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The Bulgarian Economy: Lessons from Reform during Early Transition

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## Introduction

Bulgarian society has accepted privatization as the most significant aspect of the transition towards a market economy. Although the enthusiasm, typical during the first two years of political and economic changes (1991-92), has largely been replaced by more realistic views of existing problems, public support for privatization is still high. It is, however, often based on vague expectations rather than on a precise estimate of economic results connected with the transformation of property.

In this paper we present an analysis of the development of the process of privatization. The process started with restitution of housing property and agricultural land. Although housing privatization is significant as an emotional issue, it was not a very significant move in economic terms since housing has always been private to a large extent. On the other hand, agricultural land was collectivized during the period of central planning and its restitution is a large, painful and difficult process which deserves a separate study.[1]

Here we concentrate on privatization of enterprises either through cash (or market) privatization where assets are privatized against money or debt instruments, or mass privatization where assets are privatized against vouchers distributed to citizens. In the next section we analyze the public attitude towards privatization. We emphasize the fact that, after the initial euphoria, delays in the privatization process created groups in society interested in opposing the process. In the third section we focus on cash privatization. First we describe the basic institutional framework and then highlight some special features of the Bulgarian program where debt instruments can be used by purchasers for payment for newly privatized enterprises. We also provide data on the pace of cash privatization and show that the process has slowed down. In the fourth section we analyze the process of mass privatization. After describing the basic framework, we draw comparisons between the Bulgarian scheme and similar schemes in other East European countries. Then we provide some data which characterizes the enterprises which will be part of the first round of mass privatization. The fifth section concludes the paper.

### Public and political attitude

At the present moment, the necessity for privatization of a considerable part of the Bulgarian economy is not being questioned in public debate. On the political level, there is a consensus among the main political powers regarding the necessity for carrying out a large-scale and consistent privatization policy. In practice, however, implementation of appropriate measures for carrying out the process has its difficulties. Privatization has been delayed and in the past several years groups have formed who are interested in halting or at least slowing down the process. These groups have gradually grown stronger and can currently control levers for exercising their influence.

Managerial teams in state-owned enterprises represent one such group. Most of them see privatization as a threat since the new owners will probably assign new managers. For many managers this means more than just losing their positions and salaries. By directing the purchases and sales of the state enterprise to specific firms where they have close connections, some managers have been able to obtain additional income.

Many executives possess high professional skills and loyalty to state-owned property. At the same time, however, a number of cases have become public in which managers of state-owned enterprises have put their own interest before that of the state enterprise. The State is unable to exercise much control over state enterprises. This gives executives in state-owned enterprises relatively wide autonomy. In addition, more recently it has become common to appoint executives of state-owned enterprises for political reasons rather than their professional skills and qualifications. It has become the practice for each newly elected government to change hundreds of state-owned enterprise executives. In this situation, executives can expect that their appointment will last until the election of a new government. Appointment depends on whether or not they supported the ruling party. For the executives themselves the objective becomes maximization of their personal gain during the short period of the current administration. In such an environment, the silent objection of managers to privatization in which they take no part is only natural.

Another group whose interests clash with the process of privatization are middle- and high-ranking government officials who currently supervise the state-owned enterprises in the relevant ministries. When large-scale privatization eventually comes, they will lose their direct power over the decision-making process in the enterprises and over the election, appointment and evaluation of managers. Many of these gov-



ernment officials have been appointed to governing bodies of the enterprises (i.e., Boards of Directors or Supervisory Boards), giving them considerable income and prestige but in practice no real influence on the economic results of the enterprise. Some of them are included in the governing bodies of not just one, but several enterprises. With privatization such officials will suffer considerable losses and this motivates them to give their unvoiced opposition to the process.

These government officials can also influence the privatization process in other ways. They can influence the speed of privatization through specific practical procedures that are undertaken in the administration. Second, as members of the governing bodies of the enterprises, they can have negative influence on prospective privatization initiatives. This influence can be exerted both when the privatization initiative is internal to the enterprise (i.e., by the employees) or when local or foreign strategic investors express interest in the enterprise.

Resistance or opposition to privatization may also arise from large economic organizations which have already developed. They are trying to control particular sectors of the economy. They do not presently have the resources to buy enough enterprises in a sector to control it, but given sufficient time they may be able to obtain enough capital. They are attempting to block the privatization of specific enterprises when they believe that prospective privatization may be detrimental to their interests. Tourism is an example.

Slowing down the privatization process can also be caused by the government, even when it makes frank declarations of its intentions for carrying out the process. Up to the present moment, Bulgarian governments in their realization of the necessity for privatization, remain ideologically associated with particular forms of privatization. The UDF (Union of Democratic Forces) government, driven by purely market-oriented principles, supported only cash privatization and explicitly rejected mass privatization. In their view mass privatization is associated with socialist principles. On the contrary, the current BSP (Bulgarian Socialist Party) government, again driven by ideological principles, already made public announcements that it would primarily support mass privatization. In the present situation, these alternative approaches have different advantages and disadvantages. From the position of economic rationality, the combination and equal treatment of the different approaches is required. The ideological preferences of each successive government to one particular form of privatization inevitably leads to delaying the other forms.

### Cash privatization

Privatization in Bulgaria started after a delay of two or three years, when compared with other Central European countries. There are a number of underlying reasons for this delay, but it is also means that the beginning of the process has been carefully prepared. The enabling legislation has been passed and the regulations bearing on cash privatization have now been written.[2] The responsible institutions have been created and a considerable number of state and municipal firms are organizationally prepared for privatization.

*Legal and institutional framework*

Until the end of 1995 cash privatization was the basic form of privatization in Bulgaria. This differs from other Central and East European countries where mass privatization has been the principle mechanism for privatization. Underlying this decision has been the conviction that Bulgarian enterprises should be owned by persons potentially capable of ensuring their prosperity through investments and modern management. This objective has taken precedence over speed of privatization alone. With this objective in mind legislation was passed which provided equal opportunities for investors, be they Bulgarian or foreign. This was combined with opportunities for employees to acquire shares under preferential conditions (50 per cent discount).[3]

The Bulgarian Privatization Law envisages a many faceted approach to cash privatization whereby different government entities control different aspects of privatization. The law and the extensive complementary regulations issued by the government define the prerogatives of ministries and state and local governments. Small enterprises are privatized under the authority of the relevant ministries. Large enterprises are privatized under the authority of the Agency for Privatization. Very large enterprises need the approval of the Council of Ministers as well. Municipal property is privatized under the authority of local governments. The law also takes into account specific forms of public property in Bulgaria and differentiates across economic sectors supervised by different branch ministries. The institutional scheme for privatization in Bulgaria was intended to be flexible, provide an opportunity to apply different techniques, and restrict bureaucratization of the process.

