---------TRANSFORMATIONS IN --------
BUSINESS & ECONOMICS



# IS PRIVATIZATION ENOUGH TO CREATE A MARKET ECONOMY? THE BULGARIAN EXPERIENCE

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("La mercantilización de la tierra: cambios formales y realidad en el caso búlgaro", Shkolyar, N.; Sánchez, A.; March, J. A. (eds.): *Dyesyatilyetnïy pyeryejodnogo pyerioda*. Rossiyskiy Universityet Druzhby Narodov, Moskva, 2001; or "*Reforma del sistema financiero y mercantilización en la transición búlgara*", en March, J. M.; Sánchez, A. (eds.): *Avances y bloqueos en la transición económica*. PUV, Valencia. 2002 or "*Entrepreneur women in the sector of social services. A comparative approach in Bulgaria, Spain, France and Italy*", CCS (ed.): *Development of Entrepreneurial Skills of Women in the field of Social Services*. Ikopis, Sofia. 2006).

*Received*: January, 2006
*1st Revision*: April, 2006
*2nd Revision*: October, 2006
*Accepted*: February, 2007

***ABSTRACT.*** ***The transition from a planned economy to a market economy means a systemic transformation process in which the privatization of state assets plays a central role. Fifteen years after the beginning of the Bulgarian transition the privatization process has almost come to an end. This article attempts an overview of the privatization of the whole economy, that is to say the transformation of the state assets as a whole, including financial and non-financial enterprises as well as land privatization. Privatization in Bulgaria does not guarantee the development of a market economy. In the case of land, privatization has generated the development toward farms for exclusive self-consumption. The financial system is concentrated in banking, with little credit activity and a very underdeveloped stock market. In the industrial sector, restructuring of companies is very limited and, although many are unprofitable, there are very few bankruptcy cases.***

***KEYWORDS***: privatization, economic transition, economic policy, structural reforms, Bulgaria.

***JEL classification:*** E6, L33, P48, P2.

## Introduction

The transition from a planned economy to a market economy means a systemic transformation process in which the privatization of state assets plays a central role. In 1989, practically all economic assets in Bulgaria were state-owned. Consequently, the transformation of state property into private property was a huge and complex task. Fifteen years after the beginning of the transition period the process of privatization has almost come to an end; according to the European Commission (EC, 2005), the Bulgarian economy will be ready to enter the European Union in 2007 and this successfully happened on 1st January, 2007.

Analyses of the privatization of the Bulgarian economy are usually dedicated to separate parts of the economy. Most studies focus on the transfer of state assets in the industrial and service sectors. The privatization of other key assets, such as the land and the financial system, is reviewed in works dedicated specifically to these sectors. This article attempts an overview of the privatization of the whole economy, that is to say the transformation of the state assets as a whole, including financial and non-financial enterprises as well as land privatization.

The present study seeks to assess the experience of the Bulgarian privatization process. The article is organized as follows: the first section focuses on the privatization of state-owned industrial enterprises, section two analyses the privatization of bank system, the third revises land privatization, ending with the drawing of some conclusions.

## 1. Privatization of Industrial Enterprises in Bulgaria

### *1.1. The stages*

The privatization of Bulgarian industry was a huge task. Before the transition the private sector was practically nonexistent; the state had about a 95% stake in the industrial sector. The productive structure followed the Soviet industrialization model, while the internal division of labour followed the framework of the CMAE exchange system. There was a high concentration of industries with low added value; the companies were very large and vertically integrated, presenting a marked segmentation of activities, including those of a social character (De Arriba, 1998). Under market conditions their profitability was more than doubtful and their competitiveness low, considering the obsolescence of the fixed assets. In fact, at the end of 1991 half of the state companies had made losses and were heavily in debt (OECD, 1992).

In the years 1989–1992, the first steps of the transition process were initiated, with economic decentralization and liberalization. In January 1989, Ordinance 56 on Economic Activities conferred independent legal status to state companies after their transformation into commercial societies, also granting them certain control of their assets and activities. In 1991, *Regulation 154* on Decentralization and De-monopolization and the Defence of Competition Law facilitated the partition of state companies and allowed free entry into traditionally inaccessible sectors. Also, the Commercial Law of July 1991 allowed the development of new private companies.

In the years previous to the passing of the Privatization Law of 1992, other forms of privatization had developed, such as 'spontaneous' privatization or restitution. Spontaneous privatization developed due to the absence of a proper legal framework for this, and certainly, due to the strategies of groups within the new society that wanted to establish new power positions. Another form was hidden privatization, formally legal, but disrespecting the conditions of transparency, publicity and competition[1]. State companies were also privatized through the sale of shares to employees or external agents in an illegal way. According to some estimates, 10–15% of state property was transferred to the private sector through these kinds of mechanisms (Keremidchiev, 1993).

