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A CRITICAL ASSESSMENT OF PRIVATIZATION IN TRANSITION ECONOMIES: QUANTITY IS NOT QUALITY

The author seeks an answer to the question what the unheeded practical and theoretical issues backing both the quantitative success and the qualititative failure story of privatisation are? Among those listed in this paper, management coalitions, the blurred dividing line between shareholders and stakeholders, the relative importance of ownership and management, financial-industrial groups, interlocking directorates, the violation of shareholders' rights and the corrupted redistribution of capital and property rights are included. From a brief examination of such issues the author would derive which are the still tricky problems that remain to be solved in the second stage of the privatization process and that are to be analyzed in the near future.[1]

Privatization has been considered as the institutional cornerstone of the economic transformation process in transition countries – TCs[2] – under the argument that the priority target of economies on the way out from the former centrally planned system must be to improve their economic efficiency. So that the success or failure of the privatization drive in TCs must be judged first as regards its impact on economic efficiency, whatever the secondary (political, fiscal, financial, industrial, ideological) objectives of privatization could have been.[3] In order to circumvent a long-lasting methodological discussion about the accurate criteria of economic efficiency, we would stick here, in the present economic context of TCs, to the significance of privatization assets for (macro)-economic growth, enterprise (micro)-economic performances and the attractiveness of TCs' privatization to foreign direct investment (FDI). Privatization appears to be a success story in TCs when assessed with such quantitative criteria. But it is not the whole story. The privatization drive has encountered various shortcomings in its achievement, depending on the historical legacy specific to each TC and on how privatization techniques[4] have been traded off in the local (economic and political) context. The outcome of privatization is also path-dependent on policy decisions made in the very early years of the post-Socialist transition,[5] and is plagued with two basic 'locks in' which are the unresolved corporate governance issue and the residual State property that are so widespread in privatized enterprises that only a fierce optimist would not assess them as signs of a qualitative failure.

Beyond quantitative and qualitative evaluation of privatization policies, no one can resart to theoretical implications of the observed results, namely to the question: was not it the whole standard privatization train of thought too much simplistic or even inaccurate in the economic conditions of the broken-up former Socialist system? In other words, what are the unheeded practical and theoretical issues backing both the quantitative success and the qualitative failure story? Among those listed in this paper, we include management coalitions, the blurred dividing line between shareholders and stakeholders, the relative importance of ownership and management, financial-industrial groups, interlocking directorates, the violation of shareholders' rights and the corrupted redistribution of capital and property rights. From a brief examination of such issues, we would derive which are the still tricky problems that remain to be solved in the second stage of the privatization process and that are to be analyzed in the near future.

Privatization and economic efficiency: a quantitative success story

Macroeconomic efficiency

First, let us assume for a while, that the biggest concern is how much extensive is the privatization process; that is the so-called quantitative dimension (Radygin 1994) of privatization which is supposed to matter. In this respect, the share of private production (sector) in GDP is a rather significant index (Table 1, page 84), although it is a rough one, but quite easier to evaluate than the precise number of privatized enterprises (Table 2, page 85), and safe from methodological tricks undermining the valuation of assets (Mihaly). For instance, this share is over 50% in eight Central Eastern European countries (CEECs) and in one of the New Independent States – Russia – by the end of 1995, and might have reached 80% in some countries like Hungary, Czech Republic and Slovakia in 1997. On the other hand, the lowest share is observed in Belarus, Tadjikistan and Turkmenistan. To put it otherwise, only four TCs (Czech Republic, Estonia, Hungary and Slovakia) got the mark 4 for both large-scale and small-scale privatization in the EBRD (1997) evaluation. Only Tadjikistan and Turkmenistan got two marks 2 and Belarus got 1 for large privatization and 2 for small privatization.[6] More details on this scattered distribution of the quantitative success of privatization among TCs are available in CEEPN (1997) and validate both ideas of a specific trajectory towards a private economy in each country – with a wide gap between some so-called 'most-advanced' CEECs and some lagging NIS –, and of an uneven efficiency between various (mixes of) methods of privatization. Note that the 'most-advanced' TCs usually are those that first moved into the privatization drive while the laggards are late comers (or still in the starting blocks like Belarus).

However, the share of private sector in GDP grows as the result of three cumulative factors: the transfer of public assets into private hands (small and large privatization), the increase in the number of private enterprises created from scratch (i.e. the number of new start-ups net of their bankruptcies[7]), and the higher growth rate of production in the private sector compared with the growth of the still existing public sector.[8] Defining privatization in this macroeconomic sense is relevant to assess whether it is likely to have raised macroeconomic efficiency in TCs over the one of former centrally planned economies. At this level of analysis, we have proceeded to a rough econometric test through a regression of the index of GDP growth (Ig) on the share of private sector (Sps), for a sample of 25 TCs with available data *(Table 1)*. Of course, there are several other variables explaining economic growth than ownership of the factors of production. But, under the assumption of privatization triggering economic efficiency, private resource ownership must facilitate or even boost economic growth. Thus, we have to expect that the regression coefficient between *Ig* and *Sps* must be positive if we want it to confirm that privatization paves the way for economic efficiency and growth, even though the observed results must be taken with a pinch of salt due to the very rough statistical estimate of Sps from World Bank's data. The limited number of observations compels us to rely more on adjusted correlation coefficients.

	1990		1995	
	Sps	Constant	Sps	Constant
Coefficient	- 23.395	97.952	30.114	86.477
t – Student	1.396	47.024	4.264	27.724

1990	1995
Number of observations = 25	n = 25
$R^2 = 0.078$	$R^2 = 0.441$
Adjusted $R^2 = 0.038$	Adjusted $R^2 = 0.417$

Results for 1990 are rather comforting the aforementioned assumption. At the starting point of the privatization drive, the coefficient of Sps is not positive and is not significant at a 5% threshold; the adjusted correlation coefficient is very low. The share of private sector, while small, does not explain GDP growth at all. In 1995, the coefficient of Sps is positive, and 41.7% of the variance of the economic growth index is explained by the linear regression, with significant coefficients (at $p < 5\%$). The hypothesis of an existing relationship between economic growth and privatization cannot be rejected, though the correlation coefficient is not very high. On the other hand, we have calculated the rank correlation between Ig and Sps and found $r_s = -0.44$ in 1990 which confirms the absence of relation between economic growth and private ownership. In 1995, the coefficient of rank correlation $r_s = 0.65$ means a significant concordance at 5% between the two variables for the whole set of 25 TCs. Thus, though we can associate the spread of private sector and the recovery of economic growth, we have to oppose CEECs to NIS on this basis. Now when we calculate the rank correlation for the only countries having a positive rate of economic growth (*Ig* > 100) in 1995, we get $r_s = 0.02$. This means that within the subset of TCs in which economic growth has yet recovered in 1995 (primarily

CEECs), the size of the private sector does not explain, as such, a high rate of economic growth.[9] In other words, for example, Czech Republic with the largest share of private sector in 1995 only reaches the sixth rank in terms of economic growth while Poland and Slovakia, where growth recovery is the strongest, are respectively ranked the fourth and the sixth as regards the size of private sector.

Progress in small-scale privatization has been both swift and comprehensive. Fourteen TCs – nine EU associated countries, Albania, Croatia, Georgia, Kyrgyzstan, Macedonia and Russia – have reached the EBRD mark 4 in this respect. In addition, small privatization primarily based on case-by-case and auction sales have met neither technical obstacles nor strong political opposition insofar as it has even been launched by the Communist power in some TCs, like Hungary since 1982. The only shadow on the picture here is the privatization of agriculture, namely in the NIS where agriculture is still largely organized around large collective farms and there are still restrictions on the tradebility of land rights.

The outcome of big privatization is less bright. The supporters of rapid mass privatization usually focus on Czech Republic where, as soon as 1995, over 80% of big and medium-sized State-owned enterprises have been transfered to economic entities which are distinct from the central State (Table 2). On the other hand, by the end of 1995, rather few big State run enterprises have been really privatized in TCs such as Armenia, Azerbaijan, Belarus, Romania, Tadjikistan, Turkmenistan, Uzbekistan and, while big privatization is more widespread in other TCs, it still does not reach 50% of all big State-owned enterprises in 1997, except in Czech Republic, Hungary, Slovakia and Estonia. From this overall picture, we have to stress that trade sales of State assets and enterprises do make only 6,204 cases, i.e. 13% of all big privatizations gathered in Table 2. The privileged method is management-employee buy-out – MEBO (43% of all cases), followed by mass privatization (23.5%) and 'other' methods (13%), basically municipalization and restitution of assets. Trade sales of assets is the primary method in Hungary, Estonia and more recently Bulgaria, while there is voucher (mass) privatization in Czech Republic, Russia, Latvia, Lithuania, Georgia, Moldova, Kazakhstan, Kyrgyzstan and Armenia, and MEBO is prevailing in Poland, Ukraine, Slovakia, Slovenia, Croatia, Macedonia, Romania, Tadjikistan and Uzbekistan. Stalling programmes of mass privatization have restarted in Bulgaria and Romania in 1997, while mass privatization plans are finally implemented in Azerbaijan and Croatia.

