CBS COPENHAGEN BUSINESS SCHOOL
HANDELSHØJSKOLEN

Corporate Governance Cycles during Transition

A Comparison of Russia and Slovenia

Mygind, Niels; Demina, Natalia; Gregoric, Aleksandra; Kapelyushnikov, Rostislav

Document Version
Final published version

Publication date:
2004

License
CC BY-NC-ND

Citation for published version (APA):
Mygind, N., Demina, N., Gregoric, A., & Kapelyushnikov, R. (2004). *Corporate Governance Cycles during Transition: A Comparison of Russia and Slovenia*. CEES, Copenhagen Business School. Working Paper / Center for East European Studies. Copenhagen Business School No. 54

Link to publication in CBS Research Portal

General rights
Copyright and moral rights for the publications made accessible in the public portal are retained by the authors and/or other copyright owners and it is a condition of accessing publications that users recognise and abide by the legal requirements associated with these rights.

Take down policy
If you believe that this document breaches copyright please contact us (research.lib@cbs.dk) providing details, and we will remove access to the work immediately and investigate your claim.

Download date: 17. Apr. 2024

CEES

Working Paper No. 54 **September 2004**

Corporate governance cycles during transition: a comparison of Russia and Slovenia

Niels Mygind,
Natalia Demina,
Aleksandra Gregoric,
Rostislav Kapelyushnikov

Center for East European Studies
Department of International Economics and Management
Copenhagen Business School
Sø006Edre Fasanvej 23, Porcelænshaven building 65,
Dk-2000 Frederiksberg, Denmark
Tel + 45 3815 2515 Fax + 45 3815 2500
© the authors, 2004 e-mail: nm.cees@cbs.dk

Corporate governance cycles during transition: a comparison of Russia and Slovenia[1]

by Niels Mygind*, Natalia Demina**, Aleksandra Gregoric*** and Rostislav Kapelyushnikov**

Abstract

Ownership is determined by firm specific factors and the environment. Firms change over their life-cycle. The governance cycle – here defined as changes in identity of the dominant owner and ownership concentration - is marked by key phases including start-up, growth, and possibly a restructuring or exit stage. During transition the cycle reflects: privatization often with a high proportion of employee ownership like in Russia and in Slovenia; strong pressures for restructuring and ownership changes; limited possibility for external finance because of embryonic development of the financial system. To provide simple hypothesis tests, we use Russian enterprise data for 1995-2003 and Slovenian data covering 1998-2003. In spite of differences in institutional development, concerning privatization and development of corporate governance institutions, we find that governance cycles are broadly similar in the two countries. Employee ownership is rapidly fading, but while change to manager and non-financial domestic outsider ownership is typical for Russia, manager ownership is not widespread in Slovenia. Instead change to financial outsiders in the form of Privatization Investment Funds is frequent. Foreign ownership, which is rare especially in Russia, is quite stable. The ownership diversification to employees and diversified external owners during privatization did not fit well to the low development of institutions. As expected we observe in both countries a subsequent concentration of ownership on managers, external domestic and foreign owners.

JEL-codes: G3, J5, P2, P3 - **Keywords:** corporate governance, life-cycle, privatization, ownership change, transition economies, Russia and Slovenia**.**

*Niels Mygind (corresponding author)
Center for East European Studies, Copenhagen Business School,
Howitzvej 60.2, 2000 Frederiksberg, Denmark,
nm.cees@cbs.dk.

**Natalia Demina and Rostislav Kapelyushnikov
REB-Monitoring (Russian Economic Barometer), Moscow, Russia.

*** Aleksandra Gregoric
Institute for Southeast Europe, Faculty of Economics,
University of Ljubljana, Slovenia.

I. Introduction

The identity of the owners and the concentration of ownership are key elements of the governance structure of enterprises. In the developed market economies these elements follow certain patterns of change over the life-cycle of the company, but at the same time with strong influence from the institutional framework in the specific country. In Eastern Europe these institutions have been changing very fast and in combination with the privatization process we have seen very fast changes in ownership and therefore a special pattern of governance cycles in these countries in transition. This has been studied for the three Baltic countries in Jones and Mygind, 2004. However, it would be interesting to contrast the change in ownership structures in two countries with quite different processes of privatization and large differences in the development of the new market institutions. Russia and Slovenia constitutes such a contrast. They are in fact on each side of what Berglof and Bolton (2002) call: "The great Divide" between countries, including Slovenia, which established a sound institutional foundation and those that did not, including Russia at that time.

In the following section we will first present the theoretical framework behind the governance cycle in developed market economies and the predictions about a special pattern of governance cycles in economies in transition. In section 3 we describe the differences in the transition process and developments in the institutional environment in Russia and Slovenia. Section 4 outlines the data, reviews previous work on ownership changes in transition economies, and present the results of the analysis on ownership dynamics and concentration for Russia and Slovenia in transition matrices and in econometric analyses. The final section includes conclusions and implications.

II. A special governance cycle during transition?

The theoretical starting point is that the choice of governance structure is determined by: enterprise characteristics: size, need of capital, information asymmetries, etc. as well as surrounding institutions, market conditions etc. The enterprise characteristics change over the life cycle of the firm. Ownership structures are expected to change because different stakeholder groups can contribute in different ways to the development of the company at different times in the firm's development. This means a change in governance structure over the life cycle - a specific governance cycle. However, the surroundings differ between countries, and countries in transition have specific features and specific paths of development. Therefore, we can identify a specific governance cycle during transition. Because of the rapid changing environment corporate governance patterns established at early stages of transition can be expected to change quite fast. But the speed of transition, the institutional framework, and the needs of capital and other inputs from different stakeholders

vary across countries and are expected to produce differences in the nature of the typical life cycle across countries - for example in the speed at which particular ownership changes will occur.

The ownership structure in market economies is determined by enterprise level factors and a combination of institutional, cultural and economic factors. To the extent that there is a possibility for ownership structures to adjust it can be assumed that, given the institutional setting, the type of ownership that gives the highest return to the owners will prevail. The optimal ownership structure can be explained from several perspectives including agency-, property rights-, transaction cost- and resource dependence approaches (Jensen and Meckling 1976, Williamson 1985, Pfeffer and Salancik, 1978). Based on this eclectic theoretical approach we can identify explanatory elements behind the ownership dynamics. We will start with the most important elements at the company level. The main conclusions are summarized in table 1:

The size and capital demands of the company may be very high even in relation to a wealthy owner. Therefore, growth is associated with a more diversified ownership structure, a fall in owner concentration (Jensen and Meckling 1976, Putterman 1993, Shleifer and Vishny 1997). Especially for wealth-constrained insiders, ownership of a high capital demanding company means a high concentration of risk. Insiders put all their eggs, jobs and capital, into one basket (Meade, 1972). There is a trade off between single proprietorship by the manager with no governance problem between manager and owners and the possibility of diversification and higher capital supply by external more diversified investors with less control with management (Fama and Jensen 1985). The *specificity of the different inputs* constitutes another microeconomic factor. If the fixed assets can be used in many alternative activities it is much easier to finance them by loans instead of by direct risk capital. In these cases banks will play a strong role (Williamson 1985). The larger the need for direct risk capital, the less likelihood that a single provider of capital will emerge to fulfill these needs and more diversified ownership can be expected (Fama and Jensen 1985, Putterman 1993). The existence of specific capital means a higher dependence on other links in the value chain. The hold-up problem may lead to a stronger connection to core suppliers or customers with quite concentrated strategic ownership of the company (Grossman and Hart, 1986). A special relation concerns the inputs of human capital. If it is highly specific, the risk is high for the employees. To limit this risk, the employees have an incentive to take direct control and ownership of the enterprise. A large size of the company is often used as an explanation for no employee ownership because of the need for a central monitor to avoid shirking (Alchian and Demsetz, 1972) and the larger the group the smaller is each employee's share in the ownership rights and the easier it is for a single employee to free-ride. Hansmann (1996) argues that a larger group of employees combined with higher heterogeneity means higher costs for collective decision making.

Transaction costs for outside investors are also closely connected to the specificity of the assets of the company, information asymmetries, and of the institutional framework (see below.) New and yet unproven business ideas with complex human capital make it very difficult and costly for external investors, including both passive suppliers of capital like banks and active external owners to get reliable information about the company and to monitor the performance of managers.

The *economic performance* of the firm is another potential influence on the ownership type with, for example, an economic crisis often implying a shift in ownership. However, this ownership change may take several directions: An outside raider or a strategic investor related to the value chain may take over the company and perform the necessary restructuring. A managerial buy-out may be the result if, based on insider information, the managers estimate the value of the firm to be higher than estimates of external investors (Wright et al., 2001). If the value of the company is high insiders may have a strong temptation to sell their shares (Miyazaki, 1984), while an economic crisis may induce a defensive take-over by the employees to introduce more flexible wages and to save their jobs and their specific human capital. (Ben-Ner and Yun 1996). In this case low wage would be connected to employee ownership. On the other hand does low wage signal low educational level, low human capital, which point in the opposite direction of employee ownership.

Based on these influences on and determinants of ownership some trends in the development of a typical ownership structure for a firm can be noted in relation to the *typical life-cycle of the firm*, see table 2. Over its life-cycle, a company will change technology, markets and relations to the different stakeholders. These shifts influence the role of different stakeholders including the identity of the dominant owners. Most companies *start-up* as small entities with few employees, low capital, and low knowledge about the economic potential of the firm. A high proportion fail in the early stage; but most of the succeeding companies go into a stage of *growth*, which demands higher inputs of capital, knowledge, networks and employees. The need for extra capital may eventually lead to some diversification of ownership. However, a specific shock in the environment may also lead the company into a stage of *crisis*, which makes some kind of new inputs necessary. This will often be a new input of capital, which can be facilitated through an ownership change. During these stages the change in ownership can be related to the different determinants of the ownership structure. Changing conditions both from within and from outside the company generate changes in ownership and hence changes in the development of the governance cycle, see table 2.

The *classic entrepreneurial company starts up* as a small entity with relatively low capital inputs, which can be covered by the entrepreneur and by debt based on personal loans e.g. with collateral in the family-house. Information about the core-competence, the yet unproven business idea,

is difficult to transmit to an external investor. The asymmetry in information between the insider and external investor is very large and the transaction costs of writing and controlling a contract are very high. High uncertainty and lack of reliable information about the prospects of the new business and its market potential enhance the problem of asymmetric information and risks to the external investor. Therefore, most new companies are started by single proprietors, and owned by the entrepreneur sometimes with participation of close relatives and friends. The capital needed can in most cases be covered by the founders and by loans with collateral in the entrepreneurs' personal assets.

Many small entrepreneurial companies close down during the initial stages, but eventually, those that survive enter an *initial growth stage*. The company needs high capital investments, knowledge and networks to facilitate high growth to benefit from economies of scale. At the same time, the firm starts to create some reputation and market-experience, which can improve the information and give guarantees for potential external investors. Suppliers of capital, banks or other financial institutions will in most cases not claim direct control, but often they require to closely monitor the collateral behind the loan. In some cases the owner may get new capital by issuing extra shares to new owners found within a rather closed circle of stakeholders, typically top-employees of the company, investors from the local society or close business partners.

At a later more *mature growth stage*, when the company has developed its potential, it may attract a strategic investor with an interest in including the company in its value-chain. Another possibility for attracting capital at a developed stage is to go public. The development of going public is also often part of a process of diversification of ownership. Therefore, the process of growth is often combined with a lower degree of concentration.

Sooner or later many companies run into a *stage of crisis*. Diverse internal and external factors, including changes in technology and/or markets or the institutional setting, force the company to adjust to the new conditions. The company faces strong pressures to undertake restructuring. New external capital and expertise are needed, and banks, venture capital and strategic investors may play an important role. As an alternative to closure insiders may make a defensive takeover to protect their jobs and their specific human capital. The crisis may also result in an exit of the company and liquidation of the assets, which is then taken over by new investors for other activities.

