Deloitte & Touche

Bulgaria Electronics -- Information Memorandum for Feromagnit

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FEROMAGNIT

INFORMATION MEMORANDUM

2

The purpose of this Information Memorandum is to provide potential investors with general information about Feromagnit, a company located in Pernik some 24 km from Sofia. The company converts basic raw materials into ferrite and magnetic components.

The company is currently State owned and has been selected for privatisation. The Privatisation Agency is responsible for handling the negotiation and sale of Feromagnit. It is intended that the business will be sold as a going concern. Up to 100% of shares in the company or its business and assets are available for sale on a going concern basis.

Although care has been taken to ensure that the information contained in this memorandum is correct in all material respects, no warranty is given that it is complete or accurate in all respects. Potential investors are advised to make their own investigations and satisfy themselves as to the condition and prospects of the business and the accuracy and completeness of the statements contained in the memorandum.

The information contained in the memorandum does not constitute an offer to subscribe for or purchase shares in Feromagnit or its assets and no contract may be entered into on the basis of the information contained in it. The memorandum is intended as a starting point in a process to induce bids for the company. The Privatisation Agency is under no obligation to sell the company or any part thereof to any interested party on foot of this document and reserves the right to negotiate with several potential buyers.

Eligibility to acquire Feromagnit depends on prospective purchasers providing evidence of their expertise and credit worthiness. The document does not contain, at this stage, any indication of price; price will be the subject of final negotiation with the Privatisation Agency. The following factors will be taken into account in any negotiations:

(i) The credentials of the potential investor in terms of technology and marketing.

(ii) The investor's development plan for the company covering inter alia:

- Future capital investment plans.

- Proposals regarding current and projected employment strategy.

- The extent of assumption of existing debt.

(iii) Price offered.

The information is confidential and is intended only for the use of the addressee. It should not be copied or distributed and the addressee should keep confidential all matters contained in it.

While Deloitte & Touche has assisted in the preparation of the memorandum, neither Deloitte & Touche nor any of its partners or employees makes in the memorandum any representation or gives any warranty, either expressed or implied in relation to the company, its assets or its prospects. Deloitte & Touche has not audited any of the financial information contained herein.

The Privatisation Agency reserves the right to advertise Feromagnit in other media as well as through this Information Memorandum.

Interested parties are encouraged to meet with company management to discuss business strategy and development plans as part of their evaluation of the company.

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FEROMAGNIT

INFORMATION MEMORANDUM

1. Executive Summary

2. Business Description and Development

3. Products, Sales and Markets

4. Production Process and Facilities

5. Organisation and Management

6. Summary Financial Information

7. Key Features

Appendix I Doing Business in Bulgaria

Appendix II Bulgarian Electronics Industry

EXECUTIVE SUMMARY

Section 1

1.1 COMPANY

Feromagnit is located just outside the town of Pernik (24km west of Sofia). The Company converts basic raw materials (oxide powders, metal alloys) into ferrite and magnetic components and is the only company of its kind in Bulgaria.

The Company is currently State owned and has been selected for privatisation.

1.2 PRODUCTS

The principal products produced by Feromagnit are:

(i) Soft ferrites

These are produced under a TDK license. Such ferrites can be used in acoustic equipment, long distance communication and radio equipment contour coils, intermediate frequency transformers, antenna devices, impulse and feeding transformers and absorption elements.

The production range of soft ferrites is varied and covers a wide number of products and configurations/applications

(ii) Hard ferrites/Oxide Magnets

Production of such ferrites began in 1975 under a TDK license. The following magnetic hard materials are produced:

- Barium ferrites in the form of solid solutions
- Strontium ferrites
- Plastic magnets

Oxide magnets are used in magnetic systems for loudspeakers, motors, magnetic locks, contractor systems, separators, blocking units, micro-motor stator magnets and actuators.

1.3 MARKETS

For many years, Feromagnit was a major magnet manufacturer in COMECON markets. Due to the contraction of these markets, and the current difficulties in obtaining payment there, trade has been significantly reduced. Feromagnit has sought to develop Western markets to counteract the loss of its traditional markets, and has, to date, successfully exported to Germany, Turkey and the United Sates.

Feromagnit's principal strengths in the marketplace are its lower price per unit, while providing at least equal quality in terms of performance to its competitors.

1.4 PRODUCTION FACILITIES

Two principal production capabilities exist:

(i) Standard ferrite production
(ii) Higher specification rare earth magnet (RECO) and ferrite monocrystal production.

The Company currently has significant available production capacity to produce a range of standard soft and hard ferrites to high-quality performance standards.

The Company has a range of modern, high-technology equipment for the production of RECO magnets and monocrystal ferrites. It has a capacity to produce two tonnes of RECO magnets per annum.

