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STRATEGY FOR ACCELERATED ECONOMIC DEVELOPMENT OF BULGARIA BY 2020

SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

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For the full text of the study in Bulgarian (354 pages) as well as the expanded executive summary (55 pages) of the most important conclusions and recommendations in Bulgarian and in English please refer to the following addresses: www.iki.bas.bg/CVita/angelov/index.htm or http://www.wiiw.ac.at/balkan/news.html
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In this summary we present the most important conclusions and recommendations. For obvious reasons no room is devoted to argumentation here. It is in the main text. References and tables are not included either. The study comprises references to more than 400 publications in Bulgarian and other languages and 29 tables.

1. ACCELERATED DEVELOPMENT – SUBSTANCE, NECESSITY, SOURCES AND OBJECTIVES

The analysis provides a foundation for the following most important conclusions and recommendations:

1.1. CONCLUSIONS OF GLOBAL AND REGIONAL IMPORTANCE

1.1.1. GLOBAL ECONOMIC DIVERGENCE

There is no unquestionable trend of sustainable global economic convergence. It is not evident even between the three main development centres – the US, Japan and the EU. The diverging level of developed and underdeveloped
countries creates the potential for the latter to develop more quickly and reduce the divergence with the more advanced ones. This opportunity can only be realised under a combination of appropriate economic and other conditions. Creating such prerequisites is difficult and is rarely achieved. Some western authors' claims that the average speed of convergence is two percentage points per annum are occasionally valid for some developed countries. Convergence is often slower or absent, particularly between developed and less developed economies.

Empirical proof does not confirm the hypothesis of global economic convergence implied in the neo-classical models. There is no clear-cut trend for more rapid development of the underdeveloped countries compared to the more developed ones. The trend is a growing divergence in the levels of productivity and GDP per capita. Even when the relative differences decrease, the absolute ones grow larger. The only important exception are some countries in East and Southeast Asia.

1.1.2. INCREASE OF SOCIAL POLARISATION

Accelerated economic growth goes along with an even more rapid increase of social polarisation. In 1960, per capita GDP in the 20 richest countries according to purchasing parity standards was 18 times higher than in the 20 poorest countries. By 2000 this spread was 40 times.

Rapid economic growth in itself is insufficient. It has to be for the benefit of as many people as possible on a global, regional, national and domestic scale. An increase of GDP can not be successful and sustainable if it is only for the benefit of a small minority. History has confirmed this on many occasions. This is relevant today too because regardless of the fact that history is never repeated in full, its main aspects often are.

1.1.3. “ECONOMIC MIRACLES” CAN'T BE REPRODUCED

Neither economic theory nor economic practices have discovered easy solutions and practical recipes for rapid economic convergence. Global experience proves that “economic miracles” are a result of a unique combination of country specific favourable conditions, aggressive economic, institutional, social and other policies, appropriate geographical location and a coincidence of circumstances in a specific historical context.

Progress in economic convergence is unique for any country. It is impossible to replicate it in other countries and times. “Economic miracles” can be explained post factum but they can not be reproduced. New “economic miracles” can benefit from the lessons of the preceding ones but they will always con-
tain unique innovative national elements. Otherwise they would never happen!
Each country that wants an “economic miracle” has to “make it happen”.

1.1.4. DEVELOPMENT AS A TRANSFORMATION OF SOCIETY

According to the modern paradigms development does not boil down to technical change – accumulation of physical and human capital, financial stability, higher labour productivity, competitiveness etc. As stated by J. Stiglitz, development means a transformation of society. The contemporary understanding of development does not assume development in general, but rather intensive, democratic, fair and sustainable development. Social innovation, however, should not destroy the inherited, centuries-old traditional cultural and other national values.

It is important to produce. Productive activities however must be carried out by healthy, highly skilled, free people who live in dignity and are capable of managing their own fate in an environment of personal security. People who know that in extremely unfavourable situations they can rely on the help of the community, of the society represented by the state. These people must live in an environment of openness, transparency, partnership and personal commitment to shared ideals and take part in decision making on personal and public affairs.

Development as transformation requires something more than appropriate economic policy and efficient institutions. The new theories of development as a transformation of society along with the institutions stress the importance of distribution. The problems of normal stratification or social polarisation are very important not only as development goals, but also as means for a more efficient performance of the economy. Poor people suffer not only because of a lack of means for their basic needs. They are powerless, helpless and insecure about themselves and their families. They are unwanted and rejected by society. Given such a social environment it is impossible to ensure a normal development of society, let alone any accelerated development!

1.1.5. INTEGRATION AND ECONOMIC CONVERGENCE

Theory is undecided as to whether integration always leads to economic convergence. This is apparent when the strictest assumptions of the neo-classical model are made more flexible, particularly the assumption that production technologies are identical and accessible to all countries. The poorly timed removal of capital and labour market barriers between developed and less developed countries can turn into a source of growing divergence. In some versions of the endogenous growth and integration models it can induce divergence between countries in terms of GDP per capita despite the fact that in principle it has a positive overall effect.
The experience of the less developed EU cohesion countries (Ireland, Spain, Portugal and Greece) proves that joining the European community did not result in automatic convergence. It is a possibility that can be used (Spain, Ireland and to a certain extent Portugal) or may not be used as in Greece. Its realisation presupposes the availability of a set of prerequisites – pro-active economic and other national policies of the member states is one of them. Even then convergence takes not years but decades.

Bulgarian accession to the EU will take place under more difficult conditions. First, Bulgaria is the least prepared of the applicant countries, which have joined the EU so far. Second, Bulgaria committed to a very high pre-accession price by closing four nuclear power reactors with a total capacity of 1760 megawatts. The losses and forgone benefits of this amount to several billions of US dollars. Third, Bulgaria will receive less EU transfers per capita than the cohesion countries did after their accession. Fourth, following accession Bulgaria will have to face strong competitive pressure on the single internal market, which did not exist when Ireland, Greece, Spain and Portugal joined. Fifth, Bulgaria will accede at a time when the EU will be struggling with the inevitable problems of the Eastern enlargement in 2004 in addition to the difficulties of its own internal reforms. Any decision of a group of member countries to move faster leading to a two-speed development of the EU would affect Bulgaria negatively. Sixth, Bulgarian society is not psychologically prepared for accession. Politicians are cultivating pre-accession illusions in the public, which will inevitably transform into post-accession disillusionment.

The above, however is not an argument against Bulgarian accession to the EU. For the simple reason that we don’t have a reasonable alternative. All other scenarios are either unrealistic or inferior to EU accession. Moreover, the medium and particularly long-term net effects of accession are positive for Bulgaria.

