



**UNITED
BULGARIAN
BANK**

A Member of NBG Group

**BULGARIA:
ECONOMIC & MARKET ANALYSES
March, 2008**



Current account gap widened by 16.1% y/y to 3.9% of GDP in January-February. Net FDI inflows rose by 2.5% y/y to EUR 403.5 mn in January-February

Foreign trade gap widened by 14.6% y/y to 3.7% of GDP in January-February

Gross external debt grew by 35.7% y/y to 87% of GDP as of end-January

Consumer price inflation rebounded to 14.5% y/y in March. PPI inflation accelerated to 13.9% y/y in February

Industrial sales growth decelerated to 11% y/y in February

Retail sales rose by 11.6% y/y in February

Household monetary expenditure slowed to nominal 16.8% y/y in February

Unemployment rate fell by 2.1pps y/y to 6.79% as of end-March

Consolidated budget surplus widened to 0.9% of GDP in January-February

Money supply grew by 29.8% y/y to 67.5% of GDP as of end-February. Claims on non-government sector slowed their growth rate to 59.3% y/y as of end-February

Banks' net profit grew by 30.8% y/y to EUR 116.3 mn as of end-February

Crisis affects pension funds' return rates

Market capitalisation of the stock exchange dropped by 9% m/m at end-March

I. EXTERNAL SECTOR

1. Balance of Payments

Current account gap widened by 16.1% y/y to 3.9% of GDP in January-February

Current account (CA) gap widened by 16.1% y/y to EUR 1297.1mn in January-February or 3.9% of the projected full-year GDP, according to Central bank preliminary data. In February alone, the CA gap increased by 25.7% y/y to EUR 594.3 mn as compared to revised 9.1% y/y a month earlier.

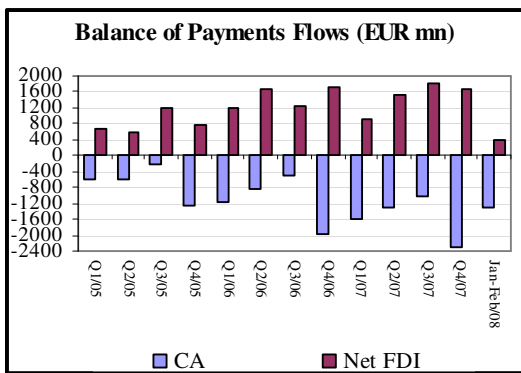
The balance on services deteriorated by 121.3% y/y to EUR 137.4 mn in January-February.

Net income balance was positive amounting to EUR 83 mn in January-February as compared to a negative balance of EUR 20.6 mn for the same period last year.

Net current transfers item was negative amounting to EUR 30.8 mn in January-February, against a positive item of EUR 23.3 mn in January-February last year. .

The overall balance of payments was negative at EUR 374.1 mn in January-February but narrowed from EUR 429.1 mn a year earlier as the net inflow in the financial and capital account improved to EUR 946.7mn in January-February.

IMF and government expects the CA gap at about 22%of GDP this year staying almost flat in relation to last year.



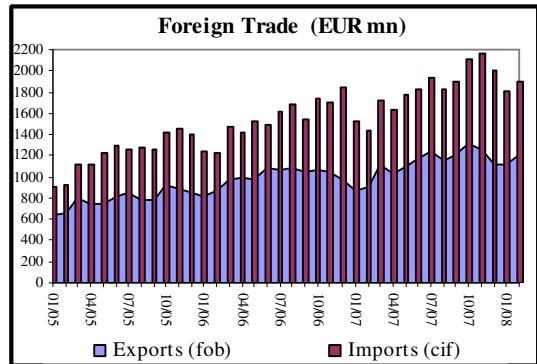
Net FDI inflows rose by 2.5% y/y to EUR 403.5 mn in January-February

Net FDI inflows rose by 2.5% y/y to EUR 403.5 mn in January-February covering 31.2% of the CA gap as compared to 35.4% a year earlier,

according to Central bank preliminary data. The growth rate however slowed from 49% y/y in January. The weak FDI performance in February alone could be a signal of trending revisions in the investment plans as a result of the global financial crisis although it is too early to make conclusions on the back of one-month statistics.

