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VOUCHER PRIVATISATION VERSUS EFFICIENT CORPORATE GOVERNANCE IN THE CZECH REPUBLIC¹

The main objective of this paper is to evaluate the impacts of the voucher privatisation, which was one of the fundamental methods of the privatisation process in the Czech economy, which proceeded during the 90s of the last century, on the formation of ownership structure in the Czech economy. The quality of the ownership structure determine even the efficiency of the corporate governance, which consequently influences the competitive strength of the Czech enterprises within the international competition and currently even in the single internal market of the European Union.

Keywords: Corporate governance, efficiency, voucher privatisation, management, firm, privatisation, transformation, market economy.

INTRODUCTION

The efficiency of firms in the market economies is conditioned by their efficient management, which is, in the theory and practise of market economies, called by an Anglo-Saxon term corporate governance. By the management of the firms (corporations) is usually meant an institutional and instrumental way of control of a firm by its owners. These are means by which the owners of a company realize their management and control on behalf of themselves, in other words they are executing their ownership rights.

At the beginning of the Czech economy transformation from the centrally planned system of the economic management to the market system becomes, within this context, the most important a thesis that the basic starting – point of the whole transformation process has to be a privatisation. Only under this condition the market forces would be enabled to direct the firms to efficiency² and to start the process of their restructuring.

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¹ This paper ensued with the financial support of the Czech Science Foundation within solving the GA402/06/0204 grant: "Complex analysis of the corporate governance aspects under the conditions of the Czech economy."

² Here it is necessary to mention, that the private ownership itself does not guarantee the maximal efficiency of a production. The failure can occur for two reasons. First, the loss of competition in the market of products and services can weaken stimuli and restrictions regulating the performance of the managers. Second, the ownership is often separated from the management, especially at great modern firms: the ownership is spread to a number of shareholders so the control is in hands of a small number of managers who profit from the information asymmetry and elude the control of the owner. This can escalate a conflict of interests because the profit pursuing – profit maximization of a shareholder – does not necessarily mean the utility maximization of

It was expected that by means of privatisation would be found such owners who will dispose of the acquired property responsibly and efficiently. The privatisation process became along the years 1991-1993 the most important moment in the life of all Czech firms. One of the most mass privatisation methods, which were used in this period, was the voucher privatisation what was an original method created in the Czech Republic.

What were the impacts of this method on the formation of efficient corporate governance tries to adumbrate, at least in elementary outlines, this paper. This paper ensued with the financial support of the Czech Science Foundation within solving the GA402/06/0204 grant: "Complex analysis of the corporate governance aspects under the conditions of the Czech economy." Successful fulfilling of this research project has necessarily include even the detailed view into the past on the primary formation of the corporate governance structures in the Czech Republic as a starting - point of the current situation in this field. In this context it is not possible to ignore neither mentioned impacts of the voucher privatisation on the functioning, performance and competitive advantages of the Czech firms.

1. POSITION AND IMPORTANCE OF THE VOUCHER PRIVATISATION WITHIN THE PRIVATISATION PROCESS IN THE CZECH ECONOMY

The Czech Republic belonged in the initial period of the transformation, in comparison with other transitive economies, to the very nationalized ones. In 1989 produced the public sector c. 86% of the gross domestic product, 10% of the product were produced by the co-operative sector and only 4% were produced by the private sector.

During the realisation of the privatisation itself it was appeared from and idea that the privatisation process has to be finished as soon as possible, because the period of the pre-privatisation uncertainty paralyses to a great extent the investment and enterprise activities and rational performance of the whole economic sphere. This idea was brought in the Czech Republic in its principle to an extreme position and the main objective de facto became the privatisation at any price³. On the date of 30th December 1998 were privatised assets in the accounting value of 1.4-1.5 billions CZK, whereas the yield of the state was only a seventh of this amount, about 0.2 billion CZK.

The means of production privatisation included so-called "small privatisation", which was related especially to a disestablishment of various shops and business premises, and "great privatisation" of state enterprises.

Within the "small privatisation" were privatised assets in the accounting value of 23 milliiards CZK, the income of the State Property Fund from realised sales reached 30 milliiards CZK. The embarrassment of this disestablishment method was the fact that the sales often proceeded without fixed and set rules, what in its results often led to liquidation of local services and to inception of business premises which were less sociality beneficial. This form of privatisation was officially finished in December 1993.

the managers. As it is shown in various empirical studies, managers' earnings are rather in correlation with the firm's size than with its profitability.

