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**ENERGY AND TELECOMMUNICATIONS SECTOR ASSISTANCE  
FOR THE CZECH REPUBLIC**

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**PRELIMINARY PRIVATIZATION PLAN FOR  
SPRAVA RADIOKOMUNIKACI PRAHA**

**USAID Contract # EUR 0014-I-00-1056-00  
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SPRAVA RADIOKOMUNIKACI PRAHA  
Preliminary Privatisation Plan

November 30, 1991

**SR PRAHA**  
**Preliminary Privatization Plan**  
**Contents**

<b>Executive Summary</b>	
<b>1. Introduction</b>	<b>1</b>
<b>2. Business Mission</b>	<b>2</b>
<b>3. Business Objectives</b>	<b>3</b>
3.1 Privatization	
3.2 Financial	
3.3 Operational performance	
3.4 New business development and divestment	
3.5 Service quality and customer satisfaction	
3.6 Social	
<b>4. Business Description</b>	<b>8</b>
4.1 Services provided, revenues, configuration	
4.2 Customer mix, pricing	
4.3 Profit performance	
4.4 Major programs and projects under way or planned	
<b>5. Assumptions Regarding Future Business Environment</b>	<b>18</b>
5.1 Competitive environment	
5.2 Economic regulation	
5.3 Technical regulation	
5.4 Spectrum management	
<b>6. Options and Option Appraisal</b>	<b>22</b>
6.1 Opportunities	
6.2 Threats	
6.3 Option identification	
6.4 Option appraisal: preliminary view	
6.5 Priorities and actions	
<b>7. Outline Implementation Plan for the Privatization Process</b>	<b>35</b>
7.1 Tasks to finish before end of May, 1992	
7.2 Tasks to start after end of May, 1992	
<b>8. Privatization Options and Option Appraisal</b>	<b>39</b>
8.1 Method of privatization	
8.2 Form of privatized entity	
8.3 State share of equity	
8.4 Share of equity to be held by other types of owner	

## Executive Summary

We have adopted the following business mission:

"SR Praha will remain the dominant provider of broadcasting transmission and radio links in the Czech Republic, and will become a competitive provider of domestic and international telecommunications."

We have three main business areas: television, radio and telecommunications. Currently, our main customers are the public sector in radio and television broadcasting, and SPT Praha in telecommunications.

Several possible competitive options for telecommunications are being considered by the Federal and Republic Ministries. The eventual outcome of these deliberations is still uncertain. Formal price controls and cost-based tariffs will almost certainly be introduced in the parts of the market which are not fully competitive.

We have selected a number of business options to exploit market opportunities profitably, and counter potential threats to SR Praha. A first view of priorities has been taken, with some extremely attractive options identified in the telecommunications sector. We believe we can become a genuine secondary carrier to SPT Praha.

We also believe that we have excellent opportunities to service private TV and radio broadcasters profitably.

If we choose our top priority options, the shape and focus of our business will change over the next 5 years. We could see real revenue growth of upto 14 per cent overall, fuelled mainly by the private sector, and in particular the telecommunications business for customers other than SPT Praha.

We have much to do, both in order to achieve our privatization and to implement our priority business options. We believe that continued outside consultancy assistance is essential.

We wish our main activities to be privatized as a whole, with foreign capital participation limited to 30 percent. We believe that this will enable us to raise the investment funds necessary for our development.

We believe that the State should hold between 51 and 61 per cent of our equity, at least in the short term.

## 1. Introduction

This document sets out the Preliminary Privatization Plan for Sprava Radiokomunikaci Praha (SR Praha or SR). A Final Privatization Plan will be submitted to the Federal Ministry of Communications (FMS) by the end of May 1992.

The Plan has been put together by SR Praha's privatization team, with the assistance of consultants from Deloitte & Touche, in conjunction with DRT Czechoslovakia and other member firms of DRT International. Their work was funded by the US Agency for International Development (USAID) under Contract EUR-0014-I-00-1056-00 Delivery Order No.4 to provide assistance on telecommunications privatization. We are grateful to USAID for their support, and to the consultants for their assistance. We are, however, entirely responsible for the facts and opinions in this document.

The assistance from the foreign consultants was available to us for an initial period up to the end of November 1991 only. In the time available to the team, it has not been possible to analyse SR Praha's business and privatisation options in detail. We intend to analyze our options in more detail over the coming months, in accordance with the outline implementation plan set out in section 7. Therefore some of the views and priorities stated in the Final Privatization Plan may change from those submitted in this document.

The Final Privatization Plan is to be submitted to the FMS, our founding Ministry, at the end of May 1992. If they approve the Plan, they will pass it on to the Federal Ministry of Finance. We will also submit the Final Privatization Plan to the Czech Republic Ministry of Economic Policy and Development (MHPR) for their information, and we believe that they will subsequently send it on to the Czech Republic Ministry of Privatization.

## 2. Business Mission

A business mission statement often stands at the start of business plans for companies (or divisions of companies) in market economies.

The statement should clearly set out the broad long-term objective of the entire organization. It should reflect the consensus amongst top management.

The business mission statement can be used to define business objectives and performance targets. It forms a clear and concise benchmark against which to judge future decision-making.

SR Praha's top management has debated draft mission statements and has resolved to adopt the following as the business mission for the next 10 years:

" SR Praha will remain the dominant provider of broadcasting transmission and radio links in the Czech Republic, and will become a competitive provider of domestic and international telecommunications. "

### 3. Business Objectives

SR Praha's business objectives are set out in this section. We recognise that some of these objectives will inevitably conflict with others, and so the major management task for our future will be to balance these objectives optimally.

#### 3.1 Privatization

For SR Praha, the overriding objective of privatization is to achieve a form of ownership which will permit the organization to fulfill its Business Mission, set out in section 2.

Specifically, a private ownership structure should:

- allow generation of the required funds for our investment programmes, possibly with the assistance of foreign parties;
- create the optimal environment for management to manage the business along commercial lines;
- ensure that best-practice management techniques and state-of-the-art technical expertise are spread throughout the organization;
- reduce the influence of the State over business decision-making to tightly defined areas;
- ensure the National Property Fund obtains the greatest possible value (both as the seller of and the continuing holder of shares in SR Praha);
- provide the necessary motivation for employees to improve performance;
- provide an appropriate level of accountability to our customers.

#### 3.2 Financial

SR Praha's long term financial objective as a privatized entity is to maximize returns to its shareholders.

In the shorter term, our objective is to achieve a financial performance similar to that of a comparable company in a more mature market economy. Taking into account differences in economic development, in local competitive environments, and in services offered, SR Praha aims to make returns similar to those of a Western European counterpart within the next 10 years.

This will be achieved by selecting profitable investments, and by charging prices that accurately reflect at least the cost of provision and if possible also the value of our services to customers. We will charge prices in line with value where customers place great importance on non-price factors (such as technical quality, reliability, customization, etc), and where SR Praha's future competitors cannot meet these requirements. This approach may be limited by any system of price control to which SR Praha is subjected.

SR Praha will set different financial targets for each of its main activities. The targets may be different in different years. They will depend on the nature of the competitive environment, the timing of investment programmes, and other factors, such as short term goals for growth or market share. For example, we would not expect to achieve profits on large telecommunications investments for the first few years, and our financial targets would reflect this.

We will revise the existing accounting system to reflect Western practice. This effort will require reprogramming the existing computerized system and possibly replacing it with a more user-friendly system.

### 3.3 Operational performance

SR Praha's operational performance objective is to provide services as efficiently as possible, whilst aiming to raise technical performance to levels achieved in the more advanced economies. We believe our customers will demand such standards in the future.

We will adopt activity-based costing so as to measure costs by type of customer and type of service provided. We will use this information to derive cost-based prices and compare them to the value-based prices.

Cost reduction targets will be achieved in a number of ways:

- Introduction of new equipment will reduce electricity demands and automate currently manual processes, both in operations and maintenance;
- Reduction of overall employee numbers in the organization in line with actual operational needs:
  - Redeployment of some existing staff to more productive roles;
  - Reorganization of the regional structure;
  - Review of our non-production and administrative activities.

SR Praha will also be setting ambitious targets in more technical areas, especially where poor performance means failure to meet our customers' needs. A primary objective is to renew all of the licenses for frequencies with the Federal Ministry as soon as required. Failure to do this would limit the core activities of SR Praha. Other technical targets include:

- Television
  - Modernize broadcasting equipment using solid state devices which allow remote diagnostics. The new equipment should also require less power;
  - Continue to investigate new standards, including the proposed Eastern European version of PAL (with 6.5 MHz channel spacing) and high definition television (HDTV).
- Radio
  - Install dynamic carrier control (DCC) devices to reduce electricity costs by up to 35 per cent;
  - Replace existing travelling wave tube equipment with solid-state devices which allow remote diagnostics;
  - Research digital radio technologies in the 88 to 108 MHz band and determine potential opportunities.
- Telecommunications
  - Research available remote management tools for new microwave equipment;
  - Minimize the error rates on the network.

