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***Creation of Joint Ventures Among Participating Countries:
Contemporary Trends and Prospects in Greece and Bulgaria
Technical Guide***

Elaborated by the University of Macedonia
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TABLE OF CONTENTS

EXECUTIVE SUMMARY	1
PART A. MEANS OF FDI AND THE ESTABLISHMENT OF A JOINT VENTURE COMPANY	2
1. PREPARATION FOR ESTABLISHING A JOINT VENTURE COMPANY	3
1.1.Evaluation of alternative investment scenarios	3
1.1.1.Exporting.....	5
1.1.2.Licensing.....	6
1.1.3.Franchising.....	6
1.1.4.Foreign Direct Investment (FDI).....	7
1.1.4.1.Green field strategy.....	8
1.1.4.2.Acquisition or Brown field strategy	8
1.1.4.3.Joint Ventures	8
1.1.4.4.Other alternatives.....	10
1.2.Parameters affecting a joint venture investment	10
1.2.1.Compatibility.....	11
1.2.2.Capability	11
1.2.3.Commitment.....	12
1.2.4.Risk analysis.....	12
1.2.4.1.Political risk.....	14
1.2.4.2.Economic risk.....	14
1.2.4.3.How to prevent risk	14
1.2.4.3.1.Things that should be taken under consideration	15
1.2.4.3.2. Adjusting risk.....	15
1.2.4.3.3. Alternatives scenarios analysis.....	15
1.2.4.3.4.Financial ratio projections.....	16
1.2.3.4.5.Sensitivity analysis.....	16
1.2.3.4.6.Simulation modeling	16

1.2.3.4.7. Internal risks: managing the risks of competitive cooperation..	16
2. PLANNING FOR THE JOINT VENTURE.....	17
2.1. Strategic and operational planning.....	17
2.1.1. Strategic planning	17
2.1.2. Operational planning.....	18
2.1.2.1. Negotiating the agreement.....	19
2.1.2.2. Structuring the agreement.....	20
2.1.2.3. Management issues	21
3. GENERAL LEGISLATIVE FRAMEWORK.....	26
3.1. European Union legislative framework	26
3.1.1. Merger regulation.....	26
3.1.1.1. Scope of the merger regulation.....	27
3.1.1.2. Compatibility with the EU legislation.....	27
3.1.1.3. Dominant position impeding competition.....	27
3.1.1.4. Risk of co-ordination	27
3.1.2. License agreements	28
3.1.2.1. Definition of the term "intellectual property rights"	28
3.1.2.2. Typical terms used in the licenses agreements.....	29
3.1.2.3. Types of license agreements	29
3.1.2.4. Industrial property rights and license agreements.....	29
PART B. COUNTRY ANALYSIS OF PARTICIPATING COUNTRIES BULGARIA & FYROM	31
4. COUNTRY ANALYSIS OF BULGARIA.....	32
4.1. Country profile	32
4.1.1. Location, Climate, Demographics	32
4.1.2. History.....	33
4.1.3. Government.....	33

4.1.3.1. Political environment-synopsis of political system in Bulgaria	34
4.1.3.2. Major political issues affecting business climate.....	34
4.1.4. Currency and Exchange controls.....	35
4.1.5. Infrastructure	36
4.1.5.1. Telecommunications.....	36
4.1.5.2. Road transportation network.....	37
4.1.5.3. Railways	37
4.1.5.4. Ports.....	38
4.1.5.5. Air Transport.....	38
4.1.5.6. Energy	39
4.1.5.7. Water system	40
4.2. Bulgaria's Economic Environment	40
4.2.1. Background	40
4.2.2. Bulgaria - resumption of growth (1998-2000).....	40
4.2.3. Stability Pact.....	44
4.2.4. Sustainable growth for 2001	45
4.2.5. Industry - Leading Branches in Bulgarian Economy.....	46
4.3. Foreign Trade	48
4.3.1. Trade Volume, Trade Partners, Structure	49
4.3.2. Major trade agreements	51
4.3.3. Foreign trade regulations.....	52
4.3.3.1. Import and export regulations.....	52
4.3.3.2. Customs law and tariff system	53
4.3.3.3. Trade license.....	54
4.3.3.4. Free trade zones.....	54
4.3.3.5. Protection of competition	55

4.4. Foreign Direct Investment (FDI)	57
4.4.1. Foreign Direct Investment Statistics.....	58
4.4.2. Foreign Investment legislation.....	60
4.4.2.1. Institutional framework	60
4.4.2.2. Foreign investors.....	62
4.4.2.3. Definitions and forms of investments.....	62
4.4.3. Legal and International guarantees for Foreign Investment	63
4.4.4. Establishment of Enterprises with Foreign Investment	64
4.4.4.1. Creating a joint venture in Bulgaria	64
4.4.5. Profit and Capital Repatriation.....	65
4.4.6. Ownership of Real Estate.....	66
4.4.7. Inter-ministerial Groups for Institutional Support for Priority Investment Projects	66
4.4.8. Concession Regime.....	66
4.4.8.1. Concessions over objects which are public state property and over activities for which state monopoly has been established.....	67
4.4.8.2. Granting concessions over object - public municipal property (regulated by the Law on Municipal Ownership).....	68
4.4.9. Licensing of the Telecommunication Activities.....	68
4.4.10. Licensing of the activities in energy sector	69
4.5 Privatization	70
4.5.1. Issues in Mass and Large - Scale Privatizations in Bulgaria.....	70
4.5.2. Cash Privatization	72
4.5.3. Forthcoming privatization deals.....	74
4.5.4. Privatization program of 2001	74
4.5.5. Privatization legislation	75
4.5.6. Voucher privatization	76

4.5.7. Restitution.....	76
4.5.8. Restructuring.....	76
4.6. Company law and business organizations in Bulgaria	77
4.6.1. Forms of Business Organizations	77
4.6.2. Formation and Registration of a Company, Branch and Representative Office	79
4.6.3. Other Forms of Business Organizations.....	80
4.7. Accounting and Auditing	81
4.7.1. Accounting and Audit Legislation	81
4.7.2. Accounting Principles.....	82
4.7.3. Valuation of the Balance Sheet Items.....	83
4.7.4. Annual Financial Statements.....	84
4.8. Taxation	85
4.8.1. Direct Tax: Individuals.....	85
4.8.2. Direct Tax: Corporations.....	89
4.8.2.1. Income determination	90
4.8.3. Withholding Taxes	92
4.8.3.1. Tax administration.....	94
4.8.4. Indirect Taxation: Value Added Tax Act (VAT)	95
4.8.4.1. VAT credit refund	96
4.8.5. Indirect Taxation-Excise Duties.....	98
4.8.6. Customs Duties.....	99
4.9. Labor Force and Employment Regulation.....	99
4.9.1. Labor Supply	99
4.9.2. Employment of Foreign Persons.....	107
4.9.3. Work Regulations for Foreigners	109
4.10. Pension insurance system in Bulgaria.....	110
4.10.1. Introduction.....	110

4.10.2. Investment regulations.....	114
4.10.3. Supervision.....	117
4.11. Main points about Country Analysis of Bulgaria.....	118
5. COUNTRY ANALYSIS OF FYROM	120
5.1. Country profile	120
5.1.1. Location, Climate, Demographics	120
5.1.2. History.....	122
5.1.3. Government.....	125
5.1.4. Infrastructure	127
5.2. Legislative, Executive and Judicial System	128
5.2.1. Introduction.....	128
5.2.2. Legislative system.....	129
5.2.3. Central and Local Government	131
5.2.4. Judicial System	132
5.2.4.1. Judicial council of FYROM	133
5.2.4.2. Public prosecutor	133
5.2.4.3. Constitutional court of FYROM	133
5.2.4.4. Ombudsman	133
5.3. Education.....	134
5.4. FYROM's Economic Environment	136
5.4.1. History - Economic Outlook of FYROM.....	136
5.4.2. Present - Economic Outlook of FYROM.....	137
5.4.3. Demand and Supply	138
5.4.4. Structure of the economy – economic indicators (1995-2000)	139
5.5. Foreign Trade and Customs Regulations.....	145
5.5.1. General provisions	145
5.5.2. Foreign trade pattern	145

5.5.3. Foreign trade: Imports and Exports of FYROM	148
5.5.4. Trade and Customs regulations	150
5.5.4.1. Registration and licensing requirements	150
5.5.4.2. Quotas	150
5.5.4.3. Duties	151
5.5.4.4. Levies and fees	151
5.5.4.5. Tariffs and customs procedures	151
5.5.4.6. Duty Free Trade Zones	151
5.6. Foreign Direct Investment (FDI)	151
5.6.1. Advantages and Weaknesses of FDI in FYROM	151
5.6.2. Foreign investment operations under the business legal environment	153
5.6.2.1. Investment promotion	153
5.6.2.2. Investment promotion institutions	154
5.6.3. Regulatory environment for FDI	157
5.6.4. Guarantees for Foreign Investments	158
5.6.4.1. Bilateral treaties and multilateral conventions	158
5.6.4.2. Multilateral conventions and other guarantees	159
5.6.5. Dispute Resolution	159
5.6.5.1. General review	159
5.6.5.2. Dispute settlement according to the commercial code	160
5.6.6. Incentives	161
5.6.6.1. General review	161
5.6.6.2. Tax and other fiscal incentives	162
5.7. Other Rules Relevant to Foreign Direct Investment	163
5.7.1. Business Organizations	163
5.7.1.1. Trading companies and a trader-individual (and a single-trader)	163

5.7.1.2.Representative offices of foreigners in FYROM.....	168
5.8.Privatization	170
5.8.1.Privatization Program.....	170
5.8.2.Methods of Privatization	175
5.8.3.Privatization procedure	177
5.8.4.Enterprise Restructuring	178
5.8.5.Evaluation of the Results	180
5.8.6.Financial performance of enterprise Sector.....	182
5.8.7.Sectors with investment potential.....	183
5.9. Fiscal and Monetary Policy, Foreign Exchange	186
5.9.1.Fiscal Policy.....	186
5.9.2.Monetary Policy.....	187
5.9.3. Foreign Exchange Regulation.....	189
5.10. Banking System in FYROM.....	189
5.10.1. Overview.....	189
5.10.2.Interest rates and borrowing conditions.....	191
5.10.3.Domestic and foreign payment operations (types of bank accounts).....	192
5.11. Bankruptcy.....	196
5.12. Competition	200
5.12.1. Overview of the general competition environment.....	200
5.12.2.Market structure: the importance of legacies	201
5.13.3.The current legal framework for a competitive market.....	202
5.12.4.New laws regulating competition policy	204
5.13. Labor Regulations	205
5.13.1.Overview of the labor regime	205
5.13.2.Categories of labour contracts	205

5.13.3. Wage Determination	207
5.13.4. Working Time	211
5.13.5. Flexibility of Employment	213
5.13.6. Employee Representation at Work Place	217
5.13.7. Labor Conflicts	218
5.14. Accounting and Taxation	221
5.14.1. Accounting and Audit System in FYROM	221
5.14.2. Taxation	224
5.14.2.1. Personal Income Tax	228
5.14.2.2. Profit Tax or corporate tax	231
5.14.2.3. Trade tax for goods and services	233
5.14.2.4. Excise tax	236
5.14.2.5. Property tax	236
5.14.2.6. Inheritance and gift tax	237
5.14.2.7. Estate and rights trade tax	237
5.14.3. Social Security Contributions	238
5.15. Participation in International Programs: Industrial Property Protection	241
5.16. Conclusions	243
PART C. GREEK INVESTMENTS IN BULGARIA AND FYROM – CASE STUDY	248
6. GREEK INVESTMENTS IN BULGARIA AND FYROM	249
6.1. Greek Business Activities in the Balkan region	249
6.1.1. Regional economic co-operation in the Balkan region	249
6.1.2. Greek government supporting policies in the Balkan region	249
6.1.2.1. General principles of Greek foreign policy in the Balkans	249
6.1.2.2. Greece create incentives for Balkan region	252

6.1.3. Greek investments in the Balkan region	253
6.1.3.1. Tools of finance	254
6.1.3.2. Areas of economic activity in the Balkans and Greek presence.....	254
6.1.3.3. Ten major Greek investors in the Balkan countries.....	259
6.2. Greek Investments in Bulgaria	260
6.2.1. Investment climate in Bulgaria	261
6.3 Greek investors in FYROM.....	264
6.4. The Case of Greek Joint Venture “DELTA Holding S.A ” in Bulgaria ..	268
6.4.1. Introduction.....	268
6.4.2. Literature.....	268
6.4.2.1. Why invest in the Balkan States?	268
6.4.2.2. FDI decision-making.....	269
6.4.2.3. Linking strategy to capital budgeting.....	270
6.4.3. Research questions and methodological issues	270
6.4.4. Case Study of Delta Holding S.A (a joint venture in Bulgaria)	270
6.4.4.1. Delta in the Greek market.....	270
6.4.4.2. Delta's internationalization strategy.....	271
6.4.4.3. Delta International Holdings (DIH)	273
6.4.4.4. FDI decision process: The case of Bulgaria.....	274
6.4.5. Uses of Accounting information in the FDI decision process.....	276
6.4.6. Conclusion: The decision criteria applied by Delta	276
PART D. CONCLUSIONS - SUGGESTIONS	278
7. CONCLUSIONS - SUGGESTIONS	279
PART E. APPENDICES, ABBREVIATIONS & ACRONYMS, BIBLIOGRAPHY & INTERNET RESOURCES	283

8. APPENDICES	284
APPENDIX I. Useful Contacts in Bulgaria	284
APPENDIX II. Useful Contacts in FYROM	292
APPENDIX III. The Largest Foreign Investors in Bulgaria, by Sector	296
APPENDIX IV. The Top Greek Investments in Bulgaria & FYROM	303
APPENDIX V. Greek Investments in FYROM.....	304
APPENDIX VI. Bulgaria's Law on Foreign Investment	310
9. ABBREVIATIONS & ACRONYMS	317
10. BIBLIOGRAPHY & INTERENT RESOURCES.....	322



LIST OF TABLES

Table 1.Types of risks.....	13
Table 2.Bulgaria: Country Profile.....	32
Table 3.Key Economic indicators of Bulgaria, (1995, 1997-2000).....	41
Table 4.Key Economic Ratios of Bulgaria, (1990, 1999-2000).....	42
Table 5.Foreign Direct Investments in Bulgaria, by year, in USD million.....	44
Table 6.Average annual growth of main Economic indicators of Bulgaria by decades and years.....	page 45
Table 7.Structure of Industry output by branches, for the year 2000.....	45
Table 8.Export and Import volumes of Bulgaria, in USD million.....	49
Table 9.Trade and Finance Indicators of Bulgaria (1995-2000).....	49
Table 10.Territorial Structure of Export and Import for the year 2000.....	50
Table 11.Direct and Portfolio Investments in Bulgaria,1996-2000, (in USD mil)	58
Table 12.Foreign Direct Investments inflows by years (1993-2000).....	58
Table 13.Foreign Direct Investments by Countries in USD millions.....	59
Table 14.Foreign Direct Investments by Sectors, by years (in USD mil).....	60
Table 15.Largest privatization deals in Bulgaria, for the year 2000.....	73
Table 16.Annual Income Taxed, (in BGN).....	87
Table 17.Monthly Employment Income Taxed (in BGN).....	87
Table 18.Tax rates under double tax treaties between Bulgaria & countries	.93
Table19.Bulgaria: Labor force, Employment & Unemployment (1993-2000).....	100
Table 20.FYROM:Country Profile.....	121
Table 21.Geographic, Demographic and Social Indicators of FYROM (1996-1999).....	122
Table 22.Basic Economic Development Indicators (1992-1996).....	137
Table 23.Basic Economic Indicators of FYROM (1996-2000).....	138
Table 24.Economic Indicators of FYROM by years (1995-2000).....	140
Table 25. Key Economic Ratios of FYROM in percentage of GDP.....	140

Table 26. Average annual growth of main Structure Economic Indicators of FYROM.....	141
Table 27. Social Product of the Industry by Sectors.....	142
Table 28. FYROM: Destination of Merchandise Exports, 1995-1998 (in millions USD)	146
Table 29. FYROM: Origin of Merchandise Imports, 1995-1998, (in millions USD).....	147
Table 30. Foreign Trade in FYROM, in millions of USD, (1990-1997.....)	148
Table 31. FYROM: Exports & Imports by final use, 1995-1998.....	149
Table 32. Export & Import volumes for the years 1999-2001, in USD millions	149
Table 33. Trade & Finance Indicators of FYROM, 1995-1999.....	149
Table 34. Foreign Direct Investments (FDI) in millions of USD (net inflows)..	152
Table 35. FYROM: Privatization by Model of Transformation, by number of firms, (1995-1999).....	177
Table 36. Distribution of enterprises by number of employees.....	201
Table 37. Employment, Unemployment and net average of wages in FYROM, (Annual percentage change)	208
Table 38. FYROM: Age, Education and Gender Structure of the Unemployment rate (1996-1999).....	211
Table 39. FYROM: Tax Summary as of April 1, 2000.....	225

LIST OF FIGURES

Figure 1.External Influences of carrying out International Operations.....	3
Figure 2.Parameters used in choosing a foreign country.....	12
Figure 3.Framework of joint venture agreement.....	18
Figure 4.Structure of Privatization deals by sectors (1993-2000).....	72
Figure 5.Financial effects from all privatization deals in Bulgaria for 1993 until 2000 (in USD millions).....	73

LIST OF DIAGRAMS

Diagram 1. Inflation rate (as % of CPI) for the years 1991-2000.....	42
Diagram 2.Gross Domestic Product (% real growth) for the years 1991-2000.....	43
Diagram 3.Bulgaria:Main partners share in trade turnover (%) 1995-2000.....	50
Diagram 4.Main trade partners in Bulgaria by countries in 2000 (in USD millions).....	51
Diagram 5.Foreign Direct Investment Inflows by years, 1992-2000 (in USD millions).....	59

SUMMARY

Many forces are driving companies around the world to globalize, in the sense of expanding their participation in foreign markets. In order for businesses to accommodate such a mentality a strategy is needed. This guide deals with the subject of Foreign Direct Investment by the mean of Joint Venture, as a strategic business expansion of Greek investors in the neighboring countries of Bulgaria and Former Yugoslav Republic of Macedonia (F.Y.R.O.M). The guide is consisted of five sections.

The **first section** consists of an evaluation of alternative investment scenarios needed for the formation of a joint venture, followed by the parameters that are affecting such as investment and a risk analysis before the actual joint venture investment takes place. Also deals with the actual organization of the joint venture. In terms of strategic and operational planning, it refers to management issues as well as marketing and human resource issues, that a joint venture has to deal with before the commencement of its operations. Lastly, follows a presentation of the general EU legal framework and license agreement concerning joint ventures.

In the **second section** there is a detailed country analysis of each one of the participating countries namely Bulgaria and FYROM. This analysis consists of the following: Country's profile, Political environment, Economic environment, Foreign trade regulations, Foreign Direct Investments, Privatization, Business law and forms of business organizations, Accounting and Auditing, Taxation, Labor Force and Employment regulations etc. All this documentation can reveal investments opportunities for a foreigner (and especially for a Greek Investor), which exists in these countries, as well as the competitive advantages and disadvantages that the investor has to take into consideration in order to implement a Foreign Direct Investment or a joint venture there.

The **third section** analyzes the Greek business activity in the Balkan region and particularly in Bulgaria and FYROM. Moreover, it presents the important role that Greece has, and its impact for the political stability and the economic growth of the Balkan countries, as well as the growth of Foreign Direct Investment there. At the end of the section a case study of a joint venture establishment is presented between a Greek private company (Delta Holding S.A) and a Bulgarian state – owned company (Vitalact), in order to understand how the joint venture was contacted, and what were the pros and cons that a potential Greek investor needs to consider in order to do FDI by the mean of joint venture in the participating countries.

The **fourth section** contains conclusions and suggestions relevant to the advantages and disadvantages of the joint venture as a strategic business choice and critical factors that affect joint venture establishment in the specific neighboring countries such as Bulgaria and FYROM.

Finally, the **fifth section** contains appendices such as a list of useful contacts for the countries mentioned above etc., the abbreviations and acronyms which are referred in the guide, and finally lists of relevant bibliography and internet resources used for the completion of this guide.

**PART A. MEANS OF FDI AND THE ESTABLISHMENT
OF A JOINT VENTURE COMPANY**

1. PREPARATION FOR ESTABLISHING A JOINT VENTURE COMPANY

1.1. Evaluation of alternative investment scenarios

International business environment is rapidly changing leading to the globalization of activities. Competition in many industries is occurring on a global scale and many companies are forced to consider the world as one vast market.

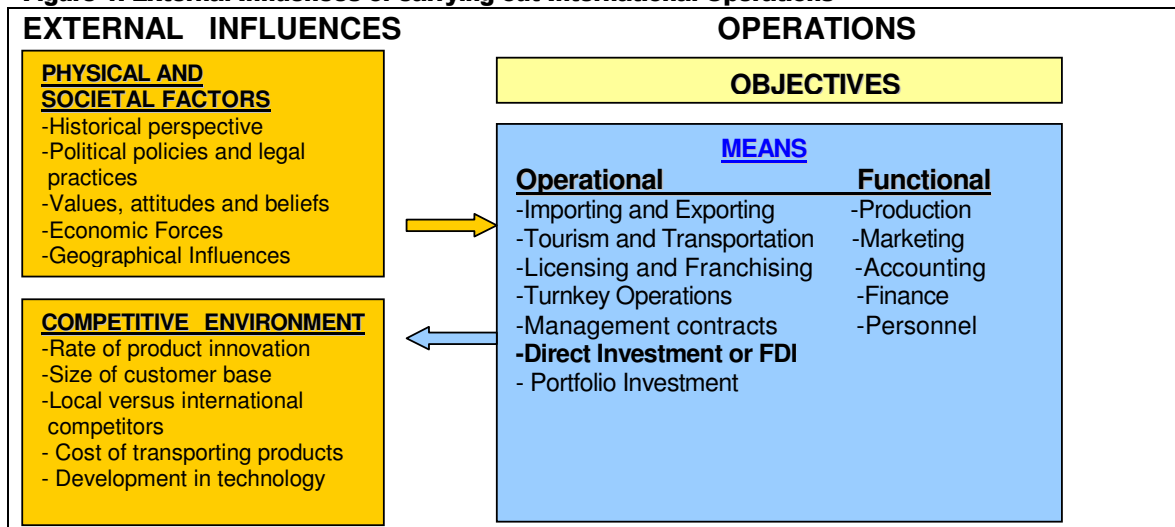
At the same time despite all the discussion about the globalization of the world, national differences still exist and are affecting the way business is conducted. So there is always the tension between the need to view the world as a single market and the need to be responsive to differences between countries and their markets.

In light of this globalize view international investments occur with increasing frequency. International investment is defined as a firm investing resources in business activities, outside its domestic market. Companies engage in international business for three primary reasons:

1. *to expand their sales,*
2. *to acquire resources,*
3. *to diversify their sources of sales and supplies.*

When a company conducts International Business, it must choose from among different operational forms, or means of conducting the business. In making its choice, a company should consider its objectives and resources as well as the environment in which it will operate. The following figure shows the means of carrying out International operations and the physical and societal factors as well as the competitive environment which are external influences on international business operations.

Figure 1. External Influences of carrying out International Operations



Source: John D. Daniels & Lee H. Radebauhg., "International Business, Environment and Operations", 7th edition, 1996, page 19.

A company environment is the aggregate of conditions outside the company that influence the success. A company also influences its external environment but usually to a lesser degree. As shown in figure 1, the external environment includes physical factors such as a country's geography, and societal factors, such as

a country's politics, economy, law and culture. It also includes competitive factors such as the number and strength of suppliers, customers and rival companies.

To operate within a company's external environment, its managers must have not only knowledge of business operations but also a working knowledge of the basic social sciences: **history, political science, law, anthropology, sociology, psychology, economics and geography.**

More specifically: ***Studying history***, particular the past relationships among countries and people's attitudes toward business and government, can help business people better understand how international business functions in the present. This understanding also can enable them to plan more effectively for the future. ***Politics*** has played and will play an important role in shaping business worldwide. Political science, in part, describes relationships between business and government and explains how the two interact with each other and react when their interests conflict. The political leadership in each country controls whether and how international business will occur in that country. Domestic and international ***law*** determines largely what a manager of a company operating internationally can do. Domestic law includes regulations in both the home and host countries on such matters as taxation, employment, and foreign exchange transactions. The related sciences of ***anthropology, sociology, and psychology*** describe, in part, people's and mental development, behavior, and interpersonal activities. By studying these sciences, managers can better understand societal values, attitudes, and beliefs concerning themselves and others. This understanding can help them function better in different countries. ***Economics*** explains, among other concepts, why countries exchange goods and services with each other, why capital and people travel among countries in the course of business, and why one country's currency has a certain price relative to another's. Managers who know ***geography*** can better determine the location, quantity, quality and availability of the world's resources, as well as the best means to exploit them.

In addition to its physical and societal environments, each company operates within the competitive environment which varies among countries. Competitive factors prompt companies to differentiate practices among countries in which they operate. They also can cause companies to choose different means of operating, depending on the country.

Thus, as shown in figure 1, a company can engage international business through various means, including: **Exporting and/or Importing, Licensing, Franchising, Foreign Direct Investment (FDI) and Strategic Alliances** with other companies. Each of these means, however, involves a firm acting alone or hiring a second individual or firm—often one further down the distribution chain, to act on its behalf. In contrast, a strategic alliance results from cooperation among two or more firms. Each participant in a strategic alliance is motivated to promote its own self-interest but has determined that cooperation is the best way to achieve its goals.

One form of FDI international investment is a **joint venture between a local and a foreign company**. **Joint ventures** are becoming increasingly popular as a way to expand internationally. The phenomenon is not limited to certain countries or industries but is happening all over the world. Characteristic examples in Greece are the mobile telephony company COSMOTE, a joint venture between OTE and the Norwegian company TELENOR and the co-operation between CONTINENT and "Marinopoulos" to establish hypermarkets all over Greece.

A joint venture is a special type of strategic alliance between international firms in which two or more firms join together to create a new business entity that is legally separate and distinct from its parents, for their mutual benefit. Joint ventures are normally established as corporations and owned by the founding parent companies in whatever proportions they negotiate. Many are owned equally by the founding firms or with an unequal ownership, although this is becoming a more rare phenomenon. Initial agreement may also provide for changes in ownership shares as well.

1.1.1. Exporting

Exporting is the process of sending goods or services from one country to other countries for use or sale there. There are three types of export activities: **Indirect exporting, Direct exporting and Intra-corporate transfers.**

- **Indirect exporting** occurs when a firm sells its products to a domestic customer, which in turn exports the product in its original or in a modified form. In most cases indirect exporting activities are not part of a conscious internationalization strategy of a firm. Thus, they yield the firm little experience in conducting international business. Furthermore, for firms that passively rely on the actions of others, the potential short-term and long-term profits available from indirect exporting are often limited.
- **Direct exporting** involves sales to customers, either distributors or end users, located outside the company's country. It means an active company participation in the exports of its production, with the subsequent acquiring of valuable experience.
- **Intra-corporate transfer** is the selling of goods by a firm in one country to an affiliated firm in another. It happens with many multinational companies, which are importing and exporting semi-finished goods and components parts to and from their domestic and foreign factories in order to lower their production costs. Such methods occur also in the service sector. A newspaper for example, with multiple local editions, will use article and data gathered from its various correspondents around the world in addition to the material used for each separate edition and vice versa.

The selection of the best export form, will be apparent once the following issues have been addressed:

- **Government policies:** The existence of export promotion policies, of export financing programs of the exporting country, tariff and non-tariff barriers of the importing country must be considered beforehand.
- **Marketing concerns** such as image, distribution and responsiveness to the potential customers in the foreign country are some of the marketing parameters that should be checked in advance.
- **Logistical considerations** affect such issues as packaging, transporting, inventory management and distribution of export goods.
- **Distribution issues** concern the choice between establishing a company owned distribution network or working with an existing distributor. The former has the advantage of eliminating another step in the distribution ladder, thus increasing profit. Therefore the control over the distribution is extended. However, it requires substantial capital investment and active company involvement. The latter solution, working with a distributor that is, is a more economically viable, does not have the positive characteristics of the previous one and in addition it requires a very good selection of the distributor, whether the distributor will be exclusive or not.

As a conclusion, **exporting has the following advantages:**

- ✓ Relatively low financial exposure.
- ✓ Permits gradual market entry.
- ✓ Acquiring of knowledge about the local market.
- ✓ Avoidance of investments in the foreign company.

However, there are, **some disadvantages**, which are the following:

- ✓ Exports are vulnerable to tariffs and non-tariff barriers.

- ✓ There are logistical complexities involved.
- ✓ There is always the risk of conflicts with distributors.

1.1.2.Licensing

Another method of entering a foreign market is licensing, in which a firm, called the licensor, leases the right to use its intellectual property technology, work, methods, patents, copyrights, brand names or trademarks- to another firm called the licensee, in return for a fee. Usually it involves little initial costs since the knowledge is already available and it allows companies to take advantage of any location advantages in the foreign country without incurring any ownership, managerial or investment obligations.

So the **advantages** are obvious:

- ✓ There are low financial risks.
- ✓ Low-cost way to assess foreign market potential.
- ✓ Avoid tariffs, non-tariff barriers, restrictions on foreign investment.

The **disadvantages** of this approach used in expanding a company into international operations are the following:

- ✓ Limits market opportunity or profits since the licensor usually has some restrictions, e.g., not to enter by itself into the foreign market.
- ✓ Dependency on licensee.
- ✓ Potential conflicts with the licensee.
- ✓ Risk of creating future competitor: If the license agreement stops, either intentionally or because it has expired, then there is always the risk of having created another competitor.

1.1.3.Franchising

Franchising is essentially a special form of licensing. It allows the franchiser more control over the franchisee and more support from the franchisee. The franchiser provides the franchisee with trademarks, operating system, reputation and so forth. Usually the franchiser has enjoyed domestic success and the concept is transferable to another country.

The **advantages** are the following:

- ✓ Low financial risks.
- ✓ Low-cost way to assess market potential.
- ✓ Avoid tariffs, non-tariff barriers, restrictions on foreign investment.
- ✓ Maintain more control than with licensing.
- ✓ Franchisee provides knowledge of local market.

The **disadvantages** are the following:

- ✓ Limits market opportunity or profits since the franchiser has some restrictions e.g. not to enter by itself the foreign market.
- ✓ Dependency on the franchisee.
- ✓ Potential conflicts with the franchisee.
- ✓ Risk of creating future competitor: If the franchisee agreement ceases, either intentionally or because it has expired, then there is always the risk of having created another competitor.

1.1.4. Foreign Direct Investment (FDI)

Foreign investments involves ownership of foreign property in exchange for financial return. Foreign investment takes two forms:

- **Direct Investment**
- **Portfolio Investment.**

Direct Investment or FDI

A Direct investment is one that gives the investor a controlling interest in a foreign company. Such a direct investment also is called a **Foreign Direct Investment (FDI)**. When two or more companies share ownership of an FDI, the operation is called a **joint venture**. When a government joins a company in and FDI, the operation is called a **mixed venture**, which is a type of joint venture.

FDI is the highest commitment a domestic company can make in international business because it usually involves not only the infusion of capital but also a transfer of personnel and technology. Hence, such investment usually comes after a company has acquired experience in exporting and importing. FDI can provide the controlling company with access to certain resources or to a market. For example, through Disney's direct investment in China, the company access that country's cheap labor to make clothing, for its Mic-Kids outlets. In addition its direct investment in Euro- Disney enables Disney to service a market it could not otherwise tap. In 1996 more than 37.000 companies worldwide have FDIs that encompass every type of business function. FDI is not the domain of large companies only.

The key features of the FDI are:

- a) control,
- b) high commitment of capital and personnel and technology,
- c) access to foreign resources,
- d) higher foreign sales than exporting,
- e) partial ownership.

Portfolio Investment

A portfolio investment is an investment that gives the investor a non-controlling interest in a company or ownership of a loan to another party. Usually a portfolio investment takes one of two forms: stocks in a company or loans to a company or country in the form of bonds, bills, or notes that the investor purchases.

Foreign portfolio investments are important for most companies that have extensive international operations. They are used primarily for short-term financial gain, that is, as means for a company treasures routinely move funds among countries to get higher yields on short-term investments.

Foreign Direct Investment

Foreign direct investment (FDI) may occur when a firm invests directly in new facilities to produce a product or a service in a foreign country or when the foreign company buys an existing company.

FDI is divided into horizontal and vertical FDI. The former is FDI in the same industry as the foreign company operates at home. The latter is an FDI in an industry that provides inputs for a firm's domestic operations.

Alternatively it may be FDI in an industry abroad that sells the outputs of a firm's domestic operations. There are three methods for FDI.

1. Building new facilities, known as **Green Field strategy**.
2. Buying existing assets in a foreign country, known as **Acquisition** or **Brown Field** strategy.
3. Participating in a **Joint Venture**.

1.1.4.1.Green field strategy

The **Green Field Strategy** involves starting a new operation from scratch. The company buys land, constructs new facilities and is locating the necessary personnel to staff the new operation.

The **advantages** of such an approach are the following:

- ✓ The firm can select area site, people and everything else in between, without any prior restrictions.
- ✓ There is no past history of debts, mismanagement or outdated equipment that the foreign company has to undertake.
- ✓ Gradual acclimatization of the foreign company to the environment and culture of the foreign country.

Disadvantages may be the following:

- ✓ Successful implementation takes time, patience and capital.
- ✓ Land or people may not be available or very expensive.
- ✓ Various local laws have to be obeyed for the construction of the facility.

1.1.4.2.Acquisition or Brown field strategy

Acquisition or Brown field strategy is another FDI strategy. It involves the purchase of an actual company (or buying existing assets of a company) in a foreign country.

Advantages to this approach are the following:

- ✓ Quick control over the acquired firm and its capabilities.
- ✓ The acquisition strategy adds now new capacity to the industry, which in times of overcapacity is an obvious advantage.
- ✓ It can assist in the strategic shift of the company to new activities.

Disadvantages to this approach are the following:

- ✓ The acquiring firm assumes all the liabilities – financial, managerial and otherwise – of the acquired firm.
- ✓ The acquiring firm usually has to spend substantial sums up front.
- ✓ The green field strategy, in contrast, allows a firm to grow slowly and spread its investment over an extended period of time.
- ✓ An international acquisition may also reveal unexpected local issues that must be subsequently resolved (e.g. the acquired firm may control assets of cultural heritage which when controlled by a foreign company may invite unwanted criticism).

1.1.4.3.Joint Ventures

The meaning of the term has already been provided in page 4. A type of ownership sharing very popular among international organizational companies is the joint venture, in which a company is owned by more

than one organization. Although a joint venture usually is formed for the achievement of a limited objective, it may continue to operate indefinitely as the objective is redefined. Joint ventures are sometimes 50/50 companies, but often more than two organizations participate in the ownership. Further, one organization frequently controls more than 50 percent of the venture.

The type of legal organization may be a partnership, corporation, or some other form permitted in the country of operation. When more than two organizations participate, **the resultant joint venture is sometimes called a consortium.**

Almost every conceivable combination of partners may exist in a joint venture, including the following:

- ✓ Two companies from the same country joining together in a foreign market such as Exxon and Mobil in Russia.
- ✓ A foreign company joining with a local company, such as Sears Roebuck and Simpsons in Canada.
- ✓ Companies from two or more countries establishing a joint venture in a third country, such as that a Diamond Shamrock (U.S) and Sol Petroleo (Argentine) in Bolivia.
- ✓ A private company and a local government forming a joint venture (called mixed venture), such as that Philips (Dutch) with the Indonesian government.

Certain types of companies tolerate a joint ventures than others can't do . Companies with a higher tolerance include that are new at foreign operations and those with decentralized domestic decision making, and multi-product companies. Because these companies are accustomed to extending control downward in their organizations, it is easier for them to do the same thing internationally.

Many joint ventures have problems, primarily because the partners evolve different objectives for them. For instance, one partner may want to reinvest earnings for growth and the other may want to receive dividends. In addition, one partner may offer much closer management attention to the venture than the other does. If things go wrong, the more active partner blames the less active partner for its lack of attention, and the less active partners blames the more active one for making poor decisions. Therefore, the choice of a joint venture partner is crucial, particularly if a company is forced into shared-ownership arrangement because of governmental regulations. For this reason, many companies will develop joint ventures only after they have had long-term positive experiences with the other company through distributorship, licensing, or other contractual arrangements. Compatibility of corporate cultures also is important in cementing relationships.

The basic **advantages** of a joint venture are the following:

- ✓ The foreign company gets a local partner which has the necessary connections, is aware of the local habits, customs and particularities of the country and of course is sharing the cost of the endeavor and the financial risks associated with it.
- ✓ A joint venture can overcome tariff and non-tariff barriers that exist in many countries, which apply mainly in other forms of other investment schemes. Sometimes a joint venture is the only way to enter in a foreign market.
- ✓ In many cases there are substantial advantages which are associated with the establishment of joint ventures in foreign countries in the form of financial and other incentives.
- ✓ Also the possibility of forming a joint venture with a local partner diminishes substantially the risk of nationalization because any harm caused to the foreign partner will inevitably affect the local partner as well. This means also that this company may enjoy special privileges that other companies cannot enjoy.

The basic **disadvantages of a joint venture** are the following:

- ✓ The parent company does not have the absolute control of the management of the joint venture.
- ✓ The parent company will have to share the profits.

- ✓ Joint ventures have a reputation of a short life span. This is due mainly to the targets set, the formation of the corporate strategy and to the cultural differences of the partners.

1.1.4.4. Other alternatives

In addition to the above, some specialized entry modes for international business are: **Contract Manufacturing, Management Contract and Turnkey project.**

Contract Manufacturing

Contract manufacturing, means in essence, outsourcing most if not all of a company's manufacturing needs to other companies. By so doing, these firms reduce the amount of their financial and human resources devoted to the physical production of their products. With this method international companies can focus on the improvement of their competitive advantage and benefit at the same time of any advantages gained by producing in a specified country. It should be noted that this method means that the foreign company surrenders control of the production process, which can lead to quality problems or other unexpected surprises.

Management Contract

Management contract is an agreement whereby one firm provides managerial assistance, technical expertise, or specialized services to a second firm for some agreed-upon time in return for monetary compensation. For its services the first firm may receive either a flat fee or a percentage of sales. The contract may also contain performance bonuses based on sales, growth and so forth.

An example could be a large airline providing managerial expertise to small state-owned companies in developing countries.

Turnkey Project

A turnkey project is a contract under which a firm agrees to fully design, construct and equip a facility and then turn the project over to the purchaser when it is ready for operation. The project may have a fixed price, in which case the firm makes its profit by keeping its costs below the fixed price or the contract may provide for payment on a cost plus basis, which shifts the risk of cost overruns from the contractor to the purchaser. Such projects involve usually large and complex constructions such as the building of a nuclear plant, an airport, an oil refinery and so forth.

Turnkey projects may come especially handy when the foreign investor company does not want to mess up with local rules, regulations, labor issues and so forth.

A B.O.T agreement is a quite usual scheme. A company ***Builds, Operates and Transfers (B.O.T)*** ownership of a project after a set period of time. Through this approach, the contractor profits from operation and ownership of the project for some period of time but also bears any financial risks associated with the project during the period before the final transfer e.g. a company builds a bridge and installs tolls which hopefully will pay up for its initial investment for a set period of 20 years, for example after which the company hands over control of the bridge to the local authorities.

1.2. Parameters affecting a joint venture investment

The first step in forming a joint venture is the obvious: one must choose a partner to proceed in this endeavor. The choice of the best partner is not easy. However most studies on the matter stress the fact that a company, and the relationships between the two or more partners, is the asset that will make or break the

agreement. One can state many parameters that can be filled in order to find a partner. However most of these questions fall under the following categories: **(a) Compatibility, (b) Capability and (c) Commitment.**

1.2.1. Compatibility

The companies that are experienced in forming joint ventures have devised some methods to cope with the problem of locating a compatible partner.

The first, and a very common method, is to contact the current allies or associates, which form the existing range of business relationships of a company. This method has some notable advantages:

There is a history of how well the relationship has stood the test of time. This is the first and obvious advantage. It is understood that any company that has worked with other companies may have had problems and/or frictions. However if these issues have been resolved, then it can be said that a successful partnership may work.

Personal ties have already been established. It is often easier to strengthen a relationship with an already familiar company than to start with a new one.

There is no "acquaintance" period, meaning there are very few if any things to hide from each other. Any of the partners knows about the other partner's issues such as personnel, capabilities, operating mode and company culture.

The only disadvantage of such an approach is that of a company which does not look away from its immediate surrounding environment. By restricting one's scope to existing business relationships, one may not find the optimum partner for a given business venture. This will work vice versa as well. A prospective qualified partner may not approach a company, because the former has the reputation of forming business ventures only with its immediate associates, becoming therefore synonymous with only a handful of companies.

The compatibility between two or more partner-companies can be tested based on both **tangible and intangible factors.**

Tangible factors are: similarity in size and capabilities between the partners, existing alliance network, previous record of successful joint ventures, strategy, management, operational and organizational issues, manufacturing methods used (where applicable), marketing and distribution, financial status and practices, safety, health and environmental policies.

The Intangible factors include the interaction of the people involved, the sense of trust among them, the corporate culture of the parties involved, their shared interests, the competitive advantages each one gains (this will also refer to tangible gains mentioned above), the competitive advantages and the complementarities gained by both ventures.

1.2.2. Capability

The capabilities of the potential partners are the first things that will be considered for a joint venture.

This includes an examination of the strengths and weaknesses of the parties involved, the level of activity concerning the particular sector, the market strength, technology level, manufacturing capabilities, distribution network and position in the market.

A very common mistake is to underestimate or to overestimate one of these characteristics. Although this may be overlooked in the beginning, depending on its importance, it is bound to surface sooner or later. Therefore it is advisable to be as precise, as the situation allows from the very beginning. Also this will be

avoided if a thorough investigation takes place before the start of the venture, which will include a present and future capabilities scenario.

At this point it must be assessed if the potential partner(s) is ready, able and willing to proceed in a joint venture. Although this may initially seem like a tangible point nevertheless it is not so.

For example if a partner is agreeing to commit the capital to finance the joint venture and his financial condition dictates otherwise, then it is clear that he is neither ready nor able to support his obligations.

1.2.3.Commitment

Partners should be equally committed to the success of the venture. This is translated to an investment by both partners of the necessary time, energy and resources to make the venture succeed.

In order to assess the commitment of each partner two questions need to be answered:

1) Is the joint venture relevant to the core business or product line of the partner? If the proposed alliance is an activity which is not one of the main activities of one of the partners, then there is the possibility that this partner may not be willing to devote the time and resources necessary to make it work. It is also easier to withdraw from a project that presents little interest for this partner.

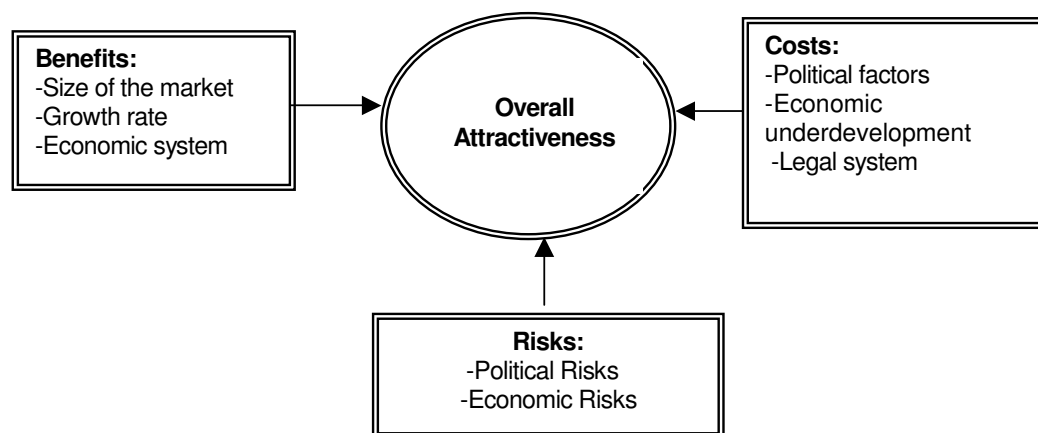
2) How difficult is for each of the partners to withdraw from the alliance? This is connected, in a way with the previous one but also goes one step further in stating that even a company that has all the positive characteristics may withdraw if this is relatively easy or neglect its commitments.

1.2.4.Risk analysis

Risk is defined as the uncertainty of attaining a standard or threshold and is a function of the probability and the consequence of failure. Risk Management (RM) is the process of identifying areas of risk and taking corrective action to reduce the risk to an acceptable level. It includes those activities required to assure efficient management of the acquisition process overall and of individual programs. In many respects, risk management epitomizes effective program management (a systematic reduction of risk in the evolution of a system acquisition).

Evaluating the overall attractiveness of a potential market and choosing a partner in a foreign country, is a process of examining three parameters, related in the following way.

Figure 2. Parameters used in choosing a foreign country



Risk Analysis is an important phase of the preparation stage for establishing a joint venture as it seeks to determine the factors of choosing a partner by examining them in terms of political and economic environment.

Political Risk: It's defined as a likelihood that political forces will cause drastic changes in a country's business environment that may adversely affect the profit and other goals of a particular business joint venture. So defined, political risk tends to be greater in countries with "low political freedom", or in countries experiencing social unrest and disorder, countries where the underlying nature of society makes the likelihood of social unrest high.

Among the criteria that characterize a country with *high political freedom* are: recent free and fair elections, a parliament with effective power, a significant opposition, and recent shifts in power through elections, while factors contributing to *low political freedom* include: military or foreign control, the denial of self-determination to major population groups, and a lack of decentralized political power.

Social unrest is defined as the intense likelihood of strikes demonstrations, terrorisms or violent conflict. Such phenomena are usually found in countries with several ethnic nationalities, or countries where competing ideologies are battling for political control, or in cases where mismanagement has created inflation and falling of living standards.

Economic Risk: has been defined as the likelihood that economic mismanagement will cause drastic changes in a country's business environment that may adversely affect the profit and other goals of a particular joint venture. Economic risk is very often bound to political risks in a relation of interdependence where economic mismanagement of a government leads to social unrest and as a consequence to political risk, or vice versa, where social unrest leads to economic risk, creating inflation. The following table shows how different types of political and economic risk may affect the operation of a firm.

Table 1. Type of risks

TYPES OF RISK	POSSIBLE IMRACT IN COMPANIES
Expropriation	Loss of future profits
Confiscation	Loss of assets Loss of future profits
Campaigns against foreign goods	Loss of sales Increased costs of public relations campaign to improve public image
Mandatory labor benefits legislations	Increased operating costs
Kidnappings, terrorist acts, threats, and other forms of violence	Disrupted production Increased security costs Increased managerial costs Lower productivity
Civil wars	Destruction of property Lost sales Disruption of production Increased security costs Lower productivity
Inflation	Higher operating costs
Repatriation	Inability to transfer funds freely
Currency devaluations	Reduced value of repatriated earnings
Increased taxation	Lower after-tax profits

Source: John D. Daniels & Lee H. Radebaugh., "International Business, Environment and Operations", 7th edition, 1996, page 25-32.

1.2.4.1. Political risk

Political Risk Assessment is a major issue for a company, in case of entering a new market of a foreign country. Experienced international businesses engage in political risk assessment, which is a systematic analysis of the political risks they face in foreign countries.

Laws and regulations passed by governments at any level can affect the viability of a company's operations in the host country.

Most **political risks can be divided into three categories:**

- **Ownership risk**, where the property of the firm is threatened through confiscation or expropriation.
- **Operating risk**, in which the ongoing operation of the firm and/or the safety of its employees are threatened through changes in laws, environmental standards, tax codes, terrorism, armed insurrection.
- **Transfer risk**, in which the government interferes with the firm's ability to shift funds into and out of the country.

Example: Minimum wage laws affect the price the firm must pay for labor, zoning regulations affect the way in which it can use its property, environmental protection laws affect the production technology it can use as well as the costs of disposing of waste material. Adverse changes in tax laws can slowly destroy firm's profitability.

1.2.4.2. Economic risk

Types of economic risk that a joint venture may incur in entering a new market are: exchange rate fluctuations, additional operational complexity and direct financial losses due to mis-assessment of market potential. In practice the biggest problem arising from economic mismanagement seems to be inflation. Inflation can be a serious problem for a firm entering a new country since the value of the cash flows it receives from its assets will fall as the country's currency depreciates on the foreign exchange market.

1.2.4.3. How to prevent risk

The extent of competition in today's new markets engages no guarantee of success when a company enters a new market. Joint ventures are used for reducing and controlling the risk. Sharing the risk, is the most direct way of eliminating the possibility of loss. For example: a company that independently undertakes a new venture of X size of investments stands to lose its entire investment if the venture fails. In case that it undertakes the same size project as a joint venture, with 50/50 split of the investment its greatest potential loss is equal to X/2. Sharing benefits and risks gives a feeling of equality and acts as a strong motivator for the potential partners.

Apart of sharing, there are systematic approaches of eliminating or assessing the risk. The following lines present some of the analysis a company should proceed into, in order to define the risk and avoid unexpected results. In any case risk should be quantified even in most difficult cases, (e.g. quantifying political risk. Political risk assessment has been proved many times, out of experience, as more of an art than a science).

A firm entering a new market should adjust the expected rate of risk which reflects the degree of risk of operating in the country. For example little if any risk adjustment is needed for investment in Greece because of its political stability, in contrast political instability of FYROM needs a larger risk adjustment for investment there.

1.2.4.3.1. Things that should be taken under consideration

Legal issues: Legal risks exist when a country's legal system fails to provide adequate safeguards for contract violations or protection of intellectual property rights. When legal safeguards are weak, firms are more likely to break contracts or steal intellectual property to serve their own interests. Legal risks might be defined as the likelihood that a trading partner will opportunistically break a contract or expropriate intellectual property rights. When legal risks in a country are high, an international business might hesitate to enter into a long-term contract or a joint venture agreement with a company in that country.

Culture differences: Differing cultural attitudes toward power orientation can lead to misunderstandings in business operations. Culture characteristics related to career progression, job mobility of employees, goal orientation, time orientation, or other factors such as the extent of social obligations, the level of quality of life, the degree of culture values similarities etc.

Ethical issues: A company should also define its strategy towards ethical issues like: if it has to adhere the same standards of product safety, work safety, environmental protection that is required in its home country. Another ethical issue is that of bribes. Should an international business pay bribes to government officials in order to gain market access to a foreign country? In many countries payoffs to government officials are part of life.

1.2.4.3.2. Adjusting risk

This method has to do with treating all risks as a single problem by increasing the discount rate applicable to foreign projects in countries where political and economic risks are perceived as high. In effect, the higher the discount rate, the higher the projected net cash flows must be for an investment to have a positive net present value.

However the truth is that if political or economic collapse were expected in the near future, the investment would not take place anyway. So for an investment being considered seriously, the political and economic risk being assessed is not of the immediate possibility type but, rather, risk that has some time distance in the future. Accordingly, it can be argued that rather than using a higher discount rate to evaluate such risky projects, which penalizes early cash flows too heavily- it is better to revise future cash flows from the projects downward to reflect the possibility of adverse political or economic changes sometime in the future. Rather than revising the discount rate upward to reflect higher risk, future cash flows several years out should be revised downward to reflect higher risk.

1.2.4.3.3. Alternatives scenarios analysis

Scenario planning is not just based on a hunch, but tries to build plausible views of different possible futures for the organization based in groupings of key environmental influences and drivers of change, which have been identified. The result is a limited number of logically consistent but different scenarios, which can be considered alongside each other. There are two main benefits of such exercise.

The first is that of examining strategic options against the scenarios, by posing questions such as "what should we do if..." or "what would be the effect of...?" The second benefit is that the implications of scenarios can be used to challenge the taken for granted assumptions about the environment in which the company operates.

The main steps in drawing up scenarios are as follows:

- Identify the assumptions or forces that are to be included. It is important that the number of assumptions is kept relatively low, since the complexity in drawing up scenarios rises dramatically, according to the number of assumptions included. This can be succeeded, by using forces which either had in the past the greater potential impact on company's operation or by focusing to factors, which have high potential impact or are uncertain.

- Scenarios can be built either from the factors, this is feasible when the number of factors is very low. If the number of factors being considered is large, it may not be feasible to built up different scenarios, then the tone of scenarios is set: (a) an optimistic future and (b) a pessimistic future. However the allocation of possibilities to factors should be avoided.

1.2.4.3.4. Financial ratio projections

The projection of how key financial ratios would change if a specific option were adopted can provide useful insight into risk. At the broadest level, an assessment of how the capital structure of the company would change is a good measure of risk. For example, options, which would require the extension of long- term loans, will increase the gearing of the company and increase its financial risk. The level of financial risk created by funding a proposed strategy from long- term loans, can be tested out, by: (a) examining the likelihood of the company reaching the break-even point, and (b) the consequences of falling short of the volume of business while interest on loans continues to be paid.

1.2.3.4.5. Sensitivity analysis

Sensitivity analysis is a useful technique for incorporating the assessment of risk during strategy evaluation. It is related to scenarios analysis and allows each of the important assumptions underlying a particular strategy to be questioned and changed. In particular it seeks to test how sensitive the predicted performance or outcome is to each of this assumption. Sensitivity analysis asks what would be the effects on performance (profitability) if something (a scenario) occurs.

1.2.3.4.6. Simulation modeling

Strategic simulation models attempt to encompass all the factors considered by the separate analyses into one quantitative simulation model of the company and the environment. It seeks to assess the overall degree of uncertainty in a particular option by mathematically combining the uncertainties in each of the elements of the option. One of the limitations on the use of strategic modeling is the need for large amounts of high quality data concerning the relationship between environmental factors and company performance.

1.2.3.4.7. Internal risks: managing the risks of competitive cooperation

Companies should never forget that their allies are often their competitors. Some of the following strategies are strongly recommended to minimize the danger of collaborating with competitors.

Foster mutual dependence: For many ventures involving technology, most companies ensure that know-how and technology exchanges are a two-way street. The greater the number of links between the partners and the greater the reciprocal needs for each others markets, capital and technology the less likely it becomes that one partner will turn around and stab the other in the back.

Keep close tabs on the venture to ensure the objectives and the goals of the partners do not diverge: Unless partners agree on a schedule for reviewing the progress and status of a venture, alliances risk derailment. Sufficient control and regular monitoring is needed.

Establish an alliance coordination unit: Management should encourage direct personal contacts between employees to strengthen the relationship and minimize problems in a specific project. Simultaneously, a central liaison group should monitor and control who works with the partner and what information is shared.

Ensure all employees understand the risks: The greatest role of alliance coordinators is to inform the employees of the risks of collaboration. It should be noted the contradiction between encouraging camaraderie among venture employees yet ensuring that too much friendliness does not result in leaks of valuable technology and know-how.

2. PLANNING FOR THE JOINT VENTURE

2.1.Strategic and operational planning

The operational and strategic direction of the joint venture begins to emerge as an important issue once the initial problems of establishing a joint venture have been overcome.

Today's joint ventures have evolved from the weak partner-strong partner scheme of the past. The emergence of joint ventures between two equally strong partners has forced executives to reassess the value of 50/50 (equal) partnerships, because this JV partnership has also its share of problems.

The positive parts of this kind of deal (50/50 equal partnership) are that both parties' interests are protected and whenever a problem arises partners have to act as equals and deal with the issue. It is also evident, that partners share equal responsibility towards the success of the endeavor. On the negative side, equal responsibility sometimes means an equal executive authority over managerial issues, which brings critical decisions to a standoff. As one experienced executive put it: "Companies are not run by committees. Someone has to take the final decision and bear its consequences whether good or bad".

There are two ways to overcome this obstacle.

- The first way is that companies may have 50-50 ownerships of the joint venture but have separated functional responsibilities between them, allowing individual partners to retain control over functions of strategic importance to them. An example could be that one partner controls Research and Development (R&D) activities while the dissemination of the technology outcomes is controlled by the other.
- The second way is that companies may retain the majority of the votes (e.g., 45% each one) with a third party (a trusted third entity) may hold the decisive vote (10%). This can resolve several issues, however it should not turn out that the majority parties spend their time convincing the third entity instead of running the joint venture.

2.1.1.Strategic planning

The long-term viability of a joint venture is dependant upon allowing the newly formed company to operate as an independent one.

There are three points of view for this issue.

- **The first one** is dictating that the joint venture should operate independently from the early beginning.
- **The second one** is saying that the venture should operate under the supervision, either strict or loose, of the founding companies.
- **The third point** of view suggests that the joint venture will start with latter relationship (supervision) and move after some time, depending on several factors, to the former relationship (autonomy).

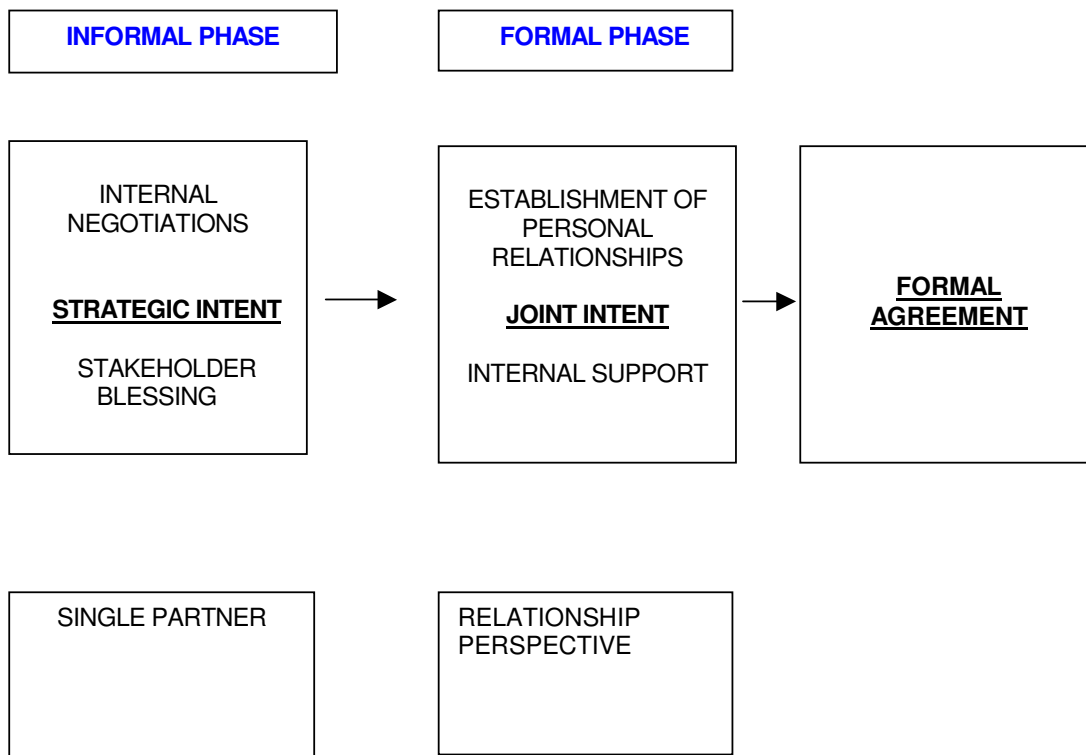
The level of autonomy of the newly created company and the type of control exerted by the partner companies which created it, will depend on how far the activities of the joint venture affect the core activities of the founding partners. In this case for example, if the joint venture operates in an area which does not interfere with the strategic interests of the partners, then in principle, it can be given greater autonomy than if the joint venture is responsible for selling its products in one of the partners' market area. The strategic orientation of the joint venture is an important basic consideration affecting the construction of the joint

venture system, from the development of a concrete business plan for the new entity, through the creation of interfaces and exchange relationships, to matters of human resource policy and co-operative culture.

The form that a joint venture takes, plays a large part in determining the type of problems managers will encounter. This means that answers should be given to the following points, without the list being exhaustive: the aims of the joint venture, allocation of resources, organizational structure, legal status of the joint venture, location of the headquarters, geographical expansion of the joint venture, recruitment of the necessary personnel for the joint venture, equity breakdown of the partners, distribution of earnings, laws, restrictions and common practices of capital/profit repatriation, currency and import regulations, inter-company agreements arrangement, protection and use of intellectual property, tax issues involved, losses deductible, membership at the board of directors (number, responsibilities, schedule of meetings and so forth), resolution of disputes (formal and informal), circumstances and methods that a partner can withdraw from the partnership, in case of withdrawal, specification of the terms and conditions under which one partner can sell his share to the other partners' market area.

The following diagram represents the framework of the joint venture formation.

Figure 3. Framework of joint venture agreement



2.1.2.Operational planning

The operational planning phase of the joint venture is the next stage, once the parameters of conceiving and early planning have been finished. At this point the newly found corporation is starting to materialize.

As far as the agreement of joint venture is concerned it should be noted that there are various ways to tackle the issue. Some partners find it convenient to do it at a very early stage, even during the preliminary discussions. At this case it is a wide structure agreement, which allows room for negotiation and offers partners a framework for discussion.

To cover such an issue, a **Memorandum of Understanding** is jointly signed by joint venture. This document is more of a psychological bond for potential partners to carry on further negotiations towards cementing a relationship. It roughly describes the boundaries of the partnership such as production and scale, investment size, investment share, location and whatever the partners have deemed as necessary.

Most joint ventures however reach the discussions up to the point of answering the strategic questions as well as the major management issues and at this point the partners, jointly will draw the agreement contract.

2.1.2.1. Negotiating the agreement

It has already been stated that most of the joint ventures of today are based on a partnership of equals (50/50 partnership). It is therefore of great importance to move forward with the negotiations within this framework.

There are **certain points that, if properly met, can greatly enhance the success of the negotiations:**

1. The negotiations move at a regulated pace and are carried out to develop mutual understanding and trust.
2. The negotiations focus on interests of parties.
3. The negotiations lead to strong convergence in the interests of both parties.
4. The two (or more parties) have a feeling that they are both going to win from the joint venture.
5. The negotiations are detailed and with the active participation of the relevant personnel (i.e., when technical matters are discussed, the appropriate personnel will be present).
6. The negotiations may need to take cultural differences into consideration and adjust accordingly. In this case an experienced translator or interpreter can assist in transmitting the right message on the other side and vice versa.
7. Every stage of the negotiation should be supported by evidence, data or a feasibility study and not plain optimism.

Also as far as the negotiating team is concerned **there are two methods of selecting the members of the team:** (a) either the negotiating members will actually join the joint venture or (b) their involvement will cease once the negotiations have been successfully finished. In the first case the members have an active participation and they will usually have a more decisive role than in the second case. On the other hand it is in the second method that members may be more impartial and objective in promoting negotiations. A third way could be to start with the impartial members and finalize the deal with the actual joint venture members.

Before the actual negotiations there are **certain points that the negotiators should keep in mind.**

1) They must have a clear focus of the strategy behind the joint venture: This means that the strategic needs that the joint venture will cover, have been decided. This also includes what each partner is ready to give and take from the soon-to-be company.

2) SWOT analysis of each of the partner: S.W.O.T stands for "Strength, Weaknesses, Opportunities, & Threats". This will reveal which are the bargaining points for each partner and will offer valuable information to the negotiator on what he can expect, demand and give to the other party.

3) Information disclosure: This is an important point for any joint venture. Apart from the obvious technological issues this may refer to vulnerable points of a company, contacts or any insider information. So negotiators should not reveal too fast what they know. Some methods of avoiding this problem is to have a frank discussion on what each partner expects to receive from this partnership. If a partner is willing to offer, with something else in exchange, what the other partner expects to get, then the negotiations can continue. Also a company that is interested in long-term alliances and has a history of such alliances with other companies is a good sign that is an honorable ally. Finally partners should provide only the information necessary and when it is needed, and not earlier.

4) Check from time to time if everything is correctly understood from both sides: This can be done by writing down what has been agreed so far in the language of each partner so as to avoid any misunderstandings. Although this may sound simple nevertheless, it may reveal some obvious misconceptions by the negotiating parties and save a lot of trouble for every one involved. It must not be assumed that partners are thinking on the same wavelength.

5) Commitments must be kept: This may initially sound more than obvious, however the practice has shown that it is easily forgotten. Many negotiating partners, in order to get the deal are willing to artificially inflate or present their capabilities better than they are risking exposure at a later stage of the negotiations or even worse when the joint venture is currently underway. Moral of the story is never to promise more it can be delivered or at least what can be found out.

6) Remain critical of the other partner(s): This point means that with each stage of the negotiations the partners should be still happy with the agreements made. Willingness and ability to work from all parties concerned will decide on the future or not of the negotiations.

7) Final point: Ability and willingness to walk away: When the following signs arise such as: one party should not go with the preconceived idea that an agreement must work, or when a lot of time and effort has been put in negotiations and become obvious that the joint venture has difficulties to work, or thoughts that disputes will be resolved in the future about the success of the joint venture, all these signs above mean that a party must be ready to stop negotiations from going further if he feels that he cannot, will not or is not interested anymore in working with the designated partners. Thus, the party must have the ability and willingness to walk away from the JV scheme before the actual negotiations should start in order to avoid the failure of the joint venture.

2.1.2.2. Structuring the agreement

The task of writing down the final agreement will be simplified if the negotiations have moved swiftly, removing any obstacles that might be presented along the way.

The agreement of co-operation can be written after the negotiations have been finished or simultaneously. Also it sometimes happens that one of the partners, who is more experienced in joint venture may bring along a draft agreement and start working on that.

An important note is that a lawyer, specialized in such matters, should be consulted before signing any agreement. One can never be too prepared, because any agreement may contain flaws or potential causes for future disputes that may have been overlooked.

In order to facilitate the structuring of the agreement, experience has shown that the following **points have been of substantial importance.**

- 1)** The agreement should be focused and directed towards the joint venture, stating clearly the **identity of the partners, its objectives, its scope, its activities, the relation between the partners, territorial activity of the joint venture**, definitions which may be a source of confusion, validity period of the agreement, and what will each partner contribute together with the responsibilities and obligations of each partner. Of course the list is not exhaustive and since any joint venture agreement should be judged on its own merits, other points may be included to make the agreement as specific as possible. The items identified are common among many companies. The joint venture partners should make certain to properly approve appropriate actions for the future company on an annual basis.
- 2)** In this context **the structure of the management team** should be identified from the early beginning. Items that fall under this category can include such issues as decisions that can be undertaken by the joint venture partners, which ones can be taken by the managers, selection of them, conflict resolution, language of communication and information exchange.

- 3) **Finance and tax issues** come afterwards. This issue deals initially with the type and size of capital invested, tax breaks or tax exemptions, availability of funds, liquidity and common financial management, meaning commonly accepted accounting practices, budgeting and financial reporting.
- 4) **Earnings** are a substantial part of a successful joint venture, because after all any company should bring profits if its existence is to continued. How the earnings will be distributed and the method of distribution, what percentage of the earnings will be reinvested and above all what do the partners consider as sufficient return for their investment should be determined. This last point is of grave importance because without the earnings target one cannot know if the joint venture is successful or not. It is needless to say that this target should be attainable and within the limitations and constraints dictated by the joint venture.
- 5) Each joint venture partner should consider a method **of evaluating its contribution**. This is quite important especially in cases where partners bring in similar tools and methods, which the other(s) will criticize to see if they have more or less in this effort. For example if two world known brands form a joint venture, they should both determine a price to be put on such issues as name and reputation of each individual partner.
- 6) **Clauses, which facilitate changes or alterations**, even in major issues, should also be incorporated in the agreement text. This does not include the "force major " clauses (war, mobilization, natural catastrophes, etc) but rather clauses that permit adjustments when phenomena like devaluations, strikes, or major raw material shortages occur; in general, problems which are strictly business related and do not belong to general social phenomena.
- 7) The **total time period** of the joint venture is strictly matter of the partners. However international experience has shown that a *five-year (5) period* is the absolute minimum to give a sense of permanence and a time period for the success or failure to be seen.
- 8) Once the agreement has been signed and sealed **the redraw of any of the partners** should be a very costly affair for him. This should be the case because if a break up is too difficult in cost or money, then the partners have a better chance of being forced to sit down and discuss all the issues that are disturbing them and find a solution. One way to avoid this before the agreement is *to make several scenarios* beforehand so as to locate the possible points of friction and eliminate them so that they will not be a problem in the future.
- 9) In case the joint venture breaks up despite of all the effort, then there must be conditions for continuity. This may include on-going financial support or otherwise and the necessary back up for the transition period to a new joint venture without the partner who left.

2.1.2.3. Management issues

With its inception the joint venture must establish some sort of steering mechanisms, which will be accepted by all partners. These mechanisms should communicate adequately with the partners. Therefore, proper interfaces between the joint venture and the partners should be established. These interfaces can run from top-level positions to the lower operational level depending on each venture.

Production and manufacturing

Many of the joint ventures that exist in the corporate world have been initiated by the interest of the partners in joint manufacturing, assembly or production. This fact, combined with the unwillingness to bear alone the costs and hassles of the production have led many to the road of joint ventures. In several cases, the two or more partners split production responsibilities along each company's area of expertise. Obviously this strategy enables the alliance to best exploit the complementary strengths of the partners, it is also the most expedient and cost effective way to launch a product.

In numerous occasions a license agreement of production will be used. License is the permission or approval, usually non-transferable, which is granted from one partner to another. According to the agreement, the licensor donates the licensee the permission to produce a range of or just one product according to his specifications.

According to various experts on such agreements, successful licensing depends largely on how a company structures, manages and executes the actual technology transfer. Any licensing agreement contains three key elements: *documentation, training and support*. The effort is to ensure the licensee's ability to effectively exploit the technology, to minimize the licensor's costs and to maximize the revenues.

In order for a **licensing agreement to succeed, certain elements have emerged as critical success factors**. These are the following:

- Language of documentation and technical terms should be agreed upon before.
- The description and quality of the technology documentation should be concise.
- Documents relating to training should be delivered when needed. If they arrive early they will be outdated or forgotten, if late, they will be of little use.
- Training is more preferable to take a top-down approach, so that every one, from senior management down to the line workers will be aware of the technology. It is obvious that the content of training should be more general in the former group and more specific in the latter group. Training must follow a pattern, and not to work on an ad-hoc basis or only when needed.
- Egos and cultural differences should be eliminated so that the transfer of knowledge and technology is free, without obstacles.
- Support should be in the form of an actual involvement of the licensor in the whole process. This involvement goes beyond the mere technology transfer and deals with active participation in the business plan, in the formulation and implementation of marketing strategies and in working closely with operations to ensure that quality standards are upheld. This support however should not go indefinitely. Any joint venture should be able, after a relative period of time, to stand up on its own two feet. Support in this case should be in the form of emergency assistance, and restricted to certain qualified personnel. Also they could be charged once the joint venture has commenced operations. Also at this point the partners should agree on the updates of the licensed technology. This is of particular importance, especially in fast moving industry like the information technology, where patents and licenses are introduced every day. When, how and under what regime updates on licenses will be given, has to be determined before the actual technology transfer

Marketing

This part of management is quite a delicate issue. This happens because the strengths as well as the market capabilities of each partner goes under the microscope. The relationship now is more intimate, since information on its market capabilities will be revealed, which may be sensitive in nature. This will include information on distribution agreements, competition information, profits margins, expenses or any other information that will strengthen the marketing capabilities of the partners.

At this point it should be noted that all claims must be thoroughly checked by the prospective partners. A rigorous evaluation of all the information provided can be proved a real life-saver in preventing future mishaps.

The evaluation should include all the basics such as partner's distribution capabilities, advertising strategies, client base, and so forth. Market research should include an extensive examination of the products' pricing

structure, present and future customer demand and servicing requirements. A point of consideration is how well the existing marketing capability can adapt to the needs of the joint venture.

From previous experience it should be noted that the clear definition of the geographical scope of the joint venture is of paramount importance for its success. The joint venture team must be aware beforehand in which geographical areas is going to act and under which conditions.

It is advisable not to go after the customer base of the partners but rather create new ones, unless of course the joint venture was formed with the sole purpose of providing services to the partners; but even at this case it is advisable to pursue other markets as well.

In the case that joint venture competes with its partners, a price war is the most likely outcome and therefore bitterness among partners will be created.

Corporate Governance

Corporate governance is the system by which business corporations are directed and controlled.

Corporate governance is only part of the larger economic context in which firms operate, which includes, for example, macroeconomic policies and the degree of competition in product and factor markets. The corporate governance framework also depends on the legal, regulatory, and institutional environment. In addition, factors such as business ethics and corporate awareness of the environmental and societal interests of the communities in which it operates can also have an impact on the reputation and the long-term success of a company.

The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as the executive board, managers, shareholders and other stakeholders, and dictates the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance.

Good corporate governance is an important step in building market confidence and encouraging more stable, long-term international investment flows. The business-corporation is an increasingly important engine for wealth creation worldwide, and how companies are run will influence welfare in society as a whole. In order to serve this wealth creating function, companies must operate within a framework that keeps them focused on their objectives and accountable for their actions. That is to say, they need to establish adequate and credible corporate governance arrangements. Many countries see better corporate governance practices as a way to improve economic dynamism and thus enhance overall economic performance. The importance of good corporate governance has also been highlighted by the recent turbulence in financial markets.

Principles of corporate government cover five basic aspects of corporate governance:

- 1.The rights of shareholders.
- 2.The equitable treatment of shareholders.
- 3.The role of stakeholders.
- 4.Disclosure and transparency.
- 5.The responsibilities of the board.

Not all corporate governance arrangements fit all companies all times. The needs of individual firms will always differ because of company specific circumstances and developments over time. The principles

provide an international benchmark that accommodates different national models and facilitates the development of best practices by the private sector. Individual companies (and countries) can draw on the principles to develop more detailed corporate governance practices that meet their particular circumstances.

As most successful companies already do, the principles recognize that the competitiveness and ultimate success of a corporation is the result of a teamwork that embodies contributions from a range of different resource providers, including employees. From this perspective, a separate section of the principles is dedicated to the role of stakeholders in corporate governance. The principles encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises. The principles also state that corporations are expected to respond positively to environmental and social standards and the expectations of the communities in which they operate. These stakeholder concerns, together with the importance of business ethics, are also addressed in the preamble of the principles, in the section on disclosure requirements, and as a specific responsibility of the board of directors.

In addition environmental and ethical concerns are addressed in the principles as being relevant to a company's decision-making.

Governments play an important and distinct role in setting the proper legal and regulatory framework for corporate governance. The ability of companies to develop good corporate governance practices is affected by a range of legal and regulatory provisions in such areas as company law, securities regulation, disclosure and accounting standards.

The corporate governance business model is gaining momentum in the structure of companies worldwide and in Greece as well. International practice has shown that the companies are increasingly turning to the proper staffing of their boards of directors with the aim of managing such issues as employment, social responsibility of the company, transparency, business time frame and profitability.

In the past few years, a clear orientation of the companies towards their shareholders, has been observed in Europe. This is a clear indication of the fact that most people are shifting from saving up to investment. The renewal of the corporate governance model and its most immediate orientation towards the shareholders makes it more attractive to investors. According to a relevant research, investors are willing of paying up to 25% more for shares of a company that applies proper corporate governance. At the same time the cost for capital is diminished and the company resources are more efficiently used, thus the company turns out to be more competitive.

This model is of particular importance for joint ventures since the excellent relationship with the partners is a prime ingredient for success. Partners therefore are encouraged to use such a model with the characteristics mentioned above to ensure the success of the joint venture.

It should not go unobserved that the corporate governance will make the joint venture more workable and successful both for the partners and for itself.

Human Resources

Success in joint ventures depends largely on the character and leadership qualities of the executives charged with running the company.

In order to choose the necessary personnel, and not only the **Chief Executive Officer (CEO)**, partners must follow the same plan and move towards the same direction. The CEO has the obligation to weight all the partners' needs and interests and move accordingly in order for the joint venture to succeed.

However, here lies a much-too-often point of conflict. If the CEO or the major proportion of the management team comes from one partner, then the unspoken rule is that the interests of this partner company come before the interests of the joint venture. It is for this reason that many joint ventures revert to hiring outsiders that will have no allegiance to the partners and will view the joint venture as their prime concern.

Some of the attributes of a successful joint venture CEO have emerged over the years. These include among others traits like independence, self-reliance, ability to work well without the daily guidance of the partners, adaptability, and sociability.

Last but not least the job of the CEO is a full time job and not a three-month interim between assignments and it should be treated like that as well.

As far as the rest of the team is concerned it is critical to find people who will manage the joint venture successfully over time. This goes beyond finding team members who will manage technology, but rather it demands individuals who understand the company and the culture in which the alliance will operate. A crucial goal of the alliance manager is to secure trust, respect and influence within the partners.

A clear indication of the importance associated with a joint venture is which kind of people the partner companies assign to the joint venture. Executives with upward mobility, talented and suited to the venture's needs are a sure sign of interest in the fate of the company.

Finally adequate communication links should exist between the partners and the joint venture. Effective and continuous communications is a very important ingredient of any type of venture. Developing a solid communications system and network helps build trust. *After all any alliance is meaningless unless the partners can build mutual trust.*

Below the chief executive officer there are many positions to fill: General manager; marketing manager; operations manager; financial manager; company secretary, company treasurer, engineering manager; and product development manager.

One executive may have more than one role. All of those positions need not be filled at once. However, the thinking for the choice is the same:

- | What positions are important?
- | What skill sets should a person in that position possess?
- | What is the full job description of that person?
- | Who does that person report to?

These are all key issues. They should be addressed by all partners even if the joint venture starts with just a few employees.

Conflicting expectations concerning staffing and human resource issues can result in serious misunderstandings later on. Misunderstandings have the potential for creating problems as well. At the very least, they deflect critical management time and resources from more productive pursuits.

With a joint venture forward planning is also necessary. In order to do it, the number of staff that will be needed and the functions they will perform should be considered. Job descriptions and an organization chart showing who reports to whom should exist.

Also power to hire or dismiss personnel resides with the chief executive officer who reports to the board of directors. In small joint ventures, the consent of each partner may be required.

3. GENERAL LEGISLATIVE FRAMEWORK

3.1. European Union legislative framework

In light of the fact that two of the four countries examined in this guide are in the pre-accession stage to enter the European Union, the joint venture and the licensing regulations of the EU will be briefly outlined in this section.

3.1.1. Merger regulation

The European Community Merger Regulation (ECMR) (Council Regulation 4064/89 1) originally came into force on 21 September 1990. The ECMR was amended by Council Regulation 1310/97 2, which came into force on 1 March 1998.

The Commission has published a guidance notice (Commission Notice 98/C 66/03 OJ C66 2.3.1998 p1) outlining what this regulation means in practice. Within the ECMR, certain business concentrations as they are called, fall within its jurisdiction, but with the added characteristic of having a community dimension. A concentration may be a merger, an acquisition or full-function joint venture, i.e. a joint venture that functions as an independent business. Whether or not a concentration has a Community dimension depends on the turnovers of the undertakings concerned. These are normally the acquiring and acquired businesses (but not the seller) or the merging parties or the parents of a joint venture (as well as the joint venture itself).

Relevant tests for a full-function joint venture include whether it has a management dedicated to its day-to-day operations, whether it has access to sufficient resources in order to conduct on a lasting basis its business activities and whether it is geared to play an active role in a market and perform the normal functions of a trading company in such a market.

A joint venture is a new company created by two or more other companies (parents) in order to pool all or part of their existing business. The parents' intentions are e.g. getting jointly into a new product or geographical market by sharing the risks and costs. A joint venture can also be an existing company that used to be under one parent company's sole control, getting into joint control by the old and a new parent company, which required ownership of it. There are different ways to create a joint venture but the key criteria, is joint control holding by parent companies.

The **creation of a joint venture can have the following disadvantages or benefits** for competition:

Disadvantages are: reinforce oligopolistic market structures, raise the barriers to market access for potential competitors, market sharing, market power strength.

Benefits are: promoting investments and developing new product or geographical markets, promoting innovation, transfer of technology, established countervailing market power, diversification, achieving economies of scale and cost reductions, restructuring or rationalisation of business.

Having such wide effects, a joint venture may change the competitive relationship between the parties more radically than other forms of co-operations. Also the relationship between the parties of a joint venture is based on a long co-operation time and has therefore a long-term effect on competition. With the respect to the benefits to the joint venture more fitting legal conditions and foreseen ability for their compatibility with the Common Market became necessary.

In this light there are the exemptions under Art. 81 III of the EC Treaty, on where to restrict. In some cases the scope of Art. 81 was not opened, so that the legal gap also should be filled. In the Merger Regulation parent companies can benefit from the "one-stop-shop-principle, which avoids parallel proceedings under national and international law. If the scope of the Merger Regulation is opened, only the Commission has

jurisdiction. The parent companies can also benefit from the fixed timetables stipulated in the Merger Regulation.

3.1.1.1. Scope of the merger regulation

The Merger Regulation governs only full function joint ventures. A not full function joint venture is a partial function joint venture, which is governed by national law or Art. 81. A joint venture is a full function joint venture when it performs on a lasting basis all the functions of an autonomous economic entity. That means a joint venture must have a long-term basis and must have an independent business from the parent companies. Criteria are for example own management, own resources, an access to market. But a support by parent companies during a start up period is not a criterion against full-function.

Also the fact that an otherwise full function joint venture makes use of the distribution network of one or more of its parent companies will not disqualify it as a full function as long as the parent companies are only acting as agents of the joint venture.

3.1.1.2. Compatibility with the EU legislation

The assessment of a joint venture under Merger Regulation demands answers at two points:

1. Does a joint venture create or strengthen a dominant position, with the result that effective competition would be significantly impeded in the Common Market or a substantial part of it?

2. Does the creation of a joint venture have the object or effect of co-ordinating a competitive behaviour between the parties?

3.1.1.3. Dominant position impeding competition

A Dominant Position, on the joint ventures relevant market, can be held by one parent company (single Dominant Position) or by more parent or not parent companies (collective Dominant Position). The single company or the collective group must have the ability to act in a considerable extent, independently of their competitors, their customers, and of consumers, the result of which would be, that effective competition would be significantly impeded in the Common Market. A collective Dominant Position presupposed oligopolistic market structure and structural or economical links between the members of the oligopoly, what creates a strong incentive to engage in anticompetitive parallel behavior. An important structural link between the undertaking can be the creation of a joint venture in the market, where the joint venture will be active. For this examination of a single or collective Dominant Position the relevant geographical and product market and the market shares of the parties must be determined.

The inspection whether or not a single or collective Dominant Position impedes significantly effective competition within the Common Market must take the following into account:

- A change of market structures, market shares, parties' and competitors' economical and financial power through the creation of the joint venture are a sign for effect on competition.
- Also the creation of market entry barriers, the availability of alternatives to suppliers and users are also important facts for the examination of an effect on competition.
- Finally supply and demand trends as well as the development of technical and economic progress and their effect on competition must be considered.

3.1.1.4. Risk of co-ordination

Finally the Commission has to take into account, whether the creation of the joint venture has the object or effect to co-ordinate the competitive behavior between undertakings that remain independent. The

Commission has to clear such effects in accordance with Art. 81 I-III. Such co-ordination may result from express agreements or from the fact, that competing parent companies, exercising joint management and joint control over the joint venture may automatically agree on their behavior outside the joint venture (spillover effect): e.g., if the parent companies fix the prices of the joint ventures' products it is possible, that they automatically make similar prices for their comparable products, on the same market, upstream or downstream, as well as closely related product and geographical market.

The way to examine possible co-ordination between the parties is another way of checking if competition rules are broken. The relevant market and the market shares of the joint venture and the parent companies are to be taken into account in order to evaluate the companies' strength and to find a significant overlapping of the parents companies business on the joint ventures or closely related market. The danger for express or automatic co-ordination in the overlapping market depends on the market shares of the parent companies in this area. If the market shares are less than 10% or 15% the overlapping is insignificant and bears no risk for co-ordinations in questions. But market shares up to 40% require a more critical evaluation of potential co-ordination. Market shares of more than 50% in the overlapping market are a sign that the co-ordination is limiting the competition, for a substantial part of the products and services in question. But the parent companies can propose appropriate remedies, which the Commission may except.

Furthermore it is to be examined whether or not a co-ordination improves or impedes competition. The joint venture can help the parents companies to extend their business to a new product or service market to which the Commission normally has a favorable attitude. The opposite attitude has the Commission to the extent of the parents companies to a new geographical market. But this examination depends on the particularities of each case. e.g. in the case for extending to new product markets, the experience shows that both parent companies usually have the necessary organizational, technical and financial resources to enter the new market independently. They decide to pool the risk. Often they have the intention to continue the new business independently after a certain time. These companies would become competitors if they would enter the new market independently. Consequently, creating a joint venture restricts competition. But the joint venture is compatible with the Common Market, if there is a compensatory benefit to balance the detriment for competition. A compensatory benefit can be a market share of the company being less than 10% or benefits, which was mentioned in the beginning.

3.1.2. License agreements

License agreements contain a multitude of terms, which maybe a source of problems if not properly addressed beforehand. Issues on who owns and under what terms the intellectual property rights, types of agreement have been the aim of a number of EU regulations. For example the technology transfer agreements are regulated by regulation No 240/96 while the joint research and development agreements are governed by Regulation 418/85, (amended with the regulation 151/93).

3.1.2.1. Definition of the term "intellectual property rights"

It includes patents, registered and unregistered designs, copyrights, trademarks and analogous rights such as plant breeders' rights. Industrial property rights confer upon their owner an exclusive to behave in a particular way. For example, the owner of a United Kingdom (U.K) patent has the right to prevent others from producing the patented goods or applying the patented process for 20 years and can bring an infringement action against anyone who attempts to do so without his permission. Patents may be granted where a product or process is technically innovative.

Horizontal agreements relating to industrial property rights

It is an agreement between competing firms. The success of a research and development project may depend upon competing firms entering into an agreement whereby they license each other to use technology since this will enable pieces of complementary information to be exploited efficiently. On the other hand, if all firms in an industry decide to their patents and agree not to grant licenses to third parties, at the same time fixing quotas and prices, they may earn supra-competitive profits and keep new entrants out

of the market. The burden of the competition authorities is to distinguish horizontal restrictions, which are harmful to the public interest from those which produce benefits and should be permitted. The Commission has not hesitated to take action against horizontal agreements which considers restrict competition. These agreements are governed by the council regulation No 2821/29.12.71 on the application of article 81 (3) of the EC Treaty.

Vertical agreements

A patentee may decide instead of producing the patented goods itself, to grant a license to another firm permitting it to do so. There are many reasons why this may happen - a patentee may lack the resources to produce in quantity or may wish to limit its own production to a particular geographical area and to encourage licensees to work other territories and many others. In a vertical agreement the parties are not actual or potential competitors. On the license the patentee may wish to impose various restrictions upon the licensee, for example, as to the quality of the goods that may be produced, tie-in clauses etc. These agreements are governed by Commission Regulation (EC) No 2790/22.12.1999, on the application of article 81 (3) of the EC Treaty.

3.1.2.2. Typical terms used in the licenses agreements

Royalties: A licensor will usually require the licensee to pay royalties in return for the right to produce and sell the patented goods.

Field-of-use clause: It is another common clause which, limits licensee's authority to produce goods to a particular purpose.

Tie-in clause: A licensor may require a licensee to purchase particular goods from it as a condition of the license. Such " tie-in" clause may be vital in quality control. "Tie-in" clauses are very often likely to be detrimental for competition and therefore be prohibited. A non-competition clause whereby the licensee is forbidden to compete or to use rival technology may encourage it to concentrate on producing the patented goods.

Territorial restrictions. the company should operate in specific area in order to avoid territorial restrictions.

Requirements to quality: (usually minimum quantity), marketing, labeling and so forth.

3.1.2.3. Types of license agreements

Exclusive manufacturing license: where the licensor gives the right only to a licensee to produce the goods in its territory itself and no one else.

Exclusive selling rights: the licensee could prevent the one who manufactured the goods outside its territory from selling them in it.

Open exclusive license: the licensor is prevented only from granting other licenses from exploiting the technology itself in the territory granted to the licensee leaving parallel importers and other licensees free to sell into the exclusive territory.

Closed exclusive license: - the licensor prohibits other licensees or traders from importing the products into the licensee's territory. The licensee is granted the right to bring an infringement action to prevent importation into its territory.

3.1.2.4. Industrial property rights and license agreements

Patents: they may be granted where a product or a process is technically innovative. Two issues should be discussed:

(a) whether the patent license is caught by Art.81(1) at all (it is also subject to limitation under the free movement of goods principle Art.28 and Art.82) and second

(b) whether it may qualify for individual or block exemption.

Utility models: it aims at protecting inventions that may meet lower standards of inventiveness than for a patent. Utility models have a narrower scope of protection than patents and for a more limited period.

Designs and models: New designs and models that are duly registered enjoy protection against unauthorized copying or imitation for a limited period.

Copyrights: a copyright confers rights similar to an industrial property right on the creator of an individual artistic or creative work of literature, music, science or applied art. A copyright prohibits unauthorized copying or other acts that compromise the integrity of the work.

Trademark: a trademark may consist - according to Art.4 of Council Regulation 40/94 - of any signs capable of being represented graphically, particularly words, including personal names, designs, letters, numerals, the shape of goods or their packaging, provided that such signs are capable of distinguishing the goods or services of one undertaking from those of other undertakings.

Know-how: It is a secret technical or commercial knowledge that provides a competitive advantage to the user. Know - how does not grant any exclusive rights but its confidential character is protected.

PART B. COUNTRY ANALYSIS OF PARTICIPATING COUNTRIES BULGARIA & FYROM

4. COUNTRY ANALYSIS OF BULGARIA

4.1. Country profile

4.1.1. Location, Climate, Demographics

Bulgaria is situated in the South Eastern part of the Balkan Peninsula and has a territory of 110,9 thousand sq. km., bordering Greece and Turkey to the South, FYROM and Federal Republic of Yugoslavia (FRY) to the West. The River Danube separates it from Romania to the North. Its natural eastern border is the Black Sea. Its climate is Continental-Mediterranean.

Bulgaria is situated in the center of the Balkan region, which is undergoing dynamic transition. Within 500 km of its capital Sofia (1.3 million people) a population of over 60 million is concentrated throughout 10 countries, most of which have only recently embarked on their way to a market economy. A network of international motorways crosses the country, making vital connections to Western Europe, Russia, Minor Asia, to the Adriatic, the Aegean and the Black Sea. Both sea and river transport (the Black Sea and the Danube River) offer communications and transportation to and from the region.

Bulgaria is a small nation of 8.2 million population (in 1999) mostly ethnic Bulgarians and has aspirations to join the European Union and NATO over the next several years.

Table 2. Bulgaria: Country Profile

OFFICIAL TITLE	Republic of Bulgaria	
LOCATION	South-Eastern Europe, bordering the Black Sea, Romania, FRY, FYROM, Greece and Turkey.	
FORM OF GOVERNMENT	Parliamentary Republic, One Chamber - 240 seats, elections every four years.	
CAPITAL CITY	Sofia	
OFFICIAL LANGUAGE	Bulgarian	
RELIGION	Orthodox Christian, Moslem, Jewish	
CURRENCY	Bulgarian Lev (BGN)	
EXCHANGE RATE	BGN 1 per DEM 1	
ETHNIC GROUPS	Bulgarian 85.3%, Turks 8.5%, Others 6.2%	
SURFACE AREA (sq. km)	110,9 thousand sq. km	
POPULATION, TOTAL	8.283.000	(1999)
POPULATION DENSITY (people per sq. km)	74.2	(1999)
POPULATION GROWTH (annual %)	-0.6	(1999)
LIFE EXPECTANCY AT BIRTH, total (years)	71.1	(1999)
FERTILITY RATE, total (births per woman)	1.1	(1999)
MORTALITY RATE, INFANT (per 1,000 live births)	14.3	(1999)
URBAN POPULATION (% of total)	69.3	(1999)
TIME	GMT+2	
COUNTRY TELEPHONE CODE	359 (Bulgaria), 2 (Sofia)	
CLIMATE	Moderate continental with four seasons.	
AIR ACCESS	Five international airports. Over 60 regular international flights.	
PUBLIC HOLIDAYS	1 January, 3 March, 1 May, Easter Day, 24 May, 6 September, 22 September, Christmas Day	

Source: The World Bank Group, *Regions and Countries, Bulgaria*. (<http://lnwed18.worldbank.org>)

4.1.2. History

The history of Bulgaria goes back more than 3.000 years. A succession of various civilizations, Thracian, Roman, and Byzantine, the Bulgarian state has existed for 13 centuries now on the Balkan Peninsula, which has long been a meeting place and a melting-pot of tribes and nations.

The *Bulgarian state was founded* in 681 AD, when Slavs and Proto-Bulgarians were brought together under the scepter of the khan. The conversion of the Bulgarians to Christianity in 865 AD joined Bulgaria to the Christian civilization. The invention of the Cyrillic script in the latter half of the ninth century, during an age when previously only Latin and Greek had been used to write, gave a powerful impetus to the country's cultural development.

The War of Liberation (the Russian-Turkish War) regained Bulgaria's freedom in 1878. In 1879 the Constituent Assembly adopted the first constitution of Bulgaria, which was one of the most democratic constitutions of the day. The first decades of the 20th century were years of economic effort and prosperity. Bulgarian goods and Bulgarian currency, the 'Golden Lev', acquired a high value on the European markets. Trade relations with Austria, Germany, France and Great Britain strengthened. The Communist end of Todor Zhivkov's regime in 1989 falls into the pattern of changes in Eastern Europe. Bulgaria took the road of a new democratic development, towards a free market economy.

4.1.3. Government

Bulgaria is a **Parliamentary Republic** and conforms with the Constitution of the Republic passed by the **Grand National Assembly in July 1991**. The Constitution of the Republic of Bulgaria is the supreme law of the country and no other law may contravene it. All international treaties, which are ratified pursuant to the constitutional procedure, are considered part of the domestic legislation.

The National Assembly is a one-chamber parliament. It consists of **240 Members of Parliament** who are directly elected every four years. The National Assembly is a permanent acting body, directed by a board of Chairmen including a Chairman of the National Assembly.

The head of the state is the President, who embodies the unity of the nation and represents the Republic of Bulgaria in its international relations.

The Council of Ministers is the executive state body and directs the domestic and foreign policy of the country. The government manages the implementation of the state budget, organizes the management of state property and approves or rescinds certain categories of international treaties pointed out in the Constitution.

Under the democratic process, there has been a smooth transfer of power, strengthening of state institutions and a consensus amongst all political parties towards promoting the market economy and respecting human rights.

Administrative Territorial Division

The territory of the Republic of Bulgaria is divided into **278 municipalities and 28 regions**. Municipalities are legal entities and have the right of ownership and independent municipal budgets. The municipal council is the local government authority, which determines the policies for development of the municipality.

The regions are administrative-territorial units, which implement the regional policy of the central government. The regions' management is carried out by a regional governor and regional administration at the cost of the state budget. Regional governors are appointed by the Council of Ministers.

4.1.3.1. Political environment-synopsis of political system in Bulgaria

Following the removal of long - time communist leader Todor Zhivkov in 1989, Bulgaria has been a Parliamentary Republic ruled by a democratically elected government. A new Constitution was enacted in 1991 which lays out the basis of Bulgaria's legal system. The Constitution allows for the freedom of association and the formation of political parties.

The Constitution provides for the separation of powers among the executive judicial, and legislative branches, and a system of checks-and-balances. The president is empowered to conclude international treaties and to schedule parliamentary (or National Assembly) elections. The president is also the commander (in-chief) of the armed forces. The National Assembly is a unicameral legislative body that consists of 240 members who are elected for a term of four years.

Petar Stoyanov of the Union of Democratic Forces (UDF) won a decisive victory in November 1996 presentation election. He assumed the presidency in January 1997 for five – year term.

Failure to follow through on reform measures through most of the 1990's led to the rapid downward spin of the economy,, high seriously affecting the living standards of all Bulgarians. Between 1989 and 1997 there were eight (8) governments in Bulgaria. By leaving local groups without management ability and priority in the privatization process and access to questionable loans, this cronyism spread weakness throughout the economy, causing the banking system nearly collapse in May 1996. The Bulgaria Socialist Party's slow progress in implementing reforms and mishandling of the economy led to a host of financial, social, and economic problems which reached crisis level in late 1996 to early 1997. Meanwhile, the UDF developed a new sense of unity and purpose by promoting a consensus, pro-reform, pro-West agenda as recommended by the International financial institutions.

In February 1997, after several weeks of escalating public protests and followed street demonstrations in Sofia, seen throughout the world on television in January 1997, against several years of disastrous rule, the Communist-successor Bulgarian Socialist Party (BSP) agreed to step down. Later that month President Stoyanov dissolved the National Assembly (Parliament) and appointed a UDF-led caretaker government to replace the unpopular Socialist government.

The caretaker cabinet moved quickly to stabilize the economy in March 1997 by concluding a \$510 million standby arrangement with the International Monetary fund (IMF) to help pull the country out of crisis. In April 1997, a reform-minded coalition headed by the center-right United Democratic Forces and which includes the UDF, the People's Union, the Bulgarian social Democratic Party, and a number of smaller parties, won an absolute majority in the per-term general parliamentary elections. The Union of Democratic forces (UDF) Chairman Ivan Kostov, was appointed Prime Minister by the National Assembly.

The key priorities of the UDF-led coalition government are:

- ✓ Economic Stabilization.
- ✓ Crime Control.
- ✓ Euro-Atlantic Cooperation.

On foreign policy matters the government has clearly stated Bulgaria's desire to seek fully NATO and EU membership. The next Parliament elections will be held in the year 2001.

4.1.3.2. Major political issues affecting business climate

The ruling Union of Democratic Forces (UDF) has enjoyed a stable parliamentary majority and has followed a mandate of leading Bulgaria out of the 1996-1997 economic crisis, although reforms have not been

implemented as fast as have hoped. And although the Currency Board has been highly successful in stabilizing the economy, **sustainable growth has yet to be achieved.**

Organized crime and corruption are a concern of both the government and ordinary citizens. Prime minister Ivan Kostov has declared that this a priority issue. The National Assembly has passed laws to amend the Penal Code and the Criminal Procedures Code. Violent crime against persons is extremely low but property crime-car theft, pick-pocketing, and burglaries are still widespread although on the decrease. Among some state-owned companies, assets have been siphoned off by unscrupulous managers in league with private businesspeople, a practice which the current government has attempted to curd.

