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The effect of the transition from a communist to a market-based economy on enterprises in the Czech Republic

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THE EFFECT OF THE TRANSITION FROM A COMMUNIST TO A MARKET-BASED ECONOMY ON ENTERPRISES IN THE CZECH REPUBLIC

BY

ANNE MILLS

A doctoral thesis

submitted in partial fulfilment of the requirements

for the award of

Doctor of Philosophy - Ph.D.

of the Loughborough University of Technology

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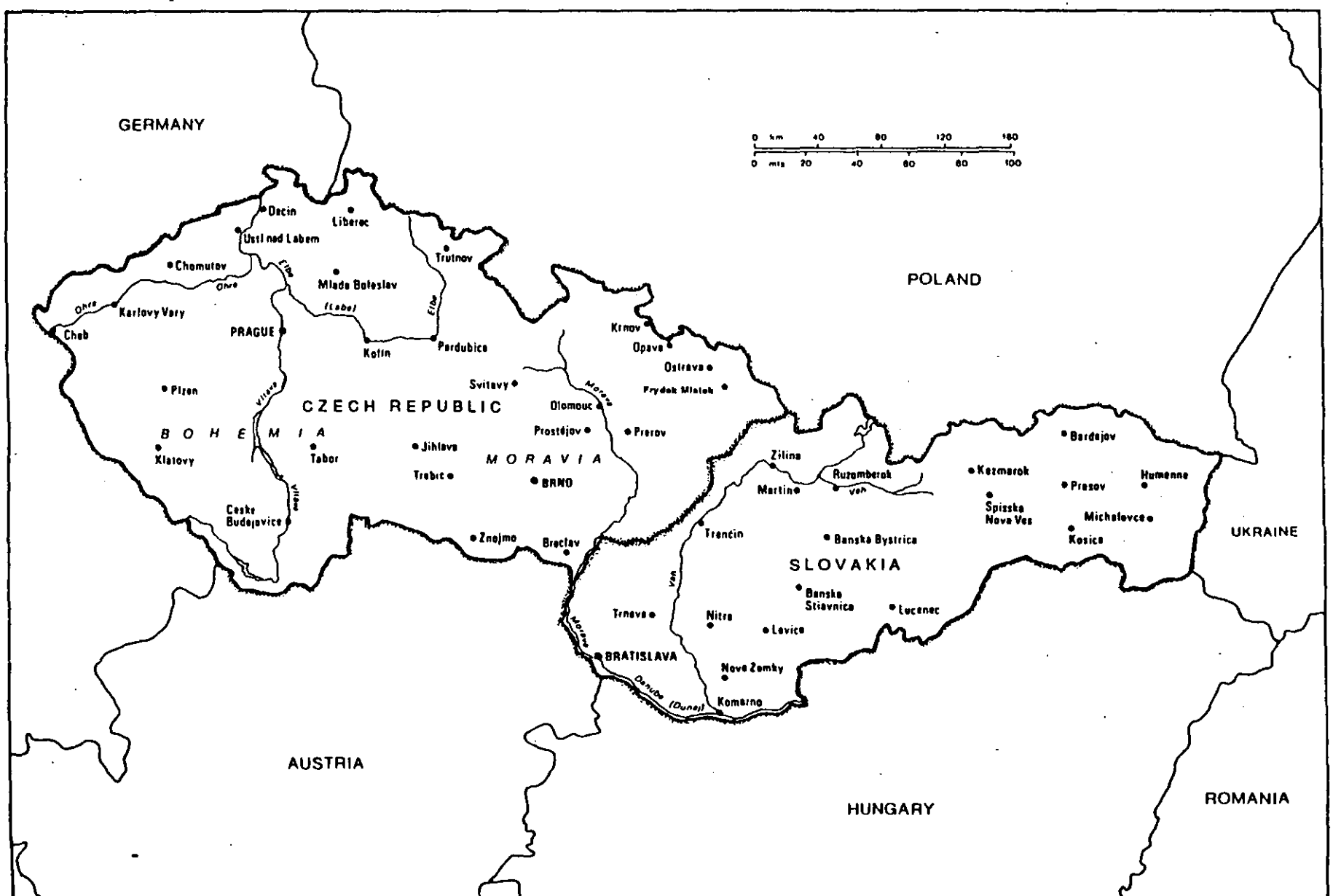

'A Great territory of unanswered questions and unresolved contradictions, a region of half-demands which until now have enjoyed as little realization as proposals counter to them, and which seem products of visionary caprice because they aim at something whole, something new and enormous'

Bruno Bauer (1854)

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CHAPTER 1

RATIONALE

INTRODUCTION

As the recent events in Eastern Europe have unfolded, it would appear that the comments of Bauer are as valid now as they were some one hundred and fifty years ago, when another great wave of revolutions engulfed central Europe in 1848. Even today, the elusiveness of this 'visionary caprice' remains an enigma to many outside observers as, yet again, international events thrust the region into the centre of the political stage, where it has 'performed' many times over the centuries.

Indeed, such has been the impact of the demise of communism on the nature of global affairs that, when historians come to identify the key landmark events of the twentieth century, there is little doubt that the year 1989 will be foremost amongst them.

The raising of the 'iron curtain' has presented researchers with many opportunities in the fields of politics, economics and the social sciences to study the phenomenon of communism and its aftermath. This doctoral thesis is the outcome of one such research study.

RESEARCH QUESTIONS

The nature of the political, economic and social changes currently taking place in the former Communist Bloc countries of Eastern Europe are unprecedented in terms of their scale, speed and scope. Since 1989, in most of these former Communist Bloc countries, a peaceful revolution has begun whereby all aspects of these societies in terms of the political economic and social structures which supported the communist regime are being dismantled. In their stead a totally new order is being established, which will underpin the development of a market-based economy similar that of Western European nations. This complex transformation is exacerbated by the temporal dimension of the change process. Each nation, as a whole, must advance simultaneously, in line with the democratic western societies with whom they are seeking to align themselves.

Within the context of the changing framework of Eastern Europe, this doctoral thesis will seek to address the fundamental question of the nature of macro economic market-based model which is likely to evolve in the Czech Republic. Is there sufficient congruence between the nature of Czech society, in terms of its political and economic development and existing western market-based economic models so that an external system can be successfully adopted in the Czech Republic? Alternatively, have the culture, traditions and communist legacy of the

region differentiated it sufficiently from western societies to the extent that an alternative economic model is likely to evolve in the Czech Republic?

In seeking to answer these questions, an analysis of Czech society will be undertaken in terms of its historical, nationalist, political and economic development up to the end of the communist regime in 1989. Thereafter, the main economic post-liberalisation measures, in relation to macro and micro economic strategy, will be considered. This area has been the main focus of change since the beginning of transition process, and consequently, has provided the richest source of research information for analysis and evaluation. However, to the extent that macro economic policy is a function of the political ideology of the nation, those areas of political change which impact directly upon the nature of the economic transition will also be considered. Through an analysis of the dynamics of the political and economic changes, conclusions will concern the extent to which existing market=based economic models are appropriate to the Czech situation.

At a micro level, the research will consider the nature of the organisational development, adaption and change required of both newly established companies and former state-owned enterprises, if they are to survive in a market-based economy. In this context, the strengths and weaknesses of the enterprises in terms of the communist

legacy, together with the threats and opportunities presented by the rapidly changing environment, will also be analysed. The evaluation process will consider the possible outcomes for these emerging and transforming enterprises within the new order.

Choice of country

Czechoslovakia has been chosen as an especially appropriate country within which to study the nature of the transition process for several reasons. When the Czech and Slovak Federal Republic dissolved itself in 1992, the Czech Republic continued the polices of the former federation, which was considered to be at the forefront of the transition to a market-based economy. The former German Democratic Republic is the most advanced, primarily, as a result of its re-unification with West Germany. The Czech Republic, Poland and Hungary are classified as the second tier of the most advanced reforming countries in the region. The remainder of the countries in the former Communist Bloc in Eastern Europe are seen to be progressing at a significantly slower rate in terms of the transition from a communist to a market-led economy.

Time period of the research

The duration of the study of the transition process encompasses the period from the fall of communism in

November 1989 to November 1994. This is considered to be a timespan of sufficient duration to allow a meaningful evaluation of the initial transformation period.

The major statutes which relate to the political and economic re-structuring of the region are in place as at Autumn 1994. The privatisation process has been completed.

Thus the emerging political and economic frameworks are sufficiently developed to allow formulation of tentative conclusions concerning the effectiveness of the process to-date, i.e. Autumn 1994, and predictions concerning the future.

There are also certain unique aspects of the Czech Republic which make it of interest from a research perspective. The Czech Republic was the only country in the region with any serious democratic traditions. It was formed as a democracy in 1918, and remained so until the Nazi invasion of 1938. Additionally, it was one of the most highly developed industrial nations in Europe, whilst the remaining countries which were to form the Communist Bloc were primarily agricultural. Thus the progress of communism did not relate to the evolution of an industrial base from an agrarian economy. This led to significantly different outcomes within the former Czechoslovakia in relation to the implementation and outcome of communist policies.

Additionally, the researcher was presented with the opportunity to lecture on Diploma in Management Studies and MBA post graduate programmes at the University of Economics in Prague. This afforded the opportunity to access information and set up networks of contacts which facilitated the progress of the doctoral research.

CONCLUSION

The study of post-communist societies in Eastern Europe is a relatively new area of research. Moreover, the time span over which it has been possible to study the phenomenon of transformation since liberalisation is relatively short. These constraints place this doctoral thesis in the early stages of research into the nature of emerging market-based economies in Eastern Europe. It is to be hoped that the findings of this study will be seen as contributing meaningfully to the debate into this new and unfolding area of research.

CHAPTER 2

METHODOLOGY

SCOPE OF THE RESEARCH

The timescale encompassed by this doctoral these comprises the period from November 1989 to November 1994 - the first five years of the transition process in Eastern Europe. The study will initially focus on an analysis of the Czech and Slovak Federal Republic from its inception in 1989 to its dissolution in December 1992. Thereafter, the Czech Republic will be studied for the period from January 1993 to November 1994. As the policies initially formulated during the period of the Federation have been continued by the now independent Czech Republic, it is possible to identify trends and to evaluate developments over the whole of the five year period being studied. As was previously stated, however, with regard to Slovakia, the economic policies this state has pursued since independence have not been within the broad parameters of the transition to a market-based economy. Consequently, the development of Slovakia beyond 1992 is beyond the scope of this research study.

CONSTRAINTS

The methodologies available to the researcher are somewhat constrained by the nature of the research topic chosen. The events which have unfolded in the Czech Republic (and the other countries of the former Communist Bloc) over the past five years are, historically, unprecedented. It is not possible, therefore, to identify relevant precedents which can be analysed and questioned to formulate meaningful hypotheses concerning the recent changes in the Czech Republic. This thesis, therefore, will form part of the initial body of research in this field and, as such, will contribute to the development of new concept and hypotheses in this area of research.

It is difficult to undertake a contemporaneous comparison with other Eastern European countries undergoing a similar transition to a market-based economy. Each country is a unique entity in national, historical and cultural terms. Additionally, all are undergoing the transformation process from different economic and political starting points, and within the context of their unique historical heritages.

Another significant challenge in undertaking any study in a foreign country presents itself in terms of a series of semantic and culture filters, through which information must pass, before it is analysed and interpreted by the researcher. This is especially true of the Czech Republic

(and other former communist countries) where business-related concepts, as well as the relevant language and terminology, are alien to much of the population.

CHOSEN METHODOLOGIES

Within these constraints, the methodologies undertaken by the researcher comprised the following areas of primary and secondary research:

> primary research in the form of case studies, structured and unstructured interviews, questionnaires and observation.
>
> secondary research focusing on the relevant literary sources in terms of texts, journals, newspapers and available survey sources together with statistical analyses, where appropriate.

PRIMARY RESEARCH

Case Studies

The case studies contained in the text were analysed by means of the 'grounded theory' approach, whereby concepts relevant to the thesis were identified, coded and analysed. However, when using the case study method, cognisance was taken of its limitations as a research tool. These

constraints relate primarily to the limitations associated with the formulation of general hypotheses or conclusions based upon the analysis of individual enterprises. However, such analyses are still of value to the researcher in terms of the provision of supporting evidence for wider assertions. Additionally, case study analysis can also highlight indicative trends which may prove worthy of more detailed research.

Moreover, due to the unreliability or lack of availability of official information concerning the previous regime, individual case examples are often the only sources of information available to the researcher. Availability of information in the new order continues to be problematical, as the transition process is still in progress.

Structured and unstructured interviews

Structured and unstructured interviews were conducted with Czech nationals and foreigners, and carried out in both Czech and English. The interviews in the Czech language were conducted by means of an interpreter from the Prague University of Economics. The interpreter in question was a highly respected professor, as a result of which, some of the potential cultural barriers to the effective flow of information during the interviews were minimised.

Questionnaires

A small number of questionnaires were distributed by the researcher. The logistics of translation and distribution of a wide number of such questionnaires precluded a survey of any great size. Moreover, in general, the issue of questionnaires and responses take on a peculiar significance in Eastern Europe, which does not apply in the West. Under the old regime, forms and questionnaires had to be completed by individuals for any change they wished to make in any aspect of their lives, from changing jobs to travel abroad. Not unexpectedly, therefore, there is now an aversion to voluntarily competing such forms.

In this context also, the use of language and terminology with which people are conceptually unfamiliar is an additional complication to survey completion. Nevertheless, the small sample of surveys carried out amongst specific groups did yield useful insights and information.

Direct observation

The researcher has visited the country on numerous occasions over the period from 1991 to 1994. This has enabled a temporal dimension to be added to the direct observation of the changes taking place in the region. The highly visible impact of many of these changes, together

with those aspects of the country which are apparently unaffected, provide interesting areas for contrasting analysis. Those visits to the regions outside of Prague provided especially valuable insights in this regard. Additionally, observations were made of the changing patterns of social interpersonal behaviour amongst people, as they emerge from the behavioral constraints of the communist regime into the greater freedom of expression characteristic of democratic systems.

SECONDARY RESEARCH

The main secondary sources used in this research will be discussed in the literature review. In general, whilst textbooks provided valuable sources of information in respect of the previous regime and the general history of the region, discussions of the more recent transitional issues tend to be found in conference papers and journal articles. Substantive academic texts are only now beginning to emerge. These tend, however, to be composite texts encompassing all the main countries of the former Communist Bloc. Consequently, depth of specific country analysis is frequently sacrificed to wide scope or coverage. The relatively few specialist texts concentrating on the former Czech and Slovak Federal Republic, and latterly, the Czech Republic do analyse the issues in greater depth.

Statistical analysis

The applications and analysis of statistical data had to be undertaken with a degree of caution, due to the fact that little credibility can be accorded the data supplied during the communist era. Since 1989 the has been a reclassification of data (especially in relation to economic performance) into categories which are broadly comparable for international reporting purposes. This of course tends to reduce the comparability of pre-liberalisation statistical data. The dissolution of the Federation in 1992 further disrupted the collation of information and classification of data, thus limiting meaningful comparisons of data over time. Additionally, there still remains in Eastern Europe generally a lack of sophisticated statistical gathering and reporting techniques which necessitate caution in interpreting data.

CONCLUSION

These limitations to the effectiveness and validity of a number of the main methodologies have necessitated constant cross-validation of data from a variety of sources to ensure validity and authenticity in analysing and interpreting information.

CHAPTER 3

LITERATURE REVIEW

The review of the literature, in relation to this doctoral thesis, will be analysed within the following framework:

EASTERN EUROPE

A study of the region will provide the wider political, economic and cultural framework necessary for a fuller understanding of the complexities associated with the development of the former Czechoslovakia, the Czech and Slovak Federal Republic, and, thereafter, the Czech Republic: the analysis of the literature relating to Eastern Europe will be reviewed chronologically, as the historical events in that region lend themselves well to this treatment.

The texts considered under this heading are, primarily, of a composite nature, in which wider issues are discussed. Additionally, they usually contain a chapter on each of the countries within Eastern Europe. Such texts are of value when studying the Czech Republic, as they set the events in that region within a wider context. In some cases though, this is done at the expense of a more detailed analysis of the specific countries. However, when read in conjunction with the country specific texts, these works, undoubtedly

add to the reader's overall understanding of the nation being studied.

THE FORMER CZECHOSLOVAKIA, THE CZECH AND SLOVAK FEDERAL REPUBLIC, THE CZECH REPUBLIC

The development of the country will be analysed in order to identify the main trends and issues which have shaped the country's past in part so that predictions can be made about the future. Although some of these texts will be analysed chronologically, the majority of the writings will be classified thematically, in relation to the crucial historical events which have influenced the development of the country.

ORGANISATIONAL DIMENSIONS

It is important to understand the impact of the external environment on organisations within the region, and their likely responses to the dramatic transformational changes they are required to undertake.

UNDERLYING PHILOSOPHICAL CONCEPTS

An appreciation of the philosophical foundation of Marxism is fundamental to the understanding and interpretation of past events, and the prediction of possible future developments in the region.

EASTERN EUROPE

The time periods delineated in the review of the literature on Eastern Europe comprise 1848 to 1989, the period between two major revolutions in Europe, and 1989 to 1994, from the beginning of liberalisation to the end date of the research for this doctoral study.

EASTERN EUROPE UP TO 1989

To appreciate the complexity of Eastern Europe generally, and the unique political, economic and cultural development of both the Czech Republic and Slovakia, it is necessary to understand something of the political history of 19th century Europe, especially in relation to the Austro-Hungarian empire and the Hapsburg monarchy. In this sphere, the works of A.J.P. Taylor, notably, The Struggle for Mastery in Europe (Oxford University Press, 1971) and The Hapsburg Monarchy 1809 - 1918 (Penguin, 1990) remain excellent analytical sources of the complex political intrigue, which pervaded the region at this time. These texts are also relevant in helping the reader to appreciate the significant cultural impact of the Austro-Hungarian sphere of influence on Europe, in general, and upon the regions of Bohemia, Moravia and Slovakia, in particular.

In relation to the subsequent inter-war period from 1918 to 1938, the seminal work for providing a full historical

framework for the understanding of events in Eastern Europe during that time, undoubtedly remains East Central Europe Between the Two World Wars by J. Rothschild (University of Washington Press, 1974). The depth and quality of analysis in relation to Czechoslovakia, especially concerning the political issues and ethnic problems experienced in the region, are commendable.

Chronologically, the subsequent books on Eastern Europe concentrate on the period 1945 to 1988, from the descent of the 'iron curtain' to the fall of the Berlin Wall.

An excellent starting place for appreciating the full impact of the events during this period, is the second of the works on Eastern Europe, by J. Rothschild, Return to Diversity: A Political History of East Central Europe Since World War Two, (Oxford University Press, 1989).

The following writings, which discuss Eastern Europe under communism and the influence of the Soviet union were produced towards the end of the communist era. As such, they encompass a longer time span over which to undertake commentaries and discussions. Additionally, both works we are about to cite adopt contrasting approaches. One is a single-author text which adopts a thematic approach to the subject, whilst the other is a multi-author work, which combines discussion of wider East European and international issues with individual country perspectives.

The first is the comprehensive single-author study of the period carried out by J.F. Brown, in Eastern Europe and Communist Rule, (Duke University Press, 1988). This well-structured writing analyses the phased structures in the development of communism in the region and its wider implications for east-west relations.

The second text, Central and Eastern Europe: The Opening Curtain? (Westview, 1989), edited by W.E. Griffiths is an interesting study, which was produced under the auspices of the East-West Forum in Washington. This institute is a research and policy analysis organisation which aims to bridge the gap between scholarship and policy formulation. The quality and composition of the writings in this book successfully reflect that aim. The main focus of the discussion is the changing political and economic relationship between the Soviet Union, Eastern Europe and the West. In this regard, it is informative, analytical and well researched. Additionally, the range of country contributors is highly varied in terms of nationality and field of expertise. This is reflected in the variety of themes discussed in the text.

It is interesting to note, however, that in predicting the future directions of east-west relations there was no vision of the future events of 1989. Indeed, in the essentially historical and descriptive chapter on Czechoslovakia, written by H. Gordon Skilling, the

conclusion is that:

> there seems little prospect that Czechoslovakia will emerge from the thrall imposed on it by the East in 1948, and again in 1968, or that anything resembling the Prague Spring will occur again in the near future (p.261).

Evaluations of the whole period of communist domination in Eastern Europe are to be found in a plethora of texts which were published after the liberalisation of 1989. They sought to offer a wider analytical perspective on the forty years of communist rule in the region, and to analyse the reasons for its failure. Some of these publications will be discussed in the next section.

Throughout the communist regime, however, probably the best source of information and commentary on developments within the Soviet sphere of influence are the weekly research papers and publications from Radio London/Radio Free Europe. These journals are an excellent source of relevant information and balanced analysis on all the social, economic and political developments in all the countries of Eastern Europe. Their use of specialist experienced journalists, such as Jan Pehe and Timothy Garton Ash, who are both acknowledged experts and astute observers of events in Eastern Europe, generally, and Czechoslovakia in particular, ensure an ongoing quality of sound journalism.

The quality of these publications has indeed continued into the post-communist era in Eastern Europe. The commentaries continue to be informative and balanced, in terms of their interpretation of events and representation of differing views. The annual reviews of the developments in individual Eastern European countries, published at the end of each year, are especially helpful in terms of interpreting trends, and putting events into perspective.

POST-LIBERALISATION EASTERN EUROPE FROM 1989 TO 1994

The studies of Eastern Europe since the beginning of the transition process have tended to follow four main stages of chronological analysis.

The initial range of publications focused upon the events surrounding the fall of communism. These were succeeded by publications which sought to take an overview of the whole communist era. In their analyses, these texts attempted to identify the reasons for its failure, and to raise the issues to be addressed in the post-communist future of these regions. These studies were in turn succeeded by debates over the speed at which the transition to a market-based economy should be undertaken. As the transition process itself developed, the focus of discussion has again progressed to the consideration of the implementation of the privatisation process in the former Communist Bloc countries. As it is now approximately five years since the

commencement of the transition process in Eastern Europe, discussions are now entering the reflective stage, whereby the reality of events is being considered against initial expectations and evaluations.

The Legacy of Communism

A major source of publications relating to the communist era and its immediate aftermath is the Centre for Strategic and International Studies. This institute was founded in 1962 as an independent, tax-exempt public policy research institution based in Washington D.C. The mission of the Centre is:

> To advance the understanding of emerging world issues in the area of international economics, politics, security and business.
> (Aslund, 1992, p.i).

A valuable work in the provision of the analysis of communism, published in association with the Institute is <u>The Bloc that Failed: Soviet-East European Relations in Transition</u> (Indiana University Press, 1990) by C. Gati. Additionally, the Centre produces the Washington Papers, an occasional series of publications which are:
'intended to meet the need for an authoritative, yet prompt, public appraisal of the major developments in world affairs'.

Of particular value to the study of Eastern Europe in this regard is V. Sobell, The CMEA in Crisis: Toward A New European Order (Praeger, 1990).

A comprehensive and well researched political analysis of this period is contained in J.M. Young Cold War Europe 1945-89: A Political History produced by (Edward Arnold, 1991). In contrast, P. Brogan author of Eastern Europe 1939-89: The Fifty Years War (Bloomsbury, 1990) produced a relatively lightweight, descriptive overview of events in the various countries of Eastern Europe for the period being discussed.

Another publication which immediately followed the fall of communism, but considered the future as opposed to evaluating the past, was G.Merrit Eastern Europe and the USSR: The Challenge for Freedom (Kogan Page, 1990). Published in association with the Office for Official Publications of the European Community: this was a perceptively analytical and well-informed treatise on the problems facing post-Communist Russia and Eastern Europe.

The Revolutions of 1989

The immediate post-liberalisation saw a group of journalistic paperbacks emerge which essentially told the emotive story of the revolutions in Eastern Europe, in chronological order of the onset of political change.

We The People: The Revolution of 89 (Granta, 1990) is essentially a fascinating eye witness account of the sequential collapse of the communist regimes in Eastern Europe. Given the authoritative knowledge and experience of the author, Timothy Garton Ash, this text incorporates a depth of knowledge and understanding beyond that of the descriptive. W. Echikson, author of Revolution in Eastern Europe: Lighting the Light (Pan, 1990) focuses in more detail upon the personalities who contributed to the collapse of Eastern Europe, as well as a detailed account of the events themselves. Two multi-author works that take a more thematic approach to Eastern Europe comprise E Gwyn Prins Spring in Winter: The 1989 Revolutions (Manchester University Press (1990) and Eastern Europe...Central Europe..Europe (Westview Press, 1991) edited by S.R. Graubard. The former of these two books attempts to identify salient themes and problems within the respective countries studied, bridging the gap between a communist past and an unknown future. The latter work is of a more philosophical nature, where renowned experts on the respective countries attempt to relate dominant country themes to the notion of a middle Europe culture and psyche.

There are many dimensions along which it is possible to analyse and classify the literature relating to Eastern Europe in the post liberalisation period. From the perspective of this thesis, the dimensions, which relate directly to the issues being discussed, comprise speed and

direction of economic change, the privatisation process, and an overall reflection and analysis of the changes over the period 1989-94. These themes are a reflection of the literature following the chronology of events as they have unfolded in the region.

Speed of economic change

The initial debate concerning the speed at which the transition process should take place was discussed in journals. In the United Kingdom, the Oxford Journal of Economic Policy published a series or articles which discussed this issue from a variety of economic perspectives. In the United States, the Columbia Journal of International Business produced a series of articles which discussed different perspectives on the debate.

One of the initial works which discussed the wider framework of the overall macro transition process is G Blanchard et al. Reform In Eastern Europe (MIT Press, 1991). The text was prepared under the auspices of the World Institute for Development Economics Research (WIDER), a research and training centre of the United Nations University, whose role is to provide:

> an independent, outspoken, and thoroughly professional academic analysis, on an annual basis, of a topic of major relevance to the world economy (p.vii).

The text strongly reflects the views and perspectives of the school of economic thought, which promotes the development of a neo-liberal economic philosophy in the region together with the view that the transition process should be effected as quickly as possible. The basis of the strategies proposed in the text are based upon previous experiences in South America, with little analysis having been undertaken of the countries of Eastern Europe. Indeed the speed with which the text was produced, after the revolutions of 1989, indicate that there would not have been sufficient time to undertake an in-depth country analysis of the regions, for which they were recommending the transition policies.

Additionally, the text recommends the same range of measures for each of the former communist countries of Eastern Europe, irrespective of the diversity of cultures, history and economic development which exists between them. It is therefore only a very general overview of the transition process in Central and Eastern Europe.

The proponents of a slower, incremental pace of economic transition are represented most strongly by A. Kornai, who discusses the debate in The Road to a Free Economy (Norton, 1990). The view expressed in this text supports the notion of gradual evolutionary change managed by the state. It is

believed that, as the economy becomes stronger and more self-sufficient, the role of the state will gradually diminish, and ultimately, wither away.

Privatisation

Subsequent substantive works have opened up the debate to consider the problems of privatisation, with its implications for property ownership and issues of governance. The Central European University Privatisation Project has produced the most substantial and theoretically based texts on this issue. The Privatisation Process in Eastern Europe by Frydman et al. (Central European University Press, 1993) provides an excellent outline for understanding and describing the complex variants of the privatisation process in the respective Eastern European countries. This publication shows commendable attention to relevant detail, and accurate descriptions of complex phenomena. It is, essentially, an explanatory work, which is designed to aid understanding, rather than a discussion on the wider philosophical and theoretical debates underlining the transition process. These issues are discussed in Privatisation Eastern Europe: Is the State Withering Away? by R. Frydman and A. Rapaczynski (Central European University Press, 1994). In the wake of the emotive journalistic publications and the more general discussions of the way forward for Eastern Europe, this is one of the first books that seek to discuss the underlying

issues of the theory and practice of corporate ownership, and provide a systematic approach for considering the issues of the transition process.

The Centre for Strategic and International Studies, in the series Creating The Post-Communist Order, has produced an interesting pamphlet by A. Aslund entitled Post-Communist Economic Revolutions How Big a Bang? (1992). This provides a helpful overview of the implementation of economic policy reform measures in the main countries in Eastern Europe. However, insofar as it encompasses only the very early stages of the transformation process, the value of the analyses is rather limited. In relation to the speed of economic transition, it very eloquently outlines the arguments supporting both the fast and gradual approaches to the implementation of the reform policies. Although the writer favours the faster approach the discussion does provide a more balanced perspective than that of Blanchard et al., which has been previously mentioned.

Reflective works

The recently published multi-author text Economic Transformation in Central Europe - A Progress Report (Central European University Press, 1993) edited by J. Portes is indicative of the phase of consolidation, reflection and thinking in relation to the transformation in Eastern Europe. The chapters relating specifically to

the Czech and Slovak Federal Republic are especially well argued. The chapter by Jan Svenjar evaluates the differential impact of the transition process on The Czech Republic and on Slovakia respectively. Additionally, the statistical analysis covers the period commencing 1985, and consequently permits a wider perspective on the transition process. In the chapter on the Czech and Slovak Federal Republic written by V. Kamarek the problems faced by the country in attempting to implement its economic reform programme are well analysed within a context, which takes cognizance of the unique cultural characteristics of the nation. The chapter which highlights the general issues to be addressed by all of the countries in the region provides a realistic appraisal of the difficulties they face during the transition process.

One of the most critically reflective analytical studies of the transition process has been that of Transforming Socialist Economies by M. Myant (Elgar, 1994). The author goes beyond the prescriptive parameters of the transition measures to undertake a wider evaluation of the nature of the transformation process in Eastern Europe at a wider political and economic level.

Another source of publications which are more reflective and analytical in relation to the discussion of the transition issues in Eastern Europe has been produced in the series Creating The Post-communist Order: Post-

communist Politics - Democratic Prospects in Russia and Eastern Europe (Washington, 1993) by M. McFaul, which discusses the emerging political systems in the various post- communist countries and assesses the future prospects for democracy in the region.

CZECHOSLOVAKIA, THE CZECH AND SLOVAK FEDERAL REPUBLIC AND THE CZECH REPUBLIC 1918-1994

CZECHOSLOVAKIA 1918 - 1989

Much of the literature relating to the former Czechoslovakia is to be found as noted at the outset in the composite texts which encompass the whole of Eastern Europe. There are, however, certain specific works which analyse the former Czechoslovakia chronologically, whilst others focus upon the critical events and issues, which are considered to be the main 20th century historical landmarks of Czechoslovakia.

In chronological sequence, Czechoslovakia at the Crossroads of History by J. Krejic (I.B. Taurus & Co. Ltd., 1990) traces the history of Czechoslovakia from the development of Christianity in the region to the demise of communism. This is achieved by analysing the course of events which marked the critical turning points in the development of the Czech and Slovak nations. Similarly, in much more precise analytical detail, R.W. Seton-Watson's, work A History of The Czechs and Slovaks (Archon, 1965) traces the development of the region up to the early 1960s.

J. Korbel's book entitled Twentieth Century Czechoslovakia: The Meaning of its History provides a wide-ranging detailed description of the way in which the communist system permeated all aspects of political, social and economic life in the region. The author perceives the outcomes of the system in a very negative way. This approach contrasts with that of J. Kalvoda whose book Czechoslovakia's Role in Soviet Strategy (Washington 1978) produces an analytical and comparative study which focuses upon the relationship between Czechoslovakia and the Soviet Union. Z. Krustyfek, in his book The Soviet Regime in Czechoslovakia (Boulder, 1981) provides a mainly economic perspective on Czechoslovakia up the end of the 1970s, in which he highlights the trends of potential economic decline, as a result of Soviet enforced economic and social policy.

An interesting work which focuses on Czechoslovakia for the period from 1945 to 1988, has been produced by H. Renner entitled History of Czechoslovakia Since 1945 (Routledge, 1989). This is a highly emotive offering which describes key personalities and events over the period covered by the publication. The use of dialogue, original documents and detailed descriptions make this book and interesting contrast to the more analytical detailed approach of the other texts.

The most informative book on the post-war economic performance of Czechoslovakia under communism is,

undoubtedly The Czechoslovak Economy 1948-88: The Battle for Economic Reform (Cambridge University Press, 1989) by M. Myant. This comprehensive work analyses the process whereby the Czechoslovak economy was re-structured to meet the requirements of the Soviet Regime. It also integrates the political and social dimensions of communism with the economic development of the region to create a wider perspective on the nature of the regime during this period.

A number of interesting works have been generated, which focus on the critical events in the history of Czechoslovakia. These comprise the nationalist question, the ethnic issue, the communist takeover of the country in 1948, the Prague Spring of 1968, and the Charter 77 movement.

The Nationalist Question

The nationalist question, which discusses the nature of the relationship between the Czechs and Slovaks, is well and objectively discussed from the Slovak perspective in National Conflict in Czechoslovakia by C.S. Leff (Princetown University Press, 1988). This highly detailed analysis provides interesting statistical analyses and interpretations of the development of the Slovaks. It also provides a balanced Slovak national perspective, which is frequently subsumed in wider analytical discussions of the historical development of the region. Such discussions

tend to view events from the perspective of Czechoslovakia as one nation, in which the Czech culture is dominant.

This well structured objective approach contrasts sharply with that of Slovakia and the Slovaks (Washington, 1977) written by J.A. Mikus. This study portrays Slovakia in terms of the romanticised struggle of a small nation trying to achieve a national identity. The rhetorical language, and omissions of less glorious aspects of the Slovak nation's history, together with the interpretative sketches of Slovak heroes through the ages, reflect this bias.

Beyond these texts, little discussion of the underlying cultural differences between the two regions, which were ultimately to lead to the dissolution of the Czech and Slovak Federal Republic in 1992, is to be found in the literature produced prior to 1989.

The Ethnic Issue

The issue of ethnic minorities, especially the large German population of the Sudeten lands is of special interest to the extent that it relates to the events surrounding the commencement of the Second World War. An interesting discussion of this issue, and the wider international implications surrounding it, is to be found in The German Minority Problem and British Appeasement Policy (Cambridge University Press, 1973) by J.W. Bruegel.

Whilst the main chronological texts listed above discuss the events surrounding the communist takeover of 1948, The Communist Subversion of Czechoslovakia: The Failure of Co-existence (Princetown University Press, 1959) by J. Korbel provides the most comprehensive analysis of the actual takeover. This book is of value in that it uses the Czechoslovakian example as a means of illustrating the strategies and techniques employed by the communists to take over the country. It is an interesting supplementary study when considered in conjunction with those writings which analyse international Soviet strategy during this period.

The Prague Spring 1968

The Prague Spring of 1968 is, perhaps, the most widely known example of Czechoslovak defiance of the Soviet regime. Whilst numerous descriptive and some emotive texts have been written about this event, the most detailed comprehensive analysis of the events surrounding the Prague Spring and its aftermath is, undoubtedly, Czechoslovakia's Interrupted Revolution (Princetown University Press, 1976) by G. Gordon Skilling. This incredibly detailed work provides a month by month analysis of the events leading up to the Prague Spring. It is interesting that Skilling perceived this phenomenon as a function of Czech culture and intellectual stimulus, as well as of the economic problems which are normally considered to be the root cause

of the protest. It also contains a stimulating philosophical debate on the extent to which the Prague Spring was a political reform or revolutionary phenomenon. The author concludes that such attempts at change by a small powerless nation in the face of threats from major aggressors are bound to fail.

Charter 77

The same author also produced Charter 77 and Human Rights in Czechoslovakia (George Allen & Unwin, 1981), which discussed the only group to oppose the government of the regime. The numerous original Charter 77 documents included in this text provide rich insights into the motivation and depth of feeling of the Chartists. A valuable supporting explanatory work on the Charter 77 movement has been produced as one of the Washington Papers series, published by the Centre for Strategic and International Studies in Washington. Czechoslovakia Charter 77's Decade of Dissent (1987) by J. Bugajski takes a longer term perspective and overview of the development of the movement throughout the 1970s and into the 1980s. The well chosen synopsis of relevant Charter documents offers valuable insights into the psyche of the movement.

THE CZECH AND SLOVAK FEDERAL REPUBLIC 1989-1992 AND THE CZECH REPUBLIC 1993-1994

The short duration of The Czech and Slovak Federal Republic and the trend for literature concerning the post-liberalisation period to take the form of composite texts, have meant that relatively little has been published on the Czech and Slovak Federal Republic specifically. Probably the main dedicated work on the Czech and Slovak Federal Republic is Czechoslovakia in Transition (Pinter Publishers, 1991) by S.L. Wolchik which provides a useful summary of the historical background of the region and,subsequently, considers the political, economic and social problems facing the new regime in 1991. The book is very well researched, drawing on a comprehensive range of sources to augment the issues being discussed. The statistical analysis is also thorough and informative. The conclusions perceptively highlight the ethnic issues which were to dominate much of the short existence of the federation. They are also relatively balanced in terms of the general problems and challenges facing the country.

The Radio Free Europe and Radio London publications continue to produce specialist information and analysis of the changes in the Czech Republic, which are thorough, wide-ranging and perceptive. The weekly English language newspaper, The Prague Post, has provided the main source of recent information and quite perceptive analysis of the changes which have been taking place in the former

Czechoslovakia and the Czech Republic. Although the newspaper medium precludes in depth discussion or analyses of the major changes taking place in the region, the commentaries do seek to present a range of views on the issues being discussed.

As regards agencies for providing information, Trade Links has provided useful information especially in relation to the legislation being passed in the new regime. The Economist Intelligence Unit provides a valuable, credible and comprehensive source of macro statistical data on both the former Czechoslovakia and the Czech Republic, which enables economic trends to be more accurately identified and analysed. Even this credible source of statistical information is subject to the constraints on the validity of such data, as was discussed in the methodology chapter.

In the final analysis, however, a nation is more than the sum of its history, economic, social and political development. Each country has its own psyche, beliefs, values and culture. To gain such an understanding of the complex nature of the Czech nation, meaningful perspectives can be found in the works of Hasek, Kundera and Havel.

In very different fashions, both Jaroslav Hasek in The Good Soldier Svejk (Penguin, 1973) and Milan Kundera in The Unbearable Lightness of Being (Faber & Faber, 1986) capture the same enduring attitude to life expressed by Czechs,

whereby one bows to the inevitability that destiny determines all outcomes in life. Consequently, it is argued, there is no point in trying to fight it. Whilst Hasek uses the humour of Svejk to convey this message, Kundera uses raw sexuality and political cynicism as the chosen emotional vehicle through which to convey this helplessness. Hasek also highlights enduring Czech cultural traits by characterising Svejk as:

> a 'little man' fighting officialdom and bureaucracy with the only weapons available to him - passive resistance, subterfuge, native wit and dumb insolence (p.754).

Indeed, such observations were also made by Vaclav Havel in Living In Truth (Faber & Faber, 1986). In his essays he speaks of people living 'within a lie' (p.62), and as having:

> no roots in the order of being, no sense of responsibility for anything higher than his or her own personal survival (p.62).

Much of the blame for this behaviour he attributes to the 'totalitarian political system' (p.62). However, observations of behaviour in the former Czechoslovakia and the Czech Republic, together with the earlier observations of Hasek and the deeper soul-searching of Kundera, lead one to believe that the traits are enduring national characteristics.

ORGANISATIONAL DIMENSIONS

In studying the nature of management and organisations in the former communist societies, Management in Socialist Countries by Witzold Kiezun (De Gruyter,1991) provides an informative and incisive overview of the nature of management in the various communist societies prior to liberalisation. A subsequent book, again published by De Gruyter (1991) and edited by György Szell entitled Labour Relations in Transition in Eastern Europe, addresses a range of approaches to the changing nature of management, employee and ownership relationships in the various transforming countries. This work exhibits a sensitivity and understanding of the variations in the nature of the respective transforming societies. A more detailed focus on enterprises within the Czech Republic and Slovakia is contained in the case study publication Managing in Emerging Market Economies: Cases from the Czech and Slovak Republics (Westview, 1993) edited by D.S Fogel. Insofar as the stated objective of the author is to give:

> a glimpse of one of the most historical changes in decades by focusing on firms and the changes they are making to survive in the emerging market economy (p.viii)

this book is reasonably successful. The description of the macro economic changes in the region since 1989 is comprehensive. The cases themselves are well documented

and informative containing an exceptional level of useful statistical data. A possible weakness of the text, however, is in its failure to emphasise sufficiently the historical and cultural background of the region. There is the implicit assumption that the management decisions made, and the outcomes expected, are those which will fit into the mind set of the 'Western' manager. The reader is being asked to evaluate changes in Eastern Europe against western business and democratic traditions that are alien to many business decision-makers in the region. Overall, however, it is a valuable source.

Human Resource Management in Europe (Routledge, 1993), edited by P.S Kirkbride, takes cognizance of these cultural variations and the complex task of organisational changes and developments facing enterprises in Eastern Europe. The section which concentrates on developments in Eastern Europe provides helpful frameworks for interpreting changing problems facing enterprises, together with possible models which may be applied to facilitate the change process.

UNDERLYING PHILOSOPHICAL CONCEPTS

Any attempt to understand the nature of the communist regimes in Eastern Europe, and the legacy that remains, must begin with a consideration of the initial text upon which so much of the communist ideal was based: The

Communist Manifesto (Penguin, 1967) by K.Marx and F. Engels. Although there have been subsequent editions of this book, the value of this edition lies in the exposition of the text in the introduction by A.J.P. Taylor. Whilst the manifesto itself may seem dated, inaccurate and contradictory, the contextual framework offered in the introduction assists the reader in understanding the subsequent monumental consequences of the text.

In terms of the practical implementation of the communist ideal, a useful and informative text providing an interesting introductory overview of the nature of communism is contained in Western Capitalism and State Socialism: An introduction (Blackwell, 1988).

Re-appraisals and evaluations of the nature of state socialism prior to the collapse of communism were provided by W. Brus and K. Laski in their text From Marx to the Market (Clarendon Press, 1988). In this work, the failures of the command system were already being identified,and alternative economic models considered, prior to the fall of communism.

LIMITATIONS OF THE LITERATURE

Much of the literature focusing upon the issues of economic transition precludes the wider discussion of the political and ideological framework, within which these major changes

are taking place. In attempting to predict a possible political and economic model, within which it is possible to interpret the change taking place in the Czech Republic, Models of Democracy by D. Held (Polity Press, 1987) is a valuable source of discussion of the various democratic models. In terms of a comparative analysis two books on Italy deserve to be mentioned, A History of Contemporary Italy (Penguin, 1990) by P. Ginsborg provides a political and societal analysis of the region. Together with The New Italians (Michael Joseph, 1994), these books offer a modern summation of the most recent trends in Italian society. These exhibit many similarities with the changing society in the Czech Republic.

Or again the influence of Germany in terms of its political and economic structure is also very strong within the region. Germany - The Tides of Power (Routledge, 1992) by M. Balfour provides valuable insights into the political, economic and social development of the nation, especially the post World War Two period. These events are especially relevant to the current political, social and economic trends which are developing in the Czech Republic, given the economic and cultural proximity of the two regions. There has also been relatively little literature produced on the underlying theoretical and conceptual problems associated with understanding the nature of the change process within organisations in Eastern Europe. This is possibly a function of the short time-span which has

elapsed since the initial introduction of privatisation within enterprises.

CONCLUSION

Overall, it is still very early days in terms of the aftermath and outcomes of the Eastern European Revolutions of 1989. Like other great revolutions in history, these events and their consequences will be revisited many times by researchers and commentators from a variety of academic disciplines.

CHAPTER 4

BACKGROUND

Leontes: Where is Bohemia? Speak!
- Act v, Scene ii

Bohemia: A desert country near the sea.
- Stage direction, Act iii, Scene iii

(From A Winter's Tale, by William Shakespeare)

LOCATION

The Czech Republic is a landlocked state of some 75 thousand kilometres located at the very heart of mainland Europe. This small nation comprises the historic regions of Bohemia and Moravia. It is bordered by Poland to the north, Slovakia to the east, Germany to the west and Austria to the south. The northern and western areas of the Czech Republic, in the region of Bohemia, are relatively mountainous, especially where the country borders onto Germany and Poland. Moravia, in the east of the country, is mainly a low lying region, which has been a traditional crossing point between Poland and south-central Europe.

The border between Moravia, Austria, and part of Slovakia is formed by the Moravia river, which flows south to join the Danube. The remainder of the border between Slovakia and the more rugged and mountainous region of Eastern

Moravia is formed by the Little and White Carpathian Mountains.

HISTORICAL OVERVIEW

The Czech Republic was formed on 1st January 1993 by the break-up of the Czech and Slovak Federal Republic. The Federation was established in 1989, in the wake of the Velvet Revolution, an allusion to the peaceful end of communist rule in the former Czechoslovakia. This was followed by the re-establishment of democracy in the region after forty years of communist rule. The Czechoslovak state which preceded the Federation was established in 1918 by uniting the historic Czech kingdoms of Bohemia and Moravia with the province of Slovakia.

Throughout their history, the regions of Bohemia and Moravia, together with the Slovak Republic, have been characterised collectively as a nation at the crossroads of Europe. Geographically, culturally and economically, this region has been the centre of a contest of larger forces throughout its thousand year existence. The Holy Roman Empire dominated the region for the period from 1041 to 1648. This was succeeded by the Austro-Hungarian Empire, which ruled from that time until the commencement of the First World War. After a short thirty year period of independent democracy the country was invaded by Nazi Germany in 1938. Subsequently, following the communist

coup of 1948, Czechoslovakia became part of the Communist Bloc until liberalisation and the re-establishment of independence in 1989. At that time, the Czech and Slovak Federation Republic was formed as an sovereign, democratic nation.

POPULATION

The former Czechoslovakia comprised a total area of 128,000 square kilometres, some 49,000 of which were encompassed by Slovakia. By the time of liberalisation, the total population of the region comprised approximately 15 million, two-thirds of whom resided in the Czech lands. When the federation was dissolved at the end of 1992, the regions divided along the land and population parameters outlined above.

The main centres of population in the Czech Republic comprise the capital city of Prague, with a population of 1.2 million, together with Ostrava, Brno and Pilsen, which have populations of 328,000, 388,000 and 173,000 respectively. In Slovakia, the largest concentrations of population are found in the capital city of Bratislava, with a population of 411,000, followed by Trnava, Presov and Kosice with 233,000, 200,000 and 238,000 inhabitants respectively.

Ethnically, the region is relatively homogeneous by the

standards of Eastern Europe. In March 1991, the census of the population in the Czech and Slovak Federal Republic revealed that 9.8 million Czechs and 4.8 million Slovaks accounted for 93% of the population. The most significant remaining national groups comprise 600,000 Hungarians (mostly in southern Slovakia), and a Romany population that is estimated at around 500,000. Additionally, there are small communities of resident Poles and Germans, mainly in the Czech Republic.

INDUSTRIAL STRUCTURE

Certain regions of Moravia boast a history of industrial production dating back to the time of the Hapsburg Empire. By the time of the communist coup of 1948, Czechoslovakia was involved primarily in the light engineering and armaments industry, and was developing a thriving culture of private enterprise and entrepreneurship. Communist domination, however, saw the commencement of a period of forced nationalisation, so that, by the time of liberalisation in 1989, 98% of all industry in Czechoslovakia was state-owned.

The industrial structure of Czechoslovakia and, subsequently, the Czech Republic, on its formation in 1993, was a reflection of the communist economic policies of the preceding forty years. The system emphasised heavy machinery and arms production, supported by the development

of extractive industries. The rationale behind this policy was that of autarky, i.e. that members of the Communist Bloc should be self-sufficient to the extent that, in each country, complete products were to be manufactured from raw materials through to the finished goods stage.

Consequently, the main production areas comprised engineering and heavy industry, followed by chemical and rubber production, metallurgy and metalwork. However, the pattern of industrial development varied between the Czech lands and Slovakia. The concentration of industry in Slovakia is much narrower than that of the Czech lands, focusing primarily upon steel and armaments production, much of which was heavily subsidised by the state before liberalisation. The principle of self-sufficiency was extended to agriculture, where the region produced approximately 90% of its food requirements.

In terms of consumer goods, the Czech lands produce glass, china, automobiles, trucks and beer, whilst Slovakia produces light electrical goods. In the former Federation, Slovakia was the only producer of refrigerators, freezers and colour televisions. When the Federation was dissolved, the respective independent countries assumed control of the industries located within their respective geographical borders.

WORKFORCE PROFILE

Approximately 58% of both the Czech and Slovak populations are of working age. As a result of the communist industrial policy outlined above, the majority of workers were involved in heavy engineering and the extractive industries, as illustrated in Appendix I, which shows the structure of the workforce by sector. Overall, 38.4% of the working population in the Czech Republic is employed in industry, while 9.9% is employed in agriculture. In Slovakia the numbers employed are 32.9% in industry and 12.6% in agriculture. The Czech and Slovak workforces are regarded as well-educated and highly skilled, possessing an outstanding literacy rate of 98.9%.

POLITICAL STRUCTURE

The political and legal structure of the Czech Republic is based upon the constitution which came into force on 1st January 1993. Under the terms of the constitution the Czech Republic is defined as:

> a sovereign, unified and democratic law-abiding state, founded on the respect for rights and freedoms of the individual and citizen
> (Rutland 1994, p.274).

The political system is:

> founded on the free and voluntary operation of the political parties respecting fundamental democratic principles and rejecting force as a means to assert their interests (Rutland, 1994, p.274).

THE STRUCTURE OF GOVERNMENT

Legislative power in the Czech Republic is vested in two chambers, the Chamber of Deputies and the Senate. The Chamber of Deputies has two hundred members, who are elected for a four year term. The Senate has eighty-one members, elected for a period of six years. Every two years one-third of the senate is elected. Members of both chambers are elected by universal suffrage. At the time of completion of this thesis in Autumn 1994, the senate had not yet been elected.

The president of the Republic is the Head of State, and is elected for a term of five years by a joint session of both chambers of the legislature. On 26th January 1993 Václav Havel, the playwright and former dissident, was elected Head of State of the Czech Republic.

The Council of Ministers is the highest organ of executive power in the state. It is headed by the Prime Minister, and is answerable to the Chamber of Deputies, which was

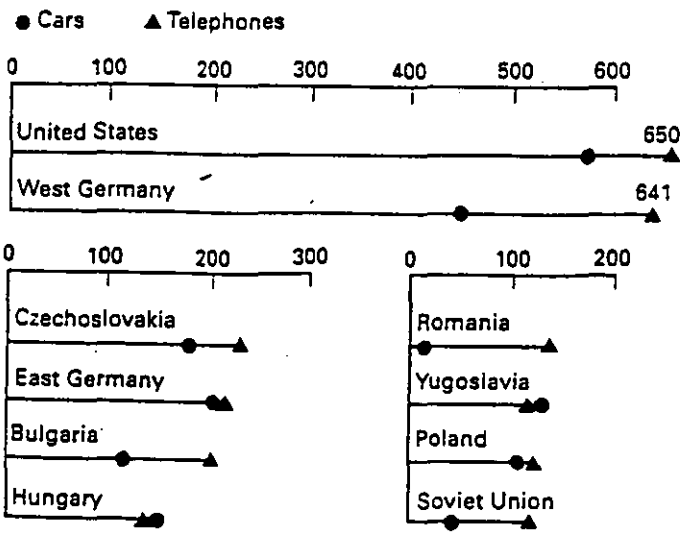
formed from the Czech National Council. During the time of the Czech and Slovak Federal Republic, the National Councils of the Czech Republic and Slovakia dealt with issues relating directly to the respective regions. The Federal Assembly, which represented the collective interests of both regions, had control over foreign affairs, defence, overall economic policy and constitutional matters. When the Federation was dissolved and the Czech National Council became the Chamber of Deputies, Václav Klaus, whose Civic Democratic Party gained the majority of votes in the 1992 elections, became Prime Minister.

LIVING STANDARDS

In terms of the living standards of the population in the former Czechoslovakia, the average GNP, based upon 1990 estimates, show that this nation was comfortably the wealthiest of the independent East European countries with a per capita GNP twice that of Poland.

Whilst such statistics must be treated with caution, the table below provides some empirical evidence of the fact that the material living standards in Czechoslovakia, although far behind the West, were higher than those elsewhere in Eastern Europe.

CARS AND TELEPHONES PER 1,000 PEOPLE



Source: KPMG (1990) Doing Business in Czechoslovakia, London, Kogan Page, p.20

Additionally, in the Federation one family in three had a weekend cottage in the country, and a fridge and colour television were the norm. Thus by the end of the communist period the Czechs were considered to be relatively well-off materially in relation to the rest of the Communist Bloc.

ENVIRONMENT

Despite the apparent comfort of the Czech population in quantitative terms, the environmental and pollution problems of the region have greatly detracted from the quality of life for the population.

The country is beset by air, water and other environmental pollution problems caused mainly by the chemical, mining,

steel and electrical power industries. A major pollutant is the sulphur dioxide which is produced by brown lignite coal, the main source of power in the region. It is estimated that the production of one kilowatt by a thermal power station using brown lignite coal emits 4.9 grams of black ash, 27.6 grams of sulphur dioxide and 4.2 grams of nitrous oxide.

In terms of the impact of this pollution on the population, it is estimated that, in the most concentrated areas of pollution around northern Bohemia and southern Moravia, that infant mortality has increased by 65% since 1960 (Economist intelligence unit (EIU), 1990, p.29).

Finally, it has to be noted that the absence of viable alternative power sources and the inefficiency and age of the power plants means that:

> lignite will remain the principal source of energy in Czechoslovakia for some considerable time with no relief in sight for the long suffering Czechoslovak environment (EIU 1990, p.29).

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APPENDIX I

LABOUR FORCE AND STRUCTURE OF EMPLOYMENT IN CZECHOSLOVAKIA, 1987-1992

Labour force

	Czechoslovakia					Czech Republic	
	1987	1988	1989	1990	1991	1991	1992
Population of working age	8,838,697	8,921,483	9,022,395	9,119,651	9,124,228	6,082,065	6,150,130
Workers of retirement age	746,641	736,224	712,027	698,593	429,529	293,644	280,267
Workers commuting outside republic	-1,006	-865	-1,051	-4,162	-3,221	-5,834	-6,619
Foreign workers	32,478	34,322	43,164	32,208	8,524	4,698	17,527
Workers from Slovakia	-	-	-	-	-	29,957	29,957
Total	**9,616,810**	**9,691,164**	**9,776,535**	**9,846,290**	**9,559,060**	**6,404,530**	**6,471,262**
of which:							
workers in national economy as sole or main employment	7,619,363	7,639,376	7,619,045	7,246,548	6,968,421	4,758,587	4,624,227
Registered unemployed	0	0	0	76,965	523,700	221,749	134,788

Sources: Federal Statistical Office, Statistická ročenka ČSFR; Czech Statistical Office, Statistická ročenka České republiky.

Structure of employment

	Czechoslovakia				Czech Republic			
	1987		1991		1991		1992	
	'000	% of total	'000	% of total	'000	% of total	'000	% of total
Agriculture, forestry & water	988	12.7	795	10.8	500	9.9	427	8.7
Industry	2,898	37.4	2,697	36.7	1,944	38.4	1,798	36.5
Construction	690	8.9	703	9.6	474	9.4	408	8.3
Transport & communications	505	6.5	526	7.2	367	7.2	366	7.4
Retail & wholesale trade & repairs	825	10.6	762	10.4	526	10.4	616	12.5
Social services	1,268	16.4	1,257	17.1	853	16.8	770	15.6
of which:								
education	461	5.9	446	6.1	286	5.6	326	6.6
health	334	4.3	347	4.7	233	4.6	268	5.4
Other non-production activities	281	3.6	412	5.6	246	4.8	176	3.6
of which:								
administration, courts & arbitration	118	1.5	144	2.0	91	1.8	123	2.5
Total incl others[a]	**7,754**	**100.0**	**7,339**	**100.0**	**5,059**	**100.0**	**4,927**	**100.0**

[a] Excluding self-employed.