### 3.4 New business development and divestment

#### New business development

SR Praha is keen to exploit the opportunity of entering new business areas, particularly those where we can build on our accumulated technical expertise.

Our main business development objective is to expand the range of our telecommunications services, as set out in the Business Mission. This is an area where SR Praha is well positioned to meet the future needs of Czech businesses and individual subscribers, and should be able to do so at competitive prices.

The extent of our potential involvement in telecommunications is examined briefly in this document. We will analyze it more fully during the months leading up to the submission of our Final Privatisation Plan.

The major business development objective for radio and television in the near future will be to provide services to the private stations which will be starting up. In addition we plan to expand the range of services we offer to public and private stations.

### Divestment

In first wave of privatization, we submitted privatization projects in respect of three small units responsible for maintenance, installation and transport. We expect these units to be privatized separately when the projects have been approved by the relevant Ministries. This will divest SR of the three units.

SR Praha's divestment objectives now are to reduce our exposure to unprofitable activities, except where this conflicts with our legal obligations. An example of an activity we would like to divest is our agricultural business, which involves farming on the land around our rural operating sites. There should be no legal impediment to this. Another similar example would be our holding in Ekotrans Moravia, which we have been trying to dispose of for some time.

Over the coming months some of our frequency management specialists will cease to be part of SR, and will be employed instead in a newly formed bureau reporting to the Federal Ministry of Communications. An as yet undecided number of staff from our Inspectorate Division will also be joining the bureau.

Finally, we plan to sell off selected housing, buildings and land if they prove to be surplus to our operational needs.

### **3.5 Service quality and customer satisfaction**

SR Praha aims to meet the evolving needs of its customers. We recognise that there may be large differences between the needs of the public and private sectors of our business. We need to define and quantify these different needs as soon as possible.

To maintain and improve service quality to customers along the lines set out in our operational objectives, we aim to be more responsive to customer demands once these have been identified.

### 3.6 Social

It will be a continuing part of SR Praha's overall objectives to balance our social and commercial duties.

To this end, we will continue to protect the health and safety of our staff at the workplace, and provide other services in line with our operational requirements.

We shall continue housing provision for employees, where this is necessary for operational purposes.

Whilst recognizing the need for staff reductions in some areas, we will redeploy or retrain staff wherever possible.

We plan to investigate how employees can be involved in owning SR Praha shares after privatization.

#### 4. Business Description

##### 4.1 Services provided, revenues, configuration

###### 4.1.1 Services provided

Services provided by SR Praha involve the following activities:

- Broadcasting radio and TV programmes within the allotted frequency bands to cover varying proportions of the territory of the Czech Republic;
- Transmitting all kinds of voice, data and video signals through radio relay links within the Czech Republic, including linkage with networks in the Slovak Republic and in neighbouring countries;
- Providing fixed satellite services for international transmission of telephone calls, TV and other signals;
- Providing research, supplies, computer services, and other work to support the core activities.

###### 4.1.2 Revenues

SR Praha generates the bulk of its revenues in three main business areas: television services, radio services and telecommunications services. Sales to these areas in 1990 and for the first half of 1991 were as follows:

	<u>1991 (first half)</u>		<u>1990 (full year)</u>	
	('000 Kcs)		('000 Kcs)	
Television	215,432	52%	339,354	41%
Radio	114,861	27%	245,030	29%
Telecommunications	54,164	13%	126,589	15%
Other business	32,545	8%	124,449	15%
TOTAL REVENUES	417,002		835,222	

The remaining revenues are derived from telegraph operations, license fees from radio operators, and through a number of support activities such as construction/installation, transport, laboratory works, agriculture and the management of estates. Whilst still included in the revenue figures for other business, the Special Maintenance and Installations Division and two Transport Centers (at Satalice and Moravany) are expected to be privatized during the first wave.

#### 4.1.3 Configuration

##### Configuration of equipment

To provide transmission services to our customers, SR Praha used the following equipment:

<u>Business sector</u>	<u>Number of transmitters (1991 est)</u>	
	<u>12/31/90</u>	<u>9/30/91</u>
Television (Main)	61	68
Television (Area)	26	29
Television (Repeaters)	851	860
UPST (OK3) transmitters	24	1
UPST (OK3) receivers	14	17
Radio (MW, SW)	52	59
Radio (USW)	37	45
Radio (Supplementary MW)	0	10
Radio (Supplementary USW)	46	46
Radio (SW)	2	2
Telegraph	2	6
Monitoring reception centers	3	2
Microwave hops	566 *	573 *

\*: Percentage usage of microwave hops across network:

Television	53.4%	52.8%
Radio	1.9%	1.0%
Telecommunications	44.7%	46.2%

Note: USW is used for FM transmissions

##### Coverage rates

With the above equipment, SR Praha was able to achieve the following coverage rates over the Czech Republic during 1991:

<u>Station</u>	<u>Coverage of inhabitants</u>	<u>Coverage of territory</u>
<u>Television</u>		
F1		
CTV	97.6%	94.1%
OK3	95.9%	76.6%
	34.0%	16.0%
<u>Radio</u>		
Praha LW	(day)	
	(night)	99.9%
CS LW/MW	(day)	99.8%
	(night)	98.0%
Praha USW	(day)	99.4%
CS (FM)	(night)	94.8%
	(mono)	95.0%
	(stereo)	96.1%
Vltava (FM)	(mono)	79.0%
	(stereo)	96.6%
		80.1%
		96.6%
		79.3%

## Divisional structure and employment

SR Praha is organized into 11 units: its headquarters in Prague, 2 specialized divisions, and 8 regional directorates.

At June 30th, 1991, we employed 2,467 people as follows:

	T	C	A	O	TOTAL
Head Office	0	0	219	0	219
Special Maintenance & Installations, Prague	0	98	87	21	206
Radiocommunications Inspectorate, Prague	128	0	31	37	196
<u>Regional Directorates</u>					
South Moravia	264	0	92	4	360
North Moravia	171	10	44	15	240
North Bohemia	71	17	16	22	126
East Bohemia	168	0	47	70	285
South Bohemia	74	26	23	31	154
West Bohemia	94	15	29	24	162
Central Bohemia	105	0	25	40	170
Prague	282	0	23	39	349

T: Technical staff  
C: Assembly and construction  
A: Administration  
O: Other (drivers, guards, etc)

We operate four regional research centers for Prague, Central Bohemia, East Bohemia and South Moravia, employing a total of 60 staff from the respective Regional Directorates.

We also have Maintenance Groups that operate within each Regional Directorate, with the exception of Prague (which has its own specialised unit, being privatized in the first wave).

During 1992, we will be losing about 180 of our staff who deal with frequency management to a bureau of the Federal Ministry of Communications. An undecided number of our staff will also be joining the Ministry from the Inspectorate Division.

## 4.2 Customer mix, pricing

### 4.2.1 Television

At present public business dominates revenues from television services, though the share of private customers will gradually increase in the coming years. In 1991, we estimate that public television will make up about 360m Kcs out of a total of 435m Kcs.

<u>Service</u>	<u>Estimated 1991 Revenues</u>
Broadcasting from the aerial	
- Station 1 (F1)	60m Kcs
- Station 2 (CTV)	120m Kcs
- OK3	29m Kcs
Domestic Microwave Transmission to the aerial (all 3 stations)	46m Kcs
Mobile Units (Outside Broadcasts)	15m Kcs
Provision of International TV Circuits (all 3 stations)	91m Kcs

A further 72m Kcs revenue is likely to be generated in 1991 through providing international TV transfer services for foreign stations. In addition to this, some local authorities pay very small extra sums for access to OK3, at Mariánské Lázně, Klatovy, Chomutov and Spindleruv Mlýn (our contract with OK3 requires us to provide coverage in only a limited area).

We charge prices for television services in accordance with the public tariff. This is separated into a fixed and a variable portion. The fixed cost portion is for the lease of equipment. The variable portion is affected by the power input of equipment, the band used for transmission, and the number of hours of operation per year. These prices are unrealistic, and need to be reviewed urgently.

### 4.2.2 Radio

As with television, public business provides the bulk of revenues for radio services. In 1991, over 90 percent of our expected income for radio transmission services will come from public sources.

We also have a growing customer base of private stations, including Radio Free Europe, the BBC and Radio France International. In addition, we serve a sizeable number of much smaller low power radio stations, such as Radio 1, Radio Vox, Radio Informatika, Radio Brno, Hallo World, Country Radio, Radio Contact Liberec, Bonton and Radio Golem. We are currently processing further private radio broadcasting applicants, who are waiting for frequency clearance.

About 70 per cent of radio revenues come from broadcasting in the AM band, which includes short wave, medium wave and long wave services. With the exception of Radio Free Europe, which operates on MW, this is all public sector broadcasting. The remainder comes from FM bands I and II. Band I (66-72 MHz) is a public sector service. We estimate that band II (88-108 MHz) will be 94 per cent public, 6 per cent private sector business for 1992.

