha and Mr. Yotzov note in their helpful statement. However, we have to underscore that the 2004 budget can raise some reasons for concern. Even though public wages have been low in relative terms, their projected significant increase may be an improper signal in the current macroeconomic environment.

Since the widening of the current account deficit originated in the private sector, it would be impossible to address it using fiscal policy alone. Therefore, financial sector policies and, more specifically, limiting the credit expansion by commercial banks will play a crucial role in the adjustment. In this vein, we are encouraged by the authorities' decisions to carry out several measures aimed at tightening banking supervision and slowing credit growth, particularly the reduction in the test period for classifying loans as losses, and the postponement of plans to reduce banks' reserve requirement to levels more in line with EU countries. We find merit in the consideration of contingent measures in case credit growth fails to slow down, such as the increase of liquidity requirements on a bank-by-bank basis and exploring the possibility of transitory restrictions on capital inflows.

The authorities have made very good progress in the structural area, even though much more will be necessary. According to governance indicators from the World Bank paper, "Governance Matters" (Kaufmann, Kraay, and Zoido-Lobatón), Bulgaria showed a significant improvement between 1996 and 2002 in voice and accountability (from 0.16 to 0.56), and regulatory quality (from -0.12 to 0.62). Progress has also been made in controlling corruption (from -0.62 to -0.17), but the sign still remains negative, which is compatible with the trend observed in the Transparency International indicators. Meanwhile, the aforementioned paper shows slower progress in the rule-of-law indicator (from -0.09 to 0.5). At the same time, the Heritage Foundation, in its 2004 Index of Freedom says, "based on new evidence with respect to the level of corruption in the judiciary, Bulgaria's property rights score is 1 point worse this year". On this same matter, in November 2003, Oxford Analytica underscored that Bulgaria's judicial system remains a substantial stumbling block to moving towards a fully functioning market economy and is widely considered slow and inefficient, as well as open to bribery and corruption. Nonetheless, the staff paper notes that "notable progress has also been made in reforming the judiciary, although sustained efforts over a number of years will be required". Perhaps the staff can elaborate more on the different assessments about the progress achieved in this area, and, especially, on the arguments for reaching their conclusion.

Mr. Wang and Ms. Wu submitted the following statement:

At the outset, we thank staff for a well-balanced paper and Mr. Yakusha and Mr. Yotzov for their candid and informative statement. We congratulate and commend the Bulgarian authorities for their impressive macroeconomic performance and constructive implementation of the Stand-By Arrangement amid the slowdown in EU countries. Supported by strong domestic demand, GDP grew robustly by about 4.5 percent in 2003. Inflation is in check, unemployment on the decline, FDI inflows are strong and reserves are rising. Based on these achievements, we support completion of the fourth review under the Stand-By Arrangement, and the requests for waivers and extensions.

While we praise the authorities' efforts to reduce vulnerability to risks and achieve robust economic growth, we caution them on challenges they face down the road to EU accession, especially with regard to the external position and credit growth. We encourage them to intensify the impetus of the structural reform agenda to alleviate the fiscal burden. Since we broadly concur with staff's appraisal, we will briefly touch upon some major issues for emphasis.

Credit Growth

While strong credit growth, on the one hand, encourages economic development, on the other hand, it may incite credit risk and threaten the current account position because of increased imports. It is reassuring that the authorities are fully aware of the situation. The central bank has undertaken intensive measures and the authorities are committed to taking additional measures should credit fail to slow. In addition, the authorities are making efforts to curtail this risk in their debt and asset management.

In Box 1, staff provides reasons for the likely slowdown in private sector credit growth. Does staff see any need for the authorities to take additional measures in the near future to further the current slowing trend?

External Position

Due to the tight fiscal policy, the budget recorded a surplus, which is significantly better than programmed. While we commend the authorities for containing the external imbalance and their impressive export record, we consider this imbalance is still too high. Therefore, a further tightening would be preferable. However, the staff projects, the external current account deficit are expected to narrow over the medium term while the medium-term current account appears sustainable. We agree with the authorities' "flexible and cautious" policy for 2004 providing they are ready to tighten the stance should external conditions fail to improve.

Structural Reform

One of the risks staff mentions in the staff paper is that FDI will not develop as expected. We, therefore, welcome the improvements in the business environment to attract more FDI. Reforms in the railway and energy sectors have also been impressive.

On the scheme to capitalize a state highway enterprise, we share concerns that the proper approach to road construction should be considered carefully. Since this plan is currently on hold, the authorities may have more time for wider consultation or a cross-country analysis on similar projects.

With these remarks, we wish the authorities every success in their future reform endeavors.

Ms. Jacklin and Mr. Epstein submitted the following statement:

Key Points

We welcome the continued good performance in implementing the Stand-By Arrangement.

The authorities continue to take important steps to strengthen the fiscal position and realize a more competitive and flexible economy.

But fiscal transparency and budget discipline are at risk through the proposed private / public partnership, and key structural reforms and privatization still lag.

The high current account deficit, at about 8 percent of GDP, continues to pose a threat to stability, although we note the high coverage by FDI and the rise in official reserves.

We also agree that excessive private-sector credit growth is a source of risk to the overall macroeconomic framework.

Fiscal Issues

We welcome the improvement seen in the fiscal position, with the general government achieving a small fiscal surplus in 2003 and a deficit of 0.7 percent of GDP projected in 2004. We note that there was some revenue overperformance in 2003, partly reflecting the deterioration in the current account deficit (higher customs duties, VAT, and excise taxes). Fiscal consolidation has remained broadly intact, and we agree that some additional fiscal tightening is both desirable and possible. We urge the authorities to continue to make efforts in this direction.

Regarding the broad objective of reducing vulnerability in the management of external assets and liabilities, we concur with the recommendation to use FRA resources to lower external debt via buy backs, as noted in paragraph 20. We strongly agree with the staff that this is a better use of FRA resources than the proposed capitalization of the state highway and other enterprises, as described in paragraph 16. Indeed, the staff is correct to note that increased reliance on budgetary spending channeled through state enterprises and joint ventures would undermine expenditure control and jeopardize important gains made so far in the area of fiscal transparency. In our view, these types of spending also directly undermine the Fund's balance sheet approach by raising the risk of sizable and unaccounted—for contingent liabilities.

Monetary and Banking Sector Issues

On the monetary side, the rapidly expanding credit to the private sector remains a concern, and we agree with the staff on the need to limit credit growth and the associated macroeconomic risks. Strengthening bank supervision ought to help in that regard. As to the proposed monetary remedies described in paragraph 18, such as postponing a planned reduction in banks' reserve requirements, we wonder if these are sufficient to curb credit growth in the near term and whether more stringent measures are needed? That said, we agree with the decision to shift government deposits from the banking sector back to the BNB, as part of a strategy to contain bank lending.

Structural Issues

The privatization agenda remains incomplete, notwithstanding the progress made in establishing a more market-friendly business environment. Delays in the key privatizations of BTC and Bulgartabac have adversely affected investor sentiment. We thus join the staff in urging the authorities to complete these sales quickly and transparently. In that regard, we welcome recent reports suggesting that the BTC sale is expected to be finalized by February 20. Since Bulgartabac is unlikely to be sold soon, as confirmed by Mr. Yakusha and Mr. Yotzov's helpful statement, we wonder about the implications for the collection of tax arrears. In the energy sector, we welcome the restructuring of district heating companies, initiating privatization of power distribution companies, and the passage of the Energy Law.

Post Stand-By Arrangement

We note from the staff paper and Letter of Intent that the authorities intend to request a successor precautionary Stand-By Arrangement. Bulgaria has been a strong performer in recent years, but it is also a prolonged-user of Fund resources. We therefore look forward to the results of the interdepartmental ex post assessment of Bulgaria's Fund programs. We assume that any request for a follow-on Stand-By Arrangement with Bulgaria would be considered after the Board has had an opportunity to review fully the ex post assessment.

Finally, we welcome Bulgaria's subscription to the SDDS, commend the authorities for their consent to publication of the staff paper, and wish them success in fully implementing the remaining program objectives.

Mr. Meissner and Ms. Wolff-Hamacher submitted the following statement:

Macroeconomic developments have been favorable and the program remains largely on track. We, therefore, agree to grant the requested waivers of applicability and of non-observance of performance criteria and support the

completion of the fourth review under the Stand-By Arrangement, as well as the extension of the program.

We broadly agree with the staff's analysis and recommendations. In particular, we share their view that the main risks for Bulgaria are that credit growth will not slow and that FDI will not develop as expected. We have several additional remarks and questions.

We commend the authorities for their successful restructuring of the privately-owned banking sector and welcome the deepening of financial intermediation. However, we share the staff's concern about the rapid growth of private sector credit. While bank profitability has improved and prudential indicators have not deteriorated so far, there is still a risk that asset quality could weaken, particularly if credit growth would not slow as expected. Further rapid credit growth could, as the staff pointed out, also lead to higher current account deficits. We therefore, encourage the authorities to continue to closely monitor bank balance sheets with regard to the quality of loans and currency and maturity mismatches, and to carefully assess the risks arising from the growth of mortgage and consumer loans. We welcome the steps already undertaken to contain credit growth and the intention to implement further measures if needed.