Source: EIU, The Czech Republic, Country Profile, 1994-1995

CHAPTER 5

POST-LIBERALISATION POLITICAL AND ECONOMIC CONTEXT 1989-1994

> 'People, your government has been returned to you'
>
> Václav Havel, President of the former Czech and Slovak Federal Republic, in his 1990 New Year's address, quoting the words of Thomas Garrigue Masaryk, in his inaugural address as first President of Czechoslovakia, in 1918.

POLITICAL OVERVIEW

Unity in dissent

The Velvet Revolution of November 1989 saw the fall of the communist regime in the former Czechoslovakia. The chain of events leading to this outcome began on 17th November 1989 when an officially sanctioned street demonstration took place to commemorate the 50th anniversary of the execution (by the Nazis) of student Jan Opetal in November 1939. Demonstrators were attacked by riot police and one hundred and forty people were injured. Strikes and demonstrations took place on the days that followed. Two days later, in the Czech Republic, three hundred opposition activists from various non-communist organisations united to form Civic Forum, a broad anti-government coalition. The counterpart of this political grouping in Slovakia was the Public Against Violence.

On 25th November some 500,000 people crowded into Wenceslas Square to hear Alexander Dubcek, the hero of the 1968 "Prague Spring", return to the political scene. Civic Forum was officially registered as a legal organisation and, on 29th of November 1989, the Federal Assembly abolished the Communist Party's constitutional monopoly of power.

Thereafter events continued to move swiftly. On 28th December 1989, Alexander Dubcek was elected Chairman of the Federal Assembly. On the following day this body elected Václav Havel President of Czechoslovakia. At this time also, Václav Klaus, the economist and staunch critic of the former regime, became Minister of Finance.

The political coalition that over threw the communist monopoly comprised all opposition groups from the far left to the far right of the political spectrum. It formed the government of national understanding, of which the communists still retained eight out of the twenty available seats.

After the fall of communism, the political system of Czechoslovakia was restructured in such a way as to afford equal rights to both the Czech and Slovak Republics. The respective regions were represented by parallel legislative structures, comprising the Czech National Council with two hundred deputies, and the Slovak National Council with one

hundred and fifty deputies. The Federal Assembly had overall control of economic policy and constitutional matters.

The first freely contested elections since 1948 were held on 8th and 9th of June 1990, under a system of proportional representation. The Communist Party was eliminated from power. Civic Forum gained 51% of the vote in the Czech lands, with its Slovak counterpart gaining 34.9% of the seats in that region.

Political fragmentation

The period following the election was characterised by significant political fragmentation. Václav Klaus wanted Civic Forum to become a clear political party with defined political groupings. Consequently, in February 1991, the Civic Democratic Party was formed under the leadership of Václav Klaus, as a right-wing party in favour of rapid economic reform. Jiri Deinebster formed the Civic Movement, which sought to retain the broader traditions of the Civic Forum movement.

As the results of the general election of June 1992 demonstrated, the range of opposition forces to the political party of Václav Klaus proved to be relatively ineffective (see Appendix I for the election results). Václav Klaus had managed to convince the voters that the

policy of monetary stabilisation and rapid privatisation offered the best opportunity for a decisive break with the socialist past, and a return to Europe.

The End of the Federation

Over the period from 1990 to 1992 the underlying differences between the political, economic and cultural heritages of the Czech lands and Slovakia became increasingly apparent. These differences manifested themselves in terms of the diverging political and economic directions which each of the respective regions wished to pursue.

The widening gap between the regions was confirmed in the election results of 1992, when the realignment of the respective political parties in the two regions was ratified. Václav Klaus' Civic Democratic Party, which was firmly committed to economic reform, won convincingly in the Czech lands, whilst Vladimír Mecair's Movement for a Democratic Slovakia triumphed as a left-orientated coalition in Slovakia. The Czech and Slovak Federal Republic peacefully dissolved itself on 31st December 1992.

OVERVIEW OF ECONOMIC TRANSITION

Policy framework

From the outset of the economic transition process, the charismatic figure of Václav Klaus has dominated much of the direction of the economic policy in the former Czech and Slovak Federal Republic, and subsequently, in the Czech Republic.

The main economic transformation measures which have formed the basis of government policy since liberalisation are based upon the recommendations of the Balcerowicz Group. This group of international economic advisors and experts was formed to assist the Polish government in the development of economic reform strategies (Komárek, 1993, p.61).

When the Solidarity-led government came to power in September 1989, it had no previous political experience, and only a vague idea of how to manage the economy. Thus, the task of designing the reform programme to effect the transition was given to a small group of experts under Leslek Balcerowitcz. Amongst the leading foreign economic advisers to this group were theorists, such as professor Jeffrey Sachs from the United States who had just returned from a short stay as an adviser in Bolivia (Komárek, 1993, p.61).

This group of economists became pivotal figures in 'exporting' reform policies from Central America to Eastern Europe, where it was felt that significant similarities existed. The perceived similarities comprised foreign indebtedness (although not in the case of the Czech Republic), high inflation and state bureaucratic interventions supported by the corrupt management of state industries and services.

These apparent parallels between the developing countries of Central America and the fledgling democracies of Eastern Europe, together with the recent experiences of Jeffrey Sachs, led to the formulation of a set of macro economic strategies based upon the experience of these Latin American countries.

A set of prescriptive, neo-liberal monetarist strategies, recommended by these advisers and supported by the International Monetary Fund together with other major international lending institutions, was formulated with the express objective of avoiding the worst economic problems experienced by Central America, especially those of hyper-inflation and excessive levels of external national debt.

The main tenets of this economic stabilisation policy were:

- price liberalisation - supported by strong monetary and fiscal policy measures to combat inflation

- external currency convertibility - to stimulate exports with the West
- balance of payments stabilisation - to avoid incurring exceptionally high levels of external debt.
- privatisation of state-owned property - to re-establish the fundamental property rights which are necessary for effective free market transactions to be undertaken

In all of these policy areas the emphasis was on speed of implementation, thus giving rise to the 'shock therapy' approach to change (Blanchard et al. 1991, p.2).

ECONOMIC POLICY IMPLEMENTATION

In response to these measures, the Czech and Slovak Federal government immediately began to formulate economic reform policies within the framework of the macro-economic policy recommendations outlined above. The performance of the Czechoslovak economy for the period 1990 to 1992, and that of the Czech Republic for 1993 and 1994, will be considered. As the economic policies of the independent Czech Republic are continuations of those initially implemented during the Federation, the overall trends for the whole period under consideration will be reviewed.

Price liberalisation

Under communism consumer prices, producer prices and socialist-sector wages were fixed. The aim of price liberalisation was to remove such price controls, and allow prices to be set by the market.

The Czechoslovak government began the process of price liberalisation in January 1991, when price controls were removed from 85% of goods and services. As shown in Appendix II, this led directly to a price increase of 54.1% in 1991 in Czechoslovakia as a whole, and price increases of 11.4% in the Czech Republic in 1992. In 1993, inflation accelerated to 20.8% as a result of the introduction of value-added tax in January of that year. The tax rates were set at 23% and 5% respectively. The forecast summary of the economist intelligence unit predicted that inflation would be 9.5% for 1994, falling to 8% and 6% respectively in 1995 and 1996, as shown in Appendix II. These predictions, however, are based upon scenarios which envisage more radical restructuring within the economy than the Czech government has carried out to date (Autumn 1994). Overall, the evidence suggests that the Czech Republic has been relatively successful in controlling inflation, once the shock of price liberalisation had been absorbed.

Control of inflation

A major step undertaken by the Czechoslovak government to control inflation involved the setting up of a social pact with employers and unions in order to control wages in the state sector. The impact of the policy is highlighted by the increases in real wages shown in Appendix III. It can be seen that the initial years of transformation led to substantial falls in real living standards for the country. The trends indicate, however, that wages have begun to increase in real terms, and should continue to do so, albeit at a predicted decreasing rate. Thus inflation has been controlled primarily through suppressing consumer demand by means of strict income policy controls.

Currency convertibility

The Czech crown, the unit of currency, was made internally convertible on 1st January 1991, whereby enterprises were able to buy convertible currency to finance imports. However, they are still required to sell proceeds from exports to authorised banks at the current rate of exchange. Individuals are allowed to buy only a limited amount of foreign exchange, so a vestigial black market continues. Since January 1990 a unified exchange rate, adjusted weekly against a weighted average of five important currencies, has applied for all trade with western countries. In May 1993, the Czech National Bank

switched to a new basket, consisting of a 65% share for the deutsche-mark and a 35% share for the US dollar.

The crown has been devalued twice since liberalisation, in 1990 and 1991 respectively. Since that time it has retained a fairly constant exchange rate of approximately 30 crowns to the US dollar. Some debate exists as to whether this is, in fact, an artificially low rate of exchange against the dollar, designed to boost the perceived export performance of the Czech Republic.

Balance of payments

In the years preceding its dissolution, Czechoslovakia had an overall current account surplus on the balance of payments. However, the country had an overall current account deficit in 1990 on the convertible currencies account, as the initial economic transformation measures were implemented. The current account surplus was restored in 1991, largely as a result of increases in invisible earnings, especially from tourism and a healthy capital account surplus (see Appendix IV). The current account showed a healthy surplus in 1993, primarily due to the continued expansion of tourism. The capital account position has been improved by direct foreign investment, portfolio investment and credits to Czech firms from abroad (EIU, 1995).

It could be inferred that the underlying health of the balance of payments is a combination of a favourable inherited debt situation, funds from tourism, the purchase of portfolio investments, and a severe recession which has suppressed demand for imported goods. As these policies do not in themselves stimulate sound industrial and commercial growth within the country, the positive aspects of the balance of payments situation should be considered in the wider context of the overall economic position of the country.

Foreign debt

Czechoslovakia's financial conservatism under the communist regime, and its limited trade with the West before 1989 when such trade comprised only 18% of overall trade, have enabled the country to avoid the more serious debt problems of its neighbours in the 1980s. Nevertheless, hard-currency debt had risen towards the end of the decade, with a shift in its structure with long-term debt increasing from US$3,875 million in 1988 to US$4328 million in 1989 (see Appendix V).

Concerning the external debt situation, however, financially the Czech Republic is secure. Total foreign debt at the end of 1992 stood at US$9,500 million with debt service payments equivalent to 11.2% of exports in 1991, and 11.7% in 1992 (Rutland 1994, p.266). The updated data

for 1993 (see Appendix VI) indicate that this trend has continued, with a gross foreign debt of US$ 8.6 billion and a debt service ratio of 11.4%. A major benefit of this positive debt situation is that it makes the Czech Republic a less risky and more attractive investment proposition for foreign investors, although, as the analysis of foreign investment later in this chapter will indicate, this has not been forthcoming to the extent that the Czech Republic would have wished.

Foreign trade

After the communist seizure of power in 1948, the bulk of Czechoslovak trade took place with the Soviet Union and Eastern Europe, with Czechoslovakia exporting predominantly machinery and importing raw materials. The collapse of these markets after 1989 has forced the country to undertake a rapid re-orientation of trade with the West. As Appendix VII shows, Germany has now become the largest single export market. In 1992, Germany was already by far the leading destination for Czech exports with 30.6% of the total. It maintained this position in 1993. It also overtook the former USSR as the largest source of imports, accounting for 24.6% in 1992 and 26% in 1993. Additionally, in 1993, 43.6% of Czech exports went to the European Union, with 42.3% of imports coming from that region also. The structure of exports to market economies is still strongly biased towards raw materials and less

towards processed goods, the major exception being the motor car industry (EIU 1994, p.28).

Industrial output

The period since liberalisation has witnessed a dramatic and continuing fall in GDP in the former Czechoslovakia, which currently (as at Autumn 1994) still persists in the Czech Republic. This has been the result of a combination of factors. The dramatic reduction in industrial subsidies and investment government spending as a share of GDP from 64.9% in 1989 to 52.8% in 1991 and 52.5% in 1993 has impacted significantly upon economic performance (Rutland, 1994).

Additionally, the collapse of its main Eastern European markets, the freeing of imports, price liberalisation and the resulting recession permeating all of Eastern Europe has adversely affected GDP. The falling levels of GDP are shown in Appendix IIX. A further contributory factor to the fall in output was the break-up of the federation in 1992. The predictions of the Economist Intelligence Unit for the period from 1994 to 1996, as shown in Appendix II, indicate a projected modest level of growth at approximately 4% per annum.

However, total output for the first four months of 1994 was down by 0.7% compared with the previous year. By the

completion date of the research, Autumn 1994, there is no sign yet of an upturn in overall industrial output (see Appendix IIX).

These are clear causes for concern. The future development and growth of the economy must, ultimately, depend on the ability of industry and commerce to produce and sell increasing quantities of higher quality goods and services in a competitive global market.

Unemployment

The transition process in the Czech Republic has been characterised by a significantly low stable level of unemployment, despite the recession and significant falls in GDP. Appendix III shows that the Czech Republic only registered a level of 3.5% unemployment for 1993 with projected levels set to rise to only 7% in 1996. However, the divergence in unemployment levels between the Czech Republic and Slovakia, as contained in Appendix IX, helps to illustrate part of the reason for the dissolution of the federation. Slovakia with its dependence on agriculture and the arms industry bore the brunt of the contraction in employment following liberalisation.

Foreign investment

The total sum of direct foreign investment in the former

Czechoslovakia and the Czech Republic for the period 1990 to 1993 was US$1898 million. As only 7% of this investment went to Slovakia, and all of the main foreign investment projects have been in the Czech Republic, the overall evaluation of foreign investment for the duration of the period assessed reflects the policy of the Czech Republic in this area.

Appendix X shows foreign direct investment for the period 1990 to 1993 by country of origin and sector of investment. Over this period Germany has proved to be the largest single investor in the region, followed by the United States. France is third in order of volume of investment, although the French figure of US$259 million is significantly less than that of the United States.

The volume of investment by sector is indicative of the pattern of investment which has taken place in the region, i.e. there has been a small number of very significant investment projects. The highest level of investment comprises the area of consumer goods and tobacco. This is accounted for partly by the purchase of the Czech Tobacco industry outright by Philip Morris. Additionally, the influx of fast food and drinks companies, such as Coca Cola and McDonalds, has augmented this figure, together with the joint venture between Colokadovny (the state chocolate manufacturer) and Nestlé.

The VW purchase of 31% of Skoda in Bohemia has been a major contributory factor towards the level of foreign investment in the automotive industry, which placed it as the second highest area of foreign investment after consumer goods and tobacco. The exceptional figure of US$223.9 million for France in 1992 was a direct result of the now defunct joint venture between the Czechoslovak national airline (CSA) and Air France.

Overall, since liberalisation the level of direct foreign investment has been well below that originally considered necessary to develop a modern industrial structure in the Czech Republic. Although, it must be noted that no exact figure for required investment appears to have been computed.

The Czech government appears to be awaiting another major project to boost the level of foreign investment in the country. However, several of such potential projects fell through during 1993. Dow Chemicals withdrew from its US$100 million acquisition of the Solokov chemical plant and Mercedes pulled out of a planned deal with the Avia and Lisa truck manufacturers (Rutland 1994, p.265).

Additionally, the statistics to September 1994 (see Appendix XI) show that the figure of US$478 million, approximately 5% more than the US$390 million received during the same period in 1993. Whilst this represents a modest increase on the previous year, it still indicates a

fall of almost 40% compared with the peak year of 1992 (EIU, 1994).

Given the pivotal role of foreign direct investment in the future development of the country in terms of funds, expertise and technology, the slowdown in this source of funds must be seen as a threat to hopes of rapid economic growth.

PRIVATISATION AND BANKRUPTCY LEGISLATION

Privatisation

Rapid privatisation has been seen as an integral feature of the transition to a market economy. Both the speed and approach of the Czech government in relation to this area have attracted much attention. At the time of liberalisation in 1989, some 98% of all Czech industry was state owned. Thus, the mass privatisation exercise embarked upon by the government in 1992 was an undertaking of immense proportions.

The legislation relating to privatisation covers some 4,000, but of the larger state-owned enterprises, including financial institutions, insurance companies, state farms, industrial enterprises and foreign trade organisations.

The main statutes relating to privatisation comprise:

The Large Scale Restitution Act of 1990, which is designed to return to Czech citizens any property that may have been confiscated from them, when the communists seized power in 1948. This led to the return of some 100,000 properties (Posustova 1993, p.61).

The Small Privatisation Act of 1990, which provides for the lease of sale of retail establishments, workshops and other small premises to the public by means of auctions. Twenty-two thousand properties were transferred to private ownership by this means (Posustova 1993, p.42-45).

The Large Privatisation Act, stipulates the means whereby the majority of the main state-owned industries are to be transferred back to private ownership. Commencing early in 1992, each state-owned firm was required to prepare its own privatisation project, proposing their chosen privatisation form from the available options of direct sale to a foreign or domestic buyer, public auction, or sale through the 'voucher method' of privatisation. Other citizens could also submit rival plans or projects. The Ministry of Privatisation selected the winning project. When enterprises had been privatised, the state shareholding in the independent firms was transferred to the government controlled National Property Fund, whose responsibility was to dispose of them over the ensuing years. It should be noted, however, that, although privatised, these enterprises were still essentially state-owned and

controlled via the National Property Fund (Frydman et al. 1993, p.77).

The mass privatisation process, using the voucher scheme, was designed to take place in three waves. The first wave of privatisation began in May 1992 involving approximately 25% of Czech industry. The businesses included in this wave were those most prepared for privatisation and having little strategic importance. By the end of the first phase of privatisation in January 1993, 1320 firms had been privatised. The second wave of privatisation which started in October 1993 saw 2,100 firms privatised. This wave dealt with more complex heavy industrial companies such as telecommunications, utilities and machine manufacture (Matesova 1994, p.8).

The overall profile of privatisation projects, together with the revised structure of ownership of Czech enterprises, is shown in Appendix XII, together with an asset valuation of the firms. As one can observe from these tables, however, not all enterprises were included in the mass privatisation programmes. It should be noted that the outcome of the privatisation process to date has been to retain some 27% of company ownership in the hands of the government controlled National Property Fund, and to concentrate ownership of the majority of the shares in the hands of a few institutional investors, i.e. banks and investment companies. Thus, one could argue that it was

not true privatisation in the sense of creating a shareholding population. The subsequent chapter on privatisation will discuss the nature of the process and its effect on the transition process. Chapter 9, will discuss the nature of privatisation and its outcomes.

Bankruptcy Legislation

Any market-related economic system requires the existence of exit mechanisms in response to the operation of market forces. The Bankruptcy and Composition Act was first passed though the parliament of the Czech and Slovak Federal Republic in July 1991. Implementation of the Act was deferred twice and entered the statute books in April 1993.

The main provisions of the Act apply to both entrepreneurs and business enterprises. The objective of the act is to ascertain the level of debtors' assets and to attempt to satisfy the creditors. A bankruptcy order can be proposed by the creditor, debtor or the liquidator by filing a petition for bankruptcy with the appropriate bankruptcy court.

The Act also contains special provisions which, it is argued, have substantially reduced its effectiveness. The Act contains an initial three month protection period, which can be extended a further three months, to give the

debtors sufficient time to settle terms with creditors.

The government has also introduced special criteria for certain groups of businesses. Insolvent state enterprises included on a government approved list are exempt from bankruptcy proceedings. Additionally, businesses, whose main activity is agricultural production, cannot be declared bankrupt between 1st April and 30th September in any year to protect them from the consequences of negative cash flow (Czechinvest 1994, 09/13-20).

There have been some major criticisms of the effectiveness of the bankruptcy legislation. There is no legal infrastructure in place to manage the bankruptcy process. This is a major disincentive for creditors to become involved in lengthy bankruptcy procedures.

The text of the law is considered to be ambiguous, leaving a large amount of discretion to the courts. This could lead to inconsistent applications of the law and to lengthy legal proceedings.

The government has also exempted from bankruptcy those firms which participate in its scheme for matching payables with receivables. The objective of the scheme is to is to reduce the level of intercompany debt, and thus the level of potential bankruptcies.

The Ministry of Trade and Industry has set up a work group whose task is to conduct a computerised matching of payables and receivables between enterprises. The work has been contracted out to several private companies. Firms participating in the scheme submitted payables of 75 billion crowns (30 crowns = 1 dollar) and receivables of 112.4 billion crowns. According to statistics produced in 1994, the total amount of funds matched was 10.2 billion crowns, only 9.1% of the submitted receivables.

The participating firms have complained about the cost of commission they are required to pay for the service and the unsatisfactory outcome of the process (Brom & Orenstein 1994, p.17).

FINANCIAL INFRASTRUCTURE

Banking structure

A key component of the functioning of a free market economy is an effective system of financial intermediation, whereby funds can be mobilised from savers to investors, and credit and loan facilities can be generated.

Prior to 1989, the Czech and Slovak banking sector was a monobank system with a single bank responsible for all aspects of the banking function, as directed by government. The system has now changed to one in which commercially

independent banks are the norm. The number of banks operating in the Czech Republic increased from nine in 1990 to thirty-nine by the end of March 1993, eight of which were entirely foreign-owned. The restructuring is less radical than it appears, however, as the former state owned bank has been divided into five separate institutions which own 55% of all capital, 87% of deposits and issue 87% of all loans.

Additionally, the banks are major shareholders in the majority of the newly privatised enterprises. The position of banks in the new financial sector is even more complex as they find themselves also in the position of being major lenders to the heavily indebted former state-owned enterprises.

Capital markets

The first publicly accessible capital markets in the Czech Republic began with the opening of the Prague stock exchange on 6th April 1994. It is modelled on the Lyon Stock Exchange and was implemented by the Societé de Bourses Françaises under contract to the Czech government. It currently trades three times a week. This stock exchange differs from the London stock exchange in that a highly controlled price setting mechanism is used to match buying and selling orders at an optimal level. Each morning of trading, brokers place their buying and selling

orders in a computerised 'quotation box' to which an algorithm is applied. This formula then determines the share price that will result in the largest amount of trading. The market is then re-opened when the price is announced. If the market fails to clear, brokers who did not make deals at the fixed price can then do so. In terms of structure, the Prague stock exchange has all the membership requirements of a typical stock exchange.

There is, however, a competing stock market in operation - the RMS. This institution was created by the same company which managed the voucher privatisation and was intended to give ordinary shareholders a cheap alternative to the Prague stock exchange. Thus, although the same method of share pricing applies in both institutions, the RMS is open to anyone and any of their offices located throughout the country can be utilised for a small commission. Additionally, it trades once every three weeks only. On the other hand the volume of trade in the Czech Republic is not sufficient to warrant two trading systems and the debate continues as to which is most suited to the needs of the financial system.

The capital markets and the banking system are virtually unregulated in relation to the conduct of members and the nature of their business dealings. The lack of sufficient legal and regulatory controls over financial activity has left the situation open to scandals and fraud which have

already beset the financial system (Eaves 1994, p.1).

CONCLUSION

Any attempt to evaluate the overall effectiveness of the transition measures outlined above, and indeed, the nature of the whole imperative towards a market economy, can only be undertaken within the framework of the past events in the region.

Additionally, the political economic and institutional implications of the strategies outlined above must be analysed in some depth before conclusions can be drawn concerning their contribution to the reform process. Finally, the impact of these substantive paradigm changes on the nature of both newly established and former state-owned enterprises must be considered.

The following sections will begin by considering the history of the region in terms of its political, economic and social conditions as they impact upon the transition process.

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RESULTS OF THE JUNE 1992 ELECTIONS TO THE FEDERAL ASSEMBLY AND THE CZECH REPUBLIC

	% of vote		Seats	
	Czech	Slovak	House of Nations	House of the People
Civic Democratic Party-Christian Democratic Party	33.7		37	48
Left Bloc	14.4		15	19
Czech Social Democrats	7.3		6	10
Republicans	6.4		6	8
Christian Democratic Union-People's Party	6.0		6	7
Liberal Social Union	5.9		5	7
Movement for a Democratic Slovakia		33.7	33	24
Party of the Democratic Left		14.2	13	10
Slovak National Party		9.4	9	6
Christian Democratic Movement		8.9	8	6
Hungarian Christian Democrats		7.4	7	5
Slovak Social Democrats		5.6	5	-
Others	26.3	20.8	-	-
Total	**100.0**	**100.0**	**150**	**150**

Source: Czechoslovak press.

Results of elections to the Czech parliament, Jun 1992

	Votes	MPs	
	%	No	%
Civic Democratic Party-Christian Democratic Party	29.7	76	38.0
Left Bloc	14.1	35	17.5
Social Democrats	6.5	16	8.0
Liberal Social Union	6.5	16	8.0
Christian Democratic Union-People's Party	6.3	15	7.5
Republican Party	6.0	14	7.0
Civic Democratic Alliance	5.9	14	7.0
Movement for Self-managing Democracy	5.9	14	7.0
Others	19.1	-	-

Source: Czechoslovak press.

Source: EIU, The Czech Republic, Country Profile, 1993-1994

FORECAST SUMMARY OF SELECTED MACRO ECONOMIC INDICATORS FOR THE CZECH REPUBLIC, 1993-1996

Forecast summary

(% change on previous year unless otherwise indicated)

	1993[a]	1994[b]	1995[b]	1996[b]
GDP	–0.3	3.0	4.0	4.4
Industrial output	–5.3	0.0	2.0	3.0
Agricultural output	–0.8	2.5	3.0	3.0
Services	4.5	8.5	9.1	9.4
Consumer prices	20.8	9.5	8.0	6.0
Unemployment rate (%; year-end)	3.5	4.0	6.0	7.0
Trade balance[c] ($ m)	–168	–200	–1,130	–1,200
Current account[c] ($ m)	360	–330	–326	–600

[a] Actual; Czechoslovakia in 1992. [b] EIU forecasts. [c] Totals including trade and payments with Slovakia.

Source: EIU, The Czech Republic, Country Profile, 1994-1995

PRICES AND WAGES IN CZECHOSLOVAKIA AND THE CZECH REPUBLIC FOR THE PERIOD 1988-1993

Prices and wages

(% average change on previous year)

	Czechoslovakia				Czech Republic		
	1988	1989	1990	1991	1991	1992	1993
Consumer prices	0.2	1.4	10.0	57.9	56.6	11.1	20.8
Foodstuffs	–0.3	0.1	11.1	45.3	44.4	9.1	16.6
Non-food items	0.3	2.6	10.5	72.0	69.7	9.0	19.4
Public catering	0.6	1.0	8.5	57.0	58.8	8.4	27.5
Services	0.9	0.8	7.4	39.5	39.1	25.6	28.7
Producer prices							
Industry	0.0	–0.7	4.5	69.9	70.4	9.9	13.1
Construction	0.0	–2.2	6.4	49.1	46.8	11.6	25.9
Agriculture	0.0	27.0	4.1	–0.3	–2.5	7.7	8.4
Cost of living (employees)	0.4	1.5	9.8	54.1	52.9	11.4	20.8
Real wages of socialist sector workers	1.9	0.8	–5.7	–24.3	–23.6	9.7[a]	3.5[a]

[a] In units of 25 or more employees.

Sources: Federal Statistical Office, Statisticka recenka CSFR; IMF, International Financial Statistics; Czech Statistical Office, Statisticka rocenka Ceske republiky.

Source: EIU, The Czech Republic, Country Report, 4th Quarter 1994

BALANCE OF PAYMENTS IN CONVERTIBLE CURRENCIES IN CZECHOSLOVAKIA, 1987-1992

	1987	1988	1989	1990	1991	1992
Merchandise exports fob	4,543	5,012	5,445	5,873	8,326	11,463
Merchandise imports fob	-4,667	-5,095	-5,029	-6,524	-8,807	-13,297
Trade balance	**-124**	**-83**	**417**	**-650**	**-482**	**-1,834**
Exports of services	1,453	1,472	1,452	1,669	2,603	4,018
Imports of services	-1,167	-1,172	-1,235	-1,627	-1,771	-2,359
Inflows of IPD[a]	311	336	391	427	530	792
Outflows of IPD[a]	-484	-562	-553	-729	-593	-790
Net private transfers	-5	-9	-5	-5	59	51
Net official transfers	-42	-42	-30	-33	-18	90
Balance on current account	**-59**	**-59**	**436**	**-949**	**328**	**-31**
Direct investment	0	0	257	173	583	1,073
Other capital	389	367	67	60	-704	734
Balance on capital account	**389**	**367**	**324**	**233**	**-121**	**339**
Errors & omissions	-71	-102	-196	-410	583	-687
Overall balance	**260**	**207**	**563**	**-1,127**	**789**	**-422**

[a] Interest, profit and dividends.

Source: EIU, The Czech Republic, Country Profile, 1994-1995

GROSS FOREIGN DEBT IN CONVERTIBLE CURRENCIES

($ m)

	Czechoslovakia					Czech Republic Jan 1,
	1988	1989	1990	1991	1992	1993
Long-term	3,875	4,328	4,674	6,792	7,257	6,189
Short-term	3,406	3,587	3,412	2,507	2,226	1,679
Total	**7,281**	**7,915**	**8,085**	**9,299**	**9,484**	**7,869**[a]

[a] Differs from the figure of $6.9bn in the text as it includes debt in non-convertible currency.

Sources: Federal Statistical Office, Statistická rocenka CSFR; Czech Statistical Office, Bulletin CSU.

Source: EIU, The Czech Republic, Country Profile, 1994-1995

SUMMARY OF SELECTED FINANCIAL AND ECONOMIC DATA FOR THE CZECH REPUBLIC: JANUARY 1993 TO FEBRUARY 1994

GDP (current prices)	US$Bil	31.7	1993
GDP, % change from 1 year ago	%	-0.3 (x)	1993
Industrial output, % change against 1 year ago	%	-5.3 (x)	Jan-Dec 1993
Construction output, % change against 1 year ago	%	-7.5 (x)	Jan-Dec 1993
Retail trade, % change against 1 year ago	%	1.2 (x)	January 1994
State budget	US$Mil	56.5	Jan-Feb 1994
Unemployment	%	3.7	February 1994
Number of unemployed	'000	196.6	February 1994
Average monthly wage (gross)	$	200	1st-4th quarter 1993
Inflation rate - 1992	%	12	Jan - Dec 1992
Inflation rate - 1993	%	21(xxx)	Jan - Dec 1993
Inflation rate - 1994 (estimate)	%	10	Jan - Dec 1994
Monthly inflation	%	0.2	February 1994
Exports	US$Mil	12,774	Jan-Dec 1993
Imports	US$Mil	12,556	Jan-Dec 1993
Foreign trade - export structure (xx)			
EC	%	54.6	January 1994
EFTA	%	10.9	January 1994
Transitional economies	%	16.5	January 1994
Developing countries	%	10.7	January 1994
Trade balance	US$Mil	218	Jan-Dec 1993
Current account balance	US$Mil	580.0	Jan-Dec 1993
Gross foreign reserves	US$Bil	6.7	February 1994
Gross foreign debt	US$Bil	8.6	January 1994
Debt service (% of goods/service exports)	%	11.4	Jan-Dec 1993
Consumer Prices, % change from 1year ago	%	9.7	February 1994
Wholesale Prices, % change from 1 year ago	%	5.3	February 1994

Source: Czechinvest Information Series, No.6 NO.MAC/11/93/6, Prague, April 1994

ECONOMIC STRUCTURE: CZECHOSLOVAKIA, 1988-1992

Latest available figures

Economic indicators	1988	1989	1990	1991	1992
GDP at current prices Kcs bn	606	618	670	828	1,010
Real GDP growth %	2.7	1.4	-1.6	-14.7	-7.0
Consumer price inflation %	0.1	1.4	10.8	57.8	10.0
Population m (year-end)	15.6	15.6	15.6	15.6	15.6
Hard-currency exports[b] $ m fob	5,012	5,445	5,873	8,326	11,463
Hard-currency imports[b] $ m fob	5,095	5,029	6,524	8,807	13,297
Hard-currency:					
current account $ m	-59	436	-949	328	-31
assets, BIS banks (Dec) $ m	1,671	2,191	1,353	2,801	4,353
liabilities, BIS banks (Dec) $ m	4,446	5,149	6,323	5,458	5,602
gross debt $ bn	7.4	7.9	8.4	9.8	9.5
Commercial rate (av) Kcs:$	14.36	15.05	17.95	29.48	28.26

Origins of net material product 1990	% of total
Agriculture, forestry & water	8.9
Industry	58.1
Construction	10.8
Productive services	22.2
Total	**100.0**

Net material product by use 1990	% of total
Personal consumption	57.0
Social consumption	23.9
Accumulation	19.1
Total	**100.0**

Principal exports to the West 1992	$ m
Manufactured goods	3,833
Machinery	1,329
Raw materials	935
Chemicals	783
Food products	490
Total incl others	**7,425**

Principal imports from the West 1992	$ m
Machinery	4,073
Other manufactured goods	1,804
Chemicals	1,027
Raw materials	408
Food products	400
Total incl others	**7,845**

Main destinations of exports 1992	% of total
EU	49.4
Germany	30.6
Other Western countries	14.3
Former Soviet Union	10.9
Former Comecon (excl Soviet Union)	13.7
LDCs	10.1

Main origins of imports 1992	% of total
EU	42.1
Germany	24.6
Other Western countries	20.4
Former Soviet Union	24.6
Former Comecon (excl Soviet Union)	6.7
LDCs	5.5

Source: EIU, The Czech Republic, Country Report, 1st Quarter, 1995

GDP FOR CZECHOSLOVAKIA AND THE CZECH REPUBLIC, 1991-1994

Gross domestic product
(Kcs/Kc bn; constant 1984 prices)

1991	
1 Qtr	122.6
2 Qtr	106.1
3 Qtr	103.0
4 Qtr	100.4
1992	
1 Qtr	94.6
2 Qtr	100.8
3 Qtr	105.6
4 Qtr	102.3
1993	
1 Qtr	93.2
2 Qtr	104.6
3 Qtr	105.6
4 Qtr	98.6
1994	
1 Qtr	96.5

Source: Czech Statistical Office.

Source: EIU, The Czech Republic, Country Report, 3rd Quarter, 1994

EMPLOYMENT AND UNEMPLOYMENT IN THE CZECH AND SLOVAK FEDERAL REPUBLIC, THE CZECH REPUBLIC AND SLOVAKIA, 1985-1992

Table 2.1 Production, Employment and Unemployment, 1985-92 (continued)

	1985-9	1989	1990				1990	1991				1991	1992[1]	
			Q1	Q2	Q3	Q4		Q1	Q2	Q3	Q4		Q1	Q2
Employment (% change)[2,3]														
CSFR	0.7	0.3	-0.7	-1.3	-1.7	-2.5	-2.5	-8.4	-9.7	-11.1	-12.5	-12.5	-13.4	-12.2
CR	0.6	0.6	-0.8	-1.3	-1.6	-2.5	-2.5	-8.4	-10.0	-11.2	-12.9	-12.9	-15.0	-13.8
SR	0.9	-0.2	-0.7	-1.3	-1.9	-2.7	-2.7	-8.2	-9.1	-10.7	-11.7	-11.7	-12.3	-11.0
Unemployment rate (%)[4]														
CSFR	-	-	-	-	-	0.8	0.8	2.3	3.8	5.6	6.6	6.6	6.5	5.5
CR	-	-	-	-	-	0.1	0.1	1.7	2.6	3.8	4.1	4.1	3.7	2.7
SR	-	-	-	-	-	1.0	1.0	3.7	6.3	9.6	11.8	11.8	12.3	11.3

Source: Svenjar, J. (1993) A Solid Foundation in Portes, R. Economic Transformation in Central Europe: A Progress Report, London, Central European Press

FOREIGN DIRECT INVESTMENT IN THE CZECH REPUBLIC, 1990-1993

Origin of Investment

Country	1992		1993		1990 - 1993	
	mil. USD	[%]	mil. USD	[%]	mil. USD	[%]
USA	289.2	28.8	255.0	44.9	572.0	27.9
Germany	158.2	15.8	82.0	14.4	641.0	31.2
Austria	66.2	6.6	55.0	9.7	126.0	6.1
France	223.9	22.3	34.0	6.0	259.0	12.6
Belgium	87.9	8.8	32.0	5.6	145.0	7.1
Netherlands	12.9	1.3	30.0	5.3	41.3	2.0
Switzerland	80.0	8.0	13.6	2.4	90.0	4.4
Italy	66.2	6.6	12.0	2.1	76.0	3.7
Others	19.0	1.9	54.4	9.6	102.7	5.0
Total	1 003.5	100.0	568.0	100.0	2 053.0	100.0

Sector of Investment

Sector	1992		1993		1990 - 1993	
	mil. USD	[%]	mil. USD	[%]	mil. USD	[%]
Consumer goods + Tobacco	275.1	27.4	244.0	43.0	533.0	26.0
Construction Industry	210.6	21.0	65.0	11.4	262.8	12.8
Banks and Insurance	101.1	10.1	55.0	9.7	207.4	10.1
Food Industry	176.5	17.6	35.0	6.2	201.2	9.8
Engineering	40.2	4.0	57.0	10.0	94.4	4.6
Trade	49.2	4.9	40.0	7.0	101.6	4.9
Electrotechnical Industry	8.4	0.8	22.4	3.9	29.9	1.5
Automotive Industry	16.1	1.6	10.0	1.8	416.8	20.3
Chemical Industry	69.2	6.9	19.3	3.4	123.2	6.0
Others	57.1	5.7	20.3	3.6	82.7	4.0
Total	1 003.5	100.0	568.0	100.0	2 053.0	100.0

Source: Czechinvest Information Series, No.2, NO FDI/08/93-2, Prague, April 1994

FOREIGN DIRECT INVESTMENT BY SECTOR

	Jan-Sep 1994		Cumulative[a] to end-Sep 1994	
	$ m	% of total	$ m	% of total
Consumer goods & tobacco	32.3	6.8	605.0	22.4
Transport equipment	21.4	4.5	469.0	17.4
Construction	96.0	20.1	381.8	14.1
Banking & insurance	116.0	24.3	344.0	12.7
Trade & services	34.4	7.2	145.1	5.4
Food	64.6	13.5	282.8	10.5
Others	113.4	23.6	471.0	17.5
Total	**478.1**	**100.0**	**2,698.7**	**100.0**

[a] Total since the fall of the communist regime.

Source: EIU, The Czech Republic, Country Report, 4th Quarter, 1994

PRIVATISATION PROJECTS APPROVED BY THE MINISTRY OF PRIVATISATION, DECEMBER 1993

	Approved	Implemented
Direct sale	1,680	1,143
Public competition	502	285
Public auction	514	278
Compensation to former owners	129	73
Restored to former owners	613	314
Free transfer	2,318	1,157
From joint stock company to joint stock company	345	278
From state enterprise to joint stock company	1,432	1,145

Source: Ministry of Privatisation.

Ownership structure of Czech enterprises, Jan 1994

Organisational form	Number of firms
State enterprises	2,462
Commercial companies	60,239
Cooperatives	4,515
Individual entrepreneurs	715,353
Individual farmers	70,390
Others	68,137
Total	**853,139**

Source: Czech Statistical Office.

Source: EIU, The Czech Republic, Country Report, 4th Quarter, 1994

PROPERTY APPROVED FOR PRIVATISATION AND PASSED ON TO NATIONAL PROPERTY FUND, DECEMBER 1993

Approved Method of Privatisation	Number of Business Units	Total Value of Property (in US$million)
Public auction	514	193.7
Public tender	502	639.6
Direct sale	1,680	1,542.8
Commercialisation into joint stock company	1,777	25,142.1
Unpaid transfer to municipalities, pension funds, savings banks	2,318	1,000.4
Restitutions	613	215.9
Restitutions with additional purchase	129	317.5
Total	7,533	29,052.1

Source: Czechinvest Information Series, No.3, NO PRI/07/09-3, March 1994

THE PAST

> The struggle of man against power is the struggle of memory against forgetting
>
> Milan Kundera, 1980

In order to understand the present, and attempt to predict the future, it is necessary to understand the past. Clearly, the market-based model which is likely to evolve within the Czech Republic will be influenced, not least, by the legacy of political, economic and social traditions which have developed in the region over hundreds of years.

Equally, the nature of the organisational responses to the changes precipitated by the fall of communism are greatly dependent upon the inherited traditions, cultures, values and behaviour of the population.

The objective of this section of the thesis, therefore, is to elicit an understanding of those aspects of the historical development of the region which will directly influence the transition process from a command to a market-based economy.

Chapter 6 discusses the nationalist question in the context of the historical development of the region. The issue of nationalism has pervaded the region for centuries and culminated in the peaceful dissolution of the Czech and Slovak Federal Republic into two independent sovereign states.

The legacy of forty years of communist rule which ended in 1989 will undoubtedly influence the future development of the country. To a lesser extent the development if the country from its inception up to the communist seizure of power in 1948 will also impact upon the progress of the transformation process in the region. Consequently, the objective of Chapter 8, which provides an analytical overview of Czechoslovakia for 1948 to 1989 will construct a framework of the political, social and economic trends in the region over this period. The structure will serve as a preface to analysing and predicting the form of market-based economy that is likely to develop in the Czech Republic.

At a more focused level, Chapter 9 on everyday life in the communist regime will seek to provide some illuminating insights into the culture and psyche of the nation, by considering the nature of daily existence under the communist regime, from the perspective of ordinary citizens. The effect of those experiences will be of major significance, when predicting their response of this generation to the structural transformation of enterprises within the regime.

CHAPTER 6

THE NATIONALIST QUESTION

> The historical sense involves a perception, not only of the pastness of the past, but of its presence.
>
> T.S. Elliot

The objective of this chapter is to focus specifically upon the nationalist dimension of the relationship between Czechs and Slovaks. The nationalist question figured prominently in the affairs of both regions throughout their joint history and culminated in the establishment of two separate regimes in January 1993.

This has had major implications from an organisational as well as a political and economic perspective. The centralist policies of the communist regime always ensured that enterprises functioned as if what later became the Czech and Slovak republics were in fact a single nation.

Thus, in both republics, the recent dissolution of the federation has created problems additional to those already posed by the whole economic transition and privatisation process.

As well as re-establishing themselves in a market economy with the extensive reconstruction which accompanies it, organisations in both republics must redefine their

business and economic relationship with each other in the context of changing sets of political economic and fiscal frameworks.

An understanding of the complexity of the nationalist issue is essential if one is to appreciate fully the complexity of the organisational problems faced by the Czechs and Slovaks as they follow their separate routes to a new political and economic order.

'The Slovak question has beleaguered Czechoslovak politics ever since 1918, despite periodic assertions that it had finally been resolved' (Leff 1988, p.274).

Prior to the Velvet Revolution of 1989, the comments of the above author would have elicited little understanding from people outside of Czechoslovakia. Relatively little was known of the domestic political affairs of the region. Indeed, some disgruntled Slovaks have commented that people outside the republic had little knowledge of the existence of Slovakia as a separate national entity before the Velvet Revolution of 1989.

Nevertheless, events since liberalisation, which culminated in the establishment of two independent states of the Czech Republic and Slovakia respectively, have validated Leff's evaluation of the political problems of the region. What then is the 'Slovak question' which culminated in the final

split between Czechs and Slovaks? Bosak (1991, p.64) accurately identified the core of dissent between the two nationalities as follows:

> In the history of Czechoslovak statehood a constant and fundamental problem has been the definition of the relationship between the two nations, Slovaks and Czechs.

It was a relationship characterised by historical diversity, national aspirations and disappointments, external aggression and internal revolution. In the final analysis both parties failed to forge a lasting union and Czechoslovakia ceased to exist as a national entity.

DIVERSE HISTORICAL LEGACY

To appreciate fully the complexity of the relationship between the two states, one must first appreciate the diverse nature of their respective historical legacies which was to have such a profound and lasting impact upon the shape of future events in the region.

As the following comparative analysis will demonstrate, the Czechs and Slovaks were at opposite ends of the political, economic and social spectrum. The face of Slovakia was very firmly turned towards the traditionalism of the East, whilst the Czech lands were culturally assimilated into the progressiveness of the West (Wolchik 1991, p.7). An

appropriate starting point for such a comparison is the year 1867; the date of the establishment of the dual monarchy within the Hapsburg empire. The division of political rule between Vienna and Budapest was parallelled by the establishment of a divided sovereignty over the Czech lands and Slovakia. The Czechs were to be ruled by the Austrians from Vienna, whilst Slovakia was placed firmly under the control of Budapest.

Although the rule of the Hapsburg monarchy ended in 1918, the legacy of the different influences of its dual political masters has continued to exert a powerful influence over the relationship between the two regions.

When the Hungarians gained sovereignty over Slovakia, they pursued a policy of Magyarisation. Their objective was to suppress the unique national characteristics of Slovakia and to assimilate the region totally into Hungary by eradicating any vestiges of Slovak identity. They sought to realise this aim by the imposition of Magyar values, standards, customs and traditions on all aspects of Slovak life (Seaton Watson 1965, p.267).

The use of the Slovak language was suppressed and Magyar was decreed to be the official language for use in schools, churches and the conduct of public life generally. Slovak political activity, including suffrage, was strictly controlled to preclude the establishment of institutions

and political groupings which might nurture nationalist awareness and development.

In her essay on the nationalist question Bosak (1991, p.67) observes that, for Slovaks, advancement was attained only at the price of abandoning their nationalist principles and submitting to Magyarisation. Those Slovaks who wished to improve their educational opportunities were required to study in Budapest. Much of this education was designed to extol the virtues of Magyar values, the objective of which was to disseminate the Magyar culture throughout Slovakia. This policy was especially influential in the training seminaries for priests, as the influence of the clergy in the many rural villages was all-pervading. This strategy proved to be a very effective way of ensuring the diffusion of Hungarian customs, beliefs and traditions. There can be little doubt that this policy significantly retarded political and nationalist development within Slovakia. Indeed, such was the power of the policy of Magyarisation in suppressing nationalism that, as late as the 1920s, many Slovaks defined themselves primarily in terms of their religion as opposed to their nationality.

This suppression of political freedom contrasts markedly with that of the Czechs over the same period. The Ausgleich, i.e. the period of Austrian domination over the Czechs, was much more politically liberal than that experienced by their Slovak neighbours under the tutelage

of Budapest. Under Austrian rule, the Czechs were allowed to develop and prosper, politically, economically and culturally. During the latter part of the 19th century, the Hapsburgs allowed the formation of nationalist groups within Bohemia. The Czechs were even permitted to participate in limited forms of self-government and were represented in the diets of Bohemia and Vienna. Universal male suffrage was adopted in 1907 (Wolchik 1991, p.9).

Within this liberal regime Czech culture flowered; education was expanded and Czech language teaching permitted in schools. Thus, the later 19th century was characterised by a revitalisation of Czech pride in their national identity. This manifested itself in the development of intellectual and politically aware leaders, notably Thomas Masaryk, the Czech nationalist intellectual who was to be a dominant figure in the formation of the First Republic. Over this period there also emerged a clearly defined national and cultural heritage, together with a political, cultural and institutional framework, within which nationalism was fostered. By 1918, the Czechs were ready for independent statehood, while the Slovaks were still politically and nationally fragmented (Korbel 1977, p.38-40).

The divergence in political and social development between the two regions was reflected in differences in their respective rates of economic progress towards a modern

industrialised society. The regions differed significantly in terms of the main parameters by which economic growth are evaluated, i.e. their degree of industrial development, level of entrepreneurial activity, and extent of financial intermediation. Bosak (1991, p.67) describes the socio-economic structure of Slovakia as having:

> An agrarian base with a solid class of peasants and rural labourers and with no large industrial proletariat or bourgeoisie in the urban area.

Essentially, the Slovak economy was dominated by subsistence agriculture which was centred around village markets. The relatively small amount of industry in the region was heavily state subsidised and relatively inefficient. Slovakia was essentially a traditional, agrarian, peasant economy (Leff 1988, p.13-15).

By 1918, however, the Czech Republic was a highly developed industrial region. From the latter part of the 19th century, the region of Silesia had been the industrial workshop for much of the Hapsburg empire. One concentrated area of industrial activity in the region was in the production of railway carriages. Even today some employees in this industry will proudly boast of their 150 year history dating back to the Hapsburg monarchy. From the late 19th century onwards, the level of industrial activity in the region far exceeded that of agriculture as the main source of wealth generation.

As regards differences in the level of entrepreneurial activity and extent of financial intermediation between the two regions, the Slovaks are portrayed as lacking 'economically enterprising individuals'. This is hardly surprising since the Magyar policy of suppression gave the Slovaks little opportunity to develop their business skills. Business activity in the region had historically been dominated by Magyars, Jews and Germans. In the Czech lands, however, the indigenous population was very much a part of the business community. The region also possessed an effective banking system where financial capitalism flourished (Leff 1988, p.14).

There were significant differences between the Czech lands and Slovakia in terms of the influence of religion on the political, economic and social development activities of the respective societies. This major issue only served to widen further the nationalist gulf between them. The role of religion in Slovakia is well summed up by Bosak (1991, p.70) who notes that the Slovaks were:

> withdrawn, deeply religious people still very much imbued with the values of a feudal agrarian order. The majority belonged to the Roman Catholic faith and looked to their parish priests for guidance on all significant issues, personal, social and political.

Thus, the village priest was often their only spiritual leader and the most educated person in the community.

There is a historic link between clerics and the development of nationalism in Slovakia which extends to significant church involvement in politics. This is illustrated by the fact that the leader of the Slovaks during their only period of independence was Father Josef Tisot - a fascist cleric (Rothschild 1974, p.117-112). The role of the Catholic church in the secular activities of Slovakia served to reinforce the traditionalist values of conservatism as opposed to promoting change and development. The power of the church, doubtless, influenced the perception of change amongst the population, making them suspicious of the progressive attitude of the Czechs and unwilling to adapt to change and new ideas.

This integrative role of the church and politics in Slovakia contrasts sharply with that of the relationship between the church and the state in the Czech lands. Czech culture was altogether more secularised. The Roman Catholic Church played no significant part in the political affairs of the region and the concepts of nationalism and national identity were not linked to religion. Indeed, the Czechs possessed a strongly sceptical anti-clericism deeply rooted in their nationalist history. The Hussite tradition of the 15th century, revered for its attempts to reform church thinking on the subject of religion and hailed as

the Czech Renaissance, continued to influence Czech attitudes to the subject of church and state.

Even today the memory of the Hussite tradition remains in the Czech psyche. Whilst touring the old town district of Prague, a professional colleague indicated to the author the spot where Hussite supporters were martyred. Additionally, when the Summer Palace in the grounds of Prague Castle was opened to the public in January 1992, after being closed by the communists for forty years, one of the newly painted murals in the palace commemorated the Hussite movement.

During the period of the Ausgleich or dual monarchy (1867-1918) many Czechs sceptically regarded the Roman Catholic church as a weapon of the Hapsburg empire. Consequently, they adopted a more secular nationalist approach to their thinking.

The perceptual gulf between the Czechs and Slovaks concerning religion is well illustrated by Bosak who notes an interesting contrast between the social and economic aspirations of the Czechs and Slovaks. It was often the ambition of Slovak peasants for their sons to become priests in order to obtain an education and a secure position in life. Czechs however encouraged their sons to go into business and commerce in order to obtain wealth and material advancement (Bosak 1991, p.67). Thus by 1918, the

Czechs and Slovaks appeared to be at different stages in their progress along those political, social and economic dimensions which required integration for a nation to be forged out of these two disparate regions. As later events were to show, such fusion never occurred.

A MARRIAGE OF CONVENIENCE

The birth of Czechoslovakia is well summed up by Leff (1988, p.274) as follows:

> The peculiar character of the construction of a state, conjoining two disparate societies with no common political past, through the action of great international political power. It was a sudden and disorientating birth, disrupting traditional administrative and economic structures in both regions.

The international power to which Leff refers is, of course, the Congress Of Versailles which met at the end of the First World War.

The reality of the creation of Czechoslovakia was 'an arranged marriage', primarily designed to meet the needs of the international community, i.e. the establishment of a stable region in Central Europe to replace the vacuum created by the dismemberment of the Austro-Hungarian empire at the end of the First World War. However, the role of Thomas Masaryk, hailed as the founder of the First

Republic, was also significant in heightening national consciousness in the region. Together with Czech nationalist groups he also played a major role in the creation of the First Republic.

From the Czech and Slovak perspectives, there were arguments for and against the creation of the new state. The creation of Czechoslovakia had both dissenters and supporters in the Czech and Slovak camps. In global terms, the regions were too weak to stand alone in the redrawn map of Europe. Together, it was hoped that they represented a viable state to succeed the Hapsburg empire (De Candole 1993, p.8).

On the issue of nationalism, the Czechs favoured an increase in the Slavic presence to counterbalance the German influence in the Northern Bohemia. From a Slovak perspective, supporters of the Republic argued that it was in their interests to join with the Czechs, thus eliminating the possibility of continued Magyar influence in Slovakia.

Those Czechs who opposed the union with Slovakia believed that it presented an unnecessary complication to their nation building objectives. Moreover, there were a substantial number of Slovaks who regarded the secular, progressive Czechs with suspicion. Their reluctance to

accept the change was no doubt greatly influenced by their deep rooted, religious conservatism. They believed that their national interests were best served by continued passive resistance to the Magyar regime which had dominated them for so long (Leff 1988, p.13-15).

Most significantly for the future of the First Republic and the subsequent relationship between the two regions, the union failed to meet the political expectations of the Slovaks who sought equal democratic representation for Slovaks and Czechs in the government of the new republic. The Czechs, however, favoured population size as the basis for political representation which would give them a majority of two to one in terms of the distribution of political power. Despite the fact that, initially, the new state represented a democratic union of shared equality between the two regions, the Czech alternative prevailed. In the Prague provincial national assembly, the ruling political body, the Slovaks had only thirteen representatives out of a total of forty and those representatives were drawn from Slovak groups who supported the union (Korbel 1977, p.160).

This issue of asymmetry, i.e. unequal distribution of power in favour of the Czechs, proved to be a bone of contention for the entire duration of the union until its dissolution in January 1993. At every political opportunity, the Slovaks sought to redress the balance of power by allying

themselves with external enemies of the Czech regime. In so doing, they sought to achieve equality of political representation in major decision making bodies or, ideally, complete independence from the Czechs (Leff 1988, p.160).

That is not to say, however, that the Slovaks did not benefit from the union. The 1920s saw an influx of Czech civil servants and administrators into Slovakia to re-organise the local administrative and educational system. These actions benefited the Slovaks in that they finally gained recognition for their own language, which could now be taught in schools. The Czechs also introduced significant other improvements in the education system. In terms of political development, a multi-party system of government was also established in which Slovaks were given freedom to exercise their democratic rights. This period afforded them the opportunity to develop and express their national consciousness in a climate of uncensored political freedom. Furthermore, as well as enhancing the quality of education and administration in the region, the union with the Czechs resulted in the development of significant agrarian reforms which greatly improved the productivity of the agricultural sector.

However, it was perceived by some disaffected Slovaks that, in fact, the Czechs were dominating the key positions in the civil service, education, government, the army and

business, to the detriment of Slovak nationals. To some extent this was true. When Bohemia was hit by unemployment during the world recession and great depression of the 1930s, the Czechs were unwilling to give up their jobs in Slovakia to return to Bohemia, where there was little prospect of finding employment. The problem was further exacerbated by the fact that the programme to educate the Slovaks had created an educational and professional elite which was then given no opportunity to gain access to power (Korbel 1977, p.116).

In terms of economic development, by the end of the First Republic in 1938, Czechoslovakia was one of the ten most industrially developed countries in the world. It had a comparatively high literacy rate and a very well trained workforce. The country had a very good reputation for producing high quality consumer and industrial goods. Such was the pre-war reputation of Czechoslovakia as a major industrial producer, it is still commented upon. In evaluating the strengths and weaknesses of the Czech and Slovak republics, as they face the challenge of economic transformation today, external observers view the quality of Czechoslovakian technical labour as a major plus factor. During informal discussions with an Austrian businessman in Prague, for instance, the author was advised that his main reason for seeking to invest in Czechoslovakia was the quality of the labour.

