

THE DEVELOPMENT OF THE PRIMARY SECURITIES MARKET IN BULGARIA - AN IMPORTANT FACTOR TO SUPPORT THE ECONOMY IN TIMES OF CRISIS

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РАЗВИТИЕТО НА ПЪРВИЧНИЯ ПАЗАР НА ЦЕННИ КНИЖА В БЪЛГАРИЯ - ВАЖЕН ФАКТОР ЗА ПОДКРЕПА НА ИКОНОМИКАТА В УСЛОВИЯ НА КРИЗА

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Резюме: В развитите страни по състоянието на пазарите на ценни книжа се съди за цялостното икономическо положение на страната. Особено в условията на криза пазарите са много чувствителни и бързо реагират на промените в средата. Историята познава много финансови кризи, но днес човечеството е изправено пред нов вид, а именно пандемията от COVID-19, която има характер на биологична война.

За излизане от кризата са необходими инвестиции, които не винаги могат да бъдат осигурени от самите предприятия или от банките. Затова емисията на първичните пазари на акции и облигации е алтернатива и много добър ход за набиране на капитали. Още повече, че рано или късно кризите ще приключат, и пазарите ще върнат загубените позиции. Играчите на повишение – „биковете“, определено ще спечелят от покупко-продажбата на подценени активи, в т.ч и от емисия на акции и облигации. Ето защо, познаването на първичния пазар, неговите особености и начин на работа ще е от особена важност както за инвеститорите, така и за емитентите и всички, които вярват, че в бъдеще икономиката ще се възроди именно чрез развитието на капиталовия пазар.

Целта на настоящия материал е да характеризира особеностите на проявление на първичния пазар на ценни книжа в България и да покаже пътищата за използване на емитирането на акции и облигации като инструмент за увеличаване капиталите на икономическите агенти и за изход от кризата.

Abstract: In developed countries, the overall economic state of a country is assessed in relation to the state of the securities markets. In times of crisis in particular, markets are very sensitive and react quickly to changes in the environment. History knows many financial crises, but today humanity is facing a new type, namely the COVID-19 pandemic, which has the character of a biological war.

Investments are needed in order to get out of the crisis, which cannot always be provided by the companies themselves or by the banks. Therefore, the issue of equities and bonds on the primary markets is an alternative and very good move to raise capital. Additionally, sooner or later the crises will end, and the markets will regain lost ground. The so-called "bulls", will definitely gain from the purchase of undervalued assets, including by issuing shares and bonds. This is why, knowing the primary market, its characteristics and mode of operation will be crucial both for investors and issuers and all who believe that the future economy will be revived notably through the development of the capital market.

The purpose of this paper is to characterize the features of the manifestation of the primary securities market in Bulgaria and to show the paths to use the issuance of

shares and bonds as a tool to increase the capital of economic agents and to overcome the current crisis.

1. Initial public offering of shares

Our legislation treats the issuer as a "the person liable under the securities:

- a) which issues or has issued through an initial public offering, including the formation of a company;
- b) which are admitted to trading on a regulated securities market. "

Issue of securities occurs when:

- limited company launches first securities to increase its capital;
- limited company issue yet again securities in order to satisfy the increased financial capacity of their business. This can be done through "issuance of new shares by increasing the nominal value of the issued shares or conversion of bonds into shares".

Joint stock companies issuing securities can be public and non-public.

POSA defines public company as a joint stock company, which has issued shares under the IPO and/or is registered in the register of public companies in the FSC issue for trading purposes on the regulated securities markets. Public offering exists when the company makes a proposal for consideration the purchase or sale of securities to at least 100 persons or to an indefinite number of persons (including through the mass media).

Public offering may be primary or secondary. The IPO is generally the process of issuing securities under certain legal requirements. A joint stock company may issue shares, whether public or not. When a company is privately circulating securities ie the issue has not been done in terms of the IPO, it may become a public company when registering these securities on a regulated market (stock exchange).

Therefore, the emission securities market is one in which there is an issue and sale of financial instruments of public and non-public companies. Since a large part of the emissions are carried out under the initial public offering, the latter dominates on the primary securities market.

Issuance and sale of shares under the POSA. The process of an initial public offering (the so-called indirect or public issue) occurs in the following sequence:

- preparation of the issue;
- submission of the required documents to the FSC and authorization of the issue;
- providing the underwriting;
- selling the issue.

