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Acquisition into Bulgarian Insurance Market”

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**"If you don't know where you're going, you'll probably never get there."**  
*Aus Forrest Gump (1994)*

*To my family*



## **Introduction**

Since the fall of the Iron Curtain in the late 1980s there has been a measurable trend of expansion of the western companies toward Eastern Europe. The liberalization of the economy among the so called ex “Soviet Union countries” has opened their borders for new entrants, seeking new enticing markets.

The expanding companies have to know exactly where they are going and exactly what they are doing. Therefore, awareness of the specific market conditions, the legal framework and economic tendencies is crucial before a company undertakes a business activity outside its country of origin. This paper discusses the process of the choice of foreign entry according to the conditions of Bulgaria as an “emerging market”- a market with a huge growth potential. Other topics covered are the benefits for the newcomers as well as the most serious problems they have to deal with when entering Bulgaria.

In this context, this paper’s goal is to try to contribute to a better understanding of a special investment location- Bulgaria and a concrete market (the insurance sector) and to identify the main factors which have influenced the choice of foreign mode of entry and location.

It is well known that mergers and acquisitions have been the major route to internationalisation among many international, as well as many Austrian companies. In the last ten years, a great number of foreign banks and insurance companies have entered the Bulgarian financial sectors, most of them by acquiring or merging with local companies.

This master thesis tries to give insights into the general factors that affect the decision of foreign companies to enter the host’s country market, and to evaluate the specific investment climate in the case of Bulgaria.

The work is structured as follows:

Chapter 1 gives some information about the start of the globalization process and the current need for expansion, and sheds light on the reasons that push to internationalisation and the motives that drive the foreign entry decision.

The next section (chapter 2) includes the main definitions, classifications and types of the main foreign modes of entry. Mergers and acquisitions are discussed in details with special attention to the kinds of acquisition, the acquisition process and the due diligence. The differences between acquisition, Greenfield investment and Brownfield investment and the choice between them are also briefly explained.

Following this, chapter 3 pays special attention to the Dunning's Eclectic Theory, The Transaction Costs Theory, and Root's Factors which have influence on the choice of foreign entry mode as a corresponding theoretical background.

The purpose of chapter 4 is, first of all, to give some general information about Bulgaria, and, second, to give an overview of the main macroeconomic factors of the country and later on to focus on the main advantages and disadvantages of this investment location. When it comes to international expansion, it is not possible to miss out discussing Foreign Direct Investments, and for this reason attention is paid to the FDI in Bulgaria, especially to the Austrian investment performance in the country and the motives that drives the Austrian companies to invest there.

Chapter 5 presents the history and the development of the Bulgarian Insurance market for the period (1989-2009) and outlines the most important insurance companies, the gross premium income and the structure of premiums by classes (life, non-life and reinsurances).Chapter 6 two focuses on the legal framework for investments according to Bulgarian law and in particular to the requirements for Mergers and Acquisition.

The main aim of the case study - Vienna Insurance Group (chapter 7) - is to contribute to a better understanding (with help of various interviews) of the reasons and factors which have affected the choice of market entry mode and the motives for

this Austrian holding to expand internationally in Eastern Europe, and especially toward Bulgaria. The development of the business, the coordination between the central office and its subsidiary and how these companies survive and succeed nowadays are other topics that the case studies explore.

The eighth and final chapter presents the main findings and outlines a short conclusion of this master thesis.

Another topic for a further research could be how the Bulgarian insurance sector and the economy in general is affected by the foreign entry, and under what terms the current financial crisis affect the foreign performance in the insurance sector.





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## **1 The expansion strategy and its necessity in the global economy**

Over the last thirty years, more and more companies have expanded their business outside of their home country. The world is now called “the global village” and it is not unusual for people around the world to buy the same goods or use the same services despite great distances, to have the same needs, to speak more than one language and to have jobs which move them from country to country. Globalisation is increasing ever more in business society nowadays.

Moreover, the technological revolution, the development of certain communication-technologies, the travel possibilities offered by low tariff airlines and, not least, the internet, allow international companies to overcome some of the barriers which would otherwise hinder globalisation.

Franklin R. Root (1994) summarized 12 implications of the global economy which, seen from today’s perspective, turned out to be a very accurate forecast of what was to come. I would like to point out three of them:

1. “A new global economy is now emerging to confront business enterprises of the West with extraordinary threats to their survival, coupled with unprecedented opportunities for growth and profits. “
2. “Eastern European countries and China are now engaged in an unprecedented effort to transform their planned economies into market economies. This transformation process is generating many opportunities for Western firms, but the latter face several obstacles in exploiting them. “
3. “In the new global economy there is no place for companies to hide from foreign competitors. All companies need to plan for growth and survival in a world of global competition.”<sup>1</sup>

One of the most important decisions which companies have to make when expanding internationally is the selection of an entry mode and its implementation. Moreover,

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<sup>1</sup> Source: Franklin R. Root, p.(19-21), Entry strategies for international markets , 1994

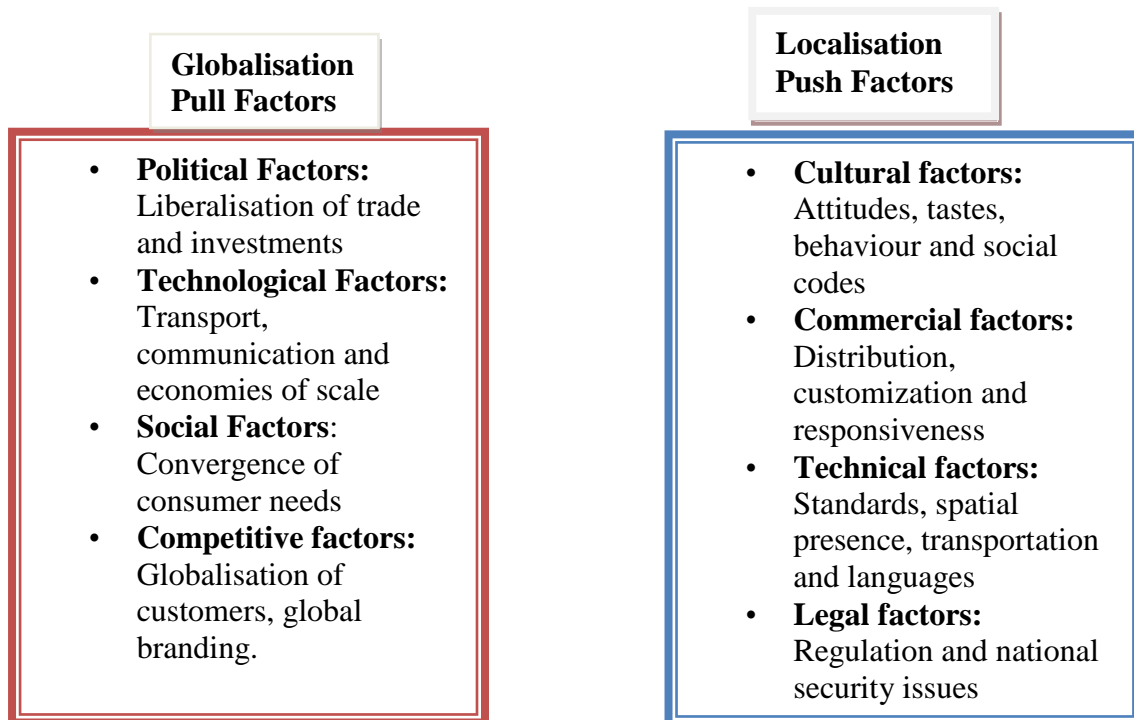
the identification of the most suitable global pathway could help to achieve success in business.

### 1.1. Factors pro and against globalisation

In the pertinent literature, I have found a combination of factors that should be considered in order to study the globalisation's forces.

I want to summarize the main arguments pro and against globalisation .These are presented in the following figure , the reasons pro globalisation or with other words the Globalisation pull factors are shown with the green arrow and on the opposite the red one shows the contra arguments or Localisation push factors.

Figure 1: Globalisation and Localisation push factors



Source: Lasserre Philippe, p. (16-24), Global strategic management, own creation

## **1.2. Reasons for internationalisation**

Mendenhall, Punnett and Ricks (1995) summarized two categories of reasons for expanding business internationally: reactive and proactive reasons.

According to these authors, the reactive reasons are those that are connected with factors outside the control of these companies which push toward internationalisation, despite the risks and costs being seen by the managers as too high. In stark contrast, the proactive reasons are those that are seen as an effort from the company to seek its competitive advantage.

In the following, these reasons with a short explanation for each of them are discussed. After this thesis is finished with the theoretical part, the case study on Vienna Insurance Group tries to answer the questions about the specific motives of internationalisation of that company and the special investment opportunities which Bulgaria offers.

### **1.2.1. Proactive Reasons**

The *variety and availability of resources* in other locations, in many different forms, such as financial, technological, natural or human form and the inability or inefficiency to take them home is another proactive reason for the companies to move and operate outside their country of origin.

The *lower costs* such as transportation, labour, etc, *the different corporate tax rates and tax systems and the encouragement of host governments* in the form of special benefits could be other competitive advantages for a company entering a foreign market.

The *economies of scale* and the *synergy effects* are other motives when talking about seeking new business locations. Economies of scale refer to a reduction in cost per unit which results from increased production, realized through operational efficiencies. The effects of economies of scale can be accomplished because as

production increases, the cost of each additional produced unit falls. Some companies cannot realize these effects at home, but they are possible internationally. The synergy is the magic force that allows cost efficiencies of the new business. In the case of expansion it could bring various benefits like improved market reach and better earnings, costs savings, revenue enhancement, distinguished know-how, technological advantage etc. (Mendenhall, Punnett, Ricks, 1995).

### **1.2.2. Reactive Reasons**

The main reactive reason for companies to go abroad is to remain or become more competitive. When the domestic market becomes smaller and saturated the need to expand arises very quickly and naturally. The fear of losing market share in their local market pushes managers to move, to internationalize and to “catch” the customers who need their products or services elsewhere in the world.

The home government regulations and restrictions may be the reason for some extra costs that could be avoided by changing location, making the company more competitive. The extended sales of seasonal products are another reactive motive for starting export, especially in the agriculture industry.

It is important to remember, however, that there are lots of barriers and unknown challenges which companies might face in an international context, hindering the process of foreign entry. For instance, the communication between people from different cultures, the specificity of the country’s resources or country’s development, the lack of foreign channels of distribution, the insufficient knowledge and many other critical factors.



### 1.3. The decision to go international

The process of making the decision of international expansion involves seeking a suitable destination, which means exploring the most adjustable regulatory, political and technological environment, and finding the competitive advantage for your business. The managers have to ask themselves questions about the capability of their company to deal with specific foreign risks and disadvantages, and not only to be aware of the benefits which might be available in the case of moving their business to a foreign country. The assessment of any specific firm's strengths and weaknesses is crucial within the decision making process. When a company is planning to expand its borders internationally, or globally, it is very important to develop exactly that strategy which corresponds best with the company's goals (both short and long-term). The availability and the assessment of company's resources has a vital importance in the process of foreign entry decision. For instance, the lack of personnel who speak foreign languages might not be so important in the host country, but it might be of critical importance in an international context.

"A strength at home may prove to be a weakness internationally, and vice versa."<sup>2</sup>

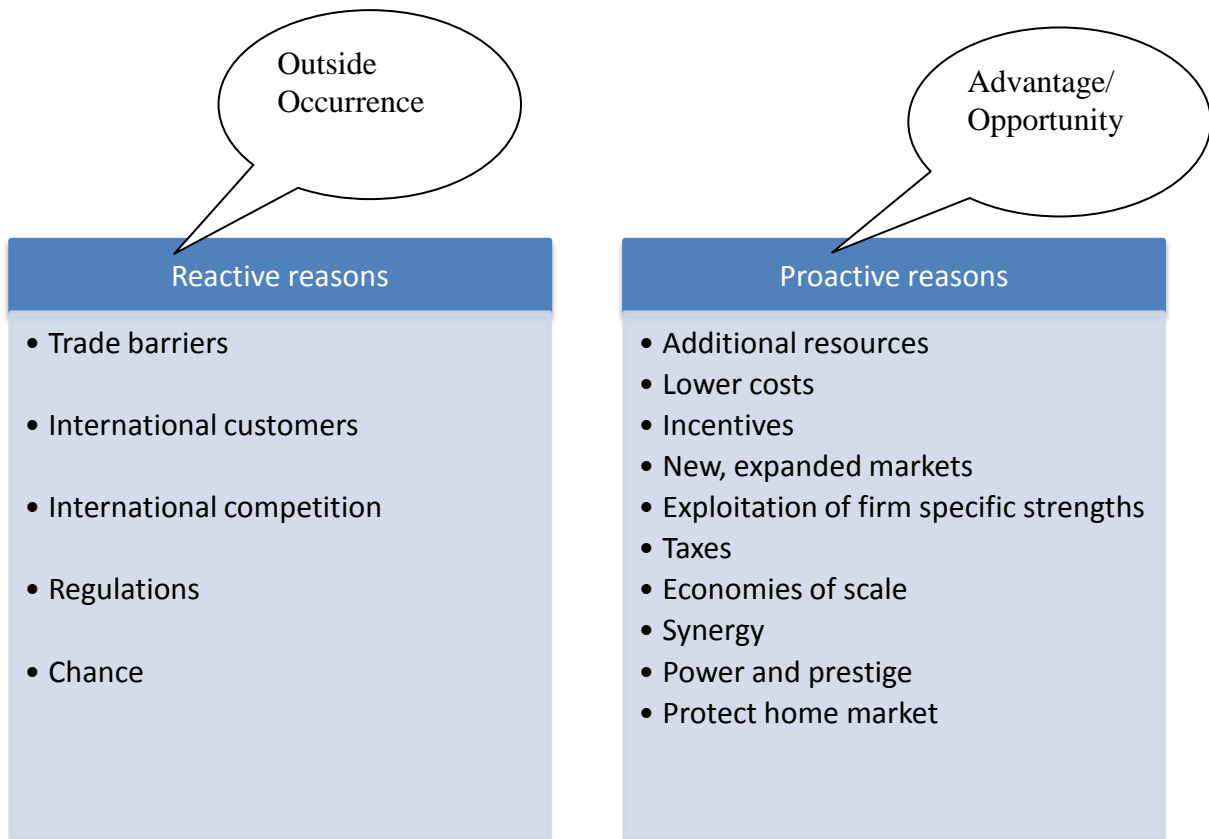
The conduction of case studies and the analysis of the experiences of other expanding companies could be very useful in helping to make the most appropriate choice of foreign entry.

Generally, there are two approaches to making the decision for foreign entry– based on experience or on analysis.

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<sup>2</sup> Source: Mendenhall, M., Punnett B.J., Ricks, D. , Global Management, p.228, 1995

**Figure 2: Reasons for internationalisation**



Source: Mendenhall, Punnett and Ricks, p.222-224, own creation

## **2 Foreign entry modes**

According to Franklin R. Root (1994), a multinational enterprise is a company that enters markets throughout the world by establishing its own sales and production subsidiaries in several countries, by using different entry modes, exercises control over its subsidiaries, and strives to design and execute corporate strategies in marketing, production, finance, and other functions from an international perspective that transcends national and regional boundaries.

Once the decision to go international has been taken, the managers have to turn their attention toward the realization and implementation of the made choice.

## 2.1. Classifications of foreign entry modes

The entry strategy consists of three different choices: what is the major reason for this entry/what the company wants to achieve or to gain, when to enter (timing strategy) and how to enter the foreign market/which legal form and kind of operations are available. According to corresponding literature, the major modes of foreign entry are imports and exports, licensing, joint ventures and ownership or direct investments. The last of these, direct investments, differentiate by various forms and degrees of control and ownership.

There are many different classifications of foreign entry modes. Philippe Lasserre defines two major dimensions which lead to the decision of one or other entry form:

“The ownership dimension: going it alone with wholly owned operations in which foreigner has full control and ownership or entering into partnerships” and “the investment intensity dimension: investing assets and competencies for value-adding activities or limiting operations to commercial, development and administrative activities “.<sup>3</sup>

Particularly interesting, in this context, is the following table of foreign entry classification:

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<sup>3</sup> Source Philippe Lasserre, Global Strategic Management, p.195, 2002

Figure 3: Foreign entry modes

**Ownership**

		Non or limited control	Full or absolute control
<b>Intensity of investment</b>	<b>High</b>	<ul style="list-style-type: none"> <li>• <b>Joint Venture with minority, equal or non – absolute position</b></li> <li>• <b>Consortium Partner</b></li> </ul>	<ul style="list-style-type: none"> <li>• <b>Wholly owned subsidiary By Greenfield investment</b></li> <li>• <b>Full or dominant acquisition</b></li> <li>• <b>Joint Venture with absolute majority (above 66%)</b></li> </ul>
	<b>Low</b>	<p style="text-align: center;"><b>Arm’s length agreements</b></p> <ul style="list-style-type: none"> <li>• <b>Distributor</b></li> <li>• <b>Licensing</b></li> <li>• <b>Agent</b></li> <li>• <b>Representative</b></li> <li>• <b>Franchisee</b></li> <li>• <b>Correspondent</b></li> </ul>	<ul style="list-style-type: none"> <li>• <b>Regional headquarters</b></li> <li>• <b>Marketing subsidiary</b></li> <li>• <b>Procurement office</b></li> <li>• <b>Representative office</b></li> <li>• <b>Technical observatory</b></li> </ul>

Source: Philippe Lassere, p.195, Global Strategic Managements, 2002

Beamish, P. (2003, p.3) includes the following entry modes:

- Exporting
- Licensing
- Joint Venture
- Establishing or acquiring wholly owned businesses outside the home country

Let us go on to give a definition of each form, and to explain its advantages and disadvantages.

### **2.1.1. Exporting**

When reviewing the relevant literature, we could state that most of the authors contemplate exporting as an alternative to other entry modes, e.g. FDI (Root 1987, Young 1989). Or with other words the decision between foreign entry modes is more seen as a choice between whether to serving foreign market by exporting or by FDI (greenfield or acquisition).

Hymer (1976) and Kindleberg (1969) highlighted the statement that a company has to own an unique advantage which will make it more competitive, and will help to overbear the costs connected with the international expansion. When comparing exporting to foreign direct investment we can say that if producing in the foreign country, the company could benefit from realizing savings of the transportation costs. On the other side a foreign entry through acquisition or greenfield causes additional costs such as communicating the technology, training foreign workers, acquiring local know-how etc. <sup>4</sup>

According to the “proximity-concentration trade off” (Helpmann, 1984, 1985), the companies are more likely to expand the production horizontally outside their country of origin if the costs of transportation, compared with the costs connected with the overbearing the barriers of internationalization and set up business abroad in a form of FDI are higher.

The problem is that when considering the bearing of different kind of costs (e.g. shipping costs, trade costs, fixed costs) on the choice between exporting and FDI-related entry modes a “perfect appraisal” would be hardly possible. These costs depend on a variety of market-specific and company-specific factors, such as the type of industry or the specificity of the host country which could not be taken accurately into account initially.

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<sup>4</sup> “Analyzing foreign market entry strategies: Extending the internalization approach” Peter J. Buckley, Mark Casson, *Journal of International Business Studies*, 29, 3, p 544,1998

In their paper "Export versus FDI with heterogeneous firms" Helpman , Melitz and Yeaple (2004) conclude that it is more likely to the most productive companies to choose investing in foreign markets, whereas the less productive companies often decide to export. Moreover according to their case study a within-sectoral heterogeneity plays an important role when discussing on export versus FDI.

The differentiation between direct and indirect export is "made on the basis of how the exporting firm carries out the transactions flow between itself and the importer or foreign buyer. The decision between the two forms involves determining the level of vertical control by the exporter. "<sup>5</sup>

When we talk about direct export, we mean the direct selling from the exporter (or manufacturer) to buyer (importer) located in a foreign country.

On the other hand, indirect exporting occurs when the exporting company sells its products to a partner, a middleman, which could even be located in the firm's home country and who is responsible for exporting and distributing these goods abroad. In this case the export risks are transferred to the partner.

Robin Jones (1997) states that direct export through a branch office or subsidiary company involves a greater degree of commitment and accompanying risk in a foreign market, but overcomes the potential problems of using foreign agents and distributors, and internalizes the "steam" of profit which would otherwise be paid to the external agents.

In general, compared to the Joint Venture and the FDI – related entry modes, exporting is connected with less risk for the multinational companies. Even if the resources to make an investment in the form of a subsidiary in a foreign country would be sufficient, both export forms allow the company to sell its goods abroad and to gain new customers internationally.

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<sup>5</sup> Source : Albaum, G., Duerr, E., Strandskov, J., International Marketing and Export Management, Pearson Education LTD, Edinburg, p.280, 2002

### **2.1.2. Transfer related entry modes**

Yadung Luo (2002), groups entry modes in two sets – transfer-related entry modes and FDI-related entry modes. His classification discussed entry modes that are associated with investment, rather than trade.

According to this author, the category of the transfer-related entry modes includes subcontracting; leasing, licensing, franchising and build operate transfer (BOT).

For all of these foreign entry forms, one party transfers some technology; know-how, assets or other resources to the other party of the contract for ownership or use, for fees or other resources.

When talking about subcontracting, we refer to a foreign company which provides its local partner only with raw materials, semi-produced goods and advanced technology for producing final products. The goods have to be finished in the host country by the local partner and finally to be bought for the company again, without change of ownerships of rights or property. The companies which use this entry form want to benefit from the low labour costs in other countries. The textile or shoe industries very often use subcontracting. Nike, Diesel, H&M and many other successful brands have their partners in China, Vietnam, Indonesia, Bangladesh, Turkey etc.

The clothes or shoes are produced in the local factories in the host countries, but the company monitor the process of production and the quality.

