

Foreign Direct Investment in Bulgaria in the Period 1992-2008: Conclusions and New Challenges

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Summary: Foreign direct investment plays a vital role in the economic development of each country. Bulgaria made considerable efforts for attracting foreign capital flows to different sectors of its national economy in the period of transition to market economy. It must be taken into account that foreign investments managed to change to a certain extent both the image and the product and technological structure of the different branches. The aim of the present paper is to analyze foreign capital flows in Bulgarian industry, to outline the results achieved and to show possible ways of solving some of the problems in the field. The changes that occurred in recent years pose new requirements and create a necessity of applying new ideas for finding new adequate solutions which allow modeling of foreign direct investment in those sectors and industries which will shape the image of the national economy in the next decades.

Key words: foreign direct investment, investment activity, economic crisis, foreign entrepreneurs, challenges.

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Investment plays an important role for the activation of economic activity in the different sectors of the national economy. It not also ensures the so much desired economic growth, but in periods of crisis, investment is also the shock-absorber mitigating unfavourable effects of the crisis and the decline in economic development of the countries. Investment was the important vehicle assisting the transition countries to implement faster their economic reforms and to meet the challenges of global change. Turning to the recent history of transition to a market economy, we should acknowledge that at its beginning, Bulgaria was not a desired location for investment, i.e. it occupied the last place among East European countries regarding attractiveness to foreign investment. The process of attracting foreign capital can be divided into three stages:

- From the 1980s to 1992;
- From 1992 to 1997;
- From 1998 to 2008.

The **first stage** was started back in the times of the command-administrative system. It dates from 1980, when the State Council, existing at that time, issued Decree № 535 on economic cooperation between Bulgarian legal persons and foreign legal and physical persons, and Decree № 1196 on joint economic activity of Bulgarian citizens and foreign physical and legal persons, thus creating the basis for foreign entrepreneurial activity in the national economy.

It would be also appropriate to mention here Decree № 2242 from 1987 on the creation of tax-free zones, Decree № 56 from 1988 on economic activity, the Trade Law from 1991, the Law on economic activity of foreign persons and on protection of foreign investment from 1992, all of them having created the legal framework for investment.

During the initial stage of the process of attracting foreign capital, which started in the early 1970s and ended in the late 1980s, foreign investors had the purpose not so much to investigate the market in our country, but to use it as a platform for entering the markets of the former Soviet Union. Decree № 535, as well as Decree № 1196 on joint economic activity of Bulgarian citizens and foreign physical and legal persons should be considered as initial stage in the process of opening the Bulgarian economy and of the integration of our country into the international division of capital, products, and labour. Two contradicting trends are manifested in this respect – on one hand, the search for liberalization of economic relations and for greater freedom of forms of economic activity, and on the other – strict state control of the activity of Bulgarian economic agents.

In the late 1980s, with the transition to company organization, the regime of foreign investment in our country was also changed; for this purpose, a special section was developed in Decree № 56 on economic activity [1, 1999, 44]. This shows that joint economic activity was starting to be accepted as an element in the transformation of the existing economic system and the mechanisms of its regulation [2, 1990, 2]. In this sense, Decree № 56, as well as the Decree on the creation of tax-free zones (Decree № 2242), represented a logical conclusion of this specific second stage in the establishment of the legal and economic regime regulating foreign investment in Bulgaria.

Table 1. Forms of economic activity according to Decree № 56

№	Forms of economic activity	Number
1	Independent economic activity	3
2	Commercial representatives	29
3	Subsidiary companies	23
4	Limited liability companies	16
5	Joint-stock companies	2
	Total:	73

The total number of permits issued for economic activity during this period was 73 (see Table 1) (3, 1995, 265). Entrepreneurs from Europe dominate almost completely – 90.41 %, or 66 permits, while those from USA are 0.54 %, or 4, and from Canada, Australia, and Asia – one from each country/region. The forms of entrepreneurial activity are the following (see Figure 1).

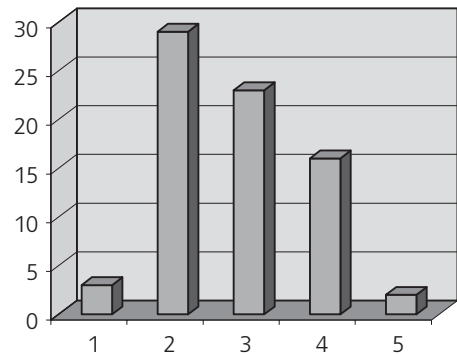


Figure 1. Forms of economic activity

The following *conclusions* can be made as a result of the performed analysis:

- A small number of companies, with a low statutory *fund* and share capital, had serious investment intentions.
- Subsidiary companies and joint ventures had with various fields of activities – electronics, machine building, light industries, transport, etc, and trade activity was always included.

- Lack of interest and initiative from the part of almost all large Bulgarian enterprises as to the implementation of joint forms of entrepreneurship.
- There were only a few companies with investment intentions in the industrial sector. None of the leading Bulgarian enterprises initiated the creation of a joint venture. Moreover, only three ventures had their own facilities – „Fanuk-Mashinex” with seat in Sofia, „Tangra” with seat in Burgas, and „Sofia-Mitsukoshi” with seat in Sofia. These were small investments – mostly exploration of opportunities to do business on the country’s territory.