1.1.6. CONTROVERSIAL TRENDS IN CEECS

The trends in the CEECs have been controversial – both in the 40 years of centralised planning and in the 15 years of transformation. There is no trend of steady convergence. The trend is towards lagging behind the most developed countries, stagnation and internal divergence between the CEECs. Only some Central European Countries (CECs) are slowly converging with the developed economies of the EU-15. Bulgaria is lagging behind both the EU and the CE countries.

1.1.7. CONTROVERSIAL TRENDS IN REGIONAL CONVERGENCE

The trends in regional convergence are also controversial – in terms of both the average EU level and average EU member country levels. There is slow
regional convergence in the most developed countries but regional divergence continues in the less developed EU economies. There is great regional divergence in the CEECs, which has even been growing over the past 10-15 years. Macroeconomic convergence of the less developed countries with the average EU level continues along with an increase in the national regional divergence. The higher the GDP growth in a country, the higher its internal regional divergence. This has been the case over recent decades. It will persist in the coming decades.

1.2. CONCLUSIONS AND RECOMMENDATIONS OF NATIONAL (BULGARIAN) IMPORTANCE

1.2.1. COMPOUNDING OF FUNDAMENTAL PROCESSES

The compounding of several major processes and simultaneous resolution of several fundamental objectives in Bulgaria and in the countries of Southeastern Europe slowed down reforms. They impeded the resolution of all objectives – overcoming backwardness, carrying out market reforms and preparing for EU integration.

This all occurred against the harsh background of great losses and opportunity costs to Bulgaria resulting from the UN embargoes against Iraq and former Yugoslavia. In spite of the absence of ethnic or military conflicts in Bulgaria their presence in neighbouring countries shed insecurity over Bulgaria and created additional difficulties to transition and integration.

1.2.2. WRONG REFORM PHILOSOPHY

The International Financial Institutions applied wrong reform philosophy and standard schemes inappropriate to Bulgarian conditions. They pursued only the means of economic policy, such as low inflation, low fiscal deficits, stable exchange rate, etc. rather than fundamental objectives such as growth, employment, income, consumption, social justice, healthy environment, etc. The health, the education, the social justice and even the life of the people were sacrificed to the altar of financial stabilisation.

External and domestic reform designers imposed a forceful speedy privatisation at any price and tolerated crony privatisation. As a result very important portion of the newly created private sector is not a bearer of positive dynamism, entrepreneurship, innovation, respect of low and order. Such a private sector does not respect loyal competition and fundamental national interests. This makes Bulgarian private sector too different from the one existent
in the advanced market economies. Such private sector is not likely to contribute much to sustainable development.

The designers of reforms ignored the fact that there was no clear process of market transformation in Bulgaria. The latter had to be paired with overcoming economic, social, institutional and other backwardness.

In this complex setting the share of problems related to backwardness was smaller in Bulgaria compared to African and Asian countries and Albania but greater compared to the reforms in the Czech Republic, the Slovak Republic, Slovenia and Hungary. This was ignored when designing the reform models.

This made Bulgarian transformation more difficult and increased tremendously its social costs. Very large portion of the Bulgarian population lives now in great poverty, much larger than under central planning. The crime is flourishing. This is not what the people expected from transition.

1.2.3. FUNCTIONING AND COMPETITIVE MARKET ECONOMY

It is far too early to claim that there is a normally functioning market economy in Bulgaria! There are no real estate and capital markets, and the money, commodity and labour markets are in the initial phases of their development, which is accompanied by severe deformations and criminal deviations. Due to the low quality of reforms and crony privatisation Bulgaria has turned into an economic minefield. The mines explode any time when the interests of the respective economic groups are at stake. This will go on during the coming years and decades.

Bulgaria will not be able to develop a normally functioning and competitive market economy in the short and medium term. Competitiveness may become a reality only in the distant future - in 15-20 years. Normal relations between the economic agents are often replaced by criminal tools for “settling bills” - intimidation, blackmail, arson and assassinations. This creates a social, economic and psychological environment that will be counterproductive to normal economic activity for many years to come.

The choice is clear – initiate accelerated development on a playing field that has been cleared of crime and corruption or sustain economic and social stagnation in an environment of crime and corruption. Bulgarian authorities do not seem to understand that the country is at a crossroad.

1.2.4. TWO DEVELOPMENT ROUTES

Bulgaria can chose between two extreme routes of economic development until 2020 and by 2050:

- Lagging behind development of about 2% annual average GDP growth, or slow development of about 3%. Given PP standards, as well as expected average
annual EU-15 GDP growth of 2.0-2.5% the first scenario would result in 30-35% of the per capita GDP of EU-15 by the middle of the century, or 40-45% according to the second scenario. Bulgaria will be doomed to socio-economic stagnation with grave strategic consequences.

- Accelerated or rapid accelerated development of 5.0-7.0% average annual GDP growth. It is desirable to have average annual growth of 6-8% in the first ten years, 5-6% in the next decade, 4-5% in the subsequent decade and 3-3.5% beyond that. This development will not be smooth. From the point of view of economic convergence it is crucial to have Bulgarian average annual growth exceeding EU-15 growth 2.5-3.0 times. In this case Bulgaria will achieve a per capita GDP of 50-55% of the EU-15 level by 2020 and 75-80% by 2050. Such a favourable prospect is on the borderline between the possible and the impossible. It requires full mobilisation of national energy as well as favourable external conditions. World economic history proves that such a lucky combination is rare.

1.2.5. FUNCTIONS, COMPONENTS AND RESOURCES OF THE STRATEGY

The strategy for development of society has several major functions. They are: to define priorities; to co-ordinate; to contribute to attaining national consensus; to serve as a catalyst for overall social change; to be a carrier of transformation ideas, prompted by internal needs; to cultivate ownership; to provide cooperation between the state and the market.

The strategy must cover all components of society: development of the private and the public sector, of the regional communities, of the family, of the individual. The strategy should treat them as integral parts of society. It is impossible to achieve sustainable development unless it encompasses each of these components!

The strategy is a sound proposal only if backed with resources. They include physical, human and financial resources, efficient macro- and microeconomic management, increase of knowledge, sectoral, subsectoral, regional and other strategies as well as social and organisational capital.

1.2.6. FUNDAMENTAL PRIORITIES

The main task of the proposed strategy on priorities is to identify the areas of sustainable development and the economic, institutional, social and other policies to be activated by the state and society.

The proposed strategy identifies the following fundamental priority areas of sustainable development:

- improving healthcare and providing general access to health services;
- upgrading the quality, widening the scope and improving access to education;
- acquiring more state of the art knowledge leading to establishing a “knowledge based society”;
- promoting research and development;
- structural and technological upgrading of the economy;
- developing a modern infrastructure;
- balanced development of the regions;
- promoting income stratification but restricting social polarisation;
- mitigating the negative consequences of the demographic crisis;
- protection and improvement of the environment;
- creating modern public institutions and NGOs and an efficient administration.
- curtailing of crime and corruption

These general priorities are subject to specification by means of strategies and programmes at sectoral, subsectoral, regional and company level to make them operational. Companies must be free to develop their own strategies and priorities.

