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The Political Economy of Corporate Governance Change in Bulgaria: Washington Consensus, Primitive Accumulation of Capital, and Catching-Up in the 1990

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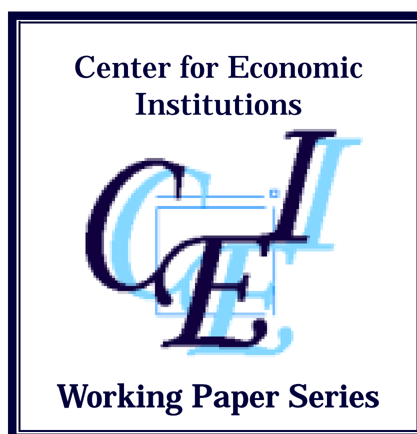

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The Political Economy of Corporate Governance Change in Bulgaria: Washington Consensus, Primitive Accumulation of Capital, and Catching-Up in the 1990*

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Abstract

This study examines three key determinants of corporate governance change in Bulgaria: the Washington Consensus policy, primitive accumulation of capital forces, and 'catching-up' factors. The study reveals that in the early transition (1989-96) primitive capital accumulation prevailed over the Washington Consensus impact on corporate governance transformation while since 1997 Washington Consensus has been in the process of becoming the decisive factor for institutional change. The emerging corporate governance system has been neither Anglo-American (market based) nor bank-based, but rather a 'crony' relationship-based one. The striking features of this system are as follows: (i) a dual enterprise sector, (ii) ownership heterogeneity; (iii) fragile capital markets; (iv) pervasive banks lending behavior; (v) globalization factors discretion. The challenge to policy-makers in Bulgaria is how to design institutions for 'catching-up' that would curb both managerial and globalization factors discretion.

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I. Introduction

In the 1990s, a policy approach known as the Washington Consensus gave rise to mediocre results in countries like Bulgaria, Croatia, Estonia, Latvia, Lithuania, Slovak Republic, Russia, other former Soviet Union states, and mixed results in all the European post-communist countries (***Table 1***).[1] The transition recession observed was comparable to the Great Depression, and for most of the transition countries it was even much worse. In 2000, real GDP was below its level at the beginning of transition for most of the countries.[2]

In the early 1990s, according to the Washington Consensus policy, the basic corporate governance issues in transition were: (i) separation of ownership and control between small shareholders and top managers; (ii) the inefficient role of the state both as owner of public enterprises and as regulator of economic activities; (iii) inefficient socialist state ownership and 'totalitarian' state. This 'conventional wisdom' was mainly based on the Anglo-American contemporary theory and practice (refer to Bearle and Means's seminal book published in 1932) and neo-conservative tendencies in the U.S. and the U.K. in the 1980s, regarding the economic role of the state and the communist economic system itself.

Respectively, the main remedies for the poor enterprise performance in transition economies were: (i) introduction of the entrepreneurial spirit of capitalism through establishment of new private firms; (ii) reduction of the role of the state through privatisation and deregulation; (iii) establishment of more efficient ownership and control structures based on concentrated ownership, outsiders control and foreign investors participation (Frydman and Rapaczynski, 1993; EBRD, 1995; World Bank, 1996). However, at the end of the decade, these 'good ideas' were to be reconsidered.

First, there is a wealth of literature on the effects of ownership and control structures on firm performance in transition economies. However, the results of empirical studies are mixed concerning any significant difference in performance of *state and privatised firms*. (See for a survey of the literature, Nellis (1999), Bevan *et all* (1999).

Second, many studies support the hypotheses that *newly established private firms* are more efficient than both state and privatised firms (for a survey, see Bilsen and Konnings, 1998). However, these studies using the conventional state-private firms dichotomy cannot explain the basic difference between newly established 'crony' private firms, on the one hand, and independent private firms, on the other hand. There is no simple correlation between *private sector* share and either national economic performance or progress in transition (S.Estrin, 2001).

Third, there is also no significant evidence that *insiders-controlled* firms underperform *outsiders-controlled* firms. (Among recent studies, see Jones and Mygind (1999) for the Baltic States, Peev et al. (1999) for Bulgaria, Romania and Albania, Djankov (1999) for Georgia and Moldova).

Fourth, contrary to the Washington Consensus expectations in the early transition, when 'insiders' and 'the state' were described as key enemies of the economic reform, typical outcomes of this policy in many countries were backstairs 'outsiders' control by interest groups and weak state (Olson, 1995; see also, Koford (2000) for the Bulgarian case).

Fifth, attempts for a deeper understanding of *evolving* ownership structures and output in transition are based on studies of the U-shape of industrial output. A number of papers explain the decline in output with supply side distortions, as disorganization in historical links of production (Blanchard, 1997), labour market frictions (Atkeson and Kehoe (1996), credit constraints Marin and Schnitzer, 1999), and demand shocks (Repkin and Walsh, 1999). In Bulgaria, for instance, after the fall in GDP during 1990-93 (1991: -11.7%, 1992: -7.3%, 1993: -1.5%), there followed a recovery in 1994-95 (1994: +1.8%, 1995: +2.1%). However, the optimistic visions about 1996 and the following years proved unrealistic (EBRD, 1995). In 1996, GDP fell sharply by 10.9%. A similar, *second* sharp fall in GDP since the beginning of the transition was also observed in Romania, Albania, and less so in the Czech Republic. The optimistic theoretical expectations underestimated fundamental reasons for further instability that were still existing and worsening, namely the emerging "crony" relationship-based corporate governance system.

[1] **For a recent overview of transition countries (under)development, see World Bank (2002).**

[2] For strong critical views regarding the Washington Consensus policy, see Gore (2001) on its methodological failures; Kornai (2001) on transition countries; Taylor (1992) on developing countries; and Cross and Strachan (2001) focusing on its theoretical framework failures; for moderate critical views, see for example, Stiglitz (1998); Srinivasan, (2000); and for 'left'- based critique, see for example, Panitch,2000.

The purpose of this paper is to examine the specific factors determining corporate governance change in transition and outline the key features of ownership, control and governance transformation. The paper focuses on the corporate governance transformation in Bulgaria, but by extension the results can explain post-communist corporate governance design in general. The study reveals that in the early transition (1989-96) primitive capital accumulation prevailed over the Washington Consensus impact on corporate governance change while since 1997 Washington Consensus has been in the process of becoming the decisive factor for this transformation. The emerging corporate governance system in Bulgaria has been neither Anglo-American (market-based) nor bank-based. The policy outcome has been rather a **'crony' relationship-based** corporate governance system. The striking features of this system are as follows: (i) a dual enterprise sector, (ii) ownership heterogeneity; (iii) fragile capital markets; (iv) pervasive banks lending behaviour; (v) globalisation factors discretion.

Section 2 presents the framework of the study focusing on key factors for corporate governance change in post-communist countries: globalisation, post-communist primitive accumulation of capital, and 'catching-up' accumulation of capital. Section 3 discusses corporate governance transformation in Bulgaria in the 1990s. Section 4 briefly analyses historical experience of developed market economies and corporate governance design in Bulgaria. Section 5 focuses on the 'catching-up' stage of development and corporate governance change in Bulgaria. Section 6 analyses Washington Consensus policy failures in the field of corporate governance. Section 7 concludes.

II. Framework of Study: Globalisation, Transition, "Catching-Up" and Corporate Governance Change

The fundamental unanswered question of the Bulgarian economic policy during transition has been which kind of corporate governance and corporate finance system has to be developed under the *Bulgarian* conditions – a 'bank-based' system (like Germany and Japan), a 'market-based' (the Anglo-American model), an 'implicit rules-based' (like Italy), a 'mixture of a capital market-based system and a bank-based system'(Dutch case) or a unique 'Bulgarian' system.[3] This theme leads to the big issue of the methods of studying separation of ownership from control in *post-communist* countries.

Corporate governance can be defined as the design of institutions that constrain potential managerial opportunism and discretionary behaviour, and compel managers to pursue strategies that are in shareholders' (stakeholders') best interests.[4] In the post-communist transition context, it includes design of property-rights transformation (corporatization, privatisation, new private firms establishment), legal, regulatory and institutional framework for business activities (especially, capital markets, a bank sector). Two basic approaches to studying these issues can be outlined. First, the conventional approach to separation of ownership and control, stressing (i) different *elements* of the corporate governance system, e.g. managerial ownership, board of directors, CEO compensations, etc. (internal ones), and market for corporate control, capital and managerial labour markets, etc. (external ones); (ii) ownership structures and types of control and their impact on firm performance and discretionary managerial behaviour (for a summary of literature, see Peev, 1995). This approach is based on a narrow understanding of both corporate governance issues in general and agency issues between top-managers and small shareholders in particular.

The second approach is partly based on some recent developments, like some unsuccessful post-privatisation stories in many transition countries in the 1990s (for a survey, see Nellis,1999), a weak state and 'state capture' observed (EBRD,1999), financial crises in some transitional economies, e.g. Russia in 1998 (Black *et all*, 1999), Bulgaria in 1996 (Koford, 2000), convergence trends in the Continental Europe and Japan to Anglo-American models in the 1990s, and the East-Asian crisis in 1997. Recent studies on corporate governance in different countries concluded that a concentrated ownership rather than a dispersed one is a more typical feature of the finance systems of countries outside the Anglo-American world (see La Porta *et all*, 1998). Expropriation of small shareholders has been observed in both developed and

[3] For a discussion about the financial system choice at early transition, see McKinnon (1991); Szego (1993); see also, Hermes and Lensink (2000) for survey of discussions on the financial system in Eastern Europe; for description of basic issues of the modern financial system, see Thakor (1996), Allen and Gale (2000) and see also, Odagiri (1992) for management and competition aspects of corporate governance; Dietl (1998) for a comparison of neoclassical and relational financial regulations.

[4] Some recent studies focus on the welfare of stakeholders (employees, suppliers, costumers, creditors, etc.), see, for example, Tirole (2000).

developing countries (especially after the East Asian crisis) and key agency issues have been reconsidered focusing also on large and small shareholders relationships, and 'crony' business links. Capital markets have been seen as a more efficient information device and in many European countries, processes of convergence to Anglo-American models have began (Coffee, 2000).

This broader approach is focused on (i) legal and regulatory framework of the corporate governance *system*, law enforcement, security of property and creditor rights (for transition economies, see Berglof and Thadden, 1999; for general analysis, see La Porta, *et all,* (1997,98,99); company *stakeholders* (for transition economies in general, see Mygind, 1999; see also Buck *et all*, 1998 (applying stakeholder-agency theory) and Fox and Heller, 1999 (applying transaction costs economics) on Russia; for property-rights approach, see Alchian and Demsetz, 1972); (ii) *economic environment* dimensions of corporate governance, especially country governance, corruption, 'crony' relations, 'captor' relations between firms and state, shadow economy, (see, for example articles at the World Bank site: www.worldbank.org/research/governance/corruption); see also, the bulk of articles on 'crony' capitalism after the East Asian crisis (for example, Rajan and Zingales, 1999).

In transition economies the *conventional* approach to corporate governance structures and their effects on performance encounters some difficulties in explaining the real business behaviour. Regarding Bulgaria, empirical studies have revealed that ownership concentration or dispersion, insiders or outsiders types of control, establishment of boards of directors and other governance mechanisms, or their absence, are not a reliable institutional basis for forecasts of business behaviour in the specific transitional environment (Peev, 2001).

This study has applied the second broader approach on corporate governance issues in post-communist transition. The subject of study is (i) ownership and control structures transformation, capital markets emergence and banking sector transformation in Bulgaria during 1989-2001; (ii) factors for the corporate governance change observed. The analysis is built on findings of author's empirical studies of corporatization and privatisation in the Bulgarian economy.[5] It also has applied results of some recent critical studies about (i) the *Washington Consensus* policy in post-communist countries (described in the previous section); (ii) studies on *'state capture'* (see, Hellman *et all*, 2000) and studies on *primitive* accumulation of capital (after Kornai's notion about vulgar Marxism and vulgar Coase-ism (Kornai, 2001), see, for example, Marx's Capital, vol. I, ch.7); (iii) studies on political economy of corporate governance *evolution* (historical development of corporate governance (see, for example, Coffee, 2000); institutional change of property-rights (Wiesner, 2001); (iv) studies on '*catching-up'* and corporate governance in transition (Morck and Yeung, 2001); etc. The study has also applied some recent findings about specific coalitions for collective actions in transition (see, Wedel (2001) for Russia; see also, the excellent latest book by Olson (2000) for a more general discussion).

The key hypothesis is that the basic factors *practically* shaping corporate governance design in post-communist countries in the 1990s were as follows: globalisation (the Washington Consensus policy, convergence to Anglo-American models, the EU enlargement), transition (post-communist primitive accumulation of capital, law voluntarism, post-communist informal rules), catching-up factors (transfer of knowledge about historical experience of developed market economies in the field of corporate governance, the catching-up stage of development of the particular country, the 'catching-up' accumulation of capital, etc.). The logic of corporate governance transformation in different transition countries can be seen in the specific power distribution among foreign actors (like the IMF), emerging international coalitions for collective action, coalitions for primitive accumulation of capital and capital flight, coalitions for catching-up accumulation of capital and national development.

The detailed investigation of all the factors described above is beyond the scope of this study. It focuses mainly on (i) the Washington Consensus policy; (ii) post-communist primitive accumulation of capital; (iii) the historical experience of developed market economies in the field of corporate governance; (iv) 'catching-up' accumulation of capital.

A. Globalisation and Corporate Governance

[5] For empirical study of ownership and control transformation in Bulgaria, see Peev (1995), Peev and Hare (1995) on corporatization; Peev *et all* (1999), Peev and Simmons (2000) on privatized and newly established private firms; see also for a brief summary, Peev (2001).

The Washington Consensus policy has been the dominant approach to development since the early 1980s.[6] This approach was initially adapted to developing countries and since communism collapse it became 'conventional wisdom' to policy reform in transition countries (see World Bank, 1991; 1996; EBRD, 1995). This approach is characterized by focusing the government attention on three main domains: (i) privatisation and deregulation, (ii) macrostabilization by low inflation and fiscal deficits, (iii) liberalization through opening of economy to the rest of the world, and a domestic prices control release. This is a top-down approach, driven by the IMF and the World Bank stabilization and structural adjustment policies and loans conditionality and based on the leading role of foreign advisers. The underlying idea of Washington Consensus policies is a shift from state-led policies to market-oriented ones. This has reflected some neo-conservative tendencies in the US and the UK in the early 80s but has also served the transition "from plan to market" in the 90s. The specific policy prescriptions are presented below (see for a detailed analysis Gore, 1996; Taylor, 1992).

First, the *national government* has to have a circumscribed role and norms of liberal international economic order like free markets, private ownership and private owner's incentives could play a decisive role. Countries adapting their policies to these norms would receive better outcomes measured by GDP growth and other country performance indicators. According to this policy, the national interest is identified by increasing economic growth and personal income welfare but such development issues, as national unity, national identification and sovereignty are not important. Countries trying to carry out policies conflicting with liberal international norms, such as an active industrial policy protecting selected industries, have been shown as examples of governments acting against their national interests. Domestic policy-makers have been selected for potential leaders on the narrow base of their loyalty to the Washington Consensus policy tenets (for the case of Russia, see Wedel, 2001). Second, the *normative frame* of reference of the policy described above was international, global, but its *explanatory frame* was local, national. Thus, the methodological approach to transition countries can be described as "methodological nationalism" (Gore, 1996). Factors contributing to the national (under) development are divided into internal (national) and external (international), the national factors being described as the most important to explain the economic situation in a particular country. The country performance (the basic subject of study) is attributed mainly to the domestic policy (World Bank, 1997). In fact, the official slogan of "transition to a free market economy" serves globalisation norms. However, according to the Washington Consensus policy approach, globalisation factors are "external" and not on the research agenda, and only domestic (internal) factors are decisive for the country performance. Third, a salient feature of this approach is the excluding of such issues as capital accumulation and human capital development from the policy agenda of transition.

