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**PRICE WATERHOUSE - IPG  
PROJECTS IN CZECHOSLOVAKIA**

**JULY 1993**

**Under contract with the Bureau of Private Enterprise  
U.S. Agency for International Development**

*Price Waterhouse*  
International Privatization Group



July 14, 1993

Mr. Mark Karns  
USAID/Washington

Ms. Lee Roussel  
USAID/Prague

Ms. Patricia Lerner  
USAID/Bratislava

Dear Mr. Karns, Ms. Roussel and Ms. Lerner:

From September 1991 until the end of 1992, Price Waterhouse's International Privatization Group (PW/IPG) was involved in the following three activities in Czechoslovakia:

- I. Czech Republic Privatization and Development Project
- II. Slovak Republic Privatization and Development Project
- III. Czechoslovakia Privatization of Public Services

In addition to summarizing the work performed by PW/IPG on these three projects, the attached report indicates the status of those enterprises that PW/IPG assisted. We recently interviewed management or officials at a number of enterprises and several ministries in order to provide the most current information possible on these enterprises. Discussions of the current status of enterprises in the attached report rely exclusively on these interviews.

If you have any questions or if we can be of any further assistance, please contact Mr. James A. Waddell at (202) 778-1737 or Mr. William P. Mako at (202) 296-0800.

Very truly yours,

*Price Waterhouse*

## **I. CZECH REPUBLIC PRIVATIZATION AND DEVELOPMENT PROJECT**

In September 1991, Price Waterhouse's International Privatization Group (PW/IPG) began a project to provide technical assistance in privatization to the Ministry of Industry of the Czech Republic. This project consisted of two components: (1) Enterprise Valuation and Privatization, and (2) Technical Training. These two components are discussed in detail below, following a summary of project highlights.

### **A. Highlights**

PW/IPG received a challenging set of assignments in the Czech Republic. These included rendering advice and assistance on the privatization of two highly sensitive enterprises: the monopoly printer of newspapers in the Prague area and western Bohemia, and a film studio regarded as a national cultural treasure. In addition, PW/IPG undertook to find foreign partners for a former weapons component manufacturer severely hurt by Czechoslovakia's decision to curtail arms exports.

The major accomplishments of PW/IPG on the Czech Republic Privatization and Development Project are as follows:

- o Three of the four enterprises assigned to PW/IPG have been successfully privatized.
- o Valuation work done by PW/IPG supported the Czech Ministry of Privatization and the Fund for National Property in obtaining an additional Kcs 40 million (about \$1.5 million) from a U.S. investor for its initial purchase of shares in a Czech manufacturing company (Ferox).
- o PW/IPG trained 117 officials or senior managers from the Ministry of Industry, Ministry of Privatization, Fund for National Property, and companies being privatized in business analysis, valuation, and privatization methods and issues. In addition, PW/IPG trained 100 officials or senior managers from the Fund for National Property, investment privatization funds, and companies in their new responsibilities as corporate directors and in practical approaches to corporate oversight and restructuring.

### **B. Enterprise Valuation and Privatization**

Enterprise Valuation and Privatization included developing criteria for the selection of four enterprises to be privatized and assisting in the selection process. As needed, Enterprise Valuation and Privatization also included conducting a thorough appraisal of each of the four enterprises; deriving a set of recommendations on operational and/or financial restructuring that should be undertaken prior to privatization; constructing a model to project future operating and financial performance; conducting a valuation of the enterprise; developing a privatization implementation plan; and assisting in the completion of the transactions.

Based on discussions with the Ministry of Industry and other interested parties, PW/IPG selected the following enterprises in the Czech Republic for assistance:

- o Ferox
- o Filmove Studio Barrandov
- o Ceska Typografie
- o Elton

The following discussion summarizes, for each enterprise, the work performed and the status of the enterprise based on the most current information available.

### 1. Ferox

When PW/IPG began working with Ferox, this manufacturer of industrial containers and cryogenic equipment was engaged in negotiations with Air Products, a U.S. company. Air Products was seeking to acquire a significant portion of Ferox's shares.

Work performed. PW/IPG provided major support to the Czech side in these negotiations. This support included preparation of an enterprise valuation; review of draft purchase documentation; and advice to Ferox's Board of Directors on possible improvements in the terms relating to such matters as future capital investment, training, technology transfer, and corporate governance.

In preparation for developing a valuation and supporting the negotiations, PW/IPG undertook the following activities:

- o Interviewing Ferox's management to understand the company's operational and financial situation;
- o Working with an industry expert from the U.S. Industrial Gas Association to evaluate Ferox's production and marketing operations;
- o Converting company financial statements into a Western format and making adjustments to bring these statements more into line with Western accounting principles;
- o Meeting with industry consultants and with members of Price Waterhouse's corporate finance group to collect, for valuation purposes, financial information on comparable Western companies and transactions;

- o Developing financial projections and discounted cash flows as part of our valuation of Ferox; and
- o Developing a database of major Western investments in Czechoslovakia, for use in all of PW/IPG's valuations in Czechoslovakia.