Microeconomic performance in a changing environment

At a microeconomic level, the first basic performance criterion to be assessed is the effect of privatization on enterprise profitability, otherwise one could not understand why privatization was so urgently needed to maintain enterprises' balance sheets in the red. Based on a large sample of 200 to more than 1,000 industrial enterprises by country, for seven CEECs,[10] a recent assessment (R. Anderson et alii 1997) shows that Czech Republic and Hungary – where privatization is the most widespread – had the highest percentage of profitable firms (74% and 70% respectively) in 1995, and Romania and Bulgaria the lowest. Even more significant, between 1992 and 1995, the profitability of firms has improved in almost all seven countries. For instance, in Poland, of a total 1,066 firms, 835 showed an improved or steady profitability while 231 showed a decline. The average annual growth in labour productivity, from 1992 to 1995, was negative only in Bulgaria and Romania and peaked up to 7% in Czech Republic and 5% in Poland and Slovakia. In the whole sample, labour productivity growth averaged 7.2% for privatized firms and -0.3% in State-owned firms. However, had the sample been extended to Russian and NIS firms, this optimistic evaluation should have been cooled down: recent data shows, for instance, that reported profits were steadily declining in nominal terms in most Russian enterprises (Gavrilenkov 1998). While 26 thousand Russian registered large and medium-sized firms had been profitable, another 39.5 thousand had been reported as loss makers.

The microeconomic performance of privatization appears even more impressive than the macroeconomic one, though the quoted results must be somewhat qualified. In 1992, the seven CEECs were still deep in the economic slump, except Poland, while in 1995, they reached the peak of their economic recovery, except Hungary. Thus we are referred back to the relationship between privatization and economic growth, from which policy recommendations should be derived for further success of the big privatization drive. Enterprise profitability must have dwindled in the CEECs with the lower rates of economic growth in 1996–1997. Another shortcoming of the above-mentioned study is that it defines as „privatized" any firm that has more than 33% of its shares transferred to private investors which is debatable on the grounds of both corporate control theory (Andreff 1996a,b) and the present economic context of share ownership in TCs.

Several privatized enterprises in the sample might well be still under State control, so that differences in performance between genuinely privatized and State-controlled firms must be partly levelled off. All the more so if we consider that some major adjustment efforts in the State sector have been achieved indeed, including lay-offs and wage control by loss-making State-run firms, under the pressure of the final cut in open-ended subsidies and the threat of a more competitive buyers' market, in spite of the absence of a private ownership structure.[11]

Privatization also might have improved economic efficiency in TCs through attracting FDI flows. The latter basically result from microeconomic decisions of foreign investors and transnational corporations, but they are also influenced by macroeconomic determinants and government policies upgrading the attractiveness of the (TC) host country, including the FDI treatment; privatization is a significant part of this treatment (M. & W. Andreff 1997, 1998). For instance, in 111 of the 200 biggest Hungarian companies a foreign owner controlled a majority share of the stock equity in December 1995; this number raised up to 134 in December 1996 (Matolcsy 1997) and 150 in 1997 (Mihaly 1997b), and Hungary is well known as the country which had attracted the biggest FDI stock among all TCs, in particular the highest FDI per capita. On the other hand, FDI is supposed to provide fresh capital, technological modernization, privatization revenue, transfer of management skills, new industrial and trade cultures, a restructured organisation of the local enterprise, and world market penetration. So that enterprises whose privatization involves FDI rapidly should be restructured and become efficient. We have calculated, from (Table 3, page 86), the coefficient of rank correlation between FDI per capita and the share of private sector in GDP, for a sample of 22 TCs; the coefficient is rather high ($R2 = 0.63$) and the relation between the two variables is significant at $p < 0.2\%$. A last quantitative success story of privatization definitely consists in its attractiveness to FDI which contributes to the recovery of economic growth. Of even greater interest is the fact (Table 4, page 86) that attraction of foreign capital into a TC privatization programme is very much linked to the methods of privatization adopted by the host country. The share of foreign capital in total transaction value of privatized assets is higher, on average, in TCs that have privileged trade sales to outsiders; this share is the weakest in TCs having primarily resorted to voucher (mass) privatization.

Privatization was expected to act as a lever in order to reduce and crunch the so-called second (informal, underground) economy that was blossoming in former centrally planned economies. Such a belief relies on the standard liberal economic thought advocating that the excess of administrative rules and regulations prevailing in the State sector and enterprises were the causes to which one has to trace back the development of illegal economic activities. Deregulation, State whithering away and dismantling the State sector through privatization were thus assumed to get rid of the informal economy and to favour its transformation into no longer forbidden private market economy. Would we like to find a sign of quantitative failure of privatization in TCs, if any, then we had to focus on the following evidence: on average, the share of informal economy has increased alongside with the progess in the privatization drive, in most TCs, and not the other way round (Table 5, page 86). Our guess must thus be that something went wrong, at least with some qualitative dimensions of privatization.

Two other indications introduce to some qualitative shortcomings of privatization, that had been forecasted as the unavoidable outcome of non-sale methods (Andreff 1992, 1993a). On hand, it is the former socialist 'hard core' of State-owned assets in heavy industries and infrastructures that has resisted longer the privatization process, even in Hungary (Mihaly 1996a), and still resists in several TCs. On the other, it is the erosion of the widespread support for privatization which was crossing the borders of many interest groups at the dawn of the privatization process. For example, in Poland, from 1990 to 1995, change in attitudes of Poles exhibited a weakening support to unrestricted privatization for all economic sectors, except municipal transport (Adamski 1997). In 1995, unrestricted privatization receives majority social support only for commercial activity and state farms. For all other sectors, respondents' preferences favoured a limited privatization while the share of supporters of no privatization in all sectors have increased since 1995. To say the least, the results of the overall privatization process have not increased satisfaction in all social groups of interest, a statement which obviously cannot refer mainly to the quantitative achievement but to the qualitative (and distributive) outcome of the process. This might well express a sort of social disappointment at the end of an initial stage of privatization which placed emphasis not only on speed (a rather satisfied preference[12]) but also on equitable distribution and the depoliticisation of property. The second stage of the privatization process started by 1995–96, was more concerned with unresolved qualitative issues such as concentrating dispersed private own-

ership, improving corporate governance, getting rid of residual State property and investing in strategic economic restructuring rather than divesting capital or stripping assets in a survival adjustment behaviour.

Corporate governance and residual State property: qualitative limitations

„Various empirical studies – large surveys, case studies, some quantitative evidence, press reports – produce a very contradictory picture and it is extremely difficult to evaluate the degree of actual adjustment of firms" in TCs (Grosfeld, Roland 1995). Since 1995, it is all the more so with the multiplication of studies with non-converging results, despite an attempt at a more systematic, though not comprehensive, inter-country comparison (R. Anderson et alii 1997). What we would present here is a sort of „average" impression derived from our non-exhaustive reading of the increasingly pervasive literature, the great bulk of which leans on the theory of property rights and focuses on the corporate governance structure resulting from privatization. According to this literature's mainstream, expanding the control of shareholders is thought to obviously follow from the view that shareholders are the 'genuine' owners of corporations within which votes could be held, on legal principles, by shareholders, bond holders, managers or other employees in any combination. The mainstream assumption is that, as the residual claimants of the firm's net income (profit and dividends), shareholders stand last in line for the distribution of gains or losses derived from the firm's performance and, thus, have the appropriate incentives to make accurate discretionary strategic decisions (Easterbrook, Fischel 1991). In particular, the ability to monitor managers (and through them other employees) is crucial for shareholders, and it is effective if their property rights are not to be alleviated by managerial behaviour of rent-seeking (larger offices, a host of handsome secretaries, retraining sessions on Caribbean sea shores, etc.) and of maximizing take home gains (higher wages, bonuses, personal cars, etc.). When shareowners are capable to monitor and discipline managers, then the profit is higher than otherwise; such a statement underlies the numerous assessments of the quality of corporate governance on the basis of firms' profitability.

Before raising some doubts against this too simplistic view, reducing the issue of corporate governance to the monitoring relationship between owners and managers, more generally between outsiders and insiders, we will admit it for a first overview of qualitative limitations of privatization in TCs. Under such an assumption, of course, the more scattered the distribution of corporate capital, the higher the shareholder's information cost for monitoring managers. Efficient management and enterprise restructuring thus require appropriate managerial incentives (Aghion, Blanchard, Burgess 1993) that are less likely the less corporate capital is concentrated. Such a situation is well known as a principal-agent problem in which the principal is in possession of less information than the agent (moral hazard) and must design a suitable procedure for inciting managers (agents) to act according to the principal's interest (maximizing profit and asset value). Quite logically, in their survey of the literature on corporate governance, Shleifer and Vishny (1997) argue for the establishment of block shareholdings, whoever are the blockholders, including financial institutions. It is a great pity that post-communist reformers in TCs, obsessed by the speed of privatization, had precisely supported, selected and implemented those (non trade) methods of privatization which do not guarantee the emergence of hard core shareholders, despite the unheard warnings of the fans (see footnote 12 above) of long way privatization for short-listed profitable enterprises. The objection against these warnings, that the privatization process would have taken decades (Schaffer et alii 1998), does not really hold if we are now to spend decades on transforming ineffective corporate governance structures into effective ones.