Equally important is a continuation of tight fiscal policy. The budget surplus for the first nine months of 2003 amounted to 2.5 percent of GDP and to a small surplus for 2003 as a whole (based on preliminary data). We understand that the overperformance due to higher than expected revenues was used in the fourth quarter of 2003 for arrears clearance and additional spending. Here we have several questions. Against the background of the high current account deficit we wonder if a higher surplus for 2003 would not have been possible and advisable. Can the staff provide any information if the revenue overperformance is expected to be sustainable? Also, can the staff give us further details on the kind of spending that is envisioned; particularly one-off expenditures, and how they might impact future budgets? Finally, what will be the impact of the additional spending on the current account in 2004 and beyond? In any case, we encourage the authorities to improve tax administration and budgeting and expenditure management. We also support the staff's recommendations to aim for at least a balanced budget or a small surplus in 2004.

Like the staff we are critical of the envisaged capitalization of a state highway enterprise with Fiscal Reserve Account resources and the creation of other enterprises that would also be capitalized by FRA resources. Such measures might be interpreted as a backward step toward interventionist policies. We also agree with staff that in the case of Bulgaria the macroeconomic impact could be badly timed (i.e. it could produce additional pressure on the current account), that this would weaken transparency and

create contingent liabilities that could complicate budget control. However, staff has in other cases in the past supported Public Private Partnerships (PPPs). We are not aware of a general analysis by staff on PPPs and wonder if this—if not yet existent—could be considered by the Fiscal Affairs Department.

Like the staff we strongly encourage the authorities to continue the implementation of structural reforms, not least to secure FDI inflows necessary for the financing of the current account deficit. This should include in particular a strengthening of the business climate and a reinvigoration of the privatization efforts.

We welcome the re-transfer of Fiscal Reserve Account resources from commercial banks to the BNB. We also welcome that Bulgaria is now a subscriber to the SDDS.

Finally, regarding the authorities' interest in a successor precautionary Stand-By Arrangement, against the background of a positive macroeconomic outlook, the prolonged use of Fund resources, and the fact that as of now the medium-term current account appears sustainable, we expect the forthcoming ex post assessment to thoroughly analyze what could be the basis for a precautionary Stand-By Arrangement.

With these remarks we wish the authorities success.

Mr. Usman submitted the following statement:

We thank the staff for the informative staff paper on Bulgaria, and Messrs. Yakusha and Yotzov for a helpful statement. Bulgaria has made good progress under the current Stand-By Arrangement. The solid economic growth under the program contributed to a decline in unemployment. A low level of inflation was also maintained under the currency board arrangement. We commend the authorities for their determination to keep the program on track in implementing most of the program parameters, notwithstanding some political difficulties relating to the strength of the coalition government.

Financial and External Sector Developments

Bulgaria's current account balance increased significantly to almost 8.5 of GDP reflecting a surge in exports. We concur with staff that the trend in the external balance is worrisome, even though it may be slightly overestimated. The staff also points out that the surge in imports is largely credit driven. This situation is confirmed by a strong rise in credit to the private sector. While the prudential indicators do not yet indicate a deterioration in the banking sector, we would urge the authorities to keep a watchful eye on credit expansion. We are reassured by the statement of

Messrs. Yakusha and Yotzov that the central bank has undertaken intensive surveillance on aggressive banks, tightened the definition of bad loans, and expanded the coverage of the credit register. The authorities should also press ahead with the implementation of their broad objectives of asset and liability management in order to reduce vulnerability and deepen the domestic securities market.

Fiscal Policy

The authorities have correctly tightened fiscal policy within the context of the currency board arrangement, which also helped contain the large current account balance. We commend the authorities' intention to maintain a prudent fiscal stance for 2004, with the needed flexibility to respond to the shocks, should they occur. The intended change in tax policy to lower the corporate tax rate could enhance incentives to invest and work. However, given the projected increase in the government's wage bill of 14.5 percent, we would urge the authorities to control other expenditures to meet the 2004 fiscal objectives. We would also urge the authorities to proceed with the implementation of structural reforms in the fiscal area to ensure medium-term fiscal sustainability.

Structural Reforms

Bulgaria has made substantial progress in implementing their privatization program. The staff, however, urge for a quick and transparent completion of the privatization of the BTC and Bulgartabac. It is our view, however, that the pace of privatization should be determined by the authorities. Under the prevailing circumstances, in this regard, we concur with Messrs. Yakusha and Yotzov, that while the privatization of these entities took longer to complete, it still falls within the strategy approved by Parliament.

Other Issues

Bulgaria has made substantial progress while implementing the Fund-supported program. They became the 55th country in December 2003, to subscribe to the Fund's SDDS framework, following its graduation from the GDDS framework. We expect the country to sustain this progress in the future, which will be further enhanced by accession to the European Union. We would support a successor precautionary Stand-By Arrangement, if requested by the authorities.

We wish the authorities every success in their future endeavors.

Mr. Ondo Mañe submitted the following statement:

At the outset, we would like to thank Mr. Yakusha and Mr. Yotzov for their insightful statement as well as the staff for the well-written staff paper.

The Bulgarian authorities have maintained efforts toward advancing structural reforms and achieving the stabilization of the economy under the Stand-By Arrangement. With the exception of the end-September performance criterion on tax arrears collection and the indicative targets on arrears of the electric company (NEK), all performance criteria and most structural benchmarks were met. Macroeconomic performance has continued to improve in 2003, led by strong industrial production, and a sharp increase in private consumption and investment. Moreover, GDP is anticipated to have increased by more than 4 percent during the first nine months of 2003, inflation is under control and the unemployment is steadily declining. Also, the widening of the current account due to substantial increase of imports was balanced by stronger-than-expected FDI inflows and the repatriation of foreign assets by commercial banks, thus contributing to covering current account deficit and increasing reserves.

Although the restructuring of the health sector has proved more difficult, good progress was made in other structural reforms, notably with the privatization of the government-owned commercial bank (DSK), the rise in the electricity and heating prices at cost-recovery levels, as well as the enhancement of the business climate through the strengthening of the judiciary system and the rationalization of the licensing regime. The authorities should be commended for all these achievements. Since we broadly agree with the staff's assessment, we support the proposed decisions and will limit our comments to a few issues.

Fiscal Policy

On fiscal policy, we welcome the authorities' resolve to further fiscal discipline. In this regard, the projected over performance in revenue collection will help reduce the deficit as the government will offset unbudgeted spending with the expenditure cuts, and efforts towards fiscal decentralization will be advanced through funding of municipal mandated spending. Although faster economic growth is anticipated, we are pleased to note that the tight budget stance of past years will be maintained, government subsidies contained and quality of spending improved. Also, a close monitoring of developments in the wage bill and public employment is critical to achieve the fiscal targets in 2004.

Structural Reforms

The authorities' committed to pursuing structural reforms in the prospect of joining the EU is welcome. Regarding the strengthening of tax administration, a pilot project aimed at improving the National Revenue Agency (NRA) was initiated, and a legislation establishing a single identifier for tax purposes will be enacted. We encourage the authorities to address technical constrains slowing down the implementation of the Financial Management Information System, the extension of program budgeting to more ministries, as well as the expansion of the Treasure Single Account coverage.

In the privatization front, we note the authorities' commitment to pursuing the privatization and restructuring of additional state owned enterprises with technical assistance from the World Bank. In this regard, the ongoing sale of the telecommunication company (BTC) and the strategy to sell the tobacco holding (Bulgartabac) into separate entities are going in the right direction. We welcome efforts to restructure railways and energy sector. However, with regard to the reforms of the railway sector, we share the staff's concern on the need for broader political support in this area. We recognize the need for the authorities to favor commercial enterprises for road construction and encourage them to proceed in consultation with the staff.

Finally, we are encouraged by the resolve of the authorities to enhancing the competitiveness of the economy through facilitating dialogue among social partners, updating the labor code and promoting flexibility in employment contracting. These measures are positive steps toward the market-friendly business environment, the diversification and the strengthening of the Bulgarian economy.

With these few remarks, we wish the authorities success in their endeavors.

Mr. Andersen and Mr. Ross submitted the following statement:

Key Points

Bulgaria's performance under the program continues to be good. To sustain the stabilization efforts, high foreign direct investments and reinvigorating the structural reform agenda will remain important under challenging political circumstances.

We concur with the focus on containing the risks associated with the widening current account deficit and rapid credit growth. A stronger fiscal stance and lower public debt, as well as further advancing structural reforms, would enhance the credibility of Bulgaria's currency board arrangement

before and after the EU accession. In that regard, the authorities would seem well advised to consider a tighter fiscal policy stance and to run sustained fiscal surpluses over the medium term.

We share staff's concern about excessive credit growth. We welcome the steps taken by the central bank in that regard as well as the plans concerning possible additional measures.

We see merit in considering a possible precautionary successor arrangement. Such an arrangement could serve as an additional strong external anchor during the run-up to EU accession.

We would like to thank staff for the comprehensive and informative staff paper and Messrs. Yakusha and Yotzov for their insightful statement. We broadly share staff's appraisal and support the proposed decisions. We also commend the authorities for subscribing to the SDDS.