Some key features of the ownership and control design in transition based on the Washington Consensus approach are as follows. First, i*nvestor relations.* The main assumption is that the origin of capital of new investors was not significant (no specific disclosure rules were required). Enterprise property-rights transformation is based on two key tools: a) 'corporatisation'(establishment of companies with a hundred percent state participation) and b) increasing the share of the private sector in the economy through privatisation of former socialist state-owned firms and entry of newly established private firms. (During 1990-99, about three quarters of the U.S. aid to Central and Eastern European countries fell under economic restructuring, including privatisation and private sector development. This was also a priority of the EU assistance to Central and Eastern Europe (Wedel, 2001).

Second, *ownership structures.* It is taken for axiom that new private owners would be firm value-maximizers. The main hypothesis is that *state-owned firms would perform less efficiently than private firms (property-rights hypothesis).* The foremost task is rapid liquidation of the state sector through accelerated privatisation. The expectations are that privatisation will automatically harden the budget constraints (Kornai, 2000). Four basic types of firms by ownership structure are observed in transition conditions: traditional state-owned enterprises (SOE) and corporatized state-owned enterprises (CE) in the state sector, privatised enterprises (PRE) and private enterprises established *de novo* (POE) in the private sector. The basic assumptions are that **s**tate firms (SOE and CE) would be less efficient than privatised firms (PRE), and privatised firms would be less efficient than private firms established de novo (POE). In fact, the number of the privatised firms served as a key indicator for reform development in a given country. According to the fulfilment of the 'plan' for privatisation, a transition country could receive further aid or face reduction. (For example, with regard to U.S. assistance to transition countries, foreign consultants

[6] For the term 'Washington Consensus', see articles by the term inventor John Williamson (1990, 1993, 2000).

were sent to the country's bodies for privatisation to accelerate the privatisation process (for the case of Russia, Hungary, Poland, Ukraine, see Wedel, 2001).

Third, *control types.* The main hypothesis about control types in the private sector is that interests of managers and owners diverge and *management-controlled firms would be less efficient than owner-controlled firms (Berle-Means thesis).* In the transition economies, the dichotomy of insiders-controlled and outsiders-controlled firms is used as a basic distinction. In the group of insiders, managers-controlled and workers-controlled firms are observed. In the outsiders-controlled group - domestic investor controlled-firms and firms under foreign investor control. Basic assumptions about firm performance by control types are that *insiders-controlled firms would be less efficient than outsiders-controlled firms, workers-controlled firms would be less efficient than managers-controlled firms, and domestic investor-controlled firms would be less efficient than foreign investor-controlled firms* (see, for example, EBRD,1995).

Fourth, *governance mechanisms.* Assumptions regarding the emerging governance mechanisms are as follows. New private owners with their inherent private ownership motivation would create new market-oriented *implicit rules* of the game. New private owners would have discretion to establish efficient *internal* governance structures (board of directors, CEO compensations, managerial ownership). *External* mechanisms (managerial labour markets, capital markets, market for corporate control) would be inefficient in the early transition and would be developed gradually. Bank control would be established by the emergence of many banks in order to compete with one another in corporate finance. Government control must be passive. A withdrawal of the state from state-owned companies would be necessary, as well as establishing of board of directors' institution in corporatized companies with a hundred percent state participation.

B. Historical Experience of Developed Countries and Corporate Governance Design

The Washington Consensus policy to transition economies was also stimulated by some trends to convergence with Anglo-American models in the 1990s. However, in post-communist countries, where the system *transformation* is the most important characteristic, the historical approach to corporate governance evolution is more reliable than adherence to some *contemporary* tendencies. The historical experience of developed countries, like U.S. in the last quarter of the 19th century and the Japanese pre-war and post-war transformation, can suggest better starting points for corporate governance design in transition economies (see, for example, Herman (1981) for evolution of separation of ownership and control in the US in 1990-74; for some recent studies, see Coffee (2000) for corporate governance genesis in the U.K. and the U.S.; see Okazaki (1999); Odagiri and Goto (1996); Kitamura *et all* (2001) for the Japanese historical experience; Nishimura (1999) for the impact of initial conditions in transition economies).

C. Post-communist Primitive Accumulation of Capital and Corporate Governance

The above described Washington Consensus approach to corporate governance in transition countries is rooted in the basic assumptions of the general policy frame explaining the transition process itself: (i) Bearle-Means thesis about separation of ownership and control is relevant in transition as could be in any market economy, (ii) a law reform would trigger efficient corporate governance, (iii) transition is an ordinary economic process, (iv) private owners in transition countries would behave like owners in any developed market economy (see, for example, EBRD Transition Report,1995; World Bank Report, 1996). This frame can explain why such issues as the genesis of the transition process, the driving forces staying beyond it, globalisation factors in the 90s, were not found on the corporate governance research agenda, at least before the Russian financial crisis in 1998.

*The origin of capital matters***.** When Bearle and Means wrote their seminal book on separation of ownership and control in the modern American corporation in 1932, they had taken for granted that somebody (saver, potential investor) had collected money through some means. The sources of this potential capital were not an issue to be studied.[7] Traditionally, corporate governance literature makes a difference between different sources of corporate finance like equity and debt financing (see for example, Jensen and Meakling, 1976). However, using the same traditional approach to corporate governance and finance in post-communist countries is fruitless. The origin of private capital does matter in a transition environment. In developed market economies, private investors and companies have had a long term of

[7] Problems of the so-called "primitive accumulation of capital" are usually studied by Marxists.

existence. In the case of transition countries, however, domestic private investors and companies *have to be created*. The magical word "privatisation" cannot explain how domestic (not foreign) private capital could be collected. For example, in the U.S. at the last quarter of 19th century, when the American corporate governance system was established, a chain connecting issuers and capital seekers (mainly railways at that time), financial intermediaries (investment bankers like Morgan) and investors (mainly foreign ones) determined the real economic structure staying behind corporate governance design. According to the Washington Consensus approach to corporate governance design in transition countries, this chain could be imitated by state-owned firms that have to be privatised as capital seekers, the state (agency for privatisation) as the intermediary, and investors (mainly foreign ones). But this remains only an imitation. In transition countries, the real economic structure had quite a different form. *The real seekers for capital were not state-owned firms but rather emerging private firms and the crucial question was where finance could come from*. In transition countries, two basic sources of "primitive" post-communist accumulation of private capital can be outlined: foreign (private debt and equity, government external debt, foreign aid) and domestic ones (state budget, state-owned banks and firms). However, the financial intermediary role has been served not by investment bankers but rather by the state institutions. In the early transition, corporate governance was designed by political class to transfer capital mainly from state sources to private hands (for the case of Bulgaria, see OECD,97; 99; Koford, 2001.) This process was described by specific terms like assets stripping, looting, tunnelling (for the Czech case), *prixvatizazija* (for privatisation in Russia), *spontaneous* privatisation (in Hungary), *collusion* privatisation or *mass fraud* (for mass privatisation) and *hijackers-swindlers* privatisation (for MEBO schemes in Bulgaria). In many cases, the term "privatisation" has been misleading because it explains only the primitive accumulation of capital. Theoretically, this is a process of accumulation of capital that is not based on production and profit distribution, but rather on wealth redistribution through outright theft, war, revolution, etc. *But if the process of primitive accumulation of capital was natural and typical of all the capitalist nations at their early stages of development (according to Marx) this process per se cannot lead to such disastrous effects like the ones in Russia and other transition countries.*

Law voluntarism and capital flight. Another important feature of the transition process is that the policy was based on the belief that laws can be efficiently transplanted from developed economies into transition ones. In the early transition years, attempts to introduce market-based legislation produced unexpected specific results. High corruption, weak legislation protecting investors and weak law enforcement have been basic features of legal environment in many transition countries. Lack of property rights security for both small and large shareholders, and private business in general, and danger from expropriation after the primitive accumulation of capital (by ex-communists or other forces) have been some of the reasons for capital flight.

Post-communist informal rules matter. In transition countries, the lack of dictator with encompassing interests (as under the communist regime) and the lack of an established democracy (as in Western societies) create a vacuum where the specific post-communist *institutional* conditions have a tremendous impact on economic reform (Olson, 2000).[8] In different countries, different attitudes to Russia and the former USSR, different degrees of nationalism, alienation from the state, state ownership and the home country determine the specific spirit of patriotism, business ethics, corporate culture, and attitudes to the transition in general.

D. 'Catching-Up' Stage of Development and Corporate Governance

The basic slogan and official goal of the Washington Consensus has been 'transition to a market economy'. However, markets exist everywhere and 'market economy' *per se* cannot explain development differences among nations (Olson, 2000). In fact, at the start of the transition many transition economies were at a stage requiring to 'catch-up' with other advanced EU market economies. 'Catching-up' should have been the real objective of economic reforms. This is a specific stage when the economy has a potential to grow applying existing technological, marketing, and managerial knowledge from other developed economies (see, for example, for the case of Japan, Odagiri and Goto (1996); Sumiya *et all* (2000); Komiya *et all* (1988). For catch-up growth the most important constraint is the availability of capital. Access to

[8] I follow the idea that institutions like informal rules, beliefs, social norms are important factors (sometimes more important than law) for explaining economic behavior (see, for example, Milhaupt (2001) for the case of Japan; see Hart (2001) for integrating norms into the theory of the firm; see also Coffee (2001) for a more general discussion.

cheap capital in order to absorb knowledge from outside the country is crucial and the institutions accumulating savings and providing finance for business are of a great importance. At this stage, ownership and control structures and corporate governance mechanisms play a minor role (Morck and Yeung, 2001). The experience of developed countries shows that quite different institutions in different countries can emerge in order to accumulate capital supporting the catch-up growth. For example, Japan and other East Asian countries have developed concentrated banking systems and active government industrial policies.

E. Coalitions for Collective Actions

Social engineering. The transition to a market economy in 1989 is not an ordinary economic transformation, based on Hayek's *spontaneous order* notion. The irony for the champions of the transplantation of liberalism is that this transition resembles the process of 'the building of communism' after the World War II. The transition is a process of social engineering where a small group of people (top communist party-state *nomenklatura,* secret services, managers of large state-owned firms) decided (probably in 1985-89) to transform their political power into an economic one using market economy ideological slogans, the alienation of population from the communist reality and the support of globalisation factors (growing national external debt, capital export, establishment of companies abroad).[9] However, *these driving forces of the so-called "transition" were not the entrepreneurial and business part of society but the parasitic circles of the communist regime*. The disproportionate power for collective action of these small groups with narrow parasitic interests is an 'internal contradiction' in the societies in transition from communism to democracy (Olson, 2000).

Internationalist coalitions for collective actions. Bearle and Means never doubted *national* orientated utility functions of managers in the modern American corporations. National development-oriented or antinational-oriented behaviour of both managers and shareholders was never seen as an important issue in corporate governance debate in developed countries which practical experience has been seen as an example what ought to be followed in transition economies. In developed market economies, national interest adherence of company owners and managers has been taken for granted. However, in transition countries, emergence of internationalist coalitions for collective actions with culture, attitudes and goals shaped partly by both the former *communist internationalism* legacy and the present new *globalisation* trends challenges our understanding of the dichotomy "national - global". Without studying these internationalist economic agents we cannot analyse such basic transition facts as the *rent-seeking* behaviour of the ruling class and its important motivational characteristics – the maximization of capital flight, typical phenomenon in the early transition. However, to identify these specific international coalitions for collective action is a difficult task. These "flex" organizations were sometimes private, sometimes state, sometimes pro-Western, sometimes pro-national (see, for the case of Russia, for example, Wedel, 2001). In transition countries, international and global values have shaped the corporate culture of new private owners. For these private owners the *rational* behaviour includes 'investing' in politicians and parties, 'buying' laws and influencing law enforcement (in short, capturing the state), benefiting from privatisation deals, government debt markets and capital markets deals, etc. Like the term 'privatisation', another misleading term "corruption" has been applied for these phenomena but in recent years a more adequate term has emerged – 'state capture' (Hellman et al. (2000); Hellman and Schankerman (2000).

III. Transition to a Market Economy and Emerging Corporate Governance in Bulgaria in the 1990s

Transition to a market economy in Bulgaria: some background information

The Bulgarian transition to a market economy in the 1990s can be divided into two periods: the first is from the end of 1989 till the financial crisis of 1996-1997; the second one - after the introduction of a currency board in July 1997 to the present. *First,* the essential initial conditions at the beginning of transition were shocks from the collapse of the CMEA market and the foreign debt (12 billions of USD in 1990) inherited from the former communist regime. The transition policy was based on the Washington Consensus. A price *liberalization* started in February 1991 and at the end of this year the inflation reached 474% ***(Table 2).*** The *privatisation* process was moving slowly because of fighting for control in

[9] How complex and contradictory transition process has been can be seen, for example, in recent critical analyses of the CIA estimations of former USSR performance (see, for example, Becker, 1994). For "insiders" analysis, see also Solzenytzin (1999); Vladimir Bukovski (1998).

corporatized state-owned companies and in the period 1991-97 only 20% of the state assets were privatised. The financial *stabilization* was fragile. Both state-owned and newly established private banks issued non-performing loans due to 'crony' relations. The central bank utilized its monetary policy for refinancing of commercial banks and for rescuing the 'crony' banks from collapse. The evolution of the GDP during 1990 - 95 corresponds the hypothesis of the U-shaped response of output to transformation shocks[10]. However, the optimistic forecasts about 1996 and the following years were unrealistic[11]. There was an underestimation of the emerging 'crony' relationship based corporate governance that led to the outbreak of the financial crisis in 1996.

Second, in 1996 the Bulgarian GDP sharply fell by 10.9%. In July 1997 a currency board was introduced as a mechanism of recovering from the financial collapse. In 1997 the fall in GDP was 6.9% and in the next years there was GDP growth (3,5 % in 1998, 2,4% in 1999). The total amount of foreign direct investments was only USD 2 517 million (accumulated between 1992 and 1999). The share of the private sector in the GDP was about 70 percent of GDP in 2000 (BNB, 2000). During the currency board arrangement, a financial stabilization was established, inflation was low (1% - in 1998, and 0,4% in 1999) and the banking system was stable. However, the legacy of the wasted years remains. Despite the great expectations, the Bulgarian economy ten years later (like at the beginning of transition) has been at a stage requiring to 'catch-up' with other advanced EU market economies ***(Table 3).***

Some basic stages of the Bulgarian transition are presented in ***Table 4.*** The logic of the economic transformation can be partly seen in the specific power distribution among emerging coalitions for national development, globalisation factors, incl. Washington Consensus institutions like the IMF, the World Bank, etc., EU institutions (out of the scope of this analysis), the emerging communist-capitalist web and its international partners like the Russian interest groups, oligarchs, etc. (not in our analysis either). Some of these stages can be outlined as follows:

(i) 1985-89, this is a pre-transition period when a huge foreign debt was accumulated and hidden privatisation has began; the gross foreign debt increased from USD 2.9 billion in 1984 to USD 10.7 billion in 1989 (ESE,1993);

(ii) 1989-91, this is a period of default on the foreign debt (March 1990), corporatization of state-owned enterprises, establishment of new private firms and hidden illegal privatisation of firms and banks;

(iii) 1992-94, laws on privatisation, banks and credit activity were adopted, but the legal privatisation was slow and maximization of primitive accumulation of capital was the actual priority of 'transition';

(iv) 1995-96, Bulgaria resumed its foreign debt service, maximization of both primitive accumulation of capital and foreign debt service turned out to be an unachievable task, and as a result the country was hit by a devastating financial crisis in 1996;

(v) 1996-97, there was a radical change of transition priorities, the foremost task became the foreign debt service, for this goal a currency board was introduced; mass privatisation was carried out;

(vi) 1997-99, there was rapid privatisation, management-employee buy-outs were prevailing; the foremost maximization of the foreign debt service continued;

(vii) 2000-01, this was a period of the start of accession talks with the EU, and as a result Bulgaria significantly reformed its commercial legal framework but the government paid lip-services to the fight against corruption and state capture;

(viii) 2001- a new coalition, oriented to the national development, took power (Prime Minister the former Bulgarian King Simeon II) and has increased great opposing expectations: (a) optimistic - about a new national policy for 'catching-up' with a radical change in policy priorities (entrepreneurs, population); (b) pessimistic - about a hidden restoration of the retrograde regime prior 1997 (former state captors). What tendencies will prevail is a crucial issue for the further development.

