

# BOOK REVIEWS

## RESULTS OF THE NATIONAL ECONOMIC EXPERIMENT IN THE MODERN ECONOMIC HISTORY IN THE CZECH REPUBLIC

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**Tomáš Hřebík**

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### **Karel Zeman. Analysis of the Privatization Process in the Czech Republic**

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This specialized monograph is the first part offering a comprehensive view of one of the most important transformation processes in Czech history, which is the privatization process. Here, readers are clearly and comprehensibly presented with the theory pertaining to the economic process, an analysis of the legal framework and institutional securing of the entire process, the macroeconomic and statistical analysis of the process, the complete synthesis of privatization, and the conclusions arising from it. Thanks to this, it's a work which serves as a comprehensive overview, and thus can be used to interpret a very interesting chapter in Czech economic history.

The book is divided into six chapters, and each chapter compares small-scale and large-scale privatization, as well as the privatization of agricultural and forest property and land. Both the course on the progress, and its positives and negatives with respect to the Czech Republic, are carefully analysed.

In the opening section of the book the author deals with individual economic theories which have an influence on the progress of privatization. It's an explanatory section relating to the theory of ownership rights, the theory of rent-seeking and the theory of government failure.

This section is followed by a chapter devoted to the legal framework, which explains the wording of individual laws, again relating to small-scale and large-scale privatization, agricultural property and forest land. Of course, this section is a mere selection of the most important laws, as the number of laws which came into existence in connection with privatization is huge. Apart from laws on the creation of institutions which managed privatization, the author also mentions laws on securities and ecological redevelopment.

The third chapter names and describes all institutions which were involved in privatization, and the roles they played. Here, for the first time, diagrams appear which capture the relationships between individual institutions, which in my opinion make orientation in the entire interconnected system much easier. As an example I would mention the diagram of institutions which participated in privatization *via* coupons, from which one can clearly see the sequence of tasks which had to be performed, as well as the number of state institutions through which privatization was carried out (for example, in this case, it involves the chain: Ministry of Industry and Trade, Ministry for the Administration of National Property and its Privatization, National Property Fund, Ministry of Finance,

Centre for Coupon Privatization). Here, among others, the author mentions the establishment (or if applicable abolition) of individual institutions, and their rights and obligations.

In comparison with the three following chapters, these three chapters are considerably shorter, because a large part of the book is devoted to macroeconomic and statistical analysis.

The analysis of small-scale privatization describes the sale of the so-called operating units by auction, which took place publicly. It names the benefits and advantages (an average 42% growth in the final price compared to the initial price), but also negative effects, which one can never completely avoid. In the case of auctions this involves the influencing of participants, secret agreements in cases involving smaller numbers of interested parties, or conflicts of interest, when the organizers of the auction simultaneously participated in the liquidation of state assets.

The process of large-scale privatization was more complicated; it differed from small-scale privatization mainly by the fact that it involved the preparation of privatization projects, whereby any person could create a competitive proposal, which was subsequently submitted to the Ministry of Privatization, and in the decisive phase it could be approved as a final privatization procedure. Public auctions, public tenders, direct sales, deposits of assets in joint-stock companies, or alternatively a combination of more than one approach, were all taken into consideration here. For example, such a situation arose with the state-owned enterprise Pramen Praha, which involved the privatization of assets with a total value of 600 million korunas, by eight various methods (again, the reader is helped by an illustrative diagram). A similar process also related to shares, where there were even more options, including the much discussed sale *via* coupons, sale on the capital market, and “gold” shares.

The most controversial method mentioned here is the sale of shares *via* coupons. On the one hand, it enabled anybody to acquire shares of a higher value than that at which they acquired them, while on the other hand the system of assigning shares to individual applicants was kept secret, and the assignment algorithm was never reliably clarified, which led to (justified) protests by both the lay and professional public. Also certainly it is worth mentioning, in addition to an evaluation of their effectiveness, all the privatization methods are accompanied by graphs illustrating the number of sales and the sums for which the units or shares were sold during the entire time horizon of privatization.

There follows a section devoted to the analysis of the development of privatized banks, which related to Česká Spořitelna, a.s. [Czech Savings Bank], Československá Obchodní Banka, a.s. [Czechoslovak Commercial Bank], Investiční a Poštovní Banka, a.s. [Investment and Postal Bank], Komerční Banka, a.s. [Commercial Bank] and Živnostenská Banka, a.s. [Trade Bank]. Here, the author sets himself four analytical goals:

- to analyse the economic condition of banks for a comparison with what some officials presented,
- to find the factors determining income from the sale of the state’s ownership interests,
- to ascertain whether the rescue of banks before the completion of privatization was appropriate,
- to analyse the effectiveness of sales, and compare income with transaction costs.