The determinants behind the ownership structure and the governance cycle are not only found within the company. The *economic institutional and cultural environment* is important and variations across countries explain differences in governance systems and ownership dynamics.

Macroeconomic cycles have an impact on the performance of companies and therefore on the governance structure. MBOs are more frequent in business cycle troughs because of low pricing

of assets during dips. This can be seen in relation to tendencies of going private (Wright et al, 2001) while boom periods on the stock market means that IPOs and going public give companies a cheaper possibility for raising external finance. Defensive employee takeovers can be assumed to be more frequent in recessions because of higher threats of closure and lower alternative employment possibilities (Ben-Ner 1988).

The *institutional setting* in relation to legislation may present specific barriers or provide advantages to different forms of ownership. The degree of protection of minority owners through legislation and the liquidity and development of the stock markets have impact on the diversification of ownership. Thus, *concentrated ownership* is widespread in countries with a lower degree of minority owner protection and less developed capital markets, while diversified ownership is more frequent in countries such as US and UK with highly developed capital markets and a high degree of protection of minority owners (La Porta et al 1999, Becht et al 2002). Also, the development of the banking sector enhances the possibility of financing growth through bank-loans, and for the role of the banks as creditors and potential owners in the governance structure of the firm.

Informal social relations and *culture*, defined as the historical traditions, cultural values, norms and preferences of the stakeholders, can also explain important differences in the governance structure between countries. Thus, the optimal ownership structure in Russia is expected to be different from the optimal structure in the Slovenia because stakeholders have different objectives and different relations to each other, and the historical experience of participation, local initiative versus paternalistic leadership styles and centralization are part of the path-dependency of the dynamics on both the macro and the enterprise level.

The *transitional economies* are characterized by a specific economical and institutional development and therefore we expect that a specific governance cycle exists in firms in those countries. The dynamics of enterprise governance and ownership are quite distinct because enterprises go through both a transition in ownership structure, a transition in relation to the changing institutions in the environment, and a transition of the market in relation to prices, costs, and competitive structure with a strong pressure for restructuring of products and production methods. Most enterprises in transition economies start with rapidly changing the structure of governance combined with a strong pressure for restructuring production simply to be able to survive. The specific elements in early transition that influence the governance cycle are shown in Table 3.

To understand the governance cycles appearing in transitional economies there are three special conditions that must be taken into account. First of these factors is *the privatization process*, which in the early years of transition created specific conditions for the initial development of pri-

vate ownership. The different methods favored different types of owners. In some countries employees had a strong political position resulting in a very high frequency of employee ownership. Often managers had a strong position in relation to the political system. On the other hand, voucher privatization supported a high degree of domestic external ownership, while direct sale without restrictions for foreign capital gave foreign investors the lead in the change to concentrated external ownership (Mygind 2001). Privatization is a state governed process where the specific methods create a specific ownership structure, which would not have developed in a more market based system for ownership adjustments. The path-dependency may create a learning process and institutional development, which may lead to specific paths for subsequent developments in the governance structure. Such path dependencies can to a high degree be used for explaining persistent differences in the governance structure in the West (Roe 1990). On the other hand, it is expected that there will be post-privatization adjustments bringing the ownership structure back to a "normal" equilibrium.

A second condition occurs because, from the start of transition, nearly all state owned enterprises are confronted with a strong *pressure for restructuring* of production, production methods, organizational structure and markets. They are in a situation of crisis with an acute need of capital, new skills, and new networks. In the developed market economies this often leads to a change in ownership bringing new investors with the necessary resources for restructuring. In some cases, privatization delivers the best-fit investor for restructuring. In other cases post privatization dynamics include a takeover to facilitate such restructuring.

The third and most important feature of transition delays this ownership adjustment. This concerns the long lasting process of building up *institutions* for a well-functioning market economy including institutions required to facilitate the adjustment of enterprise governance. In the early transition, lack of developed institutions favors special types of ownership. Insiders have an advantage in relation to outside owners because the institutions supporting outside ownership such as credible auditing procedures and transparent stock markets are not developed (Mygind 2001).

Based on these three special conditions hypotheses about the specific governance cycle in transition can be developed (table 4). However, since some conditions give tendencies whose directions are ambiguous, the final conclusions must be based on empirical analysis.

The first set of hypotheses concerns the scope and resilience of employee ownership. Privatization in many countries, including Russia and Slovenia, led to a high degree of employee ownership. However, employees' lack of governance skills, their lack of capital and the risk-concentration may lead to a tendency to rapid sale to other investors. High number of employees, high capital intensity, and low wage could strengthen this tendency. But the movement away from employee ownership could be delayed by various factors: The employees may in the past or in the transition pro-

cesses have acquired governance skills; there may be strong defensive arguments for keeping ownership to protect employment (Blanchard and Aghion 1996); or the specific company may have a high degree of specific human capital, which would be threatened by a sale to another investor.

The lack of development of the institutional environment weakens the role of external investors. The lack of transparency and high risk especially in the early stages of transition combined with the lack of markets for company shares means that, in general, managers have a strong advantage compared to external investors (Kalmi 2002). Therefore, especially during the early stages of transition, it can be expected that *managers take over* the shares that employees want to sell.

Voucher-privatization provides for a high degree of public offering of shares to diversified external owners. This often means overly diversified ownership in relation to the volatility of the markets, the low quality of information to external owners, and the lack of development of the institutional framework. Most of these initial small external shareholders are under strong wealth constraints. Therefore, during the early years these companies are in a process of *concentration of ownership* in the hands of especially *managers* and small groups of external investors who have accumulated wealth in the early transition.

When the institutional framework becomes more advanced during the process of transition it can be expected that external investors get a stronger position, and there will be shifts from *insider to outsider ownership*. This tendency is strengthened if the company, either because of high growth or because of pressure for restructuring, has a strong need for extra capital.

The stock markets in transitional countries are weak, with few companies listed, low capitalization, low turnover and few IPOs. Therefore, it is too early to observe the tendency found in the west for more mature firms to diversify ownership to small external investors. Instead we expect a tendency in direction of higher concentration also when we look at continued external ownership.

Foreign ownership is established both as new green-field entities, as takeovers directly in the privatization process, or as takeovers in the post-privatization adjustment process. In these cases we expect a rather stable ownership structure because these enterprises have reached their final stage of development in the ownership cycle at least within the relatively short time-horizon of our analysis.

The specific governance cycle during transition can be understood as a sequence where three types of governance problems are in focus: The *stakeholder problem* related to the representation of the interests of different groups of stakeholders; the manager-owner problem, which is the usual agency problems between the manager as agent for the owner as principal; and finally the problem between a dominant core-owner and the minority owners. In transitional countries the

starting point can be understood as a stakeholder system with the state representing the social interest. Privatization models where ownership is transferred to the employees address one of the most important stakeholder problems – the relations to the firms' employees.

With the change to manager ownership the focus shifts to solve the *manager-owner problem*. The clear-cut solution to this problem is simply to unite the position as manager and owner. When there are too weak possibilities in the governance system for the owners to control the managers, as is often the case in early transition, insider- and especially manager ownership may be the solution on the owner-manager governance problem.

With the development of governance institutions outsider ownership becomes feasible, but it is necessary to have a strong concentrated owner to minimize the owner-manager problem. As a trade-off the *majority-minority owner problem* comes into focus because the governance institutions are still not so developed that minority owners are protected. With the development of institutions securing disclosure and transparency, and rules protecting minority shareholder interests against dilution of shares, and other forms of appropriation of rights by majority shareholder it becomes possible to limit this governance problem to such an extent that a governance system based on diversified small shareholders may develop.

In this way the focus changes from the stakeholder problem over the manager-owner problem to the minority problem as the economy passes through different institutional stages.

Also in advanced economies there can be a trade-off between the different problems so the solution of the manager-owner problem increases the majority-minority problem, or the solution of the stakeholder problem means that the manager extends his power as "representative of the different stakeholders" on the expense of shareholders. In the most advanced corporate governance systems all three problems are targeted simultaneously. The stakeholder problem is addressed e.g. in the form of Corporate Social Responsibility and/or employee representation in the company board.

The analysis has emphasized some general tendencies for the governance cycle in transitional countries in comparison to Western countries. However, the existence of cross national differences, especially concerning *institutional differences* related to the speed and form of transition, may make both the starting points and the speed of change between different phases of the cycle different across the transitional countries. The dominant form of privatization determine to what degree the starting point of the cycle for privatized firms will be employee ownership, management ownership or perhaps other groups with strong connections to the state have been favored (Mygind 2001). The specific rules for privatization may include restrictions for later ownership changes. Some shares may not be transferable for a certain period and some forms of institutional ownership

by pension- and other investment-funds may set a path for low flexibility in the ownership structure.

In addition to the specific privatization methods the institutional development and the general economic and political stability determine the level of foreign investment (Bevan et. al. 2004). The speed of ownership change also depends on the transition of institutions. The development of the banking sector and the possibility of debt financing are especially important. The dynamics also depend on the development of the capital-market and the possibility of expanding the equity both for listed companies and for trading shares of non-listed companies. The protection of the rights of the shareholders, especially minority owners, is important for diversification versus concentration of ownership in the post-privatization period.

It is not only the specific privatization methods and the development of institutions that make ownership dynamics in one country different from another. The *economic development* and the degree and duration of the initial fall in production and possible later reversals like the 1998 crisis in Russia can influence the governance cycle in several ways. The steep fall in income of the population may put a strong pressure on liquidity-strained employee owners and low-income owners of vouchers or shares. They will sell and concentration will increase. On the other hand, high risk of unemployment may increase the defensive motive of employees to keep their shares and sustain control over their jobs to secure their specific human capital.

Finally, *cultural factors* and historical experience of management style, employees participation in ownership and control over the enterprises, and attitudes of risk-taking and involvement may play a role both for the sustainability of employee ownership and for the development of a broader shareholder-culture with diversified ownership.

In the next section we look at specific developments in Russia and Slovenia and develop hypotheses for how this can be expected to affect the corporate governance cycles, especially the starting points and the speed and direction of ownership change in these two countries.

III. Privatization and Governance Institutions in Russia and Slovenia

Some economic indicators for Russia and Slovenia are summarized in table 5 and the results of privatization in the two countries are summarized in table 6.

The background for privatization in Russia was several generations of centralized planning with limited scope for each enterprise. The management style was paternalistic with a low degree of active participation of the employees in the governance of the companies. There were several waves of reforms to increase the efficiency of the system, but these reforms did not succeed in fundamental changing the system before Gorbatjov started to make market-oriented reforms. His Perestrojka

policy included in the end of the 1980es the possibility to start small individual private firms, the possibility for starting new cooperatives with formal ownership by the employees, and possibilities for the collective of workers to lease the enterprise. The incidence of the lease-buyout scheme was particularly large in retail trade, consumer services, and in light industry. By February 1992, 9451 state enterprises accounting for 8 % of total employment were leased by their workers and managers, (Blasi et al 1997). The new cooperatives, individual firms and the leasing system were privatization processes starting up already in the time of the former Soviet Union. With the democratization process and the increasing power of the reform-wing in the different republics more wide-scale privatization plans were formulated e.g. in the Baltic countries and in the republic of Russia.

However, privatization in Russia did not take off before after the dissolution of the Soviet Union in 1991. Privatization of small entities was done quite fast, mostly during 1992 and 1993. The specific method mainly based on auctions and tenders varied between regions. Mass privatization directed toward medium and large enterprises started in the fall 1992. Vouchers distributed to the whole population could be used for buying shares in the enterprises. The companies could chose between different models: Option 1: 25 % non-voting shares were offered to employees for free, with the option to buy a further 10 % of ordinary shares at a 30 % discount of the book value of January 1992 – already much below the market value by the time of privatization. Managers were offered to purchase 5 % of ordinary shares at nominal price. Option 2: Employees could for cash or vouchers buy 51 % of ordinary shares at 1.7 times the 1992 book value, again much lower than the market value. For implementation at least 2/3 of the employee should support this model. Option 3: A managing group could buy 30 % of voting shares. Further 20 % could be purchased by insiders at 30 % discount., given the rapid inflation in Russia at that time, the prices to pay in all three options were so low, that the mass privatization really was a give-away (Hare and Muravyev, 2002).

