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TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY

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## I SUMMARY

### Background:

The United States Agency for International Development (USAID) has supported the Government of Hungary's Privatization Program since its inception. This assistance has been principally channeled through a Deloitte and Touche (D&T) team which has focused its efforts on supporting the development of the government's privatization agency, the State Property Agency (SPA).

### Coordinated and Responsive:

In an effort that has been coordinated with the support of a broad range of other donors and lenders, bilateral and multilateral, USAID has delivered a targeted technical assistance program which has been a major contributor to the development of privatization in Hungary. USAID's assistance has been viewed by its recipients as responsive, rapid, and relatively easy to access. USAID has become the "rapid response" donor/lender of preference for the SPA.

### Scope of Work:

The detailed, but generic Scope of Work of the D&T team has enabled it to carefully help target assistance quickly and appropriately within, and in support of, the rapidly evolving SPA and Hungarian Privatization Program. The Scope of Work focuses on institutional development and multiplier efforts at the organizational level, principally within the SPA. These, in turn, have a significant influence on the success of privatization in Hungary.

### Achievements:

During its first full contract year which was completed 25 September, 1991, the technical assistance delivered to the SPA took the following main forms:

- Provision of a Long Term Advisor/Project Manager
- Training assistance
- Financial management assistance
- Equipment assistance
- Control and information systems assistance
- Public information program assistance
- Program design and implementation assistance
- Investment promotion assistance

### The Future:

It is anticipated that USAID's support effort will take essentially these same forms during the next contract year with the continuation and/or expansion of the existing efforts.

### Policy and Success driven:

Continued support of Central Europe's fastest moving and most successful privatization effort is not only consistent with the economic policy of the United States, but is a vital component of that success.

## II BACKGROUND

### Key players in the beginning

In early 1989, three Hungarians involved in planning the Government of Hungary's Privatization strategy - Janos Martonyi (now State Secretary of the Ministry of International Relations and Deputy Chairman of the SPA), Mr. Lajos Bokros (now Chairman of the Budapest Stock Exchange, President of the Budapest Bank and a Director of the SPA) and Mr. Karoly Szabo (now the Deputy Managing Director of the SPA) - were invited by the US Embassy's Economic Section (Ms. Sandra Demsky) to attend a Privatization training course funded by USAID at the International Development Training Institute in Washington, D.C. The first Eastern Europeans to participate in any such program, they subsequently asked for technical assistance to help design and establish a privatization agency in Hungary.

Three of the resources at that seminar - Alec Tomlinson (former head of the Center for Privatization and now President of the Hungarian American Enterprise Fund), Paul Elicker (then head of the Center For Privatization) and Charles Twyman (A D&T privatization consultant and currently the Long Term Advisor (LTA) in the SPA) - coincidentally have played a continuing role in the development of the SPA and privatization in Hungary.

It was fortunate for the development of the teamwork underpinning the United States Government's assistance to the SPA that Mr. David Cowles of USAID was aware of and involved with the privatization process in Hungary from the beginning, first in his role at the Private Enterprise Bureau and currently, as the USAID Representative in Budapest under USAID's Europe Near East section.

Other key actors included the US Ambassador to Hungary, Mr. Charles Thomas, Mark Karns, in his role at the Private Enterprise Bureau, Robin McPhail, the D&T partner specializing in privatization and international lending agency support and D&T's privatization specialist, Ms. Teresa Mastrangelo.

### PHASE I - Concept

In January 1990, two USAID-funded advisors, Alexander Tomlinson and John Schermerhorn, participated in the planning phase of the Government of Hungary's (GOH) soon-to-be launched official privatization vehicle, originally called the National Property Agency (NPA). They gave conceptual guidance, outlined a recommended organizational framework and set out the steps which the proposed NPA should take to make itself quickly and professionally functional. Their basic guidance was to create a small transaction oriented operation, transparent in all of its activities, that should rely primarily on external resources such as merchant banks and accounting and law firms to carry out its transaction work.

One of the recommendations, to which the GOH agreed, was that the NPA should procure the services of a privatization specialist to advise its directors during its organization and implementation phase.

Based on its experience, D&T was requested to help prepare a terms of reference for such a specialist and to consider making a qualified individual available on a short term basis to respond to the needs of the GOH through the Center For Privatization.

## PHASE II - Organization and Execution

On 15 March 1990, Mr. Charles Twyman, a D&T privatization specialist was seconded on a short term basis to be the Privatization Advisor to the NPA (since renamed the SPA) through a contract between the Bureau for Private Enterprise and the Center for Privatization. When Mr. Twyman arrived in Budapest, the SPA consisted of 2 persons - Karoly Szabo, now the DMD, and a translator. Dr. Janos Martonyi gave daily guidance as the former Commissioner for Privatization, however his function had been formally ended with the 1 March, 1990 legal start-up date of the SPA.

Since March 1990 Mr. Twyman, with the strong support of the D&T team, including the American Manufacturers Export Group (AMEG) and Multinational Strategies (MNS) has worked directly with the executive directors of the SPA to help them structure an organization that will help define and achieve the objectives of the Hungarian Privatization Program. Mr. Twyman's role has been principally in the areas of organization, planning, finance, policy direction, donor coordination, and the management of technical assistance, USAID funded and other. He has periodically been involved in transaction work when his experience has been needed.

Notably, Mr. Twyman prepared the initial organization charts, directed the initial needs analysis work funded by the European Community (EC) Poland Hungary Aid to Recovery of the Economy (PHARE), prepared the SPA's initial foreign assistance funding budget, as well as its initial policy documents. He organized the initial equipping of the SPA and its first formal training through USAID. He likewise taught SPA staff in seminars and in one on one sessions. He was very involved in the initial privatization launches and in several subsequent product developments.

### Organizational Background

The SPA has continued to execute its privatization role while at the same time organizing, staffing, maturing, training, and having its role defined and redefined by the Parliament and the GOH. It has never had respite from transaction pressure while learning and developing its function. As a result, it, like the Privatization Program in Hungary, is pragmatic, transaction driven and fluid. It learns day to day and changes rapidly. The SPA is designed to perform its task over a 5-8 year period and then be dissolved.

The SPA is a creation of the pre-free election government. It is an independent agency with its own board of directors and an operating budget approved by the government. It presently does not report to or through any ministry. Since its March 1990 inception, the SPA has changed from being an agency reporting directly to the Parliament to an agency reporting to the government, specifically the Prime Minister. It has had one politically-driven change in the appointment of its Managing Director. Fortunately, it has maintained almost the same board members since their initial appointment (The SPA operated without a board of directors for its first 10 months). The present board is a working "Blue Ribbon" board which operates outside the realm of political influence as an independent entity.

Originally conceived to supervise privatizations and regulate the "spontaneous" privatization process, the SPA subsequently had been assigned to, or has assumed responsibilities for, the following:

- \* directing large privatizations
- \* organizing the retail privatization program (the sale of about 6,000 small shops)
- \* administering the warrant system under the compensation law
- \* administering a program to put state assets under management prior to their privatization
- \* tracking and dealing with warranty related issues in privatization sales
- \* directing the design, launch, and control of a "self privatization" program aimed at the entire middle-market. (This is a fast-track rapid response program designed to privatize privatization with minimal SPA involvement).
- \* generating significant statistical and other reports for the GOH and the donor community.

The SPA is essentially capped in terms of personnel -presently 120- and budgetary allocation. (By comparison the East German program employs over 3,000, the Polish Ministry of Ownership Change over 300, and the Czech retail privatization program alone over 1,500).

The SPA is designed to rely on external TA to do its job. The intent is to avoid creating a new, overstaffed, administrative bureaucracy and to stimulate the development of Hungarian consulting, accounting, and legal skills. The SPA is significantly dependent on donor and lending agencies to fund its activities.

An essential characteristic of the Hungarian privatization process is the strong and continuing commitment by the government - of all political persuasions - to carry the process forward. This political will is supported by a strong public consensus that a private sector dominated market economy is required in Hungary and transitional strains are to be expected and endured. It must be underlined that since the inception of the Hungarian privatization program, the GOH and the SPA have been very independent, self-confident and self-sustaining in the decisive policy areas. They are not driven by advisers, but use them when it is convenient and helpful.

#### US support to the SPA: Background

US aid to the Hungarian Privatization effort and the SPA is relatively small (about US \$1 million) and has been carefully targeted to supplement and support the efforts of other donors/lenders. By comparison, the grant resources being committed by the EC PHARE program total ECU 26 million, and the World Bank (WB) has committed loan funds of US \$10.5 million. In addition, the British Know How Fund has provided 3 advisors and the Canadian and French governments have each provided one advisor. The United National Industrial Development Organization (UNIDO) has sought ways to help. The Andrew Mellon Foundation provided some early training support and the Hungarian American Enterprise Fund (HAEF) has also assisted in training and other areas.

The PHARE program made its assistance available in two grant tranches of ECU 5 million and ECU 21 million, principally for transaction support. Unfortunately for all concerned, the PHARE program has encountered absorption problems. It has committed long term advisory support to manage its assistance.



The World Bank made a loan available (US \$10.5 million) for the support of 20 specific privatization transactions. This support is slowly getting absorption.

In the case of the SPA, US assistance has had impact well beyond its size by being there first, responding quickly to the agency's needs, and requiring a minimum of administrative support in return. It has been consistently administered and delivered by a team with continuity so that the wheel doesn't have to be reinvented every time a need is identified. (The benefit of continuity cannot be over-emphasized as it avoids the need for SPA managers to bring external consultant/advisors up-to speed again and again). In addition, US aid has been successfully levered by careful targeting.

The key components of the successful US assistance have been:

- \* the presence of a well qualified long term adviser that has fully integrated himself into the SPA.
- \* a carefully selected, teamed, technical assistance package to support the LTA's efforts.

Major deliverables have included:

- \* the equipment and systems support of the SPA.
- \* continuing training support.
- \* other carefully targeted assistance delivered quickly and quietly.
- \* support of the SPA's financial and administrative capacity (USAID has developed a niche role here which is most important for the success of the Privatization effort in Hungary).

#### Program Design Background

The design of the program of support to the SPA was very well defined. Based on the privatization experience of USAID and D&T, it was determined that the SPA assistance program should be professional, flexible, fast responding, and self-sustaining. This meant that an experienced team with a combination of skills should be pre-positioned to help the LTA work with the SPA to identify and carry out essential support tasks.

The combination of a flexible TA program, an experienced LTA and strong administrative support from the D&T Washington D.C. office was key to the success of the program.

On the practical level, the LTA had the basics of his office and personal support costs provided for. He was taken care of institutionally by D&T. The LTA had access to funding and skills (through the D&T network and the contract teaming partners) to solve problems as they arose. The process for approving and mobilizing support for each task was quick, effective and professionally managed with very close teamwork at the USAID project officer level.

The entire support program for the SPA was built around the needs of the client - the SPA and the GOH. It was designed to help the client solve its problems, not create additional administrative or policy burdens to bear. The speed with which the Privatization Program in Hungary was evolving and the growth needs of the SPA could not sustain the normal project cycle of support delivery. This was evidenced at every turn in the day to day dealings of the GOH and the SPA with other donor and lending agencies during this crucial start-up phase.

### III OBJECTIVES

The principal objective of the USG aid assistance to the Hungarian privatization effort, embodied in this contract to provide Technical Assistance to the State Property Agency of Hungary, is to help Hungary develop a self-sustaining privatization program that is largely market driven. The desired goals are to channel support to help Hungary avoid the problems of using institution-driven thinking instead of transaction-driven thinking, focus on creating the minimum necessary apparatus to support transactions and build free market supporting models and private institutions.

The further objective is to help sustain the strong political will supporting the Privatization process in Hungary by helping to solve the "easy" problems confronting the process. Such areas as equipping, training, technology transfer of working models and TA to help resolve Hungarian problems are easy fixes and within the area of aid delivery competence.

Managing the political aspects of the Privatization process, judging its appropriate pace, dealing with the social safety net issue and designating the program's leadership pattern are the exclusive realm of Hungary's leadership.

In all cases, the initiatives in the privatization program are generated by Hungarians. The initiatives must be perceived as helping to solve Hungarian problems which must and can be dealt with. By focusing resources selectively, considerable guidance can be provided.

During the first contract year, the objective was to guide the modest US aid funds made available in a targeted manner so as to break roadblocks and give support to the SPA's management. The support delivery was always carefully crafted to support the SPA - not to push it out of the way. It was important that the support be perceived as solving problems, not creating them. The support was guided to have key desired organizational effects on the SPA and the Privatization Process in Hungary.

The principle governing US and other major donor/lender assistance is that it would be a great loss for all concerned if the Hungarian privatization program should falter or fail because it does not receive the supporting knowledge and funding required to move it forward. It would be equally inappropriate to flow funds or advisors that would not support the reasonable and immediate progress of the privatization program.

There should never, at any time in the program, be a question as to who is in charge. The Hungarians are in charge. There should not be a problem of advisors "doing" without developing Hungarian skills. There should not be any doubt that the success of the privatization process in Hungary will be a Hungarian success.

#### IV ACHIEVEMENT OF SCOPE OF WORK

Background: The D&T team was guided in its work with the Hungarian privatization program and the SPA by a set of specific objectives. These objectives comprise the Scope of Work of the contract. They were achieved through individual actions taken by the LTA or through specific task definitions reflecting support requested by the SPA, and reviewed by and preapproved by USAID.

To understand the successful operation of this project, it must be understood how the interaction between the SPA and the LTA takes place. The LTA is fully integrated into the SPA. The LTA knows the organizational culture of the SPA, its key operating officers and the staff. He is part of the reporting and policy making layer of the organization and tracks all the major operational areas. He works carefully with directors and staff to define how he or other USAID funded technical assistance can support the SPA's activities without conflicting with the activities of other donor/lenders or local funding. This high level of integration is critical in order to accomplish the Scope of Work.

Note: Individual pieces of technical assistance, for instance the design and implementation of a Management Information System, the design and subsequent assistance in implementing a training program and the design of a Public Information strategy are incorporated in the report by reference, but are not detailed here nor incorporated as appendixes given their length. Each is a separate deliverable and available in a separate submission "First Year Reports & Deliverables October 1991".

The following is the Scope of Work outline with a summary of the achievements during the reporting period.

##### SCOPE OF WORK

#### 1. Help Define the Operational Framework of the SPA

The D&T team has been very involved in all phases of establishing the operational framework of the SPA.

- \* The LTA provided the core strategy statement for the Agency which is still valid and in use. (Appendix III)
- \* The LTA helped prepare the TOR for the initial TA project to set the formal operational parameters of the SPA.
- \* The LTA helped evaluate the original TA proposals. (Appendix V)
- \* The LTA helped direct the initial TA and set the direction of the SPA. (Appendix IV)
- \* The LTA's Initial Organization Charts were those around which future efforts were based. (Appendix XIII)
- \* The Current Organization Chart (Appendix XIV) and the LTA's Organization Proposal (Appendix XV) define the SPA now and the direction in which it is moving.
- \* The 13 August, 1991 Assistance Request from the SPA to the USAID Representative in Budapest (APPENDIX XX) is an outline of the SPA's new initiatives which will flow into its operational framework. The D&T team helped to develop these initiatives and the related request and will continue its involvement by helping to guide the proposed efforts and anticipated TA.

- \* In addition the MIS, Financial Management Assistance, Training Program design, and training all have had significant operational impact.
- \* The Organization Proposal (Appendix XV) outlines the LTA's thoughts on the directions the operational framework should take, namely strengthening the systematic support function while focussing more direct attention on the line functions.

Comment: The SPA has significant organizational control and support needs. A functioning MIS, more systematic financial controls, and a strengthened organizational structure with systematic training support should help address these needs. The new initiatives require up-front systematization to prevent a repeat of the organizational catch-up environment the SPA was forced to work within and still experiences. The LTA devotes a significant amount of effort to this area.

## 2. Help Prepare a Funding Strategy for the SPA's Activities

The D&T team has been providing financial management leadership at the SPA.

- \* The LTA prepared the SPA's basic financing strategy and is helping execute it. (APPENDIX VII)
- \* The LTA has been central in the execution of this multi-donor funding strategy. (APPENDIX VIII)
- \* The LTA prepared the SPA's budget submissions to the EC PHARE program (APPENDIX IX)
- \* The D&T team regularly interfaces with the World Bank (WB) and other donors, and helps package the SPA for donor consumption. (APPENDIX XVI)
- \* The LTA helped prepare the GOH's national donor funding request to the USG. (APPENDIX X)
- \* The D&T team is working on a regular basis with USAID and the SPA on the continued funding requirements of the SPA and related efforts. (APPENDIX X and XX)
- \* The referenced APPENDIXES X and XX contain the recommendations of the LTA on the GOH's funding strategy for the USG.
- \* The WB, PHARE, Know How Fund, Canadian, EBRD and other support strategy assistance examples are part of APPENDIXES VI, VII, VIII and IX.
- \* The GOH and the donor community are making privatization the core effort in the economic reform of Hungary. A strategic decision has been made by the GOH to support the privatization effort with a major portion of the donor funding available in the first years of the new government's activities, since privatization is central to the redevelopment of Hungary's economy.
- \* The LTA recommended and helped design the SPA to be initially dependent on donor funding (3 years). He is helping the SPA execute that strategy. As the SPA matures, its privatization proceeds flow will make it independent. If the SPA privatization efforts fail, donor support will most likely be withdrawn and the SPA will wither. It appears that the SPA's privatization efforts are having considerable success, so the strategy is on track.

### 3. Help Define the Organizational Needs of the Privatization Process

Much of the work in this area overlaps with efforts in TASK 1 (Help Define the Operational Framework of the SPA) and the contribution of the D&T team is dealt with there. Other efforts include:

- \* The Current Organizational Chart (Appendix XIV) and the Organization Proposal (Appendix XV) are most relevant to describe how the D&T team has helped the SPA evolve.
- \* The State Property Agency Assistance Request of 13 August, 1991 (APPENDIX XX) summarizes the basic organizational needs and directions of the SPA.
- \* The Warrant System and Self-Privatization Program Assistance Requests (APPENDIX XXI and XXII) provide guidance on other organizational needs as will the Unit Trust and other initiatives.

An important element which does not emerge in the organizational structure is the effective institutionalization of the SPA as an independent, technocratic agency. The Board of Directors operates free of political pressure and the directors are their own most demanding critics. The senior staff of the SPA generally work a ten hour day which is not a normal GOH work pattern. This is indicative of the institutionalization of the SPA principles initially set out. (APPENDIX III)

The LTA recommends continuation along the same organizational path. Strong structural reinforcement should be added by way of good information and control systems supported by top quality training and the systematic accomplishment of new initiatives.

### 4. Help Define the Initial and Longer Term Organizational Structure of the SPA

Tasks 1, 2, and 3 flow into this task. It should be highlighted that the Buyer Initiated Privatization Program and new Self-Privatization Program are two major initiatives that signal the SPA's effort to remove itself as a bureaucratic barrier to a market-driven privatization process.

The Hungarian Privatization Program's close attention to the fact that privatization is a market-driven function and not a primarily government-driven function has emerged as a most significant conceptual difference between the Hungarian Program and those of other Eastern European countries.

The SPA's organizational structure will continue to be built around this concept and the concept of the SPA as a small, self-eliminating effort.

The SPA will continue to be largely reliant on external TA to accomplish its task. A principle aim will be to help develop the requisite technical skills in the Hungarian marketplace for a successful market economy.

#### 5. Help Define the Office and Equipment Requirements of the SPA

The D&T team and USAID defined the equipment and system needs of the SPA, provided the core equipment, designed and put in place the agency's Local Area Network (LAN), designed and is implementing its Management Information System (MIS) and helped solve copier and FAX needs. The initial USAID equipment delivery was the first and most urgently needed equipment of the SPA. This equipment kept the SPA from faltering badly.

The USAID's responsiveness in the equipment example set the tone for the way USG assistance is perceived: focussed, appropriate, professional and rapid. It is the project's objective that this should continue.

The D&T team has made recommendations as regards the further equipment and system needs of the SPA and will continue to do so in an advisory capacity as the SPA evolves. The current equipment status and needs are part of a separate submission.

It is worthwhile to note that the costs stemming from recommendations of the D&T team are partially met by the EC PHARE Program and other donors, and partially by the GOH.

#### 6. Help Define the Personnel Requirements of the SPA

The local staffing needs of the SPA were set out in the initial external consultancy effort (EC PHARE funded) with strong inputs from the LTA. Basically, these guidelines have been adhered to. The long term advisor strategy - and much of the short term - has been a major responsibility of the LTA. (APPENDIX VI)

The role of foreign advisors and the ability of the SPA to absorb them (APPENDIX II) is limited by five major factors:

1. Foreign advisors' support needs, such as equipment, translation, and secretarial, their initial competence and learning requirements, and their expectations about having access to management, can mean that the "cost" element of using a foreign advisor can exceed his or her potential productivity.
2. Excess reliance on foreign advisors can lead to dependency in situations where the effort should be Hungarian, even at the cost of being less tidy.
3. Advisors must be made available as mentors designed to be phased out. They cannot and should not be expected to be used as policy makers.
4. In many instances, the language issue is major, in others it guarantees that the principles 2 and 3 above are easy to adhere to.
5. Most importantly, the individuals with whom the foreign advisor works must want his or her assistance and know how to direct it to obtain maximum advantage.

The D&T team is working daily with the SPA on the design and implementation of its training program.

The D&T team has recommended initiating a formal job description and evaluation process within the SPA. Training, job descriptions, evaluation, and hiring are the core of a personnel cycle which does not currently exist within the agency. The LTA and the D&T team are involved with this effort and will be further involved.

7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program

The D&T team designed the SPA's training program and is helping to implement it. USAID funding for training has been available at key junctures in the history of the SPA and has made an invaluable contribution to Privatization in Hungary. Examples are the previously mentioned initial training at IDTI, and focussed legal training at the International Law Institute (ILI) in Washington, D.C. (APPENDIX XIX).

The SPA has a tremendous need for training in job-related skills. Formal training in some instances is available. Working alongside professionals within an appropriate environment such as with merchant bankers involved in merger and acquisition activity (M&A), with lawyers in M&A negotiations or with accountants on valuation contracts is often the preferred route.

Funding for the various targeted training needs of the SPA should be made available. The EC PHARE program is funding most of the European-based training, however it has been difficult to access these funds. US based formal or informal training of SPA staff is not currently available except on an extraordinary basis. (APPENDIX XIX) In many instances, the Hungarians prefer to apply a US model to their activity. Support of this preference should be possible. The D&T team prepared a training manual which outlines the training needs of the SPA and explains policies and procedures as regards training.

8. Help Define the Prioritization of Privatization Activities

Prioritizing privatization must be an intensely Hungarian-driven activity as it ties very closely to the necessity of maintaining the political will to move the process forward.

The LTA's contribution has been in the area of defining the following principles:

- \* get the process moving and keep it moving
- \* be pragmatic and flexible
- \* privatization is a transaction driven process
- \* build on success
- \* create models
- \* hire professionals - don't become an underskilled merchant banker/valuer
- \* be aware and nurture the many privatization linkages in the economy particularly those which encourage investment.

Frequent informal counseling with SPA staff repeat this approach.

The new sectorial privatization program initiatives which were incorporated in the Report to Parliament (APPENDIX XVII) are driven by the above mentioned principles. Other activities currently underway are similarly driven. The Parliamentary Report details the candidates for immediate privatization activity. There are also lists of new enterprise privatization candidates being generated by the self-privatization program which currently incorporates 348 firms in its first phase.

The LTA, working with the various funding sources available to the SPA, helps reinforce these principles.

In addition, the D&T team is constructing the core of the enterprise database for the SPA (and probably for the Hungarian Investment and Trade Promotion Agency), to help systematize the prioritization and investment stimulation process.

9. Help Define the Critical Privatization Program Linkages in the Economy

Privatization is an activity which is not limited to the sale of assets. It requires support in the legal, economic, political and other spheres. Coordination of the various agents who must implement the components of the national privatization strategy once the strategy has been decided is most crucial.

Hungary has made privatization the cornerstone of its economic turnaround. It is the job of the SPA and the various ministries and agencies to make their efforts contribute to the success of the whole. Coordination of "linkages" are essential for any player to succeed in such a program in a period of rapid change.

The D&T team identified this principle early (APPENDIX IV, April 1990 Action Items) and has helped follow through ever since.

- \* The SPA has a close linkage to the Investment Promotion Office at the Ministry of International Economic Relations (MIER). This linkage is fostered by an SPA (USAID) funded advisor, a joint investment brochure being produced with SPA (USAID) funding support, the MIS linkage, and the part-time MIER person at the SPA.
- \* The SPA's role in the WB/PHARE restructuring program as a watchdog agency, the LTA's participation alongside the SPA in the Organization for Economic Cooperation and Development (OECD) group of 24 assistance donors for Hungary, and personal ties into the MIER, the Ministry of Trade and Industry, the National Bank of Hungary and the Ministry of Finance are other areas where the D&T team and the LTA help the linkages happen.
- \* As the SPA is the ultimate GOH agent in any enterprise sale, it is receiving the cooperation and attention it deserves. To the degree that it is helping the privatization program succeed, it gets additional cooperation.

It is well worth noting that the foreign donor/lending agencies activities are a strong encouragement to forge linkages among involved agencies within Hungary.

The conditionality language of the IMF and World Bank frequently refers specifically to the success of programs lodged in one GOH organization or another. If a given program fails, all are at risk.

Similarly, the USG, the EC and others wish to have a prioritized, consolidated and coordinated request submitted to them. If the GOH entities don't work together, they don't get the attention they merit.

The SPA as a multiple donor user has been at the forefront of trying to make this coordination happen. Its close involvement in the USG aid request is a case in point. This is closely replicated in the PHARE program and, to a lesser extent, the WB process. (APPENDIX X)



10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program

This activity involved much of the LTA's early efforts as the SPA did not have a Chief Financial Officer (CFO) and the GOH's Donor Coordination Office had not yet become functional. At the recommendation of the LTA, among others, the SPA has just appointed a CFO.

The LTA assisted in deriving and budgeting the SPA's donor financing needs (APPENDIX VII and VIII), detailed work on the design and management of the PHARE Budget until a PHARE Financial Administrator could be found (APPENDIX IX), and was involved in the USG Donor Funding Request.

The LTA is now focussing more of his time on the area of coordinating USG assistance to the SPA as its needs in the other major funding areas are gradually being assumed by specialized individuals. (APPENDIX XX, XIX, XXI, and XXII)

Detailed guidance in obtaining assistance in several areas, including training, law, accounting and systems, among others, was given in the process of managing the donor funding. Paragraph V SHORT TERM TECHNICAL ASSISTANCE AND TRAINING UNDERTAKEN gives a summary of the US funded activity with which the D&T team was involved. The involvement of the LTA in EC related activity before the EC financial administrator was hired, and involvement in the World Bank funding of the First Privatization Program (US \$10.5 million in loan funds) was also considerable and extended from budgeting to tendering and contract term definition.

The D&T team is currently working with the CFO to establish the financial control and management system required by the EC and World Bank. These and other TA management efforts should continue.

11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program

The privatization task is too large, and the time and economic pressure are too great to permit the privatization process in Hungary to be completely managed by the GOH. In addition, the people of Hungary and its technocratic leadership have a belief, based on 40 plus years experience, that something as important as Privatization should not be fully entrusted to the hands of the Government. The objective, at the time of design of the SPA, was to make the SPA incapable of becoming a new overgrown ministry by limiting its size, budget, and role. Thus, the SPA was put in place to protect the Privatization Process by providing sufficient oversight to defuse major political criticism while allowing the market-driven process of privatization to move ahead.

In addition, Hungary's acceptance of the principle that privatization must be driven by investors (domestic and foreign) wanting to invest in business and not driven by privatization agencies, no matter how comprehensive and effective, is key to understanding why the integration of the spontaneous process into the mainstream of Hungarian privatization was simply a matter of time. The design restrictions on the SPA made this a higher likelihood as the program could not be a success if the SPA smothered it with control.

The GOH has reduced subsidies to a minimum. Enterprises in Hungary are encouraged to privatize because it is the way to stay alive. The SPA is not physically in a position to review, much less add value to, the approximately 2,000 smaller enterprise privatizations (liquidations or mergers) that are being forced to take place.

The SPA has announced several programs which bring clear recognition of this market reality:

- \* The SPA launched a program to support investor-led privatizations, thus unblocking marketable enterprises which were resisting privatization. This program lends considerable impetus to the spontaneous privatization process among the larger enterprises as they must be responsive to private market "demand" and can no longer simply choose to make themselves a self defined "supply".
- \* The SPA has just launched a "Self-Privatization Program". Its first tranche is directed at the smaller enterprises (under 300 employees). The program provides that if firms in that category work out a privatization strategy with one or more Hungarian private consulting firms, of a pre-approved list of about 80, the SPA will consider the transactions pre-approved. This could ultimately involve approximately 1000 firms. As currently envisaged, the second tranche will encompass firms with less than 1000 employees, have a more select list of pre-approved consulting firms and include about 800 companies. Thus, the SPA has limited its responsibilities (and any delay it might cause) in either its active involvement or regulatory role to a total enterprise population of about 600.

Through the "Self-Privatization Program," the GOH has effectively legitimized and simplified the spontaneous privatization process for smaller concerns, provided a dramatic stimulus to the Hungarian consulting industry and focused its limited resources on the major enterprises in Hungary where the bulk of the rewards of Privatization are to reaped.

The D&T team has contributed to the integration of the spontaneous privatization phenomena by helping to design policy and organize and fund the SPA. The D&T team now recommends that the Self Privatization Program be helped to achieve its goal through institutional support and significant consultant support cost sharing at the actual transaction level.

#### 12. Help the GOH and the SPA Understand the Role of ESOP's and Specialized Tools That May Have a Suitable Role in the Privatization Program

Examples of areas where the D&T team has assisted include:

The GOH has taken a balanced position on Employee Share Ownership Programs (ESOPs). It has legislated that in privatizations, while employees should be given preferential consideration for some participation in their employing enterprises, they should receive no price or availability preference above a twenty percent share.

The GOH is considering developing Unit Trusts as a vehicle to pool enterprise shareholdings. The D&T team has supported and encouraged the development of this idea.

The D&T team has taken the lead in developing the mechanics of handling the Warrants under the compensation law and identified the market linkages in the development of the stock market, brokerages, secondary markets and investment pooling.

## V SHORT TERM TECHNICAL ASSISTANCE AND TRAINING UNDERTAKEN

### 1. Equipment

The D&T team:

- \* identified the SPA's equipment needs:
  - computers
  - copiers
  - faxes
  - typewriters
  - telephone switchboards
- \* designed an equipment funding strategy utilizing a mix of USAID rapid response funding and EC PHARE slow response funding.]
- \* designed the SPA's computerization program
- \* designed the SPA's local area network (LAN)
- \* ordered and installed the SPA's first and subsequent core computer system and software
- \* ordered and installed the SPA's initial faxes and copiers
- \* trained and supported the computer staff of the SPA
- \* continues to support the SPA's equipment needs definition and funding strategy.

### 2. Training

The D&T team helped provide a broad range of assistance in the training area.

- \* A key component in the LTA's day to day activity as well as the activity of any D&T team member working for the SPA effort is training and mentoring. This has taken the form of organized and informal training sessions and considerable one-on-one effort.
- \* The D&T team has participated in sending two six member teams and one three member team for training in privatization at the International Development Training Institute in Washington D.C. (All USAID funded).
- \* The D&T team arranged and supported the training of one SPA senior analyst at a financial analyst course at the First National Bank of Chicago. (First Chicago paid for course, USAID for transport and per diem).
- \* The D&T team arranged and supported the training of three SPA lawyers in negotiating with foreign investors at the International Law Institute in Washington D.C. (The Hungarian American Enterprise fund paid for courses and per-diems and one airfare, World Bank for the other two airfares).
- \* The D&T team wrote the training manual of the SPA.
- \* The D&T team did the training needs assessment for the SPA.
- \* The D&T team prepared the database containing an inventory of existing skills.
- \* The D&T team supported, on a two day a week basis, the establishment of a training unit at the SPA. This support continues.]
- \* The D&T team has trained the SPA computer team in LAN management and, on a continuing basis, the new Management Information System.
- \* The D&T team has provided briefings and support to SPA personnel during their activities in Washington, for instance on World Bank missions or similar activities.]

### 3. Technical Assistance

In addition to the support provided to the SPA by the LTA, the D&T team engaged in several specific tasks. The main deliverables of these tasks are incorporated in the separate submission entitled "First Year Reports and Deliverables, October 1991". The major tasks were:

- i. design and installation of a Local Area Network to accommodate the projected lifecycle needs of the SPA. The system is IBM PC driven and Novell based and can serve up to 250 users.
- ii. design of a sophisticated Management Information System built specifically around the needs of a Privatization program. This custom designed program is expandable to accommodate the full range of needs of a Privatization program. The core data base of the program is the entire enterprise portfolio of Hungary. This system is still being implemented. Upon completion, this system should be an adaptable model to other settings.
- iii. design, development and initial execution of a Public Information Strategy for the SPA. (Pending the receipt of PHARE funding, the Project funded public opinion samplings to identify the key areas on which the program should focus). This program continues.
- iv. The design of ways to improve linkages between the activities of the SPA and the investment promotion efforts of the Government of Hungary. This has resulted in formalized linkages between the SPA and the Ministry of International Relation's Investment and Trade Promotion Agency. This effort continues.
- v. financial control efforts of the SPA to specifically include a procedure and program to manage the World Bank funds of the SPA. This effort continues.
- vi. development of the training manual for the SPA and delivery of systematic training support (see the training section above).
- vii. development of a joint Investment and Trade Promotion Agency/State Property Agency "Brochure on Business Issues of Privatization and Investment in Hungary". It is foreseen that this will be distributed through the commercial offices of Hungarian embassies worldwide and by Government officials. The finalization of this project continues.

## VI RECOMMENDATIONS FOR FUTURE USAID SUPPORT

The main direction of the present USAID effort in support of Hungary's privatization process and the SPA should be continued. This direction is to continue niche support in institution building and "multiplier" efforts within the SPA and in related activities that accelerate the privatization process. USAID should not become involved in transactions on other than a pilot basis as the funding requirements are substantial and massive funding for major transactions has been made available by other donors/lenders.

The basic areas of continued effort during the next annual cycle should include at their core:

1. Continuation of the Long Term Advisor/Project Manager
2. Equip the Self-Privatization effort. Copiers (2 large) for the SPA plus specialized soft-ware and equipment add-ons to what is presently in house at the SPA.
3. Complete Implementation of the Privatization Information System
4. Continue support of the training program and help make available USA based training.
5. Continue Public Relations support
6. Continue and increase Financial Management Support - Technical, Accounting, Financial and Management Control, plus mentoring Assistance - to the Finance Director.
7. Develop the Self Privatization effort: equipment, systems, organization and information program support.
8. Provide Compensation Note Program advisory assistance and support to include the development of a registry system and asset holding (unit trust like) vehicles.
9. Assist Hungary's investment promotion effort to include the provision of a Long Term Advisor with the related technical assistance support.
10. Provide assistance to institutionalize the lessons learned in the first months of the SPA's activities: Operations manuals, job descriptions, personnel policies.
11. Long Term advisor support in an area (or areas) where absorption is possible and appropriate (ie: Investor Driven program, self-privatization program).

The individual efforts that would be recommended by the D&T team in line with the above list would be, as is the current practice, incorporated in individual task requests and reviewed carefully with USAID before a commitment is made to undertake them. Almost all of the above recommended efforts are continuations or expansions of present activities.

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INCORPORATED BY REFERENCE: "First Year Reports & Deliverables, October 1991, Technical Assistance to the State Property Agency of Hungary, Contract No. ANE-0002-C-00-0047-00" Deloitte & Touche, submitted separately.

SECTION C - STATEMENT OF WORK

TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY

I. BACKGROUND

In January, 1990, two A.I.D. funded advisors, Alexander Tomlinson and John Schermerhorn, participated in the planning phase of the Government of Hungary's (GOH) soon to be launched official privatization vehicle, the National Property Agency (NPA). They gave conceptual guidance, outlined a recommended organizational framework and set out the steps which the proposed NPA should take to make itself quickly and professionally functional. One of the recommendations, to which the GOH agreed, was that the NPA should procure the services of a privatization specialist to advise the Director of the NPA during the organization and implementation phase.

Beginning in March 1990, Mr. Chick Twyman of Deloitte & Touche was hired through PRE's contract with the Center for Privatization to be the Privatization Advisor. Mr. Twyman is now working with the Director of the NPA, since renamed the State Property Agency (SPA) to help structure an organization that will achieve the objectives of the Hungarian privatization process. Throughout his tenure as the Privatization Advisor, Mr. Twyman has been instrumental in helping the SPA to determine and refine its policies in a timely manner thereby enabling the privatization process to move along quickly.

The SPA is now in the critical organization stage of its development and the services of a privatization advisor are crucial to ensure that the SPA is properly structured and staffed and that appropriate policies are adopted. Because of the exemplary job Mr. Twyman has done and the strong preference to maintain continuity, the GOH has formally requested (letter attached) that the United States Government (U.S.G.) continue to fund the services of Mr. Twyman through a contract with his employer, Deloitte & Touche. As one of the "Big Six" accounting and consulting firms, Deloitte & Touche has demonstrated capacity to field short-term technical assistance and training in the area of privatization quickly and effectively.

In order to maintain the momentum that the SPA has gathered over the past few months, the decision has been made to waive full and open competition (see attached justification) and to enter into a direct contract with Deloitte & Touche. Because of the important role Mr. Twyman has played in the privatization process, he has been designated as key personnel to the contract.

## II. OBJECTIVE

The objective of the institutional contract is twofold: 1) to provide one long term advisor to the State Property Agency who will serve as the senior Advisor on the privatization process and in restructuring and privatizing individual enterprises and 2) to provide short-term assistance to facilitate the privatization process.

## III. SCOPE OF SERVICES FOR TECHNICAL ASSISTANCE

### A. Level of Effort

The contractor will provide (a) a Long-Term Advisor (LTA) for 12 months and (b) short-term consultants and or short-term training of up to 24 person months to be provided over a 12 month period.

