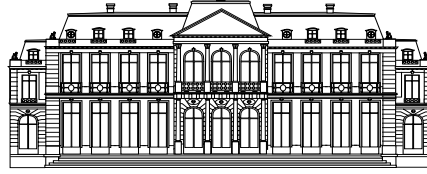


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in co-operation with the Bulgarian Centre for Economic Development

**A REVIEW OF BULGARIAN
PRIVATISATION**

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The capital market and the privatisation

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THE CAPITAL MARKET AND THE PRIVATISATION

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The privatisation as a process of transformation of the state-owned and municipal property and its adjustment to the principles of capital type of management in the conditions of a market economy cannot and should not be considered separate from the principles, problems and the dynamics of the capital market. Should the approach to the privatisation be as if it were only a purely administrative problem, then the actual change of the title over the ownership would not be a problem. But the principally important problem is not the writing off of the assets as a state ownership itself, but the creation of the necessary conditions and premises that capital to be developing and to grow in compliance with the laws of the market and in the interest of the society. From that viewpoint, when considering the privatisation as an economic process in the context of the entire transformation of the economy, the capital market is the natural environment where the capital may be found and be concentrated in its real owner and at that on purely economic basis, without any administrative intervention and under full transparency and in compliance with the laws of the market.

The capital market also provides the most efficient privatisation technique with respect to the most discussed features of any privatisation deal - time price, transparency, equal terms of access for the participants. Such privatisation technique, of course, is suitable most of all for companies with good market positions and image which do not need a strategic investor, with the selling of minority block of shares as well as with decapitalized companies which need fresh cash resources at diversified investment risk. But in so far as the strategic investors are also directly connected with the capital market along the lines of the formation of their investment resources and the investment portfolio's optimisation, as well as with regard to the diversification of the risk of the relevant direct investment, the condition and the development of that market have an immediate influence on the development of the privatisation process itself. All that requires very hard work for the market's enhancement and stabilisation, to strengthen the investors' confidence in it. This can be achieved by a strict regulation of the market and strengthening the prestige of the regulatory institution through the extension and the precisising of its authorities.

The practice established on the Bulgarian capital market is a reflection of the acting laws and regulations being characterised with a number of imperfections and incompletenesses, as well as the accepted model of mass privatisation at the initial stage of the emerging and the functioning of the regulated capital market in Bulgaria, with the scepticism and the special sensitivity to any, even though insignificant change in the economic conjuncture on the side of the mass investor, caused by the financial collapse suffered in 1995 - 1996. This practice has shown that there is a pressing need for the adoption of an entirely new law, which is to create the conditions for more stringent and efficient regulation of the market in the interest of its development and the protection of the investors' interests. Below are given some examples in support of that need. The dynamics of the Bulgarian stock market in the year past since its existence has been to a large extent influenced by the block trade of shares. That fact has been conditioned by the respective statutory restrictions regarding trade, which have compelled the privatisation funds to conclude preliminary contracts between themselves which subsequently via block trade were legalised on the stock exchange. Even though within the law, those transactions considerably differ from the real stock exchange transactions with respect to the most important element included - the price. In this way the stock exchange mechanism's operation was ignored in the formation of the market price of the shares and the natural tendencies in the dynamics of the market were deformed.

The cross transactions have also exerted a substantial influence over the dynamics of the stock exchange trade during the year. In so far as the Bulgarian capital market is newly emerging, with still insufficient liquidity and in the process of creation of stock exchange practice, such transaction may substantially manipulate the market, harm the investors' interests, especially in cases of insider trading. This influences strongly the still fragile equilibrium and the confidence in the market.

It should be taken into consideration that the above mentioned transactions have been stipulated in the Stock Exchange's Rules of Operation. The initiative, however, for any amendments that may become necessary according the specific conditions, belongs to the stock exchange. Pursuant to the presently acting law only a notification regime is in force in respect to the Commission about any amendments and changes made in those Rules, so that its regulatory authorities have been restricted.

