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GUIDELINES
of the preparation of country papers on the problems of
strategic management of industrial restructuring in East
European countries

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GENERAL INFORMATION

These guidelines are intended for support of the participants in the high level expert group meeting in the preparation of their country papers on the problems of industry restructuring and privatization. Country papers would be presented in Sofia at the meeting entitled "High Level Expert Group Meeting to Assess the Applicability of Strategic Management Methodologies to Industrial Restructuring in Bulgaria and East European Countries" held within the frames of UNIDO.

The main objective of the meeting is to discuss the possibilities for applicability of methodology for strategic management in the conditions of industrial restructuring in Bulgaria and East European countries. In view of the above the experts would be invited to share and discuss their knowledge and specific practical experience in the conditions of East and Western European countries.

Contributions are expected from the participants of the following countries: Bulgaria, Belgium, CSFR, Germany, Greece, Hungary, Poland, Turkey, UK and USSR.

MAIN TOPICS FOR DISCUSSION

The organizer of the meeting - Industry Development Institute, Sofia along with UNIDO determined the following main topics for discussion at the meeting in Sofia:

1. Transition and restructuring in Bulgaria which will be a subject of the paper presented by the Bulgarian counterpart - IDI, Sofia.
2. Main principles of strategic management - experience, examples and results which will be a basic paper

delivered by Mr. De Bandt, UNIDO consultant.

3. Privatization and strategic management approach.
4. Role of the state in the strategic management of industrial restructuring.
5. Institutional organization for strategic management approach (public and private institutions).
6. Technical support for strategic management.
7. Approval of the final report and recommendations.

It is recommended East European partners to share their experience and the experience of their countries in the transition to market economy and in the process of privatization concentrating their presentations on the process of industry restructuring. Participants of West European countries are expected to offer their views of the essence and peculiarities of market economy as well as to recommend some measures for the processes taking place in East European countries.

RECOMMENDED STRUCTURE AND CONTENT OF THE COUNTRY PAPERS

In view of the attainment of maximum efficiency and in order to give chance of comparison of approaches, methods and means used in separate countries for the implementation of restructuring and privatization as a guarantee of the transition to market economy the organizers of the meeting offer the following recommended principle structure and content of the country papers:

1. Introduction

This part contains a short description of the selected problem, its essence and practical meaning for the implementation of restructuring process and transition to market economy. The problems could be selected from the offered main topics for discussion or they may refer directly or indirectly to the topic of the meeting.

2. Approach in Solution of the Problem

This section treats the practical approach in solution of the selected by the participant problem for the respective country. The phases of solution are described, then the institutional and legal support, the obstacles and the ways of their overcoming. Experts may share their modern views concerning the solution of the specific problem despite its coincidence with the officially adopted approach for solution. The relations between the specific problem and other problems related to the implementation of the successful transition to market economy and industry restructuring are recommended to be described. The participants in the meeting are advised to offer their views for the development of the respective problem in the near future.

3. Necessity of and Possibilities for Strategic Management of Restructuring and Privatization Processes

On the basis of the analysis of the chosen problem done in the previous section participants may offer some general views and opinions concerning the management possibilities of the processes of restructuring and privatization in the countries of East Europe and Bulgaria. This part of the paper may include some methodologies, approaches and other means used as

management tools of the processes of transition to market economy in the respective country as well as the forms and methods for state impact, institutional and legal support, technical support of the process, etc.

4. Recommendations

It is recommended that experts would formulate their suggestions and recommendations for management of the processes of restructuring and privatization in view of speeding up the transition to market economy in the countries of East Europe.

Additional Information

High level expert group meeting will take place in the period January 29-February 1, 1991 in Sofia in Moskva Hotel. The arrival and registration of participants in the meeting will be on January 28 and the departure - on February 2, 1991.

Industry Development Institute, Sofia (12A Ho Shi Min Blvd, Director General - phone: 79-00-04, Dr. V. Parvanov, responsible organizer - phone: 79-01-26) is organizer of the meeting. The organizers of the meeting provide meeting of participants, local transport to the place of inhabitation and their seeing off during their departure.

The meeting is mutually organized with UNIDO within the frames of Project UC/UD/RER/90. Backstopping section: Industrial Planning Branch, backstopping officer: Mr. Yu. Akhvlediani.

UNIDO Consultant: Mr. J. de Bandt

INDUSTRY DEVELOPMENT INSTITUTE SOFIA

COUNTRY PAPER ON BULGARIA

REVIEW AND ANALYSIS

OF THE EXISTING ECONOMIC AND ORGANIZATIONAL FRAMEWORK

Sofia, 1991

PROBLEMS OF INDUSTRY PRIVATIZATION IN BULGARIA

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Privatization is one of the essential activities constituting the whole process of transition of Bulgarian economy toward market mechanisms. In view of the present specific conditions in our country it has to be looked upon in close relation with the deepening economic crisis. Therefore the three concepts - market economy, privatization and economic crisis have to be examined in our case in their interrelation.