Foreign trade gap widened by 14.6% y/y to 3.7% of GDP in January-February

The foreign trade deficit increased by 14.6% y/y to EUR 1206.8 mn in January-February or 3.7% of the projected full-year GDP as a result of the higher imports base, according to Central bank preliminary data. Merchandise exports (fob) retained faster growth rate of 33.1% y/y in February and 30.7% in January-February. Imports (cif) rose by 32% y/y in February and 25% y/y in January-February, speeding from 18.6% y/y in January.



2. External Debt

Gross external debt grew by 35.7% y/y to 87% of GDP as of end-January

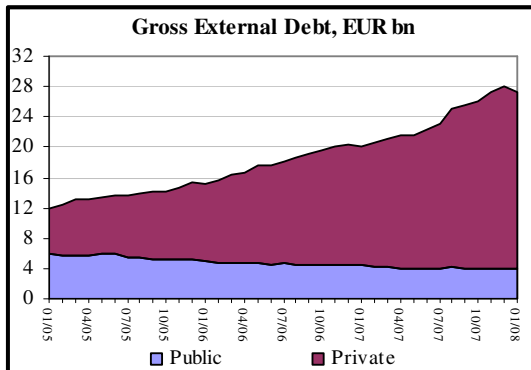
Gross external debt grew by 35.7% y/y to EUR 27.4 bn as of end-January, according to Central bank preliminary data. The debt stock reached 87% of the full-year GDP projection as compared to 69.9% a year earlier. On a monthly basis, gross external debt decreased by 2.5%. The Central bank has made revisions that pushed up the figure to EUR 28.1 bn as of the end of December as compared to initially reported EUR 27 bn. The steep monthly drop in the debt stock was most likely triggered by collection of loans disbursed to local intermediaries for purchase of equities as well as repayments to parent companies for meeting liquidity problems stemming from the global credit crunch.

Debt-servicing accounted for 3.2% of GDP as compared to 2.5% in January last year. The share

of short-term debt rose by 3.3 pps y/y but dropped by 2 pps in a month to 32% of the total external debt.

Public debt decreased by 9.7% y/y to EUR 4.1 bn as of end-January. The liabilities of the private sector surged by 48.7% y/y but dropped by 3% m/m to 85.2% of the total (against 77.8% in January last year) and continued to be the only contributor to the debt accumulation.

Internal financing within foreign-owned companies accounted for 35.1% of the total external debt. Banks' external debt rose by 63.1% y/y but dropped by 14.2% m/m to EUR 4.9 bn (15.6% of GDP) as of end-January. The foreign liabilities of commercial firms (state-owned and private companies) grew by 32% y/y to EUR 9.8 bn as of end-January.



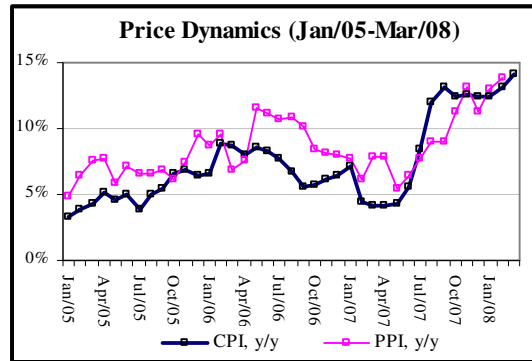
II. REAL SECTOR

1. Inflation

Consumer price inflation rebounded to 14.5% y/y in March

Consumer price inflation accelerated to 14.5% y/y in March from 13.2% y/y in February, according to NSI data. The monthly inflation is reported at 0.8% as compared to 1.1% in February. The period-average inflation was 13.3% in Q1. The harmonised index of consumer prices (HICP) used as a main price gauge by ECB, also accelerated to 13.2% y/y in March from 12.2% in February. Food prices sustained its upward trend and the annual increase in March reached 23.6% y/y against 21.9% y/y in February. Food products and restaurants have generated about 70% of the overall increase in the consumer basket. Services and non-food items also sustained high inflation rates against the EU average and were far above the benchmark for meeting the euro adoption price criterion. Moreover, the price index already

turned significantly above the government's projections for year-average inflation at 6.9%. Given the high inflation in Q1, the full-year average index is unlikely to fall below 8-9%, according to estimates.