1.2.7. THE HUMAN BEING – THE MAJOR BENEFACtor OF THE STRATEGY

Setting objectives is central to any development strategy. The main objective of this strategy is the human being. Improving the quality of life is the major reason to devise a strategy and implement economic policies.

Upgrading the quality of life is the main criterion as to whether a strategy or an economic policy is sound. In the absence of improvement after an appropriate time lag the reasons should be sought in the design of the strategy and economic policy. Policy, which does not lead to better quality of life is not an appropriate one.

In a traditional strategy the only development objective is GDP growth. GDP, however, does not reflect sufficiently the quality of life of the people. It is a very important prerequisite for wellbeing but is not a reliable measure of it. Such a measure is the sustainable development indicator that covers economic, social and environmental dimensions. The economic, social and environmental objectives interact and enhance each other. This results in powerful synergies.

1.2.8. A SYSTEM OF DEVELOPMENT INDICATORS

Notwithstanding its shortcomings, GDP is a very important aggregate indicator for economic development. There is no better indicator for operational purposes. The attempts to construct an aggregate indicator for sustainable development have not been completed so far.
In order to compensate for the shortcomings of the GDP, we use a pyramid system of target indicators. GDP tops the pyramid. There are the four important aggregate objectives – economic development, social development, healthy environment and stable democracy in the middle layer. There are a large number of more concrete objectives that specify each of the four groups of aggregate objectives in the base of the pyramid. The political objectives are not covered in this strategy while the social and environmental ones - only partially.

1.2.9. ENDS AND MEANS OF ECONOMIC DEVELOPMENT

The main objective of the accelerated sustainable development is to improve the quality of people's lives measured with GDP per capita and the system of economic, social and environmental indicators.

The means for attaining strategic objectives are the monetary, fiscal and foreign economic policies, employment and income policies, structural, investment, science and technology, educational and health policies, demographic policy, infrastructure upgrading policy, etc.

In more specific terms, a low inflation, balanced budget, balanced current account, stable exchange rate, foreign exchange reserve, moderate indebtedness and others are important means of economic policies, not their objectives.

Maintaining low budget deficit or surplus (as it was in 2003) by reducing investment in infrastructure and expenditures for healthcare, education and research has a negative impact on growth in the medium and long term. This generates negative consequences for employment, income, consumption, healthcare, education, research and ultimately - for the quality of life! This may balance the budget in the short run but at a too high cost - an unhealthy and uneducated generation growing up in Bulgaria, as it is now the case! The health and education of the population have much higher value in ranking public objectives than a temporarily balanced budget!

In all CEE countries where the IMF has had stand-by agreements over the last decade the objectives of economic policies were confused with their means. Bulgarian governments shared the same philosophy of transformation. Confusing the ends with the means of economic policy leads to self-deception, slows transformation, makes it more expensive and has grave consequences for the life of the population.

1.2.10. ECONOMIC GROWTH SCENARIOS

We assume under the above-mentioned conditionalities that the per capita GDP is a very important aggregate indicator for economic development and, to
some extent, for the quality of people’s life. The standard of life depends to a great extent (but not fully) on the dynamics of growth of per capita GDP.

Six scenarios have been constructed for the average annual per capita GDP growth by 2020, and for the sake of reflection – until 2050. These are at GDP growth of 3%, 4%, 4.5%, 5.0%, 5.5% as well as a flexible realistic scenario (5.5%) until 2020, gradually falling to 3% over the period 2041-2050 (see chart).

We recommend the scenarios of 5.0-5.5% average annual growth by 2020 to the authorities. Given the same starting point of 2000 with an average annual growth of 5.0% (and for the EU-15 of 2.0% until 2010 and 2.5% for 2011-2020), in 2020 Bulgaria can reach approximately 50% of the expected per capita GDP level of EU-15. In the case of 5.5% average annual growth Bulgaria could reach about 55% of the expected level of this index for the EU-15. This is an immensely difficult task. It verges on the impossible but could be achieved with a full mobilisation of national energy and favourable external conditions.

The recent economic history of Bulgaria (1950-1990) shows that an average annual growth of 5.0-5.5% over a 20-year period is not inconceivable evaluated
in the light of the present criteria impacted by the deep crisis of transition. These comparisons, however, must be made carefully. There are differences in circumstances between the two periods that can impede the achievement of steady growth now. There are also differences in circumstances that can make it easier. It is difficult to say which of the two will prevail.

1.2.11. ECONOMIC TARGET INDICATORS

Setting the objectives based only on GDP growth implies a great risk of strategic mistakes. In order to compensate for the imperfection of GDP we recommend a system of economic and related target indicators and set their tentative numerical levels or trends until 2010 and 2020. They are:
- productivity and competitiveness,
- employment,
- income and consumption,
- education and training,
- digital literacy,
- mitigation of the demographic crisis,
- balanced regional development and local self-government,
- free migration and labour mobility.

We recommend several additional analytical target indicators for each of them and make quantitative and qualitative estimates for their levels and/or trends for the 2010 and 2020 horizon. Altogether 30 economic target indicators are used.

1.2.12. SOCIAL TARGET INDICATORS

To compensate for the imperfection of GDP we recommend a system of social and related target indicators with estimations until 2010 and 2020. They are:
- fair distribution and social cohesion,
- access to health service,
- social protection for the needy,
- protection of consumer rights,
- social inclusion,
- healthy working environment,
- high quality of labour and flexible professional careers,
- awareness and preparedness for transformations in the family and for the lifestyle changes.

For each of those that can be quantified we recommend several analytical target indicators and estimate their level and/or trends until 2010 and 2020. For the
rest we offer a description of the expected trends. Altogether 25 social and related target indicators are used.

Today only a society that provides prerequisites for its members to income based on merit is successful. The industrious and knowledgeable generate more wealth and must acquire more than the incompetent and passive. Each infringement of this fundamental principle suppresses the incentives for work, knowledge and entrepreneurship. Without these qualities society is doomed to stagnation and a fatal end. The normal social and economic development presumes moderate income stratification, but no income polarisation. Social polarisation makes accelerated economic development impossible whereas moderate social stratification boosts it.

1.2.13. ENVIRONMENTAL TARGET INDICATORS

Bearing in mind that the protection of the environment is the third major pillar of sustainable development we share some ideas and recommend target indicators. We define environmental efficiency and its importance and investigate the link between GDP growth on one side and use of raw materials, energy, water, transport services and harmful emissions – on the other.

We propose five groups of measures for de-coupling environmental pressures from economic growth. This will help easing environmental pressure while accelerating growth. Environmental resources are and in the forthcoming decades will become even scarcer production factor than the traditional resources – labour, capital and land.