Privatization is an entirely new phenomenon for our country and our advance to it is void of experience. The situation is almost the same in the rest of the East European countries though some of them launched this process a couple of years earlier. The fact that they have not attained much high results confirms the idea that privatization is a complicated process which requires a longer period of time.

In the developed countries as USA, Germany, Great Britain and France there is a considerable accumulated experience in privatization processes. Here are some specific conclusions concerning their experience:

- Privatization has to be looked upon as economic, political and social phenomenon and neither of these aspects has to be minimized.
- A broad legal basis for privatization has to be created so as to guarantee personal interest and positive attitude of all participants to the process of privatization - the state, managerial staff and workers of the enterprises and private persons - owners of the

property.

- Privatization has to be implemented after the adoption of a clear and flexible programme intended to formulate the aims and means for its attainment.
- Privatization has to begin from enterprises and activities which are closer in their operational features to the market mechanisms.

Following aims could be attained through privatization:

- creation of direct private interest in the widest possible circles of population concerning economic state of the country.
- giving population the chance of investing its excess money which will ease the market tension.
- recruiting financial means from the state in view of pay off debts.
- raising enterprises economic efficiency.

What is the situation with our industry at the threshold of privatization?

It was built up with a high degree of concentration and specialization of production activities as a nutritional superconcern. In some branches as machinery and electronics as a result of the specialization large production units were formed - assembly plants, plants for joints and plants for parts. In this way an interrelated system of plants and firms was formed in such way that the independent behaviour of a single plant may distress operation of a number of plants. In its essence the above system contains a number of progressive elements which are the aim of many countries but in our conditions it has many defects in itself.

Which are the problems related to industry privatization?

1. Industrial system is built up on the principles of centrally planned management. After the liquidation of the central management most of the links between enterprises were destroyed and the system came to deadlock. A period of readjustment of work in the new conditions is necessary in which all elements of the market system have to be built up as well as the specific links for this mechanism of work. Capital market and raw material market are the essential elements of the market system which have to be built up. As in Bulgaria the large part of the raw materials necessary for industry are scarce such a market could be created as a part of the world market of raw materials. At the existing now currency situation in Bulgaria and in the rest of the East European countries the above aim could be attained only on condition Bulgarian Lev become convertible. Therefore industry could function successfully under the conditions of market economy only at the existence of raw materials market for which the convertibility of Bulgarian Lev is absolutely necessary condition.

2. Most of the large production facilities lack in the necessary background of various small producers who could release them from the numerous small production activities. In this relation a privatization could be done for example of supplies of some joints and parts, some peripheral activities, transport etc. Large state and joint property enterprises could become center connected to a number of small and medium-size private enterprises. After the creation of the necessary legislation the above process could be started without delay.

3. Concentration and specialization in a small country as Bulgaria led us to the situation in which most of production activities are implemented by monopolistic producers. Demonopolization of our industry is a key problem related to the creation of market economy. In case the problem with the monopolistic producers is not solved competition which is the main engine of market economy could not exist. The attempts for introduction the mechanism of market economy in the conditions created by monopolistic producers, no matter whether they are private or state inevitably lead to uncontrolled raising of prices and to the appearance of black market. This is evidently the present situation in our country.

In this respect privatization could play an important part. On the one hand parallel private production could be created in competition with the state production, and on the other hand some of large producers could be fragmented to smaller ones taken by the private owners. Fragmentation of some Bulgarian large firms is necessary. For example in Italy, the world's largest producer of shoes, this production is performed by the operation of thousand of small and medium-size firms. In our country it is concentrated in a few large state firms.

4. Due to the lack of interest at all levels of management and because of a number of other reasons the efficiency of management of state enterprises marked a continuous slow down and at present it is very low. Privatization process have to lead to improvement in business activity, management and economic results due to the direct interest of the owners.

5. In spite of our estimation of the enterprises during the process of privatization we have to acknowledge that we do

not have and we could not have clear concept for their real economic efficiency. The acting prices at present of the capital formation and that of the production differ considerably from the international ones. The picture of economic efficiency of a specific enterprise changes considerably if the latter is expressed in international prices. Reliable accounts based on international prices could be done only if Bulgarian Lev is made convertible. The lack of clear information concerning economic efficiency of enterprises expressed in international prices presents a serious obstacle to the implementation of industry privatization in Bulgaria and could lead to a capital mistakes.

6. According to the present estimation a number of state enterprises are failing down. Probably the estimation by international prices would also lead to the conclusion of the existence of a number of failing enterprises. There is the following alternative for them - either to adopt a programme which will improve their efficiency before privatization or to be sold at very low prices. According to world practice most of the publications advise to accept a programme for raising the economic efficiency.

The transition from state to private or joint property is obviously a process different in its character for the specific branches and subbranches. There are no universal prescriptions for this kind of activity. So for example for commerce, services, light industry and similar probably the transition from state property to private property by sale would be very characteristic. For other branches characteristic for our industry as machinery, electronics, chemistry, metallurgy,

energy and transport there is no question about selling out enterprises because it is practically impossible. Here the problem is how and to what extent to attract foreign capital.

