



Brussels, 18.5.2016
COM(2016) 323 final

Recommendation for a

COUNCIL RECOMMENDATION

on the 2016 national reform programme of Bulgaria

and delivering a Council opinion on the 2016 convergence programme of Bulgaria

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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 policies¹, 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 imbalances², and in particular Article 6(1) thereof,

Having regard to the recommendation of the European Commission³,

Having regard to the resolutions of the European Parliament⁴,

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 26 November 2015, the Commission adopted the Annual Growth Survey⁵, marking the start of the 2016 European Semester of economic policy coordination. The priorities of the Annual Growth Survey were endorsed by the European Council on 17-18 March 2016. On 26 November 2015, on the basis of Regulation (EU) No 1176/2011, the Commission adopted the Alert Mechanism Report⁶, 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.

³ COM(2016) 323 final.

⁴ P8_TA(2016)0058, P8_TA(2016)0059, and P8_TA(2016)0060.

⁵ COM(2015) 690 final.

⁶ COM(2015) 691 final.

- (2) The 2016 country report for Bulgaria⁷ was published on 26 February 2016. It assessed Bulgaria's progress in addressing the country-specific recommendations adopted by the Council on 14 July 2015 and Bulgaria's progress towards its national Europe 2020 targets. It also included the in-depth review under Article 5 of Regulation (EU) No 1176/2011. On 8 March 2016, the Commission adopted a Communication⁸ presenting the results of the in-depth review. The Commission's analysis leads it to conclude that Bulgaria is experiencing excessive macroeconomic imbalances. In particular, the economy is characterised by remaining fragilities in the financial sector and high corporate indebtedness in a context of high unemployment.
- (3) On 15 April 2016, Bulgaria submitted its 2016 national reform programme and its 2016 convergence programme. 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 for the 2014-2020 period. As foreseen in Article 23 of Regulation (EU) No 1303/2013, 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 this provision in guidelines on the application of the measures linking effectiveness of the European Structural and Investment Funds to sound economic governance⁹.
- (5) Bulgaria is currently in the preventive arm of the Stability and Growth Pact. In its 2016 convergence programme, the government plans a gradual improvement of the headline balance to -1.9% of GDP in 2016 and -0.2% of GDP in 2019. The medium-term budgetary objective — a structural deficit of 1 % of GDP — is planned to be achieved as of 2017. According to the convergence programme, the government debt-to-GDP ratio is expected to peak at 31.8% in 2018 and to decline to 30.8% in 2019. The macroeconomic scenario underpinning these budgetary projections is slightly favourable. The measures needed to support the planned deficit targets starting with 2017 onwards have not been sufficiently specified. Based on the Commission 2016 spring forecast, there is a risk of some deviation from the adjustment path towards the medium-term budgetary objective in 2016 as well as in 2017, under unchanged policies. Based on its assessment of the convergence programme and taking into account the Commission 2016 spring forecast, the Council is of the opinion that Bulgaria is expected to broadly comply with the provisions of the Stability and Growth Pact. Nevertheless, further measures will be needed to ensure compliance in both 2016 and 2017.
- (6) Bulgaria made some progress in addressing last year's recommendation to make its healthcare spending more efficient, particularly by producing a national health map that will enable medical expenditure to be planned in accordance with territorial criteria and the needs of the population. The Bulgarian health system faces major challenges, including limited access, low funding and poor health outcomes. In spite of recent efforts to improve tax collection, the shadow economy remains a significant challenge affecting public revenues. Undeclared work, including under-reported

⁷ SWD(2016) 72 final.

⁸ COM(2016) 95 final.

⁹ COM(2014) 494 final.

remuneration and evasion of social security contributions, distorts the labour market and reduces fiscal revenue.

- (7) Cases of imprudent business practices across the financial sector, coupled with inefficient supervision, have created an environment for imbalances to accumulate. The completion, in a transparent way and according to best international practices, of the recently launched reviews of the banking, insurance and pension fund sectors and taking the necessary follow-up actions will strengthen confidence in the financial sector. Moreover, continued efforts to improve financial supervision, in both the banking and non-banking sectors, will play an important role in strengthening the financial system and positioning it to support the nascent macroeconomic recovery.
- (8) The labour market has experienced a modest recovery but remaining weaknesses continue to hinder growth and limit the adjustment capacity of the economy. Labour market adjustment is hampered by the structural nature of long-term unemployment, a shrinking and ageing labour force, low labour market participation and skills mismatches. While unemployment is gradually improving, there are still important challenges, for example as regards the long-term unemployed and young people not in employment, education or training. Active labour market policies could play a stronger role in helping these groups to access the labour market. The activation of people on social benefits is hindered by the fragmentation of, and limited cooperation between, different agencies delivering benefits and labour market integration services. Dedicated centres for employment and social assistance, which combine the services of the Employment Agency and the Social Assistance Agency, have been developed in a pilot project but no decision has been taken yet to roll out the project on a larger scale after it ends in December 2016.
- (9) Although Bulgaria's minimum wage is still the lowest in the EU, it has increased substantially since 2011 and the lack of objective criteria for minimum wage setting creates uncertainty. Despite work of the government and social partners in this area, Bulgaria still has no clear guidelines or transparent criteria for minimum wage setting that take into account its impact on job creation, social conditions and competitiveness.
- (10) Very high 'at-risk-of-poverty or social exclusion' and inequality levels remain in Bulgaria. Progress in addressing poverty and social exclusion is hindered by continuing challenges over integrating Roma into the labour force, facilitating school-to-work transitions, and improving the coverage and effectiveness of social, health and labour market policies. The general minimum income scheme provides very limited levels of support and outreach to the population. The allowance level is below the poverty line and has not been increased in line with average and minimum wage developments of recent years. Estimates on coverage indicate that a large part of the intended beneficiaries do not receive benefits. A better outreach to the target groups, while maintaining fiscal responsibility, would help to alleviate poverty.
- (11) The education system has limited capacity to include vulnerable groups and equip learners with relevant skills. Vulnerable groups such as Roma and pupils from poor families continue to face significant obstacles in accessing and completing education. The level of enrolment among Roma at all levels of education is significantly lower than for non-Roma. The early school leaving rate continues to increase and is particularly high in rural areas and less developed regions. Removing barriers to the participation in early childhood education of disadvantaged children is essential to increase educational outcomes and prevent dropouts. A new Pre-school and School