³ It is possible to claim, that as fast as there was, in former socialistic Czechoslovakia, achieved the highest rate of the socialistic ownership in the economy (almost 95% in 1953), was at that time achieved the privatisation objective faster than in any other transforming economy when, at least according to political declarations, the transformation, including the privatisation, was declared as finished in 1994.

Much more important, in its extent or its importance, was “great privatisation”, as the value of offered assets represented almost 1 billion CZK. The “great privatisation” law determined, among others, even the methods through which it is possible to privatise the assets. These were especially the direct sale to a predetermined applicant, public competition, public auction, property investment to a company with subsequent privatisation of their concern and voluntary conveyance to municipality (Table 1).

Table nr. 1: Volume of the privatised assets according to main forms of privatisation in 1998
(in milliards CZK)

Way of transformation	Assets volume
Resituated	70 - 130
Conveyance of assets to municipalities (disestablishment)	more than 350
Small privatisation	23
Great privatisation in total:	934
- of assets invested to joint stock companies in total:	757
from that:	
deposited into a reserve fund	42
deposited into a basic capital of all companies	715
in this:	
1. sale of the stocks in total	95
a) tender offer	24
b) direct sales	45
c) employee shares	2
d) public competitions	24
2. voluntary conveyance in total	410
a) coupons	333
b) voluntary conveyance of stocks	54
c) stocks for RIF	19
d) stocks for a deposit into joint stock companies	0
e) restitutions	2
f) NIF	2
3. not privatised to date	210
- of other assets	177
from that:	
a) tender offer	8
b) public competitions	32
c) direct sales	66
d) voluntary conveyances	66
e) restitutions	5
Transformation of co-operatives	200 – 250
Assets transformation in total	1577 - 1687

Source: Ministry of Finance of the Czech Republic, State Property Fund, Czech Statistical Office.

The most important method, from the viewpoint of privatised assets volume, is the form of the assets transformation into joint stock companies (757 milliards, i. e. 80%) with consequential privatisation of capital participations. This method occurred in several forms: direct sale of stocks, voluntary conveyance of a concern in a joint stock company

to municipality, sale through a broker in a capital market or public competition, but also in the form of so much discussed voucher privatisation.

Stocks, which were not privatised by any of above-mentioned ways, were temporarily retained in the possession of the State Property Fund or the Land Fund by the reason of possible subsequent sale especially to foreign applicants. A small amount of stocks (mostly up to 5%) was conveyed to municipalities in cases when a company polluted the environment markedly in a particular urban area or was distinctively adherent to it in some other way. There were also issued employee shares, which were to a great extent underprivileged by the sale for a nominal price.

The certain speciality of the Czechoslovakian privatisation is represented by restitutions. They were put through even despite initial resistance of some authors of the economic reform. They were at first afraid of problems resulting from the endless legal disputes, which could have in eventuality negatively influence the rate of privatisation process. These premises appeared to be wrong.

On the basis of restitution law were in the first stage returned the assets nationalized in 1955-59⁴. The second stage included the program of returning the assets nationalized in 1948-1955, which was extended for the restitution of the agricultural assets and land⁵. It is not possible to express in numbers the exact assets value, which was within restitutions returned to the original owners or to their heirs, because these assets were in the majority of cases returned by particular firms, but it is estimated to be 70-130 milliards CZK in the accounting value. Assets in the value of more than 350 milliards CZK was by law returned also to municipalities.

The last form of the state assets transformation to the private assets was the property law transformation of the co-operatives affiliated with conversion to new enterprise subjects, which took place in the period 1992-93. Each co-operative had a duty to work up its transformational project and to submit it for approval to a general meeting of those, who set up a claim to a membership share till the January 1993. By this way the assets in the value of c. 200-250 milliards CZK were transformed during the year 1992. This transformation of co-operatives influenced mostly the field of agriculture⁶. The co-operatives transformation facilitated in considerably smaller extent even the privatisation in other branches⁷.

2. IMPACTS OF THE VOUCHER PRIVATISATION ON THE FORMATTING OF CORPORATE GOVERNANCE IN THE CZECH REPUBLIC

The privatisation should, as was mentioned above, solve the problem of real owners missing. In the case of the Czech Republic were used several methods, however for then and after all even for today's economic environment were and are determining following two privatisation methods, the direct sale on credit and the voucher privatisation. Both methods were an attempt to creation of domestic owners. In fact it was only an insertion

⁴ These were more than 70.000 of tenement buildings and houses with non-residential premises, which were and are used especially for trade, services and small business purposes.

