Privatization, Governance and Restructuring of Enterprises in the Baltics

Mygind, Niels

Niels Mygind

Privatization, governance and restructuring of enterprises in the Baltics

CEES Working Paper No. 30 - December 1999

Abstract:
The three Baltic countries show many similarities in the development of new ownership structures, but they have followed different paths of privatization and this has to some extent resulted in differences in the structures of enterprise governance. The first part of the paper describes the privatization process in each of the three Baltic countries. The process is divided into different stages dominated by different privatization methods. It is shown how these different methods have resulted in different ownership structures in each stage. These descriptive sections are summarized with comparative overviews which also include the main elements in the institutional framework for corporate governance.

In the second part of the paper the resulting ownership structures are described, and it is shown how these structures have changed after the initial privatization. All three countries have a quite high degree of both management ownership and broader employee ownership. This was especially the case for the early stage of privatization and concerned mainly small and medium sized enterprises with quite low capital intensity. For Lithuania also larger and more capital intensive enterprises were taken over by a broad group of employees. Estonia has been the fastest to promote significant foreign investment, but the other countries have been catching up the latest years. Some of the differences have been leveled off in the dynamic changes of ownership structures. The strongest change has been managers taking over the ownership from other employees.

Finally, findings from our studies on the relationships between ownership and economic performance are presented. Foreign owned enterprises takes the lead when it concerns pro-active restructuring: developing new markets, new products and new production methods. They have a high capital intensity and this has not yet paid off. Profitability is lower and factor productivity on the same level as in insider owned enterprises although foreign ownership have advantages in management and easy access to international market networks. Insider owned enterprises have more defensive restructuring with some downsizing, relatively low wages, problems of getting bank-loans, relatively low investments. However, at the same time they can show relatively good results on profitability and factor productivity. Compared to domestic outside owned enterprises insider ownership are doing surprisingly well in most measures across the three countries.

Contents:

1. Introduction

The experience in Eastern Europe shows that there is a clear connection between the different methods of privatization and resulting ownership structures in privatized enterprises. Ownership structure here refers to the distribution of ownership rights held by different groups of owners / stakeholders in relation to the enterprise. Different stakeholders - including managers, other employees, domestic persons, domestic non-financial enterprises, domestic financial enterprises and foreign enterprises - often have quite different objectives. In addition they possess different resources, such as capital, technological knowledge, management knowledge, and access to networks.

In this paper emphasis will be put on insider ownership which can be divided in management ownership and employee ownership when owned by a broad of employees. Both management and employee ownership have been important elements in the development of new ownership structures in the Baltic countries. At the same time insider ownership has been taken as an obstacle for restructuring of enterprises (Carlin and Landesman, 1997; Pohl et al., 1997, Frydman et al., 1997). We will also put emphasis on the development of foreign ownership which in contrast to insider ownership has been taken as a guarantee for restructuring because foreign investors have strong resources of capital, management and technological skills, as well as access to international supplier and distribution networks.

The rights in relation to the enterprise are not only derived from ownership of enterprise assets. In addition we need to take account of the role of legislation, giving other types of rights to different stakeholders. The development of legislation and enforcement of company code, rules on trade of ownership rights, bankruptcy legislation etc. often play important roles in influencing for the distribution of rights and thus for the development of corporate governance.

The ownership structure of a given enterprise is determined by the privatization methods interacting with the specific conditions in the enterprise (size, capital-intensity etc) and the resources of the potential new owners. Privatization will often favor a special group of stakeholders, and this group might or might not want to exchange these rights with another group of stakeholders. Such a change of ownership depends on the possibilities and conditions for trading - on the development of the market for ownership. The capital market plays an important role in this context. Some methods of privatization can help to develop the stock exchange by developing the regulatory framework and by boosting the trading of vouchers and shares on the stock exchange.

The institutional framework, legislation on registration of ownership, the development of the stock exchange, the transparency and quality of information on enterprise performance are important elements behind the change of ownership after privatization. Some groups who have acquired shares because of special preferential opportunities might want to change their portfolio. The possibilities of change thus depend on their preferred portfolio composition and on the possibilities for making this adjustment. This paper will include an analysis of the change in the distribution of ownership after privatization.

The governance structure is a question about who takes the decisions and what are the incentives for different groups to supply their resources and effort in improving the efficiency of the enterprises. The test of how the governance structure is functioning is the economic performance of the enterprises. In the context of transitional economies it is of special interest to evaluate their progress in restructuring the enterprises - to develop new products, production methods and markets. In this paper we will not make a deep analysis of restructuring, but summarize the preliminary results on our data for the three Baltic countries.

The structure of the paper is as follows. In the next three sections we will describe the privatization process in each of the Baltic countries. The process is divided into different stages dominated by different privatization methods. We will show how these different methods have resulted in different ownership structures in each stage. These descriptive sections end with comparative overviews also including the main elements in the institutional framework for corporate governance. In the following sections for each country we will analyze the resulting ownership structures, how these structures have changed after initial privatization, and finally present findings on the relationships between ownership and economic performance.

2. The privatization process in Estonia

2.1 Stages of privatization - organization and legislation

Privatization in Estonia may be divided in three stages. Early privatization, small privatization, and large privatization mainly based on tenders.

The first stage of early privatization began in all three Baltic countries in the Soviet period before full independence in August 1991. The first private enterprises were the result of the liberalization following the perestrojka policy of Gorbatjov and included small individual enterprises, cooperatives, and joint ventures. For Estonia the first early privatization was related to perestrojka experiments on “small state enterprises” dating back to 1987. In the late 1980´s and especially in 1990-91 the Baltic States already had started their own economic legislation. In this period further early developments in privatization are evident, making it difficult to define a strict borderline between early quite unauthorized or spontaneous privatization and more regulated development in later stages. In Estonia an economic reform program was introduced in 1989. This included the proposal for so-called “People´s enterprises”.

In October 1990 the Department of State Property in the Ministry of Economy was founded to supervise the development of privatization including auctions of small scale enterprises which began in March 1991. The basic law of fundamentals of ownership reform enacted in June 1991 gave priority to restitution and voucher privatization. However, this part of privatization was postponed and the most important part of the privatization in the early years of transition turned out to be small privatization based on legislation from December 1990. In the first years this privatization of small enterprises was governed by the Department of State Property in cooperation with local municipalities.

After September 1992 a more independent unit was established: The Estonian Privatization Enterprise with support from the German Treuhandanstalt. The authority of this agency was developed further in the general law on privatization introduced in June 1993. The Estonian Privatization Enterprise was merged with the Department of State Property and the name changed to Estonian Privatization Agency. While the June 1993 law contained the remaining provisions for parts of small privatization, its prime aim was to define the rules for large tender privatization, which can be considered as the third and last stage of privatization in Estonia.

Box 2.1 Estonia - enterprise privatization - organization and legislation

Organization

- Department of State Property, Ministry of Economy, founded October 1990 to carry out small and pilot privatization
- September 1992 The Estonian Privatization Enterprise (EPE) starts activities with support from experts from the German Treuhandanstalt
- September 1993 The Estonian Privatization Agency (merging EPE and DSP) diminished ambiguity on responsibility and increased centralized authority, EPA responsible for both small privatization and large privatization

Main legislation:

1986/1987 - Resolutions 43/1986 and 91/1987, small state enterprises in Estonia

December	1989	Charter on Peoples Enterprises
September	1990	Law on leasing
December	1990	The Law on Small Scale Privatization
June	1991	Law on the Basis of Property Reform - restitution, vouchers
September	1991	Law foreign investment - ensures repatriation of profits
October	1991	Land Reform act - reprivatization of land
May	1992	Amendments to Law on Small Privatization
September	1992	Bankruptcy law - strict, creditors get strong position
September	1992	Parliament resolution on tender of large enterprises, EPA
April	1993	Foreigners allowed to buy land with production facilities
June	1993	Privatization Law - small and large unified - EPA
June	1994	Free voucher trade among Estonian residents and companies

August 1994 Procedure for public offerings and investment funds

---

2.2 Early Privatization in Estonia

Early legislation in the Soviet period, before full independence in August 1991, favored insiders. The first transformation of state ownership started in 1987 in the form of “small state owned enterprises”. By 1989 there were 461 small state owned enterprises with nearly 6000 employees (Venesaar, 1991 p. 44) and in July 1991 the Ministry of Economics had registered 705 of this type of semi-private enterprise. Most of these were initiated and controlled by a large state owned enterprise, and often it was the start of a spin off to a private enterprise mainly controlled by people from management in the initiating enterprise. According to Frydman et al. (1993, p. 147) many of the successful Estonian entrepreneurs first established their businesses as “small state enterprises”. Compared to other parts of the Soviet Union also “new cooperatives” developed quite early and rapidly. By January, 1990, there were more than 2000 new cooperatives with about 7% of employment (Arkadie et al., 1991, p. 258). The number of cooperatives peaked in 1993. According to the Statistical Office of Estonia there were 2943 cooperatives in August 1993. Since then many cooperatives have been transformed to other legal forms In July 1998 there were 2124 cooperatives in the enterprise register, but only 769 of them were registered as profit earning cooperatives (ESA 1998).

Some of the first cases of employee ownership in this early stage of privatization in Estonia were leased enterprises established under the Soviet legislation of 1989. According to Terk (1996, p. 120) there were 12 large enterprises mainly with Russian employees which formed a lease system under Soviet law. The Soviet law gave the right to lease the enterprise to the work collective. An option to buy was also included and we assume that most of these enterprises were taken over by insiders. In July 1991 this law was changed to Estonian rules and around 200 of such enterprises were leased according to the new rules. The new rules also opened up for leasing by the management and by outsiders. According to Terk (1996 p. 199) management take-overs were favored by the state bureaucracy. The leasing option was stopped by 1993 and most of the leased enterprises were gradually changed to full ownership most often by the leaseholder.

The early reform program also favored so-called "peoples enterprises" which included a type of experimental leasing system for insiders. By 1991 only 7 large enterprises had been taken over mainly by insiders. Five of these firms had full employee ownership (Terk, 1996).

In the early period take-overs by foreign companies was not widespread. However, as with new cooperatives, Estonians were also the most active in the former Soviet Union in using the possibilities for creating joint ventures. The first joint ventures were established in Estonia already in 1987. There were 11 joint ventures in 1988 and 320 by the end of 1992 (Purju, 1996).

2.3 Small privatization in Estonia

After Estonian independence in August 1991 the political climate changed and a strategy emphasizing employee ownership was no longer in favor. Thus while the initial legislation on small privatization introduced in spring 1991 favored insiders, after May 1992 most of these preferences were at least formally taken away. In the early version of the law employees had the right to buy the enterprise for the “initial price” which in most cases was much below the market value of the assets. It is estimated that around 80% of the first wave of 450 small enterprises were taken over by insiders before the change in policy (Kein & Tali, 1994). Subsequently, while insider ownership still continued to be an element in the privatization process, its importance fell. In the bidding process insiders had now the opportunity to match the final bid. Furthermore, with the amendment of May 1992 the circle of participants in privatization was widened to include foreigners (Männik, 1997). In the general law on Privatization from June 1993 the last privileges of insiders were taken away

Figure 2.3 Small privatization in Estonia (objects sold by auction)

	1991	1992	1993	1994	1995	1996	1997	1998	total
objects	211*	556*	252	126	120	84	64	20	1433
price mill EEK	1.7*	42*	128	68	80	149	161	287	917
av. price 1000 EEK	8*	76*	508	540	666	1774	2516	14350	678

av. price 1000 1995 EEK	312	276	970	697	666	1442	1838	3689	659

*1991 and 1992 data from Purju 1996, other years from EPA. 1991 price was 18 mill Rubles.
EPA estimates the total number of object 1991-98 to 1367 for a total price of 893 mill EEK.

The control of the privatization process including small privatization was taken over by the Estonian Privatization Agency (EPA) in 1993. The development in sales can be found in figure 2.3. In this stage of small privatization the method of sale by auction included relatively small objects often split off from larger companies. However, the price per object increased considerably during the period, and since the June 1993 law there were no formal limit of the asset value for sale on auctions. From this time the distinction between small and large privatization was a question of method more than a question of size.

From table 2.3 it can be seen that small privatization proceeded very rapidly in the first years, when the assets were sold for very low prices. Note, however, that the increase in average price especially in the early years also due to inflation. Compare in figure 2.3 with the average price 1995 EEK, deflated by CPI. In the later years the increase is caused by the fact that it was another type of objects sold: fixed assets spinn-offs from enterprises in large privatization. The small privatization was very fast in the early years. Already in 1994 83% of the activities in the service sector, 90% of whole sale and 94% of retail sale were private. In 1991 more than 90% of the enterprises in the service and trade sector had belonged to the state or municipalities (Purju 1996).

2.4 Large privatization through EPA

From 1993 the strategy for large privatization changed to resemble the German Treuhandanstalt model. The Estonian Privatization Agency put out large enterprises for open tender, often announced internationally. The offered price was only one of the criteria for choosing the buyer, though employees were not given any preferential treatment. Also the proposed business plan and guarantees for investments and employment played an important role. In this model the main idea was to find a core investor. Since substantial capital was needed, foreign capital had an advantage in this process. Also at this stage, since the managerial group often had accumulated some capital, it was possible for them to begin to secure loans in the rapidly developing system of private banks. Furthermore, domestic capital suppliers were allowed to buy on installment and it was also possible for domestic buyers to use vouchers as part of the payment from summer 1994. Hence, at this stage, alliances between managers and a broad group of employees were no longer necessary. In addition, foreign capital gained increasing access during this stage of large privatization. From spring 1996 they were also allowed to buy on installment and to use vouchers as payment (Kein and Terk, 1997). Only in rare cases did broad groups of employees have the opportunity to take over their enterprises in this type of privatization.

The Treuhandanstalt model gained speed during 1993, and the largest number of privatization contracts for large enterprises was made in 1994, see figure 2.4-1. At the end of 1995 most large enterprises had been privatized. However, this type of tender privatization has continued since then so that by 1999 only a few though quite large enterprises remained. At the end of 1998, 483 large enterprises had been sold through EPA by direct sale at a total price of around 4.7 bill EEK or 400 mill USD. The investment guarantees amounted to 4.6 bill EEK and the owners took over liabilities for 2.2 bill EEK. The table shows a tendency for fewer, but larger and more expensive enterprise privatizations, between 1994-97.

The bulk of enterprises in the large tender privatization were industrial companies. The share of the private sector in industry thus gives an indication of the speed of this privatization: According to the Ministry of Economic Affairs (1999) the private share of industrial sales increased from 33.8% in the first quarter of 1994 to 65% in the first quarter of 1996 to 84% in the end of 1998.

Figure 2.4-1 Overview over Large privatization by tender in Estonia - total

	1993	**1994**	**1995**	**1996**	**1997**	**1998**	**total**
enterprises	54	215	142	43	17	12	483
price mill EEK average price 1000 EEK	353 6.5	1329 6.2	937 6.6	474 11.0	1295 76.2	318 26.5	4707 9.7
total paid by vouchers percent paid by vouchers	0 0%	294 22%	443 47%	134 28%	298* 23%	76 24%	1245 26%
debt taken over mill EEK average debt 1000 EEK	196 3.6	700 3.3	618 4.4	230 5.3	416 24.5	8 0.7	2168 4.5
invest. guarantees mEEK average 1000 EEK	237 4.4	858 4.0	1021 7.2	489 11.3	1715 100.9	281 23.4	4601 9.5
job guarantees average	9099 169	25573 119	17279 122	12742 30	2929 172	72 6	56226 116

* 50% paid by vouchers, excepts the shipping comp. sold for 700 mill EEK to Norwegian company.

Table 2.4-2 shows that foreign dominated take-overs played a considerable role already from the start of the tender privatization in 1993, and this role increased over time. For 1997 and 1998 foreign capital paid more than 50% of the total revenue for EPA and over the period 1993-98 foreign capital paid 31% of the revenue. In the first years the estimate of foreign take-overs might have been slightly underestimated. Before late spring 1996 (Kein and Terk, 1997) they could not pay by installment and use vouchers as was the case with domestic buyers, thus giving an incentive to have domestic investors formally involved (Purju 1998). In the first years installment could cover up to 80%.

From spring 1994 it was made possible to pay up to 50% of the price by vouchers and the compulsory initial payment was increased from 20% to 50% of the price. Most privatizations after June 1994 exploited the opportunity of 50% payment by vouchers. However, the overall average figure is considerably lower because some of the largest privatizations, especially by foreigners, did not use vouchers. (According to the information provided by EPA already by 1995 foreign take-overs paid on average 33% by vouchers and vouchers were used in 3 out of the 5 enterprises taken over by foreign capital).

Employment guarantees played a minor role in the foreign take-overs especially in the later years. Over the whole period foreigners took over liabilities to a lower extent than was the case with domestic buyers. On the other hand, foreigners have given much higher investment guarantees. This is not surprising since one of main advantages of foreign owners is their easier access to capital.

Figure 2.4-2 Large privatization by tender in Estonia - foreign dominated

	1993	1994	1995	1996	1997	1998	total
Enterprises	7	15	5	5	3	6	41 [1]
total price mill EEK	91	108	77	208	740	215	1439
average price 1000 EEK	13	7.2	15.4	41.6	247	35.8	35.1
% of total privatized	26%	8%	8%	44%	57%	68%	31%
total paid by vouchers	0	0	26	5	20	3	54
percent paid by vouchers	0%	0%	33%	2%	17%	1%	4%
debt taken over mill EEK	-	201 [2]	56	129	109	0	495
average debt 1000 EEK	-	13.4	11.2	25.8	36.3	0	12.1
% of total privatized	-	29%	9%	56%	26%	0%	23%
Invest. guarantees mEEK	87	131	193	338	1484	134	2368
average 1000 EEK	12	8.7	38.6	67.6	495	22.4	57.8
% of total privatized	37%	15%	19%	69%	87%	48%	51%
job guarantees	1939	2917	1460	54	0	0	6370
average	277	194	292	11	0	0	155
% of total privatized	21%	11%	8%	0%	0%	0%	11%
Total FDI mill EEK	2071	2789	2313	1814	3694	7942	20623
Estonians repurchase	-82	-23	-27	-420	-415	-507	-1474
Loans, reinvested profits	918	928	1146	1599	2333	2344	9268
in new enterprises	764	639	195	49	52	42	1741
in existing enterprises	470	1239	999	587	1723	6063	11081
FDI-priv.+inv.guarantees	178	239	270	546	2222	349	3807
% of FDI in existing e.	38%	19%	27%	93%	129%	6%	34%
% of total FDI	9%	9%	12%	30%	60%	4%	18%

Own calculations based on data from Central Bank of Estonia and EPA.

1. The 41 enterprises divided by nationality of investor: 9 Sweden, 9 Finland, 7 USA, 6 Germany, 2 Denmark, 2 UK and one from each of Canada, Singapore, Holland, Norway, Italy, Russia.

2. of which 197 mill EEK for Kreenholm, bought by Swedish investor, most enterprises no debt taken over.

Since both the actual purchase price and the following investment will be registered as FDI, table 2.4-2 shows the importance of privatization for attracting foreign capital in Estonia. Other flows of FDI are connected to green field investments and to take-overs of existing enterprises established or privatized by domestic owners. It is difficult to estimate the exact distribution on these different modes of FDI. Data from The Bank of Estonia and ESA shows that green field investment are quite high in the early years, but later on take-overs of existing enterprises played the strongest role. If we take the purchase price plus the investment guarantees as indicators for the importance of privatization, from table 2.4-2 we can see that privatization related FDI made up around 34% of FDI in existing enterprises in the period 1993-98 and 18% of total FDI in the period. There is a steeply increasing trend up to 1997, broken sharply in 1998, but this is mainly explained by huge Swedish/Finnish investment in the two largest private banks in Estonia in 1998. If the investment guarantees were spread out for the following three years also a more smooth increase would emerge.

Most foreign owned enterprises are quite small including many sales outlets and service entities established to facilitate access to the Estonian market. The initial stage took place when the Estonians used the possibilities in the new Soviet Joint Venture legislation, see section 2.2. At the start of 1991 414 foreign owned enterprises were registered in Estonia. By the start of 1993 the number had increased to 3814 (Liuhto, 1995). By July 1996 5857 enterprises or 9.4% of the total number of enterprises were registered as "foreign property". The investments were strongly concentrated in the area around Tallinn with 82% of the foreign owned enterprises (ESA, 1996). Based on the statistical profile for active enterprises (ESA 1998) there were 1981 active foreign enterprises in 1995 increasing to 2386 in 1997, respectively 6.5% and 6% of the total number of enterprises. Half of them were in trade and 19% in manufacturing.

Two types of vouchers have been distributed in Estonia. Capital vouchers were distributed to all residents depending on years of work. Compensation vouchers were distributed to owners (or their heirs) of property nationalized in the early Soviet period if they did not want this property back, or if it was not possible to return this property. By the end of 1998 8.3 bill EEK and 7.1 EEK bill compensation vouchers had been distributed (Ministry of Finance). The two types of vouchers are used in parallel for privatization of real estate and enterprises.

In March 1995 the biggest investment fund crashed implying losses for investors exceeding the losses incurred during the banking crisis in 1992-93 (Kein, 1995). This was an important reason why investment funds did not develop like in other countries with voucher schemes. Investment funds accumulating vouchers did not have any formulated role in the legislation. By June 1996 there were 6 privatization investment funds, and their amount of vouchers were only 1% of the total value of distributed vouchers (Kein and Terk, 1997).

Table 2.4-3 - The use of vouchers in Estonia

nominal value mill. EEK	**1994**	**1995**	**1996**	**1997**	**1998**	**total**
housing	500	1979	660	283	120	3542
real estate	0	30	204	470	1342	2046
small enterprises auctions	14	25	75	80	142	336

large enterprises tenders	16	726	218	490	243	1693
public offerings	0	704	666	940	0	2310
compensation fund	26	513	528	252	183	1502
total	556	3977	2351	2515	2030	11429
market/nominal vouchervalue	0.20	0.17	0.18	0.35	0.28	

based on Ministry of Finance

Vouchers were declared non-tradeable from the start, then during spring of 1994 trade of vouchers were gradually approved and from August 1994 vouchers were made freely tradeable (Kein and Tali, 1994 p. 31). At that time the expectations about the real value of vouchers were quite low, and at the same many poor people were in acute need of cash. Therefore, supply was high and demand relatively low resulting in a very low market price of the vouchers. As can be seen from table 2.4-3 the market price of vouchers has been rather volatile. The lowest price was 13% of the nominal value in July 1995. In the later years the price increased somewhat to reach a maximum of 47% of the nominal value at the end of the stock market boom in the autumn of 1997.

Since 1994 is has been a quite profitable business to buy up vouchers and use them as substitute for cash in enterprise privatization. Therefore, a considerable concentration of these owners certificates took place in the years following the distribution of vouchers. This is one reason why vouchers should not lead to a diversified structure of ownership in Estonia.

Vouchers were primarily used for privatization of housing, but from the end of 1994 it was also possible to use vouchers for buying minority shares in some large companies of which the majority of shares had already been sold to a core owner. In fact, only vouchers could be used in these public offerings of minority shares started in the end of 1994. The first two - the largest department store in Tallinn and the brewery SAKU, were sold by fixed price to around 50000 buyers, using 100 mill EEK nominal value of vouchers. In the following offerings the shares were sold in auctions and a much more limited number of bidders participated. In July 1997 a minority holding of shares in Eesti Gaas were sold for 406 mill EEK worth of vouchers to 1338 bidders. By the end of 1997 minority holdings in 39 enterprises had been privatized in this way removing the value of 2,3 bill. EEK vouchers from circulation. Beside the privatization of housing and industrial assets vouchers have been and will be massively used for privatization of land and forest. Until 2003 privatization of land by preemptive restitution rights and by auctions are expected to absorb 4-5 billion voucher EEK (estimate by the Ministry of Finance).

