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# HISTORY DEVELOPMENT

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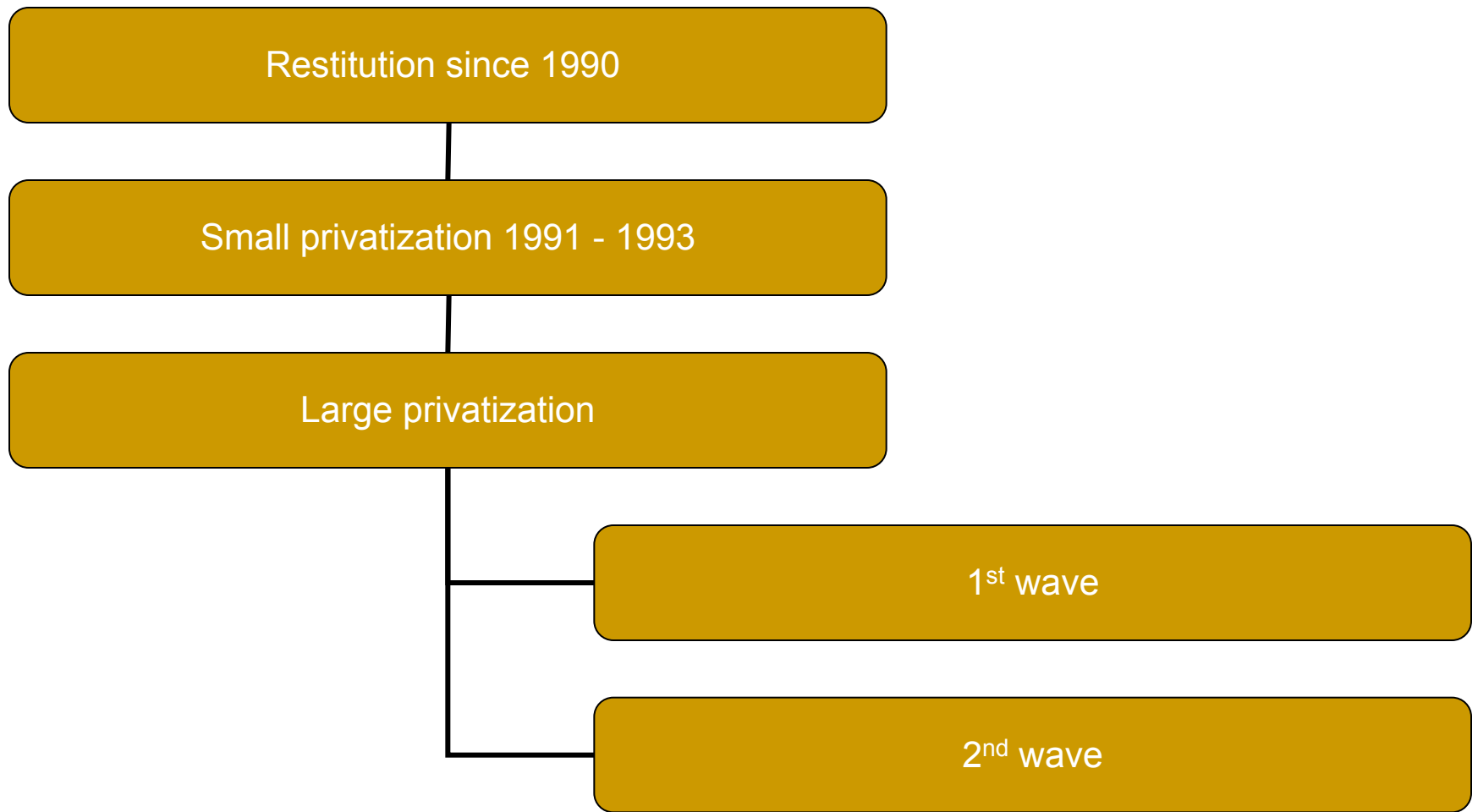
## **PRIVATIZATION PROCESS**

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# Introduction

- At the beginning of the 1990's the Czechoslovak economic structure was unitary
    - Almost all property existed in the form of state ownership
      - Suitable for central planners
      - Unsuitable for market oriented economy
    - Till the end of 1994 80 % of the state property was transferred in private ownership
  - The process of the property transformation ran in several ways
    - Re-privatization
    - Small privatization
    - Large privatization
    - Privatization after 1995
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# Structure of privatization process



