European
Commission

ISSN 2443-8014 (online)

Convergence Report 2025

on Bulgaria

INSTITUTIONAL PAPER 320 | JUNE 2025

EUROPEAN ECONOMY

Economic and
Financial Affairs

European Economy Institutional Papers are important reports analysing the economic situation and economic developments prepared by the European Commission's Directorate-General for Economic and Financial Affairs, which serve to underpin economic policy-making by the European Commission, the Council of the European Union and the European Parliament.

This paper exists in English only and can be downloaded from https://economy-finance.ec.europa.eu/ecfin-publications_en.

Luxembourg: Publications Office of the European Union, 2025

PDF ISBN 978-92-68-27418-7 ISSN 2443-8014 doi:10.2765/0736961 KC-01-25-050-EN-N

CREDIT
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European Commission
Directorate-General for Economic and Financial Affairs

Convergence Report 2025

on Bulgaria

EUROPEAN ECONOMY

Institutional Paper 320

ABBREVIATIONS

Member States

BG	Bulgaria
EA	Euro area
EA-20	Euro area, 20 Member States
EA-19	Euro area, 19 Member States before 2023
EA-18	Euro area, 18 Member States before 2015
EA-17	Euro area, 17 Member States before 2014
EU-28	European Union, 28 Member States
EU-27	European Union, 27 Member States before July 2013 (i.e. EU-28 excl. HR) and from February 2020 (i.e. EU-28 excl. UK)
EU-25	European Union, 25 Member States before 2007 (i.e. EU-28 excl. BG, RO and HR)
EU-15	European Union, 15 Member States before 2004

Currencies

EUR	Euro
BGN	Bulgarian lev
USD	United States dollar

Central Banks

BNB	Bulgarska narodna banka (Bulgarian National Bank – central bank of Bulgaria)

Other abbreviations

AML	Anti-money laundering
AMR	Alert Mechanism Report
BoP	Balance of Payments
CAR	Capital adequacy ratio
CBA	Currency board arrangement
CEE	Central and Eastern Europe
CIT	Corporate Income Tax
CPI	Consumer price index
CR5	Concentration ratio (aggregated market share of five banks with the largest market share)
EC	European Community
ECB	European Central Bank
EDP	Excessive Deficit Procedure
EMU	Economic and monetary union
ERM II	Exchange rate mechanism II
ESA	European System of Accounts
ESCB	European System of Central Banks
EU	European Union
Eurostat	Statistical Office of the European Union
FDI	Foreign direct investment
FGS	Funding for Growth Scheme
FSA	Financial Supervisory Authority
GDP	Gross domestic product
HICP	Harmonised index of consumer prices
IDR	In-Depth Review
MFI	Monetary Financial Institution

MIP	Macroeconomic Imbalance Procedure
NCBs	National central banks
NEER	Nominal effective exchange rate
NPL	Non-performing loans
OJ	Official Journal
OJL	Official Journal Lex
PIT	Personal Income Tax
PPS	Purchasing Power Standard
REER	Real effective exchange rate
RRF	Recovery and Resilience Facility
RRP	Recovery and Resilience Plan
SGP	Stability and Growth Pact
TFEU	Treaty on the Functioning of the European Union
ULC	Unit labour costs
VAT	Value added tax

ACKNOWLEDGEMENTS

The Convergence Report and its Technical Annex were prepared in the Directorate-General for Economic and Financial Affairs. The main contributors were Cvetan Kyulanov, Ivan Lozev, Benedetta Martinelli, Alina Radut and Adriana Reut.

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Statistical assistance was provided by Grzegorz Janowicz and Jannik Sielmann, and administrative assistance by Dicle Akbay, Simona State and Emel Yavuz.

The report benefited from comments and suggestions by Declan Costello, Vierke Hauke and Massimo Suardi.

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Convergence Report 2025 on Bulgaria

(prepared in accordance with Article 140(1) of the Treaty)

EUROPEAN
COMMISSION

Brussels, 04.06.2025
COM(2025) 303 final

REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

CONVERGENCE REPORT 2025

(prepared in accordance with Article 140(1) of the Treaty on the Functioning of the European Union)

{SWD(2025) 154 final}

1. PURPOSE OF THE REPORT

The euro is meant to be the single currency of the European Union as a whole. It is currently used every day by around 350 million people in the 20 Member States of the euro area. The practical benefits include more stable prices, lower transaction costs for people and businesses, more transparent and competitive markets and increased intra-EU and international trade. The euro is also the second most used currency worldwide.

Article 140(1) of the Treaty on the Functioning of the European Union (TFEU) requires the Commission and the European Central Bank (ECB) to report to the Council, at least once every two years, or at the request of a Member State with a derogation[1], on the progress that Member States have made in fulfilling their obligations to achieve economic and monetary union. The latest Commission and ECB convergence reports were adopted in June 2024.

The 2025 Convergence Report on Bulgaria has been prepared in response to a request for a convergence assessment from Bulgaria, submitted on 25 February 2025. The staff working document accompanying this report provides a more detailed assessment of the state of convergence in Bulgaria[2].

Article 140(1) TFEU requires the reports to include an examination of the compatibility of national legislation, including the statutes of national central banks, with Articles 130 and 131 TFEU and the Statute of the European System of Central Banks and of the European Central Bank ('the ESCB/ECB Statute'). The reports must also examine whether a high degree of sustainable convergence has been achieved in the Member State concerned by means of: (i) referring to the fulfilment of the four convergence criteria (price stability, public finances, exchange rate stability and long-term interest rates); and (ii) taking account of other factors relevant to economic integration and convergence mentioned in the final subparagraph of Article 140(1) TFEU. The four convergence criteria are developed further in a protocol annexed to the Treaties (Protocol No 13 on the convergence criteria).

The convergence assessment in this report is presented against the background of recent economic and policy developments. Following the EU's weak economic performance in 2023, when GDP grew by 0.4%, the economy returned to moderate growth of 1.0% in 2024, with stronger momentum at the end of the year than previously expected. Private consumption was supported by continued growth in real wages and higher employment, with a remarkably strong labour market. After the peak in EU inflation in October 2022, which was driven by the surge in energy prices from around mid-2021 until the third quarter of 2022, a disinflationary process started towards the end of 2022. This process progressed in 2023 and throughout much of 2024, with EU headline inflation averaging 2.6% that year, and is expected to continue in 2025. Inflation divergence across the EU Member States also narrowed significantly in 2024. With the disinflation process well on track, in April 2025 the ECB cut its policy rate for the seventh time since June 2024, to 2.25%.

The economic outlook, including the Commission's 2025 Spring Economic Forecast for HICP inflation for the EU as a whole and for individual Member States, including Bulgaria, is characterised by an unusually high degree of uncertainty. In early 2025, the EU and global economies were hit by the most significant policy-induced trade and economic uncertainty shock in decades. It is unclear what the landing zone for the US tariffs vis-à-vis trading partners would be, which forces the Commission forecast to rely on several technical assumptions[3]. Beyond trade, broader geopolitical tensions remain elevated, heightening risks, weighing on confidence, and posing significant risks to the economic outlook.

In Bulgaria, economic growth accelerated from 1.9% in 2023 to 2.8% in 2024, driven by private consumption, which was, in turn, sustained by higher real wages, employment gains and increased social benefits. Real GDP growth in Bulgaria is forecast to slow down again from 2.8% in 2024 to 2% in 2025. Annual average HICP inflation in Bulgaria slowed to 2.6% in 2024, while inflation developments in 2025 and in 2026 are set to be driven by several price hikes at the beginning of 2025 and, subsequently, by both external prices and domestic cost factors exerting downward pressure on inflation.

1 The Member States that have not yet fulfilled the necessary conditions to adopt the euro are referred to as 'Member States with a derogation'. Denmark negotiated an opt-out before the Maastricht Treaty was adopted and does not participate in the third stage of economic and monetary union.

2 The cut-off date for the data used in this report is 19 May 2025. The convergence assessment is based on a range of monthly convergence indicators that have been calculated up to April 2025.

3 Significantly, the individualised 'reciprocal' higher tariffs are assumed to not be reinstated at the expiry of the 90 days suspension. The forecast also assumes that the exceptionally high tariffs on Chinese imports, imposed after April 2, will be scaled back to pre-escalation levels, as they are deemed unsustainable. By the time the Commission forecast was published, on 19 May 2025, the new tariffs in place were lower than those assumed at the cut-off date.

The expected acceleration in implementing the recovery and resilience plans (RRPs) and the cohesion policy programmes can at least partly offset the negative consequences of the weaker international environment and play a crucial role in the convergence process of many non-euro area EU Member States. Besides contributing to higher growth and improved public finances in the near term, the Recovery and Resilience Facility (RRF) and cohesion policy programmes strengthen Member States' long-term growth and resilience by supporting major reforms and investments that help address both long-standing and new challenges, such as diversifying energy supplies.

In November 2024, the Commission launched the first implementation cycle of the reformed economic governance framework that entered into force on 30 April 2024. The main objectives of the new framework are to strengthen Member States' debt sustainability and promote sustainable and inclusive growth in all Member States through growth-enhancing reforms and priority investments. At the centre of the new framework are the national medium-term fiscal-structural plans, which set the Member States' fiscal paths, defined in terms of net expenditure growth rates. The plans contain priority reforms and investments and cover an adjustment period of four years as a rule. An extended adjustment period (up to seven years) can be agreed at the request of the Member State which commits to additional reforms and investments that are conducive to economic growth and fiscal sustainability. Bulgaria submitted its four-year national medium-term fiscal-structural plan on 27 February 2025. On 12 May 2025, the Commission recommended to the Council to endorse Bulgaria's plan.

On 19 March 2025, the Commission presented, as part of the ReArm Europe Plan/Readiness 2030, an ambitious defence package providing financial levers to EU Member States to drive higher investment in defence capabilities. As part of this plan, the Commission invited Member States to apply for the activation of the national escape clause (NEC) of the Stability and Growth Pact, which will provide them additional budgetary space to transition to a durably higher level of defence expenditure, within the EU fiscal rules. The amount of the deviation under the escape clause will be capped at 1.5% GDP, available for a period of four years. Bulgaria applied for the NEC on 2 May 2025. A new dedicated instrument - Security Action for Europe (SAFE) - has been established, with the Commission planning to raise up to EUR 150 billion on the capital markets to help EU Member States quickly and substantially increase investments in Europe's defence capabilities. Bulgaria submitted a request to the Council and the Commission to activate the NEC. On 4 June 2025, the Commission recommended to the Council to activate the NEC for Bulgaria, allowing the country to deviate from, and exceed, the net expenditure path that will be set in the Council recommendation endorsing its medium-term fiscal plan.

On 4 June 2025, the Commission published its European Semester Spring 2025 package. To drive long-term prosperity and resilience, the EU is aligning its economic governance with a renewed focus on competitiveness as presented in the Competitiveness Compass. Through its country-specific recommendations, the European Semester reflects the new priorities to boost competitiveness and provides guidance, including to Bulgaria, on the necessary reforms and investments at national and regional level. As part of the European Semester Spring 2025 package, the Commission recommends that Bulgaria adheres to the maximum growth rates of net expenditure in its plan, while making use of the allowance under the NEC for higher defence expenditure.

Convergence criteria

The examination of the **compatibility of national legislation**, including the statutes of national central banks of Member States with a derogation, together with Article 130 TFEU and the compliance duty under Article 131 TFEU, includes an assessment of observance of the prohibition of monetary financing (Article 123 TFEU) and the prohibition of privileged access to financial institutions (Article 124 TFEU); the consistency with the ESCB's objectives (Article 127(1) TFEU) and tasks (Article 127(2) TFEU); and other aspects relating to the integration of national central banks into the ESCB.

The first indent of Article 140(1) TFEU defines the **price stability criterion** as *'the achievement of a high degree of price stability; this will be apparent from a rate of inflation which is close to that of, at most, the three best performing Member States in terms of price stability'.*

Article 1 of the Protocol on the convergence criteria further provides that *'the criterion on price stability [...] shall mean that a Member State has a price performance that is sustainable and an average rate of inflation, observed over a period of one year before the examination, that does not exceed by more than 1.5 percentage points that of, at most, the three best-performing Member States in terms of price stability. Inflation shall be* *measured by means of the consumer price index on a comparable basis, taking into account differences in national definitions'*[4].

The sustainability requirement implies that the satisfactory inflation performance must be attributed to the behaviour of input costs and other factors that influence price developments in a structural manner, rather than the influence of temporary factors. Therefore, the convergence examination includes an assessment of the factors that affect the inflation outlook and is complemented by a reference to the most recent Commission inflation forecast[5].

The inflation reference value was calculated as 2.8% in April 2025, with Ireland, Finland and Italy being the three 'best-performing Member States'[6].

No Member States were identified as outliers in terms of inflation performance for calculating the reference value, as none of their inflation rates deviated by a wide margin from the euro area average due to country-specific circumstances.

The second indent of Article 140(1) TFEU defines the convergence **criterion dealing with public finances** is defined in the as *'the sustainability of the government financial position; this will be apparent from having achieved a government budgetary position without a deficit that is excessive as determined in accordance with Article 126(6)'.*

Furthermore, Article 2 of the Protocol on the convergence criteria states that this criterion means that *'at the time of the examination the Member State is not the subject of a Council decision under Article 126(6) of the said Treaty that an excessive deficit exists'*.

The TFEU refers to the **exchange rate criterion** in the third indent of Article 140(1) as *'the observance of the normal fluctuation margins provided for by the exchange-rate mechanism of the European Monetary System, for at least two years, without devaluing against the euro'.*

Article 3 of the Protocol on the convergence criteria provides that: *'The criterion on participation in the exchange rate mechanism of the European Monetary System [...] shall mean that a Member State has respected the normal fluctuation margins provided for by the exchange-rate mechanism of the European Monetary System without severe tensions for at least the last two years before the examination. In particular, the Member State shall not have devalued its currency's bilateral central rate against the euro on its own initiative for the same period'*[7].

The relevant two-year period for assessing exchange rate stability in this report ran from 20 May 2023 to 19 May 2025. In its assessment of the exchange rate stability criterion, the Commission takes into account developments in auxiliary indicators such as foreign reserve developments and short-term interest rates. It also takes into account the role of policy measures (including foreign exchange interventions) and international financial assistance (wherever relevant) in maintaining exchange rate stability.

The fourth indent of Article 140(1) TFEU requires *'the durability of convergence achieved by the Member State with a derogation and of its participation in the exchange rate mechanism'* to be *'reflected in the **long-term interest rate levels**'*.

Article 4 of the Protocol on the convergence criteria further states that *'the criterion on the convergence of interest rates [...] shall mean that, observed over a period of one year before the examination, a Member State has had an average nominal long-term interest rate that does not exceed by more than 2 percentage points that of, at most, the three best-performing Member States in terms of price stability. Interest rates shall be measured on the basis of long-term government bonds or comparable securities, taking into account differences in national definitions'.*

[4] For the purpose of the price stability criterion, inflation is measured by the Harmonised Index of Consumer Prices (HICP) defined in Regulation (EU) 2016/792.

[5] All forecasts for inflation and other variables in this report are from the Commission's Spring 2025 Economic Forecast. The forecasts are based on a set of common assumptions for external variables and on a 'no policy change' assumption, but also take into consideration measures that are known in sufficient detail.

[6] The respective 12-month average inflation rates were 1.2%, 1.3% and 1.4%.

[7] In assessing compliance with the exchange rate criterion, the Commission examines whether the exchange rate has remained close to the ERM II central rate. Reasons for an appreciation may be taken into account, in accordance with the Common Statement on Acceding Countries and ERM2 by the Informal ECOFIN Council held in Athens on 5 April 2003.

The interest rate reference value was calculated as 5.1% in April 2025[8].

Article 140(1) TFEU also requires the reports to take into account **other factors** relevant to economic integration and convergence. These include the integration of markets, the development of the balance of payments on the current account and of unit labour costs and other price indices. The additional factors to be considered are important indicators of whether a Member State would integrate into the euro area without difficulties. They also broaden the view on the sustainability of convergence.

The assessment of the degree of sustainable convergence for Bulgaria presented in this report draws on the Commission's Spring 2025 Economic Forecast and the policy guidance provided under the European Semester. It is informed in particular by: (i) the fiscal surveillance carried out under the Stability and Growth Pact and (ii) by the Macroeconomic Imbalance Procedure. It also reflects the Commission's assessments of fiscal sustainability risks and of the national fiscal framework, as well as the implementation of the RRP.

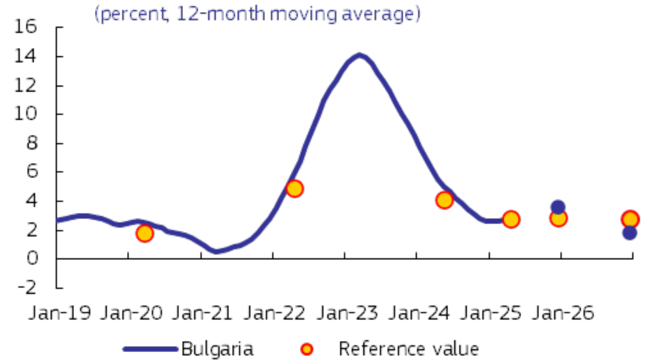
2. Bulgaria

In the light of its assessment on legal compatibility and on the fulfilment of the convergence criteria, and taking into account the additional relevant factors, the Commission considers that Bulgaria fulfils the conditions for adopting the euro.

Legislation in Bulgaria is compatible with the compliance duty under Article 131 TFEU.

Bulgaria fulfils the criterion on price stability. The average inflation rate in Bulgaria during the 12 months to April 2025 was 2.7%, below the reference value of 2.8%. A review of a broad range of indicators does not identify causes for concern regarding the sustainability of price stability.

Graph 2a: **Bulgaria - Inflation criterion**



Note: The dots at the right end of the chart show the projected reference value and 12-month average inflation rate of Bulgaria in December 2025 and December 2026. The reference values for 2020, 2022 and 2024 refer to the reference values calculated in the previous convergence reports.
Source: Eurostat, Commission's Spring 2025 Economic Forecast.

Bulgaria's annual HICP inflation rate averaged 8.6% in 2023 and decreased to 2.6% in 2024. Annual HICP inflation declined from 14.3% in January 2023, flattening at around 2.8% in May-July 2024 before declining further and stabilising at 2.1% in October-December 2024. It then rose significantly at the beginning of 2025, peaking at 4% in March before decreasing to 2.8% in April 2025. At the beginning of 2023, headline HICP inflation was still above HICP inflation excluding energy and food, due to higher energy and food price inflation. With the rapid disinflation of fuel and gas prices in 2023, overall inflation remained below core inflation for the rest of 2023. In 2024, headline HICP inflation and core inflation remained close to each other, as the fall in fuel prices in the second half of 2024 was largely offset by somewhat higher food price inflation. The sharp price hikes at the beginning of 2025 covered items both within and outside the core inflation basket. These price hikes were largely due to: (i) restored higher VAT rates for bread and restaurants; (ii) higher excise duties for tobacco; (iii) increased electricity and gas prices for households; and (iv) higher

[8] The reference value for April 2025 was calculated as the simple average of the 12-month average of long-term interest rates of Ireland (2.8%), Finland (2.9%) and Italy (3.7%), plus two percentage points.

