Board Meeting of April 28, 1998
Statement by Juan L. Cariaga

Bulgaria – Country Assistance Strategy

This Country Assistance Strategy (CAS) for Bulgaria is welcome as the government’s program now seeks to complete the transition to a full market economy through macroeconomic stabilization within the targets specified in the IMF Standby Arrangement. We appreciate staff efforts in bringing us a detailed and candid update of the social and economic situation in that country.

In the previous CAS several factors were described that have been important for the slow development of the private sector. These include inadequate enforcement of the legal framework, slow privatization, financial indiscipline in the state enterprise sector and a weak banking system. During consideration of the CAS Progress Report on May 8, 1997, we were particularly concerned with the little progress reportedly made by the country in those areas. This CAS candidly notes that at the beginning of the previous CAS period, Bulgaria’s transition process had been so uncertain that it had been left far behind by most other countries in East and Central Europe.

The CAS also tells us that some 75 percent of the industrial plant and about 74 percent of banking system assets remains in the hands of the state. State-owned industry accounts for roughly 64 percent of total industrial output, with the private sector now more dominant in the services sector. We strongly welcome the attention the new government is giving to restarting and accelerating pending structural reforms in these areas.

Several powerful “economic groups” were cited in the CAS as having been a major constraint to reforms. We would appreciate staff providing information on how the government has managed relations with these groups and what steps it might take to ensure these constraints do not affect the reform process.

In the agricultural sector, the government intends to implement trade policy reforms and complete the process of land restitution, in order to help it adjust to the market environment and restore export-oriented growth. About 35 percent of the remaining land has not yet been returned and titles to restored lands are still largely provisional. More recently, the government has made additional progress in liberalizing, but it continues some uneconomic practices, including monitoring profit margins. We expect that needed actions
will be taken in order to establish a functioning market economy in agriculture.

The CAS emphasizes that the country needs to continue its legal reforms, to improve investments in social projects and to protect the environment. Yet, in all of these areas, there are reasons for concern given. We note that there is not even a legal framework for the functioning of the civil service, the economy is still very fragile and country is highly indebted with large external payments due in the near future.

Moreover, Bulgaria remains one of the poorest countries in Central and Eastern Europe, with one of three Bulgarians living in poverty. Over 85 percent of households receive some form of income transfer.

We recognize that the Bank’s involvement in Bulgaria has been difficult. However, we must also express our reservations concerning the development effectiveness of the lending program when 50 percent of projects by number and 43 percent by amount are “at risk.” While portfolio performance has improved, it seems to us that this can only be considered relative when 3 of 8 loans are unsatisfactory.

While the CAS noted some concern that the new government must follow through on its plans to bring about basic and significant change, we are pleased to note it has made the reform of the judiciary, the civil service and the state administration a priority. It espouses local self-government and plans to enact new laws on the responsibilities of the central, regional and local governments. All of this is positive. Moreover, it would appear that the previous several years have contributed to a popular desire to break with the past and take the measures needed to “develop a market economy and to prepare the country for accession to the European Union.”

However, as the CAS notes, the proposed strategy carries some serious risks. We hope Bulgaria can implement this strategy, maintaining the firm commitments that are contained in the CAS.

We agree with the CAS finding that perhaps the greatest potential risk to the programs is a failure to sustain reforms. The fact that the development objectives are essentially unchanged from the previous CAS only emphasizes the difficulties and risks.

The approach proposed to advance these objectives requires broad engagement in key areas of the government’s program, especially at the present time. The focus of assistance on promoting structural reform and private sector development remains, in our view, the correct one. Strengthening and rationalizing the role of the state and especially public administration and the judiciary is also important. We also support the measures planned for fighting poverty, developing human capital and protecting the environment.

Overall, we find that the proposed lending strategy of phased assistance linked to reform efforts is entirely appropriate and reflects the risks that exist.

Finally, while we have recognized those risks, this is a moment when the opportunities require the Bank to provide the government and
people of Bulgaria with the support they need and to wish them well in this challenging endeavor. We agree that “...the development rewards from a successful reform process in Bulgaria” are more than worth the risks involved for the Bank and wish the Bulgarian authorities and people success in their pursuit.