This is even more indispensable considering that environmental degradation has reached a scale that endangers the future of mankind. The seemingly weaker pressure on the environment over recent years is mainly due to reduced economic activity, rather than owing to efficient environmental policy. Environmental pressures will grow again to dangerous levels in the coming years and decades with the expected revival of economic activity despite more up to date production patterns and technologies.

Bulgaria needs a long-term strategy for the protection of environment as an integral component of sustainable development.

1.2.14. LABOUR PARTICIPATION AND EMPLOYMENT

Labour activity and participation are changing slowly. Population decline will go on in the coming decades. The population in the active age will also decrease. Even in the case of stabilisation of labour participation the possibilities for GDP growth will be restricted under constant working time utilisation and labour productivity. In the case of a moderate decrease of labour participation,
the impact on potential economic growth will be even more negative. It will be compounded by the worsening age composition of the labour force.

Bulgaria can, however, increase significantly the number of the employed until 2020 and beyond by increasing the participation and the employment rates. This increase will be most significant in the first decade and in the first half of the second decade. It will decline towards the end of the second decade by reducing unemployment to normal levels. By the beginning of the third decade this potential will be exhausted and so will its favourable impact on economic growth. The negative impact of decreasing employment beyond that can only be compensated with better utilisation of working time and higher productivity. This can also be aided by immigration of work force.

By 2020 and in the decades thereafter there will be a great potential to increase the total number of worked man-hours. This growth potential will exist even under unchanged labour productivity. Considering that the latter will also grow Bulgaria will have significant economic growth potential in terms of available working time in days and hours per employed person although total number of employment will decline in subsequent decades. Using this potential will depend on the economic policy. The labour force will not be an obstacle for accelerated development in the coming decades despite the decrease in it’s size.

1.2.15. LABOUR PRODUCTIVITY

By 2020 and beyond Bulgaria will rely on a manifold increase of labour productivity as a major factor of socio-economic progress. Whereas total working time will grow in percentage terms, the increase of labour productivity will be manifold. If until 2020 per capita GDP grows by 5.5% per annum on average and if 60% of this growth is due to higher labour productivity, it would have to grow by 3.3% on average, and towards the end of the period - by 1.9 times. If productivity accounts for 70% of GDP growth on average for the entire period, until 2050 it can grow approximately 6 times compared to 2000.

Taking into account the demographic and migration prospects the major sources for extensive growth by means of the labour force will be “depleted” by 2025-2030. If the current demographic trends remain unchanged, the main and even single source for accelerated development in the coming decades will be the growing labour productivity. It will maintain its decisive role even in the case of a significant turn of the migration flows after 2020-2025. The return of some of the highly skilled emigrants may even speed up this process.

Various scenarios for substitution between labour and physical capital are possible. In the countries where labour costs are high there is a tendency to
replace labour with capital by rapid increases of the capital/labour ratio. There are no economic prerequisites in Bulgaria for fast substitution during the first and probably during the second decade due to the low cost of labour. With time labour cost will grow in parallel with labour quality and productivity, but they will hardly reach levels which will speed up labour’s substitution with physical capital by 2020. The process will become more apparent during the third decade and beyond. This will provide the technical and economic foundations for an even faster increase of labour productivity.

1.2.16. TOTAL FACTOR PRODUCTIVITY

Total factor productivity will play a growing role for maintaining accelerated growth in the first and even more so in the second decade and beyond. In the 5.5% annual GDP growth scenario until 2020, 30-40% thereof will be attributable to total factor productivity. This share will be 15-20% in the first decade, and 40-50% in the second. In the decades thereafter the share of total factor productivity can stabilise around 55-65%. The expected technological and other innovations and further deterioration of the demographic crisis can make a higher share of total factor productivity in GDP growth in certain periods possible or even indispensable.

Some believe that intensive growth will follow immediately under a high-tech oriented development, such as ICT, biotechnology etc., paired with non-technological elements.

This is a complicated process. A long period of economic maturing is necessary until the results of a modern economic development become effective. The so-called Paradox of Sollow is a good illustration.

This paradox, however, prompts an important conclusion for Bulgarian economic policy. Rapid changes are essential if 30-40 and more years are needed for tangible results to emerge after technological and other innovations were implemented. If this applies to the most developed countries, it is even more essential for a small and not well-organised economy like that of Bulgaria.

In order to gain time the technological, structural, institutional and other innovations in Bulgaria must start sooner and on a larger scale. The sooner the changes the sooner the results will become evident (after the essential lag). Unlike developed countries, Bulgaria can not reduce the time for economic maturing. It can, however, prolong it by delayed action. It does not seem that Bulgarian policy makers are aware of this.

Under current conditions Bulgaria will hardly have to wait for 30-40 years before the results of the technological innovations appear in the economic statistics. If we want these to transpire sooner, albeit marginally in the second and
third decade, and to have them feed through to accelerated development we must act now – in 2004-2007 - and on a larger scale in the following years.

2. RECOMMENDATIONS FOR ECONOMIC POLICIES TO ACHIEVE STRATEGIC OBJECTIVES

2.1. THE ROLE OF GOVERNMENT

Government’s main role is to provide an appropriate economic, institutional, social and political environment for business activities. The government should not be a business entity except in rare cases. It creates a healthy business climate by means of economic, institutional and other policies. It drafts the laws and sees to their unconditional enforcement. International experience has proven that no one performs these functions better than the government.

The government performs its functions in co-operation with the market and not in opposition to it. Their relations are complementary rather than substitutable. One must apply the constructive principle of “both government and market” instead of the naïve destructive schemes of “government or market”. This primitive construct has not functioned anywhere.

The government must provide equal conditions for the performance of both the private and public sector. They must operate in a competitive market environment and be equal before the law.

2.2. STRATEGIC PRIORITIES OF ECONOMIC POLICY

The traditional concept of “priority areas” in the strategies for economic development from the times of central planning was to outline directly or indirectly what, how, where and how much was to be produced and to whom and at what price it was to be delivered. The sectors, sub-sectors and products to be developed were specified in advance – in terms of volume, investment projects, technologies, employment etc. The time of such strategies has passed along with the rejection of central planning and the transition towards a market economy.

We do not share this concept of priorities. Neither do we agree with the current government intuitive choice of selected priority areas: new technologies, tourism, agriculture and infrastructure. These priorities are too general to be meaningful.

Priority areas of public policy include creating appropriate economic, institutional, social and other environment for entrepreneurship, research and development under clearly defined rules. These rules comprise fair competition, health
The formulation and implementation of development strategy with its priorities depends on the market and on the changes in the internal and external environment. Within this general framework market agents decide what, how much, how, where and when to produce, as well as to whom and how to sell, how to organise the production process and the relations between the business, social and other partners.