Bulgaria's economic development continues to be promising. The output expansion has remained brisk, and the authorities deserve credit for keeping the structural reform agenda broadly on track despite their political difficulties. Indeed, Bulgaria's performance since 1997 is an example of the highly positive role of the Fund's engagement in the presence of truly strong domestic ownership, which in turn is induced by Bulgaria's prospective membership of the European Union. Therefore, while we can agree with staff that Bulgaria's risks are intensified since the third review, we would like to emphasize that these risks are completely different as compared to the challenges that the country faced just a few years ago. The two immediate macroeconomic challenges—the pressure on the external balance and rapid credit growth—are at least partly a consequence of the successful macroeconomic stabilization and determined structural reforms. This combination has resulted in the perceived reduction of the risk profile, a phenomenon observed in many EU acceding countries.

The overarching objective for the authorities in 2004 and in the medium term is to maintain rapid output expansion in order to foster real convergence towards the European Union. To sustain a high productivity increase underpinning the growth will likely necessitate a higher investment propensity as Bulgaria's investment-to-GDP ratio is lower than in some other acceding countries. Thus, sizable foreign investment inflows may continue to be needed to supplement domestic savings, underscoring the need for improving the business climate. We agree with staff that maintaining the sustainability of the current account is the most important challenge for the authorities. Fiscal and financial sector policies should provide adequate cushion against possible external shocks. This together with further structural reforms should enhance the opportunities for high and sustained inflows of foreign direct investments.

Fiscal policy has been broadly adequate thus far, but we believe that the authorities could consider a somewhat tighter fiscal stance than envisaged in the 2004 budget and for the medium term. We support the authorities' intention to save any extra revenues in 2004 if the budget performance would be stronger than expected. A stronger budgetary position would also be warranted from the purely cyclical prospective as economic growth is likely to accelerate this year. We welcome the authorities' continued emphasis on fiscal discipline and their preparedness to further tighten fiscal policy should the external conditions not improve. Early design of contingency measures in that regard is recommendable. Over the medium term, it would seem prudent to run sustained surpluses in view of the external vulnerabilities. Targeting budget surplus or balance over the medium term would also bring Bulgaria's fiscal policy in conformity with the requirements of the Stability and Growth Pact.

From a monetary policy perspective, a stronger fiscal stance would enhance the credibility of Bulgaria's currency board arrangement before and after EU accession. Most importantly, it would increase the necessary budgetary cushion against the backdrop of a relatively large current account deficit and the likely increase of private foreign liabilities over the medium term.

We support the approach that the authorities have taken in addressing the strong credit growth. Rapid increase of private credit is perhaps inevitable taking into account the prospects of the EU accession and the expected rise of real income, combined with the still low credit-to-GDP ratio. Against this backdrop, stronger capital and liquidity cushions—most likely exceeding those of the mature financial systems—could be instrumental to mitigate the potential risks and to maintain the credibility of the fixed exchange rate, even if the banking system is owned by foreign investors. We welcome the steps already undertaken by the central bank as well as the plans regarding possible additional measures. A bank-specific approach in discussing the business strategies, assessing their risk management practices and increasing the frequency of on-site inspections is welcome. At the same time, the efficiency of moral suasion may have its limits and it is, of course, a matter for judgment by the authorities how deeply the supervisors should become involved in controlling the implementation of concrete business strategies of individual banks. In this regard, we would appreciate staff's comments on whether additional tightening of some prudential regulations could be considered. On monetary measures, we fully concur with the authorities that loosening of the required reserve ratios toward the EU levels would not be appropriate at this time. The decision to deposit public funds with the central bank is also very welcome. It is, however, rather uncertain whether these steps would have a direct short-term impact on the credit growth rates. In any case, sustained vigilance is required.

Structural reforms should continue to increase the efficiency of fiscal management and to support the long term sustainability of the economic growth. On longer term fiscal priorities, increasing the share of the National Health Insurance Fund in covering the hospital spending is of paramount importance as it would strengthen the direct and transparent link between public health care services and the sources of their financing. In addition, we would underline the importance of defining a clear rule for indexing the public pensions, as indicated in the appendix on the Bank-Fund relations. On other structural issues, the authorities should be commended for overall good progress, most notably in the energy sector, and in pressing forward with the privatization despite the current stage of the political cycle. At the same time, the unfinished structural reform agenda needs attention and plans to increase the role of public sector enterprises should be resisted. In this regard, we join staff in their opposition to allocate resources from the Fiscal Reserve Account to capitalize state enterprises.

Finally, we see merit in considering a possible precautionary successor program. As in a number of other EU accession countries, such a program could provide for Bulgaria's graduation from the Fund's financial support and serve as an additional external anchor during the run-up to EU accession. At the same time, we would like to underline that a precautionary arrangement will fulfill its purpose best only if its fiscal and structural conditionality is sufficiently strong. It should take into account Bulgaria's medium term Pre-accession Economic Program.

Mr. Yakusha made the following additional remarks:

As several Directors have indicated, the Board may have diverging views regarding the timing of an ex post assessment, and how this might impact discussions concerning a possible follow-up arrangement. In this context, the authorities would like to avoid any delay in the initiation of discussions for such an arrangement. During the previous Board discussion on ex post assessments, the prevailing view of the Board was that such exercises should not lead to unnecessary bureaucratic delays in the initiation or negotiation of programs, which might adversely affect the countries being assessed; this is particularly relevant in the context of follow-up arrangements.

Several Directors also commented on current account sustainability. The authorities are aware that the high coverage of the current account deficit by greenfield FDI is potentially problematic. However, the estimated current account deficit is likely to be revised downward by one percent of GDP owing to previous technical difficulties in capturing tourism receipts. Recent data indicates that tourism increased by as much as 18 percent last year, but that preliminary data on such receipts only showed a 2 percent increase.

Finally, several other transition countries also maintain currency board arrangements, including Estonia and Lithuania, which have been able to sustain high current account deficits that were also largely covered by significant FDI inflows. In this light, Bulgaria does not seem to be a unique case.

Extending his remarks, Mr. Epstein agreed that any unnecessary delay in the negotiation of a follow-up arrangement with the Bulgarian authorities should be avoided. Nevertheless, he hoped that any request for a follow-up precautionary arrangement could be considered by the Board after an ex post assessment had been completed, while noting that the negotiations for such an arrangement could begin immediately.

The staff representative from the European Department (Mr. Schiff) made the following additional remarks in response to questions and comments from Directors:

There were several questions about the advisability of stronger fiscal performance in 2003. The staff considers that a stronger performance in 2003 would have been advisable. While saving half of the revenue overperformance was an adequate policy response, the authorities missed an opportunity to save even more of these funds at the end of 2003, when revenue performance exceeded expectations. Almost all of the authorities' additional spending was non-recurring, mainly in the form of wage and pension bonuses, social assistance for laid-off military employees, and the clearance of arrears. Thus, these expenditures will not carry over into 2004. However, the public is now likely to expect a recurrence of such spending, which might be politically difficult to dismiss.

On the revenue side, one Director asked if a similarly strong fiscal performance is envisioned for next year. Given that the authorities' excellent performance in 2003 was caused in part by macroeconomic developments—e.g., higher than expected import-associated revenue, which is not likely to reoccur—the staff does not consider such strong revenue performance likely in 2004. However, revenue projections for next year are quite cautious, so there could be some degree of fiscal overperformance.

One Director asked if spending at the end of 2003 will have an additional negative impact on the current account in the future. We believe it will not, as staff accurately projected the fiscal deficit for 2003, and because the expansion at the end of the year was very similar to that which took place during the previous two years. Thus, the impact of such spending on the current account has been reflected in the current projections.

There were several questions from Directors about whether there was sufficient flexibility in the 2004 budget. From a technical perspective, the staff considers that the current budget contains sufficient contingency measures, as it provides an appropriate level of flexibility—of about 1.5 percent of GDP.

Revenues are also conservatively projected, which provides the scope for some degree of adjustment. However, the amount of adjustment that might actually be undertaken depends on the authorities' political will to do so.

There were several questions about below-the-line-spending items. There are about five such items, which were largely transfers used to capitalize several state enterprises, including the forestry and energy companies, as well as the possible capitalization of the road enterprise. The government is treating such expenditures as financing items, in the sense that they represent the acquisition of policy-related financial assets. The staff considers this practice to be consistent with GFS 2001, although there is some degree of ambiguity with respect to the guidelines. The important issue is how subsequent expenditures by such enterprises are captured in the budget. For example, the initial capitalization of the road fund could plausibly be considered a below-the-line item, but it is unclear whether activities carried out by the fund in the future should be reflected in the fiscal accounts, which would depend to some degree on the precise nature of such transactions. The Fiscal Affairs Department is producing a paper that will address these issues in detail.

There was a question about tax arrears related to Bulgartabac. The delay in the expected privatization of Bulgartabac caused a shortfall in arrears repayments, which caused the authorities not to comply with one performance criterion. We expect the privatization of Bulgartabac to resume in mid-2004, at which time arrears repayment should continue. Ultimately, difficulties with collecting arrears relate to the fact that few large enterprises have a significant share of arrears, but do not have the capacity to repay them at this stage.