Enterprise status. Ferox was privatized during the first wave through a combination of coupon privatization and a direct sale of shares to Air Products. Of the 125,212 shares reserved for coupon privatization (43% of the total), 97% were distributed to Czechoslovak citizens as a result of coupon privatization.

The transaction involving Air Products was concluded in September 1992. Air Products agreed to purchase 51% of Ferox's shares for Kcs 173 million and subsequently to invest another Kcs 170 million in Ferox in return for additional shares, which will raise Air Products' ownership to 68%. Air Products' combined investment of Kcs 343 million (about \$12.7 million) indicates a post-investment market value for Ferox of about Kcs 500 million. The purchase agreement also provided for training and technology transfer.

PW/IPG played a major role in helping the Czech Republic obtain additional value for Ferox. In January 1992, PW/IPG provided a final valuation report to Ferox's Board of Directors and to the Ministry of Industry. The Ministry of Industry subsequently forwarded our valuation report to the Ministry of Privatization, which concluded negotiations with Air Products. Based on earlier valuation work by Ernst & Young, initial negotiations with Air Products had posited a value of Kcs 260 million (about \$9.6 million) for Ferox. Our analysis, however, suggested a minimum value of Kcs 573 million (\$21.2 million) for the company. We also reviewed our valuation work with both Ferox's Board of Directors and with representatives from Air Products.

At a minimum, the valuation work done by PW/IPG helped the Czech Republic to obtain an additional Kcs 40 million (\$1.5 million) from the sale of 51% of Ferox's shares.

Industrial gases promises to be a high growth market in the Czech Republic and other former COMECON countries, as well as Western Europe. While well positioned to serve this market, Ferox needed additional financial resources, improvements in production, and marketing knowhow that Air Products can provide. Discussions with Ferox's management in June 1993 indicated that Air Products will invest Kcs 100 million in Ferox in 1993, that Air Products personnel are heavily involved in Ferox's operations, that Ferox personnel have received training in the United Kingdom, and that Air Products has established sales representatives for Ferox in the U.K. Thus, its partnership with Air Product's should significantly enhance Ferox's ability to respond to market opportunities and to increase its profitability.

## **2. Filmove Studio Barrandov (FSB)**

A repository of current film-making capability and tradition in the Czech Republic, FSB is regarded as a national cultural asset. FSB's legacy includes such well-known Czech productions as Loves of a Blonde and Closely Watched Trains as well as work on various Western productions, including Amadeus. FSB's privatization and future viability was a matter of significant concern to the Czech public and government. In response to a request from the Ministry of Culture of the Czech Republic, PW/IPG served as privatization advisors to FSB management.

Work performed. At the start of this engagement, it appeared that FSB's privatization would involve foreign equity investment or bank financing. On that basis, PW/IPG undertook a business analysis and valuation effort that involved the following activities:

- o Converting company financial statements into Western formats and making adjustments to bring these statements more into line with Western accounting principles;
- o Meeting with industry consultants and with members of Price Waterhouse's corporate finance group to collect, for valuation purposes, financial information on comparable Western companies and transactions;
- o Developing financial projections and discounted cash flows;
- o Reviewing the privatization plan submitted by FSB management; and
- o Meeting with the Minister of Culture, company management, the company's legal counsel, and a representative of the British Know-How Fund to refine our understanding of privatization issues and alternatives.

Subsequently, PW/IPG reviewed a business plan developed by U.K. consultants funded by the British Know-How Fund. In particular, PW/IPG offered comments on plans for asset dispositions, reorganization of operating divisions, and approaches to prospective investors.

Current status. Privatization through a direct sale of FSB shares to the Cinepont management group was approved by the Czech government in June 1992. Cinepont's purchase, at book value, has been financed through a 10-year interest-free loan from the Fund of National Property (FNP), with the first payment due in January 1995. This privatization transaction encompassed substantial real estate assets in Prague, including property on Wenceslas Square and in Mala Strana as well as the studio on the Barrandov estate.

As of June 1993, FSB's management expressed guarded views on the company's film-making prospects and indicated an emphasis on real estate development projects and/or foreign equity investment to offset projected revenue shortfalls from film-making.

Over the last year, the number of employees at FSB (excluding Film Laboratories) has decreased from about 700 to 600. In addition, management has scaled back its plans for producing Czech films from 5 per year to 2-3 per year. This change reflects management's estimate that 6-8 years are required to recoup the investment in each production because of the relatively small size of the Czech film public. The provision of production services to Western film-makers could be a significant source of revenues. In 1991-1992, FSB provided production services for two U.S. productions, Young Indy and Swing Kids. Currently, FSB has contracts for about Kcs 100 million to provide services for four West European productions. Because of its location, low costs, and technical quality, FSB should be attractive to Western film-makers. Overall, management sees a need for significant additional revenues to break even this year.

Currently, FSB is contemplating several new business ventures. These include investment in a Czech television channel, purchase of the distribution company Filmexport, and production of Czech television programming.