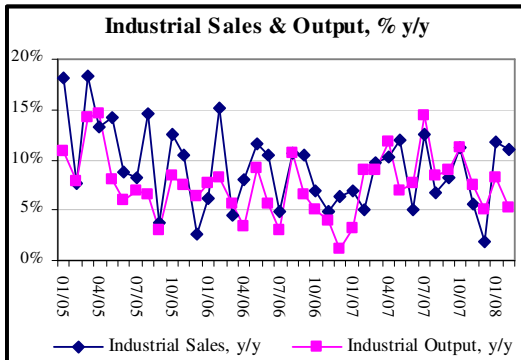
The producer price index covering industrial goods traded on the domestic market accelerated to 13.9% y/y in February from 13% y/y in January and 11.3% y/y in December, according to NSI. Metals extraction and processing as well as manufacturing of metals products were among the major drivers of the index growth acceleration. Food prices continued to rise faster as compared to the previous month – by 22.6% y/y in February against 22% y/y in January. Acceleration of PPI inflation rises expectations that consumer prices would have correspondingly sped up in March.

2. Industrial Sales

Industrial sales growth decelerated to 11% y/y in February

Industrial sales growth decelerated to 11% y/y in February from revised 11.8% y/y in January, according to NSI preliminary data. The index of industrial production, comprising sales and changes in inventory, grew by 5.2% y/y in February slowing from revised 8.2% y/y in January indicating a negative change in inventories. The slowdown was driven by the utilities sector, which declined for the first time since March last year. The downturn in the utilities sector is explained by the decision of the Ministry of economy to block electricity exports in the period January 14 – March 1 due to risks of supply shortages on the local market. Manufacturing growth sped up marginally by 12.9% y/y in February from 12.4% y/y in the previous month while extraction industries increased by 14.8% y/y as compared to a drop of 2.9% y/y in January. The performance of the industrial sector in the first two months of the year

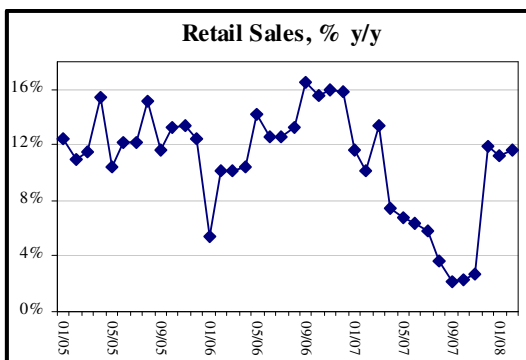
strengthens our expectations that the industry will sustain the sound growth rates from the past several years and the overall GDP growth will not be seriously affected by adverse external shocks related to the mortgage credit crisis in the USA.



3. Retail Sales

Retail sales rose by 11.6% y/y in February

Retail sales rose by 11.6% in February compared to 11.3% y/y in January, according to NSI preliminary data. The indicator rose by 11.5% y/y in Jan-Feb. Sales of clothes, household goods and appliances and pharmaceutical products continued rising at higher-than-average rates. Wholesales grew by 9.9% y/y during the month and 5.8% y/y in January-February as compared to 1.6% y/y in January. The group of trade and repair of automobiles increased by 16.4% y/y in February and 14.6% y/y in January-February.



4. Household Consumption

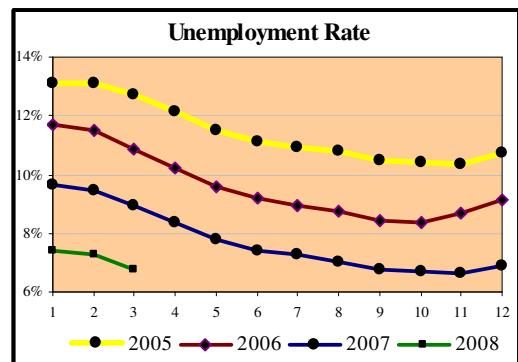
Household monetary expenditure slowed to nominal 16.8% y/y in February

The growth of household monetary expenditure slowed down to nominal 16.8% y/y in February as compared to 20.4% y/y in January, according to the household surveys of the NSI. The household monetary income also decelerated its growth rate from 22.4% y/y in January to 17.5% y/y in February.

5. Unemployment

Unemployment rate fell by 2.1pps y/y to 6.79% as of end-March

Unemployment rate fell by 2.1pps y/y and 0.47pps m/m to 6.79% in March, according to National Employment Agency. The annual margin of improvement remains quite impressive and will result into a further decline in the jobless rate to less than 5% in the summer months. It may tighten the labour market leading to wage hikes coupled with supply and demand-driven pressure on consumer prices.