The privatization was very rapid. Of the 24,000 medium and large enterprises, most had been corporatized and over 15,000 privatized by the end of 1994. Over 70 % of the firms offered for privatization chose option 2. Option 1 was chosen by 21 % giving insiders control of most enterprises. In combination with the paternalistic ownership style it meant that managers consolidated their positions. However, the incidence of employee ownership was much smaller in well-performing, capital-intensive, large enterprises. Here insiders were unable to accumulate enough funds to buy 51 % of shares under option 2, and most of these firms followed option 1 with a weaker position for insiders (Hare and Muravyev, 2002).

Foreign involvement was negligible. Investment funds collected some of the shares, owned by small external shareholders, but in general these funds played a minor role.

Many of the large jewels of Russian industry like the metal company: Norilsk Nickel and the oil-companies: Sibneft, Sidanco and some shares in Lukoil were privatized through the "loans for shares" or "mortgage" privatization in 1995. This system was direct, non-competitive sales of blocks of shares at low prices to the leading Financial-Industrial Groups, which at the same time administered the process (IET, 1997). In the following years case-by-case privatizations of a few large enterprises and leftover state holdings were performed with increasing speed and transparency.

In Russia there have been severe problems for the financial sector and its functions of channeling capital to the enterprises and to be part of the governance system by disciplining the efficient use of these capital inputs. Before August 1998 the banks made more money from lending to the government or through their foreign transactions than from lending to business. Interest rates were extremely high and firms did not invest at all these years or they based investment on internally created resources. Since the 1998 financial crisis, the banking sector remains underdeveloped and consists of over 1000 banks, most of which are small and undercapitalized except for the large and completely dominating state-controlled Sberbank.

Similarly to the banking sector, the Russian stock market has never played an important role in providing enterprises with financial resources. The number of listed equities is about 250 of which only around 60 were regularly traded in 2003. Out of these 57 had American Depository Receipts quotation in New York (Buck 2003). Most equities are illiquid. While the market capitalization of several individual companies amounts to billions of dollars and capitalization of the Russian stock market is in the start of 2004 approaching 200 billion US$. The turnover on the main Moscow stock exchange is about 100-120 million USD per week.

When looking at the governance institutions in transitional countries it is important not to focus on the legal framework, which may be quite advanced, but to look at the actual implementation of shareholders rights, protection of minority owners, and the quality of information and disclosure. Therefore, we will not give a detailed description of the complex of governance legislation and codes, but indicate the level and the main tendencies in the development.

Because of lack of legislation, regulation and enforcement the early 1990es were in Russia characterized by a very strong position of management often allied with a few strong external investors. In these days most of the powerful financial industrial groups such as Menater, Onexim, Inkombank and Alfa were created. Managers and their allies appropriated rights from employees and diversified external owners, and through widespread tunneling large fortunes were accumulated and concentrated in the hands of relatively few people. In the mid 1990es the legislation on compa-

nies and securities market developed, but lack of trained officials and widespread corruption meant that enforcement was quite weak (Puffer and McCarthy 2003).

The legislation and enforcement in relation to disclosure, transparency and protection of minority owners were strengthened somewhat in the new millennium with stronger state policies and with the start of the process for Russian accession to WTO. The Russian Federal Commission for the Securities Markets unveiled in 2002 a Code of Corporate Conduct, which is in line with the OECD Principles for good corporate governance. However, the code is voluntary, and it remains to be seen if the Commission will strengthen it activities as a watchdog. In the past investigations have been very rare. The new millennium also saw an increasing number of large companies improving their corporate governance systems with higher standard of disclosure, accountability, and protection of minority owners. In general, the development since 2001 has improved both regulation and enforcement. From a regime characterized by widespread abuses, the Russian companies have in the new millennium started to develop into a stage where corporate governance issues are taken seriously. (Puffer and McCarthy 2003). Cases where foreign investors take active part in governance and actually take over controlling positions in large Russia enterprises are still very rare with BPs' takeover of a strong position in the oil company Sidanco as an important exception.

Bankruptcy is part of the governance mechanism for adjusting ownership. Therefore, bankruptcy legislation and enforcement is important for the development of the governance cycle. The Russian development in this field has followed the general pattern of other Russian governance institutions with very weak legislation and enforcement in the 1990es, but then followed by some improvements in the new millennium. The number of bankruptcies was extremely low during most of the 1990es. However, in January 1998 the amended Law on bankruptcies was enacted. This provoked a sharp jump in the number of bankruptcies. The number of bankruptcy petitions, which were accepted by courts and were in the process of implementation were only 4.200 at the end 1997, but increased to 10.200 in 1998, 15.200 in 1999 and 27.000 at the end of 2000. Actually, bankruptcies were often used as a cheap method of hostile takeovers or asset stripping. In order to optimize tax payments many companies created special "profit centers" that accumulated revenues while enterprises per se (production entities) were transformed into "liabilities centers" (via transfer pricing etc). So a raider who succeeded in buying enterprise debts might submit a petition on its bankruptcy and easily become its new owner. The paradox is that the best performing enterprises became victims of these raiders. In 2003 the Law on bankruptcy was amended to stop this wave of false bankruptcies.

The economic development can also influence the identity of ownership and thus the dynamics over the governance cycle. From the economic indicators in table 5 it is clear that Russia had a much steeper fall in production than it was the case for Slovenia. Russian production did not start to grow before 1997, and then followed the financial crisis, which in 1998 had a negative effect on production. However, in the following years production increased rapidly because of favorable oil-prices and strong import-substitution after the steep devaluation of the Ruble in the months following the crisis. Unemployment did not increase so much as the fall in production up to 1997 should indicate, because most Russian enterprises tended to keep the employees although they produced below their capacity-level. Instead wages were kept on a very low level. Wages measured in USD fell steeply following the crisis in 1998, but then recovered in the following growth period. Table 5 also indicates the extremely low FDI going into Russia.

Slovenia's economic development has been quite different from the situation in Russia. The initial fall in production was quite fast turned around to steady growth. The relatively high level of productivity and competitiveness, which characterized the Slovenian self-management economy since the 1960es, meant that the Slovenian income level during the whole transition period has been the highest in Central and Eastern Europe. This is the background for the relatively high wage level measured in USD. It was 8-15 times higher than the Russian level. Although Slovenia as described below did not give many opportunities to foreigners in the privatization process FDI gradually increased so the accumulated amount per capita over the period is on level with the most advanced transitional countries and dwarf the FDI going into Russia.

As the most developed part of former Yugoslavian self-management system Slovenia had a quite strong tradition for active employee participation in the governance of enterprises, which were socially owned in the sense that the employees had the formal right to control and they had the residual cash flow rights. However, they could not sell shares of the company and get a capital gain if the firm had increased its market value. Formally, the governance of the enterprises was in the hands of the employees since it was the workers' councils that selected the management team. In practice however, governance of the enterprises was a bargaining process between four institutions: the self-management institutions of the employees, operative management, socio-political organizations and socio-political communities.

With the decrease of political influence on business at the end of 1980es, the power of managers in decision making increased. The managers were leading the privatization process, which in most cases was based on *internal privatization* - one of several ways of ownership transformation provided by the Law on Ownership Transformation, passed by the Slovenian Parliament in Novem-

ber 1992. After the compulsory free transfer of shares to different State-controlled Funds (10 % to the Restitution Fund, 10 % to the Capital Fund (for reserve and pension purposes) and 20 % to the Development Fund (for further sale to the Privatization Investment Funds for cash or in exchange for vouchers) and after the distribution of 20 % of the shares to insiders in exchange for their vouchers, companies could freely decide on the allocation of the remaining 40 %. They could either privatize internally and sell them to insiders according to a special scheme or privatize externally and offer them to the public through a public offering of shares, public tender or public auction. The first scheme of internal privatization required the participation of at least one third of the employees. According to the scheme, the shares had first to be transferred to the Development Fund with the first 25 % acquired by the insiders immediately, while the remaining 75 % within the next four years (25 % per year over the whole period). The shares were sold under a 50 % discount and were transferable only among the participants of the internal buyout within a period of 2 years. Alternatively, firms could choose to be liquidated and sell off their assets. In this case, the social capital and liabilities of the firm were transferred to the Slovenian Development Fund, the firm was cancelled from the Company Register, while the funds gathered by the sale of assets were used for the repayment of liabilities and the implementation of an active employment policy.

The Privatization Law was a compromise between three main approaches, all of which stressed privatization, but differed in the role of the state, managers, workers and foreign capital: i) the decentralized model that stressed worker-management buyouts of existing enterprises (proposed by Mencinger in 1989; ii) the centralized model, which was based on the re-nationalization and subsequent privatization of all enterprises with domestic as well as foreign capital (advocated by supporters of the ideas of Jeffrey Sachs) and iii) the semi-decentralized model based on mixed ownership taking into account the heterogeneity of the enterprises (advocated by Ribnikar and Prasnikar in 1991, see Prasnikar, Gregoric and Pahor, 2004). The adopted privatization method involved a combination of cash and voucher privatization; with regard to the latter, about 2 million vouchers of a total value of DM 9.4 billion (representing about 40 % of the total estimated book value of social capital) were distributed to citizens of the Republic of Slovenia. The vouchers were non-transferable and could be used only for acquiring shares in the internal distribution, the internal buyout, public offering of shares, and in exchange for shares of the Privatization Investment Funds (PIFs).

The model favored employee ownership, but at the same time it addressed the problem of risk concentration in employee owned enterprises. In this sense the 10 % to the pension fund was the base for the fully risk-diversified pension-scheme. The Privatization Investment Funds (PIFs), where Slovenian could place part of their vouchers, reflected personal investments also with a high

degree of diversification, while the shares received in the internal distribution and bought in the internal privatization implied a concentration of risk at the enterprise level, but these shares were at the same time the basis for the continuation of employees control of the company (Mygind 1991).

The companies could chose one or a combination of the proposed privatization methods and submit their approvals to the Agency for Restructuring and Privatization in charge of the ownership transformation in Slovenia. The Privatization Agency gave its first approval on 29 July 1993 and its last approval at the end of October 1998. During these six years, more than 1300 companies (96.2 %) successfully completed the ownership transformation and were entered into the Court Register. The 55 companies that did not end the privatization program were either transferred to the Development Fund or liquidated. Among privatized firms, more than 90 % chose the internal distribution and internal buyout as the main privatization method. Internal owners ended up holding about 40 % of the social capital subject to privatization. The social capital to be privatized represented only 68 % of the existing social capital, while most of the remaining 32 % remained under the ownership of the State (Privatization Agency, 1999). PIFs got about 25 %, state funds got 22 %, while the remaining 13 % were publicly sold in exchange for vouchers. Internal ownership prevailed as dominant mostly in smaller, labor-intensive firms; workers and management obtained more than 60 % stake in 319 firms (24.4 % of all firms), but only 8.1 % of total capital. On the other hand, their share did not exceed 10 % in 82 companies (6.3%) accounting for nearly 30 % of total capital (Privatization Agency report 1999).

The model based on state funds, Privatization Investment Funds and employee shares with restricted transferability for a certain period implied some limitations on trade of shares and adjustment of ownership structure. Simoneti et.al. 2001 point to the problems connected to this delay in the transferability of large volumes of shares. They also criticize the distribution of ownership on different agents with conflicting interests, often implying a battle between the outside funds on one side and the insiders on the other.