Nevertheless, by the end of the First Republic, the balance of wealth and industrial development was unequally distributed between the two regions with the greater concentration of economic wealth still concentrated in the Czech lands.

The disparity in the pace of industrial development between the two regions was a major bone of contention. Some Slovaks believed that competition from the more developed Czech lands and the depression of the 1920s had severely retarded the development of industry in Slovakia, resulting in economic hardship and a major wave of emigration from the region.

For many Slovaks, the First Republic was characterised by the absence of Slovak autonomy. Additionally, the tendency towards Czech centralism and the inequality of power sharing in the diet continued to fuel disappointment and resentment in Slovakia against the Czechs. From the Czech perspective, the First Republic saw significant political economic and cultural advances in their region which aligned them very favourably with the most advanced western European countries. As regards their relationship with the Slovaks, however, the Czechs are often criticised for failing to take the time and make the efforts to understand Slovak society and culture. They were criticised for regarding Slovakia as an extension of Bohemia (De Candole 1993, p.7-8).

The enthusiasm with which the Slovaks embraced their perceived independence under the Nazis suggests that the gap between the perceptions and aspirations of the Slovaks still differed significantly from that of the Czechs. Consequently, it is possible that the final demise of the republic might have come about, albeit later rather than sooner.

The reality is, however, that it was the intervention of the Second World War and the subsequent forty-one years of communist rule which directed the future development of the region and not the political will of the Czechs and Slovaks.

SPURIOUS SLOVAK INDEPENDENCE

The period from 1939 to 1945 represented the only time in the history of the Czechoslovak republic during which the Slovaks experienced independence from the Czechs. The events surrounding this period evoke such powerful emotional reactions that they continue to exert a significant influence over the relationship between the two nations - some forty years on. According to Bosak (1991, p.67):

> The emergence of a separate Slovak state in 1939 and its endurance until 1945 remains a very controversial question, subject to contradictory interpretations, and evokes great emotion.

The 'controversy' surrounds the fact that in 1939 the Slovaks made a pact with the Nazis to co-operate with them at the time of the German invasion of Bohemia and Moravia. As a result of this agreement, the Slovaks either 'gained independence' or 'became a puppet regime controlled by the Nazis' depending on one's point of view. An evaluation of the rights and wrongs of such political decisions are complex, subjective and emotive. The choices facing the Slovaks at this time must have been very difficult - either to sign the pact or face the same fate as their Czech neighbours.

In terms of justifying the pact between the Slovaks and the Nazis, it is sometimes argued that the negative Slovak experiences of the 1920s and 1930s justifiably led Josef Tisot to seize the opportunity, presented by the Nazi invasion of Czechoslovakia, to create an independent state.

There can be no doubt that this period saw some positive outcomes for the development of the region. The majority of Slovaks did not suffer the same harsh fate as the Czechs at the hands of the Nazis. In fact, the Slovaks were permitted to thrive intellectually and develop a stronger national identity. The region experienced significant economic growth, especially in the industrial sector, where the production of arms was expanded in order to service the Nazi war machine (Korbel 1977, p.160).

On the negative side, there was no real democracy within the independent Slovak state. It was indeed a Nazi puppet regime. The Slovaks were firmly under the control of strict clerical rule, as directed by the Nazis. Moreover, the state suffered from forced labour, and violent anti-semitism. Josef Tisot paid 100 RM (Reichsmark) to the Nazis for every Slovak Jew that was sent to a concentration camp. It should be pointed out, however, that anti-semitism has been an endemic feature of much of eastern Europe for centuries. The fact that the Jewish cemetery in Prague is shaped like a hillock as opposed to a flat piece of ground is further testimony to this anti-semitism in that the Czechs refused to grant the Jews any additional land for burials. Consequently, the Jews were forced to layer graves of their dead, one upon the other. Furthermore, it is not by accident that Hitler established the majority of his concentration camps in the East and in Poland in particular and not the West (Rothschild 1974, p.133-134).

By 1944, the repression in Slovakia resulted in an ill-fated and bloody uprising led primarily by communist partisans against the Tisot regime. The objective of the Slovak uprising appears to have been to re-establish a joint republic with the Czechs. Although the revolt was unsuccessful, it provided some basis of support for the re-establishment of a united Czechoslovakian republic in the immediate post war period. The revolt went some way towards re-establishing the credibility of Slovakia with

the Western allies and other political groups in the region (Leff 1988, p.91-92).

The Czechs, however, suffered badly under the Nazi occupation in terms of persecution, deportation and repression. Indeed, forty-five years on from the end of German occupation, the distrust and dislike of Germans is still very strong amongst them. As recently as 1992, the depth of this mistrust manifested itself in demonstrations by the older generation against the proposed Czechoslovakian - German friendship treaty.

What was the impact of the period of Slovak independence on the relationship with the Czechs? It is legitimate to pose this question as the period of Slovak independence and Nazi occupation still loom large in the psyche of many Czechs and Slovaks.

Some Slovaks identify very closely with the positive aspects of the period. They look back to this era in order to substantiate some degree of legitimacy and precedent for the establishment of an independent state after the Velvet Revolution. Some Czechs continue to remember, with bitterness, the perceived collusion of the Slovaks with the Germans at a time when the Czechs were suffering at the hands of the Nazis. They will also point out, grimly, that the date of Slovak independence, still celebrated in Slovakia, is the date of the invasion of the Czech lands by

the Germans. An additional irony is that such celebrations take place in Namesti SNP under the monument to the Slovak anti-nazi national uprising of 1944.

The divisive legacy of this period in the history of Czechoslovakia, following upon an already diverse heritage, continued to assert a strongly negative influence on relations between the two regions. The policies of the ensuing Communist regime served only to intensify these divisions over the next forty years. Communism suppressed the unreconciled differences between the two regions which would otherwise have been allowed to develop naturally to their ultimate resolution - be it separation or integration.

COMMUNIST REPRESSION

The immediate post war problem facing Czechoslovakia, in terms of political reconstruction, is described by Leff (1988, p.86) as follows:

> The central problem of 1945 was to reconstruct partisan and governmental institutions in a way that would make them flexible enough to respond to the complexities of the new balance of power in the country.

This new balance of power included such diverse elements as the Czech government in exile headed by Edward Benes, and

the Slovak partisans, a significant element of whom was influenced by the Communist Party. The period of Slovak independence had been a watershed in the consolidation of Slovak national self affirmation. During this time, Slovakia had demonstrated its ability to function as an economic and political unit independent of Czech influence. Thus, the experiences and expectations of the various interest groups, when they came to the political negotiating table, were significantly different from those that had existed prior to the Second World War.

At this point, it seemed possible that the Slovaks might achieve the equal balance of power which had been denied them in the First Republic. The Kosice agreement of 1945, which set out the framework for the provisional government, was based upon the principle of equals with equals. However, the reality was that Benes reviled the Slovak state as a Nazi puppet and was 'both judicially and by personal predilection' a supporter of the centralist constitution of 1920. Consequently, he used his influence to re-establish the principle of asymmetry (Leff 1988, p.90).

The divisions between Czechs and Slovaks were cleverly exploited politically at this time by Clement Gottwald, the leader of the Communist Party. Ostensibly, he supported greater autonomy for the Slovaks. However, as subsequent events revealed, this support was in fact part of a

carefully orchestrated strategy to gain influence and support in the region, prior to the communist takeover in 1948. It was an integral part of the communist philosophy of divide and rule which was to underpin the activities of the regime in the country for the next forty years.

In effect, the 1948 communist takeover in the region created a much more restrictive regime, with a greater degree of concentration, than that to which the Slovaks had been subjected during the First Republic. The centralised structures imposed by the communist regime in order to exercise control and gain compliance were so extreme that Slovakia almost ceased to exist as a separate entity. It was divided into three administrative regions. Bratislava no longer received any legitimate recognition as the state capital. Those Slovaks who wished to gain influence under the regime did so by seeking to gain power in Prague. During the 1950s, the population of Slovakia suffered the same purges, repression and suppression as that of their Czech neighbours.

By the early 1960s, the changing international political arena and poor economic growth internally began to foster a growing nationalism in Czechoslovakia. In Slovakia this nationalist feeling manifested itself in increasing demands for greater influence within the Party, e.g. by selecting their own party elite in Slovakia. This led to the appointment of Alexander Dubcek as leader of the Slovak

Communist Party in 1963 and ultimately to his appointment as the leader of the Czechoslovak Communist Party. This movement culminated in the 1968 Prague Spring and the subsequent period of normalisation.

FEDERATION ACHIEVED

In terms of the nationalist debate, a major outcome of the events surrounding the Prague Spring was that the communist regime agreed to the establishment of a federal republic in Czechoslovakia. In October 1968, Slovakia was given permission to proceed with federalisation. Ostensibly, the outcome of the federation was that the Czechs and Slovaks were to receive equal autonomy, with the equivalent of national sovereignty for each region.

However, the reality of normalisation ensured that such autonomy for Slovakia would not be realised. In December 1970, there was a constitutional revision which reduced the degree of Slovak autonomy granted to that of token significance. Equal Slovak responsibility was granted only in those areas where there were weak power bases, e.g. the legislature and constitutional courts. The majority principle still continued to operate in the decision-making process and the principle of asymmetry still continued to dominate the Communist Party and the political structure generally. Illusions of Slovak equality in decision-making

were reduced to declaratory significance only (Leff 1988, p.244-247).

The reality was that federalisation served only to extend the effectiveness of the policy of normalisation in the region. Under the guise of federalisation, the Party replaced dissident Czechs with more compliant Slovaks in key administrative and political positions. The milder treatment of Slovaks as opposed to the Czechs during this period further re-enforced communist control in the region, through the selective application of the divide and rule strategy. The communists gained further compliance by the selective application of the material rewards and coercion that had characterised their rule throughout the period of the regime. The Party undertook a series of economic measures designed to improve living standards throughout the country. The price to be paid was political compliance from the population. The greatest focus of concentration, however, was on improving the economic condition of Slovakia as opposed to the Czech lands. There was concentrated growth in the areas of heavy engineering, petrochemicals, armaments and agriculture. Bratislava became the second largest city in Czechoslovakia.

In terms of standard of living Myant (1988, p.261) notes that:

'Slovak equalisation of living standards has been regarded as one of the most impressive achievements of centralised planning'.

Consumer spending per head in Slovakia by 1983 was 92% of the Czech level compared with 68% in 1953. In terms of industrial output Slovak output grew from 72% of the Czech level in 1953 to 81% in 1983 (Myant 1988, p.261).

Although the economic gap between the regions was reduced, it was achieved at the price of greater political and social division between Czechs and Slovaks.

The outcome of this policy according to Leff (1988, p.263) has resulted in:
'a new roster of grievances and betrayals ...from the experience of federalisation'.

Over the period of federalisation, commentators have noted that the Slovaks exhibited much less resistance to the regime than the Czechs. Only eight of the early Charter 77 members were Slovaks and most of those lived in Prague. Moreover, the output of Samizdat, illegal political writings produced and disseminated by dissidents, was significantly lower in Slovakia, presumably due to the lower level of dissident activity in the region. In terms of Slovak commitment to a federation, they experienced a less repressive regime generally marked by milder purges in Slovakia than the Czech republic following the Prague Spring (De Candole 1993, p.8).

From a Czech perspective, federalisation has been

characterised by a policy of deliberate favouritism towards the Slovaks, which served only to increase the antagonism between them and the Czechs.

For the duration of the federation, the Czechs perceived Slovak growth in terms of their loss. This is illustrated by the Czech reaction to the greater hardship that the Slovaks have undoubtedly suffered since the liberalisation of 1989. A frequent unsympathetic response of the Czech man in the street to the situation is:
'The Slovaks did very well for themselves under the old regime. It is time they suffered a bit.'

Thus, even as the communist chapter closed in Czechoslovakia, it opened a pandora's box of suppressed tensions and latent conflict. After the Velvet Revolution, the scene was set for these problems finally to be acted out to their ultimate conclusions.

CHRONOLOGY OF THE DEATH OF A NATION

With the demise of Communism in Czechoslovakia, James de Candole (1993, p.11) notes that:

> Czechoslovakia had to look within the state for a reason to justify its continued existence.....they found only a history of perceived mutual

> betrayal, broken promises and above all a power vacuum in the federal institutions of government which made agreement on the future constitutional relationship between the two nations impossible.

As the previous sections of this chapter have shown, history deemed that the demise of the republic was almost inevitable. The following analysis will chronicle and comment upon the critical events of the short lifespan of the republic and assess their impact upon the activities of enterprises within the Czech and Slovak Republics.

NOVEMBER 1989: The liberalisation of Czechoslovakia at this time saw the continuation of the same political federal structure which had been established in 1968 in the aftermath of the Prague Spring. However, as well as the federal parliament, both republics retained their respective national councils. The role of the councils was to delay with those issues that primarily affected their own region. From the outset however, it was unclear as to how the roles of the republican and federal political institutions should be distinguished, thus creating areas of potential political conflict and disharmony which were not slow to reveal themselves.

MARCH 1990: The first critical landmark on the route to the dissolution was the 'hyphen debate' over the name of the new republic. Slovaks gathered outside the parliament in

Bratislava to protest against the country's new name - The Czechoslovak Federal Republic. The Slovaks wanted the name to be hyphenated, at least, in order to illustrate the equality between the two nations. The Czechs reluctantly agreed to change the name of the state to The Czech and Slovak Federal Republic. These incidents highlighted the fact that the spectre of asymmetry and equality of representation which had dogged the previous history of the Republic were still very much to the fore in the Slovak psyche.

The trivialisation of the event in the minds of the Czechs also illustrated that, despite the chequered history of their relationship with the Slovaks, the Czechs still failed to appreciate the depth of feeling amongst Slovaks concerning the nationalist issue. The Czechs perceived the incident as full of 'sound and fury signifying nothing'.

The continued refusal to appreciate the significance of the nationalist question was evident from comments made by professional colleagues to the researcher while visiting the Czech republic in 1991:

'The Slovak question is not important. They are always complaining.'

'The Slovaks do not want independence from the Czech Republic. They have too much to lose.'

'It is a game being played by politicians.'
Sometimes, even the author's questions on the Slovak question were not even deemed worthy of an answer and were greeted with a dismissive shrug.

JULY 1990: The first free elections took place in the republic for forty years. There was a 97% turnout. From the election results two parties emerged as the dominant forces on the political scene - the Czech Civic Forum and the Slovak Public Against Violence. Petr Pithart and Vladimír Meciar became the republican prime ministers of the Czech Republic and Slovakia respectively. Almost immediately Meciar sought greater political autonomy for Slovakia by pressing for special republican powers to deal with such questions as the issue of minority ethnic groups. It was clear that political affiliations were aligning themselves along nationalist lines and that latent fundamental differences between the two republics were beginning to re-emerge.

SEPTEMBER 1990: The growing divergence in economic aspirations between the two was highlighted when Václav Klaus launched his radical economic reform programme. At this time, Slovakia wanted a slower reform programme but their request was unheeded. Given the industrial and general economic structure of the two regions, it was clear that Slovakia was always going to bear the greater brunt of the impact of economic reform, especially in relation to

unemployment. It was not surprising, therefore, that they should wish to pursue a more gradual rate of economic change. However, as history continued to repeat itself in stark fashion, no concessions were forthcoming for the Slovaks. Indeed, it was seen by some Czechs as only just that the Slovaks should suffer some economic hardship, given that they had prospered economically more than the Czechs, under the communist regime. Relations between Czechs and Slovaks began to deteriorate more significantly from this point.

FEBRUARY 1991: As part of the process of political evolution, whereby the leadership of the country evolved from the former dissident elite to the emergent class of politicians, Civic Forum split, spawning the Christian Democratic Party led by Václav Klaus. One month later the Public Against Violence split, leading to the formation of The Movement For a Democratic Slovakia led by Vladimír Meciar. These emergent parties under the direction of their highly charismatic leaders were to prove the only significant political players in the subsequent break-up of the republic. In this month also, Havel called for the start of discussions to prepare permanent federal and republican constitutions. At this point the stark division between the two republics became clear. There were fierce debates and disagreements over the relationship between the Czech Republic and Slovakia. Meciar demanded that over a number of years Czechoslovakia should be transformed into

a loose union of two independent sovereign states, or 'confederation'. This alternative form was to dominate much of the subsequent political discussion on the future of the republic. This concept, however, like many other constitutional issues discussed by the federal parliaments was ambiguous and ill-defined, a fact which only added to the complexity of the debate.

APRIL 1991: The date is regarded by some commentators as the time at which the fate of the republics was truly sealed. At this time Prime Minister Meciar was dismissed from his position, charged with abuse of power and general incompetence. He was later accused of blocking efforts to dismantle the secret police networks and destroying evidence of his own collaboration with them. It was also claimed that he used secret police files to blackmail opponents and gain political favours. Given Meciar's classic communist background and training, the accusations were probably valid, although never proven.

Rather than discredit Meciar, his dismissal and the accusations against him achieved exactly the opposite effect. These events served to place the former communist apparatchik in the position of national hero, from which he was able to exploit the nationalist issue for his own political gain (De Candole 1993, p.10). His supporters demonstrated to demand his reinstatement claiming that it was a Czech plot to discredit Slovakia in the eyes of the

East. This sensitivity is frequently exhibited by Slovaks who feel that the West has an inaccurate perception of their nation. They will frequently exhort foreigners to tell others that they are not bad people. This view is probably a response to forty years of anonymity under communist rule and hyper-sensitivity to the fact that they support an ex-communist, nationalist leader, who is so strongly anti-Czech. Once the credibility of the Czech Republic had been undermined in the eyes of the Slovaks, they refused to believe any accusations made against Meciar, however valid.

As support for Meciar grew, that of the Slovak prime minister Jan Carnogursky waned due to a series of political compromises he undertook during negotiations with the Czechs to try to agree a constitution. So successful was Meciar in playing the nationalist anti-Czech hand that in April 1993, over 40% of Slovaks still blamed the country's problems on the post-communist government as opposed to the previous regime. As De Candole (1993, p.10) notes:

> Nationalism provided Meciar and his Communist associates with the ideological cover for regaining power. He demanded a 'confederation' together with pressure for autonomy, anti-Czech agitation and the rejection of the Czech political and economic reforms.

SEPTEMBER 1991: By this time, Meciar's Movement For A Democratic Slovakia had obtained 30% support in opinion polls in Slovakia compared with only 12% for the ruling

Public Against Violence Party. Meciar demanded that the parliament should adopt 'a declaration of Slovak sovereignty' which he finally achieved after the success of his party in 1992 elections. Meciar had set an agenda for Slovak claims concerning their relationship with the Czech republic which clearly rejected the existing federation but failed to provide a practicable alternative with which to replace it.

OCTOBER 1991: Such was the popular strength of feeling on the nationalist issue that, less than twelve months after he was hailed as the leader of the new nation, Havel was pelted by eggs thrown by Slovak nationalists, when he visited Bratislava.

NOVEMBER 1991: Stalemate over the deadlock situation regarding the constitution led to a proposal by Havel that there should be a referendum on the future of the Federation. It had taken only twelve months for relations between the two republics to deteriorate to such an extent that the dissolution of the republic was already being viewed as an option by politicians. Most Slovak deputies and communist opposition voted against all six proposed drafts of the wording of the referendum. The proposed referendum never took place. The Slovak deputies opposed the referendum because they were uncertain as to whether the Slovak people would support it. Indeed, at this time they were not sure that they wanted it either. The

communists still supported the centralist policies of the old regime and saw the dissolution of the federation as politically unacceptable.

MAY 1992: By early 1992 it was clear that the federal assembly was divided on Czech and Slovak lines. Given the wide divergences in views and aspirations between the two groups, it was impossible to reach any decisions on major issues of policy. The fundamental bone of contention between the two nations continued to be the form of co-existence that should be adopted by the respective republics. The Czechs wanted a functioning federation while the Slovaks wanted a loose confederation of sovereign states.

During the pre-election campaign leading up to the country's second post-communist elections the main parties in the Czech and Slovak republics lined up behind their respective political parties along nationalist lines. Meciar promised a declaration of sovereignty and a Slovak constitution by September 1992. Klaus and the Christian Democratic Party adopted the view that a functioning federation was their aim but that, in the final analysis, if this were not possible they would sanction Slovak independence.

5TH JUNE: The second election since the end of communism achieved an 85% turnout. Klaus and the Christian

Democratic Party together with Meciar and the Movement For A Democratic Slovakia won control of the federal parliament between them. Both parties obtained substantial majorities in their respective republican parliaments. Klaus campaigned and was successful on the platform of rapid economic reform, while Meciar was pressing for greater Slovak sovereignty and slower economic reform. The basis of Meciar's campaign was the nationalist issue, to which the Slovaks had given an unequivocal electoral mandate for support. It was clear from the outset that ideologically and economically the aspirations of the main political players were widely at variance with each other and becoming more discordant by the day. The chances of the Republic remaining intact were becoming very slim indeed.

Immediately after the election, the Slovak party strengthened its antagonistic response to the current federal situation between the states. When Havel commissioned Klaus to begin the formation of the federal government, a task usually undertaken by the majority party, the Slovaks objected. They argued that their nationalist interests were being ignored as they were not involved in the selection of the new federal government. Slovakia also unilaterally disbanded the federal information and security agency, an action which the Czechs considered to be unacceptable (Obrman 1992, p.26-31).

In terms of popular response to the situation, there was a

demonstration of 100,000 people in Slovakia in favour of a common state. In Prague, 26,000 people signed a petition calling for a referendum on independence. From such sporadic incidents involving relatively small numbers of people, it is difficult to generalise on the prevailing mood of the majority of the population. However, the incidents do highlight elements of discontent within the respective republics over the prevailing political situation.

JUNE 1992: Beginning on 9th June there took place three rounds of post election talks between Klaus and Meciar. The apparent objective of the meetings was to form a new federal government. However, the agenda very rapidly changed to that of discussions as to how the federation should be divided. At the first meeting on 9th June it took only forty minutes for discussions on the dissolution of the republic to begin. After fourteen hours of negotiations Klaus declared that 'the Federation is lost'. It was clear from the negotiations that both parties could agree on the secondary issues but were unable to find common ground on the most important issue - the constitutional structure of Czechoslovakia (Obrman 1992, p.26-31).

The Slovaks favoured a confederation where Slovakia would become an independent state under international law but would retain a joint defence, currency and foreign policy

with The Czech republic. Klaus considered this alternative a joke. The Christian Democratic Party wanted either federation or disintegration. After the Prague meeting of 17th June Klaus and Meciar agreed on a referendum on the Czechoslovakian constitutional set up in both republics. However, they failed to agree a fixed timetable and the agreement proved to be worthless. It became increasingly clear that the ideological differences between the two election winners as well as their different perceptions of the role of the federal institutions would make the formation of a solid government with a long term agenda impossible. Although there was still no agreement on the political way forward.

19TH JUNE: In a radical move towards the dissolution of the republic Klaus and Meciar emerged after twelve hours of discussion with a draft federal government programme. It greatly reduced the power of the federal government to that of a caretaker government with only a temporary mandate to manage the split-up of the Federation, thus clearly signalling the impending dissolution of the Federation.

The reality of the results of the election were that any minority federal government that failed to receive the full support of both the Christian Democratic Party and The Movement For a Democratic Slovakia could not survive. Both sides had enough votes in the Federal Assembly to block any government of which they did not approve. It was agreed at

the negotiations that the republics would be given until 1st September 1993 to decide the future constitutional set up of Czechoslovakia from the available options of federation, confederation or independence.

In some respects the meeting was successful in precipitating the orderly break up of the Federation and retaining the momentum for economic change. It was agreed that the post 1989 economic, political and social developments should continue. This was an important concession for Klaus who wished the current mode and speed of economic reform and privatisation to continue.

It was agreed that, should the republics wish to dissolve the Federation, this should be carried out in an orderly fashion. Secondary issues relating to the possible dissolution were resolved by drafting a series of laws to facilitate the dissolution process and integrate the federal members of parliament into the respective republican national councils. It was agreed that these agreements should not affect relations with the other political parties. Both parties were to sign an agreement deciding on the future of the administrative bodies by 31 July 1992. Klaus and Meciar agreed that the principles set out in their agreement should be binding and that regular meetings should be held to reinforce them.

However, the meeting still left open the final definition

of the relationship between the two republics. Thus, although some important issues had been settled, the fundamental question on the future relationship between Czechs and Slovaks was still unresolved (Pehe 1992, (a) p.12-16).

2 JULY 1992: The new federal government was sworn in.

FEDERATION, CONFEDERATION OR INDEPENDENCE?

The results of the general election had made it clear that it was no longer possible to accept the present constitutional arrangements between the republics. There was, however, great confusion and misunderstanding as to what the new relationship should be.

From a Slovak perspective, there was confusion about viable alternatives. Although ill-defined, the notion of confederation with a weak federal structure and strong republics seemed to be the favoured option rather than full independence from the Czech Republic. The position of Meciar on the subject of independence was somewhat unclear. He never overtly called for Slovak independence but advocated specific measures which it would be almost impossible to implement within the framework of a federation or even loose confederation between the republics. His adoption of an independent Slovak constitution from 1st September 1992 and his calls for a

separate Slovak president created major legal problems as they were not permissible under the terms of the existing constitution. Before the election, Meciar was considering the establishment of a Slovak National Bank that would have made it impossible to maintain a common federal economic and monetary policy.

Despite the above actions, Meciar continued to press for a confederation. There are several explanations put forward as to why this was the case. It could have been a tactical move to be in a more powerful position when negotiating with the Czechs over the new relationships between the republics. Many people questioned whether Meciar actually wanted independence from the Czech Republic, given the potentially adverse economic and political implications for Slovakia. It was also argued that Meciar could simply have been stalling for time in order to secure as much of the federal budget as possible before the split.

From the Czech perspective, the choice was clearly a functioning federation or a split. Many Czechs perceived Meciar's notion of a confederation as Slovak independence being paid for by Czech banks .... and it was not on! The Czechs accepted that the results of the election had rejected the Federation in its present form. Moreover, the current situation with the distribution of seats in the federal parliament meant that there would undoubtedly be a slowing down of the rate of economic reform. It was

becoming increasingly clear to the majority of Czechs that, given the political and economic differences between the two republics, the dissolution of the Federation into two separate states was the only acceptable alternative (Pehe 1992, (a) p.12-16).

THE REFERENDUM DEBATE

Discussions on the form that the relationship between the two republics should take led logically to considerations of how the issue should be decided. After the elections Slovak representatives called for a referendum to decide on the future of the Federation, arguing that this was the only legal and constitutional means by which the Federation could be dissolved, in accordance with the Federation Law of 1991. They accused the ruling parties of using undemocratic methods and political arrogance to decide the fate of the nation. Moreover, they pointed to recent opinion polls which suggested that most Czechs and Slovaks would like to preserve a common state.

Those who argued against a referendum believed that the dynamics of the relationship between the two republics was such that it was impossible now to avoid a split anyway. The current situation had led to a paralysis of any kind of effective decision making which would be further prolonged

by the time it would take to prepare and effect a referendum vote. Moreover, the period of campaigning could lead to emotional confrontation and conflict between the two regions which could greatly damage the image of both republics in the eyes of the West.

There were political and constitutional problems concerning the validity of the outcomes of a referendum. If there had been a nationwide referendum it would not have been democratic. Since the Czech population is twice the size of the Slovak population, the Czechs would have been able to impose their will on the Slovaks. To avoid this situation it would have been necessary to hold a referendum in each republic. If one republic had voted to secede from the Federation its decision would have had to be respected. If the other republic had voted to keep the Federation their wishes could not have been accepted.

As Pehe (1992 (b), p.37) notes:

> It seems that a referendum can only give an unambiguous answer only if the electorates of both republics reach the same decision: whether to secede or to preserve the common state.

The ambiguity does not end there, however. Even if both republics prefer a common state there is no agreement as to what that form should be. This is well illustrated by the results of a survey conducted by the Institute for Public

Opinion Research. The results were published in July 1992 and were based upon a sample of six hundred and two respondents in the Czech Republic and five hundred and sixty-two in Slovakia. The results showed that: in the Czech Republic 38% of the population wanted a unitary state and 19% preferred a federation of the two republics; 18% wanted a federation of more than two republics, presumably to include Moravia and Silesia; 3% were in favour of confederation whilst 16% wanted to split into independent states. In Slovakia, 14% of the people wanted a unitary state; 27% were in favour of a two republic federation whilst 8% wanted a federation of more than 2 republics; 30% wanted a confederation and 16% wanted a split. Based on the confusion of the population recorded by the survey Pehe (1992, (c) p.1-5) concludes that:

> Legislative actions.....may not be the most democratic way of ending the existence of the 74-year-old state but.....the most orderly, pragmatic and non-violent way of dissolving the country, ensuring that the agony of disintegrating the state is as short as possible.

AUGUST 1992: Throughout the month Meciar continued to vacillate over his stance on whether the two republics should split. In the middle of August a draft treaty on confederation prepared by the Slovaks was 'leaked' to the Czechs who totally rejected it. They claimed that the existing international treaties was sufficient to regulate affairs between the two nations if they were to split

rather than an 'ill-defined treaty'. This provoked an outraged reaction from Meciar, which was perhaps an act of political posturing for the benefit of his Slovak populist audience. He threatened to boycott subsequent talks with Klaus. Klaus, however, with his determination to pursue his radical economic reforms, wanted to continue talking. From his point of view it was desirable to resolve the situation and eradicate the uncertainty as soon as possible. Some would argue that Meciar considered it in his best interests to slow down the negotiating process in order to retain the Slovak share of the federal budget.

At this point in the negotiations both sides were still somewhat circumspect about announcing their secession from the Federation. Such an announcement would have allowed the other republic to gain the moral high ground and declare that it was the legitimate heir to the Federation.

The Czech leaders argued that they were being forced to split because the Slovaks wanted an independent identity. Indeed, by producing a republican constitution in September 1992 the Slovaks had in fact seceded from the Federation. The Slovaks argued that they had no other option but to split as the Czechs were totally inflexible with regard to the idea of a looser union.

OCTOBER 1992: At a meeting in the Moravian town of Jihlava, Klaus finally convinced Meciar to give up the

notion of confederation and reaffirm that the federation would split on 1st January 1993. The two republics would, however, form a customs union and retain a common currency during the transition process. The agreement negotiated between the two leaders was supported by their respective republican councils. The current constitutional arrangement now required that the federal assembly sanctioned the split by political means. To this end, a constitutional amendment sanctioning the split was put before the Federal Parliament.

The existing legislation stated that the federation could only be dissolved by referendum. The proposed constitutional amendment provided for the dissolution of the state if it was agreed by the Federal Assembly or the Republican Parliament. Additionally, the legislation permitted the dissolution of the Federation by means of unilateral secession. After rejecting the bill twice, The Federal Assembly passed the bill at the third time of presentation. Some opposition members supported the law when they fully appreciated the political turmoil that could ensue if they did not.

Moreover, both Klaus and Meciar had enough support in their respective republican parties to render the Federal Assembly ineffective. Indeed, on 19th November, the Czech National Council effectively ended the federation by giving itself the power to govern the republic as a de facto

independent state. The resolution stopped just short of declaring sovereignty but rendered the Federal Assembly largely symbolic.

The only demands of the Federal Parliament to which the republics acquiesced were the passing of a constitutional bill on the division of assets between the states and an amendment that the dissolution would have to be ratified by a constitutional act of both republics.

JANUARY 1993: After seventy-four years Czechoslovakia expired leaving the Czech Republic and Slovakia as its successor states.

So ended a unique experiment in social and political history whereby a nation politically and peacefully divided itself into two independent constituent elements. The civilised way in which the whole dissolution process was handled has earned it the title 'The Velvet Divorce'. In terms of the absence of civil war and ethnic conflict, this may be a valid assessment of the situation. However, from the point of view of Czech organisations, for whom Slovakia is now the major foreign trading partner, the new situation is perceived to be fraught with complications and uncertainty for future economic relations between the two countries.

ORGANISATIONAL IMPLICATIONS OF THE DISSOLUTION

What, then, has the split meant for organisations whose activities span both republics?

It has, in effect, created many additional problems for organisations, already beleaguered by the plethora of changes they must now assimilate in order to survive.

Ostensibly the agreements reached between Klaus and Meciar in relation to the formation of a customs union and retaining joint currency were designed to minimise the negative effects of the dissolution on enterprises. Despite the currency agreement, however, both currencies became independent on 8th February 1993. The currency split has potentially major implications for organisations in terms of both the added administrative complexity of trading transactions, and the uncertainty created by fluctuating exchanges and currency control.

It has created additional problems also in relation to debt and payment procedures between the two nations which are significantly weighted against the Czech Republic as the creditor nation. Arrangements for payments for trade are now based on a clearing system with both currencies pegged in Ecus. The current agreement between the two republics sets a maximum permissible quarterly deficit of 4,500 million Czech crowns. Thus, hard currency payments for

Czech exports into Slovakia is likely to be a problem.

Further additional restrictions have also been introduced concerning payment for goods imported to the Slovak Republic. In most situations the payment for such goods is made only after they have been in The Slovak Republic for three months. The introduction of customs posts along the Czech and Slovak border has already slowed down the movement of goods physically which undoubtedly costs companies time and money.

The next major obstacle facing organisations relates to the major fiscal changes which have been taking place in both republics. On 1st January 1993 VAT was introduced in both republics at the rate of 23%. In Slovakia the government has introduced an additional series of administrative procedures relating to the collection of the taxes which significantly delays the delivery of goods even more (Posustova 1993, p.22-24).

The Prague Post of 10th March 1993 has highlighted how such problems have affected a major enterprise within the Czech Republic, some three months after the split. The example chosen is that of Cokoladovny, the country's major confectionery producer, which has entered into a joint venture agreement with BSN/Nestle. The company has fifteen factories located in the Czech republic and a network of wholesalers, one hundred of whom are based in Slovakia. The

enterprise employs 8,500 people. In 1992, prior to the split between the two republics, the company exported one third of the 145,0000 tons of confectionery, which comprised some two thirds of its total production, to Slovakia via its wholesaler network located in that republic. This involved an average of four shipments per day to Slovakia. Drivers used to load several orders of biscuits and confectionery onto their trucks and distribute them directly to wholesalers throughout the republic in a matter of a few hours.

However, the new system of VAT operational in Slovakia requires that the taxes be collected locally and are payable when the imported goods arrive. Consequently, a single shipment can involve a day of waiting both for the delivery driver and the customer.

As a means of reducing the waiting time the company is considering the possibility of opening a warehouse in Slovakia so that goods can be sent directly from the factories in The Czech Republic and cleared in bulk at one or two customs points only. It is anticipated however, that this strategy would increase the company's current distribution budget by 10%, creating the possibility of a price increase for consumers. Additionally, the company can see further obstacles to trade emerging with the possible devaluation of the Slovak crown and the possibility of an import tax being introduced.

More significantly for the company is the fact that the added costs generated by the changes outlined above have retarded the long term, large scale modernisation programme now being undertaken with the support of BSN/Nestlé. Recent events have 'thrown the entire process into a tailspin' according to Max Berger, Vice President of Cokoladovny's board and a representative of BSN/Nestlé. The introduction of VAT and the dissolution of the federation are added complications that foreign investors did not anticipate when undertaking their projects. Whilst BSN/Nestlé remain committed to their joint venture partner, they believe that had they been undertaking the purchase at the present time they would have valued the investment as worth less. This prediction does not bode well for those companies looking for foreign joint venture partners. The dissolution has clearly presented potential foreign investors with added leverage with which to negotiate lower purchase prices for these companies. Berger also believes that the split and the new indirect tax regime could be a disincentive to western investors generally, who are already being made hesitant by the recession in Europe.

Clearly this added complication could result in an economic and commercial no win situation for both The Czech Republic and The Slovak Republic, as firms are forced to raise prices and possibly reduce staff in an effort to meet the added costs of doing business across the border. The Czech and Slovak Republics look to be an increasingly

unattractive investment proposition for foreign investors or new entrepreneurs who must already leap through the numerous hoops of inflexible intransigent bureaucracy and widespread corruption in order to do business in these countries. The problems faced by entrepreneurs, both indigenous and foreign, when they try to establish new business ventures, will be fully discussed in the chapter on Organisational Emergence.

THE FUTURE

As regards the prospects for future development in the two Republics, it is generally agreed that the Czech Republic is likely to be the more economically successful of the two.

However, there are certain question marks over the validity of such comparisons as they assume that the political economic and social objectives of the two Republics are moving toward similar ideological and commercial goals i.e. towards a market based economy. The evidence suggests, however, that this is not the case, to the extent that the author has decided that the analysis of events and trends beyond this time will focus only on the Czech Republic. Events in Slovakia will only be included insofar as they influence the process of transformation to a market economy within the Czech Republic.

The main reason for this decision is the author's view that events in Slovakia have indicated that their preferred course of political and economic development will not be that of a market economy. Indeed, Meciar himself stated in the newspaper Narodna Obroda in April 1993 that the society of Slovakia will be 'neither socialist nor capitalist'.

Additional evidence to support this view can be found when one observes the nature of the political changes within the Republic, the control of the media and the government's decisions on the future of privatisation, all of which are significant indicators of the underlying political ideology of the ruling government.

Concerning the new current government of Slovakia, De Candole (1993, p.26) notes that:

'Slovakia is ruled by communists: former hardline communists, reform communists and nationalist communists' who are concerned with:

'A struggle over power not principle.'

This is illustrated by the way in which the balance of power between the executive, legislative and judicial arms of government in Slovakia, so crucial for the protection of democracy, has been radically distorted. The Slovak constitution seriously undermines the legislative process in favour of executive power, which tips the balance of power significantly towards an authoritarian regime (Mates 1992, p.39-43).

Additionally, all members of the constitutional court have been appointed directly by Prime Minister Meciar, against the will of parliament and in contravention of the Slovak constitution, which gives only the President the right to make such appointments. One must question, therefore, the extent to which the political and legal pre-conditions for a market economy are likely to develop.

Concerning the role of the media, the introduction to De Candole's pamphlet, by The Institute for European Defence and Strategic Studies (1993, p.25) notes that the independent Slovak government is made up of:
'At best only partly reconstructed members of the old order.....progressively eroding freedom of the press and of expression'.

In the RFE/RL research report of 2nd October 1992 on 'The Media' (Brown 1992, p.1) comments that:
'Free media are as essential to democracy as censorship is to a dictatorship'.

If this is true, then free media are integral also to the market economic reform process of which democratic government is a fundamental pre-requisite.

In further discussions within this report Pehe (1993, (d) p.35) makes the following observation concerning the media in Slovakia:

'In Slovakia the behaviour of the new government toward the media has caused serious concern amongst the Slovak opposition and in the Czech Republic'.

These concerns relate to the fact that in July 1992 the Slovak government blocked the sale of Danubiaprint, a major printing company, to a private foreign investor, arguing that it is better to be a state monopoly than a foreign monopoly. Further worries are raised by the fact that Meciar now holds press interviews for invited journalists only, thus excluding those he considers to be critical of his regime. There have also been claims of intimidation by the editors of newspapers and the head of Slovak television.

Perhaps, however, the most frightening reminiscence of the communist era is the founding of the pro-Meciar journalists association titled 'The True Picture of Slovakia', which is perceived by many as a means of press censorship. Such has been the collective impact of the measures outlined above that opposition to Meciar in the press has almost disappeared.

Finally, concerning the privatisation process in Slovakia, a major plank of market-orientated reform, on 15th September 1992 the Slovak Republic government passed a proposal suspending voucher privatisation in favour of

selling state owned enterprises directly to the highest bidder. It was argued that this was an attempt by the Slovak Government to obtain funds quickly, as their coffers were empty (Nemessanyi 1992, p.8). The reality, however, is that there is now much confusion and uncertainty surrounding government policy on privatisation. Indeed, the level of foreign investment has been comparatively low, although this is doubtless due to a variety of causes. In effect, however, it is probably true to say that the privatisation process almost ground to a halt and with it the republic's transformation to a market economy.

Thus, given the uncertainty of the future political, economic and social direction that Slovakia will seek to adopt, and the moves away from transformation to a market economy which have already become evident, those parts of this study which relate to the period from January 1993 to November 1993 will focus on the Czech Republic only.

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CHAPTER 7

CZECHOSLOVAKIA 1918-89

AN ANALYTICAL OVERVIEW

> What happens but once might as well not have happened at all. The history of the Czechs will not be repeated, nor will the history of Europe.
>
> Milan Kundera (1982, p.257).

INTRODUCTION

The objective of this chapter is to construct a framework of the political, economic and social trends which prevailed in Czechoslovakia, from 1918 to 1989. For the purposes of this analysis the short, but eventful, history of this small nation can be divided into five distinct phases, emphasising the discontinuity and change which has characterised the country since its creation.

1918 - 1939

From the period of its inception to the Nazi invasion of Czechoslovakia prior to the outbreak of the Second World War, the Republic enjoyed full independence under a limited form of democracy, which it retained until the intervention of external agencies denied the region its political sovereignty.

1939 - 1945

This period saw the occupation of the Czech and Slovak lands by the forces of the Nazi Third Reich, during which it suffered the terrors and oppression of an occupied nation. During this time Slovakia became an independent republic under the tutelage of The Third Reich, which lasted for the duration of the Nazi occupation.

1945-48

This period of Czechoslovakian history is characterised as: 'modified pluralism and the institution of communist dominance' (Wolchik 1991, p.17).

1948 - 89

These years were dominated by communist control of all aspects of political, social and economic life within the region.

1989 - to date.

1989 saw the demise of communism as a result of the velvet revolution of November 1989. It was followed by the formation and subsequent dissolution of the Czech and Slovak Federal Republic, and finally, the establishment of the Czech Republic. During this period a democratic system

of government was re-established, and the economic transition to a market-based economy began.

The above phases will be analyzed in terms of the political, social and economic events and trends which influenced the development of Czechoslovakia from its inception as a republic in 1918, to the liberalisation of the country from communist domination in 1989.

THE FIRST REPUBLIC 1918 - 1938

The creation of the republic of Czechoslovakia was undertaken by the union of the Czech and Slovak states. The primary architect was Thomas Garrique Masaryk (1850 - 1937), whose skilful diplomacy was a factor in the creation of the republic. Of all the East European countries, Czechoslovakia was the best prepared for independence (Rothschild 1974, p.75-77).

Korbel (1977, p.160) identifies the main prerequisite possessed by Czechoslovakia, which predisposed it to function effectively as a democracy, as the existence of a fully functioning legitimate legislature, where parliamentary rights were protected.

Kaldova (1978, p.241) notes that Czechoslovakia was the largest industrial nation in the Danube area. It was in fact the sixth largest in Europe. Although the country was

not possessed of many raw materials there were ample domestic supplies of high grade coal and iron ore.

In economic terms, the nation's industry was focused upon both heavy and light industry. Czechoslovakia had a highly developed armaments industry, which was enlarged and improved in the inter-war period. Skoda and Zbrojovka were armaments works with patents on some of the most advanced weapons produced. According to Kaldova (1978, p.242), the Czechoslovakian army was amongst the best equipped in the world.

In terms of social development, much of the activity focused in this area was concerned with establishing the predominance of the Czech culture and values in the region. This created problems for the state in respect of both the significant ethnic minorities within the region and in respect of Slovakia (Skilling 1976, p.8-9). To some extent, the oversimplification of these underlying problems ultimately contributed to the demise of the Republic.

Wolchik (1991, p.15-17) presents a wider perspective on the broader underlying problems of the region, and concludes that, immediately prior to the Nazi invasion of Czechoslovakia in 1938, the continuity of the region was already threatened growing social, political and nationalist issues.

What were these issues? In terms of the political dimension, the system comprised a multiplicity of parties and proportional representation, which allowed the communist party to manoeuvre itself into a position of power. From this situation, it was ultimately able to engineer the downfall of democracy in post-war Czechoslovakia. Economically, the 1930s depression which was affecting Western Europe at this time also impacted on living standards in Czechoslovakia.

The nationalist question was, undoubtedly, a major destabilising factor in the region, where government policy consistently sought to extend Czech influence. Czechoslovakian policy on land reform towards the 3 million Germans living in Sudetenland meant that lands owned by this minority were reclaimed by the state and redistributed to Czech nationals (Brogan 1990, p.79). Moreover, loans to finance industry in this area were often contingent upon Czechoslovakian nationals being given employment in the enterprises seeking the loans. This led to an influx of Czechoslovakian nationalists into the area, which created further discontent amongst the German minority.

The other dissatisfied minorities in the region included 100,000 Poles in Teschen, half a million Hungarians in Slovakia and 400,000 Ruthenians living in the eastern section of the country. There was also the continuing tension between Czech and Slovak politics, due to a

combination of historical, cultural and social differences, which continued throughout the First Republic.

However, despite the problems and weaknesses in the system outlined above, democracy continued to exist within Czechoslovakia and was only destroyed by external forces and powerful international events, over which the region had no control (Gati, 1991, p.6).

THE NAZI OCCUPATION 1938 - 1945

The First Republic was initially dismembered by the Western Allies at the Munich agreement of 1938, whereby they agreed to the ceding of the Sudetanlands to the Germans. Bohemia and Moravia were annexed in 1939, and Slovakia was set up as a semi-independent, Catholic dictatorship.

As a consequence of this international manoeuvring, Edward Benes, the President of The Republic before and immediately after the Second World War, is said to have felt bitterly betrayed by the Allies, and was, consequently, more positively predisposed to Russia and Stalin than might otherwise have been the case.

Although a contributory influence to the events which followed the War, it is doubtful whether Benes view of Russia could have significantly influenced the course of events, as they unfolded. In terms of the impact of the

Nazi occupation upon Czechoslovakia, according to Brogan (1990, p.79) the country suffered less in the war than any other European country except Denmark.

This view is borne out to some extent by Kaldova (1978, p.242), who notes that the Nazis, when they occupied Czechoslovakia, expanded the already highly developed armaments industry in Bohemia and Moravia. Additionally, this region possessed an ample supply of skilled labour. The Allies did not bomb Czechoslovakia, and significantly for the future of the region, he comments that:

> Very little damage was done to the industrial plants of Czechoslovakia during the War, and the communists took over a highly developed industrial country. (p.242)

According to Korbel (1977, p.157-160) however, the occupation impacted significantly upon the Czechs and Slovaks in different ways, and added to the complexity of the nationalist debate. It also contributed to the tension and political conflicts, which were to characterise the future relationship between the two groups.

During the period of occupation, the Germans sought to eliminate all aspects of Czech culture, and to destroy the Czech value and belief systems. Simultaneously, the Slovak regime, in response to its initial collaboration, was given greater autonomy over its own affairs.

The Soviets liberated Eastern Czechoslovakia in 1944, and in 1945, Prague was liberated by a Communist-led resistance movement, which then welcomed Russian troops into the capital.

LIMITED POST-WAR PLURALISM 1945-1948

The immediate post war period in Czechoslovakia is termed the end of 'the Slovak Road' (Myant 1989, p.4) due to the fact that by 1948 the future development of the country would be totally suborned to the needs of the Soviet Union.

The end of the War, however, did see the re-establishment of democracy in Czechoslovakia. In 1946, there were free elections at the end of which the Communist Party emerged with the largest number of votes. They won 38% of the vote giving the party 114 deputies out of 300. The Social Democrats, who won 39 seats, joined with the Communists to form a majority government (Krystufek 1981, p.18-19).

There were sound reasons for the initial support of the communist regime within Czechoslovakia, as noted by Krystufek, (1981, p.24). In March 1945, when the agreement for the distribution of political power was agreed by the Czech government under Benes, the communists saw it as a starting point for the fulfilment of their own political objectives, whilst the democrats perceived it as a practical basis for political co-operation.

The Czechs, as a nation, held no animosity to the Soviet Union. Indeed, many felt gratitude to the Soviet Union for liberating them from the Nazis. Moreover, the inter-war period in Czechoslovakia had been characterised by economic depression, and some saw socialism as an ideological progression to a more prosperous economic order.

During this period, the Communist Party ensured that it gained control of all the essential ministries, i.e. the Interior, the Police, Finance and Information. They also resorted to techniques of manipulation, persuasion, blackmail and threats, where these were considered appropriate to achieve the aims of the Party. Even when there was some disquiet over the methods being used by the Party to gain power, there was still no overt resistance from the supporters of democracy. This lack of resistance gave the communists a psychological advantage. Moreover, the techniques of manipulation used by the Party were initially introduced by the Nazis to Czechoslovakia. Consequently, there was no shock of unprecedented novelty for the politicians or the population.

The immediate post war period saw the development of an extensive policy of nationalisation led by the communist majority. Those bourgeois parties who opposed these policies were constantly outvoted in the parliament. From 1947, the Czechoslovakian economy was characterised by:

'an overwhelmingly socialist character' (Davis & Scase, 1988, p79-81).

Davis & Scase (1988, p.81) also note that, during this immediate post war period, the Czechs nationalised 60% to 70% of all industrial concerns. Thus, there was already a strong socialist movement in place by the time of the communist takeover in 1948.

Nevertheless economically, Czechoslovakia was still orientated to the West in terms of its trade profile. In February 1948, trade with the West accounted for approximately 80% of total turnover (Myant 1989, p.8).

In many ways it was better prepared than other European countries to adapt to, and take advantage of, the post-war situation. The population was both well educated and disciplined. The industries had survived the war mainly intact, and were more modern and adaptable than those of the French. Moreover, Czechoslovakia had none of Britain's imperial pretensions and responsibilities. Thus, the country was ready to take its place amongst the leading Western industrialised nations (Brogan 1990, p.82).
The country signified its intent to be part of the reconstruction of the post war-western world, by indicating its desire to participate in the Marshall Plan for post-war reconstruction. However, it withdrew from the Plan in 1947 under Soviet pressure.

In the final analysis, the destiny of Czechoslovakia was decided by international events, and the political machinations of external powers.

As Gati (1991, p.13-15) points out, the post-war political conditions and the power vacuum in Eastern Europe were favourable to the extension of Soviet power into middle Europe. It presented Stalin with the opportunity to extend the initial concept of socialism in one country to socialism in one region, and presented Russia with an additional defence against the possibility of a third world war between the USSR and the USA.

Stalin's policy of achieving socialism in one region was designed to be achieved by a policy of satellization, and this was followed by Sovietization. The process of satellization, as outlined by Brown (1988, p.15), involved several distinct phases.

The first phase involved the co-operation with other political parties in the region within the framework of coalition governments. The objective of this strategy was to provide assistance in re-building the post-war economies. This was indeed the strategy adopted by the Communist Party in Czechoslovakia, where it gained substantial support.

The second phase of satellization involved the multi-party

system giving way to bogus pseudo-coalitions with puppet non-communists. The primary objective of this strategy was to assuage the concerns of the West. In Czechoslovakia, this second phase lasted for three years up to 1948.

Thereafter, when the communists seized power in 1948, the process of sovietization began. The objective of this policy was:

> the transformation of the region's domestic, political, economic, social structures, institutions and patterns according to Soviet norms and values.....to initiate and duplicate the Soviet model in their internal arrangements
> (Wolchik 1991, p.20-21)

The coup of 1948 meant that, according to Brogan (1990, p.84):

> a democratic regime of unquestioned legality was overthrown by the Communist Party aided by street demonstrations and the moral and political collapse of the bourgeois parties

Nevertheless, a significant number of people initially welcomed the revolution. This was partly due to the fact that there already existed some popular support for the Communist Party, which had been active in Czechoslovakia between the two world wars. Moreover, the Party was well represented amongst both workers and the intelligentsia.

Additionally, in the immediate post-war period, Czechoslovakia experienced a strong reaction against the right wing regimes, which were perceived as having caused the Second World War. This resulted in a strong move to the political left.

The initial measures undertaken by the new communist regime were concerned with nationalisation, the redistribution of land, together with the dispossession of the wealth of the upper classes and the bourgeoisie. This proved to be popular with those large sections of the population which benefited from the reallocation of resources and power.

From this time, the leadership of the Communist Party began to implement the model of Stalinist Sovietisation in Czechoslovakia in terms of political structures, social transformation and the economic development of the nation.

THE COMMUNIST REGIME 1948 - 1989

Political Framework

The political framework which operated in post 1948 Czechoslovakia was that of a formal structure of government paralleled by the shadow structure of the Communist Party. The framework of government was based upon the constitution of Ninth of May, 1948. This legislation set up a federal government within which sovereignty formally rested with

the Federal Assembly. In reality, however, the office of President and Prime Minister, designated under the constitution, together with the role of the Federal Government were merely symbolic.

In effect, it was the Communist Party structure which wielded power and was responsible for decision-making at all levels within the hierarchy. Moreover, it was the dominant determining force in all aspects of political, economic and social life.

Krystufek (1981, p.67) outlines the structure of the Communist Party apparatus in terms of primary party units which operated within all organisations. They were, ostensibly, responsible for the election of the Party Committee, which dealt with the major issues within the organisation or institution for which it was elected. In reality, however, the primary party units were told whom to elect. The organisation of the party then progressed upwards through district and regional committees to the Central Committee of the Communist Party, which represented the most powerful body within the state.

Of note within this apparatus, are the 'groups of three' or 'groups of five'. These groups were directed by the local party secretary and comprised the security secretary, the local chief of social security, the local chief of police, and the regional prosecutor, together with other officials

as required. Such groups were responsible for control and security in their area, and held considerable power.

However, the overall complexity of the Communist Party apparatus was a network of controls, checks and balances set in place by a regime which trusted no-one. Central control was in the hands of the apparatus of the central committee which ensured, through several different channels, the supervision of all organs and individuals. It had at its disposal unlimited administrative, economic, police and judiciary sanctions that could be applied toward all members of the population, without distinguishing whether or not they were members of the Communist Party.

Thus, the system maintained control by setting in place counter-balancing surveillance mechanisms, so that everyone was suspicious of everyone else. Fear was the major control mechanism in this system.

The period of consolidation of Communist Party power, immediately after 1948, was characterised by show trials, political purges, forced nationalisation of private property and deportation to labour camps. The purging of workers and officials from existing positions of influence within the system, and their replacement by Communist Party members, was a major strategy of the party. The most extensive purges took place in 1951 when 75,000 office workers were removed from the administrative apparatus and

the positions filled with communists. In many instances these individuals possessed neither the ability nor qualifications to carry out the duties.

According to Krystufek (1981, p.73), it is estimated that, from the period 1948 to 1953, approximately 300,000 blue collar workers were transferred to white collar jobs. By the late 1960s the Communist Party was still unable to restore the pre-communist professional standards to the administrative systems.

Ultimately, the Communist Party became the sole administrator and only source of social and economic rewards and punishments. Thus, it could ensure compliance by the threat of deprivation of education opportunities, degradation to lower paid employment or forced changes in employment and location. It could also cut off all means of support. The state could exclude individuals from employment, and imprison them as parasites when unemployed.

The period of communist rule in Czechoslovakia witnessed only two major focuses of resistance to the regime. These comprised the Prague Spring of 1968 and The Charter 77 movement.

The causes of the Prague Spring of 1968 are normally considered to be the culmination of events dating back from the period of the early 1960s. It is generally believed

that, at this time, the negative effects of the Stalinist policy of centralisation and central planning, i.e. negative economic growth, consumer shortages, crises in agriculture and a comparative deterioration in the country's international trade position were beginning to impact significantly on the standard of living of large sections of the population. By 1962 it was felt that some radical economic initiatives would be required to restore a balance and growth to the economy. The major initiatives in planning the changes were undertaken by professional economists, especially those in the Institute of Economics. The group was headed by Ota Sik, whose name became synonymous with the economic reforms of the Prague Spring.

The essence of the reforms was based upon an attempt to replace political criteria in part by economic considerations in decision making. Thus a plan was developed to introduce profit-making entrepreneurial organisations. Prices and wages were also to be adjusted more by market processes rather than political intervention. Greater wage and reward differentials were also proposed. In these measures, however, it is important to recognise that the reforms did not advocate the abandonment of socialism, but, according to Skilling (1976, p.59):

> sought to combine planning and other indirect controls of the economy with a greater development of market relations, including the use of profit as an incentive.

