COUNCIL RECOMMENDATION

of 9 July 2019

on the 2019 National Reform Programme of Bulgaria and delivering a Council opinion on the 2019 Convergence Programme of Bulgaria

(2019/C 301/02)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies [1], and in particular Article 9(2) thereof,

Having regard to Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances [2], and in particular Article 6(1) thereof,

Having regard to the recommendation of the European Commission,

Having regard to the resolutions of the European Parliament,

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

Having regard to the opinion of the Economic and Financial Committee,

Having regard to the opinion of the Social Protection Committee,

Having regard to the opinion of the Economic Policy Committee,

Whereas:

(1) On 21 November 2018, the Commission adopted the Annual Growth Survey, marking the start of the 2019 European Semester for economic policy coordination. It took due account of the European Pillar of Social Rights, proclaimed by the European Parliament, the Council and the Commission on 17 November 2017. The priorities of the Annual Growth Survey were endorsed by the European Council on 21 March 2019. On 21 November 2018, on the basis of Regulation (EU) No 1176/2011, the Commission also adopted the Alert Mechanism Report, in which it identified Bulgaria as one of the Member States for which an in-depth review would be carried out.

[1] OJ L 209, 2.8.1997, p. 1.
[2] OJ L 306, 23.11.2011, p. 25.

(2) The 2019 country report for Bulgaria was published on 27 February 2019. It assessed Bulgaria's progress in addressing the country-specific recommendations adopted by the Council on 13 July 2018 ([3]), the follow-up given to the country-specific recommendations adopted in previous years and Bulgaria's progress towards its national Europe 2020 targets. It also included an in-depth review under Article 5 of Regulation (EU) No 1176/2011, the results of which were also published on 27 February 2019. The Commission's analysis led it to conclude that Bulgaria is experiencing macroeconomic imbalances. In particular, vulnerabilities in the financial sector are coupled with high indebtedness and non-performing loans in the corporate sector. While there is progress in addressing sources of the imbalances, the full implementation and monitoring of recent reforms of supervision and governance in the bank and non-bank financial sectors will be crucial.

(3) On 24 April 2019, Bulgaria submitted its 2019 National Reform Programme and its 2019 Convergence Programme. In order to take account of their interlinkages, the two programmes have been assessed at the same time.

(4) Relevant country-specific recommendations have been addressed in the programming of the European Structural and Investment Funds ('ESI Funds') for the 2014-2020 period. As provided for in Article 23 of Regulation (EU) No 1303/2013 of the European Parliament and of the Council ([4]), where it is necessary to support the implementation of relevant Council recommendations, the Commission may request a Member State to review and propose amendments to its Partnership Agreement and relevant programmes. The Commission has provided further details on how it would make use of that provision in guidelines on the application of the measures linking the effectiveness of the ESI Funds to sound economic governance.

(5) Bulgaria is currently in the preventive arm of the Stability and Growth Pact. In its 2019 Convergence Programme, the government, starting from a headline surplus of 2 % of gross domestic product (GDP) in 2018, aims at a deficit of 0,3 % of GDP in 2019 and a surplus of 0,4 % of GDP in 2020, 0,2 % in 2021 and 0,1 % in 2022. Based on the recalculated structural balance ([5]), the medium-term budgetary objective — a structural deficit of 1 % of GDP in structural terms — continues to be overachieved throughout the programme period. According to the 2019 Convergence Programme, the general government debt-to-GDP ratio is expected to decline gradually from 22,6 % of GDP in 2018 to 16,7 % in 2022. The macroeconomic scenario underpinning those budgetary projections is plausible. Based on the Commission 2019 spring forecast, the structural balance is forecast to register a surplus of 0,7 % of GDP in 2019 and 0,6 % of GDP in 2020, above the medium-term budgetary objective. Overall, the Council is of the opinion that Bulgaria is projected to comply with the provisions of the Stability and Growth Pact in 2019 and 2020.

(6) Tax revenues and tax compliance are improving and a number of initiatives are in place. However, tax collection does not seem to be improving everywhere at the same pace. This is particularly the case for labour-related taxes and social security contributions and in some categories of excise taxes. There is also evidence that undeclared work and illicit trade in fuels remain a challenge. Maintaining the efforts to improve tax collection and taking additional targeted measures to face the challenges in specific areas of the tax system is of paramount importance for reducing further the still large shadow economy.

(7) The government has taken steps to improve the effectiveness of public expenditure. The World Bank completed a spending review covering a number of public institutions (ministries and municipalities) and two pilot studies, one on policing and firefighting and one on waste management, and also delivered a manual for future reviews by the government. In the 2018 medium-term fiscal strategy, the government introduced a number of performance indicators to assess the impact of spending in the different policy areas over time and to inform evaluation and planning of the budget. Following up on these initiatives is expected to raise the quality, efficiency and transparency of public spending, and consequently the quantity and quality of public goods.