In general the Slovenian legislation related to *corporate governance* is on level with the standard in most EU-countries, and the implementation is also about to reach this level. Some special features are however worth emphasizing:

An empirical analysis conducted in 2001 of 35 shareholders' general meetings, shows that 70 % of the votes were cast. This relatively high percentage is mainly explained by a quite high concentration of ownership. The system of small shareholders representation and proxy voting are not so developed in Slovenia, except for cases where managers have organized proxy voting of employee shares. Slovenia has like in Russia a system of 25 % blocking shares for important decisions

at the general meeting. Other rules give 5-10 % of the shareholders right to challenge decisions threatening the value of their shares e.g. by calling extraordinary general meetings (Gregoric 2003).

Concerning equal rights of shareholders the Companies Act imposes the one-share-one-vote rule, however this equality can be broken by issuing preference shares with priority on dividends, but without voting rights (Gregoric 2003). Caps on voting rights have been used to limit the control of large shareholders and have functioned as anti-takeover devices in some large Slovenian companies. However, voting caps have been prohibited for listed firms with the amendment of the Companies Act in 2001. There were a series of battles for ownership in large Slovenian companies in the latest years, and there are recent attempts demanding higher transparency in relation to takeovers.

The Privatization Investment Funds, which were originally capitalized through vouchers, took over quite large parts of the enterprises. They were managed by management companies, which through proxies and later through direct ownership de facto controlled the PIFs. This happened often parallel to a process where the PIFs were transformed to Public Limited Companies (PLCs), without the PIFs' 5 %-limit for the single largest shareholders (Gregoric 2003).

The Slovenian Co-determination Law from 1993 (amended 2001) gives the employees some rights to control in questions concerning human resource management. They have the right to form workers' councils and to be represented in the supervisory board by 1/3 of the seats. On top of this there 68% of the workers are members of the main union.

In 1994 Slovenia introduced new bankruptcy legislation. The implementation was reasonable, but according to the EU-Commission (2002) procedures were rather slow. However, in 2000 and 2001 the number of bankruptcy cases rose sharply because of the introduction of more appropriate legislation, higher efficiency in the judicial system and the state becoming more actively involved in tax recovery procedures and as petitioner in bankruptcy procedures.

There was already from the self-management period a tradition for commercial banks. They were, however, strongly dominated by the largest companies, and loans were based more on rationing and soft budget constraints than on sound principles like in developed market economies. However, the transition to a fully market oriented system started with the establishment of a bank-restructuring agency in 1991. In the process of rehabilitation the banks came under state governance, bad loans were cleaned and privatization process initiated. The rehabilitation process was concluded by 1997. Bad loans dropped from a level of 22 % in 1994 to 10 % of loans in 2002 (EBRD 2003). The privatization of banks was relatively slow with one of the largest banks privatized as late as 2002 to a Belgium banking group. After this most of the banking sector was privatized and 16 % of the total assets in Slovenian banks were in banks with majority foreign ownership. The banking function of lending to the private sector was already in 1991 on a level of 35 % of

GDP. Then it fell somewhat during the period of cleaning bad debt and since 1993 is has been increasing steadily to reach a level of 41 % of GDP in 2002. Although this is lower than the EU average, Slovenia is on a quite high level measured by East European standards (Cufer et. al 2002).

The stock exchange in Ljubljana opened already in 1990, but capitalization and trading did not take off before the first privatized firms were listed in 1996. Then the capitalization of shares grew quite fast to reach 23% of GDP in 2002, and total capitalization as share of GDP was in 2001 the highest in Eastern Europe (Caviglia et al 2002). However, like in other transitional countries the trade is still rather thin and concentrated around relatively few shares.

Before we go to the empirical analysis we will sum up the *hypotheses* for how the cultural, economic and first of all the institutional development can be expected to influence the governance cycle in the two countries. What specificities of the cycle can be expected? What can we say about the speed of adjustment at different stages? How advanced do we expect the cycle to be?

In both countries the privatization model gives a starting point with a high degree of employee ownership. The question is if the next step for these enterprises will be management ownership as predicted in the theoretical section and how fast this process will happen?

In Russia the managers are in a strong position because of: the paternalistic leadership style and low experience and tough liquidity constraints for the employees. The low development of governance institutions with low transparency gives high possibilities for transactions moving the assets into the hands of the manager. Although the financial system is not advanced and it is difficult for managers to get loans for buy-outs the price may be so low, that this is not an important barrier. Therefore, we expect the change to manager-ownership to be quite fast and widespread in Russia.

In Slovenia the financial system developed quite fast, but at the same time the governance institutions were also highly developed making it difficult for the managers to make covert deals. The fact, that the employees are used to participate in ownership is probably the most important barrier for manager takeovers from employees in Slovenia. We assume that employees are not easy to manipulate, and they have an understanding for the value of their shares. Because of the high competitiveness of most Slovenian firms the actual market value of the shares may be relatively high. Even if managers could get some loans in the banks it would often not be enough to finance a manager takeover. The prices for the employee shares could not be substantially reduced because the Slovenian wage-level is rather high and the employees are not desperate to sell their shares at rock bottom prices. Furthermore, the Slovenian privatization model included regulations that made employees shares less transferable for a certain period. Thus, instead of a takeover it may be a more realistic strategy for managers to make an alliance with the employees e.g. in the form of Workers'

Associations (AWAs). Such a strategy would make manager takeovers less frequent and employee-ownership more stable in Slovenia than predicted in the theoretical section.

The next step in the governance cycle to external, but concentrated owners, demands a more sophisticated development of the governance institutions to avoid the manager-owner governance problem. Such development is expected to be slow in Russia. The exception will be large companies where the manager needs an alliance with strong external groups to get a dominating position.

The different state funds and the developing Privatization Investment Funds in the Slovenian privatization model, give external owners a quite strong position already from the time of privatization. Slovenia's faster institutional development, the advanced financial sector and early tough bankruptcy legislation are expected to encourage a relatively fast adjustment to external ownership.

Finally, a fast transition process and development of the institutional system improve the business climate and attract foreign investors, and therefore facilitate a faster change in the direction of foreign ownership. We do not expect to see this development for the Russian enterprises in the period under observation. Slovenia offers foreign investors better conditions, but a move to more foreign ownership may to some degree be blocked by the different Slovenian funds.

We expect a strong tendency in the direction of stronger concentration in Russia to limit the owner-manager problem in a relatively weak institutional setting. These tendencies may not be so strong in Slovenia. The question is, if the Slovenian institutional setting has reached such a level that the majority-minority governance problem has been so much reduced that it opens up for an increased weight on diversified share-ownership. The developed system of both state governed pension funds and Privatization Investment Funds may work as alternative channels for small diversified investors. Thus, the tendency for higher concentration may prevail in the observed period.

IV. Data and empirical analysis

Much literature has examined ownership structures after privatization in transition economies with considerable attention paid to investigating the relation between ownership and performance (e.g. Estrin and Wright 1999; Djankov and Murrell, 2002.) Studies that investigate post-privatization ownership dynamics are more rare. Earle and Estrin (1996), Blasi et al (1997), Estrin and Wright (1999) and Filatochev et al (1999) analyze Russia and document the strong position of insiders in privatization and the tendency for management takeovers of employee owned enterprises. The same tendency is found for the Baltic countries by Jones and Mygind, 1999 and 2004. Jones et al (2003) using data for Estonia, also document the strong tendency away from employee ownership most often to manager owners.

Simoneti et al (2001) have analyzed ownership dynamics of 183 Slovenian mass-privatized companies from the time or privatization to 1999. They found increased concentration especially in insider owned companies. State funds and small shareholders including employees had reduced their shares while managers and strategic investors had increased their ownership. They also found that quite few foreign investors had taken over dominant shares in Slovenian companies.

In this section we wish to see if there is empirical support for our notion of the governance life cycle. We will analyze the determinants behind ownership changes and see if there are marked differences between the two countries. Ownership groups are determined according to the widely used "dominant owner" approach, where the firm is assigned to the owner group holding more shares than any other group. By using the dominant rather than the majority ownership approach we are able to include firms, which would otherwise be dropped to the "no overall majority" group.

We have got ownership data for a panel of firms in each country through special ownership surveys. However, because of varying opportunities for data collection, the panel sets data varies between the two countries. The Russian panel has been collected by a team connected to The Russian Economic Barometer (REB), which is a Moscow-based independent research center founded in 1991. They do regular business surveys and the REB respondent network of industrial enterprises includes about 700 entities from different industries and regions of Russia. In terms of size, industries and methods of privatization the REB sample is representative for the population of Russian medium- and large-size industrial enterprises. The usual response rate is close to 30 %. In two years intervals starting from 1995 blocks of questions on ownership and corporate governance have been included in the standard REB questionnaire. Since 1999 it also covered the identity and ownership of the largest shareholder.

In Slovenia the target group consisted of a representative sample of 623 Slovenian non-financial joint-stock companies (all companies) with shares registered in the Shareholders' Register of the Central Clearing Securities Corporation. The questionnaires were collected during the summer of 2003. 150 companies returned filled questionnaires giving a response rate of 24 %. They employed on average 500 employees and generated 10 billions SIT (around 50 million Euro) of yearly income. The questions addressed the whole period between 1998-2003 on a yearly basis concerning: Corporate governance: ownership structure (total ownership by separate group of owners), evaluation of the influence of separate groups of owners, composition of the supervisory board. Data on identity and ownership stakes of the largest shareholders were obtained from the Official Shareholders' Register, which is kept and updated by the Central Clearing Securities Corporation.

We will first present the ownership dynamics descriptively in transition matrices and then in multivariate analyses look closer at the determinants for ownership changes. The econometric

analysis includes more variables, but the ownership categories are more aggregated because of the relatively low number of observations.

The evidence for ownership dynamics based on the Russian sample for the period 1995-2003 is shown in tables 8 and 9. The response in the second-yearly surveys count around 150, but although the sample has remained the same there has been a rather high shift in the firms responding in every round. Table 8 shows the dynamics for each two years period including the companies who responded in two consecutive rounds. The transition matrix for 1995 to 1997 shows in the total column to the right, that out of the 41 reported firms 26 of them were employee dominated in 1995 – the group of employees had a higher stake than the other mentioned owner-groups. 7 firms were dominated by non-financial domestic outsiders, 4 by financial outsiders etc. From the diagonal it can be seen that only 13 or 50% of the employee-dominated firms in 1995 were still dominated by employees in 1997. 2 firms have changed to manager ownership, 5 to non-financial outsiders, 3 to financial outsiders, 2 to foreign and 1 back to dominant state ownership. It is clear from the table that outsider domination is much more stable than domination by insiders. Only one out of the 11 domestic outsider dominated firms has changed and this was to foreign dominant ownership.

The changes from 1997 to 1999 are quite similar to the first matrix. Again the tendency away from ownership dominated by employees is very strong, and the most frequent change is to non-financial outsiders. Dominant employee ownership continues to be reduced by around 50% per period also in the two latest matrices. Now the changes to management ownership are on level with the change to non-financial outsiders. By far the biggest number behind the category non-financial outsiders covers domestic firms. Some of these firms may be dominated by managers from the target company. Therefore, the numbers for management domination are probably too low.

The speed of change can also be summarized by the *gross intensity of redistribution* (Kapeliushnykov 2001), which shows the average percentage of shares changing from one group to another in each firm over a given period[2]. It was 31% for the two year period 1995-97, 30% for 1997-1999, 34% for 1999-2001 and 35% for 2001-2003. This means that each year on average 15-18% of the shares change from one group to another group.

