

# **BULGARIAN NATIONAL BANK**

**ANNUAL REPORT • 1991**



## Abbreviations

BNB	-	Bulgarian National Bank
BFTB	-	Bulgarian Foreign Trade Bank
SSB	-	State Savings Bank
CB	-	Commercial Bank
EIB	-	European Investment Bank
IBEC	-	International Bank for Economic Co-operation
IIB	-	International Investment Bank
CMEA	-	Council for Mutual Economic Assistance
OECD	-	Organization for Economic Co-operation and Development
EEC	-	European Economic Community
EC	-	European Community
USSR	-	Union of Soviet Socialist Republics
IMF	-	International Monetary Fund
GDP	-	Gross Domestic Product
SDR	-	Special Drawing Rights
Lv	-	Levs
MF	-	Ministry of Finance
R&D Fund	-	Fund for Reconstruction and Development
COM	-	Council of Ministers
NIS	-	National Institute of Statistics
NA	-	National Assembly
GNA	-	Great National Assembly
UDF	-	Union of Democratic Forces

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**Honourable Mr. Chairman  
of the National Assembly!  
Honourable Members of Parliament!**

*In accordance with the provisions of the Law on the BNB, Art. 1, Para. 2, the BNB reports its activities before the National Assembly and pursuant to Art. 54 of this Law, I submit to your attention the Annual Report of the Bulgarian National Bank for 1991.*

*1991 saw the **beginning of the reform of the Central Bank** and the overall banking system as an important prerequisite for the success of the economic reform and the passage to a market economy. The enforcement of the Law on the BNB (June 1991) granted the Bank the status of a state institution independent from the Government. The adoption of the other important banking law, the Law on Banks and Credit Activity, was delayed due to a number of reasons and it was not until March 1992 that it came into force. Thus the statutory regulations for the monetary and credit system were laid down but a number of laws (on the foreign exchange regulation, stock exchanges, securities, etc.) are still missing as well as banks standards and many rules and regulations which are now in the making.*

*Throughout the year, the BNB was working in collaboration and without particular differences with the Government, initially that was the Government of Mr. Dimiter Popov and, later on, the UDF Government with Mr. Philip Dimitrov at the head.*

*The two most salient features of the BNB policies in 1991 were **liberalization and restriction**.*

*The **monetary** policy of the BNB had a pronounced anti-inflationary thrust. It was generally successful since it prevented the real danger of throwing the country into a steep anti-inflationary spiral. The success, however, was only partial because (even if we ignore the leap of prices in February-March 1991) the inflation rates remained quite high, i.e. 73 per cent from March 1991 to March 1992. Given those inflation rates, interest rates which many people considered too high proved actually negative. It was the interest rates together with the credit ceilings that operated during most of the year as almost the only instruments which the BNB used to curb the inflation rates and keep them under control. Gradually, we enriched the set of instruments by introducing short-term deposit tenders, lombard loans, discount operations.*

*The Bulgarian National Bank continues to pursue the anti-inflationary policy but it should be noted that such a policy can not restrain inflation and reduce interest rates without the active support of the state budget, the income*

policies, the co-operation of the trade unions, the recovery of production and the privatization process.

Substantial results were achieved in the **foreign exchange sphere**. The foreign exchange regulations were liberalized. A uniform (floating) market-based exchange rate was introduced and an interbank foreign currency market was established and gradually developed its daily turnover up to approximately 15 million USD. The exchange rate of the Levs with respect to the US Dollar was stabilized within rather short time at about 18 Levs initially and then, during the first quarter of 1992, to 23 Levs for one US Dollar.

In the course of the liberalization, more than 800 foreign exchange offices were granted licences, the upper limit for the sale of foreign currency to individuals reached 10 thousand Levs, etc. Actually, what is known as domestic convertibility of the national currency was achieved, without declaring it officially.

The supervision of foreign currency operations with foreign countries, however, was insufficient and therefore, secret export of capital from the country took place in some cases. Many state-owned and private companies keep foreign currency deposits abroad in contravention with the regulations. The foreign currency market is still characterized by some oligopolistic aspects which will be overcome as competition grows stronger.

The national foreign currency reserves which were actually depleted at the end of 1990 increased gradually, reaching 330 million USD in December 1991 and 645 million USD at the end of April 1992. The major source for their replenishment were the loans from international organizations but the achieved equilibrium in the trade balance in convertible currency also contributed to that effect. The gold reserves of the BNB reached 1,017,041 troy ounces as of 31 December 1991.

**The issuing policy** of the BNB was oriented towards promoting the confidence in the Bulgarian national currency, overcoming the fear of a change of the currency used and undertaking the gradual replacement of the banknotes from the socialist period by a new series of banknotes with a higher face value. The money supply outside banks increased by 4 billion Levs and reached 11.8 billion Levs at the end of 1991 which, with a view of the higher prices, could be considered normal. The Bank, together with the Ministry of Finance, tried to reduce the payments in cash which created conditions for income concealment and tax evasion but it was not particularly successful. In the summer of 1991, we felt an acute shortage of banknotes but we mobilized the reserves of the system to ensure the regular payment out of wages and pensions. Such difficulties are no longer existent.

The preparation of the new series of banknotes with improved protection and radically changed layout and symbols is going on at a regular pace but there are some delays in minting a new issue of coins because of the lack of an approved new graphic and plastic layout of the state coat of arms.

In the field of **the bank supervision** difficulties are more than successes. The lack of new legislation in this sphere was felt throughout the year. The staff was and still is unprepared for the new functions; besides, many people went to the private sector and commercial banks. The supervision and the collection of banking information needed by the BNB are confronted with resistance.

*In spite of the difficulties, the bank supervision has been set into operation. After the somewhat hasty granting of licences for the establishment of new banks during the first half of the year, the supervision has become more stringent and exacting. Still rather liberal is the approach to granting licences for the opening of foreign exchange offices which contributed to the shrinkage of the role of the black market in the purchase and sale of foreign currency in cash.*

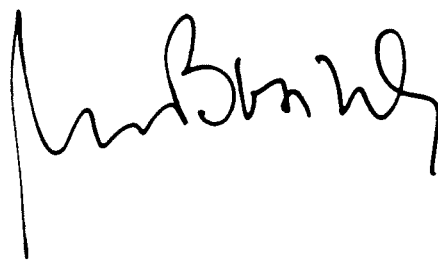
*Notwithstanding the shortcomings of the supervision, the gross violations of banking principles and standards by two commercial banks (in Yambol and Bobovdol) were detected in time to prevent the danger of chain bankruptcies or loss of deposits by savers. Besides, as early as February 1991, we rescinded the previous permission to sell state bank shares at par. When attempts were made to renew such operations, the BNB took a firm stand and prevented in due course the hidden privatization of the banking sector.*

*The Bulgarian National Bank also contributed to the preparations for the consolidation and strengthening of the banking system. Together with the Bulgarian Foreign Trade Bank, it established **the Bank Consolidation Company PLC.***

*On the **international scene** the BNB was among the most active participants in the preparation of the two letters of intent of the Government to the International Monetary Fund, in the talks with the World Bank, the European Community and other international organizations.*

*In the course of the year, the Bulgarian National Bank also performed other, quite often very important tasks which remained unnoticed by external observers but they will soon lead to qualitative improvements in the monetary and credit system. In the advanced stage of development are the preparations for the establishment of a sophisticated, reliable and quick payment mechanism, for the introduction of a new chart of accounts, the computerization of banks and others.*

*We have to do a lot of work for restructuring and updating the financial sector, introducing sophisticated bank technologies and training of personnel in order to become adequate to the world standards and requirements.*



**Prof. Dr. Todor Vulchev**  
**Governor of the Bulgarian**  
**National Bank**

# **BULGARIAN NATIONAL BANK MANAGEMENT**

## **MEMBERS OF THE PLENARY COUNCIL**

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Gancho Kolev  
Prof. Georgi Petrov, D.Sc.  
Deyan Popov  
Dimitar Kostov  
Emil Hursev, Ph.D.  
Kamen Toshkov  
Stoyan Shukerov

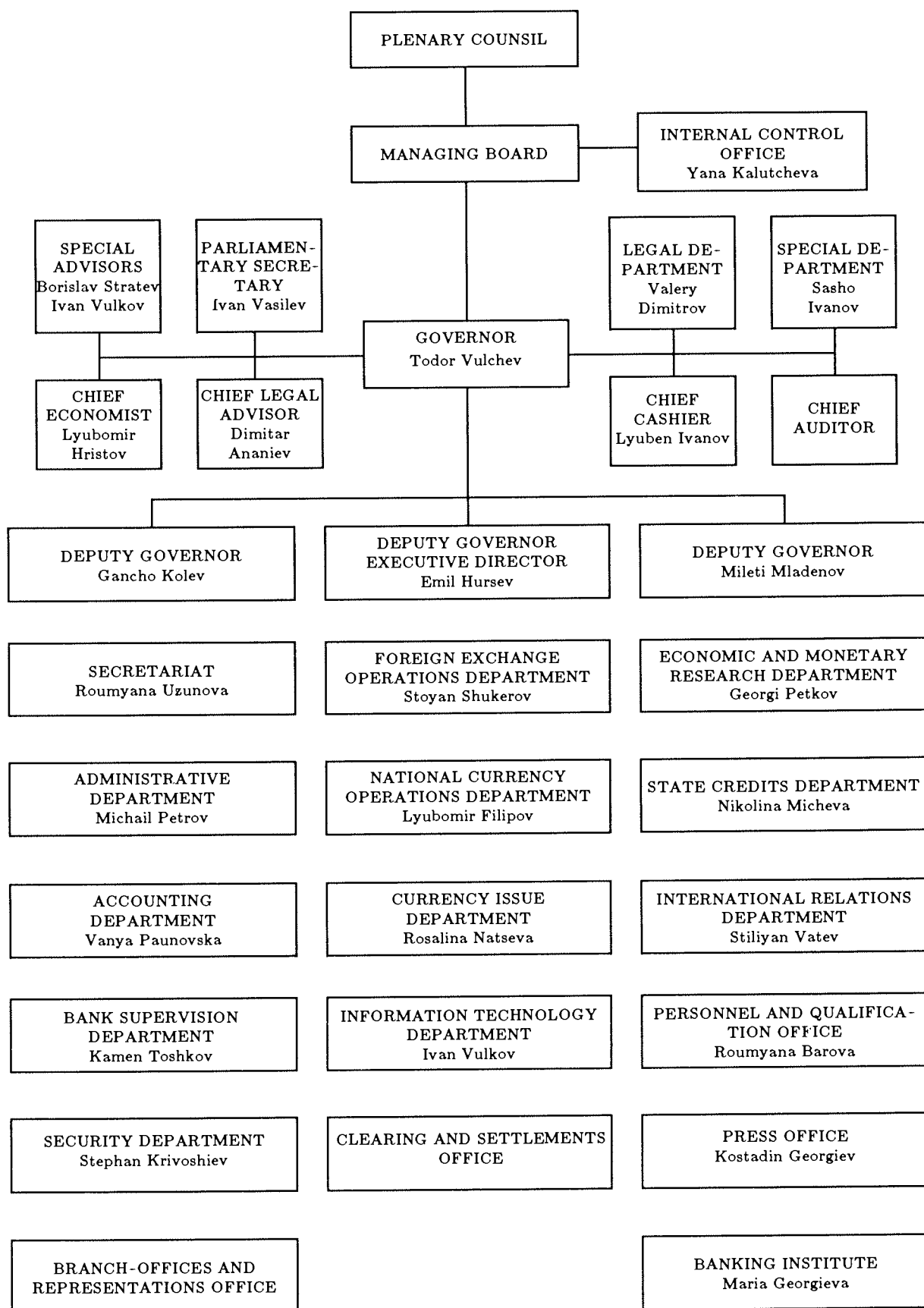
Konstantin Dimitrov  
Lyubomir Filipov  
Lyubomir Hristov, Ph.D.  
Ass.Prof. Mileti Mladenov, Ph.D.  
Oleg Nedyalkov  
Rosalina Natseva, Ph.D.  
Prof. Todor Vulchev, D.Sc.

## **MEMBERS OF THE MANAGING BOARD**

Prof. Todor Vulchev, D.Sc.  
Emil Hursev, Ph.D.  
Ass.Prof. Mileti Mladenov, Ph.D.  
Gancho Kolev

Rosalina Natseva, Ph.D.  
Lyubomir Filipov  
Stoyan Shukerov  
Kamen Toshkov  
Lyubomir Hristov, Ph.D.

# Organizational Structure of the BNB



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# **I. Economic Development**

# 1. Major Political and Economic Events in 1991

- 3 January** The Grand National Assembly (GNA) voted the Accounting Act which laid the foundations of an up-to-date accounting system adequate to the transition from a centrally planned to a market economy.
- 9 January** The Grand National Assembly adopted a resolution on the appointment of the Governor and Deputy Governors of the Bulgarian National Bank.
- 18 January** The Council of Ministers (COM) adopted Ordinance No. 5 on the interest rates on deposits, savings and loans of individuals and companies. The basic interest rate was fixed at 15 per cent per annum. The activities and functions in the formulation and approval of interest rate policies were fully transferred from the Council of Ministers to the Bulgarian National Bank.
- 29 January** COM adopted Ordinance No. 8 on price liberalization and social protection of the population. The radical economic reform designed to effect the passage to a market economy was launched on 1 February.
- 8 February** GNA passed the 1991 State Budget Act which regulated the financial parameters of the reform under way. The budget deficit was envisaged to be covered through loans from the BNB and securities issue. Later on (July), GNA adopted the Budget Revision Act in conformity with the economic changes introduced.
- 8 February** COM adopted Ordinance No. 15 on the new foreign exchange regulations. It liberalized the terms of purchase and sale of foreign currency. The BNB was entrusted with the control over the foreign exchange market by means of daily fixing the reference rate of the national currency to the major foreign currencies on the basis of the market exchange rates for the operations of commercial banks.
- 22 February** GNA passed the Farmland Ownership and Use Act. Conditions were created for the reform in agriculture on the basis of the reinstatement of former owners. (Some unspecified and controversial matters, however, prevented the actual enforcement of this Act and became the subject of debates by the next National Assembly in 1992).
- 15 March** Bulgaria signed the first Stand-by Agreement with the IMF. For the first time after the freeze on the repayment of the external debt declared in March 1990, the country received an official loan and started using IMF resources for establishing foreign currency reserves and compensating for the higher oil prices which resulted from the Persian Gulf crisis.
- 18 March** GNA passed the Statistics Act which laid the foundations of an up-to-date system of collecting, processing, analysing, storing and disseminating adequate

statistical information on the economic developments in the country.

- 2 May** GNA passed the Competition Protection Act. It provided for the protection of consumers' interests against misuse of monopoly on the market and other forms of unfair competition.
- 16 May** GNA adopted the Trade Act which came into force on 1 June and regulated the forms, functions, rights and duties of businesses, establishing the main legal frame for engaging in economic activities under market conditions.
- 17 May** GNA passed the Foreign Investments Act. In spite of its liberal character, that Act failed to attract significant foreign investments to Bulgaria and therefore, in 1992 the next National Assembly voted another Business of Foreign Persons and Foreign Investment Protection Act.
- 4 June** COM adopted Ordinance No. 106 on some changes of fixed prices. The second stage of the price liberalization was undertaken; only the prices of electricity, heating and coal remained fixed; current price ceilings were established for the prices of liquid fuels and prescribed prices of 14 goods and services were introduced to be monitored and controlled by the Government.
- 6 June** GNA passed the Law on the BNB which outlined the basis for the establishment of a modern two-tier banking system and regulated the role, functions, rights and obligations of the Central Bank.
- 5 July** COM adopted Ordinance No. 129 on the transition to negotiated wages. The first steps were made towards the establishment of a labour market, particularly the free wage bargaining depending on the current economic environment: supply and demand of manpower, inflation rates, overall business activities, etc.
- 12 July** GNA voted the Constitution of the Republic of Bulgaria. The fundamental law of Bulgaria embodied the democratic changes in the country in the wake of 10 November 1989.
- 25 July** COM adopted Ordinance No. 147 on the establishment of a State Fund for Reconstruction and Development aimed at collecting the resources from loans, subsidies, grants and other sources offered by international financial institutions and designated for the restructuring of the national economy.
- 27 July** The Republic of Bulgaria signed a Loan Agreement with the International Bank for Reconstruction and Development. The trust of world financial circles started growing; a second line of credit was opened to provide foreign currency financing for the restructuring of the national economy.
- 13 October** Elections for National Assembly (NA) and local government bodies. The 36th National Assembly was democratically elected and its composition reflected the new balance of political forces in Bulgaria. The largest parliamentary group became that of the Union of Democratic Forces.
- 5 November** NA passed a resolution on the resignation of the previous Council of Ministers. That was the end of the ruling of the coalition Government which, having received the confidence of the political forces, began the economic reform and made the initial steps along the way from a centrally planned economy to a market economy.
- 8 November** NA passed a resolution on the appointment of Prime Minister and the members of the Council of Ministers. The new Government was formed by the Union of Democratic Forces and took over the responsibilities of the executive

branch for the continuation of the economic reform.

13 November

NA passed a resolution on holding elections for President and Vice-President of Bulgaria. Bulgarian voters got the opportunity to exercise their right to vote in direct presidential elections on 12 January 1992. (The candidates of the Union of Democratic Forces won the elections.)

## 2. Gross Domestic Product

In 1991, the nominal Gross Domestic Product (GDP) was equal to 138.4 billion Levs<sup>1</sup>. In terms of comparable prices, in 1991 the GDP was 16.7 per cent less than in 1990 and 24.3 per cent less than in 1989. Statistical data on the real GDP indicated that the tendency towards shrinkage of production which had started in 1989 was still going on. 1991 saw somewhat higher decline rates which reflected the deep economic depression, concomitant of the transition from a centrally planned economy to a market one.

### Economic Reform

The radical economic reform, which started in the beginning of February 1991, drastically changed the development and structure of the aggregate domestic demand. The considerable reduction of the real income of the population and the restrictive fiscal policies of the Government led to substantial shrinkage of consumption. Whereas in 1990 it was preserved, in real terms, almost at the level of 1989, in 1991 it was reduced by almost 20 per cent.

Even greater was the shrinkage in the field of savings. The insecure economic environment as well as the increased interest rates heavily affected the demand for investments. In 1991, the savings in fixed assets were equal to 13,870 million Levs at current prices but in real terms the reduction was almost by a half as compared to the previous year. Considering the further decline in 1990 (19 per cent), the total reduction was about 60 per cent over the last two years.

The major reason for that development was the reduction of the budget spending for investment purposes. The unfavourable tendency from the previous years for distribution of investments in favour of the passive component parts of capital grew stronger in 1991. The share of expenditures for machinery and equipment accounted for about 32 per cent of the total amount of investments in 1991.

The behaviour of inventories was typical of an economic stagnation. The inventories of raw and direct materials remained at a low level, while the inventories of finished output marked a steady high level. In 1991 the total inventories growth was lower by more than 55 per cent in comparison to 1990 and some 75 per cent in comparison to 1989.

Against the background of the depressed domestic demand, foreign trade played a positive role in preventing an even more drastic reduction of the GDP. One of the measures of the economic reform was to substantially depreciate the value of the national currency to the major foreign currencies which, on the one hand, created conditions for a greater competitiveness of Bulgarian goods at international markets. But, on the other hand, the disintegration of the trade links with the former CMEA member countries, and the former Soviet Union in particular, as well as the traditional orientation of the national production limited the opportunities for efficient trade exchange. In the context of a generally worsened foreign economic environment, imports were reduced at higher rates than exports and thus in 1991 a positive foreign trade balance exceeding 5 billion Levs was recorded. Compared to 1990 when the balance was only 244 million Levs, the achieved level of the net exports in 1991 seemed encouraging but the absolute amount of exports and imports remained too low.

The different pace at which the component parts of the aggregate demand

<sup>1</sup> Estimates of the National Institute of Statistics

changed led to substantial alterations in its structure. The relative share of consumption in the GDP used in the country increased from 70.9 per cent in 1990 to 85.5 per cent in 1991, while the share of investments decreased from 29.1 per cent to 14.5 per cent respectively. Substantial structural changes occurred also in the way in which the generated GDP was used. Almost 5 per cent of the GDP left the country through the net exports, while the respective figure for 1990 was only 0.5 per cent. That phenomenon was an attempt at adapting the national economy to the conditions of a sizeable foreign indebtedness. At the same time, the reduction of savings was much faster than the reduction of consumption as a result of which the share of domestic consumption increased from 74 per cent to 75.7 per cent, while the share of savings decreased from 30.4 per cent to 12.8 per cent.

### Production Factors

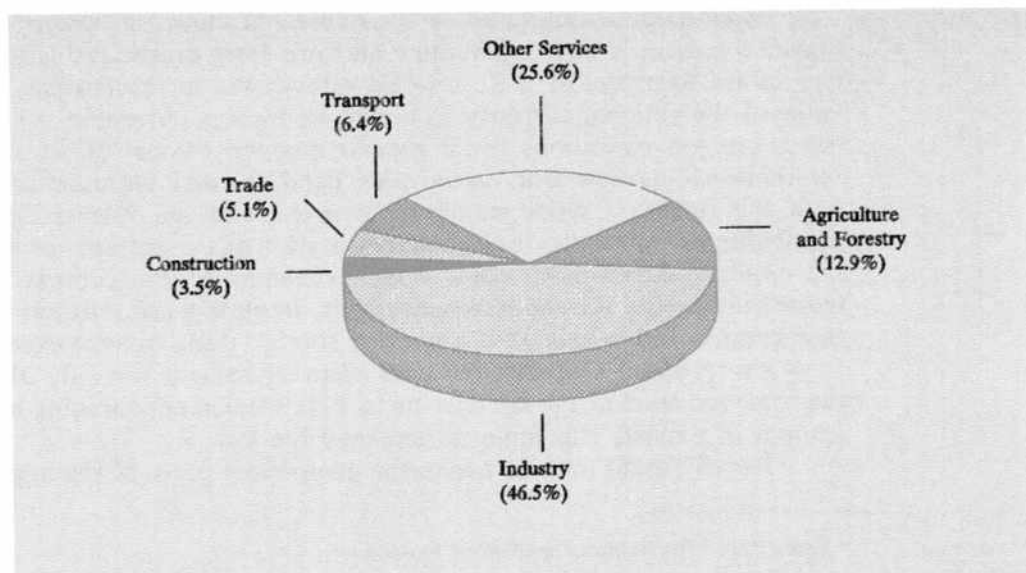
The profound economic changes were reflected also in the contribution of production factors to the generation of the GDP. While in 1990 the relative share of wages and social security contributions increased from 51.3 per cent in 1989 to 53.7 per cent which resulted only from the reduction of the profit and indirect taxes and the consumption of fixed assets kept within the limits of 14 per cent, in 1991 the relative share of wages and social security contributions was drastically reduced to 43.4 per cent, the profit and indirect taxes exceeded 50 per cent and the consumption of fixed assets went below 5 per cent. The established structure clearly reflected the drastic shrinkage of the primary earned income as well as the limited opportunities for future economic growth as a result of the great reduction of the resources for maintenance and reproduction of fixed assets.

### Sectoral Structure of the GDP

The big changes in the aggregate demand naturally led to substantial changes in the sectoral structure of the GDP. Industry and construction were the largest contributors to the reduction of the GDP and they continued to decrease at the highest rates in 1991 as well. Whereas in 1990 their decline was 12.5 per cent as compared to 1989, in 1991 it reached 21.4 per cent and thus exceeded 31 per cent over the last two years. As a result, their relative share in the GDP sank from 59.4 per cent in 1989 to 50 per cent in 1991. The decline of industry over the same period was from 51.7 per cent to 46.5 per cent and that of construction was from 7.7 per cent to 3.5 per cent.

Several basic industrial subsectors accounted for some 85 per cent of the reduced industrial output. The drastic decrease of the domestic demand which resulted from the almost non-existent investment activities as well as of the external demand due to the collapse of the traditional trade relations mainly with

COMPOSITION OF THE GDP - PRODUCED IN 1991



the former Soviet Union led to great shrinkage in some industries which had previously been attached priority, i.e. electrical engineering and electronics, machine building and metal processing, chemical engineering and oil industries. As subsidies were eliminated, losing industries marked a big decline, e.g. ferrous metallurgy and the building materials industry. The substantial decrease of the output of textiles, knitwear and foods was mainly due to the shortage of raw and direct materials.

The sectoral structure of industry changed: the relative share of machine building and electronics decreased, whereas the share of some light industries increased (glass, chinaware, textiles, knitwear, ready-made clothes, leather and furs, footwear, polygraphy and foods).

The tendency of decreasing agricultural output which took shape in 1988 continued throughout 1991 as well. Unlike 1990 when the reduction of the GDP generated in agriculture was only 3.7 per cent compared to the preceding year, 1991 saw a much greater reduction of 12.5 per cent. It occurred both in crop raising and livestock breeding where the diminishing number of livestock and poultry in the co-operative sector became a lasting tendency. In spite of the reduced output in real terms, the relative share of agriculture and forestry increased from 10.9 per cent in 1989 to 12.9 per cent in 1991.

In 1991, the tendency of increasing the contribution of services to the generation of the GDP speeded up; it grew from 29.7 per cent in 1989 to 31 per cent in 1990 and 37.1 per cent in 1991. Changes took place in that sector, too. Transportation services decreased as a result of the great reduction of the industrial and agricultural output and commercial activities suffered from the depressed solvent demand, while the amount of the other services<sup>2</sup> recorded a sustained growth in both nominal and real terms. In 1991, they accounted for 25.6 per cent of the GDP after the tentative rent of owner-occupied houses had been calculated at market prices.

### 3. Employment

The reduced economic activity had an adverse effect on employment in 1991. The statistical data for the last months of 1990 and the beginning of 1991 showed that the employment crisis had started even before the reform and the restrictive measures which were introduced in February to reduce demand and, consequently, production, only speeded up and aggravated the crisis.

The employment decline which had emerged in 1987-1988 continued also in 1991. Over the last two years, the number of employees in the public sector was reduced from 4,082 thousand to 3,189 thousand or by 22 per cent. In 1991 alone the reduction was the greatest, reaching 17.1 per cent. As far as the number of employees in the private sector is concerned, a substantial increase was reported and the figure reached was approximately 3,466 people in 1991.

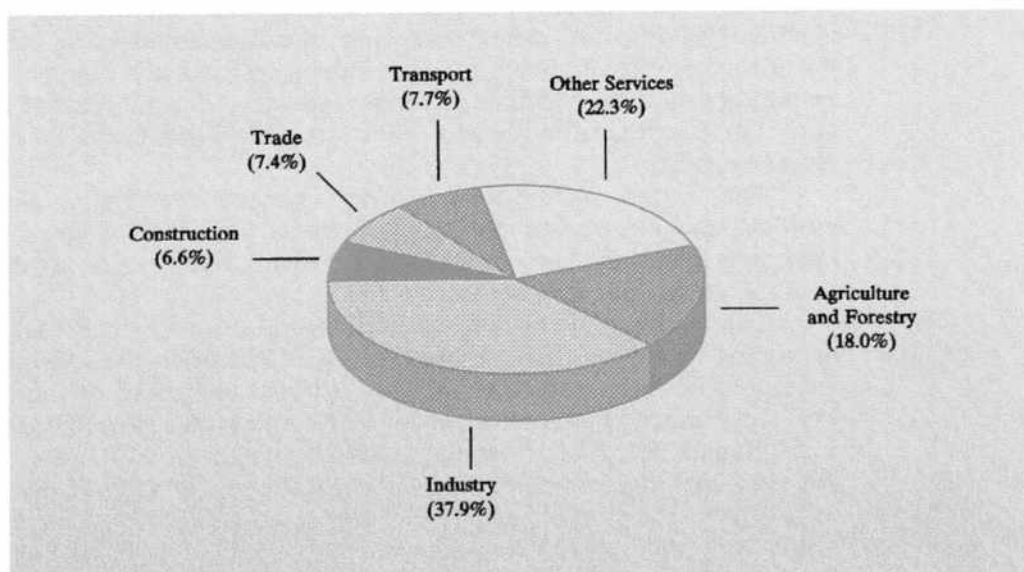
#### Industry

Over the last two years, the number of employees in industry was reduced by some 460 thousand people out of whom 270 thousand were the figure for 1991 which accounted for almost 43 per cent of the reduction of the employees in the national economy during the same year. The considerable growth of those laid off in industry was not consistent with the serious production decline. While in 1990 their rates were quite similar, in 1991 the reduction of those employed was 18.6 per cent and thus, lagging behind the drop in production by 5.6 percentage points. A similar discrepancy was observed also in most of the other sectors and therefore, the ratio between the people employed in industry and the total number of

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<sup>2</sup> The category other services includes public utilities, science and research activities, education, culture and art, health services, social security, sports, recreation and tourism, finances, credit and insurance, management.

## STRUCTURE OF EMPLOYMENT BY BRANCHES IN 1991



employees in the national economy changed insignificantly over the last two years, i.e. from 38.3 per cent in 1989 to 37.9 per cent in 1991.

Almost 70 per cent of the total reduction of jobs in industry took place in four subsectors: machine building and metal processing (30.4 per cent), electrical engineering and electronics (18.4 per cent), food industries (10.6 per cent), textiles and knitwear (10.1 per cent). Least affected by unemployment were electrical and thermal power generation and coal mining where the reduction of the output was the smallest in comparison to the other industries as well as chemical engineering and oil industries where the technological peculiarities accounted for the greatest margin between the decline of output and the reduction of employment.

### Construction

Over the last two years, the number of employees in construction was reduced by 150 thousand persons or more than 40 per cent compared to 1989. The lay-offs were most intensive in 1991 when more than 100 thousand people lost their jobs. That led to the decreased relative share of this sector in the number of employees in the national economy from 8.3 per cent in 1989 to 6.6 per cent in 1991.

### Agriculture and Forestry

In agriculture and forestry the number of employees diminished by some 240 thousand people over the last two years out of whom 98 thousand lost their jobs in 1991. In the same year, the unemployment rates in those sectors were lower than the average rates for the country as a whole and thus the share of employees in agriculture rose from 17.6 per cent in 1990 to 18 per cent in 1991.

### Transport

The number of employees in transport was reduced by approximately 45 thousand people over the last two years. In 1991 alone, the reduction was by 30 thousand or almost 13 per cent. Nevertheless, the relative share of employees in transport in the total number of employees in the national economy showed a lasting tendency to grow from 6.6 per cent in 1989 to 7.2 per cent in 1990 and 7.7 per cent in 1991.

### Trade

A drastic reduction of employees was observed in trade activities in the public sector: over the period 1990-1991, the loss of jobs in that sector developed rather evenly and reached 158 thousand which represented 40 per cent of the employees in 1989. Hence, the ratio between the employees in trade and the total number of employees in the national economy shifted from 9 per cent in 1989 to 8.1 per cent in 1990 and 7.4 per cent in 1991.



## Other Services

The sector of other services lost more than 120 thousand employees over the last two years. The lay-off rates were 7 to 8 per cent per annum and were lower than in the other sectors of the national economy. Therefore, the relative share of employees in that sector was growing steadily from 19.1 per cent in 1989 to 20.1 per cent in 1990 and 22.3 per cent in 1991. 1990 saw the most drastic reduction of employees in public utilities by almost 40 per cent and then 1991 saw the greatest shrinkage of jobs in science and research activities by more than 22 thousand or 25 per cent as well as in culture and science by more than 8 thousand or almost 19 per cent. The reduction of managerial staff continued, though at somewhat lower rates: more than 10 thousand or 17 per cent were laid off in 1990 and another 5.5 thousand or 11 per cent in 1991. Comparatively lower (within the range of 2 to 5 per cent in 1991 alone) was the reduction of employees in health services and education with a total number of 15 thousand people losing their jobs in the two sectors over the last two years.

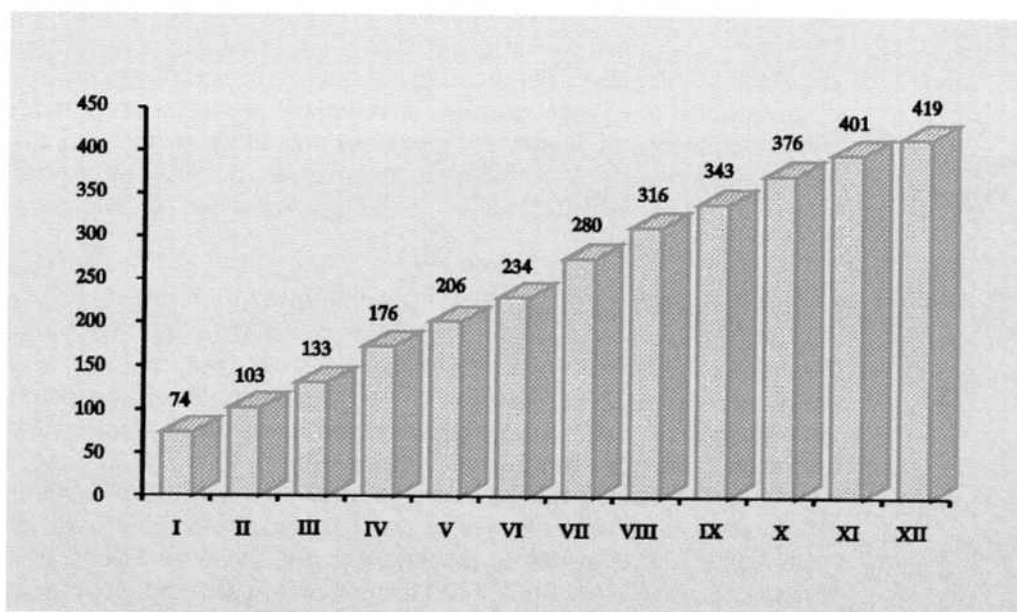
Under the influence of the accelerated development of banking, the number of employees in the financial, lending and insurance sphere remained almost unchanged. As a result of the different pace of reducing jobs in the different sectors, there was observed a steady growth of the share of employees in education, health services and finance, while in science, management and culture the number of employees decreased.