The corporate governance *change* in Bulgaria is analysed as follows: an overview of property-rights transformation (point A); the property-rights change in 1989-1996 (point B); the property-rights change in

[10] For more discussion, Blanchard O., The Economics of Post-Communist Transition, 1997.
[11] See for example the optimistic forecasts of the Annual Transition Report 1995, EBRD.

1997-2001 (point C); a summary of emerging ownership and control structures (point D); capital markets emergence (point E); banking sector transformation (point F).

A. Privatisation and Newly Private Firms Establishment: Overview

1. Private sector development

The main factor contributing to the development of the private sector in Bulgaria during 1990-96 was the creation of new private enterprises. The share of privatised state-owned enterprises was insignificant (***Table 5***). Privatisation has made a little progress and it has been applied mainly to small and medium-sized enterprises. Only 2,396 enterprises have been privatised for the whole period (1992-96), the major part of them is municipal property or parts of enterprises. Substantial progress in privatisation was observed in 1997-98 connected with the finalization of a number of large-scale deals as well as the completion of the mass privatisation. About 1,050 enterprises were privatised - entirely or part of them - through vouchers. In the period 1992-97 about 20% of total enterprise assets were privatised. In 1997 there was acceleration of this process, e.g. about 4% of assets were privatised through cash sales with proceeds of USD 421,4 million. However, the data for 1998 show only 155,8 million USD privatisation proceeds. The main reason for slow progress is the continuing fight for corporate control between different groups of interests and between different ‘crony firms’. By the end of 1999, the private sector accounted for nearly 65,3 % of value added in the whole economy, i.e. 98 % in agriculture and forestry, 53,3 % in industry. In 2000, the private sector accounted for 69,3 % of value added in the Bulgarian economy showing a steady growth during last years.

The total percentage of the privatised assets since the beginning of privatisation process on 1 January 1993 till the end of 2001 is 52.5%, which is about 80% of the state assets due to be privatised in the mid-term. Between 1 January 1993 and 31 December 2001 the total privatisation effect was 10,777.268 Bulgarian Lev (1 Lev = 1 DEM). The distribution of concluded transactions by sectors is as follows: industry - 32,6%, trade - 23,1%, agriculture - 12,4%, tourism - 10,7%, others - 21,2%. Privatisation of the basic part of the companies in *manufacturing* has finished. Some of the big privatised companies are: “Balkan Airlines”, “Neftochim”, “Petrol”, “Agropolichim”, “Himko”, “Antibiotic” - Razgrad, “Yambolen”, “OtK” - Kardjali, “Kremikovtsi”, “Promet” - Burgas, “Asarel-Medet”, “DZU”” - Stara Zagora, “Alumina”, “Arsenal”, “Beta-Cherven Bryag”. *Energy utilities* privatisation has barely started. The privatisation process of the *Telecommunication Company* is ongoing. In the *financial sector,* the United Bulgarian Bank (July 1997) and the Bulgarian Post Bank (the end of 1998) have been privatised. In 1999, Society General bought TB Express and Reagent Pacific - Hebros Bank. In 2000, Bulbank was privatised.

2. Public sector decline

The main changes in state-owned enterprises are related to their transformation (*corporatization*). This was a process transforming former state enterprises into companies with 100% state participation. In general, this process has taken place mainly in the 1991-92 and has developed at a considerably lower pace in the following years. After 1993, *non-transformed* state-owned and municipal firms decreased twice in number. This was due to two main reasons: first, the continuing process of corporatization and, second, the privatisation of non-transformed state-owned enterprises. As a result of the progress made in privatisation and enterprise restructuring, the non-private sector has decreased its share to 34,7 % of gross value added in 1999. Respectively, the share of public sector in industrial production is 46,7 % of gross value added. Employees in the public sector are about 40 % of the total employment in the Bulgarian economy.

We will use the framework discussed in the previous section to analyse the driving forces for the specific Bulgarian property-rights transformation.

B. Washington Consensus Privatisation Policy against Post-Communist Primitive Accumulation of Capital (1989-1996)

1. Initial conditions

The most striking features of the initial conditions for property-rights transformation in Bulgaria were as follows: (i) *nominal state ownership* of enterprises; (ii) informal, implicit de facto *total control* by top communist *nomenklatura* (managers, bankers, state officials, Communist party leaders, secret services) over **all** the enterprises and state institutions; (iii) tremendous uncertainty due to the volatile political environment, narrow-interest fighting groups and consequent short-time business horizons. The communist ruling group had some hypothetical strategies regarding institutional changes. First, designing a coordinated strategy with national development goals and establishing a legal and institutional framework for privatisation (given the real origin and goals of the communist *nomenklatura*-driven transition stated in the previous section, this opportunity has been regarded only as a theoretical one). Nevertheless, the presumption of a government programme, coordination and goals clearly stated were at the heart of the Washington Consensus suggestions for privatisation in transition countries. The second 'strategy' has been the looting of state-owned assets (budget, enterprises, banks). The latter strategy was typical of the period 1989-1991 (and even before, but this is another story and probably more essential for understanding the so-called "transition" in Bulgaria).

2. Corporatization of state-owned enterprises

In early 1990 the one-party system in Bulgaria was abolished; the state sector remains dominant while the private sector was burgeoning in small manufacturing, trade and services.[12] In these new conditions the large and medium-size state-owned enterprises began a process of *corporatization* (conversion into joint-stock or limited-liability companies, wholly owned by the state).[13] The first wave of this transformation began in 1989 when Decree No. 56, on Business Activity, came into effect. Since 1991 the transformation of state enterprises into companies has been carried out according to the Commercial Code.[14] As a result of this process, in the early 1990s all major non-financial companies in Bulgaria were wholly state-owned. This unique hybrid form was defined as a 'sole-trader joint-stock company' or 'sole-trader limited-liability company' by the Commercial Code (Article 61). It is a temporary business form, and should have survived for up to five or six more years under the Privatisation Act (Article 19). *This form of business organisation has been the starting point for the privatisation of enterprises in Bulgaria*. In what follows, this form is referred to as the 'sole-trader company', even though this represents a departure from the usual English meaning of this term, as it is a company with 100% state participation (for a detailed analysis of the 'sole-trader company' in Bulgaria, see Peev (1995).

Corporatisation of large enterprises in the early 1990s created confusion over the distribution of property rights. At the beginning of this process there was a shift of control rights to enterprise insiders, mainly managers. Decree No. 56 and subsequent practice reflected the enhanced power of communist *nomenklatura* managers. The inefficient behaviour of the so-called 'insiders' is well known from the literature (Voszka, 1992; Frydman & Rapaczynski, 1993).[15] The behaviour of directors belonging to the former communist *nomenklatura* was directed at bringing potentially efficient enterprises to a state of collapse and putting them up for sale through privatisation.

After the first *non-communist* government in Bulgaria came to power in 1991, however, the motivation for privatisation of companies changed. The new government tried to reassert its ownership of the enterprises and to overcome the vagueness of the property rights created under communist rule. Under the influence of this government and the trade unions, new directors were appointed in some enterprises.[16]

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[12] The coordination between economic units in Bulgaria in the early l990s has a peculiar character corresponding to one characterisation of the Hungarian economy in 1987: 'neither plan nor market' (Schroeder, 1988).

[13] For the legal procedures of this process in Bulgaria, see Frydman, Rapaczynski & Earle (l993).

[14] Concrete facts on the genesis of 'sole-trader joint-stock companies' in Bulgaria are presented in Peev (l992).

[15] Author's informal interviews with state officers and new directors, unconnected with the communist *nomenklatura*, revealed that communist *nomenklatura* insiders in Bulgaria exhibit the same inefficient behaviour as in the other East European countries.

[16] Typically, the struggle for directors' seats was stronger in large companies. An author's investigation at the end of 1993 showed that, of 70 companies, only 19 managing directors, just over 25%, remained from the former communist *nomenklatura*. The sample included 18 large companies with a workforce of over 500 people, of which only one had the same communist *nomenklatura* director.

The behaviour of these new directors, unconnected with the communist *nomenklatura*, was quite ambivalent. On the one hand, the owner state has appointed the manager to defend the national interests by keeping the companies in operation and preparing them for efficient structural adjustment, including privatisation. On the other hand, however, the incumbent directors operated in unchanged conditions of power without responsibility. Opportunities have opened up for primitive accumulation of capital, and managers rather delayed the privatisation of their companies.

Ownership structure. Empirical studies reveal the specific property-rights structure of the 'sole-trader company' (Peev, 1995). It was characterised as follows: (1) state ownership of assets; (2) the state bears the residual risk; (3) the government appoints a board of directors which manages and represents the company and appoints managers; (4) under the Act on Transformation and Privatisation of State-owned and Municipally-owned Enterprises in Bulgaria such companies must be privatised within five years of transformation. The 'sole-trader company' was a transitional form of business organisation lying between the self-managed socialist enterprise and the modem corporation.

There was an essential difference between a 'sole-trader company' and a self-managed socialist enterprise. In the former the employees do not have property rights. This is a peculiarity of the 'sole-trader company' in Bulgaria. In Hungary and Poland the workers' councils continued to exist after the commercialisation of enterprises, though in former Czechoslovakia they were disbanded after April 1990 (Mejstrik, 1992). The essential similarity between a 'sole-trader company' and a self-managed socialist enterprise is the preserving of state ownership of assets.

Another essential feature of 'sole-trader companies' was their peculiar genesis. Examination of the origins of companies indicates that administrative initiative from the executive power was the main factor in their establishment. More careful analysis of the dynamics of the process, month by month, reveals a strange surge prior to a pending election. This indicates that the establishment of companies occurs not so much as an adaptation to the changing economic environment but rather as a result of political and administrative processes. *This means that the survival of a particular company should be guaranteed by the government even in the presence of high transaction costs associated with companies' adaptation to new markets, technological conditions, restructuring requirements and the like.*[17] However, the government did not fulfil its obligations as owner, since it typically left companies to deal with these problems on their own.

The main agents of property rights in a 'sole-trader company' were the government as owner and the managers. The function of risk bearing, according to property-rights theory, was taken on by state officials and the function of management by managers. However, the state officials were risk bearers not because of their higher motivation for risk bearing but because of their status.

Who was the actual bearer of the residual risk after the collapse of the CMEA and the shock stabilisation programme in Bulgaria at the beginning of the 1990s? While a given enterprise was in state ownership the government, as owner, is the economic agent that, according to the property-rights theory, must bear the residual consequences of shocks. The managers and workers of a particular enterprise have had no liability with respect to the external difficulties felt by the enterprise. In practice, however, state officials shifted all the liabilities of the transition onto the enterprise. The 'sole-trader company' obtained so-called 'autonomy', a hypothetical promise of discretion in the held of products, markets and investment. In fact, however, this was only quasi-autonomy because, first, the state remained the owner of the assets and shifted only the risk bearing connected with the economic reform to the companies; second, the risk bearer was again impersonal-managers or employees or the enterprise at large.

The main shock for 'sole-trader companies' at the beginning of transition was not so much the CMEA market collapse as their 'autonomy', their high degree of risk bearing and managerial discretion, on the one hand, without ownership of assets and company rights to sell assets, on the other. Case studies show that some companies have had a higher degree of 'autonomy' than others. The reasons can be found in the complicated power distribution among state officials, managers and interest groups in each enterprise. In this way some companies win without effort, while others lose.

Types of control. Who has had control over 'sole-trader companies'? The simple view is that a 100% state-owned enterprise is subject to effective state control. From that point of view the government has controlled newly founded companies, wholly owned by the state. But this is only the first impression,

[17] For ideas on this point, see Pejovich (1990).

for there is a lot of empirical evidence showing a different picture.[18] An overview of the literature on the separation of ownership from control of corporations in a developed economy provides some starting points for distinguishing types of control of 'sole-trader companies'. However, every randomly selected criterion of types of corporate control fails to reflect faithfully the reality of the 'sole-trader company'. The formal quantitative stake in corporate assets does not determine who has *real* control over a particular company. A more suitable classification of 'sole-trader companies' by type of control is a qualitative one. Empirical studies show emerging specific control structures of state-owned companies in the Bulgarian economy in transition.[19]

Control based on unestablished property rights. These are property rights structures that fail to determine clearly who owns company assets, who are a bearer of residual risk, who is a decision maker, who appoints members of the board of directors.[20]

In this ownership structure, however, there were different degrees of managerial discretion. Using as a criterion the degree of managerial discretion based on unestablished property rights, distinct types of control of 'sole-trader companies' can be identified. First, *high managerial discretion owing to unclear property rights*. These were companies with a high potential for discretionary managerial behaviour. This does not mean that their managers encourage strategies for opportunism and shirking and hence inefficient enterprise behaviour at large. Under post-communist conditions managerial discretion has had an ambivalent nature. On the one hand, more managerial discretion implies removal of barriers and scope for initiative. On the other hand, though, it involves less state intervention and leaves more room for shirking. Second, *low managerial discretion owing to unclear property rights*. These were companies with a low degree of scope for discretionary managerial behaviour. This does not mean that there is strong owner control, especially government control, and hence efficient monitoring over top managers and efficient enterprise responses at large. These companies were a peculiar transition type where in fact nobody has had control. On the one hand, less discretion implies a stronger involvement of state institutions in decision making, with the possibility of forcing managers to show initiative; on the other hand, less discretion also provides less opportunity for independent managerial initiative. Which tendency prevails can be shown only by empirical analysis (see Hare and Peev, 1994).

Control based on interest groups influence. Another key feature of the control structure of the 'sole-trader company' was the influence of interest groups other than the state. There was a number of examples known from the Bulgarian press that demonstrated a three-agent structure of company management: state officials-owners, managers, and the emerging communist-capitalist web.[21]

In Bulgarian 'sole-trader companies' interest groups other than the owner state have include political forces, finance groups, trade unions, etc. (for more detailed analysis of emerging communist-capitalist web of interests groups, see point 5 below). In individual companies they have had different degrees of influence on management. The chief criterion for the strength of this influence is the degree of managerial discretion. Using this criterion of managerial discretion based on the influence of interest groups we can distinguish two types of companies. First, *high managerial discretion owing to interest groups*. These were companies in which labour exercised a low degree of influence on corporate operations (mainly over the appointment of managers and management). Here the managers have had more discretion but, on the other hand, they felt the restraining influence primarily of the trade unions but also of other forces. There was a peculiar type of monitoring of managers by groups other than the owner. The relationship between managers and interest groups was similar to that in the socialist enterprise. Everyone wields power without assuming responsibility. Second, *low managerial discretion owing to interest groups*. These were companies in which a strong influence was exerted by interest groups besides the nominal owner. Typically, these were large companies. The potential for discretionary managerial behaviour was low but in this situation the restraining effect on managers was not exerted by the nominal owner. Again no economic agent with strong owner motivation existed.

Among 'sole-trader companies' there were also companies with deliberately retained and clear government control. Examples of this type of company were to be found in the energy sector. But their

[18] The Bulgarian press reveals a number of cases of backstage fights over appointments to boards of directors of some of the biggest Bulgarian enterprises in the electronics, machine-building and military industries.
[19] For more detailed examination of the control structures in the early transition years, see Peev and Hare (1995).
[20] This obscure ownership structure is typical in the post-communist countries (Frydman & Rapaczynski, 1992).
[21] See also Financial Times, l0 May 1994, 'Ex-communists embrace a half-capitalist Bulgaria'.

number was small and this control structure was not typical of the 'sole-trader' structure of business organisation.

Despite 100% state ownership, the 'sole-trader companies' were mainly under managerial control and interest group control. These types of control were based on unestablished property rights and informal influence by groups other than the nominal owner state. This peculiar transitional kind of control was implicit and unstable.

3. Privatisation and Newly Private Firms Establishment

Privatisation. In 1989-1991, the process of unregulated and illegal transfer of capital from the state to private hands has begun. In April 1992, the Parliament has approved the 'Transformation and Privatisation of State-Owned and Municipal-Owned Enterprises Act' that has been amended many times in the years. The first regulated privatisation programme has been designed in 1993. However, till to end of 1996 the privatisation process was slow.