### B. Coordination and Reporting Requirements

The Long-Term Advisor will work with the Director of the State Property Agency and have reporting responsibilities to ANE/EUR. The Long Term Advisor will be required to provide monthly progress reports and a final report encompassing the specific areas mentioned below. The LTA will also arrange for the institutional contractor to provide short term advisors and trainers to assist with specific problems related to the restructuring and privatization process.

### C. Specific Tasks:

#### Long-Term Advisor

#### 1. Help Define the Operational Framework of the SPA:

Work with the Director of the SPA and GOH officials to bring together the various legislated, legal, and Executive orders that establish the guidelines and framework for the activities of the SPA.

-Deliverable: A part of the final report will outline the parameters of the SPA and define areas that require clarification or appear to be problems.

#### 2. Help Prepare a Funding Strategy for the SPA's Activities:

Work with the GOH and the Director of the SPA to prepare an execution oriented workplan that will attract the support of appropriate donor agencies. Assist as appropriate by laying the groundwork with the relevant agencies and assure the various agencies are coordinating their privatization activities with the SPA.



-Deliverable: Part of the final report will outline contact activities initiated and the most likely components of the GOH's funding strategy with appropriate recommendations. ]

3. Help Define the Organizational Needs of the Privatization Process:

Work with the GOH and the Director of the SPA to define the short and long term organizational needs of the privatization process. Assist then in institutionalizing the decision making apparatus in support of the privatization program. ]

-Deliverable: The final report will outline the policy and decision making apparatus that is evolving to support the privatization process with appropriate recommendations.

4. Help Define the Initial and Longer Term Organizational Structure of the SPA:

Work with the GOH and the Director of the SPA to help structure an organization that will achieve the objectives of the Hungarian privatization process without institutionalizing a bureaucratic barrier to market activity. ]

-Deliverable: Part of the final report will consist of an outline of the structural framework that is evolving for the SPA with appropriate recommendations.

5. Help Define the Office and Equipment Requirements of the SPA:

Work with the GOH and the Director of the SPA to help define the physical space, communications, computer and transportation requirements of the SPA so as to assist them in analyzing their funding needs. ]

-Deliverable: Part of the final report will incorporate a basic equipment and facilities needs list.

6. Help Define the Personnel Requirements of the SPA:

Work with the GOH and the Director of the SPA to help define the type of staffing needs that the SPA will have and work with them to establish likely sources for the needed skills and a recruitment plan. ]

-Deliverable: Part of the final report will outline the basic recruitment strategy to be followed by the SPA.

7. Help Define the Training Needs of the NPA and Help Initiate an Appropriate Training Program:

Work with the GOH and the Director of the SPA to help define the likely types of training that will be needed by the staff and policy makers involved in the privatization process. Try to establish those areas where training should be formalized and scheduled.

-Deliverable: Part of the final report will address the projected training needs of the privatization process.

8. Help Define the Prioritization of Privatization Activities:

Work with the GOH and the Director of the SPA to analyze available information on Government owned entities and begin to systematize them with the objectives of creating prioritization lists that will be the objectives of the initial SPA activities.

-Deliverable: Part of the final report will detail the progress made in defining candidates for immediate privatization activity.

9. Help Define the Critical Privatization Program Linkages in the Economy:

Work with the GOH and the Director of the SPA to understand the critical role the privatization program plays in a broad range of other national activities; capital market development, enlargement of the tax base, retraining workers, expanding export earnings, expanding political linkages in the EC and the rest of the world.

-Deliverable: Part of the final report will detail the linkages viewed as critical at the outset of the program.

10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:

Work with the GOH and the Director of the SPA to help them define their technical assistance needs and schedule that that TA so that it progresses logically and appropriately and be integrated into and support the program.

-Deliverable: Immediate assistance will be given to help prepare terms of reference for technical assistance in the areas of: Legal and regulatory matters, and training needs in accounting/valuation assistance, systems assistance, legal assistance, Merchant banking assistance, consultancy and other team assistance. Part of the final report will detail efforts undertaken in these areas.

11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:

Work with the GOH and the Director of the SPA to define a strategy for bringing value, systematic assistance and process definition to the spontaneous privatization phenomena. ]

-Deliverable: The final report will outline progress in this area.

12. Help the GOH and the NPA Understand the Role of ESOP's and Specialized Tools That May Have a Suitable Role in the Privatization Program:

-Deliverable: The final report will outline the status of such issues as ESOP's and will make recommendations as to the required followup. ]

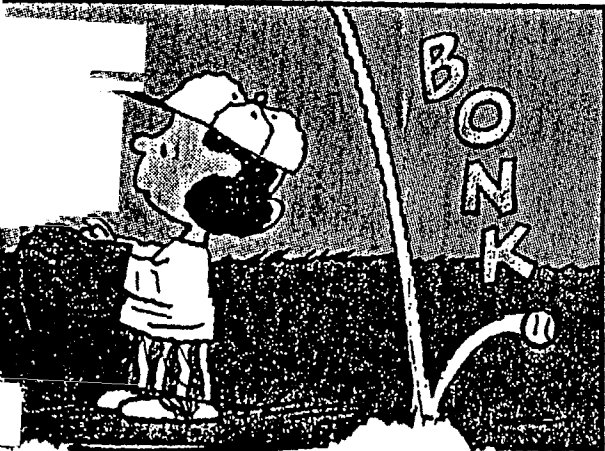
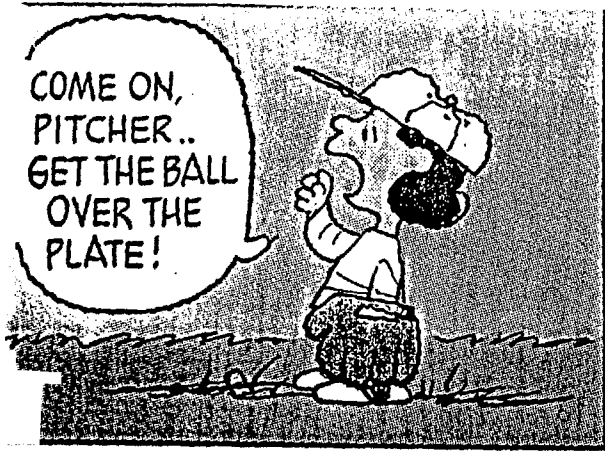
D. Short-Term Technical Assistance and Training

The contractor will provide on a timely basis short-term technical assistance and training as requested by the SPA. The TA will be provided in such areas as legal and regulatory matters, accounting, valuation assistance, and assistance in merchant banking and systems. Training will most likely be in such areas as systems,

E. Key Personnel

Because of the exemplary job Mr. Twyman has done and the strong preference to maintain continuity, the GOH has formally requested that the United States Government (U.S.G.) continue to fund the services of Mr. Twyman through a contract with his employer, Deloitte & Touche. Mr. Twyman's academic credentials, practical experience, credibility and the fact that he is a "proven product", make him the ideal candidate to provide the requested services. He is in a unique position to quickly and effectively continue the work he has begun. As it is clear that, without Mr. Twyman, the SPA would lose much of the critical momentum it has gathered over the past few months, Mr. Twyman is being designated as "key personnel" under this contract.

End of Section C



26

SEALER

## HUNGARY

### THE STATE PROPERTY AGENCY

#### BACKGROUND:

Hungary's need to revitalize its economy is everywhere apparent. Decades of trying to make a Centrally Planned economy function at a level of efficiency approaching that of the regulated market economies of the West have failed. Hungary's leadership has universally endorsed a rational and fair transformation of Hungary's economy from one that is 90% in the hands of the Government to one that is dominated by the private sector. The target set is to have 70% of the economy in private hands within 5 years.

Hungary has achieved the objective of giving its people political freedom of choice, a well executed privatization program gives its people the critical second freedom, the freedom of economic choice.

There is no reason why Hungary with its rich agricultural and human resources cannot transform itself. It is strategically located in the middle of Europe. It has a homogeneous, literate, and well disciplined population. It has a serviceable infrastructure upon which it can readily build. The dynamism of a free market economy is the missing component.

#### THE FIRST PREMISE GOVERNING THE PROCESS:

The guiding principle is that the Government "wants out" of the business of micro-managing the economy without stepping away from its role in guiding and regulating the economy.

The Government's objective is the rapid transfer of managerial and technological skills to Hungarian enterprises. A well structured and fair transaction for the enterprise and the owner (the people of Hungary) is the principal prerequisite for any transaction. Domestic and foreign private investment that makes sense is encouraged. If a transaction is structured as a majority foreign joint venture, a lease transaction, a management contract, the same common sense rules will be brought to bear.

Hungary is management, capital, and technology short. Is Hungary welcoming proposals that solve these problems? Most certainly.

#### THE PROCESS HAS BEGUN:

The Hungarian Parliament has laid the foundations for the emergence of a well founded private sector. The 1988 Economic Associations (Company Act.), and the Foreign Investments Act set the direction. The 1989 Transformation act provided the legal framework for converting state enterprises into corporate form and the 1990 Law on the Protection of State Property and

the Law on the State Property Agency provided the basic regulatory framework within which the process will be conducted.

.Encouraged by this, many individual companies, joint-ventures (domestic and foreign) have been formed and are underway. The process of "spontaneous privatization" arising as state owned units undertake to move toward the opportunities presented by privatization is a unique and encouraging feature of the Hungarian economic landscape. As at this point about 150 enterprises have been spontaneously privatized throughout Hungary and we expect and encourage this number to grow. None the less it is a feature that has its problems as well as its favorable side.

Most concretely on 14 September, 1990 the SPA formally launched its first 20 companies into the active government led privatization process in its First Privatization Program(FPP). We emphasize the "process" concept as the intent is that the orderly and transparent process that is being initiated in the FPP will, with some variations, be an outstanding feature of the program in this and anticipated future launches. We estimate that the SPA will have similar launches of new enterprises into the privatization arena every 3-4 months

### THE WORK TO BE DONE:

It must be kept in mind Hungary's privatization program is a program of scale. Since its inception on 1 March, 1990 the SPA has become actively involved in over 50 transactions and a reviewer of many more. To indicate the scale of our task there are close to 400 large enterprises in the state sector. They together account for about 78% of industrial employment, 88.6% of fixed capital and 83.5% of industrial sales. For this purpose we note that the total state sector involves about 2,800 firms excluding the cooperatives and enterprises already operating in Rt or Kft form. Given these significant numbers, to achieve its objectives the SPA needs to get impact from each transaction it becomes involved in as a stimulant, guide, and multiplier for others.

In the initial 18 month phase of Hungary's formal privatization efforts, 100-150 state owned enterprises initially valued at 80-120 billion Forints (US\$ 1.3-1.9 billion) will be privatized or well launched in that direction. Follow-up phases will bring equivalent groups of state owned enterprises to market. Much of this initial process will be significantly driven by foreign investment as foreign management techniques, technical skills, and capital are a necessary stimulus and model for the economy.

The longer term privatization process, which will be driven principally by Hungarian owners and managers, will easily span the decade. This later phase will have more significance as it will signal the training of a new generation of Hungarian managers and -more critically- entrepreneurs and the emergence of Hungarian money and capital markets.

What are the areas that Hungary's privatization process will only selectively and slowly effect?

-Agriculture: Much of Hungary's agriculture works. The activities of the cooperatives, as in many nations, have significantly decentralized this activity already. One doesn't upset a modest success particularly when it feeds you. Compound this with the land title issue and it is a problem whose solution has yet to come.

-Real Estate: The urge to own and speculate in real estate is alive and well in Hungary. The issues of land title and ownership are closely entwined with the history of Hungary. The SPA's privatization efforts will not cast themselves early on these shoals with so much clearer sailing elsewhere.

### **THE SPA - KEEPING THE FIELD LEVEL AND THE RULES CLEAR:**

Parliament has established the State Property Agency (SPA) to regulate and stimulate the privatization process. The SPA's existence reflects a realization that in the absence of the market practices and regulations that have developed over decades in other nations, Hungary requires a combination coach and referee to guide its privatization effort.

The activities of the SPA are not capitalism they are not socialism they represent pragmatism. The SPA will not be a purist, it will do what can be done. The SPA does not have its own vested interests except those defined by Government and the parliament.

The SPA's principal objective is to help stimulate the development of a strong competitive free market economy through Hungary's privatization program. The SPA accepts this responsibility in the anticipation of the constructive opportunities this creative process will develop.

The State Property Agency (SPA) was officially empowered on 1 March 1990. The SPA responds directly to Government through its Government appointed Managing Director and Board. Its mandate is to promote, assist, and regulate the orderly privatization of Hungary's state owned and operated enterprises. The SPA is the first modern regulatory agency in Hungary. It needs to regulate the privatization process without stifling it and encourage privatization while preventing abuse and inappropriate market structures.

The SPA intends to stimulate and support the Hungarian privatization process in concrete ways:

- *1. The SPA will clarify and unify the Government's policy guidance on privatization and translate that into regulatory guidelines to be made available to all participants.*
- *2. The SPA will publish and disseminate its regulations, guidelines, experience, standardized procedures, sample transaction documentation and other materials and in all ways seek to demystify and make broadly accessible the process of privatization in Hungary.*
- *3. Leading by example the SPA will engage in privatizations across a spectrum of enterprises in a variety of ways helping clear the way for others.*

- *4.The SPA will, as it accrues experience, become an excellent source of practical knowledge on privatization in Hungary. That knowledge will be freely available.*
- *5.Selectively the SPA will commit direct financial support to provide expertise to support individual transactions. Forinstance The EC's PHARE program has committed ECU 5 million principally as seed money to pay for the Merchant Banking, Valuation, and legal expertise the privatization effort requires to be professional and successful. Financial support form the World Bank, UNIDO, the U.S. British, Japanese, and Canadian sources have been made available as well.*
- *6.The SPA will help stimulate and coordinate the human side of the process; retraining, ownership distribution, workers concerns, investor personnel policies.*

### **RESPONSIBILITY AND REPRESENTING THE SELLER:**

Privatization in Hungary will be significantly decentralized though centrally regulated. It is essential to state that the SPA will expect and enforce the expectation that in the process of privatization, that the SPA or other party taking the lead in privatizing an enterprise, represents the interests of the seller, the people of Hungary. This is a position of trust that is not to be taken lightly.

### **THE SPA AND PRIVATIZATION HAVE LIMITS:**

The activities of the SPA are inextricably intertwined with and dependent upon initiatives in several areas of Hungarian social and economic life. Many of these changes are more far reaching and have more significant implications than the process of privatization.

The SPA's principal role in the privatization process in Hungary will be as a referee and model. It must be the guardian of the process. It will be working for, with, and alongside others in most cases, as they help structure the most reasonable enterprise specific answer that addresses the appropriate privatization concerns of each case.

This model can be clearly seen in the FPP announcement. The first announcement is in fact a call for advisers on the way to accomplish the privatization process on a case by case basis.

However, certain privatization process principals cannot be breached, they are transparency and independent third party valuations. Everyone who becomes involved in the privatization process is assuming a significant public responsibility and it is the goal of the process that those involved must be accountable to clear standards.

In short the SPA can only succeed in the context of a broadly successful Hungary. The SPA and privatization alone will not be the platform upon which a successful Hungary will stand, they will only be strong supports. The SPA must play a vital professional role within the area of its responsibilities.



## THE STARTING POINT:

The starting point is that there is no expert in the world on privatization in Hungary. Hungary will develop that expertise. The SPA has the responsibility to take the lead.

While Hungary must define the answers to its problems, Hungary's privatization process will benefit dramatically from being able to selectively draw upon the experience of others.

Hungary is not alone, the SPA is not alone and the privatization process in Hungary is not alone. The activities of the SPA have been and are supported financially and technically by - among others- the World Bank, the United States Agency for International Development, the United Kingdom's Know How Fund, the Economic Community under its PHARE program, and the United Nations Industrial Development Office.

The SPA has already benefited from and will continue to utilize the expertise of foreign technicians and advisers from around the world. The US, UK, EC, and Canadians have all provided or have undertaken to provide specialized skilled staff personnel to work within the SPA to help it get established.

## PRIVATIZATION:

It is a deeply committed belief that a regulated free market economy will make more efficient use of the assets in the economy than a government. Several unfortunate decades of experience with Government management have led to this conclusion.

As the SPA gets underway it is vital to understand that privatization is not an answer, it is a transition process. The benefits of a properly functioning market economy are the objective. The process should not be mistaken for the end result. Privatization is a one time opportunity to use a pool of assets under government control to stimulate a responsible marketplace. A marketplace where individuals are encouraged as they strive to exercise responsible economic choices to manage the assets available to the the economy.

It is the SPA's responsibility to help guide this process so that the benefits of a balanced and competitive free market economy are realized. Too rapid or too slow a pace can damage the process and make reaching the objective more difficult.

There is no special mystique to Hungary's privatization for a potential investor foreign or domestic. The systematic search for a good business opportunity, a careful review of the present legal and regulatory structure, and thoughtful and meticulous follow-up and follow through are the proven formula. Any investor must realize that Hungary is in a process of creative change, the rules will not always be clear but the opportunities will be present. The SPA and its needs are one of the areas to be addressed by a serious investor just as the tax regulations, foreign investment laws, and labor practices must be scrutinized.

The SPA will be making available very shortly a detailed outline of its policies and practices so that the SPA will no longer be an unknown player. The SPA's policy is transparency and openness but the administrative lead time to put together well thought out and fully reviewed guidelines has created a necessary but frustrating delay in the interim. It is hoped that the SPA's increasing experience and accessibility will be another feature that will make the SPA and Hungarian privatization "investor friendly".

### WHERE THE SPA FITS IN:

The role of the SPA in the privatization process is as a catalyst and guide not principally as an executing agency. Its role is to help match needs with resources, skills with requirements. It is prepared to regulate the privatization process in appropriate cases, inform the participants in all cases, and directly assist participants in others -financially and with advice-. It should be consulted early and often depending on the circumstances.

The goals of the SPA can be fairly simply stated, they are;

- *1. That the SPA will establish the parameters of privatization in Hungary.*
- *2. That the SPA will serve the process of privatization by making information, expertise and policy sponsorship available.*
- *3. That the SPA will do its best to assure that the transfer of the assets of the people of Hungary from the Government to the private sector is accomplished in accord with the fairest principals and in accord with the appropriate professional market practices.*
- *4. That the SPA will stimulate the inclusion of fair principals and professional practices into the way business is done in Hungary.*
- *5. That the SPA will be measured by its performance in privatization transactions imaginatively done, market mechanisms stimulated, managers identified and trained, and not paperwork generated.*
- *6. That the SPA's privatization function is to be self eliminating. The SPA's purpose is to undertake a specific series of sales. These sales will put assets fairly into play in the market. The benefits of the market are what Hungary desires, not another lingering bureaucracy.*

### WHAT WILL BE THE LEGACY OF THE SPA:

While the goals of the SPA can be simply stated, what it would hope to achieve over the long run is significant.

- *-It will take a lead in stimulating the growth of Hungary's stock market and the listing of Hungarian shares in the markets of other countries and the listing of foreign shares in Hungary.*

- *-The SPA will take a lead in stimulating and developing the financial infrastructure of Hungary; bankers, brokers, unit trusts, accountants, credit services, and the whole range of possible institutional investors.*
- *-The SPA will make imaginative solutions to suitable capital investment needs commonplace; domestic and international debt-equity conversions, employee share ownership plans, offshore Hungary funds, foreign multilateral agency investments.*
- *-The SPA will stimulate and in all ways encourage the development of Hungarian entrepreneurs and managers.*

Thus the assets that the SPA oversee will see service in more than one way. They are not simply items with price tags, they are part of a means to an end.

### **THE TOOLS:**

While there is no such thing as an expert on privatization in Hungary, Hungarians -with the support of the SPA- will become the experts, and to become expert they will initially use and modify tools developed elsewhere.

#### **These tools include:**

- *1. Transparency: The SPA has a position of trust. It is publicly accountable for its actions. Its activities will be designed to be scrutinized.*
- *2. Technical advisers: The SPA will use and be heavily dependent upon the experience of others -Hungarian and international- to help craft the right answers for Hungary. The skill of valuers, merchant bankers and the legal profession come immediately to mind.*
- *3. Training: The SPA must take the initiative to identify areas where its activities should serve as a catalyst to market development and take every effort to try to encourage the delivery of the requisite skills. Properly done its activities should add dramatic stimulus to the initiation and expansion of market activity.*
- *4. Responsiveness: The SPA is a creation of the Hungarian Parliament. The SPA will at all times be, through the Government, responsive to the needs of the Hungarian people.*

### **TRANSPARENCY:**

The necessity for transparency and accountability requires further expansion. It is critically important that the SPA is directly responsible to parliament for the actions it undertakes with the assets of the people of Hungary. This is all the more important in an environment where the bodies in authority have historically not been subject to query much less accountability. The agency will demand of itself and the process it oversees that all activities meet the

highest standards. As it is the agent of the people of Hungary it must be prepared to detail its actions and the reasons therefore to the people, be it through the Office of the State Auditor, Parliament or a court of law.

It is critical to note that the SPA will demand these same transparency standards of managers and other participants in the privatization process and will be pleased to underline the importance of this concept to the individuals concerned in the courts or other appropriate ways.

The SPA's standards of transparency will be modeled on those ascribed to by the international donor community. Their tendering procedures for services, their record keeping, and their reporting will adhere to these same or higher standards.

### THE ROLE OF PRICE:

Price is where a transaction has reality and as the SPA is a transaction driven organization its concept of "price" bears examination. The SPA expects that the sale price for any specific sale will be too high for some observers and too low for others. The SPA however will rely on a professional, transparent independent third party process to try to arrive at what a reasonable market or sale price will be for any transaction.

While the mechanics can be defined, it is clear that the process of privatization is not simply a price competition. Privatization as a process in the Hungarian circumstance must have substantial subjective evaluations brought to bear as well. It is appropriate to note that no marketplace or individual is driven solely by price determinants so there is no reason for Hungary to expect to do otherwise. That the SPA is responsive to Parliament is not happenstance, it reflects this reality.

The SPA is very aware that a closed factory that employs no one and manufactures nothing is of less value to Hungary than an enterprise that employs people and produces a salable product that can be sold profitably. Part of any pricing determination are the alternatives; not selling because of objective price determinants when heavily subsidized operation or closure are the alternatives, are real world considerations.

In short we reiterate, privatization is a process. The benefits of a well balanced competitive marketplace is the objective. The proposed price on any given sale may or may not give the right answer for who is an appropriate buyer.

However in the cases where objective criteria, for instance price, do not establish a clear reason for a sale, the need for transparency and precise and specific reasons for a specific transaction decisions plus support by appropriate policy guidance becomes all the more critical.

### THE MECHANICS:

- *-Broadly targeted active privatization program*

The SPA will be broadly targeting its activities rather than narrowly. It will be establishing the legal and conceptual way for a wide spectrum of privatization methods. In addition it will take the lead across the broad spectrum of industries and enterprises. While each enterprise's circumstances are unique and the answers case specific, pioneering efforts in public issues (as in the just accomplished IBUSZ transaction), appropriate use of management and employee participation in transactions, management contracts and leases will all be tools that will be considered for development. This approach is designed to maximize the programs impact:

- *-The market needs working examples of several alternatives*
- *-The market needs to see that the privatization effort includes the whole range of economic activity*
- *-privatized pockets in quiet government sectors can be expected to stimulate change*
- *-Reliance on specialist talents*

Selling companies is a highly detailed process. Practices have developed in other marketplaces that reflect the reality of the process. The first principal is that each transaction is unique. The second principal is that an operating entity's management is rarely properly trained or equipped to undertake what is an unusual activity for any organization. A technical manager with liquidity problems is not the best strategic analyst of a sale!

As a rule of thumb it is to be assumed to protect the owner that each transaction requires a financial specialist, a valuation specialist, and legal assistance. In the case of Hungary the interests of the owner's of the assets, the people of Hungary and their representative the SPA, must be brought to the transaction early.

While the precise definition of the activities of financial advisor to a transaction is difficult, and the role of a legal adviser may appear clear cut, the responsibility for assuring that a proper third party valuation be done is the legislated mandate of the SPA. Thus it is important to outline the SPA's thoughts on this topic in more detail.

### **THE VALUER:**

Having cautiously highlighted the appropriate use of the tool of price we can detail how the SPA must systematically go about deriving it in all circumstances. In most privatization circumstances the owner, the people of Hungary and their representative the SPA, want to know what is the fair market value on an operating company basis of the operation being privatized.

This critical "price" which the SPA as seller will use to make its judgement, as would be expected of any responsible seller, is a fair market price established by an appropriate independent third party valuer.

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The SPA realizes that valuation, particularly in the current circumstances in Hungary, is more of an art than a science. This said, the SPA in its role of registering valuers, will work with the valuation industry professionals to establish demanding but reasonable guidelines for the purposes of the privatization process.

The SPA plans to prequalify and register firms and individuals, domestic and foreign, who wish to provide valuation services in Hungary. The SPA is preparing detailed specifications for what it requires in valuations done for privatizations that it will review.

Most critically the valuers are being put on notice that their valuation, in the circumstances of a privatization being reviewed or undertaken by the SPA, are for the owner -the people of Hungary and its representative the SPA- not the manager, buyer or another party.

Only the most qualified of firms will be able to undertake the large and complex valuations. Medium sized transactions will have less stringent criteria, and the smaller transactions will require even less specialized skills.

The criteria that valuers must meet and the list of valuers prequalified to undertake valuations of transactions of a given size will all be made available to the marketplace.

Ultimately of course in the absence of a broad and deep market the answer to the value and price question will be imprecise. The "market" price will actually be established for any asset by what it is sold for, not by any hypothetical analysis no matter how well intentioned.

### **THE PACE:**

What the SPA will be doing will be pragmatic and systematic and it is clear that the requirement for an ambitious program means there cannot be painstaking maximization of each transaction. Hungary's economic revitalization can't await that. The reality of the market mechanism is that it provides what is a reasonable answer for what is perceived as appropriate at a point in time. The final and maximal answer may never be achieved. The roots of the SPA are the need for a market surrogate who sees to it that the seller's interests and the interests of the marketplace are served. However the SPA, like the market, is transaction driven, it is not an academic exercise.

### **WHO INITIATES THE PROCESS:**

While the SPA will be taking the lead in many cases and playing a strong role in others the initiative often must lie elsewhere. There are buyers and sellers in the marketplace. Either or both can initiate privatization discussions. It is dramatically important to individual Hungarian enterprises that rapid consideration be given to how to make their operations competitive.

Hungary is trying to rapidly restructure its economy to be able to compete in a free market place. It is estimated that at present over 80% of Hungarian business would not be able to compete as they are presently constituted and they are not presently operating profitably.

The choices they face are liquidation, restructuring, and privatizing,

- *-Liquidation is unattractive to the enterprises managers and workers as well as the state as owner. It may be necessary in some cases.*
- *-There is not enough money and management skill in Hungary to successfully externally restructure even a significant portion of the productive sector in Hungary.*
- *-The option of turning to the private sector for management, financial and other inputs to make the operation viable is the route most likely to yield success.*

The enterprises, the workforce, managers, suppliers, customers, or bankers are going to have to initiate and follow through on the privatization process. The SPA can help, technical assistance will be required, but the initiative and responsibility will substantially lie with those most intimately involved with the enterprise itself.

### **THE PEOPLE:**

As a final note we should state what the SPA really is. The SPA is people. Young professionals selected from various parts of Hungarian society who will be expected to learn how to execute a complex and demanding task. They will be training and learning. The SPA's people will be striving for reasonable, responsible answers. Reality does not await the perfect answer. The SPA can be expected to make mistakes but its mistakes will be honest mistakes and will contribute to it and Hungary's learning process. The agency will be small, its task large and its approach common sense.

State Property Agency

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SUGGESTED APRIL ACTION ITEMS  
Draft - 29 March, 1990

STATE PROPERTY AGENCY

BACKGROUND: The State Property Agency (SPA) has been formally established with effect from 1 March, 1990 and the Managing Director (MD) has been named. The Board of the SPA is to be nominated following the elections. Certain core staff have been identified. The SPA has a requirement to become functional immediately.

CURRENT SITUATION: The formation phase of the SPA is now underway. It must simultaneously think through the most professional way to accomplish its assigned tasks in the rapidly evolving circumstances in Hungary and begin to accomplish them.

RECOMMENDATION: During the initial period several tasks must be undertaken. These basic efforts will be revisited and refined often in coming months.

The importance of establishing the basic operating direction of the SPA quickly and clearly in its leaderships' minds cannot be overemphasized.

The core of the SPA's privatization process design and practice should be thought through before the Board is named. This should include organization, procedures, staffing, process principles and operating guidelines. In addition the budgetary realities should have been addressed. A basic action plan should be ready for presentation to the board with problem areas identified.

BASIC TASKS: The key things to be accomplished in the initial period are:

1. Establish basic operating principals and objectives.
2. Define organizational form
3. Define personnel needs and career strategies
4. Assign basic responsibilities.
5. Build a team
6. Define short and long term training needs
7. Establish a funding strategy
8. Detail initial office and equipment needs
9. Establish working relationships in the community
10. Define and initiate control/management procedures
11. Start building a constituency
12. Start informing the market
13. Compile basic company lists

Each of the above must evolve and further define themselves.



SPECIFIC ACTIONS: Certain events must be planned and their outputs integrated into the SPA building process as quickly as possible:

-- I Strategic Planning/Team Building

I hope time can be made for a 2-3 day strategic planning and goal setting session incorporating the core staff and initiators of the SPA. This might be repeated quarterly in the first year of operation and semiannually thereafter.

The meeting should be at an isolated location.

The meeting should be carefully planned.

The meeting can be organized externally but most critically for the strategic planning part of the meeting, a professional implementer should be employed to assure a dialogue and a continued focus to the discussions.

The Meeting output should derive by consensus:

- a. A mission statement
- b. An organization chart
- c. A financing strategy
- d. A recruiting strategy
- e. A training strategy
- f. A vision of long term objectives
- g. A networking strategy - allies/opponents
- h. An agreement on professional ethics
- i. An agreement on control and reporting guidelines

Which of these activities would be treated as a committee of the whole or with sub-committees bringing their work back for discussion would be decided.

Specific urgent training subjects can be incorporated in this initial and subsequent meetings. The following is recommended for the initial meeting:

1. A discussion of the SPA's legal foundation and responsibilities.
2. A discussion of the principals underlying the art of corporate valuations
3. A discussion of privatization experience elsewhere

-- II Immediate needs:

a. Define office and basic furnishing needs for the start-up period. The critical things to consider include: adjoining workspace, communications, and business center access.

b. Define office equipping needs in detail. The basic need is for a computerized, communications-heavy office.

c. Very thoughtfully Define initial staffing requirements and begin recruiting and transferring people into the organization.

d. Follow-up on funding issues to get the equipment paid for as well as the massive amounts of TA services that are going to be required. The lead time problem is already upon us.

e. Design logo, letterhead, business cards, tee shirts, organize football team?

-- III Initial Training/Getting operational/interactive consultancy

FIRST PRINCIPLES

THERE ARE NO EXPERTS ON THE PRIVATIZATION PROCESS IN HUNGARY, THE SPA IS GOING TO DEVELOP THAT EXPERTISE.

THERE ARE EXPERT SKILLS AVAILABLE FOR SOME OF THE PREDICTABLE COMPONENTS OF THE PRIVATIZATION PROCESS, THE SPA WILL USE THAT SKILL AND STIMULATE ITS DEVELOPMENT.

The SPA team will be given very capable hands on training to help guide them through the initial phase of their setup. The concept is that the Agency cannot await the results of a gradual academic training process nor can it afford an 18 month trial and error OJT training period, it must get itself immediately professionally functional and in place.

A team to provide the skills to help the SPA quickly think through and define the details of its operational setup has been identified. It is critical that the SPA staff interact with the specialists. The specialist consultants will have a responsibility to be sure their SPA counterparts are comfortable with the systems that are being put in place.

-- IV Communications/Networking

FIRST PRINCIPLE

THE SPA IS PRINCIPALLY A CATALYST AND A RESOURCE. IT CAN STIMULATE AND GUIDE THE PRIVATIZATION PROCESS, IT CANNOT UNDERTAKE IT ALONE.

The constituencies the SPA must develop and cultivate would include but not be limited to the following:

- Ministry of Finance
- National Bank of Hungary
- National Planning Office
- Ministry of Justice
- Ministry of Labor
- Ministry of Trade
- Local Councils
- Tax department
- Customs
- The Bankers Assn.
- The Accountancy Assn.
- The individual banks
- The individual accounting firms
- The Legal profession and its organizations
- The Chambers of Commerce
- The Donor agencies
- The economic and business sections of foreign embassies
- The stock exchange
- Regional Hungarian promotion organizations
- The financial press
- The Academic institutions

The SPA must develop a public information and transparency campaign with all the staff being prepared to contribute. Hungary must know who to call on privatization matters and the SPA should be prepared to provide guidance, if nothing more than as a clearing center.

MEMORANDUM: The Bidding Process and the results thereof as regards the bid for consulting services to assist in the establishment and initial organization of the State Property Agency of Hungary

DATE: 2 April, 1990

TO: Managing Director, The State Property Agency

FROM: Charles G. Twyman, Financial Consultant, Deloitte & Touche

BACKGROUND: You have requested that I prepare in English a summary of the bidding, bid review and negotiation procedure carried out by the State Property Agency (SPA) in its just concluded initial direct bid for a package of consultancy services to assist in the establishment of the SPA.

CURRENT SITUATION: The following is the final result of the bidding process.

FINAL RANKING OF THE TOP BIDS

Rank	Firm	Professional Eval.	Price/Quality Formula Eval.
1.	Barclays	87 points	85.56
2.	Rothschild	80 points	84.00
3.	Schroders	79 points	76.57

PROCESS: I detail in Phases I - II below the precise bid process that was applied in the case of this bid with the related calculation substantiating the final results.

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PHASE I Bid Preparations

-Procedure chosen

The Officials of the SPA made a policy decision that their tendering process for consultancy services would closely parallel that established by the World Bank (WB). The objective of the process chosen was to establish a procedure which incorporates a standard with worldwide acceptance in terms of professional requirements for the bidders, and a high degree of transparency for all concerned.

-Firms shortlisted

In the interest of time the Officials of the SPA prepared a shortlist of firms with the required international level of professional privatization skills and a demonstrated interest in Hungary. That list was incorporated into the bid letter sent to all potential bidders. (A copy of the bid letter and the three related attachments is appended to this memorandum)

-Terms of Reference defined

In consultation with the World Bank (WB) the senior officials of the SPA designed a Terms of Reference for Consulting Services (TOR) which was forwarded to all the prospective bidders.

-Bid documents prepared

The identical Cover Letter, TOR (attachment 1), bid instruction (attachment 2), and the procedure for Evaluation of Bids (attachment 3), was forwarded to each of the short-listed firms.

-Bid documents forwarded

The documents were forwarded to the shortlist on 20 February, 1990. Nine responses were received from ten bidders, eight affirming their receipt of the documents and their intention to bid, one declined to bid, and one bidder combined with one of the other bidders.

PHASE II Bid Evaluation

-Bid documents submitted

The deadline of bid submission was announced in the bid documentation as being Monday, 5 March, 1990. All of the bids to be evaluated were received by the deadline date.

-Evaluation of Bids

As noted in the bid documentation the bids were reviewed by a SPA team and by the State Commissioner on Privatization. The team and Commissioner prepared a consensus ranking of the bids according to the criteria outlined in the bid documents.

Second Opinion: Given the need for subjective judgements on several issues the team asked that the undersigned conduct an independent desktop review of all the proposals, and to opine -without knowing the results of the SPA's consultation- as to the merits of the various proposals. It is well worth noting that the ranking of the proposals by the SPA and the undersigned for the top ranked contenders was the same.

Overall note: The skill requirements specified in the bid documents were of such a broad nature that the most responsive bidders uniformly chose to respond with teaming partners. All chose their partners well to complement their in-house capabilities. The team bids are noted with an @ symbol on the chart. The teams who bid are as follows:

From the original shortlist -

Morgan Grenfell and Coopers & Lybrand made a combined bid

Team bids were -

Morgan Grenfell & Co. Ltd, teamed with Coopers & Lybrand and Deloitte

Barclays de Zoete teamed with Price Waterhouse, and Baker & McKenzie

Schroders teamed with Arthur D. Little and Creditanstalt

Banque Rothschild teamed with Kereskedelmi Bank and KPMG. After the first round review gave Banque Rothschild a better position than NM Rothschild, the London house joined with the French.

EVALUATION OF BIDS

(a) Professional evaluation

	1 wt 30	2 wt 15	3 wt 25	4 wt 30	TOTAL	Rank
Salomon Bros	0	0	0	0	0	nil
Shearson Lehman	0	0	0	0	0	nil
Credit Suisse 1st.Bos.	15	8	15	10	48	6
Credit Comm. Fr.	0	0	0	0	0	nil
Morgan Grenfell	25	12	15	22	74	4
Coopers & Lybrand	25	12	15	22	74	4
Barclays e	26	16	20	25	87	1
Schroders e	28	13	18	20	79	3
NM Rothschild	15	10	15	15	55	5
Banque Rothschild e	25	15	15	25	80	2

Criteria

	<u>Weight</u>
1. Bidder's recent experience in privatization issues and techniques	30
2. General approach to the problem and methodological standards, the up-to-dateness of the methods used.	15
3. Qualifications and the experiences of team members, with special regard to the team leader.	25
4. Quality of information available to the bidder and its team members about existing Hungarian legal and regulatory framework, accounting and financial system, enterprise structures, property valuation and the related problems and constraints.	30

100

e indicates a team bid

### STATISTICAL SUMMARY

Declined to bid or bid non responsively	3
Responsive bids	6*
Highest standard	4
Less well done	2

\* While 10 firms were approached and as two chose to combine, the final total number of nominated bidders became 9

### COMMENTS

- Salomon Brothers International Limited:  
Non responsive bid
- Shearson Lehman Hutton  
Non responsive bid
- Credit Suisse first Boston Limited  
Excellent name, fair team, weak Hungarian experience, fair understanding of the problem
- Credit Commercial de France  
Declined to bid
- Morgan Grenfell/Coopers & Lybrand  
Excellent name, good team, some Hungarian experience, good understanding of the problem
- Barclays de Zoete Wedd Limited  
Combined team names excellent, excellent team, excellent Hungarian experience, excellent understanding of the problem
- Schroders  
Excellent name, very good team, good Hungarian experience, very good understanding of the problem
- N. M. Rothschild & Sons Limited  
Very good name, modest team, limited Hungarian experience, limited understanding of the problem
- Banque Rothschild  
Excellent name, very good team, excellent Hungarian experience, excellent understanding of the problem

### SUMMARY OF TEAM IMPRESSION

At the end of the initial review it was the sense of the review team and the independent consultant that any of the four top bidders would be able to do an acceptable job.