Our pricing for the public radio sector is regulated in a similar way to the television business. Fixed and variable portions are related to the type of equipment used, the form of transmitted signal (MW, LW, SW or FM Bands I and II), and the number of hours in operation. The prices we can charge are not realistic, especially the variable portion.

We are able to negotiate our prices individually with our private customers. For example, Radio Free Europe has agreed to an 11 per cent annual price increase over five years.

#### **4.2.3 Telecommunications**

SPT Praha and its operating units are the customers for about 90 per cent of SR Praha's revenues in this sector. Services offered to SPT include use of our microwave routes for their long distance traffic, and the provision of telephony circuits on the Intersputnik satellite.

Over the past year, we have started providing tower space for EuroTel, and we hope to also provide equipment maintenance for them in the near future.

We have constructed a private microwave network for IBM, and intend to extend this system shortly.

On our analog microwave routes we charge a fixed tariff rate, based on transmission distance and the number of telephone channels used. For the digital routes, we calculate a price based on our full costs, including depreciation and overheads.

Satellite services are priced according to costs, on a similar basis to the digital microwave routes.

#### **4.2.4 Other production and non-production activities**

Our customers for telegraph operations are the Czech and Slovak Hydrometeorological Institutes, and Sections 12 and 15 of the Federal Defence Ministry. We also provide limited services for air traffic control around Prague.

Revenue from other services is almost negligible.

### 4.3 Profit performance by activity

In the following table we set out our profit and loss account for the six months to June 30th 1991. We are grateful to DRT Czechoslovakia for preparing the transformation of our accounts to Western accounting standards.

(Figures are stated in '000 Kcs).

	Reported figure	Adjusted figure
Turnover	417,002	411,844
Cost of sales	(284,183)	(230,474)
Gross profit	132,819	181,370
Selling, distribution, administration and other expenses	0	(67,988)
Other operating income	2,921	1,126
Subsidies	22,122	22,122
Operating profit	157,862	136,630
Interest payable	(6,802)	(6,958)
Interest income	0	404
Profit before tax	151,060	130,076
Income tax	(73,252)	(73,252)
Other taxes	(57)	(57)
Extraordinary income	159	0
Contribution to funds	(3,235)	0
Retained profit	74,675	56,767

Preliminary review of the balance sheet as at June 30, 1991, suggests that we have a debt/equity ratio which is extremely low by the standards of Western utility companies. Our profitability and strong balance sheet are likely to attract considerable interest from foreign investors.

The next table shows SR Praha's profits before tax by main business activity. 1991 first half figures are shown as reported in our management accounts and also as adjusted by DRT Czechoslovakia and our accounts department.

	1991 First half <u>Adjusted</u> ( '000 Kcs)	1991 First half <u>Unadjusted</u> ( '000 Kcs)	1990 Full year <u>Unadjusted</u> ( '000 Kcs)
Television	105,898	112,270	167,228
Radio	30,281	33,506	114,194
Telecommunications	14,923	16,918	55,831
Other business	(35,823)	(29,507)	(7,484)
TOTAL PROFIT	115,279	133,187	329,769

The corresponding figures for return on sales before tax for the same periods are as follows:

	1991 First half <u>Adjusted</u>	1991 First half <u>Unadjusted</u>	1990 Full year <u>Unadjusted</u>
Television	49%	52%	49%
Radio	26%	29%	47%
Telecommunications	28%	31%	44%
TOTAL	27%	32%	39%

The large fall in profits observed for radio services can be explained primarily by a substantial increase in electricity and component costs during the first half of 1991, the high electricity needs of the radio business, and SR Praha's inability to raise its prices to the public sector in line with such costs.

#### **4.4 Major programs and projects under way or planned**

##### **4.4.1 Television**

During the next few months we expect we will complete a 5-year program to construct the new television transmission tower Prague-City in Zizkov. This will allow the transmission of high quality signals in the Prague area, and give enough reserve capacity for fourth and fifth stations, should they be needed. This tower houses the main receiver station for the cable TV network, and adds capacity for five or six radio stations.

Large scale investment on the third station network (currently OK3, until the end of December 1991) has temporarily ceased until a private customer has been found to run the station after January 1, 1992.

We have taken our first steps into cable TV with the investment of a stake in a joint-stock company which is building a network in Pardubice. In Kadan (West Bohemia), we are acting merely as contractors in building another cable network, which is financed by local authorities.

A new transmitter has been set up in Chomotov to improve coverage for the second station in North Bohemia, and to add reserve capacity.

We are currently investigating the possibility of providing teletext services for the Czechoslovak stock exchange.

We are excited at the prospect of becoming members of Eurovision, following the end of Intervision in December 1992.

##### **4.4.2 Radio**

We are planning to introduce new medium wave networks for one of our private radio customers.

We will be using spare capacity at our short wave transmission center at Litomysl, in which private broadcasters show great interest.

We are also keen to introduce DCC technology on selected medium wave equipment, to reduce electricity costs, and are currently weighing up the choice of manufacturer.

..... Telecommunications

We have entered into a joint venture agreement with SR Bratislava and Telediffusion de France to provide radio paging services across Czechoslovakia using RDS (Radio Data Service) technology. The service is currently in the installation stage and will be ready for paying customers in 1992.

An earth station for the Intelsat satellite system is being constructed at Sedlec with Comsat equipment and expertise. This should provide improved television satellite capability, and increase the number and quality of international telecommunications lines that we can supply to SPT Praha.

Initial discussions have taken place with the Deutsche Telekom over the provision of VSAT services, with the earth station likely to be based in Germany.

We are currently in the middle of a major program to build long distance digital microwave routes across Czechoslovakia. The Prague-Frankfurt route is already in place. By mid-1992 we hope to have completed a link from Prague to Bratislava via Brno. In 1993 we intend to branch a route from Brno to Ostrava, which will eventually be taken into Poland. By the end of 1995, we would hope to have also built a route from Prague to Berlin.

We have agreed with IBM to extend the private microwave network we built for the firm. The cost will be 12m Kcs.

#### 4.4.4 Other

##### Other activities

At present, there are no major investment plans for other parts of our business.

We are currently considering the phasing out of agricultural activities, and the disposal of selected land and properties.

## Shareholdings

SR Praha has shareholdings in the following joint-stock companies:

Ekotrans Moravia, a.s	5m Kcs	3.2% of equity
Postovni banka, a.s	1m Kcs	0.5% of equity
Intes Pardubice, a.s	0.2m Kcs	5.0% of equity

Ekotrans Moravia is a company set up to build a canal between the Danube and the Oder (although the project has now been cancelled on ecological grounds). We plan to sell this stake as soon as possible. Postovni banka is a banking institution specialised in working with communications firms (and from whom we have borrowed money); we will be increasing our investment by 1m Kcs next year. Intes Pardubice is the cable TV company mentioned in section 4.4.1 above.

## Organization

We have been undertaking a major efficiency drive within SR Praha, and have reduced staff numbers by 12 per cent over the past year. Appraisal of a possible new organizational structure has been postponed until 1992.

## 5. Assumptions Regarding Future Business Environment

These assumptions about our future business environment have been developed from our current knowledge of plans for change. Each assumption could have a significant impact on our business operations and plans. However, the situation is uncertain.

### 5.1 Competitive Environment

Our future business environment is likely to be more competitive than at present. The precise form of competition which will be introduced is, however, unclear. There are several possibilities:

- break-up of SPT into companies operating in distinct or overlapping service areas. This could be organised by service type (e.g. local or long distance telephony) or geographic region (e.g. each local operator having a monopoly in certain services in its own area but able to compete in certain other services on a Republic-wide basis);
- liberalisation of certain services, to allow competition between SR and SPT and also entrants;
- complete liberalisation of all services, with SR, SPT and entrants allowed to compete without restriction.

The option adopted depends on several things, including:

- the extent to which demand for telecommunications in the Czech Republic will support competition;
- political considerations;
- the nature of the exclusive rights, of both service provision and frequency usage, given to the EuroTel consortium in the areas of mobile communications and packet switched services;

- possible restrictions on entrants - for example, limited prospects for majority shareholdings in newly privatized companies or new consortia, or restrictive license conditions.

## 5.2 Economic Regulation

### Price Control

We believe that a formal price control mechanism will probably be introduced for those telecommunications and broadcasting services which are not subject to full competition. The aim of the price control would be to limit the maximum prices of services. Services provided in full competition will not be subject to price controls.

Price control will probably be based on a tariff basket mechanism whereby individual prices are combined into a weighted average. The price cap would be applied to the average basket price.

We expect a price control regime which ensures that tariffs grow more slowly than inflation. The form of the control will probably be the "CPI-X" formula used in many countries. CPI means Consumer Price Index and would be taken as the Index Spotřebitelstých cen v CSFR in the CSFR. X is the figure that would be set by the economic regulator to reflect expected increases in our productivity.

### Cost-based Tariffs

We expect to be required to base our tariffs on the costs of each particular service plus a reasonable profit. This raises a major problem for us. Where services share network infrastructure, the costs must be apportioned in a reasonable manner according to cost causation principles.