Empirical studies show that the typical *property-rights structure* of the enterprises after their privatisation in 1992-96 is characterized as follows: 1) one party- private firm, personnel, managerial team etc., owns a big stake of assets, 2) all the shareholders owns the right of residual risk, 3) this party has the formal and factual right to appoints a board of directors, 4) all the shareholders have the right to sell their rights by public offering (Peev *et all*, 1999). This structure is similar to the ownership structure of the newly established private companies. Both privatised and private firms have *concentration* of the company assets in the hands of a large owner. The main *agents* of property rights in the privatised companies are the shareholders as owners and the managers. The function of risk bearing, according to property-rights theory, is taken on by shareholders and the function of management - by managers. However, the owners have high-risk aversion, typically the large shareholders are both shareholders and managers. Who is the actual bearer of the residual risk after the privatisation? While a given enterprise is in private ownership, the shareholders as owners are the economic agents that, according to the property-rights theory, must bear the residual consequences from the managerial decisions. In practice, the large shareholders of the firm have very close connection with the managers. These shareholders consist of other firms owned by managers, outside firms with managerial ownership stake, etc. The privatised company obtains a specific autonomy: (i) the large owner of the assets is the risk-bearer as well; (ii) the government shifts the risk- bearing of the macroeconomic financial reform to the companies, and they become hostages of the potential government voluntarism.

Till the end of 1996, the privatisation rate in Bulgaria was low. The privatised enterprises are small and medium-sized. Enterprises with a highly *concentrated ownership* structure are more frequent. From the point of view of control structure, the enterprises under *outsider control* are prevailing over the ones under insider control. The institution of the *board of directors* in privatised enterprises is characterized by the most active behaviour in comparison to the behaviour of the board of directors in enterprises with other forms of ownership. On the whole, the managers have the highest influence in decision-making in the spheres of production and personnel, while in the spheres of managerial employment and compensation and the financial sphere - the board of directors is in charge.

A specific case of coincidence between the dominant nominal owner and the real decision-maker in the firm are privatised enterprises under the control of a *foreign* investor. In these enterprises there is no separation of ownership and control. On the contrary, we observe a *very strong owner control and owner participation in the management of the enterprises, typical of property-rights structures in the so-called 'classical' capitalist firm.*

Privatised enterprises are characterized by efficient managerial strategies to restructuring, the most active being the enterprises under foreign owner control. Privatised enterprises have better performance (profitability, productivity, and age of capital) in comparison to state-owned enterprises. However, such kinds of conclusions are doubtful because in many cases it is not ownership structure which determines performance, but the other way round. The privatisation programmes select enterprises with better short-term prospects and there are specific firm characteristics determining whether firms are privatised.

Newly established private firms. The *ownership structure* of the private firms established *de novo* has had two main peculiarities. First, many firms were sole proprietorships, and very often their owner and manager are one and the same person. *These firms have a similar ownership structure as the 'classical' capitalist firm known from the literature of property rights*. Second, few private enterprises are companies. Their ownership structure is characterized as follows: 1) high concentration of the assets

in the hands of one party- private firm, private firms coalition, etc., 2) all the shareholders own the right of residual risk, 3) the large shareholder has a seat in the board of directors and appoints the other members of the board, 4) the shareholders have the right to sell their shares. The key feature of the ownership structure described here is that the large owners bring more risk, and their personal welfare is closely connected with the viability of the firm. *Their motivation adheres to the motivation of the owner-entrepreneur of the 'classical' capitalist firm who is the sole bearer of both residual risk and managerial initiative.*

Private firms *de novo* have a more concentrated ownership structure than privatised firms. The dominant owner has a majority (50-80% of assets) or private control (over 80%). A typical dominant owner is the *manager-owner*. There is no separation of ownership and control, and a most efficient managerial behaviour is expected. The newly founded private firms showed passive strategies to enterprise restructuring, which is explainable taking into consideration their origin. Private firms *de novo* show the best performance (profitability, productivity, and age of capital) compared to all the other firms. This indicated that in spite of the unfavourable semi-market environment their ownership structure induced life-giving incentives of adaptation.

However, the existence of 'crony' private firms is a specific case. These firms receive a strong political support. Typically in the early transition, Bulgarian banks pumped resources from state institutions and state budget and transferred them as loans to 'crony private' firms and state loss-makers. The latter shifted financial resources through transfer pricing or other devices to 'crony private' firms (for more details, see point 5 below).

4. Globalisation factors for corporate governance change

From 1989 to 1996 in Bulgaria, the Washington Consensus policy, and privatisation in particular, were seen as an efficient policy designed *against the looting* of state enterprises and the whole Bulgarian economy. The stabilization programme started in February 1991 with support by the IMF, but very soon the austere measures in the field of the monetary policy (September 1991) were abandoned (Agency for Economic Forecasting and Development, Annual Report, 1994). In 1991, the World Bank presented specific requirements regarding the Bulgarian foreign debt service before its structural adjustment loan (SAL) to be granted. In 1992 under the World Bank impact as a loan conditionality (first SAL for 100 million USD), the Bulgarian government implemented a programme for promoting discipline on state-owned enterprises but it was not enacted in practice (Vutcheva, 2001). *The economic policy remained inconsistent, the lack of coordination and public consensus about its goals was a key policy trait at that period*. The Bulgarian foreign debt service was resumed in 1994 (after the moratorium in March 1990) when the government signed an agreement with the London club creditor banks for re-scheduling and debt restructuring. The so-called structural reform (privatisation, state loss-makers liquidation, legal reform, etc.) was fostered by the World Bank as loan conditionality. In the period 1991-96, the World Bank issued loans of USD 500 million, about half of this sum being for 'structural adjustment'. *In the period 1989-1996 in Bulgaria, the international financial institutions and the Washington Consensus policy played the role of factors for 'market economy' development (against the communist past), 'privatisation' (against post-communist primitive accumulation of capital or simply the looting of national wealth), legal environment development (against institutional vacuum), last but not least, pro-Western development (against the Russian 'imperial' impact).*

Surprisingly, however, the Bulgarian practice follows neither the good objectives formulated in the different recommendations put forward by privatisation advisers, nor even the privatisation programmes themselves.[22] There was another logic of economic reform of state enterprises and it can be seen in the specific power distribution among the potential key players: (i) the emerging entrepreneurs and other forces for 'catching-up' and national development; (ii) Washington Consensus institutions; (iii) the communist-capitalist web – the real driving force for the so-called 'transition' in Bulgaria.

[22] After the collapse of the communist regime in Bulgaria at the end of 1989 different governments (Dmitar Popov; Filip Dimitrov) declared their strong intention to privatise the state-owned sector. The next Bulgarian government (Luben Berov) called itself 'the government of privatisation'. Despite all these ambitions only five large enterprises had been privatised by the beginning of 1994 (Annual Report of Agency for Privatisation, 1993).

5. Effects of post-communist primitive accumulation of capital on corporate governance change

Establishment of a 'crony' communist-capitalist web. The phenomenon described as 'state capture' (Hellman et all, 2000) following the World Bank and EBRD survey in 1999 can be found at the very beginning of transition in Bulgaria. There were some steps of state capture development. First, the collapse of the communist totalitarian control of the state, the Communist party, the repressive bodies, and banks on all the economic activities. Second, the establishment of *groups of interests* ('Multigroup', 'TRON', etc. at the very beginning, coalition 'G-13' in 1994, 'Orion' in 1995) and *'crony' private institutions* (non-financial firms, banks, insurance companies, etc.) based on 'state - Communist party – repressive bodies (including KGB) - state-owned banks – state-owned enterprises' network, which we can define as '*communist-capitalist web'*. Their members used to be representatives of control institutions of the former totalitarian regime. They had full information about *all* aspects of the economic, political, private, etc. life in Bulgaria.[23] The interest groups named above captured the state. The government with Prime Minister Berov (1992-94) was known as the 'Multigroup's government'; the next socialist government with Prime Minister Videnov (1995-96) established close connections with another interest group, 'Orion'. 'G-13' was a confederation of bid industrials (*de facto* different interest groups in the web), which received a monopoly position in the sectors of energy, transport, military industry, chemicals, and some others.

The key factors determining the behaviour of the 'web' were as follows: (i) tremendous political uncertainty; (ii) information asymmetry between the web and the rest of society; (iii) lack of institutional constraints to their potential opportunistic behaviour (members of the web had worked in governance institutions of the former totalitarian regime and more importantly, some had preserved their positions); (iv) omnipotent control over all the resources in Bulgaria. Theoretically, under conditions of lack of institutional constraints, informal rules and internal motivations (like patriotism, nationalism) may have an impact on business behaviour. In the Bulgarian practice, however, after about fifty years of communist regime, the negative social selection was nominated for Communist party leaders, only people loyal to Moscow (some had preserved the *same* attitudes changing only the direction of their service after 1989). The behaviour of 'web' members was *rational*. Their utility function was maximal transfer of state resources to private hands (individuals, private companies). However, to fulfil this objective the rational behaviour required a *long-term* specific investment in specific organizations and agents ('crony' firms, 'crony' banks, political parties).

State capture. In the early transition in Bulgaria, state capture, or better, society capture consisted of specific forms. First, web members' promotion of people to key political parties and state positions, called 'investment' in new persons (capture of parliament, government, state bodies like the Bulgarian National Bank, the Bulgarian Consolidation Company, etc., the court system). This means that the institutional and legal environment for corporate governance change was shaped in accordance with the 'web' interests. The process of law enforcement obeyed the same interests. For example, in 1992-1994 the specific governance institutions for control on monetary policy and bank system (special commissions of the Parliament and the Council of Ministers) never monitored the governor of the Bulgarian National Bank (Pejkov, 1996). Second, the same process of preserving web positions or penetration through 'new faces' (through the newly established trade union 'Podkrepa') into top management and board of directors' structures in state-owned enterprises or in state-owned banks was observed. The result of this process was the establishment of 'web'-based principal – agent relations. *Principals and agents, state banks creditors and private 'crony firms debtors, state managers and private 'crony' firms owners, state officials in*

[23] According to some investigators, the "transition" in Bulgaria had began before 1989, as early as 1985. In January 1985 the Politbureau of the Central Committee of the Bulgarian Communist Party has established with Resolution No.68 a special party-state commission for a science-technical policy designated for industrial intelligence. People involved in these projects used project funds, firms established in the West, etc. to build up later the web of interest groups, banks, firms that have been the real driving forces of the transition since 1989. No statistics are available to assess the financial damage for the Bulgarian society from these operations. However, there were some indirect indicators as the fast growing foreign debt during 1985-1989 (in USD billion: 1984 – USD 2,9; 1985 – 3,8; 1986 – 5,8; 1987 – 8,2; 1988 – 8,9; 1989 – 10,7). Even in 2002, about 15 years later, there is no official information and analysis about the real foreign loans utilization at that time.

corporate governance monitoring institutions (like the Bulgarian National Bank for banks and the Ministries for state-owned firms) and managers or bankers belonged to the same ' web'. Politicians from different parties – communist and anti-communist, belonged to the same web, too. In fact, the real agency issues were between the 'web' and the society as a whole (entrepreneurs, independent non-crony firms, households). Expectations that the emerging web would establish an efficient corporate governance system were illusions because this meant they should constrain themselves (incredibly, from both theoretical and practical viewpoint).

Forms of primitive accumulation of capital. Some forms of state capture and illegal state assets transfers to private structures were as follows. First, one of the secrets of the Bulgarian transition remains what happened to the sums collected through *foreign state debt financing*. However, the mismanagement of the external loans received since 1991 from the EU, the World Bank, EU Programme PHARE and countries like Austria, Sweden, Norway, Finland, Japan, Switzerland can clarify to some extent the foreign debt usage. These sums designated for the so-called structural reform of state enterprises were collected in a specially established 'State Fund for Reconstruction and Development' in 1991. In 1991-95 the gross sum of the received loans was USD 958,3 mln. However, contrary to the fund designation, these sums were not used for state enterprises restructuring but mainly for short-term credits for state enterprises with liquidity problems (some of them big loss-makers like 'Balkan', 'Kremikovtzi', defence complex enterprises, etc.). Finally, the fund was closed down in 1998 and the state budget had to pay the debt due to foreign creditors. In fact, the real beneficiaries were not state-owned firms, which received credits but 'crony' firms squeezing their resources and the real loser – the state budget and the Bulgarian society as a whole.

Second, closing down the existing *state-owned economic associations* (i.e. groups of affiliated companies) in 1990-91 and transferring their credits to state-owned enterprises. During 1989-91 these associations transferred money to establish private companies abroad and banks in Bulgaria.

Third, decapitalization of *state-owned banks* through 'bad' credits from bankers to 'crony' private firms, 'crony' private banks (e.g. 'Credit bank', 'Kristalbank', 'First private bank', 'Mollov',etc.), business groups ('Multigroup', 'TRON',etc.), and individuals belonging to the web of communist-capitalist connections. There is a special term coined about these kinds of debtors – '*credit millionaires'*. A similar scheme was the transfer of 'bad' credits from state-owned banks to state-owned firms that were intrinsic loss-makers, and then from state-owned firms to 'crony' private firms. Following the inflation process in 1991-92 the government did not manage to revaluate assets of state enterprises that had led to low depreciation norms and decapitalization. In hindsight, it seems that a typical strategy for the ruling web was using state-owned enterprises as residual risk-bearers of external decisions and transferring losses to enterprises (e.g. bad credits under communist regime before 1991 that were de facto a centralized distribution of credits to enterprises).

Fourth, decapitalization of *state-owned enterprises.* The typical relationship between 'crony' private firms and state owned enterprises was based on 'input-output' price transfer scheme, where private firms, owned by state enterprise managers (or their relatives), were suppliers and customers of the same state enterprise. The consequences were as follows: state enterprise - residual risk bearer, private firms - profit takers, and decapitalization of the state enterprise. In fact, the relationship between the state and some private enterprises ('crony' ones) was like between *victim* and *vampire* rather than between equal economic agents.

Fifth, transfers from the *state budget*. A small part of this scheme included transfers to newly-established 'crony' private banks (e.g. 'Turistsportbank', 'First private bank', etc.), business groups, and firms, through 'credits' from the military-industrial complex, via the service of the Bulgarian railways company, using the state fund 'TNTM', other budget activities, etc.

Primitive accumulation of capital and capital flight are two essential parts of post-communist transformation. Key factors inducing new domestic capitalists to transfer capital abroad were: (i) property-rights uncertainty and threat from expropriation; (ii) internationalist values and attitudes of the new private owners. No official data are available on the actual capital flight and primitive accumulation. (Some studies estimate the total sum of state assets transferred to the 'crony' communist-capitalist web for the period 1985-95 to have amounted to the equivalent of USD 13 billion, see, Pejkov,1996). However, it is difficult to verify the exact sum).

6. Key actors: 'communist-capitalist web', Washington Consensus institutions, Bulgarian population

Under the Bulgarian circumstances described above, the *potential* coalitions for collective actions against the communist-capitalist web discretionary behaviour could be: (i) entrepreneurship based opposition-oriented to the national development and 'catching-up' (in fact, very weak at that time); (ii) large state-owned enterprises (in fact, the interests of workers coincide with managerial interests in delay of liquidation or privatisation of their firms); (iii) international actors. Among the latter, the emerging Russian interest groups (very similar to the Bulgarian ones) have played a negative role for the independent market development in Bulgaria.

The position of the Washington Consensus institutions (IMF, World Bank) was specific. These external institutions were the only possible coalition for collective action in the early transition in Bulgaria that could have constrained rent-seeking and looting-oriented behaviour. In fact, under pressure by these institutions some necessary laws (among them the law of privatisation) were adopted. In hindsight, it seems that after the default on the Bulgarian debt in March 1990, the emerging 'web' was searching for external financial support. However, this illegal web never tried to design a real consistent policy for national development. They used international loans like the former communist leaders in the 1980s had done – without coordination or a strategy for a long-term national development.