FSB's management is pursuing several real estate development projects as well as foreign investment. FSB has received two offers (1 Czech, 1 Austrian) to develop an exhibition center or shopping center on FSB's property adjoining a major highway to Plzen. In addition, it appears that McDonalds' (U.S.) will help develop FSB's property in Mala Strana. While discussions with Paramount (U.S.) and Columbia Pictures (U.S.) regarding an investment in FSB proved inconclusive, management hopes that further reorganization will make the company more attractive to foreign investors. There is current interest from a Hong Kong company in one of Barrandov's divisions. In addition, FSB's management has approached the European Bank for Reconstruction and Development (EBRD) in pursuit of a \$5 million investment to be used for refurbishment of buildings and production equipment.

### **3. Elton**

Prior to 1989, Elton profited from the production of medium-quality timepieces for the Czechoslovak and East European markets and precision parts for Czechoslovakia's armaments industry. The federal government's decision, after 1989, to curtail arms exports by Czechoslovakia severely reduced Elton's revenues and profits.

Work performed. PW/IPG undertook to produce an information memorandum designed to attract foreign equity investment, one or more foreign joint venture partners, or additional export orders. Because Elton's financial results had been severely distorted by federal policy on arms exports, this information memorandum focused on current production capacity and assets. Preparation of this information memorandum involved the following activities:

- o Working with Elton's management to develop a detailed list of production equipment;
- o Obtaining, from an expert appraiser, estimates of current market values for production equipment;

- o Using an industry expert to identify alternative industrial uses for Elton's production equipment;
- o Working with management to develop detailed information on the current workforce;
- o Acquiring information on Elton's current product line and customers; and
- o Converting company financial statements into Western formats and making adjustments to bring these statements more into line with Western accounting principles.

This information memorandum was presented to the management of Elton. In addition, drawing upon the analysis by our industry expert and upon Price Waterhouse's corporate finance group, PW/IPG provided Elton's management with a list of potential investors, joint venture partners, or customers.

In addition, PW/IPG met with two potential investors and advised Elton on its negotiations. These negotiations concluded when it became apparent that these two approaches were essentially attempts to obtain concessions on product purchases from Elton.

Current status. Elton was privatized during the first wave through coupon privatization. Of the 201,190 shares reserved for coupon privatization (97% of the total), 89% were distributed through coupon privatization while 11% remain with the FNP.

Elton has attracted at least four significant new customers from Western Europe. Three of these are customers for precision parts, the product line most severely affected by the federal policy on arms exports.

Although no employees have been laid off since last summer, Elton continues to face financial difficulties. Sales to Slovakia have decreased by almost two-thirds since dissolution of the federation. The company experienced a small loss during the first half of 1993, although management hopes to break even or achieve a small profit by year-end. These hopes are based on renewed efforts to market directly to small retailers and a new wholesale/distribution joint venture with an investment fund owned by the Panok retail chain. Production remains at about 60% of capacity. Timepieces currently account for about 90% of Elton's sales, indicating significant underutilization of the precision parts division.

Despite these difficulties, Elton's computer-controlled precision machining and other production equipment and its skilled workforce have significant potential. Elton would be an attractive candidate for defense conversion and restructuring assistance.

#### **4. Ceska Typografie**

In 1991, Ceska Typografie printed about 46% of the daily newspapers printed in the Czech Republic and as much as 70% of the daily newspapers printed in the Prague area and western Bohemia. After 1989, when the company printed 1 million copies a day of Rude Pravo, Ceska Typografie's operation underwent a major transformation. By 1991, Ceska Typografie had a combined daily press run of over 1.2 million for 14 daily newspapers.

The company's founding ministry, the Ministry of Privatization (MoP), had a strong interest in privatizing Ceska Typografie. The MoP and other interested parties, however, had a number of additional goals which were difficult to reconcile. These included the following: improving customer service, preventing abuse of Ceska Typografie's market dominance, attracting capital investment, avoiding foreign dominance, and allowing the development of integrated newspaper publishers/printers in the Czech Republic.

At the Ministry of Privatization's request, PW/IPG undertook to advise the MoP on how to privatize Ceska Typografie. This had been a matter of intense debate within both the Czech government and the press. Because of a high degree of sensitivity resulting from the company's domination of the newspaper printing market, the MoP believed it important to gain information and to have access to independent expert views on the privatization of Ceska Typografie.

Work performed. PW/IPG recommended that 77-97% of Ceska Typografie's shares be offered to the public in the first wave of coupon privatization, with the remainder going to management and employees or remaining with the FNP. In addition, PW/IPG recommended certain "golden share" powers for the Czech Government, including the right to initiate the search for a foreign investor; limitations on concentration of share ownership; and several provisions for avoiding anticompetitive behavior. These recommendations were based on the following work:

- o Meeting with a number of newspaper publishers and other interested parties to obtain their views on Ceska Typografie's privatization;
- o Evaluating current capabilities in newspaper publishing, printing, and distribution in the Czech Republic;
- o Utilizing an industry expert to assess likely trends in newspaper publishing, printing, and distribution;
- o Working with management and using an industry expert to develop an understanding of Ceska Typografie's customer base, production capabilities, and capital investment requirements;
- o Reviewing a series of ownership and legal issues; and

- o Developing cash flow projections and information on comparable companies and transactions in order to develop a range of market values for Ceska Typografie.