For 123 companies observed in 1997-2003 we performed multivariate analyses (not reported) of the relation between gross intensity of redistribution as dependent variable and employee, management, and outside dominant ownership together with financial results as explanatory variables. The analysis included a rough measure for profitability[3], order book level as indicator for the adaptation to the new market conditions, number of employees and relative wage-level. Industry and regions were included as control variables. The results for the model with lagged explanatory variables show that companies dominated by managers or outsiders had a significantly lower inten-

sity of redistribution than employee dominated firms. Financial outcome were the only significant economic variable in the model showing that tendency to loss-making speeded up the intensity of redistribution. Thus, together with the ownership structure, economic problems in the firms have been important determinants of redistribution of ownership in Russia. The dynamic analysis for the most frequent blocks in the ownership transition matrix with continuing employee dominance as the control group show significantly higher intensity of redistribution for all changing categories and no significant differences in intensity of redistribution for categories with continuing dominance. Changes in the financial variables have no significant effect on the intensity of redistribution.

Table 9 summarizes all the changes for companies, which have been observed for at least two periods. More than half of all the companies are changing. Employee dominated firms are changing the most with the highest frequency going to non-financial outsiders, closely followed by a large group going to managers. The change for financial outsiders is also quite high, but spread on many different directions. The lowest frequency of change is for managers and non-financial outsiders. The single foreign company represented is too thin evidence for conclusions on stability for this group, but it is a strong indication of the extremely low importance of foreign ownership in Russia.

Table 10 includes those enterprises for the period 1999-2003 for which we have data on ownership for at least two points in time and for ownership by the single largest owners. Not surprisingly, employee-dominated firms have the lowest concentration, and financial outsiders, foreign and state have the highest. The average stake of the single largest owner has increased from 31 % to 38 % over the observed period. The biggest increase is found for enterprises taken over by managers from employees and from non-financial outsiders – these two changes are also the most frequent in this table. Some of the enterprises staying in the same category (frequencies reported on the diagonal) - management, and the two groups of domestic outsiders – also have quite steeply increasing concentration, and at the same time some of the categories of changes e.g. from state to non-financial outsiders or from non financial outsiders to financial outsiders have falling concentration.

For 70 Russian companies observed 2 or more times over the period 1999-2003 we performed a multivariate analysis (not reported) showing that management and outsider dominated firms had a significantly higher concentration than firms dominated by employees. Also low financial outcomes and low wage turned out to be explanatory factors for high concentration. However, although we have used lagged explanatory variables, the causality and the mechanisms behind are not clear. One possibility could be that low performance lead to ownership change, which again lead to higher concentration. The dynamic analysis on the categories of change from the transition matrix with continuing employee ownership as the control group show significantly higher concen-

tration for nearly all changing categories as well as for continuing dominance of managers and outsiders. Low wage and performance turning from profit to losses indicate again high concentration.

Table 11 shows the results from a logit-analysis on how different variables influence the probability for different types of ownership. The analysis is done both for the initial year and the last year of observation as well as for the determinants of ownership changes over the period. In the static analysis on top of table 11, bad financial outcome gives higher probability for outsider versus employee ownership both at the start and end year (although with weakening significance). However, higher order book level decreases the probability for employee ownership at least in the start year. Wage level and number of employees have only a quite weak influence.

The number of employees comes out quite strongly in the analysis of ownership dynamics in the bottom part of table 11. The results are quite robust to whether the level and change variables are separated or combined and to the inclusion of control variables. The probability for a change from employees to outsiders compared to continuing employee ownership increases with higher number of employees. This is consistent with our predictions that higher size makes employee ownership less sustainable. Likewise in line with our predictions is the result that higher wage and also wage growth mean lower odds for the change from employee to outsiders compared to continuing employee ownership. However, for shifts from employee to manager we do not find such significant results although the signs point in the same direction.

When comparing the transition matrices in table 9 and 12 we observe some striking similarities between the ownership dynamics in Russia and *Slovenia*: For both countries employee ownership is the most frequent observation in the initial period, and it is decreasing very rapidly in both countries with many firms changing to other types of ownership and nearly no supply of new employee dominated firms. At the other end of the specter foreign dominant ownership is quite rare, but in Slovenia it is increasing rapidly and foreign ownership seems to be rather stable. Employee ownership has the highest degree of change and non-financial domestic outsiders have a quite low frequency of changes. Exactly 50 % of the observed 150 Slovenian firms changed dominant owners over the period, which for the average firm is a bit shorter than the observation period for Russia.

However, there are also important differences between the observations for the two countries. With only 2 cases in the start and 4 in the end, management dominant ownership is surprisingly rare in Slovenian medium and large enterprises. Employee domination rarely shifts to dominant manager ownership. The governance cycle away from employee ownership goes in Slovenia directly to financial or non-financial outsiders. Like in Russia the group of non-financial outsiders mainly consists of domestic companies, and some of them may be owned by managers from the tar-

get company. Financial outsider ownership is much more stable than in Russia. The PIFs have become one of the most important dominant owners in Slovenia making up 35 of the dominant financial owned firms in the end of the period.

The speed of change measured as the *gross intensity of redistribution* is somewhat lower in Slovenia. For the two years period the average change of ownership in each company is 22 % in the first years of observation and 17 % for the period 2001-2003. This means an average change per year of 9-11 % compared with 15-17 % for Russia.

Surprisingly our multivariate analysis with the gross intensity of redistribution as the dependent variable does not show a significant difference between outside and employee dominated companies. At the same time we had the steep fall in employee dominated firms, while the different outsider groups were rather stable (table 12). The explanation is probably that the same amount of changing shares could mean a fall in employee ownership and a change in domination, but for the outside owned a similar amount of shares changing hands would normally mean a consolidation – an increase in the dominant owners' shares. This is reflected in increasing concentration for the outside owned companies, see below.

For different specifications of the variables and method of analysis (OLS, random effects, fixed effects) growth in employment turned out with a significant negative effect on redistribution while the other explanatory variables for capital intensity, labor productivity, profitability and wage level as well as changes in these variables did not have any significant effects. For employee owned enterprises increase in employment could be taken as a signal for not selling the shares. However, more importantly, steeply falling employment gives a strong pressure for the employees, especially those leaving, to sell out as indicated in the theoretical section, table 1.

Table 13 covers both the owner identity and the concentration on ownership on the first largest single owner. It covers only the period 1998-2001 because we do not have information on the identity and share of the first largest owner for 2002 and 2003. On average the level of concentration on the single largest owner is quite similar to Russia. It has increased from 32 % to 39 %. The insider owned enterprises have the lowest concentration, while foreign and state owned has the highest concentration. Those enterprises staying insider owned have a stable concentration, while enterprises continuing with outsider ownership have growing concentration. The largest increases in concentration are recorded for the change from employees to foreign ownership, but also changes from employees to non-financial outsiders imply a strong increase in concentration.

Table 14 shows the Slovenian ownership transition matrix based on the first largest single owner of the given enterprise. It is quite disaggregated to give a more precise picture. The PIFs play a strong role also in the initial period, because they usually belong to the largest investors in the

companies, where they are represented. It is however, noteworthy, that their frequency of domination is falling over the period, with domestic firms as the main beneficiary. The explanation is probably that they are increasing their prevalence in some firms, while they sell out in other firms. The domestic firms have also increased their position by taking over from the state funds (Capital Fund and Development Fund). No employees or managers are represented as the first largest single owner. However, some managers may be hidden behind the group domestic firms. Employees are often organized collectively in Workers' Associations (AWAs). In this way the employees get apparently a strong and stable stake of ownership. The concentration percentages for the AWAs are quite stable and somewhat higher than the average for the total observations.

The state funds keep a quite stable ownership share in the enterprises where they continue as the strongest single owner. In the transitions from the capital fund we see a strong increase in concentration, especially when sold to domestic enterprises, while the sale to domestic firms on average means unchanged concentration. The remaining quite few and diversified cases of change of the largest owner show a quite varied pattern of concentration/diversification processes. Like in the matrix for aggregated stakes some of the cases of no change in identity of ownership have quite strong growth in concentration. This is the case for firms owned by individuals, domestic firms and foreigners, while AWAs, PIFs, and the state funds have on average quite stable ownership stakes.

The multivariate analysis on concentration confirms the descriptive results. Outside ownership has a significantly higher concentration than the base category of employee dominated enterprises. No robust significant effects are found for the different economic explanatory variables in the different specifications[4]. However, for some specifications[5] we find like in Russia a tendency so that low and falling wage level strengthen the tendency to concentration.

Table 15 shows the results of the logit-analysis on the determinants of ownership structure for Slovenia here only divided in the two large groups of employees and outsiders. The very few manager and state dominated firms are excluded from the analysis. The analysis for the start year 1998 show no significant results while the end year 2002 analysis confirms the theoretical prediction that a high number of employees has a negative effect on the odds for employee in relation to outsider dominated ownership. This is also confirmed by the dynamic analysis in table 16 showing that higher number of employees increases the probability for a change from employees to outsiders compared to continuing employee ownership. Also in line with our predictions are the positive relation between high labor costs and odds for employee ownership for the 2002 analysis. However, this result is weakened by the positive relation between wage level and the odds for change away from employees in the dynamic analysis in the bottom part of table 15. It should be noted that this results is at the 10 % level and not robust for other specifications of the model.

The results on high capital-intensity increasing the probability of employee ownership is quite surprising and contradicting our theoretical predictions. It is only significant on the 10 % level in the static analysis, but in the dynamic analysis it is strongly significant on the 1 % level both in the first and the third column of the bottom part of table 15 and quite robust for variations in specifications. It is difficult to explain why high capital intensity should increase the likelihood of employee ownership. There could be a selection bias so that employees have been able to choose the most valuable companies. However, in Slovenia employees had to pay more for capital-intensive firms in the privatization process. The earlier referred data from the privatization agency (1999) shows that employees own less in more capital intensive firms. However, our survey data does not cover the large group of small companies with high employee ownership. Although employees are somewhat weaker represented in the larger than in smaller companies, still they have dominant positions in some of them and apparently also those with high capital intensity[6].

A high level of labor productivity, measured as sales per employee, decreases the probability of employee ownership. This is surprising in relation to the high capital-intensity, which should support higher labor productivity. More studies must be made to go deeper behind these results.

V. Conclusion

We have analyzed changes in governance structures with focus on concentration and identity of owners over the life-cycle of the company. Based on agency, property rights, transaction cost and resource dependence theory and related to key stages of the life-cycle of the firm, we can identify a typical governance cycle for developed market economies, namely: manager→outside investor participation→outside investor takeover. This cycle develops in parallel with a tendency for a change from concentrated to more diversified ownership. The governance cycles are also determined by developments in the institutional and cultural framework and by specific market developments.

The transitional economies are undergoing fundamental changes in institutions with emerging and changing markets creating specific conditions for enterprises and their life-cycles. Privatization, pressures for restructuring and weak, but developing institutions define the conditions for the evolution of ownership structures. Thus, specific transitional governance cycles can be predicted.

The method used for privatization from state to private ownership determines the initial ownership structure. In many transitional countries including Russia and Slovenia, privatization lead to widespread employee ownership. This type of stakeholder oriented ownership are not sustainable if managers de facto control the firm and can manipulate the employees and set low prices

for manager takeovers of shares from liquidity-starved employees. Such takeovers solve the basic governance problem between owners and managers and management ownership can be expected to be prevalent in the framework of weak governance institutions. More advanced institutions give external owners better opportunities to control the managers, but at this stage a high concentration of ownership is needed to give external investors both the incentives and the strength to control the managers. The most advanced governance institutions also deal with the governance problem between majority and minority owners. Institutional protection of minority owners opens up for diversified external ownership, but none of the transitional countries have yet reached this stage. Therefore, the most widespread governance cycle in transitional countries with privatization favoring employee ownership can be predicted to be: employee→manager→outsider (with the last stage split in domestic→foreign in the most advanced transitions) and this governance cycle is accompanied with increasing concentration.

Employees were favored in the privatization process in both Russia and Slovenia. This resulted in an ownership structure dominated by insiders of which the majority of firms had employees as the dominant group with the most shares. The exception was in both countries some very large and capital-intensive companies. Foreign ownership was practically excluded from the privatization in both countries and the role of foreign investors was negligible at the start of the post-privatization process. The state still owned shares, but were seldom the dominant owner.