Privatization of public utilities and enterprises related to infrastructure started with the privatization of 66% of the shares in Estonian Air in June 1996. The shares were sold to a Danish company. In August 1996 part of Estonian Oil was sold to an investor from USA. In 1997 the big shipping company was sold to a Norwegian investor and in 1998 parts of the energy sector were privatized. These privatizations were part of the normal EPA-tender process, but were often combined with public offerings of minority holdings. In most cases the objects for privatization were natural monopolies, therefore, some special state regulation was needed in each case. In February 1999 49% of Eesti Telekom shares were sold on the domestic and international stock exchanges.

Already from September 1992 Estonia had implemented a rather tough law on bankruptcy. Most state owned enterprises were cut off from subsidies and some of them were liquidated and their assets privatized. 40 medium to large enterprises had been privatized through liquidation at the end of 1998, and a much larger number of small enterprises had been privatized in this way.

As in other part of the Soviet Union there were only branches of the State Savings Banks, the Agricultural Bank and the Bank for Foreign Trade to privatize. Most banks were started as private or semi-private entities quite early in the transition process. In Estonia the state banks were commercialized and transformed into joint stock companies already prior to monetary reform in June 1992. According to EPA the public share in banks equity fell from 30% in April 1993 to 23% in 1994, to 12% in the autumn of 1996. In 1996 a large state-owned insurance company was privatized (Purju and Teder 1998). In 1998 the two largest Estonian banks were taken over by two Swedish banks. Swedbank acquires 56% of Hansapank and Skandinaviska Enskilda Banken 32% of Eesti Ühispank. According to Sutt (1999) the foreign share of ownership in Estonian banks increased from 15% of the assets in 1994 to 44% in 1997 and to 61% at the end of 1998.

Quite strict regulation of the banks was implemented early on and Estonia experienced a serious banking crisis in the early years of transition, 1992-93. All the insolvent banks, including the largest bank, were closed down except two which were restructured under guidance of the central bank. The number of banks fell from around 40 in the summer of 1992 to 20 two years later (Rajasalu 1994). The tough reaction from the Central Bank was a clear signal to he economic agent that a hard budget constraint would be enforced. The law on Credit Institutions from 1995 gave authorization for universal banking allowing banks to both own and finance other financial institutions as well as non-financial enterprises.

The Privatization Agency handles privatization of land for those businesses that have been privatized through EPA. The legislation on land ownership has been somewhat behind. Prior to 1996 land were not included in the privatization contracts, but the buyers of enterprises obtained the prerogative rights to privatize the land underneath the enterprise buildings. Therefore, the land ownership has in many cases been transferred to the new owners later than the building and equipment. In 1996 169 land purchase agreements for 179 mill EEK had been signed, increasing to 264 in 1997 and 546 in 1998.

3. The privatization process in Latvia

3.1 Stages of privatization - organization and legislation

While developments in Latvia have many similarities with those in Estonia, political developments were more unstable and a political deadlock dominated the situation for some years. Accordingly, stabilization came a little later, liberalization was not so extensive and initially the privatization process was much slower. The legislative background was rather unclear for the first years of privatization.

Box 3.1 Latvia - enterprise privatization - organization and legislation

Organization:

May 1991 - November 1991
Some authority at the Department of State Property Conversion, Ministry of Economy

November 1991 - spring 1994
Decentral model:
municipalities: small privatization - service, trade, catering
different ministries: responsibility in respective fields
ministry of Economic Reforms: some overall guidance

From spring 1994**:** centralization of privatization at Latvian Privatization Agency (LPA)
(The State Property Fund managing the ongoing state enterprises)

Main legislation

March 1	1991	decree On State Property and the Basic Principles of its Conversion privatization and reprivatization of state and municipal property
November	1991	Law on small privatization - amended February 1992
June	1992	Law on large privatization - August, list of large enterprises to be privatized
November	1992	Privatization Certificates (vouchers) - amended May 1994
March	1993	Restitution of Property Rights on Enterprises and other Objects - amended: March 1995
February	1993	Law on Leasing and Leasing with the Option to Buy
February	1994	Laws on Privatization of State and Municipality Owned Object amendments: June 1994, centralization in Latvian Privatization Agency

---

In May-November 1991 the main authority of privatization was centralized in the Department of State Property Conversion under the Ministry of Economic Reforms, see box 3.1. Then followed a long decentralized period until spring 1994 when the authority was decentralized to local municipalities for small privatization and to different ministries depending on the type of enterprises. The privatization process in this period was quite complex and rather slow since many ministries wanted to keep their control over the economy. From spring 1994 new legislation centralized the control to the Latvian Privatization Agency (LPA) and after some lack of clarity in the first year the privatization process speeded up.

The stages of privatization in Latvia resemble the Estonian pattern: First early privatization related to the Soviet period and the initial period of independence; then most of the small privatization took place in the decentralized period conducted mainly by local municipalities, while only a minor part of large privatization was undertaken in the decentralized stage. The bulk of large privatization was done by LPA in the last stage. Therefore, like for Estonia, we will distinguish between early, small and large privatization.

3.2 Early privatization in Latvia

As in Estonia the first opening for take-overs by insiders and new start ups was connected to the Soviet legislation concerning cooperatives and leasing. New cooperatives counted 246 by January 1988, 1190 by January 1989, 4086 January 4086 and 4797 July 1990 (Goskomstat). In July 1990 the cooperatives employed more than 10% of the workforce (Arkadie et al, 1991, p 307). The new cooperatives developed especially in sectors such as construction, trade and information technology.

The new cooperatives often used the Soviet leasing legislation to transfer assets from state owned enterprises. On October 1990, the Latvian government made a decree to limit this type of privatization. (Frydman et al, 1993, p. 221). In October 1991 the first Latvian Law on cooperatives was implemented. All cooperatives had to restructure and re-register before March 1992. The areas open for cooperatives were restricted forcing the dissolution of many cooperatives. The permissible areas included insurance association, credit unions, retail trade, agricultural and fishing production and processing, housing, medical care, information services, sports and recreational activities (Frydman et al, 1993, p. 210). In this way the cooperative law pointed in the direction of cooperatives owned by the suppliers and consumers, not employee ownership. Other types of new cooperatives have probably re-registered under other legal forms.

Leasing of state owned enterprises started in the Soviet period could in most cases continue, but the legal status remained unclear for a long period. In February 1993 it was made possible for the group of employees to transfer the accumulated capital under the old leasing system to a new leasing contract including an option to buy.

The early complex of legislation about different legal forms of ownership included a law on Joint Stock Companies from 1990. Here it was stated that there could be different classes of shares and that employee stock could be issued at a discount or free of charge for up to 10% of the authorized capital. These shares could be issued out of the accumulated reserves. Employee shares should carry full voting rights and their values should be paid in full upon the employee's departure from the company (Frydman et. al., 1993, p. 208).

In the Soviet law on state enterprises from 1987 the general meeting of employee was given some rights concerning future production plans and the right to elect the president of the company. According to Shteinbuka (1996 p. 182) Latvia was the first republic in the former USSR in which employees could elect the director of the enterprise. Some of these elements might have had an influence on the first years of privatization in Latvia. Six experimental privatizations of large enterprises were implemented in 1991 and most of the ownership in these firms was transferred to insiders.

3.3 Small privatization

Except for some early experiments small privatization was started by November 1991 with the law on privatization of objects of trade, catering and services. These objects had been transferred to local municipalities who administered this part of privatization. The initiative for privatization could come from the employees or other potential buyers. The decision about privatization, method, initial price etc. were carried out by local privatization commissions with representatives from: the state, municipality, trade unions and specialists. Possible privatization methods were: sale to employees, auctions to a selected group, open auctions and sale to a selected buyer. According to Vojevoda and Rumpis, (1993 p. 8) especially the latest method made room for dealings of a dubious nature.

Employees who had worked a minimum of 5 years in the enterprise had a preemptive right to buy at the initial price. Purchasers should be Latvian citizens or have at least 16 years of residency, so foreigners played no role in the first years of small privatization. The legislation was changed on February 1992. The preemptive rights for employees were removed, and the scope of objects widened. Some size restrictions were also removed and the number of branches included in municipal governed privatization was gradually expanded.

Figure 3.3 - Small privatization in Latvia (trade, catering and service)

1000 Lats (current p.)	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**total**
enterprises	302	423	231	68	45	45	48	1162
of which sold on auctions	24 8%		88* 9%*				5 10%	122 11%
initial price	361	1971	3521	1174	2242	1258	865	11392
final price	1350	3871	4044	1188	2245	1263	874	14835
final/initial price	3.74	1.97	1.15	1.01	1.00	1.00	1.01	1.30
average final price	4.47	9.15	17.50	17.47	49.89	28.07	18.21	12.77
% paid by vouchers	0%	0%	2%	5%	19%	46%	58%	11%

based on Central Statistical Bureau of Latvia. *1992-94.

The chosen method of small privatization was for 1992 only 8% at auctions because the municipal authorities were against favoring the richest purchasers, and usually auctions resulted in prices much higher than the initial price. In 1992 the auction price was on average 5 times higher than the initial price while the average final price were 3.7 times higher than the initial price (Vojevoda and Rumpis, 1993). Direct sale to employees or to another selected buyer was by far the most frequent method and more than half of these small privatization were sold by installments, see table 3.3-1.

The high price difference between auctions and direct sale shows the favorable conditions for insiders who could buy at the initial price. These advantages for insiders prevailed in practice for some time after the legislation had been changed in February 1992. The local privatization commissions simply continued to give preferences to insiders (Frydman et. al., 1993, p. 223). We do not have exact data on how big a proportion was taken over by insiders, but we estimate that especially in the first years this was the case for the majority of small enterprises (see section 7.1). Most small enterprises had been privatization by 1994, so although the proportion of payment by vouchers were high in the latest years, vouchers were not important for small privatization.

3.4 Large privatization in Latvia

A list of medium and large enterprises to be privatized was passed with a decree of August 1992 and of February 1993. The list consisted of 579 enterprises proposed by the sector ministries. 400 of these enterprises were planned to be privatized by public offerings of shares, but also 147 were planned to be leased with the option to buy. Later this list was expanded to 712 enterprises (Jemeljanovs 1996 p. 205). However, except for the leasing option the privatization proceeded very slowly and before the privatization agency took over only around 50 large and medium sized enterprises were privatized and 78 companies transformed into statutory companies as a preparatory step for privatization.

In 1992-94 when the privatization process was decentralized with a key role to different ministries the existing networks could be used to the advantage of insiders. This was mainly done using the legislation on leasing with an option to buy. Former owners had the priority right to make a leasing contract, but then followed insiders of the company. This gave especially managers good opportunities to take over their enterprises (Shteinbuka, 1996 p. 187). However, until 1994, when the possibility of making new leasing contracts was removed with the new privatization law, privatization was rather slow and this type of privatization only included 234 firms.

In January 1994 started the first stage of privatization of one of the largest enterprises, Lattelekom. A British-Finnish consortium took over 49% of the shares by guaranteeing an investment over the following 3 years of 97 mill Lats (160 mill USD).

In 1994 the legislation was changed in the direction of a Treuhandmodel and the Latvian Privatization Agency (LPA) was established in May 1994. The government gradually transferred the enterprises to LPA. 907 state property units were transferred in the period 1994-98, mostly in the first three years. They had a balance of fixed assets for 566 mill LVL and they had 100.000 employees at the date of takeover by LPA. The average enterprise had 110 employees and fixed assets for a value of 625.000 LVL (1.1 mill USD). Half of the employees were in manufacturing, most assets were in transport and communication. According to LPA (1997) 75% of the companies had less than 50 employees, 20% were medium sized with 50-500 employees, and 5% of the companies were large with more than 500 employees.

LPA made its first international tender at the end of 1994. In 1995 and 1996 the process gained some speed although slower than in Estonia. The tender privatization peaked in 1997 with privatization of 313 enterprises for a total price of 82 mill LVL. The tender process resulted in a purchase agreement with a single unit or a consortium most often acquiring a majority of shares. The exceptions were some of the largest enterprises in which a smaller share was enough to get a dominating position, see table 3.4-1. Most of these sales were to domestic outsiders, but some of the largest went to foreign owners. Insiders played a minor role. The list includes some large infra-structure companies such as Latvian Gaze which was sold to a consortium of German Ruhrgas and Russian Gazprom. The purchase agreements could involve different combinations of payment in the form of cash, vouchers, installments and taking over of debt. In addition the purchasers often guaranteed certain investments and retaining a certain number of employees.

As can be seen from table 3.4-1 more than 1000 enterprises were included in this type of privatization and the total price of shares were 190 mill LVL (345 mill USD). On average 60% of the price were financed by vouchers. The market value of vouchers was only around 10-20% of the nominal value. However, purchasers had to take over a considerable debt in most of the companies. The total take-over of debt were 244 mill LVL and the investment guarantees were 127 mill LVL over the period. Job-guarantees were given for in total 47 735 jobs or around 50 for the average enterprise.

Insider take-overs lost their importance after 1994. However, mainly in the companies with shares sold on public offerings the employees had the right to buy up to 20% of the shares. By the end of 1998 shares of nominal value of 27 mill lats had been sold for vouchers to 25 611 employees and pensioners of the companies comprising 13.56% of the shares (LPA 1998). Shares for 4.4 mill lats were sold for vouchers to 250 managers of 24 companies, making up 13.6% of the shares. (LPA 1998).

Some units of enterprises were sold off and some enterprises liquidated and sold in pieces bringing 1452 liquidation units for sale of 8 mill LVL.

Of the 234 leased enterprises in the earlier stage of privatization 204 have been bought out in most cases by the leaseholder, 16 leasing contracts have been annulled (LPA, 1998). As can be seen from table 3.4-1 the average price for leasing buy-outs were on the same level as for tender privatization.

Sale of state equity holdings represents not completed privatization where a minority, but often quite dominating share holding, have been sold to a core investor. At the end of 1998 this type of privatization included 103 large enterprises.

Many of the largest enterprises have combined different privatization methods: Sale of a dominating block of shares to a core investor, and sale of minority share holdings in public offerings. The first public offering was held in August 1995, and since then 82 offerings have been held, selling on average 25% of the shares in the largest enterprises. Some companies had more rounds of offerings. (From November 1997 and July 1998 the refinery, Ventspils Nafta, had 4 offerings selling 15% of the shares). In total nearly 1 bill Lats nominal value vouchers were redeemed through public offerings by the end of 1998.

In most cases the price is set in an auction process, but in so called “people´s round” the price is preset to cut the uncertainty and to attract a broader group of persons. This type of vouchers was performed for offering 6 mill shares of Ventpils Nafta around Christmas of 1997/98. Each person with a voucher account could buy 100 shares for 35 LVL nominal voucher value per share. 18 204 persons got shares, still comprising less than 1 percent of the share capital. In

January 23 000 bidders got shares in the Riga distillery Latvias Balzams.

Some rounds of public offerings for cash have been performed starting in December 1996. 1 mill shares of Unibanka were sold in a public offering round for cash in July 1997. Later in 1997 followed successful cash offerings of Latvias Krajbanka and a manufacturing company. However, in the end of the year the cash sale of JSC Grindeks was less successful because of the crisis started in East Asia and with quite strong effects on the Baltic markets.

Figure 3.4-1 - Large privatization in Latvia - September 1994 - end 1998

	1994	1995	1996	1997	1998	1994-98
LPA-purchase contracts* of which majority foreign capital	14 5	231 26	273 22	313 38	178 34	1009 125
price mill LVL average price 1000 LVL of which foreign capital** % foreign/total	1.5 110 1.3 87%	34.3 148 6.5 19%	37.1 136 25.5 69%	82.1 262 20.8 25%	35.1 197 18.6 53%	190.1 188 72.7 38%
of which paid by vouchers % paid by vouchers by foreigners	24 0	58 53	72 66	62 41	45 24	60 43
Liabilities assumed mill LVL average 1000 LVL of which foreign capital** % foreign/total	0.3 27	13.4 58 0.5 4%	36.5 134 2.3 6%	167.7 536 142.5 85%	27.2 152	244.1 242
Investment guarantees mill LVL average 1000 LVL of which foreign capital** % foreign/total	1.1 80 0 0	18.3 79 0.8 4%	39.8 145 24.2 61%	39.2 125 37.6 96%	28.5 160 27.5 96%	126.9 125 90.1 71%
Employment guarantees average of which foreign capital	297 21 9 2	13.594 59 1.866 72	14.964 55 5730 260	18.880 60 10.100 266	7.607 43 663 20	47.735 47 18.363 147
LPA-liquidation-priv. units*	3	49	615	652	133	1452
price mill LVL	0.2	0.3	2.1	2.6	2.5	7.7
Average 1000 LVL	73	5	3	4	19	5
Leasing buy outs*	22	95	51	23	13	204
price mill LVL	4.6	18.7	5.6	6.3	1.8	37.0
Average price 1000 LVL	209	196	110	273	138	181
Sale of State Equity Holdings		15	16	35	37	103
price mill LVL of which paid by vouchers %		9.2 44%	9.0 42%	90.2 41%	16.8 47%	125.2 42%
Foreign majority buyer		6	9	10	6	31
Foreign buyer - price mill LVL of which paid by vouchers % % foreign/total		7.3 38% 80%	8.0 35% 82%	10.0 37% 11%	4.0 18% 24%	29.3 35% 23%

Public offerings**		21	15	27	19	82
nom. voucher value mill LVL		57	124	332	441	953
Typical % of shares		20-30%	20-40%	15-25%	5-30%	av. 25%

* Central Statistical Bureau of Latvia, bulletin 4/1998, ** 1995-97, LPA annual report 1997, 1994 and 1998 own estimates based on LPA-information.

There has been a close connection between the public offering programme and the development of the Riga stock exchange. The three companies participating in the first round of public offerings in January 1995 was the first companies traded on the stock exchange in the first session of July 1995. The public offerings both for vouchers and cash were performed in close cooperation with the stock exchange. As a result of public offerings 110,659 persons and legal entities in Latvia have become shareholders.

Figure 3.4-2 privatization vouchers in Latvia - redeemed in LPA-accounts

nominal value mill. LVL	**1994**	**1995**	**1996**	**1997**	**1998**	**total**
purchase agreements* accounts (objects)	5.622 127	26.021 189	21.315 256	41.256 101	25.770 81	120.295 754
public offerings + stat.comp. accounts	655 33	93.447 104	147.241 115	199.378 201	518.143 137	958.864 590
land accounts				2.150 45	4.345 218	6.495 263
total accounts	6277 160	119.468 293	174.832 371	242.780 347	548.259 436	1085.654 1607
market value of vouchers nominal 28 LVL, end year**	4	1	1	3	2	

*incl. lease buy-outs, Calculations based on LPA, ** Ministry of Economy

In November 1992 a law on vouchers were passed after long political debates, but the vouchers did not start to be distributed before September 1993 and it did not really take off before in the summer of 1994. The people got one voucher for each year of living in Latvia after the War. Prewar citizens and their descendant got on top of this 15 vouchers while 5 vouchers were deducted from people immigrated after the War. The deduction was payment for "the use of Latvian infrastructure". People connected to the Soviet Army or KGB did not get any vouchers. The result was that 87% of the vouchers were eligible for Latvian Citizens (EIU, 2:93). By July 1995, 96,5% of the population had received 104 mill. vouchers with a nominal value of 2.9 billion Lats.

It is possible to trade the vouchers, but there is a special tax of 2% and a fee to the bank administering the special privatization account must be paid. Trading of vouchers started by August 1994. The market price was in the first months less than 10% of the nominal value of 28 Lats. Like in Estonia this reflects partly the lack of clarity about what the vouchers could be used for. The legislation about voucher-privatization of housing was not passed before July 1995; and there was also much uncertainty about the privatization of enterprises for vouchers for a long period. Another reason behind the low voucher price is the lack of information and high need of means for consumption in the poorest part of the population. Like in Estonia a concentration of wealth took place in the first three months of voucher trading when the vouchers were traded for around 1-3 Lats. Then as expected the price rose to a level of 4-6 Lats, but then surprisingly the price fell from February 1995 and in the second half of 1995 the price was only 1 Lat per voucher (Shteinbuka 1996). This was an indication of the general uncertainty in Latvia and were also related to the banking crisis. In the end of 1997 the price peaked at 3 Lats, and then it fell to 2 Lats in the end of 1998.

Only very few investment funds was formed. Since 1995 9 licences were given for investment funds based on vouchers, but only 5 were functioning. In 1995-98 vouchers for a nominal value of only around 9 mill Lats were put into investment funds making up less than 1% of the distributed vouchers (Ministry of Economy).

A large number of commercial banks of Latvia was started as semi-private entities owned by state owned companies. Their full privatization had to follow the privatization of their owners. Of the 10 largest banks 34% of the capital was owned by state owned enterprises in June 1994. Often the banks functioned as agents for their owners to organize the short time finance of trade flows (World Bank, 1993). In the first years the Bank of Latvia covered the major part of the commercial banking through special commercial branches. In December 1992 the commercial branches were transferred to the Bank Privatization Committee. In late 1993 21 of these commercial branches were merged in the new "Unibank". Non-performing loans were replaced by long-term government bonds in April 1994 and the privatization program started in 1995. In May-June 21% of the shares were sold for vouchers in public offerings. International sale of shares (or depository receipts) of Unibanka were made in 1997. Other bank privatization include Latvian Investment Bank privatized 1997-98, Trasta Komercbanka in 1997, and Krajbanka, that had to be restructured first and privatization were postponed to 1999.

Foreign capital has played an increasing role in Latvian privatization. In early privatizations and the first part of the small privatizations the share of foreign capital was negligible, but in the large privatization performed by LPA there were quite many take-overs by foreign investors. For the LPA purchase contracts, 1994-1998, (see table 4.3-1) foreign capital made up 38% of the total price, 67% of the debt taken over (1995-1997) and 71% of the investment guarantees. Foreigners took over around a quarter of the purchase contract for equity share holdings. The foreign involvement is concentrated in quite few of the largest enterprises in manufacturing, energy, transport, telecommunications and the financial sector.

4. The privatization process in Lithuania

4.1 Stages of privatization - organization and legislation

The privatization process in Lithuania has been very different from the development in Estonia and Latvia. In the first years of transition, privatization was much faster and more comprehensive. In fact, the first part of privatization 1991-95 in Lithuania was one of the fastest in Eastern Europe. Vouchers and employee-ownership had a more important role, and direct sale and foreign investment had only a negligible role in this stage. The policy put much more emphasis on the interests of the workers. The main explanation behind this development lies in the fact that non-titular Lithuanian groups played a limited role. Nearly the whole population was united in the fight for independence. Once this fight was won, the nationalist parties had a much weaker position than it was the case in Estonia and Latvia, and economic problems and questions concerning distribution were in the focus of the political debate. The workers were politically stronger, because they were not split in a Lithuanian and a Russian-speaking group. The independent Lithuanian communist party had a quite strong position in the parliament of 1990 to 1992, and the victory of its successor, the Democratic Labor Party, at the election in 1992 shows the strength of left wing political forces.

The economic reforms were planned well a head of the full independence after August 1991. In fact, already in the spring of 1990 Lithuania was acting as an economic independent unit - and was blocked by USSR. This means that the period of early privatization was very short in Lithuania. The main privatization - the LIPSP program started up already in September 1991. The process was monitored by the Department of Privatization in the Ministry of Economy, a central privatization commission approved the overall plans, local commissions approved many of the detailed plans, and most sales were conducted by local privatization offices. Vouchers played an important role and the privatization was made quite fast without major changes in the framework, but with some adjustment in e.g. employee shares.

The LIPSP-program was from the start planned to finish already after one year, but the program was extended to September 1994 and then again to June 1995, when it was finished after having fulfilled most of the planned objectives, see below.

After the end of the LIPSP-program followed a period with lack of clarity and some political turmoil. The second stage did not officially start before one year later. In this stage, leftovers from LIPSP and some of the very large companies including public utilities and infrastructure enterprises were planned to be sold. The Lithuanian Privatization Agency (LPA) was established to administrate and implement this privatization for cash, but except for this the organization was not radically changed. The founding ministries still had an important role to prepare the objects for privatization. However, now they had more scope in relation to the time and methods for privatization and the result was almost a stand-still in the privatization process.

