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## TRANSITION PROCESS IN THE CONTEXT OF PRIVATIZATION IN THE REPUBLIC OF SERBIA (2001-2010)

*Essentially, the transition process results in the transfer of ownership of companies by means of privatization which leads to management being taken over by private companies and individuals. This research is aimed at examining political and economic possibilities of transition in Serbia (2001-2010), the already achieved results and the political advantages of theoretical understanding of radical reforms, from constituting reform norms to the shift in relationships and awareness. The synthesis of these arguments, analyses and projections are used as a call for privatization as an inevitable process and the part of deep and fundamental change of Serbian society, with an aim to achieve completion of the current economic system and the foundation of modern government institutions.*

*Keywords:* privatization; transitional economy; Serbia; government policy and regulations.

*JEL classifications:* P20, P31, L33, G38.

## Веселін Перовіч, Борис Булатовіч, Браніслав Неранджіч ПЕРЕХІДНИЙ ПРОЦЕС У КОНТЕКСТІ ПРИВАТИЗАЦІЇ В РЕСПУБЛІЦІ СЕРБІЯ (2001-2010 рр.)

*У статті розглянуто перехідний процес, у результаті якого відбувається передача прав власності компаній за допомогою приватизації, що веде до передачі управління приватним компаніям і підприємцям. Вивчено політичні та економічні можливості трансформації економіки Сербії (2001-2010 рр.), вже досягнуті результати і політичні переваги теоретичного розуміння радикальних реформ, від встановлення норм реформування до змін відношення і сприйняття. Посидання цих аргументів, аналізу і бачення використовується у вигляді заклик до приватизації як невідворотнього процесу і частини глибокої корінної зміни сербського суспільства, з метою остаточного завершення поточного етапу розвитку економічної системи і заснування сучасних урядових інститутів.*

*Ключові слова:* приватизація; перехідна економіка; Сербія; урядова політика і регулювання.

## Веселин Перович, Борис Булатович, Бранислав Неранджич ПЕРЕХОДНОЙ ПРОЦЕСС В КОНТЕКСТЕ ПРИВАТИЗАЦИИ В РЕСПУБЛИКЕ СЕРБИЯ (2001-2010 гг.)

*В статье рассматривается переходной процесс, в результате которого происходит передача прав собственности компаний посредством приватизации, что ведет к передаче управления частным компаниям и предпринимателям. Изучены политические и экономические возможности трансформации экономики Сербии (2001-2010 гг.), уже достигнутые результаты и политические преимущества теоретического понимания радикальных реформ, от установления норм реформирования до изменений отношения и восприятия. Сочетание этих аргументов, анализа и видения используется в виде призыва к приватизации как неизбежному процессу и составляющей глубокого коренного изменения*

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*сербского общества, с целью окончательного завершения текущего этапа развития экономической системы и основания современных правительственных институтов.*

*Ключевые слова: приватизация; переходная экономика; Сербия; правительственная политика и регулирование.*

**Introduction.** This article examines and analyses the transition process in the context of privatization in the Republic of Serbia with special emphasis on the effects of privatization. This will be supported by the examples from everyday life with particular attention on the legally adopted methods of capital trade.

In the first decade of the 21st century, the post-socialistic countries are stepping into the phase of revising the achieved results and adopting inevitable changes in the contents of economic reforms and policies. Most of the countries have lapsed into transitional recession, which resulted in a head-long fall of the GDP to the level of nearly less than 15% of its amount in 1990 in Central and South-East European countries (Winiecki, 2002). Prior to the global economic crisis, Hungary, Latvia, Poland, Slovenia and to some extent Estonia and Lithuania faced the period of an uninterrupted growth, while Bulgaria and Romania experienced a sudden break in their economic growth as a result of macroeconomic crisis due to insufficient structural reforms in the mid 1990s (Kolodko, 2000).