There were several questions related to rapid credit growth. There are two main risks associated with this phenomenon. First, despite the fact that banking sector indicators appear quite strong, there may be prudential risks ahead. Second, there are macroeconomic risks associated with the pace of credit growth, which feed directly into import growth. Nevertheless, risks related to the growth of foreign exchange lending has declined, as such credit growth has slowed considerably during the last half of the year, and foreign exchange lending is shifting from dollar-denominated lending to lending that is dominated primarily in euros. Thus, the associated credit risks have been reduced, unless there is some change in the euro/lev exchange rate or to the currency board arrangement at some point in the future.

Credit growth seems to be declining at this point, as it has fallen in real terms from 50 to 40 percent over the last five to six months. However, this is not a dramatic decline, and risks persist. Some measures that have already been undertaken have begun to show results, and some of the natural constraints that were outlined in the staff paper—e.g., slower growth of the

deposit base—are beginning to moderate bank lending. The contingency plans that have been developed by the BNB in the event that credit does not slow are also reassuring.

One Director asked whether the authorities should tighten prudential regulations further. Such a strategy would be difficult to implement because Bulgaria's prudential regulations are generally compliant with or exceed the Basel Core Principles, so there is limited scope for further improvement.

There was a question regarding the Asian financial crisis of the late 1990s, and the similarities that might exist between Bulgaria and crisis countries. One important difference between Bulgaria and the Asian countries before the crisis is that Bulgaria's current account deficit is largely financed by FDI inflows, while that of the Asian economies was largely financed by speculative short-term capital inflows. Furthermore, the banking system in Bulgaria seems to be in good shape, and there is little evidence the sort of insider lending that contributed to the problem in Asia. Finally, another important difference is that the Asian crisis was partly brought on by an appreciation of the dollar, and it is unlikely that the appreciation of euro will have a similar impact on Bulgaria's competitiveness, as most of Bulgaria's exports already go to the EU.

Bulgaria seems to be quite competitive—exports are growing including to countries outside of the European Union. One Director suggested that the staff focused too heavily on the EU, but similar levels of export growth are also apparent for the rest of the OECD and Central and Eastern Europe. There was also a question about elasticities between FDI and imports and exports. On the export side, industries that are doing particularly well—e.g., clothing, textiles, and furniture—are sectors that have received significant foreign direct investment. Tourism, which is also a very dynamic sector, also boomed after privatization.

Finally, there was a question about the progress of the judicial reform process. The staff did not mean to imply that the authorities have completed this task; on the contrary, they have only begun to the reform process. The World Bank is also working very closely with the authorities. They have undertaken a number of important initiatives over the course of the past year, particularly several constitutional changes that were a prerequisite for EU accession. They have also hired more than a thousand new judges and initiated significant training in this area. Nevertheless, such reforms will require several years to take hold and bear fruit.

Mr. Monajemi made the following statement:

The authorities should be commended for their continued progress in implementing the Stand-By Arrangement. Macroeconomic performance has

been strong, growth robust, inflation low, and FDI inflows respectable. Official reserves have also increased to record levels. Nevertheless, the widening current account deficit has become a source of concern, which will require the authorities to exercise vigilance, despite the fact that much of the deficit has been financed by inward FDI. In this regard, it is comforting to note that competitiveness does not seem to have suffered, as evidenced by the healthy growth of exports. The authorities' commitment to a tight fiscal stance is a prudent response to recent developments that should help to narrow the current account deficit. They have also made good progress with respect to structural reforms. In light of these positive developments, we support the proposed decisions.

As indicated in Messrs. Yakusha and Yotzov's helpful statement, sound fiscal policy has underpinned the Fund-supported program. Accordingly, fiscal policy in 2003 remained tight, while revenues performed better than expected as a result of strong tax and non-tax revenues and strengthened tax collection. Nevertheless, the authorities should reconsider the envisaged increase in the wage bill and proceed with the restructuring of the railway and energy sectors in order to generate additional savings, which will further demonstrate their commitment to a prudent policy framework.

The implementation of the Financial Management Information System, which is aimed at enhancing control over spending commitments and the expansion of the Treasury Single Account, should be accelerated in order to increase its coverage to the entire general government. Improvements in tax administration, hospital sector reforms, and the full funding of municipal mandates aimed at aligning government expenditures and promoting better fiscal management are commendable. The fully operational National Revenue Agency should also help in developing a medium-term fiscal strategy. The continued expansion of bank lending to the private sector should be monitored closely, and measures mentioned in Messrs. Yakusha and Yotzov's statement that are aimed at addressing this rapid expansion are appropriate.

Efforts to further strengthen the banking system and recent changes in banking legislation for better monitoring, ownership, and a more systematic method of addressing risks from insider lending are welcome developments. While, further enhancements in banking sector surveillance and supervision are necessary, there has been commendable progress in reforming the judicial system. More importantly, the sale of the BTC and other efforts to improve the business climate should be considered high priorities. Finally, the staff's suggestion to allow the railways to operate on a commercial basis deserves further consideration.

Ultimately, the authorities should be commended for their improvements in data quality and timeliness, and progress toward the

implementation of the outstanding safeguards assessment recommendations. Bulgaria's subscription to the SDDS is also welcomed.

Mr. Sipko made the following statement:

Assisted by its currency board and Stand-By Arrangements, Bulgaria continues to turn in a good macroeconomic performance, with stable growth of about 4.5 percent in spite of the global slowdown. The authorities are successfully implementing the program agenda, albeit with some major delays due to technical difficulties. This strong track record, and the authorities' habit of keeping their promises, give assurance that they will take any measures needed to counter potential vulnerabilities, creating a favorable environment to follow the present Stand-By Arrangement. Bulgaria has made significant progress with its accession agenda, but must still do much more before it can catch up with the advanced transition countries.

Like other countries of Central and Eastern Europe, Bulgaria's current account deficit is relatively high. But the other advanced transition countries also have very high fiscal deficits, and until now Bulgaria does not. The current account might become a problem if the capital inflows that finance almost 80 percent of Bulgaria's deficit should dry up. The external current account deficit would be more manageable if the authorities could create better conditions for foreign investors, *inter alia* by reducing barriers to entry, improving the regulatory regime, eliminating government interference in private sector development, improving governance, and reforming the labor code.

Though the fiscal performance is almost in line with the program, the authorities will need to use the fiscal stance as a tool for controlling the potential effects of widening external imbalances. It is therefore regrettable that the fiscal stance for 2004 tends toward the expansionary. Here we would like to note that the significant wage increases and the expansion of the National Health Insurance Fund (NHIF) in financing hospital care will undermine macroeconomic stability.

In addition, the authorities' plan to increase the role of state enterprises in carrying out public sector activities is not encouraging. The scheme to capitalize a state highway enterprise with a Fiscal Reserve Account (FRA) of about 1.25 percent of GDP will damage the macroeconomic position. In this connection we join the staff in urging the authorities to make sure that all such activities remain transparent within the budget framework, and to avoid a proliferation of state entities. Unfortunately, several extra-budgetary funds are still operating in Bulgaria. Could the staff comment on the authorities' plans with respect to these funds?

Their medium term fiscal strategy commits the authorities to continue their fiscal reforms. Improving tax administration, and the transparency and efficiency of public spending, are badly needed. Fiscal adjustment must become more flexible. In this connection, we encourage the authorities to establish a National Reserve Agency (NRA), and we urge them to approve and put into effect a draft Bulstat law in 2004.

Even though it is very strong, the growth of private sector credit is still manageable. Compared with some other transition countries, Bulgaria's credit-to-GDP ratio is still low, as is clear from Box 1 of the staff paper. We see no great risk connected with this rapid growth as long as Bulgaria's banking supervision remains effective. Mr. Yakusha and Mr. Yotzov assure us in their written statement that the authorities stand ready to take additional measures if credit growth does not continue to decline.

We support the proposed decision.

Mr. Maciá made the following statement:

Favorable economic growth continued during 2003, fueled by private consumption and investment. Bank credit has been strong, particularly regarding consumer loans and mortgages. Inflation has remained subdued and unemployment continues its downward trend as observed in the last four years. On the other hand, consumer and capital goods imports and high oil prices affected the current account deficit, which was mostly financed by strong FDI. Prudent fiscal management brought about a large budget surplus as revenues soared from customs collection and non-tax revenues. This outcome, with lower interest payments, and a clamp on discretionary outlays, helped to finance spending overruns in health care, coped with the mandated municipal outlays, and supported wage and pension adjustments.

Progress was made in various fronts concerning structural issues. We are pleased to note the strengthening in tax administration and public expenditure controls, the reforming of the judiciary, and the streamlining of licensing and regulatory regimes to improve the business environment. We welcome the DSK bank privatization, we expect prompt resolve in the telecommunications privatization’s final steps, and we urge the authorities to press ahead in the restructuring of the energy sector and railways.

