EuPI European Policies Initiative

Open Society Institute – Sofia

Country Report BULGARIA

Economic and Political Challenges of Acceding to the Euro area in the post-Lehman Brothers' World

George Angelov,
Open Society Institute- Sofia

Sofia, October 2009

The publication is a product of the Open Society Institute – Sofia within the European Policies Initiative (EuPI) and the project "Economic and Political Challenges of Acceding to the Euro area in the post-Lehman Brothers' World".

The publication comprised of nine Country Reports and a Summary Report is available on the website of the European Policies Initiative: www.eupi.eu

About EuPI

The European Policy Initiative (EuPI) aims at stimulating and assisting the New Member States from CEE to develop capacity for constructive co-authorship of common European policies at both government and civil society level. As a new priority area of the European Policies and Civic Participation Program of Open Society Institute – Sofia, EuPI will contribute to improving the capacity of New Member States to effectively impact common European policies through quality research, policy recommendations, networking and advocacy.

Address:
Open Society Institute – Sofia
European Policies Initiative (EuPI)
56 Solunska Str.
Sofia 1000
Tel.: (+359 2) 930 66 19
Fax: (+359 2) 951 63 48
E-mail: eupi@osi.bg
Web EuPI: www.eupi.eu
Web OSI-Sofia: www.osi.bg

About the publication

The publication is a product of the Open Society Institute – Sofia within the European Policies Initiative (EuPI) and the project "Economic and Political Challenges of Acceding to the Euro area in the post-Lehman Brothers' World".

EuPI aims at stimulating and assisting new Member States from CEE to develop capacity for constructive co-authorship of common European policies at both government and civil society levels (www.eupi.eu).

The project was implemented from September 2008 to September 2009. The main outcome of the project is a publication comprised of nine Country Reports and a Summary Report.

Following a uniform structure, and addressing a set of similar questions, the nine Country Reports (Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania and Slovenia) present stylized facts about the patterns of real and nominal convergence with the euro area in nine new EU members, outline the setting and the implementation of the accession policies in those countries and emphasize the incidence of the current crisis on the strategy to adopt the common currency.

Comments are relevant to policy developments until 20 May, 2009 – the cut-off date for the submission of the last revised version of the Country Reports.

The Summary Report reviews the results of the Country Reports and systematizes some of the dominant trends they reveal. The Summary Report checks the countries' experience in dealing with the complicated concentric monetary structure inside the EU (euro area; ERM II; non ERM II countries) and pays particular attention to the evidence gathered about the political economy of the procedures in the different countries.

Each Country Report and the Summary Report include an Appendix, containing Tables that summarize significant data provided in accordance with a standardized set of indicators.

The results of the Project are correctly intelligible only if all its pieces (ToR, Summary Report, Country Reports, Appendix) are considered together.

Advisory Board
The project was able to benefit from the insights of a distinguished Advisory Board. As the Boards' mandate was limited to advice and comments on the methodology and the Summary report, responsibility for the findings and statements rests solely with the authors of the Country and the Summary reports.

Advisory Board Members:

Roumen Avramov, Program Director for Economic Research at the Centre for Liberal Strategies in Sofia

Marek Dąbrowski, Professor of Economics, President of the CASE – Center for Social and Economic Research in Warsaw and Chairman of the Supervisory Board of the CASE-Ukraine.

Luděk Niedermayer, Director at Deloitte Czech Repiublic, responsible for the area of financial institutions in Central Europe.

Karsten Staehr, Professor of economics at Tallinn University of Technology, Estonia, and a part-time research advisor at Eesti Pank, the Estonian Central Bank.

György Szapáry is a visiting professor at the Economic Faculty of the Central European University in Budapest and member of the Board of Directors of the OTP Bank

Authors of the Reports

Summary Report:	Roumen Avramov, Program Director, Center for Liberal Strategies Sofia
Bulgaria:	George Angelov, Senior Economist, Open Society Institute-Sofia
Czech Republic:	Ondrej Schneider, Associate Professor, Institute of Economic Studies, Charles University, Prague, Czech Republic
Estonia:	Hardo Pajula, OÜ Monadero
Latvia:	Jānis Bērziņš, Institute of Economics of the Latvian Academy of Sciences and Riga Stradins University
Lithuania:	Ramunas Vilpisauskas, Associate Professor at the Institute of International Relations and Political Science, Vilnius University.
Hungary:	Gabor Bekes, Research Fellow at the Institute of Economics of the Hungarian Academy of Sciences
Poland:	Dr. Przemyslaw Wozniak, Research Economist and Member of the Council, CASE - Center for Social and Economic Research, Warsaw, Poland
Romania:	Liviu Voinea, Associate Professor National School for Political and Administrative Studies, Executive Director Group of Applied Economics
Slovenia:	Vladimir Lavrac, Senior Research Fellow, Institute for Economic Research

Project Team
Assya Kavrakova, EuPI, Open Society Institute – Sofia
Georgi Stoytchev, Executive director, Open Society Institute – Sofia
Boryana Klimentova, EuPI, Open Society Institute – Sofia

Copy Editor
Courtney Lobel

CONTENTS

Executive Summary	**6**
I. Country's Economic Convergence	**9**
1. Pre-accession	**9**
2. Since EU Accession	**11**
3. Since September 2008	**13**
II. National Goals and Strategies for the Euro Adoption	**15**
1. Before the Global Crisis	**15**
2. The Impact of the Global Crisis	**19**
III. Institutional and Policy Environment regarding the Euro adoption	**21**
1. Before the Global Crisis	**21**
2. The Impact of the Global Crisis	**23**
Conclusion: Progress, Perspectives, Recommendations	**24**
Appendix	**26**

EXECUTIVE SUMMARY

Bulgaria has been converging to the European Union (EU) for more than decade. Economic growth was increasing as well as the income per capita. Foreign direct investments (FDI) were rapidly increasing (especially around the time of accession) as well as bank credit. The government improved its fiscal position, started running surpluses and significantly cut the government debt. As a result, Bulgaria was fulfilled four out of the five Maastricht criteria prior to entering the EU. The fifth criterion – inflation – was higher exactly because of the fast convergence from a relatively low level (Bulgarian GDP per capita was the lowest in the EU, the same holds true for price levels).

The same development continued after the EU accession at an even higher pace. Government debt fell to 15% of GDP – one of the lowest levels within the EU — and the fiscal surplus policy continued. FDI reached a new high of more than 30% of GDP in 2007; external debt inflow also increased because of EU-optimism and tax reforms. Inflation peaked in 2008 because of the high international prices of food and oil. Financial integration also made advances – almost all banks were owned by EU banks, most FDI came from the EU, credits and deposits were increasingly in euro, as well as the foreign trade.

The crisis relieved inflationary pressure, but also decreased GDP growth, export, inflow of capital, import and industrial production, and halted the longtime trend of falling unemployment. Because of the high level of integration, the crisis impacted Bulgaria mainly from the direction of the EU. Banks in Bulgaria did not fail nor did they need a bail-out, because of their high level of capital and liquidity, but the real economy was badly hit. The economic cycle is also synchronizing (as far as it can between prosperous and poor countries).

Bulgaria set the goal for EU and euro area membership as early as 1997. Despite this dollarization and overall preference for the dollar, it was decided that under the currency board arrangement (introduced in mid-1997) Bulgarian lev would be fixed not to the dollar, but to the Deutsche Mark. This was a clear political and strategic decision connected with the willingness of Bulgaria to enter and integrate into the EU.

In 2000 Bulgaria entered negotiations with the EU on Chapter 11 "Economic and Monetary Union". The Bulgarian position was that the country not only agrees that it will become member of the euro area, but will target membership as early as possible because this was a high priority for the government. This position was confirmed by two subsequent governments.