The second period is comprised of the years between 1992 and 1996. In 1992 the Privatization Law came into effect, although it took almost a year to complete all the accompanying privatization legislation. This law envisaged the transformation of all state enterprises into commercial companies, each of which was to be sold by the traditional case-by-case method as a complete entity. As privatization came up against many obstructions from politicians, state managers, employees and civil servants, only a small number of transactions were completed. In June 1994, the Privatization Law was reformed, introducing new elements such as mass privatization and the preferential scheme for purchase of companies by its managers and employees (manager and employee buy-outs, or MEBO system). In this period, mainly small-scale privatizations made some progress. Attempting to

[1] The process was as follows. First, state property would be rented and thereafter sold directly to the lessee, ignoring public tendering procedures. The state companies played an important role in the creation of private companies by ceding their assets and/or profits temporarily or permanently. An additional form of opaque privatisation was the creation of private companies as input suppliers for state companies that pay high prices. Yet another way was the formation of companies that acquired the subsidised goods at low price to resell them later at higher prices.

boost privatization, the socialist government started preparation for mass privatizations in 1995 and in 1996 the first wave of mass privatizations was launched. By the end of 1996 Bulgaria experienced a deep financial crisis that was followed by new elections and the introduction of a currency board system[2]. Between 1993 and 1996 only 10.84% of the state assets slated to be privatized actually were (Privatization Agency, 2006).

The years from 1997 to 2000 could be considered as a time of real development, also a period of great progress in economic reforms as a whole (Kaminski, 2006). These reforms in Bulgaria are characterized by the setting up of the currency board and close supervision by the IMF. The first wave of mass privatization was finalized by mid-1996, and preparation for the second wave was begun. Far ranging changes were made in all privatization legislation to speed up and facilitate the process. The privatization of the financial sector got underway, and state agencies became more active in searching for foreign investors. Looking at specific results in this period, privatization achieved a certain success. However, at the same time public opinion and support for privatization declined due to corruption scandals and the poor functioning of public agencies dealing with privatization. The activity in the period 1997–2000 was intense, with 66.96% of the state assets remaining to be privatized being privatized (Privatization Agency, 2006).

The fourth stage began in 2001, which saw new amendments to the Privatization Law with the intention of giving new impulse to the process. This period is characterized by the start of the privatization of the state monopolies in the sectors of telecommunications (Bulgarian Telecommunication Company), energy, transport and others such as Bulgartabac[3] (AEAF, 2003). This period is also characterized by the introduction of legal changes linked to the Bulgarian pre-accession strategy for membership in the European Union. In 2002, the Privatization and Post-Privatization Control Law (Post-Privatization Law) was approved, aimed at introducing more transparent and clearer rules for all participants in privatization, ensuring equality of treatment, and speeding up the process. Taking up this new direction, the main privatization methods would be open public tenders and public auctions at the Privatization Agency. The method of negotiations with potential buyers, much criticized, was abolished[4]. The law also strengthened post-privatization control through the setting up of the Agency for Post-Privatization Control. In 2003, the strategy changed in order to improve transparency and to speed up the process through a broader use of the Bulgarian Stock Exchange (BSE) through public tendering or public auctions. In this way, 78% of all the sales after the Post-Privatization Law was approved were made through the BSE. These changes meant the rapid acceleration of the privatization process and the predominant use of public auctions to achieve maximum prices for the assets sold. In this period, between 2001 and 2004, only 9.14% of the state assets to be privatized were privatized (Privatization Agency, 2006).

According to official data from the Bulgarian Privatization Agency, by August 2005 the total assets privatized amounted to 58.96% of state-owned assets and up to 89.29% of the state-owned assets up for privatization. Between 1993 and August 2005, stakes and shares of 5,222 companies were sold. Also, some 3,915 minority or residual packages unsold after the

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[2] See section 3.

[3] In March 2003, two district heating distributors were privatised. Majority stakes in the seven regional electricity distribution companies were privatised at the end of 2004, and three hydro-plants were sold also in May 2004, in the context of the privatisation of the energy sector. In February 2004, the privatisation of the Bulgarian Telecommunication Company was completed with the purchase by Alive Ventures (Austria) of 65% of shares for 230 million Euros. The other 35% was sold on the BSE in January 2005.