Specific strategies and priorities at sub-sector, company and product level must be devised by the businesses, while government should help in implementation by creating appropriate economic and institutional environment.

The government must monitor and interfere only with respect to compliance with the law. Effectiveness must be the concern of the business entities, which act on their own account and responsibility. They bear the full risk for their action or inaction.

The government can also initiate the formulation of specific priorities in the areas of science, research and development, healthcare, education, consumer protection, social inclusion, demographic issues, environment protection, infrastructure development, regional development, suppression of crime and corruption and others. It should discuss ideas with the businesses and other social partners, with academia, regional communities and NGOs.

The government must back its priority initiatives by providing appropriate economic and other environment for their implementation and in some cases even funding. Each level makes decisions on priorities independently by taking the overall government strategic framework into account. The respective parties should be free to deviate from government priorities at their own initiative and responsibility.

2.3. TRANSMISSION MECHANISMS FROM ECONOMIC POLICIES TO ECONOMIC GROWTH

One can assume that financial stability, technological and other innovations, skills and other factors have a positive impact on economic growth. This is beneficial, but insufficient. These causalities must be proven empirically as well. No such in-depth research has been conducted in Bulgaria so far largely due to unreliable and insufficient information.

The study comprises an attempt to model economic growth in Bulgaria and prove the existence of such causality. This problem, however, requires more empirical research to draw firm conclusions.

The solution lies in the use of evidence from other countries where such studies have been conducted. Provided that conditions in these countries are by
and large comparable to those in Bulgaria this would give grounds to expect that such causality may exist here. If certain cause and effect relationships are apparent in many countries, there will be reason to expect that they will apply to Bulgaria too even though their strength may not be the same. It is important that the dependent variable responds to the changes in the independent variable.

By means of such an analysis we identify a set of production factors that have strong enough impact on productivity and GDP. If the regression analysis proves the existence of a cause and effect link economic policy should focus on activating these production factors.

We consider the following dependent variables: GDP growth, labour productivity growth, total factor productivity growth, economic convergence. The following independent variables are used: investment, available physical and/or human capital stock, restructuring of the economy, R&D expenditures, public spending from the budget, taxation, inflation, financial development, openness of the national market, deregulation, competition etc.

The analysis gives grounds to assume that economic policy priorities for achieving accelerated development in Bulgaria over the coming decades can be as follows:

- macro-economic stability;
- regulation, deregulation, competition and entrepreneurship;
- openness of the economy towards global markets;
- investment in physical and human capital;
- high level of employment and utilisation of working time;
- appropriate income policy;
- tolerance of social divergence but not of social polarisation;
- mitigating the consequences of the demographic crisis;
- active innovation policy;
- break-through science and technology development (ICT, biotechnology etc.);
- updating of consumer and production patterns;
- financial system development and resource mobilisation;
- appropriate institutional policies;
- efficient environmental policies.

2.3.1. MACROECONOMIC STABILITY²

Macroeconomic stability implies stability of both the production and the financial systems. The stability of the production system is the core of the sta-

² Due to limited space only 7 out of 14 economic policy priorities are reviewed here briefly. For details see the extended summary in English on the web sites, cited at the beginning.
ability of the macroeconomic system. Financial stability is a function of the stability of production. A sustainable financial stability is impossible without sustainable growth. Of course the reverse is also true, but the productive macro- and microsystems and their stability lie at the root of the macroeconomic system and its stability. The cause-effect links between them are two-way, but the impulse from the production to the financial system is dominant.

The financial system ultimately serves the production of wealth and not vice versa. The fundamental goal of production is to meet the needs of the people.

In the coming 20 years Bulgaria should have a price policy that complies with at least three requirements: stability and predictability, an environment appropriate for growth and a gradual convergence to EU price levels. It is obvious that there will be high inflation according to the criteria of the neo-classicists and that this will have an impact on interest rates, income policy and the exchange rate. From this point of view the current low inflation is a defect of the system rather than indicator of long-term stability.

Evaluating the permissible inflation over the next 20 years, we need to take account that this will be a period of convergence to the EU on all important economic indicators including average price and income levels. At a projected average annual inflation in the EU of approximately 2% over the next decades, Bulgaria should allow for average annual inflation of between 8 and 10% to increase the domestic price level about 3 times over 15-20 years, i.e. to converge with the EU price level.

The economic policy of Bulgaria over the coming decades must strive for the lowest possible unemployment and lowest possible inflation. Ultimately a compromise is necessary instead of sacrificing employment for the sake of low inflation or vice versa. This conclusion is valid for Bulgaria and countries in similar conditions. The conditions in the developed European countries are somewhat different including the levels and the relations between inflation and unemployment.

We adhere to a more flexible perception of a balanced budget. This is a budget that is balanced over a longer horizon of 15-20 years with permissible annual deviations of up to ±2-3%. In years of economic decline a deficit of a couple of points is permissible whereas in years of high growth a surplus of a couple of points should be maintained. In extreme situations one can allow for higher deficits provided that non-inflationary financing is available and the public indebtedness does not grow to dangerous levels.

Budget policy must serve the attainment of fundamental national objectives. Bulgaria now prepares for EU accession being the least developed among applicant countries - lowest GDP per capita, lowest productivity and competi-
tiveness, lowest income level, highest unemployment, agonising healthcare, education and science systems, poorest infrastructure, poorest compliance with environmental, sanitary-hygienic and other accession standards. Closing part of the gap before and immediately after accession requires major investment effort by the Government and the private sector. This effort must be supported by the budget by way of a higher deficit for certain period of time.

We do not share the view of strictly balanced budget at any price and any time. Balanced budget is desirable as a means for achieving strategic objectives but strictly balanced budget each year is not the highest value to a society. Bulgaria was the only CEE country with budget surplus in 2003, but was the least prepared for EU accession.

The notion of a balanced current account should also be handled in a flexible manner. A deficit of 4-6% is acceptable in individual years. Deficits can be tolerated for a longer period when the main causes are the import of investment goods and/or other stable sources for compensation are available.

Maintaining a large current account deficit for a long time is dangerous, since it increases external indebtedness and destabilises the budget. This is especially relevant for Bulgaria because of the current high external indebtedness and the imminent large internal spending and imports in preparation for EU accession. One must explore a compromise between these in the name of accelerated growth.

The healthiest way of balancing the current account is boosting competitive exports. This in turn requires measures to upgrade competitiveness. This is the policy to be pursued in Bulgaria over the following years and decades. We do not share the present policy to balance the current account mainly through a strictly balanced budget.

The exchange rate will have an important role to play when making these hard decisions. Bulgaria already suffers from the exchange rate peg to the Euro (DM) introduced in July 1997. The pegged rate becomes particularly dangerous with an appreciating EURO, as has been the case lately. If appreciation goes on as it looks like losses will grow to a scale that can hardly be borne in the current state of the economy.