### RANKING OF TOP BIDS

1. Barclays 87 points
2. Banque Rothschild 80 points
3. Schroder 79 points
4. Morgan Grenfell 74 points

10% of number 1 bid (Barclays - 87 points) is 8.7  
thus only 1, 2, and 3 by formula would go to a price  
comparison

### INTERVIEW PHASE

Based on the high quality of the four top bidders and the requirement that this consultancy effort work interactively with the still-forming SPA team, the core team members felt to make the critical relationship judgement that a presentation and discussion with the top bidders would be of great value. The bidders agreed to adding this step to the decision making process.

The presentation/interview phase confirmed that the top three bidders could all work well with the SPA team. It was felt however that the Barclays's group due to its very strong on the ground presence would offer a substantial advantage in terms of interactive support for this very much hands on and execution oriented consultancy.

### FINANCIAL EVALUATION

In accord with the terms of the bid document, as the three top bidders were within 10% of each other in their professional evaluation, their bid prices were examined. Their price bids can be summarized as follows:

Rank*	Firm	Level of effort	Proposed Fee	Fee Per day
1.	Barclays	230 days	US\$398,000	US\$1730.43
2.	Rothschild	315 days	US\$435,000	US\$1380.95
3.	Schroders	300 days	US\$619,320	US\$2066.40

\* Rank is in order of ranking in the professional evaluation category

#### Level of effort:

##### -Basic Bid

All three bids envisioned doing the core of the work over a period of about 90 days with various deliverables and reviews during that period.

##### -Incomparability of proposed levels of effort

The Schroders and Rothschilds bids both envisioned more detailed continued strategy and valuation work on individual firms with the effect that their levels of effort numbers were expanded. As the imprecision of the TOR contributed significantly to this variance it was not felt that this was a valid number for comparison sake.

Proposed Fee:

As the levels of effort were not directly comparable the proposed total fee numbers were not directly comparable.

Fee per day:

While the level of effort was not broken down in the same detail by person and task in each of the proposals, the absolute comparability of the bids does not exist but as a yardstick this number is the most effective comparative number.

Application of Bid Formula:

Step 1

- |               |  |         |
|---------------|--|---------|
| 1. Barclays   | $\frac{(1380.95)}{(1730.43)} \times 100$ | = 79.80 |
| 2. Rothschild | 1380.95 is the lowest bid                | = 100   |
| 3. Schroders  | $\frac{(1380.95)}{(2066.40)} \times 100$ | = 66.83 |

Step 2

- |               |                                       |         |
|---------------|---------------------------------------|---------|
| 1. Barclays   | $(.8 \times 87) + (.2 \times 79.80)$  | = 85.56 |
| 2. Rothschild | $(.8 \times 80) + (.2 \times 100,00)$ | = 84    |
| 3. Schroder   | $(.8 \times 79) + (.2 \times 66.83)$  | = 76.57 |

Bid Analysis:

In this instance applying the formula in the bid documents, the bids ranked in order of price is the same as the ranking derived by the bid ranking done on the basis of the professional evaluation.

PHASE III Final Negotiations

The TOR for the contract was further defined in contract discussions and the terms of the contract were finalized.

The Barclays team agreed to undertake the Terms of Reference as mutually defined for a total price of US\$300,000 (before direct expense) for a level of effort of 210 days expandable to 240 days at no extra cost. The direct expenses are to be submitted at a separate meeting and agreed on as well, the estimate is in the US\$50,000 - US\$75,000 range.

Thus the average per diem cost for the consultants is US\$1429 - US\$1250. It is felt that this is a fair market rate for the level of skills being committed. This hourly rate range of US\$178.63 to US\$156.25 compares most favorably to standard commercial pricing.

FINAL RANKING OF THE TOP BIDS

Rank	Firm	Professional Eval.	Formula Eval.	Fee Per day
1.	Barclays	87 points	85.56	US\$1250.00*
2.	Rothschild	80 points	84.00	US\$1380.95**
3.	Schroders	79 points	76.57	US\$2066.44**

\* Final

\*\* Bid level

MEMORANDUM

TO :Managing Director, Dr. Csepi Lajos  
Deputy Managing Director, Szabo Karoly  
FROM :Advisor, Twyman Charles  
DATE :27 February, 1991  
REF :Provision of Long Term Advisors

BACKGROUND:

We are sourcing long term advisors from various funders. This involves a lengthy lead time during which the needs are defined, the individuals are identified, passed to us for selection, and put in place.

CURRENT SITUATION:

In order to clarify for all of our supporting donors the SPA's present position on long term advisors and our anticipated sourcing I would like to have you confirm the present situation so that it can be uniformly communicated to the various donors.

REQUEST:

Please Review the following list to see if it is in accord with your understanding and can be communicated (as appropriate) to the donors:

<u>Individual</u>	<u>Assignment</u>	<u>Contract length</u>	<u>Funder</u>
<u>Current</u>			
C. Twyman	Finance and Policy advisor, MD, DMD	1 year, extension requested	USAID
T. Karc	EC PHARE Financial Administrator	18 months, extendable	EC PHARE
L. Davies	Active Privatization	2 years	UK Know How
F. Faiz	Active Privatizaion	2 years	UK Know How
G. Hollo	Public Affairs	1 year renewable	Canada
T. Varosi	Computer Technician	65 work days	USAID
E. Szeman	Computer Trainer	85 work days	USAID
<u>Proposed</u>			
Unknown	EC Financial Admin. Hungarian Support Staff	18 months	EC PHARE
Unknown	EC Financial Admin Hungarian Support Staff	18 months	EC PHARE
Unknown	Computer Unit Hungarian programming support	6 months	USAID
Unknown	Active Privatization legal advisor	2 year	UK Know How
Unknown	Legal Department	unknown	French

Unknown firm	Legal Department on retainer	1 year (?)	EC PHARE
Unknown firm	Legal Department on retainer	1 year (?)	EC PHARE
Unknown firm	Active Privatization Industry specialists on retainer	1 year (?)	EC PHARE
Unknown firm	Active Privatization Industry specialists on retainer	1 year (?)	EC PHARE
Unknown	Spontaneous Privatization Financial advisor	2 year (?)	USAID
Unknown	Investor Driven Strong legal skills	2 year (?)	EC PHARE
Unknown	Asset Management Organization & Management skills	2 year (?)	EC PHARE

MEMORANDUM

TO :Managing Director, Dr. Csepi Lajos  
Deputy Managing Director, Szabo Karoly  
FROM :Advisor, Twyman Charles  
DATE :06 March, 1991  
REF :Provision of Long Term Advisors

BACKGROUND:

We are sourcing long term advisors from various funders. You reviewed a proposed sourcing and disposition list of those advisors.

CURRENT SITUATION:

You added your comments to the list I proposed that in the case of the legal advisory firms on retainer and the industry specialists on retainer that only one such firm was necessary.

ANALYSIS:

The DMD, the Director of the Active Privatization Unit and the Director of the legal department had suggested that the two firm approach was preferable.

1. The two firm approach is not more expensive
2. The two firm approach gives us a broader range of skilled individuals to chose from.
3. The two firm approach gives us a choice and injects an appropriate element of competition into the process of seeking advice on a specific transaction.
4. The two firm approach gives us more experience with a broader range of advisors.

It was my thought that you may not have known this background when you considered my memo. My apologies

REQUEST:

In light of the above analysis are you prepared to consider using the suggested two firm advisory approach or do you wish to adhere to your initial one firm approach?

Attachment: A copy of the original memo.

REQUEST:

Please Re

The State Property Agency of Hungary  
FOREIGN ADVISERS  
Actual and Proposed

<u>Individual</u>	<u>Assignment</u>	<u>Contract length</u>	<u>Funder</u>
<u>Current</u>			
C. Twyman	Finance and Policy advisor, MD, DMD	1 year, extendable	USAID
T. Karo	EC PHARE Financial Administrator	18 months, extendable	EC PHARE
L. Davies	Active Privatization	2 years	UK Know How
F. Faiz	Active Privatizaion	2 years	UK Know How
G. Hollo	Public Affairs	1 year extendable	Canada
T. Varsci	Computer Technician	As required	USAID
E. Szeman	Computer Trainer	As required	USAID
<u>Proposed</u>			
Unknown	EC Financial Admin. Hungarian Support Staff	18 months	EC PHARE
Unknown	EC Financial Admin Hungarian Support Staff	18 months	EC PHARE
Unknown(3 men)	EC Project Management	2 years	EC PHARE
Unknown	Computer Unit MIS	9 months	USAID
IDOM	Hungarian programming support	6 months	USAID
Unknown	Active Privatization legal advisor	2 year	UK Know How
Unknown	Legal Department	unknown	French
Unknown firm	Legal Department on retainer	1 year (?)	EC PHARE
Unknown firm	Legal Department on retainer	1 year (?)	EC PHARE
Unknown firm	Active Privatization Industry specialists on retainer	1 year (?)	EC PHARE
Unknown firm	Active Privatization Industry specialists on retainer	1 year (?)	EC PHARE

Unknown	Spontaneous Privatization 2 year (?) Financial advisor	USAID
Unknown	Investor Driven 2 year (?) Strong legal skills	EC PHARE
Unknown	Asset Management 2 year (?) Organization & Management skills	EC PHARE* A Canadian also maybe
Unknown	Financial Dir.'s Office 1 year (?)	US CDC
Total	15 Long term advisors the other advisory efforts have a corporate, short term presence, or are Hungarian sourced.	



MEMORANDUM

SUBJECT: The State Property Agency of Hungary  
Financing Strategy

DATE : 29 January, 1991

BACKGROUND:

Hungary's strategic economic objective is to increase the efficiency with which Hungary's productive assets are managed. Private sector ownership and management are the key to achieving that objective. To achieve this end in a rapid but orderly manner, the Government of Hungary has launched an ambitious privatization program. The objective of the program is to facilitate private sector investment in Hungary's productive assets at a pace that sees the Government's proportion of those assets decline to less than 50% in 3 to 5 years.

THE ROLE OF THE SPA:

The SPA was established in 1 March, 1990 with the objective of assisting the Government to stimulate, regulate, and implement the Government's privatization policy.

A MARKET DRIVEN PROCESS:

The market, buyers and sellers are what drive the privatization process. The success of Hungary's privatization program will depend on the ability of Hungary to facilitate appropriate investor interest. Hungary's ability to deal fairly and promptly with the broad range of investors they must attract will depend on their ability to commit the appropriate skills to individual transactions when and where needed.

HUNGARY IS SHORT OF PRACTICED BUSINESS SKILLS:

Hungary does not have in Government the business skills of the level required to carry this process through, nor should it try to develop them. Hungary's business infrastructure; investment houses, accounting firms, law firms, consultants, is not large enough to deal with the quantity or always at the skill level needed to achieve Hungary's objectives within the required time frame. The answer for Hungary and the SPA, as it is for any organization requiring a high level of specialized skills for a short time, is to purchase the required skills while making every effort to develop the necessary long term level of those skills available internally in Hungary.

PRIVATIZATION IS EXPENSIVE:

A successful major privatization which achieves the objective of attracting a competent owner/manager requires the commitment of time, effort, and money before a sale can be realized. The requisite investment advisory, accounting, legal and other skills required for a transaction cost between US\$150,000 - US\$500,000 per transaction.

Developing Hungary's business infrastructure, investment promotion program, training its managers and technicians in the required business sustaining skills, all cost money.

At the present time Hungary is not in the financial position to commit the required funding to support the full needs of its ambitious privatization program.

## SPA's FINANCING PROGRAM:

### Sources:

The SPA is principally reliant on the funding of donor and lending agencies to carry its portion of Hungary privatization forward successfully.

### Uses:

The SPA is funding or helping focus funding on three basic activities. Each of these activities have short range, medium term and long range components.

The basic activities requiring funding are

- I Internal operating costs: Consists of the office, staff and equipment costs of the SPA itself.
- II The cost of the technical skills required for individual transactions: Consists of the costs for the industry, financial, accounting, legal, and other skills necessary to close a sale professionally. Recoverable from the sale but a cash flow cost up front.
- III Institution building: Consists of the training, promotional, informational, and other efforts the privatization program needs to support its continuance.

### -Short range component:

- I Organize, equip, house, and train a staff to carry out the privatization program.
- II Establish the process that will enable the SPA for each privatization transaction it is involved in to identify the appropriate skills required, define their tasks establish appropriate cost guidelines, learn to manage them, initiate transactions.
- III Identify the necessary institutional and other support that the privatization process needs most critically, design the response, man and equip it, get it working.

### -Medium term component:

- I Train the staff anticipating turnover, commit training and skill to areas identified as the most critical.
- II Establish the transaction pace that the market and the SPA can sustain and, given the transaction portfolio's anticipated turnover, stabilize the funding level and advisory needs.
- III Continue to support institution building and training.

-Long term component:

- I Plan for a gradual decrease in the SPA's needs as the process slows helping transform the operation into what will probably be a regulatory core group rather than a transaction management organization.
- II Plan for the gradual decline in transaction volume and funding needs.
- III Continue to support the required institutions, wind others down, help design and implement the longer-term institutions.

FUNDING STRATEGY BY TYPE AND SOURCE:

Structure: The Hungarian privatization program has the good fortune of having access to multiple sources of financing. They can be used as circumstances dictates and in the most cost efficient manner for the Government of Hungary. The SPA has available budgetary support from the Government of Hungary, support from various sources for advisory assistance, and grant and loan support to meet the substantial costs of many initiatives that must be undertaken during the course of Hungary's privatization program.

Type/Source:

-I Operating expenses/Forint funding/Government of Hungary budget:

Hungary wants to be clearly in charge of and committed to the Privatization process. By assuming the responsibility for the basic staffing and office support it achieves both objectives. It must however expand the support of the areas for which it is responsible so that the required grant and loan funding are properly utilized.

-II In-House technical advisors/hard currency/offshore grant and loan funding:

The SPA and the privatization process in Hungary require significant inputs from technical advisors. However hiring and administering foreign technical advisors is a major task. The cost issues aside it is far preferable to have the administrative side handled elsewhere. The key issue is whether Hungary can get the skills they require if they must accept the constraints of the various national and multinational entities that offer such assistance. Hungary can get the benefits with a minimum of problems. The SPA has made satisfactory grant arrangements with: The United Kingdom -two long term advisers from the Know How Fund-, The United States Agency for International Development -one long term advisers and a range of short term technical advisory assistance-, Canada -one long term adviser-, France -one long term adviser has been discussed-, The EC Programme PHARE -a very flexible mix of firms on retainer, long term and short term advisors, the world bank has periodically offered assistance which, as it is loan funded, the SPA has declined.

-III Transaction and Policy related technical advisors/hard currency/offshore grant and loan funding:

The privatization processes largest single need is transaction related expertise; merchant bankers to structure deals and find buyers, accountants to help define what is being sold and value it, lawyers to help document sales plus industry and other specialists. These costs are principally hard currency denominated as the requisite skill levels are currently unavailable in Hungary in the required quantity. While these costs are frequently recoverable from sales proceeds the ongoing hard currency need to finance the program's transaction related technical advisers exceeds US\$ 55 million. Our major grant funding source in the regard is the EC project PHARE with the US Government possibly stepping up with grant funds, and the World Bank indicates a willingness to help with loan funds as an alternate source to supplement or bridge the SPA to its grant funding availability. The SPA is most clear that any loan funds should be spend on transactions where Hungary will recoup the fees paid for by the loan plus the related interest cost.

CURRENT LEVELS OF REQUIRED FUNDING BY PRINCIPLE SOURCE BY CATEGORY AMOUNT AND PERIOD:

I Internal Operating Costs:\*

<u>Source</u>	<u>Purpose</u>	<u>Need 1990/91</u>	<u>Need 1991/92</u>
-Government of Hungary	Staff costs, Opnl. costs & supplies	US\$ 3.29	US\$ 4.9
-EC Phare Program	Staff advisers Training Equipment	2.22	2.4
-USAID	Staff adviser Equipment, trng. Organization Assistance	1.35	4.1
-UK Know How Fund	Staff advisers	.5	.75
-Canadian Government	Staff adviser	.25	.25
-French Government	Staff Adviser	.25	.25
	Total	US\$ 4.32	US\$ 8.90

II The cost of Technical Skills required for individual transactions:\*

-World Bank	Technical Assistance	4.00	23.00
-EC PHARE Program	Technical Assistance	4.73	11.50*
-USAID	Technical Assistance	0	12.50
	Total	US\$ 8.73	US\$ 47.00

III Institution Building:\*

-EC PHARE Program	restructuring trust*** and others	0	41.29
-USAID			39.75
	Total	US\$	US\$ 81.04
TOTAL I, II, III		US\$ 13.05	US\$ 136.94

\* These budget numbers and the assumptions and projects underlying them and the rules governing them and their availability are different in each case. Critical discussions are currently underway with the EC, the US Government and the World Bank about the 1991/92 budget.

\*\* The EC Programme PHARE is the most flexible of the fund sources, the quickest disbursing and it is a grant. Thus it is intended as the principal funding source for the financing of the critical transaction related technical assistance costs. This large number assumes that the balance of the 1991/92 EC/PHARE moneys available in the privatization budget are used principally to support the Ministry of Trade and Industry and Ministry of Agriculture privatization transaction costs..

\*\*\* The privatization restructuring funds pool under discussion with the EC programme PHARE is a critical component of the privatization process which will make available to the seller the working capital needed to meet the surprise costs that may be blocking a sale for instance environmental cleanup, buying out of previously entered into unattractive licensing or sales agreements.

HUNGARY  
State Property Agency  
Government of Hungary operating Budget  
(91/92 preliminary)  
 (US\$ mil. by amounts proposed during period)  
 (Hungarian Forint 72 =s US\$ 1)

<u>I</u> <u>Internal Operating Costs</u>	1990/91		1991/92	
Wages	US\$ 1.92	Ft 137	US\$ 2.84	Ft 204
Social Security	.82	59	1.21	87
Operational Costs	.43	31	.64	46
Maintenance	<u>.14</u>	<u>10</u>	<u>.21</u>	<u>15</u>
Total Government of Hungary	US\$ 3.29	Ft 237	US\$ 4.90	352

HUNGARY  
State Property Agency  
EC PHARE Budget(91/92 under discussion)  
 (US\$ mil. by amounts proposed during period)  
 (ECU 1 =s US\$ 1.38)

I	<u>Internal Operating Costs</u>		1990/91		1991/92
	<u>Staff Advisers</u>	US\$	966		US\$ 1,242
	<u>Training</u>		753		759
	<u>Equipment</u>		<u>454</u>		<u>414</u>
		Total US\$	2,173		US\$ 2,415

II	<u>The cost of Technical skills required for individual transactions</u>		1990/91		1991/92
		Total US\$	4,727 *		US\$ 11,495 **

III Institution Building

	restructuring trust and others	Total US\$	Ø		US\$ 55,090
		Total EC PHARE US\$	6,900		US\$ 69,000

\* includes contingency (ECU 450,000) and audit (ECU 150,000) budget numbers (US\$828,000)

\*\* includes:

91/92 line item request	ECU	8,000,000	US\$	11,040,000
91/92 Budget Goal	ECU	50,000,000		
Less SPA items	ECU	(35,670,000)		
Balance	ECU	14,330,000		
MTI Projects		(12,000,000)		
MOA Projects		(2,000,000)		
Balance for MTI and MOA transaction costs		330,000	US\$	455,000
Total Available to support transaction costs			US\$	11,495,000



HUNGARY  
State Property Agency  
USAID Budget (under discussion)  
(US\$ mil. by amounts proposed during 91/92 period)

I Internal Operating Costs

<u>Project:</u> Complete the equipping of the SPA	Commitment: \$ 1 mil.
<u>Project:</u> Expand the rapid response assistance pool to the SPA	Commitment: \$ 1 mil.
<u>Project:</u> Equip the retail privatization effort	Commitment: \$ 1.5 mil.
<u>Project:</u> Extend the SPA long term advisor	Commitment: \$ .6 mil.
	Total \$ 4.1 mil.

II The cost of Technical skills required for individual transactions

<u>Project:</u> Pre-privatization reviews	Commitment: \$ 3 mil.
<u>Project:</u> Valuation support	Commitment: \$ 3 mil.
<u>Project:</u> Legal support	Commitment: \$ 4 mil.
<u>Project:</u> Legal review and documentation preparation	Commitment: \$ 1.5 mil.
<u>Project:</u> Individual Privatization efforts	Commitment: \$ 1 mil.
	Total \$12.5 mil.

III Institution Building

<u>Project:</u> Core Consultant Team	Commitment: \$ 1.5 mil.
<u>Project:</u> Public Information program	Commitment: \$ 1.5 mil.
<u>Project:</u> Privatization Training	Commitment: \$ .75 mil.
<u>Project:</u> Define and develop Hungary's privatization strategy	Commitment: \$ .5 mil.
<u>Project:</u> US/Hungarian Aid Assistance Coordinating Committee	
Committee Budget	\$ .5 mil.
Rapid Response Facility	5.0 mil.
	Total Commitment: \$ 5.5 mil.
<u>Project:</u> Privatization and Investment Promotion Materials	Commitment: \$ 1.5 mil.
<u>Project:</u> Investment promotion office	Commitment: \$ 2 mil.
<u>Project:</u> Support to the MIEA aid coordination office	Commitment: \$ 1.5 mil.
<u>Project:</u> Develop the Small Business Administration Agency	Commitment: \$ 3 mil.
<u>Project:</u> Legal aid bureau	Commitment: \$ 3 mil.
	Total institution Building Commitments fwd: \$20.75 mil.

	Total institution Building Commitments fwd:	\$20.75 mil.
<u>Project:</u>	Accounting aid bureau	
	Commitment:	\$ 4 mil.
<u>Project:</u>	Privatization strategy and practice consulting service	
	Commitment:	\$ 4 mil.
<u>Project:</u>	Training for privatization market intermediaries	
	Commitment:	\$ 2 mil.
<u>Project:</u>	Privatization Data Sharing in Eastern Europe	
	Commitment:	\$ 1.5 mil.
<u>Project:</u>	Privatization Analysis Bureau	
	Commitment:	\$ 2.5 mil.
<u>Project:</u>	Basic Business Training	
	Commitment:	\$ 2 mil.
<u>Project:</u>	Stock Market Development	
	Commitment:	\$ 3 mil.
	Total institution Building Commitments:	\$39.75 mil.
	Total USAID	\$56.35 mil.

HUNGARY  
State Property Agency  
World Bank Budget (under discussion)  
(US\$ mil. by amounts proposed during period)

II The cost of Technical skills required for individual transactions

The World Bank as a loan funder is less attractive than a grant funder but in circumstances where funds are needed, where other funders' usage guidelines make them unavailable, and where repayment to include interest cover is certain, World Bank funding is justifiable.

The SPA's experience with the First Privatization Programme (FPP) has established that the hard currency cost of technical assistance to position a major enterprise for sale and carry it out is in the US\$150,000 to US\$500,000 range with an average in the US\$200,000 range. The principal fee costs are:

Accounting, valuation and related:	\$ 50,000 per transaction
Legal Fees:	\$ 50,000 per transaction
Reimbursable Costs and Front end fees:	\$150,000 per transaction
Total	\$200,000 per transaction

It is anticipated that the per transaction front end costs will go up as the privatization process gets into the more difficult and less attractive transactions.

Current Situation:

Due to the nature of and rapid launch of the FPP the World Bank is the available funder to meet its transaction support costs. In addition the world bank will be asked to fund transaction costs for certain spontaneous transaction where funding is not available for similar reasons.

The World Bank has now begun the required documentary review to ascertain that the bidding procedures for the transactions proposed for funding have been properly undertaken. Those transactions judged satisfactory for funding will then be approved for funding and based on a world bank approved contract being entered into with the named provider of the technical services, the costs can be paid for by a draw down of a loan facility available from the World Bank through the National Bank of Hungary.

Present Request 1990/91:

The World Bank has been specifically requested to provide US\$4,000,000 to meet the technical assistance costs of the FPP in the 1990/91 cycle.

New proposed request 1991/92:

The World Bank is being requested to be the bridge and cushion funder for the 1991/92 privatization program. The amount requested (US\$23,000,000) is derived as follows:

- a. Number of anticipated transactions:  
125
- b. Period:  
1 March 1991 - 1 September 1992
- c. Average anticipated transaction cost:  
US\$ 300,000
- d. Total anticipated cost:  
US\$37,500,000
- e. Grant funding for individual active program transaction costs:
  - EC PHARE\*\* US\$16,222,000
  - USAID\* US\$ 1,000,000
  - Total Grant Funding US\$17,222,000\*\*
- f. Needs:
  - Shortfall (d. - e.) US\$20,278,000
  - Cushion (7%) US\$ 2,722,000
  - Total WB facility US\$23,000,000

\* The bulk of the USAID money being requested is being directed to support the spontaneous program rather than the Active Program.

\*\* This estimate is based on the willingness of the EC PHARE program to make the required program allocations to achieve this number. It is within the range of the initial agreements with the EC/PHARE officials.

MEMORANDUM

TO : Csepi Lajos, Managing Director  
FROM : Charles Twyman, Advisor  
DATE : 11 Dec., 1990  
REF: SPA's Funding position

BACKGROUND: You requested that I summarize for you my understanding of our current funding position.

CURRENT SITUATION: I am not at all aware of our Forint budget circumstances and there may be some activities that I am not aware of but to my knowledge our position can be summarized as follows.

RECOMMENDATION:

1. I urge you to appoint someone like Rajcsanyi to work on coordinating all of these efforts. As we go forward managing the various aspects of these donor activities and fitting in new donors and saying no as appropriate is an interesting and complex task. It must be well orchestrated by a Hungarian.
2. The internal control procedures for multiple activity grant's/loans I am developing around the PHARE program. That requires a financial administrators office (The PHARE properly insists). That office will probably become your budgeting and main financial control office.
3. Please consider that donor activity is not free! It costs your time and energy and takes your focus away from other activities. Unless you are convinced you want to spend the time on what they propose stay away from it. Better yet take the lead by proposing what you want and fitting them into your activities. You are riding a winning horse. They all will want to be aboard and each claim 100% of the credit for your success. Donors are noted for selling what they think will work with only some sensitivity to what is required. They also have a deserved reputation for being directive rather than consultative. However the World Bank's approach in Hungary is one of the most constructive I have ever seen for the most part. In spite of its crankiness the PHARE grant is very attractive in terms of allowing you considerable latitude to do what you want. UNIDO is the most restrictive.

USAID(USA)

1. What : Long term advisor  
Amt. : \$250,000 grant  
Status: C.G. Twyman in place for one year
2. What : Equipment  
Amt. : \$270,000 firm, \$220,000 on request grants  
Status: \$50,000 at SPA, \$220,000 awaiting customs clearance  
\$220,000 on request
3. What : Funding for technical assistance  
Amt. : \$500,000 grant  
Status: available and being delivered: PR, PHARE accounting, MIS, Strategic Planning
4. What : Significant multiple program  
Amt. : Several million in grants  
Status: Dr. Martonyi is presently in Washington requesting assistance, refer my memo

KNOW HOW FUND(UK)

1. What : Long term advisors  
Amt. : About US\$1,000,000 grant  
Status: Two long term advisors in place for two years, Leighton Davies and Fred Faiz
2. What : Privatization project assistance  
Amt. : \$500,000 grant  
Status: Funding for the front end cost of at least one privatization being considered

WORLD BANK(Multilateral)

1. What : Fund Technical Assistance required for the First Privatization Program  
Amt. : \$4,000,000 loan  
Status: Agreed in principal by WB, MOF and NBH, documents being passed and reviewed. SPA's homework still being tidied.
2. What : Funds for technical assistance for the bulk of the privatizations in 1991  
Amt. : About \$35,000,000 in loans  
Status: Very preliminary discussions with WB, awaits budgetting and a protracted reallocation fight in Hungary (my guess)

UNIDO(Multilateral)

- What : Fund one set of training trips, one in house training and one technical assistance  
Amt. : \$150,000 grant  
Status: Awaiting Vienna's approval

PHARE(EC, multilateral)

1. What : PHARE I Multipurpose grant for 1991  
Amt. : ECU5,000,000 (About \$7,000,000) grant  
Status: Awaiting approval in Brussels
2. What : PHARE II Multipurpose grant for 1992  
Amt. : To be determined, est. ECU5,000,000 grant  
Status: Currently being discussed in a Hungarian interministerial Committee, as yet we are not represented, we need to be or we will be excluded from the budgetting and allocation process!

CDC(Canada)

1. What : Long term advisor for public relations  
Amt. : \$250,000 grant  
Status: Confirming
2. What : Privatization training seminar in Canada on the Canadian experience  
Amount: About \$150,000 grant  
Status: Confirming

EBRD (Multilateral)

Potentially a major investor in Hungary and a provider of technical assistance. As their role and mission is not yet clear this conflict has yet to be resolved. I do not know what they are prepared to commit to nor whether it will be on a grant or loan basis. At this point they deserve a cautious welcome but as an organization they have as yet to weigh in on the world scene.

HUNGARY  
State Property Agency  
PHARE Budget and Work Programme  
for  
1 December, 1990 - 31 December, 1991  
With detail for the six month period  
1 December, 1990 - 31 May, 1991

October 1990



HUNGARY  
State Property Agency  
PHARE Budget and Work Programme

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N.B. Budget estimates denominated originally in US Dollar have been translated at 1.35 being the rate per The Financial Times on Oct. 11, 1990

HUNGARY  
State Property Agency  
PHARE Budget

For the period 1 December, 1990 - 31 December, 1991

Summary

(ECU 000s by amounts committed during period)

	Original Proposal* (total)	New Proposal (total)	6 Months Budget	1 June 1991 31 Dec. 1991	Notes
<u>1. Technical Assistance</u>					
3 (?) advisor(s) on retainer	500	500	250	250	1.1
1 financial administrator	200	200	100	100	1.2
Subtotal	700	700	350	350	
<u>2. Training</u>					
a. Regular (short 1-4 week) seminar	150	293	195	98	2.a.
b. Training in Hungary by foreign professionals	50	50	30	20	2.b.
c. Postgraduate education at western universities	125	175	105	70	2.c.
d. Training in Hungary by Hungarian professionals	-	28	14	14	2.d.
Subtotal	325	546	344	202	
<u>3. Technical Facilities</u>					
Subtotal	375	329	282	47	3.
<u>4. Specialist external consultancy for privatization cases</u>					
Subtotal	3,000	2,825	1,750	1,075	4.
<u>5. External auditor</u>					
Subtotal	150	150	90	60	5.
<u>6. Contingencies (9%)</u>					
Subtotal	450	450	300	150	
<u>7. Total</u>	ECU5,000	5,000	3,116	1,884	

\* figures are per paragraph 2.4 of the Annex to the Financing Memorandum between the European Economic Community and the State Property Agency.

## MAJOR BUDGET ASSUMPTIONS

(Refer to WORK PROGRAMME/DETAILED BUDGET for more information)

### 1. Technical Assistance

- 1.1. Advisors on retainer are assumed to start at a date 3 months after commencement of budget period and be employed for 12 months. The SPA cannot currently utilize additional long term in house advisers but does require rapid response assistance in a broad range of areas on a short term basis. It is envisaged tendering for firms to make available on a retained basis the range of projected skills required on a rapid deployment basis.
- 1.2. Financial administrator-assumed start date 3 months after commencement of budget period and be employed for 18 months.

### 2. Training

- 2.a. 39 staff each a 3 week seminar
- 2.b. Training in Hungary, Two programs of appr. 3-week duration each
- 2.c. Postgraduate education at western universities for 7 persons for 1 year
- 2.d. Training by Hungarian organizations on technical topics for instance computer software applications etc.

### 3. Technical facilities

The original cost estimates have been modified in accord with the SPA's expanded role in its recently revised enabling legislation and in accord with the equipment provided by another donor or tentatively pledged pending availability of funding.

### 4. Specialist external consultancy for privatization cases

The original cost estimates have been revised in accord with the increased equipment and training needs that have been identified. It is worth noting that this figure includes the already committed ECU350,000 for the start-up consultancy effort which is just being concluded.

### 5. External auditor

1 review during period plus start-up and advisory costs.

## WORK PROGRAMME/DETAILED BUDGET

**BACKGROUND:** The State Property Agency (SPA) has been operational since 1 March, 1990. It is now almost fully staffed and will be moving into permanent quarters in November, 1990. While it is currently partially equipped it lacks some basic equipment and its personnel are very much in need of detailed training. This training is expected to be a continuing feature of the SPA's activities as its needs change and it begins to experience personnel turnover. Its major cash need in the initial period is for funds to support its technical assistance requirements for its initial privatization programs, active and spontaneous. In addition the SPA's own organizational needs and public information requirements during the initial PHARE program are expected to be significant.

**CURRENT SITUATION:** The SPA has launched its First Privatization Programme (FPP) and is dealing day to day with a high volume of business. The SPA has immediate precisely-defined equipment (it already has staffed a 3 man information systems and computer unit) needs. The SPA also has training needs that are everyday more evident. Its consultancy needs are very much transaction tied and are now identifiable in terms of the scheduled active privatization launches which should encompass approximately 100 enterprises between now and 31 December, 1991. In addition the Spontaneous Privatization Program, which has already dealt with or has currently under advice over 100 enterprises, urgently requires valuation and industry-study support.

### WORK PROGRAMME:

#### GENERAL:

Upon the EC's approval of the this work programme and detailed budget for the 1st. six month period and approval and scheduling of the initial disbursement, the SPA will begin the detailed implementation of its planned work programme. While several of the activities will be done simultaneously they can be categorized in the major budgetary areas and will be undertaken approximately as indicated below.

SPECIFIC:

1. Technical assistance

-Senior Advisors:

The SPA at this point does not require additional long term internal senior advisers in addition to its a financial administrator and current externally funded specialists. It does however require specialized services to be available quickly to help resolve problems that need specialized assistance and rapid resolution. The approximate skill mix requirement is:

- advise on valuations
- Industry specialist advice
- Specialized transaction advice
- Specialized legal advice
- Public relations program assistance

How many firms it will be required to retain to get the appropriate skill mix is not certain. It is hoped that one will suffice though three, with a significant breadth of experience -varied industry expertise etc.- in the broad disciplines of merchant banking, accounting, and law may be required.

-Financial Administrator:

The SPA will require a financial administrator capable of managing the PHARE funds and overseeing the tendering and related administrative work. In addition he/she must be fluent in Hungarian and English with French desirable so that he can effectively interface with the SPA, the EC and consultants from various countries.

Budget: (ECU 000s amount committed during period)

	<u>Total in</u> <u>PHARE I</u>	<u>1st. six</u> <u>Months</u>	<u>2nd. six</u> <u>Months</u>
3 (?) advisor(s) on retainer (12 months)	500	250	250
1 financial administrator (18 months)	<u>200</u>	<u>100</u>	<u>100</u>
	700	350	350

## 2. Training

The SPA staff, reflective of Hungary in general, has a very low level of knowledge of business related issues. The SPA staff must work on a daily basis with sophisticated and experienced businessmen and advisors and make practical decisions on behalf of the Government of Hungary's privatization program. Besides the on the job training provided by experience and the resident long-term advisors, the SPA must have a mix of long and short term training on a continuing basis. The following training mix has been identified as suitable to meet a portion of the SPA's needs during PHARE I.

-a. Short term training: Training seminars at foreign locations on average of three weeks duration to include longer on the job training programs offered by international financial institutions private and multinational. It must be kept in mind that the SPA is a functioning and heavily burdened operation. The SPA can rarely afford to train large blocks of personnel at a time. It can however take personnel from various units off-line for short periods for training. For this reason more offshore training is envisaged than onshore. The additional benefit of offshore training is its language and skill total immersion and concentration feature. However the SPA will require budget flexibility to move budgeted funding from the short-term offshore training budget (a.) to onshore training budgets both by foreign (b.) and Hungarian firms (d.) when it is more efficient to bring offshore expertise in to teach at the SPA or off-site in Hungary or when a qualified Hungarian firm -typically a foreign joint venture or foreign supported operation- can provide support. The flexibility to move funds from the (b.) and (d.) budgets into the (a.) budget will not be required.

### Sample Topics:

- Asset and business valuation
- Privatization policy, mechanisms, and techniques
- Privatization of small businesses
- Private placements and public offerings
- Company restructuring
- ESOPs
- Leveraged and management buyouts
- Stock exchange
- Investment banking
- Tendering procedures
- Merger and acquisition
- Means to protect the state's interest (golden shares etc.)
- Visiting western law firms having experience in privatization
- Course on public relation

Budget: (ECU 000s amount committed during period)

	<u>Total in</u>	<u>1st. six</u>	<u>2nd. six</u>
	<u>PHARE I</u>	<u>Months</u>	<u>Months</u>
Approximately 39 persons trained 3 weeks of training each @ ECU 2500 week (1000 fee, 500 travel, 150-day per diem):	293	195	98

-b. Short Term Training: Training in Hungary for the staff and staff candidates of the SPA by foreign experts.

Sample Topics:

- valuation techniques
- Hungarian vs western accounting practices
- Privatization techniques
- Investment Banking
- Managing consultants
- Tendering procedures

Budget: (ECU 000s amount committed during period)

	<u>Total in PHARE I</u>	<u>1st. six Months</u>	<u>2nd. six Months</u>
Approximately 50 persons trained 3 weeks of training each @ ECU 2500 week (1000 fee, 500 travel, 150-day per diem):	293	195	98

-c. Postgraduate education at western universities for acquiring MBA, MA or Phd in relevant fields. Individuals selected will incur a two year employment contract for each one year of paid study. 7 person per year.