In addition, PW/IPG reviewed a proposal for a management buy-out of Ceska Typografie and provided comments to the Ministry of Privatization. These comments encouraged the MoP to reject this proposal.

Current status. In mid-1991, the Ministry of Economic Development and Policy (now within the Ministry of Economy) replaced the MoP as Ceska Typografie's founding ministry. Two factors in this decision were concern about the potential for monopoly abuse and a determination that Ceska Typografie, as former Communist Party property, should be held in trust for humanitarian purposes. The Government will not put any additional funds into Ceska Typografie. The Ministry of Economy, which currently holds 100% of the company's shares, plans a phased privatization of Ceska Typografie. As appropriate, the company will issue one or more tranches of new shares but will limit any purchaser's ownership to 15% of the total. The government will retain at least 34% of total shares until it determines that Ceska Typografie no longer dominates the newspaper printing market, defined as 30% market share. At that time, the Ministry of Economy plans to sell of its Kcs 1.3 billion book value worth of stock. Sale proceeds will be transferred to the National Health Insurance Fund, which finances medical care and income supplements.

### **C. Technical Training**

As originally intended, Technical Training was to include six five-day workshops providing hands-on privatization training for middle and senior level Ministry of Industry staff and their counterparts. In fact, PW/IPG developed two courses -- on privatization, and on corporate governance -- a conducted a combined total of 13 workshops in the Czech Republic, as discussed below.

#### **1. Course on Privatization**

This course sought to strengthen the skills of Ministry officials in four technical areas: how to assess an enterprise's performance and its ability to compete in a market economy; how to determine a reasonable range of market values for an enterprise; how to select the most appropriate privatization method or combination of methods given an enterprise's strengths and weaknesses, investor interest, and public policy considerations; and how to negotiate with investors.

Work performed. Development and conduct of this course involved the following activities:

- o Developing a course curriculum that includes modules on the privatization process and experience, basic tools and analytic concepts for evaluating business performance, valuation techniques and problems, and privatization methods and issues;

- o Holding a preview for senior officials of the Czech Ministry of Industry who would either participate in the actual workshop or assign staff to participate in order to reach agreement on the key components and structure of this program;
- o Recruiting local trainers from business and management training institutions;
- o Writing a privatization primer to provide background information on finance, accounting, and marketing terms and concepts important for evaluating privatization projects;
- o Developing technical notes and case studies for use in the privatization workshops; and
- o Training local and expatriate trainers in course materials and approaches prior to the first workshop.

**Results.** PW/IPG conducted the Privatization Course at 7 workshops. Trainee participants totalled 117, including 75 officials from the Czech Ministry of Industry, 15 managers from state-owned enterprises being privatized, and 27 officials from the Czech Ministry of Privatization or the Fund for National Property. This course was extremely well received by both the participants and their sponsoring institutions.

## **2. Course on Corporate Governance**

Responding to interest from the Fund for National Property of the Czech Republic in helping new directors on the boards of newly privatized companies to discharge their responsibilities, this course focused on four technical areas: the role and operating environment of corporate boards; how to evaluate a company's strategic position, cash situation, and financing needs; how to evaluate restructuring alternatives in light of Czechoslovakia's emerging bankruptcy law and financial market infrastructure; and how to improve the performance of corporate boards during crisis situations.

**Work performed.** Development and conduct of this course included the following activities:

- o Interviewing officials from the Fund for National Property to assess training needs;
- o Developing a course curriculum that includes modules on the corporate environment, strategic analysis, financial analysis, sources of financing, crisis management, restructuring, and board operations;
- o Acquiring training videos on relevant topics and dubbing them into Czech;
- o Recruiting local trainers from business and management training institutions;

- o Developing technical notes and case studies for use in the corporate governance workshops; and
- o Training local and expatriate trainers in course approaches and materials prior to the first workshop.

Results. PW/IPG conducted the Corporate Governance Course at 6 workshops. Trainee participants totalled 100, including 15 officials from the Fund for National Property of the Czech Republic (FNP), 11 senior managers from investment privatization funds, and 74 directors or senior managers from companies undergoing privatization. The FNP and other sponsoring institutions provided about 30% of the costs of these workshops, which were usually oversubscribed. The workshops were extremely well received. Participants were virtually unanimous in their assessment that the course provides relevant and important information and guidelines for carrying out their responsibilities as corporate directors.

## **II. SLOVAK REPUBLIC PRIVATIZATION AND DEVELOPMENT PROJECT**

In September 1991, Price Waterhouse's International Privatization Group (PW/IPG) began a project to provide technical assistance in privatization to the Ministry of Industry of the Slovak Republic, later succeeded by the Slovak Ministry of Economy. This project consisted of two components: (1) Enterprise Valuation and Privatization, and (2) Technical Training. These two components are discussed in detail below, following a summary of project highlights.