The crucial problem is which private capitals would be directed to industry. It must be born in mind that the total value of financial means in population at the end of April 1990 is 21.5 billion Leva while in industry only the value of the basic and circulation capital at the end of 1989 is 89.7 billion Leva. In addition persons who own capital at present prefer to invest it in smaller and quick profit enterprises - transport services, cafeterias, hotels, shops, restaurants, etc. Practically in Bulgaria there are no people owing capitals and willing to invest them in manufacture and especially in large manufacturing units. In addition a number of our industrial enterprises are losing and even if there were persons owing capital they would hardly decide to invest in them.

The question of whether foreign capital owners would invest in our industry remains open. It is necessary to answer the question what would attract them in Bulgaria. We have to be fully aware that our country does not have clear political system and a firm, clear and favourable economic legislation. We are not able to offer Bulgarian raw materials suitable for processing. Our territory is burdened with a number of ecological problems. The infrastructure - roads, transport, communications, etc. is not at a very high level. The only thing we could offer is a cheap labour force comparative well trained. However in this respect we could hardly stand the competition of the third world countries. Besides, recently our

labour force turned out to be an unstable factor and the above is evident for the foreign investors, too. So with the exception of some specific cases at present it would be very naive to rely on broad foreign investments for industry privatization. This could be seen from a number of publications in the foreign press.

How we could privatize industry under these conditions?

Serious potential owners of the large industrial enterprises are the persons working in them, those who have already connected their future with these enterprises. The only way for the implementation of real industry privatization is to give workers the right to buy shares under favourable conditions or to give them free according to the method of privatization by free distribution. That is the only way of creating interest in a wide circle of persons. This is not an utopia but the only possible way out. Similar steps are discussed in Czechoslovakia and Hungary.

The main problem of industry privatization is how to create an effective mechanism of economic management of firms and the interrelations between them in the conditions of simultaneous existence of all forms of property after the system of centrally planned management is eliminated. The system of economic management has to guarantee maximum profit of all investors on the one hand, and on the other hand it has to regulate the way of state participation in the forms of joint property. Only a system which guarantees such a mechanism of action could be a successful step toward the implementation of market economy.

A number of countries with developed market economy have a positive experience in that direction. The idea is about the creation of sectorial holdings as a corporation of share holding firms with the respective share of state participation. A continuous and long standing experience in that respect was acquired in Italy, Germany, Austria, Sweden, Finland, etc. No matter they are regulated by a special law or they operate on the basis of the laws concerning share holding companies, these holdings do not contradict to the principle of competition and they are well integrated in the economic structure of a country with market economy. They combine in a optimum way the interest of the state with the interests of the private sector following some main principles:

- capitals presented by the state to the holding share companies become property of the latter
- capitals are managed only by the holding share companies
- state does not have the right to interfere in the management of share holding companies
- The managerial board of the share holding companies is responsible for the economic results in front of a specialized body concerning state participation in industry.

Necessary technological relations among firms are implemented as the interested firms buy shares from the dependant firms. A part of the shares are sold to the citizens or to the personnel employed so as to guarantee their personal interests in the firm. In that case state is isolated from the

direct economic management and it observes its interests as an investor.

The state sector is presided by a state body as for example by a Ministry of state participation in industry which supports the sectorial share holding companies formed by it in building up the necessary infrastructure in the implementation of large capital investments, in the regional development, etc. By its participation in the large industrial enterprises the state may defend the interests of society as a whole and implement, guarantee and balance the relations within the sectors and among them by its share participation.

Industry privatization could not be looked upon only as a process of entire or partial transfer of state property to private persons. It could lead to a change in the conditions of management and functioning of economic units to minimizing and liquidation of subsidies, profit and quality orientation and to the creation of a real market medium. It has to raise economic efficiency by the abolishment of bureaucratic control on the operation of industrial enterprises with state participation giving them independent management, financial independence and freedom of operation.

It is obvious that industry privatization is a difficult problem which could be solved in a larger period of time. The problem is whether this will lead to a slowdown of market mechanism introduction. The reply is no because the form of property is not decisive for the operation of market mechanism. Market relations could exist in the conditions of state or mixed type of property. It is not the form of property that is important but the rules of operation of economy.

The above examinations could lead to the following conclusions:

1. Privatization is a means of raising efficiency of our economy and it has to be implemented at rates dictated by the necessity of economic crisis come out. It has to be implemented parallel to the building up of the whole system of market economy.
2. Industry privatization has three components - creation of state and joint property share holding companies, fragmentation of some large firms, and sold out of some lesser and peripheral activities of the large firms. The main form of property in industry will be joint property in some sectors with prevailing state participation.
3. Industry privatization could be done after the creation of the respective legislation and development of clear and flexible programme.
4. The main private owner in industry could be personnel engaged in it or the whole nation depending on the kind of the adopted system. The respective mechanism and legislation have to be worked out for that purpose.
5. The existence of raw materials market is of crucial importance for the effective operation of industry in the conditions of market economy and privatization for which purpose Bulgarian Lev has to be made convertible.