Budget: (ECU 000s amount committed during period)

	<u>Total in PHARE I</u>	<u>1st. six Months</u>	<u>2nd. six Months</u>
Approximately 7 persons trained at an average cost of ECU 25,000 per year derived as below.	293	195	98
Costs, 4,000 - 6,000 tuition fee			
1,000 - 2,000 travel expenses			
17,000 -20,000 living costs			
-----			
22,000 -28,000 total, avg. ECU 25,000			

-d. Training in Hungary by Hungarian professionals: The fact of the still improving language capability of the SPA means that many areas of general interest: the computer systems and programs, the Hungarian regulatory and legal environment, and the SPA's internal management control and accounting would be most effectively -cost and otherwise- delivered by firms with Hungarian experience and with Hungarian speaking experts. We estimate that nearly the entire staff (60) will be effected by this type training. The relatively small budget reflects the fact that the basic forint cost of such training would be expected to be funded through the SPA's government provided forint budget and the foreign exchange denominated costs only through the PHARE I program.

Budget: (ECU 000s amount committed during period)

	<u>Total in PHARE I</u>	<u>1st. six Months</u>	<u>2nd. six Months</u>
Approximately 60 persons trained at an average cost of ECU 500 per year	28*	14	14

\*Should this means of education prove more effective we would anticipate expanding this budget item particularly by transfers from the offshore seminar budget (a.) and the contingency line.

### 3. Technical Facilities

The EC funding for office equipment; hardware, software, training equipment, communications equipment etc. is designed to dovetail with equipment funded by another donor.

The EC supplied equipment will first be utilized to top-up the required equipment for individual workstations and the Local area network and then will be expended to complete the basic equipping of the office.

Budget: (ECU 000s amount committed during period)

	<u>Total in</u> <u>PHARE I</u>	<u>1st. six</u> <u>Months</u>	<u>2nd. six</u> <u>Months</u>
<u>Computer Hardware</u>			
5 workstation @ 4,000	20	20	
3 laptops @ 4,000	12	12	
30 Printers @ 800	24	24	
Graphics Workstation w/high speed printer	10	10	
2 Laser printers @ 4,000	8	8	
LAN and computer parts and spares	10	7	3
Monitor filters 60 @ 160	9	9	
Installation and training	14	14	
	<u>107</u>	<u>104</u>	<u>3</u>
<u>Office Equipment</u>			
Typewriters 10 @ 2400	24	24	
Copy machines:			
Large (1)	15	15	
Medium (3) @4,000	12	12	
Computerized telex	8	8	
Telefax (3) @ 1,600	5	5	
PABX (Telephone switchboard) and related equipment	40	35	5
	<u>104</u>	<u>99</u>	<u>5</u>
<u>Training and Presentation Materials</u>			
TV-sets 2 @ 600	1	1	
VCRs 2 @ 600	1	1	
Overhead Projector and supplies 2 @ 900	2	2	
Tape recorders 2 @ 500	1	1	
Slide projectors 2 @ 250	1	1	
	<u>6</u>	<u>6</u>	
<u>Software</u>			
System software	20	20	
Application software	92	53	39
	<u>112</u>	<u>73</u>	<u>39</u>
<b>TOTAL EQUIPMENT*</b>	<b>329</b>	<b>282</b>	<b>47</b>

\* This is a tentative number as another donor has yet to confirm its commitment to providing 20 PCs and 5 laptops and related equipment. Should they not confirm we will have to shift funding from the PHARE I pool in contingencies and from other line items and/or reduce our equipment purchases. The SPA will require significant flexibility among items as needs evolve. Any such movement will be properly documented.



4. Specialist external consultancy for privatization cases

The EC has funded the initial BZW/PW/BM consultancy which established the basic operating parameters of the SPA at a cost of about ECU 350,000. This is therefore already committed in the below noted figures.

It is felt that this line budget item is the major funding problem of Hungary and the State Property Agency. The purchase of the requisite skills to assure reasonable sale proceeds and suitable investors and market development will be expensive. The non-recoverable industry studies and background examination and policy work alone would dramatically tax this budget in the first year. The SPA will require budget flexibility to reallocate funds budgetted in the specialist project-related advisory work item (a. below) to the transaction related work (b. below).

a. The SPA will require specialist project-related advisory work on individual topics eg audit, valuation, industry studies, legal issues. This work is envisaged as policy related and therefore not cost recoverable from sales proceeds. We estimate the cost at 1000 ECU per day inclusive of direct expenses and the need at about 650 days or 7-12 projects. In addition the SPA, in line with its legislated requirements will undertake specialized valuation and revaluation work done at a cost of between ECU 50,000-100,000 per case. This specialized valuation, revaluation and second opinion valuation work will also not be cost recoverable from the sale proceeds in the transaction.

Budget: (ECU 000s amount committed during period)

	Total in PHARE I	1st. six Months	2nd. six Months
Spontaneous Privatization Dept. 2-4 projects	200	100	100
Active Privatization Dept. 3-6 cases	300	200	100
Valuation work, 6-10 cases	500	250	250
Legal Dept. 2-6 projects	150	100	50
	<u>1,150</u>	<u>650</u>	<u>500</u>

b. The SPA will require specific transaction related consultancy services typically from teams consisting of Merchant Bankers, Accountants and lawyers. These skill will typically be tendered for in regard to individual transactions. This will be the major cost item for the privatization program in Hungary. We estimate the cost at 1000 ECU per day inclusive of direct expense items and the requirement being for about 1,675 days. The SPA should be able to eventually recapture some significant portion of these cost from the sales proceeds of enterprises sold however the cash inflow in this regard is not expected to be significant for between 12 to 30 months and costs will have to be paid in the interim.

Budget: (ECU 000s amount committed during period)

	Total in PHARE I	1st. six Months	2nd. six Months
Spontaneous Privatization Dept.	120	60	60
Active Privatization Dept.	<u>1,555</u>	<u>1,040</u>	<u>515</u>
	1,675	1,100	575

Summary: Specialist external consultancy for privatization cases

Budget: (ECU 000s amount committed during period)

	<u>Total in PHARE I</u>	<u>1st. six Months</u>	<u>2nd. six Months</u>
a. Project related advisory	1,150	650	500
b. Privatization transactions	1,675	1,100	575
subtotal	2,825	1,750	1,075

5. External auditor

The SPA is advised that it will be required to have its PHARE program activities audited by external auditors chosen by the EC. We are advised that the EC has designated either the firm of Ernst & Young (E&Y) or Deloitte & Touche (DRT). The costs related to the external audit activity will have three principal components:

1. Set-up of the appropriate system with related programming.
2. Periodic advisory work on the audit and control system of the SPA's PHARE
3. Actual audit work.

Budget: (ECU 000s amount committed during period)

	<u>Total in PHARE I</u>	<u>1st. six Months</u>	<u>2nd. six Months</u>
Office and System Set-up	50	50	00
Periodic advisory work	20	10	10
Actual Audit (2)	80	30	50
	150	90	60

6. Contingencies

This is the SPA initial budget in its startup phase undertaking a privatization program of a scale and at a pace never before envisaged. The SPA requires some budgetary flexibility to move additional funds into individual line items as and when the need arises.

We are assuming a 9% contingency.

Budget: (ECU 000s amount committed during period)

	<u>Total in PHARE I</u>	<u>1st. six Months</u>	<u>2nd. six Months</u>
Contingency	450	300	150

BUDGET MANAGEMENT ASSUMPTIONS:

The SPA for purposes of managing the PHARE I Budget assumes:

1. With individually approved major line budget items (1-6), that it has the ability to disburse at its own discretion as long as it adheres to the EC's guidelines on tendering and related topics and the detailed operational guidelines specified in the Framework Agreement, the Financing Memorandum and related documents in in accord with good control and accounting procedures.

2. That the SPA has the ability to move allocations from the contingency item into major line items at its discretion.

3. That savings realized within any budget category can be freely reallocated within that category.

4. That savings realized within categories 1, 2, 3, and 5, can be freely reallocated to category 4.

5. That funds budgetted but uncommitted in the first six month period automatically flow into the second period.

6. That funds within category 2. Training can be freely reallocated from 2. a. to 2. b. and 2. d. but not the reverse without specific EC approval.

7. That the technical facilities budget (3.) is an indicative budget and that the SPA will be allowed considerable latitude to reallocate among items within the technical facilities budget to adjust to precise needs. This is principally driven by uncertainty as to the precise amount of equipment and the types that will be allocated by another donor.

8. That the appropriate EC office to approve shifts among budget line items other than above noted or the addition of new items is the Budapest Representative Office of the EC/PHARE program.

MIER Letterhead

His Excellency the Ambassador of the United States of America  
Mr. Charles H. Thomas  
Embassy of the United States of America  
Szabadsag ter 12  
H-1054 Budapest, Hungary

Date

Dear Mr. Ambassador

As a detailed follow-up to the initiative begun by Secretary Eagleberger in August, 1990 in his offer of assistance to the Republic of Hungary, and with the objective of bringing together the initiatives outlined in ongoing discussions with the Embassy of the United States of America, missions from the United States Department of the Treasury, the United States Department of State, the United States Agency for International Development, and other departments and agencies of the United States Government and specifically as a more detailed follow-up to the visit by Dr. Janos Martonyi, State Secretary of the Ministry of International Economic Relations of the Republic of Hungary with Ambassador Robert Barry and Mr. John Robson during their working meetings in Budapest and Washington, the Government of Hungary has prepared this Funding Request.

This Funding Request is an integral part of the execution phase of the GOH's economic reform strategy. This process is being undertaken with the cooperation of a broad range of donors and lending agencies some of whose contributions and program components I summarize below. Within a few weeks I would hope to have available for you a far more complete summary.

This Funding Request is based on the reality that the combination of the present energy cost scenario and Hungary's significant inherited debt burden means that Hungary has limited resources to focus when and where needed to carry out the required economic changes. There is a very real risk that the predictable economic hardship that will accompany the dramatic changes being undertaken in Hungary, will create too-great a political strain unless there is measurable progress in achieving the longer term goals.

It is the hope of the Government of Hungary that the United State of America can make technical assistance grant funding available totalling approximately US\$76.05 million during the USA fiscal year 1991 as a vital component of the donor support to the process of economic transformation in Hungary.

Our request, detailed in the attachment, is as follows:

PHASE I <u>Organization and immediate needs:</u>	
Fourteen Projects	\$ 24.75 mil.
PHASE II <u>Project design and implementation:</u>	
Twenty-two Projects	\$ <u>51.30</u> mil.
TOTAL REQUEST PHASE I & II	\$ 76.05 mil.

We look forward to your favorable consideration of our request  
Sincerely

Republic of Hungary  
DONOR FUNDING REQUEST  
United States of America  
Fiscal 1991

The Government of Hungary

Core Program to Achieve Economic Reform

-MISSION & STRATEGY

-The GOH's principal economic objective is to increase the efficiency of the Hungarian economy by harnessing the energy of a free market economy to the ownership and management of its economic asset base.

-This requires dramatic social and economic changes in Hungary.

-The broad range of activities that must be undertaken to bring about the required changes require a coordinated programmed approach.

-THE MEANS

-The private sector must control and lead Hungary economically if Hungary is to succeed economically.

-ACHIEVEMENTS

Hungary has demonstrated the political will to carry out this program.

-Hungary has reorganized the banking system, putting this sector on a private sector performance basis

-revised its tax laws bringing them in line with western practice

-implemented a most attractive foreign investment law which among other things permits foreign majority ownership without any required approval and the full repatriation of the initial investment and forint and hard currency profit

-passed a company's act. with the result over 15,000 have been registered in just over 2 years

-passed a bankruptcy act. and taken several (35) government enterprises into bankruptcy court

-Is to committed to convertability with a 1992 target

-and taken and is taking several other steps.

-Hungary is committed to an austerity and balanced budget and has reduced the industrial subsidies in the economy by over 80%

-Over 90% of the prices in Hungary are now set by the market (up from 77% in 1990).

-removed the import license on over 92% of Hungary's imports affecting 72% of total industrial production up from 32% in 1990

-reoriented its trade away from COMECON, now 30% down from 1989s 40%

-Hungary has the 1st. operating stock exchange in Eastern Europe

-Hungary has established a Small Business Administration modeled on the US precedent

-nearly 80 percent of Hungary's housing stock is privately owned

-Hungary has committed itself to dramatically reduce government subsidies across the board

-Hungary has already initiated a most ambitious privatization program

which has already been extended to encompass over 150 companies. It has established the State Property Agency to oversee and stimulate the process.

It has announced a retail privatization program involving well over 10,000 small "mom & pop" stores.

-RESOURCES: DONOR/DEVELOPMENT AGENCY SUPPORT

-Hungary's resources, financial and personnel, are not sufficient to support its desired and required privatization, restructuring, and financial reform program particularly given the time pressure on the process. Hungary is fortunate in having available the assistance of a several donors and development organizations. The following figures do not include more generalized support for balance of payment type purposes.

Principal Donors

The World Bank Group: This is the lead development organization in the Hungarian program. It has several years operating experience in the Hungarian environment and significant programs in place and underway. Its support is principally through loan funds. This type of funding is most logically used to fund activities where an earnings or cost recovery stream is anticipated. This principal would apply to its use for technical assistance as well as equipment and project work.

Economic Impact: US\$300 million plus per year

The EC project PHARE: This is the senior major grant donor in Hungary. The relationship between the objectives of the EC's grant assistance and of Hungary are very close. The PHARE programme's main resource commitment in its second phase are to the privatization and restructuring program. The smooth economic integration of Hungary into the EC will largely be a product of the success of the program work now being undertaken. The particular attractiveness of grant funding is that it permits the creation of program support activity, e.g. training, service delivery, administrative apparatus, which accelerate the process of change in the economy without burdening it with cost. Once in place the organizational structure of the PHARE funding makes it very responsive to the needs of operating entities.

Economic Impact: ECU100-150 million per year

The U.S. Government's program support: This has the possibility of being a second major grant donor in Hungary. The U.S.'s initial activities are very focussed on the privatization and financial structure reform objectives of Hungary. It is anticipated that the U.S. Government's programs will be project related and particularly well suited for Technical Assistance.

Economic Impact: US\$50-150 million per year.

European Bank for Reconstruction and Development: While not yet operational, it is anticipated that this regional development organization will gradually assume a major long term structural adjustment role focussing most probably on capital investment. In the short and medium term its role is unclear but the nature of its likely support; loans and capital injections into privatized operating entities, will make its activities closely represent a commercial/merchant bank on the one hand and a development operation like the World Bank on the other. It is to be anticipated that they will not have significant impact before mid-1992.

Economic Impact: US\$100-400 million per year based on Hungary's definable project needs. (estimate)

### Supportive Specialized Donors

Multilateral programs, UNDP, UNIDO, ILO, WHO and others will each have roles in their speciality areas. Their administration and absorption problems as compared to the major donor agencies will be more significant except to the extent that the individual Hungarian organizations take on the responsibility of managing their own projects. These specialized agencies lend themselves to support roles.

Economic Impact: US\$20-50 million per year (estimate)

Bilateral programs: The Know How Fund (UK), The Canadians, The French, The Germans, The Japanese, can each bring and have indeed brought focused support to major areas. Incorporating them into the fabric of the program is economically and politically important and has been most successful to date.

Economic Impact: US\$25-50 million per year (estimate)

-RESOURCE MANAGEMENT: ORGANIZATION/EXECUTION:

#### Basic Assumptions:

-Hungary's donor and development community support must be appropriately phased and directed so that it supports the various components of the economic reform program in a coordinated manner.

-The challenge for Hungary is to build the absorptive capacity to be able to properly utilize the help that can be made available.

-The program components will be executed in a decentralized manner at the level of the various executing organizations. However each basic component will be carefully integrated into the phased program.

-The work being undertaken will be largely undertaken with private sector skills. It is not the objective of the program to build into the Government a privatization and restructuring execution capability, it is the objective of the program to stimulate the expansion of the private sector skills available to this end in Hungary.

#### Structure:

#### Policy:

-The Government of Hungary through the Parliament, Cabinet, and various interministerial working groups will define the overall objectives and policies of the programs effected by donor and development agency programs.

#### The Ministry of International Economic Relations:

-The Government of Hungary's programs requiring donor and development agency assistance will be articulated and coordinated by the Ministry of International Economic Relations (MIER) with relevant input from the executing ministries and agencies, existing and planned.

-It will be the role of the MIER to coordinate the support roles of the various donor/development agencies involved in the process. MIER has established a unit responsible for coordinating all multilateral and unilateral donor aid. When fully staffed and equipped, this unit will allow the MIER to lend strong ministerial support to enabling bodies and coordinate the use of the funds throughout the economy. Individual operating entities, the State Property Agency, the Ministry for Trade and Industry, the Ministry of Agriculture, and others will carry out the individual programs.

Present Program focus:

-Donor and development agency program assistance at this point in time will be focused principally on getting the privatization and restructuring of the economy well underway.

Executing Agencies:

-The key execution agencies for carrying out the donor and development agency support focussed on privatization and the related restructuring are:

-The State Property Agency (SPA): With principal responsibility for the structuring and support of the privatization program with particular emphasis on the necessary institutional support that the process requires. They will be guiding through regulation and policy the privatization activities of the relevant ministries and the efforts of individual enterprises.

-The Ministry of Trade and Industry (MTI): The MTI is the Ministry with the largest responsibility for major operating enterprises, in addition it has the responsibility for a broad range of trade and industry related policy issues. The MTI in the context of the privatization and restructuring effort will have the principal responsibility for managing the process of prioritizing among their operating entities and helping those entities guide their activities so that they are in accord with government policy and can qualify for donor assistance. This is particularly true in privatization and related restructuring efforts.

-The Ministry of Agriculture (MA): The MA is the ministry with responsibility for the largest economic sector in Hungary with responsibilities encompassing both operational and policy matters. The MA in the context of the privatization and restructuring effort will have the principal responsibility for managing the process of prioritizing among their operating entities and helping those entities guide their activities so that they are in accord with government policy and can qualify for donor assistance. This is particularly true in privatization and related restructuring efforts.

-Other ministries: Each of the various functional ministries is touched by the privatization and industrial restructuring efforts. Their individual donor and development agency will be developed around their needs however their individual efforts would generally receive support more directly from the SPA's budget for instance to support Technical Assistance for privatization, than through general budgetary allocation.



EXECUTION:

Hungary is integrating their grant and development donors into a three phase, prioritized program cycle to support their current strategic initiative.

The three phases encompass:

PHASE I Organization and immediate needs

PHASE II Project design and implementation

PHASE III Continuing project identification, design, and implementation\*

\* Program evolution and project identification and design are a continuing technical support requirement which will flow from the ongoing technical assistance work in PHASE I move into PHASE II and then the cycle will be renewed in PHASE III. The PHASE III activities will move the project identification, design and implementation work in line with Hungary's national priorities, donor and development agency preferences, Hungary's absorption capacity and year to year funding availability.

It is the objective of the balance of this document to outline the project framework for Hungary's cooperation with the United States Government.

UNITED STATES OF AMERICA  
GOVERNMENT OF HUNGARY  
SUPPORT REQUEST 1991:

Request:

Hungary proposes that the United States of America (USA) consider funding a critical portion of a program to help sustain Hungary's political initiative to stimulate and put in place an active free market economy.

Project Components:

Hungary is requesting assistance for a series of projects. The project work is prioritized within PHASES I and PHASE II with the PHASE III activities being intended to continue the cycle.

Project Request Summary:

PHASE I Organization and immediate needs:

Fourteen projects \$ 24.75 mil.

PHASE II Project design and implementation:

Twenty Two projects \$ 51.30 mil.

TOTAL REQUEST PHASE I & II(36 projects) \$ 76.05 mil.

PHASE III Continuing program project identification, design and implementation

\*

\* The technical assistance budget for this activity is embodied in the MIER team support in PHASE I.

PHASE I  
Organization and immediate needs

US consider immediate funding for several quick disbursement facilities that we propose below. Hungary has several implementing organizations in place that require resources to carry out their ongoing tasks and thus has the absorptive capacity to utilize support.

Project 1: Core Consultant Team

The long term commitment of consultant team capable of calling on the resources to design and help manage the implementation of the USG supported projects. The team would require equipping and should be measured in terms of the projects they have launched. They should be directly responsible to the MIER. They would be directly supportive of the US donor efforts but would be responsible for integrating those resources into Hungary's overall needs. It would be hoped that within 90 days they would have accomplished the basic background work and their commitment could be reduced to a core group based in the MIER. This core group would be charged with the long term follow-up that will insure proper execution of the work we propose and PHASE III activities. The core group should be funded so that it can rapidly call on specialized resources to do the necessary design work on existing and new projects as they are identified. The Rapid availability of this team will determine the pace with which much of the other project work can commence.

Commitment: \$ 1.5 mil.

Project 2: Complete the equipping of the SPA

Complete the equipping, installation or equipment, design of systems, training of the State Property Agency (SPA) on the equipment and systems and fund the initial maintenance and programming of the equipment/systems. USAID has already initiated this activity and a needs assessment is being completed. We anticipate a need for about \$500,000 in equipment and \$500,000 in continuing systems design, training and maintenance work.

Commitment: \$ 1 mil.

Project 3: Public Information program

Complete the design and launch a full public education and communication program supporting the privatization effort in Hungary. Hungary's political will is driven by the perception of progress in this key area, privatization. The SPA needs to be able to inform the public and the world (particular investing) of its progress and programs. The fact that Hungary's experience's and successes are the pioneering ones in Eastern Europe makes communication even more vital. USAID has initiated the strategy phase of the SPA's public information program. The strategy work should be completed by the end of January and the public information program can be launched immediately thereafter.

Commitment: \$ 1.5 mil.

Project 4: Pre-privatization reviews

Fund a pre-privatization review by professional teams of each major enterprise to be actively privatized through the SPA by the Government. This will help establish what is common sense "doable" before the government calls for advisers to execute a transaction. We estimate 15 professional man days per enterprise at a \$1,000 per man day and we plan to undertake to sell at least 100 per year and would need to examine about 200 \$15,000 x 200 is \$3,000,000.

Commitment: \$ 3 mil.

Project 5: Privatization Training

Establish a fund for the training of Government of Hungary and private sector senior officers involved in Privatization and banking. For instance Hungary has trained several of its personnel in Washington with USAID and Hungarian American Enterprise Fund and World Bank assistance. We want to continue this program and expand it to include practical experience in American firms.

Commitment: \$ .75 mil.

Project 6: Define and develop Hungary's privatization strategy

Fund a continuing series of privatization strategy, team building seminars in Hungary for the involved officials. USAID is currently considering such support for the SPA. The effort could be expanded.

Commitment: \$ .5 mil.

Project 7: Expand the rapid response assistance pool to the SPA

Expand the current USAID fund to support the short term and rapid response technical assistance requirements of the SPA.

Commitment: \$ 1 mil.

Project 8: Equip the retail privatization effort

The Government of Hungary is undertaking the privatization of in excess of 10,000 small store-front operations. While the monetary impact of these transactions is small, the visibility and symbolic political impact is large. This project is presently virtually without resources. The EC programme PHARE has promised basic support. However the rapid mobilization of US assistance would be appropriate in two areas:

1. There are substantial linkages between this program and our Small Business Development effort, franchising initiatives, entrepreneurial training efforts and others. The US has much developed expertise in these areas.

Commitment: \$ 1 mil.

2. For reasons of machine and system compatibility as this group is to be attached to the SPA would request the US increase its funding support for their needed equipment.

Commitment: \$ .5 mil.

Total Commitment: \$ 1.5 mil.

Project 9: Valuation support

Fund a quick response pool of accounting and valuation skills that the SPA can call on to verify the fairness of prices proposed on transactions. The SPA must respond in 30 days to proposed privatizations and it needs the fundings in place so that it can commit skilled resources to meet this very politically visible need.

Commitment: \$ 3 mil.

Project 10: Legal support

Fund a quick response pool of legal skills to support the government's efforts in negotiating complex transactions and to quickly review key market initiated transactions. The owner, the people of Hungary are presently not well represented in many of the market driven transactions that come to the SPA's attention. Particularly in the precedent setting and model building part of the privatization program good skills should be committed.

Commitment: \$ 4 mil.

Project 11: Long Term Adviser, Ministry of Finance

Make available an internal, long term adviser in the Ministry of Finance able to assist in such areas as banking, insurance and privatization and/or taxes. The person should be equipped and funded so as to be able to call on additional support as required.

Commitment: \$ 1 mil.

Project 12: Long Term Adviser, State Property Agency

Make available an additional internal long term adviser to help support the launches of the active privatization programs. The person should be equipped and funded so as to be able to call on additional support as required.

Commitment: \$ 1 mil.

Project 13: Long Term Advisers, Credit, In the three principal state banks

Make available a long term adviser at each of the three major state commercial banks to help establish credit policies and procedures and to assist management and the government in defining how to treat their existing portfolios. The person should be equipped and funded so as to be able to call on additional support as required.

Commitment: \$ 3 mil.

Project 14: Long term adviser in the State Securities Supervisory body

Make available a long term adviser to assist the Hungarian equivalent of the SEC to get set up, organized, trained and equipped. The person should be equipped and funded so as to be able to call on additional support as required.

Commitment: \$ 2 mil.

(14 projects)

Total PHASE I Commitment: \$ 24.75 mil.

PHASE II  
Project Design and Implementation

Project 15: US/Hungarian Aid Assistance Coordinating Committee

The establishment of a focused consultative committee -US/Hungarian Aid Assistance Coordinating Committee- of practical level policy makers to deal with problems requiring rapid resolution in the US and Hungary's joint efforts to move Hungary toward a market economy. We are therefore requesting that the US continue working closely with the Government of Hungary and the consultant team to make pragmatism and implementation the guiding principle of this effort. We would welcome the strong involvement of the U.S. Embassy, and the Hungarian American Enterprise Fund. The principal input the US/Hungarian Aid Assistance Coordinating Committee would be the new projects developed by the core team in Project 1.

The Coordinating Committee would also administer a rapid response contingency facility to support the privatization and financial market reform efforts. This will permit rapid response to problem circumstances that may arise.

Commitment: Committee Budget	\$ .5 mil.
Rapid Response Facility	5.0 mil.
Total Commitment:	\$ 5.5 mil.

Project 16: Extend the SPA long term advisor

Extend the USAID long term policy advisor funding available to the SPA for at least another year.

Commitment: \$ .6 mil.

Project 17: Privatization and Investment Promotion Materials

Hungary requires support in its investment promotion effort aimed at foreign markets. It requires well designed promotional materials in several languages, updated and easily available compilations of the essential investment, tax, privatization and other materials. It requires well produced investment seminars. This effort can be coordinated by Hungary's Investment Promotion Office through such bodies as the Hungarian Chamber of Commerce and others.

Commitment: \$ 1.5 mil.

Project 18: Investment promotion office

Hungary is making a most significant effort to encourage foreign investment in Hungary in order to gain the benefit of the technology, management skills, and capital resources available elsewhere. This program is critical to the required rapid turnaround and redirection of the Hungarian economy away from its traditional COMECON market. Hungary in small and circumstances within the country are changing quickly. Hungary urgently requires a "one stop" investment office that can provide serious foreign investors with the assistance they require in working their way through the rapidly changing Hungarian environment. The successes of the Irish Development Authority and such initiatives as that undertaken by the city of Atlanta come to mind. Hungary has already established such an office within the MIER but still lacks key technical assistance, equipment, and funds to support its required activities. We would ask the immediate focus of attention on this area as we are unavoidably delaying and frustrating serious investment efforts now being considered by not having this office up and functional. A US effort to complement the EC support, to specifically include a long term adviser, would be most helpful.

Commitment: \$ 2 mil.

Project 19: Support to the MIER aid coordination office

The privatization effort requires a significant amount of inter-ministerial, inter-agency, and inter-enterprise coordination. We would like to fund and equip an administrative office within the MIER to gather together the various communications and miscellaneous coordination activities that are required. This function is presently decentralized and the follow-up is not what it should be. We would envisage this office working closely with the core consultant group, the investment promotion effort, and senior ministry officials. The EC is funding the core of this effort, US support particularly in the form of a US aid procedure knowledgeable adviser and equipment support would be most helpful.

Commitment: \$ 1.5 mil.

Project 20: Develop the Small Business Administration Agency

Hungary is privatizing over 10,000 small businesses. It also is trying to stimulate the development of the small business entrepreneurial group. Hungary's Small Business Administration equivalent has limited resources with which to develop programs, design training materials, identify the needs of small entrepreneurs. We would request assistance to equip, fund and provide technical support to this national initiative perhaps in a continuing cooperative effort with the US's SBA but with more significant formal support.

Commitment: \$ 3 mil.



Project 21: Legal review and documentation preparation

Design and implement a full legal review of the precedential and legislated experience with privatization in Hungary with the aim of designing basic "boilerplate" legal guidance to the market to speed up the process and guide it. At the present time smaller enterprises and entrepreneurs in particular cannot access the skills needed to document a transaction. Basic guidance and forms should be available in the market. In addition the Government needs assistance as the residual shareholder in many small transaction as to what its legal position should be on such issues as labor matters, warranties, etc. The project should include the design and production of the relevant forms with thought given to training the legal profession and others in their application.

Commitment: \$ 1.5 mil.

Project 22: Legal aid bureau

Based on the work in the above, design, fund, and implement a legal aid bureau for enterprises, or entrepreneurs seeking information on how to go about privatizing a government operations.

Commitment: \$ 3 mil.

Project 23: Accounting aid bureau

Design, fund, and implement an accounting assistance bureau which can help fund the delivery of the required accounting and valuation support needed for smaller enterprises and entrepreneurs.

Commitment: \$ 4 mil.

Project 24: Privatization strategy and practice consulting service

Design, fund and implement a preprivatization strategy advisory bureau that can give smaller entrepreneurs and enterprises practical advise on preparing for privatization, business plans, enterprise sale or purchase strategies, and guide them to the support available through the legal and accounting support bureaus.

Commitment: \$ 4 mil.

Project 25: Training for privatization market intermediaries

Design, fund, and deliver a training program for market intermediaries (banks, capital market players, entrepreneurs) on the privatization process in Hungary. The specific objective is to encourage and train a broader range of deal initiators. The intent is to deliver detailed guidance and training in merger & acquisition, liquidation and work-out skills custom tailored to the Hungarian market. The Hungarian Banker's Association, Stock Market and other intermediaries would be the principle participants. This would be a continuously updated training presented at regular intervals throughout each year.

Commitment: \$ 2 mil.

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Project 26: Individual Privatization efforts

The Government of Hungary would like to invite the US government to work with Hungary to design and implement the privatization of certain key enterprises or sectors. We would like to team to achieve model results in certain difficult and high impact cases hopefully on a pilot and reproducible basis. We would envisage projects that combine a high degree of financial market stimulus with significant public participation in such areas as housing or transport might be worth considering. This joint project should identify what is of mutual interest, design a program, fund it, and execute the privatization. This concept can be dramatically expanded if it proves successful.

Commitment: \$ 1 mil.

Project 27: Privatization Data Sharing in Eastern Europe

An ability to pool the experiences of the various Central European countries in the area of free market development and financial market reform would be most useful. We propose such an agency be designed, staffed, and equipped.

Commitment: \$ 1.5 mil.

Project 28: Privatization Analysis Bureau

The privatization effort requires ongoing analysis so that its short-term and long term effects can be properly judged. This information is critical for policy makers and donors alike. The significant linkages throughout the economy make proper tracking of the effects of the privatization program a complex task. We would request the funding, technical support and equipment necessary to establish a Privatization Research Bureau.

Commitment: \$ 2.5 mil.

Project 29: Basic Business Training

Hungary requires a long term training commitment to the training of Hungarians in basic book keeping and trading skills, import and export transaction mechanics, accounting, management fundamentals. This training should be delivered by a combination of programs, some available in Hungary others abroad. The programs should include funded training programs in host companies in the United States. This is a multifaceted and long term effort. We would anticipate first year disbursements in the range of 1 to 2.5 mil. Initial disbursements would focus on program designs, training materials (in many cases taking training programs available elsewhere and modifying them for Hungarian circumstances, translating them into Hungarian and training trainers) and implementation.

Commitment: \$ 2 mil.

Project 30: Stock Market Development

The work to expand the capabilities of the stock market and its related public education effort must be continued. The New York Stock Exchange, the SEC and others have already provided considerable assistance and advice. We would welcome a continuation and expansion of this effort.

Commitment: \$ 3 mil.

Project 31: Project Design Assistance

The Government of Hungary requires project design assistance in several specific areas and ministries to specifically include:

Environment: A project study to see what Hungary must do to bring its portion of the Danube in line with EC standards and better.

Transport: A project study to define what work Hungary must do to bring its navigable portion of the Danube up to at least the equivalent level of its EC neighbors.

Transport: Malev requires a study of Hungary's airports as regards adequacy, needed improvements and the related plans.

Transport: Hungary would like to commission a study as to the adequacy of its road network with the objective of developing a masterplan for its road network development.

Electricity: Hungary would like an analysis of its present electrical grid system with the objective of designing linkages to its EFTA and EC neighbors.

Gas: Hungary would like a study to review the feasibility and cost of linking its gas piping system to the western countries trying to reduce its absolute dependence on one supplier.

Commitment: \$ 3 mil.

Project 32: Housing Sector Support

The Government of Hungary would request continued support of their program to establish low cost housing guidelines and programs.

Commitment: \$ 1.2 mil.

Project 33: Social Insurance Information System

The Government of Hungary would request assistance in designing an automated social insurance data system, help programming it and training its operators, and help equipping it.

Commitment: \$ .6 mil.

Project 34: Social Welfare program automation

The Government of Hungary would request assistance in designing an automated social welfare data system, help programming it and training its operators, and help equipping it.

Commitment: \$ 1.5 mil.

Project 35: Ministry of Justice

The Government of Hungary would request a major program of assistance to the Ministry of Justice with the aim of democratizing Hungary's laws and regulations. The components include an automated law, regulation and legislative tracking system modeled on the US model, technical advisers to assist in reviewing and drafting regulations and legislation, training for Hungarian officials from the ministry of Justice, and dramatic support to equipping training the regional and local courts.

Commitment: \$ 6.4 mil.

Project 36: Hungarian American Enterprise Fund

The Government of Hungary applauds the rapid success achieved by the Hungarian American Enterprise fund and would request the US Government's continued support for this initiative. The appropriate funding level would depend on the absorptive capacity indicated by the fund and the support available for that type of project.

(22 projects)

Total PHASE II Commitment: \$ 51.30 mil.

PHASE III

Continuing Project identification, design and implementation

It is anticipated that the core consultant group working in the MIER will, in the course of US fiscal 1991, identify new projects and/or participate in the expansion of the scope of projects already considered in PHASE I and PHASE II in an additional amount of between US\$25-75 mil.

These efforts will be closely coordinated with the US/Hungarian Aid Assistance Coordination Committee.

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TRIP REPORT

STATE PROPERTY AGENCY OF HUNGARY (SPA)  
&  
MINISTRY FOR THE ADMINISTRATION AND PRIVATIZATION OF  
NATIONAL PROPERTY OF THE CZECH REPUBLIC (MP)

13-15 MAY, 1991  
PRAGUE, CZECHOSLOVAKIA

FUNDING REFERENCE:

Technical Assistance to the State Property Agency of Hungary, USAID  
Contract No. ANE-0002-C-00-0047-00, USAID Project no. 180-0002-3-0183107  
STRATEGY DEVELOPMENT/TEAM BUILDING TRIPS, Warsaw and Prague

TASK OBJECTIVES AND SCOPE:

The privatization programs in Hungary, Czechoslovakia, and Poland -while distinct and at different stages in their development- have much in common in addition to their pioneering nature. The programs' leadership and the technocrats operating the programs need as many inputs as they can get to help them focus their efforts and operate effectively. This task was designed to use DRT International's intimate knowledge of the three countries' programs to bring together on a one-to-one basis the counterparts in key operating units of the nations' privatization efforts. The expected benefits were to help each country team further develop their own strategies by discussing common and dissimilar strategic objectives, to help each team learn from the others varying technical responses to common problems, and to start a dialogue among the key professional players at the operating level in the regional privatization effort.

APPROACH AND METHODS:

A four man team from Hungary, including the Long Term Advisor (LTA) and the Canadian Public Affairs Advisor (funded by the Canadian Government) traveled to Prague. DRT in Poland and Czechoslovakia had arranged meeting schedules tailored to the make up of the Hungarian team and the program focus in the two countries. In addition DRT locally helped gather copies of the relevant legal and background materials and provided detailed entrance briefings to the Hungarian team in order to allow them to be appropriately up-to-speed in their discussions with their local counterparts. The LTA and DRT handled the logistics. The LTA provided pre-trip briefings and briefing materials to the Hungarian participants before each trip and distributed copies of the relevant materials gathered in Poland and Czechoslovakia after the trip. DRT provided background materials on the SPA and the Hungarian effort and a proposed agenda to the participants in their respective locations. The SPA made available full sets of the relevant Hungarian Laws and other materials to the Polish and Czechoslovakian teams.