([3]) OJ C 320, 10.9.2018, p. 7.

([4]) Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006 (OJ L 347, 20.12.2013, p. 320).

([5]) Cyclically-adjusted balance net of one-off and temporary measures, recalculated by the Commission using the commonly agreed methodology.

(8) State-owned enterprises suffer from weak corporate governance, which is also to a large extent reflected in their economic performance. A reform of the legal framework for the corporate governance of State-owned enterprises is under way in cooperation with the Organisation for Economic Cooperation and Development (OECD) and with the support of the Commission's Structural Reform Support Service. The reform aims to address the current weaknesses by aligning the national legislation with the OECD's corporate governance guidelines for state-owned enterprises. The adoption and effective implementation of the framework will ensure the continuity and will be critical for the success of the reform.

(9) In a favourable economic environment, banks' capital and liquidity ratios improved on average. In parallel, non-performing loans by non-financial corporations declined although they remain high. The secondary market for non-performing loans has become more dynamic. On 30 May 2019 the BNB adopted a decision to implement the EBA Guidelines for the management of non-performing and restuctured exposures. The follow-up measures resulting from the financial sector reviews have strengthened the banking sector, but some vulnerabilities remain. New regulatory initiatives in 2018 included the rules for large exposures and the identification of connected clients, an increase in the counter-cyclical capital buffer rate and the introduction of macro-prudential tools for borrower-based measures. Following up on legislative initiatives on related-party exposures, sustained supervisory efforts to limit loans to related parties and penalise infringements of collateral provisions are crucial to support sound business practices. Enhancing the bank resolution framework is another ongoing measure that will contribute to the resilience of the financial sector.

(10) Completing the insolvency reform could help reduce the high outstanding private-sector debt and the still high share of non-performing loans. Some missing elements reduce the efficiency and effectiveness of the insolvency framework, resulting in slow and costly insolvency proceedings. At the same time, the absence of adequate monitoring tools prevents a proper analysis of current and new pre-insolvency and insolvency procedures and does not allow concrete bottlenecks or weak points to be identified. In October 2018, Bulgaria asked for assistance from the Commission's Structural Reform Support Service to help it advance the reform of the insolvency framework. This project identifies gaps in the insolvency framework and will produce a roadmap to address them. It is important to sustain the reform momentum and implement the forthcoming roadmap.

(11) Bulgaria has adopted legislative amendments in 2018 and subsequently in May 2019 and is working towards a fully consistent transposition of the Directive (EU) 2015/849 of the European Parliament and of the Council [6] (Fourth Anti-Money Laundering Directive). Attention should be paid to the effective implementation of these measures. The authorities have still not finalised and notified the National Risk Assessment, which is a cornerstone to devising adequate national policies to combat money laundering and terrorist financing. Moreover, recent developments in the banking sector suggest that there is need to enhance the national supervision of international financial transactions and to ensure the effective enforcement of the anti-money-laundering (AML) framework. The risk of corruption needs to be better addressed, as it is a predicate offence to money laundering. The Bulgarian authorities will need to show concrete results and build a track record evidenced by final decisions in high level corruption cases. The use of financial investigation and financial profiling is limited.

(12) Non-bank supervision is being reformed. The Financial Supervision Commission adopted an action plan for reforming non-bank financial supervision in September 2017, in cooperation with the European Insurance and Occupational Pensions Authority. The full and timely implementation and enforcement of the action plan, still ongoing, will contribute to adequate supervision of the non-banking financial sector. Amendments to secondary legislation are in place, aiming to improve the valuation rules and their application. Their effective implementation and enforcement would address remaining valuation issues that have been identified in the past. Lastly, group-level supervision remains a challenge for ensuring an adequate risk-based insurance supervision.

[6] Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC (OJ L 141 5.6.2015, p. 73).

(13) The car insurance sector presents some vulnerabilities. Well-specified rules on compensation would facilitate a more harmonised approach by judges when deciding on individual cases. In the longer term, such a methodology would help to reduce costs, volatility and underwriting risk in the motor third-party liability line of business. The sustainability of the sector would also benefit from improved pricing that takes into account clients' driving history. The Financial Supervision Commission has proposed a bonus-malus system, which is undergoing broad public debate. Lastly, the liquidity of the 'Green Card Bureau' has raised substantial concerns, mainly due to the non-payment of claims by one Bulgarian insurer. Strict compliance of all members with their obligations is crucial for the credibility and efficiency of the system.