[4] Even before 2001, the MEBO privatisation methods and mass privatisation were abandoned. The Centre for Mass Privatisation closed in 2000.

initial privatization agreements were divested[5]. The state still keeps shares and stocks in 770 companies, including majority packages (more than 50%) in 62 and minority packages in the other 533 (Privatization Agency, 2005). At the beginning of 2005, the state tobacco monopoly (Bulgartabac) had yet to be privatized, in addition to the energy sector, the transport sector (Bulgarian River Shipping Company, Bulgarian Maritime Shipping Company and Bulgaria Air), some military-industry companies and the state's minority shares in enterprises already sold (Privatization Agency, 2006). There are also 113 companies which were excluded from being privatized, as stipulated in the Post-Privatization Law.

After the privatization of individual companies, few changes few changes have been made to their management. This has much to do with the influence of the traditional powers, such as unions, the political elite, and local communities that conserve considerable power to defend their own interests, often associated with the old management (World Bank, 2000). One of the deficiencies observed after the processes of privatization of the companies is the control of management by insiders (World Bank, 2004) and the limited role that foreign investors have played compared with other transition economies of Central Europe. However, the restructuring of the companies is advancing slowly and, in spite of the existence of many companies showing losses, the number of bankruptcies is insignificant. According to the EBRD's 2004 Sector Assessment Survey, the Bulgarian Insolvency Law is highly regarded and is one of the best regarded laws of its type among the transition economies (EBRD, 2005). However, a significant difference exists between the extensiveness of the legislation and its effective application. The number of bankruptcies has been reduced and the liquidation of companies can take several years. The number of insolvency proceedings opened in Bulgaria was 208 in 2004, relatively few compared to 7,519 in Hungary or 3,353 in Romania (COFACE, 2005).

### *1.2. Cash and mass privatization*

The Transformation and Privatization of State-Owned and Municipal-Owned Enterprises Law (Privatization Law) was adopted in 1992. The main objectives were to eliminate the chaos existing in the privatization process, to suppress spontaneous privatization and to achieve as many sale proceedings as possible. This law regulated the whole privatization process, defining the different organs and their responsibilities, the types of companies to be privatized, the terms of participation in preferential conditions, and the methods of valuation and sale. Any individual or legal entity where the state or the municipality did not possess more than 50% participation could participate in the privatization process. However, the law established preferential mechanisms of purchase for some lessees, employees and managers, and possessors of public debt titles. The preferential conditions included the possibility of paying 90% of the payment in instalments over ten years and benefiting from a 50% discount on the real interest rate. The preferences were applicable only when at least 20% of the state company's staff set up a special agreement.

The manager and employee buy-out (MEBO) system was introduced in 1994, constituting one of the principle ways of transferring state property in Bulgaria. The companies sold were small- and medium-sized and not very attractive. The prices were low and the purchases financed with credits guaranteed by the assets of the company and future

[5] According to the Bulgarian Privatisation Agency, a company is privatised if 51% of its assets are transferred. However, the IMF (1999) considers that the privatisation of state companies means the transfer of property from the state to the private sector, implying the transfer of the right to adopt strategic decisions, including the reduction of size, the liquidation of the company or the increase of capital. The IMF demands that the possibility of the state's blocking these kinds of decisions be eliminated. According to the Bulgarian Commercial Law of 1991, the owner of 33% of the shares of a company could block such decisions.

profits (World Bank, 2000). Also, the managers took control in most of the companies (Michailova, 1997; Alexandrova, 1999)[6]. The number of transactions involving foreign investors was not very high, but some of the biggest state companies were bought in this way[7].

The cash privatization process has been problematic. On one hand, privatization developed in a climate of constant political tensions, changes in government, modifications in the legal framework and numerous conflicts among the different agencies as to their corresponding responsibilities. The agents involved in the process, ministries, managers and employees of the companies, have shown resistance to losing their privileged positions. On the other hand, there weren't many really attractive companies; few of them were profitable, most of them were deeply in debt and very big.

The economic framework has changed completely compared to the old system, which was characterized by extensive growth and intra-CAEM trade. In the case of companies deeply in debt, sale was carried out at a very low price on the condition that the buyer assume the debts[8]. The unclear legal status of the companies aggravated the situation. Many documents concerning the legal ownership of assets and buildings were missing. In addition, the borders between state and municipal property were not clarified, generating conflicts between different administrative entities.