By the end of 1991, the total volume of foreign investment was about 80 mln. dollars, 20 mln. dollars coming from one “strategic investor” – the Coca-Cola Company. These investments were absolutely insufficient in both quantitative and qualitative terms and their role was not significant in the national economy and in the industrial sector.

The second stage coincides with the period of change in the economic system of Bulgaria. The official data on foreign investment from the Foreign Investment Agency, created according to the Law on the economic activity of foreign persons and protection of foreign investment, are since 1992. Throughout this initial stage, however, there was no unified information

system about the number, type, and volume of the attracted foreign investments. The work of analysts was extremely difficult for this reason. During the period 1992-1997, the level of foreign investment was extremely low from the point of view of the needs and capacities of the Bulgarian economy – not higher than 650 mln. dollars (see Table 2). The reasons for this unfavourable situation can be attributed to several factors:

- the insufficiently developed legal and institutional basis;
- the lack of a clear concept on the place and role of external capital in the restructuring of the national economy, including the industrial sector;
- the delayed process of economic reform and, in particular, the late start of privatization of the large industrial units;
- the lack of capital market;
- the existing danger of regional conflicts, mainly because of the wars for division of former Yugoslavia.

In the beginning of the period, the only possible way of making foreign investment was the so called “Greenfield investment”. This trend was reversed and investment coming from privatization at the end of the period was twice as high as Greenfield investment.

Table 2. Direct foreign investment in the national economy for the period 1992-1997

Years	Privatization		Greenfield investment		Total
	mln. \$	%	mln. \$	%	mln. \$
1992			34.4	100.0	34.4
1993	22.0	21.5	80.4	78.5	102.4
1994	134.2	63.6	76.7	36.4	210.9
1995	26.0	16.0	136.6	84.0	162.6
1996	76.4	29.8	180.0	70.2	256.4
1997	421.4	66.2	214.8	33.8	636.2

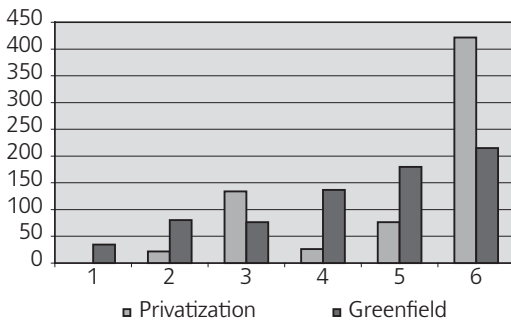


Figure 2. Types of foreign investment for the period of 1992-1997

The Law on foreign investment, developed and adopted in 1997, was based on a more advanced concept. This law preserved the statute of the foreign persons' right to acquire real estate property. The Law on foreign investment also included a regime for priority investment projects. They had to satisfy one of the following requirements:

1. the size of the investment should be over 5 mln. dollars;
2. the investment should create more than 100 new jobs;
3. the investments should be in regions with high unemployment rate, exceeding the average rate for the country, according to a list approved by the Council of Ministers.

The clearly expressed will for economic change after the bygone political, social, and economic crisis, sent positive signals, which spurred a good reaction among foreign investors. The currency board regime, introduced in July 1997, established long-term financial stability, contributing to the overall improvement of the economic climate in the country. *The main conclusion* is that, the inflow of foreign direct investment was unsatisfactory in size and irregular in the different years of the period.

The third stage covers the time from the beginning 1998 to now. It should be noted

that significant volume of foreign investment in all sectors of the national economy was attracted between 1998 and 2005; the service sector surpassing for the first time the industrial sector in the size of investment. The existing data allows make a characteristic in both quantitative and qualitative aspect. In 2004, the European Commission admitted that Bulgaria was a country with functioning market economy. From the total of more than 6.8 milliard dollars attracted during the aforementioned period, by 2005 about 30 % were in the industrial sector, but despite the positive effects, they were definitely insufficient as to their quantity and quality for the solution of the important goals to be reached in the national economy.

The last three years between 2006 and 2008 deserve special attention. In terms of quantity, they mark a peak in attracting foreign direct investment to our country, which – calculated in euro – amounted to 20 809.3 mln. euro (see Table 3). It cannot be denied that a whole set of factors contributed to the attainment of such high levels of foreign direct investment, the most important being: the favourable international economic situation, the full membership of the country in the EU; the lowest tax rates on the European continent; the good legislative framework regulating the investment regime in the country.

It is also essential to mention some of the weaknesses, tolerated in the relations with entrepreneurs, namely: low competencies of administration, language barrier in services at the regional level, lack of „transparency“ in concluding deals and use of corruption techniques.