### **A. Highlights**

PW/IPG's assignments in Slovakia, which focused on the troubled textile sector, were highly challenging. The major accomplishments of PW/IPG on the Slovak Republic Privatization and Development Project are as follows:

- o As a result of negotiating advice and assistance by PW/IPG on foreign investment in a building materials company (Izomat), the purchase price proposed by a prospective investor has increased by at least 50% from the initial offer. The Ministry of Economy is confident that a letter of intent will be signed in the near future and that the company will be privatized in the second wave.
- o Through development of an information memorandum and conduct of an investor search, PW/IPG attracted two prospective foreign investors that the Ministry of Economy expects will purchase shares in one textile company (Gemtex) as part of its second wave of privatization.
- o PW/IPG advised the Ministry of Economy on the privatization of 16 textile companies identified for the second wave of privatization. The Minister of Economy and other Ministry officials expressed strong support for PW/IPG's recommendations and findings. In addition, the Minister of Finance made a request to USAID that PW/IPG be contracted to provide restructuring and foreign investment assistance to selected companies in Slovakia's textile, leather, and glass sectors.
- o PW/IPG trained 32 officials or senior managers from the Ministry of Industry, Ministry of Agriculture, Ministry of Forests and Waters, and companies being privatized in business analysis, valuation, and privatization methods and issues. Almost all participants felt that this training provided important information and practical approaches for carrying out their various responsibilities.

## **B. Enterprise Valuation and Privatization**

Enterprise Valuation and Privatization included developing criteria for the selection of four enterprises to be privatized and assisting in the selection process. As needed, Enterprise Valuation and Privatization also included conducting a thorough appraisal of each enterprise; deriving a set of recommendations on operational and/or financial restructuring that should be undertaken prior to privatization; constructing a model to project future operating and financial performance; conducting a valuation of the enterprise; developing a privatization implementation plan; and assisting in the completion of the transactions.

Based on discussions with the Ministry of Industry and other interested parties, PW/IPG selected the following enterprises in the Slovak Republic for assistance:

- o Izomat
- o Gemtex
- o Tatral'an
- o Slovena

In addition, at the request of the Slovak Ministry of Industry (superseded by the Ministry of Economy), PW/IPG reviewed privatization projects for 16 textile companies designated for the second wave of privatization and advised the Ministry on appropriate privatization methods.

The following discussion summarizes, for each enterprise and for the textile sector project, the work performed and the status of these enterprises based on the most current information available.

### **1. Izomat**

A low-cost producer of building insulation materials, Izomat is well-positioned to respond to emerging markets and to attract foreign investment. Several companies from the U.S. and Western Europe have expressed interest in investing in Izomat and conducted due diligence and preliminary negotiations. To support the due diligence and negotiation process, PW/IPG has undertaken the following work on behalf of Izomat:

- o Developing a preliminary understanding of Izomat's marketing operations, production, organization, and management;
- o Converting company financial statements into a Western format and making adjustments to make these statements more meaningful to prospective investors;

- o Developing summaries of Izomat's operations and finances, and providing these summaries to companies interested in Izomat;
- o Meeting with companies that have expressed an interest in Izomat in order to understand their objectives and answer additional questions about Izomat's product line, finances, production, and capital requirements;
- o Developing cash flow projections and a range of values for Izomat based on discounted cash flows and comparable companies and transactions;
- o Contacting additional potential investors and meeting with some in order to provide additional information on Izomat;
- o Exploring with Izomat's management the possibility of a direct purchase of some shares by management;
- o Attempting to resolve issues on price, payment terms, post-privatization employment, and environmental indemnities through iterative negotiation sessions with prospective investors, Izomat management, and the Ministry of Industry; and
- o Arranging for one potential investor, a U.S. company, to receive a briefing from the U.S. Consul General in Bratislava on the political and economic situation in Slovakia.

Current status. By February 1993, negotiations were focusing on investment by a Danish company, perhaps with participation by the Danish Investment Fund for Eastern Europe. A preliminary letter of intent, with a price level 50% above the original offer, has been discussed with this Danish company. As of June 1993, the Ministry of Economy expected that a letter of intent would be signed in the near future.

## **2. Gemtex**

This knitwear manufacturer located in Rozhnava had reasonably good management, but needed a foreign investor to help it develop export sales.

Work performed. To help find a foreign investor for Gemtex, PW/IPG developed an information memorandum, which involved the following activities:

- o Developing information summaries on Gemtex's product lines, production, management, and workforce;
- o Converting company financial statements into a Western format and making adjustments to make these statements more meaningful to prospective investors;

- o Developing an updated discussion of key considerations for potential Western investors;
- o Developing cash flow projections and estimating Gemtex's value based on discounted cash flows and comparable companies and transactions;
- o Drafting a complete information memorandum; and
- o Developing a list of prospective investors and providing a summary of the information memorandum to these prospective investors.

Subsequently, PW/IPG helped arrange for a prospective Italian investor to travel to Gemtex and begin due diligence procedures.