Over the period of the 1960s it became clear that it would be very difficult to introduce these reforms gradually, due to the radical institutional and structural changes required to support them. Additionally, the opposition of conservative elements in the system were unwilling to acknowledge any criticisms of the existing situation.

Skilling (1976, p.46) also sees the roots of the Prague Spring in terms of broader societal discontent:

> The snail's pace of rehabilitation, Slovak discontent, ...open dissent of writers, political apathy of youth, restiveness amongst students, muffled criticism of foreign policy.

These factors, together with an intellectual awakening which undermined the political legitimacy of the regime, led to a situation where:

> All of the forces of dissent ultimately converged on the political system, as the focal point of all other faults. (Skilling, 1976, p.46).

The deepening sense of crisis and the need for change finally led to divisions within the leadership of the Communist Party itself. Novotny, the party leader was a firm supporter of maintaining existing policy, whilst supporters of the change within the Party were led by Alexander Dubcek, the Slovak party leader, who supported political and economic reform.

In January 1968, Alexander Novotny was forced to resign as head of the Communist Party, and was succeeded by Alexander Dubcek. During this period, Wolchik (1991, p.36) notes that:

'In the course of the eight months, Czechs and Slovaks challenged the shibboleths of the Stalinist system'.

It should be observed, however, that such radical changes were taking place within the existing political structure. There was no attempt to reduce the power of the Communist Party or introduce any form of political pluralism. This retention of the political framework gave rise to the phrase 'Socialism with a human face'.

The reform process ended abruptly on 21st August 1968, when the Russian tanks entered Prague. In April 1969, Dubcek was replaced by Gustav Husak, who remained in this position until the end of communist rule in Czechoslovakia in 1989.

The outcome of the Prague Spring was the policy of 'Normalisation', whereby the entire Czechoslovak political and economic system was returned to unrestricted soviet control. There was a wave of repression through education, the mass media, administration and cultural life. There was a major purge of the Communist Party and its related institutions. It is estimated that some 500,000 people, party members, intellectuals, trade unionists,

industrialists and administrators were dismissed from their positions.

The policy of normalisation also involved the 'depoliticization' of the society, whereby living standards for the population were improved in return for their non-involvement in the politics of the country. For many people this led to an escape into their private lives and the adoption of a double moral standard, whereby there was one face for the outside world, and one for one's inner circle (Davis & Scase 1985, p.156-7).

The second major focus of dissent against the communist regime began in January 1977, with the creation of a human rights campaign inaugurated by the Charter 77 organisation. This movement was not a direct political challenge to the regime. It was, however, a campaign for human, political, economic and national rights, and its very existence was seen as undermining the totalitarian system in Czechoslovakia. The objective of the movement was to achieve the widest possible involvement of citizens in defence of fundamental civil liberties.

The roots of Charter 77 lay in the alienation and repression suffered by many disenfranchised intellectuals and reform communists in the wake of the Prague Spring purges. Many were barred from public life and prohibited from following their professions. An early focal point for

the future of the human rights movements was the production and distribution of samizdat, i.e. the publication of texts and written materials which were officially censored by the regime.

The existence of Charter 77 was psychologically important, in that it was openly defiant of the regime by virtue of its existence. Despite harassment of its members, the regime was unable to eradicate this movement (Skilling, 1981, p.177-8).

In itself, the movement was limited in number and structure of membership (approximately 2,500 by 1987), and was never a political threat to the regime. However, as the events of the 'Velvet Revolution' were to demonstrate, the Charter's activities helped to destabilise the regime. Charter activists played significant roles in Civic Forum, the movement which led the revolution, and subsequently, in the non-communist government which was established in 1989 (Bugasjski, 1987, p.93).

For the majority of the population, however, the years between the Prague Spring and the revolution of 1989 were characterised by a withdrawal into private life, an apathetic view of politics, and a preoccupation with personal materialism and living standards. The almost total acquiesence of the population and the deliberately soviet-orientated policies of government have led Brogan

(1990, p.81) to conclude that:

> The Czechoslovakian Communist Party was the willing slave of the USSR. It subordinated the Czechoslovakian economic and political interests to those of the Soviet Union.

Economic Policy

The economic strategy developed by the Communist Party, and its methods of implementation, were closely integrated to the political and social objectives of the Marxist Ideology. The essence of economic strategy was based upon a planned economy with centralised direction of economic activity. Allocation of resources at national level was based upon a series of national plans to fulfil the political, economic and social objectives of the regime (Davis & Scase 1985, p.83-84).

The national plans, which were formulated and disseminated by the centre, directed the economic activity of the individual enterprises within the state. The plan determined the output quota of each company, and fixed prices at below the market level. It also determined the allocation of goods and services, as inputs and outputs of the economic system at a macro and micro level.

The criteria for planning decisions bore no resemblance to the application of the laws of supply and demand within the

economy. This strategy led to demand overhang, which resulted in a significant shortage of goods and services. Consequently, an extensive Black Market system developed. A relatively recent study of the second economy undertaken by Martin Fassman (1988, p.3), an official of the state planning office, showed that it was prevalent in all areas of economic life. It gave empirical support to the view that the use of bribery to obtain services, which were supposedly provided by the state, was prevalent throughout the system. It was also common practice for large proportions of the population to be involved in illegal economic activity. This was undertaken as a means to supplement their income, or obtain goods and services not available through official channels.

An additional weakness of the planning system is associated with the fact that company targets were set in financial terms only. Thus, organisations could produce goods not related to customer demand. The organisational implications of implementing the plan will be discussed later in this chapter.

Overall, these distortions of the economic base of the country, together with the inherent failings of the central planning system, created fundamental weaknesses which consistently undermined the stability of Czechoslovakia, and indeed, the whole region of Eastern Europe, ultimately precipitating its downfall.

The implementation of this economic strategy involved the dismantling of the capitalist system. This was achieved by means of a policy of rapid nationalisation. Property and businesses were appropriated from private individuals, and taken over by the state. Individual companies were merged into one large monopoly enterprise for each industry.

Under the communist regime, the functions of these state-owned enterprises were:

1. To produce goods and services in accordance with the national plan
2. To be a vehicle for ensuring the dissemination of the party doctrine and implementation of party objectives
3. To provide for the social and welfare needs of the employees

The absence of any profit motive, together with a situation of perennial shortages, bred an attitude of arrogance amongst employees. This was especially prevalent when they dealt with consumers who, because of the shortages and the pervasive oppression of the regime, had no power of sanction over suppliers or providers (Mills 1992, p.5).

Since the political agenda dominated every aspect of the operation of the organisation, all major planning and decision-making was carried out centrally by party officials. Within the organisation, key personnel and operational decisions were made by the party committee,

whose members were ostensibly elected by the Communist Party members working within the organisation. In reality, however, members of the committee were appointed by the local Communist Party apparatus. This committee had the right to make final decisions in all matters with which it dealt.

There was no management information in the widest sense available to budget, plan or control the future activities of the organisation. All reporting was a bookkeeping exercise of recording and reporting past performance which was relayed, retrospectively, to the centre.

All appointments and promotions were undertaken on the basis of party loyalty and qualifications. However, access to higher education was contingent upon party membership and influence. The content of education programmes was strictly screened, as a result of which the quality of management emerging from such a system was questionable in terms of competence.

The welfare function provided by the enterprise, as directed by the state, was generally considered to be of very poor quality. This was due, primarily, to the fact that many of those who qualified professionally to provide these services, e.g. dentists and doctors, were not trained to a sufficient level of competence to carry out their duties (Mills 1992, p.8). Moreover, the shortages of

medicine and equipment created a black market situation in this area also.

As part of the welfare provision, most enterprises provided crêche facilities. The rationale behind the policy was economically, rather than socially or politically driven. The economic objective was to ensure that the maximum number of people were available for employment within the regime. These additional inputs were necessary responses to the failure of the regime to invest in new more capital intensive technology. The answer to falling output levels was not to re-invest or to analyze the causes of the problem, but simply to throw more inputs, in the form of manpower, at the process.

Financially, organisations were not subject to meaningful budgetary constraints. If the enterprise incurred a substantial level of debt, it was simply rolled over into the next period by the state bank. Consequently, as a result of these 'soft budget' constraints, the state-owned enterprises accumulated massive debts over which they had little control, and within which the state encouraged them to have little interest.

A similar policy of collectivism and state ownership was implemented in agriculture, where small privately owned smallholdings were merged into large state collective farms. It was based upon the same principles of planning

which were applied to industry. The farming co-operatives were to be managed within the state plan with the application of detailed planning methods and implementation policies.

The policy of collectivism in agriculture had a relatively poor record of success. Part of the reason for its failure in summed up by Myant (1989, p.53-54) who concludes that the agricultural sector comprised:

> poorly organised and financially precarious co-operative farms based on reluctant or uninterested farmers who knew little of how to organise collective work.

The growth targets of the five year plans for agriculture were rarely achieved (Taborsky 1961, p.416). Moreover, for the duration of the communist regime, the private sector continued to supplement the output of collective farms, although the contribution declined over the period as follows:

28% in the 1960s, 13.5% in the 1970s and 10% by the mid 1980s

(Cochrane 1988, p.47-53).

Additionally, in the pre-communist years, the agricultural sector, based upon small and medium sized farms, produced enough output to meet the domestic requirements of the country. Throughout the communist period, it proved

necessary to import many categories of agricultural produce (Taborsky 1961, p.409-23).

In the final analysis, when measures were taken by the state to improve the agricultural output, it was 'at the cost of state subsidies, degradation and contamination of large areas of farm land' (Wolchik 1991). Much environmental damage was incurred by the use of low grade fertiliser contaminated with heavy metals to fertilise already severely polluted land.

Although the economic strategy of the Communist Party was ostensibly designed to disseminate the marxist ideology throughout the country, and apply the principles of its economic doctrine, the reality of Czechoslovakian economic policy was to assist the Soviet Union in the achievement of its economic and political goals. Both in terms of internal economic policy and external international relations, it was Soviet interests which were paramount, so that 'post 1950 the maximum use of Czechoslovakian industrial potential was to contribute to renewal and consolidation of the USSR economy' (Myant 1989, p.15).

These objectives resulted in a complete restructuring of the industrial base from light to heavy engineering, and from consumer goods to capital goods. The excessive demands on the raw material and energy resources of the country were never sufficient in quality or quantity to

fulfil the production quotas specified by the national economic plans.

This strategy led to structural imbalances in the system. The plan was further constrained by the lack of energy resources. Thus, every effort had to be made to find raw materials and sources of power at the expense of other economic targets. The outcome was a constant under-fulfilment of plans leading to intermittent energy shortages and power cuts.

As regards the overall effectiveness of the command economy on economic activity, Myant (1988, p.30) concludes that:

> In practice, unrealisable instructions came to be treated with contempt and orders were obeyed in a purely formal manner or evaded by methods that actually required considerable ingenuity and initiative at the lower levels in the structure. Thus the striking feature of the emerging system of economic management was the divergence between a simple theory of centralised planning and the somewhat chaotic reality.

In relation to international trade, in the immediate post war period prior to the communist takeover, trade was orientated towards the west. According to Kaldova (1978, p.243), in 1945, 45% of Czechoslovakian trade was with the West. By 1953, it had fallen to less than 15%.

Czechoslovakia joined the Soviet dominated Council for Mutual Economic Assistance (CMEA) together with the other East European countries, the ostensible objective of which was to simulate trade between the countries of the Communist Bloc. The Soviet Union became the main trading partner for Czechoslovakia. The composition of trade also changed. Czechoslovakia produced and exported heavy industrial and metallurgical goods, whilst importing raw materials and grain. The operation of a system of bilateral trade between countries also increased the dependence of the member states on the USSR. Additionally it further constrained the potential for the wider development of international trade between members.

Czechoslovakia also conducted a significant amount of trade with the developing world. Initially the primary purpose of such trade was ideologically driven, with the objective of seeking to gain political influence in these regions. Indeed, Czechoslovakia became one of the communist world's largest suppliers of economic aid to the Third World, and one of the region's main arms suppliers.

However, after the late 1970s much of the interest in trade with the Third World was concerned with the need to find sources of energy and raw materials by offering aid and trade agreements.

Nevertheless, although the negative impact of unsound economic policies created problems throughout Eastern Europe for the duration of communist rule, Czechoslovakia maintained a relatively higher level of living standard than other East European countries. This was partly due to the greater degree of industrialisation within the country at the time of the communist takeover.

This is seen as part of the reason why Czechoslovakia maintained Stalinist policies after they had been discredited by Krushev, and been rejected by other East European countries. Additionally, it is considered to be a partial explanation as to why there was less overt resistance to the communist regime than in other East European countries during the 1950s.

In response to periodic falling living standards and negative growth in the economy, there were several attempts at economic reform during the regime in 1958, the mid 1960s and the early 1980s. However, the measures were developed and designed to be implemented within the existing political and economic order, thus failing to address the fundamental weaknesses of the system (Myant, 1989, p.248-250). Moreover, there were sufficient vested interests in the retention of the old order to negate the effectiveness of any proposed reforms.

The Social Dimension

The social dimension of the marxist ideology sought to put into practice the belief that the social order of society should be revolutionised, so that the workers should gain control over the means of production. The doctrine also stated that there should be equality of income throughout the society, with the highest status being awarded to those directly involved in the production process, i.e production and manual workers (Davis & Scase 1985, p.156-7).

The implementation of this policy impacted significantly upon the occupational structure, income differentials and social stratification levels. In terms of occupational restructuring, the continued industrialisation of the country required to meet the Soviet economic objectives led to growth in the numbers of those employed in manual and technical jobs. The numbers employed in service and administrative positions within the bureaucratic structures, which were introduced to support the political regime, also increased substantially.

The shift of employees from the private to the state sector was exacerbated by the rapid nationalisation industry and the restrictions on inheritance and ownership of private property. The requirement for professionals was reduced, also, within the new order ideological conformity replaced the requirement for professional skill.

To meet the heavy industrial machinery needs of the Soviet Union and provide the energy resources required to produce them, there was a re-alignment of the labour force from the production of light industry and consumer goods to heavy engineering and mining.

Moreover, the remaining production of consumer goods involved standardisation of output to the extent that the variety of products was greatly diminished. Myant (1989, p.15) refers to the reduction in the variety of trucks and motorcycles produced and the ultimate demise of the motorcycle industry in Czechoslovakia.

The changes in the occupational structure of Czech society was accompanied by changes in the social stratification of groups within the society in terms of the status, influence, wealth and prestige that accompanied them.

A major tenet of the communist doctrine was the elimination of class and income and wealth distinctions between groups and the elevation of industrial workers to the higher levels of income and prestige within the society. This rationale was based upon the belief that the workers who are directly involved in the production of industrial goods contribute most to the economic growth of the society. Moreover, their role was considered crucial in terms of the ability of all society to achieve the output levels specified in the central plan.

The requirement to attract more workers into branches of heavy engineering led to the enhancement of rewards for these groups, and their elevation to positions of greater status within the society.

In terms of income levelling within the regime, the following tables illustrate the comparative differentials in wage levels and per capita incomes between various occupation groups.

WAGES OF DIFFERENT CATEGORIES OF WORKERS IN CZECHOSLOVAKIA (KCS) WOLCHIK, S.L. (1991) CZECHOSLOVAKIA IN TRANSITION. LONDON, PINTER PUBLICATIONS P.173

	1953	1955	1960	1965	1970	1972
Wages of: (Kcs)						
Worker	1155	1272	1406	1529	1902	2048
Engineering-technical worker	1494	1607	1868	2068	2569	2686
Administrative worker	1019	1081	1225	1319	1626	1737
Workers' wages as percentage of:						
Engineering-technical workers'	77.3	79.2	75.3	73.9	74.0	76.2
Administrative workers'	113.3	117.7	114.8	115.9	117.0	117.9

NET MONTHLY INCOME PER CAPITA BY SOCIAL GROUP (KCS) WOLCHIK, S.L. (1991) CZECHOSLOVAKIA IN TRANSITION. LONDON, PINTER PUBLICATIONS P.175.

	1956	1970	1980
Worker	501	992	1423
Employee	554	1187	1632
Collective Farmer	397	1087	1529
Pensioner	387	838	1227
Average	461	1019	1467

From the tables, it can be seen that the income differentials were comparatively small, and remained so consistently throughout the period of communist rule. Moreover the similarities in per capita income indicate that it was the numbers employed within a household which was the key factor in determining income levels, as opposed to occupation or effort within the workplace.

A lasting effect of this narrowing of differentials was the failure to provide sufficient rewards to encourage people to pursue higher education, and take more responsibility in their jobs. This excessive process of income levelling was an issue of constant concern to economic reformers, who argued that income levelling removed the incentive for workers to take on the effort and responsibility of more demanding work. Thus economic reforms proposed during this period failed to have any significant impact upon the income levelling (Wolchik, 1991, p.172-173).

Although income differentials were reduced substantially during this time, there continued to be differences based on sex, sector in which one was employed. The highest paid sectors were transport, construction and industry, whilst the lowest wages were earned by those in trade, education, and health.

The implementation of the policy of social equality led to elevation of the working class and peasants to positions of

power and influence. Such measures as the purges of the Stalin era saw 300,000 blue collar workers transferred to white collar worker jobs, for which they had neither the training or the experience. Consequently, social mobility of the society during the communist period tended to be that of the upward mobility of industrial workers.

As part of the policy of institutionalising and legitimising the communist system, access to higher education for children of previously upper and middle class children was severely restricted. Preference was given to the children of working class and peasant families.

In terms of social stratification, however, although income differentials narrowed the economic disparities between groups and educational, and promotional opportunities were designed to redress the social balance, there still remained significant differences in the values behaviour and expectations of different social groups. Educated white collar workers tended to spend more money time and effort than blue collar workers on the pursuit of cultural activities, and the furtherance of both their own and their childrens' education (Lane 1971, p.108-116).

Moreover, despite their limited access to higher education the children of white collar parents still gained some places in higher education. The children who came from well educated families tended to perform better in their

studies, despite similar material living standards to those of blue collared families.

Despite the pretensions of equality, the communist system created a new class or power elite endowed with extraordinary power and material privileges. According to Krystufek (1981, p.153-155) positions of power were held by less than 1.5% a population of 15 million. Socially, the population has suffered from the distorting influence of the communist regime on its beliefs attitudes values and expectations, not lease as a result of the 'normalisation' process which followed the Prague Spring (Skilling, 1981, p.177-179).

The role of women also changed within the new political and social order. Equality of men and women was guaranteed by the constitution, and by other legal measures within the state. There was a substantial increase in participation in higher education, and in the number of women undertaking full time paid employment. However, they still continued to be employed in lower paid and less critical occupations than men (Heitlinger 1979, p.149-152).

Moreover, despite protestations by the communist doctrine of equality of the sexes, the reality of the situation was that the inefficient system was incapable of generating growth from its existing resources. Thus, rather than undertake a programme of investment, it added to the inputs

of resources into the system. The cheapest and most available source of inputs were the under-utilised female population.

Women held fewer positions of political power in either the government or the party elites, a state of affairs which contrasted significantly with the opposition activist groups, where women had a substantial minority representation. Moreover, surveys have shown that gender inequalities continued to operate within the home which doubtless affected their ability to achieve higher status within the economic sphere and political sphere (Heitlinger 1979, p.160-161).

Wolchik (1991, p.202) concludes that:

> despite official acceptance as a goal, issues relating to gender equality were subordinated to other, high priority concerns throughout the communist period.

Conclusion

In the final analysis what then was the legacy of communism to the people of the Czech and Slovak Federal Republic in 1989?

In economic terms, the nation found itself with an obsolete uncompetitive, monolithic industrial structures, requiring

massive capital investment. Although the extent of the Czechoslovakian debt with the West was comparatively small, the collapse of the Soviet Bloc saw the demise of the market for 95% of the output of goods and services.

Politically, there was a void which required the development of a legitimate pluralist system of government with a supporting legislature and legal system.

Finally, in terms of the environment, Urban (1990, p.132-133) concludes that:

> We have inherited an industrial rust belt and natural environment savaged from forty years of scornful and systematic abuse.

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CHAPTER 8

EVERYDAY LIFE IN THE COMMUNIST REGIME

> Trying to explain life under the communist regime, is like trying to describe the sensation of flying, to someone who has never been in an aeroplane.
>
> (university professor, Leberec, April 1993)
>
> To explain living under communism, is like trying to describe life on the moon, with no gravity to pull you back to any kind of reality
>
> (government adviser, Prague, February 1992)

If the above quotes are to be believed, life under the communist regime would appear to have been akin to living on another planet.

Was life in the East so different from that in the West? Was the basis of social political and economic control under communism so fundamentally different from that of democratic western societies? The following analyses and insights into everyday life under communism will consider the extent to which the regime impacted upon the life of its citizens.

However, when considering everyday life, one must pose the question - everyday life for whom? At one extreme, for a communist party member, everyday life could reap rich

material rewards and the exercise of considerable power: even if the moral price was high. At the other extreme, for the dissident, everyday life could mean constant surveillance and harassment by the authorities. It could lead to unemployment, homelessness, transportation to the mines of Ostrava, imprisonment and death.

But what of the majority of the population between the two extremes? For them, life revolved around employment, probably in one of the monolithic state enterprises, frequently in very poor working conditions. Motivation and rewards, especially financial, were very low, unless one was prepared to join the Communist Party. Accommodation was usually a small cramped flat, frequently shared by several generations of the family. The dachas in the country, rented or owned by the majority of people, represented the only escape, as demonstrated by the weekend exodus of citizens from the town to their dachas. It was frequently commented that:
'You will only find East Germans in Prague on a Sunday' (Concierge, university halls of residence, July 1991).

Clearly, it is not possible to analyse comprehensively the full extent of the impact, which the political, economic and social policies of the communist regime had on the daily life of every section of the population.

Nevertheless, it is possible to identify some of the key

influences, which Czech citizens themselves perceive, as having the greatest effect upon their everyday existence.

POLITICAL CONTROL

The main vehicles for behavioural control within the state were the various organs of the Communist Party, which regulated all formal aspects of life within the community.

From the perspective of the ordinary citizen, the most obtrusive means by which the state tried to regulate behaviour were:

- the secret police and their network of informants
- the compilation of reports and secret police files on individuals
- the use of questionnaires to obtain information on the activities of the population
- the application of punitive sanctions and rewards to gain compliance from its citizens

As regards the secret police, the informer network was so pervasive in Czechoslovakia that the statement has been made:

'If you were in a room with five people, you knew that at least one of them was an informer' (professional colleague, Hadrec Kralove, April 1993)

A direct consequence of this system was that people stopped speaking to each other, especially if they were strangers.

The result, however, extended beyond the spoken word to that of the whole concept of body language. If one appeared too happy, then one must be hiding some good fortune - probably illegally acquired. If one appeared too depressed, then one had a skeleton in the cupboard - or was hiding something bad. Either way, such extremes of behaviour presented an opportunity for informers to ascertain the reasons for these variations from the behavioural norm by the use of spying, blackmail and other insidious techniques. This information would then be passed on to the authorities, as a result of which, the informer would hope to: curry favour with those in power, gain revenge, inflict pain on someone of whom they were jealous, or gain directly in terms of some coveted reward.

It is argued, that many people became state informers because they were pressured or blackmailed into doing so. It was not always a voluntary exercise pursued by ambitious, unscrupulous people. This view is derisively decried by those who refused to succumb to the pressures - and were willing to pay the social, economic and psychological price for their stance. In behavioural terms, the outcome of this system was that people cultivated a passive emotionless public face, which betrayed little emotion. Heads were bowed to avoid eye contact.

It was observed that:

'The loudest noise in Czechoslovakia was the deafening silence.' (travelling companion on coach journey from Liberec to Prague, April 1993).

Moreover, this fear of informants significantly affected the relationship between parents and children. They were told to go to school, sit quietly and say nothing, lest they inadvertently incriminate their parents. At home,people had to be careful not to criticise the regime in front of the children. Certain things were only discussed after the children had gone to bed.

Thus, the criticism sometimes levelled at Czechoslovakia and other Eastern Bloc countries - that the people are generally grey, expressionless and passive - is understandable. In general terms, everyone behaved in public as if they were being watched, in order to conceal any sign of disloyalty to the regime in their behaviour and activities. This was, in fact, exactly the case.

This situation gave rise to the dichotomy of having a public face, which paid lip service to the regime, and a private face, at home, which was contemptuous of the weaknesses and excesses of the communist system.

The extent of surveillance and control was also extended to include electronic monitoring and surveillance. For

example, a visit by the present writer to a management training institute for the chemical industry, located in Slovakia, revealed a room containing a bank of some forty television monitors along a wall, together with a whole range of electronic listening and recording equipment. This equipment ensured that all lectures and discussions taking place within the institution could be monitored. One suspects that such rooms could be found in most official buildings in Czechoslovakia during the communist period.

Again, a visit to the ex-regional headquarters of the Communist Party in Ostrava revealed a superbly appointed building - rumoured to be the most expensive building of its type in Eastern Europe. However, such was their obsession with eavesdropping, the walls were lined with plastic in order to soundproof them. The result is a fire hazard of horrific proportions.

In most public buildings and meeting places, one finds the ubiquitous loud speakers. In Karvina, a small town in Silesia, there is the incongruous sight of a traditional 18th century town square, complete with large telegraphs and loud speakers attached. From such loud speakers, doubtless, emanated the nationalist music and the propaganda used by the authorities to direct the assemblies and parades which took place in the town square.

At such parades one would find evidence of another dimension of the surveillance process, that influenced behaviour - the compilation of reports. Informers and secret police would be mingling with the crowd, compiling reports on the behaviour and activities of individuals. If one wanted to ensure receipt of the annual bonus at work, awarded for fulfilling the plan, one had to be seen to attend the May day rally, all political parades and visitations of foreign officials. Thus, someone would be watching and making a report on one's presence, who one spoke to, how enthusiastically one appeared to be participating in the activities. All of this information would be retained in the secret police files. If an individual wanted to advance in the regime, such a reporting system gave them the opportunity to be observed, demonstrating commitment and support for the regime. Should someone wish to protest, the same system was an active deterrent.

Any request, requiring official permission from the authorities, had to be accompanied by a series of reports from the relevant party organs attesting to the honesty and integrity of the person making the request. If someone wanted permission to travel abroad, it was necessary to receive such reports from: the local party group within one's apartment block, the party group responsible for the street, the local area Communist Party and one's employer. Individual testimonies from influential communist party

members was also helpful. Secret police files were always consulted, before permission was granted.

As will be discussed in the later section on foreign travel, this was only the beginning of a tortuous process, at the end of which, there was no guarantee that permission to travel would be granted.

The power of such reports and surveillance clearly had a major impact upon individual behaviour, both in terms of promoting support for the regime and suppressing potentially deviant behaviour.

Another weapon, related to that of the report, was the anonymous letter to the authorities - condemning an individual as an enemy of the state. The power of such letters lay in the fact that claims were always investigated. Investigations were based on the premise, that the victim of the letter was assumed guilty - until proven innocent. There was no effective appeals procedure or impartial legal system to protect innocent people.

The power of the Party was absolute. Clearly, this system was open to the exercise of abuse, and was frequently used within the regime as a weapon of blackmail and control. 'If you do not do this thing for me, I will denounce you to the authorities as a bad person' (discussions with friends during dinner, Bellevue Restaurant, Prague, September 1992).

Such an insubstantial criticism was sufficient to damn many innocent people.

Another pervading aspect of control on people's activities was the use of the questionnaire. People were required to complete questionnaires concerning their behaviour and actions on every occasion requiring a change: starting a new job, leaving a job, wishing to travel abroad, returning from a trip abroad, after meetings with any foreigners, starting and finishing higher education, wishing to relocate to another part of the state.

At the beginning of the process of normalisation in 1970, during which the government sought to remove from office all those who had supported The Prague Spring, the whole population was required to complete a questionnaire on their activities during 1968.
'Our lives were dominated by the completion of questionnaires' (professional businesswoman, during interview in Liberec, April 1993)

It is natural to assume that the response of most people completing these questionnaires would be to supply the information they believed the authorities would wish to receive. At best, therefore, the value of this information to the state must have been to keep track of the physical movements of citizens and provide a psychologically visible, although in a sense spurious, means of control

over the lives of ordinary people. Such control activities spawned a whole bureaucracy, which owed its existence to the activities of the regime. As such, the state no doubt obtained compliance from those employed within it. The range of sanctions used by the state to ensure compliance from its citizens comprised: losing one's job and home, deprivation of educational opportunities for one's family, enforced relocation, pressure to emigrate, imprisonment with hard labour and the ultimate sanction of death.

The application of such sanctions was all the more powerful, since they were controlled by a system within which the power of the state was total. There was no right of redress for people through any constitutional channels. The legal system, like all dimensions of authority and control, was, in the final analysis, totally subjected to the rule of the rule of the Communist Party. However, the impact of sanctions upon the behaviour and activities of the population changed over the period of communist rule, as a result of both internal and external pressures for change upon the regime.

Those citizens who lived under the regime for the full duration of its forty-one year existence identify three distinct phases, in terms of the impact of sanctions upon their existence.

From the period 1948 to the early 1960s, life was hard for ordinary people. During this time approximately two hundred and fifty people, including one woman, were hanged for political reasons.

People were simply taken from their homes in the middle of the night and sent to work in the uranium mines. Property was seized and nationalised, with no compensation provided to those who had previously owned it. Those families with relatives who escaped to the West in 1948, were unable to speak of them, claiming that they had died. During this time also, it was forbidden to speak English or listen to western programmes on the radio. Travel abroad during this time was forbidden, except for diplomatic or business purposes. It was perceived by many people as a truly a 'life threatening' time.

The period of the early 1960s, however, saw a liberalisation of political and economic life, as the Czechs sought to raise living standards, whilst retaining the current political and economic planning system. It was possible to travel abroad on holidays, usually to Yugoslavia, and sometimes to Italy. This new found freedom ended with what is known as the period of normalisation, which followed the Prague Spring of 1968.

The communist regime, from the period of normalisation to the velvet revolution of 1989 was perceived as 'an

unpleasant influence on one's existence' as opposed to the punitive repressive regime of the earlier period of communist control.

Thus over the period it is indeed true that the punitive sanctions were lessened considerably. However, there was a price to pay in moral and psychological, terms - and that price was political and moral acquiescence to a repressive, undemocratic regime, that had no respect for human rights.

ECONOMIC REALITIES

For the population of Czechoslovakia, much of their everyday life was dominated by the realities of coping with an economic system, that failed to provide the goods required by the market. In their capacity as consumers - and as employees, involved in the supply side of the economy - they were faced with the perennial problem of surviving in a system where goods were not available in the quality or quantity required. The integration of a social and political agenda into the operation of the economy at a micro and macro level was at the core of the inefficiencies of the system.

How did these problems manifest themselves in the everyday life of citizens? As consumers, they were faced with constant shortages of all goods and services, especially consumer goods. When such goods were available in limited

quantities, it gave rise to the perennial system of queuing in order to purchase the items required.

More insidiously, the shortages of goods spawned a black market which ultimately pervaded all aspects of economic activity. This activity went far beyond the caricature of a shady individual wishing to trade currency, jeans, cigarettes or any other popular consumer goods that were in demand and also in short supply - although such people were in evidence, especially in the Musek district of Prague.

Much black market activity was based upon long term interpersonal relationships of trust and mutual exchange of goods and services. The Black Market became an extensive informal social network, in which the majority of Czechoslovakian citizens participated.

It was not uncommon for local traders to advise some of their regular customers of the impending arrival of goods which were in short supply and offer to put some aside for them. One interviewee quoted the example of the local butcher who would keep the best cuts of meat for him under the counter. Another individual explained how he obtained a Skoda car because he had attended school with the local Communist Party official in charge of the allocation of new cars. Payment on such occasions would be either monetary, at a black market price significantly in excess of the

state controlled price, or a barter of goods or services, whichever was mutually acceptable.

The shortage situation also significantly affected the nature of power relationships within the community. If one had access to a scarce commodity, then one had power in the negotiating situation. In its most extreme negative form, it opened up the possibilities of threat of blackmail for both buyers and sellers in the black market situation: as the process implicated both parties in breaking the law.

The shortage situation also bred self-sufficiency and bartering activity within the community. If one succeeded in purchasing a car, it would be expected to last for ten to fifteen years. Due to the shortages of spare parts and the lack of service facilities, it was either necessary to maintain one's own car, or enter into some kind of barter arrangement with someone who could. Additionally, if a car was sent to the garage for repair, it frequently came back minus certain parts such as windscreen wipers or other parts, which had been removed. The general shortages of most goods was parallelled by a wider shortage of services.

> There was no point in having a fancy washing machine or television. Even if you were lucky enough to get the spare parts, you could never find anyone to repair them when they went wrong.
> (Female colleague, Bratislava, November 1992)

Such shortages extended to professional services such as lawyers. This situation arose from the communist belief that direct production of goods was the primary means by which wealth was created. Support services were seen as a secondary economic consideration - a parasitic spin-off from main stream economic activity, producing nothing of tangible value to the state. This view was reflected in the comparatively low financial rewards and status which service activities attracted. Consequently, relatively few people pursued careers in service sector.

The perennial shortage of consumer goods and services is immediately apparent, when entering the home of a Czechoslovakian citizen. It is akin to walking into a time warp, where one is transported back to the early 1950s as regards the decor, the quality of the gas and electric power facilities, the age and condition of the furniture. Again there is a distinct absence of modern labour saving devices. Any improvements within the home tend to be of a crude home-made nature with poorly constructed shelf-fittings, rooms divided into two by means of a curtain and large ceramic and metal bathroom and kitchen fittings. The quality of the more modern consumer durable purchases - mostly East European in origin - is very poor and the style is dated.

The problems of quality and availability extended beyond consumer goods to that of housing. However, as with all

goods and services, availability was a function of power supplemented by money. In the communist system:
'Money was the handmaiden of power not its mistress' (Professor Peter Lawrence, Buckinghamshire College, May 1993).

In several towns, usually located on the hills above them are blocks of flats, which stand out from the other residential buildings around them. They look to be very well appointed and maintained, with facades resembling that of modern western hotels. These would be the accommodation for the local influential Communist Party members. Alternatively, they would inhabit stone built villas in a rather dated 1960s style. Some Communist Party members inhabited older style, more traditional homes - probably seized from alleged opponents of the regime, in the early days of the communist takeover.

In stark contrast, are the extensive housing estates on the perimeters of the towns which seem to extend endlessly to the horizon. They are the small, cramped, square high flats constructed in the 1960s and 1970s. Interspersed with those flats one finds the Lenin style of Russian residential accommodation. These constructions are large buildings, some fifteen to twenty stories high, punctuated by large archways. Through the arches, one can see the blocks of flats built onto the front facades to form an L shape.

The cramped conditions of these flats are exacerbated by the housing shortage, as a result of which several generations of a family frequently lived in the same house. The overcrowded accommodation provided no real living space beyond that available for eating and sleeping.

The concept of housing co-operatives was developed by the state as a means of trying to the alleviate the housing situation and reinforce the political doctrine of shared and communal ownership. Under this system, a group of employees, usually from the same organisation, worked together themselves to built the block of flats, which they then occupied.

Some people were fortunate enough to have been able to remain in their family homes after the communist takeover. However, frequently, the original owners of the houses were only permitted to retain several rooms for their own use, the remainder being let out as flats by the state. Such homes usually reflected the style and decor of several generations of occupants. The major housing complexes are built out of the centre of the towns, usually with only one shop in the complex, or frequently with none.

This situation added to the problems faced by women trying to fulfil their domestic roles. They were required to travel the distance to work and typically by public transport. Then at the end of the day they had to queue

for shopping, come home to prepare a meal and carry out the domestic chores.

THE ROLE OF WOMEN

Whilst these were universal problems faced by most women, certain aspects of the system impacted differently on different groups of women.

Discussions with several professional female colleagues highlighted some of their special difficulties when seeking suitable marriage partners. Most professions, especially teaching, and to a lesser extent medicine, attracted large numbers of females. This single sex concentration greatly restricted their opportunities to meet potential partners in the workplace. As there was very little social interaction beyond that of family and a few close friends, there was little opportunity to meet with members of the opposite sex in a social situation. This led to a relatively high concentration of marriageable but unmarried women in certain professions.

At the other end of the spectrum, women in potentially marginalised or disadvantaged situations were supported by the system. A single mother with young children would be guaranteed a home, a job, crêche facilities and all the basic necessities of life. This is an example of the social dimension of communism, which very effectively

provided a significant degree of material support for those on the lower thresholds of the social and economic order.

For all women however, life under communism was a very hard struggle, exacerbated by the absence of labour saving amenities, and the chauvinistic attitude adopted by men inside the home - irrespective of the formal political party doctrine regarding equality.

EMPLOYEE RESPONSES

Czechoslovakians also suffered from the failure of the economic system,as employees. The majority of people were employed in the large state-owned organisations, which spawned immense unwieldy structures that were both inefficient and ineffective. Organisations also suffered from the inherent weaknesses of most nationalised industries: lack of accountability, responsibility, monitoring and control.

These weaknesses were re-enforced by the fact that all authority and power of decision-making lay with the various Communist Party organs within the enterprise, which effectively controlled the operation of the organisation. In keeping with the concept of central planning, each organisation was given the target output level it was required to fulfil, together with a series of political and social objectives.

What did this mean for the average employee in such an organisation? From the perspective of job design and work practices, there were shortages of machines capable of carrying out the jobs they were meant to do. This was partly a function of the absence of resources to undertake investment programmes. It was also influenced by the political and social objectives of the government to maintain full employment by adding labour - instead of capital equipment - as additional inputs to the production process. Thus, the organisations were severely overmanned.

As regards motivation and productivity within the workplace:

'It was an Eden for lazy and stupid people. Everyone had to be average: so we were always brought down to the lowest level' (senior manager in newly privatised enterprise (February 1992)).

It is easy to understand why people were lazy and de-motivated in this system. Promotion and additional benefits were linked to political criteria rather than job performance. There was little incentive to work hard for promotion.

Moreover, it was extremely difficult to dismiss an employee from the organisation. If someone was fired, the state agency sent a replacement, whom the company was obliged to employ. This led to the creation of a residual pool of

virtually unemployable people who moved from company to company. Thus, there was a likelihood that a dismissed employee would be replaced by someone even less able. Consequently, the 'better the devil you know' syndrome tended to operate. Employment strategies were also influenced by the fact that the chief of the company received additional bonuses in relation to the number of people employed, irrespective of their ability to do the job.

It could be argued that the effectiveness of an organisation could be evaluated against the targets set by the central planning authorities. Moreover, the process of target setting could be seen as a method of monitoring performance within the organisation. However, given the severe shortages and inefficiencies in the system, the means by which the plans were achieved, were a testimony to the ingenuity of the managers and individuals employed in the company in terms, not of their effectiveness in using the system, but in terms of their ability to operate around it effectively.

At the steel company in the large industrial town of Ostrava for instance the output of nails was specified as five hundred tonnes within the plan. The employees produced the requisite quantity of extremely large nails to the required weight. Such nails were quicker and easier to produce than smaller nails and so the target was achieved.

But the real outcome of the situation was, firstly, that the company had warehouses full of large nails that no-one wanted and secondly, there was a shortage of small nails in the Republic. Many organisations could provide similar tales of how the plan was 'fulfilled'.

If the plan was not going to be fulfilled for some reason, managers frequently contacted colleagues at other points in the value chain and requested that they put through dummy invoices so that the plan was achieved on paper.

Thus the informal networks of the black market were mirrored in the operation of organisations, when trying to fulfil their plan.

In terms of the financial rewards for employees, on the one hand, there is the view that:
'we all have the same size stomachs with the same food requirements, so we should all earn the same wages'.
The alternative view states that:
'they pretended to pay us and we pretended to work'

The latter quote reinforces the view that many people did not ideologically buy into the system. They used it to achieve their own ends in so far as they could. This is especially true of the second generation of communists who came to maturity after the normalisation, which followed the Prague Spring of 1968.

A self-confessed communist who belonged to such a group explained to the author the rationale behind his decision to join the Party. Before 1948 his father owned many businesses. After the communist takeover in 1948, his father suffered the same fate as many other private businessmen: the confiscation of his property and deportation to the mines of Ostrava. The son decided that he wanted a better material life than that of his father and was prepared to use whatever means necessary to achieve it. The only route to advancement was to become a member of the Communist Party, which he did. Even with the benefit of hindsight, this interlocutor expressed no regrets for his actions and indeed would do exactly the same thing again. This story typifies a whole generation who manipulated the system as opposed to internalising its values.

As regards remuneration, the payment levels across the board showed only minimal differentials between jobs, irrespective of their complexity or the degree of responsibility that went with them. As one would expect there was a great reluctance to make any effort at work: as it was not rewarded, either in monetary terms or in promotional opportunities.

As an incentive to encourage greater productivity, an additional bonus element was included in the wages of those employees whose organisations fulfilled their plan. In

fact all organisations 'fulfilled' the plan. However, fulfilment was achieved by means of a paper exercise or a distortion of the plan in order to meet the needs of individuals as opposed to those of the state. This created the interesting paradox whereby employees were rewarded for their ingenuity in defeating the system, as opposed to their support and commitment to its success.

However, the social agenda of the organisation did offer some tangible benefits to the employees. The employing organisation typically provided basic medical and dental care for employees. Although, it was commented that the quality of the doctors and dentists was poor to say the least, and the most effective drugs were available only on the black market, at extremely high prices. The enterprise also provided apprentice training schools. In this situation, however, it was frequently noted that the training was primarily about political indoctrination rather than technical competence. The company also provided housing for some employees at very low rents. There was, however, no provision for maintenance of the properties, many of which remained in the same condition they were in when the communist regime took them over. The existence of crêches within the workplace and the perceived equality of women could be regarded as a benefit provided by the state and the enterprise. The reality was, however, that women were not given positions of equal status with men in management positions within the workplace.

Moreover, as previously stated, perceived political and economic equality was not matched by social equality within the home. Thus, it could be argued that communism added to the discriminatory female burden - as opposed to promoting true equality.

The employing organisation also provided hotels, where employees were permitted to take holidays at reduced prices. For the majority of people, however, holidays and weekends were spent at their dachas. In fact, for most people, their main efforts were not concentrated in the workplace but in the maintenance of their dachas and gardens in the country. It is said that people worked so hard in their dachas at the weekend, they came back to work for a rest.

Thus the economic reality of everyday life for people was a combination of suffering under the shortages of the regime and of devising ways of operating around it and in spite of it, to the further detriment of its effectiveness.

At a deeper, and more insidious level, it led to the internalisation of a set of values founded upon deceit: deviant behaviour and living a double life - within a regime to which one paid lip service. Over time, this behaviour led even to an insidious moral malaise, resulting in passive acceptance of, and collusion with a politically and morally repressive regime.

SOCIAL ACTIVITIES

Beyond the work environment, the pattern of social life for most people was very limited. Media entertainment - in terms of cinema and television - was severely censored, so that most programmes were 'in Russian and very boring' (student of the University of Economics, Prague, October 1992).

There were some closed showings of films, not generally available to the public, on subjects of intellectual interest and debate. The audiences comprised groups of professionals and intellectuals, who supported the regime, together with influential members of the Communist Party.

The same restrictions were placed on access to literature. Only state approved literature was available for the majority of the people. Libraries did retain stocks of certain prohibited texts. These, again, were accessible only to restricted and privileged groups within the community.

However, dissident groups produced underground newspapers, and the institution of the samizdat was born and flourished throughout the regime. The samizdat were original papers, or sections of prohibited writings, which dissidents copied and circulated amongst themselves in defiance of the regime.

Social gatherings were usually restricted to one's family or a few close, longstanding acquaintances, whom it was hoped one could trust.

A great deal of leisure time for most people was spent at their dachas in the country, partly because, as suggested earlier, it represented a social and moral escape from the drudgery of everyday existence. The small cramped flats restricted freedom and movement and space, especially for children. Moreover, the severe restrictions on foreign travel, which will be discussed below, made it extremely difficult to arrange holiday travel abroad.

TRAVEL

It was possible to travel unhindered within Czechoslovakia to visit friends and relatives or one's dacha, using either public or private transport. However, the condition of the roads was very poor. Amenities, in respect of travel facilities and petrol stations, were few, and basic in their provision to say the least.

For those wishing to visit other parts of the country on speculative travel, there was very little available by way of residential accommodation. The available choices were the company residential hotels, or the spas. The residential hotels still represented an institutional

setting, where the restrictions of the regime on one's behaviour and freedom of expression were still prevalent. The spas were provided, primarily, for those with illnesses or those who were recuperating from illness.

As regards foreign travel, Czechoslovakia was one of the most closed regimes of Eastern Europe, in terms of access to the West. Foreign travel was strictly controlled and: 'They made it as difficult as possible to obtain visas and currency to travel abroad, in order to discourage people from doing it' (professional colleague, Ostrava, April 1993).

If one did wish to arrange a private trip abroad, as well as obtaining the series of reports previously outlined it was necessary to follow a protracted process of queuing and form filling. It was quite common for people to queue all night outside embassies to obtain a visa.

One individual interviewed in the course of the research described the despair of travelling overnight to Prague, and arriving at the embassy at five a.m. to find a queue several miles long. The usual practice was for the gates to be opened. Then, only as many people as could fit in the grounds were given forms or visas on that day.

Travel abroad required a minimum of four such trips to obtain visas, then additional queues to obtain currency.

All trips had to be undertaken personally, that is by the person wishing to travel abroad. People reckoned that it took at least two years of planning to arrange a trip abroad. Even then, at the last minute, permission to travel could be withdrawn.

Travel abroad continued to be undertaken mainly for diplomatic or business purposes. Business travel, for a significant number of people, involved travelling to the third world, as advisers, in various industrial, commercial and military capacities. It was somewhat incongruous during the course of the research project to speak to a Czechoslovakian citizen who had learned English in India, complete with accent!

As a sidelight on the foreign travel issue, the main reason for which one lecturer interviewed in the course of this study was permitted to travel to conferences abroad was to arrange invitations to the various countries for his Dean and one of the Dean's numerous lady friends!

THE ENVIRONMENT

The realities of the environmental cost of the failed communist experiment are everywhere apparent. The acid rain and pollution has rotted buildings. There are forests

full of dead trees with stripped white barks, a chilling testimony to the death of their habitat.

In the once rich farmlands, previously known as the Golden Fields of Bohemia, overfertilized soil polluted by the heavy metals of cheap fertiliser lie fallow, or produce bitter tasting poor quality crops. There is contamination of dairy products. The water from the taps in some areas of the country is opaque, as a result of the pollutants in the atmosphere and the soil.

The skyline of Ostrava, with its mines and steel plants, is a vivid representation of Blakes's dark satanic mills resurrected, pumping yet more lethal unprocessed chemicals into the environment.

Both the domestic and industrial burning of brown coal and sludge pollutes the atmosphere even more. It is a common sight to see and taste the thick brown smoke that streams from the chimneys of the older properties in the region.

For those working in and living near the chemical plant in the centre of Bratislava, pumping its poisonous fumes into the air, there was no alternative but to purchase meat and fruit from shops, where the fresh uncovered produce had been exposed to these poisons.

The cost is high in terms of infant mortality, a rising male mortality rate and a crop of cancer and respiratory illnesses which seem endemic to that part of the world.

It could be argued that the diet and lifestyle of the average Czech citizen does little to help the situation. A fatty diet, high alcohol and cigarette consumption, together with lack of exercise, does nothing to improve the health of the nation. These, however, are probably best seen as the new opiates of the masses, to ease the problems of living in a system, which promised to rid them from the need for such placebos.

The lack of sporting and recreational facilities was also a contributory factor to this unhealthy lifestyle.

The liturgy of weaknesses in the communist system and their negative impact on the lifestyle and behaviour of ordinary citizens is long and bleak.

THE BENEFITS?

In fairness to the process of evaluation one must pose the question: Was it all so bad? Was their nothing in the old system, which had a positive impact on peoples lives?

There was perhaps 'the comfort factor'. It was, after all, possible to live in a regime, where a job, an income and a home were more or less guaranteed. For most people, if

they had very little, then so did most others. It must have become seductively easy for people to live in a system where all decisions were taken on their behalf, by the state.

There was no agonizing over problems, responsibilities and difficult decisions. The state also provided a secure, relatively crime-free environment - unless the crimes were perceived to be against the state.

Some would argue that the régime provided more than comfort. State policies on housing, employment, medical care and crêche provision offered a higher minimum material standard of living for potentially disadvantaged groups than that offered by democratic societies. But at what moral cost?

The price was to adopt a passive apolitical stance, keep your head down, and be concerned only with your own living standards and immediate family.

So what of the new order? Is the loss of this comfort factor and additional state support too large a price to pay for freedom and democracy? Is the transition to the market economy too painful - politically, socially and economically?

The events, which have taken place since 1989 would suggest that the answer from the Czech Republic is a resounding 'no'. From Slovakia, however, the answer might appear to be a qualified 'yes.'

The analysis of events, which led to this divergence of views, and the ultimate separation of the two republics, was discussed in the previous chapter dealing with the nationalist question.

Yet, as the discussions of the post 1989 period in subsequent chapters will show, the euphoria of the Velvet Revolution has been supplanted by the inevitable letdown of reality.

To quote Havel:
'After every great party there is always a hangover'

CHAPTER 9

PRIVATISATION

> 'You can make a fish stew out of an aquarium, but you cannot make an aquarium out of a fish stew'
>
> (old Czech proverb).

INTRODUCTION

As the monumental nature of the transition process in general, and privatisation in particular, unfolds in Central and Eastern Europe, the above proverb seems to be gaining increasing credence. History has shown that it is possible to transfer the ownership of enterprises from private to state control. Is it possible, however, to take these obsolete, state owned legacies of communism, and privatise and restructure them in such a way as to make them viable entities in a free market economy?

In order to explore the feasibility of this proposition, this chapter seeks to clarify the concept of privatisation in the context of the Czech Republic, and, subsequently, attempts to evaluate its progress along the transition route from a command to a market economy. The later chapter on organisational transformation will consider the privatisation process from the perspective of individual enterprises.

Concepts and definitions

The most common post war usage of the term privatisation in the context of political economy is that defined by Brabant (1993, p.125) as:

'... the transfer from the public to the private sector of entitlements to residual profits from operating an enterprise'.

This notion of privatisation, together with the associated concepts of private property and ownership rights, is relatively clearly defined within the context of established free market economies.

In the post communist countries of Central and Eastern Europe, however, such notions are alien to the psyche of several generations of citizens, whose understanding of these concepts has been distorted by the experience of communism. Moreover, where governments are addressing the issues of privatisation, they are seeking to use the process to achieve multiple objectives, which are both political and social as well as economic in nature. Attempts to fulfil these complex and sometimes conflicting aims are complicating an already difficult exercise even more (De la Hesa, 1991, p.23).

In the context of Eastern Europe, privatisation has become such a pervasive concept that Thomas (1993, p.169) comments:

'Privatisation in the post communist societies is a term that begs definition'.

However, given that the notion of privatisation is implicitly understood in some form as being integral to the transition process, a more broadly applicable definition has been formulated by Brabant (1993, p.125) as:

> an umbrella term for a variety of different policies that are loosely linked by the way in which they are taken to mean the strengthening of the market at the expense of the state.

Despite the complexity surrounding privatisation, it is generally accepted that privatisation is a necessary precondition for the successful transition to a market economy.

PRIVATISATION IN THE CZECH REPUBLIC

In seeking to unravel the privatisation process as it relates to organisational transformation in the Czech Republic, the following questions will be considered. Of the various forms of privatisation available, which types have been chosen and why? What is the long term role of the government likely to be? How effective are the legal

frameworks and bureaucratic institutions the government has put in place to implement the process? How successful have the initial stages of privatisation proved to be in relation to organisational transformation and what is the likely way forward?

Privatisation in The Czech Republic is at the core of the political, economic and social changes now taking place within the country. Politically, the dispersion of ownership, with the power and influence that accompanies it, is seen as a means of securing the fledgling political pluralism now developing in that region. In economic terms, the basic operation of the market forces is fundamentally dependent upon the private ownership of property which owners are free to exchange at will.

At a social level the redistribution of property and its concomitant inequalities of income and wealth undoubtedly redefine and re-shape the social stratification of the society. In pursuit of these objectives, a range of privatisation strategies is available to the government.

FORMS OF PRIVATISATION

Of the various forms of privatisation, Benner (1993, p.338) identifies five main types.

The voucher scheme consists of transferring state property to private ownership by the mass distribution of shares to all eligible citizens.

The sale scheme involves the direct sale of property to private individuals

The financial intermediaries scheme involves the distribution of shares to financial intermediaries, e.g. mutual funds, who then distribute the shares to citizens.

Joint Venture or foreign ownership schemes entail the selling of a significant share of state owned enterprises to foreign investors.

Employee ownership schemes are concerned with the direct transfer of shares in state firms to their employees.

The Czech government has adopted the voucher privatisation as the prime method of privatisation, although direct sales and joint ventures as alterative means of transferring ownership are also used. The rationale behind the voucher privatisation is based upon the extent to which it meets the main objectives of privatisation, as perceived by the government in the Czech Republic. The potential for mass ownership of property promotes the potential

irreversibility of the process in political terms. It is, also, seen as socially equitable due to the selected criteria for the distribution of vouchers. Economically, it reintroduces the concept of private ownership of property fundamental to the operation of the free market mechanisms.

Due to the shortage of investment in Eastern Europe, the Czech Republic, in common with other Central European countries, is seeking joint ventures with foreign partners, in order to acquire much needed capital, technology and expertise to revitalise their dilapidated enterprises.

Thus, in terms of the choice of privatisation mode, Parker (1993, p.40) notes that:

> In practice, it probably makes sense to employ a mixture of methods, and top design programmes in such a way that they attract foreign capital as well as mobilise resources.

PRIVATISATION LEGISLATION

The legislative and institutional framework of the privatisation process in the Czech Republic comprises three main areas.

Restitution

The policy of restitution contains a wide-ranging reprivatization measures, under which citizens,whose property was confiscated by the Czechoslovak state under the communist regime, could claim it back.

The relevant basic rule of law is contained in The Minor Restitution Act, The Large-scale Restitution Act, The Land Act and The Co-operative Transformation Act.

Small-scale privatisation

The small-scale privatisation governs the lease and sale of state-owned shops, restaurants, hotels, workshops and similar establishments at public auctions to individuals or private firms. The provisions of the small-scale privatisation are contained in The Small-scale Privatisation Act of 25th October 1990.

Large Scale Privatisation

The Large Scale Privatisation Act concerns the privatisation of state-owned enterprises on the basis of a 'privatisation project', which outlines the proposed mode of privatisation for enterprises together with recommendations for strategic plans and restructuring.

The large privatisation legislation outlines:

the bureaucratic structure for the regulation of the privatisation process

the process by which state owned enterprises become privatised firms

the voucher privatisation scheme by which ownership is transferred to citizens

RESTITUTION

The Czech Republic has undertaken the largest reprivatization programme of any former East European country outside of the former GDR (East Germany). A very high priority has been given by the government to this controversial programme, which has proved to be both costly and time-consuming. It is generally believed that the time taken to process the large number of requests for the return of private property has extended the period of uncertainty concerning ownership of assets, thus discouraging potential investors and disrupting production.

The legislation makes provision for compensation to those who lost their jobs, or were denied the opportunity to finish their education, when the communists seized power in 1948. It also extends compensation to those who were

imprisoned by the former regimes, forced to work in labour camps or serve in special military units.

