

OWNERSHIP AND CONTROL STRUCTURES IN TRANSITION TO "CRONY" CAPITALISM: THE CASE OF BULGARIA¹

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Introduction

The Washington Consensus policy (privatisation, liberalisation, stabilisation) to transition countries is based on the presumption that the ownership transformation is not just a necessary condition of a market economy, but a sufficient one (Kornai, 2000). The emerging system, based on this policy of ownership and control transformation in Bulgaria, can be described as 'crony' capitalism and includes the following specific traits: firstly, lack of, or undeveloped institutional constraints on discretionary managerial behaviour such as property-rights, governance structures, market institutions. Secondly, post-socialist rent-seeking culture. Thirdly, economic agents are quasi-state officials, quasi-owners, and quasi-managers with a short-term existence. Fourthly, the objectives of new owners of privatised enterprises are not profit-maximising. Fifthly, winners in the specific transitional competition are these persuading objectives to asset-stripping, export of capital. (OECD,1997; Peev,1999). We cannot know what country at which stage of development is en route to transition to a market economy or 'crony' capitalism. The level of privatisation and private sector development cannot be a fully reliable feature. This is shown for example, in the case of Albania, a country with the highest private sector share in GDP among transition economies in 1996. The emergence of a 'crony' capitalism, non-planned and non-market, system made us reconsider the *real* ownership and control transformation in transition economies.

There is a wealth of literature on the effects of ownership and control structures on firm performance in transition economies. However, the empirical studies' results are mixed concerning any significant difference in performance of *state and privatised firms* (Megginson, Netter, 1999). Many studies support hypotheses that *private firms established de novo* are more efficient than both state and privatised firms (Bilsen and Konnings 98). However, these studies using conventional state-private firms' dichotomy cannot explain the basic relationship between traditional state-owned firms and new established 'crony' enterprises in transition. There is no simple correlation between private sector share and either national economic performance or progress in transition (S.Estrin, 1999). There is also no significant evidence that *insider-controlled* firms underperform *outsider-controlled* firms. (Among recent studies, see Peev et al. (1999) for Bulgaria, Romania and Albania). These and many other contradictions between the Washington Consensus predictions and the transitional reality throw doubts on the conventional approaches to separation of ownership and control in transition.

The common research framework of the study was based on an integral theoretical approach. We used the property-rights approach in the study of ownership and control structures of business organisations and the literature dedicated to empirical study of the relationship between ownership and performance - in the study of the relationship between ownership, control and business behaviour. At the core of our analysis of business behaviour does not lie profit maximisation but the *utility-maximisation hypothesis* (De Alessi 1983). In economies in transition, the specific semi-market environment, characterised by high political uncertainty, macroeconomic instability, strong fluctuation of input and output prices and financial performance measures, influences managerial behaviour. The inefficient behaviour of owners (observed in the mixed economy, too) is much more typical of transitional

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economies because of the particularities of the emerging 'crony' capitalism. The utility-maximisation hypothesis was accepted as a main connecting behavioural hypothesis about individual choices, made by managers, workers and owners under transitional institutional constraints. The present survey uses information collected from the Bulgarian Central Statistical office (1990-2001) and from the author's empirical studies of firms and industries in Bulgaria (for the methodology of these studies, see Peev, 1999; Peev, Donchev, 2001).

The subject of this paper is ownership and control transformation in Bulgaria during transition. Section 2 describes ownership and control structures in Bulgarian industry. Section 3 analyses ownership and control structures in different forms of business organisation as corporatised state-owned enterprises, privatised firms and newly established private firms. Section 4 reveals "crony capitalism" enterprise sector duality and specific property-rights structures as basic constraints on the Bulgarian enterprise sector development. The study concludes with policy issues regarding 'crony' capitalism evolution in Bulgaria.

Ownership and Control Structures in Bulgarian Industry

Bulgarian industry is characterised by four major groups of firms, classified according to the type of ownership: traditional state-owned (non-transformed), corporatised state-owned, former state-owned firms which have been privatised, and private firms established *de novo*.