Education Act adopted by the parliament in September 2015 is an important step towards a comprehensive reform of the school system. The implementation of this legislation, together with targeted measures to overcome non-legislative barriers to the full participation of disadvantaged groups in education, should contribute to improving the Bulgarian economy's growth potential and social cohesiveness in the long term. Enrolment and graduation rates in tertiary education are on the rise and the employment rate of recent graduates is recovering slowly, although it remains significantly below the EU average.

- (12) Risks stemming from high corporate debt and barriers to deleveraging remain significant. The existing insolvency framework provides little scope for an effective debt workout process and does little to address the high level of corporate indebtedness. Reforms to facilitate corporate insolvency procedures could improve deleveraging and lead the way to new lending and investment.
- (13) The public procurement system in Bulgaria continues to suffer from structural weaknesses, including systematic irregularities in procurement procedures, lack of administrative capacity and deficient control mechanisms, combined with systematic court appeals that often delay works on the ground. The transition to full e-procurement has made only limited progress. The shortcomings of the Bulgarian public procurement system have led to interruption of payments and financial corrections in EU funding programmes and also affect the wider business environment.
- (14) Unstable policies and lack of trust in key public institutions, such as the judiciary, constitute significant deterrents to investment in the Bulgarian economy. The slow implementation of public administration reforms and reforms in specific sectors such as research, innovation and energy hamper progress in improving the investment climate. Although Bulgaria has adopted a strategic framework to reform and modernise its public administration, progress is slow and implementation often postponed. New legislation is not subject to systematic impact assessment, although there have been some efforts to change this. Frequent changes to the legal framework create uncertainty and affect the businesses environment. Corruption remains a significant concern and the national authorities' response to this problem continues to be hampered by weak and fragmented institutions. Under the Cooperation and Verification Mechanism, Bulgaria receives recommendations on judicial reform and the fight against corruption and organised crime. While these areas are of crucial importance for the overall business environment, they are therefore not covered in the country-specific recommendations for Bulgaria.
- (15) In the context of the European Semester, the Commission has carried out a comprehensive analysis of Bulgaria's economic policy and published it in the 2016 country report. It has also assessed the convergence programme and the national reform programme and the follow-up given to the recommendations addressed to Bulgaria in previous years. It has taken into account not only their relevance for sustainable fiscal and socioeconomic policy in Bulgaria but also their compliance with EU rules and guidance, given the need to strengthen the EU's overall economic governance by providing EU-level input into future national decisions. The recommendations under the European Semester are reflected in recommendations 1 to 4 below.

- (16) In the light of this assessment, the Council has examined the convergence programme, and its opinion¹⁰ is reflected in particular in recommendation 1 below.
- (17) In the light of the Commission's in-depth review and this assessment, the Council has examined the national reform programme and the convergence programme. Its recommendations under Article 6 of Regulation (EU) No 1176/2011 are reflected in recommendations 1 to 4 below.

HEREBY RECOMMENDS that Bulgaria take action in 2016 and 2017 to:

1. Achieve an annual fiscal adjustment of 0.5% of GDP towards the medium-term budgetary objective in 2016 and in 2017. Further improve tax collection and take measures to reduce the extent of the informal economy, including undeclared work.
2. By the end of 2016, finalise the asset quality review and stress test of the banks. By the end of 2016, complete the balance-sheet review and stress test of the insurance companies and the review of private pension funds' assets. Take the necessary follow-up actions in all three sectors and continue to improve banking and non-banking supervision.
3. Reinforce and integrate social services and active labour market policies, in particular for the long-term unemployed and young people not in employment, education or training. Increase the provision of quality education for disadvantaged groups, including Roma. Improve the efficiency of the health system by improving access and funding, and health outcomes. In consultation with social partners establish guidelines and criteria for setting the minimum wage. Increase the coverage and adequacy of the minimum income scheme.
4. Reform the insolvency framework to accelerate recovery and resolution procedures and improve their effectiveness and transparency. Increase the capacity of the courts regarding insolvency procedures. Strengthen the capacity of the Public Procurement Agency and contracting authorities and improve the design and control of public tendering procedures. Speed up the introduction of e-procurement.

Done at Brussels,

*For the Council
The President*

¹⁰ Under Article 9(2) of Council Regulation (EC) No 1466/97.