

**FOR
AGENDA**

SM/09/45
Supplement 1

February 17, 2009

To: Members of the Executive Board

From: The Acting Secretary

Subject: **Bulgaria—Staff Report for the 2008 Article IV Consultation—
Informational Annex**

The attached informational annex is being issued as a supplement to the staff report for the 2008 Article IV consultation with Bulgaria (SM/09/45, 2/17/09), which is tentatively scheduled for discussion on **Wednesday, March 4, 2009**. At the time of circulation of this paper to the Board, the Secretary's Department has not received a communication from the authorities of Bulgaria indicating whether or not they consent to the Fund's publication of this paper; such communication may be received after the authorities have had an opportunity to read the paper.

Questions may be referred to Mr. Bakker (ext. 34649) and Ms. Zhou (ext. 34297) in EUR.

Unless the Documents Section (ext. 36760) is otherwise notified, the document will be transmitted, in accordance with the procedures approved by the Executive Board and with the appropriate deletions, to the European Central Bank and the WTO Secretariat on Wednesday, February 25, 2009; and to the European Bank for Reconstruction and Development, the European Commission, the European Investment Bank, and the Organisation for Economic Cooperation and Development, following its consideration by the Executive Board.

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities. This supplement is not being disseminated in hard copy. It can be accessed in the Institutional Repository. A link to this document can be found in the daily list (<http://www-int.imf.org/depts/sec/services/eb/dailydocumentsfull.htm>) for the issuance date shown above.

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INTERNATIONAL MONETARY FUND

BULGARIA

Staff Report for the 2008 Article IV Consultation—Informational Annex

Prepared by the European Department

February 13, 2009

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Appendix I. Bulgaria—Financial Position in the Fund
(as of January 31, 2009)

I.	Membership Status: Joined September 25, 1990				
II.	General Resources Account:	SDR Million		%Quota	
	Quota	640.20		100.00	
	<u>Fund holdings of currency</u>	606.69		94.77	
	<u>Reserve Position</u>	33.53		5.24	
	<u>Holdings Exchange Rate</u>				
III.	SDR Department:	SDR Million		% Allocation	
	<u>Holdings</u>	4.20		N/A	
IV.	Outstanding Purchases and Loans: None				
V.	<u>Latest Financial Arrangements:</u>				
	<u>Type</u>	<u>Date of Arrangement</u>	<u>Expiration Date</u>	<u>Amount Approved (SDR Million)</u>	<u>Amount Drawn (SDR Million)</u>
	Stand-By	Aug. 6, 2004	Mar. 31, 2007	100.00	0.00
	Stand-By	Feb. 27, 2002	Mar. 15, 2004	240.00	240.00
	EFF	Sep. 25, 1998	Sep. 24, 2001	627.62	627.62
VI.	Projected Payments to Fund: None				
VII.	Implementation of HIPC Initiative: Not Applicable				
VIII.	Implementation of Multilateral Debt Relief Initiative (MDRI): Not applicable				
IX.	Resident Representative				

Mr. Fernandez-Ansola is the Senior Regional Resident Representative, based in Bucharest. He took up the position on September 4, 2006.

APPENDIX II. BULGARIA: IMF-WORLD BANK RELATIONS

A. Partnership in Bulgaria's Development Strategy

1. The World Bank has been leading the policy dialogue in structural and institutional reforms aimed at Bulgaria's successful EU integration and convergence. On June 13, 2006 the Board of Directors discussed the Country Partnership Strategy (CPS) of the Bank which outlined the roadmap for the Bank's country support for the period FY07-09. The strategic priorities of the CPS focus on: (i) productivity and employment; (ii) fiscal sustainability and absorption of EU funds; and (iii) social inclusion. In addition to the Bank's ongoing lending operations in areas such as revenue administration, social investment and employment promotion, district heating, and environment, the CPS includes a three-year program of three development policy loans (DPLs) of up to US\$150 million each that supports institutional reforms in the social sectors. In addition, the CPS program includes investment lending in road, trade and transport facilitation for South East Europe, social inclusion, and municipal infrastructure, most of which is already effective. The Bank continues to undertake diagnostics providing a solid base for policy dialogue and design and implementation of its lending operations in Bulgaria.