After the years of decrease and stagnation in Serbian economy, 2004 was characterized by the GDP growth, productivity in the processing industry, and real increase of wages and public revenues but it was also accompanied by the increase of foreign trade deficit (Ristic, 2007). In the mentioned period, the macroeconomic stability was preserved by the acceleration of industrial growth and the considerable growth of GDP (Bennett, Estrin and Urga, 2007). The industry, followed by agriculture and trade, still has major influence on the formation of GDP which shows its high dependence on industrial sector. The considerable changes are demanding scientific interpretation.

Compared to development and establishment of the economy, general tendencies of transitional changes in Serbia have undergone various delusions containing fragile attempts of changes, more political in character rather than based on contemporary reasoning and acting in the scope of modern market theory tendencies and global development processes (Bjornskov and Potrafke, 2011). The set of attempts, effects and results are recorded in the practice of transitional changes and reforms. The general overview and analysis of the sequence of events can be divided into the attempts to preserve credibility of "the change in progress" by concurrent proving the quality of undertaken measures and preferences, on the one hand, and severe critiques of the level of changes, economic effects and thus projected perspectives, on the other hand (Hadzic, 2002). Among the transitional experiences that other post-socialist countries have encountered, there are numerous negative tendencies which Serbia needs to escape (Golubovic, 2002).

The transition process in Serbia started late after the adoption of the Privatization Act in 1989. In this area, there have been numerous attempts to carry out the reforms. However, as if exhausted at their earliest stage there is a lingering feeling that there were no true reforms in the country before the adoption of the above

act. The general idea of the Ante Markovic's administration was to give precedence to employees in privatization, i.e. to enable workers to buy shares in instalments. That privatization model stayed in force until the disintegration of the SFR Yugoslavia. After the breakdown, newly formed governments of newly established sovereign countries set up acts and bills on ownership transformation (Soskic, 1998).

The transitional period between 2001 and 2010 is characterized by numerous reforms with different levels of accomplishment, establishment of macroeconomic stability, restructuring of big corporate systems (Andjelkovic-Pesic, 2007), privatization of companies and the beginning of the process of applying for the EU membership resulting in intensive harmonization of legal issues in all the areas of economic and social life. However, in addition to important results in the process of transition and revitalization of industry (the constant increase of GDP) so far, Serbian economy has faced high unemployment rate and low standards of living (Stojkovic, 2004). In the forthcoming period, it is crucial to finish the process of transition and to carry on the legal harmonization with the EU as well as to generate and accelerate industrial growth. For successful realization of these objectives, it is necessary to define tasks, measures and instruments for their execution, as well as to establish constant monitoring.

General characteristics of the basis for future development can be defined as follows:

- Firstly, in the long run, the most important fact is the positive outcome of the Implementation Study by the EU which has led to the beginning of the negotiations on the Stabilization and Association Agreement. The agreement with the IMF is of key importance as an act implying the accomplishment of objectives in the agreed 3-year term credit arrangement. This arrangement has enabled to write off a significant amount of debt which is considered as a demonstration that the economic policy and the achieved macroeconomic stability are in line with the IMF's recommendations. The growth of GDP at a high rate, budget surplus and reduced deficit in international trade affairs have caused positive characterization of economic movements in the previous period. The international grades of referent institutions (World Bank, European Bank for Reconstruction and Development) have also confirmed positive changes in the transition process.

- Secondly, successfully conducted reforms have so far provided good basis for the beginning of the second phase of transition implying: completion of the process of public companies restructuring into big corporate systems, increase of competitiveness, and infrastructural reforms (Racic, 2002). However, the area which the future development greatly depends on is the field of investments, but statistical indicators show that Serbia is still not interesting enough for foreign investors.

**The Legal and Theoretical Framework.** The topics of this research as well as the established problems are the scopes and challenges of the privatization process in Serbia illustrated by the development of a transition model by taking into account the circumstances facing the society at the moment (Knezevic, 2010).

