

**PRIVATISATION AND RESTRUCTURING OF THE SOCIALLY- AND STATE-
OWNED ENTERPRISES IN THE REPUBLIC OF MACEDONIA AND ITS
IMPLICATIONS ON CORPORATE GOVERNANCE**

by

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The process of privatisation of the Macedonian socially owned companies began in late 1989 (with the Law on Social Capital of the former Yugoslav Federation). However, the process has really intensified in the last eight years, i.e. since the Macedonian Law on Transformation of Enterprises with Social Capital has been enacted, in 1993.

The Macedonian model of privatisation has a commercial, case-by-case approach. There are numerous reasons for selecting this approach, instead of the alternative, mass privatisation approach. The most important reason for adopting the case-by-case method of privatisation was the fact that the improvement of the efficiency of the economy, through increase of the enterprise management efficiency, was the primary objective of privatisation.

The main objective of the Law on Transformation of Enterprises with Social Capital – to transform the socially owned enterprises into companies with fully defined ownership rights, was associated with several others, such as:

- increasing the efficiency of the economy;
- attracting foreign capital;
- developing a capital market;
- providing new possibilities in servicing the internal and external debt of the country

According to the existing legislation (Law on Transformation of Enterprises with Social Capital – Official Gazette of RM 38/93, 48/93, 21/98, 25/99, 39/99, 81/99; 49/00) Law on Transformation of Enterprises and Co-operatives in the Agricultural Sector – Official Gazette of RM 19/96, 25/99; Law on Privatisation of the State Capital in Companies – Official Gazette of RM 37/96, 25/99) 1800 enterprises are subject to privatisation (1400 non-agricultural and 400 agricultural).

The main results from the privatisation process as of 30 of June 2001 are as follows:

1. 1,646 enterprises have been completely privatised and 113 additional enterprises are in process and are expected to get privatised in the next few months.
2. The respective figures presented according to the number of employees in each stage are: the completely privatised enterprises employ more than 226,500 employees and the enterprises, which are in the process, employ around 12,000 employees.
3. According to the financial reports, it was assessed that the already privatised enterprises have equity worth almost USD 2.1 billion, and the value of the equity of the companies to be privatised is around USD 50 million.

At present, privatisation is not performed in the following entities:

- Enterprises and organisations that conduct activities of special national interest;
- Public utilities and enterprises that conserve water, forests, land and other public goods;
- Enterprises designated as monopolies, that are to be privatised under separate laws.

Banks are being transformed as a part of a wider financial sector reform. Their privatisation is a passive one and it depends on the privatisation of the enterprises which are their founders.

However, looking for full capitalization, a number of Macedonian banks found foreign investors, supported by the EBRD and IFC.

Meanwhile, enterprises of infrastructure and utilities (e.g. the Macedonian Power Utility) are currently being prepared for privatisation, and the Macedonian Telecom was sold to the Hungarian telecom company MATAV in the beginning of 2001.

The Law on Transformation of Enterprises with Social Capital provides for the following:

- a) Employees are offered an initial discount of 30% of the appraised value plus 1% for each year of work in the enterprise. Each employee can buy shares at a discount rate up to DM 25.000. Payment can be made without down payment in five-year instalments and with a grace period of two years.
- b) At the beginning of the privatisation procedure, the company must automatically transfer 15% of the social capital (in form of shares or stocks) to the Pension Fund. These are non-voting, preference, participating stocks and they are expected to earn 2% fixed dividend.

The Law on Transformation of the Enterprises with Social Capital offers different privatisation methods according to the size of the enterprise¹ based on the number of employees:

1. Small enterprises (Article 41):
 - Employees buyout
 - Sale of a part of the enterprise (in a form of shares or stocks)
2. Medium-sized enterprises (Article 55):
 - Sale of the enterprise or a part of it
 - Buyout of the enterprise
 - Management Buy-Out
 - Issue of shares for additional investment
 - Debt/equity swap
3. Large enterprises (Article 71):
 - Large enterprises use the same methods as the medium-sized enterprises, with the only difference that the down payment for management buy-out is 10% and for the issue of shares for additional investment is 15%.

In addition, the following methods of privatisation can be applied to all enterprises, irrespective to their size:

- Leasing (Article 73-75)
- Sale of all assets of the enterprise (Article 76-79);
- Transformation of enterprises under the bankruptcy procedure (Article 80-86).

Privatised enterprises by sectors

¹ According to the Law on Transformation of Enterprises with Social Capital, two out of three conditions should be satisfied for classification of an enterprise in one of the following categories:

Small enterprise: Under 50 employees, total annual revenues under 8,000 average monthly salaries in the Republic of Macedonia and book value of operating assets up to 6,000 average monthly salaries.