In 2004, the government and the Bulgarian Central Bank (BNB) signed an agreement for the introduction of the euro in Bulgaria. Again, the goal was to implement the fastest possible accession scheme. The government and the Bulgarian National Bank intended to apply for joining the interim stage of the Exchange-Rate Mechanism II (ERM II) immediately after the date of Bulgaria's official EU membership. According to the agreement, the ERMII period should be based on the principle that the currency board would be kept at the same exchange rate until entry into the euro area. In addition, the ERMII period would be kept at minimum by "promptly taking all the necessary steps under the procedure for membership in the euro area".

The government and the Bulgarian National Bank prepared for the challenges of participation in the ERMII and euro area accession and were therefore able to achieve substantial progress in fiscal and institutional strengthening. The economic environment was positive but when difficult decisions had to be made, they confirmed the real priority of euro area membership. For more than a decade, quick euro area entry has been a goal for three different governments. However, it could not be achieved in Bulgaria owing to external issues.

In early 2007 – just after Bulgaria's entry into the EU – it was understood that there are entry barriers to ERMII participation and that countries cannot enter when they decide they want to (unlike the case with previous countries). This, of course, raised questions about unequal treatment of willing members before and after 2006. The ECB said that, in the case of Bulgaria it is worried because of the current account deficit and inflation.

After negotiations, in mid-2007 there is agreement that Bulgaria will enter ERMII, but prior to that the government will have to approve commitments to economic policy that will ensure that it will not follow risky policy (they include requirements for macro stability and structural reforms to increase the flexibility and competitiveness of the economy). The format of these commitments is the same as the International Monetary Fund (IMF) program; they even have the same name - a letter of intent. The government approved the commitments after consent was given by the political parties in the triple coalition (all this happens in a manner of secrecy as EU institutions are not willing to say publicly that they want to play an IMF-like role in countries willing to enter ERMII).

Ultimately, this didn't help either, because the subprime crisis in the United States and ensuing uncertainty made the ECB more cautious. The government decided not to challenge the ECB and risk a possible refusal. In the months that followed, scandals broke regarding the allocation of EU funds in Bulgaria, and the criticism by the EU increased as it related to corruption, the judiciary and police - which put the Bulgarian government in an even weaker position. The policy of rapid accession to the ERMII was forgotten and deprioritized.

Despite prioritizing ERMII participation and euro area membership, Bulgaria was unable to achieve either of them. The informal changes of the rules for euro area entry that was later supported by the uncertainty stemming from the US subprime crisis made the task more difficult than before. In addition, the unwillingness of the Bulgarian authorities to challenge the ECB and, later, the loss of credibility because of the problems with EU funds determined the result. The goal for fast entry in the euro area was not achieved. Nevertheless, the conservative fiscal policy was adequate not only for fulfilling the Maastricht requirements, but for enhancing overall stability – especially since the financial crisis began.

If countries are kept outside the ERMII for too long, they may decide they no longer are willing to participate. New UKs and Swedens will be created thus limiting the euro's sphere. Therefore, EU should either introduce clear criteria or allow free entry into ERMII to all willing. The Maastricht Treaty could be also reviewed as the criteria were designed in the early 1990s when the EU was two times smaller than its current size, and member countries had similar income and price levels, and rates of economic growth. Another option is a bing-bang enlargement of the euro area - all willing member states to enter immediately. Unilateral euroization is also not out of sight.

The most practical of all these scenarios is to free ERMII entry for all willing countries and then following the Maastricht criteria, loosening the inflation criterion somewhat if needed. This can both take into account the geopolitical interest of the euro area to enlarge and also the interest of keeping stability by following rules. On the other hand, it will take into account the interest of new member states to enter and will also help them somewhat during the crisis.

I. Country's Economic Convergence

1. Pre-accession

Prices

With the exception of the year 2003, Bulgaria's inflation rate has been well above the euro area and above the rate stipulated by the Maastricht criterion. After the high inflation of the early 1990s and the hyperinflation of 1996-97, the currency board arrangement[1] reduced inflation dramatically to reach its lowest rate in 2003 when average annual HICP[2] inflation was only 2.3%. In the three years prior to entering the EU, the inflation rate was consistently above 6%, reaching 7.4% in 2006.

The consistently higher inflation rate in Bulgaria compared to the EU in the last decade was not temporary. The price level in Bulgaria is the lowest within the EU (41% in 2002 and 45% in 2006). The same holds true for GDP per capita in Bulgaria. The convergence in the income and GDP per capita – a result of strong GDP growth – is keeping inflation higher as prices also tend to converge along with incomes. GDP growth in the three years before accession increased to above 6% in real terms, much higher than in the EU.

Budgetary position

In 2002, the budget had a small deficit – only 0.8% of GDP. Since 2003 – when the budget was balanced – the government started running budget surpluses. They increased from 1.7% GDP in 2004, to 3.5% of GDP in 2006. Budget spending was capped at 40% of GDP by the government.

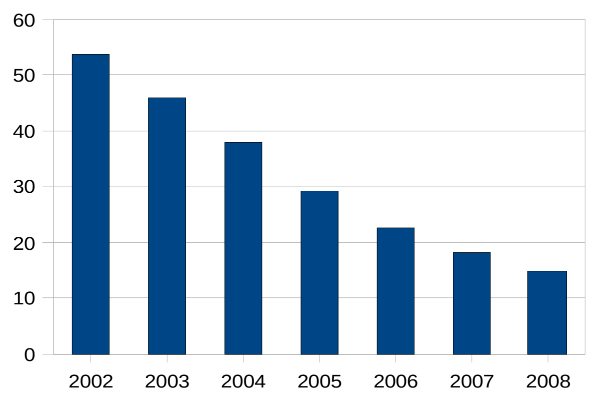
There were budget outruns as budget revenues were projected conservatively. In addition, the inflow of capital changed the structure of tax revenues (higher share of VAT on imports). The tax reforms, which significantly decreased the rates of direct taxes, also helped to increase compliance, and decreased the incentives for tax evasion.

Government debt decreased from more than 50% of GDP in 2002 to about 20% of GDP in 2006. This was part of a longer trend, as government debt was about 170% of GDP on average during the 1990s and increased even more during the crisis of 1996-97. Economic growth since then and the repayment of loans led to a continuing decline of the government debt burden. Loan repayments were made mainly using privatization revenues and budget surpluses.

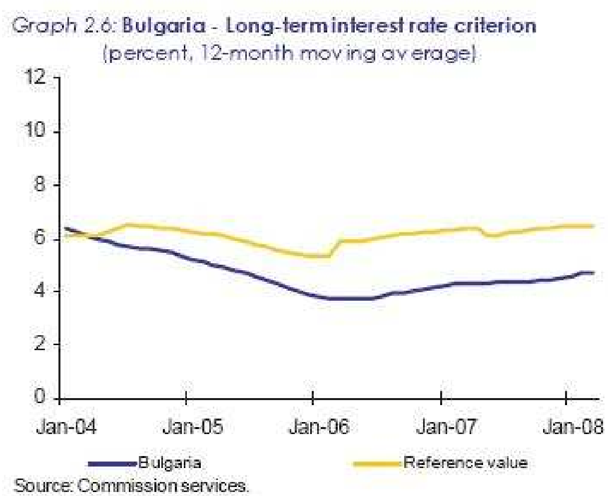
[1] Currency board is a fixed exchange rate determined by law with full backing of the local currency with foreign reserves. The central bank is obliged to exchange local currency into foreign currency and vice-versa with no limitations. The central bank cannot intervene in any other way on the markets.