Each of the five privatized banks was characterized by something different. Česká Spořitelna [Czech Savings Bank], for example, had the greatest proportion of small savers in the market. Its condition was better than how the officials presented it; nevertheless,

because a drawn-out decade-long privatization and the issue of alleged non-performing assets it fell into a negative balance, so overall its privatization was evaluated as economically inefficient.

According to the submitted statistics, ČSOB [Czechoslovak Commercial Bank] was managed better than all the other afore-mentioned banks, but when ČSOB took over IPB's assets, which was in receivership because of the risk to the stability of the financial sector, a very controversial step was taken in the author's eyes, when the then Minister of Finance decided to pay all the arising debts and losses associated with IPB from state funds, whereby between the years 2001 and 2002 these rose to an incredible 190 billion korunas, *i.e.* half of the sum the Czech Republic used for the privatization of all banks.

As for the administration of IPB itself, the book describes it as a "textbook example of government failure". The state did not participate in the registered capital increase, lost its majority share, and thanks to that the entire ownership structure shattered. The bank was criticized and sent reminders because of its mismanagement, which eventually led to state receivership and its takeover by ČSOB (see above).

Komerční Banka [Commercial Bank], as the strongest bank in the Czech market, was erroneously regarded as a bank in a bad economic condition on the basis of the quoted data, because under the new majority shareholder there was a considerable growth in profit, *i.e.* its potential was finally properly utilized. Its privatization also did not benefit from the long ten-year period.

Živnostenská Banka [Trade Bank] differed from all other banks in almost all the monitored parameters. It focussed on private banking, and its balance sheet total and number of clients were considerably lower, which is why the privatization process was also significantly shorter than that of other banks and lasted only one year. No bad shareholder decisions were made here, and the bank did not have to be financially supported by the state in any way.

In addition to the literature used and a list of the abbreviations and laws used, the section Appendices also contains lists of gold shares, materials for preparing analyses for debt recovery, and overviews of all transfers and income during the entire course of the privatization.

To conclude, I would like to state the most important strengths of the reviewed publication:

- **a very ambitious goal in terms of the breadth and depth of research**

The author's goal "*The aim of this monograph is the preparation of basic theoretical starting points and the testing of the practical applicability of renowned economic fundamentalists' relevant theories, the structured analysis of the legal framework, institutional securing, own development, and the macroeconomic and statistical analysis of the privatization process as a whole. The afore-mentioned structured analysis system is applied independently to individual processes realized by the Ministry for the Administration of National Property and its Privatization of the Czech Republic, National Property Fund of the Czech Republic, Ministry of Finance of the Czech Republic and the Land Fund of the Czech Republic*", stated by the author in his foreword, has been completely fulfilled.

Zeman chose a very attractive but also demanding theme for his publication. The name suggests that it is an ambitious synthesis of one of the most important themes in the current stage of economic policy.

- **quality of the professional economic terminology, stylistic level and linguistic apparatus**

Despite the demanding national economic theme, the highly complex structure of the work and the intricate synthetic concept, Zeman's work is comprehensible, interesting and readable for members of both the lay and professional public.

- **consistent application of the systemic approach of analysis and synthesis**

From my perspective, I have to greatly praise the author's open, courageous, uncompromising and strictly systemic attitude. The author very consistently applied a systemic approach to the processing of statistical data, or more precisely its acquisition, classification and subsequent analysis. The author managed to successfully analyse a very complex theme on a comprehensive synthesis plane. He is able to separate the important from the unimportant, and process the entire examined 20-year time interval into a comprehensible form, which no author has managed to do so far and which attests to the author's excellent knowledge of the examined issue.

- **quality and scope of appendices**

The difficulty of preparing the publication is also shown by 9 appendices, which on 43 pages among others contain 19 tables, forming the basis for the extraordinary number of 116 graphs included in the publication.

- **the clear logicity and comprehensibility of the structure**

Although the examined issue is highly complex and extensive, the author has managed to create a very logical and clear structure which has extraordinary explanatory capability.

- **the professional, or alternatively scientific, contribution of the work**

Practically all the data and text is original and unpublished so far, which in relation to the other parameters evaluated above reflects the highly professional and scientific value of the work; thus, I must state that it is a significant contribution to the modern national economic history of the Czech Republic, whose value will probably only be appreciated sometime in the future. I am sure it can be assumed that this publication will be difficult to surpass in the future in terms of the breadth and depth of research, the volume of the processed data, and its professional contribution, mainly due to the difficult accessibility of materials and data which the author collected and processed for over 20 years.