

Part I

**Restructuring
State Enterprises
in Bulgaria**

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1. Specifics of Economic Structure at The End of The 1980s.

The knowledge about the characteristics of the economic system at the start of the reform period is of considerable significance for understanding its behaviour in the new conditions and forecasting its further changes. This applies especially to those of its elements which reflect the nascent market relations and/or the structure of the economic system. In order to characterise the economic structure of a country, one should consider the ownership structure, the organisation-and-management structure, the patterns of enterprises and the organisation and nature of their relations.

1.1. Ownership Structure

Bulgaria was among the countries with the highest share of state ownership. A further argument to this conclusion is the fact that cooperative ownership has been turned into a variety of state ownership and the two of them covered 99,9% of the national economy in the 1970s.

A steady policy of restriction and liquidation of private ownership and merger of cooperative and state ownership has been pursued even till mid-70s when a compulsory purchasing of the last private units in craft industry and trade took place. The creation of agro-industrial complexes made cooperative ownership in agriculture de jure equal to state ownership.

In the next years, shifts in the ownership pattern were observed in two directions mainly. First, ways had been searched for the autonomizing of state owned enterprises. There was a very brave attempt witnessed in 1987, when by a declaration of the Parliament state ownership was committed to workers' collective to manage it. To this end, contracts should have been concluded sharing the ownership rights between the state and the workers' collective, and the General Meeting of Workers was to become the chief body of enterprises management. Given the preserved centralised character of economy and minimal opportunity of self-initiative, however, the greater part of workers collective (especially in enterprises with worse than average conditions) did not sign the contracts and the experiment proved to be a failure. Since the beginning of 1989, the rights of the General Meeting of Workers were restricted as 50% plus one of the Governance Board members were nominated by the state.

The second direction of shifts in the ownership structure was related to the admittance of some new specific patterns of private ownership. The first of them were the so-called individual farms. Within a very short time, they accounted for about 30 to 50% of the production of certain agricultural goods, mainly in cattle-breeding and vegetablegrowing. Another pattern of private ownership was for the first time since decades recognised equal in rights to the others, and citizens were allowed establishment of individual, collective and partnership firms. In 1989 the number of registered firms was 9583, of them 7875 individual, 1592 collective and 116 partnerships, in other words, 82% of firms have one employee, i.e. the owner. Actually, their number was much greater – more than 45 000 according to some estimations, it should be taken in mind, however, that 90% of them were private taxi-cabs.

Most of the established farms and firms are small-sized, individual or family businesses which are dependent and subordinate in behaviour. Actually, private activity is rather an additional source of incomes than a factor influencing the changes in ownership structure and contributing to the creation of conditions favourable to market relations development.

1.2. Organisational Structure and Subordination of Enterprises

The organisation-and- management structure of the Bulgarian economy in 1989, as described by Decree 56, was radically different from that in previous periods and rather close to the structure of market economies. There were no branch ministries and a Planning Committee, enterprises were the main entities and they could unite in groups, associations or other organisations to fulfil part of their functions, their relations were regulated on a contract basis.

In order to have a more precise and comprehensive understanding of the real state and character of economic organisation, one should consider the management-organisational structure of Bulgarian economy in the previous years as many of its characteristics were still existent in 1989.

The Bulgarian version of a reform of centrally managed economy is characterised by the presence of intermediate management bodies between the ministry and the enterprise. They vary considerably in range and names. The economic groups proved to be the most stable and long-standing organisation form; usually, they integrated the enterprises in a certain subindustry. In case the number of enterprises exceeded 30 or 40, then the economic group was created on a lower level. In the period from 1976 to 1978 the so-called committees were formed in machine-building; due to the great number of integrated enterprises (from 26 to 67), however, they were soon transformed into smaller groups.

Another form of enterprise integration was the Economic Combine. It was built up on a lower level and had a narrower scope. Economic combines existed either independently or as parts of the economic groups. During the period 1981-1986 they were considered the main economic units.

Changes were also taking place in the scope and name of higher management bodies and organisations. For the longer part of the period considered, branch ministries were

the intermediaries between the economic center and enterprises (economic groups). Though short-lived, the so-called National Economic Complexes integrated enterprises in several close or mutually dependent branches came into being as well. In 1976-1978 they were even considered the main units in the national economy. The formation of industry-based Associations began since 1986. The total of 12 associations were created and the branch ministries were integrated in the Ministry of Economy and Industry.

It is pretty obvious that the Bulgarian economy has been experiencing a non-stop reorganisation and quite dynamic changes all the time. As a rule, changes in the structure or status of economic bodies and organisations had been initiated each five years, in line with the successive Congress of the ruling Communist Party or even between whiles. Changes were of rather ostensible character and did not reflect a real strive towards creation of market relations. Actually, the main concept of the nature of socialist economy and its mode of management remained unaltered.

The proclaimed goal of economic reforms undertaken in the mid-60s was the substitution of economic for administrative way of management of main entities. In practice, this concept affected economic organisation in the following ways:

First, decrease in the number of managed units through creation of groups of enterprises. This ambition was so strong that it resulted in the following paradox: after 1986 when enterprise was declared the basic economic unit in industry not a single independent enterprise actually existed, unlike in previous years when the largest plants were directly subordinate to the branch ministries.

Second, decentralisation of part of the functions on management, coordination and distribution.

Third, estimation of the activity of enterprises groups in terms of not only administrative but some economic indicators as well. The viewpoint was essentially prevailing that production and economic processes in the public economy were related similarly to those in a factory and the problem was to merely determine the optimum scope of its subsystems and the centralism-decentralism ratio.

The changes in the beginning of 1989 were the most radical ever made; anyway, they were to a high extent affected by the former state of economic organisation. Firm organisation was declared the basis of economic activity but the greater part of groups were preserved and just formally re-named into firms. The Planning Committee was no longer existing but state plans, state orders covering up to two-third of firm capacity remained. In its prevailing part, economic activity was regulated by firm rules and normative acts. Although declared one of the bases of economic activity, along with planning and regulation functions of the state, market faced enormous difficulties in the process of its emergence and functioning. In fact, the adoption of Decree 56 in 1989 was only a simulation of market institutions and not a creation of real market relations.

1.3. Pattern and Size of Enterprises

Enterprises are the most stable pattern of economic activity and therefore their variety in size, i.e. small, middle and large scale (multiplant enterprises), is one of the

most significant features of industrial structure.

Industrialisation in Bulgaria was carried out in the 1950s and the 1960s on the basis of technics and technology typical of that time and characteristic of the second stage of development of machine production and its inherent enterprise pattern, the one-plant enterprise.

In the 1970s the necessity emerged of both horizontal and vertical integration of one-plant enterprises with view to creating conditions for their transformation into multiplant enterprises. The Economic Groups established, however, were only horizontal and included automatically all enterprises in a subindustry, while the specialised units dealt with non-production activities mostly.

The situation changed after 1976 when the setting-up of Economic Combines started and especially after 1981 when they were wide-spread in the economy. Combines were considered a pattern of organisation of itself which created possibilities for changes in the primary production unit, they comprised a small number of enterprises, 3 to 6 in average, and integrated both horizontal and vertically, i.e. there were grounds for their transformation into a united production and economic entity.

As was mentioned above, Economic Combines were intermediary management and coordination organisations. This dual nature resulted in a number of combines greater than that of emerging multiplant enterprises. Notwithstanding, the latter exist and this circumstance should be paid due attention in the processes of decentralisation, demonopolisation and privatisation of Bulgarian economy.

In some subindustries (heavy machine-building, for example) multiplant enterprises were created through new construction. One should, however, take into consideration the difficulties faced by centrally planned economies in accomplishing the changes in enterprise pattern through mergers, concentration and specialisation, based on enterprises' initiative.

Another specific feature of socialist economy was the neglecting of small enterprises. They were long treated as a foreign substance or a means for solving social problems, e.g. employment in small cities. Unlike some other socialist countries, in Bulgaria this concept was to a great extent overcome and the implementation of a Programme for building small and medium-sized enterprises was initiated in the beginning of 1981. Enterprises set up under this Programme were characterised by modern equipment, high productivity and efficiency and high quality of produce. Given this, the Programme was extended in 1984 and more than 2000 small enterprises were envisaged to be established till 1990.

After 1986 the accomplishment of the Programme went on a very slow pace and in 1990 it was actually abandoned. There were several reasons for that. First, Bulgaria was experiencing a rising deficiency of convertible currency and the greater part of small enterprises equipment had been imported from the developed capitalist countries. Second, contradictions had emerged between the high-profit small enterprises and the economic organisations they were subordinate to, connected with redistribution of profit. The arguments were that the large enterprise had participated in the design and construction of the small one. A problem like that could have been easily settled in the presence of

corporate ownership and not in the conditions of public ownership, anyway.

The number of modern small enterprises established in Bulgaria in 1981-1988 totalled to about 200-250. They still are among the most attractive subjects of privatisation, including for foreign investors. Moreover, the experience accumulated in creating conditions by the state for the development of small enterprises could be very useful in the period of restructuring of Bulgarian economy.

1.4. Principles of Management

The model of state enterprises management in the conditions of centralised economy (as was the Bulgarian case, too) was characterised by: fixed plan indicators and results reporting before the higher authorities; centralisation of enterprise profit in the budget and its top-to-bottom redistribution; regulated use of profit residual in enterprises; centralised appointment of directors, etc. Management was executed by two parallel structures, i.e. a purely production and a socio-political structure, represented by the local units of the Communist Party, the Comsomol and the trade unions.

The main shortcoming of this model was the absence of interest and initiative on the part of workers and managers in rising the efficiency of production organisation and management.

The first attempts to change the principles of management of economy dated back to the mid-60s. They were directed at increasing the economic independence of enterprises, i.e. reduction of the number of centrally fixed plan indicators and implementation of some market economy instruments (profit, in particular) for promotion of management efficiency.

These changes were accompanied by enlargement of production structures and introduction of new management units. By the end of the 60s enterprises were integrated in state economic groups. In its relationships with the latter, the Center applied some elements of the new mechanism, but the structure and mechanisms of enterprises remained unchanged.

At the same time, the multi-tier system of management made for the stronger bureaucratisation of the latter and further alienated producers from the final results of their work. Economic groups were therefore rejected and enterprises regained their role of basic economic units. The low rates of growth at the end of the 1970s pressed the state to re-estimate the management approaches.

The concept was then born about the 'new type of brigade' as a basic economic unit which had been allowed building-up of independent accounting and labour remuneration system within the enterprise. The system of so-called counterplanning was implemented aiming at the complete mobilisation and use of enterprise's resources.

Radical changes in the principles of economic management took place in the early 1980s and especially after the adoption of the new Labour Code. Compared to those in the previous years, they were characterised by: first, inclusion of all levels and structures of management in the enterprise; second, a new conceptual basis of the worker-enterprise relationship, on the one hand, and enterprise relationship on the one hand and enterprise-state relationship on the other. This concept found expression in the formula

'The state is the owner, the workers' collective is the stopanin'.¹

It was for the first in the socialist economy practice when the workers' collective had been assigned management functions. The procedures were also worked out of transferring the property of the state to be managed by the workers' collective. The new model of management envisaged also a change in the source of external pressure over enterprises, i.e. from central plan to market. The market and the workers' collective had to determine the dynamics and structure of production.

The concept about the workers' collective as a stopanin of state property introduced thorough changes in the internal structure of management as well. The General Meeting of Workers turned into the main management body which was responsible for the choice and appointment of the enterprise director. From its very beginning this practice proved to generate complete elimination of the social-and-political structures of enterprises which seriously endangered the political role of the Communist Party in the management of economy. The adopted in January 1989 Decree 56 on the Economic Activity actually stopped the democratisation of management relations and introduced the principle of firm management of economy. Some of its articles contradicted the Labour Code and were gradually abolished.

2. Macroeconomic Changes and Creation of Market Environment for the Functioning of Enterprises after 1990

Bulgaria started economic reforms under rather unfavourable conditions. It was most closely related and respectively dependent on the former CMEA and Soviet Union markets. The moratorium on foreign debt servicing of March 1990 resulted in the country's isolation from the international financial markets. The national economy still suffers the consequences of the moratorium although an agreement was made with the London Club banks providing for reduction and rescheduling of the debt. Despite the serious problems with the agreed debt serving this is perhaps the best achievement for the five years of the reform.

The Persian Gulf crisis and the Yugo-embargo contribute additionally for the collapse of the Bulgarian economy. The internal situation is far from less disturbing. From its past, Bulgaria inherited considerable imbalances, i.e. excess of solvent demand over supply, high capital and energy intensity of the industrial production, etc. The relative political stability was marked by the slow-pace solution of the avalanche-growing problems implying urgent and unpopular measures. These are partly the reasons which caused the implementation of economic reforms under the conditions of an unprecedented economic slump ever seen throughout the contemporary Bulgarian history.

¹ The term "stopanin" in its economic, social and political sense has not a direct equivalent in English. The nearest are "manager", "supervisor", "administrator"; but the term was used at the same time in political discourses.

2.1. Dynamics of Gross Domestic Product

It is since recently that the National Statistical Institute of Bulgaria (NSI) has been calculating the Gross Domestic Product (GDP) of the country. Formerly, data was published only on National Income and Social Product as according to the method of Material Product (Material Balances). The calculation of GDP is done on the basis of correlating the two accounting systems, i.e. of Material Product and of National Accounting.² As foreign and Bulgarian experts point out, this methodology has partly caused the significant discrepancy in different estimation of GDP.³ Besides, this is the reason for the differing forecasts of GDP dynamics. The question here normally arises about the horizon of business revival in Bulgaria. The Bulgarian economy is obviously very close to the "bottom". The expected stabilisation on a rather low level can hardly provide grounds for forecasting a relatively stable growth in the near future. The greatest decline in GDP was recorded in 1991. According to different estimations, in comparison to the previous year the reduction varied between 16.7 percent⁴ and 11.7 percent.⁵ The decline gradually calmed down in the next years. Yet, the figures for 1994 – 1995 are not very optimistic.⁶ The growth from these two years has compromised in (Table 1).

Table 2.1.

Bulgaria: Selected Macroeconomic Indicators

	1990	1991	1992	1993	1994	1995 Est	1996 proj.
Gross Domestic Product (%)	-9,1	-11,7	-7,3	-2,4	1,8	2,6	-4,0
Industrial Output (%)	-16,0	-27,8	-15,0	-11,8	7,8	8,6	-
Inflation, CPI, annual average (%)	26,3	333,5	82,0	73,0	96,3	62	-
Unemployment rate (as % of labour force, end-year)	1,5	11,5	15,6	16,4	12,8	10,5	-
General government balance (cash balance) in % of GDP	-	-	-13,0	-10,9	-5,8	-5,7	-5
Trade Balance (mln USD)	-	-	-212,4	-885,4	-16,8	431,8	-
Gross external debt (billion USD, end-year)	-	-	12,6	12,9	10,8	10,4	-

Source: Economic Transition in eastern Europe and the former Soviet Union, Transition report, 1996; NSI.

² National accounts for Bulgaria, sources, methods and estimations, OCDE and NSI, Sofia, 1996; Statistical Bureau of UNO, document F-20.

³ See La Bulgarie – Evaluation de la situation économique. OCDE, 1992.

⁴ The economy of Bulgaria till 1996. Sofia, 1993, pp. 29-39, 114-115.

⁵ PlanEcon Rewiev and Outlook for Estern Europe, December, 1993, p. 62.

⁶ Economic Transition in Eastern Europe and former Soviet Union, EBRD, Transition Report, October. 1994; Transition report 1996, Infrastructure and savings, EBRD, 1996.

The GDP changed considerably in structure. The sharp shrinkage in industry, construction and agriculture resulted in a decrease of their relative share at the expense of services which are continuously expanding. Regarding services, one should bear in mind that their growth is also due to the higher prices in this sector. (Table 2)

Table 2.2.

Structure of GDP

	Mln. Leva, current prices				
	1992	1993	1994	1995	1996
Agriculture and Forestry	23329	29694	60184	111041	
%	11,6	9,9	10,9	12,7	
Industry	78417	97708	180790	272699	
%	39,0	32,7	31,7	31,3	
Services	92005	151735	268668	401262	
%	45,8	50,7	45,9	46	
GDP	200832	298934	548015	871396	
%	100	100	100	100	

Source: Statistical Reference Book, NSI, 1996, 188-189.

In 1993 – 1995, positive growth rates were recorded in some industries including metallurgy, chemistry, and printing and publishing industry, the latter being in a good condition from the very start of reforms. A nucleus of big state enterprises is developing which successfully adapt to the shocks of transition. The prevailing part of enterprises, however, are in a heavy financial condition. The lack of adequate bankruptcy regulation and delay of settlement of state enterprises "bad debts" accumulated after 1990 is making for the continuing allocation of national savings with inefficient activities. The first signs of revival in industry have been neutralised by the negative results in agriculture.

The unprecedented slump in the Bulgarian economy has been caused by factors which are still working.

They can be classified into two main groups, namely: first, factors related to reduction in demand, and, second, factors related to problems of supply.

The first group of factors include the sharp decline of Bulgarian exports to the CMEA area, the deterioration of Bulgarian terms of trade amounting to nearly USD 600-800 million, the reduction and subsequent actual disappearing of investment demand, the formation of undesired production stock etc.

The second group of factors stem from relative prices modification in favour of the first-echelon industries; this might result in the disappearance of branches of high relative value added share. This modification is seriously restraining the possibilities for

economic restructuring. The difficulties in financing Bulgarian imports, which result from foreign debt problems, are acting in the same direction.

The crisis in 1996 showed that in result of not executing of the inevitable structural reforms the unfavourable action of these factors increases.

2.2. Inflation and Antiinflationary Policy

Following vain discussions on the issue of what to start reforms with, i.e. demonopolisation and privatisation or liberalisation of prices, Dimitar Popov's coalition government made what seemed to be the only possible step – liberalisation of all prices – with the exception of- but those of 14 commodity groups.

Parallel measures were undertaken for partial compensation of incomes. Besides, there were attempts to demonopolise the economy through the opening up of the existing units (and respectively the change of their governments).

Subsequently, the commodity groups under control were further reduced by seven. Under control remained the prices of fuel, energy, and some services as transport, communications etc. Except for the activities of the State Price Inspectorate, which has very limited functions, government intervention in price formation is practically non-existent. For a full liberalisation of the prices was spoken up after the crisis 1996 in the eve of the introduction of the Monetary board.

The combination of price liberalisation and foreign-trade regime liberalisation, on the one hand, and the enacting of domestic convertibility of the BG Lev, on the other, made the Bulgarian economy suffer serious price shocks. According to data of European Bank for Reconstruction and Development, the consumer price index in 1991 was 339 percent, in 1992 – 79 percent, and in 1993 – 64 percent etc. Unfortunately the pessimistic expectations of the bank for 1996 were increased twice. In the end of 1996 and the beginning of 1997 Bulgaria faces hyperinflation process.⁷ (Table 1)

Following price liberalisation, the scissors opened between consumer and producer's prices. The latter are considerably lagging behind consumer prices. In the period 1991-1992, the low prices maintained by regional purchase organizations (monopsony) had a certain restraining effect on inflation. This situation began changing in 1993, although the relative prices in agriculture still make for the rather heavy situation in the sector. The average monthly inflation rate in 1993 was 0.7 points lower than in 1992. The dynamics of consumer price index in 1993 was due mainly to the quick rise in the prices of some services resulting from the growth the controlled prices of energy, fuel, transport and communications.

The 1994 increased inflation rate is due to both the enforcement of the Value Added Tax Act which was not relevant to the local environment, and the currency market crisis which caused considerable depreciation of the Bulgarian Lev.

The avoidance of inflationary spiral remained a priority of economic reforms. In spite of this after the relatively stable 1995 Bulgaria appeared in dramatic economic

⁷ Transition report 1996, EBRD, p. 113; National Institute of Statistics.

situation and is facing the "loop" of hyperinflation.

Due to all that the antiinflationary policy is based on reduction and restructuring of budget expenditures. Price liberalisation brought forth removal of subsidies. The important problem here is the high level of budget deficit and its financing mechanism in the conditions of monetary restriction. (Table 3; Table 4) Given the almost vital delay in structural reforms, further hardening of budget restrictions makes financial discipline even worse. The inflation-generating interfirm indebtedness is increasing as well.

Table 2.3.

General Government Operations: Revenues, Expenditures, and Fiscal Balances (In percent of GDP)

	1988	1989	1990	1991	1992	1993
Revenues	57,5	58,0	53,3	42,3	37,0	30,6
Expenditures	58,4	61,4	64,3	50,7	43,9	41,7
Fiscal Balances	-0,9	-1,4	-12,7	-15,1	-14,0	-13,5

Sources. NSI, FMI staff estimates.

Table 2.4.

General Government Operations at 30 of November (mln. leva)

	1994	1995	1996 '
Revenues	118834,0	176536,7	278570,6
Expenditures	150926,8	232205,5	432727,8
Fiscal Balances	-32092,8	-55668,8	-155857,3

Sources: Information bulletin, BNB, 1994-1996.

Table 2.5.

*Money Supply, Bulgarian National Bank Exchange Rate
and Interest Rate (Mln Levs)*

	1992	1993	1994	1995	1996
Broad money	158567	234072	418009	583663	-
Money (M1)	37833	48303	75131	107886	-
Quasi -money	117149	181619	333978	463419	-
Exchange Rate – Levs/USD (end of the period)	24,429	32,711	66,015	70,704	-
Interest Rates (end of the period)	41,0	52,0	72,0	34,0	

Sources: Statistical Reference Books, NSI, 1994-1996, Sofia.

The Bulgarian National Bank succeeded in maintaining a relatively stable rate of BG Lev till the autumn of 1993 (the absence of stabilisation fund, however, hampered its use as an anchor of economic stabilisation). After that and especially since the March, 1994 the currency rate became an important pro-inflation factor. (Table 5). In 1996 the Bulgarian lev depreciated over 4 times to the USD. The economy could not stand long postponed structural reforms and the serving of the foreign debt.

Monetary and incomes policy have been and still are the main components of antiinflationary policy.

Monetary policy relies on administrative and "quasi-market" instruments, i.e. high interest rate, credit ceilings, and some forms of trading idle credit funds; determined by the Bulgarian National Bank. Restrictive monetary policy limited the growth of money stock below the inflation rate. This was particularly noticed in 1993.⁸ (Table 5)

The continuing restriction has its negative effects, too, as credit flows increasingly gravitate to "bad" loans. This is inevitable in the absence of a strict bankruptcy regulations and state strategy of large enterprises restructuring.⁹

It is a common opinion that the incomes policy in Bulgaria has not been restrictive to the full. That's why stabilisation in Bulgaria is considered rather of mixed than orthodox character. Perhaps, it was exactly the situation in the first years of system changes when the principle of collective bargaining was accepted.

⁸ Analytical Review of the Bulgarian Economy in 1993. Agency for Economic Forecasts and Development, Sofia, 1994.

⁹ Externely interesting study of the monetary polisy in the transition economies is made by N. Nenovski in his dissertation: "Money Market in the Transforming Economies (theoretical analysis and econometric studies of the example of Bulgaria)", Sofia, 1996.

Subsequently, given the sharp reduction of possibilities for budget manoeuvres (especially after the expected introduction of Monetary board), the hardening of budget restrictions on non-financial public sector and wage freeze seemed inevitable.

2.3. Unemployment

The successful course of economic restructuring depends on the level of unemployment. It is well-known that when unemployment exceeds a certain level society gradually loses patience. In Bulgaria, like in Poland and Romania, unemployment is very close, if not above the socially admissible limit. Unemployment in Bulgaria is accompanied by worsening of the demographic situation. Population growth rates have been negative since years, down to -2.9 per thousand in 1993 and to -5,0 per thousand in 1995. The average age increased from 37.5 years in 1991 to 38.7 years in 1995. By the end of 1995, the working age population numbered 4,745,423. From them to the end of 1995 employed are 3310,9 million persons. (Including 1902,3 million employed on labour agreement in the public sector).¹⁰

Table 2.6.

Unemployed Persons Registered at the Employment Offices, 1990-1995

Year	January	June	December
1990	—	—	65079
1991	74134	233724	419123
1992	426017	475822	576893
1993	578788	586538	626141
1994	631987	508638	488442
1995	499176	408453	423773
1996	-	-	-

Source: Main Macro Economic Indicators 1991-1995, NSI, Sofia, p. 105.

According to data of NSI, by the end of 1995 the rate of unemployment was 11,1 percent. The number of registered unemployed increased from 65 thousand in 1990 to 423773 thousand in 1995. The situation was extremely hard in 1991 when unemployment manifested a sudden rise from 65 thousand to more than 400 thousand. (Table 1, Table 6) The average monthly rate of unemployment decreased from 1.48 percent in 1992 to 0.86 percent in 1993.

There is a certain "normalising" of the unemployment structure by qualification. It is highest with low-qualified people and lowest with specialists. What is disturbing, however, is that about half of the unemployed are below 30 years old. The greatest decline in employment has been registered in industry and agriculture. Services mark a relatively stable level of employment, and the only increase has been observed in the financial sphere.¹¹

¹⁰ General macroeconomic indicators 1991 -1995, NSI, Sofia, 1996; Statistical Reference Book, 1996.

¹¹ See, J. Christoskov, *Mam tendencies in employment and unemployment in Bukgaria*. Ikonomicheska Missal, 1993, № 11.

Presumably, the acceptance and enacting of the Fourth chapter of Trade Law determining the failures will bring about the closing of enterprises of 300 thousand employees. In the announced for liquidation from the Videnov cabinet about 60 enterprises are employed over 60 thousands people; and the enterprises from the so-called "isolation" scheme – more than 200 thousands. These lists are abolished by the official Sofianski cabinet but the extremely serious and painful problem with the closing of the losing enterprises remains. In the middle run, the number of unemployed in Bulgaria is expected to "stabilise" at about 450-500 thousand. According to the official 1995 data a lower number of the registered unemployed individuals is reported. (Apparently, this is due to the increased number of the non-registered unemployed individuals which is normal under high unemployment rate.) In the same time the series of laws providing the legal framework of economic reforms and state enterprises restructuring is not finished by those closely related to business and production. Laws on social issues are also institutions of free market economy and bear direct relevance to securing the economic reforms. The lacking balance and complementarity between strictly economic and social laws, and the underestimation of the latter (in Bulgaria, in particular, it found expression in the continuous neglecting of the Labour Code and in the absence of Law on Employment), bring about social tension and discredit on the reform.