The slow progress of cash privatization motivated the adoption of a strategy for distribution of the state assets among the population. The first wave of mass privatization programs started in 1996. Each Bulgarian citizen older than 18 years had the right to buy a voucher for the price of 500 (old) leva that represented an investment value of 25,000 (old) leva. During the first phase the vouchers could only be used to buy shares in the companies that were explicitly offered in the programme. Every citizen in possession of such a voucher could participate directly in the process of acquisition of state company shares or indirectly through a privatization fund (Centre for Mass Privatization, 1995). During the first wave, 90.4 million shares of 1,050 state companies were offered. In total, vouchers representing about 16% of the long-term state assets were issued. By the end of the auctions, 76.4% of the shares offered initially had been transferred. Out of 6.5 million Bulgarians having the right to participate in the program, 3.5 million became shareholders. Only some 500,000 did so directly, while 3 million gave their vouchers to the privatization funds, which acquired almost all the offered shares (CSD, 1999).

For the second phase, beginning in July 1998, the government, with the support of the IMF, introduced some modifications, since the privatization funds were not contributing new capital for the restructuring of the companies (IMF, 1999). Legislative changes introduced the vouchers as a means of payment in a greater range of operations (e.g. company bids, repurchase operations by managers and employees of the company or pension funds). However, vouchers could not be transferred to a privatization fund. This restriction produced more modest results. In June 1999, only 976,000 people participated in the program, 15.2% of all eligible people. Accordingly, less than 60% of the offered shares were purchased (Miller and Petranov, 2000). In 2000, this privatization method was abandoned and the Centre for Mass Privatization was closed.

Through the Centre for Mass Privatization, 22% of the state assets to be privatized were privatized (Privatization Agency, 2005). However, with regard to the important larger

[6] The slowness of the restructuring processfor this type of company after the privatisation caused the World Bank to recommend the nationalisation of these assets (World Bank, 2000).

[7] Between 1993 and 2004 there were 163 privatisation agreements with foreign investors (Privatisation Agency, 2006).

[8] An example of this possibility was the privatisation of the company Kremikovtsi, the big metallurgy complex, which was sold for only one dollar.

companies, the programme offered only up to 33% of their assets, allowing the state to maintain control. The state lost control and its veto right on strategic decisions only in a third of all offered companies. The population did not show much interest in entering into ownership of a reduced part of the state company shares. The population lacked appropriate information on the companies and doubts existed as to the possibilities of obtaining benefits by participating in the programme. Despite the promises of the mass privatization programme, the companies on offer were not very attractive. A reduced number of privatization funds acquired almost all the transferred assets. Mass privatization involved the creation of only 81 privatization funds and the concentration of the vouchers in a reduced number of them; some 75% of the vouchers were distributed among the 18 principle funds (Miller and Petranov, 2000). The funds' strategy was to take control of the companies by buying more shares after the auctions (CSD, 1999). Almost 90% of the transactions were made in blocks of shares, purchased with the intention of creating share-holding majorities (Tchipev and Dragneva, 1999).

New relationships arose between the managers of the companies and the directors of the funds. Experience in other transition countries has shown that in mass privatization programs, shares are often transferred to the managers, this being the same as in the MEBO system (Andreff, 2005). While the directors of the funds allowed the managers to maintain their positions, the managers in turn provided the funds with insider information or employees' vouchers. The funds belonging to financial institutions and banks provided credits on privileged terms to their companies. However, the privatization funds contributed generally very little new capital for restructuring.

## 2. Privatisation of the Bulgarian Bank System

### *2.1. Slow reforms and crisis*

During the socialist period, the Bulgarian banking system was made up of the Bulgarian National Bank (which played the roles of central bank and commercial bank), the Bulgarian Foreign Trade Bank (for financing foreign trade) and the State Savings Bank (which specialized in collecting household deposits), according to the traditional pattern of planned economies' banking systems[9]. In 1987, a reform led to the creation of eight sector banks. The objective of the reform was the substitution of the monobank system by a two-tier banking system. However, this transformation took place later on, in 1989, when 59 commercial banks were authorized to operate as universal banks, that is to say, with a capacity to offer financing and to capture deposits of any business or individual. These banks were transformed into joint stock companies, and then a sale process to state enterprises and other banks began. Additionally, private entities were also authorized to acquire shares in a barely supervised process that was abandoned after one year. The opaqueness of this spontaneous privatization process was only increased by the possibility of transferring shares to other agents later on without any type of registration (Dilova-Kirkova, 1999). Private commercial banks were authorized in 1990, without the existence of a regulatory legal framework of banking activities or bankruptcy. This allowed the creation of banks by economic groups whose main objective was to obtain privileged financing (Tsantis, 1997). In fact, the number of private banks increased from 2 in 1990 to 81 in 1992.