In practice, many different institutions have been actively involved in the process of privatization. This was suppose to motivate these institutions to assist and enhance the process, as well as improve their expertise. Later it proved that this created tension between institutions and more barriers to the process.

*Role of government* The main government institution in charge of cash privatization in Bulgaria is the Agency for Privatization. It is a state institution under the direction of the Council of Ministers. Six members of the Supervisory Board are elected by the Parliament and five are appointed by the Council of Ministers for a term of four years. The executive director is appointed by the board. The main functions defined within the law render the Agency virtually independent. It is responsible for general organization and control of privatization of all state enterprises. The Agency is



responsible for promulgation of an annual privatization program which includes: the minimal number of state-owned enterprises to be privatized during the respective year, the expected amount of revenue, privatization expenses, a list of industries and/or enterprises which should not be privatized, general lines of privatization of municipal-owned enterprises. It is responsible also for decision-making for state-owned enterprises, provided their fixed assets exceed 70 million levs book value, for licensing of appraisers and for collecting information on the entire process of privatization in the country.

The sector ministries are in charge of privatization of state-owned enterprises whose fixed assets do not exceed 70 million levs book value. In their structure they have departments specialized in organizing and implementing privatization transactions.

In January 1995 a new Ministry of Economy and Development was established. One of its main functions is the general coordination of cash and mass privatization. The Ministry of Finance also assists the process of working out the financial part of the annual privatization program and exercising specific financial operations. The municipal councils are in charge of privatizing enterprises owned by municipalities. All common procedures envisaged by the privatization law for the state-owned enterprises are applied in the privatization of municipal enterprises, as well.

*Role of parliament* Parliament has a special commission for privatization and property issues. Its role is to assess the annual privatization program elaborated by the Agency for Privatization and submitted by the Council of Ministers. The Parliament debates and approves the program. The commission regularly controls the Agency through hearings on its activities. In addition each member of Parliament can request information from the Agency in accordance with common rules for parliamentary control.

*Role of enterprises* The law provides for the possibility that the management of enterprises and/or the employees can put forward privatization proposals for their enterprise. Since 1993 most of enterprise privatization programs have been initiated by their managers and employees. One of the principles underlying the Agency's decisions on privatization is to take into account the considerations of managers and employees, although the law does not explicitly state this.

*Role of the private sector* The law does not envisage that the Agency should necessarily respond to every motion for privatization made by private investors. They could, therefore, initiate privatization indirectly through managers and/or employees or the respective state or local institution in charge of privatization by convincing them of the necessity of privatizing the respective enterprise. For the time being Bulgarian investors are mainly interested in small and medium-sized enterprises.

Large enterprises are expected to attract principally big foreign investors.

The law furnishes certain possibilities for 'privatizing privatization'. The institutions in charge of making privatization decisions may authorize other persons to carry out privatization transactions, but this opportunity has not been used actively so far. The evaluation of enterprises to be sold is almost entirely 'privatized' owing to the special requirement that it should be performed by independent appraisers, most of whom are individuals and private consulting firms. The appraisers for each privatization project are chosen on a competitive basis.

The law envisages that privatization should be carried out on the basis of privatization programs which are approved annually, but so far such programs were either not created or approved relatively late. For example the 1995 program was not accepted by the Parliament until May 1995.[4]

The first steps towards privatization in Bulgaria were marked by an opportunistic approach, i.e., privatization started wherever immediate material interest existed. This was also observed in other Central European countries. This approach can be justified because it encourages the process to develop quickly, and privatization criteria and schemes thus crystallize. Nevertheless, the government is trying to focus on a systematic approach based on sector projects. The sector approach allows state organs and potential investors to form a clearer picture of the respective market: its size, level of competition, prospects, substitutes, suppliers, etc. These are factors which are relevant for the organization of privatization and estimation of the prospects for investment.

### *Debt for equity*

The lack of effective demand has always been a serious obstacle for rapid large-scale privatization in Bulgaria. The country is heavily indebted, bearing a burden of domestic and foreign debts that handicap its long-term development prospects. Cognizant of this, authorities looked for a way to reduce debt and help privatization. Debt-equity swaps were introduced as an additional means of payment in privatization. Two main groups of financial instruments were created and allowed to be used in privatization deals:

*Domestic debt bonds* In 1994 a law was adopted whereby banks were permitted to exchange state-enterprise debt totaling 32 billion levs and \$1.8 billion for government securities.[5] The debts in Bulgarian levs were exchanged for low interest bonds with 20-year maturities denominated in levs. The dollar debts were exchanged for bonds with 20-year maturities and denominated in U.S. dollars. Both instruments are tradable and have market prices. The bonds can be used as payment for state property. In order to increase the attractiveness of these instruments a premium of 40 per cent above the face amount is offered when used in privatization. At present the premium



is close to that figure as the market price of lev denominated bonds is close to their face value.

*Foreign debt bonds* In June 1994 Bulgaria reached an agreement with the London Club for restructuring of roughly \$9.3 billion in foreign debt. Following the agreement two types of bonds, DISC and FLIRB, covering the debt were accepted as means of payment in privatization under different options.[6] DISCs are accepted at 100 per cent of their face amount. Since the market price is approximately 51 per cent of their face amount, they have a value in the privatization program at almost double their market price. FLIRBs can be used for payment in the privatization process at 50 per cent of their face amount. Since they are trading at approximately 30 per cent of their face value, there is close to a 66 per cent premium if used in the privatization program.

Government has three levers for controlling this program. The premium on domestic bonds will be reduced to 30 per cent after June 1996. Second, bonds can only be used to make part of the total payment; cash must be used to pay the remainder. Initially domestic bonds could be used to make 90 per cent of the payment. This share was reduced to 70 per cent and the use of foreign debt bonds are now limited to 50 per cent of the payment. Third, the market price of domestic bonds has increased reducing the premium they received in the privatization program. Thus the advantage of using bonds in privatization is gradually decreasing as a result of both administrative and market factors.

Economic nationalists oppose the use of debt-equity swaps because they claim that it represents a 'loss of national sovereignty' and 'country's giveaway'. The introduction of these instruments has helped privatization by motivating more investors to look for placement of these new instruments. The structure of payments in privatization in 1995 was 41 per cent cash, 35.8 per cent domestic bonds and 23.2 per cent foreign bonds. This confirms the importance of these instruments in the privatization process.

But there is a serious problem arising from the substitution of debt for cash payment. Bulgarian privatization legislation channels the proceeds of privatization to specific funds. The reduced cash proceeds has decapitalized these funds and reduced their role in restructuring.