2. 4. Opening of Economy

Macroeconomic stabilisation was attended by the initial steps of opening of the Bulgarian economy. These included implementation of floating exchange rate¹² and removal of the allow-and-ban regime of foreign trade transactions and quantitative import restrictions. Subsequently, the latter was to a certain extent regulated by the imposed import taxes. Subsidies were also abolished on goods imported for production of export commodities. On 1 July 1992 Bulgaria introduced a new custom tariff. It is oriented to a rise of import duties. The average increase of duties amounted to 17.8 percent, including the formerly introduced import taxes. Experts, however, expect a lower real increase.¹³ These measures, along with import quotas, additional duties, anti-dumping import regulation, etc. make for the conclusion that – at the first stages of the reform – the liberalisation of foreign trade in 1991 and the beginning of 1992 has been gradually yielding room to protectionism.¹⁴ The policy from 1992 was continued in 1993, 1994 and 1995. Practically each government announces before the beginning of the calendar year a list of goods the trade with which (mostly their export) is determined in a specific way. During the year a different ad hoc modifications are made¹⁵.

¹² BG Lev will be fixed to one or some west currencies (may be dollar/mark) with the introducing of Monetary board.

¹³ See, T. Houbenova-Delisivkova, The association of Bulgaria to the European Community – possibilities and perspectives. *Ikonomicheska Missal*, 1993, № 1.

¹⁴ Analytical Review of the Bilgarian Economy in 1993. Agency for Economic Forescast and Development, Sofia, pp 93

¹⁵ R. Dobrinski, Current state and prospects of Bulgarian exports, Bucharest, may 1996, mimeo

One can hardly expect something quite different, having in mind the problems of import financing and the fact that Bulgarian export is dominated by resource intensive sectors. Nevertheless, a step-by-step decrease in duties is envisaged aiming at the formation of free-trade zone between the European Community and Bulgaria within the next ten years.

Three important circumstances determine the national frame of the foreign sector of Bulgaria after the disintegration of CMEA:

1) From 1 February 1995 Bulgaria is associated member of the European Unions. Foreseen is the creation of Zone for Free Trade between the European Unions and Bulgaria. The Bulgarian government ratified the three additional protocols to the European agreement concerning the trade with textile goods and clothes; temporary agreement on trade; the quantity limits upon the pherometals and goods from them, coals, etc.

2) On 2 October in Geneva was signed the Protocol for association of the country to the Marakesh agreement for creation of World Trade Organisation. With this act Bulgaria engaged with the packet of agreements concerning the rules and norms in applying its national trade policy for the movement of goods between the member countries; concerning the trade with services; as well as concerning the protection of the rights of the intellectual property.

3) The agreements for creation of zone for free trade between Bulgaria from one side and Chech Republic and Slovakia from the other dated from the beginning of 1996. These agreements lay on the institutional base of the association of the countries to the European Unions and of their membership in the World Trade Organisation and create perspectives for the association of Bulgaria in CEFTA.

There was a sharp reduction in the volume of foreign trade after the collapse of CMEA and the start of system changes. Besides, specific difficulties emerged related to its accounting. According to OECD experts, the Bulgarian statistics does not record about one-third of the foreign trade turnover of the country. Discrepancies also exist between the information provided by the National Statistical Institute on the basis of customs declarations, on the one hand, and that of the Bulgarian National Bank on the basis of settlements of commercial banks accounts, on the other. Another problem of similar nature is the accounting of trade in terms of US dollars.

At the first stage of the transition Bulgaria paid a lot the consequences of its considerable commitment to the former CMEA and the former Soviet Union. According to some estimations, the value of Bulgarian exports in current prices fell from USD 6.65 billion in 1989 to USD 3.40 billion in 1992; the value of imports respectively decreased from USD 7.33 billion to USD 3.36 billion. To make a comparison, during the same period the Hungarian exports grew from USD 9.67 billion to USD 10.68 billion, and its imports – from USD 8.86 billion to USD 11.12 billion. A sharp decline was recorded in Bulgaria's turnover with the East European Countries, i.e. from USD 7.51 billion in 1989 to USD 2.65 billion in 1992. The same situation was observed with regard to the OECD

countries from USD 4.01 billion to USD 3.0 billion. The decline was due to the sharp reduction in imports.¹⁶

The commodity structure (Harmonised system – HS) of Bulgarian foreign trade underwent considerable shifts. At present, fuel, minerals and metals are the most important items of exports. Next come foodstuffs and chemicals. In 1992, the export of investment goods was reduced down to 12 percent. The import is dominated by fuel, minerals and metals. Their relative share was 60 percent in 1991 and 40 percent in 1992. The import of investment goods was thus reduced to 10-15 percent.¹⁷

According to newer study of the Bulgarian trade with industrial goods with the countries from the European Union (...U-12) for the period 1990-1994 the Bulgarian export increased from 436 mln. USD to 1 211 mln. USD. The percentage of the goods from 06 and 08 (by SITC), where are respectively ferrous and non-ferrous metals and textile and swing industry is higher. At the same time the Bulgarian import of industrial goods (positions 05-08 – SITC) from the Union increased from 956 mln. USD to 1451 mln. USD. The goods from 07 (equipment and transport vehicles) are with the greatest percentage. The Bulgarian deficit from the trade with goods from 05 and 07 (SITC) does not compensate from the positive trade balance from 06 and 08.¹⁸

The potential of re-orienting the Bulgarian foreign trade could be assessed on the basis of comparing its regional structure to that in countries like Portugal and Spain before they joined the EC. According to J.J.Boillot, such a comparison points to a continuing overestimation of Bulgarian trade with the former CMEA-area, i.e. +13 points, and underestimation of trade with developed West European countries, -15 points, respectively. J.J. Boillot makes these estimations on the base of the use of traditional models. The tendencies of the Bulgarian specialisation can be shown using indicators of external trade specialisation such as – relative export and import structure of a specific kind of goods and for Bulgaria; position in the foreign markets (indicators Lafay); indicators intra-branche/intra-produit, etc. (Table 7)

The analysis of the relative structure of the Bulgarian export and import of industrial goods with the countries from the European Union show possible advantages in the trade with traditional industrial goods – metallurgy and textile; and significant advantages for the Union in the trade with equipment and transport vehicles. This is confirmed by the values of the indicators Lafay for the positions of the Bulgarian export and import on the international market. Concerning the indicators of B. Balassa – intra-branche/intra-produit – a specialisation for Bulgaria is seen in the trade with goods from 06,08 and mostly 07 (by SITC), on which position Bulgaria is almost the only importer.¹⁹

¹⁶ See J.J. Boillot. *La transition commerciale et la stabilisation a l'Est*. 1993, Paris.

¹⁷ *The Economy of Bulgaria till 1996*, Sofia, 1993; V. Yotsov, *Bulgaria's foreign trade in transition*, *Ikonomicheska Missal*, 1993, № 9-10, pp 74-75; NSI, *Exports and Imports*, 1992.

¹⁸ Look for details in Vesselin Mintchev, *Les échangés industriels entre la Bulgarie et l'Union Europeene*, *Enchevetrement industriel et gravitation commerciale*, PHARE-ACE P 95-2030-R, mimeo. The study is based on mirror statistics of OICR – 05-08 positions at SITC – to 3rd mark for the period 1990-1994.

¹⁹ *Ibid.*, p. 13-16.

Table 2.7.

Indicators for stabilisation of the Bulgarian trade with industrial goods with the countries from the European Union, 1994, %, (compared with the trade on the world markets)

	Relative structure		Indicators Lafay	Indicators intrabranche intra-produit
	EU - 12		EU - 12	EU - 12
	export (t)	import (u)		
05	118,42	97,68	-0,01	91,79
06	167,20	111,22	0,03	78,53
07	33,24	97,32	-0,04	49,33
08	174,37	113,88	0,00	74,87

Source: Vesselin Mintchev, *Les echanges industriels entre la Bulgarie et l'Union Europeenne*, 1996, mimeo, p. 13-16.

Even after the reduction of the Bulgarian foreign debt to the London Club banks, the diminution of foreign indebtedness will be still possible only if nearly 10 percent of GDP is placed for debt servicing. Given the present crisis of transition, it would be more realistic to prevent a further debt increase, and thus expend smaller portion of GDP on its servicing. According to some experts, with 5 percent of GDP on servicing, the debt should not grow any more.²⁰

In 1992, Bulgaria's net debt was calculated at USD 12.3 billion. (Table 1) The debt-GDP ratio increased from 0.42 in 1989 to 1.48 in 1991 and 1.39 in 1992.

Bulgaria succeeded in renewing its debt agreement with the Paris Club. Bulgaria signed the very important agreement with the London Club banks.²¹

The foreign debt service, despite its 40% reduction and the renewed access to the international financial markets, is still a serious barrier to the structural reform. The Debt Agreement covers the period up to 2003. The largest portion of payments should be made in 1995 – 1997 at a rate of 0,7 – 1,3 billion USD. In the period 1995 – 1997 the largest payments to the International Monetary Fund, World Bank and G-24 are to be provided; in the period 1998 – 2010 the payments to the Paris Club banks will mature, and in the later period (2002 – 2010) the London Club banks will require the due payments. Until the end of the century one fourth of the Bulgarian export and more than 10% of the budget expenses have to be "allocated" to serve the foreign debt. (Table 8)

²⁰ See, *Eurasia Outlook for Foreign Trade and Finance*. The WEF Group, January 1994.

²¹ "Pari" Newspaper, 6 May 1994.

Table 2.8.

Foreign Debt Service (mln. USD)

	1995	1996	1997	1998	1999	2000
Foreign Debt Service	741	910	1,313	662	774	862
- London Club	278	299	309	318	327	335
- Paris Club	36	36	36	92	165	181
- IMF, IBRD, G-24	339	336	522	168	195	225
- Miscellaneous	88	239	446	84	87	121
Foreign Debt Service/GDP – %	8,0	9,5	13,2	6,5	6,9	7,0
Debt Service Ratio %	17,4	20,4	27,6	13,0	14,1	14,4
Interest payments/ budget expenditure %	40,6	34,8	33,0	25,3	22,2	19,3
-External Debt %	12,8	13,6	14,3	9,3	9,2	9,3

Sources: Angelov, Ivan, Economic Outlook of Bulgaria, 1995-1997, S, 1994, p. 124-126.

Bulgaria could not manage with the challenge of the foreign debt in 1996. The end of 1996 is marked with the suggestions for introducing a monetary board. The currency reserves of BNB in the beginning of 1997 are 408 mln. USD. They are under the "sanitary control" according to which the reserve should be able to assure three-month import of the country. The availability of reserves with BNB and the respective possibilities of debt servicing result from the balances of the current account and capital account of the balance of payments. Bulgaria is with negative trade balance in the period 1992-1994. By preliminary data of NSI the deficit is overcome in 1995 (Table 9) Trade balance is likely to stabilise at an extremely low level, i.e. about 30-40 percent the foreign trade turnover in the period 1985-1989. This stabilisation does not generate a lasting growth and 1996-1997 will be the serial worse years for the Bulgarian transition. The balance of services is passive, too. It was for the first time in 1991, when Bulgaria recorded unfavourable balance in tourism. A turn for the better is expected to appear in 1994-1995. The problems in transportation balance are to a great extent due to the Yugo-embargo losses.

Foreign investors in Bulgaria can be classified as follows:²²

- Transnational companies, aiming at developing, consolidating and preserving their position and advantages within the international oligopoly;
- Followers', aiming at improving their general condition, taking advantage of the specific potential of the Bulgarian market;

²² See détails in L. Maroudas et Y. Rizopoulos, La Bulgarie dans les stratégies d'internationalisation des firmes occidentales, Revue d'études comparatives Est-Quest, 1995, 1 (mars), p. 125-129.

- Big groups or small and average enterprises that settled on the Bulgarian market before 1989, with steady position and contacts.

Typical of the first group are participation in privatisation – some of the first privatisation deals in Bulgaria are a result of the global strategy of transnational companies for coming into position on Eastern markets. Thus, the Belgium subsidiary *Amilum of Tate & Lyle* (the *Sara Lee* group) purchased Tzarevitchni Producti, Razgrad'. Following the same strategy, *Kraft Jacob Suchard* purchased 80% of *Republika*, Svoge, *Danone* purchased *Serdika*, Sofia, etc. It is no coincidence that *Shell* are among the first investors in the country.

Table 2.9.

Balance of Payments of Bulgaria

(*mln. USD*)

	1992	1993	1994*	1995*
Current account	-360,5	-1098,0	-24,8	293,3
Trade Balance**	-212,4	-885,4	-16,8	431,8
Export of goods, f.o.b.	3956,4	3726,5	3935,1	5110,3
Import of goods, f.o.b.	4168,8	4611,9	3951,9	4678,5
Services, net	-191,0	-249,5	-181,7	-270,4
Transport***	-2,5	-72,2	-89,9	-6,3
Tourism	-98,7	50,5	117,9	277,8
Interests****	-95,6	-192,3	-192,5	-454,8
Other •	5,8	-35,5	-17,2	-87,1
Private transfers, net	39,8	36,9	164,1	117,0
Official transfers	3,1	0,0	9,6	14,9
Capital account	785,6	791,2	31,9	-53,9•
Direct Investment, net	41,5	40,0	105,4	90,4
Direct investments abroad	-	-	-	8,0
Portfolio investments (net)	-	-	-9,8	-41,3
Middle-term and long-term credits received, net	129,9	-46,3	220,8	-93,9
Support of the payment balance	-	32,0	143,6	• 0,0
Loans extended, net	307,7	285,5	263,1	292,6
Short-term debt	-147,6	-0,1	17,0	-118,4
Other capital	454,1	480,1	7,8	-191,3
London – Club	-	-	-716,0	-
Errors and omissions	-29,2	17,3	79,7	172,1
OVERALL BALANCE	395,9	-289,5	86,8	411,5

Sources: Statistical Reference Book, NSI, 1996, Sofia, p.92

* – Preliminary data

** – Duty data

*** – Including passenger transport

**** – On the base of paid (reseived) interests

The “followers” are primarily Bulgaria's neighbouring countries, such as Greece. Comparatively non-competitive at European markets, they have comparatively big opportunities for expansion at the Bulgarian market.

In the third group of enterprises the *Dow Chemical* stands out, which have been working for years with many Bulgarian companies.

Foreign investments in Bulgaria are settled by the *Law on economic activities of foreign persons and protection of foreign investment* adopted in 1992. With its adoption the Law on foreign investment of 1991 was dismissed.

The law provides definition of the term 'foreign investment' (Art. 9 of the Law). No restrictions are provided concerning the amount of foreign share in newly established or existing companies (Art. 3).

The 'permission' regime is dismissed. There are exceptions for investments in certain sectors, as for example the defence industry (Art. 5). Investments in the banking sector are liable to registration by the Bulgarian National Bank (Art. 5). Under certain conditions, foreign companies are freed from taxes. Repatriations of gain, as well as of liquidation quotas are permitted.²³

A decline in the inflow of direct foreign investment could be observed in 1995. (Table 10) Investors expect the preparation of the mass privatisation scheme, the specifying the shares offered for mass and cash privatisation, etc. The reported decrease is compensated for by increase in items 'indirect' and 'other' foreign investment, as well as by fulfilling engagements on privatisation deals for additional investments.

Table 2.10.

Direct foreign investment, by years

Year	Total number	Amount, in USD	Percentage of total amount
1991	33	14 128 702	2.66
1992	38	50 727 798	9.56
1993	606	130 357 825	24.58
1994	2279	234 003 217	44.12
1995	1850	101 153 553	19.07
Total	4806	530 371 096	100.00

Source: Agency for Economic Coordination and Development, Sofia

Branch structure of direct foreign investment remains unchanged. The level of investments is such that any more significant engagement could seriously change the situation. (Table 11) There are changes, however, in investment structure by countries. Almost 40% of investments are of Germany. Greek enterprises are growing more and more active, especially as regards to increasing the capitals of existing companies. (Table 12) About 90% of capital invested in the country is concentrated among 70 companies. (Table 13)

²³ See the Law on economic activities of persons and protection of foreign investments.

Table 2.11.

Foreign direct investment, by branches (as of 1511211995)

Branch	Relative share, in %
Industry	37.0
Transportation	21.0
Trade	19.5
Construction	5.5
Others	17.0
Total	100.0

Source: Agency for Foreign Investment, Sofia

The bulk of investments in Bulgaria are result of privatisation deals. About \$159 million were paid about them. To this value should be added also the contracted future investments amounting to \$ 189 million. Liabilities of privatised enterprises, amounting to \$17.2 million, and BGL 146.6 million are covered. (Table 14)

Table 2.12.

Direct foreign investments by countries (as of 1511211995)

Countries	Number	Amount, in USD	Percentage of total amount
Germany	221	204 282 571	38.52
Switzerland	77	41 645 923	7.85
Belgium	64	40 768 143	7.69
Greece	781	36 543 708	6.89
USA	147	32 327 398	6.10
The Netherlands	63	31 977 526	6.03
Austria	159	26 009 771.	4.90
Great Britain	97	23 224 400	4.38
Former USSR countries	317	13 484 078	2.54
France	67	11 665 257	2.20
Others	2814	69 442 321	12.90
Total	4806	530 371 096	100.00

Source: Agency for economic coordination and development, Sofia.

Table 2.13.

Direct foreign investment, by amount (as of 15/12/1995)

Amount, in USD	Number	Value, in USD	Percentage of total amount
1 000<	3543	1 588 186	0.30
1 000 – 10 000	742	2 056 591	0.39
10 000 – 100 000	331	11 688 665	2.20
100 000 – 1 000 000	120	38 818 346	7.32
> 1 000 000 000	70	476 219 307	89.79
	4806	530 371 096	100.00

Source: Agency for economic coordination and development, Sofia.

Table 2.14.

Transaction by the Privatisation Agency with participation of foreign investors (1993-1995)

Enterprise	Date	Sector	Sold shares%	Price (mln)	Future investment	Foreign investor
Tzarevitchni		Food				Amilum,
Producti	12.05.93	industry	81	USD 20	USD 20	Belgium
Republika	15.11.93	Food	80	USD 2	USD 10	Kraft General
Hidroprobivna	10.02.94	industry	97	USD 0,35	USD 0,35	Foods, Ltd
Technika		Machine	100		DM 5,6	Breakers A/S
Gazobeton	11.02.94	tools				Co., Denmark
Sh.Z I.-Solia	13.06.94	Construe				Ytong Ltd,
Somat	02.08.94	tion	70	USD 2,1	USD 7	Germany
Eskos Dograma	16.09.94	Food	55	USD 55	USD 48	Nestle S A.
Zagorka	28.10.94	industry	80	DM 0,7	DM 4	Willi Betz,
Separate unit	03.11.94	Trans	80	USD 21,7	USD 41,4	Germany
from VAMO-		port				
Varna	14.12.94	Wood	100	USD 1,4	GBP 3,5	Gibu Ltd, Italy
Vitosha Hotel	25.01.95	process	80	DM 65	DM 31,87	Brewinvest
Kamenitza	27.04.95	brewery	67	USD 4,88	USD 19,7	S.A.,Greece
Burgasko pivo	02.11.95	automotive	80	USD 5,02	USD 6,5	Rover-
Storko	03.15.95	industry	67	BGL 185	BGL 350	Bulgaria, Ltd
Trading Ltd		Tourism	70	USD 4,88		Ivan Zografski,
Pirinska mura		Brewery	70	USD 4,88		Germany Interbrew,
		Brewery	67	USD 5,02		Belgium
		Food	80	USD 0,1		Interbrew,
		industry	80	USD 0,1		Belgium
						Luxcraft
		Wood	67	BGL 185	BGL 350	Evrotech Ltd
		process.				USA-Bulgaria

Source: V. Blagoev, Privatisation in Bulgaria, Bulgarian Privatisation Agency, 1996, mimeo

Difficulties originate from discrepancies between supply of enterprises, offered by privatisation programmes up to now, and investors' demand. No sooner than 1996 a decision was reached on the privatisation of 16 attractive infrastructure, chemical and mining industry enterprises.

Table 2.15

Registered joint ventures in Bulgaria, by years

Year	Number of joint ventures
Before 1991	17
1991	13
1992	20
1993	15
1994	16
1995	3
Total	84

Source: Agency for foreign investment, Sofia.

Bulgaria is losing its satisfactory start of making joint-ventures in the beginning of the 80s (Decree N 535 of 1980). During the period 1979-1988 among preferable forms of cooperation between the East and the West, along with joint production contracts, sub-execution and joint research, are also the establishment of joint ventures. There are about 20 ones in Bulgaria. Some of them, as BIMAC, are presently among the most successful foreign participation.

For the period 1990-1995 establishment of joint ventures in the country is rather unsatisfactory. They are not among frequent forms of foreign investments. Most numerous are Bulgarian-Russian and Bulgarian -Greek joint ventures. As Table 16 indicates, most numerous are joint ventures within the system of the Ministry of Industry, where the foreign investor is generally of a majority participation.

Filmsy establishment of joint ventures can be attributed to the country's foreign trade orientation until 1989, as well as to procrastination of privatisation and structural reforms, of oppressive and continuous procedures, duty taxation on non-monetary payments (fees) of foreign partners.

According to the Bulgarian AECD investments in the banking and financial sectors are grouped into 11 banks and bank branches, and in several investment funds.

The bulk of the banking sector investments, 67.2%, were made in 1995. Among the most significant ones are: the Bulgarian-Russian Investment Bank, Raiffeisen Zentralbank, BNP – Dresdner Bank, Ionian Bank. The efforts of most foreign banks are to administer contacts between their foreign customers and local enterprises. (Table 17)

Table 2.16.*Registered joint ventures, by branch ministries*

Institution	Number	Average amount of share the foreign investor, in %	Total amount of foreign share, in USD
Energy Committee	7	1.4	504 248
Posts and communications Committee	4	50.9	131 976
Travel Committee	14	62.2	1 334 233
Ministry of Transportation	17	76.5	24 996 016
Ministry of Industry	28	61.0	60 541 102
Ministry of Agriculture and Food Industry	14	49.4	5 802 697
Total	84	-	93 310 272

Source: Agency for foreign investment, Sofia.

Table 2.17.*Foreign Investment in the banking sector by years, in %*

Year	Relative share, in %
1993	3.29
1994	29.68
1995	67.2

Source: Agency for Economic Coordination and Development, Sofia.

2. 5. Development of the Private Sector

In the transition from command-administrative economic system to market economy, the executive power should pay special attention to the recovery and development of private sector.

In June 1992, the Council of Ministers passed a Decree 107 on creating conditions for the development of small business. Under this Decree, "Small Enterprises" Fund was established with the former Ministry of Industry, Trade and Services, subsequently transformed into Ministry of Industry. The Fund is managed by a Management Board appointed by the Council of Ministers. The Fund's resources are supplied by the state budget, foreign financing, endowments, purpose contributions, etc. The Fund is crediting on easy terms the small and medium-sized business. Besides, a Small Business Act is to be entered in the Parliament in the near future.

The Bulgarian Chamber of Commerce and Industry (BCCI), the Bulgarian Economic Chamber (BEC), and the Union of Private Enterprising (UPE) are the institutions which

represent the private sector in the country. They have suggested the setting up of an Investment Bank of private entrepreneurship aid.

According to data of the National Institute of Statistics the total number of registered firms was 508 429 by December, 31 1995; of them 466 455 were of prevailing private ownership and 41984 – with predominantly state property. The greatest part of private firms operate in trade-sector – 285 543. There are 61 121 in industry, 40 441 firms in transport and communications, etc.²⁴

At the first stage of the reforms out of the all registered private firms, 69 percent have present annual accounting reports in compliance with the requirements of the Accounting Law. Firms, which have not provided data are most probably non-operating. Of those, which produced information, 61.7 percent were profitable, 32 percent losers, and 6.3 percent break-even. Firms of annual revenue below 100 thousand BG Lev numbered 43,430, and those above 1 million BG Lev were 7,618. Of the latter, 886 reported a revenue above 10 million BG Levs.

The best financial condition was observed with firms in construction, finance and transport. Regarding employment, 91.3 percent of private firms have less than 5 employees, and only 0.3 percent – more than 50.²⁵

The relative share of employment in the private sector in Bulgaria was 5.9 percent in 1990 and 40,7 percent in 1995.²⁶ The increase is due to the entrance of part of the employees fired from the state and cooperative sectors. The estimations of employment in the private sector at the first stages of the reform vary from 670 thousand (NSI) to 900 thousand (AEFD). Given the considerable difficulties in determining the framework of private sector, these estimations should be considered rather conditional and, probably, very exaggerated. By data from NSI in 1995 the employees in the private sector were 1348 910 people.

The share of private sector in the Gross Value Added increased from 9.1 percent in 1990 to 30,5% in 1994 and 49,6% in 1995. The greatest contribution to this growth came from services and agriculture. The private sector is dominant in agriculture²⁷and trade, and comes up to 64 percent in construction.

3. National Policy and Institutional Framework of State Enterprises Restructuring

The transition to market economy in Bulgaria started in the conditions of full domination of state ownership in industry. At the end of 1989 the state sector covered more than 95% of fixed industrial assets, nearly 75% of industrial labour force and created about 84,1% of the National Income. In the state sector, subject to centralised planning was not only the prevailing part of production but also the establishment, expansion or closing (respectively reorganisation) of enterprises. Most of them were large

²⁴ Statistical Reference Book, NSI, 1996, p. 202-203.

²⁵ Results of private firm activity in 1992, NSI, 1993.

²⁶ Statistical Reference Book, NSI, 1996, p. 62-63.

²⁷ Statistical Reference Book, NSI, 1995, p. 105. Statistical Reference Book, NSI, 1996, p 190-191.

units allocated mainly in machine-building, chemistry, metallurgy, electrotechnical industry and electronics, textile industry, etc.

The specific regime of their functioning and the lack of real competition, fixed prices (often set in compliance with national expenses) secured markets within the CMEA etc., in particular, concealed to a great extent the real efficiency of particular productions, allowed the artificial maintenance of activities, organisation structures and units and made for the emergence of imbalances throughout the economy.

State enterprises restructuring is one of the means for overcoming the imbalances and for the entire restructuring of economy. This process of changes simultaneously going in production and technology structure of industry and in the priorities of individual productions and sectors, on the one hand; on the other, these are changes in the organisation-and-economic conditions of functioning, in the organisational and legal status and in management and technique of decision-making.

State enterprises restructuring in Central and Eastern Europe is connected first of all with the abolishing of the model of centralised state management of production and establishment of economically and financially independent entities. The following steps have been undertaken to carry out the process: **demonopolisation**-abolishing of giant economic structures dominated by giant enterprises and establishment of a greater number of independent economic agents; **corporatisation** -- changes in the organisational and legal status of enterprises and setting their relationships on business grounds; **privatisation**-transformation of state enterprises into private. Privatisation is considered the radical and obligatory way for economic restructuring. However, being a long process which cannot be implemented everywhere, it necessitated the search of alternative forms of restructuring, some of them representing intermediate steps to privatisation itself.

