

Bulgaria

By Petar Ivanov, Tsvetkova Bebov & Partners, member of Eversheds Sutherland

IN A NUTSHELL

- The economy slowly recovered with growth of 1.8% and inflation fell to 8.6%.
- Despite house prices and inflation, low interest rates and increasing income fuelled mortgage market growth.
- Growth continued in early 2024, as rates declined slowly.
- Two new acts of legislation aim at improving conditions for the issuance of securitisations and covered bonds.
- The Recovery and Resilience Plan facilitates energy efficiency improvements.

MACROECONOMIC OVERVIEW

The economy stabilised after a period of uncertainty due to factors such as to the war in Ukraine and an ongoing political impasse, which has left the country without a stable government since 2021. GDP growth is projected to be 1.8% (to EUR 94 bn) over the year compared to the EU and Eurozone average 0.5%. Inflation began to decrease with the HICP down to 8.6% y-o-y from 13% in 2022. Despite this, inflation is still above the EU average of 6.4% (5.4% in the Eurozone). Unemployment remained historically low at 4.3% (EU average of 5.9%, 6.4% in the Eurozone). Inflation and a shortage of qualified labour contributed to further growth of average wages, which increased 13.7%.

LOOKING AHEAD

The economy is expected to continue to recover gradually despite the ongoing political instability and wider geopolitical risks.

According to its spring economic forecast, the European Commission expects real GDP growth in 2024 of 1.9% (1.0% in the EU and 0.8% in the Eurozone) and projects a decrease of inflation to 3.1% from 8.6% in 2023 (2.7% in the EU and 2.5% in the Eurozone). As of May 2024, inflation is stable at 5.1%, y-o-y. Wage growth is expected to slow in line with the decreasing inflation, while the labour market will remain tight with a low rate of unemployment.

Expectations for a cooling of the housing market in 2023 did not materialise and in the first five months of 2024 mortgage lending is at record levels with an increase of 24.45% y-o-y. In the first months of the year rates slightly decreased compared to the 2023 average.

HOUSING MARKETS

The housing market has continued to grow. The number of issued building permits remained practically unchanged – 8,165 (8,169 in 2022), the second largest since 2008 (10,157). Housing starts increased to 5,860 (5,468 in the

previous year), and housing completions increased to 5,419 (5,390 in 2022). This contributed to a 13.2% increase in the volume of new residential lending from BGN 6.7 bn (ca. EUR 3.4 bn) in 2022 to BGN 7.6 bn (ca. EUR 3.9 bn).

Inflation and increased demand further accelerated house prices, which at the end of 2023 averaged at 186.7% of the index's base value in 2015 compared to 170% in 2022.

The housing market varies regionally: prices in the two largest cities – Sofia and Plovdiv – outperform the average and reached 210% (194.2% in 2022) and 195.7% (177% in 2021), respectively. At the opposite end is the fourth largest city – Burgas and its South-east region of Bulgaria with HPIs of 173% and 159.9%, respectively. There were higher average wages and more diverse job opportunities in the largest cities – for instance, the average wage in Sofia was 37% higher than the average contributing to the asymmetric price increases.

Similarly, the rental market continues to have discrepancies with a steady increase of prices and demand in Sofia compared to the other regions, for the same reasons.

MORTGAGE MARKET

MARKET DYNAMICS

There has been sustained growth in mortgage lending and lowering interest rates for over a decade, since 2010 with a slow recovery following the crash of 2008/2009 after the global financial crisis.

In 2023 the mortgage market grew by 20% to a total outstanding residential loans of BGN 22 bn (ca. EUR 11.3 bn). Interest rates remained stable at an average of 2.59% for BGN denominated loans (2.54% in 2022) and 3.53% for loans in EUR (3.11% in 2022), which is near the all-time lows in 2022. This contrasts to the sharp increase in interest rates in most EU countries and is due to the excess liquidity in the Bulgarian banking sector, which keeps bank funding costs low. In the first months of 2024 interest rates started to slowly decrease (2.56% in March and 2.51% in May for loans in BGN), which indicates that a long-awaited cooling off of the market is not yet in sight.

Most new loans are floating rate (97%) and BGN denominated (95% of all outstanding and 97% of new loans) due to the more favourable interest rate terms on BGN loans and despite the declared goal of joining the Eurozone by 2025. The maximum maturity for new mortgages is 35 years with an average of 20 – 25 years. Due to the rise in inflation and housing prices the average borrowed amount on new loans has increased to around BGN 198,000 (ca. EUR 100,000) with an LTV of 70-80%.

Housing NPLs continued to decrease to 1.5% (BGN 332 mn) of all outstanding mortgage loans (2.33% in 2022).