⁵ This made it possible to return other c. 30 thousand industrial and administrative objects and almost one half of state forests, state agricultural assets and agricultural land.

⁶ From 1197 farmers' co-operatives arose 1321 new private co-operatives and companies.

⁷ There were chosen approximately 500 co-operative societies, 100 consumer co-operatives and approximately 100 other co-operatives for the transformation.

of a mediator between the seller (the state) and purchaser, which is capital strong. In a case of a great enterprise it is with a high probability in most cases only a foreign strategic investor. However these were not, unlike e. g. in Hungary, brought in on the privatisation in a sufficient extent.

The interlayer of temporary owners, rather quasiowners, was and is not able to pass muster in the long term without an own capital in a highly open economy as is the Czech economy and were and are forced to sell the acquired assets soon or later as shows the present development. From a strategic viewpoint the idea of this way of privatisation would have a sense on the assumption that this subsequent sale would be carried out by the “quasiowners” very quickly and at least a part of a commission, which they obtain from the sale, would be invested back into the economy in the form of non-debt capital. However these expectations were not in the reality met in grain.

In the cases of direct sales was definitely not met the declared thesis concerning the rate of sales intermediation to a strategic investor. In the environment of a moral hazard, imperfect rules and their inconsistent enforcement had not the owners who privatised a great enterprise sufficient motivation to make a deal to a strategic investor. There were even, at first sight short-sighted, trends to set forth by an own way, i. e. to obtain another bank credits and continually enlarge the group size by purchasing of other enterprises.

The results of the voucher privatisation were and are much worse, when the small shareholders (former holders of investment coupons) expressed their preference of liquidity and subsequently sold the acquired stocks and consumed eventually lodged them into banks. The yield from the voucher privatisation for further investments was used, according to carried out surveys, by only 15% of the participants. The investment funds only regrouped their concerns and subsequently sold out the majority interests to strategic investors. Many of them than performed as money market or bond market funds. A part of privatisation funds even left the stock market, whereas the funds’ stockholders were often derogated in this process.

If we look at the structure of ownership rights set in at the late 90s of the 20th century, whose basis was the process of privatisation, we can state that the most of large and middle-sized enterprises was generally controlled by IPF. Tens of large and middle-sized enterprises were during the process of privatisation either sold to direct foreign investors or deposited into joint ventures established with foreign firms. There were also cases when some large enterprises were sold to a Czech private individual or a private firm. However the standard situation was that a typical Czech enterprise was under the control of IPF and in many enterprises privatised by a voucher method had the state henceforth an inconsiderable concern. This status persists in some cases up to these days.

The question of the ownership rights structure is in the dominant part of the Czech economy incorporated into a question, how are set the ownership rights to IPF and who are their decisive owners. If we focus only on the group of the most important privatisation funds, we will find among this group several private funds controlled by the Czech private individuals in the background with a capital of an indistinct origin, further there were several funds of foreign banks and the rest was (is) controlled by major Czech banks (Agrobanka, Česká spořitelna, ČSOB, former IPB and KB) and Česká pojišťovna. With the exception of Agrobanka the state in the form of State Property Fund has been until recently the major shareholder in all other mentioned institutions. IPF – at least much of the decisive ones – were founded by the state financial institutions and remained closely associated with them. They were not able to provide long term finances to “their”

enterprises so they were and are only another mediator between banks and enterprises who increase transaction costs in total. In this context it is not possible to miss out the fact that beside this existed and still exists in the whole Czech commercial banking system a significant cross-ownership⁸ of minority interests what further made unclear and complicated the situation in the field of ownership structures.

It is possible to say that the privatisation, whose main purpose should be solving the problem of a nebulous ownership rights settlement otherwise the missing ownership inherited from the centrally planned economy, in its principle did not bring the replacement of the one system of institutions by some completely new system of institutions but it was rather some kind of “conversion” of former institutional elements which were restructured and again consolidated into the institutional settlement which was in some features similar to the past pre-reform settlement. In our country was the role of the “recombined”, formerly state, than formally private ownership enacted by the institutional cohesion of state – privatised banks and by them founded IPF. The recombined institutional ownerships were and even today in some cases are receivers of immense assets as their portfolios include even several hundreds of enterprises, often greater than were managed by former departmental secretariats. These institutional forms were and are not very efficient. The indirect ownership of the final owners (diks) remains highly diversified and is henceforth – as an ownership right – considerably limited. The only factual right is the right of exit and even this is tied up by the limited liquidity of the stock market.