Privatization by means of asset trade and (often) effective corporate governance

In the framework of the aforementioned theoretical hypotheses, we can range all corporate governance structures along a scale at the extreme (worst) end of which we find State-owned enterprises (SOEs); then come privatized firms with insider control (by managers or workers or both) and finally private and privatized enterprises with the varieties of outsider control by banks, institutional investors (investment funds, insurance companies, pension funds, etc.), domestic private shareholders, foreign investors, and individuals. The latter's control usually emerges in newly created enterprises (start ups) and from small privatization. There is no corporate governance concern in it, insofar as in a small firm a single owner is the „boss" (or a few owners are the bosses) who can discipline at a low cost a handful of managers, if any, and even supervise all the labour force. Of course, we

witness here the common result of privatization through asset trade that had been predominant in small privatization and in asset auctions after SOEs' liquidations. For large firms, asset trade privatization is supposed to provide a strong corporate governance with either a single majority owner or a ,hard core' of monitoring shareholders; they could have only a minority share, but this one must be higher than the share of any other coordinated group of shareowners, in the company stock equity. Such effective owners should restructure the newly privatized firm and adjust it to new market conditions. Nevertheless, a qualification of what restructuring means is now needed.

Grosfeld and Roland (1995) have introduced a distinction between defensive and strategic restructuring. Defensive restructuring means taking measures that seek to reduce costs and scale down enterprise activity: cutting obsolete production lines, shedding labour, getting rid of non productive assets. These measures may be a component of both deep restructuring and survival-oriented behaviour of managers and workers in privatized firms (Andreff 1996b, Ickes, Ryterman 1994). Strategic restructuring is based on a thoughtful business strategy developed in response to a need for profound redeployment of assets and implies the introduction of new products, new processes, new technologies and thus new investment projects. Strategic restructuring requires effective corporate governance by residual claimants. Therefore, profitability and productivity are supposed to reflect, through the scope and depth of restructuring, the quality of corporate governance. It follows that an hypothesis often tested on various enterprise samples is whether privatized firms perform better than SOEs, and outsider-controlled outperform insider-controlled firms, in terms of profitability, productivity, export and some other performance variables connected with a supposed enterprise restructuring. As expected by the theory, various studies[13] have shown that privatized firms outperform SOEs or improve their performance after privatization. Nevertheless, in many studies, the result is subject to a selection bias: was it privatization which has fostered better enterprise performance or was it better performance that has led the enterprise to be selected for privatization? This causality problem remains unsolved in most studies. However, the choice of an asset trade method of privatization often reflects the fact that the firm is viable and potentially or really profitable under market conditions. Thus, finding effective owners – either domestic or foreign – for good enterprises should promote strategic restructuring.

Estonia and Hungary having opted from the very beginning for direct sales to strategic investors, it is quite logic that they have experienced less corporate governance problems, namely in FDI-acquired enterprises and in privatized firms with a domestic majority shareowner or with a group of core shareholders capable of monitoring managers. However, at least two problems have remained unsolved in some of these firms privatized by means of asset sales. In privatized firms where majority Hungarian ownership was intended to be maintained for several years, sometimes after a year or two, the foreign strategic investor was able to accumulate enough shares to dominate the annual shareholders' meeting and appoint its own representatives to the boards (Mihaly 1997b). This is not properly speaking a problem of weak corporate governance structure; quite the contrary, too strong (and too much foreign to the Hungarian taste). The second problem is one of management and corporate governance in the presence of residual State ownership in partly privatized enterprises that is dealt with below.

Weak corporate governance after non-standard methods of privatization

In a large number of TCs (NIS, the countries of former Yugoslavia, Poland, Slovakia), the privatization process has primarily created insider-controlled enterprises and, according to the aforementioned theory, has generated a problem of weak or ineffective corporate governance structure. The latter basically comes out from the use of non trade, often called non standard, methods of privatization. Three of them have been widely used in TCs: restitution, management and employee buyouts (MEBOs) and mass privatization (Bornstein 1997). The major concern with non standard methods of privatization is the resulting large-scale ownership by insiders. Indeed, non trade privatization has benefited insiders either through voucher distribution with significant concession to insiders or through MEBOs. According to the principal-agent model, insiders would prove ineffective owners, lacking the incentives to undertake strategic restructuring measures in privatized enterprises, in particular in enterprises controlled by workers. Empirical studies should confirm it in exhibiting lower performances in insider-controlled firms compared with other private enterprises, and here is a tricky issue.

We would not comment on restitution insofar as it was a significant element in small privatization and the problem it has triggered is not one of corporate governance, but one of delayed privatization by a lengthy

claims process. MEBOs, because they require a large initial borrowing by managers and employees, hinder the firms to get enough additional credit to restructure inputs and output. Hence the firms do not earn enough profit to repay the principal within the deadline. So that many MEBOs have difficulty to get bank credit and they carry out little capital investment. Even though these are not the obvious consequences of an ineffective corporate governance, the latter has steadily been assumed to be the cause of low profitability by the principal-agent model. Mass privatization took different forms: voucher coupons to bid in auctions of company shares (the Czech „model", Mertlik 1996, Sereghyova 1996), interest-free loans offered to citizens to buy shares in designated enterprises (the Hungarian scheme), and giving people free shares in investment funds that control operating firms (Poland). The outcomes of large-scale privatization include the extent of residual State shareholding, the concentration or dispersion of ownership in newly privatized firms, the distribution of shares between insiders and outsiders, and the emergence of specific institutional investors.

As to the Czech mass privatization method, it was assumed to trigger enterprise restructuring by new private owners after privatization, to be more transparent and fairer than asset trade, and to gain popular support for privatization and for the government in next elections. In 1998, the Klaus government is over, financial non transparence and embezzlements linked to privatization are among the determinants of its fall, and economic restructuring does not seem to have been much more boosted in the Czech Republic than in other TCs. On the other hand, some expected shortcomings of the Czech method had not actually occurred: even though voucher auctions had been a rather daunting administrative or even 'central planning' (Andreff 1994c) task, due to the allowed emergence of investment funds, a wide dispersion of ownership and a weak corporate governance structure had not been revealed. Studies of samples of Czech enterprises[14] show that, in many firms, one investment fund holds 20% of the shares, and in other privatized firms two to four investment funds together hold a controlling minority, sometimes a majority of shares. It is often argued that some concentration of ownership helps corporate governance while scattered distribution of shares among many small shareholders is ineffective. On these grounds, the Czech funds probably concentrate a sufficient share in many privatized firms to control their management and strategy and handle an effective corporate governance. The problem is rather to know who controls the controllers. In particular, the system of cross-ownership among State-owned banks and investment funds (Mertlik 1996) that has emerged leaves management of these institutions insulated from external control, i.e. supposedly ‚outsiders' might well behave as insiders and this can explain why restructuring is often presented as luggish in Czech Republic. Later on, some investment funds have been converted into holding companies (also in Lithuania and Slovakia). The problem remains to know who controls the holding while this latter might well hinder competition and become a means of attracting State subsidies.

In the case of Russia and most NIS, mass privatization has turned into mass asset sale to insiders, both incumbent managers and employees, while investment funds have only played a minor role in corporate governance (initial regulations limited the share of any one fund to 10% of any enterprise, but the threshold has been raised to 25% in 1994). The resulting allocation of managers to privatized firms preserved the management status quo and limited the scope for selection of new managers, even though some managerial turnover had been observed (Fortesue 1997). The entrenchment of incumbent managers, survival strategies and defensive restructuring have characterized the first stage of mass (non monetary or free) privatization. Where the managers were either competent or in position to bargain on their own terms, the evolution of ownership from insiders to outsiders had occurred. For instance, the overall share of insiders in the structure of share ownership of Russian privatized enterprises had fallen from 62% in April 1994 to 56% in June 1996, while the share of outsiders – excluding the State – had raised from 21% to 34% (Andreff, Radygin, Malginov 1996). Viewed from the theory of principal-agent, this partial switch from insider to outsider ownership should improve corporate governance. But two problems are the emergence of coalitions gathering managers and outside owners and the illegal, when not corrupted or criminal, means of transferring shares to shameless outsiders. In Russia, we have noticed no less than sixteen typical violations of (small) shareholders rights during the second stage of privatization based on monetary transfer (sale) of shares. Among the most typical are: minimal block of shares to participate at the election of the board, various charges and extra-payments on transactions and on participation of stockholders at general meetings, deliberate delays in convening these meetings, vote by show of hands, secret issues of special shares, misreporting on the shareholders' register and so on (see also Blasi, Shleifer 1996).

Financial industrial groups (FIGs) are another outcome of the second stage of privatization in Russia (Freinkman 1995), Ukraine and other NIS. Generally built up by new private banks which have bought shares into industrial enterprises, FIGs do open in these TCs the well known story of finance capital which had initiated an earlier stage of development in market economies (Hilferding 1910) in which ownership control was the key issue instead of corporate governance. Some FIGs result from the transformation of former ministerial branches or associations into joint stock companies which diversified in finance and trade. All FIGs are now challenging the insider ownership in NIS industry. A 1995 law passed in Russia attempted both to regulate the FIGs' activity and offered them tax concessions, special treatment and privileges. Even though they solve, in some way, the corporate governance issue, FIGs re-concentrate monopoly powers and industrial structures that prevailed under central planning. Their present lack of financial transparency is of concern as well as it is a springboard for the sort of studies suggested in the third part of this paper.