Medium-sized enterprise: Between 50 and 250 employees, total annual revenues up to 40,000 average monthly salaries in the Republic of Macedonia and book value of operating assets up to 30,000 average monthly salaries.

Large enterprise: An enterprise exceeding these limits.

Majority of privatised enterprises belong to the manufacturing sector (486). They account for 30% of the total number of privatised enterprises and their share is 60% in the number of employees and 63% in the appraised value.

It is followed by the agriculture sector (418 enterprises), representing 25% of the total number of privatised enterprises, with a share of 8.4% in the number of employees and 8.4% in the appraised value. The privatisation in this sector began in 1996 and is still carried out.

343 privatised enterprises in the trade sector represent a share of 21.0% of the total number, 7.7% of the total number of employees and 10.9% of the total appraised value, respectively.

Though the construction sector accounts only for a small part in the total number of privatised enterprises (121 or a share of 7.3%), its share in the total number of employees is relatively high (14) as it is a labour intensive sector and encompasses largest enterprises in Macedonia.

Privatised enterprises by methods of privatisation

Most enterprises (394 enterprises, or around 24%) were privatised by the employees' buy-out method. They employed 17.193 people (7.7% of the total number) and their equity accounted for only 3.5% in the total equity. Though the employees' buy-out was the most frequent method used, only a small share of the equity has been privatised by this method. This is attributable to the fact that by the Law only small enterprises might use it.

The next most frequently implemented method according to the number of privatised enterprises was the management buy-out method (239 enterprises or 15% of the total). Compared to the former method, the management buy-out shares were the highest with respect to the employment and the equity value, employing 71.667 or around 32% of the total, and with the equity of 34% respectively.

A significant part of privatisation was carried out by the enterprise buy-out method. This method was implemented in 172 enterprises (11% of the total number of privatised enterprises) employing 50.134 people 23% of the total number and the total equity of the privatised enterprises.

The various privatisation models apply equally to all investors in the privatising enterprises – individuals and legal entities, both from the country and abroad. However, the fact that the Law allows managers and employees to propose the privatisation method, gave them, in a way a preferential treatment. Therefore, the most of the enterprises were privatised with a participation of the insiders. They have concluded agreements with the Privatisation Agency for purchasing stocks, and in case of default, the Law allowed the repeating of the whole procedure, with another privatisation model. This became an obstacle to the smooth running of the privatisation process, and at the same time was preserving the preferential status of the insiders.

That was the reason for the first major amendments of the Law made in April, 1999. They provide for the equity that has not been duly paid-in to be transferred back to the Privatisation Agency, in order to be sold through the Macedonian Stock Exchange, which had already been established in 1996. This, together with the amendments that authorized the Agency to sell both state and socially-owned capital, which allowed it to combine the capital for sale in more attractive stakes, was considered to reorient the process towards outsiders. In the same time was introduced the method of direct sale to strategic investor, such reducing the sales methods to the forms of: sale through stock exchange, direct sale to strategic investor or public invitations to bid.

However, the implementation of the direct sale method arose the question of transparency, and was abolished with the law amendments, that followed in April, 2000. In June 2000, a new by-law was enacted, which regulates the sale of the state-owned and socially-owned capital to be performed either through the stock exchange or by public tender. Currently new amendments and

addenda to the privatisation legislative are being prepared, in order to accelerate the process and facilitate its finalization.

Privatisation and restructuring

The loss-making enterprises have been a heavy burden to the budget during the whole period of transition to a free market economy and constant efforts have been made in addressing this issue. Although the complete restructuring of these enterprises before privatisation was considered as not acceptable, for being too costly in one and unpredictable in effect if made by the state in the other hand, it soon became obvious that a certain kind of restructuring was inevitable. Therefore, in 1994 25 loss-making enterprises were identified, and in the beginning of 1995 they were included in a Special Restructuring Program. The Program envisaged a number of activities, among which: to impose strict budget constraints to the loss-making enterprises and to isolate them from the banking system, to break down the large and clumsy enterprises, liquidate the non-viable ones and privatise the viable enterprises or parts of enterprises, separate and privatise the non-core units, provide financial and other support for displaced workers, etc. This process resulted in a number of 125 enterprises, part of which were liquidated, other privatised, and a few still waiting for a proper solution. In a large number of them the State became the main owner due to debt/equity conversions, which did not prove to be the final solution. Actually, many of these enterprises were part of the next group of loss-makers to be dealt with in 1999.