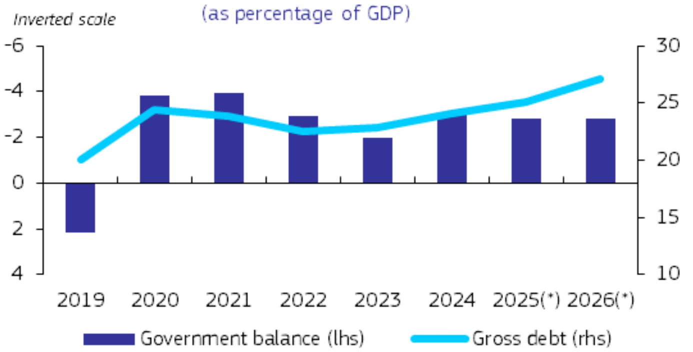
food prices due to increased international food prices. The subsequent decrease in inflation in April was largely due to reductions in hospital fees that are part of core inflation and in gas and fuel prices.

The Commission's Spring 2025 Economic Forecast projects that average annual inflation will increase from 2.6% in 2024 to 3.6% in 2025 and gradually ease to 1.8% in 2026. The 12-month average inflation rate is projected to increase above the projected reference value by the end of 2025, fall back to the reference value in the first months of 2026 and stay below it for the rest of 2026[9]. The higher VAT rates for bread and restaurants, higher excise duties for tobacco and other administered prices, including electricity, are estimated to have a full impact, including second-round effects, of around 1.5 percentage points by the end of 2025. These factors, which explain a large part of the temporary rise of inflation in 2025, are not expected to have a lasting effect on inflation. Moreover, the higher inflation in 2025 also reflects higher international prices for certain food commodities. The growth in unit labour costs moderated significantly in 2024 and, looking forward, the disinflation process in the services sector is set to benefit from wage moderation. Overall, private sector wage growth, which directly influences price formation, is expected to moderate faster than aggregate wage dynamics. On the external side, the pass-through of lower international energy and other commodities prices is also projected to keep inflation down, including via second-round effects to transport services. The relatively low price level in Bulgaria (about 57% of the euro area average in 2023) suggests potential for price level convergence in the long term.

Bulgaria fulfils the criterion on public finances. Bulgaria is not the subject of a Council Decision on the existence of an excessive deficit. The general government deficit widened from 2.0% of GDP in 2023 to 3.0% in 2024. The sizeable deterioration of the deficit in 2024 was in one part due to spending increases in public sector salaries and in social benefits, particularly on pensions, which were not fully matched by revenue increases. The other part, 0.5% of GDP, was due to a one-off statistical recording of settled liabilities for road infrastructure works from 2020-2022. The Commission's Spring 2025 Economic Forecast expects the general government deficit to decrease to 2.8% of GDP in 2025 and to remain at 2.8% in 2026. The government debt-to-GDP ratio increased from 22.9% in 2023 to 24.1% in 2024. It is expected to increase further to 25.1% in 2025 and 27.1% in 2026. On 27 February 2025, Bulgaria submitted its national medium-term fiscal structural plan to the Council and the Commission. The plan includes a commitment to fiscal consolidation in 2025-2028 in line with the Stability and Growth Pact requirements. On 12 May 2025, the Commission recommended to the Council to endorse Bulgaria's plan. Accounting for the flexibility under the NEC, the net expenditure growth for 2025 is expected to be in line with the net expenditure growth ceilings contained in Bulgaria's medium-term plan. Despite the low projected debt level by 2035 (39% of GDP), Bulgaria's debt sustainability risks appear medium in the medium term, with high uncertainty on debt dynamics over the next five years based on historical volatility. Bulgaria has the key components of a robust fiscal framework, but some difficulties in implementation remain. Bulgaria has a complex system of national fiscal rules in place and there is scope to improve key aspects, including further strengthening the mandate of the Fiscal Council.

Graph 2b: **Bulgaria - Government budget balance and debt**

(as percentage of GDP)



(*) Commission's Spring 2025 Economic Forecast.

Source: Eurostat, Commission's Spring 2025 Economic Forecast.

9 The Commission's Spring 2025 Economic Forecast does not include the impact of lower fees for hospital services and of decreases in other administered prices on inflation in April 2025. When taking into account these measures, the average inflation rate in Bulgaria would likely be close to the reference value by the end of 2025.

Bulgaria fulfils the exchange rate criterion. In July 2020, Bulgaria entered the Exchange Rate Mechanism II (ERM II) and had been participating in the mechanism for almost four years at the time of the adoption of this report. The Bulgarian lev observes a central rate of 1.95583 to the euro with a standard fluctuation band of ±15%. The Bulgarian National Bank pursues its primary objective of price stability through an exchange rate anchor as part of a currency board framework. Bulgaria joined ERM II with its existing currency board framework in place, as a unilateral commitment, thereby placing no additional obligations on the ECB. The lev exchange rate remained at the ERM II central rate for the 2 years covered by the assessment without any signs of tensions or devaluation against the euro. Additional indicators, such as developments in foreign exchange reserves and short-term interest rates, suggest that investors' risk perception towards Bulgaria has remained favourable. The (negative) spread of the Bulgarian benchmark short-term interest rate (i.e. the three-month base interest rate (BIR) to the Euribor) narrowed from -15 basis points at the beginning of 2023 to virtually no differential by the end of that year. It then widened slightly throughout 2024 and stood at 3 basis points in March 2025. A sizeable buffer of official reserves continues to underpin the currency board's resilience. Upon entering ERM II, Bulgaria committed to implement a set of policy measures (known as post-entry commitments) to ensure that its participation in the mechanism is sustainable and that it achieves a high degree of economic convergence before adopting the euro. The measures cover four policy areas: (i) the non-banking financial sector; (ii) the insolvency framework; (iii) the anti-money laundering framework; and (iv) governance of state-owned enterprises.

Bulgaria fulfils the criterion on the convergence of long-term interest rates. The average long-term interest rate in the 12-months to April 2025 was 3.9%, below the reference value of 5.1%. The Bulgarian long-term interest rate has been stable at or close to 4% since April 2023, following two stepwise increases in February and March 2023. The long-term interest rate increased from 1.9% in January 2023 to 4.2% in March. Thereafter, it remained unchanged at 4.0% for the rest of 2023 and at 3.9% throughout 2024 and up to April 2025. The yield spread relative to the German benchmark bond remained within a range of 1.4-1.9% from March 2023 to April 2025.

The Commission has also examined **additional factors**, including balance of payments developments, the integration of markets and the institutional environment. Bulgaria's external balance (the combined current and capital account) improved to 0.7% of GDP in 2023 and was almost in balance (-0.1% of GDP) in 2024. The Bulgarian economy is well integrated with the euro area through trade and investment linkages. Selected indicators related to the institutional environment show that Bulgaria performs worse than many euro area Member States. There are significant challenges related to the rule of law, fight against corruption and regulatory quality. However, as part of its participation in the ERM II and in accordance with its RRP, Bulgaria has taken measures to improve its institutional framework and the business environment, including in the four areas covered by the post-entry ERM II commitments. The financial sector in Bulgaria is smaller and less developed than in the euro area. It is dominated by the banking sector, which is well integrated into the euro area's financial sector (particularly through a high level of foreign ownership). The underdevelopment of market-based financing is reflected in the very small markets for equity and private sector debt. Continued policy action, including Bulgaria's entry into a 'close cooperation' agreement with the ECB in 2020, combined with a favourable macroeconomic environment have reduced risks to and vulnerabilities in the financial sector. As part of the Macroeconomic Imbalance Procedure, the Commission concluded in its Alert Mechanism Report for 2025 that it was not necessary to carry out an in-depth analysis for Bulgaria, while pointing to the need to monitor developments in the country's cost competitiveness, house prices and credit flows to households.

Bulgaria's RRP includes measures to address a series of structural challenges, in synergy with other EU funds, including cohesion policy funds, to boost its competitiveness and stimulate sustainable growth, and reduce the country's regional and social disparities. The RRF funding provides Bulgaria with EUR 5.7 billion in grants over the 2021-2026 period. Bulgaria received one disbursement of EUR 1.37 billion on 16 December 2022. In April 2025, Bulgaria submitted a comprehensive revision of its RRP with the aim to bring it back on track. Implementing key outstanding reforms in the areas of decarbonisation, business environment and rule of law remains important for achieving the plan's objectives. It would thus be important for Bulgaria to urgently step up its implementation of reforms and investments in order to deliver on the plan's commitments. In addition, cohesion policy funding provides Bulgaria with EUR 10.7 billion for the 2021-2027 period. Cohesion policy financing aims in particular to further support Bulgaria's competitiveness, green transition, including energy independence, the just transition and climate change resilience. It also aims to support the country's upward social convergence, including by addressing labour shortages, further developing educational and training systems and making them more inclusive for disadvantaged groups. Bulgaria has made progress in implementing EU cohesion policy but challenges remain.

Convergence Report 2025 on Bulgaria

Technical annex

1. INTRODUCTION

1.1. ROLE OF THE REPORT

The euro was introduced on 1 January 1999 by eleven Member States, namely Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain. Subsequently, Greece (2001), Slovenia (2007), Cyprus and Malta (2008), Slovakia (2009), Estonia (2011), Latvia (2014), Lithuania (2015) and Croatia (2023) also adopted the euro.

Member States for which the Council has not yet decided that they fulfil the necessary conditions for the adoption of the euro are referred to as 'Member States with a derogation'. Article 140 of the Treaty lays down provisions and procedures for examining the convergence situation of Member States with a derogation (Box 1.1). At least once every two years, or at the request of a Member State with a derogation, the Commission and the European Central Bank (ECB) prepare Convergence Reports for such Member States. Denmark negotiated an opt-out arrangement before the adoption of the Maastricht Treaty ([10]) and does not participate in the third stage of EMU. Until Denmark indicates that it wishes to participate in the third stage and adopt the euro, it will not be the subject of an assessment as to whether it fulfils the necessary conditions for such a participation.

In 2024, the Commission and the ECB adopted their latest regular Convergence Reports ([11]). None of the Member States assessed in those reports was deemed to meet the necessary conditions for adopting the euro.

On 25 February 2025, Bulgaria submitted a request for a convergence assessment. This Commission Staff Working Document is a Technical Annex to the Convergence Report 2025 on Bulgaria and includes a detailed assessment of the progress with convergence, as required by Article 140(1) of the Treaty.

The convergence assessment in this report is presented against the background of several major economic and policy developments. Following the EU's weak economic performance in 2023, when GDP grew by 0.4%, the economy returned to moderate growth of 1.0% in 2024, with stronger momentum at the end of the year. In 2024, private consumption was supported by continued growth in real wages and higher employment, with a remarkably strong labour market. The disinflationary process that started towards the end of 2022 continued to progress throughout much of 2024, with EU headline inflation averaging 2.6% that year, and is expected to continue in 2025. Inflation divergence across the EU Member States also narrowed significantly in 2024. With the disinflation process well on track, in April 2025 the ECB cut its main policy rate for the seventh time since June 2024, to 2.25%.

The economic outlook, including the Commission's 2025 Spring Economic Forecast for HICP inflation for the EU as a whole and for individual Member States, is characterised by an unusually high degree of uncertainty. In early 2025, the EU and global economies were hit by the most significant policy-induced trade and economic uncertainty shock in decades. It is unclear what the landing zone for the US tariffs vis-à-vis trading partners would be, which forces the Commission forecast to rely on several technical assumptions ([12]). Beyond trade, broader geopolitical tensions remain elevated, heightening uncertainty risks, weighing on confidence, and posing significant risks to the economic outlook.

([10]) Protocol (No 16) on certain provisions relating to Denmark.

([11]) European Commission, Convergence Report 2024, COM(2024) 270 final, 26 June 2024; European Central Bank, Convergence Report 2024, June 2024.

([12]) Significantly, the individualised 'reciprocal' higher tariffs are assumed to not be reinstated at the expiry of the 90 days suspension. The forecast also assumes that the exceptionally high tariffs on Chinese imports, imposed after April 2, will be scaled back to pre-escalation levels, as they are deemed unsustainable. By the time the Commission forecast was published, on 19 May 2025, the new tariffs in place were lower than those assumed at the cut-off date.

Box 1.1: **Article 140 of the Treaty**

'1. At least once every two years, or at the request of a Member State with a derogation, the Commission and the European Central Bank shall report to the Council on the progress made by the Member States with a derogation in fulfilling their obligations regarding the achievement of economic and monetary union. These reports shall include an examination of the compatibility between the national legislation of each of these Member States, including the statutes of its national central bank, and Articles 130 and 131 and the Statute of the ESCB and of the ECB. The reports shall also examine the achievement of a high degree of sustainable convergence by reference to the fulfilment by each Member State of the following criteria:

— the achievement of a high degree of price stability; this will be apparent from a rate of inflation which is close to that of, at most, the three best performing Member States in terms of price stability,

— the sustainability of the government financial position; this will be apparent from having achieved a government budgetary position without a deficit that is excessive as determined in accordance with Article 126(6),

— the observance of the normal fluctuation margins provided for by the exchange-rate mechanism of the European Monetary System, for at least two years, without devaluing against the euro,

— the durability of convergence achieved by the Member State with a derogation and of its participation in the exchange-rate mechanism being reflected in the long-term interest-rate levels.

The four criteria mentioned in this paragraph and the relevant periods over which they are to be respected are developed further in a Protocol annexed to the Treaties. The reports of the Commission and the European Central Bank shall also take account of the results of the integration of markets, the situation and development of the balances of payments on current account and an examination of the development of unit labour costs and other price indices.

2. After consulting the European Parliament and after discussion in the European Council, the Council shall, on a proposal from the Commission, decide which Member States with a derogation fulfil the necessary conditions on the basis of the criteria set out in paragraph 1, and abrogate the derogations of the Member States concerned.

The Council shall act having received a recommendation of a qualified majority of those among its members representing Member States whose currency is the euro. These members shall act within six months of the Council receiving the Commission's proposal.

The qualified majority of the said members, as referred to in the second subparagraph, shall be defined in accordance with Article 238(3)(a).

3. If it is decided, in accordance with the procedure set out in paragraph 2, to abrogate a derogation, the Council shall, acting with the unanimity of the Member States whose currency is the euro and the Member State concerned, on a proposal from the Commission and after consulting the European Central Bank, irrevocably fix the rate at which the euro shall be substituted for the currency of the Member State concerned, and take the other measures necessary for the introduction of the euro as the single currency in the Member State concerned.'

The expected acceleration in implementing the recovery and resilience plans (RRPs) and the cohesion policy programmes can at least partly offset the negative consequences of the weaker

international environment and play a crucial role in the convergence process of non-euro area EU Member States. Besides contributing to higher growth and improved public finances in the near term, the Recovery and Resilience Facility (RRF) and cohesion policy programmes strengthen Member States' long-term growth and resilience by supporting major reforms and investments that help address both long-standing and new challenges, such as diversifying energy supplies. The overall implementation of the RRPs progressed in 2024 and in the first four months of 2025. By the end of 2024, RRF disbursements reached EUR 306 billion, which is close to half of the total amount of support committed under the RRF. However, in a few Member States, including Bulgaria, there are significant delays in the RRF implementation. In addition, EU Cohesion Policy funds provide EUR 378 billion to Member States for the 2021-2027 period. Cohesion policy concentrates in fields that are critical for promoting convergence and competitiveness through long-term investment in line with EU priorities and will support EU GDP growth, with a particularly high impact in the Member States and regions that are the main beneficiaries of the policy.

In November 2024, the Commission launched the first implementation cycle of the reformed economic governance framework that entered into force on 30 April 2024. The main objectives of the new framework are to strengthen Member States' debt sustainability and promote sustainable and inclusive growth in all Member States through growth-enhancing reforms and priority investments. At the centre of the new framework are the national medium-term fiscal-structural plans, which set the Member States' fiscal paths, defined in terms of net expenditure growth rates. The plans contain priority reforms and investments and cover an adjustment period of four years as a rule. An extended adjustment period (up to seven years) can be agreed at the request of the Member State which commits to additional reforms and investments that are conducive to economic growth and fiscal sustainability. Bulgaria submitted its four-year national medium-term fiscal-structural plan on 27 February 2025. On 12 May 2025, the Commission recommended to the Council to endorse Bulgaria's plan.

On 19 March 2025, the Commission presented, as part of the ReArm Europe Plan/Readiness 2030, an ambitious defence package providing financial levers to EU Member States to drive an investment surge in defence capabilities. As part of this plan, the Commission invited Member States to apply for the activation of the national escape clause (NEC) of the Stability and Growth Pact, which will provide them additional budgetary space to transition to a durably higher level of defence expenditure, within the EU fiscal rules. The amount of the planned deviation under the escape clause will be capped at 1.5% GDP, available for a period of four years. A new dedicated instrument - Security Action for Europe (SAFE) - has been established, with the Commission planning to raise up to EUR 150 billion on the capital markets to help EU Member States quickly and substantially increase investments in Europe's defence capabilities. Bulgaria submitted a request, to the Council and the Commission, to activate the NEC. On 4 June 2025, the Commission recommended to the Council to activate the NEC for Bulgaria, allowing the country to deviate from, and exceed, the net expenditure path that will be set in the Council recommendation endorsing its medium-term fiscal plan.

On 4 June 2025, the Commission published its European Semester Spring 2025 package. To drive long-term prosperity and resilience, the EU is aligning its economic governance with a renewed focus on competitiveness as presented in the Competitiveness Compass. Through its country-specific recommendations, the European Semester reflects the new priorities to boost competitiveness and provides guidance, including to Bulgaria, on the necessary reforms and investments at national and regional level. As part of the European Semester Spring 2025 package, the Commission recommends that Bulgaria adheres to the maximum growth rates of net expenditure in its plan, while making use of the allowance under the NEC for higher defence expenditure.

The remainder of the first chapter presents the methodology used for the application of the assessment criteria. Chapters 2 to 7 examine the fulfilment of the convergence criteria and other requirements in the order in which they appear in Article 140(1) (see Box 1.1). The cut-off date for the statistical data included in this convergence report was 19 May 2025.

1.2. APPLICATION OF THE CRITERIA

In accordance with Article 140(1) of the Treaty, the Convergence Reports shall examine the compatibility of national legislation with Articles 130 and 131 of the Treaty and the Statute of the European System of Central Banks (ESCB) and of the European Central Bank. The reports shall also examine the achievement of a high degree of sustainable convergence by reference to the fulfilment of the four convergence criteria dealing with price stability, public finances, exchange rate stability and long-term interest rates as well as some additional factors. The four convergence criteria are developed further in a Protocol annexed to the Treaty (Protocol No 13 on the convergence criteria).