**PRELIMINARY RESULTS OF A SURVEY OF THE CYCLES AND
DEFINITION**

OF PARAMETERS OF THE CRISIS IN BULGARIAN INDUSTRY

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Bulgarian economy development and particularly its leading sector industry is objectively linked to the necessity of its privatization and restructuring. At present these processes are looked upon as a necessary condition for the successful implementation of the transition to market regulation of economy,

Cyclicity of the development of our industry and its basic sectors were examined in view of the attainment of the above aim. Special attention was paid to the indicators of the crisis and to its parameters which are closely related to the factors and conditions of its deepening.

The problem of the cycles in economy development was up to now arbitrary and until recently it was looked upon entirely as an attribute of the capitalist society. It was in the last ten years that a couple of articles appeared treating some theoretical and methodological aspects of the cycles, determination of the indicators influencing the crisis.

Our examination is based on the understanding that industrial development is of cyclic character and the separate cycles differ in type, longevity and intensity and are substantially influenced by the operation of a complex of exogeneous and endogeneous factors and some specific conditions and peculiarities including historical, social and political ones.

After some examination and analysis of the cycles in the development of the market economy countries the following economic cycles in the development of our economy during the period 1945-1990 were used:

- long cycle (long wave)
- long cycle phases: animation, rise, crisis and depression
- medium and short cycles of growth.

The type and longevity of the cycles were determined on the basis of the results of the survey carried out by the system of indicators and methods which give the possibility of their characterizing and sizing. Our survey came to the conclusion that the following indicators are widely used in international practice when characterizing the crisis and economic cycles in industry:

- Gross National Product (GNP)
- National Income (Net Production)
- Total Industrial Production
- Investments
- Unemployment Rate
- Price Index
- Production Export
- Trade Balance

Using the above indicators we carried out a survey of the cycles and determined the rate of influence of the separate indicators over the crisis in some countries with developed market economy. The obtained results were used in the comparative analysis of the development of Bulgarian economy.

A large part of the above growth indicators could not be used due to the absence of necessary statistic information and some peculiarities in the sector development based on the so far planned economy and its bureaucratic management system. As a result of the above reasons the following neglected so far indicators were not included in the survey: interest rate, price index and unemployment rate. The absence of information impelled the usage of additional indicators facilitating the conditions of more precise definition of economic cycles, crisis parameters and the tendencies in its development and deepening:

- fund consumption
- average production per person
- social labour productivity
- net production
- material consumption
- labour consumption
- energy consumption.

After the examination we came to the conclusion that the cycles of development, character and intensity of the crisis in Bulgaria and in other East European countries differ from that of the developed countries with market economy. On the first place it is necessary to point out the lower growth rate during the years of greatest depression. Even in these years (excluding Poland and Yugoslavia) growth rate did not fall under the level of the preceding year. In Bulgaria the case is without precedence - the growth rate in 1989 was expected to be lower than in 1990. Therefore, depression was not accepted intentionally and some measures were taken frequently at a high

price in support of the accepted "rate psychology" of growth. On the second hand it must be noted that the influence of the world crisis was considerably lower on our economy and industrial development. Beside its lower strength and sharpness, the world crisis appeared by rule with a certain extent of delay, i.e. one, two or three years after the respective crisis. A good evidence for the above statement is the fact that while in the recent years East European countries (USSR, Bulgaria, Rumania, Poland and Hungary) are in crisis and the first three of them - in depression, the countries with market economy and most of all the most developed of them are in animation and rise. All this is a result of the great differences (economic, historical, political and social) characteristic of the developed countries and East European countries.

There is a very essential difference between the character of the crisis in Bulgaria and that in the countries with market economy deserving to be pointed out. In market economy countries crises took place in the conditions of overproduction, destroyed proportions between supply and demand, stock exchange fluctuations and enlarged unemployment, while in Bulgaria they took place in the conditions of rising deficiency, technological progress delay, rising raw materials deficiency and loss of some of the positions on the world markets.

After the examination done by IDI using the explained methodical tools it was come to the conclusion that during the whole period from 1945 onwards national economy including industry has developed in cycles, i.e. separate repeated ebbs

and flows with the respective declines and rises of economic growth. Periodical cycles were discovered (long, medium-term and short-term) as well as separate cycle phases corresponding to the theories of "long waves". Results show first the existence of "long cycle" (long waves) in industry development taking place as long as 45 years starting in 1946. Its most characteristic features are: first - a clearly determined "rising wave", i. e. a period of speedy and steady growth rates (12-19 per cent), and second - a following "downward wave" (including the period of 1966-1967) characterized by a delay and constant growth slow down (7.1 per cent). It must be added that the downward wave in 1990 including the long cycle are not yet completed.

It is interesting to be noted the four classical phases of economic development: animation, rise, crisis and depression took place within the frames of the long cycle.