## Unemployment

The reduced demand for manpower expressed in the decreased number of employees and jobs, naturally led to excessive supply of manpower on the emerging labour market. The major indicator of this phenomenon for the time being is the number of unemployed registered at the local labour offices. At the end of 1991, the number of unemployed reached 419,123 people, the increase being 6.5 times as compared to the preceding year. The unemployment rate<sup>3</sup> rose from 1.7 to 12 per cent over the same period.

NUMBER OF UNEMPLOYED IN 1991

(thousand people)



The most substantial increase of the registered unemployed people was recorded during the second and the third quarter when their number increased by 100 and 110 thousand people respectively. The number of employees laid off was

<sup>3</sup> The unemployment rate is defined as the ratio between the number of unemployed and the total number of manpower (employed plus unemployed).

the least during the first quarter due to the slow and unwilling adaptation of most state-owned enterprises to the changing market conditions. The tangible reduction of the unemployment growth rate during the last quarter revealed the gradual exhaustion of the possibilities for reducing employment within the framework of the existing structures of manpower which developed with the start of the economic reform in 1991. As more substantial structural changes take place in the economy, the dynamic development of unemployment will probably grow faster.

The structure of the unemployed registered at labour offices at the end of 1991 was as follows: workers accounted for 44 per cent, university graduates - 28 per cent and unskilled workers - 28 per cent. In the course of the year, the share of unemployed university graduates was steadily decreasing from 41 per cent in January to 28 per cent in December. At the same time, the share of unemployed people without specific skills rose from 11 to 28 per cent. The figures cited above prove that when the labour market was taking shape in 1991 people of higher education and skills had a certain advantage. Another proof was the fact that in 1991 the share of the announced jobs for university graduates in the total number of vacant jobs increased from 2.4 per cent to 19.4 per cent.

Young people prevail among the unemployed registered at labour offices; young people below the age of 30 accounted for almost one half of the total number. The share of unemployed women was larger, ranging from 55 to 64 per cent.

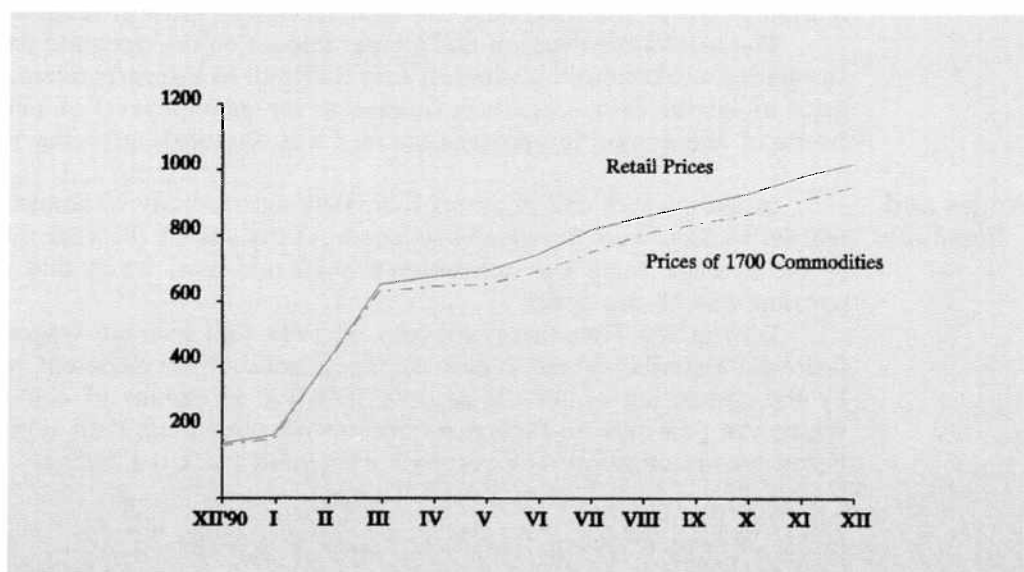
## 4. Prices, Wages, Pensions

1991 will be remembered for the exceptionally dynamic development of prices, wages and pensions. The price liberalization was an essential element of the radical economic reform which began in February. Its objective was to restore the informative function of prices and transform them into a major factor in the efficient allocation and use of resources. Besides, it was the only possible way to restore the macroeconomic equilibrium between the aggregate supply and demand. Under the conditions of a huge inflationary potential and an economy in a deep depression, the price liberalization naturally entailed, first of all, a leap in the level of prices and only then genuine inflationary processes were made manifest. The dynamic pattern of wages and pensions was more steady and somewhat delayed with respect to the price increase. As a result, the growth of wages and pensions lagged substantially behind the price increase and drastically reduced solvent consumer demand.

### Consumer Prices

The major indicator of the inflation rates in 1991 was the change of the prices of 1,700 consumer goods and services included in the "basket" of the National Institute of Statistics (NIS). In December 1991, the "basket" was 473.7 per cent more expensive in comparison to the same month of the preceding year. The greatest annual inflationary contribution came from three groups of goods and services: "Housing, Heating and Electricity", "Post Offices and Transportation" and "Foods". Taking into account the price increase in 1990 which was 65 per cent, the total increase of consumer prices was almost 9.5 times over the last two years.

Three waves could be discerned in the development of prices of consumer goods and services in 1991. The first one was registered in February-March when the price index changed in a leap-like manner (by 122.9 per cent and 50.5 per cent respectively due to the specific peculiarities of the period selected to report the changing prices). The main driving forces behind the drastic price increase above the average level were foods (their price increased by 191.5 per cent and 39 per cent respectively) and the goods belonging to the group of Housing, Heating and Electricity (by 113% and 152 per cent). The second wave took place in July-August with the liberalization of the purchase prices of some farm products and with the effects of the liberalized energy prices. Prices increased by 8.4 per cent and 7.5



per cent respectively over that period.

The third increase of inflation rates occurred during the last two months of 1991. It was partially due to some traditional seasonal factors typical of the end of the year. Yet, the main reason was the inflationary pressure which the higher income of the population generated because of the fixing of new wages and salaries in the public sector which began in August. The growing exchange rate of the US Dollar also exerted negative impact from September until the end of the year. Other essential inflationary factors were the pressure of trade intermediaries and the financing of the budget deficit which operated throughout the year.

### Retail Prices

The retail price index was not very different from the index of the consumer basket of the NIS both in 1990 and in 1991. Still, the retail price index increased at faster rates: almost 490 per cent in 1990 and a total of 916 per cent for the last two years. In 1991, the greatest price increase was recorded in services (565 per cent), followed by foods (480 per cent) and manufactured goods (438 per cent). After the first two inflationary waves, the balance of prices was relatively stabilized and reflected the new preferences in consumer demand.

### Prices of Monitored Goods

Interesting additional information was provided by the index of the retail prices of the 14 goods and services which were monitored and controlled by the Government. The elimination of the government subsidies for these staple commodities made their prices rise faster during the price leap in February. At the end of the first half of the year, their prices increased by 480 per cent as compared to 1990, while the figure for 1991 as a whole was 656 per cent. That phenomenon well justified the need for government monitoring and control by economic means only. However, at the same time it became increasingly clear that the impact of the monitored goods and services on the total consumer price index tended to grow lower because producers continuously raised the prices by modifying the structure of their output.

### Price Index for Manufacturers

It was for the first time in the beginning of 1992 that the NIS offered the price index for manufacturers of industrial output. But the form of its presentation (compared to the same month of 1990) prevented the accurate tracing out of inflation rates in the course of the year. Nevertheless, it may be stated that the general level of producer prices was lower than the level of consumer prices. The greatest price increase (6 to 10 times) was registered in "first-echelon" industries,

such as coal and oil mining, chemical engineering and oil industries whose output had so far been systematically underestimated. Conversely, the previous artificially high prices of machine building and electronics grew at relatively lower rates.

The price liberalization had a great impact on the dynamic pattern of wages and pensions. Although it was still very difficult to interpret average wages as the price of labour resources, their linkage to the general level of prices within the frame of the emerging market economy was obviously growing stronger.

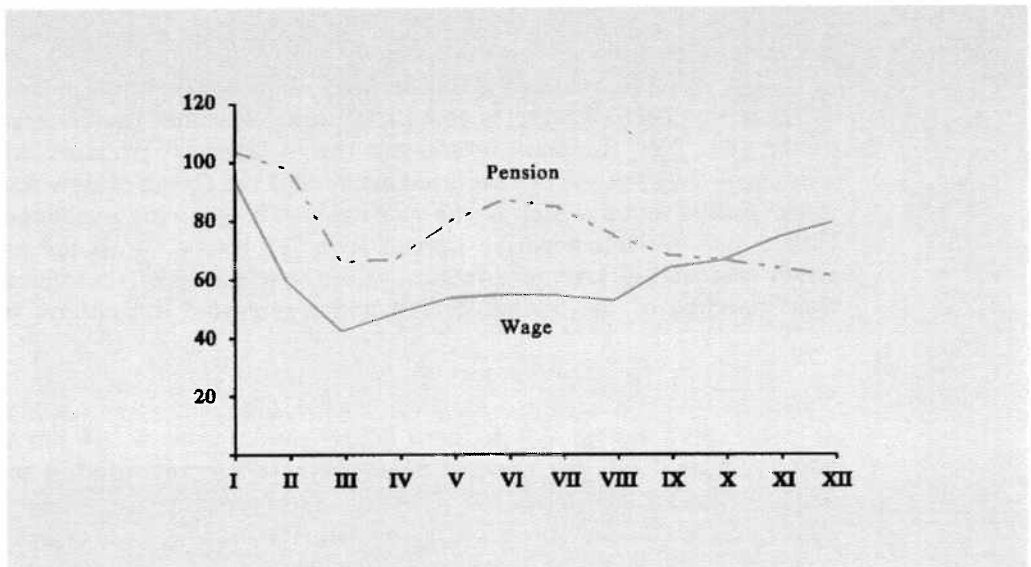
## Wages and Pensions

In 1991 wages and pensions increased substantially in nominal terms but in real terms they were drastically reduced. At the end of the year the real decrease of the average wage was approximately 20 per cent, while that of the average pension was 38 per cent.

During the first three quarters of 1991 real average wages and pensions followed a similar dynamic pattern. Their parallel development was determined by the protection of income against inflation by means of compensating both wages and pensions. In fact, real pensions decreased less than average real wages because compensations for pensions were paid from the budget.

INDEX OF REAL AVERAGE WAGE AND PENSION IN 1991  
(December 1990 prices = 100%)

(per cent)



The dynamic patterns of real average wages and pensions diverged after September 1991. That was related to the transition to free wage bargaining and the cancellation of compensations during the fourth quarter. Thus average nominal pensions were stabilized within the range of 500 to 512 Levs during the last four months of the year, while average nominal wages increased by almost 80 per cent over the same period.

The sectoral pattern of wages in the public sector was quite diverse. The average monthly wage in industry increased by 167 per cent in comparison to the preceding year which meant 7 percentage points above the average growth for the national economy. Among industrial branches, the greatest growth (almost 215 per cent) was scored in chemical engineering and oil industries, in spite of the considerable shrinkage of the output and the smaller reduction of employees. High growth rates, about 200 per cent, characterized power generation where the decline of production was less than 10 per cent, the polygraphic industry which was the single industrial branch which, regardless of its strong dependence on imported raw and direct materials, marked a growth of output of more than 20 per cent as well as food industries whose relative share in the industrial output

followed a tendency of steady increase for the last two years. The rates were lower than the average in industries which were badly affected by the changed market conditions, i.e. textiles, knitwear and dressmaking industries, notwithstanding the great reduction of employees as well as machine building and electronics where the reduction of output and employees reached its highest levels.

The last two years were insufficient to accumulate the requisite information base for asserting or rejecting certain hypotheses about the statistical linkage between the changes of output, employment and payment in various industries. Still, it can be argued that the employment reduction rates were lower than the output decline rates and the difference depended on the peculiarities of each industry and was subject to additional specification and measurement. Besides, industries less affected by the crisis were in a position to provide wages higher than the average level, especially when they successfully reduce the redundant employees.

There exist grounds to assert that the accelerated reduction of redundant employees made it possible for the average wage growth rates in **construction** to exceed the average national levels by 12.8 percentage points. A positive factor in this respect was the increased demand of the population for construction services in spite of the large spread of the private sector in construction.

Unlike the preceding year, 1991 saw a lower growth rate of wages in **agriculture and forestry** as compared to the average growth rate for the national economy; there the average wage was lower than the average for the country by about 100 Levs (11 per cent). The estimates of the output, employment and payment in agriculture and forestry are subject to further adjustment taking stock of the private sector whose role will increase significantly after the land is returned to its private owners.

The payment growth rates in **transport** were higher than the average for the country by 8 percentage points. However, that difference would have been bigger if the income of the private sector engaged in transportation services had been recorded but reliable statistics was not available yet.

Payment in **trade** was 6 percentage points above the average rates for the country but it still remained among the lowest in comparison to the other sectors. The lagging behind would have been set off provided the income of the private sector had been recorded because the development rates of the private sector were much higher than those in the public sector.

In the sector of **other services** the growth rates of the average wages slowed down in 1991 as compared to the preceding year. The greatest increase of payment was recorded in the financial, credit and insurance spheres where it was 3.4 times compared to 1990 and 4.7 times compared to 1989. Thus the financial, credit and insurance sector ranked first among the national economic sectors in terms of the average gross wage which was consistent with the situation in advanced market economies. The payment in education and health services increased faster than the average level (3.7 to 3.9 times) over the period 1990-1991. Below the average level for the country was the growth of payment in science, research, culture and art (3 to 3.3 times) which reflected the ability of the state budget to finance these activities.

## 5. Foreign Trade

In 1991 the foreign currency earnings from exports decreased by almost 50 per cent, while the import costs were up by 60 per cent as compared to 1990. That drastic shrinkage of Bulgaria's foreign trade reflected the external adaptation of the economy to the conditions of the ongoing stabilization programme.

The liberalization of foreign trade policies began in February with the cancellation of almost all quantitative restrictions on imports. Due to the low level of customs tariffs applied to the countries outside the scope of the former CMEA,

a provisional import charge of 15 per cent was introduced mainly for consumer goods with a view to protecting the local industries during their restructuring and adaptation to the new price structure. Export quotas were reduced from 57 to 33 goods, while with respect to 16 goods quotas were replaced by provisional export charges which were cancelled in July. Due to the acute shortages on the domestic market, quantitative export restrictions included primarily foods and raw materials. In conformity with the agreements with former CMEA member-countries the imports in transferrable roubles were not subject to the customs tariff, while the exemption from customs duties was done on the basis of reciprocity. Otherwise, the most favoured nation rate was applied. As of 1 January 1991, the trade with the former CMEA member-countries was based on international prices quoted in convertible currency and the trade with the USSR was carried out in US Dollars under a Clearing Agreement and on the basis of indicative lists of goods.

## Market Structure

The market structure of the foreign trade changed radically in this context. The transition to payments in convertible currency with the former CMEA member-countries provided forcible conditions for the re-orientation of exports and their substantial increase towards Western markets. The relative share of exports to the former USSR dropped from 56 to 52 per cent, while that of Eastern Europe - from 14 to 11 per cent. As far as imports are concerned, the share of the former Soviet Union was reduced from 54 to 49 per cent, and that of Eastern Europe - from 19 to 9 per cent.

### FOREIGN TRADE OF BULGARIA<sup>1</sup>

(mln USD)

Indicators	1989	1990	1991
Total amount of exports	11,091	8,458	4,366
CMEA	7,953	5,843	1,981
In convertible currency			1,352
In transferrable roubles <sup>2</sup>	7,953	5,843	629
Other countries	3,138	2,615	2,385
Total amount of imports	13,441	10,798	4,114
CMEA	9,104	7,426	1,634
In convertible currency			1,302
In transferrable roubles <sup>2</sup>	9,104	7,426	333
Other countries	4,337	3,372	2,479

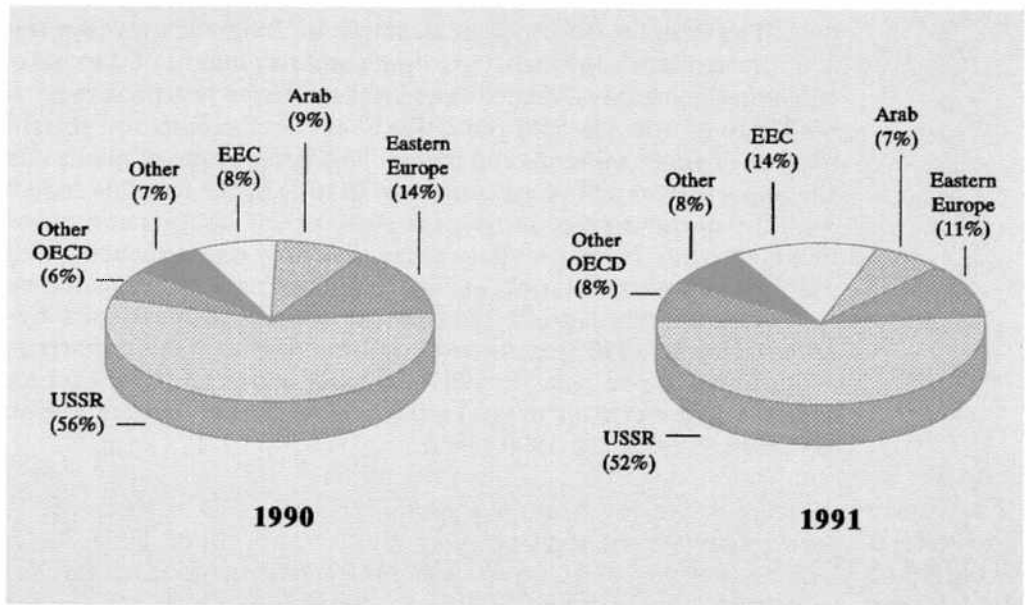
Note: <sup>1</sup> Includes the imports and exports in transferrable roubles.

<sup>2</sup> Up to 1990 transferrable roubles were converted in US Dollars at a price coefficient of 1.11 transferrable roubles to 1 USD for exports and 0.82 transferrable roubles to 1 USD for imports. In 1991 the coefficient was 2 transferrable roubles to 1 USD for both exports and imports due to the larger portion of machinery and equipment in the structure of trade.

The total amount of exports in convertible currency and transferrable roubles was reduced by 34.6 per cent instead of 25.6 per cent in keeping with the Government's programme. That was due, on the one hand, to the decrease of the exports to the former CMEA member-countries which was more than double the expectations and, on the other hand, to the smaller shrinkage of exports to all other countries which was 8.5 per cent instead of 15 per cent. Those figures were not only an evidence for the re-orientation of trade but they were also indirectly linked to the physical structure of exports. While in 1991 the exports of pharmaceuticals, cosmetics and perfumery to the USSR reached 400 million USD, the exports of textiles, products of the light and food industries as well as the output of machine building found markets in Western countries.

Reductions were even more drastic in imports, especially from the former

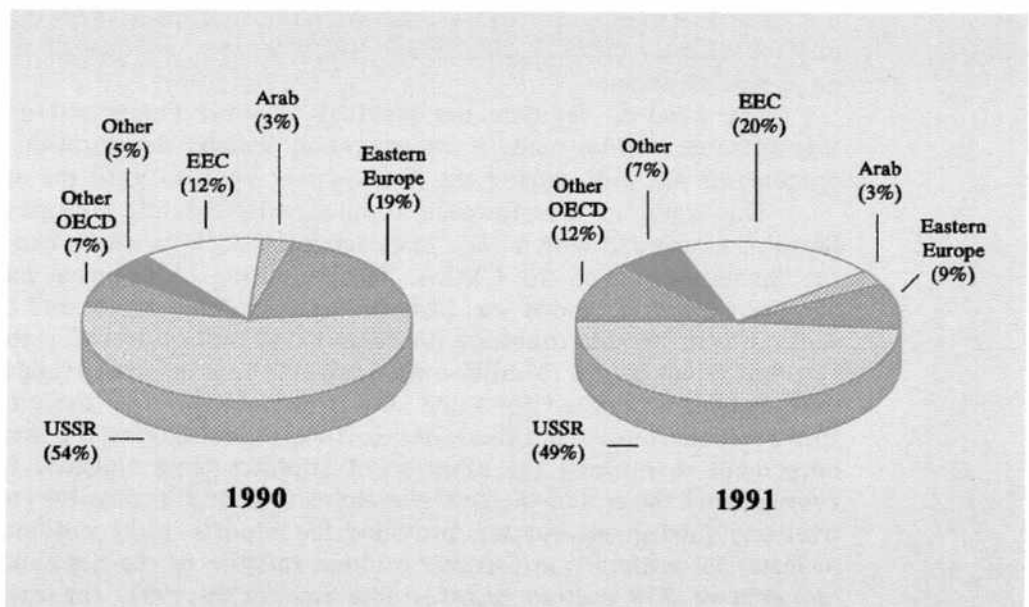
TRADE - EXPORTS



CMEA. Instead of the expected decline of the total volume of imports by some 33 per cent, the real decrease actually reached 62.2 per cent. The shrinkage proved less with respect to the countries outside the region of the former CMEA (27 per cent), while the reduction of supplies from the East European countries represented 78 per cent of the 1990 levels. The diminished amount of imports was related both to the reduction of the domestic demand and to the disintegration of the CMEA market.

Foreign exchange earnings from exports in convertible currency were 43 per cent higher than the 1990 level, while import costs rose by only 12 per cent. The increased exports in convertible currency was the most positive result of the process of external adjustment. Their share in the GDP rose from 34 per cent in 1988 to 49 per cent in 1991. Taking into consideration the fact that until very recently exports to the former CMEA accounted for more than 80 per cent of the

TRADE - IMPORTS



total export earnings, the changes observed were indicative of a partial adjustment to the external conditions and economic restructuring.

The data on the physical structure of Bulgaria's foreign trade show that in 1991 the tendency towards a growing absolute amount of exports of manufactured consumer goods to advanced industrial countries was preserved together with the tendency of considerable reduction (both in absolute and relative terms) of the exports of fuels, minerals and metals. The latter group of goods ranked first among the imports from advanced countries. In spite of the tangible reduction of the trade with the developing countries, the structure of imports and exports preserved its characteristics from previous years. Priority was attached to capital goods (in absolute and relative terms) in exports and to fuels, minerals and metals in imports.

The imported crude oil from all sources was reduced by 25 per cent in comparison to 1990, reaching 4.7 million tons and the imported natural gas was reduced by 15 per cent. (In 1989, Bulgaria imported 10 million tons of oil and 6.7 billion cubic metres of natural gas.) The physical amount of imported oil products was preserved at the 1990 level.

### **The Trade with Eastern Europe and the Former USSR**

The Clearing Trade Agreement with the Soviet Union of 1991 envisaged a total amount of supplies equivalent to 5.5 to 6 billion USD, including the import of 5 million tons of crude oil. But at the end of the year the trade exchange proved much less than the expected levels. The major reason was the fast disintegration of the USSR after the attempted coup which failed in August. As a result of internal problems, for example, the oil supplies of 3.2 million tons remained much less than the amounts agreed. The collapse of the centralized control had a negative impact on the execution of the Clearing Agreement, including the issue of licences and the subsequent distribution of Bulgarian exports to the Soviet markets.

The strongly appreciated exchange rate for the Soviet exports to Bulgaria (1.8 roubles per dollar, whereas the free market exchange rate exceeded 100 roubles to the dollar) further restricted the opportunities for imports. At the end of August the occurrence of a positive balance in the clearing accounts led to the introduction of a disagio of the exchange rate for the whole year, except for oil which made Bulgarian exports to the USSR even less beneficial. Under those terms, the positive balance on non-oil accounts could not be substantially reduced.

The value of Bulgarian imports from the USSR was approximately 1 billion USD which was distributed as follows: oil - 450 mln USD; coal - 108 mln USD; natural gas - 243 mln USD; electricity - 160 mln USD. Bulgarian exports against oil included goods equivalent to about 500 million USD out of which 325 mln USD were pharmaceuticals, 50 mln USD were meat and other processed foods, 46 mln USD were machinery and equipment, etc. At the end of 1991 the balance was positive for Bulgaria (102 mln USD) which resulted from a positive balance of 206 million USD on the non-oil account and a negative balance of 103 million USD on the oil account.

The need to regulate the residual negative balances from the trade in transferrable roubles made it imperative to prolong the duration of the relevant agreements not only during the first quarter but also until the end of 1991.

The trade in transferrable roubles with Poland, Hungary and Czecho-Slovakia continued with a view to clearing the deficits which had remained after the disintegration of the CMEA. The reduction of negative balances through further exports of goods was insignificant, reaching at the end of the year 536 million transferrable roubles with Poland, 140 million transferrable roubles with Czecho-Slovakia and 75 million transferrable roubles with Hungary. The deficit with Poland accounted for some 70 per cent of the total deficit of Bulgaria in transferrable roubles and therefore, it is worth mentioning the intergovernmental agreement to prolong the duration of supplies from Bulgaria in transferrable roubles until the end of the first quarter of 1992 and its possible further extension over any subsequent quarter, provided the exports in the previous quarter were at least 100 million transferrable roubles. In spite of the net exports to Czecho-Slovakia of 250 million transferrable roubles in 1991, the problem with the



regulation of outstanding balances is still very acute.

## **The Trade with Other Countries**

The trade with the countries outside the scope of the former CMEA was restored from the depressed levels registered during the first half of 1991. The beginning of the stabilization programme with its strong impact on prices, wages, the foreign exchange rate and the structural changes in the institutional frame of trade led to considerable shrinkage of international trade flows. At the end of the year, the exports to those countries increased almost 4 times in comparison to the second quarter. Imports recorded the same increase but from a higher starting point.

As a result of the decreased trade with the Middle East, the European Community turned into Bulgaria's major foreign trade partner with respect to convertible currencies. The General System of Preferences of the EC included Bulgaria as of 1 January 1991 and its effect might be expected in 1992. The usual tariff and non-tariff restrictions derived from the common agricultural policies of the EC were applied to Bulgarian agricultural exports. Bulgaria is a net exporter of such products and the opening of the markets of the Community might become an important incentive for production recovery. The quantitative restrictions on textiles and ferrous metals are expected to be lifted in 1995.

In October 1991, the US Congress ratified a Trade Agreement with Bulgaria granting it the most favoured nation status. As a result, a substantial decrease of customs duties is expected (2 to 9 times less than the current levels).

In spite of the substantial reduction of the total amount of trade, in the middle of the year a real trade re-orientation started increasing the relative share of the advanced countries from the OECD from 14 per cent in 1990 to 22 per cent in 1991. The figures about the exports of some major goods showed that the greatest increase was recorded for tobacco (51 per cent), urea (32 per cent) and electric trucks (56 per cent).

As for Bulgarian exports, the main partner from the OECD was Germany both in 1990 and in 1991 with a relative share of 4.2 per cent and 4.8 per cent respectively. But Germany's share among EEC countries decreased from 53 per cent to 30 per cent because of the growing exports to Italy, Greece and the United Kingdom. In 1990 Germany was the third largest trade partner of Bulgaria after the USSR and Czecho-Slovakia, while in 1991 it occupied the second place after the former Soviet Union. A rather big increase was observed in the exports to the USA and Turkey whose relative share grew by 2 and 8.5 times respectively.

The share of the OECD countries increased in imports, too, from 21.6 per cent in 1990 to 32.8 per cent. Only the imports from Germany and Japan were reduced in relative terms. The reason was the same as in the case with exports, i.e. the increased imports from other EEC countries such as Italy, the United Kingdom and France. Nevertheless, Germany remained the largest exporter to Bulgaria with a relative share of 7 per cent followed by Austria, Italy and the United Kingdom. The share of the United States grew about 5.3 times.

## **6. Balance of Payments and External Debt**

### **Balance of Payments in Convertible Currency**

#### **Current Balance of Payments**

The deficit in the current balance of payments for 1991 was calculated at 886 million USD, while initial estimates exceeded two billion USD. The relative share of the negative balance in convertible currency in exports decreased from 44 per cent in 1990 to 24 per cent in 1991. A special contribution to this "shrinkage" resulted from the developments in exports to countries outside the former CMEA, especially during the second half of the year. OECD countries accounted for approximately 60 per cent, whereas their share in 1990 was equal to 45 per cent.

The improvement of the current balance of payments was due, on the one

hand, to the fact that the deficit in the trade balance (44 million USD) was smaller than the expected, i.e. the deficit was reduced by more than 700 million USD in comparison to 1990 and, on the other hand, to the accumulation of outstanding interest payments. With an expected relative share of the deficit of the current balance in the GDP of more than 20 per cent, it was actually equal to 11.7 per cent at the end of 1991.

Prior to 1988, services and transfers accounts (the "invisible" balance) was typically positive in Bulgaria. In 1989 their deficit started growing steadily. That resulted not only from the growth of the outstanding interest payments on credits and loans but also from the excess of costs over revenues in tourism and transport which occurred for the first time in 1991. In 1989 the revenues from interest payments began to decrease in connection with the failure of a number of developing countries to fulfil their commitments to loans which Bulgaria had extended on intergovernmental as well as commercial basis.

### **Balance of Payments and External Financing**

The economic reform in Bulgaria started with almost completely lacking foreign currency reserves and confidence on the part of the financial community. A priority task in the Government's programme supported by the IMF was to replenish the foreign currency reserves and provide external financing for covering the deficit in the balance of payments. The support of the financial community for Bulgaria began to gradually recover only after the signing of the one-year Stand-by Agreement with the IMF on 15 March 1991 and the attainment of a Frame Agreement with the official lenders from the Paris Club on 17 April. Apart from the IMF, the external financing of the 1991 balance of payments proved much lower than the expectations: a total of 261 million USD from the World Bank and the EC. The financial resources received represented less than 17 per cent of the external resources needed. Actually, the second tranche from the EC came in February 1992, in spite of the lack of financing from the G-24 member countries outside the Community. Although below the expected levels, the influx of financial resources as well as the substantial delays in the servicing of the external debt made it possible to increase the foreign currency reserves above the levels envisaged in the programme of the Government throughout the year. Thus the amount of outstanding interest payments in 1991 exceeded the total amount of the financing from the IMF, the World Bank and the G-24.

The deficit of the capital account was equal to 1.1 billion USD. That resulted from the lack of access to capital markets after the interruption of the national external debt servicing and the extremely low level of foreign investments (56 million USD). In 1991 202.5 million USD were repaid for the Yamburg gas pipeline from the USSR with imported natural gas. At the same time, on the basis of the expected servicing of principals before the freeze on the external debt repayment, the outstanding debt for 1991 was 1.4 billion USD.

The total deficit of the balance of payments was equal to 2.1 billion USD in 1991. Its financing was effected through deferred payments on the external debt to official and private lenders as well as through the use of resources from the IMF, the World Bank and the G-24.

### **Balance of Payments in Transferrable Roubles**

After the transition towards payments in convertible currencies as of 1 January 1991, the former CMEA member-countries continued to keep accounts in transferrable roubles with a view to retiring the outstanding balances on the accounts over a certain period of time. The lack of a multilateral basis of the system of payments of the International Bank for Economic Co-operation prevented the mutual settlement of balances and therefore, throughout 1991 attempts were made at their reduction by means of exports of goods on bilateral basis. Generally, agreements provided the possibility to calculate the balances in US Dollars at agreed, mutually acceptable rates after the expiry of the agreements.

The current balance of payments reached a level of assets equal to 596.4 million transferrable roubles as of 31 December 1991, whereas in 1990 the deficit amounted to 872 million transferrable roubles. That change resulted from the trade balance surplus and the insignificant deficit of the balance of services achieved in 1991. As is seen in the capital account, Bulgaria was a lender in transferrable roubles. Assets amounted to 408 million transferrable roubles and reflected the positive balance with the former Soviet Union and the negative balances with the other East European countries with which the agreements for payments in transferrable roubles have not expired yet.

## External Debt

The total amount of the external debt of Bulgaria was equal to 11.4 billion USD as of 31 December 1991, including the new external financing. The largest portion of the foreign debt of the country is concentrated in the Bulgarian Foreign Trade Bank (BFTB). Other commercial banks continued servicing their external debts which reached 485 million USD at the end of 1991, though their access to fresh financing and lending terms worsened after the freeze.

The distribution of the external debt according to its sources shows that private banks accounted for 78 per cent of the total amount, official lenders contributed 16 per cent and 7 per cent was the share of the former CMEA.

### EXTERNAL DEBT OF BULGARIA AS OF 31 DECEMBER 1991

Indicators	mln USD
Total amount of the debt <sup>1</sup>	11,375
including	
debt of the Bulgarian Foreign Trade Bank	10,183
to official lenders	1,607
to commercial banks	7,870
to CMEA (in convertible currency)	705
debt of other Bulgarian commercial banks	485
External debt/GDP ratio (%)	150
External debt/exports in convertible currency ratio (%)	272

<sup>1</sup> Interests accrued delay to subject to reconsignment are not included.

The ultimate objective of the strategy of Bulgaria with respect to the external debt is to restore the viability of the balance of payments which can be financed independently without the exclusive use of external resources received or foreign debt relief as the case was in 1991.