The government actively pursues membership in Western institutions, including NATO and the European Union (EU). The UDF has declared its intention to maintain close contracts and active dialogue with NATO and the EU on the relevant political, financial, military and other issues related to future full membership. In many ways the Bulgarian Government has attempted to cooperate as though it were already a fully NATO member, as witnessed during the Kosovo crisis. The government hopes that active engagement to fulfill the membership criteria will encourage foreign investment and promote greater confidence in Bulgaria's political and economic institutions.

4.1.4.Currency and Exchange controls

During 1996-1997 Bulgaria experienced the worse economic crisis resulting in massive takeout of deposits, the crash of the banking system and the devaluation of its currency. The Bulgaria lev devaluated by 624% in relation to USD, in the same period. To overcome the economic crisis the price of 1.000 lev were set equal to 1 DM in July 1997.Later, it was decided to drop the three zeros and therefore create a new currency whose exchange rate was 1 Lev=1 DM.

The new Law on the Bulgarian National Bank (BNB) voted by the Parliament in June 1997, and the new Law on Banks adopted in July 1997, introduced a currency board in the country effective as of July 1,1997. After the introduction of a currency board, all constraints on trading with hard currency within the country were removed. Local banks can sell hard currency to physical and legal entities without any limitations. The local currency is internally convertible.

The currency unit in Bulgaria is the Bulgarian Lev. Before July 5,1999 it was denoted as BGL. Since the date mentioned, the Bulgarian Lev has been denominated in a ratio BGL 1,000 to BGN 1. At present the BGN is pegged to the DEM at the rate of BGN 1 per DEM 1. Central exchange rates are quoted daily by the BNB for statistical and accounting purposes only. The Bulgarian National Bank (BNB) denominations are: Notes BGN 1, BGN 2, BGN 5, BGN 10, BGN 20, and BGN 50, Coins BGN 0.01, BGN 0.02, BGN 0.05, BGN 0.1, BGN 0.2, BGN 0.5. The Lev denomination has facilitated payments, accounting and exchange operations.

Every local or foreign person may own an unlimited number of accounts in any currency, in any bank in Bulgaria. There are no restrictions on the repatriation of earnings, capital, royalties or interest with regard to the foreign investments and repatriation payments can be made freely.

The foreign exchange regime is based on the principle of freedom of concluding transactions, actions and payments. Transfers are governed by the Foreign Currency Act (effective as of 1 January 2000), the regulation on export and import of Bulgarian Leva and foreign currency in cash, precious metals and stones (1999), the regulation on trans-border transfers and payments (1999), and the regulation on registration by the Bulgarian National Bank (BNB) of transactions between residents and non-residents (1999).

Bulgarian citizens as well as foreigners may take Bulgarian Leva and foreign currency of up to BGN 20,000 or its foreign exchange equivalent out of the country without documentation. However, the export of Leva and foreign currency between BGN 5,001 and BGN 20,000 or its foreign exchange equivalent should be declared at the customs. Transfers above BGN 20,000 must have a prior approval of the BNB. Foreigners are permitted to export as much currency over the foreign currency equivalent of BGN 20,000 as they have imported into Bulgaria without prior approval.

Payments abroad made by businesses (or self-employed business people) can be executed only through bank transfers. Transfers over BGN 20,000 for current international payments (imports of goods and services, transportation, interest and principal payments, insurance, training, medical treatment and other purposes defined by the Bulgarian regulations) must be supported by documentation showing the need and purpose of such payments.

4.1.5. Infrastructure

4.1.5.1. Telecommunications

According to the U.S Department of State, (Country Commercial Guide of Bulgaria-published in 2001), Bulgaria has the highest penetration of telephone service in Eastern Europe, with 39.34 telephones per 100 persons, Bulgaria's telecommunications network is owned by the Bulgarian Telecommunications Company (BTC), which in turn is regulated by the Committee on Posts & telecommunications. Over 95% of Bulgaria's telephone subscribers can make automatic domestic long distance calls. As of January 1, 2000 BTC had a total of 3.254.742 telephone subscriber lines (2.394.118 residential subscriber lines and 860.624 business subscriber lines while only 30% of the business subscribers have digital lines). In 1998 BTC completed the four-year Digital Overlay Network (DON) Project, connecting Bulgaria's major cities with 17 digital exchanges, 2 satellite ground stations, 2.000 km of fiber -optic lines and a 2.000 km digital microwave network. The World Bank, the European Bank for Reconstruction and Development (EBRD) and the European Investment Bank (EIB) provided financing for the \$300 million US project.

BTC's main objective in its telecommunications network development is its technological upgrade through new digital switching and transmission infrastructure.

The BTC's priorities are:

- ✓ Building up the digital transit network continuation of digitalization, speeding up of the implementation of modern telecommunications and information services including ISDN, accelerating of the subscriber access network including broadband.
- ✓ Implementation of an access network (nX64 kbit/s) for business services including Internet.
- ✓ Participation in Building a new submarine fiber-optic cable system in the Black Sea (BSFOCS project).
- ✓ Building of a Fiber-optic long haul line from Sofia to the Greek boarder using SDH technology and STM-16 system etc.

Bulgaria has an analog cellular telephone network (450 MHz) operated by Radio Telecommunications (Modifon), **a joint venture between Cable & Wireless (49%) BTC (39%) and Radio Electronic System (12%)**. Bulgaria has one digital cellular telephone network operated by the Bulgarian company Mobitel which uses the Pan-European digital GSM standard (900 MHZ). Radio TELECOM/Modifon operates one of two national paging systems. The second system is operated by Link Communication Systems of the United States using Motorola technology.

The \$600 million US privatization of 60% of BTC and 40% of GSM, under the cash privatization program has been the largest privatization in Bulgaria. In July 2001, the only bidder, a consortium of two telecommunications firms, **Hellenic Telecommunications Organizations (OTE)**, and the Dutch telephone company KPN, agreed to purchase and operate BTC and also obtained Bulgaria's second GSM license. The consortium will invest \$150 million in BTC's telecommunications infrastructure and \$200 million for the development of the cellular telephone network over the next three years.

Packet-switching network and the value-added services (e-mail and fax by e-mail) are provided in Bulgaria mainly by Global One, **a joint venture between Sprint, Deutsche Telecom and France Telecom**. Private

networks are also widely used by private companies in the country. Global One uses X.25 networks for data transmission, as well as frame relay. An X.25 network is also used by Bulgarian Banks and local companies, while frame relay is mainly used by the big multinational companies like Glaxo-Wellcome, Coca Cola, and DHL.

To facilitate the BTC privatization, and to improve the regulatory environment for telecommunications, the Committee on posts and Telecommunications drafted a new Telecommunications Law to replace the old communist-era 1975 law. The new law went into effect on January 1, 1999.

4.1.5.2. Road transportation network

The Ministry of Transport oversees the transport sector as a whole. The road network is administrative by the General Road Administration (GRA) which falls under the Ministry of regional Development and Public Works portfolio. There are 37.000 km of roads in Bulgaria, although only 250 km is four-lane highway –and most of that is the 160 km between Sofia and Plovdiv.

Roads in Bulgaria are not to U.S standards. Streets in Sofia are frequently old cobblestone, and potholes are common in main and side streets. The U.S Embassy in Sofia recommends against driving Bulgaria's roads at night.

Bulgaria currently has two border crossing with Turkey. Given steadily improving relations between the two countries, the government of Bulgarian has requested the reopening of the third crossing which is likely to be favorably considered by Turkey. Three new border crossing will also be opened with Greece west of the current crossing at Kulata. Bulgaria, Turkey and Greece are working to improve the border crossing conditions and to alleviate bottlenecks through the Southern European Cooperation Initiative (SECI).

Bulgaria has many high way projects underway, including portions of the Trans-European Motorway (TEM). These include routes connecting Budapest with Athens via Vidin and Sofia, and with Istanbul via eastern Bulgaria. The EBRD, EIB, the European Union's PHARE program, and the Bulgarian Government's budget are the main sources for financing improvements in Bulgaria's road network.

4.1.5.3. Railways

The Bulgarian Railway Company (BDZ) oversees Bulgaria's railway system. The infrastructure consists of 4.300 km of track. An estimated 61% is electrified (25 Kv, 50 Hz).

Failure to perform the routine maintenance combined with the inability to purchase new equipment has resulted in a rapid and noticeable deterioration of the installed infrastructure. For example, an estimated 10.000 switches are worn. Nearly 85% of BDZ's maintenance equipment is obsolete. BDZ also requires new signaling equipment, aerial wires, communications system and radio equipment.

The government has a railway recon structuring project which will focus on the repair 414 km of main tracks, construction of an automated locomotive system, the procurement of new railcars and repair of existing stock, and the improvement of information and technical service. Bulgaria has received funds from the World Bank, the EBRD, and EU-PHARE totaling \$158 million with the government contributing an additional \$133 million.

Bulgaria also plans to complete a two-kilometer link with F.Y.R.O.M and to upgrade/electrify 80 kilometers of track between Sofia and the FYROM boarder. This linkage is integral to the formation of the European East-West Balkan Transport Corridor No.8, which is endorse by the governments of Bulgaria, FYROM, Albania, as well as the European Transport Ministries.

One of the main concerns of BDZ is commercialization of its activities through outsourcing and attracting private operators.

4.1.5.4. Ports

Bulgaria has two major ports on the Black Sea, Varna and Burgas. Both are the East-West transport corridor gateway of Bulgaria. Port facilities are generally adequate for bulk commodities, but lack facilities for special handling. Rehabilitation of both ports is planned.

Bulgaria has plans for a \$300 million expansion on Burgas Harbor, to include new ferry, and container terminals, and new facilities for general and bulk cargo. The Japan fund for reconstruction and Development provided a \$120 million 30 year 2.58% interest loan with a ten-year grace period to the Bulgarian Ministry of Transport for construction of new container terminal at Burgas. They also initiated a project to improve the breakwater facility in the port of Burgas. The U.S Trade and Development Agency (TDA) has also provided \$300.000 for intermodal cargo terminal feasibility study for the port of Burgas.

The EBRD has provided technical assistance to Varna for its master plan preparation assistance concerning its container and grain handling facilities. Ruse, a Danube port, is also commissioning a feasibility study on development of its port facilities.

Intermodal transportation is a new approach for Bulgaria. It provides freight forwarding and route alternatives. With joint efforts, Sea Land Services, Inc. USA, TDA and the Bulgarian Ministry of Transport recently completed two feasibility studies to establish a rail – truck intermodal terminal to handle ocean containers in Sofia and Burgas.

4.1.5.5. Air Transport

There are three international and seven domestic airports in Bulgaria. Sofia Airport is the largest in the country and handles most international traffic. All are owned by the central government (state-owned) but are required to operate independently on commercial principles.

□ **Sofia Airport**

Sofia Airport, with a terminal and other infrastructure dating from 1940, is in need of massive modernization. Plans call for a completely new passenger terminal, longer runway, and expanded taxiways. This \$200 million project is starting to come into focus as financing has become available and a detailed master plan has been prepared as part of the Sofia Regional Development Plan.

Current construction plans are for the new terminal to have a capacity of 2.5 million passengers/year (2.500 passengers /hour at peak hours) have a floor area of 26.000 square meters, and road access and parking lots covering 18.000 square meters.

In March 1998 the Government of Bulgaria approved a financial agreement with the European Investment Bank (EIB) for a loan of 123 million Euro for development planning of the expansion of Sofia airport, design and construction of a new passenger terminal building and extension of the existing runway. Technical assistance to be provided by the financial agreement includes completion of the airport master plan, planning and supervision of the project implementation, and operation and financial management of the airport. In August 1998, the Government of Bulgaria approved a \$40 million loan from Kuwait Development fund for additional financing for extension of the runway, construction of a new parallel runway and additional taxiways.

□ **Sofia Airport cargo Terminal Construction**

In September 1998 a consortium led by the large Bulgarian construction company Glavbolgarstroy and Siemens that won a tender under the previous Socialist government to build a new cargo terminal failed to obtain the necessary financing, and a \$200 million tender is expected to be announced by the ministry of Transport for a possible BOT (Build, Operate, Transfer) or concession. The new cargo terminal in intended to be able to handle 10.000-15.000 tons of air cargo annually.

❑ **Burgas Airport Modernization**

A pre-feasibility study for modernization of Burgas Airport has been performed concerning a new cargo terminal and modernization of the runway areas. The airport upgrade project will have an estimated value of \$60 million.

❑ **Varna Airport Modernization**

The Varna Airport master plan provides for extension of the runway, a new cargo terminal, modernization and extension of the international departure lounges, construction of an apron for cargo aircraft. This project will have an estimated value of \$100 million.

❑ **National Air Traffic Service Center Phase III**

In 1997 the Government of Bulgaria ratified a financial agreement with the European Investment Bank for a loan \$60 million Euro for construction of new air traffic control tower in Sofia under the authority of the Air traffic Services Authority. The National Air traffic Service Center will control all air traffic over Bulgarian air space, both civilian and military.

❑ **Balkan Bulgarian Airlines**

The national air carrier Balkan Bulgarian Airlines (BBA) flies to many destinations from Sofia with a fleet on ageing Russian planes and leased Boeings. The BBA wants to completely revamp its current fleet by purchasing modern western aircraft, but the Bulgarian government is preventing it by its agreement with the IMF from providing any sovereign guarantee to BBA, due to BBA's weak financial situation. A 75% share of BBA was purchased by a consortium of the Israeli Zeevi Group and Arkia Airlines. The new owners will invest \$100 million over the next five years and plan to repay \$30 million of Balkan accumulated debt.

4.1.5.6. Energy

Bulgaria's electrical generation capacity consists of nuclear, fossil fuel (thermal) and hydropower facilities. The nuclear power station at Kozloduy, on the Danube River, currently supplies 44.46% of Bulgaria's power. The older units 1 through 4, pose a safety concern due to lack of a containment system. The Bulgarian government is reluctant to decommission those Soviet design reactors, however, until alternative power sources are developed. An upgrade of the controls for the newer units 5 and 6 will be carried out under a \$77 million plus contract signed June 2, 1999 between the National Electric Company (NEK) and Westinghouse Electric Company of the United States with a credit guarantee from Eximbank. The \$77 million credit agreement was signed between CITIBANK and State Energy and Energy Resources Agency on July 10, 2000.

Among the larger coal-fired plants include Maritza East 1, which will be replaced by a new \$750 million plant to be built, owned and operated by a U.S.-owned AES, and Maritza East 3, which will be upgraded by U.S utility Energy for approximately \$425 million. It is expected that some of the electricity generated at Maritza East 3 will be exported to Turkey under a recent ten-year export agreement, to meet rising demand in Turkey.

The other major thermal power plant in Bulgaria is the 1260 MW in Varna. The challenge there is to upgrade and adapt the plant to use non-Ukrainian coal, which has proven harder to obtain in recent years. A number of foreign companies have expressed interests in this project.

The Trade and Development Agency (TDA) funded feasibility study for the Trans-Balkan Pipeline, to determine the potential for oil pipelines to carry Caspian Sea oil from Burgas to either the Greek port of Alexandroupolis on the Aegean sea or the Albanian port of Vlore on the Adriatic Sea may lead to future opportunities for construction and engineering firms as well as for suppliers of oil pipeline equipment to Bulgaria.

4.1.5.7. Water system

The waterworks system of Bulgaria's capital Sofia and the entire country is suffering massive leaks from the aged asbestos concrete water pipes that will require a complete overhaul of the water pipes. The first project will take place in Sofia and will be financed by the European Bank for Reconstruction and Development (EBRD).

Conservative estimates put the amount of investment needed just for the reconstruction and upgrading of the Sofia Water and Sewage Company at \$150 million. Current plans are for a three-stage competitive procedure for selection of a company that will be given 49% ownership of the Sofia Water and Sewage Company concession. Reconstruction and upgrading of the waterworks systems in other Bulgarian cities may follow. Currently four companies including **a joint venture between Bechtel and a British company**, are on the short list of bidders for the Sofia concession.

4.2. Bulgaria's Economic Environment

4.2.1. Background

In 1991, Bulgaria chose the road to a rapid and radical economic reform, beginning with the signing of Bulgaria's first program with the International Monetary Fund (IMF). The major objectives of this program were to curb inflation, slow down the decline of economy, achieve relative stability of the national currency and encourage private sector rapid annual growth. Within the first four years, the cornerstones of legal and institutional framework of the market economy were put in place. Macro-economic stabilization and structural reform were the key elements of economic reform, with monetary and income policies aiming at curbing inflationary trends.

Structural reform blockages, slow down of privatization and the loss of international market position for Bulgarian companies following the disintegration of the CMEA. The embargo on ex-Yugoslavia and debts of over \$ 2.5 billion US owed to Bulgaria by third world countries further worsened the state of the Bulgarian economy. The government supported loss-making public sector enterprises at the expense of draining out the banking sector and causing severe macro-economic dis-balances.

The severe depreciation of the national currency in early 1997 was the main factor for the high inflation (inflation in 1997 was 569.7%) during the whole year. The increasing net prices of fuel and electricity reached and surpassed international levels, which added to the high end-year inflation level.

In the first quarter of 1997, a new agreement with the IMF was reached, which marked the introduction of a currency board (July 1997) and a set of austere and radical new measures for reform. The German mark was properly chosen as reserve currency and the Bulgarian lev was pegged to it at a 1 BGL=1 DEM exchange rate, effectively the current free market rate. The introduction of the currency board did not immediately curb inflation, which failed to drop down to the levels in Germany. Compared to the macroeconomic indicators' value from the beginning of 1997, the currency board policy resulted in considerable decrease of inflation, increased credibility of the national currency and a reduced interest rate. Furthermore, all these factors, leading to a sharp decrease in the loans interest rate within the economy, subsequently reduced the government's debt interest payments, as well as the share of short-term debt, issued to finance the budget deficit.

4.2.2. Bulgaria - resumption of growth (1998-2000)

A few major events mark the 1998-2000 period. After the change of government in the beginning of 1997 and the introduction of the currency board agreement, Bulgaria registered unparalleled economic parameters in comparison to the preceding years. Macroeconomic stabilization was achieved, growth was resumed and inflation was curbed to single digit levels (inflation in 1999 was 6.2%). This has been made

possible by a combination of the strong political will of the government and the timely and adequate external support from the international financial institutions (EBRD, World Bank, IMF, etc.). Framework agreements liberalizing foreign trade between Bulgaria and the EU, EFTA (European Free Trade Agreement) and CEFTA (Central European Free Trade Agreement) countries, as well as with Turkey and FYROM expanded the market reach of domestic manufacturers to over 550 million consumers.

A broad international acknowledgement of the political and economic changes in Bulgaria was the invitation to start EU accession negotiations in December 1999 and their initiation in March 2000. The government has set up an ambitious agenda to complete them by the beginning of 2007.

The economy started to recover in **1998** as the year was marked by events with favorable impact on market reforms, e.g. the three-year International Monetary Fund (IMF) agreement and the accession to CEFTA. In 1998 practically all prices were liberalized, as only the household power consumption and industrial central heating utilities remained at their fixed levels. The centrally regulated prices in 1998 comprised 2.78% of GDP. Bulgaria achieved indubitable financial stabilization, 3.5% real GDP growth and 1% end-year inflation in 1998. The following table shows the key economic indicators of Bulgaria for the years 1995 and 1997 until 2000.

Table 3. Key Economic indicators of Bulgaria (1995, 1997-2000)

INDICATORS	1995	1997	1998	1999	2000
GDP at market prices (\$ US)	13.1 billion	10.0 billion	12.3 billion	12.4 billion	12.0 billion
GDP growth (annual %)	2.9	-6.9	3.5	2.4	5.5
GNI, Atlas Method (current \$US)	11.5 billion	9.7 billion	10.1 billion	11.4 billion	12.4 billion
GNI, per Capita Atlas Method (current \$ US)	1,370.0	1,170.0	1,230.0	1,390.0	1,520.0
Gross Capital Formation (% of GDP)	15.7	11	15	19	19
Current Revenue, excluding grants (% GDP)	35.5	32	34	35	N/A
Money and quasi money growth (annual %)	39.3	345	11.6	11.9	29
Overall budget deficit, including grants (% of GDP)	-5.2	2	2.8	1.5	N/A
Inflation (% of CPI)	32.9	569.7	1	6.2	11.4
Inflation, GDP deflator (% annual)	N/A	949	22	3	7
Structure of the Economy (% of GDP)					
-Agriculture, value added	12.7	24	18.7	15.1	14
-Industry, value added	31.0	25	25.6	23.4	24
-Services, value added	56.3	51	55.7	61.5	62
Exports of goods and Services	44.7	62	45.2	44.1	58.5
Imports of goods and Services	46.3	56	46.3	51.9	64.1
Private consumption	N/A	N/A	N/A	72.8	71.4
General Government Consumption	N/A	N/A	N/A	15.9	17.7

Source: World Development Indicator, World Bank Group, (<http://devdata.worldbank.org>)

Table 4. Key Economic Ratios of Bulgaria (1990, 1999-2000)

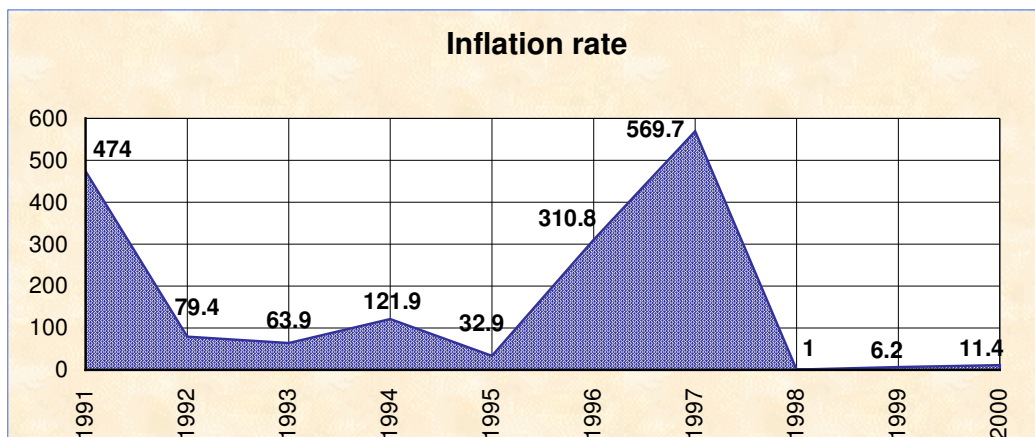
Key Economic Ratios	1990	1999	2000
GDP (\$ US billions)	20.7	12.4	12.0
Gross Domestic Investment /GDP	25.6	19.0	16.6
Exports of Goods and Services /GDP	33.1	44.1	58.5
Gross Domestic Savings /GDP	22.0	11.3	11.0
Gross National Savings / GDP	N/A	12.2	10.7
Current Account Balance /GDP	-5.9	-5.3	-5.9
Interest Payments /GDP	2.2	2.7	3.7
Total Debt / GDP	52.4	79.6	86.5

Source: World Bank Group, (<http://worldbank.org/data>)

Inflation

The government’s commitment to a currency board arrangement has dramatically reduced inflation over the past four years. After the economic crisis of 1997, inflation came down to 1% in 1998 (as presenting in the following diagram) there was a slight increase leading to a figure of 6.2%, mainly caused by higher prices in food and energy. Although inflation was expected to remain at the same levels throughout the year 2000 it increased in 11.4%. The reasons were the considerable increase of international prices of energy carries and food products, the latter caused by the low crops due to drought. In spite of that, the currency board is not endangered because the fuel prices will most probably fall in the coming two years, and inflation is expected to drop by 3.5% for 2001.

Diagram 1. Inflation rate (as % of CPI), for the years 1991-2000



Source: World Development Indicators, World Bank Group, (<http://sima-ext.worldbank.org>)

Gross Domestic Product (GDP)

It has to be mentioned that the main problem of the Bulgarian economy is its ineffective financial system and also the inability to develop its capital market. After the severe recession in 1996-1997, the government’s commitment to economic reform and restructuring has set the stage for sustainable long-term economic growth. In 1999 GDP growth decreased to 2.4% reflecting the problems caused by the war in FRY. Despite this, GDP was increase in 2001 to 5.5% as it was expected by the international financial organizations, IMF and the World Bank.

Diagram 2. Gross Domestic Product (% real growth), for the years 1991-2000

Source: World Development Indicators, World Bank Group, (<http://sima-ext.worldbank.org>)

Important steps were taken in the areas of privatization, banking sector reforms, agricultural liberalization. Fiscal policy was prudent as the general government budget deficit was limited to 0.9% of GDP, and income policy for state-owned enterprises was implemented strictly. Structural reforms were continued on a wide front. Privatization was accelerated, recording the highest level of sale of state assets in Bulgaria's history. The total financial effect of the work of the privatization bodies for the period June 1997-October 2000 has amounted to \$4.4 billion, which includes contracted payments, paid and met obligations and contracted investments. The isolation program for commercial enterprises was brought to a successful conclusion.

The liberalization of the agricultural sector, followed consistent with the Government program for structural reform. The trade and pricing policies were fully liberalized and all state control on prices of agricultural and food products was eliminated. A system of licensed warehouse receipts was introduced to provide options for further development of the grain market.

The greatest challenge for Bulgaria in **1999** - the Kosovo crisis - heavily affected practically all direct transport corridors from Bulgaria to the EU countries passing through Yugoslavia. Traffic on the river Danube was blocked. The total direct losses for Bulgaria amounted to \$95 million.

Bulgaria successfully met the economic pressure arising from the regional conflicts and the lasting negative effects of the global financial crises in 1998. GDP growth reached 2.4%, whereas the level of inflation remained moderate at 6.2%. The external current account deficit was contained to an estimated 5.2% of GDP for the full year as exports recovered after midyear. Confidence in the Bulgarian national currency remained strong, with gross official reserves at USD 3.2 billion and the fiscal reserve account at \$1.4 billion at end-1999.

In the energy sphere the power generation, transmission and distribution capacities were separated in order to eliminate the monopoly of the National Electric Company (NEK). Seven regional distribution companies were set up, the Kozlodouli Nuclear Power Plant and seven more major electricity-generating companies were also spun off.

The macroeconomic results in 2000 (i.e., 5.5% GDP growth and inflation close to 11.4% -see Diagram 1 and 2) well address that the foreign companies need to have medium and long-term planning in their strategy.

Major steps were made in mobilizing the investment market. The Cabinet focused its efforts on promoting the private sector development and measures were taken for elimination of red-tape hurdles for

entrepreneurship, business and trade caused by various restrictive regimes requiring permission, licensing, registration and consultations prior to approval. As of June 30, 2000 the following was accomplished:

- A total of 49 regimes were canceled or enhanced. The Council of Ministers approved a set of draft acts to enhance 44 regimes, and sponsored them in the National Assembly. Thus, as of 30 June 2000, a total of 93 permission regimes were eliminated, or had been in the process of elimination.
- Privatization reached its final stage as by the end of 2000, 51% of the long-term assets of the state owned enterprises were transferred into private hands, accounting to BGN 296 billion. This percentage rises to 77% if the assets, which are not subject to privatization in the long run, are excluded from the balance. Banking sector privatization is close to its completion with only one more state bank operating on the market. About 99% of the agricultural land have been restituted to its former owners.
- The first large-scale investment projects in the energy sector started in 2000. American companies launched investment projects in the largest energy complex in the country – “Maritsa East” with project costs estimated at more than \$1 billion US.

Cumulative Values of Foreign Direct Investments in Bulgaria

The cumulative value of all Foreign Direct Investments in Bulgaria, reached \$3.929 billion US in 2000. About 80.5% of them have been generated during the period 1997-2000. Attracted FDIs in 2000 were \$1.1 billion - up \$294 million compared to 1999 (i.e., 36.4% of growth). For a third consecutive year FDIs through Green-Field, Joint Ventures (JVs), reinvestments and additional investments in already acquired enterprises exceed the FDIs through privatization, which has been the main source in 1997. The top investors are: Germany, followed by Belgium, Italy, Greece and Cyprus. Other major investors include USA, Austria, Russia, the Netherlands and UK. The European Union is the major source of FDIs for Bulgaria with about 63.5% of the total. FDI distribution by sectors shows the major role of industry (50.1% of the total), followed by finance (19.5%), trade (16.1%), tourism (4.2%), infrastructure and construction (4.8%).

Table 5. Foreign Direct Investments in Bulgaria, by year, in USD mil

FDI	1995	1996	1997	1998	1999	2000	% of growth 1999/2000
	\$90.4	\$109	\$505	\$537	\$806	\$1.100	36.4%

Source: World Development Indicators, World Bank Group, (<http://sima-ext.worldbank.org>)

Besides the positive effect from the introduction of modern technologies, products and management, Green-Field FDIs during the four-year period 1997-2000 generated about 120.000 new jobs (30.000 directly in the investment companies and 90.000 in the service companies – building and construction, repairing, transport, distribution, advertising, etc.).

Foreign direct investment radically changed the food and beverages sector, cement industry, non-ferrous metallurgy, wholesale trade and banking.

4.2.3.Stability Pact

Bulgaria actively participates in the Working Tables under the Stability Pact and supports the initiatives aimed at the economic reconstruction of the region and at promoting Southeast Europe as a favorable business and investment destination. Bulgaria reached an agreement with Romania for the construction of a second bridge over the Danube river (which will be initiated in 2001), for the reconstruction of the ports along the Danube river, the construction of a new passenger terminal at Sofia airport and of a 400 kV, 120-km long electricity connection between Blagoevgrad (Southeast Bulgaria) and Dubrovo (Macedonia).

Bulgaria's infrastructure projects also include the Radomir-Ichtiman road (Corridor VIII), the Kalotina - Northern Arch road (Corridor X, going across the border with Yugoslavia), the Montana-Vidin road

(rehabilitation of a 100 km stretch of Corridor IV), the ring-roads of Vratsa and Montana (Corridor IV), the Sofia-Koulatata road (Corridor IV), reconstruction of the Radomir-Gyueshevo railway line (Corridor VIII), construction of one more line and electrification of the Karnobat-Sindel railway line (Corridor VIII), construction of natural gas storage facilities, upgrading of the Sofia water supply system, and cleaning of rivers in Southern Bulgaria.

The Kosovo crisis highlighted once again the role of Bulgaria as a stability factor in the region. The Bulgarian government has initiated and actively participates in the initiatives aimed at defining a regional framework of economic and political co-operation with clear-cut priorities, based on public consensus.

4.2.4. Sustainable growth for 2001

The updated Government Program 2001 envisages public investments in the major infrastructure projects, thus stimulating the creation of new jobs and expanding consumption.

For 2001 4.376,7 million DEM, are foreseen as investments as the private sector is expected to reach the level of public sector investments. Main priority of the government is the attraction of high and sustainable levels of investment inflows, able to guarantee the economic growth in the country. The mean annual forecasted volume of FDIs able to guarantee the accomplishment of this aim amounts to USD 1.4-2.1 billion per year, for the period 2001-2005.

The main components of the reform program continue to be: privatization of the remaining state-owned enterprises, liberalization of agricultural and energy sectors, the development of the health insurance system, the pension system reform, and increasing the public sector capacity. The forecasted real GDP growth for 2001 is about 5% with inflation of about 5.3% according to the World Bank, World Development Indicators.

Privatization in 2001 will feature the sale of the Bulgarian Telecommunications Company (BTK), Balkancar and Bulgartabac and will mark the beginning of privatization in the sector of utilities.

Table 6. Average annual growth of main Economic Indicators of Bulgaria, by decades and years

Economic Indicators	1980-1990	1990-2000	1999	2000
GDP	3.4	-2.1	2.4	5.8
GDP per capita	3.4	-1.5	3.0	6.3
Exports of Goods and Services	-3.5	2.2	-5.2	24.2
Imports of Goods and Services	-3.3	0.5	5.1	14.6
Agriculture	-2.1	0.4	0.6	-10.1
Industry	5.2	-3.7	-4.4	15.3
Services	4.5	-1.3	11.8	5.6
Private Consumption	2.5	-5.2	-4.9	11.7
General Government Consumption	9.1	-9.4	2.0	9.8
Gross Domestic Investment	2.4	3.3	18.7	-7.7

Source: *World Development Indicators, World Bank Group, (<http://worldbank.org/data>)*

Is Bulgaria's growth experience unique? The answer is no because factors of recovery and growth that have been dominant in other transition economies have also been in play in Bulgaria. In particular, prudent fiscal policy, trade liberalization, and enterprise restructuring are key to raising growth potential in Bulgaria, as well as in other transition countries. Orienting production toward exports and improving energy efficiency will also help to improve growth prospects.

4.2.5. Industry - Leading Branches in Bulgarian Economy

While most of the industrial factories are scattered all around the country, the major ones operate in middle-sized cities and keep their branches in Sofia. Heavy industry has been developed in Bulgaria in the period of socialism and its purpose was to supply the Soviet Union market. The industrial sector has shown a dramatic decrease after 1989 and especially the period 1992-1993. In 1994 and 1995 there was an upward movement but didn't last. In 1996 the annual decrease was 1% while in 1997 the decrease reached 10%. In the same period there was a significant increase of private industrial factors that covered 30% of total industrial output. Some of the problems faced both public and private industries are:

- unstable economic environment,
- difficulties in financing,
- bad economic condition of customers,
- restrained demand and shortage in resources.

In industry there is the following structure of output, by branches for the year 2000, which is presented in the following table.

Table 7. Structure of Industry output, by branches, for the year 2000

INDUSTRY OUTPUT BY BRANCHES	% of the TOTAL
Mining	5.4%
Foods, beverages and tobacco	18.4%
Textile, leather and clothing	6.2%
Wood products	1.2%
Pulp, paper products, publishing	3.3%
Chemicals, chemical products, fibres, rubber and plastic products	9.1%
Basic metals except casting	10.1%
Metal products, machinery and Equipment, casting	7.8%
Electrical and optical equipment	3.4%
Transport equipment	1.3%
Electricity, gas and water supply	14.6%
Nonmetal mineral products	3.3%
Others	5.25
TOTAL	100.0%

Source: World Development Indicators, World Bank Group, (<http://worldbank.org/data>)

Chemical Industry

Chemical industry is one of the well-developed sectors of the Bulgarian industry amounting to 20% of the total industrial output for 2000. This branch has good positions on the main export markets of Bulgaria and supplies the domestic and foreign market with intermediate and finished products. The main manufactured products are: organic and non-organic chemicals, fertilizers, soda ash, plastics, PVC, polyamide and polyester fibres, paints, varnishes, synthetic substances, pharmaceutical products, perfumery and cosmetics, oils and fuels, etc. Chemical products have significant share in Bulgarian exports, accounting to 23%, for the year 2000.

Food - processing, Beverages and Tobacco Industry

Food-processing, beverages and tobacco industries are one of the main industry branches in the Bulgarian economy. The favorable climate and long-terms traditions in the production of quality wines, cheese, tobacco products, vegetable oil, etc. stimulate its development. Food production accounts for 18.4% of the total industrial production with an export share of 9%. The main sectors of food, beverages and tobacco industries include meat processing, dairy, canning, sugar and sugar products manufacturing, vegetable oil production, wine production, brewing, fish processing, tobacco production, and milling.

Metallurgy

Ferrous and non-ferrous metallurgy are the basis of machine-building industry, construction and other branches of the Bulgarian economy. In 2000 the output of metallurgy accounted for 10% of the total industrial output. Their share in the total exports for the year 2000 is about 18%.

Machine-building

Machine-building has an important position in the national economy with a share of 9% in the total industrial output. The machine-building sector comprises some 500 enterprises in branches like production of tools and machines, automated machines, fork-lift trucks, electric chain hoists automobile completing units and details, warehouse machinery, hydraulic units, fittings, agriculture machines and spare parts, shipyards, etc.

Electrical Engineering and Electronics Industry

Electrical engineering and electronics industry have been designated as strategic sectors and have priority in long-term development programs. The production of these sectors in 2000 amounts to 3.4% of the total industrial production. Electrical engineering and electronics industry combine the potential of more than 200 enterprises, specialized in different branches like electrical engineering (electric motors, transformers, batteries, cables, etc.), computer and office facilities, electronics, radio-engineering and communication equipment, household appliances, military-industrial complex.

Textile Industry

Textile industry is one of the oldest branches of Bulgarian industry, which begun in 1834. Now the sector comprises some 3.000 enterprises in the textile, knitting and clothing branches with an about 5.3% share in the total industrial output for 2000 and 17% in exports. The main products are yarns, silk, wool, cotton and man-made textile fabrics, knitted fabrics, carpets, wearing apparel, etc.

Other Industrial Branches

Some of the other industrial branches, which have a well-developed production base are as follows: (a) building materials industry, (b) pulp and paper industry, (c) leather, fur and footwear industry, (d) glass and china industry, (e) wood-working industry, etc.

Energy

The total installed electric power capacities in the country are 12,668 MW out of which: (a) 6.556 MW, or 51.7% thermal power plants, (b) 3,760 MW, or 29.7% nuclear power plant, (c) 1.920 MW, or 15.2% hydro-power plants, (d) 432 MW, or 3.4% pumped-storage hydro-power plants.

Agriculture

Bulgaria enjoys excellent natural conditions for the development of agriculture. Cultivated agricultural land occupies about 4.9 million hectares or 44% of the total territory of the country. The favorable climate, soil and long-term agricultural tradition have led to a relatively well-developed plant-growing and animal-breeding.

Among the main crops are tomatoes, pepper, tobacco, grapes, wheat, maize, beans, potato, sunflower, peaches, apricots, apples, melons, nuts, etc. There are traditions in the sheep, pig and cattle breeding, poultry farming, and bee-keeping.

It is worth mentioning that in different periods of its recent past, Bulgaria has had a good position in the export of grapes, oriental tobacco, tomatoes, apricots and other agricultural products.

Tourism

Tourism is one of the key sectors in Bulgaria due to the specific nature and climate of the country. Bulgaria offers diverse forms of tourism as health tourism, hunting and fishing, nautical tourism and cruising, congress tourism, etc. The abundance of mineral water springs in the interior of the country and near the sea and mountain resorts creates excellent conditions for the development of tourism. The unique cultural and historical monuments, including the ones from Thracian and Roman times, the original folklore, customs, and the specific national cuisine and beverages are a major attraction for the foreign tourists.

The resorts along the Black sea coast - Golden Sands, Sunny Beach, Albena, Duni, Eleni, Sunny Day, Riviera, etc., are preferred for the summer vacation. For the fans of winter sports, the mountain resorts Pamporovo, Borovets and Bansko offer very good conditions and competitive prices. It is worth mentioning that the capital city Sofia is located very close to the Vitosha mountain, where the skiers can find good recreation facilities only 30 min away from the city center. Bulgaria has the unique Rose Valley near the town of Kazanluk, a place world famous with the growing of roses and the extraction of highest quality rose oil, used in the perfume industry by the most prestigious companies.

According to preliminary data, of Foreign Investment Agency of Bulgaria, the number of foreign tourists visited Bulgaria in 2000 is about 2.4 million (13% increase in comparison to 1999).

4.3. Foreign Trade

Until the late 1990s Bulgaria's trade regime was highly restrictive and distortionary. A first round of tariff liberalization took place in the early 1990s, after the collapse of the CMEA, to prevent disruptions in the chain of industrial supplies. While the average industrial tariff rate was reduced to 20% at that time, little additional progress was made for a number of years. The trade system continued to be geared at protecting unreformed sectors, such as agriculture and heavy industries, from international competition through a complex combination of tariffs and non-tariff barriers and export restrictions.

The overall level of protection even increased in 1996-1997, when the country experienced a banking and balance-payments crisis and near hyperinflation. Moreover, the trade system had reached a level of administrative discretion and micro management that clearly discouraged trade and investment in the country.

By the time, a new government (of Ivan Kostov) took office in the middle of the year 1997 and trade liberalization became a major pillar of the transition process, along with macroeconomic stabilization, price liberalization, enterprise privatization and financial sector reform. The aim of the trade reform was to correct distortions in the trade and production patterns created by CMEA specialization, restore the incentives for economic activity, and integrate Bulgaria into the world economy. Like its neighbors, Bulgaria used all avenues to liberalize trade-multilateral agreements, regional initiatives, and unilateral steps—although the biggest progress seems to have been achieved unilaterally, under Fund-supported programs.

Since then, Bulgaria has made major progress. The outcome of this multi-pronged policy has been a complete elimination of quantitative restrictions and major rationalization of the tariff regime. Reforms under two Fund-supported programs (*a stand-by arrangement signed in April 1997, and an extended arrangement*

signed in September 1998, supported under the United States Small Business Administration Organization, was aimed at creating high sustained growth and a competitive market economy) improved Bulgaria's rating under the Fund's Trade Restrictiveness Index - which was developed by IMF- from 7 (a moderately restrictive regime) to 2 (liberal trade regime). With the present rating of 2, Bulgaria is among the 20% most open members of the Fund, and Bulgaria has now achieved an open trade regime by international standards.

Despite the good progress, regional integration requires further liberalization and simplification of the trade system. At 12.4%, Bulgaria's simple average tariff rate remains nearly twice as that of the EU, and somewhat above the rates in the neighboring countries. In addition the tariff regime remains complex and dispersed, with as many as 22 tariff bands. Important sectors of the Bulgarian economy, particularly agriculture and heavy industries, continue to benefit from higher-than-average levels of protection, retarding their adaptation to a very competitive European market. More can be done to achieve a simpler and more liberal tariff system that would be easier for the government to administer, better for economic efficiency, and more attractive to investors and trades.

4.3.1. Trade Volume, Trade Partners, Structure

For the year 2000, the Bulgarian foreign trade turnover amounts to \$11.306 million US, which is 19.7% more towards the same period of 1999. Export and import volumes for the 2000 amount to \$4.812 million US and \$6.494 million US respectively. Data for the last two years and 10 years ago are shown in the following table.

Table 8. Export and Import volumes of Bulgaria, in USD mil

USD million	1990	1999	2000
Total Turnover	8.403	9.521	11.306
Export (FOB)	3.743	4.006	4.812
Import (CIF)	4.660	5.515	6.494

Source: World Development Indicators, World Bank Group, (<http://www.worldbank.org>)

Table 9. Trade and Finance Indicators of Bulgaria (1995-2000)

INDICATORS	1995	1997	1998	1999	2000
Aid per capita (current \$ US)	13.4	26	28.5	32.3	N/A
FDI net inflows in \$US million	90.4	505	537	806	1.100
Trade in goods (%of GDP, PPP)	23.1	24	23.3	22.9	N/A
Trade in goods as a share of goods (% of GDP)	N/A	209	165	137	150
Short term-debt outstanding (DOD, in \$ million)	507,9 mil	736,3mil	418,7mil	375,8 mil	N/A
Total debt service (TDS, in \$US million)	1.100	971,3	1.296,3	1.155,7	N/A

Source: World Development Indicators, World Bank Group, (<http://www.worldbank.org>)

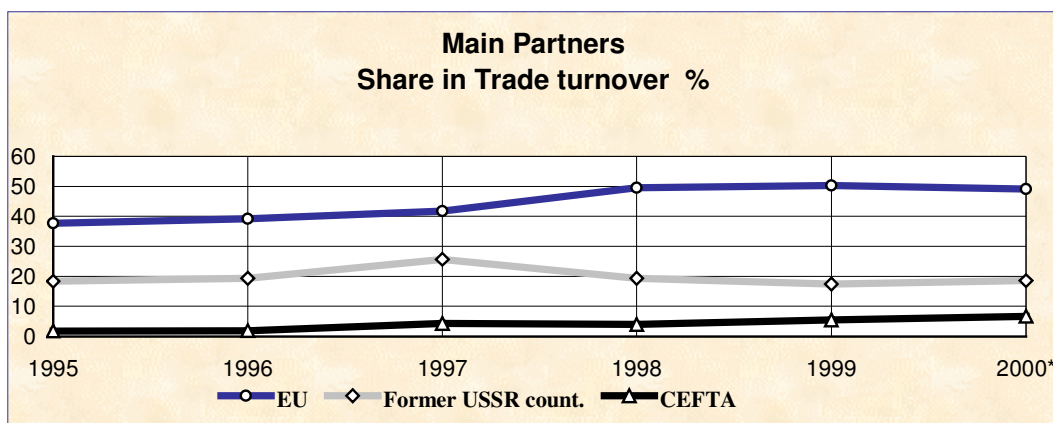
As mentioned above, Bulgaria is making significant efforts to liberalize trade and therefore, create an attractive investment environment. Among other things the government has decided to reduce average import taxes to 13.9%, eliminate the import surcharge, and gradually remove tariffs with EU. In 1998, imports reduced due to the dependence of the Bulgarian economy on Soviet trade and the loss of entrance to beneficial markets, which in turn resulted in a low level of exports. In 1999, Bulgaria's trade deficit widened due to trade disruptions caused by the war in FRY.

The largest percentage of Bulgaria's imports includes: raw materials, mines and fuels, especially oil and gas, followed by machinery and armament. Categories such as chemicals, plastics, textiles, clothes, shoes and industrial consuming products are about 10% of the total imports.

As it was mentioned above, Bulgaria is trying to shift trade from the Former Soviet union towards the European Union. As a result, the last few years the leading trading partners are Germany, Italy and Greece.

During the 2000, foreign trade with the Organization for Economic Co-operation and Development (OECD) member countries amounts to \$ 6.693,1 US million, which is 59.2% of the total turnover. Within the OECD countries, the European Union member countries are the Bulgarian largest trade partners, accounting to \$5.325,1 US million, which is 47.1% of the total turnover. The largest trade partner within the EU is Germany, followed by Italy, Greece, France, Belgium and the UK. From the non-European countries, the largest trade partner is the USA.

Diagram 3. Bulgaria: Main partners share in trade turnover (%), 1995-2000



Source: Bulgarian Foreign Direct Investment Agency (<http://www.bfia.org>) *2000 estimated

The Central and Eastern European Countries (CEEC) are the second major market for Bulgarian trade, accounting for 30.4% of the total turnover. The main trading partners from this group are the former USSR countries with 18.6% of the total turnover and main trading partners Russia and Ukraine, followed by CEFTA countries (Poland, Czech Republic, Slovak Republic, Hungary, Romania and Slovenia) with 6.7% of turnover.

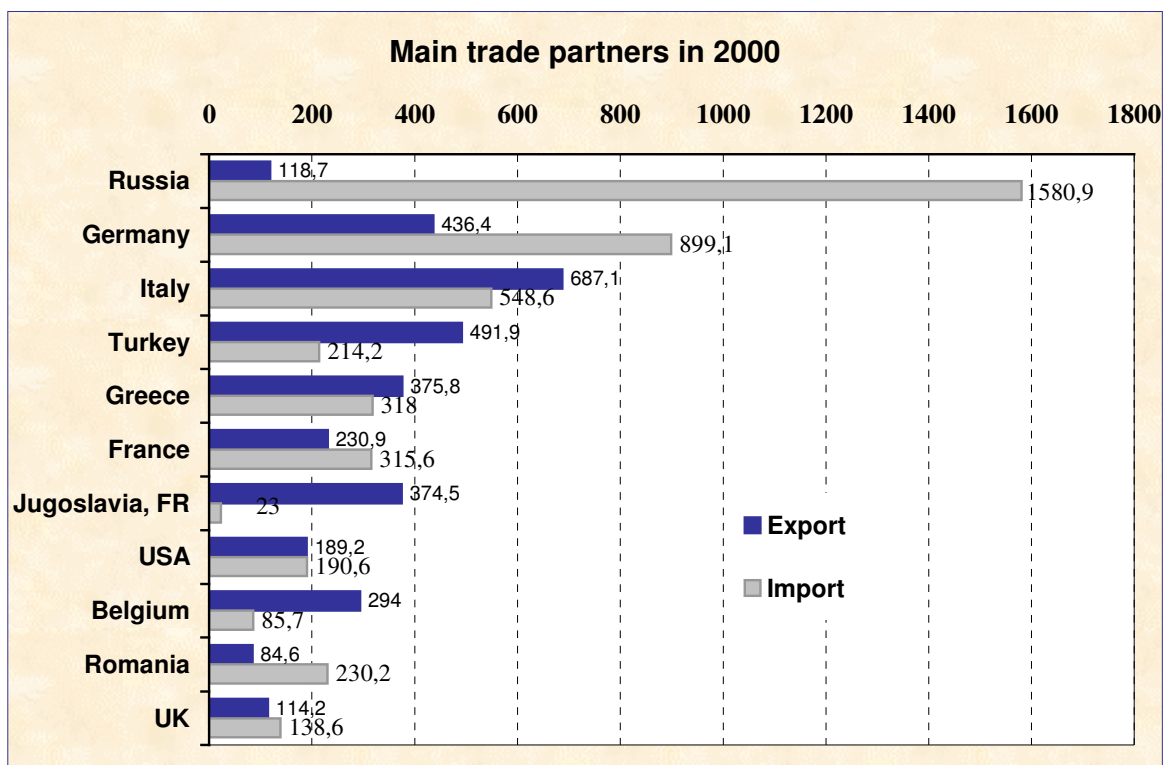
Table 10. Territorial Structure of Export and Import, for the year 2000

REGION	Export 2000		Import 2000		Turnover 2000	
	USD miln	%	USD miln	%	USD miln	%
OECD countries incl.:	3.252,9	67.6	3.441,8	53.0	6.693,1	59.2
EU	2.463,8	51.2	2.863,8	44.1	5.325,1	47.1
EFTA	52,9	1.1	90,9	1.4	147	1.3
Other OECD countries*	736,2	15.3	487,1	7.5	1.221,0	10.8
CEEC countries incl.:	1.005,7	20.9	2.428,8	37.4	3.437,0	30.4
Balkan countries**	524,5	10.9	51,9	0.8	576,6	5.1
CEFTA countries	173,3	3.6	571,5	8.8	757,5	6.7
Former USSR countries	307,9	6.4	1.805,4	27.8	2.102,9	18.6
Other countries	553,3	11.5	623,4	9.6	1.175,9	10.4
TOTAL	4.812	100.0	6.494	100.0	11.306	100.0

Source: Bulgarian Foreign Direct Investment Agency (<http://www.bfia.org>)

* Included: Australia, Canada, New Zealand, USA, Turkey, Japan and Mexico

** Included: FYROM, Croatia, Albania, Yugoslavia, Bosnia and Herzegovina.

Diagram 4. Main trade partners of Bulgaria by country, in 2000 (in USD mil)

Source: Bulgarian Foreign Direct Investment Agency (<http://www.bfia.org>)

4.3.2. Major trade agreements

WTO: Bulgaria is a member of the World Trade Organization since 1 December 1996. This will spur greater market liberalization following a transition period.

EUROPEAN UNION: In March 1993 Bulgaria signed with the European Communities and their member states the Europe Agreement of Association, entered into force on 1 February 1995. The Interim Agreement on Trade and Trade Related Matters covering trade components entered into force on 31 December 1993. In accordance with the Agreement of Association, customs duties between Bulgaria and the EU countries on industrial goods are being dismantled and should be completely eliminated by 2002 at the latest. The Europe Agreement also calls for the harmonization of Bulgaria's laws and institutions with those of the European Union in preparation for eventual full membership.

EFTA: According to the Agreement between Bulgaria and the European Free Trade Association (in force since July, 1993) preferences on trade with EFTA countries (Switzerland, Norway, Island and Liechtenstein) are granted under almost the same terms and conditions as those pursuant to the Europe Agreement of Association.

CEFTA: Bulgaria became a member of the Central European Free Trade Agreement in July 1998; the trade component of this agreement came into force on 1 January 1999. In accordance with the above agreement, Bulgaria has begun a process of liberalization of trade with industrial and agricultural goods with CEFTA countries (Poland, Czech Republic, Slovakia, Hungary, Romania and Slovenia) which will be completed by 1st January 2002.

FREE TRADE AGREEMENT with Turkey entered into force on 1 January 1999. Customs duties will be reduced gradually until 2002.

FREE TRADE AGREEMENT with FYROM entered into force on 1 January 2000. Customs duties will be reduced gradually until 2005.

FREE TRADE AGREEMENT between Bulgaria and Israel is expected to go into effect by the beginning of 2001.

4.3.3.Foreign trade regulations

Bulgaria applies a liberal foreign trade regime that meets the World Trade Organization (WTO) requirements. A limited number of goods are subject to administrative control. In accordance with the trade liberalization policy, the number of goods subject to permits has been reduced for another time, following the Council of Ministers Decree No. 233 of 8 November 2000, which establish the foreign trade regime for 2001.

Registration (automatic licensing) means registration of export and import transactions of goods, carried out for statistical purposes.

The permit (non-automatic licensing) is a license for transactions of goods, which is a requirement originating from Bulgaria's compliance with international agreements and respective domestic laws. Registration and permit are required for a limited number of goods.

In order to perform a registration or for the purposes of obtaining a permit, the company has to submit to the relevant competent Ministry a filled-in certificate form together with other documents like court registration and tax registration certificate, identification code of the BULSTAT register, as well as the relevant documents which verify the data, contained in the filled-in certificate form, such as contract or pro-forma invoice, order, quality certificate, veterinary certificate, certificate of origin. In some cases additional documents are required; for instance, for the import of matrixes for CD production a copyright certificate is required, licenses for trade or production (if necessary) and others may also be required.

The entry (*which means physical entry or introduction entry of goods into the customs territory of Bulgaria, upon border crossing*), direct transit, export and re-export of military and special production as well as goods and technologies with possible dual use (civil and military) are subject to particular rules (Bulgaria is a party to the Waassenar Agreement)

4.3.3.1.Import and export regulations

Transactions of only few goods are subject to **registration** and they include:

- Polycarbonates, stampers (matrixes) for compact disk production in case of entry. Responsible for registration is the Ministry of Economy.
- Hard alcohol drinks in bulk as well as ethyl alcohol with titre less than 80 vol.% in case of entry. Registration is performed by the Ministry of Economy.
- Precious metals and articles thereof with regards to entry, export and re-export. Responsible ministry is the Ministry of Finance.
- Some kinds of timber in case of export. Registration is performed by the Ministry of Agriculture and Forestry.

Since 2001, **permits** (licensing) have been required for transactions with several commodity groups. Some of the more significant commodity groups include:

- Entry, export and re-export of nuclear material, radioactive substances and other sources of radiation, always in compliance with the requirements of the Peaceful Use of Atomic Energy Act. Authority responsible for registration is the Committee for Peaceful Use of Nuclear Energy.
- Entry, export and re-export of gunpowder, explosives and pyrotechnic material and products made from them for civil uses, trinitrotoluene (TNT), hunting and sporting arms, gas- and signal- guns and revolvers and ammunitions for these, and in case of physical entry of sights, laser beam sights and gas sprays, always in compliance with the requirements of the Control of Foreign Trade Activities with Arms and Goods and Technologies with Possible Dual Use Act. Responsible authority is the Ministry of Economy.
- Import of pharmaceuticals for human medicine, always in compliance with the Human Medicine Pharmaceuticals and Pharmacies Act. Responsible authority is the Ministry of Health.
- In case of entry, direct transit, export and re-export of military products or special-purpose products, and of goods and technologies with possible dual use (civil and military) – always in compliance with the Control of Foreign Trade Activities with Arms and Goods and Technologies with Possible Dual Use Act, the Rules for Implementation of the Control of Foreign Trade Activities with Arms and Goods and Technologies with Possible Dual Use Act, and the List of Arms and Goods with Possible Dual Use, determined in Decree of the Council of Ministers No. 205/1998I
- In case of entry, export and re-export of controlled chemical substances used in the production of general anesthetic and psychotropic substances, always in compliance with the Control of Narcotic Substances and Precursors Act, the Ordinance for Precursor Control, said Ordinance been adopted by Decree of the Council of Ministers No.104/2000, etc.

Bulgaria applies **export quotas** only for those goods, which are subject to international agreements. Quotas are applied for the export of textile and clothes to the USA and Canada. No customs duties and taxes are charged for exported goods.

4.3.3.2. Customs law and tariff system

The new Customs Law that entered into force on 1 January 1999 is based on the EU Customs Code. The same terms and regimes as those of the EU are applied: entry into customs territory, import, temporary import, temporary storage, transit, export, temporary export, active and passive improvement, processing under customs control, postponed payment, etc.

The Bulgarian Customs Tariff, the latest version of which entered in force on 1 January 2001, is based on the international Harmonized Commodity Description and Coding System and on the EU Combined Nomenclature. The adoption of both the new Customs Law and the modified Customs Tariff is a part of the National Strategy for joining the European Union.

The customs clearance of goods requires the presentation of a customs declaration, which is similar to the Single Administrative Document (SAD) used in the EU, accompanied by the required commercial documents like invoice, certificate of origin, transport document or any other relevant official papers.

In the new Customs Tariff for 2001 customs duties on significant number of industrial goods are reduced, the average rate for industrial goods being 10% with respect to the import from countries treated according to the Most Favored Nation principle. A large number of industrial commodity groups (20% of tariff lines) are treated with zero rate of customs duties and they include mainly energy sources, raw materials, medicines and others.

According to the Association Agreement with the European Union and the Agreement with EFTA a large proportion of the imports from their member countries in 2001 is taxed with reduced or zero import duties. For instance, an average rate of customs duties for industrial goods is below 1%. In accordance with the

respective Free Trade Agreements significant reducing of duties is applied with regards of import of industrial goods. In case of CEFTA countries the average rate of customs duties is practically zero, in case of import from Turkey average rate is under 1% and for FYROM the rate is 2.4%.

Bulgaria applies the General System of Preferences, recommended by the UNCTAD, which sets lower tariffs for imports from developing countries.

Bulgaria's membership in the World Trade Organization guarantees the stability of the customs duty system.

4.3.3.3. Trade license

Some trade activities in the country, which have particular meaning in respect to the national security, life and health of people, animals and plants, environment and protection of culture values, are subject to licensing (permission) by the appropriate authorities. License is required for production and trade of spirits and alcohol drinks; trade with plant protection chemicals, trade with arms, production and trade of medicines, processing and trade of tobacco and tobacco products, etc.

4.3.3.4. Free trade zones

Duty Free Trade Zones (FTZ) were established in Bulgaria in 1987 under Decree No. 2242 on the "Duty-Free Zones and its Regulations for Application". The new economic agenda of the country raised the profile of the free zones. The new Customs Act, whose provisions do not replace those of Degree No.2242, renamed the six duty-free zones as "free zones". The Customs Acts also states that goods located in the free zones and free warehouses are not considered as being in the customs duty of Bulgaria and are not subject to customs duty. Free zones must have access control at fixed entrance and exit points. New construction within the free zones is to be undertaken in conformity with the customs authorities.

There are six free trade zones in Bulgaria. All of them are initiated and provided with land and infrastructure by the state. Each zone is managed by a purpose-set joint stock company or a state owned company. The duty-free zones are located on strategic transport routes leading to the main international markets: the EC, the Central European and ex-Soviet countries, the Middle East and Northern Africa. Two of them are along the Danube River at the ports of Vidin and Rousse with an access to Central and Western Europe via the waterway Rhine-Maine-Danube, and with the ex-Soviet countries via the Ro-Ro line between the Port of Rousse and the Port of Reni - in Ukraine.

Two other zones are at the cross points of the Trans-European motorways, connecting Western and Northern Europe with the Middle East and Greece - one near the Bulgarian-Serbian border in the town of Dragoman and the other in the city of Svilengrad close to the Bulgarian-Turkish border.

Another duty-free zone is in Plovdiv, second largest city, situated in the heart of Bulgaria. It includes the territory of the Plovdiv International Fair and the industrial zone of the town having a very well developed infrastructure. The Plovdiv International Airport has got air connections throughout Europe, the Middle East and Northern Africa.

The Bourgas duty-free zone is positioned next to the largest Bulgarian Black Sea port with convenient maritime connections to all Black Sea and Aegean countries. The zone includes a cargo terminal at the Bourgas International Port.

The Law on Customs, which has entered into force in January 1999, has renamed the duty-free zones to "free zones". It governs the regime of the free zones in detail and brings it in compliance with the new customs legislation. Under the Law on Customs, the free zones are to be established as separate parts with check-in control at fixed entrance and exit points.

A new construction on the territory of the free zones is to be undertaken in conformity with the customs authorities.

All kinds of production and trade activities and services are allowed to be performed on the territory of the free zones, as provided for in the Law.

Foreign goods may be kept in the free zones:

- under customs regime "import" as provided for in the law,
- without a special permission, as subject to operations designated to storage thereof, to improve their trade image and quality or processing for new delivery or sale,
- under customs regime "active improvement" according to the provisions of the Law,
- under customs regime "processing under customs control" according to the provisions of the Law,
- under customs regime "temporary import" according to the provisions of the Law.

Local goods, kept in the free zones, may be subjects only to operations aimed at their storage. Permission by the customs authorities is required for such operations. The local goods may be subject to other operations beyond storage, in case they will be exported.

Standard features of the Bulgarian free-trade zones are as follows:

- Convertible foreign currency is in use.
- Revenues can be transferred abroad freely without any restrictions.
- Administrative structures relieve the investor's need to directly contact the local authorities.
- Railway links are well-developed and convenient.
- Production and labor cost are low, trained and highly qualified labor is available as well.

The free trade zones in Bulgaria have attracted a number of foreign investors to undertake processing and trade activities such as: Hyundai Co., Daewoo Co., KIA motors, CITCO, Schawartskopf, Henkel, Landmark Chemicals Ltd., Group Scheider, BINDL Energic Systeme GmbH.

4.3.3.5. Protection of competition

The new Law on Protection of Competition came into force on 12/05/1998 repealing the Law on Protection of Competition 1991. The main objective of the Law is to secure protection and good conditions for the expansion of competition and free initiative in the economic activities, in order to make them main regulators of the market economy in Bulgaria.

The Law provides protection against:

- agreements, decisions and coordinated practices,
- misuse of monopolistic and dominating position on the market,
- concentration of economic activities and unfair competition,
- other actions which may result in prevention, restriction or breach of competition.

The Law applies to all enterprises carrying out activities in Bulgaria, including the enterprises with foreign investment.

Pursuant to the Law on Protection of Competition “enterprise” means any natural person, legal person or entity pursuing activities on the relevant market, regardless of the particular legal form.

Commission for the Protection of Competition

The Commission is the state authority that is responsible for the effective application of the Law. The Commission:

- ascertains violations and imposes sanctions as provided for in the law,
- issues permissions as provided for in the law,
- suggests to the competent bodies of the executive and the local government to repeal regulative acts,
- issues in violation of this Law, and files claims with the Court for the revocation of individual administrative acts which are contrary to the law.

In the course of its operation the Commission:

- conducts survey and ascertains the position of enterprises on the relevant market, pursuant to methods adopted by the Commission,
- offers opinions on projects for the transformation and privatization of enterprises or parts thereof, where requested by the relevant Government and local bodies, in the event of circumstances which may eventually violate the Law.

The Commission may permit:

- preliminary equalization of the general terms for enterprises which offer contract's conclusion by applying general terms as provided for in the law,
- state aids designated to: (1) accelerate the economic development in regions with low living standard or unemployment above the average for the country, (2) promote the economic growth in particular economic activities or regions as provided for in the law, (3) support the implementation of projects that are of significant importance for the country or to surmount considerable difficulties in Bulgaria's economy.
- concentration of economic activity as provided for in the Law.
- exemption of the prohibited acts as set forth in the Law.

Restriction of Competition

Certain acts are prohibited by the Law in case they aim at or lead to the restriction of competition. These are agreements, decisions and coordinated practices, misuse of monopolistic and dominating position on the market, concentration of economic activities, unfair competition and other actions, which may result in prevention, restriction, or breach of competition.

If these acts are accomplished in contradiction to the Law on Protection of Competition they are considered to be null and void. The Commission proclaims the invalidity although any person may rely on it.

On the other hand, the Commission may exempt from the above-mentioned prohibition an act that fosters the growth and enhancement of the production of goods and provision of services, the technical and

economic development or the improvement of competitiveness on foreign markets and does not result in restriction or elimination of competition.

Monopolistic and Dominating Position

Under the Law the position of an enterprise, which has by law the exclusive right to pursue a certain type of economic activity is considered monopolistic. Monopolistic position may be granted only by the law in cases it has been provided to the State pursuant to Article 18, paragraph 4 of the Constitution of the Republic of Bulgaria. Any other granting of monopolistic position shall be considered null and void.

According to the Law, an enterprise has a dominating position when in view of its market share, financial resources, opportunities for access to the market, technological level and business relations with other enterprises it may prevent competition on the relevant market, since it is not dependent on its competitors, suppliers or buyers. There is an assumption that an enterprise has a dominating position, if it has a market share exceeding 35 % of the relevant market.

Concentration of Economic Activity

The Law regulates the consequences in case a concentration of economic activity occurs, namely merger or acquisition of two or more independent enterprises, direct or indirect control over one or more enterprises or parts of them.

In case the total market share of the goods or services involved in the concentration exceeds 20% or the total turnover of the participants in the concentration for the preceding year exceeds BGN 15 million, the enterprises are bound to notify in advance the Commission of their intention to pursue concentration.

The Commission may take the following decisions: to declare the concentration as being beyond the above mentioned criteria, to permit the concentration, to begin investigation if there are serious doubts that it might result in the establishment or strengthening of the existing dominating position and that the efficient competition on the relevant market could be prevented, restricted or breached. The court shall enter the merger or acquisition in the commercial register after an issued permission by the Commission has been presented.

4.4. Foreign Direct Investment (FDI)

Foreign direct investment (FDI) has increased considerably in recent years, providing a boost to productivity. As a result of macroeconomic stabilization and renewed privatization efforts, FDI inflows rose from \$109 million US in 1996 to a record of \$1.1 billion US in 2000, with privatization-related inflows accounting for almost half of the total. The FDI stock exceeded \$3 billion US at the end of 2000, up from less than \$500 million US four years earlier. As in other transition countries, FDI acts as a channel for the transfer of technological and management know-how, and provides financing for investment in rehabilitation and new capacity. Studies using firm level data clearly show that Bulgarian firms with foreign participation are more efficient than those with only domestic state or private ownership. Controlling for other factors, total factor productivity in a fully foreign-owned enterprise is found to be on average 45% higher than state-owned domestic firms, and 12% higher than that in private domestic firms.

According to the IMF report (contacted in March 2001), despite the increased inflows in recent years, the level of composition of FDI in Bulgaria still falls short of what is needed to make FDI a main engine of growth. At less than \$400 US at end-2000, Bulgaria's FDI stock in per capita terms is still significantly below that of the other EU accession countries.

Compared with the more advanced transition countries in central Europe, the share of EU investors is smaller and that of investors from neighboring non EU-countries is larger. Bulgaria also lags the more

advanced transition countries in attracting knowledge—and capita-based FDI, and manufacturing FDI remains concentrated in resource-and labor-intensive branches. Finally, while foreign investors are increasingly launching green field projects, they have as yet shown little interest in taking over and restructuring inefficient privatized enterprises. The following table shows the two forms of FDI: (a) Direct (b) Portfolio Investment which took place in Bulgaria for the years 1996-2000.

Table 11. Direct and Portfolio Investments in Bulgaria, 1996-2000 (in USD mil)

Foreign Direct Investment	1996	1997	1998	1999	2000(Jan-Nov)
Inward Direct Investment *	109	505	537	806	817**
Privatization purchases	36	340	214	227	328
Direct (non privatization) purchases	73	152	290	249	259
Reinvestment earnings	N/A	0	50	-21	26
Other changes in ownership by non-residents	N/A	13	-17	351	204
Inward Portfolio Investments	-122	146	-112	8	-69
Equity securities	2	52	19	2	18
Debt securities	-124	94	-131	6	-87
-Brady bonds	N/A	-21	21	-1	-93
-Bulbank bonds	N/A	-51	-53	-36	0
-Government securities	N/A	58	-48	23	1
-Zunk bonds	N/A	109	-81	5	4
Other portfolio investment by non-residents	N/A	N/A	30	14	1
Inward Direct Investment (in % of GDP)	1.1	5.0	4.4	7.9	6.7
Inward Portfolio Investment (in % of GDP)	-1.2	1.4	-0.9	0.1	-0.6

Source: IMF Country Report No.01/54, March 2001, page.100.

*measured on a balance of payment basis,

** the FDI in Bulgaria, at end - 2000 was reached 1.1 billion USD.

4.4.1.Foreign Direct Investment Statistics

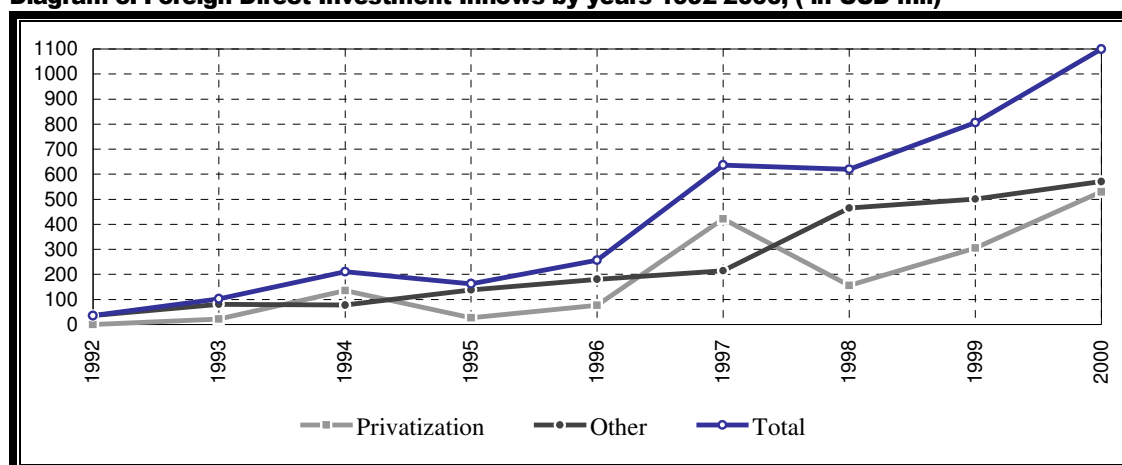
Table 12. Foreign Direct Investments Inflows, by years (1993-2000)

YEAR	VOLUME IN USD millions		
	Privatization	Other*	Total by years
1992	0	34,4	34,4
1993	22,0	80,4	102,4
1994	134,2	76,7	210,9
1995	26,0	136,6	162,6
1996	76,4	180,0	256,4
1997	421,4	214,8	636,2
1998	155,8	464,2	620,0
1999	305,7	500,4	806,1
2000	530,0	570,0	1.100,0
Total	1.671,5	2.257,5	3.929,0

Source: Bulgarian Foreign Direct Investment Agency (<http://www.bfia.org>)

Explanation: **Other* means:** Greenfield investment, Additional investment in companies with foreign participation, Reinvestment and **Joint Ventures**.

The following diagram shows the above table data of FDI inflows by years.

Diagram 5. Foreign Direct Investment Inflows by years 1992-2000, (in USD mil)


Source: Bulgarian Foreign Direct Investment Agency (<http://www.bfia.org>)

Table 13. Foreign Direct Investments by Countries, in USD millions

Nr.	Country	1992	1993	1994	1995	1996	1997	1998	1999	2000	Total by countries
1	GERMANY	0.1	56.6	111.4	16.2	53.1	31.4	55.7	101.3	72.3	498.2
2	BELGIUM	0.0	0.1	0.3	10.0	0.8	264.4	31.2	66.2	39.8	412.9
3	ITALY	0.0	0.2	5.2	2.3	1.2	0.4	2.1	23.0	339.7	374.1
4	GREECE	0.2	5.1	3.0	29.8	14.6	16.1	3.3	14.9	241.1	328.0
5	CYPRUS	0.3	1.2	0.4	1.4	7.5	20.6	109.1	108.9	-11.3	238.1
6	USA	0.0	10.5	16.2	16.1	20.7	46.6	38.6	49.8	37.1	235.5
7	AUSTRIA	13.0	1.0	14.7	1.4	12.1	12.5	46.9	23.4	88.8	213.7
8	RUSSIA	0.3	1.4	2.3	15.1	14.4	2.0	14.8	103.7	50.8	204.7
9	NETHERLANDS	0.1	0.5	37.9	0.9	46.3	10.8	41.3	28.0	17.4	183.1
10	UK	6.2	5.6	2.4	13.7	7.3	15.8	58.9	48.0	22.6	180.5
11	TURKEY	0.0	9.8	1.3	13.7	7.3	9.9	23.8	39.4	19.5	124.6
12	FRANCE	0.0	0.2	4.2	5.0	6.5	0.8	3.4	62.7	28.9	111.7
13	SPAIN	0.0	0.1	0.0	0.0	0.0	49.6	56.8	3.2	0.7	110.4
14	SWITZERLAND	0.4	6.7	0.2	7.9	23.1	31.4	6.6	13.1	15.0	104.3
15	KOREA	0.0	0.0	0.3	0.2	22.3	22.9	1.8	2.8	6.6	56.9
16	BAHAMAS	0.0	0.0	0.0	0.0	0.0	0.0	22.8	10.4	14.2	47.3
17	LUXEMBURG	0.4	0.6	0.6	0.4	0.2	11.8	22.7	3.8	0.0	40.4
18	IRELAND	0.0	0.0	0.0	17.4	0.2	5.2	1.0	3.7	1.0	28.5
19	ISRAEL	0.0	0.0	0.9	0.0	1.5	0.0	0.0	13.8	1.9	18.2
20	HUNGARY	12.3	0.1	0.0	0.0	0.1	0.0	0.7	1.7	2.0	16.7
21	CZECH	0.0	0.0	0.1	2.3	2.3	4.7	0.6	0.1	0.0	10.0
22	MALTA	0.0	0.0	0.0	0.1	0.1	0.1	8.9	0.0	0.5	9.7
23	LIECHTENSTEIN	0.0	1.1	0.1	0.0	0.0	2.5	0.8	1.3	3.0	8.9
24	SWEDEN	0.0	0.0	0.0	0.0	1.4	2.4	0.9	1.6	0.3	6.6
25	JAPAN	0.0	0.0	0.1	0.5	0.6	1.9	1.9	0.0	1.3	6.3
26	DENMARK	0.0	0.0	1.1	0.0	0.0	1.1	1.6	0.3	1.3	5.4

Source: Bulgarian Foreign Direct Investment Agency (<http://www.bfia.org>)

Table 14. Foreign Direct Investments by Sectors, by years (in USD mil)

FDI by Sector *	1996	1997	1998	1999 (Jan-Nov)	2000 (Jan-Nov)	Total by sectors
Industry	172	458	311	373	128	1,442
Trade	32	46	177	134	85	474
Finance	15	64	72	60	451	662
Tourism	23	6	18	0	0	47
Telecommunications	1	4	23	7	8	43
Transportation	5	3	6	2	6	22
Construction	1	6	6	49	23	85
Agriculture	1	5	0	2	4	12
Other sectors	5	44	6	110	112	277
Total by Years	256	636	620	736	817	

Source: IMF Country Report No.01/54, March 2001, page.101.

* As measured on the basis of contracted amounts and using nominal values for any amounts to be paid in the form of securities such as Zunk bonds.

4.4.2. Foreign Investment legislation

In 24 October 1997, the Parliament of Bulgaria adopted a new Law on Foreign Investment (promulgated in the State Gazette, Issue Nr. 97 of 1997, supplemented, State Gazette, Issue Nr. 29 of 1998, amended and supplemented, State Gazette, Issue Nr. 153 of 1998, Issue Nr. 110 of 1999). The Law brings the legal framework on foreign investment (*see Appendix VI*).

According to the IMF country report No. 01/54, which contacted in March 2001, the quality of the Institutions underpinning the market economy and the business climate continues to suffer from significant shortcoming. While the authorities have made major efforts to put a market-oriented legal and regulatory framework for conducting business, significant problems implementing this framework remain.

EU and World Bank reports continue to point out problems of administrative obstacles is doing business, and weak enforcement of laws and regulations. EBRD Transition Indicators and survey among international investors and economic experts typically rank Bulgaria behind the other EU accession candidates. The detailed 1999 Business Environment Performance Survey, administered by the EBRD and the World Bank to local enterprises, similarly revealed that more remains to be done for institutions reform in Bulgaria.

Bulgaria lagged the other EU candidate counties in such areas as government capture (private influence on the formation of laws and regulations), the frequency of bribing public officials to avoid taxes and regulations, and the efficiency of government services. Bulgaria also scored low in terms of the proper functioning of the legal system, the quality of the judiciary, and the security of contracts and property rights. Legal and regulatory implementation and enforcement problems are reflected in the significantly larger size of Bulgaria's shadow economy compared with more advanced EU accession candidates. Institutional weaknesses binder the development of a vibrant SME sector and by negatively affecting country risk, form an obstacle to attracting a sustained high level of FDI in a diversified range of activities.

4.4.2.1. Institutional framework

Foreign Investment Agency

In April 1995, the Bulgarian Foreign Investment Agency (BFIA) was established as a one-stop shop institution for foreign investors.

The Foreign Investment Agency is a governmental body within the Council of Ministers for coordination of the activities of State institutions in the field of foreign investments and for promotion of foreign investments in the country.

A key function of the Agency is to assist the companies in the investment process. It provides to prospective investors up-dated information on the investment process in the country, legal advice, searching for suitable Bulgarian partners, co-ordination of the investment policy with other institutions, etc.

Bulgaria Economic Forum

The Bulgaria Economic Forum (BEF) was founded as a non-governmental organization in July 1998 by 121 founders. It is based in Sofia, the capital of Bulgaria. The BEF has the following objectives:

- to promote Bulgarian's investment environment to foreign investors,
- to inform the Bulgarian society about the current climate and the problems that the investment process faces in the country,
- to unite the intellectual, industrial and professional potential of the country in search of new possibilities for promoting investment,
- to help state institutions in the field of privatization,
- to cooperate with the national and local business organizations,
- to cooperate with the national media in order to achieve the organization's goals,
- to be in continuous contact and to cooperate closely with similar organizations both at home and abroad.

The activities of the Bulgarian Economic Forum NGO include:

- the organization of the annual Bulgaria Economic forum,
- the organization of conferences, seminars, workshops and discussions,
- the publishing and distribution of newsletters, brochures, analyses and the Bulgarian Economic Forum Report,
- holding consultations on legislation related to foreign investment,
- preparing presentations and road-shows in foreign countries with a potential to expand their investments in Bulgaria etc.,
- maintaining regular relations with representatives and international institutions, government officials and other public organizations.

Advisory Council on Foreign Investment and Financing

An Advisory Council on Foreign Investment and Financing was established as a consultative body to the Prime Minister with the purpose of further improving the investment climate in the country. Members of the Council are representatives of the largest foreign investors, consulting companies, banks and international organizations. The Advisory Council discusses the policy for promotion and attraction of foreign investment and adopts measures for improving the investment environment in the country.

Tax incentive for investments in depressed regions

Foreign and domestic entities, investing in regions with high unemployment rate, listed annually in an appendix to the Law on Corporate Income Tax, enjoy a reduction of the corporate income tax. The corporate tax for recent years is reduced by an annual amount of 10% of the share contributions (for company incorporation or capital increase) provided that the funds generated from the contributions are invested in acquisitions, or reconstruction of tangible assets such as buildings, equipment, transmitters, electricity transmitters, and telecommunication lines. The reduction sum is accounted for as reserves and if it is bigger than the corporate tax due for the respective year it can be used to reduce the corporate tax in the following five years.

4.4.2.2. Foreign investors

Under the Law on Foreign Investments, foreign investors are:

- **legal persons** which are not registered in Bulgaria,
- **partnerships** which are not legal persons and are registered abroad,
- **individuals** who are foreign citizens and have permanent residence abroad.

A Bulgarian national, who is a national of another country as well, should choose whether to avail himself of the status of a Bulgarian or foreign national under the Law.

4.4.2.3. Definitions and forms of investments

Foreign investment is any investment, which is made by a foreign person, in any of the following:

- ✓ shares and stakes in commercial companies,
- ✓ ownership title over buildings and limited ownership title over property,
- ✓ ownership title and limited ownership title over movable property when considered long-term tangible assets,
- ✓ ownership title over enterprise, or detached parts thereof, in accordance with the stipulations of the Law on Restructuring and Privatization of State-Owned and Municipal Enterprises,
- ✓ securities, including debentures and Treasury bonds, as well as their derivative instruments issued by the State, by the municipalities or by other Bulgarian legal persons, with a remaining term until maturity not shorter than 6 months,
- ✓ loans, also in the form of financial leasing, for a term not shorter than 12 months,
- ✓ intellectual property rights - articles of copyright and neighboring rights, patented inventions, utility models, trade marks, service marks and industrial designs,
- ✓ rights stemming from concession contracts and contracts for the assigning of management.

A foreign investment shall, furthermore, include the accretion in value of the investment initially made. Bilateral treaties on promotion and mutual protection of foreign investment to which Bulgaria is a party may provide for a wider definition of foreign investment.

4.4.3. Legal and International guarantees for Foreign Investment

National Treatment

The Bulgarian Constitution and the Law on Foreign Investments provide national treatment to foreign investors which means that foreign investors are entitled to perform economic activity in the country under the same provisions applicable to Bulgarian investors except where otherwise is provided by law. In particular this principle covers the whole range of economic and legal forms of activities for accomplishing entrepreneurial businesses. The national treatment to foreign investors includes the participation in the process of Privatization and acquisition of shares, debentures, treasury bonds and other kinds of securities.

Most Favored Nation Status

Bulgaria is signatory to a system of bilateral treaties on promotion and mutual protection of foreign investment which provide, further to the national treatment regime, for the most favored nation status of the investment made by entities and individuals from one of the contracting countries on the territory of the other contracting country.

Priority of International Treaties

When international treaties to which Bulgaria is a party provide for more favorable terms and conditions for foreign investment, these terms have precedence over the local rules. This guiding principle finds expression in the treaties for protection of foreign investments and especially in the agreements for abstaining of double taxation regulations. The international treaties on mutual protection of foreign investment always include an extended concept of a foreign direct investment, and the application of this concept shall be prior to the Bulgarian legislation.

Legal Guarantees Against Adverse Changes in the Law

The Law on Foreign Investments stipulates the principle that foreign investment made prior to the adoption of amendments in law imposing statutory restrictions only with regards to foreign investments, shall not be affected by these restrictions.

The sense of the law provides for that foreign investments shall be guaranteed against subsequent legislative changes.

Protection against Expropriation

The Bulgarian Constitution allows forcible expropriation of property in the name of the state or for municipal needs only if effected by virtue of a law provided that these needs cannot otherwise be met, and after a fair compensation has been ensured in advance.

Expropriation under Bulgarian Law is governed by the Law on State Property and Law on Municipal Property.

The Law on Foreign Investments provides additional protection to foreign investors. The first added protection granted to foreign investors is that the expropriation may only occur for exceptionally important state needs, which cannot be otherwise met. Immovable property owned by foreign persons may not be expropriated for municipal needs.

As another protection for foreign investors the Law requires compensation in the form of another immovable property in the same location, and only given the foreign investor's consent, in another location, or by cash if the foreign investor prefers so. Compensation equals the immovable property's market price on the day of expropriation.

4.4.4. Establishment of Enterprises with Foreign Investment

Bulgarian legislation provides for establishment of enterprises with foreign investment. These must take the form of any of the business organizations stipulated in the Commercial Code. There are no limitations as far as the share participation of foreign persons is concerned and so is the extend of their investments.

Under the Commercial Code, the following forms of business organizations are open to foreign investors:

- ✓ private limited company
- ✓ single-owner private limited liability company
- ✓ public limited company
- ✓ general partnership (unlimited partnership)
- ✓ limited partnership
- ✓ public limited partnership
- ✓ sole trader

Foreign legal entities registered abroad, as well as foreign natural persons and entities which are not legal persons, may register **branches** if they have been registered as merchants in accordance with the legislation of their countries. A branch is a part of the main company, but with a different seat. It is entered into the commercial register of the court at its location. A branch keeps account books as an independent company. A branch of a foreign company prepares a balance sheet. No authorized capital is needed for its opening. Foreign nationals and companies can register a branch provided they are registered abroad and are entitled to engage in business activities under the national law.

Representative office is regulated by the Law on Foreign Investments. Foreign persons entitled to engage in business activities under their national legislation may set up representative offices, which are registered at the Bulgarian Chamber of Commerce and Industry. The representative offices are not legal persons and may not engage in economic activities. They may only engage in activities related to marketing, finding clients, establishing contacts within the country, as well as any other activities, which are not considered as economic or commercial by virtue of the Law.

4.4.4.1. Creating a joint venture in Bulgaria

There are several laws that govern joint ventures with foreign participation, including the Law on Foreign Person's Economic Activity and Foreign Investment Law and the Commercial Code.

Joint venture is a company formed jointly between a Bulgarian and a foreign partner. The size of foreign participation in a joint venture is not limited. Joint ventures must take one of the forms of business entities pursuant to the Bulgarian Commercial Code.

A foreign national must obtain a permit for permanent residence in Bulgaria when applying for registration as a sole trader or when participating in an unlimited partnership or a co-operative or participates as an unlimited partner in a limited partnership or in a public limited partnership.

As a rule, no prior permits from government institutions are required.

Like the Bulgarian entrepreneurs, foreign investors have to register their activities with:

- local Tax Administration Offices for taxation purposes,

- local Social Security Offices if foreign investors have employees on their pay-roll,
- the National Institute on Statistics under the registration system BULSTAT for statistical purposes,
- customs authorities when foreign trade operations are performed.

Joint ventures with state-owned companies must be approved by the relevant ministry. In most instances, this is the Ministry of Industry. The “regulations for the Regime of Exercising the State’s Rights of Ownership in Enterprises” (amended) promulgated by the Council of Ministers in January 1994, which provides the authority for the respective ministries which have issued internal regulations for the negotiation and approval of joint ventures.

The negotiation phase usually addresses the evaluation of existing assets and contribution of the foreign partner. The foreign contribution can be in cash, capital in kind and/or know-how. The contribution of the local partner is usually in long term assets (i.e., existing equipment, facilities, etc.). Other usually discussed issues are: Labor issues (employment guarantees), future businesses and marketing plans and management contracts.

Joint ventures with private companies do not follow the same procedures. No government involvement or approval is necessary. After completion of negotiations, the entity must be registered with the court. If a new legal entity is created, an evaluation of the assets must be performed by a court appointed expert. The experts’ asset evaluation may not be satisfactory from the investor’s perspective. A foreign investor who obtains a stake in an existing enterprise through an increase in the capital receives an increase in stake based on the value of the already negotiated assets. Valuation is essentially negotiated by the parties than by appointed experts.

The most successful American joint venture in Bulgaria has been the one formed by American Standard and the Bulgarian Vidima Ideal. American Standard has since bought out its Bulgarian partner and built its biggest factory in the world, which exports bathroom fixtures throughout Europe.

The most successful **Greek joint venture in Bulgaria** has been formed by Delta Holding S.A and the Bulgarian Vitalact the so called DELVI-P which was renamed DELTA BULGARIA S.A in May 2000. This company, which combines both production and distribution of ice cream, was founded by DELTA in Bulgaria in 1993. DELTA’s equity stake in the company’s capital stock is 61%. The ice - cream production factory is located in Varna which, in addition to covering the local market, also exports to Albania. DELTA’s distribution network in Bulgaria consists of more than 13.000 points of sale. The company occupies a leading position in the market with 76% share of sales. The total of the human resources employed by the DELTA international enterprises in the Balkan countries now exceeds 1.200 employees. The case study of the above mentioned joint venture is presented in chapter six.

4.4.5. Profit and Capital Repatriation

Bulgaria has established a liberal regime for repatriation of after-tax profit and capital.

Foreign investors can freely purchase foreign currency and transfer it abroad upon presentation of receipt for paid taxes in the following instances:

- income generated through an investment,
- property alienation driven indemnification proceeds, when for state needs,
- liquidation quota resulting from the termination of the investment,
- proceeds from the sale of the investment good,

- a sum received after the enforcement of a writ of execution.

This right may also be exercised by foreign nationals working in the country, with respect to the remuneration received by them, and by foreign nationals who have obtained a permit for permanent residence and are registered as sole traders or participate in a co-operative or as an unlimited partner in a partnership, after a certificate for paid taxes is submitted.

4.4.6. Ownership of Real Estate

According to the Bulgarian Constitution foreign nationals and foreign legal entities may not directly acquire ownership rights on land. If foreigners inherit land in the country, they are obliged to transfer the ownership of the land to local natural or legal persons within three years after the inheritance becomes effective.

The above restrictions, however, do not concern Bulgarian companies with foreign participation, irrespective of the percentage of the foreign participation in the company. Thus foreign persons can acquire full land ownership rights, including ownership rights on agricultural land by setting up or joining a company incorporated under the Bulgarian legislation.

At the request of an investor, the Foreign Investment Agency may trigger a special mechanism for institutional support and propose to the competent authorities (regional governors or municipal councils) to transfer, further to the Law on State Property and Law on Municipal Property, limited property rights (right to build and right to use) on real estate - state private or municipal property, with the view to implement a priority investment project.

Foreign persons and companies with foreign participation need an advance authorization from the Council of Ministers to acquire ownership rights over real estate in border zones and in areas of national security importance as determined by the Council of Ministers.

4.4.7. Inter-ministerial Groups for Institutional Support for Priority Investment Projects

The Law on Foreign Investments allows special institutional help for the investors accomplishing an investment project acknowledged by the Council of Ministers as priority one.

At the request of the investor, the Foreign Investment Agency may propose to the Council of Ministers to form an inter-ministerial group, comprising representatives of ministries and agencies concerned, in order to provide institutional support for appointed investment projects acknowledged by the Council of Ministers as priority investment projects.

Based on the institutional support mechanism, the Council of Ministers recently set an inter-ministerial group in order to co-ordinate the institutional help to the "green-field" investment project of Metro Group in Bulgaria.

4.4.8. Concession Regime

The Bulgarian Constitution 1991 proclaims that concessions can be granted for objects which are exclusive state property or over which the state exercises its sovereign right or has established monopoly, under the conditions and by the procedure set forth in a specific law - the Law on Concessions 1995. The Constitution guarantees municipalities' ownership and its exercise to the benefit of the relevant municipality, by virtue of the local self-government principle. It is the Law on Municipal Ownership which regulates the granting of concessions over objects - public municipal property.

4.4.8.1. Concessions over objects which are public state property and over activities for which state monopoly has been established

The Law on Concessions establishes the objects - public state property over which concessions may be granted:

- ores and minerals in connection with relevant extraction,
- the waterfront beach strip,
- the biological, mineral and energy resources of the continental shelf and in the exclusive economic zone, in reference to exploration, development, production, utilization thereof,
- roads-sites of the railway infrastructure, including the land on which they are constructed or which is designed for their construction, ports or technologically detached parts of them for public transport and civil airports, existing and/or such which shall be built by and with the funding of the concessionaire,
- the waters, including mineral waters – sole state property,
- the aquaculture and the water supply facilities and systems, which are public state property,
- the forests and parks of national significance,
- the nuclear facilities,
- the natural and archaeological preserves,
- other objects which are public state property, specified by law.

According to the Law, the following activities on which state monopoly has been established may be subjected to concession:

- usage of nuclear power,
- manufacture of radioactive products, arms, explosives and substances with strong biological activity,

Under the Law, concessions may be granted not only over existing objects - public state property, but also over objects which shall be built and funded by the concessionaire. The procedure for granting concessions includes:

- adoption of a decision to grant a concession by the Council of Ministers upon the corresponding minister's proposal,
- a competition or tender organized and carried out by a minister appointed in the above decision,
- assignment of the concessionaire,
- conclusion of a concession agreement with the concessionaire.

In some cases, envisaged by the law, the concessionaire may be determined without competition or tender. Concessions may be granted for a period up to 35 years. This term can be extended but the total duration of

the concession cannot be longer than 50 years. When the contract has expired, per equal other conditions the concessionaire under the contract has priority for the conclusion of a new concession contract for the same object or activity.

4.4.8.2. Granting concessions over object - public municipal property (regulated by the Law on Municipal Ownership)

Pursuant to the Law on Municipal Ownership “concession” is the grant of a particular right to use an object, which is public municipal property with the purpose of permanently satisfying the public needs of municipal importance, and allowing that the activities be conducted by the municipality.

The objects over which concessions may be granted include:

- water resources (including mineral waters) used solely for municipal needs,
- municipal water basins and beaches thereto,
- inert and other materials necessary for meeting the populations demand and extracted by a quarry method in volume not bigger than 10000 c.m. per year,
- local roads and parking lots,
- municipal forests.

The activities for which a concession may be granted by a municipality are specified as:

- water supply and sewerage,
- activities involving transport infrastructure and transportation of passengers,
- business conducted in objects which are public municipal property.

The procedure for granting concessions includes the following steps:

- adoption of a decision to grant a concession by the Municipal Council,
- carrying out of a competition or tender,
- concluding the concession contract.

Concession may be granted for a period of up to 15 years. However, the term can be extended. The total duration of the concession may not be longer than 25 years.

4.4.9.Licensing of the Telecommunication Activities

The Law on Telecommunications, adopted in August 1998, specifies the regulations concerning the regime of the telecommunications. The Law aims at liberalizing the telecommunication services, setting up the free market therefore and preventing the unfair competition. It provides for an equal treatment of the operators.

Under the Law, telecommunications are considered the following: transfer, transmission or acceptance of all kinds of signs, signals, written words, pictures, sounds or information by the means of a conductor, radio waves, optical or other electromagnetic surroundings.

The telecommunication activity is the performance of telecommunications through establishment, maintenance and utilization of telecommunication networks and/or delivery of telecommunication services.

The telecommunication operators provide telecommunication services on the grounds of licensing or free.

Pursuant to the Law "license" is considered as the permission for utilizing the radio frequency spectrum, for activities on performing telecommunication services as well as for radio and television activities.

The activities on performing telecommunication services will be realized after licensing with individual licenses, general license or free.

The radio and television activities are performed only after individual licensing is given.

The individual licenses are personal. They can be issued without competition or tender, when their object is an unlimited resource. The individual license may be issued for a period of up to 20 years. This term can be extended but the total duration of the individual license cannot exceed 35 years.

The general license shall be promulgated in the State Gazette. Every person may perform activity in telecommunications under a general license after registering by the State Commission on Telecommunications.

The Government approves the issuing of licenses for establishment of telecommunication networks and delivery of public telecommunication services by using the radio frequency spectrum upon a proposal made by the Commission on Telecommunications.

The Council of Ministers approves a National plan for assignment of radio frequencies upon a proposal made by the Council on the National Radio Frequency Spectrum.

The State Commission on Telecommunications permits:

- the import of transmission radio facilities for civil purposes,
- the production and/or distribution of transmission radio facilities for civil purposes on the territory of the country,
- the legal competence to radio operators - professionals and amateurs.

4.4.10.Licensing of the activities in energy sector

On 16th July 1999 the new Law on Energy and the Power Efficiency (LEPE) was published in State Gazette No 64. It regulates:

- public relations in the energy sector,
- the rights and obligations of legal entities related to activities in the field of:
 - generation, import, export, transmission, distribution and supply of electric power, heat, and natural gas,
 - improvement of energy efficiency, and promotion of the use of renewable sources of energy.

It cancels some provisions of the Law on Concessions concerning concessions regime in the area mentioned above. Instead of it a license regime is established.

However persons conducting activities in the energy sector on the grounds of a granted license or concession by order of another act retain their rights but they should apply for a license within one year period after the day LEPE has come into force.

State Commission issues the licenses for Energy Regulation (SCER) in case the applicant meets the strict requirements of LEPE. Only by tender an investor is determined for construction of:

- new generation capacities exceeding 25 MW,
- new heat transmission systems,
- new gas distribution networks,
- natural gas storage facilities.

The tender is held by SCER or the respective municipality after the tender documents has been cleared by SCER pursuant to a procedure defined in a special regulation. The tender winner shall be granted:

- a facility construction permit,
- electricity and/or heat generation license if requested.

The tender winner shall receive a contract with the transmission enterprise for sale of the electric power and/or heat to be generated for a term not less than 10 years

4.5 Privatization

Privatisation in Bulgaria started in 1993 using various techniques, such as public offering of shares, public auctions, public competitive bidding by invited tenders, management employee buy-outs, negotiations with potential buyers and central public offering.

The privatization process is carried out under two separate, but associated programs: (a) market (cash) privatization of state and municipal (property) enterprises and (b) voucher privatization.

Within the decentralized privatization model, the Privatization Agency (PA) operates as the main privatization authority for all companies with book value of fixed assets exceeding BGN 1 million. The small scale privatization of state-owned enterprises is managed by the respective principal Ministries, the privatization of municipal property is under the authority of the respective Municipalities, the voucher privatization scheme is executed by the Center for Mass Privatization.

4.5.1. Issues in Mass and Large - Scale Privatizations in Bulgaria

Mass Privatization Program (MPP)

According to the IMF country report (contacted in 2001), **several variants of the Mass Privatization Program (MPP) were debuted through 1993, in response to the insufficient progress with cash privatization.** In 1994, amendments to the Privatization Act were introduced to regulate the use of vouchers and provide the creation of the Center of Mass Privatization (CMP), with the responsibility for carrying out the voucher privatization program. The MPP remained a long time under consideration, and was only launched in 1996. In its design, it was modeled on the Czech variant of voucher privatization, and was prepared with the help of Czech consultants. The Czech and the Bulgarian program differed, however in their scope.

Contrary to the experience in the Czech Republic, **voucher privatization did not become the main privatization channel in Bulgaria**. Registration of vouchers began on January 8, 1996. By June 9, when the registration finally ended, only about 3 million people, or about half of all those eligible, had collected their vouchers. To a large extent, this was due to the fact that Bulgaria's fiscal position was deteriorating continuously, and that the increasingly cash-strapped government was reluctant to forgo an excessive amount of potential revenue from privatization receipts. During the first wave of privatization (June 20, 1996 to February 21, 1997), vouchers amounting to 75 billion leva was issued. The bulk of them (81%) were invested in privatization funds, participating in central auctions organized to sell approximately a sixth of the Long -Term Assets (LTA) of state enterprises. Privatization funds were eligible to buy up to a third of the shares in any given company, a strategic stake under Bulgarian corporate law. By end 1997, 14% of the Long Term Assets (LTA) have been transferred to the private sector through mass privatization.