The post-privatization dynamics show both important similarities and differences between the two countries. The Russian results supports to a high degree the proposed transition governance cycle of employee→manager→outsider ownership. Russia is still in a stage with very weak governance institutions and the managers are in a very strong position both in relation to employees and in relation to potential external owners. Most of the employee owned enterprises have changed to either manager ownership or to the next step in the governance cycle, outside domestic ownership. Change from managers to outsiders is quite rare. However, some outsiders can be quite closely related to the managers and many of the changes from employees to outsiders are probably a cover for manager ownership. Therefore, outsider ownership may be somewhat exaggerated compared to manager ownership. The last step in the cycle involving foreign owners is extremely rare in Russia.

In Slovenia we have also seen a strong development away from employee-dominated ownership. However, in contrast to Russia the Slovenian managers have only taken over dominant ownership position in quite few cases in the sample. The Slovenian cycle has to a high degree skipped this stage so the typical development is employee→outsider ownership. There can be several explanations for this development: It can be argued that the institutional development in Slovenia is so advanced that outsiders are in a stronger position than what is typical for most transitional econo-

mies. The owner-manager governance problem has not been solved by manager ownership, but by concentrated outside owners. However, if the cycle is so advanced in Slovenia, that the insider stage based on weak institutions has been passed, it is surprising still to find a relatively high number of employee dominated firms. The cultural/historical heritage, the relatively high Slovenian income level, and specific institutional settings like the format of AWA – Workers Associations – may be the explanation. The AWAs represent an alliance between managers and workers. The managers have probably a strong position in this alliance, but they are not able to manipulate the workers nor take over the workers' shares for a low price like it has been common in Russia.

A high proportion of Slovenian companies have ended up as dominated by domestic financial outsiders in the form of Privatization Investment Funds. Is this an indicator of high sophistication of the institutional system in Slovenia? The PIFs were integrated in the Slovenian privatization model, and although the regulation has been stronger than in Russia the governance system in relation to the PIFs is much debated and new legislation has been enacted in 2003 (EBRD 2003). An indication that Slovenian governance is not so advanced, is the fact that companies are still in a stage of increasing concentration. The stock exchange and the protection of minority investors have apparently not been strong enough for the development of more diversified shareholder ownership. The PIFs to some extent represent diversified domestic investors, but in the latest years a concentration of ownership has also taken place within these funds.

The governance institutions are more advanced in Slovenia than in Russia. Both countries have followed parts of the proposed governance cycle for transitional economies changing the ownership from employee ownership in the direction of concentrated domestic outsider ownership. In Russia this transformation has happened through a stage of manager ownership, a stage that seems to play a minor role in Slovenia. However, the strong role of ownership by other domestic firms may in both countries cover manager ownership and should be investigated further.

The analysis shows that both countries have had a quite rapid change in ownership structures with more than half of the companies changing dominant owners over the relatively short period of analysis. The gross intensity of redistribution is somewhat lower in Slovenia than in Russia, indicating that the first stage of rapid changes have been passed in Slovenia. In Russia the redistribution is especially high for employee dominated companies, while we see no significant differences between owner types in Slovenia. In both countries there are indications that economic problems, falling employment, induce ownership change, and this change is mostly accompanied with increasing concentration. This is probably one reason why low and falling wage levels can be connected to high concentration both in Russia and Slovenia.

The specific determinants behind the ownership changes were quite difficult to detect in the quantitative analyses. Both for Russia and Slovenia high number of employees means lower odds for employee ownership and high wage gives lower odds for change away from employee ownership. The results for other performance variables are not clear. Contrary to our theoretical predictions we found that high capital intensity increased the odds for employee ownership in Slovenia. In Russia data for capital was not collected because of lack of reliability for this type of data. Although the institutional development is more advanced in Slovenia and the accounting information more reliable, the Slovenian results on capital intensity may be questioned and needs further research.

The concept of governance cycle and the application to transitional conditions contribute to explain the ownership dynamics both in relation to the enterprise life-cycle and in an institutional perspective. However, the importance of different drivers behind the specific changes over the governance cycle opens up for further research both quantitative analyses and case studies to reveal detailed stories about the background and the actual implementation of the changes at the firm level.

Table 1. Summary of predictions for determinants of ownership change – firm level.

From employee ownership	To manager ownership
+ Size High number of employees => free rider problem, high costs of decision making. Falling number of employees => some owners become outsiders, often sell off in the process. **+ Capital intensity** High capital intensity => high capital needs per employee, capital constraint, weak financial system => low employee ownership. Increasing capital intensity => need shift of owners	Capital constraint => not too large and capital intensive. Information advantage => managers opportunity to take over best performing firms. **- Size** **- Capital intensity** **? Wage** **+ Performance**
	To outsider ownership
- Wage Low wage => liquidity constraint for employees, more sell off Indicator of low quality, low human capital => not fit for employee ownership Falling wage, increased constraint => sell off **? Performance:** indicators: profit-margin, ROA, ROE High profitability => high incentive to sell and get capital But very low profitability, crisis, also push for new owners Falling profitability => pressure for sell out	Capital advantage => size and capital intensity no constraint. Employee owners leaving the firm can increase the formal number of outside owners. Information disadvantage. **+ Size** **+ Capital intensity** **? Wage** **- Performance**

Table 2. Governance cycle in developed market economies

start up stage
entrepreneur-ownership (management, family ownership)

early growth stage
change in ownership/governance because of need of supply of
external capital, management skills and networks by:
- bank (often rather passive role in relation to management)
- closely related investors, take active part in management
- venture capital, take active part in management

later growth stage
change in ownership/governance because of need of supply of
external capital, management skills and networks by:
- strategic investor, take full control with the company
- public investors, often diversified ownership

crisis/restructuring stage
change in ownership/governance because of takeover by
- bank (bad loans de facto transferred to ownership capital)
- venture capital (often specialized in takeovers (often unfriendly))
- strategic investor (use opportunity to take over cheap assets)
- defensive takeover by insiders (to avoid close down and unemployment)
- close down (assets transferred to other use)

Table 3. Specific elements in early transition influencing the governance cycle

Starting stage determined by privatization method, which may favor managers, other employees, concentrated foreign investors or diversified external ownership.

Most enterprises have a **strong need of restructuring**
(inputs, production methods, outputs not adjusted to new market conditions, with a new set of prices and incentives.)

The **financial system** not developed,
- external finance from banks limited
- the stock exchange not functioning
- venture capital firms not existing

The **governance institutions** for securing property rights (especially shareholder rights) not fully developed

=>

widespread insider ownership
enterprises have to rely on internal finance
slow strategic restructuring

Table 4. Expected governance cycles in countries in transition

Privatized (starting point depends on privatization method)

employee → manager → outside concentrated (domestic → foreign)

diversified domestic → manager → outside concentrated (domestic → foreign)

outside concentrated, foreign stable (very long run more diversified for large listed companies)

New

manager → outside concentrated (domestic → foreign)

foreign concentrated (stable)

Table 5. Some economic indicators for the transition process in Russia and Slovenia

	production 1989=100			**unemployment**			**av. wage/month USD**			**FDI/capita**
	1995	**1999**	**2002**	**1995**	**1999**	**2002**	**1995**	**1999**	**2002**	**1989-2002**
Russia	62	61	74	9.2%	12.6%	8.6%	117	64	123	48 USD
Slovenia	93	110	122	7.4%	7.4%	5.9%	945	953	911	1702 USD

based on EBRD 2003

Table 6. Overview over privatization of enterprises in Russia and Slovenia

	Russia	**Slovenia**
Starting point pre-privatizaiton	large centralized enterprises paternalistic management, only formal control by labor collective	medium to large enterprises self-management,social ownership influence by labour-collective
early privatization / early private oriented enterprises during 1980es	1986 law on new cooperatives, employee own, manager control 1987 law: individual micro firms 1989 law: labor collective lease + right to buy, management control 1992: 9500 firms, 9% of workers	managers get quite strong position in the end of the 1980es with further liberalization
wild privatization	tunneling to new private entities => management or outside domestic core-investor ownership	probably not so widespread
small privatization	strong regional differences auctions or lease buy outs, By June 1994: 80% privatized, of which 60% employee-owned	integrated in large privatization
large privatization	**mass privatization** fall 1992-94, 15000 large and medium sized firms with > 70% of production, 150 mill vouchers to population **option 1:** (21% of firms) 25% non-voting free to employees 10% option to buy at 30% discount on low book value Jan 1992 **option 2:** (over 70% of firms) 51% for cash and vouchers to employees at 1.7 * book value 1992 => 70% of firms employee owned **option 3:** (quite few firms) 30% to buy for investor group 20% buy for insiders 30%discount	December 1992 vouchers distributed (non transferable) **privatization model:** 10% to State Restitution Fund 10% to State Capital Fund 20% to Development Fund, later sale to Privatization Invest. Funds remaining 60%: **internal priv: 90% of firms** 20% for vouchers to employees up to 40% internal buyout by min 1/3 employees, 50% discount rest: public sale (Slovenians preemptive rights before foreigners) or: to Development Fund **liquidation 4% of firms,** employee involved in the process **ownership after privatization:** 40% internal, mostly to labor-intensive SMEs 25% Privatization Investmt Funds 22% Restitution/Capital Funds 13% publicly sold (for vouchers)
	1995 **loans-for-shares**, mortgage privatization of 12 large jewel firms to Financial Industrial Groups closely related to the president	
	1996- **case-by-case** privatizations, direct sale often through tenders, increasing speed and transparency	

Table 7. The development of governance institution in Russia and Slovenia

	Russia			**Slovenia**			
Bankruptcy legislation	Strict law 1998 adjusted 2002 , enforced?			first law 1994 stronger enforcement 2000-			
Governance	**1995**	**2002**	**2003**	**1995**	**2002**	**2003**	
enterprise	2	2+	2+	3-	3	3	
competition	2	2+	2+	2	3-	3-	
corporate governance developments	1990es much tunneling + abuses of minority investor rights, 1994 MMM pyramid investment fund scandal 1996 JSC law, securities law, but still weak implementation 2002 Code of Conduct			Companies Act 1993, quite secure shareholders' rights, Takeover act 1997, problems Worker codetermination 1993 Investment Fund law 1994 revised 2003, PIF problems			
Bank market	**1995**	**2002**	**2003**	**1995**	**2002**	**2003**	
total number (foreign)	2297 (21)	1329 (37)		39 (6)	22 (6)		
state owned banks % assets	37 (1997)			41.7	48.6	priv	
private loans as % GDP	8.7	17.3		27.3	41.0		
bad loans as % of total loans	12.3	11.4		9.3	10.0 (2001)		
regulation	Quite loose			quite good			
EBRD score	2	2	2	3	3+	3+	
Stock market start	1991 Moscow			1990 Ljubljana			
	1995	**2002**	**2003**	**1995**	**2000**	**2002**	**2003**
listed firms		247		ca.40	154	139	136
share capitalization % GDP	4.8	36.5		2	17	23	23
turnover/capitalization %		5			21	23	23
EBRD score	2	2+	3-	3-	3-	3-	3-

based on EBRD 2003, Gregoric 2003, ECB 2002, RTS (www.rts.ru), Ljubljana Stock Exchange (www.ljse.si),

Table 8. Ownership transition matrices for Russia 1995-2003

1995 \ 1997	Dominant Shareholders 1997						
Dominant Shareholders 1995	**Managers**	**Employees**	**Non-fin. outsiders**	**Financial outsiders**	**Foreign**	**State**	**Total 1995**
Managers	1	0	1*)	0	0	0	2
Employees	2	13	5	3	2	1	26
Non-fin. outsiders	0	0	6	1	0	0	7
Financial outsiders	0	0	2	1	1	0	4
Foreign	0	0	0	0	0	0	0
State	0	0	1	0	0	1	2
Total 1997	3	13	15	5	3	2	41