On the supply side, credit standards for house purchases remained largely unchanged. In a recent review of the risks facing the banking system, the Bulgarian National Bank observed that the increased credit growth in 2022 and 2023 has generally not been accompanied with credit standards loosen-

ing and that banks have been taking a balanced approach to assuming risks related to the housing market.

In 2023 the main drivers of demand on the Bulgarian market were the fear from the rising inflation and borrower's desire to convert savings into a housing investment, which is perceived as a "safe haven" in an environment of regional and domestic crises and regional and domestic political instability.

MORTGAGE FUNDING

Bank funding is dominated by deposits. As at the end of 2023, the banking sector had BGN 147 bn (ca. EUR 73 bn) in deposits (2022 – BGN 134 bn), equal to 80% of GDP and 86% of banking assets. Household deposits account for BGN 82.6 bn (EUR 42 bn) or 56% of the total, followed by deposits of non-financial entities – BGN 46 bn (EUR 23.7 bn) or 31%, and deposits of financial entities – BGN 14.6 bn (EUR 7.5 bn) or 10%. This is mainly due to the well-established preference of households and non-financial entities to keep their free funds in bank deposits, which has arguably suppressed the development of the country's capital market. The growth in deposits is also a result of the strengthening of consumer confidence in the banking system in recent years.

Typical wholesale funding tools such as securitisations and covered bonds are practically non-existent. The same applies to central bank funding, which may be provided only in strictly limited cases due to the pegging of the Bulgarian Lev to the Euro. Whereas the lack of appropriate legal infrastructure has hindered securitisations, mortgage bonds – a type of covered bonds – did not manage to establish themselves as successful and marketable products despite the issuance of several mortgage bond programmes and stand-alone issues in the late 00s and early 10s. The last mortgage-backed bonds issue by a Bulgarian bank matured in September 2019.

In March 2022, the Bulgarian Parliament adopted the new Covered Bonds Act, which replaced the existing mortgage-backed bonds legislation and transposes the EU's Covered Bonds Directive (EU) 2019/2162. The Covered Bonds Act is the result of an EBRD (European Bank for Reconstruction and Development) funded project aimed at creating a modern covered bonds market in Bulgaria and encouraging cross-border investment into and from Bulgaria. In addition, in March 2021 a new law on special purpose and securitisation companies entered into force, which established a legal framework for securitisations in Bulgaria.

It is yet to be seen what the impact of these modernisation efforts on the wholesale funding of Bulgarian banks will be.

GREEN FUNDING

The National Recovery and Resilience Plan, part of Next Generation EU, establishes a National Program for Energy Renovation of Residential and Non-residential Buildings (the Program) under the auspices of the Ministry of Regional Development and Public Works. The total funds dedicated to the Program are BGN 2.47 bn (EUR 1.26 bn) for the renovation of multifamily residential buildings, public and commercial buildings in the period 2022 – 2026. The main goal of the Program is to achieve a 30% increase in energy efficiency in participating buildings through the funding of projects, such as the thermal insulation, renovation of common heating, cooling and ventilation systems,

and the construction of renewable energy installations. The application period for a first stage of the Program started in December 2022.

The National Recovery and Resilience Plan also envisages the co-funding of individual investments to increase the energy efficiency of single family and multifamily buildings, such as the construction of solar energy installations, in a total amount of BGN 240 mn (EUR 123 mn) in the period 2022-2025..

	BULGARIA 2022	BULGARIA 2023	EU 27 2023
MACROECONOMIC VARIABLES			
Real GDP growth (%) (1)	3.9	1.8	0.4
Unemployment Rate (LSF), annual average (%) (1)	4.3	4.3	6.1
HICP inflation (%) (1)	13.0	8.6	6.4
HOUSING MARKET			
Owner occupation rate (%) (1)	85.0	86.1	69.2
Gross Fixed Investment in Housing (annual change) (1)	-1.4	-0.2	-3.1
Building Permits (2015=100) (2)	47.3	47.3	94.0
House Price Index - country (2015=100) (2)	156.2	186.7	170.2*
House Price Index - capital (2015=100) (2)	163.5	210.0	165.1*
Nominal house price growth (%) (2)	15.2	19.6	3*
MORTGAGE MARKET			
Outstanding Residential Loans (mn EUR) (2)	9,390	11,263	6,782,375
Outstanding Residential Loans per capita over Total Population (EUR) (2)	1,373	1,747	15,114
Outstanding Residential Loans to disposable income ratio (%) (1) (2)	n/a	n/a	71.3
Gross residential lending, annual growth (%) (2)	23.5	13.2	-26.6
Typical mortgage rate, annual average (%) (2)	3.1	3.5	4.7

* Please note that this value is a simple average of the available values in 2023.

Sources:

(1) Eurostat.

(2) European Mortgage Federation - Hypostat 2024, Statistical Tables.