Macroeconomic gains experienced up to this moment are expected to continue. In this vein, economic growth should improve as the global economic stance strengthens, exports should expand further, and inflation is to remain subdued. In addition, it is thought that FDI will remain at levels seen in 2003, and that stronger private sector participation should enhance employment growth. We agree with staff that risks remain and that further

efforts should include the attainment of a solid fiscal stance and the strengthening of the financial sector.

A strong revenue performance is expected again in 2004. The authorities are committed to save any revenue overperformance and pursue a balanced budget. We praise the fiscal strategy that targets tax reduction on corporations, reviews exemptions in income tax, and increases some excise tax items. We agree with the decision to postpone capitalization of the state highway enterprise, and we urge caution in the creation of additional state enterprises. We welcome the strengthening of the revenue agency (NRA) and the expansion of program budgeting to other ministries. We urge prompt steps to set up the single treasury account and the full implementation of the expenditure controls system (FMIS) as both actions remain from the 2003 benchmark agenda.

We are encouraged by the authorities' readiness to keep on top of measures to maintain a sound banking system. We are pleased with the forthcoming reporting measures on loan classification. We agree with the deferment of the decision to reduce banks' reserve requirements and the measure to initiate the return to BNB government funds previously deposited in commercial banks in mid-2003 to curb the possibility of excessive credit growth. On privatizations, we expect prompt resolve in the sale of the electricity distribution companies. We praise the authorities' decision on tariff adjustment on railways in order to improve cost recovery in their operations, the steps taken to limit the wage bill in SOE's, and the initiatives to pursue changes in the labor code, which require skillful negotiation strategies. We ask the authorities to persevere in this issue.

With these comments, this chair supports the completion of the fourth review, the requests for waivers, and the extension of the program. We wish the authorities success in the challenges that remain ahead.

Ms. Rizzotti made the following statement:

We thank the staff for their interesting paper and Mr. Yakusha and Mr. Yotzov for their insightful statement. Since we broadly agree with the thrust of the staff appraisal we will make just a few comments for emphasis.

We commend the Bulgarian authorities for their broadly satisfactory performance under the program. Bulgaria's macroeconomic performance has been good and progress has been made on the structural agenda. However, a strong effort is required in the preparation for EU accession. Unemployment, although decreasing, is still relatively high. The percentage of the population living below the poverty line and the increase in inequalities (measured by the Gini coefficient) are the highest among the countries expected to join the EU. These facts can help in explaining the highly critical attitude toward the

transition process by the population at large and the very low popularity of the government. The staff's views are welcome on the risks this could pose for reform sustainability and fiscal consolidation in the coming years and the best strategy to address this issue. In particular, we wonder whether due attention has been paid to the elaboration of an effective social safety net in order to smooth the costs of transition for particularly vulnerable groups.

In the macroeconomic area, the high and larger than expected current account deficit is a source of concern, notwithstanding a number of reassuring features highlighted by the staff, who expects the deficit to decline in the medium term. In particular we welcome the authorities' commitment to take additional measures should the external conditions not improve. However, since the magnitude of the current account deficit is likely to be a relevant issue in the medium run, we would appreciate a more in-depth analysis of current account sustainability in the next Article IV consultation, of the type conducted for the Baltic countries, which was presented in Estonia's selected issues paper last October. This would also provide additional information to evaluate the need for a successor precautionary arrangement.

Regarding the structural agenda, we are concerned by some delays in the implementation of structural reforms in the fiscal area, given the crucial role of sound fiscal policies under the CBA. We also urge the authorities to complete the privatization process. At the same time, we welcome a number of the measures undertaken, in particular the progress in improving the business environment and the reform of the judiciary.

With these comments we wish the authorities every success.

Mr. Jang made the following statement:

It is encouraging that macroeconomic performance in Bulgaria has improved under the Stand-By Arrangement. We look forward to the ex post assessment of Bulgaria's experience under Fund programs, although it appears that performance under the program, which is now coming to an end, has been generally sound. In particular, one encouraging aspect is that there appears to be a good relationship between the authorities and the staff, and the authorities have been responsive to the staff's advice.

As the staff rightly note, the economy faces some significant challenges and risks, including rapid private sector credit growth and an enlarged external current account deficit. In addition, while the unemployment rate is on a declining trend, it remains quite high. Against this background, the staff is right to recommend a more concerted effort regarding fiscal policy and the implementation of structural reforms. However, perhaps the biggest operational challenge facing the government is to get the necessary public support required to implement difficult reforms while its own popularity is

remains extremely low. In such circumstances, we have considerable sympathy for the authorities' view that the staff's recommendations are not feasible politically. The authorities have pragmatically addressed some of these tensions by keeping a degree of flexibility with the aim of adjusting policy should circumstances warrant. The downside with this approach is that it is always better to set policy in a pre-emptive manner and to avoid a deterioration in conditions. Furthermore, the same political constraints may exist when the decision is taken that it is necessary to tighten or adjust policy. Nevertheless, the authorities face political constraints, and the Fund needs to take this into account.

An aspect is of interest, which will hopefully be covered in the ex post assessment, is the role that the Fund has played in helping to facilitate the implementation of reforms. For example, did the existence of a program, and its associated measures strengthen the hand of the authorities in implementing difficult and contentious measures? In short, was the Fund a political asset or a political liability?

Turning to a few specific issues, it is noteworthy that in the first three quarters of 2003, the fiscal surplus was significantly better than programmed, largely due to revenue overperformance. Although it is encouraging that the authorities have indicated that they will save a 'significant' share of the fiscal overperformance, we note that they were noncommittal with respect to continuing to accumulate a fiscal surplus should the revenue overperformance continue. While we support the authorities' intention to undertake additional unbudgeted expenditures (central government-mandated expenditures and hospital arrears), like other Directors, we feel the decision to use the revenue overperformance to increase wages and pensions is not particularly prudent. Nevertheless, we recognize the difficulty of resisting pressures for wage and pension increases when the fiscal accounts appear to be improving better than expected and better than programmed. The challenge is to be able to convince the public that a relatively 'tight' fiscal stance is required given economic developments.

On the 2004 budget, we welcome the authorities' commitment to maintain some flexibility by limiting discretionary spending and incorporating contingencies so that they could achieve a balanced budget should external conditions deteriorate. However, as noted previously, given the deterioration in the external position and risks to the outlook, it would be more desirable for the authorities to manage fiscal policy in a more pre-emptive fashion. And, as also noted, while a revision to the budget deficit of 0.75 per cent of GDP is now not considered politically feasible, will a tightening of policy be feasible if there is a further deterioration in the external position? We feel that we may need to better inform the public of the challenges and objectives of macroeconomic policy and to attempt to prepare the ground for a tightening of policies.

Regarding the capitalization of state enterprises, we join other Directors in encouraging the authorities not to set up new enterprises that are capitalized by the Fiscal Reserve Account (FRA), as this might undermine fiscal transparency. While it is somewhat disappointing to learn that some structural reforms in the fiscal area have been delayed owing to technical difficulties and legislative issues, we are reassured by the authorities' commitment to address these problems.

Second, as staff and the authorities agree, rapid credit growth is a source of concern. It is particularly encouraging to see that the government is fully cognizant of the risks of overly rapid credit growth, and that they are taking this into account in the context of debt and asset management. The BNB is taking on more intensive surveillance of aggressive banks, and we encourage the authorities to continue to develop additional measures should credit growth not return to more comfortable limits.

Third, while we are pleased to know that the authorities are cognizant of the importance of structural reforms and BTC will be privatized soon, progress in privatization has been slow. In a situation where FDI inflows have covered most of the current account deficit, it is essential to accelerate structural reforms without delay so as to ensure that there is an investor-friendly environment and FDI inflows are maintained. Such initiatives would also facilitate progress toward EU accession. In this regard, we wonder what factors have contributed to the increases in FDI inflows in 2003, despite the slow pace of privatization. Is Bulgaria a more attractive investment destination than other EU candidate countries?

Finally, as we mentioned during the previous review, a great deal of effort needs to be undertaken in the labor market in order to promote greater flexibility and, hence, help alleviate high unemployment and increase the external competitiveness of the economy. In particular, a further case for labor market reform might be made in light of the rise in the euro.

With these remarks, we support the proposed decision and wish the authorities continued success in the future.

Ms. Williams made the following statement:

We are grateful for the staff paper and for the update provided by Mr. Yakusha and Mr. Yotzov in their statement. Bulgaria has made good progress in recent years, and we commend the Bulgarian authorities for their continued progress and commitment to reform, despite the difficult political situation. We would be grateful for the staff's comments regarding whether the fiscal reform program is sufficient to maintain strong progress, and whether the reforms are sufficiently embedded, such that a change in government would be unlikely to derail the process.

We would also like to highlight three points for emphasis. First, we are concerned about the proposed increase in the average wage by 11 percent. Is this measure linked to a reform program, or is it designed to catch up with inflation? If not, we would urge the authorities to reassess this proposal, or to phase it in gradually so as to avoid fueling inflation. Second, we welcome the news of the sale of the BTC, and hope that the positive message that this sends to investors will not be undermined by the authorities' move to create public enterprises that are capitalized by the Fiscal Reserve Account. Third, we welcome the fact that efforts to restructure the state-owned railway and energy concerns are bearing fruit, but urge the authorities to intensify their efforts in this area.