As the basic hypothesis of the research, the contribution and influence of the privatization process onto corporate culture development is tested and necessary existence of clearly defined state of ownership is highlighted as a supposition of

high importance in a successful system reform (Hanousek, Kocenda and Svejnar, 2009).

In order to confirm or to deny the established hypothesis, the research shows changes in ownership structure during the privatization process and the establishment of new ownership forms and owners' liabilities. These are demonstrative issues that emphasize the successful or unsuccessful performance of management and new corporate leadership. It is examined whether the existing model provides the framework which is not only clear and visible to public but also flexible enough, whether it enables the formation of prices of share capital arising from the privatized companies according to market forces, whether it has stimulating effect on the economy in general, as well as the fairness of actions and legal security of affairs. During the privatization process, there is a possibility for the growth of GDP, productivity and real increase of wages and public revenues.

The goal of this research is to systemize theoretical knowledge in the area of privatization models under the transition circumstances (Megginson and Netter, 2001; Farkas, 2011) and their development while in the empirical part of the study, the prime interest is to examine the scope and the results of the privatization process in Serbia.

Privatization is a precondition for the EU integration process, as well as for the inclusion into the global economic processes. It is also a primary condition for economic rehabilitation and development in the long term, also creating competitive ambient for industrial growth as the main task of the state.

The first wave of privatization was introduced during the government of Ante Markovic in 1989 with the adoption of the Law on Socially Owned Capital according to which employees were given beneficial status to buy shares of their companies in installment. The privatization method in use was added capital value, with reductions on the account of socially owned capital and with gratifications that this type of privatization would lead to management efficiency increase. The privatization was not compulsory but it was stimulated by the law in a way that wage increases were to be paid out in shares only and not in cash. With slight changes, this Law was revised in 1990. During this reform year, privatization boomed (1,200 companies shifted into companies with different ownership forms). That happened partly due to technical weaknesses of the operational model and due to existing possibilities for manipulations. The follow up of the started privatization process occurred in 1991 with the adoption of the Law on Circumstances and Procedure for Transforming Socially Owned Capital into other Forms of Ownership. The characteristic of this Law is its strict approach to these procedures. However, hyperinflation of 1993 — causing depreciation of debts during share purchase in installments — became an unexpected stimulus for privatization. By the end of 1993, a great number of companies were completely privatized using the nonexistent regulations of debt revalorization for the rate of inflation. In that context, the Law on Revaluation was adopted by which all the inflation gains of citizens were annulated. Thus, by the year 1997 there was practically no privatization in Serbia (Vujacic, 1996). The Law on Ownership Transformation was passed in 1997, and it represented the continuation of the previous privatization model. Privatization was still decentralized, not obligatory and was pointed towards favoring employee shareholding. All employees and former employ-

ees in the public and state spheres, as well as insured agriculture workers had the right to shares free of charge in the amount of DEM 400 for each year of their employment. The free distribution of shares of 60% of public corporate capital was offered in the first round, 10% of corporate capital was directed to the State's Pension Fund, and the rest (30%) could be purchased for a six-year repayment period (Vujnovic, 1998). The capital that was not purchased became the ownership of the Share Fund. Priority was given to company employees but the companies themselves had the right to decide whether to step into the privatization process or not.

Following the political changes of October 5, 2000, the so-called temporary transitional government was formed and, during that administration, the privatization of some 500 profitable companies was started according to the 1997 Law. Serbian Government chose and adopted a slightly modified model of standard sale of capital. According to that, the model of sale was offered instead of free share distribution. The law embraced two privatization models: the sale of public and state owned capital and the transfer of socially owned and state owned capital free of charge. The model was chosen with the guiding idea to find real buyers, meaning to find those who will have some interest in making companies more profitable than they had been before the privatization. The second reason was to insure budget revenues from which some social expenditure could be financed. According to that model, the majority of the shares was sold to investors and by that, the full control over a company would pass to a major shareholder. One of the most important novelties of that model was that for the first time the sale of shares was favored to free distribution.