It is necessary to take into account the fact that the Law on investment introduced equal principles and rules for investors, both local and foreign. Thus, the principle of equal treatment of investments found its practical application

Table 3. Foreign direct investment in the country for the period 1998-2008 by sectors (mln. euro)

Nº	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	Total
1	0.0	-0.3	6.4	5.4	11.3	18.7	17.5	36.3	21.4	5.3	7.6	129.6
2	0.6	-0.7	17.2	7.4	33.4	22.2	7.5	19.5	65.3	89.9	30.9	293.1
3	-0.1	-0.3	0.1	-0.1	0.4	-0.1	0.4	1.2	0.8	4.6	1.1	8.1
4	-0.1	-0.3	1.7	4.9	4.7	2.6	0.0	-0.6	0.1	0.8	0.4	14.3
5	38.0	42.6	146.0	14.2	63.6	163.1	215.6	533.8	1778.0	2505.1	1900.3	7400.3
6	220.9	460.6	551.9	289.5	76.8	516.3	435.7	868.2	1064.7	906.2	810.9	6201.7
7	2.0	-4.9	-15.6	3.0	73.3	7.7	670.8	308.5	352.4	332.5	176.2	1905.8
8	0.0	0.0	0.0	0.0	0.0	0.0	2.7	0.1	0.0	0.2	0.1	3.1
9	7.8	2.2	0.0	0.6	1.5	2.2	5.6	9.5	27.8	75.2	51.5	184.1
10	2.9	21.5	29.2	19.3	35.7	4.6	81.7	171.6	501.0	797.4	465.0	2129.8
11	16.8	17.5	20.1	243.3	229.0	153.6	426.5	-108.7	447.7	89.3	214.1	1749.3
12	127.5	142.2	283.9	135.6	255.4	434.9	496.5	576.9	964.5	1237.4	796.9	5451.6
13	168.7	103.0	17.7	137.6	136.8	432.4	236.1	667.3	799.4	2112.5	1485.9	6297.2
14	18.4	22.2	10.7	19.4	8.8	24.7	26.3	52.4	103.2	163.7	53.0	502.8
15	1.8	60.8	34.0	23.3	49.2	67.6	113.0	16.2	32.2	167.7	169.0	734.8
Total	605.1	866.0	1103.3	903.4	980.0	1850.5	2735.9	3152.1	6158.4	8487.9	6163.0	33005.7

Source: NSI.

in the servicing priority investment projects with planned investment over 70 mln. dollars. This law is consistent with the Law on state aid and with the *EU Membership Treaty of Bulgaria*. The Bulgarian Investment Agency was assigned the task of administration of priority investment projects, as well as development and implementation of a marketing strategy to attract investment in the country.

The most interesting fact is related to the structure of attracted foreign investment. During the last ten years, foreign investment flows had an extremely uneven distribution (see Figure 3). The *first place* is obviously occupied by investment in real estate, with the share of 22.23 % of all foreign investment in the country. This shows that the country has become a desired location for acquisition of property and for the performance of a wide range of business services. This is enhanced by the geographical location of the country and its excellent natural

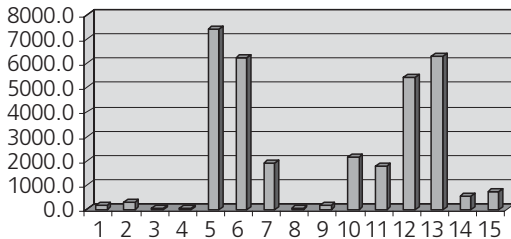


Figure 3. Foreign direct investment (FDI) by industry branches, 1998-2008, mln. euro

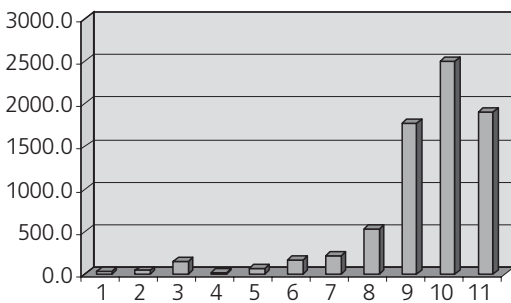


Figure 4. FDI in the real estate sector

conditions. The trend has nothing in common with the ungrounded expectations for a sharp peak in real estate prices after the accession of the country to the European Union. The present financial and economic crisis influenced real estate prices just in the opposite direction, so these prices, including prices of residential houses and buildings, dropped by 20-30 %, in some regions of the country the decrease being even more drastic.

The financial intermediation branch, including bank and insurance services holds the *second place*; the investment representing 19.45 % of foreign capital inflow. The highest growth in foreign investment was reached in 2007 (see Figure 5). This result is totally predictable as almost all Bulgarian banks became the property of foreign financial groups and large banks from Austria, Italy, Greece, and Hungary. They turned into a sort of “subsidiaries” of mother banks, operating mainly with the national financial resources and, quite expectedly, transferring profits to their “metropolises”. We arrived at logical paradoxes, when the Bulgarian government, allocating significant financial resources to assist Bulgarian business, cannot find the corresponding national partner to take up crediting in a critical moment for the survival of small and medium entrepreneurs.