The second wave of mass privatization was launched in early 1999, and is now well underway. More than a million Bulgarians have participated, and the Center Mass Privatization (CMP) has organized 14 public tenders since the beginning of 1999. Some 12.5 million shares from 547 companies were put up for sale at these tenders, with an average of 54% bought. The government intends to use this second wave to sell a large number of SMEs and to dispose of residual shares owned by the state. It will also use it to launch private pension funds. Finally the second wave could have a positive effect on the stock exchange. The impact on the pace of privatization is difficult to quantify, however, as there is no clearly defined list of assets available for mass privatization. Moreover, the take up rate by eligible citizens is not known in advance, and vouchers are also issued in conjunction with land or commercial property restitution.

Large Enterprise Privatization

Large-Scale Privatization (LSP), carried out by the Privatization Agency (PA), has proceed mainly through negotiation with potential buyers. The other methods stipulated in the Privatization Act (auctions and tenders, differ offer of **Management Employee Buy Outs—MEBOs**) were only marginally used. Privatization intermediaries were appointed to find buyers for about 13% of enterprises. However, the recent amendments to the Privatization Law led to a change in management of the PA. In December 2000, the new director announced that from then on other methods, including auctions and tenders, would be more widely used, in line with the new privatization strategy.

Management Employee Buy Outs (MEBOs) and local investors were the main buyers, with only a relatively small share of large enterprises acquire by foreign strategic investors. Foreign investors however paid an average price more than three times higher than local investors and five times higher than MEBOs. In terms of privatization proceeds, foreign investor participation was thus much larger than implied by the small number of deals concluded.

Investment commitments and employment arrangements were incorporated in nearly 90% of PA deals, and obligations to pay off debt provisions in one third of the cases. Such non-cash provisions in the privatization contracts allow the PA to monitor and intervene in post-privatization corporate management, up to five years, following the execution of the deal. The PA, for example, cancel a privatization contract with a buyer due to non fulfillment of non cash provisions. These arrangements can potentially slow the restructuring process, as many privatized companies seek to amend them in the post privatization period.

The substantial increase in the share of privately owned enterprises brought about by the renewed privatizations efforts since 1997 is having a positive impact on firm performance. As a result of the strategy to accelerate privatization, Bulgaria has largely caught up in terms of private sector share in GDP with the other EU accession candidates, except the most advanced ones. The shift to private ownership is overall having a beneficial effect. In line with the findings for other transition countries, studies using firm level panel data from a large sample of Bulgarian enterprises show that introducing private ownership improves productivity. In particular, privatizing a fully state-owned enterprise to domestic investors is found to raise total factor productivity by on average 29%.

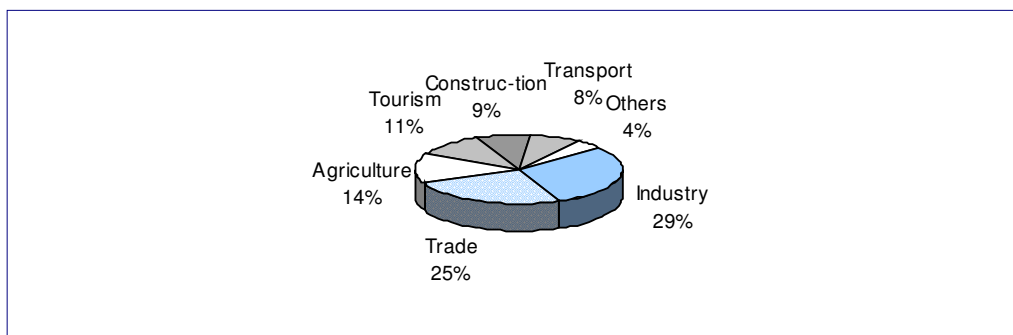
The beneficial effects from privatization in Bulgaria fall short of their potential, however, as in some sectors the market environment is not fully competitive, and in a range of enterprises corporate governance is not exercised properly. In some sectors competitive pressure, as measured by product market concentration, has not yet reached the level needed to have private ownership induce better firm performance. Similarly, corporate governance remains generally weak, in particular in enterprises that have been privatized through the mass privatization program or Management Employee Buyouts (MEBOs). Such enterprises comprise a significant part of Bulgaria's private sector, reflecting the nature of the country's privatization program as it mentioned above.

Recent survey data show that restructuring in enterprises privatized through MEBOs has lagged that the enterprises acquired by domestic and foreign strategic investors, and in some cases significant asset stripping has taken place. These survey data also show that nearly all the enterprises privatized through MEBOs have retained the same management team and that they rank behind domestic and foreign strategic investors in terms of average investment commitments. Governance problems have also arisen in enterprises privatized through the mass privatization program. The bulk of the vouchers issued during the first wave of the program have been collected by investment funds which have built up substantial shareholder positions in a range of enterprises. However, the control exercised by these investment funds is limited, which is reflected in the low valuation of their share relative to the annual earnings of the underlying portfolio. Investments funds and other external shareholders face considerable difficulties in removing inefficient managers. The market managers often have the support from other stakeholders in the enterprise, including labor unions and local authorities.

4.5.2. Cash Privatization

The structure by sectors of privatisation deals, in the period 1993 - 2000, is presented in the following figure.

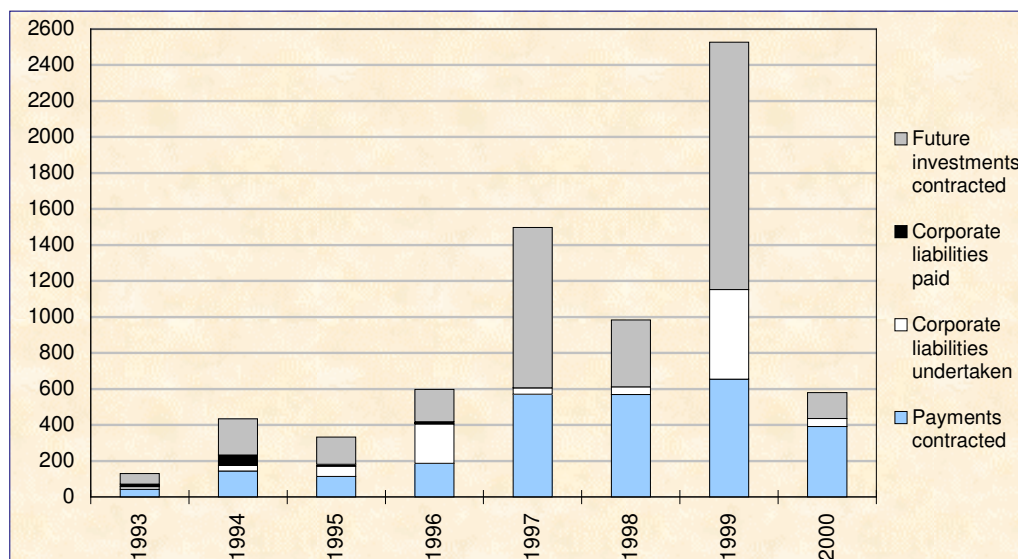
Figure 4. Structure of privatization deals by sectors (from 1993–2000)



Source: Bulgarian Foreign Investment Agency (<http://www.bfia.org>)

Some 76% of the state assets for privatization were sold in the period 1993 - 2000. The financial effect from all privatization transactions concluded in the country in the period 1993 - 2000 is presented in following figure.

Figure 5. Financial effects from all privatization deals for 1993-2000, (in USD mill)



Source: Privatisation Agency of Bulgaria (<http://www.privatization.online.org>)

In 1999, the number of privatization transactions concluded by all state bodies was 1.215. In 2000 this number was 379. The larger share of these were concluded by the Ministries (81%), and the rest by the Privatization Agency (19%). Shares of 240 companies, as well as 139 autonomous units were sold. The total number of management-employee buy-outs was 149 (41% of all transactions). Foreign buyers acquired nine companies. Some of the largest privatisation deals concluded in 2000 are presented in the following figure.

Table15. Largest privatization deals in Bulgaria for the year 2000

Name of Investor	Enterprise Name	Share bought (%)	Price (USD mil)	Future Investment (USD mil)
Consortium Unicredito Italiano - Allianz	Bulbank AD	93	324	N/A
Consortium Zlatni AD, C&N Turistic, Agrima AD	Golden Sands AD	76	96	N/A
Elpharma AD	Sopharma AD	67	24	7.5
Mecamidi - Sofia OOD	Pirinska Bistrica	100	15	0.7
MEC KCM - 2000	KCM AD	80	14.7	8
Commerce Trust	Serdikom AD	53	11	5
Tourist invest AG	Pamporovo AD	60	11	2.4
Sody Solvay AD	TEZ Devnia AD	77	5	10
Samokov - Borovets	Borosport AD	60	5	2
MEC Zahar invest	Zaharni Zavodi AD	60	4.8	5.5

Source: Privatisation Agency of Bulgaria (<http://www.privatization.online.org>)

With regards to the banking sector, a consortium led by the Italian Unicredito bought 93% of Bulbank, the largest Bulgarian bank in terms of assets. With the expected privatization of Biochim, the privatization in the banking sector will be completed as envisaged by the Bulgarian government's Program "Bulgaria 2001". In addition, some 20% of the shares of Bank DSK EAD are expected to be privatized by the end of 2001. A consolidation wave in the sector is anticipated, thus decreasing the number of banks.

The privatization in the insurance sector started in 1999. The Bulgarian company TBI bought 31% of the shares of Bulstrad, the second largest Bulgarian insurance company. The privatization of the largest

insurance company in the country, DZI EAD, is planned for the first half of 2001. Thus, the privatization in the insurance sector will be completed.

Privatization in the energy sector is gaining momentum. Twenty two (22) Hydroelectric Power Plants (HPPs), parts of the National Electric Company EAD (NEK), have been offered for sale. The successful privatization of one of them was assisted by KPMG Bulgaria. The privatization of another 42 HPPs (most with a capacity of up to 5 MW), autonomous parts of NEC, is expected to start soon.

Another method deemed by the government to spur privatization is the sale of shares from the capital of companies on the Bulgarian Stock Exchange. This method of privatization, however, has not gained popularity due to frequent changes in legislation. So far shares from 53 companies (including 16 minority stakes) have been sold on BSE.

4.5.3.Forthcoming privatization deals

The major privatization deals, launched in 2000 and expected to be finalized in 2001 are:

- Biochim AD - the fourth largest Bulgarian bank in terms of assets. The offers of the bidders are to be submitted by 24 January 2001.
- DZI EAD - the largest Bulgarian insurance company. The deadline for submitting offers is 5 February 2001.
- Hemus Air AD - the national air carrier for some destinations. The deadline for bidding for 51% of its shares is 12 February 2001.
- Forty two hydroelectric power plants. The privatization procedure started in late 2000.
- Navigation Maritime Bulgaria - the national sea shipping company. The privatization procedure started in late 2000.
- Bulgarian River Shipping Company. The privatization procedure started in late 2000.

4.5.4.Privatization program of 2001

The objective of the Privatization program in the year 2001 is to complete the privatization in the industry, construction, transport, agriculture and services sectors and to speed up the privatization of the energy, water supply and sewerage systems and the big state monopolists

New privatization procedure for the sale of 51% of the **Bulgarian Telecommunication Company** is expected to be launched by the end of 2001, after the termination of the negotiations between the government and **the consortium of the Dutch KPN and the Greek OTE**.

The privatization of Bulgartabak AD, one of the largest tobacco companies in Eastern Europe, is expected to take place by the end of 2001. A new privatization strategy will first be elaborated, before launching the privatization procedure.

The Bulgarian government initiated some major changes in the privatization process in order to increase its transparency and effectiveness. These changes are expected to result in:

- decrease of the preferences of the management-employee companies (MEC),
- increased involvement and control of the Parliament,

- management changes in the Privatization Agency (PA).

4.5.5. Privatization legislation

The Bulgarian government provides incentives for domestic and foreign investors mainly through the variety of payment instruments. Up to 50% of the negotiated price of any state-owned company put up for privatization can be paid for by the use of external (Brady bonds) or internal (ZUNK bonds) state debt instruments, as well as through compensatory notes since the end of 1998. The effective reduction in price is provided up-front which is more attractive to investors compared to the future benefits of a profit tax holiday.

As a result of the adopted new privatization strategy, the privatization legislation underwent a number of major amendments in 2000. The most important ones stipulate that:

- The Council of Ministers will become a privatization body which will take the decisions and conclude the contracts for the privatization of the companies, included in the list to be approved by the Parliament.
- The Council of Ministers will elaborate strategies for the privatization of the big state-owned monopolists and for the companies from the infrastructure sector. These privatization strategies will be approved by the Parliament.
- The Executive Director of the PA will be replaced by an Executive Board, consisting of one Director and two Deputy Directors. The Executive Board will be appointed by the Council of Ministers.
- The powers of the Supervisory Board of the PA, whose members will be elected by the Parliament, will be increased. It will become responsible for the post-privatization control of the privatization deals, concluded by all privatization bodies.
- A new privatization method - acceptance of public tender offer for share purchase - is adopted (in relation to article 149 of the Law for public offering of securities).
- The Center for Mass Privatization will start to organize public tenders, along with the centralized tenders.
- Privatization authorities are obliged to evaluate objectively MEC offers against those of strategic investors. The price offered by MEC will be discounted at 25%, instead of 10%.
- The initial payment of MEC, upon concluding privatization contracts, increased from 10% to 25% of the whole price. The term for the final payment of the price by MEC decreased from 10 to 5 years. The one year grace period for MEC is to be abolished.
- The Council of Ministers will enact a Regulation for the negotiations with potential buyers privatization method.
- The deadline for MEC to pay with compensatory notes is extended to 31 December 2001.

The formulation of privatization policy has been assisted by the foreign investors' suggestions and recommendations. Most of their concerns were associated with the frequently changing tax policy, the lack of legislation clarity and other difficulties. Some of their recommendations include tax reductions, public debates on tax policy, administration efficiency improvement and privatisation acceleration, including the Bulgarian Stock Exchange.

4.5.6. Voucher privatization

In 1996, the government adopted an ambitious voucher privatization program where more than 1.000 companies were offered for sale to the Bulgarian citizens. The first wave of voucher privatization ended in July 1997. Approximately 21.1% of all state assets were privatized.

The second wave is currently in progress. It is expected that the majority of stake owners in the already privatized companies will express interest in acquiring the remaining minority stake packages. Individuals are eligible to participate in the tenders individually or by authorizing an investment intermediary. The deadlines for registration of vouchers expire at the end of 2001. So far 14 tenders have been held and shares from 547 companies have been offered for privatization. In 2001, shares amounting to BGN 1.2 million will be offered for privatization. The objective of the government is to divest of its remaining shares in newly privatized companies.

4.5.7. Restitution

In parallel with the privatization process, the property restitution was launched. It aims at returning expropriated land, including agricultural land, forests, urban property, factories and workshops to former owners.

According to government estimates, some 90% of the land and almost all urban property subject to restitution have been returned to its former owners. The restitution of forests, is under way (56% have been returned to their owners so far).

In cases when property cannot be returned in real terms to its owners, the latter are redeemed with compensatory notes which are recognized as a legal payment instrument in cash privatization.

The recent amendments in the privatization legislation increased the attractiveness of the compensatory notes as instruments of payments in the privatization process by:

- Giving the Management Employee Companies (MEC), which had become owners of privatized companies before 1 February 2000, the right to pay the whole price of the deal through compensatory notes by 31 December 2001.
- Including the tenants and landlords, who had concluded contracts for rent separate parts before 15 October 1993, in the range of persons having right to use compensatory notes as instrument of payment.

4.5.8. Restructuring

A Government Council for supervision of financial discipline and fiscal risks was established in late 1999 to oversee a group of 154 companies with a 50% or more state - ownership. The list of these companies was prepared to meet the requirements of the World Bank with regards to the second loan for restructuring of the real and financial sector, FESAL 2, amounting to USD 100 million. The list included large state companies like Bulgarian Posts, the Water and Sewerage companies, ports, airports and some mines.

In 2000, the restructuring of some of the companies, included in the above mentioned group, effectively started:

- The Sofia Water and Sewerage Company formed a **joint-venture company with the British International Water**. The latter was granted a 25 year concession and will invest \$152 million for a nine year period. The granting of concessions for the Water and Sewerage companies of Varna, Shumen, Dobrich and Bourgas is expected in 2001.

- The Varna Shipbuilding Yard rehabilitation plan, proposed by the British Cammell Laird, was approved by the Varna district court. The plan includes the commitment of Cammell Laird to invest between \$5 and \$10 million and to pay outstanding debts, amounting to \$14 million.

In conclusion it is important to note that the execution of the Government's programme "Bulgaria 2001" is intended to complete the restructuring process in the Bulgarian economy and to create premises for stable economic growth.

4.6. Company law and business organizations in Bulgaria

4.6.1. Forms of Business Organizations

The following forms of business organization exist under the Bulgarian law:

- an unlimited (general) partnership,
- a limited partnership,
- a partnership limited by shares,
- a limited liability company,
- a joint-stock company,
- a public company,
- a sole trader,
- **a joint venture,**
- a branch,
- a holding,
- a co-operative,
- a representative office.

The forms of business organization - representative offices and co-operatives - are governed by the **Commerce Act 1991**, as for certain types of companies (e.g., banks, insurance companies, public companies) special rules apply. Representative offices and co-operatives are regulated respectively by the **Foreign Investments Act 1997** and by the **Co-operatives Act 1999**.

The most appropriate types of companies for conducting business in Bulgaria are the limited liability and the joint-stock company, including the form of a single-member company. These types of companies must be entered into the commercial register of the relevant district court.

LIMITED LIABILITY COMPANY (OOD), is a commercial company, the capital of which is formed by the quotas (sometimes referred to as shares) of its members (shareholders). The liability of a member is limited to the amount of the capital the member has subscribed. A limited liability company is founded or owned by one or more persons, including foreign natural or legal persons. The minimum authorized capital is BGN

5,000. Each share must be with a value of at least BGN 10, as any higher value must be divisible by 100. At least 70% of the capital must be paid up before registration. Contributions to the foundation capital can be paid in cash or in kind. The general meeting of members, which must be held at least once a year, and a manager (or managers), are the statutory bodies of a limited liability company.

A single-member limited liability company (EOOD) is an OOD owned by one person, including a foreign individual or legal entity. The sole owner of an EOOD exercises the powers of both the general meeting and the manager, unless another manager has been appointed to run the company.

OODs must prepare a balance sheet and financial statements each year.

JOINT-STOCK COMPANY (AD) is a company, the capital of which is divided into shares, each of a par value of at least BGN 1. Any higher par value must be determined in whole numbers in BGN. The company is liable to its creditors to the extent of its assets. An AD may be founded or owned by one or more persons, including foreign individuals or legal persons. The minimum capital of an AD is BGN 50.000.

A higher minimum capital is required to establish certain special companies like:

- ❑ **Banks** - BGN 10.000.000.
- ❑ **Insurance companies**
 - BGN 2.000.000 for life insurance and personal accident insurance,
 - BGN 3.000.000 for property insurance,
 - BGN 4.000.000 for reinsurance.
- ❑ **Investment companies** – BGN 500.000.
- ❑ **Voluntary health insurance companies** –BGN 2.000.000 (initially has to be in cash, subsequently can be in kind).
- ❑ **Voluntary pension security companies** –BGN 3.000.000 (paid in cash).

In general, contributions to the foundation capital of an AD may be paid in cash or in kind. At least 25% of the value of each share must be paid up on foundation.

A joint-stock company may issue either registered, bearer or preference shares.

Management bodies of an AD are the general meeting of shareholders, which must be held at least once a year, and a board of directors (one-tier management system) or a general meeting, supervisory board and managing board (two-tier management system).

A single-member joint-stock company (EAD) is an AD owned by one person, including a foreign individual or legal entity, as in this case the sole owner of the capital exercises the powers of the general meeting of shareholders.

ADs must prepare a balance sheet and financial statements each year.

There are some specific additional requirements as to the foundation and running of certain types of company (e.g., banks and insurance companies).

PUBLIC COMPANY – this is a type of joint-stock company initially introduced by the revoked Securities, Stock Exchanges and Investment Companies Act 1995 and regulated by the Public Offering of Securities

Act 1999 (POSA). The events, which trigger the obligation of a company to register as public, are preserved in POSA.

A company must register as public where it makes a primary offering of shares, or its shares are registered for trading on an organized securities market.

Another way to create a public company is through a business combination involving at least one public company - the surviving company will be public, too.

HOLDING COMPANY - a holding company is any joint-stock company, partnership limited by shares or limited liability company. A holding company can hold interest in any form or participate in the management of and control over other companies. As per the Commerce Act control is exercised where the holding company holds at least 25% of the shares or interest in a subsidiary company, or is in a position to appoint, directly or indirectly, more than 1/2 of the board members of the subsidiary.

A holding can conduct its own business, as the activities it can perform or is disallowed to perform are exhaustively enumerated in the Commerce Act.

BRANCH - foreign legal entities registered abroad, as well as foreign individuals or persons other than legal entities, can register a branch in Bulgaria if duly incorporated and entitled to conduct business activities under their national law.

A branch of a foreign person is part of its parent company, but has a different seat. A branch is not a legal entity. However, it must keep account books just like independent legal entities do. The branch of a foreign company has to prepare a balance sheet. No authorized capital is required to found a branch.

REPRESENTATIVE OFFICE - Representative offices can be set up by foreign persons entitled to engage in business activity under their national law. Representative offices are not legal entities and may not engage in economic activities.

JOINT VENTURE - it is a company formed jointly by a Bulgarian and a foreign partner. The extent of the foreign participation in a joint venture is not limited. Joint ventures must take one of the forms of business entities under the Commerce Act. Establishing a joint venture is one of the forms of investing in Bulgaria.

4.6.2. Formation and Registration of a Company, Branch and Representative Office

A company is incorporated as from the date of its registration into the commercial register of the relevant district court. The application for registration, furnished with certain documents required by the law, is filed in the court by the elected managing body.

LIMITED LIABILITY COMPANY - in order to be registered a limited liability company must:

- produce its articles of association (memorandum of association - for single-member limited liability companies),
- have appointed a manager (or managers),
- have paid up at least 70% (BGN 3,500) of its authorized capital, including at least one-third of each member's quota.

This information together with certain details (e.g., the manner of management and representation, the company's seat and head-office address, its business name) is recorded in the commercial register and promulgated in the State Gazette.

JOINT-STOCK COMPANY - to be registered at court a joint-stock company must:

- have adopted its articles of association (memorandum of association – for single-member joint-stock companies),
- have its authorized capital fully subscribed,
- have paid up at least 25% of the value of each share,
- have elected a managing board or respectively a board of directors and a supervisory board,
- have met any other statutory requirements (e.g., banks and insurance companies must submit to the court, apart from the other documents required, the licenses that BNB, respectively the National Insurance Council, have granted to them).

Certain details (e.g., the manner of management and representation, the company's seat and head-office address, its business name) are recorded in the commercial register and promulgated in the State Gazette.

BRANCH - it is entered in the commercial register of the district court on its location. An entry is made on the basis of a written application, furnished with the documents required by law.

REPRESENTATIVE OFFICE - it is registered with the Bulgarian Chamber of Commerce and Industry (BCCI) upon submission of a standard form and a registration card, furnished with the documents required by law. The registration takes from 1 to 3 days.

Once registered, companies, branches and representative offices are subject to registration with the National Statistical Institute, the National Insurance Institute and the tax authorities.

4.6.3. Other Forms of Business Organizations

GENERAL PARTNERSHIPS - it is a company founded by at least two partners for the purpose of engaging in commercial transactions under a joint business name. The partners bear joint and unlimited liability. A foreign person must have permanent residence in Bulgaria in order to participate in a general partnership. There are no requirements for minimum or maximum amount of registered capital.

Each partner may participate in the management of the partnership's business unless the articles of partnership provide otherwise. Each partner is entitled to one vote where the articles of partnership require that certain resolutions should be passed with a majority. A general partnership must be registered with a district court and entered in the commercial register.

LIMITED PARTNERSHIP - it is a company founded by two or more persons for the purpose of engaging in commercial transactions under a joint business name. In a limited partnership there are one or more general partners, bearing unlimited liability, and one or more "limited partners", the liability of which/whom is limited to the extent of their agreed contribution. A foreign person must have permanent residence in Bulgaria in order to participate in a limited partnership as a general partner. The general partners are responsible for managing the partnership. A limited partnership must be registered with a district court and entered in the commercial register.

PARTNERSHIP LIMITED BY SHARES - it is a transitional entity between a joint-stock company and a limited partnership, and shares features of both legal forms. A partnership limited by shares has general partners, who have unlimited liability, and at least three limited partners, the liability of which/whom is limited to the extent of their shareholding. To be able to participate in a partnership limited by shares the foreign general partners must have permanent residence in Bulgaria. The general partners are responsible for managing the business. A partnership limited by shares must be registered with a district court and enter the commercial register.

CO-OPERATIVE SOCIETY - a co-operative is a voluntary society of individuals, with a non-fixed capital and a non-fixed number of members, who carry out economic and other activities to satisfy their interests, by mutual aid and co-operation. A co-operative is a legal entity and is deemed a merchant under the Commerce Act. Just like members of commercial companies, co-operative members must make efforts and contribute to the achievement of the co-operative's goals. Co-operative members can only be individuals, at least 7 in number. To participate in a co-operative, foreign persons should have permanent residence in Bulgaria.

The general meeting of a co-operative consists of all co-operative members. The right to vote at the general meeting may be exercised only in person. Every member is entitled to one vote, irrespective of his or her shares. All members have rights to participate in the business and to share in the profits, etc.

SOLE TRADER - any capable individual, having permanent residence in the country, can register as a sole trader.

STATE COMPANIES - they exist under the forms of one-member limited liability or joint-stock companies where the quotas/shares are solely owned by the State. These forms of business are established either to facilitate the process of privatization of the state companies through the sale of their quotas/shares to private persons, or to conduct certain business activities. Notwithstanding the above, the State can be a member/shareholder in companies, having private participation, subject to certain requirements.

MUNICIPAL COMPANIES – the abovementioned in respect of the State and its fully or partially owned companies is accordingly relevant to the municipalities and their companies.

4.7.Accounting and Auditing

4.7.1. Accounting and Audit Legislation

Accounting and financial reporting is regulated by the Accountancy Act of 1991 (amended in 1992, 1996, 1997, 1998, 1999 and 2000). The accounting principles introduced are in general in accordance with the EU Directive IV and the International Accounting Standards. The Accountancy Act (the Act) establishes requirements for maintaining accounting records and for presentation of the financial information of the enterprises. The Act requirements are applicable for all types of organizations: business enterprises, public sector entities, non-profit organizations, etc. The main sections of the Act relate to:

- accounting principles,
- documentation of the transactions,
- current and closing valuation of assets and liabilities,
- annual financial statements,
- certified public accountants.

In accordance with the Act, all entities should apply "double entry" system of bookkeeping. Very small entities with a number of employees for the preceding year below 10 and total annual income below BGN 75,000 (DEM 75.000) are allowed to choose between "double entry" and "single entry" bookkeeping system.

Some general accounting and financial reporting requirements are also established in the Commercial Act of 1991 (with subsequent amendments). All companies, incorporated under the Commercial Act are required to comply with its requirements relating to the maintenance of proper accounting records and the preparation

and submission of audited accounts for statutory purposes. For specialized industries, other applicable regulations are in force such as the Law on the Bulgarian National Bank, 1997, the Insurance Law, 1996, the Law on Commercial Banks, 1997, the Law on Public Offerings of Securities, 2000.

The Accountancy Act also establishes statutory auditing requirements. Entities subject to a statutory audit are:

- joint stock and public limited companies,
- banks, insurance and other financial institutions,
- entities, which exceed at least two of the following criteria:
 1. reported total assets at the beginning of the reporting period - BGN 300.000,
 2. reported sales and financial income in the preceding year - BGN 600.000, or
 3. number of employees for the preceding year on a full year equivalent basis - 30.

A statutory audit can be performed by a Bulgarian Certified Public Accountant (CPA), member of the Bulgarian Institute of Certified Public Accountants or by a "specialized auditing company", which meets the following criteria:

- is registered as a trade company in accordance with Art.64 par.1 item 1,2,3 of the Commercial Act,
- at least 51 percent of the shares and the voting rights belong to Bulgarian certified public accountants or Bulgarian and another country's certified public accountants.

Only a specialized auditing company, approved by the Central Bank can certify financial statements of banks. Financial statements of insurance companies are to be certified by at least two CPAs, approved by the Insurance Supervisory Directorate of the Ministry of Finance. According to the Act, a National Chart of Accounts, National Accounting Standards (NAS) and National Standards on Auditing (NSA) have been established and approved by the Bulgarian Government. There are thirty-five National Accounting Standards issued. With some exceptions, as described in the following section, the NAS are in compliance with International Accounting Standards (IAS), as issued by the International Accounting Standards Committee (IASC).

Twenty National Standards on Auditing have also been issued and additional four are in the course of preparation. They are all in accordance with International Standards on Auditing (ISA) as issued by the International Federation of Accountants (IFAC).

4.7.2.Accounting Principles

Financial statements are to be prepared under the historical cost convention. The following main **accounting principles** should be followed in accordance with the Accountancy Act:

going concern, accrual basis, matching of income and expenses, substance over form, true and fair view, materiality, prudence, historic cost, separate reporting periods, matching of closing and opening balance sheets, documentary evidence, consistency.

The above principles are in substantial compliance with the principles and requirements of the IAS. However, through further regulations, as set by the Act and NAS, some of the accounting principles are modified or limited in implementation. As a result, in certain cases, the applicable accounting rules are not consistent with the internationally accepted accounting principles. Examples of such exemptions are:

Provisions for bad debts can be charged up to 50 percent of the original amount of a receivable previously recognized as income, and only if certain conditions are met, i.e. the debt is proved to be irrecoverable, a 100 percent provision can be charged. A debt is considered to be irrecoverable if: (a) the debtor is declared insolvent or in liquidation or (b) insolvency procedures have ceased, but the debt will not be recovered. Provisions for other types of assets are not allowed.

Investments in subsidiaries that are included in the consolidated financial statements should be included in the parent's own financial statements at cost or revalued amounts under the parent's accounting policy for long-term investments (NAS 25 Accounting of Investments). Equity method of recording of investments in the parent's own financial statements is not allowed.

In accordance with NAS 28 Investments in Associates, significant influence is defined as a holding of 25% or more of the shares of the enterprise which differs from IAS 28 definition.

Investments in associated companies are measured initially at cost and carried thereafter at fair value, equity method of recording of such investments in investor's own financial statements is not allowed.

In accordance with NAS 28 Investments in Associates, associates, which have a material effect for the true and fair presentation of the financial statements of the group, may be consolidated by applying proportionate consolidation method, which differs from the IAS 28 requirements.

4.7.3.Valuation of the Balance Sheet Items

Generally, the historical cost accounting convention is dominant. Assets and liabilities are normally valued at the amount at which they were historically acquired or incurred.

Fixed assets are valued at the acquisition cost less accumulated depreciation. The acquisition cost comprises purchase price, transportation, handling and any other costs related to the specific asset's delivery and preparation for use. Depreciation is calculated consistently, based on the useful life of the asset, as assessed by the management. Depreciation rates allowable for income tax purposes are established by the Corporation Tax Law.

Depreciation is not charged for land and forests, as well as for fully depreciated tangible and intangible fixed assets.

Fixed assets are subject to year-end revaluation. Land and forests are revalued at fair market value. Plant, equipment, vehicles and furniture are revalued by applying specific price index by group of assets, published by the National Statistical Institute. An increase of the fair value of a fixed asset is reported as revaluation reserve. Any subsequent decrease of the fair value is taken from the revaluation reserve unless it exceeds the revaluation surplus in which case it is charged as other expenses. The whole revaluation reserve for an asset should be released to retained earnings upon retirement/disposal of the asset.

Stocks are valued at the lower of cost and fair value. Fair value is defined as an exchange price, market price or realizable value. The revaluation is allowed only at the year-end and the revaluation loss is recognized in the income statement. The **cost of the stocks is assigned through FIFO, weighted average, LIFO** or specific cost formulas for identified supplies.

Receivables are valued at the original transaction amount less any provision for doubtful, bad and irrecoverable amounts. Such provision shall not exceeds 20 percent for doubtful debts (aging between 90 and 180 days), 50 percent for bad debts (aging more than 180 days) and 100 percent for irrecoverable debts.

Current investments are valued at market price. Revaluation is effected on a monthly basis.

Long term investments are measured initially at cost and carried thereafter at fair value. Revaluation is effected as at the balance sheet date. When a revaluation gives rise to a value uplift, it should be credited to the revaluation reserve unless it represents a reversal of a revaluation decrease of the same asset previously recognized as an expense, in which case it should be recognized as income. Any subsequent decrease of the fair value of such investment is taken from the revaluation reserve unless it exceeds the revaluation surplus in which case it is charged as financial expense.

Foreign currency monetary assets and liabilities are valued at the historical exchange rate at the date of transaction. At the end of each month, such items should be revalued at the closing exchange rate, as established by the Bulgarian National Bank. The effect of such revaluation is recognized as foreign currency exchange gain or loss for the current period.

Share capital is valued at its registered total amount. Receivables on subscribed shares are stated as an asset or as a negative amount in the equity section.

Hyperinflation restatements of the balance sheet and income statement is required by the NAS 29 in case the cumulative inflation index for three consecutive years is 100% or more. The financial statements adjusted for hyperinflation are recognized as the official financial statements.

4.7.4. Annual Financial Statements

Financial year for all reporting organizations is the calendar year. The financial statements should be prepared in Bulgarian Levs and in Bulgarian language.

The purpose of the financial statements as described in the Act is to provide true and fair presentation of the financial position, financial results and cash flows of the enterprise. Annual financial statements include:

- Balance Sheet,**
- Income Statement,**
- Cash Flow Statement,**
- Statement of Changes in Equity, and**
- Notes to the financial statements and disclosure of accounting policies.**

The Act and NAS prescribe the format of the financial statements. However, enterprises are free to add items to the standard financial statements where it would result in better presentation of the financial information. The financial statements are due to be prepared by February 15 and presented to the state authorities (National Statistical Institute and Tax Authorities) by March 31 of the year following the balance sheet date of the reporting year. All companies, subject to annual audit are required to publish their financial statements in a daily or in a specialized economic or finance edition by the end of May and submit them to the Bulgarian Chamber of Commerce by the end of June of the following year. Consolidated financial statements should be prepared by June 15 and published not later than June 30 of the following year. Banks, insurance companies and branches of foreign financial institutions **should publish their financial statements in the State Gazette.**

4.8. Taxation

4.8.1. Direct Tax: Individuals

Territoriality and residence

Under Personal Income Tax Act (PITA) tax liable persons are individuals - residents and non-residents, and corporate explicitly enumerated therein.

Residents, irrespective of their citizenship, are considered those persons: who have their permanent domicile in Bulgaria, who reside in the country for more than 183 days in a 365-day period, and non-residents are considered those individuals who do not fit the above criteria for residents.

Residents are liable for their world-wide income. Non-residents are liable only for their income derived from Bulgarian sources. Foreign experts are taxed only on their Bulgarian-source income irrespective of the duration of their stay in the country.

Bulgarian source incomes

Any income derived by an individual from the conduct of business on the territory of Bulgaria is considered to be from a Bulgarian source. A person is considered to have carried out business on the territory of the country where:

- He has a permanent establishment¹ or a fixed base² in Bulgaria,
- He has assigned or performed an assignment on the territory of the country, whether in person or through a procurator, agent or in some other way.

Any income under an employment contract or derived from rendering services is considered to have been derived from a Bulgarian source where labour has been extended or services have been delivered on the territory of the country, regardless of the source of payment for the labour extended or services rendered.

Notwithstanding the above, some kinds of incomes paid out by Bulgarian residents or from a permanent establishment to a non-resident on the territory of the country are considered to be from a Bulgarian source. These incomes include, for example, dividends and distribution of profits of entities with or without legal presence, interest, royalties, rentals, payments under lease, franchising, factoring, as well as emoluments of freelancers, or members of a managing or controlling body of a Bulgarian corporate: branch of a foreign entity, etc.

Incomes derived from the use of real estate and capital gains from the sale of real estate located in the country, as well as incomes from transactions with quotas/shares in local companies and incomes from securities transactions are also incomes from a Bulgarian source.

Tax Exempt income

Tax exempt are considered:

1 For the purposes of PITA a "permanent establishment" means specific premises through which a foreign enterprise conducts, partly or wholly, its business in Bulgaria. The premises may include: a place of management, a branch, an office, a studio, a bureau, a plant, a factory, a workshop, a shop, a warehouse wherein trade is conducted, an installation, a construction site, a mine, an oil or gas well, a quarry or any other place of extraction of natural resources. A "permanent establishment" will also be the conduct of a business through a procurator or an agent entitled to conclude contracts on behalf of the foreign person.

2 A "fixed base" means specific premises through which a foreign individual renders, partly or wholly, independent services or acts as a member of the professions (e.g. a law firm; an independent auditor or accountant).

- incomes derived from the sale or exchange of certain types of immovable property (flats, houses or villas) or means of transport, subject to certain conditions,
- incomes derived from the sale or exchange of movable property except for the means of transport as per the preceding bullet, as well as the sale of shares, quotas and other equity interest in a commercial company, etc.,
- compensations received as a result of statutory pension, health and social security and/or insurance, as well as other certain compensations,
- interest accrued on deposits in local commercial banks and branches of foreign banks, as well as the interest and expenses on court-awarded claims,
- cash and non-cash income from social financial aid and the unemployment compensations and subsidies,
- the financial aid granted by social funds and organisations,
- subsidies from the state in respect of children and payments determined by court to support a child,
- student grants for Bulgarian nationals for their education abroad,
- prizes from the lottery,
- salaries and emolument of foreign diplomats pursuant to the Vienna Convention on Diplomatic Relations,
- company profits distributed as new quotas and shares in commercial companies, as well as the profits distributed as an increase in existing quotas and shares' per value,
- rentals from agricultural land.

Incomes, not specified by PITA as tax exempt, are considered taxable.

Taxable base

The annual taxable base is the sum of all taxable incomes received, deducted by:

- incomes taxed with a final tax,
- mandatory and voluntary national insurance, pension, health insurance, unemployment fund contributions,
- statutory deductions applicable only to non-employment contracts (e.g. 35% of the gross income for services contracts, 25% for management fees) relieves for donations not exceeding 5% of the taxable income after other statutory deductions have been made – not applicable to employment income.

There are no tax deductions related to personal allowances for spouses and dependants. The loss carry forward facility is not applicable for individuals.

Annual scale

In principle, the total annual income, after the respective adjustments are made, is taxed in accordance with an annual progressive scale. The annual scale in force as from 1 January 2001 is given below.

Table 16. Annual Income Taxed (in BGN)

Annual income (in BGN)	TAX
up to BGN 1.200	non-taxable
from BGN 1.200 to BGN 1.620	20% on the excess over BGN 1.200
from BGN 1.620 to BGN 4.800	BGN 84 + 26% of the excess over BGN 1.620
from BGN 4.800 to BGN 16.800	BGN 910.80 + 32% of the excess over BGN 4.800
over BGN 16.800	BGN 4.750.80 + 38% of the excess over BGN 16.800

Source: Privatisation Agency of Bulgaria (<http://www.privatization.online.org>)

Specific rules relevant to taxation of different types of income

Employment income: Incomes from employment consist of all payments, including fringe benefits in cash or in kind, paid out by the employer or at its expense to the tax liable person during the calendar month.

Non-taxable are:

- the value of free of charge prophylactic foodstuffs, antidotes and personal safety guards pursuant to the Labour Code and other statutory instruments,
- the value of the special working clothes, the free of charge working or representing clothes and uniforms which are provided under the Labour Code or other acts (e.g., those provided to state servants),
- certain compensations under the Labour Code (e.g. business travel compensations, reassignment compensations, etc.),
- the value of travel cards provided by the employer to the employee free of charge,
- social expenditures incurred by the employer and taxed under the Corporate Income Taxation Act (fringe benefits distributed as social expenses).

The tax base of incomes, derived under employment relationships and relationships that are equalized to them, is formed by deducting the taxable income with the installments made for social, health, pension and other insurance the employee is bound to make by virtue of law. The taxable income is reduced with the sums paid for voluntary social, pension and health security.

Incomes derived under an employment contract are taxed on a monthly basis and the annual tax obligation is subject to adjustment on an annual basis, to which the annual progressive scale applies.

The employment income is taxed on a monthly basis in accordance with a progressive scale. The scale applicable as from 1 January 2001 is given below.

Table 17. Monthly Employment Income Taxed (in BGN)

Monthly Income (in BGN)	Tax
up to BGN 100	non-taxable
from BGN 100 to BGN 135	20% on the excess over BGN 100
from BGN 135 to BGN 400	BGN 7 + 26% on the excess over BGN 135
from BGN 400 to BGN 1,400	BGN 75.90 + 32% on the excess over BGN 400
over BGN 1.400	BGN 395.90 + 38% on the excess over BGN 1.400

Source: Privatisation Agency of Bulgaria (<http://www.privatization.online.org>)

Capital Gains: The tax base in case of sale or exchange of immovable and movable property is the difference between the selling price and the higher price between the factual and updated price paid for the acquisition of such property. This rule applies to certain types of vehicles (e.g. aircraft, sea vessels, and

cars). For any other type of movable property the tax base is the difference between the selling price and the re-valued price for the acquisition of such property.

Income Received by Civil Contractors and Freelancers: a 15 % advance tax payment is due upon payment and the final tax obligation is assessed and paid annually. Mandatory and voluntary social, health and pension contributions can be deducted from the taxable income before applying the advance tax. Until 1 January 2001, the contributions were tax deductible on annual basis only. The pre-paid tax is set off against the final annual tax obligation. 35% of the income is tax deductible.

Income Received by Managers and Members of Boards of Directors: Managers and members of Boards of Directors who work under civil contracts are obliged to pay personal income tax on an annual basis. 15% of the tax payable is withheld at the moment of payment as an advance tax payment. Mandatory and voluntary social, health and pension contributions can be deducted from the taxable income before applying the advance tax. Until 1 January 2001, the contributions were tax deductible on annual basis only. The pre-paid tax is set off against the final annual tax obligation. 25% of the income is tax-deductible.

Income Received by Sole Traders: The base for taxation is determined under the rules of the Corporate Income Tax Act. Advance payments of tax are made as per the rules of the same Act. The annual tax is paid in accordance with the annual progressive scale.

Rental Income Received: Personal income tax is due on an annual basis 20% of the income is tax deductible. If the real estate and/or the movable property are owned by more than one person, the income is divided in proportion to the participation in the ownership. If the rent is payable to a non-Bulgarian tax resident, a 15% withholding tax is levied.

Incomes of individuals and businesses carrying out certain activities enumerated in the PITA, whose annual turnover for the preceding year has been up to BGN 75.000, are taxed with a final patent tax. The patent tax is levied as annual lump sum, which depends on the nature of the activities and other criteria, established by the law.

Royalty payments and technical services fees, when paid to non-Bulgarian tax residents, are subject to a 15% withholding tax at the source (the paying company or partnership). No additional tax is levied. Fees for management services are not considered technical services fees and are not subject to withholding tax.

Dividends (including any distributed profit from companies or partnerships) are taxed by 15% at the source (the paying company or partnership) which is the final tax on this kind of income. Stock dividends are not taxable.

Payments under lease, factoring and franchising contracts are subject to 20% final tax on the excess over BGN 100.

Interest payments except for those defined as non-taxable, are subject to 20% final tax on the excess over BGN 100.

Other income, e.g. income from occasional transactions is taxed with 20% final tax on the excess over BGN 100. Income in the form of compensations from voluntary pension, health and social insurance is taxed under the general rules.

Tax credits

Tax credits may be granted on the basis of double taxation treaties in force. If there is no double tax treaty in place PITA provides for unilateral tax credit to be granted to Bulgarian tax residents for the taxes paid abroad. Tax credit is assessed on a per-country limitation basis and is limited to the amount of the Bulgarian tax, which would be paid on the foreign source income.

□ **Tax administration**

Returns: Persons who during the tax year have received income only from: employment, and/or, rentals from agricultural land, and/or, certain compensations taxed at their payment are not obliged to submit tax returns. Other tax payers submit annual tax returns by 15 April of the year following the respective tax year. For tax purposes, spouses are treated as separate taxpayers.

No income splitting is allowed. The standard form of the tax returns is promulgated in the State Gazette and is available on Internet.

Payment of Tax: Personal income tax on employment income is withheld from the gross remuneration on a monthly basis by the employer. The employer acts as an agent of the Revenue authorities and transfers the tax to the budget. Tax payers who are not employees in certain cases pay advance tax, either regularly (sole traders), or whenever income is received.

□ **Social security, unemployment fund and health care contributions**

In general, employers are obliged to pay social security contributions at a 26.3% rate, and employees at a 6.4% rate.

Unemployment fund contributions are payable by the employer at a 4% rate, where 3.2% is for the account of the employer and 0.8% is for the employee's account.

Health care contributions at a 4.8% rate will be due by the employer and another 1.2% by the employee.

The above contributions shall be calculated on the remuneration and other employment income of the employee for the respective month but on not more than 10-times the minimum salary for the country (which at present amounts to BGN 79).

The expatriates will attract the same payroll costs as Bulgarian employees.

4.8.2. Direct Tax: Corporations

Corporate income tax

Under the Corporate Income Tax Act (CITA) all companies and partnerships (including non-incorporated partnerships) are liable to corporate income tax. For enterprises with taxable profits over BGN 50.000 the corporate income tax rate is 20%, whereas for enterprises with taxable profits up to the above sum the rate is 15%. In addition to the corporate tax there is a municipal tax at 10%, which is deductible from the taxable base for corporate income tax. Thus the aggregate tax rate (including corporate and municipal tax) for annual taxable income up to BGN 50.000 is 23.5%, whereas for income above that amount, the aggregate tax rate is 28%.

Bulgarian resident entities are taxed on a world-wide basis. Other entities are taxed on their Bulgarian-source income. Non-business organizations (including governmental) are taxed for their business activities.

Specific tax regimes

Tax on insurance and re-insurance premiums

Insurance companies pay one-time final tax on insurance premiums and on any other kind of income and are not obliged to pay corporate income taxes separately for their activities other than insurance or re-insurance.

The tax base is the sum of all insurance premiums and any other income (even if not related to insurance) within a given month, reduced by the gross amount of reinsurance premiums and insurance premiums paid out to clients. If the tax base is a negative figure it is deductible from the tax base in the subsequent months.

The rate of the special tax for insurance companies is 7%, except for life insurance companies whose income will be taxed at 2%.

Companies in the gambling business

Companies organizing games of luck such as lotteries, number lotteries, TOTO, LOTTO, Bingo, Keno, betting on sports events and other uncertain events, will be taxed on their income (bets collected) by a final tax, and are not subject to corporate income taxes.

The tax rate for the bets made for the games TOTO, LOTTO and bets made on the outcome of sports matches and other uncertain events, is 8%.

The tax rate for the tax on the tickets for BINGO, KENO, and other lotteries is 12% and so is the rate for the tax on games organized over the phone, the tax base being the increased price of the telephone or the telecommunication connection.

Entities organizing gambling games other than those mentioned above are taxable in accordance with the general rules for corporate income taxation.

Taxation of certain company expenses

Entertainment and representative expenses and business gifts, that do not bear the trademark or the business name of the company, as well as donations and sponsorships, which are not accounted for as expenses, are subject to a final 25% tax. Social expenses representing fringe benefits in kind, as well as expenses for maintenance, repair and exploitation of cars are subject to a final 20% tax.

Property tax

Owners of immovable property are liable to property tax at a rate of 0.15%. For companies the tax base is the net book value of the immovable property plus the accumulated depreciation costs thereon.

Corporate residence

A company is resident in Bulgaria for tax purposes if it is registered in Bulgaria. Companies resident in Bulgaria are subject to tax on their world-wide income. Foreign entities are subject to tax on their Bulgarian-source income, but their Bulgarian branches are considered Bulgarian resident companies for tax purposes.

Branch income

Although branches are not legal persons, branches of non-resident companies have separate balance sheet and profit and loss account. They are subject to corporate income tax at the standard rate of 20% (or respectively at the lower rate of 15%), and to other general taxes too (municipal tax; VAT, etc). Representative offices are not subject to corporate taxation.

4.8.2.1. Income determination

The income determination is based on the taxpayers' profit and loss account.

Inventory valuation

Any of the following methods is acceptable for inventory valuation: FIFO, LIFO, weighted-average cost, or specific identification of items of inventory.

Inventories at the end of the year are to be valued at the lower of their market or book value at the balance sheet date. The difference, which is not tax deductible, is to be recorded as "other expenses."

Capital gains

Capital gains are included in the corporate income and taxed at the full corporate tax rate. Exchange rate gains and losses are reported in the balance sheet and reflected in the assessment of the taxable profit.

Dividends

Dividends received by local companies are not subject to withholding tax. Dividends payable by local companies to Bulgarian resident individuals and certain types of charity institutions, defined by CITA, are taxed with 15% withholding tax. Dividends distributed by Bulgarian companies to foreign shareholders are subject to 15% withholding tax.

Stock dividends

Dividends capitalized into shares (stock dividends) are not subject to withholding tax.

Foreign income

Income derived outside Bulgaria by resident entities and branches of non-residents is included in the taxable base for corporate income tax purposes. Resident entities utilize tax credit for the foreign source income, which is taxed abroad. The tax credit is limited to the amount of the Bulgarian tax obligation, which would have been levied if the profit or income had originated from Bulgaria.

Where Bulgaria has a double tax treaty with the state where the income originates from, the provisions of the double tax treaty shall apply. Undistributed income of foreign subsidiaries of a Bulgarian resident company is not taxed.

Deductions

Depreciation

Depreciation is calculated in accordance with the straight-line, or progressive, or declining balance method. Accounting regulations permit Bulgarian companies to establish a depreciation schedule for each tangible and intangible non-current asset on the basis of the method chosen by the company. However, for tax purposes the straight-line method and declining balance method, in relation to specific assets, apply. If the total amount of the depreciation costs is higher than the tax allowable depreciation, the difference is added back to the taxable profit.

Net operating losses

Losses are carried forward over the following five years (ten years - for banks). Carry-forward of foreign source losses is restricted. Loss carry-back is not permitted. The loss carry-over can be used with regard to the advance tax payments as well as on an annual basis.

Thin capitalization rules

The thin capitalization rules apply only if the debt financing exceeds the double amount of the equity financing (the definitions of the two terms are to be derived from the accountancy legislation). In addition to interest on bank loans, loans between related parties and other loans, the thin capitalization rules clearly

cover interest under financial lease agreements. However, the rules shall not apply to bank loans and financial leases enforced before 1 January 1999, if they are already performed. The thin capitalization rules: (a) define restricted interest costs, (b) determine a limit for their tax deductibility, and (c) provide a possibility for tax deduction in the following year.

Restricted interest costs are added back in the calculation of the taxable profit to the extent to which they exceed: **$interest\ income + [(Financial\ result - interest\ income + interest\ costs) * 0.75]$**

Restricted interest costs added back in a given year can be deducted for tax purposes in the following tax period if certain requirements are met.

Payments to foreign affiliates

Tax authorities may re-adjust payments to foreign affiliates as per the arm's length principle. Market prices would apply, whereas deviations from such prices will be tolerated if within +/- 20%.

Other significant items

Companies may also deduct the following costs for tax purposes.

- Remuneration of members of boards of directors and supervisory boards.
- Grants extended to Bulgarian educational, cultural and other institutions or non-profit entities, within certain limits.
- Promotional and advertisement costs.
- Contributions made by employers for voluntary social and health insurance of employees if such contributions are up to BGN 40 per employee per month. The excess over BGN 40 is subject to the one-time tax at 20%.

Group taxation

There is no group taxation legislation. All companies are assessed on individual assessable profits and losses. However, tax anti-avoidance rules cover transfer pricing and related persons. The funds for the investment are generated from the contributions made by shareholders for acquisition of new shares (including on incorporation) in the company making the investments. If the requirements for the tax reduction are met the corporate tax is reduced by an amount representing 10% of the amount of the share contributions used in the above manner.

The sum for the reduction is accounted for as reserves and if greater than the corporate tax in the respective year it can be used to reduce the corporate tax in the following five years. Entities, already enjoying the tax incentive regarding regions with high unemployment may choose to continue to use the old incentive (which is already repealed) or to start using the new incentive if the conditions are met.

4.8.3. Withholding Taxes

Certain types of income originating from Bulgaria and payable to foreign entities (if not realized through a permanent establishment) or individuals are subject to a 15% withholding tax. The types of income are defined in CITA as: dividends and liquidation proceeds, interest, including such under finance leases, royalties, technical services remuneration, rents, payments under operating leases, franchising and factoring, capital gains from sale of immovable property, stakes in the companies, securities and financial assets. Withholding tax rates under double tax treaties between Bulgaria and the countries listed below:

Table 18. Tax rates under double tax treaties between Bulgaria & countries

Country	Dividends (%)	Interest (%)	Royalties (%)	Technical Services (%)
Albania (Note 3, 6, 9)	5/15	10/0	10	0/15
Armenia (Note 1, 6)	5/10	10/0	10	0
Austria (Note 13)	0	0	0	0
Belarus (Note 6)	10	10/0	10	0
Belgium (Note 6)	10	10/0	5	0
China (Note 2, 6, 9)	10	10/0	7/10	0/15
Croatia	5	5	0	0
Cyprus (Note 3,12,15)	5/10	7	10	10
Czech Republic (Note 9, 11)	10	10/0	10	0/15
Denmark (Note 3)	5/15	0	0	0
Finland (Note 4, 9) (Note 13)	10	0	0/5	0/15
France (Note 5)	5/15	0	5	0
Georgia (Note 6)	10	10/0	10	0
Germany	15	0	5	15
Greece (Note 15)	10	10	10	*n.i.
Hungary (Note 6)	10	10/0	10	0
India (Note 6)	15	15/0	15/20	15
Indonesia (Note 6)	15	10/0	10	0
Ireland, Republic of (Note 3)	5/10	5	10	*n.i.
Italy	10	0	5	0
Japan (Note 3, 6)	10/15	10/0	10	15
Kazakhstan (Note 8, 9)	10	10	10	0/15
Luxembourg (Note 3)	5/15	10	5	0
Macedonia (Note 3, 6, 9)	5/15	10/0	10	0/15
Malta (Note 13)	30	0	10	0
Morocco (Note 5, 9)	7/10	10	10	0/15
Moldova (Note 3, 6, 9)	5/15	10/0	10	0/15
The Netherlands (Note 3, 7, 9)	5/15	0	0/5	0/15
Norway	15	0	0	0
North Korea (Note 6)	10	10/0	10	15
Poland (Note 6)	10	10/0	5	0
Portugal (Note 3, 6)	10/15	10/0	10	0
Romania (Note 3, 6)	10/15	15/0	15	0
Russian Federation (Note 6)	15	15/0	15	0
Spain (Note 3)	5/15	0	0	0
Singapore (Note 6)	5	5/0	5	0
South Korea (Note 5, 6)	5/10	10/0	5	0
Sweden (Note 9)	10	0	5	0/15
Switzerland (Note 3,10,14)	5/15	10/0	0/5	0
Thailand	10	10/5		
Turkey (Note 3, 6, 9)	10/15	10/0	10	0/15
Ukraine (Note 3, 6, 9)	5/15	10/0	10	0/15
United Kingdom	10	0	0	0
Vietnam (Note 6, 9)	15	10/0	15	0/15
Yugoslavia (Note 3)	5/15	10	10	0
Zimbabwe (Note 3, 6, 9)	10/20	10/0	10	0/15

Source: Bulgarian Foreign Investment Agency, * not available information

Notes:

1. The lower rate applies to dividends paid out to a non-resident, which is the direct owner of at least USD 40,000, forming part of the capital of the company making the payment.
2. The withholding tax on royalties for use (or right to use) of industrial, commercial or scientific equipment is reduced to 7%.
3. The lower rate applies to dividends paid out to a foreign company, which controls directly at least 25% of the share capital of the payer of the dividends. In the specific cases of the different countries more requirements may be in place.
4. There is no withholding tax on royalties for the use (or the right to use) of scientific or cultural works.
5. The lower per cent rate applies to dividends paid out to a foreign company, which controls directly at least 15% of the share capital of the payer of the dividends.
6. There is no withholding tax on interest when paid to public bodies (Government, the BNB, state financial or non-financial institutions).
7. 5% royalties are applicable in case the Netherlands applies withholding tax under their domestic law.
8. Up to 10% branch tax may be imposed on permanent establishment profits.
9. The 15% rate applies in specific cases pointed out in the respective treaty.
10. The zero rate on interests applies, if the loan is extended by a bank.
11. The zero rate on interest applies if the interest is paid to public bodies (Government, Municipality, the BNB or any financial institution owned entirely by the Government), to residents of the other country when the loan or the credit is guaranteed by its Government, or if the loan is extended by a company for any equipment or goods
12. The DTT is signed and ratified. It has to be promulgated in order to enter into force. The previous DTT between Bulgaria and Cyprus, which was in force as from 27 August 1986 until 1 January 2001, provided for zero rates on all payments.
13. The Council of Ministers has stated its intention to re-negotiate the DTTs with Austria, Malta and Finland.
14. 5% on royalties will apply if the Swiss Confederation introduces in its domestic law withholding tax on royalties paid to non-residents.

4.8.3.1. Tax administration

Returns

Annual profit must be declared no later than 31 March of the year following the taxable year. The annual balance sheet and the annual profit and loss account of all entities with foreign participation, as well as certain resident entities, subject to certain criteria (number of employees, legal form, etc.), are to be certified by a chartered accountant and submitted to the Tax Office at the place of residence of the legal person, together with the tax return.

Payment of tax

In 2001 the corporate and municipal tax pre-payments due by entities which ended 2000 with a taxable profit are payable monthly as follows:

- for the first quarter of the year - on the basis of 1/12 of the declared taxable income for 1999, and
- for the remaining nine months - on the basis of 1/12 of the declared taxable profit for 2000

The above bases are adjusted by a coefficient published in the State Budget Act for the respective year. Entities ending 2000 at a loss and entities founded in 2001 will pay quarterly advance tax on their taxable profit for the respective quarter. The rate of corporate tax in this case is 15%.

The monthly prepayments are to be effected latest on the 15th day of the current month. The term for the prepayments on quarterly basis is the 15th day of the month following the respective quarter. No prepayment is to be made for the last quarter of the year.

Overpaid annual tax is set off against the tax to be paid for the following period. The difference between the annual tax declared in the tax return and the prepayment of tax for the same year must be paid by the deadline for submitting the tax return, i.e. 31 March.

Withholding tax is payable as follows:

- If the payer of the income is a tax liable person—by the latter by the end of the month following the month in which the payment of income became due or the resolution on distribution of dividends or liquidation quotas was made.
- If the payer of the income is not a tax liable person -by the recipient of the income within 30 days as of receiving the income.

After payment of the withholding taxes the payer of the income should disclose this fact to the respective tax office, which shall then issue a certificate of tax compliance to the foreign person entitled to the income already taxed. This certificate is necessary for repatriation of the net income.

4.8.4. Indirect Taxation: Value Added Tax Act (VAT)

The Value Added Tax Act (VAT Act) currently in force is effective as from 1 January 1999. Although Bulgaria is not a member of the European Community, the VAT legislation in many aspects follows the provisions of the Sixth VAT Directive.

Administration

VAT is administered by the Ministry of Finance, in particular by the tax and customs administrations.

Although VAT is administered separately from the other taxes at present, any VAT refunds that arise can be used to cover other tax liabilities, subject to certain conditions and procedures.

Registration

Any person (legal or physical, resident or non-resident) who/which has a taxable turnover exceeding BGN 75.000 during the preceding twelve months is obliged to register for VAT purposes. Under the VAT Act, such non-registered persons are subject to mandatory VAT registration, through an agent, upon achieving the respective turnover, regardless of whether:

- they have a permanent establishment in Bulgaria, and
- the activities are continuing and/or performed from a “fixed place” in Bulgaria.

Voluntary registration is possible for persons with taxable turnover between BGN 50.000 and BGN 75.000. Group or divisional registration is not allowed.

The VAT Act provides for a few new instances of optional VAT registration: A local legal entity, which does not meet the requirements for mandatory VAT registration, can register if its contributed share capital is at least the BGN equivalence of \$1 million. Such a person can keep its VAT registration for a period of three years following the date of registration. After the expiry of this term the person is subject to de-registration, unless it has met the requirements for mandatory registration or optional registration, based on effected exports. There are special rules for the VAT registration in some cases of commercial companies' transformation and acquisition.

Filing requirements

VAT-registered persons file annual and monthly tax returns. The tax return must be submitted within 14 days as of the end of each tax period. VAT-registered persons providing both taxable (including export) and exempt supplies are obliged to submit annual VAT returns.

Payment requirements

VAT payments to the state and VAT refunds from the state can only be made in BGN. The payment must be made within 14 days as of the end of the tax period. In case of de-registration the payment due for the last tax period must be made within 30 days as of the date of de-registration is completed.

4.8.4.1.VAT credit refund

The VAT credit to be refunded can be set off against the VAT due, as well as against other liabilities to the state. The offsetting takes place during a 4-month term following the period in which the VAT credit occurred. If after this term there is still VAT to be refunded, the refund is to be made within 45 days.

Exporters are entitled to a VAT credit refund within 45 days, if they do not have pending liabilities to the State. Persons with turnover from export supplies exceeding 30% of the value of their supplies in aggregate are considered exporters. VAT credit is also subject to recovery in case of carrying out supplies, which are exempt by virtue of international agreements to which Bulgaria is a party.

Tax base

The tax base for supplies within Bulgaria is the price (exclusive of VAT) charged to the customer, and all other taxes and fees, including excise duties, subsidies and financing relating to a transaction, as well as any interest and penalties under a transaction. The tax base also includes transportation, package and other expenses relating to the supply, if these are borne by the customer.

The tax base for transactions between related parties is at least the market value of the goods and/or services involved.

The tax base for imports includes the customs value, the customs duties and excise duties (if any) on the import goods.

Place of supply

Bulgaria has adopted the EU definitions of place of supply of goods and services.

VAT Exemptions

There are three types of exempt supplies:

- Supplies, which, according to the statutory “**place of supply**” rule, are provided outside the territory of Bulgaria.
- Supplies of goods in customs warehouses within the frame of the respective customs procedure.
- Supplies exempt due to their subject, such as:
 - transfer of ownership and limited property rights over land,
 - financial services,
 - insurance services,
 - lease of buildings and parts thereof, provided these are leased out for dwelling purposes,
 - transfer of a going concern of a company, as well as businesses or parts thereof as per the Privatization Act,

- provision of legal advice by registered attorneys in accordance with the Attorneys Act and of services under the Notaries Act,
- land processing services rendered by co-operatives by means of their own equipment, provided that the land is owned by the co-operative members,
- supply of grain as an in-kind rent for use of land,
- betting and gambling,
- donations in favor of charity institutions.
- other.

Export of goods and services

The export of goods and services is subject to VAT at a zero rate.

Within the meaning of the VAT Act export of goods is exportation abroad or to the free zones, free warehouses and duty-free outlets. However, export supply to customs warehouses does not qualify as export.

International transport is defined to be the transportation between two points abroad, irrespective of whether part of the transport route passes through Bulgaria or not. The transport between the free zones and the free warehouses within Bulgaria is also considered international. A number of services relating to international transport (including forwarding or agent services; sales of tickets for international flights and services related thereto) are also considered export services.

Processing of import goods that are further re-exported is also zero-rated.

Exporters are obliged to charge and pay VAT at 20% if the goods intended for export are sold but not physically exported by the end of the calendar month following the month in which the ownership was transferred as a result of the sale.

When the goods are subsequently exported the sale is re-characterized and the respective VAT charged and paid to the State by the exporter should be recovered. However, there are no clear rules on how the re-characterization of the sale will be reflected in the VAT returns and how the recovery will be done in practice. It is also not clear whether the new restriction applies to sales for export effected before 1 January 2000 in cases when the goods in question are still not physically exported by the end of February 2000.

Partial exemption

Where a registered person makes both taxable (including zero-rated) and exempt supplies the following rules apply:

The input VAT charged for goods or services entirely used for taxable (including zero-rated) supplies is fully recoverable.

The input VAT charged for goods or services entirely used for exempt supplies is not recoverable.

The input VAT charged for goods or services used both for taxable (including zero-rated) and exempt supplies, is partially recoverable. The amount of recoverable input VAT is calculated by reference to the proportion of taxable supplies to exempt supplies.

VAT rates

Under the VAT Act two rates are applicable to taxable supplies.

- 20% applicable to taxable supplies, including import of goods and services.
- A zero rate applicable to exports.

Disallowable input VAT

As a rule, input VAT cannot be reclaimed for goods and services, which are:

- used for promotional purposes
- relating to cars
- used for exempt transactions.

Refund of VAT to non-registered persons

VAT is not refundable to non-registered persons. However, a number of possibilities as to recovery of VAT charged upon acquisition of assets before the registration, or upon cancellation of previous VAT registration, are provided. Such VAT refund can be claimed, if the following requirements are met cumulatively:

- the taxpayer registers for VAT purposes,
- the assets are available with the taxpayer on the date of the VAT registration, and
- the required documentation is available.

If VAT is not refunded within the statutory term, interest is charged at the statutory interest rate.

Reverse charge

Only where services are imported from abroad VAT at 20% must be charged and paid by the recipient if: (a) the latter is registered for VAT, and (b) the supplier is not a VAT-registered person, and (c) the services relate to exempt supplies.

In all other cases no reverse charge applies in Bulgaria to services received from non-resident suppliers.

4.8.5. Indirect Taxation-Excise Duties

Excise duties are levied on goods and services listed in the Excise Duties Tariff, which are: (a) subject to transactions performed in Bulgaria, or (b) subject to cross-border transactions from abroad to Bulgaria.

Subject to excise duties are: a) Spirit drinks, including beer and wine, b) Tobacco products, c) Fuels, e) Some types of automobiles, f) Gambling machines and other casino facilities, g) Coffee and tea.

The Excise Duties Act provides for reimbursement of excise duties upon exportation of goods, when excise stickers have been paid but not used by producers, etc.

4.8.6. Customs Duties

The Customs Act, effective since 1 January 1999, provides for different customs arrangements with economic impact such as customs warehousing, inward processing, placing of goods in free zones and free warehouses, etc.

In general, import goods are subject to: (a) customs duty - a percentage of the customs value, and (b) VAT 20% of the customs value plus customs duty.

The rates of customs duties applicable to certain products are significantly reduced in 1999 (down to nil) as a result of the application of Free Trade Agreements between Bulgaria and: EU, EFTA, CEFTA, FYROM, TURKEY.

4.9. Labor Force and Employment Regulation

4.9.1. Labor Supply

One of the more attractive benefits of investment in Bulgaria is the, more than adequate, **supply of skilled and well-educated workers**. The workforce in Bulgaria comprises about 3.272.200 (in 2000) well-educated and highly skilled men and women many of whom have higher education or Technical Education at one of the many possible colleges. It has always been a feature of Bulgaria society to educate the children to a high level. This has included teaching many of the European languages at specialist language schools as well as selecting for higher levels of science and technical subjects. In most cities there are English, German and French language schools that teach all of the subjects of the curriculum in that language.

Parents feel a great responsibility for the education of their children and spend money on private education in addition to that provided by the schools. In this way many of the younger generation are able to speak good English, French or German.

Most investors going to Bulgaria **do find problems with middle and upper management**. There have been **no courses available to train managers in the skills of modern management** at this level. Recently however, there have been a number of courses made available through the Universities in conjunction with Western universities and also courses provided by the European Community through the PHARE Program. These courses are available throughout Bulgaria and have been used extensively by managers of privatized companies. It is more unusual for managers of state companies to be trained in this way. There are also now part time MBA courses available to managers through the New Bulgarian University.

During 1998 the economy in Bulgaria improved considerably and inflation remained at approximately 1% throughout the year. This improvement in the economy was introduced at a cost to the unemployment rate, which stands at 16.4% in 2000. The unemployment is a more serious problem in the countryside than it is in the cities and it is also more of a problem in the smaller cities. Throughout Bulgaria there is a skilled labor force available particularly in the sectors of tourism, industry and agriculture. There has been little training in the field of agriculture where techniques have been passed on from father to son and as a result in many of the rural areas there has been little mechanization. In some parts of Bulgaria co-operative farms are still in existence on a voluntary basis and these tend to be better equipped and better managed.

The food processing industry is more modernized and employs a large part of the rural labor force. Again the European community farm program is running courses for the agriculture and food processing industries and some companies are already reaching European community standards.

Another branch of employment is the tourist industry. Bulgaria has both winter and summer tourism and good facilities for both of these. Again there are a number of skilled workers in branches of the tourist industry but the benefits produced by these persons are spoiled by poor management.

Table 19. Bulgaria: Labor Force, Employment and Unemployment (1993-2000)

	1993	1994	1995	1996	1997	1998	1999	2000
In thousands								
Population ¹	8.472,3	8.427,4	8.384,7	8.340,9	8.283,2	8.230,4	8.190,9	8.148,9
Of working age	4.735,7	4.741,2	4.745,4	4.749,2	4.749,5	4.750,3	N/A	N/A
Pensioners ³	2.439,8	2.423,7	2.409,2	2.381,1	2.391,8	2.387,3	2.380,6	2.371,5
Total Labor Force	3.809,3	3.608,9	3.552,3	3.576,2	3.564,2	3.476,8	3.387,9	3.272,2
Activity rate (%) ⁴	55.4	52.4	51.5	51.8	51.6	50.4	49.2	47.5
Employment ³	2.994,6	2.868,7	3.031,5	3.085,4	3.031,1	2.920,7	2.811,0	2.735,5
Public	2.319,0	2.130,5	2.152,7	2.070,7	1.858,7	1.641,4	1.446,5	1.277,0
Private	671.4	732.5	872.6	1.010,1	1.159,0	1.272,9	1.354,6	1.445,1
Unknown	4.2	5.8	6.2	4.7	12.3	6.4	9.9	13.4
Share of total employment (in %)								
Public	77.4	74.3	71.0	67.1	61.3	56.2	51.5	46.7
Private	22.4	25.5	28.8	32.7	38.2	43.6	48.2	52.8
Unknown	0.1	0.2	0.2	0.2	0.4	0.2	0.4	0.5
Unemployment persons ³	814,7	740,2	520,8	490,8	534,1	556,1	576,9	536,7
Unemployment rate (in %) ³	21.4	20.5	14.7	13.7	15.0	16.0	17.0	16.4
Registered Unemployment ⁵	626,1	488,4	423,8	478,8	523,5	465,2	610,6	682,8
Official Unemployment rate (in %) ⁵	16.4	12.8	11.1	12.5	13.7	12.2	16.0	17.9
Unemployment Beneficiaries ⁵	195,4	167,3	138,9	178,0	157,7	136,3	178,4	196,9
Percentage (%) of change								
Population %	-0.8	-0.5	-0.5	-0.5	-0.7	-0.6	-0.4	-0.5
Labor force %	N/A	-5.3	-1.6	0.7	-0.3	-2.5	-2.6	-3.4
Employment %	N/A	-4.2	5.7	1.8	-1.8	-3.6	-3.8	-2.7
Employment of which in Private Sector %	N/A	9.1	19.1	15.8	14.7	9.8	6.4	6.7

Source: IMF Country Report, No.01/54, March 2001, page 62.

Notes:

1. 2000- figure is preliminary
2. 2000 figure refers to end-September
3. Data are from the labor force survey, conducted for the first time in September 1993. persons of age 15 and over are interviewed. Data refer to September 1993, October 1994, October 1995, November 1996, November 1997, November 1999, and December 2000.
4. Labor force as a proportion of the working age population (age 15 and over)
5. end of period.

How to find staff

Most of the methods of finding workers that exist in Western Europe and North America can now be found in Bulgaria. There is a preference for working in the private sector and most skilled people in the state sector are looking for jobs with better pay and better conditions, which are the norm in privatized companies. There is a pool of applicants coming directly out of the Universities who are fluent in English and having some management knowledge but no skills as yet. There is however, a much smaller pool of managers with three or four years of management experience with a Western company and who have acquired a Western way of thinking. These managers are well sort after and can command higher salaries than one would normally expect. There is a serious lack of middle managers in Bulgarian industry and this leads to management

problems. Senior managers were often trained to make decisions at the top instead of delegating the decision-making. These bad habits continue when there is no adequate middle management for them to delegate to. Most companies find that a short period of working with an expatriate can be very beneficial and the Bulgarian managers are fast at learning new techniques. Most privatized companies, where the buyer is from abroad, place senior managers in the company for two or three years. After this time, in most cases, the local managers are perfectly capable of working on their own.

The commonest way of finding new staff is to use a **human resource agency**. There are agencies, which has four or five years of working in Bulgaria providing professional staff for investors. In most cases they are able to carry out, all of the work for the investors including placing adverts, prior selection and psychological testing of the applicants. Most of these companies also have a database of persons looking for a new job. In these cases new staff can be found very quickly for most positions.

The commonest way of finding staff is by using press advertisements. There are several newspapers that are commonly used by Bulgarians to look for new jobs, these include **24 HOURS** and **TRUD** and in the case of economic positions such as chief accountants or financial managers, newspapers such as **PARI** or **CAPITAL** are more commonly used.

More recently, some companies are able to head hunt for higher level managers. **Head hunting is not common**, so far, in Bulgaria and managers find it strange to be approached in this way. It has however, been successful for a number of the more senior positions where managers have either worked in the West or have heard about head hunting.

One of the more common problems is overstaffing in the newly privatized factories. There are now **a few companies of Human Resource consultants** who have the experience to restructure the work force, set new incentive schemes and assess the quality of the local managers. These consulting companies can also assist in carrying out a training needs analysis of the Bulgarian work force and organize the training.

Health and Safety is a subject that until recently only received lip service. Although the legislation was more than adequate very few companies actually took much notice of the rules in practice and companies have a long period of neglect in this area. New legislation will bring Bulgarian practice in line with European Union directives by the year 2001 and this will require a great deal of investment in equipment and training. Investors will need to make sure they use a licensed consultant for Health and Safety issues.

Specialist Personnel Service firms

The big five audit companies do, in most cases, have personnel selection functions for their clients. There are also a few western specialist firms operating in Bulgaria. These include: Hill International, NEW i, PMC and Snelling Personnel Services.

Hill International is specialized in media search and personnel selection, Snelling Personnel Services provides temporary staff as well as recruiting and interviewing for permanent staff. PMC offers staff recruitment services using press advertisements and database searches. NEW i offers all services including staff appointment, restructuring of the work force, setting up a modern HR department and Health and Safety consulting.

Remuneration and non-financial means for motivation

The full remuneration and salary structure is set up according to the Labor code in Bulgaria. The total cost of employment consists of the basic salary plus the social security payments and a number of other smaller taxes. Salaries in the private sector are usually higher than in the State sector. It is not uncommon for workers and managers in the private sector to be paid a higher salary than those of many senior government officials. There is a tendency for new companies coming to Bulgaria to pay what they consider a fair salary, lower than in their home country, but still higher than is normally found in Bulgaria. This problem is compounded when applicants for jobs state their present salary at a higher level than they actually are. For

example they might say their salary is the net figure when in reality it is the gross or they might include overtime and bonuses as part of the basic salary. It is difficult for a new investor to be able to judge what the real situation is.

The Bulgarian International Business Association (BIBA) provides, every year, a very detailed set of salary tables for most of the industry sectors including consulting, retailing and manufacturing. These figures are averaged in most cases over 20 or 30 companies and give a good guide to the real salary figures. The BIBA salary survey also gives information on the levels of bonuses, provision of cars and telephones and other components of the full remuneration package. It should be remembered that any additions to the basic salary are taxable. One must be careful that these incentives are not included as part of the basic salary otherwise they will be included in calculating the Social Security taxes. If the incentives are given as extras to the basic salary then they are not counted for Social Security and the employee is liable for taxation. It should be noted that salaries outside Sofia are lower for all positions than those for workers in Sofia.

The most common form of incentives are:

- Free medical service,
- Food vouchers,
- Transport cards for the buses,
- Clothing allowances,
- Discount on company's product.

The more senior managers frequently get a car, telephone or representation allowances and often club membership.

Employment Relations

The relations between the company and the workers in Bulgaria are governed by the Labor Code. All Bulgarian citizens have a right to work. Management cannot make any restriction on the workforce made by race, sex or any other discriminating factor. The constitution and the Labor code prevent such discrimination.

Labor relations within the country at a national level are governed by agreements between the trade unions, the government and representatives of the employers. At the work level, agreements are made between the trade unions and the employer. There are two main trade unions in Bulgaria **The Confederation of Independent Trade Unions of Bulgaria** and **Podkrepa**. Newly privatized companies can expect attempts by the trade union leaders to increase their power within the company. In general this should not be a problem because although in the state industries, trade unions theoretically did have much power, in practice their views were rarely listened to. Good managers can have large benefits by working closely with the trade union. The trade union workers tend to listen carefully to the union leaders in a factory. It is found that working with the unions to increase the quality of life of the workforce, work hygiene and the safety of working conditions can bring a good working relationship with the unions and hence increased productivity.

Employment Contracts

Employment relationships are regulated by the Bulgarian Labor Law through employment contracts. The employment contracts between the employee (not under 16-years of age) and the employer are prepared in written form and should specify the place and nature of work and the salary to be paid. It may be concluded for a fixed or for an indefinite period. The law provides an opportunity for transformation of the fixed term contract into one for an indefinite period, which is a suitable way for both parties to make the relationship more stable and effective. The parties may also choose a trial period of up to 6 months. Other types of

employment contracts are those for example for 5 days work per month and the ones for additional work for the same or another employer.

The content of the contract must comply with the mandatory provisions of the labor law, concerning the special protection of the employee: working hours and rest, labor remuneration, holidays, safe and healthy conditions of work, social and cultural services, and conditions and requirements for termination of the contract. Of importance is the influence of collective agreements concluded between the employer and the trade union organization.

The monthly labor remuneration must not be less than the amount of the minimum labor salary in the country, defined by the Council of Ministers for the respective period of 1 month (from October, 2000 onwards it amounts to 79 BGN). Its payment may be done in advance or twice a month, or as agreed. Income taxes, due and voluntary social security contributions are deducted at source.

Together with employment relationship goes the obligation of the employer to provide social security and make contributions regularly at his expense for the employee.

Another way to use the labor force is through concluding a civil contract. The difference between the civil and the employment contract extends to the following: civil contract is the contract pursuant to which the two parties agree that one of them shall perform an activity that shall produce a result of the assigned activity, while the other shall pay a remuneration i.e. the subject of the contract is the result of the activity and the employer can not specify the working conditions, working time, leaves, etc. More important he/she could not exercise a control. The employer can only specify the particular time of the activity that should be done and set requirements to the produced result. Under civil contract the employee pays 15% Advance Tax defined by the Law for Taxation of the incomes of Natural Persons, but neither the employer nor the employee pays 4.5% Unemployment Fund Contribution. Due to the last in case the contract is terminated the employee can not register him/herself as unemployed and can not receive unemployment severance. Because of those unpleasant results for the employee, the State Labor Inspectorate which provides control over the employment relations, can impose a penalty if the subject of the concluded civil contract is not as the aforementioned, and the employer attempts to conceal its employment relationship (i.e. not paying the Unemployment Contribution).

Termination of the contract is a significant point in labor regulation. The law provides three possibilities: general grounds, special grounds for termination with notice or without a notice. Notices should be in writing for a period from 30 days up to 3 months. Each of the parties may terminate the relationship without notice only in the cases listed by the law, so that parties can be protected from detrimental behavior. If notice periods are not observed, the regular party is entitled to a compensation to the extent of the gross labor remuneration or real damages caused.

There are special provisions about dismissal and protection against it in favor of some categories of workers. In some cases of terminating a contract, the employer is obliged to choose among employees.

The employer exercises disciplinary power and is still the strongest party at the labor-force market.

Social security

The employers must register at the local social security administration within 15 days from the day, they have employed anyone subject to compulsory insurance. Branches that are not financially separated do not register separately. They are included in the registration of their central company. In the case of liquidation, changes in organization or merging, the insurer must report in written form all the changes to the social security authorities.

Public Social Security is obligatory for all employees employed by Bulgarian or foreign natural or corporate bodies within the country. They are secured for all risks.

The Code of social insurance includes insurance for general illness, work accidents, professional diseases, maternity leave, old age and death, as well as additional compulsory pension insurance. The main principles are: compulsion and comprehensiveness, solidarity and equality of the insured persons, the fund organization and others.

Compulsorily, all workers and employees are to be insured, no matter if they had labor or civil contracts. An exception of this obligation is possible only if the civil contract was for monthly payment under one minimum working salary. (BGN 79) - then the obligation is only for insuring work accidents, professional diseases, disabilities and for general illness and death.

Insurers are the juridical and natural persons, having an obligation, by law, to pay in insurance installments. The amount of the insurance installments is determined by the Law of the Government and Social Insurance Budget.

The distribution of the installments between insurers and insured are at the rate of 80:20 for years 2000 and 2001, 75:25 for 2002, 70:30 for 2003 until the gradual equalization at year 2007 - 50:50. The insurance installments to fund 'Work accidents and Professional diseases' is on behalf of the insurers. On the social insurance expenses, the workers periodically pay in insurance installments. The installments are paid in banks to the respective fund accounts with separate paying orders, as well as when paying salaries as when paying in advance. The part of insurance installments due the insured persons is paid in when remuneration is paid.

The government and social insurance financial resources are grouped in three separate funds - Pensions, Work Accidents and General Illness and Maternity.

The insurance installments are paid in by the 10th of each month they apply to.

With the Code of the Compulsory Social Insurance, changes have been made in the Law of Foreign Investments, according to which the workers and employees are insured under the Bulgarian Law

The same new legal provisions, effective from 1 January, 1998, allow voluntary social security for unemployment which is possible for every Bulgarian citizen above 18 years of age who has concluded a contract for voluntary social security for unemployment with the especially created and licensed for the purpose social security institutions. Employers may participate in these social security contracts, too. The installments made under the contracts which must comply with the explicit legal requirements are deducted from the taxable income of the persons and the taxable profit of the employers.

Public social security provides the following: financial aids and compensation in case of temporary disability due to illness, accident, pregnancy, birth, raising a young child, quarantine, taking care of a sick family member, as well as additions to the salary after labor readjustment of pregnant women and persons with temporarily decreased working capacity when the new job is paid less, pensions in case of disability, age, as well as inheritable pensions of family members in case of death of the person that has provided them, one time aid after birth of a child. In case of labor accident the employers have to pay back the amount of the compensations paid by Public Social Security. Such payments are made within the monthly payments to Public Social Security.

Health Security System

The health insurance in Bulgaria is both compulsory and voluntarily. It is a system for a social health protection of the people, that guaranties a package of health services and is carried out by the National Health Insurance Fund. The voluntarily health insurance is a supplementary one and is carried out by Joint Stock Companies, registered under the Trade Act and licensed under the Law on the Health Insurance.

The health insurance contribution is not a subject of taxation. Its exact amount in percentage on the ground of the gross remuneration shall be set out in the Law for the Annual Budget of the National Health Insurance Fund.

The contribution measuring at 6% is paid by both the employer and the employee in the following proportion:

- for the year 2000 and 2001 - 80:20
- for the year 2001 - 75:25
- for the year 2003 - 70:30
- for the year 2004 - 65:35
- for the year 2005 - 60:40
- for the year 2006 - 55:45
- for the year 2007 and after - 50:50

The contribution to the National Health Insurance Fund shall be paid by the employer on a monthly basis and shall be deducted from the gross remuneration and the financial aids for temporary disability. The employers are obliged on request to submit information for the insurable income on the ground of which the contribution shall be calculated to the National Insurance Institute.

Working hours

The normal duration for a five-day work week is up to 40 hours, and 46 hours for a six-day work week. The general principle laid down in the Labor Code is that overtime work is prohibited. The code considers as overtime work, the work done by the order or with the knowledge of the employer, beyond the normal working hours. There is a governmental institution- Labor Inspectorate, which supervises the use of overtime. In enterprises where organization of work allows flexible working hours may be established. The period during which the employee must be at work in the enterprise, as well as the manner of accounting it, shall be specified by the employer. Outside the time of the compulsory presence, the employee may decide on when to begin the working day.

Holidays

The employee is entitled to an annual paid leave after 8 months length of service amounting to at least 14 days depending on the length of service.

During the maternity leave the employee is entitled to receive her remuneration paid by the National Security Institute budget. Furthermore, the Labor Code allows additional paid leave for raising a child until 2 years of age. During that period the mother is paid an indemnity from the National Security Institute amounting to the minimum salary in the country. There is also a leave for temporary disability during which compensation is paid by the funds of the National Insurance Institute.

Disability

Disability is when the employee can not or is hindered from doing his work due to: illness, work accident, professional disease, sanatorium treatment, medical examination, quarantine, taking care of a sick family member, accompanying a family member to a medical institution and also in case of pregnancy and birth for women.

Primary medical aid rendered by the duly chosen personal doctors and dentists is free of charge. The rest of the medical services are chargeable pursuant to a tariff issued by the Ministry of Health. The obligation for ensuring safe and healthy work conditions concerns medical service, special work clothes and measures for preventing and reducing injuries and general illness as a whole. A special law together with the Labor Code elaborates on the obligations of employers to assure healthy and safe work conditions. Employers must undertake at their expense all the necessary statutory measures in order to prevent accidents and avoid their detrimental consequences in case of emergencies. Employers are obliged to inform the employees about the risks for their health and safety and appoint one/several persons whose tasks is/are to organize activities for prevention and protection from these professional risks. To facilitate exercising of control, every employer must declare to Regional Labor Inspectorate his activities, number of employees, work conditions, risk factors and undertaken preventive measures when beginning his business activity and whenever he changes it or his technology.

Patient's Rights under the National Framework Agreement

Pursuant to the National Framework Agreement, signed by the National Health Insurance Institute and the professional organizations of medical doctors and dentists, each person, who has health insurance, is entitled to a promotion and prevention package, in addition to the diagnostic, treatment and rehabilitation services. Besides the patient's rights, the Health Insurance Act stipulates the obligation of the persons, having health insurance, to respond to the invitation of general practitioners to go to this type of examinations. The sanction for non-appearance is the loss of insurance rights for a period of three months. This part of the general practitioners' activity is connected with the intention of the health reform - to shift the emphasis from diagnosis and treatment to prevention, for the purpose of ensuring fuller employment, from the point of view of both the employees and employers. On the other hand, in this way both the strategy of the World Health Organization and one of the main principles of the health reform are implemented - orientation towards improving the health of the healthy, and an early diagnosing and preventing diseases.

Exemption of some types of indemnities under the Labor code from insurance contributions,

The exemption of some indemnities is regulated by the Directive on the remuneration elements and the income, on which insurance contributions are made, and on calculating the monetary indemnities for temporary disability, pregnancy and bearing a child.

The indemnities are exempt, which are paid to the heirs of the employee, when the death of the testator has occurred as a result of a labor accident, and the employer's financial liability is realized. In the event of a damage inflicted on the employee's health and a limited employer's financial liability, no insurance contributions are made on the indemnity paid.

The following indemnities are also exempt from insurance contributions: in case of removal, default in giving notice, termination of the employment contract without notice, termination of the employment contract due to sickness; termination of the employment contract due to entitlement to a full old-age pension, for unused paid annual leave, etc., under Art. 232 of the Labor Code.

Insurance of Persons Working without an Employment Contract and Receiving a Monthly Remuneration more than the Minimum Salary

Under these terms and procedures, employers usually hire consultants under a civil part-time contract, to do a specific task under specified terms of reference. The practice so far has proved that it is easier to regulate the relationship between employer and consultant under the terms and procedures of the Obligations and Contracts Act, which allows more flexibility in the bargaining than the Labor Code.

The remuneration for the work done by consultants is given, after deducting the operating costs, recognized pursuant to the Natural Persons Income Tax Act, and then the tax due under the same Act is deducted. Such persons are subject to insurance only against disability due to a general disease, old age and death, the amount of the insurance contributions being 32 per cent.

Tax Rebates for Insurance Contributions Made

The employer's contributions for additional compulsory pension insurance are recognized as operating costs, pursuant to Art. 161 of the Corporate Income Tax Act. The additional compulsory pension insurance is done for employers, working under particularly difficult conditions, and for some categories of employees, born after December 31, 1959. The ratio between the employee's and the employer's parts is the same as in the case of the compulsory pension insurance.

The Compulsory Social Insurance Code regulates the three anchors of the pension reform. The third anchor is the voluntary pension insurance. Employees can pay their contributions in the voluntary pension funds themselves. The Act, however, provides the possibility for the employer to also insure the employees. This possibility is regulated by the collective employment contract, signed by the employer and the representatives of the trade unions or those elected by the employees' general meeting. In this case, the employer owes a tax only on 20 % of the funds set aside for social benefits costs, in the event that the funds set aside for voluntary pension insurance do not exceed 30 levs per person.

The obligation for ensuring safe and healthy work conditions concerns medical service, special work clothes and measures for preventing and reducing injuries and general illness as a whole. A special law together with the Labor Code elaborates on the obligations of employers to assure healthy and safe work conditions. Employers must undertake at their expense all the necessary statutory measures in order to prevent accidents and avoid their detrimental consequences in case of emergencies.

Employers are obliged to inform the employees about the risks for their health and safety and appoint one/several persons whose tasks is/are to organize activities for prevention and protection from these professional risks. To facilitate exercise of control, every employer must declare to Regional Labor Inspectorate his activities, number of employees, work conditions, risk factors and undertaken preventive measures when beginning his business activity and whenever he changes it or his technology.

In the field of health and safety a new Occupational Health and Safety Law has been passed by the National Assembly. It obliges the employers whose staff outnumbers 100 employees to establish Occupational Health Services and Health and Safety Committee. The functions of the Occupational Health Services are mainly preventive and prophylactic. The members of the Health and Safety Committee are appointed by the general meeting.

4.9.2. Employment of Foreign Persons

All foreign persons that have permanent residence permit or are granted right of sanctuary or refugee status can be employed in the same way as Bulgarian citizens. Temporary work permits are issued by the National Office of Employment of the Ministry of Labor and Social Care. The work permits are issued for a specified time, job and employer.

The permit is issued after a request by the employer. A work permit shall be issued for work, requiring specialized knowledge, skills and professional experience. It is valid for the time of the employment contract but not more than one year. The permission can be prolonged several times but within a three year period. For issuing the permit the employer submits to the Labor Authority the following documents:

- Application-request form (2 copies).
- Four photographs of the employee.
- Motivation of the request.
- Certified copy from the court registration of the employer.
- Certificate for tax registration of the employer.

- An inquiry form of the employer on the foreigners working for him.
- Copy from the papers for the payments of contributions to the "Social Security Fund" and the "Qualification and Unemployment Fund" for the Previous 12 months.
- Legalized documents for qualifications, education, etc.
- Two copies of an employment contract signed and stamped by the Employer.
- Medical certificate form approved by the Minister of Health.
- Other documents that are necessary due to the specific job requirements according to the Bulgarian labor legislation.
- a fee of six minimal monthly salaries

The time necessary to grant a work permit is between three weeks and one month. When the employer receives the work permit on the name of the employee who is a foreign citizen, he must pay a contribution to the "Qualification and Unemployment Fund". The amount of the contribution is equal to the amount of six minimal monthly salaries.

The permit can be issued only if there is no Bulgarian citizen suitable for the job. The number of employees who are foreign citizens cannot be over 10% of the total work force. The employer must assure transport expenses for the foreigner's return in case of termination of the employment contract ahead of term, expiry or annulment of the granted work permit.

The law specifies that the permit is issued only on the name of the employee for a specified employer, job, place and a period of time.

The employment contracts concluded with a foreign person should specify some other points too: the obligations of the parties about accommodation expenses, medical treatment, insurance, transport from and to the home country of the foreigner.

The law does not allow issuing of work permits when:

- the applying employer has dismissed within the previous eight months Bulgarian citizens who are suitable for the jobs for which the issuing of work permit is asked,
- the offered work conditions and remuneration are less favorable than the usual ones for Bulgarian employees,
- the offered salary is insufficient to ensure the necessary means of existence,
- the Constitution or the laws require Bulgarian citizenship for the job.

Foreign persons

Foreign persons are obligatorily insured only for temporary and permanent disability. For this risk only, the contribution percentage is 22% of the gross monthly salary paid by the local employer. For all other risks, depending on their own choice they can be secured according to the regulations for Bulgarian citizens. The insurance conditions should be settled in the employment contract.

Disputes under contract with foreigners may be handled either by Bulgarian or other court, as agreed.

The labor law is well-organized and quite comprehensive for foreigners so there could be no problems in the legal aspect of employment relations.

The latest Law on Foreign Investments repealed the limit for transferring foreign currency abroad. In the explicitly enumerated cases, including received salaries, foreigners may transfer foreign currency freely, after presenting a certificate for paid taxes.

4.9.3. Work Regulations for Foreigners

Entry to the country

A foreign person can enter the Republic of Bulgaria only if they have valid papers. These are:

- A passport or other alternative document allowing him to travel abroad.
- An entry permit - either entry or transit visa.

A visa is not required where there is a bilateral agreement between Bulgaria and the native country of the visitor. Currently no visas are required from citizens of European Union member who stay in Bulgaria for a period of less than 30 days.

Issuing and validity of visas

Entry or transit visas are issued by the diplomatic or consulate offices abroad. Some types of visas can be issued also at the border check-points the Diplomatic or consular offices issue the following types of visas:

- Visa for airport transfer - the foreigner does not enter the country but only changes flights at the airport.
- Transit visas - the foreigner should leave the country within 24 hours after the entry with such visa.
- Short stay visa - it is only for a single entry for no more than 90 days. The visa is valid for three months after the issuing.
- Long stay visa - it is for multiple entries, up to 90 days each. The visa is valid for no more than 12 months.

Long stay entry visas can be issued to foreign persons that are in contact with a company, organization or any institution registered in Bulgaria and their activities imply multiple visits to the country. Limits of the stay for citizens of countries, with which Bulgaria has bilateral agreements, are set in compliance with those agreements.

Foreign persons that have an employment contract and valid working visa can acquire a permit for stay in the country for the time of the contract but no more than one year. This permission can be prolonged if there is a new valid working visa. Foreign persons who have legal registration to carry out business activities in Bulgaria can acquire a permit for stay up to one year. The permit can be prolonged every year.

Permits for permanent residence

Permits for permanent residence do not specify when the foreign person should leave the country.

Permits for permanent residence can be acquired by foreign persons in the following cases:

- Foreign persons originally holding Bulgarian nationality.

- Married to Bulgarian citizens or to other foreign persons that have permits for permanent stay. Children of Bulgarian citizens or of other foreign persons who have permits for permanent stay.
- Staying in Bulgaria permanently for more than ten years or 6 years if they are carrying out business activities in the country.

The permission for permanent residence is issued by the Ministry of Internal Affairs. The necessary documents must be submitted to the regional Passport Authority in the region where the foreign person is resident. The documents can also be submitted to the diplomatic or consular office in the home country of the applicant.

The applicant must submit the following documents:

- Completed application form approved by the Ministry of Internal Affairs or by the Foreign Ministry.
- Passport or other alternative document for traveling abroad.
- Bulgarian ID if the foreign person has been in the country for more than 6 months.
- Document that certifies the applicant has business in Bulgaria or is self-employed (court registration).
- Autobiography.
- Proof that there is accommodation provided for those foreign persons who do not have registration for carrying out any business activities.

The permit is issued within one month from the day of submitting the documents. If they are submitted to a diplomatic or consular office abroad - the permit is issued within two months.

At any time foreigners should have with them a valid passport or permanent residency document and are obliged to present it to the governmental authorities if it is requested. A driving license can not be used for this purpose.

4.10. Pension insurance system in Bulgaria

4.10.1. Introduction

The social security system in Bulgaria in existence since 1951 has been entirely changed to reflect the transformation from centrally-planned to western style market economy. As part of the change, a comprehensive pension reform has been launched since 1999. The old pension system financed on pay-as-you-go basis has become unsustainable under Bulgarian realities of increasing share of the old age population, negative growth rate of the population, extensive number of labor categories eligible for early retirement, and low collection of social security contributions.

The enforcement of the new Mandatory Social Security Code and the Additional Voluntary Pension Insurance Act since January, 2000 moved Bulgaria towards a diversified three-pillar pension system, involving both public and private sector. The World Bank and the USAID have supported Bulgarian government in its efforts to implement an efficient pension system.

The new architecture of the pension system provides for new principles of administration and financing of the pensions. The major ingredients of the pension system are:

- Mandatory Pension Scheme – Pillar I
- Additional Mandatory Pension Scheme – Pillar II
- Additional Voluntary Pension Scheme – Pillar III

Pension funds belonging to Pillar II and Pillar III are to be administered by the private pension insurance companies, licensed by the State Insurance Supervision Agency (SISA), and will operate on a capital accumulation principle.

Pillar I - Mandatory Pension Scheme

Mandatory Pension Scheme is regulated in the Mandatory Social Security Code. Pillar I covers the cases of old age and death. As prescribed by the Code, the new mandatory pension scheme, which is a continuation of the previous pay-as-you-go (PAYG) system, is operational since January 1, 2000. The major changes underway provide for:

- Raising minimum retirement age. The retirement age will be increased by 6 months each year until the age of 63 for men and 60 for women,
- Sharply reducing eligibility for early retirement,
- Progressively introducing closer link between benefits and actual lifetime contributions.
- Gradual redistribution of the share of employers and employees in the contributions from 2000 to 2007:

Employer: Employee

- For 2000 and 2001 – 80:20,
- For 2002 - 75:25,
- For 2003 - 70:30,
- For 2004 - 65:45,
- For 2005 - 60:40,
- For 2006 - 55:45,
- From 2007 onwards – 50:50.

This pillar is directly administered by the state and the social partners and is financed on a PAYG basis. A separate state fund 'Pensions' has been set up with contribution rates determined annually in the budget of the State Social Security. For the year 2001 the contribution rate is 29% of the social security base. Social security base consists of various sources of personal income but is limited up to ten minimum monthly salaries. The size of the minimum monthly salary in January 2001 is BGN 79, thus the maximum amount of social security base is BGN 790. All pension contributions for state employees and military officers are carried out by the State Budget. Sole traders, partners, and private agricultural workers, are all required to pay themselves their entire pensions contributions, which should be calculated on a minimum of two minimum monthly salaries.

Pillar II - Additional Mandatory Pension Insurance (AMPI): It is introduced by the Mandatory Social Security Code. However, important aspects of the activities of the pension insurance companies, which manage these funds are regulated by the Additional Voluntary Pension Insurance Act.