II. FISCAL SECTOR

Consolidated budget surplus widened to 0.9% of GDP in January-February

The consolidated budget posted a surplus of BGN 574.7 mn (EUR 293.8 mn) in January-February, which accounted for 0.9% the projected full-year GDP, up by 0.2 pps in m/m terms, according to data of the Finance Ministry. A year earlier, the consolidated budget recorded a deficit of BGN 19.9 mn (EUR 10.2 mn).

The fiscal revenues surged by 34.4% y/y to BGN 3.88 bn (EUR 1.98 bn) in January-February pushed by indirect tax growth of some 80%, still influenced by one-off effect in the base period. As recalled, charges on VAT payments on shipments from member countries were delayed by nearly two months when the country joined the EU on Jan 1, 2007. As a result, the VAT and excise tax

base from the first two months of last year is exceptionally low. This effect, however, would not hold as of March onwards.

The fiscal expenditures (excluding the installment for the EU budget) increased by 13.4% y/y to BGN 3.1 bn (EUR 1.6 bn) in January-February.

Republican budget posted a surplus of BGN 420.8 mn (EUR 215.2 mn) in January-February amid a deficit of BGN 102.3 mn (EUR 52.3 mn) for the same period last year. Republican budget revenues and grants increased by near 50% y/y to BGN 2.8 bn (EUR 1.3 bn) due to the tax revenues hike of 60.4% y/y. Revenues from direct taxes grew by 12.6% y/y after the one-off drop in January due to rebound in free-lancers payments.

Personal income taxes paid under labour contracts increased by 14.6% y/y in January-February after a drop in January.

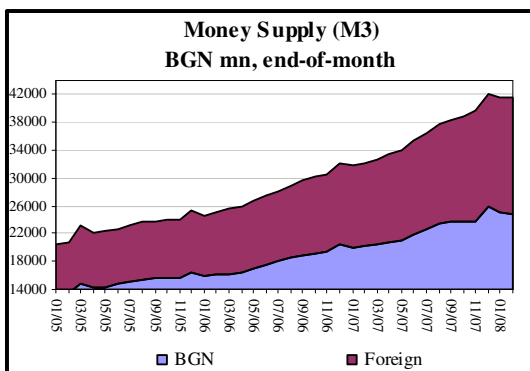
IV. MONETARY SECTOR

1. Monetary Aggregates

Money supply grew by 29.8% y/y to 67.5% of GDP as of end-February

Money supply (M3) grew by 29.8% y/y to reach BGN 41.7 bn (EUR 21.3 bn) or 67.5% of the projected GDP as of end-February pushed by the quasi-money high growth of 37.2% y/y, according to Central bank data. For a second month in a row the overnight deposits decelerated their growth rate from 28.6% y/y as of end-January to 24.5% y/y as of end-February on the back of the slowdown in the overnight deposits in leva of non-financial enterprises.

The foreign reserves rose by 36.6% y/y to EUR 11.656 bn as of end-February but dropped by 0.2% on a monthly basis.



2. Domestic Credit

Claims on non-government sector slowed their growth rate to 59.3% y/y as of end-February

Domestic credit growth decelerated to 50.5% y/y as of end-February from 57.8% y/y as of end-January and 58.8% y/y as of end-December, according to Central Bank data. The stock of domestic credit reached BGN 35.3 bn (EUR 18.1 bn) or 57.3% of the projected full-year GDP.

Claims on non-government sector decelerated their growth rate to 59.3% as of end-February from 61.8% y/y as of end-January. Though, the monthly increase exceeded BGN 1 bn as the most significant change on a monthly basis was registered in credits to households. Lending to non-financial companies slowed their growth rate for a second month in a row to 64.1% y/y as of end-February from 69.9% y/y as of end-January and 71.5% y/y as of end-December. The annual growth rate of credits to households and NPISH remained stable at 53.9% y/y as of end-February against 52.6% as of end-January. The credit growth is expected to moderate further this year in view of the upward adjustments of interest rates.