Private Sector

The main factor contributing to the development of the private sector in Bulgaria during 1992-96 was the creation of new private enterprises. The share of privatised state-owned enterprises was insignificant. Privatisation has made little progress, and up to now 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 being municipal property or parts of enterprises. Substantial progress in privatisation was observed in 1997-98 connected with the finalisation of a number of large-scale deals as well as the completion of the mass privatisation. About 1,000 enterprises were privatised - entirely or in part - through vouchers. In the period 1992-97 about 20% of total enterprise assets were privatised. In 1997, there was an acceleration of this process, e.g. about 4% of assets were privatised through cash sales with USD 421.4m. proceeds. However, the data for 1998 show only USD 145.8m. in privatisation proceeds. The main reason for the slow progress is the continuing fight for corporate control between different groups of interests and new '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 privatised assets since the beginning of the privatisation process from 1 January, 1993, until the end of November, 1999, is 46.3%, which is more than 70% of that due to be privatised in the mid-term state assets. Between 1.01.93 and 31.12.99, the total privatisation effect was 6,501.663m. USD. Distribution of concluded transactions by sectors is as follows: industry – 30.2%, trade – 24.5%, agriculture – 13.8%, tourism – 11.1%, others – 20.5%. 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 following were privatised: the United Bulgarian Bank (July 1997); the Bulgarian Post Bank (the end of 1998); in 1999 Society General bought TB Express and Reagent Pacific - Hebros Bank. In 2000 Bulbank was privatised.

Public Sector

The main changes in state-owned enterprises are related to their transformation (corporatisation). This was a process transforming former state enterprises into companies with 100% state participation. In general, this process took place mainly in the 1991-92 period, and developed at a considerably lower pace in the next years. After 1993, non-transformed state-owned and municipal firms decreased twice in number. This was due to two main reasons: firstly, the continuing process of corporatisation and, secondly, 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, according to data of the Bulgarian Statistical Institute for 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. There has been no official data for public sector assets for 1999 but it can be expected that their share has continued to be high.

Control Types

The prevailing types of control of private *de novo* and privatised companies in Bulgaria during 1992-96 are the private and majority control. One group of the companies under private control is characterised by a dominant outsider stake of company assets. But the outside institutional shareholders are: 1) firms owned by the company managers, and 2) firms with managerial participation in their ownership. Another group of the firms under private control has a dominant workers stake. But these firms are not prevailing like the former ones. The companies under majority control are characterised with two groups of enterprises as well. Some of them have a dominant outsider stake as the large shareholder is private firm. An essential feature of these enterprises is managerial participation in the company assets and the board of directors. The other companies have a dominant managerial stake of their assets. One party, usually a private firm owned by company managers, is the large shareholder in these firms. The described control structures are characterised by some key features: firstly, close relations between owners and managers; secondly, the large shareholder has formal effective control over the managerial behaviour through nominating the members of board of directors, obtaining real company information, hiring and firing of managers. This control type diminishes the transaction costs for monitoring the managers. These costs become lower than the ones of companies with dispersed ownership between many small shareholders; thirdly, the large shareholder brings more risk and has stronger motivation to compel managers towards strategies maximising the shareholders wealth.

Despite 100% state participation in their ownership, the corporatised state-owned companies are mainly under managerial control and interest group control. These types of control are based on unestablished property rights and influence by groups of interests other than the nominal owner State. This peculiar transition-kind of control is implicit and unstable. Unestablished property rights are property rights structures which fail to determine clearly who owns company assets, who is a bearer of residual risk, who is a decision-maker, who nominates members of the board of directors. In this ownership structure, however, there are different degrees of managerial discretion. Another key feature of the control structure of the corporatised state-owned companies is the influence of interest groups other than State. In the Bulgarian state-owned companies, interest groups other than the owner State are trade unions, political forces, finance groups and others, such as non-formal leaders, for example. In the distinct companies they have different degrees of influence on management.

The key features of the control structures during 1992-96 are as follows: firstly, in the existing private sector, private and privatised firms, there is strong owner-type control that is the base for constraining potential discretionary managerial behaviour; secondly, in the private companies managers participate closely in company ownership, they have a stake in private firms – large owners of company assets directly own company ownership and have a seat on the board of directors; thirdly, contrary to the

conventional view that 100% state ownership means strong government control as well, the state-owned enterprises are characterised by the separation of ownership from control and scope for managerial discretion.