Because of difficulties in the market, the Company has not been producing either RECO magnets or ferrite monocrystals for a number of years. The equipment however, has been maintained in excellent condition, and presents a significant opportunity to a potential foreign investor to engage in production in these areas.

Production capacity is currently under-utilised, and management estimate that the local Bulgarian market will use only 20% of annual production capacity. Significant spare capacity currently exists on the modern RECO and ferrite monocrystal production line.

1.5 QUALITY

The Company considers that its products are of a quality standard equivalent to its competitors, including those in Western markets.

1.6 ORGANISATION

The Company currently employs 318 staff, approximately 250 of which are members of a union.

Average pay was 1,720 Leva per month ($65) in 1992.

1.7 SUMMARY FINANCIAL INFORMATION

Summary Profit & Loss Account Information

Bulgarian Leva	1992 (000's)	1991 (000's)	1990 (000's)
Turnover	28,535	36,738	23,248
Gross Profit	15,875	22,873	12,800
Profit/(Loss) before Tax	(18,711)	1,809	4,756

Summary Balance Sheet Extracts as at 31st December 1992

	Bulgarian Leva (000's)
Fixed Assets	221,337
Current Assets	37,896
Bank Loans	(28,313)
Trade and Other Liabilities	(13,774)
Net Assets	217,146

The Company has made application under Bulgarian law to have some of its existing outstanding debt restructured, either through absorbtion of the debt by the State or through conversion to a form of equity.

9

1.8 KEY FEATURES

- The Company's products are produced at a lower cost than competitors and are considered equal, at least, in terms of quality. The international market for magnets is very large.
- The Company has a skilled and low cost workforce.
- The production capability encompasses both relatively low specification soft ferrite cores, to higher specification ferrite monocrystals.
- Significant spare production capacity currently exists.
- The Company has efficient modern high-technology equipment for RECO magnet and monocrystal manufacture.

The Company is seeking a foreign investor/partner, who can:

(i) Bring marketing expertise and distribution channels to Western markets.
(ii) Assist in keeping abreast of technological developments.
(iii) Assist in upgrading certain capital equipment.
(iv) Develop enhanced materials requirement planning, and assist in improving the logistics of transporting finished goods.
(v) Assist in introducing advanced statistical quality control techniques.

Feromagnit offers such investors/partners an attractive opportunity to develop an existing magnet manufacturer into new markets, with quality low-cost products.

10

BUSINESS DESCRIPTION AND DEVELOPMENT

Section 2

2.1 INTRODUCTION

Feromagnit is located just outside the town of Pernik (population 120,000), 24km West of Sofia. The Company converts basic raw materials (oxide powders, metal alloys) into ferrite and magnetic components and is the only company of its kind in Bulgaria.

Its principal products are soft ferrites, hard oxide magnets and metal magnets. About 75% of the plant's production has been in oxide magnets. In addition to oxide magnets, Feromagnit has facilities to produce RECO (Rare Earth Cobalt) magnets, monocrystals, and cast metal magnets.

A block diagram of the site and activities conducted in each building is shown in Figure 1.

The company employs some 318 employees and plans to further reduce this number as more efficient work practices are implemented.

2.2 HISTORY AND DEVELOPMENT

Feromagnit started production in 1964 as part of the "Elektronni Elementi" group of factories. It has undergone development in three stages.

- **1972-75** Production lines installed for production of soft ferrites and oxide magnets under TDK License.
- **1976-82** Further development and installation, including reorganising the Cast Magnets Shop.
- **1984-87** Capacity was increased. Equipment for production of rare earth magnets, high density ferrites and monocrystals was installed.

Feromagnit was registered as a separate legal entity in July 1989. Its registered activities are R&D, engineering, production of magnets and ferrites and marketing in Bulgaria and abroad.

The company had its own R&D department until 1991 when this activity was discontinued due to economic stagnation in Bulgaria.

11

The changes in CMEA markets have had a significant effect on Feromagnit's business in recent years, resulting in reduced sales volumes and capacity utilisation. To counteract this, the Company has, in recent years, commenced developing new market opportunities, principally in Western Europe.

12

PRODUCTS, SALES AND MARKETS

Section 3

3.1 PRINCIPAL PRODUCTS

The principal products produced by Feromagnit are:

(i) Soft ferrites
(ii) Hard ferrites/oxide magnets
(iii) Metal magnets

A brief description of the two principal product categories is set out below.

- ***Soft Ferrites***

The Company commenced the production of soft ferrites in 1975/6 under a TDK license. The electromagnetic characteristics of the soft ferrites compare favourably with those of foreign competitors. Dimensions of the products are in accordance with international standards. In the past, production has been principally for the local market, with a small level of exports to Italy and Yugoslavia. During 1976 to 1992, capacity increased significantly through the purchase of new equipment (presses, furnaces, grinding machines). The Company carries out research on European markets. Its main competitors are ferrite producers in Hungary, Poland, the Czech Republics and Russia.