[9] The financial system was dominated by banking before the beginning of the transition. Even now, the bank system represents more than 90% of total financial sector assets. This section analyses only the privatisation process in the bank system. The non-bank financial institutions are private-owned, especially since the privatisation of the former state insurance companies Bulstrad in 2000 and DZI (State Insurance Institute) in 2002.

In June 1991, a new law on the National Bank was issued. It redefined it's the Bank's functions and conceded considerable independence and the characteristic functions of a central bank in a market economy. The National Bank took charge of monetary policy design and the regulation and supervision of the banking system. Later on, in March 1992, the Banks and Credit Activities Law was passed, which defined the regulatory framework of the activities of banking institutions. The new regulation allowed the BNB to adopt a very flexible policy with regard to the concession of licenses to new banks. In this way, numerous banks were established with very low capitalization levels. In this period, in spite of its formal independence, the central bank could not resist political pressure on the design of monetary policy. This pressure made possible the expansion of the monetary supply through two channels: the financing of the budget deficit and the financing of state enterprises through bank credits, which the central bank supported by re-financing the commercial banks.

Although the central bank regulated the banking system, it had many difficulties in enforcing legislation. In fact, even though the central bank was able to concede opening licenses, it was not able to liquidate insolvent banks (Caporale et al., 2002). Another measure that stagnated was the creation of the Bank Consolidation Company (BCC), conceived as the institution in charge of consolidating, restructuring and privatizing state commercial banks. The few bank consolidations undertaken by the BCC were the creation of the Union of Bulgarian Banks at the end of 1992 through the merger of 22 small banks, and the creation of Expressbank through the union of 12 banks. Another example is the acquisition of Sofiabank by Biochim in 1995. Other attempts at consolidation carried out by the Bulgarian National Bank through the increase of capital minimum requirements brought no results (Caporale *et al.*, 2002). This was due in part to political pressure and to the opposition of the bank managers who feared losing their positions and privileges (Dilova-Kirkova, 1999).

At the end of 1995, there were 44 banks, almost all state-owned, with bad solvency ratios, insufficient capital and with a high percentage of unproductive assets. Around 65% of bank assets were state-owned. Some obstacles to the entrance of foreign banks explain why only 4 foreign banks existed, representing around 5% of the assets. The 7 bigger banks had a market quota of 75% of assets. Profitability/assets were very low, around 0.8%, and the capital/risk assets ratio was also limited, around 5% (Ulgenerk and Zlaoui, 2000). People's distrust in the banking system became patent at the beginning 1996, when the civil population began withdrawing deposits and a crisis erupted. A third of the commercial banks were declared bankrupt and closed (Balyozov, 1999). However, the slowness of the judicial processes delayed their liquidation (Barisitz, 2002).

### *2.2. The currency board and intensifying privatization*

In July 1997, a radical monetary reform, centred on the introduction of the currency board, was established. This reform was framed within a stabilization programme and buttressed by international assistance negotiated with the International Monetary Fund in April of the same year. The currency board meant the abandonment of an independent monetary policy. In fact, the central bank no longer carries out the functions of refinancing commercial banks, the public budget, developing exchange policy or directing open market operations[10]. In 1997, a new law on the National Bank was issued. The objective was to reinforce the control of the money supply and its regulation and supervision mechanisms. The

[10] This mechanism is composed of a set of rules foreseen to cover 100% of the reserve money with liquid foreign assets. An exchange rate anchored to a convertible foreign currency – originally the German mark (DM) and now the euro – was settled, with the central bank changing any quantity of leva against the reserve currency to the fixed rate (1,000 leva = 1 DM). A deposit created by the surplus foreign reserves on the monetary reserve allows the BNB to refinance the commercial banks in emergency cases (Nenovsky and Hristov, 2001).

new law established stricter demands on commercial banks with reference to minimum capital, liquidity and classification of assets.

The privatization of the state-owned banks began after the introduction of these changes. The entry of foreign capital into the banking system was especially stimulated. The first bank to be privatized was the United Bulgarian Bank (UBB), in 1997, followed by the First Investment Bank. A year later Post Bank was privatized and in the following years Expressbank and Hebros Bank were sold to different foreign investors (Barisitz, 2002). The sales of banks to foreigners was almost complete by 2000. The National Bank of Greece bought 90% of the UBB, which had already been privatized by a consortium of investors. Bulbank, the biggest bank in Bulgaria, was sold to Italian Unicredito, which bought a participation of 93% (Bonin, 2004). Later on, in 2003, the last two big banks, Biochim Bank and the State Savings Bank, were also privatized. In 2003 there were 35 banks, of which 25 were foreign-owned. Of the remaining ten only two small banks are not private-owned. They are Nasarchitelna Bank and the Municipal Bank of Sofia, and together they represent less than 3% of total bank assets. The system is supported by a solid legal and supervisory framework and the existence of a nucleus of well capitalized big banks with high liquidity, mostly foreign-owned, that represent 75% of the assets, deposits and capital of the bank sector (BNB, 2004).