State enterprises restructuring implies coordinated national policy based, on the one hand, on clearly determined priorities of national economic development, and on the political consensus about the model, pace and stages of transition to market economy, on the other.

It is evident from practice that attaining such a coordination is one of the most difficult elements of economies in transition, highly polarised political space in Bulgaria hampered the development of a clear national strategy on the model of transition. The absence of parliamentary consensus on the priorities of laws indispensable for economic reforms made not only for the low synchronisation of the elements of reform but also for the critical lagging of legislative behind economic reform.

3.1. Legislative Framework of Restructuring

The restructuring of the state enterprises in Bulgaria began in the conditions of a sharp deficit of legislative norms. The first juridical regulators of this process were:

- ✓ Commercial Law (State Gazette, 48, 18 June 1991);
- ✓ Decree 56 on Economic Activity (State Gazette, 4 January 1989);
- ✓ Law on Economic Activity of Foreign Persons and on the Protection of Foreign Investment (State Gazette, 8, 28 January 1992); it-evoked the former Law on

Foreign Investment (State Gazette, 47,14 June 1991);

- ✓ Law on Ownership (State Gazette, 92, 16 November 1951);
- ✓ Law on Transformation and Privatisation of State and Municipal Enterprises (State Gazette, 38, 8 May 1992);
- ✓ Law on Restitution of Ownership on nationalised Real Estate (State Gazette, 15, February 1992);
- ✓ Law on Protection of Competition (State Gazette, 39, May 1991);
- ✓ Law on Establishment of Sole Merchant Companies with State Property (State Gazette, 55, July 1991).

At quite later stage were adopted laws regulating the creation of market infrastructure, tax procedure and also additions to the Trade Law which treats the insolvency of the traders and trade deals. Here we will give just some of them:

- ✓ Law on Goods Exchanges and Market-Places (State Gazette, 93,1996);
- ✓ Law on Securities and Stock Exchanges (State Gazette, 63,1996);
- ✓ Law on Privatisation Funds (State Gazette, 1,1996);
- ✓ Law for Changing and Adding of the Trade Law (Chapter 4, Insolvency of the Traders) (State Gazette, 63,1994);
- ✓ Law for Changing and Adding of the Trade Law (Article III, Trade Deals), (State Gazette, 62, 1995);
- ✓ Law on Protection at Unemployment and Encouraging of the Employment;
- ✓ Law on Financial Recovering of the State Enterprises (1996).

The contradictory political interests related to the changes in the model of ownership postponed for more than one year the passing of the main restructuring law, i.e. the Law on Privatisation.

The Bulgarian Socialist Party (former Communist Party) which gained the majority in the first democratically elected Parliament stood up for the idea of mass or so-called 'social' privatisation as the means for state enterprises restructuring. However, BSP did not venture to put up this idea into practice.

The Union of Democratic Forces, the second big political group, backed up the idea for market methods of privatisation, the latter being preceded by a process of general restitution. Later coming into power in November 1991 the UDF together with the Movement for Rights and Freedom (Party of Ethnic Turks) succeeded in promoting the idea. Other parties and their representatives took the legislative initiative too. As a result, a total of 8 draft laws on privatisation were submitted; however, none of them was put forward to plenary discussions. In this way, the restructuring of state enterprises in Bulgaria till mid-1991 was regulated by a socialist normative act, i.e. **Decree 56 on Economic Activity (January 1989)**. Partly, it was in operation until the end of 1996.

With regard to restructuring the significance of Decree 56 found expression in two main directions:

- first, it laid the beginning of spontaneous or so-called "hidden" privatisation and created conditions for initial accumulation of capital. By starting the organisational restructuring of state enterprises on a company basis, Decree 56, on the one hand, opened bigger opportunities and freedom of organisation of economic activity, including in the

field of contradiction, amalgamation, partnerships, etc.; on the other, it allowed the establishment of firms of individuals and public organisations, with certain limitation on the number of persons employed. Parallel firms of state firms' managers working as subcontractors of state-owned enterprises turned to be the first form of hidden privatisation of state-sector created income, this model is still existent.

Expansion of firm independence and in the field of foreign economic activities, in particular, including the possibility for setting up and participation in off-shore companies and other institutions without special permission of higher authorities (except for the cases envisaged by the Decree) gave impetus to another kind of "spontaneous privatisation", i.e. through privatising the business contacts of state-owned firms by their former manager.

- second, Decree 56 provided equal rights for economic activity of foreign persons and strengthened the interest in joint ventures with foreign capital participation. By the end of 1989 the joint ventures in Bulgaria numbered 51.

With a lot of amendments, Decree 56 is still regulating the activity of non-transformed state enterprises as well as the issues related to their liquidation.

The structural adjustment of economy during the first years of transition was characterised by measures for decentralisation of economy. These processes were regulated on governmental level mainly (Decree 54 of the Council of Ministers, 3 April 1991) and resulted in the development within a month of a number of programmes for decentralisation and demonopolisation of state economic groups, combines and enterprises. In legal terms, the processes of decentralisation and demonopolisation were regulated by the Law on Protection of Competition. The law gave a post-factum determination of the concept of "monopolistic position", abolished restrictions on competition and determined the cases of unfair competition.

The administrative nature of the process and the extremely short terms of implementing decentralisation measures resulted into a series of failure connected with broken technology chains, artificial indebtedness of enterprises, preservation of particular monopolies and the subsequent difficulties in their restructuring.

Very soon the Law showed its insufficiency. It does not guarantee distraction of the monopoly situation of the economic subjects in regional scale. Quite limited and insufficient turned to be the authorities of created by it organ – Commission for Protection of Competition in order to exercise effectively its control functions.

The adoption of the **Commercial Law (June 1991)** brought about a more adequate regulation of these processes, through revocation of the texts in Decree 56 treating the establishment of different types of firms and regulation of new procedures for their establishment.

In the first version the adopted in 1991 Trade Law remained incomplete. It did not regulate in particular the relationships between the different economic subjects or the procedures on closing of their activities in case of financial insolvency. Almost till the end of 1994 this whole was filled by the Decree 56.

With the Law for Changing and Adding of the Trade Law from August 1994 the insolvency of the traders was arranged. The law gives the conditions in which a solvency

procedure is opened, determines the subject insolvency as well as the sides which can want such procedure. It explains also the procedure of opening an insolvency procedure and the management of the insolvency.

Later, in April 1995, with a new Law for Changing and Adding of the Trade Law were determined the trade deals, the order and the conditions for their making, the types of trade securities, the different types of contracts, etc.

The **Law on Establishment of Sole Merchant Companies with State Property (July 1991)** provided the legal framework for the rights of the state as sole owner. Under this law, the establishment and transformation of state enterprises is done by an act of the Council of Ministers.

The concentration of this activity in the Council of Ministers made the restructuring procedure quite difficult and exerted unfavourable influence on the development of this process, since centralism contradicted sharply with the wide range and great variety of cases in practice. Only 460 industrial enterprises were transformed in the period from September 1991 to May 1992.

This made the lately adopted **Law on Privatisation** to cover also issues related to the transformation of state enterprises into commercial companies.

The **Law on Transformation and Privatisation of State Owned and Municipal Enterprises was passed with delay (April 1992)** and not without the IMF intervention. It was a framework character. From the initially envisaged 70 articles, only 34 were adopted. For this reason, the law comprises a lot of references to normative acts regulating main procedures related to privatisation. This made for the additional delay of its application.

Under the law, priority is given to market privatisation with regulation mainly of sales of stock and capital shares owned by the state in enterprises transformed into limited and stock companies; beside, the sale of whole non-transformed state enterprises or their units is regulated too. According to the clauses of the law, the state-owned shares in transformed enterprises can be sold in the open market, by public auctions, public tenders and after negotiations with potential buyers. Non-transformed enterprises or their parts are sold by public auctions or tenders.

Owners of real estate nationalised by laws, decrees or normative acts in the period from 1946 to 1962 which currently exist but are elements of the long-term assets of state enterprises, have the right to receive due shares in capital or stock of transformed into joint companies enterprises.

There are three groups of persons who are allowed to buy at a discount up to 20% of the state-owned shares in an enterprise undergoing privatisation, namely: current personnel with at least two years length of service pending the privatisation decision; persons whose labour contracts with the enterprise were cancelled five years ago; and persons who retired from the enterprise ten years ago.

The market approach to privatisation was not backed up with texts providing for the financial support of participation in the process, on the one hand, and limited the range of implementation techniques, on the other. This resulted in the highly narrowed circle of participants.

In June 1994 the **Amendments and Additions to the Law on Privatisation** were adopted with the aim to remove the above shortcomings. These were formulated as Chapter 8 (the last) of the Law under the name of „**Privatisation through Investment Bonds (Vouchers)**„, also known as mass privatisation.

According to these Amendments, every Bulgarian citizen aged 18 and living in the country is allowed receiving privatisation investment bonds of 25 thousand BG Levs, for 500 BG Levs administrative expenses. Vouchers can be inherited or transferred on a direct line of descent and they cannot serve as a credit collateral. They can be used only for buying stock or capital shares in enterprises announced for privatisation under this scheme.

The participation in privatisation through investment bonds can be either direct or by means of vouchers. Persons given preferences for participation in the privatisation process can use vouchers as additional preference.

Under the Amendments, certain preferences are given to persons connected with the economic activities of enterprises to be privatised. For enterprises with balance value up to 10 million BG Levs and businesses in trade and services up to 5 million BG Levs, preferences are given to their personnel, including leaseholders or renters. Moreover, they are offered easier terms of payment. For example, 90% of the value of enterprises in production and 70% of the value of businesses in trade is paid by instalments within five years. A further one-year grace period of the initial instalment is envisaged for production enterprises.

The attitude to the Amendments varies considerably in the range from expectations for fast privatisation of nearly one-third of state enterprises to statements qualifying them as a means for deriving political dividends.

The arguments of the critics go along the following lines:

- first, untimeliness of the scheme of mass privatisation. It is considered that the suitable time slipped by about four years ago when this scheme could play a prerequisite for speeding up market privatisation. The experience of the Czech Republic is being referred to;
- second, the Agency of Privatisation has expressed fears about the eventual locking effect of mass on market privatisation, resulting from recently strained relations between the Agency and the Council of Ministers in the course of developing the privatisation programme;
- third, in their turn trade unions criticise the Amendments because of: (a) the priority of mass privatisation and underestimating of other methods of participation of employees in enterprise privatisation; (b) the vague criteria of enterprise selection under this scheme and the resulting possibility for including a great number of losing enterprises in it; (c) the simultaneous inclusion of too many enterprises in a rather disputed scheme;
- fourth, the employers' organisations are also critical of the Amendments. They stand for higher priority of workers and managers participation in privatisation.

Apart from the general critical notes to the Amendments to the Law on Privatisation, the implementation procedures are also criticised. These refer to the lack of adequate

legal regulation of relationships connected with mass privatisation. A number of laws are still to be elaborated, namely: on investment funds, on protection of small investors, on securities and stock exchanges, etc. The possibility that most of these relations be regulated by normative acts will rather hamper than facilitate the process as the present contents of Chapter 8 and the Law as a whole incl. a great number of references to normative acts of the Council of Ministers.

The practice show that the truthfulness of the critics, connected only with the unpreparedness for quick start of mass privatisation. It took more than one year additional work on creation of the necessary normative and other conditions (including adopting Law on Privatisation Funds, Law on Securities and Stock Exchanges and a lot of sublegal normative acts) for applying the model of mass privatisation.

In the first wave of mass privatisation (1996) the participants were about 3 million people (over 50% of rightful claimant people) with 75,2 billions investment bonds.

In December 1995 the Law on Privatisation had some changes insuring preferences to workers-managers teams in acquiring shares and percentages of the enterprises. The changes envisaged possibility for prolonging the term of the extended payment to 10 years, possibility for using the investment bonds for acquiring shares at preferential conditions, etc. At the same time a limitation to the trade with shares acquired at preferential conditions.

The last changes in the **Law on Privatisation (August 1996)** concern mainly the management of this process. It is more centralised focusing in the Government and in particular in Ministry of Economic Development which part took the functions of controlling body over the Privatisation Agency.

Three laws on restitution in Bulgaria were adopted in 1991, one of them being of certain importance for state enterprises restructuring. This is the **Law on Restitution of Ownership on Nationalised Real Estate**. It repeals eight laws on nationalisation in the period from 1947 to 1952, including the Law on Nationalisation of Industrial and Private Mining Enterprises under which more than 4000 enterprises were nationalised in 1947.

Under the Law on Restitution, subject to restitution are units preserved in their real boundaries (except for those legally acquired by private persons which are hard to find in industry) and cooperatives.

Similar to the German privatisation legislation and unlike some Central European countries, non-residents of Bulgaria are also allowed restitution of their property rights within a fixed term. This concerns both physical persons and legal entities.

Foreign participation in state enterprises restructuring is regulated by the **Law on Economic Activity of Foreign Persons and on the Protection of Foreign Investment (January 1992)** which repeals the former Law on Foreign Investment (June 1991) as the latter contained bigger restrictions on foreign presence in Bulgarian economic life.

Under the Law equal rights are provided to both Bulgarian and foreign physical persons and legal entities. The cases requiring special permission are specified by the Law. The size of foreign participation in newly established or already existing companies is unlimited.

Joint ventures enjoy a series of tax concessions, including a five-year profit tax exemption for companies with economic activities in the field of high-tech branches (determined by the Council of Ministers) and in agriculture and foodstuff industry.

Restrictions envisaged by the Law concern mainly the right of foreign citizens to buy land, and for joint ventures with more than 50% foreign capital – the purchase of arable land. Foreign investments in specific geographic areas determined by law and in specific activities (production and trade in arms and ammunitions, extraction of natural resources from the territorial sea-waters, etc.) require special license from the Council of Ministers. A license from the Bulgarian National Bank is required for carrying out banking and insurance activity and for participation in banks and insurance companies. Neither the Law on Foreign Investments, nor the Law on Privatisation contain any restrictions on the participation of foreign persons in state enterprises privatisation.

The changes in the **Law on Foreign Investments (1996)** specified the form of external investments as well as their minimal amount (\$50 000) to be registered as such. The new texts in the law foresee non-monetary payments (in the form of machines, equipment, technologies, licences and industrial models on the amount over \$100 000) to be freed from duties and taxes. Unchanged remains the prohibition for foreign persons to own agrarian land.

The successful restructuring of state enterprises depends to a great extent on laws providing the building up of market economy infrastructure. The lack of law on stock exchange and on trade in securities creates the possibility of arbitrary acts and uncontrolled entries in the market, moreover, it facilitates hidden privatisation.

In 1995 was adopted a **Law on Goods Exchanges and Market Places**. It determines the order and conditions for creation, structure and activity of goods exchanges and market places. The law enacts the creation of a state body (state commission) to regulate and control the establishment and the activity of goods exchanges and market places.

Till the end of 1995 in Bulgaria in chaos, on purely market principle appeared more than 20 stock exchanges and stock departments to the stock exchanges. The Bulgarian National Bank introduced a regime of licensing of the securities traders but nevertheless the capital market, as far as it existed, was characterised by absolute absence of public information for the deals and the financial condition of the issuers. The adopted in 1995 Law on Securities and Stock Exchanges legally regulates the capital market, defines the securities, determines the functions and conditions for work of the stock exchanges, of the investment moderators and investment companies. The law enacted the creation of a state body (Commission for Securities and Stock Exchanges) with extremely wide authorities on regulation and control over the activity of the issuers, investment mediators and investment companies.

In addition to the regulative norms of the development of the capital market in Bulgaria was adopted a Law on Privatisation Funds, closely connected with the starting of the mass privatisation. Determined were the order and conditions for establishing and activity of the privatisation funds, their behaviour and functions at the capital market, their connection with the other participants in it. Specially treated is the question for the

state control upon them and the protection of the investors.

The bad financial condition of the firms and particular their great debts to the creditors, suppliers, budget, etc., was and continues to be one of the main obstacles in the restructuring. The repeated attempts for solving the problem with so-called "bad loans" did not give a special result. Together with the many partly measures in the end of 1993 was adopted a special Law on Arrangement of the Non-Served Credits, contracted till 31 December 1990. According to this law, by issuing of long-term state bonds in levas and foreign currency the state took part of these loans. Very soon the firms had new "bad loans".

The continuous absence of legal norms determining the insolvency of the firms (of the Law on Failures) helped this situation. The further increase of the debts of the firms applied the adoption in July 1996 of the Law on Financial Recovering. The law concerns a specific number of enterprises with biggest losses which continue to work at a specific regime under the control of the Ministry of Finances.

The law foresees simultaneously stopping of the payment of old debts and prohibition for having new credits. The law does not limit the rights of the creditors to gather their debts, including by requests for announcement of the firm-debtors in Failure. The law obligates the firm-debtors to work out recovering programmes on the quality and executing of which will depend their faith.

The process of state enterprises restructuring in Bulgaria is further constrained by the absence of laws regulating the stability of market environment. What matters in this case is a comprehensive legal framework of development of private business (there is not still a Law on Small and Medium Business), an adequate law on obligations and contracts, etc. In their absence, business environment is unstable and uncertain and therefore domestic and foreign investors are demotivated to develop economic activities in Bulgaria.

The series of laws providing the legal framework of economic reforms and state enterprises restructuring is not finished by those closely related to business and production. Laws on social issues are also institutions of free market economy and bear direct relevance to securing the economic reforms. The lacking balance and complementarity between strictly economic and social laws and the understanding of the latter (in Bulgaria, in particular, it found expression in the continuous neglecting of the Labour Code and in the absence of Law on Employment, Law on Social Insurance, Law on Social Assistance, etc.) bring about social tension and discredit on the reform.

3.2. State Industrial Policy and The Problem of Restructuring and Privatisation

A wide-spread reaction against state intervention in the economy was observed in Western Europe and the United States in the 1980s. Most of the Western governments had adopted the principles of monetarism which implied strong restriction of the role of state policy, particularly on micro-level. The reaction against state intervention reflected the exhausted potential of macroeconomic regulation in the 1970s and the growing confidence in the efficiency of "market forces". In addition, there were the emerging

processes of rejection of total state control over economy in the former socialist countries. The conception was thus developed of state industrial policy being incompatible with market economy and therefore impeding the action of market forces.

The experience of Western economies points to their differing attitude towards industrial policy during different stages of their development as well as to the various sets of tools they have applied depending on the problems they have faced.

However, **the 1990s did not bring much room for policy choice in the former socialist economies.** Pressed by their domestic economic problems, the claims of foreign creditors and the activity of experts of international financial institutions, the former socialist countries took **the road towards market economy by substituting levers of monetarism for centralised regulation.**

As a result, the main efforts of the state were aimed at attaining macroeconomic stability, overcoming financial imbalance and restraining inflation. Next (in sequence, not as a simultaneous process) came the structural adjustment of economy. The stress was put on monetary policy as the main instrument of regulation of economic processes; state industrial policy was actually rejected. In the spirit of Friedrich von Hayek's philosophy, the state was expected to just "set the general rules", i.e. create market environment and conditions for competition.

There were several reasons behind this behaviour, namely:

1. The identification of state industrial policy with dirigisme and the inherited from socialism fears of new bureaucracy in economy.
2. The initially wide-spread naiveté and groundless optimism about the success of reforms based on the view-point that market economy and competition will automatically solve the problems of restructuring and economic efficiency.
3. The absence of strategy of economic development in transition and the domination of short-term goals like financial stabilisation, implying the use of tools of monetarism and underestimating, including time delay of structural reforms.
4. The prevailing monetarism views among politicians and executives (in the Government of UDF, in particular) which doubted the co-existence and compatibility of industrial policy and the transition to market economy.
5. The hostile attitude of experts of international financial institutions towards industrial policy which was treated as working rather against than pro market forces.²⁸

The denial of industrial policy as a specific aspect of governmental economic policy resulted in the sudden withdrawal of state from economy and liberalisation of domestic and external conditions of functioning of enterprises with no bearing on the structural accents of reforms.

Budget dotations to enterprises were sharply reduced, regardless of financial state and reasons. Unsuitable forms of demonopolisation and the break of economic and technology relations made for the artificial increase of enterprises' debts; in addition, the rise of interest rate on credits reduced most of them to the verge of bankruptcy.

Foreign trade liberalisation prior to any more or less successful adjustment of

²⁸ United Nations Economic Survey of Europe, p. 16, 1992-93.

Bulgarian enterprises to new conditions deprived domestic producers of any sort of protection. In addition, exchange rate liberalisation in the absence of customs policy aimed at promoting exports of particular commodity groups, on one hand, and imports of goods assisting technological development of production, on the other, resulted in the spontaneous formation of structures often contradicting with national interests.

The Government failed to suggest programmes of enterprise recovery. Measures on the redemption of "bad loans" accumulated till 1990, were late, inconsistent and halfway; beside, they concerned mainly the high-tech industries. It was only by the end of 1993 when a law was adopted giving a radical solution to the problem.

The sudden withdrawal of state from economy found expression in the lack of working procedures for efficient management of state enterprises. The rejection of managers selection through competition turned management assigning contracts into mere formality and determined the hierarchical subordination and total administrative dependence of managers on higher executive bodies. The absence of strict parameters of manager behaviour, fixed by contract, on one hand, and the impossible centralised state control over their activity, on the other, along with the non-existent market of manager services and institutions to provide objective estimations of managers activity, made the status of this group very uncertain and unstable. Manager teams were thus forced to direct their initiative towards short-term measures, most often connected with the survival of the firm. For the sake of stabilisation, the state did not provide protection and special measures to promote and improve the state of private sector – one of the potential factors of restructuring. Only few of the private firms could use credit facilitations; beside, risk investments were denied any support thus reducing to the minimum the opportunities of nascent small and middle-sized business to participate in the industrial and economic restructuring.

All this contributed to the **artificial prolongation of the stabilisation period**, also postponing the structural stage of reforms, **deepened economic hardships and created further problems for the process of restructuring**. Worsened economic state of enterprises reduced their attractiveness for potential buyers while the fast impoverishment of population due to production decline and price liberalisation restricted its capabilities to take part in privatisation.

The rejection of state industrial policy and the adoption of principles of monetarism resulted in the formulation of a **particular philosophy of restructuring and relevant approaches towards it**.

In the light of these principles, the restructuring of economy (industrial and market) was considered a natural result of the action of market forces and privatisation. By putting enterprises in market conditions, the problem of their selection (survival of viable and liquidation of the rest) had to be solved while the market behaviour of the new owner after privatisation had to determine the place of the unit in the branch and the economy as a whole. The efficiency of this selection was not considered from the viewpoint of national interests; similar attitude was demonstrated towards the role of privatisation in the economic policy of the state.

Practice in East European countries and Bulgaria, in particular, suggested that the creation of market environment and market mechanisms is far from quick and easy process as anticipated. According to estimations of Western experts, it will take from 20 to 30 years.²⁹ In the course of its emerging, the market system is imperfect. The basic institutions and mechanisms of market influence on enterprises behaviour are still non-existent. The parameters of economic environment are unstable, quickly changing and frequently unclear to economic agents. Along with deepening economic difficulties of enterprises, all this created **pressure for „rehabilitation„ of state intervention** in economy on the part of both companies and foreign observers and politicians. "In the conditions of CEE, states R. Portes, we cannot trust the market to select and eliminate negative value-added activities and to develop those that do have long-run prospects"³⁰. For this reason his advice is that "the authorities should immediately take steps to reverse the state desertion (underlined by the author) that has left state-owned enterprises floundering ... improve corporate governance insofar as is possible without privatisation and rehabilitate industrial policy"³¹. The unfavourable effects of state withdrawal from economy in transition are gradually realised as well. 'The danger of resorting to the old central planning mistakes obviously always exist but it cannot justify avoiding the issue of how best to intervene in the transition. In the absence of this realisation there will be intervention in practice but in ways that are not clearly stated and involving costs that may violate the macroeconomic budget constraints without awareness of its scope and implications".³² The restored interest in industrial policy in the transition to market economy is partly due to the revision of its role in the practice of Western economies. However, this is to a greater extent a reflection of the necessity that transition economy governments actually take part in a series of activities related to the management of economy, such as: decentralisation and demonopolisation, transformation of enterprises into different kinds of companies, centrally organised privatisation, etc.

The Government of Hungary was the first (January 1993) to manifest changes in its attitude towards industrial policy. It adopted a moderate industrial policy providing support for the creation of market-oriented microenvironment, incentives to innovations and elaboration of government programmes for technology development, modernisation of infrastructure, promotion of main market services like marketing, finance, etc.³³

In April 1993, **Bulgarian Government (led by Professor Ljuben Berov) also declared its interest in industrial policy** by stating its intentions to stress on the structural part of reforms, parallel with measures on stabilisation. At the end of 1993, the clearout conclusion was made of the **necessity in policy based on reasonable balance of stabilisation and structural measures**. The financial stabilisation and restructuring

²⁹ Landesmann, "Industrial Policy and the Transition in East-Central Europe", Discussion Papers on Economic Transition № 9204, Cambridge, Dept. of Applied Economics, 1993.

³⁰ R. Roberts, "Comment on the Contradiction of Eastern Europe's Economies' Introduction to the Conference", p 10

³¹ Ibidem.

³² M. Bruno, "Stabilisation and Reform in Eastern Europe: Preliminary Evaluation", p 32

³³ A. Tork, "Hungarian Industry and the Economic Transition", Institute of Industrial Economics, Budapest, mimeo, 1993

of certain economic activities had to be supported by moderate state budget subsidies. Structural reforms were determined as the basis of governmental policy. Its main aspects were announced as follows:

- speeding up of privatisation;
- imposing measures for losses reduction and financial discipline of enterprises;
- implementing corporate management of state owned enterprises.

The experience for working out of national strategy for restructuring and financial recovering of the state enterprises was the first visible attempt for constructing of the elements of the industrial policy. The enterprises were divided into four groups according to their financial condition, market strategy and opportunities for adjustment to the new conditions. Specific were the following groups:

- first, enterprises to be restructured by the new owners after privatisation, due to considerable financial resources needed;
- second, enterprises in which reduction of expenses and strict discipline should be applied as elements of their restructuring plan, including an explicit proposal for privatisation;
- third, enterprises and/or their parts to be liquidated, because of the lack of market prospects for covering their losses; and
- fourth, a limited number of enterprises to be restructured without direct binding to privatisation plans, as these can neither be privatised nor liquidated due to clearcut unfavourable social or economic consequences.

Compared to former views on restructuring, two new aspects are worth mentioning. The first is related to liquidation as an operational means for enterprises restructuring; the second concerns the officially stated possibility of restructuring beyond privatisation schemes.