Licensing, franchising and agents and distributors are other modes of market entry through “arm’s length agreements” (Lasserre, Philippe, 2001).

According to this author these entry modes are chosen when one or more of the following characteristics are fulfilled: The country is too risky, the market is too small for company to realise an investment, there is already an investment near the country and no market niche, there are, legally speaking, no other forms of entry available or the company just wants to test the market.

In my opinion, the choice of the form of entry mode has to take every aspect of the company specifications and goals (long- and short-term) into consideration.

### **Licensing**

“International licensing is an entry mode in which a foreign licensor grants specified intangible property rights to the local licensee for a specified period of time in exchange for a royalty fee”.<sup>6</sup>

Licensing could be a particularly appropriate choice of foreign entry when the goods are costly to transport and the other forms such as exporting are inefficient, whereas the disadvantages are mostly seen in the loss of control of the property or the quality. The holder of the licence bears the full costs of settling the business into the foreign country.

Hence, “licensing permits the parent firm to expand very fast in an international market, without having to finance this growth itself”.<sup>7</sup>

On the other hand, Porter (1985) argues that licensing could be the right chosen entry mode only when a firm is unable to exploit the technology or market of itself.

### **Franchising**

Another main type of contractual agreement is international franchising.

“International franchising is an entry mode in which the foreign franchisor grants specified intangible property rights (trademark or brand name) to the local franchisee, who must abide by strict and detailed rules as to how it does business.”<sup>8</sup>

According to the literature, the enterprise must be able to offer unique products and services in order to succeed in franchising. Other conditions for being competitive with this entry mode are the high level of standardization and international recognition.

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<sup>6</sup> Yadong Luo, p.200, 2002

<sup>7</sup> Source: Robin John, Grazia Letto-Giles, Global business Strategy p.265, 1997

<sup>8</sup> Yadong Luo, p.201, 2002



Particularly between US companies, franchising is a very common entry strategy. Examples for such famous franchising companies are McDonalds, KFC, Coca Cola or Starbucks. A risk of damaging the brand name might occur if the franchisee is not quality conscious.

### **2.1.3. FDI-related entry modes**

“In entering foreign markets, firms progressively shift from exporting to higher forms of international operations such as foreign direct investments as they gradually accumulate and integrate the knowledge of foreign markets.”<sup>9</sup>

Especially when talking about the transition economies like Bulgaria, we can say that FDI's have a big impact on the country's economy, political conflicts, changes and economic growth. Moreover, FDI's are seen as an opportunity to access otherwise unavailable resources such as technology, management, a new business culture and a chance to attract more equity. The FDI-related entry modes are always connected with more difficult managerial efforts and entail the highest risk among the entry modes. The repatriation of the investment depends on many factors such as the stability of the local business environment, the awareness of the market, possible large cultural gaps between home and the host country and the existing competition.

That which makes the CEE countries such as Romania and Bulgaria particularly interesting for research, is the fact that they obtain additional portions of the FDI flows during the period of transition (Julia Djarova, 2004).

“The world is confronted with considerable differences in wealth between countries. In Europe this disparity is particularly acute between the Western countries in one hand and the Central and Eastern European countries (CEECs) on the other.”

“Governments of host countries will make sure that they provide good conditions for foreign investors so as to enhance the growth of their economy”.<sup>10</sup>

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<sup>9</sup> Source: Zhao, Luo, Suh, Journal of Business Study, p.35, 2004

The companies that undertake a foreign direct investment expect to benefit by obtaining the local foreign government investment grants and reducing the costs of production. The major problem of a foreign entry by FDI is that it requires enormous capital investment and it is very important to choose the foreign entry mode which corresponds best with all the country specific factors like economic and political stability, considers the legal requirements and restrictions, and includes acknowledgement of taxation, wages and other costs.

## **2.2. Foreign direct investments**

### **2.2.1. Definitions in use**

Foreign direct investment is a complex phenomenon of the economy. Therefore it is very important to make their definition as clear as possible. Many definitions of FDI are in use; however the most common are the following:

According to OECD (Organisation for Economic Cooperation and Development), FDI reflects the objective of obtaining a lasting interest by a resident entity in one economy (“direct investor”)in an entity resident in an economy other than that of the investor (“ direct investment enterprise”).

And furthermore: “Direct investment involves both the initial transaction between two entities and all subsequent capital transactions between them and among affiliated enterprises both incorporated and unincorporated. “<sup>11</sup>

Another definition is given by the World Bank:

“Foreign direct investment, that establishes a lasting interest in or effective management control over an enterprise.FDI can include buying shares of an enterprise in another country, reinvesting earnings of a foreign-owned enterprise in

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<sup>10</sup> Source: Cross Border Investing, Julia Djarova, Foreword, The case of Central and Eastern Europe, 2004

<sup>11</sup> <http://www.oecd.org/dataoecd/10/16/> accessed on 29.01.2010

the country where it is located, and parent firms extending loans to their foreign affiliates.”<sup>12</sup>

According to IMF (International Monetary Fund), an investment is an FDI if it accounts for at least 10 % of the foreign firm’s voting stock of shares.

Czinkota, Ronkainen, Moffett defines FDI as the following:

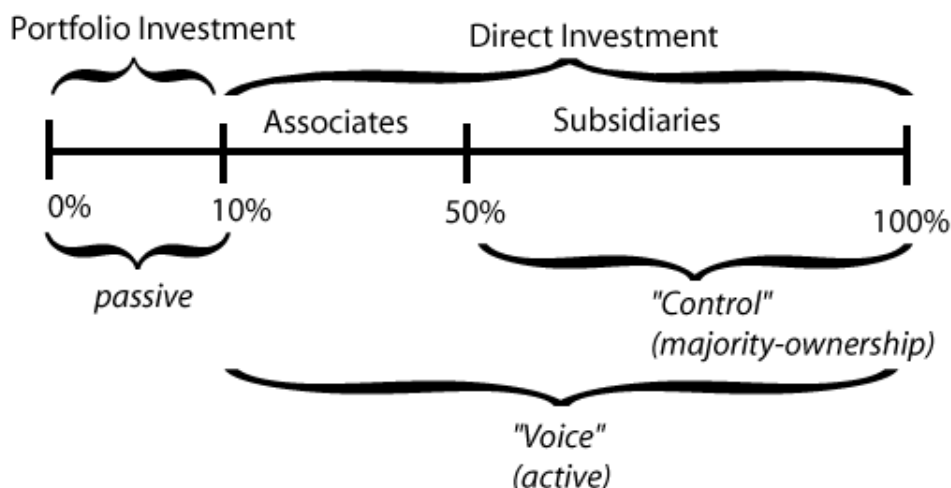
”Foreign direct investment represents one component of the international business flow and includes start-ups of new operations as well as purchases of more than 10 percent of existing companies .”<sup>13</sup>

### 2.2.2. Forms of Foreign Direct Investment

Once the decision of foreign entry through FDI has been taken, it is time for investors to choose between the available foreign direct investments forms.

First of all, when defining the forms of FDI, a distinction should be made between equity capital and reinvested earnings, or in other words between direct investment and portfolio investment .The following figure, adapted from Keith Head’s Elements of Multinational Strategy illustrates very well the controlling interest and the ownership of the firm’s equity.

Figure 4: Classification of Foreign Direct Investments (FDI)



Source: Keith Head, “Elements of Multinational Strategies”, p.5, Springer, 2007

<sup>12</sup> <http://www.worldbank.org/depweb/english/beyond/global/glossary.html>, accessed on 29.01.2010,

<sup>13</sup> Czinkota, Ronkainen, Moffet, International Business, p.397, 1999

According to this classification there are three types of international investment - branches, associates and subsidiaries. The **branches** refer to not separately incorporated units, in which equity capital is invested in foreign affiliates (Portfolio Investments) with less than 10% ownership of the company's shares.

In contrast the **associates** are separately incorporated entities in which the investing company owns from 10-50% of the equity. The firms that own at least 10 % or more have the privilege of an active voice. The **subsidiaries** are also separately incorporated, but in this case the parent firm possesses more than 50%, or in other words fulfill the necessarily requirement for controlling interest.

**Figure 5: Forms of Foreign Direct Investment**

	Partially owned	Wholly owned
<i>Existing business</i>	Capital Participation	Acquisition
<i>New Business</i>	Joint Venture	Greenfield

**Source: International Management, Beamish, Morrison, Rosenzweig, Inkpen, p.6.**

The authors considered that each of these different forms of foreign investment has profit.

### **2.2.3. Joint Ventures**

Doole and Lowe (2001, p.248) consider that the higher level of control is connected with higher potential risk, usually due to highest costs of investments. Partnerships like joint ventures and strategic alliances could offer the company a way to achieve a higher level of control at a lower level of risk. The speed of entry in a foreign country could be a benefit for the company when choosing to enter through joint venture.

Other advantages are the allocation of risk on the one hand and the combination of know-how, resources, labour forces, power, capital etc. on the other hand.

Contrary to this, the disadvantages are mostly seen in the complicated partner selection, the higher managerial complexity and the difficulties in the exercise of control.

Furthermore, Porter states that:

“Entry through internal development involves the creation of a new business entity in an industry including new production capacity, distribution relationships, sales force, and so on. Joint ventures raise essentially the same economic issues because they are also newly started entities, although they create complicated questions about the division of efforts among the partners and who has effective control”.<sup>14</sup>

The complexity in the culture and social differentiations between home and host country are other common hurdles in joint ventures. Hence, it is vital for the partnership to clearly define the separation of responsibility contractually.

### **2.2.4. Mergers and Acquisitions**

Merger and acquisition activities between companies have become common place in today's business life, a phenomenon which indicates changes in the control of a company.

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<sup>14</sup> Porter , p.340, Competitive Strategy, 1990

The differentiation between acquisition by takeover and merger is that as a takeover we describe a process when one organization attempts to take control of another. On the contrary, referring to mergers, we are talking about two organizations which form a single new entity.

Porter states that entry through acquisition is subject to a completely different analytical framework than entry through internal development because acquisition does not add a new company to the industry in the direct sense (Porter, 1990, p.350).

When a company plans a takeover activity it has to choose between number of different types of acquisition strategies and to identify and evaluate among the available candidates.

### ***2.2.5. Types of Mergers & Acquisitions***

There are a number of classifications in the types of mergers and acquisitions. One of the possibilities to differentiate between them is suggested by Brealey and Myers, who have outlined the following categories:

#### **Horizontal M&A**

In the case of a horizontal acquisition/ merger two companies that are from the same industry combine. Usually the companies have similar product range and target market and for this reason this type of acquisition can be defined as quite safe.

#### **Vertical M&A**

This also occurs when the acquired and acquiring company are active in the same industry area and have very strong relationship between their suppliers and buyers. Usually the acquired company is a supplier or a buyer of the acquiring company. The Acquisition that Vienna Insurance Group undertakes in Bulgaria, which will be discussed separately in this paper, would fall under this type.

**Conglomerate M&A** take place when the merging companies are not a competitors and do not belong to the same business area, or in other words they do not have common buyer-supplier relationship.

**Concentric M&A** represent a transaction when the acquirer and the target company are in a business relationship because of common production process, technology or market.

**2.2.6. The Process of Acquisition**

There are three main stages when describing the acquisition: preparation, negotiation and integration. The preparation and negotiation are part of the pre-acquisition process and the integration of the two merging companies is the post-acquisition process or the phase of transition.

**Figure 6: The most important steps of the acquisition process briefly**

Defining criteria	Identifying Acquisition partner	Phases
<ul style="list-style-type: none"> <li>• Industry or industry segment</li> <li>• Method of distribution</li> <li>• Size</li> <li>• Geographic constraints</li> <li>• Competitive strengths</li> <li>• Importance of management continuation</li> <li>• Preferred form of consideration (cash, stock or other securities)</li> <li>• Price range including minimum and maximum price targets</li> <li>•</li> </ul>	<ul style="list-style-type: none"> <li>• Trade Association membership list</li> <li>• Trade publications</li> <li>• Industry experts</li> <li>• Government publications</li> <li>• The acquirer's employees</li> <li>• The public library</li> </ul>	<ul style="list-style-type: none"> <li>• Making effective contact with candidate</li> <li>• Structuring the deal</li> <li>• Performing due diligence</li> <li>• Integrating the newly acquired company into existing operations</li> </ul>

Source: own creation, in reference to Mergers&Acquisitions, Ernst Young, Back to the basic Techniques for the, 90'es, p.3-18, 1994

## **List of the minimum required information from the target company (Due Diligence)**

- ✓ Corporate documentation
- ✓ Stockholder information
- ✓ Comprehensive financial information and audited accounts
- ✓ Tax status
- ✓ Contracts and agreements
- ✓ Government regulations, including permits, licensing and investigations company, activities
- ✓ Any litigation
- ✓ Product and service evaluation, market share, inventory and major suppliers
- ✓ Marketing analysis and appraisal on competition
- ✓ Management structure and system
- ✓ Identification and evaluation on property and equipment
- ✓ Research and development benefits
- ✓ Other information that is relevant

**Source: Strategic Management applied to international, Roodney Howes, Josey, H.M.Tan, London Telford, p.74, 2003**

The detailed handling of an acquisition or merger is the first major task on the path to successful business. “The legal announcement of the marriage”, is a metaphor given by Catwright&Cooper (1996), an endorsement, whereby each party has certain expectations of the other.

### ***2.2.7. Greenfield Investment, Brownfield Investment and Acquisition .The choice between them.***

Bennett, R. and Blythe J, (2002,) write about the advantages of buying existing local companies outright, compared with the creation of entirely new business entities. The benefits are seen mostly in the immediate possession of skilled workforce, functioning administrative structure, existing and working channels of distribution and all the savings of expenditures and avoidance of delays connected with starting businesses “from scratch”. Furthermore, the authors considered the difficulties in the integration of the acquired business into the organizational system of the local company. Some of these are the following:



- Control difficulties, connected with managing the arising large and diverse organization
- Sudden changes in the market conditions, after the expensive takeover
- Resignation of key employers after the acquisition
- Emerging new competitors

Investopedia defines a Greenfield investment as “a form of FDI where a parent company starts a new venture in a foreign country by constructing new operational facilities from the ground up. In addition to building new facilities, most parent companies also create new long-term jobs in the foreign country by hiring new employees.”<sup>15</sup>

The main advantage of building a wholly-owned subsidiary (e.g. Greenfield investment) is that the company may have full control of its foreign operations. Another advantage is that the investing company do not need to seek the most appropriate partner for joint venture or acquisition target. On the contrary, the disadvantages are mostly seen in the slow entry, the need for a large amount of resources and the higher risk connected with the usual delays and expenses when entering through start-up.

According to the dictionary of Investopedia, a “brownfield investment” occurs: “when a company or government entity purchases or leases existing production facilities to launch a new production activity. This is one strategy used in foreign direct investment.”<sup>16</sup>

It is very likely, after undertaking an acquisition, that the new acquired company needs to be mainly restructured and reorganised in order to fit itself much better to the business culture of its new owner.

In their paper “Brownfield Entry in Emerging Markets”, Meyer, K and Estrin S., classify the case of extremely extensive restructuring of the new acquired company

<sup>15</sup> Source: <http://www.investopedia.com/terms/g/greenfield.asp>, accessed on 20.05.2010

<sup>16</sup> <http://www.investopedia.com/terms/b/brownfield.asp>

as a “brownfield investment”, a hybrid mode of entry, which possesses most of the characteristics of the “greenfield investment” indeed. The authors also state that in fact, especially when talking about emerging markets (one of which of Bulgaria is), by most of the takeover-cases the resources transferred by the investor usually dominate over those provided by the acquired company. (Meyer, K., Estrin S., 2001)

The analysis of the casework, built on both transaction-cost theory and resource-based theory, have found that among the CEE emerging markets many investments which pretend to be acquisitions,” in fact resemble greenfield projects. In such “brownfield” cases, the foreign investor initially acquires a local firm but almost completely replaces plant and equipment, labour and product line.

Moreover, greenfield and acquisition differ in the origin of the resources, involved in the new transaction.

“Whereas a greenfield uses the resources of the investor and combines them with assets acquired on local markets, an acquisition uses primarily assets of a local firm and combines them with the investor’s resources, notably managerial capabilities.”<sup>17</sup>

Especially among the cases of acquisition of companies which had belong to the former Soviet Union-countries, or the so named “transition economies”, the lack of information, or the imperfect information during the pre-acquisition phase often might lead to unpleasant surprises in the post -and integration process and sometimes even to their failure.

Another question, concerning the phase of integration and adaptation of an acquisition is how well the new affiliate fit into the organizational culture of the investing company. Furthermore it depends additional on how great is the cultural distance between the two countries of origin of the companies.

Later on the interviews taken for the purpose of the case study about Vienna Insurance Group will give examples of such cultural differences in business context between the employees of the affiliates in Bulgaria and the expatriates delegated from the Headquarter in Austria.

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<sup>17</sup> Source : Meyer, K., Estrin S, p.576, Journal of International Studies,2001

According to UNCTAD Investing Report (Source UNCTAD WIR 2000), in some cases, especially at the time of entry, short-term Greenfield investments are better than M&A. However, in long-term investments many differences between the two types of investments diminish or even disappear.

Both M&A and greenfield FDI transfer foreign capital to the country .However when talking about the composition of personnel, a greenfield creates its totally new employment at the time of entry. On the contrary, acquisitions, may lead to lay-offs from existing employment, but it is also possible to generate new work places in the host country. There is also a trend that usually M&A are the chosen mode of entry when undertaking a production investment, whereas Greenfield investment is much more preferred when setting up new technologies or completely new, none or underdeveloped business services. The reasons about that are mostly seen in the costs of international relocation of resources from one side, and the more difficult integration process, which typically accompanies the post-acquisition phase from other side.

Another issue, when discussing on multinational companies(MNC), is the need of expatriates who are dispatched direct by the headquarter to their subsidiaries and the costs for their assignment, including training programs, replacement, compensations, family housing and living, costs necessary for overcoming cultural shock and different surrounding, etc. The delegation of expatriates is an essential step in order to administrate additional direct control over the subsidiary locally.

Moreover, Madhok(1997) argues that the success at the local markets depends strongly on the ability of the companies to transfer their know-how to the local market, but also on the ability of the local partner to absorb that know-how.

### **3. Theories on the choice of foreign entry mode**

#### **3.1. Eclectic Theory (OLI –Ownership, Location, Internalisation– Paradigm)**

In his dissertation Hymer S. (1960) initially contributed to a better understanding on FDI and on MNC and their operations of transferring knowledge, technology and other recourses and assets among their different countries of business activities.

Later on, Dunning introduced his Eclectic Theory in 1977 and developed it more by himself in 1980, 1988, 1995, 1998, and 2000. The studies have given great insights into explaining FDI determinants and international production. According to his approach, there are three important criteria which are essential when a company decide to undertake FDI. These are:

**Ownership advantages** require that a company have to possess ownership (unique specific advantage) that overbears the disadvantages of the competition with foreign firms. This firm-specific advantage might be a product, know-how or a special process of production which is available only to the home company, (patent or property right including). Or with other words the competitiveness of a company acting in a foreign market depends on its asset power (on the possession of all kind of resources).

**Location advantages** which consist not only of resource endowments but also of social and political factors, and allow the company to benefit from different resources, institutions and regulations in the host country and which affect the costs and the earnings of the company.

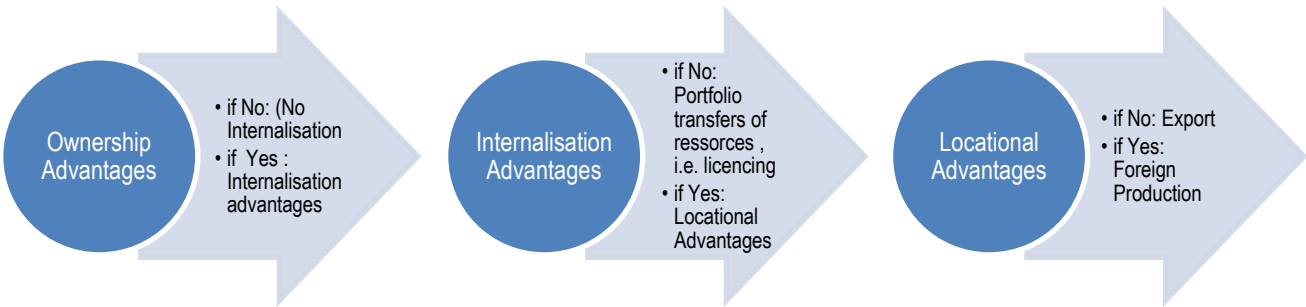
“The direct effect of high market potential indicates a choice of investment modes, while low market potential indicates a choice of o entry. On the other hand the direct effect of high investment risk indicates a choice of investment modes. The combined effect of market potential and investment risk, therefore, for high/low combination should be an investment mode and for low/high combination should be no entry.”

Or the gaining of the benefits of international investment correlate positive with the market characteristics “size” and “growth” and depends on whether the company enters a low- or a high-potential country.<sup>18</sup>

**Internalisation advantages** assert that a company should be able to internalise and utilise these advantages. Or in other words, the company must profit more when undertaking a foreign activity, compared with the other arm’s length agreement alternatives such as franchising, licensing or hiring independent local firms to provide the same services.

Summarized, according to the Eclectic Theory we can state that the more OLI advantages the company has, the greater the capability of the company to implement an entry mode with a higher level of control, such as wholly-owned subsidiary. Another implication considered by some authors is that the lack of multinational experience of a company is more likely to lead to a choice of non-investment kind of entry mode. The next figure shows the effects of interrelationships among the independent factors ownership advantages (resources), location advantages and internalisation advantages.