National Investment Funds (NIFs) are specific to the Polish method of mass privatization. Each NIF must control a set of operating firms and eventually sell some of their shares, probably after some restructuring. It is thus admitted that large SOEs were needing restructuring before privatization. Each NIF is run by a private management firm owned by a consortium of several Polish and foreign management and banking companies. Such a scheme should avoid the Czech problem of controlling the controllers, insofar as these consortia are profit-oriented, managed with Western techniques, and the banks involved in are affected by a more rapid privatization in Poland than in the Czech Republic. Insofar as no share in the operating firms is distributed to the population which can only acquire shares in the NIFs, the stock value of each NIF is of concern to the management consortium. The latter's trade-off should be to restructure or disinvest from less profitable operating firms in order to invest in more profitable ones. Thus NIF's managers should put a strong pressure on managers of the operating firms in which the NIF holds a controlling block of shares, assigning them such objectives as restructuring and seeking profitability; this is obviously a rather effective corporate governance structure. In Poland, concentrated outside ownership of enterprises has been created from the very beginning of mass privatization (delayed up to 1995 anyway) with the target of avoiding non desirable consequences in terms of corporate governance instead of speeding up the process.

The initial patterns of corporate governance established in the first stage of transition will not necessarily remain stable over time. We have already mentioned some significant evolution. In Russia, large banks and FIGs have become the major participants in the cash sales of State shares in large enterprises and in the secondary market for equity stakes. This has led to weaken the initial control of insiders. In the Czech Republic, the conversion of investment privatization funds into holding companies may have a substantial impact on the initial structure of corporate governance depending on who will control the banks which hold major stakes in these holding companies.

Testing corporate governance and restructuring

Widespread strategic restructuring has been observed in no TC up to 1996 (Carlin, Aghion 1996). Surveying empirical studies[15] to date leaves us with some robust findings. Foreign owners of former SOEs engage in strategic restructuring by bringing in expertise and capital. On average, private firms are more profitable than SOEs and, in line with the discussed theory, this difference reflects more defensive restructuring in SOEs. For privatized firms, the picture is rather blurred, but more studies exhibit insider-controlled firms engaged in survival-oriented adjustment than the other way round. Fairly representative of this mainstream results is the recent study by Frydman et alii (1997). While claiming to avoid a selection bias, this study explicitly leaves out the industrial 'dinosaurs' of the communist era (sic!). It finds that, in terms of revenue growth and employment reduction, firms owned by outsiders enjoy an advantage over SOEs, firms in which investment funds are the largest owners perform rather well, firms owned by domestic non-financial companies exhibit a weaker performance,[16] while insider-owned firms shed labour at significantly lower rates than either SOEs[17] or private companies and do even worse on costs and revenues. Employee-owned firms not only behave like SOEs in terms of their revenue performance, but also underperform SOEs in terms of labour shedding. A quite orthodox conclusion derived by the authors is a strong case against the effectiveness of privatization programmes that put employees in control. The most annoying problem – except the mentioned selection bias – is the increasing number of conflicting observations that accompanies the growth of case and

sample studies. So many different results finally may have the meaning that the studies did not control enough for country, sector and sample specificities or, more deeply, that something went wrong with the theoretical background of empirical studies, i.e. the approach to corporate governance in the principal-agent analysis.

Among the most striking results that confront the mainstream hypotheses, let us recall the following. Some have found that strategic restructuring has taken place in all ownership types, including SOEs and insider-controlled firms. Managers, under the pressure of new market conditions, unexpectedly initiated restructuring, at least defensive restructuring, even in not yet privatized SOEs for which Pinto and van Wijbergen (1995) concluded that a „behaviour remarkably in line with what one would expect from profit oriented forward looking entrepreneurs". For the Czech Republic, Capek and Mertlik (1996) have not found significant restructuring in outside-owned firms, except in foreign-owned. Coffee (1996) has identified three problems in the Czech corporate structure: the securities market is neither transparent nor liquid, cross ownership between banks makes obscure the governance structure of related investment funds, and the State still holds significant block of shares in the-largest enterprises and banks. Another study (Lizal et alii 1997) has established that, contrary to the most common picture of the Czech method (privatization first, restructuring thereafter), enterprise performances had been favoured by pre-privatization break-ups of SOEs that took place in 1990 in Czechoslovakia. Thereafter, it was easier to include more performant and smaller units into privatization programmes. On the other hand, many of the large (privatized) firms continued receiving credit for non-performing projects, and State-owned limited liability companies dominated all domestic private firms in terms of the investment-production ratio (Lizal, Svejnar 1998), so that the authors conclude that the widely accepted notion that during the transition investment is high in the new private firms and low in the SOEs is not supported by the larger Czech data set. Some empirical investigations, in particular a survey of 200 Polish manufacturing enterprises, have found that those firms privatized to workers were relatively well performing and capable to adjust more flexibly because worker ownership might reduce worker-manager conflicts (Earle, Estrin 1996); Nivet (1997) finds that Polish employee-owned firms are among the best performers for the ratio of costs to revenues and profitability. However, this result is arguable not because workers are better or worse owners but because workers are more likely to have bought profitable enterprises (the selection bias again!). A recent study, controlling for the selection bias (Earle, Estrin 1997) shows that Russian firms that have been privatized to managers have restructured more and performed better compared not only to SOEs, but also to firms that have been privatized with dominant worker ownership.

We would not discuss the very numerous possible intepretations of all these conflicting results any longer. To say the least, the qualitative picture of corporate governance is less bright than the quantitative evaluation of privatization. On the other hand, the theoretical relationship postulated by the principal-agent model between corporate governance and restructuring (profitability, productivity) is probably too much restrictive and, in the real world of current business, this relationship is affected by macroeconomic evolution, moreover it is not stable due to frequent changes in the share ownership of each single corporation (sales of shares, takeovers, acquisitions, etc.), and finally the same agent may unpredictibly[18] modify his/her economic behaviour depending on macro and micro circumstances including the threat of a takeover, the re-distribution of share ownership whatever it is, the election of new members on the enterprise boards, the result of a proxy fight, the emergence of a FIG, the loopholes in the corporation law, the opportunity of corruption, and the claims of non residual claimants (a non exhaustive list of unheeded factors in the model). More or less regular bonuses, premiums, perks and bribes can link insiders to outsiders, in not yet fully-fledged institutions of a market economy, in a way unpredictible by the theoretical model, so that profitability for example remains a meaningless variable, not to speak of profit distortions in a still imperfect competition. A lower profit may reflect the existence of a coalition, though efficient, between outsiders and insiders, which is a fairly frequent case in the West, not to speak of hiding profit strategies that are by far more widespread in TCs for tax evasion purposes. Before introducing some of these unheeded factors into the discussion, let us examine a last qualitative limitation of privatization in TCs: the residual State property.

Corporate governance and residual State property

„The success of partially privatized firms in which the State remains the largest owner offers perhaps the biggest surprise of all" (Frydman et alii 1997). Not so surprising, if we compare the overall stock of assets to be privatized

to the sum of existing domestic savings and international aid! Even less surprising with the use of non standard methods of privatization than with asset sales. Those TCs that have finished their first wave of large-scale privatization now turn to the privatization of remaining State ownership in the economy (i.e. still State-owned firms) and of partially privatized enterprises.[19] There is no other way-out than direct sales, auctions and tenders on a case-by-case approach, insofar as in the now starting second stage of transition, privatization is more concerned with attracting long-term investment into key enterprises and with improving corporate governance structures, than with the speed emphasized in the first stage. Asset trade should probably supplant non standard methods of privatization. So that a long and lengthy process will be needed to remove residual property from the State's hands in some TCs.

The residual State property resulting from a privatization process is more or less extensive. The least extensive one is due to the State keeping a golden share in the stockholding of a privatized enterprise. The most extensive appears with public enterprises that the State is not capable to sell or give away for free at the moment, so that these enterprises remain in full (or majority) State ownership. More frequently we observe a mid-way situation in TCs: the State is willing to either withdraw from the shareholding of the privatized enterprise but finally it is stuck with a minority share in total capital,[20] or keep a blocking stake in order to discourage an unwanted foreign takeover. The second case often corresponds to a postponed privatization basically due to the current state of capital market or to political (governmental) change. For instance, in Hungary where asset trade was privileged, between 1990 and 1996, the volume of divested assets amounts to 55% of the initial stock (Mihaly 1997a). The task that TCs are facing now is thus the privatization of 'core assets' of the former centrally planned economy, insofar as the first years of the privatization process affected chiefly the non-essential parts of the economy and carefully avoided privatizing („non-privatizable") Soviet-type heavy industries. State assets still consist of long-term ownership and left over shares, and their full privatization is unlikely to be achieved in the foreseeable future.