The opening not only of the country’s economy as a whole, but also of its different sectors and

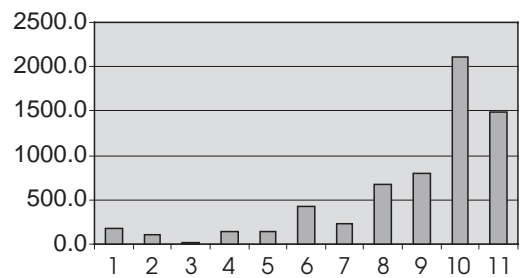


Figure 5. FDI in the financial mediation sector

branches, to foreign capital, is undeniably a positive fact that should be welcomed; however, it is important not to forget that the process of attracting foreign investment must be a mean, but not an end in itself. On the other hand, the free movement of capital, as well as people and commodities, is one of the fundamental principles in the actual construction of the European Union and no limitations should be imposed in this respect on any national government. The question is what kind of strategies and priorities are to be followed in the different sectors, including in the field of financial services. The stability of the financial system is of primary importance during periods of financial crises. Until now, the system has demonstrated good level of liquidity and the potential capacity of performing active operations. However, the high interest rates on both loans and credits entail certain risks of impossibility in servicing the loans and risks in case of deeper recession.

The *third place* is occupied by the processing industry sector. This sector should be considered in close connection with the other sectors, including processing industry, production and distribution of electricity and heating, and construction. The **"Industry" sector** is constituted in this way, including diverse classes of economic activities, according to Eurostat

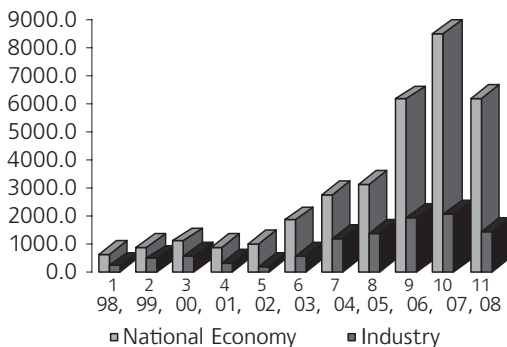


Figure 6. FDI in the national economy, 1998-2008, mln. euro

requirements. It represents, with 10 505.3 mln. euro, 31.12 % of all foreign direct investment attracted since 1998 (see Table 3 and Figure 6). The incontestable leader in attracting foreign capital is the group of activities related to production and distribution of electrical energy, with the input of about 1.9 milliard euro by the first months of 2009.

Undoubtedly, **energy supply** occupies a leading place among the industry branches. The development of industrial branches is impossible without electrification: it makes possible the running of sophisticated technological and chemical processes, the operation of production equipment, and of the systems of management and control of production processes.

The highest peak in this field was observed in 2004, when the energy distribution companies in the country were privatized for the value of about 600 mln. euro. In our opinion, the suitability of this privatization deal is still questionable and can be the subject of serious discussions and analyses. This also includes capital related to renovation and rehabilitation of the production capacities in the Maritza-Iztok complex by American and Japanese companies. Conformity to ecological parameters and the use of sulphur purification installations with minimum emissions, are of extreme importance for the Bulgarian state, as this would permit selling quotas under the Kyoto protocol.

The most important issue related to the future of the country as a distribution centre continues to be the question of the future if Bulgarian power industry. This is a vibrant issue at the present stage because of the importance of determining future commitments under the already started project of the construction of NPP "Belene". If the cost of the project, at the moment of signature of the agreement with "Atomstroyexport" and "Siemens", was 4 milliard euro, any "freezing" or rescheduling in time would make the final

cost of the project significantly higher. Solving a short-term problem by postponing the project would be associated to a risk for the country of losing its role of energy exporter to neighbouring countries, as Turkey has signed an agreement with the Russian Federation for the construction of a nuclear power plant with five reactors, 1 000 megawatts power each. Even if the price for a kilowatt-hour rises beyond the planned 4 euro cents, it should be taken into account that similar projects in Western Europe are usually planned at prices above 10 euro cents.

Gross internal consumption of electrical energy shows a decreasing trend. If the decreasing electrical energy consumption was due to implementation of the achievements of scientific and technical progress, we would witness increased energy efficiency. The decreased consumption is due to recession, which has spread to almost all industry branches, to the lack of modern technology, to decreased competitiveness, and to the lack of external markets for product sale. Undoubtedly, the energy branch has significant hidden potential and attracts the interest of foreign investors; its development would turn our country into a powerful energy production and electricity distribution centre on the Balkans. This sector could create preconditions and opportunities for the development of other production sectors.

The production capacities of metallurgic industry are concentrated in three centres – “Stomana” AD – Pernik, “Kremikovzi” AD – Sofia, and MK “Promet” – Debel; the rest are smaller

plants like „*Precis Inter Holding*” AD, “Zhiti” AD, “Inetpipe” AD, “Metalsnab holding” AD, “Rovotel” AD. The first two giants were built in the 1950s and 1960s, and the last – in the 1980s. „Kremikovzi” AD has taken the road of insolvency and eventual liquidation procedure. The plant’s situation reflects all problems in the Bulgarian economic and political reality during the transition period – namely: unsuccessful privatization, companies at the “entry” and the “exit” privatizing profits, while the losses were assumed by the “metallurgy giant”, intervention of trade unions in the management of the enterprise. In the nonferrous-metals industry, the main producers of metals and rolled stock are: “Kumario” AD, KCM-SA, “Alkomet” AD, “OCK” AD, “Sofia Med” AD, “Stillmet” AD.