Domestic credit, % of GDP

	02/07	01/08	02/08
Domestic credit	42,8%	55,1%	57,3%
Claims on general government	-2,4%	-7,1%	-6,8%
Claims on non-government sector	45,3%	62,2%	64,0%
o/w Loans	44,0%	60,9%	62,7%
Non-Financial Corporations	26,3%	37,4%	38,4%
Financial Corporations	0,4%	0,7%	0,7%
Households and NPISH	17,3%	22,8%	23,6%
Consumer loans	7,4%	9,7%	10,1%
Loans for house purchase	6,7%	9,3%	9,6%
Deposits of NFIs and other clients	53,6%	62,1%	62,3%
Assets	78,6%	92,4%	94,1%

Source: BNB's Monetary survey and Balance sheet of the banking system

V. FINANCIAL SECTOR

1. Banking Sector

Banks' net profit grew by 30.8% y/y to EUR 116.3 mn as of end-February

The aggregated net profit of the 29 commercial banks rose by 30.8% y/y to BGN 227.5 mn (EUR 116.3 mn) as of end-February, according to Central bank data. The total value of assets increased by 34.8% y/y to BGN 58.1bn (EUR 29.7

bn) or 94.1% of the projected full-year GDP. However, the asset growth rate decelerated from 38.2% y/y in January and 40% y/y in December last year. The growth of the credit stock slowed to 40.6 y/y as of end-February from 43.7% y/y as of end-January and 67.5% last year. It accounted for 77.1% of all banks' assets. The credit growth is still financed by the increase of the deposits as the credits to deposits ratio stands at 89.9%.

The gross loans to enterprises amounted to BGN 25.2 bn (EUR 12.9 bn) at end-February, up by 2.4% m/m. Retail exposures rose by 3.8% m/m to BGN 13.8 bn (EUR 7.1 bn). Consumer loans increased by 4.1% m/m and mortgage loans – by 3.4% m/m at end-February. The stock of all deposits rose by 34.5% y/y to BGN 50.874 bn (EUR 26 bn) at end-February. The private sector deposits amounted to BGN 38.4 bn (EUR 19.7 bn) or 62.3% of the projected full-year GDP.

The Central bank does not report worsening of the credit portfolio of the banks. The liquidity of the banking sector is still good during the period.

According to the last report of the Central Bank, the crack of the loan standards in the struggle for the market shares and the overvaluation of the solvency of the households are among the main risks for the Bulgarian banks in 2008.

2. Pension Funds

Crisis affects pension funds' return rates

The global financial crunch has affected the growth of pension funds in Bulgaria. At the end of September 2007 companies boasted annual return rates comparable with those of mutual funds. Six months later the average return rates for the past two years were lower by 37% to 44%: **8.15%** for universal funds, **8.03%** for professional funds and **8.08%** for voluntary funds. The highest average return rate was below 13% while as of end-2007 three of the pension funds achieved average return rates of more than 15%.

The voluntary pension funds usually register the higher return rates because they have smaller number of restrictions of their investments. They have no minimum and upper cap of the yield. Occupation and voluntary pension funds have achieved lower than the voluntary ones yield. However, Financial Supervision Commission has defined for them required minimum rate of return and upper cap. The upper rate is the limit the yield should not exceed. Otherwise, the exceeding funds have to be allocated as a reserve.

The best performers last year have been affected the most: the biggest decrease in return is reported by CCB-Sila, Saglasie, Badeshte and Lukoil Garant.

Nevertheless, CCB-Sila's funds remain first in the segment of universal and voluntary insurance. They have posted for the past two years average rate of return of 11.4% and 12.82%, respectively. Saglasie retains the top position among occupational pension schemes with 10.81% return rate as of end-March.

The lower results are mainly due to the decrease on the stock exchange. According to specialists, the drop in pension funds' return rates will encourage them to invest abroad.