### *Progress of the process*

Following the adoption of the Law on Privatization in April 1992 and the creation of the Agency for Privatization in September 1992, several months were needed to prepare for the first privatization transactions. The first, the sale of a servicing shop, was completed by the Ministry of Trade in February 1993. The first big transfer of \$20 million was contracted between the Agency for Privatization and the Belgium

'Amillum' company for a modern maize-processing enterprise in north-eastern Bulgaria. In the following months of 1993 and 1994, the number of both enterprises being prepared for privatization and completed privatization transactions increased. This changed when the Bulgarian Socialist Party came to power in February 1995. The new government completed a larger number of privatization transactions, but these were primarily small shops and or small-scale equipment. Often these were separate parts of larger producing units. The total value of privatization transactions decreased in 1995 when the value is calculated in convertible currency (so that it can be adjusted for inflation). The main results of the privatization process in terms of the number and value of transactions are presented in Tables 10.1 and 10.2.

The introduction of new payment instruments, the gradual clarifying of the administrative schemes, and the accumulated experience by the administration were among the conditions which contributed to speeding up the process in 1994. The political environment was definitely unfavorable for privatization in 1993 and 1994. Although the Berov government defined itself as a government of privatization, Parliament failed to pass the 1993 and 1994 privatization programs. Towards the end of 1993 and in the first half of 1994, these contradictions became very clear with regard to both the privatization of tourism and mass privatization. This created an unfavorable environment for the operation of the Agency for Privatization.

The interests of concerned managers of state-owned enterprises and potential investors were promoted through the parliamentary commissions. This provoked debate and eventually increased the pressure on privatization officials. In this period, some of the bigger privatization transactions were subject to severe attacks regarding their economic purpose and legality. As a result, the public began to view privatization as a process for the enrichment of a few who were now acquiring property rights to all the wealth accumulated by society throughout the decades. These feelings intensified during the pre-election campaign in the fall of 1994, and this became a psychological obstacle to the privatization process in the first half of 1995.

Another problem was that important positions in the privatization bodies were occupied by people who lacked experience with the privatization process. They had great expectations regarding the price and other terms of the privatization transactions. As a result, some large transactions were revised on the eve of their conclusion and were not successfully finalized.

On the other hand, a number of favorable conditions for privatization existed in 1995. For the first time, Parliament adopted an annual privatization program, thus legitimizing the ambitious goals set by the government in the field of cash privatization. In addition, a relatively well-functioning scheme was created for the use of debt bonds in privatization as well as opportunities for high discounts. This stimulated the participation of potential investors.



**Table 10.1**
**Number of privatization transactions**

| | *1,993* | *1,994* | *1,995* |
|---|---|---|---|
| State property | 63 | 162 | 309 |
| Agency for privatization | 6 | 33 | 69 |
| Other state bodies | 57 | 129 | 240 |
| Municipal property | 53 | 384 | 1,213 |
| Total | 116 | 546 | 1,522 |

*Source*: Agency for Privatization.

**Table 10.2**
**Financial results of state property privatization** (in millions)**

| | *1,993.00* | | *1,994.00* | | *1,995.00* | |
|---|---|---|---|---|---|---|
| | BGL | USD* | BGL | USD* | BGL | USD* |
| Revenue | 384.80 | 13.90 | 10,820.0 | 199.50 | 7,464.40 | 111.10 |
| Liabilities undertaken** | 818.90 | 29.60 | 2,161.80 | 39.90 | 4,937.10 | 73.50 |
| Future investments contracted | 1,464.50 | 53.00 | 9,762.20 | 180.00 | 10,282.0 | 153.10 |

*Source*: Agency for Privatization.
* Calculated by converting the value in lev into US dollars on the basis of the official exchange rate of the Bulgarian National Bank.
** Liabilities undertaken are mostly bad debts of enterprises that are taken on by the new owners. These include liabilities to banks, the state budget, and employees.

The number of privatization transactions concluded in 1995 considerably surpassed the results from previous years. To a large extent, however, this was due to a large number of small projects where preferential participation was given to employees or renters. The increased privatization activity also reflected the greater participation of municipalities in the privatization process. A more adequate picture of the situation is given by a comparison of the financial results achieved. These show a considerable decrease in 1995. The same applies to the volume of investments carried out by buyers in the years following the transaction.

The role of foreign investors in the process of privatization has always been considered particularly important, notwithstanding the ever present support for the view that Bulgarian enterprises should remain for Bulgarian investors. Data on foreign investments in privatization are presented in Table 10.3.

**Table 10.3**
**Foreign investments contracted by agency for privatization**

| | *1993* | *1994* | *1995* |
|---|---|---|---|
| Number of transactions | 2 | 6 | 4 |
| Revenue (millions USD) | 22 | 123.1 | 7.8 |
| Liabilities undertaken (millions USD) | - | 6.3 | 13.6 |
| Future investments contracted (millions USD) | 30 | 108.1 | 49 |

*Source*: Agency for Privatization.

According to Foreign Investment Agency data, direct foreign investments in Bulgaria during the period 1991-95 was $530 million. The volume of investments made through the process of privatization was $220 million or about 40 per cent of the total. Both in absolute and in relative terms foreign investments in privatization is low compared to other countries from Central and Eastern Europe or Latin America.

After four years, using primarily a revenue maximizing approach of cash privatization, the amount of privatization is still very limited.[7] Both domestic authorities and international financial institutions (not to mention investors) are dissatisfied. Privatization policy and practice in Bulgaria has been systematically criticized as weak and limited. The failure to successfully carry out privatization programs has been a constant feature during the last four years. Even the 1995 program, backed by an ambitious new government and supported by a majority in Parliament, fulfilled less than 50 per cent its objectives with respect to the key parameter – revenues.

## Voucher (mass) privatization

After traveling along a long and winding road, in 1995 the Bulgarian government offered and the Parliament passed a mass privatization program. Different concepts



and schemes based on the experience of other Central and East European countries were discussed.[8] Initially a Polish-type mass privatization program dominated by the state was proposed. Then the 'opposite' Czech-type liberal model gained support. Finally, a Bulgarian model, deviating from the others, was adopted.

There are strong indications that no reversal will take place and mass privatization will be implemented as planned. First, the political will of the majority in Parliament can be seen as a guarantee. The credibility of the governmental is higher. Second, and may be more important, is the possible social dissatisfaction if things go backwards. The lack of strong political opposition reduces significantly the probability of blocking mass privatization. Furthermore, 1995 was a relatively successful year for the economy. Lower interest rates on deposits increased the attractiveness of alternative investment opportunities. This combined with positive public expectations makes this the most suitable time for starting a mass privatization program.