**Figure 7: Meeting decision on for foreign market entry**



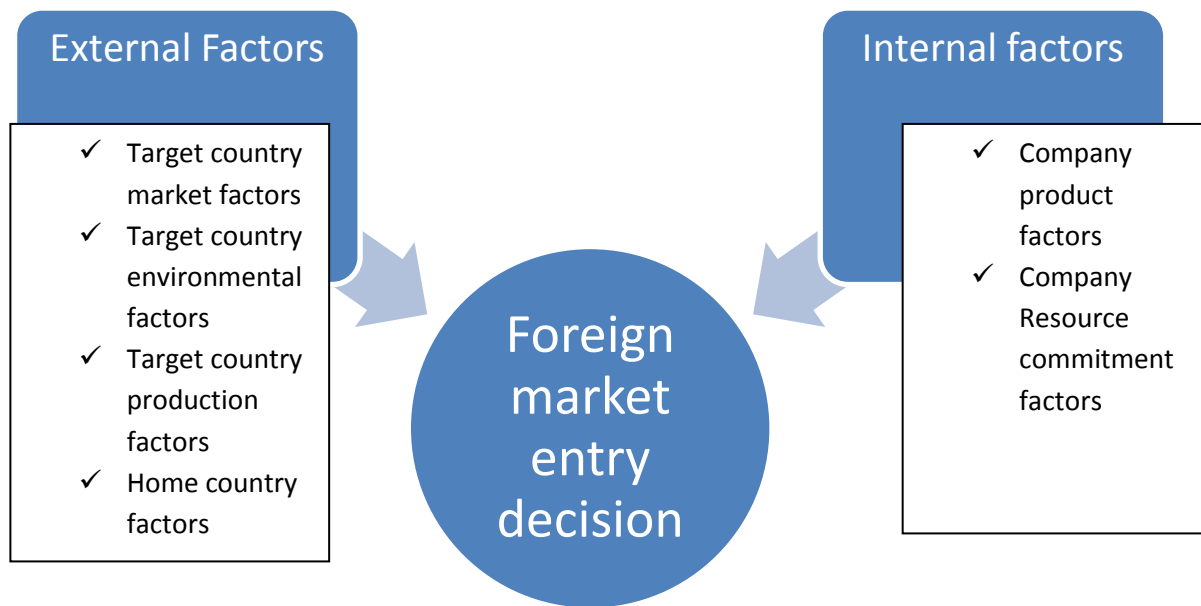
**Source: Based on Dunning and Michael Klug, market entry strategies in the Eastern Europe on the context of the European union, Dissertation, p.30, 2006**

<sup>18</sup> Source: Sanjeev, A., Sridhar, N., R. Choice on foreign market entry mode: Impact of Ownership, Location and Internalization factors, Journal of international Business Studies, Vol. 23, (1992), p.9

### 3.2. Factors influencing the choice of entry mode

Franklin R. Root (1994, p.28-35), suggests four external and two internal factors, which might have influence on the choice of foreign entry mode.

**Figure 8: Overview of the factors influencing the choice of entry mode**



**Source Root F., Entry strategies for international markets,p.29, 1994, own creation**

Other factors that shouldn't be underestimated are the geographical locations and the cultural differences.

Furthermore, the corresponding literature investigates the relation between international experience and the choice of entry mode heavily.

According to Davidson (1980), the companies tend to prefer selecting similar markets for their foreign entry initially, about which they have better information and which are "physically as well as psychologically close" to their country of origin in order to reduce the level of uncertainty. Or we can argue that the more the experience of company increases, the more its ability and confidence to enter far distanced and dissimilar (or geographical and cultural) foreign markets grows.

Some other studies have outlined the importance of the sequential foreign direct investment of a company, which could be very helpful in learning and gaining experience from early entries by the same company.

Chang and Rosenzweig (2001), argue that after a period of time during which the company gains local experience, recruits local employees, acquires knowledge about local way of doing business, it will be able to overbear the difficulties in communication due to cultural distance easier. Moreover the barriers and hurdles connected with the “foreignness” may diminish or disappear. The authors also suggest that when exploring the history of international expansion of a company, earlier entries, which are often motivated by a desire to exploit home-based advantages are most likely undertaken in a form of greenfield investment, whereas the subsequent entries, which are much more motivated by a desire to explore a host-country-specific advantage usually prefer to enter by acquisition or joint venture. Moreover their hypothesis which say that “subsequent entries by the firm will tend to use the same mode as used previously” and “subsequent entries in the same line of business will tend to use the same mode as used previously” were significantly proven by their study.(p.756, p. 769).<sup>19</sup>

In this context, the case study about Vienna Insurance Group included in this paper is also an example and proof for the influence and the importance of the international experience on the foreign entry decision.

### **3.3. Transaction Costs Theory (TCT) and the choice of foreign entry mode**

Anderson and Gatington (1986) were the first authors who connected the Transaction Costs Theory (TCT) with the choice of foreign entry mode in international context. The core point of the TCT is that the companies obtain different government forms which diminish the sum of the costs of transaction.

Williamson (1991) recommends the choice of an entry mode with a high degree of control and integration in a case of high external and internal uncertainty.

Furthermore, according to TCT, the “external uncertainty” (the inability of the company to predict the future), the “internal uncertainty” (international experience and

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<sup>19</sup> Source: Chang, S.J., Rosenzweig, P.M., The choice of foreign entry mode in sequential foreign direct investment, 2001, Strategic Management Journal, p.752

cultural distance), as well as the “asset specificity” and the “free-riding potential” will affect the choice of foreign entry mode.<sup>20</sup>

The conducted meta analytical review on the transaction cost determinants and the ownership-based entry mode choice, (2004), from Luo, Zhao and Suh, had confirmed that the TCE-related factors have great influence in affecting ownership-based entry mode choice. However the study also outlines that TCE is only one perspective, which contribute for a better understanding of entry mode decision. According to their findings, “the resource allocation in international expansion should consider not only transaction cost minimization (as documented by the importance of asset specificity and external uncertainty) but also resource exploitation in a promising location (as documented by the moderating effect of location and industry).”<sup>21</sup>

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<sup>20</sup> Source: Zhao, 2004, p.526

<sup>21</sup> Source : Zhao., Luo, Y., Suh, T. Journal of international Business Studies,Vol.35, Transaction Cost determinants and ownership-based entry mode choice: a meta analytical review, 2004, p.541



## 4. Foreign entry in Bulgaria

Figure 9: Geographical Map of Bulgaria



Source: <http://www.imotibg.com/en/bulgarian-property-news/about-bulgaria-general-information-location-climate-history-state-government-enno8363.html>

### 4.1. General information

Bulgaria is a country situated on the Balkan Peninsula, in South-eastern Europe, a region with a very important geographical position. The bordering countries are Greece and Turkey on the South, Serbia and Macedonia to the West, Romania to the North and The Black Sea to the East.

Bulgaria has a population of 7.8 million inhabitants, most of them living in the big cities. The capital of Bulgaria is Sofia with 1.2 million people. The other large, important towns are Plovdiv, Varna, Bourgas and Rouse. The area of the country is 110,910 km<sup>2</sup> and its total population according to the last census 7.7 million (at the end of 2008). The official language is Bulgarian and the alphabet is Cyrillic. The

traditional religion in Bulgaria is Eastern Orthodox Christianity (83%), but there are also Muslims (12%), Roman Catholics (3%), and Jewish people (3%).<sup>22</sup>

#### **4.1.1. A brief history**

Founded in 681, Bulgaria is one of the oldest European countries. The people who once inhabited this area on the crossroads between Asia and Europe were the Thracians, The Proto Bulgarians and Slavonic. In 865, the Slavonic Literacy was invented by the brothers Cyril and Methody. It became official by the time that Christianity was accepted as a religion for the Bulgarians. The Cyrillic alphabet was used later by many countries such as Russia and Serbia.

The 8<sup>th</sup> and the 9<sup>th</sup> centuries were called the Golden Age of Bulgaria because of the cultural prosperity and the enlargement of its territory. During the khans Krum (803-14), Boris (852-89) and especially Simeon (893-927) the Bulgarian kingdom reached its greatest size and power. It stretched across three seas – the Black Sea in the East, The Adriatic Sea in the west and the Aegean Sea in the south.

In 1018 Bulgaria was conquered by Byzantine. Despite a large number of battles, the occupation continued until 1186, when the boyar's brothers Asen and Peter drove the Byzantines out of Bulgaria. In 1839 Bulgaria became part of the Ottoman Empire and with thus began the most bloodiest and violent historical period in its history.

Throughout the 1800s, Ottoman authority in the Balkans had been breaking down. Bulgaria won its freedom with the War of Liberation (The Russian –Turkish War from 1879).

The new Bulgarian history began in 1878 (3.03.1878) with the treaty of San Stefano which restored the Bulgarian state. The 3th of March has been the national day of Bulgaria until today.

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<sup>22</sup>Source:[http://www.bulgariatravel.org/eng/view\\_rubric.php?r=abou&id=1](http://www.bulgariatravel.org/eng/view_rubric.php?r=abou&id=1),  
[http://europa.eu/abc/european\\_countries/eu\\_members/bulgaria/index\\_en.htm](http://europa.eu/abc/european_countries/eu_members/bulgaria/index_en.htm),  
accessed on 24.02.2010

In 1912 the Bulgarian Kniaz Ferdinand Sax Cobourg Gotha became a king of Bulgaria and proclaimed independence from the Ottoman Empire.

The First Balkan War (1912) was won by Bulgaria but the instability and weakness led to the Second Balkan War (1913). Bulgaria took part in The First and the Second World Wars on the side of the Central Power which led to a national catastrophe. The country lost a large part of its territory and had to pay reparations, which has weakened the economic stability.

The next largest historical period for the country started with the occupation of the Soviet Army, on 9 September 1944. The Bulgarian communist party came to power and continued to rule until 1989. The traditional trade with the West was cut and import and export were available only from and to The Soviet Union.

Since 10th of November, 1989 - Bulgaria has been a parliamentary republic. The head of the state is the President, Georgi Parvanov since Jan, 2002, the new Prime Minister is Boyko Borisov, since July, 2009 and the head of the state is the President. Since 2007 Bulgaria has been part of the European Union.<sup>23</sup>

#### **4.1.2. The Economy**

During the term of office of Todor Zhivkov (1950-1989) and the communist party the state was under conditions of command economy. The transition to a market oriented economy was a very hard political and economic process and in 1996-1997 Bulgaria was hit by a major crisis.

The state owned industries were mass privatized in the late 1996. In 1997, after an agreement with the World Bank and the International Monetary Fund a currency board was introduced. Its main goal is to support economic stabilisation and to carry out the economic reforms and changes in the country. Bulgarian local currency is Lev (BGN). Lev .BGN is pegged to the Euro at the rate of BGN 1 per EUR 0.51129.

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<sup>23</sup> Sources:

[http://www.bulgariatravel.org/eng/view\\_rubric.php?r=hist](http://www.bulgariatravel.org/eng/view_rubric.php?r=hist)

<http://www.investbg.government.bg/index.php?sid=16&ssid=42>

The economic turmoil in Bulgaria is addressed from three different perspectives: the historic roots of the crisis; the actual evolution of the fiscal, banking and currency crises, and the political economy of the transition in Bulgaria.

In the last 5 years Bulgaria has achieved good results in terms of macroeconomic stabilisation. The government has cut the corporate tax (2000), which is having positive influence on the flow of Foreign Direct Investments.

#### **4.2. Investment profile of Bulgaria .Emerging markets and transition economies**

According to Yadong Luo ( 2002, p.5) an emerging market is a country in which “its national economic grows rapidly , its industry is structurally changing, its market is promising but volatile, its regulatory framework favors economic liberalization and the adoption of a free market service , and its government is reducing bureaucratic and administrative control over business activities.”

Generally speaking, when determining the indicators of emerging markets we refer to GDP per capita, GDP growth rate, unemployment, inflation, corruption and other macroeconomic tools. Most commonly we can say that the developing countries or the transition economies that undertake significant structural, political, financial, legal and /or social reforms, and which have opened their borders for FDI, can be classified as emerging markets.

Bulgaria is a typical representation of a transition economy, shifting from a centrally planned system to a market-determined system.

Julia Djarova (Cross Border Investing, The case of central and Eastern Europe, 2004,) points out four effects and number of characteristics of the transition economies which are very important for foreign direct investments.

According to the author these are:

- ✓ irreversible economical growth
- ✓ wide scope transition covering governance and enterprise restructuring, price liberalization , introduction of trade and foreign exchange system and competition policy, banking reform an interest rate liberalization , establishment of the securities markets and non –bank financial institutions.
- ✓ privatization of a unprecedented scope and scale , including large and small scale privatization
- ✓ development of the business environment: private sector development, improved business and investment climate.

There are not only benefits for the new entrants , many risks such as government restrictions, lack of skilled labour forces, poor health system , insufficiently developed infrastructure ,a local way of doing business and the local culture are only a few among the variety of known (but sometimes unknown) barriers for the multinational companies entering the Bulgarian market.

Lasserre Philippe , states that” a country will be attractive for a foreign investor if in investing in that country, she/he gets a return that is equal to or higher than her/his risk-adjusted weighted cost of capital”.<sup>24</sup>

According to the author, the assessment of the country attractiveness involves the evaluation of various risks for both the shareholders and the employers with help of different approaches, which give the score or ranking of the studied country. The two big categories are market and industry opportunity and country risk.

#### **4.3. Country Risk, Credit rating and Competitiveness**

The country risk assessment is an approach which ranks the place of investment according to its financial, political, economic, structural and institutional obligations and presents the risk of the selected investment area. Worldwide, there are many recognized and commercial rating agencies dealing with the country risk. The three most important recognized credit rating and risk analysis agencies in the world are Moody's, Standard and Poor's and Fitch Ratings. Among the commercial and unofficial recognized providers of country risk appraisal the important names are these of Euromoney, Economist Intelligence Unit, Coface and the International Country Risk Guide.

The required statistical information was gathered from the following publications, year's Issues, institutions and internet sources in the period of November 2009 – August 2010 :

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<sup>24</sup> Philippe Lassere, p.161, Global Management, 2007

- Bulgarian Investment Agency (BIA )
- Bulgarian National Bank(BNB )
- Financial Supervision Commission( FSK)
- Bulgarian Privatisation Agency
- Bulgarian Ministry of Finance
- Bulgarian National Statistical Institute ( NSI )
- United nations conference on Trade and Development ( UNCTAD)
- EUROSTAT
- European Investment Bank ( EIB)
- Bulgarian Agency for Credit Rating ( BACRA)
- Bulgarian chamber of commerce and industry
  - [www.bcci.bg](http://www.bcci.bg)
- Coface
  - [www.coface.bg](http://www.coface.bg)
- <http://investbulgaria.com/BulgarianMacroeconomicInformation.php>

#### 4.3.1. Selected macroeconomic indicators

Figure 10: Major macroeconomic indicators

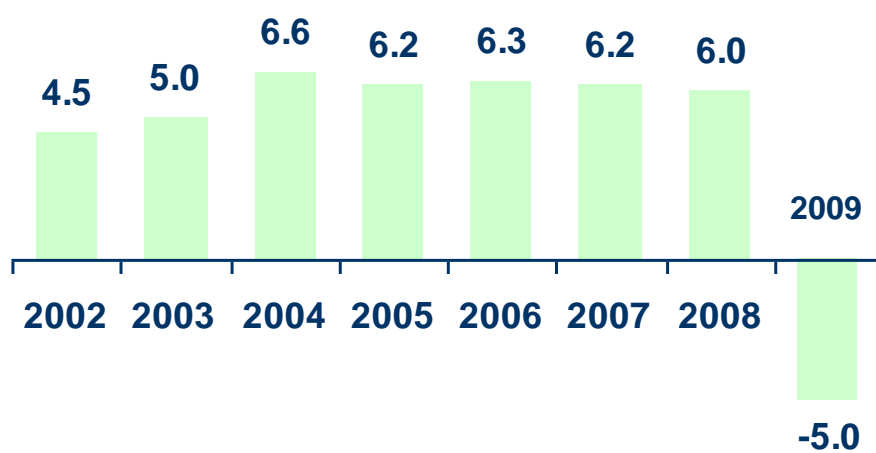
<b>MAJOR MACRO ECONOMIC INDICATORS</b>				
	<b>2007</b>	<b>2008</b>	<b>2009(e)</b>	<b>2010(f)</b>
<b>Economic growth (%)</b>	6.2	6.0	-5.3	1.0
<b>Public sector balance (%GDP)</b>	0.1	1.8	-1.5	0.1
<b>Current account balance (%GDP)</b>	-25.4	-25.2	-12.1	-9.9
<b>Foreign debt (%GDP)</b>	107.9	103.1	107.4	107.7
<b>Foreign exchange reserves (in months of imports)</b>	5.2	4.3	6.5	7.2

(e) estimate (f) forecast

Source:

[http://www.coface.com/CofacePortal/COM\\_en\\_EN/pages/home/risks\\_home/country\\_risks/country\\_file//Bulgaria?nodeUid=572094](http://www.coface.com/CofacePortal/COM_en_EN/pages/home/risks_home/country_risks/country_file//Bulgaria?nodeUid=572094), accessed on 19.04.2010

Figure 11: GDP real growth (%), 2002 – 2009



Source : Invest Bulgaria Agency , General presentation

Figure 12: Credit Rating Bulgaria

Agency	Date	Foreign currency			Local currency		
		Long-term	Short-term	Outlook	Long-term	Short-term	Outlook
Japan Credit Rating Agency	24 July 2009	BBB	-	Negative	BBB+	-	Negative
Fitch	30 April 2009	BBB-	F3	Negative	BBB	-	Stable
Standard& Poor's	1 Dec 2009	BBB	A-3	Stable	BBB	A-3	Stable
Moody's	20 January 2010	Baa3	-	Positive	Baa3	-	Positive

Source: adapted from Bulgarian Investment Agency, Brief Investment Handbook 2009, Publication

### 4.3.3. Foreign Trade

Figure 13: Export by commodity 2008 Figure 14: Export by country 2008

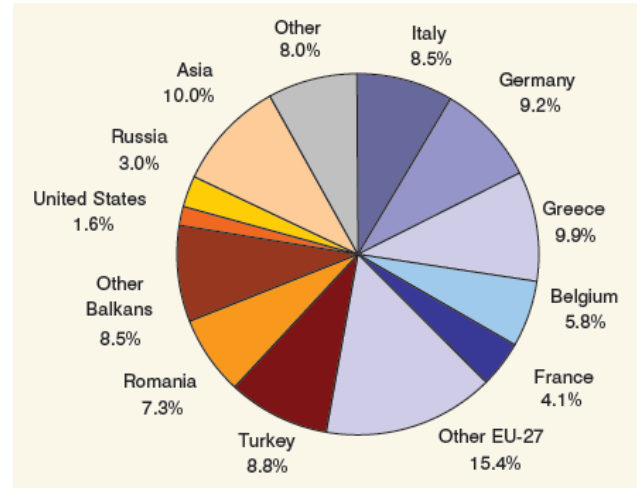
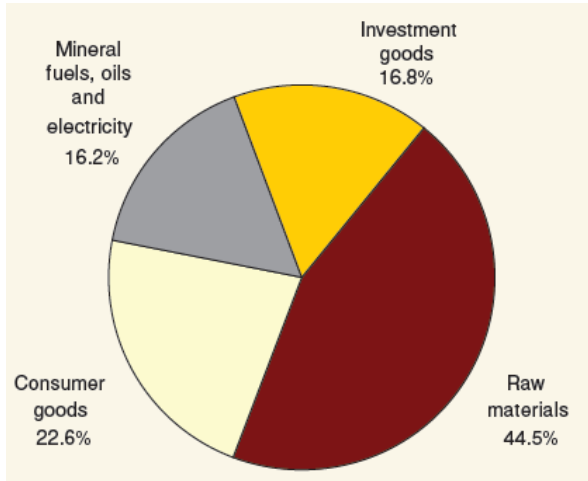


Figure 15: Import by commodity, 2008

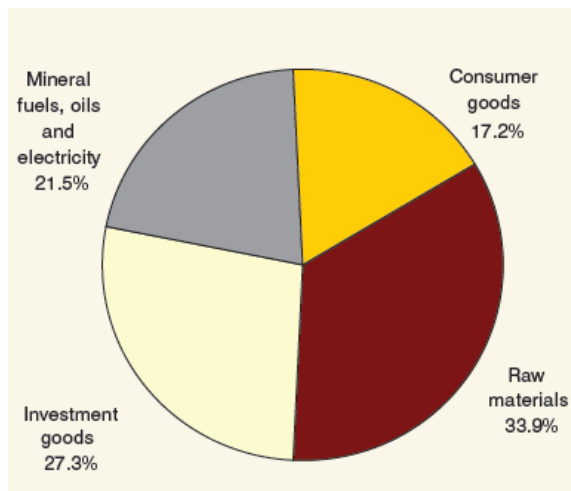
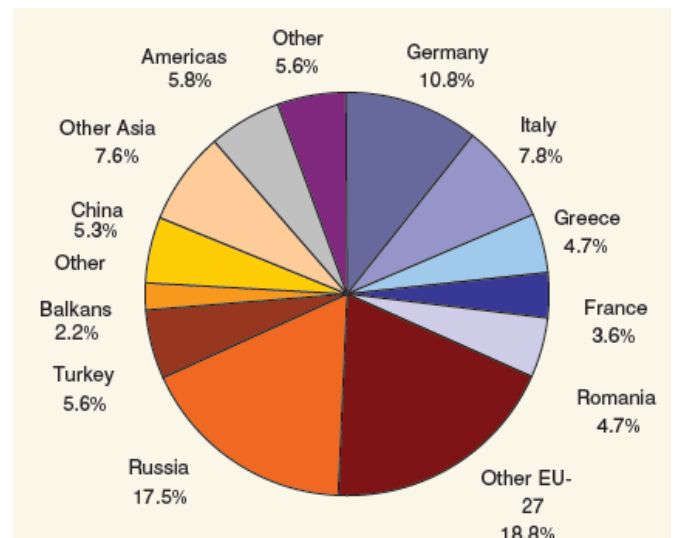


Figure 16: Import by countries, 2008



Source, Bulgarian National Bank



#### 4.3.4. Inflation

Figure 17: Inflation rate

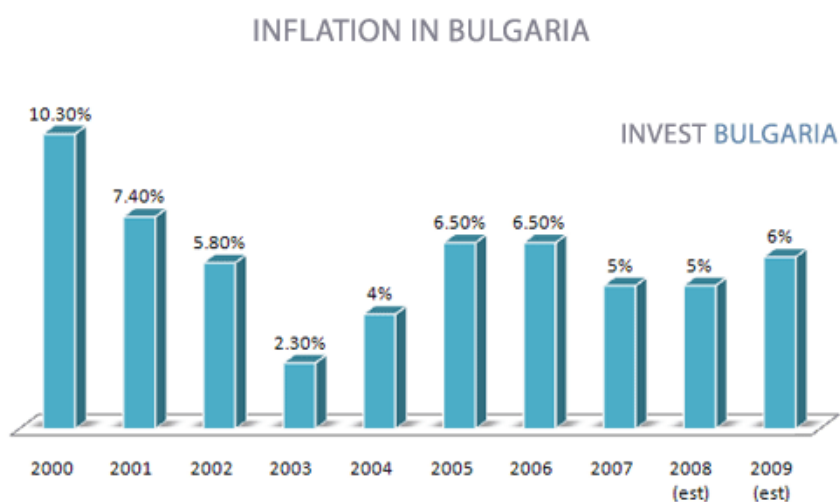


Figure 18: Average yearly inflation in Bulgaria

AVERAGE YEARLY INFLATION IN BULGARIA (IN PERCENT)	
Year	Inflation
2000	10.3
2001	7.4
2002	5.8
2003	2.3
2004	4.0
2005	6.5
2006	6.5
2007*	5.0
2008*	6.0

Source : <http://investbulgaria.com/InflationInBulgaria.php>, accessed on 20.04.2010

#### **4.4. Risk assessment**

After the transition process in 1989, the economy of the country entered a period of destabilisation and depression. The Bulgarian industry and production was extremely weak. The activities and industries, which had been working with the ex Soviet Union countries, such as agriculture, machinery, chemical industry, coal mining, oil refining etc. were hit worst.