The Company has the capacity to produce between 150 and 200 tonnes of soft ferrites per annum.

The technology used in production of soft ferrites is similar to that used in the production of ceramic and powder metallurgical products. Production includes three main groups of ferrite material, depending on raw material inputs, i.e. manganese zinc, nickel zinc and manganese magnesium ferrite.

Soft ferrites can be used in acoustic equipment, long distance communication and radio equipment, contour coils, intermediate frequency transformers, antenna devices, impulse and feeding transformers and absorption elements.

The production range of soft ferrites is varied, with a wide number of products and configurations/applications, e.g. ferrite cores, E Type ferrite cores, ferrite toroidal cores, RM-cores, deflection yoke cores, ferrite antenna, etc.

The Company produces a range of nickel zinc ferrite materials and products which operate at frequencies from 300 KHz to 150 MHz.

The Company supplies communications ferrite cores, mainly for communication equipment.

In recent years, the Company has had a policy of seeking to develop high performance ferrites in response to new market demands.

- *Hard Ferrites/Oxide Magnets*

Production began in 1975 under a license from TDK. Until 1990, the Company produced primarily for the local market, with low levels of export to Italy, Yugoslavia, Turkey and Poland. During 1991 and 1992 production has been mainly for export to Russia, Spain and Germany.

Feromagnit produces the following magnetic hard materials:

- Barium ferrites in the form of solid solutions
- Strontium ferrites
- Plastic magnets

Production includes isotropic and anisotropic oxide magnets and isotropic plastic magnets.

The technology requires precise milling of raw materials, granulation, rough milling, fine milling, preparation for pressing, final pressing, mechanical treatment and magnetisation.

The production of anisotropic barium and strontium magnets is done by two basic methods, dry and wet. The wet method of production of anisotropic magnets ensures the achievement of higher magnetic parameters than those achieved by the dry method.

The production range includes:

- Toroidal permanent magnets
- Segmented magnets
- Parallelopiped form magnets
- Isotropic magnets with various configurations and applications

Oxide magnets are used in magnetic systems for loud-speakers, motors, magnetic locks, arch-damping chambers, contractor systems, separators, blocking units, micro-motor stator magnets and actuators.

3.2 SALES AND MARKETS

For many years Feromagnit was dependent upon COMECON markets for all its output. These Eastern Bloc markets have contracted significantly and currently can pose difficulties in obtaining payment, with the result that a reduced level of trade has been carried out there on a barter basis. The table below shows the significant change in the Company's markets over the past five years.

Turnover:	1992 %	1989 %
Domestic	30	96
CMEA	52	0
Western Europe	16	2
Other	2	2
Total	100%	100%

Feromagnit has sought to export into Western markets to counteract the loss of its traditional Eastern European markets. To date, it has exported to Germany and has contracts with companies in Turkey and in the United Sates. The development of contact with Western European companies in particular, has resulted in orders being generated for:

- Anisotropic magnets
- Isotropic magnets
- Soft ferrites

Feromagnit's principal strengths in the market place are its lower price per unit, while providing at least equal quality in terms of performance to competitors. Its anisotropic magnets in particular, have high quality specifications, and management consider them to be of equivalent standard to those produced by Philips and TDK. The equipment and technology currently on hand are adequate for production to market standards.

The Company has currently no orders for RECO magnets or ferrite monocrystals, but existing equipment, which is modern, can be readily be brought back into production. In addition, there is considerable spare capacity on all production lines.

Management acknowledge the need to develop a strong marketing oompetence. A key credential for any prospective investor concerns the marketing capability and sales distribution channels which he can bring to the Company.

3.3 SUMMARY

Feromagnit offers prospective investors an opportunity to access both Eastern and Western European markets with products manufactured to international quality standard, but at significantly lower costs than competitors.

16

PRODUCTION PROCESSES AND FACILITIES

Section 4

4.1 INTRODUCTION

Figure 4.1 sets out the layout in diagrammatic form. The principal areas of production, namely ferrite production, oxide magnet, plastic magnets, rare earth magnets, ferrite monocrystals, high density ferrite and cast metal magnets, are set out below.

4.2 PRODUCTION OF SOFT AND HARD FERRITES

The main building contains two principal lines for the production of soft and hard ferrites. The lines for hard ferrites cover production of both isotropic and anisotropic ferrites. The lines for anisotropic magnets are split between a line for wet processing of anisotropic magnets which is the largest and more modern, and a line for dry processing of magnets.

The main building contains a small production line for plastic isotropic magnets.

4.2.1 Material Preparation

The materials for the different lines are prepared by different types of equipment. Similar preparation procedures apply to both soft ferrites and to hard ferrites (oxide magnets). The line for the preparation of the wet pressed magnets is comparatively new and modern. The equipment for the rest of the production lines is old but still functioning.