The initial time table for mass privatization corresponded with a temporary positive shift in macroeconomic policy. But delays in starting the program threaten a loss of momentum generated by these macroeconomic improvements. At the end of 1995 some negative tendencies are in evidence, challenging the confidence of the public and the attractiveness of privatization. The most important is the growing crisis in the banking system. During 1995 the cumulated loss of Bulgarian banks reached 35 billion levs and the total decapitalization of the banking system was 103 billion levs. A few banks are threatened with bankruptcy. The problem is spreading among both state-owned and private banks, raising doubts about the crucial anticipated role of financial intermediaries in the mass privatization process and their role in corporate governance. The popular dissatisfaction with the destabilization of the financial system can easily be channeled to the privatization funds and the mass privatization program itself.

### *Legal and institutional framework*

Recognition that the existing privatization approach faces severe limitations both on the demand and supply side motivated the acceleration of implementation of a mass privatization scheme. Ideologically it was introduced as a mean of 'restitution of labor', as a counterpoint of the earlier governments' policy of 'restitution of property'. Economically it was introduced to compensate for the chronic lack of effective demand for privatized enterprises.

From the middle of 1991 to the middle of 1993, mass privatization in Bulgaria was a purely academic endeavor, although this was the time when other countries in the region did their most serious preparation work. Mass privatization in other countries under real conditions can now be analyzed, and Bulgaria should benefit from the lessons learned.

The second period of interest in mass privatization began in May 1993, when simultaneously but independently of one another, the Prime Minister and the Deputy Prime Minister put forward alternative proposals for mass privatization. The Prime Minister's proposal was quite different from any proposals implemented elsewhere, but the Deputy Prime Minister's clearly resembled the Polish program, although there were also some elements of the Czech program. After heated debated in the Trilateral Commission and the government, it was decided that, for the sake of unity and uniformity, a synthesized version should be created and brought to Parliament. Once the idea of adopting a separate law for mass privatization was rejected, it became necessary to pass amendments to the already existing Law of Privatization and Reorganization of State-Owned and Municipal Enterprises. This tied mass privatization to all other elements of the law concerning cash privatization and further impeded and slowed the process. Designing the legal framework for mass privatization took more than a year. Over this period there was considerable change in the political sphere, leading to changes in the prevailing ideas of the privatization model. Slowly, the model of mass privatization was altered so that it depended less on the numerous regulations and state control factors which characterize the Polish version. Initially the law regulating mass privatization was very general, consisting of only ten paragraphs. As a result, many important decisions were left to the discretion of the government which was able to influence the process substantially.

In comparative perspective, the Bulgarian model, at least in its present form, is relatively liberal. It restricts the role of the state and the bureaucracy and allows reasonably easy entry of privatization investment funds. It depends to a certain extent on market mechanisms and does not exclude participation of foreign financial institutions.

Mass privatization will be carried out in separate waves (rounds). For each wave the government has to design specific program to be discussed and approved in Parliament. So far, the program for the first wave has been approved. The government declared that it is trying to achieve three main goals:[9]

1. *Abruptly accelerate the privatization process* The achievement of this goal would overcome the difficulties associated with cash privatization: low demand, slow administrative and legal procedures, and conflicts of interest. Achievement of this goal is expected to reduce the alienation towards privatization felt by a considerable part of the population – a problem that is already creating particular public attitudes. At the same time, the government is attempting to create a modern capital market which it views as a basic element in the infrastructure of a market economy.

2. *Involve the people of Bulgaria in the process of property transformation and open up possibilities for participation in the control and management of transformed property* This goal is unlikely to be achieved. What can be expected is an educational process. In the beginning people have a choice whether to participate or not. Over time they will begin to understand that making investments means



taking risks, and incomes are uncertain. It is unrealistic, however, to expect that the program for mass privatization would provide significant possibilities for influencing the management of enterprises, especially given the low concentration of ownership shares and the lack of experience in a corporate environment.

3. *Adjust the specific objectives of the short-run policy measures to the long-run structural policy: recovery of the state budget; improve the management of the state-owned sector; create clear-cut priorities regarding state investments* With successful implementation of the program, the state would rid itself of its present obligations regarding management of and investment in a number of enterprises. This would enable the state to concentrate on a limited number of enterprises. This may lead to improvement in the management investment policies of the remaining state enterprises. At the same time, mass privatization alone is not enough for achieving the desired improvements. The quality of management in state enterprises depends not so much on the number of state-owned enterprises, but rather on the motivation of these managers and the environment in which they operate. Furthermore, the problem of investments in state-owned enterprises may remain, even with fewer enterprises under state control.

The state budget cannot be expected to benefit greatly in the short-run. The program itself does not generate considerable revenues nor does it impose great expenditure obligations. Possible improvements in the state budget will come only after privatization process creates enterprise restructuring leading to improved efficiency and growth.

The program as planned includes the following stages:

a. Proclamation of the program and popular persuasion campaign.

b. Opening of registration bureaus, registration of the population for participation in the process, transformation of limited liability companies on the list for mass privatization into joint-stock companies. This stage will continue for three months.

c. Transfer of investment vouchers of individuals into privatization investment funds,[10] announcement of minimum prices for the shares of the enterprises in the first bidding session. This stage will take at least one month.

d. Centralized bidding for the exchange of investment vouchers with shares from the enterprises on the list. This will be carried out in three bidding session. Each session will take three months.

e. Post-privatization period of six months after the end of the last bidding session.

Under the scheme all adult Bulgarian citizens above 18 years old have the right to participate on an equal basis if they register at local post offices. After registration, a certificate (voucher book) is given to the participant for 25,000 'investment bonds'. The scheme uses the denomination 'investment bonds' instead of levs. The registration certificate and the bonds themselves are not tradable, and their transfer is limited to close relatives. It is expected that it will be difficult to overcome the official restrictions on transferability of the investment bonds. This puts the emphasis on establishing a secondary market in shares of enterprises distributed under the scheme rather than a market for voucher books and investment bonds. The investment bonds can be used only as a means of payment for shares of the enterprises included in the program. The bonds are divisible. Thus an individual investment portfolio can be created by any participant. There is a small registration fee of about $8 with a $1.50 discount for pensioners, soldiers and students. The registration process began on the 8 January 1996 and was scheduled to end on the 8 April 1996. (The deadline was later extended for one month.)