Nowadays the situation looks better. The financial and macroeconomic situation of Bulgaria tends to remain satisfactory. The foreign debt of the country is still high, but the levels of foreign exchange reserves have been improved and the memberships to European Union and NATO have brought an improvement of the Bulgaria's international position.

In 2009 the elections were won by the centre-right party (GERB) .The main points of its economy policy are the campaign against corruption and crimes, the management of community funds. The bank system has been developed and some changes in legal regulations have been come into force in order to provide the investors with a stable legal environment.

#### **4.5. Bulgaria Competitiveness score**

According to Yadong Luo(2002)

*“Competitiveness is the relative strength that one needs to have to win in competition against rivals. Country competitiveness is the extent to which a country is capable of generating more wealth than its competitors in world markets. It measures and compares how countries are doing in providing firms with an environment that sustains the domestic and international competitiveness of those firms.”<sup>25</sup>*

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<sup>25</sup> Yadong Luo, Multinational Enterprises in emerging markets, p. 8, 2002

I would like to represent the score of Bulgaria according to IMD World Competitiveness Yearbook, that analyzes and ranks the ability of nations to create and maintain an environment that sustains the competitiveness of enterprises. IMD is an independent non profit foundation, situated in Lausanne, Switzerland.

According to the homepage it covers 57 countries , using 329 different criteria. The methodology of the WCY consist of four main factors : economic performance, government efficiency, business efficiency and infrastructure.

It is used by the business community to assess national environments – in an open and global environment , because the choice of location is very important for the companies when expanding their business.

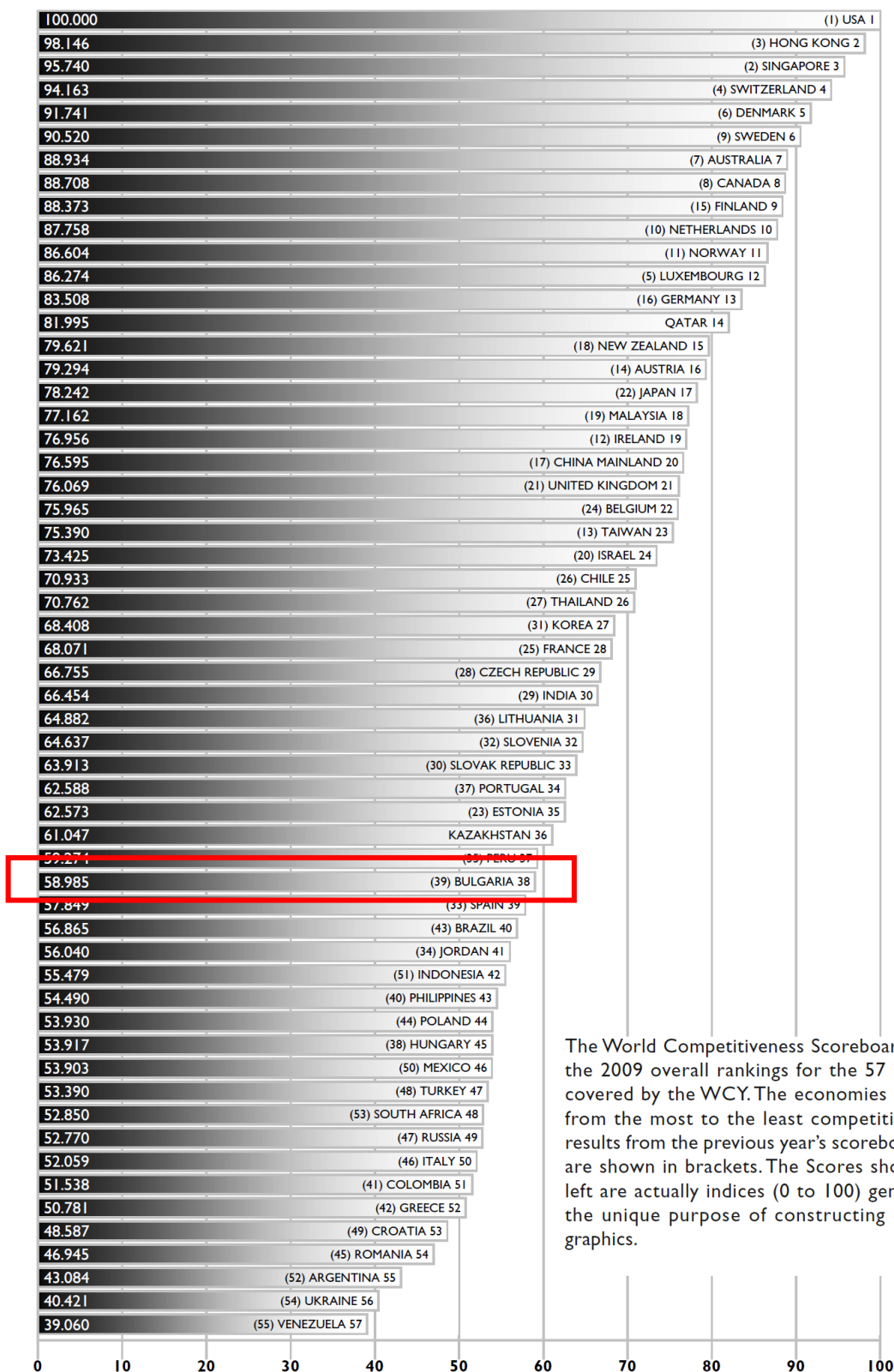
There are also the report from the World Economic Foun (GGR) Global Competetiveness Report, which covers many more economies (134) , but few criteria ( 116). That is the reason why both of comparisons and the rankings differ.<sup>26</sup>

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<sup>26</sup> Source: <http://www.imd.ch/research/publications/wcy/upload/FAQs.pdf>

Figure 19: Bulgaria Competitiveness Score

The World Competitiveness Scoreboard 2009

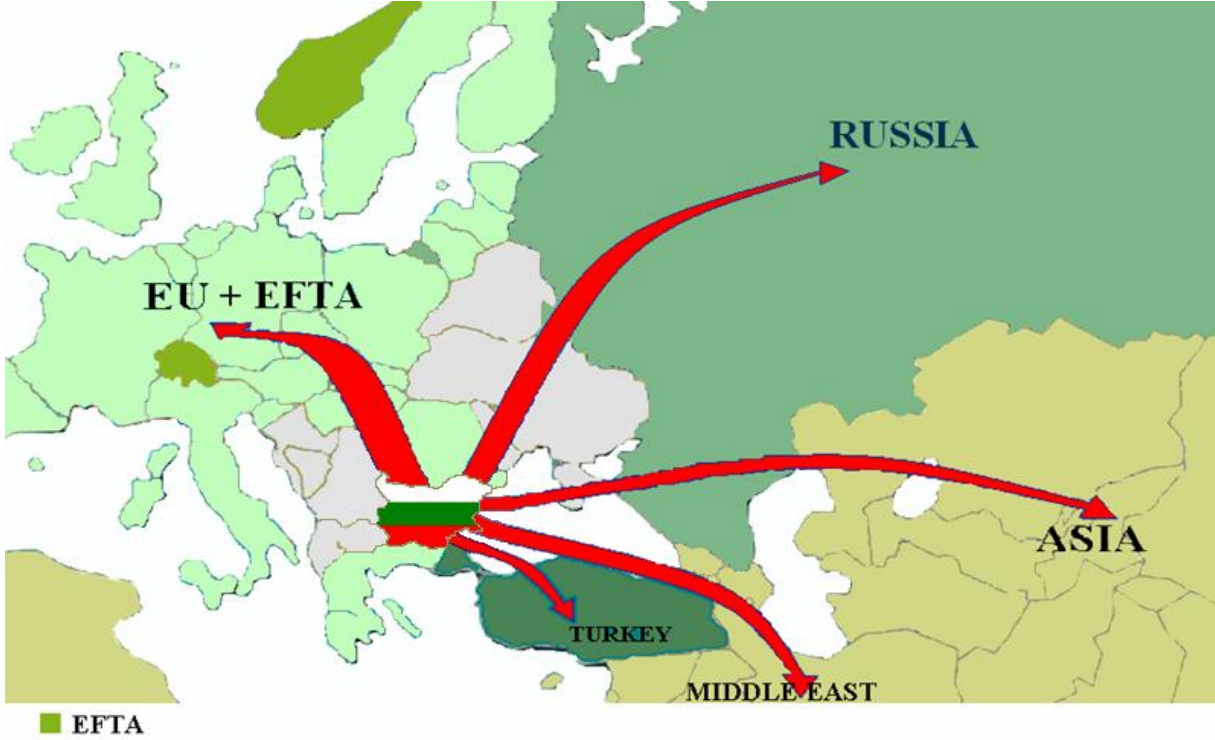


The World Competitiveness Scoreboard presents the 2009 overall rankings for the 57 economies covered by the WCY. The economies are ranked from the most to the least competitive and the results from the previous year's scoreboard (2008) are shown in brackets. The Scores shown to the left are actually indices (0 to 100) generated for the unique purpose of constructing charts and graphics.

Source : <http://www.imd.ch/research/publications/wcy/World-Competitiveness-Yearbook-Results.cfm>, accessed on 15.03.2010

**5. Summary of the main advantages and disadvantages from Bulgaria as an investment location**

Figure 20: Bulgaria Location Map



Source: Invest Bulgaria Agency

First of all attention has to be drawn to a banal but also very vital factor – Bulgaria’s strategic location.

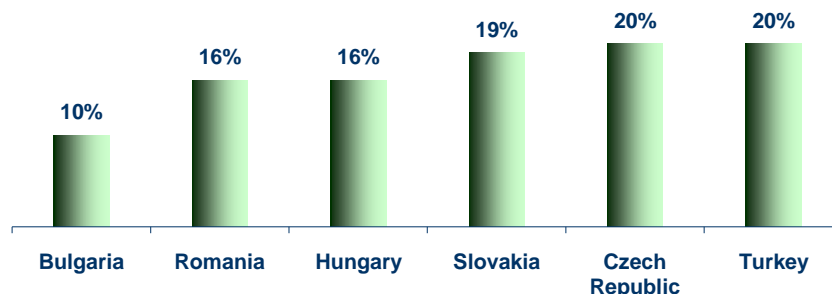
One of the reasons that make the country attractive for foreign investors is its strategic location, as a getaway between Europe and the Middle East.

**Figure 21: Bulgaria, compared with Europe**

	GDP 2008 (EUR bn)	Average GDP growth, 2006 - 2008	Average inflation, 2006 - 2008	Corporate tax rate, 2009	Monthly average labour costs (EUR), 2008	Average wages growth, 2007 - 2008
Bulgaria	34.1	6.2%	9.0%	10%	280	17.9%
EU-27	12,507.0	2.3%	2.7%	28%	2,560	3.8%
Hungary	105.2	1.9%	6.0%	16%	1,055	7.7%
Italy	1,572.2	0.9%	2.6%	31.4%	3,350	5.4%
Romania	137.0	7.1%	6.5%	16%	526	21.5%
Poland	362.1	5.9%	2.7%	19%	997	9.8%
Turkey	498.4	4.2%	9.5%	20%	943	n/a

**Source: Invest Bulgaria Agency; Eurostat, Bank Austria Creditanstalt**

**Figure 22: Corporate income tax rates, 2010**



**Source: Invest Bulgaria Agency**

Bulgaria has the most favorable tax in the European Union and other advantages such as:

- 10 % corporate income tax rate
- 0% in high-unemployment areas
- 10% flat tax rate on personal income
- 2-year VAT exemption for imports of equipment for investment projects over € 5million, creating at least 50 jobs
- 5% withholding tax on dividends and liquidation quotas (0% for EU tax residents)
- Opportunity for R&D expenditure write-off

The government offers financial support for priority investments.

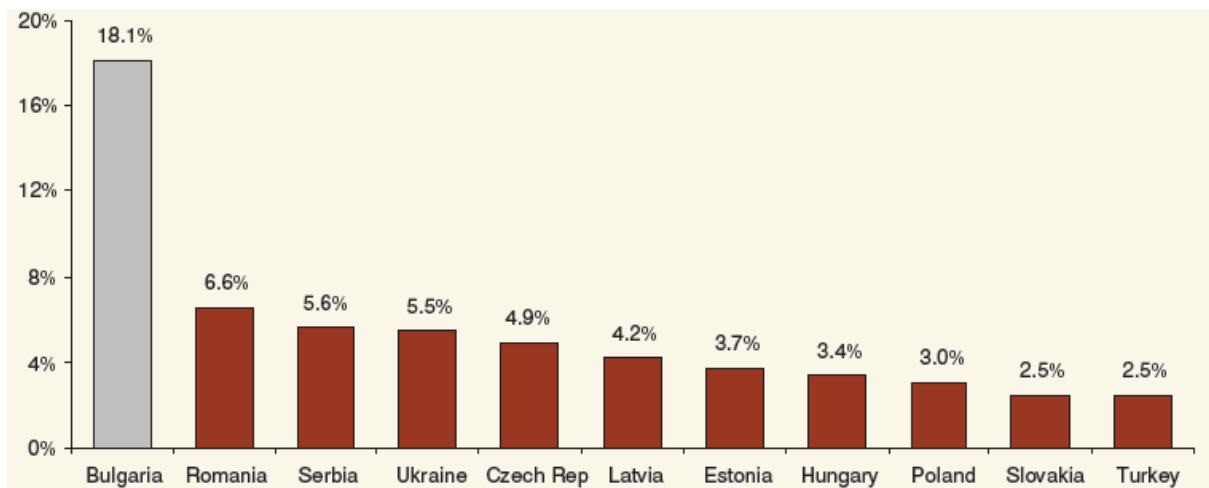
Summarized, it can be state that the greatest strengths of Bulgaria as an investment area are the stable banking sector, the skilled labour forces , the growth opportunities enhanced by the asseccion to the European union, the very low costs of living, the low corporate taxes and its strategic geographical position.

On the contrary, among the weaknesses the most serious are the heavy private foreign debt, the lack of progress on governance, the excessive current account deficits, the inefficient bureaucracy, the high level of corruption, and the fact that the growth is primarily based on construction, property and financial intermediation.

### 5.1. Foreign Direct Investments in Bulgaria

“The risks are, for instance likely to be reduced, since an economic downturn in one country can be compensated by growth in another market in which the organization operates”.<sup>27</sup>

**Figure 23: FDI as % of GDP, 2008**



**Source: Invest Bulgaria Agency**

<sup>27</sup> Hollenson , S., Global Marketing, a market responsive approach , 1998

## **5.2. Motives for foreign investors to come to Bulgaria**

I would like to give an illustration of the reasons that motivate the investors to start their expansions or other investment projects in Bulgaria with an interview which was given on 25.03.2010, by Fabrice Reynaud, the Senior Manager from Ernst & Young, France, for one of the most serious Bulgarian financial and economic internet portals Econ.bg, The interview was initialized by the fact that he is one of the experts in the team that created a Survey called South Central Europe FDI Attractiveness Survey 2009 ,which focused on Bulgaria.

The complete interview is to be found in the Appendix of this paper.

### **Summary of Interview 1**

According to Fabrice Reynaud, the accession of Bulgaria to the European Union has been playing a very important role in attracting foreign investors, since it offers them more safety and predictability.

He is also convinced that ,despite the financial crisis and the severe decrease of the FDI flows in 2009 ,Bulgaria ,is and will continue to be a country with a very big growth potential, which is usually another reason that drives FDI toward such markets. The report on the conducted survey about Bulgaria, confirmed that the country is among the few numbers, matching the Maastricht criteria today (April, 2010).

He sees a possibility for the global companies to overbear the disadvantages that come with the increasing sovereign debt of Bulgaria by balancing between their countries/locations portfolio.<sup>28</sup>

Another interview with interesting questions I have found on internet was given by Mr. Dr. Michael Angerer, Commercial Councillor of the Austrian embassy in Bulgaria.

As a following I want to present a summary of this interview, in order to explain the motives for Austrian companies to enter the Bulgarian market.

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<sup>28</sup> Source: [www.econ.bg](http://www.econ.bg), accessed on 27.04.2010  
*This interview was taken by **Kaloyan Staykov, econ.bg***



## **Summary of Interview 2**

As a “Commercial Councillor” of the Austrian embassy in Bulgaria, Michael Angerer is responsible for supporting Austrian companies, which want to start business activity in Bulgaria, by seeking potential Bulgarian partners, giving information about investment opportunities etc.

Generally said, his job is to look after and to support the well-established trade relationship between Austria and Bulgaria.

In this interview he announced his experience gained while working on a very big steel plant project, whose deadline was postponed due to the financial crisis.

The greatest difficulties he had to deal with were mostly connected with government administrative restrictions, bureaucratic procedures, the loss of good facilities and the loss of the so called industrial zones regulations and promotion schemes (which normally exist in other countries). According to him, improving these could have positive impact on the attraction of foreign investors to Bulgaria.

He also points out the main benefits for foreign direct investors, namely, the growth potential, the low taxation, the low operational costs and the location, but also the friendly mentality of the people, which make business negotiations easier.

Asked about the main motives for the Austrian companies to invest in Bulgaria, Mr. M.Angerer says that these are, in particular, the growth of the market, the need and demand for all kinds of products and services and, not least, the geographical location and the proximity to the home country.

His future forecast for Bulgaria is very realistic -he is aware of the sharp reduction of the Austrian investments flows during the last year and the effects of the global crisis, especially in some sectors like real estate, but also sees chances for new business transactions( e.g. acquisitions), because many Bulgarian companies are likely to be sold for reasonable prices.

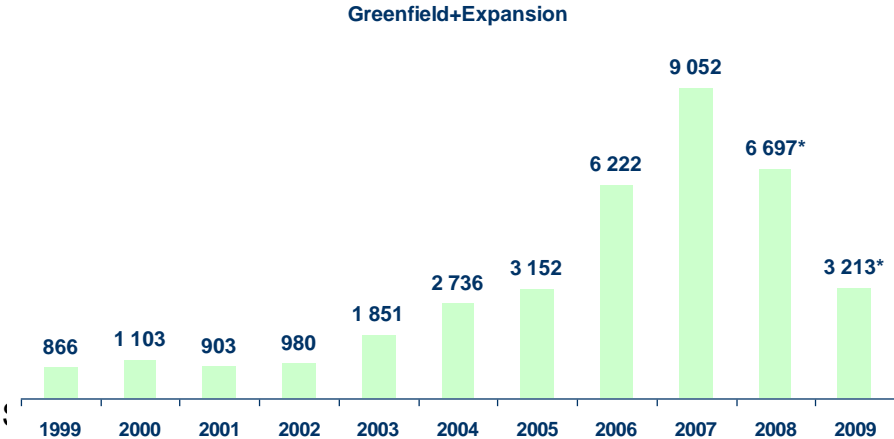
According to his experience the main problems that Austrian companies usually have to face in Bulgaria are connected with the transparency, the slow administration procedures and the loss of built infrastructure and facilities.

As a big cultural difference between Austria and Bulgaria, but also for other business partners coming from western European countries or the USA, he gives an example of a Bulgarian peculiarity, which is that of thinking rather in the short term. Two years

is typically seen in Bulgaria as extremely long period, which in his opinion is not suitable in a business context.<sup>29</sup>

### 5.3. Overview of the FDI

Figure 24: FDI Inflow in 2006-2008, in EUR m



FDI inflows toward Bulgaria had their begin from the late 1990, but the major players in order of volume, came in Bulgaria in 2003. The most investments were made in the food and drinks-processing industry, chemical fertilizer, the oil refinery, mining, electricity etc.