1.2.1. Compatibility of legislation

In accordance with Article 140(1) of the Treaty, the legal examination includes an assessment of compatibility between a Member State's legislation, including the statute of its national central bank, and Article 130 and 131 of the Treaty. This assessment mainly covers three areas.

- First, the independence of the national central bank and of the members of its decision-making bodies, as laid down in Article 130, must be assessed. This assessment covers all issues linked to a national central bank's institutional and financial independence and to the personal independence of the members of its decision-making bodies.
- Second, in accordance with Articles 123 and 124 of the Treaty, the compliance of the national legislation is verified against the prohibition of monetary financing and privileged access. The prohibition of monetary financing is laid down in Article 123(1) of the Treaty, which prohibits overdraft facilities or any other type of credit facility with the ECB or the central banks of Member States in favour of Union institutions, bodies, offices or agencies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States; and the purchase directly from these public sector entities by the ECB or central banks of debt instruments. As regards the prohibition on privileged access as set out in Article 124, the central banks, as public authorities, may not take measures granting privileged access by the public sector to financial institutions if such measures are not based on prudential considerations.
- Third, in accordance with Article 131, the integration of the national central bank into the ESCB has to be examined, in order to ensure that at the latest by the moment of euro adoption, the objectives of the national central bank are compatible with the objectives of the ESCB as formulated in Article 127 of the Treaty. The national provisions on the tasks of the national central bank are assessed against the relevant rules of the Treaty and the ESCB/ECB Statute.

1.2.2. Price stability

The price stability criterion is defined in the first indent of Article 140(1) of the Treaty: 'the achievement of a high degree of price stability; this will be apparent from a rate of inflation which is close to that of, at most, the three best performing Member States in terms of price stability'.

Article 1 of the Protocol on the convergence criteria further stipulates that 'the criterion on price stability [...] shall mean that a Member State has a price performance that is sustainable and an average rate of inflation, observed over a period of one year before the examination, that does not exceed by more than 1.5 percentage points that of, at most, the three best performing Member States in terms of price stability. Inflation shall be measured by means of the consumer price index on a comparable basis, taking into account differences in national definitions.

Since national consumer price indices (CPIs) diverge substantially in terms of concepts, methods and practices, they do not constitute the appropriate means to meet the Treaty requirement that inflation must be measured on a comparable basis. To this end, the Council adopted on 23 October 1995 a framework regulation ([13]) setting the legal basis for the establishment of a harmonised methodology for compiling consumer price indices in the Member States. This process resulted in the production of the Harmonised Indices of Consumer Prices (HICPs), which are used for assessing the fulfilment of the price stability criterion.

([13]) Council Regulation (EC) No 2494/95 of 23 October 1995 concerning harmonised indices of consumer prices (OJ L 257, 27.10.1995, pp. 1-4), amended by Regulations (EC) No 1882/2003 and No 596/2009 of the European Parliament and of the Council, and repealed by Regulation (EU) 2016/792 of the European Parliament and of the Council.

Box 1.2: Assessment of price stability and the reference value

The numerical part of the price stability criterion implies a comparison between a Member State's average price performance and a reference value.

A Member State's **average rate of inflation** is measured by the percentage change in the unweighted average of the last 12 monthly indices relative to the unweighted average of the 12 monthly indices of the previous period, rounded to one decimal. This measure captures inflation trends over a period of one year as requested by the provisions of the Treaty. Using the commonly used inflation rate – calculated as the percentage change in the consumer price index of the latest month over the index for the equivalent month of the previous year – would not meet the one-year requirement. The latter may also be excessively volatile from month to month and excessively affected by temporary factors.

The **reference value** is calculated as the unweighted average of the average rates of inflation of, at most, the three best-performing Member States in terms of price stability plus 1.5 percentage points. The outcome is rounded to one decimal. While in principle the reference value could also be calculated on the basis of the price performance of only one or two best performing Member States in terms of price stability, it has been existing practice to select the three best performers. Defining the reference value in a relative way (as opposed to a fixed reference value) allows taking into account the effects of a common shock that affects inflation rates across all Member States.

Table 1:
Inflation reference value in previous and current convergence reports

Convergence Report adoption date	Cut-off month	Three best performers [1) 2)]	Reference value [3)]	Euro area average inflation rate [4)]
1998	January 1998	Austria, France, Ireland	2.7	1.5
2000	March 2000	Sweden, France, Austria	2.4	1.4
2002	April 2002	United Kingdom, France, Luxembourg [5)]	3.3	2.4
2004	August 2004	Finland, Denmark, Sweden	2.4	2.1
2006 May	March 2006	Sweden, Finland, Poland	2.6	2.3
2006 December	October 2006	Poland, Finland, Sweden	2.8	2.2
2007	March 2007	Finland, Poland, Sweden	3.0	2.1
2008	March 2008	Malta, Netherlands, Denmark	3.2	2.5
2010	March 2010	Portugal, Estonia, Belgium	1.0	0.3
2012	March 2012	Sweden, Ireland, Slovenia	3.1	2.8
2013	April 2013	Sweden, Latvia, Ireland	2.7	2.2
2014	April 2014	Latvia, Portugal, Ireland	1.7	1.0
2016	April 2016	Bulgaria, Slovenia, Spain	0.7	0.1
2018	March 2018	Cyprus, Ireland, Finland	1.9	1.4
2020	March 2020	Portugal, Cyprus, Italy	1.8	1.1
2022	April 2022	France, Finland, Greece	4.9	4.4
2024	May 2024	Netherlands, Italy, Latvia	4.1	3.4
2025	April 2025	Ireland, Finland, Italy	2.8	2.3

1) EU15 until April 2004; EU25 between May 2004 and December 2006; EU27 between January 2007 and June 2013; EU28 between July 2013 and January 2020; EU27 (without UK) from February 2020 onwards.
2) In case of equal rounded average inflation for several potential best performers, the ranking is determined on the basis of unrounded data.
3) Reference values are only computed at the time of Convergence Reports. All calculations of the reference value between the Convergence Reports are purely illustrative.
4) Measured by the percentage change in the arthmetic average of the latest 12 monthly indices relative to the arithmetic average of the 12 monthly indices of the previous period.
5) Based on revised data, Germany would replace Luxembourg as one of the three Member States with the lowest 12-month average inflation in April 2002. This change would not affect the price and long-term interest rate reference values in April 2002.
Sources: Eurostat and European Commission calculations.

As Article 140(1) of the Treaty refers to 'Member States' and does not make a distinction between euro area and other Member States, the convergence reports select the three best performers from all Member States – EU-15 for the convergence reports before 2004, EU-25 for the reports between 2004

(Continued on the next page)

Box (continued)

and 2006, EU-27 for reports between 2007 and 2013, EU-28 for reports between 2014 and 2018 and EU-27 for the reports between 2020 and 2024.

The notion of '**best performer in terms of price stability**' is not defined explicitly in the Treaty. It is appropriate to interpret this notion in a non-mechanical manner, taking into account the state of the economic environment and country-specific factors at the time of the assessment. In particular, an outlier analysis should be performed to identify those countries whose inflation rates cannot be seen as meaningful benchmarks. These outliers are identified on the basis of two criteria taken in combination: i) an inflation rate substantially below the euro area average; and ii) an inflation rate driven by country-specific factors that cannot be seen as representative of the process that is driving inflation in the euro area. In this convergence report, no Member States were identified as outliers in terms of inflation performance for the calculation of the reference value, as none of their inflation rates deviated by a wide margin from the euro area average due to country-specific circumstances ([1]).

([1]) For more details on past outlier analyses, see Box 1.2 on page 29 of the European Commission's 2024 Convergence Report (https://economy-finance.ec.europa.eu/publications/convergence-report-2024_en).

As has been the case in past convergence reports, a Member State's average rate of inflation is measured by the percentage change in the arithmetic average of the last 12 monthly indices relative to the arithmetic average of the 12 monthly indices of the previous period. The reference value is calculated as the arithmetic average of the average rate of inflation of the three 'best-performing EU Member States in terms of price stability' plus 1.5 percentage points (see Box 1.2).

Accordingly, the reference value is currently 2.8%, based on the data of Ireland (1.2%), Finland (1.3%) and Italy (1.4%) over the 12-month period covering May 2024 – April 2025. No Member States were identified as outliers in terms of inflation performance for the calculation of the reference value, as none of their inflation rates deviated by a wide margin from the euro area average due to country-specific circumstances (see Box 1.2).

The Protocol on the convergence criteria not only requires Member States to have achieved a high degree of price stability but also calls for a price performance that is sustainable. The requirement of sustainability aims at ensuring that the degree of price stability and inflation convergence achieved in previous years will be maintained after adoption of the euro. This deserves particular attention as sustained divergences in price developments in one or more euro area Member States can lead to the emergence of competitiveness losses that must be corrected via painful adjustment processes and can trigger negative spillover effects on other Member States.

Inflation sustainability implies that the satisfactory inflation performance must essentially be due to the adequate behaviour of input costs and other factors that influence price developments in a structural manner, rather than reflecting the influence of cyclical or temporary factors. Therefore, this Technical Annex also takes account of the role of the macroeconomic situation and cyclical position in the inflation performance, of developments in unit labour costs as a result of trends in labour productivity and nominal compensation per head, and of developments in import prices to assess how external price developments have impacted on domestic inflation. Similarly, the impact of administered prices and indirect taxes on headline inflation is also considered.

From a forward-looking perspective, the report includes an assessment of medium-term prospects for price developments. The analysis of factors that have an impact on the inflation outlook is complemented by the projections from the most recent Commission inflation forecast. Medium-term inflation prospects are also assessed by reference to the economies' key structural characteristics, including the functioning of the labour and product markets.

1.2.3. Public finances

The convergence criterion dealing with the government budgetary position is defined in the second indent of Article 140(1) of the Treaty as 'the sustainability of the government financial position; this will be apparent from having achieved a government budgetary position without a deficit that is excessive as determined in accordance with Article 126(6)'. Furthermore, Article 2 of the Protocol on the convergence criteria states that this criterion means that 'at the time of the examination the Member State is not the subject of a Council decision under Article 126(6) of the said Treaty that an excessive deficit exists'.

The convergence assessment in the budgetary area is thus directly linked to the excessive deficit procedure which is specified in Article 126 of the Treaty and further clarified in the Stability and Growth Pact (see Box 1.3 for further information on the excessive deficit procedure as strengthened by the 2024 reform of the Stability and Growth Pact). The details of the excessive deficit procedure are defined in Regulation 1467/97 as amended in 2024 which sets out the way in which government deficit and debt levels are assessed to determine whether an excessive deficit exists, under Article 126 of TFEU. The convergence assessment of the budgetary position is therefore judged by whether the Member State is subject to a Council decision under 126(6) on the existence of an excessive deficit ([14]).

On 4 June 2025, the Commission adopted a report under Article 126(3) of the TFEU for 4 Member States. The report did not cover Bulgaria, as its government deficit in 2024 did not exceed 3.0% of GDP.

In the context of the European Semester, the country-specific recommendations for 2025 invite Member States to reinforce overall defence spending and readiness in line with the European Council conclusions of 6 March 2025. Member States are called to adhere to the maximum growth rates of net expenditure recommended by the Council, while - where relevant - making use of the allowance under the national escape clause for higher defence expenditure.

([14]) The definitions of the government deficit and debt used in this report are in accordance with the excessive deficit procedure, as was the case in previous convergence reports. These definitions are laid out in the amended Council Regulation (EC) No 479/2009. In particular, government debt is general government consolidated gross debt at nominal value. Information regarding the excessive deficit procedure and its application to different Member States since 2002 can be found at: http://ec.europa.eu/economy_finance/economic_governance/sgp/deficit/index_en.htm.

Box 1.3: **Excessive Deficit Procedures under the new EU fiscal framework**

The new EU fiscal framework was adopted on 29 April 2024. The rules on the opening of a deficit-based Excessive Deficit Procedure (EDP) remain unchanged while the rules on the opening of a debt-based EDP are changed and clarified in the amended Council Regulation (EC) 1467/97. ([1])

In order to simplify the EU fiscal framework and increase transparency, a single operational indicator (net expenditure) anchored in debt sustainability serves as a basis for setting the fiscal path and for carrying out annual fiscal surveillance. Net expenditure means government expenditure net of interest expenditure, discretionary revenue measures, expenditure on Union programmes fully matched by revenue from Union funds, national expenditure on co-financing of programmes funded by the Union, as well as cyclical elements of unemployment benefit expenditure. One-offs and other temporary measures will also be excluded from the net expenditure indicator.

The EDP is specified in Article 126 of the Treaty on the Functioning of the European Union (TFEU). Protocol 12 of the Treaty gives further details on the excessive deficit procedure, including the reference values on deficit and debt. Council Regulation (EC) 1467/97 on speeding up and clarifying the implementation of the EDP (the corrective arm of the Stability and Growth Pact) clarifies the implementation of the excessive deficit procedure. Together, these provisions determine the steps to be followed to reach a Council decision on the existence and correction of an excessive deficit.

The Commission will produce reports under Article 126(3) of TFEU on the basis of the following criteria:

- whether the ratio of the planned or actual government deficit to gross domestic product exceeds 3% of GDP, unless:
  - the ratio has declined substantially and continuously and reached a level that comes close to the reference value;
  - or, alternatively, the excess over the reference value is exceptional and temporary and the ratio remains close to the reference value;
- when the ratio of the government debt to GDP exceeds 60% of GDP, the budgetary position is not close to balance ([2]) or in surplus and when the deviations recorded in the control account ([3]) of the Member State exceed the established annual or cumulative thresholds (0.3% and 0.6% of GDP respectively).

When assessing the existence of an excessive deficit in accordance with Article 126(3) TFEU, the Commission should take into account all relevant factors. Substantial public debt challenges in the Member State concerned should be considered a key aggravating factor. The increase of government investment in defence, where applicable, should be considered as a relevant factor when assessing the existence of an excessive deficit. The Commission shall give due and express consideration to any other factors which, in the opinion of the Member State concerned, are relevant in order to comprehensively assess compliance with the deficit and debt criteria and which the Member State has put forward to the Council and the Commission. In that context, particular consideration shall be given to financial contributions to fostering international solidarity and achieving the common priorities of the Union

([1]) OJ L, 2024/1264, 30.4.2024, Council Regulation (EU) 2024/1264 of 29 April 2024 amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure (europa.eu). The consolidated version of Regulation No 1467/97 can be found at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A01997R1467-20240430.

([2]) The budgetary position shall be considered close to balance if the general government deficit does not exceed 0.5 % of GDP.

([3]) The Commission will set up a control account for each Member State to keep track of annual and cumulative upward and downward deviations of the net expenditure observed from the net expenditure path as set by the Council pursuant to the new preventive arm Regulation (see footnote 5).

(Continued on the next page)

Box (continued)

referred to in the new preventive arm Regulation. ([4]) For deficit-based EDPs, the relevant factors can be considered for i) those Member States with debt below 60% and ii) those Member States with debt exceeding 60% of GDP and satisfying the double condition of the overarching principle, i.e. that the general government deficit remains close to the 3% of GDP reference value and its excess over the reference value is temporary.

In the next step of the procedure, the Economic and Financial Committee (EFC) should formulate an opinion in accordance with Article 126(4) TFEU within two weeks of the adoption by the Commission of a report issued in accordance with Article 126(3) TFEU. Taking fully into account this opinion, the Commission, if it considers that an excessive deficit exists, should address an opinion and a proposal to the Council in accordance with Article 126(5) and (6) TFEU and inform the European Parliament thereof. The Council should then decide on the existence of an excessive deficit in accordance with Article 126(6) TFEU, as a rule within four months of the reporting dates established in Article 3(2) and (3) of Regulation (EC) No 479/2009. When it decides that an excessive deficit exists, the Council should at the same time make recommendations to the Member State concerned in accordance with Article 126(7) TFEU.

In its recommendation, the Council shall request that the Member State implements a corrective net expenditure path which ensures that the general government deficit remains or is brought and maintained below the reference value within the deadline set in the recommendation. The corrective path should also ensure that the debt is kept on a plausibly downward path or remains at prudent levels below 60% of GDP in the medium term. In the case of a debt-based EDP, the corrective net expenditure path shall be at least as demanding as the net expenditure path under the preventive arm from which the Member State deviated and correct as a rule the cumulated deviations of the control account.([5])

([4]) OJ L 1263, 30.4.2024, Regulation (EU) 2024/1263 of the European Parliament and of the Council of 29 April 2024 on the effective coordination of economic policies and on multilateral budgetary surveillance and repealing Council Regulation (EC) No 1466/97 (europa.eu).

([5]) OJ L 1264, 30.4.2024. Council Regulation (EU) 2024/1264 amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure.

1.2.4. Exchange rate stability

The Treaty refers to the exchange rate criterion in the third indent of Article 140(1) as 'the observance of the normal fluctuation margins provided for by the exchange-rate mechanism of the European Monetary System, for at least 2 years, without devaluing against the euro'.

Article 3 of the Protocol on the convergence criteria stipulates: 'The criterion on participation in the exchange rate mechanism of the European Monetary System [...] shall mean that a Member State has respected the normal fluctuation margins provided for by the exchange-rate mechanism of the European Monetary System without severe tensions for at least the last 2 years before the examination. In particular, the Member State shall not have devalued its currency's bilateral central rate against the euro on its own initiative for the same period' ([15]). Based on the Council Resolution on the establishment of the ERM II ([16]), the European Monetary System has been replaced by the Exchange Rate Mechanism II upon the introduction of the euro, and the euro has become the centre of the mechanism.

([15]) In assessing compliance with the exchange rate criterion, the Commission examines whether the exchange rate has remained close to the ERM II central rate, while reasons for an appreciation may be taken into account, in accordance with the Common Statement on Acceding Countries and ERM II by the Informal ECOFIN Council, Athens, 5 April 2003.

([16]) 97/C 236/03 of 16 June 1997, OJ C 236, 2.8.1997, p.5.

Box 1.4: **A reinforced approach to ERM II participation by means of upfront policy commitments by the applicant Member States**

Participating in ERM II is an essential step for a Member State with a derogation on the way to fulfil the exchange rate criterion and to euro adoption. Fulfilling the exchange rate criterion through the smooth participation in ERM II is provided for in Article 140 of the TFEU, Protocol No 13 to the TFEU on the convergence criteria and the Resolution of the European Council on the establishment of an exchange-rate mechanism in the third stage of economic and monetary union adopted in Amsterdam on 16 June 1997 ([1]). In accordance with this framework, ERM II entry of a Member State with a derogation requires a mutual agreement of all 'ERM II parties'. These include the finance ministers of euro area Member States, the European Central Bank, and the finance ministers and the central bank governors of the non-euro area Member States participating in ERM II. The European Commission provides analytical support to the ERM II process, but has no voting right and no right of initiative in the ERM II entry process.

