

THE COMPETITIVENESS OF THE BULGARIAN ECONOMY 2015

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Competitiveness profile and macroeconomic overview

In 2015 Bulgaria has regained one position compared to the previous year in the economic competitiveness ranking of the World Competitiveness Yearbook (WCY), published by the Institute for Management Development (IMD). **The country is ranked 55th out of 61 economies. This is only a marginal improvement and remains significantly lower compared to its highest achievement in 2009 – 38th place** (Figure 1). Bulgaria remains among the least competitive countries. Only Croatia and Ukraine are ranked lower among the European states. The country has been surpassed by its southern neighbor Greece, which recovery (from 57th to 50th place) comes on a strong performance in business efficiency and availability of skilled labor. The ranking highlights **two particular commonalities** among the best ranking countries. Firstly, nine countries from the top 10 are also listed in the top 10 of the business efficiency factor. And secondly, all top positions are occupied by economies which are driven by innovation-based growth.

KEY POINTS

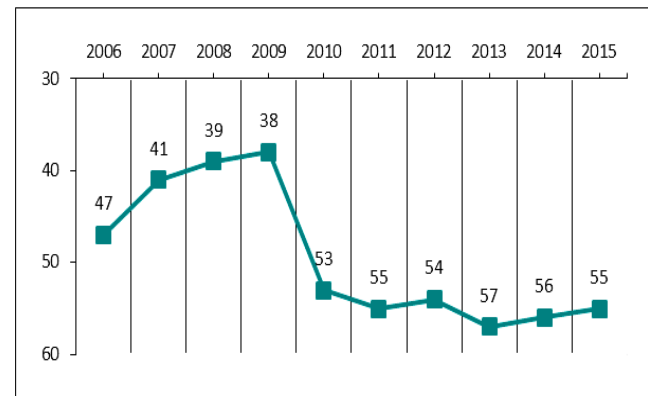
- Bulgaria ranks **55th** in the World Competitiveness Yearbook 2014 – a stagnation for a sixth year.
- Bulgarian government and business leaders have still **not been able to formulate and carry out coherent policies based on a long-term strategy to improve competitiveness.**
- The forced closure of the fourth largest bank and the ensuing **banking crisis of 2014** and the **increased government spending and borrowing** have had a negative impact as they have weakened the overall competitive position of the economy. The Eurozone and Greek crisis continue to be a major external drag on the economy.
- The **low level of education** remains a serious problem as the country continues to be characterized by one of the weakest education performances in Europe.
- Despite the increasing number of vacancies in 2014, **unemployment and youth unemployment rates remain relatively high** signaling that skills mismatch is a persistent problem for the labor market in Bulgaria.

The United States remains at the top of the ranking as a result of its strong business efficiency and financial sector, its innovation drive and the effectiveness of its infrastructure. The other most competitive economies, according to the WCY, are Hong Kong (2nd place) and Singapore (3rd place). The Asian countries move up overtaking Switzerland, which drops to fourth place. Their success lies with very high government and business efficiency. **The most competitive EU member state is Denmark (8th place)**, which improved from ninth place in the ranking last year and is now ahead of its neighbours Sweden and Germany, who both dropped four places to ninth and tenth. According to the WCY, Denmark has achieved the best further and vocational education in the world and has the second highest employee motivation. The Scandinavian country is ranked top of the pile when it comes to green-tech solutions, and it is also the country that spends the most money on education.

Among the **Central and Eastern European member states** with a similar legacy to Bulgaria, **Lithuania is the front-runner**, reaching 28th place, six positions higher than 2014. The ranking of the Baltic state highlights an innovative, profitable and responsible business performance based on increased business management standards and availability of venture capital for business development. Bulgaria could also follow the example of successful economic policies from the Czech Republic, Estonia and Poland, ranked 29th, 31st and 33rd respectively. Elsewhere in the region, the downfall in their positions of Russia (from 38th to 45th place) and Ukraine (from 49th to 60th place) highlight the negative **impact that armed conflict and the accompanying higher market volatility have on competitiveness** in an increasingly interconnected international economy. According to the WCY, both countries have seen their economic competitiveness plummet amid

heightened tensions in the region, and bilateral economic sanctions. The conflict has greatly exacerbated economic difficulties in the former Soviet republic, which scored worst of all the countries listed in the economic growth category, after seeing its economy contract 6.5% last year. Russia's competitiveness has also taken a hard hit, as the Ukraine crisis has chilled Moscow's ties with Europe and the United States to a degree comparable to the Cold War era.