B. IMF-World Bank Collaboration in Specific Areas

2. The Bank has the lead on the dialogue on the core structural aspects of the reforms while the Fund has the lead on the dialogue on the macroeconomic, in particular fiscal and financial sector, aspects of the reforms. The IMF leads in the areas of macroeconomic stability, fiscal, income, external sector policies, and its analyses serve as inputs into World Bank policy formulation and advice. The Bank and the Fund share responsibility in the financial sector, public expenditure management and budgeting, and tax administration.

B.1. Areas of shared responsibility

3. **Financial Sector.** In late 2001, staff of the two institutions carried out a joint IMF-World Bank *Financial Sector Assessment Program* (FSAP) for Bulgaria, providing a shared perspective on the development agenda of the country and on the prioritization and sequencing of reforms in the financial sector. Key findings of the FSAP have been used as conditionalities on financial sector policies under both the SBA and the PAL program. A follow-up to the FSAP was undertaken by Fund staff in the context of the 2004 Article IV Consultation mission in March–April 2004 with the most recent update completed in June 2008.

4. **Revenue Administration.** Joint World Bank-IMF efforts led to the Revenue Administration Reform Project (€31.9 million), approved by the Bank's Board in 2003, under which the new National Revenue Agency became operational on January 1, 2006, integrating collection of tax and social security revenues and establishing an economically

efficient public revenue collection system that facilitates private sector development and complies with EU requirements.

5. **Public Expenditure Management.** The Bank has taken the lead in the dialogue on the efficiency and effectiveness of public expenditures and has outlined policy directions in the context of the Public Expenditure and Institutional Review¹ of 2002, and the Public Finance Policy Review² of 2006.

B.2. Areas where the World Bank leads and its analyses serve as inputs into the IMF policy formulation and advice.

6. **Education.** The Bank has supported the government program in education. The first and the second DPLs, which were approved by the Bank's Board respectively in March 2007 and November 2008, support the deepening of education reforms, in particular strengthening of the institutional capacity of the Ministry of Education and Science to assess the quality of education, and improve school governance and financing system. In addition, a second Public Finance Policy Review³, that was finalized in 2007, outlined options for reforms aimed at improving quality of education at all levels with special focus on vocational education and training as well as the quality of and access to tertiary education.

7. **Health.** The Bank has supported the government program in health through two investment operations and the DPL program. The Bank's first and second DPLs focused on strengthening the financial sustainability of the national health insurance system and enhancing the efficiency of public spending on hospitals and pharmaceuticals.

8. **Social protection programs.** Social protection programs—pensions, labor market programs, social assistance, and short-term and family benefits—have a wide coverage among the population. The Bank's first and second DPLs support an employment promotion program, which includes interventions to alter incentives both on the labor supply and the labor demand sides. To create additional incentives for job searching and lower reliance of able-bodied individuals on social welfare programs, the government has changed eligibility criteria of some social assistance programs. The Bank has recently completed a policy note

¹ *Bulgaria: Public Expenditure Issues and Directions for Reform*, August 2002, The World Bank (Report No. 23979-BUL).

² *Bulgaria: Public Finance Policy Review – Leveraging EU Funds for Productivity and Growth*, February 2006, The World Bank (Report No. 33992-BG).

³ *Bulgaria: Accelerating Bulgaria's Convergence: The Challenge of Raising Productivity*, July 2007, The World Bank (Report No. 38570).

focusing on policies to raise employment and address emerging shortages of labor and skills mismatches.

The Bank has embarked on a multi-year poverty monitoring program aimed at assessing the impact of government policies and economic growth on the poor. The first poverty monitoring report, that is currently being finalized, provides a feedback loop so that policy adjustments can be made as appropriate to take account of findings. In addition, the Bank's Board approved recently a Social Inclusion Loan aimed at addressing longer term constraints to social inclusion, and facilitating the government's absorption of grants from the European Social Fund.