In July 2018, learning from past episodes of economic overheating in ERM II and the euro-area crisis, the ERM II parties clarified the modalities of a reinforced approach for future ERM II participation with a view of ensuring a smooth transition to, and participation in, ERM II, in their statement on Bulgaria's path towards ERM II, stating that this approach would apply to all Member States wishing to join ERM II from then onwards ([2]). The reinforced approach was confirmed in the later statement of the ERM II parties of July 2019 on Croatia's path towards ERM II participation ([3]).

According to this reinforced approach, the applicant Member State and ERM II parties agree on a number of policy commitments to be implemented by the former before joining ERM II. This package of so called prior policy commitments aims at maximising the country's chances to operate smoothly in ERM II. It is country-specific, targeted and covers policy areas that are highly relevant for a smooth transition to and participation in ERM II including, for instance institutional quality, governance, the financial sector, fiscal policy, or the business environment.

In particular, as being part of the euro area now also implies for a Member State to be part of the Banking Union's pillars of the Single Supervisory Mechanism (SSM) and the Single Resolution Mechanism (SRM), the applicant Member State is expected to enter into 'close cooperation' with the ECB for banking supervision purposes at the latest by the time of its participation in ERM II. A Member State with a derogation can join the Banking Union before its euro adoption via an arrangement called 'close cooperation'. Entering in close cooperation with the ECB means that the significant credit institutions established in the country concerned are supervised by the ECB via the involvement of the domestic national supervisor. Entering in close cooperation also implies participation in the Single Resolution Mechanism, including the Single Resolution Fund.

In terms of process, the ECB and the Commission monitor the fulfilment of the prior-commitments undertaken by the applicant Member States in the respective areas of competence of the ECB and the Union and in close cooperation with the Member State concerned. The two institutions regularly inform ERM II parties on the progress made with the prior-commitments. A comprehensive assessment of the applicants' banking sector is carried out by the ECB as part of the process of establishing close cooperation with the ECB. This includes an asset quality review and a stress test that aims at assessing whether banks are fundamentally sound. The results of the comprehensive assessment are made public on the ECB's website ([4]).

([1]) https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A31997Y0802%2803%29
([2]) See: https://www.consilium.europa.eu/en/press/press-releases/2018/07/12/statement-on-bulgaria-s-path-towards-erm-ii-participation/
([3]) See: https://www.consilium.europa.eu/en/press/press-releases/2019/07/08/statement-on-croatia-s-path-towards-erm-ii-participation/
([4]) The results of the comprehensive assessment of six Bulgarian banks are available at: https://www.bankingsupervision.europa.eu/press/pr/date/2019/html/ssm.pr190726~1b474e3467.en.html

(Continued on the next page)

Box (continued)

In line with the long-standing ERM II practice, ERM II parties also expect applicant Member States to take further policy commitments at the moment of joining ERM II with the aim of achieving a high degree of sustainable economic convergence by the time the euro will be adopted.

At the time of writing this report, Bulgaria and Denmark were the only non-euro-area Member States participating in ERM II. Bulgaria joined the ERM II on 10 July 2020 after having completed its prior policy commitments ([5]). Bulgaria established close cooperation with the ECB. In addition, the prior policy commitments of the Bulgarian authorities covered measures related to the macroprudential framework, the supervision of the non-banking financial sector, the insolvency framework, the anti-money laundering framework and the governance of state-owned enterprises ([6]).

At the time of ERM II entry, the Bulgarian authorities also committed to pursue sound economic policies with the aim of preserving economic and financial stability and achieving a high degree of sustainable economic convergence. In particular, the Bulgarian authorities committed to implement specific policy measures (the so-called post-ERM II entry commitments) on the non-banking financial sector, state-owned enterprises, the insolvency framework and the anti-money laundering framework ([7]).

([5]) For the details on the decision of the ERM II parties on Bulgaria see: https://ec.europa.eu/commission/presscorner/detail/en/IP_20_1321
([6]) For more details on the prior-commitments taken by Bulgarian authorities see: https://www.consilium.europa.eu/media/36125/st11119-en18.pdf
([7]) See: https://www.ecb.europa.eu/pub/pdf/annex/ecb.pr200710_annex~29156bba37.en.pdf

In its assessment of the exchange rate stability criterion, the Commission takes into account developments in auxiliary indicators such as foreign reserve developments and short-term interest rates, as well as the role of policy measures, including foreign exchange interventions, and international financial assistance wherever relevant, in maintaining exchange rate stability.

The assessment of this criterion verifies the participation in ERM II (see Box 1.4 for further information on ERM II participation) and examines exchange rate behaviour within the mechanism. The relevant period for assessing exchange rate stability in this Technical Annex is 20 May 2023 to 19 May 2025.

1.2.5. Long-term interest rates

The fourth indent of Article 140(1) of the Treaty requires that 'the durability of convergence achieved by the Member State with a derogation and of its participation in the exchange rate mechanism' is 'reflected in the long-term interest rate levels'. Article 4 of the Protocol on the convergence criteria further stipulates that 'the criterion on the convergence of interest rates [...] shall mean that, observed over a period of one year before the examination, a Member State has had an average nominal long-term interest rate that does not exceed by more than 2 percentage points that of, at most, the three best performing Member States in terms of price stability. Interest rates shall be measured on the basis of long-term government bonds or comparable securities, taking into account differences in national definitions' (see Box 1.5).

Box 1.5: **Data for the interest rate convergence**

The fourth indent of Article 140(l) of the Treaty requires that the durability of nominal convergence and exchange rate stability in Member States should be assessed by reference to long-term interest rates. Article 4 of the Protocol on the convergence criteria adds that these '*Interest rates shall be measured on the basis of long-term government bonds or comparable securities, taking into account differences in national definitions*'.

Article 5 of the Protocol requires that the Commission should provide the statistical data used for the application of the convergence criteria. However, in the context of the interest rate criterion, the ECB has developed the criteria for harmonising the series of 10-year benchmark bond yields on behalf of Eurostat and collects the data from the central banks. The selection of bonds for inclusion in this series is based on the following criteria:

- issued by a central government;
- a residual maturity as close as possible to 10 years;
- adequate liquidity, which is the main selection criterion; the choice between a single benchmark or the simple average of a sample is based on this requirement;
- fixed coupon;
- yield gross of tax.

For fifteen Member States, the residual maturity of the benchmark bond is at least 9.5 years. For twelve Member States, the residual maturity of the benchmark bond is below 9.5 years, in particular for Bulgaria with the residual maturity slightly above 6.55 years. All yields are calculated on the basis of secondary market rates, where available. For Czechia, Germany, Malta and Spain a basket of bonds is used, while a single benchmark bond is used in twenty-three Member States.

Data used in this Report can be found on Eurostat ("Maastricht criterion bond yields (mcby): EMU convergence criterion bond yields", code: tec00097). The same series is also published by the ECB's Statistical Data Warehouse (code IRS.M.*Country Code*.L.L40.CI.0000.*Currency Code*.N.Z) and in a dedicated page in the ECB website with additional information:
http://www.ecb.europa.eu/stats/financial_markets_and_interest_rates/long_term_interest_rates/html/index.en.html.

For the assessment of the criterion on the convergence of interest rates, yields on benchmark long-term bonds have been taken, using an average rate over the latest 12 months. The reference value for April 2025 is calculated as the simple average of the average long-term interest rates in Ireland (2.8%), Finland (2.9%) and Italy (3.7%) plus 2 percentage points, yielding a reference value of 5.1%.

1.2.6. Additional factors

Article 140(1) TFEU also requires that the reports take into account other factors relevant to economic integration and convergence. These additional factors include financial, product and labour market integration and the development of the balance of payments. The analysis of the development of unit labour costs and other price indices, which is also prescribed by Article 140 of the Treaty, is covered in the price stability section.

The assessment of additional factors gives an important indication of a Member State's ability to integrate into the euro area without difficulties. As regards the balance of payments, the focus is on the situation and development of the external balance ([17]). Market integration is assessed

([17]) The external balance is defined as the combined current and capital account (net lending/borrowing vis-à-vis the rest of the world). This concept permits in particular to take full account of external transfers (including EU transfers), which are partly recorded in the capital account. It is the concept closest to the current account as defined when the Maastricht Treaty was drafted.

through trade, foreign direct investment and a smooth functioning of the internal market. Moreover, progress in financial integration is examined, together with the main characteristics, structures and trends of the financial sector. Given that Member States which adopt the euro also participate in the banking union, developments in national banking sectors are specifically looked at as well.

Starting with the 2012 Convergence Report, the convergence assessment is aligned with the broader European Semester approach which takes an integrated look at the economic policy challenges facing EMU in ensuring fiscal sustainability, competitiveness, financial market stability and economic growth.

The section on additional factors makes reference to the surveillance of macroeconomic imbalances under the Macroeconomic Imbalance Procedure ([18]).

([18]) The key elements of the Macroeconomic Imbalance Procedure are described in Box 1.7 of the European Commission's 2024 Convergence Report.

2. BULGARIA

2.1. LEGAL COMPATIBILITY

2.1.1. Introduction

The legal basis for the Bulgarska Narodna Banka (the BNB – Bulgaria's central bank), the Law on the Bulgarian National Bank (the BNB Law) of 2024 ([19]), has been amended since the 2024 Convergence Report by the Law on the State Budget of the Republic of Bulgaria for 2025 (Law on State Budget) ([20]). The Bulgarian authorities have amended the BNB Law to remedy the incompatibility highlighted in the Commission's 2024 Convergence Report. In particular, this concerns issues flagged in the section on central bank independence in relation to Article 99(5) of the Bulgarian Constitution ([21]). In accordance with paragraph 14 of its transitional and final provisions, the BNB Law shall enter into force on the date specified in the Council Decision on the adoption of the euro by Bulgaria. The entry into force would therefore be automatic and would not require further action from the Bulgarian authorities. The BNB Law will replace and repeal the previous BNB Law ([22]). Once it enters into force, the BNB Law is compatible with the relevant provisions of the EU law.

2.1.2. Central bank independence

Article 15(3) of the BNB Law provides that the grounds for the early dismissal of a member of the Governing Council, with the exception of the Governor, shall be established by a decision of the Governing Council. A member of the Governing Council whose dismissal is proposed shall cease to exercise their powers from the day of the Governing Council's decision. The Governing Council's decision is subject to appeal before the Supreme Administrative Court within 7 days. The Supreme Administrative Court gives its decision within 14 days of receipt of the appeal. This decision is final. Ensuring personal independence requires that national legislation should allow reasonable time for appealing a dismissal decision as well as for the judicial review to take place for appealing. The short time-limit for the appeal and the very constrained timeframe for the judicial procedure in Article 15(3) may be seen as a residual imperfection that Bulgaria should consider addressing in the near future.

The Bulgarian Constitution has been amended in January 2024 in a matter that could indirectly impact the BNB's independence. The new Article 99(5) of the Bulgarian Constitution provides that, in a case where no agreement is reached on the formation of a government, the President, following consultations with the parliamentary groups and acting on a motion by the caretaker prime minister-designate, appoints a caretaker cabinet, and schedules new elections within 2 months. A caretaker prime minister is to be appointed from among the Chairperson of the National Assembly, the Governor or a Deputy Governor of the BNB, the President or a Vice-President of the Bulgarian National Audit Office, and the Ombudsman (or a deputy thereof).

The appointment as caretaker prime minister of the Governor or one of the Deputy Governors of the BNB could disrupt its effective and independent functioning. This would be potentially a serious cause for concern. The appointment would only be for a limited period (until a regular government is formed), but the caretaker government could be reappointed for several successive periods as long as election results do not result in the formation of a government and new elections have to be scheduled. To avoid such potential disruption and its possible impact on the BNB's independence, one possible solution stated in the Commission Convergence Report 2024 was the

([19]) Law on Българска народна банка (Bulgarian National Bank), Darjaven vestnik issue 13, 13.2.2024.

([20]) Law on the State Budget of the Republic of Bulgaria for 2025, Decree No. 53, 21.3.2025, Darjaven vestnik issue 26, 27.3.2025.

([21]) Constitution of the Republic of Bulgaria, Darjaven vestnik issue 56, 13.7.1991.

([22]) Law on Българска народна банка (Bulgarian National Bank), Darjaven vestnik issue 46, 10.6.1997.

amendment of the BNB Law to provide sufficient and effective safeguards for the BNB's independence as required by EU law. Firstly, any appointment of the Governor or a Deputy Governor of the BNB as a caretaker prime minister should be conditional on their explicit consent and they should be empowered to refuse such an appointment. Secondly, if such consent is expressed, the rules should prevent that person from holding both positions simultaneously, because this could lead to conflicts of interest and lack of independence. In this respect, the effective and independent functioning of the BNB must be preserved. This could be ensured through the person's resignation from their post at the BNB at the time of their appointment as caretaker prime minister.

Article 13 of the BNB Law has been amended by paragraph 32 of the Transitional and Final provisions of the Law on the State Budget, published on 27 March 2025, and a new paragraph (5) has been added, stating that in the event that the Governor or Deputy Governor has expressed the explicit consent to be appointed as caretaker prime minister (Acting Prime Minister) under the procedure of Article 99, paragraph 5 of the Constitution of the Republic of Bulgaria, he/she shall resign. The Governor or Deputy Governor has the right to refuse to be appointed as caretaker prime minister (Acting Prime Minister) under the procedure of Article 99, paragraph 5 of the Constitution of the Republic of Bulgaria. The Commission also welcomes the amendments made to paragraph (4) of Article 13 according to which, in the event of the appointment of the Governor or Deputy Governor as caretaker prime minister (Acting Prime Minister) under the procedure of Art. 99, para. 5 of the Constitution of the Republic of Bulgaria, the appointment of a new Governor, respectively Deputy Governor, shall be held no later than one month from the termination of the powers under the procedure of paragraph 8 of the BNB Law. Until the appointment, the powers of the Governor shall be exercised by a deputy designated by him from among the Deputy Governors, and for a Deputy Governor, Art. 20, paragraph 4 of the BNB Law shall apply. This procedure ensures the continuity of central bank's activities in case of appointment of the Governor or Deputy Governor as caretaker prime minister (Acting Prime Minister).

Therefore, the incompatibility mentioned in the Commission's Convergence Report 2024 in this area has been resolved.

2.1.3. Prohibition of monetary financing and privileged access

There are no incompatibilities and imperfections in the BNB Law with regard to the prohibition of monetary financing and privileged access, as enshrined in Article 123 and 124 of the TFEU.

2.1.4. Integration into the ESCB

Objectives

The objectives of the BNB are compatible with the TFEU.

Tasks

There are no incompatibilities and imperfections in the BNB Law with regard to the tasks of the ESCB and the ECB.

2.1.5. Assessment of compatibility

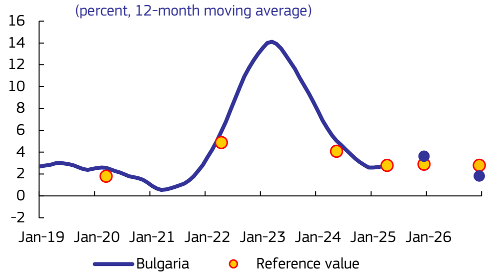
The Bulgarian authorities have taken measures to remedy the incompatibility that was identified in the 2024 Convergence Report. The BNB Law is compatible with Article 130 and Article 131 of the TFEU and the ESCB/ECB Statute.

2.2. PRICE STABILITY

2.2.1. Respect of the reference value

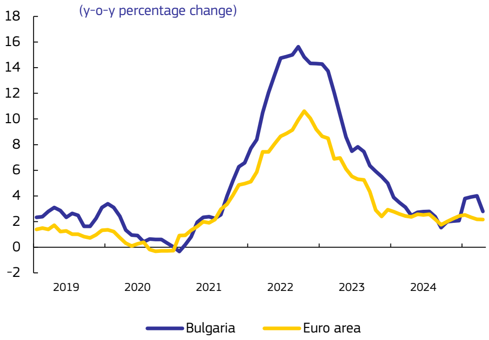
The 12-month average inflation rate, which is used for the convergence assessment, was above the reference value at the time of the last convergence assessment of Bulgaria in 2024. The 12-month average inflation rate decreased gradually from a high of 14.1% in March 2023 to 2.6% in December 2024. In April 2025, the reference value was 2.8%, calculated as the average of the 12-month average inflation rates in Ireland, Finland and Italy plus 1.5 percentage points. The corresponding inflation rate in Bulgaria was 2.7%, below the reference value. The 12-month average inflation rate in Bulgaria is projected to increase above the projected reference value by the end of 2025, fall back to the reference value in the first months of 2026 and stay below it for the rest of 2026 ([23]). A review of a broad range of indicators does not identify causes for concern regarding the sustainability of price stability.

Graph 2.1: **Bulgaria - Inflation criterion**
(percent, 12-month moving average)



Note: The dots at the right end of the chart show the projected reference value and 12-month average inflation rate of Bulgaria in December 2025 and December 2026. The reference values for 2020, 2022 and 2024 refer to the reference values calculated in the previous convergence reports.
Source: Eurostat, Commission's Spring 2025 Economic Forecast.

Graph 2.2: **Bulgaria - HICP inflation**
(y-o-y percentage change)



Source: Eurostat.

2.2.2. Recent inflation developments

The annual HICP inflation rate started to decline from 14.3% in January 2023 and flattened around 2.8% in May-July 2024 before declining further to 2.1% in October-December 2024. It then rose sharply at the beginning of 2025, peaking at 4% in March, before decreasing to 2.8% in April 2025. At the beginning of 2023, headline HICP inflation was still above HICP inflation excluding energy and food (core inflation), due to higher energy and food price inflation. With the rapid disinflation of fuel and gas prices in 2023, overall inflation remained below core inflation in the rest of 2023. In 2024, headline HICP inflation and core inflation remained close to each other, as the fall in fuel prices in the second half of 2024 was largely offset by somewhat higher food price inflation. The sharp price hikes at the beginning of 2025 concerned items both within and outside the core inflation basket. These price hikes were largely due to restored higher VAT rates for bread and restaurants, higher excise duties for tobacco, increased electricity and gas prices for households, other utilities and administered prices, and higher food prices due to increased international food prices. The drop in April 2025 of the annual HICP inflation rate was largely due to a substantial reduction in hospital fees. Decreases in other administered prices and in gas and fuel prices also contributed to the drop. Inflation in Bulgaria has been reconverging with that of the euro area over the past 2 years. The average annual inflation rate in Bulgaria was 8.6% in 2023, 3.2 percentage points above the euro area. It then declined to 2.6% in 2024, narrowing the gap to 0.2 percentage point.

HICP inflation excluding energy and food declined from 11.1% in January 2023 to 3% in the May-August 2024 period, decelerated further to 2.5% in December 2024. It then increased to 3.8% in

([23]) The Commission's Spring 2025 Economic Forecast does not include the impact of lower fees for hospital services and of decreases in other administered prices on inflation in April 2025. When taking into account these measures, the average inflation rate in Bulgaria would likely be close to the reference value by the end of 2025.