The preparation of the issue is a very important preliminary stage, tracing the future success in the sale of newly issued shares, whether this will happen in the very lending institution or exchange. When a company sells first issue of shares on the stock exchange, then in most cases this is the day of its introduction into the stock trade or conversion of the company in a quoted joint-stock company.

The candidate-issuer, but mostly selected investment intermediary (bank or financial brokerage house) conduct thorough preliminary work on the preparation of the issue.

Investment intermediary: provides consulting services to prospective issuer; prepares the necessary documents for resolving the issue; analyzes the the financial situation of the company; specifies conditions of issuing, underwriting and placement of securities. After completion of preliminary talks between the candidate issuer and

investment intermediary a definitive agreement for public offering and sale of the issue, is signed.

The issue is authorized by the Financial Supervision Commission (FSC) on the basis of mandatory documents the deposited, one of the most important is the prospectus for the initial public offering.

In most countries, law and other legislation regulate the contents of the prospectus. In our country, it's POSA and Regulations Prospectus for public offering of securities.

The Prospectus contains information, divided into three documents:

- The registration document containing information about the issuer;
- a securities note containing information about the securities offered to the public or admitted to trading on a regulated market;
- a summary of the prospectus.

The signed prospectus by the issuer or an authorized investment intermediary, together with its statutes, the most recent annual financial statements of the issuer, audited by a registered auditor and other documents shall be submitted to the FSC together with an application for approval of the prospectus.

In some countries, pending approval of the prospectus by the competent authority shall be authorized the publication of the preliminary prospectus jargon known as a "red herring" (red herring). In Bulgaria, prior publication of a prospectus is not allowed, and for the establishment of such offense shall be punished with a fine, unless it is a crime.

Based on the documentation provided, the FSC within one month decides on the application for confirmation of a prospectus. Rejection usually occurs when a prospectus is not eligible or when affected investors' interests. Important requirement that must be respected by the companies is that the issue price of the shares is not less than the book value per share before the capital increase.

After approval of the prospectus by the Commission, the issuer or selected investment intermediary have the right to publish notice of a public offering.

The announcement of the public offering shall be published in the "Official Gazette" and in one national daily newspaper at least 7 days before the start of the subscription period or the beginning of the sale. So the public is informed that the company has the legal right to issue securities and that a subscription for the particular issue begins. Commencement of the public offering shall be the date of publication of the notice.

To enable investors to learn about the company and the issue of new securities which it offers, the public must have the opportunity to access current information. This information is usually obtained from the prospectus to be published in the press in the form of a brochure or otherwise. Especially useful is its publication on the Internet. The law prohibits disclosures to the general public, contrary to the stated in the prospectus. It is obvious that the prospectus is the most important document and for its preparation expertise and experience are needed that economists-financiers have. In future, this work will be increasingly run by financiers in the departments of the company, rather than by specialist consultancies. Another important point is disclosure. FSC, a regulatory body as well as investors must have current, accurate, complete and not misleading information about the company and issues of securities.

In most cases, the issuing company is not able to only assume for distribution and to sell the securities issued. Then the services of an intermediary are used, as the basis of a contract for assuming are determined the ways in which to achieve that activity.

According POSA "assuming" occurs when under contract with the issuer, an investment intermediary records (or is obliged to write) for his account part (or the entire issue) of securities and to offer initial public sale".

In practice, several forms of assuming securities are used:

- wholly or partly by assuming of the issue by the investment intermediary;
- assuming on commission basis;
- mixed form of payment.

The first form is totally or partly assuming the issue by the investment intermediary. When the assuming is whole, the intermediaries based on comprehensive, firm commitment, buy all securities. The latter are distributed among the general public at the expense of the underwriter, while in possibly the non-sale of shares, the risk and loss remains only with the intermediary. Such assumption of securities shall be made when the rating of the issuing company is high, the demand for stocks is high and the bank is secure in their placement. Otherwise, after a period, the non-sold shares of the issuing company remain in the bank's portfolio. This form of payment allows the intermediary to buy parts from the issue of securities on the basis of the so-called firm commitment with option rights. In this case, the bank buys parts of an issue with the stipulation that after a certain period and will buy other parts of it also.