Financial recovery of enterprises turned into indispensable element of the policy of restructuring. The first steps in this direction were connected with the issue of "bad loans" and the normative regulation of their redemption. By Decree 45 of 9 March 1994 the Council of Ministers adopted Ordinance on the criteria for working out programmes for financial recovery and restructuring of state enterprises, firms and commercial companies. The Ordinance was supplementary to the set of normative acts regulating the "bad loans-into-government debt" swap (for credit negotiated till 31 December 1990) against long-term government bonds. State enterprises with bad loan swaps effected under the Law on bad Loan Settlement (State Gazette, 110, 1993) make a contract with the Ministry of Finance or other authorised body, stipulating the term and conditions of redemption of swapped loans. This was done on the basis of programmes for financial recovery and restructuring developed by enterprises which included analysis of current state, strategy for future development and anticipated financial results. The estimation of these programmes showed that a great part of the companies in the main economic sectors are insufficient in revenues to maintain normally their economic activity, i.e. to meet expenses on raw material, wages, depreciation charges, credit repayment and social insurance contributions.

This made liquidation turn into an explicit element of restructuring policy. Prior to the adoption of the Law on Bankruptcy, the Ministry of Industry worked out an Ordinance and relevant rules and procedures for closing enterprises by liquidation. It concerns units which cannot organise their production activity independently and have no market prospects and possibilities for production and technological restructuring in the near future. Based on the analysis of operation of 1420 state firms in 1992 and 1993, a list was prepared of the first 34 enterprises (mainly in machine-building, light and foodstuffs industry) subject to liquidation. Liquidation procedures have been opened for 10 firms. The financial state of enterprises was estimated in terms of several indicators, namely: liquidity coefficient, fixed assets and stock turnover, profitability of sales and debt capital, interest payment on credits, total indebtedness.

State firms in heavy financial condition were classified in three groups, with respectively stages of liquidation:

This government could not realise the positive thought of its policy mainly due to two reasons: first, it did not come out of the frames of the traditional state administrative policy with its inherent vices: bureaucracy, clumsiness, inaction, etc., second, the role of the mechanisms and institutions of the market environment was underestimated as a factor, forming the behaviour of the firms (including their financial discipline). By the same reasons the attempt for stimulating the internal restructuring by changes in the cooperative management turned to be unsuccessful.

The first declarations of the next (1995) government (of the socialists) provoke new expectations for development and application of the conception for the industrial policy. It declared as a main priority the structural reform and the use of regulative-market approach in its executing and the management of the economy.

Declared was the intention for speeding the privatisation, for continuing the line of financial recovering of the enterprises, as well as of liquidation of enviable and non-perspective firms. For the first time was clearly determined the strategy of the state participation in the privatisation. Determined were the enterprises forbidden for privatisation without the explicit allowance of the state as well as those in which the state keeps the decisive share.

On the background of the overcome shocks of the reform (decreasing of the markets, of subsidies and competition from outside) extremely actual sounded the intention for active industrial policy connected with the looking for new sources of investments.

The expectations were strengthened on the result of the great public confidence in the government (at its coming to govern at the beginning of 1995) and of the absolute majority of the governing party in the Parliament which created the unique for the last 7 years chance to be worked out and adopted by the Parliament agreed national strategy for the restructuring and the future development of the economy in transition.

These expectations did not realise for some reasons:

First, the conception for the industrial policy in practice identified with the state regulation of the economy turned to be wrong. The mechanism of its working out was reduced to the expert foreseeing of the main macroeconomic indicators and structural ratios in middle-term perspective. There was lack of clear looming of the national priorities and the corresponding strategies at product, technologic, resource, market,

organisational, etc. restructuring. The public dialogue and empathy of the industrial elite and the syndicates for the working out of the national strategies was not searched. In the same way were worked out the branch and other programmes (as far as there were such) by the different ministries.

They remained at the level of "intentions" of the governments of the ministries: not connected between each other, uncoordinated and non-supporting. The approach to the conception for industrial policy determined the character of the used means for its realisation: centralised management of the processes of the privatisation and restructuring including the administration of the liquidation, centralising the management of the firms by artificially created (without the necessary conditions for this) holdings and consortiums, expanding of the controlled prices including the use of the state offers as an instrument for administrative influence upon the prices, etc.

Second, the role of the market environment and market institutions for the restructuring of the economy is underestimated. The practice of the first years of transition shows that the market instruments do not solve effectively the structural problems. But having clearly formulated aims and national priorities and programmes, they can play significant role for the speeding the structural changes. From the experience of the developed industrial countries is known that the small and medium business (the general institution of the market economy) at determined conditions can be a significant factor for the product and technologic restructuring of the big (including the state) firm.

The lack of the consistent, supporting this sector state policy (including the lack of law on small and medium business in spite of the existence of some projects for such) makes impossible the use of this reserve for speeding of the structural changes. On the contrary, the anaemic and unprotected small business turns into an additional load for the state enterprises increasing the pressure for the employment places and threat in them. Almost unused are the reserve of the capital and labour market for speeding of the restructuring of the economy.

On purely administrative reasons the use of the market of the managerial services as a source of effects in the field of interfirm restructuring is hold. The adherence to the state institutions for regulating generated the idea for administrative creation of the semi-market forms for investment crediting (Fund "Industry", "Development") and prevents the appearance and the use as a source of investments of the different private institutional investors (social, assuring, pension and other funds).

Third, the strong interference of the state in the management of the economic life in the country was surprisingly combined with sincerely liberal attitude to the international economic relations and encouraging of the competition from outside. The fear from national economic protection and the lack of protection measures for the domestic producers did not increase their competitiveness but surely cooperates for the destruction of the traditional productions and change for the worse of the structural relations in the economy. The same is for the underestimation of the export oriented productions and the lack of incentives for the expand of the export.

The unsuccessful till now restructuring and the deep financial crisis in which fell the country applies radical change in the policy and the ways of carrying out of the structural changes. They will be carried out in the conditions of total lack of financial instruments

according to the aims of the financial stabilisation of the country. This means total reconsidering of the idea for industrial policy and the possible ways for its carrying out.

3.3. State institutions of Restructuring

The success of reforms depends on the role and efficiency of institutions influencing the course of state enterprises restructuring.

Underdevelopment of market environment and market institutions in the transition to market economy made for the increased importance of state institutions and their functions in the process of management, organisation and control of economic restructuring. Public institutions are responsible for the development of adequate legislative framework for restructuring and privatisation of state enterprises and for the creation of the institutional infrastructure of market economy which is of great importance for state sector reorganisation.

The following state institutions share the responsibility for state enterprises restructuring in Bulgaria:

- ✓ the Council of Ministers;
- ✓ Branch Ministries (and the Ministry of Industry in particular);
- ✓ Agency of Privatisation;
- ✓ Center of Mass Privatisation;
- ✓ State Fund for Reconstruction and Development.

The Council of Ministers is responsible for and controls the whole activity on economic restructuring. Its functions are related to:

- ✓ development of a global strategy of the contents and directions of economic restructuring in compliance with the national goals, real possibilities and experience of other Central and East European countries;
- ✓ elaboration and pursuit of economic policy in support of the restructuring strategy chosen;
- ✓ coordinating and control over the activity of other state institutions effecting restructuring.

The peculiarities of the political situation in Bulgaria (the late Government is missing actual parliamentary support and pre-term elections are therefore expected) are impeding the Government from efficiently fulfilling its functions. Only some of the elements of the restructuring strategy are existing. The coordinating of activities of state institutions is imperfect and low-efficient.

One of the reasons for that is the absence of strict and clear regulation of institutions' relationships and especially between the Agency of Privatisation and the rest of them. According to the Law on Privatisation, the Agency has been established as an independent unit to organise, control and carry out the privatisation process (Article 10.1.). However, it is actually dependent on the Ministries, for unlike the Agency, they exercise the ownership rights of the state in the subordinate enterprises and therefore have great administrative and economic power over them.

On the other hand, the efficient restructuring of enterprises is impossible without the

coordinated actions of branch ministries and the Ministry of Finance. Beside, the structural reform will hardly progress if the Ministry of Trade fails to provide a selective and balanced protection of particular productions through export-and-import regime, customs duty, etc. The uncoordinated actions of these institutions result in their low efficiency.

The Agency of Privatisation is a body of the Council of Ministers with the main task to organise and control the process of transformation and privatisation of enterprises.

The first Agency of Privatisation was set-up on the basis of Decree 16 of the Council of Ministers before the adoption of the Law on Privatisation. It had rather limited functions, mainly in the field of studying the experience of other countries and preparing drafts of relevant documents.

In August 1992 the former Agency was closed down in compliance with the already adopted Law on Privatisation and the new Agency of Privatisation was established with the technical and financial assistance of "Treuhand Osteuropa Beratungsgesellschaft".

The Agency has two Departments, namely: "Programmes and Methods of Privatisation" and "Organisation of Privatisation". The Agency has a network of regional offices acting in parallel with municipal authorities. It is run by an Executive Director while the controlling functions are exercised by eleven-member Supervisory Council, in which the Government and the Parliament have respective quotas.

The activities of the Agency of Privatisation include:

- ✓ elaboration of annual privatisation programmes;
- ✓ methodological direction and preparation of privatisation procedures;
- ✓ negotiations with potential buyers and execution of that part of transactions which is within its capacity.

The first privatisation programme was adopted in fall 1992. It envisaged the opening by end-1992 of privatisation procedures for 92 enterprises with total assets value of about 2359 billion BG Levs; two of them were to be privatised by the Agency, 32 by the Ministry of Transport, 15 by the Ministry of Industry, etc. At the end of the year, the 1993 privatisation programme was adopted. The new programme comprised a further 292 enterprises; later their number was increased to 318. In the two programmes, priority was given to enterprises in industry, agriculture and tourism. Market privatisation was the prevailing method.

The next years did not exceed the rates of privatisation. There is lack of deals for big enterprises. From the realised in 1995 309 deals – 205 are for specific parts, 100 – for small and medium enterprises and only 4 are sold big enterprises. From the realised from the beginning till the middle of 1996 total 2069 deals only 7% are the deals for whole enterprises. The predominant technique of privatisation (60%) are negotiations with potential buyers, at 35% of the deals are used public auctions and 15% of the sells are executed by a contest. In the end of 1996 almost 1/2 of the privatised objects are owned by the personnel of the enterprises. Till now as a whole are privatised only 4,2% of the assets of the state enterprises. More 12% are proposed for mass privatisation from which at its first auction are sold 40%.

By Decree 44 of the Council of Ministers of March 1994, a **Privatisation Revolving Fund** was set up with the Agency of Privatisation. Its main purpose is to provide funds to Bulgarian participants in privatisation. The Fund is run by a Governing Board, in which the Council of Ministers, Ministry of Finance, Bulgarian National Bank, Agency of Privatisation and Ministry of Industry are represented by one member each, plus two free experts. The members of the Governing Board are appointed by the Council of Ministers.

The Fund provides financial support to Bulgarian citizens to take part in privatisation by means of:

- ✓ extension of soft credits;
- ✓ application of by-instalment payment scheme covering up to 70% of the selling price of privatisation object.

The resources of the Fund are supplied by international organisations.

The Branch Ministries have the following functions in the field of restructuring:

- ✓ transformation and privatisation of enterprises with long-term assets up to 70 million BG Levs;
- ✓ selection and presentation to the Agency of privatisation of enterprises with higher value of assets;
- ✓ management of state participation in economy;
- ✓ closing down through liquidation of enterprises incapable to operate as independent entities.
- ✓ Given these functions, most of them have set up specialised departments responsible of restructuring. For example, in the Ministry of Industry these are the following:
- ✓ "Restructuring of State Industrial Ownership", including a specialised section "Liquidation";
- ✓ "Structural Policy and State Industry Management".

The Ministry of Trade is considered the most successful in the field, it has opened nearly 180 procedures which implies a start of denationalisation of almost 50% of the enterprises in the sector. Fifty privatisation transactions have been concluded amounting to 356 million BG Levs.

Due to many reasons, including the financial debts of the industrial firms, the privatisation in the industry is considerably slower. Only in 270 of total 1200 firms the capital is privatised over 50%. In 35 firms is introduced a regime of financial recovering and 34 firms are in the process of liquidation. About 100 other enterprises are expected also to be liquidated. In compliance with the additions to the Law on Privatisation, a new body was established with the Council of Ministers, i.e. the **Center of Mass Privatisation**. It is responsible for the organisation and supervision of privatisation through investment bonds. The Center is governed by an Executive Director appointed by the Council of Ministers.

For mass privatisation were prepared 968 enterprises with total capital over 200 milliards leva. The first auction (end of 1997) of the mass privatisation resulted in denationalisation of over 50% in 330 enterprises, 200 of which in industry.

The State Fund for Reconstruction and Development is a supradepartmental

body promoting economic restructuring through both financing of profitable projects in the private sector and temporary extension of renewal and investment credits to state firms and commercial companies.

State institutions have the difficult task to promote **also the building up of the institutional framework of market economy**, the underdevelopment of which is considerably delaying the state sector restructuring.

The first step made in this direction was the reorganisation of the financial sphere. The functions of the central and the commercial banks were full-delimited. A process of bank consolidation was initiated aiming at banks recovery. Still unaccomplished, it hampers bank privatisation. Notwithstanding the radical changes in the terms of functioning of commercial banks, their public status influences their behaviour as credit institutions and therefore reduces the effect of the economic policy of the state.

The lagging of the bank system behind the changes in economy and the delay in bank privatisation, in particular, has resulted in the low level of development of other institutions of the financial system. The number of hitherto organised stock exchanges is 16 with quoted stock of not more than 10 to 15 companies. The creation of a normally functioning money market to secure strong competition among participants is going very slowly as well.

Difficulties in institutional reforms are to a high extent common event for all Central and East European countries. They stem from the necessity in simultaneous reorganisation of economy and creation of relevant market institutions. The effect of reforms depends also on the synchronised building up and functioning of institutions, time is therefore additionally pressing state institutions. According to J. M. Buchanan, time "is the scarcest resource in the transition to market economy"³⁴. This imposes the necessity of transformation and use of some former institutions (the State Savings Bank, labour offices, etc.), restoration of previously established institutions (credit and mortgage banks, etc.) and widening the functions of the newly established ones.

3.4. Other Institutions

Pluralism in policy and economy established after 1989 created conditions for some non-governmental institutions to practically influence the course of reforms and economic restructuring. These with the greatest influence are the following:

- ✓ trade unions;
- ✓ employers' organisations;
- ✓ financial groups of big private capital.

Trade unions. They are represented by two most powerful trade unions, namely: the Confederation of Independent Trade Unions in Bulgaria (CITUB) and the Confederation of Labour "Podkrepa".

CITUB emerged in February 1990 as a successor of the former trade unions and made a successful transformation into a politically independent organisation. It numbers

³⁴ J. M Buchanan, "What Should Economist Do?". Indianapolis, Liberty Press, p. 67, 1979

about 500 thousand members united in 70 federations and more than 30 regional structures.

CL "Podkrepa" was established before November 1989 as an underground organisation. At present, it has about 50 thousand members organised in 22 federations and 12 regional structures.

Trade unions exert impact on state enterprises restructuring on mostly national and branch level. The means they mainly use are the following:

- ✓ participation in the tripartite social partnership and attainment of mutually acceptable agreements with Government and employers on the issues of economic and structural policies with regard to employees; interests;
- ✓ strike remonstrance.

Workers are the party hit hard by restructuring in the course of reforms in both their incomes and job security. For this reason trade unions insist that restructuring is economically grounded and accompanied by programmes of alternative employment.

The coordination of interests of state powers, capital and labour in solving the problems of economic reforms opens wider possibilities for the Government to pursue its policy and guarantees social peace for its implementation. Trade unions have signed hitherto four national-level agreements with the government and the employers.

The first national agreement (March 1990) couldn't effect much the reforms but put the beginning of social dialogue. A tripartite body (National Committee on Coordinating of Interests – NCCI) was set up for discussions and search of a mutually beneficial solutions of the problems of economic reforms and their reflection on production and the social sphere.

In August 1990, **another national agreement** was signed concerning the acute problems stemming from the deepening economic crisis, i.e. the sudden and speculative rise in prices, the slump in production, etc. Eight working groups were created with the NCCI, including on privatisation and state firm management.

Immediately after the coalition government of Dimitar Popov came into office, it started negotiations with the trade unions and the employers which resulted in the **national agreement on preserving the social peace (January 1991)**. The Agreement included provisions on the rise of interest rate, gradual liberalisation of prices, changes in labour and social legislation, etc. The Agreement gained the support of the International Monetary Fund.

The **national agreement (June 1991) on further development of economic reforms and social peace preservation** had the greatest importance for economic restructuring. It included a coordinated programme for the continuation of the reform, i.e. stabilisation measures, restructuring and privatisation steps. Special attention was paid to the problems in uranium and ore mining and their future development.

The system of national tripartite partnership underwent considerable changes after 1992. Instead on national level, agreements are signed in specific spheres, e.g. coal mining industry, transport, etc. These changes stem from the unstable political environment and the absence of clear-cut parliamentary support to the Government of professor Berov.

There were three rather indicative cases after 1989 in which the institutional instruments (negotiations and tension control) failed to solve the conflicts, later resulting in national strike actions, namely:

- ✓ in the fall of 1990 – against the inertness of the Government of Audrey Lukanov; these caused its downfall;
- ✓ in the fall of 1992 – against the openly neoliberal stand to reforms and trade unions and the delay of structural reforms of the Government of Phillip Dimitrov. From January to June 1992 more than 40 branch-level strikes were organised. The major centers of tension were the military-industrial complex, coal mining industry, machine-building, chemical industry, etc.
- ✓ in April-May 1994 – against financial instability and further deepening of the economic crisis, including the uncoordinated policy of professor Berov's Government in the field of restructuring.

Employers' Organisations. They are represented by:

- ✓ Bulgarian Chamber of Commerce and Industry. It was created nearly a century ago; currently it numbers 7 thousand members (employers) from 10 industries in the state and private sectors organised in 212 territorial structures, its main functions are related to assistance, promotion and protection of interests of employers and development of their cooperation and association.
- ✓ Bulgarian Industrial Association, it was created in 1990 as a successor of the former Industrial Association (1984). It has 2 thousand member-enterprises from 37 branches, its functions include promotion of technical development, market policy formation, management, assistance in the process of association of its members, joint ventures, foreign trade activities, attraction of foreign capital, implementation of modern forms of organisation and management.
- ✓ Union of Private Enterprising (UPE). It is the first organisation of private entrepreneurs in Bulgaria. The Union was established in December 1989. At present, it numbers 503 members united in 40 regional and branch structures, the Union determines itself as a free voluntary non-profit organisation aiming at the promotion of business initiatives of citizens, creation of fair trade relations and abolishing of monopoly.

The functions of considered organisations give them wide opportunities to participate in the process of economic restructuring. They are however quite passive with regard to restructuring. Their attitude is due to: first, the rather limited powers of state employers in the field of economic reforms and restructuring. Power is considered in the hands of branch ministries; second, the fact that private employers represent small and middle-sized capital which is lacking the potential to intervene in restructuring processes; third, the existence of competition among employers' organisations which disunited their efforts.

Financial Groups of Big private capital. These financial groups take part in economic restructuring chiefly through the financial institutions. The main part of their capital is concentrated in banking and insurance activities, finance management and foreign trade. For the time being, only one of them (Multigroup) has really joined the

privatisation process; its subsidiaries has bought a sugar processing plant, a hotel, oil stations, etc. investment in new productions is still inconsiderable in size. A process of intensive concentration of the private capital, mainly in the form of holding groups, can be seen. 18 groups are already formed. Some of them are with especially big size and include more than 50 firms in the country and abroad, have foreign companies, etc. An attempt for coordination of the activity of the big financial groups was the creation in the end of 1993 of the Confederation of Bulgarian Industrials, known as "G-13". The internal contradictions of G-13 prevent it from participation in privatisation with a common strategy and lately it was destroyed.

Financial groups outside "G-13" also hesitate to announced their participation in privatisation. Most attractive to big private capital prove to be financial and forex transactions, trade in securities, foreign trade, tourism and foodstuffs industry. This was confirmed also by the analysis of subject of activity of investment companies. In the end of 1994 it was only 4 out of 12 registered investment stock companies which have mentioned participation in privatisation as one of their activities. Most of them deal in export and import, financial and forex transactions, trade in securities. One of them has declared interest in infrastructure projects.

The starting of the mass privatisation and the expected revival of the trade with securities on the stock exchanges stimulates the activity of the financial groups.

4. Structural Changes in The System of State Enterprises

4.1. Ownership and Organisational Structures

Changes in the ownership structure are among the most important characteristics of the transition to market economy and the conditions in which enterprises operate. In order to study this problem, however, it is not sufficient to just analyse the ratio of stateowned and private enterprises. It should be known whether private enterprises are privatised former state ones or *de novo* established, whether state enterprises are transformed into entities of new legal status, or not. It is therefore necessary to examine not only the changes in ownership structure and its present condition, but also the distribution of enterprises by their legal status.

a) Forms of economic entities in Bulgaria

The legal status of economic agents in Bulgaria is regulated by the Law on Commerce³⁵ which was adopted in June 1991 and which was aiming to harmonise the Bulgarian legislation with that of developed market economies. It was difficult to obtain a complete identity, since the historical and cultural specifics of different West European countries had resulted also in the forms of their economic activity. The goal, therefore, was an approximation rather in the essence and not in the terms, so that the Bulgarian system was made consistent with the western one.

Pursuant to the provisions of the Law on Commerce, a merchant is the common

³⁵ Law on Commerce, State Gazette, 48/18.06.1991.

denotation for any physical or legal person engaged in business activity (purchasing and sale of merchandise, production, services, financial transactions, etc.) in Bulgaria. A merchant can be a commercial company, a cooperative or a person who has established an enterprise requiring that its activity be conducted as a commercial business. A "merchant" therefore is the most general concept on which the Law on Commerce is based.

The private merchant is the first form of economic activity envisaged by the Law which refers to any physical person who is registered at the court and who bears full liability for his obligations. The association of two or more physical or legal persons for the purpose of performing business activities is denoted as a commercial company. A commercial company shall be any of the following: an unlimited partnership, a limited partnership, a private limited company, a public limited company, and a public limited partnership. An unlimited partnership is a company incorporated by two or more persons engaged in business activity (commercial transactions) who bear joint and unlimited liability.

In the case when one or more of the partners bear joint and unlimited liability while the liability of the remaining members is limited to the extent of their pledged contribution, the commercial company is called a limited partnership. The management and representation of the company is executed by the unlimited liable partners.

A private limited company (Ltd.) is formed by one or more persons who are held liable to the extent of their contribution to the company's capital. The managing bodies of the company include the general meeting of the partners and the managing director. Should the company have more than 50 employees, they shall be represented at the general meeting with the right to a deliberative vote only.

A public limited company (Pic.) is a company which has its capital divided into shares and which is liable to its creditors to the extent of its assets. The managing bodies of Pic. include a general meeting of the members and a board of directors (onetier system) or a supervisory board and a management board (two-tier system). The members of the board of directors, respectively of the management board, represent the company jointly, except when provided otherwise by its articles of association. The difference comes from the fact that in a two-tier system the members of the management board are appointed by the supervisory board and not directly by the shareholders.

A public limited partnership is similar to the limited partnership except for that aspect that the limited liable partners are issued shares in return for their capital. The company is promoted and managed by the general partners who have a voting right in the general meeting and constitute the board of directors. Apart from these main forms of merchants, the Law on Commerce provides also for the existence of their alliances, or commercial groups, such as consortiums and holdings. The consortium is a contract-based group of merchants, while the holding is a public limited company established for the purpose of management, without engaging in any production or commercial activity of its own.

The Law on Commerce contains also provisions for the legal forms of state-owned and municipal enterprises, the main of them including the single-person limited company and the single-person public limited company. The formation of other commercial

companies or associations thereof is further allowed. It is also provided that, by virtue of a law, state-owned enterprises can be founded which are not commercial companies. The incorporation and transformation of state-owned enterprises in commercial companies is regulated by a special law, while the municipal companies are subject to a resolution by the municipal council.

b) Enterprises restructuring in terms of ownership and legal status

The most considerable changes in the industrial organisation of the Bulgarian economy are related to its organisation structure. These were accomplished in two main directions, namely: changes in the organisation forms of state-owned enterprises and a sharp increase in the number and forms of commercial companies owned by other economic agents, legal and physical persons mostly.

The provisions of the Law on Commerce had quite an advanced character, especially in the part on public limited companies, since they regulated economic relations which at that time were either completely non-existing or quite underdeveloped.

The Law on Commerce settled the problem about the consistency of formerly registered firms and the requirements of the new legislation. Firms registered pursuant to Decree No. 56 were re-registered with the following amendments:

- a one-man firm shall be considered as a private merchant;
- a collective or associated firm shall be considered as a partnership;
- a limited liability firm shall be considered as a limited liability company;
- a joint-stock firm shall be considered as a joint-stock company;
- an unlimited-liability firm which has not issued shares shall be considered as a limited partnership, while that which has issued shares – as a public limited partnership.

The above-mentioned regulations indicate that the transformation of the existing private firms (so-called citizens' firms) into commercial companies was a nearly automatic operation. The main problem pertained to the re-registration and changes in the legal status of state-owned enterprises.

Based on the provisions of the Law on Commerce, the Law on Establishment of Commercial Companies³⁶ was passed in July 1991, by which the transformation of state-owned firms into single-person commercial companies had started. State jointstock firms were registered as public limited companies, while the remaining state firms were registered as limited liability companies. In addition, a number of new joint-stock companies and limited liability companies were created as a result of the process of decentralisation.

The changes in the firm organisation of state-owned enterprises are presented in Table 1. Re-registrations pursuant to the Law on Commerce proved to be difficult to accomplish within short terms, hence the appearance in the statistical data on enterprise forms of both commercial companies and firms registered under Decree No. 56.

³⁶ 36 Law on Establishment of Single-Person Commercial Companies with State Property, State Gazette, 55/12.07.1991.

Table 1.*Registered Enterprises By Ownership and Legal Status*

Ownership, Legal Status	1993	1994	1995
A. Private Ownership			
1. Private Merchant	273194	341818	383382
2. Unlimited Partnership	36728	36769	34439
3. Private Limited Company	11867	20005	28655
4. Joint-Stock Company	941	1391	1983
B. Public Ownership			
I. Transformed Enterprises (Law on Commerce)			
5. Single-Person Limited Company	7711	12025	17021
6. Single-Person Joint-Stock Company	392	508	574
II. Non-transformed Enterprises (Decree 56)			
7. State Firm	1458	1097	776
8. Municipal Firm	1515	1036	459
9. Firm of Public Organisation	1558	778	554
C. Joint Ownership			
10. Unlimited Partnership	414	418	344
11. Private Limited Company	1189	1182	2416
12. Joint-Venture (Decree 56)	597	878	402
D. Other			
13. Subsidiary	1926	2115	2291

Source: Author's computations based on data from Statistical Reference Book, NSI, Sofia, 1996.