This was the background for the change in organization in the end of 1997 by establishing the State Property Fund. SPF replaced LPA and at the same time SPF took over the role of the founding enterprises. In this way, SPF to a high degree got the same authority as the sister organizations in Estonia and Latvia. However, the responsibility for the implementation of some of the largest privatizations oriented towards international investors were given to the Ministry of European Affairs.

Box 3: Lithuania - stages of privatization - organization and legislation

Organization:

First stage: February 1991-June 1995 - LIPSP-program

Department of Privatization, Ministry of Economy - monitored

Central Privatization Commission - approved privatization plans

local municipalities and founding ministries - prepared entities for privatization

Second stage: July 1995 - December 1997 - decentral privatization for cash

Founding ministries - prepare enterprises for privatization, chose methods etc.

Lithuanian Privatization Agency - implements

Parliamentary Privatization Commission - approves

Third stage: from January 1998 - centralized privatization for cash

Centralization of the functions as founder and administrator in the State Property Fund (SPF),

Parliamentary Privatization Commission - final approval

Strategic objects for international tender carried out by sector specific Public Tender Commissions and Ministry of European Affairs

Legislation:

April 1990 - Law on accumulation of Employee shares up to 10% of the capital

October 1990 - Insiders in leased companies can convert leasing-fees to shares

February 1991 - Law on the Initial Privatization of State Property (LIPSP)

October 1991 - Government decree legalizing investment funds

April 1992 - LIPSP amendment - employees priority to buy 30% of shares

September 1992 - Accumulated profits can be used for shareholder shares

January 1993 - LIPSP amendment - employees priority to buy 50% of shares

June 1995 - LIPSP officially ended, remaining vouchers usable for a few items

July 1995 - Law on the Privatization of State-Owned and Municipal Property

July 1995 - Law on Investment Companies (strengthening regulation)

February 1997 - announcing case by case privatization of 14 large companies

July 1997 - Law on investment companies (strengthening regulation)

November 1997 - new Law on the Privatization - SPF

4.2 Early privatization in Lithuania

The new cooperatives were not so widespread in Lithuania as in the other Baltic Countries. In 1990 they made up around 4500 enterprises with about 5% of the total workforce. Because they were not included in the official legal forms in the enterprise law from 1990, they were transformed into other legal forms of partnerships and closed Joint Stock Companies (Mygind, 1995 p 264).

The first privatizations were in the form of transfers of shares of leased enterprises to employees according to a resolution of October 1990. The amount transferred was the sum of the leasing fees paid, plus delayed wage payment invested in production plus part of social funds. Almost 60 enterprises were included in this program. Another early transfer to employees was included in a law from December 1990. Enterprises with capital exceeding a certain amount could sell up to 10% of their capital to employees. Part of this could be paid by vouchers. 50-60% of state enterprises used this method in the start of priva-tization until July 1991, when another program started (Frydman et. al. 1993).

4.3 First stage privatization - the LIPSP-program

The cornerstone in the fast privatization in Lithuania was the voucher scheme. The Law on the Initial Privatization of State-owned Property (LIPSP) was passed in February 1991 at a time when the result of the fight for independence was far from clear. The privatization plan was one of the elements in the fight for independence in Lithuania. The scheme signaled determination in the struggle for economic self-management. It included privatization of enterprises formally owned and controlled by the central authorities in Moscow. The vouchers and the cash quotas, described below, were given only to residents. This made an effective barrier for a flow of rubles from the rest of (former) Soviet Union to join the privatization process.

The voucher scheme was probably inspired by the Czech discussion and plans, but the Lithuanians were the first to implement the system. The vouchers were distributed in April 1991, the sale of enterprises started in September 1991 and investment funds were approved in December 1991 at the time when the Czech-voucher system took off. The distribution of vouchers was dependent on the age of the citizens. People 35 years or older received a face value of 5000 Rubles. People younger than 18 years received 1000 Rubles, and between these groups the amount was stepped down from 5000 to 1000 Rubles. The voucher rights and all the transactions were recorded in special accounts in the public Savings Bank. The nominal amount was revalued several times increasing the nominal value of the vouchers to compensate for inflation and the revaluation of the assets to be privatized. The account system was made to control the limited allowed transferability of vouchers. It was only allowed to transfer vouchers to relatives, but later it was also possible to use voucher in exchange for outstanding loans in housing, and there was made a loophole in relation to investment funds. In reality there were some official trading of vouchers. Up to the end of 1997 the State Property fund has registered a turnover of 421 mill Lats of vouchers, or around 4% of the distributed vouchers. The price was even higher than the nominal value in the start of the process in 1992. This fact reflects the policy of limited use of cash. The turnover peaked in 1993 with around 200 mill Litas. Later the market price of vouchers fell in relation to the indexed nominal value. In the second half of 1994 it was only 7-8% of the nominal value indicating the uncertainty about whether the remaining vouchers could be used for buying assets after the termination of LIPSP. When it was clear that the unused vouchers still had some limited use the price stabilized around 10-13% in 1995-97 (based on information from SPF).

Many investment funds were established on private initiative in the autumn of 1991, and the law was amended in December 1991 to legalize their functions. People could invest their vouchers in the funds. In return, they got shares in the funds. The funds invested the vouchers in different firms. Investment-fund-shares could be sold for cash. The funds were most active in 1992-93. In March 1994, about 33% of the privatized capital was owned by Investment Funds According to Lee (1996) around 400 funds were established in relation to the LIPSP privatization. Around 300 funds were formed to purchase single enterprises, insiders pooling their shares to acquire control with the company, 60-70 funds having diversified ownership and the remaining 30-40 having sizable capital and up to 25000 shareholders. According to Semeta (1996) 308 investment funds participated actively in the privatization of 1092 enterprises and acquired assets worth of 1586 mill Litas - book value 737 mill Litas or 21% of the total book value of privatized assets.

A law on investment companies was passed on July 1995, strengthening the regulation on auditing, reserves etc. and requiring the funds to get a license either as a mutual fund or a holding company. The deadline was July 1, 1997 and most of the investment funds did not fulfil the requirement. By the end of 1998 there were only 22 investment companies left with a total of 228 mill Litas worth of shares (Latvian Statistical Department, 1999). It is not clear to what extent equity has been channeled back to the original voucher owners, or to what extent the investment funds has been used for "tunneling" assets to enterprises owned by the people controlling the investment funds.

Figure 4.3-1 The use of vouchers in the LIPSP-privatization - by July 1995

public subscription of shares	5833 mill Litas	55.3%
Tenders	415 mill Litas	4.0%
auctions - small privatization	165 mill Litas	1.6%
sale residual state shares (2nd round)	392 mill Litas	3.7%
enterprise privatization Total	6805 mill Litas	64.6 %
for privatization of flats	2042 mill Litas	19.4%
for agricultural entities	410 mill Litas	4.0%
for land	521 mill Litas	5.0%
not used	726 mill Litas	7.0%
Total	10504 mill Litas	100.0%

Dept. of privatization, Ministry of Economics

The vouchers could be used both in the auctions for small enterprises, in share subscriptions for large enterprises, and in privatization of housing. The assets were sold for a combination of cash and vouchers. The cash quota connected to the vouchers set a limit for how much cash a person could use to bid on the assets to be privatized. The cash limits were softened, when existing tenants bid on their apartment, or when enterprises were not sold in the first auction. On February

1994, about 30% of the vouchers were still not used, and it was discussed what to do with the remaining vouchers. In the law, it was stipulated that the vouchers not used for buying assets would be converted to state bonds at the end of the planned privatization period. However, such a solution would be very expensive for the state budget. Instead, it was decided to move the deadline to July 1995 and prepare the remaining firms for privatization. After the deadline, still around 7% of the vouchers were not used. They were not terminated, but had still some limited use in acquiring plots of land and housing.

Under LIPSP employees had the opportunity to buy a certain percentage of the shares in the first round at concessional rates before most of the remaining shares were sold in public offerings in later rounds. This percentage of shares available for employees was increased from 10% in 1991, to 30% in 1992 and to 50% after the labor party took over the government in early 1993. Employees could use vouchers as well as cash to buy shares. The price paid in the first round was usually below the market price. Moreover, because of only partial indexation of the price of the assets and the value of the vouchers, the advantage of employees increased over time (Martinavicius, 1996). This system made it possible for employees to obtain a considerable part of the ownership even in large enterprises with relatively high capital-intensity. The 20% extra shares reserved for employees after 1993 initially did not have voting rights, but later it was made possible for the general meeting of the enterprise to convert these shares into normal voting shares.

Contrary to the case in the other Baltic countries, the advantages for employees in small privatization was usually smaller than in large privatization because small enterprises were mostly sold in public auctions.

Programs for sale of state owned enterprises to foreigners were introduced already in 1992, but until 1995 this program was used only in a limited number of cases. Also, little use was made of restitution of industrial enterprises to former owners. Hence, employee ownership was an important element in the privatization process, especially in large enterprises. The LIPSP program did not formally include special preferences for employees in small privatization, but because of inside information and access to resources for purchase in the form of vouchers, insiders also had a relatively strong position in the privatization of small firms. It should be noticed that although small privatization included around half of the 6000 enterprises to be privatized in the LIPSP program, the small enterprises only covered a small percentage of the total assets and the total number of employees, see table 4.3-2.

Data from the Privatization Department in the Ministry of Economics clearly show the spread of employee ownership over time in Lithuania. Soon after the start of privatization, at the end of 1992, employees had got a relatively small part of total privatized equity and 67% of enterprises had no employee ownership. This figure does not include the earliest insider-takeovers of shares which were formally outside the LIPSP-program. In just two years there was an astonishing change. By 1994 fewer than 5% of the privatized firms in the LIPSP program had *no* employee ownership and the percentage of enterprises where the majority of *privatized* assets were taken over by employees increased from 3% in 1991-1992, to 65% in 1993, and to 92% in 1994-1995. These developments reflect the massive increase in support for employee take-overs. However, in most of the enterprises the state kept some equity.

Small privatization of enterprises with a book value below a certain amount was done by auction, where vouchers and cash quotas could be used. There were special conditions to secure the continuation of the current activity for at least three years, and lay-offs of employee were restricted to max 30% in the same period. By August 1992 1300 small enterprises were privatized by October 1994 the number was 2498, and in July 1995 it was 2727 (Ministry of Economics).

In the normal procedure for privatization the enterprise initially made a privatization plan that should be approved by the Central Privatization Commission often represented by Privatization Committees of regional governments. In most cases, 89% of the shares were for sale. The initial offer for the first round was based on the book value revalued by some inflation parameter. If the bids did not hit the price within an interval of 10%, the price was regulated up or down, and a new round of bids took place.

Figure 4.3-2 Employee-owned share of privatized capital - LIPSP mill Litas

% owned by insiders		0%		1-10%		11-30%		31-50%		51-100%		total	
Sept. 1 1991	firms	510	100	0	0	0	0	0	0	0	0	510	100
April 7 1992	capital	338	100	0	0	0	0	0	0	0	0	338	100
April 7 1992	firms	410	43	47	5	172	18	240	25	76	8	945	100
Febr. 1 1993	capital	433	46	96	10	191	20	162	17	60	6	942	100
Febr. 1 1993	firms	29	2	39	3	66	5	141	10	1190	81	1465	100
July. 1 1995	capital	13	1	83	6	174	13	230	17	851	63	1351	100
Sept. 1 1991	firms	949	33	86	3	238	8	381	13	1266	43	2920	100
July 1. 1995	capital	785	30	179	7	365	14	391	15	912	35	2632	100
	c./firm	1.21		2.08		1.53		1.03		0.72		0.90	

Based on data from Dept. of Privatization, Ministry of Economy, Oct. 1995

The table is based on the privatized capital, more than 50% might not imply majority employee ownership because the state have retained a proportion of the shares. In the other direction counts the fact, that only registered employee owned capital in the LIPSP program is included. This do not include certain stocks which also could be controlled by insiders e.g. through investment funds, or stocks bought before LIPSP or after the first offering.

It was most difficult to sell the large energy intensive enterprises in heavy industry with close relations to the former Soviet Union. There were attempts to break them up into smaller units, and part of them was put on sale for foreign currency. In August 1992, a list of 114 state owned enterprises/objects for unrestricted sale for foreign currency were published. By July 1995 the list had been reduced to 71 enterprises. Out of these 48 were sold for 28 mill Litas of which only 4 were sold to foreign investors. This type of privatization was relatively slow and foreign sales were negligible. In fact, since the Litas were convertible in the latest years it would be more correct to call this part "privatization for cash". It is interesting to note that it was not mainly the Labor Party, but the conservative opposition who resisted sale to foreigners. This especially concerned enterprises considered to be of strategic importance. The opposition feared Russian take-overs. Therefore, they resisted strongly liberalization of foreigners´ right to buy land. The opposition was for some years able to bloc changes because liberalization in this field needed a constitutional two-thirds majority. However, the legislation was a barrier for further integration into EU, and in the end of 1995 a parliamentary committee agreed about giving rights to buy land for foreigners coming from states that were OECD members in 1989 (Baltic Independent, Dec 15, 1995).

By July 1995 the Ministry of Economics estimated the total number of state enterprises before privatization to 8177 with a total book value of 13547 mill Litas, (measured in 1995 Litas). Of these had 6698 enterprises with a total bookvalue of 9853 mill Litas been presented for privatization. 5740 were included into the privatization program, and many of these were not planned to be 100% privatized. Planned for privatization were only bookvalue of 4849 mill Litas. Included in LIPSP with sale mainly for vouchers were 2936 large enterprises with 6145 mill Litas of total capital and 2727 small enterprises with 79 mill Litas of capital. Parts of 15 (12) large enterprises with capital of 499 (360) mill Litas were put on special tender mainly for vouchers.

Figure 4.3-2 - Overview over LIPSP-small and large privatization

	1991	1992	1993	1994	1995	total	plan	%
firms privatized	846	2224	1257	821	551	5700	5740	99%
accumul. % of plan		38%	62%	75%	99%			
public subscription						2926	2936	99%
small, auctions assumul. % of plan		57%	70%	76%	100%	2726	2727	100%
Tender						15	15	
hard currency						48	71	
book value mill Litas								**Voucher value**
public subscription						2632		5833
Small						79	79	165
Tender						499	499	415
hard currency						28		-
priv. before LIPSP						545		-
residual sold						252		392
	121	1047	1240	1071	548	4035	4849	85%

Dept. of privatization, Ministry of Economics

Out of the enterprises for sale there were already in the end of 1992 sold 57% of the small and 38% of the large enterprises. By 1993 the numbers had increased to 70% and 62%, and by 1994 the numbers were 76% for small and 75% for large enterprises. This testifies a very fast privatization process. According to the Ministry of Economics by the end of LIPSP all 2727 small enterprises and 2926 or 99% of the large enterprises included into LIPSP had been privatized. By the end of the LIPSP-period July 1, 1995 83% of the capital to be privatized had been privatized. This covered nearly 100% in construction and services, 91% in industry, but only 31% in transport and public utilities. Out of the total amount of vouchers 7% had been unused, 64% had been used for payment of shares in enterprises, 19% for privatization of apartments and 9% for land and agricultural entities (Ministry of Economics).

In this stage of privatization Lithuania had the lowest level of foreign investments in the Baltics both in absolute and especially in relative terms. Foreign investment in Lithuania accumulated at the end of 1995 was 228 mill USD distributed on 5018 units. Of these were 70%

joint ventures and 30% wholly owned. The largest investor countries were UK, Germany and USA. Russia accounted for only 4% of FDI (World Bank 1996).

4.4 Second and third stage of privatization in Lithuania - 1995-1998

After the termination of the voucher privatization Lithuania established in the end of 1995 a Privatization Agency which should implement the privatization of the remaining assets for privatization. That was mainly: residual shares, public utilities and infrastructure companies. The process was based on a new law from July 1995 on Privatization of State and Municipal Property. The law delegated significant powers to the so-called founders of enterprises, in most cases line-ministries or local municipalities. They should prepare a list of companies to be privatized, sometimes after certain restructuring and they should propose the privatization methods, which could be auction (small enterprises), public subscription of shares (small and medium), tender (medium and large), lease with option to buy and direct negotiations. No vouchers were involved in this new stage of “privatization for cash”.

In 1996 a new list of 454 objects with 835 mill Litas of state capital to be privatized was approved by the government. Later the list was extended to include 1114 entities with state capital of 1.5 bln Litas. The value of state owned shares varied from a few percent to 100 percent. In 1996, only 47 small blocks of residual shares were privatized for a total price of 3.2 mill Litas. The process accelerated in 1997 to include 272 entities for 82 mill Litas. In 1996 and 1997 nearly all privatizations were done by public auction, table 4.4.

In February 1997, the new Lithuanian government announced the privatization of 14 major state enterprises in communication, energy, airlines, shipbuilding with a total of 2.3 bln Litas of state capital and 10791 employees. The Ministry of European Affairs should manage this part of the privatization.

On December 1997 a new law on privatization came into effect starting the third stage of privatization in Lithuania. The authority was centralized in the Lithuanian Property Fund (LPF), which both took the function as founder and as administrator of privatization. The Property Fund way has similar functions and authorities as the privatization agencies in Estonia and Latvia.

Figure 4.4 Second and Third stage privatization in Lithuania

	1996	**1997**	**1998**	**Total**
no of objects privatized	47	272	344	663
Privatized cap. (bookvalue) mill Litas	4.8	54.7	846.7	906.2
initial price mill Litas	3.0	56.8	2323.0	2382.8
Selling price mill Litas	3.2	82.4	2328.8	2414.4
Methods of privatization				
Public auction objects Mill Litas	46 3.2	264 80.8	321 72.1	631 156.1
Public tender objects	0	1	14	15

Mill Litas	0	0.9	214.9	215.8
direct negotiations objects mill Litas	0 0	0 0	1 2040.0	1 2040.0
Leasing with option to buy objects Mill Litas	1 0	7 0.7	2 0.1	10 0.8
Public subscription objects Mill Litas	0 0	0 0	6 1.7	6 1.7

based on information from SPF

The sale of state-owned property accelerated in 1998. The biggest deal was made for Lithuanian Telecom with 60% of the shares sold to the Telia-Sonera consortium. The Swedish/Finnish group paid 2.04 bln Litas (510 mill USD) and guaranteed investments for 884 mill Litas. This privatization makes up 88% of the total selling price for the period 1996-1998 so in this way foreign investors clearly dominate the privatization in the second and third stage. Also some of the other large privatization were sold to foreign owners including two shipyards, some sugar factories, and the largest hotel in Vilnius sold to Danish and Norwegian investors (revenue around 50 mill USD). The privatization method for minority holdings continued to be public auctions, but the remaining larger enterprises were sold by tenders or direct negotiations as was the case with Lithuanian Telecom, see table 4.4.

By the end of 1998 the government had approved a list of over 2000 entities with state capital to be privatized. However, only around 200 of these enterprises were majority controlled by the state.

The commercial activities of The Bank of Lithuania were transferred to the State Commercial Bank in September 1992. As in the other Baltic countries in a number of private commercial banks grew up. A banking crisis 1995/96 was followed by a strengthening of regulation and a fall in the number of banks. There were still three large state-owned banks including the Agricultural bank and the Savings Bank which was the main deposit bank for individuals. The state tried to privatize the Agricultural-bank in 1998. The State Commercial bank was merged with the Savings Bank and planned to be privatized in 1999. By 1998 there were 10 banks of which 2 state owned and 4 foreign owned.

5. Overview over privatization and institutions for corporate governance

In this section we will summarize and compare the development of privatization in the three Baltic countries and look at the institutional framework of corporate governance such as bankruptcy legislation, the role of the financial sector and the capital market. The results of privatization in the Baltic countries are summarized in figure 5-1.

There have been important differences in the political development in the three countries which have meant that they have chosen different paths of changing the ownership structure from a planned system to a market system based on private ownership (see Mygind 1994, 1995, 1996). In Estonia and Latvia, the nationalist-oriented policies in relation to the large Russian speaking minority meant that the period supporting broad employee take-overs of enter-prices was very short. Before independence employee take-overs implied that control was taken away from central authorities in Moscow to the Baltic Republics. When this goal was accomplished the next goal was to strengthen the position of the titular population and to find the most efficient ownership structure. In Lithuania with only a negligible Russian speaking minority, the workers and employees in general had a much stronger political role. Therefore, the early ideas of insider-take-overs were further developed in the early years of transition with the implementation of the LIPSP program. At the same time, there was strong resistance against selling out Lithuania to foreign investors and Lithuanians feared Russian take-overs in the form of Russian FDI into Lithuania. Thus, the Lithuanian policies for a long period was quite restrictive toward FDI in sharp contrast to Estonia implementing very liberal rules for foreign capital opening up for inflow of especially Finnish and Swedish investors.

In all three countries there was in the second half of the 1980´s the first movements in the direction of private enterprises in the form of new cooperatives, individual firms and in the end of the period leasing and joint ventures. This development was strongest in Estonia functioning to a high degree as a lab for market reforms in USSR. The “small state enterprises” with semi-private spinn offs from state owned enterprises is part of this development. Also in Latvia a fast development of new-cooperatives made an early start of private entrepreneurship.

In 1989 both in Estonia and Lithuania new economic reform programs were defined and started to be implemented and in both countries plans for privatization were developed. In Estonia the idea of employee-controlled “people enterprises” was only implemented in a limited number of cases because of the change in policies related to the dissolvement of USSR. The insider bias in legislation continued until spring 1992 in small privatization, but the bulk of privatization was without preferences for insiders. In Latvia most advantages for insiders in small privatization were also taken away in 1992 although there were more scope for continuation of some insider advantages in the following years.

In Lithuania the comprehensive LIPSP program implemented already in September 1991 meant that insiders got a strong role in the privatization of not only the small, but also most of the medium and larger enterprises. The LIPSP program was to a high degree based on vouchers. The largest enterprises including most utilities were only to a limited extent included in the LIPSP privatization.

All three countries have had large voucher schemes involving most of the residents. However, in both Estonia and Latvia the bulk of vouchers were related to the privatization of land

and housing. In Lithuania 65% of the vouchers were used in enterprise privatization, in Estonia 28% and in Latvia 42%. In Estonia and Latvia most of these vouchers went to broad public

Figure 5-1 Overview over privatization of enterprises, 1989-98

	Estonia	**Latvia**	**Lithuania**
early	Small SOEs and new coops, mostly owned by management. Soviet leasing, 12 empl.owned Estonian leasing 200, insider mainly management owned	new cooperatives mostly owned by management Soviet leasing to employees	new cooperatives mostly owned by management Soviet leasing, 60 empl. Owned, 1990-91, Employee-shares, 2-3% of assets
Small	Dec 1990 law: insider advantages 80% of 450 employee owned, advantages limited May 1992 and cut away June 1993 most privatized by end of 1992	Legislation November 1991 partly by local municipalities, below 10 employees, auction bidders >16 years residency trade, catering, service 85% privatized 1994 mainly by management some to other employees.	LIPSP vouchers and cash quotas can be used in auctions, conditions: employment cannot be reduced more than 30% and same activity 3 years. 1992 1993 1994 1995 sold 57% 70% 76% 100% no advantages for employees
large	1989: 7 peoples enterprises 1991: 7 SOE experiments most employee owned ------------------------------------ 1992: EPA Treuhandmodel. advantage: outsiders,foreigners tenders based on price, and investment- and job-guarantees by the end of 1998: 483 enterprises for 4.7 bill EEK (400 mill USD) 4.6 bill EEK invest. guarantees 56000 job guarantees peak of privatization 1994 most privatized 1995 nearly all by end of 1998 by 1998 15.4 bln EEK vouchers distributed Public offering of minority shares for vouchers started autumn 1994, by the end of 97: 39 holdings for 2.3 bln EEK (most vouchers for housing) end 1998 only few utilities left	1991, 6 SOE sold to insiders 1992-94 decentral privatizat. by sector ministries ca. 50 firms privatized 78 corporatized 234 leased, mainly to insiders ---------------------------------- May 1994 centralized at LPA by the end of 1998: 1009 tender privatizations for 190 mill LVL (350 millUSD) 244 mill LVL debt taken over 127 mill LVLinvestguarantee 47735 job guarantees peak of privatization 1997 most privatized 1997 nearly all by the end of 1998 by Jan. 1996 3 bln LVL vouchers distributed to 2,4 mill 97% of the population Aug. 1994 voucher market 1995-98 82 public offerings 1 bln LVL vouchers (most vouchers for housing) end 1998 only few utilities and large enterprises left	Sept. 1991, LIPSP privatization - sale of shares through vouchers and cash quotas, Dec. 1991, Investment Funds, the share employees can buy at preferential terms increased 1991:10%,1992:30%,1993:50% 1992 1993 1994 1995 sold 38% 62% 75% 99% of LIPSP 2926 enterprises, tenders of min. shares utilities, 46 SOE "hard currency sale", peak of privatization 1992 most medium and large firms privatized by end of 1994 remaining shares and very large quite slow process ------------------------------------- 1996 Lit. Privatization Agency privatization for cash founding ministries and municipalities slow down process 1998 Centralization of process in State Property Fund, remaining privatizations faster including some of largest firms end 1998 some utilities and large enterprises left.

offerings of minority holdings after sale of the majority to a core investor, but also in both these countries a core investor could finance a big share of the down payment by vouchers in the tender privatizations, figure 5-2.