Residual State shareholdings may become an obstacle to effective corporate governance due to a State passive („hands off") management of non strategic enterprises together with private owners who do not commit themselves into governance (the more scattered shareholding, the more so) because they wait for full State divestiture. When the State remains the wholly or majority-owner in strategic enterprises, the situation is even worse and leaves room for incumbent managers to behave as stakeholders. The problem usually emerges in the behaviour of the State representatives on the board of directors or the supervisory board of (partly) privatized enterprises (Schwartz 1996). They are not often committed or even encouraged by the State (or some State body) to take an active role in enterprise management, and when they are, it could even be to vote against the decision envisaged by the representatives of private owners (investment instead of dividend payouts, against increase of foreign capital in total shareholding, etc.). In addition, the State representatives on the corporation boards often are civil servants, academics, teachers, etc., i.e. are not professional experts in management, accounting, finance, marketing, business law, etc., all skills rather rare in the TCs. They even may turn into a new category of stakeholders for their own sake, after seating some time on the corporation board, and then start lobbying from one board (corporation) to the other[21] – as in the well-known interlocking directorates in the West (Bunting, Barbour 1971, Dooley 1969). One basic purpose of this lobbying is to maintain the status quo (profitable to them[22]) to the detriment of further privatization of residual State ownership. Moreover, we see the very same names as owners, managers, board members, ministry officials and trade unionists in many privatized enterprises in the TCs and this should deserve some new inquiries and investigations.

On the other hand, when the State keeps a share in the stockholding of strategic enterprises, a big issue appears to be the possible constraints imposed by line (or other) ministries or other administrative tutelage bodies on to the enterprise management. These constraints are used to be more derived from macro-economic and social policies (sustaining economic growth, cutting prices, hiring or not firing excess manpower, etc.) than from micro-economic criteria of efficient management, adjustment and restructuring. The risk here is one of inertia in corporate governance and management of partially privatized enterprises, favouring the „survival" behaviour of insiders, their pressures for getting State subsidies and bail-outs, and the still possible politicization of residual State ownership and State share management. Such a risk may delay further privatization. Yet some bureaucratic methods and political influences have apparently survived in the new control system at public and partially-privatized enterprises in the TCs.

In some countries, like in the Polish „capital privatization", the State had to put on a reserve percentage (20%) of company shares and make them available to the employees of the company on preferential terms. In many cases, the employees had not exercised their rights, and the unclaimed employee shares became the property of the State. A smaller percentage (5%) of shares were reserved as an endowment for national restitution funds to be created in the future. Hence, any strategic investor was not able to buy over three-quarters of a company's shares. In other countries, like Hungary, joint ventures (JV) with foreign partners have been privileged. Nevertheless, a joint venture is a way to create residual State assets corresponding to the percentage of total equity provided by the State to the JV, often 50% or more (Mihaly 1996b). This method of privatization obviously leads to mixed ownership. Then the motivation and expertise of the foreign strategic partner determine the real division of power and authority and, therefore, the corporate governance of the JV. In the majority of Hungarian JVs, the State privatization entity (APV Rt.) had three to five seats on the board of directors. More important decisions are to be approved at the annual shareholders' meetings, but often a single representative of the APV Rt. vote with all the shares the State happens to own. He/she usually did not behave exactly as a shareowner, being a civil servant. Therefore, there is again a principal-agent problem: who is vested with the power to give guidelines to board members appointed by the State? The question arises all the more that the board members are responsible for their actions (and can even be sued in a court).

Finally, the TCs might well be stuck with residual State ownership for a while. What is to be done? To some extent, the main difference between private and public is not ownership (Böss 1986). The main difference is management and the multitude of political and economic determinants of public enterprises' activities as compared to the mainly commercial determinants of private enterprises. The French story exhibits anyway that a privatization of management (with the government imposing a profit-seeking and market-oriented behaviour upon managers) is the best springboard for a further transfer of the (then profitable) State assets to private owners (Andreff 1987, 1992). For partially-privatized enterprises and still State-owned enterprises in the TCs, such an experience of privatization of management that warranted furter privatization of assets in French public enterprises should be of interest.

For instance in Hungary, the State agencies have made some attempts to manage State assets by indirect business-like methods; their basic idea was formulated as „private management of State assets" subcontracted for predetermined terms and fees (Csillag et alii 1996). What we have in mind under the wording „privatization of management" is quite different and unrelated to subcontracting State assets, but relates to the management criteria implemented in the public and partially-privatized enterprises, to manager incentives and behaviour in the daily management and on corporation boards, and to the strategy of the State and its representatives on these boards, in particular how did (and do) they vote. It is not enough to distinguish passive, selective and active management of residual State shares, as in the Czech Republic (Brom 1996), without elaborating on the criteria and targets provided in these three approaches to management and on the impact of management on the future value (and thus on profitability) of State shares which remain to be sold. That is the reason why the creation of holding companies is never a solution unless these holdings do behave as private investors, maximizing profit and the value of their assets (and thus 'inciting' the managers of operating enterprises to downsizing, lay-offs, asset reallocation, financial and physical restructuring, etc.), i.e. unless they are private and not State-run holdings.[23] In Poland, there is some evidence that – if taken as one management criterion of public enterprises, like in France – the decrease of employment has been sharp in the State sector (Mickiewicz 1996) reinforcing the argument that „the key issue is not to privatise a firm but to improve its governance structure" and, we would add, its management criteria. Some hindrances[24] to the privatization of management may appear where (Hungary, the Czech Republic) a so-called ‚recombinant property' (Stark 1996) has created networks of assets and managers, connected with chains of debt, which are likely to trigger lock-in effects (Pistor, Turkewitz 1996).

Thus, we can only agree with the ‚soft landing' attitude, compared to speeding privatization at any cost, adopted in a World Bank technical paper (Pannier 1996) stating that „the reform of the public enterprise sector is at the heart of structural transformation in TCs" and considering that „a number of enterprises are likely to remain in the public sector for an indefinite period awaiting privatization". The same study covers various useful suggestions (recipes?) for selecting agents to represent the State on corporate boards, for improving the management of SOEs (public enterprises), for selecting managers,

evaluating their performance and providing them with accurate incentives (including management contracts between the government and private managers) and, even more basic, for running properly the board of directors in a public enterprise. The last point opens a research area which goes far beyond corporate governance and the principal-agent model.

Corporate governance and beyond: a new research focus on the tracks?

„When ‚privatization' became the word of the day in Eastern Europe, most policy makers and external observers made a number of rather simplistic assumptions which have since become increasingly hard to maintain", and „assumptions underlying the initial approach became increasingly inadequate" (Frydman, Rapaczynski 1994, p. 168-169). No doubt, this statement applies to the assumptions derived from the principal-agent model. Now, let us abandon this mainstream approach to corporate governance that had mushroomed in the first stage of privatization following up the influential articles by Jensen, Meckling (1976) and Fama, Jensen (1983) on principal-agent problems. We are not left without alternative or, better, complementary theoretical explanations of who makes decision in emerging corporations in TCs. First there is a theory of corporate control, that had prevailed since the work by Berle, Means (1932) in a less-developed stage of market capitalism in the West and before the emergence of the agency costs analysis. Second, we can also dwell upon the more recent literature on coalitions within economic organizations.

Now the TCs are entering a second stage of the privatization process, giving up the focus on speed and quantity, and switching the emphasis on to the quality of corporate governance, the structure of corporate control and the legality, confidence, reputation and trust normally associated with private ownership in market economies. Such qualitative problems had been solved several decades ago in Western capitalism. The theory of corporate control and the first analyses of economic organizations are contemporary to the solutions brought to these qualitative problems a few decades ago. The corresponding literature should recover some interest for TCs – it is at least our assumption – insofar as they had not yet achieved a fully-fledged capitalist corporate control and structure; thus, they are more facing the same corporate control shortcomings of an earlier stage of capitalist development than the characteristics of financial market discipline imposed in last resort on corporate governance nowadays by the financial globalization in the West.

In some way, an attempt to initiate a new approach is present in the recent work by Earle and Estrin (1997). They argue that the peculiarities of ownership structures in Russia require a „reconsideration of conceptual approaches to the analysis of corporate ownership, control and behaviour". Ownership structures are quite peculiar in all other TCs, at least when compared to today's Western market economies. Maybe less peculiar if compared to ownership structures of an earlier stage of capitalist development that prevailed some decades ago in the West. As it is emphasized in the Earle-Estrin research, what matters is not only the concentration of ownership, but also the idendity of owners. I fully agree. Let me go further and cross the Rubicon: who personally are the new owners and what are their number on seats on different corporate boards, their behaviour of shameless tycoons, the shares they personally own, their alliances (or interest groups), their wealth, their legal or illegal manoeuvers, etc.? These also do matter. Part of such information can be submitted to a scientific treatment with economic analytical tools which were up to date in the West a few decades ago, in an earlier stage of development. We only draw some guidelines of what could be done in coming researches.

Who owns whom? The realm of core shareholders, mergers and takeover bids

The theory of corporate control originated by Berle and Means has developed either as a reaction against the idea of managerial enterprise (Marris 1964, Galbraith 1967) or as a consequence of empirical studies of corporate control (Burch 1972, Kotz 1978, Larner 1966, Morin 1974, Pastrò 1979). According to this literature, governance had not become utterly independent from ownership in corporations operating in Western market economies, a fact that was exemplified by existing ‚hard cores' of monitoring shareholders, cross shareholding among several corporations and ‚locked up' companies; the latter are meant to be corporations whose capital is owned by their own affiliates in a significant (majority) proportion and which cannot consequently be taken over by raiders. Even before the theory of property rights and corporate governance, this literature distinguished insider (usually managerial) control and outsider control by a hard core of strategic shareholders, family members of a former tycoon, banks, and institutional investors. The whole

issue was not only depending on the concentration or dispersion of shareholding, but also based on distinguishing majority and minority control of shares (and the blocking percentage of shares). The basic hypothesis was that corporate control structures are not static or fixed for ever, and that they are moving due to mergers, acquisitions, takeover bids (tenders) and, in the most sophisticated versions, to proxy fights for electing the firm's boards (for some more details, Andreff 1996b). Though moving, the financial capital structure is interlocking a number of industrial firms and banks, through cross shareholdings, into so-called financial industrial groups (FIGs) with a 'parent company' (a bank or non financial firm) at its core. This is precisely a valuable analysis for TCs today.