<sup>29</sup> Source: <http://www.italkcash.com/forum/general-investment-opportunities/177180-michael-angerer-austrian-commercial-counsellor-bulgaria-interview.html> accessed on 25.05.2010

### 5.3.1.FDI by countries

Figure 25: FDI by countries

Country	FDI stock %	FDI stock, EUR m
<b>Austria</b>	<b>16%</b>	<b>5903.8</b>
<b>The Netherlands</b>	<b>12%</b>	<b>4642.7</b>
<b>Greece</b>	<b>9%</b>	<b>3419.7</b>
<b>United Kingdom</b>	<b>8%</b>	<b>3036.7</b>
<b>Germany</b>	<b>7%</b>	<b>2526.3</b>
<b>Cyprus</b>	<b>5%</b>	<b>1921.1</b>
<b>USA</b>	<b>3%</b>	<b>1310.2</b>
<b>Hungary</b>	<b>3%</b>	<b>1276.4</b>
<b>Italy</b>	<b>3%</b>	<b>1170.0</b>
<b>Russia</b>	<b>3%</b>	<b>1088.1</b>

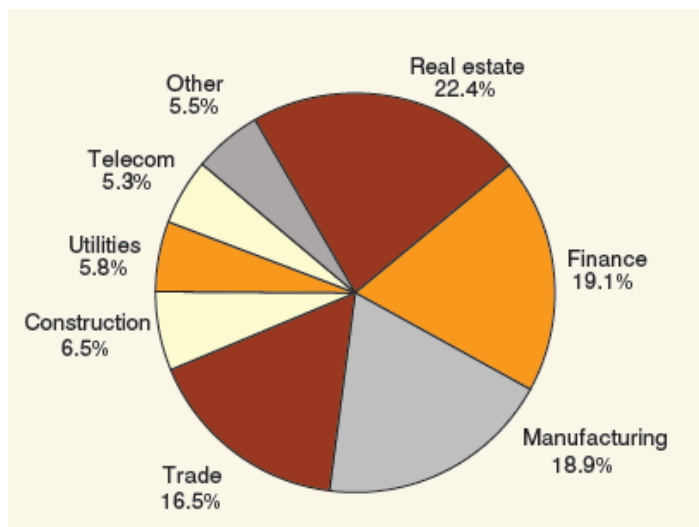
Source: own creation, data based on Invest Bulgaria Agency, Bulgaria General Presentation, April 2010

<http://www.investbg.government.bg/index.php?sid=74>, 20.04.2010

As we can see, Austrian companies have made the most foreign direct investments for this long period in Bulgaria with 16%, followed by the Netherland with 12%, Greece (9%), Great Britain (8%) and Germany (7%).

### 5.3.2. FDI by sectors

Figure 26: FDI Stock by sector 1998-2008 (%)



Source: Invest Bulgaria Agency

During the last ten years most FDI inflows were in real estate, followed by financial intermediation, manufacturing and trade.

### 5.3.3. Austrian FDI

Austria is very well set up in Bulgaria these days. The total of Austrian FDI until 2008 is about 6.5 billion EUR.

The main attraction for the Austrian investors are the dynamic and growing market, the low taxation, the low operational costs and the low costs of living. Since it became member of the European Union (2007) Bulgaria has been even more attractive investment location. Among the main problems that obstacles the investors are the bad transparency, the miss of infrastructure, the corruption, and the bureaucracy in the administration.

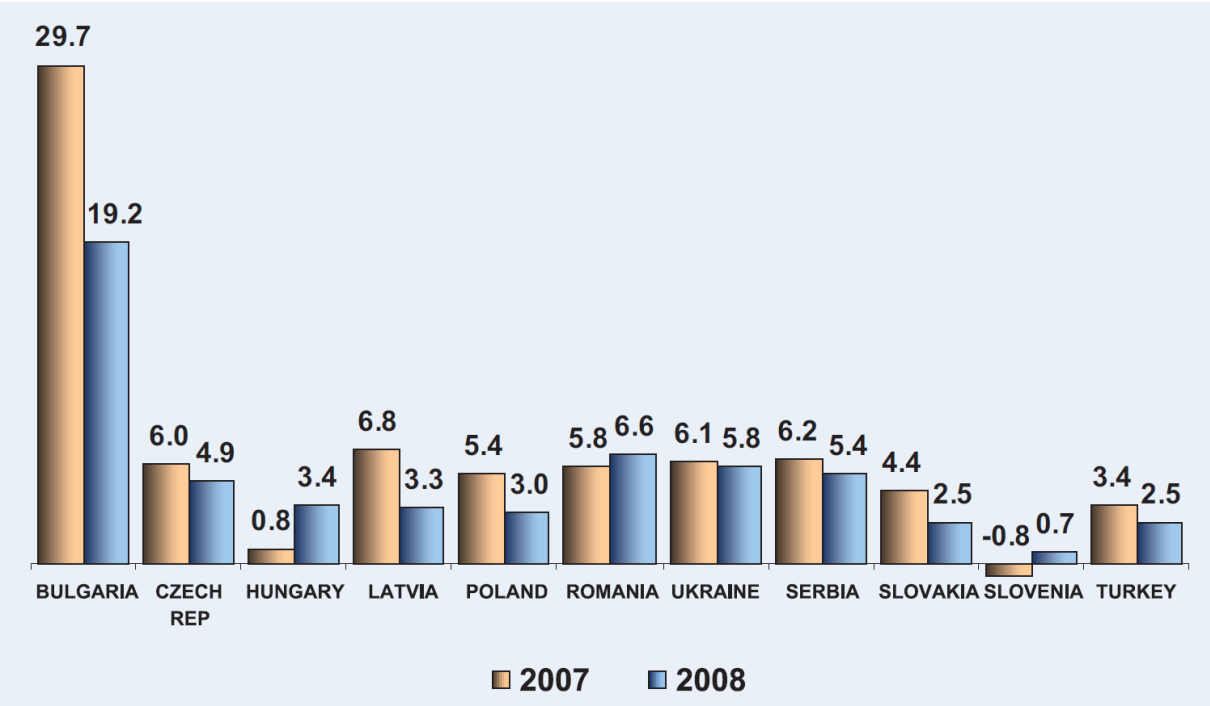
The Austrian FDI in Bulgaria cover lot of different sectors such as communications, financial intermediation, wholesale and retail sale, electricity distribution and generation, real estate, machine building etc.

Some of the main Austrian investors in the country are presented in the following table:

**Figure 27: Austrian big investors in Bulgaria**

Name of the company	Sector
EVN	Energy
Telecom Austria MobilTel	Telecommunications
Bank Austria Creditanstalt	Banking
Raiffeisen Zentral Bank	Banking
Vienna Insurance Group	Insurances
Grazer Wechselseitige	Insurances
Uniq	Insurances
OMV	Oil refinery
Strabag AG	Building & Construction
Schenker&CO AG	Transport & Logistics

**Figure 28: Bulgaria leads CEE countries in terms of FDI to GDP ratio**



Source: BNB, Bank Austria Creditanstalt

**6. The Bulgarian Insurance market from 1999 – 2009**

I have chosen to write about the Bulgarian insurance sector and later on to present an Austrian insurance company- Vienna Insurance Group which has entered the market in the case study, because in my opinion it is a very good illustration of what happened with the economic phenomena of the last 20 years – the transformation of the former planned economy to market economy and the opening of the market to foreign companies.

The initial development of the insurance sector in Bulgaria and the need for new international entrants later will also be discussed in this chapter.

In his paper “Foreign Insurers in Emerging markets: Issues and Concerns” (2006) Harold D. Skipper, Jr. states seven ways in that insurances add economic development.

According to the author, the opening of the insurance market to the appropriate foreign insurers might aid economic development, to enhance overall social welfare and may even solve some serious problems.

As a next step I would like to outline the seven ways of adding economic development through insurances:

- (1) Promotion of the financial stability and anxiety reduction
- (2) Private insurance as a substitute for government security programs
- (3) Greater financial trade and commerce; improvement of innovations
- (4) Private insurance as a motor for national savings
- (5) Foreign insurers permit business and individuals to manage with the risk more efficiently by risk transformation, risk pricing, risk pooling and risk reduction
- (6) An economic ability to reduce losses
- (7) Foreign insurers permit more efficient allocation of the country's capital

The same paper outlines the arguments against the opening of the market for a great number of foreign insurance companies. These are as follows:

- (1) Foreign insurers will dominate the domestic market
- (2) Foreign insurers will service the market selectively
- (3) Foreign insurers fail to make lasting contributions to the local economy
- (4) Market opening should await certain reforms
- (5) The domestic market is already well served by local insurers
- (6) The insurance industry should remain locally owned for strategic reasons
- (7) Foreign insurers will provoke a greater foreign exchange outflow.<sup>30</sup>

Despite the awareness of these contra arguments, the entrance of the foreign insurers into a country whose economy has been shifting from planned to market-based economy, such as Bulgaria, and the simple fact of the enhancement of the financial services, has played a very important role and had a great contribution to the further development of the national economy.

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<sup>30</sup> Source: Foreign Insurers in Emerging markets: Issues and Concerns" (2006) Harold D. Skipper, Jr.

## **6.1. The transition process and the changes in the insurance sector**

In 1991, Bulgaria, as many other eastern European countries who have followed the Soviet Union model, began its new independent path toward market oriented economy. Following, the model of the insurance sector in Bulgaria before the transition process is described. The so called "Soviet-style" insurance model was organized in such a way that in fact the insurance companies were departments of the Ministry of Finance.

How did it work? For instance, there were state-owned monopoly insurance departments which were responsible only for the domestic market and others which had to cover the import and export activities.

The main principle of the planned economy was state ownership and control in any industrial sector, as well as in financial services and insurances.

A good example, which could be helpful in understanding what the central philosophy of the central planning economy was, is that the main goal and motivation of the managers was to meet production targets at the end of a period and not to realize profit, as with western economies. The state was the only one who could provide people with social insurance or employment.

During the communist rule in Bulgaria there were only two insurance companies DZI( The State insurance Institute/Durjaven zastrahovatelnen institut ) for the domestic market, which was registered in June, 1946 and BULSTRAD (registered in July 1962), and was responsible for trade and commodity transactions.

The state monopoly was not broken until 45 years later, in 1991, when the voting of the new commercial law allowed the opportunities for the occurrence and development of new private insurance companies. This period was a hard time for the underdeveloped non-banking financial sector - the insurance business had to learn how to operate under the new conditions of market competition, which had been completely unknown to that point.



## **6.2. The privatisation, the legal changes and the opportunities and need for Internationalization of the Bulgarian insurance market**

A great number and variety of changes to the Law on banks were undertaken in order to strengthen the intensity of supervision and the rational and intelligent banking and insurance regulations.

A new legislation - The Insurance Supervision Directorate, which is now responsible for the licensing process and the liquidations of the closed insurance companies - was established in 1999.

Since 1st January, 1997, the Insurance Business Act has been in effect and has been regulating the stricter minimum capital and form for the insurance companies.

As a consequence of the new requirements, by the end of 1998, 85 insurance companies had been closed and liquidated by the Directorate of Insurance. At that point the number of the insurance companies which still continued to operate was 27.<sup>31</sup>

At the beginning of 2000, the privatization of the banking sector started and by the end of 2001, the main banks (Bulbank, Hebros, Biochim, Corporate bank and State Savings Bank) had been sold. In 2000, Bulgaria had 34 banking institutions, most of which were privately owned. From 27 locally incorporated banks, 14 had a majority, with 51% or near majority foreign ownership.<sup>32</sup>

The insurance sector had become more and more attractive for the foreign investors. The initial tendency among the foreign entries for foreign insurance companies was to enter the Bulgarian market through acquisitions into small offshore insurance companies. Currently, the trend toward acquisition of shares is greater.

Chapter 7 presents in the case study Bulstrad, an insurance company that was the second largest state monopoly in the Bulgarian insurance sector, and whose main shareholder at the moment is Vienna Insurance Group. The case study gives an example of foreign entry by acquisition of shares.

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31 Source: From Transition to Accession, Developing Stable and Competitive Financial market in Bulgaria, Esen Ulgenerk, Lejla Zlaoui, World Bank Technical Paper Number 473, 2000, p.18

32 Source: Bulgaria The dual challenge of transition and accession, A World Bank Country Study, 2001, p.60-61

The legal framework of Bulgaria's securities markets, which is in consensus with the requirements of the European Union, was brought with the new Law on the Public Offering of Securities, in force since 31.01.2000.<sup>33</sup>

Since 1<sup>st</sup> March, 2003, The Financial Supervision Commission (FSC) has been the core institution, a substitute of the Directorate of Insurance with the function of providing transparency, stability, legal and administrative assistance on the investments, insurance and social insurance markets.

### **6.3. Structure of the Bulgarian insurance market**

The insurance market in Bulgaria is very crowded nowadays. In general, it can be characterized by the domination of the non-life insurances, in particular the motor insurances, which cover about 70 % of the whole market. This percentage is divided proportionally, between "Autokasco" (47.8%) and the second most widespread insurance the "Citizen responsibility" (22.9 %), a product which is also connected with the possession of a motor vehicle.<sup>34</sup>

Life insurance is the most underdeveloped segment – a sign which indicates that the income per capita per annum is too low, compared to the other European countries. As a consequence of the dynamics of the unemployment during the financial crisis, the local savings have not improved.

Nevertheless, the market growth from the Bulgarian insurances can still be defined as a greater and developing more rapidly, compared to other CEE countries.

Currently, there are 20 non-life, 17 life and 20 health licensed insurance companies. The market leaders are the former state monopoly DZI, and, among the foreign groups, Bulstrad (today a local subsidiary of Vienna Insurance Group with 15% market share) and Allianz Bulgaria (10%), which leads in the life segment.

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<sup>33</sup> Source: Bulgaria The dual challenge of transition and accession, A World Bank Country Study, 2001, p.63 -64.

<sup>34</sup> according to [www.nsi.bg](http://www.nsi.bg)

The growth of the written gross premium during recent years indicates a positive financial achievement and a promising tendency for slow, but solid development of the whole sphere of activities. The foreign participants dealing on the Bulgarian insurance scene are extremely well represented. Most of the foreign companies prefer to enter the Bulgarian market by acquiring shares from a local company which already has an established infrastructure, proven brand and a strong market position, than to invest in “green”, or from scratch.

**Figure 29: Structural Business Statistics on Insurance Enterprises**

Variables	2005		2006		2007*		2008*	
	Non-life insurance	Life insurance	Non-life insurance	Life insurance	Non-life insurance	Life insurance	Non-life insurance	Life insurance
Insurers number	20	11	21	15	19	17	20	17
Employees number	3499	894	4316	1190	4393	981	4943	1202
Turnover or gross premiums written - thousand levs	920969	147578	1060768	186181	1269546	235524	1534395	270247
Gross claims incurred - thousand levs	391326	51513	421152	70186	559277	78681	772090	97758
Production value - thousand levs	554512	143172	606295	170341	657865	216312	767223	243944
Total purchases of goods and services - thousand levs	344806	27795	251594	18474	220697	18768	457981	66576
Value added at factor costs - thousand levs	209706	115377	354701	151867	437168	197544	309242	177368

Source: <http://www.nsi.bg/otrasalen.php?otr=69>, accessed on 01.06.2010

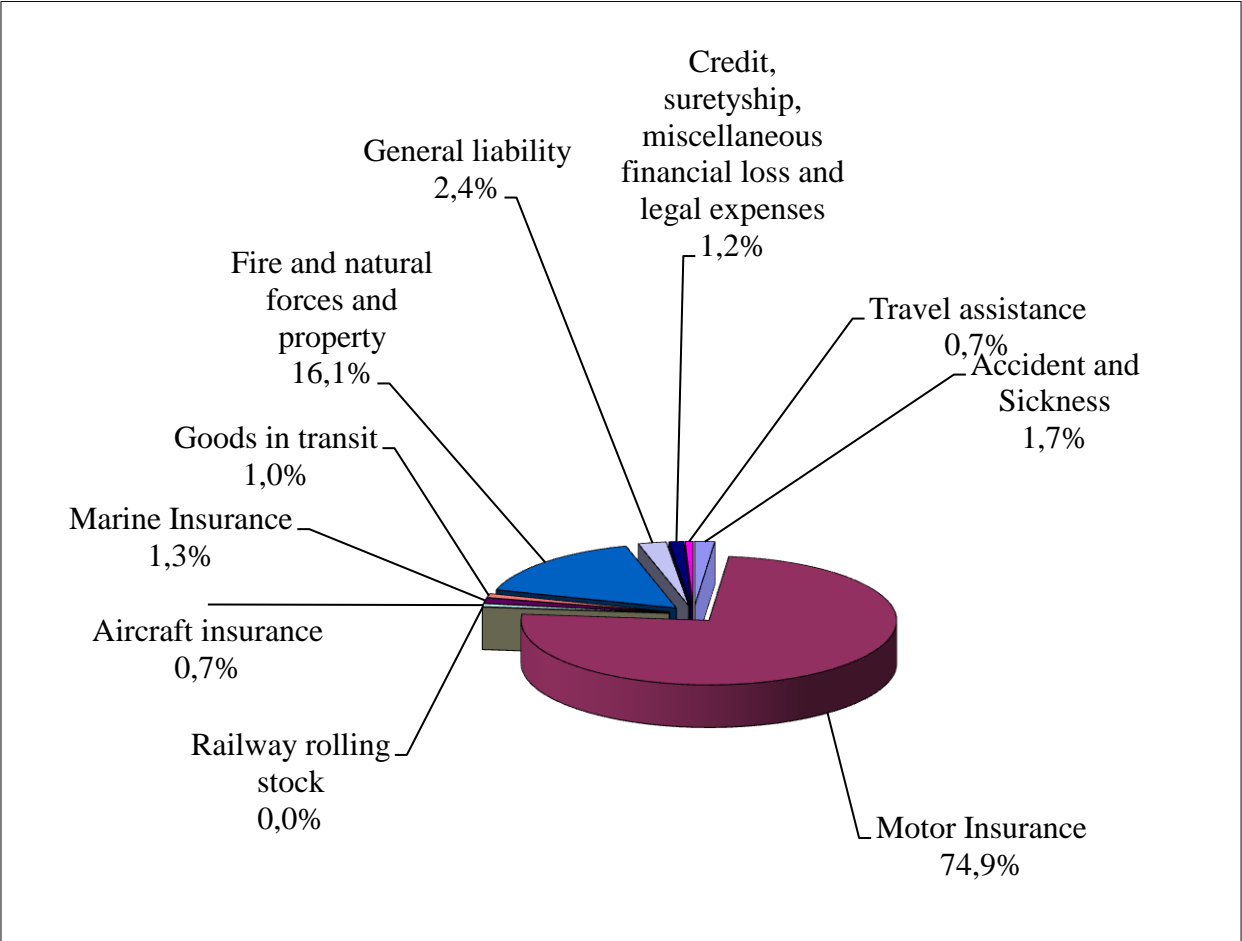
In the following the most important companies in the Bulgarian insurance market are represented according to their market share, based on gross premium income, until 31.03.2010.

**Figure 30: Insurance Companies in Bulgaria**

<i>The Companies are listed into descending order of the market share by premium income, divided in classes of insurances</i>			
	<b>Non life</b>	<b>Life</b>	<b>Reinsurances</b>
<b>1</b>	Bulstrad Vienna Ins.Group	Allianz Bulgaria Life	GP Reinsurance
<b>2</b>	DZI General Insurance	Sy VZK	Euroins
<b>3</b>	Bul Ins	DZI	Allianz Bulgaria
<b>4</b>	Allianz Bulgaria	Bulstrad Life Vienna Ins.Group	UBB AIG
<b>5</b>	Lev Ins	Uniqa Life	Armeec
<b>6</b>	Armeec	Alico Bulgaria life	
<b>7</b>	Generali Insurance	Generali Life Insurance	
<b>8</b>	Euroins	UBB Alico Life Insurance Company	
<b>9</b>	Viktoria	Grawe Bulgaria Life	
<b>10</b>	Uniqa Insurance	Sogelife Bulgaria	

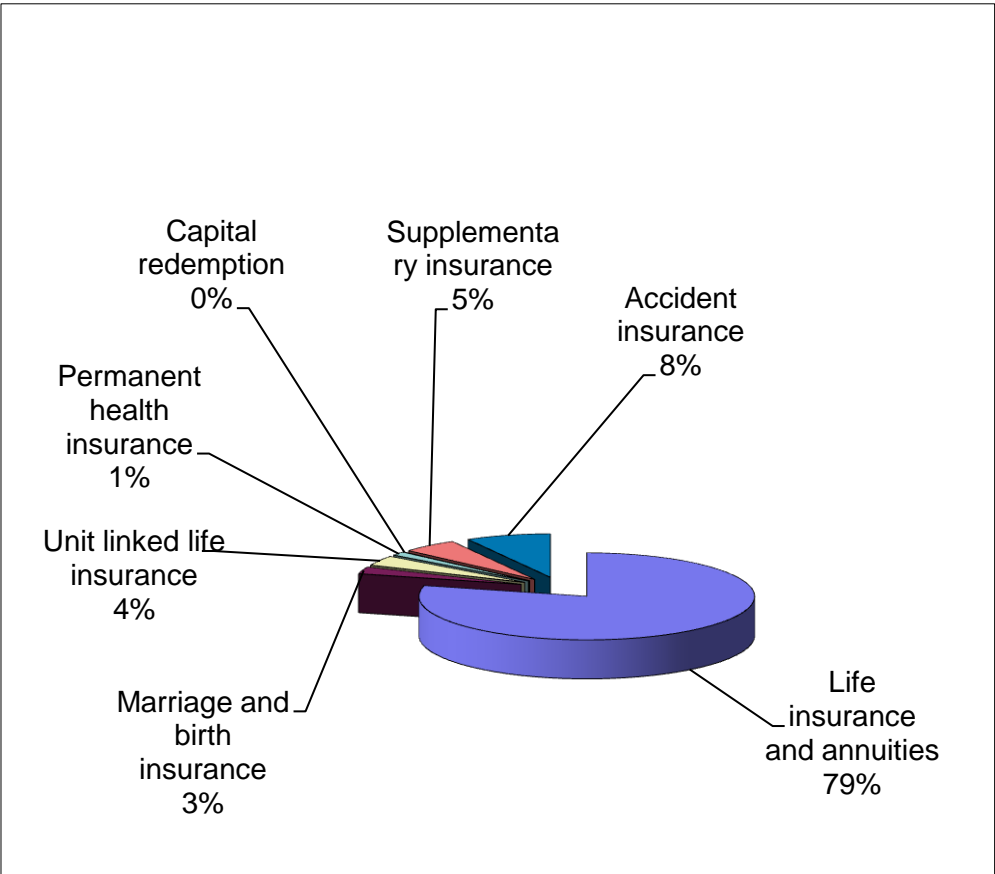
Source: own creation, according to [www.fsc.bg](http://www.fsc.bg) (Financial Supervision Commission)

**Figure 31: Structure of Gross Written Premium by classes of non-life insurances**



Source: figure adapted from Bulgarian Supervisory Commission  
<http://www.fsc.bg/go.idecs?c=1520>

**Figure 32: Structure of Gross Premium Income by classes of Life Insurances as at 31.03.2010**



**Source: adapted from: Bulgarian Supervisory Commission**  
<http://www.fsc.bg/go.idecs?c=1522>

**6.4. Legal framework**

This chapter analyses the legal framework, a very important factor in the external environment that has an enormous influence on the success and competitiveness of the companies investing in a foreign country and entering a specific market, (e.g. the insurance sector) and which should not be underestimated.