Figure 5-2 - The use of vouchers for privatization in the Baltics

Nominal value mill local currency	**Estonia**	**Latvia**	**Lithuania**
mainly core owners,tender/LIPSP*	2030 (13)	165 (5)	6805 (65)
public offering - minority holdings	2310 (15)	****1120 (37)	0 (0)
housing - land - agriculture	7090 (46)	596 (20)	2973 (28)
not used (end year)	1998 3970**(26)	1998 878 (38)	1995 726 (7)
total distributed	15400 (100)	3032 (100)	10504 (100)
USD per capita ***	755	2028	706

*incl. small privatization (less than 10% of the amount), **incl. compensation fund. ***1994 exchange rates
****Ministry of Economy includes also cases when majority of shares have been sold, but not to a core investor.

In Lithuania, vouchers could only be used in the LIPSP-program. Often majority share holdings were bought mainly for vouchers. Although the LIPSP privatization resulted in a more diversified ownership structure, than the tender privatizations in Estonia and Latvia, we estimate that in most cases a core group of owners, most often insiders, acquired a majority of shares. Therefore, this type of privatization are categorized together with tenders on figure 5-3. In the later stages of privatization minority share holdings were sold for cash. In this way Lithuania had a complete opposite way of using vouchers for majority/minority shares compared to the two other Baltic countries.

Because of the limited role of vouchers in enterprise privatization in Estonia and Latvia investment funds played only a limited role in these countries. In Lithuania around 3-400 investment funds were started in relation to the LIPSP-program. Most of them were used as leverage for a group of insiders to take control with their companies, but a few developed to investment funds representing a high number of investors and with a diversified portfolio in a large number of companies. However, when the regulation was tightened in 1997 most of the investment funds were dissolved.

The timing of privatization was quite similar for the small privatization, but quite different between the three countries for the large privatization. In all three countries, the majority of small enterprises were privatized already in the early years of transition 1992-93. However, for the medium and large enterprises there have been marked differences. With the implementation of the LIPSP-program, Lithuania had the peak of privatization already in 1993 and most larger enterprises were privatized by the end of 1994. Note, however, that in most companies some shares remained state owned, and especially in some very large companies only around 10% of the shares were privatized, so in total only around 50% of the capital were privatized in the involved companies. In Estonia the privatization through EPA had the highest momentum by 1994 and most larger enterprises were privatized by the end of 1995. In Latvia the privatization through LPA gained momentum in 1995-96 to peak in 1997, and large privatization was nearly accomplished by the end of 1998.

Figure 5-3 - Different types of privatization of large enterprises end 1998

mill local currency	leasing mainly insiders	mainly insider buy-outs	tender core-investor	of which minority publ.offer	restitution liquidated /other	still state owned**	total
Estonia							
firms %	100* 16	7 1	483 75	39 (overlap)	40* 6	10* 1	640* 100
price	? -	? -	6875 67	2300 22	100* 1	? 9*	10300* 100
Latvia							
firms	237 18	6 0	1009 75	82 (overlap)	?	100* 7	1350* 100
price	37 -	? -	434 27	953 60	?	? 13*	1600* 100
Lithuania							
firms %	60 2	2940 89	100* 3	300 (overlap)	?	200* 6	3300* 100
price	? -	4000* 42	2500* 26	100* 1	?	? 30*	9600* 100

Price = price for the share privatized incl. nominal value of vouchers, (For Estonia incl. debt taken over). Vouchers counted as nominal value (if market value price for e.g. public offerings in Latvia would be only 10% of the nominal value). * Estimate. ** Firms, majority state owned, value, including minority state shares.

Looking at the largest enterprises in utilities and infrastructure Estonia has been the fastest followed by Latvia. Here Lithuania has been relatively slow. This has also been the case for the sale of residual state share holdings in companies already included in the LIPSP privatization. So while being fastest in the first round Lithuania is slowest in the last round of privatization, but after 2-3 years of hesitation and slow action from the end of LIPSP in June 1995 the privatization gained momentum in 1998.

In all three countries, foreign investors played only a minor role in the privatization of small enterprises. The advantages for insiders crowded out the possibilities for outsiders especially foreign investors. After 1992, they had some possibilities in Estonia. That was to some extent also the case in Latvia. However, for Lithuania the foreigners had a very weak position in the LIPSP-privatization.

Estonia was the first country to use privatization for the promotion of foreign investment in relation to large privatization. In the tender process foreign capital had a strong position because of their access to capital, management skills, and international business networks. Already from 1993 foreigners took over some of the largest enterprises under privatization. By the end of 1998 foreigners had taken over approximately one third of enterprise assets included in large privatization - in the years 1996-98 the foreigners paid 56% of the price paid for privatization. Latvia started the same process in the autumn of 1994 and the foreign share of purchase was 38%

for the years 1994-1998. In Lithuania the LIPSP-privatization gave very little room for foreigners, and only 4 enterprises out of 46 were taken over by foreign investors in the privatization for hard currency up to 1995. After LIPSP followed the period of stagnation and not before 1998 did foreign capital start to play an important role in privatization in Lithuania. However, just the single foreign investment in Lithuanian Telecom of more than 2 bln Litas imply that privatization revenue makes up a very big part of total FDI-stock in Lithuania, see figure 5-4.

Figure 5-4 The role of foreign investors in large privatization in the Baltics

mill local currency units	**Estonia**	**Latvia**	**Lithuania**
FDI accumulated end 1998* per capita Local/USD	20623 (100) 13568 /1130$	846 (100) 344/615 $	6501 (100) 1757/437 $
purchase of privatized firms % total privatization revenue	1439 (7.0) 31%	111** (13)	2250 (35)
debt taken over % of total large privatization	495 (2.4) 23%	150? (18)	
investment guarantees % of total large privatization	2364 (11.5) 51%	184 (22)	900? (14)

* Estonia 1993-1998, Latvia and Lithuania, stock of FDI end of 1998, Lithuania dominated by foreign investment in Telecom (purchase price 2040 mill Litas, investment guarantees 884 mill Litas). Latvia investment guarantees includes Lattelekom with 97 mill Lats. ** based on LPA-report 1998.

The methods of privatization have had a great impact on the ownership structure in the Baltic countries. However, privatization can only be considered to be the initial stage of developing the ownership and corporate governance system. Especially in the cases where special groups have been given specific advantages to acquire the assets, it can be expected that they have not got the preferred portfolio-combination through the privatization process. Many new owners will be interested in selling their shares and some other groups might want to take-over. Quite intense trading in the period after privatization is expected. However, in the transitional economies the system for trading shares - the market for ownership - is not highly developed and lack of transparency, uncertainty about registration and implementation of ownership rights might be an important barrier for the post-privatization dynamics.

The most important institutions for the dynamics of ownership are:

- competition on the product market
- bankruptcy procedures, securing the take-over by creditors in case of default
- legislation on registration, transfer, and enforcement of ownership rights
- the development of the financial system for supply of loans to enterprises
- the development of the stock exchange and a market for ownership of firms

The legislation on bankruptcy procedures was developed quite early in Estonia, September 1992. The law was strictly enforced so already by 1995 more than 1000 bankruptcy procedures had been implemented. Therefore, take-overs of liquidated assets can be assumed to play an important role in the ownership dynamics in Estonia. This is not the case in the two other countries. Also in Latvia and Lithuania bankruptcy laws were passed in 1992, but the implementation was relatively weak. The legislation has been strengthened in Latvia in 1996 and in Lithuania in 1997 and the implementation have been tightened in the latest years.

Figure 5-5 - Overview over institutions important for corporate governance

	Estonia		**Latvia**		**Lithuania**	
Product market **Competitive pressure**	very high because of totally liberal trade		increasing		increasing	
Bankruptcy system EBRD-score*	strict legislation 1992 tough enforcement 4-		strict legislation 1996 tighter enforcement 3+		Strict legislation 1997 tighter enforcement 3	
Commercial law* **Shareholders rights**	extensiveness 3+ effectiveness 4-		extensiveness 4- effectiveness 3		extensiveness 4 effectiveness 3	
Financial system Loans to private firms % of GDP	1997 856 mill $ 19%	1998 1101mill$ 20%	1997 510 mill $ 9%	1998 842 mill $ 13%	1997 907 mill$ 9%	1998 1065 mill$ 10%
Stock market Start stock exchange	May 1996		July 1995		September 1993	
	1997	1998	1997	1998	1997	1998
Listed firms	28	25	50	69	516	611
Capitalization stocks mill $	1147	619	337	396	1295	1074
% of GDP	26%	11%	6%	6%	14%	11%
turnover stocks mill$	1594	950	80	61	85	223
turnover/capitalization	1.34	1.61	0.24	0.16	0.07	0.21
% foreign portfolio	42%	45%				

* EBRD Transition Report 1999, the score with max 4+ covers the result of a survey of experts and private law firms on bankruptcy and commercial law. Capital market based on data from central banks and stock exchanges.

The legislation on registration, transfer and enforcement of ownership rights connected to the commercial code, laws on joint stock companies etc. are quite developed in all three countries. However, according to an EBRD-survey the implementation of the laws are somewhat behind in Latvia and Lithuania.

The financial system developed relatively fast in Estonia. Already in 1992-93 the system was strengthened after a major financial crisis. In Latvia there was an even more serious banking crisis in 1995 involving the largest commercial bank in Latvia. In Lithuania three of the largest banks were in crisis in the end of 1995 and 1996. In both countries the banking crisis have been followed by a period of consolidation.

In spite of a crisis for some medium banks in 1998 Estonia has now a relatively strong financial system. The two largest banks have been taken over by Swedish investors and they constitute now the strongest banks in the Baltics. Also in the two other countries the banking system have been in a positive development the latest years. However, the crisis in Russia has delayed the consolidation and some medium sized banks have been closed or merged. In Estonia loans to private enterprises made up 12% already in 1994, by 1997 it had increased to 19%. In Latvia and Lithuania the similar figure was 9% by 1997. This development is also reflected in the development of interest rates which reached a level under 20% for long term loans in 1994 in Estonia. This happened 1-2 years later in Latvia and Lithuania. Therefore, bank credits have had higher importance for the situation of corporate governance in Estonian companies compared to the situation in the other two countries, but with the consolidation of the banking system we find an increasing importance for the bank loans in all three countries.

The Tallinn Stock Exchange was opened in May 1996. Before that time some trading of shares had taken place in the over the counter market. The development of the public offerings for minority shares facilitated the development of the exchange, but there has been no strong relation between the privatization process and the development of the stock exchange. The firms dominating the main list are the big commercial banks which were started as private entities. A few large companies have been added after their privatization. In general the Tallinn stock exchange is characterized by a low number of companies - only 25 by the end of 1998. A few of them are heavily traded, especially a few large banks dominate the turnover. There have been quite high volatility since the start in 1996. Foreigners are strongly involved both with portfolio investment and in the control of core-holdings. From 1998 Swedish ownership of the two largest Estonian banks makes up a big proportion of the Western ownership of shares listed at the Tallinn Stock Exchange. By the end of 1998 the foreign share of the listed stocks were 45% (Bank of Estonia).

The capitalization and turnover on the Riga Stock Exchange are considerably lower than in Estonia, see figure 5-5. However, the Latvian stock exchange has developed quite rapidly in the latest years in close connection with the acceleration of privatization of large companies and of public offerings of shares. Of the 67 companies listed on the Riga Stock Exchange in 1998, 59 are privatized companies.

The National Stock Exchange of Lithuania (NSEL) was established already in September 1993. The early start is closely connected to the high speed of privatization in the early years of transition in Lithuania. Many of the enterprise involved in large privatization were listed on the Lithuanian Stock Exchange, so the number of enterprises listed have been much higher than in the other Baltic countries. In the second and third stage of privatization many of the minority state holdings were sold directly on stock exchange. However, most of the companies have been relatively small compared to the average listed company in Estonia. Only 4 companies were listed on the main list in Lithuania, less than half of the numbers in Estonia and Latvia. Even, including all the more than 600 enterprises listed in Lithuania, the capitalization in relation to GDP was not higher in Lithuania than in Estonia, see figure 5-5. The main problem in Lithuania, however, has been very thin trading, so the price set at NSEL has not been a good indicator for the market value of the shares in most of the listed companies.

The three Baltic stock exchanges have started a cooperation with the aim of a high degree of integration including the start of a common Baltic list of blue-chip stocks. This integration will probably further accelerate the strengthening of regulation and transparency which has happened in the latest years in all three exchanges.

The development of the exchanges are, however, relevant for only the few very large companies. For all the small and medium and most of the larger enterprises the development in competition, the general development in legislation and enforcement, and the development of the credit system is the decisive variables for the corporate governance environment. In these areas Estonia have had a reasonable functioning system since the mid of the 1990s, while for Latvia and Lithuania the same level was not reached before 1997-98. In the following sections we will look at the effects on the dynamics of ownership and on economic performance and restructuring.

6. Results of privatization - Estonia

6.1 The ownership structure after privatization

Figure 6.1-1 gives an overview over the distribution of ownership in an Estonian sample of 666 enterprises at the time of privatization before January 1995 (Jones and Mygind, 1998). 83 enterprises privatized during 1995 and 1996 were included in the 255 state (and municipality) owned enterprises. 6 enterprises did not give information about their ownership at the time of privatization. Among the 405 responding private enterprises (666-255-6) there are slightly more outside owned than insider owned. Enterprises with outside majority dominated by domestic owners constitutes 31% of the private enterprises or 19% of the total. Outside majority with foreign dominance are at the same level as inside majority with employee dominance - 22% of the private enterprises or 13% of the total. Inside majority with management dominance makes up 16% of the private enterprises and 10% of the total enterprises. 6% had no majority for either state, outsiders or insiders.

Based on information about the total distribution of enterprises for different size groups and branches a "normalization" for the whole economy can be calculated, see figure 6.1-1. The proportion of foreign ownership out of the total number of firms with 5 or more employees increases in this calculation because foreign ownership is very high in trade (35% of trade enterprises), including a high number of enterprises. Foreign ownership was also strong in transport (20%) and services (18%). Employee ownership was most widespread in agriculture (39%) and lowest in transport (3%) in January 1995. Manager ownership was most widespread in fishing, mining and wood production (27%) and lowest in trade (6%). However, by January 1997 the share of manager ownership for the whole economy increased to 26%, and for trade to 13%, (not reported in the table).

A normalization based on capital show that foreign ownership amounted to 37% of the nominal capital for the privatized enterprises on January 1995. However, if calculations are made according to the number of firms, then foreign ownership is found to play a smaller role. This is because the nominal capital is much higher in foreign owned companies (Mygind 1995).

There is no clear tendency in the distribution between different private ownership types concerning the average size measured as the average employment in 1994. However, state owned enterprises tend to be relatively large with an average size of 205 employees. A few very large state owned enterprises account for this result - the median state owned enterprises are on the level with the whole sample. The high number of small foreign owned trading companies explains why foreign ownership is most common for small enterprises, (average of 66 employees). Also insider majority owned enterprises with management dominance tend to be rather small. Comparing these results with the situation of ownership in January 1997 and average employment in 1996 (not reported in the figure) it is striking that most of the large employee dominated enterprises in the sample have disappeared.

The Statistical Office of Estonia has done a survey representing all active enterprises in Estonia. Some of the results are given in table 6.3-1. The distribution of ownership fits quite well with the earlier analysis based on the smaller sample. The enterprises that remained state or municipal owned by 1997 were relatively large and foreign owned companies were on average larger than the domestic owned enterprises. In the period 1995 to 1997 the relative weight of net sales in the public sector has been halved from 18% to 9%. However, the table show that the number of foreign enterprises only makes up 6% of the total, indicating that there might be a number of inactive foreign owned "paper" companies. It is also striking that the foreign enterprises have on average nearly around the double size measured as number of employees in comparison with other private enterprises. Looking at other indicators such as sales the share of foreign owned enterprises increases to 19% by the end of 1997 or by assets the share is 18%. Still the small sample results in a higher proportion of foreign enterprises. The difference might be explained by ESA using the legal definition of foreign ownership, and not all foreign owned enterprises are formally registered as such.

Capital intensity both measured as total assets per employee and nominal capital per employees is relatively high in foreign owned enterprises and relatively low for insider owned enterprises. For the small sample in January 1995 the nominal capital per employee is only 2000 EEK per employee or less for more than half of the insider owned enterprises. The average number of 299000 EEK per employee in foreign owned companies versus 4000 EEK in employee dominated enterprises show a striking difference. For total assets the difference is "only" ten times higher in foreign owned than in insider owned. These results can also be found for the data for 1993 and 1994 (Mygind 1997a p. 31). Table 6.3-1 for the total population of larger enterprises confirms the tendency of a quite high capital-intensity in foreign owned enterprises although the tendency is much less significant than for the small and earlier data-set.

The results can probably partly be explained by the fact that outsiders especially foreigners can afford enterprises with a higher capital per employee. Also, typically foreign owners have paid a price that is relatively high (at least compared to insiders) for similar enterprises. Relatedly, foreign ownership became more prevalent in the later stages, with insiders dominating during the early stages of the privatization process.

This last point is supported by the observation that insider takeovers were especially important during the early stages of privatization. This is shown at the bottom of figure 6.1-1. Insider ownership was very important especially in 1991, when takeovers with broad employee ownership were quite prevalent. During 1992-1994, after the ending of preferences for insiders, we see that the percentage of nominal capital owned by outsiders has become more important. In 1995 and 1996, 65 out of 243 state owned enterprises were privatized. It is worth noting that in this group there were no cases of insider majority with employee dominance. Nearly half of the responding enterprises (46%) went to majority outside domestic ownership, 16% to majority foreign ownership, 25% to management dominated insider ownership, and 7% to no majority.

The variation in the incidence of employee ownership also applies across individuals as well as firms. Even in majority owned enterprises on average 46% of the employees were not owners in 1995, and the percentage of non-owners were increasing over time. The participation rate for all enterprises varies enormously across sectors, from 78% in agriculture to less than 10% in hotels and restaurants and transport. Also at the individual level employee ownership seems to be most stable in small enterprises, and more small enterprises have a fairly equal distribution between the employee owners compared to the situation in larger enterprises. Based on the sample it is estimated that for the whole economy 29% of the employees were owners in 1995 falling to around 25% in January 1997 (Jones and Mygind 1998).

6.2 Dynamics of ownership - Estonia

The privatization process and the start of new firms are only the start of the development of new ownership structures. By using our survey data we are able to examine changes in ownership in sample firms between the time of privatization and subsequent times, (for details see Jones and Mygind, 1998).

At the top of table 6.1-1 results for the ownership structure on time of privatization and on January 1995 and 1997 are shown. Not surprisingly the number of state and municipal owned enterprises have fallen. Many of them have moved to the no answer category, which also include enterprises closed down. Out of 76 "no answers", 47 are known to be closed state owned enter-prices. Among the private enterprises the number with foreign dominance is stable while domestic owned and management owned enterprises are increasing and enterprises with insider majority with employee dominance are falling.

Table 6.1-1 shows that at the time of privatization there were 28 employee dominated enterprises with more than 100 employees in the sample. By January 1997 this number had fallen to 9. For the similar enterprises with less than 100 employees the numbers fell from 60 at the time of privatization to 42 in January 1997. Normalized for the whole economy employee ownership had in 1995 a higher proportion in large enterprises (17%) than in small (10%), but in 1997 the proportion of employee ownership in large enterprises fell to 7% (not reported). For management dominated enterprises especially the number of small enterprises in the sample increased. Domestic outside majority owned enterprises increased their share especially for large enterprises.

To analyze the dynamics more closely we present two transition matrices. Figure 6.2-1 shows the same ownership categories presented earlier, comparing the change from the situation at the time of privatization and the situation on January 1997. The earlier shown fall in employee ownership from 88 to 52 enterprises is shown, but additionally it can be seen that this change covers a stable group of 38 enterprises combined with a deduction of 50 enterprises and an addition of 14 enterprises. The flow away from employee dominance has gone mainly to management dominance, 21 cases, and to domestic outside ownership, 17 cases. Only 4 enterprises have developed in the other direction from management to employee dominance and only 3 from domestic to employee ownership. Management ownership has got 14 case from domestic outside ownership and 16 cases from state ownership. It is revealing to see that the number with no clear majority ownership group has fallen from 38 to 17, indicating a strong tendency in Estonia for an ownership configuration to emerge in which there is a clear core-owner. Most of the no-majority cases have gone to domestic and management ownership.

Excluding the no-answer group and the state-owned group, only looking at changes within the private ownership enterprises giving information for the two dates, 100 enterprises have changed category while 232 have been stable. This means a change of 100/332 = 30% in the period of approximately 3 years - a quite dynamic ownership adjustment. From the time of privatization to January 1995 this transition percentage was 71/405 = 18%, from 1995 to 1996 it was 52/373 = 14%, and from 1996 to 1997 it was 60/378 = 16%. (The sum of the three periods is less than 30 because a firm can change more than once).

Figure 6.2-2 shows a transition matrix for employee ownership comparing the time of privatization and January 1997. There is a clear tendency so that the frequency of the high degree employee ownership are falling and the frequency of the low degree of employee ownership are increasing. The cases with 0% employee shares includes mainly state owned enterprises. Thus the fall in this category reflects privatization. From the matrix it can be seen that the 85 enterprises with 50-100% employee ownership at the time of privatization has been reduced to 36 enterprises. The enterprises have transferred mainly to the neighboring categories 10-30% and 30-50%, but some majority employee owned enterprises has also transferred to the lowest categories of employee ownership. Only 45 enterprises have jumped to a category with higher employee ownership and of these 41 enterprises have jumped from 0, indicating that it covers mainly privatization cases. 80 enterprises have moved in the other direction. A similar transition matrix for management ownership (not shown) shows complementing tendencies: fall in the low categories and an increasing number of enterprises in the high categories of management ownership. This is not surprising seen in combination with the earlier mentioned tendency of transfer from employee to management ownership.

6.3 Ownership and economic performance - Estonia

To assess the economic performance of different ownership structures the initial conditions - size, capital-intensity and profitability - must be taken into consideration. We have already shown how foreign owned enterprises have a relatively high capital-intensity while the opposite is the case for insider owned enterprises. Because, insiders especially concerning small enterprises often had the first choice it could be expected that they had “skimmed the cream”. We have relatively few observations with information about profitability before privatization, and we do not have any significant results indicating that insiders took over the most profitable enterprises (Mygind 1997b). However, insiders might have acquired their enterprises at a relatively low price as also indicated by the early small privatization. Foreign investors on the other hand have advantage in the access to capital and have been able to buy highly capital intensive enterprises.