The first phase of the cycle within the rising waves - animation took place about 15 years starting in 1946-1947 and ending in 1960-1961. During that phase the average annual growth rates are between 14 and 15 per cent which is an indicator for a speedy economic growth. The positive results of the main indicators of economic growth are proof for that. The average annual growth rate of net production is 8.75 %, that of investments - 13.7 %, of total profit - 9.2 %, of export - 17% and of employed persons - 9.7 %. Besides, the average production during the period 1948-1960 has grown 2.13 times, public labour productivity - 2.75 times, fund consumption based on total industrial production and basic production funds - 1.37 and 1.77 times, while efficiency based on main production

funds has grown by 3 points. Despite that it must be noted that the obtained results were attained on a very high basis, forced with a considerable for the possibilities of the country investments in the sector, mainly intended for machine-building industry accounting for the enlarged employed personnel. This is a period of an emphasized extensive growth of the sector.

The second phase - rise, started in 1961-1962 and ended in 1970 and lasted about 14-15 years. The average annual growth rate of the total industrial production is 10.6 % and for the rest of the growth indicators they are as follows - export 14.35 %, net production -9.45%, investments - 13.15%, total profit - 10.55%, employed - 3% and main production funds - 12%. During that phase industry took its leading place in the sectorial structure with a constantly increasing share. The above is due to the priority sectors in heavy industry - machine-building, chemistry, electronics and energy. The highest growth rates of the indicators were attained during the four phases of the cycle: average rate of production - 6.8%, public labour productivity - 5.8%, efficiency based on main production funds and total industrial production - 1.6% and 3.0%, and especially - profit per person - 8.05%. The great contribution of export with preceding growth rates and the rise of export for steady currency has to be noted. It is only the large investments and the considerable increase of main production funds that show that the rise during that period has a considerably high cost and it was attained mainly at the expense of the increased consumption of public labour (12%).

International comparisons show that during that period our growth rate was lower only in comparison to Japan - 12.2% and

Spain - 11.6% but it was higher than that of Holland, Italy, Canada, Sweden and Australia. Despite the great growth rates of our industry, in international comparison one must bear in mind first that they were obtained on a lower base which is characteristic for the newly industrializing countries, and second that in quality and technological aspect we were weaker than the developed countries with market economy.

The third phase, the crisis, starts from 1976-1977 and goes on to 1984-1985. It is characteristic by its sharp slow down, stagnation of growth in relation to that attained during the rise phase. The average annual growth rate is 5.5 %, i.e. 5.1 points lower than that of the previous phase. During that cycle many negative factors are accumulated - destroyed proportions and conditions (build-in structures, accelerated development of heavy industry sectors with larger consumption of resources, energy and investments, retarded development of innovation processes, agriculture stagnation, etc.) leading to a future deepening of the crisis.

That is why the growth of total industrial production and the number of the engaged personnel lessened double, that of investments - 1.7 times, main funds and profit - 1.4 times, net production - 1.3 times and export - 1.2 times. The destroyed proportion in the very high growth of main funds compared to the manufactured total and net production and to the total profit are the first serious sign for destroyed internal relations, worse economic condition and for the transition of the sector to the rising crisis. An evidence for that is the lesser fund consumption and that of other indicators compared to the phase of rise. The growth of average production is two

times down, that of public productivity of labour - 1.4 times, profit per person employed - 1.35 times. It is necessary to point out that personnel growth with 1.7 influenced very much the attained total industrial production growth.

The phase of depression started in 1964-1985 and is not concluded yet. It is characterized by a perpetual stagnation, i.e. slow down of rates. For the first time during the first half of 1990 there is a great slow down compared to the same period of 1989 while the volume of production lessened by 14%. This tendency is expected to last in the next 2-3 years, too.

The rates of export lessened drastically by more than 5.66 times while the investment rates lessen only by 14%. This shows that one unit of investments is attained by 2 times smaller growth of total and net production and total profit.

Fund consumption decrease by 10-12 % are proof for the worse economic situation. For five years only, from 1985 on, the internal debt increased threateningly by 5 billion US \$. The influence of the total crisis is unfavourable in economy, civil engineering, transport and in the sharpening of financial, raw materials, energy, currency crisis and some political and international factors.

The examinations showed that the cycle phases, the sharpness and character of the crisis and depression differ for the main sectors of industry.

The rising wave in metallurgy is shorter while the phases of animation, rise and crises end in 1962, 1972 and 1982. In chemistry the rising wave is longer, the rise ends in 1971, the crisis - in 1981 and depression starts earlier - in 1982. In contrast to them in machine building the phases of rise and

crises started later. The above shows that each sector has its specific conditions and cycles of development.

Within the frames of the long cycle separate phases there are six medium cycles lasting from 7 to 10 years and 13 short cycles lasting from 3 to 4 years. They are characteristic with different character and tendencies of economic growth. As it is seen from Figure 1, the first of the medium cycles is characteristic with rapid growth, the second is with non-linear character with a strong slow down in 1956, the third one is a rising curve with a peak in 1965, etc. The last one, the sixth cycle coincides with the phase of depression. It is characteristic with considerable stagnation which evidently will transfer to recession during the next two years.