March 2025, before declining to 2.3% in April 2025. In 2023, services price inflation remained on average 1 percentage point above non-energy industrial goods inflation while both components were on a declining path. Services inflation reached 3% in April 2024. It then increased, mainly due to tourism and transport services, and stabilised around 5% in the second half of 2024. Since mid-2024, annual inflation in prices of packaged international holidays picked up to around 15%, as VAT rates were restored. Apart from these items, services inflation in 2024 was driven by price increases in catering and accommodation services. Services inflation then rose to 7.2% in March 2025 and then fell to 3.5% in April 2025. Higher administrative and other fees, prices in restaurants, and prices of communication services accounted for around 1.5 percentage points of the acceleration in services price inflation between December 2024 and March 2025. In April, hospital fees were reduced from 5,8 BGN to 1 BGN, that led to 2.9 percentage points decline in annual services inflation. Other administered prices also contributed negatively to services inflation in April 2025. Annual inflation in non-energy industrial goods prices continued to abate throughout 2024, and remained around zero in the September 2024 – March 2025 period, benefiting from low inflation in imported goods. Inflation in non-energy industrial goods then increased to 0.9% in April 2025 due to a base effect from the decision to reduce co-payments for certain medicines from April 2024.

Table 2.1:
Bulgaria - Components of inflation

	(percentage change)[1]							weights in total
	2019	**2020**	**2021**	**2022**	**2023**	**2024**	**Apr-25**	**2025**
HICP	2.5	1.2	2.8	13.0	8.6	2.6	2.7	1000
Non-energy industrial goods	0.2	-0.1	0.7	7.1	8.5	1.3	0.5	306
Energy	1.4	-6.1	10.6	26.8	-1.3	-1.4	-1.0	108
Unprocessed food	5.3	5.5	-0.3	20.0	15.5	3.4	3.4	50
Processed food	4.0	4.1	2.9	17.2	12.0	3.3	4.0	227
Services	3.2	2.3	2.0	8.2	9.4	4.8	5.4	309
HICP excl. energy, food, alcohol and tobacco	1.8	1.2	1.4	7.6	8.9	3.1	3.0	615
HICP at constant tax rates	2.4	1.5	3.2	13.3	8.7	2.3	2.3	1000
Administered prices HICP	2.6	1.7	2.4	6.2	6.9	4.4	4.3	148

1) Measured by the arithmetic average of the latest 12-monthly indices relative to the arithmetic average of the 12-monthly indices in the previous period.
Source: Eurostat, European Commission calculations.

2.2.3. Underlying factors and sustainability of inflation

Macroeconomic policy mix and growth developments

Economic growth accelerated from 1.9% in 2023 to 2.8% in 2024, driven by private consumption. In a context of a tight labour market and falling inflation, real wages continued to expand in 2024. The continued growth in aggregate employment, as well as increased social transfers underpinned strong nominal income expansion in 2023 and 2024. Combined with abating inflation, this led to robust growth in real disposable income, which fuelled private consumption. The strong growth in consumer credit also supported private consumption in 2023 and 2024.

Goods exports contracted in 2023, due to the decline in external demand, the strong negative base effect from 2022 and some one-off factors ([24]). In 2024, exports of goods and services contracted both in nominal and in real terms, while the terms of trade deteriorated. The decline in exports was broad-based in terms of product categories, with somewhat deeper decline in cereals due to weak harvest, but more concentrated geographically with sharp declines in a few destination countries. The Russian war of aggression against Ukraine and the economic difficulties in other countries have weighed on goods export.

Services exports expanded robustly in 2023, benefiting from the continued recovery in the tourism sector and the expansion of services outsourced to Bulgaria. While these positive trends continued

([24]) Notably planned maintenance in the steel industry and the nuclear power plant and the ban on exports of petroleum products processed from Russian oil.

in 2024, the volume of international transport services temporarily declined. Overall, in 2024 services exports contracted by 0.6% in real terms.

Investment held up well in 2023, increasing by 10.2% with an important contribution from public sector investment and purchases of new equipment. In 2024, investment declined by 1.1% due to lower public spending and roughly constant private sector borrowing. The accumulation of inventories turned sharply negative in 2023. Firms accumulated more inventories in the form of unfinished production and final goods in 2024, in parallel with the increase in imports and decline in finished construction.

In 2023, imports contracted sharply, following the decline in exports and inventories and then expanded in 2024, reflecting the buoyant private consumption growth.

Real GDP growth is forecast to slow down to 2% in 2025 and 2.1% in 2026 due to both external and domestic factors. Private consumption is set to grow more moderately, as lower real disposable income growth and precautionary savings constrain purchases by households. The outlook for exports has also been revised downwards but is expected to accelerate moderately in 2026. In addition to subdued external demand, exports of goods in 2025 are affected by planned maintenance works in the steel production and oil refining industries. Private investment is projected to contract in 2025 and 2026 due to the heightened economic uncertainty. The assumed acceleration in EU funds absorption is expected to support moderate investment growth that accelerates in 2026. Wage moderation in the private sector is expected to continue, accompanied by limited job losses, related to the worsened economic environment and the need to preserve competitiveness and profitability among firms. Public sector wages are projected to grow strongly in 2025, amid strong hiring in both years.

Bulgaria's fiscal stance ([25]) is estimated to have been broadly neutral in 2024 and, based on the Commission's Spring 2025 Economic Forecast, the stance is expected to become supportive in 2025 (-1.1 of GDP). It is projected to turn contractionary in 2026 (0.8% of GDP).

The BNB pursues its primary objective of price stability through an exchange rate anchor in the context of the currency board with the lev pegged to the euro. The currency board serves as a key macroeconomic policy anchor. The monetary tightening in the euro area has affected the non-financial corporations lending segment of the Bulgarian banking sector by increased interest rates, but the pass-through to the mortgage lending segment has been rather muted. Country-specific factors in the setting of interest rates, high domestic liquidity and competition in the sector explain the continued strong lending for house purchases. The deposit base continued to grow due to growing disposable income and as households prioritise liquidity and remain risk averse, while awareness of alternative investment options remains weak in a context of low financial literacy. The ample liquidity in the banking sector provided cheap and abundant funding for credit expansion. Moreover, mortgage lending interest rates are predominantly linked to the domestic deposit interest rates, which has contributed to keeping down the lending rates, against a backdrop of strong competition among leading banks. In 2024, with the easing of inflation and monetary conditions in the euro area, the practice of Bulgarian banks seeking temporarily higher returns from arbitrage on financial markets abroad instead of expanding domestic market shares, appears to have declined.

Given the risks to the debt-servicing capacity of borrowers, and the quality of banks' assets, the BNB reconfirmed the systemic risk buffer at 3% on 11 December 2023. Moreover, the BNB's Governing Council increased the minimum required reserves on the funds attracted from non-residents from 5% to 10% as from 1 June 2023. The minimum required reserves on the funds attracted from both residents and non-residents were increased from 10% to 12% as from 1 July

([25]) The fiscal stance is measured as the change in primary expenditure (net of discretionary revenue measures), excluding COVID-19-related temporary emergency measures but including expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other EU funds, relative to medium-term potential growth. A negative (positive) sign of the indicator corresponds to an excess (shortfall) of primary expenditure growth compared with medium-term economic growth, indicating an expansionary (contractionary) fiscal policy.

2023. The increased reserve requirements were motivated by high inflation, high consumer demand, dynamic credit activity, and slow and weak transmission from the monetary tightening in the euro area to the domestic financial market. As of October 2024, the BNB imposed borrower-based limits to commercial banks in the form of a maximum loan-to-value ratio of 85%, a limit of debt service to disposable income of 50% and maximum maturity of 30 years. The measures appear targeted at the low-income higher-risk borrowers that would be the first and hardest-hit by adverse economic conditions.

Table 2.2:
Bulgaria - Other inflation and cost indicators **(annual percentage change)**

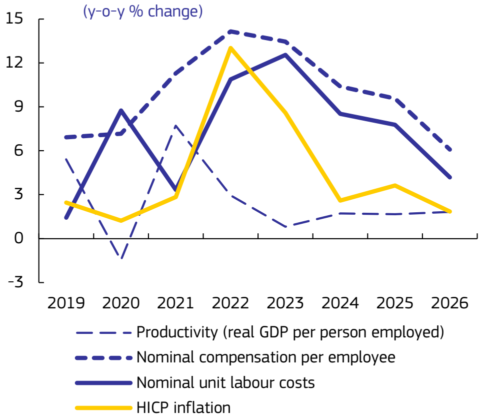
	2019	2020	2021	2022	2023	2024	2025 1)	2026 1)
HICP inflation								
Bulgaria	2.5	1.2	2.8	13.0	8.6	2.6	3.6	1.8
Euro area	1.2	0.3	2.6	8.4	5.4	2.4	2.1	1.7
Private consumption deflator								
Bulgaria	2.1	-0.6	6.0	16.0	8.1	4.9	3.5	2.5
Euro area	1.2	0.6	2.3	6.7	6.3	2.5	1.9	1.7
Nominal compensation per employee								
Bulgaria	6.9	7.2	11.3	14.2	13.4	10.4	9.6	6.1
Euro area	2.3	-0.4	4.3	4.5	5.3	4.5	3.3	2.7
Labour productivity								
Bulgaria	5.4	-1.5	7.7	3.0	0.8	1.7	1.7	1.8
Euro area	0.3	-4.6	4.7	1.1	-1.0	-0.1	0.3	0.8
Nominal unit labour costs								
Bulgaria	1.4	8.8	3.3	10.9	12.5	8.5	7.8	4.2
Euro area	2.0	4.4	-0.4	3.4	6.4	4.7	3.0	1.9
Imports of goods deflator								
Bulgaria	-0.2	-6.0	16.4	23.2	-3.6	-0.6	-0.1	0.3
Euro area	-0.5	-3.9	9.8	21.8	-4.3	-2.1	-0.6	-0.1

1) Commission's Spring 2025 Economic Forecast.
Source: Eurostat, Commission's Spring 2025 Economic Forecast.

Wages and labour costs

The labour market remained tight in 2023 and 2024, with the unemployment rate fluctuating between 4% and 4.5%, amid increasing participation rates and employment rates. Compensation per employee grew nominally by 13.4% in 2023 and by 10.4% in 2024. Throughout 2024 wage growth slowed from 13.8% in Q1 2024 to 4% in Q4 2024 and the number of employees in manufacturing declined, as inflation pressures subsided and firms aimed to improve their competitive position given weakened external demand.

Graph 2.3: **Bulgaria - Inflation, productivity and wage trends**



Source: Eurostat, Commission's Winter 2025 Economic Forecast.

Given the relatively low-income levels in Bulgaria, the setting of the minimum wage has an important effect both on income inequality and on labour market outcomes, such as participation rates and regional disparities. The minimum wage was increased by 9.9% at the beginning of 2023, still below the accumulated inflation since the previous update on 1 January 2021. As from 1 January 2024 the minimum wage was increased by 19.6%, to BGN 933 (EUR 477), following an amendment to the Labour Code aligned with Directive (EU) 2022/2041 on adequate minimum wages. Accordingly, the minimum wage in 2024 has to amount to 50% of the average wage in the July 2022 - June 2023 period. The same rule led to a further increase in the minimum wage by 15% in January 2025. Aggregate labour productivity improved by 0.9% in 2023 and by 1.7% in

2024, reflecting the stronger output expansion and some employment gains. Overall, unit labour costs (ULC) increased by 12.3% in 2023 and 8.5% in 2024.

The aggregate ULC dynamics in 2023 and 2024 conceal important sectoral developments. In 2023, wage growth in manufacturing accelerated to 23% in Q1 2023 (possibly reflecting the strong productivity gains in 2022) and then decelerated to 14% in Q4 2023 as firms tried to gain competitiveness in export markets. In 2024, manufacturing firms optimised production costs through labour shedding to accommodate the sizeable wage increases that reached almost 24% on aggregate in the sector. Wages in key service sectors (e.g. trade, transport and hospitality) have been growing much more moderately, especially in 2024. In the other services sectors, buoyant domestic demand led to intensified hiring and strong wage increases. Consequently, domestic cost pressures in services with low productivity gains contributed to higher value added deflators in these sectors. Wage increases in the public sector were also an important factor in the strong aggregate wage dynamics in 2023 and 2024.

External factors

Import prices are an important channel through which external price shocks affect the domestic price dynamics. The import deflator turned negative in 2023 and was almost constant in 2024. The disinflation process abroad has affected consumer prices directly via imported consumer goods and indirectly through prices of raw materials, etc.

The lev's real effective exchange rate, which is determined by the price of the lev vis-à-vis the currencies of 37 major trade partners, appreciated by 2.5% in 2023 and 1.1% in 2024. The appreciation in 2023 was strongly influenced by the depreciation of the Turkish lira against the euro. Türkiye is Bulgaria's most important trading partner outside the EU, accounting for 5.6% of total exports and 8.2% of total imports in 2023. In 2024, the appreciation of the Bulgarian lev was close to the long-term average and is explained by the higher domestic inflation compared to that of the major trading partners.

Administered prices and taxes

The share of administered prices in the HICP basket in 2025 is slightly higher at around 15%, compared with 12% in the euro area. Prices of electricity and water were increased substantially in 2023 and 2024 by the regulator. Electricity prices were subsequently increased by 8.4% in January 2025. Heat energy prices were also increased in 2023, and were subsequently decreased in 2024, broadly following price developments for natural gas. The decision to reduce co-payments for certain medicines in late March 2024 has also brought down the administered prices since April 2024. Overall, annual administered price inflation remained on average 1.9 percentage points above headline HICP inflation in the November 2023-March 2025 period and then fell 2.7 percentage points below overall HICP inflation in April 2025.

Indirect taxes had a slight negative effect on inflation in 2023 and a positive effect in 2024 and at the beginning of 2025. The energy measures (lower VAT rates for natural gas and central heating and exemption of excise duties for gas and electricity) expired only in mid-2023. As a result, HICP inflation at constant tax rates was above headline HICP inflation in 2023. In 2023 and 2024, excise duties on cigars and cigarettes were increased cumulatively by almost 10%. Combined with the full effect from the abolition of energy support measures in mid-2023, these changes led to a negative gap between HICP inflation at constant tax rates and headline HICP inflation in 2024. This gap widened at the beginning of 2025, following the expiration of VAT decreases for bread, flour and restaurants and the increase in excise duties on tobacco products by 6% ([26]). Another increase of the excise duties on tobacco products of around 4% was introduced in May 2025. In the euro area, annual constant-tax HICP was below headline inflation by 0.1 percentage point in 2023 and by 0.5 percentage point in 2024.

([26]) VAT rates of 20% were restored, after the expiration of the 0% VAT on bread and flour and the 9% on restaurants, introduced in mid-2020.

A comparison between the HICP index and Eurostat's measure of HICP at constant tax rates shows that the changes in indirect taxes in Bulgaria in January 2025 contributed directly to an increase in Bulgaria's month-on-month headline inflation in January 2025 by around 0.6 percentage point. This, together with the impact from higher regulated electricity and gas prices, which is estimated at around 0.4 percentage point, drives the forecast increase in annual inflation throughout the current year.

Medium-term prospects

The Commission's Spring 2025 Economic Forecast projects that average annual inflation will increase from 2.6% in 2024 to 3.6% in 2025 and gradually ease to 1.8% in 2026. After the price increases in Q1 2025, as discussed in Section 2.2.2., and the reduction in April 2025, inflation developments in the rest of 2025 and in 2026 are set to be driven by both external prices and domestic cost factors. Food prices are projected to broadly follow international developments. The pass-through of lower international energy and other commodities prices is projected to keep inflation down, including via second-round effects on transport services. The disinflation process in the services sector is set to benefit from the continuation of wage moderation and the need to preserve the competitiveness position in exported services in a context of a worsened external environment.

Increased inflation in 2023 has brought the consumer price level in Bulgaria closer to the euro area average. The level of consumer prices in Bulgaria nevertheless stood at about 57% of the euro area average in 2023. This suggests that there is potential for price level convergence in the long term, as GDP per capita in terms of purchasing power standards (about 61% of the euro area average in 2023) rises towards the euro area average.

Medium-term inflation prospects will depend on the containment of price expectations and on wage-productivity developments, as well as on the functioning of product and services markets. These developments may be substantially affected by the cyclical position of the economy.

2.3. PUBLIC FINANCES

2.3.1. Recent fiscal developments

The Bulgarian deficit has remained within the 3% of GDP Treaty reference value since 2022. However, after decreasing to 2.0% in 2023, the deficit returned to 3.0% in 2024. The expenditure-to-GDP ratio increased from 38.8% to 39.8% whereas the revenue-to-GDP ratio in 2024 remained broadly stable at 36.7% from 36.8%, also due to higher social security contributions and direct taxes, which benefited from favourable employment dynamics.

In 2023, changes in income policy parameters such as the minimum and maximum insurable income drove social contributions up. Revenues were further supported by the introduction of a 100% dividend policy on SOEs. Increases in public sector salaries and pensions that had been enacted in previous years started to have a budgetary impact. However, the outturn deficit for 2023 was also affected by the normalisation of energy prices, which contributed to a sharp decrease in subsidies (down by 46.7% from 2022, the equivalent of 2.2% of GDP).

Declining inflation in 2024 resulted in more moderate revenue increases, while the expenditure side continued to grow steadily due to legislative changes from 2022 that continued to have an impact in 2024. The deterioration in the deficit was partly driven by the sustained spending increases in public sector salaries and in social benefits, in particular on pensions, not fully matched by revenue increases. For pensions the main driver was the yearly indexation based on the so-called 'Swiss rule' (by 12% as of 1 July 2023 and by 11% as of 1 July 2024) and top-ups for pensions under the poverty line. Further increases were recorded in sickness and unemployment benefits among others. The one-off statistical recording of settled liabilities for road infrastructure works from 2020-22 also contributed, by 0.5% of GDP, to the increase in the deficit. Public investment decreased compared to 2023, partly due to the base effect in 2023 coming from the end-of-period absorption of the EU funds of the 2014-2020 programme.

Measures on the revenue side included a package of measures to fight tax evasion and avoidance, including improved checks on goods with high fiscal risk and improved exchange of information on cross-border payments. On the other hand, SOE dividends collected in 2024 were lower than in 2023, driving down other current revenues.

The fiscal stance was broadly neutral in 2024, driven by the expansionary contribution of net nationally financed primary current expenditure and of other capital expenditure that were largely offset by lower nationally financed gross fixed capital formation and the slightly contractionary contribution of EU-funded expenditure compared to 2023, which was the last year for the absorption of the EU funds for the programming period 2014-2020.

The debt ratio increased from 22.5% in 2022 to 22.9% in 2023. The primary deficit of 1.4% of GDP in 2023 and the impact of nominal GDP growth cancelled each other out, but the joint impact of interest expenditure and a positive stock-flow adjustment led to the increase. In 2024, the general government debt-to-GDP ratio further increased to 24.1%, mostly driven by a larger primary deficit (2.5% of GDP) and interest expenditure, which more than offset the impact of robust nominal GDP growth.