The basic law concerning privatization process is the Law on Privatization dated 2001 (passed by the National Assembly of the Republic of Serbia, enforced in 2002). By this law, general regulations are set for the preparation and privatization of companies. Due to the necessity to adopt changes related to altered circumstances, it has been amended and supplemented 3 times.

The process is carried out by the following institutions: Ministry of Economy and Regional Development, Privatization Agency of the Republic of Serbia, Share Fund of the Republic of Serbia, and Central Securities Depository. Apart from this, the Law on Privatization also prescribes that the Decree on Methods and Competency of the Privatization Agency will regulate the sale of companies in the field of electricity distribution, traffic and infrastructure, but not the companies in the field of road transportation, water economy, exploitation of minerals and woods, public information services, military industry, military equipment, veterinarian and communal services that are adopted on the proposal of the Privatization Agency and passed by the Government of the Republic of Serbia (Djordjevic, 2005). The list of these companies is set by Serbian Government.

The Law on Privatization includes the obligation of free distribution of shares to all legally adult citizens of Serbia. The law provides two sale methods: auctions for smaller and tenders for bigger companies (Pljakic, 2004). Furthermore, 70% of the capital is offered on sale and 30% is distributed among employees and citizens. For the first time, the voluntary character of privatization is established lapsed and its durability is insured by preset dates. According to the Law, 5% of any sale are to be set aside for future provisions for nationalized property. For those companies with no real chances of finding a buyer in their current state of affairs, restructuring program is to

be implemented. The law enforcement supervision is assigned to the appointed Ministry for Privatization. The capital for possible distribution of shares free of charge is limited to 30% of public and state capital depending on the method of capital sale (15% on tenders and 30% on auctions).

In order to start the privatization process, it is necessary to create the institutional and legal background (Mickiewicz, 2009). The institutional framework is represented by the establishment of the Privatization Agency of the Republic of Serbia, the Share Fund of the Republic of Serbia and the Central Securities Depository and Clearing House of the Republic of Serbia. The legal framework include laws, bylaws and decrees in the field of privatization. By now, 11 laws and 10 ordinances have been passed in the form of decrees or regulations and the set of important decisions has been made. However, the legal framework for the privatization has not been completed yet. The unresolved question is the issue of restitution since the Law on Restitution has not yet been passed, as well as the necessity to pass laws which will define the privatization strategy for companies in the field of electrical industry, telecommunications, communal activities, gas etc.

**The Effects of Privatization Process in the Republic of Serbia.** In the last 20 years, the turbulent development of Serbian reality shows some tendencies that have - under the influence of international affairs and regional conflicts - determined the processes and scope of transition (Petrovic, 2008). From the "favorite in the socialist block", Serbia has got lost in internal and Balkan conflicts (Stepic, 2001), numerous systemic and everyday distortions and has reached the "transition bottom".

The basic principles upon which the concept of privatization lies in the Republic of Serbia are:

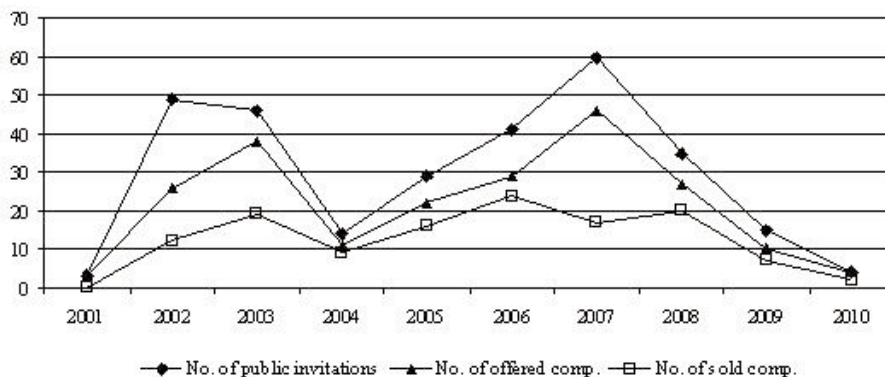
- Securing publicity: the rules for taking part in privatization procedures are transparent which enables public has access to information on each and every sale.
- Fastness: it is planned to carry out privatization in a short period of time. In this way, transition period will be shortened for companies enabling them to improve their performance and leaving space for opening new positions in future.
- Competitiveness: equal opportunities are offered to all interested in taking part in privatization.
- Equity: not only that the process has to correspond to legality but also to justice, as a higher moral category with an intention to put emphasis on the necessity of this process in accordance with the highest moral standards.

