

Monitoring Bulgaria: Building momentum ahead of the euro era

Bulgaria's economy gained momentum in 2025, led by consumption and investment, despite weak exports and an industrial drag. The country's euro adoption on 1 January 2026 is set to unlock new growth potential, especially in services, tourism, and financial flows



The catch-up process is currently in full swing for Bulgaria

Bulgaria at a glance

- **GDP growth and outlook:** Bulgaria's GDP growth accelerated in the first half of 2025, driven by private consumption and investments, but net exports remained a drag. We've marginally increased our growth estimate from 3.0% to 3.3% in 2025 and from 2.3% to 2.7% in 2026.
- **Sectoral performance:** While construction, services (especially IT and tourism) and public sector output improved, industry and trade sectors continued to struggle. The industrial recovery may be supported by infrastructure investments and fiscal stimulus in Europe.
- **Trade & balance of payments:** The trade deficit widened significantly due to weak external demand and strong imports. Tourism remains a bright spot, with rising EU arrivals and expanded offerings.
- **Inflation:** Inflation rose to 5.3% in July-August, driven by wage growth, demand, and VAT changes. We expect it to close the year at 5.7%, easing to around 3.0% by the end of 2026.
- **Fiscal policy:** Fiscal spending focused on consumption and investment, with EU fund pre-financing impacting the cash deficit. Deficits are projected to stay around 3.0% of GDP,

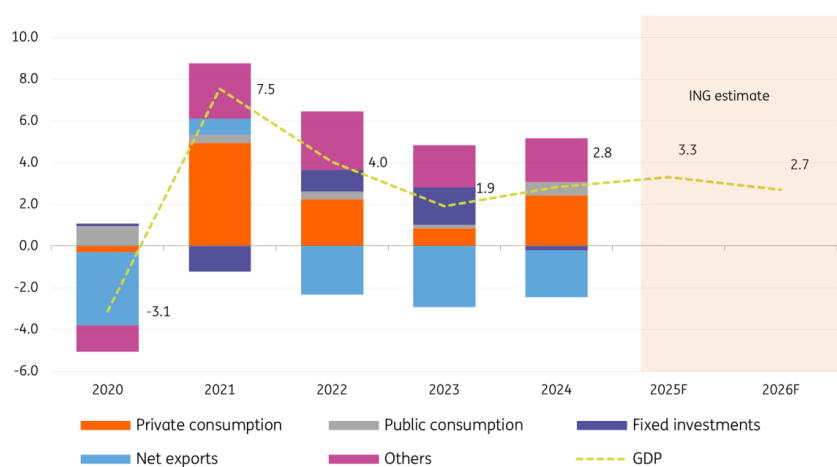
supported by rising tax revenues and potential EU reimbursements.

GDP growth: picking up but not without caveats

Annual growth in Bulgaria picked up in the first half of 2025, with private consumption and investments as key contributors. The latter even saw double-digit growth over the period. On the other hand, net exports weighed on growth given weak external demand. The tight labour market, doubled by persistent wage growth, kept the tailwind alive for consumption. Fiscal stimulus was also at play, propping up demand and key investment projects to an extent.

On the supply side of the economy, amongst the largest contributors, the industrial and trade sectors continued to struggle, while the public sector output improved. The construction and services sectors, more broadly, brought improvements to the table.

GDP growth (YoY) and contributions to growth (ppt)