[2] HICP stands for Harmonised Indices of Consumer Prices. The HICPs are economic indicators constructed to measure the changes over time in the prices of consumer goods and services acquired by households. The HICPs give comparable measures of inflation in the euro-zone, the EU, the European Economic Area and for other countries including accession and candidate countries. They are calculated according to a harmonised approach and a single set of definitions. They provide the official measure of consumer price inflation in the euro-zone for the purposes of monetary policy in the euro area and assessing inflation convergence as required under the Maastricht criteria.

Government debt: % of GDP



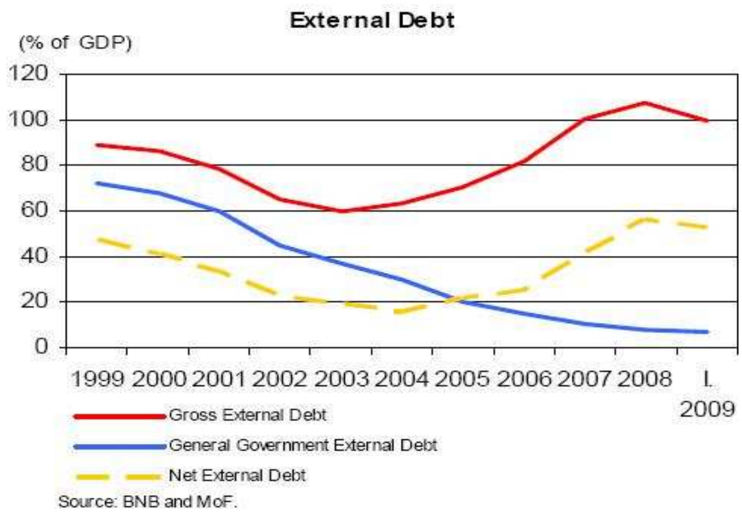
Bulgaria fulfilled both of the fiscal criteria from Maastricht[3] as early as 2002. Since then these indicators have been improving – budget is at surplus and government debt is lower. Long-term interest rates on government bonds have also been within the Maastricht requirements since 2004. The interest rate spread on government long-term bonds between Bulgaria and the euro area fell dramatically – from more than 300 basis points in 2002 to practically zero in some periods of 2006-07.



External sector

Gross external debt fell rapidly from the end of the 1990s until 2003 because of a decrease in the public debt. Then it started increasing because of the inflow of funding – through banks (that had been privatized by big European banking groups) and through the corporate sector that could get external financing because of the stabilization of the economy and improved credit rating. Nevertheless, before joining the EU in 2006, external debt was still lower than in 1999.

[3] Budget deficit should be no more than 3% of GDP and government debt should be lower than 60% of GDP.



Net external debt (gross external debt minus foreign reserves) followed a similar pattern. It fell from almost 50% of GDP in 1999 to less than 20% of GDP in 2004. Then it started rising, following the gross debt. Still, in 2006 it was less than 30% of GDP.

Current account deficit rose significantly from 2.4% of GDP to more than 18% of GDP in 2006. The main reason for the deficit is the rapid increase of the investment activity that could not be financed by local savings (they remained broadly stable). Strong investment growth was financed by FDI that more than covered the current account deficit. FDI rose from 5.9% of GDP in 2002 to 24.4% of GDP in 2006. The EU's share in the FDI inflow was rising from about two thirds in 2002 to 84% in 2006.

The current account deficit was not a result of a decrease in competitiveness of the Bulgarian economy. Exports were growing every year with an accelerating pace. Export growth was 6% in 2002 and increased to almost 27% in 2006. Also, Bulgaria's share in world trade and EU imports was increasing. From 0.35% in 2002 Bulgarian exports share in total EU imports increased to 0.5%[4]. More than 50% of exports went to EU countries between 2002-06 (although the EU's share of exports decreased slightly in 2005 and 2006). The exchange rate was stable because of the currency board.

Economic and Financial Developments

The growth of GDP increased form 4.5% in 2002 to above 6% since 2004. GDP per capita increased from 31% of EU average in 2002 to 36.5% of EU average in 2006. Although Bulgaria was not among the fastest converging countries, its growth was not slow. Employment (aged 15-64) increased significantly from 50.6% in 2002 to 58.6% in 2006.

Credit growth was fast but from a low level. Between 2002-2004 credit increased by 44-48% per year. In 2005 and 2006 it decelerated somewhat to 32% and 24% respectfully. Credits denominated in euro increased their share from 34% in 2003 to 43% in 2006. Euro-denominated deposits also increased from 25% to 39%. Monetary aggregates also showed double-digit growth every year. Stock market index was growing by 30-50% per year.

[4] Republic of Bulgaria, Convergence program, 2008-2011

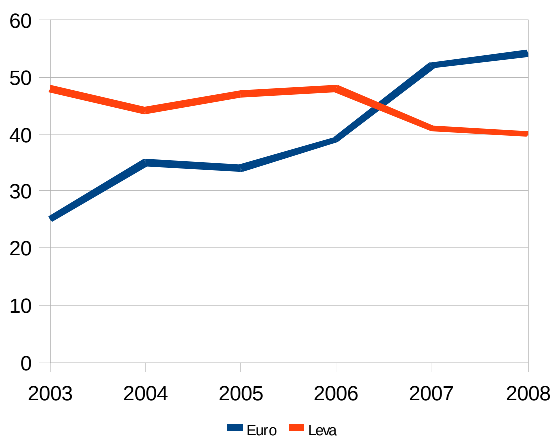
2. Since EU accession

Inflation did not change much in 2007 when Bulgaria entered the EU; the rate was 7.6%. In 2008 average annual inflation rate reached 12%, but started to fall rapidly after the summer of 2008. The annual inflation rate peaked at 14.7% in June 2008 (compared to the same month of the previous year) and went down each successive month. The inflation peak in 2008 was mainly a result of the increase in food and energy prices on the international markets (a bad harvest in 2007 also contributed to this development). This was a temporary phenomenon that dissipated after oil and food prices fell in late 2008.

The budget situation did not change after Bulgarian entry in the EU. Budget surplus was 3.5% of GDP in 2007 and 3% in 2008. Tax system reforms continued as direct taxation was cut and indirect taxes were increased (mainly because of EU-required changes in excises duties). Lower direct taxes led to higher revenues in the budget as they increased compliance. Government debt fell to less than 15% of GDP. Long-term interest rates continued to fulfill the Maastricht requirement.

Gross and net external debt continued increasing as tax reforms and EU entry increased optimism. FDI also increased significantly reaching almost 30% of GDP in 2007. That inflow of capital also drove the current account deficit above 25% of GDP both in 2007 and 2008. FDI from EU members reached 88% of GDP in 2008, trade with EU also increased – share of exports to EU increased to more than 60%, and for the first time imports were mainly from EU countries in 2007 and 2008. Exports continued growing at double digit rates until September 2008.

Share of deposits denominated in Euro and Leva in the banking system



Source: BNB

GDP growth continued at more than 6% per year in 2007 and further increased to 7% in the first three quarters of 2008. GDP per capita increased to almost 40% of EU average in 2008. Employment was increasing faster and reached 64% in 2008, very close to the EU average level. Unemployment fell to historic lows and labor shortages started to increase wages faster. Credit growth accelerated in 2007 to 62.5% year on year and the central bank had to take measures to slow it; this tactic became effective in the beginning of 2008. EU banks controlled more than 81% of the banking system in 2008 and the share of Euro-denominated loans and deposits increased to more than 50% in 2007 and even higher in 2008. Thus, Bulgaria follows the path of other countries that joined EU earlier.

Basically, after EU entry the economy continued to converge at an even faster rate. Only the stock exchange index suffered at the end 2007 and 2008 because of the financial crisis. But the overall economy was doing well.