It should be taken into consideration, however, that data presented in Table 1 refer to the registered enterprises. Similar to other East European countries, the registration procedure in Bulgaria is lacking preciseness regarding the exclusion of non-operating enterprises from the list. According to expert estimations, functioning enterprises account for about 50-60% of the total number of registered. On the other hand, data are not included in the table about the number of operating cooperatives, agricultural farms and firms, and other entities of municipal or state significance which are registered pursuant to other laws and not to the Law on Commerce. Totally, they account for less than 10% of the number of registered entities.

The major factor contributing to the development of the private sector in Bulgaria is the creation of new private enterprises. The share of privatised state-owned enterprises is insignificant. Privatisation has made a little progress and up to now it has been applied mainly to small and medium-sized enterprises.

This conclusion is further confirmed by data in Table 3 which show that only 1558 enterprises have been privatised for the whole period (1992-95), the major part of them municipal property or single parts of enterprises. Substantial progress in privatisation is expected in the next year connected with the finalisation of a number of large-scale deals

as well as the completion of the first stage of mass privatisation. About 1,000 enterprises are to be privatised – entirely, or parts of them – through vouchers.

Table 2.

Enterprises Approved for Privatisation and Privatised Enterprises by legal forms and type of ownership

Legal forms and type of enterprises	Approved (nr.)	Privatised (nr.)
Total-	3607	1558
commercial companies	844	128
- non-transformed enterprises, autonomous parts	2763	1430
State ownership	1293	295
- commercial companies	791	108
- non-transformed enterprises, autonomous parts	448	187
Municipal ownership	2368	1263
- commercial companies	53	20
- non-transformed enterprises, autonomous parts	2315	1243

Source: Author's computations based on data from Statistical Reference Book, NSI, Sofia, 1996.

The main changes in state-owned enterprises are related to their transformation (incorporating). In general, this process has taken place mainly in the first year following the adoption of the Law (1991-92) and has developed at a considerably lower pace in the next years. After 1993, non-transformed state-owned and municipal firms decreased twice in number. This was due to two main reasons: first, the continuing process of transformation, and, second, the privatisation of non-transformed state-owned enterprises. Comparing the figures in Table 3 on the number of approved for privatisation non-transformed enterprises and the number of the remaining non-transformed public enterprises (Table 1), it can be concluded about a prevailing policy towards privatisation without a preliminary transformation of enterprises.

The increased number of independent enterprises in the economy as a whole and in sectors and subsectors is a solid ground for abolishing of monopoly. The maximum possible level of decentralisation has been achieved thus providing the prerequisites for economic demonopolisation in most of the sectors. Some one-plant enterprises have preserved their monopoly positions due to their role of sole producers of particular goods; the same applies to some enterprise complexes in sectors and productions in which Bulgaria has formerly specialised within the CMEA area (for example, Balkancar, Bulgartabak, etc.). Yet, even those complexes don't integrate all enterprises in the subindustry as it used to be before. For example, in lifting and transport machine-building

the production of elevating gears and equipment (cranes, lifts, electric hoists, store equipment) is allocated in independent plants. The same applies to some primary productions as electromotors, diesel engines, etc. As a result, except for "Balkancar" a further 31 independent joint-stock companies, limited -liability companies and firms have emerged in the subindustry of lifting and transport machine-building.

As is well-known, antimonopoly policy can be pursued by either domestic or competition from abroad. The impact of foreign producers is of considerable importance to large economic organisations in Bulgaria. The case of "Balkancar" is indicative of the fact that such kind of groups face extremely sharp competition not only at foreign markets but also at home because of the increasing supply of cigarettes from America, West Europe and Greece. State enterprises decentralisation is the main factor predetermining the creation of conditions for demonopolisation of economy. Although much more in number, private firms and other institutional owners exert a far smaller influence on the creation of competitive environment. This is due to both their small size and their just symbolic presence in many of the industrial sectors and especially in large-scale heavy industry. State enterprises decentralisation is the main but yet one of the steps towards establishing of really demonopolised and market competition sensitive enterprises. The latter should be further privatised (or the greater part of them, at least) and the very market environment should be created for their functioning.

The variety of organisation patterns in Bulgaria could be given a similar estimation. More and more firms and groups of different kind are continuously coming into being under the regulations of the Law on Commerce (for example, commercial groups like consortiums, holding companies, etc.). This is not enough, however, to state that organisation patterns of enterprises are created as institutions of normally functioning market economy. Their real creation and full-value existence needs time first; and second, this process is closely related and dependent on the development of other market economy institutions.

Changes in enterprise management and control are of the most important elements of the process of enterprise change. Depending on the different organisation patterns of enterprises, two aspects should be mentioned: first, building up of entrepreneurs capable to promote development and execute management and control in small and medium enterprises; second, creation of corporate management in joint-stock companies. The problem is complicated by the need in changes in two parallel directions, i.e. in the emerging private businesses and in the transforming state enterprises. Problems in the second direction are more complicated and hard to solve due to emerging non-economic contradictions and the necessity of bringing the requirements for efficient changes in compliance with avoiding the crash of the state sector since the latter is still the basis of economy.

Management and control of enterprises are closely connected and dependent on the clear-cut determination of property rights. In this respect, an important change was made in 1991 by abolishing the rather confused combination of workers' self-management, technocracy and state intervention. The Council of Ministers was assigned the responsibility for the functioning of state property and in August 1991 an Ordinance on the management of single-person commercial companies with state participation was

adopted. The basic rules of manager competition were developed aimed at changing the system of managers' appointment from based on political to one stressing the professional qualities of applicants.

Another important act regulating the activity of state enterprises was adopted in early June 1992. The Council of Ministers passed a Decree under which the Ministers of Industry, Trade and Transport were assigned the transformation of firms registered pursuant to Decree 56 into single-person commercial companies with state property, in this way, the final step was made towards equalising the status of state enterprises in correspondence with the provisions of the Law on Commerce. Under above mentioned Ordinance (1991) manager competitions were carried out by branch committees appointed by the Government. Moreover, direct state participation in management and control was also secured by the inclusion of government officials in the collective governance of enterprises.

The criteria of estimating the merits of applicants incl. not only their personal and professional qualities but also evaluation of the proposals they have presented on improving the functioning of enterprises, analysis of current state and programme for future development. Manager competitions failed to meet their goals in full. The greater part of former managers were dismissed but in many cases the newly nominated were not the proper ones in terms of competence and professional experience. This was partly due to the short terms of organising the competitions and the strong pressure exerted by influential and very active trade unions. The actions of the latter resulted in very difficult to settle contradictions between the Ministry of Industry and trade unions themselves. For particular cases, a compromise was reached by transforming limited-liability companies into joint-stock companies, so that representatives of both parties could enter the collective management bodies.

The competition results were unsatisfactory with regard to the second goal, i.e. approval of programmes for improvement of enterprise functioning. Given the applicant hadn't a preliminary prepared programme, it was simply impossible to cover in such a short time the enormous work on analysis of current state, estimation of possibilities, strategy choice and most adequate means for its implementation. Besides, a general branch committee is hardly expected to give a most precise estimation of specific production suggestions and programmes. Third, the general economic environment does not provide executives with much freedom for real manager behaviour. The general conclusion can be made, therefore, that changes in the ownership structure of Bulgarian economy are still at their initial stage. Most probably, the creation of modern forms of economic organisation will be completed in the next year. Certain problems can emerge in the functioning of enterprises, stemming from insufficient changes in ownership patterns. The large share of state ownership is sure to have a negative effect on the control exercised by proprietors on managers as well as on enterprises performance.

4.2. Enterprise Size Structure

In the conditions of transition, fast changes have started in the size structure of enterprises in the Bulgarian economy. These changes are accomplished in the following main directions: first, an increase in the total number of enterprises, both in the economy

as a whole and by branches.; second, an extremely fast growth in the number of small enterprises, which is the main generator of the changes in the former size structure.

The aim of studying these changes is to determine their intensity and to answer the question of whether and to what extent has the size structure of Bulgarian economy got closer to that in the developed market economies.

a) decentralisation and increase of the number of enterprises In April 1991, the Council of Ministers adopted a Decree providing for the accomplishment in very short terms of the decentralisation and demonopolisation of large state-owned associations and combines. The firms in seven branches, including electronics, telecommunications, energy, metallurgy, machine-building, chemical and cereal-processing industry, had to be restructured following a profound expertise according to a list of indicators suggested by the Minister of Industry and approved by the Council of Ministers.

Apart from associations, another group of state-owned and municipal firms with more than one enterprise had to be decentralised as well, which at that time hadn't the status of independent legal entities.

In its general part, this program was accomplished within several months, the greater part of associations decentralised in July 1991 by a series of decisions of the Minister of Industry and Trade.

Data point to the emerging variety in the organisation forms of state-owned enterprises as well as to the extremely sharp growth in their number resulting from decentralisation. For a 5-year period, this number has increased by more than 26 times, the fastest pace being in 1991.

The increase in the number of non-private enterprises (state-owned, municipal, cooperative, etc.) is observed in the total economy and by sectors (See, Table 1).

Table 1.

Distribution of State-Owned and Other Non-Private Enterprises by Sectors

	1989	1990	1991	1993	1994	1995
Total	1534	3491	30660	38779	42401	41984
Industry	563	823	3508	3971	4048	3798
Construction	305	409	1154	1313	1284	1106
Agriculture	259	1245	2537	4499	5570	5367
Transport	89	120	506	651	644	594
Trade	141	430	2449	3386	3511	3422
Science	81	198	534	833	793	643
Education	4	9	8459	9110	9067	8902
Culture and Art	8	12	5005	5158	5059	5043
Health, Tourism	12	34	3278	4024	4202	4210
Finance, Insurance	2	5	63	792	882	938
Other	-	2	2089	5042	7341	7961

Source: National Statistical Institute

Regardless of inevitable differences, the number of entities has increased by several times in each of the sectors. A particularly high growth is observed in trade, education, culture, tourism and finances. This is due to comparatively better opportunities for the creation of small enterprises in these fields, the higher profitability and certain preferences provided by Law.

Recent data, however, point to a stagnation and even a decreasing number of nonprivate enterprises. This indicates for an exhaustion of the capacities for existing enterprises decentralisation or for the creation of new enterprises in non-utilised production and service niches.

The highest growth rates are demonstrated by new-established private enterprises, i.e. from 24537 by end-1990 to 466445 by end-1995, of them more than 60000 operating in industry. Estimating the significance of private enterprises, it should be taken into consideration that by expert appraisals about 40-50% of them are not functioning, while more than 90% employ less than 5 persons. Therefore, admitting the high 'birth' rates of this sector, one should at the same time account for their weakness and quite probable high rate of 'mortality' unless incentives and preferences are adopted to support the small business.

b) changes in the size structure of Bulgarian economy

The decentralisation of state-owned enterprises and the fast growth of the private sector have made for the substantial changes in the size structure of Bulgarian economy.

Table 2.

Enterprises by Size Groups in the Bulgarian Economy (1995)

Sectors, Ownership	Total number	Micro, %	Small %				Medium %		Large %
			2-10	11-20	21-50	51-100	101-300	301-500	
Economy	77518	75.2	6.9	7.5	4.7	3.8	0.8	1.1	
- private	60074	92.2	4.9	2.7	0.9	0.4	0.05	0.06	
- state -owned	17444	19.6	14.9	23.9	17.7	15.9	3.4	4.6	
Industry	14863	70.6	6.7	6.6	5.4	6.6	1.7	2.4	
- private	11967	86.3	6.7	4.2	1.7	0.9	0.1	0.1	
- state- owned	2896	6.0	6.8	16.7	20.6	30.1	8.0	11.8	

Source: Author's computations based on data of NSI.

In Table 2, data are presented only for state-owned and private enterprises employing more than one person. The smallest size group, i.e. 1 or 0 employees, is excluded although it covers about one-half of the total number of enterprises in the developed countries and more than three-fourth of enterprises in Bulgaria. On the other hand, the greater part of non-functioning and unstable enterprises come from this size group.

In 1995, the size structure of enterprises in the Bulgarian economy approached the levels in the developed economies (See, Table 3). The share of micro and small enterprises in Bulgaria is still lower, while that of medium and large enterprises is exceeding the levels in the developed countries. Anyway, these differences are not so substantial given the initial structure in 1989. It is obvious from the figures in Table 2, that even after a multifold increase of the number of small state-owned enterprises, their structure differs a lot from the usual structures in market economies. The share of different size groups cannot present the whole picture of the on-going processes of adjustment of the size structure of a transition economy. An additional indicator could be the number of enterprises in a particular size group per 10,000 inhabitants (See, Table 4). The comparison of data points out that the total number of enterprises in Bulgaria is by 1.5-3.5 times smaller than that in the developed countries. The same ratio is valid with regard to micro and small size groups. Considering the upper subgroup of small enterprises (50-99) and the group of large enterprises (500+), the number of enterprises in Bulgaria is coinciding with the average levels in developed countries, while the middle size group outnumbers the corresponding figures by 1.5-2 times.

Table 3.

Enterprises by Size Groups in the Developed Market Economies

Countries, Enterprises	Total number	Micro, % 1-9	Small, %			Medium, % 100-499	Large, % 500+
			10-19	20-49	50-99		
EU	6744024	84.7	8.2	4.6	1.3	1.0	0.2
USA	5044808	77.1	11.2	9.3	5.2	1.7	0.7
Canada	822494	91.8			1.7	1.1	0.2
Japan	1706926	70.4	14.1	9.6	3.2	2.7	
Australia	360900	80.0	11.0	5.8	1.7	1.6	

Note: EU, USA, Canada, Australia – 1990; Japan – 1991.

Source: Enterprises in Europe. Third Report, Vol. I, Eurostat, p. 28

Table 4.

Enterprises by Size Groups per 10,000 inhabitants

Countries, Enterprises	Total number	Micro, % 1-9	Small, %			Medium, % 100-499	Large, % 500+
			10-19	20-49	50-99		
EU, 1990	2060	1744	169	95	27	21	4
USA, 1990	2019	1556	226	189	161	34	14
Canada, 1990	3092				53	34	6
Japan, 1991	1377	970	194	132	44	37	
Australia, 1990	2111	1687	232	122	36	34	
Bulgaria, 1995	923	695	64	69	43	42	10
- private	715	654	33	19	6	3	0.4
- state-owned	208	41	31	50	37	39	9.6

Comparing the figures, the following directions of changes in the size structure of Bulgarian economy can be expected: first, an increase in the total number of enterprises; second, an expansion of small size groups (1-49). The preconditions for such developments are available, since the total number of enterprises, incl. the zero-group, is equal or larger than that in the developed countries. It is normal to expect transformations and resulting expansions of the upper size groups.

Changes in the size structure of transition economies through an increase in the total number and the number of micro and small enterprises create better conditions for the development of market relations. As a next stage, a development of the relationships between small and large enterprises can be expected which will result in the formation of the 'dual' size structure of the economy.

4.3. Financial Restructuring

In the transition period to market economy the necessity is still preserved of intensive relations between the state and the firms. Under the conditions of quasi-market environment and absent market institutions, the state has to fulfil functions similar to that of the market in normal market economies, such as obeying financial discipline, financial restructuring or liquidation of enterprises, etc. In Bulgaria, the main problems in this sphere are connected with subsidies and budget dotations, liquidation and financial restructuring of enterprises.

a) production subsidies and budget dotations

Direct budget financing of enterprises amounted to 12.5 bin. BGL in 1994 and 12.6 bin. in 1995. In terms of constant prices, this is a reduction of about 30-40% in both the relative share of subsidies and dotations in the total operational income of enterprises and in their absolute value. As seen from Table 1, as a relative share in operational incomes, this decrease is bigger in dotations (about 2 times) than in subsidies (25%), which is a positive tendency.

The major part of production subsidies (96%) is directed to two sectors, industry and transport. In terms of relative share, however, they are higher (4 times) than the average for the economy only in transport, almost equal to the average in industry, and lower than the average in all other branches.

The main part of dotations in 1994 (53%) was directed to industry. This share demonstrated a considerable decrease in 1995, down to 21%, yet remained above the average for the economy. The highest share of dotations went to construction, while the greatest increase in 1995 was observed in trade, the three sectors thus receiving about 80% of total volume of dotations.

Production subsidies and dotations are quite unevenly distributed between the subsectors of industry (See, Table 2). Nearly a three-quarter of subsidies is directed to coal mining and production of electricity. The same branches have also the highest level of subsidies per unit of operational income – 2-3 times in electricity and more than 20 times in coal mining. The rest of industrial branches are either close to the average for the economy (for example, non-ferrous metals) or considerably lower.

Table 1.

Production Subsidies and Budget Dotations by Sectors and Years (in bin BGL and current year prices)

Sector	Year	Operational Income	Production Subsidies	Budget Dotations
Total,	1994	714.9	9.9	2.6
incl.	1995	1029.3	10.7	1.9
Industry	1994	462.0	6,5	1.4
	1994	694.8	6.4	0.4
Construction	1994	28.8	0.1	0.3
	1995	39.4	0.1	0.5
Transport	1994	66.8	3.1	0.1
	1995	86.2	4.0	0.2
Communicat.	1994	14.0	0.02	0.3
	1995	19.3	0.04	0.3
Trade	1994	127.9	0.07	0.1
	1995	164.8	0.4	0.6
Other	1994	4.0	0.025	0.009
	1995	4.8	0.016	0.021

Source: Author's computations based on data of NSI, Financial Condition of Enterprises '95.

Table 2.

Production Subsidies and Budget Dotations in Industry (in mln. BGL in current year prices)

Sector	Year	Operational Income	Production Subsidies	Budget Dotations
Industry,	1994	462036.4	6464.1	1419.2
incl.	1995	894786.8	6382.0	378.7
Electricity and	1994	38099.2	1856.6	860.5
Steam Production	1995	59987.5	1425.0	4.9
Coal Mining	1994	11591.8	2919.0	-
	1995	15699.3	3943.1	-
Non-ferrous Metallurgy	1994	27782.8	545.2	397.2
	1995	43545.2	480.9	263.0
Chemical and Oil	1994	114866.3	7.1	2.4
Industry	1995	183309.2	6.5	2.6
Machine-Building	1994	41164.9	27.0	5.2
	1995	59630.5	20.2	10.6
Textile	1994	19281.8	0.2	0.9
	1995	27207.9	0.2	1.3
Sewing Industry	1994	5938.4	2.4	2.0
	1995	8249.0	8.8	8.9
Foodstuffs	1994	84605.8	334.2	82.6
	1995	118959.8	93.4	22.8

Source: Author's computations on data from NSI, Financial Condition of Enterprises '95.

In their main part (88%), 1994 dotations were directed to production of electricity and non-ferrous metallurgy. Actually, non-ferrous metallurgy was the only branch dotated in 1995. There was a drastic decrease in dotations for electricity, while their level in the other branches was insignificant.

Studying data in Table 2, it can be concluded that the main reason for direct financing of enterprises by the budget is the maintenance of lower prices of energy carriers.

b) Financial restructuring and liquidation of enterprises

The delay of structural reforms in Bulgaria has brought about a series of problems, incl. bad financial results in a great number of enterprises. In April 1996, the Government advanced a program for restructuring, consisting of two main parts – liquidation, and financial restructuring of loss-making state-owned enterprises.

The program of financial restructuring includes a list of 36 industrial enterprises: 15 in machine-building, 5 in electrotechnical industry, 4 in chemistry and oilprocessing, 5 in textile, 3 in non-ferrous metallurgy, 2 in ferrous metallurgy, and 2 in glass industry.

The total debt of these enterprises amounts to 54.6 bin BGL, which is equal to their capital (54.5 bin. BGL), or their fixed tangible assets (59 bin. BGL). This is an indicator of a very high degree of decapitalisation of enterprises included in the Program, yet comparing the figures it should be kept into account that a revaluation of assets has not been made in Bulgaria since 1992, therefore the value (resp. price) of these enterprises should several times higher.

In terms of current financial results and indebtedness, enterprises can be classified into 4 main groups, namely: positive results and small debt, positive financial results and very big debt, current loss and small debt, and current loss combined with very high indebtedness. Obviously, enterprises suffer different problems and the solutions should be searched for each case in particular.

Enterprises are given three months to prepare individual plans for financial restructuring in a one-year term. Be they successful, enterprises will be allowed rescheduling, reduction or cancellation of old debts; in the opposite case, measures will be undertaken for their liquidation. Enterprises included in the financial restructuring program are under the governance and supervision of the Ministry of Finance.

Like in some other East European countries, the governments in Bulgaria have proved to be rather reluctant towards the liquidation of state-owned enterprises. The reason here is neither the absence of adequate legal basis, nor the non-existence of badperforming state-owned enterprises. Actually, there hasn't been adopted a particular law on bankruptcy, yet the Commercial Law (1991) includes a special chapter regulating this issue.

It was realised only in spring 1996 that any further delay in the solution of these problems would be crucial, and steps were undertaken in two directions: first, workingout a program for liquidation of a part of enterprises in extremely bad financial condition, and, second, creating the prerequisites for the normal functioning and application of already existing legislation regarding the liquidation of loss-making state enterprises.

The program for liquidation has been initiated by the World Bank and the International Monetary Fund and is accomplished with the financial and expert assistance of these institutions.

There are 64 state-owned companies included in the list for liquidation, of them 38 in industry. These companies account for 3% of the total number of employees, 7% of the fixed assets, and more than 30% of the losses in the sector. The total debt of enterprises in the list exceeds by 2.6 times their fixed capital and by 2 times their long-term tangible assets. The goal of the program, therefore, is to improve the general performance of the sector, with a minimum negative effect on the employed.

Liquidation procedures have been opened for 27 of enterprises, while the remaining 11 will be privatised. Privatisation deals have been already concluded for 8 of them, the rest are in process of negotiations with potential buyers.

As a result of the application of the provisions of the Commercial Law regulating the liquidation of companies, closing and liquidation procedures have been opened for another group of 44 loss-making enterprises. These are mainly small-sized enterprises with a total of 1070 employed.

5. Case Studies of Bulgaria

5.1. Electronics — A Restructuring at the Price of Severe Reduction of Personnel

5.1.1. General State of the Sector

In 1993, Bulgarian electrical engineering and electronics produced 5.9% of total industrial production and employed about 10% of total industrial work force. The sector has fallen in a deep crisis since the start of reforms in early 1990s. In volume terms, 1993 production was 61.6% down the level in 1990. The decline is due both to the collapse of former CMEA markets and the problems connected with finding new raw material suppliers. (In the expenditure structure of enterprises in electrical engineering and electronics in 1993, material expenses amounted to about 60% of total expenses.).

The last data available give information for the first three quarters of 1994, evidencing for a continuing decline of production. Compared to the same period in 1993, the decline equals to 12 percent. The average machine loading as of October 1st, 1994 was 52% (51% in 1993, respectively).

5.1.2. Characteristics of P-01

P-01 is a state-owned company specialized in the production of three main product groups: disks, technological equipment and consumer goods. Till now, information has not been collected on the structure of sales by product groups.

The state company consists of 26 enterprises, all of them located at the territory of the city where the company's head office is placed.

P-01 can be classified as a 'big company', as under the classification standards companies with 1000 and more employees belong to the group of big companies. The employed numbered 6966 as of 31 December 1990, 5088 and 4015 at the end of 1991 and 1992, respectively.

The volume of sales in 1990 is incomparable to those in the next two years as in 1990 P-01 was still a state-owned firm with subsidiaries located outside the city of the head office. The volume of sales was 430974 thous. Leva in 1991 and 663480 thous. Leva in 1992. There was a reduction in the physical volume of production in the studied period, and the growth of sales was due to the rise in prices and product restructuring.

P-01 was established as a state-owned company in 1968 by an act of the Council of Ministers. The company was under the supervision of the Ministry of Industry.

After the transformation on November 1st, 1991, P-01 became a single public limited company (PLC) with a hundred percent state share. The pattern of ownership has not been changed since then. Managers are not informed about whether and, if 'yes', how the company will be privatized.

5.1.3. Shocks of the reforms

Since the start of reforms in early 1990s, the collapse of the CMEA market has been the major shock effecting the company. Till end-1989, P-01 had a narrow specialization and a guaranteed share in that market fixed by the intergovernmental agreements between the East European countries. The fulfillment of planned orders has been provided by priority state assistance in the field of investments, credits and raw material supplies. The collapse of the CMEA market, however, put an end to the priority place of P-01 in the Bulgarian economy. The chain reaction of shocks started with the breakdown of CMEA relationships, went through the loss of preferences provided to P-01 by the state, and finished in the lack of markets for its production.

At the first stage of reforms, the following changes effected the company most severely, namely:

1. The collapse of the CMEA.
2. The abolishment of state subsidies.
3. The changes in employment terms, i.e. wages and dismissals.

The last one resulted from the lack of outlets. In practice, this meant permanent problems with payroll payment and firing of nearly 40 % of the employed in the period 1990-1992.

According to the managers, changes in ownership rights (relaxed ministerial control, changes in ownership, higher autonomy or changes in the management) cannot be estimated as considerable shocks to the enterprise.

In the opinion of managers, the company has been facing one and the same problems at the start and during the last six months of the reforms.

The loss of markets is the major problem.

Other priority problems include the increased resource expenses and the higher labour expenses, in particular, the improvement of quality, and the lack of investments in new technologies.

The change of information systems, mainly in the field of marketing and accountancy is an important problem as well.

It should be mentioned that the enterprise doesn't suffer considerable problems connected with durable equipment and labour force employed, as these are of high level. Neither has a necessity arisen in changing the volume of store.

5.1.4. Short-term responses of the enterprise

5.1.4.1. Changes in management

The present organization structure is a public limited company with 26 subsidiaries. The managers may propose the organization and management scheme of the company.

P-04 has a one-tier management system as under the Commercial Law and is governed by a Board of Directors. The members of the Board were changed eight months ago by the Minister of Industry. According to the managers, it is the Minister who can explain in detail the reasons behind the new appointments.

The constitution of the Board of Directors follows a procedure based on an order of the Minister of Industry. The competencies of the Board are regulated by the Commercial Law.

P-01 has a two-division organization structure: the first division is connected with the production of disks and disk components, and the second one with electro-mechanical equipment, parts and servicing. The top managerial staff of the company includes the Executive Director and the directors of the two divisions. The company hasn't a director of finance, nor a director of marketing.