Where possible, the government seeks to provide restitution in kind by the return of the original assets seized. If this is not possible, financial restitution is made. In this situation, former owners receive up to a maximum payment of kcs 30,000 in cash, and the remainder in shares in the investment Money Market Privatisation Fund. This Fund is managed by institutions appointed by the National Property Fund, whose role will be discussed below. The Fund invests in privatised enterprises using vouchers, which comprises 3% of the value of each organisation privatised under the provisions of the large privatisation legislation. All such privatising organisations are required to transfer 3% of the value of their enterprise into the National Property Fund for this purpose.

THE SMALL PRIVATISATION

The small privatisation programme is perceived by government to be a fast and effective means of creating a thriving private sector in the small to medium sized firms within the Czech Republic. Historically, compared to other socialist countries, this sector has experienced an extraordinarily high concentration of state ownership. The arrangements for the small privatisation have been organised on a regional basis by local privatisation boards under the direction of the Ministry of Privatisation. Any

individual can propose a scheme for privatisation, as long as it is not part of a large privatisation project, or subject to a restitution claim. Additionally, if the privatisation claim involved selling off part of a larger enterprise, the management of that enterprise could block the sale by claiming that the loss of that unit would threaten the activity of the parent enterprise (Frydman et al. 1993, p.77-78).

The small privatisation has been implemented primarily by auction, with the successful bidder being required to pay the monies due within thirty days. In the initial rounds of auction, the new owner mainly leased the property from the state or municipal authority for a period of two to five years. In subsequent rounds, this was extended to encourage owners to invest, and led also to higher prices being paid for the properties in question. Eligibility for participation in the initial auctions was restricted to Czechoslovak citizens, but was subsequently extended to include foreigners.

The funds generated by the small privatisation auctions were deposited with the National Property Fund, where they were frozen for a period of two years. Their function is to serve as deposits in the banking system and, as such, are not available for use for budgetary purposes.

The numbers suggest that the small privatisation process

was successful. Parker (1993, p.395), however, comments that there has been suspicion of collusion amongst those bidding, in order to keep prices down. Moreover, it is believed that many foreign bidders purchased property through the use of domestic intermediaries in the initial auction phases. Finally, those with the funds to purchase the properties appear to have been the nomenklatura of the old regime, who used their position of power in the Communist Party to acquire and secrete away hidden wealth.

Whilst there is little doubt that the small privatisation successfully disseminated ownership of private property into the hands of the community, the chapter on Organisational Emergence will illustrate the problems and difficulties experienced by the new owners, as they attempt to transform their newly acquired properties into profitable businesses (Mills et al. 1994, p.4).

THE LARGE PRIVATISATION

The large privatisation in the Czech Republic is at the heart of the government macro and micro policies of transition. The methods by which the Czech government has undertaken the privatisation of the majority of its industries, together with the massive transfer of company ownership from the state to the private sector, is unique and unprecedented in terms of its speed and scope. The strategy has been criticised as moving too quickly, on the

grounds that there should be appropriate social and institutional support already in existence before privatisation can be achieved. The Czech strategy, however, has been to forge ahead, and change the ownership structure as quickly as possible, with restructuring being left to the new private owners. Additionally, the government has chosen to develop new legal frameworks and institutions only when the need becomes pressing (Sacks, 1994).

This strategy is supported by the argument that, if the traditional western approach to privatisation is undertaken, it would take fifty years to complete the process. In 1990, the former Czechoslovakia set the ambitious target of privatising more than 4,000 organisations in three years. The number actually purchased was nearer 2,000.

The fact that this is a totally novel situation, with no comparable precedents, makes it difficult to evaluate the validity of either argument, i.e. whether the transition period should be fast or slow. However, this debate in relation to the speed and mode of implementation of privatisation will be developed further, when the role of the government as a stakeholder is considered later in the chapter.

STATE PRIVATISATION INSTITUTIONS

The Czech government has adopted a centralised regulated approach to privatisation and has established a new set of bureaucratic institutions to manage it. These comprise the Ministry of Privatisation and the National Property Fund respectively.

The Ministry of Privatisation

The Ministry of Privatisation is the most powerful institution in the privatisation process with overall responsibility for implementation. It initiates requests for the submission of privatisation projects from any interested parties. The founding ministry, i.e. the ministry to which the enterprise reported under the old regime, plays an intermediate role by reviewing all the privatisation projects submitted in relation to the relevant enterprises. The founding ministry will pass them onto the Ministry of Privatisation together with their recommendations as to which one should be accepted.

The Privatisation Ministry is extremely influential to the extent that it selects the enterprises which will be privatised in each wave, and the exact method of privatisation to be adopted.

In the small privatisation process, the ministry appoints twenty-five local privatisation commissions for each of the seventy-five local districts. It also gives the final approval for those enterprises which have to be auctioned off under the small privatisation legislation.

The Privatisation Ministry also plays a central role in the restitution process. It decides on the validity of restitution claims, and the level of compensation to be awarded, on the basis of the valuation of the property. The ministry is also responsible for resolving restitution claims in the context of the large privatisation projects.

The National Property Fund

Once a privatisation project has been agreed, the enterprise changes its form from that of a state owned enterprise to a private enterprise, in the form of a joint stock company as defined in the Commercial Code. Interim ownership of the enterprise is transferred from the state to The National Property Fund.

The aim of the Fund is to privatise all enterprises under their control by 1996. In the interim period, The National Property Fund undertakes the legally defined roles of owners and shareholders respectively, in those enterprises for which they have control.

In its capacity as shareholder the Fund undertakes the main shareholder duties, i.e. appointing the Supervisory Board and the Board of Directors. The Fund is also ultimately responsible for organising and managing the sale of the enterprise by whatever means have been specified in the privatisation project.

However, insofar as the funds are directly supervised by the privatisation ministries and a presidium of members elected by the parliament, they are effectively controlled by the government. The presidiums appoint a ten member executive of Fund employees, which carries out the work of the Fund itself within the framework of the guidelines laid down. The government oversees the activities of the Fund by the appointment of five member supervisory boards elected by parliament. All Fund members hold their posts for a period of five years (Frydman et al. 1993, p.73-75).

PROCESS OF PRIVATISING STATE OWNED COMPANIES

Micro privatisation

The legislation on 'large privatisation' established in 1991 is considered to be the most far reaching and all-encompassing privatisation programme of all the Central and East European Countries.

From the organisations perspective, the crucial document in this process is the proposal for privatisation, or the privatisation project. This is the document upon which the ministry of privatisation will decide the future ownership and structure of the company. Although the existing management of an enterprise usually submits a 'basic project', any other interested party can submit privatisation projects, referred to as 'competing projects'. There is no limit to the number of privatisation projects which can be submitted for a single enterprise, and the same group of interested parties can submit multiple bids. The milk processing factory in Brno, for example,received the one hundred and twenty-six competing bids, in fact the highest number to date.

Macro privatisation

The main methods of ownership transfer under the large privatisation scheme comprise direct property sales to domestic or foreign buyers, and the transfer of property ownership to the public through the voucher privatisation scheme.

Under the voucher privatisation scheme, property is transferred from state to private ownership in two separate waves. The procedure for the various stages in each wave of privatisation is as follows:

Registration by those eligible citizens who wish to participate in the first wave of privatisation.

Assignment of vouchers by those citizens who wish the investment funds to act on their behalf.

Commencement of a series of privatisation rounds during which participants exchanges vouchers by bidding for shares in privatised enterprises.

Distribution of shares to new equity owners.

The first wave of privatisation began in February 1992 and ended in July 1993. During this wave of privatisation 200 billion crowns worth of shares in enterprises were distributed. Preparation for the second wave of privatisation began in October 1993. The value of the shares available for privatisation in the second wave was only 50 billion crowns (Hawker, 1993a, p.7).

In terms of its application, the voucher method operates from both the supply and demand sides of the economy. On the supply side, the government, through the Ministry of Privatisation, decides on those firms to be privatised, wholly or partly, by means of vouchers.

On the demand side, the voucher scheme operates as follows:

> At a designated time, each resident Czech citizen, who is eighteen years or over in October 1992, can purchase a voucher booklet at a cost of Kcs 35, and register it for Kcs 1,000. The voucher is divided into 1,000 points which individuals can either invest directly in organisations of their choice, or through intermediaries, i.e. investment funds. The role of investment funds will be outlined in the section on financial intermediaries.

Shares are allocated on the basis of 'discretement tatonnement' (over sequential link periods).

In the first round of the voucher privatisation all shares are valued at the same price in terms of voucher points.

The calculation formula adopted for this process is:

$$\frac{\text{total book value}}{\text{total number of points}}$$

with three shares equal to one hundred points. Thus, the number of shares held by each organisation is proportional to its value.

If demand for the shares in each round of privatisation is less than 25% greater than the available supply, demand is

considered to be satisfied. In this instance, individuals have priority over intermediaries in the allocation of shares. If the available supply of shares in a company is greater than the demand, the excess shares in the enterprise are carried forward, and sold at a lower price in the next round of bidding.

Thus, the process of share price adjustment in subsequent rounds is dependent, primarily, on the results of the previous round. In theoretical economic terms the objective is to set a share price at which demand equals supply. At this time, all shares available under the voucher scheme will have been allocated to the Czech citizens, thus ensuring that the desired level of transfer of property ownership from the state to private citizens. In the first wave of privatisation 97% of shares were successfully allocated by this means (Frydman et al. (1993, p.85).

THE ROLE OF INTERMEDIARIES

One of the most unusual and striking features of the voucher privatisation process has been the emergence of investment privatisation funds, and the investment companies which manage them.

Indeed, so pervasive is their role in the voucher privatisation process, it has been suggested that these

intermediaries are responsible for its success. Indeed, such has been the outcome of the privatisation, that the investment funds are set to play a crucial role in the future ownership pattern of companies (Brom & Orenstein, 1994, p.14).

The investment funds are defined as joint-stock companies, which are established by a founder, the investment company. The role of the funds is to collect independent citizens vouchers, and invest them in the mass privatisation scheme, by creating a portfolio of shares in the privatised enterprises. The fund then issues fund shares to the voucher holders they represent. The influential ministry of privatisation regulates their activities by setting out guidelines to the founding investment companies, and issuing licences to funds.

In order to obtain a licence the fund must be established as a joint-stock company with a start-up capital of 100,000 crowns. It is also required to appoint a founder, i.e., investment company to manage the fund. The investment company must have fixed assets of at least 1 million crowns.

In order to ensure diversity of investment fund share portfolios, two parliamentary amendments were introduced in 1992. These changes preclude a fund from owning more than 20% of any one company or form investing more than 10% of

its own capital in any one company. Additionally, a group of funds managed by the same investment company cannot collectively own more than 40% of any one company. These provisions were subsequently amended so that currently a group of investment funds cannot own more than 20%. The final amendment stated that investment funds are no longer required to have investment companies as managers but, could now manage themselves.

The investment funds have been set up by private individuals, companies and banks. The banks, notably the Czech Savings Bank, were especially active in establishing intermediaries, as they were in a position to employ their network of information and facilities to attract potential investors. Foreigners were also permitted to establish investment funds, with the Austrian Creditanstalt as one of the largest intermediaries. By the commencement of the first wave of privatisation, four hundred and twenty-nine investment funds had been registered (Matesova, 1994, p.14).

When the voucher scheme was launched by the ministry of finance,it was anticipated that 4 million of the 8.5 million eligible citizens would participate. However, due to the introduction of investment funds, the uptake proved to be significantly higher. The first fund to be established was the Harvard Fund, which launched an advertising campaign, promising a guaranteed ten fold

return on the value of shares within twelve months. Other investment funds were started, which made even more spectacular claims than the Harvard Fund. The outcome of the first round of voucher privatisation was, that of the 8.5 billion investment points represented by the vouchers, 6.1 billion were invested by the investment companies. The extensive concentration of share ownership in the hands of a small number of these investment funds, as shown in Appendix I, has set the stage for them to play a major role in the management of those enterprises in which they have major shareholdings. Additionally, as the investment funds and the investment companies which manage them are owned primarily by the banks, they too are likely to have an integral role to play also in the ownership and control of these privatised companies.

EVALUATION OF THE PRIVATISATION PROCESS

Any attempt at evaluating the effectiveness of the privatisation process within the Czech Republic at this point in time (Autumn 1994) must be at best a tentative exercise. Privatisation is very much still in the early stages of its implementation. The short time span of its implementation, i.e. only a three year period, limits the available evidence from which one can attempt to make feasible predictions and draw meaningful conclusions.

Moreover, as privatisation is an ongoing process which is

constantly being modified by policy makers in the light of their experience, the establishment of a discrete time frame within which to carry out an evaluation can lead to some distortion in the interpretation of events as they unfold within a constantly changing context.

Finally, and possibly most importantly, the whole transition process has introduced new sets of institutions, interest and pressure groups with their own objectives, agendas and power bases. Such groups frequently have differing and often conflicting views on the underlying rationale and objectives as well as the implementation strategy in relation to privatisation.

Thus given this divergence of perspectives, a meaningful evaluation of the effectiveness of privatisation against a universal set of criteria is inappropriate, clearly these various groups have formulated their own subjective sets of criteria against which to evaluate the privatisation process. Moreover, objectivity in relation to the evaluation exercise is severely limited by the inherently subjective ideological basis upon which any system of private ownership and property rights is based.

As privatisation will be very much influenced by the motivation and interrelationships of the main interest groups a stakeholder analysis of these key players will be applied in order to evaluate the privatisation process

against their respective objectives

MAIN STAKEHOLDERS

The main stakeholders identified as having a key role in the privatisation process comprise:

THE GOVERNMENT which is seeking to redefine its role in the new political order in order to develop and implement the privatisation programme effectively.

THE BANKING SYSTEM which is required to undergo revolutionary changes in terms of its role within the economy. It has now become a main instrument of government economic policy at macro level and a major influence on the financial affairs of individual enterprises at micro level.

THE FINANCIAL INTERMEDIARIES whose development is vital to the effective functioning of the market economy in terms of the mobilisation of capital for lending, investment and consumption purposes together with establishment of the financial institutions required to facilitate this process. In this context THE INVESTMENT COMPANIES which control the investment funds in whose hands is concentrated the ownership of many privatised enterprises will doubtless have a significant role to play in the new economic order.

THE SHAREHOLDERS both private and institutional whose role in terms of ownership and control of organisations will have a significant influence on the future strategic direction of the enterprises.

THE MANAGEMENT and EMPLOYEES whose role in the change process in critical since their motivation and behaviour are integral to the future efficiency and effectiveness of the enterprises for which they are employed. Additionally, however, they have their own agendas for survival within the new order.

THE FOREIGN INVESTORS who can bring with these the much needed financial investment and new technology which is critical to the modernisation and development of the economy.

ANALYTICAL FRAMEWORK

The stakeholder analysis will be undertaken at two levels. Firstly, at a macro level, the impact of the objectives and activities of the main interest groups on the privatisation process will be considered. Secondly, at a micro level, the role of the major stakeholders in relation to corporate governance, i.e. the nature of ownership and control within the newly privatised organisations will be discussed.

Corporate Governance

As direct control of business activity is removed from the direct sphere of government influence, the critical question must be raised as to who will assume that role. As such control carries with it the power to influence the future economic direction of the society, the establishment of an effective system of corporate governance is vital to the effective functioning of the newly privatised enterprises in the free market economy.

However, observations of the operation of the various systems of corporate governance within market-based economies indicate that this is an extremely complex process. Studies of corporate governance indicate that there are two main models of ownership and control categorised in the literature as the anglo-saxon 'outsider model' which predominates in the United Kingdom and the United States, and the 'insider model' of corporate governance found in Germany and Japan (Jenkinson & Mayer, 1992, p.2).

The 'outsider model' is characterised by the situation where the main institutional investors, although shareholders in the enterprise, take no active role in managing the activities of the company. If an enterprise is not operating to the satisfaction of investors in relation to their expectations, e.g. the required short

term rate of return on their investment, the financial markets provide an exit for shareholders by facilitating the process of buying and selling shares. Moreover, if the firm continues to operate below the expected level, then the market is structured to allow for external control mechanisms to influence the future ownership of enterprises by precipitating merger and takeover activity. Another essential feature of the system is the role of the banks. Whilst the banking institutions lend to enterprises they do not own any shares in them. Their main priority is to maximise their own profitability for the benefit of the banks shareholders. Thus, beyond safeguarding their investments in enterprises the banks do not have any real interest and control over the way in which organisations are managed. Thus the institutions and consequently the enterprises themselves adopt a very short term view when it comes to the issue of corporate planning. If the return on bank loans is expected to be long term, the banks will be unwilling to make the loans and commit their funds. If the shareholders to not receive a short term return on their investment they will sell their shares and invest their funds elsewhere. The short-termism enshrined in this model is considered by many business observers to be a major weakness of enterprises in both the United States and The United Kingdom. This system creates further problems for effective ownership and control due to the 'subsequent development of the 'free rider' and 'agency' problems respectively.

The 'free rider' problems occur where there are many small shareholders who because of the small stake in the enterprise do not have the funding or the influence to exercise control over the management. If they are not happy with the performance of management they simply make exit decisions by selling their shares. Thus, as 'free riders' they do not constitute an effective mechanism for controlling the activities of executives in the enterprise. In an ideal world this would not be a problem, as the management would share the same common goals for the enterprise as the owners (Mayhew & Seabright, 1992, p.110-111). As 'agents' of the owners the managers would carry out their duties in such a way as to fulfil their objectives of the shareholders. In reality, however, the management have their own agendas, e.g. job security, status protection and risk aversion, all of which can be at variance with the goals of the owners. Thus, the 'agency' problem arises for the shareholders when they attempt to control the activities of managers who are seeking to pursue their own self-interest. Shareholders attempt to resolve this problem by exercising control over the recruitment, reward and dismissal of managers.

However, there are major difficulties associated with attempting to control these activities which are exacerbated still further by the situation in the Czech Republic (Frydman et al, 1994, p144-145). These problems will be discussed when the role of managers as stakeholders is analysed later in this section.

The 'insider' model, which is prevalent in Japan and Germany is characterised by a situation of interlocking ownership so that institutional investors such as banks have major shareholdings in enterprises. This system of interlocking ownership inextricably links the long term stability and future success of the enterprises to those institutions with which it has ownership links. Within this system the priorities for enterprises and their owners focus more on the needs of management, employees, the lead banks and customers as opposed to the interests of the wider shareholders as it is believed that the long term success of the enterprise depends primarily upon the former groups. This system is marked by a much greater stability which in turn facilitates the process of long term planning and is characterised by the absence of hostile takeovers and merger activity. With the insider model, institutions will actively participate in the activities of the enterprise and seek to resolve problems which arise, as opposed to simply selling their shareholding if they are dissatisfied with the performance of the company. Consequently the free rider problem with its destabilising effect on enterprises in minimised. The agency problem is also less of an issue as the long term survival of the enterprise tends to set a framework for the establishment of common goals between the management and the owners.

However, this model is not without problems. It does lend itself to the problems of the transfer of insider

information between institutions which may have cross holdings in various enterprises. It can also lead to conflicting priorities for banks in their roles as both lenders to and shareholders in the same enterprises (Davis, 1994, p.1).

On the basis of the above analysis it can be seen that all the main shareholders have a role to play in the way in which corporate governance develops in the Czech Republic. Their respective roles will be analysed with a view to considering which of the models of corporate governance is likely to emerge in the new regime.

GOVERNMENT

The role of government as a stakeholder in the privatisation process will be analysed in terms its chosen method of privatisation, the level of government intervention at a micro level and the attitude of government to foreign investment.

These specific dimensions of the government role in privatisation will be considered as they are indicative of the degree of long term government intervention in the economy. This will impact directly upon the overall transition generally, and the development of private ownership and control at enterprise level, in particular.

CHOSEN METHOD OF PRIVATISATION

Although the government has adopted a range of traditional methods of privatisation, it is the development and implementation of the voucher programme which has attracted the most attention (Zolzaslaw & Sadowski, 1991, p.50). The evaluation of privatisation methods will focus upon this particular mode not only because of the uniqueness of the process but because of the major impact it has had upon the pattern of ownership in enterprises.

In this wider context, Ben-ner (1993, p.338) identifies a set of criteria against which it is possible to evaluate the overall effectiveness of the voucher privatisation from the perspective of government. These criteria are of value in that they address the social, institutional and organisational as well as the economic dimensions of the privatisation process. This is especially relevant given the multiplicity of political, economic and social objectives the Czech privatisation programme seems designed to fulfil.

The criteria comprise:

efficiency in terms of speed and cost

equity in terms of the voucher distribution criteria

expected equality of returns and equal access to scarce resources so that all citizens may acquire state property

completeness of bureaucratic control

the establishment of effective management during the transition

Efficiency

The efficiency of the privatisation process will be considered in relation to both the speed with which the government is implementing privatisation at a macro level and the pace of transfer of private ownership to individual firms. The issue of costs as they relate to efficiency will also be considered.

Speed of implementation

Concerning the pace of implementation of the overall privatisation programme, this issue has emerged as a philosophical debate expounded by two opposing schools of economic thought. These comprise the gradualist school of economic transition promoted by Kornai, the eminent East European economist, and the 'sudden shock' proponents of rapid economic change mainly supported by the monetarist school of economic thought. The gradualist school argues

that state owned enterprises should not be privatised until they have been restructured to the extent that they are able to compete successfully in foreign markets. Once so restructured, they argue, these enterprises will attract greater foreign and domestic capital for investment if they are seen as viable potentially profitable economic entities. Additionally, the gradual pace of economic change will ensure that the extensive social upheaval required to effect such a transformation will be introduced more gradually, thus reducing the negative motivational impact of the transition upon the community. Concerning the role of the state, the gradualists argue that, as the enterprises become more successful and self-sufficient the role of the state will become less and less interventionist and in the long term will wither away completely (Parker, 1993, p.400).

The supporters of the shock therapy approach are diametrically opposed to this view (Boycko, 1991, p.8). They argue that effective private ownership is a prerequisite of efficient and effective organisations which are driven primarily by the profit motive. They also point to situations where continued government intervention and control in nationalised industries has promoted inefficiency rather than reducing it. This argument further states that the prolonged period of uncertainty concerning the ownership of enterprises will lead to the unfettered pursuit of self-interest on the part of managers

which could result in organisational chaos and breakdown. They further argue that by implementing the necessary changes simultaneously and speedily, people will accept them and adjust more quickly to the new order.

From the government point of view the rhetoric of Václav Klaus would suggest that they are committed to the latter approach (Sacks, 1993, p.192). The Czech prime minister has always identified closely with the Monetarist School and was a great supporter of the privatisation policies of Margaret Thatcher's government in the united Kingdom during the 1980s. These views have led him and his colleagues to be nicknamed 'the Chicago boys', referring to the economic doctrine of Milton Friedman, by those who disagree with the government on this issue. As the ensuing analysis will show, however, in practice, the actions of government have been much more cautious than their words.

In effect, the government privatisation has been criticised for being both too slow and too fast. Clearly, the gradualist believe that the whole programme has been too radical and introduced too quickly. The radical monetarists however believe that the government delayed too long in waiting until 1992 to introduce the privatisation programme. In response to this criticism however, the timing of the government programme has been defended on the grounds that its main priority was the negotiation of the dissolution of the former Czechoslovakia. The 'cynical'

school of thought comments wryly that the government has been slow to implement the changes because:

> Members of parliament are so busy making money with all the insider information to which they have access that they do not have time to attend parliament and make decisions concerning the running of the country.

It is certainly true that the absence of any legal regulatory framework concerning the activities and interests of members of parliament and the unwillingness parliament to introduce one does lend some credence to this view.

There has also been wide-ranging criticism of the delays by the government in the issue of shares at the end of the first wave of privatisation. Most vociferous in their criticisms have been the investment funds who are anxious to know if their bids for shares in their selected enterprises have been successful and are anxious to get on with the business of managing them.

A further criticism concerns the concentration of assets which still remain in state ownership after the first wave of privatisation. Moreover, the delay in the commencement of the second wave has led to vociferous complaints from numerous quarters that the government has deviated from its radical approach to that of a more cautious interventionist

strategy. It is further argued that the main determinant of the pace of government privatisation is not to complete the transfer property from state to private control as quickly as possible but to minimise the number of bankruptcies (Brom & Orenstein, 1994, p.15). The validity of this argument will be discussed when the role of the financial intermediaries is analysed in the section below.

Concerning the speed with which the government manages the privatisation of individual firms this has also been criticised as slow and cumbersome. The main delays are attributed to the large number of government bureaucracies involved in the process and the lack of clarity in relation to their respective roles. The outcome of these weaknesses have manifested themselves in frustrating delays for potential purchasers which have been exacerbated by confusion and conflict and amongst the various relevant government departments.

This confusion is well illustrated by the events surrounding the proposed joint venture between Avia the Czech truck manufacturer and Mercedes Benz. An agreement had been signed between the two companies in January 1992 setting out the conditions for the joint venture. Under the agreement, Mercedes Benz was expecting to acquire a 31% stake in the company with a view to increasing it to 86% by 1997. It was expected that the agreement would be ratified by the government in June 1992. Prior to this date,

however, the Czech Economic Council announced that it was going to put 51% of the company into the voucher privatisation scheme. Clearly, this would make it extremely difficult for Mercedes to increase their stake as planned. The Council's decision was opposed by Karel Dyba the Minister for Development who highlighted that paradoxical situation whereby the government gives approval for the merger yet gives the majority of its shares to the public. Ultimately, the joint venture proposal was abandoned (Crosby, 1992 (a), p.9).

However, whilst there is clearly the issue of conflict in relation to the roles and objectives of the various institutions involved, there were also significant underlying agendas for the various other stakeholders, namely politicians and management. For the politicians, the cry of 'Germanisation' is never far from the lips of many Czechs especially after the acquisition of Skoda by Volkswagen. There may well have been fears of a car industry dominated by Germany which could prove politically unpopular at election times. From the management perspective, there is little doubt that the new joint venture would have undertaken a programme of restructuring which would have led to significant management job losses. Thus, from the point of view of the retention of both their jobs and their influence in the enterprise it is likely that many of the managers supported the voucher privatisation. However, as the analysis of the role of

financial intermediaries later in this chapter will show, management expectations of their control in relation to the voucher privatisation programme were very much at variance with the ensuing reality.

In an attempt to address the criticisms of the slow rate at which individual firms were being privatised, the government created the Czech Privatisation Commission whose function was to streamline the privatisation process. The main function of the Commission was to be the arbiter in disputes over privatisation. Objections to privatisation projects must be submitted within ten days of the initial decision and the judgement of the Commission is final. In this context one could question the logic of creating yet another government bureaucracy to speed up the activities of existing institutions (Crosby, 1992 (b), p.5).

However, despite these measures to accelerate the process, privatisation is still a very centralised government controlled function which continues to concentrate an extensive degree of power in the hands of the Privatisation Ministry. As long as government maintains this strict control on privatisation and restructuring decisions the process will inevitably be a protracted one and the frustrations and delays are likely to continue.

Costs

When considering the costs incurred in the privatisation process, in terms of administration and organisation, these areas are difficult to evaluate due to the un-reliability of statistical data and an insufficient degree of understanding of the cost concept in this context. Given the sensitive political dimension of the programme there is every likelihood that statistical data would be distorted to meet the needs of the government's political agenda. Possibly a more meaningful cost consideration would that of the concept of opportunity cost. These costs can be evaluated in terms of the lost revenue from the free distribution of property through the voucher privatisation scheme as opposed to selling the enterprises to the highest bidder. In the long term this may prove to be a heavy cost for the country to bear.

Any evaluation of the efficiency of government policy in relation to privatisation must be at best circumspect. As this type of privatisation on this scale has never been implemented before there is no standard against which to evaluate the speed of implementation. Additionally, many of the 'gradualist' versus 'monetarist' arguments have a philosophical theoretical basis which makes it difficult to validate objectively the claims they make. What does appear to be true, however, is that there are concerns, based upon peoples perceptions of what the pace of change

should be, that indeed the government is moving forward too slowly in this area. These comments are echoed by financiers, potential foreign investors and the management of some enterprises. The logical way to speed up the process would undoubtedly require the government to devolve some of its centralised control to other agencies or generally allow market forces to operate more freely. This is unlikely to happen. The government has committed itself to a centralised interventionist policy in relation to privatisation at a micro level which is likely to endure for at least the medium term. Moreover, the growing pre-eminence of the policy of government, whereby minimisation of bankruptcies is a major priority, has effectively shifted the aims of privatisation towards a more social and political interventionist orientation at the expense of progress towards a market-based economy.

Equity

The issue of equity in this context refers to equality in terms of distribution of vouchers and expected equality of returns to investors. There can be little basis for the allocation of vouchers, i.e. all Czech citizens over the age of eighteen resident in the country, meet this criterion. However, concerning equity in terms of expected returns, the situation is not so equitable. In this context, the value of returns on investment choices are

very much dependent upon the quality of available information upon which to make investment decisions.

It has been argued that, as result of the corrupt and inept practices of the past regime, there is very little meaningful information available to prospective investors. In reality, however, there is evidence of widespread corruption in the sale of information on the part of those bureaucrats who have access to the relevant data. This is and example of the continuation of corrupt practices of the old regimes transferring to the new order.

Additionally, the emerging pattern of bank cross ownership within major enterprises has given rise to problems of insider information and dealing.

Bureaucratic Control

In relation to the break with state control, the subsequent stakeholder analysis will illustrate the fact that, in effect, the government has retained and indeed extended the bureaucratic control of the privatisation process as opposed to the reduction in government intervention usually associated with the growth in free market activity. The extent of this control is demonstrated most clearly by the dominance of the National Property Fund and the Konsolidacni Banka.

Managerial Effectiveness

The effectiveness of management during the privatisation process has proved to be a highly problematical area for those trying to privatise enterprises. Discussions with senior management of various companies have indicated that many managers have been slow and unhelpful in the preparation of privatisation projects. Managerial intransigence in this area is understandable in that they are seeking to retain their jobs and their status in a situation where everything around them is rapidly changing in an unprecedented way, usually to their detriment.

However, such was the reluctance of managers to provide information to those wishing to submit competing projects the government was forced to extend the final date for submission of the competing projects for inclusion in the first wave of privatisation.

When the management projects were submitted, as illustrated by the Avia truck company, example cited above, voucher privatisation was favoured, not necessarily because it would create the most beneficial pattern of ownership for the company but because it would ostensibly protect their power and control within the enterprise. There are also instances where the management have stripped the assets of the company in order to reduce its value and subsequent

selling price to a level where they can submit bids to buy the enterprise at a lower price. Thus, the effectiveness and commitment of management to some aspects of the privatisation process could be regarded as questionable. However, Czech managers did not participate in any 'spontaneous privatisation' whereby managers took '*de facto*' control of the companies and ran them as if they were privately owned companies. Thus, their behaviour presented the government with less problems in relation to privatisation than those countries where such activities were undertaken (Frydman & Rapaczynski, 1994, p.62).

There is much speculation as to why this did not occur in the Czech Republic. Some believe that it was due to the completeness of state control of enterprises up to the time of liberalisation. There was no evidence that the Czechoslovak government recognised market activity as did the governments in Hungary and Poland. Others believe that it is attributed to the Sveck mentality of the Czechs who will pay lip service to their current master demonstrating ostensible obedience to the current ruling regime whilst privately exhibiting cynicism and disdain.

Evaluation

In terms of evaluating the privatisation process against the criteria set by Ben-ner it appears that the Czech voucher privatisation does to some extent fulfil

significant social and political criteria. The basis for initial distribution was socially equitable and there is no doubt that the scope of the privatisation exercise served to contribute the development of political pluralism. Institutionally, however, it has not significantly weakened the role of the bureaucracy. It has, in effect, substituted one set of bureaucratic institutions for another. It should be noted that this extended bureaucratic control is not necessarily an endemic feature of the voucher privatisation process. It is a function of deliberate government policy to retain strong central control of privatisation and to pursue a strongly interventionist policy in respect of the transition process generally. In dealing with management, the government's policy of open privatisation bids may to some extent have mitigated against the questionable effectiveness of management. It could be argued equally that this could have a negative motivational impact on the attitude and behaviour of managers who felt rejected.

Finally, however, in economic terms, the voucher privatisation has failed to provide the funding required for long term investment and technological expertise which the privatised enterprises require to survive in a market economy. This could possibly have been forthcoming had more direct sales activity taken place both to domestic entrepreneurs and to foreign investors. It is difficult to know, however, if this would in fact directly stimulate

additional foreign investment. Currently, there are many more global opportunities that are more secure and attractive investment propositions than those offered by Eastern Europe. Additionally, the world recession has to some extent reduced the availability of funding and the responsiveness of investors to long term business opportunities. The role of foreign investors as stakeholders and the rationale behind their investment decisions will be discussed below.

The complexity of the issues discussed above in relation to the role of government serves to illustrate the problems of evaluating the effectiveness of unprecedented phenomena such as voucher privatisation in a new environment. In this context the situation is further complicated by the multiplicity of seemingly conflicting objectives being pursued by government.

GOVERNMENT ATTITUDE TO FOREIGN INVESTMENT

The policy of government in relation to foreign investment serves to give some indication of the degree of freedom that the government is willing to accord to the operation of market forces and the extent to which the operation of free market principles is likely to prevail in the new order.

It is generally agreed that the newly established legislation relating to foreign investment in the Czech Republic is very liberal. However, if one accepts the premise that legislation is only as effective as the will of the government to impose it then the situation in the Czech Republic is rather different. In reality, the attitude of the Czech government to foreign investment is somewhat ambivalent. This is illustrated by the 'family jewels' policy which was adopted by Government especially in the early stages of the privatisation programme (Ceska, 1992, p.8). This policy sought to retain ownership and control of the country's most successful industries, i.e. porcelain, glass and brewing, in the hands of Czech citizens. This policy has ben cited as one of the main reasons for limiting the inclusion of such industries in the first wave of privatisation. In other instances examples of government intransigence and inconsistency in its attitude to foreigners have sent conflicting signals to potential foreign investors, e.g. Avia and Mercedes.

It would appear that in this context the government is still seeking to manage demand and supply within the economy despite the evidence of forty years of communist rule that this macro economic strategy failed. The administration is seeking to decide not only which foreign enterprises may purchase Czech enterprises but also which enterprises they should be permitted to purchase.

The ambivalence of government to foreign investment and to some extent the whole rationale behind the privatisation programme is well illustrated by the privatisation of the tobacco industry. This was an ideal situation for the government to introduce competition into a potentially extremely lucrative market by dismantling the state monopoly and dividing it amongst the competing US tobacco companies. Instead, the government decided to sell the whole industry to Philip Morris. By exchanging one monopoly for another, it helped to perpetuate the inefficiencies of the old regime, both psychologically and organisationally (McQuade, 1992, p.7).

Prospective foreign investors also tend to be the most vociferous, when condemning the slow pace of government decision-making in relation to the privatisation of individual firms. The perspective of foreign investors on this aspect of privatisation will be explored later in the present chapter.

GOVERNMENT INTERVENTION AT A MICRO LEVEL

Technically, when companies are privatised, then the government transfers control of state enterprises to the temporary ownership of the National Property Fund. In fact, however, the government continues to exercise considerable direct and indirect control over the activities of privatised organisations. Direct controls

continue to be exercised through the control of the National Property Fund whose role in privatisation has already been discussed.

Additionally, the government maintains indirect control of enterprises through retention of a 40% ownership stake in the banking system, upon which the heavily indebted companies are so reliant. Moreover, the investment companies, in whose hands the major shareholdings of companies are now concentrated, are owned by the main banks, thus, further re-enforcing indirect government control.

The main objectives of government in respect of this continued intervention relate to the long term objective of industrial restructuring, while minimising the impact of bankruptcy. As would be expected the two goals are proving difficult to achieve simultaneously. Government strategy in relation to the control of bankruptcy has been implemented, primarily, through their financial intermediation in relation to the management of company indebtedness. A primary vehicle developed for this purpose is the 100% government-owned Konsolidacni Banka. The bank's role, in relation to the debt management and bankruptcy of state enterprises will be analysed with that of the other financial stakeholders.

The direct interventionism of the government, in re-structuring and corporate governance issues, has led to dramatic instances where government has come into direct conflict with the management of enterprises. One of the most widely publicised confrontations concerns the Kralovy Porcelain Works. The government proposed a restructuring plan for the porcelain works which would have split the industry into separate divisions enabling each to be sold as a separate entity. These proposals were bitterly opposed by the management of the company, especially the director, whom the government summarily dismissed.

The government then proceeded to appoint and subsequently dismiss several directors, who would not give their support to the planned re-structuring. The relationship between the government and the enterprise deteriorated to the extent that the company took out an injunction to prevent the government implementing the proposed changes. The outcome was that the government was fined by the courts for contempt. A major court case threatened, but the situation was resolved when the government appointed a director who agreed to implement the government proposals, and withdrew the law suit (Crosby, 1992 (c), p.6).

Although the outcome would suggest a victory for the government policy of restructuring, it remains to be seen to what extent the outcome will be implemented in practice. Whilst the government can force acceptance of the plan in

principle, it is possible to envisage extreme opposition and difficulties in its implementation, if the plan does not have the support of the management and employees. Indeed, these groups have already voiced their opposition and hostility to the project.

The above example illustrates the difficulties involved in attempting to apply universal criteria when considering the effectiveness of privatisation. In terms of the objectives of government, the strategy was successful. From the perspective of management and employees the privatisation process was failing them.

EVALUATION

As a stakeholder, it seems clear that the government is determined to continue to exercise a strongly interventionist role in the privatisation process, both at a macro and micro level. This makes somewhat paradoxical the notion that privatisation is primarily concerned with the establishment of private ownership and property rights. It serves to illustrate the continued complexity and conflict inherent in the privatisation objectives of government. The critical issues for the privatisation process in terms of the government's interventionist role is the degree and time span over which it is likely to exercise such control in the future. These considerations will clearly have significant implications for the future

political development of the country. It may be that, ultimately, a social democratic political form will develop, where a substantial degree of direct government intervention, planning and control becomes an intrinsic part of the economic process, as opposed to a temporary interventionist policy to facilitate the process of transformation.

THE BANKING SECTOR

With its pivotal financial intermediation role at both a macro and micro level, the development of an effective banking system is a crucial element in the successful functioning of any market based economy. At a macro level, it fulfils the dual role of managing government monetary policy. Its prime functions, at a macro level, concern the mobilisation of savings and lending for investment and consumption purposes together with a general financial intermediation role which facilitates the process. In the Czech Republic and, indeed, all the reforming countries of Central and Eastern Europe there can be little doubt that the future of the private sector is inextricably linked to the progress of banks and banking reform.

The banking system has been reformed into a two tier model similar to that adopted by most western economies. This model establishes separate banks with control over lending and control of the money supply respectively. The Czech

banking legislation follows the German model which assigns a highly independent position to its central bank, in this case the Czech National Bank. It is overseen by a board of governors who are appointed for a period of seven years. In its capacity as controller of the money supply, the Bank applies the main regulatory tools as directed by the Government, e.g. interest rates and commercial deposits.

At a commercial banking level, there has been a substantial growth in the number of both domestic and foreign banks since liberalisation. By October 1992, fifty-three commercial banks had obtained licences to undertake commercial banking activities. However, as Appendix II shows, the majority of deposits went to the four largest banks. In 1993, over 45% of all deposits were controlled by the Czech Savings and Loans Bank - Ceska Spořitelna, the main savings bank used by depositors during the old regime. The evidence clearly suggests that it is still perceived as such by the majority of Czech citizens (Matesova, 1994, p.4).

Konsolidační Banka

The new structure of ownership in the banking system is such that it will remain very much under the influence of government. The intent of government to retain a heavily interventionist role in the economy at a macro and micro level is well illustrated by the role of the Konsolidační

Banka. This bank was established by the government in 1991 specifically to attempt to deal with the massive debts accumulated by the banks in respect of the former state owned enterprises. The main objective of the government and the bank is to manage this debt in order to reduce the potentially massive number of bankruptcies which would sweep the country if banks were forced to call in their loans. Their accumulated debt was tackled by the Konsolidační Banka, which purchased 15 billion crowns worth of bad loans from the state bank and 110 billion krowns worth of debts from the main Czech banks at a very favourable discount rate. The Konsolidační Banka then became responsible for the management and recovery of these debts, and now collects loan payments from over six hundred companies. Thus, it is, in fact, the largest receivables management company in the Czech Republic.

The Konsolidační Banka is proposing to widen its role further by purchasing the payables of companies in bankruptcy liquidation, using monies obtained from the National Property Fund. The bank would buy out the claims of other debtors, at approximately a 50% discount, and give some of the money back to the creditors. It would then have the options of selling on the debt claims to other creditors, seeking to redeem loans through undertaking bankruptcy proceedings, or taking equity holdings in firms. It is also likely that the Konsolidační Banka would have a significant role to play in the creditors' committees of

bankrupt firms, as 80% of firms owe money to the bank. The bank is also seeking to reduce intercompany indebtedness by introducing a computerised netting system, which matches receivables to payables in attempts to reduce overall levels of company debt. However, some discontent has been expressed by firms participating in the exercise, who are somewhat sceptical of its effectiveness (Brom & Orenstein, 1994, p.17).

In terms of evaluating the role of the Konsolidační Banka, there is little doubt that the bank has been successful in that its injection of capital into the banking system has freed the banks from the deadly legacy of non-performing loans. There are questions to be raised, however, as to whether the establishment of yet another government controlled institution is the most effective way of achieving this. Indeed if the role of the bank is extended as is envisaged, it could become a powerful centralised state planning mechanism, very similar to those which were abolished in 1989. Additionally, one can question the opportunity cost of the funds used to prop up technically bankrupt industries with money which could be used more effectively for funding the development of new commercial initiatives and enterprises.

More critically, however, the extent of Konsolidační Banka involvement in so many areas of corporate and financial control has raised fears that it could effectively become

a state-planning commission fro government long term industrial planning policy. Implicit in this financial policy and that of bankruptcy minimisation, is the assumption that government will be committed to a significant interventionist role in the economy beyond that usually found in the market economies of Western Europe. This is turn has raised fears that the continued government intervention with the essential mechanisms of market forces could prove to be a serious drawback and, indeed, amy influence adversely the future direction of the transformation process itself.

PROBLEMS OF THE BANKING SYSTEM

The wider role of the banking system generally has been criticised for its ineffectiveness and inefficiency (Rooney, 1993, p.7). In essence, it is argued that the banks have not changed their culture and practice sufficiently to fulfil the new functions required of them. Informally, some individuals believe this is due to the fact that the old nomenklatura or the new corrupt elements in the society are now playing dominant roles in the major banking institutions. However, such claims are difficult to substantiate. Additionally, criticisms are levelled at the technical ability of the banks to undertake the commercial roles required of them primarily as a result of the poor quality of staff who are reluctant to change their ways.

In describing how loans were negotiated under the old regime, one manager explained that:

'my boss went to visit the bank manager with a bottle of whisky. They had a few drinks, agreed the loan and proceeded to finish off the bottle.'

In response to the criticisms of the effectiveness of the banking system, the vice president of the Investiční Banka highlighted some of the staffing problems faced by the bank. Many of the existing staff do not wish to change their ways. When it comes to recruiting new staff, the bank must compete with other new enterprises for the best of the new generation of university graduates. However, they are unable to match the remuneration levels offered, due to government control of wage levels in privatised industries. Additionally, even when the bank does recruit able staff, it experiences problems in finding suitable training programmes for them. Most international banking courses require a knowledge of English or one other language. For most Czechs, their second language is either Russian of German. The banks also faces problems of lack of knowledge and experience of commercial banking procedures especially when granting loans. It has been wryly observed that there is no need to worry if you do not know how to prepare a business plan, when requesting loans from the banks, as bank staff do not understand them anyway.

THE BANKING SYSTEM AND CORPORATE GOVERNANCE

The concerns over the inefficiency of the banking system are further exacerbated, when one considers the significant governance roles they are set to assume within enterprises. This is a direct result of the complex system of cross ownership that has developed, due to bank ownership of the main investment companies.

The complexity and potential ramifications of this situation can be interpreted from Appendix III, which lists the financial institutions in the portfolio of selected investment funds. VUB IC is a bank controlled investment fund, which has purchased shares in the main commercial banks, Ceská Spořitelna and Komerční Banka. This investment company may own shares, also, in companies which are massively in debt to these banks. Thus, the situation is rife for the passing of insider information and for collusion amongst banks. It is highly likely also that enterprise business decisions concerning enterprises will based upon banking strategy rather than up to corporate priorities. The situation is made even worse by the fact that the legal framework and regulatory institutions required to control the process are not yet <u>in situ</u>. It is not yet clear how the banks will use the power they have. However, given the series of business scandals that are currently emerging in the Czech Republic, it is highly

likely that more significant abuses of the system will emerge (McQuade, 1992 (b), p.8). This is especially likely, when one considers the degree of fraudulent activity in those countries where the appropriate legal and regulatory institutions exist to monitor it.

In terms of control of the economy at a macro and micro level, it is clear that the banks are emerging as the most powerful institutions next to government. Government policy, instead of stimulating competition and promoting fragmentation of monolithic financial institutions, seems to be swapping one set of centralised controlling regulatory bodies for another. This control has been further re-enforced by the system of cross-ownership which has emerged directly as a result of the government voucher privatisation programme.

INVESTMENT COMPANIES

A uniquely significant feature of the transformation of the Czech Republic into a market based economy has been the high degree of concentration of share ownership in the hands of the investment funds. This has placed them very much at the heart of the privatisation process in general, and corporate governance in particular.

The extent to which investment funds and the companies which manage them are heavily intermeshed within the system

of private ownership will doubtless influence the role that investment companies will play within enterprises, although it is too early to speculate on what that role will be. In the initial stages of privatisation, there were fears that when the shares were allocated the investment companies would have insufficient cash to sustain the promises made to shareholders concerning the returns on their investment. It was argued that this would necessitate the sale of shares in enterprises to foreign institutional investors, who would then have a disproportionate degree of influence in the management of enterprises. It was also believed that the problems for investment funds would be compounded, because people were likely to sell their shares for cash thus depressing share prices.

In the event, neither of these fears was realised. The low liquidity of the investment funds is to some extent being offset by the fact that they are also selling shares for cash to finance their operations (Hawker, 1994, p.9). Additionally, the government delay in issuing shares has given the investment companies more time to improve their liquidity situation, before having to fulfil the promised returns to investors. Moreover, there is some evidence that rather than adopt the short term outlook of financial management only, the investment funds are taking an active part in the restructuring and management of those enterprises in which they have a significant stake (Brom & Orenstein, 1994, p.17).

INVESTMENT FUNDS AND CORPORATE GOVERNANCE

The significant concentration of investment company holdings in the former state enterprises will clearly have major implications for the development of corporate governance. Although still in the embryonic stages of their development as owners, the evidence suggests that the investment funds, and the banks which control them, are set to become directly involved in the management of those enterprises in which they have major shareholdings. The pattern of interlinked cross-holdings now emerging is likely to lead to an insider model of corporate governance similar to that of the German model with which there are already significant similarities in the industrial structure.

The legislative framework of corporate control set out in the Commercial Code re-enforces this comparison. The Code draws heavily upon the German model of corporate ownership and control. Under the Commercial Code, now introduced within the Czech Republic, all joint stock companies, the form adopted by most privatised companies when they become corporatised, must have two boards:

THE EXECUTIVE board which is directly responsible for the day to day management of the enterprise

and

THE SUPERVISORY board whose role is to review the financial reports of the executive board, and ensure that the enterprise is managed within the law.

In enterprises with more than fifty employees, one third of the members of the supervisory board must be employees elected by a general vote of the workforce. The executive board may be elected by a general meeting of the shareholders or appointed by the supervisory board. The Commercial Code, however, does not specify whether the owners of the company should sit on the supervisory or executive board. This clearly allows for direct owners to intervene in the day to day management of the enterprise, if they choose to sit on the executive board. In those firms where investment companies constitute the majority shareholders, surveys have shown that they generally dominate the executive board. In some cases, this is against the wishes of the management who believe that this is their role. They consider the presence of the investment companies on the executive board to be a constraint on their management activity.

Brom and Orenstein (1994, p.33) recently examined the role of investment companies in four companies, where the majority of shares had been distributed via the voucher privatisation. In these enterprises the dominance of the investment companies was clearly visible in terms of their involvement in strategic decision-making.

Although it is too early yet to formulate the long term role of the investment companies within enterprises Brom and Orenstein interviewed nineteen investment companies with a view to eliciting their future management roles within enterprises. Not surprisingly, given the short time period that has emerged since they acquired ownership of the enterprises, the managers of the investment companies were unwilling, or possibly at this juncture unable, to articulate how they saw their future role developing. They did however, identify key features they believed would influence their roles within the enterprises in the future. These comprised the level of their financial backing, the number and qualifications of their staff and the overall financial strategy of the investment companies itself. Given that the financial strategy of the investment companies is likely to be dictated by the banks which own them, the enterprises are likely to be indirectly controlled by the banks.

Within organisations, the investment companies identified the quality of management in enterprises as being a main problem. Although the Lustrace Laws removed many senior managers, they have been replaced by other senior managers who had held positions of responsibility under the old regime. As these managers also were appointed primarily on the basis of their membership of the Communist Party as opposed to their ability, their level of competence was still questionable.

However, as the investment companies recognise that they need continuity of management to run the companies and management wish to retain their jobs, it is in the interests of all concerned to establish an effective working relationship. The funds also see effective financial management and marketing as the next priorities. Whilst aware of the necessity of dealing with bankruptcy and work force reductions, they are not planning to address these issues at this point in time. This view must beg the question as to how enterprises can expect to be effective if they try to function with the same structures that proved inadequate and ineffective under the old regime. The problems associated with restructuring of enterprises will be discussed in the chapter dealing with organisational transformation.

SHAREHOLDERS

Shareholders in the newly privatised enterprises comprise essentially the National Property Fund, the investment companies and private individuals. As the roles of the main institutional investors have already been discussed, this analysis will concentrate next on role of private individuals as shareholders (Mills et al, 1994, p.4). This role is clearly a new phenomenon to the current generation of Czech citizens. As would be expected, there is an absence of a shareholder tradition and culture which will

undoubtedly influence the activities and perceptions of the new class of shareholders.

The poor uptake of vouchers prior to the advertising campaigns of the investment funds indicated a high degree of apathy and disinterest in the process on the part of potential shareholders. The fact that people assigned such a large portion of their shares to investment funds re-enforces this view to some extent. Some would argue however, that the shares were transferred to the investment companies as a result of people's ignorance of share ownership in general and a lack of specific information on enterprises which prohibited them from making informed choices.

There were also fears expressed that individuals with shares might immediately rush to sell them thus putting downward pressure on the share value of enterprises. There was concern that this might create significant problems for the embryonic financial markets. In fact, this proved not to be the case. It is not entirely clear why this was so. Possibly, it was due to the lack of developed and accessible facilities for buying and selling shares. Additionally, there may be a strong element of habit in people's decisions to keep their shares. Under the old regime, people saved their money because there was nothing left for them to spend it on. Moreover, as people saw their incomes fall and their savings eroded as a result of

price liberalisation, they may be seeking to establish their previous savings and spending patterns.

One frequently hears the complaint that:

> Under the previous regime we had plenty of savings because there was nothing in the shops to spend it on. Now the shops are full of goods but they are so expensive that we have no savings left to spend.

SHAREHOLDERS AND CORPORATE GOVERNANCE

The high concentration of share ownership in the hands of the investment companies has minimised the potential role of individual shareholders in the area of corporate governance. Their influence will only be exercised indirectly by the way in which the investment companies manage their shareholdings.

Even where shareholders are given the opportunity to exercise some kind of control through the medium of the shareholders meeting, in most instances, the attendances have been minimal. This is probably a function lack of understanding of the shareholder role. Additionally, it may be a manifestation of the communist bred attitude that

someone else should take the responsibility for decision making.

It is clearly much too early to evaluate the extent to which the Czechs have become a nation of shareholders, although the investment companies have significantly reduced the likelihood of that happening. Moreover, the evidence from the U.K. suggests that it is not a pattern of behaviour widely adopted by the population, even in a culture where it was politically and financially encouraged as during the Thatcher Regime.

MANAGEMENT

Whilst the activities of management will be discussed in the later chapter dealing with organisational issues, the role of managers as stakeholders in the enterprise has direct significance for corporate governance, especially in relation to the 'agency' problem.

Although it is possible in theory for shareholders to control the activities of management by recruiting, motivating, rewarding and dismissing them, the ability to do so, in practice, requires a significant concentration of control, access to substantial amounts of information supported by an effective system of communication and the ability to interpret and apply this knowledge. At best this is logistically a very difficult task for

shareholders. This is especially so, given the absence of information on management performance, especially in relation to financial information. Additionally, the task is made even more complex by the inexperience of both individual and institutional shareholders, who do not have the skills and experience to evaluate the information they receive. Generally, the effectiveness of the communication systems providing the information must be questionable especially given the convoluted bureaucratic structures through which they must pass to reach the recipients.

In this context Brom & Orenstein (1994, p.30-38) quote the example given by an investment company. When the fund they manage became owners of one company, they found that the management were preparing to sign a highly disadvantageous joint venture with a foreign partner, probably for a very significant bribe. The deal was immediately halted by the supervisory board.

EMPLOYEES

Concerning the role of employees as stakeholders, current company legislation, based upon the German model of industrial democracy, provides for employee involvement in the supervisory board of joint stock company. In theory, this affords employees the opportunity to participate in the process of strategic decision-making. Clearly, this situation has potential implications for the issue of

corporate governance, in terms of the possible conflict between the goals of management and shareholders, with those of employees.

However, research on the German model of employee involvement has concluded that successful participation requires the support of an active trade union and the provision of a wide range of educational and training opportunities to qualify employees for a meaningful role as members of the supervisory board. It also requires the commitment and will of employees to take up the participation opportunities offered to them.

The evidence of the Czech situation suggests that none of these conditions is present. The role of the unions in the new regime is that of a consultative as opposed to an executive decision-making body, although this may change in the longer term if the system of industrial democracy prevails. Despite the training and development opportunities for trade union training and development offered by the German Trades Union Federation there is little money available for funding employees to attend them.

Finally, there is little evidence that employees generally wish to change from the traditional pattern of acquiescence to which they have been programmed to that of a more participative decision-making role (Mills, 1991, 104-5).

FOREIGN INVESTORS

At a national level the relationship between potential foreign investors and host countries is to some extent indicative of the role that the government wishes to play in the economic activity of its country. By considering the relationship between the Czech Republic and some foreign investors, some indications of the future role of government in the privatisation process and the economic activities of enterprises generally should emerge. Moreover, the signals sent to potential future foreign investors from the current attitude of government to foreign enterprises will undoubtedly influence future levels of foreign investment in the region.

From a micro perspective, many of the newly privatised companies are seeking joint venture foreign partners to inject badly needed technology and investment into their ailing industries. From the perspective of foreign investors their motivation in this area in less than clear. However, given that, as owners and part owners of many Czech firms they will play a significant part in the domestic issues of corporate ownership and control. Consequently, the strategy and rationale behind investment decisions and the strategies of some foreign enterprises will be discussed.

Given the multiplicity of strategic objectives upon which investment decisions are based, this is a complex task. However, Holmes (1993, p.472-488) undertook a series of in depth interviews with sixty enterprises which had invested in Hungary, Poland and the former Czechoslovakia with a view to establishing the rationale and motivation behind their investment decisions. The interviews took place between October 1992 and May 1993 and were conducted primarily amongst US multinationals, although some local firms were also included. Interviews were carried out at corporate head offices, European headquarters and the location of the business activity in the host country to gain a wider perspective on the issues being discussed. The enterprises were in the manufacturing sector and comprised consumer durable and non-durable goods together with industrial goods.

For most enterprises the decision to invest in Eastern Europe was part of a strategic response to increased global competition, mature western markets and poor product penetration in the former communist countries. Additionally, balancing of regional manufacturing locations was also a significant consideration. Interestingly, none of the respondents cited the lower costs of production in Eastern Europe as a reason for investing in that region. In fact, such were the inefficiencies and social costs associated with setting up in Eastern Europe that there was no perceived cost advantage to setting up in those areas.