The purpose of AMPI is to guarantee additional income in early retirement for persons working in the first and second labor categories as well as life-long additional pension for all categories of persons. The AMPI covers old age and death. At present additional mandatory pension insurance is still under construction. There are already nine funds licensed till December 2000, and the total number of funds is expected to be around 12 - 15.

Under pillar II, two types of pension funds are to be set up - occupational and universal. Pension insurance companies are entitled to establish and control only one universal and one occupational pension fund.

From 1 January 2000, persons working in the first and second labor categories must contribute to an occupational pension fund, irrespective of their age. For the year 2001 the rates for additional mandatory pension contributions covered by the employer are set at 12% (of the social security base) for employees working under the first labor category and at 7% (of the social security base) for employees working under the second labor category. The minimum number of insured in an occupational pension fund is 15 000 (This condition is not applicable during the first two years after the fund has been registered). Payments of insurance contributions to the occupational pension funds are entirely covered by the employers. They must be paid simultaneously with the mandatory social security contributions to the account of the National Insurance Institute.

Currently the pension insurance contributions to occupational pension funds are paid to the account of the National Insurance Institute. The accumulated amounts will be transferred to the accounts of the already registered nine occupational funds.

From 1 January 2002, all persons born after 31 December 1959 are required to make contributions to a universal additional mandatory pension insurance fund if they have state social security. It has been suggested that the pension contribution may be set at 2% of the social security base. The minimum number of insured in a universal pension fund must be at least 30 000. (This condition is not applicable during the first two years after the fund has been registered).

Payments to the universal pension fund are divided between the insurer (employer) and the insured person (employee) in the same ratio as contributions for Mandatory State Social Security.

Self – insured persons contribute to universal pension funds entirely on their own account.

The AMPI is executed through contracts between the insured person and a licensed pension insurance company. The additional pension is personal. Funds are accumulated in personal accounts under a personal pension number and may be paid out to person after his/her retirement under the general pension rules or to their survivor in the case of death.

Insured persons must submit an individual application form to the pension insurance company three months before the insurance obligation arises in order to choose a pension fund. Those who do not choose the pension fund will be automatically assigned to a licensed pension fund.

Pension insurance companies are entitled to receive charges for the operations they perform connected with the AMPI. These charges and deductions should be regulated in the insurance contracts and comply with the following limitations:

- up to 5% of each contribution (administration fee),
- investment fee of up to 1% of the assets of the pension fund,

- The pension insurance company may collect additional charges in the following cases:
- transfer of the funds accumulated in the individual account to another fund,
- when the insured requests statements more than once a year.

The additional charges may not exceed 200% of the expenses really incurred. The pension insurance companies may not collect charges different from the specified above.

The AMPI payments of the employer (assignor) are recognized as expenses for tax purposes for the company. Similarly, personal installments are tax deductible for individuals.

Revenues from the investment of assets of the pension funds, distributed to insured persons' accounts, are not taxable under the provision of the Taxation of Income of Natural Persons Act. Services rendered with regard to AMPI are VAT exempt.

AMPI operates on a capital accumulation basis. The size of the pension payments will be in correlation with contributions made to the account, the yield on the investments of the fund, and the biometrical tables.

Pillar III - Additional Voluntary Pension Insurance (AVPI): Additional Voluntary Pension Insurance (AVPI) was legally regulated by the Additional Voluntary Pension Insurance Act (July 20,1999), enforced as of January 1, 2000. Since 1994 however, over 20 pension funds have been founded. Currently nine funds have been licensed under the new regulations. As of September 2000 the number of people included in the additional voluntary pension schemes exceeded 400,000. The assets under management exceeded BGN 74m.

The AVPI covers old age, disability, death, and a variety of other products. It provides for an additional pension on the basis of contracts between the insured person and/or his/her employer (or assignor) and a pension fund. Each person, who has reached the age of 18, can voluntarily insure himself with a pension insurance company. The AVPI is carried out through participation in voluntary pension funds, established and managed by the licensed pension insurance companies.

Similarly to the AMPI its purpose is to guarantee an additional pension for the beneficiary. However, the accumulated funds in personal accounts are available to the insured person at any time (i.e. not only after retirement as with the AMPI). In the event of death, the funds accumulated in the account can be inherited.

Pension insurance companies introduce charges and deductions for the operations connected with the AVPI. These charges and deductions are regulated in the insurance contracts and are as follows:

- up to 10 BGN entry fee,
- up to 10% of the generated income on the investments of the fund (investment fee),
- up to 7% of each contribution (administration fee),

The pension insurance company may collect additional charges in the following cases:

- for each withdrawal (full or partial) from the individual account,
- for each transfer (full or partial) of accumulated funds from the individual account to another account/fund,
- for each requested information not specified in the general terms and procedures.

The pension insurance companies may not collect charges different from the specified above.

Revenues from the investment of the assets of the pension fund, distributed to the insured persons' accounts are not taxable under the provision of the Taxation of Income of Natural Persons Act. Services rendered with regard to AVPI are VAT exempt. Any contributions made by the individuals or by their employers are recognized as a tax-deductible expense, irrespective of the amount. In addition contributions for additional pensions, not exceeding BGN 40 per month for each insured person, are not subject to 20% tax withheld at the source.

4.10.2. Investment regulations

Pillar II Funds

The assets of the universal or occupational pension fund may be invested only in:

- Government securities – issued or guaranteed by the State,
- Securities admitted for trading at regulated stock markets,
- Municipal bonds,
- Bank deposits,
- Real estate and mortgages.

The assets of a pension fund may not be invested in: (a) Securities which are not fully paid in, (b) securities issued by the pension insurance company managing the fund, and (c) securities issued by related persons to the pension insurance company managing the fund.

The assets of a pension fund may be invested in compliance with limitations specified below: At least 50% of the assets of the pension fund should be invested in securities, issued or guaranteed by the State and/or in bank deposits. Up to 5% of the assets of the pension fund may be invested in real estate.

Up to 5% of the assets of the pension fund may be invested in securities issued by a single company. Up to 10% of the assets of the pension fund may be invested in securities issued by a single company upon a permission of the State Insurance Supervision Agency and in coordination with the State Securities Commission.

The managing pension insurance company and the universal or occupational fund are not allowed to acquire more than 10% of the shares of a single issuer or to hold a capital stake enabling the insurance company and the fund to appoint (directly or indirectly) over half of the members of the governing body, or to materially influence the decision-making of the issuer.

The pension insurance company may invest abroad up to 5% of the pension fund's assets in government securities and municipal bonds. The pension insurance company may invest abroad up to 5% of the pension fund's assets in securities admitted for trading at regulated stock markets.

Pillar III Funds

The assets of the voluntary pension fund may be invested only in:

- Government securities – issued or guaranteed by the State,

- Securities admitted for trading at regulated stock markets,
- Municipal bonds,
- Bank Deposits and Mortgage Bonds,
- Real estate and mortgages.
- Other investment instruments.

The assets of a pension fund may not be invested in:

- Securities which are not fully paid in,
- Securities issued by the pension insurance company managing the fund,
- Securities issued by related persons to both the managing pension insurance company and the investment intermediaries appointed.

The assets of a pension fund may be invested in compliance with the limitations specified below:

- At least 50% of the assets of the voluntary pension fund should be invested in securities, issued or guaranteed by the State and/or in bank deposits and municipal bonds.
- Up to 10% of the assets of the voluntary pension fund may be invested in real estate and mortgages.
- Up to 5% of the assets of the voluntary pension fund may be invested in instruments specified as “others”.
- Up to 5% of the assets of the voluntary pension fund may be invested in securities issued by a single company. Up to 10% of the assets of the voluntary pension fund may be invested in securities issued by a single company, upon the permission of the State Insurance Supervision Agency.

The managing pension insurance company and the additional voluntary pension fund are not allowed to acquire more than 10% of the shares from a single issuer or to hold a capital stake enabling the insurance company and the fund to appoint (directly or indirectly) over half of the members of the governing body or to materially influence the decision-making of the issuer.

The pension insurance company may invest abroad up to 10 % of its own assets and of the assets of the pension fund, but only in government securities, in municipal bonds and in securities admitted for trading at regulated stock markets.

Pension Insurance Companies and Pension Funds

□ Pension Insurance Company

Pension Insurance Company has to be a joint stock company registered under the Commercial Code and licensed under the Additional Voluntary Pension Insurance Act. The business name of a pension insurance company shall contain a combination of the words “pension” and “insurance”.

The pension insurance company is allowed to establish only one occupational, one universal pension fund (under the provisions of the Mandatory Social Security Code) and one additional voluntary pension fund (under the provisions of the Additional Voluntary Pension Insurance Act). The pension insurance company

and the pension fund, established by the company are separate juridical bodies. The pension insurance company is responsible with its assets before the insured persons for losses incurred when it fails to meet its obligations.

The founders of pension insurance companies may be both Bulgarian or foreign physical persons and legal entities. In order for the foreign person to be a founder of a pension insurance company in Bulgaria it has to:

- (1) Be registered as a pension, insurance or a financial institution under its national legislation and
- (2) Submit a bank reference by a first-class foreign bank, confirmed by the Bulgarian National Bank.

The pension insurance company can issue only registered book-entry shares of one vote each. It may not issue bonds. The pension insurance company is not allowed to carry out commercial transactions not connected with its core activity. The pension insurance companies are not entitled to participate in public companies, commercial companies and consortiums as unlimited liability partners. It is important to underline that pension insurance is the only object of activities of the pension insurance companies.

The minimum capital of the pension insurance company has to be BGN 3m in cash. The capital should be fully deposited prior to the filing of the application for granting of a license.

When entering into insurance agreements, the pension insurance companies may use the services of insurance intermediaries, physical or legal persons. The insurance intermediary shall not work for more than one pension insurance company. The pension insurance company shall issue each insurance intermediary a document as a legal proof of his powers. Specimen of the document shall be submitted to the State Insurance Supervision Agency. The pension insurance company is obliged to submit a list of its insurance intermediaries to the Agency. For any changes in that list, the Agency shall be notified within 15 days.

□ Pension Funds

Pension funds and pension insurance companies are different legal bodies. The pension insurance companies establish and manage the pension funds. The managing bodies of the pension insurance company manage and represent the pension insurance fund. The name, the seat and the address of the management of the pension fund is the same as the name, the seat and the address of the founding pension insurance company. The business name of a pension fund shall contain a combination of the words "pension", "voluntary" /"universal"/"occupational"/ and "fund". The pension insurance companies are liable with their assets to the insured for any losses stemming out of their responsibilities to manage and represent the respective funds. The pension funds are not liable with their assets for any losses incurred as a result of the activities of the founding pension insurance companies.

Under the AMPI the insured chooses the fund personally. However, if no application is submitted, then the person eligible to be insured is assigned to any of the existing registered funds. The participation of a person in the pension fund may be changed after a year of his registration in the fund.

The pension fund established under AMPI is not allowed to split up or transform into a commercial company, cooperative or NGO. Pension fund established and managed by one pension insurance company can merge with a pension fund established and managed by another pension insurance company according to the terms and conditions prescribed by a regulation of the Council of Ministers. The pension fund cannot cease to exist, except in the case of insolvency. In case of insolvency the amounts accumulated in the individual accounts are transferred to another pension fund by means of a contract between the appointed liquidator and the other pension insurance company.

Under AMPI a custodian council represents the insured in the pension funds. Members of this council are representatives of the trade unions, employers and the pension insurance company. Under AVPI a consultative council represents the insured in the pension funds. The members and the functions of the council are to be determined in the by-laws of the pension insurance company.

4.10.3. Supervision

The Council for Additional Social Insurance is the major decision-making authority in the field of pension insurance. On suggestion of SISA it is authorized to:

- Grant and revoke license for additional social insurance (within the 2-month term after the proposal of the Agency has been made),
- Issue permission for mergers, acquisitions, split up of the pension insurance companies, after permission for the merger or the acquisition is provided by the Anti-monopoly office if needed,
- Open an insolvency procedure for the pension insurance companies,
- Approve the list of the depository banks in coordination with the BNB.

The council has 7 members: the Minister of Labor and Social Policy, the Minister of Health, the Minister of Finance, the Minister of Justice, the Minister of Internal Affairs, the Chairman of the State Securities Commission and the Chairman of the Agency. A representative of the Association of the additional pension insurance companies takes part in the activities of the Council. The Minister of Labor and Social Policy chairs the Council.

State Insurance Supervision Agency (SISA)

The SISA is an administrative structure under the Council of Ministers, which supervises the pension, health and unemployment insurance activity in Bulgaria. Over the pension insurance companies and pension funds SISA exercises both preliminary and current control.

Preliminary control refers mainly to the licensing process, the key objective being – maximum protection for the insured. SISA oversees the compliance of the following documents and issues with what is required by Law:

- the basic legislative acts, regulating the activity of the pension insurance company and the pension funds -the Statute, and the Rules and Regulations of the pension insurance company,
- the samples of insurance contracts,
- the persons, managing the pension insurance company, shareholders, holding over 10 per cent of the equity, as well as the company's actuaries,
- the availability of the minimum required equity,
- the forecasts for the company's activity, including financial and actuarial projections for offered pension schemes,
- the rights of the insured and the insurers as well as guarantees for those on behalf of the insurance institution.

Current control is related to the general and financial supervision over the activity of pension insurance companies and pension funds.

It encompasses current supervision of the financial reporting and the financial standing of the companies and funds, monitoring the segregation of pension reserves, the amount of assets and their investment. Minimum rate of return on investing the fund's assets is expected to be introduced soon to guarantee that the interest of the insured is being taken good care of.

4.11. Main points about Country Analysis of Bulgaria

- Bulgaria has followed a sure path towards a market economy since Prime minister Ivan Kostov of the Union of Democratic Forces (UDF) took office in 1997.
- Since 1997 the severe economic hardship for the Bulgarian people has greatly eased as the lev stabilized and inflation was tamed. Confidence in the Banking system is starting to return with very credible and well-endowed foreign corporate banks (among them and Greek banks) coming on the scene. The Gross Domestic Product (GDP) reached \$12.392 million in 1999 and real GDP grew by 2.4%.
- The Bulgarian government has been operating under a Currency Board Arrangement (CBA) and thanks to the CBA and its associated IMF program, inflation has been cut from 569.7% in 1997 to only 6.2% in 1999. Official reserves rebounded from \$400 million US in January 1997 to \$3.412 million at the end of 1999. Moody' s Investors Service upgrade Bulgaria's credit rating to B2, while Standard and Poor' s raised Bulgaria' s long term foreign currency credit rating to B+ with a positive outlook from B. Foreign investment, including participation by American investors, has also revived as macroeconomic stabilization and friendlier business climate have taken hold. The closure of 18 troubled banks has also helped to increase confidence in the banking system
- Bulgaria has a leading role to play in regional economic and infrastructure integration: more efficient border crossing stations to promote regional trade, European Corridor & road transport links, rail links, and a number of energy and telecommunications projects will keep Bulgaria and some of its neighbors unrelentingly busy improving the overall image and economic prosperity of Southeast Europe.
- The government's campaign against crime and corruption can also enhance Bulgaria's ability to perform on the world's commercial. Bulgaria was the first non-OECD nation to ratify the Anti-Bribery Convention. Additional market-oriented changes have been made to the laws governing foreign investment, taxation and land ownership by international investors.
- Transparency in general has improved and recent developments have shown the Bulgarians to be rededicated to encouraging the highest standards of ethical business practices. The Bulgarian government needs to diminish the role the bureaucratic delays and corruption have had in stifling Foreign Direct Investment.
- Bulgaria has one of the most liberal foreign investments laws in the Balkan region. Foreign investment typically assumes one of the following forms: establishing a joint venture with existing companies, state-owned or private enterprises, acquiring a company through privatization, setting up a new (Green Field) venture or making portfolio investment. Portfolio investment has been minimal (only 0.1% of the GDP in 1999 compared with Direct Investments which reached 7.9% of the GDP in 1999) given the relative lack of development and inefficiencies of the capital markets.
- A lot of work remains to be done. A large part of the responsibility belongs to the Bulgarian government to make the Business climate of the country as desirable as possible. The judicial system must always follow the rule of law and be immune to inappropriate influences. Rooting out corruption is essential and an ongoing task.
- The pace of privatization of thousands of state – owned enterprises, must continue, since privatization is the only practical way for Bulgaria to restructure its economy, create new jobs, and introduce new technology. Privatization is also crucial to efforts to attract Foreign direct investment, halt the slide in production and increase exports to generate revenue to support needed imports. The Kostov government has also recognized the importance of small and medium sized enterprises in creating jobs.

- Bulgaria is still a poor country with average per capita income at under \$1.500 per year. While this limits consumer purchasing power for relatively expensive products, Bulgaria's work force offers attractions to manufacturing investors for its good education, especially in engineering and foreign – language ability. Moreover, the average wage of approximately \$110 per month is one of the attraction for foreign investors interested in production in Bulgaria.
- With the improved economic climate (after 1997), a wide variety of products of all types can now be found in Sofia's increasing number of shops, and the Bulgarian government and some large state – owned enterprises can finance priority imports by themselves. Bulgaria has an active trade show calendar attracting exhibitors from all over the world. Bulgaria is moving forward on USA billion in transport and environmental remediation project Nonetheless, international financing of major infrastructure projects remains essential and Bulgaria is still very dependent on financing from multilateral and other non-Bulgarian sources (such as World Bank, EBRD, EIB e.t.c.).
- The Stability Pact, a comprehensive regional plan for economic development, democratization and security, will lead to new and expanded trade and investment opportunities in Bulgaria over the long term.
- Market access for Greek companies and also for European and U.S companies is improving, but Bulgaria is not yet an easy place to do business. There are several business conglomerates with suspect origins and business practices that yield considerable influence in Bulgarian economy and which the government of Bulgaria is trying to limit. Bureaucratic delays due to ministry reorganization, replacement of senior officials and enterprise advisory boards dictate the need for good relationships building and patience. Tenders occasionally get bogged down for lack of clarity in the rules or even-handed enforcement, but transparency in general has improved. However international investors are less subject to pressures such as bureaucratic delays or corruption than Bulgarian companies.
- Although the Bulgarian government has achieved some successes in the fight against organized crime and corruption, many observers (such as World Bank, IMF, EBRD, etc) believe that corruption and political influence in business decision making continue to be significant problems in Bulgaria's investment climate.
- Finally, as a relatively small market in the Balkans, Bulgaria will have to make extra efforts to attract investors-by providing transparency, for example-as well as by more fully marketing its many advantages including a highly skilled, low cost labor force and proximity to both European and Near Eastern markets.

5. COUNTRY ANALYSIS OF FYROM

5.1. Country profile

5.1.1. Location, Climate, Demographics

The Former Yugoslav Republic of Macedonia (**FYROM**) is situated on the Balkan Peninsula and it is a transport and communication crossroad, linking Europe and Asia. It covers 25.713 sq. kilometers and borders with Bulgaria to the east, Greece to the south, Albania to the west and Federal Republic of Yugoslavia (FRY) to the north. The length of the frontiers is 850 kilometers out of which 262 km with Greece, 232 km with FRY, 191 km with Albania and 165 km with Bulgaria.

There are three border crossings with **Bulgaria**: (1) Deve Bair (Kriva Palanka), (2) Delcevo and (3) Novo Selo (Strumica), three border crossings with **Greece**: (1) Dojran, (2) Bogorodica (Gevgelija) and (3) Madzhitlija (Bitola), four border crossings with **Albania**: (1) Jafasan (Struga), (2) Sveti Naum (Ohrid), (3) Stenje (Resen) and (4) Blato (Debar), and six border crossings with **Federal Republic of Yugoslavia** (FRY): (1) Blace, (2) Tabanovce, (3) Jazince, (4) Sopot, (5) Pelince and (6) Volkovo.

FYROM is predominantly mountainous country. There are 14 mountain peaks higher than 2.000 meters, and the highest is Golem Korab, at 2.753 meters.

There are three large tectonic lakes, 15 artificial ones and 25 glacial lakes located in the highest areas of the mountain ranges dating from the Ice Age.

The largest tectonic lake, Ohrid Lake, with the total area of 349 sq. kilometers, 118,9 sq.k of which belong to Albania, lies at altitude of 693 m. The water of this lake is characterized by its special color and reaches a summer temperature of 24 °C. Its singular natural conditions have made the survival of life forms from the Tertiary Period possible, owing to which Ohrid Lake has often been called a museum of living fossils. The Ohrid Lake is under UNESCO protection.

East of Ohrid Lake, in a beautiful and fertile valley, lies Prespa Lake. At an altitude of 853 m, at the junction of the borders of FYROM, Albania and Greece, this lake occupies an area of 274 sq. kilometers, out of which 49,4 belong to Albania, and 15,6 to Greece. The water temperature reaches between 18 and 24 °C.

The smallest tectonic lake, Dojran Lake is in the south-eastern part of the country. It's area is 42,7 sq. kilometers, of which 15,6 belong to Greece. Lake Dojran lies at an altitude of 148 m and is exposed to the influence of the mild sea climate of the Aegean sea. The temperature reaches up to 27 °C.

Some of the major artificial lakes are: Mavrovo, Globocica, Debar, Tikves, Vodoca, Kalimanci, Berovo, Lipkovo, Mantovo and Strezevo. The 25 glacial lakes are located on mountains Sar, Pelister, Jablanica and Jakupica.

There are 38 thermal mineral springs in FYROM, concentrated at eight spas: Katlanovo, Kumanovo, Kosovrasti (Debar), Stip, Bansko (Strumica), Negorci and Smrdliiva Voda (Gevgelija). The origin of this springs is either juvenile or volcanic, which means that their water comes from the deep red-hot layers of the Earth, reaching relatively high temperatures (72,3 °C at the Strumica Spa). Owing to the high pressure in the depths of the Earth, these waters have absorbed numerous minerals and natural gases which are very important for their use.

The three tectonic lakes, Ohrid, Prespa and Dojran, owing to their natural characteristics, have been protected by law. There are also four national parks in FYROM, Mavrovo, Pelister, Galicica and Jasen forest reserve, protected by law. They cover an area of 130.000 hectares.

FYROM's climate is transitional, regional between Mediterranean and continental climates. Along the valley of rivers Vardar and Strumica the climate in temperate is Mediterranean. The interior has a moderate continental climate with warm and dry summers and cold and wet winters. The openness of the Aegean Sea river basin and the high mountains reaching 2.700 m bring about an influence of the Mediterranean and continental climates, as a result of which there is insufficient rainfall (about 500-700 mm annually), badly distributed throughout the year. The average annual temperature is above +10°C, which is the characteristic of semi-arid areas.

Table 20. FYROM: Country profile

COUNTRY NAME:	- <i>Conventional long form</i> : The Former Yugoslav Republic of Macedonia is used by the United Nations, the U.S.A, Greece and other countries. - <i>Conventional Abbreviation</i> : FYROM - <i>Local long form</i> : Republika Makedonija - <i>Local short form</i> : Makedonija
LOCATION	South-Eastern Europe, bordering with Albania, Bulgaria, FRY, Greece - FYROM has 123 municipalities.
FORM OF GOVERNMENT	Parliamentary Democracy or Emerging Democracy by CIA – Assembly of the Republic of Macedonia, 120-140 seats, elections occur every four years.
CAPITAL CITY	SKOPJE
ETHNIC DIVISION	Country's people 66.6%, Albanians 22.7% Turks 4.0%, Phomas 2.2%, Serbs 2.1%, Vlachs 0.4%Other 2.0%,
OFFICIAL LANGUAGES	Macedonian 70%, Albanian 22.7%, Turkish 3%, Serbo-Croatian 3%, other 3%.
RELIGIONS	Orthodox Christian 67%, Moslem 30%, other 3%.
CURRENCY	Macedonian Denar (MKD)
EXCHANGE RATE	Macedonian denars per US dollar- 64.757 (January 2001), 65.904 (2000) 56.902 (1999) 54.462 (1998)
SURFACE AREA (sq. km)	25.713 thousand sq. km
POPULATION, TOTAL	2.046.209 (2001 estimated)
POPULATION DENSITY (people per sq. km)	79.5 (1999)
POPULATION GROWTH (annual %)	0.43 (2001 estimated)
LIFE EXPECTANCY AT BIRTH, total (years)	74.02 years (2001 estimated)
FERTILITY RATE, total (births per woman)	1.79 (2001 estimated)
MORTALITY RATE, INFANT (per 1,000 live births)	12.35 (2001 estimated)
URBAN POPULATION (% of total)	69.3% (1999)
TIME	GMT+1
COUNTRY TELEPHONE CODE	+389 (FYROM)
CLIMATE	Moderate continental with four seasons. Warm, dry summers and autumns and relatively cold winters with heavily snowfall.
GETTING TO FYROM	Skopje International airport, Passenger train services international: south to Greece and north to Belgrade and beyond.
PUBLIC HOLIDAYS	January 1 & 2, January 7 & 8, April 19 & 20, May 1 & 2, August 2 & 3, September 8, October 11 & 12.

Source: The World Bank Group, *Regions and Countries, Bulgaria*. (<http://lnved18.worldbank.org>)

The territory of FYROM is divided in 123 municipalities. The largest municipalities are Skopje with 545.228, Tetovo with 172.171, Kumanovo with 127.814, Bitola with 108.203 and Gostivar with 108.181 persons. All other municipalities are with less than 100 thousand inhabitants.

Population

According to the 1994 Census, the population of FYROM was 1.945.932 persons, with 59.5% living in the urban areas and 40.2% living in rural areas. For 2001, population in FYROM estimated at 2.046.209

persons. The average population density is 79.5 persons per square kilometer (1999). In 2001 the age population structure is the following:

- **0-14 years:** 22.92% (total 469.064: male 243.715, and female 225.349),
- **15-64 years:** 66.94% (total: 1.369.709: male 688.484, female 681.225),
- **65 years and over:** 10.14% (total: 207.436: male 92.043, female 115.393).

For 2001:

- the number of births rate per 1.000 of the population is 13.54,
- the number of deaths rate per 1.000 persons is 7.7,
- the infant mortality rate is 12.95 deaths per 1.000 live births,
- the total fertility rate is 1.79 children born per woman,
- the life expectancy is 74.02 years (male life expectancy is 71.79 years, and female life expectancy is 76.43 years).

Table 21. Geographic, demographic and social indicators of FYROM, (1996-1999)

Indicators	1996	1997	1998	1999
Land Area (in sq. km)	25.713	25.713	25.713	25.713
Population (in thousands)	1.983	1.997	2.009	2.002
Population growth (% annual)	0.9	0.7	0.6	0.6
Population Density (people per Sq. Km)	78.0	78.5	79.0	79.5
Life Expectancy at birth, total (years)	N/A	N/A	N/A	72.8
Urban population (% of total)	N/A	N/A	61.2	61.6
Per Capita GDP (in USD, at market rates)	2.225	1.852	1.740	1.698

Source: *World Development Indicators, World Bank, (<http://devdata.worldbank.org>)*

Ethnic structure

The total enumerated population in the 1994 census shows that the Macedonian population represents 66.6% of the whole population in FYROM. The nationalities represent the rest of 33.4% of the whole population with 22.7% Albanians, 4.0% Turks, 2.2% Phomas, 2.1% Serbs, 0.4% Vlachs and 2.0% of others respectively.

The proportion of Albanians in the population is significant in Tetovo (74.4%), Gostivar (63.7%), Kicevo (49.2%), Struga (45.2%), Debar (44.4%) and Kumanovo (36.9%).

5.1.2. History

Even in its most distant past, FYROM was a place where different civilizations and religions came into contact.

Classical Period

In the 4th century BC, King Philip II consolidated the ancient state of FYROM.

The Romans began to encroach on the Balkans and after the course of four wars with FYROM in just 66 years finally made it a province in the mid 2nd century BC. The Roman Empire spread further eastwards, eventually establishing its eastern capital at the Greek city of Byzantium (Istanbul) in 330 AD. The city was named Constantinople in honor of its founder, Constantine. The Romans built the Via Egnatia from the Adriatic Sea to the Marmara Sea via present-day Bitola and Thessaloniki.

Beginning in the 5th century AD Slavic tribes from beyond the Carpathian Mountains and Volga and Dnieper Rivers began to settle in Central/East Europe and the Balkans and over the next two or three centuries became the dominant population. In the southern Balkans they occupied the agricultural lowlands and the peoples they displaced were pushed to the coastal and mountainous peripheries.

During the course of these continual migrations and conquests the ethnic composition of the region's population was substantially changed. The southern Balkan area was populated by Slavs, Greeks, Vlachs (Arumanians), Bulgars, Jews and Albanians. Later during the Ottoman conquest in the 14th and 15th centuries Turks and Rhomas (Gypsies) came. More Jews arrived as refugees from the Spanish Inquisition. The Slavs have developed various national identities: Serbians, Croatians, Bulgarians, etc.

Religious trends have been as convoluted as the ethnic. Pagan beliefs of ancient FYROM and the Roman Empire, gave way to Christianization (Eastern Orthodox) during the Byzantine Empire, followed by the penetration of Islam during rule by the Ottoman Empire. The resulting religious, ethnic and cultural cleavages continue to haunt the region today.

The valley of the Vardar River flowing from northern FYROM and emptying into the Gulf of Thessaloniki, as the Axios River, represented the easiest route from the Aegean to the north and served as a gateway to Europe. Consequently, both the Byzantines and Ottomans considered it essential to hold FYROM for strategic and military-political reasons. It was also contested by the Serbians, Bulgarians and others.

Samuel's State

The waves of penetration of the Slavs in the 6th and 7th centuries AD resulted in FYROM becoming a Slav territory. The *sclavinia* was their first form of social organization and structure. Subsequently they fell under the Byzantine and Bulgarian Empires for varying periods. Samuel, a skilled military leader, broke away and established the first post-classical FYROM state, which endured from 976-1018 AD. Bulgaria and FYROM both claim him as their own.

The Archbishopric of Ohrid was established at the time of Samuel and the town of Ohrid became the religious center and capital of his empire. The monks **Cyril and Methodius** from Thessaloniki had devised the first Slavonic alphabet, Glagolitic, from which Cyrillic is derived. The monks Clement and Naum continued the mission of the brothers Cyril and Methodius. Clement founded the Ohrid Literary School, the first Slav institution of higher learning, instructed hundreds of teachers and priests in the Slavonic alphabet, introduced the Slavonic language in religious services and became the first original Slav writer. These monks translated the bible and basic religious service books from Greek into the language spoken by the indigenous Slav population in the region and established the Old Slavonic literature.

Following the tragic defeat of Samuel's army and the fall of his Empire, FYROM was transformed into an ordinary Byzantine province. At the end of the 11th century the Byzantine Balkan territories were attacked by the Normans, then penetrated by the Crusaders and for brief periods subjugated by mediaeval Serbian and Bulgarian states. In the 13th century a Bulgarian king extended his frontier all the way west to the Adriatic, while in the 14th the Serbian King Stefan Dushan ruled from Croatia in the north to the Aegean Sea in the south.

Turkish Rule

The Byzantine (Eastern Roman) Empire held sway off and on for a thousand years until around 1300 when the Ottomans from Anatolia began to encroach on it and finally destroyed it in 1453. The reign of Suleiman

the Magnificent (1520-1566) represented the apogee of Ottoman rule, after which it began a gradual decline under pressure from the Russian and Austrian Empires. The Turks extended their control to FYROM.

The Ottomans established various forms of feudal exploitation, particularly of agriculture. In addition, the local population was religiously and ethnically discriminated against. FYROM as subject to a dual rule: economically and politically by the Sultan, and religiously by the Constantinople Patriarchate of the Greek Orthodox Church. The Turks, however, did not impose the Muslim faith on their subjects, although many Albanians, Gypsies and Bosnians adopted it to gain benefits and advantages of the Turkish society.

The struggle against feudal exploitation and Turkish domination in FYROM took the form of repeated rebellions and insurrections. In 1564-5 the Mariovo-Prilep rebellion took place and in the 17th century *ajduk* (outlaw) companies attacked Osmanli feudal property. In 1689 Karpos organized an uprising. As the economic and political situation deteriorated, the power of the central Ottoman authorities weakened leading to the rise in power of big landowners.

The demise of the Ottoman Empire at the end of the 18th and beginning of the 19th century was accompanied by intensification of national liberation activities and migrations whereby towns acquired a FYROM (Slav) character.

Following its defeat in the 1877-1878 war with Russia and the Treaty of San Stefano, the Ottoman Empire's Balkan territories were considerably reduced. Serbia, Montenegro and Romania were proclaimed independent, and FYROM was annexed to the newly established Bulgarian state. This was quickly overturned by the European Great Powers at the Congress of Berlin held in July 1878, according to which FYROM remained under the authority of the Ottoman Sultan.

As a result of growing national and political ferment, several underground groups sprang up, including the Internal Macedonian Revolutionary Organization (IMRO), which was launched in 1893. The habitants took an active and fierce part in insurrections on their own territory and in neighboring countries. The local nationalists further stirred up the European political scene in 1903 with the Ilinden Uprising and the formation of the short-lived Krusevo Republic, which was suppressed by the Turks after only 10 days. Over these decades bands of militias embodying the region's various ethnic and religious persuasions had used all the tactics of terror and fanaticism which have once again become weapons of some extreme modern causes.

The area has also been torn by various religious currents. During Ottoman rule the Muslim faith prevailed among the Turkish population and those who converted to it, while the Eastern or Greek Orthodox Church held sway over the rest of the people. As the Ottoman Empire disintegrated, national churches in Serbia and Bulgaria, attempted to lay claim to the people in FYROM and to control the priesthood, the churches and the educational system. Only after the Second World War an autocephalous FYROM Orthodox Church was established, which was tolerated by the subsequent, atheist communist regime.

Independence

The dissolution of the Ottoman Empire and the two Balkans Wars (1912-1913) changed the situation in the Balkans, but did not result in freedom for FYROM and the local people. The First Balkan War was fought by Greece, Serbia and Bulgaria against Turkey, while in the Second the three belligerents fought among themselves. With the Treaty of Bucharest, FYROM was divided among Greece, Serbia and Bulgaria. Following World War I, the Treaty of Versailles in 1919 endorsed the previous division.

"Vardar Macedonia" (the territory of today's FYROM, approximately 25.713 sq km, or the size of the American State of Vermont) became part of the newly established Kingdom of Serbs, Croats and Slovenes – later changed to the Kingdom of Yugoslavia – which existed until 1941.

During the Second World War the people of FYROM in the present - day country were organized against the invasion of the Axis Powers and in 1944 liberated most of the territory with their own military forces. On August 2, 1944, the first session of the National Anti-Fascist Liberation Council of Macedonia (ASNOM) was

held and founded the modern FYROM state. The Socialist FYROM became a constituent part of the Socialist Federal Republic of Yugoslavia and was integrated politically, socially and economically into the communist systems established by President Josip Broz, "Tito".

With the collapse of the Union of Soviet Socialist Republics and the breakup of the Socialist Federal Republic of Yugoslavia, the way was open for the Socialist FYROM to pursue its own destiny. On September 8, 1991, a referendum overwhelmingly voted in favor of sovereignty and independence and on September 17th the Parliament affirmed its results, which meant that Yugoslav federal law was no longer effective when it conflicted with FYROM's law. On November 20, 1991, a new Constitution became effective, which proclaimed the "FYROM" as a sovereign and independent state. However, recognition was not immediate or universal.

The country finally was admitted to membership in the United Nations Organization (UN) on April 8, 1993, under the provisional name of "Former Yugoslav Republic of Macedonia" (FYROM) and by now has been recognized by most nations, with the notable holdout of the Federal Republic of Yugoslavia (Serbia and Montenegro). The United States of America has recognized FYROM as an independent country and has established diplomatic relations. A United States Liaison Office, in Skopje (USLO) conducts official affairs. The Agency for International Development (USAID) and the Information Service (USIS) have active operations in FYROM.

5.1.3. Government

The first multiparty elections were held in November 1990, under the old Constitution and an assembly was organized in January 1991, which adopted a Declaration of Sovereignty and at which a President of the Republic was elected, Kiro Gligorov, for a four-year term. The next elections were held in 1994. The existing Government, was elected in November 1998, and the Prime Minister is **Ljubcho Georgievski** from the Internal Macedonian Revolutionary Organization - Democratic Party for Macedonian National Unity or **VMRO-DPMNE**.

The main framework for the transformation of the political and economic system of the country was defined with the 1991 Constitution of FYROM. The basic intention of the Constitution was to constitute FYROM as a sovereign and independent, civil and democratic state, and also to create an institutional framework for the development of parliamentary democracy, to establish the rule of law as the principal system of government, and to guarantee human rights, civil liberties and national equality.

These precepts are summarized in the following basic tenets:

- Basic freedoms and rights of the individual and citizen,
- Free expression of national or ethnic identity,
- Rule of law,
- Executive and judiciary branches,
- Division of powers into legislative,
- Direct and democratic elections,
- Political pluralism and free,
- Legal protection of property,
- Freedom of the market and of entrepreneurship,

- Humanism, social justice and solidarity,
- Local self government,
- Proper urban and rural planning to promote a congenial human environment, as well as ecological protection and development,
- Respect for the generally accepted standards of international law.

On April 8, 1993, FYROM became the 181st member of the United Nations (UN). It has acquired a special guest status in the Council of Europe and a observer status in the Organization for Security and Cooperation in Europe. In April 1993 FYROM was declared a successor to former SFRY in the International Monetary Fund (IMF) and in December 1993, it was declared a member of:

- International Bank of Reconstruction and Development (IBRD),
- International Development Association (IDA),
- International Finance Corporation (IFC)
- and Multinational Investment Guarantee Agency (MIGA).

The legal system is based on civil law. The judicial branch is independent and judges may not hold other jobs or be political party members. There is a constitutional court of nine judges elected by Parliament for a single nine-year term, which is responsible for constitutional issues. There are in addition supreme, higher and lower courts, as well as appeal and municipal courts set up on the European model. A special Judicial Council, elected from the ranks of outstanding members of the legal profession, proposes the election, discipline and discharge of judges. There is a Public Prosecutor's Office. There is also a Public Ombudsman's Office.

The national legislative branch is unicameral and consists of 120 deputies elected by majority suffrage. A vote of no confidence in the government may be passed by a simple majority of deputies. At the local level councils are elected and total some 1.500 delegates throughout the country. There are at present 123 political sub-divisions or communities. Over 50 political parties and associations have been formed, but many of them still are in a period of flux.

FYROM has its own armed forces manned by conscription of draftees and commanded by a professional officer corps, which are oriented entirely at external defense. Police fulfill internal security functions.

In early 1993, the United Nations was invited to station peacekeeping troops on the northern and western borders. Under the mandate of UNPROFOR, subsequently renamed UNPREDEP, a battalion each of United States and Scandinavian soldiers observe and inform on developments which may endanger the security, stability or territorial integrity of FYROM. The danger emanated from the conflicts to the north, particularly that the wars in Bosnia-Herzegovina and Croatia may spill over into the south Serbian province of Kosovo, with its largely ethnic Albanian, Muslim population. In addition, the Organization for Security and Cooperation in Europe (OSCE) has a small mission to monitor risks of spill-over and to evaluate destabilization threats. With the apparent resolution of the above-mentioned major problems, tensions in the area should have been decreased significantly.

The executive branch of the government consists of a president, prime minister and council of ministers. There are 15 ministries and 4 ministers without portfolio (dealing with urgent tasks), and several agencies including the Customs Administration, Public Revenue Office, Payments Operations Service, Privatization Agency, Bank Rehabilitation Agency, Civil Aviation Board, etc. Three of the ministers are vice prime ministers in the same time.

The core economic ministries are: Ministry of Finance, Ministry of Development and Ministry of Economy. The National Bank also plays a very well defined role in the overall economic management. The Ministry of Finance has the responsibility for the central government revenue, expenditure and budget. The budget preparation starts in July, it is being adopted by the Parliament by end December and is effective by January 1 of the current year. The Ministry of Development has the function of formulating the macro-economic and development policy proposals and coordinating the development expenditures. The Ministry of Economy has the regulatory function for facilitating private business development while protecting the public interest. The Ministry of Foreign Affairs has a mandate for external economic relations.

5.1.4. Infrastructure

Roads

FYROM has a network of roads totaling over 9.400 kilometers. The country's strategic locations as Balkans crossroads have attracted international finance to upgrade its motorway network. A number of major projects are in progress, financed by the European Union (EU), European Investment Bank (EIB) and the World Bank. One of the Pan-European Transport Corridors identified by EU for development is the one that connects Thessaloniki, Skopje, Belgrade, Zagreb and Munich. The World Bank is funding a project for Trade and Transport Facilitation in Southeastern Europe, which involves modernization of customs administration, upgrading of information systems to border crossing infrastructure and equipment, and technical assistance for trade facilitation.

Railways

Makedonski Zeleznici operates the railways and maintains over 900 km of lines, 315 km of which are electrified. The main north-south line from Belgrade, Serbia, to the port of Thessaloniki, Greece, on the Aegean Sea, passes through Skopje. There is also a project to construct a new east-west line, which would connect Burgas, Bulgaria, on the Black Sea, with Durrës, Albania, on the Adriatic Sea. The first phase will be construction of a line from Gjuesevo, Bulgaria, to Kumanovo, FYROM to link up the existing lines. The second, more difficult phase will be construction of a line to connect with Albania.

Airports

There are two international airports: "Petrovec" at Skopje and Ohrid. Skopje is serviced by two domestic and several foreign airlines, which have direct flights to and from various West European cities and connections through Ljubljana, Slovenia, and Zagreb, Croatia. The airports are operated by a public company.

Electricity

Elektrostopanstvo na Makedonija (ESM), an independent public utility, integrates production, transmission and distribution of electricity. They have 3 thermoelectric stations with installed capacity of 1.010 MW powered by lignite and oil, 6 hydroelectric stations with installed capacity of 390 MW, 9 distribution hydroelectric stations with installed power of 34 MW, and 2 lignite coal mines.

FYROM forms part of the European electric energy system (UCPTE). Linkages exist with the Federal Republic of Yugoslavia (110/220/400 kV), Greece (150/400 kV) and Bulgaria (110 kV), while the transmission network in FYROM is at three levels: 380, 220 and 110 kV. The distribution network is at 35, 20, 10 and 0.4 kV. Residential use is 380/220 Volt/50 Hz. Ambitious programs envision significant investments to maintain and upgrade systems financed in part by international institutions.

Moreover, privatizations are also discussed for the above only distributor (ESM) in FYROM. Although, the sale is to be realized after the year 2002, potential investors have shown their interest and are having discussions with the government. The government has drawn up an investment program for ESM worth total of \$276 million US for projects to be carried out over the next years, including a new gas-fired thermal energy

plant near Skopje, a new hydropower plant near Debar, renovation of existing hydropower plants and new transmission links with neighboring countries.

Telecommunications

FYROM Posts and Telecommunications (formerly PTT) are organized as independent state-owned companies encompassing postal and telecommunication services respectively. However, great developments have been achieved in the Telecommunication sector with the government's decision, on April 2000, to sell 51% to 66% of the state - owned Makedonski Telekomunikacii (MPT). The sale took place in January 2001 and the final buyer was MATAV that bought 51% stake for 4.3 million Euros

The headquarters offices in Skopje are housed in a modern structure, which has a national and international telephone exchange open to the public 24 hours 7 days a week. The postal network includes 283 offices. Most postal activities are located at the Number Two office next to the Skopje railroad station. The present installed capacity is more than 400.000 telephone lines (21.8/100 inhabitants). Several exchanges in Skopje are digital, although still many equipment and cables are fairly antiquated. MPT intends to extend capacity using fiber optic technology, enabling all new lines to be digital.

Since the Belgrade telecommunications center was cut off upon independence, a mobile terrestrial satellite unit was leased to connect via EUTELSAT to Switzerland. Subsequently an earth satellite station was put into service via INTELSAT AOR to the United States and Canada. To supplement the existing east-west analog transmission system, a new corridor is under construction with the laying of optical cables linking FYROM with Italy, Albania, Bulgaria and Turkey. Direct international circuits connect to 16 countries.

Arrangements with AT&T (an American telephone company) permit the use of their USA Direct and World Connect services. Commercial pager systems and radio telephones cover the whole country. There are several dial-up electronic mail service providers (ITL, INFORMA) and 3 direct, full service Internet connections utilizing satellite dishes: one commercial (ULTRA), one quasi-commercial (FYROM Telecom) and one non-commercial (MARNET: C&M University and the Soros Open Society Institute). The GSM mobile telephony started to operate in 1996 and Roaming service provided for many countries in 1998.

FYROM Telecom has embarked on an ambitious five-year development plan costing \$239 million, which includes adding nearly 300.000 telephone lines for a target density of 33%, an earth satellite center consisting of 3 dishes with diameters of 8 to 15 meters, expanding switching facilities from 10.228 to 26.118 trunks, constructing a cellular network on the GSM standard supporting up to 50.000 subscribers, etc.

5.2. Legislative, Executive and Judicial System

5.2.1. Introduction

After the independence and the adoption of the Constitution in 1991, FYROM constituted as a sovereign, autonomous, democratic and social state.

The Constitution of FYROM defines the FYROM state as a civic state, because it adopts the civil sovereignty as the source of the state government. The Constitution also defines FYROM as a democratic state because the political pluralism, the direct and free elections are the basic values of the constitutional system. According to the Constitution, the rule of law is a fundamental principle of the constitutional order.

The basic human and civil liberties and rights as well as the system of government are the building blocks of Constitution. Human and civil rights and liberties (personal, political, economic, social, and cultural) are of primary importance in the normative part of the Constitution and they are treated in a large number of constitutional provisions.

The organization of the state governance is based on the provisions of article 8 of the Constitution of FYROM, which sets out one of the basic principles of the constitutional framework - the division of the legislative, executive and judicial power. The legislative power is vested in the Assembly (the Parliament), the executive power is vested in the President and the Government of the country, and the judicial power is vested in the courts.

In addition to the above, the organization of the state government includes the following organs: The Constitutional Court, the Public Prosecutor, the Judicial Council, the Public Defender and in certain sense the Council for Inter-Ethnic Relations as an advisory body to the Assembly of FYROM.

- Chief of state: President Boris **Trajkovski** (since December 1999).
- Head of government: Prime minister Ljubcho **Georgievski** (since November 1998).
- Cabinet: Council of Ministers elected by the majority vote of all the deputies in the Assembly. Note: current cabinet formed by the government coalition parties VMRO-DPMNE, LDP and DPA.
- Elections: president elected by popular vote for a five-year term,. Election last held 14 November 1999 (next to be held October 2004). Prime Minister elected by parliament for a four-year term. Election last held November 1998 (next to be held 2002).
- Election results: Boris Trajkovski elected president on second-round ballot. Percent of vote Boris Trajkovski 52.4%, Tito Petrovski 46.2%.
- Political Parties and Leaders:
 - **DA**: Democratic Alternative (president: Vasil **Tupurkovski**).
 - **DPA**: Democratic Party for Albanians (president: Arben **Xhaferi**).
 - **VMRO-DPMNE**: Internal Macedonian Revolutionary Organization – Democratic Party for Macedonian National Unity (president: Ljubcho **Georgievski**).
 - **VMRO- VMRO**: Internal Macedonian Revolutionary Organization – True Macedonian Reform Option (president: Boris **Stojmanov**).
 - **LDP**: Liberal Democratic Party (president: Risto **Gustervo**).
 - **PDP**: Party for Democratic Prosperity (president: Imeri **Imeri**).
 - **SDSM**: Social Democratic Alliance of Macedonia (former Communist Party-president: Branko **Crvenkovski**).
 - **SP**: Socialist Party of Macedonia (president: Ljubisav **Ivanov**).
 - **SRM**: Union of Romanies of Macedonia.

5.2.2.Legislative system

The position, rights and obligations of the Assembly of FYROM are defined in articles 61 - 78 of the Constitution of FYROM.

The Assembly is the representative body of the citizens and the holder of the legislative power in FYROM. The organization and the functioning of the Assembly are governed by the Constitution and by Operating Procedure of the Assembly.

According to the Constitution, the Assembly is composed of 120 to 140 Representatives. The current body of the Assembly number 120 Representatives.

The Representatives are elected for a four year term of office, through general, direct and free elections by secret ballot, in a procedure provided by law. The elections for Representatives are held during the last 90 days of the term of the old body of Representatives or within a period of sixty (60) days following the dismissal of the Assembly.

The Assembly of FYROM performs the following functions (art. 68):

- adopts and amends the Constitution,
- passes Laws and gives authentic interpretation of the laws,
- determines the public taxes and levies,
- adopts the Budget and the Budget Balance,
- adopts the spatial plan of FYROM ,
- ratifies international agreements,
- decides on war and peace,
- passes resolutions concerning the change of borders of FYROM,
- passes resolutions on association and disassociation from union or community with other states,
- issues a notice of referendum,
- decides regarding the state reserves,
- sets up councils,
- elects the Government of the country,
- appoints and discharges judges,
- makes selections, appointments, discharge of other holders of public offices, as provided by the Constitution and by law,
- carries out political monitoring and supervision of the Government and other public offices responsible to the Assembly,
- proclaims amnesties,
- performs other functions, as provided by the Constitution.

The assembly may hold a session if the majority of the total number of Representatives is present at the session. The decisions of the Assembly are valid if such decisions are passed by the majority of the

Representatives present at a session, except as provided otherwise by the Constitution (for instance, 2/3 majority is required for the adoption of the Courts Law and the Local self-government Law).

In performing duties of its own domain, the Assembly adopts, apart from the Constitution and the laws, decisions, declarations, resolutions, recommendations and conclusions.

The right to propose new laws is allowed to any of the Representatives or the Government of FYROM or at least 10.000 voters (qualified proponents), and the initiative to pass a law may be submitted to the qualified proponents by any citizen, a group of citizens, institutions or associations.

5.2.3. Central and Local Government

Central Government

The executive power is vested in the Government of FYROM. Following to the mandatory (which is the President of FYROM) proposal and program, the Assembly elects the Government by majority of the Representatives present in the session.

The Government of FYROM performs the following functions (art. 91):

- determines the policy of exercising the legislation and the other regulations of the Assembly and is responsible for their implementation,
- proposes laws, the budget of FYROM, and undertakes activities concerning its implementation,
- proposes the spatial plan of FYROM,
- proposes resolutions regarding the State reserves and sees to their implementation,
- passes other regulations and by laws,
- determines the principles for the internal organization of the Ministries and other government bodies, directs and supervises their work,
- prepares appraisals of draft laws and other proposals submitted to the Assembly by qualified proponents,
- decides on the recognition of states and governments,
- establishes diplomatic and consular relations with other states,
- passes resolutions on the opening of diplomatic and consular offices abroad,
- proposes the appointment of Ambassadors and Representatives of FYROM, abroad and chief of consular offices,
- proposes the Public Prosecutor,
- appoints and discharges holders of public and other offices provided by the Constitution and by law,
- performs other duties, as provided by the Constitution and by law.

The Government and each of its members report to the Assembly for their work. The Assembly may take a vote of confidence in the Government. The vote of confidence may be proposed by either the Government

itself or by at least 20 Representatives. The vote of confidence is valid if the majority of the total number of Representatives have voted in favor of such decision.

The State administration is composed of the Ministries and other government bodies and organizations, as provided by law. It carries out its functions independently, pursuant to provisions and within the framework of the Constitution and the legislation and is responsible to the Government.

Locally, the state powers are exercised through the regional offices of the Ministries and other organs of the administration.

Local self-government

The chapter 5 of the 1991 Constitution of FYROM, defines the local self-government and guarantees the citizens' rights to local self-government. The municipalities are defined as units of local self-government.

However, the Constitution allows the possibility to establish other basic forms and types of local self-government within the municipalities, particularly considering the tradition of local communities.

The constitutional provisions of articles 114 through 117 determine the main issues of importance for the local self-government, such as the financing, the direct and indirect involvement of the citizens in the decision making process for matters of local relevance, with "particular" mention of the urban planning, public utilities, culture, sports, social and children welfare, pre-school education, elementary education and basic health care.

However, even if the designer of the Constitution has "particularly" enumerated the above areas, the involvement of the local self-government is not fully exhausted; there exists the possibility for direct and indirect participation of the local self-government in other areas, as provided by law.

The Constitution regulates that the city of Skopje is a special unit of local self-government, apart from the municipalities; however, the opportunity for direct and indirect participation of the citizens in deciding on matters of local character in the above and other areas has been set out in consistent manner.

In accordance with concept for the local self-government determined with the Constitution, the constitutional provisions were codified with the Law on Local Self-government, Law on the city of Skopje, Law on Territorial Division of FYROM and Definition of the Areas under the Units of Local Self-government and the Law on Local Elections.

5.2.4. Judicial System

The provisions of articles 98-108 of the Constitution of FYROM, set out the basis of the judicial system. According to those provisions, the judicial power in FYROM is exercised by the courts. The courts are autonomous, independent and judge on the basis of the Constitution, the laws and the international agreements ratified in accordance with the Constitution. The organization of the judicial system is uniform, emergency courts are prohibited; the types of courts, the jurisdictions, the establishment and abolishment, the organization and composition of the courts and the cases administered are determined by law, which is adopted by a vote of 2/3 majority of the total number of Representatives.

According to the Constitution and the Courts Law, judges are elected without time restriction of the term of office. Judges are appointed and discharged by the Assembly, following to a proposal by the Judicial Council.

The judicial power in FYROM is exercised by the Supreme Court of the country, the appellate courts and the courts of general jurisdictions.

The supreme Court of FYROM is the highest court in the state which ensures the uniform implementation of the laws by the courts. In particular, the jurisdiction of the Supreme Court is in reviewing and deciding in on administration cases and appeals in first, second and third instance.

The appellate courts, being the second highest are authorized to decide on: appeals against judgments of the courts of general jurisdictions and resolving conflicts in jurisdictions between courts of general jurisdiction from their region and perform other functions, as provided by law. In the country there are twenty seven (27) courts of general jurisdiction operating as courts of first instance, three (3) appellate courts and a Supreme Court.

5.2.4.1. Judicial council of FYROM

The Judicial Council facilitates the judicial function by providing autonomy and independence of the courts without interference in their work. According to article 105 of the Constitution, the Judicial Council proposes the election and the discharge of judges and determines the proposal for revoking a judicial function in cases provided by law it assesses the professional conduct and ethics of the judges in the performing of their function and proposes two judges to the Constitutional Court of FYROM.

5.2.4.2. Public prosecutor

According to article 106 of the Constitution of FYROM, the Public Prosecutor Office is the only and autonomous government body that prosecutes criminal offences and other deeds punishable by law and it also performs other duties, as provided by law.

5.2.4.3. Constitutional court of FYROM

The Constitutional Court of FYROM is the body of the Republic responsible for the protection of constitutionality and legality. The Constitutional Court performs the following functions:

- decides on conformity of the laws with the Constitution,
- decides on the conformity of other regulations and the collective agreements with the Constitution and the laws,
- protects the freedoms and rights of humans and citizens with respect to the right to believe, conscience, freedom of thought and public voicing of opinions, political association and activity and it prohibits the discrimination of citizens with regard to race, gender, religion, or social or national affiliation,
- rules on conflicts of competencies among the legislative, executive and judicial power,
- rules on conflicts of competencies among the bodies and local self-government units,
- decides on the responsibility of the President ,
- rules on the constitutionality of programs and articles of the political parties and the associations of citizens,
- decides on other matters, as provided by law.

5.2.4.4. Ombudsman

In order to protect the constitutional and legal rights of the citizens where such rights have been violated by the bodies of the government administration and/or other organization with public authorities, the Constitution of FYROM defines the function of the ombudsman.

5.3. Education

The educational system of FYROM is aimed to provide full development of the personality and to enhance his rights and basic freedoms. The educational activity in the institutions and the other forms of non-institutional education is based on the generally accepted values of democratization and humanism. The basic principles are applied by creating equal opportunities to all children in the compulsory eight-year elementary education, education after completing elementary school, equality in the educational system irrespective of ones nationality, sex, social origin, religious affiliation, as well as through the changes of the contents and organizational educational process in the kindergartens, schools, faculties, institutes, etc.

The right of parents to select the type of education for their children is guaranteed. Education in the kindergartens and elementary schools is provided. Special educational groups with instruction in the mother tongue are formed for children of the nationalities (Albanian, Turkish and Serbian). These rights are also guaranteed in the secondary schools. This contributes to the fostering of understanding, tolerance and friendship among children, young people and adults of different national affiliation. The democratic educational processes are intensified by training teachers of the nationalities at different university level study groups and by systematic publishing of textbooks, manuals and other literature for pupils who have instruction in the language of FYROM, Albanian, Turkish and Serbian.

The activity in the educational institutions on all levels, is carried out in accordance with the legislation. Elementary education is compulsory; secondary education on different levels and forms, is accessible to the young people and adults depending on their interest for schooling, especially by introducing cost-free instruction for pupils, college and university. Education is accessible under the same conditions for everyone according to his abilities.

The continuity, the horizontal and vertical connection between particular levels of education, apart from general advancement from elementary to secondary school, is expressed in the advancement from one to another type of secondary school (if there are differences in the curriculum, certain additional knowledge is required), as well as from secondary to college and university education.

The moderate pedagogical contents, forms and methods and the scientific character of the instruction process come to expression in the curriculum and textbooks and other activities. Moreover, the educational concepts, more precisely the curriculum, define the function of the general, skilled theoretical education and practical training, in compliance with the demands of new technology in the enterprises, the vocational and scientific institutions, administrative and other services.

The forthcoming changes of education will strive to improve the quality of the educational process and will continue to make efforts to reach the international standards of knowledge and practical training.

Structure of the educational system

- **Pre-school education** (1-7 years of age): a) Nurseries, b) Kindergartens, c) Infant-schools.
- **Elementary education** (7-15 years of age): a) Classroom teaching, b) Subject teaching.
- **Secondary education** (15-19 years of age): a) High school education, b) Four-year vocational for different occupations, c) Art school, d) Other vocational with programs of shorter duration e) Specialization.
- **Education of adults:** Elementary and secondary school for different occupations.
- **Higher level education:** a) Faculties and institutes b) Two-year colleges.
- **Post-graduate studies:** Masters degree and specialization.

There are ninety (90) secondary schools with more than 77.000 students of which more than 18.000 graduate annually. There are over 250.000 pupils in 1.000 elementary schools of which a tenth graduate each year. Literacy is 89% of persons over the age of ten.

University education

The higher educational system covers two-year studies at the colleges and between four and six-year studies at the faculties of the two universities in FYROM. The higher educational curricula are developed by relevant Teacher's Councils while the university also gives its opinion, as well as the competent ministry.

Besides instruction for students at the university institutions, scientific and research activity in different fields is organized, as well as permanent staff training.

There are two main universities: (a) St. Cyril and Methodius University in Skopje, which has twenty- four (24) faculties (departments) and ten (10) research institutes, and (b) St. Clement of Ohrid University in Bitola, which has three faculties. Together they have over 1.300 teaching staff. There are about 30.000 students in higher education, of which more than 24.000 are full time. From 2.500 to 3.000 graduate each year, and more than 100 get advanced degrees.

Full-time or part-time students enroll in the first year in the colleges and faculties. After secondary school, approximately 27% of the students enroll in the faculties. The conditions for enrollment of new students are established by the university educational institutions and the candidates that apply are with high school education and other four-year vocational and art schools. The interest for studies exceeds the planned enrollment number. In recent years, the students who meet the conditions but are not included in the number determined in the announcement, pay a tuition fee, and thus additional sources are provided.

Due to the limited enrollment number, a ranking procedure is implemented depending on the candidates' grades in secondary school and the results achieved in the entry exam. The same criteria is applied both for full-time and part-time students. If ranking the candidates it is shown that at least 10% out of the total number of chosen candidates are not members of the nationalities, the candidates who meet the conditions but have lower grades (at least 60 points), are also enrolled. Due to this measure, the natural structure of the students has been improving in recent years.

The Law on Higher Education, presently in parliament procedure, will create a legal basis for reform of university and higher education. It stipulates that five-year programs are to be adopted for the activities and development of the universities and higher educational institutions established by the state. It also sets forth that funds are to be provided by the state and other sources.

Vocational education

The technical and other vocational schools educate technicians for different occupations and other professional staff with secondary education. In some fields, such as construction, agriculture, building mechanization, etc., there are programs with shorter duration (from several months up to three years) for training for different occupations and crafts. The network of schools is well-developed except for the technical courses, agriculture, economics, medicine, food-stuff, textile and other profiles. The contents for technical and other vocational schools are systematized by occupations (according to the character of education and its function).

The curriculum for the technical and other vocational schools specifies the type, level and duration of the secondary education. As by rule, the curricula refer to several related occupations, but there are also for each specific occupation. The secondary school curricula provide general education, vocational and theory subjects and practical training. The relationship between the general and vocational education is conceptualized according to the type of occupation. The curricula is the same both for the regular students and the adults.

The final exam in vocational education (4-year and 3-year) consists of elaboration of a theme or practical examination and written exam in mother tongue and literature. The contents of the practical part depend on the kind of vocational education the student had taken. The certificates of the technical and other vocational schools provide the right for entrance examinations at the relevant faculties, universities and colleges. A considerable number of students exercise this right.

The schools of arts (music, ballet, applied art) last four years. In these schools, the pupils acquire general and vocational education from the relevant field of art. Students enter these schools by taking an entrance examination, the purpose of which is to test their skills. At the end of schooling, the students take a final examination and are entitled to enroll in the university.

5.4.FYROM's Economic Environment

5.4.1.History - Economic Outlook of FYROM

Over the period 1989-1995, the economy of the FYROM underwent a constant contraction. The cumulative GDP has decreased by almost 50%, the external trade deficit has been increasing as well as the unemployment level.

After its independence in 1991, FYROM inherited adverse economic trends, mainly expressed through dropped output (the 1996 output is about a half compared to 1989), enormously high inflation, followed by a daily evaluation of the domestic currency (amounting to 86% monthly rate in April 1992 - the month of establishing the monetary independence), decreased employment in 1996 for more than one third compared to 1989 when it was at maximum, maintained low levels of export and reduced total investments of about two thirds compared to those of 1989. The wages significantly decreased and the employment in 1996 approached 37.4% (537.592 people employed) of the total active working population (which was 1.436.603 working age people in 1996).

Within that period, however, FYROM implemented deep reforms, as a result of which the macro-economic stability, measured by low levels of inflation and foreign exchange rate stability, was achieved. The foreign debt was being regularly serviced. The structural reforms were also successfully implemented. Within this context it appeared that FYROM had the natural and human resources necessary to transform its economy and its political system.

The seven year trend of declining output has finally been stopped in 1996 and the first positive changes in the economic sectors became visible. This trend has also continued until 1999 before the Kosovo crisis.

Major Economic Indicators for the years 1992-1996

In 1998 the major economic indicators started to demonstrate an obvious revival of FYROM economy which shows a positive growth for the first time after 1990. Besides this fact, because of the more favorable environment in the region, as it was pointed out, the future prospects are more favorable than in the previous years of reform.

TABLE 22. Basic Economic Development Indicators of FYROM (1992-1996)

	1992	1993	1994	1995	1996
GDP growth rates - total	-7.99%	-9.05%	-1.89%	-1.16%	0.86%
Structure of the Economy					
Industry	-15.81%	-14.39%	-7.07%	-7.72%	4.42%
Agriculture	-0.25%	-20.44%	9.29%	4.25%	-3.26%
Trade	-30.16%	41.83%	9.24%	-8.10%	-0.08%
Labor Force					
Employees - total	446.117	421.028	395.686	356.617	537.592
Unemployed	172.089	174.848	185.906	216.222	251.490
Investments -total	-29.5	-8.5	-18.6	8.5	4.1
Foreign Trade					
Export of goods	9.4	-12.0	2.9	10.8	-4.7
Import of goods	-5.3	-0.6	23.7	15.8	-5.4

Source: *Statistical Yearbooks - Statistical Bureau of FYROM, 1996.*

The rise of the investments in the country has started to show an increasing trend in 1995. However, as a result of the foreign trade, trends expressed by faster increase of imports than exports, the worsening of the balance of payment occurred.

Also it has to be mentioned that starting from 1996, with the support of the World Bank, the government has undertaken a specially designed **Social Reform Project**, part of which are the employment and re-deployment components. The project also contains establishment of several institutional ways of settling the unemployment problem. In addition, a project on the development of small and medium sized enterprises, financed by the EU PHARE program, initiated by the end of the year 1996. All these activities were designed to relax the tight situation with the unemployment, as mentioned before, which is an unavoidable issue during transition periods.

5.4.2. Present - Economic Outlook of FYROM

Simultaneously with the overall transition efforts, after independence, FYROM had to face the challenge of deep institutional transformation. Being one constituent part of Former Federal Yugoslavia, it already possessed many institutions. They had, though, to be restructured and provided with the decision making power. However, the core institutions of an independent state did not exist and they were to be established. A lot of effort was put at capacity building throughout the public administration. What can be now stated is that the country has made remarkable progress in this respect, especially having in mind the extremely difficult circumstances it was in.

At dependence in November 1991, FYROM was the least developed of the Yugoslav republics, producing a mere 5% of the total federal output of goods and services. The collapse of Yugoslavia ended transfer payments from the center and eliminated advantages from inclusion in a de facto free trade area. An absence of infrastructure, United Nations (UN) sanctions on its largest market Yugoslavia, and Greek economic embargo hindered economic growth until 1996.

After a generally good performance in 1998, the FYROM economy suffered a setback in the first half of 1999, mainly owing to the Kosovo crisis. The impact of the crisis, however, was less severe than initially feared. With the ending of the conflict in early June economic activity picked up markedly and the balance of payments improved. The stance of financial policies was generally prudent in 1999, and inflation remained low. Structural reform initiative resumed in the second half of 1999, but the follow-through was weak because of uncertain political climate.

A broad-based pickup in economic activity in the wake of the Kosovo crisis was key to GDP growth of 2.7 % in 1999. Unlike the experience of the previous years, an improvement in net foreign demand was major

driving force behind the growth performance. Domestic demand was sluggish, mainly owing to erosion of investor confidence. Consumer Prices declined in the course of the first seven months of the year 1999 because of lower food prices. Thereafter, inflation turned positive (6% for 2000) with the firming of food prices and higher oil prices. Unemployment fell slightly, but the rate remained high at 32.4% in 1999.

The balance of payments position in 1999, and indicators of external vulnerability remained satisfactory. The current account deficit (excluding grants) narrowed sharply to 6% of GDP (from 9.5 % in 1998), as both exports and imports declined for the year as a whole. After a severe trade disruption during the Kosovo crisis, exports and imports picked up strongly with the ending of the conflict. Service receipts also surged in the second half of the year, with FYROM serving as a key transit route for travel and delivery of goods to Kosovo. The capital account surplus contracted, as the FDI inflows experienced in 1998 were not sustained. With a sizable amount of unrecorded inward transactions, many of them Kosovo-related, gross official reserves increased by about \$125 million to the equivalent of 2.7 months of next year's imports at the end of 1999.

Table 23. Basic Economic Indicators of FYROM (1996-2000)

Economic Indicators	1996	1997	1998	1999	2000
	Percentage (%) of Change				
Real GDP (%)	1.2	1.4	2.9	2.7	5.1
Consumers prices , period average	2.3	2.6	-0.1	-0.7	N/A
Real wages, period average	0.5	0.2	3.8	3.6	N/A
Unemployment rate (average)	31.9	36.0	34.5	32.4	N/A
	(In percentage (%) of GDP)				
Government Finances					
General government balance (accrual)	-0.5	-0.4	-1.8	0.0	N/A
Central government balance (accrual)	-0.7	-1.2	-0.9	0.9	N/A
Government debt	41.5	48.1	45.7	53.2	N/A
Balance of Payments					
Trade balance (% of GDP)	-7.2	-10.4	-12.0	-11.9	N/A
Current Account Balance (% of GDP)	-6.5	-7.4	-8.8	-4.0	N/A
Official gross reserves (\$mil US)	267	280	334	458	N/A
External debt to GDP ratio %	25.4	31.5	41.1	43.3	N/A

Source: IMF Country Report No.00/72, June 2000, page 4.

5.4.3. Demand and Supply

Following a long recession in the first half of the 1990s, real economic growth turned positive in 1996 and accelerated to 2.9% in 1998, the highest growth achieved since independence. In 1999, despite the Kosovo crisis, growth was estimated to have slowed down only slightly. However the pattern of pectoral growth dramatically changed in 1999, on the demand side, net foreign demand became a major driving force, while on the supply side industry relinquished its growth-leading role to construction, communications and trade sectors.

According to the IMF country report No.00/72, in June 2000, following two years of rapid growth of FYROM, **domestic demand was sluggish in 1999**, reflecting a significantly lower inventory accumulation and continued weak fixed capital formation. The investment environment deteriorated with onset of the Kosovo crisis in the first half of 1999. Trade disruptions adversely affected the import intensive investment in equipment and machinery. This was partially offset, however, by a surge in investment in construction, which accounts for about one half of the fixed investment.

While the deteriorating in Federal Republic of Yugoslavia (FRY) adversely affected the investment behavior in the country, the low investments growth in the past decade reflects a number of structural factors, which are: (a) weak domestic savings and limited access to foreign resources, (b) lack of a development domestic capital market that limited the availability of longer-term financing for investment, (c) high level of real

interest rates, (d) inefficiencies in the banking system, which continuous to channel scarce financing to unviable enterprises through connected lending or at the behest of the government and, (e) the slow pace of structural reforms, as private sector firms in FYROM have tended to substantially outspend the state-owned enterprises in investment. (For example, investment of public enterprises declined by 1.5% in 1998, whereas private sector investment grew by 13.3% and its share in total investment increased from 49.5 % in 1996 to 57.1% in 1998).

Consumption growth accelerated in 1999, reflecting mainly the jump in the growth rate of government consumption (from about 4% in 1998 to 10.1% in 1999) due to increased expenditures on refugees. This more offset the slowdown in private consumption as uncertainties in the region encouraged precautionary savings. The downward trend in net foreign demand was abruptly reversed in 1999, as Kosovo related disruptions in trade in a severe compression of imports. As a result, unlike in the previous years, net foreign demand was the driving force behind the overall growth in 1999.

On the supply side, growth during 1996-1998 was spurred by a strong pickup in industry and a gradual recovery in transport and communications. Following a sustained decline averaging over 12% a year during the period 1991-1995, industrial output recovered in 1996 and grew at an average rate of 4% over the period 1996-1998. Industrial growth was helped by a number of favorable developments, including:(a) the reactivation of the capacities, especially in the iron and steel and metal processing industries following their divestiture to foreign strategic investors in 1998 and (b) increased access to foreign markets, particularly after the trade cooperation agreement was signed with the E.U in November 1997.

There were signs already in 1998, however, that structural weaknesses in the enterprise sector, as well as developments in the neighboring FRY, and important export market for industrial output in FYROM (*the sectors that traditionally export to the region have suffered most in 1998. For example production of construction materials in 1998 fell by 2.1%, beverages by 7.8% and electrical equipment by 9 %*), stood in the way of sustained economic growth in the industrial sector. The outbreak of the crisis in Kosovo in mid-1999 delivered a major blow to industrial production in 1999, which is estimated to have declined by 2.5% for the year as a whole. The decline occurred despite the pickup in production following the surge in Kosovo-related demand.

Several sectors benefited in the aftermath of the Kosovo crisis, and they took up the growth –leading role played in the previous years by industry. These were trade, transport, communications and construction, which together contributed 2.7% points to GDP growth in 1999, with the remainder distributed relatively evenly across the remaining sectors (excluding industry).

5.4.4. Structure of the economy – economic indicators (1995-2000)

The following table shows the key economic indicators of FYROM for the years 1995 and 1997 until 2000.

Table 24. Economic Indicators of FYROM by years (1995-2000)

INDICATORS	1995	1997	1998	1999	2000
GDP at market prices (current \$ US)	2.5 billion	3.2 billion	3.4 billion	3.5 billion	3.6 billion
GDP growth (annual %)	-1.1	1	2.9	2.7	5.1
GNI, Atlas Method (current \$US)	N/A	2.8 billion	3.1 billion	3.3 billion	3.5 billion
GNI, per capita Atlas method (current \$US)	N/A	1,410	1,540	1,660	1,710
Gross capital Formation (% of GDP)	20.8	22	23	21.4	N/A
Money and quasi money growth (annual %)	11.7	23	13.0	32.0	21
Inflation (% of CPI)	15.9	4.4	0.8	-1.1	6
Structure of the Economy (in % of GDP)					
Agriculture, value added	13.2	13	12.2	11.6	11.8
Industry, value added	32.5	34	35.0	35.2	33.1
Services, value added	54.3	53	52.8	53.2	55.1
Foreign Trade (in % of GDP)					
Exports of goods and Services	33.0	37	43.5	41.5	N/A
Imports of goods and Services	42.8	50	58	55.7	N/A
Consumption (in % of GDP)					
Private consumption	N/A	N/A	N/A	73.8	N/A
General Government Consumption	N/A	N/A	N/A	19.0	N/A

Source: World Development Indicator, World Bank Group, (<http://sima-ext.worldbank.org>)

Inflation

Inflation has been fluctuating dramatically over the past seven years, starting from hyperinflation (in 1994 inflation was 121.8%) giving way to deflation (in 1999 inflation was -1.1%) and finally stabilizing at normal rates in 6% for 2000. The negative sign of the inflation rate over 1999, reflects the tightness of monetary policy even though it was election year. Other causes included, restrained consumer demand and drop by 10% for prices of basic agricultural items following harvest. In 2000, inflation rose to about 6% reflect in higher oil prices and the effects of the introduction of VAT in April 2000. Estimations by IMF, show that inflation will drop to 2 – 3% in 2001.

Table 25. Key Economic Ratios of FYROM, in percentage of GDP

Key Economic Ratios	1990	1999	2000
GDP (\$ US billions)	N/A	3.5	3.6
Gross Domestic Investment /GDP	19.0	21.4	N/A
Exports of Goods and Services /GDP	25.9	41.5	N/A
Gross Domestic Savings /GDP	8.9	7.1	N/A
Gross National Savings / GDP	N/A	17.3	N/A
Current Account Balance /GDP	N/A	-0.4	-0.5
Interest Payments /GDP	N/A	1.9	1.8
Total Debt / GDP	23.8	41.5	37.9

Source: World Bank Group, (<http://worldbank.org/data>)

Gross Domestic Product (GDP)

After a slow recovery in 1996 and 1997, following the recession of the early 1990s, the 2.9% annual growth recorded over 1998 was final the proof that the country's economy is back on track. Although less than the 5% originally targeted, this rate of growth is a far indication of a country-wide recovery that took place over 1998 showing a little effect from the Russia crisis. Indeed, over 1998 the country was successful in re-orienting trade towards the EU and away from traditional but economically underdeveloped trading partners such as Serbia. The economy grew strongly in 2000 at a rate of 5.1%, thereby continuing the recovery that

became evident soon after the end of NATO bombing Yugoslavia in June 1999. Most of the recovery is concentrated in the western part of the country reflecting large increase in construction, trade and services.

Table 26. Average annual growth of main Structure Economic Indicators of FYROM

Average Annual growth of main Structure Economic Indicators	1990-2000	1999	2000
GDP	-0.3	2.7	5.1
GDP per capita	-0.9	2.1	4.6
Exports of Goods and Services	3.1	2.5	N/A
Imports of Goods and Services	7.2	2.8	N/A
Agriculture	-0.4	0.7	N/A
Industry	-4.7	0.4	N/A
Services	0.1	4.7	N/A
Private Consumption	0.7	3.3	N/A
General Government Consumption	-0.3	10.1	N/A
Gross Domestic Investment	2.2	-16.5	N/A

Source: World Development Indicators, World Bank Group, (<http://worldbank.org/data>)

The country's biggest achievement lies on the fact that it managed to survive after the break up of Former Yugoslavia. However, it was badly hit within the transition period, not only because of the restructuring inevitably happening in these turbulent times, but even more, because of the loss of the former markets, because of the imposed embargoes and the risky political environment the country was in for several years after the independence. These were the reasons why the economic output contracted. These uneven trends of economic activities in the country provoked also some sector movements with a slight increase of the role of trade, agriculture and some other sectors and decrease of the role of industry in the overall structure of GDP and the total value added in the country.

Industry

At the end of the Second World War, FYROM was a typical agrarian and underdeveloped country, only small-scale handicrafts and very few small manufacturing industries were carried on in the towns. Over the next 40 years under the aegis of the Socialist Federal Republic of Yugoslavia, by the end of eighties, investment poured in and growth averaged 5.3% annually causing the gross domestic product (GDP) to be magnified by 8 times. Industrial production grew at over 8% annually and doubled its share of GDP, while the service sector's share grew by 50%.

Since then, the economy has experienced declines in almost all parameters. The breakup of former Yugoslavia, the loss of markets, the transition to a free market and an open society, the sanctions, droughts, etc., have all contributed to this predicament. Many of the industries who were dimensioned to serve all of former Yugoslavia or export markets, were lost and only now just reopened. However, it seems that the bottom in the economy has been reached and the positive growth commenced in 1996, with the 3.2% industrial production annual growth rate. The trend continued in 1997, so that 1997 industry production was 1.5% higher than 1996 level.

In the light of what was previously noted about the significance of the industry for the GDP, it is important to have more insight into the industry structure. The industry structure will be presented through the presentation of the so called **Social Product figures**. Table 27. presents the structure of industry for the years 1989 and 1995 and estimates for 1997. The 1989 is the last year when the industry production was still increasing, so that, in a way, it shows the potential of different industries, whereas, 1995 is the last year when official (non-estimated) data for different industries are presented by the Statistical Bureau.

TABLE 27. Social Product of the Industry by Sectors (current prices¹)

SECTOR	Thousand of dinars	% of Industry SP	Thousand of denars	% of Industry SP	Thousand denars	% of Industry SP
	1989		1995		1997 ²	
INDUSTRY - Total	6.846.204	100.00%	47.204.879	100.00%	49.446.167	100.0%
Electricity	401.468	5.86%	7.240.086	15.34%	7.535.767	15.2%
Coal	70.869	1.04%	60.035	0.13%	59.030	0.1%
Oil derivatives	86.268	1.26%	1.374.420	2.91%	4,648,000	9.4%
Iron ore	25.312	0.37%	50.771	0.11%	-	-
Black metallurgy	351.927	5.14%	1.211.655	2.57%	1.808.240	3.7%
Non-ferrous metals ores	127.978	1.87%	1.027.408	2.18%	1.032.897	2.1%
Non-ferrous metals	135.296	1.98%	904.449	1.92%	1.062.778	2.1%
Non-ferrous metals products	48.080	0.70%	171.855	0.36%	151.245	0.3%
Non-metal ores	51.529	0.75%	376.847	0.80%	448.937	0.9%
Non-metals products	192.882	2.82%	587.198	1.24%	526.448	1.1%
Metal-works	335.279	4.90%	1.676.759	3.55%	1.627.028	3.3%
Machine-building	154.558	2.26%	552.138	1.17%	395.750	0.8%
Electrical machines and appliances	448.684	6.55%	2.136.940	4.53%	2.155.816	4.4%
Chemical products	226.964	3.32%	2.437.231	5.16%	2.612.523	5.3%
Construction materials	156.591	2.29%	2.180.623	4.62%	2.092.469	4.2%
Timber	25.912	0.38%	242.241	0.51%	177.199	0.4%
Furniture	165.882	2.42%	860.071	1.82%	470.286	1.0%
Garments	892.880	13.04%	3.833.562	8.12%	2.808.454	5.7%
Leather and fur	126.489	1.85%	623.303	1.32%	489.024	1.0%
Food	517.942	7.57%	5.241.293	11.10%	5.036.479	10.2%
Beverages	200.173	2.92%	3.224.474	6.83%	4.599.759	9.3%
Tobacco	355.034	5.19%	3.565.202	7.55%	3.144.806	6.4%
Graphical industry	44.056	0.64%	867.251	1.84%	648,155	1.3%

Source: Statistical Bureau: Statistical Yearbooks of FYROM and Preliminary Data, 1997.¹: Except 1997 figures, which show the industry product in 1995 prices.²: Estimates (1995 prices).

Ferrous and non-ferrous metallurgical industries were developed based mainly on serving export customers. The Skopje Steel Works has an annual capacity of 1.2 million tons of hot and cold rolled sheet metal. Other plants can produce ferrous alloys, seamed tubing and ferrous-nickel products. Other installations produce lead, zinc, copper, gold and silver. Their share of social product resulting from mining and industry in 1989 was about 13.6% and it declined to 9.2% in 1995. Metal fabrication, vehicles and electrical equipment industries manufacture various structures including buses, castings, batteries, cable, pumps, etc., while others produce household appliances, etc. Machinery for metal, wood and plastic processing industries is available. This segment's share of social product's industrial activity in 1989 and 1995 was about 17.1% and 11.4% respectively.

Basic and process chemical industries have accounted for about 9.4% of industrial social product in 1995 as compared to 6.2% in 1989. Capacities exist for basic chemicals, polyacrylonitrile fiber, polyvinyl chloride, as well as detergents, fertilizers, polyurethane foams and fibers. Pharmaceutical and cosmetics firms are well established.

The textile industry, including fibers, fabrics and finished products, is a major employer and contributor to industrial social product, although its contribution to the industry social product has been sharply decreased (from approximately 25.2% in 1989 to only 11.7% in 1995), showing the big problems this sector is facing especially with the loss of markets. Cotton thread and fabric, denim cloth, wool yarn, fabric and knitted fabric, are the principal products. Ready-made clothing production has increased in response to demands from European and North American markets for quality merchandise at reasonable costs. A significant leather and leather-processing industry exists. Pig, calf, cow, bull, lamb and sheep skins are all processed for the local manufacture of furniture, clothing and shoes. With capacities for annual production of 7 million pairs of shoes, this industry has been a major export earner.

The construction and building materials industries rely on domestic raw materials: feldspar, calcium carbonate, bentonite, crumbled and micronized quartz, perlite, etc. Outputs include china, tile, sanitary ware, asbestos, cement and cement products, as well as gypsum and gypsum products.

Food and beverage processing are highly developed: flour milling and baking, canned and bottled fruits and vegetables, bulk and bottled wines; beer malt and beer. Skopje Brewery is very often ranked as the most successful enterprise in FYROM several years in a row. Besides brewing beer they also are a licensee of Coca-Cola. However, if one compares the food and beverages sector to the opportunities (natural and others) which exist there, it is far from having utilized its full potential.

Agriculture and Livestock

After World War II, 75% of the population was engaged in agriculture, today it is about a sixth, though it still accounts for about **12-14% of Social Product**. Total agricultural land is 1.3 million hectares, 43% of which is arable, 4% is in vineyards and orchards, and the rest is meadows and pasture. Only about 10% is irrigated. Over 80% of agricultural land and production is in private hands.

FYROM's agricultural development has been based on its favorable weather conditions, fertile soil, skilled technological resources, irrigation systems, mechanization and qualified personnel.

Crop production in 1996 in thousand tons included: wheat (269), maize (142), sugar beet (78), rice (22), sunflower (21), tobacco (15), tomatoes (146), peppers (121), cabbage (51), apples (65), grapes (215). Early-market garden vegetables produce over 500.000 tons annually: tomatoes, cucumbers, peppers, cabbage, beans, melons, etc. Almost 2 million hectoliters of beer, wine and brandy are produced. Health foods are increasing in importance: honey, mushrooms, cereals, etc. Two of the country's industrial crops are world-wide recognized. They are tobacco, especially the one grown around the town of Prilep, which is being used for blending with the Virginia tobacco in brand-name American cigarettes and the opium poppy, grown for medicinal extraction around Kumanovo, Strumica, Gevgelija and some other towns, which is of the highest quality in the world and is a basis for the pharmaceutical industry.

Figures for livestock in 1996 in thousands are cattle (295), pigs (192), sheep (1.814), horses (66), poultry (3.361). Some milk and cheese are imported and there is export potential for goat products. One of the country's major agricultural exports is the lamb.

More than 37% of the area of FYROM is covered by forests and nature preserves. Forests are a source of wood for fuel and timber for furniture and construction industries.

Natural Resources

FYROM has a complex geological structure and a large number of ore deposits, including reserves of lead-zinc, copper, nickel, besides coal, decorative and architectural building stone, and non-metallic minerals. Deposits of non-ferrous metals and minerals are very significant and present good opportunities for exploitation. Bentonite, fire-resistant clays, gypsum, quartz, opalite, feldspar are among the ones which have special significance for the economy. Some of these are world-wide known for their purity and quality.

FYROM is a significant producer of non-ferrous metals. It contributes 2% to the world's production of lead and zinc. Geological reserves of lead and zinc ore amount to more than 42 million tons, and the potential reserves are assessed at over 85 million tons. The existing capacities for mining and flotation are 2 million tons annually. Mines which are now being exploited are Zletovo, Sasa and Toranica. The capacity of the metallurgy for processing the ores is 110.000 tons annually. The main plant is the Zletovo Smelter, located in Veles. The Bucim copper mine is the principal producer of copper ore, producing 4 million tons annually. Nickel-ferrous ore is being produced in the Rzanovo mine, which is processed in Fenimak - Kavadarci. Some precious and rare metals and elements can be found close to the deposits of lead and zinc: gold, silver, wolfram, cobalt, cadmium and others.

The total proven reserves of decorative and architectural building stones amount to 16 million cubic meters. Marble is the most significant stone, whose quality and variety of colours make it famous all over the world. The most famous marble producer in FYROM is Mermeren Kombinat from Prilep. Other stones being found and produced are travertine, igneous rocks, breccia opal, onyx, granite, schist etc.

It is worth noticing that the soil is abundant with different non-metallic raw minerals. Out of the total of 60 non-metallic raw minerals known now in the world, 46 have been discovered in FYROM. Unfortunately, for some of them, the geological conditions are not favourable, so that their production is not viable so far. As long as the proved reserves and production of dolomite, lime, quartz, bentonite, diatomaceous earth, perlite, gypsum is concerned, they offer a lot of opportunities for viable investment. Many precious and semi-precious stones can also be found, but they have not been studied systematically so far.

Four-fifths of energy needs are satisfied by domestic production of thermo- and hydro-electric power, the deficit is imported from FRY and Bulgaria. The installed capacities of thermoelectric power stations is 1.010 MW and 390 MW of hydroelectric power stations. Their annual production amounts 6.400 GWh. Oil and derivatives must be imported, though there is a crude oil processing refinery. A natural gas pipeline has been constructed to carry Russian gas from the Bulgarian border to Skopje, which will substitute for a substantial amount of imported oil.

The total energy potential of the country's rivers is 5 billion kWh, out of which, 3 billion kWh can be used, but in fact only 25% of the potential is being used. Some new projects will help better use the water resources in the country. Such are the projects for building hidro-electric power stations in Kozjak, Boskov Most, Gradec, and probably one of the most complex ones is the Vardar Valley project, comprising of many different elements. FYROM is also rich with geothermal and thermo-mineral waters. With proper equipment, the quantity of water amounts to 700 liters per second with temperature ranging from 60°C to 100°C. These waters are used and can be used even more for agriculture and tourism.

Construction and Trade

Construction has had a long tradition in FYROM: craftsmen, workers and companies have been active throughout the Balkans and indeed the world. The industry is very capable and highly developed, but has experienced a recession in recent years for reasons mentioned elsewhere. Projects undertaken have included hydroelectric power plants, irrigation systems, airports, hotels and hospitals, roads and bridges, etc.

Trade and services are the segments of activity which have shown the most immediate impact of a reorientation to a market economy. The phenomenal growth in number of organizational units (from 5.000 in 1990 to over 100.000 in 1997) is largely attributable to the formation of new private (domestic, foreign and mixed) enterprises in these segments. Unfortunately, the influx of foreign tourists has fallen off. Still, the trade and services segments represent nearly a quarter of Social Product.

What is hard to measure is the extent of unregistered businesses and the size of the so-called "**Gray Economy**", which has flourished in recent years and is becoming a serious problem. Some analyses estimate the level of the informal economy to be somewhere between 30% and 40% of GDP. The Government has announced its intention to bring it under control.

5.5. Foreign Trade and Customs Regulations

5.5.1. General provisions

FYROM, as one of the former socialist republics of Yugoslavia, participated in the then system of administered trade. That has changed since it was recognized as a separate and independent country. The government monopolies on exporting and importing and foreign exchange control have been replaced by a new system where private enterprises are allowed to engage in trade and all major banks are licensed for international operations using their own foreign exchange. Although the system has been still and subject ed to certain regulations and restrictions, it is evolving into a more free and liberal system. Changes and modifications are occurring at a frequent rate.

The Foreign Trade Law and amendments published in the Official Gazettes numbered 31, 41 and 78 in 1993, currently regulate foreign trade. Export and import of goods can be executed freely on the basis of a customs declaration. Enterprises have to be legally established in order to conduct foreign trade activities. When drafting contracts, they have to specify the manner, conditions and source of financing for the relevant importation. A certificate from the authorized bank must be also submitted together with the customs declaration, as proof that the necessary foreign currency for payment has been secured. This certificate is not required for customs purposes in the following cases: 1) Imports for compensation deals, 2) Import for export, 3) Import and then export with added value, 4) Import in goods value (import paid with export), 5) Import of equipment under lease, 6) Temporary import of goods for consignment, 7) Import for diplomatic and consular establishments, 8) Temporary import of goods for fairs and exhibitions, 9) Samples and advertising material, 10) Import of goods on the basis of a deferred payment agreement.

The Government periodically imposes quotas on some exports and imports. The aim has been to defend the national economy and to prevent mass export of natural resources. On the other hand there are subsidies to promote certain exports, particularly agricultural. Exporters should obtain certificates of origin from the Economic Chamber of FYROM and especially for exports to European Union countries.

Some goods can be exported and imported on the basis of special licenses issued by the Ministry of Foreign Affairs. The import of spare parts for maintenance of imported equipment, the equipment itself and all related consumption materials is free. Import from abroad of weapons, munitions, explosives and materials for manufacture of explosives is not allowed for individual citizens. Also, import and transport of dangerous refuse and waste material is forbidden without special approval.

Foreign trade is based on agreements made in accordance with FYROM regulations as well as pursuant to international agreements and conventions. Goods that require compulsory health, veterinary or plant pathology control or quality control, cannot be imported or temporarily imported if they do not satisfy the necessary requirements and conditions. Also, the same applies for goods whose sale has been forbidden in their country of origin, unless special approval is granted by the Ministry of Foreign Affairs.

Certain goods can be temporarily imported for refinement, testing and processing, if they do not harm people's lives and health or the natural environment. The Government reserves the right to forbid the import and transport of goods on the basis of preserving and promoting the surroundings and nature. Imports from and transit trade through the Federal Republic of Yugoslavia were prohibited in accordance with United Nations Security Council Resolutions until late November 1995. In addition, until October 1995 the Government of Greece placed an embargo on trade with FYROM, except for humanitarian goods, necessitating that merchandise transit through ports in Bulgaria and Albania. These impediments have now been lifted, but trade has yet to return fully to normal.

5.5.2. Foreign trade pattern

FYROM has been changing its trade pattern, redirecting it from the former Yugoslavian countries to the European Union members. Trade with Serbia has been down due to the worsening of its economic crisis

and trade with Slovenia was also reduced due to a trade dispute. On the contrary, Germany, Italy and Greece are three of the most important trade partners of FYROM and their importance in continually increasing.

According to the Economist Intelligent Unit, in 2000 the main partner in foreign trade was Germany, where 21.4% of all the imports came from and 13.6% of the export went to. The second big partner is Federal Republic of Yugoslavia (FRY), especially on the export side, where 10.1% of FYROM' s goods were exported and 21.3% of all the imports were driven from. Very and increasingly significant is the trade with Greece, with 9.1% of total exports and 7.2% of total imports Next on the list is USA, accounting for 4.0% in export and 11.4% in import and Italy accounting for 5.2% in total exports and 5.9% in total imports. Slovenia, Russia, Holland, Bulgaria, Croatia and Turkey etc. are also very important trade partners of FYROM. The table below present the destination of Merchandise Exports, for the years 1995-1998, in million of U.S.D, by countries.

Table 28. FYROM: Destination of Merchandise Exports, 1995-1998, (in mil USD)

	1995	1996	1997	1998
	In million of U.S.D			
Total Exports (FOB)	1.204,0	1.147,4	1.236,8	1.322,1
Industrial countries	523,3	616,5	681,1	822,1
EUROPEAN UNION	407,8	490,2	462,0	584,5
– France	23,5	6,0	5,7	17,7
– Italy	118,4	51,4	42,5	96,8
– Netherlands	29,7	47,9	41,3	43,7
– Germany	153,1	214,6	194,8	283,0
– United kingdom	21,1	30,6	30,2	23,4
– Greece	14,2	102,4	97,4	83,3
– Austria	30,3	20,4	18,5	9,9
– Other	17,5	16,9	31,6	26,7
E.F.T.A	37,1	33,2	80,6	45,3
– Switzerland	36,7	33,1	64,4	40,3
– Other	0,4	0,1	16,2	5,0
Other Industrial countries	78,4	93,1	138,5	192,3
– Japan	1,1	2,4	1,3	2,1
– United States	35,6	70,7	114,5	175,1
– Turkey	38,3	18,2	22,7	9,1
– Others	3,4	1,8	0,0	6,0
Former CMEA area	446,2	134,9	116,0	109,5
– Bulgaria	256,0	38,2	31,7	42,6
– Russia	87,2	38,6	25,5	26,1
– Albania	24,7	32,6	30,1	13,3
– Ukraine	29,2	4,9	1,9	3,7
– Other	49,1	20,6	26,8	23,8
Developing Countries	44,0	11,3	20,9	32,8
Republics of the Former SFRY	190,0	380,0	387,4	355,2
– Federal Republic of Yugoslavia	84,8	245,8	273,9	240,2
– Croatia	32,1	34,0	37,8	54,1
– Slovenia	72,4	82,1	55,5	41,3
– Bosnia and Herzegovina	0,7	18,1	20,2	19,6
Other countries	0,5	4,7	31,4	2,5

Source: International Monetary Fund (IMF), Country report No.00/72, June 2000, page 123.

In terms of group of counties, in 1998, 62.1% of all exports go to the industrial countries (E.U, E.F.T.A, JAPAN, USA and others), 2.4% is exported to developing countries, 26.8 % is exported to Republics of the former SFRY (FRY, Croatia, Slovenia, Bosnia and Herzegovina) and 8.2% exported to former CMEA area (Bulgaria, Russia, Albania, Ukraine and others).

In 1998, 48.4% of all imports came from the industrial countries (E.U, E.F.T.A, JAPAN, USA and other industrial countries), 20.9% is imported from former CMEA area (Bulgaria, Russia, Albania, Ukraine and others), 24.3 % is imported from Republics of the former SFRY (FRY, Croatia, Slovenia, Bosnia and Herzegovina) and 5.9% is imported from developing countries, The following table present the origin of Merchandise Imports, for the years 1995-1998, in million of U.S.D, by countries.

Table 29. FYROM: Origin of Merchandise Imports, 1995-1998, (in mil USD)

	1995	1996	1997	1998
	In million of U.S.D			
Total Imports (CIF)	1.716,1	1.626,3	1.778,5	1.913,5
Industrial countries	860,8	806,2	827,4	927,0
EUROPEAN UNION	689,6	629,8	658,5	693,9
– France	36,1	48,6	35,3	36,6
– Italy	179,3	109,8	94,7	109,1
– Netherlands	43,4	39,8	39,8	42,2
– Germany	283,0	239,9	233,4	255,0
– United kingdom	20,2	22,5	22,2	30,3
– Greece	28,9	77,4	127,1	113,3
– Austria	44,9	38,2	43,4	53,5
– Other	53,8	53,6	62,6	53,9
E.F.T.A	20,0	24,9	27,8	35,7
– Switzerland	19,1	23,2	22,5	27,7
– Other	0,9	1,7	5,3	8,0
Other Industrial countries	151,2	151,5	141,1	197,4
– Japan	14,6	15,5	11,7	16,6
– United States	57,8	67,8	80,1	101,6
– Turkey	55,2	44,3	49,3	51,4
– Others	23,6	23,9	0,0	27,8
Former CMEA area	434,7	334,0	357,4	400,1
– Bulgaria	255,9	107,5	98,2	86,2
– Russia	62,8	122,3	68,5	91,0
– Albania	8,2	5,1	3,9	2,0
– Ukraine	37,3	31,4	91,7	118,9
– Other	70,5	77,7	95,1	102,0
Developing Countries	85,9	97,5	110,4	114,0
Republics of the Former SFRY	334,7	342,1	413,2	465,4
– Federal Republic of Yugoslavia	161,1	165,6	202,3	244,6
– Croatia	56,3	48,9	68,5	64,4
– Slovenia	116,5	124,3	135,5	148,8
– Bosnia and Herzegovina	0,8	3,3	6,9	7,6
Other countries	0,0	36,5	70,1	7,0

Source: International Monetary Fund (IMF), Country report No.00/72, June 2000, page 124.

5.5.3. Foreign trade: Imports and Exports of FYROM

The following table presents the foreign trade in FYROM, for the last decade, from 1990 until 1999, in millions of USD.

TABLE 30. Foreign Trade in FYROM, in million of USD, (1990-1997)

	1990	1991	1992	1993	1994	1994	1995	1996	1997	1998
TOTAL TURNOVER	2.626	2.369	2.405	2.254	3.282	2.920	2.774	3.014	3.235	2.988
-EXPORTS	1.113	1.095	1.199	1.055	1.442	1.204	1.147	1.236	1.322	1.192
-IMPORTS	1.531	1.274	1.206	1.199	1.840	1.716	1.627	1.778	1.913	1.796
Deficit	-418	-179	-7	-144	-398	-512	-480	-542	-591	-604

Source: Statistical Yearbooks 1996, Skopje & IMF country report No.00/72, June 2000.

Exports

Exports continued to increase on account of the lagged impact of the July 1997 devaluation and a cooperation agreement with the European Union which was signed in November 1997 and simplified the customs clearance system between FYROM and the EU. The strong growth of exports of clothes and textiles as well as iron and steel, accounted for nearly half of FYROM's total exports in 1998 and the main countries of exports were Germany, FRY, Greece, Italy and U.S.A

According to the IMF country report of 2000, the major goods being exported in 1998 are the following: *Clothes and Textile 28%, Iron and Steel 20%, Beverages and tobacco 11%, Machinery 7%, Food 5%, Chemicals 5%, Others 24%.*

Imports

Imports also grew strongly owing to increased domestic demand and a surge in imports of intermediate inputs for processed goods of exports. FYROM has a trade structure that links exports and imports closely, most of exporters of textiles and clothes, and iron and steel took processing contracts with foreign firms. Because of this, imported inputs for processing rose in line with hikes of exports of these products. The main sources of imports were Germany, FRY, USA, Greece, Italy.