The processes used are:

(i) For Soft Ferrites

The raw materials are mixed while wet in mills. After filtering and drying of the ferrite materials, they are sintered. The new material is milled while wet in mills, to correct particle size. During the procedure, other materials are added in order to achieve the desired electromagnetic properties of the material. The chemical composition is controlled by means of X-Ray and fluorescent analysis.

17

(ii) **For Hard Ferrites (oxide magnets)**

The firm's production of hard magnet ferrite materials comprises:

- isotropic and anisptropic barium materials ($BaO.6Fe_2O_3$)
- isotropic and anisptropic strotium materials ($SrO.6Fe_2O_3$)
- plastic magnets

The raw materials used in production are Fe_2O_3, barium and strotium carbonates and other supplements. The raw materials are mixed and then made homogenous while dry in a vibromilling machine. The mix is then made into granules of the correct size, after which they are placed in rotating furnaces. The ferritized material is milled roughly in vibro milling machines. The material is then milled in wet mills to the correct particle size, together with other raw materials to improve the properties of the magnets.

4.2.2 Pressing

Material for dry processing is placed in the silo, from where it is transported to the press. The presses are automatic and semi-automatic, and of Japanese and German origin.

Wet material, in the form of a suspension is transferred via pipes to the press (anistropic oxide magnets only). There, it is fed into the press in measured doses. The pressed materials are removed from the tool by means of manipulators. These presses are relatively modern, were manufactured by the Japanese firm YUKEN and are capable of working in a semi-automatic mode.

4.2.3 Sintering

The pressed products are sintered in tunnel furnaces (a firing process using kilns). The soft magnets are fired in a nitrogen environment in one of three sintering lines. One of the lines is relatively new, but the remainder need modernisation, although they are still operational.

Oxide magnets can be burnt on 6 sintering lines. One of these lines is new and can handle 75% of production (Tokai 360 kW). The other lines require modernisation.

18

4.2.2 RECO

Feromagnit has a modern RECO production facility consisting of:

- Vacuum electric arc furnace for the preparation of the input mix.
- Autoclaves for the separation of the existing alloy.
- Vibromilling machine for the calculation of dosage to correct size of particles.
- Vibromilling machines mill in 1kg lots in acetone.
- 2 Presses; Yuken (1986) - in very good condition.
- Computer controlled vacuum heat treating and thermal processing machine (DALA 1985).
- 3 furnaces for subsequent heat processing.
- Final processing and grinding and cutting.

The capacity is two tonnes of RECO per year. The company has not produced RECO magnets for over a year.

4.4 FERRITE MONOCRYSTALS

The equipment for producing ferrite monocrystals (suitable for use in VCR recording heads or computer read/write heads) is modern and in excellent condition. Crystals of 60 mm in diameter and 140-160mm in length can be produced. The monocrystals produced are of good quality.

Feromagnit has purchased equipment for hot isostatic pressing, along with two furnaces which can work up to 1,200°C from 1,600-2,000°C, and at 2,000kg/sq. pressure. The equipment can be used both for the production of high density ferrites and for enhancement of the properties of other materials. The pressure of 2,000kg/sq. cm is created by means of inert gas (N2 or Ar). This equipment is in very good condition.

19

4.5 PRODUCTION OF CAST MAGNETS

The cast magnets shop produces magnets from alloys of pure metals. Induction furnaces are used to heat and melt the material (ALNICO) and the molten metal is poured into formaldehyde resin moulds. When the metal is cold, mechanical processing is done. There is further processing equipment (principally annealing and magnetisation equipment) which is relatively old and in need of upgrading. The equipment for final processing is adequate and most of it is in good condition.

4.6 OTHER FACILITIES

There is a reasonable selection of test and measurement equipment (Scanning Electro Microscope 'Jul', 2 X-Ray spectral devices 'Rigaku Denki', BH testing equipment). For tool-making, there is a spark erosion machine (DEM 315 AGIE) and a Hauser precision milling machine.

4.7 CAPACITY UTILISATION

Due to the contraction of its principal markets in the East, Feromagnit's production capacity is currently under-utilised. Management estimate that local Bulgarian market requirements will absorb approximately 20% of annual production capacity. Significant spare capacity currently exists on the RECO and ferrite monocrystals and high density ferrite lines.

4.8 RAW MATERIAL SUPPLY

Raw materials were supplied from the following territories in 1992:

Bulgaria	22%
CMEA	77%
Europe	1%
America	0%

The Company experiences no difficulties in securing materials of an appropriate type and quality for production.

20

4.9 QUALITY

The Company considers that its products are of a quality standard equivalent to its competitors, including those in Western markets. Quality control procedures include:

- Testing incoming raw materials in a chemical and X-Ray laboratory.
- Carrying out Quality Control procedures throughout the production process. Electromagnetic parameters are checked in a testing laboratory on ferrite output.