(14) Infrastructure suffers from major investment gaps. The coverage and quality of transport infrastructure have improved but remain below the Union average. The Trans-European Transport Network in Bulgaria is still incomplete. Moreover, greenhouse gas emissions from road transport have increased strongly over the last five years. There is a need for further development of rail and road sections and the respective European rail traffic management systems and intelligent transport systems. Bulgaria has low connection and treatment rates for urban waste water, high air pollution levels and landfilling rates for municipal waste and a recycling rate, considerably lower than the Union average. Investments to promote sustainable water management, resource efficiency and the transition to a circular economy are necessary. In addition, investment needs in the fields of energy and climate change mitigation and adaptation are significant. The high energy intensity of the economy and the slow progress towards meeting energy efficiency targets, in particular in the buildings sector, are holding back the productivity and competitiveness of businesses in the country. Efforts thus need to be stepped up to ensure that significant energy savings are achieved via targeted investments in the industrial, transport and buildings sectors. Increased investments in clean energy infrastructure (such as clean and low-carbon power generation, interconnections, and smart grids), in line with the priorities outlined in Bulgaria's draft national climate and energy plan, would further help improve the economy's overall competitiveness and people's quality of life.

(15) Despite an increase in the public research budget in 2018, research and development (R & D) spending remains very low in both private and public sector. Private R & D investment is dominated by large multinational companies and concentrated in the capital region. The slow pace of implementing reforms and high fragmentation in the research, development and innovation system hampers the contribution of R & D investment to productivity and growth. A large number of universities and research institutes continue to perform poorly in high-quality scientific research. Science-business links remain very weak and the availability of human capital in the R & D system is a source of significant concern. Clusters and their potential in Bulgaria are underdeveloped as they often lack a critical mass. Further reforms, combined with efficient governance and more effective public investment can maximise the impact on productivity and improve the competitiveness of the economy. In addition, increasing the digitisation of companies and introducing new business models are critical for the country's productivity.

(16) Public administration and e-government reforms continue to be slow and are yielding insufficient improvements while the business environment remains weak. A number of reform measures have been adopted, but their practical implementation is lagging behind. Institutional shortcomings, regulatory uncertainty, corruption, and an insufficient labour supply remain among the main obstacles to investment. Governance in the public sector could benefit from more transparency, clearer rules and a long-term perspective. Shortcomings are also apparent in the area of product testing and safety due to limited financial and human resources. Moreover, while the vast majority of measures included in the national procurement strategy have been adopted, their implementation requires continuous monitoring, control and assessment. The frequent use of direct awards and the high number of single bids represent a threat to the system's transparency and effectiveness. The public procurement sector's administrative capacity is an ongoing challenge, as are also the professionalisation of public buyers and aggregated purchases. The significant delay in the uptake of electronic procurement is preventing further improvement in the transparency and efficiency of public procurement processes.

(17) The labour market has improved but challenges remain. The employment rate has reached the highest level since Bulgaria joined the Union and the unemployment rate is below the Union average. Despite these positive developments, some groups such as the low-skilled, young people, Roma and people with disabilities still face difficulties to find work. Specific measures are being implemented to support the long-term unemployed, who represented 3 % of the active population in 2018. A combination of effective and sustained outreach measures, active labour market policies and integrated employment and social services could improve disadvantaged groups' employability and chances of finding work.

(18) Bulgaria's increasing skills shortages warrant significant investments. Young people might be more employable if the quality and effectiveness of traineeships and apprenticeships were improved. Moreover, the participation in upskilling and reskilling measures among the adult population is very low. Despite measures launched to encourage the development of digital skills, Bulgaria's level of basic digital skills (29 % of individuals possess basic digital skills against a Union average of 57 %) remains among the lowest in the Union.

(19) Despite the ratification of the International Labour Organization's Convention concerning Minimum Wage Fixing and of several rounds of negotiations during 2018, employers and trade unions still have diverging views on the criteria to be applied when setting the minimum wage. There is scope for greater consensus about an objective and transparent wage-setting mechanism. Meanwhile, although the involvement of the social partners in the design and implementation of policies and reforms seems to have increased, continuous support for a reinforced social dialogue remains necessary.

(20) Educational outcomes are still low and continue to be strongly influenced by parents' socioeconomic status. This reflects challenges relating to the quality and inclusiveness of the education and training system. Bulgaria invests insufficiently in education, particularly in pre-primary and primary education, two areas that are instrumental to creating equal opportunities from an early age. Participation in quality early childhood education and care is low, in particular for Roma and children from other disadvantaged groups. The rate of early school leaving is still high, with negative consequences for future employability and labour market outcomes. The labour market relevance of vocational education and training and the availability of dual vocational education and training remain insufficient. While some measures are underway, further efforts are needed to ensure that the skill set of higher education graduates can address short- and mid-term skills shortages in a consistent way. Some measures to retrain teachers and make the profession more attractive have been put in place. However, initial and continuous education programmes for teachers require further strengthening and efforts are still needed to improve the working conditions of education staff.