Figure 1: Overall ranking of Bulgaria – rank assigned in IMD WCY



Source: IMD WCY 2015

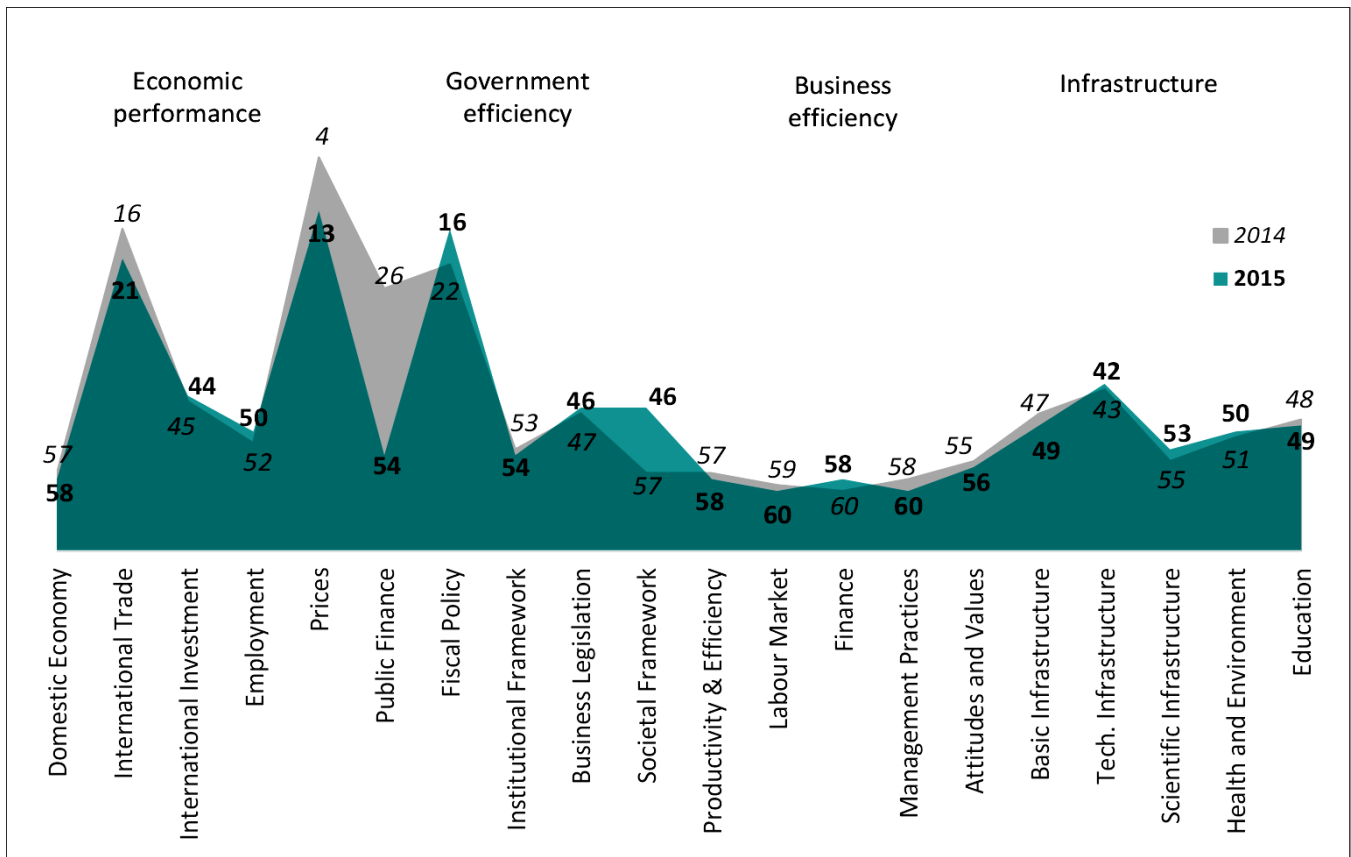
Among the 33 countries included in the overall ranking which have a **population of less than 20 mln.**, Bulgaria is occupies **31st place** (two places lower than 2014), ahead of only Croatia and the latest addition to the competitiveness ranking - Mongolia. **Bulgaria ranks in 24th place out of the 30 countries with a GDP per capita of less than \$20,000** (in 2014 it was in 26th place out of 29 countries). This is a much lower ranking than Bulgaria's best in this category, which was in 2009, when it was in 13th place out of 29 countries. **Bulgaria also ranks 36th among 38 economies in the EMEA region**, again surpassing only Croatia and Ukraine.