Testing equipment is considered good, with adequate back-up equipment in the event of failure.

Final quality control checks are carried out on a statistical basis, in accordance with Bulgarian national standards.

While quality control procedures, both prior to, and during the production process, ensure that output is to a high quality standard, management accept that there is scope for the introduction of more advanced quality control techniques.

4.10 SUMMARY

Feromagnit has significant available capacity to produce a range of soft and hard ferrites to high quality standards, together with the capability to produce higher specification RECO magnets and monocrystal ferrites.

The equipment to produce standard ferrites, while in some cases relatively old, is functional, and modern equipment is on hand for the production of anisotropic oxide magnets and for higher specification manufacture.

ORGANISATION AND MANAGEMENT
Section 5

5.1 CORPORATE STRUCTURE

The company is state owned and has being transformed into a limited company, with the state as the sole shareholder.

5.2 CORPORATE ORGANISATION

An Organisation Chart is shown in Figure 5.1.

5.3 SENIOR MANAGEMENT

Georgi Georgiev

The Executive Director, Mr. Georgiev, has worked in Feromagnit since 1970. He assumed the role of Managing Director in October 1992, and is a member of the Board of Directors. He has considerable experience in the design, R&D, and production of ferrites.

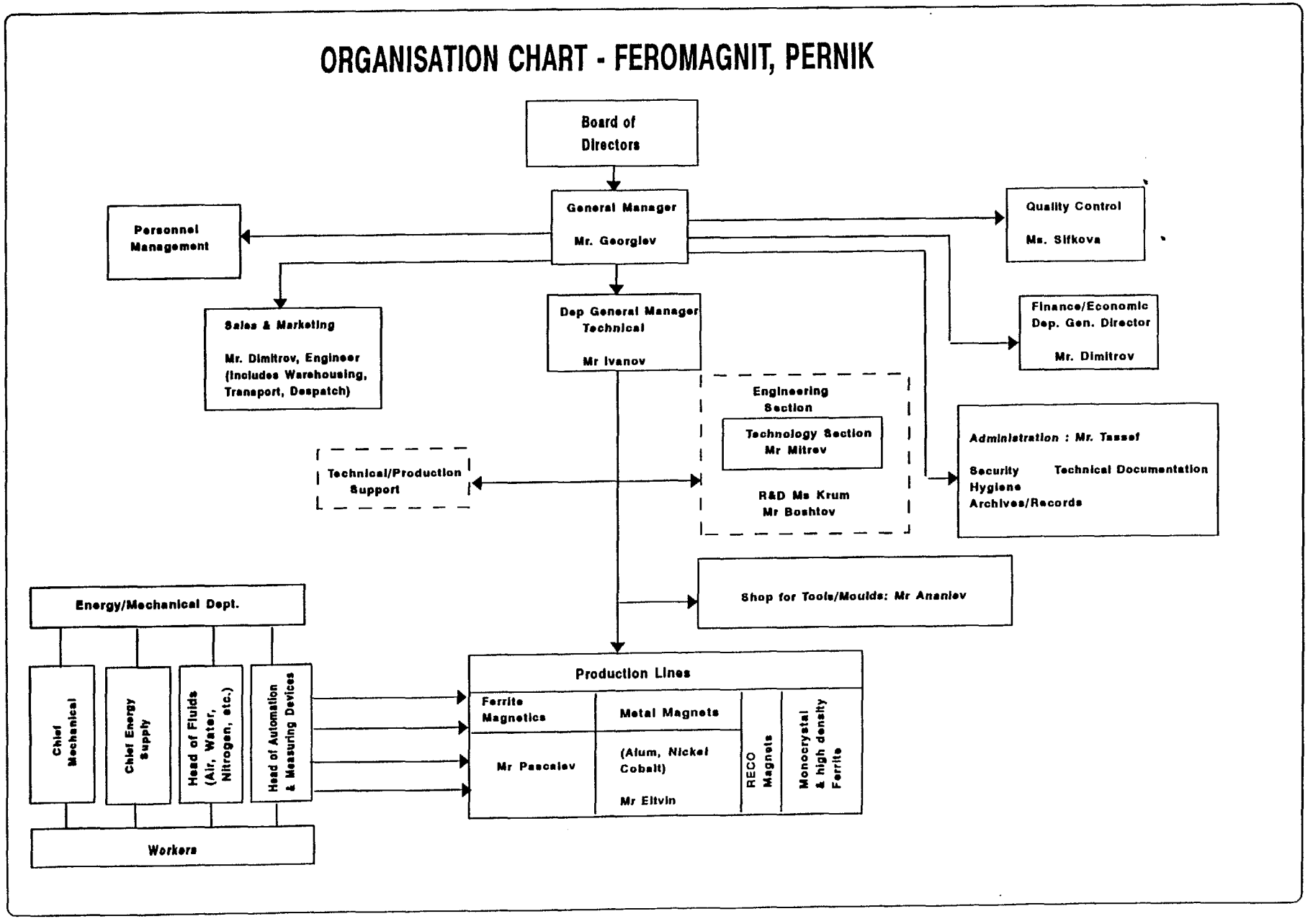
Iordan Ivanov

The Deputy Director for Production, Mr. Ivanov, has been working in Feromagnit since 1976. He has held positions as Head of Construction Department, Head of Mechanical Plant and Head of Auxiliary Production. In his current position (held since October 1992), he is responsible for production scheduling, capital budgeting and maintenance and repair of process equipment.