The enterprises clearly identified some of the major problems associated with their investment decisions. Facilities frequently had to be purchased without financial valuations or clear titles of ownership. The rudimentary state of the legislation and the lack of experience of the judicial system meant that property protection was not yet fully specified. Thus, although intellectual property laws were on the statute books there was as yet no formal system of redress. In fact, foreign companies were advised to avoid the courts where possible. The poor quality of telecommunications was considered to be a major problem also.

Despite these problems, the enterprises believed that the risks involved were less than the potential strategic opportunities available to them. They recognised that any investment decision would only reap benefits in the longer term. This was especially true of the consumer goods industry which believed that early positioning of their products would ensure that they moved down the income pyramid as the wealth of the region grew.

However, for those industries involved in the production of capital goods the view was not so positive. The industrial goods market had not yet settled down from the dislocations of the command economy and the privatisation process. Additionally, the continued subsidies from government have tended to mask the restructuring requirements of many

manufacturing enterprises. Moreover, the insistence by banks that loans are used for working capital purposes only has precluded Czech enterprises from making investment decisions.

Amongst foreign companies the most common method of entering markets was by way of formalisation of previous licensing agreements or by joint ventures, which although not usually the most favoured form of business partnership, does seem best suited to the uncertain and constantly changing business environment in which they find themselves. The internal organisational problems faced by both domestic and foreign companies will be dealt with in the next chapter. However, certain key organisational issues were identified by enterprises as influencing their investment decisions and, consequently, are likely to impact on the issue of corporate governance.

All enterprises stressed that managerial control of joint activity was vital even if the foreign enterprise had a minority shareholding in the joint venture. In such situations the investor tried to ensure that, in the short term, managerial control was written into the agreement and ultimately sought to gain a majority interest in the enterprise in the longer term. Clearly, the dissemination of ownership via the mass voucher privatisation mitigates against this situation, as the Avia-Mercedes Benz situation highlighted. Paradoxically, however, the ultimate

concentration of share ownership in the hands of investment funds may, in effect, facilitate the transfer of ownership, although the absence of effective financial markets may well delay such transfers of ownership.

Some enterprises cited major problems of dealing with government and uncertain and taxation regimes.
There are certainly examples of foreign enterprises, which experienced difficulties in both these areas when dealing with the Czech Republic.

NEW TAX REGIME

The new taxation regime introduced in January 1993 defined as a resident of the Czech Republic:
'any individual physically resident in the Czech Republic for more than 183 days in a calender year'

As such, they would be taxed on their world-wide income. From the perspective of expatriate employees on long term secondment to the Czech Republic this had the effect of increasing their tax burden from 17% to 47% (Krochen, 1992, p.9). Additionally, unlike most European countries, there were no special provisions granted to expatriate employees because of the higher expenses they incurred. The response of foreign companies to this situation was mixed. However, several firms threatened to reduce their ex-patriot

workforce significantly in response to the 'prohibitive tax laws'.

The new tax regime also included the taxation of previously untaxed benefits in kind which effectively doubled the cost of employing expatriates. In response to the widespread concern generated by these measures, some amendments were introduced in July 1993. It is not yet clear what their impact will be on the tax position of foreigners working in the Czech Republic.

There can be little doubt that these measures send strongly negative signals to foreign companies and could well lead to a reduction in vital technical expertise. It is difficult to rationalise the actions of government in the area of taxation. Some put forward the argument of inexperience. However, there are many instances of existing tax regimes from which the Czechs could draw an acceptable working model. More frequently, however, the informal response from some quarters is that the Czechs simply do not like and do not want foreigners, to whom they are at best indifferent and frequently rude. As the rationale behind the design of the taxation regime has never been revealed, the possible reasoning behind it can only be speculation.

The overall evidence from the survey tends to suggest that locational investment decisions tend to be a result of

global strategies rather than the efforts of individual countries. Thus it is difficult for East European countries to attract industry positively. It does appear, however, that lack of co-operation and problems with government and bureaucracies can negatively influence investment decisions. Overall, in many instances the behaviour of government in relation to foreign investment has been at best ambivalent and at worst obstructive. In the long term this could have significantly adverse effects on the economic development of the country.

CASE STUDY

Thus, privatisation is not only a complex administrative process to implement, it is a function of the subtle interplay of the objectives and agendas of the various stakeholders, who have vested interests it its progress.

Against this backdrop of competing interests the problems of the privatisation process are well illustrated by the case of Skoda Pilsen, one of the oldest and largest producers of industrial, energy and transport equipment in the Czech Republic. Czech citizens will tell you proudly that Skoda Pilsen has been making railway carriages since the time of the Hapsburg empire. The company has been the mainstay of employment in Northern Bohemia for one hundred and fifty years, employing 34,000 people before liberalisation. In January 1992, however, it was forced to

lay off 9,000 workers reducing its workforce to 25,000 as a result of the loss of its main East European markets.

In September 1992 shock waves and consternation swept the Czech Republic when it was announced that this flagship of Czech engineering prowess was about to be made bankrupt as it was almost 5 billion crowns in debt. The impending bankruptcy situation was precipitated by the failure of CSD, the Czech railway system, to take delivery of fifteen railway carriages. It was unable to pay for them due to the withdrawal of government subsidies.

Previously in 1991, the Czech government had given Siemens permission to enter into negotiations with Skoda with the objective of entering into a joint venture with two subsidiaries, Skoda Energo and Skoda Transport. It was anticipated that the agreement, which would have absorbed 43% of the firm's workforce, would be finalised by October 1992. Prior to that date, Siemens had already demonstrated their commitment to the joint venture by sending company managers to provide technical support. It was also anticipated by the National Property Fund that the 24% of the company which was considered profitable could be sold off separately to potential private investors (Biswas, 1992, p.1).

A main stumbling block to the joint venture was the degree of product and environmental liability Siemens would be

expected accept. The main concerns of the German company focused on the area of nuclear power where problems could arise over Skoda built energy equipment. The situation was made even more critical by the fact that Czechoslovakia had never signed the Vienna Accord on nuclear power safety standards and as such was not bound by them. Siemens were hoping that the Czech government would assume some liability in the same way as the German government had done for similar GDR projects.

The view of the government expressed by the Czech minister of industry Vladimir Dlouhty, however, was that:
'the new owner must take the old responsibilities of a factory. It's part of the price and the owner should know it'.

The government's intransigence over this issue clearly had an adverse influence over the future development of the joint venture. The situation was made even worse when the government intervened directly in the running of the company by giving the board of directors the task of proposing solutions to the economic problems of the enterprise. Clearly the board was faced with an impossible task. When their proposals did not meet the expectations of the Ministry of Industry, Dlouhty declared that:
'the managements capability to suggest any solutions to the situation in the plant was insufficient'

He also indicated that he might well remove the board. The directors themselves decided that they would resign after the completion of the joint venture deal with Siemens. In the event the board resigned in November 1992 while the joint venture negotiations were still in progress (Crosby, 1992 (d), p.5).

The possibility of the joint venture being completed became even more remote when a new board of directors was appointed. Up to this time, Siemens had expected to acquire 51% of Skoda Transport in November 1992 and subsequently to obtain a 67% holding in Skoda Energo. The new chairman of the board was back-tracking on the latter venture, whilst Siemens was demanding both. As a result of the combination of problems outlined above, Siemens finally withdrew from the proposed joint venture.

The new chairman of the board was the head of a consortium including the main Skoda Pilsen creditors, Investiční and Komerční Bankas, which had just purchased 34% of Skoda Pilsen. This consortium had submitted the winning privatisation project whereby, as a result of their proposed restructuring plans, the government pledged to pay 1.88 billion crowns of Skoda debt to the Konsolidacni Banka. A condition of this debt amortisation was that the enterprise should be restructured by breaking the organisation up into thirty-four separate companies. According to Korcanik, the minister of finance, the

restructured companies would be better able to find new creditors of their own.

By January 1993 there had been significant disagreement between the government and the board of directors of the holding company of Skoda Pilsen. The directors insisted on remaining a majority shareholder in all its subsidiaries arguing that the firm should remain intact. They believed that if they divided the firm up into separate entities it will jeopardise its greatest asset - its name. The management of Skoda Pilsen sent a letter to Václav Klaus in February 1993 stating that:

> the loss of the traditional Skoda Pilsen trademark would seriously worsen the possibilities of further development of all its subjects

At this time also, the government initially agreed to purchase the unsold railway carriages which had precipitated the bankruptcy. However, the decision was reversed five days late by Kornacik who stated that it would take the Czechoslovak Railways back to socialist times (Crosby, 1992 (e), p.8).

This case study serves to crystallise the conflicting objectives and agendas of the various stakeholders in the privatisation process together with the complexity of re-establishing private ownership in the new regime.

The interventionist role of government at a micro level is very clearly illustrated together with its intransigence in relation to foreign investment. The government espouses its desire to restructure Skoda Pilsen and divide it into separate companies in order to sell it off. However, when the joint venture opportunity with Siemens presented an opportunity to achieve this aim, the government proved to be deliberately obstructive both in relation to product liability and the choice of privatisation project for Skoda Pilsen.

This case also illustrates the way in which the government is seeking to intervene with the operation of the exit mechanisms in relation to market principles. Despite the rhetoric on restructuring the government used the Konsolidacni Banka to capitalise the loans and prop up a company which is clearly bankrupt.

A further major criticism of the privatisation policy that the government had adopted is the view that policy decisions will be made in response to situations as they arise. The decisions made by government in relation to Skoda Pilsen show no evidence of consistent policies emerging in relation to privatisation. The logic behind government decisions and actions is not always clear (Hawker, 1993 (b), p.1).

The integral role of the Investiční and Komerční Banks as

both creditors and owners is indicative of the pattern of insider control in relation to corporate governance which is clearly emerging. In this context, the spectre of banks' weaknesses as both owners and effective financial intermediaries could well loom large in the future.

From the perspective of management, the agency problem is clearly manifesting itself over the reluctance of the directors to restructure the enterprise and divide it into separate companies. Dismantling these monolithic state enterprises is the only way forward for the long term survival of the enterprise but is significantly at variance with the job security, status and the personal objectives of the management. This area of impasse is creating significant problems for government in trying to engineer restructuring of industry without allowing market mechanism to effect the necessary bankruptcies and structural changes that industry must undergo if it is to compete effectively against increasing international competition (Hawker, 1993 (c), p.8).

Overall, this case study serves to illustrate pervasive government intervention in all areas of the economy, possibly to the long term detriment of the transformation process. It also crystallises the conflict of interests, roles and objectives amongst the various stakeholders. Unfortunately, there appears to be no readily available compromise or resolution to these conflicts which can only

have a long term detrimental effect on the economic development of the country.

CONCLUSIONS

There can be little doubt that the Czech government with its consistently supportive popular mandate has undertaken an extremely radical programme of property redistribution from state to private ownership. The task facing the government in pursuit of this goal is indeed monumental. As the experience of developed economies has shown, the establishment of a private property regime within a market economy is a result of the development of a capitalist system which has evolved over time through a unique set of historical circumstances. Moreover, it is developed in ways that are not even fully appreciated or understood by those who function within it. The very concept of private property and the institutions and regulatory frameworks required to secure its continued existence are constantly evolving concepts which change over time in the light of changing political philosophies and their accompanying economic doctrines.

How successful is the Czech government is its attempts to fulfil the essentially ill-defined and evolving objectives of a market economy though its chosen privatisation route? The monetarist vision of Václav Klaus with its emphasis on the ever diminishing role of the state has remained very

much in the realms of political debate and discussion. As the Skoda Pilsen case has shown the reality is that the actions of the Czech government are very much at variance with the central tenets of monetarism which stress private ownership and the free operation of the market economy. The government has undertaken a set of economic and financial policies which are structured to ensure long term government planning and intervention in the economy. Thus, the government has perceptibly moved along the political spectrum to that of social democrat as opposed to a more less interventionist role.

One could argue that a simple reformulation of stated government economic objectives to encompass long term industrial planning policy may be enough to resolve the dichotomy between rhetoric and reality. However a political redefinition of government objectives could have major implications for the future privatisation process and the whole concept of private property together with the rights and obligations that accompany it. Essentially, the government is trying to control and manage processes which, by definition, must be free to respond to market signals. Given the inherent paradox of managing the unmanageable the government could be seen as merely postponing the wave of bankruptcies and closures which must inevitably occur at some point. Indeed the cost in terms of the funds and expertise being committed by the government in pursuit of this policy will almost inevitably be to the detriment of

the long term development of the newer industries and enterprises upon which the future of the Czech economy will ultimately depend.

As regards the emerging role of stakeholders, in keeping with the interventionist role of government the most powerful institutions currently emerging in the new order are those which are directly and indirectly controlled by government, i.e. the banks, investment companies and the bureaucracy. The problem is that whilst government backing has given these institutions a great deal of power in the new order, it has not yet developed the legal and regulatory framework to control their activities or hold them directly accountable for their actions.

Effectively therefore, through the system of cross-ownership the banks control economic activity in the majority of the privatised industries. The voucher privatisation has concentrated ownership in the hands of the investment companies and has thus consequently reinforced the power of the banks even more, a strategy that is clearly questionable given the inadequacy of the banking system.

Concerning the role of foreign investors, the Czech Republic is a mixed bag of opportunities and problems. Many of the main problems relate to inconsistent protracted government decision-making and ponderous, corrupt

bureaucracies. One could see where continued direct government intervention and the extension of bureaucratic control could send strongly negative signals to potential foreign investors. Additionally, the structure of voucher privatisation has favoured concentration of ownership in the hands of Czech citizens as opposed to the new technology and investment which could have been generated by potential foreign investors. Thus the Czech government is sending yet more powerful signals of the significant degree of ethnocentricism which permeates much government decision-making.

As regards the managers and employees, here lies a major key to sustaining any meaningful change in policy and practice in the area of privatisation. In the final analysis, it is the actions and responses of the individuals within the privatised enterprises which will determine the extent to which privatisation is effectively implemented. The power of inertia at this level would render the transition process at worst impotent and at best protracted. The issues of privatisation in relation to organisations will be discussed in the next chapter.

In the final analysis, the answer to the question: is the privatisation process successful? - must be - for whom? The privatisation process has undoubtedly exacerbated the stratification of different social and economic groups, clearly dividing them into winners and losers, at least in

material terms. Thus, the perceived success of privatisation will be dependent upon the group to which one belongs. The problems arise, however, when those who are winning have sufficient power to arrest or divert the course of privatisation towards their own ends, at the expense of the majority of the people. Moreover, the current void being crested, as the old order is swept away and the long term process of re-structuring begins, is undoubtedly facilitating this process. It is to be hoped that the restructuring process will be of sufficient speed and effectiveness to prevent the institutionalisation of these potentially corrupting and disturbing trends.

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APPENDIX I

CONCENTRATION OF SHAREHOLDINGS IN INVESTMENT FUNDS

Česká Spořitelna (ČS)	950 million
První Investiční (IB)	714 million
Harvard Capital and Consulting (HCC)	639 million
Všeobecna Úvěrová Banka Invest (VUB)	501 million
IKS Komerční Banka (KB)	466 million
KIS Česká Pojišťovna (KIS)	334 million
Creditanstalt	220 million

Source: Brom, K. & Orenstein, M. (1994) Privatisation in the Czech Republic. Unpublished paper, Central European University, p.24

CONCENTRATION OF BANK DEPOSITS

Banks	Percentage of Total Deposits
Ceska Sporitelna	47.8
Komercni Banka	24.2
Investicni Banka	8.4
CSOB	4.3
Agrocanka	4.1
Konsolidacni Banka	1.8
Others	9.4

source: Matesova, J (1994) Corporate Governance and Financial Infrastructure. Paper presented at the conference for the Advancement of Socio-Economic Research, Paris, Appendix

APPENDIX III

FINANCIAL INSTITUTIONS IN THE PORTFOLIO OF SELECTED INVESTMENT FUNDS

Všeobecná Úverová Banka's IC*
Česká Spořitelna
Komerční Banka
Obchodní Banka
Všeobecná Úverová Banka
Živnostenská Banka

Obchodní Banka's IC*
Česká Spořitelna
Investiční Banka.
Komerční Banka
Všeobecná Úverová Banka
Živnostenská Banka

Harvard Capital and Consulting's IC
Česká Spořitelna
Komerční Banka
Česká Pojišťovna

Prva Slovenska Investica's IC*
Česká Spořitelna
Investiční Banka
Investičná a Rozvojová Banka
Komerční Banka
Všeobecná Úverová Banka

source: Brom, K. & Orenstein, M. (1994) Privatisation in the Czech Republic. Unpublished paper, Central European University Press, p.26

CHAPTER 10

ORGANISATIONAL TRANSFORMATION

THE MANAGEMENT OF CHANGE

'It is difficult to talk of the ocean
to a frog who has only lived in a well'

(ancient Chinese proverb).

INTRODUCTION

To even begin to conceptualise the ocean of organisational changes sweeping Eastern Europe, in terms of the psyche of people, whose perceptions and behaviour have been constrained inside the well of communism for forty years, is a task of monumental proportions.

Equally, however, for those who have never been inside the well, it is a complex task to understand the starting point from which organisational transformation must be undertaken, and the inherent problems and constraints which the new order must, inevitably, inherit from the old.

The former state owned enterprises in the Czech Republic, together with organisations in the former communists countries, are facing fundamental changes in every aspect of their identity.

The external environment is changing dramatically at an unprecedented speed in almost every dimension, leaving voids of uncertainty and confusion in its wake. Politically, the old order has been swept away, and replaced by an embryonic political pluralism, which has yet to develop a supporting bureaucratic and regulatory legal framework.

Economically, the collapse of Comecon in 1989, immediately after the velvet revolution, saw most companies lose their major export markets almost overnight. When these companies were forced to look west instead of east for new markets, they found their own enterprises lacking in quality, technology, capital investment and funding (Brogan, 1990, p.112).

At a social level, the norms and values underpinning the behavioural patterns which had been followed for almost forty years were swept away. They have left in their wake a moral and behavioural abyss, and many new questions and challenges to be faced.

Internally, organisations faced similar paradigm changes in the fundamental reasons for their existence. Under the old regime, the main priorities for the enterprises were driven, primarily, by the dissemination and internalisation of the communist political doctrine, supplemented by the provision of a social support system comprising guaranteed

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full employment, housing, creches and basic medical care. The economic objectives of the organisation in terms of the output of goods and services were considered to be of secondary importance to these former goals. The fundamental external changes in the environment have necessitated a whole re-ordering of their strategic objectives. Additionally, behaviours precipitated by the priorities of the old regime, either in terms of positive support, passive compliance or subversive deviance, were no longer appropriate to the new challenges facing the enterprises.

The nature of the changing external environment, and the privatisation process have been analysed in the previous chapters. The challenges faced by the newly established enterprises will be dealt with in the chapter on organisational emergence. This chapter will focus upon the issues faced by the former state owned enterprises, as they attempt to undergo the metamorphosis from politically orientated, party driven behemoths to commercial, profit orientated enterprises.

The transformation process itself is very much at an embryonic stage with enterprises at varying stages in the transition from state-owned to privately owned companies. Consequently, at a micro level, there is an absence of any formalised frameworks and models with which to evaluate the effectiveness of the transformation process. Thus the

discussion in this chapter will focus upon primary interviews and observations together with a questionnaire analysis. Reference will also be made to the growing number of organisational case studies which are now being produced, specifically that of Mototechna, a case prepared by the author. Where appropriate to the analysis, behavioural and change models have been applied.

EXTERNAL ENVIRONMENT

The main external threats for these enterprises undoubtedly emerge from the loss of the old Comecon markets, and the collapse of the East European markets generally. This problem has been compounded by the fact that withdrawal of government subsidies and the price increases following liberalisation have precipitated a general recession, especially in the Czech Republic, where strict wage controls were enforced to control inflation. Additionally, the fall of the Berlin wall opened the markets of Central and Eastern Europe to the influx of goods from abroad, with which domestic enterprises could not compete, either on grounds of quality or availability.

Unfortunately, most of the former state owned enterprises were totally ill-equipped to find new foreign markets or to compete with foreign imports. They suffered badly from a lack of capital investment and new technology leaving the companies with obsolete, inefficient machinery. The

absence of technology was accompanied by a dearth of the technological training and know-how necessary to employ the latest technology effectively. These problems also manifest themselves at a wider level in terms of the absence of an effective telecommunications network. One only has to attempt to make a telephone call or send a fax from the Czech Republic during the day to appreciate the amount of time and energy that can be dissipated in such a pursuit (Kreberg & Schreiber 1991, p.250).

The enterprises are also significantly lacking in the knowledge of the skills necessary to compete in world markets. Before liberalisation, the concepts of marketing, management accounting and control, strategic planning and human resource management were alien to the state owned enterprises. These functions were either unnecessary, as a result of the way in which the economy was structured , or carried out by the Communist Party. Other major barriers to the ability of the enterprises to compete relate to the absence of a fully convertible currency, and insufficient knowledge of foreign languages.

However, if one were to ask the management of the former state owned enterprises, which are the three main problems facing them at this point in time, they would say: 'money, money and money'.

There is little doubt that the issue of lack of funding and the massive debts inherited by the enterprises from the old regime have left them technically bankrupt. Despite the support given to these enterprises by the Konsolidační Banks, as described in the previous chapter, most enterprises receive only sufficient short term loans to finance the working capital necessary to keep their business functioning. There is no question of money being made available for capital investment.

In response to these problems, enterprises are seeking joint venture partners to bring the funding, technology and know-how, which are crucial to their long term survival. Whilst seeking to address these new external challenges, organisations are, simultaneously, being faced with the many internal problems of privatisation, restructuring and change management.

INTERNAL ISSUES

Management of change - the human dimension

The success of the organisational transformation is dependent, primarily, on the commitment of the people within the enterprises to the acceptance and implementation of the proposed changes. The finest strategies for change will fail, if the structure and culture of the enterprise are not conducive to their implementation, or cannot be

adapted to accommodate them. This is not to say that the successful management of people will necessarily ensure that change is successfully implemented within an organisation. However, effective change management policies, in relation to human resources within the enterprise, are undoubtedly necessary prerequisites of successful organisational transformation strategies (Burnes, 1992, p.261).

Thus, the following discussion of the internal issues facing the enterprises in this chapter will focus, primarily, on the problems of change management in relation to the human resource dimension of the organisational transformation process.

The Process of Privatisation

The complexity of the process of privatisation was illustrated in the previous chapter. The role of management, as stakeholders in the process, was discussed with reference to the agency problem, which highlighted the conflict of managerial and organisational interests in respect of privatisation. This has led to much criticism on the part of senior management and directors, that middle managers were effectively slowing up the process of privatisation as much as possible to protect their own jobs security for as long as possible.

Whilst this is probably a valid claim, if one considers the amount of information and preparation required for the compilation of the privatisation prior to submission, this was indeed a major challenge for managers. Information was required on proposed strategic plans and structures together with financial information on such issues as asset valuation, and the overall financial situation of the enterprise for investment appraisal purposes. These were complex tasks to ask of managers who had never been required to undertake them previously, especially as these activities had to be undertaken within set time constraints. In recognition of some of the problems of privatisation, many enterprises employed the services of external foreign consultants. However, as the section dealing with foreign advisers will highlight, this strategy has proved to be something of a curates egg - good in parts (McQuade, 1992, p.6).

Additionally, against this background of ongoing problems concerning privatisation, managers are also expected to continue with their day to day management duties running the company. Indeed, part of the decline in GDP over the period of privatisation has been attributed to the fact that managers found it impossible to carry out both tasks simultaneously.

The difficulties of privatisation have not been made any easier by the questionable quality of management in the

Czech Republic, generally. This issue will be developed further in the section which focuses on managerial effectiveness within enterprises.

Foreign advisers

'Provided that someone in a dark suit and a red tie appears with a file, the business is done' (Representative of Zivostenska Banka, McQuade 1992, p.6).

Many enterprises have employed foreign advisers or consultants to assist in the process of privatising the enterprise, mainly, in terms of strategy formulation, asset valuation and restructuring proposals. The advisers, who come from many parts of the world, including the United Kingdom, Japan and the United States, are employed by leading management consultant and accounting firms, investment and merchant banks together with marketing and asset management firms. Apparently, some advisers also had the brief of finding appropriate joint venture partners. The role and effectiveness of these advisers has received a very mixed response. One cynical manager, who wished to remain anonymous, commented that their foreign advisers found potential joint venture partners by sticking a pin in the pages of a telephone directory.

There were, however, much more wide-ranging criticisms of foreign advisers. The general discontent felt by

enterprises concerning the advisers' role and contribution in relation to the privatisation process is well illustrated by the criticisms contained in the article by Scott McQuade (1992, p.6), in The Prague Post entitled: 'For foreign advisers: The Honeymoon May Be Over'.

The main criticisms relate to overcharging, and offering little expertise in return. More critically, advisers are accused of fooling Czechs into negotiating unfavourable contracts with potential foreign partners. It is further claimed that the international consulting companies charge western level fees, but send only junior staff to carry out the work. Moreover, even when experienced consultants are sent, some enterprises claim that an inordinate amount of time must be spent teaching the local laws, and business culture to them.

The claim that only junior consultants are sent is denied by Ernst & Young, a major international consultancy and accounting firm. They claim that, in fact, the problems in Eastern Europe are so complex that they demand the expertise of the most senior advisers. Additionally, it is argued that once foreign consultants have acquired local knowledge, it can be passed on through the consultancy services they provide to other enterprises. Moreover, the largest consulting firm in Prague, Price Waterhouse, with more than one hundred staff, employs more than two-thirds local staff.

However, Geoff Upton, the senior partner at Price Waterhouse, agrees that there are some ruthless western advisors who offer unskilled advice. This view is echoed by Toby Mitchell, central European manager for Visa International, who comments that:

'Western advisers now run the risk of biting the hand that feeds them' (McQuade 1992, p.6).

Despite the issues raised above, the presence of foreign advisors is likely to continue into the foreseeable future. However, the emphasis is likely to change, with the needs of the enterprises to that of providing consultancy services in the development, and implementation of strategic change. Foreign advisers are set to remain a major source of expertise and advice, at least, until the new cadre of managers acquire the necessary experience,and knowledge to internally manage their enterprises more effectively.

Restructuring

The issue of restructuring the enterprises is, crucially, at the heart of the challenges facing the enterprises. Clearly, the splitting up, and selling off, of these enormous enterprises is a fundamental prerequisite for survival. However, this major change, and the others previously outlined, are only as effective as the quality and commitment of the management and employees of the

enterprises who must carry them out. The cases of Siemens, the Kralovy Porcelain works and most importantly Skoda Pilsen illustrate the major problems in introducing fundamental restructuring policies, if they are opposed by the management and employees.

The process of restructuring, however, is a much more complex activity than simply redesigning an organisation chart. It is a process whereby job relationships in terms of accountability and responsibility are totally redefined. Moreover, due to the constantly changing global environment, successful restructuring no longer implies moving from one fixed state to another. The restructuring process must incorporate the change mechanisms and flexible thinking which will allow organisational forms to constantly adapt to a changing environment.

Such changes in thinking regarding organisation design and development present major difficulties for western organisations, which have been functioning in a changing environment for the last twenty years. How much more difficult will it be for the former state owned enterprises in the Czech Republic, as they emerge from a controlled, predictable environment into the ever changing prism of the Global market economy (Drucker 1992, p.128-137).

Quality of human resources

To the extent that the effective management of change in respect of the human resources is fundamental to the success of the transformation process, this presents a major set of problems for enterprise. Despite the universally recognised reputation held by the Czechs for technical competence (Ernst & Young 1994, p.37), there is little doubt that employees are de-motivated and unwilling to change: a situation exacerbated by the poor quality of management. For all transforming organisations, success will depend greatly upon the extent to which they can effectively formulate strategic plans, and support them with the necessary changes in structure and culture. These fundamental adjustments must take place within the enterprises, if the strategies are to be effectively implemented. This will necessitate major changes in the attitude and behaviour of employees, from the epithet of 'they pretended to pay us and we pretended to work', to a commitment to producing goods and services of a quality that will enable the enterprises to compete successfully in the domestic markets against foreign competition. These issues are especially noticeable in the fast moving goods industry, where the former stated owned soft drinks company, Zatka, is trying to compete with Coke and Pepsi (Kalina 1993, p.6).

To achieve such a change however, is a task of monumental proportions as the discussion on resistance to change, later in the section, will illustrate.

Managerial Effectiveness

'Lack of management skills remains a severe problem after years of passive resistance against central planning injunctions' (King 1993, p.8).

The above comment comes from a six country business survey of business attitudes carried out by Deloitte Touche Tomatsu International amongst foreign enterprises which have invested in Eastern Europe (King 1993, p.8). In terms of major business problems, it was rated a close fourth behind the banking system, staff language skills and telecommunications.

Concerns over the issue of management performance permeate most aspects of current enterprise research in the Czech Republic. The case study of Viktor Kozeny and the Harvard Group investment fund company discussed the problems of recruiting key managerial personnel for the organisation. According to Kozeny, the 'ideal' manager would have two to six years experience in the West, possess good managerial skills and have access to information from government and other official bodies. Clearly, given the recent history of the country, such people are very difficult to obtain.

The prime source of recruitment for the Harvard Group is government circles and the banking sector (McIntyre 1994, p.163).

The study of Ferox Manufactured Products, also, echoed similar concerns in respect of management ability. The U.K. joint venture partner of Ferox, Air Products and Chemicals, Inc. perceived the lack of depth of managerial talent as a problem. They felt that this was partly a function of the 'compartmentalized' structure of enterprises, which failed to identify managerial talent. The company, also, believes that it encouraged the lateral thinking skill, which is an important facet of effective managerial performance (Pearce & Carkt 1994, p.101). One could argue with the validity of this last comment. The chapter dealing with life under the old regime provided illustrations of management action in situations, where lateral thinking and innovative practices were necessary to ensure that the economic plan was fulfilled, at least on paper.

Another interesting perspective on the issue of managerial quality emerged from discussions between the author and Klaus Wohler, an agent of Volkswagen Skoda. When Volkswagen took over Skoda in 1991, they undertook a skills audit to ascertain the quality of the management they had inherited from the old regime. They found that a significant number of managers, especially at middle and

senior level, did not possess the necessary skills and ability to carry out their roles effectively. A wider skills audit found that many of the skills which the company sought were possessed by people who held much lower positions in the enterprises. There are various reasons as to why this could have been the case. Some people doubtless had the necessary intellect to appreciate the flaws and weaknesses of the system but could not become part of it by joining the Party. Alternatively, given the lack of differentials in earnings between management and manual employees, some people felt that promotion to management positions was not worth the effort.

The breadth of concern in respect of managerial ability is further echoed in the survey of selected managers within the Czech Republic, carried out by the author. The results of this research will be discussed in the later section dealing with managerial perspectives on organisational transformation.

The views of the author, after undertaking a series of lectures to Czech and Hungarian managers on the Brunel University MBA programme, are that the education system and past experiences of these managers have given them a skewed perception of the management role. Almost without exception, they possess a very high degree of numeracy. The benefit of this skill is that they quickly understand the mechanics, if not the concepts, of the numeracy led

management functions, e.g. accounting and operations management. The limitation of this skill is that it severely limits their managerial thinking. When seeking to identify enterprise problem areas on which to base their MBA dissertations, many managers focused, strongly, upon attempts to build some type of quantitative models of business problems. They believed that if they could somehow incorporate all the variables of the problems into this model, the outcome would be a prescriptive model for solving the problem. It was also believed that such a problem could be transposed to other similar problem areas. Clearly, such thinking is the product of a controlled environment of managed stability, and takes no account of either the informal 'deviant 'management activity in which most of the managers indulged. Moreover, it fails to incorporate the qualitative, human resource dimension of the management function. In this context, managers often react with confusion, when it is pointed out to them that, essentially, the management role is concerned with getting things done through people (Huczynski & Buchanan 1991, p.12), and not the application of prescriptive models. The challenges faced by management, when they do try to address the issues of managing people, are discussed in the section dealing with management of change.

Resistance to change - a foreign perspective

'It is like hitting your head against a brick wall of paper procedures and bureaucracy' (project manager, Unisys, 1994).

There is little doubt that, in terms of attitude to work, the communist regime encouraged employees to be de-motivated, inflexible, and ineffective. These responses are understandable in a system where reward was linked to political compliance, or in the case of financial bonuses, administered by the grace and favour of the manager. Moreover, where compliance and control were fundamental to the maintenance of political order, peoples' behaviour adopted an outward and to some extent internalised programmed response to the system or encouraged deviance from it.

The evidence of the problems faced because of the attitude and behaviour of employees is well illustrated, where East meets West. When foreign managed projects involve the employment of Czech staff, the extent of the problems becomes apparent. A prime example of the gulf in expectations, understanding, and behaviour between foreign and Czech employees is illustrated by the Unisys computer company project.

The objective of this project was to introduce a computerised banking system into the Czech Posta Banka. From the perspective of the Unisys project team, integral to the process of introducing the computer system was the revision and development of existing banking systems and procedures to take advantage of the many flexible facilities offered by the system. This is where the project encountered its first set of major problems. The bank had virtually no computerised systems. They operated purely on a paper and pencil administrative basis. When the computer systems were being developed employees expected simply to see the old systems replicated on computer networks. There was no apparent comprehension that computerisation would bring with it a major change in both the structure and culture of the organisation. Attempts at explaining the new systems and procedures were frequently greeted by the production of the paper administrative procedures currently in use.

The complete unwillingness to change was accompanied by an even greater unwillingness to take any managerial responsibility for decision-making. When trying to get a decision made, the project team were frequently referred to various people across and up the organisation. Even when the person apparently responsible for making the decision was identified, he or she was usually travelling abroad, taking advantage of the new found freedom or perks of liberalisation.

The problems for the project team did not end when the decision was made. If problems were encountered when the decisions were being implemented, people frequently denied that they had made them or claimed that they had been misunderstood. In response to this scenario, the team were required to ensure that all decisions were agreed in writing. Essentially, therefore, the goal of introducing the concepts of flexibility and change in respect of attitudes and behaviour were being defeated. The project was abandoned prior to completion due to the withdrawal of the Czech government. The reasons for this action were never satisfactorily conveyed to the project team. It was suspected, however, that the Czech government did not want to pay the fees for the work done on the project, and that they were likely to attempt to complete it themselves, when the team had been disbanded.

Management of change - problems and processes

The application of the context and content theories of motivation together with models of organisation culture change serve to illustrate the enormity of the tasks faced by enterprises in the area of managing change. The context theory of motivation emphasises the importance of identifying which rewards motivate people to work harder. The organisation can then be structured in such a way as to provide them (Huczynski & Buchanan 1991, p.54-63). However, the capacity of organisations to reward employees

by the provision of higher salaries, promotion prospects or greater job satisfaction, though job enrichment schemes, for example, is very limited. As regards remuneration, former state owned enterprises either have insufficient funds to pay more money or are precluded from doing so by the government wage-capping controls. Moreover, given the chronic overmanning in these enterprises and the labour shakeouts that are now taking place there are few promotion opportunities available. Finally, in the short term, the possibility of job enrichment is limited by the structural intransigence of many organisations, and the lack of financial investment in training and development which must underwrite such initiatives, if they are to be successful.

The context theories of motivation emphasise the role of expectations in changing behaviour together with the significance of the effort reward bargain, i.e. whether the reward one receives is worth the effort required to obtain it (Huczynski & Buchanan 1991, p.63-68). In terms of expectations, many of the initial expectations of people in the former Eastern Europe, both socially and organisationally, have been realigned sharply downwards in the light of the reality of events following liberalisation. Ordinary people find themselves in a situation of rising prices in relation to food, housing and energy. The shedding of labour has created a new environment of insecurity and uncertainty. Additionally, the influx of foreigners, advertising and the media have

presented images of a lifestyle which seems to be moving further out of the reach of ordinary people, rather than nearer, which was the hope of many ordinary people in Eastern Europe (Ballon 1993, p.3). As wages are controlled and prices rise people find themselves relatively worse off and, in terms of the effort reward bargain may justifiably consider that they should put in less effort to their work. They are, after all, receiving less of a reward in real terms. Thus the problem of motivating employees to work harder is no easy task in this already problem ridden organisational environment.

Ideally, enterprises are seeking to change the culture in organisations, and influence the values and beliefs of the employees in order to redirect their behaviour towards the achievement of the organisation's goals. Indeed, it is argued a change in the culture of these enterprises is fundamental to their long term survival. However, the problems of attempting to change the culture of organisations in this context can be highlighted by the application of Schein's model of organisational change (Schein 1985, p.237-243).

According to this model, culture change comprises a set of primary mechanisms which initiate the change process itself and a set of re-informing mechanisms which seek to imbed these changes. In terms of primary mechanisms, culture change is frequently initiated by changes in the

leadership. In many organisations in the Czech Republic, changes of senior management did take place, as the old nomenklatura were removed from power. However, they were frequently replaced by either relatively inexperienced managers or by recently promoted middle managers, who were still tainted by the old regime. As the previous case studies of Skoda and Siemens have shown, however, many of the new managers were either opposed to the restructuring changes, or obstructive to the privatisation process if they perceived that it threatened their self interest.

This creates additional problems is terms of Schein's model when one considers the importance of the role modelling aspects of the new leadership role. The leaders behaviour emits important change signals in terms of identifying those things now considered to be important in the organisation. Particularly, the leaders reaction to crisis situations is perceived to be a powerful signal of the changing culture. The concept of role modelling, as a means of changing behaviour, is unlikely to impact significantly upon employees, as a result of the behaviours inherited from the old regime. As previously described in the chapter on everyday life under the old regime, leaders were held in contempt in private but received lip service in public. Instead of responding to the examples set, people frequently sought out informal means of defeating and subverting them. It is likely to take a significant period of time before the institutional respect for

leadership and authority is re-instated within organisations (Mills 1993, p.6).

This problem of the absence of institutional trust could have significantly adverse effects on the future functioning of organisations. It is necessary to legitimise the sources of decision-making, delegation and authority within enterprise if they are to operate effectively. This will be difficult to achieve in the short term,where the programmed responses of people will be a lip service response to instructions. Subsequently, however, they may act purely in their own self interest, at the expense of operational efficiency.

Schein, like the motivation theorists, highlights the importance of human resource management initiatives such as the role of rewards in influencing behaviour. He further emphasises the importance of selection and dismissal criteria as a means of introducing new behaviours and values into the enterprise. The ineffectiveness of the financial reward strategies of state owned enterprises has already been discussed. However, the situation is further exacerbated by the fact that newly established and foreign enterprises are not constrained in terms of their reward strategies. Not only does this have a de-motivating effect on the existing employees, it means that the enterprises are losing their most highly qualified staff.

A major secondary mechanism for embedding and re-informing culture change relates to the issue of organisational structure. Managerial intransigence in this area has been highlighted previously. However, the extent of the problems goes further than simply obstructing the change process. The retention of the traditional structures and relationships in the new order will make the change process even more difficult. The intransigence of managers concerning change will reinforce the values of the old regime in the new order, thus undermining the change process further.

Overall, the Schein model provides an interesting framework for analysing the problems associated with organisational change, both culturally and behaviourally. However, the limitations to the applicability of the model suggests that it is relevant primarily in the context of incremental change within fixed paradigms, as opposed to paradigm change situations.

Education, training and development are seen as major long term strategies for effecting significant organisational change. Volkswagen, when recruiting Czech graduates, sends them to Germany for initial training. The plethora of MBA programmes in Eastern Europe, and the ever growing demand for more management education courses, are indicative of the fact that there is an awareness of this education need. However, one must question the value of seeking to impose

culturally defined management strategies and techniques onto an alien environment. This is especially true where the perceived wisdom of American management techniques, with its emphasis on short-termism, meets a system of ownership and control which favours the long term approach to organisational strategic planning (Beaumont 1992, p.25). This is not, however, to discount the educational value of Western experience and management practice to Eastern European countries, even if it is only to learn from the mistakes of the West. The role of education and training will be discussed in greater depth in the section dealing with human resource strategies for change.

Facilitators of change

The transformation process is re-defining the role of respective organisational actors and institutions together with the reallocation of power within enterprises. Thus, the effectiveness of the transformation will be greatly influenced by the willingness and ability of the key players and institutions to facilitate the process of change within organisations.

The major players, as they relate to the management of change, comprise the trades unions who have a significant role to play in the re-definition of the employment relationships and the future balance of power and influence within enterprises. The role of human resource management

is, also, seen as having a critical role in the strategic management of change within western organisations.

The framework of both individual and collective employment law will also be considered, in this context, as it has a critical role to play in defining the long term parameters and interactions of employment relationships within organisations.

The role of trade unions

'For forty years trade unions were the handmaiden of communism. Now, it is a very difficult task to re-gain the trust of the people' (trade union official, April 1993).

The role of the trades unions under the new order in the Czech Republic appears to be paradoxical in its nature. The analysis of its role, however, could prove enlightening in terms of the future direction of the political transition.

The lack of faith in the unions, apparently, reflected in the above statement is a widely reiterated comment amongst management and employees in Czech enterprises and echoed in the views of selected managers involved in the informal survey carried out by the author. There is little doubt that the stigma of communist collusion and co-operation bears heavily on the newly reformed trade union movement.

This has been evidenced by both the falling membership numbers and the negative views of trade unions expressed by union members in a survey in April 1994, which was carried out by the Institute for Public Research. It showed that only 53% of the economically active population and 36% of all people aged over fifteen were trade unions members. This reflected a decline of 9% since April 1993. The major areas of decline were in the services industries and the private sector where only 22% of employees were trade union members. On the other hand 60% of blue collar workers and 67% of employees in state industries declared membership of trade unions. Whilst 69% expressed confidence in their workplace union leadership, only 46% supported the national leadership (Orenstein 1994, p.10).

It is argued that there are various structural reasons for the low union support from members and the population generally. This is due partly to the limited disruption to social peace experienced during the transition process, as a result of the relatively low unemployment within the Czech Republic, and a falling external debt situation. Moreover, the government's successful attempts to control inflation have minimised the fall in living standards for the majority of the population. However, if and when the government permits the market exit mechanisms to function through the operation of the bankruptcy law, it remains to be seen how far these conditions can be maintained, and the impact it will have on the role of the unions.

Additionally, the centralised structure of nation-wide branch unions is relatively unchanged from that which operated under the communists. This has led Orenstein (1994, p.9-10) to conclude that:

> As a result of this smooth transition.....the reformed chamber of trades unions suffers from a lack of popular legitimacy and therefore the inability to mobilise support.

The paradox inherent in the position of trade unions arises because of the perceived power and influence they hold, as a result of their membership of The Council of Economic and Social Agreement of The Czech Republic. This Council was founded in October 1990 and based upon a voluntary agreement between the government, trades unions and the employers association. On an annual basis, the council negotiates a General Agreement which sets out general wage agreements for the year. The objective of the meetings is to achieve consensus on the basis of agreement between its members. Although all agreements reached are binding on the members of the Council, they do not have the force of law.

When considering why a 'radical' government should include the unions in such an agreement, there is an interesting structural argument which states that the Czechs have a consensual political culture, characterised by non-confrontational decision-making. Peter Rutland (1992, p.122) supports this view by arguing that:

> The Czech government's acceptance of corporatism can be attributed to the underlying consensual nature of Czech political culture, a willingness to replicate the labour institutions of neighbouring Austria and Germany, and Klaus' own style avoiding direct confrontations.

There is some validity to this statement, in so far as the new commercial code, which regulates business activity, draws heavily on the German model of business law. Additionally, the insider model of corporate governance reflects strong elements of the German model, with its underlying corporatist philosophy. On the other hand, the government has not set the framework for trade union involvement and participation in a legally binding prescriptive framework, as the German model. Neither the agreements of the Social Council nor collective bargaining arrangements carry the force of law.

The view is also expressed that, given the lack of popular support for the unions, the perceived influence at macro level is all they possess. This gives the government a high degree of influence over the trade unions, as it can threaten to dissolve the Social Council. This would leave the unions with no role and few vestiges of real power and influence in the new order.

In the longer term, the future role of trade unions, both at a macro and enterprise level, will be determined by the nature of the legislation, accompanying institutions, and

custom and practice that will shape the nature of industrial relations. It is in these areas that the true extent of the representational strength of the unions will become apparent. In terms of the legislative framework, as previously stated, there is no evidence to suggest that the German legalistic model of trade union power and rights is being incorporated into the collective employment laws which are still being formulated, as at Autumn 1994, the completion date of this doctoral study (Orenstein 1994, p.10).

Moreover, given the system of indirect maximum wage controls that are determined and applied at a national level there has been little opportunity for unions to apply the legislation in practice through the application of the collective bargaining process at enterprise level.

The Labour Code, which will be discussed in the section dealing with individual employment law, allows for consultation and notification of trade unions in respect of matters relating to redundancy. However, there is little in the Code as yet to determine the extent to which trade unions will be permitted to participate in the system of corporate decision making. It is difficult to forecast what the long term role of the unions will be at this point in time. The re-definition of the nature of the employment relationships and the system of industrial relations is at a very early stage. Collective employment law is either

based on modifications to that which existed under the old regime, or is still in the process of being reformulated.

The human resource management function

'Those in the personnel department were the Party's mouth. The stink of the Party's dead body is all over us' (Personnel Manager, Ferox Manufactured Products, Pearce & Carkt 1994, p.99).

The view expressed above is one which pervades much of organisational life in the Czech Republic. In the former regime the personnel function was controlled, directly, by the Communist Party. It was responsible for the selection and reward mechanisms as well as retaining secret files on employees. It was seen as the major executor of communist policy and practice within the organisation. This inherited mistrust has created significant problems for enterprises, as they seek to transform themselves into commercially orientated enterprises (Kieuzun 1991, p.10-12).

It is almost universally recognised that human resources are the major asset of most enterprises. As such, they should be led, motivated, rewarded, and developed, in such a way as to contribute to the achievement of the strategic goals of the enterprise. Thus the development of effective selection, appraisal, reward, motivational and development

strategies are crucial to the achievement of this goal (Blyton & Turnbull 1993, p.5). Additionally, effective human resource management policies and practice have a critical role to play in the change process within organisations. Many western organisations are now recognising the importance of human resource management in the management of change. Thus, if Czech companies look to the West, to observe those instances of good management practice, where change has been successfully implemented, they will observe the weight that is given to human resource management policies, and the role of the human resource management function.

In attempting to compare the role of the human resource management function in the East with that of the West, (Prokopenko 1994, p.150), has adapted the Eshoulam and Baird model of the relationship between the stages of human resource management which links the maturity of the enterprise and the main HRM components (See Appendix I). The dividing line between East and West reflects some of the inherited organisational problems outlined above. It can be seen that the functional growth of the human resource management function is still very much in its embryonic stage, partly as said as a result of its past association with the Communist Party. The main role of the HRM function is that of an administrative adjunct to the management of the enterprise. The function is not yet integrated into the fabric of the enterprises, although

this could be due to the compartmentalised bureaucratic structure and culture of the former state owned enterprises. Additionally, the model illustrates that, potentially, the main strategic facilitator of change, the human resource management function,is organisationally marginalised.

Thus, enterprises are faced with a very complex dilemma in respect of human resource management. How can an organisation implement forward looking HRM policies and procedures, and introduce strategies of change, with all their concomitant problems and uncertainties, if the major vehicle for achieving this, has no credibility in the enterprise? Indeed, the personnel manager from Ferox continues:

> There would be uproar if I developed a succession plan - it would be seen as the restitution of the old 'cadre reserve system' by which the Party controlled positions' (Pearce & Carkt 1994, p.99).

To some extent this problem has been mitigated by the use of external consultants to assist in selection, designing reward systems, management development and culture change. Nevertheless, given the fact that the most effective change and development processes should be developed from within, where they are 'owned' by those who are affected by them, the use of external consultants is not necessarily the optimum approach. However, in the short term, it may be

the most effective means of initiating the change process (Burnes 1992, p.248).

It is likely that, in the long run, management development and education programmes will precipitate changes in the attitudes of people towards the HRM function. Although such programmes can assist in resolving the problem, educators, like the author, who lecture to managers on human resource management and the management of change, find that the problems in relation to this function go much deeper.

Firstly, managers have little practical experience of the way in which human resource management functions, in terms of its strategy, policy formulation or implementation. Because of the complex value laden nature of HRM, educating managers in this area is a two-fold function. It requires the imparting of knowledge in terms of understanding what the human resource management function does, and how it can contribute to the change process. Additionally, it requires changes in the attitudes and perceptions of managers in terms of how they manage people, and indeed what their overall role as managers should be.

In the face of 'western style' human resource strategies, which emphasise the importance of empowerment, communication, motivation and involvement, there is the frequent criticism that these policies are inappropriate.

Management have argued that organisations have not changed sufficiently for those strategies to be applicable. It is at this point, that the author, whilst lecturing, advised the managers that they must undertake the active roles to begin the change process. If they all wait for change, and do not take the initiative in implementing it, advises the author, the change will not happen, because, if they do not take the initiative, no-one else will. This is where the attitudes and perceptions of managers must begin to change, if the transformation of there enterprises is going to have some chance of success. The Berlin wall may have come down, but its spectre remains fixed in the psyche of many managers.

Thus, to develop the role of HRM successfully in the Czech Republic requires much more than descending upon organisations with external consultants and an HRM policy and procedure manual. In re-defining the HRM role, people are being asked to blot out the past negatives of the old function, to learn new techniques of management, and to rethink their whole value system in respect of the nature of their employment relationships, both vertically and horizontally. This is, indeed, a major challenge which, at best, will only achieve success over the longer term. Even then, it will require a major commitment, both financially and psychologically, on the part of the enterprises involved.

EMPLOYMENT LEGISLATION

The legal redefinition of the relationship between employers and employees will be fundamental in shaping the nature of the transforming enterprises within the Czech Republic. Whilst it is still very early in the revision and reformulation of employment law in this area, it is possible to detect some trends, which may assist in the prediction of the future nature of the employment relationship within organisations.

The main legislative act governing the employment of people is The Labour Code. It was first devised in 1966 but has been updated, frequently, to reflect the ongoing transformation processes. Thus, whilst the Labour Code continues to be amended, the most recent Trades Links (1993, p.2) changes comments that:
'its ''socialist spirit'' is still evident'.

Essentially, the legislation seems to be very protective of employees rights, but more circumspect in terms of their application. All employees are required to receive a written employment contract, which is valid for an unlimited period of time, unless otherwise specified. Any subsequent modifications must be agreed to by both the employer and employee, in writing. All employees have a three month trial period at the end of which their employment is deemed to be permanent.

The legislation, also, stipulates a minimum wage (2340 Czech crowns for 1994). In order to control inflation, there is wage capping legislation whereby wage increases of more than the government set maximum can lead to penalties.

The extent of employment protection is a useful indicator of the relative power of the employer and employee within any enterprise. As regards the power of the employer to dismiss the employee, this is not clear from the legislation, which states that:

> if failure to meet (the organisation's) work requirements takes the form of unsatisfactory work results, the employee may be given notice for this reason, only if during the last twelve months, the organisation called upon him in writing to eliminate the deficiencies.....within a reasonable period of time' (Trade Links 1993, p.49).

In the case of 'a serious violation of work discipline' the period is six months. The legislation also makes provision for instant dismissal in the event of gross misconduct (Trade Links 1993, p.50).

In the event that the organisation serves an 'invalid notice', i.e. an alleged unfair dismissal, the organisation is obliged to pay compensatory wages up to a period of six months. At the end of that period the organisation can apply to the courts to have it reduced or stopped completely. The legislation also outlines the provisions

for redundancy and redundancy payments (Trade Links 1993, p.58-59).

It is difficult to evaluate the extent to which recent amendments to the Labour Code will affect the transformation process of organisations. The Labour Code itself was a product of the communist regime, and was never applied in practice. There was no official unemployment, and virtually no-one was ever sacked, as discussed in the chapter dealing with everyday life in the old regime, the state would have insisted that you employ someone who is even less efficient than the employee being dismissed.

Under the new regime, overmanning still continues and dismissals are still being carried out under the redundancy provisions. Indeed, it is highly unlikely that the invalid severance provisions of the legislation have ever been invoked. The impotence of the legislation is indicated by the fact that the legal and institutional arrangements necessary to implement it are absent.

Thus the current state of employment legislation is not really helpful in attempting to determine the redefinition of the employment relationship in the transforming organisations at this point in time. However, commentators in the recent revisions to the Labour Code have indicated that it is likely to be overhauled in the next few years.

by the provision of higher salaries, promotion prospects or greater job satisfaction, though job enrichment schemes, for example, is very limited. As regards remuneration, former state owned enterprises either have insufficient funds to pay more money or are precluded from doing so by the government wage-capping controls. Moreover, given the chronic overmanning in these enterprises and the labour shakeouts that are now taking place there are few promotion opportunities available. Finally, in the short term, the possibility of job enrichment is limited by the structural intransigence of many organisations, and the lack of financial investment in training and development which must underwrite such initiatives, if they are to be successful.

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According to this model, culture change comprises a set of primary mechanisms which initiate the change process itself and a set of re-informing mechanisms which seek to imbed these changes. In terms of primary mechanisms, culture change is frequently initiated by changes in the

leadership. In many organisations in the Czech Republic, changes of senior management did take place, as the old nomenklatura were removed from power. However, they were frequently replaced by either relatively inexperienced managers or by recently promoted middle managers, who were still tainted by the old regime. As the previous case studies of Skoda and Siemens have shown, however, many of the new managers were either opposed to the restructuring changes, or obstructive to the privatisation process if they perceived that it threatened their self interest.

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It is only when this process has taken place that a meaningful evaluation of the nature of the employment relationship can be undertaken. However, given the corporatist interventionist tendencies of government in its reform programme, and the extent to which it draws upon the German model of legislation, it seems likely that any future employment legislation will be highly protective of the rights of employees.

A MANAGERIAL PERSPECTIVE

INTRODUCTION

In order to ascertain a wider Czech managerial perspective on the issues of organisational transformation outlined above, questionnaires were distributed to nine managers over the period form 1991 to 1993. It must be stressed that no wide reaching generalisations can be developed from the questionnaire findings. The quality and quantity of information varied between respondents. However, the views expressed do serve to highlight the main organisational problems. The function of our questionnaire survey analysis is to provide insights into the situation facing enterprises from the perspective of those managers who work within them.

The questionnaires asked people to identify, broadly, what they perceived to be the main strategic objectives, and to

consider the enterprise in terms of its strengths, weaknesses, threats and opportunities, in relation to the possible fulfilment of these goals. Additionally, the earlier respondents were asked to comment on issues of decision-making and control. Questions concerning the role of HRM in terms of the role of unions and issues of recruitment, promotion and reward were posed to all the managers surveyed, in order to ascertain the potential nature of management of change in respect of human resources.

The questionnaires will be analysed on the basis of nine responses. Four were received from the previously state-owned service sector, all of which were completed in 1991. The remaining five responses were gathered from the manufacturing sector over the period 1991-1993.

The constraints concerning the wide use of questionnaires as an research tool in former communist countries has been discussed in the chapter on methodology. However, over the period from 1991 to 1993 the author lectured to two groups of management delegates, numbering eight and seven respectively, on a post-graduate management programme. The author took the opportunity to elicit the views of the delegates concerning the changes which were taking place within their enterprises. Of the fifteen distributed, nine were completed and returned. It is possible only to speculate upon the reasons for non-submission of seven

questionnaires. These reasons probably comprise pressure of work, failure to see any personal benefit accruing from completing the questionnaire, and the legacy of communism.

SERVICE SECTOR RESPONSES

The responses from the service sector were from the main import and export companies, Strojimport, Strojexport and Skodaexport respectively. As the questionnaires for these specific enterprises were completed in 1991, prior to privatisation, they focus upon the general issues of change only and do not deal directly with the problems of privatisation. These are dealt with in the case study at the end of this chapter, and mainly in later questionnaires.