After mass privatization, in Russian enterprises, various interest groups gathered around a new tycoon and/or a handful of managers, often with the cooperation of one bank, have started to collect privatization certificates or shares during the second stage of monetary privatization. The result is both an increased weight of outsiders in the new emerging FIGs (Andreff, Radygin, Malginov 1996) and the coordination of (namely supply) strategies among the firms linked through cross shareholding to each group. In Russia, after some delay, the government has begun to sell its remaining shares in some most prominent enterprises, including the ones that were held by commercial banks through the 'loans-for-shares' scheme in 1995. Tenders and auctions for these shares have become a battleground between rival FIGs with a move of the boundaries between their networks of cross ownership. After 1995, acquisitions and takeovers had developed in Russia. Just to mention a few recent examples, Oneximbank took over Norilsk Nickel and Sviazinvest in buying shares through monetary privatization, Yukos and Sibneft merged into Yukos and, with the participation of foreign firms, ARCO acquired 10% of Loukoil's capital, BP took a 10% share in Sidanco, Elf-Aquitaine bought 5% of Yuksi's stock equity. We are now facing the need to study all the networks of these financial stakes linking firms and banks together in order to detect which interest group, possibly associating various outsiders or outsiders to insiders, controls a FIG, i.e. to know really who owns whom. With a FIG structure, two hypotheses of the theory of corporate governance are no longer relevant: on the one hand, the assumed relationship between profitability and the nature (insider/outsider) of corporate governance may well be disrupted in many cases, so that some conflicting results between the aforementioned empirical studies of sampled enterprises may turn us back to the missing dimension of the interest groups involved; on the other hand, corporate governance is not stable and moves with mergers, takeovers, redistribution of shares and possible new alliances or coalitions between insiders and outsiders.

The interest groups backing the FIG structure are going beyond the theoretical cleavage between outsider and insider governance, so that it is no longer realistic to assume that outsiders (and which group among them?) must have, as residual claimants, the last say on firm's boards. Do outsiders (or their representatives) benefit from majority proxy votes for the board of directors? Which outsiders' group does obtain the majority? Is the controlling interest group maintained or not (namely after a proxy fight)? All questions that arise now in the new privatized corporations of the TCs, in particular for FIGs and for FDI that has proceeded through acquisitions of shares in local enterprises, a rather frequent operation (Meyer, Estrin 1997) in most of the TCs. A wide area of research will open as soon as enough information will be published on the precise distribution of the firm's stock equity between various (groups of) shareholders, because it will enable us to detect cross ownership, financial chain control among the firms of a FIG, etc., in using the methodologies used by Berle, Means, Larner and others, or to put it otherwise, it will enable us to study the structure of the 'bank-based financial capitalism' (Mertlik 1998).

Interlocking directorates

When one is to deal with economic situations that fall between market and hierarchy, namely the observed resilient networks of managers in many TCs or the new emerging FIGs, a glance at the literature on interlocking directorates (Bunting, Barbour 1971, Dooley 1969) is a must. The market relationships of the interlocked firms are not nullified, yet interlocks impose some hierarchy (Pennings 1980); both competition and control are implied in a cluster of interlocked firms. Multiple interlocks usually indicate a strong relationship between firms that can express a common interest group governing, controlling or, at least, coordinating the strategies among the interlocked firms. The basic idea underlying interlocking directorates is that corporate control cannot be studied for a firm (a fortiori a FIG) in isolation, contrary to what is done in the standard corporate governance analysis. A well-established result of studies based on the statistical treatment with the graph theory of sampled board mem-

bers, is that in Western market economies, interlocked firms are clustered together by 'linkers' or 'big linkers', i.e. often managers, sometimes owners, who simultaneously belong to the boards of two, three, four, etc., different firms and who increasingly link firms of different national origins; some banks are usually interlocked in each cluster (Fennema 1982, Koenig, Gogel 1981, Pastrò 1979).

Could we expect some interesting results from a similar approach applied to firms in TCs? Let us consider first the TCs in which we can already observe the formation of FIGs, first of all in Russia and some NIS. It would be of strong interest to check whether the industrial firms and banks are connected in the FIGs through interlocking directorates – my guess is that they actually are! The problem is that testing the existence of interlocking directorates requires to have at our disposal information such as the one published (in the West) by Who's Who, Kompass, Moody's, Fortune Directories and so on. Such information is not yet fully available in the TCs, except some pieces of it in journals like Kommersant for instance. However, a first step towards this sort of study consists in examining in how many enterprise boards have a seat some business VIPs named Yevgeny Ananiev (MAPO-Bank), Boris Berezovski (LogoVaz), Mikhail Fridman (Sidanko), Vladimir Gusinski (Most-Bank), Mikhail Khodorovski (Yuksi), Igor Malachenko (NTV), Vladimir Potanin (Oneximbank), Alexander Smolenski (SBS-Agro), Rem Viakhirev (Gazprom), etc., in Russia. Detecting clusters of firms through interlocking directorates might also be helpful in the case of recombinant property (Stark 1996a,b) mixing private and public interests in Hungary[25] or in that of links and alliances between the directors of Czech enterprises (Mc Dermott 1990) which had been swallowed but not dissolved by the privatization process.

Another case in point is the exercise of residual State property rights in partially privatized enterprises, particularly in the TCs where a same State representative can be appointed on the boards of more than one enterprise (up to four in some TCs). A first attempt at elaborating on this kind of analysis is already provided in a recent research on enterprise-State relations after mass privatization in Mongolia (J. Anderson et alii 1997). The authors present data on board membership in order to detect how many representatives do seat on the boards of privatized corporations, and conclude that the State is not a disinterested owner. Indeed, 63.7% of Mongolian enterprises have some State representation on one or both their boards (board of representatives and auditing board) and even 41.5% of enterprises with no State ownership have a government official on at least one of the boards. In view of reinforcing another conclusion of this research, namely that „the picture that emerges is of a cohesive public sector that has arisen after the privatization process" due to State representation on firms' boards, a further research may be suggested: it should consist in checking whether we can find among State representatives some ‚linkers' or ‚big linkers' who interlink the boards of different firms together.

Coalitions, shareholders and stakeholders

The theory of economic organizations, at least a part of it, focuses on coalitions (Cyert, March 1963, Mintzberg 1979, 1983). Among the participants in a firm, some subsets or groups can coalesce around a mutual target of satisfying results under the hypothesis of a bounded rationality of economic agents. At any moment, some coalition dominates the enterprise but can be removed by another in the making. The ruling coalition should adopt a management providing the highest return on assets (Tirole 1988) if we want a formally privatized firm to be transformed into a private firm maximizing its profit. But that is the type of coalition in power and contingencies of economic environment that determine, according to the theory of organizations, the kind of target which must reach a satisfying level in the firm: efficiency, survival, autonomy, growth, asset value or another one (Mintzberg 1983). The emergence of a new dominating coalition within the enterprise can obviously change the prevailing target (Cornelli, Li 1994). Even though survival usually characterizes insider coalitions and profit making outsider coalitions, the real picture in a corporation is often more blurred. It is all the more so when managers are shareowners (and vice versa), when employees own shares, when there is discord within the management team or the corporate boards or (rather frequent) alliances between some managers and core shareholders. More subjective elements can play a role. According to Mintzberg, major factors of a coalition stability are organization (enterprise) ideology, resource slack, and the coordinating role of the chief executive officer (company head director). Once all these factors are taken into account, the objective functions of insiders and outsiders might well overlap in many respects and in many firms. A deeper analysis of the ruling coalitions in various privatized firms would help to detect a revealed (probably

multi-variable) objective function for each type of coalitions. Less simplistic than the distinction between the profit-seeking behaviour of residual claimants versus the rent-seeking and take home gains behaviour of managers and employees, this seemingly old-fashioned analysis is of peculiar interest in a nascent market capitalism, which is the case of the TCs today.

In an inner coalition of the firm can of course participate shareholders as well as stakeholders; in fact the latter are also, to some extent, shareholders, if we consider that a firm needs both finance capital and human capital to function, and thus both are residual claimants, and must be 'rewarded' as such out of the firm's revenue. In a nutshell, this is the core argument of an attempt to renew the analysis of corporate governance (Blair 1995). As to Blair, most Western modern corporations do not fit the Easterbrook-Fischel model of corporate governance and the underlying analysis of the principal-agent, because in practice shareholders are rarely the only residual claimants. As some of the newest work in the economics of organizations is only beginning to recognize and deal with, any time there are parties other than shareholders who make investments specific to a given corporation, namely employees with specialized knowledge or skills. These 'firm specific investments' create several complex governance problems (in the West). If assets such as finance capital and human capital are dependent on each other, co-specialized, by definition neither has much value without the other. Neither as a more legitimate claim for residual revenue than the other. Then the mainstream model falters.