At first glance, losses due to the expensive BGN in the area of exports are balanced by the benefits in imports and external debt service. But the agents who export differ from both those who import and of the budget. The losses incurred by export manufacturers are not compensated to them by the benefits to the importers and to the budget and vice versa. Stagnation and even bankruptcies of exporting companies due to appreciating BGN will jeopardise future revenues to the budget and the current account and hence their stability.
If this persists, the expensive BGN can trigger bankruptcies of exporting companies, can destabilise the economy and suppress growth. This is the cost that Bulgaria is already paying for adhering to a pegged exchange rate. This may have severe consequences for businesses and consumers, for instance a shock immediately after accession.

The convergence of prices is related to the currency board arrangement with its inherent low inflation and fixed exchange rate, which make the convergence of Bulgarian prices and income to those in the EU impossible. Bulgarian politicians tend to disregard these problems in spite of the signals we have been conveying over the past years. The authorities are opting for a surprisingly short-sighted approach on such fundamental issues for the future of the nation. The longer the delay in tackling these issues, the more difficult and painful it will be to resolve them.

The fiscal and current account policy will determine debt policy to a great extent. The latter should be a policy of a moderate overall indebtedness. On the one hand, Bulgaria needs external investment loans and direct foreign investment for accelerated innovation of production capacities, of infrastructure, for the protection of environment and other areas of activity. On the other hand, one must take consideration of indebtedness. This necessitates looking for compromises, once again for the sake of accelerated growth.

The macroeconomic stability policy in the coming 20 years could be expressed in numerical terms. These are: average annual GDP growth of 5.0-5.5% (6-7% for the first decade), reducing unemployment to 4-6% by the end of the period, an average annual inflation of 8-10%, an average annual budget deficit of 1.5-2.0%, an average annual current account deficit of about 5%, total indebtedness of 50-65%.

2.3.2. COMPETITION AND TYPES OF PROPERTY

The fundamental principles of mainstream economics assume private property and competition as preconditions for sound economic performance. Neither of them existed in Bulgaria. They are in the process of being established. The emphasis is, however, confined to private property only.

Privatisation as the focus of transformation is being justified with motivation. Privatisation is claimed to be the only mechanism capable of inducing economic motivation for delivering efficient economic activity. This may be true for a small business but is not so for the medium size and large companies where the functions of ownership and management are split. Privatisation, therefore, is necessary but insufficient for creating an efficient motivational mechanism.
The managers act in a market environment where no one is interested in the specific institutional and corporate makeup of the company that has manufactured a commodity. Only price and quality matter to the buyer. They depend mainly on the competitive environment in which production and sales take place.

International practice offers thousands of examples of well managed state owned companies and of poorly managed private businesses. The reverse is equally true. Companies go into bankruptcy not because of the type of their ownership, but due to poor management. Naturally there is a correlation between the ownership (shareholders) and the quality of management. But such equally strong correlation exists between the competitive environment and quality of management. Even the best private company tends to abuse its monopoly status.

The relations between shareholders and managers of medium size and large companies and their ability to influence each other have always been complex. In the era of globalisation they are even more complex and the boundaries between them are indistinct. The importance of managers is increasing for the performance of companies in general and particularly of large corporations and multinationals.

The quality of management is impacted also by the pressure of stakeholders – the people working in the company, those living in the neighbourhood, the community, the trade unions, the budget as a tax collector and the social security system as a social security contributions collector. The suppliers of a company and other partners are also interested in its good performance and exercise constructive pressure on its management.

There are no simple, one-way and permanently valid relations in the modern economy. Private property is important, but it is no less important (and is becoming increasingly important) to have a competitive environment. Private property and competition have to complement rather than contradict each other. Relations between the two are relations of mutual complementarity and not of substitution. Competition is a powerful driving force of the modern economy, and so is private property. Splitting them and opposing one to the other impedes the normal functioning of the economy.

A private sector based economy can not develop without competition because private monopoly suffocates it. It “buys” governments and MPs, and sharpens social polarisation. International experience provides numerous examples of socio-economic stagnation and chronic political instability under a total dominance of the private sector but weak state and lack of competition such as in Central and Latin America, Africa and southern Asia.
2.3.3. HUMAN CAPITAL DEVELOPMENT POLICY

The economic and social convergence of Bulgaria to the EU is impossible without convergence of human capital in both quantitative and qualitative terms. Bulgaria can not prosper without a modern system of education. The authorities tend to neglect this obvious truth.

The participation of the state in maintaining the health, education and skills of the citizens is of fundamental importance for Bulgaria's development. The state should involve the private sector but these very important and delicate matters that go far beyond commercial interest can't be entrusted entirely to the private sector. Measures for health and education do not bring about results quickly and are largely outside the scope of the private enterprise.

Complex literacy is needed nowadays. This means reading and writing in the native language; solid foreign language skills; digital literacy, ability for individual and team work; analytical skills; communication skills; independence in learning and in life.

A fundamental concern of the state should be to secure access to healthcare and education for all citizens. Depriving the poor and their children of healthcare and education deprives the society of people who may prove to be great talents. And more importantly, it deprives many Bulgarians of a fundamental human right - the right to life, health and knowledge.

In the absence of state intervention, economic polarisation leads to social polarisation that nurtures educational polarisation. It intensifies digital divide, which in turn deepens social and economic polarisation.

Without state intervention and EU assistance the polarisation processes can become even more dangerous for Bulgaria due to the severe economic situation and the current state of education. The absence of measures in this area will make accelerated development impossible. Educational polarisation, coupled with deterioration of quality of education may have grave long-term consequences for the Bulgarian economy and the society at large.

The deepening educational polarisation and leaving the problem of complex literacy unresolved harbours the danger of leaving Bulgaria at the economic, social and intellectual periphery of Europe, as is the case nowadays. No accelerated development is possible in such an environment.

Education requires large resources - public and private financing, professional expertise, technical and other infrastructure, subsidies for the municipalities, support by the parents. The result depends on the size of the expenditures but also on their composition and management.
The strategy recommends that the expenditures of Bulgaria for education grow from 3.8% of GDP in 2000 to 6.5-7.5% in 2010 and 8-9% by 2020. The intention is that the cumulative education of the population within the 15 to 65 age bracket should grow from 8.4 years per capita in 2000 to 10 years in 2010 and 11.5 by 2020.

Financial allocations for education are very important but they should not be exaggerated. Larger public spending does not automatically lead to better quality of education. Prior to providing additional resources to the education system, it has to be rationalised. Only then will resources be used in an effective manner.

The larger part of education expenditures in Bulgaria is provided by the state. This is also the case in the EU countries. The dominant role of the state in this area must continue. This function can be performed in various ways. The most widely used is and will be the financing of public schools, which spend the funds according to certain rules.