The Law of Privatization and Restructuring of State-Owned and Municipal Enterprise created a Center for Mass Privatization to govern the process of mass privatization. The law guarantees some independence for the center. It is managed as a legal entity and financed from non-budgeted funds. The center oversees the entire set of activities concerned with the development and implementation of the program. This includes the development of proposals for regulation of the program, printing and distribution of vouchers, and the development of a computer network system for the registration of participants and bidding. The scale, complexity, and innovative character of its tasks would present a serious challenge for even the most experienced institution. By contrast, the center was created *ad hoc*, operates on short deadlines in an atmosphere with vaguely defined regulations. It has suffered from serious personnel turnover. The first director was replaced only a few months after his appointment.

There are similar concerns about another key institution, the Securities and Stock Exchanges Commission. This Commission was created to license the activities of the privatization investment funds. According to the law, the government was supposed to establish this Commission by the end of August 1995. Instead, the chairperson and several members of the Commission were appointed in January 1996. Only a couple of weeks before the end of the campaign for the registration of the voucher books, the Commission was organizing itself and seeking the right personnel and premises for its operations. As a result, not a single privatization fund was registered in March 1996, and the promulgation of regulations pertaining to privatization funds were seriously delayed. This has had a negative impact on the advertising campaigns of the privatization funds and lowered the participation rate of the population in the mass privatization program.

Holders of a certificate (voucher book) have two basic options. They can take part directly in the centralized bidding and acquire shares in one or more enterprises.[11] Alternatively they can invest some or all their vouchers in privatization funds. When they invest in a privatization fund they become shareholders in the fund. One investment voucher equals one lev of capital in a privatization fund. With these investment vouchers the privatization funds bid for shares in the newly privatized enterprises.



The activities of the funds are regulated by a specially designed Privatization Funds Law. The main goal of this law is to avoid weaknesses that have arisen in the regulation of other financial institutions.[12] The law puts a number of restrictions on the activities of the funds. These can be grouped under three main concerns:

1. *Securing maximum transparency and availability of information regarding the funds aimed at protecting small investors.* There are specific requirements that funds must observe regarding publicizing information in the form of fliers. These fliers must provide information about the larger shareholders, the professional qualification and experience of executives and the investment and dividend policies of the fund.

2. *Reducing the risk for small investors and stimulating competition among funds.* In order to minimize the risk a number of restrictions have been placed on funds. They are not allowed to invest more than 10 per cent of their capital in shares issued by one company, nor are they permitted to extend credits or to take loans, issue bonds or guarantees, or invest in companies related to members of the fund's governing bodies.[13] Privatization funds are not allowed to invest in other privatization funds without the Commission's approval. There is a limitation on the stake in one company that a privatization fund is allowed to buy. To avoid monopoly control, the law restricts this stake to 34 per cent, which compared to restrictions elsewhere is a relatively large stake and should allow a high degree of corporate control.[14]

3. *Establishing a mechanism for exercising supervisory control over the privatization funds.* The funds are obliged to present annual and semi-annual reports of their activities to the Securities and Stock Exchanges Commission. These reports are required to provide details about securities transactions including buying and selling prices, clients and dates of transactions. The funds are also obliged to present to the Commission quarterly reports for the investment vouchers. Besides the supervision provided by the Commission, many funds are controlled by depositories.

A comparison with the supervision presently in place to oversee other financial institutions is enlightening. Control over the entire banking system is exercised by a department in the central bank that has between 30-40 employees. Due to the lack of a legal regulation, insurance companies have no special regulations and operate within the framework of the commercial code as common joint-stock companies. By contrast, the Securities and Stock Exchanges Commission intends to operate with a staff of about 300 employees.

Most Central and East European countries have already carried out or are in the process of preparing mass privatization programs as a radical means for the fast restructuring of their economies. These programs differ because of specific economic circumstances and differing public attitudes towards privatization.

Russia has already carried out such a program. The Russian model has ended up favoring the large financial institutions and state-enterprise managers. The program started quickly in December 1992, but people did not receive an explanation of how to use the vouchers, and they willingly sold them for a small price. Many vouchers were sold on the secondary market instead of used to invest in privatization transactions. By the end of January 1993, 98 per cent of the total of 150 million vouchers were distributed among the population. This suggested a high level of readiness for participation. The participation itself, however, was much more complicated and limited in scope. For example, sales were often segmented through the application of different payment instruments for one and the same transaction.

Presently there is a strong mass privatization campaign taking place in Slovenia. Each citizen of Slovenia, regardless of age, is eligible to open a 'privatization account' with the national statistics office. The value of the account varies between $800 and $3200 depending on individual's age. The total amount of the operation exceeds nine billion German Marks or 40 per cent of the capital of state-owned enterprises. Participation is fee-free and the expenses are minimal due to the cashless character of the operation. No special papers or documents are issued for either the certificates or the shares in the enterprises. Private investment funds applying to participate in the scheme are licensed on the basis of high capitalization requirements. In addition, the funds must demonstrate that they will be managed by a management company of proven skills and professionalism.

The basic principles of the mass privatization program in Poland are entirely different.[15] By administrative decision, 15 National Investment Funds have been created, each of them governed by a consortium composed of an international investment bank, a consulting company, and a Polish commercial bank. Polish citizens will acquire shares from these funds. The ownership structure of every state-owned enterprise listed in the program is fixed initially with a distribution whereby: one fund gets a 33 per cent stake, all remaining funds receive equal stakes of 1.9 per cent, the employees of the enterprise receive 15 per cent, and the state preserves a block of 25 per cent. The majority stakes of 33 per cent are distributed among the funds on the basis of a specially designed bidding process.[16] The total number of enterprises to be privatized in this way is relatively small, and they account for about 5.4 per cent of Poland's GDP.

From the beginning, the Bulgarian mass privatization was strongly influenced by the Czech scheme and in some aspects it is similar. Based on parallel implementation of two basic streams of participation, direct and indirect, the scheme assumes



two basic types of participants. In the transition economy there is a lack of a systematic investment culture and a great number of people will probably be unprepared or unwilling to make strategic investment decisions. For them the scheme offers the indirect participation option, institutionalized through the privatization funds. Others who are willing and ready to risk making an investment themselves can do so by directly buying shares. In this sense the scheme is adaptive.

Political support for mass privatization in Czechoslovakia and later in the Czech Republic is paradoxical. Mass privatization was imposed with strong pressure from the right-oriented political forces of the Prime Minister Vaclav Klaus, not from the left and populist forces. The populist effect of mass privatization was used to balance other unpopular right-wing measures. In Bulgaria, the process is ideologically more straight forward since it is carried out by a new socialist-oriented government.