It is important to notice that it is forbidden to import waste, harmful and radioactive materials, to import biologically non-degradable materials for production of detergents and pesticides containing polyphosphates and to import technologies that were prohibited in the country of origin.

According to the IMF country report in 2000, the major goods being imported in 1998 are the following: *Consumption goods 22%, Textile processing 13%, Investment goods 13%, Mineral fuels 8%, Iron processing 5%, other processing 4%, Others 38%.*

Table 31. FYROM: Exports and Imports by final use, 1995-1998

	1995	1996	1997	1998
	In million of U.S.D			
Exports (FOB)	1.204,0	1.474,4	1.236,8	1.322,1
Industrial Supplies	651,5	567,6	650,0	645,9
Investment goods and spare parts	50,4	38,5	42,1	52,9
Consumption goods	446,6	540,3	543,3	621,7
Other	55,5	1,0	1,4	1,6
Imports (CIF)	1.716,0	1.626,0	1.778,0	1.913,0
Industrial supplies	989,9	904,9	1.087,7	1.242,5
Investment goods and spare parts	181,2	218,0	188,5	247,3
Consumption goods	527,9	492,4	491,6	412,1
Other	17,1	11,0	10,7	11,6
<i>In percentage (%) of total exports</i>				
Exports (FOB)	100%	100%	100%	100%
Industrial Supplies	54.1	49.5	52.6	48.9
Investment goods and spare parts	4.2	3.4	3.4	4.0
Consumption goods	37.1	47.1	43.9	47.0
Other	4.6	0.1	0.1	0.1
<i>In percentage (%) of total imports</i>				
Imports (CIF)	100%	100%	100%	100%
Industrial supplies	57.7	55.6	61.2	64.9
Investment goods and spare parts	10.6	13.4	10.6	12.9
Consumption goods	30.8	30.3	27.6	21.5
Other	1.0	0.7	0.6	0.6

Source: International Monetary Fund (IMF), Country report No.00/72, June 2000, page 125.

Current Trade Volume

For the year 2000, the Economist Intelligence Unit estimates that, the foreign trade turnover in FYROM amounts to USD 3.2 billions. Export and import volumes for the 2000 amount to USD 1.3 billion and USD 1.9 billions respectively. Data for the last years are shown in the table below as well as the projected year 2001.

Table 32. Export and Import volumes for the years 1999 –2001, in USD millions

USD million	1999	2000* (estimated)	2001* (projected)
Total Turnover	2.988	3.276	3.564
Total Exports (FOB)	1.192	1.344	1.536
Total Imports (CIF)	1.796	1.932	2.028
Deficit (Imports-Exports)	-604	-588	-492

Source: World Development Indicators, World Bank Group, (<http://www.worldbank.org>) and *Economist Intelligence Unit estimated and projected trade for the years 2000, 2001.

Table 33. Trade & Finance Indicators of FYROM, by years (1995-1999)

INDICATORS	1995	1997	1998	1999
Aid per capita (current \$ US)	40.1	49	46	135.1
FDI net inflows (in \$ US million)	14.0	11.0	118.0	30.1
Trade in goods (% of GDP, PPP)	34.6	34.0	35.9	33.1
Short term-Debt Outstanding (DOD, in \$ US million)	142.8 mil	N/A	157.2 mil	68.0 mil
Total Debt Service (TDS, in \$US million)	1.100	971,3	1.296,3	1.155,7

Source: World Development Indicators, World Bank Group, (<http://www.worldbank.org>)

According to the Commission of the European Communities (PHARE) on the improvement of Export capabilities, a number of sub-sectors were identified as having particular export potential such as: Finished Textile Goods, Finished Leather Goods, Shoes, Packaging, Lamb meat, Fruits and Vegetables, Processed foods, Wines, Automotive Accessories, Vehicle and Bus Assembly, Electronic Equipment, Telecommunications Equipment, Electric Motors, Metal Fabrications Equipment, Steel Pipe, Furniture, Construction, Tobacco, Cigarettes.

Investors and traders should investigate the situation in these industries and others, in order to evaluate their current potential.

5.5.4. Trade and Customs regulations

5.5.4.1. Registration and licensing requirements

There is no formal registration requirement either for exporting or for importing. This is simply regulated by the company's registered charter, since it is not allowed to undertake any business activity unless it is part of its charter. The company itself regulates the type and nature of goods that are allowed to be traded and therefore exported or imported. There is no special limit on the number of business activities for which a company may be registered. The only constraint is that for some business activities a special approval or license is needed from the appropriate ministry (such as TV and radio stations, airlines, publishing, etc.).

Licenses are required for export and import of certain goods that are tightly controlled, because of their nature or if part of a contingent quota. For trade with weapons, drugs, poisonous materials and waste materials, a special license is needed from the appropriate ministry. Also, agricultural products are subject to sanitary and health inspection and depending on the result, they are allowed or not allowed to be imported. Some agricultural products are usually contingent quota goods and therefore need special approval by the authorities.

5.5.4.2. Quotas

For the purpose of protection of domestic production and market, export and import of certain goods can be limited by quotas. However, they apply to less than 2% of import categories. The Government, upon the recommendation of the Ministry of Foreign Affairs issued by December 31st of each year, as well as based on the opinions received from business, agricultural and forestry entities, specifies the quantities and values for approved quotas. Quotas on imports are imposed on goods that are manufactured in FYROM as well, and also for some agricultural products. The contingent quotas are issued upon request and usually cover a one year period. One element in the decision by the Ministry is whether the importer has traditionally had trading links with regard to the goods.

Import quotas are distributed at auctions organized by the Government where companies have the right to bid for certain quantities. The actual share that they get depends on the number of companies that apply, the quantity applied for and the result of the auction. The final decision on distribution of quotas is published at the Ministry of Foreign Affairs. Meanwhile, for export, if exported goods are subject to quotas in the country of destination, then the exporter should secure the necessary share of contingent quota.

In the process of distribution of quotas, special care is taken that 10% reserve is left for additional distribution and for new production whose needs could not have been foreseen in the initial distribution.

With prior approval of the Ministry of Foreign Affairs so-called compensation goods or barter transactions may be arranged. For example, in the autumn and winter months tropical fruits may be imported if country's apples have first been exported to an equivalent value.

5.5.4.3. Duties

Customs Tariff Law of FYROM, regulating the tariffs has been published in Official Gazette 38/96. A comprehensive new Customs law has been drafted to conform with World Trade Organization (WTO) norms and European Union standards and it is to be enacted shortly. Customs duties are levied on imported goods. In most cases the rates vary from zero to 25%, except rates on luxury goods which are higher 50%. Services are not subject to duties, levies or fees.

The Customs Law (Official Gazette and amendments) sets up certain benefits for foreign investors, such as duty exemption on imports of equipment or other assets to be used for capital contributions, provided that the investor commits to a period of at least five years and holds 20% or more of the equity. The Foreign Trade Law stipulates that importation of equipment and goods meant for the foreign investor's own use and as original or increased capital contributions is free of duty.

5.5.4.4. Levies and fees

A number of products, except those that are free from customs duties, are subject to special import levies in addition to any applicable tariff duties. Import and export levies for all types of goods which are payable on top of any customs duties are regulated by the Law on Special Levies Imposed on Imported Goods (Official Gazette No. 70/94) and can be found in the Tariff Book.

5.5.4.5. Tariffs and customs procedures

The complete customs procedure is regulated by the Customs Law (Official Gazette and amendments). This law regulates the system of customs protection of the economy, and the rights and obligations of all the subjects in the customs procedure. It also specifies the customs area, customs line, customs borderline, customs super intendency and customs supervision.

For exports, the procedure is rather simple and there are no customs duties to be paid, while for imports it is a much more complex operation. The Customs Law explains the procedures, while the Tariff Book contains the information on customs tariffs and duties, additional levies that are to be paid, as well as the regime for export and import of all goods in trade. Import of certain goods may be exempt from these duties and levies by special decree or decision of the Government.

5.5.4.6. Duty Free Trade Zones

The Parliament adopted the law on free trade zones in July 1999 and construction of the zone started in 2000.

5.6. Foreign Direct Investment (FDI)

5.6.1. Advantages and Weaknesses of FDI in FYROM

One of the **main objective of FYROM development policy is to attract foreign capital in the country.** The legal environment was designed so that it provides a national treatment to foreign investors and even more, there are some tax and duties incentives for foreign investors.

However, the adverse external environment, the abrupt loss of markets and the low visibility of FYROM as a possible investment site produced a result that FYROM had very small inflow of foreign capital as compared to other Central and Eastern European countries. So the total inflow of foreign capital in the country, for the period 1990-1996, amounted to \$64 million US, out of which approximately \$30 million US came from the privatization process.

The following table shows that the net FDI inflows in 1998 was increased by 637.5% compared with the previous year (1997) and the reasons are that, the FDI took off on account of the sales of a brewery (\$33 million US) and a cement factory (\$31 million US) as well as investment in Macedonian Telecom (\$50 million US).

Table 34. Foreign Direct Investments (FDI) in millions of USD (net inflows)

FDI in millions USD	1995	1996	1997	1998	1999
	\$14.0	\$11.0	\$ 16.0	\$118.0	\$30.1

Source: World Development Indicators, World Bank Group, (<http://sima-ext.worldbank.org>)

Similarly to the trade patterns, the most significant foreign investors come from the EU and USA, so that most of the investments came from 32 countries, but the most significant capital inflow was from the following ones: Germany, Italy, Greece, United Kingdom, Turkey, USA, France, Austria Spain, Switzerland etc. These ten countries account for more than 93% of all foreign investments that came in FYROM.

The most significant investments happened in gypsum, technical gasses, tobacco leaf production, supermarkets, textiles and clothing, shoes, food processing etc. It is expected that there will be a significant foreign investment in the banking sector.

This unsatisfactory trend has put even harder push to the government to rank the attraction of foreign investment very high on its economic and development policy priorities. It is now preparing a national strategy for attracting FDI, which includes the establishment of the investment promotion agency, reconsidering of all the existing laws and their compliance with the policy to attract foreign capital in the country, enacting all the missing laws and trying to make the overall environment for investment as business friendly as possible.

When discussing the foreign investments, it is worth mentioning some of the **main advantages of FYROM** site for investment which are mainly the following:

- Although FYROM it is perceived, as a politically risky country, during most of the period after the independence, it managed to maintain political stability and it was the only country of former Yugoslavia which obtained its independence without a war conflict with its neighbours.
- The business friendly legal environment has been established to a great extent, and it is still subject to further adjustments, in order to better meet the requirements of potential investors.
- The FYROM possesses a relatively good infrastructure and it is also subject to continuous further improvement in order to better serve the businesses' needs,
- It has well educated and relatively non expensive human resources. The technical skills of the workers is especially at a high level. They have both a high starting educational basis and a good potential to acquire new knowledge and skills with very little investment.
- A great percentage of the population has proved to possess entrepreneurial spirit, which can well be used for developing (differently) various businesses.
- The existing industrial base is very diversified. It may be a good start for very different businesses.
- FYROM already possesses competitive advantages in some sectors and it has potentials to develop such advantages in some other sectors as well. This is mainly referred to the sectors which are natural resources and human resources based.
- These points can make FYROM a possible hub for some businesses in the Balkan or South-Eastern European area, where a lot of businesses can be located in order to service a broader region.

On the other hand **FYROM has weaknesses**. They are mainly the following:

- FYROM is a small market and this is one of its major weaknesses. Knowing this, the government has made an effort to conclude free-trade agreements with most of its neighbors.
- FYROM population has a relatively low purchasing power which emphasizes even more the first weakness of the small market.
- FYROM's is not very visible on the international market and very little is known about it. Although there are some natural reasons for this, it is also true that the country itself has not made much effort to promote its investment site. It was estimated that the investment promotion activities would not be effective so far, because of the problems that the country was facing. Now that the political climate has been improved, it has gained the momentum to show the world the potentials of its location for investment and business.
- The capital market is not developed. The banking system is still facing difficulties, although it has been subjected to massive rehabilitation programs. The biggest problems is the loss of credibility in banks by the local population, which make them keep their savings out of banks and out of the potential financial flows. This has produced a low level of national savings, at least a low level of bank savings. It is expected that the upcoming foreign investment in the banking sectors will tremendously restore the credibility and start improving the banking sector operations. On the other hand, although there is a Stock exchange, it is still very illiquid.
- The overall legal framework has still not been completed entirely. Some laws, institutions, or even procedures are still missing or not well established.
- The development process has still not been recovered in all areas, so that there are still some negative indicators and movements.

5.6.2.Foreign investment operations under the business legal environment

5.6.2.1.Investment promotion

The general cornerstones of the policy for enhancing the inflow of foreign direct investment (FDI) into the economy of FYROM are connected to three most important issues which generally direct the FDI internationally. The main aim is making this investment site more attractive.

1. The first unavoidable (given) issue which very strongly determines the attractiveness of the economy of FYROM as an investment location are the size and the position of the country, the size as economic issue and the position as a geographical one.

The economy of FYROM, in international terms, is a very small economy, which means that, in terms of attracting FDI this characteristic has to be turned-by measures of the economic policy-as an advantage rather than a disadvantage, as it is, on an ad hoc basis, considered as. It becomes very clear that foreign investors will not be strongly attracted (and inclined) to gain dominant position (share) on this market solely, simply for the demand it can create. It is not a question of their capability to do this, it is rather the low aggregate consumption this small market has (and will eventually have) that is an element of it's unattractiveness. This, in turn, means that foreign investors would likely penetrate in this market (economy) in the first place if possibilities for exploiting certain advantages of macro economic (in the production factors) character exist in this small economy, which will, again, enhance their own international competitiveness, and hence, allow them to easily penetrate other markets - first of all in this region.

In other words, it appears that, FYROM is likely to be more attractive for the multinational companies with a strategy of a truly global horizon, rather than for investors with a multi domestic strategy. In this context, if the

geographical position of the country is also considered, it's attractiveness points to the multinationals of non European countries that aim to European markets, on one side, and, the position of FYROM between the central European countries as emerging market economies, points to it's potential attractiveness for the multinationals of the western European countries.

Referring to the policy measures for the investment promotion in this domain, they are, in practice, two-fold. One set are the policy measures for maintaining sound and stable political relations with the countries in the region (neighbors and wider), thus creating the possibilities for co-operation. And the second set of measures are all various types of regional economic unification, being: creating custom unions, harmonization of duties, etc., all up to creating common markets - in relatively near future. FYROM can already say that the country has a population of two million and a market of twenty million, when one considers the Multinational and Bilateral agreements already established with FRY (1996), Slovenia (1996), Croatia(1997), Turkey and Bulgaria (1999) and is in the negotiation process of free trade agreement with Albania, Romania, Bosnia Herzegovina, Ukraine and EFTA.

2. The second very important issue for determining the attractiveness of the country for enhancing the inflow of FDI is the identification of the business sectors which as such can be the focal points for creating clusters of competitive businesses. Such sectors (allowing for changes in future) are considered:

- Raw material based sectors: agriculture (early vegetables, fruits), food processing industry, forestry, non-metals, ferrous-metals etc. - have immense opportunities for new value added.
- Mature traditional industries - can be competitive if restructured and market niches are discovered.
- High growth and human resources intensive industries (pharmaceuticals, telecommunication, computer software, services etc.) - strategic alliances are needed.
- Public sector (utilities) - energy generating plants, irrigations and melioration, road construction, through various **Built Operate Transfer (BOT)** and similar schemes.

Of course, this focusing of business sectors is not intended for any discrimination at all, since the overall policy approach for promoting FDI is project driven (any profitable project is appreciated), but it is rather a targeting indication.

The policy measures behind emphasizing this issue is undertaking different specific incentives measures for the potential large investments, as well as measures for creating the domestic investment environment more attractive in these domains. Such incentives are being prepared, summarized in a drafted law for pioneer foreign direct investments.

3. The third important issue for determining the attractiveness of the country for enhancing the inflow of FDI are all various measures aimed at setting up the domestic economy in a market friendly manner, as well as measures for making the investment site more visible and recognizable. Activities such as: building the legal framework, capacity building of the administrative institutions and courts, adopting stabilization type of monetary and fiscal policy, creating an (one stop-shop) investment promotion agency, marketing the country, and other similar policy measures are gathered.

5.6.2.2. Investment promotion institutions

The Government of FYROM, on it's session held on December 1st 1997, brought a decision for creating a Macedonian Investment Promotion Agency (MIPA) within the Macedonian Privatization Agency (MPA).

MIPA is tied up to the Macedonian Privatization Agency at the beginning for, at least, two obvious reasons. First of all, in performing it's privatization activities until now, the Privatization Agency has done a lot of work which practically belongs to an investment promotion agency, hence, it has, as an institution, already built much of the necessary infrastructure needed. This means various types of data bases, other significant

information, Internet Web site, prepared investment guides, etc. It also means that part of the staff has, in practice, gained certain training and knowledge about the specific duties for promoting a country. The second reason is the financing, or in other words, sources of funding the MIPA. In short, the Privatization Agency will play the role of an incubator for the MIPA.

The MIPA is likely supposed to become an independent non-profit business type institution, 100% government owned. This is so due to the need for efficiency in it's work, meaning avoiding bureaucratic procedures. It will certainly have linkages (clearly defined counterparts) with different ministries and other governmental institutions in order to allow it's duties to be fulfilled properly and easily.

The tasks or the activities of the MIPA can be separated into four different types:

1. Image-building activities.
2. Investment-generating activities.
3. Investment-servicing activities.
4. Advising/reporting to the Government.

For the fulfillment of the Image-building activities the following techniques can be applied:

- Advertising in general business media (Information on FYROM business environment - taxes, tariffs, foreign trade, financial and employment legislation, general legal regulation, etc.),
- Disseminating the appropriate information through INTERNET.
- Participating in investment exhibitions.
- Advertising in industry- or sector-specific media.
- Conducting general investment missions from source countries to host countries and vice versa (Road-shows).
- Conducting general information seminars on the investment opportunities in this country.

For the fulfillment of the Investment-generating activities the following techniques can be applied:

- Engaging in direct mail or telephone campaigns.
- Conducting industry- or sector-specific investment missions to source countries, and personal selling.
- Conducting industry- or sector-specific information seminars.
- Engaging in firm-specific research followed by "sales" presentations.
- Disseminating the appropriate information through INTERNET.

The Investment-servicing activities can be distinguished to two kinds of activities:

- Providing pre-investment services.
- Providing post-investment services.

The MIPA is perceived as an “**one-stop-shop**” for the foreign investors, and this is the main objective behind the approach for defining the tasks pertaining to the servicing activities. The pre-investment servicing activities can be summarized by:

- Providing investment counseling services,
- Expediting the processing of applications and permits and issuing a written confirmation about this,
- Arranging the hosting of prospective investors.

The post-investment servicing activities mainly can consist of:

- Advising on different pending legal issues and matters,
- Advising (or expediting and processing of) on supplementary and additional permits and licenses),
- Disseminating important and relevant information.

The tasks named advising/reporting to the Government can include the following:

- Advising to the Government (the Ministry of Development) about the revealed difficulties within the policy matters for the foreign investors, thus proposing changes in the policy framework or in different laws, regulations, etc.-feedback function.
- Advising to the Government (the Ministry of foreign affairs - due to its responsibility for the final approval for the foreign investment) about the solvency and the reliability of a potential foreign investor.
- Reporting to the Government (annually or semi-annually) about the achieved results and/or difficulties.

The MIPA is not a “competitor” to any existing governmental institution, meaning that it will not undertake some of their competencies and responsibilities. Rather, the MIPA is intended to represent a complementary reinforcing counterpart engaged in the activities for **attracting foreign direct investment** in the country, and as such to be an institution that will be competent and responsible for the activities which can not be done by the existing governmental bodies. This means that the MIPA for the investment promotion will have competencies to:

- acquire information from different administrative institutions, such as: the ministries, the Statistical Office, the Payment Operations Service, the Central Bank, the Chamber of Commerce, etc.,
- acquire all the documents (applications and permits), on behalf of the foreign investors, from the different administrative institutions, necessary for the realization of the investments,
- collect various data necessary for the investment promotion purposes,
- keep records and data-base for all the foreign investment realized in the country and disseminate these data to the Government or the Central Bank on request,
- co-operate and undertake mutual efforts with representatives in the embassies of FYROM throughout the world for the realization of the tasks of investment promotion,
- conclude contracts for co-operation with different investment promotion agencies (institutions) from other countries,

- engage in negotiations with potential foreign investors/partners on behalf of certain enterprises, providing a written approval by the Board of directors of those enterprises has been issued to the IPA,
- advise to the Government (the Ministry of Development) about the revealed difficulties within the policy matters for the foreign investors, thus proposing changes in the policy framework or in different laws, regulations, etc.

Apart from the Macedonian Investment Promotion Agency (MIPA), within the Ministry of Development, an Investment Promotion Department has been constituted, and this unit is intended to be a counterpart to MIPA with a clearly separated responsibilities. In fact,

-MINISTRY OF DEVELOPMENT: creates the policy.

-MIPA: implements this defined policy.

The MIPA also have close linkages and co-operation with the National Enterprise Promotion Agency (**NEPA**), **responsible for implementing the SME development policy in the country**. In fact, this both institutions deal with investment generating activities - one being more inward oriented, the other outward. Finally, the MIPA conduct sound relations with the Chamber of Commerce, as it is an institution having competencies which can have positive impact on generating FDI.

5.6.3.Regulatory environment for FDI

FYROM has enacted legislation to establish environment for foreign investment, which together with other laws, should create a legal basis to attract foreign investors and provide protection of legitimate interests as well as for foreign capital.

FDI was first allowed in 1967. The gradual liberalization of FDI legislation between 1967 and 1988 stayed within the framework of specific, sui generis, contractual joint ventures, the only permissible type of FDI at the time. The major change of attitude towards FDI happened only in the framework of the overall market-oriented reform launched in 1989. Thus in December 1988, the new Foreign Investment Law was passed. The Law introduced fundamental liberalization of FDI legal framework and its harmonization with international standards in the field. **In 1993 the Foreign Investment Law in FYROM was adopted .**

Since 1996, the operations of all enterprises including foreign investment enterprises, fall under Commercial Code, which entered into force on June 1996.

The regulatory framework for foreign investment in FYROM is provided by the following laws and regulations:

- Commercial Code (28/96)
- Concession Law (42/93)
- Transformation of Enterprises with Social Capital Law (38/93)
- Securities Law (7/97)
- Profit Tax Law (80/93, 33/95, 43/95, 71/96, 5/97)
- Customs Law (4/93 and 20/93)
- Foreign Trade Law (31/93 and later)
- Foreign Currency Operations Law (30/93 and prior)

- Credit Relations with Foreign Countries Law (4/93 and 31/93)
- Banks and Savings Institutional Law (29/96)
- Obligations Law (57/89 and prior)
- Industrial Property Law (42/93)
- Copyright Law
- Basic Ownership Legal Relations Law (6/80 and 36/90)
- Employment Relations Law (80/93)
- Insurance Law (49/97)
- Urban Planning Law (28/97)
- Construction Law (15/90 and 11/94).
- Expropriation Law (33/95)
- Game on Chances Law (10/97)

Bills are being drafted in a number of areas. Interested parties should check with legal counsel on the latest laws that have been enacted.

5.6.4. Guarantees for Foreign Investments

5.6.4.1. Bilateral treaties and multilateral conventions

FYROM has also concluded a number of investment protection under relevant international treaties and multilateral conventions, which form a network that is rapidly expanding. Most issues addressed in these documents are also covered in domestic laws dealing with foreign investment but such instruments provide a stronger protection standards to foreign investors.

Bilateral investment protection treaties: ratified agreements with the following:

- Republic of Croatia (17/95)
- Republic of Slovenia (55/96)
- Federal Republic of Yugoslavia (69/96)
- Republic of Turkey (5/97)
- Switzerland (8/97)
- Federal Republic of Germany (8/97)
- Republic of Poland (17/97)
- Republic of Italy (34/97)
- People's Republic of China (49/97)

Agreements signed with: *Russian Federation & Republic of Bulgaria*

Bilateral avoiding double taxation treaties: ratified agreements with the following:

- Republic of Croatia (17/95)
- Republic of Turkey (45/95)
- Federal Republic of Yugoslavia (8/97)
- Republic of Poland (17/97)
- Republic of Italy. (34/97)
- People's Republic of China (49/97)

5.6.4.2. Multilateral conventions and other guarantees

Multilateral conventions of FYROM where is a party to:

- Multilateral Investment Guarantee Agency (MIGA) Convention –MIGA is a member of World Bank Group for the protection of foreign investments abroad.
- the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention),
- the Washington Convention on the Settlement on Dispute,
- Cooperation Agreement with the European Union.

Under procedure - the Energy Charter Treaty and World Trade Organization (WTO)

FYROM is not a party to: Convention on the International Center for Settlement of Investment Disputes.

5.6.5. Dispute Resolution

5.6.5.1. General review

Domestic, general and internal sources of arbitrary law, which is implemented in investment dispute settlement, are:

- The Constitution of FYROM,
- Litigation Procedure Law (Official paper of SFRY, no 4/77),
- Law for settlement of disputes concerning the laws and regulations of other countries in certain relations (Official paper of SFRY, no 43/82),
- Commercial Code of FYROM.

International sources of the country arbitrary law are bilateral and multilateral conventions, which the RM has signed, or ratified, or inherited from the former Yugoslavia on the basis of succession, and which comprise certain questions for arbitrary solution of the disputes. Out of the most important, we shall emphasize the following multilateral documents:

- Geneva Convention of 1972, which deals with execution of certain arbitrary decisions,
- New York Convention for recognition and execution of foreign arbitrary decisions, of 1958.

It was ratified by the former Yugoslavia, with three reserves:

a) it is implemented for Yugoslavia only after its going into effect,

b) it is implemented only under the principle of reciprocity, and

c) SFRY implements it only for disputes, which originate from legal relations, which according to its law are considered to be economical.

- Europe Convention of 1961, and
- Washington Convention for solution of investment disputes among countries and citizens from other countries, of 1965.

Regarding the relations between the stated internal and international sources, three rules can be separated: 1st) all these sources must be in accordance with the Constitution of the country,

2nd) the ratified international agreements are given priority to domestic legislation, and

3rd) the New York Convention among the countries which have signed the agreement, derogates the implementation of the Geneva Protocol and Geneva Convention.

Concerning the question, on which arbitrary decisions can be subject of refuting, the view has been distinguished, according to which decisions of the domestic arbitration, are competent according to the domestic process law. It is pointed out that responsible court for canceling of an arbitrary decision is only the court of the country, on which territory the decision has been made, or the state court where the law is implemented.

5.6.5.2. Dispute settlement according to the commercial code

a) Settling of disputes by mutual consent or in court

Disputes between the founders of the enterprise concerning the agreement of the enterprise, should be settled by the founders by mutual consent.

The founders of a public company and the complementary partners in a limited partnership company may settle disputes concerning the company agreement in court at the Economic Chamber of FYROM, if so agreed upon by the parties in the company agreement.

b) Protection of the rights arising from the founders relations by the registration court

Should the rights arising from the founders relations be violated by the bodies of the enterprise, every founder may require protection of those rights from the court keeping the trade register according to the seat of the enterprise.

c) International settlement of disputes according to the bilateral documents

Disputes between Contracting Parties regarding the interpretation and application of the provisions of the Agreement shall be settled by consultation and negotiation through diplomatic channels.

If both Contracting Parties cannot reach an agreement within six months after the beginning of the dispute between themselves, it shall, upon request of either Contracting Party, be submitted to an arbitration tribunal which shall be constituted as follows:

- Each Contracting Party shall appoint an arbitrator and these two arbitrators shall nominate a chairman who shall be a national of a third State, which maintains diplomatic relations with both Contracting Parties.
- If one of the Contracting Parties has not appointed its arbitrator and has not followed the invitation of the other Contracting Party to make that appointment within two months, the arbitrator shall be appointed upon the request of that Contracting Party by the President of the International Court of Justice.
- If both arbitrators cannot reach an agreement about the choice of the chairman within two months after their appointment, the latter shall be appointed upon the request of either Contracting Party by the President of the International Court of Justice.
- If, in the above mentioned cases, the President of the International Court of Justice is prevented from carrying out the said function, or if he is a national of either Contracting Party, the appointment shall be made by the Vice-President, and if the latter is prevented or if he is national of either Contracting Party, the appointment shall be made by the most senior Judge of the Court who is not a national of either Contracting Party.

Subject to other provisions made by the Contracting Parties, the tribunal shall determine its procedure. The tribunal shall reach its decisions by a majority of votes.

The decisions of the tribunal are final and binding for each Contracting Party.

Each Contracting Party shall bear the costs of its own member of the tribunal and of its representation in the arbitral proceedings, the costs of the chairman and remaining costs shall be borne in equal parts by the Contracting Parties. The tribunal may, however, decide that a higher proportion of costs shall be borne by one of the Contracting Parties and this award shall be binding on both Contracting Parties.

5.6.6. Incentives**5.6.6.1. General review**

FDI incentives are provided both on individual basis (case by case negotiations) and to all foreign investors, in addition to incentives provided without discrimination between foreign and domestic investors.

FDI incentives are provided on case by case negotiations only for some important FDI for FYROM which can bring benefits for the country but in the framework of international and domestic legal standards. There is no special definition or criteria concerning this form of incentives.

Some incentives are granted to all foreign investors (tax holidays, reinvested profit and customs incentives) and some incentives are granted to both domestic and foreign investors (undeveloped regions, accelerated depreciation environment and rehabilitation firms). A new incentive program prepared by the Government is under way.

5.6.6.2. Tax and other fiscal incentives

Accelerated depreciation

In case of technological modernization and structural adjustment, the taxpayer is entitled to accelerated depreciation of the fixed assets, but up to amount which is 25 % higher than the depreciation calculated in a manner defined in the Law on tax income.

The taxpayer is entitled to accelerate depreciation of means used for protection of the environment and the nature.

Reinvested profit

The taxpayer has the tax base deducted for the amount from the profit invested into new investments (reinvested profit) in FYROM.

Undeveloped districts

The taxpayer who has invested an amount from the profit in economically undeveloped districts, in border regions and compact undeveloped regions, as well as in certain mountain districts and villages, has the tax base deducted.

Tax holidays

The profit tax payment obligation of the domestic legal or physical persons performing a registered activity, is reduced for the corresponding amount of the profit which belongs to a foreign person, on the basis of investments for the first three years, under a condition that the participation of the foreign capital should be at least 20% from the total invested permanent capital of the taxpayer.

The profit tax payments obligation of a foreign taxpayer performing a registered activity and is not a resident of FYROM, is reduced for the corresponding amount of the profit, which belongs to him on the basis of the investments from the first three years.

Tax exemption occurs once and can amount at most to the amount of the basic input of the foreign person (or input funds). This exemption, concerning Article 33, paragraph 3 of the Profit Tax Law concerns the total inputs done in this period of three years, namely the tax exemption can be used only for the first three-year period from the foundation - if a newly established legal person is in question, in the first three years of inputting - and an input of a foreign person as a subject, that has already been established and performed activities before the foreign person input.

Tax exemption on the basis of a foreign person input funds is realized by an approval of the public income body.

With the Profit Tax Law it is anticipated that if the basic input is done in the first half of the year, that same year should be considered as the first year of the activities. On the other hand, if the basic input is done in the second half of the year, the following year should be considered as the first year of the activities.

Besides this, with the Law, it is regulated who are the persons having an obligation, who are not considered as newly founded, defining that, for the persons having an obligation, and who became by joining, or separation and by their own transformation, the exemption anticipated on this basis is not related.

In order for the persons having an obligation to be able to use the tax exemption on the basis of foreign persons input funds, they are obliged to work (to perform an activity) at least three more years after the completion of the third year, determined in the sense of the solution in Article 33 of the Profit Tax Law

Revenues

The revenues, realized on the basis of funds which are strictly for the purpose of performing the activities of the legal person - taxpayer (budgeted, funds), are not included in the tax base for the calculation of the profit tax.

Environment

The tax payment obligation of the taxpayer is reduced for the amount of the funds of the profit invested in preserving the environment and nature.

Rehabilitation firms

Rehabilitation firms, employing disable persons, where the products and the services are completely produced or being carried out in the protective workshops, are exempted from paying the profit tax. This right is exercised by a written request submitted to the Public Revenue Office, on the basis of an appropriate documentation.

Transfer tax

10% repatriation tax is applied to the money repatriated by a foreign investor. This applies whether the repatriation occurs in the form of cash, dividends, equipment or products.

Under the term transferred part of the profit one can understand the transfer of funds on behalf of non-residential account in the country. The profit tax is counted and paid by the person having an obligation, who is established, or who is input funds from a foreign legal person.

During the conveyance of this regulation one should have in mind the solution according to which the transfer of funds on the basis of profit is done after presenting corresponding evidences, to the public income body, for paying the obligations on the basis of the earned profit on the territory of FYROM .

Personal profit tax

In case the investor is a natural person, dividends and other incomes, realized by participation into the profit of the legal and natural persons, are taxed according to the Law for Personal Profit Tax.

The income based on profit - dividend from the foreign investor invested funds - a natural person in an enterprise or store, who performs work on the territory of FYROM, is taxed at the moment of giving these funds to the disposal of the foreign founder. The personal tax of the profit is counted and paid after deduction, which means that it is an obligation of the person who pays while transferring the profit abroad.

5.7. Other Rules Relevant to Foreign Direct Investment**5.7.1. Business Organizations****5.7.1.1. Trading companies and a trader-individual (and a single-trader)**

Pursuant to the Law on Trading companies (Official Gazette of FYROM No. 28/96), an alien may be:

- a founder of a trading company which is registered in FYROM,
- a partner of a company which is registered in FYROM,

- a shareholder in a joint-stock company which is registered in FYROM, and
- a purchaser of shares and entitled to a share in profits from companies which are registered in FYROM.

The concept of “**a foreign person**” encompasses the following categories:

- a foreign juristic person registered in a foreign country,
- a foreign physical person and all individuals that have foreign citizenship, respectively,
- citizens of the country that have permanent residence in foreign countries,
- an alien who has its own enterprise on the territory of FYROM.

For the purpose of:

- establishing of a company, which is completely owned by one or more aliens, and in which they secure a majority,
- transforming the company into which they will have majority in the share,
- or transforming the company into which they will acquire such major participation in it,
- a permission by the Ministry of Foreign Affairs is also necessary.

On the basis of such a permission, the procedure for entering the company into the Trade Register, kept at the basic courts, follows and after the certification that the company was entered into the Register is issued, this company should be filed into the Statistical Office and in the Office of Money Operation of FYROM.

According to their forms, the companies, without distinction as to their lines of business, may be divided into:

1. Partnership

2. Limited partnership

3. Limited liability company (Incorporated company)

4. Joint-stock company

5. Limited stock company

1. Partnership

The partnership is an association of two or more legal juristic or physical persons who bear personal responsibility and have unlimited joint liabilities by their entire private property towards the creditors of the partnership's commitments.

The partnership is established by a memorandum of association, signed by the co-founders, which includes:

- Name and second name, citizenship, place of residence and address of the co-founders, or name and place of the company of the co-founders if they are legal juristic persons,

- Registered name and address of the partnership,
- Line of business of the partnership,
- Estimated value, type and size of the investments for each founder,
- Type of personal participation in the operation of the partnership,
- Method of distribution of profit,
- Method of covering the loss,
- Methods of the partnership management and representation, and
- Way of making decisions.

The partnership is entered into the Trade Register after appropriate application is submitted. The application for such entry should include:

- Registered name and address of the partnership,
- Line of business of the partnership,
- Personal name, profession, citizenship and place of residence of each co-founder.

If the founder is a legal juristic persons, the application should include:

- Registered name and address of the company,
- Methods of management and representation of the partnership, and
- Way of making decisions.

Along with this application, the memorandum of association should be also submitted.

The co-founders and persons, respectively, who, pursuant to the memorandum of association are authorized to represent the partnership, legalize their own signatures at the Court.

2.Limited Partnership

The limited partnership is a partnership in which two or more persons are associated, at least one of whom is jointly and severally liable for the limited partnership obligations by his/her entire property (an active partner) and at last one of them is liable for the limited partnership obligations to the amount of the entered/registered investments in the limited partnership (a silent partner).

This limited partnership is established by a memorandum of association, signed by the co-founders, which on the basis of the application is entered into the Trade Register.

The memorandum of association should contain:

- name and second name, citizenship, place of residence and address of the co-founders, or name and place of the company of the co-founders if they are legal juristic persons,
- registered name and address of the limited partnership,

- line of business of the limited partnership,
- total amount of the investments (deposit) by each founder,
- type and proportion of the investments by each founder,
- way and time of payment of the investments,
- methods of distribution of profit and covering the losses,
- methods of the partnership management and representation, and
- way of making decisions.

The application contains the all elements that are put down in the application for registering the limited partnership in the Trade Register.

3. Limited Liability Company

The limited liability company is a company in which each co-founder participates, in the previously defined amount of company capital (major part), with his/her basic investment (deposit). The basic investments may vary in the amount. The co-founders are not liable for the company obligations. The company is established by a written charter of the company signed by each founder. If such company is established only by one founder, this charter is then substituted by a statement of the founder, which is submitted to the notary.

The charter of the company and the statement of the founder, respectively, should include:

- name and second name, citizenship, place of residence and address of the co-founders, or registered name and address of the company if the founder is a legal juristic person,
- registered name and address of the company,
- line of business of the company.

Total amount of the major part and the amount of the basic investments by each founder separately. If the basic investment consists of items and copyrights, they should be elaborately described and their value indicated:

- way and time of payment of the investments in full,
- methods and criteria of distribution of profit and the method of covering the losses,
- company management,
- rights and liabilities of the founders beside their payment of the basic investment,
- company representation.

The major part of the company is the sum total of the basic investment by each co-founder and can not be less than DM 10,000 in denar counter value at the official average current rate of exchange, which is defined and published by the National Bank of the country on the day of payment. The amount of the basic investment of each founder can not be less than DM 200 in denar counter value. The amount of both the major part and the basic investment have to be expressed in a whole number (an integer) which can be divided by 100.

The limited liability company is entered into the Trade Register on the basis of the application, signed by the manager, along with which the charter of the company, the act for the manager appointment, the proof that each founder has paid at last 1/3 of the major part in money and that at last 1/2 of the major part was paid are enclosed.

4. Joint Stock Company

The joint stock company is a company which, by its Statute, has a major part determined and separated into equal shares (stocks). Each shareholder participates with one or several shares and his/her liabilities are secured by the entire property of the company.

If the joint stock company is established through a public invitation, the lowest nominal amount of the major part equals to DEM 50.000 in denar counter value whereas if the company is established without public invitation, the lowest nominal amount of the major part is DM 20.000.

The lowest nominal amount of the aforementioned major part does not refer to the joint stock company for carrying out bank and insurance operations, as well as trading operations with securities. The lowest nominal amount of one share may not be less than DEM 10.

The joint stock company will be entered into the Trade Register after the appointed managing body submits the application.

The application for registration should contain a statement that the requirements for establishing the company has been satisfied, including the number of shares and the amount already paid in.

Along with the application, the evidence (a proof) that the company may freely handle the amount already paid in is also presented as well as the following acts:

- Founding act,
- Act of taking over the shares and one copy of the booklet on the basis of which the whole or part of the amount of the major part was subscribed,
- Minutes of the constituent conference, along with the invitation and the list of participants,
- Statement of the appointed managing body that the payment for the shares has been made and that from the moment of the company registration the sum paid in, together with the non-money investments and procurements, are placed at its own disposal,
- Certificate/receipt from an authorized financial institution that the payments were made in cash,
- List of the members of the board of directories, managing board and supervisory board, with their names and second names, profession, place of living and citizenship; if they are foreign nationals - the statements of the members of the company that they accept their membership, the permission, if it is necessary pursuant to the law, a report from the founders and appraiser, if such report had to be made pursuant to the law.

The all members of the managing board sign the application at the Court.

5. Limited stock company

The limited stock company, the major part of which is divided into shares, is established by one or several active partners, who are jointly and severally liable by their entire property for the company's liabilities, and by silent partners-shareholders who are not liable for the company's liabilities (commitments).

The limited stock company is established by a charter of the company which includes data such as name, second name, citizenship, profession and place of living and registered name of the company, respectively and address of each active partner. The investments by active partners are defined according to type and size and can not be lower than 1/10 from the major part. The limited stock company is entered into the Trade Register.

5.7.1.2. Representative offices of foreigners in FYROM

Pursuant to the Ordinance (by-law) on More Detailed (thorough) Conditions for Starting and Operating the Representative Office of Foreigners in FYROM (Official Gazette No. 25/95), foreigners are allowed to open such representative office.

The representative office may start its operation after it is entered into the Register of Representative Offices of Aliens in FYROM, which is being kept at the Ministry of Foreign Affairs.

The request for entering into the Register should include:

- the registered name of the company of the founder,
- the registered name of the representative office and its place of registration,
- its line of business (field of activities),
- total number of the employed at the representative office.

In addition, the alien is to submit both an original and a certified copy of:

- the document of registration of the alien in the Register that is being kept in his/her country or other appropriate document in accordance with the regulations of his/her country,
- the work program of the representative office,
- the certified statement of the alien that he/she is undertaking the obligations that will appear in FYROM in relation to the representative office,
- the decision on appointment of manager (director) of the office by which he is authorized to work at the office,
- data on the citizens of FYROM who are employed at the office,
- the approval of the National Bank if the office opens a foreign bank or other financial institution,
- and the approval of the Ministry of Finance if foreign insurance company opens a representative office in the field of insurance.

The representative office may open a branch office in conformity with the provisions for opening a foreign office.

Additional information

Pursuant to the laws of FYROM foreign trading companies and foreign traders on the territory of FYROM are equalized with the domestic juristic and physical persons, except, according to the Law on Particular Companies, it is not differently prescribed (defined).

By accepting the international agreement for more favorable trading conditions for foreign persons, FYROM provides good conditions for trading activities of foreigners.

The foreign companies and foreign traders, respectively, may acquire ownership of buildings and limited real rights over immovable assets (property) for that line of business. They cannot acquire ownership over land, and yet may become owners of apartment or apartment building.

In FYROM, the foreign companies and foreign traders, respectively, cannot get into business as long as they do not establish subsidiary company (branch office). They have the right to establish subsidiary only if they are entered in the Register of the State in which they have a registered address for at least two years.

If a foreign company establishes several subsidiaries in FYROM, the main one should be pointed out in the application for the purpose of its registering in the Trade Register.

The foreign company, through its subsidiary, has the right to carry out, according to the form and subject of business, all the operations, undertake and acquire obligations, approach the courts and other authorities under the same conditions as domestic companies of the same or related form or subject of business operate.

The foreign company has the right to establish its subsidiary on the territory of the country if it is entered in the Register of the country in which it has a registered address for at least 2 years. If the foreign company establishes more than one subsidiary, the main one should be pointed out in the application for registering.

The Ministry of Foreign Affairs grants a permission for opening a subsidiary, representative office or other organizational unit of the foreign trader after which the procedure continues at the registering courts.

The following documents are to be presented at the Basic Court, where the Trade Register is being kept:

- Certificate from the Register in which the founder is registered and in which the content and the data of registering can be seen,
- Copy of the Charter of founding of the company or the Statute, certified by an authorized and official state body pursuant to the state regulation to which the company belongs, as well as the Certification by the foreign authorities that the presented Charter and/or Statute are still effective and valid.

If, pursuant to the laws of the state to which the company belongs the written Charter and/or the Statute are not required, a certification from the competent diplomatic-consular office of FYROM where the company exists is then presented as well as the name of the co-founders and the forms of their liabilities, the list of the persons authorized to represent the company in FYROM, their names and second names, profession, address and citizenship. Along with this list, the following documents are also submitted:

- evidence that the representatives are properly appointed in conformity with the acts and charter of the company, respectively, Statute and other state regulations to which the company belongs,
- decision of the competent body of the company on subsidiary establishing,
- attested copy of the annual balance-sheet,
- report of the managing body for the last two years, if it is possible according to the form of the company and the law regulations of the state to which the company belongs,
- description of the subsidiary's line of activities, and
- permission from the ministry which is competent in the economic foreign relations.

After the company or organizational unit is registered in the Trade Register, it should be included in the Statistical Office and the Payment Operations Service of FYROM.

The following papers are submitted at the **Statistical Office** of FYROM:

- a copy of the decision for registration in the Trade Register,
- a copy of the decision along with the permission of the Ministry of Foreign Affairs of FYROM,
- a copy of the Act of Founding,
- a form of the Payment Operations Service,
- an original application for registration in the Trade Register.

For the registration in the Payment Operations Service, the following documents should be submitted:

- a form-application, given by the Payment Operations Service,
- three signature-cards of the current account signers,
- the agreement with a bank of FYROM which the foreign,
- person is going to cooperate with,
- a copy of the Court Decision for registration in the Trade Register,
- a copy of the decision along with the permission of the Ministry of Foreign Affairs of FYROM a copy of the Act of Founding,
- a form of the Payment Operations Service.

Last, but probably most interesting for the foreign investors is the fact that the rights, acquired on the basis of the capital invested in the company (partnership) cannot be decreased by any law or other regulation. The share of the company profit, which belongs to the foreign person and the sum which belongs to the foreign person in case the company terminates its activities, respectively, or in case of partial or entire writing-off of the foreign person's contribution, may, upon the order of the foreign person, freely and without permission be remitted abroad in the same currency as the currency of investment if the company has disposal of money cover.

5.8. Privatization

5.8.1. Privatization Program

Initiation

The main business unit in FYROM economy, and similarly in the whole former Socialist Federal Republic of Yugoslavia was the socially-owned enterprise. Essentially, the people employed by the enterprise were the nominal owners as representatives of the public at large, but in fact they did not hold title to shares nor might they could transfer their ownership. "Everybody but nobody" was the owner. At the same time management of socially-owned enterprises was effected through workers' councils.

Country Enterprises started with the privatization process early, after the passage of the Law on Social Capital (Official Gazette 84/89) by the federal parliament of former Yugoslavia in November 1989, under the direction of the then Prime Minister, Ante Markovic. Immediately after the referendum for independence in 1991, the Government of FYROM announced that the federal law was no longer in force and that a new law would soon be promulgated. The new Law on Transformation of Enterprises with Social Capital (Official Gazette No. 38/93) was enacted after extensive debate two years later. The practical realization of the law occurred with the establishment of the Privatization Agency of FYROM for Transformation of Enterprises with Social Capital in October 1993 (Official Gazette 38/93).

Later on in the process, there was another Law on Transformation of Enterprises and Cooperatives with Social Capital Working with Agricultural Land. This law was enacted in March 1996 (Official Gazette No. 19/96).

Consequently, until December 10, 1994, the privatization process was largely autonomous and decentralized. Starting from that day, small and medium-sized enterprises with completely social capital had to be privatized according to methods or models determined by the Agency. The second deadline for another group of companies was June 28, 1995 (two years after the Privatization Law was enacted). Starting from that date, the privatization of all enterprises with mixed capital which had not been initiated had to be decided upon by the Agency. The deadline for large enterprises with social capital to initiate their privatization was December 10, 1995 (2 years after the methodology for valuation was decided).

The philosophy of self management was reflected in the country's approach to privatization. Rather than a top-down approach, enterprises themselves are responsible to propose the privatization model they wish to follow, to prepare all the documentation and to carry it out according to the law and under the supervision of the Privatization Agency.

The underlying philosophy of the privatization program is that privatization is considered to be a means and not a definite end. It is perceived as a vehicle for increasing the efficiency of the economy, since it is believed that higher efficiency in an enterprise can be achieved with dominant owners, who care and who are committed to preserve and increase the value of their shares in the company. The common understanding is that commitment comes when somebody pays for the shares he receives. That is why the main method for privatization in FYROM has a commercial case-by-case approach, rather than vouchers or some other non-cash system.

There are numerous reasons for selecting this approach, instead of the alternative, mass privatization approach. The most important reason for adopting the case-by-case method of privatization was the fact that the improvement of the efficiency of the economy, through the increase of the enterprise management efficiency, was the primary objective that was supposed to be achieved with privatization. Other objectives of privatization were the following: to increase the credibility and the support of the reforms, to attract foreign capital, to start the economy moving at a more stable pace, to develop the capital market, to de-freeze the so called frozen saving deposits, to productively engage the free money saved out of the banking system etc.

Objectives of the privatization process

As mentioned above, the **primary objective** of the privatization process is to increase the efficiency of the economy through the conversion of enterprises with social capital into enterprises with private ownership. Apart from this, other objectives are the following:

- start the economy growing at a more stable and sustainable rate of growth,
- mobilize and liquefy the so-called frozen savings deposits,
- increase credibility of other reform programs and support for them,

- assist in attracting foreign capital,
- support the efforts required to establish a capital market.

The major approach to privatization is commercial. It was a strategic decision of the Government not to embark on a mass privatization program (e.g. through distribution of vouchers) since it was believed that this would only delay the main objective of the transformation process, namely restructuring and improvement of efficiency.

However, as a matter of fairness in the process, the law provides for special terms to employees, concerning the following: (a) Employees (current or retired) with at least two years service are offered a generous discount scheme. They have an initial discount of 30% plus 1% for each year they have been employed by the enterprise. (b) For certain business units which were built with so-called common consumption funds, most of them being holiday resorts or restaurants, the initial discount is 50% plus 1% for each year worked in the firm, so that the maximum discount can be as high as 90%. Each employee may buy shares at a discount up to an amount not higher than DEM 25.000 and employees as a group may not exceed 30% of the appraised value of the company. According to an agreement with the unions, payment terms for employees involved in any model mentioned above have been extended to 7 years, the first 2 years of which are a grace period.

At the beginning when the enterprise starts the privatization process it must automatically transfer 15% of the social capital (in the form of shares or a stake) to the State Pension and Disability Fund free of charge. Thus, it is expected that the Pension Fund will receive a large number of shares. These are non-voting, preferred and participating shares and they are expected to earn 2% fixed dividend. This should significantly improve the financial situation of the Fund, especially in two to three years time. It is also expected that this would be one of the methods for restructuring the Pension Fund and for its transformation into an important financial intermediary on the market.

A restitution or denationalization law wasn't enacted until 1997. In the meantime the Privatization Law deals with the problem in the following way. When deciding to transform the enterprise it makes an announcement informing the general public that it is to be privatized and calling on former owners to declare their claims. The former owners or their legal successors must submit such claims within 60 days of the public announcement. The enterprise transfers shares corresponding to the amount claimed to the Privatization Agency and the Agency holds the shares on behalf of the alleged owner, until a new law has been enacted and until the former owners have received legal permission that they may exercise their ownership rights.

Under the law foreign investors have exactly the same status as domestic investors. Having in mind that there are some incentives in the tax and trade regimes for foreign investment, the foreigners actually have a more favorable status in the privatization as compared to the domestic investors.

Transformation of Socially Owned and State Enterprises

As a part of its transition toward a market economy the FYROM undertook in mid 1993 to dismantle the social ownership system of enterprises inherited from the former SFRY. Privatization, however, did not gain momentum until late 1994. In early 1995 a special law on the **Special Restructuring Program (SRP)** mandated the restructuring and privatization of an additional 25 large loss-making enterprises, including the state-owned electric utility and the railways. In April 1996 privatization was expanded to agricultural enterprises and cooperatives. With the privatization process nearing its end, the outcome has been below expectations. Internal ownership by workers and managers has widened, owing to the predominant reliance on insider privatization, the government has been increasingly burdened with the liabilities of large insolvent loss-makers, privatization of the state-owned utilities has not yet been initiated and notwithstanding the impact of external factors the overall financial performance of transformed enterprises failed to improve significantly.

Two state-controlled agencies have been instrumental in assisting the privatisation and restructuring process: the Privatization Agency (PA) and the Bank Rehabilitation Agency (BRA). The former also holds the unsold shares of privatized enterprises on behalf of the country. As of end-June 1999 shares with an appraised value of 465 DM million, representing 11.3% of the total appraised value of privatized enterprises, had been transferred to the Privatization Agency.

The BRA is an asset management agency that was initially considered as temporary arrangement for resolving the portfolio of non-performing denar-dominant loans of Stopanska Banka, the country's largest stated owned bank. Subsequently, however, additional claims were also transferred to the BRA. To date, most of these non performing loans are still on the BRA's books, as collection of claims by the BRA has been minimal and only a few loans were sold, generally to the original debtors either at a steep discount or using government-issued bonds. The shares associated with the \$121 million US debt to equity conversion of bank debt effected under the 1995 SRP were transferred from the BRA to the Privatization Agency, following the adoption in April 1999, of the *Law on Privatization of State Capital*.

Although up to 12 transformation models of socially owned enterprises were allowed under the Law on the Transformation of Enterprises with Social Capital, buyouts have been the predominant method of privatisation. Buyouts, together with the internal shares granted under the "old law" accounted for about half of the privatisations undertaken as of end-1999. Meanwhile, sales of enterprises to private investors accounted for about 19% of total transformation, of which about 10% with social capital had been privatised.

Scope of privatization

Under the Law on Transformation of Enterprises with Social Capital (Official Gazette No. 38/93), also known as the Privatization Law, some 1.132 enterprises were privatized by the end of 1997, 113 of them was large, 274 medium-sized and 740 small ones¹. As of December 31, 1994, the book value of the enterprises to be privatized was 83.2 billion Denars, or about USD 2.2 billion. These enterprises represent over half of the total assets of FYROM economy and employ roughly half of all workers. When the Law was enacted the number of all enterprises with social capital was 1.920. Out of them, 1.250 were subject to privatization according to the existing Law. The remaining 670 enterprises are the enterprises in public utilities, public works, large infrastructure systems, natural monopolies, social services, agriculture, land, forestry and other natural resources management and they are not subject to privatization according to this Law. However, in 1996, an agriculture privatization law was enacted and it encompasses about 360 legal entities (150 enterprises and 210 cooperatives). Banks and other financial institutions are being transformed according to other laws, part of a wider financial sector reform. They are all already private in majority. The biggest banks have been restructured. Socially owned apartments and business premises were privatized earlier, according to different laws and procedures.

The privatization process has not ended by the main privatization law only. There will still be some activities for privatization. First of all, there is a new process which is already on and this is the privatization in the agriculture. The agriculture privatization law - Law on Transformation of Enterprises and Cooperatives with Social Capital Operating with Agricultural Land was enacted in April 1996. There are approximately 360 enterprises to be privatized according to this law. It is expected that the majority of these enterprises will be privatized by the beginning of 1998. The privatization in the agriculture has the same philosophy and procedure as the privatization of the industrial sector, with the only difference that the restructuring of combines containing several different businesses is compulsory. This process has also started and it will continue during this and probably next year.

¹ In accordance with the Privatization Law at least two conditions out of three should be met for an enterprise to be classified as small, medium or large. A small company has no more than 50 employees, its total annual revenues are less than 8,000 average monthly salaries and the book value of its operating assets is not higher than 6,000 average monthly salaries. A medium-sized company has no more than 250 employees, its total annual revenues are less than 40,000 average monthly salaries and the book value of its operating assets is not higher than 30,000 average monthly salaries. Other companies exceeding these limits are categorized as large enterprises.

The most important part of this privatization is the privatization of the agro-kombinats. These kombinats control less than 20% of the agricultural land. More than 80% of the agricultural land is already private and has been privately owned by farmers during the whole socialist history of the country. The socially owned sector generates approximately 35% of GDP in agriculture of FYROM. The market of the agricultural land has been in existence ever since. However, the land issue is still not resolved in the country. The law on land is being prepared and it is in the Parliament procedure and should be enacted by end 1997. In the meantime, the Law has a provision that the privatized enterprises will have the right to lease the land free of charge for the 5 years subsequent to privatization. The draft law on land contains a provision that 85% of the land will be given free of charge and 15% will be offered on the market to be leased by private farmers. No preferential treatment is considered for domestic investors.

The kombinats were historically established as a mix of different agricultural and sometimes processing industries. So, one can find primary production of wheat, grapes, fruit, vegetables, cattle breeding, poultry farms, as well as wineries, canning factories, abattoirs, dairies, even hotels, shops etc. in one kombinat. The Government policy regarding these kombinats is to restructure them by selling them as separate businesses. In order to facilitate this process, the Agency demands from the kombinats to have separate valuation for different businesses. Together with the Ministry of Agriculture, it has also published guidelines on how to do the restructuring. The Ministry of Agriculture produced guidelines for extracting 15% of the land, so far used by the kombinats, to be offered on the market for lease.

Institutional Framework

The central legal document governing the privatization of socially-owned enterprises is the Law on Transformation of Enterprises with Social Capital enacted in June 1993, that was cited above. Other laws connected with the privatization process that have been enacted by Parliament are the Law on Transformation of Enterprises and Cooperatives with Social Capital Operating with Agricultural Land (Official Gazette No. 19/96), Concession Law (Official Gazette 42/93), Trading Companies Act (Official Gazette 28/96), and Law on Issuing and Trading with Securities (Official Gazette 7/97).

The institution responsible for administration and support of the process is the Agency of FYROM for Transformation of Enterprises with Social Capital, also known as the Macedonian Privatization Agency. The Agency is a public enterprise, that is a governmental institution. It is self-funded by proceeds from sales of enterprises. The Agency, which is managed by a Management Board consisting of nine members, is headed by a Director. All these officers are nominated by the Government. The Agency must submit a semi-annual report on its operations to the Government and an annual report to Parliament. The Agency has been subject to an external audit by the Public Revenue Office and by Coopers and Lybrand. There is still not a law demanding annual audit of state agencies. It will soon be provided in the legal system of the country. The audits done so far, were done with a special request by the Ministry of Finance or by the Agency itself. In order to fulfill its responsibilities the Agency has organized its resources into several departments: transformation and restructuring department, finance and control department, legal department, public relations department and administrative and software support department.

There is also a Government Privatization Commission consisting of nine members, who are all Ministers except for one. This Commission makes the final decisions regarding the transformation of each enterprise. This means that after this decision the sale may start. The transaction itself is administered by the Agency.

An important supporting institution that is very much involved at the beginning of the privatization process is the Public Revenue Office (Uprava za Javni Prihodi). This institution controls the privatization undertaken so far on the basis of former laws and verifies whether the procedure was in accordance with the then existing laws. The biggest transformation of equity before the existing Law happened with the Law on Social Capital - the former privatization law, being enacted within former Yugoslav Federation. The Public Revenue Office thus checks whether and how much of the equity has already been privatized and how much of the equity is available for privatization according to the new Law. In the private sector a number of auditing firms, management consulting firms, valuation firms, etc., have been established and have become involved.

One specific issue was at a very close attention during the implementation of the law. This was the issue of transparency of the process. The Law itself does not contain very detailed provisions regarding the privatization transactions. So, the Agency was forced to build transparent rules and guidelines and to offer them in the information package to investors before they place the bid. The Agency adopted criteria for selection of bids if competing bids would arrive. All information that a company will start the privatization transaction, according to a certain privatization technique is publicly announced. It is announced in the main local newspaper "Nova Makedonija". After the announcement, containing the main figures of the enterprise's operation plus an information where the other data might be collected, the potential investor may come to the Agency and collect the information package for the respective enterprise. It can buy it for the price of 1.000 denars for a small, 2.000 denars for a medium and 5.000 denars for a large enterprises. The package contains the summary of the valuation, the privatization program (being a sort of prospectus for the enterprise), the criteria for valuation of bids and the guidelines on the procedure how the bids will be selected. Additional information can also be available upon request.

The experts, if selected within a foreign technical assistance program, are selected with the rules of the donor. There were also many local experts who were involved in the process. They are mainly recruited by the enterprises - valuation, corporate finance, or legal experts. The Agency also, from time to time, uses the help of consultants - valuers, auditors, lawyers, professors. It usually collects several bids for the selection.

The foreign investors do not have a very straight forward access to information about a specific privatization going on. The first reason for this is that the public announcement for collection of bids is announced in local newspaper. However, the Agency provides regularly information in Internet about the enterprises that will soon be privatized. Once the investor know about a certain enterprise, they may get the information about it from the Agency.

5.8.2.Methods of Privatization

According to the Law for Transformation of Enterprises with Social Capital, several methods or models of privatization are available to enterprises. The models are somewhat different depending on whether the enterprise is defined as small, medium or large. Small and medium-sized enterprises may propose their own models, whereas large ones must select a model in consultation with the Agency.

Small enterprises may be privatized according to the following models:

- **Employee buy-out (E.B.O):** The employees are given the opportunity to buy out the enterprise. They may do that if they purchase at least 51% of the appraised value of the enterprise. They are obliged to buy the remaining part in equal annual installments over the next 5 years without interest.
- **Sale of a so called ideal part of the enterprise (in the form of quotas, stakes or shares):** A part of the equity - a stake of the enterprise may be sold by a public call for bids. If there are more than one bidder an auction is to organized. If the sale was unsuccessful, after the second public call a direct agreement with a prospective buyer may be conducted.

Medium-sized enterprises may be privatized according to the following models:

- **Sale of the enterprise or a part of it:** This is the same model as applied for the small enterprises.
- **Public offering:** A public offering is considered to be successful if at least 51% of the value of social capital has been sold. The shares are sold through a public offering. The enterprise transfers the remaining unsold shares to the Agency as a preferred, non-voting stock. The Agency is obliged to offer these shares to the public within a three month period after converting them into common shares.
- **Leveraged management buy-out/management buy-in (LBO):** A public announcement is made to collect bids to buy an enterprise according to this model. This is an attractive model because it

offers the possibility to buy the enterprise on an installment basis. Same as other models, it is open to all domestic and foreign, physical and legal persons. An LBO agreement may be made with the investor who offer a business plan for the enterprise. According to this model the buyer that offers the most attractive program through public tender can obtain the right to control the enterprise by means of a down payment of only 20% of the appraised value of the enterprise. They will be obliged to purchase at least 51% of the shares in not more than 5 annual installments with no interest charge. In the meantime the Agency holds the unpaid shares, which are preferred shares with an option of their conversion into common stock if the shareholders do not pay the installments or if other conditions are not fulfilled.

- **Issue of shares for additional investment:** The enterprise may increase its capital with a new issue. If the new issue is greater than 30% of the appraised value of the company, the Agency will make an agreement with the investor in which the investor will be offered an opportunity to purchase 51% of the total number of shares of the firm within a period of not over 5 years. The Agency receives preferred shares with an option to convert them into common stock if the shareholders do not comply with paying the installments on time.
- **Debt/equity conversion (D/E Swap):** If the creditors and the enterprise find it viable, an exchange of debt for equity may be used as one of the models of privatizing a firm.

Large enterprises may be privatized according to the same models as medium-sized ones. One difference is that the down payment for a leveraged buy-out is only 10% rather than 20%. Another difference is that the additional capital investment required is 15% instead of 30%. The Agency also plays a much more active role in the privatization of large enterprises as compared to small or medium-sized ones. A special body, the Transformation Board, has been established to prepare the privatization of large enterprises. Half of the voting power in this Board is vested in the Agency and the other half in the enterprise. In addition to these models, there are three more possibilities for transformation. They may be applied to all enterprises irrespective of their size.

- **Leasing:** An enterprise may conclude a leasing agreement with a lessee after a call for public tenders. A clause of buying out the firm is included in the agreement, so that the lessee, while paying for the lease, also pays installments on the purchase of the company over a period not longer than seven years.
- **Sale of assets of the enterprise:** Upon liquidation of an enterprise, its assets may be sold separately. If some liabilities remain uncovered, the Agency is not obliged to compensate for them. Creditors participate in the proceeds. Employees are treated as under bankruptcy proceedings and may be rehired by the successor enterprise.
- **Transformation of enterprises under the bankruptcy procedure:** Upon the proposal of the leading creditor or creditors, an enterprise may suspend its bankruptcy proceedings for a period not to exceed 12 months in order to undertake certain activities for transformation, such as debt/equity swaps, programs for refinancing, etc.

Table 35. FYROM: Privatization by Model of Transformation, by number of Firms, (1995-1999)

Model of Transformation	1995	1996	1997	1998	1999
Number of Firms					
Old law	59	65	66	67	66
Buy outs	267	511	649	764	780
– Employee Buy outs	210	301	331	363	384
– Management Buy outs	42	123	190	253	247
– Other buy outs	15	87	128	148	149
Sale of ideal participation	12	23	35	59	67
Leasing	3	4	4	4	4
Additional capital	5	14	16	19	20
Residual	11	35	27	26	28
Debt/equity conversion	1	15	36	63	75
Foreign equity	153	154	156	156	156
Private equity	60	55	95	113	128
Liquidation	33	38	48	164	164
TOTAL NUMBER OF FIRMS	604	914	1.132	1.435	1.488

Source: IMF country report, June 2000, page 113.

5.8.3. Privatization procedure

Required approvals

The process of privatization proceeds as follows. The company (or the Agency after the deadline period expires) decides to transform. It chooses the model or the combination of models it wishes to apply. It requests one of the licensed appraisers to value the enterprise at its expense. If the company has already started privatization under the previous Yugoslav law, it must be submitted to scrutiny by the Public Revenue Office and follow the procedure laid down in the report of this institution, which must have been approved by the Agency. The company procures all the necessary documents and submits them to the Agency. At the same time an announcement must be placed in the press to inform the prior owners of the enterprise of the impending privatization. The Agency analyzes the proposal of the enterprise and issues an opinion within 60 days. The Government Commission makes the final decision within 30 days and after that the transaction may proceed.

All values used in the privatization process (appraisals, share prices, etc) must be stated in Deutsch Marks (DEM). Payments, however, may be made in local currency, frozen foreign currency or Government bonds issued for bank rehabilitation purposes.

Valuation is obligatory for all enterprises that are to be privatized. The Agency consequently prepared a Methodology for Valuation of Enterprises with Social Capital. The methodology is based on internationally known methods and with the use of international accounting standards. The main methods proposed are the adjusted book value method, income approach methods (e.g. discounted cash flow) for the larger and strategically more important companies, and a number of shortcut methods (e.g. comparable or earnings yield) for the smaller companies. The methodology elaborates the main principles of valuation, the contents of the valuation report, etc. and it gives the appraisers the discretionary right to find and put forward arguments for the price that they would suggest. Valuers suggest a fixed price and the valuation is then reviewed by the Agency. That price is actually the sale price of the enterprise. Valuations are to be made by appraisers licensed by the Agency. More than 150 valuers have been licensed thus far.

The privatization program is to be carried out in accordance with the Guidelines for Preparing Privatization Programs issued by the Agency. These Guidelines suggest that the privatization programs be prepared

much like a prospectus, informing potential investors about the enterprise, its main features, its major strengths and weaknesses, and overall potential. The model selected for privatization is also presented in this document.

Other documents that should be submitted to the Agency together with the Decision for the Transformation are the following: register of the charter from the Commercial Court, evidence of ownership of real estate, and the report prepared by the Public Revenue Office and approved by the Agency for verification of privatization done according to the former law.

5.8.4. Enterprise Restructuring

In accordance with the strategy to introduce a market economy, the Government of the country regards privatization and restructuring as the most efficient means to implement structural reforms.

The legal restructuring – of the company is automatically performed with the privatization of the enterprises. The name of the Law for transformation actually means that two types of transformation are happening in the process: ownership transformation of a state-owned enterprise into a privately owned company and legal transformation of a state-owned enterprise into a limited liability or a joint stock company. So, the data for the enterprises undergoing legal transformation (restructuring) are equal to the enterprises being privatized.

As long as the financial and especially operational restructuring is concerned, an intensive debate was on in FYROM. The dilemma was in the order of the restructuring, should it be performed before or after privatization. At the beginning, it seemed much more logical not to have any restructuring before the privatization, because of the following reasons: restructuring is expensive, and the restructuring will be done with the best possible results if it is done by the new private owner and not by the state. The new owner knows best how to restructure the company. And this was indeed the attitude of the Government: to try to sell as many enterprises as possible without restructuring them and let the real owners do the restructuring which would suit their needs.

However, it was soon realized that some of the companies, especially some large ones, would not be able to get privatized. This is true for the very big loss-making enterprises who are not attractive for any potential investor, and who represent a heavy burden to the economy. The way they operated, they spent the rare resources in the country, rather than creating new value. It became obvious that a certain kind of restructuring was inevitable. This was especially needed because these enterprises were in a very bad financial state. Inherent inefficiencies, the collapse of former trading links, the imposition of a hard budget constraint have been all causes of this phenomenon. This situation generated the so called bad debt problem. A large number of assets (debts) in the portfolios of banks are either non-performing or of a doubtful quality. On the other hand, payments arrears between enterprises have grown substantially. The ratio receivables/company assets for FYROM economy as of December 1997 amounts 28%, which is considered to be rather high.

The kind of restructuring which was to be performed was defined as a “defensive”, pre-privatization restructuring. This was in line with the country’s model of the privatization - the commercial, case-by-case approach. The idea was that more effort should be put in the pre-privatization phase in order to have a smoother and easier post-privatization adjustment.

This approach was supposed to include the liquidation of nonviable enterprises and units, with an aim to reduce the total costs in the overall economy and to promote the development of the economy by directing the scarce financial resources towards their most efficient utilization.

In order to stop the escalation of the negative repercussions resulting from the bad functioning of these enterprises, in 1994, the Government has taken actions for the preparation of a Special Restructuring Program (SRP) of the 25 biggest loss-makers in the country. The 25 largest loss-making, socially-owned enterprises are very sensitive both economically and politically. In 1993 they generated losses equivalent to 13% of the GDP, or more than 80% of the total losses of the business sector. Loans to these enterprises

made up about 60% of the total bad loans in the banking system. The 60.000 workers employed in these enterprises at the end of 1994 represented over 10% of the national work force.

The mentioned restructuring process was composed of the following elements: stopping the cash outflow, cost reduction, closure of nonviable units and concentration of the whole production in all units which were able to survive, laying-off redundant workers, reorganization of assets, managerial and financial reorganization. There was no new investments within the framework of this program, except some necessary minimum self-liquidating investments that were supposed to accelerate the restructuring process and make it more efficient. In the creation of the program and in the many phases of its development so far, the Government was supported by a significant input from the World Bank. The Government received abundant technical assistance in the creation and implementation of the project, but it was also financially supported by the agreed financial and enterprises restructuring and social reform credits.

The main features of the special restructuring program are to establish transparent set of rules with time bound program, providing for: hard budget constraints, isolation of SRP enterprises from banking system, financial and other support for displaced workers, liquidation of non-viable enterprises or non-viable components of enterprises, transfer of social assets to local government, carve-out and privatization of non-core commercial assets, privatization of viable enterprises or viable components of enterprises. The objective was to force the enterprises to be self financing during the life of the program and incorporated a requirement that each of the enterprises be in the process of privatization.

Following that program, a special Law on Restructuring of Some of the Enterprises Showing Losses was enacted by the Parliament in January 1995 (Official Gazette 2/95) and this Law had been effective until December 31 1995. The SRP Law provided the following: abolishment of workers councils, placing Government nominees in control of enterprise boards of directors, suspending collective bargaining agreements, including right to long advance notice of termination of employment, providing funds from budget to cover cost of severance payments to displaced workers, setting tight deadlines for enterprises to demonstrate viability, a moratorium on payments against existing bank loans and other credits, placing enterprises on a cash basis so that there will be no further accumulation of arrears to suppliers, conversion of the debts to State-owned banks and utilities into SRP shares, limitation of any credits to enterprises to self-liquidating trade credits tied to firm sales orders from creditworthy customers, allowing the enterprises to use the proceeds from the sale of assets or business units for their own operations, creation of inter-ministerial commission, chaired by Minister of Economy, as body responsible for implementing SRP Law etc.

The special restructuring program has started to demonstrate certain effects. Over 15.000 workers, all of the defined surplus workers with the program have been laid off and have accepted enhanced severance packages. The enterprises were divided into smaller units. A lot of spin offs from the core businesses were designed, so that instead of 25 enterprises there were some 130 enterprises working on FYROM's market.

One of the biggest activities of the enterprises was their preparation for privatization. They were all in the privatization transaction procedures. By the end of June 1997, some 80 enterprises had been privatized and the process for privatizing them all was very intensive. Nine enterprises were liquidated and the expectations were that there was be more liquidations, especially among the hard-to-sell enterprises. The Special Restructuring Program required the mandatory conversion of certain categories of debt (primarily obligations due to banks and government agencies) into equity. Each of the enterprises in the program had issued the required shares, with the result that certain of the enterprises had effectively been privatized by this step alone. The expressed intent of the Government, and the Bank Rehabilitation Agency, was to sell the SRP shares which they hold as soon as possible.

In trying to asses the results of the SRP program, from the perspective of its objectives, it may be concluded that lots of its objectives were fulfilled. The reasoning for this is presented in the following lines.

These enterprises were put under strict hard budget constraint. Had there was no the SRP, they would have still been a heavy burden to the economy and a drain to the very rare resources in the country. The

enterprises were completely isolated from the banking system. With the exception of very small amount of self-liquidating credits they worked with their own cash flows. The Government provided financial support for displaced workers. It paid the severance payment to these workers from the Budget. It also provided financial support to the Labor Re-deployment Fund (within the World Bank credit) for assisting unemployed people in their re-deployment efforts. Nine enterprises have been liquidated so far, with the expectation that there will be more of them, especially the ones which won't be able to get privatized. All the social assets (hospitals, kinder gardens, school etc.) were transferred to the local government. All non-commercial assets are elaborated separately in the privatization plans of the enterprises and they are privatized separately from the core business. The privatization plans of the enterprises are prepared having in consideration the separate parts of the business and letting them privatize separately as viable enterprises.

It can also be concluded that the psychological impact of the program was tremendous. The enterprises understood what a hard budget constraint really meant and they soon found out that this restructuring was completely different from the ones that they were used to in the past. The program helped them and the society as a whole to better understand the functioning of the market.

The cost of this type of restructuring was not very high, because it was a defensive, non-investment oriented restructuring. The biggest costs were associated with professional help, but it was provided by a technical assistance program, financed by the World Bank loan worth \$3 million US. The Government also committed itself to provide self-liquidating loans in total amount of \$10 million US.

Unlike many of other CEE countries (such as Bulgaria), FYROM did not adopt mass privatization schemes, because of the policy of its government to find dominant owners for its enterprises. This was the reason why investment funds were not created in the country. This has produced problems, not only in the privatization itself, but more with the lack of the funds' good contributions to the economy. So, the capital market in FYROM is very undeveloped and the enterprises are deprived of an important agent which might help a lot in their corporate governance and in their post-privatization restructuring. The Law on investment funds is being prepared and it is expected that the first funds will soon be established afterwards.

The banks also do not have very big role in the corporate governance of the enterprises. The capital structure of companies is equity oriented. The banks exercise such a role to a greater extent in the 25 large loss-making enterprises, since they were forced by law to make a debt-equity conversion. Owing to this law, banks are now majority owners in 5 big enterprises. No special favors are accorded to the banks to accept equity position in the enterprise and to be more active in the corporate governance.

5.8.5.Evaluation of the Results

In the effort to value the privatization process in FYROM, it can be said that it was relatively fast, transparent and open. Shortly, the ownership transformation can be considered as accomplished to a great extent. The domestic private sector is now dominating most of the formerly socially owned companies. More than 1.000 enterprises, out of the total of approximately 1600 industrial and agricultural enterprises have been privatized. As of December 31, 1994, the book value of the enterprises to be privatized was about \$2.2 billion U.S. The transaction value of the privatized enterprises by mid 1997 was USD 1.9 billion. The proceeds from the privatization, according to the existing laws, together with the debt/equity conversions and the additional capital so far are approximately \$560 million US. The difference comes from the fact that most of the payments are deferred, the employees buy 30% of the shares with discounts, some part of the equity was already privatized with the former privatization law, a small amount of minority shares was not sold etc.

However, when one comes to more qualitative assessment of the results, two issues for which different results would have been better appreciated become very obvious.

The first one is the inflow of foreign capital in privatization. FYROM enterprises were not able to attract enough foreign investment in the privatization. The main reason for this was *the high political risk that was associated with investment in FYROM*. In the period when many investment opportunities were opened for the businesses all around the world, investment in FYROM was perceived to be too risky and on the other

hand *it was low visible*. So there were only 15 enterprises that were privatized by majority participation of a foreign partner with a total of approximately \$31 million. The foreign partners came from European Union countries and from USA.

The second objective which was not achieved enough was the *corporate governance*. It happened that in most of the Agency's announcements for bids, the only bid for buying the company came from its employees and management. Thus, the ownership structure of most of the companies now is such that they are predominantly owned by their employees. It is perceived that this may be one of the biggest problems in the future, because the good corporate governance, with so many MEBOs in the privatization process is not in place. In the majority of such companies the management has not been changed, no new capital and management skill have been injected. The new achievement is only the new incentive structure in the enterprises. The employees, now being owners of the enterprises should only be motivated to work better for better results of their company. Unfortunately, this link is not perceived so directly and openly and many enterprises still do not exercise any major change in their operation. One additional process which needs to be improved in order to have better overall results and market-based discipline is the bankruptcy procedure.

Although the law on bankruptcy is in existence and has been implemented for many years, there are still many issues for correction, especially in the field of implementation. The hard budget constraint is being imposed more and more in the real life, but it is expected that the new law on bankruptcy, which is about to be enacted by the Parliament will put much more order into this important sphere of economic life.

This problem is also tied to the first one - to attraction of foreign capital in the country. It can often be noticed that the new owners are not very much willing to give the control to some other partner - no matter local or foreign.

This is the reason why the government is resolute in designing and implementation of various post-privatization efforts. **Everybody in the country agrees that it was a good decision to go on with privatization** in spite of the unfavorable environment and that it was better to continue with the privatization than wait for better circumstances. However, the public is also expecting some other activities, especially in the field of attracting foreign capital and in the field of strengthening corporate governance.

From a political point of view, the privatization has certainly contributed to dispersion of economic power in the country. The enterprises have always had a great deal of independence from the state, but after the privatization, this link is definitely broken, the different types of subsidies are diminishing evidently and the state has no power to interfere into the companies' decisions, but it is also making it clear to them that it is no more granting subsidies and that a hard budget constraint is being imposed in the economy.

There will still be some activities in the privatization. The next more significant privatization will be the privatization of the telecommunication sector. The Government has already taken a decision to privatize the telecom. The post enterprise has been already divided into two companies: posts and telecoms. The telecom company is in rather good shape. There were massive investments in the company, with the involvement of EBRD in the previous years. The law for telecommunications is in place, so that all the necessary preparatory activities are already done. The tender for selecting an international investment bank as an adviser in the process has already been published. The idea is to attract a foreign telecom company as a strategic investor with a sizeable stake of shares and later on, to float part of the shares on the stock market.

The next phase will be the concessions with Build-Operate-Transfer (BOT) arrangements in the public infrastructure sector. There will be some projects in the energy sector and in the road construction sectors. The tenders for these arrangements will be publicly announced.

Additional Information

The Agency publishes a monthly bulletin in the local language entitled *Privatization FACTS*, which summarizes information about the privatization program and data on companies being privatized. An English

translation is also available. The bulletin and other materials, such as translations of laws, are available on the Internet: <http://www.mpa.org.mk>.

Specific Considerations for Involvement of Foreign Entities

Domestic and foreign entities have an equal position in doing business in FYROM, i.e. foreign investment restrictions do not exist with a few exceptions in a case of investing in some special areas (defense, for example). This principle covers also the securities industry. The issuing of securities is not taxable. There are, thus no specific tax relieves, other than the general ones and which are specially elaborated in the chapter taxation. It should be noted here that there are also no restrictions for countries citizens on the purchase of foreign share issues.

Having all this in consideration, it may be concluded that the opportunities for foreign participation are good for FYROM's Stock Exchange. The Exchange is still not well developed, but the potentials do exist and it is mainly an issue of time when it starts being more busy. The legal framework, with few exclusions, has already been set up. The potential risk for the buyer is probably not very high because the prices on the Stock exchange are very low and in most cases they would provide a good value for money. As an exit vehicle, the Stock Exchange is still not well established, but it will start satisfying this objective as long as it gains liquidity, which should happen in the next year or two. It is also important to be mentioned that after the privatization, most of FYROM's companies are owned by many individual owners, so that control over the company may be achieved even by a minority stake, which can be freely acquired on the country's Stock exchange. Additional shares can be easily bought later on from the existing shareholders.

After all the above analysis the question **"Did Privatization increase profitability in FYROM?"** is revealed.

According to the IMF resources, a substantial empirical literature suggests that privatization improves the profitability of firms but much of this literacy fails to correct for potential sources bias. A number of studies suggest that privatized firms tend to be more efficient and profitable than those that have remained in state sector. However, many of the studies that compare the performance of privatized or private firm, with firms in the state sector have not addressed the fact that privatization is endogenous. In particular, there is a reason to believe that more profitable or potentially profitable enterprises are likely to be privatized early in process. A simple comparison of the performance of enterprises that have been privatized with those still in state sector will therefore be subject to selection bias. Comparisons of pre-and post privatization performance have often failed to account for changes in economic conditions that may affect all firms. This is a particular **concern for economies in transition (such as FYROM and Bulgaria)** where privatization is often accompanied by other reforms, such as stabilization, which may lead to general improvement in profitability in the enterprise sector.

5.8.6. Financial performance of enterprise Sector

Since 1998, the authorities had attempted to address the financial situation of a core group of 12 major loss-makers through sale liquidation although aggregate losses for this group accounted for about 1% of GDP as of end-1998, mounting losses by these enterprises pose a major threat for the country's medium-term development as they crowd out bank credit to viable firms and contribute to misallocation of resources. The implementation of the authorities' enterprise reform program has been considerably delayed primarily reflecting the authorities' concerns about the social impact of the reform. However, as part of the authorities efforts to secure financial support from the international community, enterprise reform recently regained momentum. As a result of end March 2000, 6 enterprises had been sold to private investors or workers, including OKTA oil processing, two enterprises were liquated, the outcome for Feni, the nickel mining and processing holding company is pending finalization of agreement with the World Bank and agreements on the sale or liquidation of the remainder remains to be addressed. The direct costs for the budget association with the enterprise reform identified thus far, is expected to amount to about DM 64 million. In addition, the government implemented debt equity swaps in 2 enterprises in an amount of DM 13.1 million. The authorities are identifying a list of additional loss-makers for inclusion in the next stage of enterprises reform under preparation.

The legal framework supporting enterprise operations still needs further revamping in order to strengthen creditors rights and the efficiency of the court system. To the end, the amendments to the laws on Bankruptcy, on Execution Procedures, and on Contractual Mortgages, are near finalization. The new bankruptcy law is intended to reduce the excessive complexity of the 1997 law, to ensure efficient bankruptcy administration by district courts and to reduce the considerable delays in processing. Under a new Central Registry Law, the company register is expected to be transferred from the courts to a new central company register. **The legal framework for foreign investment is under review.**

5.8.7.Sectors with investment potential

The objectives of the development strategy of FYROM are to build an open, stable and market-based economy. In the focus of its future development the prosperity of the private sector is positioned. It will predominate in the major part of the national economy. In the next period there will be an effort to privatize the remaining part of the state ownership in the enterprises, banks and some of the public sector.

The next pillar for the private sector development will be the capital market development. The establishment of the treasury system, the establishment of the confidence in the financial system, helped by a massive education and promotion of the new skills and knowledge will help the capital market to start working with full capacity.

FYROM is committed to IMF and World Bank, to build an export oriented economy. Having a small market, the export is a must for obtaining a stable and sustainable growth. The export-oriented projects will be fully supported by all potential market-friendly measures.

The official National strategy of development of FYROM was prepared by the Government and formulated at the beginning of 1998. National preferences for the further development are the following:

- development of an open and free market economy in an open society and a democratic political system,
- completion of the transition process,
- positioning attraction of foreign capital and foreign economic relations high on the priority list of the government development policy,
- coping with unemployment,
- achievement of a sustainable economic growth.

Having these premises in mind, it is already obvious that FYROM won't lead a policy for investment in some special sectors. It tries to lead an equally market friendly macro-economic and micro-economic policy for all the participants on the market and not to have some sector incentives policy.

What is important to know in the field of the investment policy is the Government's Public Investment Program for 1997-1999. The Public Investment Program envisages 43 projects, 23 of them being completely new projects. The total value of these projects is \$1.3 billion U.S. The main orientation is towards reconstruction and modernization of the existing infrastructure and in the building up of some new capacities. The projects are mainly in the energy, transportation and telecommunication sector. Some of the projects will be financed by some credit line, whereas some others will be financed by BOT arrangements.

It has already been mentioned that sectors with export potential so far proved to be the following: finished textile goods, finished leather goods, shoes, vehicle and bus assembly, electronic equipment, telecommunications equipment, packaging, lamb meat, fruits and vegetables, processed foods, wines, automotive accessories, electric motors, metal fabrications, steel pipe, furniture, construction, tobacco,

cigarettes. Many of them can offer good opportunities for further investment and development. This variety once again shows the diversity of FYROM's economy.

Textile, leather and leather goods: The manufacturing textile and leather goods already possesses a big number of capacities. The textile industry, including fibers, fabrics and finished products, together with the leather products industry are major employers and contributors to the industrial product of the country, although their contribution to the industry product has been sharply decreased (from approximately 30.8% in 1989 to only 13.9% in 1995), showing the big problems these sectors are facing especially with the loss of markets. Cotton thread and fabric, denim cloth, wool yarn, fabric and knitted fabric, are the principal products. Pig, calf, cow, bull, lamb and sheep skins are all processed for the local manufacture of furniture, clothing and shoes.

The competition in these sectors, even in the former, socialist system was very high, so that their performance tended to be better than in some other sectors. They have developed good products, they have managed to train well their workers, they have established good contacts with their consumers, being, thus, present on the major European and American markets etc. The majority of these enterprises are now privatized. The restructuring in these sectors is also going relatively well. The enterprises are now thinner, with less employees in the former social sector, and many new private ones entering the market. The prospects for the future of these sectors are the following: these industries are capable of developing further, they have skilled and non-expensive working force, they have well established markets, their proximity to Europe is very convenient and they can easily compete internationally. However, in order to increase their competitiveness further, they must re-think their strategies, try to find niche markets and add more value to their products.

With capacities for annual production of 7 million pairs of shoes, this industry has been a major export earner in the country. This industry has managed to attract foreign capital in the privatization process. The privatization in all the companies has been completed and new private ones entered the market.

The biggest textile factories are the following: Teteks from Tetovo, Oteks from Ohrid, Vinka - Vinica, Biljana - Prilep, Mokel - Bitola, Astibo - Stip, Makedonka - Stip, Frotirka - Delcevo, Kimiko - Struga. The most famous leather production companies are: Godel - Skopje, Kozarski kombinat - Kumanovo, Dimko Mitrev - Veles etc. and the shoes companies are: Bargala - Stip, Gazela - Skopje, Miska - Tetovo etc.

Vehicle and bus assembly and automotive accessories: FAS 11 Oktomvri, the bus factory from Skopje, Ruen - Kocani, and the group of HTD Zastava companies from Ohrid are among the biggest vehicle and bus parts factories in the Republic of Macedonia. Some of these factories (e.g. Ruen) are among the biggest of their kind in Europe. They are export oriented and have acquired a lot of skills and experience for their further development.

Machine building, electronic equipment, domestic appliances: The contribution of these sectors in the industry product was 13.7% in 1989 and 9.3% in 1995. Metalski Zavod Tito - Skopje, Rade Koncar - Skopje, Emo - Ohrid, Videoinzenering - Ohrid, Mikron - Prilep, Frinko - Bitola etc.

Lamb meat, fruits and vegetables, processed foods, wines: The food and beverages sectors are probably some of the most promising sectors, not only because of their development so far, but even more because of the opportunities not yet revealed and exercised. These sectors generated 10.5% of the industry product in 1989 and 17.9% in 1995. FYROM possesses some natural advantages for the primary food production such as a favorable climate, fertile soil, enough arable land and pastures etc. There are several processing capacities, but the opportunities are even higher and the search for new products, specialty foods and more added value may be the main features of the future prospects of these industries. The main factories are: Zora - Gevgelija, Makedonija - Negotino, Zelop - Sveti Nikole, which are fruit and vegetable processing factories, IPOZ - Resen, Konzervaeksport - Skopje - juice production plants, Mlekara - Bitola, Mlekara - Skopje - dairies, Tikves - Kavadarci, Povardarie - Negotino, Lozar - Veles, Vinojug - Gevgelija - wineries, Pivara - Skopje, Pivara - Prilep - breweries etc.

Tobacco, cigarettes: The tobacco and cigarettes industry have been traditionally important sectors for Macedonian economy, because of the big recognizable quality of FYROM's tobacco. They created 5.2% of the industry product in 1989 and 7.6% in 1995. They have attracted foreign capital so far and the interest for these sectors is existent even after their privatization. There are three cigarettes factories: Prilep, Skopje and Kumanovo and many tobacco stations, the region around Prilep being the best known tobacco production region in the country and world-wide.

Mines, metal and non-metal products: These, mainly resources based industries produced 13.6% of the industry product in 1989 and 10.2% in 1994. The Skopje Steel Works has an annual capacity of 1.2 million tons of hot and cold rolled sheet metal. Other plants (Jugohrom - Jegunovce, Fenimak - Kavadarci) can produce ferrous alloys, seamed tubing and ferrous-nickel products.

Other installations produce lead and zinc (mines: Sasa - Makedonska Kamenica, Toranica - Kriva Palanka and Zletovo - Zletovo, as well as the smelter from Veles, with a capacity of 110,000t.yearly), copper (Bucim - Radovis), gold and silver. FYROM is a significant producer of non-ferrous metals. It contributes 2% to the world's production of lead and zinc. Geological reserves of lead and zinc ore amount to more than 42 million tons, and the potential reserves are assessed at over 85 million tons. The existing capacities for mining and flotation are 2 million tons annually. Deposits of other non-ferrous metals and minerals are very significant and present good opportunities for exploitation. Bentonite, fire-resistant clays, gypsum, quartz, opalite, feldspar are among the ones which have special significance for the economy. Some of these are world-wide renown for their purity and quality.

The total proven reserves of decorative and architectural building stones amount to 16 million cubic meters. Marble is the most significant stone, whose quality and variety of colors make it famous all over the world. The most famous marble producer in Macedonia is Mermeren Kombinat from Prilep. Other stones being found and produced in Macedonia are travertine, igneous rocks, breccia opal, onyx, granite, schist etc.

It is worth noticing that the soil of FYROM is abundant with different non-metallic raw minerals. Out of the total of 60 non-metallic raw minerals known now in the world, 46 have been discovered in Macedonia. Unfortunately, for some of them, the geological conditions are not favorable, so that their production is not viable so far. As long as the proved reserves and production of dolomite, lime, quartz, bentonite, diatomaceous earth, perlite, gypsum is concerned, they offer a lot of opportunities for viable investment. Many precious and semi-precious stones can also be found, but they have not been studied systematically so far. The main capacities in these industries are the following: Radika - Debar - gypsum production, Mermeren Kombinat - Prilep, Sileks - Kratovo, Silika - Gostivar - marbles and other non-metal minerals, Bitolasil - Bitola etc.

Presented differently, there are some points on which the national development strategy will be based, which are obvious even now and they are a good direction where the investment potentials can be looked for:

1. ***Agricultural products, non-metal products, non-ferrous metal products, forestry and other resources based products*** will continue to be important for the national economy also for the future and the strategy will be to stimulate the producers to add more value to the products using those resources. Some of the industries developed on these resources may be the focus for the national industry clusters that would help build the competitiveness of the country.
2. ***The traditional and mature multi-factor industries*** will have to lean their further development to strategic foreign partners, some of them being the main players in the global industries in the world. They will have to re-think their strategies, they will have to try to find niche markets and add more value to their products.
3. ***The high-growth industries (pharmaceutical, tele-communication, computer software etc.)***, being marginally presented in the development so far, will have to be more widely promoted, especially because the main factor for their emergence and growth - the ability of the human

resources - promise a prosperous future for them as well. Strategic alliances with global industries for those businesses is also essential such as joint ventures.

5.9. Fiscal and Monetary Policy, Foreign Exchange

Financial Services

The financial system of FYROM is relatively simple. Unlike other Central and Eastern European (CEE) countries it has had a two tier banking system for a long period before the transition officially started. The financial system consists of a central bank - National Bank of Macedonia, commercial banks and savings houses. The National Bank is responsible for maintaining the stability of the national currency, by controlling the money supply and supervising the banking system. The system is dominated by banks and other financial institutions have limited role.

After the independence, the banking system was very concentrated. Four big banks dominated the sector. As a result of a thorough bank rehabilitation program the bigger bank (Stopanska Banka) was separated to six independent smaller banks. One of the banks was put into the liquidation procedure. All banks in the country were privatized so far and five of them have foreign participation. The Bank Rehabilitation Agency (BRA) administer the rehabilitation process of the banks.

Financial intermediaries, like investment funds, pension funds (other than the state pension fund) etc. do not exist in the country, with the exception of a state pension fund. There are several insurance companies.

There is a Stock exchange, which has been established in 1996 and it is still lacking liquidity. There are several brokerage houses and many financial consulting enterprises.

5.9.1.Fiscal Policy

Fiscal policy reforms are one of the central points of the overall financial sectors reforms. Changes in tax regulation represented a new philosophy in the taxation, approaching it to the experiences of the developed market-based economies. New taxes have been introduced, such as: corporate income tax, personal income tax, real estate tax, with a different definition of the tax base. The turn-over tax has also been changed towards a gradual adjustment to the new VAT tax system, whose implementation started in April 1, in 2000. A mutual feature of the tax reforms is the simplicity of the system, having eliminated the large number of tax allowances for many tax payers, as well as having reduced the large number of different tax rates to single tax rates.

The reforms were also aimed at an excessive decline of the budgetary expenses adjusted to the budgetary revenues. The amount of budgetary deficit has been sized only to the level of the state's foreign obligations. All types of former social categories, or all the categories representing a non-market or state financing of enterprise projects have been eliminated from the budgetary expenditures. These expenditures have been reduced to the level of implementing the basic functions of the state.

Changes have been made also in the legislative regulations for the establishment of a special tax administration, and in the rules providing for a more market approach in the accounting system, and all the necessary preparations have been undertaken for the shift towards a unified treasury system.

The most recent changes in the fiscal policy are even more business friendly. They provide for a decline of the tax burden of the corporate profits from 30% to 15% and the re-investment of profits are deductible from taxes.

According to the IMF country report, in June 2000, fiscal policy in FYROM over the past few years has been supportive of restrained demand management. Fiscal deficits have been relatively small, and mainly reflected externally - financed (on concession terms) capital expenditures. However, the overall fiscal position conceals a number of weaknesses. The taxation of labor income is very high, creating disincentives for job creation. With co-discretionary spending-mainly wages, transfers and social sector outlays – accounting for nearly four-fifths of total government expenditure, the scope for the budget to contribute to the restructuring of the economy is limited and fiscal management of contingencies is difficult. Many line ministries have recourse to self-generated special revenues that are not subject to the centralized budget allocation process, resulting in possible misallocation of scarce resources.

5.9.2.Monetary Policy

FYROM established its monetary independence in April 1992, with the establishment of its own currency - the denar. At the end of 1992 and in the beginning of 1993, the National Bank of FYROM prepared monetary reform program commencing its implementation in May 1993. Monetary reforms were oriented to further growth of the monetary independence of the Central Bank, as well as to a reform of the instruments for monetary regulation, in respect of more efficient control on money supply in the national economy (abolishment of selective credits burdened with para-fiscal functions and introduction of indirect instruments for monetary control, i.e., open market operations). The initiative for reserve money issue was put under comprehensive control of the Central Bank. Starting from May 1993, official foreign exchange market has been established within the frameworks of foreign exchange system reforms in FYROM as well as flexible denar exchange rate.

The reforms implemented throughout 1993 were a solid basis for comprehensive macro-economic policy construction of FYROM for 1994, 1995, 1996 and 1997. Namely, with the cooperation and financial assistance of the International Monetary Fund (IMF) and the World Bank, the government of FYROM has been implementing stabilization macro-economic policy, with monetary policy holding one of the central places. Basic purpose of these programs was to create stable financial frameworks for implementing economic reforms, revitalization of economic activity and realization of long-lasting non-inflationary economic development. The result of such comprehensive macro-economic policy, and, within this, the restrictively oriented, though market determined monetary policy, was the decreasing trend of the inflation rate (measured by the consumer price index) from 1.791% in 1992 to 6% in 2000. Throughout all these years, high denar exchange rate stability was constantly preserved.

The last years, monetary authorities direct their activity towards further reform of instruments for monetary regulations, strengthening the supervision of financial institutions in the country, reform of payments system and further liberalization of interest rates. There is gradual decrease and abolishment of credit constraints within the above mentioned activities, enhanced implementation of indirect instruments in leading the monetary policy, as well as liquidity improvement in the system through payments operations reform in the country.

One of the features of the monetary reform was the gradual abolishment of selective credits, so that the focus of the monetary policy was rightfully shifted away from sector support towards inflation control. The reserve money of the National Bank of Macedonia (NBM) was recognized as the primary target of monetary policy. Movements in the exchange rate were also monitored.

According to the IMF country report - in June 2000, FYROM has been pursuing an exchange rate based monetary policy since 1996. This has proved successful in reducing inflation to industrial country levels. However structural weaknesses in the financial system have prevented a more vigorous economic recovery. Imbalances in the enterprise and banking sectors and in the transmission mechanism of monetary policy. The rapid economic recovery in the aftermath of the crisis, as well as prospects of reforms has helped restore confidence in the banking system.

For most of 1998 there were no significant pressures on the exchange rate, but a tightening of monetary conditions in November was needed to counter short-lived speculative pressures in the foreign exchange market.

With the onset of Kosovo crisis in late –March 1999, there were withdrawal of deposits from commercial banks and delays in debt-service payment by enterprises, causing some banks to experience severe liquidity shortages. Denar deposits contracted by 4% in the first quarter of 1999 while **foreign currency deposits declined by about 20%**. In the event the National bank responded by injecting liquidity while allowing the deposit auction rate to increase to 25% by May 1999. Also the National Bank intervened in the foreign exchange market in April and May with net sales to counter the increasing pressure on the denar.