The main role of these enterprises was to sell Czech made goods in foreign markets, and import foreign goods. All such transactions were required to go through these agencies. They were also responsible for carrying out all the accompanying financial transactions related to the sale and purchase of goods and services. The numbers employed in these enterprises ranged from four hundred and fifty to eight hundred employees. These current levels of staffing were at significantly reduced levels from that of before 1989. In one enterprise the numbers had been reduced from one thousand two hundred to four hundred and fifty.

Strategic objectives

Only two of the four respondents saw the main objectives of their respective enterprises in terms of turnover and profit. The others saw their main objective as the continued provision of the same service to industry, which it had supplied under the old regime. The retrenchment focus or defensive strategies implicit in the answers of these respondents may be a function of the fact that they have few diversification options open to them. They provide a specialised and ultimately redundant service to companies, which are already starting to develop their own import and export markets. The only competitive advantage which these organisations possess is their specialist knowledge and network of contracts in those countries to which the Czech Republic traditionally exported, and from whom it imported goods. However, given that these were primarily third world or other Eastern Bloc countries one could question the value of the networks they possess. However, whilst it is likely that such enterprises will fade away in the longer term, the current employees who filled in the questionnaires are attempting to formulate strategies to ensure the survival of the enterprise in the foreseeable future.

Organisational problems

Three respondents recognised the strengths of the

enterprises in terms of their specialist knowledge and contacts, whilst highlighting the same critical internal weaknesses. These were identified, primarily, in terms of the quality of management together with the attitude and motivation of the workers. The other main structural weaknesses relate to too much bureaucracy, and overmanning. The forth respondent saw the lack of company experience in working with private enterprises in the Czech Republic as a major weakness.

The main managerial criticism concerned the fact that the top and middle management in these enterprises and had not changed after the fall of communism. Consequently, the same informal power networks of the old guard continued to operate in the enterprise. This was felt to have created much bad feeling in the organisation. There was also concern that the structures of the organisation has remained unaltered and that this was presenting a major obstacle to change. In terms of threats to the organisation, one respondent predicted imminent bankruptcy, if major structural changes were not undertaken immediately within the enterprise. As regards the quality of decision-making and control, three of the four respondents were very critical of their organisations in terms of the quality of decision-making, the dissemination of decisions and the nature of control. The forth described rather than commented on the nature of decision-making in the company.

Human resource management issues

Concerning HRM issues, none of these respondents felt the necessity for union involvement in their enterprises. This is probably part of the negative backlash experienced by unions as a result of their overt collusion with the communist regime. The recruitment issue was not relevant, as the enterprises are currently downsizing. Wage awards and increases continued to operate along the same principles as those of the old order. Wage differentials remained very low, and salary increases were based upon length of service. Concerning the criteria for promotion, three of the four respondents cited length of service. The fourth, however, stressed that the main criteria for promotion continued to be 'acquaintance and friendship with the leaders'.

The major external threats to the enterprises were perceived in terms of the world recession, and the indebtedness situation of companies within the Czech Republic, which are very much the general areas of concern for most enterprises.

Future prospects

Concerning the future, the main opportunities for the companies related to the greater freedom they had to function as economic enterprises. One respondent was

hopeful that their department of forty people might be able to split from the main company, and form a consultancy enterprise in its own right. This strategy is, probably, the only long term viable course of action for these now, potentially obsolete import and export enterprises. However, informal discussions between the author, managers and entrepreneurs in a variety of enterprise and industries have indicated that, in learning about foreign markets and contacts abroad, for many of them the import and export corporations are still the main source of information at least in the short term.

MANUFACTURING SECTOR

The questionnaires from the manufacturing sector came specifically from mining and geological exploration, from the brewing industry, and from petrochemicals. The questionnaires relating to geology, brewing, and one of the petrochemical enterprises, company A, were completed in 1991, whilst the mining questionnaire, and remaining petrochemical enterprise, company B were completed in 1993, after the commencement of privatisation. The numbers of employees within the various companies ranged from four hundred in the geological exploration enterprise to 10,000 in petrochemical company A. The respondents held a range of managerial posts within the organisations within which they were employed.

Strategic objectives

In terms of the manufacturing responses completed in 1991, the geology manager saw the achievement of higher profits as a main objective of the enterprise, whilst the brewery manager perceived that an improved position in the world market was critical. Both indicated some awareness of the commercial objectives organisations must pursue, if they are to survive as competitive privatised entities. The petrochemical manager of company A regarded the main objective of the enterprise as the successful privatisation of the enterprise. One would, perhaps, have expected the director to have the vision to see beyond the immediate transformation stage and think in terms of some kind of commercial organisational objectives. However, this response may be an example of the 'agency' problem of management, which was discussed in the chapter dealing with privatisation.

Their objective was the adoption of their privatisation proposals as opposed to other projects submitted, not because the management proposal was more beneficial for the company, but because it protected or enhanced the position of the management within the enterprise.

In terms of the later responses, the mining department head saw the main objectives of the industry in terms of mining and selling coal. The manager of the petrochemical company

B saw the ability to commission and complete processing plants as the major objective of the organisation. The mining manager included a commercial dimension in terms of sales, whilst the petrochemical manager of company B appeared to be production led in his strategic thinking. This view is in line with the common phenomenon inherited from the previous regime, that the objective is to produce anything irrespective of the commercial viability of the project. This was a reflection of the situation where the political and social objectives superseded commercial considerations.

Organisational issues

As regards the main strengths of the relative enterprises, in keeping with much of manufacturing industry generally the technical skill level of the workforce was considered to be very high. From the perspective of the brewing industry this was re-enforced by the one hundred year old reputation held by that enterprise.

The geologist and the brewery director recognised similar weaknesses in their organisations, in terms of obsolescence of equipment and facilities. Only the brewery manager identified the educational background and ability of lower and middle managers as a weakness, although the manager of chemical company A did recognise that the level of competence in the enterprise, generally, was deficient.

This may be a function of the differentiated nature of the respective businesses. The geological exploration company had a higher degree of technical and professional staff. Consequently, the relationship between managers and workers would be based upon levels of technical competence. For the production director in the brewery, position in the hierarchy would probably be the main differentiator. Additionally, the management roles in the respective organisations would also differ considerably. The threats to both organisations were similar in relation to indebtedness and lack of money generally.

As regards the later respondents, the problems for the mining industry lay with the worsening economic conditions due to the withdrawal of government subsidies, and the loss of the Slovakian markets, when the country split in 1993. For chemical company B, the main issues for the enterprise related to the recurring themes of indebtedness and obsolete equipment. Like the mining industry it too has suffered from the loss of the Eastern European markets after 1989. In common with the service sector responses, all the later respondents in the manufacturing sector identified the quality of management as a major problem within their respective enterprises.

Privatisation issues

From the perspective of the geologist, the fact that their

organisation had been separated from the main state owned company in 1990, and was about to be privatised, represented a challenge and an opportunity. The brewery production director, on the other hand, perceived the unknown future ownership pattern of the enterprise as a threat. Given the priority accorded to privatisation by the petrochemical director, this is clearly a major priority for the enterprise. The mining industry was to remain within state control, and consequently, privatisation was not an issue. Petrochemical company B had submitted its privatisation project with an ownership structure which comprised: 3% to the local town of Hadrek Kralovy, 19% to foreign investment, and 87% to be sold under the large privatisation scheme. The respondent did not comment on the difficulties of preparing the project.

Decision-making and control

Concerning decision-making in the respective organisations both the geologist and the petrochemical manager of company A indicated that all decisions were made at the top of the organisation by the senior management. In the case of the geology exploration enterprise, the main criticism of decision-making was that it was very slow, and thus, less effective than it could be. The brewery production manger felt that decision-making in their company was not very effective, but getting a bit better. As regards improving the quality of decision-making in the enterprise, the

geology manager stressed the need for better communication, faster implementation, and greater co-operation between different levels of management. The brewery production manager, however, linked possible improvements in decision-making to changing the structure of the organisation, thus perhaps reflecting a wider perspective on the scope of change required within the previously state owned enterprises.

Concerning decision making in petrochemical company A, it was noted that new top management had been appointed whom the manager believed were really interested in the future. He still considered decision-making to be relatively ineffective within the organisation, believing that good information systems were required to improve the communication flow.

The question of who should control the enterprise was not commented upon by the geologist. The brewery manager felt, however, that control should rest with the board of directors and the new major shareholders. Similarly, the manager of chemical company A expressed the view that the board of directors should control the organisation.

Human resource management issues

Opinions concerning the role of the union differed slightly between respondents, which may be a function of the

differing industries within which they are employed. The geologist saw a role for unions in terms of representing the opinions of workers, but not in the area of scientific problem solving. The brewery manager, however saw the union in terms of a more traditional role within manufacturing, i.e. protecting workers and their rights. This was reflected, also, in the views of the petrochemical company A manager, who believed that unions had an important role to play in the enterprise.

The mining manager saw a major role for unions to play in seeking to re-establish the conditions and advantages the miners had enjoyed before 1989. He was of the opinion, however, that overall, unions were decreasing in significance. The manager of petrochemical company B did not believe that the unions were playing a very constructive role, which he believed should be to help the prosperity of the company.

There appeared to be little recruitment taking place within all the manufacturing respondent companies, with the exception of petrochemical company B. They were still recruiting from their own apprentice schools and universities and by the use of advertising.

From the perspective of HRM practices within their respective enterprises, the basis of promotion, in those companies where promotions were still taking place,

appeared to have changed from the traditional communist criteria of compliance, to that of education, experience and ability. Payment levels, also, appeared to be a function of these criteria, although, at the time of completing the questionnaires, the government was operating a strict incomes policy.

As all the respondents were on management training programmes, where they were requested by the researcher to complete the questionnaires, clearly, their respective enterprises were demonstrating commitment to management education and development. The most structured training and development programme was operated by petrochemical company B, which had its own training centre. It had recently set up a language school, and had sent twelve managers on MBA programmes. Within the mining industry, the majority of the development activities comprised technical training for miners and some language training for managers.

Finally, the opportunities for the geological company were seen in terms of for offering a broader range of exploration services to assist in the solution of ecological problems, ideally with the co-operation of foreign enterprises. The brewery manager also saw the possibility of joint ventures as opportunities for the company to explore wider markets. The link with joint ventures was clearly identified by major enterprises as a

employment. However, in what size and form it will remain is not yet clear.

CONCLUSION

For the most part, the broad commonality of views expressed in this informal survey serve to reinforce the organisational transformation problems highlighted in this chapter. The concerns over privatisation, restructuring, lack of investment and the problems of indebtedness were especially prevalent, together with concern over the quality of management. As the discussion on the management of change has shown, however, it is a major step from awareness of these problems to implementing the strategies which will help to resolve them.

MOTOTECHNA - AN ENTERPRISE IN TRANSITION

INTRODUCTION

To provide a focused perspective on the challenges and opportunities faced by the transforming state owned enterprises a case study of Mototechna, the state owned monopoly responsible for the sales, service and distribution of motor vehicles, has been developed (Mills 1992, p.2-8).

The major problems facing Mototechna at the start of the free market period are typical of those faced by the extremely large state controlled monopolies which characterised the communist era, and must now undergo a dramatic transformation if they are to survive within the new political and economic order. The major challenges for these organisations concern the establishment of a new corporate identity together with the development of a supporting organisational structure. This will require the formulation of a new set of strategic goals together with a compatible corporate culture, through which to implement these changes.

COMPANY PROFILE

The researcher first visited Mototechna in April 1992. At this time the company was made up of fourteen divisions based upon product lines each of which had their own functionally based organisation to support it. There was a director at the head of each division who reported to the director of the overall company.

In 'the old days', Mototechna had five hundred retail outlets for the purchase of cars and spare parts together with thirty-one service centres located throughout the former Czech and Slovak Republics. It also had two major plants for the repair and renovation of vehicles both of which were located next to the Skoda production plants.

Before the liberalisation of 1989 the company employed 10,000 staff, and had a sales volume of 100 Bill Kcs. (£1 = 50Kcs, at 1992 conversion rates).

By the end of 1991, the numbers employed had fallen to 6,000 with an annual turnover of 5 Bill Kcs. which, given price increases of 100%, was equivalent to 2.5 Bill Kcs. in real terms.

Situation before liberalisation

In common with other state-owned enterprises, the strategic priorities for the company were primarily political, then social, with economic issues being of significantly less importance. Nevertheless, the failure of the central economic planning mechanism, which led directly to the development of the black market, was especially prevalent in the car industry. There were long waiting lists of up to two years for the purchase of cars, unless one was a member of the nomenklatura, or could pay black market prices.

As with most state-owned companies, the quality of management was questionable, due to the fact that all appointments and promotions were undertaken on the basis of party loyalty rather than qualifications. Additionally, even if education and training were considered as selection criteria, access to higher education was contingent upon

party membership and influence anyway. Moreover, as the content of education programmes was strictly controlled, it is not unreasonable to assume that the quality of the management emerging from such a system would be poor.

This complete distortion of any kind of economic or commercial order meant that by the end of the communist regime Mototechna found itself with:

- a debt of 5 billion Kcs. mainly tied up in obsolete stock
- major re-investment requirements
- poor quality and ineffective management
- a workforce with a psychologically limited perception of consumer service and choice
- no meaningful financial measures of asset values, performance costs or profitability
- and with the collapse of the communist regime no markets in which to sell their goods

Post liberalisation situation

After liberalisation, much of the responsibility for shaping the future of the organisation rested with the newly appointed director, Mr Zdenek Skarda, the previous director having been dismissed at the time of liberalisation in 1989, together with other members of the nomenklatura.

Mr.Skarda, at sixty-two years old, belonged to the cadre of individuals who held positions of influence before the normalisation of 1968 and were re-instated after liberalisation. Key appointments were now also being given to the younger generation, who were never committed to the old regime. In many positions of authority there is an absence of the 'tainted generation' who were perceived as having supported the old regime. It is difficult to evaluate the wisdom of such changes. Whilst some, although by no means all, the functionaries of the old regime doubtless had the ability to perform well in their administrative roles, the fall from grace of the political system they supported and their subsequent loss of credibility may well have made it impossible for them to continue to carry out their duties effectively.

Whilst an able man, the director was old and tired, having suffered at the hands of the former communist regime, a fact which is probably applicable to other men in similar positions. The dilemma of this situation lay in the fact that Mototechna, and other similar organisations on the threshold of significant changes and challenges, required dynamic and energetic leadership.

These challenges were identified as:

- the formation of Mototechna as an independent corporate entity by the successful completion of privatisation process

- the formulation of appropriate strategies to achieve success in the new political and economic order as it impacts upon the car market
- the restructuring of the organisation in order to achieve the company's strategic aims
- an improvement in the quality of the management and the workforce to fulfil the strategy

The privatisation process

The company has been involved in all dimensions of the privatisation process - restitution, small and large privatisation.

Restitution was a major problem for the company. The enterprise was created in 1949, partly through nationalisation of existing retail and service outlets, which had to be returned to the descendants of the original owners. Due to the large number of outlets involved, it has proved very difficult to identify the original owners.

Many of the retail outlets originally controlled by the company have been returned to private ownership by means of auctions through the small privatisation. The funds generated by the sales have gone to reduce the company's debt burden.

During the course of 1992, the plans for privatising the company, under the large privatisation scheme, had been formulated with the aid of foreign consultant and were in the process of completion for submission to the Ministry of Finance for approval. The organisation hoped to find a suitable foreign partner with whom to set up a joint venture. There has been some interest shown from various organisations, but the situation was still uncertain at this time.

Moreover, it was further complicated by the fact that some potential joint venture partners were waiting until the recession and restructuring process led to further reductions in the value of the company's assets. They would then be able to purchase a share in the company at a much reduced price.

Nevertheless, the proposed strategy for Mototechna discussed below will be clearly linked to the ultimate privatised status of the organisation together with that of a joint venture partner.

Proposed strategy for Mototechna

In common with all state owned enterprises, Mototechna lost most of its East European markets with the collapse of Comecon in 1989, whilst simultaneously experiencing a fall in domestic demand caused by the recession following price liberalisation.

The changes in lifestyle precipitated by the transition to a market based economy have also had a significant impact upon the Company. In Western Europe, it is reckoned that the average life span of a car is five to six years. In the former Czech and Slovak Federal Republic, it was twenty years. This was due partly to the fact that, for the majority of people, it was impossible to purchase a new car as a result of demand overhang, the effect of the black market, and the priority given to Communist Party members in car purchase. Moreover, spare parts were very cheap in comparison to the price of new cars, even if the latter were available for purchase, and often they were not.

Because of the poor quality of manufactured goods and services, as well as the perennial shortage situation, the socialist lifestyle was based on self sufficiency. People repaired their own cars or bartered goods and services with someone who could. Consequently, as a result of the long lifespan of the cars, and correspondingly higher demand for repairs and spare parts, the sale of these items comprised a high percentage of company revenues.

In the current regime, however, where businessmen must be more geographically mobile if they are to promote their products and services, cars are considered vital for daily use. Thus, the growing tendency is to purchase newer, more reliable cars. This has led to a change in the revenue earning structure of the company towards increasing revenue

from sales. However, during the transition period, there is still the demand for service and spare parts.

The Volkswagen purchase of Skoda created problems for the enterprise economically, commercially and, to some extent, politically. The strategy adopted by Volkswagen in respect of pricing and distribution created the seemingly paradoxical situation of a shortage of Skodas in the former Czech and Slovak Federal Republic, similar to that experienced under the communist regime, albeit for different reasons.

The reason for this paradox is that Volkswagen was exporting two-thirds of the Skodas it produces in order to gain hard currency. The Skodas available for sale could be purchased domestically for DM 7,000, whilst the same Skoda was sold in Germany for DM 13,000. Not surprisingly, a significant number of dealers were buying the cars to re-sell in Germany at a significant profit. Thus, Mototechna saw the market for spares being reduced still further, as the newer cars are sent abroad.

In this post liberalisation regime, Mototechna was seeking to answer the fundamental strategic management question - What business do we want to be in? The Company decided that it wanted to be in the business of importing and distributing new vehicles, used cars and spare parts.

Consequently the Company proposed to:

- import new cars for sale in the former Czech and Slovak Federal Republic, they appreciate that demand at the moment is low but would look to profiting from this strategy in the longer term
- Import and sell good quality second hand cars, ideally twelve months old or with less that 20,000 Kms mileage
- continue to sell and distribute Skoda cars through much reduced dealer network of sixty-five retail outlets in the most geographically advantageous locations
- import spare parts for the cars they import and distribute them through their two wholesale distribution centres to independent retailers

The strategy of the Company was not formulated in sufficient detail to enable the management to specify the source of the vehicles, the quantity required or the location of the network through which they will be distributed.

The Company decided that the service outlets they currently owned did not fit in with this business strategy. Two possibilities for the disposal of the outlets were considered:

1. They should be auctioned off under the small privatisation scheme referred to earlier and the funds used to reduce the Company's debt.

2. The outlets should be leased to existing employees.

If the first option were selected, it was felt that this would allow Black Market money to purchase the outlets. Because of their prime locations the purchasers might well choose to convert them into hotels.

The Company considered this to be unacceptable, as it would not only prevent the existing employees from having the opportunity to purchase the businesses, but it was likely that they would lose their jobs, if the businesses were converted to other uses. Moreover, it was possible that in the longer term Volkswagen may wish to purchase the whole service network. Thus it was decided that Mototechna would retain ownership of the outlets but lease them to employees to operate and manage.

In common with the other state enterprises Mototechna found itself with a major debt liability due to the soft budget constraints and subsidies of the old regime. With liberalisation, such subsidies ended, as the government sought to effect the transition from a command based to a free market economy. Enterprises had to begin quantifying the value of their assets and stock, and identifying costs and sources of revenue. For Mototechna this meant that in October 1991 it had a debt of 6 Billion Kcs. the majority of which was tied up in apparently unsaleable stock.

By February 1992, the debt had been reduced to 1 Billion Kcs. This feat has been achieved by:

- the continued sale of retail outlets under the small privatisation scheme
- selling stocks of spare parts at reduced prices through any available retail outlets
- exporting obsolete stock to countries with mainly obsolete vehicles, i.e. China, The Commonwealth of Independent States (the former USSR) - where the Commonwealth of Independent States was unable to provide hard currency a trade barter system was set up through the Slovak distribution centre where the company accepted anything in trade that it could re-sell for a profit in the former CSFR.
- certain stock locations complete with stock were auctioned under the small privatisation process
- much of the selling was achieved through a network of individual and personal contacts, which operated informally throughout the previous regime

A continuing major problem for Mototechna was the fact that they needed the foreign investment and expertise of a joint venture partner if they were going to survive. But the major debt burden made the Company a less attractive proposition for foreign investment. The government stated that the valuation of the company for the purposes of joint venture should be discounted by the amount of the debt.

However, Mototechna felt that this would be giving their company away.

Restructuring the organisation

The process of restructuring had already begun in 1990, with the appointment of the new director of the enterprise.

The reduction in staff had been achieved by:

- natural wastage
- retirement
- employees staring up their own business
- compulsory redundancy

The staff reductions took place throughout the network at all levels within the organisation. At the head office the number of staff was reduced from two hundred and twenty to seventy employees.

Ultimately it was proposed that the company would comprise a small head office, function together with separate strategic business units. The main objective was to design a structure that would be flexible, efficient, and minimise costs.

The major constraining factors for Mototechna and many similar organisations in attempting to survive and grow in the new economic order are lack of technology and the poor quality of staff.

The historical legacy of appointments and promotions based on political criteria has left in situ managers who were not competent to carry out the duties required of them. Mototechna took the opportunity offered by the labour reduction strategy to dismiss some of them but a significant number still remain.

Even those within the organisation who have the potential ability to carry out the duties do not have the experience, skills or training to enable them to operate effectively. Already, however, management training and development initiatives were underway to provide training in the previously absent disciplines of accounting, marketing, strategic planning and human resources management.

Beyond the education process at skills level, however, lies the much more complex and long term re-education process of changing people's attitudes, expectations and behaviour. It is arguable that it will take at least a generation for people to rethink their values and beliefs.

Nevertheless, in the interim, it falls to the manager to motivate people for whom the concept of reward related to effort is still alien. Rather than see the organisation as a provider, employees must begin to perceive themselves as contributors to the final outcome. For many people, it was comfortable in 'the old days' to have all independent thought and decision-making removed, and to rely on

external bodies to fulfil all their perceived needs. Now such decision-making and responsibility has been devolved back to individuals, who do not know how to exercise it.

All of these concerns will impact upon the ability of Mototechna to survive. The issue is exacerbated by the fact that the most able employees are leaving the state enterprises where wages are still state controlled to join the new foreign and private companies which can pay much higher salaries. The other major area of concern is the lack of language training amongst employees, especially training in English. The majority of the management education programmes being run by the various institutions require a knowledge of English.

CONCLUSION

In 1992, Mototechna saw unfolded before it many challenges for survival and opportunities for success, as it faced an unknown future. However, this organisation was more fortunate than most in that the motor industry in the Czech Republic had already attracted much foreign interest and activity. Consequently, Mototechna seemed to have a better chance of long term survival than many of the other former state enterprises. However, it remained to be seen if the organisation could survive the current recession, the influx of foreign competition, the lack of investment and the long-term restructuring of the economy which must be

undertaken if the Czech Republic is to achieve a level of economic performance comparable to that of Western Europe.

POST SCRIPT

By the completion of the period of doctoral research in November 1994, Mototechna had witnessed a further period of major political upheaval and economic change. On 1st January 1993, the Czech and Slovak Federal Republic peacefully dissolved itself into two separate sovereign states. In 1993, Mototechna became a much leaner organisation, when Volkswagen purchased the Mototechna service outlets. In the same year the company was privatised in the second wave of privatisation, using the voucher method. However, Mototechna is still seeking a suitable joint venture partner to provide the funding and expertise which the company requires in order to ensure its long term survival and met its strategic objectives.

CONCLUSIONS

In reality there are as yet few conclusions which can be drawn from the process of transformation within the former state owned industries in the Czech Republic. There are, at best, the shoots of tentative beginnings from which one might try to predict the likelihood of their flourishing in the future, or being overwhelmed by the enormity of the change process.

Externally the environmental challenges facing organisations are immense. They are made even more complex by the fact that organisations must undertake fundamental internal paradigm changes, whilst seeking to re-establish an ordered relationship with an environment which is changing at a rate, and in a fashion, which could not have been predicted in the relatively recent past.

The analysis suggests that there is a broad common awareness of the problems facing the privatised enterprises. The challenge, however, is to convert awareness to understanding of the problems and subsequently to ownership, internalisation and implementation of the strategies which can help to resolve them. Unless this fundamental process takes place within organisations, these enterprises will fail to adapt to the new environment, become obsolete and ultimately cease to exist. Indeed, as the previous analysis of Skoda Pilsen has shown, some organisations are perilously close to this terminal state.

There are, however, many major challenges to this change process. As concluded in the chapter on privatisation, the new order will create new winners and losers in terms of power and influence. Clearly, whilst the current changes may be avidly sought by those who would gain such power, it is rarely, if ever, voluntarily relinquished by those who hold it now, and are likely to lose it. Hence, in the survey analysis, there was deep discontent in the

organisation which had experienced no real changes in their management structure since liberalisation. Additionally, informal discussions between the author and some of the younger generation have indicated that there is an increasing feeling of hostility towards those who have succeeded in remaining in power.

The analysis has also shown the deep seated embeddedness of the behaviours and attitudes developed under the old regime permeate all aspects of both the enterprises, and the bureaucratic institutions with which they are required to interact. This latter issue is developed in more detail in the later chapter which deals with organisational emergence. In this context, the role of the bureaucracy will be shown to be a major constraining factor on the change process.

The litany of external structural deficiencies faced by enterprises is well documented. However, once again, it is the ability, opportunity and willingness of those in powerful positions to turn awareness into action at all levels of the society.

The preceding analysis has shown that this is not the case. At a government level, the continued interventionist macro and micro economic policy of government is without doubt a major constraining factor on the change process. It is a major block to the reconstruction and market realignment of

enterprises, which must take place, if the transformation process is to continue moving forward.

Within the enterprises themselves, there are undoubtedly major limiting forces for change, also, in terms of the quality of management and negative attitudes and motivation of employees towards internalisation and implementation of the change process. In this regard, the application of some analytical models of motivation and change have illustrated the complexity of motivating people to change their behaviour.

However, even if enterprises were to formulate policies to assist in this change process, the major enabling vehicle for such changes within companies, the human resource management function, has neither the credibility nor, frequently, the expertise to carry out the job. Moreover, at a legislative level, the fact that the new framework for employment law has not yet been developed is another major drawback. It is difficult for enterprises to change, if they do not have a definition of the employment relationship they must establish between themselves and their employees.

On the credit side of the balance sheet, however, there is no doubt that the privatisation process is forcing managers, to learn about western style strategic management and restructuring issues. The use of foreign advisers and

consultants could be an aid to the introduction of more modern advanced organisational forms by moving directly from state owned bureaucracies to flexible core and peripheral organisational modes. This could be achieved without requiring the enterprises to pass through some of the evolutionary phases, which took place within privately owned enterprises over time in market based economies.

Additionally, if one considers the role of trade unions, who generally treat change negatively and with a high degree of suspicion, the extremely limited influence exercised by the unions in real terms has not proved to be a major block in this area.

There are many proposed strategies being developed to address some of the issues which have been discussed in this chapter. Once again, however, policy makers meet with the difficulties of dealing with a unique situation for which there are no precedents, comparisons or guidelines. At the core of the change process, however, must lie the re-education of the people carrying it out, in order to change their attitudes and behaviour. Within this context, the role of education and training is of core significance.

It must be ensured, however, that the communicators of change, though the education system, possess the necessary expertise to carry out the re-education process. The content of the programmes should seek to inculcate new

values systems and behaviours, which are congruent with the national cultural context within which they are set, and the changed states to which they are seeking to aspire. At best, inappropriate or conflicting messages through the re-education process could retard the progress of the change and, at worst, could create more problems for implementing the change process than they solve.

This is especially so in relation to the philosophies of management, which are so culture specific. As the process of re-education must unlearn old values before new ones are instilled the duration and complexity of this exercise, as well as the other range of problems outlined above, will doubtless limit the potential success of the change process in respect of the current working population. The long term success of the change process, in terms of the attitude and behaviour of the people who must implement it, will lie with the quality of education, as it relates to the value systems and concepts which are passed on to the next generation.

In other national contexts, this has been an evolutionary process which has developed over many generations. The uniqueness of the Eastern European system is that they are required to make conscious choices in the development of value systems and behaviours. This task is made more complex by the fact that there are many additional uncontrollable influences shaping the formulation of new

value systems, including the lawlessness of 'wild west capitalism,' which are capable of distorting beliefs and behaviours.

These behaviours have manifested themselves in the area of social concerns by such newspaper headlines as:

'Sleaze endangers the soul of Prague's velvet revolution' (Green 1993, p.12).

To the observer who has witnessed the transition process over the past five years, the 'sleaze' is highly visible in the centre of Prague, especially in the area of Wenceslas Square. On her fist visit to Prague in 1991, the author met colleagues at the most popular meeting point in the city - 'under the rump'. This refers to the area at the top of Wenceslas Square, under the statue of King Wenceslas, seated on his horse. In more recent visits, the researcher was advised that this area of Wenceslas Square, and indeed, the surrounding areas were no longer safe enough for such meetings to take place after dark.

Additionally, at a political and economic level, the arrest for bribery of Jaroslav Linzer, the director of the coupon privatisation scheme, in October 1994, has sent shock waves to the core of the whole privatisation process, and all that it symbolises in terms of the new order (Bloomberg Business News 1994, p.1).

The above trends suggest that in the short term at least, the latter scenario is gaining prominence amongst those with the power and influence to shape the future development of Czech society.

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APPENDIX I

THE DIVIDING LINE BETWEEN HRM MATURITY LEVELS OF EASTERN AND WESTERN EUROPEAN COMPANIES

Stages/components	I Initiation	II Functional growth	III Controlled growth	IV Functional integration	V Strategic integration
Management awareness	Awareness of functions administrative role	Aware of function's broad role but not committed	Aware, often frustrated at fragmentation	Cooperative and involved	Integrated
Management of personnel function	Loose, informal, often none	Personnel manager, programme orientation, manage conflicts among subfunctions	Personnel executive. Business orientation, measurement, goals	Function orientation. Long-range planning, line/staff relations collaborative	Company orientation consistent/integrated with business strategy
Portfolio of programmes	Basic salary and benefits administration, basic record keeping	Many new programmes added responding to business needs, revisiting basic programmes	Management control, budgets. Portfolio reevaluated in measurable terms, advanced compensation	Inter-disciplinary programme. Focus on goals. Productivity, change management, flexible planning	Cultural, environmental scanning long-range planning emphasis on effectiveness
Information technology	Manual employee profile, record keeping	Automated salary and basic profile. Advance record keeping	Automated personnel work, mainly profiles, tracking, basic statistics	Utilize computer for projection, planning, analysis and evaluation	Long-range planning. 'What if' questions linked to personnel and organizational data
Personnel skills	Administration, routine and housekeeping	Functional specialists	Increased professionalism in function and managerial skills	Integrating activities, skills in systems, planning and analysis	High-level involvement in organization, macro skills
Awareness of internal and external environment	Not aware	Aware of environment and corporate culture but do not incorporate them into functions	Aware of risks and opportunities in environment, address some in programmes.	Aware, react, incorporate into planning environmental changes	Systematic search for environmental impacts, take active role in decision-making
	EAST		WEST		

Source: Prokopenko, J. (1994) The transition to a market economy and its implications for Eastern Europe. In Kirkbride, P. Human Resource Management in Europe London, Routledge, p.150

CHAPTER 11

ORGANISATIONAL EMERGENCE

> By pursuing his own interest (the individual) frequently promotes that of the society more effectually than when he really intends to promote it. I have never known much good done by those who affected to trade for the public good.
>
> Adam Smith

IMAGES OF CHANGE

During the author's numerous trips to the former Czechoslovakia and later to the Czech Republic over the period from 1991 to 1993, some of most visible signs of the transition to a market economy have been the mushrooming of small retail and service outlets. There is now a proliferation of fast eating places in, at any rate, Prague, together with an ever increasing number of small electronic, electrical and sports goods retail outlets. Their growing presence has added bright spots of colour to some of the formerly fine buildings now defaced by pollution. They have transformed Wenceslas Square from a faceless sombre street to a multicoloured - some might say gaudy - backdrop against which many foreign visitors wander up the hill to view the statue of King Wenceslas. The streets off Wenceslas Square are also lined with the ubiquitous street traders whose stalls and vans are to be found in ever increasing numbers in all areas of urban

concentration.

Travelling through the suburbs, one's eye is taken by the odd flash of colour proclaiming the existence of a hairdressing salon or fast food pizza outlet. The images of imported Western culture contrast vividly with the surrounding, grey, faceless rows of depressing apartment buildings that stretch endlessly into the fog of a murky horizon polluted by the emissions from the nearby industries.

The heightened visibility of this growing number of small retail establishments is outweighed only by the advertising messages blazoned across the city trams exhorting one to fly British Airways, buy National Panasonic, and smoke Marlboro cigarettes. Additionally, while descending the moving staircases to the metro, one's visual senses are now assaulted by the range of advertising placards suspended from the ceiling skimming the heads of the downward moving passengers.

Progress in terms of the provision of service is also evident in The Hotel Crystal in Prague, where the author always stays when visiting the city. At the first visit, the reception area contained only a smoke- filled television lounge. The unadorned walls were wood-lined reflecting the seeming communist predilection for 1960s decor. There was no porter assistance and a distinct lack

of taxis in the vicinity of the hotel. Although there was a telephone in each bedroom, this could only be used for contacting reception. All external telephone calls, domestic and international, had to be made from a bright red telephone in the reception area. Payment for calls was operated on the basis of an honesty system on the part of the user.

The bedrooms were functional, but the quality of the toiletries in terms of towels and soaps, such as they were, left much to be desired. The hotel provided a virtually inedible breakfast, and did not serve dinner. There was a snack bar which opened from 10 a.m. but served a limited range of snacks from a menu written only in Czech. On each floor of the hotel there was a kitchen with tea and coffee making facilities but no room service.

How then has the Hotel Crystal responded to the transition process? There is still no porter service, but a line of taxis is permanently available outside the building. The downstairs T.V. room is now a very smart hotel shop selling crystal and glass. The wooden walls are adorned with showcases of luxury goods which visitors can purchase in Prague. The red telephone was initially replaced by two pay phones in reception. There is now a pay phone on every floor. The snack bar sports a T.V. monitor as do lounge areas on each of the floors. The rooms remain unchanged although the visitor is now greeted by piped, popular music

in the lift. The range of toiletries has now been extended to include towels instead of napkins and Hotel Crystal wrapped soap. The breakfast remains almost inedible, and sullen serving staff will argue that tea and coffee are hot, despite the obvious evidence that they are cold. Thus, there still remains an absence of any service culture as regards customer care. Staff serving on reception will come forward to serve a customer, whilst they are smoking. Even in the Forum Hotel, the most expensive and well appointed in Bratislava the author had to wait until the receptionist finished a telephone conversation with a friend, and rinsed a coffee cup, before being given the room key.

This chapter will seek to analyse the changes underlying the scenarios outlined above, and seek to evaluate the challenges and constraints facing entrepreneurs wishing to set up their own businesses. It will consider also the wider problems and opportunities associated with the development of the service sector. In order to appreciate the complexity of this phenomenon of organisational emergence, it is important to understand why the previous regime was characterised by a virtual absence of small business activity and a service sector.

ABSENCE OF ENTREPRENEURIAL TRADITION

The core of the explanation lies with the underlying

philosophical rationale of communism, which believed that property should be owned collectively by the people. In practical terms this led to the forced nationalisation of all business activity in Czechoslovakia, when the Communists seized power in 1948. Marxist theory also stated that wealth was generated, primarily, through mass production in the manufacturing sector rather than the development of small business and a service sector. It was argued, therefore, that the most efficient means of organising enterprises was on the basis of large monolithic state-owned organisations. Moreover, as the direct factory workers were perceived as contributing in the most significant way to the generation of wealth, they received a comparatively higher rate of pay than those engaged in the professions. Consequently, people were discouraged from pursuing professional service orientated careers, which led to the concentration of all business activity into a single state-owned enterprise for each major industry classification.

The fundamental tenet of price control, which was basic to the functioning of economic policy, was also a disincentive to the development of small business and service activity. It took away the opportunity for would-be entrepreneurs to obtain those rewards, in terms of profit, which they seek as compensation for the risks they take by being self-employed.

As Brabant (1990, p.121) notes:

> State ownership.....inhibits venture capitalism. For that there must be the possibility for individuals in principle to found their own firm, and, hence, to assume the full risk of succeeding or failing with their own or borrowed capital.

Additionally, in ideological terms, the notion of service carried with it the concept of master and servant which was considered an anathema in terms of the communist doctrine of equality. Much service activity was regarded as parasitic and reminiscent of capitalism.

Thus, by the end of the period of communist rule virtually all economic activity was concentrated in the monolithic state-owned behemoths. In terms of service activity, there was no expectation of any standard of behaviour or quality of delivery, as power lay with the provider instead of the recipient (Ericson 1991, p.13).

A full analysis and evaluation of the communist regime in Czechoslovakia from 1948 to 1989 is contained in Chapter 8.

The general problems faced by both emerging and transforming organisations have been dealt with in Chapter 11 on Organisational Transformation. This chapter will focus on the emergence of new organisations, and discuss those critical areas which impact most directly upon the

development of entrepreneurial activity.

ORGANISATIONAL EMERGENCE

The immediate post-1989 Velvet Revolution period has seen a mushrooming of small businesses and a flurry of entrepreneurial activity. People are taking advantage of the new business opportunities which have been presented by the transition to a market type economy. The number of entrepreneurs registered by industry is shown in Appendix I.

EMERGING PATTERN OF ENTREPRENEURIAL ACTIVITY

A profile of the status of selected legal forms of organisational entities is shown in Appendix I and will be analysed in order to identify the major areas of entrepreneurial activity in the region. For the purposes of this discussion, analysis of the data will concentrate upon private entrepreneurs and companies and partnerships, as these groups contain most of the new companies.

A private entrepreneur is defined in the Commercial Code, the legislation which regulates business activity, as: 'a person conducting the activities on the basis of a trade authorization (Živnostenské oprávění")' issued by the Trades Licensing Office ("Živnostenský úřad").

Organisations defined as Companies and partnerships comprise:

'a person (individual or an entity) incorporated into the Business Register' (Posustova 1993, p.40).

The private entrepreneurs comprise 89.5% of all registered companies within the Czech Republic. This is due, primarily, to the fact that many new businesses are operating on a very small scale, where the owner is frequently the only employee. Furthermore, it is considerably easier for a private entrepreneur to obtain a licence to carry out trade than for a company to be incorporated in the business register. The procedures and problems associated with obtaining licences and business registration will be discussed below in the section dealing with legislative complexity.

The pattern of business activity for private entrepreneurs and businesses and partnerships is similar in terms of concentration of activity.

22.5% of the new private entrepreneurs have concentrated their efforts on trade and repairs; 22% have set up business in manufacturing; 20% are engaged in real estate. R&D and commercial services comprise 18.4% of new entrepreneurial activity.

Some concentration of activity in the area of trade is to be expected as the privatisation of the economy unleashed a pent-up demand for consumer goods. The growth of real estate activity is a direct result of the re-establishment of private property rights and the policy of restitution. Thus, liberalisation has created many opportunities for new businesses to meet this increased demand in the retail sector. For example, the concentration of entrepreneurial activity in the repairs and manufacturing sector is due partly to state companies reducing their number of employees. Some of those who have been made redundant are setting up their own manufacturing facilities with the skills that they have learned. Additionally, the provision of repair and maintenance services to the owners of the newly-purchased consumer durable have encouraged some people to set up their own businesses.

Service activities comprise 55.94% of all new entrepreneurial activity, whilst almost 80% of the partnership and companies' classification is in the service sector. Moreover, the concentration of companies and partnerships in the trade and repairs section is even more concentrated than that of the private entrepreneurs and comprises 40% of the total of registered companies. The growth in real estate and commercial services indicate the demand for accountants, lawyers and other professionals required to support a demand economy. Those who have set up in this area have mainly adopted the Western

organisation form of partnerships. Additionally, partnerships have been formed to enhance available financing for business ventures. The limited liability companies have probably chosen this form to limit their financial exposure in an economy where the spectre of indebtedness and defaulting on payment is ever prevalent. The finance and insurance sectors of business activity still represent only a small area of service activity comprising 0.17% and 0.91% for the entrepreneurs and companies respectively. This is to be expected given the lack of expertise of professionals and the relatively underdeveloped state of the financial system generally. There is a lesser degree of activity in the catering and accommodation areas than might be expected, given the influx of tourists and business travellers to the area. This limited growth is probably a function of the protracted restitution policy of the government and the poor state of much of the accommodation when it is finally privatised. The problems of property acquisition are discussed below.

Whilst the above statistics provide a valuable overview of the current trends and patterns of entrepreneurial activity, they must be treated with some caution. In terms of categories, they do not include the street vendors, nor do they include those numbers of people who have set up in business without going through the registration procedure.

Moreover, the systems and procedures for the collection and collation of statistical data are new and relatively untried. Consequently, the findings should be interpreted as general trends rather than accurate statistical data. Finally, in terms of analysis, the overall pattern of entrepreneurial activity is incomplete insofar as there is no statistical information available on business failure rates. However, once the banking system has developed greater expertise in the financing of business activity, and the Bankruptcy Law is fully operational, this information should be available.

ENTREPRENEURIAL PERSPECTIVE

Within the context of this pattern of activity what are the main problems and challenges faced by entrepreneurs, as they seek to develop and capitalise on the new business opportunities, which are now presenting themselves.

> Laws work against each other; taxes fail to encourage small business; the court system works with no precedents; and the bureaucracy is nearly impossible.
> (Auster 1992, p.10).

To what extent is this view valid? The following analysis of the main problems facing entrepreneurs will seek to answer that question.

LEGISLATIVE COMPLEXITY

'What we have now is an Austro-Hungarian Socialist hybrid. It has to change'.
Roman Paul, Director of the Entrepreneurs Association of the Czech Republic (Hawker 1993, p.10).

How accurate is this assessment of the newly-established commercial legislation? It is generally accepted that, integral to the transition process and the stabilisation of political pluralism, is the establishment of an effective legal framework which will regulate economic affairs, protect property rights, and provide a means of legal redress and support for business activity.

In the Czech Republic the main pieces of legislation, so roundly condemned by Mr Paul, which regulate this area of business activity for entrepreneurs, are the Trades Licensing Act and the Commercial Code.

The Trades Licensing Act regulates the conditions under which an entrepreneur may engage in trade together with procedures for monitoring compliance with the Act. All business activities require licences with the exception of state activities and professional bodies such as physicians, pharmacists, and barristers. These occupations are regulated by professional bodies through the process of examination and setting of performance standards. It is

envisaged that a commission will be set up to evaluate the fitness to practice of those who do not possess the necessary qualifications, but are currently engaged in professional activities.

All individuals who wish to engage in trade must be a minimum of eighteen years of age, legally competent and honest in that they do not have a criminal record and have not recently been declared bankrupt.

The Act classifies trade into two main categories:
Notifiable trades ("Živnosti ohlašovací") which an individual can undertake upon the submission of a notification of trade to the appropriate trade licensing office ("Živnostenský úřad") which issues a trade licence to the applicant.

Licensed trades ("Živnosti koncesované") which can only be undertaken if an individual has the appropriate professional qualifications. Certain trades can only be undertaken when the individual has been vetted to ensure that there has been no involvement with the secret police, the people's militia, and has no had no leading role in the Communist Party. A trade licence is then issued.

Trades are also classified according to their activities, i.e. commercial, manufacturing and service rendering trades. Individuals must acquire a separate trade licence

or certificate for each activity to be undertaken, which leads to a very complex licensing procedure (Posustova 1993, p.61).

The Commercial Code outlines the basic legal rules concerning the rights and obligations of entrepreneurs in the conduct of their business. Under the Code, both a private individual or a company may be classed as an entrepreneur. The Act defines four categories of entrepreneur:

- those conducting activities on the basis of a trade certificate or licence;
- persons incorporated into the Business Register;
- enterprises which undertake business on the basis of special legal regulations;
- those engaged in farming who are entered into the appropriate list under special regulations.

The code also defines four legal classifications of business entity:

- a general or unlimited partnership ("veřejná obchodní společnost") where all partners are jointly and severally liable for the business debts of the firm;

- a limited partnership ("komanditni společnost") which can have a combination of general partners and limited liability partners whose financial obligations are

restricted to the amount they have invested in the firm;

- a limited liability company ("společnost s ručenim") where the liability of the company members for the organisation's obligations is limited to their investments in the company (the limited liability company is a very popular legal form amongst small and medium-sized firms);

- a joint stock company ("akciová společnost") which is defined as a company whose capital stock is divided into a given number of shares of a certain nominal value. The company is liable to the extent of its assets if it fails to fulfil its obligations, but the shareholders do not bear any such liability (Posustova 1993, p.42-45).

From a management perspective, an important aspect of the joint stock company is the supervisory board which supervises the activities of the directors. The board comprises a minimum of three members elected for a maximum of five years. Two-thirds are elected by a general meeting of the shareholders and one-third by the employees if the firm has more than fifty full-time employees (Posustova 1993, p.42-45). This system is based upon the German model of industrial democracy, with its related implications for the role of management (Mills 1991, p.80).

The joint stock company is considered to be a more complex legal entity, best suited to large organisations who wish to trade on the stock exchange. It is likely to be the business form adopted by most of the state enterprises which are currently being privatised.

All of the above defined businesses are required by law to be incorporated into the Business Register which is defined as follows:

> A public list in which the appropriate register court enters such information on business entities and individual entrepreneurs as required by the law. Entrepreneurs whose business does not take the form of one of the legally defined business entities do not require to be entered into the Business Register.

The registration process requires that all businesses seeking to register must produce the founding document of the company. Such documents can become exceedingly complex, and usually require the services of a lawyer or specialised agency. The documentation must also be authenticated by a public notary.

It is also a legal requirement in the code that, prior to registration, the business must open a bank account in which is deposited an amount of initial capital as specified in the founding document. Money can only be

drawn from the account once the company has been incorporated.

The actual incorporation process requires the submission of a petition to the registration court to have the business entity incorporated into the companies register. The company must then notify the tax authorities of its existence and advise the social security authority of any Czech nationals employed by the company (Posustova 1993, p.41).

In addition to the above legislation, companies are subject to a plethora of local by-laws and restrictions which operated under the previous regime, and are still applied today in an ad hoc fashion by local officials. The main areas of complaint in relation to the legislation concern:

- the licensing process
- the arbitrary use of by-laws by local officials;
- the complexity of the business registration process.

The Licensing Process

'Entrepreneurs must wade through a labyrinth of government licences and court approvals to register a new company.' (De Luce 1993, p.8).

An example of the complexity of the situation regarding licences is well illustrated by the example of Jan Svehla

who wished to open a dry cleaning store using machinery imported from Italy. He required separate licences for working with gas, electricity, undertaking building renovations, buying and selling (Auster 1992, p.9).

Mazacek wryly comments that:
'If he (the entrepreneur) wants to make a hole in the wall, he has to have a licence for it.' (Auster 1992, p.9).

Professors Robert DeFillippi and Charles Wankel (1993) in their case study of "An American Entrepreneur in the Czech Republic" outline the bureaucratic problems faced by Greg Husek, a young American who is seeking to start up a new business.

When attempting to get the amount of electricity to his flat increased to accommodate the needs of his home office, he met the full force of an intransigent unhelpful bureaucracy. He visited the appropriate office of the bureaucracy and was given a special form which had to be completed by an electrician. On returning to the appropriate department, he was advised that he should have been given two forms. Husek was now required to complete two additional forms, and take them to yet another government office in Prague. When he reached this office, he was advised that it would take at least a month to

process the forms. After much shouting and remonstration, mainly in German, his form was stamped and the process completed.

The Czechs with whom Greg discussed the scenario pointed out that, normally, one would have been expected to bribe the clerks in question to expedite the process. DeFillipi and Wankel (1993, p.450) state that:

> Some lawyers or other people hired by entrepreneurs to help get a new business underway pay bribes on their own initiative that they consider necessary to get the business started.

According to the case, it would appear that the motto of Prague entrepreneurs is:
'If you want to move fast, you have to pay for it'.

On a second occasion, he was advised that the stamping of a form concerning an equity loan would, once again, take 30 days. It appears that the thirty days is the minimum official length of time for most official activities, and one must purchase quicker service in processing documentation by means of bribery.

The general operation of the Trades Licensing Act is considered by some experts to be in need of a general overhaul, despite the fact that it has only been in operation since the beginning of 1992. The Trade Licensing

Act differentiates between one hundred and thirty-four different trades with an additional forty-two defined by other pieces of legislation. It is based upon the German "medieval" model of trades licences. Schmidt (1993, p.6) quotes the example of a mechanic who requires one licence to practice as a mechanic, a second to repair transport equipment, a third for installing funiculars and yet a fourth for fixing their motors. Trades, like renting out videos, require:

'A school leaving examination in the specified field and three years of practical experience.'

Although it is accepted that the law is not as strictly enforced as it might be, there are many trades which could be liberalised and some for which no trade skill is required at all.

The process is further complicated by the fact that it is necessary to carry out all the procedures required to apply for a new licence, even when one is merely applying to change it.

There is growing pressure in the business community and the government to change this legislation.

'There is no need for delaying the implementation of more responsive laws.' (Schmidt 1993, p.9).

The issues concerned with the implementation of the Licensing Act will be discussed further in the section

below which deals with bureaucratic inefficiency.

Application of By-laws

As well as the complexity of the licensing process, entrepreneurial activity is subject to a whole range of local by- laws inherited from the old regime. The situation is made worse by the fact that they are applied by local authority officials in a totally arbitrary, inconsistent fashion.

Amy Auster (1992, p.9) cited a typical example of this situation in The Prague Post. An entrepreneur who purchased a formerly state-owned restaurant in the Old Town undertook some refurbishment of the premises before opening for business. Two days after the restaurant opened a hygiene official closed it down. He claimed that a restaurant of that capacity required larger kitchens, and twice as many toilets. When asked why this regulation was only being enforced now, the official replied, 'because now this is a private restaurant'.

Business Registration

In terms of legislative requirements, the process of business registration is one of the major areas of contention for entrepreneurs. The whole process is complex, intensely bureaucratic and is in effect a social vetting process.

Entrepreneurs must incur a substantial degree of expense if they register. They must hire lawyers to prepare the extensive and complex paperwork required to obtain registration, which of course requires a substantial amount of time, effort and money. The status criteria requires that the applicant should be vetted and cleared under the Lustrace Law, which was passed to ensure that individuals in government and senior business positions had no past links with the secret police or high level activity in the Communist Party. This, in effect, makes it a "political cleansing" process.

Due to the backlog of applications coming through, the final registration period can take from three to five months depending on the district. Ultimately, the final decision lies with the whim of the district court judge.

Clearly, this vetting process influenced the comments made by Roman Paul. As concerns the Austro-Hungarian barb, this may be partly due to the fact that the legislation itself is a combination of Austrian, German and European Community law, rather than a legal system devised internally. The legislation is also intensely bureaucratic in terms of its implementation, which harks back to the ruling bureaucracy which imposed the Austro-Hungarian political legal system upon the Czechs and Slovaks in the 19th century. Additionally, the complexity of the regulations creates a climate where entrepreneurial

activity is controlled and suppressed as opposed to nurtured and developed. This belief is further re-enforced by his comments that:

'Premier Václav Klaus and economics minister Karel Dyba would like to control every company, and draw profits from all of them.' (Hawker 1993, p.10).

The implementation of the business register, like the licensing procedure, lends itself well to the influence and control of a corrupt and inefficient bureaucracy.

BUREAUCRATIC INEFFICIENCY

'If a Czech official can give you ten papers to fill in instead of three he will do it with pleasure.'
Jan Mazacek, General Secretary of the Czech Association of Entrepreneurs (Auster 1992, p.9).

This criticism of the bureaucracy in terms of procrastination, inefficiency, and intransigence permeate all aspects of business activity in the Czech Republic. These problems, together with corruption seem to be much more prevalent, however, in dealings with entrepreneurs than with other sections of the business community.

Essentially, the effectiveness of any piece of legislation is inextricably bound up in the ability and commitment of the bureaucracy which must enforce it. Litwak (1991, p.78)

notes that, in the final analysis:

'Legality is a social phenomenon depending upon the beliefs of the population.'

The current bureaucracy in The Czech Republic is virtually unchanged from that which was in situ during the communist regime. The culture which prevails in terms of attitudes and values is virtually unchanged from the corrupt, unhelpful, inefficient system which operated under the communists. See Chapter 7 for an evaluation of the bureaucracy under the communist regime.

Such is the negative power of the bureaucracy that Jan Mazacek, noted that:

'They can drag down even the most enthusiastic entrepreneur.' (Auster 1992, p.9).

Additionally, he concluded that:

A similar comment was made by Ron Stillman and Alan Wertheim, the American entrepreneurs who own the New York Pizza off Narodni Tridi in Prague. They commented that:

'It's still a pretty daunting bureaucracy .....many would be business people have packed their bags and gone home.' (Medrow 1992, p.4).

The recurrent theme in the comments of most entrepreneurs is the interminable waiting for government approvals, and the necessity of using bribes to have one's business registered and approved.

The case of Jan Nemetja, the owner of the Baretta Pizza and Pasta is a typical example of the problems entrepreneurs must face. He had to wait six months to obtain final approval to open his business. The local district office claimed that they had lost all his carefully collected papers. When he tried to call them, he was advised that they did not answer telephone queries. Only after complaining to the mayor with the help of an attorney, and a meeting with the clerks at the local magistrates office were the papers found. Mr Nemetja does not say if bribes were paid.

However, Jarislav Veverka, the owner of Goldex, paid his lawyer five times the standard legal fee in order to push for swift approval of his company. He commented that when he spoke to other firms who had obtained permission quickly to open their businesses, they confirmed that they had used bribes (De Luce 1993, p.8).

When Messrs Stillman and Wertheim of New York Pizza wanted to import gas ovens from the United States, they were advised that they required special permits for the equipment, which they could obtain only after the ovens had been extensively tested in Brno. The process could have taken many months. However, they enlisted the help of a Czech consultant who used to work for the government. She obtained permits for them within one month, and the

equipment did not need to be tested. It is extremely likely that bribes changed hands in this situation.

Jan Mazacek provided an example of the potentially disastrous effects of crossing the bureaucracy. When one bistro in the centre of Prague began its renovation, and opened for business two weeks before it received approval, they were fined 400,000 crowns (Medrow 1992, p.4).

From the perspective of the entrepreneur, the damning comments which they make concerning the bureaucracy do seem to have some validity. The evaluation at the end of this chapter will seek to analyse the role of the bureaucracy in the wider political framework, where the entrepreneurs, as yet, are still very small stakeholders.

PROPERTY ACQUISITION

A universal problem for most entrepreneurs is finding suitable premises with a good location from which they can operate their businesses. However, there are specific circumstances unique to the transitional situation in the Czech Republic which make this an especially difficult problem for potential entrepreneurs.

The real estate and property market are still at an embryonic stage in their development. The intermediation stages between buyer and seller are still very much an ad

hoc arrangement. For most entrepreneurs, word of mouth seems to be the most effective means of obtaining suitable premises.

Stillman and Werthheim found their premises by asking local business people and investigating all possible locations until they found something suitable (Medrow 1992).

Belka Delp, the Czechoslovak co-ordinator for Dairy Queen, the ice cream and sandwich seller, astutely noted that: 'Five years ago, the only way to get tomatoes was by word of mouth. So, now it's in our culture.' (Medrow 1992, p.4). Her own experience of finding premises proved to be a protracted, tortuous undertaking. Having signed a lease agreement with the owner of a building she then found out that he was only one of twelve owners, all of whom had to agree the lease.