(21) Bulgaria is still facing high income inequality and risk of poverty or social exclusion. Though decreasing, the rate of poverty or social exclusion in 2018 was 32,8 %, still well above the Union average. The social security system does not cover all people in employment and the social protection system is insufficient to tackle the significant social issues. This reflects the low level of social spending, the uneven availability of social services across the territory and the limited redistributive effects of the taxation system. In 2018, the income of the richest 20 % of population was 7.7 times higher than that of the poorest 20 %, still one of the highest in the Union. Despite some measures, the adequacy and coverage of the minimum income remain limited and an objective mechanism for regularly updating it is still missing. Social services are hampered by low quality and lack of an integrated approach towards active inclusion. Disparities in access to social services, healthcare and long-term care persist. This undermines their ability to provide comprehensive support for the most vulnerable, such as the Roma, children, the elderly, persons with disabilities and people living in rural areas. Part of the population has difficulty getting access to affordable housing. More efforts are therefore needed to foster active inclusion, promote the socioeconomic integration of vulnerable groups including the Roma, enhance access to quality services and address material deprivation.

(22) The healthcare sector is still characterised by low public spending. People in Bulgaria face limited access to healthcare caused by an uneven distribution of limited resources and low health insurance coverage. Out-of-pocket payments are considerable, as they need to compensate for the low level of public expenditure. The low availability of general practitioners is constraining the delivery of primary care. There is a significant shortage of nurses with the number per capita among the lowest in the Union. Swifter and more effective implementation of the national health strategy would help tackle these weaknesses.

(23) Under the Cooperation and Verification Mechanism, the Commission continues to monitor the judicial reform and the fight against corruption and organised crime in Bulgaria. These areas are therefore not covered in the country-specific recommendations for Bulgaria, but are relevant for the development of a positive business environment in the country. The November 2018 Cooperation and Verification Mechanism report noted that Bulgaria had continued its efforts to reform its judiciary and address shortcomings in the fight against corruption and organised crime, but that further efforts were needed in a number of areas. The Commission expects to assess progress again in early autumn 2019.

(24) The programming of Union funds for the period 2021-2027 could help address some of the gaps identified in the recommendations, in particular in the areas covered by Annex D to the 2019 country report. This would allow Bulgaria to make the best use of those funds in respect of the identified sectors, taking into account regional disparities. Strengthening the country's administrative capacity for the management of these funds is an important factor for the success of this investment.

(25) In the context of the 2019 European Semester, the Commission has carried out a comprehensive analysis of Bulgaria's economic policy and published it in the 2019 country report. It has also assessed the 2019 Convergence Programme, the 2019 National Reform Programme and the follow-up given to the recommendations addressed to Bulgaria in previous years. The Commission has taken into account not only their relevance for sustainable fiscal and socioeconomic policy in Bulgaria, but also their compliance with Union rules and guidance, given the need to strengthen the Union's overall economic governance by providing Union-level input into future national decisions.

(26) In the light of this assessment, the Council has examined the 2019 Convergence Programme and is of the opinion ([7]) that Bulgaria is expected to comply with the Stability and Growth Pact.

(27) In the light of the Commission's in-depth review and this assessment, the Council has examined the 2019 National Reform Programme and the 2019 Convergence Programme. Its recommendations made under Article 6 of Regulation (EU) No 1176/2011 are reflected in recommendation (2) below,

HEREBY RECOMMENDS that Bulgaria take action in 2019 and 2020 to:

1. Improve tax collection through targeted measures in areas such as fuel and labour taxes. Upgrade the State-owned enterprise corporate governance by adopting and putting into effect the forthcoming legislation.

2. Ensure the stability of the banking sector by reinforcing supervision, promoting adequate valuation of assets, including bank collateral, and promoting a functioning secondary market for non-performing loans. Ensure effective supervision and the enforcement of the AML framework. Strengthen the non-banking financial sector by effectively enforcing risk-based supervision, the recently adopted valuation guidelines and group-level supervision. Implement the forthcoming roadmap tackling the gaps identified in the insolvency framework. Foster the stability of the car insurance sector by addressing market challenges and remaining structural weaknesses.

3. Focus investment-related economic policy on research and innovation, transport, in particular on its sustainability, water, waste and energy infrastructure and energy efficiency, taking into account regional disparities, and improving the business environment.

([7]) Under Article 9(2) of Regulation (EC) No 1466/97.

4. Strengthen employability by reinforcing skills, including digital skills. Improve the quality, labour market relevance, and inclusiveness of education and training, in particular for Roma and other disadvantaged groups. Address social inclusion through improved access to integrated employment and social services and more effective minimum income support. Improve access to health services, including by reducing out-of-pocket payments and addressing shortages of health professionals.

Done at Brussels, 9 July 2019.

For the Council
The President
M. LINTILÄ