With the ending of the conflict , demand for currency in circulation normalized with impressive speed and both denar and foreign currency deposits were quickly reconstructed. The NBM intervened in the foreign exchange market to neutralize appreciation procedures. The monetary effects of these large foreign exchange purchases were partly sterilized through the unwinding of previously auctioned NBM credits along with an increased issue of NBM bills. Money increased rapidly in the second half of the year. As the liquidity position of banks improved, the money market interest rate declined to 11% 2000, compared with a peak of 22% in May 1999.

Despite the large swings in liquidity position of commercial banks, deposits and lending interest rates of commercial banks were broadly inflexible. Deposit rates hovered around 9% while lending rates remained within a broad range of 19-27%.

As a part of measures to create a more market –oriented and effect financial system, the NBM is in the process of revamping its set of instruments for the conduct of monetary policy to secure a smooth transition to indirect monetary policy instruments from April 1, 2000. The NBM received technical assistance missions from the funds MAE in December 1998, and December 1999.

Monetary Policy Reforms

The reforms of the financial sector in FYROM, similarly to other countries in transition have three basic goals: increasing the local savings, the investment, the economic growth and attractiveness for the foreign investors, then enabling the most efficient allocation of savings, and development of the active role of the monetary and fiscal policy in initiating the economic development. Starting from the belief that a long-term stability of prices contributes best to increasing the production and opening new jobs, as well as increasing the savings, and efficient allocation of the expensive financial resources, the Central Bank of FYROM, from the beginning of its monetary independence, tends to achieve stability through the monetary targeting strategy. For this purpose, appropriate money supply was used. During 1992 and 1993, the monetary policy provided financial support for the specific priority activities, especially the agriculture, that indirectly influenced the global economic stability. In the second half of 1993, the National Bank started a monetary reform, tending to transform the money supply from a passive into an active variable. Thus, leaving the selective loans for supporting the agriculture and the exports in 1994, the Central Bank could start to control the money supply. The key instrument to the monetary control became the open market operations in the form of central bank deposits and central bank bills.

The economy experienced very high inflation and concomitant high interest rates during the five-year period ending in 1993. Restrictive fiscal and monetary policies have squeezed out most of the inflation but at cost of drying up liquidity. The control over the inflation was followed by high expenses, increased by local and foreign shocks. Locally, the most difficult was the fall of the productivity as a result of the inappropriate allocation of financial resources in the associated labor economy. This contributed to a real decrease of the GDP for 43.5% in the period between 1990 and 1994. However, by increasing the financial stability, there was a clear tendency for showering down the decrease of the GDP. As it was expected, the first signs of economic growth were registered during 1996.

By the end of 1993, the foreign exchange rate of the denar was not an anchor or indicator of the monetary policy, but it was used for adjustment of the payment balance. This caused, in spite of the restrictive monetary policy, the depreciation of the foreign exchange rate to become a source for the increase of prices. That is why, by the end of 1993, the financial instability was still high. Since 1994, the stable foreign exchange rate of the denar in regard to the German mark, supported by a restrictive monetary policy, provided the main stabilizing anchor to the stabilization program. It played an important role in decreasing the inflation to the rate in the developed countries. If the exchange rate starts depreciating at a rate higher than the current inflation rate, it signals that the money offer is higher than the demand. In such case, the National Bank acts immediately and tightens up the monetary policy, and vice versa.

The macroeconomics stability was thus achieved, and starting from March 1994 the inflation rate started to decrease obviously. In 1995 it declined to 15.9%, and it was below 3% in 1996. During 1996, the control over the monetary aggregates was achieved by using instruments and measures that, dictated by the current conditions, were still not in function of the efficient allocation of resources, or in function of the financial market development. The control over the money supply was disturbed by the need to direct almost all of the loans in the largest bank. The monetary policy in 1996 to a great extent resided on the loan limits of the banks, and on the accumulation of government deposits in the National Bank.

5.9.3. Foreign Exchange Regulation

After the independence, a massive liberalization of export and import regimes has been implemented, following the basic World Trade Organization (WTO) principle to eliminate quantitative restrictions to trade. In the import regime, a limited protection is affixed only to the products which are more significant for FYROM, such as the agricultural products, ferrous alloys, vehicles, chemicals etc. Some export protection has been affixed to products having a vital significance to the economy and population of FYROM: some agricultural products, oil and oil derivatives, wood products. A new law for duty tariffs has been enacted, which led to further liberalization of imports, through the decrease of duty tariffs and through the implementation of a harmonized tariff system with the principles of WTO.

The trend towards liberalization and deregulation has been also applied in the foreign investment regulations. Foreign investors have the same status as the domestic ones, and in some areas they have more favorable treatment, enjoying some fiscal and duty holidays. There is no restriction for the industry in which the foreign capital can be invested, nor for the percentage of the company's equity the foreigner can possess. The foreign investor can freely decide whether to retain or transfer the profits out of the country.

5.10. Banking System in FYROM

5.10.1. Overview

A new legal framework for the financial sector in FYROM is now mostly in place, established by enactment of package of laws 1992-93 and subsequent amendments - including the National Bank Act, Banks and Savings Houses Act, the Securities Act, Financial Transactions Law, International Transactions Law Act, Foreign Currency Law, Payment Operations Law and Accounting Law. The National Bank Act of the FYROM was adopted in April 1992 (*Official Gazette* No.26/92) and was amended in 1996 (*Official Gazette* No.17/96). Few months later, in May 1993, the Parliament adopted a new banking law (*Official Gazette* No.31/93), the Banks and Savings Houses Act, that was amended in 1996 (*Official Gazette* No.17/96). These laws established the basis for a new two-tier banking system in FYROM. Prudential regulations for banks covering liquidity position, capital adequacy, asset classification, provisioning and exposures to connected parties, issued by the NBM in the 1992-94 period, were amended at the end-1995 and are now fully harmonized with international standards. Existing legislation encourages the entry of new, well capitalized banks with sound managers and reputable owners. There is still, however, a need to develop a well articulated and implemented set of banking supervision policies and procedures.

The banking system in FYROM is consisted of the National Bank Macedonia of FYROM (central bank), commercial banks and savings houses or institutions, as well as insurance companies and a stock exchange. The NBM is the main regulatory body responsible for the supervision over banking institutions, while private commercial banks are authorized to perform banking operations. Inter-bank payments, including payments between banks and the National Bank, and all commercial financial transactions, are settled through the Payments Operations Service (ZPP - Zavod za Platen Promet).

The traditional financial system is rather weak compared to Western standards, but it compares favorably to other former socialist countries. The use of cheques and credit cards is not widespread and a large portion of small-scale financial transactions takes place in cash outside the formal market. Although short-term credit is available, it is extremely expensive and of difficult access without excessive collateral security. In most cases, local banks have failed to show innovation and initiative in delivering a range of new products tailored to the needs of private businesses. Furthermore, while many of the banks have correspondent relationships with commercial banks in other countries and make use of the REUTER and SWIFT system for transfers, although their world-wide communications still can be improved.

According to the IMF country report, in June 2000, **weakness in the banking and enterprise sectors remain a major cause of low growth**. A large share of non performing assets in the portfolio of large banks, stemming from losses in the enterprises sector. Has been a key impediment to development in the financial sector. The banking system has been crippled by the low level of intermediation, high cost of capital severe lack of financial discipline, and poor allocation of credit. Reforms aimed at strengthening lending practices, encouraging foreign bank participation, improving bank supervision and above all, a consolidation process that breaks away from the past will be key to help pave the path to economic recovery.

Market Structure

The number of banks in FYROM is large. In 1999 there were 22 commercial banks, 2 branches of foreign banks and 15 savings houses. Of the total number of banks, 13 were operating under an NBM license allowing both domestic and foreign operations, while the remaining licensed banks had licenses only domestic operations. Since-and April 1999, a minimum capital of DM 5 millions is required for a domestic operation license and DM 15 million for foreign operation. The minimum capital for foreign operations is scheduled to increase to DM 18 million at end-April 2000 and DM 21 million at end-April 2001.

The banking systems is heavily concentrated. At end-September 1999, Stopanska Banka, the largest bank, accounted for 31% of the system's total assets and 41% of total deposits.

The banking system is dominated by banks controlled by formerly socially owned enterprises, most of them now private. Some of the shareholding companies have become shareholders during bank-reorganizations in the early years. This pattern of ownership jointly with underdeveloped capital markets, has resulted in less than active shareholding participation in banks.

The ownership structure has little foreign participation. The share of foreign capital in the total founders' capital of commercial banks was about 15 % at end 1998. Foreign capital holds a majority stake in only four banks, including one foreign branch from Turkey, two banks from Russia and one from Bulgaria. Western banks have, so far, abstained from participation in the FYROM banking system. This changed rapidly in 1999, with one small equity acquisition by a Greek bank (National Bank of Greece), in addition to the large Greek investment in Stopanska banka.

Banking System Operations – Recent Developments

According to the IMF country report, the level of banking system financial intermediation remains quite low, reflecting low confidence in the banking system, a precautionary preference for holding cash in foreign currency and an attempt to avoid control –and obligations– imposed by the Bureau of Payments Operations (ZPP). Total banking system deposits–denar and foreign currency amounted to only 12% of GDP by September 1999, despite a steady increase in the last two years. The low confidence in the banking system has deep roots associated with events that go back to the time of FYROM independence, particularly the freezing of foreign currency deposits that took place at the time of dissolution of the former SFRY.

Banking system vulnerability

Assessing the banking system's vulnerability is particularly important in FYROM in light of the repeated macroeconomic shocks with economy –wide implications from the recent past. Although more general systematic risks will be significantly reduced upon completion of the sale and recapitalization of Stopanska Banka, the banking system remains vulnerable and subject to large risks associated with its bad loan portfolio, large off balance sheet exposures maturity gaps and interest rate and foreign currency risks.

The banking system is highly vulnerable to credit risks, because of the high share of unclassified exposure and possible under provision. If one-third of total credit exposure were to become non recoverable, the about 60% of the banking system's own funds would be wiped out.

The improved overall liquidity position has reduced the maturity gap and the vulnerability of banks to higher interest rates. During 1999, banks have managed to reduce their short term borrowing and debt to the NBM (mostly short term deposit auctions). As a result the coverage of short term liabilities by liquid assets increased to 70% in September 1999, compared with 60-65% over the last two years. However, a group of banks with maturity gaps of less than one month has remained dependent on Interbank funds for over a year, rendering them vulnerable to liquidity from other banks, eventual NBM support, and sustained rising costs of funds.

The banking system's vulnerability to off-balance sheet risks remains very high given the magnitude of outstanding off-balance sheet claims, the risk of under provisioning and the low compliance ration by borrowers.

The fragility and structural problems of the banking system have affected the transmission channels of monetary policy, making it less efficient. In particular unsound banking practices that continue to lead to misallocation of resources have implied that additional credit has not been channeled in way that maximizes benefits to the real economy. In addition, the high cost of intermediation and a harmful bias in the cost of credit toward dad debtors have effectively, led to an interest rate wedge that taxes viable enterprises and re

The last changes of the Law on Banks and Savings Banks, enacted by the middle of 1996, urge the entry of new banks with higher amount of capital, with good management, and known owners. In order to increase the financial stability, the changes in the Law on Banks presume formation of a fund for insurance of the saving deposits, expected to be founded by the end of the year. The new Law on the National Bank of FYROM strengthens the function of the bank regarding its responsibility for the banking sector stability, its control, and supervision. The purpose of these changes in the banking sector is that the banking system of FYROM approaches to the world trends of banking development such as: a) capital concentration, b) decentralization while making the banking decisions, and c) regional dispersion of the banks' operation.

5.10.2. Interest rates and borrowing conditions

The interest rate policy of the Central Bank was not defined from the moment it became monetary independent till November 1993, with frequent up and down motions. The increases of the interest rate for the current month resulted in their decreasing the next month. Such a type of interest rate policy did not strengthen the confidence, but the inflationary expectations. The consistent policy of the interest rates was

applied in November 1993, when the variations in the Central Bank discount rate were stopped. Decrease of the interest rates was carried out without changing the tendency of their motion. That way the interest rates became an indicator for the condition and the directions of the monetary policy. Anyway, the interest margin between the discount rate and the interest rate of the commercial banks was kept on a rather high level. In average, the interest rate of the quarterly denar deposits of the commercial banks was 60% higher than the discount rate. There is a tendency for decreasing the interest margins.

In the first months after monetary independence real interest rates on both the deposit and lending sides were negative. However, as monetary policy was tightened, nominal interest rates moved up while inflation declined, causing real interest rates to turn positive. Furthermore, there is a large spread between deposit and lending rates.

There are no legal or administrative limitations or restrictions on interest rates. Rates are negotiated freely between banks and their customers. However, the members of the banking section of the Economic Chamber of Macedonia signed a gentlemen's agreement in mid 1995, which, among other things, places a ceiling on interest rates. The ceiling was adjusted quarterly according to a formula which takes into account inflation rate. There were no penalties for non-compliance, but it has helped to diminish rates. In December 1996, in attempt to liberalize financial markets, in a public statement, the NBM advised commercial banks against coordinating their deposit and lending rates by interbank agreements.

The National Bank collects and publishes data on maximum and minimum nominal deposit and lending rates. During the second quarter of 1997 lending short-term rates for Denars varied from 18 per cent to 30 per cent per annum and rates on deposits from 2.5 rate to 7.5 per cent per annum. In October 1996, the short and long term rates for working capital and small-scale industry varied between 30-19.5 per cent per annum with virtually no inflation in the economy. The trend has been for rates to decline as inflation has moderated.

Although short-term credit is available, it is expensive and of difficult access without high collateral security. The largest source of funding for SMEs today is internal savings and informal borrowing instruments. Most start-ups in the private sector begin operations with no bank financing and there is relatively minimal reliance on bank loans as a source for further investment outlays or turnover capital of the country's SMEs. Indeed, there is a widespread reliance on self-financing sources from private and corporate savings. Loans are generally granted for 30 to 90 day periods and occasionally to 180 day periods, with possibilities to rollover.

Availability of credit to the private sector is constrained also by burdensome security requirements. Collateral required by the banks is real estate, foreign currencies, gold, etc., and only rarely will the banks not require security arrangements. An effective Collateral Law that would provide a systematic basis for collateralizing loans and registering liens or charges on a borrower's property being drafted. Currently the use of movable property is possible only if the bank takes the property in hand, which makes this solution impractical in most cases.

5.10.3. Domestic and foreign payment operations (types of bank accounts)

On basis of the legislation regulating the matters of foreign exchange, foreign trade and banking operations, the Government of FYROM and the National Bank of the country (NBM) passed several by-laws, that is, resolutions and regulations which deal with these matters in detail, and are applicable to foreign and domestic physical and legal entities. Some of these by-laws are: *Decision on the manner of effecting foreign payment transactions* (Official Gazette No. 45/93), *Decision on the terms under which funds may be received in deposit from physical and legal entities* (Official Gazette No. 40/93 and 28/94), *Decision on carrying in and carrying out cash denar bills when traveling abroad* (Official Gazette No. 40/93), *Decision on the terms and permissions to enterprises and other legal entities to keep foreign currency deposits abroad* (Official Gazette No. 40/93), *Decision on the manner of acquiring denar inflows by foreign entities in the Republic of Macedonia* (Official Gazette No. 57/93), *Decision on the manner of working with the foreign currency accounts and foreign currency deposits of domestic and foreign physical person* (Official Gazette

No. 63/93), *Regulation on the specific requirements for the opening and operation of representative offices of foreign entities in FYROM* (Official Gazette No. 25/95) etc.

In essence, domestic and foreign entities have equal treatment in respect of the right to open bank accounts in FYROM. There are no differences in the treatment of the manner in which funds are used. The term domestic entities denotes enterprises, banks and other legal entities, including mixed and foreign legal entities domiciled in Macedonia and physical persons resident in FYROM. Foreign entities are foreign legal entities domiciled abroad and physical persons resident abroad.

Foreign currency accounts of legal entities

The foreign payments are effected through the foreign accounts of country's banks, the accounts of foreign banks and other foreign entities in FYROM as well as through foreign currency accounts in which foreign funds are held pursuant to article 90 of the Foreign Exchange Operations Law (accounts of legal entities performing investments abroad, legal entities which have consignment warehouses and accounts representing foreign currency investments of foreign persons). The foreign collections and payments are effected by way of: bank transfers, letters of credit, documentary collection, checks, drafts and other payment instruments which are customary in international financial operations. Official order forms and other documents (prescribed by the NBM) are used in all foreign payment transactions.

The manner of effecting foreign payments is regulated in detail with the Decision on the manner of effecting foreign payment transactions ("Official Gazette No. 45/93), which was passed by NBM on the basis of article 27 of the Law on Foreign Exchange Operations, the guidelines on the manner of effecting foreign payment transactions, No. 09-2/III of June 1994, as well as other by-laws.

Foreign currency deposits of domestic legal entities

For the purpose of effecting foreign payments domestic legal entities are allowed to open the following types of accounts:

- a) foreign currency accounts with authorized banks in FYROM for effecting foreign payment transactions;
- b) foreign currency accounts with authorized banks in FYROM for legal entities that either (i) perform investments, (ii) have consignment warehouses or (iii) have foreign currency investments of foreign persons;
- c) foreign currency accounts with foreign banks, subject to NBM approval.

a) For effecting foreign exchange transactions domestic legal entities can open accounts with banks in FYROM which are authorized for payment operations and foreign credit relations.

The opening of an account is made with a written application by the legal entity to the bank, accompanied by the following documents: documents evidencing the court registration, Notice from the Statistical Office regarding the registration number of the legal entity, information on the authorized signatories of the account as registered with the court, a copy of the regular account card issued by the Payment Operations Service. Initial opening deposit is not required, and there are no account opening charges.

The collection of foreign currency (inflow) in these accounts, may be effected through all payment instruments: payments from abroad, cash payments in foreign currency upon obtaining special approval from the NBM, transfers from non-resident accounts opened with a banks in FYROM and consignment sales commission. Domestic legal entities are required to collect their receivables from export sales of goods and services within 90 days of the day such exports take place. Within 48 hours of collection of the funds in the bank, the legal entities make an order for transfer to the beneficiaries. Realized foreign currencies may then: be either sold on the foreign exchange market to other legal entities or to authorized banks, or be used for own payments abroad and deposited in a foreign currency account with an authorized bank. Foreign

currencies realized through exports of goods and services may be held deposited with authorized banks up to 90 days from the date of collection.

Domestic legal entities may make payments in foreign currency (outflow) from these accounts, through all payment instruments, for the purpose of: payments for realized imports of goods and services, payments to consignment accounts opened with a bank in FYROM, payments to non-resident accounts opened with a bank in FYROM, withdrawals of foreign cash for business trips, cash payments in foreign currency subject to a special approval by the NBM and sale in the foreign exchange market for the denar currency equivalent. Domestic legal entities may make payments abroad only after goods have been imported or service provided, but not later than 180 days of the realization date. According to the Decision on effecting advance payments for imports of goods and services ("Official Gazette No.22/94), domestic entities may make advance payments only for purchases of equipment, intermediate goods, and spare parts for investment maintenance, as well as in repayment of foreign credits used for payment for imports of goods and services, documentary L/C payments and payments for consumer goods of vital importance for the supply.

For the services rendered in processing collections and payments, banks charge a commission, which varies depending on the payment instrument, the business policy and the bank fee schedule. Collection fees for bank transfers are around 0.226%, and for L/C collections around 1.582%. Payment fees for bank transfers are about 0.339%, for L/C payments around 0.678%, and for cash withdrawal the charges range from 1.13% to 0.5%. Fees are calculated in foreign currency at the transaction face value, and domestic entities pay them through their regular accounts, in the equivalent amount in denars, at the average exchange rate valid on the payment date.

b) foreign currency accounts for legal entities that perform investments or have consignment warehouses

Article 90 of the Law on Foreign Exchange Operations provides that authorized banks can open foreign currency accounts and allow collections in convertible foreign currency to domestic entities that perform investments abroad. The same is also allowed for domestic entities that have consignment warehouses with foreign goods in FYROM and for domestic entities that have foreign currency representing foreign investments. The manner of working with these types of foreign currency accounts is regulated in detail with the Guidelines of the NBM on the foreign exchange operations, no. 09-2/III of June 1994.

c) Also, subject to a special approval by the NBM, domestic legal entities may keep foreign currencies in accounts with foreign banks.

In order to regulate this matter, the National Bank of FYROM, on the basis of article 39 of the Law on Foreign Exchange Operations passed a Decision on the terms and approvals to enterprises and other legal entities to keep foreign currency deposits abroad ("Official Gazette No. 40/93). Approvals are granted on application of the legal entity, for a period of up to one year, for the following purposes: investment operations abroad, for the amount of non-transferable local currency in which payment has been collected on the basis of approval, for security deposit, for payment of operating expenses of a representative office or business unit abroad and for the expenses of legal entities which provide services in the international insurance or transport of goods and passengers.

Foreign currency accounts of foreign legal entities

Foreign legal entities can open the following types of accounts with banks in FYROM foreign currency account (non-resident) for foreign legal entities and foreign currency account (non-resident) for representative offices of foreign companies. These matters are regulated with the Decision on the terms under which funds may be received in deposit from physical and legal entities ("Official Gazette No. 40/93 and 28/94), Regulation on the specific requirements for the opening and operation of representative offices of foreign entities in FYROM ("Official Gazette No. 25/95), all of which have been passed on the basis of article 46 of the Law on Foreign Exchange Operations and article 37 of the Foreign Trade Law. It is particularly important to point out that funds of the foreign entity which are earned as profit, return on

investment in domestic entity, share in the net assets (if the funds were invested in a mixed company, in the case of dissolution of such company) or repatriation and other claims of the foreign entity are freely transferable abroad, after settling all outstanding obligations in FYROM.

a) non-resident foreign currency accounts of foreign legal entities

The opening of this type of account is relatively simpler. The documents that are required, in addition to the application from an authorized person, include a certificate of incorporation of the foreign company (not more than 3 months old) and information on the deposited signatures to the account. No deposits are required, nor is necessary to prove special commitment with the foreign entity with FYROM, and there are no account opening charges.

The collection of funds (inflow) in the accounts may be from: payments from abroad, payments from domestic legal entities, payments from another non-resident account, and in accordance with the decision of the NBM, cash payments in foreign currency. Payment of funds into the accounts may be made by: the owners of the accounts, other foreign entities and authorized banks on order of domestic entities paying for imports of goods and services.

Payments from the accounts (outflow) may be made for: transfers abroad, transfers to another non-resident account, payments to domestic legal entities, withdrawals of cash for use within the country, denars payments in the country. That is, foreign entities may use the funds in their accounts for denar payments in FYROM, for transfers abroad, as well as for foreign currency payments in FYROM and abroad, but also for cash withdrawals in foreign currency in accordance with regulations which are in force for the domestic entities. For the purpose of acquiring denar funds, banks purchase foreign exchange from non-resident foreign currency accounts. In effecting payments from these accounts, the authorized banks may convert funds from one to another convertible currency.

b) non-resident foreign currency accounts of representative offices of foreign entities

To open a foreign currency account with an authorized bank in FYROM, a representative office of a foreign company must submit an application, information on the authorized signatories whose signatures are deposited and a Notice of Registration in the Registry of representative offices of foreign entities in FYROM which is maintained with the Ministry of Foreign Affairs. The representative office does not have a status of a legal entity.

Payments into the accounts of representative offices may be made only by the foreign legal entity which opened the representative office or as a deposit of previously withdrawn unused cash foreign funds. On the other hand, payments from these accounts may be made only for the operating expenses of the representative office (salaries, cash expenses, purchase of equipment, withdrawal of cash foreign currency for business trips or for purchase of the foreign currency).

Transactions with the foreign currency accounts of foreign legal entities and foreign representative offices are effected through a written order of the authorized employees to the bank.

The bank charges for collection and payment processing services for foreign clients are essentially same as for domestic clients. They vary depending on the collection instrument, the banks business policy and the banks' fee schedules. For collection through bank transfers to a non-resident accounts of foreign legal entities banks do not charge commissions. On the other hand, for documentary collections they charge around 1.582%, for payments by bank transfer around 0,339% (with the exception of payments made by foreign diplomatic, consular and the International red Cross, which are not charged for), for L/C payments the bank charges are around 0.678%, and for cash withdrawal they range from 1.13% to 0.5%. Fees are calculated at the transaction face value, and they are collected from foreign currency accounts of the foreign entities.

5.11. Bankruptcy

The *Bankruptcy Law* was published in the "Official Gazette in 29.10.1997. It came into force on the eighth day following the publication date, and its practical implementation begins at the end of the period of six months beginning with the day on which it came into force.

This law regulates the aims and reasons for commencing a bankruptcy case, the case administration, management and use of property of the estate, reimbursement to creditors, plan of reorganization, personal management, discharge from other debts, special types of bankruptcy cases for individuals with a tradesman status, bankruptcy cases involving foreign elements and other issues connected with the case.

Reasons for commencement of a bankruptcy case:

- In the case of insolvency, a financial condition such that the debtor is unable to pay matured financial liabilities within 60 days of such liabilities becoming due
- In the case of impending insolvency, the debtor may file a voluntary petition for bankruptcy.
- In the case of over-indebtedness, a condition such that the entity's property cannot cover the existing debts, i.e. the sum of the entity's debts is greater than all of such entity's property.

Principles of case administration:

- A bankruptcy case is commenced by the filing of a petition for bankruptcy by a qualified person.
- Bankruptcy is an emergency proceeding
- The court officially verifies all the facts relevant to the case
- The court may make decisions without oral argument
- A bankruptcy case dismissal may only be requested in cases specifically provided by this law

Decisions:

The decisions in the bankruptcy case may only be made in the form of **judgment** and **decree**. An appeal may be filed against the judgment within 8 days, and such appeal cannot stay the execution of the judgment. A complaint may be filed against the decree within 3 days of serving notice or the announcement on the board of such decree, as the case may be and it is reviewed by the bankruptcy panel.

Other legal remedies

A motion to reopen a case or an appeal to review a case is not allowed. An appeal on questions of law is allowed (writ of certiorari).

Organs of the bankruptcy case

1. Bankruptcy panel - consists of three judges, one of which is the presiding officer. The bankruptcy judge cannot preside at the bankruptcy panel.

2. Bankruptcy judge - supervises the work of the trustee and gives binding instructions, monitors the work of the creditors' committee and the meeting of the creditors.

3. Trustee - a physical person may be appointed as trustee in a bankruptcy case if such person has professional qualification and a minimum of five years of work experience. A trustee cannot be appointed at the same time in more than one large and one medium company or more than two small companies. The trustee in a case is appointed with an order of the bankruptcy panel. The president of the court in which the case is administered, having obtained the opinion of the Ministry of Economy, determines a list of trustee candidates. This list is updated every year. At the first meeting of the creditors following the appointment of the trustee, the creditors may substitute the trustee appointed by the bankruptcy panel.

The bankruptcy panel may vacate the appointment of trustee elected at the meeting of the creditors, if it determines that the selected person fails to satisfy the requirements of the law. Every trustee is allowed to file a special complaint against such an order.

As soon as a trustee is appointed at the meeting of the creditors, the trustee appointed by the bankruptcy panel ceases to hold office.

The work of the trustee is supervised by the bankruptcy judge and the bankruptcy panel, and they may, at any time request information or a report on the bankruptcy case progress and on the condition and the administration of the estate.

If the trustee fails to perform the obligations stipulated by the law, following a court warning, may be fined with 10.000 to 300.000 denars.

The appointment of a trustee may be vacated officially by the bankruptcy panel, on motion of the bankruptcy judge, or the committee or meeting of the creditors or on the trustee's own motion.

Immediately after the acceptance of official duties the trustee must obtain a liability insurance cover. The bankruptcy judge determines the amount of the bond, having considered the size of the estate and the complexity of the case.

The trustee may be awarded compensation for services rendered, the amount of which is determined with a resolution of the bankruptcy panel at the closing of the case. The Government of the Republic of Macedonia shall determine the terms of reference for the compensation and the reimbursement of actual, necessary expenses allowable to trustees.

4. Creditors' committee - the meeting of the creditors decides whether or not to appoint a creditors' committee. The creditors' committee consists of representatives of the lien creditors (creditors having a lien right, redemption right or other right entered in public books - registry of ships/aircrafts, intellectual property etc.), the creditors having the largest claims and the creditors with small claims. Debtor's employees shall also be represented on the creditors' committee. Other disinterested persons may also be appointed in the creditors' committee, if their professional qualification can assist in the work of the committee.

Members of the creditors' committee shall comprise an odd number and that number is designated by the bankruptcy panel.

The meeting of the creditors may substitute members appointed by the trustee for other or additional members of the creditors' committee.

The creditors' committee shall supervise the work of the trustee and assist him in the administration of affairs, give prior permission for cash receipts and disbursements and control the available amount of cash. On request of the bankruptcy panel, the creditors' committee advises the panel regarding the continuance of business operations commenced by the debtor; as well as regarding the allowance of justified inventory deficits.

The creditors' committee decides regarding matters within its domain on a meeting. The first meeting is convened officially by the bankruptcy judge or by the trustee or by the majority of the members of the

committee. At the first meeting the committee elects a presiding officer. The bankruptcy judge and the trustee are allowed to attend the meetings of the creditors' committee.

The bankruptcy judges must attend the meetings of the creditors' committee, and the committee may decide that a meeting can be held without the trustee's presence.

A resolution of the creditors' committee is valid if such resolution is approved by the majority of the members present at the meeting and entitled to vote.

Member of the creditors' committee are entitled to compensation for their work and to a reimbursement of actual necessary expenses.

5. Meeting of the creditors - is called by the bankruptcy judge.

A creditor has a right to vote if a claim of such creditor is entered without contest by neither the trustee nor any of the creditors entitled to vote.

Creditors of lower classes of priority are not entitled to vote.

A bankruptcy case is commenced on petition by either the creditor or the debtor (petitioner).

On petition to open a bankruptcy case, the bankruptcy panel shall order a hearing to determine the reasons for opening a bankruptcy case, or it shall dismiss the petition with an order. A special complaint against such an order is not allowed

With the order for a hearing, the bankruptcy panel may determine assurance measures:

- appoint an interim trustee
- place a general ban on the use of property of the debtor or allow that the debtor can use the property subject to a prior approval by the bankruptcy judge or the interim trustee
- suspend or delay the order for collection or the enforcement of collection or redemption of property from a lien
- stop payments from the account of the debtor
- If the other measures are not sufficient, the bankruptcy panel may order a compulsory apprehension of the debtor.

After receiving the report of the bankruptcy judge, or the interim trustee, as the case may be, and the report of the professional person on the insolvency and over-indebtedness of the debtor, the bankruptcy panel sets a date for hearing on the reasons for commencing a bankruptcy case. Notice of process is served on the petitioner, the debtor, the interim trustee and the professional persons.

With the order for commencement of the case the bankruptcy panel shall set a hearing date for:

the meeting of all creditors, for the examination and verification of claims entered (**hearing on examination**), between the last date for the filing of claims (bar date) and the examination date there may be no fewer than 8 days and no more than 60 days

the meeting of the creditors having the largest claims, for a decision on the further course of the bankruptcy case, on basis of the trustee's report (**hearing on a trustee's report**), this hearing cannot be held before the meeting of all the creditors nor after a period of 15 days following the meeting of all the creditors

Both hearings may be combined and in that case first the claims are examined and then the meeting of the creditors having the largest claims is held.

On motion of a creditor or a liquidator, the bankruptcy panel may order the commencement of a bankruptcy case without hearing and examination of the reasons for commencing a case.

If during the hearing it is found that the property of the debtor that becomes property of the estate is insufficient to cover the filing fees or the sum is of inconsequential value, the bankruptcy panel shall open and close the bankruptcy case. In that case the bankruptcy case will not take place.

In such cases the bankruptcy panel by official duty and in compliance to the rules of the executory procedure shall dispose of the property of the debtor and use the proceeds to cover the expenses incurred in the bankruptcy case and shall credit any remaining funds to the Budget of the Republic of Macedonia.

Notice of commencement of a case is given to the debtor, the creditors, the bearer of the payment operations with whom the debtor has accounts, the public prosecutor and the organs maintaining registries, that is, public books.

Creditors - are the personal creditors of the debtor who, on the day of commencement of a bankruptcy case have a claim against the debtor. Creditors claims are designated in classes by priority. Creditors of a lower priority class may be paid only after the creditors of the higher priority class have been paid in full. Creditors of the same class are paid on a pro rata basis.

Unmatured claims become due as of the date of commencement of the bankruptcy case.

Where several debtors are liable to one creditor for the performance of the same obligation in entirety, such creditor may file a claim against each of the debtor seeking full recourse for the amount claimed at the commencement of the case.

Exempt creditors - for whom on basis of an real or personal right it can be proved that some asset does not belong to the estate, i.e. that person is not a creditor.

With the opening of the bankruptcy case the right of the debtor to manage and use the property that becomes property of the estate is conveyed to the trustee; the authorities over the property of the former representatives of the debtor become void after the opening of the case; if during the period of 30 days before the filing of a petition for bankruptcy the trustee acquires a lien or other right to the property of the debtor that becomes the property of the estate, such right terminates with the commencement of the case.

After the commencement of the case the trustee has the right to terminate the employment of persons employed, whether or not such employment has been assumed on a full-time or temporary basis. Termination of an employment contract is subject to a notice which must be provided in no less than 30 days and no more than three months.

The trustee may, subject to a prior written approval of the bankruptcy judge conclude agreements for continuation of commenced transactions and elimination of potential damages.

The salaries and compensations of employees are determined by the trustee, in compliance with applicable law and the collective agreement, subject to a prior written approval of the bankruptcy judge. Salaries and compensations are paid by the estate.

Bids which have been tendered by the debtor or received by the debtor, become void on the day of commencement of the case, unless such bids had been accepted by that date.

The commencement of the case operates as stay of contracts of the debtor concerning the property that becomes property of the estate become. If the contract party without any knowledge of the commencement

of the case continues to fulfill the obligations under such contract, it shall be deemed that the contract remains in force.

Any claims of the contract party with respect to such perfection of the contract are treated as creditor's claims.

In the event of repairing damages, the contract party is obliged to continue to perform activities of urgent nature after the commencement of the case until the trustee takes over the administration.

Claims of the contract party arising out of such arrangement are treated as creditor's claims.

Termination of contracts for lease of business or part of business

If the contract for lease of the business or part of the business stipulates benefits for the property that becomes the property of the estate, the trustee shall consult with representatives of employees of the business or part of the business regarding the reduction of such benefits. The lease contract is subject to three months termination notice, even if the contract allows a longer period for such notice. For cause, the lease contract may also be terminated without advance notice.

Social plan

If the plan filed during a bankruptcy case proposes economic, technical, structural and other similar reorganizations, the trustee is required to prepare a social plan for alleviating the negative consequences from the layoff of employees. In particular, such plan must elaborate the criteria and the conditions for termination of employment on notice, in compliance with the applicable provisions of the *Law on Employment Relations* and the collective agreements.

The court shall dismiss or confirm the proposed social plan, and the parties in interest have the right to file a complaint within 15 of the courts decision.

The social plan prepared after the commencement of the case must assure one of the rights under an employment contract and with respect to the right of severance pay, such severance may not amount to more than two monthly salaries. The liabilities arising out of the proposed social plan are deemed liabilities of the estate.

In the event that the employer had begun economic, technological, structural and similar reorganization before the commencement of the bankruptcy case and a social plan with respect to such reorganization has been prepared not earlier than three months before the filing of the petition for bankruptcy, such social plan may be revoked by the trustee or the representatives of the employees. Social plans prepared earlier than three months before the filing of the petition for bankruptcy cannot be revoked.

5.12. Competition

5.12.1. Overview of the general competition environment

On the eve of transformation to a market economy the country's industry was heavily specialized and concentrated. The market structure was dominated by single producers or a few producers of many industrial goods and their parts. In order to avoid widespread monopoly practices, after independence the Republic of Macedonia needed to adhere to broad foreign trade liberalization and to establish legal and institutional basis for protecting fair competition.

At present anti-monopoly legislation and fair competition protection are regulated by the Law on Trade (Official Gazette 23/1995). However, this law is a legacy of the past and is ill-suited to the market environment. Having that in mind, the new competition laws are already drafted (as a Law against restriction of competition and a Law against unfair competition. These regulations are expected to be adopted by the Parliament within the first half of 1998. With respect to unlawful competition and monopoly practices the new law should follow standard Western definition and procedures, natural monopolies are to be dealt with by imposing direct price fixing and/or advance price monitoring.

5.12.2. Market structure: the importance of legacies

Market concentration

The market concentration of country's economy can be assessed by the following data (Table 5.16):

Table 36. Distribution of enterprises by number of employees

Number of firms	Small (1-249)	Medium (251-999)	Large (1000-1999)	Extra large (2000 or more)	Total
1990	3.734	257	49	33	4.073
1991	8.482	349	64	32	8.927
1992	15.083	314	41	34	15.472
1993	16.237	247	29	25	16.538
1994	24.183	244	30	21	24.478
1995	29.386	219	27	18	29.650
<i>As a percentage of total (%)</i>					
1990	91.7%	6.3%	1.2%	0.8%	100.0%
1991	95.0%	3.9%	0.7%	0.4%	100.0%
1992	97.5%	2.0%	0.3%	0.2%	100.0%
1993	98.2%	1.5%	0.2%	0.2%	100.0%
1994	98.8%	1.0%	0.1%	0.1%	100.0%
1995	99.1%	0.7%	0.1%	0.1%	100.0%

Source: Statistical Bureau of FYROM : Annual Yearbooks.

The data presented in the above table show that the concentration of FYROM economy is not significant. However, being a small economy, there are several factories being the only producers of their industry in the country. It is visible that the number of enterprises has grown substantially and among them the number of small enterprises grew most. The number of all other enterprises (employing more than 250 employees) has decreased in the last years. The reason for this trend is the fact that the economy of FYROM went through a thorough restructuring within the past decade, meaning that most of the large enterprises were subject to downsizing, splitting businesses in their effort to gain competitiveness on the market and to adjust to the changes. On the other hand, a great number of new entrants on the market (mainly small ones) continued to appear on country's market. These trends, together with the liberalization and deregulation of the overall economy increased the level of competition in the country.

The inherited industrial structure

FYROM, similarly to other countries of former Yugoslavia, inherited an industrial structure with a small portion of small firms. It is also true that the total number of companies was also small and it was not changing over the years. Although there was a law on bankruptcy, it was difficult to implement, so that there was not much movement in the industry structure. The changes started happening after 1990, when the establishment of new, private enterprises was made possible.

Already in 1993, there were about 16.5 thousand enterprises, 16.2 thousand of them being ones (with less than 250 employees). The respective numbers in 1995 are 29.700 and 29.400 enterprises. The majority of SMEs are firms with approximately 50 employees in manufacturing and 20 employees in other activities, mostly found in the trade sector in the form of very small, typically family activities. SMEs outnumbered larger enterprises by a factor of fifty four-to-one in 1993 (16.237 to 301) and 111-to-one in 1995 (29.386 small to 264 larger enterprises).

Yet when expressed in terms of output, the picture looks different: in terms of output, large firms are still bigger producers than SMEs, indicating the very typical concentration of capital in larger enterprises. This is even more obvious in terms of fixed assets. They are mainly concentrated in the largest companies. Especially at the beginning of the reforms, the over-significance of the large firms meant that they were dominant in terms of technology, employment and market position. Once the changes started, the large companies started losing power and they started showing their rigidity to change. They had to restructure heavily.

Price controls

At the time of gaining independence the prices in FYROM were mainly formed freely on the market. Yet the prices of some products and services were under control and the level of control amounted to 25% of the retail price index. In the later years, the control was decreased to 18% in 1992, 15% in 1993, 15.5% in 1994 and 19.5% in the later years until now. Products which are under control are the following: one type of flour (T-500), bread made of that flour, some post and telephone services, some communal services and a part of the insurance of vehicles. The Government has plans to decrease the price control further in 1998. At the same time, the form of control over some prices changed. To stimulate production and guarantee the purchase of specific agricultural products, protective prices have been set up only for the corn and oriental tobacco.

5.13.3. The current legal framework for a competitive market

The competition policy in FYROM is defined by the Law on Trade (Official Gazette 23/1995). The Law on trade defines the wholesale and the retail industry, the conditions needed to perform this activity. The Law also contains measures against monopolistic position and monopolistic behavior on the market and against boundaries to free market and free enterprise system. This Law, however, is considered to have very modest provisions for the competition policy. New laws on anti-monopoly protection and on competition policy are the right now in the procedure of being enacted.

Protection against Monopolistic Behaviour

Monopolistic types of behavior, as defined by the existing Law can be the following: making monopoly agreements, abuse of the dominant position on the market, as well as actions for creation or use of the monopolistic power on the market. The monopoly agreement is defined as an agreement between two or more trading companies whose objective is to limit the free competition on the market and to create a favorable position for the companies making the contract. Such can be the contracts for division of the market, the contracts for limitation of the production, or the conditions of the production, or the conditions of production, the price agreement etc. A dominant position on the market has the producer whose products or services participate with more than 40% of the total market of the product or service in FYROM. Abusing this dominant position means trying to obtain a favorable position on the market not in accordance to the good business conduct.

The main measure that the Government can take against the monopolistic behavior is the limitation of prices, with the duration of no more than six months.

Protection against Restrictions of Free Market and Free Enterprise

The Law on Trade defines the activities directed towards restriction of free market and free enterprise system as those activities performed by the Government or by the municipalities by which some form of limitation of trade, limitation of access to the market or other form of obstruction of the competition is being achieved. These activities are the following: not allowing the enterprise to perform some business activity, although it fulfils the conditions as defined by the law; making the procedure for granting some license unjustifiably lengthy; discriminating enterprises on the basis of their location in the municipality; prohibition of trade outside of municipality.

As an exclusion, the Government can make a decision to restrict the free competition only in the case of defense of bigger disturbances of the market. These measures can be no longer than one year. If the Government measures prove to have provoked damage for the company, the Government is supposed to compensate for the damage.

Other forms of market and enterprise disturbance are the un-fair competition and the dumping prices.

The unfair competition is defined as an activity of a trading company which is not in accordance with the good business conduct and which can do harm to some other participant on the market. The major fields of unfair competition, as defined by the Law, are the following:

- advertising, with the aim of making confusion on the market and to create more favorable conditions for the company, selling products with marks and signs which can make confusion for the origin, producer, quality and other features of product,
- hiding away the failures of the product and confusing the customer about the product, announcing a misleading sale in order to make a confusion for the customer; unauthorization of some other trading company, if this is meant to produce confusion on the market,
- giving gifts or other favors to some trading company in order to receive a more favorable position on the market, unauthorized use of services of other company's representative,
- activities raising hope that the customers will obtain some product, service, or favor without having to pay for it if they are not happy enough,
- making artificial disturbances on the market and creation of deficiency of different products and tied (packaged) trade - selling some products only in combination with some others.

Apart from those, unfair competition is the activity when some company breaks some rules of trade, accounting, banking, employment, health, pension and disability insurance, taxes, prices, working time etc., thus creating more favorable position for its own. All the activities been taken not in accordance with the honest and sensible trade and business practices being harmful to other companies, persons, or customers may be also defined as unfair competition.

The Law provides for creation of a Commission for protection against monopolistic behavior and against different types of limitation of market and free enterprise within the Ministry of Economy, but such a Commission has not been formed. The initiative for assessment of some activity whether it can be treated as a monopolistic behavior, unfair competition or as some forma of disturbing the market can be placed by any individual, legal person, chamber of commerce, Government bodies, municipalities etc. Most of the measures that can be taken against the companies violating some provisions of the Law are penalties in money, plus prohibition for performing the activity for a certain period of time for the company.

A supervision over the implementation of the Law is done by the authorized inspections, being part of some of the Ministries - Ministry of Economy, Ministry of Health, Ministry of Finance, Ministry of Labor etc.

A legal protection against a monopolistic act or against an act of unfair competition can be achieved with a lawsuit. The procedure on such a case is considered to be urgent. The right to file suit becomes obsolete in one year after the prosecuting agent found about the act, but no more than three years after the act has been done.

5.12.4. New laws regulating competition policy

The new laws regulating competition policy are based, mainly on the German Cartel Act and German Act against Unfair Competition. These acts are in harmony with European principles and the articles 85 and 86 of the Treaty of Rome.

The law against restriction of competition

The main provisions of this (cartel) act are:

Prohibition of cartels: if competitors coordinate their market conduct and thus restrict competition, this is deemed to be a cartel; it may in particular take the form of an agreement on prices, quantities or regions. These cartels are prohibited in general, although certain types may be allowed, provided they meet the legal requirements. In particular they include cartels regulating general terms, rebate cartels, cartels for standardization, specialization or rationalization, as well as crisis and export cartels. Legally allowed cartels are subject to constant supervision. Concerted actions, having the same effect like cartels, even not being included in binding agreements, are also prohibited.

Prohibition of vertical restraints of competition: these restraints are inadmissible in principle. However, in exceptional cases, vertical agreements are allowed, for example the agreements on exclusive dealership. Also, for reasons of cultural policy, resale price maintenance is allowed for the products of publishing enterprises.

Control of abusive practices by market dominating enterprises: this control is a Government regulator designed to offset the absence of genuine competition. The strength of an enterprise on the market concerned is assessed in the light of the market structure (proceeding from the market share) and the enterprise's market conduct.

Prohibition of discrimination and hindrance: market dominating or powerful enterprises often possess ways and means of impeding or discriminating against other companies. The prohibition of hindrance is mainly intended to protect the competitors of the powerful enterprise, while the prohibition of discrimination is designed to protect buyers and suppliers against unjustified disadvantages in relation to their competitors.

Merger control: if a merger is likely to create or strengthen a market-dominating position, the Cartel authority must prohibit the merger. However, if the participating enterprises prove that the merger will also lead to improvements in the conditions of competition and that these improvements will outweigh the disadvantages of market domination, the merger has to be allowed. Also, the minister of economy will have authority to allow the merger in the cases where the restraint of competition is outweighed by advantages to the economy as a whole.

Exemptions: in certain economic sectors the Cartel Act applies only to a limited extent on account of technical, structural or other peculiarities. Such sectors include transport, agriculture, banking and utilities. These are, however, subject to supervision by the cartel authority and also to public supervision in some cases.

Powers of the Cartel authority: this office will be responsible for the implementation of The Law against restraints of competition and it lies in the area of responsibility of the Ministry of economy. For the purpose of enforcing cartel law, the Cartel office will be vested with far-reaching investigative powers. It may demand information from enterprises, inspect business documents and, pursuant to an order by a judge, search

enterprises and confiscate evidence. The Supreme court of FYROM is competent for the complaints of decisions of the Cartel authority or the Minister responsible for the economic issues.

The law against unfair competition

The enterprises must heed not only the provisions of the Cartel Act, but also those of the Law against unfair competition. This embodies from the classical liberal principle according to which the state should merely establish abstract laws as a framework for market activities.

The prohibitions contained in the Law against unfair competition meaning that everyone must comply with them. Where contraventions also affect the public interest, every person engaged in trade or business, certain associations having legal capacity and trade or commercial chambers may take legal action. If only individuals are directly impeded, they alone may take legal action.

5.13. Labor Regulations

5.13.1. Overview of the labor regime

The Law on Labor Regulations (Labor Law), adopted in 1992, provides the rights and obligations of the employers and the employees, and equal rights and status of the workers regardless of their place of work. The Law is in accordance with the Constitution of FYROM and ILO Conventions. Working relations in the defense, internal affairs and governmental institutions are subject to separate laws, where only the specific conditions are treated.

According to the legal regime in FYROM, rights and obligations can be stipulated only by the law, which means that the courts are the institutions where the law is carried out only. Customs and practices are not legal instrument in FYROM. By our assessment neither employers nor employees are privileged by the court.

5.13.2. Categories of labour contracts

Persons not younger than 15, or for hard labor conditions, not younger than 18, who fulfill the general conditions of the Law on Labor Regulations, can be employed in FYROM.

According the Law for Employment and Unemployment Insurance, adopted in 1997, an employer can employ a person by direct contracting, using the services of the Employment Bureau of FYROM, or other private agency authorized to provide such services.

Relations between employer and employee are regulated by an individual employment contract. Both country's citizens and foreign citizens are subject to country's law. The employment contract, which must be in writing and registered in the Employment office, should contain the following clauses:

- Duration of the contract (finite or not),
- Effective date and termination date,
- Qualifications and training,
- Description of the employee's duties,
- Hours of work,
- Salary and pay-day,

- Location of the working place,
- Kinds of protection of the working place,
- Rest periods and vacation periods.

All the conditions of the contract regarding the relations between the employer and the employee are matter of mutual agreement between the employer and the employee, in accordance with the existing Macedonian laws and Collective agreements.

According to the Law, there are two categories of employment contract, contract for an indefinite period and contract for a definite period. The only difference between these two categories of contracts is the duration of the contract.

Contract for Indefinite period is normal contract of employment and there are no legal or court restrictions on freedom to contract.

The termination of this type of contract occurs:

- by mutual agreement between the employer and the employee,
- if stipulated by the law,
- by dismissal,
- if there are employees to be laid off by economic reasons (technological, structural or under similar conditions).

Termination of the contract by mutual agreement is the act of good will between the employer and the employee.

The law proscribes the following cases as a basis for termination the contract:

- if the employee can not fulfill his working obligations due to the loss of his working ability,
- if according to decision by the court or other body the employee can not fulfill his duties and there is no possibility to be disposed to another job according to his qualifications,
- if the employee is absent more that 6 months due to the prison sentence in duration longer than 6 months or other penalty which requires more than 6 months absence,
- if the employee fulfils the pension conditions,
- if the legal entity is under bankruptcy procedure,
- for the foreigners if the permit for stay in the country is cancelled, expired, or revoked.

Contracts for a Definite Period and Related Contracts

The other category of Labor Contracts, according the Labor Law, are the Contracts for a definite period of time. This category of contracts are signed in cases when the employer has to maintain the uninterrupted performance of the certain tasks, and there is no real opportunity to have contracts for an indefinite time signed. This category of contracts are signed for: season works, enlarged volume of work, replacement of an absent employee, work on a specific project.

The duration of season works is limited in time, determined by certain weather conditions, so the duration of the contract is usually for a particular season in the year (spring, summer, autumn), but no longer than nine months.

When the regular tasks are, from certain reasons, so much enlarged so they can not be accomplished by the regular employees, the employer may contract additional personnel for that purposes, for a definite period of time that is no longer than six months in a calendar year.

The employees that are absent for a longer period of time from different reasons (military service, health reasons, maternity leave etc.), may be replaced with other employees on the contract basis for the duration of the absence. The duration of the contract for a definite period of time for a specific project is connected with the duration of the project.

The procedure for employment for a definite period of time is the same as the one for the employment for an indefinite period, only that the employee must be informed about the duration of the contract and the period must be stated in the contract with precise dates.

The conditions for the termination of this category of contracts are the same as the ones for the contract for an indefinite period, plus when the circumstances that have brought to these employment no longer exist, e.g.: (a) tasks are accomplished, (b) the duration of the contract has expired, (c) the absent employee has come back to work, (d) the project has ended. With the expiration of these contracts, the employer must inform the employee about this in writing.

The contracts for a definite period of time can not be transformed in the ones for an indefinite period. If the employer wishes to do so, he must undergo the same procedure as for employment for an indefinite period of time. The employees under these contracts have the same rights and obligations as the ones on the indefinite period of time. If the employees for season works, work for more than 40 hours a working week, that period is considered as full time job.

5.13.3. Wage Determination

According the Constitution of FYROM every employee has a right on adequate earning. This constitutional right is rendered into the Labor Law as the employee's right on wage. This right of the employee, according to the General Collective Agreement (CGA) of FYROM, is redefined as an obligation and a duty of the employer to pay wages to the employees for the work done. The wage of the employee is determined within the Employment Contract, which means that it can not be a matter of good will of the employer.

Wage earning is according the following criteria: (a) proportionally to the work done and (b) according to the participation in the profit made.

The conditions for the second criteria are stipulated in the Branch and Employer Collective Agreements (BCA and ECA). According to the GCA, there is a possibility of 0.5% increase of the wage for every year of employment up to a total of 20% for each employee. However this is to be determined with the BCA and ECA.

The wages of the management staff and personnel with special responsibilities are determined by the one who has nominated them.

The basic wage is the lowest one for the certain level of complexity of the job. There are nine levels of complexity of the job, beginning with the simple routine job not requiring some special education, and the ninth level for very complex jobs requiring initiative, creativity and special education. The ratio between them is 1:3. This ratio can be higher if so agreed within the BCA and ECA. The basic wage can be increased for jobs in hard conditions. The increase and conditions for such cases are determined within BCA and ECA.

The basic wage is paid for full time job and normal production and can be increased for higher results than normal. The expected results from the working process are proscribed by the employer, written in a document, and introduced to the employees. These are in accordance with the BCA and ECA. If many of the employees do not fulfill these proscribed results, the Union can raise the issue of their reconsideration, and the Union must do that if this is the matter with most of the employees. The criteria of the evaluation of the results are also proscribed by the employer in accordance with BCA.

The lowest wage is determined by the GCA, it varies in connection with the change of the living expenses, and it is proscribed monthly. In the case of certain difficulties in the working, the employer must make a program for their overcoming, and if that program is accepted by the Union, he can pay lower wages than the proscribed lowest one. The decrease can be up to 20% and only up to 6 months. If these difficulties are objective ones and they are the same for the whole branch this decrease can be higher, but only as a prevention of a bankruptcy. At the end of the year, if there are financial possibilities, the employer can pay the employees the difference between the real paid and the lowest wage. The wage is increased for working on nonworking holidays, night work and for work over 40 hours a week. The increase is determined with the GCA.

The wages can be calculated in denars or foreign currency, but they are paid in denars, at least once a month for the previous month. That leaves the opportunity of payment on ten, fifteen days, or weekly. Together with payment of the wages, the employer must pay the taxes and contributions for the employees. According to the Financial Law from July 1997, the employer must pay the contributions first till the 25th day in the month for the previous month. In FYROM the employees are paid the net wage. The gross wage include the taxes and contributions. he wage compensation is paid to the employees for the period of summer vacation, nonworking holiday, maternity leave, and for the period of qualification or study for the needs of the employer. The amount of the compensation depends on the case, and is determined with the GCA. According to the GCA, the employer will pay not less than 70% of the basic wage to the employees which are by his decision, on temporary vacation due to the production problems. All enterprises in the "economic sector" are obligated by law to make contributions based on payroll to support the national and local Economic Chambers, which automatically entitle them to membership and associated benefits.

**Table 37. Employment, Unemployment and net average of wages in FYROM,
(Annual percentage change)**

	1992	1993	1994	1995	1996	1997	1998	1999
Employment , total	-1.8	-5.6	-6.0	-9.9	-2.1	-4.7	5.4	1.0
Economic sector	-5.4	-6.8	-7.7	-12.5	-3.1	-6.1	6.2	1.2
Of which in industry	-6.5	-5.1	-5.9	-13.4	-4.0	-9.7	8.3	-0.7
Non - economic sector	-2.0	-0.6	0.6	-0.1	0.9	1.4	1.2	0.0
Of which: state administration	-8.1	-0.6	2.0	-1.0	0.6	0.6	8.3	6.0
Unemployment rate	N/A	N/A	N/A	N/A	31.9	36.0	34.5	32.4
Nominal net average wage, total	N/A	495.6	105.0	10.7	2.8	2.8	3.7	2.9
Economic sector	N/A	478.9	110.3	12.3	3.2	3.7	4.5	3.6
of which industry	N/A	454.0	105.8	11.1	3.6	2.3	3.1	1.5
Non-economic sector	N/A	535.3	85.6	4.0	0.8	0.3	1.6	1.4
Of which state administration	N/A	520.2	87.1	3.0	1.4	2.3	1.3	2.8
Real net average wage, total	N/A	28.7	-10.2	-4.4	0.4	0.2	3.8	3.6

Source: IMF, country report, June 2000, page 11.

Labor Market

According to the IMF country, in June 2000, the decline in employment that accompanied the recession in the first half of the 1990's bottomed out the end- 1997. Employment increased by 5.4% in 1998 and a further 1% in 1999, reflecting, albeit with a one-year delay, the pickup in overall.

Employment growth in the economic sector (6.2% in 1998 and 1.2% in 1999) was more buoyant than in the non-economic sector, as it benefited from relatively higher rates of growth during the period. Unlike in the past, small private firms (i.e., firms founded with private capital) were the main source of the increase in employment, with their share in total employment increasing from 43% in 1996 to 49% in 1999. Employment in the non economic sector has increased gradually and steadily since 1996, spurred by an expansion in public administration (of 8.3% in 1998 and a further 6% in 1999. This increase occurred despite the hiring restriction implicit in the freeze on the budgeted wage bill in both 1998 and it more than offset the shedding of labor in education and health sectors.

Wages

Nominal net wages continued to grow during 1998-1999, averaging over 3% a year. As a result real wages grew by close to 7% during the two-year period ending 1999. Wage growth in the economic sector substantially outpaced that in the non economic sector, owing mostly to the restrained wage stance followed by the authorities in the latter over the past several years. As a result, the wage differential between the two sectors was virtually eliminated by end 1999. Within the economic sector financial services, catering and tourism, and trade led the wage growth , averaging over 7% in 1999, twice growth rates registered in other economic sectors. Wage growth in the non - economic sector remained about half that of the economic sector, with wages in public administration leading growth, averaging an estimated 2% a year during 1998-1999.

Unemployment in FYROM

The unemployment rate in FYROM is extremely high, at 32.4% in 1999. Unlike most other transition economies, the high unemployment is not the outcome of reform-related lay offs. Rather, the unemployment has been historically high, hovering around 30% in the past decade, mainly reflecting anemic economic growth and rigidities in the labor market. While the structure reforms undertaken in the context of the Special Restructuring Program in 1995-1996 may have contributed to the worsening of the unemployment situation, it did not fundamentally alter the nature of the underlying problem. The pickup in economic growth in the past years has had a positive impact on the unemployment dynamics, with the new qualified entrants into the labor market being able to secure jobs with relative ease with the unemployment rate declining.

Several features of the unemployment in FYROM suggest that unemployment is essentially structural and that it is a problem of entry into the labor market, rather than of lay-offs. These features are:

- The concentration of unemployment among the entrants into the labor market, the young, and the less educated/low skilled,
- its long duration,
- the low rates of inflow into and outflow from unemployment and
- the low share of unemployment due to layoffs.

Causes of Unemployment

There are two main underlying causes of unemployment in FYROM: anemic economic growth and labor market rigidities, including high labor costs. Over the pasts 10 years economic growth averaged about 2%, with positive growth rates experienced only in the past two years. Industry the main source of employment in

the economy, has declined at an average annual rate of 6% during this period. This tepid economic performance has both directly constrained the economy's ability to create jobs and has made the rigidities in the labor market a constraining factor for faster employment growth.

Rigidities in the labor market, which inhibit hiring and job creation, have resulted from (a) high costs of dismissal and (b) high labor costs.

The labor legislation makes it very difficult and costly to dismiss workers. For example, employers must exhaust all available opportunities to keep the worker prior to dismissal, including redeploying him to other parts of the firm, reducing overtime for other workers, limiting new hires, providing vocational training and paying a generous lump sum in severance in case of firing. In case of group layoffs, employers are required to provide as in severance in case of firing. In case of group layoffs, employers are required to provide as much as three months advance notice to workers. The high dismissal costs embedded in the labor code have discouraged employers from hiring new workers for fear of being unable to downsize the labor force during economic downturns.

Hiring is also directly inhibited by high labor costs imposed by the wage legislation and the fiscal code. - These are a result of (1) high payroll taxes, (2) high non-wage benefits and (3) mandatory wage floors for tax assessment.

1. Payroll taxes currently constitutes about 75% of the employee's net earning. The high level of taxation has both discouraged new hiring and has led to the widespread practice of employing workers without registering them officially as employed as a way of avoiding payment of taxes and contribution. This practice, in turn, accounts for the large discrepancies between official employment/unemployment data and those obtained from the LFS.
2. High non-wage benefits are mandated by national and branch-level collective agreements and are mandatory for all enterprises that are less than 70% private. The main non-wage benefits are food allowances (about 25% of the average monthly wage), transportation allowances, and allowances (equivalent to one average monthly salary).
3. While there is no institutional minimum in FYROM, the wages imposes a mandatory (65% of the average wage in the branch) for assessing taxes and contributions. Thus, tax burden on enterprises with average wages that fall below this floor is particularly high. This puts at a disadvantage small and medium-size private enterprises, the backbone of job creation in the country, and also inhibits the hiring of the young or uneducated to the extent that the productivity of these groups of workers is below that justified by the wage floor, which also accounts for the high incidence of unemployment among the young and less educated.

To alleviate the unemployment problem there is a well-developed social safety net. Unemployed persons who have been laid off are entitled to receive unemployment benefits which are quite generous in relation to the other countries in the region.

Recent Labor Markets Measures

The authorities have undertaken several measures over the past few years to mitigate the severe restrictions on firing imposed by the labor legislation and to make the labor market more flexible.

The Law on Labor Relations (LLR) a major component of the labor code, was originally adopted in 1993, but underwent two rounds of important amendments in 1997-1998 as part of World Bank social sector programs. These amendments aimed to easing labor market restrictions, in particular restrictions on firing and hiring as well as the high costs of terminating labor. More recently, new amendments to the LLR was adopted end March – 2000 that further reduced labor market rigidities by decentralizing wage bargaining and lowering dismissal costs.

The Law on Employment and Insurance in case of Unemployment, the second major component of the labor code, was adopted in 1997, also in the framework of the World Bank's program, with the view of increasing labor market flexibility by reducing the amount and the duration of the unemployment benefits. The law also aimed at directly encouraging employment by exempting firms from payroll taxes on new hires for a period of three years and providing wages subsidies to employers who hire an unemployment person. Subsequently, a new set of amendments was adopted at end March, 2000 that restricted eligibility for open-ended unemployment benefits.

Table 38. FYROM: Age, Education and Gender Structure of the Unemployment rate (1996-1999)

	1996	1997	1998	1999
Age structure of Unemployment	Unemployment rate (%)			
15-24	69.5	74.2	70.9	62.9
25-29	48.2	53.8	51.8	51.2
30-39	28.0	32.0	30.7	31.3
40-49	15.3	19.1	18.0	17.0
50-59	16.1	13.1	16.5	17.0
60-64	10.1	7.7	8.1	8.8
65-80	3.0	6.6	1.5	5.0
Education Structure of Unemployment	Unemployment rate (%)			
Without Education	41.7	40.2	35.6	34.0
Incomplete education	30.9	29.0	31.0	27.3
Primary education	40.6	46.7	44.7	40.3
3 years of secondary	34.0	38.8	37.8	36.9
4 years of secondary	28.9	33.0	32.2	31.9
Higher education	16.2	20.2	17.8	18.5
University and higher	14.5	18.9	16.2	15.0
Gender Structure of Unemployment	Unemployment rate (%)			
Males	29.1	33.0	32.5	31.9
Females	36.2	40.8	37.6	33.3

Source: IMF, country report, June 2000, page 83.

5.13.4. Working Time

Working time is the period when the employee is at his place of work at the disposal of employer. Normal working hours per Working day of an employee are eight hours, respectively 40 hours per working week, or five days in a week (full working hours), in accordance with the provisions of the Labor Law. The employer may also introduce working hours less than 40 hours per week (reduced working hours). This may be done when the work is organized in shifts. Such working time may not be less than 32 hours for employee working in shifts, and his working time is equal to full working time. Therefore the rights of employees working with reduced working hours are equal to those working with full working hours.

The working hours of an employee exposed to exceptionally difficult, strenuous and detrimental job with harmful effect on his health, i.e. working capability that cannot be fully eliminated through protective measures, will be reduced in proportion to the harmful effect to his health or working capability. The working time may be reduced 10 hours the most, i.e. it may not be less than 30 hours per week. Also, an employee with reduced working ability who is not able to work with full working time at his working place or at other relevant job, is entitled to work at his working place or other job with working hours corresponding to his reduced ability, but not less than half of the working time. In such case of reduced working hours, the employer has to adopt a decision for shorter working hours, upon prior written approval issued by the Ministry of Labor and Social Policy, based on an opinion previously provided by the Organization for Labor Medicine and Labor Inspection. The employers' and the Ministry's decision must be in accordance with the BCA, respectively ECA.

According to the Labor Law, the General Collective Agreement for the Economy of FYROM and the General Collective Agreement for Public Services, the employee may also have shorter working hours than those considered as full time. This shorter working time may be from one to eight hours per week. The employer will introduce such shorter working hours in cases when: 1) the scope of the daily work is smaller and does not require full working time, and 2) some tasks are to be performed or when the nature of the work so requires. Such employee is entitled to all rights and obligations deriving from labor relations, depending on the length of work and labor results.

Working time exceeding 40 hours

The working time may exceed 40 hours per working week only temporarily and in exceptional cases, under certain conditions. But it may not surpass 10 hours week. This may occur in case of force major; assistance to other employer affected or threaten by force major; completion of a process which, if not completed might cause significant material damage, or would present a threat to people's life and health, to prevent squandering of raw material, or to elimination of defect, to replace unexpected absence of an employee in a continuous process, to begin or completion urgent medical (human or veterinary) intervention or other pressing health measure, and to complete urgent and pressing activities in the process that may not be delayed. In case the employee fails to proceed according to the employers' decision, he may be dismissed. Some categories of employees falling under special protection are excluded from such obligations, such as: pregnant women or women with a child less than 2 years of age; single parent with a child less than 7 years, or a parent with handicapped child without his prior consent.

The employee working longer than 40 in a week is entitled to 35% per hour increase on his base salary as set forth in the Collective Agreement.

Annual leave and Public Holidays

According to the Labor Law, the employee is entitled to paid annual leave during the course of one calendar year of a minimum 18 to a maximum 26 working days. The right to 18 working days in a calendar year is exercised after completion of one year at work. In cases when the employee has less than one year working age, he is entitled to reduced annual leave, two working days for each months at work but not exceeding 18 working days. This is in accordance with the ILO Convention 132. The annual leave is increased from 18 up to 26 working days on the basis of the working conditions (work in an office, factory, building site or outdoors etc.), the length working experience (for each year of working experience or group of years of working experience), the complexity of working duties (secondary, college and university education) and the employee' state of health (degree of reduced health condition).

The BCA and the Labor Law provide for longer annual leave for employees working under specific conditions, however such annual leave may not exceed 36 working days.

As by rule the annual leave is used during the calendar year, but may also be used in two portion (in accordance with ILO Convention 122), provided that three conditions are met: (1) the first part be minimum 12 working days during a calendar year without interruption, (2) the second, remaining part, to be fully used without interruption, (3) the second part must be used by June 3th the following year the latest.

Public holidays may be of different types, respectively state holidays (events of historical importance for the state, nation or different nationalities) class holidays (important for the working class of a given state); religious holidays (important for members of different religion); international holidays, etc. The employees shall not work on holidays if so stipulated by the Law. If such holiday falls of Sunday the employee shall not work on the following day too. But in case some of the employees in certain businesses do work he is entitled to receive increased wage.

Holidays in FYROM, which according to the Law on State Holidays are considered as non-working days are:

- New Year - January 1 and 2,

- International labor day - May 1 and 2,
- Ilinden - August 2,
- Independence day - September 8,
- October 11.

Scheduling of Working Time during the day, week or year

The scheduling of the working time, within the framework of the annual working hour, is determined by the employer in the employee's working contract, in compliance with the collective agreement and the Labour Law. The daily working time may be scheduled into seven or eight hours depending on the working days during the week (five or six days). The scheduling of the working time during the months and during the year should be made within the total annual working time, provided that it does not exceed the sum of the annual working time. It may be single as for example five days in a week, eight hours daily starting from seven a.m. to three p.m.; in two shifts so that the employee will work four hours in the morning and four hours in the afternoon etc. The scheduling of the working time in shifts should be made so, to provide relevant daily and weekly rest between shifts. The scheduling of working time in the field of traffic and communications, sales of retail goods, health, social and child care, pre-school education, education and other public services, public utilities, catering, tourism, craftsmanship, etc. is defined by Law. For example the working time for trade of retail goods is defined by the Ministry of Economy in accordance with the Trade Law, in health care, the Ministry of Health in accordance with the Law and the enactment of the Ministry etc.

The working time may be rescheduled for the purpose of the efficiency in using the capital and the labor force in such a way that during a given period of the year the working time will be longer, and in the other period shorter. The total fund of the working time in average may not exceed the full working time of 40 hours per week during the year.

Rescheduling of the working time may be made only in certain activities and certain cases, depending on the work, respectively technology, seasonal character of the business and caused by force major. The working time may be scheduled to be longer than 40 hours in a week, in the course of the several months of the year. In the remaining parts of the year it will be shorter, provided that the total working time in the year may not exceed the sum of the annual working time.

5.13.5. Flexibility of Employment

Termination of Employment at the Initiative of the Employer

The employer can terminate the contract by written notice only in two cases:

- if the employee is not capable of fulfilling the working duties proscribed by the law, collective agreement and employment contract, and
- if the employee has broken the working discipline and working regulations.

The working duties and obligations are proscribed by the law, collective agreement and employment contract. If established by an authorized person or a competent body, that an employee is not capable of fulfilling these duties, the employee can be disposed to a working place according to his/hers capabilities. If the employee does not accept the new disposition, the employment will be terminated.

The working discipline and the working regulations are proscribed by the employer according to the law and in connection with the collective agreement and employment contract. With the signing of the employment contract, the employee has accepted these regulations as one of the conditions of the contract. The matter of

the working discipline is the matter of agreement between the employer and the Union during the collective bargaining. Not obeying this regulations leads to dismissal of the employee.

Employee can not be dismissed for:

- membership in the Union, or Union activities that are according to the law and collective agreements,
- submission of claim, or taking part in the process against the employer in relation to employers not obeying law or other regulations,
- absence from work during maternity leave,
- absence from work for approved sick leave,
- absence for summer vacation, or other approved vacation,
- absence for the military service,
- absence for the education or professional improvement for the needs of the employer, and
- other cases regulated by the law (working in other countries on the grounds of scientific or technical help, working in the diplomatic service, governmental or public service etc.).

The question of the working discipline is not only the question of obeying simple rules like working time, vacation period, justified absence for different reasons but also the employee's attitude towards the working duties, assets, business secret, and even loyalty to the firm. All of these matters are regulated on different levels, starting from the Labor Law through collective agreements, ending with the employment contract, as a document with the most concrete regulations according to the specific firm and employee's position.

In the case of not obeying or breaking of these regulations, the employer is obliged to give a written notice to the employee for 30 days period for correction. After this period, if there is no correction, the employee can be dismissed. The dismissal can be replaced with the financial penalty by the employer. The penalty can be up to 15% of the wage for 6 months at most.

The termination is always by a written notice. There can be a period of notice, or a dismissal can be immediate. According to the Labor Law, the length of the period of notice can not be shorter than 30 days and no longer than 3 months, and according to the GCA this period can be up to 6 months depending on the period of working age.

For the period of notice the employee has all the rights and obligations from the working relation, plus a right to use 4 days in a month for search of a new employment.

In the cases of:

- unjustified absence from work for three days in a year successively, or five days in a year,
- misuse of sick leave,
- not obeying the rules for: work protection, protection from fire, explosives, poisons, other dangerous materials and environment protection,
- use of alcohol and narcotics,
- stealing from or connected with work,

- misuse of a given authorization,
- betrayal of business, official or state secret
- the dismissal is without a period of notice.

There can be other cases for this, if so determined in the BCA or some other law (military service, police service etc.).

Even though dismissal without notice is a shorter procedure, there is a certain period of time while it is accomplished. The employee can be suspended from his working place or from the firm for that period of time. The decision for the suspension must be in written form issued by authorized person (director, manager etc.).

The employee may complain against the decision for dismissal without period of notice. The complaint can not suspend the decision for termination.

For all the above cases the reason for dismissal is connected with the personal behavior of the employee. In the case of lay-off due to economic, technological or restructuring changes, the reason is connected with the needs of the employer.

According to the Labor Law the employer can initiate the lay-off of a certain number of employees if: (a) the employer has no need of certain number of employees due to economic, technological, structural or similar changes, and (b) the employer intends to introduce major changes in the production, program, reorganization, structure etc. which will result with downsizing of the number of employees.

The procedure in this case has five steps. In the first step the employer has to prepare a full study or program taking into consideration all the possibilities to decrease the number of laid-off employees. The employer should think of replacement, retraining, additional training of the employees, shortening the overtime work, shortening the regular working hours and similar measures. All of these measures should be presented in the program with strict schedule and timetable.

In the second step the employer must inform the employees and the Union. In this information the employer must present:

- the kind of changes to be undertaken,
- what are the consequences of the change of the number of the employees,
- the number and the structure of the laid-off employees,
- the measures undertaken by the employer to mitigate the consequences of the changes, and
- the rights of the laid-off employees that will be provided by the employer.

The number and the structure of the laid-off employees is established according to the criteria set up in the Labor Law and GCA. The criteria, according to the Labor Law include:

- the need of work effectiveness of the employer,
- the skills and qualification,
- working experience,
- successfulness at work,

- the kind and importance of the working position,
- working age,
- age, and
- other criteria set up in the GCA.

The other criteria set up in the GCA are:

- health condition, and
- social and economic condition of the employee.

In the case when two or more employees are in the same position the priority to keep the place will have:

- pregnant woman, or mother with child not older than two years,
- self-supporting parent with child not older than seven years,
- parent with handicapped child,
- disabled, or employees with professional disease,
- the husband or the wife, if they work for the same employer,
- Union representative,
- employee who has less than five years to the retirement.

In the next, third step, the employer brings the decision and informs the employees individually. At the same time the employer is obliged to inform the Employment Bureau about its decision, also. If the number of employees to be laid-off is less than 150, or less than 5% of the total number of employees, the employer must inform them one month in advance, and if that number is more than 150, or more than 5% of the total number of employees, the term is three months before the termination of the working relation.

- The fourth step in this procedure is the delivery of the decisions for termination of the employment. The employer can issue such decisions, only if he had fulfilled one of these three conditions:
- if the employer has provided the employees a new direct employment according to their skills and education,
- if the employer has provided the employees pre-qualification, additional qualification etc. for his needs or for another employer, and
- if the employer has paid the laid-off employees a severance pay in the amount of a monthly wage for every two years of the working age but not more than twelve monthly wages in total.
- If the employee refuses to accept one of these solutions, he/she can be considered dismissed, because the employer has fulfilled his/hers obligations.

The last, fifth step is the realization of the lay-off. When the employee has accepted one of the three above mentioned solutions the employment is considered as terminated.

The procedure of termination of the employment depends on the case.

- If it is by mutual agreement between the employee and the employer it is terminated with the written agreement.
- If the termination is due to expiring of the employment period there is no special procedure.
- If the termination is according to some legal provision, the employee gets the written notice once it is determined that he/she has fulfilled the required provision.

The termination of the employment due to economical, technological or structure changes, it is according to the above mentioned legal procedure.

In all these cases, the employee may first appeal to the employer, and if not satisfied with the response, the employee can ask for protection of his/hers rights through a regular administrative or court procedure.

In the case of dismissal with notice, if the notice is given by the employee, by his/hers free will, the employer have to accept it with the possibility to demand for fulfillment of the employee's obligations during the notice period.

In the case of dismissal with notice from the employer, the things are more complicated, and the procedure has several phases.

First of all the employer has to establish the fact that the employee is not capable of fulfilling the working duties proscribed by the law, collective agreement and employment contract, or the employee has been breaking the working discipline. The reason for dismissal must be justified by the employer, managing body or authorized person in written report with all relevant details and facts about the case e.g.: time and place of the "incident", protagonist(s), conditions, circumstances, evidence etc. In this case the employer is obliged to require explanation from the employee for the quotations in the report.

The second phase is issuing of the legal document for dismissal in a written form. The employer is not obliged to explain the decision for dismissal, if that is not required by the employee. The decision is issued by the employer or the managing body. For the employees with the working age over 25 years, or at least 20 years working age for the same employer the decision is issued by the managing body.

The third phase is the execution of the decision. Taking into account the seriousness of such decision, the employee is given the right to appeal. The written appeal is submitted to the employer or the managing body, within the period of 8 days after the reception of the dismissal decision. The employer must decide upon the submitted appeal within the next 15 days. If the employee does not receive any decision upon the appeal, or is not satisfied with the decision, the employee can ask for the court protection to his/hers rights.

The appeal to the dismissal decision does not suspend the execution of the decision.

The fourth phase is alternative, and is actually out of the dismissal procedure. It is the case when the court will cancel the dismissal decision. In that case the employer is obliged to employ the dismissed employee on the working position in accordance to his qualification, and to provide the employee all other rights from the working relations.

5.13.6. Employee Representation at Work Place

According to the Labor Law, in order to protect their economic and social rights deriving from the working relation, employees may establish or join Union organization. The employees may freely establish Unions, with no previous approval required. The employees are free to decide weather to join the Union or not. The only legal Union activities of the employees are those undertaken through organized Union that has its statute, rules and program. The internal organization of the Union, rights of the members, their activities, Union management, election of the Union representatives etc., are set forth in the statute of the Union. The Union representatives must be elected through free elections. The Union representative is elected by the

Unions, members of the Unions or the employees within an enterprise, registered in the Union register. The Unions are registered in the Union register at the Ministry of Labor and Social Policy.

The employer is obliged to provide conditions for regular Union activities. On the other hand, the Union representative must exercise the activities in a way not to interrupt the working process. In order to fulfill their Union activities, the Union representatives may be released from their working duties for few hours a month. They may also be released from their working duties for their training. All this matters are agreed within the BCA and ECA.

The employer is obliged to inform, in writing, the Unions and the employees about all the matters related to the economic and social status of the employees, regularly, as well as for all the matters that may affect the rights of the employees. The Union may ask, and the employer is obliged to provide the additional information about all the matters that affect directly the economic and social position and the rights of the employees. The employer is also obliged to take into consideration the opinions and suggestions of the Union on these matters. The employer has the obligation to invite the Union representative to the meetings where the employee's rights are discussed. In case when more Unions are organized within one enterprise, the employer is obliged to provide working conditions only of the majority Union.

The Union representative enjoys special protection, and is not liable for his Union activities that are in accordance with the Law and Collective Agreement. This special protection includes:

- his employment can not be terminated as a result of Union activities or Union membership after the working hours, and during the working hours if agreed with the employer,
- in case of termination of his employment, the decision for termination must include the reason for the termination,
- there must be obtained opinion by the Union, before the decision for termination is adopted,
- the procedure upon appeal by the Union representative is urgent,
- prohibition for change on worse the working conditions of the Union member,
- in case of redundancy due to economic, technological or restructuring changes, the Union representative has the priority to keep his job.

According to the GCA the measures of special protection for the Union representative are valid for a period of two years after the expiration of his Union mandate.

According to the Commercial Law, if so proscribed in the statute of the company, the employees in the companies with more than 300 employees and with one level management, can elect up to $\frac{1}{4}$ of the no executive directors in the board of directors.

If the company has two level management, than the above mentioned stipulation refers to the election of the members of the supervisory board. If the majority of the employees do not want to elect member(s) in the supervisory board they can do so. In the case of two level management, anyhow, the supervisory board is obliged to nominate one member in the board of directors who will be in charge of all matters related with employees and their relations.

5.13.7.Labor Conflicts

Settlement of Disputes over rights and duties

Rights deriving from working relationship established by the Constitution Law and Collective Agreements are inalienable and cannot be restricted neither by law, enactment or by the employer. In the case when the

employee is deprived or limited in his rights by any act or by the employer he may initiate one of the protection mechanisms set forth in the Constitution, the Labor Law, the Company Law, the Law on Labor Inspection, the Law on protection at work, the Employment Law, the Law on Health Care, the Law on Pension and Disability Insurance, the Law on Courts. Therefore he may request protection at the employer; the competent court, the Constitutional Court; the Trade Union, Inspection bodies or other bodies.

The employee desiring to exercise some of his rights or not being satisfied by the employer's decision regarding his rights, obligations or responsibilities is entitled to submit a **request** for exercising his right deriving from labor relations or **complaint** against a decision adopted regarding his rights, obligations or responsibilities. Such request or complaint is submitted to the body as set forth in the Collective Agreement within 15 days from the day the decision violating his right is received, respectively the day when he found that his right is violated.

The request, respectively complaint is submitted to the employer, respectively the managing board, member of the managing board or other body. The decision for which a request, respectively the complaint is submitted shall not be exercised until the final decision is adopted by the employer, except in cases such as a decision for suspension. The employer will decide on the body, respectively responsible person, who is to decide about the rights of the employee. During the entire procedure the employee has the right to attend the session and be represented by the Trade Union. In case the employer fails to adopt a decision within 15 days, or the employee is not satisfied with such a decision, the employee is entitled to request protection at the relevant court. But, it should be noted that the employee may not request protection of his right at the relevant court unless he failed to request such protection at his employer first, except in case of his right for remuneration. The relevant court, i.e. the regular court is the one that decides upon the complaint of an employee who is not satisfied with the first instance decision, in a procedure for protection of the rights of the employee. The employer is liable to execute the court decision immediately or within 8 days.

Every citizen who believes that by an individual act or action his rights and freedom are violated, respectively his rights and obligations deriving from labor relations are discriminated, may request protection at the Constitutional Court within two months, or five years the latest. In his request to the Constitutional Court the employee in his capacity of a citizen will state the reasons for requesting protection, the evidence upon which the request is based as well as other data required for the Court to decide. As by rule, after the public hearing, the Constitutional Court, by its decision for protection of freedoms and rights will rule whether such freedoms and rights are violated and consequently the individual act, forbid the action or refuse the request. The Constitutional Court will define the manner of eliminating the consequences.

The Trade Union plays an important role in the protection of the rights of the employees. It may contribute in several ways, such as: a) to give its opinion before a decision, respectively complaint is adopted, b) to participate in the procedure before the competent body which decides on the submitted request or complaint by the employee, c) upon employee's request, to represent him in exercising his right. Therefore, the employer is liable to request the opinion from the Trade Union which member is the employee, before adopting its decision. Otherwise he will violate the Labor Law. Nevertheless the Trade Union may or may not submit its opinion, also the employer is not liable to wait for its opinion.

The Trade Union may participate in the procedure in the competent body which decides upon the request or complaint, and upon request or in agreement with employee, may represent him in exercising his right. In this case the Trade Union acts as a representative of the employee with all its rights and obligations as a representative in the procedure before the competent body deciding on the submitted request or the complaint by the employee. In this respect the Ministry of Labor and Social Policy (through its Labor Inspector) competent for labor matters, plays a special role regarding the protection of rights deriving from labor relations. In case when the Labor Inspector finds that a law, other regulation, collective agreement and working contract have been violated, he will adopt a decision requiring that all irregularities are eliminated within a given period. If the employer fails to do so, the Inspector will initiate the procedure before a relevant court. The employee may also request protection from the Labor Inspector when the decision regarding his rights and obligations is final. In such cases two conditions should be met.

According to the first, the Labor Inspector has to define whether such decision violates the rights of the employee. While according to the second he has to define whether the employee has initiated court procedure at the relevant court. If both of these conditions are met, the Labor Inspector will adopt a decision for postponing the execution of the final decision until the court decision becomes final.

Strikes

The Constitution of FYROM guarantees the right to strike. Therefore, the right to strike is regulated in the Law on Strike dated April 5, 1991. According to the Law, the strike is organized cessation of work for the purpose of attaining economic and social rights and interests of the employees based on labor. The employee is free in deciding about his participation in the strike. The strike may be organized by the employees at the level of an enterprise, within some units of the enterprise, at the level of a branch, in certain activity or as general strike. When the strike is organized in an enterprise and in some units of the enterprise, the decision to go on strike is adopted by the Trade Union body organized within the enterprise.

When the strike is organized in a branch or in an activity the decision to go on strike is adopted by Trade Union of the branch, respectively the activity, while the decision for general strike is adopted by the supreme body of the Trade Union in FYROM. In case of a so called unorganized strike, or spontaneous strike, the decision is adopted by the majority of employees in an enterprise or in a enterprise unit. The decision to go on strike establishes the requests of the employees, the time when the strike should start and the, place where the participants in the strike will gather. At the same time a committee is established, called Strike Committee that will represent the employee's interests and conduct the strike on their behalf.

The Strike Committee is liable to inform the managing board of the enterprise about the strike at least five days before the date of its begging, by submitting the decision for strike. In case of a strike decision in a branch or activity or general strike, such decision is submitted to the relevant body of the Chamber of Commerce as a branch association. The Strike Committee and the representatives of the body to whom the strike was announced, as by rule, should try to settle the dispute by mutual consent, starting from the day of the announcement and during the strike itself. In cases when the Trade Union is not an organizer of the strike, members of the Trade Union when invited by the parties involved in the dispute, may participate in the negotiations for resolving the dispute by mutual consent. Representatives of the Chamber of Commerce, respectively the organization of the employers and the Government, may also be invited to participate in the negotiations even if not informed for the strike previously.

The strike may be stopped by an agreement reached between the entities that brought the strike decision and the bodies to whom such a decision was submitted. It may also stop by an unilateral decision by the Trade Union, or the employees who had brought a strike decision.

The employees in public services or employees performing tasks of public interest as defined by law, in the military forces, police and the administrative bodies, may exercise their right on strike provided that the following conditions are met: a) minimum workload which provides security for the people and the property in order to provide existence and work for the citizens and for the work of the other organizations, b) execution of international obligations. In the activities falling under public interest, the strike must be announced to the managing board, to the Trade Union - if the Trade Union is not an organizer of the strike, to the competent state organ at least 10 days before the begging of the strike by submitting a strike decision and by a statement about the manner in which minimum workload is provided.

The Strike Committee and the representatives of the managing board and the representatives of the state body are liable to offer proposal for resolving the dispute until the date of the beginning of the strike. The employees announcing the strike and the public should also be informed about the proposal. The Strike Committee is liable to cooperate with the managing boards during the strike in order to provide minimum workload. Also, the employees performing the so called minimum workload are liable to exercise the assignments given by the employer during the strike.

Organization of strike, respectively participation in a strike is not considered to be violation of working obligations, and may not be a basis for material responsibility of the employee and result in termination of working relations only if the strike is in accordance with the law and collective agreements. Any employee participating in a strike is entitled to his basic rights deriving from working relations, the right to salary and the right to pension and disability insurance. But organizers of the strike, respectively the participants in the strike may not enjoy such protection if acting contrary to the Law and the Collective Agreement.

Therefore, the strike as an organized stoppage of work by employees for purpose of achieving economic and social rights and interests base on labor, will be legitimate only if it is consequence from failure of the employer to meet its obligations regulated by Collective Agreement, or if it is a result of aggravation of the economic situation of the employees when all means for consensual resolution of the disputes are used, so that mutually acceptable solution may not be reached. The strike should be primarily directed towards the employer. It is his economic and other interests, and not the interests of the citizens that should be affected. Therefore it is very important how the strike is organized and what means, or techniques are used to impose pressure e.c. by temporary stoppage of work, by reduced scope of work, by stoppage of some stages in the work process (partial strike), by producing low quality products and by complete stoppage of the work process.

There are many issues regarding the legality of the actions both on the part of the employer and employees, when organizing and implementing the strike. Among the most important are so called strike-breaking and means for protecting the employer's interests.

The Strike Committee and the employees participating in the strike may not prevent the employees not participating in the strike from working. When the strike is organized in accordance with the Law the employer may not hire new employees to replace those on strike, unless the public interest is affected. This means that strike-breaking is not permitted.

5.14.Accounting and Taxation

5.14.1.Accounting and Audit System in FYROM

Over the course of the entire existence of the former Yugoslavia, the accounting regulation underwent frequent amendments. The main characteristic of those amendments was the introduction of the income category and its distribution, along with the ensuing numerous unwanted consequences (particularly with reference to the abolishing of the cost of acquisition category, the accounting in management, and the promotion of accounting methodologies in corporate governance). A substantial move towards radical improvement of the accounting practice in the former Yugoslavia was made in 1988, with the undertaking of activities leading to synchronization of the then current Yugoslav accounting system with the world standards, and in particular the legislation of the European Union. The *Accounting Law* was passed in 1989 and this law abolished the use of the income as an accounting category, and the costs components were incorporated in the cost figure. This law contained provisions for auditing of financial statements, although such provisions were not implemented in practice. Finally, the advantage brought by this law is its intention to substitute regulation with deregulation.

The framework of the accounting system in FYROM was laid out with the *Accounting Law*, adopted in July 1993 (Official Gazette No. 42/93, 48/93, 6/95). Comparative analyses of the provisions of the current legislation in FYROM show that it is based on and affected by the solutions provided in the text of the 1989 law. Furthermore, it contains provisions which correspond to the Fourth and the Seventh Directive of the European Union. This law can be easily adapted to the contemporary trends in accounting and has a universal application, that is, it applies to commercial and non-commercial entities. The accounting plan is an integral part of the *Accounting Law*, even though it exists as a separate regulation.

The main provisions of the *Accounting Law* determine who is obliged to keep accounting records in accordance with the law - those are the legal entities domiciled in FYROM and physical persons performing

business activities. The law also applies to companies and offices abroad in which capital has been invested (representative offices, business units and other forms of operating business abroad). In that respect, depending the number of employees and the value of the assets disclosed in the annual statements in the preceding two years, the entities are divided in two categories: small and large.

The provisions regarding the manner of keeping the accounting records comprise a separate part in the *Accounting Law*. Entities are obliged to keep business records in accordance with the Law, to comply with the standard accounting practice and the accounting standards developed thus far. Hence, it is apparent that the accounting regulation in FYROM has considered the necessity of fully developed accounting standards as a replacement of the regulation and an instrument for defining the terms, the principles, the postulates the rules and methodologies in the accounting practice.

The Law provides that business records are to be maintained by way of prescribed standard forms and other types of evidence, which allow tracking of the condition and the flow of assets, capital, liabilities, revenues, expenses, operating income and its distribution. Business records are kept according to the double entry system, except in the case of government bodies and other budget-financed organizations, for which budget accounting may be allowed. The accounting documents represent the basis of the business records; they are defined as written documents showing a change in the business, which proves the change in the assets, liabilities, capital, revenues and expenses.

Every organization is obliged to maintain business books (journal, ledger and analytical records) and apply standard account codes and an accounting chart consisting of 10 classes.

However, every organization may, for their own purposes, break down the accounts into analytical ones. Business books may be administered only by a professional - an authorized accountant, who is liable for the validity of the records and the plausibility of the data and their presentation.

The mandatory financial statements include the following: balance sheet, profit and loss statement and a supplemental accounting statement (annex) and a report on the operation. They are required at the time of filing the annual statement, while the semi-annual statement contains only the profit and loss statement. For organizations which have a majority vote in other organizations, consolidated statements are required.

The balance sheet shows the condition of the assets, liabilities and the capital on the day of its preparation. The revenues, expenses and the operating income (positive or negative) are shown in the profit and loss statement. The distribution of income statement is an integral part of the profit and loss statement. The forms used in preparing the financial statements are prescribed by the Law. Together with the annual account, large organizations are obliged to file a supplementary accounting statement - annex (which contains detailed explanations on the applied rules in estimating and accounting), as well as an annual report, which provides information not only on the financial aspect, but also on the entire operation of the company (major events, future development prospects, perspective of the production programs, research activities, company share purchases). Their content is regulated with the *Rules and regulation on the content of accounting items and the manner of preparing the Balance sheet, the Profit and Loss Statement and Distribution of Income* (Official Gazette No. 13/94) and the *Rules and Regulation on the form and content of the supplementary accounting statement - annex* (Official Gazette No. 13/94)

With the *Accounting Law* the issue of estimating the items in the accounting statements, that is, the estimation of the value of the assets, capital, liabilities, revenues and expenses is treated in FYROM in the same the manner as in the international accounting standards. The same applies to the acknowledging of items of abnormal size in the profit and loss statement.

The estimate is performed according to the rules determined with the accounting policy of the organization and in compliance with accepted accounting concepts, principles, standards and a positive accounting policy. For the preparation of the accounting statements definitions are made regarding the basic assumptions (reliability, consistency, recording at historical cost) and the principles (realization, non-matching values, individual valuation of assets and liabilities, time connection, relevancy). The basic rule in

assessment is the cost of acquisition for products purchased, and cost of manufacturing for own products. The Law also defines the principles and the manner of evaluating the individual accounting items in the balance sheet and profit and loss statement. The write-off of tangible and intangible assets is done in accordance with the *Regulation on the manner of calculating depreciation, write-off of tangible and intangible assets and the nomenclature of assets for depreciation* (Official Gazette No. 13/94).

For the purpose of updating the condition of the assets and liabilities in the accounting records with the actual condition, organizations do an inventory count at least once a year. The principles and the deadlines for inventory count are regulated with the *Rules and regulation on the manner and the deadlines for doing inventory count and harmonization of the accounting with the actual condition*" (Official Gazette No. 14/94), passed by the Minister of Finance.

In view of the fact that FYROM had a high inflation during the period following its independence, the *Accounting Law* pays particular attention to the issue of assets revaluation. Tangible and intangible assets, including their depreciation are revalued by the rate inflation of the price of industrial products. The result of that is the revaluation reserve, which is distributed to corresponding sources of funds after the annual filing of accounts. The manner of revaluation is regulated in detail with *Rules and regulations on revaluation* (Official Gazette No. 14/94). The inflation figures are published by the Statistical Office of FYROM.

On request of companies, the annual accounting statements can be inspected and assessed by an authorized auditing organization. Although the *Commercial Code* contains similar provisions regarding audits, such provision have not been widely implemented in practice. It is expected that the *Law on Audits* and the *Law on Government Audits* will be adopted in the very near future. Their objective is to make possible for objective and independent audits, a higher quality of the audits in compliance with international auditing standards, and establishment of professional liability of auditors. According to the proposal - *Law on Audits* it is anticipated that audits be performed by auditing companies which will have to meet the requirements of the *Commercial Code* and the *Accounting Law*.

Some aspects of the accounting regulation have been covered in other laws as well: *Profit Tax Law*, the *Law on Financial Operations*, the *Commercial Code*, the *Securities Law*.

Commercial Code deals with business books and annual accounts, but in a partial manner. These provisions define the obligation of keeping business books, the manner of their keeping, the inventory count, the archiving of the accounting statements and their presentation and use in court procedures and cases. This Law also contains provisions regarding qualified accountants - specialists who can be entrusted with the keeping of accounting records. The provisions of the *Commercial Code* refer as well to the annual accounts, their contents, and the auditing of the annual accounts and their inspection. All commercial enterprises which have either have above 150 employees, or annual revenues above 6 million DEM or an average value of the assets at the beginning and at the end of the year above 1.5 million DEM, are obliged to have their annual accounts audited. Finally, the *Commercial Code* deals with the issues of income distribution and dividend calculation.

According to the law, the income is determined according to the accrual method. Considering that the income in the profit and loss statement serves as a tax basis, the allocation of the expenses is of particular importance. Among the expenses, special treatment is given to the personal income and the depreciation, which is deductible up to an amount determined in separate regulation. Certain revenues (vehicle allowances, presents, food and drink) for members of the board of directors or shareholders are not deductible expenses. Supplies, according to the tax regulation are itemized as expenses at the average cost of acquisition, that is, LIFO and FIFO methods cannot be applied. Companies prepare a tax return every six months.

FYROM has experienced accounting professionals. This is a result of the numerous changes of the accounting legislation in the past. These professionals are organized through the Association of accountants, financial officers and auditors in FYROM. There are a number of consultant houses and other associations. They all have an active role in the modernization of the accounting practice in FYROM and its

harmonization with the world trends. Companies like Coopers & Lybrand, Deloitte & Touche and KPMG have been present in FYROM.

It is a general conclusion that the accounting legislation in FYROM is concise and clear, however, adjustments and harmonization with the international accounting standards are necessary. In 1997 *Rules and regulations on the accounting standards* (Official Gazette No. 40/97) was passed. It prescribes the accounting standards that will apply in the accounting practice, and the preparation and filing of the financial accounts. These are, in effect, the International Accounting Standards determined by the International Accounting Standards Committee (IASC). Out of the existing 34 accounting standards FYROM has adopted the first 32. Their practical application is to begin on January 1st, 1998. For this purpose, amendments of the *Accounting Law* is in procedure, and there will be new rules on the account chart. Numerous preparations and training of the accountants are underway in order to ensure a correct application of these standards.

5.14.2.Taxation

Introduction

The new Tax System in FYROM was introduced in 1994. With the Tax System there are eight different taxes, instead of sixteen in the previous system. The solutions in the new Tax System are close to the ones in the modern tax systems in the developed countries. The adoption of the VAT was in 1998, and its introduction in 2000.

The taxes that are in force in FYROM are:

- Personal Income Tax,
- Profit Tax or Corporate Tax,
- Trade Tax for Goods and Services,
- Excise Tax,
- Customs,
- Property Tax,
- Inheritance and Gift Tax,
- Estate and Rights Trade Tax.

The following table presents the tax summary as of April 1, 2000 which introduced the new VAT system.

Table 40.FYROM: Tax Summary as of April 1, 2000

TAX	Nature of Tax	Exemptions and Reductions	Rates
Central Government			
1. Taxes on Income and Profits			
1.1. Profit Tax	<p>A tax on annual business profits. Resident legal entities and physical persons are taxed on their global profits. Nonresidents are taxed on profits earned in the FYROM. An entity is a resident of the FYROM if it is established and registered there.</p> <p>The taxable base is the different between total revenues and expenses, as well as depreciation.</p> <p>Tax payers make monthly advance payments based on the previous year's profits, adjusted for inflation. Payments for the period July - January are adjusted based on actual profits.</p>	<p>Fixed assets used for:</p> <ul style="list-style-type: none"> i) Technological modernization, ii) Structural adjustment iii) Protection of the environment receive accelerated depreciation. <p>Reinvested profits are deductible.</p> <p>Investment in economically undeveloped districts, border regions and certain mountain districts are deductible.</p> <p>The profits of:</p> <ul style="list-style-type: none"> i) Joint ventures with foreign partners, where the foreign partners hold at least a 20% share, iii) Foreign enterprises, are exempted of paying the corporate tax in a period of three years, as of the year in which profits are gained. iv) Rehabilitation firms employing disabled persons are exempt. 	<p>Standard rate: 15 percent</p> <p>For remitted dividends: 15 percent</p>

TAX	Nature of Tax	Exemptions and Reductions	Rates
Central Government			
1. Taxes on Income and Profits			
1.2. Personal Income Tax	<p>A tax on annual aggregate net personal income from all sources.</p> <p>Residents are taxed on their worldwide income. Nonresidents are taxed on income earned in the FYROM.</p> <p>The tax is withheld source on a monthly basis</p>	<p>All social security contributions are deductible.</p> <p>¼ of the average salary amount is deductible.</p> <p>Investment in land improvement or in land consolidation is deductible by 50% and 100%, respectively.</p> <p>Investments in far in buildings and agriculture implements is deductible for up to 30% of the cadastral income.</p> <p>Interest on demand deposits is exempt. Distributed dividends are 50% exempt.</p>	<p>Progressive tax rates are applied as follows:</p> <ul style="list-style-type: none"> i) Income below two times the average monthly wage (AMW): 23%. ii) Income between two and five times AMW: 27%. iii) Income over 5 times AMW: 35%.