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# Restitution

- It is process of confiscate property reversion to former owners.
  - In the Czechoslovakia several disputes against restitutions
    - Several strong pressure groups against restitutions
      - Advocate of former political regime
      - Managers of companies that were a subject of restitution process
      - Economists
        - Slow down and postpone of privatization process
        - Doubts about social acceptability of property reversion
    - Very strong public support of restitution process
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# Problems with restitution

- Date of setting restitution claims
  - If restitution in the forms
    - Money compensation
    - Physical compensation
  - How evaluate the property
  - Identification of former owners with claims for restitution
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# Restitutions

- In Czechoslovakia was decided that during the restitution process there
    - will be returned the property confiscated after communist coup in Feb 1948
    - Will be returned the property only of Czechoslovakia citizens (Czechoslovak citizens in 1948) and
    - In specific cases will be returned the property of the Church
    - Restitution did not concern
      - Corporations, associations, clubs and foreigners
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# Restitutions

- Whole restitution process started at the end of 1990 and continues till now
- Data about total value of restituted property are different
  - According to Official Report of the Czech government total value of restituted property was from 70 to 130 billion CZK.
  - The main source of restitutions financing was The Restitution Privatization Fund
    - Concentrated of financial resources from the privatization
  - In first phase
    - Restitution of confiscated property from 1955-1959
    - 70 000 civil buildings and office buildings
    - Later extended in farmlands, woods, etc. Returned 50 % of state ownership of farmlands and woods
- Czechoslovakia had the second largest re-privatization program of any of the former socialist European countries, with the exception of the former East Germany

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# Restitutions

- Beside the physical restitution there existed also financial compensation if the physical restitution was impossible
  - Main financial resources came from Restitution Privatization Fund
    - In this fund there was concentrated financial resources from privatization process – 3 % of company stocks designed for privatization
      - Owners of confiscated property got stocks from this fund in the case if they could not get back their property physically and besides they got 30.000 CSK in cash.
  - Restitution had the significant impact in some branches
    - Retail sale
    - About 15 % of population profited from the restitution
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# OVERVIEW OF PRIVATIZATION PROGRAMS

## SMALL PRIVATIZATION

- ❑ Small privatization process was launched in January 1991
- ❑ The background was the sale of small units in public auctions
  - ❑ There was no limit for the value of property designed in small privatization
    - ❑ The largest unit Stama Bzenec in the price 305 million CSK
- ❑ It began with an amount of 120 thousand restaurants, shops, and small business, designated for selling
- ❑ Public auctions were directed by local privatization
  - ❑ Listed privatized units at least 30 days before the auction
  - ❑ If there was no interest about privatized business was applied so called the Dutch auction
    - ❑ Decreasing in the initial price from the extreme high price to lower
      - ❑ Decreasing about 50% in 1<sup>st</sup> and about 20% in 2<sup>nd</sup> auction round
- In the first round of the small privatization was opened only for Czechoslovak citizens

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# OVERVIEW OF PRIVATIZATION PROGRAMS

## SMALL PRIVATIZATION

- Unsold firms from the first round were re-auctioned later in the second round, in which foreign participation was allowed to participate
- The first auction took place in 1991 and last in 1993
  - The most auctions took place in 1991 and 1992
- By the end of the year over 22.000 enterprises had been sold for 30 billion CSK
- The total value of call price was 21 billion CSK
- It means that total value of earnings were about 50% higher than total value of initial call price.
- Those enterprises that remained unsold had to be moved into the large privatization program
- Earnings from the auctions were deposited in the National Property Fund

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# National Property Fund (NPF)

- One of the important transformational institution
  - It was established in 1991 and its initial function was execution of privatization decision of the government.
  - All state owned companies designed in privatization were transferred under control of National Property Fund.
  - It executed privatization and got in earnings.
  - Fund did not take care of transferred property.
    - It was criticized because company in control of NPF was paralyzed and not able to decide about long-term investment or restructuralization.
    - On the other hand NPF did not hampered cost wasting of state owned company management and forbidden dividing of companies.
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# National Property Fund