Data on performance can be taken from the sample of 666 enterprises covering the period 1993-97 with detailed ownership information and financial variables and the financial survey 1997 done by ESA covering all large enterprises and a representative sample of small enterprises, with information on foreign, but without information on insider ownership, see table 6.3-1. We will look at key variables such as sales, adjustment of labor, productivity, wages, profitability, financial sources and investment.

In a multivariate analysis based on the early data it was found that state-owned enterprises were significantly more reluctant to reduce the labor force. To some extent this was also the case for majority employee-owned enterprises, because the wage was used as a buffer instead of employment. For upwards adjustments of employment the early results show a tendency to increase employment relatively more in majority employee- and management owned enterprises (Mygind 1997, p. 33).

In the large data set for 1997 based on simple averages sales per employee are by far the highest for the group of foreign owned enterprises, and they have also the highest share of exports. Labor-productivity is also the highest for foreign owned companies although the difference is not so significant indicating that foreign owned enterprises only process a relatively small part of the whole value chain in Estonia.

Results based on simple averages give a strong weight to large companies, and it does not count for a number of other relevant factors such as size, sector, location, fixed enterprise effects, etc. For Estonia we have made some more sophisticated analysis on total factor productivity including these factors (Jones and Mygind, 1999c). The analysis is based on panel-data for the period 1993-1997. Depending on the exact specification of the model the analysis show that private ownership has 13-15% higher factor productivity than state ownership. Majority ownership by foreigners are 19-21% higher, majority management ownership 15-31% higher, and majority ownership by a broad group of employees 13-24% higher that state ownership. These results are, noteworthy, both because of the high reliability and because standard theory would not expect so high efficiency by insider owned enterprises.

The high labor productivity of foreign owned enterprises can to a high extent be explained by the high capital intensity, but if the productivity of capital is relatively low it will turn out as low total factor productivity. The high labor productivity for foreign owned enterprises might also partly be explained by high advantages in recruitment of labor. On average foreign companies pay much higher salaries than their domestic counterparts in the private sector. This was both the case in 1997 and for earlier years. Data for October 1994 on wage levels for different occupational groups shows that both foreign owned and domestic outside owned enterprises had quite high wage levels. The levels for insider owned enterprises were relatively low indicating that they hold back wages in times of trouble (Mygind 1997a).

Profitability measures for the early years show that insider ownership has quite high profitability, while foreign especially for return on assets are quite low for foreign ownership. However, this might be connected with high levels of assets, which at this point in time have not started to pay off. The surprisingly high profitability measures in table 6.3-1 for state owned enterprises might be explained by the dominance of some natural monopolies doing quite well in 1997 - e.g. telecommunication and energy. There are no significant differences between domestic and foreign ownership in the private sector.

The indicators for investment level in 1997 point out that foreign owned companies take the lead in relation to domestic private enterprises. The high level for public enterprises might again be explained by sector specific factors. Investment data for earlier years for the small sample shows in a multivariate analysis with total assets and number of employees as explanatory variables and with control for branch and location that foreign owned enterprises clearly have the highest investment level (Mygind 1997).

On average 80% of the investment were financed by internal funds, but for foreign owned enterprises this percentage was only 64%. Foreign owned companies had a relatively high financing by banks. Insider owned enterprises on the other hand have much less debt and bank loans per employee than the average for the whole group (Mygind 1997).

The data for 1997 show that private enterprises have a faster turnover of their assets and a higher debt/equity ratio than state enterprise. Within the private group domestic enterprises have a faster turnover of assets than their foreign counterpart, again indicating that foreign enterprises still not have employed their huge capital assets in the most efficient way. The higher debt/equity ratio in domestic firms compared with foreign ownership can better be explained by low equity than by a high level of debt.

Appendix 6

Figure 6.1-1 Estonia: Ownership January 1995 (plus Jan.1997),

size 1994, capital intensity, time of privatization.

frequency row percent	Majority					no majority	no answer	total
	state	outsiders		Insiders				
		foreign>dom	domestic>f	managers>e	employees>m			
TOTAL								
sample at priv.	255(38)	89 (13)	125 (19)	65 (10)	88 (13)	38 (6)	6 (1)	666 (100)
sample Jan. 95	243(36)	96 (14)	144 (22)	83 (12)	74 (11)	26 (4)	0 (0)	666 (100)
whole economy	4383(39)	2204(20)	1861(17)	1064(10)	1232(11)	415 (4)	-	11158(100)
sample Jan. 97	110(17)	86 (13)	145 (22)	106 (16)	52 (8)	17 (3)	150(23	666 (100)
whole economy	621 (5)	3621(31)	2208(19)	2947(26)	1185(10)	974 (8)	-	11556(100)
EMPLOYEES	normaliz	whole	economy					
5-19	3315(41)	1823(23)	1226(15)	570 (7)	790 (10)	292 (4)	-	8017(100)
20-99	902(33)	346(13)	500(18)	466(17)	368 (14)	122 (5)	-	2705(100)
100-	166(38)	34 (8)	135(31)	28 (6)	73 (17)	0 (0)	-	436(100)
average	205	66	118	59	137	26	-	133
25% quartile	13	10	21	20	26	10	-	14
50% median	47	22	59	32	60	22	-	42
75% quartile	128	68	146	62	138	38	-	110
BRANCHES	normalize	whole	economy					
agricult.	285(28)	0 (0)	338 (33)	0 (0)	390 (39)	0 (0)	-	1013(100)
fish,mine,wood	179(31)	28 (5)	144 (25)	154 (27)	67 (12)	3 (1)	-	576(100)
manu. food etc	126(20)	54 (8)	227 (35)	81 (13)	109 (17)	46 (7)	-	642(100)
manu. paper et	239(22)	173(16)	361 (34)	121 (11)	94 (9)	80 (7)	-	1068(100)
construction	696(57)	61 (5)	223 (18)	86 (7)	115 (9)	41 (3)	-	1222(100)
trade	1748(43)	1404(35)	255 (6)	255 (6)	343 (9)	29 (1)	-	4035(100)
transport	132(26)	99 (20)	116 (23)	75 (15)	17 (3)	64(13)	-	504(100)
service	977(47)	383(18)	197 (9)	293 (14)	96 (5)	153 (7)	-	2098(100)
nom. capital / employee1000EEK								
average	35	299	34	6	4	13	-	66
25% quartile	2	5	2	1	0	0	-	0,7
50% median	10	49	8	2	1	1	-	4
75% quartile	28	141	29	7	5	7	-	22
total assets / employee1000EEK								
average	412	398	154	44	42	179	-	258
25% quartile	19	71	30	15	16	20	-	24
50% median	56	161	57	34	35	60	-	54
75% quartile	122	437	125	61	52	99	-	123
year of priv.								
-1990	6 (5)	7 (10)	22 (32)	13 (19)	9 (13)	10(14)	2 (3)	69 (100)
1991	5 (5)	13 (12)	25 (23)	24 (22)	31 (28)	10 (9)	1 (1)	109 (100)
1992	6 (5)	30 (24)	40 (32)	16 (13)	23 (18)	9 (7)	2 (2)	126 (100)
1993	3 (4)	12 (15)	27 (35)	8 (10)	20 (26)	7 (9)	1 (1)	78 (100)
1994	3 (11)	2 (7)	11 (41)	4 (15)	5 (19)	2 (7)	0 (0)	27 (100)
1995 (own ult.)	4 (8)	5 (10)	25 (48)	11 (21)	0 (0)	3 (6)	4 (7)	52 (100)
1996 (own ult.)	14 (45)	2 (6)	7 (23)	3 (10)	0 (0)	1 (3)	4(13)	31 (100)
total	41 (8)	71 (14)	157 (32)	79 (16)	88 (18)	42 (9)	14 (3)	492 (100)

Figure 6.2-1 Estonia - majority at privatization by majority January 1997

majority at time of privatization	majority January 1997					no majority	no answer	total
	state	outsiders		Insiders				
		foreign	domestic	Managers	employees			
state	110 (43)	15 (6)	33 (13)	16 (6)	2 (1)	3 (1)	76 (30)	255 (100)
outsider foreign>domestic	0 (0)	64 (72)	1 (1)	3 (3)	1 (1)	1 (1)	19 (21)	89 (100)
outsider domestic>foreign	0 (0)	2 (2)	79 (63)	14 (11)	3 (3)	2 (2)	25 (20)	125 (100)
insider managers>employees	0 (0)	1 (2)	5 (8)	44 (68)	4 (6)	2 (3)	9 (14)	65 (100)
insider employees>managers	0 (0)	1 (1)	17 (19)	21 (24)	38 (43)	2 (2)	9 (10)	88 (100)
no majority	0 (0)	3 (8)	9 (24)	5 (13)	3 (8)	7 (18)	11 (29)	38 (100)
no answer	0 (0)	0 (0)	1 (17)	3 (50)	1 (17)	0 (0)	1 (17)	6 (100)
total privatization	255 (38)	89 (13)	125 (19)	65 (10)	88 (13)	38 (6)	6 (1)	666 (100)
total Jan. 1995	243 (36)	96 (14)	144 (22)	83 (12)	74 (11)	26 (4)	0 (0)	666 (100)
total Jan. 1996	162 (24)	89 (13)	155 (23)	94 (14)	71 (11)	21 (3)	74 (11)	666 (100)
total Jan. 1997	110 (17)	86 (13)	145 (22)	106 (16)	52 (8)	17 (3)	150 (23)	666 (100)

Figure 6.2-2 Estonia - employee ownership at privatization by Jan. 1997

Time of privatization	January 1997							no data	total
Employee shares	**0%**	**0-5%**	**5-10%**	**10-30%**	**30-50%**	**50-100%**	**100%**		
0%	332 (67)	13 (3)	5 (1)	14 (3)	5 (1)	4 (1)	0 (0)	126 (25)	499 (100)
0-5%	2 (20)	6 (60)	0 (0)	0 (0)	0 (0)	0 (0)	0 (0)	2 (20)	10 (100)
5-10%	1 (14)	2 (29)	1 (14)	0 (0)	1 (14)	0 (0)	0 (0)	2 (29)	7 (100)
10-30%	4 (15)	0 (0)	3 (19)	15 (27)	0 (0)	0 (0)	0 (0)	4 (15)	26 (100)
30-50%	0 (0)	1 (4)	4 (17)	6 (25)	5 (21)	3 (13)	0 (0)	5 (21)	24 (100)
50-100%	6 (7)	5 (6)	3 (4)	19 (22)	19 (22)	25 (29)	0 (0)	8 (9)	85 (100)
100%	0 (0)	0 (0)	0 (0)	0 (0)	2 (22)	3 (33)	2(22)	2 (22)	9 (100)
no data	3 (50)	0 (0)	0 (0)	1 (17)	0 (0)	1 (17)	0 (0)	1 (17)	6 (100)
total at priv.	499 (75)	10 (2)	7 (1)	26 (4)	24 (4)	85 (13)	9 (1)	6 (1)	666 (100)
total Jan. 1995	476 (71)	25 (4)	11 (2)	52 (8)	34 (5)	61 (9)	7 (1)	0 (0)	666 (100)
total Jan. 1996	409 (61)	23 (3)	17 (3)	49 (7)	35 (5)	50 (8)	6 (1)	77 (12)	666 (100)
total Jan. 1997	348 (52)	27 (4)	16 (2)	55 (8)	32 (5)	36 (5)	2 (0)	150 (23)	666 (100)

Figure 6.3-1 Estonia: economic performance 1997 - large sample

	state	municipal	domestic private	foreign private	total
active enterprises	206 (1)	440 (2)	25253 (91)	1728 (6)	27627 100
number of employees	43599 (11)	18664 (5)	302183(75)	38167 (9)	402613 100
average number of employees	211	42	12	22	15
net sales 1995 mill EEK	16805 (15)	3146 (3)	74205 (65)	17431 (16)	111588 100
net sales 1997 mill EEK	13489 (7)	4412 (2)	128901(71)	33816 (19)	180618 100
sales per employee 1000 EEK	309	237	427	886	449
percentage export	18%	1%	22%	31%	23%
value added mill EEK	4069 (15)	952 (3)	17981 (66)	3961 (15)	27217 100
value added per employee	93	51	60	104	68
staff cost per employee	78	58	48	80	55
total assets mill EEK	14401 (13)	6456 (6)	71494 (63)	20819 (18)	113171 100
total assets/employee ultimo	330	346	236	545	281
tangible assets/employee ult.	208	259	88	226	122
change in tangible assets before depreciation per employee	26	50	33	52	35
new tangible assets per empl.	76	87	29	59	40
new plant and equipment/empl	25	24	12	21	15
increase of fixed assets %	8	18	40	22	27
return on equity	11.5	-0.7	8.9	8.5	8.6
return on total assets	7.8	-0.4	3.2	3.4	3.7
gross profit to net sales	15.7	14.8	10.7	11.6	11.3
asset turnover	1.01	0.74	2.17	1.81	1.85
debt/equity	0.48	0.75	1.96	1.52	1.47

Based on ESA - Statistical Office of Estonia, Financial Statistics of Enterprises 1997, I.
12 148 enterprises were surveyed.
State and municipal and larger private were included 100%, while a sample was drawn from the smaller ones.
Simple averages - a few large companies have a relatively high weight.

7. The results of privatization - Latvia

7.1 The ownership structure after privatization - Latvia

Table 7.1-1 show ownership distribution for 5589 enterprises for January 1995 (Jones and Mygind, 1998). At this time most of the small privatization had been done, while most of the larger enterprises were still not privatized. The ownership distribution is quite interesting since typically one group of owners has more than 50% of the ownership and in only 2% of the enterprises did no group of owners have a majority of the ownership. Although one group could consist of a number of individuals we can take this distribution as an indication of a high degree of concentration.

In 16% of cases, enterprises were mainly owned by the state, 5% of the firms were owned by foreigners, 26% by domestic outsiders while in 51% of firms insiders owned more than 50%.

Based on a survey on managers in 167 enterprises we have evidence for the distribution between managers and other employees in companies. These results are in figure 7.1-2 used to divide the insider ownership in two groups. However, it must be noted that this procedure includes some modifications since the 73 enterprises with majority insider ownership is not a representative sample of the total. First of all they have 20 or more employees. From the small sample we can see that employee and management dominance have the same frequency for enterprises with 20 or more employees, and we assume this is also the case for the large sample.

As can be seen from figure 7.1-1 state ownership was still quite high in manufacturing in January 1995 with, the state having majority in around 24% of the enterprises. In particular, the state maintains a strong ownership stake among the largest enterprises and 54% of firms with more than 500 employees were still predominantly state owned in January 1995. This result is consistent with the time-profile of large privatization in Latvia. The state owned less than 15% of enterprises with fewer than 100 employees. These small enterprises have mainly been taken over or are started by insiders and more than 50% of companies with fewer than 100 employees are majority insider owned. More than two thirds of enterprises with 1- 4 employees were majority insider owned. For enterprises with more than 500 employees the corresponding figure is only 18. Most of the enterprises with majority insider ownership in 1995 were 100% owned by insiders. It is striking that for enterprises with 20-199 employees there are slightly more management owned enterprises than employee owned. However, for large enterprises with more than 200 employees we have no enterprises with management dominance in our small sample of 167 enterprises.

Foreign ownership are relatively low on average 5% in the large sample of 1995, but here is a clear tendency to an increasing proportion with increasing size, rising from 3% for the smallest group to 6% for the largest enterprises.

We have data also for another large sample from ultimo 1997. Here the classification of ownership is based on the code indicated by the enterprise register of Latvia. In this data foreign ownership makes up as much as 17% of the total, and again highest for the largest enterprises (24%). The difference from January 1995 to the end of 1997 is both due to an increase in foreign ownership, and some change in definitions. Some enterprises with minority foreign ownership are included in the foreign ownership group in the enterprise register..

By the end of 1997 only a very small proportion of enterprises were still state or municipal owned in sectors such as manufacturing, construction and trade (less than 6%), but public ownership was still strong in utilities sectors such as electricity, water and gaz and in the broad group of services, including branches such as health, education and liberal and social services. Foreign ownership was low in these sectors and in agriculture, but high in the other sectors.

From the 1995 data it can be seen that there is substantial dispersion in the extent of insider ownership across sectors. Insider ownership was highest in agriculture and fishing and lowest in transport and services. From the small sample it can be seen that the bulk of insider owned enterprises in agriculture and fishing were broadly owned by employees, in manufacturing there is about balance, while managers were dominating in sectors such as construction, trade and transport.

Table 7.1-1 shows some data for capital intensity, measured as nominal capital per employee. There is a similar tendency like in Estonia that enterprises with insider majority have much lower (around ten times lower) capital intensity than other enterprises. This is also confirmed by the data from the small sample. These data do not point to significant differences between management and employee dominated enterprises. Like in Estonia foreign owned enterprises and state owned enterprises have quite high capital intensity.

A distribution based on the year of privatization for the small sample is shown at the bottom of the table. However, from these results no clear tendencies can be seen, so a tendency to lower insider or lower employee ownership in later stages of privatization cannot be confirmed.

Only in the small sample of 167 enterprises we can distinguish between new started and privatized enterprises. The proportion of new started enterprises is clearly highest among the small enterprises. The division of new and privatized on different ownership groups can be seen from table 7.1-3. Although, the sample is quite small the following strong tendencies can be assumed to have general validity. Foreign ownership is mainly established as completely new entities. We assume that this is the case for small enterprises - sales outlets etc, while larger foreign owned enterprises are mainly the result of privatization. Managerial owned enterprises are dominantly started as new entities, while on the other hand broadly employee owned enterprises are mostly established in the privatization process. Note, however, that the distinction of new and privatized might not be so clear in reality since most entities categorized as new all to some extent use privatized assets. The process in which these assets were acquired can be part of the formal privatization procedure or part of more informal processes.

From the study of the 167 enterprises we have evidence about the distribution within the group of employees (Jones and Mygind, 1998). The tendency known from Estonia with a more equally distributed ownership in small enterprises cannot be confirmed in the Latvian sample. There is not a tendency for an increasing number of non-owners from 1994 to 1996 like it was the case in Estonia. For both years about one third of the employees in the sample own shares in their own enterprise. The distribution of shares among the employee is rather equal for half of the enterprises with some insider ownership and “unequal” for 25% and “very unequal” for the remaining 25%. This is the same pattern as in Estonia, but in Latvia the numbers do not show a significant variation between different size groups.

7.2 Dynamics of ownership - Latvia

The dynamics of ownership in Latvia can be examined by constructing transition matrices based on the survey of the 167 enterprises analyzed for the period 1993-1996 (Jones and Mygind, 1998). In the transition matrix shown in figure 7.2-1 the results in the end of 1994 are compared with the results ultimo 1996. We have not gone back to 1993 since the number of non-answers is as high as 28%. The enterprises were asked in 1997 about their ownership structure in the preceding four years. The reliability of the data is probably falling the further back in time we go, and there is likely to be a tendency of under reporting changes in ownership since it is simply easier to answer “unchanged” instead of specifying the changes. Even with this concern, the transition matrix do show some interesting developments. 4 companies have been privatized from 1994 to 1996. 5 out of 34 enterprises with domestic outside ownership have changed, and most markedly 7 out of 37 employee dominated insider majority have changed, 3 to management dominance, 3 to domestic ownership and one to no majority. Looking at the summary table at the bottom there is a tendency for foreign ownership, management ownership and no majority ownership to increase.

The tendency from Estonia with falling employee ownership is also reflected in the transition matrix in figure 7.2-2. The ownership is especially shifting from employees to managers like it was the case in Estonia, although there is a weaker tendency in the Latvian data. Measuring the speed of change for majority ownership (excluding changes including state and no-answers) show a change between 4% and 7% year to year, and a 18% change from 1993 to 1996. This is about half the speed of change compared to Estonia. This can probably partly be explained by a bias in the data-collection method, but it also indicates a more open and dynamic market for ownership in Estonia. (In fact, an analysis of 694 enterprises on ownership in 1994 and 1995 without division of the group of insiders in managers and other employees, show that the ownership change is 7.6% compared to 3.7% in the small sample of 167 enterprises, (Jones and Mygind, 1998)).

Still the general picture is a quite low degree of change. This is confirmed by the data from the large sample with broad owner groups based on the enterprise-register categorization, figure 7.2-3. Although the matrix covers a period of three years the change between groups are very small. Most markedly, the privatization process is cutting the number of state owned enterprises by 20%. 14 out of the 100 going from state to other forms become foreign owned. Foreign owned companies have taken over 51 firms from the private domestic enterprises and have sold 20 the other way. The number of foreign owner enterprises has increased by 20% over the 3 years through privatization and takeovers. On top of this come new established enterprises for which we do not have any numbers. Here we find probably a more important contributor to the increase in the number of foreign enterprises, while a few large privatizations make this the most important road for foreign ownership when measured as the value of the assets.

Figure 7.2-4 shows a matrix for the dynamics during 1997. Again the low dynamics is striking. However, it should be noted that the main dynamics is excluded, because of the broad categorization of the group of private domestic enterprises. As shown before the main dynamics takes place within this group, namely, as management take-over of the majority from the broad group of employees.

Finally, the matrix for the dynamics of foreign ownership during 1997, figure 7.2-5, shows the stability of ownership structures. There are 54 cases with foreign ownership shifting to a higher category and 35 cases going in the opposite direction. In the upward direction, 5 cases are jumping from 0% to majority foreign ownership, while 10 cases takes the smaller step from 30-50% to majority. In fact, the shifts in the matrix, shows that a process of a gradual takeover by foreigners is more frequent than one-step takeovers.

7.3 Ownership and some indicators of economic performance - Latvia

Figure 7.3-1 and -2 gives some indicators of the performance of 1997 for the large sample, but only for quite broad ownership groups. Further information on insider ownership for the early period is taken from Mygind 1997a.

As earlier mentioned for the initial condition around privatization we found that insider owned enterprises, and especially manager-owned enterprises have a quite low capital intensity, while foreign owned enterprises on the other hand have a very high capital intensity. Insider owned enterprises tend to be relatively small. We do not have any information about profitability before 1994.

Growth in sales for 1997 is like in Estonia highest for foreign enterprises, and private are higher than state.

A multivariate analysis based on the early data show that labor-adjustment in Latvia are considerably lower than in Estonia and Lithuania. Only foreign ownership show some more dynamic adjustments (Jones, Mygind and Rahman 1996). Foreign owned enterprises have the highest growth in employment in 1997, and private is higher than state (figure 7.3-2).

Production function analysis based on cross sections from 1994 and 1995 do not show any significant differences in factor productivity between ownership groups (Jones and Mygind, 1999b). However, the 1997-data show that labor productivity is much higher for foreign owned enterprises than it is the case for the remaining groups, see figure 7.3-2.

For the 1997-data the wage level is like in Estonia clearly the highest in foreign owned enterprises, while other private enterprises are lower than state owned enterprises, see table 7.3-2. We have not yet results on the wage level in insider owned enterprises.

The profitability measures from 1997, figure 7.3-2 show that private enterprises have higher profit margins than state owned (but there are no big variation within the group). However, foreign enterprises are doing worse than their domestic counterpart on return on assets. This result is confirmed on multivariate analysis on earlier data. Like in Estonia, foreign owned companies cannot in this stage report profits following the relatively high level of assets. The highest returns on assets are found in enterprises with insider majority (Mygind 1997a p. 37).

Looking at the capital structure a multi-variate analysis for the 1995 data show that the debt ratio for insider-owned enterprises is significantly higher than for state owned enterprises. Bank loans is, however, significantly lower the more insiders own, and bank loans per employee are relatively low for insider owned enterprises (Mygind 1997 p. 40). Figure 7.3-1 shows that the private enterprises in general have a higher debt/equity ratio than state owned enterprises and that foreign owned have a slightly lower ratio than other private enterprises. However, foreign enterprises have the highest bank loans per employee and also slightly higher access to long term loans than the other companies.

The 1997 data show that netinvestment per employee is the highest in foreign owned enterprises and private is higher than state, figure 7.3-2. Analysis on earlier data shows the same tendency, and shows also that insider tend to be higher than outside domestic owned enterprises (Mygind 1997a, p. 41).

Appendix 7.