2.3.2. Medium-term prospects

On 27 February 2025, Bulgaria submitted its national medium-term fiscal structural plan to the Council and the Commission, covering the 2025-2028 period.

The net expenditure growth in the plan averages 4.9% over the 2025-28 adjustment period. In terms of structural primary balance, the plan envisages a yearly adjustment of 0.16% of GDP. The indicative strategy to meet the fiscal targets included in the plan is heavily reliant on revenue measures, and it envisages expenditure increases, notably in public sector salaries, pensions and social benefits.

On 12 May 2025, the Commission recommended to the Council to endorse Bulgaria's plan. Based on the plan's policy commitments and macroeconomic assumptions, the net expenditure path put forward in the plan is consistent with the requirements as set out in Article 16(2) of Regulation (EU) 2024/1263.

The 2025 budget was adopted by the National Assembly on 21 March 2025. On the revenue side, it heavily relies on the yields of measures to fight tax evasion and avoidance and on dividend policy, but it is also supported by other measures such as planned increases in excise duties on tobacco products and by the reinstatement of standard VAT rates including for restaurants, bread and flour. A positive impact on the budget is also expected from increases in maximum and minimum insurable income, resulting in higher social security contributions, and by improvements in arrears management.

On the expenditure side, the budget for 2025 envisages public sector salaries to grow, in line with recent trends, with the largest budgetary impact from increases in the remuneration of defence and security staff, followed by salary increases for teachers and increases in the minimum wage. Pension spending is expected to increase further, largely due to the impact of the Swiss rule, of other pension supplements (for instance widow's supplements), as well as the impact of newly-awarded pensions. Public investment is expected to increase considerably in 2025 compared to 2024, driven by the planned acceleration of RRP implementation, which needs to be completed by mid-2026, and also driven by strong increases in defence investment due to the accrual of planned deliveries of military equipment.

On 2 May 2025 Bulgaria submitted its 2025 Annual Progress Report, reporting on relevant fiscal outturn data and projections, and the implementation of reforms and investments responding to the main challenges identified in the European Semester country-specific recommendations. The 2025 Annual Progress Report also reflects Bulgaria's biannual reporting on the progress made in delivering on its recovery and resilience plan in accordance with Article 27 of Regulation (EU) 2021/241.

Based on the Commission's 2025 Spring Economic Forecast, the general government deficit is projected at 2.8% of GDP in both 2025 and 2026. Net expenditure is expected to grow by 9.2% in 2025, above the recommended growth rate of 6.2% for the same year. This is due to the combination of expenditure increases on pensions and public sector salaries and of a marked increase in expenditure on defence, including investment, as well as to higher public investment in other areas. On 2 May Bulgaria submitted a request to activate the National Escape Clause (NEC) for increases in its defence spending. On 4 June 2025, the Commission recommended a Council recommendation for the activation of the NEC for Bulgaria, allowing Bulgaria to deviate from, and exceed, the net expenditure path to be set in the Council recommendation endorsing its medium-term fiscal plan. Accounting for the flexibility under the NEC, the net expenditure growth for 2025 is expected to be in line with the net expenditure growth ceilings contained in Bulgaria's medium-term plan. The general government debt-to-GDP ratio is forecast to increase to 25.1% in 2025 and to reach 27.1% in 2026.

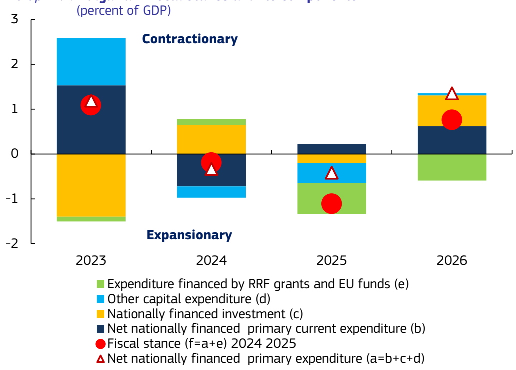
Table 2.3:

Bulgaria - Budgetary developments and projections (as % of GDP unless indicated otherwise)

Outturn and forecast 1)	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**1)	**2026**1)
General government balance	2.2	-3.8	-4.0	-3.0	-2.0	-3.0	-2.8	-2.8
- Total revenue	38.6	37.5	37.5	38.3	36.8	36.7	38.8	38.4
- Total expenditure	36.4	41.3	41.5	41.3	38.8	39.8	41.6	41.2
of which:								
- Interest expenditure	0.6	0.5	0.5	0.4	0.5	0.5	0.6	0.7
p.m.: Tax burden	30.5	30.3	30.7	31.1	29.9	30.9	32.2	31.8
Primary balance	2.7	-3.3	-3.5	-2.6	-1.5	-2.5	-2.2	-2.1
Fiscal stance 2)					1.1	-0.2	-1.1	0.8
Recommended growth in net expenditure (%)							6.2	4.9
Growth in net expenditure (%)							9.2	1.7
Government gross debt	20.1	24.4	23.8	22.5	22.9	24.1	25.1	27.1
p.m: Real GDP growth (%)	3.8	-3.2	7.8	4.0	1.9	2.8	2.0	2.1

1) Commission's Spring 2025 Economic Forecast.
2) The fiscal stance is based on the increase in net expenditure (including that financed by the EU budget) relative to medium-term potential GDP growth. A positive (negative) sign indicates a contractionary (expansionary) fiscal stance (in % of GDP). The fiscal stance profile in 2020-2023 does not include the temporary impact of COVID-19 emergency measures.
Source: European Commission.

Graph 2.4: **Bulgaria - Fiscal stance and its components**
(percent of GDP)



Source: Commission's Spring 2025 Economic Forecast.

Based on the Commission's estimates, the fiscal stance is projected to become expansionary in 2025, at –1.1% of GDP. The expansionary fiscal stance in 2025 is largely driven by EU-financed expenditure. The contribution of net nationally financed investment is also projected to be slightly expansionary (-0.2% of GDP) in 2025. The fiscal stance is expected to turn contractionary in 2026 (0.8% of GDP), mainly on account of the slower growth in nationally financed primary current expenditure and nationally financed investment.

Medium-term fiscal sustainability risks are assessed as medium. Government debt is projected to increase from 24.5% of GDP in 2024 to around 39% in 2035 ([27]). This projection assumes that the structural primary deficit (prior to accounting for expected changes in the cost of ageing) will remain constant at 2.3% of GDP as of 2025 ([28]).

The sensitivity analysis confirms this risk assessment since negative macro-fiscal shocks (i.e. a lower structural primary balance, a higher interest-growth rate differential or a temporary interest rate shock) would result in only somewhat higher debt ratios by 2035. On the other hand, if the structural primary balance were to return to its historical 15-year average of 0.6% of GDP, the debt ratio would be about 14 percentage points lower in 2035. The stochastic projections point to a large degree of uncertainty around the baseline projection.

Several factors mitigate risks, including the low share of short-term government debt and the small amount of general government contingent liabilities. Risk-increasing factors include the relatively high share of non-performing loans in the Bulgarian banking sector and the substantial share of public debt denominated in euro although this risk is mitigated by the currency board and the prospect for euro adoption.

The key elements of a robust fiscal framework are in place in Bulgaria, but some difficulties in implementation remain. Bulgaria has a complex system of national fiscal rules in place, unchanged since the 2024 Convergence Report. Several rules target the same budget aggregates but the fact that they are expressed according to different accounting standards (accrual and cash-based) may create conflicting messages. Moreover, the capacity of the Ministry of Finance to monitor, plan, forecast and report on the general government budget in both accrual and cash terms remains a challenge, especially with respect to the management and planning of government finances. The Ministry does not always have as much information or access to detailed data as would be desirable for budgetary planning. Information is lacking on the operations of entities outside the central administration and occasionally even of some other ministries. The Ministry of Finance also has weaknesses in producing projections on an accrual basis (e.g. under the European System of National and Regional Accounts (ESA)).

There is potential to enhance the capacity and independence of the Bulgarian independent fiscal institution (IFI), the Fiscal Council of Bulgaria (FCB). It currently has a narrow mandate, monitoring compliance of fiscal rules and assessing the macroeconomic and budgetary forecasts and is supported by a thinly staffed Secretariat of only two full-time employees. The six-year mandates of Members are not staggered, increasing the need for transparency in the appointment process. The mandates of the current Members expired in November 2021 and new Members were appointed in March 2025. The amended Budgetary Framework Directive (2011/85/EU) which is to be transposed by 31 December 2025, will affect some aspects of the Bulgarian fiscal framework, particularly relating to the Fiscal Council's independence safeguards and tasks.

The planning and budgeting of public investments is undergoing reform, but implementation challenges remain. Bulgaria shows scope for improvement on key dimensions such as (i) aligning investment decisions with their long-term strategic goals; (ii) vertical (between levels of government) and horizontal (across sectors) coordination; (iii) the application of consistent value-for-money criteria and methodologies to investments not financed by EU-funds; (iv) limiting the under-execution of capital expenditure; and (v) the carry-over of unspent funds.

2.4. EXCHANGE RATE STABILITY

The Bulgarian lev joined the Exchange Rate Mechanism II (ERM II) on 10 July 2020. The Bulgarian National Bank (BNB) entered in parallel into a 'close cooperation' agreement with the ECB. After

([27]) For more details on the methodology, see European Commission (2025), Debt Sustainability Monitor 2024, Institutional Paper 306, March 2025.

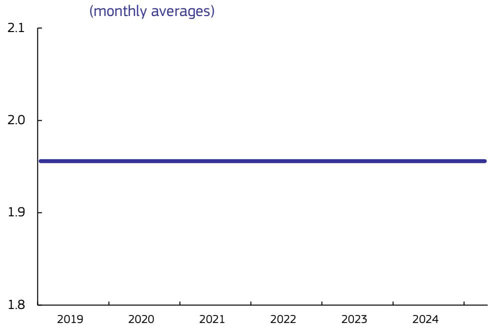
([28]) Bulgaria's medium-term plan implies that debt would reach around 41% of GDP in 2035, broadly similar to the baseline projection at unchanged policy in the Debt Sustainability Monitor 2024.

joining, Bulgaria committed to pursue a set of policy measures (known as post-entry commitments) to ensure that its participation in the mechanism is sustainable and achieves a high degree of economic convergence before the adoption of the euro. The measures cover four policy areas: (i) the non-banking financial sector; (ii) the insolvency framework; (iii) the anti-money laundering framework; (iv) and governance of state-owned enterprises.

Bulgaria introduced its currency board framework on 1 July 1997, pegging the Bulgarian lev to the German mark and subsequently to the euro (at an exchange rate of 1.95583 BGN/EUR). Under the currency board framework, the BNB has to fully cover its monetary liabilities with foreign reserves. The BNB is obliged to exchange monetary liabilities and euro at the official exchange rate without any limit.

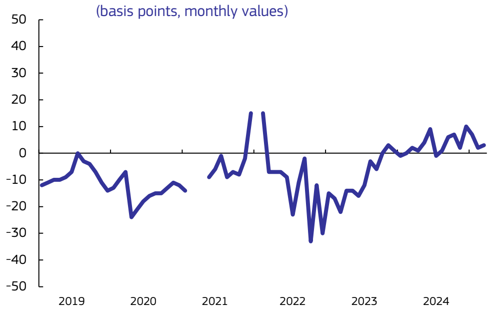
Bulgaria's international reserves are large, at 41% of GDP in 2024 (down from around 44% of GDP in 2023). International reserves increased from around EUR 38 billion at the beginning of 2023 to around EUR 42 billion at the end of 2023. The reserves decreased in the first half of 2024 to around EUR 38 billion and then increased to around EUR 42 billion by the end of 2024. Most of the inflows to the reserves in 2023 reflected the issuance of government securities on international financial markets. Positive contributions were also made by a net positive flow from purchases and sales of reserve currency by commercial banks. In 2024, sales of reserve currency by banks had the largest negative contribution to the gross international reserves, while Government and other depositors' funds had a positive contribution.

Graph 2.5: **Bulgaria - BGN/EUR exchange rate**
(monthly averages)



Source: ECB.

Graph 2.6: **Bulgaria - Annual effective interest rate spread to 1-M Euribor**
(basis points, monthly values)



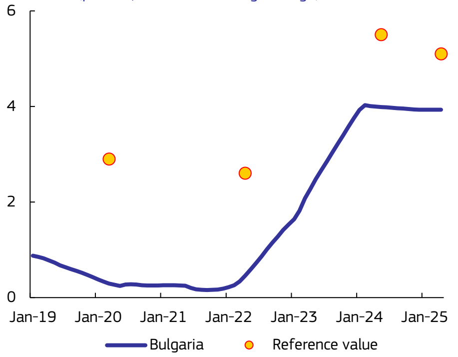
Source: Eurostat and National Bank of Bulgaria.

The BNB does not set monetary policy interest rates. The euro area's monetary policy affects domestic interest rates directly through the operation of Bulgaria's currency board. The BNB discontinued the production of short-term reference rates (e.g. SOFIBOR) from 1 July 2018. The BNB instead publishes a base interest rate (BIR) based on the LEONIA Plus (LEv OverNight Interest Average Plus) index, which is a reference rate of concluded and effected overnight deposit transactions in Bulgarian lev on the interbank market in Bulgaria. The BIR stood at 1.8% in January 2023. It increased throughout most of 2023, reaching 3.9% in October 2023 and remained at that level until May 2024. It decreased gradually to 2.4% in March 2025. The changes in the BIR closely tracked those of the 1-month Euribor rate. The interest rate differential between the BIR and the 1-month Euribor narrowed from -15 basis points at the beginning of 2023 to virtually no differential by the end of that year. The interest differential widened slightly throughout 2024 and stood at 3 basis points in March 2025.

2.5. LONG-TERM INTEREST RATES

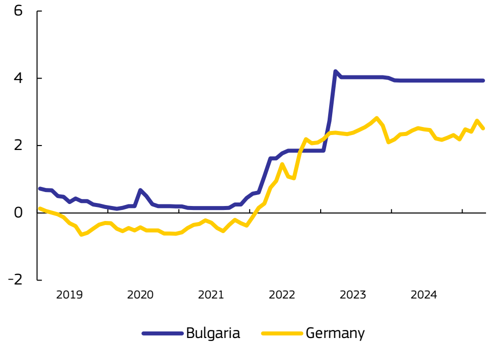
Long-term interest rates used for the convergence examination reflect the secondary market yield on a single benchmark Bulgarian government bond with a residual maturity of around 6.5 years.

Graph 2.7: **Bulgaria - Long-term interest rate criterion**
(percent, 12-month moving average)



Source: European Commission.

Graph 2.8: **Bulgaria - Long-term interest rates**
(percent, monthly values)



Source: Eurostat.

The Bulgarian 12-month moving average long-term interest rate relevant for the assessment of the Treaty criterion was below the reference value in the 2024 convergence assessment of Bulgaria. The average interest rate increased from 1.6% in January 2023 to 3.9% at the end of 2024. It stood at 4.0% until September 2024 and slightly decreased to 3.9% since then. In April 2025, the reference value, calculated as the average of long-term interest rates in Ireland, Finland and Italy plus 2 percentage points, was 5.1%. In that month, the 12-month moving average of the yield on the Bulgarian benchmark bond was 3.9%, i.e. 1.2 percentage points below the reference value.

The Bulgarian long-term interest rate has been stable at or close to 4% since April 2023, following two stepwise increases in February and March 2023. The long-term interest rate increased from 1.9% in January 2023 to 4.2% in March. Thereafter, it remained unchanged at 4.0% for the rest of 2023 and at 3.9% throughout 2024 and up to April 2025. The increase in the long-term interest rate at the beginning of 2023 reflected the very high inflation that Bulgaria experienced in 2022 and the tightening of monetary policy in the euro area that year. The stability of the long-term interest rate at the higher level is due to the use of a single benchmark bond at any point in time for this assessment and the fact that the bond is infrequently traded on the secondary market. Financial developments are therefore not seen in the yields until the bond is either traded or replaced by a new benchmark bond. The difference between the Bulgarian and German long-term interest rates remained within a range of 1.4-1.9% from March 2023 to April 2025. The higher spread compared to its historical average of around 1.2% during the past decade likely reflects the combined effects of higher inflation, heightened political uncertainty in Bulgaria and the thin secondary market for Bulgarian government debt securities.

2.6. ADDITIONAL FACTORS

The Treaty (Article 140 TFEU) calls for an examination of other factors relevant to economic integration and convergence that the Commission should take into account in its assessment. The assessment of the additional factors (including balance of payments developments, and product, labour and financial market integration) gives an indication of a Member State's ability to integrate into the euro area without difficulties.

In December 2024, the Commission published its 14th Alert Mechanism Report (AMR 2025) under the Macroeconomic Imbalance Procedure. The report concluded that it was not necessary to carry out further in-depth analysis on Bulgaria in the context of the Macroeconomic Imbalance Procedure. Developments related to cost competitiveness, dynamic household borrowing, and strong house-price growth remain a concern and require continued close monitoring. Nevertheless, nominal wage growth has been on a declining path with sharp deceleration in Q4 2024. House prices have continued to increase. They have been growing more slowly than income since 2013 but are estimated to be overvalued by around 10-15%. Household debt remains low as share of GDP despite dynamic credit flows that are supported by very low interest rates on mortgages. In terms of financial stability, in February 2024, the European Systemic Risk Board concluded that the residential real estate market in Bulgaria was subject to medium risks and the macroprudential policy mix was partially appropriate and partially sufficient to mitigate the situation. Borrower-based macroprudential measures were introduced by the Bulgarian National Bank in September 2024.

Bulgaria's recovery and resilience plan (RRP) includes measures to address a series of structural challenges by reforming the energy sector, investing in sustainable transport and green transition, promoting deployment of 5G networks, strengthening rule of law and the fight against corruption, promoting entrepreneurship and e-governance, improving the quality and inclusiveness of education and reforming the minimum income scheme. The plan is supported by EUR 5.7 billion of RRF funding.

Bulgaria has implemented 23% of the plan's milestones and targets and received one disbursement of EUR 1.37 billion or 24% of the overall allocation.

On 16 April 2025, Bulgaria submitted a request to revise its RRP in line with Art. 21 of the RRF Regulation. The revision concerns nearly all measures in the RRP and aims to bring the plan back on track and deliver on the original plan's key objectives. Together with its request for revision, Bulgaria has submitted a proposal for a REPowerEU chapter.

Some important reforms in areas such as anti-money laundering, insolvency framework, SOE governance reform and education have progressed. Implementing key reforms in the areas of energy, business environment and rule of law, is crucial to deliver on the RRP commitments. Investments providing support for small and medium enterprises, industrial modernisation and healthcare have progressed. However, overall implementation faces significant delays and needs to accelerate in order to complete all measures by August 2026.