Surprisingly, there existed a mutual interest in the Washington Consensus policy among the emerging ruling web, international financial institutions and the Bulgarian population. The latter has had special attitudes, beliefs and preferences. First, in the early 90s, the Bulgarian society was divided into two groups due to the long existing "crony" socialist relations favouring communist *nomenklatura* members. This artificial 'communist – anti-communist' division had its deep roots of real alienation of people in: (i) the ruling communist *nomenklatura* and the state itself (labelled as "totalitarian state"); (ii) socialist *state ownership*; (iii) socialist *society* and socialist *home country*. Under these conditions of alienation, the Washington Consensus ideas for withdrawal of the state from the economic life, privatisation of state-owned firms and adherence to the more developed world based on liberal international market economy principles seemed quite reasonable. New liberal international economic order values have had a good reception by post-communist beliefs and attitudes.

Second, at the same time (and this is one of the key contradictions in transition), adherence to the communist values of collectivism, etatism and egalitarism carried on.[24] These social attitudes were used by the Washington policy designers and filled with new content that strangely resembles the old communist tenets. Thus, important pillars of the new policy adoption were new "market-oriented" beliefs that: (i) a social engineering process like the transition could be successful and ten years were enough to build a market economy; (ii) anybody else (in the past - the Communist party committee, now, for example, the IMF or well-experienced Western advisers) would know better what the national interest was and what policy would defend it better; (iii) emerging new private owners would be the new heroes, "captains of the transition". At the same time, these beliefs were based on limited knowledge or no knowledge at all about the real economic situation in Bulgaria and mechanisms of economic transformation in general. However, these attitudes were harnessed to the ideology of the Washington Consensus policy to development aiming at a free market economy. Even at that time, this seemed strange and contradictory. Ten years later Kornai called this policy both "vulgar Marxism" and "vulgar Coase-ism" (Kornai, 2001). However, the specific post-communist culture described above cannot explain *per se* the Washington Consensus policy transplantation in the Bulgaria conditions. Two other factors played a crucial role: (i) the high *foreign* debt and, consequently, the strong IMF impact on the Bulgarian policy and (ii) internationalist political elite in Bulgaria serving foreign interests under communism and motivated to preserve its attitudes in transition too.

In the early transition years in Bulgaria, the 'internal contradiction' (Mansur Olson) of the enormous power of *parasitic* forces for collective action (the emerging communist-capitalist web of former top communist *nomenklatura,* totalitarian secret services, etc.) was observed. These forces had to design an efficient corporate governance system (ownership, control, legal and regulation environment) simultaneously preserving the status quo, their power. This has created the **dual character of the corporate governance design in transition**: (i) *corporatization* should have been a process of transformation of socialist state enterprises, establishing more efficient governance structures, but de facto it was a corporate governance change favourable for looting the state-owned companies; (ii) *privatisation*

[24] For the contradictory nature of post-communist beliefs and norms, see Peev (1990). The author coined a special concept, 'economysticism', trying to explain the specific transition phenomena more properly.

should have been a transfer of state assets to private firms to enhance allocative efficiency, but in fact it was designed to loot state assets and to transfer them to 'crony' private firms; (iii) the *new private sector* established both independent private firms and also 'crony' private firms aiming at state assets expropriation; (iv) the *legal system* and *law enforcement* should have been designed to constrain insiders and the totalitarian state, and to defend creditors and shareholders, but de facto it led to a weak, captured state, and strong captors and 'crony' firms.

C. Washington Consensus Privatisation Panacea against Post-Privatisation Reality (1997-2001)

1. Voucher privatisation

Since 1996 there has been acceleration of the privatisation process (***Table 5***). The basic forms applied were a Czech-like voucher privatisation (named 'mass privatisation' in Bulgaria) and management-employee buy-outs (MEBO). In 1996-97, 1050 enterprises were included in the mass privatisation programme and about 15% of the state assets were privatised through voucher privatisation. This scheme was designed by the socialist government (Prime Minister Videnov). The officially stated objective was to satisfy the demands for social justice and to carry out a fast transfer of state assets. According to the scheme, every Bulgarian citizen resident of the country, over the age of 18 was entitled (practically free of charge) to receive 25,000 investment vouchers. In contrast, in developed market economies, share purchases involve opportunity costs that induce shareholders to pursue wealth maximization objectives. However, the Bulgarian give-away scheme created a specific lack of interest on the part of the citizens – potential small shareholders, in companies' affairs due to the practical lack of opportunity costs to acquire shares. 81 privatisation funds were established, entitled to collect vouchers and build their own capital. Around half of the potential participants took their vouchers and 2.5 million (bearing about 80% of vouchers) transferred them to privatisation funds. These funds participated in auctions to 'invest' collected vouchers in companies involved in the programme for mass privatisation. In fact, this was a give-away scheme for privatisation funds (established mainly by domestic banks and managers of state-owned enterprises). The bulk of privatisation funds belonged to the communist-capitalist 'crony' web described above. After collusions among ex-privatisation funds to redistribute and concentrate their holdings in different enterprises, 15 largest funds owned about 10% of the former state assets.

Privatisation funds were later transformed into holding companies. The emerging *ownership and control* structures were specific. Holding company ownership in a given subsidiary was concentrated, the typical control being the majority one, but the ownership of holding companies itself was dispersed. The *ultimate* control of a subsidiary company was a minority and managerial one. However, the risk-bearing function was quite specific: (i) holding companies' main shareholders (ex-privatisation funds founders) received company assets practically free of charge; (ii) they could expropriate profits from good projects and shift losses from bad ones to small dispersed shareholders. The typical ownership structure formed was *dispersed* ownership with *managerial* or *minority* control exercised by the new holding companies (former privatisation funds). The specific separation of ownership and control has led to inefficient behaviour models: (i) ex-privatisation funds founders (minority *controlling* shareholders of holding companies) behaving against small dispersed shareholders (through tunnelling, looting, etc.); (ii) incompetent ex-privatisation funds founders (majority shareholders of subsidiaries) faced discretionary managerial behaviour. In fact, these theoretical predictions were corroborated. The new large owners after mass privatisation showed deteriorating financial results after privatisation (***Table 6***). The typical behaviour of holding companies was sale of assets, debt increasing, and negligible dividends distribution. Their profits and profitability were diminishing.

2. Management-employees buy-outs (MEBO)

In 1997, with the support of the international financial institutions a basic institutional change was introduced, a currency board. The Washington Consensus policy was put on the agenda again in Bulgaria, like at the very beginning of transition in 1990s. The basic task of the new government (Prime Minister Kostov) was financial stabilization, rapid privatisation of state enterprises (to compensate for lost time), liquidation of the state-owned loss-makers. During 1997-2001 the tenets of the Washington Consensus regarding privatisation became an official policy.

In 1998-1999, the government preferred insider privatisation, due to contentious close connections between policy makers and managers. A large part of the privatisation was taken by the management-employees buy-outs (MEBO). In 1998 about 74,4% of the privatisation deals were MEBO, in 1999 – this share was 39%, and significantly dropped (after the critique by the IMF and the World bank) in 2000. The MEBO scheme allowed management-employees teams to buy enterprises in cash under preferential conditions (discount to 10% of the price offered and payment of the remaining 90% through instalments in a ten years' period). However, in fact, the finance sources for privatisation belonged to interests groups outside the enterprises. Managers were only formal participants in this process. The real control was held by outsiders.

This scheme created in practice specific governance problems: (i) agency issues between managers and employee-shareholders regarding wage determination, layoffs, etc; (ii) a shortage of investment needed for enterprise restructuring. In fact, after the inefficient post-privatisation performance and failures to fulfil privatisation contract obligations, some of the contracts with companies privatised through MEBO were cancelled (Public register of unsuccessful privatisation deals that will be cancelled by the Privatisation Agency, Privatisation Agency, Bulgaria).

3. Key players: Washington Consensus institutions, anti-communist 'crony' web, and foreign investors

The *state officials* in privatisation bodies (Agency for Privatisation, ministries, etc.) were not neutral about the privatisation method chosen. 'Open' procedures (auctions, public offers) accounted for only 7% while 'closed' procedures (tenders, negotiations) were 93% of the total number of deals for the period 1993-99 (Privatisation Agency). The Council of Ministers was formally in charge of the privatisation of natural monopolies and a special list of companies, but de facto it was involved in many privatisation deals. In practice, there was dispersion of responsibilities of different decision-makers in the privatisation process. The legal and regulatory framework of privatisation allowed high state officials discretion and lack of transparency. There was no regulation regarding the selection of privatisation procedures. The method (procedure) of direct negotiations was the least regulated and most discretionary (in practice, most frequently applied by state officials!). The 'closed' procedures required a commitment of new owners concerning investment, number of employees, etc. that created a necessity of post-privatisation control by state officials. However, the post-privatisation control was very controversial. On the one hand, there were cases of discretionary state intervention in the private property-rights domain and potential corruption. On the other hand, the state officials were 'selective' regarding 'crony' and independent firms. *This is a typical case of the dual face of the state in transition – captured, weak (for the web of captor members) but bureaucratic, interventionist (regarding independent firms).* The final result of the privatisation process (*de facto* prevailing tenders and negotiations) was a low cash flow for the budget and rent-seeking activities by state officials.

The *anti-communist government* with Prime Minister Ivan Kostov was the first Bulgarian government since 1990 with a clear EU-accession and market-economy orientation. The currency board together with the new parliamentary majority excluding former communist parties greatly increased the stability in the country. This government was anti-communist but nevertheless the 'crony' relationship style of privatisation established by the former communist governments was going on. There was only a change of the 'crony' actors. A new 'crony' network 'Olympus' was established. However, many of the government leaders and politicians of the ruling 'anti-communist' coalition, Union of Democratic Forces, were well known faces from the very beginning of transition (for example, Prime Minister Kostov was a member of the government in 1991). *This can indicate that despite some policy differences between ex-communist (the Socialist party) and anti-communists, their origin at the beginning of transition and political behaviour in 1997-2001 showed a mutual interest to preserve the status quo.*

Foreign participation in the privatisation process was humble (***Table 7***). *Foreign investors* preferred green field investment. On the other hand, portfolio investments were negligible due to the undeveloped capital market. The Washington Consensus expectations regarding the foreign investment concerned the introduction of a new market-oriented style of management. For the time being, however, enterprises under foreign control have showed mixed performance. First, foreign investors with long-term traditions and reputation had the expected performance (like Solvay (chemicals), Union Miniere Group (copper), Brewinvest (brewery), etc.). Second, there exists another type of foreign investors, however, with specific features: (i) unclear origins of capital (sometimes a Bulgarian one!); (ii) a public unknown for the

Western market; (iii) based in off-shore zones, which is normal for the Western practice but not for transition countries (see for example, the case of Gad Zeevi (Israel), which privatised the Bulgarian national air carrier 'Balkan').

Finally, the driving force for the currency board establishment and for the policy design of the government in 1997-2001 were the *Washington Consensus institutions* (especially the IMF). According to some recent studies, the currency board introduction satisfies the IMF interests because it enables Bulgaria to service its foreign debt (for more details about the IMF role in post-communist countries, see Stone, 2000). The payments of the external debt were a first priority of the budget under real restrictive monetary and fiscal policies. The currency board story is out of the scope of the present analysis but these findings confirm the notion of 'methodological nationalism' and the need for studying globalisation factors as an essential part of national institutional changes.

From the point of view of the enterprise sector, the economic policy seemed to be aimed simultaneously at different objectives: of the international financial institutions (the IMF, the World Bank), of the market-oriented and the EU accession-oriented Bulgarian government, and of the agents with looting behaviour (the economic legacy of the previous ten years). For example, in the autumn of 1998, at the conclusion of the three-year agreement between Bulgaria and the IMF, the IMF emphasized the export demand while the government the domestic demand as the priority source of economic growth. In 1998, the report of the EU Commission on the progress of Bulgaria to accession mentioned corruption as a serious problem, but it remained on the agenda in the following years.

In 1997-2001, privatisation driven by international financial institutions led to mediocre results. After the general elections in June 2001, the new government (Primer Minister the former Bulgarian king Simeon II) prepared a public register of unsuccessful privatisation deals that the Privatisation Agency should cancel. According to different estimates, these deals are about 200 but for the time being the list consists of 48 new owners, including private owners after the MEBO scheme and foreign investors (source: Privatisation Agency).

D. Property-Rights Transformation Outcomes

The emerging ownership and control picture of the Bulgarian economy has been too complicated and changeable but two important characteristics can be outlined: (i) dual enterprise sector; (ii) ownership heterogeneity.

1. Dual enterprise sector

The most important aspect of the enterprise sector in Bulgaria in the 1990s is its duality. There are simultaneously two types of enterprises and two types of corporate culture in the Bulgarian economy: normal and 'transitional'. The first type shows a clear structure of property rights (newly founded private firms and privatised firms with market motivated owners). The others are corporatized state-owned enterprises (including the biggest state-owned loss-makers), state enterprises in process of privatisation, newly founded private firms and privatised enterprises with owners oriented towards the expropriation of state assets and other 'transition" attitudes. The grey economy and the household production for own consumption belong to the second group. The existence of the second type of enterprises and its interaction with the first type gives rise to a *dual economic culture*. The same economic agents have to show market-oriented behaviour with the market-oriented subjects and perverse behaviour on other occasions. The macroeconomic signals of the currency board are refracted through this culture. It is difficult for policy-makers to predict enterprise behaviour.

2. Ownership heterogeneity

The emerging ownership heterogeneity based on the state enterprise transformation is another important characteristic of corporate governance in Bulgaria. The concentration or dispersion of ownership, majority owner control or managerial control, the board of directors and other internal governance mechanisms are not

a reliable institutional basis of understanding and forecasts for business behaviour. In the Western practice, different governance mechanisms have been developed and a common characteristic of all surviving companies is that they have constrained the potential managerial opportunism. In transition economies under conditions of tremendous uncertainty, there has been managerial inclination to short-run company survival strategies. The long-run survival depends on access to investable funds and innovation. The basic property-rights structures observed and survival strategies are summarized below.

First, *corporatized state-owned enterprises.* The owner - the government - has withdrawn from control, and managers and other non-owners have discretion to decapitalise the enterprises in their favour. In the short run, managers adopt strategies for their utility maximization through primitive accumulation of capital at the expense of company state-owned assets (price transfer to 'crony' private firms, 'bad' credits and re-distribution of loans received for pet projects, outright looting, etc.). Under these circumstances, in the *short* run companies can survived accumulating payment arrears. In fact, the loss-making behaviour of companies has been tolerated from the state authorities. Unconditional financial bailout operations are typical policy measures, especially in the early transition years. State-owned enterprises survive living on bad credits thanks to this 'soft' budget constraints policy. The efficient corporate governance transformation of these enterprises is from control based on unestablished property-rights to fighting among interests groups for explicit corporate control and *privatisation*. However, the improved property-rights arrangements would be not relevant if soft credits prevail and companies would be able to seek survival there rather to satisfy consumers' demands.

Second, *privatised enterprises with dispersed ownership and perverse behaviour.* These are privatised enterprises with dispersed ownership. Their inefficient behaviour is shown not only by managers but also by the new controlling shareholders. The latter are typically not entrepreneurs and do not have owner's market motivation. The ex-privatisation funds transformed into holding companies after the *mass privatisation* are a typical case of this type of new private owners. How their subsidiaries survive? In the *short* run, in the following years after the mass privatisation in 1997, there has been re-distribution of funds among subsidiaries under the holding company control. However, neither shareholder value nor subsidiary restructuring is the driving strategy rather controlling shareholders desire to advance their own utility through tunnelling (channel money to their own accounts usually abroad). The further transformation of these enterprises is to ownership concentration and emergence of new objectives of owners. *Secondary privatisation* is due through internal mechanisms or capital markets.

Third, *privatised enterprises with concentrated ownership and perverse behaviour.* These are enterprises, whose ownership is concentrated, but their owners stand for a post-totalitarian corporate culture and pursue assets-stripping strategies. Typically these firms are privatised by *MEBO* schemes and are formally under insiders control after their privatisation. However, some foreign investors belong to this group too (for example, the Gad Zeevi case mentioned above). In the *short* run, these companies can survive selling their assets. The efficient development of these enterprises requires *secondary privatisation* (it can be through liquidation, too) and a change of owners.