After the mass privatisation in 1996-97, many companies, especially large firms, acquired dispersed ownership structure. Their shareholders acquired an insignificant property stake, and managerial and minority types of control emerged. There is separation of ownership from control and potential for inefficient managerial behaviour. A stage in the evolution of property-rights structures since 1998 has been the fight between minority owners after the mass privatisation, and outside participants, for the acquisition of efficient control over the enterprises. This process will objectively lead to a concentration of ownership (though not necessarily to higher efficiency). Because of insufficient development of the capital markets, both the stock exchange and OTC markets, the basic way to compete for corporate control is by proxy fights. In Bulgaria there exists a corporate culture of post-totalitarian primary accumulation of capital. The share of the grey economy is assessed to be about 40% of GDP. In our study, 70% of the firms in the sample estimate the share of the underground economy to be over 50%. Corruption exists that determines the unhealthy business climate. All these factors predetermine more specific owner objectives, which may not be directed to development of the enterprises but rather to their decapitalisation and short-term use.

Emerging Property-Rights Structures in Corporatised State-Owned, Privatised and Private *De Novo* Firms

The property-rights approach examines ownership structure in different kinds of business organisations. The study uses this approach in an investigation of the ownership structure of corporatised state-owned, former state-owned firms that have been privatised, and private firms established *de novo* in the Bulgarian industry.

Corporatised State-Owned Firms

Property-rights structure

Corporatised enterprises prevail in the state sector. Untransformed traditional state enterprises have an insignificant share and are actually of no importance for the development of the national economy. The property-rights structure of the corporatised state-owned company is characterised as follows: 1) state ownership of assets; 2) the state owns the right of residual risk; 3) the government appoints a board of directors, the latter manages and represents the company and designates managers; 4) the state has the right to sell its rights of central status and residual risk bearer. The state-owned company is a transition form of business organisation between the self-managed socialist enterprise and the modern corporation. There is an essential difference between a state-owned company and a self-managed socialist enterprise. Here the employees are not agents of property rights. This is a peculiarity of the state-owned company in Bulgaria. In Hungary and Poland, the workers' councils continued to exist after the commercialisation of enterprises. The essential similarity between a state-owned company and self-managed socialist enterprise is the preserving of state ownership of assets.

The main *agents* of property rights in a state-owned company are the government as an owner and the managers. The function of risk bearing, according to property-rights theory, is taken on by state officials and the function of management - by managers. However, the state officials are risk-bearers not because of their higher motivation for risk bearing, but because of their status. Who is the actual bearer of the residual risk after the collapse of CMEA and the shock stabilisation programme in Bulgaria at the beginning of the 90s? While a given enterprise is in state ownership the government, as owner, is the economic agent which, according to the property-rights theory, must bear the residual consequences from the shocks. The managers and the workers of a particular enterprise have no

liability with respect to the external difficulties felt by the enterprise. In practice, however, the state officials shift all the liabilities of the transition onto the enterprise. The state-owned company obtains so-called "autonomy", a hypothetical promise of freedom in the field of products, markets and investments. In fact, however, this is only quasiautonomy because: firstly, the state remains the owner of the assets and shifts only the risk-bearing of the economic reform to the companies; secondly, the risk-bearer is again impersonal - managers or employees or the enterprise at large.

Business Behaviour

Corporatised state-owned enterprises are characterised by an unestablished property-rights structure. The only nominal owner is the government. The control rights are to be exercised by the Board of Directors, but the survey shows that the managers have the most active influence on decision-making. There is separation of ownership and control, which, however, is of a specific 'transitional' type. This is due to the inefficient behaviour of the state in transition that withdraws from the control of enterprises, gives great managerial discretion and allows post-totalitarian accumulation of capital at the expense of the enterprises. The Board of Directors cannot fulfil its functions of a disciplining mechanism to potential managerial behaviour because it consists of people (including representatives of the private business) who have interests definitely different from the interests of the enterprises. Corporatised state-owned enterprises show passive managerial strategies to restructuring in all spheres of economic activity in general management. These enterprises have the lowest performance indicators measured in profit sales ratio and productivity in comparison to the firms with the other types of ownership structure. Their turnover and personnel number is the highest because large-sized firms prevail. A feature of corporatised state-owned enterprises is their oldest structure of equipment.