Looking ahead, structural reforms and fiscal discipline will continue to be important focuses of the program as Bulgaria moves toward EU accession. Given Bulgaria's strong macroeconomic performance in recent years, we hope that the staff will make a comprehensive assessment of the authorities' needs and respond constructively to any requests for a new precautionary Stand-By Arrangement. Furthermore, any new program should continue to incorporate demanding criteria and remain conducive to the authorities' EU accession goals.

Finally, we look forward to receiving the ex post assessment. Having reviewed two of these documents recently, we hope that Directors' previous comments on the initiative have been carefully considered. Specifically, we trust that the ex post assessment will reflect a balanced picture of both the authorities' and Fund's performance, and that the staff will attempt to view past performance under Fund-supported programs from a different vantage, while seeking varied views.

With these remarks, we support the completion of the fourth review under the Stand-By Arrangement, and Bulgaria's requests for waivers and an extension of the arrangement.

Mr. Watanabe made the following statement:

I thank the staff for a concise and insightful paper and Mr. Yakusha for his statement.

The country's macroeconomic performance is relatively solid despite the prolonged slowdown in the EU. Robust growth and a decline in unemployment reflect the authorities' solid macroeconomic policies and broad structural reforms implemented since 1997. The authorities should be commended for these achievements. At the same time, they should be well aware of a new set of challenges that must be addressed. In the short term, strengthened domestic demand, fueled by rapid credit growth, has put

increased pressures on Bulgaria's external positions, requiring continued prudent fiscal policies and strengthening of banking supervision. Over the medium term, while I recognize that Bulgaria is ahead of its regional neighbors in structural reform, the authorities need to make further progress in order to attract solid FDI inflows and ensure the viability of their EU accession strategy.

Since I generally agree with the thrust of staff appraisal, I will limit my comments to just four issues.

The fiscal stance for 2004 worries me somewhat even though it is only mildly expansionary, given that external pressures are expected to continue for the time being. While the authorities' plans to fully fund municipal mandates, and to clear overruns on medicine reimbursements and some hospital arrears, are understandable, I strongly question the appropriateness of increases in pensions and wages. These increases are inappropriate, not only in light of increased pressures on external positions as the staff notes, but also in the context of the currency board arrangement (CBA), which requires a flexible fiscal policy. Furthermore, these increases could be perceived as a departure from the authorities' vision of a small and efficient public sector, which may adversely affect investor confidence.

Looking ahead, the authorities should attach greater importance to fiscal structural reform. In particular, strengthening tax administration and enhancing the efficiency of public spending should both be prioritized. I urge them to take significant strides during 2004 to ensure that the National Revenue Agency (NRA) is operational by 2005 as planned. I agree that some of the fiscal reserve account (FRA) on capital projects might not be ideal given the growing current account deficit, and concur with the staff's recommendation to use FRA resources to lower external debt via early debt retirement or buy backs. In this regard, I welcome the fact that the authorities will analyze carefully this issue in collaboration with the IFIs and put this option on hold until the risks surrounding the macroeconomic environment are under control.

Regarding the financial sector, the authorities must be vigilant to rapid credit growth, and its associated macroeconomic risk. To this end they need to continue to enhance banking supervision. I agree that they have taken the right approach to addressing the rapid growth in private sector credit, including tightening the definition of bad loans and expanding coverage of the credit register. That said, additional steps, including an increase in liquidity requirements on a bank-by-bank basis, may be needed should credit continue to grow rapidly.

Good progress has been made in structural reforms. In particular, I welcome the authorities' efforts to enhance the business climate and the

legal system, both of which are essential for the country's entry into the EU in 2007. I hope to see solid developments in these areas. Moreover, I encourage the authorities to take further steps in restructuring loss-making public enterprises, including railways and the energy sector.

Finally, regarding the ex post assessment, Appendix I of the staff paper is not clear on when this discussion will take place. I would appreciate the staff's clarification on this issue. In this regard, I would reiterate this chair's view that Board discussions on ex post assessments should take place separately from those on requests for successor arrangements in order to ensure a candid and objective assessment by the staff and to facilitate early inputs from the Board. From this standpoint, Like Ms. Jacklin and Mr. Epstein, I would prefer an ex post assessment of Bulgaria in the context of the discussion on the Article IV consultation, and a separate meeting on a successor arrangement at a later date. Given the absence of urgent balance of payments needs, it would be beneficial not only for the Fund, but also for Bulgaria, to undertake an objective assessment of past programs and draw lessons from it before entering into a new form of engagement.

With these remarks, I support the proposed decision and wish the authorities every success in their endeavors.

Mr. Yakusha noted that a few of his constituents might be affected by the policies and procedures surrounding the conduct of ex post assessments given their prolonged program engagement with the Fund. Delays in negotiation and implementation of Fund-supported programs owing to ex post assessments were not generally advisable and could have unfortunate consequences for affected countries. Furthermore, the Board should remain conscious that if such assessments were to become standard practice, there would be a proliferation of such undertakings, which could involve significant additional costs to the Fund.

Mr. Basdevant made the following statement:

We would like to thank the staff for their interesting papers, and Messrs. Yakusha and Yotzov for their informative statement. At the outset, we would like to express our support for the completion of this review, particularly given the authorities' strong track record and their efforts to stabilize the economy. Since we broadly agree with staff's appraisal, we will limit our intervention to a few points.

Strong growth performance has led to a reduction in unemployment, and inflation remains low. Furthermore, debt levels remain sustainable, which is likely the result of prudent fiscal policy. The sustainability of the currency board arrangement relies heavily on the soundness of fiscal policy, and in this light, we are concerned with the possible fiscal slippages that might result

from recent and forthcoming political developments. We thus encourage the authorities to resist pressure to take an expansionary fiscal stance.

While the current account deficit could remain financed largely by FDI inflows, it is also important to continue improving the business climate. We particularly welcome the information provided by the staff regarding the progress toward the privatization of the BTC, and urge the authorities to proceed expeditiously with the sale of Bulgartabac. The authorities should continue to improve the business climate by addressing corruption and improving administrative capacity, which will improve investor confidence and reinforce the political consensus in support of reforms. Furthermore, credit growth should be monitored closely, and we welcome the steps taken by the authorities to improve surveillance.

We would like to note that Bulgaria remains a creditor in the context of the HIPC Initiative, and that it has only partially implemented the necessary debt cancellations. Finally, we encourage the authorities to move forward with a successor precautionary arrangement that will help to reassure financial markets.

In light of the authorities' strong performance, we support the proposed decisions, and wish the authorities success in the future.

Mr. Prasad made the following statement:

Bulgaria's performance under the Stand-By Arrangement continues to be strong. Led by strong industrial production and a sharp increase in private consumption and investment, macroeconomic performance remains favorable. We commend the authorities for their prudent macroeconomic management and progress toward establishing a market-friendly business environment.

With the exception of the performance criterion on tax arrears collection and indicative targets on the arrears of the electric company, all performance criteria were met. Most of the structural benchmarks were also met. We thank the staff for an excellent paper and generally agree with their recommendations. We join other Directors in supporting the completion of the fourth review under the Stand-By Arrangement, and the authorities' requests for waivers. However, we would like to make a few comments for emphasis.

Though the political situation appears to be somewhat tenuous, we are encouraged by the fact that policies remain broadly on track. The stabilization effort has focused on attracting FDI and reinvigorating the structural reform agenda. The staff's focus on policies aimed at containing risks related to the current account deficit and rapid credit growth is prudent. The authorities must maintain a tight budgetary stance, contain government subsidies, and improve the quality of spending. We encourage them to address technical

constraints in order to accelerate the implementation of the Financial Management Information System, the extension of program budgeting to more government ministries, as well as the expansion of the coverage of the Treasury Single Account. Further progress toward fiscal decentralization would also be advisable. A tighter fiscal stance, including sustained fiscal surpluses over the medium term, would help to improve the macroeconomic situation, and set the stage for stronger economic growth and stability in the future.

In light of their considerable efforts under the current Stand-By Arrangement, we wish the authorities success in the future, and support the proposed decisions.

Mr. Faircloth made the following statement:

Like other chairs, we are satisfied with Bulgaria's performance under the Stand-By Arrangement. The relatively strong macroeconomic performance over the past year is a testament to the authorities' sustained efforts to transform and modernize their economy. While we commend the authorities on this achievement, we agree with the staff that the economy faces new economic challenges which demand a renewed commitment to: fiscal discipline, strong banking supervision, and structural reforms that further enhance the business climate.

Overall, we agree with the staff's assessment of risks and their policy recommendations. I will make a few points for emphasis.

First, we agree that expansionary fiscal stance in 2004 is disappointing given the risks that a sustained widening of external pressures poses to the currency board arrangement and economic stability more generally. The authorities will need to monitor developments closely and stand ready to tighten should the external environment fail to improve. Indeed, our preference, like other chairs, would have been to target a budget balance or small surplus. Enhancing fiscal flexibility should remain a priority and, to that end, fiscal reform efforts need to be reinvigorated, particularly in the areas of tax administration and public expenditure management.

