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## ПРЕГЛЕДНИ ЧЛАНЦИ

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### OUTCOMES OF UP-TO-DATE PRIVATIZATION

#### Abstract

*The paper presents data and observations related to the transition process carrying out in the Serbian economy. It exposes known concepts, efforts and difficulties encountered by the society in attempting to achieve the transition results. There is also given a critical review of measures taken to date by the society in terms of implementation of privatization in our country, and estimation of their effects to privatization speed and results.*

*Although there are positive movements in the transition of Serbian economy, it is expected that they could be better and bigger if the Government monetary and fiscal policies were less restrictive. Then, the competitiveness of our economy would also be better, because the foreign exchange policy would be different. With all that, privatization would not be just the bare change of the title, but it would be carried out by introduction of better (modern) technology.*

**Keywords:** Transition, privatization, reform, business, market economy, competition, socially-owned capital and state capital, property.

### РЕЗУЛТАТИ ДОСАДАШЊЕ ПРИВАТИЗАЦИЈЕ

#### Апстракт

**Резиме:** У раду су презентирани подаци и виђења процеса спровођења транзиције у привреди Србије. Изложене су познате концепције, залагања и потешкоће друштва да транзиција да резултате. Дат је и критички осврт на до сада предузимане мере друштва на плану имплементације приватизације у нас, те оцена њиховог дејства на брзину и резултате.

Иако има позитивних помака у транзицији српске привреде, очекивања су да би они били бољи и већи да су монетарна и фискална политика Владе мање рестриктивне. И конкурентност наше привреде била би тада боља, јер би и политика девизног курса била другачија. Уз све то, и приватизација се не би сводила на промену титулара, већ би се вршила уз увођење модерније технологије.

**Кључне речи:** Транзиција, приватизација, реформа, бизнис, тржишна привреда, конкуренција, друштвени и државни капитал, својина.

## Introductory Considerations

From the very beginning of transition in Eastern Europe and up to date, there have been discussions in economic science regarding the best strategy – is it better to carry out the reforms in the widest front as soon as possible, or is it better to establish a reasonable order of reforms and carry them out gradually. The basic argument of the first consideration is that it is necessary to use a good opportunity for reforms, which, for political reasons, may not be maintained for a long time and everything should be done to quickly carry out the basic reforms in order to prevent forces wishing to return to the old situation. Main arguments of the second consideration are, firstly, that it is necessary to introduce order in the sequence of reforms carrying out to ensure efficiency, and secondly, that for political reasons, it is necessary to build up other measures on first measures good results, which would bring growing respect for authorities carrying the reforms out.<sup>1</sup>

The rethorics of our economic and political elites, all the more frequently contain „the stop-watch“ – term-bound privatization, more and more worse forecasts of current transition status, but also proofs of all the more present disputes of some, until yesterday, untouchable beliefs of our economists. However, we all know well that transition has its price and that the authorities and the public should eventually understand the situation in which the economy and businessmen are, the climate for successful business and that finally they should take the side of development-relevant people, entrepreneurs, those who save and dispose of the property significant for our economy. Namely, the practice of rejection and first reactions (like „Where and how he/she could acquire that and what dishonest actions and procedures he/she undertook to accumulate the wealth“) addressed to those who acquired something and have possessions, must be left behind?

With such behaviour and mentality it is very difficult to overcome the existing bad business climate and speed up the transition to the market economy.<sup>2</sup>

It may often be heard that transition of our economy could go much faster, without thinking of what it would eventually mean. I am not one of those who think that way, and I urge that neither the speed nor the progress degree of the transition way should be fetishized, because it is a big issue at what speed and tempo should the transition of our economy and the society be carried out. I think that there are two basic problems which are often neglected, and even mixed up in our professional, but political public, as well. One of them is: how we see ourselves in the future? Here, it seems that there are no dilemmas and disagreements, we travel the road which leads to: the market economy, with democratic government, fair elections, transparent control of all centers of power, safe and protected private property, observed contracts, and independent and efficient judiciary.