Dimitir Dimitrov

The Deputy Director for Engineering and Marketing, Mr. Dimitrov graduated from the Higher Institute of Chemistry and Technology. He has worked in Feromagnit since 1978 and has held positions as an engineer, Head of Technology, Head of Research & Development and assumed his current position in 1992.

ORGANISATION CHART - FEROMAGNIT, PERNIK



5.2 OTHER INFORMATION

The Company currently employs 318 staff. Approximately 250 employees are members of a Union. Average pay was 1720 Leva per month ($65) in 1992.

The Company's financial and Accounting Department produces a monthly information package within 15 days of each month end.

SUMMARY FINANCIAL INFORMATION

Section 6

Key summary financial information on Feromagnit is set out below. This information is based on the annual financial statements of the Company. The information has not been audited by Deloitte & Touche.

Summary Profit & Loss Account Information

Bulgarian Leva	1992 (000's)	1991 (000's)	1990 (000's)
Turnover	28,535	36,738	23,248
Gross Profit	15,875	22,873	12,800
Profit/(Loss) before Tax	(18,711)	1,809	4,756

Profit before Tax has been arrived at after charging

Personnel costs	12,715	8,405	3,952
Interest	12,064	5,192	197
Depreciation	3,316	3,297	3,661

Summary Balance Sheet Extracts as at 31st December 1992

	Bulgarian Leva (000's)
Fixed Assets	221,337
Current Assets	37,896
Bank Loans	(28,313)
Trade and Other Liabilities	(13,774)
Net Assets	217,146

The following points are relevant:

(i) The volume of sales has fallen over the period, principally due to the loss of Eastern European and CIS markets. The increase in sales value reflects the effects of high inflation.

(ii) The loss in 1992 is due to contraction in business activities and the high interest charged on bank debt.

(iii) Fixed assets were revalued at 31st December 1992.

(iv) Bank loans of c. 28m. leva (US$1m. approx.) at 31st December 1992, includes 9m. leva accrued interest.

The Company has recently had difficulties in obtaining sufficient working capital for its requirements. This has constrained its production capability, with a resulting slowdown in meeting orders.

Under Bulgarian law, application can be made to reorganise outstanding debt, either through assumption of the debt by the State or through conversion to equity. This reflects the recognition by the State that historical debt should not act as an impediment to privatisation. The Company has made such application. It is expected that this matter will be resolved prior to, or as part of, the privatisation of the Company.

KEY FEATURES

Section 7

Feromagnit has many attractive features for a potential investor. Several challenges also face the company, particularly in relation to developing new markets and modernising certain equipment.

Key features of this investment opportunity include:

- The Company's products are produced at a lower cost than competitors and are considered equal, at least, in terms of quality. The international market for magnets of the type manufactured by the Company is extremely large.

- The Company has a skilled, low cost workforce. It has reduced its workforce by over half over the last two years. This means that a readily available pool of highly qualified and skilled employees exists locally and also that any over-manning has been dealt with to a significant extent.

- The production capability encompasses both relatively low specification soft ferrite cores, to higher specification ferrite monocrystals. This product range can be expanded to cover other sizes and types of components.

- Significant spare production capacity currently exists.

- The Company has efficient modern, high technology equipment for RECO magnet and monocrystal manufacture.

- There are no property or land restitution issues or major environmental problems affecting the Company.

The key areas in which the Company requires to improve its capabilities are:

(i) The development of marketing and distribution channels in Western markets. The company has identified the need for a formal marketing and distribution strategy in order to take advantage of its position in Europe. Marketing up to now has been performed on a somewhat informal basis. The company needs assistance to improve its technical marketing capability, to focus more specifically on growth sectors of the market, and to identify market opportunities.

(ii) Assistance in keeping abreast of technological developments.

(iii) Upgrading of certain capital equipment. In particular, inefficiencies in the sintering ovens have been recognised as being a potential problem in the long term.

(iv) In developing enhanced Materials Requirements Planning and in the logistics of transporting finished goods, in order that goods of a consistent quality can be delivered on time.

(v) In introducing advanced statistical Quality Control techniques.