Mass privatization in Czechoslovakia occurred in two waves. The first, in 1992-93, covered Czechoslovakia as a whole. The second was carried out only in the present Czech Republic.[17] Territorial differences make a comparative analysis of the two waves more difficult, but it is meaningful that the more developed Czech Republic demonstrated greater consistency of action and was quick to start another privatization wave while Slovakia gave up the plan. Nevertheless, experts in both countries share the unanimous opinion that mass privatization is best carried out in one wave, with the maximum volume of enterprise assets involved. The Czech experts admit that they would never have initiated a second wave were it not for the necessity to 'soften' some of the inequities that have emerged from the division of the country. Contrary to this recommendation, the Bulgarian model is designed around several successive waves.

In Czechoslovakia, nearly 80 per cent of the eligible population over 18 years took part in the first wave, although no more than 30 per cent was initially expected. It is generally agreed that the investment privatization funds played a crucial role in encouraging participation through their advertising campaigns at the beginning of privatization. Preliminary estimates on the readiness of population to participate in mass privatization proved unreliable since they had not anticipated the impact on the demand for the privatization funds.

To register, participants in the Czech plan had to pay to $30. In return they received a voucher book of 1,000 points. Unlike Bulgaria, where a voucher book will be equal to 25,000 levs, the Czech scheme is based on points, the price of which is not bound directly to the national currency. For most people in Bulgaria, the price of the voucher book is psychologically connected to the 25,000 levs valuation announced by the government and not with the 500 levs paid for the book. In Czechoslovakia, the advertising was based on a promised return relative to the participation fee of $30, not on the value of the shares acquired against points. Some privatization funds, for example, advertised an amazing tenfold guaranteed increase in the fee invested, from $30 to $300, for instance. In Bulgaria, the market value of shares of privatized enterprises is expected to fall below their nominal value. This makes advertising more difficult and lays the ground work for possible wide-spread discontent due to unsatisfied expectations.[18]

The first wave of mass privatization in Czechoslovakia took 21 months, including one month for promotion, four months for registration of participants, three months for citizens to invest their vouchers in privatization funds, eight months for the five successive rounds of bidding, and four months for summarizing the results. It was only after this technical period that the enterprise shares were actually transferred to their new owners.

The establishment and registration of privatization funds in Czechoslovakia followed a relatively easy procedure. The funds had to meet two conditions: 1) be a joint-stock company and 2) meet a minimum capital of one million Kcs (about $30,000). Their capitalization increased as they acquired additional privatization voucher books from citizens.[19] The funds were obliged to issue shares and thus turn their clients into shareholders of the fund. The registration was assigned to the Ministry of Privatization. No restrictions were imposed on the number of funds that could be registered by one person, legal or physical, nor on the persons who could register a fund. There were 264 investment funds registered by 186 sponsors, including one company which registered 11 funds.

By comparison the Bulgarian legal framework pertaining to investment funds is much more restrictive. The law creates a more complicated procedure of registration with a large number of requirements. It is likely that those who drafted the Bulgarian Law on Privatization Funds paid attention to the Czech experience and are trying to avoid a situation where funds become powerful economic agents which the state might have difficulty controlling. The Bulgarian regulations make a clear attempt to avoid such a phenomenon.

*Supply side*

A specific feature of the Bulgarian privatization scheme is the bidding procedure. It is regulated in a way which combines acceptable prices, competition on the demand side and perfect price discrimination. Individuals and privatization funds will bid for shares of companies. The process will begin when they bid by announcing a price denominated in investment bonds and the number of shares they are willing to buy of each company. The offers will be ranked and fulfilled according to the bid prices. There will be minimal prices per share for each company announced before the start of each session. If the number of shares demanded is smaller than the number of shares supplied, the differential will be offered at the next session and the minimal price will be lowered. If, after the third session, there are still unsold shares, the remaining shares will be distributed proportionally among those who have already bought shares in the company. Trading in the new shares will be permitted six months after the end of the last session.



While there was no price bidding for the shares in the Czech scheme, Bulgarians must bid by offering a price per share in investment bonds. There will be no cancelling of bids if an oversubscription takes place, rather low bids simply will not be fulfilled. Such a scheme is more complicated to execute and difficult for the general public to understand. Analysis is needed not only of the viability of companies but also of the expected effective prices of the targeted shares. These complications should lead to greater participation in the investment funds since they should have better knowledge of the market situation. But common sense is not always present in a society in transition.

The total number of shares to be distributed among the population is 80.461 million with book value of 80.461 billion levs. The number of enterprises included in the scheme is 1,063 state-owned companies out of 3,701 state-owned enterprises from all branches of the economy.[20] In its final version, the Bulgarian scheme demonstrates a desire to broaden the number and volume of shares included. Different companies are offered for privatization with different stakes of their capital. Basically, the companies can be classified in three groups:

Group 1: These are companies where only 25 per cent of the capital is offered for mass privatization.[21] Typically, these are large-scale enterprises with an important place in the national economy. Having the majority stake of 75 per cent, the state clearly wants to dominate the governance of such companies. In this way, the government will have the discretion to look for strategic investors or to keep control over the enterprises.

Group 2: These are companies where 65 per cent of the capital is offered and in a very few cases where stakes of 50 per cent are offered. The enterprises in this group are primarily medium-sized, although some large enterprises are included as well. The state will continue to be a very important shareholder in these companies given the fact that privatization funds are allowed to hold no more than 34 per cent of the shares, while the state will hold 35 per cent. Clearly, the state will exercise control over the strategy of such enterprises even when the private owners have a well-synchronized policy.[22] It is likely that the state will try to gain from the eventual improvement of such enterprises after they are privatized and will probably attempt to sell its stake at a relatively high price later.

Group 3: In this group are companies where 70 to 90 per cent of the capital is offered. These are medium and small enterprises. They will be entirely transferred to private ownership. The remaining stake is being reserved to compensate former owners of buildings or land in these enterprises.

The distribution of the state-owned companies with respect to the relative share of their capital offered for mass privatization is presented in Table 10.4.

**Table 10.4**
**Distribution of state-owned companies included in the list for mass privatization**

| *Companies offered with* | *Number* | *Book value of capital offered (mil. Lv.)* | *Relative share of capital offered (book value, %)* |
|---|---|---|---|
| <25% stake | 199 | 32,563 | 40.5 |
| 26-65% stake | 347 | 30,218 | 37.6 |
| >66% stake | 517 | 17,680 | 21.9 |
| Total | 1,063 | 80,461 | 100.0 |

The program includes enterprises from all branches of the economy and in this sense it is well-diversified. Only companies from branches with exclusive legal restrictions on privatization like the extraction industry, ports, and telecommunications are entirely excluded. Probably, a weak point of the selection process was its great centralization and the fact that enterprises were not given a choice. Unlike Czechoslovakia, managers and employees were not asked for their privatization plans, thus losing their cooperation. At the same time, however, this centralization gave the government the opportunity to speed up the process and to follow a more consistent structural and regional privatization policy. In Tables 10.5 and 10.6, the distribution of the enterprises offered for mass privatization with respect to the branches of the economy and to the regions in the country are presented.