The Executive Director is an engineer graduated from a Bulgarian higher institute, and has an international experience. He was promoted by the internal company circles.

The Director of the first division is an engineer, graduated in Bulgaria, appointed after a promotion from inside.

The Director of the second division is an engineer by education, graduated abroad. He was appointed after a company promotion, too.

Recently, some changes have taken place in the managerial staff of P-01. These were connected with the new management structure and the emergence of additional posts, i.e. the directors of divisions were appointed deputies to the Executive Director.

The remuneration of the managerial staff hasn't undergone recent changes. Due to its hard financial condition, the company couldn't take much advantage of Decree 265 of the Council of Ministers of December 28, 1992. The salaries of managers are rather close to the average level in the company.

5.1.4.2. Organisation and management structures

The shock connected with the collapse of the CMEA market has set forth the necessity in developing products oriented at the Western market. At present, a restructuring of the company is going on with product restructuring of P-01 as a first priority. Each of the 26 divisions of the company has undertaken restructuring, too, aimed at developing sellable products.

Organization and technological restructuring are on-going, too, yet they are subordinate to product restructuring as far as it is the determinant, and not vice-versa.

Notwithstanding shocks and negative effects, the reforms from the early 1990s have presented some, though rather small, opportunities to the company's development. These are connected with access to new markets and greater independence in setting prices, changes in the product structure and in the markets. The access to new markets and the investment decisions, however, are still goals to achieve. The release of abundant work force is also a positive factor in the new environment, yet it is under the limiting pressure of trade-unions.

The company has not found new sources of financing and resource supply. Though in an active search for foreign investors, the latter are not considered an important factor of company's development in the near future.

5.1.4.3. Markets, sales, production

The main responses of P-01 to above-mentioned problems relate to the following aspects of its activity:

1. Production: A reduction in the volume. Production will be further diversified and its quality will be gradually improved. Prices are compatible with world price levels. A process of product restructuring is going on in the 26 divisions of the company.
2. Finance: An increase of bank loans. Even payroll payments are covered by bank loans.
3. Utilization of production capacities: It is hard to determine the movement in labour expenses per unit of production because of the rise in wages connected with inflation rate and dismissals.

A small part of the machinery is under rent. The management is in a process of negotiating the sale of part of the long-term assets of the company.

4. Suppliers: New suppliers have been found both at home and abroad. These should not be connected with the creation of whatsoever new companies or ventures.

5. Markets: There is a certain number of customers created but it is not sufficient. The company makes technological transfer of licenses and not patents.

6. Organization and management restructuring: It is a result of product restructuring. The company is not privatized and there aren't clearly stated privatization plans. An important response to mention are the intensified negotiations with foreign partners aiming the attraction of investments and establishment of joint ventures.

The information systems of the accountancy and marketing departments are in a process of restructuring as well.

The managers estimate these responses as parallel in time and mutually consistent. Some of them are already accomplished – the reduction of production and the rise of prices, for example.

Anyway, the main adjustment responses of the company are on-going, including negotiations with foreign investors, the search for outlets, diversification of production, selling of non-usable assets, improvement of information systems.

Managers find it hard and useless to rank the responses according to their importance. They estimate them as a complex of factors directed at achieving the company's competitiveness at the international markets.

The factors which hamper the adjustment of P-01 to new conditions are ranked according to their significance in the following order:

First, the deficit of financial resources.

Second, the barriers to capital restructuring.

Third, the intervention of trade-unions in labour-force restructuring (reduction).

In their efforts to solve the problems of adjustment, managers have always been looking for the cooperation of other economic agents. With regard to domestic sources, the following initiatives can be mentioned, namely:

1. Attraction of foreign investors by providing guarantees for know-how, repatriation of profits, tax facilitation, etc. To this end, P-01 has approached the government with a proposal for creating a free customs zone on the territory of the company and on the territory of the city later on, given its importance as both commercial and production center.

2. In the sphere of product restructuring. The company has submitted projects to the Ministry of Industry and Technologies in order to apply for financing by the "Restructuring Fund".

3. In the sphere of financing. P-01 has applied for bank credits with guarantees provided by the Ministry as the owner of the company.

There is also a search for foreign cooperation but the company lacks guarantees to offer to potential foreign investors even when turnover capital is concerned.

5.1.5. Long-term responses of the enterprise

Since the start of reforms, survival has been the main goal of the company. The maintenance of the current situation is a priority goal for the next year.

Growth of production, restructuring and marketization are the goals set in the midterm three-year programme of the company.

According to managers, the goals and priorities of the company change in compliance with the general economic state of the country. In the period following the first shocks, the aim was a mere survival. At present, having undertaken a series of steps for financial stabilization, the company makes efforts to preserve some of its achievements. Growth in production and penetration into new markets is expected after intrafirm restructuring which is connected with the general governmental policy towards restructuring of the economy.

Till now, the company has never been close to bankruptcy.

At present, finding of new outlets, providing of resources and maintenance of employment constitute the main strategy of the company. Profit maximization is not a strategic goal for the time being.

The design of new products, increase of market share, attraction of foreign partners, and investments in new technologies are set as both short and long-term goals of the company. Profit maximization, however, will be a priority in three years at earliest.

5.1.5.1. Enterprise management. Changes in ownership

The managers of the state-owned P-01 do not consider ownership rights an issue of prime importance. The changes in ownership rights since the start of reforms in early 1990s (relaxed ministerial control, changes in ownership, greater autonomy, changes in the management) have not had the effect of shocks to the enterprise. A certain unclarity of this problem is not a factor limiting the enterprise adjustment. Managers have no information on eventual changes in ownership in the near future.

The collapse of the CMEA market and the abolishment of subsidies are pointed out as the main shocks to P-01. The loss of market is the main problem, along with the deficit of financial resources necessary for capital restructuring. The responses of the enterprise include various economic actions, and not restructuring of ownership rights, i.e. privatization.

The current situation of P-01 points to some other conclusions as well.

The main economic agents of P-01 as a single PLC are the government, the Board of Directors and the managers. In the structure of ownership rights, the owner of assets, i.e. the government (governmental officials) takes the residual risk and relevant responsibility, while the operative management is carried out by the managers under the supervision of the Board of Directors.

The question is who takes the residual risk for P-01 after the collapse of CMEA markets and the abolishment of subsidies? All the negative consequences should bear the owner, i.e. the government. State officials, however, take the risk rather because of their position than of any adventure inclination. Besides, they often lack the necessary personal and professional qualities and usually transfer to the company the responsibilities connected with the search for new outlets and financial resources for capital restructuring. This is done by giving the company the so-called 'autonomy', i.e. a hypothetical freedom in determining products, markets and investments. The residual risk is thus transferred to the company, which is very inefficient because: first, the bearer of the risk remains non-personified, i.e. board of directors, managers or the whole personnel; second, the risk-bearing function is transferred without legal restructuring of ownership and hence the great insecurity of future development.

Having this in mind, the main shock for P-01 since the start of reforms seems to be rather the higher autonomy of the company (residual risk and management functions) than the collapse of East European market, as the company is not the owner of assets and is therefore not allowed selling its ownership rights.

What is the reason behind the different degrees of autonomy given to different companies? Generally, it is determined by the quite complicated relationships between state officials, on the one hand, and managers, staff and company, on the other. Sometimes, as is the case of P-01, managers and staff suffer unfair losses, in other, enterprises gain unfair advantages. All this results in inefficient distribution of resources and social tensions.

P-01 has been established as a single PLC under the will of the executive power and not the free initiative of independent economic agents. Therefore its existence must be

supported even at the price of high transaction costs, including information supply, conclusion of contracts, supervision of labour behaviour, etc. Due to these high expenses, the government fails to meet its responsibilities and hence behaves as an irrational owner.

With the given structure of ownership rights, managers pursue strategies directed at company survival, revival of production and gradual growth. The absence of radical rationalization of ownership rights, however, turns these strategies into mere intentions. In the case of P-01, privatization will solve the problems with markets and financing of capital restructuring. At the present stage, state officials prove to be the most irrationally behaving economic agents. The members of the Board of Directors share different risks to lose their jobs. Managers and staff appear to be most interested in the company's vitality. They are therefore expected to undertake an efficient privatization initiative and make proposals for a substantial change in the way the company's problems are solved.

5.1.5.2. Investments. Changes in the production structure.

At present, the enterprise is in a search for foreign investors. The available facilities are rationally used, including by renting and selling parts of the assets. Product restructuring is a priority from the viewpoint of creating real markets for the company.

5.1.6. Estimation of adjustment measures and perspectives of the company

P-01 is a big company and its main agency problems are related to the mediation between the single shareholder-the government and the managers of the company.

It is a theoretical assumption that as far as the owners bear the residual risks of company activity, they are interested in the efficient use of capital and to this end can find mechanisms to 'disciplinize' the eventual manager opportunism. In the mixed Western economies, such kind of mechanisms are for example the capital market, the manager labour market, the market for corporate control, the managerial ownership, the system of manager compensations, the establishment of a special institution called 'board of directors', etc.

Obviously, since the start of reforms P-01 has functioned in an environment lacking developed market institutions, hence their negligible effect on manager behaviour. The peculiarity of the case is that by transferring to the company the risks from the market collapse and paying no attention to its initiatives related to the customs free zone, financing from 'Restructuring' Fund and providing credit guarantees, the owner, i.e. the state officials, behave in a way rather contradictory to the main axiom of capital ownership, i.e. that of efficient capital management.

In this situation the nominal owner, in fact the government and the Ministry, acts very inefficiently. Instead of preventing a possibly irrational manager behaviour, it is the owner of P-01 that manifests opportunism towards capital management. Who should defend the interests of capital in the company? Are managers capable of doing it provided they are interested in preserving their jobs?

In the conditions of underdeveloped capital and manager markets, it is hard to expect

anybody else but the capital investor to defend the company interests. The 'autonomy' of P-01 is a rather unstable condition with negative effects to both the national wealth and social peace. There are two possible directions of behaviour out of this disequilibrium state, namely:

First, the government should undertake all the rights and responsibilities related to residual risks, restructure the capital and take measures for the financial recovery of the company (its further privatization is just another question).

Second, instead of present 'pseudo-autonomy', the government should transfer to the managers and staff not only the responsibilities but also the ownership rights on the company assets.

State officials seem to dislike both the alternatives as in the first case they have to spend a lot of efforts and funds, and in the second they will lose their power.

The hypothesis of real company autonomy can be realized by a bottom-to-top manager initiative for privatization under Art. 4 of the Law on restructuring and privatization of state-owned and municipal enterprises, which provides big shares in ownership to managers and staff along with considerable financial sources for capital restructuring. To be fulfilled, such a project needs the approval of the government and the provision of guarantees to potential foreign investors. In other words, state officials take the leading role again.

The Board of Directors is the institution to exercise the supervision on managers of P-01. Its members are often changed, however, which is yet another proof of the lack of clear-cut and efficient owner behaviour.

Managers are not aware of any privatization plans; actually, they follow a wait-and-see position on the most important issue related to the use of capital.

5.2. Machine-Building — Active Management Towards Restructuring

5.2.1. General State of the Sector.

During the last thirty years there was only one major producer of foodstuff machinery at the Bulgarian market. This was the enterprise under study, P-02, its main three product groups covering more than a half of the market in the country. The rest of the domestic demand in foodstuff machinery was covered by imports, mainly from Italy.

The monopolistic market structure was shattered with the start of reforms in the early 1990s. At present, the share of P-02 in the Bulgarian market is about 25 %. The remaining part of production of foodstuff machinery is covered by other Bulgarian producers, 25 %, and by foreign producers, 50 %. According to an expert assessment of the managers of P-02, the competitive producers number from 5 to 20.

The production of foodstuff machinery and technological equipment in 1992 was 74.2% the level in 1991, and 61.2% the level in 1990. This is in conformity with the general tendency of decline in machine-building and metal-working as a whole. The volume of production in 1993 was nearly 55% less as compared to that in 1990. In 1993,

the sector accounted for 9% of the total industrial production in Bulgaria (17.3% in 1990), and employed 21% of the total number of employees in industry.

Statistical data for the third quarter of 1994 point to a slight upswing in the sector, i.e. a growth of 1% in production (compared to the same period of 1993) and an increased use of capacities as of 1 October 1994 (53% against 50% in 1993). This positive trend applies to the enterprise under study as well.

5.2.2. Characteristics of P-02

P-02 is a state-owned enterprise in the machine-building sector, specialized in foodstuff machinery. In 1994, it had the following production structure: bottling machinery (40% of sales), canning machinery (20% of sales), dairy machinery (20% of sales), and other machinery for processing of agricultural products (20% of sales).

P-02 was established by the state in 1968. It is under the supervision of the Ministry of Industry. In 1991 the enterprise was transformed into single public limited company (PLC) under the Commercial Law (Art. 62).

At present, the enterprise has ten plants. Of them, five are located in the region of Stara Zagora, one in Haskovo region, two in Kardjali region, and two in Turnovo region. The plants are located in five towns and in two administrative-and-territorial districts, these of Haskovo and Lovech.

For the years since its establishment and till the start of the economic reform in the early 1990s, P-02 has been a monopolist in the production of foodstuff machinery in Bulgaria. Its production was traded in the domestic market, in the CMEA membercountries and in the Third World developing countries from Asia and Africa.

P-02 can be determined as a large enterprise. The active roll numbered 5000 employees by end-1991, 4500 in 1992, and 3385 in 1993. Data for 1994 are incomparable due to the decreased number of plants included in the enterprise. (Till early 1994, P-02 had 12 plants; later, two of them were declared for liquidation, so the total present number is ten).

The volume of sales of P-02 was 233 mln Leva in 1991, 334 mln Leva in 1992, and 382 mln Leva in 1993. The production is oriented for the domestic market and for export.

The status of ownership has not been changed since the transformation of P-02 into a single PLC in 1991. The enterprise is on the initial list of enterprises for mass privatization planned by the Government.

5.2.3. Shocks caused by the economic reform

Since the start of reforms in early 1990s, P-02 has experienced the impact of several main shock, as follows:

1. The collapse of the CMEA market.
2. High interest rates on credits.
3. Higher prices of resource input.
4. Changes in the exchange rate.

This is the way the managers of the enterprise rank the main shocks of the economic

reform. P-02 has large production potential, with long-term assets estimated at more than 1 billion Leva and production capacity to build whole plants for the processing of agricultural raw materials. Till the end of the 1980s, the foreign production orders of the enterprise were provided and secured by governmental agreements. The destabilization of markets in the former socialist countries in the early 1990s and the withdrawal of the state from the economic life made the enterprise face a sharp shortage of outlets for its large production potential. The high interest rates set by the Central Bank are the second shock for the enterprise connected with the long production cycle in machinebuilding and the slow turnover of capital. The higher prices of resource input influence the enterprise through the changes in the exchange rate towards devaluation of the Bulgarian Lev. The sharp devaluation of the Bulgarian currency in 1994 (almost 85% within half an year) entailed an artificial rise in prices of import resources. Although at first glance beneficial for P-02 as an exporter, the movements and sharp fluctuations of the exchange rate act in rather a destabilizing and generally negative way. For example, the artificially maintained "strong" Lev in the beginning of reforms resulted in a cheap export for the enterprise. Managers point to some other developments in the economic environment, too, which have influenced the enterprise, yet with a smaller effect. These include the competition from imports, the decline in domestic demand and the rise in energy prices. The enterprise is no longer a monopolist at the domestic market for the presence of competition (mainly Italian producers).

There are two groups of factors, one impeding and the other favouring the adjustment of P-02 to the new conditions. The first group of factors includes:

- ✓ a deficiency of funds and the subsequent strong dependence on banks;
- ✓ lack of investments in new technologies, higher expenses on resources and labour, with the equipment available;
- ✓ a small number of clients at the domestic market (state-owned canneries which are close to bankruptcy, and small private producers of foodstuffs).
- ✓ The second group of factors favouring the adjustment of the enterprise includes:
- ✓ the monopoly position of P-02 in the main product lines of foodstuff machinery in Bulgaria;
- ✓ the bigger independence in setting prices, in the range of products and markets used;
- ✓ the bigger independence in work force dismissal;
- ✓ the enterprise hadn't been subsidized in the 1980s so it has no problems in adapting to the new subsidy-free conditions.

Managers point out the access to foreign investors and the access to new technologies as favourable factors for the enterprise. On the other hand, opportunities are lacking with regard to the access to new markets and new resources.

5.2.4. Short-term responses of the enterprise

5.2.4.1. Changes in the management

After the transformation of the enterprise into a single PLC in 1991, the governing bodies of the enterprise include the Board of Directors, appointed according to the

Commercial Law by the Minister of Industry with a managerial contract, and the Executive Director, him(her)self appointed by the Board of Directors with a contract of agency.

At the start of reforms, under the strong influence of CL "Podkrepa", a new Board of Directors and a new Executive Director have been appointed to replace the former director who was member of the Communist Party. Recently, another change took place in the Board of Directors, enforced by a decree under which a person may occupy only one place in one board of directors. (The former practice permitted that a person may participate in two or even three different boards of directors in single PLCs). The top management of the enterprise hasn't been changed since the last change mentioned above. The Board of Directors has four members. Of them, one is the Executive Director, the other three are officials in the ministry.

The top managers of P-02 include the Executive Director and two deputies, the sales director and the director of plant operations. The top managers have the following main characteristics:

Executive Director. Engineer, specialty "Electronics". Appointed without a competition, a long-year service at the same enterprise.

Sales Director. Engineer, specialty "Electronics". Appointed without a competition, a long-year service at the enterprise.

Director of plant operations'. Engineer, specialty "Machine-building". Appointed without a competition, with service at the same enterprise.

The predominant part of the directors of plants in the P-02 system are engineers by education. Data collected point to the conclusion that the top managers in the enterprise are mainly engineers, with long-year service at the enterprise and insufficient international experience.

No considerable changes have taken place in the remuneration system of the enterprise. The wage of the executive director is connected by a coefficient to the average gross wage in the enterprise. The remuneration of the members of the Board of Directors are determined as a percentage to the average wage in the enterprise. There is a very low differentiation between the wages of managers and those of other personnel. The wage of the executive director is 3.5 times the average wage and those of the members of the Board of Directors – 1.5 times the average.

The low level of remuneration during the years of reforms resulted in the outflow of high-qualified personnel who finds better paid jobs outside P-02. The shortage is particularly acute in specialists in the R&D department (designers, technologists).

5.2.4.2. Organization and management structures

After the transformation of the enterprise into a single PLC, its plants have lost their legal independence, they don't submit independent balances and have no bank accounts of their own. As a result, the rights and responsibilities of the plants and their relationships are rather unclear.

In the opinion of some of the managers, the profitable plants subsidize the losing ones in the system of P-02, which is a factor non-incentive and inefficient for the

goodworking collectives. On the other hand, according to the executive director, the directors of plants are allowed to sign foreign-trade contracts but it is the management of P-02 who is responsible for their execution and not the plants.

Due to negative financial results in 1994, two plants of P-02 were declared for liquidation. For the time being, this is a kind of a stabilization for P-02 but just a shortterm response to the challenges of adjustment.

The coordination among the plants is executed by a specially formed body called "Board of Directors". It is in charge for the operative management of the enterprise. The directors of the plants and the executive director of the single PLC are members of this body.

A lot of efforts have been directed at improving the marketing activity. A network has been established of representative offices abroad. The marketing department makes specialized studies of the regions the enterprise is interested in.

5.2.4.3. Markets, sales, production

Till the start of reforms in the beginning of 1990s, P-02 was a monopolist in the Bulgarian market and a major exporter in the markets of CMEA and the developing countries. The collapse of the CMEA-market and abolished system of central planning of resources called for the necessity of searching new consumers. The enterprise has partially succeeded in the solution of this difficult task by penetrating in some new markets as South Asia, Nigeria, Argentina. The management made a proposal for P-02 to participate by a certain quota in the intergovernmental agreements with Russia and China, but it was rejected by the Bulgarian government. New customers were created in the domestic market outside the circle of state canneries which suffer a very hard situation. These are mainly small private producers of foodstuffs.

Due to the sharp market destabilization, P-02 was forced to sharply curtail the production and use hardly 30 % of its production capacity. Another response was the drastic reduction in personnel (nearly 1600 people, or 32%, within three years). According to the managers, this resulted in reduced labour expenses per unit of production. A restructuring of production was undertaken in order to meet the specific demands of the domestic market. Small-capacity units were created for the processing of fruits and vegetables.

By rising the producer prices, the enterprise has attained a permanent growth in the volume of sale during the last years.

Another response of P-02 was the selling and leasing of machinery and equipment.

The enterprise has succeeded in finding new suppliers (mainly from abroad) and it is speeding up the negotiations with foreign partners (China, Orenburg, etc.) on the establishment of joint ventures.

P-02 is cutting down the volume of investments and this is one of the main factors hampering the improvement of the quality of production.

In short, the most important steps of the adjustment of P-02 to the reform as seen by the managers, include:

1/ a search for new markets after the collapse of the CMEA;

2/ cooperation with West-European firms producers of foodstuff machinery for the supply of parts and functional units;

3/ a restructuring from large into small production units (small bakeries, dairies, etc.);

4/ shrinkage of credits by demanding bigger advance payments (up to 50%) from the clients.

Since the start of reforms, the most important goal of the enterprise was two-fold: new outlets and survival.

5.2.5. Long-term responses of the enterprise

The main long-term strategic goals of P-02 include the penetration into new markets, the development of new products (for example, machinery for the production of vegetable oil, sesame-paste, etc.), and the maintenance of employment.

For the time being, profit maximization is a missing item on the agenda, as it will make production rather expensive. The more preferable strategy includes low prices and low profitability (from 1% to 5%).

Finding foreign partners is also connected with attaining the long-term goals of the enterprise.

5.2.5.1. Enterprise management. Changes in the pattern of ownership

The managers of the enterprise plan to restructure it into a holding. The former plants will be transformed from units of the single PLC into joint-stock companies. The former management of the enterprise will be transformed into a mother-company.

A project has been developed, connecting the restructuring of P-02 with its privatization. According to it, the formation of a holding will be of benefit to the individual plants in the system of P-02 as it will accumulate funds and make plants independent of banks and bank credits. Besides, a holding is quite attractive from the viewpoint of taxation. Given the possibility that a holding may report smaller profits, or even losses, as a whole, the enterprises with bigger profits will pay smaller taxes. In short, the main purpose of the organizational restructuring of P-02 into a holding is the formation of a common fund of resources to be used for the financing of the individual plants. The holding once established, a state participation in the mother-company and the subsidiaries is envisaged in the project followed by their privatization mainly through manager buy-outs. The privatization process will be initiated by the plants' managers who will form manager teams and offer the following privatization scheme: 51% of assets to the manager team (this share including the privileged ESOP plans) and 49% to the state. With the privatization of all plants concluded, the holding will manage only the state share in the subsidiaries, i.e. the new joint stock companies.

P-02 is on the list of enterprises for mass privatization. The enterprise is subject of diverging interests and different privatization projects. Anyway, it is hard to answer the question of how the privatization scheme suggested by the managers will coincide with the model of mass privatization. At this stage, the response of the managers to eventually

mass privatization will be the attraction of employees to a mass participation in the process.

5.2.5.2. Investments. Changes in the production structure

The export of production is the main opportunity of P-02 to rise the volume of sales. This means an increase of investments in new technologies, yet it is the shortage of funds and the high interests on credits that are stopping the process of capital restructuring.

In the long term, the solution is seen in the creation of joint ventures and a holding structure to accumulate funds. At the start of reforms, the expectations have been directed mainly towards the attraction of foreign investors to participate in the privatization of the enterprise. According to the managers of P-02, however, the would-be foreign partners haven't offered projects of mutual interest. At present, real possibilities are seen in the attraction of local capital. The privatization of present plants, i.e. the stock companies in the future holding, will be financed by means of manager buy-out of the debts of P-02 at a considerable discount. The present discount of the debt-equity swap at P-02 is about 35% and it is an important source of funds for the manager teams in the process of privatization.

5.2.6. Assessment of adjustment measures and perspectives of P-02

Regardless of the hard collapse of markets in the early 1990s, the enterprise has succeeded in adapting to the new conditions, though by a liquidation of two plants and a sharp reduction in production and personnel. As a whole, its survival strategy can be considered a success. According to the managers, a strategy of growth can be developed only after the enterprise is privatized.

It is interesting to analyze the evolution of managers' attitude towards privatization. At the start of reforms, the idea for privatization initiated by the manager team and with the support of employees was considered a good theoretical statement; no practical measures were taken, however. Four years later now, when the enterprise is already on the list of mass privatization, the managers have both the projects and the will to act towards privatization of P-02, yet after its restructuring into a holding. The idea is the same: privatization by a manager initiative. The reasons for the delay and the changes in managers' behaviour are hard to explain. Keeping in mind the existence of powerful private firms in the same sphere of activity, governed by the former communist directors of the enterprise and the presence of government officials in the board of directors with rather doubtful positions, the management of P-02, with its CL "Podkrepa" members, is certain to face a difficult balance of powers in the enterprise. The main problem the managers face since the start of reforms, i.e. about the financing sources of the privatization of P-02 – whether a foreign investor, Bulgarian financial groups, or managers' own and loan capital, is now getting its solution in the later two alternatives.

5.3. Electrical Engineering — A Hesitant Start on the Road of Reforms

5.3.1. General state of the sector

In 1993, the share of electrical engineering and electronics in the total industrial production in Bulgaria amounted to 5.9 percent. The sector employed about 10 % of total

personnel in industry. Being in a deep crisis since the start of reforms in 1990, its production in 1993 decreased by 61.6% the level of 1990. The decline is due to both the collapse of markets in former CMEA-countries and problems connected with the new suppliers of raw materials. (In 1993, the share of material expenses in the enterprises of electrical engineering and electronics amounted to nearly 60% of total expenses).

The last data available give information for the third quarter of 1994. For this period, the decline in production continued, its level falling down by 12% as compared to that in 1993. The average machine loading in the sector as of 1 October 1994 was 52% (51% in 1993).

The market structure of enterprises in electrical engineering is strongly influenced by the liberalization of imports. The existence of foreign competitors, however, proved to be insufficient of the formation of a high-competitive market. There are rather cases of unfair competition instead, as the case study below will show.

5.3.2. Characteristics of P-03

P-03 is a state-owned enterprise in the sector of electrical engineering. It is specialized in the following product groups: street illuminants (46% of sales), industrial illuminants (46% of sales), and transport illuminants (8% of sales).

The enterprise was established by the state in 1956. It was under the supervision of the Ministry of Industry. In 1991, P-03 was transformed into a single public limited company (PLC) under the Commercial Law (Art. 62).