On the basis of the obtained results the following generalized conclusions could be done:

- The development of our industry is cyclic and it comes through all phases of the long cycle
- In contrast to the developed countries with market economies where the long cycle ended with depression in 1985-1986 and has started a new long cycle with animation phase, our sector is in its final phase - growing depression which is expected to end as late as the period 1992-1993 and in the case of retarded implementation of economic reform - even in 1994-1995.
- In our country the phases of the long cycle have developed with a constantly growing in time delay in comparison to the developed countries. At present the delay is about 1-1.5 phases, i.e. 8-9 to 11-12 years. Despite that, their

development in our country is less sharp by rule with less drops - almost without cases of recession excluding 1990.

- Planned economy and bureaucratic system of management influenced decisively the cycle and longevity of the phases. In fact they invalidated and distorted the influence of the objective economic laws inherent to the market economy. Due to that the cycles and crises in East European countries are not crises of overproduction but crises of deficiency of commodities, raw materials, fuels, delay of innovations and mainly of old fashioned and non-effective structures of production irrespective to market requirements.

- There is a great difference in the ways of come out of crises. Western countries come out of crises by rule by market renewed and adapted structures for which they pay very high price including the social aspect of it. Unlike them Bulgaria and other East European countries took measures for limitation of the crises with lesser price and tension but without substantial structural renewal. Therefore the world crisis in 1974-1975 and in 1982-1983 did not have healing influence on our economy and that of other East European countries.

In the conditions of deteriorated economic situation in Bulgaria and the complicated international political situation only the adoption of rapid and efficient measures for a radical economic reform combined with decisive restructuring and a reasonable privatization could stop the depression and create necessary economic conditions for a gradual stabilization and new animation in the sector corresponding to the principles of market economy.

**METHODICS OF MARKET EVALUATION OF THE FIRMS AND
ENTERPRISES OFFERED FOR PRIVATIZATION**

**Mr. Peter Lichev, Mrs. Emiliya Petrova,
Mrs. Stoyka Christova**

Industry Development Institute, Sofia

Privatization is envisaged to include both small and large firms at a price of million Leva. That is why real determination of the market value of the firms is an important condition for the successful implementation of the programme for outcome of the crisis and development of economic reform. Industry Development Institute, Sofia has developed methodics of market evaluation of the firms.

Methodics of market evaluation of the firms and enterprises offered for privatization includes the following main problems:

1. Estimation of the Value of the Main Funds and the Size of the Normed Means of Circulation

It is a condition for a really based estimation of the market value of the firms and enterprises. In view of the more complex characterization of the level of means of labour the elaboration of name lists of main funds is necessary which give information about machines and equipment in respect to their quantity, their initial and residual value, the year of purchase and the name of supplier, export for convertible and non-convertible currency. They supply also information about the unnecessary and useless machines and equipment.

Circulation means of machine-building plants influence efficiency directly and they are necessary condition for the normal production activity of the firms and enterprises. Due to

that the problems of circulation means are of primary importance during the elaboration of methodological problems concerning the estimation of market value of the firms and enterprises.

During the process of production activity enterprises form excess production under the influence of different in character factors - subjective and objective. A part of this overproduction is good and necessary but they are in larger quantities than the expedient one for the normal operation of production-business activity of the firms and enterprises. At the same time an excess of unnecessary commodities is formed which in some cases are of low quality and useless. That is why they must not be included in the market value of the firms and enterprises envisaged for privatization.

In view of the normal implementation of their business economic activity firms and enterprises deal with the so called circulation funds, including the finished production and money means which have to be taken into consideration in the estimation of market value and financial state of the firms and enterprises.

Normal functions of the firms and enterprises are connected not only with the use of own means of circulation but with the attraction and use of bank credit necessary both for the direct production activity and for the whole financial support of the processes of enlarged production, including the financing of investment process. Having in mind that in the conditions of socially oriented market economy credit will get even greater importance, the estimation of the financial state has to include also a concrete analysis of the credit policy

and that of the actives and passives of the firms and enterprizes.

A really based estimation of the market value and financial condition of the envisaged for privatization firms and enterprizes is related to the strict estimation of the own and equal-to-own means according to the sources.

2. Estimation of Financial Condition and Efficiency of

Production Economic Activity of the Firms and Enterprizes

In view of estimation of the efficiency of the firms and enterprizes envisaged for privatization it is necessary a system of mutually connected indicators to be adopted as for example public labour productivity and profit norm. Profitability is an expression of income but it is not a measure of income. Measuring the degree of income is done by the norm of profit.

Estimation has to be done also on the basis of indicators characterizing economic efficiency of the used resources as for example - fund consumption, material consumption and labour productivity.