Therefore, the knowledge and awareness of the specific laws and legal procedures of the country where the foreign entry is to take place is an essential issue.

I will start with the development of the Bulgarian legal system, and later pay special attention to the specific legal regulations for foreign direct investments, in particular mergers and acquisitions and the establishment of a subsidiary of an insurance company with different countries of origin.

#### **6.4.1. The Bulgarian legal system and its development**

The roots of the Bulgarian legal system can be traced back to the Middle Ages, when at the beginning local customs and practice were applied.

When classifying the Bulgarian legal system, the key question is whether it belongs to the group of countries who adopted the system of civil law or common law. Whereas the civil law has its double-tier structure, which is primarily based on legislation, the common law is based on cases and applying of precedents and has only a one-tier structure , adjusted by judges. Under civil law, all of the laws and norms are written and codified <sup>35</sup>.

The Bulgarian legal system belongs to this of the Civil Law, which has its roots from the earlier Roman law and later has been influenced by both subgroups: French and German's law.

#### **6.4.2. History of the Bulgarian Law**

After the adoption of Christianity in Bulgaria /864/, the canon law was applied.

As Bulgaria fell under Ottoman domination / 1393 - 1878 /, the country applied Turkish civil law - Medzhele.<sup>36</sup>

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<sup>35</sup> James R.Silkenat, Jeffrey M, Aresty, Jackueline Klosek, The ABA Guide to international Business Association; A comparison of cross-cultural issues and successful approaches , Chapter 24 Bulgaria Georgi T. Guginski and Lilia Kisseva, 3 Edition, 2009, ABA Publishing, United States of America

<sup>36</sup> Tokushev, D. New Bulgarian History of the state and legislation( 1978-1944), Sibi, Sofia, 2008, p.175.

Under the decree of the Sultan Mohamed II of 1453, both religion and civil courts were kept. According to the Bishops Statute, adopted in Bulgaria in 1871, there were three types of courts: court conciliation, diocesan councils, and the Holy Synod.<sup>37</sup>

The national legal system, established in the period 1878-1879 played temporary, transitional role. It consisted of written and unwritten law, as of feudal and bourgeois forms and sources.

Of fundamental importance for the Bulgarian legal system was the adoption of the first Bulgarian constitution, called the Turnovo Constitution. In force since, sixteen of April, 1879, it laid the foundations of the state and the legal structure of Bulgaria under the new conditions.

When it came into effect, the constitution recognized “the peculiar triangle of supreme power model of the country – Prince- Government- National Assembly”, which is held as a modern functional structure, filtered from the best of European and Balkan constitutional law .<sup>38</sup>(History of Bulgaria, authors, team Hristo Botev, Sofia, 1994, p.415).

It can be stated that the constitution of Turnovo is held as one of the most democratic constitutions of our time. The different types of social relations are subject to separate laws.

For the most part, the new Bulgarian civil law was built on the basis of the Roman legal system, which was established with the French Civil Code from 1804 by the Italian Civil Code of 1865, but there are also some legislation borrowed from other countries.

Until the advent of the Turnovo Constitution, trade relations had been governed by the Turkish Commercial Law (1850), which was chiefly based on the French Commercial Code (1807).

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<sup>37</sup> according to Tashev, R. Theory of the legal system , Sofia, 2006, p.164, Sibi

<sup>38</sup> . History of Bulgaria, authors, team Hristo Botev, Sofia, p.415, 1994



Gradually, parts of “The Medzhele” and the Commercial law were replaced by laws created by the National Assembly: Law on Obligations and Contracts of 1892, Heritage Act and Guardianship Act of 1892, Trade Act of 1897, and others.<sup>39</sup>

The second Bulgarian constitution (1947) declares that Bulgaria is a national republic which was not changed in the next constitution (adopted in 1971) and in the last Bulgarian constitution (adopted in 1991, last amended in 2007).

From 1944 until 1989 Bulgaria was part of the communistic block. The country later became a member of the World Trade Association (1996), NATO (2004), and European Union (2007).

#### **6.4.3. New Bulgarian Legislation**

The Bulgarian law has come a long way in order to harmonize with the standards and norms of the European law. The Commerce act (1991), (The new Commerce register act 2008), regulates all procedures and requirements, considering the registry of a legal entity under Bulgarian law.

Under Bulgarian law, these are all available forms of commercial companies:





-  General partnership
-  Limited Partnership
-  Limited Liability Company
-  One person owned limited liability company
-  Joint stock company (publicly listed or private)
-  One person owned joint stock company
-  Company limited by shares

Secondary, business can be formed in following entities:

-  Sole trader

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<sup>39</sup> Tokushev , D. History of the new Bulgarian State and law (1978-1944), 2008, Sofia, p.176-177

-  Holding
-  Branch
-  Trade representative office
-  Co-operative

The regulations and procedures valid for establishment of a company are the same for the Bulgarians as for foreign citizens. Up to 100% of the local company's equity can be held by a foreign owner.

In pursuance of the Commerce Register, the most common forms, used by foreign participation in Bulgaria, are Limited Liability Companies (LLC), Joint Stock Companies (JSC), Branches and Trade Representative Offices (TRO).

According to the last changes in the rule of art. 117, (1) of the Trade Act, adopted in 2009, the minimum share capital of 5000 BGN or (equal to 2600 EUR) has been reduced to the symbolic amount of 2 (two) BGN.

JSC minimum is 50 000 BGN or (equal to 26 000 EUR). The minimum necessary capital for banking and insurance companies is much higher and is pointed in the special legal acts for this business activity. For instance, in the Insurance Codex referred to that the registered should not be less than the guaranteed capital - from 2.2 million BGL to 4.6 million depending on of the kind of insurance.

#### **6.4.4. Legislation of Foreign Direct Investments**

The fundamental law, when we are talking about business activities, e.g. investments, is ***The Bulgarian Commercial Law***.

***The Bulgarian Investment Encouragement Act (2007)*** contains additional conditions and procedures which aim to encourage and protect the flow of foreign investments into Bulgaria.

The taxation of the companies is regulated in:

- ***Bulgarian Companies Income Tax Act***, promulgated, State Gazette No. 105/22.12.2006, effective 1.01.2007
- ***Bulgarian Local Taxes and Fees act***
- ***Bulgarian Income Taxes of Natural Persons Act*** (promulgated, State Gazette No. 95/24.11.2006, effective 1.01.2007)

The employment legal requirements are part of the following legislations:

- ***Bulgarian Employment Promotion Act*** contains useful information about:

1. Promotion and support of employment
2. Vocational information and consultation and the vocational training of unemployed and employed persons
3. Intermediation for furnishing information and placement of Bulgarian citizens abroad and of Bulgarian and foreign citizens in the Republic of Bulgaria.<sup>40</sup>

- ***Bulgarian Labour Code , which subject and aim are corresponding Article 1 of this law the following:***

- (1) This Code shall regulate the labour relationships between the employee and the employer, as well as other relationships immediately related to them
- (2) (New - SG, No. 2/1996) Relationships related to providing labour force shall be arranged as employment relations only.
- (3) (Amended - SG, No. 25/2001) This Code shall aim to ensure the freedom and protection of labour, equitable and dignified working conditions, as well as the conducting of social dialogue between the State, the employees, the employers and their organizations, for the purposes of settlement of labour relations and other immediately related relations.

- ***Bulgarian Vocational education and Training act , which shall regulate social relations about :***

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40 Source : Employment Promotion Act, Chapter One, Article one

- “1. Ensuring the right to vocational education and training of the citizens according to their personal interests and possibilities
2. Meeting the needs for qualified manpower which is competitive on the labour market
3. Providing conditions for functioning and development of the system of vocational education and training based on cooperation between its institutions and the bodies of the executive power and the local independent government and the social partners.”<sup>41</sup>

The government has adopted also the Measures against Money Laundering Act, in order to restrict the black economy’s activities.

Last changed 12.07.2006, amended and supplemented, SG No. 54/4.07.2006, amended, SG No. 59/21.07.2006, effective on the day of entry into force of the EU Treaty of Accession of the Republic of Bulgaria, SG No. 82/10.10.2006

Article 2 of this law defines what money laundering shall be:

1. any transformation or transfer of property acquired through or in connection with any criminal activity or participation therein in order to conceal the unlawful origin of such property, or abetting a person participating in such an activity in order to avoid the legal implications of their actions
2. Concealing the nature, origin, location, allocation, movement or rights related to property acquired through criminal activity or participation therein
3. Acquisition, possession, or use of property, with the knowledge at the time of receiving, that it has been acquired through criminal activity or participation therein
4. Participation in any activity under Items 1-3, association for the purpose of performing such activity, attempt to perform such activity, as well as abetting, inciting, facilitating performing of such activity or its concealment.

(2) Money laundering shall also be the case when the activity, through which the property under Paragraph 1 has been acquired, has been performed in a European Union member state, or another country not falling under the jurisdiction of the Republic of Bulgaria.

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<sup>41</sup> Source: Vocational education and Training Act, Article one, (1), 1,2,3.

This Act shall regulate preventive measures against using the financial system for money laundering purposes, as well as organisation and control over such measures.

***Bulgarian Employment Strategy 2004-2010.*** (adopted by the Council of Ministers on 6.11.2003)

This is” an essential document setting the tasks and channelling the efforts of the government institutions, employer organizations, trade unions, non-government organizations, etc. towards enhancing the labour force participation and labour potential of the population. The implementation of this goal is a milestone on the road to achieving the major objective in the economic development of the country, namely – improving the welfare of all social groups.

The developed strategy is harmonized with the main regulatory documents and the studies on employment, education and vocational training: Labour Code, Social Insurance Code, Employment Promotion Act, Act on Public Education, Act on Vocational Education and Training, National Employment Action Plan, National Plan for the Economic Development of the Republic of Bulgaria for the period 2000–2006 and its Operational Program for Human Resource Development, Joint Report on the Assessment of Employment Priorities in the Republic of Bulgaria (2002), National Strategy for Equal Opportunities for the Physically Disadvantaged, etc. The strategy was prepared taking into consideration the priorities in the development of the Single EU Labour Market that were set in the European Employment Strategy and the new dimensions for employment development adopted in Thessalonica in June 2003, as well as the Global Employment Agenda of the ILO.”<sup>42</sup>

#### The Legal process for Mergers and Acquisitions

Mergers and Acquisitions (M&A) are generally regulated in the Commercial act. Other important law regulations concerning vital aspects of the M&A transactions are:

- Obligations and Contract Act
- Competition Protection Act

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42 Source: Employment Strategy, Introduction

- Labour Code
- Ownership Act
- The Social Insurance Act
- The Credit institutions Act
- The Privatisation Funds Act
- The Insurance Act
- The Special Purpose Investment Company Act
- The Privatisation and Post privatisation Control Act
- Investment Protection Act

### Restrictions and special rules

In principle, the investment rules are the same for Bulgarian citizen as they are for foreigners. When the target is a public company, specific regulations contains **POSA** (Public Offering of Securities Act).

Interesting is that there is a official listing of countries, posted by the Bulgarian Council of Ministries ,that contains countries which are discriminative towards the Bulgarian investors: for these countries other investment regulations are to be considered.

Normally before the realisation of a transaction, e.g. an Acquisition, recognition from the relevant controlling body is necessary.

#### **6.4.5. Legal requirements concerning the establishment of the insurance companies**

Particular sectors, such as instance insurance or banking, are governed by specific regulations additional to the general rules of the Commercial Act.

More in details, the insurance activity is regulated in a Commercial act in Article 1; Paragraph 1 of the Insurance Codex defines the following criteria of the establishment form of an insurance company: it can be organized in its legal form as a Holding (AG), as cooperation or as a subsidiary of foreign insurer.

The foreign investment legal regulations, concerning the establishment of JSC (Joint Stock Company) are included in Article 12 of the Insurance Codex.

An important step is the applying for a licence from the FSC (Financial Supervisory Commission) which have to be received in advance before the notation of the new established insurance company in the Commercial registry. The requirements are content of the Article 30 of the Insurance Codex.

The business activity of an insurance company in Bulgaria, from an insurer, which has other country of origin part of European Union as its seat, is regulated in Article 52 of the Insurance Code. It says the following:

” An insurer with seat and address of management in other European Union country , who has got the license for practicing insurance activity is allowed to undertake the activity, exactly for which this license is published, on the territory of Republic of Bulgaria.”

In addition, according to the first directive of the European Council from 24.07.1973, about the coordination of the law, under law and administrative regulations, information has to be given to the European commission, concerning the concrete insurance activity, different from Life insurances (73/239/EIO).

## **7. Case Study: Vienna Insurance Group as one of the most successful foreign companies in the Bulgarian insurance market**

The main aim of the case study is to compare the theory given in the first part of this paper with the practice, and to find out accordance or discrepancies, as well as to gain more additional interesting information from reliable sources by evaluating the interviews.

With the help of two personally taken interviews with the local managers of both subsidiary companies (Bulstrad Vienna Insurance Group, Bulstrad Life Vienna Insurance Group), I have tried to find answers to questions concerning the factors which have influenced the choice of foreign entry mode, the changes resulting from the post-acquisition process, the process of coordination and control between the headquarters and its subsidiaries and to learn more about the main potential gains or pitfalls which lie ahead for the foreign companies currently dealing within the Bulgarian insurance market. Furthermore, the appraisal of how successful the investment is and an outlook for the future perspectives of the investigated company in Bulgaria are discussed. The group has been entering most of the countries through horizontal acquisitions. The main reasons for this foreign entry decision are maybe the lack of local know-how, together with the desire to gain the existing key employees and customers and to keep the market position of the acquired company. A very important role is played by the motto of the company “think globally, act locally”, which best defines its very much locally driven business approach.

The design for the questions I have used for the interviews, as well as their complete transcript is listed in the Appendix at the end of this work.

### **7.1. Presentation of the company**

*“We use our pole position in CEE to create sustainable value for our future success, based on region, people, financial strengths and best solutions.”<sup>43</sup>*

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<sup>43</sup> Dr. Günther Geyer, CEO Vienna Insurance Group  
( Source ; <http://www.vig.com/en/home.html> , accessed on 14.06.2010)



## Overview of activities

The Vienna Insurance Group (V.I.G.), with its registered office in Vienna, is now one of the largest international insurance groups in Central and Eastern Europe with approximately 23,000 employees and a premium volume of around EUR 8 billion. With its focused and clear internationalisation strategy in the CEE economic region, the insurance provider made the transition from a national insurance company to an international insurance group with more than 50 insurance companies in 23 countries. In total, about 50% of all group premiums already come from the Central and Eastern European markets.

Outside its Austrian core market, the Vienna Insurance Group have been active in Albania, Bulgaria, Germany, Estonia, Georgia, Croatia, Latvia, Liechtenstein, Lithuania, Macedonia, Poland, Romania, Russia, Serbia, Slovakia, the Czech Republic, Turkey, Hungary, Ukraine and Belarus through interests it holds in insurance companies. The Group also has branch offices in Italy and Slovenia.

The insurance companies of the Vienna Insurance Group offer high-quality insurance services in both the life insurance and non-life insurance areas. The main goal thereby is providing local insurance solutions for all possible situations as well as an optimal customer service.<sup>44</sup>

### **7.2. History in briefly**

The history of one of the leading insurance group in Austria began in the earlier 1824, with the foundation of Wechselseitige, k.u.k. privat Brandschadensversicherungsanstalt by Georg Ritter von Höglmüller

In 1898, the Vienna City Council adopted a resolution for the foundation of the Städtische Kaiser Franz Joseph - Jubiläums - Lebens - und Rentenversicherungs – Anstalt, occasionally the 50 years of the accession of Empreur Franz Joseph I.

The name Wiener Städtische, which has been used until today, is a shortened form of Gemeinde Wien- Städtische Versicherungsanstalt, which came into force in 1919.

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<sup>44</sup> Source : <http://www.vig.com/en/vig/group/profile.html> accessed on 18.06.2010

The today's Austrian head office, which is located at the Schottenring 30, in first district in Vienna has opened its doors on 14.06.1955.

The next steps have historical importance for the company's growth –in 1966 Wiener Städtische acquires 40% of the shares of Österreichische Volksfürsorge(The Austrian National Welfare) , followed by acquisition of the majority shares of Donau in 1971.<sup>45</sup>

### **7.3. The management principles of Vienna Insurance Group**

#### The Management of VIG: Think globally , act locally

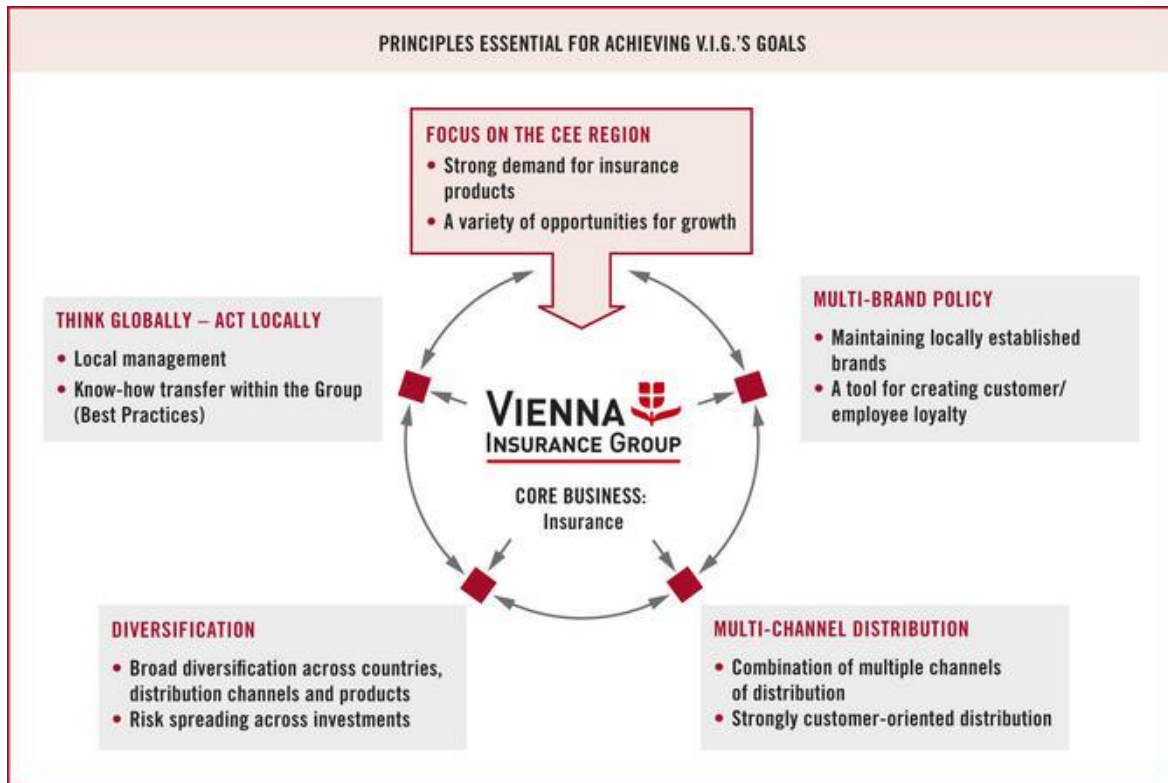
The realisation of growth and expansion in the CEE region has been always among the objectives of the Vienna Insurance Group.

The company succeed due to its quick and flexible adjustment to the conditions of the local markets, as well as due to the durable spread of distribution channels across the foreign countries and new insurance products, developed exclusively for where they are needed.