In both variations of the first form of assumption, ownership of securities is transferred by sale of the bank underwriter, which then resells them to the public. Usually, the price at which the bank acquires shares is not less than the nominal value and the sale price is higher than the nominal value. In this case, the bank operates as a dealer and possible implementation of speculative buying and selling of emissions targets and parts thereof. At total or partial assumption for the intermediary's account, the emission market is a dealer market.

The second form of assumption is on commission basis. Here, the investment intermediary negotiates with the issuer for assuming of securities and their distribution in its own name and for the service he is paid a commission. Everything else remains for the issuing company, incl. risk and cost of the non-sale of securities. In this case, the bank operates as a broker and taking on commission basis, the emission market is brokerage.

The third form of assuming is called mixed or assuming on behalf and for the account of the issuer. Here the bank performs an intermediary role by engaging within a specified period to take for certain amount of marketing issue. The risk of failure of marketing is entirely on the issuer.

The final stage in the issue of securities is their distribution among the general public. It is essential that adequately shares and bonds to reach specific investors.

In world practice are known various forms of sale of securities. Very popular and broadly applicable is the public placement, which is subdivided into:

- disposal by public subscription with a proposal on hard or variable rate of the securities;
- transactions;
- disposal by sale of securities on the exchange.

Of these three types of public placement is the most applicable one is subscription, whether in hard or variable rate. It is known that a subscription is made open offer to all interested potential customers to take part in the filing and recording the purchase of securities of an issue. Comprehensive information about the issuing company, the type of securities emission, etc. can be found in the: notices in newspapers, letters from banks, especially in the prospectus. When disposing of

shares through public subscription, in the foreground stand out several major moments:

- the general public must be informed by the prospectus and the media to organize a petition;
- each subscription has firm deadlines - beginning and end. After its completion, recording of investors is not carried out;
- the subscription means that investors are willing to buy (and are obliged to do so) the amount of the nominal value of the issue, i.e. a number of securities offered.

Investors should carefully familiarize themselves with the features and the data in the prospectus and then the deadline to make application for the subscription. In this application it is necessary to indicate the amount or number of securities to be purchased.

The risk in the issuance of new shares is great for investors and for underwriters and guarantors. When selecting securities from new issues there are no agreed rules for investment. Naturally, the information contained in the prospectus approved by the FSC should be reliable and thus help to protect investors from delusions. However, it can not guarantee a high profit or prevent any losses. The fate of newly issued shares largely depends on proper targeting of the money collected in the company of reliable management and the market situation.

Another way for public sale of securities is by way of free sale. The banks, having published a prospectus for issue freely, without time limit, start marketing the securities. Typical here is that is declared only the beginning of the issue, rather than fix his deadline. An important point is that "the issuer may adjust to the demand by means of offering amount of securities and their rate." This means that a rate in the prospectus that will sell papers can be changed depending on the status of the secondary securities market. Durable issuers commonly use this method of marketing.

Sort of manner for public sale of securities is selling shares of a new issue on the stock exchange at the time of the introduction of the company in this market.

On the stock exchange is usually quoted already issued financial effects. Is not excluded, however, the ability to sell shares of new issues via the secondary market but this is subject to conditions. The most important part is the company and the issue of shares to be admitted by the competent authorities to trade. On the exchange the stock price is not firmly fixed, and is determined by a number of economic, political, psychological factors and force majeure circumstances.

A joint stock company issuing shares under the IPO shall be entered in the commercial register and it becomes public. Within 7 days, it is required to submit documents to the FSC and be entered in its register. On regulated markets (stock exchange) stocks are traded only on public companies that have already been entered in the Commission's register. Registration is done on each issue, whether it was public or not. Shares of public companies are dematerialized and their statutes cannot contain provisions for their transfer or forced withdrawal.

2. Determination of stock's issue prices

One of the most complex issues relates to the determination of the issue price of the securities.

In practice, the most common offers for selling by subscription are with fixed rate (fixed price offers). It is generally believed that the securities are purchased at a nominal value, i.e. at a rate of "al vapor". Often, however, in determining the price of the offer at a fixed rate, the issuing company shall comply with the outlook for profits and dividends in the current year and the rates of securities of similar companies in the

same industry. Based on the above factors as well as supply and demand, the price of emissions is fixed at a slightly lower level than forecast calculations show. This is done for several reasons.