**Table 10.5**
**State-owned companies by branches**

| *Branches* | *Total no. of state-owned companies* | *No. of companies offered for mass privatization* |
|---|---|---|
| Industry | 1,930 | 760 |
| Construction | 320 | 79 |
| Agriculture | 280 | 40 |
| Transportation & communications | 266 | 73 |
| Trade & others | 692 | 27 |
| Services | 213 | 84 |
| Total | 3,701 | 1,063 |



**Table 10.6**
**Regional structure of state-owned companies offered for mass privatization**

| | *Total no. of state-owned companies* | *Total equity (millions Levs)* | *No. of companies offered for mass privatization* | *Equity offered for privatization (millions Levs)* | *Potential no. of inv. bonds* (millions)* |
|---|---|---|---|---|---|
| Sofia-city | 628 | 40,134 | 129 | 13,333 | 24,014 |
| Bourgas | 316 | 26,263 | 104 | 9,455 | 16,635 |
| Varna | 402 | 25,800 | 107 | 8,911 | 17,629 |
| Lovech | 459 | 21,605 | 162 | 10,746 | 20,031 |
| Montana | 292 | 12,922 | 90 | 5,667 | 12,427 |
| Plovdiv | 468 | 19,901 | 138 | 8,852 | 23,654 |
| Rousse | 351 | 15,244 | 107 | 7,092 | 14,843 |
| Sofia-region | 464 | 23,131 | 127 | 9,880 | 18,987 |
| Haskovo | 321 | 16,245 | 99 | 6,525 | 16,991 |
| Total | 3,701 | 201,245 | 1,063 | 80,461 | 165,211 |

*Calculated by multiplying the total number of eligible individual-residents of the region, by 25,000.
*Source*: Mass Privatization–Where to Invest?, Club 'Economics 2000', authors' calculations.

The financial position of the companies in the list for mass privatization is close to the average for the economy. The 'deadbeats' are deliberately excluded, thus reducing the probability of quick loss of confidence or immediate failure. Still a portfolio weighted by the share of the companies capital, included in the list, is loss-making according to the 1994 data. The distribution of the profitability of companies is presented in Table 10.7.

One of the most important characteristics of mass privatization is connected with the supply of information. Since many individuals are hesitant, good information with respect to enterprises provided in a timely fashion might increase the credibility of the process. Moreover, better information will contribute to better investment decisions and better allocation of investment bonds.

**Table 10.7**
**Number of profitable state-owned companies**

| | Total no. of state-owned companies | No. of profitable state-owned companies* | No. of companies offered for mass privatization | No. of profitable companies offered for mass privatization* |
|---|---|---|---|---|
| Sofia-city | 628 | 346 | 129 | 77 |
| Bourgas | 316 | 131 | 104 | 52 |
| Varna | 402 | 166 | 107 | 47 |
| Lovech | 459 | 182 | 162 | 69 |
| Montana | 292 | 92 | 90 | 25 |
| Plovdiv | 468 | 210 | 138 | 72 |
| Rousse | 351 | 137 | 107 | 56 |
| Sofia-region | 464 | 152 | 127 | 55 |
| Haskovo | 321 | 113 | 99 | 46 |
| Total | 3,701 | 1,529 | 1,063 | 499 |

*According to the official financial statements of enterprises in 1994.
*Source*: authors' calculations.

There are at least three ways in which better information could contribute positively to the process. In each case the situation is far from being satisfactory. First citizens need to understand the importance of the process itself. Why is the mass privatization crucially needed for the country? What are the potential benefits of participation in the program for the common citizen? Do these benefits exceed the registration fee? Why should people pay money for participation? What could people who have never seen corporate shares do with the shares of the privatized companies? These and many other questions have not been explained in the government's campaign. The campaign has dealt only with basic information about who is eligible and where to register.

Secondly, the public is not well informed about the privatization funds. Since funds were not licensed until the very end of the registration period, official advertising was illegal during the period when people were making decisions whether to participate or not. Some funds did a kind of 'semi-official' campaign, but the danger always existed that they could be subject to legal prosecution. Although many financial groups have announced their plans to establish privatization funds, no intensive private advertising campaign took place. This might help explain why participation in the program has been so low. The invasion of funds, if allowed, and official advertising campaigns would increase the number of participants, as it did in Czechoslovakia during the first wave.



Thirdly, more information related to enterprises on the list for mass privatization should have been made available. At the end of the registration period a large number of enterprises had not prepared the information required. The requirement includes information on the economic prospects of the firm, financial indicators, legal analysis on ownership rights, and some additional documents. Table 10.8 presents the state-of-affairs only a month and a half before the registration period. Nearly half the enterprises are still lacking regular documentation, the problems being connected most often with legal analyses. Only three companies have not presented information prospects, while 52 have not presented either information prospects or legal analyses. Many enterprises have the legal status of limited liability companies, and before being offered for mass privatization they must be transformed into joint-stock companies. Additional time will be needed for these administrative procedures. Under the present circumstances people were making decisions for participation without reliable information about the financial and legal situation of many companies.

**Table 10.8**
**Readiness of the mass privatization process in terms of information**

| | No. of enterprises | No. of enterprises with irregular documents | No. of enterprises which have not presented: Information prospects | Legal anal. | Both cases | No. of ltd. liability companies |
|---|---|---|---|---|---|---|
| Ministry of industry | 659 | 363 | 1 | 315 | 42 | 455 |
| Ministry of regional development | 68 | 27 | 1 | 6 | 0 | 51 |
| Ministry of agriculture | 176 | 50 | 0 | 34 | 6 | 175 |
| Ministry of transport | 73 | 7 | 0 | 1 | 4 | 18 |
| Ministry of trade | 27 | 17 | 0 | 10 | 0 | 6 |
| Ministry of culture | 1 | 0 | 0 | 0 | 0 | 0 |
| Committee for tourism | 54 | 8 | 1 | 7 | 0 | 5 |
| Committee for energy | 5 | 4 | 0 | 4 | 0 | 4 |
| Total | 1,063 | 476 | 3 | 377 | 52 | 714 |

*Source*: *Bulgarian Business*, 1996-97.