- Earnings from privatization of state property did not pass in state budget but became property of NPF and was used as settlements for several actions
    - Ecological accident costs
    - Discharge from debts of privatized companies
    - Capital support of companies designed for privatization
    - Transformation and stabilization of banking sectors
    - As a resources for the support of social, health and retain insurance funds.
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# Problems of small privatization

- 75 % buildings were auctioned without property right to building it means that the subject of privatization was only occupational lease for 2 and later for 5 years
  - If the subject of privatization was some public utility business this business had to be provided for 10 years (right of user)
  - The largest problem was related with financing of small privatization
    - The most of households disposed only by limited number of savings and all privatization was financing by debts
      - The National Property Fund, banks
    - There were established roots for the future problems in banking sector.
      - In 1990 total value of property designed for privatization was 1400 billion CSK but total value of households savings and cash was only 323 billion CSK.
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# Advantages of small privatization

- Established small business sector
  - At the end of 1991 small private companies provided 41 % of all retail sales.
  - But small privatization was financed with debts and thus determined future development in companies
  - A lot of companies had problems with debt settlements
    - Were not able to get next credits and had to use supplier credit that were not able to settle.
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# Large privatization

- Form of the quick privatization
    - No will of the government to restructure companies designed for the large privatization
    - The task for new owners
  - The aim
    - Growing in the effectiveness of the Czech economy as a whole
    - Brake up monopoly structures in the market
  - Brake up monopoly structures in the market
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# Dispute about pace of privatization

- Reasons for quick privatization
    - Negative experience in Hungary – privatization of state-ownership in hands of former management
    - Afraid of “pre-privatization”
      - Company existed without management till finishing of privatization process and was getting worthless
      - tunneling of company by management
        - Cheap selling of company assets in the hands of management
    - This occurred in every transformation economies because state failed as the owner and supervisor.
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# Privatization projects

- Specific of the Czechoslovakia privatization was
    - Competition between submitter of privatization projects
    - In Czechoslovakia anybody had a right to submit privatization project for property designed for privatization programme
      - 5 projects for one company in average, some companies 20-30 competitive project, maximum Lacrum Brno – 126 projects
    - Submitter could use several privatization methods or combination of methods
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# Privatization projects

- In July 1991 was introduced the list of companies designed for the first wave of privatization
  - Management of companies submitted privatization project till Nov 1991
  - Competition projects could be submitted till February 1992
  - Management project had to introduces project for company as a whole
  - Competitive projects could introduce plans only for specific part of company
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# Privatization projects

- Then particular Ministry was decided about projects and suggested the best one
  - Final decision was done by Ministry of National Property
    - Only in specific cases by government (only 5 % of all privatization projects)
  - After approval of privatization project company property was transferred in NPF that
    - Carried out privatization
    - Control un-sold property
    - Get in earnings
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# Privatization projects

- In reality almost all projects were submitted by former company managers or its employees
  - Management applied several methods
    - To buy whole company
    - To get a company share
    - To get the most profitable parts of a company
    - To delay privatization and use an absence of the shareholder's control
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# Small Privatization-

- The privatization process reflected the government effort to privatize to Czech citizens
    - Called as the “Czech Way”
  - It reflects the moods of the Czech representatives
    - Against the sale of the „family silver“
    - Against „German colonisation“
  - Barriers over the flowing of foreign capital
    - In small privatization
      - Attendance after the lack of interest the Czech citizens
    - Privatization proposal submitted with auditor’s report
    - Asset pricing based on market value
      - Czech citizens – book value if  $BV > MV$  then MV
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# Privatization methods

- Voucher privatization
  - Public auction
    - Won the highest offer
  - Public tender
    - Multi-criterion decision
    - Not only price
  - Direct selling without public tender
    - Approved by government
    - Higher probability of corruption
  - Transformation of a company in joint-stock company and then sale of company stocks
    - In stock exchange, voucher privatization or OTC
  - Free transfer of state property in municipal units, funds of social insurance, etc.
    - Public buildings, kindergartens, etc
  - Temporary transfer in NPF
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# Privatization methods