We also encourage the authorities to hold true to their vision of a small and efficient public sector. Increases in public sector wages and employment of the scale approved recently should be avoided going forward. The authorities should also refrain from broadening the scope and reliance on state-owned enterprises, which risks introducing contingent liabilities and would seriously complicate fiscal transparency. Rather, our strong preference is to dedicate FRA resources to reduce the debt burden and accelerate structural reforms to promote private-sector led growth.

Second, on the structural reform agenda, we place a heavy emphasis on: judicial reform, strengthening property rights, and reducing bureaucratic "red tape" in establishing new business. We associate ourselves with the points made by Messrs. Le Fort and Vogel on redoubling efforts to strengthen governance across the board.

The authorities have generally done well in implementing the privatization agenda. We hope that the privatization Bulgartabac will proceed swiftly. Early decisions need to be taken on how to reform the railway and electricity sectors to minimize their drain on the budget. Like other chairs, we applaud the authorities' decision to refrain from pursuing discretionary investment incentives.

Third, on financial sector policies, the staff paper does a good job in stressing the importance of properly managing the rapid growth in private sector credit. To that end, we are encouraged by the policies outlined in paragraphs 18 through 20, particularly the decision to tighten the definition of "loss" loans and postponing plans to reduce reserve requirements.

Lastly, rising political pressure against fiscal consolidation remains an important risk that the authorities will need to manage proactively. We encourage them to mount a widespread public campaign that clearly explains the benefits of sustained policy prudence and ambitious structural reform. We welcome the decision to publish the staff paper as a part of this effort, particularly in light of the staff paper's reference to a "country specific" scenario in paragraph 10, which examines a pragmatic deterioration in the economic environment. This scenario gives a reasonable sense of the potential costs associated with a slackening of reform momentum, although the staff paper could have delivered this message more clearly by elaborating on this scenario within the text itself.

More generally, we believe that staff papers could become a much more powerful "consensus building" tool by incorporating a range of economic scenarios, including a medium-term "no policy reform" scenario, to highlight the trade-offs between the changing policy today and future progress in living standards. We encourage the staff to expand their analysis along these lines going forward.

To sum up, we support completion of the fourth review and the proposed decisions, and wish the authorities success in their policy endeavors.

Mr. Al-Nassar made the following statement:

I join other speakers in commending the Bulgarian authorities for their strong economic performance. Growth remained robust with low inflation and falling unemployment. These welcome results could not have been achieved

without the authorities' commitment to the agreed adjustments and reforms. Nevertheless, the widening current account deficit remains a source of vulnerability to the economy, notwithstanding the high levels of FDI and reserves. Here, the authorities' continued commitment to their policy framework, as further confirmed in the helpful statement of Mr. Yakusha and Mr. Yotzov, is key to enhancing the economy's resilience and to sustain high growth rates over the medium term. I broadly agree with the staff's appraisal and will add a few remarks for emphasis.

The fiscal overperformance last year is commendable. Indeed, allocating the higher than expected revenue collection to deficit reduction underscores the authorities' commitment to a cautious fiscal policy. Turning to this year's budget, I agree with the staff that a tight fiscal stance should be maintained in view of continued external pressures. In this regard, the authorities' contingency measures and their strong track record of responding flexibly to shocks are reassuring. Further structural reform is critical for successful implementation of the government's medium-term fiscal strategy. In this connection, improved efficiency of government spending and additional strengthening of tax administration cannot be overemphasized.

Turning to monetary policy, the rapid expansion in credit to the private sector is a concern. Therefore, I welcome the steps taken recently by the Bulgarian National Bank (BNB) to contain lending and further strengthen the health of the banking system. The authorities' commitment to take additional measures, if needed, is also reassuring. I am encouraged by the ongoing efforts to enhance public debt management and improve the debt profile.

On structural reforms, I welcome the completion of the sale of the last major state-owned financial institution. Additional efforts to privatize the remaining public enterprises, however, are still needed. Enhancing the business climate is also essential to encourage domestic and foreign investment. To this end, the progress made in reforming the judiciary and streamlining investment procedures and regulations are welcome. Using the Fiscal Reserve Account (FRA) resources to capitalize a state highway enterprise and to create and several small enterprises, however, will undermine achieving the objective of reducing the government involvement in economic activities.

With these remarks, I support the proposed decision and wish the authorities success.

Mr. Martinez made the following statement:

As others we would like to thank the staff for a well-written staff paper, and Mr. Yakusha and Mr. Yotzov for their useful statement.

The Bulgarian economy has continued to perform remarkably well since the last review of the Stand-By Arrangement. Sound macroeconomic policies and structural reforms have pushed growth and reduced unemployment, but more efforts are needed toward reaching higher living standards.

In 2003 there have been significant positive developments. GDP has risen substantially due to the growth in fixed investment and the strong increase in private consumption, fueled by the improving labor market and low inflation. The outlook also appears to be promising, but is subject to downside risks stemming from credit growth and negative external shocks. On the political side, the results of recent elections indicated a decline in popularity of the coalition government that has increased the pressure to relax fiscal policy and might hold up necessary structural reforms. In this regard, maintaining the authorities' commitment to the reform agenda and the prudent conduct of fiscal policy are essential. We join the staff in commending the authorities for maintaining a tight fiscal stance and for making progress in difficult reforms.

Based on the generally satisfactory program implementation of the Stand-By Arrangement, we support the completion of the fourth review and the proposed decisions. We broadly agree with the thrust of the staff appraisal and recommendations and therefore we would concentrate our comments on some relevant aspects for emphasis.

On fiscal policy, the authorities should be commended for going beyond the fiscal targets in 2003, with a projected small surplus in the budget as the authorities dedicate most of the revenue overperformance to deficit reduction. For 2004, the authorities are maintaining their commitment to fiscal discipline by building sufficient flexibility within the budget to achieve again a balanced budget, should the external position weaken further. We believe that the measures taken by the authorities provide a good basis for ensuring that the budget does not add to external pressures. Equally appropriate is the linking of potential revenue overperformance to developments on the external position.

On fiscal management, we welcome the authorities' efforts and encourage them to go forward with their agenda to have the National Revenue Agency fully operational by 2005 and to enforce budget constrains on municipalities. Also, the use of state enterprises and joint ventures with commercial enterprises to address infrastructure expenditures should be made in a transparent manner that appropriately takes into account contingent liabilities.

Developments in the financial sector are especially encouraging. The authorities have taken prompt and correct actions to limit the rapid expansion

of credit growth and to overcome the risks posed by its current pace of increase, namely the risk of future deterioration of bank asset quality and the effect over the ongoing import boom. We share staff's positive assessment of the authorities' policies in this area. Their strategy seems appropriate and we encourage the authorities to implement it.

On structural reforms, we note the progress being made by the authority's agenda since the last review. In July, we insisted on the need for the authorities to send positive signals to investors and strengthen the credibility of a strategy of enhancing an investment-led growth and attracting FDI. In this respect, we welcome the shift of focus on completing the privatization agenda and improving the business climate, which is a step in the right direction.

With these comments, we wish the Bulgarian authorities all success in their endeavors.

The staff representative from the European Department (Mr. Schiff) made the following additional remarks in response to questions and comments from Directors:

A number of speakers have asked about the sustainability of political reforms and the government's lack of popularity. This is a very important issue, and the relative weakness of the government has certainly complicated efforts to maintain fiscal discipline and push forward the structural reform agenda. However, it is important to make a distinction between the popularity of the government and the public's general view regarding the reform process. All of the major political groups and much of civil society have endorsed the main elements of the reform program—i.e., the currency board arrangement, the cautious fiscal policy stance, and the structural reforms required for EU accession. There are certainly some differences of opinion across such groups, but the staff is confident that the overall direction of policies would not change if the government were to change.

Regarding the role of poverty and the social safety net, it is important to note that these issues, as well as the unemployment situation, have improved quite dramatically since the crisis in 1997. Nevertheless, we would like to see the authorities make further progress, but they are certainly moving in the right direction. The social safety net in Bulgaria is relatively well developed, as is described by the World Bank's poverty assessment and public expenditure reviews. Expenditure as a share of GDP on the safety net has increased, but more can be done to increase its effectiveness. For example, eight of every ten Bulgarians receive some form of social assistance, which suggests that significant streamlining should be undertaken, as well as better targeting of the poor. However, it is unclear whether sufficient political will exists to undertake such reforms.

There was a question about wages increasing by 11 percent. The staff would have preferred a more modest increase, as public sector workers have received wage increases equal to or above inflation during the last several years. However, the overall public sector wage bill remains about 4 percent of GDP, which is rather low by international standards. Nevertheless, given the associated macroeconomic risks, a more moderate increase might have been appropriate.

Regarding the government's plans regarding the extra-budgetary funds mentioned in the staff paper, the staff hopes that some of these funds will not be created. The fund related to the forestry enterprise was created as a consequence of a World Bank project loan, but the staff of the Bank is currently debating whether such a strategy is appropriate. Regarding the road construction enterprise, the government is receiving advice from the World Bank on how to proceed. Historically, the authorities have been very successful at eliminating extra-budgetary funds and similar mechanisms, and the staff hopes that this will continue to be the case.