It should be noted that the banking system constitutes the largest part of the financial system. Other institutions represent less than 10% of total financial sector assets, and the development of the stock market has been very poor (IMF, 2004). In this context, financial intermediation comes from the credit activity of the banking system. In the first half of the transition, until 1997, only a limited share of domestic credit was dedicated to the private sector. Since then, the private sector has been absorbing most of the financing needs, although the volume of total credit is low[11] (CED, 2005).

## 3. Land Privatisation in Bulgaria

### *3.1. The process*

The structure of land ownership inherited from socialism was characterized by the domination of collective farms. At the beginning of the transition, only 678 big collective farms existed, although they occupied almost 60% of all arable land. There were 196 state farms occupying almost 9% of the total surface area. Adding the working brigades, another form of public management of land, state (public) control of land at the beginning of the transition represented more than 80% (NSI). During the socialist period, there was no private land ownership. However, personal plots existed on which only private rights of use were granted, not full ownership rights. The number of personal farm structures reached 1,600,000 and they occupied 13.1% of the total area. They were very small plots with an average area of 0.4 ha (NSI). Members of cooperatives and state farm workers cultivated these plots mainly for self-consumption. Their participation in the total agrarian production was very significant, around 33%, especially in the production of fruits, vegetables, and eggs (NSI).

The central elements of land privatization in Bulgaria have been the restitution of land and the liquidation of collective farms[12]. The Law on Ownership and Use of Agrarian Land (Land Law) of February 1991 is the principle law that regulates land reform and was

[11] From 2003 onwards, the credit growth rate has been rising fast, especially consumer and mortgage credit.
[12] This section only analyses land reform with respect to agricultural land, leaving aside the study of the privatisation of industrial land and forests. On the privatisation of the forests in Bulgaria, see Cellarius (2004).

approved by the government of the Socialist Party[13]. The law established restitution as the mechanism for the privatization of land. According to this law, those who had been owners in the 1940s, prior to the collectivization, were entitled to receive land in the same quantity and quality as the land they had surrendered to the collective farms. The law included diverse restrictions on the full enjoyment of private ownership rights[14] (Land Law). Also in 1991 the Cooperatives Law was passed. This law allowed the transformation of the collective farms into new cooperatives, thereby avoiding their dissolution. Accordingly, cooperatives would be forced to pay rent and dividends to their members (Cooperatives Law).

After the arrival in power of the anticommunist coalition, the Union of Democratic Forces, the Land Law suffered its first modification in April 1992 in an attempt to radicalize land reform[15]. The restitution of land to those who had been owners, or their heirs, at the time that the Agrarian Reform Law of 1946[16] came into force, would now be made in real or historical terms and not in representative terms; that is to say, if the property existed or if it could be re-established at its previous limits, the restitution would consist of the delivery of that actual property. In these cases, the size, category, location and limits of the property had to be clearly specified. This requirement sought to impede the perpetuation of the old collective farms. The old farm would be divided into parcelled properties and only then could the new owners form a new cooperative (Dobreva and Kozhouharova, 1994). If the land was not returnable in real or historical terms, new comparable lands would be restored in quantity and quality, based on a land reassignment plan (Land Law). In the end, this has been the dominant method. The land reassignment plans have been developed according to the consolidation principle. That is to say, the owners receive consolidated land in order to avoid, insofar as is possible, land fragmentation, and to facilitate its cultivation.

Access to land was initially limited with respect to the maximum surface area of new properties[17], a limit which was removed in 1997, and with respect to the possibility of access to land ownership by foreigners. The restrictions on land ownership by foreign citizens have been decreasing with regard to the original text of the Land Law of 1991. At that time foreigners could only acquire land through inheritance or restitution, and even then they had to transfer it to a non-foreign owner within a three-year period, in accordance with Article 22 of the Bulgarian Constitution of 1991. Beginning in 1998, foreign legal entities registered in Bulgaria could acquire agricultural land. Finally, following the EU entry conditions, on 16 February 2005 the National Assembly approved a modification to the Constitution that would allow land purchases by foreigners without limitation. This amendment was made in March, although a transition period for its application until 2014 has been established.