In addition, cohesion policy funding helps tackle Bulgaria's growth and competitiveness challenges and aims to reduce the country's territorial and social disparities. In the current 2021-2027 programming period, cohesion policy provides Bulgaria with EUR 10.7 billion to further support Bulgaria's competitiveness, green transition, including energy independence, the just transition and climate change resilience, as well as upward social convergence, including by addressing labour shortages, further developing educational systems and skills and making them more inclusive for disadvantaged groups. Bulgaria has made progress in implementing cohesion policy but challenges remain.

2.6.1. Developments in the balance of payments

Bulgaria's external balance (i.e. the combined current and capital accounts) turned positive to 0.7% in 2023 and deteriorated to -0.1% in 2024. Net services exports improved markedly in 2023 with the recovery in tourism exceeding pre-pandemic levels and other services, including those outsourced to Bulgaria (e.g. IT and business services). It then slowed down in 2024 largely due to a temporary decline in transport services exports to Germany and Greece in Q2 and Q3 2024. The trade balance improved in 2023 as imports declined more steeply than exports on account of a deep contraction in inventories accumulation and more moderate private consumption. In 2024 trade balance deteriorated as external demand remained constrained, while imports of goods increased on account of stronger domestic demand. The Russian war of aggression continued to weigh on the export performance in 2024, with goods exports to the Russian Federation and Ukraine contracting by 26% and 38%, respectively, in nominal terms. The terms of trade deteriorated in both 2023 and 2024. The primary income deficit widened to 6.6% of GDP and then shrank to 5.1% in 2024, driven by the rise and the subsequent decline in foreign direct investment (FDI) income. Secondary income balance deteriorated as a share of GDP in 2023 and 2024, while capital account balance improved in both years. The developments in the secondary income balance were largely determined by the current transfers from the EU to the government, including direct payments under the Common Agricultural Policy and other non-investment grants. In 2023, the capital account balance improved mostly due to lower value of purchases of land abroad by residents. In 2024, capital transfers from the EU in the form of investment grants account for most of the increase in the capital account balance.

The financial account, net of official reserves, deteriorated to –2.5% of GDP in 2023 and then turned slightly positive in 2024. FDI, notably in the form of reinvested earnings, made the largest negative contribution to the financial account balance in both years. Net investments in debt securities abroad contributed by 1% of GDP and 1.5% of GDP to the financial account in 2023 and 2024, respectively. The improvement in 2024 is largely attributable to the increased investments in long-term debt securities abroad by the banking sector, related to the high domestic liquidity and higher returns on foreign financial assets. The balance of other investments had a limited impact on the financial account balance, with gross inflows and outflows of currency and deposits roughly offsetting each other. The BNB's reserve assets increased by 3.5% of GDP in 2023 and then decreased by 0.9% of GDP in 2024, largely mirroring the developments of the external balance and financial account ([29]).

Table 2.4:

Bulgaria - Balance of payments **(percentage of GDP)**

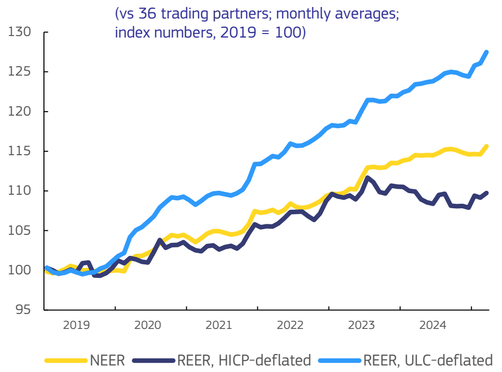
	2019	2020	2021	2022	2023	2024
Current account	1.7	0.4	-1.1	-2.7	-0.9	-1.8
of which: Balance of trade in goods	-4.7	-3.1	-4.0	-5.9	-4.2	-5.2
Balance of trade in services	8.1	5.7	6.5	7.0	8.3	7.5
Primary income balance	-4.8	-3.7	-4.8	-5.6	-6.6	-5.1
Secondary income balance	3.1	1.6	1.3	1.8	1.6	1.0
Capital account	1.5	1.4	0.7	0.9	1.6	1.7
External balance [1)]	3.1	1.9	-0.4	-1.7	0.7	-0.1
Financial account	3.6	4.2	3.9	2.7	1.0	-0.6
of which: Direct investment	-2.0	-4.1	-1.6	-4.1	-4.2	-2.2
Portfolio investment	2.6	1.2	3.2	1.2	1.3	2.3
Other investment [2)]	3.9	-2.2	-2.8	1.0	0.4	0.1
Change in reserves	-0.9	9.4	5.1	4.6	3.5	-0.9
Financial account without reserves	4.5	-5.1	-1.2	-1.9	-2.5	0.2
Errors and omissions	0.5	2.3	4.3	4.5	0.3	-0.6
Gross capital formation	20.7	20.1	20.7	22.7	19.7	20.4
Gross saving	22.4	20.7	20.5	20.1	20.4	19.5
Net international investment position	-30.8	-23.4	-15.6	-8.7	-6.3	-3.7

1) The combined current and capital account.
2) Including financial derivatives.
Sources: Eurostat, European Commission calculations, the Bulgarian National Bank.

The net international investment position further improved to –5% of GDP in 2024, having stood at over -50% of GDP a decade ago. The improvement reflects both nominal GDP growth as well as higher growth in foreign assets than in liabilities on the back of subdued FDI inflows.

The real effective exchange rate deflated by the HICP appreciated in 2023 and then depreciated in 2024 as domestic inflation abated. By contrast, the real effective exchange rate deflated by unit labour costs (ULC) accelerated, as domestic wage growth outstripped the wage dynamics abroad.

Graph 2.9: **Bulgaria - Effective exchange rates**



Source: European Commission.

With the deterioration of external demand in

([29]) Valuation changes (exchange rate or price changes) of the country's external assets and liabilities, as well as other changes, e.g. arising from changes in residence, are not included in the balance of payments.

2023, exporters sharply reduced inventory accumulation and cut purchases from abroad. Wage growth also decelerated throughout 2023 and 2024, reflecting firms' efforts to secure competitiveness gains against the backdrop of deteriorated foreign demand. In an environment of deteriorating world exports in 2023, Bulgarian export market share improved by 1.8%, driven by services exports.

The Commission's Spring 2025 Economic Forecast projects that the current account will remain slightly negative at to –1.1% of GDP in 2025 and -1% of GDP 2026 as imports grow faster than exports.

2.6.2. Market integration

The economy is well integrated with the euro area through trade and investment linkages. After a decline between 2019 and 2020, the ratio of trade openness (see Table 2.5 for a definition) rebounded to close to 71.2% in 2022, which was a new peak. It decreased to 61.5% in 2023 and further to 55.6% in 2024. Bulgaria is a relatively open economy. Trade with the euro area was around 25% of total trade in 2024. Germany, Italy and Greece were the main trading partners. Outside the euro area, Bulgaria's main trading partners were Türkiye and Romania.

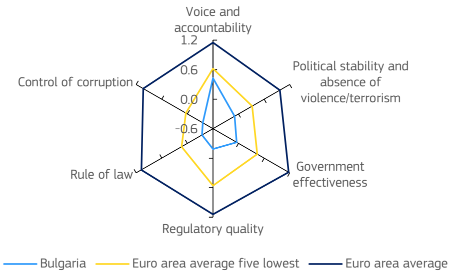
Table 2.5:
Bulgaria - Market integration

	2019	2020	2021	2022	2023	2024
Trade openness [1] (%)	64.4	56.8	62.0	71.2	61.5	55.7
Trade with EA in goods & services [2)+3)] (%)	29.0	25.7	28.0	30.7	27.5	24.5
IMD World Competitiveness Ranking [4]	48	48	53	53	57	58
Internal Market Transposition Deficit [5] (%)	0.6	1.6	2.2	1.8	1.7	1.6
Real house price index [6]	118.3	124.4	127.5	125.1	127.1	141.1

1) (Imports + Exports of goods and services / (2 x GDP at current market prices)) x 100 (Foreign Trade Statistics, Balance of Payments).
2) (Imports + Exports of goods with EA-20 / (2 x GDP at current market prices)) x 100 (Foreign Trade Statistics).
3) Trade in services with EA-20 (average credit and debit in % of GDP at current prices) (Balance of Payments).
4) International Institute for Management Development (IMD).
5) Percentage of internal market directives not yet communicated as having been transposed, relative to the total.
6) Deflated house price index (2015=100) (Eurostat).
Sources: Eurostat, World Bank, International Institute for Management Development, European Commission calculations.

Net FDI inflows have remained low, at 5.5% of GDP in 2023 and then declined to 3.1% of GDP in 2024. Reinvested earnings accounted for most the FDI inflows in those two years, while direct investment in equity from abroad contracted in 2024. The low inward FDI since the 2008-09 global financial crisis reflects low investor appetite and difficulties to attract fresh capital. The stock of inward FDI as a share of GDP continued to decline to 62% in 2024, down from 65% in 2023, due to both low FDI inflows and sustained nominal GDP growth. In 2024, financial and insurance, real estate and manufacturing constituted around 60% of the total inward FDI stock, in almost equal proportion.

Graph 2.10: **Bulgaria - World Bank's 2024 Worldwide Governance Indicators**



Note: Estimate of governance ranges from -2.5 (weak) to 2.5 (strong). The values in this chart are for 2023.
Source: World Bank.

Unsupportive business environment and institutional quality remain important challenges. According to the World Bank's 2024 Worldwide Governance Indicators, Bulgaria ranks markedly lower in rule of law, fight against corruption and regulatory quality than the average of the five euro area Member States with the lowest scores ([30]). Political favouritism has been shown to have a strong impact on public tenders and to have adverse effects on productivity and competitiveness ([31]). The Bulgarian RRP includes several measures to improve the business environment. These include ambitious reforms of the judiciary and anti-corruption reforms (including on whistle-blowing), the overhaul of the public procurement framework, the liberalisation of the electricity market, and strengthening the frameworks for insolvency, anti-money laundering and the governance of state-owned enterprises. The last three are also part of the post-entry commitments that Bulgaria made when it entered ERM II. After considerable delays, the implementation of several of these RRP reforms is under way and progressing (see also Section 2.7. on the Sustainability of Convergence).

Bulgaria has taken action to improve the framework for preventing and fighting money laundering, its predicate offences and the financing of terrorism. These actions include amending the Law on Measures Against Money Laundering to strengthen the capacity of national anti-money laundering and countering the financing of terrorism (AML/CFT) supervisory authorities to act where obliged entities fail to comply with their obligations and adopting an action plan for countering money laundering and terrorism financing (2023-2027) whose implementation is underway.

Bulgaria has also taken steps to: enhance the accuracy of beneficial ownership information through a mechanism for the reporting of discrepancies; reinforce the analytical capacity of the Financial Intelligence Unit to make better use of suspicious transaction reports (STRs) through the implementation of new IT software for the submission of STRs and other reports and information which became operational in March 2024; communicate swiftly targeted financial sanctions adopted and amended by the UN Security Council; and to identify the subset of non-profit organisations which are likely to be at risk of abuse for terrorist financing. Bulgaria underwent an assessment of the effectiveness of its AML/CFT framework against international standards developed by the Financial Action Task Force. As a result, Bulgaria was placed under increased monitoring and adopted an action plan, in October 2023 to address the deficiencies. The Bulgarian authorities are in the process of implementing the action plan.

The education system faces serious difficulties to ensure quality and inclusiveness. Around half of 15-year-old students lack basic numerical and reading competences according to the Programme for International Student Assessment. Socio-economic background has a major impact on students' performance, with children from disadvantaged groups performing considerably worse. To tackle some of these challenges, the Bulgarian RRP supports the creation of STEM learning centres, which is ongoing. The lack of basic skills translates to significantly fewer students entering higher education than the EU average, while quality standards for admission are lower.

Labour and skills shortages remain a significant challenge and risk worsening, considering the educational attainment and negative demographic trends. This in turn, combined with the high

([30]) A Member State is considered to have a 'low' ('high') ranking compared with the average five euro area Member States with the lowest scores for each indicator if its score is at least 0.3 percentage point lower (higher) than that of the average of this group of five euro area Member States. See also European Commission, 2024 Rule of Law Report, Country Chapter on Bulgaria.

([31]) Fazekas, M., Poltoratskaya,V., Schiffbauer, M.T., and Tóth, B., 'Procuring Low Growth: The Impact of Political Favoritism on Public Procurement and Firm Performance in Bulgaria', Policy Research Working Paper, Prosperity Washington, D.C.: World Bank Group, 2025.

inactivity rates for Roma and persons with disability, poses challenges for economic growth and social outcomes.

Bulgaria also scores low on digital skills and the update of digital technologies. Only 35.5% of Bulgaria's population has basic digital skills, which is among the lowest rates in the EU. Bulgaria scores very low on the digitalisation of businesses, with small and medium enterprises particularly affected. One of the priorities of both Bulgaria's RRP and Cohesion policy investments is to improve digital skills with significant investment to adapt the skill set of the workforce. Moreover, the RRP includes measures such as a voucher scheme for the digitalisation of small and medium sized enterprises and is complemented by targeted Cohesion Policy investments.

Public and private R&D investments remain amongst the lowest in the EU as share of GDP. The public research landscape is very fragmented with many educational institutions and research organisations receiving limited funding. Linkages between academia and business are not well-established and make commercialisation of research results difficult.

Regional disparities in Bulgaria remain high. GDP per capita in the capital Sofia is around three times higher than in the other regions. Similar differences are observed in labour productivity, demographics, education and training, employment, healthcare and infrastructure. In addition, the lower administrative capacity in some regions further impairs their ability to organise procurements, implement investments and to deliver public services and policies Addressing territorial disparities is one of the high-level objectives laid down in the Bulgaria's 2021-2027 Partnership Agreement.

Table 2.6:
Bulgaria - Allocation of assets by financial sub-sector

						Ratio to GDP (%)
	BG		**EA**		**EA 5 smallest**	
	2019	**2023**	**2019**	**2023**	**2019**	**2023**
Financial corporations (total)	172	169	721	698	177	189
Central bank	41	44	52	56	46	53
Monetary financial institutions	95	90	271	278	86	89
Other financial intermediaries	16	15	192	172	17	20
Non-MMF investment funds 1)	1	2	113	113	5	5
Insurance co. and Pension Funds	19	18	94	79	23	23
						Share of total (%)
	BG		**EA**		**EA 5 smallest**	
	2019	**2023**	**2019**	**2023**	**2019**	**2023**
Central bank	24	26	7	8	26	28
Monetary financial institutions	55	53	38	40	49	47
Other financial intermediaries	9	9	27	25	9	10
Non-MMF investment funds	1	1	16	16	3	3
Insurance co. and Pension Funds	11	11	13	11	13	12

1) MMF stands for money market funds.

Source: Eurostat.

Bulgaria's financial sector is smaller and less developed than the euro area's. The assets of the financial sector amounted to 169% of GDP in 2023, which was much less than in the euro area (698% of GDP) but broadly similar to the average of the five euro area Member States with the smallest financial sectors. As in the euro area, the size of the financial sector as a share of GDP has shrunk in Bulgaria since 2019. Banking dominates the Bulgarian financial sector, making up 55% of the financial sector's assets in 2023. The BNB is the second largest holder of financial assets with a share of 26% in 2023, more than all non-banking financial intermediaries taken together. These shares are larger than in the euro area, reflecting a relative underdevelopment of non-bank financial intermediaries and investment funds, similar to that of the five euro area Member States with the smallest financial sectors. At the same time, the relative share of the insurance and pension-fund sector in Bulgaria is similar to that in the euro area.

Table 2.7:

Bulgaria - Financing of the economy1)

						Ratio to GDP (%)
	BG		EA		EA 5 smallest	
	2019	2023	2019	2023	2019	2023
Total liabilities	361	345	762	725	318	301
Loans	114	93	235	219	104	94
Non-financial co. debt securities	3	2	12	12	3	2
Financial co. debt securities	1	1	67	60	3	5
Government debt securities	18	19	79	71	48	42
Listed shares	10	8	70	65	13	11
Unlisted shares	72	69	191	189	53	52
Other equity	84	95	72	73	60	61
Trade credits and advances	61	59	35	36	34	35
						Share of total (%)
	BG		**EA**		**EA 5 smallest**	
	2018	**2023**	**2019**	**2023**	**2019**	**2023**
Loans	33	27	31	30	33	31
Non-financial co. debt securities	1	0	2	2	1	1
Financial co. debt securities	0	0	9	8	1	2
Government debt securities	5	5	10	10	15	14
Listed shares	3	2	9	9	4	3
Unlisted shares	21	20	25	26	18	19
Other equity	25	28	9	10	18	19
Trade credits and advances	18	17	5	5	11	11

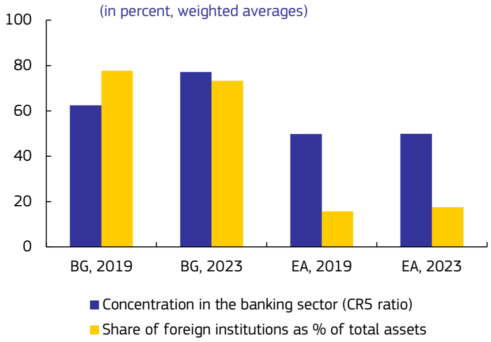
1) The table focuses on the financing needs of a country and how these are met by the financial system. The table is constructed from the liabilities of all economic sectors, but only considers loans, debt securities, equity and trade credits. The sum of liabilities in the table only reflects the total for the liabilities considered.

Source: Eurostat.

As to the financing of the economy, outstanding liabilities are much lower than in the euro area (345% of GDP in 2023 vs 725% of GDP in the euro area) but higher than those of the euro area Member States with the lowest financing needs. As in the euro area, loans are the dominant source of funding. However, Bulgaria has less developed bond and equity markets than the euro area and market financing (debt securities and listed shares) is relatively underdeveloped. Equity and private-sector-debt markets represented 2% of liabilities in 2023 (and only 11% of GDP altogether), compared with 19% of liabilities in the euro area (where private-sector debt and listed stocks amounted to 72% and 65% of GDP respectively). Bulgaria's financing structure is broadly similar to that of the five euro area Member States with the smallest financial needs, except for the smaller size of its bond market. The latter mostly reflects the low level of public debt in the country. Trade credits and advances play a bigger role in the financing of the economy in Bulgaria than in the euro area, even when compared with the five euro area Member States with the lowest financing needs.

Bulgaria's banking sector is well integrated into the euro area's financial sector, in particular through a high level of foreign ownership in the banking system. The ratio of foreign-owned institutions to total bank assets was 73% in 2023, down from 78% in 2019. Bank concentration (as measured by the market share of the five largest credit institutions in total assets) has increased significantly since 2019 and reached almost 77% in 2023. This is 27 percentage points above the euro area average in 2023.

Graph 2.11: **Bulgaria - Foreign ownership and concentration in the banking sector**
(in percent, weighted averages)



Source: ECB, Structural financial indicators.

2.7. SUSTAINABILITY OF CONVERGENCE

This concluding section draws together elements that are key for gauging the sustainability of Bulgaria's convergence with the euro area. The analysis reviews sustainability from a number of angles.