First, issuers want to be convinced in the sale of the securities, while trying to preserve the good image of the company. This is achieved while maintaining the famous rule that the price of the market (the official market, second market or OTC) must be higher than the quoted selling price of the emission market.

Second, the lowered data for the company's profit surely leads to the execution of the forecasts in the prospectus. The sale of shares in slightly lower emission rate makes these securities currently undervalued, and this gives a "better chance of a quick profit of speculators with new securities - the deers."

High demand for some securities issues leads to offers for selling by subscription at a fixed price higher than the nominal value, i.e. at a rate of "above money." Our legislation prohibits that the issue price is less than nominal. When the shares are sold at a rate of "above money", the amount in excess of the nominal value is paid to fund "Reserve" of the issuing company.

Upon placement of securities through public subscription for variable rate the so-called tender offers are applied. In this case, the subscription is organized in the form of an auction, as investors wishing to acquire securities of the issue, offer price of purchase. Classification is performed in descending order starting with the highest price offered.

When marketing through public subscription a major issue is not only the determination of the issue price, but also the distribution of the securities of the issue. Often the securities requested in the offers are over than the offered shares in the issue. In this case, the tender is called oversubscribed. Issuers and underwriters are the ones who decide, depending on their company policy and the amount of oversubscription, how to proceed. In some cases investors are given a certain percentage of shares in issue. In other cases, a runoff is set up as shares are distributed to those who have succeeded in the standings, and the money is returned to the rest.

The opposite is also possible - those who want to buy shares of a particular issue are not sufficient in number, i.e. the offer is undersubscribed. In this case, part of the issue that is not bought by the general public remains in the underwriter or when the issue is guaranteed - a guarantor and underguarantor. The latter attempts to sell these so called hanging market shares, but cases in which the price of such shares on the market is lower than the cost are rare.

The determination of the issue price of the shares depends on many contingencies and the method of its formation cannot be the same for:

- the start-up issue or subsequent issue of shares that the fund company or fond put into circulation;
- emissions of joint-Stock Companies in various sectors of the economy and emissions of investment companies;
- Issues which are issued by public and non-public companies;
- emissions that are traded on regulated markets and those that are not traded there;
- emissions for which trading is continuous, regular on stock exchange, and such that are traded from time to time, etc.

Naturally, supply and demand play a decisive role, but the issue price and the method by which it will be determined, depend on the listed conventions. Experience

shows that the most commonly used manner for determining the issue price of shares is a method based on the net asset value of the issuing company.

The problem of the valuation of the shares of the public company is a legal decision by adopting a special regulation. It establishes requirements for the items in the fair value of the shares of public companies as well as of non-participating in the transformation of commercial companies with at least one public company.

Variety of conventions and specific objects assessment led to the identification of three ways, assumptions or opportunities for trading of shares in different markets and hence the determination of the fair value of each of them. These three options are:

- shares of public companies that are traded internationally recognized and liquid securities markets.

FSC prepare a list of these highly regulated markets. This fair value is determined by a variety of methods, i.e. basket of methods including the fundamental evaluation method has for market price. For a market price is considered the price at the last transaction executed on a regulated market.

- shares of public companies that are traded on national and international regulated markets of securities, other than those approved in the Commission's list.

The fair value of the shares of these companies also "is based on a basket of methods. Among them is a core weight method for assessing market price on a regulated market, as for a market price is assumed the weighted average price of the transactions effected in such shares for the previous three months".

- shares of public companies that are not traded regularly and intensively regulated securities markets

This basket of valuation methods that measure the fair value excludes the evaluation method at market price. This is because the temporary interest in the shares of companies that trade infrequently regulated markets is driven by various factors. Sometimes it targets market manipulation, and this is unacceptable on the highly liquid markets.

In the Ordinance is detailed three types of valuation methods:

- a) a method of discounted net cash flows;
- b) a method of net book value of assets;
- c) a method price ratio / profit for the companies analogues.

The risk in the issuance of new shares is great for investors and for underwriters and guarantors. When selecting securities from new issues there are no agreed rules for investment. Naturally, the information contained in prospectuses should be reliable and thus help to protect investors from delusions. However, it cannot guarantee a high profit or prevent any losses. The fate of newly issued shares largely depends on proper targeting of the collected funds in the company of reliable management and the market situation.