Figure 7.1-1 Latvia: Ownershipstructure, January 1, 1995
size, branches, capital intensity

frequency (row percent)	**Majority**						**no majo-rity**	**total**
	State	**outsiders**		**insiders**				
		foreign>dom	domestic>f	total	managers>e	employees>m		
TOTAL	895 (16)	279 (5)	1464(26)	2838 (51)	36 (25)*	37 (25)*	113 (2)	5589 (100)
EMPLOYEES								
1-4	47 (6)	23 (3)	161 (21)	528 (67)	-	-	26 (3)	785 (100)
5-19	196 (15)	62 (5)	332 (25)	681 (52)	-	-	38 (3)	1311 (100)
20-99	366 (14)	141 (5)	693 (27)	1343 (52)	(29)*	(23)*	44 (2)	2587 (100)
100-199	119 (24)	28 (6)	160 (32)	193 (39)	(22)*	(17)*	3 (1)	503 (100)
200-	165 (41)	25 (6)	118 (29)	93 (23)	(0)*	(23)*	2 (0)	403 (100)
average	215	70	74	45	64*	182*	31	
25% quartile	17	16	13	7	25*	38*	5	
50% median	52	33	33	23	40*	83*	17	
75% quartile	145	76	77	44	102*	184*	36	
BRANCHES								
agricult. fishing	72 (12)	5 (1)	124 (20)	406 (67)	(11)*	(56)*	2 (0)	609 (100)
mining wood	93 (19)	29 (6)	101 (20)	269 (54)	(27)*	(27)*	7 (1)	499 (100)
manufacturing	130 (22)	36 (6)	92 (16)	310 (53)	(32)*	(21)*	12 (2)	580 (100)
manufacturing	51 (26)	13 (7)	19 (10)	108 (55)	(14)*	(41)*	4 (2)	195 (100)
construction	102 (13)	15 (2)	180 (24)	455 (60)	(43)*	(17)*	7 (1)	759 (100)
trade	217 (14)	105 (7)	379 (24)	825 (52)	(39)*	(13)*	47 (3)	1573 (100)
transport	75 (20)	49 (13)	112 (30)	130 (34)	(34)*	(0)*	11 (3)	377 (100)
service	153 (15)	27 (3)	453 (46)	332 (34)	-	-	23 (2)	988 (100)
nominal capital /employee 1000 lat								
average	5289	6568	5170	477	488*	630*	3696	2846
25% quartile	380	125	99	7	4*	58*	13	20
median	1663	1137	538	35	90*	195*	100	165
75% quart.	3965	5333	2240	211	1035*	650*	625	1200
year of privatization								
1991	8 (26)*	2 (6)*	3 (10)*	14 (35)*	7 (23)*	7 (18)*	4 (13)*	31 (100)*
1992	0 (0)*	4 (7)*	15 (27)*	35 (64)*	17 (31)*	18 (33)*	1 (2)*	55 (100)*
1993	4 (10)*	4 (10)*	14 (35)*	17 (43)*	7 (18)*	10 (25)*	1 (2)*	40 (100)*
1994	4 (29)*	1 (7)*	2 (14)*	7 (50)*	5 (36)*	2 (14)*	0 (0)*	14 (100)*
total	16 (11)*	11 (8)*	34 (24)*	73 (52)*	36 (26)*	37 (26)*	6 (4)*	140 (100)*

* the numbers are based on the sample of 167 enterprises with 20 or more employees, percentages are normalized so the total equals insiders total, numbers for employees and nominal capital cannot be

directly compared with other ownership groups.

Figure 7.1-2 Latvia: Ownershipstructure (register class.*), ult 1997
size, branches, year of registration

	State	coop	private	foreign	total
EMPLOYEES					
1997 total N	653 (18)	152 (4)	2196 (60)	632 (17)	3633 (100)
0-19	33 (5)	33 (5)	466 (72)	136 (21)	648 (100)
20-99	386 (18)	101 (5)	1360 (62)	330 (15)	2177 (100)
100-199	118 (25)	23 (5)	251 (52)	87 (18)	579 (100)
200-	116 (35)	15 (5)	119 (36)	79 (24)	329 (100)
average	211	84	66	116	101
25% quartile	37	30	22	22	25
50% median	67	51	38	47	43
75% quartile	140	100	70	107	89
BRANCHES	653 (18)	152 (4)	2196 (60)	632 (17)	3633 (100)
agricult. fishing	19 (7)	49 (18)	197 (72)	9 (3)	274 (100)
mining wood	3 (10)	1 (3)	18 (60)	8 (27)	30 (100)
manufacturing	55 (6)	25 (3)	650 (68)	229 (24)	959 (100)
El., water, gas	70 (90)	1 (1)	7 (9)	0 (0)	78 (100)
construction	11 (3)	1 (0)	332 (87)	38 (19)	382 (100)
trade	13 (2)	46 (6)	543 (70)	176 (23)	778 (100)
hotels restaur.	12 (14)	1 (1)	47 (57)	23 (28)	83 (100)
transport	48 (18)	6 (2)	144 (55)	62 (24)	260 (100)
service	422 (48)	22 (3)	258 (30)	87 (10)	789 (100)
year of registration	643 (18)	152 (4)	2196 (61)	632 (17)	3623 (100)
- 91					
1991	167 (23)	0 (0)	476 (65)	93 (12)	736 (100)
1992	95 (12)	78 (10)	532 (65)	119 (14)	824 (100)
1993	108 (14)	55 (7)	442 (59)	149 (20)	754 (100)
1994	97 (16)	10 (2)	342 (58)	140 (24)	589 (100)
1995	74 (22)	4 (1)	184 (54)	76 (22)	338 (100)
1996	45 (18)	3 (1)	167 (67)	36 (14)	251 (100)
1997	57 (44)	2 (2)	53 (40)	19 (15)	131 (100)

Table 7.1-3 Ownership on privatization/new - 1996

\majority ownership	state	foreign	domestic	manager	em-ployee	no majority	no answer	total
Privatized	0	3	21	18	26	4	1	73
new started	0	10	14	32	5	10	0	71
state owned ultimo 1996	20	0	0	0	0	0	0	20

Based on a survey of 167 enterprises performed spring 1997, (Mygind 1999)

Figure 7.2-1 Transition matrix Latvia - ultimo 1994 by ultimo 1996

majority ultimo 1994	Majority ultimo 1996					No Majo-rity	no answer	total
	State	outsiders		insiders				
		foreign	domestic	managers	employees			
State	12 (75)	1 (6)	0 (0)	2 (13)	0 (0)	1 (6)	0 (0)	16 (100)
Outsider Foreign>domestic	0 (0)	10 (91)	0 (0)	1 (9)	0 (0)	0 (0)	0 (0)	11 (100)
Outsider Domestic>foreign	0 (0)	1 (3)	29 (85)	2 (6)	1 (3)	1 (3)	1 (3)	34 (100)
Insider Managers>employees	0 (0)	0 (0)	0 (0)	36 (100)	0 (0)	0 (0)	0 (0)	36 (100)
Insider Employees>managers	0 (0)	0 (0)	3 (8)	3 (8)	30 (81)	1 (3)	0 (0)	37 (100)
no majority	0 (0)	0 (0)	0 (0)	0 (0)	0 (0)	6 (100)	0 (0)	6 (100)
no answer	1 (4)	1 (4)	2 (7)	0 (0)	2 (7)	1 (4)	20 (74)	27 (100)
Total 1993	15 (9)	7 (4)	29 (17)	29 (17)	34 (20)	6 (4)	47 (28)	167(100)
Total 1994	16 (9)	11 (7)	34 (20)	36 (22)	37 (22)	6 (4)	27 (16	167(100)
Total 1995	14 (8)	13 (8)	35 (21)	38 (23)	35 (21)	9 (5)	23 (14)	167(100)
Total 1996	13 (8)	13 (8)	34 (20	44 (26)	33 (20)	10 (6)	20 (12)	167(100)

Figure 7.2-2 Latvia - employee ownership ultimo 1994 by ultimo 1996

Ultimo 1994	Ultimo 1996							no data	total
Employeeshares	**0%**	**0-5%**	**5-10%**	**10-30%**	**30-50%**	**50-100%**	**100%**		
0%	60 (94)	0 (0)	0 (0)	2 (3)	1 (2)	1 (2)	0 (0)	0 (0)	64 (100)
0-5%	1 (13)	4 (50)	0 (0)	2 (25)	1 (13)	0 (0)	0 (0)	0 (0)	8 (100)
5-10%	0 (0)	1 (17)	4 (67)	1 (17)	0 (0)	0 (0)	0 (0)	0 (0)	6 (100)
10-30%	2 (12)	1 (6)	2 (12)	12 (71)	0 (0)	0 (0)	0 (0)	0 (0)	17 (100)
30-50%	0 (0)	0 (0)	0 (0)	2 (22)	6 (67)	1 (11)	0 (0)	0 (0)	9 (100)
50-100%	0 (0)	0 (0)	0 (0)	4 (12)	3 (92)	27 (79)	0 (0)	0 (0)	34 (100)
100%	0 (0)	0 (0)	0 (0)	0 (0)	0 (0)	0 (0)	1 (50)	1 (50)	2 (100)
no data	4 (15)	0 (0)	0 (0)	1 (4)	0 (0)	2 (7)	0 (0)	20 (74)	27 (100)
total ult. 1993	53 (32)	5 (3)	6 (4)	15 (9)	9 (5)	30 (18)	2 (1)	47 (28)	167 (100)
total ult. 1994	64 (38)	8 (5)	6 (4)	17 (10)	34 (5)	34 (20)	2 (1)	27 (16)	167 (100)
total ult. 1995	67 (40)	9 (6)	4 (2)	20 (12)	35 (5)	32 (19)	2 (1)	23 (14)	167 (100)

total ult. 1996	67 (40)	6 (4)	6 (4)	24 (14)	11 (7)	32 (19)	1 (1)	20 (12)	167 (100)

Figure 7.2-3 Latvia - transition-matrix - owner-categories 1994 on 1997

Majority Jan. 1997 Majority Jan. 1994	**state**	**coop**	**private domestic**	**foreign**	**mix**	**Total**
State	382 (79)	0 (0)	73 (15)	14 (3)	13 (3)	482 (100)
Coop	0 (0)	123 (95)	6 (5)	0 (0)	0 (0)	129 (100)
Private domestic	0 (0)	1 (0)	944 (95)	51 (5)	2 (0)	998 (100)
Foreign	0 (0)	0 (0)	20 (9)	199 (88)	7 (3)	226 (100)
Mix	3 (3)	1 (1)	71 (70)	9 (9)	17 (17)	101 (100)
Total	385 (20)	125 (6)	1114 (58)	273 (14)	39 (2)	1936(100)

Based on enterprise register categorization by Latvian Statistical Bureau

Figure 7.2-4 Latvia transition-matrix majority primo 1997 by ultimo 1997

Majority ultimo Majority primo 1997	**state**	**coop**	**private domestic**	**foreign**	**No majority**	**total**
State	564 (94)	1 (0)	30 (5)	5 (1)	1 (0)	601 (100)
Coop	0 (0)	35 (92)	1 (3)	2 (5)	0 (0)	38 (100)
Private domestic	7 (0)	1 (0)	2405 (99)	13 (1)	3 (0)	2429(100)
Foreign	0 (0)	0 (0)	7 (2)	321 (97)	2 (0)	330 (100)
No majority	0 (0)	0 (0)	0 (0)	1 (14)	6 (86)	7 (100)
Total	571 (17)	37 (1)	2443 (72)	342 (10)	12 (0)	3405(100)

Based on balance-sheet data primo and ultimo 1997. 16 categorized as "other" have been excluded

Fig. 7.2-5 Latvia - foreign ownershare primo 1997 by ultimo 1997

Ultimo Primo	**0%**	**1-10%**	**11-30%**	**31-50%**	**51-100%**	**100%**	**total**
0%	2789 (99)	5 (0)	10 (0)	8 (0)	5 (0)	0 (0)	2817(100)
1-10%	1 (3)	26 (90)	0 (0)	1 (3)	1 (3)	0 (0)	29 (100)
11-30%	2 (4)	4 (7)	43 (80)	3 (6)	2 (4)	0 (0)	54 (100)
31-50%	3 (2)	3 (2)	7 (5)	128 (84)	10 (7)	2 (1)	153 (100)
51-100%	2 (1)	0 (0)	0 (0)	5 (2)	212 (94)	7 (3)	226 (100)

100%	1 (1)	1 (1)	0 (0)	2 (1)	5 (4)	133 (94)	142 (100)
Total	2798 (82)	39 (1)	60 (2)	147 (4)	235 (7)	142 (4)	3421(100)

Based on balance sheet data

Fig. 7.3-1 Latvia: Ownership (register class.*), ult. 97 capital-structure

	state	coop	private	foreign	total
Equity N /employee **1000 lat**	648	141	1828	520	3137
average	3560	2133	3870	13536	5330
25% quartile	405	820	797	2057	765
50% median	987	1258	1638	5107	1703
75% quartile	2483	13984	3447	14179	4143
total assets/ N **employee** **1000 lat**	648	141	1828	520	3137
average	14138	8174	6611	24256	11161
25% quartile	1483	1800	1577	4076	1759
50% median	3842	3020	3087	9544	3746
75% quartile	11230	4574	6382	21037	8992
short/to.loan	645	151	2181	631	3608
average	0.89	0.89	0.80	0.75	0.81
5% quantile	0.22	0.30	0.17	0.08	0.15
10% quantile	0.47	0.56	0.30	0.17	0.30
25% quartile	0.99	0.91	0.62	0.56	0.67
50% median	1.00	1.00	1.00	0.97	1.00
debt/equity N	647	151	2195	632	3625
average	0.65	0.69	0.44	9.35	2.04
25% quartile	0.05	0.14	0.29	0.15	0.16
50% median	0.18	0.43	1.12	0.92	0.73
75% quartile	0.54	0.99	3.24	2.38	2.37
90% quartile	1.88	1.89	9.03	6.57	7.23
95% quartile	3.96	2.36	19.57	12.48	14.43
Bankcredits N /employee **1000lat**	93	56	629	189	967
average	2947	380	2302	6534	3080
25% quartile	74	109	165	245	158
50% median	401	202	571	1011	577
75% quartile	2336	382	1693	4074	1936

Figure 7.3-2 Latvia: Ownership (register class.*) ultimo 97 - performance

	state	coop	private	foreign	total
Value added/ Employee 1000 lat	491	135	1764	487	2877
Average	2194	1760	2977	7245	3509
25% quartile	825	918	967	1752	985
50% median	1404	1645	1703	3773	1789
75% quartile	2316	2550	3218	8624	3531
sales growth N	441	130	1628	466	2665
average %	47	7	37	53	40
25% quartile	-7	-19	-5	4	-6
50% median	9	-3	16	25	15
75% quartile	29	12	53	67	49
Profitmargin N	493	146	2125	597	3361
Average %	-3	10	11	10	9
25% quartile	-6	3	3	5	3
50% median	4	10	10	13	10
75% quartile	16	21	19	26	19
Return on assets	485	142	2125	599	3351
Average %	-2	4	13	7	9
25% quartile	-4	-4	3	-4	-1
50% median	0	1	8	6	5
75% quartile	4	6	24	20	20
90% quantile	15	17	47	38	41
95% quantile	24	21	64	54	59
salary per N employee 1000 lat	648	141	1828	520	3137
average	1413	892	1056	2009	1280
25% quartile	937	626	584	924	690
50% median	1152	849	869	1565	1017
75% quartile	1586	1076	1320	2555	1520
netinvestmentN /employee 1000lat	648	141	1828	520	3137
average	1262	89	951	4383	1546
25% quartile	-31	-124	-100	-66	-85
50% median	116	32	157	622	167
75% quartile	446	331	806	3475	857
90% quantile	1696	829	2589	9489	3232
95% quantile	2978	1159	4936	19114	6550
growth in N employment%	581	138	1739	501	2959
average	12	13	18	25	18
25% quartile	-7	-14	-8	-4	-8
50% median	0	-3	2	9	2
75% quartile	7	5	21	30	18
90% quantile	25	26	58	64	55
95% quantile	51	114	107	103	98

8. Results of privatization - Lithuania

8.1 The ownership structure after privatization

The following presentation is based on a small data set of around 350 enterprises in manufacturing with detailed ownership data 1994-1996 and around 150 enterprises in construction and trade with data for 1995-96 (Jones and Mygind 1998). Furthermore, we have a large data set of 6-7000 enterprises for 1996 and 1997 with some ownership information. We have financial information for all these enterprises collected by the Statistical Department of Lithuania. The data do not distinguish between private new-started and privatized enterprises. The data covers mainly enterprises with 20 or more employees. We assume that most of the large private enterprises are privatized.

The first ownership survey, undertaken in July 1994, elicited responses from 356 industrial enterprises. It confirms to some extent the rapid extension of insider ownership in large enterprises in Lithuania. By July 1994 only 8% of these enterprises had no insider ownership and most of these 25 enterprises were still state owned. 25% of the enterprises had 31-50% insider ownership, and 18% of the enterprises had majority insider ownership. Most of these enterprises have more shares owned by the employees than by managers. In July 1994 in only 13% of cases with some insider ownership did managers own more equity than do the rest of employees. This result shows a strong difference from the Estonian data where managers owned more than the other employees in most cases.

The survey data also indicate that ownership by foreigners plays a limited role in Lithuania. Only 6 of the manufacturing enterprises were owned by outsiders dominated by foreign investors, see table 8.1-1. Some of the 4 enterprises privatized to foreigners in the "hard currency privatization" are probably included here. A few of the foreign enterprises in the sample can also be new or taken over by foreigners short after privatization.

As can be seen from table 8.1-1, 15% of the industrial enterprises had insider majority with employee dominance and only 3% had insider majority with manager dominance in July 1994. As the entries in the lower rows of figure 17 indicate, the degree of employee-ownership in July 1994 is not dependent on the time of privatization. The difference in relation to the distribution of ownership at the time of privatization is probably the result of two tendencies from the privatization date to July 1994 - a gradual takeover by employees through enterprise reserves and profits, and secondly the sale of some employee shares, with the strongest effect in enterprises where employees owned a high proportion of the shares. The proportion of "no majority" is quite high in general and especially in enterprises privatized in 1993 and 1994. This can be explained by the state still keeping a relatively high proportion of shares especially in the larger enterprises.

The Lithuanian industry sample consists of rather large enterprises with an average employment in 1994 of 600 employees. Manager dominated insider majority has the largest average, but the data do not reveal striking differences in the size-structure. There are also no clear tendencies among the industrial branches shown in table 8.1-1.

The survey for construction was not undertaken before July 1995, but the results show many of the same tendencies as in industry. Out of 148 enterprises only 6% had no employee ownership in July 1995, and 40% had majority insider ownership, table 8.1-2. However, for construction and trade there are more enterprises with insider majority which have management dominance, 26%, compared to employee dominance, 14%. However, this difference from the tendency in industry partly reflects the fact that the numbers for construction and trade are from July 1995. Leaving one more year for the change of ownership from employees to managers. There are no striking tendencies in the variation of ownership when comparing enterprises of different sizes except for a weak tendency for higher management dominance in smaller companies. Comparing construction and trade there are about the same degree of employee ownership. However, managers are stronger in trade with 29% of the sample with insider majority with manager dominance. In construction the percentage is 23%.

The large sample of enterprises with ownership data from January 1998 represents all branches and for large enterprises we have full coverage. The ownership structure is based on dominant owner, that is the largest owner group out of the five given in the table. However, there is not much difference since in most cases the dominant owner has a majority of the shares.

Comparing tables 8.1-1, -2 and -3 it can be seen that the state owned enterprises has fallen from 20% to 10%, construction from 12% to 6% while trade already in 1995 were down at a level of 6%. State ownership is still quite high in enterprises related to agriculture and fishing, in service and in water supply.

The group, domestic persons, covers both domestic outsiders and insiders. We assume that most of the enterprises in this category are insider owned. Ownership by domestic enterprises makes up 7%, and out of these is 2% of the total dominated by owners representing financial enterprises. Ownership by banks and investment funds play a rather limited role in Lithuania, however, for large enterprises with more than 100 employees this group represents 4% of the enterprises. Financial owners dominated 4% of the manufacturing enterprises. This percentage was lower for other branches. Foreign owners dominated in 8% of the enterprises, slightly more in small than in large enterprises, and slightly more in mining and wood, manufacturing and trade than in other branches.

Looking at the capital structure for the data from the early years the most striking difference between the different owner groups in industrial enterprises is the fact that insider owned and especially employee owned enterprises have a relatively low nominal capital or equity per employee, see table 8.1-1. It is the same tendency although not so strong as in Estonia. State owned, foreign owned and no majority companies have relatively high capital intensity. Turning to construction and trade there is another pattern with insider owned companies around the average of nominal capital per employee. Only management dominated enterprises have a slightly lower nominal capital per employee. Looking at the total assets per employee, however, insider owned companies in all the analyzed sectors follow to a high degree the pattern of the average enterprise. This might indicate that in industry insiders and especially managers have been able to get a majority of the shares at a relatively low price. It fits well to the fact, that insiders had the first bid at the initial price.

For the 1998 data in the large sample the group of domestic persons including insider ownership we again find the lowest capital intensity. This is especially the case for equity per employee indicating that this group has taken over assets at a relatively low price. However, there might be the same tendency for foreign owned enterprises with quite low equity per employee and the highest asset value per employee.

The number of non-owners among employees in the Lithuanian sample is relatively low compared to the other countries (Jones and Mygind, 1998). 75% of the employees in the sample were owners in July 1994. For the management staff the corresponding percentage were as high as 87%. This low percentage of non-owners among the employees suggests that the Lithuanian voucher system has helped employees as a group to overcome the problem of lack of capital. There is also a tendency for the percentage of non owners to be higher in large enterprises than in smaller, the opposite result of the situation in Estonia. Finally, table 8.1-3 shows a strong tendency for almost all categories of an increasing share of non-owners. In total for both manufacturing, construction and trade the share of owners fall to 61% in July 1996.

Figure 8.1-4 show the share of foreign ownership in different ownership groups. In 174 or 3.3% of the enterprises dominated by domestic persons there is a minority holding of foreign capital. The similar number for ownership by financial enterprises is 6.6% and by non financial enterprises 12.4%. For state enterprises the numbers are 2.6%. Domination by foreigners is made by 50% or less of the share capital in 94 enterprises and by a clear majority in 496 enterprises.

Figure 8.1-5 shows the share of ownership by financial enterprises in different ownership groups. In 196 or 3.7% of the enterprises dominated by domestic persons there is a minority holding owned by financial enterprises. The similar number for ownership by non financial enterprises is 6.8%. For state enterprises the numbers are 3.3% and for foreign dominated enterprises 4.4%. Domination by financial enterprises is made by 50% or less of the share capital in 27 enterprises and by a clear majority in 124 enterprises.

8.2 Dynamics of ownership - Lithuania

The dynamics of ownership is illustrated through the transition matrices shown in the figures 8.2-1-7 . Figure 8.2-1 for industry shows a strong tendency of a fall in the number of enterprises with majority insider ownership and employee dominance. The number is more than halved from July 1994 to July 1995. From July 1994 to July 1996, 40% of the 53 employee owned enterprises have changed to outside domestic ownership, 19% to no majority and 6% to management ownership. A few enterprises have changed to more employee ownership. Most of these changes took place from 1994 to 1995. It is worth noting that there do not seem to be the same tendency in Lithuania as in Estonia with stability for employee ownership in small enterprises. All size groups show a steep fall from 1994 to 1996. Outside ownership has increased both for foreign ownership which increased from 6 to 18 and domestic ownership which increased from 124 to 168. The number of industrial enterprises with insider majority with management dominance is relatively stable. However, only 4 or 33% have stayed in this category for both 1994 and 1996. In total the Lithuanian industrial enterprises show very dynamic changes. About 40% of the enterprises (excluding no answers) have changed category in the period of two years.