The restitution scheme for reassignment has been a slow process. First, rights of ownership were granted in the abstract, that is to say, the right to possess land of a certain area and category was formally recognized before restitution took effect. The sub-division plan of the land for assisting the restitution by reassignment required the development of a new

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[13] The first laws dedicated to land reform were two ordinances that appeared in 1989 authorizing a certain decentralization of agrarian production. Ordinance 922 granted to individuals the right to rent collective farmland for private use. Starting from this point, some of these individuals organized more or less informal cooperatives. The ordinance also allowed the registration of new cooperatives as new legal entities (Dobreva and Kozhouharova, 1994). On the other hand, Ordinance 56 allowed the establishment of commercial companies and individuals of a private character, both in agriculture and in the whole of the economy. Both ordinances helped to create new agrarian structures outside the control of the state.

[14] For example, foreigners or companies with foreign partners could not own land.

[15] After this change, the Land Law was amended several times. The latest changes refer to the development of land transactions and the development of the land market.

[16] This reform consisted of the allotment of the land into small plots and it meant the confiscation of the properties of the Church and of the rich peasants, as well as of those lands not being cultivated.

[17] During practically the whole restitution process, the maximum area that each new owner could possess was 20 ha, or 30 Ha in the region of Dobrudza, that is to say, inside the limits set by the Agrarian Reform Law of 1946.

cadastre. Next, a sketch of each parcel had to be prepared by the Municipal Agrarian Commission and given to the new owner. After that, a notary sent a title deed for the property and, finally, the Agrarian Commission issued the permanent title to the property (Howe, 1998).

The Land Law contemplated the liquidation of collective farms and other similarly structured organizations, including the new cooperatives created after Ordinances 922 and 56 and the Cooperatives Law of 1991. The objective was to avoid the perpetuation of these types of organizations in the Bulgarian countryside. Assets were distributed between the landowners and workers in the form of land and other assets, according to their contribution, although in many cases the owners received devaluated monetary compensation. In 1999 a new Cooperatives Law was adopted, according to which cooperatives cannot acquire land for free, having to buy or lease it.

### *3.2. Outcomes*

In spite of many difficulties (Miller, 2003), the restitution process has now been concluded. According to the official data, in December 2000, 99% of land subject to restitution had been delivered back to its owners, who had received a state title equivalent to a final title deed. Only a quarter of this land was restored in real terms (NSI). Although information on the new agrarian structures is imperfect due to the informal character of many of them, it is certain that private ownership has become the new dominant form and that it represents 81% of total agricultural land, 96% of all arable land. Some 8.7 million plots exist in total and 5.1 million citizens, or 65% of the Bulgarian population, are landowners (Kopeva, 2003). According to data of the Bulgarian office of the United Nation Development Program, 1.5 million families cultivate land, that is to say, half of all Bulgarian families (UNDP, 2004).

According to official data from the *Agricultural Census in Bulgaria 2003* of the Ministry of Agriculture, 40.2% of utilized agricultural land has been grouped into new cooperatives (MAF, 2004). In spite of the liquidation of collective farms, cooperativism in the Bulgarian countryside has not disappeared; rather, it has developed under a new form. Several reasons exist to explain this phenomenon, including psychological explanations such as risk aversion in a climate of economic uncertainty, or cultural explanations, such as the habit of collectivism in Bulgaria. Additionally, the difficulties associated with the individual cultivation of land are diverse; many new owners lack knowledge, experience, economic resources and the necessary machinery. Under these conditions, and facing difficulties in selling or renting their land, many new owners give their land to a cooperative in exchange for some type of rent. Also, the new cooperatives benefit from the possibility of using the former political networks and the traditional forms of organization (Meurs and Begg, 1998). A large proportion of cooperatives organize their production structure based on the needs of the members, such as personal consumption, food for livestock, mechanization services for personal farms, warehouses, bakeries, etc. The remainder orients its production in accordance with market conditions and seeks to obtain revenues in order to undertake further investment (OECD, 2000).

The second type of private agrarian structure is the individual farm. Such farms represent 42.9% of the utilized agricultural area. More concretely, individuals have 30.2% of the land and sole traders have 11.7% (MAF, 2004). Almost all of the individual properties are very small farms of less than 1 Ha where the land is cultivated with the objective of providing products for self-consumption and, if possible, to provide some additional income. The expansion of farming for self-consumption constitutes a guarantee of survival for those low-income families facing the lack of alternative forms of employment or income in other sectors (Kostov and Lingard, 2004; Mathijs and Noev, 2004).