The normalization of relations with lenders is of special importance. The Agreement between Bulgaria and its official lenders within the frame of the Paris Club signed on 17 April 1991 could be considered as the first step to that effect. The payments of all outstanding debts as of 31 March 1991 as well as those due by March 1992 were deferred. Not all bilateral agreements, however, have been signed though 31 March 1992 was fixed as the deadline.

After the moratorium was declared on 29 March 1990, Bulgaria started regulating the relations with lender banks on a short-term basis, i.e. through a roll-over at every 90 days. Such an approach postponed the settlement of the problem but, at the same time, created opportunities for undertaking and implementing the radical economic reform which was indispensable to the solution of the debt problem. The debt/exports in convertible currency ratio was 271 per cent and the debt/GDP ratio was 150 per cent in 1991, while the average level of that ratio for

the 15 largest debtor nations was below 40 per cent. The debt and its servicing were even greater with respect to budget resources which were the only possible source for reducing the indebtedness of the country.

Taking into consideration the fact that the burden of the external debt is huge and the adjustment process is hard and risky, it becomes clear that the prospects for the Bulgarian economy depend on the settlement of the foreign debt problem. Therefore, on 23 January 1992 the National Assembly decided to assign the Government the task to reach an agreement with creditor banks on the final settlement of the problem through reduction of the debt and its servicing.

## **II. Fiscal Policy and State Budget**

In Bulgaria the consolidated state budget incorporates the budget of the Government, of local Government (regional and municipal councils) and the budget of the State Social Security.

## 1. Aims of the Fiscal Policy

Fiscal policy was accorded a key position at the start of the economic reform in February 1991. It had to simultaneously be reorganized in conformity with the requirements of the market-oriented reform, and to assume the role of a major macroeconomic lever for managing stabilization. That set two principal aims to fiscal policy:

- to reduce the redistributive functions of the state budget in the productive sphere;
- to get over the inherited fiscal imbalances.

The attainment of these aims meant to decrease the relative share of the state government revenue and expenditure in the GDP, and to relatively reduce the budget deficit at the same time. Such a trend of the fiscal policy should facilitate the imposition of "hard" budget constraints on producers.

The implementation of the 1991 budget took place under a high degree of inconclusiveness engendered by the uncertainty of the economic reform course, the unstable foreign economic environment, and the absence of reliable information on the relations between the macroeconomic variables. It necessitated a flexible fiscal policy course, responding to unexpected changes during the year. At the same time, in the course of the year, the budget had to "stop the gaps" of the not always well-coordinated economic policy, which eventually led to a deficit greater than the sustainable one in the complicated economic situation. Examples in this respect are: the spending on subsidizing the prices which remained fixed up to June 1991, the spending on financing the exporters to the Soviet market when Bulgaria reached a surplus in her trade with the former Soviet Union, etc. The excessive spending on social security remained a burden on the budget throughout the year.

## 2. The Budget Deficit and Its Financing

The restrictive nature of the fiscal policy pursued by the Government is reflected by the positive primary balance of the state budget.<sup>1</sup> In 1991 it amounted to 3.6 billion Lv, or 2.7 per cent of the GDP, whereas in 1990 it was 0.1 bln Lv, or 0.2 per cent of the GDP.

In 1991 the cash deficit<sup>2</sup> ran up to 5 billion Lv, or 3.6 per cent of the GDP. 2.3 bln Lv should be added to it, paid to cover passive foreign trade balances with

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<sup>1</sup> The primary balance on the state budget is the difference between the revenue and the total expenditure of the budget, the outstanding interests on the internal and external debt being deducted.

<sup>2</sup> The state budget cash deficit is the difference between the revenue and the total expenditure of the state budget, the accrued but actually unpaid interests on external loans being deducted.

## STATE BUDGET

Indicators	mln Lv		% of GDP		Structure	
	1990	1991	1990	1991	1990	1991
<b>Revenue</b>	24678.0	55922.9	54.3	40.4	100.0	100.0
Tax revenue	19944.0	51390.2	43.9	37.1	80.8	91.9
Direct taxes	10351.3	27744.9	22.8	20.0	41.9	49.6
Indirect taxes	4523.2	11202.0	10.0	8.1	19.0	20.0
Social security contributions	5069.5	12443.3	11.2	9.0	20.5	22.3
Non-tax revenue	4734.0	4532.7	10.4	3.3	19.2	8.1
<b>Expenditure</b>	26920.0	60946.5	59.3	44.0	100.0	100.0
Current expenditure	25513.0	58288.4	56.2	42.1	94.8	95.6
Wages and scholarships	3202.0	8774.6	7.1	6.3	11.9	14.4
On goods and services	7707.0	17528.1	17.0	12.7	28.6	28.8
Transfers	12218.0	23265.0	26.9	16.8		
Subsidies	6753.8	5470.9	14.9	4.0	25.0	9.0
Social security and welfare	5464.2	17794.2	12.0	12.9	20.3	29.2
Interests - paid	2386.0	8720.6	5.3	6.3		
On external loans	2079.4	566.4	4.6	0.4	7.7	0.9
On internal loans	306.6	8154.2	0.7	5.9	1.1	13.4
Capital investments	1407.0	2658.1	3.1	1.9	5.2	4.4
<b>Cash deficit</b>	-2242.0	-5023.6	-4.9	-3.6		
<b>Financing</b>	2242.0	5023.6	4.9	3.6		
External	-421.0	-2040.4	-0.9	-1.5		
Internal	2663.0	7064.0	5.9	5.1		
Bank	1991.0	3416.2	4.4	2.5		
Non-bank	672.0	3647.8	1.5	2.6		

Source: Ministry of Finance.

former CMEA member-countries from previous years. Thus, the total credit needs of the 1991 budget amounted to 7 bln Lv, or 5.1 per cent of the GDP.

Half of this deficit (49.8 per cent) was covered by a loan from the BNB. In this way the State Budget Act stipulation was met. The net issue of treasury bills financed 41.5 per cent of the budget deficit. The absence of secondary market for government securities, however, turned the treasury bills issue into a hidden form of BNB lending. Treasury bills were bought by commercial banks, which then received liquidity from the BNB.

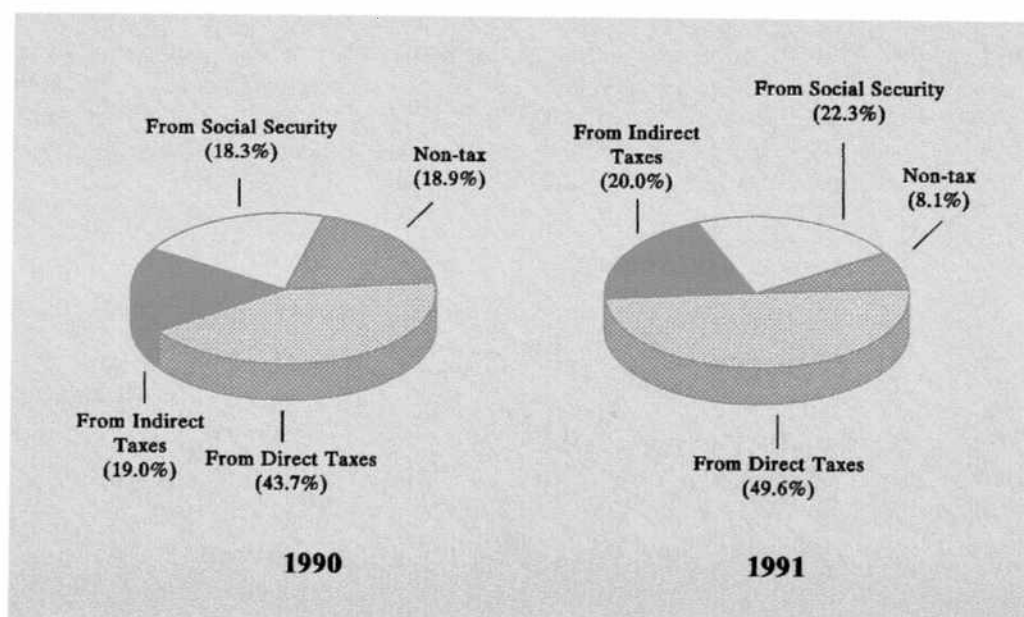
The Budget Act which has been passed envisages a deficit of 9.2 bln Lv, or 4.3 per cent of the GDP for 1992. The BNB is expected to directly finance 73 per cent of the government sector credit needs. The Central Bank deems it its duty to draw attention to the fact that to cover the budget deficit, or parts of it, by loans from the BNB contravenes Art. 49 of the BNB Act. If efficient measures are not taken in the medium-term to balance the budget, or to reduce the BNB share in its financing, the internal debt and its servicing will keep on growing as compared to the GDP. It will exert pressure for higher interest rates, will lead to more expensive loans to the Government, and to an even faster absolute and relative growth of the share of budget spending in servicing the internal debt.

Fiscal policy influences economic activity not only through the budget deficit, but through the revenue and expenditure policy as well.

### 3. State Budget Revenue

In conformity with the objectives of the economic stabilization, in 1991 the state budget revenue showed a relative decrease of 14 points, and reached 40.4 per cent of the GDP. In 1990 they accounted for 54.3 per cent, and in the end of the 80-s - 58 per cent of the GDP. There was a relative reduction of all major groups of revenues, but the reduction of the non-tax revenue was the most drastic (from 10.4 per cent to 3.3 per cent of the GDP). On the one hand, it reflected the fact that the Government discontinued the practice of seizing the financial assets of the enterprises at the end of the year. On the other hand, however, it was a result of the delays in bringing government fees and charges in line with the higher general price level, as well as of the absence of initiative in government property transactions - leases or sales. The effect of the delayed start of the small-scale privatization, as compared to the initial expectations, is also felt here.

#### BUDGET REVENUE



As regards tax revenue, in 1991 several amendments to the tax laws were made, constituting an intermediate stage in the overall reform of the tax system. The differentiation in the profit tax rates which varied from 15 to 95 per cent was eliminated. A unified profit tax rate of 40 per cent was introduced. The multiple indirect taxation was abolished by instituting three turnover tax rates - zero per cent, 10 per cent, and 22 per cent, with a clearly defined base.

The main problem with taxation, and hence with the budget tax revenue, is the relatively narrow tax base. There still exist a number of exceptions and privileges in taxation. The tax administration is adapted to an economy functioning on the basis of state ownership. For this reason, the emerging private business has a series of opportunities for tax evasion.

Thus, with practically the same revenue structure and taxation mechanisms, the budget had to cope with the tasks of the stabilization and the economic reform. The delay of the overall tax reform led to a slower growth of the budget revenue in comparison with the possibilities in the economic situation which emerged in 1991. This delay will continue having an adverse effect on the revenue dynamic pattern, and on the budget deficit in 1992 as well.



## 4. State Budget Expenditure

In 1991 the budget expenditure underwent more substantial structural changes in comparison with the revenue. The total budget expenditure fell by 15.4 points with regard to the GDP (from 59.3 per cent in 1990 to 44 per cent in 1991). There is virtually no field whose financing has not been restricted by the budget. At the same time, the required minimum for the functioning of the vital spheres financed by the budget was guaranteed.

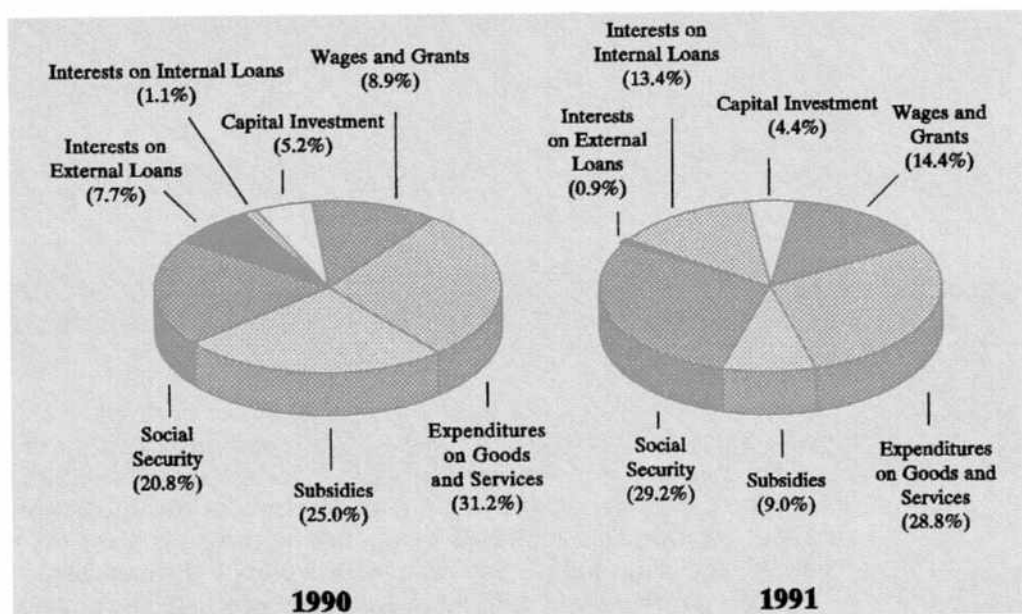
The price liberalization in February and June 1991 was accompanied by a drastic reduction of subsidies - by about 11 points as regards the GDP.

There was a considerable relative decrease of the current spending on goods and services, and of the investment expenditure of the budget - by 4.3 and 1.2 points as regards the GDP respectively. In this way, the budget contributed to a drop in the aggregate demand, and to a weakened inflationary potential.

At the same time the budget expenditure on pensions, benefits, and scholarships grew, as a result of the measures taken for the social protection of the population. However, there is yet a lot to be done for constructing the social safety network. So far its major drawback is that it does not accurately identify the range of the socially vulnerable who really need social welfare.

The internal debt servicing also turned into a substantial expenditure item in the budget. Whereas in the 80-s the spending on the internal debt servicing was infinitesimal, in 1990 it amounted to 0.7 per cent of the GDP, and in 1991 its level came up to 5.9 per cent of the GDP.

### BUDGET EXPENDITURE



### **III. The Monetary Policy of the Bulgarian National Bank**

# 1. Objectives and Tasks of the Monetary Policy

1991 saw the beginning of a qualitatively new monetary policy pursued by the Bulgarian National Bank. In the times of the centrally planned economy, the activities of the Bank in this sphere were aimed at the automatic meeting of the needs of the budget and the economic organizations for loans which were extended at actually fixed low interest rates (which were practically negative), ignoring the need to ensure medium-term stability of the macroeconomic indices and to maintain the equilibrium of the balance of payments. Thus the monetary policy turned into a factor generating excessive liquidity in the economy.

The reform in the monetary sphere is seeking to achieve the following major tasks: to radically change the approach to the formulation of the monetary policy in order to transform it into a major instrument for the attainment of macroeconomic stability; to set up adequate infrastructure of the monetary policy, i.e. a two-tier banking system with a central bank independent from the executive branch of power on the one hand, and on the other hand, to provide normal conditions for competition among commercial banks; to gradually develop sophisticated levers for indirect monetary control which is compatible with the market economy. With a view to accomplishing the three major and interrelated objectives of the monetary policy, the Bulgarian National Bank had to undertake decisive measures for eliminating the monetary overhang, overcoming the inflationary pressures and stabilizing the foreign exchange market in 1991. A series of measures was drawn up in order to restrict the monetary overhang, including the time deposits (one-month, three-month, six-month, and one-year) offered to the population at higher interest rates, the relative reduction of the bank loans extended to the Government, the repayment of housing and consumer loans at preferential interest rates. Alongside with the price liberalization, those measures were the major instruments for eliminating the excessive liquidity. The inflationary expectations were reduced by means of a stringent and restrictive crediting policy which, together with the drastic increase of interest rates, promoted the attractiveness of the national currency and encouraged the release of commodity stocks.

## 2. Monetary Policy Instruments

### Credit Ceilings

Under the conditions of an inherited indebtedness of the economy and the need to stabilize it at much lower levels with a view to restructuring it from a medium-term perspective, the BNB had to pursue a strongly restrictive lending policy in 1991 and especially during the first half of the year. Credit ceilings were the main instrument for that purpose.

In order to restrict the credit expansion of commercial banks, ceilings were introduced for the maximum possible increase of the total debt on the loans in local currency for the business activities of the firms and other organizations owed to the banks. During the first quarter of 1991 the ceiling was equal to 102 per cent

of the balance of the total debt on such loans as of the end of 1990.

During the second quarter of 1991 ceilings reached 112 per cent of the above base and banks were recommended to channel new loans mainly towards overcoming the production decline and increasing the amount and diversity of consumer goods. For the purposes of the normal seasonal expansion of production during the summer months and in the beginning of autumn, the BNB raised credit ceilings successively to 125 per cent and 132 per cent during the third quarter and 152 per cent during the fourth quarter.

The main positive outcome of the applied credit ceilings was the fulfillment of the major indicator in the programme agreed with the IMF, i.e. the "net internal assets" growth which was kept below the upper limit envisaged in the programme.

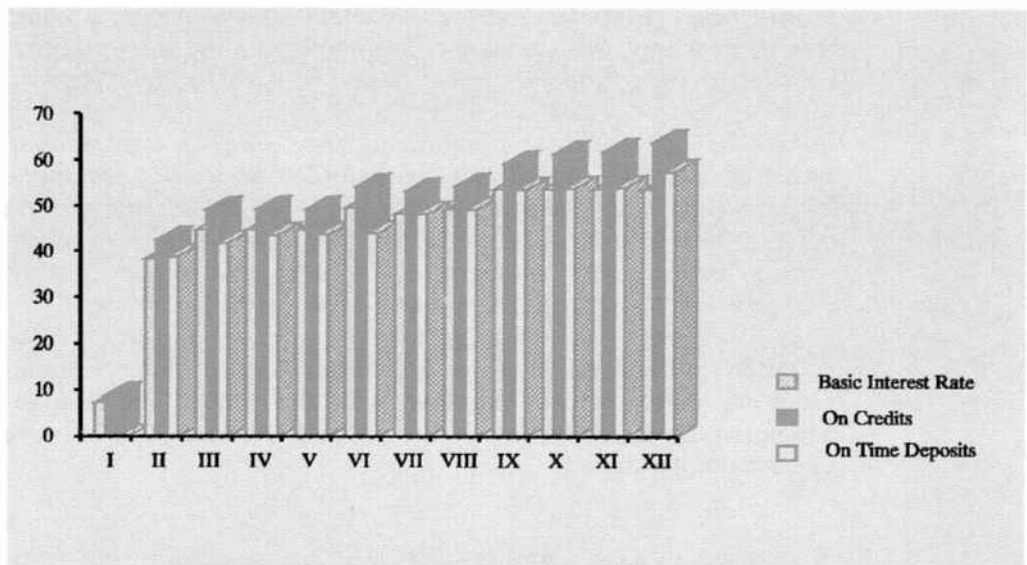
As a result of the rigid restrictive policy, the total amount of the domestic lending decreased in nominal terms during the first four months of the year. During the following few months, however, it started rising again but it was not until the fourth quarter that its level surpassed that of December 1990.

## Interest Rates

An urgent necessity to change interest rates arose as early as 1990. The maintenance of steady and low interest rates (interest rates were invariably equal to 4.5 per cent throughout the whole 1988-1990 period ) was inconsistent with the development of inflationary processes. The transition to an active utilization of interest rates as an element of the monetary policy was inevitable and it was, in fact, the beginning of the economic reform. On 18 January 1991 the Council of Ministers, which was the then competent authority on that matter, fixed the basic interest rate at 15 per cent per annum and ceded the right to its further quotation to the BNB.

INTEREST RATES IN 1991  
(average annual amount)

(per cent)



The management of interest rates on the part of the BNB was fully subordinated to the general objectives of the monetary policy of the Bank to keep the inflation rates under control and maintain the stability of the national currency.

In the beginning of February the Government liberalized the prices of most goods and services and the huge latent inflationary potential accumulated over the years led to a drastic price increase. Against this background on 7 February the BNB raised the basic interest rate to 45 per cent. As a result the inflationary blow was softened and gradually the acute shortages of goods started disappearing. In

the course of the year the basic interest rate level changed three times parallel to the inflation rates and inflationary expectations; the basic interest rate was 54 per cent as of 31 December 1991.

### **Interest Rates Policy of the BNB**

The new policy of interest rates led to changes in the nominal amount and structure of the money supply. The maintenance of a relatively high nominal level of the basic interest rate contributed to the substantial reduction of the loan expansion. On the other hand, high interest rates on deposits motivated savings and the accumulation of "excess money" in the banks. As a result, the less liquid components of money, such as time deposits and savings accounts, increased their relative share.

In spite of its high level, except for some months (March, April and September), the basic interest rate remained below the inflation index which implied that it was actually negative. The interest rate policy of the Bank which was supported to a certain degree by the policy of restricting wages and government spending played an important part in keeping inflation and exchange rates within relatively tolerable limits in the context of the general delay of the structural reform.

An important aspect of the interest rates policy of the BNB as the central bank was the adopted Provisional Interest Rate Tariff which the BNB applied to the operations in local currency in the country. It was for the first time that it introduced diversity in the interest rates used in the refinancing of banks which were conducive to the development of the lombard and discount policy of the Bank as well as in the interest rates applied to different time deposits.

### **Interest Rates Policy of Commercial Banks**

Important changes in principle were effected also in the interest rates policy of commercial banks. Prior to the end of 1990 the interest rates on loans which were formally subject to agreement with lenders proved actually very restricted up to two percentage points above the basic interest rate. Deposit interest rates were fixed primarily by the State Savings Bank (SSB) at very low levels.

With the interest rates liberalization in 1991 the establishment of interest rates was based on market principles. Undoubtedly, throughout the year banks were too much dependent on the resources obtained in the form of refinancing on part of the BNB. Insofar as those resources were offered under terms which were directly related to the basic interest rate, the interest rates policy of banks was too dependent on its level. Yet, the structure of lending sources (the small relative share of the banks' own resources and the settlement accounts of firms which were not interest-bearing until October and afterwards had an interest rate equal to about 15 per cent) exerted an increasing influence on the possibilities of banks to offer cheaper loans. Beneficiaries in this respect were those commercial banks which were former BNB branches and stood closer to the clients because a smaller portion of their lending resources resulted from refinancing by the BNB or from the interbank market. Besides, the monopoly situation of some banks (mainly in smaller towns) enabled them to apply lower interest rates on deposits. Gradually this difference in the conditions gave rise to a certain differentiation of interest rates on loans and deposits; the difference between the lowest and highest interest rates reached 6 to 8 percentage points on an annual basis.

The chart shows the change of the average levels of the basic interest rate and the interest rates on loans and deposits calculated on an annual basis through the average monthly levels.

### **Refinancing**

This instrument preserved its substantial role in 1991 as well, because the BNB continued to provide a considerable portion of the lending resources of commercial banks. At the same time, its application underwent great changes. Although it continued the practices applied over the past years to deposit a big part of the free resources of the State Savings Bank, the State Insurance Institute and the Bulgarian Foreign Trade Bank at the BNB, the Central Bank gave up its monopoly position with respect to the allocation of lending resources among banks

in the beginning of 1991. Banks had most of their needs for credits met at the interbank market.

In 1991 the refinancing of commercial banks was carried out along the following lines:

(i) In February loans as a form of replenishing the resources of commercial banks were replaced by **short-term deposits** with a term of up to three months. Deposits were offered within the framework of the direct, unsecured refinancing. Until 20 August 1991 the BNB offered commercial banks three-month deposits of up to 20 per cent of the total amount of the debt from loans for production needs and capital investments as of 31 December 1990. The amount of deposits increased from 6,254 million Levs in the beginning of the year to 6,828 million Levs during the second quarter.

(ii) The BNB continued to provide lending resources **to cover the capital investment loans which it had transferred to commercial banks** and whose repayment was deferred to the time after 1 January 1991 as per Protocol No. 41 of 1987. The size of those loans was 7,674 million Levs in the beginning of the year. The provision of resources for bad debts continued throughout the year since the overindebtedness of firms was partially settled at the end of the year when 1,789 million Levs of the funds related to the freeze were converted into government debt.

(iii) Until 15 October 1991 the BNB provided some commercial banks with deposits to ensure that part of the borrowed resources which was designated to cover the balance of the loans to firms and enterprises **undergoing conversion** from military to civilian production in accordance with Ordinances Nos. 54 and 119 of the Council of Ministers of 1990. The total amount was 2,449 million Levs. After 15 October 1991 the BNB undertook a gradual reduction of those deposits (by 25 per cent monthly) to eliminate the direct refinancing of such loans before 15 February 1992.

(iv) Alongside of the reduction of the direct, unsecured provision of deposits to banks, the BNB gradually introduced the classical forms of refinancing, such as **loans against collateral and discount operations**. But the lack of statutory regulations as well as the small amount and diversity of securities was the major reason for the transition from the direct, unsecured refinancing of banks to the new monetary instruments to involve another instrument for injecting liquidity into the banking system, i.e. the auctions for offering deposits to commercial banks.

### **Interbank Deposit Auctions**

The BNB started applying the system of auctions for short-term deposits at commercial banks on 15 September 1991. Auctions were held twice a month, on the 1st and the 16th day of the month. In 1991 seven auctions took place and the deposits at those auctions were equivalent to 14,718 million Levs. The debt of commercial banks on the deposits got at the auctions amounted to 5,984 million Levs as of 31 December 1991. The Regulations on Holding Auctions for Interbank Deposits in Levs enabled commercial banks to purchase and sell deposits at the auctions. However, the latter possibility was not used. Out of the total 14,718-million-Levs-worth deposits, 14,700 million Levs were provided by the BNB and only at the first auction two commercial banks offered deposits equal to 18 million Levs for sale. That came to prove that commercial banks preferred to offer their free resources at the interbank market mainly because in the case of direct agreements deposits had shorter terms (usually they were due at call) which made them more dynamic as compared to the one-month term of the auction.

The average monthly interest rate on deposits at the auctions was 4.9 per cent (which represented a simple interest rate of 58.8 per cent per annum or a margin of 4.8 per cent above the basic interest rate over the relevant period). The lowest interest rate was recorded at the first auction (monthly interest rate of 4.5 per cent or annual interest rate of 54 per cent), while the highest rate was reached at the last auction in 1991 (5.26 per cent). The high interest rate at the last auction (63.12 per cent per annum) can be explained with the introduction of the

Provisional Interest Rate Tariff which the BNB applied to the operations in the country in Levs (in accordance with its provisions, the Central Bank offered commercial banks three-month deposits at 5 percentage points above the basic interest rate or 59 per cent and one-month deposits at 3 percentage points above the basic rate or 57 per cent) as well as with the increased demand for resources in the wake of the withdrawal of deposits equal to 3.8 billion Levs from the direct refinancing of commercial banks in November and December.

In 1991 the average number of participants in the auctions was 41 commercial banks with approximately 75 bids which was indicative of a substantial interest in the auction system of refinancing. At the end of the year, 27 per cent of the refinancing of commercial banks came from deposits offered at auctions whose interest rates were market-based. The interest rates reached at the auctions influenced also the growth of interest rates at the interbank market but, at the same time, it made commercial banks manage their own and borrowed funds in a more efficient way.

### **Lombard Loans**

The refinancing of commercial banks through lombard loans, in the form of loans against collateral of treasury bills issued by the Ministry of Finance, began in the second half of October. Until 31 December 1991, the BNB extended loans equal to 845.1 million Levs to 15 commercial banks against a collateral of government treasury bills with a total face value of 1,273 million Levs. Lombard loans seem to be the most promising form of refinancing commercial banks for the time being. On the one hand, they create conditions for a considerable portion of the state budget deficit to be financed by means of purchasing government securities by commercial banks or households and private businesses (after the secondary market develops) which will ensure non-inflationary financing of the government debt. On the other hand, the orientation of banks towards this type of refinancing contributes to improving the quality of their active operations through an increased share of more liquid assets at a much lower risk.

### **Discount Operations**

In October the BNB set the beginning of a discount policy in the refinancing of commercial banks. Before the end of the year several discount operations were carried out with bills of exchange and promissory notes issued by commercial banks and secured by the Ministry of Finance or other commercial banks. The total amount of discount loans extended by the BNB was equal to 612 million Levs.

The BNB undertook swap operations in order to create additional facilities for refinancing the activities of commercial banks.

### **Minimum Reserve Requirements**

The minimum reserve requirements which commercial banks deposit at the BNB for the borrowed funds were used mainly as an instrument of the monetary policy rather than for ensuring the stability and reliability of the banking system in 1991. Although their level was preserved at 7 per cent, some new aspects characterized the application of this instrument. First and foremost, banks were entitled to transfer in foreign currency the minimum reserve requirements on the borrowed foreign exchange. Another important change was the fact that borrowed funds obtained at the interbank market were deducted from the amount used to calculate the minimum reserve requirements.

The total amount of the minimum reserve requirements was almost trebled reaching 3,497 million Levs as of 31 December 1991 as compared to 1,191 million Levs as of 31 December 1990. The reason was the increased amount of borrowed funds in foreign currency due to the higher exchange rate of the US Dollar.

## **3. Money Supply**

In 1991 there was a tangible increase of the money supply (measured in "broad money") by almost 62 billion Levs (2.25 times). The foreign currency

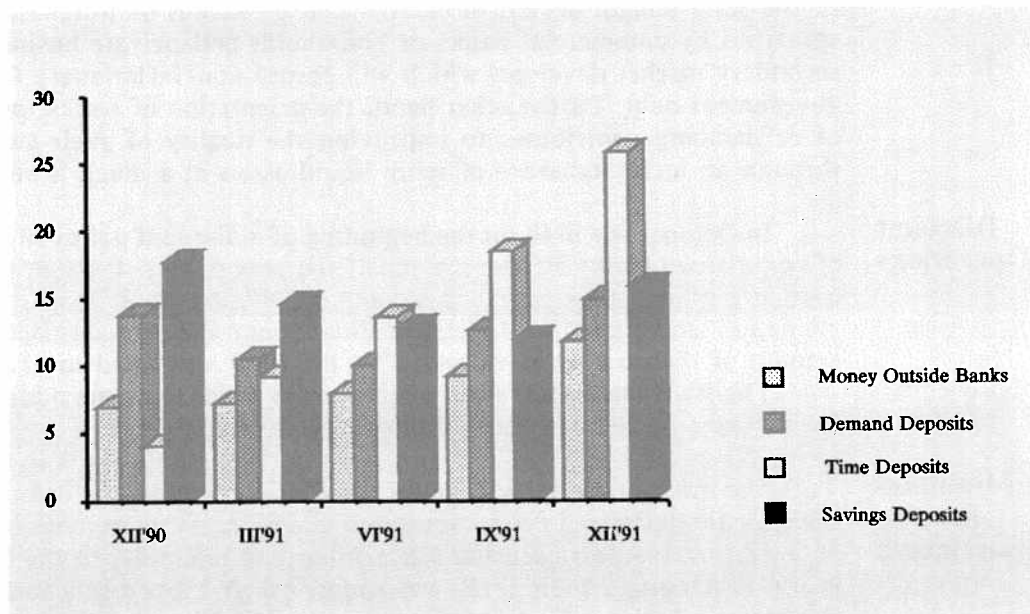
element increased more substantially (almost 8 times) as a result of the changed exchange rate of the Levs to the major convertible currencies. If we put the impact of the exchange rate aside, the increase was only by 0.7 per cent. The local currency element increased by some 25.5 billion Levs (58.9 per cent).

### Dynamic Pattern of the Money Supply

The dynamic pattern of the money supply showed some interesting fluctuations in the course of the year. During the first month after the price liberalization (February) a tangible real decline was observed as compared to January (approximately 8.3 per cent). The foreign currency element decreased more sharply (by 12.6 per cent), while the local currency was reduced by some 2.1 billion Levs (4.9 per cent). The reduction was entirely at the expense of highly liquid money ( $M_1$ ). Demand deposits in Levs (including current accounts of firms and individuals with banks) decreased by more than 2.8 billion Levs or 20.1 per cent, while the availability of foreign exchange on business accounts was reduced by 12.5 per cent with a minimal increase of money outside banks equal to 184 million Levs (2.5 per cent). Conversely, quasi-money (potential money) recorded a minimal real growth of 2.2 per cent, while the decrease of savings deposits by more than 1.3 billion Levs (7.6 per cent) was set off by the greatly increased time deposits (over 1.8 billion Levs or 43.3 per cent) as a result of the interest rates policy.

DYNAMICS OF THE LEVS COMPONENTS OF MONEY AGGREGATES

(bln Levs)



The subsequent period which lasted until the middle of the year was characterized by a comparatively moderate growth of the real value of broad money as a whole, but with a different intensity of its structural elements. The total increase was about 6.5 per cent; foreign exchange increased insignificantly (2.6 per cent), while the local currency element increased by some 3.7 billion Levs or 9 per cent. That was the time of a certain stabilization of the highly liquid money ( $M_1$ ) which increased only by 2.3 per cent. The increase came from the foreign currency element, whereas the growth of the money outside banks by almost 584 million Levs was set off by the reduction of the demand deposits in Levs by some 1.3 billion Levs. The impact of the interest rates policy was felt stronger. Time deposits increased by 7.6 billion Levs (more than 2.2 times) to which part of the demand and savings deposits (reduced by 3.2 billion Levs) was shifted. Part of the foreign exchange savings of individuals (reduced by approximately one quarter) were either converted into Levs or transferred to time deposits. In the final



analysis, quasi-money increased by 17.6 per cent.

Money supply processes became much more dynamic during the second half of the year. Broad money increased in real terms by more than 33.7 per cent (calculated at a steady exchange rate of 20 Levs for one US Dollar). Less dynamic was the change of highly liquid money ( $M_1$ ) which increased by almost 25 per cent. The most substantial growth was recorded by the money outside banks - almost 3.8 billion Levs (47.4 per cent). As a result of the interests introduced on the current accounts of firms, the absolute amount of demand deposits in Levs increased (by 4.9 billion Levs for the six-month period and 2.7 billion Levs in December only). Greater fluctuations were observed in the foreign currency accounts of firms; they increased by 20.8 per cent over the period June through November and then dropped drastically in December, reaching 11.6 per cent above the level for the six-month period. The substantial monthly deviations in the foreign currency accounts at that time resulted from the influence of both seasonal and psychological factors related to objective or speculatively generated inflationary expectations.