C. The World Bank Group Strategy and Lending Operations

9. **The Country Partnership Strategy (CPS) for Bulgaria**⁴, discussed by the Bank's Board on June 13, 2006, focused on three main themes: (i) productivity and employment, (ii) fiscal sustainability and absorption of EU funds, and (iii) social inclusion.

10. **The World Bank's assistance program in Bulgaria to date comprises 43 IBRD operations with a total original commitment of US\$2,655 million equivalent**, consisting of 14 adjustment loans (US\$1,525.8 million), 22 investment projects (US\$1004.4 million), one debt reduction loan (US\$125.0 million), four Bank-managed Global Environmental Fund (GEF) grants, and two Bank-managed Prototype Carbon Fund (PCF) operations. Of these 43 operations, 31 have been completed, of which eleven have been partially cancelled during implementation, and 11 operations are currently under implementation (Table 1).

⁴ Memorandum of the President of the International Bank for Reconstruction and Development and the International Finance Corporation to the Executive Directors on a Country Assistance Strategy of the World Bank Group for Bulgaria, May 31, 2006.

Table 1. Bulgaria–Active World Bank Operations (Net of Cancellations)

Operation	US\$ million	Board Date
1. Registration and Cadastre	24.2	2001
2. Wetlands Restoration and Pollution Reduction (GEF Grant)	7.5	2002
3. Social Investment and Employment Promotion	69.3	2002
4. Revenue Administration Reform Project	34.2	2003
5. District Heating Project (PCF)	5.0	2003
6. Wood Residue to Energy (PCF)	1.6	2003
7. Energy Efficiency (GEF Grant)	10.0	2005
8. Second Trade and Transport Facilitation in Southeast Europe (TTFSE 2)	52.8	2007
9. Road Infrastructure Rehabilitation Project	122.5	2007
10. Second Social Sectors Institutional Reform Development Policy Loan (SIR DPL 2)	150.0	2008
11. Social Inclusion Project	59.0	2008

11. **Economic and Sector Work.** The country diagnostic work recently completed by the Bank includes a Public Finance Policy Review focused on reforms in labor and product markets, education and R&D aimed to boost productivity and employment and thus accelerate convergence to EU income levels. Various pieces of country diagnostic work have been finalized. These include a Judiciary Public Expenditure and Institutional Review focusing on developing a judiciary-wide modernization program to improve judiciary's performance and accountability; an investment climate assessment benchmarking study on product market regulation in Bulgaria compared with OECD countries; and a regulatory impact assessment study. In addition the following studies are currently being finalized: programmatic poverty monitoring and an investment climate assessment.

12. **IFC, as of November 2008, has 17 projects in its portfolio with total commitments of US\$505 million for its own account and an additional US\$234 syndicated from partner banks.** In the financial sector, IFC has supported two specialized SME banks, established Bulgaria's first micro lending bank, and has invested in a venture capital fund that also targets the SME sector. IFC has been involved in an oil and gas project in the country and is investing in a renewable energy plant in the North of the country, which will considerably add to the renewable energy capabilities of Bulgaria and contribute to the government's sustainable development goals. IFC has also supported a company investing in agricultural land and promoting land consolidation. Also, IFC has invested in a number of key manufacturing projects to support a cement plant modernization, the expansion and modernization of an electronic assembly facility, the rehabilitation and capacity increase of a wood panel production facility, revamping of a copper processing facility, and a project in retail sector to establish discount stores, hypermarkets and distribution centers in the country.

As a good example of South-South investments, IFC has committed about US\$90 million to support post-privatization restructuring of a steel mill and two glass processing plants.

Questions may be referred to Ms. Stella Ilieva (3592-9697-251).