The firm (i.e. capital shareholders) must share with employees some of the economic rents (or quasi rents) from 'their common' enterprise. But, for instance, if the employees helped pay the cost of their training (by accepting a lower wage during the training period) in exchange for a promise of higher wages later, the firm is then in a position to expropriate some of the rents promised to employees by threatening to close down the business unless workers agree to work at a wage that is lower than what they have been promised, or to fire them. The promised higher payments to employees thus are viewed as a cost to the shareholders. Anyway, we can witness no (or very few) close downs or job cuts after each training session. This is due to the most compelling evidence that firm-specific human capital is extremely important to the firm, and finally is worth being extra-paid, of course on the economic surplus generated by the firm. So that the emphasis of the mainstream model on the potential conflict between shareholders and managers is wrong. This is the stakeholder management nexus that is important, whoever the stakeholders (managers, employees, shareholders) are, and the modern corporations should be run in the interest of all the stakeholders, rather than just for the shareholders[26]. In the same vein, Nuti (1995) argues that in employee-owned privatized enterprises, each employee should own a share in the stock equity of the same value as his/her share in the total wage bill. If the wage is assumed to reward specific skills and training, then each employee will share in the residual revenue proportionally to his/her stake among all stakeholders.

A last problem is the legal or non legal behaviour of stakeholders and shareowners. We have already referred to embezzlements, pressures on small shareholders, law violations, exploitation of loopholes and so on, that partly are a legacy of the informational cheeting inherited from the former system (Andreff 1996c). Such distortions call into question the legitimacy of ownership and of sharing the residual revenue with (or among) economic criminals. Beyond the moral concern, it is an issue of economic efficiency just like it is with other illegal or corrupted activities. Corruption is of course a kind of criminal behaviour which threatens the development of the market economy. In addition, organized crime, illegal transactions, protection rackets impose an economic cost on the TCs (the more eastwards, the higher cost) in the forms of distorted resource allocation, a heavy „private tax" burden[27], limited competition and capital flight abroad. The average corruption score, obtained in the World Bank survey of 3,600 entrepreneurs in 69 countries, is higher for the TCs than in any other region in the world (EBRD 1997). In many TCs, in particular in NIS, it seems that after the collapse of the planned economy managers continue to develop networks of personal relationships with government officials and with other firms (Andreff 1996c, Rizopoulos 1997). Corruption is often the fuel for such networks. This obviously means that managers involved in corrupted networks either are not under the control of supposedly honest owners or are colluded with new shameless or somewhat criminal tycoons, namely in Russia and eastwards. Anyway, in all such cases, privatization is then turned into its contrary, business corruption ,which was not the purpose of the privatization process and might not be a foot ahead on the path to a true market economy. Such a deviation is the more dangerous one for the future of NIS and should not remain uncriticized and unrepressed; only a stronger

Table 1

Index of GDP growth and the share of private sector in GDP of transition countries (1990, 1995)

Countries	Index of GDP growth		The share of private sector in GDP (in %)	
	Ig 1990	Ig 1995	Sps 1990	Sps 1995
Albania *	86,9	113,4	5%	59%
Armenia *	91,8	105,2	12%	44%
Azerbaijan *	88,7	82,8	10%	25%
Belarus *	96,8	90	5%	12%
Bulgaria	90,9	102,5	9%	35%
Croatia **	91,5	98,5	10%	47%
Czech Rep.	98,8	105,2	5%	69%
Estonia	91,9	102,5	10%	60%
Georgia *	95,7	102,4	26%	30%
Hungary	96,7	102	19%	60%
Kazakhstan *	99,1	91,1	7%	25%
Kirghizstan *	104,8	93,8	7%	40%
Latvia	97,3	98,4	10%	57%
Lithuania	93,1	102	11%	55%
Macedonia **	89,8	97	14%	40%
Moldova *	98,5	97	10%	30%
Poland	88,4	107	27%	58%
Romania	91,8	106,9	17%	37%
Russia	96	96	6%	58%
Slovakia	97,5	107,4	6%	59%
Slovenia	95,3	104,8	11%	37%
Tadjikistan *	100,2	87,6	10%	15%
Turkmenistan*	101,8	92,5	10%	15%
Ukraine *	96,4	88	10%	36%
Uzbekistan *	104,3	99	10%	30%

* Net material product in 1990; ** Gross material product in 1990.
Sources : UNECE (1996) for growth indexes and World Bank (1996) for the share of private sector in GDP.

State could crack down on corruption with a chance of success (Andreff 1995b). After the first stage of transition, when prominent neo-liberal assertions associated State minimalism with market efficiency, a closer analysis is now re-evaluating the role of the State in the market economy, and influential economists like N. Stern, J. Stiglitz, or E. Malinvaud (1997) emphasize the importance of cooperation and partnership between public and private activities. This does not mean increasing the government interference in privatized enterprises which still remain pervasive in many TCs, in particular in NIS. State regulation is required to control again monopoly power in privatized utilities and sectors where private stakes have won privileged position, often from the government and sometimes through illicit or corrupted means.

Conclusion: Where has all the privatization gone?

„Rather than an unquestionned boon, privatization thus becomes an ambiguous, open-ended process that might lead to bad as well as good consequences" (Frydman, Rapaczynski 1994). Let us conclude first with the good news. Small privatization is a big success. Privatization, as a general drive of the whole economy, has improved macroeconomic performance as well as microeconomic performance for a subset of large and medium-sized firms. The privatization process has been able to attract significant FDI and some domestic strategic investors. But if we stopped the listing here, it could only be for the sake of providing a rosy picture. The overall picture of privatization also encompasses a lot of deviations from the initial objectives of the privatization drive, the short-list of which is: ineffective corporate governance, corruption, ‚socialization' and municipalization of assets, a variety of ownership types (and not only a fully-fledged private ownership) including a 'sticky' residual State ownership. Many of these distortions reflect some kind of path-dependence in the privatization process.

Some readers will regard my second concluding remark as a piece of economic semantics. Well, the result of a process transfering assets out of the central State hands is defined as privatization. What about this label when ownership falls into the hands of employees? Why not call it employee-owned privatization? If so, not long ago employee-ownership was associated with ‚socialization' of ownership, profit sharing and self-management. Should we also speak of privatization when assets are transferred to municipalities? Why not 'municipalization' of ownership? In old times – maybe not so old – a manager-controlled enterprise simply was denominated a managerial firm (remember Burnham, Galbraith, Marris), and a „mixed" enterprise was the label for both a private firm with residual State ownership after privatization and a public enterprise with residual private ownership after nationalization. Thus the privatization process resulted in ... some privatization as well as some socialization, municipalization, mixed ownership and 'managerialism'. In the first years of transition, in many circles, it was probably taboo to put it this way. But all these forms of ownership have existed, to some extent, in Western economies in the past, and some have not yet completely disappeared. Probably was it dreamed that the TCs could jump over this earlier stage of capitalist development directly to the ‚realm' of international finance markets and economic globalization, starting the whole story by its very end. The economic reality is that the TCs have got through the privatization process a ‚motley crew' of ownership structures for a while.

Table 2

Big privatization by mid – 1995 (number of entreprises)

Countries (1)	State-owned trusts (2)	Trade sales (3)	Mass privatization	Employee buy-outs	Tender price offer	Other methods	Liquidation	Privatized firms (4)	State control remains (5)
Belarus	3000	25		125				150	5%
Bulgaria	3500	286		109				395	11%
Czech Rep.	4319	3898	1622	n.d.	n.d.	5310(7)	260	3505	81%
Estonia	500	357		120 (6)				357	71%
Georgia	1100	6		19				25	2%
Hungary	1848	866	2	2787(6)		662	536	1400	76%
Kazakhstan	n.d.	4	532					536	n.d.
Latvia	650	45		200		55	n.d.	301	46%
Lithuania	4800	62	2920	n.d.				2982	62%
Moldova	3000		800					800	27%
Mongolia	1406	41	430	98				650	46%
Poland	8200	142		806	22	165	1400	2535	31%
Romania	7100	10		981	9			1000	14%
Russia	31000	40	4400	11520			1000	17000	55%
Slovakia	1265	361	392	n.d.		135(8)	n.d.	556	44%
Slovenia (9)	1280	60	n.d.	25			20	113	9%
Ukraine	3500	1	49	3500				3550	n.d.

(1) The only medium and big sized enterprises taken into account are those with 50% or more State-owned stock equity.

(2) OECD estimate of the number of medium and big sized enterprises at the starting point of privatization.

(3) Direct sales to private buyers, auction sales and tenders of State assets and enterprises.

(4) This number can be different from the sum of figures given in all the left-hand rows, due to break-ups, liquidations, mergers, etc., going alongside with privatization.

(5) Estimated percentage which is only indicative insofar as it is biased by what is stated in (4).

(6) Buy-outs for compensation vouchers.

(7) Of which 4380 are given away for free to municipalities and 930 are subject to restitution.

(8) Free transfers to municipalities.

(9) Data by mid-1994.