The higher growth rates of the quasi-money supply were the logical outcome of the anti-inflationary policy of the Central Bank. The interest rates policy pursued by the BNB, though slowly, influenced the structure of the money supply. In the course of the year, the share of the less liquid element of money, i.e. time and savings deposits, increased. The growth of 53.8 per cent resulted from the new drastic increase of time deposits (more than 12.1 billion Levs or 88.2 per cent) and the increase of savings deposits (22.4 per cent) with an insignificant decrease of foreign currency deposits.

## Monetary Overhang

A salient feature of the national economic development over the recent years was the steadily increasing monetary overhang. Thanks to the strict monetary policy pursued by the BNB in 1991, that negative tendency was decisively reversed. That was most clearly illustrated by the ratio between the money supply and the GDP, as shown in the following table:

(mln Levs at the end of the period)

Indicators	1986	1987	1988	1989	1990	1991
GDP	34,424	36,531	38,345	39,579	45,390	138,400
Broad money	33,511	35,473	39,133	43,250	49,648	111,608
Broad money/GDP	97.4	97.1	102.1	109.3	109.4	80.6

That ratio is also known as a quantity characterizing the velocity of money movement. The smaller the ratio, the higher the velocity, i.e. the smaller the amount of money needed to serve the economy.

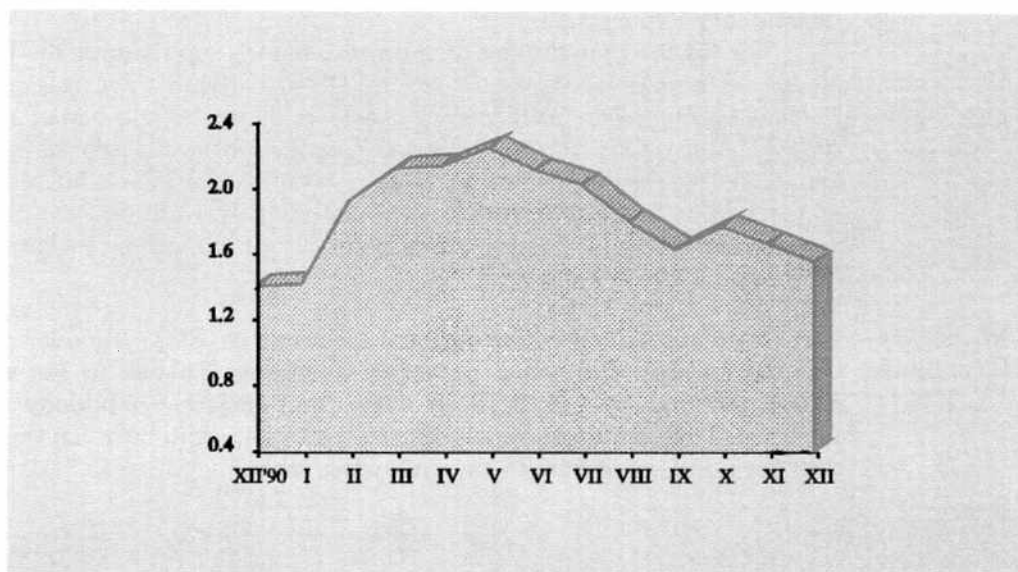
The dynamic pattern of reserve money (including the issue of money, deposits of commercial banks with the BNB and the mutual deposits of commercial banks) followed a trend of smooth increase after an initial decline (mainly due to the clearance of old relations between banks). The more substantial growth over the last three or four months emerged also as a result of the growing mutual clearing operations.

This pattern determined the hyperbolic curve of the money multiplier. The above results, however, can not serve as a reliable basis for qualitative assessment of the monetary policy. In practice the optimal value of the money multiplier varies from country to country depending on the respective economic environments.

## DYNAMICS OF RESERVE AND BROAD MONEY IN 1991

Indicators	XII.1990	I	III	V	VII	IX	XII
On current exchange rate basis, levs	2.84	2.88	15.165	18.247	18.692	18.952	21.811
Broad money, levs	49648	49869	69508	75960	83139	88274	111608
Reserve money, levs	40055	39611	32398	32872	40977	57857	77312
Money multiplier (broad money / reserve money)	1.24	1.26	2.15	2.31	2.03	1.53	1.44

## DYNAMICS OF MONEY MULTIPLIER IN 1991



## 4. Loan Dynamics

Over the last few decades, loans were a major factor for creating monetary overhang in the economy and generating inflation. Therefore, the development of the indebtedness of the economy to the banking system was very carefully scrutinized and controlled in 1991.

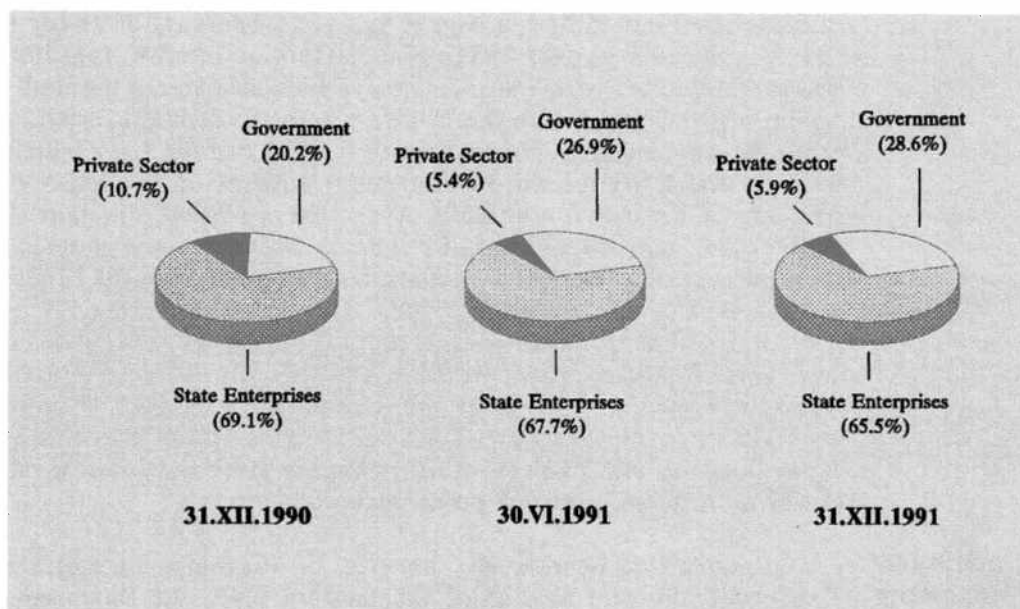
The information on the loan characteristics of the various economic factors was summarized in the consolidated monetary survey.

### Net Domestic Assets

One of the most important elements of the total internal debt was the net receipts of the banking sector from the Government. They increased from 13,657 million Levs in the beginning of 1991 to 32,425 million Levs at the end of the first half of the year (137 per cent) and reached 46,165 million Levs (238 per cent) during the second half of the year, where the foreign currency element increased most substantially. The receipts in local currency from the Government were seemingly stable: 9,821 million Levs at the end of 1990; 8,556 million Levs in the middle of 1991 and 9,403 million Levs at the end of 1991 or a total reduction by 4.3 per cent. Actually, the reduction resulted from the debt repaid with the receipts from the sale of gold to the BNB by the Ministry of Finance. The tangible increase of the exchange rate of the US Dollar affected the calculation of the foreign currency element in all indicators characterizing the national economy. The same

picture was observed in the calculation of the foreign currency receipts of the Government. They increased from 3,836 million Levs in the beginning of the preceding year to 36,762 million Levs at the end of 1991 or a total increase of 9.6 times. Leaving aside the influence of the exchange rate, we can say that the increase of the receipts in convertible currency was only 25 per cent in 1991.

#### CREDIT INDEBTEDNESS OF THE ECONOMY



The receipts from the non-government sector were the second essential element of the net internal assets. In 1991 their development was as follows: from 53,787 million Levs in the beginning of the year through 87,984 million Levs in the middle of the year and 115,509 million Levs at the end of the period. The structure of the receipts of banks from the non-government sector pointed to a substantial increase of the receipts from non-financial government institutions which developed from 46,540 million Levs in the beginning of 1991 to 105,976 million Levs as of 31 December 1991 or an increase of 127.7 per cent. A more thorough analysis, however, comes to prove that the local currency element increased only by 51.2 per cent, while the substantial increase of 603 per cent of foreign currency receipts actually resulted from the changed exchange rate. Adjusted to a steady exchange rate, this figure is reduced by 8.5 per cent.

The comparatively weak (against the background of the inflation rates) growth of the local currency debt of non-financial government institutions to banks was due to the restrictive lending policy of the BNB. The stagnation in the foreign currency lending resulted primarily from the production decline as well as from the liberalized foreign exchange regime in accordance with which every firm was free to buy the foreign currency it needed.

The analysis of the bank receipts from the private sector showed a total increase of only 31.5 per cent. The increase, in fact, resulted only from the private business development loans which reached 4,651 million Levs at the end of 1991, compared to 767 million Levs at the end of the preceding year. However, that was set off through the reduced debt on mortgage loans to households (by 28 per cent) and the loans for current needs of the population (by 19 per cent) which was determined by the interest rates policy of the BNB that restricted not only the demand for fresh borrowings but also the repayment of old debts before maturity.

## 5. The Relationship of the State Budget with the BNB and Commercial Banks

### The Internal Debt

In 1991 the BNB extended to the Ministry of Finance eight loans equivalent to 4,299.5 million Levs to finance the annual budget deficit adopted with the 1991 State Budget Revision Act.

The debt of the Ministry of Finance as of 1 January 1991 was equal to 11,279 million Levs, including the loan extended in February 1991 for the purposes of covering the 1990 budget deficit of 2,600 million Levs. In July 1991 an agreement was reached under which the Ministry of Finance offered the BNB to buy the gold which was deposited with the Ministry and had been purchased also with funds from the state budget. The amount of 5,720.1 million Levs which was due to be paid by the BNB retired an equivalent amount of the loans extended to the Ministry of Finance by the BNB. After that operation, the debt of the MF to the BNB on the loans extended as of 1 January 1991 remained equal to 5,558.9 million Levs. As a result, the debt of the Ministry of Finance to the BNB reached 9,795.4 million Levs as of 31 December 1991.

In 1991, pursuant to para. 7 of the Transitional and Final Provisions of the 1991 State Budget Revision Act, the Ministry of Finance assumed part of the bad debts of state enterprises to the banks equal to 4,125.3 million Levs as a government debt. For that debt, commercial banks are issued bonds with a repayment term of 15 years as of 1 January 1997 and interest rates equal to the basic interest rate plus one percentage point.

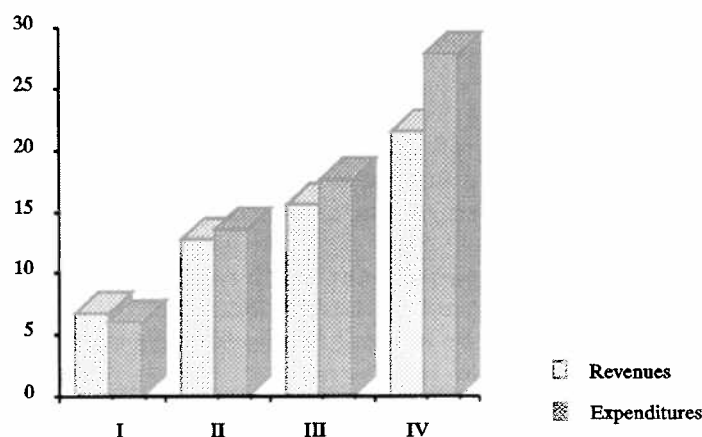
### Cash Basis Reporting of the State Budget

Pursuant to Section III, item 21 of the State Budget Composition and Execution Act, and Art. 45 of the Law on BNB, the Bulgarian National Bank organizes and effects cash basis reporting of the state budget through commercial and other banks. For this purpose, twice a month it receives, from the banks-correspondents on the state budget cash execution, information by the unified state budget classification, endorsed by the Ministry of Finance.

The amount of revenues for the cash execution of the consolidated state budget, calculated on the basis of the accounting data received after the annual settlement of the budget accounts of the BNB and commercial banks was 85,258.4

CASH BASIS REPORTING OF THE STATE BUDGET BY QUARTERS, 1991  
(revenues and expenditures)

(bln Levs)



million Levs as of 31 December 1991, while the amount of spending was equal to 84,847.9 million Levs. Those amounts did not include the data on the budget accounts with the Bulgarian Foreign Trade Bank, the State Savings Bank and the State Insurance Institute since those institutions did not send information to the BNB. The excess of the revenues equal to 410.4 million Levs remained on the accounts of budget users for the purposes of financing the budget in 1992.

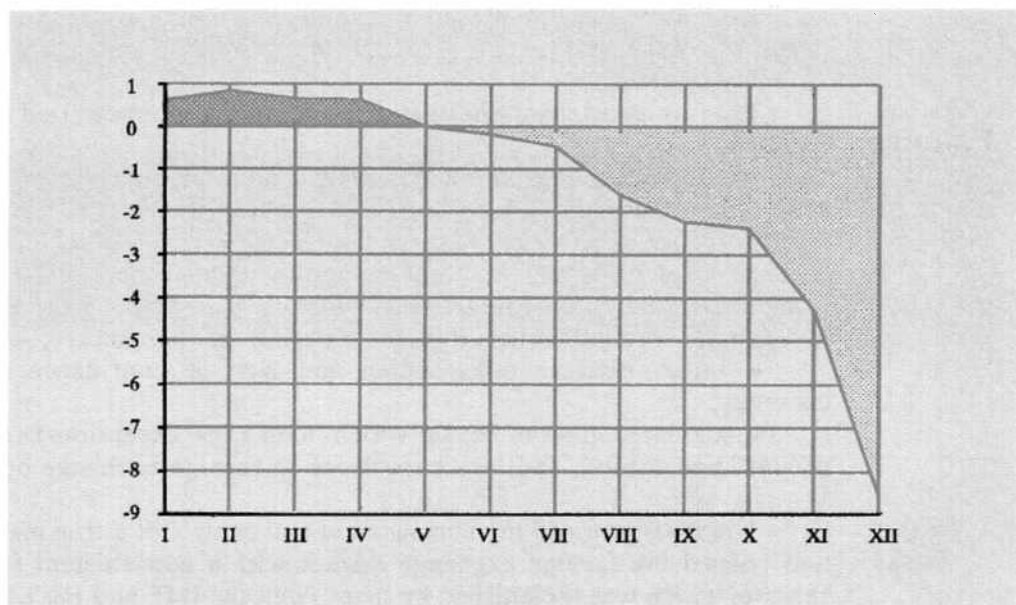
The amount of net revenues for the same period was 56,732.6 million Levs and accounted for 91.8 per cent of the revenues voted with the 1991 State Budget Revision Act. It was calculated as a balance between the revenues and the inner budgetary transfers (19,553.9 million Levs), the loans (net) extended by the BNB (4,236.5 million Levs) and the revenues from the issued government securities (4,735.4 million Levs). The biggest share in the total revenues for the year had the revenues in the fourth quarter. That was primarily the result of the faster growth of tax revenues, i.e. the tax payable on the profit of banks and insurance institutions.

The amount of net spending was 65,294 million Levs or 92.9 per cent of the spending voted with the 1991 State Budget Revision Act. Again, the largest portion of the total amount was spent during the fourth quarter. Net spending was calculated as the balance between the outlays and the inner budgetary transfers (19,553.9 million Levs). The amount of net spending did not exclude the repayments on the loans used and the government securities since they were not recorded under separate items of the state budget.

A budget surplus was reported over the period January–May 1991 (the largest amount was reached as of 29 February - 837 million Levs)<sup>1</sup>. It was gradually reduced and as of 30 June 1991, net outlays in the cash budget exceeded net revenues by 175.1 million Levs. The surplus reached 8,561.4 million Levs as of 31 December 1991.

**CHANGES IN THE RATIO OF REVENUES AND EXPENDITURES ON THE CASH BASIS REPORTING OF THE STATE BUDGET, 1991**

(bln Levs)



The 1991 State Budget Revision Act envisaged financing of the budget deficit through government securities and loans from the National Bank, whereby loans could not exceed 50 per cent of the total financing. That condition was observed and the BNB financed the budget with 4,236.5 million Levs (in net terms)

<sup>1</sup> The data do not include resources of the budget accounts with the BFTB.

over the period January–December 1991.

According to the information from the Ministry of Finance after the final settlements of the state budget with all financial institutions, the amount of the cash deficit in the consolidated state budget was 7,638.6 million Levs. The report of the Ministry of Finance on the execution of the state budget as of December 1991 showed the following financing (in million Levs):

Non-banking	4,220.6
Issue of bonds and other securities	626.8
Issue of treasury bills and others	2,408.6
Repayments of treasury bills, BNB	-514.8
Issue of treasury bills, BFTB	1,700.0
Banking	3,827.0
Loans from the BNB	4,236.5
Servicing of debts, BFTB	-409.5
In cash	-409.0

## 6. Foreign Exchange Operations

### Forex Market

On 18 February 1991 a foreign exchange market started functioning in Bulgaria, based on the same mechanism, as those in countries with convertible currencies. This is the market mechanism of a free (floating) quotation of the major exchange rates to the Lev by commercial banks, and the daily fixing of the central rate by the BNB. This became possible after the enforcement of Ordinance No. 15 of the Council of Ministers of 8 February 1991, which liberalized the foreign exchange regime in the country. A similar regulation of the functioning of the market is contained in the Basic Principles of the Organization of the Interbank Foreign Exchange Market adopted by the BNB Board. A characteristic feature of the Bulgarian national currency remains its closed nature: settlements with foreign partners are effected in foreign currency units, and the participants in the interbank market (Levs for foreign currency) are only local persons.

### Forex Market Features

The foreign exchange market in the country is characterized by the following features:

- a high degree of liberalization of foreign exchange operations for natural and juridical persons, which (for some participants and types of operations - foreign exchange offices, brokerage houses) proved excessive, and encourages the speculative element and the emergence of a parallel market;
- extremely unfavourable economic environment - semi-paralyzed economy, a huge foreign debt, full credit blockade of the country;
- initial extreme dollarization and lack of confidence in the national currency;
- a great number of banks, which (with a few exceptions) are weak in terms of staff and capital, and lack experience in foreign exchange operations.

### Major Tasks

The BNB assumed the management and control of a true market mechanism and opened the foreign exchange market with a non-existent foreign currency reserve, which was replenished by loans from the IMF and the EEC in the course of the year. The concrete tasks faced by the National Bank were coordinated with the IMF recommendations to a great extent: maintaining the minimum required foreign currency liquidity of the banking system, and hence - of the economy. For this purpose the BNB, through interventions, placed over 200 mln US Dollars - part of the resource formed by the stand-by credit from the IMF; keeping the foreign exchange market operational by a relative stability of the volumes; maintaining the stability of the exchange rate of the Lev in the narrowest possible range at the minimum foreign exchange cost; developing a normal foreign

exchange market, and getting over the speculative expectations of devaluation of the Lev against foreign currencies, eliminating the "black" and the "grey" foreign exchange markets.

These tasks were largely accomplished as evidenced by the IMF comments on the BNB policy in 1991.

## **Developments in the Forex Market**

In 1991 the foreign exchange market gradually developed its qualitative characteristics. Initially, it was primarily a market between commercial banks and their clients. The interbank market covered transactions between the BNB and commercial banks. A period of stabilizing the exchange rate and the spread was needed for the decreed interbank market to really evolve into a mutual balancing of the foreign exchange earnings and expenses of commercial banks.

At the opening of the market there was a leap of the exchange rate and a large difference between the buying and selling rates - an average of about 2-3 Levs for the US Dollar, or about 10 per cent of the exchange rate. After the natural initial fluctuations there came both a stabilization of the rate, and a narrowing of the spread which, as early as the first half of March, fell below 1 Lv, or below 5 per cent of the exchange rate. There followed an active participation of the BNB in the foreign exchange market. It made for bridging the buying and selling rates closer. From the end of April to the end of May was the period of development of a most essential important element of the interbank market - foreign currency transactions between commercial banks. After the BNB presence on the market had led to a relatively long period of an exchange rate stability and of a spread below 0.5 Levs, or between 1 and 3 per cent of the dollar exchange rate the market between commercial banks evolved, at first hesitantly, and then more steadily. Consequently the BNB participation in the market had a two-fold result - stabilization of the exchange rate, and an organizational development of the foreign exchange market towards its transition from a formal into a real interbank market.

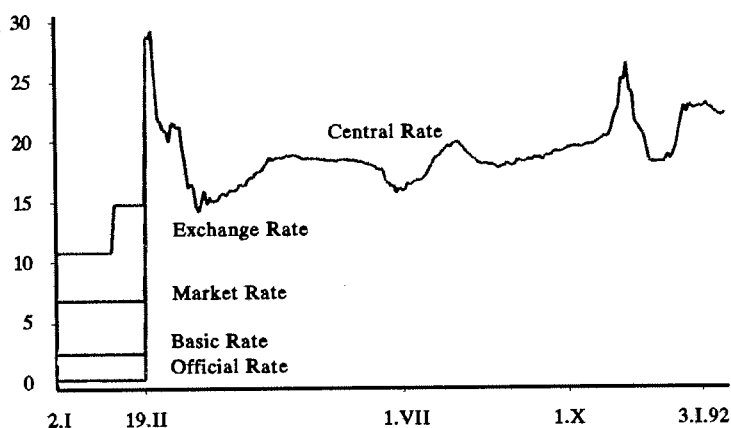
Without considering the foreign exchange operations in January and the first half of February, by the end of 1991 the turnover on the spot market (transactions with a value date of up to 2 days) in a dollar equivalent exceeded 1 billion US Dollars in one direction, and just as much in the other, the general trend being a volume growth. As an average for the year, nearly one-third of the officially registered payments on the foreign trade turnover in convertible currency passed through the forex market.

In 1991 the BNB initiated the swap market in the country. It developed after the BNB Board adopted the Tariff of Interest Rates on Extended and Received Funds in Levs of 11 November 1991. By the end of 1991, the BNB performed one-week swap transactions in both directions for a total of 50 mln US Dollars and 15 mln Deutsche Marks, for the purpose of covering the short-term needs for settlements in national and foreign currency. At the end of the year a one-month operation was effected for 3 mln US Dollars, due to end in 1992. In November short-term operations for the exchange of Levs and foreign currency between commercial banks and their clients started in November.

## **Central Exchange Rate of the BNB**

The reference rate (an indicator reflecting the condition of the convertible currencies market as of each date) became the so-called Central Bank Rate. It (as reflecting the condition of the foreign currencies market) serves to evaluate the operations on the clearing foreign trade transactions, which had a considerable share in the foreign trade turnover for 1991 - the clearing with the USSR amounted to one-third of the foreign trade turnover.

The quotation of a central rate of the Bulgarian Lev to the major convertible currencies is made by the BNB by means of calculating, at the end of each working day, the average weighted rate of the dollar equivalent of the foreign exchange transactions, made against Lev on the domestic forex market by the banks licensed for operations in the country and abroad, i.e. the banks whose foreign currency assets and liabilities abroad directly express the assets and liabilities of the



Bulgarian economy abroad. The reference rate of the Lev to the US Dollar determines the reference rate to other currencies, and for this purpose it is multiplied by the rate of the dollar to the other currencies at the same time on international markets on the value date of the transactions on the Bulgarian market. The reference rates come into force as of the beginning of the next working day.

After the transition to unified central rate, the publication of the former system of rates was discontinued. It included a basic rate, a market rate (based on the quotations from the foreign exchange auctions), and an exchange rate for banknotes. The only exception from the reference rate scheme was the disagio to the dollar rate, introduced at the end of August and referring to the clearing operations with the USSR.

The general trend of the Lev rate after the initial abrupt fluctuations was towards the gradual depreciation of the Lev, in spring the rate to the Dollar moving between 15.5 and 18.5 Levs for one Dollar, and during the last months of the year

**REAL EXCHANGE RATE OF  
LEV INDEX AGAINST USD**

(per cent)





- between 20 and 22 Levs for one Dollar.

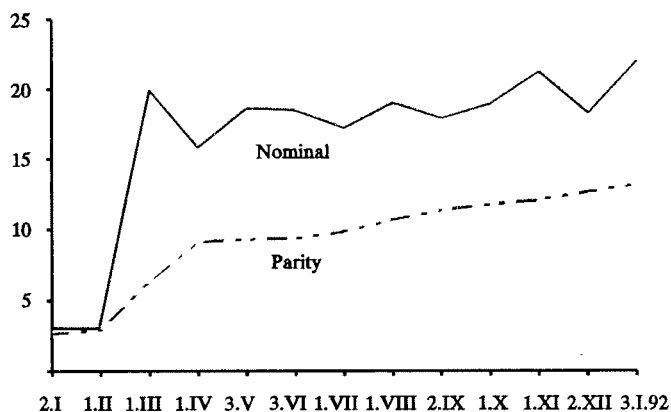
Thus the movement of the nominal rate (i.e. of the price of foreign currency transactions) showed a drop as compared to the various levels of the former banking quotations, and then, with its stabilization, it came to the former level for cash operations (the exchange rate), and by the end of the year there was a one-third depreciation as against the highest rate in March.

An indicator for the ratio between the agreed change of the rate of one currency to another (or to a "basket of currencies"), and the change of the price level in the respective countries is known as a "real" exchange rate index. The bilateral indicator for 1991 (Lev for US Dollar), shown on the value of the index of the real rate of the Lev to the US Dollar diagram, is calculated on the basis of the parity of the purchasing power of the Lev to the Dollar in 1990, and as price indices - the consumer price indices in Bulgaria and the USA. On the rate of the Lev to the US Dollar diagram there is a graphic presentation of the nominal and the parity rate in 1991.

The data on the real index show an initial drop, and after the stabilization of the foreign exchange market and of the exchange rate during the second quarter - a gradual rise. Despite the fact that the market rate remained depreciated as compared to the parity, a trend is observed of the nominal and the parity rate coming closer.

#### EXCHANGE RATE OF LEV AGAINST USD

(Levs per USD 1)



One may look for a link to the real depreciation of the Lev: in the inflationary expectations after the February price liberalization which led to a surplus demand for foreign currency, and respectively to a faster nominal depreciation of the Lev; in the psychological perception of the change of the rate for banknotes in February as a depreciation following the "parallel" market; in the import outstripping export in convertible currency not only during the first but also during the second quarter which predetermined the greater demand for foreign currency in the beginning of the year. Obviously, at the opening of the market the above-mentioned leap of the nominal rate, exceeding for a while even the average inflation rate, was inevitable.

With regard to the subsequent decrease in the degree of the Lev depreciation, a possible cause in general economic context are the changes in the relative importance of the factors determining the difficulties in production. The information of the National Institute of Statistics on the production performance in 1991 shows a change in the relative importance of the two major reasons for

the decline in output: the shortage of prime and raw materials, and the uncertain sales of the output. At the beginning of the year, when the first factor was relatively stronger, was observed a drastic fall of the real exchange rate. This may be due to the greater demand for imported substitutes of local raw materials in short supply, and respectively to the faster growth of the price of foreign currency as compared to the price of domestic products. The further change in the proportion between the two factors towards strengthening the importance of the second one testified to a new phase in the economy shrinkage, which forced producers to adjust and to reduce the demand for raw materials. Parallel to this relative change a rise of the real Lev rate index was observed.

On the other hand, a factor for drawing the nominal and the parity rates closer was the influence of the BNB on strengthening the nominal rate through instruments such as operations on the foreign exchange and the money markets, change in the basic interest rate, etc. Depending on the condition of the economy and the foreign exchange market situation, these approaches alternated, and sometimes complemented each other. The rise of the basic interest rate was usually accompanied by an appreciation of the nominal exchange rate, and in case of a fall of the basic interest rate the BNB used measures counteracting the Lev depreciation (e.g. interventions through the purchase of foreign currency on the market). In case of an abrupt depreciation of the Lev, the restrictive credit policy had a corrective impact on the exchange rate movement.

### **Foreign Exchange Regime**

The high extent of foreign exchange market liberalization presupposes a considerable liberalization of the relevant operations. In practice Ordinance No. 15 of the COM of 8 February 1991 provided free access to the foreign exchange market for almost all operations on the current account, and introduced a permissive regime for the operations on the capital accounts (the export of capital from the country - investments abroad, free transfers). With the existence of a functioning foreign exchange market after 18 February 1991 it became possible to:

- freely buy currency for all current payments against the submission of documents certifying the need for payments to foreign persons: import of goods and services, transport expenses, education and training, and medical treatment (the cases are enumerated in Art. 3, para. 2 of Ordinance No.15 of the COM). By the middle of the year the documents submitted by the depositors wishing to buy foreign currency (contracts, invoices, etc.) were replaced by declarations of the depositor stating the need for foreign currency;
- eliminate any compulsory sale of foreign currency by exporters. The export earnings can be transferred to accounts with Bulgarian commercial banks, freely utilized for import, deposited, or freely sold on the foreign exchange market. By the end of 1991 the free purchase and sale of foreign currency between companies registered with the seller's bank was permitted;
- to permit by Regulation No. 2 of the BNB of 28 March 1991 the opening of foreign exchange offices, sole proprietors and private companies included. By December 1991 their number ran up to 693 (opened by 336 companies). Unfortunately, owing to the absence of strict regulations for their operations, the foreign exchange offices "left" the premises and became the chief speculator on the foreign exchange market by the end of the year;
- to set up brokerage houses, financial ones included. Three of them were licensed by the BNB and used as its agents on the foreign exchange market;
- to fully liberalize the regime for the foreign currency owned by local natural persons with the only exception of free transfers abroad. The low limit of 50 US Dollars to be bought for travel was raised to about 500 US Dollars (10,000 Lv) a year.

However, the liberalization of the foreign exchange regime was carried out in the absence of two important factors, which had a negative effect on the exchange rate stabilization and the foreign exchange market balance:

- Absence of a stable modern legislative framework. The relevant Act in

force since 1966 is hopelessly outdated (in spite of the multitude of amendments). The new legislation - Ordinance No. 15 of the COM, and Regulations No. 2 of the BNB - was passed hurriedly which explains the omissions. The problem is further aggravated by the almost total absence of effective control and of procedures for imposing penalties for violations against the foreign exchange regime.

- The permanent acute deficit on the foreign exchange market in 1991 presupposed a constant speculative element in all participants on the market, banks included.

During the whole period under consideration these distinctive features stimulated inadequate actions of the participants, expressed by a drive towards instant profits through spreads reaching sometimes 30 per cent (6-7 Lv); maintenance of open dollar positions for prolonged periods against expensive loans in Levs; export of capital abroad.

Despite the change, by the middle of the year, in the actions of the banks participating in the market, and the shift of speculative element to the foreign exchange offices, the brokerage houses and some smaller provincial banks, the major problem of the absence of clear and explicit legislation still remains.

### Foreign Currency Reserves

The Bulgarian National Bank took active steps to form the foreign currency reserve in February 1991, with the receipt of the first tranche from the International Monetary Fund. It is typical of the Bank's foreign currency reserves that the major sources for their increase are the tranches from the IMF, and the loan in ECU from the European Economic Community.

The foreign currency reserves are distributed primarily among foreign banks due to the more favourable terms they offer of keeping the accounts.

The distribution by type of currency - mainly in US Dollars, is necessitated by the basic requirements of the domestic interbank market. In 1991, 240 mln US Dollars were sold, and 72 mln US Dollars bought as interventions of the Central Bank. The selection of other currencies - ECU, Deutsche Marks, British Pounds - is determined by the more favourable terms for short-term placement.

The foreign currency reserves were placed largely in the form of deposits in the country (in the beginning of the year), and abroad. But during the last few months of 1991 part of the foreign currency in securities was placed for the purpose of increasing the BNB liquidity under the conditions of unstable foreign exchange prices.

#### BNB FOREIGN EXCHANGE RESERVES IN 1991

(mln at the end of the period)

Indicators		III	VI	VII	VIII	IX	X	XI	XII
Foreign currency on current accounts	USD	157.5	129.3	78.0	61.9	121.6	37.2	27.0	79.0
	DEM	-	1.0	7.6	3.3	4.7	5.9	4.7	6.3
	GBP	-	0.1	0.1	0.1	0.2	0.3	8.0	0.6
	ECU	-	0.2	0.2	98.8	86.7	72.8	48.3	54.5
Deposits	USD	10.0	15.0	10.0	65.0	59.5	70.5	47.5	60.5
	DEM	-	9.0	9.0	19.0	9.0	-	-	-
	GBP	2.8	2.8	7.8	7.7	12.7	12.7	5.0	12.7
	ECU	-	-	-	50.0	50.0	50.0	50.0	50.0
Securities purchased (at face value)	ECU	-	-	-	-	5.0	20.0	25.0	20.0
	USD	-	-	-	-	-	49.0	5.0	-
	SDR	-	-	-	-	10.0	10.2	5.8	5.8

## **IV. Activities of the Bulgarian National Bank**

# 1. Annual Balance Sheet of the BNB

In January 1991, five BNB branches were opened in Sofia, Plovdiv, Bourgas, Varna, and Pleven, which began issuing operations at the end of March. As of 29 June 1991, pursuant to the newly-passed Law on the BNB, the manner of forming and reporting profit was radically changed. The BNB became the official depositor of the government cash funds, and as of 15 July 1991 accepted for servicing the accounts of the Ministry of Finance, and of the primary dispatchers of budgetary funds by the classification of this Ministry.