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<sup>1</sup> See about this in more detail in: Prof. dr Borivoje B. Prokopović; Modern Economic Systems (3<sup>rd</sup> issue), Proinkom, Beograd, 2005., pp. 314 to 324.

<sup>2</sup> Opinions, according to which the basic obstacle to transition in Serbia is in self-management awareness of many citizens, are true. The expression of such awareness are opinions that enterprises exist in order the employees could receive wages and „hot meals“, that the state is responsible in case the wages payment is not regular, or in case somebody lost the job, that it must be compensated on the account of tax payers, that the one who earns something should share it with those who have not, that an individual should not bear the risk, but the state should fully insure the citizens from all risks, that each citizen of Serbia has inalienable rights to various services free of charge, etc..

But, when it is to do with speed of goals achievement, there are differences; so many people think that it can be done overnight, right away and now. And, at that point, it seems as if it is being forgotten that great speed may cause demolishing of those bad institutional mechanisms, which are better anyway than no mechanisms at all. Asymmetry which is present in these processes – old structures demolishing goes quickly, while new structures are being built slowly - is burdened with risks of entering into institutional gaps, which may be very bad. And it may be particularly bad when the existing enterprises are liquidated, leaving a great number of employees without jobs. It is bad, in the first place because of the fact that, when one company ceases to exist, there emerges the question if there will ever be established some new or similar company. Secondly, by a company liquidation, many people lose jobs and work on which their existence depends, because they have no possibility of employment. In that way, it is not only that a great number of jobs is lost, but also a part of newly created value, that contributing to decrease of our gross domestic product.<sup>3</sup>

Anyway, I think that the speed of transition and the speed of Serbian economy and society restructuring should be adjusted to our abilities to build new institutions and relations in order not to have the situation where we disintegrate old structure, without starting to build something new. It would be the worst possible variant, where higher speed may cause invaluable damages.

## 1. Up-to-date Problems and Outcomes

When the deputies of the National Assembly of the Republic of Serbia were passing the new Privatization Law (in July 2001), which replaced the Law of 1997, they had in mind the efforts of the society to speed up the privatization process of socially-owned and state capital, in the first place that of medium and big enterprises. It really happened, because for only two years of its application, there were privatized 1.999 enterprises, of that number 878 in 2003., and 1.121 in 2004.

From the total number of privatized enterprises the greatest number goes to small ones (1422), while the least number goes to big companies (around 100). The number of employees in them was 175.625, which makes around 15 % from the total number of employees (1,196.833) of all 75.885 enterprises at the end of 2004.

The buyers of privatized enterprises capital (stocks and shares) are domestic and foreign natural and legal persons. In that, foreign companies and natural persons were primarily buying social capital of big enterprises, in the first place, those solvent and prospective.

It is always spoken about the necessity to attract much more foreign direct investments, because it would significantly increase the level of economic activity.<sup>4</sup> And we are the witnesses that currently there are no such effects, because, generally, the enterprises are being bought with the existing technology. As a rule, new owners want to get rid of a significant number of workers, in order to effect in that way the expected increase of the labour productivity.

It can also be often heard: „Let the foreign investors go in, and the export sector of economy would develop, increasing export significantly in that way“. The question may be immediately posed at that point, in terms of how the export could be increased when, according

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<sup>3</sup> Ibid.

<sup>4</sup> See Ekonometar; Četiri godine tranzicije u Srbiji (Four years of the Transition in Serbia) (1).

to MMF Report, we have lost a lot in price competitiveness. Namely, in the existing conditions, productivity should enormously grow in order to provide space for much better sales of our economy at the world market. In that, it is not doubtful at all, that we need direct foreign investments, particularly *greenfield* investments, but currently some essentially significant inflow implies much better business climate.