The set objectives of the privatization process are: (1) contribution to the economic reforms and transition to institutions and mechanisms of the market economy, (2) regaining lost markets and inclusion into the international flows of capital and goods, (3) introduction of western standards and norms in business, (4) ensuring assets for the state and disburdening the state budget, (5) ensuring the flow of foreign capital in order to revitalize the economy, (6) development of competitiveness and breaking monopolies at the markets of goods and services, and (7) creating new jobs.

In order to analyze the process of privatization, a research has been carried out with the emphasis on correlative relationships that exist between the numbers of offered and sold companies in the period between 2001 and 2010 (Figures 1 and 2).

The first diagram shows the number of offered and sold companies at public tenders in the Republic of Serbia.

**The number of offered and sold companies (tenders)**



**Figure 1. The Number of Offered and Sold Companies (Tenders)**

It is obvious that the number of offered companies by the method of public tender, including the number of public invitations, was the highest in the first years of the process although the number of the realized sales was modest. The relationship between the offers and the sales was the most favorable in 2004; the reason was the modest level of offers in that year. After that, there was a rise in both numbers. Thus, in 2007, the increase of offers continued although the realization of deals considerably fell down. During the period 2001-2003, the process was in the situation of growth with high number of offered companies but the investors showed the highest interests during 2006 and 2008. It is obvious that in the institutions in charge of the privatization process the biggest challenges were experienced after 2003 when it was the hardest to secure necessary number of solvent investors for the offered companies. The Government acted accordingly and passed decrees and amendments to the Law on Privatization in order to create preferable environment for investors (Skuflic and Botric, 2006) and introduced certain relieving matters with reference to process participants (e.g., conditional deduction of government and commercial liabilities).

The research has been also carried out to see the results of privatization at public auctions. The numbers of the offered and sold companies by the method of public auctions in the Republic of Serbia are presented in Fig. 2.

It is obvious that the number of companies, both offered and sold, was the highest in the first years. The relationship between the number of the offered and sold companies has not changed considerably; not even in the years with lower offer. In the forthcoming period, officials will have to deal with the challenge of finding solvent investors willing to invest in the companies that will be on sale and which are relevant to their operating results in a more complicated situation than those that have already been sold, i.e. most of these companies are heavily indebted with a number of surplus labor force and unattractive physical assets for sale.

The number of offered and sold companies (auctions)

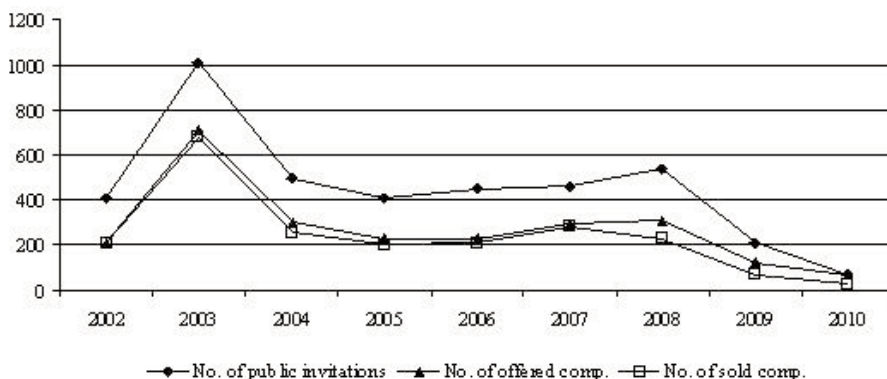


Figure 2. The Number of Offered and Sold Companies (Auctions)

The significance of the following issues has also been studied: the actual method of privatization, achieved effects in the terms of contracted investments and realized budget revenues from the sale of companies (Figure 3).