Current status. The Italian company has proposed to make an investment in Gemtex. Negotiations with the Italian company are continuing. In addition, Gemtex has received an additional offer from a foreign trading company. As of June 1993, the Slovak Ministry of Economy expected that Gemtex's privatization will include a direct sale of shares to at least one of these prospective investors.

### **3. Tatral'an**

This company has a diverse product line. It includes linen and half-linen products for consumers and non-woven textiles for such industrial uses as construction and automobile production. PW/IPG was asked by the Ministry of Industry to attempt to find a foreign investor.

Work performed. In support of the search for a foreign investor, PW/IPG developed and distributed an information memorandum and undertook a valuation of Tatral'an. This involved the following activities:

- o Collecting and analyzing information on Tatral'an's marketing, production, and management;
- o Working with an industry expert to develop an understanding of Tatral'an's plant and production operations;
- o Converting the company's financial statements into a Western format and making adjustments to make these financial statements more consistent with Western accounting principles;
- o Developing cash flow projections and using discounted cash flows and information on comparable companies and transactions to estimate Tatral'an's value;

- o Developing a list of almost 200 prospective investors in the U.S., Western Europe, Middle East, and Asia and identifying key contacts at these companies;
- o Completing the information memorandum as well as a 2-page summary; and
- o Sending the information memorandum summary to almost 200 prospective investors and following up with telephone or fax messages to key contacts.

Current status. At least 11 companies asked to review the complete information memorandum. Of these, one Italian manufacturer of non-woven textiles showed further interest. PW/IPG arranged for representatives from this company to travel to Kezmarok and meet with Tatral'an's management. Preliminary negotiations ended, however, because of disagreement about market prospects and product demand and development. As of June 1993, the Slovak Ministry of Economy expects that Tatral'an will be privatized during the second wave of privatization through public tender.

#### 4. Slovena

Slovena produces woolen fabric. This is the most distressed segment of Slovakia's textile industry. PW/IPG was asked by the Ministry of Industry to try to find a foreign investor for Slovena.

Work performed. In support of the search for a foreign investor, PW/IPG developed and distributed an information memorandum and undertook a valuation of Tatral'an. This involved the following activities:

- o Collecting and analyzing information on Slovena's marketing, production, and management;
- o Working with an industry expert to develop an understanding of Slovena's plant and production operations;
- o Converting the company's financial statements into a Western format and making adjustments to make these financial statements more consistent with Western accounting principles;
- o Developing cash flow projections and using discounted cash flows and information on comparable companies and transactions to estimate Slovena's value;
- o Developing a list of almost 200 prospective investors in the U.S., Western Europe, Middle East, and Asia and identifying key contacts at these companies;
- o Completing the information memorandum as well as a 2-page summary; and

- o Sending the information memorandum summary to almost 200 prospective investors and following up with telephone or fax messages to key contacts.

Current status. At least 6 companies asked to review the complete information memorandum. Of these, one U.S. manufacturer of blankets showed further interest. PW/IPG arranged for representatives from this company to travel to Zilina and meet with Slovena's management. The U.S. company decided against any investment at this time but did purchase product from Slovena.

Slovena is experiencing serious financial problems and finding it difficult to obtain supplies. As of June 1993, the Ministry of Economy plans to stabilize production at Slovena and perhaps restructure the company before making any decision on its privatization.

### **5. Textile Sector Privatization**

PW/IPG was asked by the Ministry of Industry (subsequently absorbed by the Ministry of Economy) to advise the ministry on the privatization of 16 textile companies designated for the second wave of privatization. The textiles sector is an important, but particularly troubled, portion of Slovakia's economy. Together, these 16 companies employed over 28,000 workers in 1991.

Work performed. In order to advise the Ministry on the second wave privatization of these 16 companies, PW/IPG undertook the following activities:

- o Reviewing basic privatization projects filed by the companies, as well as a number of competing privatization projects;
- o Reviewing company financial statements for indications of profitability and liquidity;
- o Visiting each company with a team that included an industry expert in order to obtain a better understanding of product line quality, marketing effectiveness, production capabilities and deficiencies, capital investment requirements, and managerial strengths and weaknesses;
- o Recommending a specific privatization method or combination of methods for each company to working groups at the Ministry;
- o Providing additional observations on company strengths and weaknesses and any restructuring requirements; and
- o Briefing Ludovit Cernak, the Slovak Minister of Economy, on our findings and recommendations.

Both the Minister of Economy and the Director of Light Industry at the Ministry of Economy expressed strong support for the recommendations and observations presented by PW/IPG. They indicated that PW/IPG's work would be extremely useful to the Ministry in choosing appropriate privatization methods for these 16 textile companies.

Eight of the 16 companies were in severe need of restructuring and foreign investment assistance. The Minister of Economy made a request to USAID that PW/IPG be contracted to provide such assistance.

Current status. The textile sector remains an important but troubled portion of Slovakia's economy. The basic problem is that under COMECON planning, Czechoslovakia's textile sector was sized to produce for 50 million consumers in Eastern Europe and the Soviet Union. The collapse of COMECON trading arrangements and the Soviet Union left Czechoslovakia with a textile industry (concentrated in Slovakia) sized to service 50 million customers but enjoying ready access to only 10 million Czechs and 5 million Slovaks. Dissolution of the Czechoslovak federation has further hindered access to Czech markets.