The assets, liabilities, and resultant accounts in foreign currency were converted into Levs at the exchange rate as of 31 December 1991, and the exchange differences were accounted as profit or loss of the BNB.

In 1991 precious metals were revaluated twice on the basis of the average price of gold for the period, as quoted in the BNB News Bulletin on the interbank exchange rates. As of 31 December 1991 precious metals were 8,494.1 mln Lv-worth, against 89.9 mln Lv by 31 December 1990.

Up to 31 June 1991, the BNB was taxed 80 per cent of the balance sheet profit. With the enforcement of the Law on the BNB, the terms and procedures of taxation were altered - the balance of the annual excess of the revenue over the expenditure of the Bank is paid in the state budget as revenue.

## DISTRIBUTION OF THE ANNUAL EXCESS OF THE REVENUE OVER THE EXPENDITURE OF THE BNB FOR 1991

(thousand Lv)

I. BNB revenue	15,528,647
II. BNB expenditure	6,618,571
III. Balance (I-II)	8,910,076
IV. Provisions	2,558,000
V. Amount to be distributed	6,352,076
1. 25 per cent to the Reserve Fund	1,558,019
2. 1 per cent to the R & D Fund	63,520
3. Insurance	6
4. Balance to be paid in the budget	4,700,531
VI. Amount paid in the budget by 31 Dec. 1991	5,232,470
VII. Amount overpaid in the budget by 31 Dec. 1991	531,939

The interest earnings for 1991, amounting to 11,191 mln Lv, exceed those in 1990 by 10,169 mln Lv. This increment is due to the floating basic interest rate on the loans in Levs for refinancing - from 4.5 per cent in the beginning to 54 per cent at the end of 1991.

The expenditure on interests paid on deposits of the State Savings Bank and other ministries run up to 5,776 mln Lv, and exceed those in 1990 by 5,435 mln Lv. As of September 1991, the BNB set a 15 per cent annual interest rate on the current accounts with the Bank. On the current accounts of the Ministry of Finance the BNB paid interests to the amount of 75 mln Lv, and on the current accounts of commercial banks - 197 mln Lv.

## Annual Balance Sheet of the Bulgarian National Bank

		mln Lv
<b>ASSETS</b>	1990	1991
Cash in Bulgarian coins	46	53
Cash in foreign currency	-	1
Interest in international institutions	1	862
Amount available in foreign securities	-	1,232
Deposits and loans extended to banks	21,270	33,847
Loans extended to the Government	11,279	9,795
Securities	845	833
Other assets	106	12,010
	<b>Total</b>	<b>58,633</b>
<b>LIABILITIES</b>		
Common stock	150	200
Reserves and other funds	2,382	13,544
Banknotes in circulation	7,666	13,612
Current and deposit accounts	21,488	29,875
Other liabilities	1,861	1,402
	<b>Total</b>	<b>58,633</b>

Pursuant to Art. 7 of the Law on the BNB the common stock increased from 150 mln Lv in 1990 to 200 mln Lv in 1991. Pursuant to Art. 8, the National Bank formed a Reserve Fund to the amount of 25 per cent of the annual excess of the revenue over the expenditure of the Bank, and R & D Fund to the amount of 1 per cent, pursuant to Art. 8, para. 2 of the Law, and a resolution of the BNB Board.

In 1991 the BNB extended to the Government, the Ministry of Finance respectively, loans to the amount of 4,299.5 mln Lv, out of which 1,470 mln Lv for the Social Security Department. The total commitment of the Government to the BNB by 31 December 1991 was 9,795 mln Lv against 11,279 mln Lv in 1990. This decrease is due to the partial repayment of the debt of the Ministry of Finance to the BNB through the sale of gold.

The interest of the Republic of Bulgaria in the European Bank for Reconstruction and Development, the International Monetary Fund, and the International Finance Corporation runs up to a total of 862 mln Lv, divided equally between the BNB and the Ministry of Finance, as follows:

	Levs
European Bank for Reconstruction and Development	100,166,028
BNB	50,083,014
MF	50,083,014
International Monetary Fund	729,701,547
BNB	364,850,773
MF	364,850,773
International Finance Corporation	31,497,134
BNB	15,748,567
MF	15,748,567

The BNB owned stock in commercial banks and other companies to the amount of 834 mln Lv. With the registration of the Bank Consolidation Company - PLC, the shares and the provisional certificates for the BNB stock in commercial banks at a face value of 748.936 mln Lv was transferred to the name of the holding company.

In 1990 the BNB paid in the state budget the balance of the annual excess of its revenue over the expenditure to the amount of 5,232,470,133 Lv.

The long-term tangible and intangible assets were evaluated at acquisition cost, with straight-line depreciation; the shares were evaluated at par; receivables in Levs were evaluated at par; and those in foreign currency - at the rate as of 31 December 1991; cash funds in Levs were evaluated at par, and in foreign currency - at the rate as of 31 December 1991; the BNB common stock was evaluated at par.

## 2. Bank Supervision

In the banking reform underway in Bulgaria a special significance is attached to the development of the regulation and supervision functions, characteristic of market-oriented banking systems. In the course of the debates on the Law on Banks and Credit Activity, the question arose of where the bank supervision should be - with the Central Bank, or separated as a distinct government institution. It was decided that it should remain with the Central Bank for a period of two to three years, during which a group will be working on the legislative and statutory framework for the establishment of a bank supervision government institution.

The delay in preparing the legal framework had an adverse effect on the development of the bank supervision functions (the Law on Banks and Credit

Activity was passed in March 1992). It prevented the BNB from sanctioning banks which violated the existing banking regulators, few as they were, and extended large loans to government-owned and private enterprises, running unjustified risks. With some banks the violations were drastic. An extreme case was the Yambol Commercial Bank whose credit expansion by far exceeded the credit ceilings, determined by the BNB. The danger arose of chain bankruptcies of commercial banks, whose activities were linked with the Yambol Bank. Through its intervention, the BNB did not allow the development of such a trend, guaranteed individuals' deposits and the claims of enterprises. A committee was formed of the Yambol Commercial Bank creditors.

Gross violations were allowed as a result of the unprofessional management of the Bobovdol Commercial Bank which also faced bankruptcy. The BNB took measures to overcome this situation.

## **Current Control**

The Bank Supervision Department of the BNB is suffering the lack of skilled staff. The staff is not prepared for the specific functions and methods of work under the new conditions of the banking system. For this reason in 1991 efforts were focused primarily on forming an adequate structure, recruiting the needed staff, and setting minimum standards for monitoring and regulating commercial banks operations. In conformity with the recommendations of the IMF and the World Bank, a systematic monitoring of the commercial banks' financial position began, through the indicators of liquidity, capital adequacy, quality of assets and liabilities, profitability, etc. For this purpose, on the basis of the monthly balance sheets a concise aggregated balance sheet is compiled, according to the degree of liquidity and claimability. Commercial banks are divided into three groups, depending on the amount of the common stock and the licence granted. The monitoring of the major indicators is done within the framework of the group, making a comparison with its average level. On a quarterly basis, the financial performance of commercial banks is monitored through their profit-and-loss accounts and the provisions against bad and doubtful loans. The strict observance of the norms and regulators is also followed, and in case of establishing a violation, meetings with the bank managements are held.

Alongside the direct monitoring of commercial banks operations, methodological instructions are worked out on issues related to the classification of assets, capital adequacy, liquidity, loan concentration, credit ceilings, etc. In cooperation with the IMF and the World Bank, tenders were held and well-known international consultant firms were engaged to render methodological and practical assistance to bank supervision in Bulgaria. Studies were carried out with a view to constructing a system of evaluating the creditworthiness of bank clients.

## **Licenses**

The requirements for receiving permits for banking operations have been revised several times. In 1991 eight permits for banking operations were granted, and a number of other applications were turned down. The activities on licensing new banks are connected with detailed inquiries, in compliance with the requirements of the IMF and the World Bank. Permits for performing foreign exchange operations in the country and abroad were granted to 14 banks, and 58 banks and 16 branches of the SSB were granted permits for the sale and purchase of foreign currency and for collecting deposits.

After the adoption of Regulation No. 2 of the BNB of 28 March 1991, 569 applications for permits for sale and purchase of foreign currency were submitted. A total of 388 licences were granted, including 818 foreign exchange offices. 49 companies and 54 foreign exchange offices were denied permits.

In 1991 three licences for brokerage operations were granted to companies.

## **Auditing**

In 1991 the annual reports of all commercial banks were checked and verified. Inspections on other occasions were conducted in 16 banks, and full financial audits - in the Yambol Commercial Bank, the Tran branch of the Pernik Commercial Bank, etc.



In connection with the restructuring of the banking system, a team of consultants from the World Bank, together with experts from the Bank Supervision Department, work on the problem of cleaning bank portfolios. The improvement of the procedures of on-site inspections, auditor's activities in banks, etc. is forthcoming.

### **3. Issue of Banknotes and Coins**

#### **Money Supply**

In 1991 the money supply growth accelerated even further, increasing over two times and reaching 107.1 billion Lv for the year. The currency in circulation also grew by more than 50 per cent (by over 4 bln Lv), (less the vault cash of commercial banks and the SSB), reaching about 11.9 bln Lv. It is a logical consequence of the economic processes taking place in the country. The higher inflation rates (an almost treble growth of the average monthly salaries, and a nearly six-fold rise of consumer prices) naturally require greater money supply. The instability of the market, the preserved trend of paying out most of the population's income and the corresponding structure of payments, with retail trade carried out almost entirely in cash, necessitate the maintenance of an adequate money supply. (In 1991 the state-owned and cooperative retail trade turnover at current prices was worth 34.2 bln Lv, against 20.8 bln Lv in 1990, which means a 64 per cent growth. If an allowance is made for the private commodity turnover, on which there is no accurate information, but by all indications it shows substantial recovery in 1991, then the needs for cash funds become even greater.)

An additional pressure for money supply growth was exerted by the express propensity of some companies - private, state-owned, and co-operative - to service their entire turnover in cash, under the pretext of accelerating settlements. However, in this way, income is concealed, taxes are evaded, commitments to banks and bona fide clients are not repaid, which induced the BNB and the Ministry of Finance to take a number of measures to bring settlements in order. On account of this, Regulation No. 3 of Payments were amended.

The vault cash of commercial banks also increased. Whereas by the end of 1990 commercial banks had at their disposal vault cash of 690 mln Lv in banknotes and coins, by the end of 1991 the vault cash was about 2 billion Lv, or nearly three times more.

At the same time, the relative share of the currency in circulation in the total money supply fell from 14.1 per cent by the end of 1990 to 11.1 per cent at the end of 1991.

#### **Denomination Composition**

In spite of the general economic decline in 1991, the BNB was forced to service the money circulation by more cash funds, looking at the same time for opportunities to make the necessary changes in the denomination composition of the issue. The relative share of the banknotes of 10 and more Levs grew from 76.8 per cent in 1989 to 79.4 per cent in 1990, and 85.9 per cent in 1991. By the end of 1990, 50-Levs banknotes accounted for 7.1 per cent of the total banknotes supply in the country. As of 1 November 1991, the BNB circulated 100-Levs banknotes. By the end of the year the 50-Levs and 100-Levs banknotes accounted for as much as 36.4 per cent, and by the end of the first quarter of 1992 they reached 38.1 per cent.

By the end of 1992 the average banknote in circulation was about 12 Levs. Nevertheless, the denomination composition of the banknotes in circulation is not the optimal one, and for this reason the work on the new issue of banknotes of higher par values (200, 500, and 1,000 Levs) is still in progress. Taking into consideration the international experience in projecting the denomination composition of the banknotes in circulation, the annual needs for banknotes, and the growth of the currency in circulation, it should be noted that at the present stage

the nominal money supply growth, deriving from inflation, has to be assumed by banknotes of higher denominations.

**AVAILABILITY OF PRECIOUS METALS  
IN THE BNB VAULT**

(in troy ounces)

Indicators	31 Dec. 1990	31 Dec.1991
BNB gold reserve	1,017,041	1,017,041
Current availability:		
a) Gold	79,903	108,884
b) Silver	181,156	596,018
c) Platinum	5,063	6,301

**Notes:**

1. The gold reserve is in bullion of the exchange standard.
2. The current availability consists of gold, silver, and platinum in a standard form (bullion, tape, or government issue coins).
3. One troy ounce is equal to 31.10348 grams.

By the end of 1991 an increase of the current availability of precious metals was noticed. It was due, on the one hand, to the preserved BNB monopoly to buy up the precious metals extracted in this country, and on the other hand - to the drop in the production consumption by producers, and to their getting rid of inventories for economic reasons.

Up to 1947 the BNB had its own gold reserve. After the nationalization of banks and the introduction of the government foreign exchange monopoly, the BNB gold reserve was governmentalized and a monopoly regime was instituted. The BNB was granted the power to only buy up, on a compulsory basis, the gold extracted by all producers in the country. The BNB was also the only institution which, on instruction by the Ministry of Finance, sold gold for productive purposes to domestic consumers. The sale and purchase of gold were at prices set by the Council of Ministers. By the money reform of 1 January 1962, the gold reserve kept with the BNB was revaluated according to the determined gold content of the Lev (for 1 Lev = 0.759548 grams of gold). When gold was purchased by the BNB vault, it was accounted for in the BNB balance sheet at a price of 1.32 Lv for 1 gram. When in subsequent years the price rose, the difference up to the purchasing price was paid by the state budget. Conversely, with the sale of gold, the BNB retained only the balance sheet price of 1.32 Lv for 1 gram, and the difference up to the selling price was paid in to the budget as revenue. In 1990 that difference came up to 22.21 Lv for one gram.

In 1991, in relation to the formation of a foreign exchange market and the introduction of a floating exchange rate of the Lev to the other currencies, by an agreement between the Ministry of Finance and the BNB, the BNB ownership of the gold reserve kept in its vaults was restored. The BNB bought up from the Ministry of Finance the gold in the Bank's safe-keeping, initially purchased with state budget funds, to the value of 5,720.1 mln Lv. The value of the gold was calculated on the basis of the BNB reference rate, accounted arithmetically for 30 working days preceding the date of concluding the agreement.

## 4. Internal Control

A new Internal Control Office directly subordinated to the Managing Board was established within the framework of the new organizational structure of the

bank approved in June 1991. The independent internal bank evaluation on accounting, financial and other bank operations carried out by this office is intended to render assistance to the governing body.

The main scope of activities and tasks of the Internal Control Office provided by the Law on the BNB are : to audit and check the activity of the bank and its branches; to develop the internal control procedures in the BNB by departments and offices. Implementing these tasks the office is to audit the Bank's books, vaults and safes; to check the Bank's assets and liabilities and to make an evaluation of the balance sheet and the budget of the Bank; to check the annual financial report and the periodical reports prepared by the Bank; to submit to the Managing Board the reports after auditing and to make recommendations for eliminating the errors detected; to organize and to manage the internal control of the BNB in compliance with the requirements provided by the Law on the BNB and other legislative acts. Guided by the principal requirement of non-interference with other departments' activities, the Internal Control Office aims to guarantee impartiality of the control carried out. Along with that it comments on draft documents before submitting them to the Managing Board and makes recommendations for eliminating the errors detected after auditing.

Internal Control Office launched its activity without any experience in this field characteristic for the market-oriented bank systems. In major European banks the internal control has been reduced to a form of observing the correct and efficient operation of the created already automated control system of all bank operations covering up all levels. Recently, a similar approach was unfeasible for us in the existing environment. At present the Office is working and amassing experience following the principle of checking each operation and each document the operation is reflected in.

New procedures for auditing the accounting, currency issue and other bank operations have been worked out with the assistance of the IMF experts. Work organization, personnel qualification and training, books' finalization, duly implementation of current accounting tasks, organization of the internal control of each department, accountancy state and implementation of Board's decisions are matters subject to control. A flexible program for control of each object was preliminary prepared and adopted. Overall auditing of the accounting and other operative departments is the main objective of the programme. Detail procedures have been elaborated for each concrete check up.

The Internal Control Office informs the Bank's Board or the respective head of department of each check up effected and makes recommendations for eliminating the errors detected.

Throughout 1992 further check ups will be effected under the programme elaborated. Computer control where a package of modern software products will be applied, including these for direct control of Information Technology Department is envisaged to be introduced.

The lack of such controlling system limits the possibilities for overall auditing of the main accounting, foreign exchange and financial operations of the Bank. Special personnel training is envisaged in order to meet all the requirements for effective internal control.

## **5. Relations with the International Financial Institutions**

With the admittance of Bulgaria to the IMF and the World Bank in September 1990, real preconditions emerged for the rapid normalization of the country's relations with the international financial community. The BNB was one of the major institutions taking part in the elaboration of the Government's stabilization and structural policies, which later received the financial support of the IMF and the World Bank. Besides, a strong impetus was given to the relations and contacts

of the BNB with other international financial organizations and central banks.

## **International Monetary Fund**

In March 1991 the Executive Board of the IMF approved the Bulgarian Government's Letter of Intent and agreed to give to the Republic of Bulgaria a stand-by credit to the amount of 279 SDR (about 400 mln U.S. dollars).<sup>1</sup> The funds were intended to normalize the country's balance of payments in accordance with the economic programme, as well as to increase the foreign exchange reserves managed by the Central Bank.

Pursuant to the provisions of the Stand-by Agreement, in addition to its five tranches Bulgaria received an emergency tranche to the amount of 56.9 mln SDR through what is known as emergency external financing. In this way the total amount of loans received from the IMF in 1991 and the beginning of 1992 comes up to 335.9 mln SDR (about 482 mln US Dollars). Their repayment will take place in the period 1994-1997. Besides, in February 1991 Bulgaria received an additional loan from the IMF to compensate for the increased costs (as compared to projected estimates) on the import of energy resources (oil and gas). Due to the reported actual overcompensation at the beginning of March 1992 Bulgaria retired this loan. The technical assistance rendered by the IMF Central Banking Department was also of great importance for the modernization of the BNB. With the active participation of IMF experts and consultants from various central banks, substantial progress was made in the following priority areas for the development of our Central Bank: banking legislation, monetary instruments, money market, forex operations and management of foreign currency reserves, monetary analysis, accounting and internal audit, bank supervision, information technologies, and system of payments.

## **World Bank**

In July 1991 the first loan agreement was concluded with the World Bank for a Technical Assistance Loan to the amount of 17 mln US Dollars, with a repayment period of 17 years, a 5-year grace period included. The loan is a component of a parallel co-financing for an overall technical assistance project at the value of 31.5 mln US Dollars. The remaining amount is gratuitously financed by the PHARE Programme - 13.2 mln USD, and by the British Know-How Fund - 1.21 mln USD. The project provides primarily technical assistance and some equipment intended for priority sectors and components of the structural reform. Within the framework of the Technical Assistance Loan, the banking sector is included with 1.4 mln USD for financing consultant services in four fields: studies of the banking system structural problems; development of effective bank supervision; consultant services on commercial banks management; development of a modern clearing and settlement system.

In August 1991, another loan agreement was concluded with the World Bank for a Structural Adjustment Loan (SAL) to the amount of 250 mln US Dollars in two tranches - the first one of 150 mln USD, and the second one of 100 mln USD. The repayment period is 17 years, a 4-year grace period included. The loan was made on the basis of the Letter of Development Policy, signed by the Government, and reflecting the major trends of the structural reform in the country and the conditions for the disbursement of the loan tranches. The funds from the first tranche, received relatively rapidly, were entirely used to import oil products, and to stabilize the energy balance of the country. But the delay in the structural reform, and the failure to meet some of the conditions, mainly in the field of privatization and the agricultural reform, caused a temporary delay of the second tranche disbursement.

In 1991 Bulgaria became a full member of the International Finance Corporation, and of the Multilateral Investment Guarantees Agency.

## **G-24**

Bulgaria is included in the G-24 programme for supporting the process of structural adjustment and transition to a market economy in the East European

<sup>1</sup> At the rate of 1 SDR = 1.434 US Dollars.

countries. In August 1991 a loan agreement was concluded with the European Economic Community for a 7-year two-tranche loan to the amount of 290 mln ECU. At the end of the same year the Government of the Republic of Bulgaria and the Commission of the European Community signed a financial memorandum for technical assistance to the financial sector, through the PHARE Programme. The funds on this project are gratuitously provided for a period of 3 years. Within the framework of the overall project for the financial sector, 4.5 mln ECU are appropriated to the banking system, out of which 1.21 mln ECU - to the BNB. The USA made available a 10 mln USD grant to support the development of private farming in Bulgaria, and at the beginning of 1992 a Bulgarian-American enterprise fund to the amount of 55 mln USD was set up to promote private small and medium-sized enterprises.

### **European Bank for Re- construction and Development**

An important element in our integration into the international financial community is Bulgaria's membership of the European Bank for Reconstruction and Development (EBRD). On 25 November 1991 the EBRD Board of Directors approved a Strategy for Bulgaria - a document which actually opens up opportunities for a start of the EBRD operations in the country. The following priorities were identified: privatization and restructuring of state-owned enterprises and banks, and support to individual private enterprises in key areas; modernization of the financial sector, incl. through the stimulation of the emergence and development of specialized institutions, such as leasing companies and export credit agencies; projects in the field of the infrastructure, particularly transport, telecommunications, and energy; investments in agriculture. The first loan with the participation of the EBRD to the total amount of 114 mln ECU was approved by the Board of Directors on 24 March 1992. The EBRD participates in it with 40 mln ECU, the co-financing includes also the European Investment Bank (45 mln ECU), and the National Electric Company (29 mln ECU). The loan is made for the technological renovation and expansion of the East Maritsa thermal power plant.

### **European Investment Bank**

The country maintains active relations with the European Investment Bank (EIB). In June a financial memorandum was signed affirming the willingness of the EIB to finance various projects in Bulgaria within the framework of a special common resource of 700 mln ECU for Bulgaria, Czecho-Slovakia, and Roumania.

### **International Bank for Economic Co-operation and International Investment Bank**

The range of the country's relations with the international financial community would not be well outlined, if no mention was made of the relatively long history of its membership of the financial institution of the former CMEA - the International Bank for Economic Co-operation (IBEC), and the International Investment Bank (IIB). The reforms in the member-countries of these two financial institutions have radically changed our financial relations with them. The main purpose of the IBEC was to provide financial services to the international trade within the CMEA through a multi-lateral clearing on the basis of the transferrable rouble. The position of the Bank has become precarious due to the total crash of this system of international trade. At the same time the IBEC Board, and the member-countries of the Bank respectively, are faced with the challenge of preserving the IBEC, thus facilitating and promoting trade between the member-countries. According to them, the future of the Bank lies in the commercialization of its operations, and in the increase in the number and quality of the services it offers. The IIB's operations are also made difficult by the crisis conditions of the member-countries' economic development. A common feature of these countries' economic policy is their drive to get out of the excessive mutual dependence, which was imposed in the CMEA without taking the world market development trends into consideration. The preparation of large joint investment projects is practically at a standstill, in all these countries there is a decline in the economic, and particularly in the investment activities, and the future does not hold serious promises for the development of joint projects. Of course, the nature

of some of the projects financed by the IIB so far, mainly in power-production, is on such a large scale, that their completion is expected after the year 2000.

## **6. Legal Regulation of the Economy**

The period under consideration, covering 1991 and the first months of 1992, was of paramount importance for the development of Bulgarian legislation. The radical changes in the statutory framework testify that this country is really parting from the centrally planned model of economic management and moves along the lines of the market economy.

### **New Constitution**

In this respect, the adoption of the new Constitution ranks first. The provisions of the fundamental law establish that the economy of the Republic of Bulgaria is based on the free economic enterprise. An express clause in the Constitution proclaims the inviolability of private property. Equal legal conditions for the business activities of all citizens and juridical persons are guaranteed, and their investments are protected. The possibility to establish a government monopoly, by law alone, is provided only for the area of rail transport, the national postal and telecommunications networks, the nuclear energy use, the manufacturing of radioactive products, weapons, explosives, and substances with strong biological effect.

The subjects of exclusive government ownership and sovereignty rights are exhaustively enumerated. Thus, the statutory and constitutional mainstay of the government banking monopoly have been finally eliminated.

### **Law on the BNB**

The passage of the Law on the Bulgarian National Bank and the Law on Banks and Credit Activity are of exceptional significance for the banking system. Both legislative acts are based on the modern trends and permits in the regulation of banking transactions, characteristic of the countries with developed market economy.

The Law on the BNB regulates the structure and activities of the Central Bank in a radically new manner. It draws an explicit distinction between the two major parts of banking - central banking, on the one hand, and commercial banking on the other. The Central Bank no longer services the national economy directly. That is done solely by the commercial banks. The BNB has the principal task of maintaining the internal and external stability of the Bulgarian national currency. It works out and pursues the national monetary and credit policy. The regulatory and controlling functions of the BNB are directed to the other banks with a view to maintaining the stability of the banking system.

The law regulates transactions and activities, characteristic of central banks of developed countries, but virtually unknown in this country until quite recently. Such as, for instance, the discounting of marketable securities by banks and other financial institutions, the open market transactions, the determination and regulation of minimum reserve requirements.

For the first time the new legislation gave a statutory regulation to the interrelations between the BNB and the Government. The Law expressly states that lending to the Government shall observe the stipulated restrictive conditions - a term no longer than three months, and no later than the end of the calendar year, with a maximum amount of the outstanding loans at any point not exceeding 5 per cent of the annual state budget revenue.

The functions assigned to the BNB require also a radical change in its legal status. From an agency subordinated to the Council of Ministers (pursuant to the repealed Statute of the BNB), the Central Bank now has turned into an institution answerable to the National Assembly. This concerns general principles and can not be conceived as a possibility for Parliament to interfere with the Bank's operational activities. In these activities the Bank is autonomous and independent not only of

the directions of the National Assembly, but of the Government and all government bodies as well. The autonomy and independence of the Central Bank are also guaranteed by the status of the officials sitting on its managing bodies. The Governor and the Deputy Governors of the BNB are elected by the National Assembly for a term of five years, and the other members of the Board are appointed by the President of the Republic for the same term. During their term of office they may be recalled only on grounds explicitly stated in the Law (sentence for a criminal offence, continuous inability to perform the functions assigned for more than a year). This virtual tenure during the term of office makes it possible for the BNB bodies of management to be truly independent in making and executing their decisions. Thus the Central Bank becomes a relatively autonomous and independent centre of the executive branch. It is a partner of the Government in pursuing the government economic policy, and in some cases, due to its autonomous status, it may even restrict government actions.

### **Law on Banks and Credit Activity**

For the first time in several decades, commercial banking has also received statutory regulation. Pursuant to the Law on Banks and Credit Activity (in force as of 31 March 1992) a bank is a juridical person, set up as a joint stock company or a co-operative, which has been granted the right to perform deposit, credit, and other banking transactions. The transactions to be regarded as banking transactions are exhaustively listed. Each person performing them shall be subjected to the regulations and control provided by the law. A permissive regime for performing banking transactions is established - a written licence from the Central Bank is required. The Law specifies the terms and procedures for granting a banking licence, including the opening of foreign banks' branches. The deadline for granting the licence is six months after the application has been submitted to the BNB. The permissive regime also covers foreign persons' interest in banking institutions, the BNB having to consider the application within three months.

In cases specified by the Law, the Central Bank may revoke, temporarily or permanently, the licence granted. In case of a revocation of the licence, a controller is appointed to supervise the bank's activities.

Certain actions may be taken only by the permission of the BNB, such as the acquisition of shares in local banks securing over 5 per cent of the total number of votes at the shareholders' meeting, banks acquiring over 10 per cent of the capital of a non-banking enterprise, opening bank branches abroad, transformation of banks, altering the name indicated on the licence, as well as performing banking transactions beyond the ones referred to in the licence.

The Law provides a number of conditions and restrictions to insure the safety of the valuables entrusted to banks, to reduce the risk, and to guarantee liquidity. These are the requirements for a minimum owners' equity and its ratio to the balance sheet assets and liabilities, for maintaining minimum liquid funds, provisions to cover bad and doubtful loans, and a certain difference between the assets and liabilities in foreign currency as a percentage of the owners' capital, determined by the Central Bank. Besides, there are restrictions on lending and investment, stipulating that the total value of the loans to one person shall not exceed 25 per cent of the bank's owners' capital, and that the total amount of the bank's investments in real estate, equipment, shares, stocks in non-banking enterprises shall not exceed the owners' capital.

The law also provides restrictions on making loans to shareholders or other persons related to the bank. Such loans may be made only by a decision of the collective body of management, and with the approval of the internal auditing body.

General legal regulations were introduced for the banking secret, as well as for the conditions under which the obligation to observe it may be waived. The deferment of bank commitments, and the annual accounts are also regulated.

The new legislation pays particular attention to the supervision of banking operations. It envisages mandatory submission of periodic accounts and reports to the Central Bank. Banks shall notify the Central Bank in writing of certain

circumstances (reshuffle in the management bodies, change in the capital, discontinuation of certain activities, unexpected overindebtedness or insolvency). The BNB bank supervision bodies monitor the operations of banks, conduct inspections and audits, take measures to remove malpractices. In case of failure to observe the statutory regulations and the requirements for liquidity and stability of banking operations, the Central Bank may take a broad range of actions, including: issuing mandatory instructions to remove the malpractices; sending its representatives to sit on the managerial bodies of the supervised bank; convening a shareholders' meeting and sittings of the managerial and auditing bodies; appointing persons empowered to give advice on how to get out of the difficult situation; restricting the bank's activities; establishing special supervision through persons authorized to manage and represent the supervised bank; removing from office persons with managerial and representative powers; revoking the licence granted.

## **Other Acts**

The legal framework formed by the two fundamental banking Acts functions within the context of the whole package of legislative acts passed by the Bulgarian Parliament during the period under consideration. Particular direct significance for the banking system attaches to the new Trade Act, specifically to its part on joint stock companies, the New Co-operative Act, the Business of Foreign Persons and Foreign Investment Protection Act. The latter also regulates foreign persons' investments in banking activities.

The National Assembly passed three important restitution acts, whose enforcement laid the beginning of the process of restoring ownership. Essential amendments were made to the Farmland Act, aiming at the formation of a true land market. In April 1992 Parliament passed the crucial Privatization Act. Tax laws are to be adopted. Work is in progress on the drawing up of a new Securities and Stock Exchanges Bill, on a new Foreign Exchange Act.

During the period under consideration the process stated of regulating banking activities through secondary legislation. The BNB Board exercised its statutory powers on several occasions and adopted important regulations, referring to the terms and procedures of granting permits for the sale and purchase of foreign currency, for interbank deposit auctions, for the issue, sale and buyback of short-term government securities, on payments, on refinancing banks against a collateral and through rediscounting marketable government securities.

## **7. Bank Staff Training**

By the end of 1991 the banking system employed a total of 19,114 people, out of whom 10,950 at commercial banks, 7,750 at the SSB, and 414 at the BNB. In comparison with the previous year, the bank staff number grew by 1,114 people. Out of a total of 11,364 at the BNB and commercial banks, 8,584 are women, and 2,780 are men. 3,708 are university graduates, 7,183 have a secondary or vocational education, and 473 have primary education. 2,724 are below 30 years of age, 7,060 are between 30 and 50 years of age, and 1,580 are over 50.

The success of the reform in the banking sector and the dynamic development of financial operations require the constant upgrading of the knowledge and skills of the staff in the various financial institutions. These were the motives for the establishment, in 1991, of a specialized unit at the BNB - the International Banking Institute. Its activity concerns primarily commercial banks, which later necessitated its transformation into an independent joint stock company. The principal objective of the Banking Institute is to enable bankers to achieve a degree of qualifications and expertise, meeting international standards and facilitating the formation and functioning of a modern banking system in Bulgaria.

The Banking Institute organizes courses of diverse duration and scope, where the staff acquires practical knowledge and skills in performing banking operations.



The instruction is based on non-traditional methods, the banking transaction techniques being combined with the clarification of the underlying theoretical concepts and the international practice. The activities of the Institute began with three courses, conducted by French lecturers, on the subjects: The Place of Commercial Banks in the Market Economy, Financial Analysis of Bank Loans, and Banking Accounting and Banking Control. Owing the keen interest displayed, the courses continued in January-February 1992. A two-module integrated seminar on commercial banking was organized, where the major topics for discussion were money and capital markets, capital structure of the bank, bank management, liquidity of banks, and banking investment analysis. The seminars, organized with the cooperation of the Karl Duisberg Society from Germany, on particular banking operations and bank management deserve special attention. The co-operation with this institution will go on in 1992 as well. Computer training and courses training foreign exchange cashiers are also being organized.

In the beginning of 1992, the co-operation with the British Know-How Fund started with a series of three seminars on the subject of financial analysis of investment projects in agriculture and in the processing industry.

During the short period since the establishment of the Banking Institute, 329 trainees have attended various training courses. In 1992 the practice will continue of inviting foreign lecturers, trying at the same time to more fully utilize the potential of Bulgarian lecturers and practitioners. Catalogues of the offered course subjects will be published, as well as hand-outs, reference materials, etc.

The training of Bulgarian staff is included in the European Community PHARE Programme for 1992, which will make it possible to organize a number of specialized seminars in priority areas of banking. The technical assistance from the USA will also be utilized.

## **8. Information Publications**

The process of moving towards a democratic society and a market economy has posed new challenges in all areas of the BNB activities. One of them is the opening of the banking system for a wide public control, i.e. providing transparency to making and executing decisions in the field of finance and lending. For that purpose the BNB Public Relations Service was established in March 1991, with the main task of offering up-to-date, accurate, and timely information to both business and financial institutions in the country and abroad, and to the mass media.