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<sup>45</sup> Source: <http://www.vig.com/en/vig/history/beginnings-of-the-vienna-insurance-group.html> , accessed on 16.06.2010

Figure 33: Management principles



Source: <http://www.vig.com/en/vig/strategy/management-principles.html>  
accessed on 14.06.2010

#### 7.4. The Mission of the company

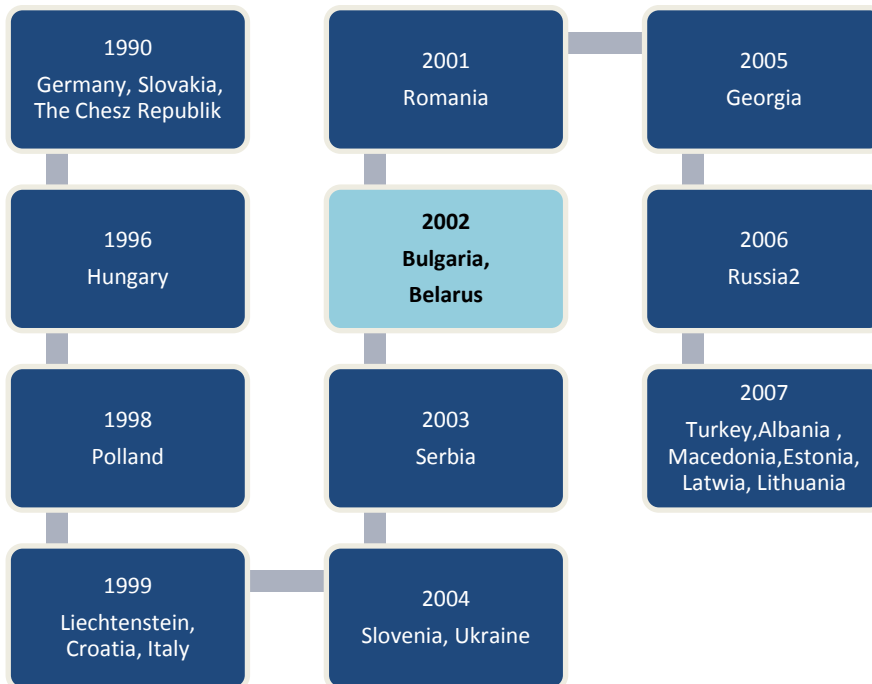
##### The Mission Statement of Vienna Insurance Group:

*WE ARE FAMILY.*

1. We are at home in Central and Eastern Europe
2. We are a leading insurer in CEE
3. We are family
4. We care about people especially
5. We are aware of our social responsibility
6. We create value sustainably.
7. We want to be the leader.

## 7.5. International expansion

Figure 34: Expansion Steps of Vienna Insurance Group



Additionally to subsidiaries, branch offices are maintained in Italy and Slovenia.

The group has been entering most of the countries through horizontal acquisitions. The main reasons for this foreign entry decision are maybe the lack of local know-how and the desire to gain the existing key employees, customers and to keep the market position of the acquired company.

A very important role plays the motto of the company "think globally, act locally", which defines in a best way its much more locally driven business approach.

Figure 35: Vienna Insurance Group in the CEE

## Welcome to the family of VIENNA INSURANCE GROUP







<b>AUSTRIA</b>	<b>CZECH REPUBLIC</b>	<b>SLOVAKIA</b>	<b>ROMANIA</b>	<b>POLAND</b>
  	  	   	   	   
<b>GERMANY</b>	<b>HUNGARY</b>	<b>BULGARIA</b>	<b>ESTONIA</b>	<b>UKRAINE</b>
	 	  	 	   
<b>LIECHTENSTEIN</b>	<b>CROATIA</b>	<b>ALBANIA</b>	<b>LATVIA</b>	<b>GEORGIA</b>
	   			
<b>ITALY BRANCH</b>		<b>MACEDONIA</b>	<b>LITHUANIA</b>	
				
<b>SLOVENIA BRANCH</b>	<b>SERBIA</b>	<b>RUSSIA</b>	<b>TURKEY</b>	
				
<b>BELARUS</b>				
 				

June 2008  
For more information visit [www.vig.com](http://www.vig.com)

Source: <http://www.vig.com/de/vig/konzern/vig-in-cee/group-logos.html>

## **7.6. Foreign entry in Bulgaria**

Since 2007 Vienna Insurance Group is in possession of Bulstrad , Bulstrad Life and Bulgarski Imoti In 2009 the group acquired directly the shares in Albania, Bulgaria and Macedonia held from TBIH Financial Services Group

### ***7.6.1. Presentation of Vienna Insurance Group's subsidiaries in Bulgaria***

In Bulgaria, Vienna Insurance Group is represented by three companies- Bulstrad Vienna Insurance Group, Bulstrad Life Vienna Insurance Group and Bulgarski imoti Life and Non Life Insurance Group. I would like to present each of them briefly.

#### **BULSTRAD VIENNA INSURANCE GROUP JSC**

Bulstrad Vienna Insurance Group has been a major player on the Bulgarian insurance scene for very long period - 46 years.

The long years of experience, the loyalty of many generations of customers, the high professionalism and the variety of products and services are some of the keys of success which stand behind the trade mark of the company.

Since April, 2007 the company became part of Vienna Insurance Group. This step, joining a company with 180 years of insurance experience, made the company even more successful and has been allowed the easier introduction of best practises, which are very helpful in order to satisfy the increased need of the customers after the accession to the European Union.

The company offers motor insurance, property insurance, liability insurance, travel and personal insurance, transportation insurance, agricultural insurance, financial risk insurance, as well as reinsurances.

Bulstrad Vienna Insurance Group is the first insurance company for the year 2008 - with growth in the premium income of 24.98%, compared to the market growth of 20.80%. The gross premium income of Bulstrad Vienna Insurance Group for financial

2008 is BGN 222 million. The company was also selected for the first insurer of the year 2009.<sup>46</sup>

### BULSTRAD LIFE VIENNA INSURANCE GROUP JSC

Bulstrad Life Vienna Insurance Group JSC. was established in 1994. It is one of the first licensed life-insurance companies in Bulgaria.

Bulstrad Life Vienna Insurance Group is among the most dynamic and successfully developing companies on the Bulgarian life-insurance market. The company is specialized in offering adequate life-insurance solutions to its client thus to guaranteeing security, insurance coverage and financial support for their long-term plans.

### BULGARSKI IMOTI LIFE AND NON LIFE JSC

In 2002, Vienna Insurance Group acquired 95% of the capital of Bulgarski Imoti.

Later, in 2005, Vienna Insurance Group made a decision to realise an investment and have increased its participation up to 98.1%

Currently, the equity capital of the company is structured as 99.9% possession of Vienna Insurance Group and 1% in possession of other persons.

The company has a two stage-management which consists of Management Committee and Supervising Committee.

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<sup>46</sup> Source: <http://www.bulstrad.bg/en/AboutUs/FinancialResults.htm>, accessed on 01.08.2010

Figure 36: BULGARSKI IMOTI /KEY FINANCIAL INDICATORS

	<u>31.12.2008</u>	<u>31.12.2007</u>	<u>Growth</u>
	Tsd. BGN	Tsd. BGN	%
<b>Gross written premium /GWP/</b>	<b>52 202</b>	<b>50 866</b>	<b>2.63%</b>
<b>Gross insurance reserves</b>	<b>61 158</b>	<b>38 255</b>	<b>59.87%</b>
<b>Total assets</b>	<b>78 793</b>	<b>58 236</b>	<b>35.30%</b>

Source: <http://www.bulgarskiimoti.bg/pagesen/history>  
Presentation, accessed on 2.08.2010

For the purpose of this master thesis case study, two interviews have been carried out, kindly supported by Dr Klaus Mühleder, a member of the Management Board of the company and one of its managing directors in Bulgaria, and Ms Romyana Gergova, CFO of Bulstrad Life Vienna Insurance Group.

The questions for the interviews, as well as the complete transcript of them, are published in the appendix at the end of this paper.



### **7.6.2. Discussion of findings**

In order to gain a clearer picture of the main findings I would like to mention the main topics discussed in the interviews, and then to analyze them by comparing the theory with the practice.

- ***Foreign Entry Mode Decision***

According to the theory, the companies are expected to choose an entry mode that suggests the highest risk-adjusted return of investment. Entry mode choices are often, choices and compromises between the resource availability and control.

Vienna Insurance Group entered the Bulgarian insurance market by acquiring local insurance companies.

The control between the Headquarter in Vienna and its affiliates in Bulgaria happens, in this case, through daily communication and by managers who are specifically responsible for the business coordination between the companies.

As Mrs R. Gergova reported, Vienna applied very strict control to administrative costs. Various business and financial reports are used additionally in order to gain a clearer picture of the financial results and to assess the success of foreign investment. Discussing resource availability, it is very clear that the most important influence on the foreign entry decision has been the human resources, local know-how and experience.

In our conversation, Mr Mühleder underlines that the composition of human resources is one of the reasons for foreign entry through acquisition, since the acquiring of a local company allows the legacy of highly experienced staff, local contacts, know-how and specific culture to be preserved, which is a huge advantage. The strength of the staff is one of the reasons for the success of the post-acquisition process.

Comparing Greenfield investment to acquisition it can be stated that it would be much more difficult for a company to start “from scratch”, and especially in such a sector as insurance, which was completely underdeveloped until the transformation process in

1999. In this context the choice of the target company (Bulstrad) was crucial, since this local company has a long history (50 years) and a great deal of experience in the insurance sector.

On the other hand, becoming an owner of an existing company, which has already established its corporate culture, could be a challenge in terms of adapting and fitting the local company to the new owner's culture.

- ***Assessment of the investment location Bulgaria***

Despite the financial crisis, Bulgaria still tends to be an attractive location for FDI flows. The expectation of future development of the market and rapid economic growth have been motivating a great number of foreign companies to expand their businesses into the country.

The interview partners do not consider the level of corruption, the slow administrative procedures or the loss of infrastructure as serious problems or hurdles in conducting business. This is particularly from the perspective of the insurance companies, which do not supply material goods.

- ***Delegation of authority/decision making***

Discussing how the coordination between the Headquarter and the affiliates works, we can conclude that the key strategic decisions are exclusively made by the main shareholders (Vienna Insurance Group), whereas the local management is delegated with the operational decisions.

According to Mr K. Mühleder, expatriates have been playing very important roles within the coordination process since they facilitate knowledge transfer and corporate culture on one side, and act as intermediaries between the headquarters and the local company on the other.

- ***The financial crisis and the Bulgarian insurance market - consequences and expectations***

The economic stagnation is clearly acknowledged by both of the interview partners. Mrs Gergova sees the reasons for this as lying mainly in the reduced income caused by high unemployment rates on the one hand, and the increasing prices of basic necessities on the other.

Asked to give a non-binding prediction, Mrs Gergova said that in her opinion the crisis is likely to start easing off, and that the company expected to return its lost customers within the next 1-2 years.

Mr Mühleder pointed out that in principle the insurance market is unattractive in terms of current profit and compared with Austria is more underdeveloped, but that there are good opportunities to profit from the future potential, including the expected increase in the need for insurance products and the development of the market.

However is a fact that the market share of the company is expanding constantly and although the common falling in insurance market, Bulstrad is the only company with a growth of premiums.

- ***Restructuring, reorganisation and changes after the acquisition***
- After the acquisition the company strategy and structure remained almost the same. Concerning the price and product policy there were only a small number of tariff changes - these were necessary due to the current market and economic situation. Some of the existing products have been released, others have been improved. According to Mrs Gergova, the implementation of innovative products or changes in prices always needs to be carried out by local experts, since the insurance market in Bulgaria is different.
- ***Cultural differences/fitting in with the culture of the acquired company***

When discussing on MNC (Multinational Company) the different cultures and cultural dimensions have been always vital topics.

As Prof. Dr. Hofstede G. (2003) stated:

*"Culture is more often a source of conflict than of synergy. Cultural differences are a nuisance at best and often a disaster."*

According to my interview partner Dr Mühleder, managing people from different cultures is a challenge which should be taken very much into account.

Vienna Insurance group is acting in the whole CEE region in nearly 25 countries and is dealing with such cultural differences – and exactly how the newly acquired companies fit best into its corporate culture is an ongoing learning experience which must be continually extended and enriched.

In terms of human resources (Bulgarian and Austrian), according to Mr Mühleder, there are some differences in team approach, decision making, time management and setting/meeting of deadlines, as well as feedback reaction to critical appraisal.

- ***Measuring the success of investment***

"The success of investment is measured by the market position based on premium income, by technical results and financial results, by the percentage of administrative costs in the premium , by the increase in technical reserves, which best indicates positive business development and by the profitability of the investment portfolio."

Mrs.Rumyana Gergova

- ***The "key of success" for Vienna Insurance Group***

Vienna Insurance Group have realised on time the chances offered them in the CEE countries, and more concrete in Bulgaria and had used the chances to expand into such developing and economic rapidly growing area. The company has gain its experience in a great number of sequential entries in the CEE most of them through vertical acquisitions.

Both of my interview partners attribute the success of the company to the long business tradition and well-established brand name of Bulstrad, the high level of technical experience and know-how resulting from its 50 year history, the highly qualified staff, and the fact that the company relies heavily on local entrepreneurship and benefits from retaining local key employees. This is not, however, at the expense of maintaining diversity and internationality in terms of human resources.

In summary, the company profits greatly from the arising opportunities which the CEE region offers. This is possible due to its sustainable policy of enlargement combined with a professional customer focus, but also with the careful market selection. The company uses best practice programs in order to succeed in offering the highest level of products and services, matching the needs of the local customers. Vienna Insurance Group aims to maintain its position as insurer leader in the CEE. The realisation of growth and expansion in the CEE region has been always among the objectives of the Vienna Insurance Group.

The company also succeeds due to its quick, flexible adjustment to the conditions of the local markets, as well as the broad spread of distribution channels across the foreign countries. New, tailor-made insurance products, developed exclusively for where they are needed, also contribute to the success.

## **8. Conclusions**

In the continuing globalisation of the economy and expanding businesses, a better understanding of FDI and international management is of crucial importance. When the domestic market has become small and saturated, the opportunities offered somewhere outside the country of origin act as stimuli for entering foreign markets. Factors such as the local economy, legal systems, government policies etc. also affect international business. Therefore, specific knowledge and careful evaluation of the location of expansion should be considered in advance.

The transformation of the former planned economy to a market economy and the opening of the market to foreign companies have added to economic development in various ways.

Most of the world's largest firms have their wholly-owned subsidiaries outside their countries of origin, initially established as Greenfield or acquisition. The development of the business after an acquisition, the coordination between the central office and its subsidiary and how to manage people from different cultures successfully are all challenges inherent in the internationalisation process.

This paper has shown, by using personally taken interviews, that despite the difficulties caused by the financial crisis, Bulgaria still tends to be attractive for FDI flows and that having a successful business in Bulgaria is not only a "vision".

Moreover, the general view which relates the country to factors such as corruption and bureaucracy, and depicts a place where unwritten rules and laws play the most important roles, was not confirmed and even refused by all of my interview partners.

The investigated company (Vienna Insurance Group) have expanded to almost 25 CEE countries using the rapid entry mode of horizontal acquisition, which provides fast access to distribution channels, access to existing customers, and in the case of entering Bulgaria, a well-established brand name with extensive experience. In this way it was possible to overcome some of the barriers of internationalisation, such as limited local know-how/knowledge of the peculiarities of the local market (specifically the insurance sector) in such a transitional economy as the Bulgarian.

The analysis of the theory, compared with the practice, sheds light on the main factors which influence the foreign entry decision. It contributes to lessons which can be learnt on the process of control and coordination between the headquarters and its affiliates, and on challenges associated with the integration of the corporate culture with the newly acquired company during the post-acquisition process, giving an example of how to be successful in an international context.

## **APPENDIX**

Interview with Fabrice Reynaud,

Source: [www.econ.bg](http://www.econ.bg), accessed on 27.04.2010

*The interview is taken by **Kaloyan Staykov, econ.bg***

Econ.bg:

Mr. Reynaud, the SCE region has attracted around 25% of FDI in Eastern Europe and Bulgaria has benefited greatly. Since the country has acceded to the European Union can we expect a relative decrease in FDI in the following years - due to the financial crisis on one hand and due to the inability to take advantage in programs targeted at countries outside the EU? In your opinion how important is the absorption of EU funds as part of the FDI flow?

Fabrice Reynaud:

The EU accession is rather a driver to increase FDI projects, as it gives more predictability to the international investors.

Econ.bg:

International business leaders point out that Bulgaria is most likely to improve its attractiveness in the following three years. In your opinion what is the cause of their optimism - the relatively low base of comparison with past performance, strong government commitments, the flexibility of the local business or other reasons?

Fabrice Reynaud:

The confidence regarding Bulgaria can be mainly interpreted as the country with the most growth potential. Investors seek return on investment for their development, and it is easier to reach in fast growing countries.

Econ.bg:

What are your projections regarding the size of the expected FDI flow in Bulgaria in 2010 - either in absolute or relative terms?

Fabrice Reynaud:

Bulgaria experienced a severe decrease in 2009 in the number of foreign projects, so it is probably fair to say that 2010 will be between 2009 and 2008 figures. On average between 2004 and 2008 Bulgaria welcomed around 60 projects per year (including green field, extension, but no M&A)

Econ.bg:

Despite the strong macroeconomic position of the country, there are some fiscal concerns both domestic and international - Greece notably. How sensitive do you think is FDI flow to these risks and what policy measures can have a beneficial effect on the attractiveness of the country?

Fabrice Reynaud:

As we said during the presentation of our report - Bulgaria is one of the few countries that is matching the Maastricht criteria today.

Econ.bg:

Although international investors are looking for new market possibilities as they see new profit opportunities, do you think their prospects can be dimmed by the increasing share of sovereign debt? Accumulating debt now is likely to result in higher taxes and slower growth in such countries and investors can't be expected to expand abroad when they have problems in their back-yards. Does such a risk exist and how plausible is it?

Fabrice Reynaud:

For the biggest players, for global companies, they balance their risk among their locations/countries portfolio.<sup>47</sup>

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<sup>47</sup> The interview is taken by Kaloyan Staykov, [www.econ.bg](http://www.econ.bg)



Source :www. Econ.bg, accessed on 27.04.2010

*The interview is taken by **Kaloyan Staykov, econ.bg***

Interview with Dr. Michael Angerer, Commercial Counsellor, Austrian Embassy in Bulgaria

**1. What are your main tasks as the Commercial Counsellor at the Austrian Embassy in Bulgaria?**

My position in Bulgaria is both as a Commercial Counsellor and as a representative of the Austrian Chamber of Commerce. My main task here is to support Austrian business in Bulgaria and in particular Austrian companies, which are looking for commercial information and business partners in Bulgaria, and for export, import, and investment opportunities. The other important task I have is to get in touch with Bulgarian institutions and companies and to bring them in contact with Austrian companies and business. Thus, in general, I am working to improve the already existing very good trade relations between Austria and Bulgaria.

**2. In your opinion, what has been your most challenging task here until this moment?**

I am lucky to have a really interesting job because of the many things going on in Bulgaria in the business sector. As a challenging task, I can mention one project which could have worked on a very high level but was not realized because it coincided with the start of the crisis. We were working very eagerly on the project, which was a new steel production facility on the Black Sea. It is the first Alpine Project, a project similar to Kremikovtzi but even bigger. It was supposed to be completed by 2013 but was postponed because of the crisis.

The challenge for me was the preparation for the project. I had to get in touch with government and local authorities, with companies that were going to build the steel plant, and others. There was one positive effect from this preparation for the project though. The Bulgarian Ministry of Economy realized it had to start supporting the

establishment of industrial zones. Until that moment, Bulgaria had no promotion schemes for industrial zones, unlike other new EU member states like the Czech Republic, which has really good system for setting up such zones. The Bulgarian authorities found out that it would be necessary to have such industrial zones, and I believe that to a certain extent, the Alpine project pushed them in this direction. Now, two months later, the Ministry came up with presentations and plans for industrial zones. Thus, this unrealized project was a little push for the Bulgarian Ministry. Industrial zones are a hot topic right now because there is competition between countries that want to attract more investors by offering better facilities.

#### **4. How would you qualify the investment climate in Bulgaria?**

The investment climate in Bulgaria has been very good for the last few years. The crisis this year surely affects it. However, it was good because Bulgaria has a growing economy. Investors are coming to a country in which they can participate in the development – not only in real estate but also in services in all fields. They come to a market on which they can sell more products because there is a high and growing demand. For the moment, however, demand is reduced and prices are not going up. I hope that Bulgaria will come back to its previous levels of growth faster because there is too much to be improved here, like infrastructure and others, in order for the country to catch up with the rest of Europe.

#### **What are the five positive things you would tell a potential foreign investor in Bulgaria?**

The first thing is that Bulgaria is a growth market. It is dynamic and has potential to grow. The second is the low taxation, which is a good benefit. The third thing is the relatively low level of costs to operate in a country, which is a member of the EU. The fourth positive aspect is the friendly mentality of people. Bulgarians are people with whom you can start a conversation and strike a deal. The fifth thing, which is strictly from Austrian perspective, is the geographical proximity. This is important because

Bulgaria is not on the other side of the world. Small and medium Austrian companies are quite attracted to come here because they find it easier and accessible.

**5.) What is the main attraction for Austrian companies to invest in Bulgaria?**

The main attraction for Austrian companies is the growth market. All kinds of products and services are needed in Bulgaria. There is a lot to improve, so there are many opportunities for foreign investors to enter the Bulgarian market.

**6.) What are the most interesting sectors in Austria for Bulgarian investors?**

As far as I know, there are not that many big Bulgarian investments in Austria. Traditionally, there are smaller companies, mainly real estate agencies and private persons that settle in Vienna because it is close both to Bulgaria and to other European countries. Also, companies open their subsidiary branches in Vienna and operate from there in order to reach the rest of Central and Western Europe. I would say this is a clever step and should be encouraged because Bulgaria needs to export as much as possible. By settling in Vienna and working from there, companies can learn a lot and can achieve more within EU.