APPENDIX III. BULGARIA: STATISTICAL ISSUES

1. Data provision is generally adequate for surveillance purposes. Bulgaria has participated in the SDDS since 2003.

Real sector

2. The National Statistical Institute (NSI) is responsible for compiling national accounts, based on a system consistent with the *System of National Accounts 1993 (SNA 1993)* and the *European System of Accounts 1995*. GDP data by activity and expenditure categories are compiled and reconciled within an annual supply and use framework. However, government output and final consumption are estimated on a cash basis. In addition, published national accounts include current and capital accounts for the five main domestic sectors (general government, financial corporations, nonfinancial corporations, nonprofit institutions serving households, and households). Work is underway on compiling financial accounts and balance sheets.

3. The NSI has compiled estimates of quarterly GDP by the production and expenditure approaches in current and constant prices since 1994. The preliminary data are now disseminated 70 days (from the previously 80 days) after the end of the reference quarter with final figures disseminated after approximately 5 quarters. The annual data are disseminated about 5 quarters after the end of the reference year. The estimates at constant prices, which follow international standards, use chain-linked indices. Problems remain in the coverage of private sector activities as well as regarding constant price estimates of capital formation and external trade, although progress has been made in the development of export and import deflators.

4. On price data, the NSI produces a domestic consumer price index (CPI), a harmonized consumer price index (HICP) according to Eurostat methods, and a producer price index (PPI). All are updated monthly. The CPI series begins in 1995, the PPI in 2000 and the HCPI in 2005 (for earlier years it is set equal to the CPI). The coverage of the CPIs was extended, although they still exclude some important sectors, mainly owner-occupied housing and health and life insurance. Since 2004, financial services are included. The geographical coverage of the index is restricted to 27 urban areas that account for an estimated 65 percent of sales.

5. The flow of customs data has improved significantly in recent years and a new system for processing customs records is near completion. The development of export and import unit value indices is progressing smoothly and additional support is expected from Eurostat in this area. The current indices are used as deflators for the import and export components of the national accounts. The Import and Export Division of the NSI meets monthly with the BNB to review data issues and ensure consistency between the NSI export and import data and the balance of payments data.

6. The national account data on employment and hours worked are compiled by the NSI based on Labor Force Survey and adjusted according to the ESA'95 methodology. The NSI also obtains current monthly estimates from a quarterly survey of establishments using all public enterprises and a sample of private employers that excludes establishments with less than five employees. The sample included 14,500 private employers out of approximately 142,000 qualifying private enterprises. The NSI household labor force survey is an alternative source of data, but improvements are needed to make it more consistent with the establishment survey, especially regarding agricultural employment. The survey is conducted four times a year.

7. The NSI also compiles and publishes wage data for various economic sectors. The main shortcomings include: (i) under-reporting of private sector wages; and (ii) reporting of average gross earnings only, not wages for time worked and wages by occupation. However, the National Social Security Institute (NSSI) administrative data are used to estimate wages by occupation and age (as well as the number of self-employed and employment in small firms). The household budget survey could provide an alternative source of data for private sector wages.

8. A Population Census was conducted in early 2001 and is a source for redesigning the household surveys conducted by the NSI, particularly the household budget survey and the labor force survey.

Government finance

9. In recent years, following the recommendations of a combined STA/FAD mission and within the framework of fiscal reporting requirements for EU accession, the authorities have made significant progress on implementing accrual accounting for government, budgetary and statistical systems. Consolidated data on central government operations are routinely reported for publication in the *GFS Yearbook* and in *IFS*. For the *GFS Yearbook 2006*, 2005 data for the general government sector and its subsectors were reported on a cash basis. Since September 2008, the Ministry of Finance (MOF) prepares and submits the SDDS indicators for the central government finances in the IMF's GFSM 2001 format. The same indicators are published on the MOF's website on a monthly and quarterly basis.

10. The Ministry of Finance prepares data on the execution of the consolidated government budget on a monthly basis. These data do not conform to *GFS* standards. Aggregate data on revenue, expenditure, balance of the general government and composition of the financing are published in the monthly bulletin and posted on the MOF's website. The authorities have made progress in presenting data on a disaggregated basis, including expenditure by functional classification. In addition, a full economic classification of expenditure is now available, and the authorities have provided such data on an annual basis back to 1998.