*The News Bulletin* of the BNB, issued twice a month since the middle of 1991, is the basis of the operational information circulated by the BNB for the time being, and the *semi-annual and the annual report* present a generalized picture of the monetary policy, the financial position, and the major macroeconomic indicators. Since November, the BNB has started publishing the *Bank Review*, a quarterly journal, featuring articles on purely banking and financial issues, as well as analyses and theoretical studies of other economic problems of importance for the country. For the purpose of providing assistance to the bank staff, regular publications are issued, containing up-to-date information on topical problems of the course of the banking reform. All publications are printed in Bulgarian and in English.

In the near future the publishing of a monthly and a quarterly statistical bulletin will begin, to be issued in Bulgarian and English, like almost all BNB publications.

For the sake of informing the public, regular press-conferences are organized, articles and interviews with the BNB Board members, heads of departments, and other experts are published in the press with regard to decisions made, forthcoming actions, missions of the international financial organizations, etc. It is often done through press releases to all interested institutions, foreign information agencies and embassies included.

## **V. Development of the Banking System**

# 1. Organizational Changes in the Banking System

In 1991 the organizational structure of the banking system continued its formation under the impact of two opposite trends. On the one hand, the liberalization of the economic relations, inevitable in the transition to a market regulation, provoked a drive on the part of many state-owned and private organizations to set up their own banks. During the year it was reinforced by the favourable environment which promised substantial profits for banks. On the other hand, the prevailing opinion (not only of Bulgarian, but of foreign experts as well) was that the structure formed after the last reorganization was too scattered and ineffective. First, because the number of banks is too high for the size of the country (70 by the beginning of the year), and, second, they are very small - more than half of them have ownership capital of up to 10 mln Lv (recalculated at the exchange rate to about 500 thousand US Dollars), with an average volume of the credit investments for the year of up to 250 mln Lv (12 mln US Dollars), which considerably restrict their possibilities to fully participate in the financing of large-scale projects.

## Licence Issuing Restrictions

That predetermines the policy of the BNB as a Central Bank in defining the permissive regime for opening new banks. The aim was not to hinder initiative, but at the same time not to allow the formation of many small banks, as there are enough of them already. With respect to banks with Bulgarian capital, this was expressed by the major requirement for a minimum initial ownership capital of 50 mln Lv, and for foreign banks - the equivalent of 20 mln US Dollars.

Trying to facilitate the emergence of private banks, the BNB Board was not particularly exacting in granting licences for banking activities.

During the first half of the year, the following new banks were established: the Central Co-operative Bank (Sofia), the Bulgarian Postal Bank (Sofia), the Credit Bank (Dragoman, later moved to Sofia), the Agrobusiness Bank (Plovdiv), the International Bank for Trade and Development (Sofia). A licence for limited banking operations was granted to the Sirbank (Sofia), servicing the major activities of the Bulstrad International Insurance Company.

The second half of the year saw the opening of the Touristsportbank (Sofia), and the first bank with mixed capital - The International Bank for Investments and Development (Sofia), with equal interests of Bulgarian and American capital, which will begin operations in 1992. A permit was granted to the Reiffeisen Centralbank (Vienna) to buy 21.3 per cent of the shares of the Bank for Agricultural Credit.

The absence of a clear concept of the optimum size and capacity of a commercial bank under the present conditions, and of a final decision on the question of the future banking structure, induced the BNB Board to suspend the issuing of new licences for banking activities. Exceptions are allowed only for opening new banks with substantial foreign capital interest, or with a capacity to play a key role in the restructuring of the economy.

## **Banks Consolidation**

At the same time, with the assistance of the World Bank, a possible mechanism was sought for the restructuring of the banking system. Upon the initiative of the BNB and the Bulgarian Foreign Trade Bank, the formation of the Bank Consolidation Company began, and its registration was promulgated on 14 February 1992.

The initial capital of this Company amounts to 933.206 mln Lv, including about 750 mln Lv from the transferred BNB interest in commercial banks, and 180 mln Lv from the Bulgarian Foreign Trade Bank. The share capital of all state-owned companies will also be transferred to the possession of this Company. It is expected for the Company to concentrate over 1.8 billion Lv of capital which accounts for about 80 per cent of the sum total of the shares sold within the banking system.

With the co-operation of the World Bank, the U.S. Treasury Department is rendering valuable consultant assistance through the resident adviser, Mr. Robert Perry.

A basic function of the Bank Consolidation Company is to prepare and effect a regrouping of the banks down to 8-10 large ones, on the basis of a thorough study, analysis and evaluation of the assets and liabilities of each bank. A bid invitation for official consultants on the banking restructuring was published in the Financial Times. Many of the well-known consultant companies in the world took part in the bid, and the British company DFC Limited won it.

The major guiding principles in the future restructuring of the banking system will be the combination of the voluntary basis in merging banks and the requirement for a maximum stability of the coming banking system, through an even and balanced distribution of the assets and liabilities of the system among the consolidated banks.

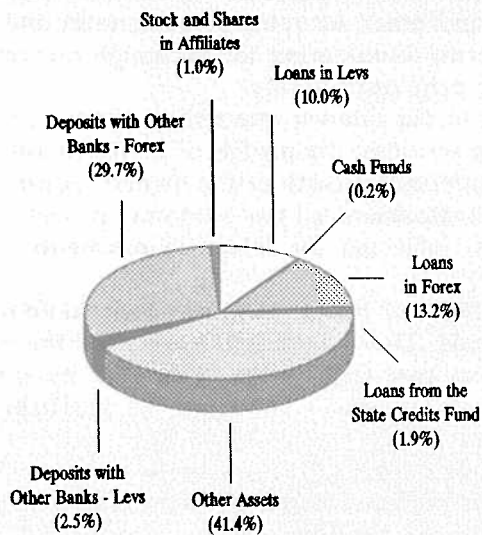
After the banking reform, carried out in 1991, the only purely state-owned bank which has not been transformed into a joint stock company is the State Savings Bank. For the time being, it is the only bank with a narrow specialization in lending to households, although it is getting more closely involved in the competition of lending to private and government-owned companies. In spite of the difficulties related to covering the negative interest rates on the old housing and consumer loans (specified by a specific Act), the SSB remains a stable bank popular with the public.

## **2. Balance Sheet Performance of Commercial Banks**

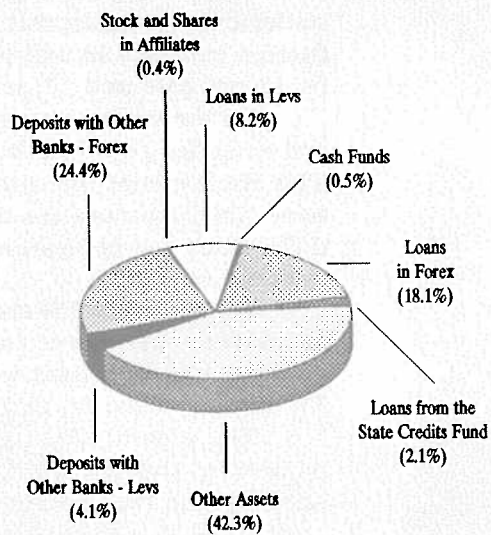
The analysis of the reported balance sheet data of commercial banks indicates some steady trends. In the assets operations of the banks, an anticipating increase is observed in the securities, the cash funds, and the tangible assets, the deposits and current accounts with other banks in Levs (increased 14.5, 2.2, 2.13, 1.80, and 1.51 times respectively). From among the more significant elements, the bank loans in Levs grow fastest - by 51 per cent, and thus their relative share went up from 13.23 per cent at the end of 1990 to 18.15 per cent at the end of 1991. The foreign exchange components grow in nominal terms, but recalculated at a single exchange rate, most of them show a drop - deposits, current accounts, and loans in foreign currency by about 10 per cent each, and the stock and shares in affiliates decrease more than two times in real terms. The only exception to this rule are Other Assets which incorporate the exchange rate differences from the foreign currency revaluations.

In the liabilities operations, an activation is observed of most of the more insignificant components - individuals' deposits (3.54 times, with elimination of the exchange rate impact on forex deposits), common stock, and the funds of banks (by 84 per cent), stock and shares in affiliates (by 53 per cent), etc. The dynamic

**STRUCTURE OF COMMERCIAL BANKS LIABILITIES**  
(Levs 20 per USD 1)

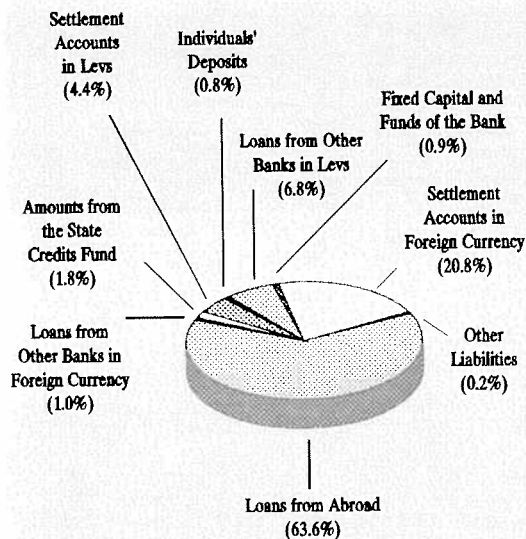


**31.XII.1990**

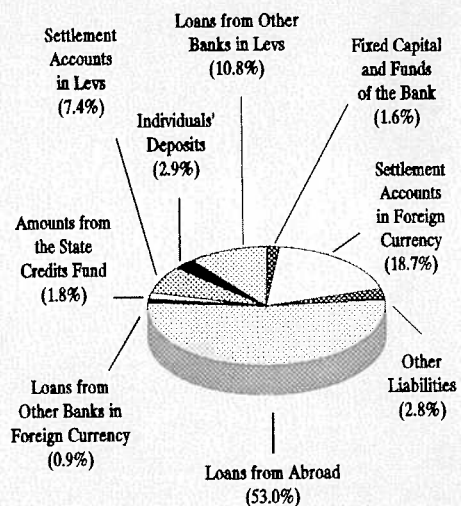


**31.XII.1991**

**STRUCTURE OF COMMERCIAL BANK ASSETS**  
(Levs 20 per USD 1)



**31.XII.1990**



**31.XII.1991**

group covers also the settlement, fund, deposit and other accounts of companies and organizations in Levs, and the loans received from other banks - increase of 63 per cent and 56 per cent respectively.

Despite their substantial nominal growth, the loans from abroad, and the settlement, fund, deposit and other accounts of companies and organizations in foreign currency in real terms (eliminating the exchange rate impact) are falling by 12 per cent and 18 per cent respectively.

On the whole, owing to the interest rate policy pursued, and to the diverse and extended paid banking services, the profits of banks increased substantially. This also explains the considerable growth of the owners' equity of banks. At the same time, the negative development of the economic processes created serious difficulties for companies, reflected by delays in payments of principals and interests on loans.

To strengthen the stability of banks, measures were taken to allot substantial amounts to the reserve funds. The criteria and norms for the provisions against doubtful and bad loans were specified by the BNB, and, by agreement with the Ministry of Finance, deductions were made from the profit before taxation.

The general conclusion is that as a result of the freeze on the foreign debt payments, and the subsequent foreign currency stagnation, the role of forex operations in the operations of banks is reduced to a considerable extent. At the same time, elements which were considered insignificant until quite recently are being felt ever more tangibly, such as the mutual assets deposit operations between banks, and the unemployed cash funds of companies and individuals kept with banks in liabilities operations. Moreover, there is an impressive growth of the owners' equity of banks which is an indication of their strengthening.

CONSOLIDATED BALANCE SHEET OF COMMERCIAL BANKS AS OF 31.XII.1991

<b>Assets</b>	<b>Sum total in mln Lv</b>
Cash funds	1896
Precious metals	2118
Stock and shares in affiliates	1544
Deposits and current accounts with other banks in Levs	12024
Deposits and current accounts with other banks in forex	95329
Investment and working capital loans in Levs	60077
Loans in forex	37994
Investment loans from the State Credits Fund	7955
Tangible assets of banks	328
Securities	5374
Balance on a settlement account with the BNB	1197
Other assets	179693
<b>Total</b>	<b>405529</b>

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**Liabilities**

Common stock and funds of the banks	13725
Individuals' deposits	12228
Settlement, fund, deposit, and other accounts of companies and organizations in Levs	25616
Loans received from other commercial banks	34152
Settlement, fund, deposit, and other accounts of companies and organizations in foreign currency	50257
Loans from abroad	250985
Loans in foreign currency received from other commercial banks	4241
Amounts from the State Credits Fund	7892
Stock and shares in affiliates	725
Other liabilities	5708
<b>Total</b>	<b>405529</b>

**Note:** The data above previously published by the BNB was calculated on the basis of the methods assuming certain discrepancies. Introducing new calculating methods the problem was overcome.

**VI. Major Trends of Monetary  
Policy and Banking Development  
in 1992**



In 1991 the legal and organizational framework was set for pursuing a monetary policy in the country.

Despite the difficult economic conditions, reflecting the macroeconomic imbalances at the start of the reform, as well as the external shocks, inflation was held in check. The restrictive monetary policy pursued had a decisive significance for obtaining this result.

## **Objectives of the Monetary Policy in 1992**

In 1992 the BNB will pursue a monetary and credit policy, making for the maintenance of the internal and external stability of the Lev, as the Law on the BNB mandates. The Central Bank will look for more regular consultations with the Government on economic policy issues.

The projections for 1992 envisage a continued decline in production, although to a much lesser extent as compared to 1991. At the same time, after the real income growth in the second half of 1991, the demands for its further increase continue in the beginning of 1992. The budget deficit as a percentage of the GDP is growing. There is a fall of the budget expenditure on subsidizing the fixed prices of some commodities. The range of goods with projected or fixed prices is being narrowed. All that comes to show that in 1992 there will be a mounting inflation pressure. The BNB will be guided, as it has been until now, by the understanding that the monetary policy is an important instrument for the stabilization of the economy at large. In our case, the monetary policy assumes particularly great significance due to the fact that we, unlike some other East European countries, do not have the crucial nominal "anchor" of prices - the fixed exchange rate.

### **Control over Inflation**

The main task of the monetary and credit policy for 1992 is the preservation, maintenance, and strengthening of the control over inflation, so that no reversal of the 1991 economic reform result is allowed. In pursuing the monetary policy, the BNB will bear in mind the aim, announced in the Letter of Intent, of gradually reducing the annual inflation rate by the end of 1992 to half the level reported in January 1992.

Taking into account the general condition of the economy during the last quarter of 1991, and the projections for 1992, we think that it is premature to assign the monetary and credit policy functions of stimulating real production growth and unemployment reduction. The 1991 experience has shown that the premature easing of the credit restrictions only feeds the inflationary pressure, destabilizes the economic situation, and in the long run subverts the medium-term growth prospects. At the same time, curbing inflation is regarded as the key factor of the economic environment which favours investment expansion, effective resource allocation, and stimulates growth in the long-term. Strengthening the control over inflation would support the stability of the economic situation, protect the interests of the groups with fixed nominal income, provide conditions for private businesses and state-owned enterprises to operate with greater certainty, and ultimately make for the social and political stability in the country. The BNB is determined to contribute to the achievement of price stability in the country as one of the most important objectives of the Government's economic

policy, at the same time being well aware that no matter how consistently the monetary policy is pursued, it would not be able in itself to ensure price stability, if the behaviour of the Government and the other economic agents is incompatible with such an objective. The monetary policy can not be successful without the support of the other economic policy branches, and particularly of fiscal policy. If public spending, household consumption, investments, and export together exceed the production potential of the economy, a crisis would arise sooner or later, forcing the adjustment of the aggregate demand to production capacities. This type of crisis is expressed in abrupt changes of both the general price level and the relative prices, in shrinkage of production and unemployment growth. The same consequences would follow from the probable trade union demands for an increase in the income of certain categories of employees regardless of the real economic growth.

### **Exchange Rate Stabilization**

Another important task of the BNB in 1992 will be the stabilization of the exchange rate. The general economic prospects and the insufficient foreign currency reserves of the country do not allow the exchange rate stability to be interpreted as a stability of the nominal exchange rate. The BNB will try to achieve a relatively constant real effective exchange rate. In 1992 the system of a floating exchange rate of the Lev to the convertible currencies will be preserved. The regulation of the exchange rate will be directed mainly to neutralizing the abrupt changes in the volume of supply and demand of foreign currency, and to maintaining the temporary fluctuations of the exchange rate within a narrow range.

The foreign exchange regime in the country is based on an outdated legislative act which is incompatible with the market economy - the Foreign Currency Valuables Transactions and the Foreign Exchange Control Act, and the forex control mechanism should be specified by a new Foreign Exchange Act.

## **Monetary Policy Instruments**

### **Credit Ceilings**

In 1992 credit ceilings again will be a major monetary policy instrument, set to commercial banks in accordance with the general economic objectives of credit expansion. This is necessitated by the still lingering inflationary situation, as well as by the insufficient development of the money and capital markets. The economic prospects for 1992 require strict control over credit. At the same time, the BNB envisages a modification of the manner of setting the individual credit ceilings for commercial banks. The purpose of the modification is to take into account the differentiation between banks in attracting deposits and client service. Thus one of the most serious disadvantages of credit ceilings as a monetary policy instrument will be moderated - the suppression of competition in the financial sector.

### **Indirect Instruments**

The BNB intends to gradually move on to a wider use of the indirect instruments of monetary policy. Their importance will grow in 1992. There will be a further introduction and consolidation of the instruments and mechanisms, inherent in the credit system of the market economy: open market operations, refinancing of commercial banks through discount and lombard operations, etc. This difficult and continuous process will be completed only with the permanent establishment of the market economy principles in the country.

The BNB will entirely withdraw from the direct covering of needs of the banking system for resources, and will refinance the economy only through the classical instruments of a Central Bank. The lombard and discount operations, restored in 1991, will be developed further, as well as the short-term deposit auctions which were initiated during the year under consideration and which laid the beginnings of the money market in this country. Government securities operations (open market operations) are also expected to start. A commercial

securities market is to be developed, as without it the liquidity of financial investment is heavily constrained.

## **Interest Rate Policy**

In 1992 the BNB interest rate policy will try to maintain a zero or low (1 to 3 per cent), but positive real interest rate, and a stability of the interest rates structure. In this respect, the BNB will be guided by the understanding that the positive interest rate is an important condition for the selection of profitable investments and for effective resource allocation in the economy. At the same time the BNB considers that the change in the basic interest rate has a substantial impact on the stability of the financial system, as well as on the decisions on expenses, investments, and savings in the economy as a whole. Bearing in mind the influence of the interest rate on inflationary expectations, the BNB will closely monitor the economic situation, and will make decisions on changing the basic interest rate only when there is a certainty of stable alterations in the aggregate demand trends, the dynamic pattern of prices and supply.

## **Financing the Structural Changes in the Economy**

In 1992 there will be a development, on a broad and widely accessible basis, of the operations of the State Fund for Reconstruction and Development, formed by resources from the Government's external lenders. This Fund will finance both profitable projects in the private sector, and investment projects in the area of the infrastructure. The Government is in a position to provide preferential financing for the promising economic sectors, provided those advantages do not affect the fair competition between entrepreneurs. It is particularly urgent to establish a system of stimulating exports and of government guarantees for foreign trade transactions.

## **Reform of the Banking Sector**

The reform found Bulgaria with a scattered, unstable, and ineffective banking system. At the same time, the transition to a market economy sets requirements first and foremost to the banking system, and poses serious challenges to it. The main objective of the banking sector reform is the consolidation of the existing commercial banks into several economically stable bank chains, which would be able to offer the needed services to the economy, and to withstand the competition of foreign banks, gradually appearing in Bulgaria. These are tasks to be accomplished by the newly-established Bank Consolidation Company. It will coordinate, in a non-administrative manner, the banking sector consolidation, and will prepare the ground for the privatization of banks.

The banking system needs a strict bank supervision, whose aims are to protect the interests of depositors and shareholders, and to ensure the observance of the norms and regulators of banking operations. The strengthening of bank supervision should be based on the Law on Banks and Credit Activity, in force as of March 1992.

## **Institutional and Technical Infrastructure of the Monetary Sector of the Economy**

Bulgaria does not have at its disposal modern technical facilities for effecting payments and interbank communications. For this reason, the payment process is slow and engages substantial money resources of economic agents. The payment

forms and practices, imposed by the centrally planned economy, are still in effect. In 1992 it is envisaged to institute a new regulation of the payment system, introducing documents, procedures, and forms of payment, applied in the developed European countries. To make it possible, large-scale technological projects will be prepared, and substantial resources will be invested in the payment system of the country.

In 1992 the system of national accounts will be introduced also in the banking sector.

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**GROSS DOMESTIC PRODUCT**

(million levs - at current prices)

Indicators	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
GDP - Produced	25791	27818	29013	29815	31671	32595	34424	36531	38345	39579	45390	138400
Industry and Construction	13869	14448	16802	17894	18988	20382	22035	22454	23379	23507	23273	69208
Agriculture and Forestry	3719	4625	4984	4317	5008	3869	4447	4309	4394	4331	8055	17876
Services	8204	8745	7228	7514	7675	8344	7942	9768	10572	11742	14062	51316
GDP - Used	26274	28818	29835	30472	32097	33283	36551	37393	39360	41103	47385	122531
Final Consumption	17506	18946	19933	20666	21581	22788	24201	25372	26162	27999	33585	104802
Gross Accumulation	8768	9872	9902	9807	10516	10495	12350	12020	13197	13105	13800	17729
Capital Investment	7289	7690	7973	7975	8112	8613	9291	9817	10260	10328	9652	13870
Changes in Inventories	1479	2182	1929	1832	2404	1882	3059	2203	2937	2776	4148	3859
Foreign Trade Balance, Losses and												
Statistical Discrepancy	-483	-1000	-822	-658	-426	-687	-2128	-861	-1015	-1524	-1995	15869
Foreign Trade Balance	-197	-1166	-779	-1024	-1057	-1596	-2311	-1855	-637	-97	-	-
Others	-286	166	-43	366	631	909	183	994	-377	-1427	-	-

**GROSS DOMESTIC PRODUCT**

(million levs - at constant prices)\*

Indicators	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
GDP - Produced	27027	28351	29013	30008	31028	31860	33201	35211	36131	35453	39579	39800
Industry and Construction	14569	15366	16802	18085	19194	20172	21219	22359	22904	22828	23507	20559
Agriculture and Forestry	4509	4711	4984	4170	4657	3697	4512	3851	3785	3696	4331	4170
Services	7949	8275	7228	7754	7177	7992	7470	9000	9443	8929	11742	14534
GDP - Used	26347	27978	29835	29773	30298	29947	31432	35840	32299	28539	41103	33952
Final Consumption	18271	19221	19933	20492	21480	21791	22520	23523	24050	24461	27999	20376
Gross Accumulation	8076	8757	9902	9281	8819	8156	8911	12316	8879	4078	13105	9812
Capital Investment	6302	6366	7973	7358	6271	6099	5703	10018	5758	1681	10328	8415
Changes in Inventories	1775	2391	1929	1923	2548	2057	3209	2298	3121	2397	2776	1397
Foreign Trade Balance, Losses and												
Statistical Discrepancy	680	373	-822	235	729	1913	1769	-629	3202	6914	-1524	5848
Foreign Trade Balance	-1069	-1733	-779	-1062	-1022	-1388	-2163	-2193	-1926	-911	-97	-
Others	1748	2106	-43	1297	1752	3301	3932	1564	5128	7824	-1427	-

\* The data for the period 1980-1989 are calculated at 1982 prices, the data for the period 1989-1991 at 1989 prices, and those for 1991 - at 1990 prices.

(million levs)

## GROSS CAPITAL INVESTMENT

92

Indicators	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Industry	3145	3378	3732	3626	3782	4224	4714	5097	5335	5499	5034	6070
Agriculture and Forestry	895	632	627	639	654	708	620	699	875	873	964	696
Construction	117	210	227	268	261	326	337	347	371	505	443	2946
Services	3131	3471	3387	3442	3415	3354	3690	3900	3707	3550	3352	4158
Transport	699	860	779	755	735	738	655	1009	763	618	792	526
Trade	219	232	269	280	248	284	308	231	282	445	376	743
Other Services	2214	2378	2340	2407	2432	2333	2727	2660	2662	2487	2184	2889
Total	7289	7690	7973	7975	8112	8613	9361	10043	10288	10427	9793	13870

(million levs - at current prices)

## CHANGES IN INVENTORIES

Indicators	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Industry	404	936	1001	-49	1215	631	1289	1168	1239	1501	3275	3631
Agriculture and Forestry	210	387	405	220	263	-62	185	-152	21	-6	524	3120
Construction	88	52	38	-4	80	52	43	46	63	92	-31	-1014
Services	770	810	482	1664	845	1258	1541	1141	1615	1189	380	-1381
Transport	20	22	25	18	13	35	40	11	40	36	110	500
Trade	459	414	242	640	-363	335	173	149	606	629	37	-2114
Other Services	291	374	215	1007	1195	888	1328	981	969	524	233	233
Total	1472	2184	1926	1832	2403	1879	3058	2203	2938	2776	4148	2975



(million levs - at current prices)

## INVENTORIES AS OF THE END OF THE YEAR

Indicators	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Industry	6615	7383	8754	8678	11032	11186	12870	13740	15213	16701	19458	21999
Agriculture and Forestry	4555	4220	5367	5593	6498	6417	6657	6591	6600	6585	7470	9558
Construction	819	872	921	942	1041	1078	1121	1165	1241	1349	1850	835
Services	6230	6862	7108	7798	7629	7946	8004	8118	8759	9376	9681	9674
Transport	316	334	383	382	397	436	457	459	503	557	738	1242
Trade	5562	6174	6331	6979	6662	6963	7019	7118	7759	8370	8391	6095
Other Services	353	355	394	437	569	548	528	540	497	450	553	2337
Population	58	61	79	86	96	91	102	99	102	128	212	212
Total	18219	19337	22150	23011	26200	26627	28653	29615	31813	34011	38458	42067

## EMPLOYMENT BY BRANCHES

(in thousands)

Indicators	1970	1980	1985	1986	1987	1988	1989	1990	1991
Industry	1304	1600	1736	1748	1775	1766	1714	1529	1207
Agriculture and Forestry	1484	1057	926	915	885	861	814	672	575
Construction	349	357	375	375	374	370	361	312	211
Services	1014	1350	1422	1436	1453	1471	1475	1310	1195
Transport	216	258	255	258	258	257	247	231	246
Trade	254	352	373	375	381	387	395	311	237
Other Services	544	741	795	803	814	827	833	768	712
Public Utilities	86	93	97	98	99	101	97	58	58
Science	47	66	81	82	84	89	97	88	66
Education	177	246	268	272	272	276	277	276	271
Art, Culture	30	45	48	48	47	46	46	44	36
Public Health	113	187	203	203	209	213	215	215	205
Finance, Credit, Insurance	16	20	22	22	23	25	26	25	25
Management	62	66	59	59	63	61	61	51	45
Others	14	18	18	19	18	16	16	12	6
Total	4151	4364	4460	4473	4487	4468	4365	3824	3188

## INDUSTRIAL COMPOSITION OF EMPLOYMENT

(per cent)

Indicators	1970	1980	1985	1986	1987	1988	1989	1990	1991
Industry	31.4	36.7	38.9	39.1	39.6	39.5	39.3	40.0	37.9
Agriculture and Forestry	35.8	24.2	20.8	20.4	19.7	19.3	18.7	17.6	18.0
Construction	8.4	8.2	8.4	8.4	8.3	8.3	8.3	8.2	6.6
Services	24.4	30.9	31.9	32.1	32.4	32.9	33.8	34.3	37.5
Transport	5.2	5.9	5.7	5.8	5.7	5.8	5.7	6.0	7.7
Trade	6.1	8.1	8.4	8.4	8.5	8.7	9.1	8.1	7.4
Other Services	13.1	17.0	17.8	18.0	18.1	18.5	19.1	20.1	22.3
Public Utilities	2.1	2.1	2.2	2.2	2.2	2.3	2.2	1.5	1.8
Science	1.1	1.5	1.8	1.8	1.9	2.0	2.2	2.3	2.1
Education	4.3	5.6	6.0	6.1	6.1	6.2	6.3	7.2	8.5
Art, Culture	0.7	1.0	1.1	1.1	1.0	1.0	1.0	1.2	1.1
Public Health	2.7	4.3	4.5	4.5	4.7	4.8	4.9	5.6	6.4
Finance, Credit, Insurance	0.4	0.5	0.5	0.5	0.5	0.6	0.6	0.7	0.8
Management	1.5	1.5	1.3	1.3	1.4	1.4	1.4	1.3	1.4
Others	0.3	0.4	0.4	0.4	0.4	0.4	0.4	0.3	0.2
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

**WHOLESALE PRICE INDEX OF THE INDUSTRIAL BRANCHES**

(1980 = 100)

Indicators	1985	1986	1987	1988	1989	1990
Overall	115.2	116.2	116.9	119.9	123.3	141.5
Electric and Thermal Generation	103.4	104.8	105.3	112.3	113.6	115.8
Coal-Mining	102.6	102.2	102.4	102.5	100.8	100.8
Oil and Gas	100.0	100.0	99.8	99.9	99.8	112.4
Iron and Steel Industry	104.3	105.0	104.6	108.2	108.9	127.0
Non-Ferrous Metallurgy	125.4	124.5	124.2	146.7	146.7	169.3
Machine-Building and Metal Working	112.4	114.5	115.2	117.2	122.0	130.8
Electrical and Electronic Industry	107.4	108.7	109.7	111.1	113.3	117.8
Chemical and Rubber Industry	113.6	114.3	115.3	122.3	122.2	138.5
Construction Materials	113.5	114.2	114.9	115.5	129.0	167.3
Wood and Woodprocessing Industry	112.5	115.6	118.6	123.2	134.5	144.7
Cellulose and Paper	105.8	105.6	105.2	112.7	116.3	137.6
Glass, China and Faience	105.6	106.0	105.3	123.8	131.0	152.9
Textile and Knitted Goods	122.9	123.6	124.0	126.4	129.0	157.8
Sewing Industry	139.9	146.7	154.6	158.1	160.9	176.5
Leather, Furriery, Shoe Industry	106.8	107.6	109.6	113.4	128.4	139.4
Printing and Publishing Industry	121.9	126.1	126.3	136.8	155.1	174.5
Food Industry	124.4	124.0	123.7	129.6	134.2	172.0
Other Industries	102.9	107.3	111.2	112.7	113.0	143.3

CONSUMER PRICE INDEX IN 1991

(December 1990 = 100)

Commodity (Service) Groups	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Foodstuff	108.7	316.9	440.8	420.9	418.4	422.2	445.8	517.1	535.3	548.8	574.4	602.6
Liquor Products	105.7	131.3	198.0	209.9	212.4	220.0	220.4	215.1	219.1	215.6	221.5	226.6
Tobacco Products	105.5	190.0	251.9	254.2	260.3	255.6	253.3	262.9	262.0	267.6	272.9	277.5
Clothing and Footwear	113.8	155.2	215.1	231.2	232.1	247.7	254.6	264.8	275.7	294.2	323.0	341.0
Housing, Heating, Electricity	103.9	221.4	557.9	646.0	671.8	778.6	936.7	958.2	1011.9	1018.2	1048.3	1047.7
Home Furniture	117.6	189.2	286.6	310.1	311.7	348.2	419.9	422.4	452.2	476.9	485.6	518.7
Social and Cultural Life	121.7	230.1	293.4	309.5	297.8	317.2	330.8	359.9	374.7	396.5	405.9	440.4
Hygiene and Public Health	162.1	238.6	343.3	352.9	375.8	384.8	429.8	434.1	450.9	482.2	510.4	556.4
Postal and Transportation Services	128.9	363.4	510.6	505.5	516.6	584.3	689.5	681.2	705.8	716.2	752.1	748.1
Taxes and Fees	112.2	156.6	207.2	227.5	221.4	237.6	245.2	256.2	261.9	271.6	288.2	330.0
Others	116.6	216.6	346.3	367.4	382.1	418.4	465.3	472.7	493.4	514.8	544.9	567.2
Consumer Price Index	113.6	253.2	381.1	390.6	393.7	416.9	451.9	485.8	504.3	520.9	546.9	573.7

CONSUMER PRICE INDEX IN 1991

(previous month = 100)

Commodity (Service) Groups	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Foodstuff	108.7	291.5	139.1	95.5	99.4	100.9	105.6	116.0	103.5	102.5	104.7	104.9
Liquor Products	105.7	124.2	150.8	106.0	101.2	103.6	100.2	97.6	101.9	98.4	102.7	102.3
Tobacco Products	105.5	180.1	132.6	100.9	102.4	98.2	99.1	103.8	99.6	102.2	102.0	101.7
Clothing and Footwear	113.8	136.4	138.6	107.5	100.4	106.7	102.8	104.0	104.1	106.7	109.8	105.6
Housing, Heating, Electricity	103.9	213.1	252.0	115.8	104.0	115.9	120.3	102.3	105.6	100.6	103.0	100.0
Home Furniture	117.6	160.9	151.5	108.2	100.5	111.7	120.6	100.6	107.1	105.5	101.8	106.8
Social and Cultural Life	121.7	189.1	127.5	105.5	96.2	106.5	104.3	108.8	104.1	105.8	102.4	108.5
Hygiene and Public Health	162.1	147.2	143.9	102.8	106.5	102.4	111.7	101.0	103.9	106.9	105.9	109.0
Postal and Transportation Services	128.9	281.9	140.5	99.0	102.2	113.1	118.0	98.8	103.6	101.5	105.0	99.5
Taxes and Fees	112.2	139.6	132.3	109.8	97.3	107.3	103.2	104.5	102.2	103.7	106.1	114.5
Others	116.6	185.8	159.9	106.1	104.0	109.5	111.2	101.6	104.4	104.4	105.8	104.1
Consumer Price Index	113.6	222.9	150.5	102.5	100.8	105.9	108.4	107.5	103.8	103.3	105.0	104.9