This is not an easy task. We do not have a well developed system for allocating costs to specific services. Nonetheless, it is in our interests to move to cost-based tariffs, so as to head off threats of competition. We must not allow SR Praha to be a target for competitive attack as a result of charging prices which are significantly greater than a competitor would need to charge.

It will be necessary for us to develop management information systems that track costs accurately according to customer, within both the public and private sectors, and services. This will be especially important where the pricing principle differs by sector.

### 5.3 Technical Regulation

Privatization and the introduction of competition will likely lead to an increase in the extent of technical regulation under which we will be expected to operate.

We believe that the overall result of the changes will be to place certain types of obligation on us. We believe that the most significant potential developments for SR are likely to be:

- the introduction of operating licenses for us which include as conditions targets relating to our network performance and service level parameters. Based on overseas experience, these could include:
  - network performance parameters, such as error rates on digital lines, signal-to-noise ratios and mean times between failures;
  - service level parameters, such as geographic coverage, availability, grade of service;
- the adoption of European Community or European Telecommunications Standards Institute (ETSI) standards for all future network development;
- regulation of interconnection arrangements between our facilities and SPT's facilities, and between our facilities and SR Bratislava's. Interconnect regulations typically cover parameters such as availability of the interconnecting facilities, number of interconnect points, their capacity and technical interfaces used. Similar arrangements may be required for interconnect between our facilities and those of new operators, although we expect that the interconnect obligation may well be limited to SPT.

#### 5.4 Spectrum Management

Under the proposed telecommunications legislation, the majority of radio spectrum management functions presently carried out by SR Praha and SR Bratislava will be transferred to a new department of the Federal Administrative Bureau of Telecommunications (FABT), which will report to the Federal Ministry of Posts and Telecommunications.

This, and liberalisation of the sector in general, will have several implications for SR:

- our frequency usage rights, especially for new services, will be dependent on an external body. While this has nominally always been the case in the sense that the Federal Ministry has been responsible for overall spectrum management, it delegated many spectrum management functions to us;
- since frequency allocation planning will be remote from us, our internal planning will be made more difficult. This will be particularly true for new services where precise frequency allocations will not be known as far in advance;
- the introduction of entrants in the sector will mean more competition for the use of frequencies in certain bands;
- the operational coordination of frequency use with other operators will grow more complex and will place greater administrative burdens on our organisation.

We propose to retain a small number of frequency management experts, with the following functions:

- negotiate our spectrum rights with the FABT;
- administer usage of our spectrum rights;
- sell our advice on spectrum issues to other operators (this is a profitable business in other countries).

## 6. Options and Option Appraisal

With privatization and simultaneous liberalization of the sector, we have opportunities in each of our main activities and also threats in each area. In the light of these we have set out the options for SR Praha, to exploit the opportunities and counter the threats.

### 6.1 Opportunities

#### 6.1.1 Television

We believe that we have substantial opportunities for expansion in the television sector. In the long term, as standards of living in the Czech Republic rise towards Western levels, the penetration of television services (the percentage of households with TV sets) will approach the levels seen in more mature economies. Consumers will also have more disposable income to spend on products. Hence the potential for TV advertising should improve over time, and our customer base of private broadcasters will increase accordingly.

These assertions are illustrated through the chart on the next page. It shows that there seems to be a very strong relationship between the growth of private consumption per head and expenditure on television advertising per head. However, the level of TV advertising per head for a given standard of living varies considerably in different European countries. This is due to differences between countries in factors such as the number of television stations, the availability and cost of other advertising media, and the regulatory environment. Nevertheless, advertising expenditure in the Czech Republic can be expected to rise strongly in line with private consumption.

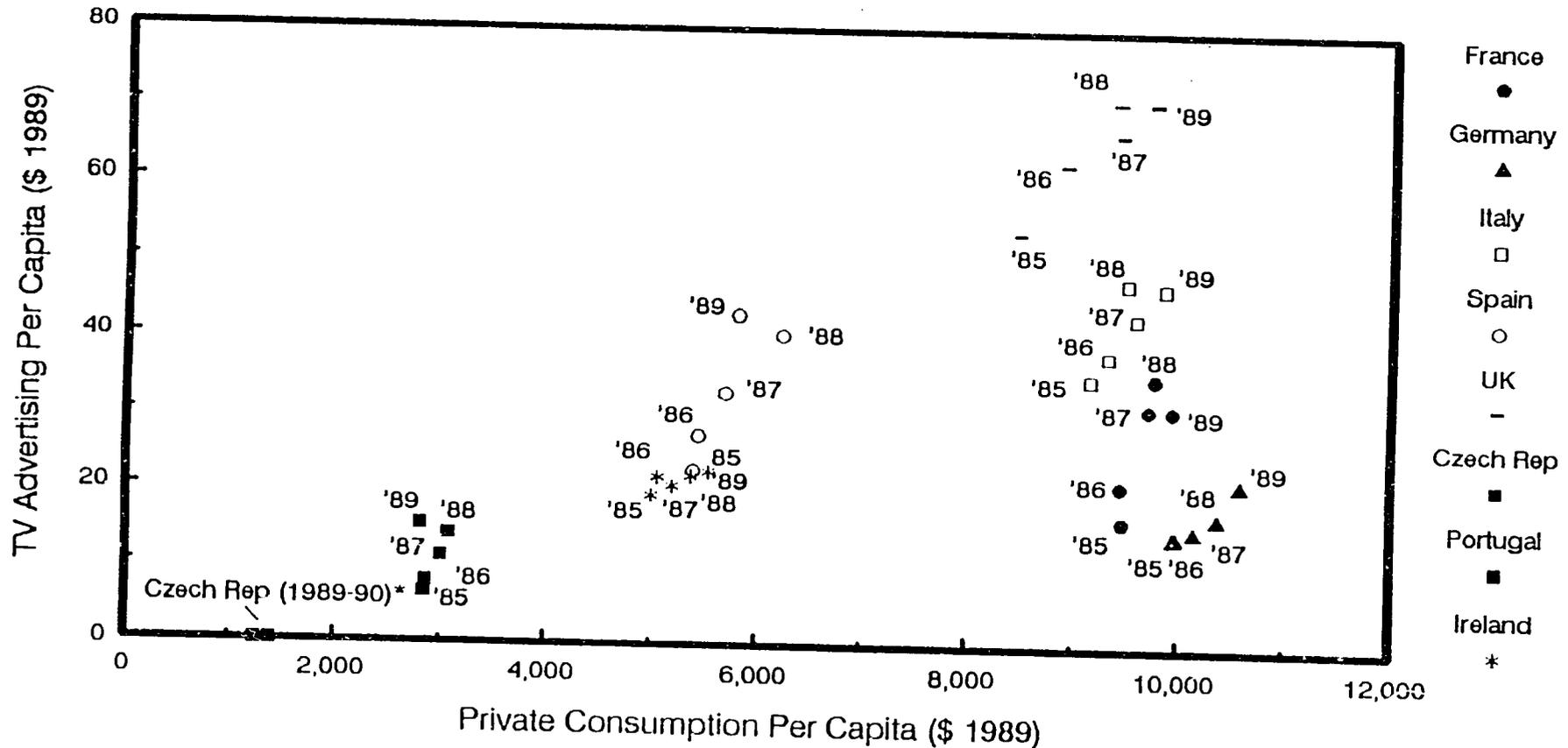
The growth of our private sector television business will begin with the transfer of the OK3 station from public to private hands in 1992. We await the Federal Ministry's decision as to whether this network will be retained intact for one broadcaster, or split up for regional transmission. We hope to realize better prices on this transferred business in the future, should the new operators choose to use our services. We believe that there is a profitable opportunity to invest capital in this third network to extend its coverage to the levels of F1 and CTV.

The possibility of building a fourth terrestrial network reaching about half the Republic's population is an opportunity for SR Praha in the period from 1993. The network would consist of several low power transmitters in and around major cities. In the longer term, we will also be investigating a fifth local network, transmitting to Prague and its periphery.

# TV ADVERTISING EXPENDITURE

## Relationship To Private Consumption

### 1985-1989



Source: IMF, Euromonitor, Carat Int'l,  
CISLA pro kazdeho

\* D&T estimate

For public business, we see a key opportunity for rebalancing the tariff towards the price structure prevailing in more developed economies, in line with long term Federal goals. Not only did the previous tariffs set prices too low, but the inflation of the first half of 1991 was not accompanied by any price increases. It is time to restructure the tariff on more commercial principles.

As with all of our business, SR Praha aims to reduce its costs through the introduction of more modern energy-saving transmission equipment. There is considerable opportunity to reduce maintenance and technical staff costs, as well as improving the quality of signal.

Finally it may be possible to change the television band spacing to 5.5 MHz, in line with Western European accepted practice, and CCIR standards. The change should also reduce transmission equipment and TV set prices. The background is as follows.

Television sets in the Czech Republic use a 6.5 MHz channel spacing decoder. If the channel spacing is changed to 5.5 MHz, a household will not be able to receive the transmission acceptably unless it acquires a new set or installs a new decoder in its existing set. This may reduce the households reached by the broadcasts and hence the penetration of advertising carried by the station.