An investment of approximately 8m leva (US$315,000) primarily for machine repairs and materials is required to ensure the Company satisfies production orders for the rest of 1993. Further investment of 16m leva would allow a comprehensive upgrading of furnaces, presses, ball mills and the compressor station.

Feromagnit offers investors/partners an attractive opportunity to develop an existing magnet manufacturer into new markets with quality low cost products.

28

APPENDIX I

BULGARIA

OPEN FOR BUSINESS AND INVESTMENT

BULGARIA
OPEN FOR BUSINESS AND INVESTMENT

INTRODUCTION

Successful changes towards pluralism in political life and in the economy have taken place in Bulgaria since the end of 1989. Bulgaria was among the late Eastern European reformers but has made significant steps towards a western style mixed economy in a short timeframe. A range of important laws covering ownership and use of agricultural land and restitution, a new Trade Act and importantly, laws on Foreign Investment and Transformation of State and Municipal Enterprises have been enacted in recent years.

Bulgaria's strategy for economic reform aims to achieve:

(i) Stabilisation of the national economy in a new macro economic framework, and

(ii) Rapid introduction of market mechanisms and restructuring of the economy.

Price reform commenced on 1 February 1991. This was designed to correct price distortions and reduce demand to a level corresponding to the level of supply. A complete liberalisation of trade took place in the course of 1991. Import liberalisation advanced quickly. Tariffs and floating exchange rates were introduced as major policy instruments.

The exchange rate liberalisation process introduced a unified inter-bank floating exchange rate and the creation of a decentralised framework of foreign exchange allocation, based on an inter-bank foreign exchange market.

ABOUT BULGARIA

- ***Capital City***: Sofia (Population 1.219m - (1991))

  Language: The official language is Bulgarian

30

Currency: The official currency is the Bulgarian Lev

Area: The total area of Bulgaria is 110,993.6 Sq Kilometres

Location: Bulgaria is situated in south eastern Europe in the eastern half of the Balkan Peninsula. To the north it has a common border with Romania (609 Kilometres), and to the east, the Black Sea with a coastline of 378 kilometres. The southern board of Bulgaria is 752 kilometres long, running north of Turkey (259 kilometres) and Greece (493 kilometres). To the west, Bulgaria borders on Serbia and Macedonia.

Climate: The climate of the largest part of the country is moderately continental with four clearly differentiated seasons - Spring, Summer, Autumn and Winter. The country's average temperature is 10.5°C. The coldest month is January with an average temperature of 2°C while the warmest is July with an average temperature of 25°C.

GEOGRAPHY

The country covers a comparatively small terrain and contains a wide variety of plains, hills, valleys, and deep river gorges. 70% of Bulgaria consists of high altitude plains and hills.

POPULATION

The population of Bulgaria, according to the census at 31 December 1991, was 8.5m. The average density of the population was 80.9 persons per sq. kilometre.

BULGARIAN ECONOMIC SITUATION

In common with other Eastern European countries, Bulgaria has experienced a number of specific problems on its road to democracy and a free market economy. The collapse of Comecon, the switch to hard currency intra Comecon trade, unpaid debt from Iraq and other countries, as well as the unreliability of the former Soviet market have constrained Bulgarian reforms.

In February 1991, Bulgaria agreed with the IMF to implement a tough austerity plan introducing major economic reforms such as price liberalisation, restructuring of the banking system and access of foreign enterprises to foreign exchange.

One of the key objectives has been to reduce the annual inflation rate. With that aim in mind, prices of all goods were liberalised in order to allow prices find their free market level, eliminating all subsidies except those on energy products. The inflation rate in 1992 was approximately 80%.

Over the past three years, significant efforts have been undertaken to break up monopolistic structures which were a previous characteristic of the Bulgarian economy. A wide number of newly established limited liability and joint stock companies have been established in Bulgaria as part of its reform to a market economy.

During 1992, the production of goods and services in the Bulgarian economy fell by 20% relative to 1991. This was mainly due to decreases in the engineering, food, chemical and oil processing industries.

PRIVATISATION IN BULGARIA

The privatisation process is a key factor in economic reform in Bulgaria.

In 1991, the parliament adopted a law on the ownership and use of agricultural land. This guaranteed the right of private ownership of land for Bulgarian citizens, restoring as far as possible, ownership rights existing in 1946. Every Bulgarian citizen who has permanent residence in the country is allowed to own agricultural land. Companies which have less than 50% foreign ownership can also buy agricultural land.

In 1990, the Bulgarian parliament adopted a law on establishment of sole proprietary commercial companies with State property. This law provided that all Bulgaria's State owned companies were to be transformed into either joint stock or limited liability companies to be later privatised or remain under State control. In April 1992, a law on the Transformation and Privatisation of State and Municipal Enterprises was adopted. Privatisation will be put into effect by transferring shares

32

and interests from State or Municipal owned enterprises to individuals or new legal entities.