Some portions of Slovakia's textile sector are doing better than others. While woolen producers are experiencing severe difficulties, knitwear manufacturers are having some success in adapting to free market conditions and entering Western markets.

The Slovak textile sector desperately needs the access to capital, knowhow, and export markets that foreign investment can provide. To date, however, little foreign investment in the Slovak textile sector has occurred. A key cause of this, in the current view of the Slovak Ministry of Economy, is the need to restructure Slovak textile companies.

The privatization of about half of these textile companies is proceeding as part of Slovakia's second wave of privatization. The emphasis in Slovakia has shifted somewhat from coupon privatization to privatization through public tender. In general, however, the Ministry of Economy's current plans are consistent with the recommendations presented by PW/IPG in August 1992. As of June 1993, the Slovak Ministry of Economy indicated the following plans for these companies:

- o Finis, a knitwear producer in Spiska Nova Ves, will be privatized through a direct sale to management and a foreign partner. The Ministry of Economy has submitted this proposed purchase to the Ministry of Privatization for approval.
- o LKZ, a linen fiber and carpet producer in Holic, did not succeed in its negotiations with a potential foreign investor. This company may be offered for public tender.
- o Levitex, a yarn and non-woven textile manufacturer in Leviec, will be reorganized into two companies. The Ministry of Economy will monitor their performance before deciding on privatization.

- o Luna, a knitwear producer in Nitra, will be privatized through public tender. The Ministry of Economy has forwarded investor proposals and its recommendations to the Ministry of Privatization for approval.
- o LTZ, a linen fabrics and products manufacturer in Revuca, has received some joint venture offers for its linens line and its glass fiber products line. Letters of intent have been signed with two foreign companies.
- o Makvta, a garment company in Puchov, may be privatized through public tender.
- o Modus, a knitwear producer in Kosice, has been liquidated.
- o OZKN Presov, a manufacturer of ready-made outerwear garments, is continuing negotiations with a prospective foreign investor.
- o OZKN Svikon Svidnik, another manufacturer of ready-made outerwear garments, has been sold through public tender to a combination of domestic investors and GFT, an Italian textile company.
- o Pol'ana, a wool fabric and products company in Lucenec-Opatova, has been reorganized into several companies. The Ministry of Economy will monitor the performance of these companies before deciding on their privatization.
- o Pratex, a wool fabrics and products company in Cadca, has an uncertain future. The Ministry of Economy feels that Pratex will not survive unless it is restructured and attracts a foreign partner.
- o Selanka, a knitwear producer in Turzovka, will be privatized through public tender. The Ministry of Economy has forwarded investor proposals and its recommendations to the Ministry of Privatization for approval.
- o Slovenka, a knitwear producer in Banska Bystrica, will be privatized through a direct sale to management. The Ministry of Economy has submitted this proposed purchase to the Ministry of Privatization for approval.
- o Trikota, a knitwear producer in Vrbove, will be privatized through public tender. The Ministry of Economy has received proposals from domestic investors with foreign backing. The Ministry of Economy is reviewing proposals and expects to submit these proposals and its recommendations to the Ministry of Privatization for approval in the near future.

- o UMOV, a textile machinery producer in Trencin, will be privatized through public tender. The Ministry of Economy is reviewing proposals and expects to submit these proposals and its recommendations to the Ministry of Privatization for approval in the near future.
- o Zornica, a knitwear company in Banovce and Bebravou, will be privatized through public tender. The Ministry of Economy is reviewing proposals and expects to submit these proposals and its recommendations to the Ministry of Privatization for approval in the near future.

Thus, progress is being made on privatization of 13 of these 16 textile companies. A number of these companies, however, are continuing to experience varying degrees of difficulties, as are Slovena and Tatral'an. The Ministry of Economy remains interested in USAID support for restructuring and finding foreign partners for a number of companies in Slovakia's important but troubled textile sector.

### **C. Technical Training**

As originally intended, Technical Training was to include six five-day workshops providing hands-on privatization training for middle and senior level Slovak Ministry of Industry staff and their counterparts. Because of the relatively small size of this Ministry, PW/IPG was able to meet its training needs in 3 workshops.

The Privatization Course sought to strengthen the skills of Ministry officials in three technical areas: how to assess an enterprise's performance and its ability to compete in a market economy; how to determine a reasonable range of market values for an enterprise; and how to select the most appropriate privatization method or combination of methods given an enterprise's strengths and weaknesses, investor interest, and public policy considerations.

Work performed. Development and conduct of this course involved the following work:

- o Developing a course curriculum that includes modules on the privatization process and experience, basic tools and analytic concepts for evaluating business performance, valuation techniques and problems, and privatization methods and issues;
- o Holding a preview for senior officials of the Slovak Ministry of Industry who would either participate in the actual workshop or assign staff to participate in order to reach agreement on the key components and structure of this program;
- o Recruiting local trainers from business and management training institutions;

- o Writing a privatization primer to provide background information on finance, accounting, and marketing terms and concepts important for evaluating privatization projects;
- o Developing technical notes and case studies for use in the privatization workshops; and
- o Training local and expatriate trainers in course materials and approaches prior to the first workshop.