The 2008 Convergence report5 was the first for Bulgaria. According to the report:

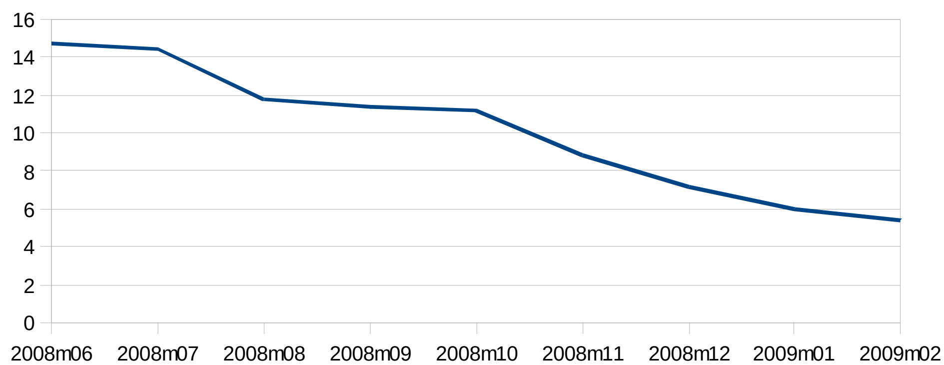
- Bulgarian legislation is not fully prepared for euro adoption.
- Bulgaria does not fulfill the criterion on price stability as inflation is higher than reference value.
- Bulgaria fulfils the criterion on the government budgetary position as government debt is low and declining and budget is on surplus.
- Bulgaria does not fulfill the exchange rate criterion as the country is not part of ERMII. However, according to the Convergence report "The currency board remains well supported by official reserves, which increased robustly in recent years."
- Bulgaria fulfils the criterion on the convergence of long-term interest rates.

In addition, the report examined the external position. According to the report, the external deficit of Bulgaria widened significantly to 20% of GDP in 2007, reflecting consumption and investment that expanded rapidly in the context of catching-up. Its size has clearly surpassed a level that can be considered sustainable in the medium term, implying that a considerable adjustment will be required over time. The external shortfall has been fully financed by FDI inflows, amid positive investor sentiment. Given the high level of external debt, Bulgaria's external position implies significant financing needs in the medium-term. The Bulgarian economy is highly integrated with the EU.

3. Since September 2008

After peaking at 14.7%, in mid-2008 inflation started to slow as oil and food prices started to fall. This drop intensified after October 2008 when the crisis started to affect Bulgaria. In February 2009 the annual rate reached 5.4% and this downward trend is not expected to stop until at least the second half of the year.

HICP inflation rate, annual



Source: Eurostat

Budget surplus was already high in September-October 2008, but the government spent half of it from November to December and the year finished with 3% of GDP surplus. Still, revenue slowed at the end of 2008 and in the first months of 2009. Nevertheless, in the first two months of 2009 the government was still running a budget surplus, and the

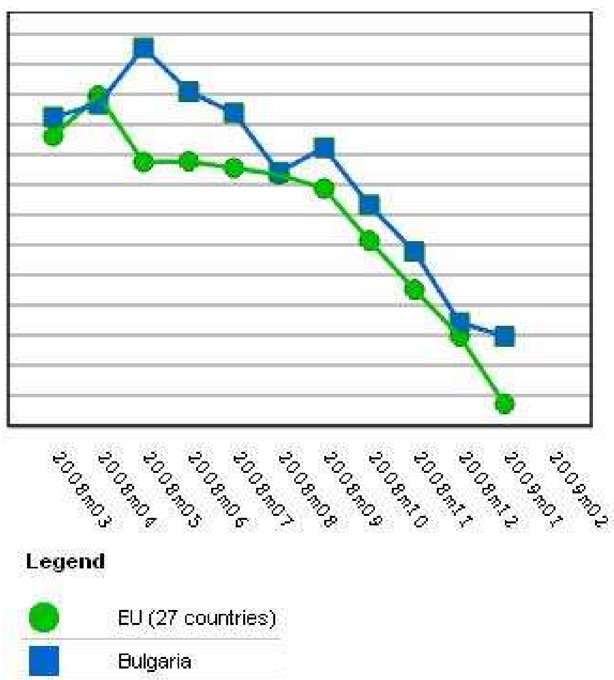
[5] European Commission, DG ECFIN, *Convergence Report 2008*, European Economy 3, 2008

budget is targeting surplus for the end of the year.

Gross and net external debt continued increasing for a few months and then started declining in December 2008 and January 2009 as a result of the worsened external financial markets. FDI started decreasing, but current account deficit also decreased rapidly in the first month of 2009 confirming the flexibility of the economy. Both exports and imports were declining.

GDP growth slowed by half to 3.5% in the forth quarter of 2008 compared to 7% in the first three quarters. Industrial production slowed and then started decreasing on an annual basis – following similar developments in the EU. In January 2009 it was 12% lower compared to a year earlier. Unemployment started edging up, and credit growth almost stopped on a monthly basis, as credit and deposit interest rates increased to levels unknown for four to five years. The interest rate spread on government long-term bonds between Bulgaria and the euro area increased rapidly – from 39 basis points (BP) in mid 2008 to more than 400 BP at the end of the year (with some improvement in the beginning of 2009). Stock exchange index plunged even faster after September 2008 and fell by three-fourths within six months until March 2009.

Industrial production, annual rate



Source: Eurostat

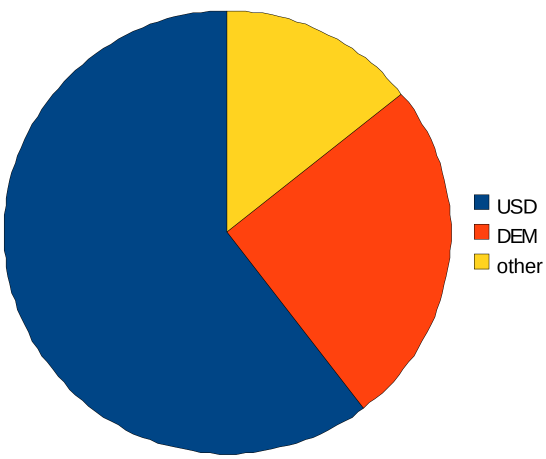
Over the years, both before and after the inception of Bulgaria as an EU member, the financial and economic integration with the rest of the EU strengthened significantly. Because of this high level of integration the crisis came in Bulgaria mainly from EU. Banks in Bulgaria did not fail nor did they need a bail-out, because of their high level of capital and liquidity, but the real economy was badly hit. Since most foreign trade, banks and FDI were connected with the EU, these were the channels that transferred the crisis. Export and import declined, FDI slowed and bank credit growth almost stopped. The economic cycle is also synchronizing (as far as it can between prosperous and poor countries).

II. National Goals and Strategies for the Euro Adoption

1. Before the Global Crisis

Early decisions During the period of hyperinflation, a severe banking and economic crisis in 1996-1997 resulted in a decrease in trust in the Bulgarian lev to reach very low levels and the dollar was the preferred currency for hoarding, saving and many contracts (such as real estate deals etc.). The dollar exchange rate was also the most cited economic indicator in the media, all central bank reserves as well as foreign debt and trade were calculated and mostly denominated in dollars. Thus, there was practical dollarization in Bulgaria.

Currency Structure of Exports in 1999



Source: BNB

Despite this dollarization and preference for the dollar, it was decided that under the currency board arrangement (introduced in mid-1997) the Bulgarian lev would be fixed not to the dollar, but to the Deutsche Mark. This was a clear political and strategic decision connected with the willingness of Bulgaria to enter and integrate with the EU. At this time, this was not an obvious decision (the euro did not even existed)[6].