The situation is further exacerbated by the fact that there is too little space available for entrepreneurs to set up in business. In Prague, especially, where the demand for property greatly outweighs supply, landlords are able to charge extortionate rents which are out of the price range of many would-be entrepreneurs. The lack of property availability is made worse by the fact that there is a large backlog of housing demand. The pace of construction is very slow and there is a lack of maintenance of existing properties. In terms of government macro-economic

priorities, property renovation is seen to have a low priority in terms of the allocation of funds. It took McDonalds two years to find a suitable location for their first restaurant (Medrow 1992, p.4).

Space problems are further exacerbated by irregularities in the implementation of both the privatisation laws and property restitution.

During the first round of the small companies privatisation auction, bidding was to be undertaken by Czech nationals only. However, potential foreign investors found Czech residents to bid for them at prices with which local people could not compete. After a period of two years, ownership of the property can be transferred to foreign owners.

Although the Ministry of Privatisation was aware of the irregularities in the operation of the privatisation policy, it stated that:
'Our job is to put capital to work. We are not concerned with how (bidders) obtained capital.' (Pitter 1991, p.3).

An additional disincentive to entrepreneurial activity and development is the regulation covering the length of leases purchased by the entrepreneur during the auctions of 1991. The duration of the lease was only two years. Consequently, entrepreneurs are unwilling to undertake

long-term projects, as they are uncertain as to whether their leases will be extended.

The policy of restitution was based upon returning to private owners the property seized by the communists and nationalised from 1948 onwards. The process of restitution must be completed before the property in question in returned to the owner who is then at liberty to rent out or sell the real estate.

The restitution process is lengthy and protracted. Many of those making claims must wait in long queues outside municipal buildings to obtain access to real estate purchase books. It can then take several months to collect the documents necessary to prove family ownership. Even after ownership has been established, the new owner may have to find funds to pay existing occupants for improvements they have made. The new owners may also experience difficulties in evicting tenants with a legally protected lease. Additionally, there is the problem of trying to raise funds for the improvements necessary to make the property suitable for business operations. Finally, there is no guarantee that those to whom the property is returned will be able to manage it well (Parker 1993, p.395).

Entrepreneurs also complain about the absence of legislation to regulate rents. The municipalities, which

own most of the buildings available for rent, can increase rental levels without warning. As a result of this entrepreneurs are unwilling to undertake renovation and development of property.

GOVERNMENT POLICY

Throughout the developed world, most small and medium-sized enterprises look to government for the provision of a supportive financial and institutional structure to assist them in their development. Traditionally, such enterprises have looked for government monetary policy incentives through low interest rates in order to facilitate borrowing and, if possible, special forms of low interest finance. Tax incentives are also greatly favoured by entrepreneurs as a means of increasing profits to reinvest and stimulate growth (Griffiths & Wall 1993, p.78).

Current government economic policy has been determined by the strict monetary constraints stipulated by the I.M.F. Such "stabilisation" programmes are a prerequisite to ensure economic stability for developing countries during the transition process (Kregel and Matzner 1992, p.16). The revised government fiscal policy, which will provide the taxation framework, came into effect on 1st January 1993.

Government policy for reconstruction of the economy has focused primarily on the implementation of legislation relating to large scale enterprises. Despite the fact that small and medium-sized business is the fastest growing economic sector, and will form the backbone of the Czech economy, there is no evidence that the government has adopted any policies or strategies to assist in tackling the problems of small business. Indeed, the evidence suggests that the reverse is true.

The availability of funding for entrepreneurs is being reduced by the financial policy of the government, which has been using strict control of monetary policy, especially interest rates, to maintain economic stability during the transition process (Blanchard et al. 1991, p.3). Interest rates for entrepreneurs doubled during 1993 to between 15 and 20%, almost double those charged in 1992.

The already limited sources of finance are becoming even less available due to the tight monetary measures introduced by the National bank. The new ruling requires that banks with deposits of more than 25 bill. Kcs must have at least 3% deposits in reserve. Those banks who fail to meet this target are charged 20% interest on the amount by which they fall short. Whilst funds are being made available to assist the privatising companies with their indebtedness problems, no provision of funding is being made for smaller and medium-sized organisations.

Criticism amongst entrepreneurs, that the government economic policy is a disincentive, is supported by the furore which ensued, when the new taxation and social security system was introduced in 1993.

In 1992, the government abolished the start-up tax credits which had been introduced as a means of ameliorating the financial burden of new firms. The new system of taxation provides no similar incentives for small business.

A major confrontation took place between the government and representatives of small business over the introduction of the health insurance tax and social security premiums. All firms are required to pay these contributions to finance the social security system and health care programmes. The proposed rates of 13.5% health insurance tax and 36% on social security were to be deducted from total earnings leaving the entrepreneurs with only 50% of their gross revenues.

The governments proposed measures resulted in 20,000 entrepreneurs cancelling their business licences with an additional 150,000 threatening to follow suit. After some negotiation with the government, it was agreed that the rates would remain the same, but would be deducted from 50% of their gross earnings. This scenario was evaluated by all those concerned as:

'An inevitable by-product of a legislative system operating

primarily through trial and error' (King 1992, p.7).

This is perhaps a valid assessment of the situation. In this context, Kregel & Matzner (1992, p.16) comment, accurately, that:

'By their very nature, transitional economies have weak governments of limited jurisdiction and administrative capabilities.'

LACK OF ACCESS TO CAPITAL AND CREDIT

Nowhere is the echo of "money, money and money" as the major source of organisational problems heard more loudly than amongst the budding group of entrepreneurs. However, the problem is particularly acute for entrepreneurs in the emerging market economies of Eastern Europe. They are suffering from the similar problems to those being experienced by privatising state organisations, as discussed in Chapter 10.

Small businesses and would-be entrepreneurs face specific problems in the area of finance, which are particularly acute. Access to capital and credit is essential for small business which requires debt to finance rapid expansion and to diversify and adapt to changes in the market place. The dilemma for most small businesses is that they do not have access to the traditional means of obtaining finance which

are available to small firms in the developed market economies e.g. second mortgages, savings, borrowing from family, and sources of government funding. The main exceptions are those who belonged to the nomenklatura and criminals! These groups were able to acquire substantial funds through illegal black market operations and bribes. The majority of entrepreneurs do not have the capital available to start their businesses, nor do they have significant land and buildings which can be used as collateral with which to raise loans. Only a small minority of people who have had property returned to them under the restitution policy can use it as collateral for loans from the bank (Mills et al 1994, p.5).

James Varanese (1993, p.7), a lawyer in Prague, suggests, however, that the establishment of a lien system. Under this procedure, the bank can place a charge on movables as collateral for the loans, which it can seize in the event of default.

The operation of such a system would require the introduction of a central registry, whereby banks could notify other creditors of the fact that the movables had been pledged as collateral for a loan. The introduction of new legislation to accommodate this registry, which is a common feature in many Western countries, is being discussed. However, given the slow pace of legislative change and the other priorities upon which the government

is currently focusing, such a registry is not likely to be seen as a priority (Varanese 1993, p.7).

The absence of available capital funding is further exacerbated by the lack of experience of the newly developing system of financial mediation. The lack of financial experience affects the ability of both the entrepreneur and the banking system to negotiate appropriate financial arrangements. Neither the state nor the commercial banks feel that they have the qualification or the experience to evaluate financial proposals from small businesses. Additionally, most small business owners do not have the knowledge or experience to prepare business plans which banks would be able to evaluate (Hare 1993, p.6).

Moreover, as a result of increased inflation and future economic uncertainty there are few long-term deposits with the banks. Consequently, most loans are only negotiated over a period of eighteen months, and are granted for working capital only as opposed to long-term fixed capital purchases. This has given rise to the latest joke to circulate amongst entrepreneurs on Prague.
'Want to get a cheap long-term loan?.....Die and go to heaven. Your payments will be stretched over years' (King 1993, p.7).

A critical problem for entrepreneurs is the fact that

short-term loans require extremely high repayment instalments. The impact of this situation can have a fundamentally significant effect upon the profile of small business generally in the Czech Republic. The lack of finance for capital investment will force entrepreneurs to undertake those activities which give a quick return on their investment, as opposed to small business development in areas of the economy which deliver a long-term return on investment.

Some measures are being undertaken by The Czech and Slovak American Enterprise Fund, an American agency sponsored by the American Agency for International Development. The agency is proposing to enter into a joint venture with a local bank, which would allow the fund to provide additional funding for smaller firms. The funding officials are of the belief that the local banks do not have the expertise to provide this service.

Stephen Wald, President and Country Manager of the Czech and Slovak American Enterprise Fund, is quoted by Nemessani (1992, p8) in the Prague Post as commenting that:

> They (the local banking industry) say they can, but they cannot handle the size, the volume, and the documentation required to expedite the loans (to small businesses).

Five of the $60 million advocated to the Czech and Slovak American Fund has been allocated to this "micro lending programme" with an additional $5 million becoming available from another international investor.

However, the original aim of the fund, which was to help small business, has broadened due to political pressure. Czech Prime Minister Václav Klaus would prefer that the funding went to encourage the development of technology in larger businesses. On the other hand, the Czech Association of Entrepreneurs felt that insufficient loans were being granted to smaller firms.

This issue of availability of finance is a perennial problem for all entrepreneurs for which there is no easy answer. Although, in the longer term, the development of greater financial expertise on the part of banks and business people will facilitate the process somewhat (Nemessanyi 1992, p.9).

PRIVATE SECTOR INSTITUTIONS

Most small businesses rely heavily on private sector institutions such as local chambers of trade and commerce to provide a support network, and function as a pressure group on their behalf.

Given the short time period that has elapsed since liberalisation, those private sector institutions which exist in most developed countries to advance the interests of small business are still in an embryonic state. There are some emerging groups such as The Czech Chamber of Commerce and The Association of Czech Entrepreneurs.

However, the nature of their role and its potential influence within the business sphere is yet to be decided. The future role of the Chamber of Commerce will depend in part upon whether it follows the British model of voluntary membership for business or the German model of compulsory membership. Federal legislation was passed in May 1992 which followed the German model of making membership compulsory. However, since the dissolution of the Republic, the legislation has been reviewed by the government which is now seeking to make membership voluntary. The Chamber's Executive Director, Antonin Smid, has argued that the Chamber needs the fees generated by compulsory membership to provide the private sector with the support and influence it requires to promote the interests of business within the community.

The government believes that entrepreneurs should make up their own minds about membership. It believes, however, that it may be possible to reach a compromise by allowing compulsory membership for a period of three to five years at the end of which membership should be voluntary.

The Chamber believes that the government fears the power that it could generate within the economy. It has 150,000 members and is the largest of such associations. It was also a signatory to the social contract drawn up with unions, employers and the federal government as part of the transition to the market economy (Boland, 1993, p.10).

There is much debate surrounding the compulsory versus voluntary status of chambers of commerce. Some argue, like the Czech chamber, that it should be compulsory. Others argue that, if membership is made compulsory, the large organisations will dominate the associations. Others see the compulsory role of chambers as creating yet another layer of prescriptive bureaucracy which will simply be another control instrument of government. Finally, most entrepreneurs wish to see government control, although not government support, minimised, and would prefer a voluntary arrangement. The heart of the debate is not about membership of chambers of commerce, it is about the re-definition of the relationship between the rights and freedoms of citizens and the role of state intervention. This issue will be developed further in the section below and will evaluate the impact of the fundamental political re-definition of the country as it affects the activities of entrepreneurs (Bruner, 1994, p.1).

CASE STUDY

To illustrate some of the issues discussed in the previous sections, the following case study focuses upon the problems and opportunities identified by one of the new entrepreneurs. Some of the issues are common to most businesses during the transition process, whilst some are specific to entrepreneurs.

PROPRINT LTD

Petr Pasek is one of four shareholders of PROPRINT Ltd, a small printing company located in Ostrava in Northern Moravia, some five kilometres from the Polish border. It was established in 1990, and in 1992 it became a limited company. The firm offers a full range of design and printing services from the graphic design stage up to the final printing and including book-binding. The majority of the work done by the firm is concerned with producing advertising and custom-made public relations and advertising materials for companies. The firm also acts as a distributor of printing colours in the region of Northern Bohemia on behalf of an Austrian firm.

In terms of company structure, each of the four shareholders is in charge of the art/graphics department, the print department, the department of photoprint and printing preparation and finally the department of

management and marketing of which Petr is in charge.

The company employs ten people, four men and six women. Four are located in the print department with two employees in each of the remaining departments. The firm currently conducts its operations from a suite of rented rooms in the local theatre building.

Petr sees the main objectives of the firm in terms of producing goods of the highest quality possible which meet the needs of the consumer. In the longer term the company hopes to expand into the production of specialised magazines.

As regards the strengths and weaknesses of the firm in terms of its capability to fulfil its objectives, Petr believes that the company is flexible and can fill client's orders very quickly. The workforce are also highly trained and are developing a customer care and awareness approach. He is optimistic in the sense that he believes that there are real possibilities for growth now that the market has opened up, and believes that there are opportunities to be capitalised upon from possible joint venture business activities with potential foreign partners.

Possibly, the main challenge for the organisation is to find new markets for their products. A real difficulty in this area is the fact that until recently, it was not

possible to check in advance the creditworthiness of potential customers. Their ability to find new markets is also constrained by the technology that they have available, which is in turn constrained by the financial situation of the company. Like many small firms they find themselves caught in the trap of being unable to obtain a bank loan without any collateral but cannot generate the wealth to purchase capital equipment without being given the finance to do it. The initial funding for the company was obtained from the savings of the four owners and family contributions.

Concerning the development of new products and services as a strategic option, the company feel that it is limited here by the lack of highly qualified workers. Additionally, they are restricted by the space constraints of the rooms in the cultural centre from which they operate.

There is also a lack of knowledge concerning the latest technological and management know-how within the firm. The previous regime restricted the flow of new technology and information on the latest printing techniques which is now proving to be a drawback to the company's development.

The language problems create added complexity to the situation. The employees and owners are so busy that they do not have time to develop their language skills and must

rely on translators and interpreters. Petr feels that the main problems in dealing with government relate to the lack of reliable information available from them. It is often necessary to track down information from a variety of sources and this takes up valuable time.

Petr perceives that human resources management-related issues are the real problems within his company. A major obstacle is the negative attitude to work, inherited from the past regime. The previous system did not encourage or reward quality effort or responsibility. In the words of Petr:

> It is difficult to change people's thoughts towards the idea of: if working in the company, the better you work the better the profit of the firm is, and the better profit the company can achieve the better salary and profit you can be given and offered by the company.

In order to change this attitude, Petr gives new employees a probationary period during which time their ability, flexibility, responsibility and interest in the job can be observed before making the post permanent.

Regarding the personnel practices of his own company, Petr recruits people on the basis of qualifications and experience. Most of the employees are referred by word of mouth or are known from Petr's previous employment with the state printing company.

Pay levels for employees are determined by level of responsibility, the quality and quantity and speed of work produced and previous experience. Promotion is also based on quality of work, relationships with clients and the range of relevant skills that an employee can offer.

The company offers employees training and development opportunities by covering the costs of different courses offered by the training agencies e.g. accounting courses, computers and the new taxation system.

Although relatively optimistic about the future, Petr has suffered negatively from the split between the Czechs and Slovaks. Before the dissolution of the federation, Petr used to liaise with companies in Slovakia in order to assist with some of the print processes and distribution of the inks. After January 1993 it became so difficult to carry out this process that much of the work is now carried out elsewhere.

EVALUATION

Whilst the issues outlined above create real problems for entrepreneurs, and, consequently, for the overall effectiveness of the economy, the issues must be understood and evaluated within the context of the wider political and economic framework.

Regarding the concerns of Czech entrepreneurs, it is interesting to note that the new Chairman of the Confederation of British Industry's smaller firms council criticised the British government because:

> There were still constraints inhibiting the growth of small companies ..... including lack of adequate finance and management skills.
> (Daily Telegraph 1994, p.28).

He also demanded:

> ...an easing and avoidance of unnecessary regulations which have a disproportionately high impact on smaller firms.
> (Daily Telegraph 1994, p.28).

Thus, the reality is that some of the problems faced by small businesses are a function of their size and endemic to the problems of entrepreneurs in most developed market economies.

Nevertheless, the problems for entrepreneurs are undoubtedly compounded by both the communist heritage and the problems of transition. Some of the problems of transition which are due to inexperience and lack of the appropriate institutional expertise will be resolved over time.

However, at a more fundamental level, the problems of the entrepreneurs are symptomatic of much deeper, complex problems, for which there are no easy solutions.

The Role of the State

At a fundamental level the role of the state, and its relationship to the rights and freedoms of its citizens must be clarified and legitimised. The wider arguments concerning the appropriate degree of state intervention in the economy are discussed elsewhere. Nevertheless, the appropriate role of the state in the context of business is well identified by Kregel and Matzner (1992, p.23) as follows:

> The active role of the state is a condition for the staging of a socio-economic context, in which the participation of individuals and social groups in the socio-economic framework occurs in the pursuit of self interest.

Entrepreneurs would argue that the state is not fulfilling this role, and from their perspective, within the framework of their own priorities, this is a valid assessment of the situation. However, the state has only limited resources and expertise with which to manage the economy, and clearly perceives that the main priority is the privatisation of the large organisations, as a major source of finance and employment. From the perspective of a manager in a privatised organisation, government policy may be

considered right and proper. In the long term, however, it is from small and medium-size firms that employment opportunities and growth will develop, and at some point their needs must be addressed as part of a coherent government policy for small business.

Legislative Complexity

Concerning the problems of legislative complexity, it is true that the laws appear complicated, protracted, distorted and open to corruption at all levels. However, the legislation chosen was based upon models of existing legislation in Austria and the European Community, and Germany in particular, where they seem to function well.

The difficulty lies not so much with the problems of legislation as with problems concerning the concept of legality. This view is reinforced by Litwack (1991, p.81) who comments that:

> Although reforming socialist countries, especially the Soviet Union, have been writing and re-writing such laws at a mind-boggling pace in recent years, the countries have not yet succeeded in building genuine legality.

In terms of how genuine legality can be achieved, Scruton (1991, p.24) concludes that:

> No amount of constitutional reform will undo their (the Communist Party) evil work if it is not accompanied by the restoration of legality: which means the training of a new generation of judges and advocates, a re-ordering of the procedures and practices of the courts, the establishment of an impartial, civilian and strong police-force, and a concerted effort to subject the decisions of the administration to the scrutiny of independent judges.

However, given that 'the process of institutional development involves a complex interaction of cultural, political and economic variables' there is no guarantee that the process of legality will evolve as outlined by Scruton (1991, p.24). The system requires pro-active powerful change agents who will facilitate the process of evolution and paradigm change within the society. There is no guarantee that this will happen.

Undoubtedly, a major stumbling block to the process of change outlined above lies with the bureaucracy. Robert Jones (1992, p.4) likens the weaknesses of the state bureaucracy to those exhibited by the standard Weberian model of bureaucracy. Additionally he comments that the functioning of the bureaucracy was additionally disabling as:

> In the absence of accountability and effective machinery of redress, bureaucratic behaviour was geared to satisfying superiors and nominally fulfilling targets.

Misha Glenny (1990, p.19-26) reinforces the belief that the bureaucracy has remained intact because:

'They are the very heart of Communist rule, and to an extent are irreplaceable.'

Consequently, he argues, the government has little option but to assimilate the structures into the democratic process. However, given that the Czechs have adopted a German model of law, which spawns great bureaucracies for its implementation, it may be that the conclusion of Jones (1992, p.28) is valid:

> In post-communist Eastern Europe there is a widespread fear that bureaucracy will increase its power and that it could present a formidable obstacle to change.

Given that much of the bureaucracy is unchanged from the communist era and that:

> Whole areas of law..... remain either non-existent or entirely embryonic.....the party, the secret police, and the party organisations have never accounted for their actions, for their property, or their income. (Scruton 1991, p.28)

there is indeed a danger that the process of fundamental change required to legitimise the operation of the new system will be retarded or distorted to an unacceptable hybrid.

Additional progress in legislative and bureaucratic change is inhibited by the notion of the state and the bureaucracy being a "social arbitrator" in terms of regulating activity as opposed to the "unbiased administrator" concept implicit in the Weberian model. This role is characterised by the civil services of those market economies which the Czech Republic seeks to emulate.

In fact Scruton (1991, p.28) believes that:

> This state (social) arbitration has been, and remains, a great cancer in the life of sovietized economies, as well as being a major obstacle to legal and economic reform.

The existence of this phenomenon can be seen for instance in the vetting processes required to obtain licences and business registration. It can also be seen in the interventionist attitude of local authority officials and bureaucrats, who seek to influence and regulate, rather than process, the issues with which they are dealing. It is also apparent in the general lack of consistency in the application and implementation of procedures prescribed in the legislation.

Financial Intermediation

Concerning the role of the banking system and the development of financial intermediation, there are many foreign models on hand which are being adapted for the

Czech situation. As regards the availability of finance for small businesses, entrepreneurs will always be faced with the problem that most small businesses are high risk, and banks are generally risk averse institutions. In the short term, it is unlikely that the government will address this area. Most support for small business finance is likely to come from the European Community and various other state agencies.

In the short term, also, it is unlikely that the problems of complex legislation, bureaucratic inefficiency and lack of capital will be resolved. These issues will only be addressed when questions of the role of the state, the function of the bureaucracy and the legitimisation of the concept of legality have begun to be clarified. Nevertheless, liberalisation has afforded excellent opportunities for entrepreneurs to start up new businesses in a whole variety of areas.

Additionally, the development of chambers of commerce and the media will provide potential sources of collective pressure which the entrepreneurs can apply to government in order to improve their situation within the community. At the end of the day, however, risk and size factors associated with small business are endemic to entrepreneurial activity. In the final analysis, it is the cost benefit analysis of potential gains against the risk of failure which the entrepreneurs must evaluate. This

pursuit of self-interest and freedom of choice is, after all, an integral feature of the operation of a market economy. So too, however, is the exceptionally high failure rate which accompanies any entrepreneurial business venture. The certainties of the old regime, with its accompanying constraints, are gone. The entrepreneur now has the opportunity to succeed or fail in the pursuit of self-interest.

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NUMBER OF REGISTERED ENTITIES AND ENTREPRENEURS IN THE CZECH REPUBLIC

Main activity	Total		of which			
	No. of companies	Percentage	Private entrepreneurs	Companies and partnerships	Co-operatives	State enterprises
Agric. and forestry	87,643	7.29	80,567	1,245	1,592	338
Fish farms and fishing	434	0.04	370	25	1	14
Mining and quarrying	1,157	0.10	928	122	3	59
Manufacturing	230,211	19.15	218,339	9,979	531	893
Electricity and gas generation, water supply	1,332	0.11	1,010	140	5	80
Building industry	172,526	14.35	166,238	5,408	448	271
Trade and repairs	266,902	22.20	242,728	22,806	297	297
Catering and accommodation	64,138	5.34	61,895	1,945	43	100
Transport and communications	46,251	3.85	43,832	1,991	58	82
Finance and insurance	3,431	0.29	1,803	515	0	0
Real estate, R and D, commercial services	213,858	17.79	198,504	10,570	1,488	710
Administration, defence	10,501	0.87	3,221	40	6	10
Education	15,766	1.31	12,086	244	22	7
Health care, social security	17,897	1.49	2,872	366	8	15
Other public, social and personal services	70,100	5.83	41,725	1,149	79	102
Others	53	0.00	49	1	0	0
Total	1,202,200	100.00	1,076,167	56,546	4,561	2,978

Source: News From Prague, Prague, Trade Links, November 1993, p.5

CHAPTER 12

CONCLUSIONS

> 'There is nothing more difficult to take in hand, more perilous to conduct or more uncertain in its success than to take the lead in the introduction of the new order of things'
>
> (Machiavelli, from the translation by Mansfield, 1985)

There can be little doubt that the challenge facing the inexperienced government of the Czech Republic in 1989 as it undertook 'the introduction of the new order of things' was a task of monumental proportions. It is indeed a massive undertaking to construct a new political, social and economic order. Over the five year period from November 1989 to November 1994 - the timespan of this analysis - not only has the region undergone massive political and economic restructuring, the same time period also encompassed the division of the former Czechoslovakia into the two independent states of the Czech Republic and Slovakia.

The broad nature of the changes taking place within the country comprised the establishment of a new political order, the development of a new legal and regulatory framework, the redefinition of the social order and the development of appropriate political, economic, financial and social policies in order to implement these changes effectively.

In terms of evaluating the success of the Czech Republic in effecting this transition, the range of relevant areas to consider is diverse. The focus of this analysis, therefore, has been to evaluate the effectiveness of the key political and economic changes, taking place in the new environment, which are likely to impact most directly upon the capacity of enterprises to undertake the fundamental changes required of them if they are to survive in the new order.

The following conclusions do not seek to consider the progress of events in this area in terms of success or failure, but to consider whether the current economic changes are conducive to maximising the potential effectiveness of enterprises in a market-based economy. In this context conclusions will also be drawn concerning the ability and willingness of enterprises to respond positively to the myriad of changes taking place all around them.

Concerning the issue of the effectiveness of the relevant political and economic changes, both generally and in relation to the restructuring of organisations, a wide range of diverse opinions have been expressed by commentators on the Czech Republic. As the following excerpts will make clear:

> The strong hand of government has produced carefully controlled economic reforms, which have ensured social well-being and thus contributed to a peaceful political scene.
> (Fisher 1994, p.31)

or again:

> ....the economic transition in the Czech Republic is far from over, as problems in certain sectors remain critical and a large scale restructuring has yet to take place.
> (Fisher 1994, p.31)

> The Czech economy may be flourishing but it remains enmeshed in a complex web of bailouts, props and government controls.
> (King & Murray 1994, p.10)

> In 1993 it (The Czech Republic) managed to create political and economic conditions that appear to give reform a reasonable chance of success.
> (Pehe 1993, p.6)

> The absence of regional economic recovery....the failure to bring inflation rates down to OEDC levels, the lack of effective programmes for privatising many of the large industrial enterprises....indicates that for much of the region, the worst of the economic transition may still be to come.
> (Slay 1993, p.42)

The diversity of opinions expressed above is indicative of the difficulties associated with undertaking this evaluation exercise. It can be argued, however, that all

of the views have some validity depending on the conceptual framework within which the events and trends of the last five years are evaluated.

DIFFERING CONCEPTUAL FRAMEWORKS

There is evidence of a view amongst some influential commentators and policy advisers that the transition from communism to capitalism is a linear progression along a set continuum. At one end is located the command economy, whose characteristics are derived from the political ideology of Marxism. At the other end of the spectrum is the notion of a market economy based upon the neo-liberal monetarist principles.

These market-related concepts are underpinned by the Anglo-Saxon model of democracy, whose form is associated mainly with the economic policies of the United States and the United Kingdom during the 1980s. The main neo-liberal economic policy derivatives of this philosophy comprise minimal government intervention in the market together with the significance of monetary targets and monetary policy measures as the basis of economic stability and growth.

The promotion of the principles of free market forces also promotes the concept of individualism as a fundamental tenet of the philosophy. Short-termism is an additional characteristic of this model, partly as a result of the

outsider model of corporate governance which predominates in this system (Held 1987, p.276-277).

These neo-liberal economic principles proved to be major determinants of the economic policy advice and targets set by the International Monetary Fund, when it developed its 'standard stabilisation package' for the countries of the former Communist Bloc. The implementation of the main policy measures comprising price liberalisation, control of inflation, currency convertibility, balance of payments stabilisation and privatisation of state owned enterprises were outlined in Chapter .

The standardisation measures were developed by western economic policy advisers to facilitate the transition of the Eastern European states from a command to a capitalist system, as quickly as possible, whilst minimising the negative effects of inflation and exceptionally high levels of external debt.

Within the framework of the IMF standardisation package, it is possible to claim some measure of success for the Czechs in the transition process, superficially at least. The process of price liberalisation which began in 1991 with the liberalisation of some 85% of goods and services is still continuing. Through the operation of an effective incomes policy and the application of strict fiscal and monetary measures, especially in relation to interest rates

and lending, the Czech Republic has maintained a relatively low rate of inflation and avoided the hyper-inflation experienced in some of the other Eastern European countries. The absence of any major external debt with the West at the time of the transition has enabled the Czech Republic to achieve a relatively low stable external debt situation. The currency is now internally convertible, and is progressing towards partial convertibility.

In addition to its ostensible success in implementing the constituent elements of the standardisation package outlined above, the Czech Republic is also praised for maintaining a relatively low rate of unemployment and comparative social peace during the transition process. However, at an economic policy level one can question whether the apparent short-term success of the Czech Republic in relation to fulfilling these objectives is conducive to the attainment of the long term restructuring that must take place, if the country is to function effectively in a competitive global environment.

Control of inflation during the period of price liberalisation has been achieved, primarily, by the adoption of a punitive monetary policy in relation to interest rates. These peaked at 24% in 1993 and thereafter have remained at punitively high levels. Moreover, strict controls on bank lending, which accompanied these policies, have resulted in banks restricting their lending policies

in relation to the former state-owned enterprises to short term loans for cash-flow financing only. This unwillingness to lend has prevented the obsolete manufacturing enterprises from undertaking the necessary capital expenditure required to improve the quality and efficiency of their production techniques.

Moreover, as the former chapter on organisational emergence has demonstrated, the availability of finance is even more restrictively controlled and expensive to obtain than is the case with the transforming enterprises. This is due in part to the system of cross-ownership, whereby many of the banks to whom the former state-owned enterprises are indebted also own shares in these companies. Clearly, when banks are providing loans, these enterprises will receive preferential treatment over the smaller, newly established organisation.

Additionally, the banks are extremely conservative in their lending policy to new, untested entrepreneurs with little business experience and no collateral. Frequently they refuse to lend, or do at penal rates of interest.

Finally, the use of interest rates and bank lending as a macro-economic tool of government policy removes much control of lending from the banks. As government policy is committed to supporting the continued existence of the former state owned enterprises in order to keep down

unemployment, the banks are required to charge this loss to these companies. This policy has undoubtedly helped to inhibit organisational growth in this vital area of the economy.

The other main policy measure of government in relation to controlling inflation has been the implementation of a strict incomes policy administered by the social pact between unions and employers whilst consumers were experiencing substantial price increases as a direct result of the policy of price liberalisation. Thus, the introduction of an incomes policy led to a significant fall in living standards, and, consequently, in consumer demand. It is difficult to see how a demand-led recovery from recession is likely to emerge, while wage constraint and price liberalisation measures continue together.

The privatisation process within the Czech Republic is seen by some as a major step forward in returning property to private ownership. However, as the chapter on privatisation has shown, the continued concentration of the ownership of firms in the hands of bodies which are either directly or indirectly controlled by government, raises questions as to whether true privatisation has been undertaken at all. Moreover, the continued direct intervention of government in the affairs of individual private enterprises is contradictory to the underlying philosophy of private ownership, implicit in privatisation.

Concerning balance of payments stability, Myant (1994, p.203) notes that the recovery in exports within the Czech Republic has been amongst less advanced goods. This has manifested itself in a fall in the export of heavy machinery and consumer goods, with increases in the export of intermediate goods. As they are of a lower value-added than was previously the case under the old regime, the contribution of exports to GNP is less than under communism.

Finally, concerning the issues of social peace and low unemployment, it can be argued that the government has bought social peace through artificially maintaining a low rate of unemployment. The evidence supporting this claim becomes apparent when one considers that the unemployment level since 1989 has risen to 4%, whilst productivity has fallen by 25% during the same period. Moreover, the ambivalence of government towards the issue of bankruptcy, which manifested itself in the weakness of the resulting legislation and its subsequent implementation, further hindered the necessary labour-shakeout and re-structuring of former state-owned enterprises. There is no doubt that the delays in implementing bankruptcy legislation, the fact that it excluded the privatising enterprises and the protracted restructuring period awarded to bankrupt firms have exacerbated this situation.

The above concerns in relation to the potential impact of the stabilisation measures on the long-term development of the country has led some commentators to question the applicability of the IMF standardisation package to the Czech Republic.

In this area, Myant (1994, p.273) concludes that:

> the fundamental mistake was that the strategies were too narrowly conceived. They were based on economic thinking alone and within economic terms derived .....partly from neo-liberal thinking.

TOWARDS A SOCIAL DEMOCRACY

Despite the fact that the Czech Government has sought to implement the policy measures contained in the IMF stabilisation package, as discussed previously in this chapter, the author would question the extent to which the Czech government has embraced the underlying philosophy of minimal government intervention implicit in the concept of Anglo-Saxon democracy. There is a significant body of evidence to suggest that in fact the Czech Government is seeking to develop a democratic system underpinned by the concept of the social market, similar to that adopted in post-war former West Germany.

This German model is characterised by a significant degree of government intervention in relation to economic and

industrial policy together with a consensus approach to decision-making. The financial structure is dominated by an insider model of corporate governance encouraging an integrative strategic approach to long-term decision-making on the part of the relevant stakeholders. These concepts of collectivism, consensus, mutual interdependence and long-term planning contrast sharply with the conflicting short-term individualism characterised by the outsider model of corporate governance which underpins the neo-liberal thinking implicit in the Anglo-Saxon model (Fulbrook 1991, p.182-183).

Additionally, the relationship between the legislature, the state and the role of the political process differs between the respective models. The Anglo-Saxon model emphasises the dominance of the concept of civil society, which promotes the culture and ethics of legality in the context of which the institutions of civil society predominate over the state and the law.

The German model places greater importance on the concepts of social arbitration, enlightened bureaucracy and the role of law as an educative function. This approach sets certain policy areas in the realms of bureaucratic and legal jurisdiction, which would have been set in a political forum in the context of an Anglo-Saxon model of democracy. It also concentrates a significant degree of power in the hands of the bureaucracy (Fulbrook 1991, p256-258).

An analysis of political and economic transition in the Czech Republic demonstrates strong similarities between Germany and the Czech Republic in relation to the degree of government intervention, the consensus style of decision making and the traditionally influential role of the bureaucracy.

In the economic sphere, the implementation of company legislation based upon the German model of business can, together with the adoption of the insider model of corporate governance, re-enforce the similarity between the two countries.

Government intervention

The degree of government intervention in the economy is a critical differentiating factor between the Anglo-Saxon and German models. The chapters on organisational transformation and privatisation in this thesis have demonstrated the extent to which government intervention pervades the economy at both a macro and a micro level in the Czech Republic. The likelihood that this trend will continue in the longer term is re-enforced by the fact that the ownership structure of the newly privatised enterprises can indirectly, and in some cases, directly, be traced back to government control. Additionally, government domination of both the Konsolidacni Banka and the National Property Fund are further indications of the governments intention

to retain a long term involvement in the activities of the 'privatised enterprises'.

Direct government intervention in this area can also be identified in terms of its direct influence on the distorted operation of market forces as a direct consequence of bankruptcy legislation.

A system of company legislation which is also very similar to the German model has been adopted, especially in relation to the joint stock company, the most commonly adopted company form for the large former state-owned enterprises. This legislation makes provision for the establishment of a system of employee participation similar to the German concept of mitbestimmung (worker participation). Implicit in the philosophy underpinning this concept is the notion of consultation, co-operation and long-term planning which has led to the climate of consensual decision-making characteristic of much of German industry (Mills 1991, p.102).

Consensus decision-making

The concept of consensus decision-making in the Czech Republic has been reflected not least in the way in which the government has undertaken a social pact with the unions. Additionally, the inclusion of employee participation in the company legislation as outlined above

is indicative of the government's desire to develop a consensual approach to decision-making as an integral feature of organisation development. It must be said, however, that the rationale underlying this consensual approach may be attributed in part to the national characteristics of the Czech nation. The chapter analysing the nationalist question was prefaced by a discussion of the historical development of Czech culture, where consensus and mediation were often the strategies for survival for a land-locked region surrounded by larger and potentially stronger and more aggressive neighbours. Conclusions on the impact of the role of national culture on the transformation process within the Czech Republic will be developed later in this chapter in the section which discusses the notion of 'habitus'.

Conflict of values

If one accepts that the emerging form of democracy in the Czech Republic approximates more to the German than the Anglo-Saxon form, what might be the implications for the effectiveness of the policy measures being implemented in the region? It is possible to foresee yet more problems emerging to contribute to the major difficulties already being experienced in the Czech Republic during the transition. Confused thinking and resultingly inappropriate actions could occur where foreign advisers on policy promote economic behaviours and business practices

underpinned by the assumptions of short-termism and minimal government intervention but in a political and economic situation where the values and structural mechanisms are more closely aligned to government intervention and long term integrative strategic planning and decision-making.

Effectiveness of government policy

Notwithstanding the potential political conflict situation outlined above, the fact remains that the government is seeking to develop a more socially-orientated model of democracy than has been assumed by external advisers. Within this context, we have to ask how effective have their policies been in relation to the transformation of the former state owned enterprises and the development of the newly emerging organisations?

There can be little doubt that deliberate government policy has left unchanged or recently created, a structure of ownership that is unlikely to possess the will or the expertise to undertake the major restructuring necessary to facilitate the long term survival of the majority of the former state owned enterprises. Additionally, the policy of the government in relation to bankruptcy, and its decision to continue the financing of technically bankrupt industries, can only exacerbate the situation. The problems, thus created, are compounded by the fact that the scarce financial and administrative resources allocated to

this exercise are thus directed at the expense of vital investment which is required to stimulate the growth of the newly emerging enterprises.

However, the propping up of these technically bankrupt enterprises cannot continue indefinitely. It is a classic stock versus flow situation, whereby, eventually, the stock of funds from the privatisation process and other sources will become exhausted. The critical question then becomes 'what happens when the money runs out?' Since government policy provides little incentive for the majority of industries to restructure, they are unlikely to become profitable enough to generate their own funds and contribute positively to economic growth in the country.

As the newly-emerging organisations are still at an embryonic stage, they are unlikely to make a significant contribution to gross national product in the short term. Indeed the chapter on organisation emergence could lead one to conclude that the government is at best apathetic and at worst positively unhelpful in stimulating growth and profitability amongst these small businesses.

Foreign investment is another possible source of external funding. However, as the stakeholder analysis contained in the chapter on privatisation, and the statistics included in Appendix XI of chapter 5 demonstrate, this is a relatively small and unreliable stream of funds.

Additionally, the somewhat negative attitude of government to foreign investment does little to stimulate potential inflows of funding from abroad.

The future does not seem hopeful for some of these technically obsolete industries. At best, the government can only be delaying the inevitable labour shakeout which must occur at some point in the future. It remains to be seem whether it is to the greater benefit of the country that the resulting unemployment comes later rather than sooner. The Czech Government would appear to be hoping that the former will be the case.

In this context, it is the view of the author that, in principle, the philosophy behind a social democratic model has much to support it, given the post-war success of the German economy. Within this framework, however, it is highly questionable as to whether the government has implemented the most advantageous policy measures for the long-term development of the country.

BUREAUCRATIC CORRUPTION AND ORGANISED CRIME

There are also major forces within the economy which make the problem of policy choices and implementation even more complex and challenging for the emerging economies of Eastern Europe. In seeking to formulate a new political and economic philosophy, the Czech government is faced with

complex constraining problems that are not wholly identifiable with the preceding models. These comprise institutionalised bureaucratic corruption and organised crime. So significant is the potential impact of these issues on the transition process that they could significantly distort the emerging economic and political form of the country.

As the chapters on the nationalist question, everyday life and the functioning of the old regime have demonstrated, bureaucratic corruption had been endemic in the former Czechoslovakia since the time of the Austro-Hungarian empire. It was subsequently further empowered by the inception of communism, when the central planning system spawned powerful bureaucracies to direct and regulate its implementation and control. These previous chapters have also highlighted the extent to which the pervasiveness and power of the bureaucracy permeated all aspects of life. Unfortunately the demise of the central planning system did not take with it the concomitant corrupt bureaucratic practices, as the recent major bribery scandals, especially in relation to the privatisation process, have shown.

From the perspective of trying to predict the potential impact of this phenomenon on the future of the Czech Republic, a comparable model of bureaucratic corruption within the democracy was sought. A suitable model to predict the likely outcomes for the Czech Republic was

considered to be that of the Italian experience.

In his observation of the operation of the Italian bureaucracy, Richards (1994, p.55) could equally have been describing the Czech Republic, when he noted that:

> Citizens pay in cash or kind, to obtain services which should have been theirs by right but which in much of Italy had become privileges granted conditionally.

Indeed there has developed in Italy a more powerfully corrupt bureaucracy controlled by the various political parties, which runs in parallel with, but is more powerful than, the state civil service. This parallel government has been able to transform hundreds of thousands of jobs in the public sector into the largest field of patronage in any Western country. All jobs within the bureaucracy, from drivers and clerical assistants up to the highest levels, are allocated to members of the various political parties, thus earning these employees the nickname of 'nomenklatura'(Richards 1994, p.49).

The influence of corruption is so extensive that it permeates all aspects of public and business life, with everyone involved expecting to receive some payment. This system has resulted in serious negative outcomes for the Italian economy which could be replicated in the case of the Czech Republic. The inclusion of bribe and commission

payments in respect of all dealings with the government has greatly inflated the prices of contract work and services, especially in the field of public works and government contracts. This in turn has led to the accumulation of a massive national debt, with all its concomitant economic problems.

Additionally, the degree of corruption has had a significantly adverse effect on the level of foreign investment to the extent that, as Richards (1994, p.65) speaking of Italy notes:
'they (foreign investors) could not do business in a climate so corrupt that they had to pay bribes at every turn'.

One can envisage a situation whereby the already ambivalent attitude of the Czechs in relation to foreign investors could exacerbate the situation further.

Moreover, as Mills and Stenson (1994, p.5) noted the predominant role of bureaucracies afforded by the German model of democracy, which the Czech Republic seems to be adopting, gives greater influence and power to these 'adaptable corrupt bureaucracies' than would be the case in the Anglo-Saxon model.

The series of government bribery scandals and the refusal of government to pass legislation on conflicts of interest

in respect of politicians re-enforces the message of legitimised corruption. So integral is the concept of corruption to the bureaucratic system, it is difficult to envisage that the government will be willing or able to irradiate it in the foreseeable future.

Organised crime

The problem of organised crime is now a highly publicised phenomenon in Eastern Europe, where comparisons are frequently made with the activities of the Sicilian Mafia. Indeed, the evidence from the Czech Republic suggests that the Mafia and other criminal bodies whose structure is modelled upon this organisation have already permeated Eastern Europe.

In a telling observation on the potential growth of the influence of organised crime, Richards (1994, p.230) makes a comment on Berlin, that could equally well apply to Prague when he posed the question:
'How soon will it be before Berlin is divided again between the Sicilian Mafia and the Russian Chechens?'

There is little doubt that within the Czech Republic during the time of communism black market activities and currency dealing contributed to the development of organised criminal networks. Since liberalisation, the time gap between the dissolution of the old control systems and

structures and the reestablishment of a new regulatory order has enabled these networks to flourish and grow. Additionally, just as legitimate foreign investors see potential market opportunities, the barons of organised crime see potential opportunities for developing their empires.

Clearly, the crusade for the eradication of organised crime is a global issue and, already, international law enforcement agencies are consulting with their Czech counterparts to tackle the issue. It remains, however, an area of ever growing concern, not least for its distorting effect on the economic development of the country.

ORGANISATIONAL TRANSFORMATION AND EMERGENCE

What then has been the organisational response to the environmental policy changes which have, at a stroke, rendered the '<u>modus operandum</u>' of these behemoths both impotent and without legitimacy in the new order?

What is the probability that these enterprises will be able to formulate successfully and develop the radical change strategies that must be undertaken if they are to re-establish an equilibrium position that is in congruent with the radically different environment in which they find themselves? What are the prospects for the newly formed enterprises which find themselves at an embryonic stage in

their development, with no past experience upon which to draw, and little certainty concerning the future prospects for survival in unchartered waters?

There are several key areas of Czech industry, primarily glass, porcelain, brewing and cars, which are already internationally successful enterprises, and, as such, are likely to undergo the necessary metamorphosis required for them to survive as commercial enterprises. For the majority of state-owned enterprises the future is much less certain.

Whilst the external environment is, undoubtedly, a major driving force for change, external pressures do not necessarily precipitate the appropriate automatic responses on the part of enterprises to adapt to those changes. The powerful intermediation role of the stakeholders have the ability to choose in respect of the future strategic direction of the organisation that may not be in congruence with the environment. This is especially so if they do not perceive the proposed changes to be in their own best interests. The concept can be encapsulated in the application of Lewin's force field analysis. This theory is based upon the premise that the likelihood of an enterprise undergoing substantive paradigm change is dependent upon the relative strength of those forces which support or oppose the change.

As highlighted in the stakeholder analysis contained in the chapter dealing with privatisation, the array of forces seeking to inhibit the change process would appear to be markedly more formidable than those supporting the transition. The problem is made more complex, and the opposition to change more intransigent, because the major inhibitors to the process derive not only from the residual legacy of the past regime, but also from the previously discussed policy measures instituted by government in relation to privatisation and restructuring.

The structure of ownership which is concentrated primarily in the hands of the banks, re-enforced by the insider model of corporate governance, gives little incentive for change. Indeed, the structure is likely to set in motion a series of major conflicts of interest issues between banks and enterprises, if major change initiatives were successfully set in motion.

Within the enterprises themselves, the agency problems in relation to management, whereby they pursue their own self-interest at the expense of the company, together with the understandable negative attitudes and behaviour of many employees, further inhibits the likelihood of any major changes taking place with the enterprises, even in the longer term.

Even if one considers the possible interventionist change agents who might facilitate the transformation process, problems arise in this area too. The limitations of the effectiveness of the human resources management functions have been discussed previously in terms of their credibility gap. The external policy advisers and management teachers, who one would expect to have a fundamental role in initiating the change through the re-education process in relation to management and organisations, experience major limitations to their effectiveness. A main reason for their lack of success in this area relates to the conflict of values discussed earlier in the chapter.

Much of the re-education process taking place is based on the notion of the Anglo-Saxon model of management and organisation thinking, which encompasses the notion of short-termism as a key aspect of decision-making. Such strategies are in congruence with the outsider model of corporate governance, as opposed to the insider model which is developing in the Czech Republic.

Additionally, the culture specific nature of much management education and consultancy is prefaced by erroneous assumptions concerning the existence of a parallel external business and financial institutions which are underpinned by shared value systems implicit in the Anglo-Saxon model of democracy.

Foreign investors are also considered by some to be potentially prime change agents, bringing with them the new technology ideas and strategies that will help to drive the transition process forward. The reality is, however, that foreign investments constitute only a minimal part of the overall value of state owned enterprises. The ambivalence of the Czech government to the contribution of foreign investors has been well documented. The insistence on retaining Czech ownership and control of the relatively more successful major industries precludes the introduction of changes into those enterprises which are in a position to benefit most from their implementation.

Additionally, the failure of some joint ventures, notably Czechoslovak Airlines (CSA) with Air France, together with a number of lost joint venture opportunities, such as Skoda Pilsen and Siemens, re-enforces the validity of the assertion that resistance to change is very strong in both the political and economic sphere.

Thus, on balance, the failure to make adaptive changes in many former state owned enterprises is likely to result in their ultimate demise or the perpetuation of uneconomic and inefficient work practices which will make these organisations reliant upon state support for their continued existence.

For emerging organisations the future looks equally problematic. It is unlikely that major change inhibitors discussed in the chapter dealing with organisational emergence will be overcome, certainly in the short term. The fundamental problems in relation to a corrupt bureaucracy are unlikely to diminish, as the emerging political form in the Czech Republic is providing them with greater legitimate power. Additionally, due to the endemic nature of corruption in the system, it is unlikely that it will be eradicated. Moreover, the financial constraints under which they operate are likely to remain as long as the government's fiscal and monetary policy is committed to directing the majority of the available funding to the support of technically bankrupt state owned enterprises.

There is little doubt, however, that there is a substantial demand for goods and services in some areas, and that the rapid growth in the number of related small businesses is evidence of a strong entrepreneurial spirit in the region. Perhaps, most threateningly, however, is the fact that new business development and growth is a major channel through which criminal funding and activity is channelled, thus distorting and limiting the potential economic contribution of such businesses to the gross national product of the region.

NATIONAL CULTURAL CONTEXT

In the final analysis, policy decisions, evaluations and predictions of the likely future direction of the Czech Republic must be set within its unique national cultural context. This is to a great degree set within the historical development of the region from which it is possible to identify some of the main underlying cultural and behavioral traits of the country which will influence the nature of the transition at a macro and micro level.

The impact of the cultural characteristics of the nation, its value systems and resulting behaviours is well encapsulated by Bourdieu's concept of habitus (1994, p.95-97). In this context, habitus can be defined as a set of shared predispositions with respect to thought, speech and body language and the rituals of social interaction. Importantly, the habitus concept is not just a feature of individual personality but operates dialectically in a mutually re-enforcing way in the spaces between the individual, social interaction and institutional contexts.

The prescriptive behaviours emerging from this notion of habitus under the communist regime are well documented in the chapter on everyday life. Primarily, they comprise a tendency to adopt a particular set of behaviours in the public domain, characterised by acquiescent and deferential responses to the disciplinary controls of surveillance and

censorship and secretiveness that formerly pervaded the communist system. In private, however, the system was ridiculed. This double standard gave rise to the 'living in truth' condemnation of such behaviour amongst Czechs by Václav Havel (1987, p.62).

Some commentators have perceived this notion of habitus and its resulting behaviours as a direct result of communism. In fact, some of these cultural traits can be traced back to the period when the Czech Republic was under the domination of the Austro-Hungarian Empire which was also characterised by surveillance, secret police and a strong bureaucracy. Indeed, these habitus traits are exhibited in Hasek's novel of the Good Soldier Svejk (1973, p.15-18).

Concerning the likely impact of the behaviours implicit in this notion of habitus on the transition process, Stenson and Mills (1994, p.7) concluded that:

> The tendency to reproduce secretive and sometimes corrupt bureaucracies and for individuals to adapt to bureaucratic domination through humour and artful accommodation rather than through open resistance, is very deep-rooted in Czech culture and is unlikely to change simply through the adoption of neo-liberal economic reform.

These traits have major implications for foreign advisers and negotiators liaising with Czech nationals at a variety of levels. The culture and resulting behavioral

characteristics of the nation are unlikely to change, and as such must be accommodated by those foreigners who seek to interact with the Czech people. In the view of the author this behaviour is exhibited most manifestly by Václav Klaus. He talks of radical monetarism because that is what the foreign financiers and advisers wish to hear, but an analysis of the actual measures taken show them to be social democratic in nature.

At micro level, these behaviour traits could have negative implications for the effective functioning of organisations. The implicitly unpredictable and uncontrollable behaviour that emerges from this habitus notion underpins the absence of institutional trust, which was discussed in the chapter dealing with organisation transformation. This problem makes it very difficult for strategic decisions to implemented, if people do not do what they say they will do. It is necessary for enterprise managers, especially of foreign companies, to be aware of this cultural dimension of the Czech psyche and effect the appropriate management style to accommodate it. The difficulties experienced by foreigners in this area are well highlighted by the experiences of the Unisys manager discussed in the chapter dealing with organisational change.

THE WAY FORWARD

In many ways the Czech Republic was better placed than other East European countries to undertake the economic transition to a market-based economy. The low level of the inherited national debt, a relatively strong industrial base, a fortuitous geographical location. Additionally, the inter-war reputation of the short lived democracy and its highly skilled labour force is still prevalent in the minds of potential foreign investors. Finally, the international stature of Václav Havel as the President provided a powerful figurehead and role model for the embodiment of the democratic will of the country.

Has the government capitalised upon these opportunities in terms of its economic policy generally, and in relation to organisational change and development in particular? The author would argue that the government policies in this area are not conducive to optimising the long-term economic development of the country or the facilitation of the transition process generally. The government is faced with the choice of managing the inevitable de-construction and reconstruction of industry that must be undertaken if these enterprises are to function as economically viable units in a competitive global environment, or inhibiting the introduction of major change for as long as possible. It is hoped that, during this interim period, the economic environment will improve.

The author believes that the government has chosen the latter of these strategies by implementing policies to inhibit the change process and in so doing has decided to implement policies that are designed to inhibit the progress of change as opposed to managing it. It could have chosen to implement the bankruptcy legislation earlier. Concerning the restructuring of industry, the government could have channelled the funding which is being used to prop up former state-owned enterprises towards the development of small and medium-sized business activity.

The argument that the price in terms of social disruption would be too high is not, in the view of the author, a tenable one. So low is the reputation of the trades unions, as a result of their links to the communist regime, that they are unlikely to be able to mobilise much public opinion against government policy.

Additionally, throughout the history of the region, the Czech response to unpopular regimes or policies has been exhibited in terms of the habitus concept outlined above, rather than in direct confrontational opposition. The most recent example of this behaviour was the relative ease with which the 'Velvet Revolution' was effected.

The government could also have facilitated the process of transition more effectively by adopting a more conducive attitude to foreign investors. The market economy is

becoming an ever increasingly global concept and failure to encourage foreign investment is to lose opportunities for funding, technology, management expertise and potential access to foreign markets.

However, as economic and political pressures for change continue to increase, the government could find itself in a situation whereby it is no longer able to restrain or contain these forces. Thus, paradoxically, forces by which the government seeks to control the shape of economic activity could be wrested from its control, leaving the government relatively powerless to influence the ensuing chain of events.

It is to be hoped that, during this intervening period of grace, the development of a civil society, external pressure groups and an effective legal and regulatory system will create an environment which effectively challenge some of the governments economic policy measures.

Additionally, as politicians, business people and managers progress along the learning curve of democratic politics and market economy principles, it is to be hoped that their collective influence and expertise will increasingly influence the future economic development of the country. Within this temporal dimension, however, it must be remembered that the existing market economies continue to develop on an ongoing basis and it is possible to envisage

the gap between East and West becoming ever wider, especially in relation to technology.

From the perspective of organisations adjusting to this changing environment, their effectiveness in this regard will be greatly influenced by the development of the external groups outlined above insofar as they are direct stakeholders within these enterprises. Internally, successful transition will depend to some degree upon the extent to which internal stakeholders are willing and able to change and re-shape the future strategic direction of the organisation, undertake the major restructuring exercises and effect the culture change initiatives that must underpin it, if they are to survive.

The evidence suggests that this is unlikely to happen in the short term, especially where the government's continued support for ailing enterprises is sending signals to employees that their job security is guaranteed. A more realistic time span for effective organisational change may well stretch to the next generation, not least because these are the groups of management and employees who may well be forced to undertake massive restructuring or see the enterprises totally collapse. It is to be hoped that this new generation will have been educated into a new set of economic behaviours and attitudes that are more in congruence with the changed political, social and economic environment in which they find themselves.

Additionally, it is to be hoped that the evolution of an effective civil society will assist in the minimisation if not eradication of the corrupt bureaucratic institutions and organised crime, both of which are such potentially negative influences on the economic development of the country.

The best case scenario for the Czech Republic would be if the notion of 'wild west' capitalism which is often applied to the region, were to prove accurate. This would imply an evolutionary situation whereby the 'lawlessness' of the system would be superseded by a relatively ordered civil society, supported by an effective, legislative political framework.

The worst case scenario would emerge where bureaucratic corruption and organised crime became so imbedded within the system that they become too powerful and institutionalised to be controlled. The likely outcome in this situation would be an approximation to many of the worst features of say the Italian economic and political situation, i.e. a permanent black market economy.

The challenge faced by the Czech Republic in this regard is well encapsulated in the following quotation from R.H.S. Crossman (1943, p.239):

> The main task of a free society is to civilise the struggle for power. Slavery of the acquiescent majority to the ruthless few is the hereditary state of mankind: freedom, a rarely acquired characteristic.

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