3. Issuance of corporate bonds

Bonds are debt securities, which in the world practice are above 100 types. The issue of different bonds - state, municipal, corporate, mortgage, etc. has its specifics and legal regulation.

Corporate bonds in Bulgaria can issue stock companies under the public offering or non-public issue. The aim is to increase the company's capital and primarily finance specific investment projects. For example the collected by the issuance of corporate bonds in a company funds in "Energy" AD are directed towards the purchase of equipment for the production of a new kind of self-generated batteries. In "Prosoft"

AD the funds of the issue are used to finance sales of new computer equipment on lease.

The procedure for the issuance of corporate bonds in listed companies differs significantly from that of non-public companies.

Issuance of corporate bonds through public offering is governed by the Commercial Law and Securities Act. The legislature authorizes the placing of bonds to be carried out by Companies that have existed for at least two years of its formation, i.e. not be allowed to raise the issue of constituent capital. The size of the bond issue can be up to half of the capital contributed.

The bonds can be present and dematerialized, secured and unsecured.

Initial public offering of secured corporate bonds authorized by the FSC on the basis of a number of documents, of which the most important is the IPO Prospect. A novelty is the mandatory conclusion of a contract between the issuer and the intermediary in the form of commercial bank, named trustee of the bondholders.

The prospectus of the bond issue shall contain:

- the conditions under which the issuer is obliged to pay an early bond issue;
- certain financial ratios to the repayment of the bond issue;
- the conditions to be met by an issuer for issuance of new bonds of the same class;
- contract with the bondholders' trustee.

The trustee of the bondholders is called upon to care for the interests of the bondholders and the legislature determines to be a credit institution chosen by the issuer which is not a bank underwriter or trustee for another issue of the same issuer and bank that directly or indirectly controls or is controlled by the issuer. The trustee must observe no conflict of interest between the parties to the bond issue, and between himself and the issuer. The issuer is the one who pays his salary.

The trustee for the bondholders:

- act in the best interests of shareholders;
- convene a general meeting of shareholders;
- evaluate the performance of the issuer's ability to fulfill its obligations under the issue and provide information based on the analysis;
- ensure the availability, condition and value of collateral;
- take concrete measures against the issuer for failure to meet the terms of issue;
- notify the issuer for the circumstances under POSA prohibiting the trustee to perform further duties and repair it in time.

In turn, the issuer is obliged to cooperate and provide the client information specified by law, such as:

- quarterly reports submitted to the issue - for the trustee, the FSC and the Stock Exchange and the information under Section I, Chapter Six POSA - for the trustee;
- notify the trustee of changes for the security and for deadlines defined in the prospectus financial indicators;
- termination of the contract in case of non-compliance with non-removable law against the trustee and signing a new contract with another trustee;
- initial and annual award of valuation of collateral.

4. Issuance of municipal bonds

In nature and requisites municipal bonds do not differ from the classical form of debt securities. They have their own specificity in individual countries, which may be characterized in terms of: legal regulation, market model and the pattern of trade, the

reasons for the issue, the subjects of sale, method of disposal, secondary trading with them and others. Therefore more accurate study of a municipal securities and trade patterns with them could give if they are not considered in general and within the legal and economic situation in individual countries.

In the literature different terms are used to refer to securities linked to debt of local authorities. Often is written about "municipal", "regional", "urban" securities which for the most part are accepted as synonyms of municipal securities, especially municipal bonds. From the perspective of spatial planning, especially in Anglo-American and European-type local authorities and government could be sought a degree of variation in these terms. In Bulgaria, the municipalities are the main issuers of bonds and the term "municipal bonds" is therefore mostly used.

The need for a loan and municipal bond issues in the context of fiscal decentralization becomes more evident. The reasons or motives for this issue are:

- economic - raising additional funds for the development of the municipality, solving the problem of uneven receipt of funds in the municipal budget, financing of investment projects and those of local infrastructure, financial market development and attracting local and foreign investors and others;
- Social - financing of social programs, creating new jobs, improving people's lives in the region and others;
- Political - strengthening the autonomy of the municipality and increasing the authority of local governments.