According to the World Bank:

> *The exchange rate was fixed prior to the CBA introduction on the basis of the prevailing market Bulgarian Lev (BGL)/Deutschemark (DM) exchange rate. The choice of the reserve currency was made after a period of public debate amongst economists and politicians. Three different options were considered: the USD, DM and a basket of the two currencies. Taking into consideration the European Union (EU) accession strategy of the newly elected Government led by Prime Minister Kostov, the choice was made in favor of the DM[7].*

---

[6] See analysis and discussion on the choice in Yotzov, V., and N. Nenovsky, "Choice of a Reserve Currency and Fixing of the Exchange Rate at the Introduction of the Currency Board Arrangement", BNB Monthly Bulletin, 4/1997

[7] World Bank, *Bulgaria's Currency Board Arrangement* <http://go.worldbank.org/BSLSMME4S0>

This is the opinion of the Central Bank itself[8]:

> *Bulgaria has chosen the Deutschemark as a reserve currency (and as of 1 January 1999: the Euro). This choice is strategic. It reflects Bulgaria's will to converge Europe and facilitates future Bulgarian accession to the European Union and affiliation to the European Monetary Union.*

Under the Bulgarian National Bank law (adopted in 1997) the reserve currency of the currency board would be changed from Deutsche Mark to the euro when the euro was introduced. According to the law[9]:

> *Article 29. (2) When the euro becomes legal tender in the Federal Republic of Germany, the official exchange rate of the lev to the euro shall be determined by multiplying the exchange rate as per para. 1 by the official exchange rate of conversion of the Deutschemark to the euro. Thus established exchange rate shall be published by the Bulgarian National Bank in the Darjaven Vestnik.*

As early as 1997 the choice was made that Bulgaria would target membership in the EU and then membership in the Monetary Union as well as economic integration. The whole monetary system was linked to the EU despite the previous preference for dollars. Through the currency board, the country transferred a big part of its monetary sovereignty to the German Central Bank and later, to the European Central Bank (ECB).

The currency board was perceived as a step toward eventual entry in the euro area and the entry into the euro area has always been perceived as the only exit strategy from the currency board. This has been the consistent position through the years. As early as 1999, the Bulgarian National Bank insisted that the currency board was a tool for achieving rapid convergence and should be kept in the ERMII (if participation in the ERMII could not be avoided)[10].

Euro adoption strategy

In 2000, Bulgaria started negotiations with the EU on Chapter 11 "Economic and Monetary Union". The Bulgarian position was that the country not only agrees that it will become member of the euro area, but will target membership in the EMU as early as possible because the entry into the euro area was a priority for the government[11].

The new Bulgarian government, elected in 2001, confirmed that euro area entry was a priority. It declared that its economic policy would targeted faster entry into the euro area[12].

In 2004 the Government and the Central Bank signed an agreement for the introduction of the euro in Bulgaria[13]. The agreement had ambitious targets for rapid accession.

---

[8] BNB, Annual Report, 1997

[9] Law on the Bulgarian National Bank (Adopted by the 38th National Assembly on 5 June 1997; published in the Darjaven Vestnik, issue 46 of 10 June 1997; amended, issues 49 and 153 of 1998; issues 20 and 54 of 1999; issue 109 of 2001; issue 45 of 2002; issues 10 and 39 of 2005; issues 37 and 59 of 2006: in force on the date of entry into force of the Treaty of Accession of the Republic of Bulgaria to the European Union; issue 108 of 2006; issues 52 and 59 of 2007)

[10] *Currency board and EMU – a Bulgarian perspective*, Presentation by Mr. Svetoslav Gavriiski, Governor of the BNB at the Seminar on The Accession Process organised by the ECB and the Bank of Finland, Helsinki, 10 - 12 November 1999

[11] Bulgaria, Negotiation Position on Chapter 11, Conference on EU accession of Bulgaria, Brussels, October 24, 2000, CONF-BG 43/00

[12] Bulgaria, Negotiation Position on Chapter 11, Conference on EU accession of Bulgaria, Brussels, November 26, 2001, CONF-BG 77/01

[13] *Agreement between the Council of Ministers and the Bulgarian National Bank on the introduction of the Euro in the Republic of Bulgaria*, 25 November 2004

The Republic of Bulgaria shall adopt and fully comply with the European legislation and practices until its accession to the euro area, respectively until the introduction of the Euro, implementing a strategy for the fastest possible accession. The Government and the Bulgarian National Bank intend to apply for joining the interim stage of the Exchange-Rate Mechanism II (ERM II) immediately after the date of Bulgaria's official EU membership. Upon the fulfilment of the commitments provided for in this Agreement, we expect that in the second half of year 2009 or on 1 January 2010, Bulgaria will join the euro area, and the BNB – the Euro system.

According to the agreement, the period of ERMII participation should be based on the principle that the currency board would be kept at the same exchange rate until Bulgaria's entry into the euro area. In addition, the ERMII period would be kept at minimum by "promptly taking all the necessary steps under the procedure for membership in the euro area".

The agreement stipulates specific obligations for the Government and the Central bank.

The Council of Ministers undertakes:

- First, in accordance with the commitments taken during the negotiation process, to prepare and submit for discussion and approval to the National Assembly all required laws relating to Bulgaria's participation in the EMU;

- Second, to follow a principled policy of a balanced budget on a consolidated basis until Bulgaria's membership in the EU and its participation in the ERM II.

- Third, during its participation in the ERM II, not to propose changes in the indirect taxes and administered prices, which would lead to higher inflation, other than the commitments made in the negotiations process with EU and in the PEP;

- Fourth, to develop the necessary institutional and analytical capacities that would ensure the country's full-fledged participation in the process of co-ordination of EU member countries' economic policy, and for drawing on the Structural Funds and the Cohesion Fund.

- Fifth, from the time Bulgaria joins the euro area, to pursue a consistent principled policy based on compliance with the requirements of the Stability and Growth Pact.

The Bulgarian National Bank undertakes:

- First, to contribute to the maintenance of the existing currency board regime until Bulgaria's EU membership and during the time of its participation in ERM II.

- Second, to the time of this country's membership in the euro area and its own membership in the Euro system, to develop the necessary institutional and administrative capacities for full-fledged participation in the process of designing and implementation of the monetary policy of the Community.

<http://www.bnb.bg/bnb/home.nsf/vPages/Release_20041125/$FILE/agreementfinal1-EURO-MS-eng.pdf>

- Third, to invest in the development of a secure and efficient technological infrastructure, which would allow for:
  - Full-fledged participation in the process of implementation of the Community's monetary policy;
  - Management of the international reserves made available by the ECB;
  - Integration of the national payment system into the European one.

- Fourth, to ensure reliable and efficient arrangements for the changeover from the Lev to the Euro from the time of euro area accession, as well as for the smooth distribution of the Euro and its protection against counterfeiting in compliance with the ECB requirements.

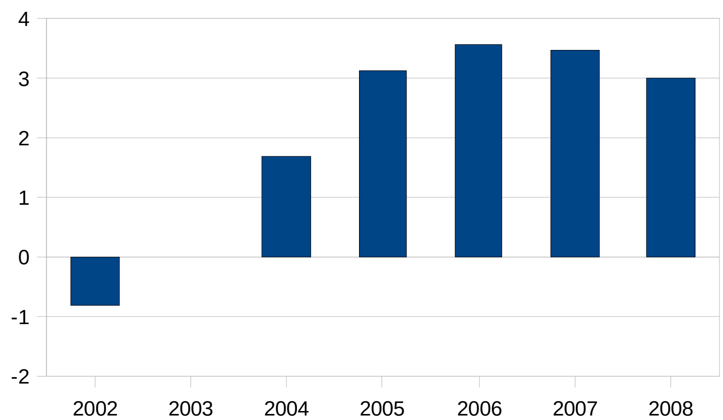
- Fifth, to perform its supervision function targeting its efforts into two main directions:
  - Preparation and introduction of the European *acquis communitaire* in the area of banking;
  - maintaining a high degree of stability in the banking system, adequately serving the growing banking intermediation, and the free competition of EU financial institutions.