Actually, the circumstance that big enterprises (total 667) are most endangered and with biggest losses, is the main reason for their slow privatization. It is clearly confirmed by facts that these 667 big enterprises used to employ 543.392 workers by the end of 2004, which makes 45.4 % of the total number of employees, that 67.75% of totally cumulated and 55.53% of current losses may be subscribed to these, that their missing long-term capital amounts to RSD 378.2 billions (dinars), which makes 52.9 % of the missing socially-owned capital of all 75.885 enterprises, that 1/3 of them lost the entire or prevailing part of their own capital through various losses.<sup>5</sup>

Therefore, it is clearly expected that privatization of 500 big enterprises with around 400.000 employees, implies, in the first place, taking over of endangered enterprises, with recapitalization, the primary goal being rehabilitation, and which is, certainly, not possible to do with current privatization regulations, as well as the practice of privatization revenues inclusion in the state budget, which are spent to cover the projected budget expenses, without any impacts on the financial position of the economy.

## 2. Credit-Based Privatization

A special privatization problem is the circumstance that buying of socially owned capital of numerous enterprises has been financed by the money, originating from bank credits, granted at very strict conditions in terms of interest and principal settlements. Due settlements of the mentioned credit liabilities means not only operating with relatively high profit, but also the possibility to use, for that purpose intended, additional capital release through, so-called „*cash flow*“ (for the amount of not spent depreciation). Otherwise, the beneficiaries of credits, intended for liabilities settlement based on social capital buying enter hopeless economic situation and insolvency.

Through public bidding (auction) and public tender method, Privatization Agency is in charge of organization and sales of enterprises with state and socially-owned capital, which, for that purpose defines the initial sales price, based on its estimation and verification.<sup>6</sup> It is not rare that the price is set very low, that being achieved by shifting the assessment day even several years back in time, in which case the price is under strong influence of inflation which was very high in two consecutive years, 2003 and 2004 (11.1% and 13.7%, respectively), while in 2005 it was over 17% - the highest in Europe. Import was covered with export in 2004 with 30% and in 2005 with 41%. It explains why 70% of drugs factory „Zdravlje“ Leskovac

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<sup>5</sup> Big internal debts (in relation to gross domestic product) make normal functioning of financial system difficult. The biggest part of these debts is concentrated in the relation enterprise – state. The status of such debts has been tried to solve by the Law, regulating receivership and liquidation matters, but without success. There are proposals for it to be solved by multilateral system of debts and receivables settlement, and even to have the state its receivables from industry converted into temporary (till the end of financial crisis) enterprise deposit.

<sup>6</sup> Ibid.

estimated value, in the amount of 2.7 billions dinars was sold in October 2002 for only 3.5 million Euro, which is not an isolated case.

In contracts on socially-owned or state capital buying, the Privatization Agency, as a rule, was imposing on buyers the obligation of some amount additional investment in facilities (investments), but in that, the opportunity was missed to impose the obligation of taking the enterprise back to its financial balance, which is the request of the safety and liquidity of the enterprise finance principle. Instead of that, new investments conditioned new aggravation of financial structure, that resulting from the fact that each new investment requires additional working capital.<sup>7</sup>

The circumstance that the enterprises sold had, as a rule, disturbed financial structure, which means that they did not have enough ownership, and particularly, not enough long-term capital, explains all the more difficult situation in view of capacity to settle the due liabilities (insolvency). For that reason, much more attention should be paid in future to general goals of sustainable development conditions creating:<sup>8</sup> a) economically justified production, oriented to growth, which ensures opportunities for future generations; b) improvement of employment; and v) reducing pollution and other pressures to ecosystem.<sup>9</sup>

### 3. Advancement to Market Economy

According to the achieved transition results, it may be said that we have made a significant advancement towards the effective market economy, but also that additional endeavours are necessary to make our economy capable and competitive at the European Union market.<sup>10</sup> In the past period, the economy of Serbia continued with powerful economic growth, however, on the macroeconomic plan, there were turbulences. As a backup of big challenges for Serbian economy there may be used the data as follows:<sup>11</sup>

- a) Insufficient number of direct foreign investments is the result of instable political climate;
- b) There is a serious standstill in structural reform of the economy;
- c) High unemployment;

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<sup>7</sup> Crucial limiting factor of private sector development in Serbia is weak banking system, which does not succeed in accompanying the finance needs. Namely, the old state banking system did not have that role, so practically, the private enterprises had not been credited. After its liquidation, still new banking system is in process of formation, which, being small, does not have necessary financial potential.