Fourth, *privatised enterprises with dispersed ownership and market-oriented behaviour.* Ironically, this ownership structure, typical for the Anglo-American corporate governance models, is not typical in Bulgaria after the Washington Consensus driven privatisation. These are privatised enterprises with dispersed ownership whose inefficiency is due to a high degree of managerial discretion. Ownership concentration and introduction of *governance mechanisms* for disciplining managers, known in market economy, need to be introduced.

Fifth, *privatised enterprises with concentrated ownership and market-oriented behaviour.* These are enterprises where the behaviour of large shareholders is in favour of both short-run and long-run development. Here, the basic problem is not the contradiction between owners and managers, but rather that between large and small shareholders. Typically, *foreign investors* belong to this group (see, for example, the Solvay-Sodi and Union Miniere cases of large shareholder discretionary behaviour against small shareholders' interests (Bates, Cook, 2000). *Governance mechanisms* for protection of small shareholders are to be developed.

E. Capital Markets Emergence

For the time being the Bulgarian capital market is fragile in comparison with the securities markets developments in other post-communist countries (***Table 8***). Three stages of its evolution can be

outlined: (i) early transition beginning in 1992; (ii) after the mass privatisation program in 1996-97, (iii) after the general elections in June 2001, when former financial analysts in the London City became ministers in the new Bulgarian government.

In the early transition since 1992, the only legal framework regulating shares was the Commercial Code. There existed about twenty companies and about twenty stock exchanges. The outcome was the market crash in 1995; many companies went bankrupt and their founders and managers escaped abroad with the shareholders' funds.

The mass privatisation program in 1996-97 was the driving force of the further development of capital markets and their regulation. The Bulgarian Stock Exchange – Sofia (BSE-Sofia) began to function on 21 October 1997. The stock exchange initially functioned under the Law on Securities, Stock Exchanges and Investment Companies (1995), which was replaced by the Law on Public Offering of Securities (1 February 2000). Basic institutions established to regulate the market were: the Bulgarian Stock Exchange – Sofia (a semi-private institution for securities trading), the Securities and Stock Exchange Commission (a regulatory body overseeing securities markets, recently renamed as the State Securities Commission) and the Central Depository (registering transfers and shareholdings in companies).

The stock exchange activity was very small. Till the end of 1997 only three transactions were concluded. After that, following the mass privatisation, there was a sharp increase in the listed companies (1040) in 1998 and a following decline (861) in December 1999. The total market capitalization of all the listed companies amounted to BGL 1 702 billion that amounted to about 7,4 % GDP in 1999 (***Table 9***). However, these numbers cannot by themselves explain the real capital market maturity. For comparison, in the Czech Republic about 1716 companies traded on the Prague Stock Exchange in 1996, in Poland – only 253 companies traded on the Warsaw Stock Exchange, but the Czech experience was much more inefficient than the Polish one (see Coffee,1999).

Despite the regulatory framework establishment, striking traits of the Bulgarian securities market are as follows: (i) low credibility of the market, (ii) low liquidity; (iii) lack of efficient governance mechanisms. *First*, the Bulgarian Stock Exchange was divided into two markets: the official one (C, B and A market segments with listing requirements increasingly stringent and a market segment for corporate bonds) and a free market with listing requirements less stringent (see ***Table 9)***. Of 861 companies listed in 1999, only 32 have been listed on the more "qualitative" official market, and the reminder 829 companies were listed on the free market. But even among the companies listed on the official market there were only 3 in segment A (the most stringent requirements), 5 companies in segment B, and 24 companies in segment C. This means that the reputational integrity of the market as a whole was very low and the bulk of the companies placed there after mass privatisation could not fulfil more strict requirements for listening in higher market segments. *Second*, the illiquidity of the Bulgarian securities market is another important feature. The annual stock market turnover decreased from 1998 to 1999 by about 40 %. The main factors were limited stock supply because companies gained no advantages after being listed (because of additional disclosure rules requirements, decrease in managerial discretion, low probability of raising capital through equity market). There was little foreign portfolio investor interest, especially after the Asian and Russian crises in 1997-98. *Third*, the illiquidity of the market diminishes the role of the capital market as a disciplining device against the potential managerial opportunism. The market for corporate control, especially hostile takeover, cannot play its role of a governance mechanism because of concentrated ownership, lack of information about company shareholdings and lack of mechanisms for communication among minority shareholders.

However, the specific traits of the Bulgarian capital market described above can be understood only in the framework of mass privatisation based on the Washington Consensus policy to transition. The policy intentions of establishing many private owners *quickly* that would behave as rational private agents in securities markets gave rise to paradoxical results: (i) capital markets *institutions* were utilized not as a market place but only for formal registration of collusions among privatisation funds; (ii) the main obstacles to efficient company restructuring after mass privatisation were *private controlling* shareholders.

The stock exchange as a pseudo-market institution. Like board of directors' utilization in corporatized state-owned enterprises as a specific mechanism for looting and against company restructuring in the early transition, the stock exchange is another example that "institution-building" remedy is very important but not sufficient under the specific transition conditions. The Bulgarian experience shows how this 'market mechanism' could be used simply for imitation and for disguising the real purpose of mass privatisation. In Bulgaria, all the listed companies on the stock exchange were listed through the mass privatisation process and the main capital market activity of privatisation funds was re-distribution of

shares through private placement not mediated by the price mechanism. The basic tool was block trades of shares (trade involving more than 200 000 shares) and key goals were private benefits of fund managers, directors and controlling shareholders. The stock exchange was used only to register already conducted trades. These trades led to ownership concentration and dilution of minority stakes. Contrary to the 'conventional wisdom' that security markets have to be developed in order to resolve agency issues based on expecting separation of ownership from control, these markets themselves were utilized as a specific tool for company ownership concentration.

Threat of private controlling shareholders. In Bulgaria, the behaviour of privatisation funds after mass privatisation resembles both the behaviour of their Czech counterparts (well-known as 'tunnelling') and the behaviour of the board of directors and top-managers of corporatized enterprises in Bulgaria (simply looting) in the early transition. 'Tunnelling' includes transfer of company products (in corporatized firms) or both products and assets (in privatised firms) below their market price to private 'crony' firms, controlled by the same managers (or their relatives or 'cronies') which are in control of the original company. Sales and purchasing contracts are designed to go through these 'crony' firms, raking off profits from a given subsidiary.

The experience of other countries (for example, Russia) has also shown similar patterns of privatised companies decapitalization and minority shareholders expropriation. Another example is the Slovenian experience after mass privatisation when large institutional investors emerged and issues how to constrain their discretionary behaviour were on the agenda (Bainbridge, 2000). It can be concluded that: first, mass privatisation led to company owners aiming to obtain control and becoming controlling shareholder to exploit minority shareholders (by self-dealing transactions, withholding dividends, etc.). But this gave rise to a totally different concept of '*private owners'* not envisaged initially by the Washington Consensus policy. Second, even where mass privatisation outcomes were better (like in Poland till 1998) they were unstable and were due to state-created privatisation funds, highly constrained by regulation.

The described failures have limited capital market development. Newly established private firms cannot raise new capital through the public sale of new equity. The lack of development of the secondary market for shares of privatised companies has led to lack of capital needed for their restructuring. Finally, diversifying risk through portfolio investment in domestic companies is difficult. Only concentrated ownership and investments under private and majority control can be viable under the Bulgarian conditions. Capital flight has become rational business behaviour because of the lack of viable investment opportunities in the country.

F. Banking Sector Change

In Bulgaria, a two-tier banking system was established, the first tier covering the Bulgarian National Bank (BNB) and the second tier the commercial banks. In the 1990s, the Bulgarian banking system development was characterized by a steady increase in private banks and foreign participation (***Table 10***). At the end of 2000 about 80% of bank assets were privatised and the foreign investors' share of bank assets was 74%. The concentration in the banking system is high; the three largest banks (Bulbank, United Bulgarian Bank and DSK Bank) hold almost 50% of the total bank assets, incl. 36% of the total credits (Bulgarian National Bank, 2000). The present corporate investment finance is embarrassed by both fragile capital markets and the specific passive lending behaviour of Bulgarian banks. The share of the domestic credit of GDP decreased dramatically from 115% in 1996 to 18% at the end of 2000. This kind of bank behaviour can be explained by both the financial crisis in 1996 and conditions under currency board introduction since 1997.

In the period 1989-96, before the currency board establishment in July 1997, banks-firms relations were integrated into the system of primitive accumulation of capital among 'crony' private firms and different interest groups (Koford and Tschoegl, 1999; Caporale et al., 2001). In 1989-92, the first stage of the banking system development began. In 1990, the regional branches of the Bulgarian National Bank were transformed into state-owned joint-stock companies. The official version was fostering of competition and decentralization, but in fact, a process of illegal and hidden privatisation of bank sector had begun. In 1991, newly established *private* banks emerged. There was no new legislative framework for bank activities. The emerging web of communist – capitalists had used the institutional vacuum to decapitalize state-owned banks and transfer capital to establish new 'private' banks. Second, in 1992, two basic laws were adopted: the Law on the Bulgarian National Bank and the Law on Banks and Credit Activity.

However, the existing 'crony' links among bank controllers (the Parliament and the Bulgarian National Bank) and bankers led to a bulk of illegal bank operations.

The typical utility function of both bank managers and 'crony' firms' borrowers was credit maximization. The banking sector, like the real sector and the state, showed the same *dual behaviour*, typical of the Bulgarian transition. On the one hand, there was de facto unavailability of credits for the majority of private firms (independent ones). But on the other hand, there was a huge concentration of credits in a few 'crony' private firms (***Table 11***). Recent *ad hoc* investigation revealed that in 1989-97, 356 'bad' credits (each over DEM 1 million) were lent to only 274 'crony' agents. For 129 of these credits there was no collateral. The total sum was around DEM 2 billion (Trud newspaper, 14 January 2002). This gave rise to the bank crisis in 1996 and at the beginning of 1997, when 14 banks, whose balances accounted for 25 % of the consolidated balance of the Bulgarian bank system, were closed (OECD,1999).

The currency board, introduced in July 1997, established a new institutional framework of all economic agents, breaking off the inefficient links between the state and the banking sector, on the one hand, and the state and the central bank, on the other. Under currency board constraints the central bank cannot lend to the government, cannot refinance banks and has no monetary policy. Following the financial crisis in 1996-97 and more recently the accession talks and harmonization with the EU legislation, the law on the central bank was amended and improved and a new law on the commercial banking was adopted introducing efficient governance structures: consolidated supervision, stringent collateral requirements for large credits, increase of capital adequacy, etc. However, banks are overcapitalised (about 34% capital adequacy in the whole system that is quite higher than the 8% international requirements) and have soft liquidity constraints. The typical bank lending behaviour to the domestic sector is very passive, interest rate spread (difference between deposits and credits interest) is high (10-12%). Under low domestic treasury bills supply (because of practically always balanced government budget), *the Bulgarian banks mainly invest abroad*, especially in foreign banks deposits and foreign governments treasure bills. The bank assets abroad accounted for 2 billion EURO or 36 % of their assets (Bulgarian National Bank, 2000). However, the low banks credit activity hampers Bulgarian business and economic growth and under specific conditions could even undermine the Bulgarian currency board itself. In the whole enterprise sector, internal financing has been the most frequently used source of finance up to now, used by 89 % of MEBOs and 75 % of foreign and local investor-owned companies; debt finance was used in 42 % and 45 % cases, respectively and equity finance was a less important source of finance (Manev et al., 2000).

IV. Historical Experience of Developed Countries and Corporate Governance Design in Bulgaria

In Bulgaria, the actual corporate governance design sharply contrasts with the historical experience of corporate governance design in developed countries like the U.S at the end of 19 century, and pre-war and post-war Japan. *First*, in Bulgaria, the driving force of the transition was the *political class* (a specific social hybrid that can be described as "former communists-present capitalists"), the approach to corporate governance design was "top-down", based on non-transparent decisions of a small group of ruling people with rent-seeking behaviour. In a sharp contradiction to the Bulgarian political class based approach, in the US case, economic agents like investment bankers and investors were key actors designing new governance mechanisms in order to protect minority shareholders and company managers against a potential incoming hostile raider. This determined the "bottom-up" approach to corporate governance design with a very limited scope for political influence (Coffee, 2001). The Japanese experience shows that company managers, commercial banks and government (especially the Ministry of Finance) played a crucial role. That resembles a mixture of both the "bottom-up" approach observed in the American case and the "top-down" approach to transformation in transition economies like Bulgaria. *Second*, in Bulgaria, *international institutions* (IMF, World Bank, EU) and Western advisors were the main initiators of legislation transplantation, while in the U.S. legal changes can be seen as a result of lobbying forces efforts (coalitions including investment bankers and investors as well), stock market speculations and scandals were frequently a trigger to a legal reform. In the American case, the design of efficient corporate governance structures was based on private ordering and self-regulation (not on laws). *Third*, in both Japan and the U.S., private investors and companies have had a long-term track while in Bulgaria they have to be established. The Bulgarian managers of state-owned firms have never had the incentives of their private counterparts in the U.S. and the Bulgarian state agency for privatisation has never had the reputational capital needed in order to attract investors. In the Bulgarian case, there has been a *simultaneous process of both capitalist corporate governance system establishment and primitive accumulation of capital*. Fourth,

in both countries, Japan and U.S., the national development orientation of company owners and managers was a driving force for the development of the countries. However, in Bulgaria, there has emerged an *internationalist* ruling class motivated by values of a liberal international economic order.

Table 12 presents a historical focus on corporate governance *mechanisms* designed in Bulgaria and developed market economies. In Bulgaria, despite formal policy adherence to Anglo-American corporate governance, there is a striking difference between corporate governance design and the American historical experience. First, *mechanisms for protection of minority shareholders* are not developed in Bulgaria and also in Japan after the war. In salient contrast, these governance mechanisms were key elements in the early American stage of corporate governance design. Second, the *board of directors* as a governance device has been implemented in all the three countries. However, in the case of Bulgaria, this mechanism was not enough to constrain managerial opportunism and even worse, this mechanism was used as a specific institution not for development but rather decapitalization and assets stripping of state-owned enterprises. In the case of Japan, the board of directors' functions have been reshaped by implicit social norms stressing not on monitoring but on employee representation. Third, *implicit* governance rules are important institutions in both Bulgaria and Japan while in the American case they have had limited influence.

V. 'Catching-Up' Stage of Development and Corporate Governance in Bulgaria

The Bulgarian economy ten years later (like at the beginning of transition) was at a stage requiring to 'catch-up' with other advanced EU market economies (***Table 13***). In 2000, the Bulgarian GDP per capita was 24% of EU average. Some forecasts envisage that in 2015 Bulgaria will have 32% of EU average per capita assuming 4% annual GDP growth (WIIW, 2001). Such kind of intellectual exercises are very risky (imagine who expected the communist collapse 15 years ago), nevertheless they focus our attention on the actual issues, the backwardness of the Bulgarian economy and the high-rate growth need. Rapid accumulation of large quantities of cheap capital is crucial to support the catching-up growth and different corporate governance systems can be used. For this purpose neither corporatization and privatisation, nor the private sector development are foremost tasks, but rather a policy for promoting a high saving rate and financing business expansion (Taylor, 1992; Morck, Yeung, 2001). However, the real results of the Bulgarian transition in the 1990s were totally different (***Table 14***). The gross savings and gross fixed capital formation as a share of GDP declined in the 1990s and reached 10%, respectively 16%, in 2000. The domestic credit sharply fell from 119% in 1991, and 115% in 1996 to 18% of GDP in 2000. The analysis in the previous sections definitely shows that the banking sector and capital markets were not efficient devices for business finance. The striking outcome of the transition policy in Bulgaria ten years later was the dependence of the Bulgarian economy on external financial sources (FDI, loans, etc.). Some policy lessons about 'catching-up' factors could be drawn from both the Bulgarian communist 'catching-up' experience after the Second World War and the Washington Consensus based primitive accumulation of capital in the early 1990s.