Source: Adaptated from OECD (1995).

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Table 3

Foreign direct investment and privatization in transition countries (1995)

Countries	FDI stock per capita (1)	Share of private sector in GDP(%)	Countries	FDI stock per capita (1)	Share of private sector in GDP(%)
Armenia	44%	5.56	Lithuania	55%	38.92
Azerbaijan	25%	39.08	Moldova	30%	24.32
Belarus	12%	3.86	Poland	58%	222.08
Bulgaria	35%	40.00	Romania	37%	42.59
Czech Republic	69%	398.06	Russia	58%	27.58
Estonia	60%	424.67	Slovakia	59%	108.33
Georgia	30%	2.55	Slovenia	37%	278.42
Hungary	60%	1289.90	Tajikistan	15%	3.77
Kazakhstan	25%	41.81	Turkmenistan	15%	48.78
Kyrgyzstan	40%	8.51	Ukraine	36%	16.07
Latvia	57%	180.00	Uzbekistan	30%	11.18

(1) Stock of foreign direct investment in dollars divided by population (M. & W. Andreff 1998).

Sources : UNCTAD (1997) for FDI, World Bank (1996) for the share of private sector.

Table 4

Foreign share of privatisation and methods of privatization

Countries	Foreign share (1)	Trade sales to outside owners	Voucher mass privatization	Management-employee buy-outs	Other methods
Bulgaria	24%	Primary	Secondary		
Czech Republic	5%	Secondary	Primary		Tertiary
Estonia	14%	Primary		Secondary	
Hungary	58%	Primary			Secondary
Latvia	8%	Secondary	Primary		
Lithuania	2%		Primary	Secondary	
Poland	22%	Tertiary	Secondary	Primary	
Slovakia	13%		Secondary	Primary	

(1) Percentage of foreign capital in the total transaction value up to January 1996 (OECD).

Source: EBRD (1997) for the ranking of privatization methods.

Table 5

Share of the unofficial economy in GDP, 1989–1995, selected transition economies (in %)

Countries	1989	1990	1991	1992	1993	1994	1995	Variation *
Azerbaijan	12.0	21.9	22.7	39.2	51.2	58.0	60.6	(+48.6)
Belarus	12.0	15.4	16.6	13.2	11.0	18.9	19.3	(+7.3)
Bulgaria	22.8	25.1	23.9	25.0	29.9	29.1	36.2	(+13.4)
Czech Republic	6.0	6.7	12.9	16.9	16.9	17.6	11.3	(+5.3)
Estonia	12.0	19.9	26.2	25.4	24.1	25.1	11.8	(-0.2)
Georgia	12.0	24.9	36.0	52.3	61.0	63.5	62.6	(+50.6)
Hungary	27.0	28.0	32.9	30.6	28.5	27.7	29.0	(+2.0)
Kazakhstan	12.0	17.0	19.7	24.9	27.2	34.1	34.3	(+22.3)
Latvia	12.0	12.8	19.0	34.3	31.0	34.2	35.3	(+23.3)
Lithuania	12.0	11.3	21.8	39.2	31.7	28.7	21.6	(+9.6)
Moldova	12.0	18.1	27.1	37.3	34.0	39.7	35.7	(+23.7)
Poland	15.7	19.6	23.5	19.7	18.5	15.2	12.6	(-3.1)
Romania	22.3	13.7	15.7	18.0	16.4	17.4	19.1	(-3.2)
Russia	12.0	14.7	23.5	32.8	36.7	40.3	41.6	(+29.6)
Slovakia	6.0	7.7	15.1	17.6	16.2	14.6	5.8	(-0.2)
Ukraine	12.0	16.3	25.6	33.6	38.0	45.7	48.9	(+36.9)
Uzbekistan	12.0	11.4	7.8	11.7	10.1	9.5	6.5	(-5.5)
Mean	**13.6**	**16.7**	**21.8**	**27.7**	**28.4**	**30.5**	**29.0**	(+15.4)

* From 1989 to 1995

Source: EBRD (1997).

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Footnotes

1 This paper was read at the Conference on Privatization, Corporate Governance and the Emergence of Markets in Central-Eastern Europe, Berlin, May 22-23, 1998

2 In this paper, TCs are meant to be all the former CMEA and former Yugoslavia countries, even though we will only focus on some most meaningful experiences with privatization.

3 A more comprehensive coverage and personal analysis of privatization objectives can be found in Andreff (1993a, 1993b, 1994a,b).

4 For a personal comparative evaluation of the efficiency of all the existing – standard and non-standard methods (techniques) of privatization -, see Andreff (1992, 1993a,c, 1994a,b,c).

5 Path-dependency is the core anaytical framework of some non-standard theoretical approaches to economic transformation in TCs, namely: Chavance-Magnin (1995), Mc Dermott (1994), Rizopoulos (1997), Stark (1992, 1996a, 1996b), Van Zon (1995). We have assessed elsewhere how much it is valuable for increasing our analytical understanding of the post-Socialist 'systemic change' but also which are the methodological hindrances to its successful empirical test in Andreff (1996c).

6 For large-scale privatization, 1 means little private ownership, 2 comprehensive scheme almost ready for implementation, 4 more than 50% of former State-owned enterprises in private ownership and significant progress in their corporate governance. For small-scale privatization, 2 means substantial share privatized, 4 complete privatization of small companies with tradable ownership rights.

7 According to estimates quoted in EBRD (1997), on average in 1995, the ab initio private sector accounted for 42% of GDP in the CEECs (including the Baltic states) against only 23% in the NIS.

8 For instance, between 1992 and 1995, industrial output in Poland increased by 34%, and the new private sector accounted for approximately two-thirds of this increase (Gomulka 1997)

9 In 1997, according to EBRD (1997), the private sector share had reached or exceeded 50% of GDP in 19 of the EBRD's 26 countries of operation, while economic recovery was on the tracks in 18 of them.

10 Bulgaria, Czech Republic, Hungary, Poland, Romania, Slovakia and Slovenia.

11 The results of several studies or inquiries and with various enterprise samples converge towards such a conclusion, namely Pinto, van Wijnbergen (1995), Andreff (1995), Mickiewicz (1996), Nivet (1997), Grosfeld, Nivet (1997).

12 The alternative „long way" to privatization advocated, on various grounds, by Janos Kornai, Peter Murrell, Wlodzimierz Brus, David Stark, Kazimierz Laski, Lubomir Mlcoch, Lubomir Rychetnik, myself and (a few) others, actually has not so far been adopted in most TCs, partly due to political and ideological reasons (according to Mlcoch 1997), and not after a comparative assessment of how much efficient are all the different methods of privatization, namely in terms of corporate governance, as suggested in (Andreff 1991a,b, 1992, 1993a).

13 Namely R. Anderson et alii (1997), Barberis et alii (1996), R. Frydman et alii (1997).

14 Namely Lastovicka et alii (1995), Capek, Mertlik (1996), Coffee (1996).

15 See R. Anderson et alii (1997), Carlin et alii (1995), Carlin, Aghion (1996), Frydman et alii (1997), Grosfeld, Roland (1995)

16 This findings is less mainstream than expected and is interpreted by the authors as follows: 'domestic non-financial companies' may be a label that sometimes hides more complex insider holdings resulting from cross ownership (a nice introduction to the third part of this paper).

17 Not much mainstream either.

18 Within the tight model of principal-agent realtionships.

19 The swiftly growing literature on residual State property primarily focuses on partly privatized enterprises: Bim (1996), Brom (1996), Mihaly (1996b), Pistor, Turkewitz (1996), Radygin (1996), Schwartz (1996), Thieme (1996).

20 Sometimes, the residual State property is only refered to as „shares that are still kept on the State's books, as a consequence of a partial privatization of formerly wholly-owned State assets" (Thieme 1996).

21 Especially in countries where a same State representative can seat on the boards of more than one enterprise.

22 Mihaly (1996b) reports that desk officers are strongly motivated and well-paid, thus they tend to use the economic and managerial power they possess.

23 Here we also could mention the experience and failure of the Algerian holdings (Fonds de participation) launched, as a pre-privatization device, in 1988 and finally abandoned in 1996 (following the experts report to the Minister of Restructuring and Participation of Algeria in 1994 the writing of which we have participated to). See also Andreff (1995a).

24 Or, more often, distorsions introduced by a sort of non legal or criminal privatization of management with the help of former (or new) informal networks connecting managers to the irregular economy and, to some extent, to the mafia (especially in NIS). Contrarily to Pejovich (1997), we consider that there cannot be any „case for the Mafia" in a successful process of privatization (and transition).

25 By the way, ownership links between banks and SOEs were cut drastically in Hungary, and by 1996 cross ownership has become rare exception (Mihaly 1997b). It would be interesting and significant to investigate whether interlocking directorates have been maintained between these entities.

26 For a more comprehensive, detailed and convincing demonstration, see Blair (1995).

27 One can find in Raiser (1997), the rates of „unofficial fees" (in dollars) that were to be paid in Russia and Ukraine, in 1994 and 1996, for „favours" such as enterprise registration, each visit by fire, health or tax inspector, each phone line installation, a lease in State space, an export or import licence, a border crossing, and a hard currency loan. Of course, the most criminal private taxation escape to the scope of (safe) inquiries.

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