For construction and trade 18% of the enterprises have changed category during one year from July 1995 to July 1996, figure 21. Employee dominated insider owned enterprises seem to be more stable than in industry. However, in the same period from 1995 to 1996 employee ownership was also rather stable in industry. In construction and trade the number falls from 20 to 18. Most changes are recorded for no majority enterprises falling from 24 to 18 with most enterprises going to domestic outside ownership. The number of foreign owned enterprises increases from 0 to 2.

The transition matrices in figure 8.2-3 and figure 8.2-4 show the strong tendency away from employee ownership. For the industrial enterprises in figure 8.2-3, only 23 are shifting to more, while 137 are shifting to lower employee ownership and 139 are unchanged - a rate of change of 54%. There is especially a strong change away from majority employee ownership falling from 30 to 8 and enterprises with 30-50% employee ownership falling from 79 to 42. The categories with low employee ownership are increasing. A similar tendency can be observed in figure 8.2-4 with enterprises in construction and trade. 7 enterprises have had increasing, 31 falling, and 101 have had constant employee ownership in the period July 1995 to July 1996, a rate of change of 27%. For industrial enterprises there is from July 1994 to July 1995 a tendency for increasing management ownership (56 up, 36 down and 208 constant, a rate of change of 31%) while in the following year from 1995 to 1996 there is stability with 33 up, 31 down and 231 constant, 22% rate of change. The stability from 1995 to 1996 is also seen for management ownership in the sample for construction and trade with 14 up, 13 down and 112 constant, 19% rate of change.

We do not have so detailed ownership information after July 1996. However, we can combine most of the enterprises from the small sample with the large sample like it is done in figure 8.2-5 showing some developments in ownership for the period July 1996 to ultimo 1997. For the large sample figure 8.2-6 shows the dynamics during the year 1997. Both figures show relatively low dynamics. The privatization is evident in both figures. The strange movements from private to state might be tax-arrears converted to shares. Foreign dominance is especially increasing by takeovers of private domestic enterprises, and foreign dominance is increasing with 12% in 1997. A more detailed picture of the development in the foreign ownership shares can be seen in figure 8.2-7 showing that foreign takeovers is often a gradual process

8.3 Ownership and some indicators of economic performance

We have data for the small sample for the early years 1992-1995 and for the large sample for 1996 and 1997. Management ownership had a higher incidence in small enterprises, but employee ownership had a quite high frequency both in small and large enterprises. The data for the very early years do not indicate a bias in direction of low capital-intensity for insider owned enterprises as was the case in Estonia and Latvia. In Lithuania high captial intensity has not blocked takeovers by employees, because vouchers combined with a preferential price favored the group of employees. There does not seem to be a selection bias according to profitability (Mygind 1997a p. 37).

Early data from 1993-94 show that the highest growth of sales (lowest decrease) is found in foreign owned enterprises, but also management owned enterprises are doing better than the rest while employee owned enterprises follows the average, domestic outside owned enterprises are below the average (Mygind 1997a). These results fits well with the 1997 data, figure 8.3-2. Foreign owned enterprises have again the highest growth in sales. Enterprises owned by domestic persons are also doing relatively well, while enterprises owned by domestic enterprises, especially those with financial ownership, are underperforming.

The early data on employment adjustment give some indicators of a somewhat hesitant adjustment process in employee-owned enterprises (Mygind 1997 p. 33). For the 1997 data the growth in employment is negative for the median enterprise owned by state or domestic enterprises. Employment is constant for the median domestic owned enterprise, but growing 8% for the median of foreign owned companies.

A cross section analysis on factor productivity levels for the early data show no clear tendencies of variation between owner groups (Jones and Mygind 1999b). Averages for the early data indicates that insider owned enterprises have quite high labor-productivity (Mygind 1997, p.34). The results from the large sample show that foreign owned enterprises have the highest labor-productivity for the year 1997, while enterprises owned by domestic companies, especially financially owned, have low labor-productivity, see table 8.3-2.

For the early data foreign owned enterprises have clearly the highest wage-level, but also employee owned enterprises have for 1994 a wage level above the average (Mygind 1997 p. 36). In the 1997 data foreign owned enterprises have higher salary per employee than the average, enterprises owned by domestic persons are lower than the average, see figure 8.3-2.

In the early data employee owned enterprises are doing well compared to other groups both in relation to profit margin and return on assets. Management owned enterprises are around the average (Mygind 1997, p 38). Foreign owned enterprises have quite low return on asset. For the 1997 data the return on assets is relatively high for both foreign owned enterprises and enterprises owned by domestic persons. For domestic persons, however, this is partly due to the quite low value of assets. The profit-margin is somewhat lower than for foreign dominated enterprises.

The early data confirms the observations from Estonia and Latvia that insiders have relatively low bank loans (Mygind 1997, p 40). The data for the capital structure in the large Lithuanian sample ultimo 1997, figure 8.3-1, show that foreign owned enterprises have the highest debt/equity ratio. Surprisingly enterprises dominated by domestic financial companies have a relatively low debt equity, only state owned enterprises have a lower ratio, while enterprises owned by domestic persons are higher than the average. Most of this debt is short run loans for all the domestic firms, while for most of the foreign companies long loans is higher than short loans for most of the enterprises. Bank loans are quite rare, the median for bank loans per employee is 0 for all owner groups. Domestic financial enterprises have the highest proportion of enterprises with bank loans - state owned enterprises and firms owned by domestic persons are on the low side, while also enterprises dominated by foreigners and by domestic non financial enterprises are higher than the average.

The 1994 data on investments per employee show that employee- and management owned enterprises have relatively low investment levels, while foreign and domestic outside-owned enterprises are higher than the average (Mygind, 1997 p. 41). The 1997 data show that enterprises with high investment are mainly found in the groups owned by foreigners and by domestic persons. Most of the state owned enterprises and enterprises owned by other enterprises have negative netinvestment, see figure 8.3-2.

In general the 1997-data shows that enterprises dominated by financial ownership have low growth in sales, low productivity and negative netinvestment. This indicates that many of these enterprises have been taken over by banks because of economic problems. Financial enterprises do not seem to have a strong role as owners in Lithuania. On the other hand financial take-overs of firms in economic crisis can be taken as an indicator that creditors try to enforce financial discipline through such takeovers. In this way financial enterprises can play an important role for corporate governance by enforcing their rights as creditors.

Appendix 8.

Figure 8.1-1 Lithuania: Ownershipstructure July 1994, industry - size, capital intensity, time of privatization.

frequency / row percent	**Majority**					**no majo-rity**	**no an-swer**	**total**
	State	**outsiders**		**insiders**				
		foreign>dom	domestic>f	managers>e	employees>m			
TOTAL	70 (20)	6 (2)	124 (35)	12 (3)	53 (15)	60 (17)	31 (9)	356 (100)
EMPLOYEES	1						6	7
5-19	1 (33)	0 (0)	0 (0)	1 (33)	0 (0)	0 (0)	1(33)	3 (100)
20-99	15 (32)	0 (0)	11 (23)	0 (0)	4 (9)	3 (6)	14(30)	47 (100)
100-199	15 (18)	0 (0)	36 (44)	1 (1)	12 (15)	15 (18)	4 (5)	83 (100)
200-499	18 (18)	2 (2)	38 (37)	2 (2)	19 (19)	21 (21)	3 (3)	103 (100)
500-	20 (18)	4 (4)	39 (35)	8 (7)	18 (16)	21 (19)	3 (3)	113 (100)
average 1994	496	753	616	1092	639	657	333	601
25% quartile	113	401	168	418	207	194	70	153
median	221	750	327	798	322	311	94	304
75% quartile	596	1084	753	1831	737	793	131	722
BRANCHES							3	3
mining, wood	41 (24)	2 (1)	40 (23)	5 (3)	30 (17)	43 (25)	14 (8)	175 (100)
manufacturing	18 (14)	3 (2)	62 (48)	4 (3)	17 (13)	14 (11)	10 (8)	128 (100)
manufacturing	11 (22)	1 (2)	22 (44)	3 (6)	6 (12)	3 (6)	4 (8)	50 (100)
assets/employee								
average 1994	29867	32838	16699	31853	20664	27689	21380	23002
25% quartile	9996	18876	8545	12006	9141	14872	4505	9083
median	22232	32004	13217	24730	17096	21815	8394	16856
75% quart.	37712	39881	20711	51948	26427	28731	24638	27345
equity/employee								
average 1994	8669	5839	2769	2403	1895	7424	-	4695
25% quartile	768	1738	503	315	386	678	-	497
median	3290	3986	1319	1529	738	2698	-	1524
75% quart.	8571	8714	3071	4398	1733	5566	-	4236
year of privatization								
1991 (own 94)	0 (0)	0 (0)	3(100)	0 (0)	0 (0)	0 (0)	0 (0)	3 (100)
1992 (own 94)	0 (0)	0 (0)	56 (70)	0 (0)	14 (18)	8 (10)	0 (0)	78 (100)
1993 (own 94)	2 (2)	2 (3)	42 (50)	7 (8)	9 (11)	21 (25)	0 (0)	83 (100)
1994 (own 95)	1 (1)	3 (4)	34 (49)	0 (0)	7 (10)	21 (30)	4 (6)	70 (100)
1995 (own 96)	3(20)	0 (0)	7 (47)	1 (7)	3 (20)	1 (7)	0 (0)	15 (100)
total	6	5	142	8	33	51	4	249 (100)

Figure 8.1-2 Lithuania: Ownership structure July 1995, construction and trade, size, capital intensity, time of privatization.

Frequency row percent	Majority					no majority	no answer	total
	State	outsiders		insiders				
		foreign>dom	domestic>f	managers>e	employees>m			
TOTAL	13 (9)	0 (0)	50 (34)	37 (26)	20 (14)	24 (17)	1 (1)	145 (100)
EMPLOYEES								5
5-19	1 (17)	0 (0)	1 (17)	2 (33)	1 (17)	1 (17)	0 (0)	6 (100)
20-99	3 (6)	0 (0)	20 (37)	16 (30)	7 (13)	8 (15)	0 (0)	54 (100)
100-199	5 (12)	0 (0)	15 (37)	9 (22)	3 (7)	9 (22)	1 (3)	41 (100)
200-	3 (8)	0 (0)	11 (28)	9 (23)	9 23)	6 (15)	0 (0)	39 (100)
average	151	-	134	173	214	173	383	165
25% quartile	78	-	65	72	73	48	-	68
median	136	-	134	106	172	116	-	124
75% quartile	211	-	183	208	251	206	-	213
BRANCHES								
construction	9 (12)	0 (0)	26 (34)	18 (23)	11 (14)	13 (17)	0 (0)	77 (100)
trade	4 (6)	0 (0)	24 (36)	19 (29)	9 (14)	11 (17)	1 (1)	68 (100)
total assets /employee								
average	81609	-	31434	30174	23078	33641	9022	34965
25% quartile	14519	-	14959	10390	14361	15324	-	14362
median	19345	-	22707	16000	19727	24943	-	21924
75% quartile	34549	-	36364	38579	24503	36857	-	35522
nom. capital /employee								
average	4682	-	4367	3090	4457	8794	-	4818
25% quartile	1398	-	244	588	505	632	-	492
median	3243	-	1302	1399	1097	2272	-	1622
75% quartile	6206	-	6466	3250	7455	10497	-	5589
year of privatization								
1991	0 (0)	0 (0)	1 (50)	1 (50)	0 (0)	0 (0)	0 (0)	2 (100)
1992	2 (7)	0 (0)	11 (37)	9 (30)	4 (13)	4 (13)	0 (0)	30 (100)
1993	0 (0)	0 (0)	15 (38)	13 (33)	3 (8)	8 (21)	0 (0)	39 (100)
1994	2 (5)	0 (0)	13 (33)	10 (26)	9 (23)	5 (13)	0 (0)	39 (100)
1995	0 (0)	0 (0)	5 (31)	3 (19)	4 (25)	4 (25)	0 (0)	16 (100)
total	4 (3)	0 (0)	45 (36)	36 (29)	20 (16)	21 (17)	0 (0)	126 (100)

Figure 8.1-3 Lithuania: Ownershipstructure (dominant), Ultimo 1997 - size, branches, year of registration

	State	domestic persons	domestic financial	domestic non-fin.	foreign	total
Employees N	982 (13)	5222 (72)	151 (2)	338 (5)	590 (8)	7283 (100)
-19	176 (6)	2251 (82)	30 (1)	65 (2)	216 (8)	2738 (38)
20-99	488 (14)	2361 (69)	73 (2)	204 (6)	305 (9)	3431 (47)
100-199	154 (24)	383 (60)	28 (4)	36 (6)	35 (6)	363 (9)
200-	164 (34)	227 (48)	20 (4)	33 (7)	34 (7)	478 (7)
average	194	56	104	91	67	78
25% quartile	25	14	22	22	15	15
50% median	59	23	53	39	27	26
75% quartile	129	48	130	86	53	60
BRANCHES N	1245 (17)	5222 (69)	151 (2)	338 (4)	590 (8)	7546 (100)
agricult. fishing	325 (78)	75 (18)	5 (1)	2 (0)	8 (2)	415 (100)
mining wood	20 (4)	344 (75)	12 (3)	26 (6)	56 (12)	458 (100)
manufacturing	146 (10)	1068 (71)	53 (4)	97 (6)	142 (9)	1506 (100)
construction	50 (6)	773 (86)	18 (2)	36 (4)	17 (2)	894 (100)
trade	164 (7)	1887 (78)	34 (1)	106 (4)	238 (10)	2429 (100)
restaurants	43 (13)	237 (72)	8 (2)	12 (4)	28 (9)	328 (100)
transport	85 (14)	444 (73)	8 (1)	28 (5)	47 (8)	612 (100)
service	303 (39)	386 (49)	11 (1)	29 (4)	54 (7)	783 (100)
water supply	109 (90)	8 (7)	2 (2)	2 (2)	0 (0)	121 (100)

Figure 8.1-4 Foreign ownership by dominant owners - ultimo 1997

frequency row %	State	domestic persons	domestic financial	domestic non-fin.	foreign	total
0%	956 (15)	5048 (78)	141 (2)	296 (5)	0 (0)	6441 (100)
1-10%	16 (17)	62 (66)	4 (4)	12 (13)	0 (0)	94 (100)
11-30%	4 (5)	54 (70)	2 (3)	16 (21)	1 (1)	77 (100)
31-50%	6 (3)	58 (33)	4 (2)	14 (8)	93 (53)	175 (100)
51-99%	0 (0)	0 (0)	0 (0)	0 (0)	286 (100)	286 (100)
100%	0 (0)	0 (0)	0 (0)	0 (0)	210 (100)	210 (100)
total	982 (13)	5222 (72)	151 (5)	338 (5)	590 (8)	7283 (100)

Figure 8.1-5 Ownership by financial enterprises by dominant owners-ult 97

frequency row %	**State**	**domestic persons**	**domestic financial**	**domestic non-fin.**	**foreign**	**total**
0%	949 (14)	5026 (73)	0 (0)	315 (5)	565 (8)	6855 (100)
1-10%	16 (15)	69 (63)	1 (1)	10 (9)	13 (12)	109 (100)
11-30%	13 (11)	85 (74)	1 (1)	9 (8)	7 (6)	115 (100)
31-50%	4 (5)	42 (53)	25 (31)	4 (5)	5 (6)	80 (100)
51-99%	0 (0)	0 (0)	96 (100)	0 (0)	0 (0)	96 (100)
100%	0 (0)	0 (0)	28 (100)	0 (0)	0 (0)	28 (100)
total	982 (13)	5222 (72)	151 (5)	338 (5)	590 (8)	7283 (100)

Figure 8.2-1 Transition matrix Lithuania - industry majority July 1994 by July 1996

majority July 1994	Majority July 1996 State	outsiders foreign	outsiders domestic	insiders managers	insiders employees	no majo-rity	no answer	total
state	47 (67)	2 (3)	9 (13)	1 (1)	2 (3)	4 (6)	5 (7)	70 (100)
outsider foreign>domestic	0 (0)	4 (67)	2 (33)	0 (0)	0 (0)	0 (0)	0 (0)	6 (100)
outsider domestic>foreign	0 (0)	8 (6)	98 (79)	4 (3)	2 (2)	2 (2)	10 (8)	124 (100)
insider managers>employees	0 (0)	1 (8)	3 (25)	4 (33)	1 (8)	2 (17)	1 (8)	12 (100)
insider employees>managers	1 (2)	1 (2)	21 (40)	3 (6)	14 (26)	10 (19)	3 (6)	53 (100)
no majority	0 (0)	2 (3)	32 (53)	1 (2)	3 (5)	16 (27)	6 (10)	60 (100)
no answer	2 (6)	0 (0)	3 (10)	1 (3)	2 (6)	1 (3)	22 (71)	31 (100)
total July 1994	70 (20)	6 (2)	124 (35)	12 (3)	53 (15)	60 (17)	31 (9)	356 (100)
total July 1995	59 (17)	9 (3)	148 (42)	14 (4)	25 (7)	53 (15)	48 (13)	356 (100)
total July 1996	50 (14)	18 (5)	168 (47)	14 (4)	24 (7)	35 (10)	47 (13)	356 (100)

Figure 8.2-2 Transition matrix Lithuania - construction and trade majority July 1995 by July 1996

majority July 1995	majority July 1996 state	outsiders foreign	outsiders domestic	insiders managers	insiders employees	no majo-rity	no answer	total July 1995
state	10 (77)	0 (0)	2 (15)	0 (0)	0 (0)	0 (0)	1 (8)	13 (100)
outsider foreign>domestic	0 (0)	0 (0)	0 (0)	0 (0)	0 (0)	0 (0)	0 (0)	0 -
outsider domestic>foreign	0 (0)	2 (4)	43 (86)	2 (4)	0 (0)	0 (0)	3 (6)	50 (100)
insider managers>employees	0 (0)	0 (0)	2 (5)	31 (84)	2 (5)	1 (3)	1 (3)	37 (100)
insider employees>managers	0 (0)	0 (0)	2 (10)	1 (5)	15 (75)	2 (10)	0 (0)	20 (100)
no majority	0 (0)	0 (0)	6 (25)	2 (8)	1 (4)	15 (63)	0 (0)	24 (100)
no answer	0 (0)	0 (0)	0 (0)	0 (0)	0 (0)	0 (0)	1 (100)	1 (100)
total July 1996	10 (7)	2 (1)	55 (38)	36 (25)	18 (12)	18 (12)	6 (4)	145 (100)

Figure 8.2-3 Transition matrix Lithuania - industry degrees of employee ownership, July 1994 by July 1996

July 1994	July 1996						total
Employee shares	0%	1-10%	11-30%	31-50%	51-99%	100%	
0%	20 (83)	2 (8)	2 (8)	0 (0)	0 (0)	0 (0)	24 (100)
1-10%	3 (4)	65 (88)	5 (7)	0 (0)	1 (1)	0 (0)	74 (100)
11-30%	2 (2)	43 (43)	48 (48)	5 (5)	1 (1)	0 (0)	99 (100)
31-50%	2 (3)	15 (20)	29 (38)	28 (37)	2 (3)	0 (0)	76 (100)
51-99%	1 (4)	5 (20)	8 (32)	9 (36)	2 (8)	0 (0)	25 (100)
100%	0 (0)	0 (0)	1(100)	0 (0)	0 (0)	0 (0)	1 (100)
total July 1994	27 (8)	84 (26)	105 (32)	79 (24)	29 (9)	1 (0)	325 (100)
total July 1995	25 (8)	105(34)	111 (36)	53 (17)	14 (5)	0 (0)	308 (100)
total July 1996	28 (9)	130(43)	93 (31)	42 (14)	6 (2)	0 (0)	299 (100)

Figure 8.2-4 Transition matrix Lithuania - construction and trade degrees of employee ownership, July 1995 by July 1996

July 1995	July 1996						total
Employee shares	0%	1-10%	11-30%	31-50%	51-99%	100%	
0%	8 (80)	0 (0)	2 (20)	0 (0)	0 (0)	0 (0)	10 (100)
1-10%	0 (0)	34 (95)	1 (3)	0 (0)	1 (3)	0 (0)	36 (100)
11-30%	0 (0)	14 (21)	42 (72)	2 (3)	0 (0)	0 (0)	58 (100)
31-50%	0 (0)	1 (0)	7 (28)	16 (64)	1 (4)	0 (0)	25 (100)
51-99%	0 (0)	0 (0)	3 (30)	2 (20)	5 (50)	0 (0)	10 (100)
100%	0 (0)	0 (0)	0 (0)	0 (0)	0 (0)	0 (0)	0 (100)
total July 1996	8 (6)	49 (33)	55 (38)	20 (14)	7 (5)	0 (0)	145 (100)

Figure 8.2-5 Lithuania, transition matrix: July 1996 by ult. 1997

Dominant July 1996	dominant ultimo 1997 state	foreign	domestic persons	domestic financial	domestic non-fin.	Total
State	46 (68)	1 (1)	19 (28)	0 (0)	2 (3)	68 (100)
Outsider foreign>domestic	2 (13)	9 (56)	4 (25)	0 (0)	1 (6)	16 (100)
Outsider domestic>foreign	13 (5)	3 (1)	152 (67)	36 (15)	31 (13)	235 (100)
Insider managers>employees	1 (2)	0 (0)	53 (96)	1 (2)	0 (0)	55 (100)
Insider employees>managers	2 (4)	1 (2)	44 (92)	0 (0)	1 (2)	48 (100)
total ultimo 1997	64 (15)	14 (3)	272 (64)	37 (9)	35 (8)	422 (100)

Figure 8.2-6 Lithuania, transition matrix: primo by ultimo 1997

Dominant primo 1997	Dominant ultimo 1997 State	foreign	domestic persons	domestic financial	domestic non-fin.	Total
State	778 (87)	8 (1)	70 (87)	10 (1)	26 (3)	892 (100)
Foreign	0 (0)	316 (94)	17 (5)	0 (0)	2 (1)	335 (100)
Domestic	57 (1)	50 (1)	3482 (89)	121 (3)	218 (6)	3928 (100)
total January 1998	835 (16)	374 (7)	3569 (69)	131 (3)	246 (5)	5155 (100)

Fig 8.2-7 Lithuania, foreign ownership, primo by ultimo 1997

primo 1997	ultimo 1997						
foreign share	**0%**	**1-10%**	**11-30%**	**31-50%**	**51-99%**	**100%**	**total**
0%	4550(98)	23 (0)	24 (1)	17 (0)	26 (1)	6 (0)	4646 (100)
1-10%	6 (12)	44(85)	0 (0)	1 (2)	1 (2)	0 (0)	52 (100)
11-30%	8 (15)	6 (12)	30 (58)	5 (10)	1 (2)	2 (4)	52 (100)
31-50%	6 (5)	2 (2)	8 (6)	100(76)	13(10)	0 (0)	131 (100)
51-99%	4 (2)	3 (2)	0 (0)	4 (2)	161(90)	6 (3)	178 (100)
100%	1 (1)	0 (0)	1 (1)	0 (0)	4 (4)	87 (94)	93 (100)
total ult. 1997	4575(89)	78 (2)	63 (1)	127 (3)	206 (4)	103 (2)	5152 (100)

Figure 8.3-1 Lithuania: Ownershipstructure (dominant), ultimo 1997 - capital-structure

	state	domestic persons	domestic financial	domestic non-fin.	foreign	total
equity N	979	5222	151	338	590	7280
/employee 1000 lat						
average	73899	11737	33111	31309	45551	24188
25% quartile	7410	909	4193	2454	917	1085
50% median	16461	3844	14570	11519	8000	5488
75% quartile	42875	11771	42813	30773	32851	16686
total assets N	977	5222	151	338	590	7288
/employee 1000 lat						
average	95873	44952	63500	76966	176880	64354
25% quartile	16227	10406	19485	16326	29571	12253
50% median	28549	22046	40125	33360	73487	25669
75% quartile	63304	47297	82279	73827	157731	57450
debt/equity N	977	5222	151	338	590	7278
average	3.56	27.37	14.79	26.15	64.32	26.85
25% quartile	0.16	0.91	0.31	0.37	1.21	0.63
50% median	0.58	3.47	1.16	1.37	5.48	2.61
75% quartile	1.50	13.54	4.61	7.75	45.28	11.35
short/long loans	173	1186	38	94	240	1731
average N	12.21	136.96	12.96	2234.37	13.04	218.48
25% quartile	0.54	0.68	0.55	1.04	0.34	0.58
50% median	1.55	1.99	1.45	2.87	0.96	1.78
75% quartile	5.01	7.07	4.77	7.47	4.16	6.12
bankcredits N	982	5222	151	338	590	7283
/employee 1000 lat						
average	9661	3365	7818	11241	9028	5131
50% median	0	0	0	0	0	0
75% quartile	0	0	2637	1295	0	0
90% quantile	2173	6067	18840	14647	10000	6147
95% quantile	10127	15000	38392	36656	32353	17026