A. 'Catching-up' under Communism after World War II

After the Second World War Bulgaria carried out a specific 'catching up' policy under the Soviet Union occupation forces impact. *First*, accumulation and centralization of capital was achieved by forcible industrial *nationalization* and land cooperation under the communist revolutionary slogan: 'Expropriation of expropriators'. The basic importer of new technologies was the Soviet Union. *Second*, the key institutions for 'catching up' were the emerging 'socialist' *public ownership* and totalitarian state. The change of ownership from private hands to 'more progressive' public ownership was the most important driving idea at the beginning of 'communism building'. This obsession was the key difference between the communist type of post-war 'catching up' growth and East Asian models. *Third*, financial institutions were nationalized too, and the central plan and different *totalitarian state* institutions emerged. *Fourth,* however, despite the strong capital control constraints the general utility functions of the emerging communist party elite were not oriented to the national development but rather to Moscow directives.[25]

[25] There was a forcible *adverse social selection* in the early years of communism. During the first months of 'communist freedom' in 1944 tens of thousands of Bulgarian intellectuals, bankers, priests, journalists, teachers, craftsmen, peasants, etc., belonging to the economic, political, intellectual and cultural elite of the nation, were killed

The striking features of the communist 'catching-up' process were: (i) forcible nationalization as a tool of accumulation of capital; (ii) hypertrophied public ownership and overestimation of ownership change *per se*; (iii) emerging totalitarian state institutions, and (iv) a new pro-Soviet communist elite. The emerging totalitarian institutions were suitable to complete the accumulation and centralization of capital but were not capable of establishing efficient management and governance structures. In the early 1960s in Bulgaria, a need to improve the existing governance structures arose (for analysis of corporate governance reforms in the 60s and 80s, see Peev,1995). The entrenchment of top communist nomenclature leaders and the nature of the totalitarian state terror can explain why only the natural generation change in the Soviet Union in the 80s did manage to trigger reforms leading to the communist collapse.

B. 'Catching-up' under Washington Consensus Based Transition (1990-1996)

In the early transition period, 'catching-up' with the developed market world was based on a policy deserving the name 'vulgar Marxism and vulgar Coase-ism' (as Janos Kornai stated in a recent article, Kornai,2001). The transition to a market economy in Bulgaria resembles the early post-war years of 'communist building'. It seems that the approach remained the same, only the *direction* of ownership change was different. *First*, in the early 90s, the basic source of capital accumulation of the domestic private sector (newly established firms and privatised ones) was the state sector. However, this capital was not directed to absorb technological knowledge from outside but rather to 'escape' from the country. *Second*, there were no institutions for 'catching up'. Private initiative should have played the main role. The state withdrew its activities from the economic life and the bank system was weak and orientated to state assets re-distribution and looting. *Third*, a salient feature of this type of 'transition' was capital flight. New political ruling class (mostly from former communist nomenclature) has preserved internationalist attitudes under the new post-communist conditions.

The basic traits of the process described above were as follows: (i) overestimation of privatisation and private sector establishment and private initiative; (ii) preservation of political elite orientation to 'liberalization' rather than national development; (iii) lack of policy prescriptions for absorbing the knowledge needed for 'catching up'; (iv) lack of institutions designed for 'catching up'. The post-communist *creative destruction* process was characterized by: a) destructing totalitarian state, public ownership, state control in state-owned firms, and state regulatory functions; b) creating new private owners but without a national strategy or policy for national development, absorption of knowledge and establishment of institutions for 'catching-up'.

C. 'Catching-up' since 1997

During 1997-2001, a currency board arrangement, starting negotiations for EU membership and two new governments shaped a new framework of economic policy in Bulgaria. In fact, the *most important positive* event in the recent Bulgarian history since the beginning of transition was the decision of the European Council in Helsinki on 10-11 December 1999 to start accession talks with Bulgaria. As a result, Bulgaria significantly reformed and aligned its commercial legislation with the European Community legal framework. Recent surveys reveal that the Bulgarian commercial laws have been improved consistently and can be characterized as reasonably good for supporting investment and other commercial activities (see EBRD,2001; Peev, 2000). This has led to increased public confidence in the rule of law. The commercial law of Bulgaria is perceived as being at the same level as that of Estonia, Latvia, Lithuania, Poland, Slovenia, Hungary, Croatia, and Romania. However, the legal reform introduced is merely a necessary condition for corporate governance development but not a sufficient one and there still exists a gap between law development and law implementation and enforcement. The positive tendencies observed for the so-called 'institutions building' focusing attention on corporate governance issues are not a foremost task from

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by Soviet collaborationists in Bulgaria. Under special Moskow orders politicians from different parties like Nikola Petkov (Bulgarian Agrarian Party), Trajcho Kostov (Bulgarian Communist Party), different right-wing leaders were executed through patched up lawsuits. The real goal of fighting against 'capitalism' in Bulgarian after the war was destroying the Bulgarian patriots and appointment of *mediocre but loyal* to the Soviet Union puppets.

a 'catching up' perspective. The crucial issue becomes the role of the state regarding 'catching-up' accumulation of capital.

The new government elected after the general elections on 17 June 2001 has encountered specific difficulties regarding 'catching-up' to EU market economies. Theoretically, the efficient 'catching-up' policy in Bulgaria could be determined by the following cause-effect relationships: 1) establishment of coalitions oriented to national development (this is a crucial point); 2) consolidation of state institutions for a strategy for national development aiming at some key issues: (i) accumulation of psychical and human capital, including human capital development through education, learning, etc. (ii) development of institutions (including bank system) for accumulation of capital and enterprise finance, encouragement of the entrepreneurship; (iii) policy for technological capabilities development, including technology and knowledge importation, active industrial policy for sectoral development; (iv) active government policy for fostering demand through public investments, controlling foreign trade, capital control in order to keep savings in the country, etc. However, the measures shown above are drawn from the *historical* experience of successful and non-successful 'catching-up' stories (see, for example, the Japanese experience from 1867 to the post-war times, Odagiri and Goto (1996) . The real challenge before policy-makers in Bulgaria is how to adopt these lessons to *globalisation* constraints facing their policy at the beginning of the new century.

First, in 2001-2002, the positive great expectations are connected with the emerging new coalition for collective action – a new prime-minister (the former Bulgarian King Simeon II), his ministers (former financial analysts in the London City) and their ties to the international financial world. Second, at the same time, however, *country-specific* globalisation factors, like IMF discretion in the Bulgarian internal affairs (based on the huge domestic external debt), EU enlargement policy requirements (based on the Bulgarian negotiations talks and policy for accession), also currency board arrangements have significantly constrained the potential Bulgarian 'catching-up' policy. The four key issues stated above encounter specific difficulties in Bulgaria.

(i) After the wasted years of primitive accumulation of capital, state firms and banks decapitalization and of capital flight, the basic problem has been the scarcity of domestic capital. Foreign investment, foreign loans and proceedings from a new style of privatisation (a more transparent one) could be the main sources of capital. However, this has significantly decreased government discretion for an independent 'catching-up' policy.

(ii) The prevailing foreign banks in Bulgaria (and requirements of international financial institutions for privatisation of the remaining state-owned banks) narrows the scope of government discretion for a more active national policy and establishment of a bank system in lines of Japanese and East Asian concentrated banking models. The currency board arrangement and the practical lack of monetary policy of the Bulgarian National Bank also decrease government discretion. The restrictive monetary policy under a currency board provided an increase in the monetary supply mainly by external sources: increase in net exports, increase in foreign investment in new private firms, revenues from privatisation, portfolio investments, loans from international financial institutions. The restrictive fiscal policy set the payments of the external debt as the first priority of the budget.

(iii) During transition years, despite some government programmes (Investment Programme for the period 1998-2001; Strategy for the development of Bulgarian high-tech industry in 1999; specific restructuring programmes applied for some sectors etc.), a prominent feature of the industrial policy has been its passivity and bureaucratic carelessness to real sectoral development. The new government has intended to carry out more active sectoral policy but the EU requirements for accession are restrictive in this field.

(iv) Since 1997, the external trade was further liberalized. The current payment regime was also liberalized as in September 1998, the government assumed the obligations under item 8 of the Statute of the IMF. The currency regime led to further liberalization of the capital flows though with noticeable restriction to the export of capital from Bulgaria. At the same time, the inherited profitability of the Bulgarian economy was low, and many products were uncompetitive both in the domestic and foreign markets. Each attempt of the Bulgarian government against liberalization measures would run against IMF opposition.

VI. Failures of Washington Consensus and Searching New Approaches

The experience of reforms in countries like China, Eastern Germany, Estonia, Poland, Hungary, and Slovenia show that under certain circumstances some transition countries could perform better than the others. Apart from the different initial conditions and the historical background regarding the former Russian Empire and the geographical remoteness from Brussels, these countries have experienced specific *policy* approaches to corporate governance design that can be summarized in some points. Poland adopted a slow mass privatisation programme designed carefully by its government. Hungary preferred cash privatisation, privatising case-by-case state-owned enterprises and showing great transparency to the public. Estonia had a unique experience (deriving from the fight for freedom against the Russian occupation) introducing currency board at the very beginning of transition, adopting the German style of privatisation and inviting experts from the German agency for privatisation *Treuhandanstalt* for advisors. In Slovenia, the government adopted a special strategy about which firms can be privatised and which not. The Eastern Germany privatisation approach is probably the most specific. In this case there was both FDI from the Western Germany and import of human capital (about one million specialists, lawyers, top-managers, professors,etc., including descendants of German entrepreneurs who had left East Germany after the World War II). The experience of China shows that national development can be successful under a communist party ruling and when competition fostering is a more important task than privatisation. The picture observed is quite complicated but some lessons can be outlined. Better performance is typical of countries which: (i) preserve strong *government* commitment to privatisation policy (carefully designing privatisation strategies, national industrial structures priorities, etc.); (ii) import both *financial and human* capital; (iii) preserve their *national* development priorities against foreign influence.

Comparing these developments with both the Washington Consensus prescriptions and the Bulgarian experience, one can see the striking difference. *The government active involvement in corporate governance design, human capital development and even human capital import, and national development (but not just privatisation, stabilisation, liberalization) really matter.*

The overview of the Washington Consensus policy failures themselves is not a subject of this study. However, without outlining some systematic policy flaws it would be impossible to understand the particular failures of the Washington Consensus in the field of corporate governance.

Internal factors/external goals dichotomy. First of all, there was an intrinsic contradiction between the *normative* frame of reference of this policy (adherence to global normative objectives) and the *explanatory* frame (focusing mainly on national factors as contributing for a country performance). In this respect, Gore (1996) defines the basic explanatory method of this policy as "methodological nationalism" and states that: "Explanations which are methodologically nationalist try to explain economic and social trends in countries, basically by reference to facts about the countries themselves" (Gore,1996: 80). *First*, this approach overestimates the impact of internal factors and assumes that countries face *the same* external environment. Differences in their performance have been considered to be due to the internal factors. External shocks in transition (as for example former CMEA market collapse) are understood as changes of their general external environment and are to be common for all the transition countries. But these assumptions sharply contradict the transition reality: (i) the origins of transition are based on internationalist political elite coming to power in mid 80s; (ii) international financial institutions and developed countries have different interests and policies in different transition countries and "external" environment is not neutral.

Second, this approach assumes *national performance* as a result of internal factors, especially domestic policy. National governments are taken to be like rational individuals with strategies and goals to pursue national interests. However, under a turbulent transition environment narrow political interests have been the actual driving force of unstable governments. In the case of Bulgaria, governments have had a low degree of discretion and external advisors have frequently reshaped the national policy based on the aid regime of the IMF and the World Bank. Access to donor funds has become conditional to the policy of 'structural adjustment'.

Third, adherence to global normative objectives, principles and norms (economic liberalization) determine which policy is "rational", "good" (as fast openness of economy) or "bad" (as selective active industrial policy). Here the key defect of this policy can be found. *Its goal is not an efficient long-term country development based on specific national interests (despite magical slogans like "free market" and "structural adjustment") but rather economic liberalization itself becomes both an objective and a means to transition.*

Failures in corporate governance design. The Washington Consensus policy approach to corporate governance transformation in transition countries is based on the presumption that the ownership

transformation is not just a necessary condition of market economy, but sufficient one (Kornai, 2000). This approach to ownership and control structures and their effects on firm performance, encounters difficulties to explain the real business behaviour in transition economies. Some of these *explanatory analysis* failures are presented below.

(i) State versus market. The main dilemma of this policy is state or markets and the "right" answer is that the market rationality is superior to the state intervention. However, the real issue is not about state versus market rather the specific state and markets interactions promoting national development.

(ii) Ownership and performance. First, the main issue is whether relationship between ownership structure and performance under transition conditions can be interpreted as causal. Firms, which are selected for privatisation, are not selected randomly. There would be reverse causality from performance to privatisation. The differences in privatisation rules across regions and countries can determine foreign ownership structure and insiders-outsiders control structures in general. Second, *state sector - private sector dichotomy*. The typical relationships between private firms established de novo and state owned enterprises are rather between victim and vampire than between equal economic agents. Third, *privatised firms – state-owned firms' dichotomy.* Some private owners are as inefficient as the former state owner after privatisation. By definition privatisation is a political process directed to efficient reallocation of resources. However, in many cases the privatisation process only leads to national wealth re-distribution. Many privatised firms are run by kleptocrats with aiming actually at plundering the firms' assets and to transfer money abroad. Privatisation is misleading concept. The real economic phenomenon is wealth re-distribution with *random consequences* about efficient firm performance.

(iii) Insiders control – outsiders control' dichotomy. The distinctions made between insiders and outsiders have rather artificial nature in a transitional context. Insiders and outsiders are usually described as groups with distinctive interests. But in fact, within these groups there are significant differences - between young and old workers, between top and other managers. Besides, there exist wheels within wheels type of interests of the top managers and outsiders that are informal and frequently mean evading the law. Therefore, they are difficult to detect. By definition enterprises privatised by MEBO scheme are under insiders control. In fact, the finance sources for privatisation belong to groups of interest outside the enterprise. Managers are only their 'post boxes' and 'puppets'. The real control is held by outsiders.

(iv) Transitional institutions with transitional functions. New established private and state banks, corporatized state-owned companies, board of directors are new institutions that should have aimed at increasing either competition or managerial incentives for restructuring. However, these new so-called 'market' institutions were designed and simply used for state-enterprises decapitalization. Conventional market economy terminology leads to misunderstanding of emerging post-communist 'crony' relations.

(v) Reallocation and restructuring. The basic observed facts of ownership evolution are rather prolonged state enterprises decapitalization than exit. There are two types of private firms established *de novo*, independent ones and 'crony' firms with close political connections. In fact, the process of reallocation is characterized by primitive accumulation of capital from state firms to private ones. Important stages of state enterprises restructuring and ownership evolution are: 1) decapitalization; 2) *primary* privatisation; 3) resale and *secondary* privatisation; 4) restructuring, exit or nationalization. After primitive accumulation of capital, private firms have met two options in middle term, either to restructure or to exit.

Finally, as regards the Washington Consensus policy normative evaluation failures, "crony" capitalist motivation for domestic state firms decapitalization and capital flight can be understood from international liberalization norms viewpoint as a "rational" and even "good" market-oriented corporate culture (to invest in developed financial markets than to fragile domestic ones). However, from the point of view of the national development and national interest this behaviour has led to a national disaster.

About ten years after the beginning of transition, searching new policy ideas, lessons and theoretical approaches has become the actual agenda of corporate governance in transition. The recent financial crises (East Asia in 1997, Russia in 1998) have had significant effects on the search for new policy ideas and propositions for both transition countries and developing countries corporate governance design. Josef Stiglitz argues that a "post-Washington Consensus" policy has to be developed. The new approach should focus on: (i) institution building, (ii) human capital and sustainable long-term democratic development, (iii) people participation and consensus-building as the driving force for change (Stiglitz, 1998). This approach preserves the principles of open economy and competitive markets. Key tasks are establishment of an efficient system of corporate governance and corporate finance, capital markets, and financial sector development.