The main reasons for the current state of affairs are rooted in the model of privatization, in which everything is done to drive away foreign investors with traditions, experience, and high capacity. At this point, it should be noted that part of the smaller enterprises – casting workshops –over the years also found new owners – foreign entrepreneurs, but it is still early to speak about stable economic results. By 2008, the total investment was 630 968.5 mln. euro. Challenges faced by economic agents are: conformity to ecological norms and standards, as well as creating safe work conditions. Enterprises also need support to increase energy efficiency by concluding long-term agreements with the state for the implementation of appropriate projects under the program “Building capacity in management and development of the public-

Table 4. Foreign direct investment in industry

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	Total for the period
mln. euro	225.8	476.8	571.9	317.2	197.2	547.3	1205.7	1384.6	1939.4	2041.4	1459.7	10367

Source: BNB.

private partnership for energy efficiency in industry" (7, 2009, 26). It is crucial to look for appropriate new forms of cooperation between the state, the scientific units, and businesses in staff training, qualification, and re-qualification, and in increasing the competitiveness of the human factor in metallurgy.

Machine building industry is one of the most important sectors in the national economy. Its development started during the second half of the 20th century with a strong advance of the light machine building industry at first; then the heavy machine building industry was assigned the highest priority in the 1980s. The bright hopes for massive invasion, for penetration of foreign investment, were inconsistent with reality and, at the end of the day, the available capacities did not play the significant role, expected to result in restructuring of the subsector [3, 1995, 277]. Nevertheless, there are some foreign investments, which can be regarded as a sort of "islands" of foreign entrepreneurial activity. These are "ABB" – Sweden, "Liebherr" – Switzerland, "Sparky" and "Grimer" from Germany, "American Standard Company", and after its withdrawal – the investment fund „Bain Capital Partners". Most of them have acquired their property by participation in the privatization process; others like "Liebherr", „Bain Capital Partners", etc. became owners through the so called "Greenfield investment". The favourable conditions for attracting foreign direct investment include the stable financial state of companies in the sector and their export orientation in producing machines and equipment. As for factors like labour costs, qualified specialists in the sector, and development of labour legislation, Bulgaria is ahead of its direct competitors in attracting investment in the region – Rumania and Croatia. The experience of the ten new members, which joined the EU in 2004, shows that such conditions are beneficial for bringing considerable foreign investment into the machine building industry. Foreign investment in the production

of machines and equipment during the analyzed period amounts to 269 809.1 mln. euro.

The most significant transformation after 1990 occurred in the **food industry** sector, which according to the opinion of a number of experts, is expected to become the "supporting construction", the spine of the future Bulgarian industry. Food industry, despite the idelogemes of priority development of heavy industry, formed a large part of the export list. Foreign investment here amounted to 685 501.4 mln. euro by the end of 2008. The sector's attractiveness for foreign entrepreneurs is due to good traditions, relatively well-preserved facilities, and the highly qualified workforce employed in the subsector as a whole. In the production of food products, established companies like "Nestle" – Switzerland, "Danon" – France, "Kraft-Jacobs" – Switzerland, "Delta" – Greece, "Chipita-International" – Greece, "Provimi" – Holland, "Softbul Investment" – Cyprus, "TKM Fruit and Juice" – Greece gained stable presence on the Bulgarian market. Their activity introduced to the Bulgarian market great variety in the range of food products. Moreover, the quality of their products corresponds to European standards with respect to consumer characteristics, among which packaging, advertising, prices, and other elements of the marketing mix. Undoubtedly, the membership of our country in the EU leads to positive effects, offering larger market for the production of national enterprises; but it also brings in stronger competition. A number of enterprises which have limited capacity in dealing with European standards, including some companies with foreign involvement (usually small ones – dairy farms, sausage producing workshops, bakeries) may be exposed to the risk of being closed for many different reasons.

The "**Electrotechnics and electronics industry**" branch is characterized by large production capacities owned by large structures, which are not very flexible in the current, strongly dynamic,

market situation. Within the foreign investors group, the presence of leaders like *ABB* (Asea Brown Boveri), Hyundai, and Schneider is notable. Meanwhile, the fact that the market environment in the area of high technologies is quite complicated should be taken into account. The possibilities of realization of manufactured high technology products are only and uniquely on external markets. Electronic equipment together with information technologies is some of the most promising sectors for investment. Some vital conditions for drawing in foreign direct investment include availability of highly qualified specialists, as well as opportunities for partnership with scientific research centres and the academic community. Foreign investment in the manufacturing of electric, optical, and other equipment during the considered period amounts to 193 958.6 mln. euro.

Investments in the **textile industry** and production of clothes are targeted mainly at technological renewal of the equipment, as the purchase of new machines and technology lines requires large capital investment. In the future, textile industry will be an increasingly favourable spot for foreign investments because of the low production costs on one hand, and the relatively favourable geographic location, on the other (in comparison, for example, with the countries of Southeast Asia). Investment comes mainly from large and world famous representatives of the industry branch like the Miroglio Group and Safil from Italy, Rollmann-Partners and Alt Group from Germany, Demo Bulgaria and Kosmos Textile from Greece, Maser Holding and Menderes Tekstil from Turkey, Dewavrin Group from France, Coats from Great Britain, etc. The industry branch as a whole needs serious investment, expected to come from foreign companies. In 2004, a sector strategy "Premiana Bulgaria – production of clothes" was developed as a result of the joint work by the Ministry of the Economy and the Bulgarian apparel and textile business with the support of *German Technical Cooperation*

(*GTZ*). The common vision on the development of the sector at the European scale covers *three directions*: transition to production of high technology products; transforming textile into a preferred material for new sectors; limiting mass production and transition to producing items against order. A special roadmap – the European technological platform – was developed for the implementation of specific measures in these three directions (11, 2007, 46). These investments amount to 405 447.1 euro by the end of the analyzed period.