Methodics includes also a system of indicators which allows the accounting of the financial state of the firms and the efficiency of the circulation means - solvency and circulation of the circulation means, etc.

3. Specification of the Production Output of the

Enterprizes and Firms Envisaged for Privatization

The estimation of the market value of the firms and enterprizes envisaged for privatization is related to the specification of their production output - the profile, magnitude and character of the manufactured production. That is

why despite the great methodological and practical difficulties this indicator was included as one of the basic initial factors of the market value of the firms and enterprizes envisaged for privatization and it includes essence and range of the production output, calculation of the production output by machines and sectors, utilization of the production output, balance of production output.

Specific characteristics of the separate enterprizes and partially the estimation of the expert commission were taken into consideration in specifying the production output.

4. Estimation of the Market Value of the Firms and Enterprizes Envisaged for Privatization

Market value is determined on the basis of preliminary developed problems - lists of the main funds and magnitude of the circulation means, financial state and the efficiency of the productive economic activity as well as the magnitude of the production outputs using the formula:

$$Mv = Nv + Cc,$$

where: Mv is the market value

Nv is the net value

Cc is the complexz corrective coefficient calculated on the basis of expert analysis.

There are also other factors which quantitative influence on the market value has to be taken into account as for example resource provision, labour and legal legislation, infrastructural provision, communications, personnel provision, etc. The influence of the above factors is specific for the separate sectors, production activities and firms and their

significance to a given degree could be estimated on the basis of a specific deep analysis and expert estimations.

Market value of the firms is envisaged to be estimated after the reduction of their net value by the complex corrective coefficient. Comparative data concerning the firms in the developed countries have to be used in estimation of the market value. There are data for about 1500 firms including information for each firm by 70 indicators available at the Central Institute for Scientific and Technological Information. It is reasonable the indicators of the firms of the developed countries manufacturing similar production to be taken into account in the estimation of the market value of the specific firms. This approach is necessary to be used in the estimation of the market value of the firms and enterprises in convertible currency.

Net value is estimated by the formula:

$$Nv = Bfrv.Kr + Vbpc.Ccc + Ec + Acn - D + \\ + Vnabf.Cnm + Vnm p. + Knm p.$$

Bfrv - is the basic funds by residual value (excluding the cost of the buildings and earth)

Kr - is the complex corrective coefficient reflecting the difference between amortization (depreciation) life cycle, the exploitation-technological life cycle and the economic life cycle. It is determined by the method of expert analysis.

Vbpc - is the value of the buildings by their initial cost

Ccc - is the complex corrective coefficient reflecting the state of the buildings and the degree of correspondence of the constructions to the technological and ergonomical

requirements. It is determined by the method of expert analysis.

E_c - earth cost

A_{cm} - available circulation means

D - debt amount

V_{nmabf} - is the value of the non-manufacturing active basic funds by residual cost.

C_{nm} - is the complex corrective coefficient reflecting the difference between the depreciation life cycle, exploitation-technological life cycle and economic life cycle of the non-manufacturing active basic funds. It is determined by the method of expert analysis.

$V_{nm p.}$ - is the value of the non-manufacturing passive basic funds by primary cost.

$K_{nm p.}$ - is the complex corrective coefficient reflecting the state of the buildings and other passive non-manufacturing basic funds and the degree of correspondence of the constructions and their technological parameters to the ergonomical and technological requirements. It is determined by the method of expert analysis.

The greater degree of the increase of the difference between the physical term of service of machines and equipment, the degree of depreciation and economically profitable term of their use is characteristic for the state of the production-technological basis. Due to that re-estimation of the basic funds in accordance with their technological-economic parameters and inflation processes is of primary importance for the estimation of the market value of machines and equipment. In respect to that the specification of the life cycle and the

introduction of the difference between the economic and physical concept of time is a very important point. It is appropriate to accept the following three categories in specification and characterizing the term of work longevity of machines and equipment:

- exploitation-technological life cycle
- (reproductive) depreciation life cycle
- economic life cycle.

Exploitation-technological life cycle of the operation of machines and equipment is predetermined by the degree of their physical amortization and the ability of restoration of the labour means to the marginally necessary direct technologically-economical qualities and parameters.

Reproductive (depreciation) life cycle is predetermined by the amount of the adopted amortization norms and their longevity of operation.

The specification of the economic life cycle of machines and equipment is of primary importance for the estimation of the state, rate and proportions of renewal of production-technological basis.

In the conditions of new regime of functioning of economy and firm organisation of economic activity the estimation of the market value of labour means requires the use of complex corrective coefficients which will reduce the value of the basic funds in the firms and enterprizes. In view of the better grounding of the corrective coefficients a differentiated approach was adopted in accordance with which different complex corrective coefficients are envisaged for the active, passive and non-manufacturing basic means.

Modernization of the prices of machines and their reduction to a common scale is a very complex problem. As it was already indicated, the last re-estimation of the basic means was as late as 1974. Due to that it will be necessary correction coefficients to be elaborated differentially for the firms and enterprises. For such cases the nominal value is determined by the formula:

$$Nv = E$$

where:

$Bfrv_i$ - is the residual value excluding the value of the buildings and earth for the i -type of machines and equipment.