- The most of companies transferred from state-ownership to joint stock company
  - Then was applied combination of privatization methods
    - Part of stock was sold in voucher privatization
    - Rest was sold by auctions or by other methods
      - E.g. Jitex Pisek
        - 69 % of asset – voucher privatization
        - 10 % of asset – direct sale
        - 5 % of asset - employee shares
        - The rest The Restitution Fund
  - Method of direct selling was used in the case of large state companies
    - E.g. car company - Skoda
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# Small Privatization

- In the first wave
  - 198 billion – 42 % voucher privatization
  - 10 billion – transfer to municipals
  - 40 billion – auctions, tenders and direct sale



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# Voucher Privatization

- Dominant privatization method was voucher privatization
    - About 50 % of all joint stock companies were offered for vouchers
      - Authors Dusan Triska, Tomas Jezek, Vaclav Klaus
  - The aim of voucher privatization was quick transfer of property rights into private hands
  - Other aims
    - Establishment of positive relation of Czech citizens to market economy
    - Quick transfer of property and limitation of pre-privatization tunneling
    - Equitably of private property
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# Mechanism of voucher privatization

- Voucher privatization was proceeding in several phases
  - First phase
    - Registration of Investment Privatization Funds
  - Second phase
    - Registration of privatization participants
    - Voucher privatization was open for all Czechoslovak citizens 18 years old
    - In price of 1035 CSK got voucher booklets with 1000 points that were divided in 10 lots with 100 points
  - Third phase
    - List of companies designed for voucher privatization with basic information about a company (revenues, number of employees, number of share, value of basic capital, existence of a golden share etc.)
    - Golden share – the possibility of the government intervene in company business activities although the government is not majority shareholder
  - Fourth phase
    - Zero round
      - Voucher participants could invest voucher points via Investment Privatization Fund
    - Voucher participants invested their voucher points on their own
  - Fifth phase
    - Several rounds of voucher privatization

# Mechanism of voucher privatization

- Fifth phase
  - Announcement of number of shares designed for particular voucher round sale
    - Announcement of price of this shares
      - How many cost one share, how many points
      - In first round all shares had same price 3 shares cost 100 voucher points
      - In next rounds the price determined by previous rounds
    - Voucher participants and investment privatization funds ordered shares. Investment funds could hold at most 20 % of company
    - This orders was collected and processed in The Center for Voucher Privatization
    - It could lead to several situations
      - Supply and demand were same or supply was higher then demand
        - All orders were executed
      - Demand was higher than supply but not more than about 25 %
        - Demand of privatization funds was limited to balance demand and supply
      - Demand was significantly higher than supply
        - The orders were cancelled and investors got back their voucher points
    - All companies that were not sold moved in next privatization round with new price of shares.
      - In next round price was determined by level of demand and supply in previous round
  - Next privatization round started

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# 1<sup>st</sup> wave

- Started in Nov 1991 finished in Jan 1993
  - Participate 5,95 million of Czech citizens (from 7,4 million available)
  - There were offered 1491 joint stock companies
  - 72 % voucher booklets were investment via investment funds
  - Total revenues 6 billion CSK
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## 2<sup>nd</sup> Wave

- Started in September 1993
  - Only in the Czech Republic
  - Participate 6,169 million of Czech citizens
  - 63,5 % voucher booklets were investment via investment funds
    - Bad experiences with Investment Funds from 1<sup>st</sup> wave
      - Delays of shares transfer from Investment Funds to investors
    - Total revenues 4,4 billion CSK
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# Privatization after 1995

- Privatization process was continuing after 1995
  - But the pace of privatization was decreasing because a lot of property was transferred in private sector and the public support of privatization was decreasing
  - The most usage privatization method was direct sale.
    - Government retain majority share in banks, telecommunications, gas and electricity companies
    - The role of foreign capital was increasing
  - Revival of privatization with left oriented government of Milos Zeman
    - Privatization of banks
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# Total value of property

- Book value of property designed for privatization and transferred
    - 780 billion CSK
      - Small privatization – 45 billion CSK
      - Free transfer in voucher privatization – 333 billion CSK
      - Free transfer in municipal units – 121 billion CSK
      - Restitution – 25 billion CSK
      - Privatized by standard privatization method– 121 billion CSK
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Thank you for your attention

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