The Federal Ministry wants to change the channel spacing to comply with the PAL transmission standard used in most of Western Europe. Currently, broadcasts in the Czech Republic use SECAM as the transmission standard. Changing our transmitters to standard PAL spacing will be very expensive (approximately 200 million Kcs). It is possible that before the conversion is concluded, a new standard, such as high definition television, will be globally adopted.

The issue will therefore arise as to whether we should convert our transmitters for bands I and III to PAL with 5.5 MHz spacing, or wait until new standards are adopted. (Our transmitters for bands II, IV and V have already been equipped with PAL at 5.5 MHz spacing). We would not convert the transmitters unless we received a special payment from public funds to do so.

Because of the cost involved, discussions are currently taking place about accepting 6.5 MHz spacing as an alternate Eastern European television broadcasting standard. If our existing standard is approved, the cost of changing the transmission equipment from SECAM to PAL would be small.

### 6.1.2 Radio

We believe that we have opportunities in the radio sector both to consolidate our current business, through cost reductions and quality improvements, and also to extend the range and scope of services to customers. The opportunities will be generated by a similar process as for television - higher standards of living leading to greater potential for advertising and hence to more demand by private broadcasters for our transmission services. The main differences from the television market are:

- the number of households with radios is unlikely to increase significantly (though there may be a switch towards FM-receiving equipment);
- on the other hand, the scope for new stations is greater, because the limitations of available spectrum are not so severe.

By replacing outdated transmission equipment, there is great potential for lowering costs, especially in LW and MW. Use of DCC equipment would decrease electricity costs by at least 20 per cent and possibly up to 35 per cent, and newer transmitters would ensure greater automation and reliability, thus saving on staffing and maintenance costs.

SR Praha is keen to exploit the opportunity of expanding its services on FM band II (88 MHz to 108 MHz), as part of the eventual migration from FM band I (66 MHz to 72 MHz). The Geneva Agreement discourages use of FM transmission in band I.

Moreover, end-users are increasingly sophisticated and will be demanding quality stereo reception in the future. With the possibility of six national coverage FM networks in the future, it seems likely that private broadcasters will require both the extension of existing networks and also the construction of new ones. One remaining question is whether the six networks will be spread over bands I and II, or simply band II.

As discussed in the previous section, there will be an opportunity for us to renegotiate the terms of the tariff for radio services. SR Praha aims to move towards realistic prices for its services as quickly as possible. This will be particularly important the variable cost portion of our MW and LW business in the public sector.

Another key opportunity is the release of various frequencies to private broadcasters under the terms of the new Broadcasting Law. We believe that private customers will be an important and growing part of our radio business in the future.

We are looking at the possibility of expanding the range of engineering services we offer to customers, and there is an opportunity which mostly concerns the radio sector. This would be to provide a radio coverage advisory service to prospective broadcasters. This service could also be extended to television and certain telecommunications applications.

Finally, SR Praha is considering the introduction of static/dynamic data transfer technology on our radio networks - i.e. simultaneous transmission of data with the radio broadcast. This can be used for applications such as radio subtitles.

### 6.1.3 Telecommunications

The background to any discussion of telecommunications opportunities is the probably substantial latent demand for telecommunications services within the Czech Republic. Coupled with the increase in demand for telecommunications in all (even mature) economies over the past decade, it is clear that telecommunications will be an important and very fast growing sector, where more than one supplier would probably be profitable if competition were allowed.

SR Praha can broadly split the opportunities in the telecommunications sector into those which will affect its dealings with SPT Praha and those which affect other existing (or potential) business.

#### SPT Praha business

The opportunity of installing a digital microwave network alongside the analog routes is a large source of potential revenue from SPT Praha, or perhaps other future telecommunications providers in the Czech Republic. Given the length of time it would take SPT Praha to install fiber optic or other cables to support digital traffic, they are likely to use SR Praha services in this field for the next three to five years.

There is great scope for an improvement in the quality and capacity of international telecommunications services to people in the Czech Republic should SPT Praha choose to take our circuits on the Intelsat satellite system. This will mean greater revenues per channel for us than with Intersputnik, and will provide SPT Praha's customers with lines that are of a quality that will permit data transfer, as well as voice telephony.

Another opportunity would be to offer SPT Praha (or EuroTel) radio access technology for use in the local loop. This would be a very short lead-time solution to the telecommunications problems faced by businesses and individual customers in the Czech Republic, especially in large cities.

#### Other business

We aim to increase the scope of our involvement in this sector, and with a modest extension of our existing activities, our service offering could include the following:

- Expanding the number of private networks we provide to users such as IBM;
- Providing trunked radio network services in urban areas, such as Prague;
- Providing radio paging services on a country-wide basis;
- Offering international transit services to foreign telecommunications customers through the Intelsat satellite;
- Expanding engineering services or facilities/network management. This could be a profitable way of gradually reducing staff numbers in the core organization, whilst ensuring their future employment.

However, given the expertise that already exists within our organization, and with the aim of completing our Business Mission, SR Praha is keen to become a far more significant player in the expanding Czech telecommunications market.

We believe SR Praha is very well positioned to provide local loop, long distance and international services via radio access, microwave and satellite technologies. With the addition of switching capability, we would become a full secondary carrier to SPT Praha, competing directly against them by providing a better service. We could achieve this by taking advantage of new technologies, such as the Cordless Telephone 2 (CT2) or Digital European Cordless Telephone (DECT) standards, to provide a local loop quickly, without the need to install cable.

However, we will need to clarify the scope of our possible involvement in telecommunications over the coming months with the authorities. In particular the implications of the EuroTel license agreement with the FMS will be a key input into our decision-making.

#### **6.1.4 Other production and non-production services**

We are considering the possibility of leasing tower space to other operators across a range of possible applications. We also hope to be able to lease out our accompanying facilities at these sites. However, rather than the lease charges, it could be the maintenance of our customers' equipment that is the major source of revenue from this type of business in the future. This is because we will be able to supply maintenance services using our existing staff on site much more cheaply than the other operators, so we should be able to make a significant profit.

We will also be able to use the context of the privatization project to rationalize our non-core activities, including agriculture and housing.

#### **6.2 Threats**

Whilst this section outlines potential threats to SR Praha business, we sincerely believe we have the capacity to counter them effectively.

##### **6.2.1 Television**

Along with the radio business, we accept that there are limits on the level of funds to public broadcasters, but see it as unlikely that the volume of business will fall below current levels. The public sector is obliged by the new Broadcasting Law to broadcast two stations (one Federal and one Republic), and we do not expect severe reductions in coverage or time of broadcast per day. Clearly the conditions of the public tariff will be a key concern.

Potential threats in the television sector therefore relate primarily to the private sector. In the short term, we must ensure that the former OK3 broadcast business is placed with SR Praha. The unreliability of the current network could be a concern for a potential investor.

Whilst many television broadcasters may be international, or at least backed by foreign capital, SR Praha recognises the potential for bankruptcy of private stations, especially in the formative years of private television in the Czech Republic.

There is also a potential threat of customers choosing to build their own transmission networks, or employing the services of a competitor to SR Praha. This situation is unlikely in the very near future, but is a distinct possibility in the longer term, should SR Praha fail to perform. This will certainly be a threat if, as seems likely, competitors to SR Praha are allowed to use our existing network of transmission towers to set up their equipment.

Finally, whilst penetration of cable and satellite television has been rapid in some mature economies, we think it unlikely to affect our business greatly in the near future.

### 6.2.2 Radio

SR Praha will have to serve both public and a number of private customers. The public sector has an obligation under the new Broadcasting Law to provide national radio broadcasting to its citizens, but we must recognise that there are competing demands on public funds. In the long term, therefore, this sector is unlikely to grow.

We are also concerned about the public sector's apparent commitment to FM band I in the future. Whilst it is clear that the replacement of listeners' equipment to receive FM band II will take time (through consumer purchases), we would not regard large future investment of our funds into maintaining the old band I networks as a rational one in commercial terms. It is becoming increasingly difficult to buy transmitters and spare parts for band I applications without ordering customized, and hence expensive, equipment.

In the private sector, as with television customers, SR Praha recognises the threat of bankruptcy to radio broadcasters, and the implications this may have for our cashflow.

The potential rush of private broadcasters to the market in the Czech Republic will also present SR Praha with a challenge to its current position. The sheer number of applications for broadcasting licenses indicates that the handling of this business will place new demands on management time and expertise. If we fail to deliver a quality service to these customers, the threat from competition would be substantial. Under the new Broadcasting Law, private broadcasters can set up their own signal transmission equipment, or choose to use the services of a competitor to SR Praha.

### 6.2.3 Telecommunications

As with the opportunities for telecommunications services, the threats to SR Praha divide into those relating to SPT Praha business, and other business.