Source: NSI, ING

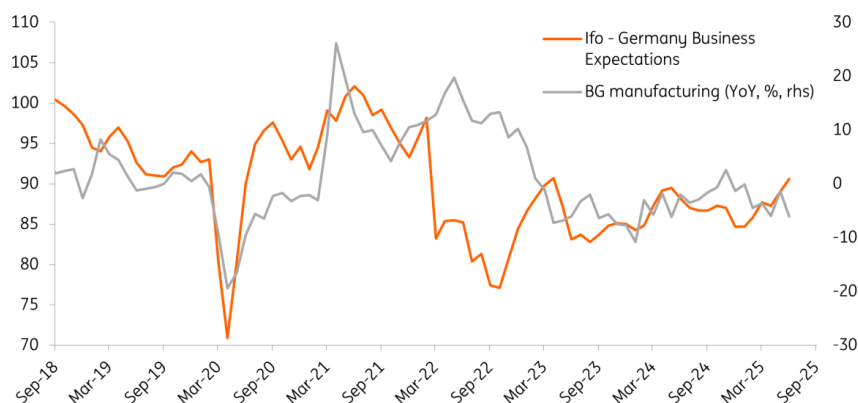
On the outlook, we expect GDP growth to firm up slightly and reach 3.3% in 2025, before moderating towards 2.7% in 2026 as the consumption cycle loses some speed and base effects come into play. Net exports should remain a burden for growth, at least this year, as the consumption momentum continues to provide tailwinds for imports. Concerning exports and industry, growth numbers could start looking better through 2026 on the back of a more stimulative fiscal policy across Europe, especially Germany.

Moreover, the added benefits of the euro adoption and Schengen membership, as well as some marginal productivity improvements on the back of recent and upcoming investments, should continue to benefit output. In this context, we expect the services sector to stimulate some pockets of growth through certain subsectors.

One such example is the IT sector, which should still show some regional competitive benefits on the one hand, at a time when both the local financial sector and the broader business environment need system overhauls in the euro adoption process. Financial services should also benefit from growth, especially as significantly more liquidity should be available in the market once Bulgarian banks align with the European Central Bank's minimum reserve requirements for eurozone banks.

On top of that, tourism momentum should also see some tailwinds, given the recently added flight routes and the local hospitality businesses on offer continuing to broaden. Overall, these factors should help to mitigate – at least to some extent – the still-struggling industrial sector's development.

Industry: improvements would be welcomed



Source: NSI, Ifo Institute, ING

The situation in industry remains lacklustre, with the weaknesses of previous years continuing into 2025, setting the stage for another contractionary year. The ongoing lack of momentum in German and Romanian industrial activity was a contributing factor here.

In manufacturing, year-to-date data up to July shows another contraction and levels of activity roughly on par with pre-pandemic benchmarks. The other key components, both mining and quarrying, as well as energy production, remain more visibly below their pre-pandemic levels.

Granted, the overhaul of copper production facilities (a key export component) throughout this year was also a factor that has been preventing a bit more upside. Nonetheless, capacity expansion on this front and our team's view that copper prices are set for a rise next year should benefit output.

In the short-to-medium term, new capital expenditure in rail and port infrastructure, as well as defence-related production and infrastructure, should provide some new boosts to certain parts of activity – all in the context of a likely more secure and competitive energy provision on the back of the Vertical Corridor project. Fiscal stimulus in Germany should also leave a positive mark on industrial exports, although the extent of the upside potential is yet to be confirmed.

Trade and the balance of payments: consumption driven

The trade deficit deteriorated visibly through the first half of the year, rising by a whopping 62% in annual terms. EU-side demand softness has been a key element here, with exports falling 3.5% and imports rising 2.9%, in line with deficit levels that accounted for 52% of the EUR 3.4 bn total trade deficit increase through H1 2025 vs H1 2024.

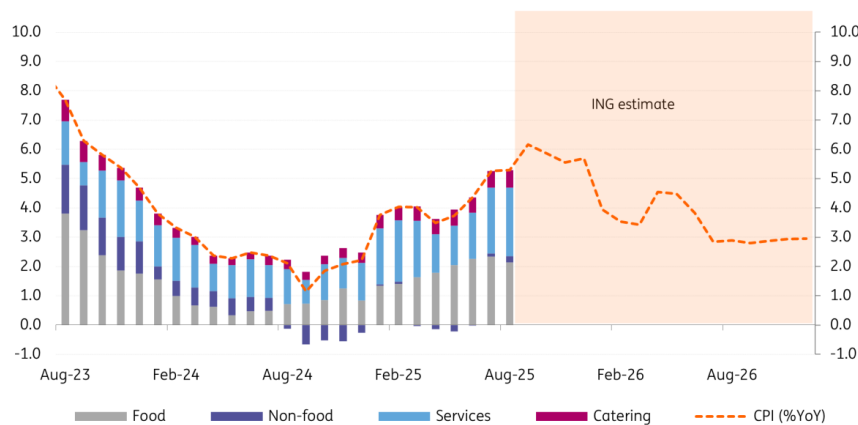
Overall, worsening trade balances with Germany, Turkey and China have been the key drivers of the trade deficit, amplified by the strong consumer momentum at a time when external demand was rather lacklustre. On the other hand, a partial counterbalance of this came from significant