<sup>8</sup> Munter, K; Counselling report on development of industrial strategy in Serbia and Montenegro in the context of EU stabilization and accession process, SCEPP, Belgrade, 2003, pages 26. to 28.

<sup>9</sup> Ibid.

<sup>10</sup> The initial orientation in transition of Serbian economy was good, because there was a sincere determination of new leaders for reforms, alleviated by the needs of a political moment or party-spirited rating. Transition was facilitated to some degree by using experiences gathered in other transition countries, owing to late transition in Serbia. In that way, for example, better privatization model was selected, and unnecessary money spending on rehabilitation of banking system was avoided. However, in every country there are local specificities, on one hand, and transition has not produced definitive instruction manuals for changes, on the other, so that there is left a lot of space for innovative approach to Serbian reforms.

<sup>11</sup> Group of authors; about our economic reality today, Ekonomika, Niš, No. 5-6/08.



- d) Increasing inflation pressures;
- e) Instability of the exchange rate and prices;

Monetary policy enabled us to achieve the goal in terms of better inflation control in 2007. Similarly, there was achieved some advancement in privatization, and significant advancement was also noted in non-banking financial sector.

In the same period, negative foreign trade balance got increased, that is, indebtedness to foreign creditors got increased. Therefore, since in the long-run, there exist all conditions for relatively fast and sustainable economic growth, it is necessary that its framework be export-oriented production, no matter if it is to do with industry, agriculture or services. In that, the greatest role should be played by new private enterprises and generally, private economy. Regarding the state, it must completely withdraw from the economy. In that, it must be started from the fact that our economy cannot rely on cheap labour force, as its competitive advantage on European or world markets. This is because of the fact that on that basis, there are many competitive economies. Therefore, it is necessary to make more investments in human resources and all forms of infrastructure, because it is possible to be competitive only with quality and lower trading and transportation costs. Nowadays, the financing quality got worsened on the internal plan, and macroeconomical vulnerability was increased due to global financial crisis. Tax policy still remained expansionistic, and, as such, it impacts the growth of external imbalances, which makes inflationary pressures in 2009, as well.

In spite of strong economic growth during the last years, unemployment is still a big challenge of the society. It is interesting that the economy of our country is, at the same time, affected by the lack of skilled workforce, which requires from the society to start dealing with reform of education.

Although in the past period some movements happened in privatization of companies and banks owned by society or state, there has not been established competitive and dynamic private sector yet. Exaggerated bureaucratic requirements and complicated legislative procedure still have bad impacts to the market and market relations. However, there are some announcements from the Companies Registration Agency that businessmen will soon be able to register companies in Serbia more easily. In order to have their company registered, the owners will not be obliged to go to Tax Administration to apply for Tax Identification Number (PIB), but together with registration application for company foundation, submitted to the Companies Registration Agency, the procedure will be automatically initiated for PIB obtaining. The Agency will get that number from the Tax Administration in one day and enter it in the Decision on Company Foundation, on the occasion of registration, and that will be the end of the entire foundation procedure.<sup>12</sup> The so-called legal predictability and trust in judicial system are still limited, particularly in view of exercising ownership rights, and the impact of the state and its bodies to competitiveness is still high.