The programmes of the *government* for liquidation of state-owned loss-makers and 'isolation' and privatisation or liquidation of other losing enterprises were being carried out slowly. The 'isolation' combined restructuring with limits on further borrowing. The positive effects of the "isolation" for loss-makers were decreasing production and, as a consequence, decreasing material costs. However, the biggest loss-makers continue to exist even in 1998, when ten enterprises only were responsible for about half of the inter-enterprises arrears. According to some estimations, the size of the total arrears was about 8 % of GDP at that time.

Privatised Firms

Property-rights structure

The typical property-rights structure of the enterprises after their privatisation is characterised as follows: 1) one party- private firm, personnel, managerial team etc., owns a big stake of assets; 2) all the shareholders own the right of residual risk; 3) this party has the formal and real right to appoint a board of directors; 4) all the shareholders have the right to sell their rights by public offering. This structure is similar to the ownership structure of the private companies established *de novo*. Both have concentration of the company assets in the hands of the large owner.

The ownership structure of the enterprises after "*mass privatisation*" is different. Their key feature is dispersion of ownership between many small shareholders, privatisation funds, financial institutions, etc. The main peculiarities of this property-rights structure are: 1) many owners of assets and no agent has real power based on his shareholding or strategic position; 2) all the shareholders own the right of residual risk; 3) formal right to appoint a board of directors; 4) all the shareholders have the right to sell their rights by public offering. This ownership structure is similar to the structure of the so-called "managerial firms" and control is the managerial and minority type known about from the literature. It will create the problems of separation of ownership and control between small shareholders and managers.

The main *agents* of property rights in the privatised companies are the shareholders as owners and 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 privatisation? While a given enterprise is in private ownership, the shareholders as owner, are the economic agents that, according to the property-rights theory, must bear the residual consequences of the managerial decisions. In practice, the large shareholders of firms have a very close connection with the managers. There are other firms owned by managers, outside firms with managerial ownership stake, etc. The privatised company obtains a specific autonomy: firstly, the owner of the assets is the risk-bearer as well; secondly, the risk-bearer is personal - private firm and private person; thirdly, the government shifts the risk-bearing of the macroeconomic financial reform to the companies and they become hostages of the potential government voluntarism.

Enterprise Behaviour

The privatisation rate in Bulgaria till 1995 was low. The privatised enterprises are small and medium-sized and are characterised by varied ownership structures. Enterprises with a more concentrated ownership structure prevail. From the point of view of control structure, the enterprises under outsider control prevail over the ones under insider control. The institution of the Board of Directors in privatised enterprises is characterised 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, in privatised enterprises, at the decision-making level in the spheres of production and personnel, the highest influence is in the hands of the managers, while in the spheres of managerial employment and compensation and the financial sphere - the Board of Directors. A specific case of coincidence between the dominant nominal owner and the real decision-maker in the firm are enterprises under the control of a *foreign investor*. In these enterprises, there is not separation of ownership and control. On the contrary, we observe 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 characterised 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.

After the *mass privatisation* in 1997-98, about 1,000 new enterprises were privatised. The typical ownership structure formed was dispersed ownership with managerial or minority owner control exercised by the new holding companies (former privatisation funds). Here separation of ownership and control emerges. A stage in the evolution of property-rights structures that began at the beginning of 1998 is the fight between minority owners after mass privatisation, and outside participants, for the acquisition of efficient control over the enterprises. This process will objectively lead to a concentration of ownership (though not necessarily to higher efficiency). Because of insufficient development of the capital markets, both the stock exchange and OTC markets, the basic way to compete for corporate control is by proxy fights. The problems with post-privatisation restructuring of the already privatised enterprises will be on the agenda very soon. In 1998-99, the basic task of the government was the privatisation of state enterprises and the liquidation of the unprivatised state-owned loss-makers. The main reason for slow progress in privatisation is the continuing fight for corporate control between different groups of interests and '*crony*' firms. In 1998-1999, the government preferred insider privatisation, due to the contentious close connections between policy makers and managers. A large part of privatisation is taken by the worker-manager privatisation (MEBO).