improvements in the trade balance with Romania (most likely from energy and key inputs for Romania’s capex pull) and Algeria (given the strong wheat exports). Overall, the 15.2% rise in the exports to Romania, which now reached EUR 4.5 bn, has been a key trade development this year, in level terms remaining second only to the German exports of EUR 5.6 bn, which fell 14.6% over the same period.

On the services front, the country should continue to benefit from another year of healthy tourism inflows. Tourist arrivals were up 2.5% in annual terms in January-August, with a rise in EU arrivals of 14.0% over the same period, at a time when new external flight routes have been introduced. More broadly, Bulgaria’s resorts (both seaside and mountain) remain a good value-for-money travel destination, especially at a time when the European economy continues to search its ways towards better growth prospects. Upside potential ahead stems from the further development of year-round tourism products centred on city breaks/cultural activities, balneology, corporate retreats and medical tourism.

Concerning other BoP categories, the capital account and secondary income accounts should be boosted by new EU funds inflows stemming from at least a partially approved second payment request (re-submitted in July 2025), and next year from a third request intended to be sent by the end of this year. On foreign investments, the quartet of Schengen, euro, competitive taxes and nearshoring trends should continue to make a strong case for FDIs in the medium-to-long term. The relocation of some production facilities from neighbouring countries is also key to watch ahead. Tailwinds from Nato and EU defence initiatives with dual civil-military uses provide upside potential.

Inflation: a contained short-term uprising in sight



Source: NSI, ING

Price pressures saw a discernible pick-up over the summer months and have remained rather elevated throughout the whole year. Labour costs, firm private demand, and restored VAT rates were the key culprits. Putting some numbers to it, inflation averaged 3.9% in the first half of 2025, before picking up to a constant 5.3% in July-August.

We expect the upward momentum to carry on through year-end, and we have pencilled in a 5.7% print in December, with a temporary overshoot above 6.0% in autumn. Next year, we expect the inflationary situation to cool off but not disappear entirely – we foresee price pressures converging

towards 3.0% by the end of 2026.

Fiscal: attention required

Throughout the first eight months of the year, fiscal policy has been oriented towards both consumption and investment-related spending. Compensation of employees and social expenditures sat at around 72% of total spending in the last reading; this was similar to the outcome recorded in 2024, when the ratio increased compared to the 2021-2023 period, averaging around 65%. The sustainability of the public income trajectory has started to gain prominence in public debates.

That being said, the local pre-financing of projects that benefit from EU money, which have not yet been reimbursed, is also significant and accounts for 35% of the budget shortfall up to August. This wasn't the case in previous years, and it currently impacts the cash deficit. The resubmitted second payment request, should it come in due course, should make up for a significant part of the EU funds cash gap recorded so far.

In principle, should the reforms and milestones stay largely on track from now on, keeping the ESA deficit at or below the 3.0% threshold and sticking to the Public Finance Act should be feasible – even if the cash deficit may see more upside in the meantime. Concerning the sustainability measures, the current consumption trends go hand in hand with an increase in tax revenues (as a percentage of total revenues and versus non-tax revenues). Indeed, tax collection could have also played a role, but the current private spending trends seem to allow (at this stage) for a predictability cushion when it comes to various tempering measures of public income growth, if needed.

All in all, our current base case remains for deficits of around 3.0% this year and in 2026, with potentially higher prints on the cash series given EU refund timing or potential defence-related one-offs.

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