Worldwide there are different types of municipal bonds, but two types stand out as the most widely used. These are:

1. General obligation bonds are issued to help finance programs in areas of great social importance - health, education, or to provide funds for such activities which do not bring direct revenue - the construction of parks, streets, squares and more. These kinds of bonds are guaranteed by the municipality, as the payment of income and principal of the bond issue going from the municipal budget. In a number of countries before issuing them a consultation with the residents is required.

2. The bonds backed by revenues from projects are particularly popular in recent decades and are increasingly used in many applications. They are issued to finance specific activities, such as construction or repair of roads, parking lots, bridges, sports facilities, water supply and sewerage systems, university campuses, etc. Repayment of the bonds is done with revenues from completed projects.

In addition to these two main types, in practice are also used:

- Bonds mixed coverage (hybrid bonds). These bonds are convergent type between the two main types of municipal bonds. part of the income on the bonds is paid from the municipal budget and another part comes from the realization of revenues from the project. These can be insurance bonds, bank guarantees, lease bonds and others;

- The industrial revenue bonds are similar to bonds guaranteed by the projects. They are intended for the construction of commercial and industrial property, which is available for lease or for private owners;

- Housing bonds are issued to raise funds for the construction of new homes. Especially popular in the U.S., but the mortgage crisis of 2007 reduced their volume. Are also developed in Russia, where private housing is growing significantly;

- Bonds to refinance old issues. These are emissions placed by municipalities seeking to replace existing bonds with new parameters, which are more favorable to the issuer;

- Special tax bonds are those which income is guaranteed by the fees and prices of local services. It is known that investors in municipal bonds do not pay taxes on them.

In different countries depending on the needs, the municipality is oriented towards one type or another. In Bulgaria, more municipalities issue bonds, as the goal is to put more of the second type - a guaranteed income from projects. The municipality should build its strategy for financing its activities with bonds and make program in which to analyze in detail: the type of the bonds; nominal and issue value; intermediaries who will deal with the preparation, issuance and placement of the securities; potential investors; markets on which securities will be offered, etc. The listing of the bonds on the stock exchange is an additional incentive and guarantees their liquidity.

5. Procedure of issuing municipal bonds in Bulgaria

Municipal bonds in Bulgaria have the same purpose as those in developed countries. They are part of the municipal debt. Municipalities can take long-term debt for:

- financing of investment projects benefiting the local community;
- refinance existing debt;
- prevent and mitigate the effects of the force majeure;
- provide payments required municipal guarantees.

Bond issue is predominantly realized due to the first two reasons - the financing of investment projects and refinancing of debt. It can be done in two ways - under the initial public offering and pursuant to the public offering. In the first case in the country, the provisions of POSA and the procedure for the issue resembles that of corporate bonds. In the second case, the purchaser of the issue can only be institutional investors.

The procedure for the issuance of municipal bonds includes the following major steps:

- The proposal to issue municipal bonds shall be submitted by the mayor for discussion in the municipal council;
- The idea of a bond issue may be offered to discuss in the local community and rational views to become part of the emission. The invitation shall be published in a local or regional newspaper and placed in a public space available in the city hall, the date of the discussion of the project is at least one month before the examination of the proposal by the council;
- To the proposal is attached a full description of the project - name, goals, feasibility, the expected timescales for implementation and socio-economic analysis of the expected results of its implementation;
- A detailed description of the financial parameters of the project - all sources of financing and the size of the financial resources, the maximum amount of debt, and ways to its utilization, interest rate, repayment schedule, costs of consulting and administrative management services sources of repayment of the debt, the effect of debt financing costs and debt service on the municipal budget;
- The Municipal Council, after discussion and voting, decides to issue municipal bonds as a mandatory defined: the maximum amount of debt, expressed in nominal value; currency and type of debt; way to secure; terms of repayment; maximum interest rate, fees, commissions and other;
- The preparation for the issue, and the very issuance and sale of bonds shall be assigned to an investment intermediary who is selected according to the Law on

Public Procurement. It is desirable that the firm is a bank that has an extensive branch network in order for the issue to be disposed to a wide range of investors;

- When the issue is carried out under the public offering, it shall be submitted to the FSC for approval. Then the investment intermediary distributes it, mostly through subscription;

- The Ministry of Finance has set up a central register of municipal debt. There are written records of each municipality, which in turn supports a sub issuance of municipal securities.

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