## SUMMARY OF RESULTS AND CONCLUSIONS:

- Both trips took place as planned.
- The respective teams each obtained a more detailed understanding of and appreciation for the other country's efforts.
- The relative youth of the personnel staffing the agencies is noteworthy in all three countries as is their technocratic (economic primarily) base.
- The differences created by the distinct political circumstances were most notable. The one most effecting the process seems to be the pending elections in both Poland and Czechoslovakia and the related need for public display of success or progress. The voucher systems seem to be largely driven by this political circumstance.
- The technical solutions to the various problems were quite similar though they evolved differently in their respective environments.
- To the degree that political solutions to technical problems were created early in the programs it made the technical problems more difficult or close to impossible. The Polish and Czech voucher system concepts are examples as is the Hungarian centralized retail privatization effort.
- The lack of local business and market skills slows the privatization and market development process and requires a reliance in many cases on foreign skills.
- The organizational and administrative problems of the various agencies were observed as very similar and equally frustrating. They focus on training, salary levels, rapid growth, changing and expanding responsibilities, staff turnover, equipping and funding.
- The problems of dealing with donor funding so as to employ them effectively were similar in Poland and Hungary.
- It was observed that Hungary is furthest along in its basic legal and policy infrastructure and appears to have the best focussed political support of the privatization process and the clearest consensus as to its related and very much privatization linked economic objectives.
- Hungary's major enterprise privatizations are significantly more advanced than in the other two countries in spite of for instance the "common knowledge" concept of the Polish progress as a result of their use of the "Big Bang" approach.
- Hungary's retail privatization effort has not made the progress of the other two countries. Hungary took back and is immediately applying some of the lessons learned in the small scale privatization programs in Czechoslovakia. Its political requirement to centrally manage and control the process is the major roadblock creating significant rigidities.
- Hungary's privatization public information program is less advanced and less organized than the Pole's but ahead of Czechoslovakia. However, Hungary's strong and consistent -if not fully organized- national information effort to support and promote investment seems to have had a comparatively very strong positive effect on its movement towards its economic goals and privatization in spite of its unfocussed support of its particular privatization goals and achievements.
- For Historic reasons Poland is very sensitive to foreign domination of its economy (foreign effectively means German in Poland) Czechoslovakia is sensitive but not to the same degree. Hungary for its part is the most open to foreign investment.

## LESSONS LEARNED:

- One work day is about optimal for this trip concept with generalized briefings and updates followed by meetings on specific topics, legal documentation, etc.
- The individual trips benefit require good organization and local knowledge particularly so the interests and needs of the teams can be matched.
- A major contributor to the longer term success of the trips was found to be the joint dining at lunch and dinner. In this and in other ways the trips benefit by being orchestrated to give one-on-one formal and informal time.
- The Hungarian team probably benefited most as it had the advantage of detailed prebriefings and the dynamics of its group being entirely focused on the trip effort.
- The team building within the SPA observed during and after the trip was significant but requires followup.
- The opportunity for SPA professionals to get away from their desks as cross-specialist teams appears valuable and gives internal communications a boost.
- The benefit of broadening the SPA's viewpoint and helping them get a sense of perspective seems to have been partially realized.
- Getting technicians together as technicians seems to have a more immediate applicability benefit than taking them to generalized seminars.
- Getting together the various laws and other documents to allow more detailed review was found to be of major importance.
- Reciprocal visits make sense. The team dynamics benefit in the Polish and Czech efforts should be developed and personal contacts should be expanded. A one trip contact doesn't do that.
- There appears to be a real benefit to cross briefings at the USAID and US Embassy level and potentially at the Hungarian Embassy during these trips.

## RECOMMENDED FOLLOW-UP:

Thesis: The Hungarian, Czech, and Polish privatization efforts will continue to be compared (and to a lesser degree the East German program) by many: multilateral and bilateral donors and lenders, financial markets, national policy analysts, and domestic political leaders. The SPA must be in a position to know and be able to compare its efforts with its most comparable neighbors, likewise it wants to be able to learn from and exchange lessons learned with these same neighbors.

### Response:

1. To continue to derive benefit from this initiative the SPA should have a specialized in-house committee that focuses on the various programs so that it can continue to build on the expertise that the initial trips developed. Adding the East German agency experience is the present missing link in this concept. The core team should probably be the DMD, a representative from the Active Privatization Program, a representative from the Preprivatization program, a representative from the Legal department and an archivist/researcher who continuously gathers materials, distributes it, arranges meetings and can quickly assemble data in the case of need.
2. Continuing contact at the working level should be encouraged. Reciprocal visits by the Poles and Czechs would seem to be the next step.
3. Bringing Bratislava into the loop and bringing the SPA up to date on the Treuhandanstalt's activities are initiatives that should be pursued.

TEAM COMPOSITION:

Concept: Hungary, Poland and Czechoslovakia have all established privatization organs. In each case however they encompass a somewhat different range of responsibilities. Where those responsibilities overlap with the Hungarian SPA is where the dialogue is the most useful from the SPA's viewpoint. The Czech program for instance is driven at the National Policy level principally through the Ministry of Finance however the execution and details of the privatization program are carried out at the State level with the SPA equivalents being based in Prague and Bratislava (for Slovakia) respectively. The Slovakian effort is at present still getting organized so a dialogue would not have been useful. The Bohemia/Moravia effort is underway and the contacts were scheduled in Prague. The Polish Program is based in a Ministry set up for the purpose of defining and executing the privatization process. However the Polish national program did not administer the small retail outlet privatizations but it does administer the development of the capital markets.

Practical Problems: The trips have to be built around the skills and interests of the team members. The availability of the various team members is not always predictable particularly for the team that must travel. The maximal team mix cannot always be achieved. It is most appropriate that the priorities of the technocrats getting on with the program are the transactions and that priority over-rides fact finding trips regardless of their importance. In this instance on neither trip could an appropriate person from the legal department join the team. Similarly in both cases the head of the Active Privatization unit had transaction related activities that forced him to cancel his travel. Related problems when senior people are involved are that Board meetings at which they must be present block out key parts of their schedules.

Identified Overlaps effecting the team composition:

Poland:

- Large Scale Privatization Program
- Enterprise Transformation (regulation) Program
- Public Information Program
- Legislative framework
- Significant donor support
- Role of compensation legislation
- How title issues are being resolved
- Capital Market involvement

Czechoslovakia:

- Large Scale Privatization Program
- Enterprise transformation (regulation) program
- Public Information Program
- Small Scale Privatization Program
- Legislative framework
- Significant donor support (on the way)
- Role of compensation legislation
- How title issues are being resolved

Hungary:

- Large Scale Privatization Program
- Enterprise transformation (regulation) program
- Public Information Program
- Small Scale Privatization Program
- Legislative framework
- Significant donor support
- Role of compensation legislation
- How title issues are being resolved
- Capital Market involvement

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Differences effecting the programs' relative positions that need to be understood that effected team composition:

Poland:

Imminent elections  
Voucher system under consideration  
Role of labor  
Legislative differences  
Excellent progress in retail unit privatizations  
Slow progress in major privatizations  
Direct role in capital market development  
The size of the Polish undertaking

Czechoslovakia:

Imminent elections  
Voucher system apparently in place  
Legislative differences  
Excellent progress in retail unit privatizations  
Slow progress in major privatizations  
The practical effect of operating the program with a centralized policy but independent operating agencies in two states

Hungary:

A privatization Agency not a ministry i.e. not cabinet level  
Relatively small Hungarian manpower and budgetary commitment

Actual Csechoslovakian trip team Composition

Hungarian Team:

Racz Erno: Director, Preprivatization Program SPA  
Lascsik Attila: Officer Active Privatization Dept. SPA  
Twyman Charles: Advisor, SPA  
Hollo Gyorgy: Advisor on Public Affairs, SPA

Czech Party:

Ministry For the Administration and Privatization of National Property of the Czech Republic:

Dr. Alexova: Specialist, retail privatization  
Dr. Holub: Specialist, restitution  
Dr. Jirilos: Specialist, large privatizations  
Mrs. Falharova: Secretary to the Minister of Privatization  
Judr. Charles Francis Jelinek: Legal Adviser to the Minister of Privatization

DRT Resource Consultants:

Mr. Mel Mraz: Office Management Partner, Bratislava  
Mr. John Mandak: Office Management Partner, Prague

USA Embassy Briefing:

Harvey D. Lampert: First Secretary (Economic)

Canadian Embassy Briefing:

Jennifer Daubeny: Third Secretary

AGENDA:

Monday 13 May, 1991

08:30-09:30 Briefing at DRT Czechoslovakia  
09:30-12:30 Joint Meetings at DRT Czechoslovakia  
12:30-14:00 Luncheon discussions  
14:00-17:00 Joint Meeting at the MP  
17:00-18:00 Hungarian team debriefing  
19:30-21:00 Dinner discussions

Tuesday 14 May, 1991

08:30-10:30 Individual meeting followups

\* during the individual session Racz Erno had most valuable detailed meetings with the retail privatization unit. Mr. Hollo met separately with the Canadian Embassy on Tuesday. Mr. Twyman met with the US Embassy on Tuesday separately from the Hungarian party.

AGENDA TOPICS:\*\*

\*\* The following items were agreed to be of mutual interest however the discussion was free-form rather than structured and was a dialogue between equals after some ice was broken.

1. Legislative issues - title, taxes, investment laws, bankruptcy laws, foreign exchange regulations, company law, other regulations. What are the local ground rules how are problems being solved.
2. Advisors - how to locate, terms of reference, good and bad experiences, costs
3. Program designs: Government initiated sales, market initiated sales, small business sales programs
4. Public Relations: programs, advisers, problems
5. Funding of the privatization process: the donor and lending agencies roles, how to deal with them, current trends among donors.
6. Organizational issues: How to equip, staff, organize, train, motivate, pay, manage the privatization process.
7. Longer term coordination opportunities: exchange of documentation, information bank on advisers, donor coordination, exchange of investment opportunity information.
8. Finding capital: capital and money market development
9. Management skills and technology transfer: the prospects
10. Linkages: accounting systems, training, communications etc.
11. Valuation: guidelines and problems.
12. Conflicts: Transparency vs. speed, selection vs. open tender
13. How to deal with Monopolies
14. Labor issues
15. Previous owner compensation

OVERALL IMPRESSIONS:

Organizational:

- 1. The Czech program's basic policy is driven by the National Ministry of Finance approved by the National Assembly and much of the execution occurs at the Czech and Slovak state level.
- 2. The organizational responses to the needs of the large privatization program are slow forming. The problem is complicated by having to establish simultaneously a National and two State Property Funds to take over the ownership rights of the assets while establishing two state privatization agencies all having to be orchestrated around a restitution program and a voucher scheme. My judgement is that they are way behind on their organizational efforts given the several tasks they have set themselves. The fact that several organizations haven't been formed yet and several related key documents like the basic privatization guidelines haven't been authored but are scheduled means it is a bit early to tell.
- 3. The donor community has not yet been able to focus resources on assisting the Czechs as the Czechs have only just recently rejoined the intl. community thus the Czechs have not as yet had international technical assistance made broadly available to them.
- 4. The Czech Republic have had a quite successful retail privatization effort. They claim it potentially will involve about 100,000 operations. They decentralized the process down to 76 Municipal committees (each 20 member committee paid for by the MP, Chairman named by the Minister and one staff person seconded from Prague). The committees run auctions under quite flexible rules particularly as to price which has resulted in a large number of sale of both retail operations and small state enterprise.
- 5. The Czech privatization ministry has about 65 personnel the Slovak about 80 (excluding the retail program field staffs). The minister is actively involved in most of the areas of activity of the agency.
- 6. The Czech privatization ministry does not have any residual management or ownership role, the large enterprise privatizations are not managed by it (they are done on an ad hoc basis at the national basis -Skoda-Bata-Prague Hotel). They have executed the small privatization program, are helping set up the property funds and are involved in trying to make the voucher scheme workable. They have the responsibility of outlining the detailed privatization guidelines that all enterprises will have to adhere to. That is due to be published on 1 July. Eventually they will have a responsibility for reviewing for approval the mandatory enterprise prepared privatization programs which are under their state's jurisdiction.
- 7. The Czechs do not have a stock exchange.
- 8. The Czechs, like the Poles have an election imminent which effects much of what they do.
- 9. The closest Czechoslovakian analog to the SPA appears to be the yet unconstituted property funds which are to be operating holding companies that have the power to act as owner on behalf of the State and negotiate sale of the enterprises among its other activities. It is envisaged that essentially all of the state enterprises will be transformed into corporate form and lodged in a the state or federal fund. At the national level the fund will have a nine man presidium nominated by government and elected by the national assembly for a 5 year term. The presidium will name an 9 member executive council to manage the fund. In addition there is an independent 5 member supervisory council named by the assembly to review the activities of the Fund. These funds appear to be conceived to have a very broad role. How they will manage those various roles to yet to be seen. The Czechs do not appeared to have had to grapple with the practical effect of having ownership in the Funds for certain purposes but management is many cases apparently to continue in the hands of the relevant ministry.

-10. The Czechoslovakians apparently do not have a coordinated public relations program focused on privatization. The Minister of the MP handles much of the activity and firms have been engaged regarding individual sales (SKODA).

-11. The problems of staff training, competitive salaries (a difference exists between private sector finance related jobs and the MP's salary range), inexperience, and unclear and changing policy guidance parallel to a greater or lesser degree that seen elsewhere.

Substantive:

- 1. The Czechs have very little foreign or domestic debt. As a result the externally driven urgency of their privatization program and their enterprise restructuring effort is not as great as in Poland and Hungary.
- 2. The perceived lack of economic urgency gives the Czech privatization and the related programs -the restitution program, voucher program- a social reform twist with apparently little of the the public or national leadership pressure to get a viable national economic apparatus in place quickly. This is in marked contrast to the situation in Hungary and to a lesser degree in Poland. However the fact of elections coming up shortly require that the privatization program be seen as delivering some of its social objectives in accord with the Government's oratory, the voucher scheme being a major item in this regard.
- 3. The Czech voucher scheme forseees eligible individuals over 18 years of age purchasing vouchers for 1,000 Krs. each. Each voucher is the property of the named buyer but he can assign the power to manage it. Vouchers can be exchanged for shares in certain companies or pools of companies. The rules on how shares will be priced or what companies or how much of them will be available through voucher holder schemes have not been worked out. In sum the details of the voucher scheme haven't been sorted out yet but it is viewed as politically important. The philosophy of the program is redistributive not practical or market development oriented.
- 4. The Czechs tightly control foreign investment through a required government (MOF) approval procedure. They apparently have not established the full level of their need for capital to help restructure their economy and with limited debt and a surplus national budget they are hesitant to bring about a rapid inflow of foreign capital. The split between the Czech and Slovak republics as regards investment authority etc. further confuses matters.
- 5. The Czechs have just begun to address the legislative and subsequent administrative agenda that will refocus their economy (forinstance the April 1990 enactment or modifications of: Business Code, Private Enterprise Act, Foreign Trade Act, Joint Venture Act (Foreign Investment Act), State Enterprise Act, Foreign Exchange Act, Income Tax Act, Turnover Tax Act, Non-Residential Premises Act) much significant additional legislation is planned and the implementation phase of them is still forming.
- 6. The Czech Restitution Law sets an effective start date of the Nationalization decrees of 25 February 1948. The law envisages restitution in kind with an option of financial restitution (capped) to eligible citizens (which is tightly defined) who file for restitution within a defined time period. Agricultural land is specifically excluded from coverage under the law. Individuals claiming restitution of land and buildings assume the liabilities and lease obligations for the sites when they assume ownership. The major pragmatic benefit is hoped to be to create an immediate market in real estate and houses and a related stimulus in the construction industry. The practical aspects of handling the restitution claims are still being resolved.
- 7. The large Privatization law makes it the responsibility of the individual enterprise (about 3,000 enterprises) to come up with a privatization plan in accord with a to-be-published guideline. The founding ministry, if there is one, or the Federal Ministry of Finance (in certain cases), or the Czech and Slovak Republics' Ministry of Privatization review the privatization plan for approval. The first step is uniformly to effect the transfer of the enterprise or its assets into one of the property funds, essentially removing effective ownership control of the enterprises from the enterprise. The practical ramifications of this approach had not been fully thought through or planned for at the time of our visit. Followup visits with the Property Funds -when they are instituted- and at the MPs as the program evolves will be interesting as will visits at the MOF.

-8. The Czechs seem to be favoring minority worker and management position in firms. They have not had to deal either with a strong labor movement or an initial euphoria with the ESOP concept.

-9. The Czechs intend to try to defuse the problem of the independence of the Enterprises and their ruling councils by making them responsible for their own privatization programs and then placing legal control of them through transformation into legal entities and placing them with the funds.

-10. The pace of the Czech privatization program is very much effected by the limited amount of political urgency associated with the program, the linking of the program to the voucher and restitution issues and their related administrative needs, unclear signals being send to domestic and international investors, and a recently initiated legislative agenda addressing basic business related issues -tax, foreign investment legislation, foreign currency restrictions etc.

## RESOURCE MATERIALS

"Investing in the Czech and Slovak Federal Republics", February, 1991, DRT Poland information brochure

"Large-Scale Privatization Law", Dr. Bohuslav Klein, Supplement of the Czechoslovak Foreign Trade Magazine, undated

"Large Privatization Law passed", CTK-ECOSERVICE news release, 28 Feb. '91

"Law on the Conditions of Transfer of State Property to Other Persons" (large privatisation law), Federal Assembly, 26 February, 1991

"Law covering the divesting of some state ownership rights attached to certain things to legal or natural entities" (Small privatization law), Federal Assembly, 25 October, 1990

"Law of the Czech National Council of November 15. 1990 on the activities of the Czech Republic in the course of divesting certain state ownership rights attached to certain objects to other legal or natural entities" (Small privatization law of the Czech Republic)

"The Joint-Stock Companies Act", Federal Assembly, 18 April, 1990

"The Enterprise with Foreign Property Participation Act" (Joint Venture Act), Federal Assembly, 19 April, 1990

"Creating the Invisible Hand", The Economist, May 11th 1991

"From Marx to the Market", The Economist, May 11th 1991

"Act on Protection of Economic Competition" (Competition Law), Federal Assembly, 30 January, 1991

"Law on Extrajudicial Rehabilitation" (Restitution Law), Federal Assembly, 22 February, 1991

"Market Relations and Hard Currency - feature", ECOSERVICE, 5 March, 1991 the summary of a study by Tomas Parizek, departmental head at the Czechoslovak State Bank titled "Market relations and Hard Currency"

"Doing Business in Czechoslovakia", Canadian Embassy, Prague, Feb. 1991

"Going to Market: Privatization in Central and Eastern Europe", Manual Hinds and Gerhard Pohl, The World Bank, April 1991

MEMORANDUM

TO : Attached Distribution List  
FROM : Charles G. Twyman, Advisor, State Property Agency of Hungary  
DATE : 10 July, 1991

REF. : Trip Report, visit by the State Property Agency (SPA) of Hungary to the Ministry for Ownership Change (MOC) of Poland

BACKGROUND:

The USAID funded visits by SPA team to their counterpart organizations in Poland and Czechoslovakia. The principal purposes of that trip were to:

1. Initiate a mutually beneficial dialogue with our professional peers in the Privatization agencies in Poland and Czechoslovakia.
2. To try to exchange information on the technical aspects of the nations' respective privatization programs.

PURPOSE OF THIS TRIP REPORT:

The purpose of this Trip Report is to give the participants and interested observers a summary view of what was learned on the trip. The individual participants, depending on their area of interest, learned far more in their individual specialities.

This report is not designed as an exhaustive comparative analysis of the privatization programs of the nations concerned. It must be particularly noted it is designed for an audience with a detailed knowledge of the Hungarian privatization program and as a result presupposes the reader is comparing the comments in the report with the Hungarian experience which the reader knows.



DISTRIBUTION LIST

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Poland  
Czechoslovakia

DRT

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MEMORANDUM

TO :DRT Hungary, Ben Case, George Szelecki  
DRT Poland, Jan Maciejewicz, Piotr Cyburt  
DRT Czechoslovakia, John Mandak, Mel Mraz  
DRT Washington (ILA), Robin McPhail, Teresa Mastrangelo

FROM :Charles G. Twyman, Adviser, State Property Agency of Hungary,  
DRT Washington (ILA)

DATE :11 July, 1991

REF :Visit by the State Property Agency of Hungary (SPA) to their  
counterpart agencies in Poland and Czechoslovakia

BACKGROUND: We are all working in our respective practices on various aspects of the privatisation product. It is helpful every now and again to participate in an effort that overlaps us all. With the excellent cooperation and assistance of DRT Czechoslovakia -Mel Mraz- and DRT Poland -Piotr Cyburt- we just completed working level visits between the operational staffs of Hungary's privatization agency and their Czech and Polish counterparts.

CURRENT SITUATION: We in Hungary have had a chance do digest our visit and the attached trip report is one product. It is useful in that it gives a summary snapshot of the Polish and Czech programs at this point in time. It is useful for followup and our professional skill levels that we periodically update ourselves on this type information. This is particularly the case as the ILA practice has just developed an excellent contractual opportunity that has a major focus on this subject. Robin and Teresa will be bringing you more up to date on that in the future.

REQUEST: I would ask that you review what I have written. If you have thoughts, additions, or modifications let me know. I am particularly interested in getting copies of new laws and regulations as they come out on this and related subjects, for instance the Czech Privatization guidelines were due to be published on 1 July (I suspect they were a bit delayed), the voucher system in Poland was just announced and as TR London designed it we should have some information on that. If you could keep me in mind when those materials come across your desks I would appreciate it. I have just received a draft copy of the Romanian Privatization law and have had a chance to review it if that is of interest, etc.

OBSERVATION: I suspect two things will happen:

1. The dialogue between the privatization agencies will continue and we can benefit from continuing to play a part.
2. The new ILA IQC will give us a very sound business reason to become very knowledgeable on this subject. On the short visits to Poland and Czechoslovakia I saw a broad range of opportunities.

FOLLOWUP REQUEST:

I would request that Piotr Cyburt deliver a copy of this report (enclosed) to USAID Mr. William R. Joslin perhaps in a meeting where you have discussions on reciprocal visits by the Polish team to Hungary. I would suggest getting briefed by Robin and Teresa on the USAID IQC before such a meeting.

I would likewise request that Mel Mraz do the same in Prague however as the USAID person was out when I visited he may want to initiate a visit with her (Lee Roussel-the spelling may not be correct-) and deliver a report with a copy to Harvey Lampert the Economic Secretary at the US Embassy with whom I did meet.

TRIP REPORT

STATE PROPERTY AGENCY OF HUNGARY (SPA)  
&  
MINISTRY FOR OWNERSHIP CHANGE OF POLAND (MOC)

3-5 JUNE, 1991  
WARSAW, POLAND

FUNDING REFERENCE:

Technical Assistance to the State Property Agency of Hungary, USAID  
Contract No. ANE-0002-C-00-0047-00, USAID Project no. 180-0002-3-0183107  
STRATEGY DEVELOPMENT/TEAM BUILDING TRIPS, Warsaw and Prague

TASK OBJECTIVES AND SCOPE:

The privatization programs in Hungary, Czechoslovakia, and Poland -while distinct and at different stages in their development- have much in common in addition to their pioneering nature. The programs' leadership and the technocrats operating the programs need as many inputs as they can get to help them focus their efforts and operate effectively. This task was designed to use DRT International's intimate knowledge of the three countries' programs to bring together on a one-to-one basis the counterparts in key operating units of the nations' privatization efforts. The expected benefits were to help each country team further develop their own strategies by discussing common and dissimilar strategic objectives, to help each team learn from the others varying technical responses to common problems, and to start a dialogue among the key professional players at the operating level in the regional privatization effort.

APPROACH AND METHODS:

A five man team from Hungary, including the Long Term Advisor (LTA) and the Canadian Public Affairs Advisor (funded by the Canadian Government) traveled to Warsaw. DRT in Poland and Czechoslovakia had arranged meeting schedules tailored to the make up of the Hungarian team and the program focus in the two countries. In addition DRT locally helped gather copies of the relevant legal and background materials and provided detailed entrance briefings to the Hungarian team in order to allow them to be appropriately up-to-speed in their discussions with their local counterparts. The LTA and DRT handled the logistics. The LTA provided pre-trip briefings and briefing materials to the Hungarian participants before each trip and distributed copies of the relevant materials gathered in Poland and Czechoslovakia after the trip. DRT provided background materials on the SPA and the Hungarian effort and a proposed agenda to the participants in their respective locations. The SPA made available full sets of the relevant Hungarian Laws and other materials to the Polish and Czechoslovakian teams.

## SUMMARY OF RESULTS AND CONCLUSIONS:

-Both trips took place as planned.

-The respective teams each obtained a more detailed understanding of and appreciation for the other country's efforts.

-The relative youth of the personnel staffing the agencies is noteworthy in all three countries as is their technocratic (economic primarily) base.

-The differences created by the distinct political circumstances were most notable. The one most effecting the process seems to be the pending elections in both Poland and Czechoslovakia and the related need for public display of success or progress. The voucher systems seem to be largely driven by this political circumstance.

-The technical solutions to the various problems were quite similar though they evolved differently in their respective environments.

-To the degree that political solutions to technical problems were created early in the programs it made the technical problems more difficult or close to impossible. The Polish and Czech voucher system concepts are examples as is the Hungarian centralized retail privatization effort.

-The lack of local business and market skills slows the privatization and market development process and requires a reliance in many cases on foreign skills.

-The organizational and administrative problems of the various agencies were observed as very similar and equally frustrating. They focus on training, salary levels, rapid growth, changing and expanding responsibilities, staff turnover, equipping and funding.

-The problems of dealing with donor funding so as to employ them effectively were similar in Poland and Hungary.

-It was observed that Hungary is furthest along in its basic legal and policy infrastructure and appears to have the best focussed political support of the privatization process and the clearest consensus as to its related and very much privatization linked economic objectives.

-Hungary's major enterprise privatizations are significantly more advanced than in the other two countries in spite of for instance the "common knowledge" concept of the Polish progress as a result of their use of the "Big Bang" approach.

-Hungary's retail privatization effort has not made the progress of the other two countries. Hungary took back and is immediately applying some of the lessons learned in the small scale privatization programs in Czechoslovakia. Its political requirement to centrally manage and control the process is the major roadblock creating significant rigidities.

-Hungary's privatization public information program is less advanced and less organized than the Pole's but ahead of Czechoslovakia. However, Hungary's strong and consistent -if not fully organized- national information effort to support and promote investment seems to have had a comparatively very strong positive effect on its movement towards its economic goals and privatization in spite of its unfocussed support of its particular privatization goals and achievements.

-For Historic reasons Poland is very sensitive to foreign domination of its economy (foreign effectively means German in Poland) Czechoslovakia is sensitive but not to the same degree. Hungary for its part is the most open to foreign investment.

## LESSONS LEARNED:

-One work day is about optimal for this trip concept with generalized briefings and updates followed by meetings on specific topics, legal documentation, etc.

-The individual trips benefit require good organization and local knowledge particularly so the interests and needs of the teams can be matched.

-A major contributor to the longer term success of the trips was found to be the joint dining at lunch and dinner. In this and in other ways the trips benefit by being orchestrated to give one-on-one formal and informal time.

-The Hungarian team probably benefited most as it had the advantage of detailed prebriefings and the dynamics of its group being entirely focused on the trip effort.

-The team building within the SPA observed during and after the trip was significant but requires followup.

-The opportunity for SPA professionals to get away from their desks as cross-specialist teams appears valuable and gives internal communications a boost.

-The benefit of broadening the SPA's viewpoint and helping them get a sense of perspective seems to have been partially realized.

-Getting technicians together as technicians seems to have a more immediate applicability benefit than taking them to generalized seminars. ✓

-Getting together the various laws and other documents to allow more detailed review was found to be of major importance.

-Reciprocal visits make sense. The team dynamics benefit in the Polish and Czech efforts should be developed and personal contacts should be expanded. A one trip contact doesn't do that.

-There appears to be a real benefit to cross briefings at the USAID and US Embassy level and potentially at the Hungarian Embassy during these trips.

## RECOMMENDED FOLLOW-UP:

Thesis: The Hungarian, Czech, and Polish privatization efforts will continue to be compared (and to a lesser degree the East German program) by many: multilateral and bilateral donors and lenders, financial markets, national policy analysts, and domestic political leaders. The SPA must be in a position to know and be able to compare its efforts with its most comparable neighbors, likewise it wants to be able to learn from and exchange lessons learned with these same neighbors. ]

### Response:

1. To continue to derive benefit from this initiative the SPA should have a specialized in-house committee that focuses on the various programs so that it can continue to build on the expertise that the initial trips developed. Adding the East German agency experience is the present missing link in this concept. The core team should probably be the DMD, a representative from the Active Privatization Program, a representative from the Preprivatization program, a representative from the Legal department and an archivist/researcher who continuously gathers materials, distributes it, arranges meetings and can quickly assemble data in the case of need.

2. Continuing contact at the working level should be encouraged. Reciprocal visits by the Poles and Czechs would seem to be the next step.

3. Bringing Bratislava into the loop and bringing the SPA up to date on the Treuhandanstalt's activities are initiatives that should be pursued.

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## TEAM COMPOSITION:

Concept: Hungary, Poland and Czechoslovakia have all established privatization organs. In each case however they encompass a somewhat different range of responsibilities. Where those responsibilities overlap with the Hungarian SPA is where the dialogue is the most useful from the SPA's viewpoint. The Czech program for instance is driven at the National Policy level principally through the Ministry of Finance however the execution and details of the privatization program are carried out at the State level with the SPA equivalents being based in Prague and Bratislava (for Slovakia) respectively. The Slovakian effort is at present still getting organized so a dialogue would not have been useful. The Bohemia/Moravia effort is underway and the contacts were scheduled in Prague. The Polish Program is based in a Ministry set up for the purpose of defining and executing the privatization process. However the Polish national program did not administer the small retail outlet privatizations but it does administer the development of the capital markets.

Practical Problems: The trips have to be built around the skills and interests of the team members. The availability of the various team members is not always predictable particularly for the team that must travel. The maximal team mix cannot always be achieved. It is most appropriate that the priorities of the technocrats getting on with the program are the transactions and that priority over-rides fact finding trips regardless of their importance. In this instance on neither trip could an appropriate person from the legal department join the team. Similarly in both cases the head of the Active Privatization unit had transaction related activities that forced him to cancel his travel. Related problems when senior people are involved are that Board meetings at which they must be present block out key parts of their schedules.

### Identified Overlaps effecting the team composition:

#### Poland:

- Large Scale Privatization Program
- Enterprise Transformation (regulation) Program
- Public Information Program
- Legislative framework
- Significant donor support
- Role of compensation legislation
- How title issues are being resolved
- Capital Market involvement

#### Czechoslovakia:

- Large Scale Privatization Program
- Enterprise transformation (regulation) program
- Public Information Program
- Small Scale Privatization Program
- Legislative framework
- Significant donor support (on the way)
- Role of compensation legislation
- How title issues are being resolved

#### Hungary:

- Large Scale Privatization Program
- Enterprise transformation (regulation) program
- Public Information Program
- Small Scale Privatization Program
- Legislative framework
- Significant donor support
- Role of compensation legislation
- How title issues are being resolved
- Capital Market involvement

Differences effecting the programs' relative positions that need to be understood that effected team composition:

Poland:

Imminent elections  
Voucher system under consideration  
Role of labor  
Legislative differences  
Excellent progress in retail unit privatizations  
Slow progress in major privatizations  
Direct role in capital market development  
The size of the Polish undertaking

Czechoslovakia:

Imminent elections  
Voucher system apparently in place  
Legislative differences  
Excellent progress in retail unit privatizations  
Slow progress in major privatizations  
The practical effect of operating the program with a  
centralized policy but independent operating agencies  
in two states

Hungary:

A privatization Agency not a ministry i.e. not cabinet  
level  
Relatively small Hungarian manpower and budgetary  
commitment

Actual Polish trip team Composition

Hungarian Team:

Lajos Bokros: Managing Director National Bank of Hungary  
Capital Markets Department, Member of the SPA Board of  
Directors, Chairman of the Hungarian Stock Exchange  
Eathory Laszlo: Director, Investor-led Privatizations  
Department, SPA  
Tamas Tibor: Officer, Active Privatization Department SPA  
Twyman Charles: Advisor, SPA  
Hollo Gyorgy: Advisor on Public Affairs, SPA

Polish Party:

MOC Participants:

Kryzysztof Lis: former Minister of State for Ownership  
Change (MOC)  
Dr. Grzegor E. Domansky: Professor of Business Law, former  
chief legal advisor to Minister Lis  
Kryzysztof Stupnicki: Director Large Enterprise Privatization  
MOC  
Jacek Korpoly: Vice Director Large Enterprise Privatization  
MOC  
Jacek Michalski: Senior Legal Counsel for Small Enterprise  
Program, MOC  
Monika Rajsky: Legal Advisor to the Minister, MOC  
Hanna Weglewsky: Director Public Affairs, MOC

DRT Resource Consultants:

Piotr Cyburt: Consultant DRT Poland

Jan Maciejewicz: Partner DRT Poland

Cliff Dean: Touche, Ross & Co. London, Advisor to the MOC  
on the mechanics of the voucher scheme

USAID Visit:

William R. Joslin: Representative

AGENDA:

Monday 3 June, 1991

15:30-18:00 Briefing at DRT Poland

19:00-22:00 Private Dinner with former Minister Lis. and  
Professor Domansky

Tuesday 4 June, 1991

09:00-12:30 Joint Discussion Sessions

13:00-15:00 Luncheon discussions

15:15-17:00 Individual sessions\*

19:00-21:00 Dinner discussions

\* during the individual session and during much of the morning  
Mr. Hollo was with the Public Relations Department. Mr. Twyman met with  
the USAID representative separately from the Hungarian party.

AGENDA TOPICS:\*\*

\*\* The following items were agreed to be of mutual interest however the  
discussion was free-form rather than structured and was a dialogue between  
equals after some ice was broken.

1. Legislative issues - title, taxes, investment laws, bankruptcy laws, foreign exchange regulations, company law, other regulations. What are the local ground rules how are problems being solved.
2. Advisors - how to locate, terms of reference, good and bad experiences, costs
3. Program designs: Government initiated sales, market initiated sales, small business sales programs
4. Public Relations: programs, advisers, problems
5. Funding of the privatization process: the donor and lending agencies roles, how to deal with them, current trends among donors.
6. Organizational issues: How to equip, staff, organize, train, motivate, pay, manage the privatization process.
7. Longer term coordination opportunities: exchange of documentation, information bank on advisers, donor coordination, exchange of investment opportunity information.
8. Finding capital: capital and money market development
9. Management skills and technology transfer: the prospects
10. Linkages: accounting systems, training, communications etc.
11. Valuation: guidelines and problems.
12. Conflicts: Transparency vs. speed, selection vs. open tender
13. How to deal with Monopolies
14. Labor issues
15. Previous owner compensation



## OVERALL IMPRESSIONS:

### Organizational:

- 1. The MOC has organizational growing pains as it now has over 350 staff from a position of about 35 in September 1991. This is principally a result of the increased political emphasis brought to the program by the new Minister.
- 2. The MOC is tightly compartmented into five major directorates; legal, communications, capital markets, small & medium and Admin., and the Large enterprise program.
- 3. The size of the communications unit 35 people and growing, is indicative of the role that fulfills.
- 4. The capital market responsibility is also in the MOC where that function is separate in Hungary and Czechoslovakia. In a suitably ironic gesture the Poles have housed the Stock Exchange in the former Communist Party Headquarters.
- 5. The Poles decentralized the retail privatizations and the smaller privatizations down to the municipal and district levels and never even considered them in the MOC. The Czechs decentralized it to the municipality level but kept it in the Privatization agency. Hungary centralized in entirely in the SPA due to the basic political power distribution difference between the local and national government.
- 6. The problems of staff training, competitive salaries (a 10X difference exists between private sector finance related jobs and the MOC's salary range), inexperience, and unclear and changing policy guidance parallel to a greater or lesser degree that seen elsewhere.
- 7. There are continuing interministerial struggles on who takes the lead in what privatization effort and in addition the office of the President (Lech Walesa) has its own agenda which makes for an interesting mix.
- 8. The Poles, like the Czechs and Hungarians place a strong reliance on the various laws being passed to support various parts of the privatization process. Those laws are subject to frequent changes and revisions and key ones are still under debate. A definitive snapshot of what is happening has to be based on the most recent revisions and their practical interpretation if that has been accomplished. Thus what is currently observable in the three countries is a dynamic situation and subject to legislated and sometimes surprising defacto changes. The Hungarians appear farthest along legislatively, the Poles are next trailed by the Czechs.

### Substantive:

- 1. The Poles are very sensitive to foreign investment -by which they understand German- and tightly control it. This dramatically effects the pace at which privatization can be expected to go ahead assuming everything else is in order (which they aren't).
- 2. The Polish approach to the compensation issue is still evolving but their basic approach at this point is that if an individual or legal entity lost as a result of a legal act -forinstance a nationalization decree- they are not due compensation even though that decree is now judged inappropriate. This approach will significantly reduce the number of eligible compensation claimants. The form of compensation -in kind vs financial- is still to be resolved. Until this is resolved privatization in some cases will be stalled.
- 3. The pending Polish elections create a requirement for public success of the privatization program. While the retail privatizations are a major achievement it appears political attention has been focussed on the larger units. The voucher system concept is viewed as a public distribution of wealth and a political promise that will be delivered regardless of its utility.

-4. The voucher system (still being reviewed and designed) may well work via every eligible Pole getting a voucher, the vouchers will then be aggregated by Unit Trust like holding companies managed by professional investment management teams (probably western) and the individuals will probably get marketable Units from the trust in return for their vouchers. The avowed purpose is to create instant market interest in exchanging capital instruments, create awareness at the individual level of the mechanisms of investment, bring probably the major 500 operating assets of Poland under the scrutiny of professional investment managers, and let every Pole feel he has a vested interest in the success of the nation's economy.

-5. The Poles to get around the problem of the Worker or Enterprise Council's effective control -in many cases- of State Owned Enterprises (SOEs), have given a central role to the transformation of the SOE (See attached graphic "Privatization Through Transformation") into a corporate form as the first major objective followed by resolution of the actual privatization problem. The poles indicated of about 4,000 SOEs eligible for this program about 150 have been transformed and about 10 then privatized. The goal is to transform about another 1,000 in this calendar year. (Hungary currently considers the transformation "renationalization" and at this point a mechanical process that can be done simultaneously with concluding a privatization transaction however a more broad-based transformation program may be adopted but it will probably continue to be viewed as a procedural step and not a major objective).

-6. The Poles have widely used the privatization principle of getting management/ownership into SOEs on a lease/purchase agreement, speeding the process and reducing the initial capital requirement.