TAX	Nature of Tax	Exemptions and Reductions	Rates
Central Government			
2 .Value –Added Tax(VAT)			
A new VAT system was introduced April 1,2000.	<p>A tax on consumption, calculated at all stages of production and supply, using the destination-based credit invoice method.</p> <p>The threshold for monthly filers is denar 25 million (\$417.000 US) and quarterly filers denar 1 million (\$17.000 US).Payments are due within 15 days from the end of the tax period. Refunds are point within 30 days.</p>	<p>The following are zero rated: exports, goods transported to/or dispatched from duty –free trade zones, services related to import and export, services performed by brokers and other intermediaries, aircraft leases used in international commercial air traffic, and international air transport of passengers.</p> <p>The following are exempt from VAT: residential building and apartments except the first supply, rents, postal services, banking and financial services, insurance, health services, medical and dental services, educational services, and funeral services.</p>	<p>General rate:19% Returned rate 5%.</p> <p>The reduced rate applies to: food procedures except alcoholic beverages and soft drinks, basic agricultural products, water, electricity coal, wood, gas, air conditioning and heating, drugs, personal care products, books, pamphlets, newspapers, and periodicals, public transportation, waste disposal and public sanitations, and services of lawyers, accountants, and auditors.</p>
2.1. Excise Tax	<p>A tax on the sale or import of goods. Excises are generally imposed at the manufacturing and import stage. However, excises on luxuries are imposed at cash distribution stage.</p> <p>Control marks are widely used to enforce payments of all excises.</p>	Exports are exempt.	<p>Oil 11% except, Gasoline, Diesel, Heating oil, SL:38.3% Jet fuel (17%), LPG:5% standard rate LPG: for cars/vessels 40% Fuel oil.</p> <p>Alcohol Alcohol (3 denars per % of alchol/liter) Spirits (2 denars per % of alcohol/liter) Beer 15denar/lier</p> <p>Tobacco Cigarettes Domestic:1,350 denar/kilo Imported:40%</p> <p>Automobiles Up to 2-liter cylinder:25%. Over 2-liter cylinder:55%.</p> <p>Luxury items:50% Coffee Unroasted:70 dn/kilo Roasted:85 den/kilo Instant:90 dn/kilo</p>

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TAX	Nature of Tax	Exemptions and Reductions	Rates
Central Government			
2. Value Added Tax (VAT)			
2.2. Import Duties	Tax on import goods.	<p>Exemption for these items:</p> <p>i) re-exports .Must provide a bank guarantee for the amount of duty, in case re-export does not occur.</p> <p>ii)raw materials. Must pay duty, but after exporting finished product receive a duty-drawback.</p> <p>Exemptions for these organizations:</p> <p>i) Diplomats and consular missions</p>	<p>Rates range from 0% to 25% .</p> <p>Lower rates on raw materials. o duty on cotton or crude oil.</p> <p>Preferential trade agreements specifying 1% statistical change alone, apply to trade with:</p> <p>i)SLOVENIA (Agreement 1996) Exception tariffs on industrial goods reduced gradually, with final elimination by 2000.</p> <p>ii)FR Yugoslavia (Agreement 1996) Beyond a specified quantitative limit, general tariff rates apply.</p> <p>iii)BOSNIA (agreement 1997)</p> <p>iv)CROATIA (agreement 1997) Exemption: refined oil is subject to prohibitive tariffs. 1997 average tariff rate:6.3%</p>

TAX	Nature of Tax	Exemptions and Reductions	Rates
Central Government			
3. Taxes on Property			
3.1. Inheritance & gift tax.	A tax on inheritance and gifts.	In general recipients within the first degree of kinship (a spouse, child, or parent) are exempt. Recipients within the second degree of kinship (a grandchild, brother, or sister) are exempt only if they lived in the donor's household at the time of death or when the gift was given.	For recipients within the second degree of kinship: 3% (prior to 1997: 5%) All other: 5% (prior 1997: 10%)
Social Security Funds			
4. Social Security Funds	All persons are liable to compulsory monthly social security contributions. For employed persons the contributions together with the income tax are withheld at source. Self-employed persons pay the Contributions with their monthly income tax.		Rates are the same for employed and self-employed persons: Pension & Disability fund: 20%. Health Care fund: 8.6% Employment fund: 1.5%.

Source: IMF country report, N. 00/76, June 2000, page 98.

5.14.2.1. Personal Income Tax

Personal Income Tax is paid annually to the income of the taxpayer, considered as a sum of all the net income of the taxpayer from different sources for the period of one calendar year, except the income that is not a subject of taxation. Net income of the taxpayer is the difference between the gross income and the expenses made for its realization. Tax is not paid for income due to: awards from international organizations, awards due to significant results in science, culture and sports, scholarship, social and other help, severance pay, interest on public loans etc.

The income is due to taxation no matter the place or the form it is realized in, meaning the income realized in FYROM or abroad is treated the same, as well as the income is in currency or goods. If the income is paid in goods the payer should declare their market value in denars and add it to the other income.

Taxpayer

There are three categories of taxpayers:

- individual, resident of FYROM, for the income realized in the country and abroad,
- individual, nonresident of FYROM (foreign person), for the income realized only in FYROM,
- individual that is getting income from not registered business.

Taxable Base

Taxable base consists of the sum of separate net incomes of the taxpayer during the year, decreased for:

- personal exemption up to 25% of the average annual net wage in the country, according to the Statistical office data,
- contributions for social insurance (disability-pension fund, health fund and employment) and other public contributions upon the taxpayer's income (except contribution paid upon the land registered income).

The income that is the ground for the calculation of the taxable base consists of five categories:

- personal income from the employment, pension or disability,
- income from agriculture,
- personal income from professional activity,
- income from property and property rights,
- other income.

Any income on the ground of working relation established in the country, nevertheless the person is working in the country, abroad, in the diplomatic or other international office in FYROM, income from contractual engagement, pension and disability payment is treated as personal income. According to fees for membership in governing, supervisory boards, parliament, local government, professional sportsmen, seek-leave compensation and other compensations for the engagement not treated as an employment, are also subject to taxation.

Tax exempted are head and personnel of the foreign diplomatic and consular bodies FYROM, UN officials, honorable consular representatives and country's citizens working in the international organizations.

Income from agriculture consists of registered land income on the base of agriculture land unit (cultivated or not), and real income.

The taxpayer is the owner or the one who uses the land. Taxable base is the registered land income, but the taxpayer can choose taxation on the real income. Taxable base is the real income in the case when it is much bigger than the registered land income. In this case the taxable base is the profit calculated according the Profit Tax Law.

Income from agriculture is not calculated for the land that is prohibited for agriculture, courtyards from religious objects, residence courtyards up to 500 sq.m, and land used for building of objects for protection from accidents from natural forces.

Temporary exemptions of five years are provided for the land transformed into cultivated, with certain investments and for the land with new plants. Total exemption is provided for the taxpayers in passive districts. There are tax benefits for the taxpayers that invest in the melioration, production objects and agromechanical equipment.

Personal income from professional activities includes income from professional and intellectual services. Tax base is established from the personal statement in the tax return, according to the regulations of the profit tax, but the minimum can not be lower than the average wage in FYROM.

In certain cases when the activities are small or temporary and the income is lower than the average wage in FYROM, Public Revenue Office may, on request of the taxpayer, or independently, decide tax to be paid on a lump sum income.

Income from property and property rights derives from rental of assets, equipment etc. The tax base is annual income from rent decreased for the maintenance and managing expenses up to 35% of the income.

In the category of other income there is:

- income from copyrights and patent rights,
- income from capital,
- capital gain income,
- income from luck games etc.

In the first case the taxpayer is the person who owns the right. The taxable base is net income. The tax rate is usually progressive according the profit tax, but the income from literary works, art, architecture, cinematography are treated with the lowest rate of 23%.

In the second case income includes: dividend and other incomes from profit sharing, interests on credits, bonds, savings, deposits etc. In this case tax is paid on each separate payment with the tax rate of 23%, and at the end of the year they are included in the taxable base of the annual profit tax.

Capital gain is income measured by the difference between the selling price and adjusted value.

In the case of long term capital gain, they are included with 50% in the tax base, and the short term ones are included with 100%. The tax rate is 23%.

In the case of winnings in luck games, every each of the winnings with the value higher than the average monthly wage in the country, is subject to taxation with the tax rate of 23%. This taxation is not included in the annual tax base.

Tax rate

Tax rate is progressive and there are three categories:

- for the tax base up to two average monthly wages - 23%,
- for the tax base over two and up to five average monthly wages - 23% for the part up to two average monthly wages + 27% for the part over two average monthly wages,
- for the tax base over five average monthly wages - 23% for the part up to two average monthly wages + 27% for the part over two average monthly wages up to five average monthly wages + 35% for the part over five average monthly wages.

Administration

The Public Revenue Office (PRO) is in charge for administration of the tax.

The annual tax is calculated according the data from the tax return and financial papers of the taxpayer, and other data available to the PRO.

The taxpayer is obliged to submit the tax return till the end of February for the previous year. To simplify the procedure and to ease the data processing at the end of the year, there is a possibility for exemption of this rule. If the only income of the taxpayer is the income from the employment, pension or disability, and if the only tax base is income from registered land on the base of agriculture land unit, the taxpayer is not obliged to submit the tax return.

Personal Income Tax for the income from: the employment, pension or disability, professional activity, capital, property and property rights and luck games are calculated and paid on each payment to the taxpayer, as "advance" to the annual tax. The taxpayer have to receive an written information about the calculation and payment for each of these tax payments, and at the end of the year, a summary annual information about the tax payments for the income on the above mentioned grounds. The copy of this annual information is also submitted to the PRO.

In the case of taxation of income from agriculture, capital profit and other income than the ones mentioned in the previous paragraph, the PRO may issue a decision for their payment. The decision is issued according the data from the land register, tax return, financial papers of the taxpayer and other relevant information, and the payment is done monthly or quarterly.

In 60 days after the submission of the tax return, the PRO must bring the decision about the amount of the annual tax. In 30 days after the receipt of this decision the taxpayer is obliged to pay the difference between the annual tax and the amounts paid during the year. If the taxpayer has paid more than the amount of the annual tax he has the right to be reimbursed for the difference.

5.14.2.2. Profit Tax or corporate tax

Subject of this taxation is the profit as a final result of the activity of the legal entities as well as individuals.

Taxpayer

Taxpayers are all legal entities, no matter what is their ownership structure, organizational or legal status and all individuals, residents of FYROM, having registered activity in the country or abroad. Taxpayer is also a foreign legal entity or individual, non resident of FYROM, having registered activity, for the profit made in FYROM. The main legal entity and its subsidies may act as a single taxpayer.

Taxable Base

Taxable Base is the profit calculated as a difference between the total revenue and the total expenses of the taxpayer. The profit is stated in the tax balance where the elements of the total revenue and total expense are according the accounting and tax regulations.

In the tax balance, the revenue is established through the data from the sale of products, services or else. In the part of the expenses two categories are of big importance: the wages of the employees and depreciation.

The expenses for the materials and purchase value of the sold goods are calculated with the method of average price.

All the transactions of the taxpayer must be stated in the tax balance together with the realized transfer prices so they can be checked out. To prevent the tax evasion through reduction of the profit with the transfer prices, only the prices that can be realized on the domestic or comparative foreign market are recognized, so the difference between the market and transfer price will be added to the taxable base.

Calculated and paid gross wages of the employees are recognized in total as expense. On the other hand, the income of the employees from the profit of the taxpayer are not treated as expense, because that is distribution of the profit after taxation.

Depreciation of the assets, as one of the major categories of the expenses of the tax balance, can be calculated by proportional, functional or method of depreciation chosen from the taxpayer. The only thing is that once chosen method of depreciation for an asset or group of assets, must be used till final their final depreciation. The only limitation in the calculation of the depreciation is in the use of functional method, in the case when the depreciation according this method is higher than the depreciation calculated with the proportional method, for 10% and more. In that case, the further calculation of the depreciation with functional method, must be approved by PRO.

Interest on the credits taken in relation with the business activities are treated as expense in the tax balance. Penalties are not treated as expense. Expenses for the use of the vehicles, food and drinks, gifts etc. not strictly connected with the business activity, are not treated as expenses of the taxpayer. Total expenses for promotion, propaganda, advertising etc. are treated as expense but only up to 3% of the total revenue. Payment for scholarship, if not made through certain foundations are not treated as expense. The exemption from this are scholarships for top sportsmen. For taxpayers (bank or other financial institution, insurance company), all risk or security funds are cause for tax base decrease, but only up to **15%**.

Capital income is due to taxation if tax is not paid from the one who pays them off. Capital profit is also due to taxation. Short-term capital gain from sale of shares and bonds, being in the portfolio for less than 12 months, as well as sale profit of equipment and real estate is included in the tax base in whole. Long-term capital gain is included in the tax base with 50%. Eventual capital loss is compensated with the capital gain in one or three next years.

The loss from business, financial or other transactions can not be transferred into next year to be compensated with that year's profit.

Tax Rate

The tax rate is 15%, and it is unique.

Tax Incentives

The policy of Tax Incentives is restrictive. The mechanisms of the Tax Incentives are:

- quicker depreciation,
- tax base deduction,
- tax exemption.

Quicker depreciation means using of higher depreciation rate than the rate from usual methods. The taxpayer has the right to use a rate 25% higher than the usual if implementing a technological modernization, structural adjustment, or for depreciation of assets used in environmental protection.

Tax base can be deducted in these cases:

- for reinvestment of the profit in new investments in FYROM the tax base deduction is the same with the amount invested,
- for investment of the profit into extending of the own business, the tax base deduction is the same with the amount invested,
- for investment in passive, highland and areas near the border, the tax base deduction is the same with the amount invested.

- for domestic legal entity or individual, if the portion of the foreign capital is at least 20% of the total investment, and for the foreign investor the tax deduction is the same as the portion of the profit of the foreign legal entity or individual, for the period of the first three years.
- for the transfer of the profit, foreign investors pay tax with the tax rate of 10%
- for the funds invested in the environmental protection and international sports in FYROM .

Enterprises for professional rehabilitation are tax exempted.

To avoid the double taxation, the tax is deducted for the amount of the profit tax paid abroad, up to the amount of the tax calculated with the rate of 15%. The main legal entity has right of tax deduction for the amount of tax paid by its subsidiary abroad for the profit included as a revenue of the main legal entity.

Administration

The taxpayer is calculating and paying the tax with the semi-annual and annual balance. During the year the tax is calculated and paid monthly, as "advance", not later than 15th in the month for the previous month.

5.14.2.3. Trade tax for goods and services

Trade Tax for Goods

This tax is paid for the goods sold to end consumers or to resale. The sale for end consumers include:

- import of goods,
- taking of own products for own purpose,
- giving products without compensation (gifts, replacement etc.),
- shortage of products,
- outgoings, if bigger than proscribed with standards,
- use of the product of the individual that has to be registered annually,
- giving without compensation a motor vehicle or a boat that has to be registered annually.

The tax is not paid for:

- sale of material for reproduction to production enterprises, shops, agriculture enterprises,
- sale of products to legal entities or individuals for repair and servicing of products,
- sale of products to trade enterprises, restaurants, hotels etc. and shops for their further manufacturing or resale, except refreshment drinks, mineral waters, excise products as liqueurs, coffee, beer etc.
- sale to the local communities for building of infrastructure,
- import of products for reproduction, etc.

Tax Exemptions

Trade Tax exemptions are for:

- food: all kinds of bread, raw milk, oil and fat,
- products for export,
- imported products that are duty exempted,
- products sold to the diplomatic and consular offices and their personnel,
- armory and products for the arm forces,
- water and water steam,
- administrative and mail stamps, shares, bonds etc.,
- products for the Red Cross of FYROM without compensation,
- products produced from the enterprises for rehabilitation and employment of disabled persons, according to proscribed conditions,
- pharmaceuticals,
- orthopedic accessories,
- funeral accessories,
- motor cars for the disabled persons according to the proscribed regulations.

Taxpayer

The taxpayer is:

- legal entity or individual who sells the products to the end consumer,
- by exemption, legal entity or individual who bought the products,
- legal entity or individual who imported the products for resale or own use
- every legal entity or individual that is part of the trade: producer, gross seller, retail seller etc.

Taxable base

The taxable base is the sale price of the product. The taxable base for import is the value of the product according to the customs regulation including the customs and other import expenses. In the multiphase trade the taxable base is sale price decreased for the calculated tax for the previous salesman or importer.

Tax rates

Tax rates are proportional and are proscribed as a percentage of the taxable base.

Trade tax for the products for the end consumers is 25% except for:

equipment for own activity, used cars and boats that has to be registered annually, agricultural equipment, fertilizers, generic products for agriculture and fishery, products for nutrition of humans and animals, original art pieces, computers, hardware and software, electric power, coals, daily and weekly papers and periodical, school books, notebooks, dictionaries , books, brochures, magazines, cocoa, chocolate, salt, sugar products, motor vehicles and spare parts, industrial waste, soaps, toilet paper shaving soap, toothpaste etc.

For the above listed products the tax rate is 5%.

Trade Tax for Services

This tax is paid for all the services provided with compensation. Tax is not paid for:

- services for giving credits for liquidity of banks, foreign currency deposits, interest on deposits of the legal entities in the banks, and deposits of the commercial banks in the National Bank etc.,
- life insurance, insurance of foreign legal entity or individual in foreign country, international ship insurance, international airplane insurance, additional truck insurance for outside the FYROM,
- transportation of passengers and goods in railway traffic, transportation with buses, public lake transport of passengers and internal transport,
- health services and social services,
- services of the Red Cross of FYROM,
- post, telephone and telegraph services,
- services in culture, education,
- services of religious organizations,
- geological research and research and development jobs,
- services in child and youth hostels,
- services of individuals to legal entities and entrepreneurs,
- compensations for legal services,
- transportation services in the international traffic,
- services of foreign diplomatic and consular offices.

Taxpayer

The taxpayer is the legal entity or the individual that provides the services.

Taxable Base

The taxable base is the value of the compensation for the service in money, goods or counterservice, or the realized provision, difference between the purchase and sale price, positive difference between the active and passive interest, etc.

Tax Rates

Tax rate is proportional and is proscribed as 13% of the taxable base.

5.14.2.4. Excise tax

Excise tax is a different type of trade tax for products. It is a tax on the sale or import of goods.

Excise tax is paid for: *petrol products, tobacco products, liquors, beer, coffee, motor cars, luxury products.*

Excise tax is calculated and paid not only in the import or trade with them but also in the cases when they are inherited, given with no compensation, replacement for other product or service, shortage of products, outgoings, if bigger than proscribed with standards, use of own product for personal purposes.

Taxpayer

The taxpayer for the petrol and tobacco products is the producer, respectively the importer. The taxpayer for the motor cars is the buyer. For all the other products the taxpayer is every part in the trade (producer, importer, wholesaler, retail seller, restaurants, hotels, shop or individual producer).

Legal entities, entrepreneurs or individuals that produce products due to the excise tax have to be registered in Excise Taxpayer Register as a condition to trade and produce these products.

Taxable Base

The taxable base for the petrol and tobacco products is officially proscribed price on which the tariff rate is applied. That means that the excise tax is calculated into the retail price.

The taxable base for all the other products is the retail sale price decreased for the amount of the calculated excise tax for the previous partner in the trade or import. That means that every part in the trade pays the excise tax only for the new added value in particular phase of the trade.

Taxable base for imported product is the price of the product according the customs regulations, including the duties and import expenses.

Tax Rate

The tax rate for the Excise Tax is different for different products.

The Excise Tax is paid together with the duties for the import of petrol products, tobacco products, liquors, beer, coffee and luxury products.

The taxpayer - wholesaler of the petrol products, liquors, beer and luxury products pays the excise tax every 15 days.

5.14.2.5. Property tax

Property tax is paid for the real estate and other assets.

Taxpayer

The taxpayer is the legal entity or individual, owner or user of the property.

Taxable Base

The taxable base is the market value of the property. According to the regulations the owner is supposed to express the value of the property, and the tax administration can adjust it if necessary.

Tax Rate

Tax rates are proportional and it is 0.10% for real estate and 0.05% for the other assets.

Tax exemption is proscribed for: land and buildings in state property, buildings of public enterprises, land and buildings in the property of religious organization, economic buildings in agriculture, rural living areas, infrastructure objects etc.

Tax deduction of 50% is proscribed for the flats or buildings in which the taxpayer lives with the family.

The property tax is paid quarterly.

5.14.2.6. Inheritance and gift tax

This tax is paid for inherited or gifted real estate and the right of its using. Inherited or gifted money, shares, bonds or other assets if worth more than one average annual wage in FYROM is due to taxation.

Taxpayer

The taxpayer is legal entity or individual who was gifted or inherited property in the country or abroad. Non resident individual is taxpayer only for the inherited or gifted property in FYROM.

Taxable Base

The taxable base is the market value of the property decreased for debts and expenses for the property.

Tax Rate

Tax rates are proportional and different regarding the generation.

For the taxpayer in the second generation the tax rate is 3% (prior in 1997 tax rate was 5%)

For the taxpayer in the third generation or not in any relation the tax rate is 5% (prior in 1997 tax rate was 10%).

Tax exemption is provided for the individual who has inherited flat or house, and has lived with the late owner for no less than a year, does not have other flat or house. Tax exemption is also provided for the individual who has inherited agriculture land, if his main activity is agriculture, and has lived together with the late owner in one family.

5.14.2.7. Estate and rights trade tax

The subject of this tax is trade with estate and rights, transactions of compensations of the property rights, exchange of estate and other obtaining of estate with compensations.

Taxpayer

The taxpayer is:

- legal entity or individual who sells the estate or property rights,
- legal entity or individual who makes the exchange of the estate or property rights with bigger value,
- owner of the share of the estate that is assigned,
- the one who takes over the estate on the ground of contract for life support.

Taxable Base

Taxable base is the market value of the property or right in the moment when the obligation occurs. In the case of exchange of estate the taxable base is the difference of market values of the estates.

Tax Rate

The tax rate is proportional and it is 3% .

Tax exemptions are the following cases:

- trade with estate in process of expropriation,
- transfer of rights of ownership of the foreign diplomatic or consular office,
- investment of estate in the capital of the shareholding company or company with limited liability,
- transfer of the right of ownership for the payment of the public debt,
- trade of estate between government institutions.

The tax is calculated according the tax return, business books of the taxpayer and other data available for the PRO.

5.14.3.Social Security Contributions

The system of Social Insurance in FYROM consists of: health insurance and pension-disability insurance, both regulated with separate laws. The rights from health and pension-disability insurance are realized through the Fund for Health Insurance and Fund for Pension-disability Insurance, respectively. These funds are financed from the budget, income or profit of the organizations, wages of the employees and other working persons, wages for additional work, total income of the organizations, interests and dividends, gifts etc.

Insured persons pay contributions from the wages for the social insurance.

Health Insurance

According to the Law for Health Protection the basic health protection is guaranteed through the obligatory health insurance for the following categories of citizens:

- all the employees in the public services, political organizations etc.
- all other employees working for a certain employer,
- citizens of FYROM working for a foreign employer, diplomatic service, international organizations or individuals in FYROM ,

- citizens working in agriculture,
- self-employed persons,
- writers, artists, composers and other persons doing their job under particular regulations,
- sportsmen as members of sport's associations,
- religious clerks,
- pensioners,
- temporary unemployed persons while registered in the Employment Bureau,
- veterans from the World War II,
- users of the Social Benefits,
- foreign citizens or persons with no citizenship, if employed in FYROM ,
- foreign citizens or persons with no citizenship, working for foreign employer in FYROM
- foreign citizens for the period of their education in FYROM ,
- foreign citizens working in the diplomatic service, international organizations or individual,
- prisoners,
- persons in military service.

The members of the family of the insured person have the same rights.

For certain categories of citizens, amongst others for foreign citizens or persons with no citizenship, if employed in FYROM, foreign citizens or persons with no citizenship, working for foreign employer FYROM, additional health insurance is obligatory.

All the citizens and the members of their family, as well as the employees through their organizations may be voluntarily insured for health services not included in the basic health protection.

All insured persons are registered in the Fund for Health Insurance. Registration is made by:

- the employer for the employees,
- the Fund for Pension and Disability Insurance for the pensioners
- the Employment Bureau for the unemployed,
- the particular Government institution for the war veterans, war invalids, members of the family of the victims of the war, persons in regular military service etc.
- prisons and similar institutions for the persons in their custody.
- All other persons are registered by themselves.

- The Fund for Health Insurance is financed through:
- the Budget of the country,
- income and profit of the legal entities,
- wages of the employees and contributions of the citizens,
- fees for additional work,
- total revenue of the organizations,
- contributions of the insured persons,
- interests and dividends,
- gifts,
- donations
- other income.

The Government pays for the regular expenses of the Fund, preventive measures for health protection, protection programs for AIDS, tuberculosis, obligatory vaccination, health protection of mothers and children and other guaranteed rights and established needs and interests of the society, insurance for prisoners and persons in regular military service, emergency medical help to the foreign citizens and other administrative expenses.

Expenses for basic health protection, covered by the obligatory insurance for the pensioners are provided from the Fund for Pension-disability Insurance, for the unemployed from the Employment Bureau, for the war veterans, war invalids etc. from adequate institution.

Expenses for citizens of FYROM working for a foreign employer, diplomatic service, international organizations or individuals in FYROM, citizens of FYROM working abroad, foreign citizens or persons with no citizenship, working for foreign employer in FYROM, foreign citizens for the period of their education FYROM, foreign citizens working in the diplomatic service, international organizations or individual are provided by themselves.

Expenses for all the employees in the public services, political organizations etc., all other employees working for a certain employer, citizens working in agriculture, self-employed persons, writers, artists, composers and other persons doing their job under particular regulations and foreign citizens or persons with no citizenship, if employed in FYROM, are provided through contributions from the gross wage.

The base for calculation and payment of the contribution is the gross wage including the contributions and taxes paid from the wage. For the unemployed, war veterans, war invalids, persons receiving social protection the base is 70% from the minimum wage proscribed with the General Collective Agreement.

The base for the persons working in the agriculture is the wage from their agricultural activities or the revenue from the registered land.

For the pensioners the base is their pension.

Expenses for the obligatory additional insurance are provided from the contribution from the income or profit of the organizations.

The contribution rate is proposed by the Government and adopted by the Parliament of FYROM. The contribution rate is 8.6%.

The contributions are paid up to 25th in the month for the previous month.

Pension and Disability Insurance

The Pension and Disability Insurance is obligatory for the employees that are citizens of FYROM, foreign citizens and persons with no citizenship. There is also a possibility for voluntary insurance for the persons not included in the obligatory insurance and for the persons who wish to obtain a wider range of rights than provided with the Law for Pension and Disability Insurance.

The management and implementation of the Pension and Disability Insurance in FYROM is through the Fund for Pension and Disability Insurance. As this is an obligatory insurance the resources are provided mainly from the employers and insured persons with the payment of the contributions.

The basis for calculation and payment of the contribution is the gross wage of the employee.

The contribution basis can not be lower than 65% from average monthly wage in the economic sector.

The contribution rate is unique proportional rate which is 20%.

The contributions are paid up to 25th in the month for the previous month.

NOTE: As for the customs, duties and levies, they are explained in the Part dealing with Customs Regulations.

5.15. Participation in International Programs: Industrial Property Protection

Membership of the WIPO

Since July 23, 1993, FYROM has been a member of the World Intellectual Property Organization (WIPO).

FYROM expresses its intention to be considered, in respect of the territory of FYROM and by virtue of succession of the Socialist Federal Republic of Yugoslavia, a party to:

- the Convention Establishing the World Intellectual Property Organization, signed at Stockholm, on July 14, 1967, and amended on October 2, 1979,
- the Paris Convention for the Protection of Industrial Property, of March 20, 1883, as revised at Stockholm on July 14, 1967, and amended on October 2, 1979,
- the Madrid Agreement concerning the International Registration of Marks, of April 14, 1891, as revised at Stockholm on July 14, 1967, and amended on October 2, 1979,
- the Nice Agreement concerning the International Classification of Goods and Services for the Purposes of the Registration of Marks, of June 15, 1957, as revised at Geneva on May 13, 1977 and amended on October 1, 1979,
- the Locarno Agreement Establishing an International Classification for Industrial Designers, signed on October 8, 1968, and amended on October 2, 1979,

- the Berne Convention for the protection of Literary and Artistic Works, of September 9, 1886, as revised at Paris on July 24, 1971, and amended on October 2, 1979.

FYROM accepts the obligations set forth in the said treaties, with all reservations made by the Socialist Federal Republic of Yugoslavia.

FYROM declares that, for the purpose of establishing its contribution towards the budgets of the Paris and Berne Unions, it wishes to belong to class VII.

Industrial Property Law (Official Gazette 42/93) governs the acquisition and protection of the rights for industrial property.

Rights for industrial property and procedure

The rights for industrial property shall be: ***patent, model and sample, designs trade mark, and service mark and appellation of origin.***

The administrative procedure and other administrative affairs regarding acquisition and protection of the rights for industrial ownership, shall be executed by the Office for Protection of Industrial Property of FYROM (hereinafter the Office).

Protection of inventions, new shape of a body, pictures and drawing, trade mark and service marks shall be requested, in FYROM, by submitting a relevant application to the Office.

The Office shall also accept applications requesting protection of inventions, new shapes of a body, pictures and drawing, trade mark and service marks abroad, if they comply with the international agreements and conventions to which FYROM have been admitted.

Protection of inventions, new shapes of body, pictures and drawing, trade mark and service marks in FYROM may also be requested by submitting an application abroad if they comply with the international agreements and conventions to which FYROM have been admitted. These applications shall have the same rights as the national applications, unless otherwise stipulated by a relevant agreement or convention.

Foreign legal persons and foreign citizens, regarding protection of industrial property in FYROM, shall enjoy the same rights as the domestic legal persons respectively citizens of FYROM, if it is in compliance with the international agreements and conventions or the principle of reciprocity.

The existence of reciprocity shall be proven by the person referring to reciprocity.

In procedures before the Office, the organs of the administration and the courts, foreign legal and physical persons shall achieve their rights arising from this Act through their authorized agent who is a domestic legal person registered to act as an agent in the field of industrial property, or a citizen of Macedonia whose profession is a representation in the field of industrial property.

An administrative procedure regarding protection of industrial property of first degree shall be decided on by the Office.

The party shall be entitled to a complaint against a first degree decision, passed by the Office, lodged to the Ministry of Development.

Contents of the rights

The holder of the patent, model or design shall have:

- i) exclusive right to use in the production a protected invention, shape of body, picture or drawing,

- ii) exclusive right to put on sale objects manufactured according to the protected invention, shape of body, picture or drawing,
- iii) the right to handle the patent i.e. the model or design,
- iv) the right to forbid use of the protected invention, model or design in production or in sale to third persons, who have not given his approval.

Protection of the rights for industrial property

The person that violates the right of a registered or protected invention, model, design or mark or that uses illegally the appellation of origin of the product, shall be responsible for the damage in accordance with the general rules for compensation of damage.

The person whose right has been violated may request, besides compensations of the damage, that the person violating his right be forbidden further performance of the activity by which a violation is made and the judgment announcing the violation be published in the newspapers on account of the defendant.

Should subject of violation be a registered or protected invention which refers to a procedure for manufacture of a new material, it shall be considered that any material of the same composition is manufactured according to the protection procedure, unless otherwise proven. The persons producing such a material shall bear the costs for providing proof, but care must be taken for their legal interest regarding the keeping of a production secret.

Agreement for license

The waive of use of a patent, model or design, respectively mark, shall be done by concluding an agreement. The agreement for license must be made in writing.

In case when several persons submit an application for a patent, model or design or in case when the right for patent, model or design is granted to several persons, consent by all persons shall be required for the agreement for license.

The collective mark cannot be subject to a license.

Should the holder of a patent, himself or through someone else, fail to use or insufficiently uses the invention protected by patent in FYROM, the right of use may be granted to another person, with obligation to pay the compensation to the holder of the patent (compulsory license).

Should the patent be used for reaching unjustifiably high prices on the market, or should the use of the invention protected by a patent be in the interest of health, defense, protection and promotion of human environment and nature, or be of particular interest to a specific economic branch, a license may be granted even before the expiration of the term (official license).

5.16. Conclusions

Overview

Despite its peaceful transition to independence from Yugoslavia in 1991, FYROM has faced several obstacles in its transition to a market oriented economy. In particular, FYROM economic transition was beset by a triad of events:

- ❑ the loss of former Yugoslav markets,
- ❑ United Nations sanctions against the Federal Republic of Yugoslavia (FRY-Serbia Montenegro) from 1992 to 1996,
- ❑ and Greece's trade embargo against FYROM, which ended in 1995.

Now that the effects of these external economic shocks have diminished, FYROM is positioned to solidify its macroeconomic stability, to progress with enterprise restructuring and to offer new business opportunities.

The trade embargoes and loss of FRY market were stifling blows to FYROM's economy. Trade volume declined by 40% between 1990 and 1995, and the level of investment in 1995 fell to less than half of 1990 levels. By the 1995, GDP had declined by nearly 30% from 1990 levels.

The government of FYROM embarked on an economic stabilization program to mitigate the effects of the trade embargoes and to create a favourable business climate. The leading goals were: **Macroeconomic Stabilization, Banking Sector Rehabilitation, and Enterprises Restructuring**

Macroeconomic Stabilization: Monetary and Fiscal austerity precipitated a steep decline in inflation and low budget deficit since 1994 (about 1.5% of GDP). In addition, external debts in fairly low for the region about 1.4 billion for the \$3.6 billion economy. The country is reform oriented, with permanent arrangements with the IMF of the World Bank, which are an additional guarantee for macroeconomic stability and the creation of a good entrepreneurial atmosphere. Moreover, favourable debt servicing arrangements were also reached with the Paris club, London Club, IMF, and World Bank, EU, EBRD etc

Despite advances in macroeconomic stabilization, GDP growth has been slow. After several years of economic contraction, FYROM's GDP grew by nearly 1% in 1996 and about 3% in 1997. Industrial output is growing and GDP growth approach 5% in 1998. Further enterprise restructuring and banking sector should help stimulate domestic demand and vitalize FYROM's economic health.

Banking Sector Rehabilitation: The banking sector in FYROM was rehabilitated in 1995, but remains fairly weak. Due to economic difficulties and the old Yugoslav system of politically –based loan decisions, 85% of FYROM's total loan portfolio was non-performing by 1993. By the end of 1997, this rate fell to 22% (about \$155 million). Although this rate is still fairly high, it poses little threat to the economy, as it accounts for only 4% of GDP. These numbers also indicate that few loans are being offered to companies. Increased foreign participation should improve the efficiency of FYROM's banking sector and facilitate decision making on commercial loan applications. Foreign participation should restore the public's confidence in the banking sector and provide additional capital through greater savings deposits.

Enterprise Restructuring: Many uncompetitive firms were closed following the banking sector rehabilitation program's elimination of easily –available bank credit. As a consequence, unemployment now stands at 25% and many firms, in order to stay afloat, have taken on an increasing level of inter-enterprise debt and tax arrears. Competitive firms are now trying to attract Foreign direct Investment and Foreign partners to accelerate restructuring and increase their competitiveness.

Privatization and Foreign Direct Investment: the lack of available domestic capital requires FDI for economic growth and enterprise restructuring. FYROM has privatized 1.125 of its 1.500 state-owned commercial entities to date. The principal privatization method was through buyouts from workers and /or management, which kept most companies controlled by their original managers. In fact, FYROM Privatization Agency claims that 90% of privatization cases received bids only from employees and managers. This privatization process transferred state ownership, but provide little enterprise restructuring or new capital.

FYROM has one of the lowest per capita FDI figures in Central and Eastern Europe (CEE). From 1990 until 1999 FYROM, has attracted approximately \$228,1 million US in FDI, one 3rd of which was from Greece. The leading industries receiving FDI interest are:

Tobacco processing, marble production, mining of lead and zinc, as well as **planned joint ventures in the brewing and soft drink industries**. The United States has one notable joint venture: ICN pharmaceuticals will invest \$24 million in a new factory with the FYROM company Ohis.

Significant foreign investments are anticipated through banking and telecommunications sector privatisation.

FYROM offers the following incentives to attract FDI:

- ❑ National treatment for foreign investors,
- ❑ corporate profit tax rate of 15%,
- ❑ three-year profit tax exemptions (minimum 20% capital participation),
- ❑ additional profit tax exemptions for reinvested profits, no restrictions on quantity of foreign entity equity holding, no industry sector restrictions, and two year exemptions for reinvested profits, no restrictions on quantity of foreign entity equity holdings, no industry sector restrictions,
- ❑ and two - year exemptions on employer contributions to the state for new employees. However, there is a 10% tax placed on profits transferred out of the country or to a non-residential account inside the country, and foreign ownership of urban land is not yet allowed. Future legislation will continue on a trend that is increasingly more favourable to foreign commercial participation.

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External Political Factors

There is no question that the uncertain environment in neighbouring countries in the Balkans that one reads about in the press daily, hears on the radio or watches on the television news shows, gives potential investors in FYROM cause for concern.

Legal and Administrative Infrastructure

FYROM is adjusting its political and legal systems, and is still evolving structures, procedures and modalities for conducting private business. Under the old systems everything was proscribed unless explicitly allowed, now everything is permitted that is not specifically prohibited by law. Consequently, it is taking time to draft and enact legislation covering all the areas required by an open society and free market economy.

There are, however, still complaints and concerns about, for example: lack of a full complement of laws and regulations governing business (missing companies law, public enterprises act, uniform commercial code, movable property for security (collateral) law, bankruptcy law, environmental laws and regulations, denationalization and restitution laws, anti-monopoly law), lack of reliable statistical data and market information, no organized market for trading securities, ambivalence towards some government institutions, difficulties in acquiring title to real estate (land), courts deficient in enforcing claims of creditors, police abuse of discovery proceedings, insufficient social policy (safety net), inadequate scope of the current privatization program (as regards agriculture, financial institutions, public utilities), unenthusiastic public support for privatization and some suspicion of the process, and imperfections in the system, such as cronyism.

Domestic Economic Environment

FYROM has made major strides in stabilizing and restructuring the economy. Nevertheless, complaints still are voiced over the following areas: high unemployment, high deficits, large “grey economy” or off-the-books economy (tax evasion, customs duties evasion – legitimate businesses obeying rules and laws say they cannot compete), interrupted trade routes to north and south (increased costs of raw materials, spare parts, finished goods, uneven flows of supplies), over dimensioned “large companies” burden the economy (too high head counts, too many facilities), small domestic market, high tax burden, company data insufficient, inadequate and unreliable (lack of published balance sheets) etc.

Financial Sector

Financial institutions are in the process of being restructured, banks are now being inspected regularly, there are strict requirements to open and operate new banks, and interest rates have been falling.

Nevertheless, problems persist to varying degrees: a number of bank failures and a large number of non-performing loans evidence the need for restructuring and rehabilitation, inadequate credit facilities and tight official monetary policy lead to high borrowing costs, which are accompanied by burdensome security requirements; bureaucratic and unimaginative banks are slow to meet the needs of the new breed of customers; there is general distrust of banks by the populace (large amounts of “mattress/pillow money,” many transactions are required in cash and there is almost no use of consumer credit); and, there is a large amount in frozen foreign currency accounts (one billion dollars).

On a positive note, the flow of remittances from immigrant country citizens is significant and helps support the balance of payments.

Practices in Business and Government

Orientation to the customer is hard to learn and harder still to practice. This is true at all levels of society and business in FYROM. The other concepts that are hard to understand are that cash is king, that cost does not determine price, and that engineering and manufacturing a product does not mean it meets the needs of customers. These notions are beginning to penetrate and where they do appear, it is very noticeable.

The way business is conducted in FYROM does not always meet the high standards of most Western countries, though they are far ahead of most former East Bloc countries. Nevertheless, one should be aware that there are problems in observing payment terms both in the public and private sectors (overdue payables, late payrolls, delayed pensions, etc); tax collection suffers due to evasion by citizens and legitimate businesses alike, not to mention the gray economy which evades contact with the official economy; and finally, although the necessity for contacts and connections is not untypical, the emergence of graft and corruption is receiving close Government attention.

Complaints are voiced about frequently changing customs regulations, excessive paperwork and inept procedures, antiquated and inefficient equipment and facilities, “old style” thinking and behavior of customs officials, rampant smuggling, and high customs costs (40% and more). Some businessmen wishing to register their investment contracts and others who must register their operations with the authorities have experienced formidable bureaucracy and time delays. It is not unusual for the process to take several months, although foreigners are supposed to receive priority attention. High costs and delays in obtaining phone lines are also sometimes experienced.

Decision making is not as straight forward and expeditious as many Westerners may wish. Investors should be prepared for some degree of frustration. The process is either a legacy of the old socialist system where nobody wanted to stand out for taking responsibility or the Balkan/Eastern propensity to arrive at the main points in a convoluted fashion after protracted discussion on unrelated matters.

Resourceful and Adaptable People

The country was never fully communist or even completely socialist. There was no command system or all-pervasive central economic planning, though some decisions were occasionally politically motivated. Enterprises devised their own plans and were not penalized for not fulfilling them. FYROM was more entrepreneurial than even some of its sister republics of former Yugoslavia and certainly more than most of the ex-East Bloc countries. Businesses operated close to western models as to profit orientation and all operating functions were grouped under one company's control. (The Soviet model had separate companies for manufacturing, sales and procurement). Trade and technology were directed both eastwards and westwards. Still, social capital enterprises are learning to drop the former emphasis on employment and wages which led to insufficient investment and even losses.

The people are surviving successfully in spite of the sanctions and embargoes. They have established new trade routes. Even during the last years of the Socialist Federal Republic of Yugoslavia a few entrepreneurs opened their own businesses, which has turned into a flood since independence. The vibrant private sector is creating new wealth and employment opportunities, albeit still for a limited section of the population. The people are well educated, many are trained in the use of computers and modern business methods, and many speak foreign languages. It is not hard to find many qualified candidates for job openings.

Many believe that FYROM is much better off and better positioned than its former socialist neighbors to reap the benefits of an open society and market economy. This is not to say that certain segments of the population still need to be convinced of the benefits of the new systems, which take time to show broad results.

Infrastructure Highly Developed

The country has a well developed communications network: telephone, telefax, telegraph, telex, post and internet. However, more investment is needed to improve technology, and to add capacity and lines. A new capital investment program has just been announced by MPT to address these shortfalls.

The transportation system is good: two international airports, paved and well marked highways, and extensive railroads. New and improved road and rail links along the east-west corridor are planned or already under construction. There are good inter-city bus connections and the cities have good public transport. There is an ample number of taxis.

Main factors that make FYROM attractive to foreign investors

The main factors that make FYROM attractive to foreign investments are the following: (a) Its good strategic position –it is located in the middle of Balkans, (b) it is a cross road of many roads and it's a beginning spot for the penetration of Foreign investment into the wider region, (d) The country has a cheap and well trained labor and (e) the country has a good and well organized infrastructure.

**PART C. GREEK INVESTMENTS IN BULGARIA
AND FYROM – CASE STUDY**

6. GREEK INVESTMENTS IN BULGARIA AND FYROM

6.1. Greek Business Activities in the Balkan region

6.1.1. Regional economic co-operation in the Balkan region

The transition of most of the Balkan countries to market economies opened a new era of collaboration and of mutually beneficial economic relations between the countries of the Balkan region. Greece in particular, contributed to the re-establishment of its historical economic and trade relationships with these countries and especially with Bulgaria and FYROM, which during the post war period had experienced a significant shrinkage in relative terms.

Although armed conflicts, political differences, and internal economic imbalances did not allow the development of economic relations with all countries of the area, significant achievements can be noticed during the period 1990-2000 in the fields of trade, investment, labor mobility and technological cooperation. The improvement of Greece's relations with FYROM and Bulgaria lead also to a significant intensification of economic cooperation with these countries.

Greece became one of the biggest investors in the Balkan region specifically in the countries that gradually built market economies. Despite political upheavals, economic problems and the lack of a clear legal framework in doing business, increasing numbers of Greek companies have moved into the region. They are attracted by the size of the market-about 50 million people compared with 10 million in Greece and by the potential growth over the next decade. The low-inflation, high growth pattern of today's Greek economy provides a solid base from which it can reach out to foreign partners and markets.

A large number of Greek enterprises expanded to neighboring countries through Foreign Direct Investment (FDI) and /or participation in the large infrastructure projects. The majority of these investment initiatives is concentrated in the fields of trade, services, finance and to some extent, also in manufacturing. A small number of foreign enterprises established in Greece and a range of Greek – owned companies created affiliates in different countries, including Bulgaria, Romania, Albania and FYROM.

This process of physical integration between the economies of the Balkan area will be largely reinforced as non-economic problems subsided. A new spectrum of opportunities is appearing, extending from Greece to other Balkans countries. All these countries have strong historical economic ties that, in combination with new initiatives, can generate multiple benefits for all participants.

In order to enhance the prospects of economic development and cooperation with regard to the Balkan area, the Greek government initiated a number of supporting policies.

6.1.2. Greek government supporting policies in the Balkan region

6.1.2.1. General principles of Greek foreign policy in the Balkans

Greece's policy in the Balkans is guided by the principles of maintenance stability, peace and security as well as of the full respect of human rights, including those relating to minorities. The inviolability of the international recognized borders, in accordance with the relevant U.N and OSCE principles, remains one of the cornerstones of Greece's foreign policy.

To serve these goals, Greece supports the establishment of good neighborly relations and the development of close economic ties among all Balkan countries. This is particularly important to

Greece which, during the communist era had limited relations with its northern neighbors, with whom it had maintained for centuries close cultural and economic ties. It will also further promote economic development and stability in the region.

The resolution of the Yugoslav crisis, for which Greece made and is continuing to make intensive efforts, will further increase economic ties among all Balkan countries. This cooperation has been a leading goal of Greek foreign policy since 1976, when the first meeting of the parties concerned was convened in Athens upon Greece's initiative.

The systematic cooperation of Greece with the Balkans countries contributes also to the long term goals of their economic and political re-approchement with Europe and other international institutions. The realization of important infrastructure projects of Balkan –wide importance, such as in the transport, energy, and telecommunication field remains among Greece's high priorities.

Greek investment and trade exchanges with its Balkan neighbors have recently increased. Today, Greece is the third largest investor in Bulgaria and the fourth one in FYROM.

Greek Bulgarian Relations

Greek Bulgarian relations have developed steadily in all fields during the past years. Economic and commercial cooperation showed very positive results for both countries and a number of agreements have been concluded.

Among the agreements signed one should mention the Agreement concerning the Nestos river and the Agreement on the opening of the three new border crossing points, in addition to the two existing ones. This is expected to lead to a further increase in visits and trade from both sides.

Other agreements signed include those on the seasonal employment of labor force, on the readmission of illegal immigrants, as well as a Protocol on police cooperation.

A large number of Greek firms is active in Bulgaria, having invested in many sectors of the economy, thus placing Greece the 4th largest investor in Bulgaria representing 10% of foreign capital investment there.

Greek FYROM Relations

On September 13, 1995 an interim agreement was signed in New York between Greece and FYROM, with a view to normalizing Greek-FYROM relations and particularly facilitating the movement of persons and goods. In addition, two Memoranda on Practical Measures and on the Mutual Establishment of Liaison Offices were also concluded. Following this Accord, a new round of talks was initiated under the auspices of the Special Representative of the UN with a view to solving the remaining important difference over FYROM's name.

Recognizing the existence of a legitimate difference over the new country's name the UN Security Council adopted in 1993 Resolution 817, by which it accepted FYROM in the UN under the provisional name of the Former Yugoslav Republic of Macedonia (FYROM).

Greece, convinced that a solution of the difference over the name will further enhance stability in the region and will positively contribute to the promotion of the good neighborly relations, actively participates in the talks for a solution under United Nations auspices.

Parallel to the negotiations for the resolution of the name issue, Greek authorities have inaugurated various bilateral contacts to facilitate economic cooperation between the two countries and to reinforce FYROM's transition to a market economy.

Greece takes the lead in the Balkan region

Greece deserves a leading role in the political and economic reconstruction of the Balkans. Many countries including the USA, Czech Republic, Italy, Russia, Turkey, France, United Kingdom, Germany and Canada, have sought bilateral cooperation with Greece to implement other Balkan initiatives.

Faced with this challenge, Greece has created a comprehensive regional strategy, the so called “**Total Balkan Approach**” which is pursuing a foreign strategy aimed at creating greater regional stability, democracy, security, prosperity and development in the Balkan region. The objectives are to control potential sources of conflict, and to create the prerequisites for political and financial developments. The ultimate goal is regional integration of the Balkan countries into European Institutions. This strategy is founded upon the principles of respect for sovereignty and territorial integrity, respect of existing borders, and the dissuasion of separatist tendencies and divisive ideologies

Greece mobilizes to aid Balkan region

The recent decision of the government, to base Balkan reconstruction agency for South East Europe, in Thessaloniki, is yet another step in further upgrading Greece role in the greater Balkan region (especially the upgrading role of the second capital of Greece, Thessaloniki in the development of the Balkan region by designed headquarters of both the agency for the reconstruction of South East Europe and the Balkan Stability Pact).

New credit lines that are scheduled to commence in the region are expected to transform northern Greece into a center where auxiliary organizations and private sector firms will be based in order to penetrate the Balkans.

Recently, Greek government presented its own five-year “National Balkan Reconstruction Plan 2000-2004” **worth 100 billion drachmas**. This action plan includes Albania, FYROM, Bulgaria, Romania, the Yugoslav province of Kosovo, and is projected to fund major infrastructure projects, particularly in the transport sector, communications and energy.

Significant outlays will also be allocated for health care, education and investments, in trade and industry. Athens’ Balkans reconstruction plan is projected to function alongside with other credit lines and initiatives for the area, the OECD’s DAC development aid, PHARE, the SECI initiative for South East Europe and the special World Bank funds expected to be established for the development of the Balkans.

Reconstruction through Multilateral investments

Greece is increasing its investments in value added activities in the Balkans, and Building the energy, transportation and telecommunications infrastructure needed to fully integrate into the European Union. Some examples:

- Construction will soon begin on the \$1 billion **Burgas-Alexandroupolis** pipeline, allowing Caspian Sea oil to bypass the heavily trafficked Bosphorus Straits by creating an overland route through Bulgaria and northern Greece.
- Greece seeks to extend the existing **trans-Balkan natural gas** pipeline from Russia to include Albania and FYROM.
- **Telecommunication axes** such as Kavala-Haskovo, Thessaloniki-Sofia and Bulgaria’s linkup with the Black Sea optical fiber network.

- The construction of **EGANTIA Highway** is being built across northern Greece, from the Turkish border to the Ionian Sea, as well as the vertical routes connecting North-South parts of the Balkans which will also connect major cities in Albania, Bulgaria, and FYROM, will greatly contribute to economic development and regional integration
- The **National Bank of Greece**, with branches and subsidiaries in Albania, Bulgaria and Romania, as well as a foreign partner in the biggest bank of FYROM Stopanska Bank, is poised to become one of the most influential lending institutions in Balkans.
- Nowadays numerous infrastructure projects are undertaken in Northern Greece, enhancing regional and Trans frontier cooperation among Balkans countries.
- Modernization works in a number of ports and airports, as well as improvement of telecommunications networks in Northern Greece are expected to facilitate trade and communications in the Balkan regional market.

Greek strategies in the Balkan and the Eastern Mediterranean region - driven largely by the private sector but increasingly supported by government policies and public opinion in the past five years - have improved Athens' prospects as the region's leader in growth and economic prosperity.

6.1.2.2. Greece creates incentives for Balkan region

Creation of incentives

During the last years, a broader spectrum of actions has been undertaken to support outward-looking initiatives of enterprises. Incentives for new business plans, networking, vocational training programs for employees, entrepreneurs etc, commercial agreement with neighboring countries, and the creation of a Stock Exchange Office in Thessaloniki, are some of the most important examples.

The new law on "venture capital" is expected to assist enterprises to participate in business initiatives to the Balkan countries.

Human Resources

The prospects of growth, employment and welfare of the Balkan countries demands not only transfer of capital but also managerial skills, training in new technologies and promotion of scientific exchange programs.

During all these years, Greece has provided to hundreds of thousands of immigrants from Balkan countries the opportunity to be employed, thus, contributing to the efforts of reconstruction of these countries, to the alleviation of significant social problems, and to the overall, stabilization of their economies.

The Greek government also strongly supports exchange programs that promote scientific cooperation, management training and joint development of technology.

Stable macro-economic environment

Economic cooperation among Balkan countries requires the attainment of a relatively stable macro-economic environment in all countries, without extreme uncertainties. Increasing the degree of tax harmonization, developing a compatible financial system, and avoiding monetary surprises are steps towards this goal. Joint activity in the banking sector, information exchange by Central Banks and economic policy – makers, and a deeper knowledge of each others economies will help achieve a level of mutual understanding and cooperation among economic authorities.

The aim of European Union is to integrate energy, transport and telecommunication infrastructure into Trans-European Networks by the year 2010. Greece, the only member-state of the European Union in the Balkans region, fully supports and participates in the implementation of these policies and will do its best to ensure their extension to, and utilization by the Balkan countries.

The Trans-European Transport Networks include the construction and modernization of major routes connecting Greece and Balkan countries with Central and South – Eastern Europe. The construction of EGNATIA route, will provide new impetus to regional development and economic integration.

Finally, the Trans-European Transport Networks (TENS) for telecommunications will improve speed, reliability, and availability of communications. They will also allow the introduction of new services, thus helping the countries to adjust to the requirements of the Information Society. Coordination between Telecommunications Organizations of Balkan countries has already started.

6.1.3. Greek investments in the Balkan region

The launch of the **Balkan Stability Pact**, is expected to reduce the political risks of doing business in the Balkans. Greek companies are keen to see the international community participate in rebuilding the region, and organizations such as IMF are giving lead with broader financial support.

Western pressure for the removal of tariff barriers across the region will result in bigger trade flows. Almost 20% of Greek trade is with the Balkan countries, and this percentage is projected to increase, as recovery gets underway in regional economies that have been affected by the Kosovo conflict. In the longer term, these commercial ties will have been further by the EU accession talks of several Balkan states, which Greece has championed within EU.

The total Greek investment in the region is estimated at about \$3 billion US. This figure reflects small investments by over 3.500 flourishing Greek firms established to promote cross-border trade, including retailing and distribution operations, as well as more substantial amounts spent on acquiring and modernizing manufacturing. Greece's biggest banks all have operations across the region.

The biggest single investments have been made by O.T.E Greece's public Telecoms operator which aims to become the region's leading operator of both fixed wire and mobile services. **Telecommunications** will remain the leading sector, with OTE committed to bidding for equity stakes in the Albanian and FYROM fixed-line operators when they are offered for privatization

Greek investment in the Balkan is projected to increase rapidly as stability improves (by **Balkan Stability Pact**) and companies extend their activities across the region.

But Greek **manufacturing companies** are expected to lead the investment drive as they seek to lower costs and expand their markets. The strategic aim of the bigger Greek companies is to become **Key Regional Players** in specific sectors.

Greece is also expected to become the leading provider or **financial services** as Greek-owned banks expand their branch networks and offer new products to small and medium-sized businesses and retail clients.

Beyond the food and clothing sector, Greek business interests have also invested in transports, chemicals, communications, and consulting services, of late, via the PHARE programs.

Greece accounts for more than half of total Balkan productivity. Over 70% of foreign businesses active in the Balkans today are based in Greece, particularly in Athens and in Thessaloniki.

For the Balkans countries, Greece represents the most important market in the Balkan area, thus contributing to the efforts of the transition economies for the restructuring and stabilization of their economies.

6.1.3.1. Tools of finance

It would be inconceivable, for any serious trade and economic development activity to blossom without the direct support and services offered by major credit institutions, something that has made the ever-increasing presence of Greek companies indispensable.

The foremost problems faced by a Greek Small Medium Enterprise (SME) entrepreneur in the Balkan region are the following:

- the excessive initial costs incurred for travel and local support,.
- crime, and corruption,
- the compatibility of promoted products in the local markets,
- poor infrastructure,
- concerns that deal directly with a firm's entrance into a country's market and the way "investment risk" will be divided.

Conversely, the primary credit tool employed to support SMEs in their seminal steps amid new SE European markets were the **PHARE-TACIS "JOP PROGRAM"**, funded the formation of **Joint Ventures** by financing trips to further contacts and to find local partners, as well as the investment plan's feasibility studies and the investment itself.

Venture capital funds, such as Balkan Fund and Commercial Capital, are also available for prospective investors, or through international credit institutions. Businesses can also vary on the experience from "one-stop-shops" and "Info Centers" in Greece especially set up to offer investors information on Balkan countries, their business environment and internal markets. The collection and provision of relative information for the development of cross-border cooperation, the operation of data banks, promotion of Greek firms for the expansion of activities in neighboring countries and the specialized support for such SMEs are some of the actions that are already being implemented by such info centers such as DIPEK in Thessaloniki, in part by local chambers.

Similar actions are forecasted in the actions plans of industrial reorganization bureaus. Finally, relevant services are envisioned by SME support centers expected to operate in border areas with INTERREG II subsidization, offering technical assistance to Greek firms that want to develop activities in neighboring countries.

6.1.3.2. Areas of economic activity in the Balkans and Greek presence

In the course of rebuilding the Balkans, there are four key areas on which international investors will focus their interest, and these are:

- **Telecommunications**
- **Mining (cement- metals)**
- **Networks, infrastructure, construction**
- **Energy**

In all these four areas of activity, as well as in banking, food supply, textiles and individual manufacturing sectors, Greek enterprises have a very important part to play, while several Greek companies have plans for investment.

- **Telecommunications**

This sector will be the powerhouse of developments in the region with OTE as one of its foremost figures. The amount of capital OTE plans to invest in the Balkans approaches \$2.5 billion, of which \$1.075 billion have already been invested in Romania and Yugoslavia. These investments form part of OTE's long-term strategy, through which it is planning to become a major regional player through a series of acquisitions and to eventually control a homogeneous market of 70 million people OTE's interests in local telecom organizations in each country are as follows:

- ◆ **BULGARIA** - in a joint venture with the Dutch company KPN and Hellas Telecom OTE has made a majority share (51%) of the Bulgaria phone company BTK, as well as for a second license for a mobile phone network. The total cost of the package is expected to be somewhere in the region of \$600 million U.S.
- ◆ **FYROM** – In this case, OTE has responded to an invitation from the FYROM government to purchase a majority share of the state telecom company for approximately \$300 billion, with negotiations still in progress.

The private enterprise **INTRACOM group** (telecommunications, information technology and games of chance) has established a strong presence in the Balkan region through investments reaching \$32 million. It possesses a network of subsidiaries and mixed joint ventures in Romania, Serbia, Albania, FYROM and Moldova, while its presence is particularly strong in Bulgaria with Bulfon, where it is creating a cell-phone network, a card-phone network and an optic fibre network. Through its gaming subsidiary Intralot, the group also owns a group of subsidiary companies running lotteries etc. These are: Stigmieo Laheio (51%), Yogolot (100%), Bilot (65%), Loteria Moldavei (30%) and the Ukrainian Nika (40%). It also plans to set up a Balkan Lotto. An up-and-coming player, meanwhile, which has already developed significant activity and more promises, is OTE's subsidiary Hellas com.

- **Mining (cements and metals)**

TITAN

As one of the two protagonists of the cement industry within Greece, Titan began its international career in the US, where it owns a private plant in Virginia with a production capacity of one million tones a year. It went on to establish a distribution network in Western Europe and is now focusing on the Balkans. The Titan group own seven cement-production units, with a total capacity of nine million tones (Greece, US, Bulgaria, FYROM) and eight distribution stations in the US, Italy, France, Spain, United Kingdom, Egypt.

Total turnover for the group came to 159.8 billion drachmas, while that of the parent company was 102.6 billion drachmas. The overall net profits came to 24.5 billion drachmas while those of the parent company were 19.9 billion drachmas. During 1998, the Titan group invested heavily in fixed installations and acquisitions worth 18.5 billion drachmas in Greece and abroad, as part of its strategy to become a major regional cement producer and supplier.

Among these investments was the purchase of production units in Bulgaria and FYROM for \$48.3 million. Specifically, Titan bought 83 % of Plevenski Cement in Bulgaria, which has a 17 % share of the Bulgarian market and produces up to 360.000 tones cement a year. In FYROM, meanwhile, a joint venture by Titan and Holderbank, TITAN bought 84% of the Cementarnica USJE plant, with each partner getting a 42% share. This is the only cement plant in the republic, with a production capacity of one million tones a year. Titan is pressing ahead with its plans for expansion, and now

intends to acquire a cement plant in Egypt in partnership with French cement-producer Lafarge, while it has also declared an interested in the Serb cement producer Kosjeric.

AGET HRACLES

Titan's alter ego in the Greek cement market as regards size, the AGET Hracles group notched an overall turnover of 158.1 billion drachmas in 1998, with the turnover of the parent company coming to 105.6 billion drachmas. The group's net pre-tax profits in that year came to 24.371 billion drachmas, while those of the parent company were 20.8 billion drachmas. AGET Heracles sold 3.56 million tones cement in Greece and 2.87 million tones abroad (EU, US, West Africa). The group is carrying out an investment program worth \$15 million in Albania, in collaboration with Lafarge and a local company, K.A. Holding. It has already signed an agreement with the Albanian government to bring an old cement factory in the Vlore region back on line and to run it. Part of this proposal includes the construction and operation of a cement supply depot in the same area.

MYTILINAIOS GROYP

The main activity of this group of companies is trading in metals, such as iron alloys (steel, wire and cable), other metals (copper, lead, mercury and aluminum) and unprocessed ores. It buys these from suppliers abroad and then sells them to clients within Greece and in international markets.

The group has invested \$32 million in mines in Romania, FYROM and Yugoslavia, with which it has signed long-term association agreements worth \$1.5 billion. The most significant feature of these agreements is that the companies involved need the funds provided under the terms of the agreement in order to continue operating. On the basis of these contracts, which go beyond simple trade agreements, Mytilinaios provides the companies in the partnership with floating capital, machinery and raw materials in return for finished products of the same value, based on metal prices at the London Metal Exchange (LME).

To date, Mytilinaios Holdings has signed such agreements with the RTB Bor complex in Serbia, one of the largest copper-mining and processing plants in Eastern Europe, the RMHK Trepca lead and mercury mines in Kosovo and the SASA lead and mercury mines in FYROM. The group has also signed an agreement with one of the most modern steelworks of eastern Europe, DUNAFER in Hungary, which manufactures quality products made to high specifications (large steel rings). This agreement, which was signed in July 1998, is for five years and worth \$150 million. It makes Mytilinaios the exclusive supplier of Dunafer products in Balkan countries and Egypt, without excluding the option of selling the same products to third countries.

Finally, the acquisition of 60.44% of the Sometra SA foundry in Romania upgrades Mytilinaios into a major regional player in the metal trade. The group won a tender for the privatization of the Romanian mercury and lead industry, buying 60.44% of Sometra SA from the State Ownership Fund. The sole financial consultant for this deal was the Bucharest investment Group, subsidiary of Alpha Finance.

ALUMIL MYLONAS

The Greek company ALUMIL MYLONAS, which produces finished aluminum products, estimates that its exports will increase by 50% in 1999 and reach 9 billion drachmas, with an estimated turnover during 1999 of 25.1 billion drachmas. These exports are: to Romania, Bulgaria, Egypt, Germany, Poland, Hungary, Slovakia, the Czech Republic, Cyprus, Spain, the Ukraine and Armenia.

The company is completing the construction of an aluminum factory in Bucharest, with a total budget of \$10 million (\$2.5 million in the initial phase) where raw materials imported from Greece will be processed. At these installations, the company will have storage areas that will serve the region as a whole, while it is also commercially active in Bulgaria.

BIOHALKO GROUP

Mindful of the business risk, the company has only set up one production unit in the Balkans, which is situated in Bulgaria. This is the Steel met plant and storage facility in Sofia.

Other sectors of industry

PLASTICS

The plastics sector, which employs 5% of the Greek workforce, is also active in Romania via the Petzetakis plastics firm, which has invested \$3.5 million, and Cretan Plastics, which are the third largest plastic producer in Greece. Cretan Plastics exports 55% of its production as master batches (raw materials for plastics). It has a 51% in Romcolor 2000 SA (founded in 1994), and since April 1997 Romcolor has produced master batches for the local market and for other countries of Eastern Europe, while a 400 million drachma investment plan is in progress for its expansion in 1999-2000.

PAPER

Thrace Paper Mills has made a \$6.4 million investment to buy the Belovo paper mill in Bulgaria.

PACKAGING

The Mailis group, which is one of Europe's leaders in the production of materials for secondary packaging, has a plant in Romania. The size of the investment comes to \$2.7 million, while it also a retail outlet in Bulgaria

FOODS STUFFS, SUPERMARKETS, DISTRIBUTION CHAINS

In the Balkan region the Greek companies appears to be dominated by its food industry, particularly 3E, DELTA, Chipita, Athens Breweries, Goody's Nikas, the Agiou Georgiou and Louis flour mills and the supermarket chains Veropoulos, Trofo and others.

HELLENIC BOTTLING COMPANY (3E)

The Hellenic Bottling Company (3E), which is the fifth-largest Coca-Cola bottling company in the world, has invested \$177 million for the purchase and construction of production units in Yugoslavia, FYROM, Bulgaria and Romania. In 1998 the company produced grouped pre-tax profits of 43.5 billion drachmas (a 6.5 % increase relative to 1997). 3E and Athens Breweries have jointly signed a deal with AD Pivara Skopje, whose products have the largest share of the FYROM market, acquiring 51% of this company. Pivara is the local agent for "The Coca Cola Company", producing and distributing soft drinks (Coca-cola, Fanta, Sprite), as well as the beers Scopko and Star Lisec.

DELTA HOLDING S.A

The Delta group (20 per cent of which belongs to the French company Danone) has ice-cream factories in Bulgaria, Serbia and Romania and has invested a total of \$50 million in the area. Within 1999 it aims to increase its distribution network by 50 per cent by investing in new facilities (freezers, trucks) worth 2.5 billion drachmas.

The group has six factories in Greece (milk and fruit juices, yogurt, ice-cream, two frozen food factories and one animal feed factory) as well as eight milk collection and processing centers. Delta has established a presence in eight countries (Greece, Bulgaria, Romania, Serbia, Skopje,

Cyprus, Lebanon and Italy) and produces 160 different product lines. At present, it has 30.000 sales points in Greece and 25.000 abroad. Outlining the performance of Delta Holding for 1999, managing director Dimitris Daskalopoulos predicted sales of over 125 billion drachmas and profits of more than six billion drachmas. Equity capital will come to 66 billion drachmas, fixed assets to 2.3 billion drachmas and its participation in subsidiary companies to 64 billion drachmas.

CHIPITA

This company, which recently increased its share capital by 12 billion drachmas, has made a strategic alliance with Delta in the countries of eastern Europe, with the assistance of Global Finance. For 1999, Chipita will focus on expansion into eastern Europe, with packaged croissants as its flagship product. Chipita spent \$15.5 million to buy a production base in Bulgaria, and a further \$23 million to buy the Star Foods factories in Romania and Poland. Because of the current economic crisis, the company has a limited commercial presence in the Ukraine and Russia. Chipita Bulgaria (in Sofia) is the most profitable unit of the group, since in the space of two years it has gained a 60 per cent share of the local market with 1998 sales reaching \$8 million.

Sales in Poland reached \$10 million (Star Foods) and in Romania \$7 million (Star Foods). Chipita's profits in 1998 increased overall by 58%, reaching 3.2 billion drachmas, while sales increased by 31 per cent reaching 35 billion drachmas. For 1999 the company predicts an increase in sales of 30% and an increase in profits of 40-45%

The alliance with Delta, which is also very active in Eastern Europe, aims to achieve scale economies, capitalize on Delta's large distribution network and help both companies gain greater leverage with local authorities in the region. Delta participates in Chipita's international activities in Eastern Europe through the purchase of 15% of Chipita Bulgaria and 15 per cent of the packaged croissants sections of Star Foods Poland and Star Foods Romania, both Chipita interests. At the same time, Delta has the option to participate in any future expansion by Chipita world wide, with a minimum percentage of 15%.

Other food industries

Another active player in the Balkan food market is Nikas, with two factories in Sofia and Skopje respectively, and the Greek fast food chain Goody's, which has two outlets in Sofia (Fast Foods), and is due to open another in Plovdiv, Bulgaria. Goody's Sofia outlet had a turnover of 500 million drachmas in 1998.

Ice cream manufacturer EVGA, of the Philippos group, and chocolate producer ION SA are also commercially present in the region, as is the pasta brand Melissa, which notched 15 billion drachmas turnover in 1998 and exports 20 per cent of its total sales volume to central and Eastern Europe.

SUPER MARKET CHAINS

Veropoulos Bros has opened two supermarkets in Skopje (FYROM), investing \$6.5 million. The Trofo cash-and-carry group is due to open its first foreign outlet in Sofia in mid-June, in an building of 2.000 square meters. The Trofo group (75 billion drachmas sales in 1999) has 44 outlets in Greece, while its wholesale subsidiary ENA SA (40 billion drachmas sales in 1999) has 11 cash-and carry outlets.

FLOUR MILLS

The jointly owned Loulis and Agios Georgios flour mills have invested a total \$16.1 million in Romania to buy out local bread manufacturer Titan and found a production unit.

GLOBAL FINANCE-CREATION OF NEW FUND

The investment organization Global Finance has established four venture capital funds, worth 50 billion drachmas. The company, after the resounding success of the Euromerchant Balkan Fund (EBF), established the \$62 million Black Sea Fund (BSF) in order to support business activities by Greek companies in the Balkans and greater Black Sea region. The capital comes from major international organizations, such as the European Bank for Reconstruction and Development (EBRD) and the International Finance Organization (IFC), the World Bank and a select group of top-notch Greek businesses, including the Latsis group, Alico, Ergobank, shipping tycoon V. Konstantakopoulos etc. Most of these investors had also participated in the Euro Merchant Balkan Fund.

The BSF will invest in the above-mentioned areas by participating, usually with a minority holding, in private-sector businesses. The presence of Global Finance in Bulgaria and Romania, as well as its expansion to the countries of the Black Sea, will aid this effort.

6.1.3.3. Ten major Greek investors in the Balkan countries

Greece is rapidly emerging as a key source of Foreign Direct Investment (F.D.I) in the Balkans, as the region emerges from the political difficulties of the past decade, and begins to focus on economic growth within a market economy. A market of some 50 million people could become a potentially major outlet and investment opportunity for Greek companies, who are expanding rapidly into this region.

The total amount invested by Greek interests in the Balkans is estimated at approximately \$3 billion USD an amount spread between 3.500 businesses. Of these, about 1.000 figure most prominently, with the Hellenic Telecommunications Organization (O.T.E) in the lead. Apart from telecommunications Greek enterprises are also strongly involved in the production of consumer and industrial goods, raw materials, commerce and banking and they play an important role in local communities.

In 1998, Greek exports as a whole totaled \$10.6 billion of which 12.7 %(\$1.38 billion) went to the Balkan countries. Conversely, of a total of \$ 26.2 billion—worth of imports to Greece, 3.1% (\$800,7 million) came from Balkan countries. The total volume of Greece's foreign trade for 1998 came to \$36.8 billion, out of which 5.8 % (\$2.14 billion) represented trade within the Balkans.

Greek exports to Balkan countries (with the exception of Turkey) increased by 3.4 times in 1992-1997, and imports by 2.7 times. In the period 1992-1996, the positive balance of trade for Greece has increased by a factor of six, creating a surplus of \$546.2 million in 1996, up from \$71.1 million in 1992.

The ten major Greek investors in the Balkan countries are the following:

1. **O.T.E:** The Greek public Telecom operator has acquired equity stakes in state Telecom operators in Serbia and Romania and has agreed an acquisition in Bulgaria. It also plans to bid for strategic stakes being offered in the Albania and F.Y.R.O.M telecom.
2. **HELLENIC BOTTLING COMPANY:** Greece's Coca Cola franchise holder bottles in Bulgaria, Romania, Serbia, Moldova and the F.Y.R.O.M.
3. **HELLENIC PETROLEUM:** the state –controlled oil refining group has acquired a controlling stake in Okta, the state oil refinery in FYROM. In partnership with Metro–Etep, it is building a pipeline linking Thessaloniki and Skopje, the FYROM capital.

4. **NATIONAL BANK OF GREECE:** the country's biggest banking group has set up networks in Albania, Bulgaria, and Romania and has acquired Stopanska Banka, the biggest Bank in F.Y.R.O.M.
5. **ALHA CREDIT BANK:** Greece's biggest private banking group has set up a subsidiary in Romania-Banca Bucuresti - and has acquired Creditna Banka, the leading private bank in FYROM. It controls a branch in Bulgaria through a Greek subsidiary, Ionian Bank, and has launched a branch network in Albania.
6. **TITAN CEMENT:** Greece's second-biggest cement producer has acquired a majority stake in Plevenski Cement, a Bulgarian Producer. In partnership with Holderbank of Switzerland, the world's biggest cement producer, it has acquired a majority stake in Usje, a FYROM cement producer.
7. **MYTILINEOS:** the metals-trading group has acquired Sometra, a Romanian metallurgical processor and is negotiating to buy a state owned lead and zinc smelter at Veles in FYROM. It has long-term trading contracts with Bor, the Serbian state - owned copper producer, with Trpca, the Kosovo lead and zinc producer, and with Sasa, a FYROM lead and zinc producer.
8. **ATHENIAN BREWERIES:** the Greek affiliate of Heineken, Europe's biggest brewer, controls two breweries in Bulgaria through **joint ventures** with Greece's Leventis Group. It also has a majority stakes in Privara Skopje, a FYROM brewer and soft drinks producer, in partnership with Hellenic Bottling Company.
9. **DELTA DAIRY:** Greece's biggest dairy producer has set up a **joint venture** to produce ice cream in Bulgaria, with the European Bank for Reconstruction and Development (EBRD) as a partner. It has also set up **joint venture** with local partners to produce ice cream in Romania and Serbia.
10. **CHIPITA:** the snacks manufacturer has set up a subsidiary in Bulgaria making packaged croissants for sale on the local market and for export in the Balkan and Black Sea region. Another subsidiary in Romania produces packaged croissants and salty snacks.

6.2. Greek Investments in Bulgaria

With an overall FDI investment of \$328 million (from 1991 until 2000), Greece - based companies are the fourth largest investors in Bulgaria, representing 10% of foreign capital invested there.

Out of total of 1.000 Greek businesses that have ventured there 450 are currently doing business in telecommunications, trade, food stuffs, beer, clothing and footwear, medical and hospital supplies, elastics, plastics, chemical products, steel products, energy, transport, services and tourism.

Bilateral trade transactions in 1997 (a year of political and economic crisis in Bulgaria) came to \$782.2 million (compare with \$931.1 million in 1995 and \$ 692 million in 1996), of which Greek exports accounted for \$ 315.8 million and imports from Bulgaria \$412.4 million. In the first half of 1998 the volume of trade reached \$407.5 million, with exports representing \$214 million and imports \$193.5 million. The figures indicate a positive reversal of trends in the indices for bilateral trade and in the balance of trade.

The most importance Greek investors in Bulgaria are:

- 1.3E (\$55 million), Coca-Cola, distributors.
2. Eurobank (\$38 million), which bought 78% of Post Bank.
3. Athens Breweries (\$14 million) which bought several large breweries.
4. Intracom (\$8 million) telecommunications and information technology.

5.Delta (\$5.5 million) food and beverages, (the biggest Greek - Bulgarian joint venture).

- 6.Chipita (\$5.5 million) snack foods.
- 7.Alpha Bank (\$3 million) banking.
8. Goody's (\$1 million) fast food chain.
- 9.Mechaniki group (1million) construction.

Other Greek investors in Bulgaria include Vardinoyiannis group (petroleum fuels). Thrace Paper Mills, TXM (fruit and juice canners), NIKAS (processed meat), FANCO (textile mills) and Florina – Chonaios (fruit juices) etc.

Three Greek banks have set up branches in Bulgaria: Xios, Alpha Bank, and National Bank of Greece, while the Commercial Bank of Greece has acquired an 86 % equity share in the Bulgarian Investment Bank. Eurobank of the Latsis group, in collaboration with the US firm AIG, has bought Port Bank and the Hellenic Investment and Industrial Development Bank (ETEVA), and it has established a stock broking firm and an office of representation.

Companies involving Greek interests employ some 22.000 people, particularly in southern Bulgaria where 80 factories produce clothing to order for customers in the US and West Europe.

6.2.1. Investment climate in Bulgaria

In an era of declining fortunes of emerging markets through out the world such as in Asia and Russia, Bulgaria is a market that deserves closer attention by Greek companies for its trade and investment potential. This economic and political stability in the Balkan peninsula has greatly expanded its commercial ties with Western Europe and the United states. Over half of Bulgaria's exports currently go to Western Europe, and the United States is one of the Bulgaria's top foreign investor.

Since 1997, the severe economic hardship for the Bulgarian people has greatly eased as the Bulgarian currency, the lev (BGN) has been stabilized at a current rate of BGN (equivalent 1 lev per deutschmark), inflation has been reduced to a single digit, and confidence in the Banking system is starting to return. Bulgaria's Gross Domestic Product (GDP) reached \$12.700 million in 1998 and 1998's real GDP growth rate of 3.5 percent. The 1999 GDP growth rate of only 1.5% is in part due to the Kosovo conflict.

Bulgaria is still a poor country with average pre capita income estimated at under \$1.500 per year. While this limits consumer purchasing power for relatively expensive foreign products, Bulgaria's workforce offers attractions to manufacturing investors for its good education, especially in engineering and foreign language ability.

Openness to Foreign Investment

Bulgaria has one of the most liberal foreign investment laws in the region. Between 1992 and the end of 2000, Foreign Direct investment (FDI) inflows into Bulgaria amounted to approximately \$3.147,4 U.S. Foreign investment typically assumes one of the following forms:

- ✓ establishing a **joint venture** with existing state-owned companies,
- ✓ establishing a **joint venture** with existing private companies,
- ✓ acquiring a company through privatization,
- ✓ setting up a new (Green field) venture,
- ✓ or making portfolio investment.

The **most common type** of foreign investors is a **limited liability company**. Other forms are companies limited by shares (joint stock companies), joint enterprises, business associations, general partnerships limited partnerships and sole proprietorships.

The **problems most often cited by foreign investors** in Bulgaria are:

- ✓ Poor Infrastructure,
- ✓ Little advance notice of new laws or regulations or amendments,
- ✓ A relatively high tax burden,
- ✓ The Banking system,
- ✓ The protracted privatization process
- ✓ And government bureaucracy.

The 1993 Law on Foreign Person's Business Activity and Foreign investment Protection (the (Foreign Investment Law) as amended, establishes the **Foreign Investment Agency (http://www.bfia.org)** as the government's coordinating body for foreign investment. The law extends national treatment to foreign investors, guarantees compensation in the event of expropriation, and allows the repatriation of profits. The law explicitly recognizes intellectual property and treasury bonds as foreign investment.

The law does not limit the extent or amount of foreign participation in companies. Foreign companies have the right to open deposit accounts in hard currency and Bulgarian levs.

Foreign companies are permitted to engage in various forms of business activity including the acquisition of shares in companies, with some restrictions. Foreigners cannot own a land (this is a constitutional prohibition which will eventually be changed to comply with European Union accession requirements). However, the Foreign Investment Law removed most restrictions on acquisition of land by locally- register companies with majority foreign participation. Local companies where foreign partners have controlling interests must obtain prior approval (licenses) to engage in production and export of arms/ammunition, banking and insurance and acquisition of property in certain geographical areas/zones. Licenses are granted by the Council of Ministers or, in the case of Banking, the Bulgarian National Bank (BNB). These institutions have published conditions for licenses which Bulgarian officials assert are nominal and routine.

Joint ventures in Bulgaria

There are several laws that govern joint venture with foreign participation including the Law of Foreign Person's Economic Activity and Foreign Investment Protection/Law and the Commercial Code as they have already been described in chapter four on "Country analysis of Bulgaria".

Joint ventures **with state-owned companies** must be approved by the relevant ministry. In most instances, this is the Ministry of Industry. The regulations for the Regime of Exercising the state's rights of ownership in Enterprise (amended), promulgated by the council of Ministers in January 1994, provides the authority for the respective ministries have to issue internal regulations for the negotiation and approval of joint ventures.

The negotiation phase usually addresses the evaluation of existing assets and contribution of the foreign partner. The foreign contribution can be in cash, capital in-kind and know how. The contribution of the local partner is usually in long-term assets (i.e., existing equipment, facilities, etc.). Other usually discussed issues are: labor issues (employment guarantees), future business and marketing plans and management contracts.

Joint ventures **with private companies** do not follow the same procedures. No government involvement or approval is necessary. After completion of negotiations, the entity must be registered with the court. If a new legal entity is created, an evaluation of the assets is performed by a court-appointed expert. The expert's asset evaluation may not be satisfactory from the investor's perspective. A foreign investor, who obtains a stake in an existing enterprise through an increase in the capital, receives an increase in the stake based on the value of the already negotiated assets. Valuation is essentially negotiated by the parties rather than by appointed experts.

Among successful Greek joint ventures in Bulgaria, one has been between the Greek company Delta Holding S.A and the Bulgarian state-owned company Vitalact, and home created the DELTA BULGARIA S.A (which was renamed in May 1000 from DELVI-P). The case study of the above joint venture is presented in this chapter.

Bulgaria's Growth Experience and Prospects by IMF

As a result **of the lack of sound economic policies until 1997**, the country is lagging the advanced transition countries in the recovery from the transformation recession. Output is still around 30% below its pre-transition peak, and per capita income purchasing power terms is only one fourth of that in current EU members. Bulgaria therefore still has a long way to go to fully realize the potential for productivity improvements from the move to an open and market-based economy, and to reach its goal of catching up with the EU countries.

Bulgaria's growth in the last decades has been uneven. The extensive growth model introduced under planning more than 40 years ago was initially highly successful in achieving rapid growth. But the strategy based on industrialization and high investment had exhausted its growth potential by the early 1980's and the authorities' inability to change course left Bulgaria with a highly distorted economy and a heavy external debt burden at the onset of the transition in 1990. The initial transformation recession was prolonged and deepened by the inability of successive governments to implement prudent macroeconomic policies and pursue structural reform, which culminated in the 1996-1997 financial crisis and a second pronounced recession. The consistent implementation of sound economic policies since 1997 has however resulted in a turnaround. Notwithstanding unfavorable external developments, including the Kosovo crisis, GDP growth has been positive since 1998 and it accelerated to a robust 5.8 % in 2000.

Despite a remarkable turnaround since 1997, conditions for self-sustained growth appear not yet to be fully in place. Aggregate demand growth in recent years has been driven mainly by the rebound from the 1996-1997 crisis and external factors. A look at the supply side also suggests that the economy is still in a recovery phase, with the factors of production being far from fully

utilized. Moreover, significant structural and institutional bottlenecks continue to curtail Bulgarian's growth potential. Enterprise access to bank financing system is low and corporate governance remains weak. *Foreign Direct Investments (F.D.I)* and exports are still concentrated in more traditional sectors, and the quality of the institutions and the business climate falls short of what in need to support a dynamic private sector.

Bulgarian can reach sustained growth of at least 5% per year, provided the proper macroeconomic and reform policies are in place and investment and effective labor input are raised.

6.3 Greek investors in FYROM

Seven years ago, Greece slapped an economic embargo on the FYROM because of disputes over its name, flag and minorities policies. Greek FDI recorded a fast grow (from \$1.0 million USD in 1994 to \$230 million USD in 1999).

Greece is the largest foreign investor in FYROM, with 70 Greek companies conducting over 250 million dollars in trade to date. Greek entities will expand FYROM electrical grid, modernize its oil refineries, and construct a \$60 million thermoelectric plant and a new oil pipeline connecting Thessaloniki to Skopje.

With strong disagreements in Athens concerning this nascent republic's chosen name of "Macedonia" (also the name of an immediately adjacent region in northern Greece), bilateral relations got off to a patchy start in the early '90s. The signing of an interim agreement between the two countries in New York in 1995, which established diplomatic relations and a framework for resolving differences, marked the turning point in economic relations also, with Greek investments here constantly increasing.

Today these investments total \$292 million (from 1994-1999), a large part of which concerns a \$182 million agreement for the purchase of the state-controlled OKTA oil refineries and the construction of a Thessaloniki –Skopje oil pipeline, recently signed by Hellenic Petroleum S.A.

The governments of the two countries have also made an initial agreement for the purchase of the state-owned telecommunications organization PTT Macedonia by OTE and of Stopanska Banka by the National Bank of Greece. It should noted that there is interest in developing cooperation in the construction sector, transport, transfer of know-how and in the foundation of mixed joint enterprises.

The volume of bilateral trade in 1997 came to \$333.3 million, up from \$271.3 million in 1996, of which \$273.1 million were Greek exports. For the first half of 1998, bilateral trade reached \$162.9 million, with \$136 million worth of Greek exports. Greece according to figures for the first seven months of 1997 is FYROM's third largest trading partner after Yugoslavia and Germany. The created Greek investments (except those concerning petroleum products) maintained approximately 4.000 jobs in FYROM, which are expected to increase to 5.000 when the investment plans in progress are realized, especially in the areas of consumer goods and clothing.

The largest Greek investments from the point of view of capital were:

1. The purchase of a majority share in OKTA (\$182 million)
2. The purchase of USJE cements (80% share) by the Titan cooperative and Swiss-based Holderbank. This investment, worth 52 million DM, was the largest investment in FYROM up until the end of 1998.

3. The purchase of Strumnica Tabac by Mihailides Tobacco. This was an investment of 8.58 million DM, to which the purchase of tobacco worth \$10 million should be added.
4. An agreement with the Mytilinaios group, rights to the exploitation of the Zletovo and Sasa mines (mercury and lead). The agreement is for \$6 million, while with the supply of assets it is expected to come to \$12 million.
5. The purchase of 61% of the stock of the Privara Skopje breweries by Balkanbru Holding Ltd (**a joint venture by 3E and Athenian Breweries**). The size of investment comes to \$32 million.
6. In addition, the list of companies active in the neighboring country include:
 - ❑ **VERO**-Two supermarkets of the Veropoulos chain in Skopje, representing an investment of ten (10) million DM.
 - ❑ **NIKAS Skop**- A subsidiary of Nikas Thessaloniki created with a local partner, which is building a processed meats factory-an investment of seven (7) million DM.
 - ❑ **DELTA**- An import and distribution agent for Delta ice creams, involving and investment of nearly 5 million DM.
 - ❑ **LARIN MARMOR Co**- a mixed company created by Lazaridis Marbles and a local partner. Size of investment 1.5 million DM.

Finally, other Greek companies active in FYROM include several ice cream manufacturers (Torre-Kri-Kri, Kumanovo), processed meat manufacturers (Zlatis - Prilep) soft drinks (Kroner Star) clothing manufacture (Laskou, Rodon) and others.

Cooperation between FYROM and GREEK companies-FDI

FYROM is a country with a very limited market potential. Therefore, the most important precondition for the survival of the economy is the implementation of an export orientation being essential for providing a development strategy.

One of the traditional trade-partners of the FYROM is Greece. It has almost always had a relatively high level of participation in the foreign exchange of goods and services, which is due not only to its geographical closeness, traffic connections and interdependence, but also to the complementarity of different economic segments of both the countries. During the period 1981-1991 the exchange of goods and services in this direction had been realized according to the Trade agreement between the SFRY and the EEC. Greece had gained the same rights and terms for the realization of cross-border small-scale trade as other countries that had signed special agreements with FYROM on the regulation of this specific kind of economic cooperation. This form of cooperation comprised 24% of the total exchange of goods and services between FYROM and Greece until 1990, and Greece was the first among neighboring countries with regard to the scope of trade with FYROM. During this period Greece participated with 4.5% of the total foreign exchange of goods and services with FYROM. However the exchange was unbalanced, characterized by an unsatisfactory product diversification and by a lack of developed forms of economic cooperation.

The cooperation of the FYROM and Greece was interrupted many times during the period 1992-1993, while in 1994 it was completely cancelled, because of the Greek embargo imposed in FYROM for political reasons.

The lifting of the embargo contributed to the intensification of the exchange of goods and services with this country. Of course such a trend in FYROM foreign trade is a positive one, as Greece is not

only a neighboring country, but it is also a member of the EU. Thus, only one year after the lifting of the embargo the trade with Greece reached the level of 1989 (in 1996 Greece participated with 4.2% in the total foreign exchange of goods and services of the FYROM). The fact that, only a year after the embargo–lifting, Greece had become the most important trade-partner among neighboring countries is significant.

In the import structure, according to the certificates of product origin, the following items have the greatest participation: cotton, fatty pies and soya remains, petroleum bitumen, oranges, raw vegetable oil, ice-cream, sports wear, aluminum drums, other prepared vegetables and gas oil. This points out that here are dealing again with a traditional structure of foreign exchange which is dominated by basic products with a low processing level. The trade balance between FYROM with Greece records a continuous deficit which reached the amount of \$ 20.4 mil U.S in 1996

More developed forms of cooperation are not yet intensive, although Greece, as an EU-member, is expected to help FYROM to narrow the gap with the Union's standards, which especially concerns cross-border cooperation. However, the removal of the embargo has increased the interest of Greek firms in the effectuation of capital in the form of FDI in the FYROM economy, especially in sectors provided with raw materials from domestic sources, which have a strategic importance for the country (for example the food–processing industry). Actually, Greek interest is especially strong in those sectors that have a potential to compete with Greek products on foreign markets in the near future. Greek FDI recorded a fast growth (they amounted only \$1.0 million US in 1994, \$3 million USD in 1995, while in 1996 they reached the figure of \$9.9 mil USD and continued to grow. However, they were eight times smaller in comparison with German FDI. In May 1999 the **Office for Economic and Commercial Affairs of the Hellenic Republic Liaison** in Skopje estimated Greek FDI up to **\$230 mil USD** and claimed that **Greece is the largest Foreign Investor in the country**.

One should bear in mind that a substantial part of the above-mentioned amount is operative, which leaves the primacy in this sphere in the hands of German and Austrian Firms. At first glance this situation may appear a paradox considering the fact that Greece is the only neighboring country that at the same time is the member of EU. The political embargo has, however, resulted in a climate of mistrust in the environment and caused diverse opinions about the entrance of Greek capital in the form of FDI in FYROM economy. Above all, Greece is a partner who could provide more advanced technology in the existing industries and does not have its own developed technological base, but is heavily dependent on the import of foreign technology. Therefore, FYROM firms prefer capital inflows from the developed EU countries. Of course, a positive Greek solution of the political status of the Republic of Macedonia could significantly contribute to the intensification of all kinds of cooperation between the two countries.

Foreign Direct Investments in FYROM

Strategic involvement in global changes imposes a need for better utilization of the effect of liberalization of the international, economy and direct foreign investments (FDI). FDI is considered as a factor that generates export-led development, based on the domestic labor force and the existing natural resources. Motivated from the concept of export promotion, this activity includes several goals and consequently, measures that have technological modernization of the export economy as their particular.

In the creation of the export development policy and the attraction of the FDI to FYROM, the FDI take an even greater significance, as they are used as a substitute for domestic crediting. Consequently they produce closer linking with the external markets, while changing the structure of the economy in accordance with the export criteria. FYROM should be open to FDI because of:

- (a) the concept of open export-oriented development,
- (b) the strategic aim of integration into the EU,

(c) and the existing trends of international economic collaboration.

For FYROM economy, the most important long term effects of FDI are those linked to the restructuring of the exporting part of the economy, the improvement of quantity and quality of the production factors, the efficiency in the allocation of resources and use of capacities, the technical and technological progress and the increased factor of productivity and the possibility of stimulating the dynamic of the development through innovations. Taking this into consideration, the basic question is to what extent the state can influence companies to adopt FDI as their company strategies, i.e., to consider them as private entrepreneurship goals.

There are four types of FDI in practice:

- 1.FDI in search for natural resources,
- 2.FDI in search for market access,
- 3.FDI in search for greater (Economy of scope),
- 4.FDI in search for strategic resources.

In the forthcoming period FYROM needs a clear strategy toward attracting FDI to the exporting sectors. This strategy must answer the question of what is really expected of FDI and what instruments and type of institutional organizations are needed to fulfill the aims. FDI should be a development factor in the adoption of technology, an access to foreign markets, better management and organization, and integration into the international economy. Priorities should be given to what is known as horizontal FDIs, that have a similar type of production in different countries, instead of vertical FDIs where the company locates separate levels of production in different countries. This is due to the fact that the conditions that the FYROM offers to FDI for providing a larger market and exploiting the natural resources of the country are rather limited, when compared with strategic FDI.

By accepting these general assumptions, the approach and policy of the FYROM toward FDI should be based on the following principles:

- 1.Stability and transparency of the relations, regulations and economic policy.
- 2.Equal treatment of foreign investors and domestic companies.
3. State interventions in FDI should be based on principles of active and positive stimulation of the desired treatment, and not passive and negative rejection through different limitations and prohibitions.
- 4.In the long term, FDI should increase to a level needed to ensure an active foreign-oriented internationalization of the Macedonian companies.
5. Whether it is a case of FDI in the form of buy-out and expansion, purchasing new investments, reinvested profit and other capital investments that happen between the Multinational Companies and their affiliates, they should ensure productive –technological restructuring in order to increase the presence of propulsive structures.

The amount of \$210 million USD in the period from 1991-1998, doesn't even approximately represent the desired amount, but rather speak of the low level of FDI. The largest part of these investments have come from the EU (mostly Germany and Greece) and are directed towards gypsum and cement industry, technical gases, the iron and steel industry, production of tobacco, supermarkets, textiles and clothing, food production etc.

6.4. The Case of Greek Joint Venture “DELTA Holding S.A ” in Bulgaria

In the past years, a very limited number of Greek enterprises had invested abroad (foreign direct investment-FDI) and the cost of investment was rather immaterial. This situation changed radically during the current decade with the trend of economic co-operation and investment activity in the Balkan States. Many big and medium sized Greek enterprises invested in the Balkans and continue to do so.

Since investing abroad is something new or unknown for the vast majority of Greek industrial firms or banks, the investment practices particularly similarities and differences between FDI and domestic investment activities, are important and interesting to examine. The following case study aims to examine the joint venture project undertaken by Greek company “ DELTA HOLDING S.A “ in Bulgaria.

6.4.1. Introduction

Foreign investment decision processes have attracted considerably less attention from researchers compared to domestic investments. It has to be noted that the scope of study is capital and not offshore investments. Dealing with Foreign Direct Investments (FDI) is very different from investing in a home country because more factors have to be taken into consideration. Thus, the decision making process is probably more complex and risky (Aharoni, 1966). The main reason for this is the lack of the organization’s lack of knowledge concerning the foreign countries that are the potential hosts for their investments. In addition to the usual business and financial risk in relation to a capital investment, investing abroad contains other specific risks defined as country or political risks, of both an economic and non-economic nature.

FDI could involve the establishment of a new enterprise overseas (Greenfield strategy), the expansion of an existing branch or subsidiary or the acquisition of an overseas business enterprise or its assets. **The presentation of the case study seeks to answer three questions. First**, what are the differences (as well as similarities) between foreign direct investment (FDI) decision processes and domestic capital investment decision processes. **Second**, how management accounting information is used in the decision process in relation with the financial analysis applied. **Third**, how corporate strategy is linked with the foreign investments and what is the role of politics in the determination of foreign expansion strategy.

6.4.2. Literature

6.4.2.1. Why invest in the Balkan States?

The common characteristic of East European countries is that they are currently in a state of transition, moving from a centrally programmed economy towards an open market economy. This transition gives the opportunity to western companies to invest in Eastern Europe in different ways, in order to gain market share and make profits out of this investment.

The reasons for investing in Eastern Europe include the following: selling to a growing market with unsatisfied demand, producing cheaply, exporting possibly to the new wider European region or entering Eastern Europe before competition. For the first time, Eastern Europe offers many attractions to foreign investors such as low asset sale prices, low wages, economic growth, transferability of profits and advantages of entering other markets. But nothing appears to be ideal. On the contrary, as mentioned before, these economies are in a state of continuous transition and currently they are suffering shocks on their way to becoming like western economies. Despite the poor economic situation and the insecure political condition, many companies from western countries are investing in the Balkans, among them many Greek companies. Greek investors were among the first to invest in these countries.

6.4.2.2. FDI decision-making.

Managers are reluctant to face risks and thus do not consider investing abroad unless an initiating force appears that would change their mind. An initiating force might be an outside proposal from a source that cannot easily be ignored, fear of losing a market, successful activities abroad of a competing firm or strong competition from abroad in the home market. After the appearance of an initiating force to invest, the investigation process starts within which many general factors are considered. These factors refer either exclusively to the foreign investment (government policy/politics, economic, legal, social environment, infrastructure and provided services, etc.) or to factors relevant to any investment opportunity. Following, the stages of the FDI process according to Aharoni (1966) are outlined as outline:

- **General Indicators.**
 - Risk and Uncertainty (political, economic, nuisance)
 - Changes in perceived risk through investigations.
 - Market Size.
- **On the spot investigation. Information about sales, prices, cost of investment, etc.**
- **The presentation.**

The final stage after the investigation is the decision to invest. Before the final agreement, the project is modified after negotiations within the firm and with outsiders. Thus, the final decision is influenced by commitments, social structure and power relations in the organization (Mintzberg, 1985). Wei and Christodoulou (1997) define FDIs as either equity or capital investment by the parent company in a new or existing overseas enterprise.