Kr_i - is the complex corrective coefficient reflecting the difference between the amortization (reproductive) life cycle, exploitation life cycle and economic life cycle for the i -type of machines and equipment.

$Vbpc_i$ - is the primary cost of the i -building.

Ccc_i - is the complex corrective coefficient reflecting the state of the i -type of building and the degree of correspondence of its constructions to the technological and ergonomic requirements.

It is evident that the detailed estimation of the net value of the basic means is extremely labour taking. That is why the above method is advisable to be used only in the estimation of unique machines and equipment and these with high value.

After an analysis it is necessary all non-solvent circulation means to be excluded from the amount of the circulation means which has to participate in the formation of the market value. It is also evident that obligations and

takings of the firms and enterprises have to be taken into consideration.

The suggested methodological approach accounts for the influence of the most important factors and is suitable for a based estimation of the market value of the firms and enterprises envisaged for privatization.

Taking out of anonymity of the huge for the scale of our country property is one of the basic moments in the transition toward market economy. The implementation of privatization affects live interests of some hundred thousand members of our community from all spheres of material production and with different professional qualification. That is why the implementation of privatization in the specific firms and enterprises is necessary to be accompanied by an implementation of a sociological examination concerning the forms of privatization and the degree of labour motivation for raising quality production and efficiency of labour in the conditions of different forms of property by means of an inquiry card.

5. Formation of the Market Price of the Firms and Enterprises in the Conditions of a Socially Oriented Market Economy in the Developed Countries

According to the methodological approach discussed so far, the price of the firms and enterprises envisaged for privatization is formed according to the viewpoint of the salesman - the state (owner). At the same time the price of the basic and circulation means of the firm is not essential for the potential buyers of the whole firm or of shares of it. According to the opinion of the experts of the developed countries the existing accounting system including that in the

countries of East Europe is wrong and it is unable to support a real estimation.

In the conditions of market economy the maximum price which is profitable to be paid by the buyer is limited to the amount of the bank interest. Namely, the relation of the profit expected by the firm and the invested for purchase capital must not be less than the amount of the bank interest rate. For example, if the interest rate for the capital invested in the bank is 8 %, it will be profitable for the buyer to pay not more than 10 million Leva for an enterprise with an annual profit of 800 000 Leva or the profitability norm of the specific enterprise has to be at least 8 % and if we account for the element of risk - not less than 8.5 %. In this specific case the total scheme of the main and circulation means of the firm could be for example 12 million or 8 million Leva, this could not influence its market value which in the case of 8 % bank interest is about 10 million Leva. For the firms and enterprises purchased by foreign firms and foreign citizens the top limit of the market price will be formed finally in accordance with the financial policy and the amount of the rate percent in the developed countries. It must be noted that according to the nowadays acting legislation and legislation in the sphere of finances and banking, the above method is very difficult to be applied.

The existing financial and banking-credit system does not create conditions for the use of rate percent and discount as powerful and multifunctional economic regulators in the conditions of the transition to a socially oriented market economy.

In the conditions of market economy purchasing of enterprises, parts of them or shares of enterprises is an investment process. It is reduced to a great degree to a comparison of the future positive incomes and present expenses which actually present a negative income. Therefore the choice between the individual variants of capital investments from economic point of view appears to be a choice of variants of incomes in time. The difficulty of the problem comes out of the circumstance that money means that will be at disposal for example in the following ten years are with different purchasing power and they could not be compared directly. Coefficient of their modernization expressing the economic relation between the present and the future is of fundamental importance for the comparison of the various in time effects and single expenses. That is why the new methodics for estimation of investment process economic efficiency which came into force on 01.11.1988 requires modernization of single expenses and balance profit.

Method of discount of various in times incomes and expenses is applied in the practice of the developed countries firms in the formation of economic policy and taking decisions for investments. The reduction of different time expenses and effects to comparable type is implemented by the discount coefficient under the formula - the present moment value of one dollar (one pound, etc) payable after years. Interest percent lies is grounded on discounting. In the conditions of market economy, the interest, as well as any other economic parameter expressed in the type of price which appears to be an important regulator has a double character. In the case of

growing interest rate there is a transfusion of the incomes of the debtors to that of the creditors. At the same time in the process of formation of investment policy and choice of variants, the greater interest percent requires a more effective decision and strengthens the requirements and strictness in the choice of optimum variants for distribution of the restricted financial means and for determination of the priorities of the financial policy. As it concerns the interrelations of debtor-creditor the category of interest percent is used and for the formation of the specific strategy of the investor firm discount norm is used.

The problems of privatization including the estimation of market value of the firms are part of the whole complex of problems connected with the transition to market economy. In connection to that intensification of privatization processes and the estimation of the market value of the separate firms and enterprises requires implementation of cardinal reforms in the sphere of financial policy and banks.