BULGARIA

A STRATEGIC BALANCE:
FDI AND IN-COUNTRY BUSINESS ALLIANCES

Sofía, Bulgaria – November 2003
According to Prof. Michael Porter the key for competitive success is the strategy. It means, "deliberately choosing a different set of activities to deliver a unique mix of value"\textsuperscript{1}.

Notwithstanding the national strategy-makers use various instruments in order to achieve better export performance; they tend to assign highest priority to foreign direct investments (FDI) as means for creating new export capacity and value-addition in the national export mix.

Competition for FDI is, however, intense and will become even more so if forecasts prove to be correct that FDI inflows will continue the current downward trend.

Of additional concern to strategy-makers in most countries in transition should be the fact that FDI inflows in the region are highly concentrated on a few of the larger “host” countries.

In this situation, “best practice” suggests that national strategy-makers should be looking to alternative means, other than FDI, to generate new export and competitive capacity.

**What are the alternatives?**

The classic Trade Promotion measures usually include provision of information, consultations, training in export marketing, organization of matching meetings, participation in business missions and trade fairs, financing and insurance of exports.

Along with the listed means the national strategy-makers should also consider promotion of export services (such as Tourism, ICT services, Logistics) or direct support of in-country business alliances.

**In focus: In-country alliances**

At present, insufficient attention is paid to the potential contribution such alliances can make to competitiveness and export performance. The unused potential has to be further developed.

The strategy-makers should shift the balance from promoting FDI to directly supporting in-country business alliances. They have to consider an integrated set of initiatives in order to establish the necessary environment for in-country business alliances to flourish.

While such alliances are, by definition, a private sector undertaking, it is imperative that the public sector is to act as the catalyst and that this role be reflected in the national strategy. The strategic emphasis should not simply be on promoting such commercial alliances, but on directly supporting them.

**The role of the state**

In the current context of globalization, financial liberalization and continuous technological change, SMEs can’t survive isolated; it is necessary to create a collaboration environment or context. This collaboration can be implemented by nets or vertical and horizontal integrations, on one side, and on the need for the state to focus on:

- Establishing regulatory and institutional frames, to regulate competence, provide juridical security, simplify and make transparent all document procedures and fiscal regime.

- Formulating, evaluating and actualizing norms, policies and programs oriented to improve entrepreneurial administration, emphasizing on the support on innovation and technological diffusion, which would lead to improvement on quality and competitiveness, thus promoting

the development of productive chains, fomenting associability and action coordination within the involved actors.

- Support the development of financial mechanisms oriented to meet the needs of the SMEs (regarding terms and costs), to allow a broader access to financing, in order to facilitate their processes of expansion and re-conversion. Also, facilitate the access to financing to entrepreneurs, as well as financing for research development in order to improve competitiveness and quality.

Types of in-country alliances

Taxonomy of alliances according to the type of integration:
- Regional
- Horizontal
- Vertical

- **Regional**
  “A cluster is a geographically proximate group of companies and associated institutions in a particular field, linked by commonalities and complementarities.”
  Generally, industrial clusters are designed to create production efficiency and commercial synergies. The promotion of clusters is a modality of local and territorial economic promotion, in a way that allows indirect measures for the institutional development.

- **Horizontal integration** - *Cooperation with other agents within the same context.*
  Enterprises, the management of which, is based on partnership, will be able, through specialization and cooperation, to accelerate their learning process, to reach scale economies and to focus on targets where they have bigger competitive advantages. Participation in consortia solve the problem of supply for raw materials, as well as other supplies, along with company improvement policies, negotiating in block with financial institutions, thus obtaining more beneficial credits regarding terms and rates, and also negotiating with the state the definition of policies that improve their sector.

  However, the formation of these consortia requires overcoming the barrier of lack of confidence, self-sufficiency, individualism and the fear of being used by others.

  The horizontal cooperation within the SMEs or specialization will contribute to create collective efficiency, which is defined as competitive advantage derived from the local economies.

- **Vertical integration** - *Backward/Forward linkages between exporters and local suppliers of materials, components and value-added services.*
  Through vertical integration it is possible to increase competitiveness of the SMEs if access to certain critical resources is guaranteed, such as information, financing, technology and managerial capacity.

Taxonomy of alliances according to the field of cooperation:
- The **R&D alliances** as general include entrepreneurial and innovation partnerships between SMEs, universities and research institutes, and export-oriented firms.
- The **Production alliances** aim process improvements, better quality control, cost reduction, and appropriate packaging.