This kind of hybrid ownership structures provides a large room for moral hazard in various non-transparent activities. The recombined ownership of this, let's suppose, transitional type still falls into the category of wrong defined structures, which could be characterized by very imperfect divisibility, portability and enforcement of the ownership rights. At that it is not possible to miss out the fact that the cross-ownership structures are very arduous for direct determination of choice range and restrictions, i. e. rules for the ownership rights exercise of managers, various owners, executive boards, supervisory boards, municipalities and state in the given stage of a privatisation process.

The problem of such a settlement is given by a fact, that on the one hand are the IPFs ineffective from the viewpoint of efficient corporate governance of hundreds enterprises which they have in their portfolios and on the other hand are the individual participants ineffective from the viewpoint of their control over the funds. If there had been, for the state ownership of the past system, characteristic the certain quasi-ownership structure, during the 90s of the last century was formed the ownership, which was formally private but de facto quasi-private. The institutional interconnection and cohesion of promotion banks (originally state-owned, later privatised) and their IPF, accentuated by mutual “cross-ownership” of the banks and funds and the integral dependence of this institutional interlacement on the state results in the new type of paternalism. This settlement could be considered as a reproduction of pre-privatisation negative models of performance: the information privilege henceforth remains on the part of enterprises which provide to their governing bodies only the purposefully filtered information (the question of asymmetric information), the enterprises are henceforth controlled by managers who might at best co-opted into their coalitions the representatives of IPF. These representatives are in the

⁸ This is also often referred to as the recombined ownership.

majority of cases individuals, who should represent funds under inferior mandate or other contracts in the statutory bodies.

As a common feature of the cross-ownership development in this stage of ownership rights redistribution can be considered the strong influence of managers during the ownership rights exercise without effectual institutional control of their responsibility. The position of the management within the structure of the corporate governance in the Czech economy at the end of the last millennium seems to be thus far the surest and as compared with the period before the privatisation it even seems that the power of the management has even grown. In this context it is very often discussed as so-called "managers' capitalism". The enterprise's management as an agent who fundamentally controls the internal information about the enterprise is usually able to persuade the other members of the executive board and supervisory board of correctness of his suggestions and proceedings within the decision-making processes. The executive board as well as the supervisory board than usually do not intervene in the decision-making processes of the management very much.

According to course books the only one effectual instrument in this system, which would maintain the discipline of the managers is the threat of "hostile takeover" of the enterprises and with this related possible threat of the management exchange once this allows that the price of stocks depreciate below a certain value. The efficiency of the "hostile takeover" threat however depends to a great extent on such a course books presumptions, which condition the functioning of securities markets. On the assumption that the stock markets are characterised by a scanty liquidity, by a distortion of information concerning enterprises and investment funds, as is often the case of the Czech Republic, all the presumptions fall in and the threat of "hostile takeover" of the enterprise is minimal.

Especially in consequence of the voucher privatisation occurred the complicated and non-transparent interconnection of the enterprise sphere with banks and by them founded investment funds⁹. It is necessary to state that the investment funds these days are not engaged in exercising the of such ownership rights, which could lead to restructuring of enterprises and increasing their efficiency. Thanks to this the enterprise managers can and often surpass the control not only of small shareholders (they are in the majority of cases ignored) but even the control of significant and major shareholders who rather concentrates on operations on the stock market. It is not possible to be surprised than that there increases a number of asset stripping cases committed by the receivers of the assets or various financial groups. Instead of a concern for a due course of the management and a strategic development of the enterprise is than a major part of them obliged to face the threat of the asset stripping.

There existed and still exists a number of enterprises, which did not pay not only to their suppliers but also to revenue authorities, social and health insurance companies. If these enterprises pay back their credits it is possible only due to gaining another credits. The banks in a way adopted the redistribution policy of the state. As they were and some of them still are in the final instance covered by the government, they afford to carry out the policy of a moral hazard on which they try to make a profit through the interest policy.

It is possible to suppose that the authors of the voucher privatisation conception were aware, since the beginning of this experiment, of the fact that by the transfer of the

⁹ Within the same context is also used the term "bank socialism".

citizens' imaginary concern in the all-society ownership to a tradable form will arise the most diversified form of a private ownership that it is possible to be imagine and that this form is not able to set up efficient corporate governance. It is indisputable that this considerably diversified ownership will have to be necessarily concentrated again. There exists a correspondence among the economists at this point as well. The question is by which form and by which ways should this concentration take its course so the institutional settlement, which will be set up, would provide a chance for a successful result of the whole operation, i. e. for the forming of the corporate governance efficient structures.