The enterprise has one plant and for the years of its existence has been producing mainly for the domestic market.

P-03 can be determined as a middle-size enterprise. By end-1991, the average roll numbered 506 employees, in 1992-450, and in 1993 their number decreased to 400.

The volume of sales was 40 mln Leva in 1991, 61 mln Leva in 1992, and 78 mln Leva in 1993.

The pattern of ownership hasn't been altered at all and the enterprise is still stateowned.

5.3.3. Shocks of the reform

Since the start of reforms in the beginning of the 1990s, P-03 has experienced the impact of the following shocks:

1. Higher prices of input resources. The greater part of materials used in the production of illuminants come from import. The fluctuations of the exchange rate towards devaluation of the Bulgarian currency result in a rise of prices. The sharp rise in the rate of the USD had a particularly negative effect as it produced an artificial jump of prices and worsened extremely the financial condition of the enterprise.

2. High interest rates on credits. The managers determine them as a scourge for the enterprise. P-03 is forced to use more short-term credits due to the decreased demand in its production and subsequent growth of production in store which entails freezing of financial resources.

3. Unfair competition from imports. This quite a specific shock for the enterprise came on the part of a private Bulgarian-Turkish firm selling low-quality and even hazardous products in the Bulgarian market. Anyway, P-03 lost a lot of its clients. Notwithstanding the fact that the action of unfair competition was proved by the Committee on Competition Protection, the inflicted damages were multiplied in bigger credits, reduction of production and forced leaves. The managers have claimed damages to the private firm in question in order to get some compensations.

4. Liberalization of prices and the rise in energy prices, in particular, which generate inflationary expectations and instability.

5. Changes in employment. The dismissals were particularly shocking at the very start of reforms. In the period of 1990-1993, the number of employees decreased from 1500 to 400, or by more than 70 percent.

Two groups of factors influence the adjustment of P-03 to the new conditions. The first group of factors hampering the process of adjustment includes:

- ✓ unclear ownership rights;
- ✓ unclear responsibilities of the management in the long-term development of the enterprise;
- ✓ shortage of financial resources.
- ✓ This is the way the managers rank the most unfavourable factors. In addition, they mention also the lack of investments in new technologies (a production factor stemming from the deficit of funds), the loss of markets and the higher expenses on input resources.
- ✓ The second group of factors favouring the adjustment of P-03 includes:
- ✓ higher independence in setting prices;
- ✓ higher independence in changing markets;
- ✓ more freedom in the hire and fire of labour force.

According to the managers, the reforms have created very small opportunities for the firm. The access to new markets is hard to achieve while the lack of new resources dooms the enterprise to stagnation..

5.3.4. Short-term responses of the enterprise

5.3.4.1. Under the Commercial Law, P-03 as a single PLC is governed by a management body in the person of the manager of the company. He was appointed at the beginning of reforms; no changes in the managerial personnel have taken place since then.

The manager is an engineer in specialty, with long service at the same enterprise. He was appointed by a competition and on the basis of a contract of agency signed by the Minister of Industry.

The remuneration of the manager follows a system applied to almost all single PLCs in Bulgaria. The manager is rather a member of the personnel than a representative of the owner. His wage is connected to the average gross wage in the enterprise.

5.3.4.2. Organizational structure of management

The enterprise hasn't changed its organizational structure since the start of reforms. After its transformation into a single PLC, the manager became the one and sole body of management of the company. The managers find this structure of management very inefficient.

The estimation of the managers was motivated as not directed against the personality of the manager himself but rather against the provisions in the Commercial Law under which the manager of PLC has very big rights. This is a deviation from the wellknown economic or management councils of the 1980s, with the participation of workers and incompetent party leaders, to a one-man decision-making on the part of managers of newly established public limited companies.

According to the managers, the formation of a management body including the heads of departments of finance, production and trade, and respectively rising their status, may be a solution to this problem.

5.3.4.3. Markets, sales, production

Since the start of reforms in early 1990s, P-03 has undertaken steps on the search for raw materials and development of new products. These efforts, however, haven't proved to be much of a success.

The unfair competition and subsequent loss of clients have caused a reduction in the volume of production. There are some achievements in the diversification and improvement of the quality of products. Sales grow constantly in volume as a result of the rise in prices.

The amount of short-term bank credits is growing, too. To mitigate the hard financial situation, the enterprise is selling machines by auctions.

There is little enthusiasm shown towards negotiations with foreign partners for investments or establishment of joint ventures. Neither the cooperation and assistance of international institutions is searched for the solution of adjustment problems.

The manager of the company is looking for the assistance of the Ministry of Industry mainly.

In short, the short-term strategy of the enterprise includes the maintenance of employment, the development of new products and the penetration on new markets.

5.3.5. Long-term responses of the enterprise

In the long run, the management strategy is directed at investments in new technologies, maintenance of employment and providing of liquidity. The maximization of profits is neither a middle-term nor a long-term priority.

5.3.5.1. Enterprise management. Changes in ownership

According to the managers, the failures in adjustment are mainly due to the unclear ownership rights and the unclear future of the managerial team. The managers, however, haven't undertaken any steps towards privatization of P-03. In addition, the enterprise is missing from the list for mass privatization.

The wait-and-see position of the managers towards privatization is an evidence for the postponed long-term adjustment of P-03.

5.3.5.2. Investments. Changes in the production structure.

The shortage of financial resources, on the one hand, and the necessity of investments in new technologies, on the other, postpone the long-term adjustment of the enterprise.

The unfavourable interest and taxation environment is further worsening the financial condition of P-03, yet the managers are unwilling to search for foreign investors. The development of new products is made by the equipment available.

5.3.6. Estimation of adjustment measures and perspectives of P-03

At present, P-03 is in a very hard situation, yet it is not close to bankruptcy. The later has never been on the agenda of the enterprise, according to the managers. The undertaken steps of adjustment to new suppliers and introduction of new products, however, are only short-term and they cannot solve the problems of the enterprise in the long run.

Ever since the start of reforms, for the coming year and in the middle 3-year term survival is the main goal of the enterprise. Since there are no important positive changes in the enterprise activity, no need occurs for changes in its goals.

The lack of long-term adjustment strategy in the sphere of ownership rights and investments makes the hard process of adaptation to new conditions even longer.

The demand in investments stemming from the specifics of production to adapt to new markets and the lack of reliable investors present insuperable obstacles to the managers.

The existing one-man management pattern (in the institution of the manager) and the old socialist mentality of administrative personnel characterized by negligence and shirking are additional barriers to real manager behaviour.

Given the four factors mentioned above, the efforts and personal qualities of the managers are to a large extent devaluated.

5.4. The Chemical Industry — Expectations for Intervention by the State

5.4.1. General condition of the sector

The pharmaceutical industry in Bulgaria is characterized by the same tendency of decline in production typical for the whole industry since the start of reforms in early 1990s. The production of perfumery and cosmetics in 1992 was 72.9% the level in 1991 and 60.0% the level in 1990. In the production of volatile oils and essences, the fall down was 94.6% and 74.7%, respectively. In 1992, the production of medicines and chemical-and-pharmaceutical preparations, decreased to 76.8% of the volume in 1991. For the period 1990-1993, production of humane antibiotics was down twice and of antipyretics 1.9 times. The only positive trend was witnessed in production of vitamins – a growth of 1.5 times.

The market structure of the sector is represented by several main Bulgarian produces and is characterized by rather oligopolistic competition than a competitive environment.

5.4.2. Characteristics of P-04

P-04 is a state-owned enterprise specialized in the production of three main product groups, namely: pharmaceuticals, perfumery and cosmetics, and volatile oils. In 1994, the product structure included 45% pharmaceuticals, 10% perfumery and cosmetics, and 45% volatile oils.

P-04 is located in a town with traditions in the branch and has been established in the place of former small-size rose-distilleries which existed till 1944. In fact, the enterprise has continued the traditions only in the production of volatile oils. As far as no crafts shops have been located on the territory of the newly built plant in 1945, no former owners exist as under the Law on Restitution. Therefore, the enterprise will be free of answering any claims for property compensations in case it is privatized in future.

The enterprise was transformed into a single public limited company (PLC) in 1991. Under the Commercial Law, the state is the only owner, with a 100% share. At present, it is an one-plant enterprise under the supervision of the Ministry of Industry.

During its existence, the production of P-04 has been directed at the domestic market and the ex-Soviet Union. The enterprise can be determined as a middle-size one. In 1992 and 1993 the average roll numbered 440 employees. There was a considerable reduction in 1994, when 153 people or about 35% of personnel were dismissed.

The volume of sales was 180 mln. Leva in 1992 and 220 mln. Leva in 1993. The products were realized in the domestic market though many of the firms trading in medicines actually export them in the former Soviet countries.

The pattern of ownership of P-04 hasn't been changed in the last years. For the time being, the enterprise is missing from the initially announced list for mass privatization. The managers don't expect it to happen in the near future.

5.4.3. Shocks of the reform

Since the start of reforms in the early 1990s, the enterprise has experienced the following main shocks:

1. The collapse of the CMEA market is the main shock for the enterprise. Till the beginning of 1990s, almost 100% of the exported production was directed at the CMEA countries which provided a very suitable and stable- market. Since then, however, it became harder and harder to win and fill orders at the Russian market, notwithstanding long-established contacts and traditions. For the export of medicines, the Russian partners offer barter which is quite unusual practice for P-04. The so-called 'structures' to be traded in the Russian market and the high degree of risks and instability they generate is another obstacle to the enterprise.

2. High interest rates on credits. Similarly to all other Bulgarian enterprises, their effect on the activity of P-04 is definitely negative. The managers point out that revenues

from sales are enough to cover just interest payments and wages, which, in its turn kills any possibility for investment and capital restructuring.

According to the managers, the weakened control by the Ministry and the higher autonomy of the enterprise since the start of reforms as well as the changes in the conditions of employment related to wages and dismissals haven't the effect of shocks on P-04's activity. The destabilization of the CMEA markets and the Russian market, in particular, is the main shock on the enterprise.

There are two groups of factors influencing the adjustment of P-04 to the new conditions. First, the group of unfavourable factors, including:

- ✓ unclear ownership rights,
- ✓ shortage of financial resources and the stemming barriers to capital restructuring,
- ✓ unclear responsibilities of the management with regard to the future development of the company.

The managers stress on the unclear ownership rights as the main factor hampering the restructuring and adjustment of the enterprise to the new conditions. This entails the unclear responsibilities for the future development of P-04. The attempts to directly connect remuneration in Trade Department to revenues from sales proved to be a failure not only because of the prevailing inclination towards equalization but also for the insufficient economic power of managers to impose their decision and the imaginary owner – the state.

Higher resource expenses, insufficient qualification and the necessity in rising the quality of production are not determined by managers as obstacle-factors to adjustment. Neither is the lack of investments in new technologies.

In short, according to the managers the loss of markets is the main shock and the unclear ownership rights is the main obstacle to the adjustment of the enterprise.

The group of factors favouring the development of P-04 since the start of reforms includes:

- ✓ the access to new markets,
- ✓ higher independence in setting prices,
- ✓ higher independence in changing the production range.

5.4.4. Short-term responses of the enterprise 5.4.4.1. Changes in management

After P-04 was transformed in a single PLC, its management body consisted of a manager and a controller. The controller is an official in the Ministry of Industry. The main characteristics of the top managers of P-04 are the following:

Manager: An engineer, with higher education in chemistry, appointed by a competition, with service at the enterprise before getting the position.

Sales Director: Higher education in economics, with long service at the enterprise.

Director of plant operations: An engineer, with higher education in chemistry, appointed by a competition, with service outside the system of P-04 before getting the new position.

In P-04, there isn't a specially developed system of manager remuneration. Similarly to the rest of personnel, their wages are not connected to profits and differ slightly from the average wage in the enterprise. Attempts were made to connect wages of staff in Trade Department to revenues from sales and profits. The reaction of the rest of personnel was rather hostile, however, and the managers were forced to give up the initiative. This is indicative of the socialism-inherent populationistic attitudes prevailing over economic rationalism.

5.4.4.2. Organization and management structures.

Since the start of reforms in early 1990s, the organization structure of the enterprise hasn't been changed with the exception of an workshop recently closed. As a result, 90 employees were fired. Some other changes in labour organization are connected with re-direction of staff from administrative department to the production shops.

The management structure was changed in the beginning of 1994 when a new member entered the management body, i. e. a controller appointed by the Ministry. His functions in real management are rather unclear, however.

Attempts have been also made to improve the information systems in the main management units, i.e. in trade and marketing and financial department, yet the managers are quite skeptic about the results achieved.

5.4.4.3. Markets, sales, production

Till the start of reforms, the production of P-04 was oriented mainly at the CMEA markets. The collapse of the later had a very unfavourable effect on the enterprise. Its main response during the years of reforms was the search for new customers. In its greater part, these are private Bulgarian firms which buy medicines from P-04 and export them in the Russian and other ex-Soviet markets. The exports are made on barter basis. In this way, P-04 is actually exporting its production abroad though formally selling in the domestic market. Given this and in compliance with state regulation of medicine prices, however, profitability of only 20% is calculated in producer prices of P-04. Any attempts of management to change the situation proved to be a failure. The claims of the enterprise are rejected by the government authorities by stating the necessity in strict state control on medicine prices.

For the time being, the search for outlets in West-European countries is not an item on the agenda. Direct exports to the Russian market (without the mediation of private Bulgarian firms-exporters) are considered nonbeneficial due to risk operations and barter deals.

The shrinkage of market resulted in a reduction of the production of P-04. The decline was especially grave in perfumery and cosmetics, for example, down to about 30 times since the start of reforms.

The main response of the enterprise is expansion of product range through diversification of production. According to managers, the quality of products is preserved while prices are growing continuously. Given the reduced volume of production and diversification of products, in value terms sales have increased in the recent years.

Yet no reduction was achieved in labour expenses per unit of production, and reduction in material and energy expenses was negligible. A retraining of labour force was not undertaken either.

The enterprise is not selling machinery but it is renting some of its stores.

Regarding negotiations with foreign partners, the managers consider their interest towards the enterprise rather 'unserious'. According to the managers, the foreign partners are far from any firm intentions but rather try to take advantage of the present situation.

In short, the main short-term strategies of P-04 include providing of resources, employment maintenance and preventing bankruptcy, which, though not fearing the enterprise directly is still a problem to solve.

5.4.5. Long-term responses of the enterprise

The main strategy of P-04 for the next three years and in the longer run is connected with the development of new products and penetration in new markets. At present, managers consider outlets at the Western markets rather unrealistic a goal to achieve.

5.4.5.1. Enterprise management. Changes in the ownership pattern.

According to the managers, the unclear ownership rights and unclear responsibilities with regard to the long-term development of the enterprise are the main obstacles to its adjustment to the new environment. Perhaps this is one of the reasons for the lack of clear-cut concepts on the future management structures. It makes no sense to develop strategies for the enterprise when other economic agents (a ministry, financial groups, etc.) make the decisions on its future.

There is a contradiction between the clear stand of managers on the issue of ownership rights and their attitude towards privatization. At present, the enterprise is missing from the list for mass privatization. It is on the list of enterprises to be financially recovered by the state. The managers are not quite sure, however, what do these measures of financial recovery actually mean.

5.4.5.2. Investments. Changes in the production structure.

Investments in new technologies are considered unnecessary at the present stage. The main goal is to use and eventually further expand the existing production capacities.

The rather conservative stand of managers towards investments is determined by their unclear responsibilities with view to the long-term development of P-04. For the time being and in the near future the expansion of product range within existing capacities is the main goal of the management.

5.4.6. Assessment of adjustment measures and perspectives of P-04

Since the start of reforms, P-04 has been transformed into a 100-percent stateowned limited liability company, with a manager and a controller as management bodies.

However, the remuneration of managers is still unchanged and the new form of organization doesn't differ considerably from the former one.

The attempts of managers to introduce a higher differentiation in remuneration proved to be a failure because of the strong resistance of the equalization-inclined workers' collective. "A lot of efforts and no reward as a result", to cite one of the managers.

The most important goal of the enterprise is its survival. The management is directed at a short-term adaptation to the new environment.

It is really a paradox that though managers consider unclear ownership rights the major reason behind the need of adaptation, they are afraid of any own initiative towards privatization and direct their efforts at solving only current problems. Such kind of managerial behaviour is sure to prolong the existence on the edge of survival. On the other hand, keeping in mind the strong influence exerted by economic agents like the branch ministry, financial groups, etc., the development of P-04 in the near future is hard to predict.

5.5. Textile — A Break-Through in the International Market

5.5.1. General condition of the sector

In 1993, the textile and knitwear industry produced 4% of total industrial production and employed about 7.5% of industrial personnel in Bulgaria. Since the start of reforms, the sector fell in a crisis caused mainly by the collapse of CMEA markets, unfair competition from imports and changes in the macroeconomic environment connected with high interest rates on credits and unfavourable exchange rates. Compared to 1990, the volume of production in 1993 decreased by 46.2 percent. The decline in production was gradually overcome, however, down to 11% in 1993 against 1992, and 7% in the three quarters of 1994 against 1993 same period.

The production of woolen cloth and yarn is showing a trend of declining rate of decrease. There is a great number of producers in the Bulgarian market, the half of them from abroad. The enterprise under study is one of the biggest producers of woolen cloth and yarn in Bulgaria. It holds 40% of the woolen yarn and 25% of the worsted cloth market. Notwithstanding the presence of a lot of contractors since the start of reforms in early 1990s, the market structure is inefficiently competitive due mainly to unfair competition from imports.

5.5.2. Characteristics of P-05

P-05 is an enterprise in the textile branch. Its main product groups in 1994 included cloth (95% of sales) and yarn (5% of sales).

The enterprise was established in the place of a private factory nationalized in 1947. A general reconstruction took place in the 1960s. The enterprise is under the supervision of the Ministry of Industry. In 1991, it was transformed into a single public limited company (PLC) as under the Commercial Law.

At present, the enterprise has one plant. For the years of operation, P-05 was selling

its production mainly in the domestic and ex-CMEA markets.

With nearly 2000 employees in 1994, P-05 belongs to the group of large enterprises.

The enterprise is on the list for mass privatization. The Ministry of Industry has made the decision without consulting the managers. As a result, they are not only rather displeased to know the fact but also fear a probable destroying of an enterprise built in the course of many years.

5.5.3. Shocks of the reform

Since the start of reforms, P-05 has faced two main shocks: first, the collapse of the CMEA market, and second, the high interest rates on credits. They, however, have not effected the enterprise in the way some other sectors, like machine-building for instance, suffered it. The reason behind is the specific place and role of textile and woolen textile, in particular, which has a wide network of consumers producing clothing.

The branch peculiarity of textile mitigates the unfavourable changes in the economic environment influencing P-05. The competition from imports and mainly that of low quality goods imported from Turkey is not of considerable importance to the enterprise. The domestic demand in woolen cloth, mainly on the part of small firms, has also decreased; still, it is not a shock for the enterprise.

To a certain extent, problems have arisen related to the supply of raw materials, wool and polyester, yet with insignificant effects on P-05. The rise in energy prices is another burden the enterprise manages to bear so far.

The devaluation of Bulgarian currency in the recent years has had a favourable effect on P-05 as it is constantly expanding its orientation abroad, thus rising the prices of its production. As a whole the movement in the exchange rate is a positive factor for the enterprise.

It the course of adjustment to new conditions P-05 has faced the influence of two types of factors, i.e. impeding and favouring its efficient behaviour. According to the managers, the first group includes:

- ✓ the big scale and respectively large enterprise capacities for cloth production, with long production cycle, which is not suitable for volumes exceeding certain level, while the free market economy in Europe is more flexible and P-05 has difficulties in meeting its requirements;
- ✓ the higher labour expenses due to surplus labour force employed and, on the other hand, the lack of key knowledge, qualification and inclination to work in a market environment where the customer is the determinant;
- ✓ the insufficient quality level of production which hampers the invasion in new market niches;
- ✓ the higher expenses on raw materials imported at international prices.

The lack of financial resources, the unclear responsibilities of management with regard to the future development of the company and the unclear ownership rights, however, are not mentioned as factors limiting the process of adjustment.

The second group of factors favouring the company's adjustment includes the following:

- ✓ access to new markets stimulating the development of new skills of personnel and market orientation in improving the quality of production;
- ✓ access to new resources;
- ✓ bigger independence in setting prices and determining the sort of cloth produced;
- ✓ higher level of qualification and skills of new-coming employees.

The difficulties connected with the increased requirements of new West European customers to the quality and assortment of products have a surprisingly positive effect on the personnel. The production is connected with certain customers and certain orders and this, according to managers, is the main factor for the changes in the socialist-type mentality of workers to produce independently of market demands.

However, P-05 is still missing another favourable factor, i.e. the access to foreign investments.

5.5.4. Short-term responses of the enterprise 5.5.4.1. Changes in the management

After the transformation into a single PLC in 1991, P-05 has been managed by the Board of Directors and the Executive Director. The members of these bodies were entirely changed in 1992 under the pressure of CL "Podkrepa". The new-appointed executive director formed a new management team. Since then, the management of the company remained unchanged.

Unlike other enterprises where "Podkrepa"-dictated staff changes have proved to be rather inappropriate or purely cosmetic, the new director of P-05 has manifested competence and activity and has made a very proper choice of managerial staff with marketoriented behaviour.

Main characteristics of the top managers of P-05:

Executive Director. An engineer, appointed by a competition, with very rich experience within the same enterprise.

Director of Market Policy Department', a Specialist with two university degrees, in economics and philology, with rich international experience. Previous service – outside the system of the enterprise.

Director of Plant Operations: An engineer, appointed by a competition, with long service at the same enterprise.

Director of Marketing and Development Department: An engineer, appointed by a competition, with long service at the same enterprise.

Chief Expert at Economic Department'. A specialist with higher education in economics, with long service at the enterprise, dealing in the problems of finance and personnel.

The enterprise hasn't developed a special top manager remuneration system. The remuneration of the members of the Board of Directors was 1.6 times the average gross wage in the enterprise in 1993; the same level was maintained in 1994, too. For the periods in consideration, the remuneration of the Executive Director was 2.1 times the average gross wage. The conclusion is, therefore, that the remuneration of managers differs very slightly from that of personnel as a whole.

5.5.4.2. Organization and management structure

Under the initiative of the Executive Director, an operative bureau has been formed for the day-to-day management of P-05, including the executive director and the deputy-directors of departments. Apart from traditional departments on finance and production, two new management units have been formed, i.e. on market policy and on marketing and development. The later are in compliance with the main efforts of the management directed at the investigation, penetration and holding of new markets.

Problems and contradictions still arise, however, between the units of management as they work in different worlds, to cite one of the managers. Managers dealing in market policy try to implement the style and requirements of the West European and American markets; at the same time, however, the managers in the production department face the former mentality and socialist-type attitude towards work with minimum efforts and regardless of customer requirements. In order to change the situation, the managers see a great potential in the development of a remuneration system stimulating the whole personnel towards working on orders from West European and American customers.

5.5.4.3. Markets, sales, production

The start of reforms and the collapse of the CMEA markets have brought about a decline in production. The response of the management units on marketing, development and market policy was the search for new customers in Western Europe. Their efforts proved to be a success.

At present, the volume of production is growing. What is more, in summer 1994 the demand exceeded the supply of products of P-05.

Production has been diversified as a result of own design projects and orders from abroad. The requirements of the new customers have made for the improvement of quality of production. There is a slight rise in prices as well.

Finding new suppliers from abroad is another specific response of the enterprise. Attempts have been also made to find foreign partners for joint ventures, yet without any particular results.

There is no reduction in the expenses on labour, raw materials and energy. Machinery is not sold, facilities and equipment are not rented either.

The enterprise hasn't increased its debt to banks but hasn't made new investment either thus relying only on the efficient use of production capacities available.

In short, P-05 has created a network of customers in the new markets thus providing export opportunities for 80% of its production and, on the other hand, importing 20% of its raw materials. The entry and holding of new markets means a lot of efforts and struggle for the improvement of quality which, in its essence, means a struggle against old socialist attitude towards labour, neglecting of customer requirements and shirking from work.

5.5.5. Long-term responses of the enterprise

Asked about the long-term strategy of P-05 and even within the mid-term of three years, one of the managers gave the following question-reply: "Who knows in this country?". This skepticism of managers is easy to understand under present conditions of high instability and changeability of the environment. A very recent example of that was the news that P-05 was entered into the list of enterprises for mass privatization.

Though not in the long term, managers define as permanent strategies of the company the following ones: new market entries, development of new products, increase of the market share.

Establishing contacts with new foreign partners is another strategic goal. The aim is cooperation and selling the enterprise production abroad.

Maintenance of employment is a strategic goal, too, meaning a maximal utilization of working time and growth of production with the same number of personnel employed. According to an expert manager assessment, this will be a tedious process.

5.5.5.1. Enterprise management. Changes in ownership.

At present, P-05 is a profitable enterprise. The managers estimate this result as to a great extent owing to their efforts both under the Ministry's withdrawal from the management of state property and in the lack of investments. On the other hand, the relaxed ministerial supervision, the bigger autonomy of the enterprise and the unclear ownership rights are not considered factors impeding the adjustment of P-05 to new conditions. On the contrary, manager actions and behaviour prove to be quite successful under the existing pattern of ownership rights.

Given the short-term adjustment of the enterprise, its privatization is an issue of rather odd manager attitude. Stressing on enormous efforts made in the most difficult times and the success and stabilization achieved in coping with new challenges, the managers are rather suspicious about present plans and appetites from outside, which can easily spoil the fruits of their hard work. These fears are further nourished by the mysterious way P-05 entered the list of enterprises for mass privatization, without any preliminary consultations with the management. The mass privatization scheme is therefore suspected to serve interests rather opposite to those of managers and personnel. Now, the Executive Director has to find a solution to the problem by an alternative project promoting a more active managers' participation in the future management and ownership structure of the enterprise.

5.5.5.2. Investments. Changes in the production structure.

With no investments made since the start of reforms, possibilities are now searched for investments in new technologies. A new workshop has been built equipped with old machinery. The problems of restructuring in compliance with customer requirements are solved within the existing equipment, both outdated and modern. Nevertheless, new investment is not a permanent strategy of the enterprise. According to the managers, the market positions of P-05 in the near future will be maintained on the basis of present equipment and by putting in operation non-utilized reserves.

5.5.6. Estimation of adjustment measures and perspectives of P-05

For the three years of its functioning, the new management of P-05 has succeeded in stabilizing the enterprise and finding new outlets in Western Europe. At present, P-05 is a profitable enterprise with good prospects to hold the market positions it has won and for its personnel to adapt to the requirements of West European market economy.