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- The **Marketing alliances** often include cost share for marketing analyses, common promotion activities, distribution and marketing of partners' products, franchising.
- The **Financial alliances** are designed to increase the readiness for meeting the new business opportunities or for managing commercial risks.

The taxonomy of alliances according to the companies' activities:

- **Industrial alliances** such as clusters within the sectors and between the sectors
- Examples for **agricultural alliances** are the export production villages and contract farming
- The **Services alliances** bring additional competitive advantages.
- **Export consortia** unify the efforts of exporters usually through better logistics, cost reduction, risk share and beneficial financing. They broaden the export base and lead to new levels of international competitiveness.

**Bulgarian experience on creating exports capacity**

In 1998, a study on the competitiveness of the Bulgarian economy was conducted³. The diamond below shows the competitiveness factors structure of Bulgarian economy.

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³ Source: Bulgarian competitiveness exercise (BCE) website: [www.competitiveness.bg](http://www.competitiveness.bg), managed by MSI, JNA Associates funded by USAID
The strategy, structure, rivalry are assessed as neutral due to the lack of innovation, the low quality/price ratio, the existence of lobbying structures.

Notwithstanding of the prospect for growth, the demand is negative due to the lack of information, restricted incomes and delayed consumption.

The Clusters in 1998 were not developed. There were no significant regional, horizontal or vertical integrations, as well as coordination between sectors and public services.

The Factor Conditions are neutral because of the low productivity and the restricted access to capital.

In conclusion, the environment is not favorable for creating of export capacity. The Government had to develop a set of measures in order to support clusters and demand, as well as to achieve a more equitable balance between means in order to deliver a unique mix of value.

What initiatives were undertaken in order to improve the competitiveness of Bulgarian Economy?

Supporting Clusters
- Development of sector strategies for Bulgarian electrical engineering sector
- A joint initiative of business and politics for the development of the Bulgarian woodworking and furniture industry.
- Strategy for development of vine and wine sector.
- An analysis “State of the tourism in Bulgaria and major tasks for its development till 2005” is preparing by the Ministry of Economy.
- Creation of conditions for development of Cultural tourism (PHARE BG 0102.03, BG PHARE 0102.04), as well as the Eco tourism (PHARE BG 0202.02)
- Creation of conditions for agricultural alliances through EU SAPARD Program.

Increasing Demand
- Establishment of the Bulgarian Trade Promotion Agency in order to fill the information gap in demand and strengthening its capacity through EU PHARE Programmes BG 0002.01 and BG 0201.01.
- Decrease of the share of the grey economy and increase in disposable incomes through programs for better tax and social securities collection.

Improving Factor Conditions
- Launching a Governmental micro credit Program
- New insurance services provided by the Bulgarian Export Insurance Agency.
- Improved skills and productivity of the local workforce through EU PHARE 0102.05 “Initiatives on the labor market”
- Improved export skills through implementation of Bulgarian-Canadian training project

Government policy
- Improved Investment Strategy through adaptation of new act on investments with accent on stimulating local investments.
- Improved Institutional stability through several EU PHARE Programmes
- New generation of administrative services through accepting the concepts for one-stop shop and e-government and initiatives for its realization.
Strategy, Structure and Rivalry

- Enhanced structural reforms in the process of NATO and EU accession.
- Creation of conditions for production of qualitative Bulgarian products through EU PHARE BG-0004.01 Grant Scheme for Introduction of Quality Managements system (Quality Management, Equipment, Training)
- Development of a National Strategy on innovations by the Ministry of Economy
- Promotion of innovations through EU PHARE BG 0102.02 “Hi-technology business incubators in Areas of Industrial Decline”

The described initiatives trace the tendency toward improving Bulgarian competitiveness.

The next step

The major challenge for the national strategy-makers, in short-term, is the development of a National Export Promotion Strategy, including unique mix of means for creation of new export capacity and value-addition.

Conclusions

Firstly, the potential of in-country business alliances, as a mean for creation of export capacity, has to be further exploited. Their direct support complements the governmental policies on attracting FDI and promotion of Bulgarian goods and services thus leading the economy of new levels of international competitiveness.

Secondly, the state should develop a collaboration environment through establishment of regulatory and institutional frames; it should develop policies and programs oriented to improve the entrepreneurial administration, as well as promotion of innovations; it should also ensure access to financial resources.

Thirdly, initiatives launched by economies in transition to create new export capacity through in-country business alliances are suitable for application in other countries.