The chemical, caoutchouc, and plastics industry is among the leading sectors in the economy of the country. The large capacities for production of calcinated soda and artificial fertilizers, of chlorethan and dichlorethan are concentrated in the town of Devnia, those of polyester fibres – in Yambol, cellulose and viscose silk – in the town of Svishtov. The pharmaceutical industry is concentrated in Sofia, Dupnitsa, Trojan, and Peshtera. The perfume and cosmetics industry is developed in Sofia, Plovdiv, Karlovo, Shumen, and Rudozem. The production of plastic products is located mainly in Russe, Gabrovo, Botevgrad, Assenovgrad, and Sofia. **Caoutchouc producing** enterprises are situated in Sofia and Pazardjik. According to the opinion of experts, this type of production will continue to grow, as it is linked to the development of other branches and activities, and there still are non-occupied market niches. As to employment generation, the share of the branch is the same as in the EU – it provides 2.6 % of the jobs in the processing industry.

Foreign investment in the production of chemical substances, processed products, and fibres amounts to 528 926.1 mln. euro, and in the production of caoutchouc and plastic products – to 83 869.4 mln. euro. In this type of production, with a view of future development, the emphasis should be placed on innovative projects in order to receive funds from operative programs

like the Competitiveness program – a set of measures directed towards loyal competition on the market through control of the application of ecological and other standards.

The most important enterprises in the structure of **the industry producing non-metal raw materials** became through privatization the property of foreign investors. Thus, for example, the cement plants in Devnia and Zlatna Panega were acquired by the French company “Cement France” and by the German “Heidelberg Cement”, respectively. The cement production group also associates the production of glass and glassware, pottery, clay products, extraction and processing of marble and marble products. The glass production complex of Shishedjam in Targovishte – “Trakia glass Bulgaria” EAD, which was started in 2004, is the largest “green investment” project in Bulgaria with 220 mln. U.S. dollars invested in it. The development of this sector is favoured by the availability of high quality resources and good natural conditions. The Greek company “Yioula Glassworks Group” has invested about 70 mln. euro in glass factories in Plovdiv and Sofia. The total foreign capital inflow is 516 593.3 mln. euro.

The government policy with respect to this and other similar types of production should be oriented to the following goals: implementation of the National plans for trade with harmful emissions, looking for opportunities to defend the interests of enterprises from the sector at the respective European forums on issues related to their production specifics, improving the dialogue with local administration for active collaboration with the enterprises in the sector.

In the last few years, **the wood processing industry and the closely connected furniture production** acquired stable market positions. This was made easier by the availability of relatively cheap raw materials, the use of which, however, involves wasting a national

treasure – the forests. At present, the paper and cardboard/pasteboard industry goes through a hard time, because of the economic crisis; but before the crisis, the publishing business was definitely on the rise. The branch has good market positions and relatively high profit/cost ratio for the past period. The amount of foreign direct investment is 113 437.9 mln. euro. The possibilities for future development and solution of the problems of this production type is to be explored in supporting innovation and new technologies, and in the further development of clusters in Trojan – Teteven, Veliko Tarnovo, Velingrad – Peshtera – Batak, and Burgas until 2013; in cooperation with the Branch Chamber as a partner in cluster management, supporting the process of certification and implementation of EU standards, becoming a part of European production and trade chains in order to deal with competition of Asian producers at world markets.

Transport equipment manufacturing is at a crossroad. The enterprises in this sector had different destinies and only a part of them found a foreign strategic investor (the Russe Shipyard) or partner (“Madara” – Shumen) and have good development and prospects. Unlike the Czech Republic and Hungary, where millions of dollars have been invested in the creation of car assembly plants, our national industry is facing a dilemma between expectations for foreign direct investment in the future and investment for renovation of technologies now. There are prospects in this direction, especially after the steps that have been taken to build a Chinese car assembly plant near Lovech. The foreign investment made until the end of 2008 amounts to 30 610.7 mln. euro. The possibilities of direct aid from the state are limited by the existing international and national legislation. At the same time, there is an imperative need for improvement of the cooperation between companies and universities in the field of innovation and technology, in staff development,

as well as in encouraging the creation of clusters.

The low labour productivity in Bulgarian processing industries is related to **high specialization in clearly labour-intensive branches with low level of innovations and of absorption of high technologies.** This is also directly linked to the low level of labour payments – which was believed for a long time to be the main advantage in attracting foreign investment to Bulgaria. Several processing industry sectors appear to be especially appealing to foreign investors. They are: processing of non-metal mineral materials and metal production and casting. The investments in these branches are induced mainly by the growth in the construction sector, but also by high external demand, at least before the onset of the crisis (11, 2007, 173).