Private Firms De Novo

Ownership structure

The ownership structure of the private firms established *de novo* has two main peculiarities. Firstly, many firms are sole proprietorships and their owner and manager are one and the same person. These firms have similar ownership structure to the 'classical' capitalist firm known about from the literature. Secondly, few private enterprises are companies. Their ownership structure is characterised 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) this party – the large shareholder – sits on the board of directors and appoints the other members of the board of directors; 4) the shareholders have the right to sell their shares by public offering. The key feature of the described ownership structure is that the large owners bring more risk and their personal welfare is closely connected to 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 residual risk and managerial initiative.

Enterprise Behaviour

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 in them is the manager-owner, which is typical of the property-rights structure in the 'classical' capitalist firm in the capitalism of the 19th century. In this ownership structure, there is not separation of ownership and control and a most efficient managerial behaviour is expected. The newly founded private firms show passive strategies to enterprise restructuring, which is understandable 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 indicates that in spite of the unfavourable semi-market environment, their ownership structure creates life-giving incentives of adaptation.

'Crony' Private Firms

The existence of 'crony' private firms is a specific case. During 1992-1996, a system of 'crony' capitalism emerged with a main network among former communist nomenclature circles, weak state institutions and the criminal world. The typical motivation of the agents in this symbiosis has been to ransack the national wealth. The industrial policy was directed towards slow privatisation of the state-owned enterprises, which led to their asset-stripping. The private sector existed mainly in the form of newly established domestic firms with two characteristics: 'crony firms' and 'non-crony firms'. The Bulgarian banks pumped resources from state institutions and the 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 with strong political connections.

During 1997-98, the currency board together with the new government decreased the possibilities for rent seeking 'crony private firms'. However, the road to the end of 'wild crony capitalism' turned out to be long. In 1997, about 29% of state-owned enterprises went on losing. In 1998, loss-makers were 40% of the state enterprises. They survived due to the growing inter-enterprises arrears, the lack of effective adoption of bankruptcy legislation and new 'crony firms'. There exists a risky tendency towards growth of the liabilities of the state enterprises in comparison with 1997, tolerated by the government. The large part of the losses (about 74%), and liabilities (about 63%), are concentrated in 26 big enterprises. Despite the limitations sets to the budget by the currency board, the 'black financial holes' keep on sucking in fiscal revenue and transferring state assets to private 'crony' firms. In 1998-99, the prevailing MEBO privatisation schemes established new 'crony' private firms.

"Crony" Capitalism and Its Evolution to European Structures

Dual Enterprise Sector

The dual enterprise sector is the most important aspect of the emerging 'crony' capitalism in Bulgaria during 1992-99. Two types of enterprises and two types of corporate culture in the Bulgarian economy co-exist simultaneously: normal and 'transitional'. The first type is with a clear structure of property rights (newly founded private firms and privatised firms with market motivated owners). The others are corporatised state-owned enterprises (including the biggest state-owned loss-makers), state enterprises in the process of privatisation, newly founded private firms and privatised enterprises with owners oriented to state assets expropriation and other 'wild capitalism' attitudes. The grey economy and the household production for own consumption belong to the second group. The expectation regarding the *foreign investment* enterprises is that they will introduce a new market-oriented style of management. For the time being, however, these enterprises show both types of corporate culture and behaviour. 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 operate with market behaviour to the market-oriented subjects and with perverse behaviour on other occasions. The macroeconomic signals of the currency board are refracted through this culture. It is difficult for the policy-makers to predict enterprise behaviour.

Firm Ownership Heterogeneity

Firm ownership heterogeneity is another important characteristics of 'crony' capitalism in Bulgaria. The research reveals that in a transitional context, the specific features of state and private firm owners are: a) *a* disintegrated state institutions, which withdraw from the control of enterprises and gives them pseudo-autonomy and non-owners' discretion (for example, corporatised state-owned enterprises); b) private owners with specific corporate culture, aiming not at developing, but at plundering the enterprises (for example, some privatised enterprises). With these 'transition' owner objectives, 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 forecasts for business behaviour. There is specific firm heterogeneity based on state enterprise evolution. The main inefficient property-rights structures in corporatised-state and privatised enterprises during 1992-98 and their positive evolution after 1998 are summarised below.