-7. The Poles accept as the norm that workers will participate in individual enterprises at the level of about 20%. Apparently the original enthusiasm for ESOPs as the solution to all problems has faded and a more realistic approach is being taken.

-8. The Poles have a formal program of "Privatization through Liquidation" -refer to the attached graphic- which consists of SOE's selling their assets into corporate forms (liquidating the SOE). This apparently has been a normal route for smaller privatization efforts with about 250 small SOE's sold by this process, 80% to the employees.

-9. The retail and small SOE privatizations were handled at the municipal and local level with no central government role. The transfers were done through a broad range of methods including restitution to former owners, auctions, etc. There was no qualitative information available but it appears clear that process occurred quickly and without major problems. The number of transactions well exceeds 10,000.

-10. The Poles are still grappling with how to prioritize their privatization program and are beginning sectorial approaches while simultaneously deal with individual major transactions. The number of cases they have become involved in directly through their major assets program is about 10 (see attached "Advice for Prospective Foreign Investors", Privatisation Schedule for 1991).

-11. The Poles are grappling, as are Hungary and Czechoslovakia, with the role of the various national players in the privatization process i.e. whether the privatization agency, the office of the President, the Ministry of Trade and Industry, or whoever has the ball. By being cabinet rank the MOC does have a good hearing.

-12. The pace of the Polish program is very much effected by the limited amount of investor confidence in Poland, unattractive and cumbersome foreign investment laws, the strong political position of labor, and the common problem they share with Hungary and Czechoslovakia as regards title issues.

## RESOURCE MATERIALS

"Pole Position, a Newsletter on Privatization in Poland", February, 1991

"Legal Ground for Privatization in Poland" article by Robert Uberman and Grzegorz Spiewak

"Accelerating Privatization in Eastern Europe", Jeffrey D. Sachs, 25 April, 1991

Excerpts "Poland, Privatization and Restructuring Project" World Bank, April, 1991

"Foreign Investor's Guide to Poland", Foreign Investment Agency, Warsaw 1990

"Legal Framework of Joint Venture", Foreign Investment Agency, Warsaw 1990

"2 legal Framework of Joint Venture", Foreign Investment Agency, Warsaw 1990

"Act on the Privatisation of State-Owned Enterprises, The Office of the Minister of Ownership Changes Act" 1 August 1990, Republic of Poland

"Prywatyizacja, lista Firm Konsultingowych" May 1991 (list of privatization consulting firms in Poland) Ministry of Ownership Change

"Law on Public Distribution of Securities and trust Funds" 22 March, 1991 Republic of Poland

"The Law on Economic Activity with the Participation of Foreign Parties/The Polish Foreign Investment Law", Foreign Investment Agency, Warsaw - January 1990

"Advice for Prospective Foreign Investors", undated from the Ministry of Ownership Changes but prepared to cover 1991

"Privatisation Through Transformation", Graphic done by the Ministry of Ownership Change undated but released for 1991

"Privatisation Through Liquidation", Graphic done by the Ministry of Ownership Change undated but released for 1991

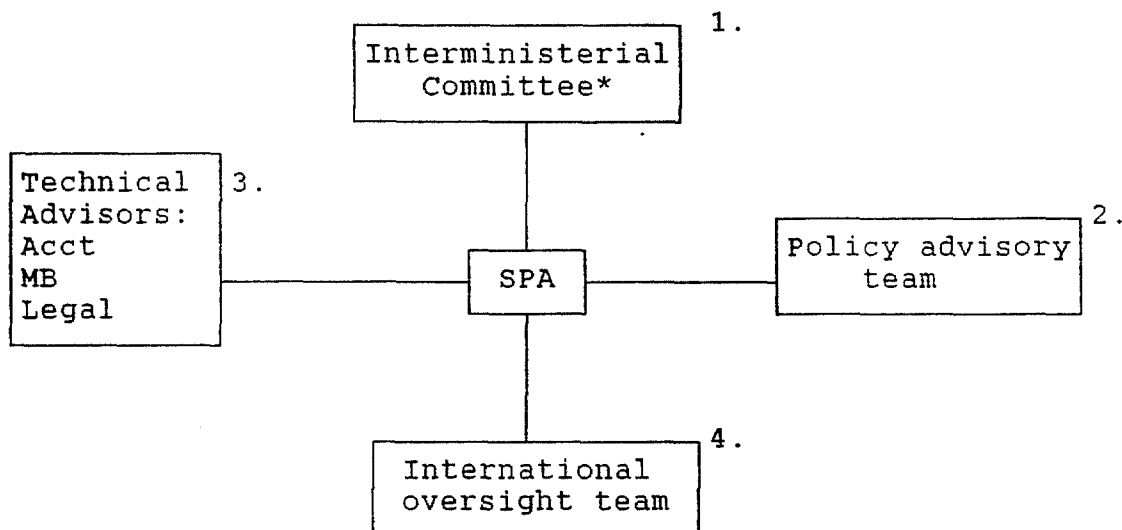
"Privatization of State Enterprises" excerpt from a draft work on privatization in Poland prepared by Touche Ross & Co. as an internal working paper

"Going to Market: Privatization in Central and Eastern Europe", Manual Hinds and Gerhard Pohl, The World Bank, April 1991

## ORGANIZATION CHART

### SPA Overview

TOTAL SPA STAFF: 40



1. Serves the function of the Board until the Board is appointed, This interministerial group can direct and support the SPA as regards individual transactions particularly those of a problematic nature. Some members would not be permanent but would be called in to opine on issues that effected their ministeries. This committee might be a useful alternative to the suggested parliamentary board.

2. This group is a non SPA selected team of Hungarian professionals able to provide the SPA with guidance on day to day policy issue particularly during the initial startup phase.

3. Technical advisors on the key technical areas with which the SPA must be involved; Merchant Banking, Accounting/Valuations, legal matters.

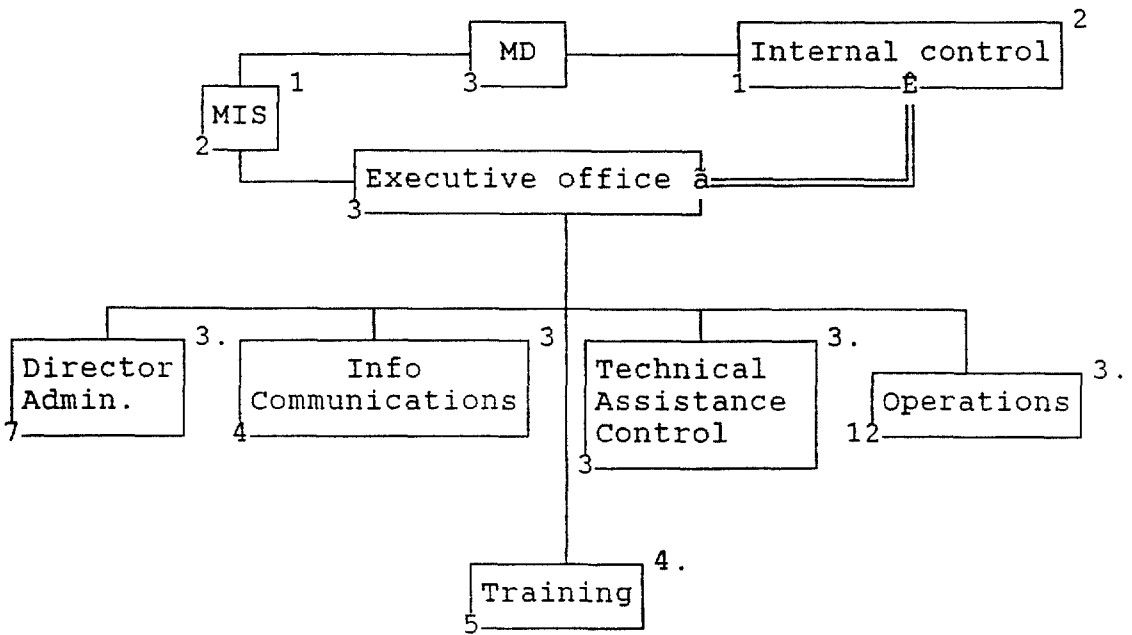
4. An international oversight team may be a useful device which might include members from the IFC, EC, a senior Merchant Banker, etc.

ORGANIZATION CHART

SPA Internal

Staffing  
Summary

MD -	3
IC -	1
MI -	2
EO -	3
AD -	7
IN -	4
TA -	3
OP -	12
	35
TR -	5
	40



1. MI - Management Information System: This office will provide the data tracking and reports required by the SPA and its management, internal budgeting, and special project work in conjunction with other units.

2. IC - Internal Control: This office will advise the Managing Director and the various operational areas as regards their adherence to SPA's internally established procedures and any external rules the SPA must follow. This office will be the liason point for the State Audit office and other external review agencies.

3. These individual units' activities are described in the following pages.

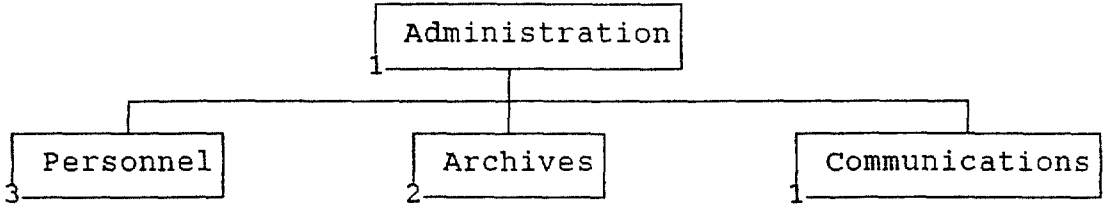
4. Training - At any one time the SPA can expect to have about 5 of its personnel on training and thus unavailable for work in an operating unit.

ORGANIZATION CHART

Administration

Admin  
Staff

Director 1  
Pers. Dir. 1  
Pers. Off. 1  
Sect. 1  
Arch. Dir. 1  
Arch. Sta. 1  
Comm. Sta.  $\frac{1}{7}$  3



Administrative Officer: Will oversee the administrative control apparatus of the SPA to include administrative personnel matters, record keeping, communications, office supplies, facilities matters etc.

Personnel: Will administer pay matters, hiring, training, vacations, and other personnel related matters

Archives: Will maintain the reference library, buyer and seller information files, technical assistance reference materials, working files on privatization matters, Technical Assistance matters, General and Administrative matters, and the Record files on contracts etc.

Communications: Will control and maintain the FAX and Telex operations, the Large copying and binding facility, manage the mail, and the initial data entry of incoming project work.

ORGANIZATION CHART  
SPA Operating Committees

Review  
Current Structure

SPA Policy Committee

Permanent members	Policy Advisory team representative/s MD Executive officer
As required	Director Admin. Information Communications Technical Assistance Control Operations
By invitation	Outside technical advisors, merchant bankers, legal, valuation etc.

This committee would meet weekly, or more frequently as required, to address and deal with internal policy matters and operational policy matters. The MD would make his decisions a matter of record which would become part of the operational procedures and guidelines that would gradually become codified. This would be part of the Administrative officer's responsibilities.

Operations Review Committee

Permanent members	Managing Director (as and when appropriate) Executive Officer Director Operations
As required	Team leaders Team Members handling projects being considered
By invitation	Outside technical advisors, merchant bankers, legal, valuation etc.

This committee would meet weekly, or more frequently as required. The Operations Review Committee will review and approve all the work and recommendations of the individual Operations teams, recommending action for the MD, the Board or other appropriate authority.

ORGANIZATION CHART

Review

Information - Technical Assistance Control

Staff

Director	1
Exec. Asst.	2
Secretary	<u>1</u>
	4

INFORMATION

Promotion of the Privatization Concept and Process

- Privatization Reference Materials
- Sample Documentation
- Sample Checklists
- Promotional and explanatory materials
- Etc.

Press and Public Communications

- Press Materials
- Briefings and Communications activities
- International clipping and review service

Staff

Director	1
Exec. Asst.	1
Secretary	<u>1</u>
	3

TECHNICAL ASSISTANCE CONTROL

- Help prepare funding requests for donor agencies
- Help prepare Terms of Reference for consultants
- Control tendering
- Review bids
- Negotiate Contracts
- Track and help review deliverables
- Maintain records for and make necessary reports to donor agencies



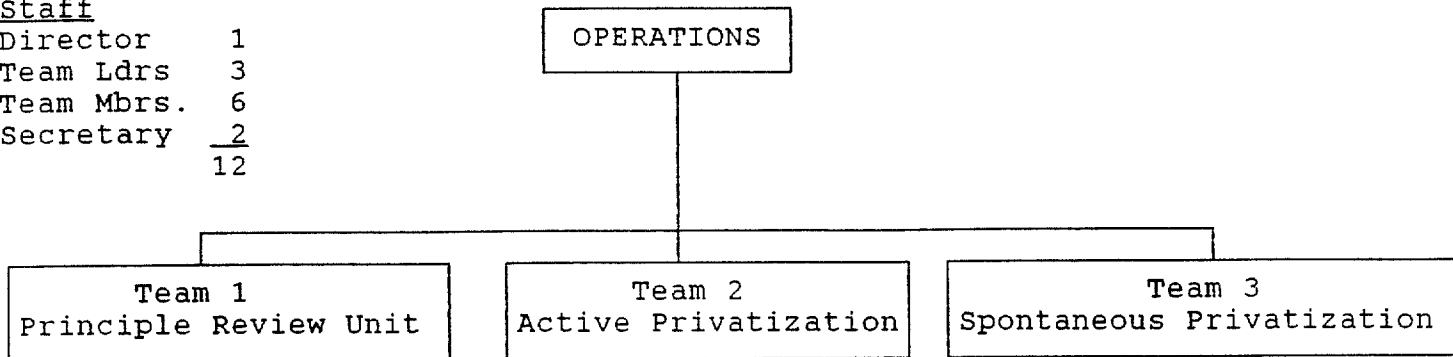
Review

## ORGANIZATION CHART

### Operations

#### Staff

Director 1  
Team Ldrs 3  
Team Mbrs. 6  
Secretary 2  
12



The Operations Unit will support and review actual privatizations exercises. It will have the direct contact with operations being privatized initiate requests for technical assistance, distribute and explain privatization materials, direct technical assistance, review procedures and otherwise support the process of privatization.

#### Team 1 Principle Review Unit

This team's main activity will be reviewing the submissions of organizations requesting approval for privatizations that are being undertaken without significant SPA support.

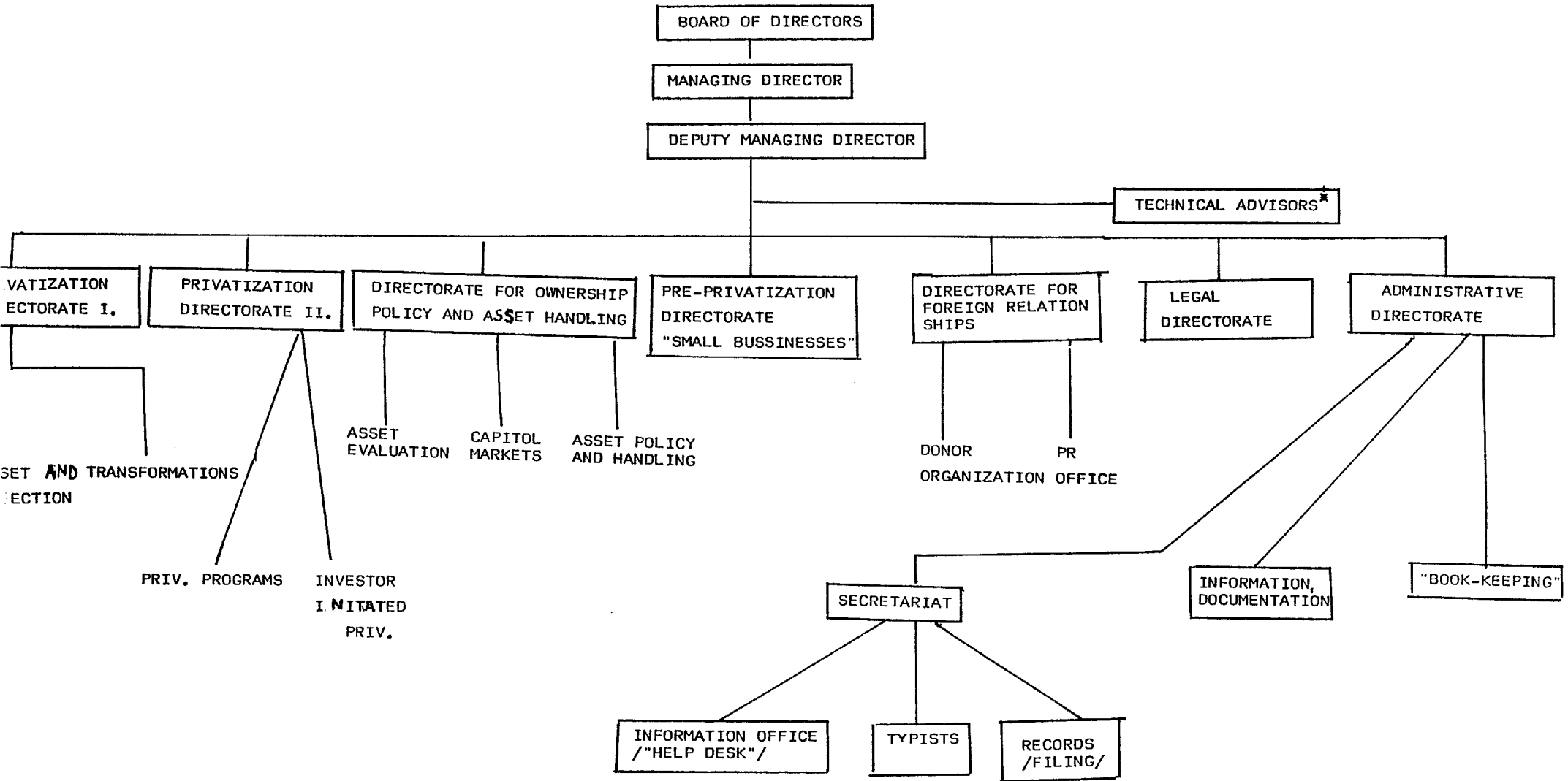
#### Team 2 Active Privatization

This team's main activity will be supporting major privatizations being undertaken with the involvement of the SPA such as the large state owned enterprises.

#### Team 3 Spontaneous Privatization

This team's main activity will be to support and guide spontaneous privatizations.

ORGANIZATIONAL CHART OF THE SPA /1991/



\* Technical advisors: They can be persons or organizations. They are under the supervision of the Managing Director. He decides who do they work for, can be foreigners and Hungarians. They are paid by donor organizations. They have to a confidentiality agreement.

*sign*

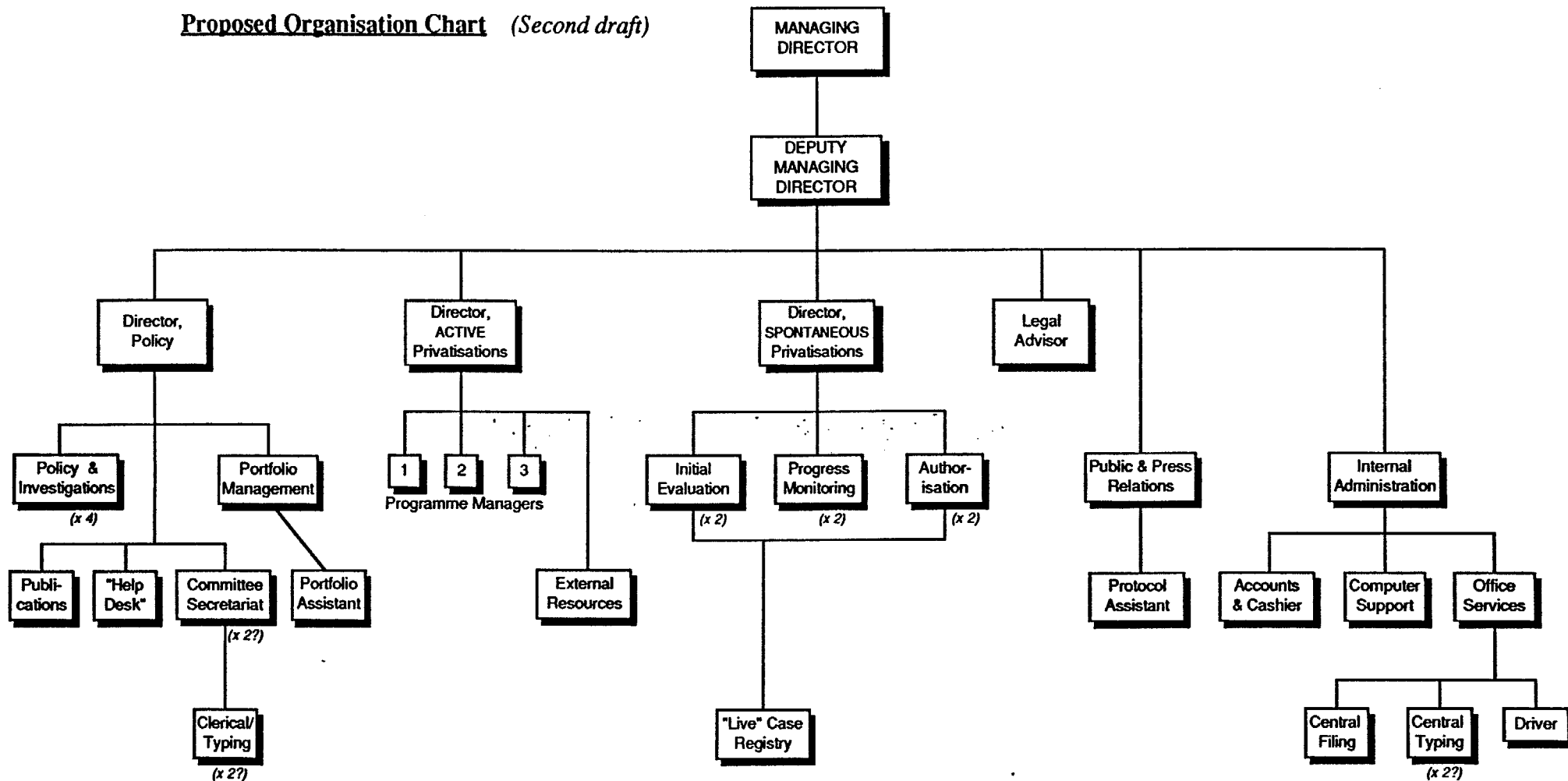
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STATE PROPERTY AGENCY

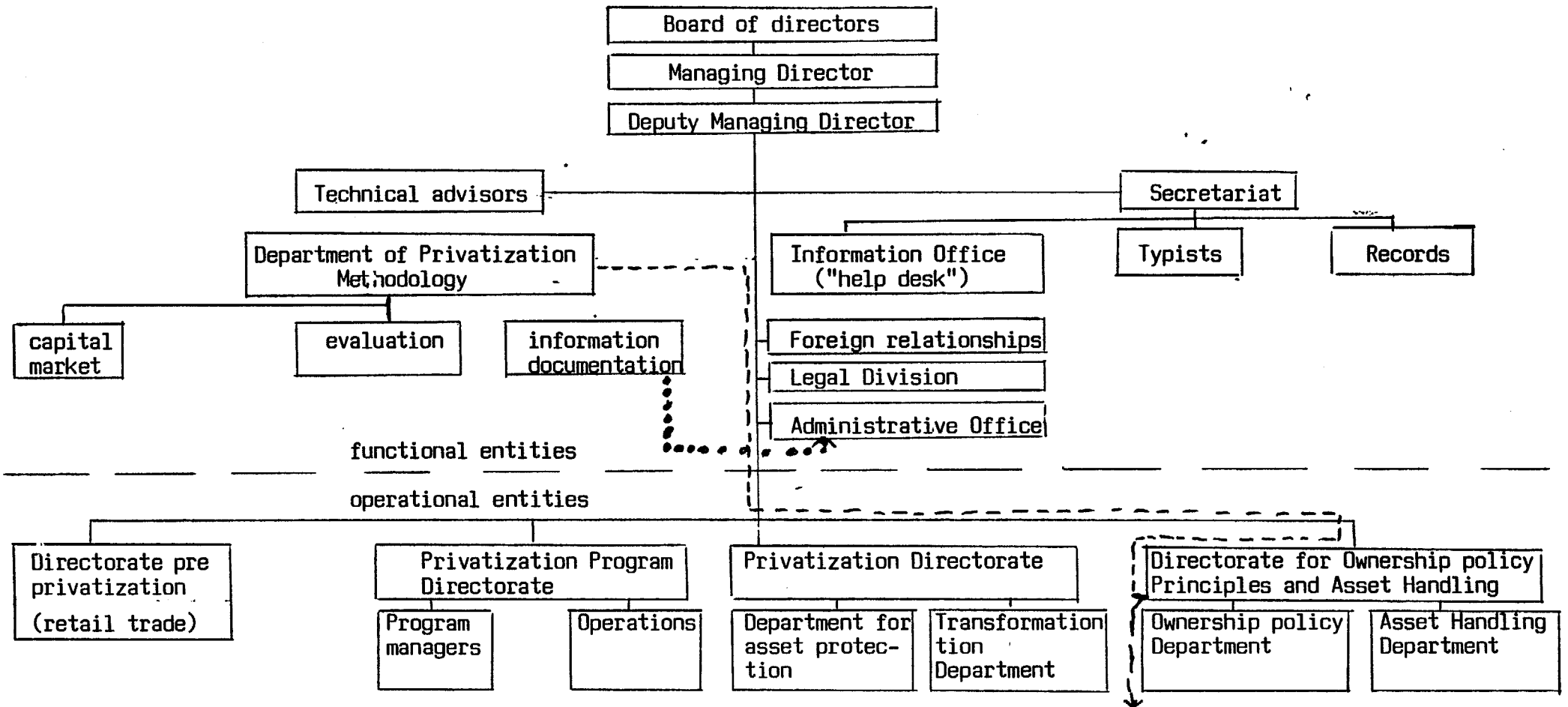
Proposed Organisation Chart (Second draft)

Appendix I



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ORGANIZATIONAL CHART OF THE SPA



MEMORANDUM

TO : Managing Director Csepi Lajos  
FM : Advisor Twyman Charles  
DATE : 28 April, 1991  
REF : World Bank (WB) suggestions in its Enterprise Restructuring and Privatization (ERP) Loan aide memoire

BACKGROUND:

This World Bank (WB) is encouraging the SPA to make a systematic statement of the way it intends to develop as an institution to cope with its many responsibilities. The SPA already has several initiatives underway that address the WB's areas of interest.

MEMO PURPOSE:

At your suggestion I have developed with Lukacs Erzsebet an outline of an SPA institutional development program. If the Board confirms it then we can continue implementation and outline it to the WB and the other Doners. With guidance from you and Karoly we can complete a piece for the WB and the SPA.

BASIC PREMISES:

The SPA must:

1. Be transaction driven i.e. it must be designed to efficiently and rapidly deal with its role in moving the privatization process forward. The SPA's other activities cannot detract from that role but rather those activities must support it.
2. The SPA has an immense responsibility. It must be organized so that it trains, directs, controls, informs, and supports these responsibilities. Its activities in this regard must be exemplary.
3. The SPA is at the forefront of activities being watched and supported by the world development and donor communities. It needs that support. The SPA must be in a position to guide that support and continue to deserve it. The SPA should not be in a position that it responds, it must lead.

ANALYSIS:

In the WB report are three areas of great interest to the SPA.

1. Asset Management:

The WB is supporting the concept of keeping the management and supervisory function for state assets out of the SPA except for privatization related issues. This permits us to streamline our organization as to the role we need to be able to perform. The SPA should retain the power to transform and privatize entities and be able to override ministerial and enterprise vested interests in enterprises but it does not want day to day board and other responsibilities. The detail of how this split is to be done is of great importance to the SPA. A misallocation of powers can bar us from the rapid and efficient privatization action.

Recommendations:

I agree with the basic concept as long as the SPA:

- a. retains its ability to trigger privatization activity.
- b. retains its ability to override "restructuring" or "workout" decisions in favor of clean privatization when the situation warrants.

I have the least knowledge in this area so I will limit my comments.

2. Institution building:

The WB is encouraging the SPA to continue refining its organizational structure to deal with its changing and expanding role. Principally the SPA needs to "clear its decks" so that its line functions can move ahead while its internal support and Administrative efforts firm up. SPA has initiated several activities and needs to signpost others. The WB, like other outside reviewers, put the issue of a strategic plan -with its implementation steps clearly defined- in a premier position in terms of things the SPA must do.

My recommendations are in two areas: A. Organization  
B. Institution building activities

A. Organization:

-I  
I suggest that the SPA have two Deputy Managing Directors. One would handle Operations (Szabo) the other would handle Support (unknown).

-Operations: Would encompass: -Privatization Directorate I.  
-Privatization Directorate II.  
-Directorate for Asset Management  
-Preprivatization Directorate  
-Legal Directorate

Support : Would encompass: -Directorate for Public Information & training  
-Financial Directorate (new)  
-Administrative Directorate  
-Spokesman and liaison (new)  
-Policy

From this structure would emerge:

- a. a major policy Executive Committee: The MD and the Two DMDs.
- b. Two internal director level boards, each one chaired by its respective DMD.
- c. The MD and the two DMDs would be the main management attendees at the external board meetings.

-II

I support the WB suggestion that a small and independent audit and control office be established responsive to the MD, the DMDs and the external board. This small unit would -working with the financial directorate but independent of it- help codify and enforce operating procedures. I think we can get donor support for such an effort.

-III

I feel that Csaba Gelenyi's directorate should only be focussed on the area of Public information and training and that its donor organization coordination efforts be moved into a newly formed Financial Directorate.

-IV

Support

I suggest that a new directorate be formed called the Financial Directorate whose activities would encompass: Donor coordination, supervising and managing donor funds, Planning, Budgeting, Accounting systems, the MIS system (design and control aspects not the mechanical), control, and audit. I suggest that the EC's project management unit, a World bank coordinating unit, and a USAID and other donor coordinating unit report to this director. This office would also incorporate a budgeting and strategic planning unit. I strongly feel that there should be a Hungarian director of donor activity making sure that they are orchestrated. The SPA is multiple funded. It must coordinate and direct those funds as a part of a SPA and a Hungarian national plan. The SPA should not be committed to spend time and resources -regardless of their cost- other than in a way the SPA feels appropriate.

(I attach the resume of a Maria Borda who might be a suitable candidate for the financial director position, I also attach the resume of Gabor Domokos who might be a suitable candidate to coordinate the WB activities.)

-V

I suggest that we designate an internal non-executive Director level spokesman and liaison office whose task it would be to maintain the SPA's links with other ministries and agencies, act as a spokesperson in a broad range of circumstances, and particularly support the investment promotion activities of the SPA in conjunction with the MIER.

E. Institution Building Activities:

Several activities are underway. They can be woven into a suitable document for consumption by our Board, the WB and the other doners.

-Strategic Planning: This exercise, conducted at several levels, external board, Internal Board, and at various staff levels is critical. From it flow, objectives, work plans, job descriptions, training programs. This we should get rolling now. I can get some USAID resources on this quickly if you can help me develop some guidelines.

-training: a. We have funding for a generalized list of activities in the EC budget and we have requested US sourced training funding support from USAID. We should have a consultant in place in the next few days to flesh out a formal training program and a training manual for the SPA.

-Public Relations: all are in agreement the SPA needs a proactive program. We have done a strategy piece and the board called for an action plan which should be presented next week. The Canadian PR person is in place and we are getting part-time support from Sawyer Miller. The EC has approved some funds (ECU 150,000) to support this. We will require considerable more funds, the US has been asked. We are close to the action phase but require more funding.

-Statistics and information availability: The LAN and MIS system development are moving ahead. They should go a long way toward relieving these problems. A coordinated financial and budgeting information system must be designed for inclusion in it by the proposed Financial Director.

-Accountancy and budget control system: A system to accommodate the SPA's increased requirements as the administrator of the proposed major additional EC funding PMU and the needed World Bank funds. We can get donor support for this activity.

-Personnel management: The SPA needs individual job descriptions and a performance review and monitoring system. This undertaking fits into the training strategy task. We can probably get such a piece of work funded.

-Management of foreign advisors: The WB highlights the absorption problem we will shortly have with foreign advisors. The practical problems relate to physical issues like office space, equipment support, secretarial support. There should be some formal time spent defining policies on foreign advisors and expectations of them. The SPA must maintain control of the advisors not the reverse.

I suggest that this issue be discussed on a policy basis as a separate topic.

-Space: If we undertake to reorganize ourselves and are planning to input additional senior and support Hungarian staff and several foreign advisors, we need space in this building. I know this is easier said than done.

-Equipment: computers and similar equipment we can get funded you know the lead time problem but we have quite a lot underway presently.

-Code of Conduct: I believe we can quite quickly get funded and developed a code of conduct for SPA staff. This is a major training and public image effort.



-Staff: I can probably get technical assistance in the form of trained personnel in the Finance area to support a Hungarian Financial Director. They may have a Forint cost component of about HF25,000 per month each. This technical support would be in addition to myself. We need to discuss this. I attach the resume of one good possible Hungarian candidate for the financial director slot and the resume of a support person to specialize in world bank issues. I have no leads on a second DMD.

-Training: We have the EC budget, we have some USAID funding, we hope to formalize a program in the next few weeks. Some things are already underway.

### 3. Financial Management:

The WB highlights the need for an SPA Chief Financial Officer. The SPA, unlike most other government ministries and agencies, has a major role in obtaining and managing significant amounts of funding derived from several sources. In this regard it is more like a major private company than a government entity. For this reason it should use private sector financial management tools to deal with this situation.

#### Recommendations:

1. The SPA's requires a knowledgeable Hungarian Director to head this function. Hungary wants to be controlling this phase of the SPA's activities. The functions of this office overlap several of SPA's critical needs: Strategic Planning, information, control, budgeting, and donor relations. I attach the resume of Maria Borda as the type candidate who might well fill that position.

2. The office will need to coordinate the SPA's administration of its various funds: EC, WB, USAID, Government of Hungary and other. As currently envisaged the SPA will be managing and dependent on renewing and restructuring US\$50-US\$80 million a year.

a. You have an EC PHARE coordinator and it is recommended that that office be expanded into a Project Management Unit in the next PHARE budget cycle.

b. We need a World Bank Coordinator. I attach the resume of Gabor Domokos who might be a suitable candidate.

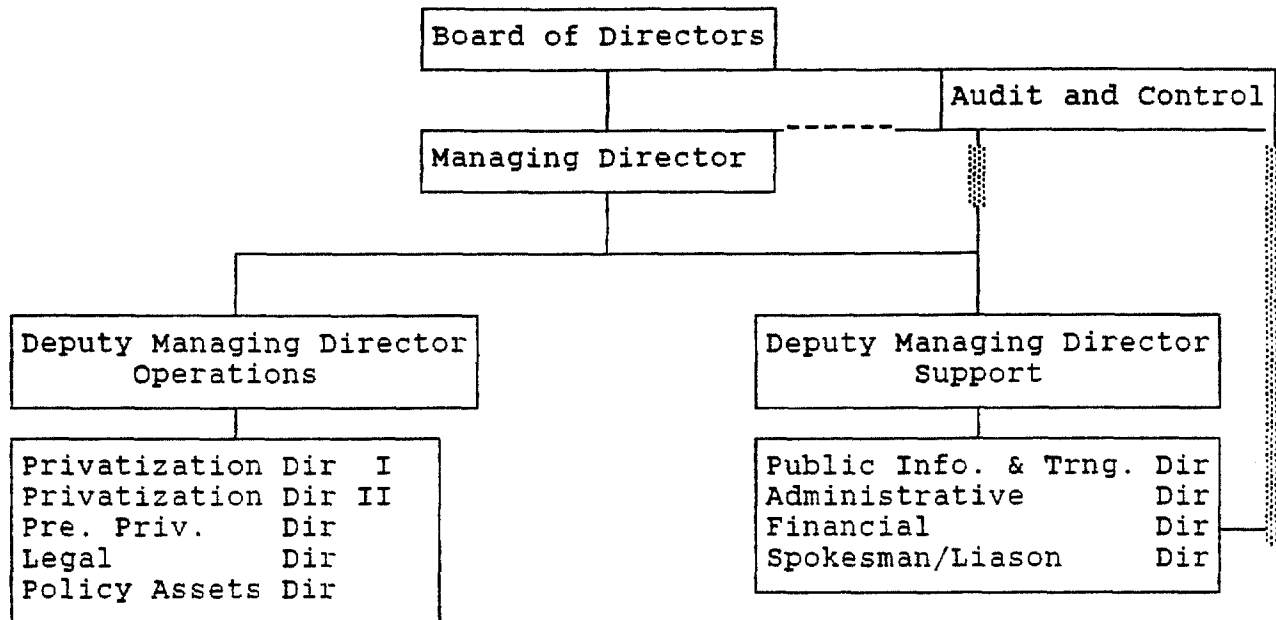
c. I can deal with USAID coordination

d. Fejesne Pecsí Eva manages the Forint activities well

3. I recommend we seek additional support to get that office started in terms of a trained treasury/ budget control person. I think we can find one. We can get technical assistance to help with accounting and other systems.

Review

Organization Chart  
State Property Agency  
29 March, 1991



Operations

Privatization Dir I : Asset & Transformation protection  
Privatization Dir II : Active Privatization Program  
Pre-Privatization Dir : Investor Initiated Privatizations  
Legal Dir : Small businesses  
Policy and Assets Dir : Legal support to the various programs  
: Asset Evaluation  
: Policy  
: Capital Markets  
: Asset Management

Support

Public Info. & Trng. Dir : Public Relations  
: Training  
Administrative Dir : Secretariat  
: Typists  
: Records/filing  
: Personnel  
: Information/documentation  
: Book-keeping  
Financial Dir : Donor Coordination: EC, IBRD, USAID and other  
: Planning  
: Budgetting  
: Accounting Systems  
Spokesman & Liason Dir : Government agency liaison  
: Spokesman

Audit & Control

This office shall be responsible for helping define and enforce policies and procedures. The office will report to the Board and the Managing Director and will work particularly closely with the financial director's office.