Particular attention must be given to improvements in the quality of education, which is mediocre and deteriorating. The minds of Bulgarian students must become thinking machines and not depositories for facts, dates and numbers, which they may never need.

2.3.4. MITIGATING THE CONSEQUENCES OF THE DEMOGRAPHIC CRISIS

The demographic crisis in Bulgaria is deteriorating rapidly. It will be one of the most serious challenges in the coming decades. This crisis coincides and even exceeds similar problems in Western Europe in spite of an economic and social development, which lags that of Western Europe by 40-50 years. The current demographic problems in Western Europe are, according to claims of its analysts, the result of a demographic maturity. In Bulgaria they are the fallout of a state of crisis. Hence, we are decades behind in terms of social and economic development and decades ahead in terms of the manifestations of this crisis.

One must opt for a cautious increase in the retirement age. This requires early measures for improving living and working conditions, healthcare, lifelong learning measures and the transition to an “active old age”. Given the current difficult living and working conditions, increasing the pension age would be impossible since people at that age already suffer physiological and mental exhaustion.

These measures can be used for the 65+ age group to encourage them to stay on the labour market for longer. One can introduce further incentives and support in terms of gradual retirement from active labour activity by combining work with rest, a wider application of part-time employment, work from home,
consultancy over the Internet etc. This will be possible in the second, particularly in the third decade and beyond, when a significant growth of life expectancy and an overall improvement of the general health of the elderly are expected.

One of the consequences of the demographic crisis is the deterioration of the ratio between employed and unemployed. In this country it is one of the most unfavourable in Europe at approximately 0.8:1 (which also includes the people working in the shadow economy) and is deteriorating. In the EU countries the ratio between employed and unemployed is three times higher.

The composition of the employed and of the unemployed raises additional concerns. This is because the share of the young and the students is shrinking, the share of adults is growing and the share of the long-term unemployed is very high. The number of retirees in Bulgaria compared to the employed was 2.5-3.0 times higher than the EU average in 2000.

The ageing of the Bulgarian work force is becoming more and more apparent. In the future it will be accompanied with an upward movement of the retirement age. On the one hand, the share of the young people in the work force, the groups under 25 and fewer than 35 years will fall. On the other hand, the share of the working people between 55 and 64 years and above 64 will grow. Toward the end of the second and particularly in the 3rd and the 4th decade, with the expected increase of life expectancy (75—77 years for men and 80-82 for women) the share of the working people older than 65 will grow.

This sets new problems for Bulgaria. A mass introduction of the life-long learning will have to be accelerated, particularly for the work force of the middle aged and elderly generation. This is because the enhanced development of science and technology speeds up the ageing of knowledge. By 2015-2020 the major part of present knowledge of the work force will be obsolete. This fact speaks for the scale of the challenge. It will require radical changes in the education system and in training outside it. The life-long learning system will become increasingly important.

The ageing of the population is exerting stronger pressure on public finances. It will grow in the coming decades due to larger number of pensioners, larger average pension, additional costs of healthcare and other services for the elderly. We estimate that additional expenditure of 6.5-7.5 percentage points of GDP will be needed by 2020. This has to be added to the 8% registered in 2000. Judging by the experience of the EU member states the additional expenditures may be even higher than this estimate.

Stabilising public finances is also a priority task for Bulgaria against the background of the growing demographic pressure. This task will be very difficult considering the incredibly low level of pensions and the imperative need for
their increase. One could add to this the danger of shocks (bankruptcies and other collapses) in the private pension funds, the large public debt and the necessity for an active budget policy for EU accession. The expected burden of pension expenditures, about 13-15% of GDP by 2020, will be very severe indeed.

Gradual increases in the pension age must be prepared, which goes along with providing the option to continue work to all that chose to do so. This will be harder to apply while there is high unemployment, but will become essential after 2015-2020 when this problem will be resolved and the consequences of the demographic crisis become more severe.

No single measure can resolve the problem. The stability of the budget and of the social security system in the conditions of an ageing population can only be resolved by means of a complex set of interrelated measures. High growth will be central to this.

2.3.5. ALLEVIATING SOCIAL POLARISATION AND ALIENATION

Bulgaria has the highest social polarisation in CEE – a Gini coefficient of 0.41. It is higher only in the CIS countries.

No accelerated development is possible given such social polarisation. Successful development in a country of 7.8 million people is unthinkable when 2.5 million are doomed to severe poverty and are isolated from the benefits of human civilisation. This is not due to the state’s insufficient financial resources but mainly to the irrational in economic and social terms distribution of these resources. A small minority of 2-3% appropriates in criminal and semi-criminal ways a part of wealth that is much larger than their contribution to its generation and in doing so deprives the majority from their share. The government not only tolerates, but also by withholding active measures, contributes to the increase of income polarisation.

The state has ignored the poor and unemployed and has isolated them for more than a decade. They have responded with total alienation and growing hostility to the state and society. There can be no normal social and economic development and civil peace in such a society, let alone any accelerated sustainable development. World experience over the past century as well as the comparative analysis of the social and economic development of Africa and Southeast Asia over the past 50 years has proved this.

Alleviating social polarisation by means of changing distribution relations and inclusion of the alienated is one of the most important measures, which the Bulgarian government must address immediately. This, however, can not be done quickly because of the large scale of poverty and the weakened statehood.
Accelerated social and economic development implies encouraging income divergence, based on contribution by labour, capital and entrepreneurship of various groups, but restricting social polarisation.

2.3.6. ECONOMIC ASPECTS OF INNOVATION POLICY

Bulgaria’s internal innovation potential is restricted. It can provide no more than 10-15% of the core technological and other innovations it needs for economic and social development in the next two decades. The main source for technological and other innovations will be FDI, EU transfers, import of investment goods, projects and contacts with foreign experts, import of know-how, scholarships for Bulgarian scientists and other professionals abroad.

Bulgaria must be prepared. This calls for accelerated development of education, of applied sciences, of research and development, as well as first steps in marketing new technologies. Bulgaria will be unable to absorb, disseminate and use imported innovations without certain minimum of innovation potential. This will be the main role of Bulgarian innovation policy in the coming years and decades.

The state innovation policy can assist in establishing proactive innovation development in many areas: development of an appropriate set of economic incentives for innovation activity (subsidies, tax relief, etc.), developing research in public research institutes, establishments of higher education and subsidising research in private research establishments. The same applies to help increasing the efficiency and the scale of private investment in innovation, supporting effective working relations among the participants in the innovation system, simplifying regulation where necessary and maximising deregulation of everything else in innovation activities.

The establishment and development of hi-tech innovation enterprises and of small regional R&D facilities must be encouraged. The initiation of strategic alliances between Bulgarian high-tech innovation companies and foreign high-tech companies must be facilitated.