Similar to Aharoni (1966) they examine the **FDI decision process according to three phases, which are:**

- 1. Initiation and Preliminary thinking,**
- 2. investigation and,**
- 3. evaluation and final decision-making.**

Past experience with foreign operations, high sales (thus growth) and, cultural similarities between the company's home and host countries could be considered as factors effecting a decision in favor of FDI. Cost and price competition was identified as important reasons for a company to internationalize its activities (Wei & Christodoulou, 1997). Environmental changes and company's growth goals were identified as major initiating forces for considering foreign direct investments. Among the companies in the sample, a limited number undertook formal and long run planning procedures for the FDI assessment. It was noted that the main information collected was about regulations and laws in the host country. The majority of the companies considered a single option rather than multiple choices during the FDI decision aking. Finally, the most used financial analysis method was return on sales and political risk analysis (Wei & Christodoulou 1997).

When discussing capital investments, most people have in mind capital budgeting theory that is represented by the rational investment decision model and the financial techniques used to assess candidate projects and determine the final decision. The decision process is not as simple as to be fully explained by a model. Political, social and behavioral factors exist within the business organization and influence the decision-making (Northcott, 1992). The economically rational

decision-maker stands only in the assumptions of economic theory. When used, financial techniques rather help decisions or justify a decision made. King (1975) conducted two case studies and found that the first stages of the decision processes (identification, screening and definition) are the most important because during those stages it is in fact determined which projects would be selected.

6.4.2.3. Linking strategy to capital budgeting

«All investment decisions could be regarded as strategic in the sense that they had long-term implications for the organization and helped to set its future course of action»(Butler et al, 1993). Most of the literature on capital investment focuses on the financial appraisal techniques and the need for sophistication. Strategic considerations were considered only during recent decades. Financial analysis is unable to examine all the variables related to capital investment decision making, specifically marketing and strategic issues that are usually difficult to quantify but are key decision determinants (Barwise et al, 1989). Companies that pursued a strategic planning approach appeared having achieved better performance both in financial and competitive terms. That can be explained through focusing on those key strategic factors which, though not quantified, were identified as being directly related to success. Such factors were: *knowledge of the market products, technology and competition*. Sophisticated, formal Management Information system does not necessarily result in better decision making. As shown in the literature, strategic rather than financial considerations appear to be more important motivations for Foreign Direct Investment (Eitman et al, 1991).

6.4.3. Research questions and methodological issues

The research method selected **is the case study approach** since it provides an in-depth analysis of the investing company and allows the researcher the opportunity to study in detail the organizational practices and decision making process. Field study research includes participant observation, interviewing and document analysis and is useful in order to study accounting within its organizational and social contexts (Burchell et al 1980).

6.4.4. Case Study of Delta Holding S.A (a joint venture in Bulgaria)

6.4.4.1. Delta in the Greek market

Delta Holding S.A, originally a family-run firm, is the holding company of one of the largest food manufacturing group of companies in Greece, actively involved in the dairy business, ice cream market, fresh juices market, frozen food market and food retailing services. In 1990 Delta was listed on the Athens Stock Exchange, thoughts emerged towards the internationalization of its activities and the first moves took place.

Delta targets a regional market of 50 million consumers. The Group's facilities consist of six factories in Greece, and three in South East Europe namely in Romania, Bulgaria and Serbia. Overall, it maintains operations in eight countries in S.E Europe through 85.000 points of sale. It produces 160 different products and co-operates with more than 1.000 farmers representing more than 25% of domestic milk production in this region and employs in excess of 2.500 employees.

Delta is:

- (c) the leading fresh milk distributor in Greece with **41% of the market** share and
- (d) the leader in the fresh chocolate milk market in Greece with **42% of the market**.

Furthermore, in June 2000, **Delta established a joint venture with ARLA FOODS Amba**, the biggest cheese and butter producer in the world. The new joint venture operate under Aria Foods

Hellas S.A. further reinforced Delta's position in the dairy sector in Greece, making it number one in the cheese and butter Greek market.

The new Delta Holding S.A successfully capitalizes on its many advantages. A dominant position in its core business, strong partnerships, the flexibility of its new structure and finally a strong financial position.

Targets regions for Delta Holding are Western Europe as well as Eastern Europe and the Balkans, in which during the last years the company has experienced a rapid growth.

Delta in South East and Western Europe

In March of 2000, recognizing the fact that the Group's operating units needed more flexibility to pursue business opportunities and maximize their competitive advantages in their own market segments, DELTA group underwent a major restructuring. Its S.E Europe investments were essentially completed in 1998 and now Delta's presence in the region is significant, with 30.000 sales outlets and overall production twice as important as those in Greece (over 100 million pieces) Overall investments in the region exceed \$70 million Euros.

Delta has been engaged in the production and distribution of ice cream in Bulgaria, Romania, Serbia and FYROM (where the company holds 80%, 37%, 52% and 55% market share respectively) with venture capital companies and organizations such as the EBRD. Delta also exports its products to Cyprus, Lebanon and Croatia. Total sales in the Balkan region are estimated to have reached 44 million Euros in 2000.

In Western Europe, Delta capitalizes on its alliance with the multinational Danone. Delta Greek style yogurt is produced by Delta in Greece and exported to France, where Danone distributes it. The Group's collaboration with Danone, which participates by 30% in the share capital of Delta Dairy S.A has resulted in the introduction of new technologies, know - how and products.

Delta's company profile

Delta's main stockholder is the Daskalopoulos family, which owns 56% of the share capital. The son is the managing director and CEO of Delta, and runs and manages the company. He is the key decision-maker in the FDI process. According to the latest corporate structure of Delta, the company has three separate operational divisions that are called **Strategic Business Units (SBU)**. The Fresh Food Division, which is the first strategic business unit, deals with the production, distribution and sale of milk, juices and fresh dairy products (yogurt, desserts). Delta is the national market leader in milk. In juices, the competition is very strong and thus Delta attracts a market share of only 30%. Similar conditions exist for yogurt. Ice cream is the second SBU in Delta. Delta is a major ice cream producer and distributor in Greece having an overall 48% of the total market. Its strategy focuses on the creation of strong brands with high added value. Frozen Foods is Delta's third SBU and the main products are frozen vegetables and various pies.

6.4.4.2. Delta's internationalization strategy

The strategy, analyzed into goals and means, is expressed in the business plans and annual budgets that each of Delta's Strategic Business Units prepares. Business plans have a three-year horizon but are reviewed yearly. A business plan could be characterized as strategic, depicting the long-term goals that should be achieved. The annual budget is more detailed in terms of financial figures and contains data on future income and expenses. Delta does not usually apply formal techniques like S.W.O.T analysis in formulating its strategy.

Good knowledge of the market and long-term experience from operations is considered by Delta's managers to be an adequate basis for formulating corporate strategy. During the late 1980s the

company faced considerable growth both in sales and profits. The annual rate of growth was around 20% to 30%.

The C.E.O. considered the Greek market in milk and ice cream to be very competitive, and felt that in the long run it would be stable, making it more difficult to gain huge increases in market share. Thus, in order to maintain similar rates of growth in the future, Delta had either to diversify its activities in Greece or to expand into foreign countries. In line with the first strategic choice the company entered the juices market in 1989, invested in yogurt production in 1995, acquired Frozen Foods SA and came to strategic alliance with Danone, a French global leader in fresh dairy products.

Recently, Delta has been considering expanding in the mineral water market in Greece, possibly in co-operation with Danone. Concerning foreign expansion, it was decided that Delta would rather enter a foreign market through FDI and not exports because of protectionism and lack of foreign currency reserves in Balkan countries. Also, these countries have been encouraging foreign investments because of the decrease in domestic production and the increase of unemployment. Delta chose to invest in the Balkans for the following reasons:

- The countries targeted are just next to Greece, so they are very close to visit.
- There was a lack of considerable competition because strong western companies preferred to invest in Central - Eastern European states and not in the Southeast of Europe because of higher country risk, inferior infrastructures and poor industrialization basis.
- Greek managers' potential for effective cross-cultural management was greater in the Balkans due to historical ties, similar habits, culture, etc, which allow them to understand the external environment in those countries and make valuable contacts with locals.
- There was a lack of strong brands, both domestic and foreign in these markets so it was less expensive for Delta to built brands.
- Existing low cost distribution channels are characterized by lack of expertise.
- Delta has the experience and is able to finance a high quality and high cost logistics infrastructure, such as refrigerators at sales points and suitable lorries. By building a network in such conditions, the investor gains a competitive advantage in the market and the company can build a barrier to entrance of potential competitors. For Delta, distribution channels amount to around 50% of total investment and that explains the importance of a trading company.

Having resolved the question of which foreign market to invest, the second major issue was what product(s) should be produced and distributed there. The answer was ice cream because of the following:

- Ice cream offers a higher gross and net operating margin than other dairy product because it is not a basic commodity. As a result, the company is insulated in a way from high country risk being suffered.
- Sales point settings (refrigerator, posters, umbrellas, stands, etc.) self-promote the product.
- There was a lack of quality ice cream in these countries. Existing brands were few and characterized by low quality and poor packaging. Consumers needed new brands, a variety of tastes and, differentiated quality products.
- The local population's disposable income is low and in recent years the economic situation has not allowed spending on durable consumer goods. Therefore, better quality ice cream is not an

expensive consumer good, but gives the illusion of a little luxury in every day living. (Similar goods are Coca-Cola, Macdonald's etc).

Delta's mission was to build a strong overall leadership position, targeting a high market share. This did not mean ignoring profitability but required allowing a time period of five years at least for the investment to yield. The strategy of entry in a foreign market was developed as follows: Domestic production for avoiding import duties.

- A relatively high selling price (premium) compared to local brands.
- Development of sales networks aiming to cover all the urban and semi-urban areas.
- A variety of ice creams and innovation. A strong management team from expatriates.
- A search for local partners. Their contribution was thought to be vital for dealing with red tape and resistance from local competitors. Delta was considering acquiring an existing plant or doing a joint venture in local production in order to reduce time and resources spent as well as risk.

6.4.4.3. Delta International Holdings (DIH)

Delta Dairy S.A, has created a fully owned holding company in Luxembourg named Delta International Holdings (DIH). Delta International as a holding company participates in or owns firms in which the parent company has made foreign direct investments or at least has a trading interest. The companies belonging to DIH are only ice cream distributors and/or producers and are currently located in Bulgaria, Romania, Yugoslavia, Former Yugoslav Republic of Macedonia (FYROM) and Ukraine. Delta International operates as a tax shell for Delta. Dividends, royalties and other remittances are transferred from foreign subsidiaries to DIH since in Luxembourg offshore companies are tax-free, so Delta can re-invest these amounts received in the future without incurring taxation. DIH has the responsibility for financing ice cream foreign investments, organizing management reporting and consolidating group financial statements. Delta's ice cream SBU is responsible for running and monitoring foreign operations. Other business presence abroad from the remaining Strategic Business Units, concern export or trading companies that do not belong to DIH.

As mentioned earlier, Delta's internationalization process started in 1991. By 1993 the first investment abroad, in Bulgaria, was ready. **It was a joint venture with Vitalact**, a state-owned dairy company. The joint venture owned Delvi-P, an ice-cream manufacturing plant and Delvi-T, which is a trading company. EBRD participated as a venture capital partner. In the beginning Delta had the majority of shares in Delvi-T while retaining a minority position in Delvi-P. Today, Delta controlled both Delvi companies that merged and create the Delta Bulgaria S.A. Also, Delta acquired Vitalakt and currently claims a 70% of the ice-cream market in Bulgaria. In 1994, Delta invested in a distribution company in Romania, Delrom.

The idea was to invest in marketing networks, which would be supplied from exports from the Bulgarian plant at which production costs were 30% cheaper than in Greece. But next year the Romanian government increased its tariff on ice cream from 20% to 70%. Delta's choice was either to get out of the market or to begin local production. Therefore, the company decided to buy an existing local producer, Queen and to expand further the current distribution network. The last huge FDI was in Yugoslavia, where tariffs are low, but quotas are imposed. Here, Delta invested in Delyug, a Greenfield production unit. Delta has trading companies in FYROM and Ukraine that are being supplied from the existing production plans. Also, limited areas of Russia are covered through exports but on a rather experimental basis. The parent company is considering investing in Ukraine in the near future in order to develop its position in that market. Over the past decade,

Delta has moved from being a Greek company with solely domestic markets, to having production and sales interests in a number of eastern European countries.

6.4.4.4. FDI decision process: The case of Bulgaria

The initiating force

As mentioned the C.E.O. was considering foreign expansion as a mean of preserving high rates of growth and dynamism in the company. The initiating force to consider investing in Bulgaria derived from a legal advisor to the company. That legal advisor had political connections in Bulgaria and operated there as a representative of various Greek firms. He suggested to the C.E.O. that Delta should be present in the Bulgarian market and offered to make needed contacts for that purpose.

The reason for selecting Bulgaria among other countries was rather political. It was the country beyond the borders, which appeared to be more stable at that time. Yugoslavia was in a better condition in terms of economic indices and industrial infrastructure until 1991, but the war and the consequent split of the federation prevented any second thought of investing there. Albania remained very unstable, with diplomatic disputes with Greece during the early 1990s and is still the poorest country in Europe. Bulgaria's economic condition was bad, but it was the only ex-communist state in the Balkans whose transition to democracy and market economy was almost without troubles.

Investigation and screening

Investigation and collecting data is the most important stage of the decision process because this information is vital in order to make a final decision. One of the main persons seeking information for Delta is the Business Development Director (BDD). The BDD usually goes first into the targeted country and participates in negotiations with local partners. He has to make all the necessary business and political contacts, to handle legal aspects and local information about the market. He executes consumer and market studies and examines the country from a macro-economic perspective. His role is to help create a firm ready to operate. Information about the economic and political environment as well as the market is important in order to examine whether a project fits the corporate strategy for expansion and to determine projected cash inflows. The International Business Director (IBD) assist the gathering of information. The IBD may have rich information on the market and how ice cream is being sold because before investing Delta had export or trading activity in many countries through a representative.

One reason for the almost entire dependency of Delta on its staff for the collection of market information was the absence of consultancy firms in Bulgaria during the period 1991-1992. Government reports on the economy were not reliable. Macro-economic data came from banks or the Economist Intelligence Unit. Governmental forecasts were much more optimistic than analysts' estimations. The business plan contained detailed information on demand, ice-cream production and consumption as well as market shares. This information was provided by state ice-cream industries but did not give any indication of consumer preferences, since under communist administration production the law of supply and demand was not followed. In the next main projects, Romania in 1994 and mainly Yugoslavia in 1997, market information derived from the potential local partners of Delta as well as from market research performed by Delta's staff. Also, external consultants were used by Delta for various tasks like market and consumer research, analysis of the ice-cream industry and competition, etc. All the information discussed above was crucial in order to decide whether the project would continue.

In Yugoslavia, Delta's reason for investing was based on information about the per capita consumption of ice cream and about the sales volume per refrigerator. These data derived from a pilot study organized by Delta in 1997, in the major cities of Yugoslavia. Local consumption of ice cream was higher compared to any other Balkan country and almost reached the levels in Greece.

This occurred due to the co-operation in the past of multinational companies like Unilever with local producers. So, Yugoslavia was a good case for investing despite the tough political situation.

Country risk (political and economic) is a major element of FDI decision making. Country risk was defined qualitatively. Political risk consisted of political change and instability due to transition from the socialist system of governance to the democratic system. Because that process was underway, no business law and other legislation existed and it was difficult to rely on authorities that might not exist the next day. Other reasons for political risk had to do with tensions existing between some Balkan countries, minority issues, and security problems.

Country risk has to do with a country's macro-economic environment as well. Risk factors under consideration include rising inflation, unemployment, exchange rate volatility, decrease in GNP, the cost and availability of funds, etc. The investor is concerned about public finance policy, import duties and foreign currency availability. Also, economic conditions determine the expected demand for ice cream and thus the future cash flows. Furthermore, instability of local currency will influence sales price, the cost of imported raw material and remittances of dividends. In the business plan for the Bulgarian project, Delta introduced in its analysis a link between consumers' disposable income and the per capita consumption of consumer goods. Disposable income is the average income per consumer that can be used either for consumption or for savings. In other words, the disposable income is the income received net of taxes and other withholdings. Delta estimated that the first years' reductions in disposable income would result in a decrease of demand for ice cream, and later there would be a reversal of that trend. It is evident that, in the analysis of calculating future sales, the main factor was not competition and market shares but whether the Bulgarian customer would have enough money to buy ice cream, in other words whether the market was expected to grow or shrink.

Implementation of decision and negotiations

Having prepared a project's Business Plan, the business development team makes a presentation to the C.E.O. and to the management committee. The management committee is informal. If the proposal is accepted then the implementation stage follows. That entails recruitment of new staff, finding overseas offices, sending a management team from Greece to deal with the details of the project and make a plant operational, signing contracts and agreements, and making capital investment expenditures. The final decision is dependent on the outcome of negotiations that Delta's executives have with potential local partners. If the negotiations failed the Business Plan would not be implemented as such and consequently it would have to be materially altered or even withdrawn.

In Bulgaria, Delta started negotiations for a joint venture with the largest state owned dairy company, named Cerdika . Cerdika appeared to have many advantages. It was settled in the capital Sofia and had higher market-share than its competitors. But with the political instability in the early 90s, Cerdika had no permanent top executives, since every month another C.E.O. and board were appointed. There was not a set basis for talks. Next Delta considered the market's number two producer, Vitalakt, whose C.E.O. had personal power and had been twenty years in his position. Delta took data on the market from Cerdika to build the Business Plan. The company started negotiations with Vitalakt later, and just after having presented the Business Plan, the two future partners signed a letter of intent. Delta took a decision to invest in Bulgaria and found someone to co-operate with, but nothing was yet finalized. After signing the letter of intent, the main part of **negotiations started and lasted over 14 months.**

Delta would agree only under specific terms. These terms involved:

- (a) having management control and,
- (b) the majority in share capital and a trading company separate from the other activities of Vitalakt.

On the other side, the Bulgarians did not want to loose control. The outcome **was that a joint venture comprised of two separate companies was established.**

Delvi-T was the trading company in which Delta had the majority of share capital. Delta's contribution was in used carriage lorries and refrigerators. Vitalakt controlled Delvi-P, the production plant and Delta held 23% of shares. This 23% represents the contribution by Delta in used machinery. The percentage was determined through valuation of the machinery by both parties and a subsequent mutual agreement. As it is understood, Delta was trying to reduce risk by offering cash only for working capital while their main contribution to the investment was fixed assets previously in operation in the Athens plant. The rule was that when investing in a high-risk country, the investment should grow gradually to reduce risk, getting experience and managing self-financing expansion through existing cash flows. Delta had to deal with bureaucracy in Bulgaria. In Bulgaria there was no legislation about foreign investments and joint ventures, so **Delta's case was used as a pilot for a bill on such issues.**

6.4.5. Uses of Accounting information in the FDI decision process

According to most of the executives in Delta, the FDI decision is based more on "hunches and feelings than in numbers" (Business Development Director, 1999). For the Bulgarian project in particular there were not any reliable figures to perform financial and time series analysis. Negative economic forecasts and high risk were prohibitive for investments in the short run under rational decision criteria. To this extent, the C.E.O. had to be convinced that there was a business opportunity and that the only important risk variable was the time period required for the project to mature.

Projections of sales and cash flows were mere hypothesis and subjective assumptions about the future. In the projects that followed, the degree of subjectivity may have been reduced, due to experience and better information, but not eliminated completely. In Bulgaria, cost analysis was based on some crude estimates. It was not possible then to predict how wages, inflation or exchange rates would evolve. Cost variables from the Greek experience were not always applicable because of very different conditions. Financial analysis was performed and used as an indicator for decision making.

The financial techniques that Delta applies to its analysis of capital investment projects are Return on Investment (ROI), Internal Rate of Return (IRR) and Net Present Value (NPV). The treasurer provides in full the WACC calculation. Country risk is included in the WACC analysis and it is expressed by the market premium that the investor requires from the investment. As previously discussed, the market premium is a subjective estimate. Delta applies the market premium for each country as suggested in official publications like the Economist Intelligence Unit. The NPV of a project, having applied the WACC, was sometimes negative. In that case the treasurer notified the C.E.O. about the outcome but in reality no investment has been based exclusively in the outcome of a DCF model. As the treasurer says, relying only on NPV no investment would have take place in the Balkans. Greek entrepreneurs made FDI decisions with their instinct. Any decision to invest or not is usually made prior to any formal business plan presentation or NPV computation.

The decision is based on a feasibility study with several arbitrary facts and figures and relying on market and strategic criteria. Delta chose to expand in the Balkans because there was no substantial competition and thus there would be great advantages in the future from being the first to enter the market.

6.4.6. Conclusion: The decision criteria applied by Delta

Most of the criteria applied to decision making could be characterized as more strategic than merely financial. The company believes that indicators of the market and the country in general are critical in the FDI decision process. Fundamental information available at the screening stage

determines materially whether the investment occurs or not. Another decisive factor is the outcome of negotiations. According to the previous analysis, Delta requires that the following criteria should be met in order for a FDI proposal to be accepted:

- Positive expectations about the country and market.
- Leading position in the market.
- Growth on sales and a high market share.
- Break-even in profit by the third year.
- Satisfactory profitability ratio for capital employed.

PART D. CONCLUSIONS - SUGGESTIONS

7. CONCLUSIONS - SUGGESTIONS

Conclusions

This guide was formed in a way to provide helpful summarized information to the prospective business investor/reader. For this purpose, the following conclusions were obtained after a thorough examination of all the sources of information presented in this study.

- Joint Venture (Joint Venture) relationships are, on average, fragile affairs, difficult to negotiate and, once negotiated, difficult to hold together. Although the reasons for breakdown may differ substantially between countries and between different types of partners, the pattern of frequent JV dissolution seems to be a global occurrence. This study has cited a number of reasons why this pattern holds and, implicit in their enumeration, also may suggest methods that might be used in reducing the probability of relationship difficulties among new partners. This is important, because JVs are becoming more and more common in developing countries as economic growth continues to take place more rapidly in these countries than in the industrial world. The contribution of these JVs to the development process is contingent upon their success as viable and ongoing business enterprises.
- The study did not explicitly consider the search process to be undertaken in locating potential JV partners, but it is clearly a vital dimension in any future relationship. Although personal compatibility is important at the beginning, it can be a transient phenomenon as managers move to new assignments. JV relationships should be determined much more by complementarities that will continue to exist between the respective organizations. These complementarities, together with a careful matching of corporate cultures, are the most promising focus of the search process.
- Even for partners who have had experience with one another, the agreement specifies terms of a relationship that is normally anticipated to go on for many years. While it is certainly true that no agreement can substitute for partners who are deeply committed to making the JV work, even committed partners can be expected to have conflicts of interest. An agreement doesn't have to be an overly legalistic document in order to provide the basis for overcoming these future conflicts in an orderly manner. Negotiating a suitable agreement, therefore, is a vital component of a successful relationship.
- The JV agreement is best considered as a "living" document in the sense that among its provisions there are procedures to amend or change the agreement itself. Rigid documents can themselves become the source of friction, and partners need to have confidence that if disagreements arise, there are clear procedures in place to allow further negotiations and reconciliation.
- Partners need to realize at the outset that their respective comparative advantages in establishing the JV may change over time. JVs are, after all, power relationships. Therefore, wise partners make sure that their companies are vital to the JV's success over the long-run. It is not sufficient for firms to depend on their intimate knowledge of government affairs or familiarity with local financial markets for continuing relevance in the JV, since these contributions are bound to erode. More substantive advantages are required: control of distribution channels, access to continuing sources of technology, control of export channels, etc.
- There is a belief that JVs not controlled by one party or the other are more susceptible to failure; equally shared ownership is to be avoided. The study did not support this belief. Nor is there evidence in the study that earlier experience with JVs by either partner had much to do with the enterprise's ultimate success or failure. The lesson would seem to be that satisfaction with a JV's performance is likely to have more to do with the ability of the

partners to adapt to changing circumstances and to maintain mutual respect than to any formal aspect of the JV itself.

- Technology transfer is one of the more sensitive and difficult issues confronting JV managements. It is a topic, therefore, that deserves detailed attention by both parties during negotiations, and clear and complete provisions are best included in the agreement. The problem for developing country firms is that technology also is an area where they have least control over the actions of their industrial country partners and, therefore, implicitly have to rely on trust. Although agreement provisions are important in setting out an operational framework for technology use in the JV, it is one area where formal provisions cannot substitute entirely for good will and understanding between partners.
- Agreements need to contain fairly detailed provisions covering dispute resolution and, in the event of failure to reconcile differences, the exit mechanism to be employed in terminating the JV. Such matters should not be avoided in the belief that good relations will be maintained over the life of the JV or that thinking about disputes at the outset somehow is tantamount to assuring that disagreements will ensue. In our interviews, several cases arose where problems were apparent but where no such provisions existed in the agreement. Trying to resolve disputes in an *ad hoc* fashion as they occur can be a messy exercise.
- Finally, the fact that this study accented difficulties that arise in JV relationships is not intended to imply that JVs are to be avoided. Correctly structured between two or more partners with sustainable complementarities, JVs can be advantageous to all sides. There were many examples, through the study of JVs, that had successfully endured a variety of difficulties and had gone on to become thriving businesses in which the partners both continued to make contributions. Mutual trust and respect among the partners is important to such relationships, but so too is attention to maintaining compatible corporate goals and to assuring that the JV business continues to depend importantly on contributions from all partners.
- Greek investors must consider Joint Ventures as a business activity focused on a specific strategic intent. That is, an Foreign Direct Investment (FDI) approach will be a long term objective of the investors business plan. At the time the size of the investing company and its readiness to respond in small project must be assessed.
- The implementation of Greek investments in the Balkan region through FDI can benefit Greek government 's influence in the Balkan countries thus, it will reveal its dominant role in the greater area of Southern Europe.
- Despite the liberal legal frameworks of Bulgaria, including very liberal regulations for profit and capital repatriation, the law lacks a transparent and stable implementation and this is a serious impediment to FDI and further more for joint venture. There are also a lot of problems with the extent of government bureaucracy and corruption, which are partially due to the inadequacy of existing investment procedures. A feedback from foreign companies show the amazing fact that the difficulties most of all were experienced at the beginning when newcomers do not yet know the rules.
- Even though FYROM has been constantly stricken by external shocks, due to the instability of the whole region, it still stay an active area for foreign investors. Today Foreign Direct Investments (FDI) in the country are estimated to over \$400 million US, which is a relevant high amount for such a small economy. The fact that the economy infrastructure has also been included in the privatization process will also contribute to the further growth of the foreign investments in FYROM. The country is reforms oriented, with permanent arrangements with IMF and World Bank, which are an additional guarantee for the macroeconomic stability and the creation of a good entrepreneur atmosphere.

- The main factors that make FYROM attractive to the foreign direct investments are the following: (a) its good strategic position –it is located in the middle of the Balkans, it is a crossroad of many roads and it is a beginning spot for the penetration of foreign investments into the wider region, (b) the available cheap and well trained labor is an important comparative advantage of the country (e.g the average monthly net salaries in Gevgelija Municipality for private enterprises is 334DM, and for public jobs 315 DM for 2001), (c) the country has good infrastructure due to the financed program from IMF, World Bank and the EU Phare program, (d) especially important for the foreign investors from the cross border region are concessions given in the Interim Agreement for trade and trade related matters. According to the Article 128 of Stabilization and Association agreement between FYROM and the EU, provisions related to free movements of goods should enter into force prior to the Stabilization and Association Agreement - the interim Agreement was signed in April 2001 in Luxembourg and entered into force on June 2001. The interim agreement is preferential and in favor of FYROM due to the fact that the EU approved full market liberalization for country products the day when the agreement was entered into force.
- Evaluating the advantages for the SMEs and MNCs and the need to promote and develop the SMEs sector in the cross border region, the common effort undertaken within the project makes the first step towards recording and pointing out their main problems such as: (a) the lack of flows of information about markets, (b) the lack of flows of information about services, regulations and procedures, (c) the insufficient organizing and technical structure, (d) the difficulties of the local product's display abroad, (e) bureaucracy, different bank and law systems. The project collects data on a wide range of issues for the SMEs of the two regions, such as their accurate economic picture and the opportunities for cross-border cooperation, defines the areas of activities that the attractive development and joint investments and examines the potential **of joint ventures** that will provide opportunities for the Greek partners to transfer new technologies and know-how, and for the FYROM and Bulgaria counterparts to utilize fresh capital and secure markets to their products.
- For Bulgaria and FYROM Joint Venture barriers often cited by Greek investors are: government bureaucracy, poor infrastructure, little advance notice of new laws or regulations as well as frequent changes in the legal framework, low domestic Purchasing Parity, the lack of trust in the Banking System, the protected privatization process and the relatively high tax burden.
- Finally, It is hoped that, potential investors (and particularly Greek investors) will have been made aware of the potential risks associated with investing in Bulgaria and FYROM and that this Guide will provide them with a head start in their search for suitable investments. But, in the end, it is the responsibility of the investor to make his own investigations and come to his own conclusions in light of his particular circumstances and his alternative opportunities in Bulgaria and FYROM.

Suggestions

- Creation and formation of a self evaluation tool-questionnaire, according to which the Greek investor company will be able to assess its readiness to form a Joint Venture in Bulgaria and FYROM. This evaluation can be done in two ways. First internally, by creating a specialized project team responsible to perform the specific task. Secondly, by hiring an external consulting firm specialized in Foreign Direct Investments projects.
- In Bulgaria and FYROM, due to their previous political conditions, business mentality and the way of thinking in term of a free market economy is lacking. Thus, there is a strong need for education and training concerns into the European way of doing business and business management. All the above lead to the inference that there is a great opportunity for academic institutions to cooperate and to increase middle management employees know-how through their training, since they are critical part of success for any business activity. It is obvious that there is a “potential market” for business training services for the University of Macedonia in Thessaloniki.

**PART E. APPENDICES, ABBREVIATIONS &
ACRONYMS, BIBLIOGRAPHY & INTERNET
RESOURCES**

8. APPENDICES

APPENDIX I. Useful Contacts in Bulgaria

1. Bulgarian Government and Non-government Contacts

Office of the President and the Prime Minister

2, Dondoukov, Boulevard, Sofia
Phone: (359)(2) 983-839, 940-2064, Fax: (359)(2)980-4484, 980-2042
E-mail: president@president.bg, Website: <http://www.government.bg>, <http://www.president.bg>

Ministry of Finance

102, Rakovsky Street, 1000 Sofia
Phone: (359)(2) 985-91, Fax: (359)(2) 980-6863
Website: <http://www.minfin.government.bg>

Ministry of Economy

8, Slavianska Street, 1000 Sofia
Phone: (359)(2) 980-2430, Fax: (359)(2) 980-5106
Website: <http://www.mi.government.bg>

Ministry of Foreign Affairs

2, Aleksandar Shendov Street, Sofia
Phone: (359)(2) 714-31, Fax: (359)(2) 971-2413
E-mail: mfabg@mb.bia-bg.com

Ministry of Agriculture, Forestry and Agrarian Reform

55, Hristo Botev Boulevard, 1000 Sofia
Phone: (359)(2) 980-7873, Fax: (359)(2) 981-7955, 981-7542
Website: <http://www.mzgar.government.bg>

Ministry of Defense

1, Aksakov Street, 1000 Sofia
Phone: (359)(2) 546-001, Fax: (359)(2) 987-9693
E-mail: mod-deo@bulnet.bg

Ministry of Environment and Water

67, William Gladstone Street, 1000 Sofia
Phone: (359)(2) 940-6000, Fax: (359)(2) 986-4848

Ministry of Regional Development and Public Works

17-19, Kiril and Metodius Street, 1000 Sofia
Phone: (359)(2) 985-91, Fax: (359)(2) 980-6863

Ministry of Transport and Communications

9/11, Vasil Levski Street, 1000 Sofia
Phone: (359)(2) 940-9414, Fax: (359)(2) 987-3916
Website: <http://www.mt.government.bg>

Ministry of Labour and Social Policy

2, Triaditsa Street, Sofia
Phone: (359)(2) 914-08, Fax: (359)(2) 986-1318
E-mail: pmu-mlsw@bg400.bg

Securities and Stock Exchanges Commission

23, Vrabcha St., Sofia
Phone: (359)(2) 981- 1655, Fax: (359)(2) 981-8197

"Roads" Executive Agency

3, Macedonia Blvd., 1606 Sofia
Phone: (359)(2) 521-768, Fax: (359)(2) 951-5422

Bulgarian Chamber of Commerce and Industry

42, Parchevich St., 1000 Sofia
Phone: (359)(2) 987-3629, 987-2631/35, Fax: (359)(2) 987-32-09
E-mail: bccihead@main.infotel.bg, Website: <http://www.bcci.bg>

Bulgarian International Business Association

36A, Patriarch Evtimii Blvd., 1000 Sofia
Phone: (359 2) 981-9564, 981-9169, Fax: (359 2) 800-263
E-mail: biba@mobicom.com, Website: <http://www.bol.bg/biba>

Bulgarian Industrial Association

16-20, Alabin Street, 1000 Sofia
Phone: (359)(2) 980-9996, 980-9103, 980-9923, Fax: (359)(2) 987-2604
E-mail: office@bia-bg.com, Website: <http://www.bia-bg.com>

Bulgarian Building and Construction Chamber

23, Chumerna St., 1202 Sofia
Phone: (359)(2) 988-6861, 988-63-92, 988-6393, Fax: (359)(2) 988-6860
E-mail: bbcc@bnc.bg

Bulgaria Builders Association

6 Sveta Nedelya Sq., 1000 Sofia
Phone: (359)(2) 883-169, Fax: (359)(2) 876-8647

Bulgarian Association of Information Technology

13, Shipka St., entr., B, FL 1, 1504 Sofia
Phone: (359)(2) 946-1513, Fax: (359) (2) 438-694
E-mail: bait@spnet.net, bait@nat.bg

Bulgarian Franchising Association

6, Tsar Simeon St., Entr. II, Ap. 12, 9000 Varna
Phone/Fax: (359)(52) 600-724

Bulgarian Foreign Investment Agency

3, Sveta Sofia Street, 1000 Sofia
Phone: (359)(2) 980-0918, Fax: (359)(2) 980-1320
Website: <http://www.bfia.org>

Privatization Agency

29, Aksakov Street, 1000 Sofia
Phone: (359)(2) 987-7579, 861-3294, Fax: (359)(2) 981-1307
E-mail: bgpriv@mbox.digsys.bg, Website: <http://www.privatisation.online.bg>

National Statistic Institute

2, Panayot Volov Street, Sofia
Phone: (359)(2) 9857-2727, Fax: (359)(2) 9857-2000
Website: <http://www.nsi.bg>

State Agency on Energy and Energy Resources

8, Triaditza Street, 1000 Sofia

Phone: (359)(2) 988-5932, Fax: (359)(2) 81-502

State Telecommunications Commission

6, Gurko St., 1000 Sofia
Phone: (359)(2) 949-2335, Fax: (359)(2) 987-0695

Standardization

6, Gurko St., 1000 Sofia
Phone: (359)(2) 949-2575, Fax: (359)(2) 987-0695

Bulgarian Agency for Standardization and Metrology

21, Shesti Septemvri Street, 1000 Sofia
Phone: (359)(2) 988 5043, 980 8920, Fax: (359)(2) 986-1707

General Customs Directorate

1, Aksakov Street, 1000 Sofia
Phone: (359)(2) 869-222, 985-91, Fax: (359)(2) 980-6897

Patent and Trademark Office

52-B G. M. Dimitrov Street, 1000 Sofia
Phone: (359)(2) 711-3302, Fax: (359)(2) 708-325

2.Major State Enterprise

Bulgarian National Bank

1, Battenberg Sq., 1000 Sofia
Phone: (359)(2) 914-59, Fax: (359)(2) 980-2425
Website: <http://www.bnb.bg>

Bulgarian State Railroad

3, Ivan Vazov Street, 1000 Sofia
Phone: (359)(2) 981-1110, Fax: (359)(2) 987-7151

Bulgarian Telecommunications Company

8, General Totleben Street, 1000 Sofia
Phone: (359)(2) 949-4438, Fax: (359)(2) 951-5355
Website: <http://www.btc.bg>

Bulgargas

66, Filipovsko Shosse, Ljulin –2, PO Box 3, 1336 Sofia
Phone: (359)(2) 925-040, 259-074, Fax: (359)(2) 984-25313

National Electric Company (NEC)

5, Veslets Street, Sofia
Phone: (359)(2) 925-0401, 259-074, Fax: (359)(2) 984-25313

3.United States-Based Financial Institutions in Bulgaria

Bulgarian American Enterprise Fund

333 West Wacker Dr., Suite 2080, Chicago, Illinois, USA
Phone: (312)(2) 629-2500

CARESbac - Bulgaria AD

45, Oborishte Street, Floor 1, 1000 Sofia
Phone/Fax: (359)(2) 943-4417, 943-4163, E-mail: caresbac@bg400.bg

Citibank N.A-Sofia Branch

2, Maria Luisa Blvd, TSUM Business Center, 1000 Sofia

Phone: (359) (2) 946-0118, Fax: (359)(2) 917-5100

4. International Financial Institutions

European Bank for Reconstruction and Development (EBRD)

Sofia Resident Office, 17, Moskovska Street, 1000 Sofia
Phone: (359)(2) 987-6611, Fax: (359)(2) 981-5336
Website: <http://www.ebrd.org>

European Investment Bank (EIB)

100, Boulevard Konrad Adenauer, L-2950 Luxembourg
Phone: (352) 4379-3150, Fax: (325) 4379-3189
Website: <http://www.eib.org>

Multilateral Investment Guarantee Agency (MIGA)

1818 H Street, N.W. Washington, D.C. 20433, USA
Phone: (202) 473-8058, Fax: (202) 522-2630
Website: <http://www.worldbank.org>

EU PHARE Program

World Trade Center
36, Dragan Tsankov Street, 1040 Sofia
Phone: (359)(2) 973-3240 or 973-3857, Fax: (359)(2) 973-3872

World Bank

World Trade Center
36, Dragan Tsankov Street, 1040 Sofia
Phone: (359)(2) 973-3220, 973-3219, Fax: (359)(2) 971-2045
Website: <http://www.worldbank.org>

Foreign Agricultural Service

NDK Administrative Building - 5th Floor, 1, Bulgaria Square, 1414 Sofia
Phone: (359)(2) 951-5561, 963-1247, 951-5587, Fax: (359)(2) 981-6568
Website: <http://www.fas.usda.gov>

Department of State

1, Saborna Street, 1000 Sofia
Phone: (359)(2) 980-5241, Fax: (359)(2) 981-8977

U.S. Agency For International Development (USAID)

NDK Administrative Building - 5th Floor, 1, Bulgaria Square, 1414 Sofia
Phone: (359)(2) 951-5670, 951-5381, Fax: (359)(2) 951-5070

U.S. Information Service

18, Vitosha Street, 1000 Sofia
Phone: (359)(2) 980-4838, 980-3667, Fax: (359)(2) 980-3646
E-mail: usis@library.usis.bg, Website: <http://www.usis.bg>

5. Banks

Bulgarian Banks - Contact information for all Bulgarian banks may be found on the Bulgarian National Bank web site <http://www.bnb.bg>

6. Business Service Provides in Bulgaria

a. Accounting, Auditing and Consulting Firms

Arthur Andersen

1 Bulgaria Square, NDK Main Building, Floor 4, 1463 Sofia
Phone: (359) (2) 546-181, 963-1012, Fax: (359) (2) 980-1669
E-mail :boris.genovski@arthurandersen.com

Deloitte & Touche

9, Fritioff Nansen Blvd., 1000 Sofia
Phone: (359) (2) 980-8500, Fax: (359) (2) 980-00436
Website: www.deloitte.bg

Ernst & Young AFA

46, Alabin Street, 1000 Sofia
Phone: (359) (2) 986-0943, 981-9338, Fax: (359) (2) 980-0426
E-mail: EYBulg@mobitel.bg

KPMG Bulgaria

13, Slavyanska Street, 1000 Sofia
Phone: (359) (2) 980-5325, Fax: (359) (2) 980-0458
E-mail: consult@nat.bg

Price Waterhouse Coopers

2, Serdica Street, 1000 Sofia
Phone: (359) (2) 980-8884, Fax: (359) (2) 980-0404
E-mail: pwc.bulgaria@bg.pwcglobal.com

Institute of Transport and Communications

44, Parchevich Street, P.O. Box 1479
1000 Sofia
Phone/ Fax: (359) (2) 986-7704, (359) (2) 986-7721
E-mail: itc@bccci.bg, kvn@bulnet.bg

[b. Advertising and Public Relations Companies](#)

M3 Advertising Ltd.

1606 Sofia
Phone: (359)(2) 951-6775, Fax: (359)(2) 540 636

ATL 50 Todor Kostadinov Company,

P.O. Box 121, 18 Khristo Smirnenski Blvd. 1000 Sofia
Phone: (359)(2) 650-598, 650-479, Fax: (359)(2) 659 146

[c. Law Firms](#)

Arsov-Natchev-Ganeva Law Office

4A Benkovski Street, 1000 Sofia
Phone: (359)(2) 986-4365, 986-6703, Fax: (359)(2) 986-6223

Mr. Petur Bozhkov – Attorney at Law

1 Verila Street, 1463 Sofia
Phone: (359)(2) 515-579, 512-371, Fax: (359)(2) 543-330

Dr. Emil Benatov & Partners

Bl. 36B Liuliakova Gradina Street, 1113 Sofia
Phone: (359)(2) 973-3610, 971-2799, Fax: (359)(2) 973-3603

Mr. Valery Borisov, Attorney at Law

14-16 Buntovnik Street, 1407 Sofia
Phone: (359)(2) 656-711, Fax: (359)(2) 651-300

Borislav Boyanov & Co.

24 Patriarch Evtimii Blvd.1000 Sofia
Phone: (359) (2) 981-3007, 981-3103, Fax: (359) (2) 981-7733

Braykov's Legal Office

Dimitar Manov Street, Block 15, Floor 12, Apt. 43, 1408 Sofia
Phone: (359)(2) 543-077, 951-6040, Fax: (359) (2) 954-9325

Chernev, Komitova, Kalaydzhev & Partners

51, Parensov Street, 1000 Sofia
Phone: (359) (2) 980-2733, 980-1504, Fax: (359) (2) 980-2733

Dardov, Raykovski & Associates

11 Lavele Street, 3rd Floor, Apartment 9, 1000 Sofia
Phone: (359) (2) 89-8921, 987-5577, Fax: (359) (2) 981-5686

Dzhingov, Guginski, Kyutchukov & Velichkov

10, Tsar Osvoboditel Blvd., 1000 Sofia
Phone: (359) (2) 980-1358, Fax: (359) (2) 980-3586

Donev & Cholakov, Noblex Ltd.

1, Rilska St., 8000 Burgas
Phone: (359) (56) 843-745, 843-756, Fax: (359) (56) 840-124
Website: <http://www.digicom.bg/business/noblex>

Mr Stefan Chernokolev

13 Dunav Street, 1000 Sofia
Phone: (359) (2) 980-1628, 519-905, Fax: (359) (2) 964-4868
E-mail: emil@bulnet.bg

Modus Law Firm

13 Lozenska Planina Street, 1421 Sofia
Phone: (359) (2) 963-3122, 980-3648, Fax: (359) (2) 981-1296
E-mail: concord@datacom.bg

Goleminov & Goleminov

36-A Alexandur von Humboldt Street, 1113 Sofia
Phone : (359) (2) 989-5212, Fax : (359) (2) 706-203
E-mail: goleminov@mail.techno-link.com

Lega Interconsult, Penkov-Markov & Partners Law Offices

Iztok District, Block 22, 1113 Sofia
Phone : (359) (2) 732-936, 736-133, 737-930, Fax: (359) (2) 722-452
E-mail: lega@bg400.bg

Niesar Diamond & Todorova Law Offices

1, Jury Venelin Street, 1000 Sofia
Phone/Fax: (359) (2) 980-4136, Phone: (359) (2) 981-0765

Mr Rumen Raykovsky

11 Lavele Street, Floor 3, Suite 9, 1000 Sofia
Phone: (359) (2) 987-5577, Fax: (359) (2) 981-568
E-mail: rraysof@mail.bol.bg

Seplex Consulting Co.

8, Sveta Sofia Street, 1000 Sofia
Phone: (359) (2) 880-935, Fax: (359) (2) 988-8036

Stoyanov Mitov Tanev, Attorneys & Legal Advisors

82, Dondukov Boulevard, DAGA P.H., floor 5, 1504 Sofia
Phone/Fax: (359) (2) 943-4786, 756-335,
E-mail: smtlegal@bulgarvoice.com, Website: <http://smtlegal.bulgarvoice.com>

V.O.R.I.

55, Knjaz Boris I Street, 1000 Sofia
Phone: (359) (2) 987-7696, E-mail: vcheytanov@mb.bia-bg.com

d. Printing and Publishing Firms

Independent Information Agency LTD. NKIA

1 Bulgaria Sq.National Palace of Culture, Entr. A3, 1414 Sofia
Phone: (359)(2) 9166-3102, Fax: (359)(2) 657-497
E-mail:iia@online.bg

P&R Partners Ltd

31A, Cherni Vrakh Boulevard, 1000 Sofia
Phone: (359)(2) 658-310, Fax: (359)(2) 667-662
E-mail:pr partners@hotmail.com

e. Real Estate Firms

Aristo Real Estate Advisors

22, 6-th September Street, 1000 Sofia
Phone: (359)(2) 911-44, Fax: (359)(2) 981-3371

City-M Leasing Ltd.

5, Rilski Ezera Street, Apartment 2, 1407 Sofia
Phone: (359)(2) 629-108, Fax: (359)(2) 624-087

Continental Properties

7A, Aksakov Street, 4th Fl., 1000 Sofia
Phone: (359)(2) 981-2313, 981-3959, Fax: (359)(2) 986-7664

Construction-Investment Company "Sofia Estates"

60, Vassil Levski Street, 1000 Sofia
Phone: (359)(2) 981-5085, 981-5084, Fax: (359)(2) 981-5086

f. Trade Show and Conference Organizers

CIM – Company for International Meetings

18, Christo Belchev Street, 1000 Sofia
Phone: (359)(2) 981-0918, 980-8961, Fax: (359)(2) 981-9919
E-mail :cim@einet.bg

VIA EXPO

3, Anton Chehov square, 4003 Plovdiv
Phone/Fax: (359)(32) 960-012
E-mail:via-expo@mbox.digsys.bg

g. Other Service Providers

Institute for Strategic Investigations
40, Alabin Street, 1000 Sofia
Phone: (359)(2) 988-8212, 807-711, Fax: (359)(2) 980-8144

BBSS Gallup International
12, Gurko Street, 1000 Sofia
Phone: (359)(2) 980-5254, 986-3143, Fax: (359)(2) 986-3594
E-mail: gallup@aster.net

Snelling Personnel Services
199, Rakovski Street, 1000 Sofia
Phone: (359)(2) 963-3585, 963-3595, Fax: (359)(2) 963-3575
E-mail: snelling@snelling.bg

h. Additional Bulgarian Business Publications

nfo-business (published in English)
Bulgarian Chamber of Commerce and Industry
42, Parchevich St., 1040 Sofia
Phone: (359) (2) 987-7479, Fax: (359) (2) 987-3209
Website: <http://www.bcci.bg>

Bulgarian Foreign Trade (published in English)
P.O. Box 21, 1418 Sofia
Phone: (359) (2) 872-034, Fax: (359) (2) 981-9548
E-mail: ftp-bg@bgnet.bg

Sofia Western News
16 Batenberg St., 1000 Sofia
Phone: (359) (2) 815-698, Fax: (359) (2) 814-329
Website: <http://www.mobikom.com>

i. Online Versions of Bulgarian Publications

<http://www.bta-bg.net> Bulgarian Telegraph Agency
http://www-us.capital.bg/bp_digest/ Bulgarian Press Digest
<http://www.pari.bg> Pari newspaper
<http://www.capital.bg> Capital newspaper
<http://www.online.bg/banker> Banker newspaper
<http://www.standartnews.com> Standard newspaper
<http://www.zone168.com> Monitor newspaper
<http://cash.internet.bg.net/> Cash newspaper
<http://www.online.bg/sofiaecho> The Sofia Echo weekly newspaper in English
http://www.mobikom.com/sofia_westnews/Business/business.htm The Sofia Western News
monthly magazine in English
<http://www.bcemag.com> Business Central Europe

APPENDIX II. Useful Contacts in FYROM

1. Government Ministries

Ministry of Trade

Jurij Gagarin, 15, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 384-901, Fax: (389) (91) 384-902

Ministry of Transportation and Communications

Plostad Crvena Skopska Opstina, 4, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 123-292, Fax: (389) (91) 126-228

Ministry of Economy

Bote Bocevski, 9/3-4, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 119-628, Fax: (389) (91) 111-541

Ministry of Agriculture, Forestry

Forestry and Water Resource Management
Leninova, 2, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 113-045, Fax: (389) (91) 211-997

Ministry of Development

Bote Bocevski, 9/7-8, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 111-077, Fax: (389) (91) 112-799

Ministry of Finance

Dame Gruev, 14, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 116-140, Fax: (389) (91) 116-313

Ministry of Foreign Affairs

Dame Gruev, 6, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 119-190 or Fax: (389) (91) 115-790

Ministry of Science

Boulevard Ilinden, bb, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 238-610 or Fax: (389) (91) 235-573

Ministry of Defense

Orce Nikolov, bb, 91000, Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 112-872, Fax: (389) (91) 221-808

Ministry of Health

Vodnjanska, bb, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 231-128, Fax: (389) (91) 230-857

Ministry of Sports and Youth

Jurij Gagarin, 15, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 384-470, Fax: (389) (91) 384-472

Ministry of Labor and Social Welfare

Dame Gruev, 14, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 117-288

Ministry of Education & Physical Culture

Dimitrija Cupovski, bb, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 117-277, Fax: (389) (91) 118-414

Ministry of Culture

Bulevar Ilinden, bb, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 220-823, Fax: (389) (91) 225-810

Ministry of Urban Planning and Construction

Dame Gruev, 14, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 227-204, Fax: (389) (91) 117-163

Ministry of Justice & Administration

Dimitrija Cupovski, bb
91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 230-732, Fax: (389) (91) 226-975

Ministry of Information

Guro Gakovic, 64, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 114-162, Fax: (389) (91) 115-659

Ministry of Interior Affairs

Dimce Mircev, bb, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 221-972, Fax: (389) (91) 112-468

Ministry of Environment

Drezenska, 52, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 366-930, Fax: (389) (91) 366-931

2. FYROM's Government Offices

Prime Minister's Office

Boulevard Ilinden bb, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 115-389, Fax: (389) (91) 113-512

Agency for Transformation of Enterprises with Social Capital

Nikola Vapcarov, 7, PO Box 410, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 117-564, Fax: (389) (91) 126-022
E-Mail: agency@mpa.org.mk.

Investment Promotion Agency

Nikola Vapcarov, 7, P.O.BOX 410, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 117-564, 119-007, Fax: (389) (91) 126-022, 113-565

Economic Chamber of FYROM

Dimitrie Cupovski, 13, 91000, Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 227-814, Fax: (389) (91) 116-210

Bank Rehabilitation Agency

Kompleks Banki, bb, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 213-490, Fax: (389) (91) 222-427

Customs Administration

Lazar Licenovski, 13, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 224-467, Fax: (389) (91) 237-832

National Bank (Central Bank)

Kompleks Banki, bb, PO Box 401, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 112-177, Fax: (389) (91) 111-161

Statistical Office

Dame Gruev, 4/3/66, PO Box 506, 91000 Skopje, Former Yugoslav Republic of Macedonia

Phone: (389) (91) 115-022, Fax: (389) (91) 111-336

Payments Operations Service (ZPP)

Kompleks Banki, bb, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 228-102, Fax: (389) (91) 222-346

Protection of Industrial Property Office

Bulevar Ilinden, bb, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 220-232, Fax: (389) (91) 239-046

3. U.S. Government Contacts

Embassy of the United States of America

Department of Commerce / U.S. FCS
Boulevard Ilinden, bb, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 116-180 ext.172, Fax: (389) (91) 117-103

International Trade Administration

Mr. Jonathan Kimball, International Trade Specialist, U.S. Department of Commerce
14th and Constitution, NW, Washington, D.C. 20230
Phone: (202) 482-3684, Fax: (202) 482-4505

CEEbic

Ms. Jenny Gothard, International Trade Specialist, U.S. Department of Commerce
14th and Constitution, NW, Washington, D.C. 20230
Phone: (202) 482-2645, Fax: (202) 482-3898
Website: www.mac.doc.gov/eebic/Balkan/

U.S. Trade and Development Agency

Mr. Paul Marin, Project Manager
1621 North Kent Street, 200, Arlington, VA 22209-2131
Phone: (703) 875-4357, Fax: (703) 875-4009

U.S. Business Council for Southeastern Europe

Mr. Thorsten Knuttson, Executive Director
Wall Street Station, P.O. Box 1521, New York, NY 10268-1521
Phone: (212) 439-9025, Fax: (908) 439-9105

4. International Organizations

Delegation of the International Federation of the Red Cross and Red Crescent Societies

13, Koco Racin, 91000 Skopje
Phone: (389) (91) 114-355, Fax: (389) (91) 230-542

European Bank

14, Dame Gruev, 91000 Skopje
Phone: (389) (91) 134 – 39, Fax: (389) (91) 126-047

International Monetary Fund (IMF)

Kompleks Banki bb, 91000 Skopje
Phone:(389) (91) 121 – 034, Fax: (389) (91) 121-048

OSCE Spill over Monitor Mission

Mito Hadzivasilev - Jasmin bb, 91000 Skopje
Phone: (389) (91) 111-143, 112-413, Fax (389) (91) 111-267

The World Bank Resident Mission

Leninova 34, 91000 Skopje
Phone: (389) (91) 117-159, Fax: (389) (91) 117- 627

PHARE Implementation Office

Leninova 34, 91000 Skopje
Phone: (389) (91) 126-212 / 116-371, Fax: (389) (91) 126-213

UN High Commissioner for Refugees - UNHCR

Partizanski Odredi 63, 91000 Skopje
Phone: (389) (91) 366-482 / 366-485, Fax (389) (91) 366-483

UN Commissioner Human Rights Office

Voena Bolnica bul Ilinden bb PO Box 515, 91000 Skopje
Phone/Fax: (389) (91) 363-293

UNICEF Office

Rampo Levkata 2 PO Box 491, 91000 Skopje
Phone: (389) (91) 365-798 / 365-197, Fax (389) (91) 117-909

UN Preventive Deployment Forces, UNPREDEP Headquarters

Boulevard Ilinden bb, 91000 Skopje
Phone: (389) (91) 361-168, 364-086

5. Business Services Provides in FYROM - Accounting Firms

MBC Excel

Representing Andersen Worldwide, SC
Dame Gruev, 14/a, 1000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 214-700, Fax: (389) (91) 214-710

Deloitte & Touche

Dame Gruev, 16/7, 91000 Skopje, Former Yugoslav Republic of Macedonia
Phone: (389) (91) 111-300, Fax: (389) (91) 119-544

Coopers & Lybrand

Bulevar Marks i Engels, 3, P.O. Box 355, 91000 Skopje,
Phone: (389) (91)-116-638, Fax: (389) (91) 116-525

6. Market Research

Market information is available at

Website: <http://www.mchamber.org.mk/www1/m001.htm> & <http://www.mpa.org.mk/>

APPENDIX III. The Largest Foreign Investors in Bulgaria, by Sector

Mining

1. NAVAN BULGARIAN MINING (Ireland)
2. BRITISH GAZ EXPLORATION AND PRODUCTION (UK)
3. RHEINBRAUN (Germany)

Metallurgy

1. HALKOR (Greece)
2. UNION MINIERE (Belgium)
3. FAF METAL (Turkey)

Mechanical engineering

1. ATUSA (Spain)
2. CONSORTIUM FRANCE IRELAND (France)
3. DEN HAAN GROUP (Belgium)
4. EAGLE (USA)
5. EUROTECH (USA)
6. KONTRAKO (USA)
7. LIFTON (UK)
8. MAILER (Germany)
9. MESER GRISHEIM (Germany)
10. PLANZEE TIZIT (Austria)
11. WELDE (Austria)

Sanitation

1. AMERICAN STANDARD (USA)

Electrical engineering

2. ASEA BROWN BOVERI (Switzerland)
3. FESTO (Austria)
4. HYUNDAI (Korea)

5. KOSTRA DEVELOPMENT (Israel)
6. LIEBHERR (Germany)
7. MICHIGAN MAGNETICS (USA)
8. PRAMET (Czech Republic)
9. SCHNEIDER ELECTRIC (France)
10. SIEMENS (Germany)
11. SIGMA DELTA (Belgium)
12. SILWAY TECHNOLOGY (France)
13. SPARKY TRADING (Germany)
14. VIDEOTON HOLDING (Hungary)

Chemicals

1. FRANCE ARNE (France)
2. LUKOIL PETROL (Russia)
3. SOLVAY (Belgium)
4. WHITEBEAM HOLDING LTD (USA)

Pharmacy

1. BIOLAND (France)
2. DEUTSCHE BANK (Germany)
3. SWEDISH MATCH (Sweden)

Glass industry

1. BARECK OVERSEAS LTD. (Cyprus)
2. GLASINVEST LTD (Cyprus)

Building materials

1. BRAMACK DACHSYSTEME (Austria)
2. KERAMIK HOLDING (Switzerland)
3. KNAUF (Austria)
4. YTONG (Germany)

Cement industry

1. CEMENT FRANCAIS (France)
2. HEIDELBERGER ZEMENT (Germany)
3. HOLDERBANK (Switzerland)
4. PLEVCEM Ltd. (Cyprus)

Energy

1. ACCESS INTERNATIONAL (USA)
2. ENTERGY (USA)

Paper industry

1. ADUT-ADOX SKALICA (Slovak Rep.)
2. ISIKLAR HOLDING (Turkey)
3. NOREKOM GmbH (Germany)
4. PROFITECH ENTERPRISES (Cyprus)
5. **TRACE PAPER MILL (Greece)**

Textile

1. MARLAND INTERNATIONAL LTD (Ireland)
2. MASER (Turkey)
3. MIROGLIO (Italy)
4. SALVADORI (Italy)

Clothing

1. HAINER & PETER ROESLER (Germany)
2. ROLLMANN (Germany)
3. BRANDEX (Netherlands)

Breweries

1. **BREWINVEST (Greece)**
2. INTERBREW (Belgium)

Vine production

1. BOYAR INTERNATIONAL (UK)
2. SEABORD OVERSEAS (USA)
3. UNIBUL WINES (UK)
4. VINPROM SERVICE KORK (Portugal)

Food industry

1. **CHIPITA INTERNATIONAL (Greece)**
2. DANONE (France)
3. **DELTA (Greece)**
4. EASTSTARCH (Netherlands)
5. KLARINA HOLDING (Luxembourg)
6. KRAFT FOODS INTERNATIONAL (USA)
7. LUXCRAFT (UK)
8. NESTLE (Switzerland)
9. PROVIMI (Netherlands)
10. SOFTBUL INVESTMENT LTD (Cyprus)
11. **TKM FRUIT AND JUICE (Greece)**

Transport

1. FRANZ WELZ (Austria)
2. INTERLICHTER (Hungary)
3. M + M MILITSER INTERNATIONAL (Switzerland)
4. VAE (Austria)
5. WILLI BETZ (Germany)
6. ZEEVI HOLDING (Israel)

Telecommunications

1. CABLE AND WIRELESS (UK)
2. EASTERN MARKET TELECOM FUND LTD (Bahamas)
3. GLOBAL ONE HOLDING (Netherlands)

4. INTRACOM (Greece)

Tourism & Hotel

1. AUTO RICAMBI SRL (Italy)
2. CLASMAN ENTERPRISES (Cyprus)
3. CSN TOURISTIC AG (Germany)
4. DAEWOO CORPORATION (Korea)
5. HILTON INTERNATIONAL (USA)
6. HUN-EX (Hungary)
7. IVAN ZOGRAFSKI (Germany)
8. JOVANDA INTERNATIONAL Ltd. (USA)
9. PRINCESS HOLDING GROUP (Turkey)
10. VERIMARK MARKETING Ltd. (Cyprus)
11. WORLD TRADE COMPANY (USA)

Restaurants

1. **GOODYS (Greece)**
2. Mc DONALDS (USA)

Trade

1. DTS (USA)
2. **ENA (Greece)**
3. EUROBILLA (Austria)
4. G. FOGELSTETTER (Austria)
5. HUGO PFOHE (Germany)
6. INTERINVESTMENTS CORPORATION (USA)
7. KLOCKNER & CO AG (Germany)
8. KOMKO HOLDING (Switzerland)
9. METRO (Germany)
10. OMV (Austria)

11. RAO GAZPROM (Russia)
12. REGENT PACIFIC GROUP (UK)
13. ROSNEFT (Russia)
14. SHELL OVERSEAS HOLDINGS (UK)
15. STAMBOULI ENTERPRISES (Cyprus)
16. UKOS FINCONSULT (Cyprus)

Finance

1. ALICO (USA)
2. ALLIANZ (Germany)
3. **ALPHA BANK (Greece)**
4. BANQUE NATIONALE DE PARIS (France)
5. BEARING BROTHERS LTD (UK)
6. BONARKO LTD (Cyprus)
7. BULGARIAN AMERICAN INVESTMENT FUND (USA)
8. CARESBACK (USA)
9. CARGIL FINANCIAL MARKETS (UK)
10. CITIBANK (USA)
11. **COMMERCIAL BANK OF GREECE (Greece)**
12. CS FIRST BOSTON LTD (UK)
13. DEMIR BANK (Turkey)
14. DRESDNER BANK (Germany)
15. EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT (E.U)
16. EUROPEAN PRIVATISATION AND INVESTMENT COMPANY (Austria)
17. EVROBANK (Slovak Rep.)
18. HYPOVERENSBANK, SOFIA BRANCH (Germany)
19. ING-BANK (Netherlands)
20. LONDON INVESTMENT PARTNERS LTD (UK)
21. MUENICH RE (Germany)

22. NATIONAL BANK OF GREECE (Greece)

23. PARMAN CAPITAL INVESTMENTS (USA)

24. PROGRESS FINANCE CORPORATION (Cyprus)

25. RAIFFEISEN BANK (Austria)

26. REGENT PACIFIC GROUP LTD (UK)

27. SOCIETE GENERALE (France)

28. TC ZIRAAT BANK (Turkey)

29. TETRA INTERNATIONAL (Luxembourg)

30. TOKUDA CREDIT EXPRESS BANK (Japan)

31. UNICRADITO (Italy)

32. XIOSBANK (Greece)

Mass media

1. ANTENA (Greece)

2. NEWS CORPORATION (USA)

3. WESTDEUTSCHE ALLGEMEINE ZEITUNG (Germany)

Source: Foreign Investment Agency of Bulgaria (<http://www.bfia.org>)

APPENDIX IV. The Top Greek Investments in Bulgaria & FYROM

a. Top Greek Investments in Bulgaria

COMPANY NAME IN BULGARIA	COMPANY NAME IN BULGARIA
1.ADONIS MEGA	30.INTERFOODS (Papadopoulos)
2.AGROMET	31.INTERMODEN
3.AMPEREL LTD	32.INTERMODEN
4.AUTOTECHNIKA LTD	33.KARAT BULGARIA (Filippou Group)
5.AXON BULGARIA (Vardinogiannis Group)	34.KOSMOS TEXTIL
6.BALKAN RESTAURANT (Goody' s)	35.KOSMOTEX LTD
7.BELOVO AD PAPERMILL (Thraki Papermills)	36. LESKO OOD
8.BEST FOODS	37. METKO LTD
9.BLUE POINT LTD	38.NIKAS RODOPA (Nikas)
10.BULFANCO S.A	39.PAN EOOD
11.BULFON (Intracom)	40.PAGNEA EOOD
12.BULTEKS LTD	41.PLECENSKI CEMENT JSC (Titan Cement)
13.BULVARIA (Vardinogiannis Group)	42.RILATEX LTD
14.CHIPITA	43.SANTINEX
15.CLARINA BULGARIA (Coca Cola)	44.SAVELLA TEX
16.CONVOY LTD	45.SAVINIA EOOD
17.CRESNA TEXTILE (Ariadni S.A)	46.SOULIS BULGARIA LTD
18.DELTA BULGARIAN S.A (Delta Holding S.A)	47.SPACE LTD
19.DEMO BULGARIA	48.STIND SA (Yioula /Frigor /East)
20.DIKA	49.SUCCESS
21.DRUJBA S.A (Yioula-3E)	50.THREE P BULGARIA (Ipoma)
22.ENA BULGARIA	51.VENTA LTD
23.EVROCOMMERCE-95	52.VERDOSA LTD
24.FAROS	53.SOFIA MED
25.FEDON	54.NATIONAL BANK OF GREECE
26.FLORINA BULGARIA S.A (Florina Honaios)	55.INTERNATIONAL COM.BANK (Bulgaria AD)
27.GROSMAN LTD	56.BULGARIAN POST BANK (Eurobank)
28.HERMES TEXTILE	57.ETEBA (ETEBA Bank)
29.ILLMATEX	

Source: Economic Industrial Review, "Special Report for the 100 Diamonds of Greek Industry", Greek Monthly Periodical, July 2001.

b. Top Greek Investments in FYROM

COMPANY NAME IN FYROM	COMPANY NAME IN FYROM
1.STOPANSKA BANKA (National Bank of Greece)	8. NIKAS SKOP (Nikas)
2.OKTA (ELPE)	9.LARIN MRAMOR (Lazaridis Drama Marble)
3.PIVARA SKOPJE (Balkan Brew Hol)	10.MERMEREN KOMBINAT-PRILEP (Kyriakidis)
4.USJE (TITAN)	11.KRI-KRI KUMANOVO (Kri-Kri Industry)
5.STRUMICA TABAK (Michailides)	12.VERO (Veropoulos)
6.KOCANI TABAK (Michailides)	14.TORRE Skopje (TORRE E. Glatounis S.A)
7.KREDITNA BANKA (Alpha BANK)	15.ZLATIS (Zlatis Sausages S.A)

Source: Economic Industrial Review, "Special Report for the 100 Diamonds of Greek Industry", Greek Monthly Periodical, July 2001.

APPENDIX V. Greek Investments in FYROM**Organization Name: KREDINTA BANKA**

Address: ul. Dame Gruev, Po Box 564 -1000-Skopje
Phone Number: (+389 2) 116-433, Fax Number: (+389 2) 116-830
Contact Name: Mr. Jan Iordanidis, General Director
Field: SERVICE (SRV), Banking
Details: Takeover by ALPHA BANK of 65% of the shares of "KREDITNA BANKA".

Organization Name: USJE A.D.

Address: ul. Provamajska bb-1000-Skopje
Phone Number: (+389 2) 783-688, Fax Number: (+389 2) 421-075
Contact Name: Mr. konst. Mitsiou, General Manager
Field: PRODUCTION (PRD), Cement
Details: Takeover by TITAN (July 1998) in common with HOLDERBANK (SWI) of 80% of share of USJE.

Organization Name: PIVARA SKOPJE

Address: ul. 808 b. 12-1000-Skopje
Phone Number: (+389 2) 611-279, Fax Number: (+389 2) 611-482
Contact Name: Mr. Sveto Janevski-General Manager
Field: PRD, Brewery
Details: Takeover of PIRAVA SKOPJE (51% shares) from BALKANBREW, which is a Joint Venture of Athenian Brewery & Hellenic Bottling.

Organization Name: ZITO LUKS

Address: ul. V. Gjorkov 11-1000-Skopje
Phone Number: (+389 2) 238-155, 113-088, Fax Number: (+389 2) 213-1663
Contact Name: Mr. Jan Kavalieratos, General Manager
Field: PRD, Bakery Products
Details: Purchase by "Hellenic Biscuit Co. S.A." (Athens) of "ZITO-LUKS.

Organization Name: LARID A.D. Skopje

Address: ul. Ankarska 29 a. Lok.32-34 -1000-Skopje
Phone Number: (+389 2) 362-365, Fax Number: (+389 2) 362-365
Contact Name: Mr. Dimitar Hristov, Director
Field: PRD, Marble
Details: Joint Venture LAZARIDIS (85% Greek). Surface extraction started in '97, marble is sent to Greece.

Organization Name: MERMEREN KOBINAT

Address: ul. Marshal Tito br. 222-7500-Prilep
Phone Number: (+389) (98) 279-40, 279-41, Fax Number: (+389 2) 329-98
Contact Name: Mr. Giorgos Sintros, Director
Field: PRD, marble
Details: Takeover by Kyriakidis (90% of the shares).

Organization Name: KOCANI TABAK (ex JUCOTUTUN)

Address: ul. Nikola Karev 25 -2300-Korani
Phone Number: (+289) (903) 221-02, 210-07, 221-94, Fax Number: (+289) (903) 223-58
Field: PRD, Cigarettes
Details: Takeover by SRUMICA TABAK (MICHAILIDIS) of JUFOTUTUN (new name KOCANI TABAK since April 2000).

Organization Name: SRUMICA TABAK

Address: ul. V. Kitanov b.1-2400-Strumica
 Phone Number:(+389) (902) 266-25, Fax Number (+389) (02) 239-12
 Field: PRD, Tobacco

Organization Name: PETZETAKIS Makedonian Plastics

Address: ul. Vas Kosulceva bb-1400-Veles
 Phone Number: (+389) (43) 212-401, 212-402, Fax Number: (+389) (43) 212-403
 Contact Name: Mr.Mic. Leonidis, Mechanical Engineer
 Field: PRD, TRD, Dairy products
 Details: Production & Trade with plastics (100% Greek), establishment on May 2000.
 Details:Takeover, by MICHAILIDIS of Strumica Tabak, investments in new technology (1997).

Organization Name: VERO SUPER MARKET

Address: ul. Jane Sandnski 111 - 1000-Skopje
 Phone Number: (+389 2) 447-610, 375-747, Fax Number: (+389 2) 162-390
 Contact Name: Mr. K. Theodossiadis, General Manager
 Field: SRD, Super market
 Details: Opening by VEROPOULOS BROS, of 2 super market in Skopje (Karpos-Aerodrom) and one in Tetovo.

Organization Name: KRI-KRI D.O.O.

Address: Bul. Vera Kotroska, Dobrosane-1300-Kumanovo
 Phone/Fax Number: (+389) (901) 451-300
 Contact Name: Mr. Giorgos Zevrantis, Marketing Director
 Field: PRD, daily products
 Details: Joint-Venture by KRI-KRI Milk Industry, Production of yoghurt & ice-cream (1992).

Organization Name: NIKAS SKOP

Address: Nasell Llinden, kaj Hotel Belvi-1000-Skopje
 Phone Number: (+389 2) 572-668, Fax Number: (+389 2) 572-664
 Contact Name: Mr. Boris Lazarov, General Director
 Field: PRD, Sausage
 Details: Production unit for sausage.

Organization Name: TORRE

Address: ul. Skupi 47-1000-Skopje
 Phone Number: (+389 2) 332-092, Fax Number: (+389 2) 331-092
 Contact Name: Mr. Ang. Vlahavas-Com. Director
 Field: PRD, Production of ice-cream
 Details: Joint-Venture TORRE-Glatsounis (51%) with TERMOSKOPJE.

Organization Name: BALIS SUPER MARKET

Address: ul.Marsal Tito bb-7000-Bitola
 Phone Number: (+389) (97) 222-262, Fax Number: (+389) (97) 229-262
 Contact Name: Mr. K. Tosounidis, General Director
 Field: SRV, supermarket
 Details: Opening by BALIS (Trikala) of a supermarket in Bitola.

Organization Name: CBL Papageorglou

Address: ul. Ivo Lola Ribar. bb-7000-Bitola
 Phone Number: (+389) (97)228- 585 , Fax Number: (+389) (97) 228-585
 Contact Name: Mr. S. Dermisovski, General Director
 Field: PRD, clothes
 Details: Establishment of CBL by CBL Papageorgiou (Frankfurt), production (facon) of leather clothes.

Organization Name: DIMOUVELIS

Address: ul. Marsal Tito 165-1484-Bogdanci

Phone Number: (+389) (34) 221-031, Fax Number: (+389) (34) 221-031
Contact Name: Mr. Andreas Stergiou, Manager
Field: PRD, clothes
Details: Establishment of factory of clothes production (facon of denim trousers). Exclusive importer BIG STAR.

Organization Name: Emporio Ltd

Address: ul. Marsal Tito bb-1062-Radovis
Phone Number: (+389) (902) 601-260, 601-583, Fax Number: (+389) (902) 601-260
Contact Name: Mr. Hristos Milonas, Manager
Field: PRD, clothes
Detail: Production of ready made clothes.

Organization Name: GRANTS

Address: ul. Kllment Ohridski -2400-Srtumica
Phone Number: (+389)(902) 345-240, Fax Number: (+389) (902) 345-322
Contact Name: Mrs. Maria Nikolaou, Manager
Field: PRD, clothes
Details: Production lines for clothes in Stumica, Valandovo & Berovo.
Organization name: HELMATEX
Address: ul. Goca Delcev bb -2400-Stymica
Phone Number: (+389) (902) 344-598, 346-598, Fax Number: (+389) (902) 344-598
Contact Name: Mr. Konst. Garsidis, Manager
Field: PRD, textile
Details: Joint - Venture (57% Greek). Production of bed linen (1997). Exports to Greece & Serbia.

Organization Name: JOYCE

Address: ul-1480-Gevgelija
Phone Number: (+389) (34) 212-030
Field: PRD, clothes
Details: Establishment of factory producing clothes (shirts, trousers, jackets) (JOYCE, Thessaloniki).

Organization Name: KAOL ATH. NATSIS & CO

Address: Kruzevski pat bb-7500-Prilep
Phone Number: (+389) (98) 221-40, Fax Number: (+389) (98) 221-41
Contact Name: Mr. Ath. Natsis, Owner
Field: PRD, clothes
Details: Production of clothes, facon.

Organization Name: KAVASKO Ltd

Address: ul. Industriska bb -1440-Negotino
Phone Number: (+389) (93) 365-028, 365-128, Fax Number: (+389) (93) 365-028
Contact Name: Mr. Savvas Foundoukis, General Director
Field: PRD, clothes
Details: Joint-Venture by LASKOU S.A. Production of (facon) clothes.

Organization Name: KONST. LEGERAS DOOEL

Address: ul. Lence Kodinski br. 50 -7500-Prilep
Phone / Fax Number: (+389) (98) 22-140
Contact Name-Mr. Kons. Legeras, Owner
Field: PRD, clothes
Details: Production of clothes (facon).

Organization Name: MIKOTEKS

Address: ul. Prileska 70a, Mokel-7000-Bitola
Phone Number: (+389) (97) 251-999

Contact Name: Mr. Mihos, General Manager
Field: PRD, clothes
Details: Production of (facon), sport clothes PUMA.

Organization Name: RODON Ltd.

Address: ul. Industriski pat bb. Javor D.C.-7000-Bitola
Phone Number: (+389) (97) 225-051, 221-835, Fax Number: (+389) (97) 225- 051
Contact Name: Mr. Spyros Ginis, General Manager
Field: PRD, clothes
Details: Production (facon) of women & men's clothes (1996). Exports to Greece, Italy, Denmark, Germany, Sweden.

Organization Name: SAT MODA

Address: ul. Gjorce Petrov bb. - 7000-Bitola
Phone Number: (+389) (97) 229-766, 225-992, Fax Number: (+389) (97) 225-992
Contact Name-Mr. Stavros Saitis-Gen. Manager
Field: PRD, clothes
Details: Production of (facon) clothes (1994).

Organization Name: STEFANOS NIAKAS

Address: ul. Pijali 2/11-7500-Prilep
Phone/Fax Number: (+389) (98) 217-72
Contact Name: Mr. Stefanos Niakas, Manager
Field: PRD, clothes
Details: Production of clothes (facon).

Organization Name: AMADEL

Address: ul. Industriska br. 8 Macizari -1000-Skopje
Phone Number: (+389 2) 551-563, Fax Number: (+389 2) 551-562
Contact Name: Mr. Mih. Triantafylou, General Manager
Field: PRD, TRADE (TRD), nuts
Detail: Production unit for nuts.

Organization Name: ARTEMIS

Address: ul. Blagoj Muceto 35-2400-Srtumica
Phone Number: (+389) (902) 324-68
Contact Name: Mr. Vasilis Karakolis, Manager
Field: PRD, TRD candies
Details: Production of sweets, patisserie.

Organization Name: MELIN

Address: ul. Nikola Karev b.b. -1450-Valondovo
Phone Number: (+389) (902) 382-858, Fax Number: (+389) (902) 381-004
Contact Name: Mr. Blaze Savovski, Manager
Field: PRD, candies, halva, marmalade
Details: Production of sweets, locums,& Halva "Salonikos".

Organization Name: KRONER STAR

Address: ul. Lerinska 9-7000-Bitola
Phone Number: (+389) (97) 284-022, Fax Number: (+389) (97) 170-292
Contact Name: Mr. Laz Marvoudis, General Manager
Field: PRD, Beverages
Details: Joint-Ventures with local partner. Factory for production of beverages.

Organization Name: MARIO TD

Address: ul.-1480-Gevgelija
Contact Name: Aristidis Katavenis, General Manager

Field: PRD, Snails

Details: Joint-Venture which produces snails, in cooperation with VINOJUG-Gevgelija.

Organization Name: SUCCESS BROKERS

Address: ul. Marsal Tito 19-1480-Gevgelija

Phone Number: (+389 2) 113-020, 220-471, Fax Number: (+389 2) 1130-20, 220-471

Contact Name: Mr. St. Vasilopoulos, Economic Director

Field: PRD, coffee

Details: The company has a production unit for coffee ("Paskalin Company d.o.o. in Gevgelija) and a trade company named "Success Distribution d.o.o."

Organization Name: A + B PLAST

Address: 1480-Gevgelija

Phone Number: (+389) (34) 211-241, Fax Number: (+389) (34) 211-241

Contact Name: Mr. G. Kehaglopoulou, Manager

Field: PRD, shoe parts

Details: Establishment of factory producing shoe parts.

Organization Name: MELIZA

Address: ul. Deko Kovacev b.b.-1480-Gevgelija

Phone Number: (+389) (34) 211-370

Contact Name: Mr. George Stogidis, General Manager

Field: PRD, perfumes

Details: Production of various types of perfumes.

Organization Name: HERMES

Address: buil. AVNOJ br. 60-1000-Skopje

Phone Number: (+389 2) 444-84, Fax Number: (+389 2) 444-829

Contact Name: Mr. Ilias Andronikidis, General Manager

Field: SRV, Inter, Forwarding

Details: Opening by HERMES AGENCIES ltd (Thessaloniki) of a representative office for international forwarding & customs clearance.

Organization Name: ORBIT Ltd

Address: Madzerl -1000-Skopje

Phone Number: (+389 2) 550-861, Fax Number: (+3892) 551-550

Contact Name: Mr. Th. Vlachos, General Manager

Field: SRV, Inter. Forwarding

Details: Opening by ORFEE BENOGLU S.A. of a representative office for international forwarding and customer clearance.

Organization Name: ERNEST & YOUNG

Address: 1000-Skopje

Phone Number: (+389 2) 111- 637, Fax Number: (+389 2) 113-438

Contact Name: Mr. Koufakis, Business Consultant

Field: SRV, Business Lawyers

Details: Opening of a representative office for business consultant services.

Organization Name: IKRP ROKAS & PARTNERS

Address: ul. Vasil Gjorgov 20/2-1000-Skopje

Phone Number: (+389 2) 298-280, 298-282, Fax Number: (+389 2) 225-089

Contact Name: Mr. Dim. Raptopoulos, Business Consultant

Field: SRV, Bus. Lawyers

Details: Opening a representative office for business consultant services

Organization Name: DIPAPA

Address: ul. Zlatko Snaider 6 -1000-Skopje

Phone Number: (+389 2) 227-031, Fax Number: (+389 2) 227-031

Contact Name: Mr. Dion. Papadopoulos, Manager

Field: SRV, Art design

Details: Opening by Mr. Papadopoulos of an art design studio for architecture, decoration, printing.

Source: Hellenic Liaison Office in SCOPJE (OEY)

APPENDIX VI. Bulgaria's Law on Foreign Investment**Law on Foreign Investment**

Published in the State Gazette issue No 97, of 1997, corrected, SG No 99, of 1997, supplemented, SG No 29 of 1998, amended and supplemented, SG No 153 of 1998, No 110 of 1999.

Chapter OneGeneral Provisions

ART. 1 This law shall govern the terms and procedures for making investments by foreign persons in the country and the protection of those investments, as well as the conditions and procedures for the implementation of priority investment projects.

ART. 2 A foreign person shall make investments in the country under the terms set out for Bulgarian persons and shall have equal rights with them, unless otherwise provided by law.

ART. 3 (1) Where an international agreement, to which the Republic of Bulgaria is a party, provides for more favorable terms for undertaking of economic activities by foreign persons, the more favorable terms under the international agreement shall apply.

(2) The provisions of this law shall not apply, in whole or in part, for investments by discriminatory measures are applied with regard to Bulgarian companies or nationals.

ART. 4 With regard to foreign investments made prior to changes in the Law, introducing regulatory restrictions solely on foreign investments, the legal regulations in force at the moment the investments were made shall apply.

ART. 5 (1) For the purposes of this law, a foreign person shall be:

1. a legal person which is not registered in the Republic of Bulgaria,
2. a company which is not a legal person and is registered abroad,
3. a natural person - a foreign national with a permanent residence abroad.

(2) A Bulgarian national with permanent residence abroad, who holds another nationality, shall choose whether to avail himself of the status of a Bulgarian or foreign national under this law.

ART. 6 (1) Foreign persons, who have the right to carry on business activities under their national legislation, may open in the country trade representation offices, which must be registered at the Bulgarian Chamber of Commerce and Industry.

(2) The representation offices under paragraph 1 hereinabove are not legal persons and may not carry on economic activities.

(3) Transactions of foreign persons with local persons for the needs of representation office registered under paragraph 1 hereinabove shall be subject to the rules on transactions between local person.

ART. 7 A foreign natural person or a company which is not a legal person may open a branch, provided it (the person/the company) is registered with the right to carry on business activities under

its national law. The branch shall be entered into the commercial register at the district court, where the branch's seat is located.

ART. 8 (1) A company with foreign participation shall have all the rights of a company without foreign participation, except for the cases provided for in this law.

(2) The amount of foreign participation in newly-formed or existing companies shall not be limited.

ART. 9 (1) A foreign natural person must hold a permit for permanent residence in the cases where, for the purpose of carrying on economic activities:

1. he registers as a sole trader,
2. he participates in a co-operative,
3. he participates in a general partnership,
4. he participates as a partner with unlimited liability in a limited partnership or in a limited partnership with shares.

(2) (Amended SG No 153 of 1998) The right to a permanent residence of a foreign person under paragraph 1 may be withdrawn by the Minister of Interior or by authorized by him officials only in the cases provided for by Law. The administrative act, by virtue of which the right to a permanent residence is being revoked, shall be subject to appeal before the Court in accordance with the Law on Administrative Proceeding.

Chapter Two

FOREIGN INVESTMENT AGENCY

ART. 10 (1) The Foreign Investment Agency shall be a State body with the Council of Ministers for co-ordination of the activities of State institutions in the field of foreign investments and for encouragement of foreign investments and of priority investment projects.

(2) The Agency shall be a legal person, financed by the State budget, seated in Sofia and shall have regional divisions.

ART. 11 (1) The Agency shall set up and maintain a Unified Information System, where data about all foreign investments in the country shall be compiled.

(2) The Ministry of Finance, the National Statistical Institute, the Central Depository and the Bulgarian National Bank shall submit at the end of each calendar quarter summarized data concerning the type and volume of foreign investments, for the purposes of the Unified Information System for Foreign Investments. Other central and local authorities shall provide information at the request of the Foreign Investment Agency.

(3) The Foreign Investment Agency shall provide with information from the Unified Information System for Foreign Investments state bodies and other interested parties on the terms set out in the Regulations on the Structure and Activities of FIA. Chapter Three

Chapter Three

FOREIGN INVESTMENTS

ART. 12 (1) For the purpose of this law, a foreign investment shall be any investment by a foreign person or its branch in:

1. shares and stakes in commercial companies,

2. ownership title over buildings and limited ownership title over property,
3. ownership title and limited ownership title over movable property where considered long-term tangible assets,
4. ownership title over an enterprise, or detached parts thereof, within the stipulations of the Law on Restructuring and Privatization of State-Owned and Municipal Enterprises,
5. securities, including debentures and Treasury bonds, as well as their derivative instruments issued by the State, by the municipalities or by other Bulgarian legal persons, with a remaining term until maturity not shorter than 6 months,
6. loans, also in the form of financial leasing, for a term not shorter than 12 months,
7. intellectual property title - articles of copyright and kindred rights, patentable inventions, utility models, trade marks, service marks and industrial designs,
8. rights stemming from concession contracts and contracts for the assigning of management.

(2) The foreign investment shall also include the increase in the value of the investment under paragraph 1 hereinabove.

ART. 13 The branches of foreign persons and the companies, in which foreign persons participate directly or through other companies with foreign participation, shall submit to the National Statistical Institute summarized data about foreign investments, in accordance with the Law on Statistics.

ART. 14 (Repealed SG No 153 of 1998)

ART. 15 (Repealed SG No 153 of 1998)

ART. 16 (Repealed SG No 153 of 1998)

ART. 17 (Repealed SG No 153 of 1998)

ART. 18 (Repealed SG No 153 of 1998)

ART. 19 (Repealed SG No 153 of 1998)

ART. 20 (Repealed SG No 153 of 1998)

ART. 21 (Amended SG No 153 of 1998) At the request of the investor, the Foreign Investment Agency may propose to the Council of Ministers to form an inter-ministerial group, comprising representatives of ministries and agencies concerned, in order to provide institutional support for appointed investment projects and which projects may be acknowledged by the Council of Ministers as priority ones.

ART. 22 (1) At the request of the investor, the Foreign Investment Agency may propose to the competent authorities to transfer limited property rights on real property which is private State or municipal property, with the view of the implementation of a priority investment project.

(2) The proposed investment project shall be deemed an integral part of the contract for transfer of the limited ownership right. In that case, Art. 57, paragraph 1 of the Law on State Property and Art. 40, paragraph 1 of the Law on Municipal Property shall not apply.

Chapter Five

PROPERTY RIGHTS

ART. 23 (1) A foreign person may acquire ownership titles and limited ownership titles over property.

(2) A foreign person may not acquire an ownership title over land, including such acquisition through a branch or in a sole trader capacity.

ART. 24 (1) A foreign person must obtain a permit for the acquisition of ownership title over buildings and limited ownership titles on properties in the area of border zones and other areas as determined by the Council of Ministers, related to the national security.

(2) A company with foreign participation must obtain a permit for the acquisition of the right to ownership and limited ownership property titles in the area of border zones and in other areas as determined by the Council of Ministers, related to the national security.

(3) Permits under paragraphs 1 and 2 hereinabove shall be issued by the Council of Ministers or its authorized body, which shall make a pronouncement on the application within 45 days. Refusal to grant a permit shall be motivated.

ART. 25 Transactions made in breach of articles 23 and 24 hereinabove, or through a proxy, shall be declared null and void by means of a court ruling after a motion brought by the Public Prosecutor or by the parties concerned.

ART. 26 (1) Properties owned by a foreign person may only be alienated on the grounds of a law for particularly important needs of the State, which cannot be satisfied in any other way, and only after an advance and equitable compensation at market prices.

(2) Properties for indemnification must be equal to the alienated property and must be located in its vicinity, or, with the consent of the owner - at a different place. Where compensation consists in property, the difference in values shall be covered by the owner or by the State.

(3) If the foreign person so agrees, the compensation may be pecuniary.

(4) To the extent that the present section does not contain special provisions, the provisions of Chapter Three of the Law on State Property shall apply.

Chapter Six

SPECIAL PROVISIONS

ART. 27 (1) A foreign person may transfer and/or buy in order to transfer foreign currency abroad, after submission a certificate for paid taxes, in the following cases:

1. income generated through an investment,
2. property alienation driven indemnification proceeds, when for State needs,
3. liquidation quota resulting from the termination of the investment,
4. proceeds from the sale of the investment good,
5. a sum received after the enforcement of a writ of execution.

(2) The right under paragraph 1 hereinabove may also be exercised by foreign nationals working in the country, in respect of the remuneration received by them, and by foreign natural persons under Art. 9, paragraph 1, after a certificate for paid taxes is submitted.

ART. 28. (1) A foreign person may open accounts, make deposits in foreign currency and in Levs in banks, as well as dispose of shares, debentures and other securities.

(2) The claims of a foreign person in Levs and in foreign currency may be secured by means of a pledge or mortgage. No permit from a State authority shall be required to enlist a mortgage.

(3) The transactions of a foreign person entered into through a branch, shall be subject to the rulings valid for local persons.

(4) Where local persons have the right to make payments in foreign currency abroad in favor of foreign persons, those payments may also be effected in the country, including by means of checks, promissory notes and bills of exchange.

ART. 29 The labor relations between a company with foreign participation, as well as a branch or representation office of a foreign person, and the employees who are foreign nationals, shall be governed by the contracts of employment. The contract of employment cannot derogate from Bulgarian labor legislation in respect of the following elements:

1. written form of the contract,
2. maximum duration of working time, minimum duration of rests in-between two days and in-between two weeks, and duration of the annual full-pay leave,
3. minimum wage established for the country,
4. minimum time-limit for the notice of termination of the contract of employment, where this is negotiated or is required by the law, as well as the minimum amount of indemnity where the contract of employment is terminated with or without advance notice,
5. liability of the employer for damages inflicted as a result of an labor accident or professional illness,
6. rules of hygiene and safety at work.

ART. 30 (Amended SG No 110 of 1999) Employees who are foreign nationals shall be insured in accordance with the Bulgarian legislation.

ART. 31 Labor disputes between employers under Art. 29 and employees who are foreign nationals shall be resolved in accordance with the contract of employment.

ART. 32 (Amended SG No 110 of 1999) On all matters pertaining to the labor relations with an employer under Art. 29, which are not explicitly governed by the contract of employment, Bulgarian legislation shall apply.

Chapter Seven

ADMINISTRATIVE PENAL PROVISIONS

ART. 33 (1) Any bank which effects a transfer of foreign currency, where the certificates required under Art. 27 above have not been submitted, shall be liable to a pecuniary sanction equal to the amount of the transfer made.

(2) Where the offence under subsection 1 above is repeated, the pecuniary sanction shall be imposed in a double amount.

ART. 34 (1) The penal acts for recorded offences under Art. 33 shall be drafted by persons authorized by the Deputy Governor of the Bulgarian National Bank in charge of the Banking Supervision Department, and the penal orders shall be issued by the Deputy Governor or by a person authorized by him.

(2) The drafting of acts, the issuance, the appeal against and the enforcement of penal orders shall be made in accordance with the Law on Administrative Violations and Penalties.

FINAL PROVISIONS

§ 1. This Law repeals the Promotion and Protection of Law on Foreign Investments (published, State Gazette, issue 8 of 1992, amended, issues 92 and 102 of 1995, issue 109 of 1996, corrigendum, issue 110 of 1996, amended, issues 55 and 58 of 1997).

§ 2. The Law on Statistics (published, State Gazette, issue 25 of 1991, amended, issue 64 of 1991 and issue 60 of 1992) is amended as follows:

- a. In Art. 21, the words "five hundred to one thousand" are replaced with "80.000 to 600.000".
- b. In Art. 22, the words "from one thousand to one-thousand and five hundred" are replaced with "600.000 to 2.000.000".
- c. In Art. 23, the words "one thousand to two thousand" are replaced with "1.000.000 to 2.000.000".
- d. In Art. 24, the words "five thousand to ten thousand" are replaced with "from 1.000.000 to 3.000.000".

§ 3. Within two months after the entry into force of this law the National Statistical Institute shall develop a methodology in accordance with which statistical information shall be produced about foreign investments and which shall be in conformity with international standards.

§ 4. Companies with foreign participation which have made imports under the conditions of Art. 15a of the Law on Promotion and Protection of Foreign Investments, as prescribed by § 1, shall submit to the customs authorities a court ruling for inclusion of the contribution in kind in the company's capital within 6 months from the of entry of the law into force.

§ 4a. (Supplemented, Official Gazette issue No 51 of 1998) Beyond the cases of the precedent paragraph, Art. 14, 15 and 17 of this Law do not apply to goods imported under the conditions of temporary import as of 24.10.1997.

§ 5. In cases where a tax relief is used under other laws, the provision of Art. 20 above shall apply for the remainder of the 10-year period.

§ 6. Within two months from the date of entry of the law into force the Council of Ministers shall adopt Rules for the Organization and Activities of the Foreign Investment Agency.

§ 7. Within one month as from the entry of the law into force the Council of Ministers shall publish a list under Art. 18, subparagraph 3 which shall be updated annually.

§ 8. The implementation of this law is entrusted to the Council of Ministers. The Minister of Finance shall exercise supervision as regards the implementation of sections 14 to 17.

§ 9. The law shall come into effect as from the date of its promulgation in the State Gazette.

The law was passed by the XXXVIIIth National Assembly on 16 October 1997 and the State seal is affixed hereto.

Chairman of the National Assembly

Yordan Sokolov

Source: Foreign investment Agency (<http://www.bfia.org>)

9. ABBREVIATIONS & ACRONYMS

- AMPI:** Additional Mandatory Pension Insurance
- ASNOM:** Anti Fascist Liberation Council of Macedonia
- BBA:** Balkan Bulgarian Airlines
- BCCI:** Bulgaria Chamber of Commerce and Industry
- BCA:** Branch Collective Agreements
- BDD:** Business Development Director
- BDZ:** Bulgarian Railway Company
- B.E.F:** Bulgarian Economic Forum
- B.F.I.A:** Bulgarian Foreign Investment Agency
- BIBA:** Bulgarian Investment Business Association
- BNB:** Bulgarian National Bank
- BOT:** Builds, Operates, Transfers
- BRA:** Bank Rehabilitation Agency
- BS.E:** Bulgarian Stock Exchange
- B.S.P:** Bulgarian Socialist Party
- BTC:** Bulgarian Telecommunications Company
- CBA:** Currency Board Agreement
- CEE:** Central East European
- CEEC:** Central & Eastern European Countries
- CEFTA:** Central European Free Trade Agreement
- CEO:** Chief Executive Officer
- CMP:** Center Mass Privatization
- CPA:** Certified Public Account
- CPI:** Consumer Price Index
- CITA:** Corporate Income Tax Act
- DA:** Democratic Alternative

DPA: Democratic Party for Albanians

DON: Digital Overlay Network

EC: European Commission

ECA: Employer Collective Agreements

ECMR: European Community Merger Regulation

EFTA: European Free Trade Agreement

EBRD: European Bank for Reconstruction and Development

EIB: European Investment Bank

EU: European Union

FDI: Foreign Direct Investment

FIFO: First In First Out

FRY: Federal Republic of Yugoslavia

FTZ: Free Trade Zone

FYROM: Former Yugoslavia Republic of Macedonia

GCA: General Collective Agreement

GDP: Gross Domestic Product

GNP: Gross National Product

GRA: General Road Administration

IAS: International Account Standards

IASC: International Accounting Standards Committee

IBD: International Business Director

IBRD: International Bank of Reconstruction and Development

IDA: International Development Association

IFAC: International Fed of Accounts

IFC: International Finance Corporation

IMF: International Monetary Fund

IMRO: Internal Macedonian Reconstruction Organization

IRR: Internal Rate of Return

ISA: International Standard of Auditing

LBO: Leveraged Buy Out

LDP: Liberal Democratic Party

L.E.P.E: Law on Energy and the Power Efficiency

LIFO: Last in First Out

L.S.P: Large Scale Privatization

L.T.A: Long Term Assets

MEBOS: Management Employee Buy Outs

MEC: Management Employee Companies

MIGA: Multilateral Investment Guarantee Agency

MIPA: Macedonian Investment Promotion Agency

MPA: Macedonian Privatization Agency

MPP: Mass Privatization Program

NATO: North Atlantic Treaty Organization

NAS: National Account Standards

NBM: National Bank of Macedonia

NEK: National Elect Company

NEPA: National Enterprise Promotion Agency

NGO: Newly Government Organization

NPV: Net Present Value

NSA: National Standard Auditing

OECD: Organization for Economic Co-operation Countries

OSCE: Organization for Security and Cooperation in Europe

PA: Privatization Agency

PAYG: Pay-As-You-Go

PDP: Party for Democratic Prosperity

PITA: Personal Income Tax Act

POSA: Public Offering of Securities Act

PPP: Purchasing Power Parity

PRO: Public Revenue Office

R&D: Research & Development

ROI: Return on Investment

SAD: Single Administrative Document

SBDI: South Balkan Development Initiative

SBU: Strategic Business Unit

SCER: State Commission of Energy Regulation

SDSM: Social Democratic Alliance of Macedonia (former Communist Party)

SECI: Southeast Europe Cooperation Initiative

SEEAP: South East European Regional Action Plan

SISA: State Insurance Supervision Agency

SFRY: Socialist Federal Republic of Yugoslavia

SP: Socialist Party of Macedonia

SRM: Union of Romanies of Macedonia.

SRP: Special Restructuring Program

SWOT: Strength, Weaknesses, Opportunities, Threats

TDA: Trade & Development Agency

TDS: Total Debt Services

TEM: Trans European Motorway

UDF: Union of Democratic Forces

U.K: United Kingdom

ULC: Unit Labor Cost

UMRO: International Macedonian Revolutionary Organization

UNCTAD: United Nations Conference on Trade and Development

UNO: United Nations Organization

USA: United States of America

USAID: United States Agency for International Development

USIS: United States Information Service

USLO: United States Liaison Office

VAT: Value Added Tax

VMRO-DPMNE: Internal Macedonian Revolutionary Organization – Democratic Party for Macedonian National Unity

VMRO- VMRO: Internal Macedonian Revolutionary Organization – True Macedonian Reform Option

WIPO: World Intellectual Property Organization

WTO: World Trade Organization.

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