Budapest, 31 May, 1991

MEMORANDUM FOR EC

Subject : Privatization in Hungary

SUMMARY: The Hungarian privatization program has been in place just over one year. It is designed to be market driven, Government supported and Government regulated. Its objective is to focus the private sector's more effective resources; management, technology, capital, on the assets of Hungary. The goal is to rapidly increase the economy's efficiency. Hungary is particularly sensitive to increasing the productivity of its economy quickly due to its heavy per-capita foreign and domestic debt service requirement. The privatization program is pragmatic and learns as it goes. It is transaction and reality driven not ideology and regulation structured.

The formal program is overseen by the State Property Agency (SPA). The program has four major components. These components in conjunction with the new Foreign Investment law, Company and Transformation acts, revised tax and accounting regulations, bankruptcy laws, upgrade of the financial system, and particularly the government's policy of cutting subsidies to state owned companies and other changes are helping transform the economy. It is clearly recognized that while the privatization-led regeneration of state owned assets draws much attention, that the economic future of Hungary significantly lies with newly forming operations outside the program.

Key Statistics:

- The Government's objective is to have over 50% of the control of production (not number of firms necessarily) in private hand within 3 years.(from a 90% control starting point)
- Less than 400 enterprises account for 85-90% of industrial production and 75-80% of manufacturing employment
- The Active and Regulatory program involve about 2,200 enterprises
- Active Program: Presently is reviewing over 134 enterprises
- Regulatory Program: Has approved over 151 transactions
- Retail Program: Involves approx. 10,000 units, 151 sold
- The Portfolio Management Program: Will become significant, its first 5 company program is in the market

update

1. The Regulatory Program (Spontaneous Program):

Established in response to real and perceived abuses in the "spontaneous" privatization process, the SPA's activities in this area are its core activity. Hungary's privatization program relies on stimulating the market but the SPA must try to establish and maintain a fair market environment. In addition the SPA acting on behalf of the owner, the people of Hungary, have an interested right in reviewing the value (price, competitive effect, and interests of the nation) of each transaction. The balance the SPA as regulator and owner's representative must strike is to keep the market fair and active without stifling it with bureaucratic procedure. There is no regulatory or procedural preference as regards the percent of the asset -if any- to be left with the State, rather each transaction is reviewed on its own merits. The Lehel case where the SPA insisted Electrolux (the foreign investor) take 100% is a case in point.

-This department has approved 180 transactions: with 95 in process (See Annex I for details).

Status: Conducting its regulatory activities in two basic areas; changes in ownership and the transfer and sale of assets, the regulatory arm of the SPA must review the transfer of the ownership of assets through both the transfer of shareholdings and the actual sale of major assets. The first principally involves price and competitive issues while the second must be alert for asset stripping and "sweet heart" deals. The transformation cases to date have involved book values of over HUF 111 billion Forint with over HUF 150 billion Forint in transactions under consideration while the asset based transactions have involved over HUF 6.3 billion Forint.

Financing: With only occasional statutory requirements to get second valuations and obtain legal opinions this unit has less financing needs than the active unit. The EC/PHARE 3 mil. facility supports this need, and more is on request. There is a possibility that USAID will grant some small assistance in this area.

Operational lessons learned:

- a. Striking the balance between being a regulator without impeding the privatization effort is difficult.
- b. There is no way that all "inequitable" transactions can be stopped as every transaction has losers.
- c. Lack of knowledge of how to proceed (within enterprises and within the SPA), lack of good data, and inexperience at the enterprise level is a greater impediment to moving privatization ahead than outright attempts at fraud.
- d. The scale of what is being attempted creates bottlenecks in many areas, valuation, the company registry office, within the SPA, in legal advisors offices, etc.

2. The Active Privatization (State Property Agency Lead) Program:

Designed to confirm the Government's commitment to privatization, break new ground, establish market precedents, handle large and difficult transactions, and focus some of the worlds best professional skills on major transactions, this program is now maturing.

The department currently has 134 enterprises either in or projected for inclusion in its formal programs. The program will continuously take additional enterprises into the program to the extent the enterprise don't make privatization progress independently.

Status: The Program was launched with its First Privatization Program (FPP) consisting of twenty companies in September, 1990. All of the FPP are scheduled to be in the market by the 2nd. quarter of 1992. It is noted that Pannonplast is already officially being marketed, IBUSZ's launch is awaiting the right market time, and Danubius is targeted for September. The privatization methods range from a mixed public and private placements in Budapest and Vienna and elsewhere (Ibusz, Pannonplast), management buyout (Tritex), sale (MEH Troszt), and various admixtures including ESOPs and liquidation as appropriate.

The Second Privatization Program (SPP) was launched in March, 1991 three months later than expected. Three other sectorial programs are currently under review.

Non program sales, expected to be more the norm rather than the exception, proceed as need and market reality dictate. The Lehel/Electrolux, Chinoin/Sanofi, Gundel, Oberoi, Videotone and other transactions have been most noteworthy.

Financing: FPP-World Bank (US\$10.5 mil.)-, EC/PHARE ECU 3 mil. both are anticipated to give additional support to this, the major funding need of Hungary's privatization effort. Some contracting problems are being encountered. They are gradually being dealt with but they are delaying the program.

Operational lessons learned:

- a. Valuations, among the other necessary pre-sale steps, take more time than originally anticipated
- b. The requirement that local authorities be paid with shares for the value of the land of operations being privatized within their jurisdiction is creating problems. Frequently the future owners won't accept the local authorities as shareholders and want to pay them out instead.
- c. The Investor Initiated Privatization program as been launched as a subsidiary of the Active Program in recognition of the frequent need to focus SPA support on both investor and enterprise needs in major transactions. This special unit was found to be needed to signal investors and the enterprises that the Government intends to vigorously support market initiated transactions.

3. The Retail Program:

Designed to deal equitably with the approximately 10,000 small retail operating units under government control throughout the country. This program's objective is to quickly privatize the units through means of public auctions. Assigned to the SPA as a responsibility in September 1990 the first auctions were held in March 1991.

This department has conducted 260 auctions to date since 6 April 1991 and sold 151 units with a yield of 593 million Forint. Its target for 1991 is 1500 units sold.

Status: The program is decentralized by assigning the packaging for sale of the units to private contractors with the auction rules and reserve price set by the SPA. The results to date have been disappointing as the reserve prices have apparently been higher than market perceptions of the unit's worth -particularly as we are selling only short term leasehold rights on locations as the underlying property is not being sold with the facility-, the bank financing mechanism designed to assist the purchase of such units is not fully functioning, and the process has been too rigid. Title issues and uncertainty created by the still-awaited passage of a Compensation Act have compounded the problems.

Financing: As the auctions and sales are run on the principal of success fees, the direct costs of this program are low. The EC has made its principal support felt through helping finance equipment.

Operational lessons learned:

- a. Market prices and valuations do not always coincide ]
- b. Inflexibility in a market environment (auction) means limited sales. ]
- c. A weak financial infrastructure means insufficient funds for purchases much less inventorying etc. and thereby limits sales. ]
- d. A limited public awareness campaign means limited public interest. ]
- e. Short term leasehold rights to sites creates great uncertainty for buyers. ]

#### 4. Portfolio Management:

By law the SPA becomes the named shareholder of any enterprise transformed into a legal entity form. Also by law the SPA cannot directly manage its ownership position except for an interim period and must turn to professional managers. The different roles portfolio/asset managers will be called upon to play range from that of a simple registrar through unit trust like operations of various descriptions, investment trusts with management objectives, decentralized privatization exercises, and finally work-out and liquidation companies. In order to address this issue the SPA has launched its first Portfolio Management Program. This Program calls for portfolio managers to bid for the management of pools of the SPA's asset holdings. While Government policy is not yet settled as to which assets the SPA will continue to have responsibility for putting under management, it is clear that this program will become significant.

This unit has placed its first 5-asset package in the market and is working on the 2nd. 8-asset package.

Status: The outline of the program has been announced. The terms of reference (TOR) for the initial 5 companies to be put under management has been announced. This TOR in this instance is calling for a manager to step in and manage the 5 companies toward privatization with a significant success and failure sharing between the management company and the SPA.

Financing: This program is at its initial stages and limited financial needs have been identified. As the success fee approach is being taken (if it succeeds) little financing will be required except for program design, legal documentation preparation, and legal follow-up.

#### Operational Lessons learned:

- a. The analysis to date indicates that this will be a complex program that will have significant segment design needs.
- b. Government clarification is required as to precisely what portion of the assets that the SPA holds it must manage.

#### ATTACHMENTS:

- I Data: The Regulatory Program
- II Data: The First Privatization Program
- III Data: The Second Privatization Program
- IV Data: The First and Second Portfolio Management Programs

# State Property Agency

This annual report covers the activities of the Hungarian State Property Agency from its inception March 1, 1990 until May 31, 1991.

August 1991.



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## Introduction

Passed by the Parliament in late 1988, the Transformation Law and the Companies Act made it possible for state owned enterprises to reorganize themselves into new, western-style company structures. Originally known as "spontaneous" privatization, this situation was considered an essential, if imperfect, method on the route to a decentralized, market-driven economy. Anxious to continue the process of creating ownership operating at risk, the government understood the need to regulate the process in order to prevent abuse, as well as to create a structure that would be fair and reliable. Real privatization, meaning the passing of state owned property into the control of private investors, would follow.

The crucial legal framework establishing the system of privatization in Hungary is contained in four laws – the Transformation Law, the Companies Act, the Law on the Protection of State Assets and the Law on the State Property Agency – as well as the Property Policy Directives. The role of the State Property Agency (SPA) is, not surprisingly, central to the entire process. With the creation of the SPA, the activities of the state as both proprietor and public authority were separated, creating the possibility for the commercial tasks of a state agency to be carried out far more efficiently.

The Hungarian economy, operated for decades as a centrally planned command economy, is confronted with enormous practical problems directly effecting the privatization effort. There is essentially no capital market to speak of, there is substantial internal and external debt to contend with, and there are still important political changes to be considered. To promote a radical change in the economy's ownership structure at a time of dynamic change in other parts of the economy and society requires vision and great determination.

Time is of the essence. The framework created to establish and nurture the development of a market economy will only be successful if genuine private ownership begins to take hold of a continually growing share of the economy. To this end the SPA has supplemented the original "spontaneous" privatization with a variety of methods designed to attract the widest possible interest in the Hungarian restructuring. In order to gain the attention of foreign capital and to better coordinate the interests of the state and its state owned enterprises, it organized the so-called "active" privatization program. Investor initiated privatization makes it possible for potential investors to put a state owned company "into play"; the SPA has also worked out a model for "self privatization" a process that doesn't require the direct participation of the state. In addition, the privatization of the retail trade (preprivatization) and systems allowing for more efficient handling of assets remaining in state hands were introduced.

The existing legal framework – including a new constitution, the laws governing the privatization process and legislation regarding the transition to a civil society – helped to create an overall context for privatization, making it a significant part of a larger whole. Among the primary aims are to create a social market economy, to achieve a dramatic transformation of the country's ownership structure, to inspire the creation of a powerful stratum of entrepreneurs and a middle class on the basis of economic freedom. The strengthening of company structures that serve the interests of working people and the development of economic units and systems operating under conditions of real ownership should result as well. In accomplishing these goals Hungary would help further the internal development of the country, broaden international cooperation, improve living standards, and provide the means for a higher quality of life.

At the moment the Parliament has before it proposed legislation intended specifically to provide assistance in achieving the concrete aims of privatization. These aims include the introduction of both foreign and domestic capital, new technology and expanded market opportunities; the benefits of participating in the mainstream of the global economy; the transformation of company structures and the end of market restrictions; the creation of 'real' jobs; and the spread of modern management techniques.

The role of privatization within the overall restructuring of the Hungarian economy and society is well known and has been much commented upon. This is described to a certain extent by the relevant legislation which addresses itself to organizational and procedural aspects as well as defining the SPA's authority. This Annual Report then seeks to give an account of the first year of the peaceful revolution known as privatization, the results until now and the extent to which declared aims have been accomplished.

There is no doubt that the pace of privatization has not been quick enough when compared with expectations generated by Hungary's relatively fast political transformation. Under these circumstances it is not surprising that a considerable amount of the criticism has been levelled at individual companies, ministries and, especially, the State Property Agency and the government in general. The force of such criticism, however, must be harnessed for the sake of improving the process. This also applies to the experience gained in the actual practice of privatization up to now, the process of "learning on the job". Some issues, of course, require further legislation and decisive action on the part of the government.

In spite of some shortcomings, however, it must be said that the first year of the Hungarian privatization showed results that are significant even by international standards, and that both the mechanism and the direction of privatization are healthy. A great deal has been accomplished since privatization began. This is detailed in various parts of the Annual Report, but nevertheless it would be worthwhile to consider a few examples from the outset. The SPA, for example, took part in developing the legal procedures concerning its work; it has developed a viable organization; training in privatization and related issues has been organized for its staff; it has worked out the various methods of privatization; it has built up relationships with companies, banks, ministries, arbitration organizations, foreign privatization and investment institutions, domestic and foreign consultants and with the world's biggest investment banks. All of these accomplishments have long term significance, yet had to be completed "up front".

Some of the figures on the performance in the first year show the following: 160 cases of company initiated transformations, 213 companies requiring property protection procedures, 150 companies involved in the active privatization programs. This amounts to more than 500 companies involved in privatization with a collective value exceeding 400 billion forints (approximately \$5.33 billion). It's true that only a small part of this has been completed (approximately 160 companies), but this too is indicative of the enormous complexity of the process.

The restructuring of large companies, for example, can involve as many as 50 or 60 constituent units, property in the domain of a dozen or more local authorities, a staff of several thousand, complicated employment issues, an extensive system of international relationships and obligations related to servicing bank credits and debt, all of which must be satisfactorily resolved in order to complete the transformation of ownership. That the process often involves months of intense negotiation should come as no surprise.

Even within this environment, however, the number of successes is hardly insubstantial. Some examples are: the announcement of 1000 auctions in the pre (i.e. small) privatization process since April of this year alone; the privatization of 250 companies initiated by foreign investors; the taking of 48 companies under state administrative control for the purpose of ensuring maximum results from their privatization; and the downtown office building program involving 12 prime buildings. Furthermore, hundreds of consultants, representing important western banks, accounting and law firms have shown an interest in the Hungarian privatization process. These, in turn, make up only a specific part of the more general interest shown by foreigners.

The results of privatization thus far, rather than hiding the many drawbacks encountered, on the contrary, make them obvious. Furthermore, these practical difficulties require solutions, a situation where the SPA is well positioned to make a contribution. Various parts of the report point to symptoms related to the growing pains of privatization. They also point to steps that should be regarded as nec-

essary in the interest of accomplishing the government's privatization strategy, including potential solutions based on new legislation.

## **1. Characteristics of the Privatization Process**

### **1.1. Company Initiated ("spontaneous") Privatization**

According to the relevant laws, company initiated privatization of state owned assets may take place in one of two ways. It is possible that the traditional company may be transformed into a limited company as a single unit and then, in a second phase, be sold either in parts or as a whole. Alternatively, it is possible that part of the property entrusted to state companies may be used to establish, generally by way of foreign participation, a limited company. In either case the SPA acts both for the sake of promoting privatization of state property and to insure that the aims of the company and the national economy are fulfilled.

#### **1.1.1. The Transformation of State Owned Companies Into Limited Companies**

Since the establishment of the State Property Agency on March 1, 1990, the transformation of 160 state companies into limited companies has been initiated. The value of the state property involved in this process is 237.6 billion forints.

Through March 31 of this year, 40 transformations were completed. The commercial value of the transformed companies exceeded the value of their predecessors, as reflected by traditional accounting methods, by 58.4%.

According to the financial accounts of the transformed companies, revalued property exceeded 70 billion forints. The proportion of shares retained by the state is 64.2%, while that of foreign capital is 19.6%. The transformations which have taken place up until now have primarily involved small and medium sized companies in processing industries (sugar refining, brewing, tobacco, road building, etc.).

1991 has thus far seen an acceleration in the process of transformation. While 27 transformations occurred during nine months of 1990, 13 took place in the first three months of this year, and 15 more have been carried out since then. The number of cases in progress shows that the process of transformation is being utilized by a constantly growing number of firms. This cannot, however, hide the fact that the great majority of state companies (nearly 2000) have made little attempt to use the legal framework that allows them to exercise significant judgement over the future course of their enterprise. As a result of this, demand arose for additional forms of privatization aimed at accelerating the process (an issue that will be dealt with shortly). In the majority of transformation cases in 1991 the introduction of a strategic foreign investors is involved; the proposed foreign shareholdings have called for a minimum 30% stake in every case, a higher figure than was previously the case.

The selection of foreign partners takes place on the basis of either open or closed tenders. Competition is necessary in the interest of observing and controlling the privatization, as well as to allow the market to best assess the value of companies given the current circumstances.

The main criteria for judging offers is the opportunities the prospective venture will create regarding the asset in question and the economy as a whole. Competitors for the assets therefore should focus on a strategy that provides dynamic answers to the questions that face many Hungarian companies. These would include the establishment of financial stability, the introduction of modern technology and securing long term market prospects. An understanding to undertake employment obligations or a willingness to engage in new activities are further advantages in this respect.

The organization of competitive tenders has been a source of conflict in many cases. Many potential foreign investors believe that participation in competitions is an unnecessary complication and many claim that the process wastes time. It is true that the selection of partners by way of competition draws out the transformation process; it is also true, however, that substantially better conditions are usually achieved as measured against the original offer (sometimes more than twice or three times the price). In any case, the average time needed in order to reach a decision has been only 2.2 months in the transactions completed so far.

On occasion the organization of competitive tenders can bring to light conflicts of interest between (state) company managements and state property. Management's priorities are usually to get the privatization completed quickly, without complications, and with their positions held safe.

An increasingly frequent source of tension in the course of preparing transformations is the size of the shareholding due to local authorities. Although clearly the decision regarding the proportion of property to be assigned to the district council is the responsibility of an independent property valuating organization, occasional difficulties in getting acceptance on this point can add weeks to the time required for the preparation of contracts. In addition, some prospective new owners express reluctance in accepting local councils as co-proprietors.

The State Property Agency rejected 12 transformation proposals. The primary reason behind these rejections was to ensure that these companies would not be able to withdraw their businesses from the jurisdiction of the preprivatization law. In one or two cases the reason for the rejection was the disorderly financial situation of the company; the need to prevent a transfer [of monopolistic position] to the private sector has occurred as well.

#### 1.1.2. Property Protection Cases

The Law on the Protection of State Assets states that the sale of any part of state property, or cases involving taking such property into a limited company, should be communicated to the SPA beforehand. The agency may then supervise the sale of the company in question and may disallow the proposed transaction.

The State Property Agency examined 213 transactions within its authority and reached a decision in 153 cases. It approved 129 approved the transaction, 24 cases were rejected and 60 are in the process of being decided.

The most typical arrangement is a partnership, with the company's existing assets taken into a limited company as contribution in kind. In almost two-thirds of the approved cases a foreign partner is participating in the company. However, it should be noted that in 1991 the proportion of new companies brought into being with Hungarian partners increased.

There is also a majority domestic shareholding in the companies established with foreign participation. The accepted business value of the properties taken over as contribution in kind amounts to 21.6 billion forints. This is against 13.1 billion forints according to the original book value. These figures show that the devaluation of state property can be avoided thanks to the exercise of provisions in the legal framework.

The State Property Agency rejected transactions involving company initiated sales of state assets in 14 cases (the sale of shareholdings or of real estate, etc.). The majority of rejections sought to prevent companies from exploiting state property (usually valuable downtown buildings) in an attempt to solve financial problems resulting from their adjustment to operating under market conditions. Approved cases generally called for constructive utilization of income for the purpose of company restructuring and adjustment to the demands of the market.

## 1.2. The ("active") Privatization Programs

In addition to the requirements of the state property protection law, the State Property Agency, from the summer of 1990 and in accordance with the tasks prescribed by law, began to initiate company privatization. The aim of these so-called 'active' programs is that with the active influence of the state, to facilitate in a systematic way the acceleration of privatization, attract new circles of investors into the Hungarian economy, establish better coordination of state and company interests, and to build up a 'culture' of privatization in the widest sense. Active privatization obviously goes hand in hand not only with all of these goals, but it indirectly furthers the process of company-initiated privatization as well. The idea that "if we don't privatize ourselves someone else will," became a significant stimulating factor in Hungarian business circles.

Due to the wide publicity of the programs, opportunities became available not only to Hungary's traditional trading partners, but to investors from all over the world. Many of these may not have considered Hungary an appropriate investment opportunity previously; changing that mindset is but one of the aims of the active programs. The relationship that is being built up between the SPA and various responsible ministries helps to guarantee that privatization will increasingly become an organic part of policy efforts affecting different parts of the economy. The actual work of developing and implementing a privatization strategy, utilizing domestic and foreign consultants, should ensure that the growing number of participants are exposed to privatization theory and practice in developed market economies.

As of May 1991, three programs and two sector-specific privatization efforts, coordinated in the manner of programs, were initiated by the agency. Within this framework approximately 150 companies, with a value of some 160-170 billion forints, have been transformed.

### 1.2.1. The First Privatization Program

Announced in September 1990, the program comprised 20 of the larger and generally better performing companies in the country and represented a wide cross-section of the national economy. The voluntarily registered firms had an annual turnover of approximately 100 billion forints and assets of 70 billion forints.

For the privatizations of these companies the State Property Agency sought international consultants with substantial privatization-related experience. This was accomplished by publishing the conditions of the open competition for the 20 companies' advisors. Approximately 300 offers were received, most representing interest on the part of the world's best known investment banks.

Ultimately, consultants were selected by the SPA's Board of Directors and its Managing Director based on the recommendation of committees whose membership included representatives from the privatizing company, the relevant ministries, the National Bank of Hungary and independent experts. The consultants, after close examination of the companies, gathering the necessary documents (financial accounts, financial and business plans, etc.) and making a presentation to the State Property Agency, then make recommendations regarding the most advantageous method for attracting foreign investment.

The implementation of the program generated income for the state of approximately 30-40 billion forints, a significant proportion of which was in convertible currency.

### 1.2.2. The Second Privatization Program

The Second Privatization Program is intended to articulate the organizational, financial and legal conditions of the so-called "shell" companies, as well as the enforcement of the state's ownership interest. A significant part (at least 50%) of the property of these companies has, in the past few years, been transferred to limited liability companies. The role of the head office of the original company –

having passed on its traditional functions – is confined to that of trustee. The loss of state property exists as a real danger therefore, as a result of potential losses on the part of the limited companies.

Twelve companies were introduced in the first phase of the program. This group of companies disposed of assets totalling 14 billion forints and more than 115 limited companies. Relying on domestic consulting organizations, professional committees, with the direct participation of the relevant ministries (Trade and Industry and Agriculture) examined the realistic privatization potential of companies belonging to the machine and light industries. The primary aim was to bring about sales to investors operating in the same industry; in cases where this could not be accomplished, the agency recommended liquidating the head office of the company in question. Where a successful privatization is anticipated privatization is expected either at the end of this year, or early next year.

### **1.2.3. The Coordinated Privatization of State Agricultural Companies and Limited Companies Operating In the Wine Producing Sector**

The goal of these privatizations, as established by experts from the Ministry of Agriculture, is the modernization of the most important companies in this sector. It is hoped that with the participation of investors from the same industry, the financial situation of the 15 companies involved can be improved dramatically. It is also hoped that the quality for their products and their market positions may be enhanced as well. Of special significance is the integrated development of agricultural production. This privatization program was introduced in May 1991 and the invitation for foreign investment should take place in the second half of this year.

### **1.2.4. The Construction Industry Privatization Program**

The aim of the Construction Industry Privatization Program, initiated in the spring of this year, is to facilitate the adjustment of these companies to the most significant changes in the market. This will be accomplished by creating a system of small and medium sized companies, technologically better equipped and with a more manageable structure than those now in existence.

The program will respect the preparations for privatization that the companies have already put in place. Based on negotiations with the company managements, the relevant ministries and trade unions, consultants are preparing privatization strategies. The pace of implementation is changing, however, and actual privatization is now expected in the first few months of 1992.

### **1.2.5. Companies Affected by the Collapse of COMECON**

Due to problems related to the dramatic decline in Soviet-Hungarian trade, the SPA endeavored to accelerate the privatization of a group of companies suffering serious consequences. The Ministry of Trade and Industry, in response to a request from the State Property Agency, made possible the accelerated privatization of 15 companies. The Agency asked eight well known investment banks to examine the situation of each company and to gauge whether or not the companies had a realistic opportunity to attract foreign investment.

In the case of four companies the foreign advisors could not foresee the successful introduction of foreign investors. An attempt to attract foreign investment is under way with regard to seven companies, with results expected in the autumn. The privatization of the remaining four companies has been rejected.

## **1.3. Preprivatization**

Enactment by the Parliament of Law LXXIV of 1990 specifically regulates the privatization of the retail, catering and service industries. In accordance with this law, all the economic activity characteristically carried out in a market economy by family businesses or small scale entrepreneurs is to be

transferred to private owners. This transfer is expected to be accomplished quickly, within the framework of a simplified privatization procedure.

Many factors created difficulties in the implementation of this law. At the time it was passed, for instance, the number of units to be included was not known (it became more than ten thousand), while the credit structure necessary for widespread participation by the general public did not exist. Only in January 1991 did Parliament introduce a law determining the range of income due to local councils as a result of transactions.

Furthermore, in the initial phase of implementation it turned out that public opinion did not feel that leasing rights were a secure enough basis to risk entrepreneurial activity. Consequently, the start up of the program involved many difficulties and the auctions began only in April 1991.

By June 15th, the auction of 900 shops and businesses had been announced and dates had been decided for 200 others. Two hundred and three shops and businesses have been sold thus far and the income derived from them is 800 million forints. Half of the companies offered at auction were bought in the first round, a third of them for cash and the rest by means of the 'livelihood' loan, earmarked specifically for entrepreneurial activity.

On the basis of provisions contained in Law LXXIV of 1990 many of the companies concerned sought exemption from the sale of their shops and businesses. In accordance with the law, the State Property Agency rejected these requests and, in the majority of cases, held that the privatization of these small businesses would be the most economically beneficial result.

In the interest of implementing the law as broadly as possible, the State Property Agency took over the proprietary rights regarding the former contractual and/or lease operations of the transformed business. In addition, it is arranging the sale of interests and shareholdings, as well as for SPA representation in companies where a significant residual share remains in state hands. The privatization of 70 of these companies has already begun.

The Coordination Consultative Committee, which operates under joint management with the Ministry of Trade and Industry, has provided regular analyses of work in progress and – partly in response to a request from Parliament – has worked out detailed proposals for accelerating privatization. These proposals suggest changes in the law concerning utilization of premises, the determination of rental fees for business premises, the procedure for taking up loans, and other considerations aimed at increasing interest in the privatization process on the part of companies and their employees. These changes, apart from replacing property valuation with property estimation, are also likely to have a beneficial effect on the economic environment of preprivatization, thereby making it possible to implement the program within two years, as called for in the law.

#### **1.4. Investor-Initiated Privatization**

In order to speed up privatization and extend the range of participants, the State Property Agency announced a new, investor-initiated privatization method in February 1991. Within the framework of this program, offers for the purchase of state companies or state owned shareholdings (shares) can be made directly to the State Property Agency; it does not, however, refer to shareholdings of state companies already transformed into limited liability or shareholding companies.

In the first few months since the announcement of investor-initiated privatization nearly 250 offer ('intentions to purchase') have been made. These offers cover a range of property from shareholdings of 1-2 billion forints up to the purchase of entire companies. A public offer then results in quick and clear implementation of the process of privatization. The opportunity to lease, combined with an option to purchase, offered by this method also creates an opportunity for small scale entrepreneurs.



Offers made for the purchase of small companies (premises, business units, shops not subject to preprivatization, etc.) cannot, however, utilize 'livelihood' loans because this fund is available only for the purchase of property put on sale by the SPA. Another complication is that because of some company managements' reluctance to cooperate in this process, the companies in question can be dealt with only by means of taking them under state administrative control. The disadvantage of such a course is that it may be regarded as an attempt to assert the influence of the state in the privatization process. The large scale transformation of these companies into limited companies may, however, solve these problems relatively easily.

### **1.5. The Self-Privatization Program**

In another attempt to speed up the process of privatization, the State Property Agency has also worked out a method which makes possible the transformation and sale of companies without direct involvement from the state. With regard to the requirements of the Law on the Protection of State Assets, this method makes it obligatory for companies choosing this path of privatization to employ one of the independent consulting and property evaluating companies to be selected by the State Property Agency by way of competition. When this requirement is fulfilled the State Property Agency will fully accept the final result of the sale in all cases. If, however, the implementation of privatization violates legal regulations or contradicts the interests of the Hungarian economy, the State Property Agency will impose sanctions against the participating independent organization or will exclude it from any further participation. It is, therefore, very much in the interests of the consulting companies to bring about quick and complete privatization. For this reason there is a supplementary fee and premium based on results.

The invitation to tender in the selection of participating organizations was published at the beginning of June 1991. After closing the competition, the State Property Agency will sign contracts with the selected organizations and the process of self-privatization will probably begin some time in the summer of this year. As this method is as yet new and untested, at present only those companies whose staff does not exceed 300 and whose annual turnover and gross property value is less than 300 million forints are authorized to pursue self-privatization. After analyzing the first experiences in self privatization the type of companies to be privatized in this way may become less restricted.

### **1.6. Other Tasks and Initiatives of the State Property Agency Related to Privatization for the Period Considered in this Report**

#### **1.6.1. The Downtown Office Building Program**

Trustees of the state in charge of premium office buildings in Budapest are in a position to benefit from this extremely scarce commodity – by way of renting these buildings – since the market is faced with a shortage of office space and, therefore, extremely high rental rates. For the sake of stimulating the Budapest real estate market, as well as the utilizing these buildings in accordance with the interests of the national economy, the State Property Agency has initiated a program for the privatization of valuable office buildings in Budapest.

In the first phase of the program – after its coordination with the relevant ministries and local councils – 12 buildings were transferred to the State Property Agency. After a two-year grace period, the present tenants may continue to use these premises if they are prepared to pay a rental fee established in accordance with the demands of the market. If not, the State Property Agency will then offer them some other, cheaper accommodation in a lower cost district.

The program is also intended to renovate, modernize and develop these building so that they reach international standards for office space in a capital city. Significant foreign interest in this type of privatization will also provide an opportunity for the involvement of foreign capital. The clarification of the legal status of the buildings and their examination from a technical point of view has been carried out;

the evaluation of the properties has also been accomplished. Irodaház Ltd., whose director has been selected by the State Property Agency by way of competition, will soon be incorporated. The previously 100% state owned limited company will take over corporations' head offices as a contribution in kind and undertake the modernization and utilization of these properties. This is in addition to collecting all rental fees and carrying out a satisfactory privatization of the state's title or portion in them.

### **1.6.2. The Taking Under State Administrative Control of Self-Governing Companies**

For the sake of the protection of state property and in order to provide conditions necessary for successful privatization, the law concerning the State Property Agency entitles its Board of Directors to take self-governing state companies under state administrative control. The Board of Directors has used this authority in 48 cases.

In most cases the relevant ministry has initiated the taking of companies under state administrative control after agreement has been reached between them and the SPA. This instrument was designed to lay the foundation for privatization or reorganization in 15 cases; in 12 cases at initiating the downtown office building program; in 11 cases the goal is liquidation of the so-called 'shell' company's head-office; while in a further ten cases the intention is to prevent the 'disappearance' of state property. In order to keep the process under control – as suggested by the relevant ministries – commissioners have been appointed to the companies involved. In cases where the director of a company was ready to cooperate, he himself was appointed commissioner.

The State Property Agency, in order to achieve a better basis upon which to appoint commissioners, has contacted the secretariat of the Hungarian Council for the Coordination of Interests with the request that the Council provide a preliminary opinion about proposals regarding the selection of commissioners.

### **1.6.3. Transfer of Property to the Social Security Organization**

In accordance with the regulations of the law concerning the State Property Agency and the Property Policy Directives, the SPA has started to select the range of property to be transferred to the Social Security Organization. The agency has also made proposals which would lay the foundation for the transfer. The SPA has consulted with the staff of the Social Security Organization's head-office about the selection of property to be transferred. With regard to the amount of property, a proposal will be made by the government in its updated Property Policy Directives. The actual structuring of deals will be possible only after the proposal has been accepted.

### **1.6.4. Management of Insolvent and Loss Making Companies**

Privatization has revealed a variety of difficulties and limitations in the overall economic restructuring process. For example, privatization often fails to solve bankruptcies, or is able to manage such situations only with the great difficulty. Several examples involving large companies show that crisis situations resulting from loss of market, low levels of efficiency, and gross overstaffing are causing enormous financial difficulties. Not surprisingly, these problems cannot be solved by privatization, because foreign partners are largely unwilling to become involved with these companies.

A lasting solution can be reached only by the radical reorganization these companies. The SPA has now gained substantial experience in this field, but it does not have the necessary resources or number of experts to fulfill such a task. The size of the State Property Agency's staff and its organizational system has been developed for the purpose of property protection and the income from privatization is to be spent primarily for the reduction of state debts.

The Hungarian economy and Hungarian economic policy is faced with a significant number of companies either making a loss and/or operating at very low levels of efficiency. Some possible options exist for finding a solution to this problem. Among them would be to assist in the process of reorgani-

zation by using part of the income derived from privatization and other financial resources; to provide a better macroeconomic environment (e.g. in tax policy); to reduce the size of some companies in order to make them more efficient; to allow privatization at a low price; and to liquidate companies that do not have realistic prospects for the future, etc.

The Government will specify its strategy regarding these questions in its program concerning property and privatization, as well as in the provisions of related laws. A new version of the Property Policy Directives should clarify the situation further.

### **1.7. Property Belonging to the State Property Agency and the Exercise of Ownership Rights**

In accordance with the law concerning the State Property Agency, state property in limited companies (shares and shareholdings) is held by the SPA. The volume of this property is expected to grow with an increase in company transformations. It will subsequently be reduced as a result of the privatization process. According to data from April 1991, property in the value of 95 billion forints in limited companies belongs to the State Property Agency.

The sale of property belonging to the State Property Agency has been carried out in two types of transactions. First, residual shares and shareholdings are continuously being sold (in accordance with the original regulations of the Transformation Law) and secondly, the SPA also sells shares and shareholdings directly.

#### **1.7.1. Exercise of Proprietary Rights and Property Management**

With regard to the state property in its portfolio, the State Property Agency carries out all those functions transferred to the owners in accordance with the Transformation Law as well as the contracts establishing individual limited liability companies. As agreed between the SPA and relevant ministries, ownership rights were exercised by the Ministry of Trade and Industry in the case of five limited companies, and by the Ministry of Transport, Telecommunication and Water in the case of two limited companies in 1990. In 1991 these agreements have not been extended, consequently ownership rights will be exercised by the State Property Agency until the property is handed over in a trust arrangement or until the completion of its privatization.

In February 1991 the Agency published a general document in which it laid down the aims, types and structural solutions characteristic of the trust system. The portfolio-package of the first property management tender was also published in order to put the property share of five companies (valued at 718 million forints) into trusts. The tender for the second portfolio package is also being prepared with the trusteeship expected to begin in the third quarter of 1991. This portfolio contains a share of state property value at 2.5 billion forints. Following consultations with the management of several sugar companies and representatives from the Ministry of Agriculture, it was decided that four sugar companies and several limited companies would be placed in trusts.

Although these developments are very promising, significant improvement is still needed in order to achieve greater efficiency in property management and, subsequently, privatization. This, however, does not exempt the State Property Agency, even in the short term, from taking the necessary steps to insure more efficient management and sale of the property in limited companies (with a value of nearly 100 billion forints) which has been transferred to it. The government is expected to announce its policy on this question in the near future, after the compensation law comes into effect. The compensation legislation, of course, could have potentially serious consequences on privatization. This, then, may help to determine any alteration of the State Property Agency's role, as well as the methods used for implementing new procedural regulations.

### **1.7.2. Financial Matters Related to the Privatization Process Involving the State Property Agency**

The State Property Agency is obliged to keep a record of the income and expenditures related to exercising ownership rights which are separate from its own budget.

From the sale of shares and shareholdings, as well as from preprivatization, an income of 676 million forints was realized in 1990. More than two-thirds of this income was in convertible currency. Five hundred and eleven million forints of this income, after deducting expenses, was used to reduce the national debt. Other types of financial transfers allowed for in the Property Policy Directives did not take place because of the lack of additional income.

Privatization expenses for which limited companies may not be held liable – for example, the cost of maintaining a shareholding or advertising and privatization costs related to the introduction of shares on the stock market – amounted to 3.2 billion forints.

As a result of the acceleration of the privatization process, the State Property Agency realized an income of 2.7 billion forints in the first quarter of 1991. At the close of this report the total stands at nearly 7 billion forints. The majority of this income is in convertible currency. Until now expenditures from this income have been used exclusively for reducing the national debt.

Expenses of the State Property Agency resulting from privatization programs and the start up of preprivatization have increased significantly. These amounted to 8.2 billion forints in the first quarter of 1991, 60% of which arose in connection to preprivatization.

The Hungarian national budget for 1991 projects privatization income of 40-50 billion forints. There is great pressure being applied by various interest groups that would like to utilize part of the privatization income. The current Property Policy Directives allow the free transfer of property only to the Social Security Organization. The government, however, will submit its new proposal to Parliament concerning the future disbursement of privatization income within the framework of its new Property Policy Directives.

### **1.8. Employee Ownership and Representation in the Course of Privatization**

Current legal regulations provide various opportunities for employees to obtain property ownership. The Companies Law, for example, provides an opportunity to issue shares for employees, while the Transformation Law, in certain cases, makes issuing these shares obligatory. Furthermore, the Property Policy Directives make it possible for employees to obtain shareholdings in limited companies by way of concessions up to 50%. The purchase of property bonds and the provision of free property bonds is also possible and these may be transferred into shares and/or shareholdings later on.