*) for this firm share of managers and workers were equal in 1995

1997 \ 1999	Dominant Shareholders 1999						
Dominant Shareholders 1997	**Managers**	**Employees**	**Non-fin. outsiders**	**Financial outsiders**	**Foreign**	**State**	**Total 1997**
Managers	5*)	2	0	0	0	0	7
Employees	1	13	8	0	0	0	22
Non-fin. outsiders	1**)	3	4	0	0	0	8
Financial outsiders	0	2	0	2	0	0	4
Foreign	0	0	0	0	1	0	1
State	0	0	1	0	0	4	5
Total 1999	7	20	13	2	1	4	47

*) for 2 firms share of managers and workers were equal in 1997
**) for this firm share of non-financial outsiders and workers were equal in 1997

1999 \ 2001	Dominant Shareholders 2001						
Dominant Shareholders 1999	**Managers**	**Employees**	**Non-fin. outsiders**	**Financial outsiders**	**Foreign**	**State**	**Total 1999**
Managers	9	0	1	0	0	0	10
Employees	9	9	7*)	1	0	0	26
Non-fin. outsiders	2	4	21	3	0	0	30
Financial outsiders	1	0	0	4	0	1	6
Foreign	0	0	0	0	0	0	0
State	0	0	2	0	0	4	6
Total 2001	21	13	31	8	0	5	78

*) for 1 firm share of non-financial outsiders and workers were equal in 1999

2001 \ 2003	Dominant Shareholders 2003						
Dominant Shareholders 2001	**Managers**	**Employees**	**Non-fin. outsiders**	**Financial outsiders**	**Foreign**	**State**	**Total 2001**
Managers	7*)	3	2	1	0	0	13
Employees	4	9	4	0	0	0	17
Non-fin. outsiders	6	1	16	2	1	0	26
Financial outsiders	0	1	2	1	0	0	4
Foreign	0	0	0	0	0	0	0
State	0	0	1	0	0	0	1
Total 2003	17	14	25	4	1	0	61

*) for 1 firm share of managers and workers were equal in 2001

Table 9. Ownership transition matrix Russia 1995-2003 (first by last years recorded)

1995 \ 2003	Dominant Shareholders (end)							
Dominant Share-holders (start)	**Mana-gers**	**Em-ployees**	**Non-fin. outsider**	**Finance outsider**	**For-eign**	**State**	**Total start**	**change**
Managers	10[*)]	2	3	0	0	0	15	33%
Employees	17	22	21	6[**)]	1	1	68	68%
Non-fin. outsiders	9	4	25	5	1	1	45	44%
Financial outsiders	2	1	2	4	1	2	12	67%
Foreign	0	0	0	0	1	0	1	0%
State	0	1	5	0	0	5	11	55%
Total (end)	38	30	56	15	4	9	152	56%

*) for 2 firms share of managers and workers were equal in the beginning

**) for 1 firm share of workers, financial outsiders and state were equal at the end

Table 10 Russia 1999-2003 with average concentration on first largest owner

1999 \ 2003	Dominant Shareholders (end)						
Dominant Share-holders (start)	**Manag-ers**	**Em-ployees**	**Non-fin. outsiders**	**Financial outsiders**	**Foreign**	**State**	**Total (start)**
Managers	10[*)] (30/37)	0	2 (20/37)	0	0	0	12 (29/37)
Employees	5 (14/28)	10 (15/14)	3 (11/21)	0	0	0	18 (14/19)
Non-financial outsiders	7 (30/57)	2 (11/21)	19 (31/40)	3 (54/54)	1 (20/51)	0	32 (32/44)
Financial outsiders	0	0	2 (61/68)	3 (41/50)	0	0	5 (49/57)
Foreigner	0	0	0	0	0	0	0
State	0	0	2 (64/21)	0	0	3 (87/68)	5 (76/49)
Total (end)	22 (26/41)	12 (15/15)	28 (32/38)	6 (48/52)	1 (20/51)	3 (87/68)	72 (31/38)

Average size (%) of the first largest block (beginning /end) in parenthesis.

*) for 1 firm share of managers and workers were equal in the beginning

Table 11. Determinant of ownership, 1997-2003, Russia
multinomial logit.

	Managers versus Employees[a)]		Outsiders versus Employees[a)]		Managers versus Outsiders[b)]	
(123 observations)	Start	End	Start	End	Start	End
financial outcome, t-1 profit=1, balance=2, loss=3	-0.59 (0.42)	0. 09 (0.37)	-0.81** (0.32)	-0.48* (0.28)	0.22 (0.44)	0.54* (0.30)
Order book level, t-1 Normal = index 100	2.80** (0.95)	1.11 (0.98)	1.30** (0.61)	0.23 (0.88)	1.50* (.85)	0.88 (0.76)
Ln no. of employees t-1	-0.67* (0.41)	-0.33 (0.29)	-0.13 (0.22)	0.12 (0.27)	-0.54 (0.40)	-0.45** (0.22)
Wage (deviation from years' mean) t-1	0.72 (0.99)	-0.41 (0.65)	0.84 (0.66)	-1.18* (0.62)	-0.12 (0.88)	0.77 (0.65)
Industry	Yes	Yes	Yes	Yes	Yes	Yes
Region	Yes	Yes	Yes	Yes	Yes	Yes
Constant	2.72 (2.76)	2.05 (2.05)	2.86* (1.53)	1.66 (1.93)	-0.14 (2.73)	0.39 (1.46)

1997-2003 combined year to year changes, (165 observations)	Change from employee to managers vs continuing employee[c)]	Change from employee to outsiders vs continuing employee[c)]	Continuing managers vs continuing employee ownership[c)]	Continuing outsiders vs continuing employee ownership[c)]	Change from outsiders to insiders vs continuing outsider[d)]
financial outcome, t-1	-1.03* (0.60)	-0.47 (0.56)	0.10 (0.63)	-0.88** (0.41)	-0.55 (0.40)
financial outcome change: loss to profit	-0.03 (1.08)	1.22 (0.95)	1.59 (1.34)	-0.17 (0.90)	1.00 (0.85)
financial outcome change: profit to loss	0.79 (1.26)	1.38 (1.08)	-1.46 (1.12)	1.05 (0.80)	-0.94 (0.85)
Order book level, t-1	0.08 (1.72)	-0.63 (1.32)	2.15* (1.10)	-0.49 (0.97)	2.13* (1.15)
Order book level, changes	-1.31 (1.81)	-1.19 (1.63)	0.79 (2.02)	-0.15 (1.26)	-0.53 (1.19)
Ln number of employees, t-1	0.04 (0.31)	0.90*** (0.36)	-0.07 (0.36)	0.47* (0.26)	-0.19 (0.29)
Number of employees, index	3.57 (2.60)	2.07 (1.81)	1.88 (1.82)	2.10 (1.65)	1.57 (1.87)
Wage, t-1 (deviation from years' mean)	-0.01 (0.98)	-3.80** (1.94)	-0.10 (0.87)	-0.97 (0.72)	0.21 (0.70)
Wage, index	-0.67 (0.50)	-0.96*** (0.47)	-1.10*** (0.44)	-0.39 (0.36)	0.24 (0.31)
Industry (dummy)	Yes	Yes	Yes	Yes	Yes
Regions (dummy)	Yes	Yes	Yes	Yes	Yes
Years (dummy)	Yes	Yes	Yes	Yes	Yes
Constant	5.14* (3.08)	-2.47 (3.15)	-0.66 (3.53)	2.99 (2.53)	0.14 (2.03)

a) employee dominated firms as base category, b) outsider dominated firms used as base category
c) continuing dominant employee as base category, d) continuing dominant outsider base category
*** significant at 1%, ** at 5% and * at 10%.

Table 12. Ownership transition matrix for Slovenia 1998-2003 (first\last years recorded)

1998 \ 2003	Dominant Shareholders (end)							
Dominant Shareholders (start)	**Managers**	**Employees**	**Non-fin. outsider**	**Finance outsider**	**Foreign**	**State**	**Total start**	**change**
Managers	1	0	1	0	0	0	2	50%
Employees	3	23	24	14	3	7	74	69%
Non-fin. outsiders	0	0	17	0	1	1	19	11%
Financial outsiders	0	1	5	17	0	0	23	26%
Foreign	0	1	0	0	3	0	4	25%
State	0	1	4	5	2	12	24	50%
Total (end)	4	26	51	36	9	20	146	50%

Employees include (few) former employees, Non-financial outsiders = domestic firms and individuals, Financial outsiders = Privatization Investment Funds (PIFs) + one bank, State = state funds+other (state).

Table 13 Slovenia 1998-2001 with average concentration on first largest owner

1998 \ 2001	Dominant Shareholders (end)						
Dominant Shareholders (start)	**Managers**	**Employees**	**Non-fin. outsiders**	**Financial outsiders**	**Foreign**	**State**	**Total (start)**
Managers	2 17/17	1 12/20	0	0	0	0	3 15/18
Employees	1 12/10	25 23/22	17 27/49	15 27/38	3 23/66	8 24/36	69 25/35
Non-financial outsiders	0	0	16 40/49	0	0	1 18/20	17 39/47
Financial outsiders	1 50/40	1 12/13	3 21/38	16 34/42	0	0	21 32/40
Foreigner	0	1 28/21	0	0	3 52/67	0	4 46/55
State	0	1 74/19	5 38/47	2 22/40	2 37/31	12 60/51	22 50/46
Total (end)	4 24/21	29 24/22	41 33/48	33 30/40	8 37/58	21 45/44	136 32/39

Table 14. Slovenia first largest owner matrix, & average concentration *1998/2001* %

1998 / 2001	AWA	Indi-vidual	Dom. firms	PIF	Bank	For-eign	Capi-tal F	Restit. Fund	Dev. Fund	State	Total	change %
AWA	6 *45/43*	0	0	0	0	0	0	0	0	0	6 *45/43*	0
Individuals	0	6 *19/30*	0	0	1 *36/43*	0	0	0	0	0	7 *21/28*	14
Domestic firms	0	0	22 *37/54*	0	1 *12/13*	1 *20/59*	1 *25/17*	0	0	0	25 *35/51*	12
Privatization Invest. Funds	0	2 *21/23*	9 *37/54*	34 *30/35*	2 *21/41*	2 *20/50*	0	1 *20/10*	0	2 *12/40*	52 *28/36*	35
Banks	0	0	1 *34/52*	0	0	0	0	0	0	0	1 *34/52*	100
Foreigners	1 *28/21*	0	0	0	0	9 *41/57*	0	0	0	0	10 *44/53*	10
Capital Fund	0	0	9 *19/40*	1 *22/60*	0	0	12 *21/21*	1 *12/12*	0	0	23 *19/30*	48
Restitution Fund	0	1 *10/23*	0	0	0	0	0	3 *26/27*	0	0	4 *22/26*	25
Development Fund	0	1 *35/20*	5 *35/35*	2 *51/26*	0	0	0	0	0	0	8 *39/31*	100
State	1 *70/64*	0	2 *55/65*	1 *20/27*	0	0	0	2 *24/25*	0	8 *66/59*	14 *56/53*	43
Total	8 *46/43*	10 *20/27*	48 *33/47*	38 *31/35*	4 *22/35*	12 *36/56*	13 *21/21*	7 *23/22*	0	10 *55/55*	150 *32/40*	33

Table 15. Determinants of Ownership Structure, Slovenia.
Binary Logits.

	1998	**2002**
	Employee vs. Outsider	Employee vs. Outsider
LnK/L_{t-1} Fixed capital per labor	-0.26 (0.35)	0.49* (0.27)
$LnEmployees_{t-1}$ number of employees	-0.48 (0.36)	-0.53** (0.26)
Average Labor Costs	0.49 (0.80)	1.31** (0.60)
$LnLaborProd_{t-1}$ Laborproductivity (sales per labor)	-0.34 (0.28)	-0.24 (0.20)
Constant	6.0 (8.06)	-12.5** (5.8)
Industry	yes	yes
Number of observations	86	119

.