**In your opinion, how is the flow of foreign direct investments from Austria to Bulgaria going to be affected by the global crisis?**

For now, Austria is extremely well set-up in Bulgaria. The total of Austrian FDIs to Bulgaria until 2008 is 6.5 billion EUR. There is a sharp reduction in Austrian FDIs this year according to BNB. Still, Austria is among the top investors. This year is relatively weak because Austrian investors are conservative when it comes to new investments. However, this is true not only for investing in Bulgaria but in other countries as well. I have the hope that after the crisis, there will be a shift in investments. They would not be that concentrated in real estate but other opportunities will be explored as well. Bulgarian companies would look for partners or

even for options to sell their companies. There would be a shift to production, take-over opportunities, and acquisition of companies for reasonable prices.

**7.) What are your recommendations for the improvement of the investment climate in Bulgaria?**

Quick decision-making by authorities is very important for investors, especially when it comes to administration. Time is money, and you cannot wait for years to get a decision. The other significant problem is transparency in general, and specifically for public announcements and tenders. These are the problematic issues that I get as feedback from Austrian companies which have to wait to get permissions for operation here. For example, a company wanted to start its operation in a plant, but the road to it was not built. The company was even ready to pay for the construction of the road itself. However, it needed permission for this. It had to wait for the permission to get through the administration and could not start working until then. Such situations are obstacles to good business.

**8.) Finally, do you think cultural differences matter in investments? Could you please tell us a story from your experience in Bulgaria?**

As Austrians, we can very well communicate with Bulgarians. We have had exposure to South-Eastern Europe. We know Bulgarians much better than other Western Europeans. Nevertheless, there is a different way of thinking here. It is usually a kind of short-term thinking. Everything can work very well in the short run. However, if you plan ahead and if you have a business plan for the next two years, this is a very long term for Bulgaria. In life, this is quite pleasant because planning too far in the future is burdensome. In business, however, this approach is not that useful.

An example for this cultural difference is the preparation of the special event we wanted to make in order to welcome Bulgaria in the EU. I think it was very well organized, almost two months in advance. The idea was to welcome Bulgaria with really good feelings in the EU. We had invited a minister to the event, and he had agreed and was quite enthusiastic about it. Then, an hour before the event, he

cancelled his appearance. He had no bad feelings – but he also didn't have a sound reason not to attend it. I believe he didn't perceive it as such a serious arrangement, but there were no bad feelings in this. We were lucky there was another minister who could attend it, and it all worked out in the end. In Bulgaria, when you plan in the long term, there are more obstacles to the realization of the thing. However, if you call somebody and ask them to meet you in an hour, it works. This is a big cultural difference. I got used to it, but for people who come from Western Europe or USA, this Bulgarian peculiarity is a problem. They feel offended by it because they don't understand it as a cultural difference. Thus, it can turn into a problem for business. If you understand it, you can live with it.

**Dr. Angerer, thank you very much for the interview. We would like to wish you every success in all your future professional endeavors'.**

Dr. Michael Angerer, Commercial Counsellor, Austrian Embassy in Bulgaria

Source:

<http://www.italkcash.com/forum/general-investment-opportunities/177180-michael-angerer-austrian-commercial-counsellor-bulgaria-interview.html>  
accessed on 25.05.2010

## **Personally taken interviews**

### **Transcript of Interview 1**

Interview partner: Mrs. Romyana Gergova,  
Financial Manager, Bulstrad LIFE Vienna Insurance Group JSC/Affiliate of Vienna  
Insurance Group in Bulgaria  
given on 16.07.2010 , at 11 am

#### **Iskra Kostadinova:**

Mrs. Gergova, firstly I would like to thank you for your time and for agreeing to this interview which is part of my master thesis.

Here are my questions:

As CFO of one of the most successful insurance companies in Bulgaria, how would you describe the economic and political situation in the country? What are the difficulties the company currently faces in its activities?

#### **Mrs. Romyana Gergova:**

Overall, and due to the global economic crisis affecting the European Union member states as well, the situation in both aspects is more or less volatile. Being a part of an economical entity Bulgarian economy is inevitably influenced by the economic stagnation. In particular, our core business is directly affected by these negative changes, since our current and potential clients experience the economic difficulties even more directly themselves. The reduced income, caused by high unemployment rates and increasing prices of basic necessities, leads to decline in insurance demand and higher buying out rates of the existing policies.

#### **Iskra Kostadinova:**

Could you confirm that since your company became part of Vienna Insurance Group, it was able to keep its existing clients and attract even more new customers?

**Mrs.Rumyana Gergova :**

Generally yes. The fact is that our company from fifth in the life insurance market rating in the end of 2009 improved its ratings since and currently is in the top three.

**Iskra Kostadinova:**

It is interesting in terms of human resources,are the Bulstrad management positions filled by people selected directly by the central office of Vienna Insurance Group or you are authorized to select and appoint the staff here?

**Mrs.Rumyana Gergova :**

All employees of Bulstrad Life Vienna Insurance Group are selected by us and appointed by the local management.

**Iskra Kostadinova:**

What has changed in the "Bulstrad" after "Vienna Insurance Group" has become your main shareholder? Did the company start an entire reorganization or continued to follow its previous strategy and the organizational structure remained the same?

**Mrs.Rumyana Gergova :**

In general, the company strategy and organizational structure remained more or less unchanged. Naturally, the current market situation and the new owners require some changes, but these have not been in any way drastic.

**Iskra Kostadinova:**

Did the management style and principles of the company change and if so, in what direction? In which of the following aspects did they change:

a / pricing policy

b / product range

c /company mission and vision.

**Mrs.Rumyana Gergova :**

As mentioned above, changes are necessitated primarily by the new developments in the insurance market leading to some tariff changes, whilst in response to demand new products have been released, or the existing ones have been improved in order

to enhance company compatibility. The company's mission and vision are determined by our strategic objectives, consistent with the shareholders views of business development.

**Iskra Kostadinova:**

6. As we know, life insurance is an underdeveloped part of the Bulgarian market in comparison with property insurance. Can you say that after "Bulstrad" became part of "Vienna Insurance Group ", you have achieved better results in this direction?

**Mrs.Rumyana Gergova :**

Definitely. The fact is that, as mentioned above, we are constantly expanding our market share size. Significantly, in 2009 and the first half of 2010, within the background of a falling insurance market, Bulstrad is the only company with a growth of premiums.

**Iskra Kostadinova:**

Are the products you offer the same, or had the Headquarters developed new products created specifically for the Bulgarian subsidiary company?

**Mrs.Rumyana Gergova:**

In general the products are more or less the same. We receive logistical support from the Headquarters in Vienna based on the advanced insurance practice and experience there. Overall pricing, product improvements and innovations in our company are carried out entirely by local experts as the market in Bulgaria is very different.

**Iskra Kostadinova**

How does the coordination between the Headquarters in Vienna and Bulstrad run?

**Mrs.Rumyana Gergova:**

By daily communications in both directions and by managers who are specifically responsible for business coordination with our company.



**Iskra Kostadinova:**

How does the planning and development of corporate strategy materialize?

**Mrs.Rumyana Gergova:**

Vienna has the full control over the business and the results. There are monthly and quarterly reports which give a clear picture of the business and financial results. Very strict control is applied to administrative costs. The company's investment policy and the levels of income from investment of funds are monitored.

This information is used as a planning framework for subsequent years, for preparing the business lines budgets, and is presented at the headquarters in Austria to be approved by the supervisory board. The strategic objectives are determined by the representatives of the shareholders and on the whole they are aimed to achieve front market positions and profitability.

**Iskra Kostadinova:**

Are the important business decisions dictated by Vienna or you are authorized to take independent decisions in Bulgaria?

**Mrs.Rumyana Gergova:**

In Bulgaria we concentrate on the operative activities of the company, and with regards to these activities the management here is authorized to make decisions. Strategic decisions relating the future development, equity, and general management are set in Vienna.

**Iskra Kostadinova:**

As a Bulgarian who lives in Austria, I fully realize that despite the geographical proximity between the two countries / Austria and Bulgaria/, there are many cultural differences between us. For me it would be very interesting to learn more from your experience, what cultural differences exist between you and your Austrian partners in business context?

**Mrs.Rumyana Gergova:**

It is difficult for me to answer this question, since our Austrian partners do not seek to impose their governance model in our country, but act in accordance with the local

situation. They draw the global framework and ensure budget implementation, evaluate achievements and employ company strategy, whilst the operational management is in the hands of the local managers.

**Iskra Kostadinova:**

According to a theory, ROI (Return on investment) and ROS (return on Sales), as well as market share size is often used as tools to measure company success. By what methods and criteria is the success of "Bulstrad" in the Bulgarian insurance market measured?

**Mrs.Rumyana Gergova:**

It's measured by the size of the market share, by the market position based on premium income, by technical results and final financial results, by the percentage of administrative costs in the premium, by the increase in technical reserves, which best indicates positive business development, and by the profitability of the investment portfolio.

**Iskra Kostadinova:**

What is the key to "Bulstrad" success?

**Mrs.Rumyana Gergova:**

The question is interesting. But perhaps summed up the success is a result of very good operational management, of a long tradition in the Bulgarian insurance market /the brand Bulstrad has been in the Bulgarian market for the last 50 years, whilst the life insurance group has been there for the last 15/, and the contribution of many innovative, young and ambitious, highly competent professionals.

**Iskra Kostadinova:**

From your position, could you make a non-binding prediction as to what opportunities and risks may be expected in the Bulgarian insurance market in the following five years?

**Mrs.Rumyana Gergova:**

Presuming that the crisis once reaching its lowest point should start easing off, the chances are that we will see an economical revival, higher exports and domestic consumption. Our business should also emerge from the stagnation and during next one to two years should recover its lost positions. In Bulgaria this segment, especially life insurance is quite undeveloped, so I hope there will be a positive development.

## **Interview 2**

Vienna Insurance Group /Affiliate Bulstrad Vienna Insurance Group,

Interview partner: Dr. Klaus Mühleder, Deputy Chairman of the management and Executive Director of Bulstrad JSC, Bulstrad Life JSC, Bulgarski Imoti JSC

**9<sup>th</sup> August, 15 pm**

### **Transcript of Interview 2**

#### ***Iskra Kostadinova:***

Dear Mr. Mühleder, what is your exact position in Vienna Insurance Group? I would like to learn more about the specification of your job and your main tasks.

#### ***Klaus Mühleder:***

My position is a “Deputy Chairman of the Management Board” and “Executive Director”. My function is Chief Financial Officer: as a Deputy Chairman I have to run meetings in the cases of absence of the Chairman.

As a CFO (Chief Financial Officer) I am mainly responsible for managing investments financial risks, for providing the main shareholders and the management with reliable information and data from the financial point of view. This includes inter alia the preparation and proceeding of monthly, quarterly and yearly financial and management accounting reports.

In terms of investments, the essential function of my work is the management of investment, in terms of adequate return safety and liquidity, as well as keeping regulatory provisions in respect of assets.

***Iskra Kostadinova:***

In your opinion what are the main problems you have to face up in Bulgaria? What has been the most challenging task since you have been working as a “Deputy Chairman of the Management Board and Chief Executive” from Bulstrad JSC?

***Klaus Mühleder:***

I am not sure what do you mean with “challenging”.

***Iskra Kostadinova:***

I mean for example the red tape and the long administrative procedures, the corruption, the lack of developed or the not enough developed infrastructure or some other circumstances which are usually hurdles to the foreign companies investing in Bulgaria and participating in Bulgarian business circles.

***Klaus Mühleder:***

I haven't had problems with the corruption, or with the lack of infrastructure .For example the bad roads are not a particular problem for our company, since we do not produce and supply material goods, bad roads are an inconvenience for other sectors they are certainly a bigger hassle.

For me, the challenges are more connected with the cultural differences between people in a business context.

There are two ways of dealing with the cultural difference, either to ignore it completely and to deal in your way as you are used to or to be very flexible, to try to adapt and respond to the local culture.

I will give you an example: a contract in Austria means that all parties expect to be very strictly bounded to their contractual obligations.

In Bulgaria, I have seen many contracts “annexed”- and people have given me the impression that changing contract does not seem to be an issue.

As an expatriate, dispatched from the Headquarter you have to learn how the business works locally or with other words how to work with people from different culture and how to manage them locally successful.

The challenge is more in managing people, and in particular managing people from different cultures. Also I believe that every company has its own corporate culture, organizational structure, written, as well as, unwritten ethic rules, etc.-for example

McKinsey tend to hire people with similar characteristics, people which fit in a best way with its company culture and I guess this is true for most corporations.

Now, Vienna Insurance Group has subsidiaries in ca 25 countries. When we are talking about Human Resources of the company, the key words are “diversity” and “cultural particularities”.

One of the main differences between a Greenfield investment and an acquisition persist in the composition of their Human Recourses.

When you start up a Greenfield you start a completely new business entity and have first to find and appoint new employees, where the „corporate lion” in hiring may be much stronger.

On the contrary in a case of acquisition you become an owner of an already existing company, which has its corporate culture already built. The people are there with their know-how, personal contacts, and local experience, as well as their specific culture.

Bulstrad is a company with a long history-nearly 50 years and hence a strong personality. The staff of the company has a great technical experience and excellent know-how. So it depends very much on the context in terms of corporate culture.

***Iskra Kostadinova:***

From your position, how would you describe and evaluate the current business situation in Bulgaria? Could you say, that the country is still attractive for the foreign companies, and in particular for the Austrian companies as an investment area?

***Klaus Mühleder:***

Well, I cannot speak generally. I could only refer to the insurance sector. It is definitely more difficult as before, since the insurance market from Bulgaria is per se not very unattractive in terms of current profit.

The people are used to close only the MTPL and maybe Auto Kasko, as in Bulgaria the possession of a car is seen as an important asset.

Given the low MTPL tariff, insurance lines is not very low, whereas the commission which we have to pay to our insurance intermediaries is high. The risk is too high, compared to the premiums of Citizen Responsibility which are very low from one side, and the commission which is to be paid to our brokers is very high from other side.

The demand of other insurance products like life insurances or household insurances is very low, compared to this in Austria for example.

But if you are meaning “attractive” in a sense of future potential, I would definitely say, yes. So for us being in Bulgaria means being ready to benefit from the potential in and to be present in the entire CEE –since VIG is a CEE player. The unknown factor is the time.

So if there would be a possibility for future development like increase of our market share or additional demand for insurance products, Vienna Insurance Group is already in Bulgaria and that as a leader. We are proud that we were selected for insurer of the year 2009 and 2008 and it underlines the strengths of our staff.

***Iskra Kostadinova***

According to the theory, ROI and ROS, as well as the reached market share and the volume of sales are often used for the measurement of business success. How does Vienna Insurance Group measure the success of its foreign investment?

***Klaus Mühleder:***

It is measured by market share, Return on Equity, Return of Premium, and Return of Investment, but also by technical parameters, such as Cost and Loss ratios.

***Iskra Kostadinova***

What methods of control are used by the Headquarter in Vienna?

***Klaus Mühleder:***

Above parameters and qualitative reports.

***Iskra Kostadinova:***

Where are made the strategic decisions? And further my question would be how standardized and strict are the procedures and rules exerted by the Headquarter in Vienna to its local subsidiaries?

***Klaus Mühleder:***

It depends how you define “strategic”. Of course, we are allowed to take decisions independently on an operational level.

In case of major changes in structure, board issues, expansion we are clearing the decisions according to the by-laws, through the supervisory board and general meeting. In any case, Vienna Insurance Group is highly involved in making the important decisions, and that is absolutely understandable as they are the main shareholders, who predominantly act through the Supervisory board.

***Iskra Kostadinova:***

How important is the role of „dispatching expatriates” in managing the local subsidiary according to the cooperate culture of Vienna Insurance Group?

***Klaus Mühleder:***

It is very important, as this is an efficient way to facilitate know-how transfer, corporate culture, etc.

In general, VIG sends highly qualified staff with experience in both insurance and VIG culture. The expatriates hence are not only transferring know-how but also act as intermediaries between HQ and the local company.

***Iskra Kostadinova:***

Particularly interesting would be the question how does the Headquarter (Vienna Insurance Group) proceed in a case when the local benchmark changes for the worse. Could be a possible decision to dispose of Bulstrad JSC?

***Klaus Mühleder:***

This question is to be answered by the shareholders, rather than me.

In principle, I would say, I cannot imagine VIG to leave a country fully. Maybe to dispose of an individual company would be a possible decision. A total exit may be taken in case of dramatic changes in terms of the business environment of a company e.g. expropriation.

***Iskra Kostadinova:***

As a Bulgarian who lives in Austria, I fully realize that despite the geographical proximity between the two countries / Austria and Bulgaria/, there are many cultural differences between us. For me it would be very interesting to learn more from your



experience, what cultural differences exist between you and your Bulgarian partners in business context?

***Klaus Mühleder:***

In my opinion, the cultural differences, could not be overbear completely.

In business context, I would say that there are some differences in team approach, decision making, time management and deadlines, as well as feedback reacting to praise or critics.

***Iskra Kostadinova:***

In your opinion, what is the key to “Vienna Insurance Group „ success?

***Klaus Mühleder:***

The question is really hard to answer or there are most likely many factors, as well as “fortune”.

Maybe the pragmatic approach, less tendency to changes and the fact that our subsidiaries are much more locally driven. When we look at, for example, US companies, their strategy is, to my knowledge and experience, to have a much more rigorous approach, more regulated, exceptions not allow.

Vienna Insurance Group tends to be an original player and that in everything. Of course we have our best practices, our ethic rules, business guides etc. as a part of our corporate style and organizational culture. But furthermore we really rely on local entrepreneurship, retaining the local key employees, diversity and internationality in terms of our Human Resources.

The top management of Vienna Insurance Group is really multicoloured. There are managers from Hungary, Czech Republic, Austria; we also have gender diversity on the board of management.

Vienna Insurance Group wants to remain a leader and I think the key is to be from one side flexible and partnership driven and of the other side its pragmatic approach.

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## Abstract Deutsch

Es gibt eine Vielzahl an unterschiedlichen Theorien, Studien, Modellen und Recherchen über die Relevanz der Wahl der richtigen Markteintrittsstrategie in einen ausländischen Markt.

Die entsprechende Literatur betrachtet in erster Linie die Entscheidung zwischen ausländischen Direktinvestitionen und Export sowie zwischen „greenfield investment“, „brownfield investment“ und Akquisition.

Heutzutage haben viele österreichische Unternehmen nach Osteuropa expandiert – mit der Erwartung, die Internationalisierungsbarrieren zu überwinden und von den zusätzlichen Möglichkeiten, die ihnen am heimischen Markt selbst nicht zur Verfügung stehen, zu profitieren.

Das Ziel dieser Arbeit ist auf der einen Seite, ein breites Spektrum an Theorien sowie die wichtigsten Aspekte, die mit der Entscheidung, in einen ausländischen Markt einzutreten, verbunden sind, aufzuzeigen und andererseits anhand eines konkreten Fallbeispiels – Markteintritt der „Vienna Insurance Group“ in Bulgarien – zu untersuchen, wie die Theorie in der Praxis funktioniert.

Bulgarien ist einer der typischen Vertreter der „Übergangswirtschaft,“ die durch ein sehr rasches Wachstum und ein hohes Entwicklungspotential gekennzeichnet ist.

Die Vorstellung des Landes, die Einschätzung von Bulgarien als Investitionsplatz, die gesetzlichen Rahmenbedingungen betreffend die ausländischen Direktinvestitionen sowie die anfängliche Entwicklung und gegenwärtige Situation des bulgarischen Versicherungssektors sind Teil dieser Arbeit.

Die persönlichen Interviews sollten Antworten auf folgende wesentliche Fragen geben:

Welche Faktoren beeinflussen die Wahl einer Markteintrittsstrategie?

Welche Veränderungen in der Unternehmensstruktur und Unternehmensstrategie erfolgen in der Post-Akquisitionsphase?

Wie erfolgen der Koordinationsprozess und die Kontrolle zwischen der Zentrale in Wien und der Tochtergesellschaft in Bulgarien?

Wie werden die wichtigsten Entscheidungen getroffen?(Wer ist wofür zuständig?)

Was sind die größten Hürden, vor denen ausländische Unternehmen, die am bulgarischen Versicherungssektor tätig sind, stehen? usw.



Die Analyse der theoretischen Ansätze verglichen mit einem konkreten Fallbeispiel soll die wichtigsten Faktoren, die die Wahl einer Markteintrittsstrategie beeinflusst haben, erhellen und aufzeigen, wie Unternehmen im internationalen Kontext wettbewerbsfähig sein und bleiben können.

## Abstract English

Great number of theories, studies and theoretical models emphasize how important the choice of a certain foreign entry mode is.

The relevant literature discusses primarily the choice between FDI and Exporting, as well as the choice between Greenfield investment and Brownfield investment.

Today lots of companies have expanded their businesses in Eastern Europe, expecting to overbear the barriers of internationalisation and to benefit further from the opportunities not available in their home market, but might be possible somewhere else.

In this context the purpose of this work is to present a wide spectrum of the theory and the most important issues about the entry mode from one side and to oversee how theory works in the practice on the other, with the help of a Case Study – “Vienna Insurance Group enters the Bulgarian Insurance Sector”.

Bulgaria is a typical representative of the transition economies which has been developing very fast recently. The presentation of the country, the evaluation of Bulgaria as an investment location, the legal framework, concerning Foreign Direct Investment as well as the initial development and the current situation of the Bulgarian insurance sector are part of this work.

The personally taken interviews are used to find answers of the questions about the factors which have influenced the foreign entry decision making, the changes due to the post acquisition phase, the process of coordination and control between the Headquarters and its affiliates, and the main hurdles and problems in front of foreign companies dealing at the Bulgarian insurance market

The analysis of the theory, compared to the practice is aimed at better understanding of the main factors influencing the foreign entry decision making and learning lessons about how to be more successful internationally.

## Lebenslauf



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