Firstly, *corporatised-state enterprises*. The owner - the government - has withdrawn from control, and managers and other non-owners have discretion to decapitalise the enterprises in their favour. The efficient evolution of these enterprises ranges from control based on unestablished property-rights to fighting for explicit corporate control and *privatisation*.

Secondly, *privatised enterprises with perverse behaviour*. (1) These are privatised enterprises with dispersed ownership. In them, the inefficient behaviour is due not only to managers but also to new owners. They are not entrepreneurs and do not have owner market motivation. The evolution of these enterprises is towards ownership concentration and new objectives of owners. *Secondary privatisation* is due through internal mechanisms or capital markets. (2) These are privatised enterprises, whose ownership is concentrated, but their owners have post-totalitarian corporate culture and pursue asset-stripping strategies. The efficient development of these enterprises requires *secondary privatisation* (it can be through liquidation, too) and change of owners.

Thirdly, *privatised enterprises with market-oriented behaviour*. (1) 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, are due. (2) These are enterprises where the behaviour of large shareholders is directed towards their development. Here, the basic problem is not the contradiction

between owners and managers, but rather between large and small shareholders. *Governance mechanisms* for the protection of small shareholders are to be developed.

'Crony' Capitalism Evolution

'Crony' capitalism evolution in Bulgaria depends on many uncertain political and economic factors and it is hazardous to make predictions in this area. In Bulgaria after 1997, the currency board together with the new parliamentary majority excluding former communist parties has greatly increased stability in the country. The present government under Prime Minister Ivan Kostov is the first Bulgarian government since 1990 with a clear orientation towards EU accession and a market economy. However, the legacy of the wasted years remains. The dualistic enterprise sector and the three inefficient groups of enterprises in the Bulgarian economy analysed above will behave with different responses to the signals of the economic policy. This means that the policy-makers have to be more oriented to forecast both market-oriented and pervasive responses to one and the same macroeconomic policy decisions in the short run (until about 2003). One of the basic issues before policy-makers in Bulgaria is how to establish corporate governance mechanisms that will simultaneously curb potential managerial and owner inefficient discretionary behaviour during the negotiations for EU membership.

The start of the accession talks by Bulgaria in 2000 resembles the beginning of the transition to a market economy in the 90's. Both now and at that time, there are tangible discrepancies between the expectations and the real outcome of the processes. The expectations then were that privatisation meant a heavy blow against the monopoly state ownership and the communist nomenclature; liberalisation - a blow against totalitarian planning and totalitarian state; stabilisation - setting hard budget constraints. Now, ten years later, it could be ascertained that none of these expectations was achieved. What actually happened was redistribution and ruin of national wealth (not privatisation), persistent destruction of the economy through unfair competition and export of national capital and bureaucratic financial chaos. There was a positive (but not qualitative) change in the major participants then, and is now at the start of the talks with the EU. There are not new political forces, there is no exhaustive analysis of what happened during the past ten years, there are no sentenced criminals (except for some petty crimes) and there is no true market ideology. This leads to suspicions in the public about a new discrepancy between the announced advantages and disadvantages of joining the EU and the real outcome of it. In the recent history of Bulgaria, there are several examples of mass lies with disastrous consequences for the people. Besides the road to "market economy" after 1989, there was "the building of communism" (1960 - 80), of the "developed socialism" (1970 - 1990), of Bulgaria with a "qualitative new growth" (1985 - 2005). Consequently there followed grotesque analogies with the new aspiration to "accession". Positive expectations are connected with the *revival of the efficient for the conditions in Bulgaria industrial structure*, deformed after the Soviet invasion in 1944. This means priority development of tourism, agriculture and the food industry, and the light industry among the traditional branches, development of modern information technologies, and closing down or restructuring of the sectors unable to produce goods for the European markets. The latest surveys show that the basic factor for the economic recovery of the country in 1989 - 1995 was export to the EU, whereas there is no redirecting of products sold on the former market of CMEA to the European markets. Our accession to the EU is conceived as a long-term objective, that is why there are no concrete expectations of the very accession but rather of the preparation for it - e.g. *new laws normalising the relations between employers and employees*. The expectations are not only for a high standard in industrial relations, but also for an *easier access to capital* and increase in employment. If the accession process developed normally, the *main loser* should be the second "transitional" sector in the economy described above. The losers would be the peculiar network among political circles, 'crony' firms and the criminal world, who flourished in Bulgaria in 1992 - 96 and now have fading functions (but are ready for revenge in the next elections). State bureaucracy is in the middle position, typical of the managers before privatisation. It will win in the process, but lose from the result. The hopes of all retrograde forces ('crony capitalism' network, communists, Russian oriented parasites) are that the Bulgarian population will be incapable of creating a government which