Privatisation is carried out in accordance with annual privatisation programmes prepared by the Council of Ministers and the Agency of Privatisation.

The practical management of the privatisation programme is carried out by the Agency for Privatisation.

FOREIGN INVESTMENT FACTORS

Foreign investment is considered to be of crucial importance to the process of economic reform in Bulgaria. Foreign capital invested in Bulgaria is regulated by the provisions of the Business of Foreign Persons and Foreign Investment Protection Act passed by the Bulgarian Parliament in January 1992. The Act creates favourable conditions for attracting foreign capital under simplified legal regulations and under the same terms as for Bulgarian persons and legal entities. It also establishes a legal framework for protection of foreign investments, placing strong emphasis on the significance and need for genuine and effective legal guarantees for the investment operations of foreigners in Bulgaria. Under the Act, any foreign person has the right to carry on business in Bulgaria and to acquire shares or interest in a commercial operation.

There are a number of clearly defined restrictions for foreign persons contained in the Act. One principal restriction is that a foreign person may acquire a right to ownership of buildings but not a right of ownership over land.

Foreign investment is defined as any investment made by a foreign person acting inter alia in a sole trader capacity or through a branch or by a partnership in which a foreign person holds an interest exceeding 50% of the entity.

TAXATION, ACCOUNTING AND AUDIT

The current taxation regime in Bulgaria is based on a 1950 law on personal income tax and a 1951 law on local taxes and duties, together with a 1989 decree on economic activity. Significant reform of the tax system is now under way. VAT and excise duties will be introduced and well as a profit tax law and income tax law.

It is intended to have all of these in force by end 1994.

Corporate tax, or profit tax as it is known in Bulgaria, was introduced in 1982. The basic annual corporate tax rate is 40%. This rate applies when the foreign participation is under 49%. Companies which have foreign participation exceeding 49% and having a minimum share capital of US$100,000 are taxed at 30%. The same rate is applied when annual profits are under Bgl 1m. Taxable profit is determined in the same way as for State and private enterprises on the basis of a revenue and expense statement.

Dividends and profits from shares in companies with foreign participation are subject to a withholding tax of 10%. Income of foreign persons such as receipt of interest, royalties, rents and dividends are subject to a withholding tax of 15%.

Turnover tax is the main indirect tax levied on the sale of goods and services. The main rate is 22% for most goods and services. A lower rate of 10% is applied to basic necessities such as food, childrens goods and medicines.

Bulgarian foreign persons are liable for personal income tax on incomes earned in Bulgaria. Personal income tax is progressive.

Bulgarian employers have to pay social security contributions for their Bulgarian employees. There are three rates: 35%, 45% and 55% dependent on job category. There is also an additional payment of 7% of Bulgarian employees remuneration for a special fund for the unemployed.

In companies with foreign participation, employers have to pay a social security contribution for their foreign employees at a rate of 20% of employee remuneration.

All enterprises in Bulgaria are required to keep financial records in accordance with the Accountancy Act. This came into force on 1 April 1991 and incorporates a national chart of accounts.

BANKING SYSTEM

The banking system is Bulgaria has a two tiered structure. On one tier is the Bulgarian National Bank, the State bank. The second tier consists of commercial banks. Banking reforms are underway, which aim to establish a financial credit system which operates on a completely commercial basis. Parliament has passed two laws for the reform of the banking system to facilitate this transformation.

APPENDIX II

BULGARIAN ELECTRONICS INDUSTRY

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In 1989 the Bulgarian electronics industry accounted for some 17% of Bulgaria's industrial production, employs about 100,000 people, and comprised a diverse range of products from computer equipment to consumer electronics and telecoms. There were some 130 companies in the industry. The industry has undergone significant change in recent years following the collapse of Comecon and CIS markets which has reduced the demand for products produced by many Bulgarian companies. Bulgaria was once the foremost supplier of electronic equipment to the former USSR. The combined turnover of the industry in 1991 was ECU 255.9m, principally computer equipment (ECU 106m) consumer electronics and components (ECU 48m) and telecommunications (ECU 72m). Military production (which represented a significant part of the overall industry) has been negatively affected following the changes in Eastern Europe.

The industry offers a broad range of products including:

- Computers: PCs, mini, micro and mainframe computers, disk drives, floppy discs, peripherals, disc packs, software application, cash registers.

- Telecommunications: Public and private switching equipment, radio stations, telephone sets, antennas, remote controllers.

- Components: Integrated circuits, silicon dials and transistors, printed circuit boards, optoelectronic devices, switches, capacitors, resistors and others.

- Consumer Electronics instruments: TV sets, audio equipment, video tapes, radio receivers, household appliances, electronic devices for other industries (automobile, textile, food processing, medicine)

The electronics industry is dependent on the import of raw materials, intermediate goods and on foreign technology. Given the rapid changes in technology, many companies have found that they do not have the equipment required to upgrade their

37