Figure 8.3-2 Lithuania: Ownership (dominant), ult. 1997 - performance

	state	domestic persons	domestic financial	domestic non-fin.	foreign	total
value added/ employee 1000 lat	981	5222	151	338	590	7282
average	-1855	3293	-2463	962	16287	3424
25% quartile	-6547	-6720	-13806	-10535	-8605	-7053
50% median	-1123	229	-2334	351	8514	152
75% quartile	3953	11185	5855	10248	45828	11150
sales growth N	832	3561	131	246	372	5142
average %	17.3	84.4	24.0	46.1	13827	1064
25% quartile	-6.7	-5.0	-19.3	-11.3	4.06	-5.4
50% median	9.7	20.8	4.2	9.8	31.9	17.1
75% quartile	26.5	64.8	28.6	48.9	79.2	57.2
profitmargin	975	5215	150	338	587	7265
average	1.8	13.6	9.3	8.8	20.4	12.2
25% quartile	-2.8	2.9	2.1	5.3	8.2	2.5
50% median	7.8	13.4	14.4	15.7	18.1	13.4
75% quartile	18.5	25.3	23.8	24.3	31.7	24.8
return o assets	977	5222	151	338	590	7278
average	0.6	7.9	-1.4	0.1	3.9	6.0
25% quartile	-4.6	-2.0	-5.5	-4.2	-3.6	-2.7
50% median	0.8	5.6	0.5	1.4	5.4	4.2
75% quartile	6.7	20.3	10.1	14.1	19.2	17.7
90% quantile	17.3	40.9	18.2	30.0	33.9	36.7
95% quantile	26.7	54.9	22.7	36.0	44.7	51.1
salary per employee 1000 lat	982	5222	151	338	590	7283
average	9667	7444	9253	9301	13078	8324
25% quartile	6339	4020	6168	5620	5640	4404
50% median	8247	5779	8296	7819	9374	6488
75% quartile	11163	8790	10813	11928	16775	9872
90% quantile	14894	13034	14318	16547	28182	14578
95% quantile	18221	16608	15634	18857	35788	18916
netinvestment/ employee 1000 lat	831	3524	130	242	371	5098
average	7726	2439	-2197	-188	15927	4039
25% quartile	-1235	-453	-2786	-1565	-826	-641
50% median	-252	191	-492	-97	1003	71
75% quartile	470	2600	804	1611	6612	2388
growth in N employment	835	3569	131	246	374	5155
average	-7.3	13.4	-9.7	6.0	30.3	10.3
25% quartile	-17.9	-15.3	-25.0	-23.3	-6.4	-16.0
50% median	-6.7	0.0	-10.2	-8.7	8.0	-1.7
75% quartile	0.0	21.7	0.0	7.7	35.9	16.1

9. Summary on ownership analysis and economic performance

The privatization process and the results on ownership, corporate governance, and economic performance have many similarities between the three Baltic countries, but there are also differences depending on specific policies and the development of the institutional framework. In this summary we will start each point by outlining the general trend and then go deeper into some of the main differences between the countries. We have already summarized the main elements in the privatization process in section 5. This section will focus on ownership and economic performance or restructuring, but also make some connections back to the specific privatization models and institutional conditions in each country. We will follow the division in three subsections: 1) ownership structure after privatization/establishment of new firms, 2) ownership dynamics after privatization, 3) governance structures and economic performance/restructuring.

9.1 Ownership structure after privatization/establishment of new firms

The ownership structure now existing in the Baltic countries is both a result of privatization/start of new enterprises and of dynamic change in ownership after the establishment as private entities. It is seldom possible to make a clear distinction between de novo enterprises and privatized enterprises, but in general most of the small enterprises with less than 20 employees are started as new starts although often with some privatized assets. On the other hand most large private enterprises with 100 or more employees are privatized. In between it is more difficult to distinguish the group of medium sized enterprises, and only in some cases we have been able to make a clear distinction in the analysis.

The general trend in all three countries is that management ownership is dominant for small enterprises, both for new started and for privatized. Like in the West, most small enterprises in trade, small manufacturing etc. have been started by a sole proprietor. The new cooperatives have been a special way of early private start ups giving the broader group of employees a more formal role in the ownership-structure, but we assume that most of these enterprises very quickly transformed to management owned enterprises. In the privatization process managers of enterprise of small enterprises or more often smaller branches of a larger enterprise have got relatively good possibilities to take-over their units. This was especially the case in the early period of transition in all three countries. In some cases, especially in Estonia and Latvia broader, employee ownership were encouraged in the early small privatization. In Lithuania, on the contrary, in privatization of small enterprises there were less advantages for employees than was the case for large privatization in relation to the LIPSP program.

The result on ownership structure was a very high proportion of manager owned small enterprises especially in Estonia and Latvia and a somewhat lower proportion in Lithuania. Ownership of a broader group of employees is also found in small enterprises, but this type of ownership was more evenly distributed also to cover medium and large-sized enterprises. This brings the total proportion of insider ownership to a quite high level compared with international standard. Thus in January 1995 it is estimated that in 30%-60% of the private companies in the three countries insiders own at least 50% of the firm. The percentage is highest in Latvia and apparently lowest in Lithuania, but in Lithuania the number are relatively high in large companies and insiders own shares in nearly all companies including those which do not have a single group owning the majority. In the industrial enterprises in Lithuania around 75% of the employees own shares. In Estonia, we find an incidence of employee ownership, with one in four employees owning shares in private firms in 1995.

In Lithuania, nearly all enterprises have at least an element of employee ownership, the broad group of employees has a quite strong position versus management, and there are fewer non-owners among the employees than in Estonia and Latvia. In Lithuanian industry the employees dominate managers in relation to ownership. In Estonia and Latvia the two types of ownership have about the same weight when measured in January 1995. However, in Latvia there is a higher proportion of enterprises with majority insider ownership than in Lithuania.

Foreign ownership has been most important in relation to some of the very large privatization in all three countries. However, this type of privatization started some years earlier in Estonia than in Latvia and are first in these years taking off in Lithuania. This is a major reason why foreign ownership up till 1996 is very important in Estonia while minor important in Latvia and of negligible importance in Lithuania. Because of the proximity to Finland and the general international openness Estonia has also seen a quite high proportion of foreign ownership in small enterprises especially in trade. There are some tendencies in this direction also in Latvia while in Lithuania the share of foreign ownership is lower than in the two Northern countries.

By 1996, in Lithuania, a relatively high proportion of enterprises are categorized as “no majority”, no single group - state, outsiders or insiders - have the majority of the shares. This is mainly because the state kept a substantial minority stake in many enterprises in the LIPSP-privatization, and the following process of selling out these shareholdings has been relatively slow up to 1998. In both Estonia and Latvia there is a considerable concentration of shares at a single group of owners leaving only 2-6% of the private enterprises in the category of “no majority”.

One of the main barriers for establishing insider ownership is the lack of capital. Foreign investors on the other hand have a strong advantage in access to capital. Special advantages for insiders in the privatization process might change this relation. In the Baltics this was the case in Lithuania. In Estonia and Latvia there is a strong tendency for a relatively low capital intensity in insider owned enterprises. This is especially the case when measured as nominal capital per employee, but this is also the tendency for total assets per employee. Here is a significant difference from the situation in Lithuania. Here, total assets per employee is about the same in insider as in outsider owned companies. Nominal capital per employee in employee owned enterprises in industry is lower than for other ownership types, but the tendency is much weaker than it was the case in Estonia and Latvia. It is probably the higher level of support for employees in Lithuania which explains this difference. In the other countries insiders including the broad group of employees could only afford a take-over when the price reflected in the nominal capital per employee was relatively low.

9.2 Ownership dynamics after privatization or start up

The initial ownership structure after privatization cannot be expected to fit to the long run preferences of different stakeholders and to the most efficient distribution of ownership on different owner groups. Therefore, the dynamics of ownership structures after privatization is very important. However, trading of shares, enforcement of ownership rights and other elements in the institutional framework for corporate governance might hamper the dynamic adjustment resulting in a high degree of inertia in the ownership structure.

In fact some degree of inertia characterize all three countries. Except for the continuing privatization transferring ownership from the state to the other groups there is only little dynamics between the broadly defined private ownership categories such as insiders, domestic outsiders and foreign outsider. In this respect we find somewhat more dynamics in Estonia than is the case in the two other countries. However, the main change takes place within the group of insiders. In all three countries there is a strong dynamic trend of transferring broad employee ownership to management ownership.

Especially in Estonia and Lithuania the data show a quite fast change in ownership. The dynamics are not so profound in Latvia, however, here the survey covers only 167 enterprises and they were asked about historic data, implying a bias in the direction of stability. Thus, our conclusion is that there has probably been a rather dynamic change also in Latvia. There is a tendency, most pronounced in Estonia, especially for change away from employee ownership in large enterprises. Also the group of enterprises with “no majority” is falling in all three countries.

The tendency away from employee ownership can also be found on the personal level in the enterprises. The number of non-owning employees is increasing in all three countries, except for small enterprises in Estonia. This confirms the tendency for higher stability of employee ownership in small enterprises.

Dynamics with foreign owners taking over privately owned enterprises can also be found in the material although the frequency is rather low. Here we find some indication of gradual takeovers to a higher extent that takeovers in one blow.

9.3 Ownership structures and economic performance

The general conclusions in most theoretical literature on the relation between ownership and economic performance / restructuring is that private performs better than state, outsiders better than insiders, and within these groups: managers better than employees and foreigners better than domestic investors. We can construct a scale like shown in figure 9.3-2.

Foreign ownership is considered to have the highest potential for efficient economic performance and restructuring because of the access to capital, management skills, including corporate governance abilities, and access to international business networks. All the companies in the transition economies will meet strong barriers because of the lack of developed institutions and high market uncertainty, but foreigners have an advantage because of their strong links to the Western markets. This is the main advantage in relation to concentrated domestic outside ownership.

Insider ownership on the other hand, and especially employee ownership, are considered to have specific disadvantages because employees might have special objectives of stable jobs and high wages differing from profit maximization. They might lack the necessary management skills and they have limited access to capital. Management ownership lies somewhat between employee ownership and outside domestic ownership.

Figure 9.3-1 Theoretical predictions on efficiency for different owner groups

---> higher efficiency

State	**employee**	**manager**	**outside dom.**	**foreign**
Information and incentive problems	spec.goals lack of skills and capital	between employee and outside	specific barriers in transition	profit-max + capital + manage skill + networks
	specific barriers on the domestic market lack of efficient financial marktet etc			access to well functioning int. markets

----

However, before evaluating the actual performance of the different owner groups it must be checked whether they have the same starting conditions. Foreign owned and management owned enterprises are both the result of new start ups as well as privatizations, while broader employee ownership are mainly the result of the privatization process. There are striking differences concerning size and capital-intensity. Management ownership is especially found in small enterprises, while employee ownership tend to be larger on average. Insider-ownership has a quite low capital-intensity and foreign owned a rather high intensity and this concerns both privatizations and start ups.

For privatized enterprises an important question is if specific owner groups can “skim the cream” when choosing the companies for takeovers while other groups are left with the low performing enterprises. Data for the very early years before privatization are difficult to get and not very reliable, but the indicators we have got show that there is no significant variation in the level of pre-privatization profitability between owner groups. There is no evidence of “cream skimming”. However, both the description of the early privatization process and the data on capital-intensity gives some indications that insiders might have acquired their enterprises for a relatively low price.

Looking at the economic results for different ownership structures quite strong general trends in all countries are apparent, and these trends are both covering data for the small samples of the early periods of transition, 1993-1995 and the large samples covering 1996 and 1997. A few of the results are based on deeper econometric analysis, eg factor productivity for Estonian panel data, but much of the results are based on simple descriptive data and shall be taken as preliminary, see a summary of the result in figure 9.3.

The performance of foreign owned enterprises has the following characteristics:

- high capital-intensity from the start
- high sales per employee, and high growth rate of sales
- high export share (only documented for Estonia)
- high labor-productivity, measured as value added per employee,
  (difference to other groups lower when measured as sales per employee).
- high investment level
- relatively high level of debt and good access to bank loans
  (bank loans per employee much higher than for other ownergroups).

These figures show that foreign owned enterprises takes the lead when it concerns pro-active restructuring, that is developing new markets, new products and new production methods. In this way the foreign owned companies used their advantages in relation to access to capital, and market networks.

The other side of the coin is that foreign owned enterprises have:

- relatively high wages,
- higher cost of capital connected to the high capital-intensity
- factor productivity on the same level as insider ownership
- relatively low return on assets

The results indicate that the high level of assets have not yet paid off in foreign owned enterprises. Profitability is lower and factor productivity on the same level as in insider owned enterprises although foreign ownership have advantages in mangement and easy access to international market networks.

If we look at insider owned enterprises, they seem to be examples of more defensive restructuring:

- cutting down employment - sometimes somewhat sluggish,
- paying relatively low wages,
- having problems of getting bank-loans,
- implementing relatively low investments.

However, at the same time they can show relatively good results on:

- relatively high profitability and factor productivity.

This is related to relatively low capital-intensity at the starting point, but it also indicates that they have done some restructuring and improved their use of scarce resources in a direction of higher efficiency. Compared to domestic outside owned enterprises insider ownership are doing surprisingly well in most measures across the three countries. This is the case for factor productivity for Estonia - no significant differences for the other countries can be found.

The most important deviation from the general trend is a somewhat higher capital-intensity in employee owned enterprises in Lithuania. This was the result of the first stage privatization program enabling employees to use vouchers for buying also relatively expensive enterprises. This gave room for somewhat higher wages in these enterprises although still significantly lower than in foreign owned enterprises.

For Lithuania we also have results from 1997 showing that enterprises owned dominantly by financial companies are doing comparatively worse than other private enterprises. We take this as a sign of banks taking over enterprises in economic crisis. In this way financial companies have started to play a role a active creditors, but we se no strong signs that financial institutions play an active role as owners in the economy in general.

10. Final remarks and perspectives

The three Baltic countries show many similarities in the development of new ownership structures, but they have followed different paths of privatization and this has to some extent resulted in differences in the structures of enterprise governance.

All three countries have a quite high degree of both management- and broader employee ownership. This was especially the case for the early stage of privatization and concerned mainly small and medium sized enterprises with quite low capital intensity. For Lithuania also larger and more capital intensive enterprises were taken over by a broad group of employees. Estonia has been the fastest to promote significant foreign investment, but the other countries have been catching up the latest years.

Some of the differences have been leveled off in the dynamic changes of ownership structures. The strongest change has been managers taking over the ownership from other employees. Although this process probably will continue for a longer period, the ownership structure of all three Baltic countries will for the foreseeable future have a quite strong element of employee ownership, and management ownership will continue to be on a high level especially in small and medium sized enterprises. At the same time foreign ownership will play a strong and increasing role in these small open economies.

How are the perspectives for restructuring under these conditions? The results on economic performance suggests that not only foreign companies can implement restructuring, also management- and employee owned enterprises undertakes restructuring although often more defensive than is the case for foreign owned enterprises. The task for the Baltic economies will not only be to further develop the cooperation with foreign investors, but also to improve the conditions for the domestic owned enterprises to match the foreign advantages. This could be the case in relation to access to capital, management training, building networks for exports etc.. Important for the development of a business infrastructure would be the development of the financial markets in general and more specific the development of specific credit-schemes for small and medium-sized enterprises. Also the development of institutions for management training, management consulting and activities promoting exports-connections and international networks for SMEs can be an important elements in restructuring the Baltic economies. Concerning employee owned enterprises some consulting efforts could further develop their advantages in relation to employee participation, motivation and alignment of the interests of owners and employees.

9.3 Summary on economic performance of different ownership groups

	Estonia	**Latvia**	**Lithuania**
initial conditions size capital intensity profitability	 FO low EO average, MO low FO very high EO and MO low IO average, FO ?	 FO average IO smaller FO very high IO lower no information	FO average MO smaller EO average FO high EO and MO average FO and IO average
growth in sales	FO high	FO high	FO and MO high EO average, OO low
export share	EO?, FO higher	-	-
employment change	FO highest growth EO less reductions EO and MO higher increases		FO high growth EO sluggish adjustment
factor-productivity	FO 19-21% higher EO 13-24% higher MO 15-31% higher OO same level as SO	no significant differences found	no significant differences found
labor-productivity	EO average	FO highest	FO highest EO and MO high
wage level	EO and MO lower FO higher	FO highest PO lower than SO	FO highest EO and MO high
profitability, (return on assets)	FO lower EO and MO higher	FO lower IO higher	FO low, later high EO high, MO average
finance debt/equity bankloans/employee	 EO and MO higher FO higher EO and MO lower SO lower	 FO average, IO high FO highest IO low SO lowest	 FO higher FO higher EO and MO lower
investment/employee	FO highest EO and MO average	FO highest IO higher than OO	FO highest
special note			financial owned firms worst performance

FO=foreign owned, EO=employee, MO=management, IO=insider, OO=outside domestic, SO=state, PO=private
Based on Jones and Mygind 1999 a, b and c and Mygind 1997 a and b.

References

Arkadie B.V. et. al. (1991): *Economic Survey of the Baltic Republics*, Stockholm.

Bradshaw, Michael, Phillip Hanson and Denis Shaw (1994) Economic Restructuring in *The Baltic States: The National Self Determination of Estonia, Latvia and Lithuania*, Edited Graham Smith, pp. 158-180. New York, St. Martins Press

Carlin W and M. Landesmann (1997): From Theory into practice? Restructuring and Dynamics in Transition Economies" *Oxford Review of Economic Policy*, vol 13, no 2 pp 77-104.

Earle, J.S., S. Estrin and L Leshchenko (1995) "Ownership Structures, Patterns of Control and Enterprise Behavior in Russia" mimeo, Central European University.

EBRD 1995 *Transition Report for 1995*, EBRD, London.

ESA - Estonian Statistical Office - statistical publications

Estrin, Saul (ed.) 1994 *Privatization in Central and Eastern Europe*, Longmans

Frydman R, C. Gray, M. Hessel and A. Rapaczynski (1997): Private Ownership and Corporate Performance: Some Lessons from Transition Economies, *C.V. Starr Center for Applied Economics, Economic Research Reports.*

Frydman et al. (1993a) *The Privatization Process in Russia, Ukraine and the Baltic States.* CEU Privatization Reports, V.2, Budapest, London/NY.

Jones D. and N. Mygind (1998): Ownership Patterns and Dynamics in Privatized Firms in Transitions Economies: Evidence from the Baltics, *CEES Working Paper Series,no 15,* Forthcoming in Baltic Journal of Economics

Jones D. and N. Mygind (1999a): The Nature and Determinants of Ownership Changes after Privatization: Evidence from Estonia, *Journal of Comparative Economics, vol 27 no 3 pp 422-441.*

Jones D. and N. Mygind (1999b): Ownership and Productive Efficiency: Evidence from Estonia, *CEES Working Paper Series, no 24*

Jones D. and N. Mygind (1999c): The Effects of Privatization on Productive Efficiency: Evidence from the Baltic Republics, *CEES Working Paper Series, no 22*

Kein A. & V. Tali (1994): The Process of Ownership Reform and Privatization, paper from Institute of Economics, Estonian Academy of Sciences.

Kein A (1995): Capital Market Institutions in Estonia, Estonian Academy of Sciences, Discussion Papers, no 44.

Kein and Terk (1997): Management-Buy-Out and Management-Buy-In in Estonia, Chapter 4

Lee B. (1996): Lithuania, in (Lieberman et al. eds.): *Between State and Market*, World Bank/ OECD, 1997.

LPA - Latvian Privatization Agency (1995-1998): Annual reports, Riga.

Liuhto K. (1995): Foreign Investment in Estonia: A Statistical Approach, *EUROPE-ASIA STUDIES*, vol. 47, no 3, pp 507-525.

Martinavicius J. (1996): Privatizaiton in Lithuania: The Legislative and Political Environment and the Results Achieved, in in Mygind, 1996, pp. 267-294.

Ministry of Economic Affairs (1999): (A. Purju ed.) *Estonian Economy, 1998-99*

Mygind N. (1994): The Economic Transition in the Baltic Countries - Differences and Similarities" pp.197-234 in *The Politics of Transition in the Baltic States - Demo cratization and Economic Reform Policies*, J. Å. Dellenbrant and O. Nørgaard, Umeå University, Research Report nr. 2, 1994.

Mygind N (1995): Privatization and employee-ownership in the Baltic countries - a comparative analysis of conditions and development" pp. 199-284 in Mygind ed.: *Privatization and Financial Participation in the Baltic Countries - Midterm Results*, CBS,

Mygind N (1996): *Privatization and Financial Participation in the Baltic Countries* mimeo, CEES, Copenhagen Business School.

Mygind N. (1996b): The Baltic Countries in Transition - a comparative analysis, in Mygind (1996) pp 13-94.

Mygind N (1997a): The economic performance of employee-owned enterprises in the Baltic Countries, *CEES Working Paper Series,no 6, 46 pages.*

Mygind N (1997b): Employee ownership and Participation in the Baltic Countries" in Uvalic and Vaughan-Whitehead (eds.)

Pohl G., Anderson R.E.,S. Claessens and S. Djankov (1997): Privatization and Restructuring in Central and Eastern Europe: Evidence and Policy Options, *World Bank Technical paper no 368*, Washington D.C.

Purju, A. (1996): *The Political Economy of Privatization in Estonia*, working paper, Centre for Economic Reform and Transformation, Heriot-Watt University, Edinburgh.

Purju A. (1998): Interrelationships between privatization methods, ownership structure and economic results: evidence from Estonia, conference paper 1st INTER-conference, Copenhagen, CEES/CBS august.

Purju A. and J. Teder (1998): Company adjustment and restructuring problems in Estonia between 1992-1995, working paper no 11, March, Tallinn Technical University.

Rajasalu T. (1994): Estonian Economy: Summer 1994, *Report*, no 2, Institute of Economics, Estonian Academy of Sciences, Tallinn.

Reardon, Jack (1996) "An Assessment of the Transition to a Market Economy in the Baltic Republics" *Journal of Economic Issues* vol. XXX, #2, June, 629-638.

Semeta A. (1997): Economic Transition in Lithuania - 1996, mimeo, Vilnius.

Shteinbuka. I. (1996) *Privatization in Latvia and the role of Employee Ownership,* in Mygind, 1996, pp. 155-200.

Sutela, P. (1994) Privatization, Employment and Inflation in the Baltic Countries. *Communist Economies and Economic Transformation*, v.6, # 2.

Terk, E. (1996) “Employee ownership in Estonia” in Mygind ed., 1996.

Uvalic, Milica and Daniel Vaughan-Whitehead (1997) “*Privatization Surprises in Transition Economies*” Elgar, Cheltenham, UK.

Venesaar U. and J. Hackey (1995): *Economic and social changes in the Baltic States in 1992-1994*. Estonian Academy of Sciences, Tallinn.

Vojevoda, L. and L. Rumpis (1993) “*Small Privatization in Latvia*” mimeo, Inst. of Economics, Latvian Academy of Sciences.

World Bank (1993) *Latvia-The Transition to a Market Economy*

World Bank (1996) *World Development Report: From Plan to Market* Oxford Press, New York

World Bank (1998) *Lithuania - An Opportunity for Economic Succes, vol 2. Analytical Background*, World Bank Country Study, Washington D.C.