The new government in 2005 confirmed the goal of rapid entry into the euro area. In the program of the government[14] it is explicitly written that Bulgaria will enter ERMII immediately after the start of EU membership. In connection with this goal, the government confirms the goal for a balanced budget and keeping the currency board until euro area membership is granted.

Implementation

In 2003 the government achieved a balanced budget and since 2005 it is running a budget surplus above 3% of GDP per year. Government debt is rapidly declining, reaching all-time lows. Thus, on the fiscal side the goals have been achieved.

Budget balance, % of GDP



Source: Ministry of Finance, BNB

In 2006 the government decided to increase excise duties in advance – and to reach the EU minimum level faster than projected. The reasoning behind this decision was that it will increase inflation in 2006, and will then decrease the inflation pressure on the economy in 2007 when Bulgaria was expected to enter the EU and the ERMII soon

[14] *Program of the Government of European Integration, Economic Growth and Social Responsibility*, November 23, 2005 <http://www.government.bg/cgi-bin/e-cms/vis/vis.pl?s=001&p=0037&n=9&g= >

thereafter. The goal was to help the economy achieve lower inflation within the ERMII period in order to fulfill the inflation criterion and join euro area as soon as possible[15]. This was not an easy decision, but it was taken and supported in this way the fulfillment of the Maastricht criteria.

At the same time, the currency board arrangement continued to bring exchange rate stability. Interest rates continued to converge toward EU levels, including long-term rates. Thus Bulgaria was consistently fulfilling all of the Maastricht criteria (with the exception of inflation) even before entering the ERMII.

The Bulgarian National Bank was also preparing for ERMII participation and euro area entry. The bank approved a "Strategy for Bulgarian National Bank Development between 2004 and 2009"[16]. The explicit goal of the strategy was to address the challenges of EU membership and the integration into the euro area. Through the implementation of this strategy, the Bulgarian National Bank was able to develop capacity for participation in the Euro system and to prepare the institution for the euro area membership. The Bulgarian National Bank drafted all the required laws to harmonize the Bulgarian banking and financial laws with the EU's acquis communitaire[17].

The Government and the Bulgarian National Bank prepared for the challenges of ERMII and euro area participation and were able to achieve substantial progress in fiscal and institutional strengthening. The economic environment was positive but when difficult decisions had to be made, they were made to confirm the real priority of euro area membership. For more than a decade, rapid euro area entry has been a goal for three different governments.

However, in early 2008 when the government could not enter the ERMII for more than a year, quick euro area entry was silently deprioritized. At this time serious problems with Bulgaria's administrative capacity emerged in connection with the absorption of European funds. In addition, the European Commission was more and more critical of the slow pace of reforms in the sphere of internal order and security. Some EU pre-accession funds were frozen, others were permanently lost. The ERMII entry was forgotten for the whole of 2008.

2. The Impact of the Global Crisis

ERMII entry was revived as a priority only after the first effects of the crisis reached the Bulgarian economy at the end of 2008 and in the early months of 2009. After September 2008 the positive view of Eastern Europe on the part of investors was revisited and the inflow of foreign capital started slowing. Bulgaria's credit rating was downgraded, banks sharply reduced new lending and export declined; interest rates increased.

The euro area was appealing again as it was increasingly seen as safe heaven for small open economies. Even a country with a currency board and fixed exchange rate like Bulgaria stands to benefit significantly from the introduction of the euro in terms of stability and trust and, thus, lower interest rates. It is no surprise that ERMII participation again became a priority.

In the beginning of March 2009 the prime minister of Bulgaria participated in the informal meeting of EU leaders and posed the issue of quick entry into the ERMII

[15] See for example „*Pressconference of the Prime Minister on the First Year of the Government*", August 23, 2006 <http://www.government.bg/cgi-bin/e-cms/vis/vis.pl?s=001&p=0043&n=000019&g= >
[16] BNB, *Strategy for Bulgarian National Bank Development between 2004 and 2009,* Sofia, September 2004 <http://www.bnb.bg/bnb/home.nsf/vPages/BNB_strategy/$FILE/BNBStrategy-04-09-e.pdf
[17] BNB, Annual Report, 2006 <http://www.bnb.bg/bnb/home.nsf/vPages/periodic_AnualReports_2006/$FILE/2006_P_AReport-en.pdf>

mechanism, which precedes euro area entry[18]. According to the prime minister, participation in the ERMII would support reforms and confirm the financial and macro stability of the country. He stressed that Bulgaria fulfils four out of five Maastricht criteria even before entering the ERMII. We do not want a change of criteria, the prime minister stressed at a subsequent speech, we just want to enter the ERMII and fulfil the criteria.

Surprisingly, the finance minister was not so keen on supporting adoption of the euro as a top priority. According to him, there is no reason to rush. As long as the finance minister is the one who is responsible and the one who should undertake the technical preparations, this may be seen as a sign that fast entry is out of reach (or that he is unwilling to give it another try). According to a TV interview with one of the economic experts of one of the parties from the ruling coalition, finance minister did not start formal or informal procedure for consultations with other EU countries on ERMII entry. The absence of coordination between the Prime Minister and the Minister of Finance is presenting Bulgaria as a country that doesn't know what it is doing and thus lowering the chances for a fast entry in ERMII.

Still, government target for budget surplus in 2009 and next years as well as the low level of debt, the rapidly falling inflation, the sharp decline of the current account deficit and the stable exchange rate because of the currency board are creating a unique opportunity for Bulgaria to enter the Euro area. Paradoxically, the crisis increases the chances to fulfil the Maastricht criteria. This opportunity should not be missed.

The next government – if stable and with clear Parliamentary support, have more chances to achieve ERMII entry, especially if other problems with the EU institutions are also solved and different institutional players in Bulgaria manage to avoid public arguments between themselves and work in a coordinated fashion.

[18] Bulgarian Government, Press Release, March 1, 2009 <http://www.government.bg/cgi-bin/e-cms/vis/vis.pl?s=001&p=0011&n=1352&g=%20Г,Вµ>

III. Institutional and Policy Environment regarding the Euro adoption

1. Before the Global Crisis

For years Bulgaria was preparing for immediate entry into the ERMII right after its entry into the EU and then fast entry into the euro area. The Baltic countries and Slovenia were regarded as the example to follow – they became members of the ERMII less than two months after they entered the EU in May 2004. It seemed that the difficult part will be within the ERMII (fulfilling the last Maastricht requirement - inflation) as there were no barriers to entry in the ERMII itself. This expectation turned out to be wrong.

In early 2007 - after the entry of Bulgaria into the EU – it was understood that the process of ERMII entry would not be as easy for new candidates as it has been on previous occasions. This, of course, raises some questions about unequal treatment (although some may argue that ERMII entry has always been a game without clear rules). While European institutions argue that the Maastricht criteria may not be changed because of the "equal treatment" principle, at the same time they quietly altered the procedure for entry into ERMII, doing exactly the opposite of equal treatment.

Formally and informally, the European Central Bank said that in the case of Bulgaria it is worried because of the current account deficit and inflation. These imbalances, says the bank, will have to adjust and the adjustment may be disorderly – and this may put the confidence in the mechanism ERMII at risk and may discredit it. This is clearly changing the criteria (note that the Maastricht criteria does not include current account and that they should be fulfilled after ERMII entry, not before). In addition, countries with much weaker macroeconomic indicators have been accepted not only in the ERMII but also in the euro area. Even currently there are countries in the euro area that do not fulfill the criteria for budget deficit and government debt - which Bulgaria has fulfilled for years.