At the end of the period for registration about 20-25 per cent of the eligible population is expected to buy their voucher books.[23] Judged against the government's expectations, this number is low, but still high if compared to the first month of the Czech mass privatization when privatization funds were not advertising. It is even higher than in Romania where only seven per cent of the eligible population decided to participate in the mass privatization program at the end of the registration period.[24]

## Conclusions

Four years of privatization experience after the privatization law was adopted in 1992 the scale of cash privatization is disappointing. Both domestic authorities and international institutions supporting the market-oriented reforms in Bulgaria were dissatisfied. The privatization policy and practice in Bulgaria have been systematically criticized as weak and limited. Annual privatization programs, which by law the government must announce each year, are either not created at all or not fulfilled. The last program, for 1995, backed by an ambitious new government and supported by a majority in the Parliament fulfilled less than 50 per cent of its revenue objective – a key parameter.

The slow pace of cash privatization can be attributed to the time-consuming political debates about what and how to privatize, whether there should be domestic or foreign investors, and whether maximum revenue must be obtained. These delays finally led to the creation of groups in society whose interests opposed the process.

At the same time foreign investors often confronted misunderstanding, slow procedures and political uncertainty. As a result, in 1995 direct foreign investments were small but, more important, even less than 1994.

Recognition that the existing approach to privatization faced systematic failures and severe limitations both on the demand and the supply side created a motivation to accelerate implementation of a mass privatization scheme. The program started but already shows many administrative weaknesses. The program has experienced serious delays and the government still has not prepared some important procedures. This might postpone the program further and conceivably erode the credibility of the program.

## Notes

1 See for example Schmitz, A., *et al.*

2 The Law for Transformation and Privatization of State and Municipal-Owned Enterprises was adopted by the Parliament in April 1992. Amendments mak-



ing possible application of a mass privatization scheme passed in June 1994 and December 1995. A bundle of regulation acts was passed by the Council of Ministers, more important ordinances of which are on: auctions, tenders, appraisals, preferential acquisitions of state and municipal-owned shares, information provided to potential investors.

3 Up to 20 per cent of the property rights in the respective enterprise may be bought in this way. As a limitation exists on the maximum value of the discount, which should not exceed a two-year salary, the average value of the preference shares should amount to less than 20 per cent generally, and even less than ten per cent for bigger and technically well-equipped enterprises.

4 The 1995 priority privatization sectors were: tourism, food, agriculture, mechanical engineering, transport, etc. Among the enterprises excluded from the privatization list draft for 1996 were enterprises in the defense industry, mining, power plants and energy transmission facilities, water supply, railway transport and some other with specific functions.

5 The Law on Settlement of Non-performing Credits permitted banks to exchange debt of state-owned enterprises negotiated before 31 December 1990.

6 DISC bonds are discount bonds. These are bonds issued to creditors who have agreed to reduce their claims on the principle. The reduced principle has to be paid in the year 2024 in one payment. The interest is LIBOR +13/16 annually. FLIRBs are Front Loaded Interest Reduction Bonds. These bonds have been issued to creditors who would not agree to reduce the principle obligation but agreed to reduce the interest payments for a certain period. The interest starts at two per cent annually in 1994 and increases gradually until 2002 when it becomes LIBOR +13/16. The bonds must be repaid by July 2012.

7 See Pamouktchiev and Parvulov (1994).

8 See Pamouktchiev and Parvulov (1994).

9 Privatization program through investment vouchers, adopted on 19 December 1995 in Parliament.

10 Investment vouchers, although there are restrictions, can be transferred to close relatives as well as to attorneys.

11 They can also participate through an attorney if they observe specific restrictions.

12 In 1995 many people lost their savings in pyramid schemes. At the end of 1995 and in the beginning of 1996 the first manifestations of a banking crisis began to take shape. The causes were weaknesses in licensing procedures, poor bank supervision, and credit policies.

13 Actually funds can obtain short-term loans with a maturity up to three months after a special approval of the Commission. These loans have to be earmarked for fixed assets related directly to fund's activity.

14 In France, Germany, and Russia this share is ten per cent. In the Czech Republic, Slovakia, and Lithuania it is 20 per cent. In the United States it is

significantly lower, five per cent.

15 A similar approach is being used in Romania.

16 The process is similar to the NBA draft system in United States where each fund draws straws to determine the order of first round choices. The order is reversed for the second round, and so on.

17 Slovakia abandoned the idea of carrying out a second wave.

18 It is hard to explain in an advertising campaign that holding shares of 25,000 levs nominal value and selling them for 15,000 levs actually means a profit and not a loss. Since these shares have been acquired for a participation fee of 500 levs, there is a clear profit.

19 This differs from the Bulgarian case. In Bulgaria the privatization funds announce a preliminary capitalization target and a stated number of shares that can be sold in the fund. Once these shares have been sold for vouchers, the fund cannot acquire more vouchers.

20 This is compared to 299.4 million shares from 1,491 companies in the first wave of mass privatization in the former Czechoslovakia.

21 Some cigarette companies are being offered with a 20 per cent stake due to the fact that small stakes in them have already been privatized.

22 According to the commercial code, the most important decisions in joint-stock companies are made by qualified two-thirds majority. In many by-laws of state-owned companies the qualified majority is even higher, i.e., three-fourths.

23 The paper was completed a week before the end of the registration period.

24 As a result, the government prolonged the registration period and started an intensive propaganda campaign including school teachers and church priests. At the end, 30 per cent of the eligible population registered for participation.

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# 11 Nature and role of small firms in Bulgaria

*Will Bartlett and Rossitsa Rangelova*

## Introduction

Throughout the post-war period communist planners in Bulgaria pursued a strategy of rapid industrialization of an agrarian economy based on state ownership of industrial enterprises and a system of central planning. With the exception of some private activities in agriculture and widespread private-owner occupation in the housing sector, there was virtually no private economic activity in the economy. Industrialization was assisted by substantial financial and technological transfers from the former USSR, high domestic investment rates, and growing specialization in machinery exports into the protected market of the CMEA countries. However, the negative side of this progress became more and more evident in the 1980s: environmental degradation, difficulties in maintaining high economic growth, a rapid increase of the external debt in convertible currencies. According to one estimate (Minassian, 1992), industrial output based on a pattern of extensive development eventually stopped growing and began to fall from 1983 onwards.

A key feature of the industrial structure which was developed in Bulgaria under the previous regime was an extreme over-concentration of the economic activities in very large scale enterprises. In the early 1980s the size of enterprises in Bulgaria in comparison with enterprises in other Eastern European countries ranked immediately behind that of the former USSR. This aspect of economic development was reinforced by the complete lack of experience with markets as a basis for trade. In contrast some other countries in the region such as Hungary and the former Yugoslavia, while being heavily dependent on large scale state enterprises had nevertheless begun to introduce some limited experiments in decentralized market mechanisms and therefore had a more favorable set of initial conditions from which to launch the transition process (Bartlett and Hoggett, 1995). The negative consequences from this over-concentration and absence of market incentives to improve the efficiency