An agreement with SPT Praha to take SR Praha circuits on the Intelsat satellite has not yet been signed. Given the low number of international lines that SPT Praha can currently offer its customers, and its decision to terminate its telephone business on the Intersputnik satellite from January 1992, we believe that a refusal to enter into an agreement with us shortly would not make sense. Failure to do so might adversely affect the level of international telecommunications services in the Czech Republic and would leave us no option but to sell the circuits to other customers or offer international services ourselves.

We are concerned about our long term revenues from SPT Praha on our digital microwave routes. At present, and for the next few years, SPT seems likely to use these routes. However SPT has decided in principle to lay its own fiber cable routes to carry its traffic, putting large scale SR revenues at risk.

Moreover, with an uncertain competitive environment for the provision of telecommunications services, we cannot exclude the possibility that SPT Praha will be allowed to compete against us directly in our core business of microwave transmission. We will need to determine quickly whether SPT Praha will be allowed to compete, and whether they would do so, given the opportunity.

More generally, if SR Praha is to become a genuine competitor to SPT Praha, this might lead SPT to refuse to do business with SR, except where absolutely unavoidable.

With regard to SR Praha's goal to become a competitive telecommunications provider in the Czech Republic, our major threats relate to the nature of competition that will develop. Clearly the legislative and regulatory situation that will become clearer in the coming months will directly affect this. Threats relate to the number of competitors in each segment, and the degree of regulation that will be imposed.

Finally, the sheer scale of the investment programmes required to develop our telecommunications business may be a threat of sorts. This does not merely relate to the financial risk of such large investments, and the potential for starving other parts of the business of fresh capital. We will clearly need the assistance of foreign capital and expertise to undertake some of the proposed projects, which implies careful selection of partners and structuring of possible deals.

32

#### **6.2.4 Other production and non-production services**

The major threat to our other business relates to telegraph operations. This form of communications is not very sophisticated, and is being replaced by other technologies, such as facsimile and satellite. We have witnessed a steady decline in customer numbers, and expect that our meteorological and military customers may discontinue their business in the near future as they become more ready to accept alternative technologies.

#### **6.3 Option identification**

As a result of assessing general market opportunities and threats, and in the light of SR Praha's current business configuration, a number of possible business options has been identified for our main activities. These are designed to exploit the opportunities and counter the threats.

##### **6.3.1 Television**

- (1) Installing cable for outlying areas within the Czech Republic. This would increase the coverage of television broadcasts to citizens, and the cables could also be used for telecommunications business.
- (2) Changing the band spacing on TV bands I and III for station F1 from 6.5 MHz to 5.5 MHz. This would be part of a long term technical objective to comply with television transmission equipment norms in Europe, including the use of the PAL standard.
- (3) Investing capital to replace transmission equipment used to support networks for stations F1 and CTV. This should directly reduce electricity costs and improve technical performance. Moreover, through automation and better reliability, it will also reduce technical and maintenance staff costs.
- (4) Further increasing coverage on the networks supporting stations F1 and CTV.
- (5) Extending the coverage of the third national television network to similar levels to F1 and CTV. While extending the coverage, increase the reliability and reduce the costs.
- (6) Building a fourth terrestrial television network to the maximum coverage of inhabitants within the Czech Republic.
- (7) Building a fifth local terrestrial television network, possibly based around the Prague area.

- (8) Marketing our services actively to both local and national private broadcasters who are likely to be potential customers in the future.
- (9) Offering the installation and operation of new microwave links directly from the studio to transmitters, for low power private television broadcasters.
- (10) Offering digital data services to private customers, such as the stock market.

### **6.3.2 Radio**

- (1) Investing capital to replace transmission towers and introduce DCC technology in the MW and LW bands. Use of DCC should reduce energy costs by up to 35 per cent per year. More modern transmission equipment will automate operations and be more reliable, so there should be potential for both technical and maintenance staff reductions, as well as service quality improvements. Equipment with remote monitoring capabilities may allow SR to centralize some of its maintenance personnel and reduce costs further.
- (2) Investing capital to increase coverage levels on FM band II, as part of the long term goal of migration from FM band I. The programme will extend coverage (population and territory) and reduce costs on existing national networks and ensure the construction of enough capacity to support 6 national networks in total.
- (3) Marketing SR Praha services actively to potential private radio customers. The short term rationale is to find private customers for currently idle capacity. In the longer term it is to dissuade future applicants for licenses from using their own transmission equipment, or that of a potential competitor.
- (4) Introducing static/dynamic data transfer technology on the existing radio network.

### **6.3.3 Telecommunications**

- (1) Extending the digital microwave network for long distance links across the Czech Republic, linking up with similar routes in neighbouring territories. Major future investments would include a Prague-Brno-Bratislava link, a branch from Brno to Ostrava and Poland, and a link from Prague to Berlin.

Business Options  
Telecommunications  
First View

	Business Option	Sector	Need to act quickly	Size of annual investment	Length of investment	Need for partner(s)	Likely Risk	Higher Revenue	Lower Cost	Profit Impact		
1	Extend microwave digital routes - long distance links including international	SPT	Yes	100m	4 Years	No	Med	++	-	+		
2	Invest in Intelsat earth station - Secure major customer	SPT	Yes	Med	1 Year	No	High	++	-	+		
3	Offer radio access local loop technology to SPT	SPT	No	High	10 Years	Yes	Med/high	++	-	+		
4	Provide radio access local loop technology to new competitor to SPT (not SR)	Other	Yes	High	10 Years	Yes	High	++	-	+		
5	Become full secondary telecoms carrier - Add switching capability	Other	Yes	Very high	10 Years	Yes	High	+++	---	++		
6	Develop radio paging services - in line with business plan	Other	Yes	Med	3-5 Years	Yes	Med	++	-	+		
7	Offer trunked radio network services - based in Prague	Other	No	1m	2 Years	No	Med	+	-	+		
8	Expand private microwave business networks	Other	Yes	12m	2 Years	No	Med	++	-	+		
9	Offer VSAT services	Other	No	7m	1 Year	No	Low	+	?-	?+		
10	Engineering services or facilities management	Other	No	Low	1 Year	No	Low	+	?-	?		

Values in Kcs

Business Options  
Telecommunications  
First View

	Business Option	Impact on other parts of business	Comments
1	Extend microwave digital routes - long distance links including international	Possible use by other services	SPT won't be major customer for very long
2	Invest in Intelsat earth station - Secure major customer	Possible use for TV transmission	-----
3	Offer radio access local loop technology to SPT	Limits our opportunity to compete in local loop	-----
4	Provide radio access local loop technology to new competitor to SPT (not SR)	Limits our opportunity to compete in local loop	-----
5	Become full secondary telecoms carrier - Add switching capability	-----	Our biggest opportunity But will affect SPT relationship
6	Develop radio paging services - in line with business plan	-----	-----
7	Offer trunked radio network services - based in Prague	-----	Current demand may not support costs
8	Expand private microwave business networks	Rosalo may take away some business from option 5	
9	Offer VSAT services	May take some business from option 5	Could be a profitable market niche given SR experience VSAT customers usually need other telecom services
10	Engineering services or facilities management	Redeploy staff	

## 6.5 Priorities and actions

Our first view of the priorities for action is shown in the upper chart on the following page. Our views may change before we submit our Final Privatization Plan to the Ministry at the end of May 1992, in the light of the more detailed financial and operational analysis.

A preliminary forecast of SR Praha's main activities is set out in the lower chart on the next page. Like all the financial projections in this preliminary plan, the revenue figures are in real terms, thus ignoring inflation. We have, however, taken account of prices which we expect to change relative to the general price level in the Czech Republic as a whole.

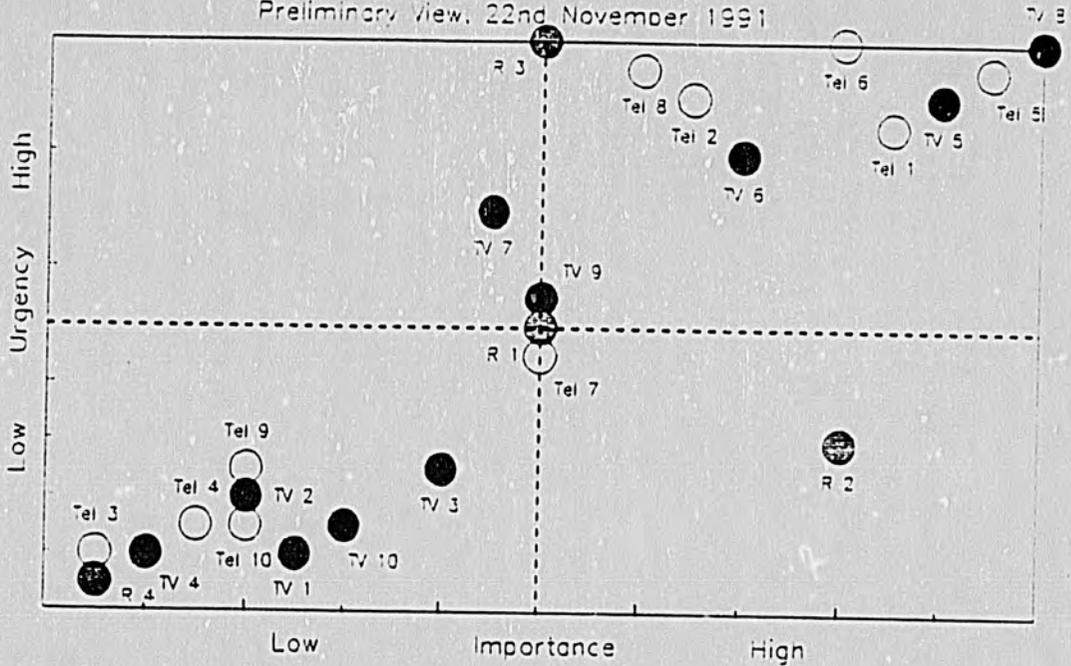
The chart assumes that we implement all the high priority options and that all future TV and radio services operate at full capacity.