(million US \$)

Indicators	1980	1985	1986	1987	1988	1989	1990	1991
<b>Exports - Total</b>	1641	1133	981	1079	1110	1301	1161	791
Food, Raw Materials	139	189	143	211	223	233	227	186
	8.5%	16.7%	14.6%	19.6%	20.1%	17.9%	19.5%	23.5%
Foodstuffs	138	72	88	103	107	115	132	98
	8.4%	6.3%	9.0%	9.5%	9.6%	8.8%	11.4%	12.4%
Fuel, Minerals, Metals	1017	665	503	474	397	575	428	163
	62.0%	58.7%	51.3%	43.9%	35.8%	44.2%	36.9%	20.7%
Industrial Consumer Goods	106	101	124	142	145	139	141	158
	6.5%	8.9%	12.6%	13.1%	13.1%	10.7%	12.2%	20.0%
Chemical Products, Fertilizers	98	63	50	70	119	96	85	64
	6.0%	5.6%	5.1%	6.5%	10.7%	7.4%	7.4%	8.1%
Capital Goods	115	32	57	60	98	126	116	97
	7.0%	2.8%	5.8%	5.6%	8.9%	9.7%	10.0%	12.2%
Other	28	12	16	20	20	18	31	23
	1.7%	1.0%	1.6%	1.8%	1.8%	1.4%	2.6%	2.9%
<b>Imports - Total</b>	1663	2077	2344	2479	2582	2597	1932	861
Food, Raw Materials	297	406	391	341	465	541	208	150
	17.9%	19.6%	16.7%	13.8%	18.0%	20.8%	10.7%	17.5%
Foodstuffs	52	28	41	50	89	101	94	18
	3.2%	1.4%	1.8%	2.0%	3.4%	3.9%	4.9%	2.1%
Fuel, Minerals, Metals	487	429	440	486	452	389	340	214
	29.3%	20.6%	18.8%	19.6%	17.5%	15.0%	17.6%	24.8%
Industrial Consumer Goods	65	103	131	171	203	200	168	64
	3.9%	4.9%	5.6%	6.9%	7.9%	7.7%	8.7%	7.5%
Chemical Products, Fertilizers	279	342	333	413	427	356	250	103
	16.8%	16.5%	14.2%	16.6%	16.5%	13.7%	12.9%	11.9%
Capital Goods	445	669	905	910	853	938	820	296
	26.8%	32.2%	38.6%	36.7%	33.0%	36.1%	42.5%	34.4%
Other	36	100	103	108	92	71	52	15
	2.2%	4.8%	4.4%	4.4%	3.6%	2.7%	2.7%	1.8%

TRADE WITH DEVELOPING COUNTRIES

(million US \$)

Indicators	1980	1985	1986	1987	1988	1989	1990	1991
Exports - Total	1586	2072	1584	1841	1881	1278	1373	594
Food, Raw Materials	160	133	75	71	133	153	130	57
	10.1%	6.4%	4.7%	3.9%	7.1%	12.0%	9.5%	9.6%
Foodstuffs	190	135	107	144	164	117	65	29
	12.0%	6.5%	6.8%	7.8%	8.7%	9.2%	4.7%	4.9%
Fuel, Minerals, Metals	283	284	200	225	244	233	146	101
	17.9%	13.7%	12.6%	12.2%	12.9%	18.2%	10.7%	17.0%
Industrial Consumer Goods	75	61	65	77	94	57	48	37
	4.7%	2.9%	4.1%	4.2%	5.0%	4.5%	3.5%	6.3%
Chemical Products, Fertilizers	120	235	155	135	180	179	205	115
	7.6%	11.3%	9.8%	7.3%	9.6%	14.0%	14.9%	19.3%
Capital Goods	624	908	875	1119	988	484	689	236
	39.3%	43.8%	55.3%	60.8%	52.6%	37.9%	50.2%	39.7%
Other	134	317	107	70	78	55	89	19
	8.5%	15.3%	6.8%	3.8%	4.1%	4.3%	6.5%	3.2%
Imports - Total	532	1236	1304	914	1524	1376	1154	429
Food, Raw Materials	121	278	253	293	371	305	233	107
	22.8%	22.5%	19.4%	32.0%	24.3%	22.2%	20.2%	25.1%
Foodstuffs	17	7	20	18	13	30	18	3
	3.3%	0.5%	1.5%	2.0%	0.9%	2.2%	1.5%	0.6%
Fuel, Minerals, Metals	264	828	896	400	901	878	684	281
	49.6%	67.0%	68.7%	43.8%	59.1%	63.8%	59.3%	65.5%
Industrial Consumer Goods	41	32	32	69	80	75	108	20
	7.7%	2.6%	2.4%	7.6%	5.3%	5.4%	9.4%	4.7%
Chemical Products, Fertilizers	47	46	48	69	94	51	47	7
	8.8%							
Capital Goods	33	42	51	60	60	33	54	10
	6.1%							
Other	9	4	4	5	5	5	10	0
	1.8%	0.3%	0.3%	0.5%	0.3%	0.3%	0.9%	0.0%

TRADE WITH CMEA COUNTRIES

(million tr. rbl.)

Indicators	1980	1985	1986	1987	1988	1989	1990	1991
Exports - Total	4718	8022	8405	8668	9171	8844	6591	100.0%
Food, Raw Materials	246	234	238	241	220	172	112	
	5.2%	2.9%	2.8%	2.8%	2.4%	1.9%	1.7%	2.5%
Foodstuffs	1008	1295	1212	1124	1125	1074	863	
	21.4%	16.1%	14.4%	13.0%	12.3%	12.1%	13.1%	19.5%
Fuel, Minerals, Metals	168	307	312	288	367	282	277	
	3.6%	3.8%	3.7%	3.3%	4.0%	3.2%	4.2%	4.6%
Industrial Consumer Goods	486	896	965	978	1032	1039	718	
	10.3%	11.2%	11.5%	11.3%	11.3%	11.8%	10.9%	27.9%
Chemical Products, Fertilizers	138	184	193	187	188	185	138	
	2.9%	2.3%	2.3%	2.2%	2.0%	2.1%	2.1%	9.5%
Capital Goods	2550	4902	5261	5642	6013	5856	4312	
	54.1%	61.1%	62.6%	65.1%	65.6%	66.2%	65.4%	35.2%
Other	121	205	224	208	226	236	169	
	2.6%	2.6%	2.7%	2.4%	2.5%	2.7%	2.6%	0.8%
Imports - Total	4925	8191	8562	8555	8082	7267	6070	100.0%
Food, Raw Materials	255	406	383	405	372	362	235	
	5.2%	5.0%	4.5%	4.7%	4.6%	5.0%	3.9%	2.2%
Foodstuffs	40	64	42	51	57	47	44	
	0.8%	0.8%	0.5%	0.6%	0.7%	0.6%	0.7%	7.0%
Fuel, Minerals, Metals	2237	4080	4052	3794	3062	2635	2048	
	45.4%	49.8%	47.3%	44.3%	37.9%	36.3%	33.7%	77.7%
Industrial Consumer Goods	214	299	328	345	365	336	342	
	4.3%	3.7%	3.8%	4.0%	4.5%	4.6%	5.6%	2.5%
Chemical Products, Fertilizers	189	207	222	220	247	228	178	
	3.8%	2.5%	2.6%	2.6%	3.1%	3.1%	2.9%	1.8%
Capital Goods	1940	3031	3438	3646	3873	3570	3137	
	39.4%	37.0%	40.1%	42.6%	47.9%	49.1%	51.7%	8.3%
Other	50	104	98	94	107	89	86	
	1.0%	1.3%	1.1%	1.1%	1.3%	1.2%	1.4%	0.5%

## BALANCE OF PAYMENTS IN CONVERTIBLE CURRENCY

(million US \$)

Indicators	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Current Balance	907	562	813	292	727	-85	-715	-773	-840	-1306	-860	-906
Trade Balance	806	286	473	66	288	-387	-832	-955	-972	-1199	-757	-44
Exports (FOB)	3338	3360	3103	2719	3299	3307	2656	3277	3539	3138	2615	3737
Imports (FOB)	2532	3074	2630	2653	3011	3694	3488	4232	4511	4337	3372	3781
Services (Net)	437	434	431	209	387	261	184	346	417	385	185	-86
Transport	221	217	197	121	106	44	36	81	120	108	51	-14
Tourism	154	118	156	141	134	130	110	179	207	169	78	-84
Other	62	99	78	-53	147	87	38	86	90	108	56	12
Interest Payments (Net)	-394	-240	-186	-87	-22	-29	-128	-250	-363	-555	-396	-826
Private Transfers (Net)	58	82	95	104	74	70	61	86	78	63	108	50
Capital Balance	-756	-580	-385	-395	-332	-90	228	440	1882	596	-135	-1119
Credits Received (Net)	-280	-505	-384	-216	-7	495	664	553	2139	712	-414	-1339
Credits Granted (Net)	-129	-66	-36	-38	-327	-305	-436	-442	-445	-167	299	295
Short-Term Debt	-347	-9	35	-141	2	-280	0	329	188	51	-20	-131
Foreign Investment												56
Errors and Omissions	84	-343	302	315	22	473	-398	-164	-385	276	127	-67
Overall Balance	235	-361	126	212	417	298	-885	-497	657	-434	-868	-2092

## BALANCE OF PAYMENTS IN NON-CONVERTIBLE CURRENCY

(million tr. rbl.)

Indicators	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Current Balance	46	-668	-692	-285	-222	-61	-320	64	696	933	-872	596
Trade Balance	-158	-631	-836	-528	-541	-140	-475	-70	582	879	-897	593
Exports (FOB)	4706	4983	5246	6843	7405	8338	8393	8692	9135	8892	6282	1259
Imports (FOB)	4864	5614	6082	7371	7946	8478	8868	8762	8553	8013	7179	666
Services (Net)	222	177	165	282	355	156	193	186	179	94	7	-8
Transport	-46	-96	-104	-82	-83	-114	-106	-114	-145	-143	-113	-27
Tourism	145	190	229	262	259	275	290	304	323	369	92	-10
Other	123	83	40	102	179	-5	9	-4	1	-139	28	29
Interest Payments (Net)	-18	-22	-29	-45	-44	-81	-46	-79	-105	-65	-12	7
Private Transfers (Net)	0	8	8	6	8	4	8	27	40	25	30	5
Capital Balance	-113	196	360	53	109	-88	248	43	-619	-874	-57	408
Credits Received (Net)	-112	-46	-125	-102	335	17	531	-205	-293	-327	-306	0
Credits Granted (Net)	-1	-9	-22	-7	-6	-22	-33	-17	-12	-110	-34	133
Short-Term Debt	0	251	507	162	-220	-83	-250	265	-314	-437	283	275
Foreign Investment												
Errors and Omissions	68	274	339	233	115	150	73	-105	-77	-60	929	188
Overall Balance	1	2	7	1	2	1	1	2	0	-1	0	1193



## GROSS DEBT

Years	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
Million US \$	4865.4	4080.9	3500.1	3068.5	2922.9	4119.7	5511.6	7404.0	9125.7	9201.0	10007.0	11375.0

## CREDIT INDEBTEDNESS OF THE ECONOMY (million levs)

Indicators	December 1990	June 1991	December 1991
Current Exchange Rate	2.84	17.554	21.811
Domestic Credit (Net)	67444	120409	165795
- in levs	57157	60962	83417
- in convertible currency	10287	59447	82388
Claims on General Government (Net)	13657	32425	51725
- in levs	9821	8556	14963
- in convertible currency	3836	23869	36762
State Budget (Net)	10241	28260	48967
- in levs	6405	4391	12205
- in convertible currency	3836	23869	36762
Extrabudgetary Accounts (in Levs)	3416	4165	2758
Claims on Non-Government Sector	53787	87984	114070
- in levs	47336	52406	68454
- in convertible currency	6451	35578	45626
Claims on Non-financial Public Enterprises	46540	81542	105030
- in levs	40089	45964	59414
- in convertible currency	6451	35578	45626
Claims on Private Sector (Levs)	7247	6442	9040

## AVERAGE INTEREST RATES ON CREDITS<sup>1</sup> AND DEPOSITS IN 1991

Indicators	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Average Monthly Basic Interest Rate	0.63	3.21	3.75	3.75	3.75	4.16	4.04	4.12	4.5	4.5	4.5	4.5
Average Monthly Margin above the Basic Interest Rate on New Credits	0.125	0.35	0.37	0.38	0.38	0.385	0.425	0.43	0.46	0.64	0.68	0.85
Average Annual Interest Rate on New Credits	9.05	42.77	49.44	49.56	49.56	54.52	53.55	54.64	59.52	61.68	62.16	64.20
Average Annual Interest Rate on Credits <sup>2</sup>	8.84	41.44	48.03	48.13	48.17	53.18	52.13	53.26	58.07	59.67	60.12	61.46
Average Annual Interest Rate on Deposits	1.00	31.98	34.80	35.54	36.51	38.06	41.56	42.60	45.89	47.88	48.35	48.96
- demand deposits <sup>3</sup>	1.00	30.00	32.00	32.00	32.00	32.00	34.67	34.00	34.67	38.00	38.00	38.00
- time deposits	-	39.00	42.00	43.80	43.88	44.12	48.45	49.48	53.82	54.12	54.26	57.73

Note: <sup>1</sup> The data indicated are based on the predominant interest rates applied to credits for industrial needs.

<sup>2</sup> Pursuant to the Law on Settlement of the Outstanding Credits, interest rates by 1 percentage point above the basic interest rate have been fixed for the outstanding credits for industrial needs.

<sup>3</sup> Current accounts of the companies excluded. Until 30 September 1991 no interest was charged on them and after that date a 15% annual interest rate has been applied.

**MONEY SUPPLY**

(million levs)

Indicators	1991												
	1990	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
Exchange Rate: levs/US \$ 1	2.84	2.88	20.735	15.165	18.499	18.247	17.554	18.692	17.637	18.952	20.528	18.73	21.811
M <sub>1</sub>	26606	27117	49646	41935	46361	47228	45904	51053	50248	53073	59745	58146	64954
Currency Outside Banks	7110	7283	7467	7334	7031	7172	8051	8233	9055	9301	9871	10389	11866
Demand deposits	19496	19834	42179	34601	39330	40056	37853	42820	41193	43772	49874	47757	53088
- levs	13990	14266	11433	10648	10533	11328	10164	10355	11222	12747	12492	12283	15024
- convertible currency	4678	4763	29999	23287	28168	28228	27316	32216	29733	30770	37129	35210	37874
- non-convertible currency	828	805	747	666	629	500	373	249	238	255	253	264	190
Quasi Money	22396	22071	24020	25250	26033	26659	28006	29513	30689	31889	34315	36005	43068
Time Deposits	4221	4287	6144	9274	10307	11850	13745	15768	17286	18551	20841	22632	25867
Savings Deposits	17916	17554	16216	14767	13868	13434	13024	12534	12277	12066	12024	12046	15945
Foreign Currency Deposits	259	230	1660	1209	1858	1375	1237	1211	1126	1272	1450	1327	1256
M <sub>2</sub>	49002	49188	73666	67185	72394	73887	73910	80566	80937	84962	94060	94151	108022
Restricted Deposits	646	681	3489	2323	2202	2073	1906	2573	2353	3312	3543	3598	3586
- convertible currency	541	576	3385	2219	2194	2065	1899	2566	2346	3305	3536	3592	3583
- non-convertible currency	105	105	104	104	8	8	7	7	7	7	7	6	3
Broad Money	49648	49869	77155	69508	74596	75960	75816	83139	83290	88274	97603	97749	111608
- levs	43237	43390	41260	42023	41739	43784	44984	46890	49840	52665	55228	57350	68702
- convertible currency	5478	5569	35044	26715	32220	31668	30452	35993	33205	35347	42115	40129	42713
- non-convertible currency	933	910	851	770	637	508	380	256	245	262	260	270	193

EXCHANGE RATE IN 1991

Indicators	1991												
	XII'90	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
<b>Average Monthly Exchange</b>													
Rate (levs per US \$ 1)	-	-	23.61	15.90	17.31	18.46	18.07	18.97	18.71	18.28	19.40	20.78	21.99
<b>Exchange Rate at the End</b>													
of the Month (levs per a													
currency unit)													
USD	2.84	2.88	20.74	15.17	18.50	18.25	17.55	18.69	17.64	18.95	20.53	18.73	21.81
DEM	-	-	13.61	8.85	10.43	10.66	9.78	10.72	10.17	11.25	12.20	11.60	14.37
CHF	-	-	15.80	10.40	12.41	12.51	11.33	12.28	11.64	12.92	13.93	13.13	16.15

DENOMINATION COMPOSITION  
IN NOTES AND COINS

(levs)

Indicators	31.12.1989	31.12.1990	30.06.1991	31.12.1991
Notes - Total	6909381629.00	8758495545.00	9620918962.00	15099969194.00
in 100 levs				340000000.00
in 50 levs		618999900.00	1307999400.00	2096864400.00
in 20 levs	2621660632.00	3393558442.00	3551769142.00	4018021222.00
in 10 levs	2681566077.00	2938978197.00	2971958547.00	3460076322.00
in 5 levs	1211541029.00	1386351309.00	1386037794.00	1686028279.00
in 2 levs	244718596.00	262369255.00	251106359.00	290031154.00
in 1 lev	149895295.00	158238442.00	152047720.00	148947817.00
Coins - Total	222578619.64	228734595.17	231617985.22	238024182.72
in 50 levs	15000000.00	15000000.00	15000000.00	15000000.00
in 20 levs	5999980.00	5999980.00	5999980.00	5999980.00
in 1 lev	6040099.00	6461099.00	7490099.00	13136099.00
in 50 stotinki	30629132.00	30828497.50	30828497.50	30828497.50
in 20 stotinki	37198937.80	37614739.80	38041939.80	38041939.80
in 10 stotinki	26836102.70	27545187.90	28140188.10	28900388.10
in 5 stotinki	11432248.80	11928132.25	12559522.10	12559519.60
in 2 stotinki	10590869.04	10971508.44	10971508.44	10971508.44
in 1 stotinka	8306872.30	8864072.28	9010872.28	8984872.28
Jubilee	70544378.00	73521378.00	73575378.00	73601378.00

INCOME AND EXPENDITURES  
OF THE BNB IN 1991

(thousand leva)

Expenditures		Incomes	
I. Financial Expenditures	6 590 219	1. Income from Interest Payments Received	13 749 181
1. Interest Rates:	6 364 729	Interests:	13 389 073
on the accounts of the Ministry of Finance	75 314	on short-term and long-term credits extended to the Ministry of Finance	4 870 399
on deposits	5 775 224	on bank deposits	5 943 050
on foreign exchange operations	302 492	on capitalized interests of the Economic Bank	2 558 000
on current accounts	206 265	on minimum overdue non-interests reserve	17 624
on the State Fund for Reconstruction and Development	5 434	Interests Received from Foreign Exchange Transactions	360 108
2. Commissions and Fees	39 881	2. Adjustments from Foreign Exchange Transactions	1 778 444
levs	139		
foreign currency	39 742		
3. Foreign Exchange Adjustments	12 769	3. Commissions and Fees	122
		levs	53
		foreign currency	69
4. Currency Circulation Costs:	163 829	4. Other Financial Receivables	900
Banknotes Production Costs	161 777		
Banknotes Delivery Costs	1 929		
Banknotes Mint Costs	-		
Other Material Costs	46		
Costs on Legal Tender Designing	77		
5. Other Financial Expenditures	9 011		
II. Administrative Expenditures	28 352		
Salaries and Related Costs	11 960		
Social Security Payroll Deductions	3 738		
Expenditures on Civil Contracts	201		
Other Social Security Deductions	4		
Stationery	4 863		
Trips	2 992		
Bank Periodicals	1		
Clothing	460		
Equipment and Inventory Repair	604		
Payment Transaction Costs	962		
Other Costs	1 545		
Depreciation Costs	1 022		
Expenditures - Total	6 618 571	Income - Total	15 528 647
Income Surplus over the Expenditures	8 910 076		

## **Resolutions of the Board of the BNB in 1991**

- 4 February** Since 7 February 1991 the BNB has determined a 45% annual basic interest rate which will be applied on lev credits extended by the BNB for refinancing of commercial banks. The interest rate charged on credits extended to the state budget will be by 1 percentage point lower than the basic one.
- 5 February** The Board of the BNB issued a license for conducting banking activity to the International Bank for Trade and Development with registered office in the city of Sofia.
- 6 February** The Board of the BNB issued a license for conducting banking activity to the Agro-Business Bank with registered office in the town of Plovdiv.
- 7 February** To stimulate the increase of commercial banks' own capital and to limit the amount of capital investments, a 5% quota-level was determined pursuant to Article 6, para. 2, item 1 of the Regulations for banks' minimum admissible relative share in which credits should be covered by banks' own funds. The Regulations are effective since 30 June 1991.
- 11 February** Commission on Foreign Exchange Rate and Foreign Currency Purchase and Sale was established with the following staff: Emil Hursev, Ph.D, - Executive Manager, Deputy Governor of the BNB, Stoyan Shukerov - Head of Foreign Exchange Operations Department, Lyubomir Filipov - Head of Lev Operations Department. The terms of references of the Commission are as follows: a) to determine at the beginning of each working day the exchange rate of the lev on the basis of the preliminary set principals by the BNB; b) to determine the tangible opened items; c) to give a permission for a provisional daily deviation from the open positions fixed primely; d) to take decisions on current portfolio allocation of the open market operations within the framework of the targets and limits determined by the BNB.
- 18 February** The BNB licensed the following banks to conduct foreign exchange operations in the country and abroad: Bulgarian Foreign Trade Bank, Economic Bank, Mineralbank (Bank for Economic Enterprise), Balkanbank, Stroybank, Biochim Commercial Bank, Electronica Commercial Bank, Agro-Co-operative Bank of Plovdiv, Transport Bank of Varna, Bank for Agricultural Credit, First Private Bank.  
The BNB granted a permit for conducting foreign exchange operations in the country to the following banks: Commercial Bank of Sofia, Sredets Commercial Bank, Doverie Commercial Bank, Vuzrazhdane Commercial Bank, Vitoshka Commercial Bank, Hemus Commercial Bank, Iskar Commercial Bank, Kremikovtzi Commercial Bank, Commercial Bank of Assenovgrad, Commercial Bank of Blagoevgrad, Commercial Bank of Bobovdol, Commercial Bank of Botevgrad, Commercial Bank of Bourgas, Commercial Bank of Varna, Commercial Bank of

Veliko Turnovo, Commercial Bank of Vidin, Commercial Bank of Vratsa, Commercial Bank of Gabrovo, Commercial Bank of Gorna Oryahovitsa, Commercial Bank of Gotse Delchev, Commercial Bank of Devin, Commercial Bank "Trakia", Commercial Bank of Elin Pelin, Commercial Bank of Elhovo, Commercial Bank of Kazanluk, Commercial Bank of Karlovo, Kristalbank Commercial Bank, Commercial Bank of Kurdzhali, Commercial Bank of Kyustendil, Commercial Bank of Lovech, Commercial Bank of Lyaskovets, Commercial Bank of Mezdra, Commercial Bank of Mihailovgrad, Commercial Bank of Nova Zagora, Commercial Bank of Pazardzhik, Commercial Bank of Pernik, Commercial Bank of Petrich, Commercial Bank of Peshtera, Commercial Bank of Pleven, Commercial Bank of Plovdiv, Commercial Bank of Popovo, Commercial Bank of Provadia, Commercial Bank of Purvomai, Commercial Bank of Razgrad, Commercial Bank of Rouse, Commercial Bank of Samokov, Commercial Bank of Silistra, Commercial Bank of Sliven, Commercial Bank of Smolyan, Commercial Bank of Stanke Dimitrov, Commercial Bank of Stara Zagora, Commercial Bank of Toulbuhin, Commercial Bank of Troyan, Commercial Bank of Turgovishte, Commercial Bank of Haskovo, Commercial Bank of Chepelare, Commercial Bank of Cherven Bryag, Commercial Bank of Shoumen, Commercial Bank of Yambol. Foreign exchange purchases should be effected using commercial banks' own resources, the amount of which is fixed by their Boards, but it should not exceed 10% of them.

- 18 February** From 19 February 1991 the basic exchange rate of the BNB and the market exchange rate of the Bulgarian Foreign Trade Bank endorsed by Decree No. 32 of the Council of Ministers of 1990 were revoked, as well as the exchange rate of the BNB fixed by Statement No.13 of the Session of the Council of Ministers of 31 March 1991. For accounting and statistical purposes, customs evaluation and money transfers the central exchange rate of the BNB will be applied. The rates at which foreign exchange purchases and sales are effected will be determined by commercial banks. The central exchange rate of foreign currencies against lev will be determined by the BNB daily.
- 25 February** The Board of the BNB issued a license for conducting banking activity to the Central Co-operative Bank with registered office in the city of Sofia.
- 5 March** The Board of the BNB issued a license for conducting banking activity to the Sirbank with registered office in the city of Sofia.
- 13 March** Installment of automated teller machines is allowed after it has been co-ordinated with the BNB.
- 14 March** Banks not observing the Regulations for minimum non-interest reserves requirements (if banks do not transfer reserves to the non-interest account of the BNB duly or in full amount) will be levied 5 percentage points over the basic interest rate. This sanction will be used for amounts not transferred from the sixth of the current month to the date they are transferred, effective from end-March 1991.
- 21 March** Authorized capital in the amount of 50 million Levs was determined for newly established banks, as the half of it should be deposited with the BNB before the legal registration of the respective commercial bank. The authorized capital of the newly established foreign banks should amount to 20 million US \$ which is to be deposited with the BNB before the legal registration of the bank.
- 28 March** Ordinance No.2 of the BNB on Issuing Licence for Purchase and Sale of Foreign Currency was adopted.
- 5 April** The Board of the BNB issued a license for conducting banking activity to Saedinie Commercial Bank with registered office in the city of Sofia.

- 15 April** The Board of the BNB issued a license for conducting banking activity to the Credit Bank with registered office in the town of Dragoman.
- 23 April** From 1 May 1991 on the BNB bounds the commercial banks to calculate and report on the interest rate applied to credits and deposits in its effective amount. For this reason: a) in the cases of annual capitalization of the interest due, the effective monthly interest rate ( $r$ ) at nominal interest rate ( $R$ ) should be calculated according to the formula:  $r = \sqrt[12]{1+R} - 1$ ; b) at nominal monthly interest rate agreed ( $r$ ), the effective interest rate is to be calculated according to the formula:  $R = (1+r)^{12}$ .
- 9 May** Establishment of the interbank body for the automatization of the banking system and participation of the banks in the national settlement system was approved.
- 9 May** In compliance with the agreements for restructuring of the banking system of Bulgaria concluded between the Republic of Bulgaria, the International Monetary Fund and the World Bank, the BNB stopped issuing licences for conducting banking activity, except for the following cases: if the establishment of the bank leads to new direct investments in convertible currency, but not less than the equivalent of 20 million US \$; if the establishment of the bank solves problems of crucial importance for the structural adjustment of the economy (this may be determined by the Council of Ministers only and the paid registered capital should be at least 50 million Levs, deposited with the BNB according to the requirements of the BNB). Licences issued by the BNB for establishment of new banks are valid in case if the terms mentioned above have been met. A list of documents required for issuing a licence was approved (foreign exchange operations excluded).
- 30 May** The BNB shall pay 50% of Bulgaria's participation in the International Monetary Fund and 50% of its participation in the European Bank for Reconstruction and Development.
- 4 June** As of 10 June 1991 the basic interest rate on lev credits for refinancing of commercial banks by the BNB was determined at 52% per annum.
- 21 June** The BNB shall buy up 50% of the joint stock capital of the Mint, a state ownership managed by the Ministry of Finance, establishing a limited liability company in co-operation with the Ministry of Finance as a Government representative.
- 5 July** As of 10th July, 1991 a basic interest rate of 47% per annum has been set for refinancing commercial banks by the BNB.
- 5 July** In the third quarter of 1991 banks can extend credits above the fixed ceilings for the same period to enterprises for buying up agricultural produce.
- 5 July** According to the schedule, but not later than 30 September 1991, all banks and their branches should join the national automated clearing system. Banks which do not comply with this shall be sanctioned as per Art. 44 of the Law on Bulgarian National Bank, including closing down of branches, temporary withdrawal of the commercial bank licence till its actual joining the national automated clearing system.
- 5 July** An approval has been given to grant the "Social Insurance" Chief Department an interim credit of 450 million Levs for paying pensions for July, 1991 with redemption term of 3 months. The Ministry of Finance is the guarantor of the credit.
- 19 July** Pursuant to the Provisions of Article No.4 of the Law on the Bulgarian National Bank an interim credit, value date 22 July 1991, amounting to the reserve

available, but not exceeding 800,000,000 Levs, with a 3-month term of redemption and an interim credit, value date 26 July 1991, amounting to the reserve available, but not exceeding the balance of the credit approved on 22 July and 1,000,000,000, with a 3-month term of redemption, have been extended to the Ministry of Finance.

- 19 July** The Board of the BNB confirmed the terms and conditions of the loan extended to the Republic of Bulgaria by the European Community, as follows: nominal amount - 150,000,000 ECU; term of the loan - 7 years; payment date - some 3 weeks after the date of extending the loan; interest rate - floating, determined at six month period at present between 9.25 and 9.30%.
- 24 July** A credit ceiling, amounting to 112% of the adjusted debt as of 31 December 1990 was imposed for the highest permitted increase of the total debt on credits in levs extended by the commercial banks as of 30 September 1990.
- 24 July** The interest rate the Bulgarian National Bank is to pay on deposits with itself, shall be as follows: a) 1-month deposits - 2 percentage points below the basic interest rate for the period concerned; b) 3-month deposits - 1 percentage points below the basic interest rate for the period concerned; c) 6-month and longer time deposits - on contractual basis.  
The amount of a deposit placed with the BNB shall not be less 1,000,000 Levs. Where the depositor do not comply with the term provided, the interest rate on such deposits shall be equal to 1/4 of the interest rate valid for the moment of breaking the term.
- 25 July** The Board of the BNB issued a license for conducting banking activity to the International Bank for Investments and Development with registered office in the city of Sofia.
- 25 July** Where the banks are to be established the interest rate on the deposits placed with the BNB shall be, as follows: in levs - 2 percentage points below the interest rate for the period concerned; and in foreign exchange - on contractual basis between the depositor and the Foreign Exchange Department at the market rate less 1%. Interest on such deposits shall accrue until the date when the bank is registered in court.
- 12 August** A basic interest rate on credits in Levs for refinancing commercial banks by the BNB equivalent to 54% per annum and effective as of 21 August 1991 was set.
- 13 August** Pursuant to Art.46 of the Law on the BNB and in line with a schedule approved by the Ministry of Finance and the BNB, by the end of 1991 the BNB will extend short-term credits with a maximum total amount of 800 million Levs to the Ministry of Finance.
- 13 August** The BNB will administer Bulgaria's clearing agreement with the USSR and by end-1991 may credit the surplus accrued by Bulgarian exporters in the clearing account reflecting Bulgaria's trade with the USSR within a limit of 1.5 bln Lv. By the end of the year the outstanding balance should be transformed into a public debt and should be guaranteed with government stocks issued by the Ministry of Finance.
- 13 August** The BNB will restrict its extension of direct non-collateralised deposits to commercial banks and will promote as a major form of refinancing lending against collateral (i.e. lombard credits), e.g. loans received against government stocks issued by the Ministry of Finance, foreign currencies, commercial bills, etc. given as security.
- 15 August** New credit ceilings equivalent to a growth of 125% calculated as at 30 September



1991, in relation to their respective level as registered at the end of 1990 have been approved. Within these new ceilings accrued but not yet paid interests on credits, as well as on loans granted for purchasing farm produce, should be taken into account. Future refinancing of commercial banks should expand based both on the introduction of auctions for the extension of deposits and on the extension of deposits and loans on security.