1998-2002	Change from Employees to Outsider vs Continuing Employee Ownership	Change from Employees to Outsider vs Continuing Outsider Ownership	Continuing Employee vs. Continuing Outsider
LnK/L_{t-1} Fixed capital per labour	-14.7*** (0.41)	-0.16 (0.26)	0.70*** (0.26)
$LnEmployees_{t-1}$ number of employees	0.51** (0.23)	-0.12 (0.27)	-0.34 (0.25)
Average Labour Costs	1.39* (0.74)	-0.0013 (0.65)	0.27 (0.68)
$LnLaborProd_{t-1}$ Sales per labor	0.44** (0.2)	-0.32 (0.25)	-0.48** (0.20)
Growth in Fixed capital per labor	-3.95 (2.75)	-1.21 (1.14)	0.59 (0.78)
Growth Employment	-5.87* (3.24)	-2.20 (1.45)	-0.59 (1.16)
Growth in Average Labour Cost	2.6 (1.99)	1.15 (0.94)	0.43 (0.67)
Growth Labour Productivity	-2.23 (1.43)	-1.19 (0.79)	-0.98** (0.42)
Constant	-4.41 (5.06)	2.43 (6.8)	-3.32 (6.28)
Industry	Yes	Yes	Yes
Time Dummy	yes	Yes	Yes
Number of observations	154	243	331

*** significant at 1%, ** at 5% and * at 10%. Robust standard errors in brackets.

REFERENCES

Alchian, Armen, and Demsetz, Harold, 'Production. Information Costs. and Economic Organization'. *American Economic Review*. **62**: pp. 777-795. 1972.

Becht, Marco, Bolton, Patrick, and Röell, Ailsa "Corporate Governance and Control", *ECGI Working Paper Series in Finance, www.ecgi.org/wp* , 2, October, 2002.

Ben-Ner, Avner, 'The Life Cycle of Worker-owned Firms in Market Economies: a Theoretical Analysis'. *Journal of Economic Behavior and Organization*. **10:** pp. 287-313, 1988

Ben-Ner, Avner, and Yun, Buyong, 'Employee Buyout in a Bargaining Game with Asymmetric Information'. *American Economic Review*. **86**, 3: pp. 502-23, 1996.

Berglöf, Erik, and Bolton, Patrick, "The Great Divide and Beyond – Financial Architeccture in Transition, *Journal of Economic Perspectives*, **16**, 1, 2002

Berglöf, Erik, and Pajuste, Anete, "Emerging Owners, Eclipsing Markets?" in P.K. Cornelius and Kogut, Bruce, Eds., *Corporate Governance and Capital flows in a global economy*, pp. 267-304, New York, Oxford University Press, 2003.

Bevan, Alan A., Estrin, Saul, and Meyer, Klaus, "Institution Building and the Integration of Eastern Europe in International Production", *International Business Review*, forthcoming 2004.

Bim, Alexander, Jones, Derek C., and Weisskopf, Tom, "Hybrid Forms of Enterprise Organization in the Former USSR and the Russian Federation," *Comparative Economic Studies*, **35**, 1: pp. 1-37, 1993.

Blanchard, Olivier, and Aghion, Philippe, On Insider Privatization, *European Economic Review*, **40**: pp. 759-766, 1996

Blasi Joseph R., Kroumova, Maya, and Kruse, Douglas, "*Kremlin Capitalism: The Privatization of the Russian Economy"*, Ithaca, New York, Cornell University Press, 1997.

Buch, Trevor, "Modern Russian corporate governance: Convergent forces or product of Russia' s history?" *Journal of World Business*, **38**, 4: pp. 299-313, 2003.

Caviglia, Giacomo, Krause, Gerhard, and Thiman, Christian, "Key features of the financial sectors in EU accession countries", in Christian Thiman Ed. , *Financial Sectors in EU Accession Countries*: pp. 15-30, Frankfurt, European Central Bank, 2002.

Cufer, Uros, Fabian, Janez, Majic, Mojca, Prelovsek, Danica, and Tratnik, Janko, "The structure and the functioning of the financial sector in Slovenia", in Christian Thiman Ed., *Financial sectors in EU accession countries*: pp. 217-228 Frankfurt, European Central Bank, 2002.

Djankov, Simeon, and Murrell, Peter, "The determinants of enterprise restructuring in transition -an assessment of the evidence" Washington, D.C., World Bank, 2002,

Earle, John S., and Estrin, Saul, "Employee Ownership in Transition", in Frydman, Roman, Gray, Cheryl, and Rapaczynski, Andrzej, Eds., *Corporate Governance in Central Europe and Russia. vol. 2: Insiders and the State*, Budapest, CEU Press, 1996.

EBRD, "*Transition report*", London, 2003.

Estrin, Saul, and Wright, Mike, "Corporate Governance in the Former Soviet Union: an Overview". *Journal of Comparative Economics.* **27**: pp. 398-421, 1999.

EU-Commision, "*2002 Regular Report on Slovenia's Progress towards Accession*", Brussels, 2002.

Fama, Eugene F., and Jensen Michael C., "Separation of Ownership and Control", *Journal of Law and Economics*, **26**, 2: pp. 301-325. 1983.

Filatochev, Igor, Wright, Mike, and Bleaney, Michael, "Privatization. Insider Control and Managerial Entrenchment in Russia", *Economics of Transition*. **7**: pp. 481-504, 1999.

Gregoric, Aleksandra, "*Corporate Governance in Slovenia: An International Perspective*", PhD Dissertation, University of Ljubljana, Faculty of Economics, 2003.

Grossman, Sanford, and Hart, Oliver, "The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration", *Journal of Political Economy*, **94**: pp. 691-719, August, 1986.

Hansmann, Henry, "*The Ownership of Enterprise"*, Cambridge. MA: Belknap Press, 1996.

Hare, Paul, and Muravyev, Alexander, "Privatization in Russia", RECEP, Research Paper Series, 2002.

IET (1997), "*Russian Economy in 1996: Tendencies and Perspectives*", Moscow: Institute for the Economy in Transition, 1997.

Jensen, Michael C., and Meckling, William H., "Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure", *Journal of Financial Economics*, **3,** 4, pp. 305-360, 1976.

Jones, Derek.C., Kalmi, Panu, and Mygind, Niels, "Choice of Ownership Structure and Firm Performance: Evidence from Estonia", *William Davidson Working Paper*, no 560, 2003.

Jones, Derek C., and Mygind, Niels, "The Nature and Determinants of Ownership Changes After Privatization: Evidence From Estonia", *Journal of Comparative Economics*, **27**:pp.422-441, 1999.

Jones, Derek C., and Mygind, Niels, "Ownership and Productive Efficiency: Evidence from Estonia, *Review of Development Economics*, **6**, 2: pp. 284–301, 2002.

Jones, Derek C., and Mygind, Niels, "Corporate governance cycles during transition: Theory and Evidence from the Baltics", forthcoming in Filatotchev, Igor, and Wright, Mike, Eds. (title yet unknown) 2004.

Kalmi, Panu, "*On the (In)stability of Employee Ownership", Ph.D serie 10.2002,* Copenhagen Business School, 2002.

Kapelyushnikov, Rostislav, "The Largest and Dominant Shareholders in the Russian Industry:

Evidence of the Russian Economic Barometer Monitoring", *Journal of East-West Business*, **6**, 4, pp. 63-88, 2001.

La Porta, Rafael, Lopez-de-Silanes, Florencio, and Shleifer, Andrei, "Corporate Ownership around the world", *Journal of Finance*, **54**, 2: pp. 471-517, 1999.

Meade, James E., "The Theory of Labor-Managed Firms and of Profit-Sharing", *Economic Journal,* **82**: pp. 402-28, 1972.

Miyazaki, Hajime, "On Success and Dissolution of the Labor-managed Firm in the Capitalist Economy" *Journal of Political Economy*, **92**: pp. 909-931, 1984.

Mygind, Niels, "Democratic Privatisation – A Model", CBS, April 1991, conference-paper IAFESM Ithaca, New York, proceedings August 1991,.

Mygind, Niels, "Enterprise Governance in Transition: A Stakeholder Perspective", *Acta Oeconomica* **51**, 3: pp. 315-42, 2001.

Pedersen, Torben, and Thomsen, Steen, "European Patterns of Corporate Ownership: A Tvelwe Country Study", *Journal of International Business*, **28**, 4: pp. 759-778, 1997.

Pfeffer, Jeffrey, Salancik, Gerald R., *The External Control of Organizations: A Resource-Dependence Perspective*, New York, Harper & Row, 1978.

Prasnikar, Janez, Gregoric, Aleksandra, and Pahor, Marko, "Corporate Governance in Slovenian Enterprises: From Self-Management to Blockholder Control, forthcoming" in *the Politics and Economics of Central and Eastern Europe*, 2004.

Puffer, Sheila M., and McCarthy, Daniel J., "The emergence of corporate governance in Russia", *Journal of World Business* **38**, pp. 284-298, 2003.

Putterman, Louis, "Ownership and the Nature of the Firm", *Journal of Comparative Economics*, **17**, pp. 243-263, 1993.

Roe, Mark, "Political and legal restraints on ownership and control of public companies", *Journal of Financial Economics*, **27**: pp. 7-41, 1990.

Shleifer, Andrei, and Vishny, Robert W. "A Survey of Corporate Governance", *Journal of Finance*, no 2, **52**, 2: pp. 737-783, 1997.

Williamson, Oliver E., *The Economic Institutions of Capitalism: Firms, Markets, Relational Contracting*, New York, The Free Press, 1985.

Wright, Mike, Hoskinsson, Robert E., Busenitz, Lowell W., and Dial, Jay, "Finance and Management Buyouts: Agency versus Entrepreneurship Perspectives", *Venture Capital*,**3**,3 pp. 239-61, 2001.

Endnotes

[1] This research is supported by a grant to the Institute for Southeast Europe, Slovenia; REB-Monitoring (Russian Economic Barometer), Russia; Center for East European Studies, Denmark, from USAID's SEGIR EP Contract No.220/001.0-03-354, reference Russia task order no. 803, Improvement of Economic Policy Through Think Tank Partnership Project, administered by IRIS. The findings expressed herein are those of the authors and do not necessarily reflect the views of the U.S. Agency for International Development.

[2] Gross intensity of redistribution in t-th year = $1/N\ \Sigma d_j(t)$, (j=1…N), where $d_j(t)$ is intensity of redistribution of j-th company in t-th year. $d_j(t) = \frac{1}{2}\ \Sigma|\ sh_{ij}(t)-sh_{ij}(t-2)|$, (i=1,...6), where $sh_{ij}(t)$– share of i-th group in j-th company in t-th year.

[3] Because of the lack of reliability of profitability data REB uses three rough categories: 1 loss making, 2 balancing losses and profits and 3 profit making.

[4] Capital intensity is measured as fixed capital or equity capital per employee, and performance is sales per employee or ROA (both sets are strongly correlated), while wage measured as labor costs per employee and number of employees are included in all specification. We have used both OLS, Random Effects and Fixed Effects, and tested for the preferable method in given specifications.

[5] In a Fixed Effects model with the level and change in fixed capital per labor, employment, average cost per labor and ROA as explanatory variables we find a strong negative effect of the wage level on 1 % level. The Hausman test with 1% significance prefers the Fixed Effects to Random Effects model. The latter also has a negative effect for wage level, but in this case it is not significant. In the OLS version of this variable-specification again wage is negatively related to concentration, but not significant. However, here we have a negative relation to wage growth significant at the 10 % level.

[6] In fact, the mean for both fixed capital and equity per employee is the highest for the group of employee owned firms compared with all other subgroups including foreign and financial outsiders.