In year 2000, a new group of loss-making enterprises has been identified, owing to the firm resolution to finally solve this problem. Their number is 40, and according to the officially adopted governmental Action Plan for Restructuring of the Loss Making Enterprises, analyses will be made in order to assess their viability, which will help make decisions whether they will be liquidated, or privatised and restructured. Reputable independent consulting firms with strong international technical, marketing and financial expertise in the respective industries and in providing privatization and financial restructuring advice will be given the task of making the analyses and finding strategic investors. These enterprises will be sold by public tenders, in condition as they are. According to the schedule, five of them, taking a major part in the total loss, are to be privatised by the end of 2001 and their solving is part of the arrangements of the Macedonian Government and the international financial institutions.

The portfolio of the Agency's residual shares

The basic common principle in all methods of privatisation according to the Macedonian Law, is that the privatisation is considered successful if at least 51% of the capital of the enterprise is sold. Therefore, only in "perfect" conditions it may be expected that the enterprise will be fully privatised in one turn, or that the buyers will be willing to purchase all the available shares. Hence, a substantial part of the shares in the privatised enterprises have been transferred to the Agency as residual shares, in order to be sold afterwards.

The other source of generation of the residual shares are the unsuccessfully implemented privatisation models, i.e. shares that had not been paid by their buyers, and, therefore, (pursuant to the amendments to the Law made in 1999) had been returned to the Agency for further sale.

Regarding their sources of generation, it is understandable that the major part of these shares make "minority stakes", but there are enterprises in which the Agency holds "strategic interest" in a form of residual shares as well. Nevertheless, there still are blocks of residual shares with rather high growth potential in their value, regardless of their volume and the Agency is selling them through the Macedonian Stock Exchange.

The portfolio of the Agency's residual shares is worth almost 500 million USD, and is spread over 650 enterprises. The value of this portfolio fluctuates, on the one hand depending on the number of terminated contracts, and on the other on the sales volume. Its sale is one of the Agency's priorities for the coming period.

Conceptual and practical issues in the corporate governance in the Republic of Macedonia

The process of privatization in the Republic of Macedonia has commenced in 1993 and has been performed and completed in circumstances where the companies were not based on market-oriented legal principles and, consequently, their management did not match the principles of corporate governance. Namely, the Law on trading companies, in which the corporate governance was introduced, was enacted in 1996 and the companies had a time period left for registration according to the new Law by 1999. However, this process has not been completed yet and there are still companies that need to re-register as trading companies.

Another obstacle for effective corporate governance is the wide dispersion of shares in the privatised companies, which resulted in more than 250,000 individual shareholders in the Republic of Macedonia. This is closely related to the privatization methods applied, which, in a way, were more favourable to the existing employees in the companies, as insider buyers.

Furthermore, the frequent implementation of the MBO method of privatization contributed towards strengthening the role of the old management structures, i.e. the existing management teams, who acquired the most profitable companies in the Republic of Macedonia through MBO, in the beginning of the process.

In addition, the residual shares of the process of privatization and restructuring transferred to the Privatisation Agency make the state an owner and strengthen its interventional role in the governance of the trading companies. This has numerous side effects, as the state, in general, is not a good owner and manager. Therefore, the main priority of the Privatization Agency is sale of these shares. In the mean time, the Government and the Board of the Privatisation Agency appoint their representatives in the companies in order to participate in the management of the companies, according to the percentage of capital represented.

Foreign direct investment has been identified as a crucial component for supporting the transitional process of the Macedonian economy, and one of the objectives of privatisation – to increase the efficiency of the newly privatised enterprises, was to be achieved through attraction of foreign capital in privatisation.

One of the main advantages that are expected from foreign investors is introducing of new management skills and techniques in the newly acquired companies, both through the process of privatisation and post-privatisation. However, in most actual cases, the foreign investors rely on the old management teams or employee local people on very high managerial positions, which, in some cases, results in lower performance due to the lack of new experiences and management techniques.

After more than a decade of privatization in the Macedonian economy, 95% of the enterprises which entered the process have already been privatised. The small-scale privatization may be considered as completed, while the finalization of the large-scale privatization is currently being addressed by the implementation of the Action Plan for privatization and restructuring of the loss-makers, which mostly are large enterprises. However, 86% of the total revenues in the Macedonian economy have been produced in the private sector, i.e. 43,6% in the privatised and 42,4% in the originally private sector.

The main objective of the privatisation process, at this stage of its implementation, is sale of the remaining Agency's and state capital and increasing the efficiency of the already privatised enterprises, as well as full introduction of the principles of corporate governance.

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