- 15 August** Pursuant to Art.46 of the Law on the BNB and in line with Letter No.17-0023 of 15 August 1991 of the Ministry of Finance, the BNB extends a short-term credit amounting to 300 million Levs to the Ministry of Finance.
- 26 August** From 1 September 1991 the BNB shall pay interest of 15% per annum on the commercial banks current accounts held with the central bank. The interest that the banks will pay on the current accounts of the enterprises is negotiable.
- 26 August** The activities of the Interbanking Committee for Standardization of the National Non-Cash Settlement System are being extend. The Committee was entrusted to as an advisory body on the unification of the banking operations and the standards of the Bulgarian banking system. The Interbanking Committee changed its name to Committee on Unification and Banking Standards.
- 26 August** Ordinance No.4 of the BNB for holding interbank deposit auctions in levs was adopted.
- 12 September** New credit ceilings were approved allowing an increase of 132% by September 1991 compared to the end of 1990. When setting the credit ceilings the provisions of para. 2.3 of Protocol No.46 of 15 August 1991 shall be observed by taking into account the accumulated outstanding interest amounts on credits as well as the credits granted for purchasing agricultural production.
- 16 September** Pursuant to Art.46 of the Law on the BNB a short-term credit in the amount of 400 million Levs will be extended to the Ministry of Finance with value date 16 September and redeemable within 3-month period.
- 19 September** From 1 November 1991 the BNB will put into circulation a banknote of 100 Levs.
- 26 September** An additional credit ceilings shall be extended to commercial banks to credit payments for the executed construction works at the Kozlodui nuclear power plant and the Chaira hydro-electric power station, the BNB guaranteeing refinancing through discount of bills issued by the respective investors to the benefit of commercial banks.
- 30 September** As a consequence of the unchanging surplus on Bulgaria's clearing account with the USSR (as of 1 October Bulgaria financed the USSR by more than 220 million clearing Dollars), the exchange rate of the clearing Dollar against the lev will continue to be managed with disagio (reduced) to values which are to lead to balancing of our settlements with the USSR through activating Bulgarian imports. Together with it, this clearing will be serviced by the BNB without any limits.
- 3 October** The Board of the BNB issued a license for conducting banking activity to the Touristsport Bank with registered office in the city of Sofia.
- 24 October** The BNB will participate as a founder in the Bank Consolidation Company. In this respect the stock hold by the BNB with commercial banks will be transferred to the Bank Consolidation Company.
- 6 November** In compliance with the last edition of the Letter of Intent to the IMF, the credit ceilings of the commercial banks were extended, which enables the credits given

by the commercial banks to the national economy to show an increase of 152% compared to those at the end of 1990. At the same time, taking into consideration the status of the economy and particularly the pressure exerted on the lev at the market, as well as the increased liquidity of the commercial banks, the Board of the BNB adopted a Temporary Tariff for the Interest Rates Charged by the BNB and Applied to its Domestic Operations.

The interests on the funds extended by the BNB are differentiated in accordance with the type and the period of the credits or deposits extended. The basic interest rate will be charged when the commercial banks borrow using securities, bills of exchange, gold, silver and other precious metals, as well as precious stones and articles of precious metals as collateral. A discount rate corresponding to the basic interest rate will be applied for refinancing of the bills of exchange. The deposits offered to commercial banks within the 10% credit ceiling will bear a margin over the basic interest rate. This margin for 1-month deposits is 1% for prime rate borrowers and 3% for all other banks. The margin for 3-month deposits is 2% and 5% respectively.

The interest rates on the deposits with the BNB are considerably increasing. They vary according to the period for which the funds are deposited starting with 18% for 2-day deposits up to 48.5% for 1-year deposits.

The interest rate charged for the overdraft on the current accounts of the commercial banks with the BNB increased to form a rate consisting of the basic interest rate plus 8% for the first 3 days and 18% for the next days.

- 8 November** The BNB will extend to the Ministry of Finance a credit in the amount of 1,343 million Levs, which is the difference between the budget deficit that could be covered by the BNB (4,250 million Levs) and the already withdrawn credit by the Ministry of Finance for budget needs (2,907 million Levs) for this year. The credit will be extended in November 1991 in two tranches.
- 11 November** Temporary Tariff for the Interest Rates Charged by the BNB and Applied to its Domestic Operations was adopted. In compliance with it, the basic interest rate should be applied only to credits extended to commercial banks against collateral placed with the BNB such as government securities, foreign currencies, bills of exchange, etc., while non-collateralized deposits will be charged a margin over the basic interest rate. Due to these changes in the BNB monetary policy commercial banks' investments in government securities will not be included in their determined credit ceilings for the largest increase allowed of general debt in levs.
- 4 December** On behalf of the BNB the Board adopted a proposal for the amendment of Decree No.15 of the Council of Ministers of 1991. In coordination with the Ministry of Finance this proposal was submitted to the Council of Ministers. and adopted by it.
- 4 December** The BNB issued a licence for brokerage services to the financial brokerage house - 105, managed by Stefan Krustev and to the financial brokerage house "Capricornus" - Sofia, managed by Damyán Balabanov.
- 20 December** The BNB will refinance the commercial banks whose submitted bills are signed by the companies which were granted loans following government recommendations pursuant to Decision No.415 of 4 December 1991 of the Council of Ministers. The BNB requested alternation to Decision No.415 of 4 December 1991 of the Council of Ministers.
- 30 December** In compliance with the existing legislation, the acquisition of 15,000 Bank for Agricultural Credit shares, accounting for 10% of the shareholders equity of this bank, by the Raiffeisen Zentralbank, Vienna, has been approved.

**Bulgarian National Bank**  
**1878-1990**

The establishment of the Bulgarian National Bank immediately after the Liberation was a projection of the yearning of the Bulgarian people to overcome the economic backwardness left over by the Ottoman rule and to gradually build a modern banking system according to the standards of those times. Its development ran parallel to the comparatively rapid advancement of a capitalist economy in the country.

### **Establishment of the BNB**

The idea to establish a National Bank was first promoted by the provisional Russian authorities in Bulgaria. K. Buch, head of the finance department in the Russian administration prepared the Statute of the Bank which was endorsed by Prince Dondoukov-Korsakov on 25 January 1879. The Bank was inaugurated on 23 May 1879 after the replacement of the Russian administration by a Bulgarian one.

The Bulgarian National Bank was established as an autonomous state bank with capital equivalent to 1,800 thousand gold Levs and initial reserve fund of 200 thousand gold Levs. It was situated in Sofia but it had the right to open branches in other towns as well. Its objective was formulated in Article 1 of the Statute which read that the BNB was "established to promote the recovery and proper development of local trade as well as to regulate commercial relations and the population's lending in the Principality". The Bank operated under the supervision of the Ministry of Finance where it submitted its annual report. The official promulgation of its balance sheets was also envisaged.

### **Commercial Deposit Bank**

Over the initial years of its existence, the BNB was a purely commercial deposit bank financing trade in the urban areas. That was due to the fact that Bulgaria had no other banks yet to finance the emerging local industries and trade. The Bank was also the free cashier of the state budget and therefore, it could use the temporary surplus in the budget for short-term loans. It was not entitled to issuing banknotes yet but it kept time and demand deposits and opened current accounts of some larger companies. Right from the beginning of its existence it was decided that the Bank would not lend any loans to the government.

Initially, the BNB was supposed to extend only short-term loans (up to three months) against discounted bills or against a collateral of securities or precious metals. However, under the pressure of circumstances, the major instrument became long-term loans (loans to local communities for urban development purposes as well as to the so-called "agrarian savings funds"). The practice of discounting bills and lending against collateral did not develop to any considerable extent. The interest rates on loans were fixed at 8 per cent per annum.

### **The Reform of 1885**

In accordance with the Act of 1885, a reform of the BNB was effected which promoted its role as an issuing bank which issued banknotes payable in gold and kept a gold cover equivalent to 1/3 of the banknotes supply in its vaults. But the reform did not change the diversity of bank operations in terms of both the types of loans and their sectoral orientation because the BNB was still the only important credit institution in Bulgaria (though the first large private bank with Bulgarian capital was established in 1895 and three other large banks with foreign interest started operating in Sofia during the period 1903-1905). The Bank increased its capital to 10 million gold Levs and was granted the right to issue bonds in order

to attract credit resources from abroad.

After the economic crisis of 1898-1899 and especially in the course of the overall boom of the economy from 1902 onwards, the Bank expanded its operations very rapidly. The scope of that expansion could be illustrated by the fact that the total balance (as of 31 December) of the discounted portfolio plus the long-term loans increased from 5.9 million in 1887 to 53.1 million in 1900 and 130.3 million gold Levs in 1911. The upper limit for loans was raised to 500 thousand Levs or, in the case of entrepreneurs of railroads and other major public projects, up to 1,500 thousand Levs against a concession of the government receivables and with a special permit by the Board of Directors of the Bank. However, the maximum amount of the loans which could be extended to the state, could not exceed a half of the capital of the Bank.

At that time, the BNB abandoned the position of a commercial deposit bank and reinforced its stand of an issuing authority which also regulated borrowings in the country. After 1895 and particularly after the emergence of the three large private banks with foreign interest in 1905 (the Balkan Bank, the General Bank and the Credit Bank), the BNB ceded the crediting of industries and exports to the private banks though it still played an important part in that sphere until 1912.

### **Banknote Circulation Expansion**

The banknote circulation became an increasingly important source for the lending operations performed by the BNB. In spite of the continuing devaluation of silver as compared to gold, in 1900 the Bank was entitled to issue also silver-cover banknotes (but only up to one half of the issued banknotes of that type). That move led to some complications but, nevertheless, it contributed to the growth of the banknote circulation in the country. In 1890, the money supply included Bulgarian coins with a value of 17.1 million Levs and banknotes for only 1.5 million Levs but the ratio began shifting substantially in 1900. In 1900, the banknotes in circulation were already 14.2 million Levs as compared to local coins equivalent to 39.4 million Levs, whereas in 1911 the ratio was 131.9 million to 72.1 million Levs respectively. In the context of the growing banknote circulation, time deposits which had been the basic lending resource became ever more costly to the Bank and it started directing them to the large private banks in the country in an indirect manner, i.e. through reducing its deposits interest rates below the interest rates offered by the private banks.

Prior to September 1912 (the First Balkan War), the money supply in Bulgaria was characterized by completely free convertibility of the banknotes issued by the BNB into precious metals. Anyone could exchange their banknotes for gold or silver coins with the BNB or with the private banks and bankers. Initially, a small disagio, usually several per cent and very rarely up to 6-9 per cent, was paid for the conversion of banknotes into gold (depending on the demand for gold on the domestic market) when current payments were effected abroad. In 1906-1907, the disagio began disappearing as a result of the improved balance of payments of Bulgaria.

The rate of exchange of the gold Bulgarian Lev to the major currencies on the domestic and international markets was stable until 1912 and did not deviate from the nominal level by more than 1.7 per cent (99 to 101.7 Levs for 100 French Francs). Indeed, according to the estimates of the then Director of the Statistics Office K. Popov, over the period 1879 to 1911 the balance of payments of the country was viewed as slightly negative (a deficit of 209 to 245 million Levs with a total amount of the spending in foreign currency equal to 3,758 to 3,798 million Levs for the whole period) but that was probably due to some mistakes in the computation. The BNB was the basic factor for the stability of the exchange rate of the Bulgarian Lev until 1912. That was a substantial success of the Bulgarian economy unlike Greece, for example, which was also oriented towards the then Latin Monetary Union.

### **Discounting Operations**

The amendments to the Banking Act of 1906 rationalized to a certain extent the short-term credits for artisans and small tradesmen. In 1906, the BNB

undertook rediscounting operations discounting a growing share of the portfolio of various banks and bankers. In 1907, the Bank made arrangements for mortgage loans with maturity of 10 to 40 years and a possibility for issuing interest-bearing collateralized bonds. Pursuant to the Banking Act of March 1911 its capital expanded from 10 to 20 million gold Levs (only 17.8 million gold Levs were effectively deposited in 1912).

Alongside with the growing scale of lending operations, the BNB increased the number of its branches in the country. The first branch of the Bank was established in Rousse in May 1884; the branches in Varna and Plovdiv were established in 1885 and 1886 respectively. In 1893, the Bank already had five branches in the big towns and three agencies in smaller towns. In 1911, the network of the Bank incorporated 15 branches in the larger towns and 63 agencies in country centres.

The range of the discount rate of the Bank was as follows:

1879-1884 - 9 per cent  
1885-8 per cent  
1886-1887 - 7.5 per cent  
1888-8 per cent  
1889-9 per cent  
1889-1897 - 8 per cent  
1898-7 to 7.5 per cent  
1898-1906 - 8 per cent  
1907-1911 - 6 to 7 per cent.

## **Deposit Operations**

The interest rates on long-term loans were equal to 8 per cent initially and then they were lowered to 7 per cent in 1907. At the beginning the BNB paid very low interest rates on deposits (3 per cent annually for demand deposits, 4 per cent for time deposits of up to 5 years and 4.5 per cent for deposits of up to 10 years). Therefore prior to 1885 the Bank collected few deposits but that was set off by the opportunity for interest-free use of large transitional balances of the state budget. In 1890, deposit interest rates increased to 5 per cent for demand deposits of up to 1 year, 6 per cent for up to three-year deposits and 7 per cent for deposits up to 5 years (in 1897 the interest rates for all three types of deposits were reduced by one percentage point). Over the period from 1892 to 1900 deposits (almost exclusively five-year deposits) accounted for 36 per cent of all the liabilities of the bank balance sheet on the average but later on declined considerably (the amount of deposits rose from 1.9 million Levs in 1887 to 61.2 million Levs in 1900 and decreased to 42.2 million Levs in 1911).

From the 1890's up to around 1906 approximately 65 per cent of the discount credit (the major form of lending operations of the BNB) went to trade, 25 per cent to industry and entrepreneurship and 10 per cent to artisans and private banks. During the period from 1907 to 1912 the share of trade decreased to about 50 per cent on the average compared to 20 per cent for industry (mainly larger enterprises) and 30 per cent for private banks. But loans extended to urban municipalities and districts continued to occupy an important place in the long-term lending of the BNB.

## **External Loans**

After the first attempt at attracting foreign capital in 1889 which led to the insignificant amount of 4 million gold Francs, the BNB managed to involve larger external resources for the purposes of its lending operations. In 1893, the Bank contracted a loan of 20 million gold Francs against mortgage bonds at the European financial market and in 1909 it received a similar loan of 30 million gold Levs, part of which was used to convert the outstanding debt on the previous loan.

During the war years from 1912 to 1918 the BNB went through big difficulties. The disturbance of the economic life during and immediately after the First and the Second Balkan Wars (1912-1913) was not very serious but during World War I it reached disastrous levels and together with the recruitment of the

majority of the bank staff for service in the army to almost brought to a half the lending operations performed by the Bank. In 1915-1918 the BNB extended government-guaranteed credits only to local committees in accordance with the provisions of the legislation actual in 1914 for "economic affairs and social prudence" as well as to some industrialists and merchants who delivered military supplies. Given the large deficits in the state budget, the Bank was actually forced to finance the main bulk of the military spending at the expense of printing large amounts of new banknotes. All principles of issuing operations were violated. The government debt to the Bank increased from 8 million at the end of 1912 to 881 million Levs at the end of 1918.

## **Post-War Inflation**

The inflationary pressure continued during the first post-war years when the big deficits in the state budget continued due to the delayed payment of war-time requisitions, the costs incurred in the enforcement of the Neuilly Peace Treaty, etc. In the context of active inflationary financing of the state budget through banknote issues the amount of the government debt to the BNB reached 3.97 billion Levs at the end of 1922. The banknotes in circulation were equivalent to 3.78 billion Levs in the same year. It was not until 1922 that a law was passed on the restriction of the banknote issue because of a resolution made at the Genoa Conference. It ruled that the Bank could lend to the government an advance amount of up to 4.7 billion Levs. Inflation rates at that time can be illustrated with the following fact: the market price index from the base of 1912 reached 3,045 in 1923. In other words, the purchasing power of the national currency was reduced by more than 30 times which almost coincided with the growth of the banknote circulation during those years (29.2 times).

In order to outline the general unfavourable inflationary background against which the BNB had to operate in the wake of World War I, one should note the deep-going changes effected in the "cambial" policy of the Bank, i.e. the policy towards foreign currencies. When the First Balkan War broke out, the BNB stopped the exchange of banknotes for precious metals which was initially proclaimed to be only a temporary measure. That ban continued until 1919 when the new legislation introduced the compulsory banknote circulation without any convertibility of the already "paper" national currency into precious metals (although formally the BNB had to observe to a fixed percentage of gold cover of the banknote supply). Consequently, the exchange rate of the national currency began to decline rapidly. For the purpose of artificially maintaining a higher exchange rate of the new Bulgarian paper Lev, first government supervision and then government monopoly on the trade in foreign currencies was introduced in December 1918. For that purpose, the Central Office for Foreign Exchange Earnings was set up in 1919 but its activities were subsequently taken over by the BNB.

## **The BNB in the 1920's**

The scope and orientation of the lending operations changed in the immediate post-war period. From 1919 to 1922 the capital of the Bank kept on growing to reach 200 million Levs plus 50 million Levs "reserve capital" but, in real terms, that was only half of the pre-war levels (250 million Levs in 1922 were equal to no more than 9.8 million gold Levs). The early 1920's saw a tendency of actual reduction of the loans to local natural and juridical persons because private banks took up that activity. Besides, savings and current credit accounts decreased as a credit resource of the Bank. Similar was the reduction of savings in private banks which resulted from the decreased confidence in the Bulgarian national currency but the BNB made no attempts at undertaking counter action. In 1922, the amount of time deposits and current credit accounts at the Bank reached 1.47 billion Levs which, taken in real terms, was 2.5 times less than the amount on the eve of the First Balkan War (the amount was equivalent to about 53 million gold Levs in 1922).

1924 marked a new stage in the activities of the BNB which coincided with the new developments in the money supply under the conditions of the emerging

economic recovery. The government of the Democratic Alliance managed to halt the continuous growth of the banknote supply and curb the price increase which had been irresistible before but it could not avoid two subsequent, though weak, waves of additional increase of the cost of life in 1925 and 1928-1929. That stage lasted until the autumn of 1929 with a slight and fluctuating further rise of the price level (a total of 17 per cent as compared to 1924) as a result of some not particularly persistent attempts at restrictive policies with respect to budget expenditures and the attempts at partial deflationary policies for reducing the banknote circulation through external borrowing. The government debt to the BNB stopped growing and it ranged from 4.19 to 4.47 billion Levs over the period from 1924 to 1929. A new development was the National Currency Stabilization Act which reduced the theoretical gold cover of the Levs from 0.290326 to 0.010870 grams (26.7 times). That figure was not an accurate reflection of the extent of devaluation on the domestic markets as compared to 1912 but it was close enough to the real one. In 1924, the Equity Chamber was established at the BNB as an agency for mutually compensatory clearings and settlements among banks in Sofia.

From 1924 to 1928 the BNB tended to increase the amount of loans for private industries and trade though their level remained several-fold lower than the pre-war level of current accounts and discounted bills. The Bank went on with the policy of transferring such operations to private banks. The BNB almost discontinued mortgage loan practices. Pursuant to the BNB Act of 1924 its nominal capital was raised to 500 million Levs but the real equivalent of that capital was still lower than the pre-war level. The Bank continued to operate as a state institution but the Act of 1924 substantially reinforced its autonomy. The Board of Directors acquired greater independence and powers. The state, in its turn, preserved the right to supervise the activities of the Bank through a government delegate appointed to participate in the meetings of the Board of Directors as well as to use loans from the BNB up to 300 million Levs against treasury bills. Besides, the state continued to receive part of the proceeds of the Bank and to rely on the free cash execution of the state budget.

### **Transformation of the BNB into Purely Issuing Bank**

The reform of 1 January 1927 relieved the BNB from all long-term operations and turned it into a purely issuing bank. Short-term lending operations were quite limited; the practices of lending or opening current accounts against collateralized commodities were reduced and gradually discontinued. Lending on current accounts on the basis of mortgages or cession of indisputable receivables were discounted. The Bank reduced the term for advance payments against collateral of securities or guarantee in the form of bills of bona fide debtors from 9 to 3 months. But the practices of rediscounting part of the portfolio of private banks expanded.

The transformation of the BNB into a purely issuing bank and regulator of the money supply and the banking system was finalized with the new Bank Act of 1928. The government debt ceiling was slightly raised to 400 million Levs. One should note as a positive development also the fact that the stabilization loan of 1928 was used to retire a substantial portion of the government debt to the BNB, thus promoting the flexibility of the Bank.

In the 1920's the discount rate of the BNB increased from 6.5 per cent prior to July 1922 to 7 per cent in July 1923, 9 per cent in November 1923 and 10 per cent in August 1924. That increase resulted from the substantial spread between the rates of the BNB and the free money market where interest rates of 18 to 30 per cent were common, if not prevailing. In 1927, however, the private discount rate fell to 14 per cent and in 1928 to 13-11 per cent (later on even down to 10-8 per cent).

All that came to indicate that only for a few decades (until 1928) in an underdeveloped country, the BNB managed to go all the way through from a relatively small commercial deposit bank to a modern issuing bank according to the standards of those times, coping very well with the national task to regulate



the money supply and the overall lending activities. In the beginning of the 20th century the BNB had already become a bank well respected by all foreign and local partners. Its Governors in those times were highly educated and cultured professionals.

### **The Great Depression**

After the Depression of 1929-1933 the amount of the controlled banknote circulation was considerably reduced because of the spontaneous economic development (price decrease of 39 to 48 per cent on the average as compared to the level of 1929) which was not the result of a deliberate issuing policy of the Bank. The exchange rate of the Bulgarian Lev with respect to the "hard" foreign currencies was stabilized at the end of the 1920's and remained formally the same until the late 1930's though in 1931-1932 a hidden bonus was introduced at the sales of "hard" currencies in private compensatory transactions, reaching up to 35 per cent. Those bonuses, as well as the complicated system of foreign trade supervision and regulation of the balance of payments, were tantamount to admitting that the official exchange rates were unrealistic. Due to the large critical reduction of the foreign exchange earnings from exports from October 1931 onwards, the BNB was compelled to reinstate in a much more rigid form the government intervention in the trade operations with foreign currency which was cancelled from 1928 to 1931 when the Bank was the major buyer and seller of foreign currency in Bulgaria.

During the 1930's, the BNB reduced its credit operations in the spirit of the overall issuing orientation of its policies and as a result of the repercussions from the economic crisis. Credit placements amounted only to 373 million Levs in 1933 and 410 million Levs in 1938 as compared to 1,423 million Levs in 1929. The discount rate of the Bank over the same period of time was reduced from 10 per cent to 6-8 per cent with a tendency to further decline.

### **The Act of 1937**

The dependence of the BNB on the government increased during the second half of the 1930's. In accordance with the statutory regulations of 8 February 1937, the net profit of the bank (after the deduction of resources for various funds) was remitted directly to the revenue part of the state budget. The Bank was forced to participate in the capital of a number of public enterprises established on the grounds of special laws. That was the case, for instance, with the Central Co-operative Bank of Bulgaria, Bulgarian Credit Bank, Vucha hydropower station, etc. Besides, the Bank took active part in the credit securing of the large compensatory transaction with Bulgarian tobacco in 1934. At the end of 1936 the government debt to the Bank was on the increase again, reaching 3.44 billion Levs in 1938. All that restricted the adaptability of the BNB and its abilities to regulate the money supply and lending in Bulgaria.

### **The BNB during the World War II**

The last stage in the development of the Bank prior to the coup on 9 September 1944 was in the years of World War II when it was placed again under unfavourable extreme conditions and forced to finance the military spending of the government through new banknote issue. As a result of the higher inflation rates, the banknote circulation increased from 4.24 billion Levs in 1939 to 45.83 billion Levs in 1944, while the amount of deposits grew from 12.21 to 58.59 billion Levs. That increment of 6.3 times as compared to 1939 of the aggregate potential purchasing power of the population in the context of a continued drastic decline of the agricultural and industrial output in Bulgaria after 1942 led to a new precipitous depreciation of the national currency. The official retail price index pointed to an increase of the cost of living of 3.79 times in 1944 compared to 1939. Taking into account also the "blackmarket" prices, the actual increase of the cost of living was about 8 times over that period.

During the years of the World War II the BNB once again increased credit placements. In 1939 they were equivalent to 866 million Levs, while in 1944 they reached 17,737 million Levs which was actually a triple increase. The reason for that situation was the fact that the BNB had to cover the negative balance of the

German-Bulgarian clearing and also fulfil a number of government assignments to finance various industries and governmental organizations.

### **“Planned” Banking System**

In the post-war period the banking system underwent a series of structural and functional changes. One should point out the following stages of its development:

- 9 September 1944 - 1947: nationalization of banks;
- 1950 - 1970: transformation of the banking system into an appendage to the planned economy;
- 1971 - 1988: attempts at undertaking reforms and establishing a more efficient banking system;
- 10 November 1989 - 1990: transition to a market economy.

The changes in the social system in the wake of 9 September 1944 did not result in immediate substantial changes in the economic structure, including the banking system. From September 1945 to December 1947 Bulgaria had the same two-tier and strongly fragmented banking system which was typical of the pre-war period. Then the Bulgarian National Bank operated as a classical central bank and, at the same time, tried to use bank instruments and policies to regulate some basic proportions in the national economy.

The Agrarian and Co-operative Bank of Bulgaria remained an important element of the national economic system. It extended loans to general farmers' co-operatives, co-operative societies and their associations in forestry, tobacco growing, viticulture and wine distillery and other spheres. Larger enterprises were serviced by several commercial banks out of which the most important ones were the Bulgarian Credit Bank and the Trade Bank of Bulgaria as well as commercial banks with prevailing foreign interest. Loans to small-scale artisans, tradesmen and consumers were left largely to the co-operative banking sector, i.e. popular banks and lending co-operatives. They had a well ramified network in the smaller settlements all over the country. The confidence existing between those banks and their clients greatly facilitated the bank supervision. Regrettably, their role in the national economy was underestimated and they were eliminated in March 1951.

On 2 September 1946 a new Law on the Trade in External Means of Payment was passed; it superseded the law of 1929. Other important measures of the government were the new Regulations on Imports and Exports of 26 October 1946 and the replacement of money carried out from 10 to 16 March 1947. The objective was to replace the banknotes in denominations exceeding 200 Levs and the then existing treasury bills with 3 per cent interest rate. Amounts up to 2,000 Levs were exchanged in cash in a one-to-one ratio, while larger amounts were entered into blocked accounts. Private enterprises were allowed to exchange up to 50 per cent of the wage bill paid in the previous month but not more than 35 thousand Levs. State-owned enterprises and organizations were allowed to exchange all their cash. A month later a single property tax was introduced and thus more than 2 billion Levs were collected from enterprises. That was the second decisive blow sustained by the national economy which had just started recovering after the so-called Freedom Loan of 1945.

### **Nationaliza- tion of Banks**

The second stage of the post-war development of the banking system in Bulgaria began with the passage of the Banks Act of 26 December 1947 when banking was nationalized. The new legislation led to fundamental changes of the structure and functions of banks, following the model of the Soviet banking system. The property and functions of all commercial banks were taken over by the Bulgarian National Bank and the newly established Bulgarian Investments Bank which was assigned to perform the long-term financing of state-owned enterprises. The mutual lending among economic organizations was cancelled and they had to submit their cash to the banks' vaults on a daily basis, while the short-term financing of enterprises was geared to the indicators of the central plan.

## **The Money Reform of 1952**

Popular banks and lending co-operatives existed until 2 March 1951. They were dissolved by force of an ordinance which also spelled out new principles of short-term lending, reorganized the savings network and introduced new interest rates. Later in the course of the same year new Regulations on Payments were adopted together with a number of documents related to the "Wage Fund" control. Widely publicized was the so-called "supervision through the Lev" which was supposed to be performed by the banks.

A money reform was carried out on 10 May 1952. Old money was replaced by the new model of 1951. Three types of money were issued: banknotes in denominations of 10, 25, 50, 100, 200 and 500 Levs; government treasury bills of 1, 3 and 5 Levs and coins of 1, 3, 5, 10 and 25 Stotinki (1 St. = 0.01 Lv). Old money was exchanged in a 100:1 ratio and, at the same time, the scale of prices changed in a ratio of 25 to one. Savings of the population up to 50,000 Levs kept in savings banks were exchanged at a 100:3 ratio; from 50 thousand to 200 thousand - 100:2 and over 200 thousand Levs - 100:1. Funds of state-owned and co-operative enterprises were exchanged at a ratio of 100:4, while the exchange ratio for funds of private enterprises on bank accounts was 200:1. A new gold cover of the national currency equal to 0.130687 grams of pure gold was established. The exchange rate of the new Bulgarian Lev was bound to the rouble at the ratio of 1.7 Levs for 1 Rouble. That proportion was used to calculate the exchange rate with respect to the other foreign currencies.

The new Statute of the Bulgarian National Bank was drawn up in 1956. With all subsequent amendments (in 1957, 1958, 1959, 1961, 1963, 1965 and 1987), it failed to substantially change the activities of the Bank. It continued to follow Communist Party directives and in many cases also instructions coming from people in the top party echelon which lacked legislative or economic justification.

## **The Money Reform of 1962**

A new money reform was carried out on 1 January 1962. The gold cover of the national currency was increased to 0.759548 grams of pure gold and the scale of prices increased 10 times. New official exchange rates of the Levs with respect to the rouble (1 Rouble = 1.30 Levs) and the US dollar (1 USD = 1.17 Levs) which corresponded to the gold cover of those currencies - 0.987412 and 0.888671 grams respectively. Wages, salaries, other remunerations, pensions, savings as well as wholesale and retail prices, factory prices and purchasing prices were recalculated on a ten-to-one basis. Actually, the reform was a hidden devaluation of the national currency. Its gold cover increased only 5.8 times rather 10 times which would have been consistent with the increased scale of prices.

The Bulgarian Foreign Trade Bank was established in 1964. Its task was to effect external payments and finance foreign trade organizations in Levs and foreign currencies. Its bodies were the Shareholders' Meeting, the Board of Shareholders headed by the Governor of the Bulgarian National Bank, the Board of Directors and the Auditing Commission. The Board of Shareholders had a chairman, deputy chairman and 5 to 9 members elected by the Shareholders' Meeting for a three-year term of office. The Board of Directors chaired by the First Deputy Governor of the BNB had 7 to 9 members. Formally, the Bulgarian Foreign Trade Bank was established in the form of a shareholding company where the interest of the BNB was 72 per cent. The other shareholders were the Ministry of Finance, the Ministry of Foreign Trade, the Ministry of Transport and some foreign trade organizations. Actually, the bank was a purely governmental agency. Its task was to perform the monopoly external operations of a typical central bank, serve cash payments of the nation, while exercising the foreign exchange monopoly of the government. "Shareholders" neither paid in capital contributions nor took any interest in the functions of the bank, unless those functions were related to their own operations. One reason for the choice of the shareholding organization of the bank was to avoid any commitment of the government to the external bank debts which were contracted at government instructions at that time.

The efforts to incorporate the national economy in the "international division of labour" ran up against the inefficient and rigid foreign exchange

system. In the 1950's and 1960's a number of statutory and administrative regulations tried to streamline the foreign exchange system.

### **Structural Changes in the 1960's**

During the second half of the 1960's some structural changes were introduced in the banking system. Two new banks, i.e. the Bulgarian Agrarian and Trade Bank and the Bulgarian Industrial Bank, were established on 1 April 1969. They were the result of the aspirations of some top officials in the national economy to have their own banking institutions in order to avoid the credit restrictions imposed by the BNB and the Bulgarian Foreign Trade Bank. The newly established banks had capital of 50 million Levs each which was quite insufficient for their proper operation in agriculture, trade and industry. Deposits were rather limited, too. The two banks failed to develop their own branch network and they were closed on 1 January 1971.

With a view to maintaining the integrity of the banking system and introducing uniformity in the financing and comprehensive servicing of enterprises by a single bank, the Bulgarian Investments Bank was also closed on 1 January 1967. Its functions in the field of capital investments were taken over by the BNB, while the functions in the field of savings and loans for housing construction were taken over by the State Savings Bank.

### **Reform Attempts**

The twenty-year-long efforts to establish the banking system as an appendage to the planned economy and at the same time be in harmony with it failed; therefore partial reforms, aimed at the distinctive development of the banking system, were initiated in the early 1970's. Some of the measures were as follows: the introduction of a new mechanism of lending and payments in the beginning of 1971; the new regulations on the relationship between banks and the national economy in 1975 (amended and adjusted in 1976, 1977 and 1978); the establishment of Mineralbank in 1980 which operated on the basis of semi-market principles. The 1980's saw ever more frequent Communist Party forums discussing the economic restructuring which assigned new tasks to the BNB. For example, as a result of the decisions of the 13th Congress of the Bulgarian Communist Party the banking system acquired a new structure with the following elements:

1. The Bulgarian National Bank - central issuing bank;
2. Commercial banks:
  - (a) the Bulgarian Foreign Trade Bank - actually a second central bank;
  - (b) specialized commercial banks: Electronica CB, Biochim CB, Transport Equipment CB, Agrarian and Co-operative Bank, Construction Bank, Transport Bank, Bank for Economic Initiatives and Economic Bank;
3. The State Savings Bank.

Dozens of new shareholders' banks were established later on (until 1990). The general economic crisis affected the banking system which was left with insufficient resources. Except for the larger banks in Sofia whose capital reached 180 million Levs, the capital of other banks was rather modest. Some 30 banks had capital below 10 million Levs at the end of 1990. The total amount of the loan capital of commercial banks was about 30 times larger than their own capital which was well above the normal gearing ratio in market economies. Besides, their operations were strictly regulated and stable; if any of them encountered financial difficulties they could rely on assistance by their central banks and also by a number of foreign financial institutions which they were related to. Banks in smaller settlements abroad are not independent as they were in Bulgaria, they are branches of large banks which supervise and assist them if necessary. Local Bulgarian banks could not rely on any substantial assistance from local or external sources. Due to their isolation from the world banking system the Bulgarian National Bank had to maintain their stability.

For the last four decades the development of banking in Bulgaria was directly determined by political factors which impeded its independent contribution to the

establishment of an efficient economy. The hectic and occasional attempts at influencing the economy which were confined to the encouragement or sanctions of individual economic organizations on the microlevel proved unsuccessful. On the other hand, the organization of the economic system and mainly the state ownership of enterprises doomed to failure the measures undertaken by the banking system to influence the economy. Since, in the final analysis, all economic organizations were financially dependent on the government, bank and budget resources were blended, bank loans lost their identity and ability to exercise control and influence. Thus banks turned into mere settlement houses but even that function was difficult to perform because of the great mutual indebtedness of enterprises and their debts to banks. In that context the banking system neither had the objective opportunities nor was allowed by the top authorities of the totalitarian regime to influence the economic development of the country.