The treatment in the laws and regulations of the general concept of "public offering of securities" to a considerable extent limits the possibilities for more precise regulation of the trade with securities itself. Considering also the non-binding definition of the "underwriting" of issues which describes the process only as "offering securities for primary selling" on the side of the investment intermediary, it becomes clear that there is no sufficiently categorical economic commitment of the intermediary and motivation system for active stock exchange trading of the respective issue of securities. Accentuating on the enhanced economic motivation of the investment intermediary, the stock exchange trade will in practice accelerate the privatisation process itself with the possibility at that of realising the best market price with full transparency of the transactions.

Something specific of the Bulgarian privatisation model, combining the cash and mass privatisation, is also that starting its practical realisation in the conditions of a complete economic ruin and financial collapse, which have given rise to the exceptional mistrust and restraint on the side of the potential investors, it is already realised in the conditions of strengthened lasting political and financial stability with a potential for economic growth which will in practice stimulate relevant investment activity of the mass investor inclusive. That means that the connection between the capital market and the privatisation will be continuously extended and strengthened. The more so as the strongly diversified shareholder ownership with the predominant part of the privatised via investment vouchers companies will start at a certain point the natural for the capital process of concentration. New investment opportunities are opened in the forthcoming second wave of mass privatisation as well.

The substantial changes that have occurred in the economic environment as well as in the legislature, the prospects in the development of the Bulgarian economy, the rather rich experience already gained and the necessity of harmonisation of our legislature to that of the EC require the adoption of a wholly new law on securities. The prepared draft is based on the philosophy that the strict regulation of the market and the adequate authorities of the regulatory body are the most reliable guarantee for the development of an efficient market and for protection of the investors' interests. That is particularly important for newly emerging market as the Bulgarian is, because besides the solving of all other problems - economic, technological, institutional, etc. a special attention should be given on the formation and the development of the needed investment culture of the mass investor. His confidence in the capital market and its institutions should be gained, kept and enhanced on such grounds.

In that aspect and in the context of the relation capital market - privatisation, of special importance are the new provisions in the law which concern the regulation of the public companies and the increased requirements towards them. The rights of the shareholders of those companies are clearly defined and protected, including also in the increase of the capital or in transformation.

The investment intermediaries are a major and at the same time most risky entity of the capital market. In relation to that the new law sets up a considerably more detailed and efficient system of regulation and control of their activities. It includes an explicit and comprehensive defining of the kinds of transactions and activities which the investment intermediary may execute on the grounds of a licence granted by the Commission with considerably increased requirements to the persons who manage the intermediary and to the activities themselves of the company as an investment intermediary. The powers of the Commission have been enlarged with respect to the possibilities for control, refusal to issue or withdrawal of a licence for performance of the activity of investment intermediary, the aim being not to allow unnecessary additional risks for the market.

The new Securities Act will provide further possibility for control over the stock exchange trade. As far as the Stock Exchange's Rules define and regulate the whole system of the stock exchange and its functioning, any amendment to it will be possible only after the explicit preliminary approval of the Commission. The regulatory body will have an additional mechanism for continuous control over the system. The law also introduces an additional regime of licensing on the side of the Commission with regard to the execution of time transactions with securities.

An important condition for the capital market's development, and in this case for the successful development of the privatisation is the availability of a good system for protection of the interests of the portfolio investors, as has been provided for in the new Act. It is based on several principles:

- the availability of licensing and approval procedures for respective actions and activities;
 - permanent supervision over the activities of the market participants on the side of the regulatory body;
 - ensuring access to the necessary for the investor information through disclosure in the way provided for by law;
 - tender offering for the purchase of shares by majority owner;
 - possibility a minority holder to approach the court in the stipulated by law cases;
 - introduction of the institutions of the management company and the questor;
 - enhancing the administrative and penalty responsibility and increasing the property sanctions in violation of the law and the acts of its implementation.
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- These new Act and regulations of the capital market will meet the requirements of the serious portfolio investors which are a very important factor for the successful process of the privatisation.