After negotiations, in mid-2007 an agreement was reached that provided for Bulgaria's entry into the ERMII, but before that the government will have to approve policy commitments for economic policy to ensure that it will not pursue risky policies (they include requirements for macro stability and structural reforms to increase flexibility and competitiveness of the economy). The format of these commitments is the same as the IMF program; they even have the same name (a letter of intent). The government approved those commitments after approval by the political parties in the triple coalition (all this happens in a manner of secrecy as the EU institutions are not willing to say publicly that they want to play an IMF-like role in countries willing to enter the ERMII mechanism).

This started the actual process of accession for Bulgaria to the ERMII. The European Commission prepared a report on the accession of Bulgaria, which is neutral, but still positive for Bulgaria. A meeting of deputy finance ministers from 27 countries expressed no disagreement with Bulgaria's membership in the ERMII. There was informal confirmation from the Euro group that Bulgaria will be accepted. It looks like Bulgaria is ready to enter and start the two year period before adopting the euro. In a sign of goodwill, Bulgaria is among the first countries that supported the new European Treaty of Lisbon and expects the same favorable treatment from their European partners (although it was suggested that the country should not support the treaty before being accepted into the ERMII as this is its right).

But this time again the expectations were not justified. At the end of 2007 senior representatives of the ECB made public comments against currency boards in Eastern Europe, despite the ECB's official position that currency boards are consistent with the procedure for entry into the euro area[19]. Immediately after signing the Treaty of Lisbon, Bulgaria learned that most likely it will not be allowed to enter into ERMII. Later it became clear that the ECB threatened to use its right of veto if Bulgaria asked to become a member of ERMII. This information appeared even in newspapers at the time[20]. Again, the problems cited were the external imbalances (despite the policy commitments that addressed these issues). Inflation was also indicated as a problem, despite its temporary nature as a result of the high prices of fuel and foodstuffs. All this information leaked from the EU institutions and markets knew about it (creating some damage for Bulgaria, although rather small as fundamentals were strong).

What changed the ECB's position between mid 2007 and the end of 2007? The explanation is the start of the subprime crisis in the US and rising uncertainty. The ECB believed that Eastern European countries were more vulnerable than those in the West (that proved to be an erroneous assumption).

At this moment, there are two options. The first is to submit an application for ERMII to see if the ECB really wants to use its right of veto. In previous situations - on the issue with the spelling of the euro in Bulgarian – the ECB insisted on its opinion but Bulgaria was able to win the battle and the Euro would be spelled in Bulgarian according to Bulgarian standard and not under the standard created by bureaucrats from Frankfurt. In other words, the idea is that the ECB will not dare to use its veto because it would mean a formal confirmation that the rules for entry into ERMII have changed – criteria were introduced that do not exist in the regulations and new countries are treated differently than the old member states.

The second option is do nothing, to wait for a period of one year and then to try again. The ECB indicated that after one year it may reconsider its position. The government chose the second option, not to risk a possible refusal. The argument is that this could negatively affect the markets - although they already knew that we were not accepted, despite the supposed "secret" nature of the process, information was leaking. Rather, the reason is political, the government was afraid of not been rejected – the first year of EU membership had already been difficult. Plainly, the decision was made based on the insufficient courage of politicians.

In the months that followed, scandals broke about the spending of EU funds in Bulgaria, and the criticism from the EU increased on corruption, the judiciary and police that put the government in a particularly weak position. It started losing the trust of other countries and did not have the possibility to trigger diplomatic and political mechanisms for ERMII entry. The policy of rapid accession to the ERMII was forgotten. The Minister of Finance formulated exactly the opposite policy in public statements. Since early 2008, the ministry of finance stopped efforts for ERMII entry and deprioritized this goal.

---

[19] See Policy position of the Governing Council of the European Central Bank on exchange rate issues relating to the acceding countries, 18.12.2003
„With regard to currency boards, the ECB does not consider them to be a substitute for participation in ERM II, implying that countries operating a currency board will be required to participate in ERM II for at least two years before the convergence assessment that is made before a country can finally adopt the euro. However, countries that operate a euro-based currency board deemed to be sustainable might not be required to go through a double regime shift, i.e. floating the currency within ERM II only to re-peg it to the euro at a later stage. Such countries may therefore participate in ERM II with a currency board as a unilateral commitment, enhancing the discipline within ERM II. However, the ECB has stressed that such an arrangement will be assessed on a case-by-case basis and that a common accord on the central parity against the euro will have to be reached." <http://www.ecb.int/pub/pdf/other/policyaccexchangerateen.pdf>
[20] Trichet, l'euro e la bolla che viene da Est, Corriere della Sera, 17.03.2008

2. The Impact of the Global Crisis

After the start of the crisis in September 2008 and especially in early 2009, the prime minister made a few statements on the need for a faster ERMII entry. Initially, this was perceived as a change of policy and, in effect, making ERMII participation a priority again. However, as far as can be seen, this is not the case as the finance minister seems not to be willing to invest efforts in this direction.

The current government is increasingly seen as lame-duck – so the remaining few months from the government's term are not stimulating any targeted efforts in this direction. In addition, there are no signs that the ECB changed its mind and thus the ministry does not have the incentives to change its policy of "no application – no rejection".

For Bulgaria, fast entry in to the euro area is still the best policy and will build on the currency board's success, bringing even more stability. But real efforts may need to wait until the next government takes office.

Conclusion: Progress, Perspectives, Recommendations

Despite prioritizing participation in the ERMII and targeting euro area membership, Bulgaria was unable to achieve these goals. The informal changes of the rules for euro area entry that was later supported by the uncertainty stemming from the US subprime crisis made the task even more difficult than before. In addition, the unwillingness of the Bulgarian authorities to challenge the ECB and their subsequent loss of credibility because of the problems with the spending of EU funds determined the result. The goal for rapid entry in the euro area was not successfully achieved.

Nevertheless, the currency board proved to be a successful mechanism for convergence and its contribution to the economic stability was even higher after the start of the financial crisis. Bulgaria's conservative fiscal policy was also adequate not only for fulfilling the Maastricht requirements, but for the overall stability – especially since the financial crisis began. Therefore, the economic policy for euro adoption was by no means unsuccessful, it proved to be the prudent policy even if euro adoption itself has not yet achieved.

However, keeping the currency board and prudent fiscal policy will eventually help Bulgaria to enter the euro area, especially if accompanied by diplomatic and political efforts (after all, ERMII entry is a political decision with no criteria). On the other hand, this path may prove too long with resulting political changes. For example, if a country is able to sustain its prudent macro policy for an extra decade outside the euro area, it may decide that euro area entry is not such a pressing priority. New UKs and Swedens[21] will be created thus preventing the creation of a full monetary union and lowering the chances that the euro will replace the US dollar as a global currency. After all, if EU institutions can keep willing members outside of the ERMII indefinitely (despite the Treaty), unwilling members can also keep themselves out of the ERMII indefinitely.

In the Bulgarian case, the geopolitical changes may be an additional reason to keep the currency board instead of entering the euro, as this allows for greater flexibility (for example, by changing the reserve currency in case of instability of the euro). If the currency board is able to serve the country well during so many crises, why change? In a decade the currency board in Bulgaria will be as old as it currently is in Hong Kong. Enough time to create political and public support for the lev that will rival – or even surpass - support for the euro.

If the EU is willing to avoid this scenario and if it is willing to show equal treatment, it has to make clear under what conditions a country can enter the ERMII. That is, it can either introduce clear criteria or allow free entry into ERMII to all willing EU members (as was the case before 2006). The second option is better, as this will be the real equal treatment.