will govern independently of the bureaucratic whims in Brussels (such as the idea that gypsies in Bulgaria do not have equal rights with Bulgarians), and the economic advice a la Harvard Institute for International Development, leading to a handful of wealthy people, and general ruin (like that in Russia). The vague intentions and inefficiency of the IMF and the European clerks feed these hopes. According to Bulgarian nationalists, these expectations coincide with interests of circles from the so-called Great Powers (the USA, Western Europe, Russia) which look upon Bulgaria as a dependent state (formerly Russian, currently of the IMF, and in the future of the European bureaucracy). Thereof comes the scepticism of the Bulgarian intellectuals about who will be the real winners after the accession to the EU.

According to the most optimistic views on the accession of Bulgaria to the EU, it could happen in 2006. In 1998, GDP per capita in Bulgaria was 28 per cent of the EU-15 average. There is even an income-level gap between Bulgaria and transition countries such as Poland, Hungary and the Czech Republic. According to different estimations, if Bulgaria grew on average by 2 percentage points faster than these countries by 2020, she would only reach 65 per cent of their 2020 GDP per capita level. Even if the average rate of growth of per capita income in Bulgaria exceeded that of the three transitional countries by 5 percentage points, Bulgaria would only reach 90 per cent of the average GDP per capita level of these countries in 2020. The objective lag in Bulgaria at the beginning of the talks shows that it is necessary to have a fundamental change in the economic climate in the country. The uncertainty is tremendous and it is hazardous to make predictions in this area. If there were a change in the business climate (positive or negative) in the near future (the next 5 years), it would be a result of a political decision made outside Bulgaria. In a more distant perspective (10 - 20) years, a positive development can be expected due to the natural change of generations.

We can forecast different *scenarios* of country evolution. In the short term (1 -2 years), the preservation of the currency board will be the basic indicator of the positive development of the financial stability in the country. Positive changes in the business climate of the country will be connected with the dismissal of corrupt people from governing positions. A basic debate in Bulgaria is that there is corruption at a high level of state administration, but nobody is ever punished. Another significant indicator will be the results of the parliamentary elections (June 2001).

The first scenario for Bulgaria in the short run is the preservation of financial stability under the currency board, state loss-makers restructuring, quick privatisation and social tensions based on loss-makers restructuring and post-privatisation perverse behaviour. This scenario is associated with the preservation of the status quo. This means that the new government will maintain the same line of action. The positive side is the preservation of the currency board and an orientation to real European integration; the negative side is, conservation of bureaucracy, the existing political class, and the bureaucratic business conditions in Bulgaria, which would be normalised slowly *step by step*.

The second, pessimistic scenario assumes replacing the fixed exchange rate and a delay of both enterprise restructuring and social tensions. The second option is based on the presumption of a new government that would have vague responsibilities and a populist policy. There would be a *revenge* of forces known from the early stages of 'crony' capitalism and a government in the style of 1990 - 1996 with postponement of the actual reforms, and a new lack of business rules. It seems unlikely, however, that people will once more be taken in by socialist slogans as they were at the beginning of the 1990s, and at the end of 1994.

The third scenario is a fast *revolutionary* change of the existing 'crony' capitalism with market institutions based economic system.

The *conservative* optimistic approach to Bulgaria is to expect the second best (or first described above) scenario.

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