The chart shows that by 1996 our business could look radically different from today's. The non-SPT related telecommunications business would be our largest revenue earner, and would grow the fastest over the five years shown. Private television and radio would grow rapidly, whereas the public sectors would show constant real growth, at best. Our other business activities would decline over the five-year period.

Overall, we expect real annual revenue growth of about 15 per cent per year.

# SR PRAHA

Business option prioritisation  
Preliminary View, 22nd November 1991



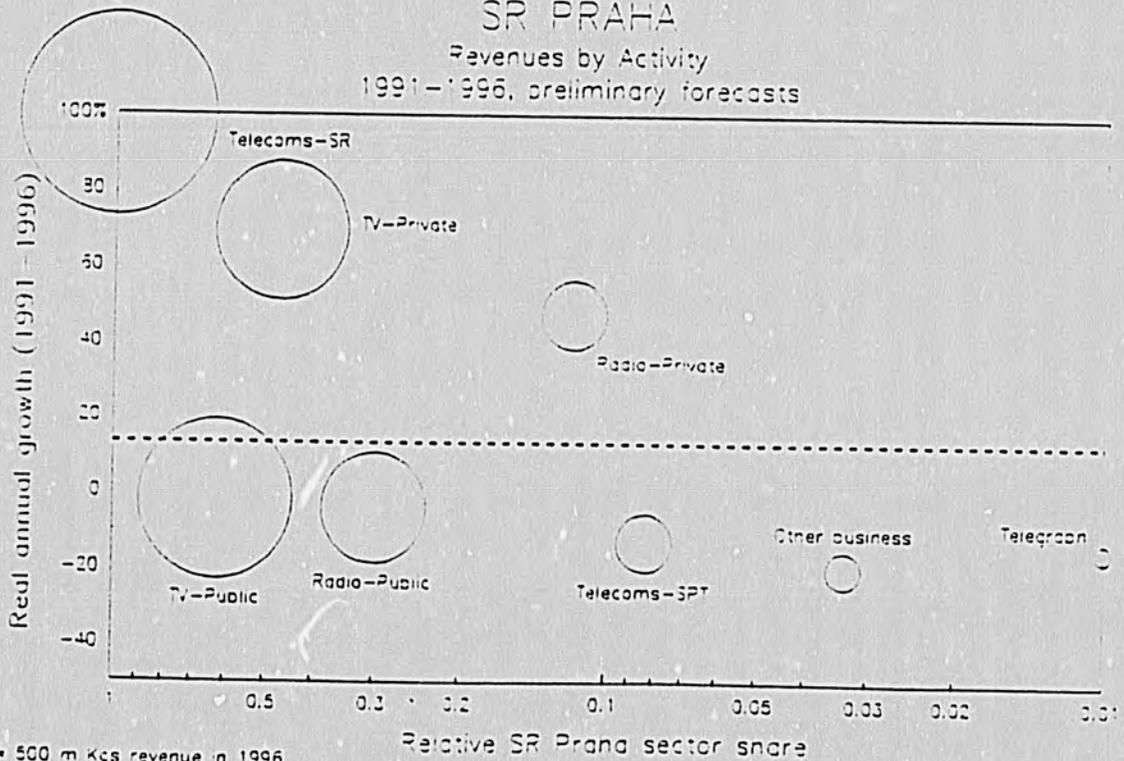
Note: Views taken before detailed financial analysis of each option and its impacts was conducted.

Source: SR Prana estimates

Ref: SRP-Prna

# SR PRAHA

Revenues by Activity  
1991-1996, preliminary forecasts



○ = 500 m Kcs revenue in 1996  
Note: Assumes above average urgency and importance business options implemented

Average Growth: 13.44%  
Source: SR Prana, O&T analysis and estimates  
Ref: SRP-Prna

## 7. Outline Implementation Plan for the Privatization Process

The most important actions we will take to define and realize our overall business strategy fall into three main areas:

- Determining the range and scope of our future activities and defining the strategy within each business area;
- Designing the organizational structure and operating systems to support these activities;
- Implementing the privatization process

The Final Privatization Plan must be submitted to the FMS by the end of May 1992. We have therefore chosen to divide SR Praha's key implementation tasks into those that must be finished before submission and those that we can undertake afterwards. A non-exhaustive list of tasks is set out below.

We are currently investigating the possibility of securing further USAID funding for consultancy assistance with the Final Privatization Plan from Deloitte & Touche, who have been working with us during the past month.

### 7.1 Tasks to finish before end of May, 1992

#### Main Business Activities

Clarification of legislative and regulatory situation, and likely nature of competition in each business sector. Attempt to persuade FMS to our views.

Detailed investigation of options identified in section 6.3:

- Forecast market demand for each business area;
- Define likely revenues, costs and profits under different competitive scenarios;
- Define capital requirements for each option;
- Determine need for foreign and possibly Czech management and technical assistance;
- Quantify impact of each option on other parts of the business;
- Prioritization of options;
- Determine capital structure for SR Praha;
- Identify possible business partners;

- Active marketing to potential customers:
  - Priority is to find customer for OK3 network;
  - Private television broadcasters;
  - Private radio broadcasters;
  - SPT Praha for digital microwave and Intelsat
- Renegotiate public sector tariff for television and radio.

#### Other Business activities

Resolve issue of the long term future of the telegraph business.

Phasing out agricultural activities.

Analysis of SR Praha's portfolio of land and property with a view to assessing its value to the business operations.

#### Organization

First review of possible organizational changes within SR Praha:

- Structure;
  - Regional;
  - Divisional/functional;
- Operating systems
  - Control systems;
  - Personnel management systems, including incentive and reward systems for all staff.

#### Privatization Process

Determine optimal equity allocation in the light of our chosen business strategy.

Transformation of our accounts to Western accounting standards.

Preparation of information memorandum to offer to selected potential foreign partners.

Periodic consultation with FMS over progress with foreign partner selection.

Completion of transfer of assets of departments privatized in first wave:

- Maintenance and installation division;
- 2 transport divisions.

Completion of transfer of SR Praha staff to the Federal Ministry:

- Frequency management department;
- Part or all of Inspectorate department .

Independent valuation of SR Praha's business.

Drafting and submission of the Final Privatization Plan .

Coordination of all these activities with SR Bratislava as appropriate.

## 7.2 Tasks to start after end of May, 1992

### Business Activities

Acknowledgment/approval from FMS of chosen form of partnership.

Foreign partner selection.

Preparation of 5-year business plan.

Definition of detailed operating performance targets for each business area.

Preparation of detailed budget for 1993.

Refinement and finalization of chosen strategy, where needed, and continued analysis of new business options.

Renewal of SR Praha's frequency allocations with the FMS.

### Organization

Detailed analysis of current organizational structure, operating systems and culture.

Evaluation of organizational needs.

Redesign of organization and evaluation of the organizational change involved:

- Establishment of new departments (eg. telecommunications department; sales and marketing departments);

- Redesign of operating systems:
  - Invest in computer-based accounting package to produce accounts to Western accounting standards;
  - Development of management information and budget systems to measure costs by customer and service and conform to regulatory requirements;

Implementation of organizational change.

#### Privatization Process

Conversion of SR Praha into a shareholder company, with all shares owned initially by the State.

Implementation of other legal and administrative steps towards privatization.

Disposal of selected land and properties.

## 8. Privatization Options and Option Appraisal

We contributed to the "Study on the Strategy Concerning the Denationalization and Privatization of Telecommunications in the Czech Republic", the strategy document written by the Czech Republic Ministry of Economic Policy and Development.

In that document, the plan for privatizing SR Praha is given as privatizing the organization as a whole, with the exception of:

- the three separate units which are to be privatized in the first wave of privatization (the Special Maintenance and Installation Division, the Transport Center Satalice and the Transport Center Moravany); privatization projects were submitted in respect of these units by the deadline of October 31, 1991;
- the paging operation, which is a joint venture with SR Bratislava and Telediffusion de France;
- our current and planned stakes in cable TV networks - the only current stake is in Intes Pardubice, which is constructing a cable network in Pardubice and other towns in Eastern Bohemia;
- our housing assets, which would be privatized separately by a trade sale. (We want to privatize our housing assets in such a way as to be able to retain the proceeds).