Bulgaria’s competitiveness landscape (figure 2) shows that there have not been any significant changes in the majority of the indicators, not only compared to 2014, but compared to 2010 levels. **The country’s competitiveness is stagnating**, while the policies and measures introduced over the past 8 years since Bulgaria became an EU member state have not resulted in any significant economic improvements, as the country has **not been able to catch up with the other Eastern European countries**. This shows that Bulgarian government and business leaders have still **not been able to formulate and carry out coherent policies based on a long-term strategy to improve competitiveness** in line with the national interests, needs and competitive advantages of the respective regions.

The Bulgarian economy continues to rely on narrow cost competitiveness, which makes the country vulnerable to changes in the international business environment.

Long-term competitiveness factors such as environment, education, health quality, as well as business efficiency indicators like management practices, productivity, and efficiency expose very serious long-term challenges, as their levels remain among the lowest in the ranking. As expected, the toppling of the fourth largest bank (by value of the assets) in the **banking crisis of 2014** and the **increased government borrowing and spending** have had a negative impact as they have weakened the overall competitive position of the country. EU funds under Operational Programme Regional Development that were suspended for Bulgaria back in the middle of 2014 have been **unfrozen by the European Commission**, which has helped progress in basic infrastructure, but do not seem to

Figure 2. Competitiveness landscape of Bulgaria 2014 – 2015



Source: IMD WCY 2015

have made a decisive difference for the country's competitiveness.

The **low level of the quality of education** remains a serious problem as the country continues to be characterized by one of the weakest education performances in Europe. The ranking clearly indicates the need for better education and qualified staff in order to meet the demands of employers. At the same time, despite the increasing number of vacancies in 2014, **unemployment and youth unemployment rates remain relatively high** signaling that regional skills mismatch is a persistent problem for the labor market in Bulgaria. High long-term unemployment rates combined with relatively low labor remuneration are likely to continue to provide incentives for citizens to engage in hidden economic activities in Bulgaria in the long run thus counterbalancing any government efforts to increase regulation. Social security regulation instability and tax structure and administration coupled with low satisfaction with public goods quality seem to still provide overriding incentives for citizens to avoid and evade paying taxes.

Bulgaria continues to have a **fiscally stable, open and export-oriented economy** with one of the lowest living and business costs in Europe. However, the country continues to suffer from the **lack of adequate business culture and institutional framework**. Relative to other EU members, Bulgaria performs rather poorly in European and international rankings related to governance quality, jurisdictional capacity and human development.

In 2014 the government debt as a percentage of GDP has increased by 9,3% compared to 2013 data. Despite this increase Bulgaria has registered one of the **lowest ratios of government debt as a percentage of GDP in Europe** but the Greek and Eurozone crisis and local elections in the country in 2015 can challenge fiscal discipline. Provided

the country's very high dependence on EU funds, and the coming to an end in 2015 of Bulgaria's first EU budget cycle, it is also likely to expect some budget strains from non-recognized EU-supported expenditures, which will increase the burden on the national budget.

A continuing positive trend is the increased **business expenditure on research and development**, which is widely recognized as the backbone of every globally competitive, knowledge-driven economy. EU funds' backed start-up, technological upgrade, and risk capital vehicles have supported the process.

Competitiveness challenges and policy recommendations

The Center for the Study of Democracy has identified the following five key challenges, which hinder the competitiveness of the Bulgarian economy:

- Tackle **high level corruption and state capture**;
- Modernize **public administration** and strengthen **independent regulators**;
- Adopt **education** for innovation-based growth;
- Tackle **energy poverty, energy intensity and supply dependency**;
- Improve the country's **branding**.

Addressing these challenges has the potential of improving the competitiveness profile of the Bulgarian economy with regards to public administration efficiency, education, energy security and corruption in the private and the public sector. This would require sustained collective efforts and common vision among government, nonprofit and business leaders in the next decade.