First, the sustainability dimension is inherent in the individual convergence criteria themselves. This holds most explicitly for the price stability criterion, which includes the requirement of a 'sustainable price performance'. In principle, the fiscal criterion (EDP) also involves a forward-looking aspect, providing a view on the durability of the correction of fiscal imbalances. While the exchange and interest rate criteria are, by construction, backward-looking, they aim to capture an economy's ability to operate durably under conditions of macroeconomic stability, indicating whether the conditions for sustainable convergence following euro adoption are in place.

Second, the assessment of additional factors (balance of payments, product and financial market integration) required by the Treaty broadens the view on sustainability of convergence and allows for a more complete picture, complementing the quantitative criteria. In particular, a sound external competitiveness position, effectively functioning markets for goods and services and a robust financial system are key to ensuring that the convergence process remains smooth and sustainable.

Third, the convergence assessment should be informed by the results and findings of enhanced policy co-ordination and surveillance procedures (MIP, fiscal governance), taking into account the comprehensive reform of the EU's economic governance rules in 2024. The aim is not to add to the existing requirements for euro adoption, but to make full use of the comprehensive economic and financial analysis undertaken under the European Semester. While some elements drawn from the European Semester (e.g. related to AMR scoreboard indicators) are included in the relevant chapters on convergence above, this section uses this framework more systematically to provide an integrated view of the sustainability dimension.

Any assessment of the sustainability of convergence has limits and must be based on a judgement of the likely future development of the economy. In particular, as experience has shown, the sustainability and robustness of the convergence process after euro adoption is to a significant extent endogenous, i.e. it depends on a Member State's domestic policy measures after it has joined the euro area. Therefore, while the assessment of sustainability is an essential element in determining a Member State's readiness to adopt the euro based on initial conditions and existing policy frameworks, the outcome of such an assessment should be seen as a snapshot at a specific point in time. The long-term sustainability of the convergence process will also depend on the adoption of appropriate policies over time. In this respect, the ongoing surveillance carried out in the context of the European Semester will play a major part in ensuring that such policies are implemented by the Member State after euro adoption.

The analysis below looks at sustainability from four different perspectives: price stability; fiscal performance and governance; structural resilience and growth sustainability; and financial resilience.

Price stability

The synchronisation of Bulgaria's business cycle with that of the euro area (see next sub-section) tends to keep Bulgaria's headline and core inflation at levels similar to those of the euro area. Bulgaria's inflation developments were particularly closely aligned with those of the euro area over the decade preceding the energy price shock of 2022. On average, between 2011 and 2021, Bulgaria's headline inflation rate averaged 1.1%, which was below the euro area average of 1.3%. Core inflation during this period, at 0.4%, was considerably below the euro area average at 1.1%.

By contrast, between 2022 and 2024, inflation in Bulgaria was significantly higher than in the euro area, with an average annual rate of 8.1% compared to 5.4% in the euro area. The de-coupling of inflation in Bulgaria and the euro area during these years was mainly due to Bulgaria's greater exposure to the food and energy price shocks. The price hikes in imported energy and other materials in 2022 led to a surge in production costs, thereby also contributing to higher prices for domestically produced goods and services. The cost-push factor was more pronounced than in the euro area because the Bulgarian economy is around three times more energy intensive than the euro area and its cyclical position was stronger. As food accounts for a significantly higher share of household consumption in Bulgaria, the food price shock had a disproportionately stronger impact on headline inflation. Subsequently, the unwinding of the shocks led to a stronger disinflation process in Bulgaria compared with the euro area. Headline and core inflation in Bulgaria both fell in 2024 by around 6 percentage points compared with a drop of 3 and 2.2 percentage points respectively in the euro area.

The pick-up in inflation in Bulgaria in 2025 is of a temporary nature and mainly reflects increases in January 2025 in a mix of taxes and administered prices, partially offset by the lowered hospital fees in April. This effect is set to lead to higher inflation throughout 2025. As the temporary effect of higher taxes and administered prices fades away, annual inflation is forecast to fall steadily throughout 2026, leading to a decreasing inflation gap compared to the euro area (see Section 2.2.3.). Additional evidence on the temporary and not broad-based nature of the increase in inflation in 2025 is provided by the median HICP inflation rate ([32]), which has remained below 2.5% since the beginning of the year, as well as by price expectations in the Commission's consumer and business surveys, which remain below their long-term averages ([33]).

Notwithstanding their recent deceleration, nominal unit labour costs (ULC) in Bulgaria have risen strongly historically, with an annual average growth of 6.3% since 2011. This trend increase in ULC occurred in both the tradeable and non-tradeable sectors of the economy, with a relatively limited difference between manufacturing and the rest of the economy. Nevertheless, the increase in ULC has not been associated with a loss in Bulgaria's export market share, which increased by around 10% between 2011 and 2013 and has remained broadly steady since then ([34]). This preservation of Bulgaria's export market share was supported by a mix of margin compression, i.e. reduced profits per unit of exports, non-labour cost compression, and improved non-cost competitiveness through a gradual shift towards higher value-added and tech-intensive products ([35]). The growth

([32]) Median inflation is the month-on-month inflation rate of the component whose expenditure weight is in the 50th percentile of price changes. By omitting outliers (small and large price changes), median inflation provides an alternative measure of underlying inflation. The value above refers to the unweighted measure of median inflation.

([33]) European Commission, Business and consumer survey results for April 2025, Statistical Annex.

([34]) Market performance of exports, Annual macro-economic database (AMECO) of the European Commission's Directorate General for Economic and Financial Affairs.

([35]) Evidence supporting this conclusion is also provided in Ivanov Evgeni and Ivanova Neli (2021), 'Determinants of Bulgarian Exports: the Role of Price and Non-Price Competitiveness', Bulgarian National Bank, Discussion Paper DP/118/2021.

profile of wages and ULC will need to be carefully monitored in the coming years in view of the important implications for price stability, the economy's adjustment capacity and external competitiveness. In this context, it will be important to focus structural policies and reforms on productivity growth, including technological upgrades to continue sustainable economic convergence without lasting price pressures.

Bulgaria's successful integration into the euro area will require the continued careful monitoring of inflation pressures, with longer-term inflation prospects contingent on wages growing in line with productivity. In this respect, continued high growth in public sector wages constitutes a risk for higher aggregate wages in Bulgaria. These factors could weigh on the adjustment potential, cost competitiveness and inflation prospects of the economy.

Structural resilience and growth sustainability

When assessing Bulgaria's capacity to function smoothly in the euro area, an important dimension is its current degree of cyclical synchronisation with the euro area and risks that that this synchronisation may weaken in the future. Such a risk will depend on Bulgaria's macroeconomic vulnerabilities and exposure to economic shocks as well as its capacity to adjust to such shocks.

Bulgaria's economic cycle has been closely synchronised with that of the euro area for the past two decades, both in terms of the real GDP growth rate and the output gap and it is forecast to continue doing so in 2025 and 2026. This cyclical synchronisation is higher than for most other non-euro area Member States. To a large extent, it is explained by Bulgaria's highly open economy, its strong integration in the EU single market, and the pegging of the lev to the euro since 1999 in the context of the currency board framework. In turn, the latter has been backed by prudent fiscal policy and low government debt. Bulgaria's trade grew strongly from the early 2000s up to its EU accession and then throughout its EU membership. More than half of exports and imports of goods and services are with the EU, with Germany, Romania, Italy and Greece being the most important markets. Türkiye is also an important trading partner.

As to vulnerabilities and exposure to shocks, Section 2.6. stressed that the Macroeconomic Imbalance Procedure did not identify major imbalances in Bulgaria in 2025. In particular, the country's external position appears solid. The external balance (the combined current and capital account) has been positive most of the time since 2011 and the net international investment position (NIIP) improved substantially from –97% of GDP in 2009 to around -4% of GDP in 2024. Moreover, Bulgaria's NIIP excluding non-defaultable instruments, such as foreign direct investment and equity shares, has been positive over recent years and reached 46% of GDP in 2024. Bulgaria also enjoys relatively high export diversification, which reduces its exposure to sectoral trade shocks. Measures of export diversification such as the Herfindahl-Hirschman Index put Bulgaria among the EU Member States with a high export diversification ([36]). Nevertheless, two sources of external vulnerability should be mentioned. The first is cost competitiveness, which was already mentioned in the subsection on inflation. The second relates to the country's high exposure to energy and food prices. As witnessed in recent years, shocks to global energy and food prices have a stronger pass-through into domestic inflation than the euro area average. The decarbonisation of energy production in Bulgaria, including through higher investment in renewables, would strengthen the competitiveness of the Bulgarian economy and reduce its exposure to energy price shocks.

The 2025 MIP also identifies two sources of domestic vulnerability: strong growth in credit to households and signs of overvaluation in house prices. Although the household debt-to-GDP ratio remains low, at 26% in 2024, credit flows remain high - in 2024, they were equivalent to 21% of the debt stock in 2023 - and has stood above the MIP threshold of 14% since 2021. According to

([36]) Herfindahl-Hirschman Market Concentration Index a measure of the dispersion of trade value across an exporter's partners. It ranges from 0 for perfect diversification and 1 for perfect concentration (i.e. lower values indicate that exports are more diversified).

the 2025 Alert Mechanism Report, house prices are estimated to be slightly overvalued by around 10-15%, with continued strong growth in 2023 and 2024.

Several features of the Bulgarian economy support its capacity to adjust to shocks, including its labour market and low public debt. Bulgaria's adjustment capacity was amply tested during the pandemic and energy crises, when the economy faced extraordinary headwinds. The contraction in economic activity in 2020 was lower than in the euro area and the recovery in output in 2021 and 2022 was stronger.

Bulgaria's labour market is relatively flexible and efficient and this flexibility should facilitate adjustment to changes in economic conditions. Despite unprecedented shocks, the unemployment rate has declined by more than 1 percentage point since the COVID-19 crisis and now stands more than 2 percentage points below the euro area. However, the Bulgarian labour market also suffers from some weaknesses in terms of skills shortages (see Section 2.6.2.) and structurally fast growth in wages (see subsection on inflation above). The former requires structural challenges in the education system to be addressed and increases in adult training. Another positive feature of Bulgaria's adjustment capacity relates to the level of its public debt. In 2024, the country's public debt amounted to 24% of GDP, the second lowest ratio in the EU. In the medium term, such a low level of government debt should provide the fiscal space that is needed in a monetary union in the event of adverse shocks. In the shorter term, however, Bulgaria's fiscal space is constrained by a deficit, which remains close to the 3% limit.

Bulgaria's adjustment capacity remains hindered by a non-supportive business environment. Various reports and indicators by international institutions, such as the World Bank's Worldwide Governance Indicators, IMD's World Competitiveness Report and OECD's Product Market Regulation (PMR) indicators ([37]), point to an unfavourable business environment, and low government and business efficiency. Businesses in the country report that the most significant hindrances to a better business environment are corruption, frequent changes in regulations, bureaucracy, and biased public procurement ([38]). Businesses have also consistently complained about the quality of regulatory work ([39]) and the failure to ensure a level playing field ([40]). Regulatory barriers remain higher in Bulgaria than in comparable countries for lawyers, notaries, architects and civil engineers. Improving the business environment would both enhance productivity and improve the capacity of firms to respond to shocks.

In recent years, Bulgaria has implemented several reforms that should support its resilience and adjustment capacity. There is, however, substantial scope for further progress in this area. In July 2019, the country committed to implementing policy measures prior to joining the ERM II in the following six policy areas: banking supervision; the macroprudential framework; the supervision of the non-banking financial sector; the anti-money laundering framework; the insolvency framework; and the governance of state-owned enterprises (SOEs). In June 2020, the Bulgarian authorities notified the ERM II parties of the fulfilment of these commitments, which the ECB and the Commission assessed as effectively implemented. At the time of its ERM II entry in July 2020, Bulgaria committed to implementing further policy measures in the following four areas: i) the non-banking financial sector; (ii) insolvency framework; (iii) the anti-money laundering framework; and iv) the governance of SOEs.

Measures implemented in the non-banking financial sector aim to improve supervisory practices and the governance and functioning of the insurance sector. Insolvency framework measures included: an overhaul of the legislative framework; training programmes for insolvency

([37]) See: https://www.worldbank.org/en/publication/worldwide-governance-indicators; International Institute for Management Development/World Competitiveness Centre, World Competitiveness Booklet 2024; and OECD's Product Market Regulation (PMR) indicators, Key takeaways from the 2023-2024 update of the OECD Product Market Regulation indicators, ECO/CPE (2024)99.

([38]) Bulgarian Industrial Association – 2024 through the eyes of the business.

([39]) EIB Investment Survey 2022 – European Union overview.

([40]) European Commission, 2023 and 2024 editions of the Rule of Law Report, Country Chapter on Bulgaria.

practitioners; development of manuals, guidelines and specialised electronic tools; and improved data collection and publicity. Regarding anti-money laundering, Bulgaria committed to enhance the capacity of supervisors and adopt a risk-based approach to detecting and countering such activities. On SOEs, the authorities committed among other elements to improve their governance by ensuring competitive procedures for board appointments and regular financial performance reporting.

Bulgaria's recovery and resilience plan includes an ambitious set of structural reforms and investments but has faced delays. Bulgaria made some progress with implementing reforms to strengthen the rule of law and improve the overall business environment. It has yet to implement major reforms to and investments in the decarbonisation of the energy sector, as well as further business environment reforms, notably on anti-corruption. In April 2025, Bulgaria submitted a comprehensive revision of its RRP, including a REPowerEU chapter, with a view to bringing the plan back on track and achieving its ambitious objectives. Accelerating the implementation of the planned investments and reforms would strengthen the resilience of the economy and ensure Bulgaria benefits fully from its funding allocation under the recovery and resilience facility.

Financial resilience

Bulgaria's financial sector has shown stability and resilience, particularly since the 2009 international financial crisis and during the COVID-19 pandemic and in the aftermath of Russia's invasion of Ukraine. The banking sector is by far the largest financial subsector in Bulgaria, although it is still small relative to the size of its economy when compared to the EU and euro area Member States on average.

The accession of Bulgaria to the Banking Union in 2020 led to the direct supervision by the ECB of 5 commercial banks registered in Bulgaria, which hold approximately three quarters of all assets in the banking sector.

The banking sector is well-capitalised and profitable. Bulgaria's banking sector capital adequacy and liquidity ratios have remained at consistently high levels. The tier-1 capital ratio is estimated at 22.0% as of December 2024, compared with an EU average of around 17.5%. Bulgaria's banking sector liquidity coverage ratio, at around 240% at end-December 2024 ([41]), was also well above the EU ratio of around 165% ([42]) and around two-and-a-half times higher than the regulatory minimum required level of 100%.

The banking sector records healthy profits. The sector is expected to have achieved record profits in 2024, driven by strong net interest income. The Bulgarian National Bank estimates a return on equity (ROE) at the end of December 2024 of around 16.0%. This compares with a return of 10.5% in 2024 for EU banks ([43]). The Bulgarian banking sector has experienced rapid growth in lending over the past several years, with a focus on mortgage lending. Low interest rates, abundant liquidity in the banking system, rapid income growth and positive consumer sentiment together have contributed to the dynamic credit activity. In September 2024, the total amount of loans for households grew by 21.3% year on year, while loans to non-financial corporations (NFCs) increased by 9.1%. The prolonged period of strong lending activity leads to a possible accumulation of credit risks in the banking system's balance sheet, which in the medium term could put some downward pressure on the high levels of profits by Bulgarian banks. However, while the ratio of non-performing loans (NPLs) remains relatively high, the rapid increase in loan volumes has not translated into growing NPLs. The share of non-performing exposures continue to decline to historically low levels in all major segments of the banks' loan portfolio, mostly due to write-offs and sales of NPLs. A roadmap on the insolvency framework reform was adopted in

([41]) Banks in Bulgaria October–December 2024, Bulgarian National Bank (see: https://www.bnb.bg/bnbweb/groups/public/documents/bnb_publication/pub_b_in_b_2024_12_en.pdf).

([42]) Liquidity coverage ratio, EU countries participating in the Single Supervisory Mechanism. ECB Data Portal (see: https://data.ecb.europa.eu/data/datasets/SUP/SUP.Q.B01.W0._Z.I3017._T.SII._Z._Z._Z.PCT.C).

([43]) European Bank Authority, Risk Dashboard Q4 2024.

2019 as part of the ERM II prior-commitments to prepare Bulgaria for successful participation in ERM II. The ERM II post-entry commitment on insolvency sought to implement the roadmap. To this end, the changes to the Bulgarian Commercial Act in 2023 and secondary legislation aim to address long-standing shortcomings in Bulgaria's insolvency and restructuring regime. The legislative amendments and measures to implement these are also part of the Bulgarian RRP. In recent years, the Bulgarian National Bank has repeatedly increased the countercyclical capital buffer rate applicable to domestic credit risk exposures to further strengthen the resilience of the banking system and prevent an excessive build-up of risks. The Bulgarian National Bank also introduced borrower-based measures targeted at low-income higher-risk borrowers as of October 2024.

Bulgaria's capital market is underdeveloped and does not adequately support financing needs for both the government and corporates. Recent initiatives could help increase capital market growth by increasing financial literacy and engaging market participants. In April 2023, the Bulgarian Ministry of Finance published a report, which included 60 recommended actions, with the objective of increasing the availability of investable assets and the level of trust in the Bulgarian capital market and ultimately making the use of the capital markets cheaper and more efficient within a time horizon of 5 years ([44]). Over the past few years Bulgaria has been a net lender to the rest of the world, partially due to limited domestic investment opportunities, depicted by still underutilised and relatively inefficient domestic capital markets. Local private-equity (PE) and venture-capital (VC) markets remain too small to meet the financing needs of innovative firms. In addition, VCs in Bulgaria focus more on early-stage businesses, which is positive for innovation but may pose challenges when scaling start-ups, supressing growth prospects.

The supervisory framework for Bulgaria's non-banking financial sector has been significantly strengthened both in preparation for the country's Exchange Rate Mechanism II entry in 2020 and since then, in addressing post-ERM II policy commitments. The insurance market, though highly concentrated, remains significantly smaller than the EU average, with notable distinctions between its life and general insurance segments. The low insurance penetration and steady economic growth present promising opportunities for insurers to grow and both life and non-life insurance are projected to expand rapidly in the years to come.

Conclusion

The broad-based analysis of underlying factors relevant for the sustainability of Bulgaria's convergence suggests that sufficiently robust conditions are in place for the country to be able to maintain a sustainable convergence path in the medium term, thus supporting a positive assessment. However, significant challenges remain, and policy discipline will need to be maintained in a determined manner to fully exploit the benefits of participation in the euro area and minimise risks to the convergence path going forward.

([44]) Bourse Consult (2023), 'Bulgaria: Diagnostic of the State of the Capital Market', Gap Analysis and Recommendations Reports, August 2022 (https://reform-support.ec.europa.eu/publications-0/bulgaria-diagnostic-state-development-bulgarian-capital-market-gap-analysis-and-recommendations_en).

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