When providing subsidies for public and private innovation activity, one must seek appropriate trade-offs between government subsidies and company resources. This is particularly relevant for private innovation companies, so as not to crowd out private investment. One must target a ratio of financing sources that guarantees the complementarity of public and private investment which avoids their mutual substitution. Business practice in developed countries proves that the share of government investment should not exceed 25-30% of total investment in the respective innovation projects.

Public expenditures for innovations in Bulgaria will most probably prevail in the next 5-7 years while the share of private expenditures will grow. Judging by
the experience of developed countries, the two sources will reach equal shares by 2010 and by 2015-2020 private expenditure would account for 60-70% of the total.

Public funding will remain significant for a long time due to the weakness of private research facilities and their focus on highly profitable projects with short payback periods. Activities of longer-term significance, particularly those where private sector benefits are much lower than the public benefits should be funded by the state as they are not attractive to the private sector. Such projects are valuable to society and must be financed.

Innovation projects in the area of defence, healthcare, environment protection and fundamental research will be a prerogative of the state for many years to come for obvious reasons. The same applies to high-risk innovation investment. These can attract private resources but must be supported by state participation and/or state guarantees. If not, private capital will avoid high-risk projects.

Funding of innovation activities and particularly public funding is needed not only for direct technological and other solutions that lead to the creation of products of short and medium-term importance. It is even more important for Bulgaria's preparation to absorb and implement imported innovations and become a part of the international innovation networks. Countries with low innovation activity are not capable of understanding and using imported technical and other innovations. It is essential that Bulgaria does not remain a passive observer of the global innovation processes. To prevent this from happening we recommend a significant increase in research expenditures from 0.5% of GDP in 2000 to 1.4% in 2010 and 2.5% by 2020.

2.3.7. POLICY ON UPDATING OF PRODUCTION PATTERNS

Active intersectoral restructuring has been taking place in Bulgaria over the last 50 years. The share of agriculture has been declining in favour of industry and services. The share of industry first stabilised and over the past 10-15 years started declining in favour of services.

This process will go on in the next 20 years. The share of agriculture and forestry will decline to 5-7% of GDP and of the work force by 2020. This will lead to a significant increase of productivity in the economy as a whole and in agriculture but will make redundant the majority of the employed in agriculture with harsh social consequences. The process will be active until 2015-2020 and will then decelerate.

Industry (mining, processing, power generation, gas, water and construction) will continue to lose its share both in production and in employment, to reach 22-24% by 2020.
The services sector will develop fastest and will absorb the workforce released from agriculture and industry. It may account for 69-71% of GDP by 2020 and will have a similar share in employment.

The dynamics of production adjustment in the coming years will increasingly move from the intersectoral to the intrasectoral area. The structural changes within industry, services and agriculture will be the most intensive - sub-sectoral and product adjustments.

Nowadays Bulgaria produces and exports primitive low added value goods, which are capital intensive, energy intensive and unskilled labour intensive. Their content of skilled labour and high technology is very low. The share of high-tech products is insignificant. A very large part of Bulgarian exports (30-40%) consists of simple labour intensive goods of low added value, subcontracted by western companies to Bulgarian manufacturers - the so-called outsourcing. They are made with designs and materials of the customer using low cost labour and cheaper energy in Bulgaria.

As a future EU member Bulgaria must develop its sectoral, sub-sectoral and product profile. The question is whether the structural menu should be compiled based on the current sectors, sub-sectors and products with the respective comparative economic advantages. These sectors are low tech, resource intensive, energy intensive (with cheap energy) and labour intensive (with low salaries). In other words Bulgaria would confine itself to the framework of low-tech sectors and products. This may currently be an inevitable choice, due to the cheap energy and labour that generates some income, but will be wrong in the medium and particularly in the long-term.

Bulgaria has to make a great strategic move in the structural reorientation of its economy over the next 20 years. In view of the current and to a certain extent - the medium term realities Bulgaria will be forced to sustain its profile in low-tech operations by constantly renewing them with new products of medium, high and top level technology. The share of labour intensive low-tech goods can be reduced to some 15-20%, resource intensive low tech products - to 15-20%, medium level technology products should be increased to 40-45% and high-tech products to about 20-25% by 2020. This will be a very difficult structural transformation. It is, however, indispensable because no accelerated development is possible without it.

From the point of view of export efficiency, attention should be focused on producing more complex machines and installations, electromechanical and optical machines and installations, more complex transport machines and equipment, pharmaceuticals, ecologically clean agricultural products etc. Management of the companies will make the specific decisions on structural
readjustment. They have to formulate their priorities independently. Any attempt of public authorities to impose them would be inappropriate.

The existing energy sector development strategy must be revised. It is not based on an overall long-term strategy for Bulgarian economic development and, therefore, on an estimate for future domestic energy consumption. Energy saving policy in the consuming sectors has not been incorporated in this strategy. No reliable investigations have been conducted on the long-term electricity needs in the neighbouring countries.

The new energy strategy until 2020 must be based on a more economical use of energy in the business and the household sector, the development of gas distribution and supply, and environmentally appropriate methods of power generation. It is cheaper to focus on rationalising energy consumption rather than increasing power generation based on imported primary energy sources at unpredictable prices.

Major structural readjustment is needed in the service sector. It is insufficient to state that the share of services will grow at the expense of agriculture and industry. The type of services to be developed is more important. The rapid growth of security services (private bodyguard armies outnumbering state army and police by a factor of 2.0-2.5), the mushrooming parasite intermediary activities, the old-fashioned transport services, the abundance of primitive trade and restaurant services is a ground for concern. This is an evidence of the backward level of the services sector and unhealthy developments in the economy and society.

World experience demonstrates that it is more reasonable to develop modern services of the ICT-related type, modern healthcare, education, pre-school facilities and childcare. The same goes for research, other innovation activities, modern recreation facilities, services for the elderly, intensive tourism, financial intermediation, modern business services, protection of the environment etc. This is what the advanced European countries are doing.

There will be important adjustments with severe consequences in the geographic structure of business activities. As already stated, accelerated development will be the major focus for Bulgaria in the coming 20 years and beyond. High-speed growth can be generated in existing growth centres - mainly in regions and communities that offer favourable conditions - modern production capacities, telecommunications, transport, technical, social and other infrastructure, qualified personnel and market proximity.

The most intensive development in the coming years and decades will occur in the big cities - Sofia, Plovdiv, Varna, Bourgas, and other larger towns and will be least intensive in the small towns, in the villages, mountainous regions with poor infrastructure and human resources.
The internal regional divergence in Bulgaria will grow until 2020-2030. This is inevitable but policies can be initiated to mitigate the negative implications. This calls for partially compensating preventive measures by the authorities at both national and regional level. The Bulgarian public must be informed about this trend and be prepared to face the consequences!