The extraction industry occupies a modest place with its 129 mln. euro of foreign investment – in the conditions of the current crisis, this branch is one of the most affected. According to the opinion of a number of experts, however, after the financial and economic crisis will be gone, a very serious energy and raw materials crisis is expected because of the limited natural resources and their exhaustion.

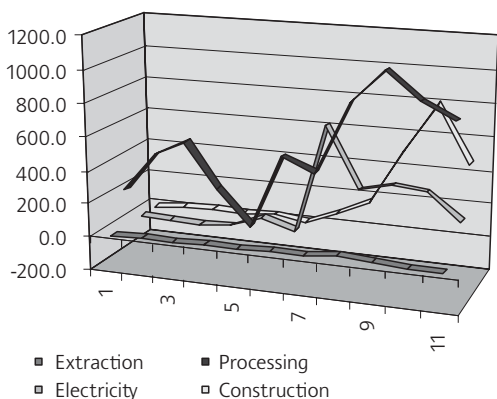


Figure 7. FDI in industry, 1998-2008, mln. euro

The construction sector had a rapid development during the last few years. This applies to business and to residential construction, as well as to building vacation villages. Basically, the construction sector was one of the “motors” of economic growth, generating employment and high salaries. The construction boom was characteristic for the capital city, for some of the big regional centres, and the Black Sea coast. This process has also some negative aspects, mostly associated with ecological and infrastructure problems.

Nonetheless, the interest towards real estate purchase was curbed in the second half of 2008, when banks restrained their credit lines, and managers started to refrain from expensive purchases (4, 2009, 48). The accumulated foreign direct investment exceeds 2.1 milliard euro by the end of the analysed period,.

Our survey would be incomplete, if we paid no attention to some subsectors and production types, in which our country has definitely strong traditions on world markets, irrespectively of their low relative share in the national economy. In the present moment, it is very difficult to describe the production of fine and precision equipment, medical and surgery equipment, as the share of this industry is very low compared to others. Serious presence of foreign capital is observed in „**Trade, repair and technical**

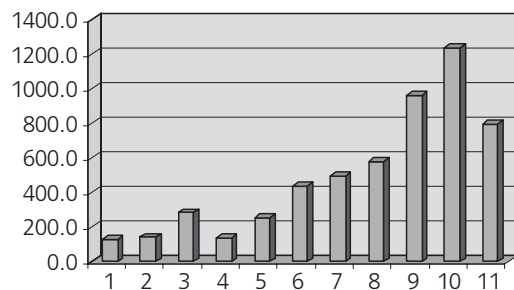


Figure 8. Trade, repair and technical service of cars and motorcycles

service of cars and motorcycles". In the last fifteen years, serious trade chains like "Metro", "Billa", "OMV" have settled on Bulgarian land, and almost all renowned automobile brands like "Toyota", "Ford", "BMW", "Opel", "Mercedes", etc. have their distributors in the country. They succeeded in raising the quality of service at acceptable prices, implementing new marketing techniques and approaches, and improving discipline. Bulgarian consumers now have increased access to a larger variety of products with certified origin and guaranteed quality. Standards of aftersale service and technical maintenance of the newly purchased cars and light trucks are at world levels and represent a model for good practices in the work with customers. The total volume of investment in the country reached 5595.6 mln. euro at the end of the observed period.

From the more than 33 milliard euro invested by the end of 2008, about 32 % are in the industrial sector, but despite the generated positive effects, they are clearly insufficient in terms of quantity and quality in order to fulfil the great tasks faced by the national economy. The biggest investments in the non-financial sector come from the Nederland – 3.917 milliard euro, Austria – 2.43 milliard euro, Greece – 1.265 milliard euro, Germany – 1.092 milliard euro, etc.

Among industrial sectors attracting foreign investment, a special place should be attributed to power industry, metallurgy, petrol, chemical, and plastics industry, the production of mineral products, the processed food industry, and construction. They are a crucial part of the structure of the national economy and form a considerable part of the generated gross internal product. In addition, they create employment and provide opportunities for better conditions and higher living standard of persons employed in enterprises of these branches. In some subsectors like apparel and

textile industry, foreign investors attracted by the lower price of production factors compared to countries of Western and Central Europe and in their pursuit of higher profits in some cases violate Bulgarian labour legislation, not observing regulations regarding working time, not paying in time labour remunerations, not allowing the respective supervising bodies to enter the premises. According to a competitiveness study of 57 countries performed by the Swiss Institute of Management Development in May 2009, Bulgaria is at the 38th place, showing slight progress with one position up compared to 2008. As it is pointed out in the study, part of the problems are due to the low efficiency of government investment and to the unsatisfactory level of education and scientific infrastructure.