BULGARIA FACT TABLE

Which entities can issue mortgage loans in your country?

In Bulgaria there are no specialised mortgage banks. Therefore, all licensed commercial banks (credit institutions) can provide mortgage loans. The largest and most active lenders of residential mortgage loans are 'tier 1' banks DSK Bank (DSK), UniCredit Bulbank (UCB), Eurobank Bulgaria (Eurobank), United Bulgarian Bank (UBB), First Investment Bank (FIB), as well as 'tier 2' banks KBC Bank Bulgaria (ex Raiffeisenbank Bulgaria) (KBC BG)*, Central Cooperative Bank (CCB) and Allianz Bank Bulgaria (Allianz).

*In March 2023 KBC BG has merged into UBB following an acquisition of KBC BG by UBB in the course of 2022..

What is the market share of new mortgage issuances between these entities?

From 31.12.2021 to 31.12.2022 the total nominal (principal) value of residential mortgage loans issued by Bulgarian banks has increased by ca. BGN* 2.6 bn from BGN 15.82 bn to BGN 18.37 bn. The 8 most active banks on the Bulgarian residential mortgage loan market account for around 95.4% of this increase – UBB and KBC BG (21.3%), UCB (21.2%), Eurobank (20.2%), DSK (18.4%), FIB (5.4%), CCB (4.7%), Allianz (4.2%).

* EUR 1 = BGN 1.95583

Which entities hold what proportion of outstanding mortgage loans in your country?

As of 31.12.2021 the total nominal (principal) value of residential mortgage loans issued by Bulgarian banks is BGN* 18,37bn. The 8 banks mentioned above form BGN 17.57 bn (ca. 96%) of this amount, of which DSK holds BGN 4.25 bn (ca. 23.2%); UBB and KBC BG – BGN 4.13 bn (ca. 22.5%); UCB – BGN 3.30 bn (ca. 18%), Eurobank – BGN 3.06 bn (ca. 16.6%), FIB – BGN 1.14 bn (ca. 6.2%), CCB – BGN 959 mn (ca. 5.2%), Allianz – BGN 725 mn (ca. 4%).

* EUR 1 = BGN 1.95583

What is the typical LTV ratio on residential mortgage loans in your country?

The average LTV ratio is 80%.

How is the distinction made between loans for residential and non-residential purposes in your country?

The official statistics of the Bulgarian National Bank (BNB) provides information only on residential mortgage loans extended by Bulgarian banks (and Bulgarian branches of foreign banks) – reported at nominal (principal) value before deduction of provisions, without fees and currently accrued interest.

BNB defines "residential" or "housing" loans as loans granted to households for the purpose of investing in dwellings for their own use or for letting out, including for the construction and improvement of dwellings, which can be secured by various types of assets.

What is/are the most common mortgage product(s) in your country?

The most widely used mortgage products in Bulgaria are BGN denominated housing loans with variable rates, which are generally defined in the banks own lending policies. The average size of loans is being cited as BGN 150,000.

Interest rates have been decreasing over the last years. In 2022 the average interest rates on BGN denominated housing loans is 2.54%.

What is the typical/average maturity for a mortgage in your country?

The average maturity of mortgage loans in Bulgaria is around 20 – 25 years with maximum term of any mortgage being 35 years.

What is/are the most common ways to fund mortgage lending in your country?

Funding of mortgage loans is based largely on deposits. Alternative funding sources are uncommon in Bulgaria. There is practically no mortgage bond market in Bulgaria, with last mortgage bond issuance dating back to 2014 and all issues being redeemed since, the latest in September 2019. In March 2022 a new Covered Bonds Act transposing the Covered Bonds Directive (EU) 2162/2019 was adopted by the Bulgarian Parliament. There is yet no market for covered bonds in Bulgaria.

What is the level of costs associated with house purchase in your country (taxes and other transaction costs)?

A variety of taxes and fees are associated with purchasing properties in Bulgaria, most of which vary according to the property's price, but which may also depend on whether the property has land attached, whether it is being bought through an agent (as opposed to directly from the vendor), or whether there are other consultants involved (e.g. lawyer, surveyor or translator).

In particular, a purchaser should be aware of the following related costs: municipal tax (up to 3% of the purchase price depending on municipality involved, no cap); notary expenses for the purchase and for the establishment of a mortgage (each notarisation costs between BGN 500 and BGN 6000 depending on the price of the property); state fee for registration of the purchase and the mortgage in the Bulgarian Property Register (each registration costs 0.1% of the property price, no cap); potential VAT implications of the purchase must also be considered.

What is the level (if any) of government subsidies for house purchases in your country?

Not available, other than limited tax benefits for young families (spouse not elder than 35 years), which can deduct from their taxable income interest payments on loans (or the part of loans) up to BGN 100,000.