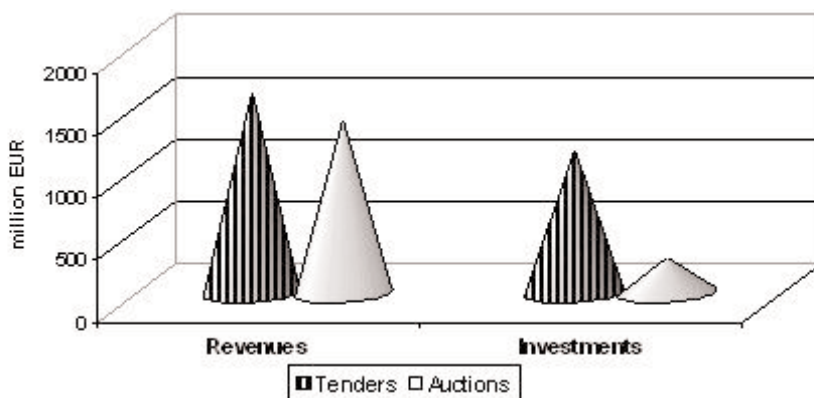


Figure 3. Budget Revenues and Investments Realized by Tender and Auction Methods of Privatization (2001-2010)

The level of investments and revenues obtained by the sale of companies on the territory of the Republic of Serbia is illustrated in Figure 3. The method of public tenders has been proved to be more successful (Kecman, Susnjar, 2009) both in the cases of investments and in the case of generated revenues. The reason for this tendency lies in the characteristics of companies that have been sold on tenders (big corporate companies with many employees and high value assets). The sale made by the method of auction, and investments are dependant on accumulated amortization. Nearly the same amount of budget revenues generated by both methods is the result of the fact that the number of companies sold by public auctions is far greater than the number of companies sold by public tenders. The research also contains the analysis of the companies sold according to their business activities (Figure 4).



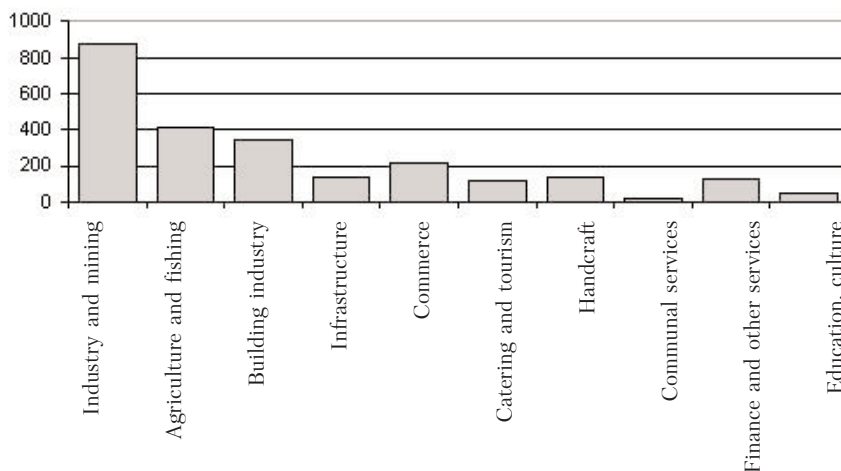


Figure 4. Companies Sold, by Types of Business Activities

According to the results of the research, the authors have come to the conclusion that the biggest number of sold companies is achieved in the field of industry, then in agriculture and building. The reason for this can be found in the characteristics of these companies (reliable business results, possession of land and other assets) and in the fact that they represent the majority in the total number of the companies. The structure of entities which are in the process of privatization is similar to the structure of companies that have already been privatized.