In sectors and branches analyses, it is necessary to define a development role and tempo of growing of the second key activity and change in the investment plan. In that regard, it is necessary to define tasks for sectors, the basic role of which would be maximization of export and reduction of trade deficit, and ensuring of quality infrastructure and competitive

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<sup>12</sup> According to the World Bank Report on business operations in 2008, in order to start business in Serbia, one will need 23 days and 11 procedures. Registration costs amount to 8.9 % of BDP value *per capita*. In comparison to other countries of the world, such conditions are not stimulant for investors. Anyhow, it is possible to found a company in Slovenia in two to five days, in Hungary – in two to thirty days, in Bulgaria - in 14 days, and in Romania in three days.

domestic inputs.<sup>13</sup> Priority in further transition efforts must be given to issues beyond economy, because the transition is inhibited just there. The first one is the issue of the state and its behaviour, the second – democracy stabilization and maturity and the third one – building of institutions. In parallel with them, there come narrower economic measures: continuation of privatization, key issue of monetary and financial policies (RSD exchange rate), reduction of tax and public consumption, public enterprises restructuring, etc.<sup>14</sup>

Serbian economy restructuring programme realization must, basically, be accompanied by modernization on bases of legal regulations, standards, work technology, organization and information structure of EU, and the existing and new industrial structures of EU.<sup>15</sup>

After the drop of entrepreneurial initiative by the end of the last year, in the sense of reduced number of new business entities, in the beginning of this year the number of new companies is growing. In Serbia, the new private sector has grown, but it does not represent as big driving force as it was the case in other countries in transition (e.g.: in Poland), where in a very short time it became the main bearer of the economic advancement. The causes for that were, firstly, in the fact that the private sector had existed and was relatively developed even before the October changes, while in most transition countries it was starting from zero, and for that reason, it was growing very fast during first phases. Secondly, an important limiting factor of the private sector development in Serbia, is a weak banking system, which had great difficulties in accompanying finance needs. So, from the beginning of this year, there were founded 1.969 new industrial companies and 7.133 firms.

#### General structure of registered companies in Serbia

Type	Number	%
Industrial companies	111.874	100,00
- Big and medium	3.373	3,01
- Small	108.501	96,99
Entrepreneurs	217.433	100,00

*Source: Daily newspaper Politika, 21 March 2009*

Quite a big grey economy sector still exists due to weak economic framework, inadequate tax policy, weaknesses in the law implementation, including corruption and organized crime suppression.

### Conclusion

From all aforementioned, it is clear that the way of privatization, adjusted to stipulations of the Law, as of 2001, has the following effects:

1. vanishing of socially-owned capital, to be eaten by its inclusion in the budget;

<sup>13</sup> See Guidelines for Doing Business with the EU – Industry, Fond za evropske integracije, Beograd, 2006.

<sup>14</sup> Prof. dr Borivoje B. Prokopović; Ibid.

<sup>15</sup> Smernice za poslovanje sa EU; Ibid.



2. capital outflow from the country by transfer of profit, paid on behalf of dividend and share in the profit, to the foreign companies owners;

3. difficulties in interests payments and repayment of maturity installments of credits, granted for settlement of commitments based on social capital buying in tender procedure;

4. additional disturbance of financial structure, with increase of current and cumulated losses, by conditioning the inflation increase and reduction of the employees number;

5. Inability to privatize around 400 to 500 financially broken and solvency endangered big enterprises with almost 400.000 employees, which may be a decisive reason for the state decision to solve the respective problem according to the example of Smrederevo company „Sartid“, in which case the biggest price would be paid by all big creditors, and then, viewed in long-term period, by all citizens.

Due to big difficulties on the way to privatization problems solving, with application of now valid Law provisions, it is necessary to have expert approach to this problem solving, where it is, in the first place, indispensable to have wide consideration of the complete situation in a round table discussion, where experiences and knowledge, necessary to gradually bring the transition situation of our economy to the end, could be exchanged. Otherwise, even worse situation should be expected in this field. Currently, priorities of further transition efforts must also be those beyond the economic domain, because the transition is mainly inhibited just there.

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