Money and banking statistics

11. In 2002, the BNB began to harmonize progressively its data collection and compilation methods in line with the ECB's framework for monetary statistics. The revised data for June 1995 and onward resulting from these efforts are published in IFS. Recent work in mid-2006 aimed at fully meeting the remaining ECB requirements beginning in February 2007, in accordance with 1995 ESA, the institutional coverage of monetary financial institutions includes money market funds. Consistency in the coverage of the BNB's claims on banks (which included claims on liquidated banks) and the banks' liabilities to the BNB improved in January 2003 after the BNB wrote off most of the claims on the liquidated banks.

Balance of payments

12. Bulgaria reports monthly balance of payments and external debt data on a regular and timely basis, but data on reinvested earnings by foreign-owned companies are subject to large revisions due to incomplete responses on surveys used for preliminary estimates. The data on reinvested earnings and equity are revised with the annual survey of the NSI on foreign direct investment in non-financial enterprises. In early 2006, the authorities revised the methodology for estimating trade-related transportation receipts and payments to align it more closely with actual costs. Since joining the EU in January 2007, the trade data with EU countries are being collected following the INTRASTAT system.

Table 1. Bulgaria: Common Indicators Required for Surveillance
As of February 10, 2009

	Date of latest observation	Date received	Frequency of data ⁶	Frequency of reporting ⁶	Frequency of publication ⁶	Memo Items:	
						Data Quality – Methodological soundness ⁷	Data Quality Accuracy and reliability ⁸
Exchange Rates	Feb 2009	02/10/2009	D and M	D and M	D and M		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities ¹	Dec 2008	01/23/2009	M	W	D		
Reserve/Base Money	Dec 2008	01/23/2009	W/M	M	D and M	O, O, LO, LO	O, O, O, O, O
Broad Money	Dec 2008	01/23/2009	W/M	M	W/M		
Central Bank Balance Sheet	Dec 2008	01/23/2009	W/M	W/M	W and M		
Consolidated Balance Sheet of the Banking System	Dec 2008	01/23/2009	M	M	M		
Interest Rates ²	Feb 2009	02/10/2009	D/W/M	D/W/M	D/W/M		
Consumer Price Index	Dec 2008	01/13/2009	M	M	M	O, LO, O, O	LO, LO, O, O, O
Revenue, Expenditure, Balance and Composition of Financing ³ – General Government ⁴	2007	1/31/2008	A	A	A	O, LO, O, LO	LO, O, O, O, NO
Revenue, Expenditure, Balance and Composition of Financing ³ – General Government ⁴	Dec 2008	01/29/2009	M	M	M		
Stocks of General Government and General Government-Guaranteed Debt ⁵	Nov 2008	01/23/2009	M	M	M		
External Current Account Balance	Nov 2008	01/23/2009	M	M	M	LNO, LO, O, LO	LNO, LNO, LNO, LO, LO
Exports and Imports of Goods and Services	Nov 2008	01/23/2009	M	M	M		
GDP	2008 Q3 (Quarterly); 2007 (Annual)	12/15/2008	Q/A	Q/A	Q	O, LO, O, LO	O, O, O, O, O
Gross External Debt	Nov 2008	01/23/2009	M	M	M		

¹Includes reserve assets pledged or otherwise encumbered as well as net derivative positions. ²Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds. ³Foreign, domestic bank, and domestic nonbank financing. ⁴On a gross cash basis. The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and local governments. ⁵Including currency and maturity composition. ⁶Daily (D); Weekly (W); Monthly (M); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA). ⁷Reflects the assessment provided in the data ROSC published in December 2003, which is based on the findings of the mission that took place during January 15-30, 2003 for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning (respectively) concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), or not observed (NO). ⁸Same as footnote 7, except referring to international standards concerning (respectively) source data, statistical techniques, assessment and validation of source data, assessment and validation of intermediate data and statistical outputs, and revision studies.