Pension funds average return rates, 2-year period: 31/03/06-31/03/08

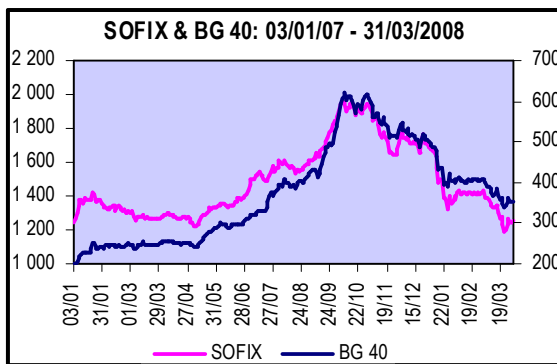
	Universal			Occupational			Voluntary		
	09/07	12/07	03/08	09/07	12/07	03/08	09/07	12/07	03/08
Doverie	10,4%	9,8%	5,9%	11,4%	10,5%	5,8%	12,3%	11,4%	6,4%
Saglasie	15,7%	15,2%	10,1%	17,7%	17,0%	10,8%	18,3%	16,5%	10,7%
DSK-Rodina	13,2%	12,3%	8,5%	14,5%	13,1%	8,5%	15,6%	13,8%	8,7%
Allianz Bulgaria	10,2%	9,6%	7,0%	10,7%	9,5%	6,5%	12,0%	10,2%	7,4%
ING	12,2%	11,5%	8,0%	13,1%	12,2%	8,5%	13,9%	13,0%	8,6%
CCB-Sila	18,3%	16,1%	11,1%	17,4%	15,5%	10,8%	23,0%	20,3%	12,8%
Lukoil-Garant	15,9%	14,2%	10,0%	14,4%	11,7%	7,6%	14,5%	12,5%	7,1%
Badeshte	15,6%	14,1%	9,2%	16,6%	15,3%	10,0%	21,1%	20,4%	10,6%
Non-modified weighted average	12,0%	11,3%	7,5%	13,0%	12,0%	7,4%	13,2%	11,7%	7,7%
Modified weighted average	12,9%	12,1%	8,2%	13,8%	12,5%	8,0%	14,3%	12,8%	8,1%
Arithmetic average	13,9%	12,9%	8,7%	14,5%	13,1%	8,6%	16,3%	14,8%	9,0%
Min return	7,7%	7,2%	4,9%	8,3%	7,5%	4,8%			

Source: Financial Supervision Commission

3. Stock Exchange

Market capitalisation of the stock exchange dropped by 9% m/m at end-March

Since the beginning of the year the blue-chip SOFIX index has declined by 27.8% to 1254.99 on March 31. The broader BG40 lost 31.3% of its value ending the month at 354.83 points. Total market capitalisation of the bourse dropped by 9% m/m or BGN 2.27 bn to BGN 23.25 bn (EUR 11.89 bn) at the end of March. The main reason for the decrease of the stock exchange in March was the buybacks from the mutual funds and the closures of repo deals, according to analysts. This has caused massive sales of the most liquid stocks.



In March the subscription for the capital increase of Bulgaria's Mekom finished successfully. A total of 2,603,614 shares were subscribed, or 24.4% of the offering. The IPO was successful because more than 2.5 mn shares were subscribed. The placement price of the shares was set at BGN 2.20 per unit, which is the minimum price set in its prospectus. The company, which hoped to raise some BGN 23.5 mn for capacity expansion and investments abroad, has attracted BGN 5.728 mn in the placement. Secondary trade in Mekom's shares on the Bulgarian Stock Exchange is expected to begin by the end of April. The free float will be about 5%. Institutional investors subscribed 40% of the issue.

In January Mekom offered to the public 10,682,800 shares with a face value of BGN 1.0 in the IPO. It was the first company which extended the subscription period for its IPO by 44 days due to the slump of the domestic capital market prompted by global stock exchange falls.

Investors' poor interest in initial public offerings (IPOs) and the crisis on the capital market have thwarted the plans of many companies to acquire a public status. A number of other local firms, which were in a hurry to go public, have announced plans to postpone their offerings after bottle cap manufacturer Herti earlier this year sold just 0.46% of the offered capital through an IPO. Market players are now much more cautious, because investing in an IPO may bring not only high return but high risk, too.

In 2007, a total of 68 companies expressed willingness to get listed on the Bulgarian Stock Exchange through initial or secondary offering. Five companies rejected or postponed their plans: BG Agro, Papas Olio, Max Telecom, investment fund Ceres, and Contrax

As of end-March the Vienna Stock Exchange (VSE) has announced it is starting to calculate a national index for Bulgaria: Bulgarian Traded Index (BTX). The new index will include seven of the most traded companies with the highest capitalisation on the BSE. At present these are Chimimport, Fist Investment Bank, Eurohold Bulgaria, Industrial Holding Bulgaria, Corporate Commercial Bank, Monbat, and Kaolin. Calculation of the new index starts on March 28. BTX is a capitalisation-weighted index and the weight of each company should not exceed 25%. This index, however, will not include adjustments for dividend payments. Vienna Stock Exchange will be calculating the new index in real time in three currencies, BGN, EUR, and USD. BTX will be used for standardised derivatives such as futures, options and structural products. The starting value of the index is 1,000 points. Changes in the index can be made every six months.

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