As well as privatization, land reform has caused land fragmentation. Fragmentation means the division of land into properties of reduced size, the existence of several holders sharing the same ownership rights and the division of properties into diverse and non-contiguous plots. According to the *Agricultural Census*, 78% of farms have an area smaller than 1 Ha (MAF, 2005). With regard to the fragmentation of ownership rights, although the total number of restitution applications was 1.7 million, the current number of owners, some 5.1 million, is much larger due to the multiplicity of heirs. Finally, as to the subdivision, there are now around 8.7 million plots. Land fragmentation is one of the main causes of the underdevelopment of the land market (Swinnen and Vranken, 2005). The objective of the Ministry of Agriculture is to impel the process of land consolidation. Currently the government is working on the development of land consolidation through the creation of a National Land Company that would take charge of buying and selling land. The growth of farm structures devoted to self-consumption could limit the success of this process.

## Conclusions

Privatization in Bulgaria has almost come to an end. The majority of wealth generated in the country now comes from the private sector. In the industrial sector, the sales of minority state shares in some small and medium private enterprises, one large state holding (Bulgartabac), and the privatization of infrastructure branches (energy, electricity production, and water supply) are still to be finalized. In the financial sector, practically all banks and other financial companies are privately owned. Finally, after the restitution process, arable land is also in private hands.

Following a brief analysis of the privatization process in Bulgaria, its major features can be outlined as follows. Privatization of the Bulgarian economy has been a slow and difficult process. The privatization of state assets implies a process of redistribution of wealth and economic power that has caused the mobilization of different social groups which have tried to maintain or improve their positions. An analysis of Bulgarian privatization shows the failure to remould old structures and economic groups; for example, the managers and employees or some privatization funds acquired the control of the companies. On many occasions, the old directors have been able to maintain their position in privatized companies. In agriculture, after the liquidation of the old cooperatives and the restitution of the agrarian land, new cooperative structures have developed.

The nature of the economic structures inherited from the socialist period has limited the possibilities of privatization. Companies were not profitable, needing a thorough restructuring to make them so. Under these conditions, many of the state assets have been distributed to the population, either for free (through land restitution and mass privatization) or under very favourable conditions (through the MEBO sales). At the same time, the real development privatization, especially in the financial sector, has taken place through the entry of foreign capital.

Summing up, privatization of the economy is no guarantee of the development of a market economy. In the case of the land, privatization has generated the development toward farms for exclusive self-consumption. The financial system is concentrated in banking, with little credit activity and a very underdeveloped stock market. In the industrial sector, in spite of privatization, restructuring of companies is very limited and although many are unprofitable, there are very few bankruptcy cases.

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## AR PRIVATIZACIJOS INICIJAVIMAS LEMIA RINKOS EKONOMIKOS KŪRIMĄ? BULGARIJOS PATIRTIS

**Raúl de Arriba Bueno**

**SANTRAUKA**

Perėjimas nuo planinės ekonomikos prie rinkos ekonomikos reiškia sistemos transformaciją, kurioje valstybės turto privatizavimas sudaro centrinę proceso dalį. 15 metų po pereinamojo laikotarpio pradžios privatizacijos procesas iš esmės pasibaigė. Šis straipsnis siekia apžvelgti visos ekonomikos privatizaciją, tai yra, valstybės turto, jos finansinės bei nefinansinės ekonominės veiklos ir žemės privatizaciją kaip visumos transformaciją.

Privatizacija čia suprantama kaip turto ir ekonominės galios perskirstymo procesas, sukėlęs įvairių socialinių grupių, siekusių išlaikyti ar pagerinti savo padėtį, mobilizaciją. Bulgarijos privatizacijos analizė atskleidžia nesėkmes performuojant senąsias struktūras ir ekonomines grupuotes.

Apibendrinus, privatizacija Bulgarijoje neužtikrina rinkos ekonomikos raidos. Žemės grąžinimo klausimas ir jos privatizacija sukėlė ūkių, apsiribojančių savo produkcijos vartojimu, susiformavimą. Finansinė sistema yra koncentruota bankininkystėje, kreditinė veikla nežymi, o akcijų rinka itin neišsivysčiusi. Pramonės sektoriaus kompanijų restruktūrizacija labai ribota, ir nors daugelis jų nėra pelningos, bankroto atvejai labai reti.

*REIKŠMINIAI ŽODŽIAI:* privatizacija, ekonomikos transformacijos, ekonomikos politika, struktūrinės reformos, Bulgarija.