However, if the ERMII stays practically closed and or criteria are introduced, this is unequal treatment. This opens the question for the Maastricht criteria also. If ERMII policy is changed (and it is), the policy on euro area entry should be also changed. The Maastricht criteria were designed in the early 1990s when the EU was two times smaller than it is now, and member countries had similar income and price levels and rates of economic growth – therefore they are inappropriate (especially the inflation criterion) to apply to the present situation where poorer countries are rapidly converging toward EU incomes.

The catch-up process is associated with higher economic growth and faster increase of

[21] UK and Sweden did not enter the Euro area as the public support for their own currencies is huge.

wages and prices. This leads to either appreciation of the exchange rate (for floating exchange rate regimes) or higher inflation rates (for fixed exchange rate regimes)[22]. Therefore, Maastricht criteria are outdated and should be changed (or their interpretation should be changed – for example, why is the inflation criterion measured against the three countries with the lowest inflation? The ECB inflation target is 2% but lower so this should be the ideal inflation rate, not the rate in the three countries with the lowest inflation).

Another option is a bing-bang enlargement of the euro area: all willing member states can enter immediately. That would discipline the fiscal policy and stimulate economic reforms as there would be no other way to promote adjustment (the market will punish governments that are not fiscally prudent by imposing higher interest rates). There cannot be any negative implications – the combined GDP of the new member states is too small a portion of the GDP of the EU. The current financial crisis provides an additional argument in this direction as it is increasingly understood that a single financial market can not work smoothly without a common currency (for example, what is the point of a floating currency in Romania if most deposits and credits are denominated in euro and thus any exchange rate movement may be detrimental to banking or corporate stability?). It should be kept in mind that by leaving some countries outside of the euro area their risk is not left outside – as far as euro area banks dominate their banking market the risk is directly transferred inside the euro area.

Unilateral Euroization is also not out of sight. It may be against the rules – but isn't ERMII closure also against the rules and unaligned with previous practice? If countries are left alone during the crisis and the ECB plays it safe by prioritizing only its own stability, but not allowing new countries to enter (which against the Treaty), it is an entirely plausible scenario that countries outside will also play safe and will euroize (also against the Treaty). It was during a crisis when Bulgaria introduced currency board – a new crisis can create enough political momentum for euroization (in 2007 the Bulgarian minister of economy publicly supported the idea for unilateral euroization).

The most practical of all these scenarios is free ERMII entry for all willing countries and then a following of the Maastricht criteria, loosening somewhat the inflation criterion, if needed[23]. This can both take into account the geopolitical interest of the euro area to enlarge and also the interest of keeping stability by following stated rules. On the other hand, it will take into account the interest of new member states to enter and will also help them somewhat during the crisis.

[22] See Georgi Angelov, Martin Zaimov, „*Big Bang Enlargement of the Euro area*", European Voice, January 2006
[23] It might not be needed as current crisis is lowering inflation anyway.

Appendix

Yearly data, 1999-2008 (for countries that joined EU in 2004); 2002-2008 (for countries that joined EU in2007)

	2002	2003	2004	2005	2006	2007	2008	2009
HICP (EU harmonized inflation index)	5.8	2.3	6.1	6	7.4	7.6	12	
Budget deficit/surplus - % of GDP (General Government Budget Balance)	-0.8	0	1.7	3.1	3.5	3.5	3	
General Government Gross debt, % of GDP	53.6	45.9	37.9	29.2	22.7	18.2	14.9	
Long-term interest rates (10-year government bonds) – end of year	8.26	6.42	5.25	3.8	4.01	4.42	5.81	
Exchange rate - % change against the Euro	0	0	0	0	0	0	0	
Price level compared to the EU average (Eurostat)	40.8	40.7	42	43.2	44.6	46.5		
GDP per capita at PPS as % of EU average (Eurostat)	31	32.5	33.7	34.5	36.5	37.3	39.7	
GDP growth	4.5	5	6.6	6.2	6.3	6.2	6.0	
Employment rate (15-64)	50.6	52.5	54.2	55.8	58.6	61.7	64	
Export growth	6.10%	9.98%	19.75%	18.55%	26.89%	12.49%	13.07%	
Current account - % of GDP	-2.4	-5.5	-6.6	-12.4	-18.4	-25.1	-25.3	
FDI - % of GDP (+ % of FDI coming from EU countries, if data exist)	5.9	10.5	13.8	14.4	24.4	29.4	18.1	
FDI from EU countries - % of GDP	4.1	7.6	11.5	10.7	20.4	25.1	15.9	
External debt (private + public) - % of GDP (+ net external debt, if data exist)	65.0	60.1	63.8	70.9	81.7	99.8	107.4	
Trade with EU countries, % of total - EXPORT	55.69%	56.54%	54.25%	51.50%	50.39%	60.83%	60.15%	
IMPORT	50.27%	49.60%	48.16%	43.90%	41.24%	51.85%	50.49%	
Bank credit growth (% change)	44	48.3	48.6	32.4	24.6	62.5	31.6	
M2 (% change)	11.72%	18.84%	23.31%	24.30%	26.88%	31.30%	8.67%	
Interbank interest rates, monthly averagesfor the corrersponding year								
Share of deposits and credits denominated in Euro		25	35	34	39	52	54	
EU banks ownership of local banks, % of total assets						79.4	81.2	
Stock market index		454.34	625.31	825.53	1224.12	1767.88	358.66	
World bank doing business ranking					62	54	44	45

Monthly (starting from June 2008) and quarterly (starting from IQ 2008) data according to the frequency (monthly; quarterly) of their issue

	2008							**2009**		
	1Q	**2Q**	**3Q**	**4Q**						
GDP growth, % change from the same quarter of the previous year	7.0	7.1	6.8	6.5						
	June	**July**	**August**	**Sept.**	**October**	**Nov.**	**Dec.**	**January**	**Feb.**	
Industrial production, % change from the same period of the previous year	4.18	2.77	-1.17	0.46	-3.35	-6.43	-11.14	-12.6		
Unemployment rate	6.0	6.0	5.9	5.8	5.9	5.9	6.3	6.5	6.7	
HICP (EU harmonized inflation index), % change from the same month of the previous year	14.7	14.4	11.8	11.4	11.2	8.8	7.2	6	5.4	
Exchange rate - % change against the Euro, monthly	0	0	0	0	0	0	0	0	0	
Government debt - % of GDP	14.5	14.4	14.6	14.7	15.3	15.3	14.9			
Long-term interest rates (10-year government bonds)	5.17	5.17	5.17	5.17	5.17	6	7.76	7.14	7.09	
Export growth – monthly data compared to the same period of the previous year	17.2%	22.1%	14.2%	17.00%	-1.39%	-15.12%	-14.37%			
Current account - % change yearly	142.18 %	45.23%	-14.28%	0.08%	39.40%	3.86%	-20.29%	-45.50%		
FDI - % change compared to the same month of the previous year	27%	-14%	-36%	-42%	-18%	-80%	-62%	-37%		
External debt (government + private) - % of GDP	99.6	96.1	102.5	105.3	107.1	110.3	108.4			
Bank credit growth, % change from the same period of the previous year	52.0	51.2	48.3	46.6	43.1	38.1	31.6	29.9		
M2, % change from the same period of the previous year	24.3%	23.8%	20.9%	19.4%	14.8%	10.7%	8.7%	8.2%		
Interbank interest rates	5.06	5.25	5.23	5.38	5.72	5.77	5.17	3.92		
Stock market index	1240.14	1128.61	1012.57	1009.61	802.94	482.51	365.62	359.58	273.1	265.34
Indicator of country risk premium (monthly since January 2007)										
5-years CDS for Government debt (monthly since January 2007)	not publicly available									