As o problem appears the fact that the state did not fulfil in the sufficient extent the role of a controller over the adherence of the legal order so the economic relationships were and are significantly deformed by not-solved problems of the moral hazard. From the part of the state it is necessary, for the enhancement of the ownership rights exercising, to define formal rules of law into a managers' budget constraint, which would ensure the extinguishments of privations resulting from the information asymmetry, transaction costs and setting the ownership rights.

If we should draw a conclusion we can state that the new owners of the former state enterprises were in the late 90s of the last century in the majority of the cases IPF, thus institutional owners without appropriate managing, controlling and supervising abilities and capacities. They manage the extensive asset shares in tens of enterprises but their personal and technical prerequisites of this assets management were to a great extent limited. As was often the cases in the period of the centrally planned economy they suffer from the lack of information, when the information ascendancy, if not the monopoly, is on the part of the enterprise managements. In this situation is for the efficient functioning of these enterprises very important the interest unity of the management and IPF or the banks as owners. On the other hand, in a case of a conflict or split between managers and owners arises the problem, which is in the economics known as the relationship principal – agent. In the very specific Czech conditions of the loopholes and such phenomenon as bad payment morals and the insignificant stock market can this fact have considerably unfavourable effects. The given situation can to a certain extent remind a situation of the “pre-privatisation agony” where are the enterprises without any efficient ownership control and their managements can in principle dispose of them as they please. The proceeding privatisation results in an extensive and long-term phenomenon of “missing the real owner”.

What is more, the most of enterprises privatised with the help of the voucher method were in the situation when they had not any major owner and particular IPFs, which often control only relatively small equity securities, are not able, but often also are not willing, to look for and find mutually acceptable solution as they have different strategic interests and objectives. An example of the conflict situation within an enterprise, which is controlled by several IPFs, can be the dispute between IPF, which prefers high dividends, and IPF, which prefers the capital accumulation and the growth of the enterprise.

3. CONCLUSION

The starting – point for the formation of the current ownership rights in the Czech Republic became in the early 90s the privatisation. The privatisation in the Czech Republic was based on the institution of individualized privatisation projects for the

particular parts of assets. As a result it was a highly decentralized process whereof the government generally set up the rules according to which should the particular players, the private individuals, firms, managements and others play and to adhere and respect them. The success of the great privatisation than in an extreme extent depended on the private initiative of the above mentioned players. The most important forces in this process proved to be the enterprise managements, which often in the voucher privatised enterprises factually exercised and exercise a number of the ownership functions. The government could usually only approved or rejected what the managements proposed.

The privatisation process to a great extent predestines the future of each privatised enterprise. On the other hand it is necessary to mention that not any exploratory study on the given topic confirmed the existence of a significant relationship between the form of privatisation and the economic results (including efficiency, profitability and productivity) of the privatised enterprises. Two enterprises with similar initial conditions privatised in the same way can get onto considerably different development paths, whilst e. g. a development of two other enterprises with similar initial conditions but very differing in the way of privatisation can be very alike.

The ownership provisional arrangement, turbulences of owners' relationships or even the ownership interregnum create at most specific environment for the activities of a management. In such an environment originates an unusually wide room for the management's activities, sometimes broking out into the loss of the factual owners' control over its activities. Admittedly, in a standard economy with clearly defined owners' relationships and properly fulfilled owners' duties should not exist anything like this.

The instability of the ownership rights settlement and from them derived to a certain extent functionless structure of the enterprises management became during the last years self-evident. The promising stabilisation step were the decisions concerning the sales of the government concerns in the banks and their subsequent realisation. Positive in the same way could be the sale of these state capital participations in particular enterprises.

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PRYWATYZACJA VOUCHEROWA A EFEKTYWNE ZARZĄDZANIE PRZEDSIĘBIORSTWEM W REPUBLICE CZESKIEJ

Streszczenie

Głównym celem artykułu jest ocena wpływu prywatyzacji kuponowej, która była jedną z głównych metod procesu prywatyzacji czeskiej gospodarki w latach 90-tych ubiegłego wieku, a także kształtowała strukturę własności w czeskiej gospodarce. Jakość struktury własnościowej decyduje o wydajności nadzoru korporacyjnego, który w konsekwencji wpływa na konkurencyjność czeskich przedsiębiorstw na rynku międzynarodowym oraz na rynku Unii Europejskiej.

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