Thanks to their managerial skills and high creative potential, the new managers have achieved considerable results in coping with new environment, without privatization and changes in the ownership pattern.

Given this, the suggested scheme of mass privatization looks rather intrusive and the managers question the need in privatization. Moreover, they have developed their own privatization project envisaging a wide manager and personnel participation which, obviously, contradicts certain group interests.

It can be concluded, therefore, that the passive managers' behaviour towards privatization and, on the other hand, their high activity in adapting to the requirements of market economy, proved to be a disadvantage in the new conditions. The underestimation of the issue of ownership rights, which seems even non-existent in a single PLC, has suddenly come to the surface and turned into the major problem asking for very quick manager initiatives towards privatization.

5.6. Tailoring Industry — A Day-to-Day Management without Manager Strategies

5.6.1. General state of the sector

In 1993, the share of textile and knitwear industry amounted to 4% of total industrial production in Bulgaria. The sector employed about 7.5% of industrial personnel. Since the start of reforms, the sector fell in a crisis resulting from the collapse of CMEA markets, unfair competition and changes in the macroeconomic environment connected with high interest rates on credits and unfavourable exchange rate of the Bulgarian currency. Compared to 1990, the volume of production in 1993 decreased by 46.2 percent. The decline is however gradually overcome, down to 11% in 1993 compared to 1992, and further to 7% in Q3 of 1994 as compared to Q3 of 1993.

5.6.2. Characteristics of P-06

P-06 is a state-owned enterprise in the knitwear branch of light industry. It is specialized in two product groups: knitwear, including outer clothes and underwear, and tailor's goods such as training suits, dressing gowns, sportswear, etc.

The company has six shops. Of them, four are located in the production site in the town of Stara Zagora, including a knitting shop, a finish shop, and two shops for readymade clothing. The remaining two are also ready-made clothing shops, one located in the town of Radnevo and the other in the village of Glavan.

P-06 is a middle-size enterprise. The average payroll numbered 1032 employees as of December 31, 1990; their number then decreased to 847 in 1991, and further to 788 in 1992.

In value terms, the volume of sales was 25,938 thousand Leva in 1990, 73,548 thousand Leva in 1991, and 98,991 thousand Leva in 1992. The growth in sales' volume in the studied period was due to the rise in prices, though considerable reduction in production.

P-06 was established as a state-owned company under the Law on Nationalization of December 23, 1947 on the basis of formerly existing dye-house. Since then, it was under the supervision of the Ministry responsible for light industry. At present, this is the Ministry of Industry.

On October 4, 1991 the company was transformed into a single public limited company (PLC) with 100-percent state capital.

The pattern of ownership has not been changed recently. The company is not on the initial list of enterprises to be privatized. Claims have been announced by former owners of the nationalized factory to participate in the privatization of the company. Managers have no clear idea about the privatization scheme that should be applied. They rather fear an immediate dismissal provided the former owners acquire property rights over the enterprise.

5.6.3. Shocks caused by the reforms

Since the start of reforms in early 1990s, the rise in interest rates has been the greatest shock to the company. In 1987 P-06 took a loan of 5 mln Leva to cover the construction of new facilities. The drastic rise in interest rates since early 1990s has made the company re-direct its profits at covering interest payments on former loans as well as on turnover credits for the normal course of production.

Liberalization of prices is another significant negative factor. The rise in raw material and fuel prices resulted in a sharp growth of product costs, which, in its turn makes produced goods hard to sell.

The collapse of the distribution system is yet another shock to the company. The liquidation of whole-sale trade enterprises has destroyed the connections of the company with its customers. Production thus remains beyond consumers' reach. Small-sized trading firms have recently emerged, yet their orders cannot cover the production capacity of the enterprise.

The competition from imports is also an important shock to the company. These are mainly goods from Turkey and China, which are inferior in quality as compared to P06 products but are offered at lower prices. According to the managers, this is unfair competition as these goods are of rather doubtful origin (illegally imported) and therefore with non-paid customs duties. On the other hand, they are distributed mainly by small private firms which often fail to strictly fulfill their obligations towards taxation authorities, social security payments, etc.

The shocks to P-06 can be ranked as follows:

1. High interest rates
2. Price liberalization
3. Collapse of the distribution system
4. Decline in domestic demand
5. Competition from imports (Turkey and China mainly)

5. Competition from imports.

Managers do not consider the changes in ownership rights (relaxed ministerial control, changes in ownership, higher degree of autonomy, changes in the management) a considerable shock to the enterprise. The same applies to changes in the terms of employment, including remuneration, benefits, or dismissals.

Changes in the economic environment engender a lot of problems to P-06. The major of them are connected with higher expenses on resources and capital equipment.

The expenses on dyes, mazut and water have resulted in a sharp rise of the production costs. As far as fixed assets are concerned, the main problem is connected with the possibilities for their renewal given the high interest rates on credits.

Next to mention are the second-class problems stemming, to a certain degree, from the first group of problems. These include the need in changing the information system and especially that in the sphere of marketing, the loss of markets which is considered a consequence of high production costs and subsequent fall in orders, etc.

The shocks and difficulties faced by P-06 provoke relevant responses of the company so as to adjust to new conditions.

One of the measures is connected with the development of new assortment policy based on new collections and designer projects.

Another measure is connected with a policy aiming the reduction of production costs. In practice, this means economizing of raw materials, fuels and energy spent which count for about 70% of production costs.

Last but not least to mention is the creation of a distribution system, and finding whole-sale distributors in particular..

What are the opportunities for the company that have emerged since the start of reforms in early 1990s? Managers estimate them as rather small.

Among more significant opportunities managers point to the greater independence in setting prices and changing the range of production. Access to new markets is considered just a potential factor; for the time being there is only a process of searching yet without concrete results achieved.

Access to new investors is not mentioned among the favourable factors. The higher independence in making investment decisions is determined as a theoretical possibility which is hard to turn into reality due to the shortage of financial resources.

The bigger independence in the hire and fire of labour is considered a factor quite insignificant and non-decisive for company's adjustment to the new conditions.

5.6.4. Short-term responses of the enterprise

5.6.4.1. Changes in management

The managers have developed both an organizational and management structure of the company.

Under the Commercial Law, the company has one-tier system of management, with the Board of Directors being the management body. The members of the Board have been appointed by an order of the Minister of Industry and related contracts of agency

concluded between the Minister, on the one side, and each of the members – on the other. The competences of the members of the Board of Directors are regulated by the relevant provisions of the Commercial Law. The members of the Board have not been changed since appointment.

The management structure of the company includes an executive director and director of plant operations. There are no directors in finances and in marketing.

The present executive director has a university degree, specialty textile engineering, and has graduated from the Higher Machine and Electrotechnical Institute in Sofia. He has a long non-interrupted service with the company and has passed through all stages of hierarchy to reach the post of the executive director.

The director of plant operation is a textile engineer, too, and has graduated from the same higher institute. He has a 20-year service with the company. He was appointed to the present position without a competition.

The Board of Directors has four members. Of them, one is the executive director of the company. The other three work with different institutions as the Ministry of Industry, the Committee on Quality, a commercial bank.

No changes have taken place on managerial level recently.

Remuneration of managerial staff is determined under the provisions of Decree 265 of the Council of Ministers of December 28, 1992. The salary of the executive director is 350% the average gross wage in the company. The director of plant operations gets 150% that sum, and the members of the Board of Directors 130% respectively. The salaries of managerial staff depend on the profitability of the enterprise. For example, a rise or fall of 1% in quarterly profitability as compared to figures in the previous quarter generates a rise, or respectively fall of 10% in managerial staff salaries.

5.6.4.2. Organizational and management structure

P-06 has undertaken steps to answer the challenges of new economic environment, the main of them being the following:

First, reorganization of the company. P-06 has implemented a new management structure, with two director positions, i.e. an executive director and director of plant operations. There are five main departments: economic and legal-and-administrative, financial, technical, marketing, and trade and design.

Second, improvement of information systems and computerization of accounting in particular, which is under implementation.

Third, intensification of negotiations with foreign partners for the establishment of joint ventures, without particular results yet achieved.

5.6.4.3. Markets, sales, production

Another response of the company was related to reduction of material expenses, determined by managers as a policy of 'squeezing out resources'.

The next step was the reduction of the physical volume of production. There is an increase of production in value terms due to the rise in prices; it should be mentioned, however, that the company applies a minimum rate of profitability, i.e. about 5% so as to make its products sellable.

The company has not applied for getting subsidies, neither before nor in the course of reforms.

Managers find it difficult to range the responses according to their significance to the company. Though rather conditionally, managers point to management structure reorganization and improvement of the information system as the main responses of P-06. The main limiting factor faced by the responses of the company is the shortage of funds.

Managers give a negative answer to the question of whether the company has asked for some specialized assistance in solving its adjustment problems. This applies to both domestic and international sources. The only assistance asked from the Ministry of Industry was related to the transformation of company's capital investment credits into state debt.

5.6.5. Long-term responses of the enterprise

Since the start of reforms, survival has been the main goal of the company. This applied especially to maintaining the number of staff and preserving the funds available. It was to a certain extent successfully achieved since the reduction in personnel resulted only from retirement or free-will resignation and not dismissals. Production machinery and equipment was also preserved and the need in partial selling had been avoided. Yet, the degree of depreciation is more than 90 percent.

Keeping the present situation is the main goal for the coming year. Production capacities are not fully loaded, the enterprise applies one-shift instead of three-shift scheme of working. Loading of existing capacities is the target of the company in the short run. Growth and restructuring is the main goal of the company in the next three-year period. The search for new markets will be a priority yet with a higher volume of production.

The short-term one-year strategy of the company is connected with the maintenance of employment level. Next in priority come the penetration into new markets, the development of new products and the expansion of market share.

The long-term three-year strategy of P-06 envisages the penetration into new markets and the finding of foreign partners.

Profit maximization is not considered a strategic goal in the near future.

5.6.5.1. Enterprise management. Changes in ownership.

The problem of ownership structure hasn't been openly stated by the managers. According to them, the changes in ownership rights, i.e. relaxed ministerial control, changes in management, etc. which were undertaken following the start of reforms in early 1990s had no shocking effects on the enterprise.

On the one hand, managers have no clear-cut views on privatization as a form of ownership restructuring. On the other hand, however, privatization is considered a danger for their director positions. This unannounced fear explains the underestimation of ownership rights by managers in their interpretations of company's behaviour since the start of reforms.

The main shocks to the company are related to the changes in macroeconomic environment, i.e. interest rates, prices, collapse of wholesale trade, competition from imports, low solvent demand in the domestic market. The main problems are high production costs and old equipment. The main limiting factor is the shortage of financial resources and not unclear ownership rights. The present and planned future responses of the company are not related to privatization but rather to management restructuring, reduction of expenses and negotiations with foreign partners, yet customers not investors.

Apart from managers' fear from privatization, there are some other factors determining the place of the issue of ownership rights.

5.6.5.2. Investments. Changes in the production structure.

At present, no investments in new technologies are planned. The fuller loading of existing capacities and the expansion of product range are considered priorities for the time being.

5.6.6. Estimation of adjustment measures and perspectives

P-06 is a single PLC with the government, the Board of Directors and the managers being its main economic agents. In the structure of ownership, the residual risk is carried out by the owner of assets, i.e. the government (state officials) and the management function is carried by the managers under the supervision of the Board of Directors.

Since the start of reforms in early 1990s, the risk of shocks on P-06 should be met by the owner, i.e. the government. Actually, however, the state officials transfer all responsibilities regarding the transition to the new economic system to the enterprise. The latter is given the so-called autonomy, i.e. a hypothetical ability to independently determine products, investments and markets. This is a pseudo-autonomy, however, because: first, the state continues to fully possess the assets, while the company carries the risks of the reforms; second, the state does not perform regulation, and therefore a normal economic environment is not created for the functioning of the company.

The state is failing to efficiently fulfill both its role of owner of the assets and its functions on regulating the economic environment. The problem is more complicated as it concerns not only the structure of ownership rights in the company. At this initial stage of transition, the role of the state in economic life as a whole is far more important than its owner's rights.

Since the start of reforms P-06 has faced the following main shocks, namely: interest rates, price liberalization, commercial network collapse, and imports competition. From the viewpoint of the two functions of the government as owner and regulator, two types of attitudes emerge on the part of the company, i.e. to the owner of its assets and to the regulator of its activity in the entire economic system. In this sense, the residual risk of different types of shocks should be distributed between the company and the government. From the viewpoint of economic rationality, for example, the company is overloaded with the burden of high interest rates while these should be met by the owner, i.e. the state.

Liberalization of prices and the collapse of wholesale trade network are shocks which the company cannot neutralize by its own efforts. While the creation of a new distribution network can to a certain extent result from greater managers' activity and initiative, the burden of higher prices of raw materials is transferred to the customers and the company operates at minimum rate of profitability.

This, however, is a short-term adjustment. It cannot provide the financial resources necessary for capital restructuring and production expansion which are of key importance for the survival of the company in the emerging market environment.

The shock stemming from unfair imports competition is the most severe one to the company. The irrational and rather irresponsible behaviour of the government in state regulation puts P-06 in unequal positions as compared to private firms-importers.

The latter prove to be more flexible in applying the laws on taxation, customs duties, and social insurance thus reducing their expenses and respectively the prices of goods offered in the market which finally means unfair competition for P-06 and subsequent loss of customers.

Actually, and this is a partial conclusion of the analysis, the present state regulation acts against P-06 as a state-owned enterprise and in favour of the private business in the branch considered.

The long-term strategy of P-06 includes the search for new outlets and the finding of foreign partners-customers. Growth is the priority goal for the next three-year period. How can this be achieved without ownership restructuring, i.e. privatization?

For the time being, managers follow the wait-and-see position, they have no plans for privatization nor seem to be inclined to initiate it under Art. 4 of the Law on privatization and restructuring of state-owned and municipal enterprises.

Given the inefficient behaviour of the government in the field of state regulation, they focus mainly on the problems of the macroeconomic framework. Provided active state protectionism of light industry is applied or equal conditions are at least guaranteed for the operation of the state and the private sector, the greater part of problems of P-06 connected with unfair competition will disappear. Similarly, if loans for capital investments are transformed into state debt, the burden of credit and interest servicing will disappear and funds will be provided for the renewal of equipment.

These, however, are merely manager expectations and hopes for a more efficient behaviour on the part of government as both regulator of economic processes and owner of company's assets. In the new conditions and with former state ownership structure preserved, managers will keep on searching customers and loading the existing capacities so as to secure the fulfillment of their one-year strategy, i.e. the maintenance of present number of personnel.

In the long run, however, growth in production is impossible to attain without capital restructuring and renewal of equipment, i.e. without fresh investments. To this end, funds can be attracted through loans and therefore privatization of assets is not absolutely indispensable.

Evidently, managers are rather inclined to follow such a way of solving the company's problems. Provided the state behaves as a rational economic agent and the company succeeds in finding markets for its production with the existing ownership

pattern, it can adapt to new conditions without necessarily restructuring the ownership. The first condition is rather improbable to accomplish.

As far as the second is concerned, it can be attained, yet the problem will sooner or later arise about the quality of products, high production costs, worn-out equipment and, finally, about the efficiency of management. For the problem of company's adjustment is not privatization as a change of nominal owner but rather the efficient manager behaviour.

Which are the mechanisms that can make managers behave efficiently? At P-06, there is a conflict between the single-person shareholder, i.e. the government, and the managers of the company. In the case of P-06, incentive mechanisms which operate in mixed economies and make managers work efficiently are either applied in a very peculiar way, or do not exist at all.

The institutions of the capital market, the manager labour market, and the corporate control market have insignificant effect on manager behaviour and on limiting manager obstruction, in particular. The potential control mechanisms, therefore, remain concentration of ownership in the single-person owner, manager participation in ownership, the board of directors, and the manager compensations package.

Up to now, the single-person owner, i.e. the government has obviously manifested a very irrational behaviour by transferring to the company all the risks of on-going reforms. In the case of P-06, it is the very owner who behaves in a opportunistic manner regarding capital utilization. It is yet another illusion to expect, however, that other economic agents, e.g. tradeunions, etc. will be able to more efficiently control the managers of the company.

As far P-06 is a single PLC, the managers cannot participate in ownership. The Law provides no preferential conditions for manager participation in the privatization of the company. Privatization through competition is a hypothetical possibility under which the managers who are best acquainted with the situation of the enterprise can have some relative advantages. Anyway, this opportunity was not mentioned as a probable privatization scheme.

The Board of Directors is the institution to protect the interests of the owner, i.e. the state, in P-06. With the irrational behaviour of the owner and the wait-and-see position of the managers, the Board has a rather strange role to play. As a result, it is quite inactive in the adjustment measures of the company.

Manager compensations adopted by Decree 265 of the Council of Ministers of Dec. 28, 1992 are directed at connecting manager remuneration with company profitability. At present, it is only the remuneration of the executive director which is relatively higher than the average in P-06. Anyway, there are no other incentives applied. Given the general high level of unemployment and difficulties in establishing private business in the region, in this case the provisions of Decree 265 are related rather to a "satisfactory" level of remuneration of managers than to a more efficient use of capital.

With all the specific mechanisms of manager control mentioned above, the managers of P-06 behave in a rather peculiar way. Though the issues of new markets and capital renewal are of key importance, there is no policy of active marketing pursued nor a marketing for potential investors. Capital attraction is not put to the floor either. This is

easy to understand as a would-be new investor can bring new requirements and regulations of management and work. Here interests of managers and workers coincide totally. That is why the main strategy of P-06 at the present stage is preserving the number of personnel employed. In their behaviour, managers are guided rather by the idea to preserve the labour force and their own governing positions than by a more aggressive management strategy aiming an independent solution of problems and attraction of new efficient owners.

5.7. Foodstuffs Industry — A Stable Branch Position

5.7.1. General state of the sector

Foodstuffs industry is ranked second in importance in the structure of Bulgarian industrial production. In 1993, its share was 21.6% against 21.9% of the chemical and oil-processing industry, and it employed 12% of total industrial personnel.

Compared to 1990, the decline in production in 1993 was about 45 percent. The last data available relate to the third quarter of 1994 and point to a decline of 10% as compared to 1993 same period. Regardless of general trend of decline, some of the enterprises in the branch reported positive results. Out of one hundred enterprises which accounted for 73% of industrial revenues in Q3-1994, 24 operated in the foodstuffs industry.

The enterprise under study is in the milling branch. As a whole, the branch is characterized by a decline. The statistical data, however, are not precise as far as information collected excludes production with raw materials of clients. There are several large producers in the market, yet the latter is segmented by regions and competition is therefore oligopolistic rather.

5.7.2. Characteristics of P-07

P-07 is a state-owned enterprise in the foodstuffs branch. In 1994, its production structure included flour (80% of sales) and bran (20% of sales).

P-07 was established as a state-owned enterprise in 1962. Since then, it has been under the supervision of the Ministry of Agriculture. The enterprise was transformed into a single public limited company on September 1, 1991. At present, it consists of two units: a flour-mill in the town of X. and a flour-mill in the town of L.

The production of P-07 is oriented at the domestic market. It is among the five biggest producers in the branch and occupies a 25-percent share of the regional market.

P-07 can be classified as a middle-size enterprise. Its average payroll numbered 114 employees as of 31 December 1992 and 120 employees by end- 1993. This number remained stable during 1994.

The volume of sales was 101476 thous. Leva in 1992 and 125911 thous. Leva in 1993. The total volume of production was sold in the domestic market.

Since 1991, no changes have taken place in the pattern of ownership. At present, the enterprise is on the initial list for mass privatization. Managers have not been consulted

prior to this decision and have completely negative attitude towards this scheme of 'offered from top' mass privatization.

5.7.3. Shocks caused by the reform.

Since the start of economic reforms in early 1990s, the following changes have caused the most severe shock to P-07, namely:

1. High interest rates on credits. The basic interest rate of Bulgarian National Bank has been continuously growing in the period 1990-1994 to reach the level of 72% (September 1994). Due to seasonality in raw material supplies, and wheat in particular, P-07 has increased the amount of short-term credits. To this, two main reasons should be mentioned:

- ✓ first, the seasonal irregularity in wheat supplies;
- ✓ second, the maintenance of excessive grain reserves due to high inflationary expectations.

2. A speedy rise in raw material and energy prices. This is a factor destroying the stable operation of the enterprise and making managers feel insecure.

3. A downfall in domestic demand. The constant rise in prices of P-07 products since the start of reforms has brought about a shrinkage in domestic demand

Managers do not point to other changes in the economic environment as having shock effects on the enterprise. The factor of subsidies, for example, has never existed for P-07. The changes in the terms of employment (new wages, benefits, dismissals) are not of considerable importance. Neither have the changes in ownership rights (relaxed ministerial control and higher autonomy of the enterprise) effected to a great extent the situation of the enterprise. On the contrary, managers consider present freedom of action a factor favouring its more efficient adjustment. There are two groups of factors influencing the adjustment of P-07 to new conditions. The first of them are these hampering the adjustment, namely:

- ✓ shortage of financial resources;
- ✓ non-guaranteed raw materials supply, including low quality of wheat;
- ✓ higher expenses on raw materials.

Managers are optimistic with regard to capital equipment available, the quality of production, and the loss of markets. In their opinion, the enterprise has outlets for its production.

The second group of factors favouring the adjustment of P-07 to the new environment includes:

- ✓ access to new markets (mainly in other regions of the country);
- ✓ access to new resources (new domestic suppliers of grain).

However, the access to foreign investors is missing from optimistic manager estimations. The same applies, however, to the higher independence in setting prices. The government has fixed a 12-percent rate of rentability in setting prices on flour, which is a limiting factor according to the managers.

5.7.4. Short-term responses of the enterprise

5.7.4.1. Changes in the management

Under the Commercial Law, after its transformation into a single PLC P-07 is governed by a manager. The present manager has been appointed without a competition. In fact, this is the former director of the enterprise. He has worked at the enterprise for long years and has never had considerable contradictions with trade-unions.

P-07 has no director of finance and a sales director. These two departments are headed by chief experts. Both of them have long service at the enterprise and have been appointed without competition.

The relatively simplified top-management structure of P-07 corresponds to its size. Given the lack of considerable difficulties connected with outlets, an intensification of marketing activities is not indispensable. The maintenance of employment level, regular wage payments and relatively small in number personnel stabilize the position of the manager. Interests of managers coincide with those of the employees. Managers share the idea of initial privatization of P-07 through transfer of ownership rights to the personnel.

P-07 hasn't developed a special system of remuneration of the managerial staff. The wage of the manager is connected to the average gross wage in the enterprise. In 1994, it was 2.8 times the average level. The relatively low nominal level and slight differentiation in manager wages do not create incentives for more active adjustment to new environment.

5.7.4.2. Organization and management structures

Since the start of reforms, no changes have been undertaken in the organization structure of P-07. There was only an expansion of production capacities by the construction of a new flour-mill.

The management structure has not been changed, too, the departments of finance and sales remaining the main management units.

5.7.4.3. Markets, sales, production

Till early 1990s, the production of P-07 had been oriented mainly to the domestic market. The economic reform entailed a certain shrinkage in demand, yet due to the nature of production (flour) the effect on the enterprise was not that negative as compared to other industrial branches.

P-07 has managed to find new customers and new suppliers of wheat in the domestic market.

The relatively stable markets of P-07 helped the maintenance of volume of production. The specificity of production does not suppose its diversification, and P-07 keeps on producing three types of flour.

The management attempts an improvement of production quality. Prices, however, rise constantly as a result of the general inflationary situation in the country. Labour expenses per unit of production are not reduced since the staff has not changed in number while wages grow continuously. There hasn't been attained a reduction in material and

energy expenses as well.

The preserved market share, although with new customers, and the maintained physical volume of production at growing prices have resulted in a continuous increase of volume of sales in price terms.

Given the favourable market situation, P-07 is not forced to apply measures typical of the behaviour of other enterprises in the new conditions. It is not selling long-term assets, nor renting machinery or facilities.

According to the managers, a retraining of the staff is not necessary at the present stage. Negotiations with foreign partners for attracting investments and establishment of joint ventures have not been initiated either.

In summary, meeting the credit payments, resource supply and maintenance of employment are considered by managers the main short-term strategies of the enterprise.

5.7.5. Long-term responses of the enterprise

Managers do not consider the unclear responsibilities for the long-term development of the company a factor limiting its adjustment responses. In their opinion, the main long-term strategy is connected with employment maintenance and resource supply. Though looking strange but regardless of existing unclarity of ownership structure the managers act efficiently, keep the enterprise away from bankruptcy and adapt themselves to the new conditions.

5.7.5.1. Enterprise management. Changes in ownership.

The managers of P-07 estimate its functioning successful under the new conditions and with 100-percent state ownership preserved in the single PLC. Though having developed a privatization project, the managers haven't initiated privatization steps till now.

Following the amendments to the Law on transformation and privatization of stateowned and municipal enterprises and the new provisions for mass privatization included, the managers were surprized to find the enterprise on the preliminary list for mass privatization by the voucher scheme. They consider this act too high a 'reward' for their efforts in the recent years to save and adapt the enterprise to the new environment. Moreover, the managers haven't taken part in the preliminary consultations with the Ministry of Agriculture as representative of the owner, which is quite indicative of the strange owner-manager relations.

The way out of this enforced and undesired mass privatization is seen through active steps towards a speedy implementation of the managers' project for privatization envisaging an employee ownership scheme. In more operative aspect, this means efforts for creating a favourable lobby at the local and district administrations, the Ministry and the Privatization Agency, so as to promote the idea for market and not mass privatization of the enterprise.

5.7.5.2. Investments. Changes in the production structure.

After the construction of the second flour-mill the managers do not plan further investments. The maintenance of new outlets is connected rather with more efficient utilization of existing capacities. To this end, however, there hasn't been developed a special programme and managers rely on the favourable trends in the growth of sales volume and relatively good work of the personnel.

A restructuring of production in the near future is unrealistic to expect, too, due to limited range of produced goods.

5.7.6. Estimation of adjustment measures and perspectives of P-07

P-07 has accomplished a successful short-term adjustment in the last years. This, however, is due rather to preserved positions in the domestic market than to new managerial structures or new management of the enterprise.

Maintaining the current situation is considered both short and middle-term strategy of the enterprise. Managers tend to prefer this strategy to any other alternatives of survival or growth and restructuring. They motivate their position by the nature of production, i.e. flour, which a controlled balance item.

Till now, the managers' behaviour has been directed at short-term adjustment and passive preparations for privatization. The moment they got informed about the presence of P-07 on the list for mass privatization, managers suddenly gained a strong impetus for speeding up a privatization procedure initiated by the enterprise.

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