The staff representative from the Policy Development and Review Department (Mr. Muniz) stated that the current guidelines for ex post assessments allowed for the associated Board discussion to coincide with the request for a new program. However, such timing might not be consistent with the objectives of such assessments, which were designed to provide the staff with a fresh perspective regarding the program, and to incorporate such lessons into future programs. The Board had recommended on several occasions that ex post assessments should coincide with Article IV consultations or final reviews of Fund-supported programs. The ex post assessment for Bulgaria was likely to be discussed before any request for a follow-up precautionary Stand-By Arrangement were to be considered by the Board.

Mr. Yakusha made the following concluding statement:

I welcome Directors' suggestions and comments, which I will convey to the authorities.

Regarding questions about similarities between Bulgaria's situation and that of the Asian countries prior to the regional financial crisis of the late 1990s, there are many significant differences between the two. First, Bulgaria's exchange rate appears to be undervalued rather than overvalued, as was the case for the Asian economies. Second, the appreciation of the euro does not appear to have adversely affected competitiveness, particularly given the fact that 60 percent of Bulgaria's trade takes place with the rest of the European Union. Furthermore, half of the country's debt is denominated in dollars, so the appreciation of the euro has allowed the country to save on debt servicing. The rising euro has also translated into savings on fuel imports. Finally, the authorities have done a good job of sustaining a flexible fiscal policy framework. The authorities have a strong track record, since the significant financial problems that emerged in 1997, which almost resulted in

hyperinflation. Nevertheless, despite the significant improvement in the business climate, which was also a function of strong FDI inflows, there remains room for further improvement in domestic confidence.

In this light, it is important for Bulgaria to initiate a new precautionary arrangement with the Fund in order to instill confidence in international and domestic capital markets. In that context, given that ex post assessments are not yet well understood by the public or market participants, the Board should not risk sending mixed messages by calling for such assessments to precede the initiation of a follow-up precautionary arrangement. Such a strategy may penalize Bulgaria, which has been a strong performer, as well as run the risk of damaging relations with a country that has benefited tremendously from Fund involvement. Bulgaria is a country where the staff is genuinely revered by the public, particularly as a result of their efforts to help the country weather the financial crisis in 1997—they are actually greeted by public applause as a result of their helpful contribution to crisis resolution. It would be a shame if this relationship were adversely affected by inadvertently sending conflicting signals to the public.

The Acting Chair made the following summing up:

Executive Directors commended Bulgaria's continued strong macroeconomic performance and the authorities' efforts to maintain economic stability in the face of external risks. Directors also welcomed the generally good progress with structural reforms. They underscored the importance of structural reforms in attracting foreign direct investment and ensuring the viability of the government's medium-term fiscal strategy, and urged timely completion of these reforms.

Directors commended the authorities' success in utilizing fiscal policy to contain external risks. They emphasized the need to maintain a prudent fiscal policy, particularly given the currency board arrangement in Bulgaria, the high external current account deficit, and uncertainties regarding the sustainability of foreign direct investment inflows. Directors considered that the fiscal overperformance in 2003 was an appropriate response to the current account deficit, and some felt that, given the credit and import boom, the authorities could have saved more of the revenue overperformance in the fourth quarter.

For 2004, Directors urged the authorities to exhibit restraint and to adjust their policies accordingly if external conditions fail to improve. Given the built-in flexibility in budget implementation and Bulgaria's strong track record, most Directors agreed that the fiscal deficit target of 0.7 percent of GDP for 2004 appears to be adequate, while some Directors noted that the authorities could have targeted a lower deficit, or even a small surplus. Directors emphasized that it will be critical to monitor external developments

closely and to take prompt action, if needed. Directors welcomed the full funding of local government mandates and the implementation of health care reforms, which limit the scope for payments arrears and spending overruns in 2004. They also attached priority to collecting tax arrears and to improving payment discipline in general. It was also suggested that the authorities adopt a transparent, rules-based, budgetary framework.

Directors expressed concern regarding the proposed financing of state enterprises to carry out public sector activities using resources from the Fiscal Reserve Account (FRA), stressing that this could undermine expenditure control, jeopardize important gains made so far in fiscal transparency, and create contingent liabilities for the government. In this context, they endorsed the policy of postponing potential transfers to a state enterprise for road construction at least until the second half of 2004, and of making such transfers contingent upon macroeconomic developments. Directors agreed that FRA resources should be used to lower external debt via buy backs, and also supported the authorities' intention to increase the share of domestic debt in total public debt.

Directors endorsed the authorities' approach to addressing the rapid growth of private sector credit, and some suggested that more stringent measures are needed. While Directors considered the increase in such credit from low levels to be a welcome development, they agreed that it requires continued vigilance to ensure that the banking system does not become vulnerable to risks. In this connection, Directors welcomed the measures taken to intensify the central bank's surveillance of aggressive banks, tighten the definition of bad loans, and expand the coverage of the loan register. They supported the government's decision to return deposits from commercial banks to the central bank, since this will help moderate the pace of credit growth, and recommended that further action be taken should rapid credit growth continue.

Directors welcomed the sharp decline in unemployment in 2003. They noted that active labor market policies have contributed to this decline, and agreed that increased labor market flexibility is required to ensure continued progress in this area. Directors welcomed the authorities' policy of wage moderation in state enterprises. However, they expressed concern about the planned increase in public employment and the wage bill, underscoring that such plans could delay the attainment of a small and efficient public sector.

Directors commended the privatization of the DSK Bank, the last major state-owned financial institution. They welcomed the authorities' decision to invite the winning bidder for the sale of the telecommunications company to sign the sales contract by February 20, 2004, and the authorities' new plan for privatizing individual units of the tobacco company. Directors also commended the steps taken to restructure the energy and railway sectors,

but noted that a clearer political decision is required on the scope of subsidized social activities to be carried out by the railway sector. Directors welcomed the regulatory reforms undertaken in the past year, which have eased administrative burdens on business activities. Similarly, they commended the authorities for the steps taken to modernize the judicial system, and urged that these efforts and other actions to improve governance continue. Calling for greater priority to fiscal structural reforms, Directors urged that the National Revenue Agency be made fully operational by January 2005, that faster progress be made in implementing the Financial Management Information System and expanding the coverage of the Treasury Single Account, and that a clear rule be defined for indexing public pensions.

Directors welcomed Bulgaria's subscription to the Special Data Dissemination Standard, and commended the considerable progress made in implementing the remaining safeguards assessment recommendations.

A number of Directors expressed support for a follow-up precautionary Stand-By Arrangement, and in that regard, several also looked forward to the ex post assessment of Bulgaria's Fund-supported programs.

The Executive Board took the following decision:

1. Bulgaria has consulted with the Fund in accordance with paragraph 3(d) of the Stand-By Arrangement for Bulgaria (EBS/02/24, Sup. 2, 3/5/02) and the third paragraph of the letter of the Minister of Finance and the Governor of the Bulgarian National Bank dated June 18, 2003 to review program implementation, and has requested a waiver for nonobservance in respect of one quantitative performance criterion, waivers of applicability in respect of two quantitative performance criteria, as well as an extension of the Stand-By Arrangement until March 15, 2004.

2. The letter of the Minister of Finance and the Governor of the Bulgarian National Bank dated January 15, 2004, together with its attached Supplementary Memorandum of Economic Policies, shall be attached to the Stand-By Arrangement for Bulgaria, and the letters of the Minister of Finance and the Governor of the Bulgarian National Bank dated February 12, 2002, July 5, 2002, January 22, 2003 and June 18, 2003, together with their attachments, shall be read as supplemented and modified by the letter dated January 15, 2004.

3. Accordingly, paragraph 1 of the Stand-By Arrangement for Bulgaria shall be amended by deleting "For a period of two years from February 27, 2002 to February 26, 2004" and replacing it with "For a period of two years and two weeks from February 27, 2002 to March 15, 2004".

4. The Fund decides that the fourth review contemplated in paragraph 3(d) of the Stand-By Arrangement for Bulgaria is completed and that Bulgaria may make purchases up to a cumulative amount of SDR 214 million until February 15, 2004 notwithstanding the non-observance as of December 31, 2003 of the quantitative performance criterion on the ceiling on tax and social security arrears specified in paragraph 3(a)(ix) of the Stand-By Arrangement for Bulgaria on the condition that the information provided to the Fund by Bulgaria on its performance under this criterion is accurate and notwithstanding the unavailability of information necessary to assess the observance of the December 31, 2003 performance criteria specified in paragraphs 3(a)(i) and (iii) of the Stand-By Arrangement for Bulgaria on the conditions that Bulgaria has accurately represented to the Fund that such information is unavailable, and that the information provided to the Fund by Bulgaria on performance under these criteria for September 30, 2003, and the information provided to the Fund by Bulgaria on the implementation of the measures specified as prior actions in Table 3 to the Supplementary Memorandum of Economic Policies, is accurate. (EBS/04/6, Supplement 1, 2/2/04)

Decision No. 13179-(04/10), adopted
February 4, 2004

APPROVAL: March 10, 2004

SHAILENDRA J. ANJARIA
Secretary