The proposed capital structure for the privatized SR was given as:

- 3 per cent restitution fund;
- 3 per cent social security fund;
- 3 per cent old age pension fund;
- 30-40 per cent foreign partners;
- 51-61 per cent Czechoslovak State, with no voucher privatization for the next three years.

We now provide more detail on our privatization plans for our main business.

### **8.1 Method of Privatization**

Our most urgent need is for extra capital, even if we do not decide to develop our business in telecommunications (the most capital-hungry option for our future). Therefore it does not seem appropriate for SR to be privatized by the voucher method, which will raise no new capital for the business.

In order for foreign companies' expenditure to be most productive for SR, new shares in the joint stock company should be issued, so that the money paid by the foreign companies is received by SR and can be used for investment. If the foreign companies first have to buy shares from the State, the money will be received by the National Property Fund, and will be of no direct benefit to SR.

We believe it would be sensible if we were privatized at the same time as SR Bratislava.

### **8.2 Form of Privatized Entity**

The privatized entity should be a joint stock company. Before privatization, all the shares will be owned by the State.

After privatization, the SR company will itself own shares in other enterprises such as the paging joint venture, Intes Fardubice and Postovni banka, the bank which specializes in the communications sector. These other enterprises will therefore not be directly privatized themselves, but they will be privatized indirectly to the extent of our interest in them, through the privatization of SR as their holding company.

### **8.3 State Share of Equity**

We currently plan that the State share of the equity should be 51-61 per cent, preferably nearer the higher figure. We acknowledge, however, that a majority State share may well deter foreign investors. This is because they will want to control an enterprise in which they will be investing substantial sums. Foreign investors will accept regulation if there is a clear and stable framework, but they will fear that if the State retains a majority shareholding it may use this to influence SR's policy in non-commercial ways.

#### **8.4 Share of Equity to be Held by Other Types of Owner**

We believe that we will benefit very significantly from a collaboration with foreign partners, some of whom should be among our major shareholders. We see some advantages in confining the share of our equity held by foreign investors to 30 per cent, rather than the 30-40 per cent range given in the Czech Republic strategy document.

The number of foreign partners chosen could vary from one to perhaps three or four. Our decision will be based on a number of criteria; these will include the range of skills provided, the likelihood of conflict within the management group and the relationship between the foreign partners. We will need to organize some sort of tender procedure so that we can compare the best offers from potential foreign partners.

One possible option would be that both SR Praha and SR Bratislava would collaborate with the same foreign partner. This option would be more attractive to the foreign investor if the two enterprises were to be privatized at the same time.

It might be possible for two or more foreign companies to form a consortium which would be represented by just one of the companies.

We see some advantages in having a portion of our equity held by Czech people. This could be achieved by selling some of the State's shareholding in due course.

We wish to investigate the possibility of our employees being involved in owning SR shares.

- (2) Completing the current investment in the building of the Intelsat earth station at Sedlec and securing customers for the telecommunications circuits.
- (3) Offering local loop radio access technology to SPT Praha.
- (4) Providing radio access in the local loop to a new competitor to SPT Praha (though not SR Praha itself).
- (5) Becoming a full secondary telecommunications carrier offering local loop, long distance and international services. This would require the addition of switching capability.
- (6) Developing the radio paging business in accordance with projections developed in the SR Praha, SR Bratislava, TDF business plan.
- (7) Offering trunked radio network services, based in large cities. The most likely option would be to pilot this service in Prague.
- (8) Expanding the current number of private microwave business networks to further customers.
- (9) Offering VSAT services to customers.
- (10) Expanding our engineering services business to potential customers for facilities and private network management.

#### **6.3.4 Other production and non-production services**

It will be important for SR Praha to rationalize these activities. Options arise in several areas.

##### Telegraph

There is a question over the future of SR Praha's telegraph business. The provision of telegraph transmissions has been an important source of revenue in the past, but long term demand for this service is doubtful. Given the range of alternative technologies in the market, and on the assumption that competition in the telecommunications market will be opened up, it is likely that our existing customers may choose to discontinue their business in the near future. SR Praha will address this issue over the coming months.

##### Agriculture

Our agricultural activities may have to be wound down to allow us to concentrate on our core businesses.

## Housing

SR Praha will also be addressing the question of whether it needs to support its current portfolio of accommodations, buildings and land for future operational requirements. For example, we have little need for the barracks which were used to house the soldiers who guarded some of our transmitters.

If housing is privatized separately in the second wave, we will receive none of the proceeds.

### **6.4 Option appraisal**

This section focuses solely on the options for SR Praha's three main business activities. Our views are set out in summary tables.

We will be updating the output of this section in the months leading up to the submission of our formal Final Privatization Plan to the Ministry. The results of subsequent analysis will allow us to put more robust financial numbers onto each of the business options, which will enable us to confirm or refine our initial views of the best overall business strategy for SR Praha.

SR Praha's Privatization Plan will include a detailed five- or ten-year financial forecast of revenue, cost and profit flows for each of the main activities.

Business Options  
Television  
First View

	Business Option	Sector	Need to act quickly	Size of annual investment	Length of investment	Need for partner(s)	Likely Risk	Higher Revenue	Lower Cost	Profit Impact		
1	Install cable to serve outlying areas	All	No	High	3-5 Years	Yes	Med	+	--	-		
2	Change band spacing on bands I and III to 5.5 MHz - Quality improvements and CCII1 compliance	All	No	25m	5-10 Years	No	Low	0	negl	negl		
3	Programme to upgrade equipment and reduce costs for stations 1 & 2	State	No	40m	5 Years	No	Low	0	++	++		
4	Further increase coverage on stations 1 & 2 - implement data transfer services	State	No	Low	1-3 Years	No	Low	?+	-	-		
5	Extend coverage of third station	Priv	Yes	35m	3-5 Years	Yes	Med	+	?-	?+		
6	Build fourth terrestrial station to maximum coverage around large cities	Priv	No	25m	2-4 Years	Yes	Med	+	?-	?+		
7	Offer fifth station based in Prague	Priv	No	25m	2-3 Years	Yes?	Med	+	?-	?+		
8	Active marketing of released frequencies to private broadcasters	Priv	Yes	Negl	Cont	No	Low	+	0	+		
9	Offer microwave links from the studio to low power private TV broadcasters	Priv	No	Negl	weeks	No	Med	?+	0	?+		
10	Offer digital data services to customers - eg Czechoslovak stock exchange	Priv	No	Low/ Med	1 Year	No?						

Values in Kcs

Business Options  
Television  
First View

	Business Option	Impact on other parts of business	Comments
1	Install cable to serve outlying areas	Can also offer telecommunications services via cable .	Low priority Could support ISDN in future
2	Change band spacing on bands I and III to 5.5 MHz - Quality improvements and CCIR compliance	-----	Only undertake if State gives full subsidy
3	Programme to upgrade equipment and reduce costs for stations 1 & 2	-----	-----
4	Further increase coverage on stations 1 & 2 - implement data transfer services	-----	Public broadcasting authorities unlikely to want this in near future
5	Extend coverage of third station		Large revenues, large investment Create some spare capacity Second half of 1992
6	Build fourth terrestrial station to maximum coverage around large cities	-----	Financed from own credit Apply early for frequency license 1993-1995
7	Offer fifth station based in Prague	-----	Financed from own credit Apply early for frequency license 1993-1995
8	Active marketing of released frequencies to private broadcasters	-----	Create marketing department
9	Offer microwave links from the studio to low power private TV broadcasters	-----	Much of equipment already in place
10	Offer digital data services to customers - eg Czechoslovak stock exchange	-----	-----

Business Options  
Radio  
First View

	Business Option	Sector	Need to act quickly	Size of annual investment	Length of investment	Need for partner(s)	Likely Risk	Higher Revenue	Lower Cost	Profit Impact		
1	Programme of equipment replacement to reduce costs and improve quality - Emphasis on MW/LW bands	All	No	Low 15m	5 Years	No	Low	0	++	+?		
2	Programme to increase national coverage on FM band II and to migrate from band I	All	Within 2 Years	Low 20m	3-5 Years	No	Low	+	+	+		
3	Market SR services to private customers - Existing SR idle capacity, frequencies freed under new law and subsequently by State radio	Priv	Yes	Very Low	Cont	No	Low	+	0	+		
4	Develop static/dynamic data transfer	All	No	Low 6m	1 Year	No	Low	1m ?+	0	?+		
5												
6												
7												
8												
9												

Values in Kcs

Business Options  
Radio  
First View

	Business Option	Impact on other parts of business	Comments
1	Programme of equipment replacement to reduce costs and improve quality - Emphasis on MW/LW bands	-----	Use of Dynamic Carrier Control
2	Programme to increase national coverage on FM band II and to migrate from band I	-----	High growth, depends on commitment of public broadcasters to FM Band I
3	Market SR services to private customers - Existing SR idle capacity, frequencies freed under new law and subsequently by State radio	-----	Create marketing department
4	Develop static/dynamic data transfer	-----	-----
5			
6			
7			
8			
9			

65