As many experts indicate, and this is also proven by NSI data, from the mid-2009, our economy is in the state of recession, which is a reflection of the world financial and economic crisis. The production decrease is due to the decrease of gross added value by 14.5 % in industry compared to the same period last year. The leading economies of the world – USA, Germany, France, etc. show positive signals of slow but gradual recovery from the crisis. This is undoubtedly a positive signal, as the „upward thrust“ of the national economy from the bottom is directly linked to the economic situation in the leading countries of North America and the EU. The forecast for 2010 is weak economic growth. On this basis, it is natural that foreign entrepreneurs

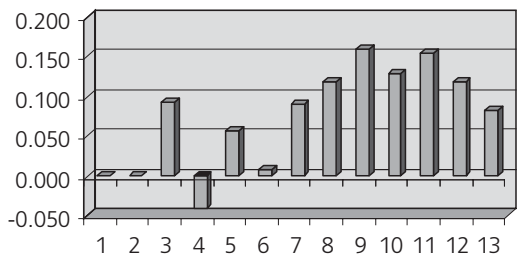


Figure 9. Ratio of reinvested profit to FDI for the period 1998-2008

would reconsider their business intentions, which would result in postponing or correction of their plans. The data for the first quarter on incoming capital flows show that they fluctuate at the level of about 1.1 milliard euro and the most optimistic forecasts are for 4 – 4.5 milliard euro for the whole 2009. They cover 57.5 % of the current account deficit of the balance of payments on yearly basis for the period January – May. The deficit itself is going down from 3.56 milliard euro to 1.97 milliard euro (4, 2009, 11). In the first half of the current year, the expected total amount of investment is 1534.7 milliard leva, only 15.48 % of them in the real sector. This is one of the lowest levels of foreign investment since 2005. The „financial mediation“ sector still occupies the leadership position with almost 490 mln. euro, due to the stable positions of the bank and insurance sectors. The second place is occupied by the sector of “Transactions with real estate, tenancy, and business services” with 304.6 mln. euro, as real estate attractiveness is a factor making deals profitable. On the third place, with 228,8 mln. euro of foreign investment, is the trade sector. In general, except for the low levels of investment, with certain conditionality we can conclude that no radical change is observed in the “status quo” with respect to the structure of incoming foreign investment.

Conclusions

First, the process of attracting foreign direct investment has to be in conformity with the priorities of the national economy, so that it would be possible to integrate the latter into the European economy. The investment in human and intellectual capital should be a paramount task of management teams. Unfortunately, the data show that foreign direct investment in activities providing services to persons is below 1 %, and its levels in healthcare are symbolic. The situation with respect to the investment activity in the education and science sector is the same. Data are missing on the attracted foreign investment

in the field of high technologies like energy-saving and new technologies, development of new materials, communication technologies. For this reason, it is impossible to analyze the type and structure of high technology products. Regarding infrastructure, it should be emphasized again that data are indirect; the sector „Transport, storage, and communication“, has attracted 1749.3 milliard euro, representing only 0.053 % of the volume of foreign direct investment. Our country suffers from a critical need of investment both in infrastructure and in the agricultural sector (see Table 3). However, these sectors are currently not attractive for foreign investors. The quantitative parameters are not sufficient to make an objective assessment of the place and role of foreign direct investment in economic development.

Second, the opinion is gaining strength that in its qualitative aspect, foreign direct investment does not correspond to the country needs and to the priorities of future economic development. The attention is increasingly focused on the necessity of developing and implementing government policies, which introduce economic incentives for investment in branches, sectors, and industries corresponding to the pursued national goals and priorities. The ratio of reinvested profit to direct investment in the first years was 0 %, reaching 15.4 % in 2006 (see Graph 9). The prevailing trend is obviously to export profits and generate negative financial results through different price transfer mechanisms. Some authors defend the thesis of the wrong orientation of resources, considering the full isolation of the state as one of the reasons for the current global crisis [6, 2009, 10].

Third, once the current crisis is overcome, the transnational corporations, which are the motive force of the international capital inflow, will be much more cautious in their investment initiatives. They will probably reconsider their investment policies, including policies towards new raising markets like Bulgaria. This will

apply fully to portfolio investment. Whether the focus will be on speculative profits putting the international financial system to trial or on investment oriented towards “reasonable” profitability levels – this will depend on the new financial architecture. Negative attitudes will still exist in 2010, when stronger signs of revitalization of the world economy are expected.

Fourth, an important element, disregarded so far, is the ecological problems, arising after the continuous disturbance of the environment. Part of these problems are received as a legacy from privatized enterprises, others are being created in the production activity of joint ventures and foreign industrial enterprises operating in the country. One of the potential opportunities for bringing foreign direct investment consists in the so called „green technologies”, which can be used to transform the decreased remaining part of the harmful emissions quotas into new investment. The idea to return the traded quotas back to the country in the form of investment input is a rational one. It is necessary to cover this segment because of the low energy efficiency, the need for environmental conservation, and development of several sectors of the national economy like tourism and the rural economy. To implement these measures, it is necessary to improve the work of both central and local administrations in providing services to investors; this requires high language competency, better administrative capacity, and higher flexibility. In such a dynamic environment, it would be appropriate for the Bulgarian Investment Agency to take on the task of making its own analyses in the field of investment activity and investment attractiveness. The speed, transparency, and quality of service from the part of the central and local administration will be crucial for the improvement of the investment image of the country both in the conditions of recession and during the period of recovery and growth. Moreover, it should be taken into account that our country will be placed in the strongly competitive

external environment of the countries of Central and Eastern Europe, potential recipients of foreign direct investment.

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