Results. PW/IPG conducted the Privatization Course at 3 workshops. Trainee participants totalled 32 including officials from the Slovak Ministry of Industry, Ministry of Agriculture, Ministry of Forests and Waters, and managers from state-owned enterprises being privatized. This course was extremely well received by both the participants and their sponsoring institutions.

### **III. CZECHOSLOVAKIA PRIVATIZATION OF PUBLIC SERVICES**

PW/IPG was asked to provide technical assistance in the privatization of municipal services, focusing particularly on the provision of solid waste management services by the private sector. While this project's original design called for a feasibility study of private participation in solid waste management, a subsequent scope of work modification outlined a more practical approach involving direct technical assistance to two municipalities (one in each republic) in their efforts to transfer municipal services to the private sector.

With remaining resources, PW/IPG conducted two technical training sessions (one in each republic) to provide municipal leaders with guidelines and performance indicators for their efforts to privatize municipal services.

These two components, direct technical assistance and technical training, are discussed in detail following a summary of project highlights.

#### **A. Highlights**

Municipalities in Czechoslovakia were extremely interested in privatization of municipal services because of severe constraints on municipal budgets. It was for this reason that the focus of this project shifted from an assessment of feasibility to practical technical assistance. The major accomplishments of PW/IPG on the Czechoslovakia Privatization of Municipal Services Project are as follows:

- o In its privatization of municipal waste disposal (landfilling) services, Hradec Kralove (in the Czech Republic) implemented PW/IPG's recommendations, concluding a contract that safeguards the interests of the community.
- o In its privatization of municipal waste collection services, Trnava (in the Slovak Republic) implemented PW/IPG's recommendations, placing a particular emphasis on contract monitoring and information systems and bid evaluations.
- o In two separate training sessions organized by PW/IPG, 74 officials from 67 municipalities received training in issues and guidelines for the privatization of municipal services. The great majority of participants indicated that these training sessions will be of great practical assistance in their efforts to transfer delivery of municipal services to the private sector.

## **B. Direct Technical Assistance**

In addition to providing specific technical assistance to Hradec Kralove and Trnava, PW/IPG positioned itself to provide more general assistance to municipalities throughout Czechoslovakia in the area of municipal services privatization.

Work performed. As a starting point, PW/IPG undertook an analysis of municipal services privatization activity throughout Czechoslovakia and identified practical solutions to common problems. This involved the following activities:

- o Meeting with officials in a number of municipalities to assess municipal services privatization activity and issues;
- o Conducting a survey of privatization activity by a number of municipalities in order to identify "best practices;"
- o Collecting cost and equipment information from several municipalities;
- o Meeting with acknowledged private sector leaders in municipal services privatization in order to identify proven practical approaches that could be replicated in other municipalities;
- o Reviewing draft or final contracts in several municipalities;
- o Developing guidelines on contracting procedures, financial analysis, measurement of operational efficiency, and contract monitoring.

Relevant sections from the report were translated into Czech or Slovak and provided to officials in Hradec Kralove and in order to support their ongoing contract negotiations and in Trnava to guide the implementation of monitoring and information systems. PW/IPG supplemented this with additional commentary and advice on draft contracts.

Results. Recommendations by PW/IPG were implemented by Trnava in its negotiations over the privatization of waste collection services and by Hradec Kralove in its negotiations over the privatization of the public landfill. Officials in both municipalities indicated that PW/IPG's recommendations significantly improved the terms of their contracts, served the public interest, and contributed to public support for privatization.

### **C. Technical Training**

In order to accelerate the privatization of municipal services throughout Czechoslovakia, PW/IPG undertook to organize two technical training sessions (one in each republic) in order to disseminate lessons learned in Czechoslovakia as well as from experiences in the United States.

Work performed. Organization of these technical training sessions included the following activities:

- o Developing a training schedule that covered privatization issues, infrastructure financing, foreign joint ventures, environmental and political issues, financial and operational analysis, and contract monitoring;
- o Arranging for several U.S. experts, including two officials from the City of Phoenix, and officials from several municipalities in Czechoslovakia to speak on their experiences in municipal privatization; and
- o Developing a set of background training materials for participants.

Results. Two 2-day training sessions were held in Prague and Bratislava. In addition to scheduled presentations, working group sessions gave Czechoslovak mayors, deputy mayors, city managers, and heads of municipal finance departments an opportunity to share their experiences and concerns. The working group sessions also afforded an opportunity for these municipal officials to apply the concepts from the presentations to specific problems in order to identify alternatives and solutions applicable to Czechoslovakia local communities. Each working group was responsible for discussing local situations and presenting proposed solutions to the audience.

These training sessions were very well received. Participants indicated that this training was highly relevant to immediate issues in the area of municipal services privatization.