VII. Concluding Notes

The key lesson from the Bulgarian transition story in the 1990s is that the *unhistorical* approach to corporate governance design in transition does not work. The basic traits of this approach are as follows: (i) the historical experience of corporate governance design in developed countries does not matter (underestimating the spirit of nationalism as a driving force for national development; (ii) the 'catching-up' policy of developing countries does not matter (underestimating the role of the state); (iii) the historical experience of countries 'building communism' after the Second World War does not matter (underestimating the initial transition conditions in the early 1990s).

The emerging corporate governance system in Bulgaria has been neither Anglo-American (market-based) nor bank-based. The transition outcome has been rather *'crony' relationship-based* corporate governance system. The striking features of this system are as follows: (i) a dual enterprise sector, (ii) ownership heterogeneity; (iii) fragile capital markets; (iv) pervasive bank lending behaviour; (v) globalisation factors discretion.

Some specific outcomes of the study are as follows.

First, as regards the Washington Consensus, corporate governance design in Bulgaria in the early transition was *partly* based on policy prescriptions by Western and American advisers and directed to convergence to market economy models of corporate governance but these prescriptions themselves: (i) contravened the American historical experience in designing corporate governance; (ii) contravened the historical experience of successful non-communist countries in 'catching-up'; (iii) resembled the Bulgarian communist property-rights transformation after World War II. The basic *traits* of the Washington Consensus policy in the 1990s were as follows: (i) overestimation of privatisation and private sector establishment and private initiative; (ii) preserving of political elite orientation for 'liberalization' rather than national development; (iii) lack of policy prescriptions for absorbing of the knowledge needed for 'catching up'; (iv) lack of institutions designed for 'catching up'. The post-communist *creative destruction* process was characterized by: a) destructing totalitarian state, public ownership, state control in state-owned firms, and state regulatory functions; b) creating new private owners but without national strategy and policy for national development, absorbing of knowledge and establishment of institutions for 'catching-up'.

Second, concerning primitive accumulation of capital, in the early transition years in Bulgaria, the 'internal contradiction' (Mansur Olson) of the enormous power of *parasitic* forces for collective action (the emerging communist-capitalist web of former top communist *nomenklatura*, totalitarian secret services, etc.) was observed. These forces were expected to design efficient corporate governance system (ownership, control, legal and regulation environment) and simultaneously to preserve the status quo, their power. This created the *dual* character of corporate governance design in transition: (i) corporatization should have been a process of transformation of socialist state enterprises in order to establish more efficient governance structures but de facto it was a corporate governance change for state-owned companies looting; (ii) privatisation should have been a transfer of state assets to private firms to enhance allocative efficiency but in fact it was designed to loot state assets or to transfer them to 'crony' private firms; (iii) the new private sector established both independent private firms and also 'crony' private firms aimed at state assets expropriation; (iv) the legal system and law enforcement should have been designed to constrain insiders and the totalitarian state and to defend creditors and shareholders, but de facto they led to weak, captured state and strong captors and 'crony' firms. Capital flight was an essential part of this process due to internationalist attitudes of the communist-capitalist web and property-rights uncertainty.

Third, regarding 'catching-up' accumulation of capital, the efficient 'catching-up' policy in Bulgaria could be determined by the following cause-effect relationships: 1) establishment of coalitions oriented to national development (this is a crucial point); 2) consolidation of state institutions for a strategy for national development aiming at some key issues: (i) accumulation of psychical and human capital, including human capital development through education, learning, etc. (ii) development of institutions (including bank system) for accumulation of capital and enterprise finance, encouragement of the entrepreneurship; (iii) policy for technological capabilities development, including technology and knowledge importation, active industrial policy for sectoral development; (iv) active government policy for fostering demand through public investments, controlling foreign trade, capital control in order to keep savings in the country, etc. The challenge before policy-makers in Bulgaria is how to adopt this policy to *globalisation* constraints decreasing government discretion, namely: a) servicing of the external debt as the

first priority of the budget under restrictive fiscal policy; dependence on foreign investment, foreign loans and proceedings from privatisation as the main sources of capital; (b) prevailing foreign banks in Bulgaria; (c) dependence on external sources for the monetary supply under a currency board: increase in net exports, increase in foreign investment in new private firms, revenues from privatisation, portfolio investments, loans from international financial institutions; (d) EU requirements for accession, especially restrictive industrial policy; (f) last but not least IMF loans conditionality and liberalization policy required.

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Table 1. The Transition Recession

Countries	Consecutive years of output decline	Cumulative output Decline	Real GDP, 2000 (1990=100)
CSB*	3.8	22.6	106.5
Albania	3	33	110
Bulgaria	4	16	81
Croatia	4	36	87
Czech Republic	3	12	99
Estonia	5	35	85
Hungary	4	15	109
Latvia	6	51	61
Lithuania	5	44	67
Poland	2	6	112
Romania	3	21	144
Slovak Republic	4	23	82
Slovenia	3	14	105
CIS*	6.5	50.5	62.7
Armenia	4	63	67
Azerbaijan	6	60	55
Belarus	6	35	88
Georgia	5	78	29
Kazakhstan	6	41	90
Kyrgyz Republic	6	50	66
Moldova	7	63	35
Russian Federation	7	40	64
Tajikistan	7	50	48
Turkmenistan	8	48	76
Ukraine	10	59	43
Uzbekistan	6	18	95
Output decline during the Great Depression, 1930-34			
France	3	11	n.a.
Germany	3	16	n.a.
United Kingdom	2	6	n.a.
United States	4	27	n.a.

n.a. Not applicable
* CSB – Central and Southeastern Europe and the Baltics, CIS – Commonwealth of Independent States.
Simple average, except for the index of 1990 GDP, which shows population-weighted averages.
Source: World Bank 2002

Table 2. Bulgarian Economy in the 1990s (some indicators)

	1991	1992	1993	1994	1995	1996	1997	1998	1999
GDP Growth (%)	-11.7	-7.3	-1.5	1.8	2.1	**-10.9**	-6.9	3.5	2.4
Inflation (CPI, end of period, %)	473.9	79.6	63.2	121.9	33.1	**310.8**	578.4	1.0	6.2
Base Interest Rate (end of period, %)	54.0	41.0	52.0	72.0	34.0	**180.0**	6.7	5.1	4.46
Foreign debt/GDP (%)	168	127	109	129	73	**243**	91	72	78
Private sector (share of GDP, %)		26.0	34.0	40.0	48.0	**52.0**	59.0	65.0	65.0
Privatisation (USD mn)			22,0	134,2	26,0	**76,4**	421,4	155,8	305.7

Source: National Statistical Institute, Bulgarian National Bank.

Table 3. GDP of the 'first-wave', 'second-wave' transition countries and some other countries in 1999, USD billion

	at current exchange rates	Per capita, EU 15=100	Index, 1990=100
A. Economies in transition			
'First wave'			
Czech Republic	53.1	62	96.5
Estonia	5.2	38	85.7
Hungary	48.9	53	102.7
Poland	154.7	42	137.6
Slovenia	19.6	73	113.3
'Second wave'			
Bulgaria	*12.0*	*24*	*74.9*
Latvia	6.3	29	57.8
Lithuania	10.6	31	65.6
Romania	34.0	28	79.6
Slovak Republic	18.8	49	104.2
Other transition economics			
Croatia	20.1	33	82.3
Macedonia	3.4	21	92.5
Ukraine	30.8	16	40.8
Russia	181.8	32	59.4
B. EU and other developed industrial states			
EU-15	8511.0	100	117.8
Greece	125.6	69	120.6
Portugal	109.0	72	124.9
Spain	595.2	80	122.4
USA	9221.8	143	132.3
Japan	4366.9	120	112.8

Notes.' First and second wave' transition countries – division of the candidate countries for the EU membership, based on the decision of the EU in December 1999. *Source:* WIIW (2000)

Table 4. Bulgarian Post-Communist Transition: Some Basic Stages

Key players / Years	Catching-up Accumulation of Capital	Globalization Factors	Primitive Accumulation of Capital	Actual Policy Objectives	Corporate Governance and Institutional Change
	Coalitions for National Development	Washington Consensus, EU Institutions	Communist-Capitalist Web		
85-89	3*	2	1	foreign debt maximization	hidden privatization
89-91	3	2	1	maximization of primitive accumulation of capital	corporatization, hidden privatization, private firms, establishment
92-94	3	2	1	maximization of primitive accumulation of capital	cash privatization, illegal privatization
95-96	3	1	1	maximization of both primitive accumulation of capital and foreign debt servicing	financial crisis
96-97	3	1	2	maximization of foreign debt servicing	mass privatization, currency board
97-99	3	1	2	maximization of foreign debt servicing	MEBO privatization, bank privatization, stock exchange
2000-1	3	1	2	maximization of foreign debt servicing	legal framework harmonization to EU

Note. * Priority of utility functions of players in actual policy implementation. Index ranges from 1, indicating the first importance, to 3, indicating little importance.

Source: Author's studies.

Table 5. Privatization in Bulgaria

	1993	1994	1995	1996	1997	1998	1999	2000	2001	total
	Percentage of the state assets that were privatised									
Cash Privatization	0.37	1.63	1.07	4.09	3.78	4.48	16.97	4.43	1.12	37.93
Mass Privatization					14.58					14.58
Total	0.37	1.63	1.07	4.09	18.36	4.48	16.97	4.43	1.12	52.51
	Percentage of the state assets due to be privatised									
Cash Privatization	0.56	2.47	1.62	6.19	5.72	6.78	25.69	6.70	1.70	57.44
Mass Privatization					22.08					22.08
Total	0.56	2.47	1.62	6.19	27.8	6.78	25.69	6.70	1.70	79.52

Source: Privatization Agency

Table 6. Consolidated Financial Indicators of the 20 Largest Holding Companies (ex-privatisation funds) in Bulgaria

	(thousand Bulgarian levs)		
	1998	1999	2000
Assets	784 093	938 038	855 056
Revenues	612 953	702 243	834 176
Profits	40 490	-13 897	-3 991
Long-term debt	47 688	59 256	97 893
Short-term debt	113 252	162 886	194 774

Source: State Securities Commission

Table 7. Foreign Investments in Bulgaria (USD million)

Year	Privatisation	Portfolio	Greenfield	Total per year
1992			**34**	**34**
1993	**22**	**n.a.**	**80**	**80**
1994	**134.2**	**n.a.**	**76**	**200.2**
1995	**26**	**n.a.**	**136**	**162**
1996	**76.4**	**n.a.**	**180**	**256.4**
1997	**421.4**	**29.7**	**185**	**636.1**
1998	**155.8**	**64.2**	**400**	**620**
1999	**305.7**	**53.1**	**447**	**805.7**
TOTAL	**1141.5**	**147**	**1538**	**2794.4**

***Source*: Foreign Investment Agency**

Table 8. Post-Communist Countries Stock Exchanges: Overview

	Turnover (USD mn)			Market Capitalization (USD mn)		
Country	**1998**	**1999**	**2000**	**1998**	**1999**	**2000**
Bulgaria	146.11	5.8	4.11	144.32	102.49	129.09
Croatia	100.04	68.81	189.08	2928.58	2508.85	2742.43
Czech Republic	4725.69	3933.79	6650.03	10430.79	10582.93	9746.16
Estonia	690.99	280.39	305.86	519.39	1789.28	1812.76
Hungary	16037.11	13454.57	12078.35	13791.36	16108.97	11908.44
Latvia	88.65	43	272.69	385.01	390.87	563.31
Lithuania	222.1	308.47	201.87	1074.12	1138.44	1587.65
Romania	151.26	100.99	56.52	356.59	313.69	363.98
Poland	8913.37	11139.37	19305.44	20461.09	29576.8	31428.61
Slovak Republic	1012.02	478.03	533.93	650.48	459.97	436.18
Slovenia	789.29	914.43	646.6	2984.94	2854	3099.65

Source: Capital Press

Table 9. Capital Markets in Bulgaria (1999)

	Official market (1)				**Free market (2)**	**Total (1+2)**
	A Segment	B (Parallel market)	C (Provisional market)	Bond market		
No. of listed Companies	3	5	24	1	828	861
Market capitalization in BGLev (mn)	58	75	141		1 428	1 702
Market capitalization in EUR (mn)	29	38	72		868	1 008
% GDP (GDP 22 780 mn BGLev)	0.25	0.33	0,62		6.3	7.47

Source: See Bates and Cook (2000).

Table 10. Banking System in Bulgaria

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
No. of banks	70	53	56	37	42	44	45*	34	34	35
No. of privately owned banks	1	3	6	10	18	22	23	28	29	29
Foreign Banks	0	0	0	0	2	4	7	9	10	19
Market share (assets) of largest banks (no. of banks in parenthesis)	n.a	77.8% (6)	74.8% (8)	81.6% (13)	78.5% (13)	74.9% (7)	67% (7)	75.4% (7)	70.4% (7)	70.2% (7)

* bank in liquidation are included
Source: BNB Annual Reports (see, Caparole, 2000)

Table 11. Concentration of commercial credit to the private sector in Bulgaria, December 1995

Amount of loan (BGL'000s)	< 100	100 – 1 000	1 000-5 000	5 000-20 000	20 000-50 000	50 000-100 000	>100 000
Share of credit (%)	0.00	0.03	0.08	0.13	0.13	0.12	0.49
Share of number of loans (%)	0.27	0.41	0.19	0.08	0.03	0.01	0.01

Source: BNB Monthly Bulletin (Bulgarian edition), No. 6, 1996; OECD, 1997.

Table 12. Corporate Governance Design: A Historical View to Anglo-American Model

Protection of minority shareholders:	**Bulgaria***	**U.S.****	**Japan*****
- investment bankers	no	yes	no
- reputational capital pledge			
by bankers to issuers	no	yes	no
- stock exchange	fragile	yes	
- disclosure rules	no	yes	no
Market for corporate control	no	yes	no
Board of directors	yes	yes	yes
Implicit norms as a basic mechanism	yes	no	yes

Notes. * - Bulgaria – in the early 1990s;
** - US at the last quarter of 19th century
*** - Japan – pre-war and post-war experience

Table 13. GDP per capita at current PPPs (ECU/EUR), from 2001 constant PPPs

	1990	1994	1995	1996	1997	1998	1999	2000	2005	2010	2015
Bulgaria	33	27	28	25	23	23	23	24	27	29	32
Romania	36	30	32	33	31	28	27	27	29	32	35
Hungary	49	46	46	46	48	49	51	53	59	65	72
Russia	57	36	34	33	33	30	31	33	37	40	45
Germany	102	110	110	107	108	107	107	106	106	106	106
Austria	109	111	110	112	111	112	112	112	112	112	112
Greece	60	65	66	66	66	66	67	68	68	68	68
EU (15) average	100	100	100	100	100	100	100	100	100	100	100
Japan	114	116	116	119	119	112	110	108	108	108	108
USA	148	148	144	147	150	152	153	156	156	156	156

Source: The Transition Economies: Externally Conditioned Improvements in 2000, Slowdowns and Adjustments Likely in 2001 and 2002, WIIW, 2001, p.34

Table 14. Dynamics of Credits, Gross Fixed Capital Formation and Savings in Bulgaria (1991-2000)

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Domestic Credit (mn Bulgarian lev)	160.8	242	398	543.7	634.7	2011	5136	4227	4237	4654
Gross Fixed Capital Formation (mn BGlev)	24.64	32.6	38.7	72.33	134.3	238.5	1932	2496	3632	4111
Gross Savings (mn Bulgarian lev)	24.8	25.1	17.7	36.5	95.95	148.8	2695	2494	2276	2530
Gross Domestic Product (mn Bulgarian lev)	135.7	201	299	525.6	880.3	1749	17103	21577	22672	25454
Domestic Credit/GDP	119%	121%	133%	103%	72%	115%	30%	20%	19%	18%
Gross Fixed Capital Formation/GDP	18%	16%	13%	14%	15%	14%	11%	12%	16%	16%
Gross Savings/GDP	18%	12%	6%	7%	11%	9%	16%	12%	10%	10%

Source: IFS.