In the next period, structural reforms should continue in order to achieve faster growth and reintegration of Serbian economy into international institutions. The high rate of economic, legal and political stability needs to be kept in order to increase foreign investments (Kovac, 2006), competitiveness and exports. The legal framework should be finalized and the process of harmonization with the EU regulations should be continued. The efficient use of the Law on Bankruptcy Procedure should be enabled. The sale of the Privatization Agency's portfolio should also be continued, as well as the sale of minority shares in companies owned by the government in order to improve corporate management and business performance, especially regarding companies with good development results. The development of small and medium size companies should be stimulated since newly established companies are the main sources of employment and industrial growth in the country. Without new productive work positions which can absorb the part of unemployed population created by the privatization of big industrial systems, the social costs of the transition can have negative effect on the process of reforms.

**Conclusions.** The research carried out has established some of major features relevant to the current state of affairs considering the privatization process in the Republic of Serbia which has experienced numerous challenges such as: (1) slow process of privatization and the undetermined attitude of the Serbian Government towards necessary steps in order to accelerate the process (the privatization of corporations with socially owned capital is in the final phase while the privatization of companies with state owned capital is in the earliest phase), (2) suspicion of general pub-

lic relevant to the necessity, transparency and legality of the privatization process which greatly contributed to the public's negative approach towards the matter and the lack of continuous efforts made to educate the public on the process of privatization (especially relevant to the post-privatization period), (3) weak interest of foreign investors to take over companies of strategic interest and failure of expected inclusion into the flows of global economy, as well as the incorporation of new technologies and corporate skills through the privatization, (4) the global economic crisis, that has caused the absence of foreign investments (Cerovic, 2009), (5) huge amount of corporate debts, i.e. indebted companies considering unpaid wages, social benefits, liabilities, public funds, creditors etc., (6) inadequate protection from unemployment and inadequate system of social protection have arisen from the fact that the process has been carried out in the atmosphere of deep social tensions, (7) investors faced with conditions originating from non-market economy and unfavorable deadlines, rigid labour laws and public policy that leads to cost increase in business affairs through overemphasized administrative demands and unnecessary political interfering, (8) part of the state capital not prepared for sale due to affairs regarding ownership, unknown hidden liabilities of companies, and especially unwillingness to show the real state of affairs in passive balance sheets, (9) unsynchronized approach of the legal system regulating same matters in several different ways and non-existence of the Law on Restitution, (10) lack of global strategy concerning companies in the area of infrastructure (public and communal enterprises) which slows down the development of normative and legal framework necessary for attracting new investors and (11) disregard and negative approach of managerial and executive boards and management towards the process of privatization in order to retain their positions.

Characteristics of most important negative effects of the privatization process that has been carried out so far in the Republic of Serbia are: insufficiency reduction of budgetary expenditure to cover the costs of the public sector, incomplete development of competition, unresolved questions of ownership, imprecise data on assets and liabilities, disproportionate labor force, low number of key investors and strategic owners with the vision and motivation to increase productivity and competitiveness, accumulated debts of corporate bodies, liabilities that surpass the worth of assets and slow and unequal process of restructuring in public and communal enterprises that are connected with strategic objectives and programs for development. The positive effects are: reduction of monopolies at the markets of goods and services, provision of revenues for the state budget, flow of foreign capital, faster and wider integration into international capital markets, development of existing technologies, better offer of goods and services, dynamic growth of the private sector, transparent ownership structure, formation of production structure that can be sold at domestic and international markets, increase of efficiency, open market economy, development of financial markets, increase of competitiveness, macroeconomic stability and growth of the living standards.

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