The State Property Agency has approved transformations and sales in which employees were offered an opportunity to obtain shares and shareholdings to the value of 4.3 billion forints. In the case of most limited companies, employees have obtained the right to a share of property not exceeding 10% of the total property of the limited company. The various ways that employees can currently obtain property and the Employee Share Ownership Program (ESOP) to be introduced in the near future have very different conditions. There are a great many variables involved in the opportunities for employees to obtain property, depending on the type of company, its ownership structure and the financial position of the limited company. In this situation the Board of Directors of the State Property Agency has supported the idea of standardizing concessions and, of course, decided that the opportunity for obtaining concessions has to be provided for all employees. The total amount of concessions, however, cannot exceed 10% of the founding capital.

The government will soon submit its proposal concerning the Employee Share Ownership Program to the Parliament, thereby expanding the possibilities for employees to obtain property. The question

of representing the various interests involved in a privatization case, and specifically, the representation of employee interests, therefore is an issue of immediate concern. The Board of Directors of the State Property Agency currently requires that the management of companies submit their plans concerning transformation and privatization only after these have been reconciled with groups representing the interests of employees. The State Property Agency then tries to achieve the same arrangement in the actual privatization process. The Agency and the government reconcile the most important issues with regard to privatization at forums of the Interest Coordination Council.

In addition, the government has coordinated its viewpoint with the Interest Coordination Council so that in the future an opportunity will be provided for employees to represent their interests on the Board of Directors of the State Property Agency.

Representation of interests is also a significant issue in limited liability companies; if a state company is transformed into a public limited liability company then the employees also have to be represented on the supervisory committee.

Although the mechanisms regarding ownership rights and the representation of interests has been developed, or are in the process of being developed, significant difficulties remain. Some feel that the "voice" given to employees is often little more than a formal consideration; tensions sometimes arise between the employees and individual members of the company's management; the State Property Agency and some ministries are criticized; there is also a great deal of anxiety in the case of companies which have lost their market and which are struggling with bankruptcy. The government has requested that both the State Property Agency and the ministries apply all the guarantees provided by law in order to assure that employees' ownership interests are taken into consideration at every stage of the privatization process.

## **2. The Future of the Privatization Process**

The previous parts of this report are not merely an outline of facts, figures and events related to the period in question, though this was their main purpose. They have also highlighted the difficulties and problems that have been revealed by the privatization experience until now. Parts of the report also indicate what measures the government might take in order to resolve these problems. Problems not discussed, or merely mentioned in passing, must also be noted here.

### **2.1. Property Subject to Privatization and Income to Be Expected**

On December 31, 1990 the total amount of state property accounted for was 2200 state owned companies, valued at 1900 billion forints according to their accounts. The actual range of companies and property subject to privatization, however, is much smaller. Approximately 100 companies, possessing property valued at 500 billion forints, will remain state owned for the foreseeable future, in accordance with the government privatization strategy now being prepared. Four hundred companies that were unprofitable in 1990 will be liquidated or reorganized, but not as part of a privatization program. The majority of the 800 small companies should be privatized shortly by taking advantage of the self-privatization program. Because of their low profitability, however, the income deriving to the state in these cases will amount to 50-60 billion forints, at most. Given these considerations, the range of companies available to provide privatization income for the state amounts to 900 units with a total value of approximately 700 billion forints.

This approximately 700 billion forints in property subject to privatization, however, will not all result in state income. The total will be reduced by the share of property due to the local councils, amounting to 8-12%, and by various concessions provided for employees, the average volume of which is to be 10% of the original value of the company. From the roughly 560 billion forints of potential revenue remaining the cost of transactions (6-8%), as well as the guarantee fund to be separated from income for the purpose of compensating environmental damage (an amount difficult to estimate), also have to be subtracted. It should also be noted that, in accordance with the transformation law, 20% of the

gross income from the sale of company shares has to be returned to the limited companies as a contribution toward financing employee shareholding on preferential terms. This will result, on average, in a further 12% reduction of income from privatization. In some cases the State Property Agency cannot avoid taking responsibility for the financial condition and property belonging to the company being put up for sale, the consequence of which cannot be expressed in figures.

Judging by the experience so far, i.e. taking into account the approximately 25% reduction in income, an eventual income of 380-390 billion forints, at current prices, can be expected from the privatization of state companies. The State Property Agency may initiate measures to extend the range of property subject to privatization, and therefore increase the volume of income from privatization to a certain degree, but these measures have obvious limitations.

On the basis of the above said:

- it can be stated that income from property sales will not be enough for a significant reduction in, let alone liquidation of, the national debt;
- It is important that the government, in its privatization strategy, select the range of companies that are currently not, or only partially, subject to privatization; furthermore, those companies for whom full privatization is expedient should also be identified. This is expected to be carried out in the near future, following the approval of the government's overall privatization strategy;
- it has to be acknowledged that it will be difficult to accelerate the privatization of unattractive companies and that acceleration can only be achieved under unfavorable conditions;
- the government will decide upon the method and arrangement for financing reorganization processes, again within the framework of its privatization strategy.

## **2.2. Privatization and Problems Related to Its Further Development**

Privatization processes are subject to sharp domestic criticism all over the world, and Hungary is no different in this respect. Taking into account the variety of financial interests involved, as well as the conflicts resulting from the fundamental transformation of the nation's ownership structure, this must be regarded in many ways as inevitable. Certain concrete problems have made this criticism even more virulent.

One problem in this regard is the restricted volume of domestic and foreign investment capacity, particularly where domestic Hungarian private investors are concerned. Up until now, most property has been purchased by foreigners; however, one of the main aims of the government is to strengthening domestic investment capacity and to develop entrepreneurship. This will be assisted by already existing privatization loans, investment companies, compensation bonds and the ESOP. Large scale investment and substantial entrepreneurial activity, however, can only be developed gradually.

Another obstacle is the lack of a well-defined ownership situation, a problem noted both in Hungary and abroad. The government position is that this obstacle can be removed easily by accepting the provisions of the Compensation Law.

Information about the Hungarian economy, both on the macro- and micro level, is extremely outdated and incomplete. Recordkeeping with regard to land and real estate is a complicated affair, while the condition of the environment is completely unclear. Because of this, the sale of Hungarian companies to foreign investors is extremely time-consuming and requires the extensive and expensive use of expert consultants.

The government has given its support to developing a statistical information system to be coordinated by the State Property Agency. It also wants to establish a background organization designed to fulfill the need to provide information, keep accurate records, and perform accounting tasks related to property. Such a system and an organization should lead to significant progress in the area of information management. The new accounting law should establish a foundation for such changes.

The macroeconomic environment also plays a decisive role in the privatization effort. The rigidity of Hungary's depreciation system, unusually high social security contributions, high taxes, and the concessional priorities of the tax system, for example, have a decidedly unfavorable effect on state companies and their attractiveness to investors. The rate of inflation in Hungary also renders the purchase of shares and shareholdings unattractive and the collapse of the COMECON market similarly reduces interest in privatization. In accordance with its principles regarding economic policy, the government will attempt to find solutions to these problems.

There is little hope for quick and easy solutions. However, the new accounting system and the coordinated modification of other regulatory instruments, particularly the system of depreciation and taxes, can ease many problems in the short run.

Accelerating the pace of privatization and the multi-faceted practical considerations involved inevitably comes into conflict with the rigidity of legal regulations. Legal regulations concerning competition, property management the reorganization of companies, provision of property for employees and local councils (of, for instance, downtown land), and the purchase and development of real estate by foreigners, are far from perfect. Laws concerning the protection of the environment have not yet been developed. Company-initiated privatization must be regulated on the basis of a better, more supportive approach. The wider establishment of limited companies and of holdings held by real owners also requires new regulations. For its part, the government intends to make decisions regarding these issues within the framework of its privatization strategy, which is currently being prepared, and through legislation that is now being debated.

By confronting these issues and attempting to apply imaginative and substantial solutions to them, the Hungarian privatization can expect not only to maintain the momentum it has developed in the first year, but to increase it in the immediate future.

## Appendix I.

### **Legal regulations governing the privatisation process and the activities of the State Property Agency**

Parliament created the State Property Agency by means of Law VII. 1990 in order to promote and supervise the privatisation of state companies.

Many legal regulations govern the authority and the range of tasks of the State Property Agency:

- modified law VII, 1990 concerning the State Property Agency and the handling and utilization of property belonging to it;
- modified Law VIII, 1990 concerning the protection of property entrusted to state companies;
- modified Law XIII, 1989 on the transformation of limited companies and economic organizations;
- Law LXXIV, 1990 concerning the use, sale and privatisation of the property of state companies conducting activities in the retail trade, catering and in consumption services (preprivatisation law).

In addition to legal regulations the Parliament annually determines the Property Policy Directives.



### 1. Summary data on the state owned companies Involved in privatisation

Year	1. Number of state owned company	2. Property according to financial accounts	3. Gross Profit according to the balance sheet	4. Net Profit after tax	5. Gross income on the basis of property (3./2.)	6. Net income on the basis of property (4./2.)
<b>State companies</b>						
1989	2201	1,841.9	169.9	98.0	9.2	5.3
1990	2197	1,888.1	174.3	99.8	9.2	5.3
<b>Profitable companies</b>						
1989	220	915.0	155.0	76.3	16.9	8.3
1990	220	828.8	177.3	104.8	21.4	12.6
<b>Loss making</b>						
1989	158	115.2	-13.7	-10.1	-11.9	-8.7
1990	404	354.4	-38.3	-28.1	-10.8	-7.9
<b>Preferred companies/1</b>						
1989	105	478.2	80.5	40.6	16.8	8.5
1990	103	531.2	97.3	59.6	18.3	11.2

/1 Companies which will remain majority state owned in the foreseeable future in accordance with the government policy.

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## 2. Approved transformation cases

	Book value of the shareholder's fund million HUF	Company value recognised at transformation million HUF	SPA's particip. %	Foreign particip. %
<b>Year 1990</b>				
CARBON	148.00	200.00	12.70	36.51
Debreceni Konzervgyár	2624.00	2624.00	85.79	0.00
DÉLKER	800.00	1462.00	14.57	0.00
Egri Közúti Ép. Váll.	273.40	306.00	39.58	50.00
Folyamszab. és Kav.kotró V.FOKA	910.59	3492.86	100.00	0.00
Kaposvári Cukorgyár	746.54	1770.00	13.77	31.13
Kecskeméti Borgazdasági Komb.	1162.55	936.07	16.71	0.00
Kőbányai Gyógyszerárugyár	8343.00	13589.00	99.04	0.09
Köztépülettervező Váll.	147.55	1113.98	17.00	51.00
Közúti Beruházó Vállalat	47.40	113.90	16.68	68.84
Műszaki Árut Értékesítő Váll.	819.74	973.69	74.31	0.00
Nagykanizsai Sörgyár	843.00	843.00	100.00	0.00
Petőfi Nyomda	319.15	800.75	16.36	50.00
Petőházi Cukorgyár	1198.30	2653.30	14.00	30.00
Pécsi Agroker	534.75	900.00	76.90	0.00
Pécsi Közúti Építő V.	186.00	263.50	10.00	50.00
Statisztikai Kiadó Vállalat	138.05	293.54	87.00	0.00
Szerencsi Édesipari Vállalat	868.00	1777.00	63.76	33.33
Székesfehérvári Közúti Ép.V.	205.00	373.00	39.30	50.00
Villanyszerelőipari Vállalat	1175.18	2131.20	80.50	0.00
Volkswagen Óbudai Autójavító V.	116.40	116.40	16.41	0.00
Zalaegerszegi Hűtőipari Váll.	486.03	764.00	100.00	0.00
Zalaegerszegi Ruhagyár	422.02	455.24	15.70	30.66
Úvegipari Gép és Szerszámgyár	258.53	258.50	100.00	0.00
<b>Subtotal:</b>	<b>24</b>	<b>22773.18</b>	<b>65.00</b>	<b>11.90</b>

### Year 1991 (up to 31 March)

Borsodi Sörgyár	2040.00	5930.00	74.30	16.70
COMPACT Keresk.Csomagoló Váll.	3149.25	3737.80	57.49	40.00
Debreceni Közúti Építőip.Váll.	300.50	404.60	38.90	50.00
GENERÁL Autójavító Váll.	38.10	46.88	84.00	0.00
HALDEX Vállalat	564.88	116.08	88.50	0.00
Hajdúsági Cukorgyár	2491.00	4554.00	63.66	30.34
Pest Megyei Nyomda Vállalat	32.09	35.23	90.00	0.00
Szegedi Konzervgyár	141.69	1068.00	0.00	0.00
Székesfehérvári Hűtőipari V.	508.97	1047.52	89.70	0.00
<b>Subtotal:</b>	<b>9</b>	<b>9266.48</b>	<b>65.00</b>	<b>30.00</b>

### After 31 March, 1991

	Book value of the shareholder's fund	Company value recognised at transformation	SPA's particip.	Foreign partic.
	million HUF	million HUF	%	%
ALFA ÉLELM. ÉS VEGYÁRU KER.V. 1828.23		2641.76	100.00	0.00
Budapesti Szeszipari Vállalat	797.00	1801.21	58.10	30.00
Bácska Kereskedelmi Vállalat	222.83	216.70	95.00	0.00
ELZETT, Sopron	436.75	622.00	96.00	0.00
Erdészeti és Faipari Tervező V.	41.03	49.41	100.00	0.00
Győri Keksz és Ostyagyár	583.54	1592.86	4.00	84.00
KORONA Nagyker-i és Szolg.V.	322.64	310.20	96.72	0.00
LEHEL Hűtőgépgyár	4280.00	4280.00	0.00	100.00*
Oxigén és Disszougázyár	1261.00	1891.00	90.00	0.00
Paletta Kereskedelmi Vállalat	454.67	46.00	99.00	0.00
Pécs-Baranya m. Beruházási V.	10.82	23.90	61.50	0.00
Tatabányai Autójavító Vállalat	29.30	44.00	85.90	0.00
Subtotal:	12	10267.81	68.50	22.80
Total:	45	42307.47	64.50	19.00

### 3. Rejected transformation cases

	Book value of the shareholder's fund million HUF
<b>Year 1990</b>	
AMFORA	890.00
ERDÉRT	5604.69
Habselyem Kötöttárugyár	750.60
KALIBER	195.00
KOPINT - DATORG	260.00
Kossuth Nyomda	510.90
Kőbányai Sörgyár	1908.00
Lignimpex	684.00
<b>Total:</b>	<b>8</b> <b>10803.19</b>
<b>Year 1991 (31 March)</b>	
Zalai Nyomda	89.05
<b>Subtotal:</b>	<b>9</b> <b>10892.24</b>

#### 4. Transformation cases in process

	Present book value of the shareholder's fund million HUF	Planned SPA particip. million HUF	Planned foreign partic. million HUF
AGROGÉP Vállalat	33.00	0.00	0.00
AGROÉP NYIRTELEK	33.80	0.00	0.00
ALKALOIDA Vegyészeti Gyár	3056.00	51.00	44.00
AUTOFER	155.30	85.00	0.00
AUTOKER	4600.00	19.35	0.00
Alföldi Porcelángyár	1450.00	30.00	60.00
Alföldi Vendéglátó Vállalat	88.00	31.62	0.00
Autókomplex Vállalat	30.00	0.00	0.00
Badacsonyvidéki Pincegazd.	1195.60	79.00	0.00
Baranya megyei Sütőipari Váll.	251.00	0.00	0.00
Borsod m. Állami Ép. V.	1103.00	0.00	0.00
Bp-i Szeszipari V. BUSZESZ	893.00	58.10	30.00
Békés m. Gabonaforg. Vállalat	2043.00	0.00	0.00
Bács-Kisk.m.Gabona és Malom.V.	1587.00	97.00	0.00*
Bácska Ker. Vállalat	217.00	0.00	0.00
CAOLA Kozm.és Háztart-vegyip.V.	1793.00	0.00	100.00*
CHEMOKOMLPEX	50.00	82.70	0.00
CHEMOLIMPEX	2744.00	97.44	0.00
Chemimas	254.00	50.00	0.00
Csepel Művek Fejl-Terv.Váll.	30.87	43.00	0.00
DELTA Kereskedelmi Vállalat	139.90	14.93	0.00
DOMUS	1611.00	93.00	0.00
Debreceni Baromfiipari Váll.	596.00	91.00	0.00
Dél-Pest Megyei Sütőipari Váll.	207.40	80.00	0.00
Délmagyarországi Építő Váll.	609.78	0.00	0.00
Délröviköt	330.00	0.00	0.00
ELZETT-CERTA , Sátoraljaújhely	2000.00	23.10	75.00
ERDÉRT	7000.00	0.00	0.00
Egervin	1000.00	0.00	0.00
Egri Dohánygyár	616.00	0.00	100.00
Elektromodul	2407.00	100.00	0.00
Energiagazdálkodási Intézet	487.00	100.00	0.00
Fővárosi Ruházati Szolgáltató	179.62	16.61	0.00
Győr-Sopron m. Bank Vállalat	15.00	0.00	0.00
Győr-Sopron m.Tan. Tervező V.	22.00	0.00	0.00
Habselyem Kötöttárugyár	643.00	0.00	100.00
Hajdú-Bihar m. Sütőipari V.	445.00	0.00	0.00
Hajdú-Bihar m. ÁÉV	1571.00	0.00	0.00
Hajtóművek és Festőberend.Gy.	834.00	65.00	32.00
Hídépítő Vállalat	990.00	36.00	54.00
Hódmezővásárhelyi Közúti Ép.V.	324.00	100.00	0.00*
KIPSZER	46.00	51.00	49.00
KOMPLETT Ruházati Vállalat	123.60	0.00	0.00
Karamell Sütő és Édesip.Váll.	198.00	80.00	0.00
Kecskeméti Sütő- és Édesip. V.	193.40	90.00	0.00
Komárom m. Kályhacsempegyártó	45.20	10.00	80.00
Konsumex Külkereskedelmi V.	2000.00	71.75	0.00
Középmagyarországi Kőbánya V.	143.47	65.00	30.00
Középvületépítő Vállalat	879.18	0.00	0.00
LENTA Asztalosipari Vállalat	351.00	0.00	0.00

#### 4. Transformation cases in process

	Present book value of the shareholder's fund million HUF	Planned SPA particip. million HUF	Planned foreign partic. million HUF
MAHIR	434.00	0.00	0.00
Magyar Kábel Művek	3844.00	0.00	0.00
Miskolci Közúti Épít. Vállalat	182.00	39.00	51.00
Mohácsi Farostlemezgyár	620.00	0.00	0.00
Monitor	10.00	0.00	0.00
Mátravidéki Cukorgyárak	1271.00	58.10	39.00*
Ny.-Pest m. Sütőipari Váll.	229.00	0.00	0.00
Nyíregyházi Közúti Ép. Váll.	286.60	48.00	49.00
Növényolajip. és Mosószergy. V.	5142.30	0.00	0.00
Pannon Autójavító	96.00	0.00	0.00
Pécsi Bőrgyár	1494.00	0.00	100.00*
Pápai Autójavító	26.00	89.00	0.00
REKARD Győri Mg. és Mechatr. Ggy.	492.00	85.00	0.00
Remix Rádiótechnikai Vállalat	994.00	0.00	0.00
Salgótarjáni Öblösüveggyár	581.00	0.00	0.00
Sarkadi Cukorgyár	2486.00	69.00	30.00*
Senior Váci Kötőtárugyár	514.00	0.00	0.00
Soproni Sörgyár	313.00	0.00	100.00
SzIKKTI	350.00	20.00	45.71
Szabadegyházi Szeszipari V.	3529.00	0.00	100.00
Szegedi Paprikafeldolgozó V.	704.00	45.00	30.00
Szerencsejáték Vállalat	1817.00	100.00	0.00
Szerencsi Cukorgyár	1019.00	39.00	37.00*
Szigetvári Konzervgyár	718.00	0.00	0.00
Szigma Ker. Vállalat	530.00	49.00	51.00
Szolnoki Cukorgyár	1800.00	53.30	33.30*
Sárvári Cukorgyár	458.60	49.18	30.20*
TECHNIKA	1059.00	100.00	0.00
Tatabányai Autójavító	29.30	86.00	0.00
Tokajhegyaljai Állami Borkomb.	2008.00	0.00	0.00
Universum Autójavító	158.00	100.00	0.00
Út és Vasútépítő Vállalat	776.90	0.00	0.00
Veszprém. m. Gabonaforg. Vállalat	478.00	0.00	0.00
Villért	1659.00	0.00	0.00
Zala m. Gabonaforgalmi Váll.	586.00	0.00	0.00
Zsolnai Porcelángyár	511.00	51.00	49.00*
Általános Géptervező Iroda	82.00	100.00	0.00
Észak-Pest m. Sütőipari Váll.	258.00	0.00	0.00
Északmagyarországi Kőbánya V.	380.00	46.00	46.00*
<b>Total:</b>	<b>88</b>	<b>85545.82</b>	<b>35.69</b>
			<b>25.38</b>

\* Approval in principle already given

### 5. Approved associations with foreign participation

	Book value before non financial contribution  million HUF	Approved value of the contribution during transaction million HUF	The share capital of the receiving company  million HUF	The particip of the contributing company  %	Foreign partic.  %
<b>1990</b>					
Alföldi Porcelán	318.50	591.00	726.60	81.30	18.72
Békéscsabai ÁG	100.00	350.00	500.00	70.00	30.00
DELTA Szaklapkiadó Leányváll.	27.00	53.00	52.00	0.00	5.77
FORCON	62.88	150.00	324.70	49.90	49.90
GANZ Villamossági Művek	600.00	1000.00	2060.00	49.00	51.46
Győr m.Állami Épip.Vállalat	7.10	63.00	126.00	50.00	50.00
Győr m.Állami Épip.Vállalat	2.90	15.10	46.80	49.00	51.00
HÓDIKÓT	78.27	162.50	325.00	50.00	50.00
KERIPAR	101.00	230.00	460.00	50.00	50.00
Kaposvári Közúti Ép. V.	175.70	183.00	1083.00	16.90	50.00
LÁNG Gépgyár	40.00	40.00	160.00	25.00	75.00
Masterfil	180.00	270.00	675.00	40.00	60.00
NIKEX	n.a.	368.00	800.00	51.00	49.00
Országos Érc- és Ásványbányák	321.92	490.00	700.00	50.00	50.00
Ózdi Kohászati Üzemek	700.00	780.00	1950.00	40.00	60.00
Pamutextilművek	26.00	26.00	40.00	65.00	35.00
Pannonplaszt Műanyagipari V.	483.20	612.00	1224.00	50.00	50.00
Papíripari Vállalat	3746.00	7995.00	13325.00	60.00	40.03
Robix	75.00	75.00	150.00	0.00	50.00
Révai Nyomda	23.00	40.20	500.00	9.60	55.00
Salgótarjáni Kohászati Üzemek	126.00	808.51	1650.00	49.00	51.00
Szabadegyházi Szeszipari V.	n.a.	2626.91	5200.00	51.50	48.54
Szabolcs Cipőgyár	21.30	48.70	61.40	1.60	98.37
TEMAFORG Vállalat	13.56	38.47	76.94	50.00	50.00
VILATI	5.80	24.00	60.00	40.00	60.00
Villamos Állomásszerelő V.	160.20	166.60	368.60	45.30	49.26
Élelmiszeripari Vállalat	43.00	67.00	187.00	35.80	53.48
Észak-Budai Vendéglátó	44.46	103.00	698.00	14.70	76.65
<b>Subtotal:</b>	<b>28</b>	<b>7455.79</b>	<b>17376.99</b>	<b>51.26</b>	<b>46.51</b>

### 5. Approved associations with foreign partner

	Book value before non financial contribution million HUF	Approved value of contribution during transaction million HUF	The share capital of the receiving company million HUF	The particip of the contributing company %	Foreign particip. %
<b>Year 1991 (31 March)</b>					
Békés m.Állami Építőip. Váll.	4.87	45.00	293.22	1.02	5.83
Cement és Mészművek, Vác	280.00	280.00	1800.00	51.00	49.00
Debreceni Elektr.Karbantartó V.	37.96	50.00	100.00	50.00	40.00
Hírlapkiadó Vállalat	n.a.	40.00	100.00	40.00	40.00
KERAVILL	222.22	240.27	702.00	98.50	0.80
Kaposvári Ruhagyár	46.00	52.06	104.00	50.00	50.00
Kőfaragó és Épületszobrászip.V.	17.29	100.00	230.00	43.50	43.50
MASPED	351.41	450.00	650.00	69.20	30.80
Magyar Optikai Művek	n.a.	113.07	226.14	50.00	50.00
Papíripari Vállalat	2.05	1.78	7.70	50.00	50.00
Pest megyei Fémipari Vállalat	8.46	25.00	50.00	50.00	50.00
VILATI	16.20	36.30	146.40	25.00	75.00
Subtotal:	12	986.46	4409.46	56.31	30.03
Total:	40	8442.25	18810.47	51.85	45.29

### 6. Rejected associations with foreign participation

	Book value before non financial contribution million HUF
<b>Year 1990</b>	
Budai Téglaiipari Vállalat	no value
Fővárosi Garázsipari Vállalat	no value
Nógrád megyei V.V.	no value
ÁFOR Ásványolajforgalmi V.	19.23
ÉGSZI	no value
Total:	5 19.23
<b>Year 1991 (31, March)</b>	
22.sz. ÁÉV	32.00
Mechanikai Laboratórium	20.00
Subtotal:	2 32.00
Total:	7 51.23

## 7. Approved associations with domestic partner

	The particip. of the contributing company	Book value before non financial contribution	Approved value of the contribution during transaction	The share capital of thereceiving company
	million HUF	millio HUF	million HUF	%
<b>Year 1990</b>				
43. ÁÉV	491.00	491.00	491.00	100.00
BUBIV Egri Bútorgyár	20.60	34.80	35.80	100.00
Békés m. Állami Építőip. Váll.	23.10	29.30	41.90	99.76
CHEMIMAS	130.00	130.00	130.00	100.00
DÉLÉP	150.00	150.00	221.00	68.00
Elektroakusztikai Gyár	3.69	80.89	81.89	100.00
Grabocenter	53.44	53.44	50.05	97.00
Hazai Fésűsfonó és Szövőgyár	101.77	101.77	174.10	61.50
Heves m. Iparcikk Kisker. Váll.	176.38	287.91	411.31	91.10
Kertészeti Egyetem Tangazdaság	n.a.	118.00	168.00	70.00
Mezőgazdasági Kombinát, Bóly	35.00	48.00	138.00	35.00
Ózdi Kohászati Üzemek	6.32	8.74	29.87	29.30
PANNONKER	180.00	387.00	600.00	65.00
Pest megyei V. V.	13.40	27.80	40.00	69.00
Szabolcs Cipőgyár	13.00	13.20	14.65	96.60
Szabolcs Cipőgyár	1.37	4.80	10.00	48.00
Szabolcs-Szatmár m. Élelm.Kisk	n.a.	25.40	34.20	70.00
VASIPARI KUTATÓ	82.00	82.00	82.00	100.00
<b>Subtotal:</b>	<b>18</b>	<b>1331.07</b>	<b>2074.05</b>	<b>2753.77</b>
<b>Year 1991 (31, March)</b>				
DELTA Szaklapkiadó Vállalat	68.08	109.55	109.00	100.00
Elektroakusztikai Gyár	0.52	35.76	150.00	23.70
Fogtechnikai Vállalat	1.97	11.99	13.69	95.00
Hírlapkiadó Vállalat	n.a.	44.00	160.00	27.50
Opál Kereskedelmi Vállalat	n.a.	0.00	343.58	96.30
Ózdi Kohászati Üzemek	10.59	10.54	17.04	73.60
Papíripari Vállalat	5.82	1.80	3.00	100.00
Papíripari Vállalat	60.81	73.45	104.94	100.00
Villamos ÁLLomásszerelő V.	2187.60	17520.00	30720.00	57.00
Villamos Állomásszerelő V.	28.87	40.05	58.97	95.00
Visoram Szemüvegkeretgyár	30.27	30.27	48.00	75.00
Visoram szemüvegkeretgyár	8.93	12.72	19.80	75.00
Zala Volán	18.31	39.08	56.00	99.00
Zala Volán	2.80	3.94	6.08	76.00
Zala Volán	33.43	45.35	65.42	69.00
Zala Volán	44.57	56.45	81.64	69.00
Zala Volán	2.60	3.97	5.67	80.60
<b>Total:</b>	<b>17</b>	<b>2505.17</b>	<b>18038.92</b>	<b>31962.83</b>
<b>Subtotal:</b>	<b>35</b>	<b>3836.24</b>	<b>20112.97</b>	<b>34716.60</b>



## 8. Rejected establishment of limited companies with a domestic partner

		Book value before non financial contribution million HUF
<b>Year 1990</b>		
21. ÁÉV		120.00
Csepeli Szerszámgépgyár		104.80
PALOCKER		36.00
<b>Total:</b>	<b>3</b>	<b>224.80</b>

None of the cases were rejected in 1991

### 9. Approved property protection cases

	The book value of the transaction	The contract value of the transaction
	million HUF	million HUF
<b>Year 1990</b>		
23. ÁÉV	n.a.	63.00
Alba Volán	38.34	69.40
Alba Volán	51.28	119.17
Alföldi TŰZÉP	70.00	83.00
Budapest Film	n.a.	46.40
Bázis Déldunántúli Épip.Váll.	n.a.	84.00
Bázis Déldunántúli Épip.Váll.	52.00	84.00
CENTRIKÖT	71.00	250.00
Csepregi Állami Gazdaság	n.a.	4.00
DUNA Cipőgyár	3.14	38.88
Felsőbabádi Állami Gazdaság	n.a.	10.00
Fővárosi Szerelőipari Vállalat	54.00	54.00
Graboplaszt Állami Váll.	100.00	125.00
Győr m.Állami Épip.Vállalat	49.80	81.00
Gép és Szerszámértékesítő V.	90.00	104.00
KÖSZIG	6.50	100.00
Lajta Hansági Államigazdaság	10.00	33.00
Látszerészeti Eszközök Gyára	6.16	33.70
Mecseki Ércbányák	20.00	50.00
Mezőgazdasági Kombinát, Agárd	105.00	105.00
Mezőgazdasági Kombinát, Agárd	n.a.	130.00
Mezőgazdasági Kombinát, Baja	187.90	187.90
MÁFKI	5.28	70.00
MÉM Repülőgépes Szolgálat	25.00	31.00
ORION	70.00	186.00
Ózdi Kohászati Üzemek (Meteor)	7.62	7.62
PALLAS Lap és Könyvkiadó Váll.	n.a.	108.00
Pénzüntézeteki Központ	25.00	60.00
RÁBA	39.52	56.40
Szabadegyházi Szeszipari V.	n.a.	106.69
Szentesi Baromfifeldolgozó V.	92.70	93.00
Szerszámgépipari Művek	40.00	150.00
Szombathelyi Állami Gazdaság	n.a.	16.00
Tisza Cipőgyár	19.39	176.60
VOLÁN-TEFU Rt.	73.00	700.00
Videoton	n.a.	42.00
Állami Fejlesztési Intézet	n.a.	61.60
Élelmiszeripari Váll. (ÉLGÉP)	n.a.	6.00
<b>Total:</b>	<b>38</b>	<b>3726.36</b>

## 9. Approved property protection cases

	The book value of the transaction	The contract value of the transaction
	million HUF	million HUF
<b>Year 1991 (31. March)</b>		
23. ÁÉV	17.00	80.00
Alföldi Porcelán	103.00	162.00
Balaton Volán	125.05	180.00
Csepel Művek Szerszámgépgyár	35.79	248.70
Csákvári Állami Gazdaság	n.a.	2.01
FALCO Fakombinát	458.00	458.00
Fűrész- Lemez és Hordóip. V.	17.20	18.46
Információtechnikai Vállalat	1.76	9.00
Iskolabútor és Sportszergyár	35.71	100.00
KEMIKÁL	25.92	80.00
Kaposvári Mezőg. Gépgyártó V.	2.19	47.70
Kőbányai Sörgyár	285.00	650.00
Könnyűbeton és Szigetelőip. V.	40.80	84.00
Mélyépítő Vállalat	155.00	162.50
Telefongyár	35.75	60.00
Volánbusz	1.60	4.86
<b>Subtotal:</b>	<b>16</b>	<b>1339.77</b>
<b>Total:</b>	<b>54</b>	<b>2347.23</b>
	<b>2652.40</b>	<b>6073.59</b>

## 10. Rejected property protection cases

		The book value of the transaction million HUF
<b>Year 1990</b>		
ALBA REGIA		25.00
DÉLÉP, Magyarországi Ép.Váll.		4.20
Fegyver és Gázkészülékgyár		n.a.
Fűrész- Lemez és Hordóip. V.		15.00
GAMSZOV (Gerbaud)		46.00
Helvéciai Állami Gazdaság		n.a.
Tiszai Vegyi Kombinát		n.a.
Út és Vasútépítő V.		n.a.
VEGYTEK		650.00
É-Dunántúli Közmű- és Magasép.		5.20
Észak D.túli Közmű és Magasép.		0.80
<b>Total:</b>	<b>11</b>	<b>746.20</b>
<b>Year 1991 (31, March)</b>		
Alföldi TŰZÉP		79.60
Délmagyarországi Építő Váll.		87.50
Tiszai Vegyi Kombinát		681.50
<b>Subtotal:</b>	<b>3</b>	<b>848.60</b>
<b>Total:</b>	<b>14</b>	<b>1594.80</b>

### 11. First Privatisation Program

	Book value of the property million HUF	Type of the planned first transaction	Planned time of the transaction	Name of the advisor
HUNGARHOTELS	11000.0	priv.plac.	3rd-4th qrt 1991 sale of employees share 1st qrt 1992 shares on stock market	SwissBank Corporation
HUNGEXPO	1600.0	priv.plac.	3rd-4th qrt 1991 sale of employees	CCF Corp.
MÉH Tröszt	3700.0	sale	4th qrt 1991	Rotschild (Paris)
Tritex	700.0	manag.buy.	3rd qrt 1991 MBO 2rd qrt 1992 shares on stock market	Landerbank
Pietra	653.0	priv.plac.	Oct. 1991	Wricor Grp
IDEX	618.0	priv.plac.	Oct. 1991	Hydec- Agrocons.
KNER Nyomda	1500.0	priv.plac.	Oct. 1991	CCF Corp. Finance
Erdőgép	61.0	Working out of the ESOP	Dec. 31, 1991	Co-Nexus
KUNEP	197.0	priv.plac.	Nov. 1991	Ernst a Young
IBUSZ	4191.9	priv.plac.	Jun. 1991	Rotschild (London)
Salgótarjáni Süküv.	1186.0	sale	4th qrt 1991	Daiwa (Europe Ltd.)
INTERGLOB	761.0	priv.plac. sale	4th qrt 1991 1st qrt 1992	DRT Touche Rosse

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## 11. First Privatisation Program

	Book value of the property  million HUF	Type of planned first transaction	Planned time of the transaction	Name of the advisor
Volán Tefu	1554.0	priv.plac. sale	4th qrt 1991 1st qrt 1992.	KPMG
Hollóházi Porc.	416.0	priv.plac. sale	3rd-4th qrt 1991	Nesbitt Thomson G.
Gamma Művek	883.1	transaction with foreign participation	Aug. 1991	Pénzügy
Pannonplast Műany.V.	2649.8	selling of shares market	June 1991	Kutató Rt. Credit Swisse First Boston
Pannónia	2862.0		Dec. 91-Jan. 92.	J.P.Morgan
Danubius	2453.0		Sep. 91.	Nomura
CENTRUM	5200.0	founding of PLC	Sep. 91.	Barclays de Zoette
Richter Gedeon Rt.	12417.0	priv. sale	4th qrt 91.	Wedd/coop. Nomura/OKHB
<b>Total:</b>	<b>20</b>			
	<b>54602.8</b>			

Total estimated value of the companies: 90.4 billion HUF  
 Planned share of the State Property Agency: 36 %  
 Planned foreign share: 42 %

## 12. Enterprises Involved In the Second Privatisation Program

### Phase I

Enterprises	Shareholder's fund million HUF
Csavaripari Vállalat	1095
Csepel Művek Ruhaip.Gép-és Kpárgy	1108
Elegant Május1 Ruhagyár	692
Élelmiszergépipari Vállalat	1206
Építőgépgyártó Vállalat	436
GANZ Szerszámgyár	416
GRABOCENTER Sz.V.V.	2694
Információtechnikai V.	451
MOM	2016
SZATMÁR Bútorgyár	348
Szék-és Kárpitosipari V.	877
Szerszámgépipari Művek	2850
<b>Total:</b>	<b>12 14189</b>

### Phase II

Enterprises	Shareholder's fund million HUF
AUTÓKER AUTÓ-és Alkatrészker.V.	5326
Bajatex	n.a
Budaflax	n.a
Budalakk	1406
Budapest Harisnyagyár	816
Budapesti Bútoripari V.	833
Budapesti Finomkötöttárugyár	364
DUNA Élelmiszer és Vegyiáru Ker.V.	1053
Hódmezővásárhelyi Mezőgép	532
Magyar Aszfalt	848
Nyiregyházi Mezőgazd.Gépgyár V.	72
Papíripari Vállalat	14963
REANÁL Finomvegyszergyár	900
TRIÁL Sport-Játék és Hangszerker	788
Üvegipari Művek	4649
<b>Total:</b>	<b>15 32850</b>

## 12. Enterprises involved in the Second Privatisation Program

Enterprises	Shareholder's fund million HUF
43.sz. Állami Épip.V.	1458
Agrikon Mezőg.és Élelm.ip.Ggy.V.	1182
Alföldi Cipőgyár	58
Alföldi Porcelángyár	1427
Április 4.Gépipari Művek	1296
Baranya Kereskedelmi V.	382
Baranya M. Tanácsi Magas-és Mélyép V.	164
BORSODI Ércelőkészítőmű	1928
Budapesti Édességbolt V.	99
Csepel Művek Szerszámgépgyár	1239
Dél-Budai Vendéglátó Vállalat	354
Déalföldi Téglá és Cserépip.V.	1146
DÉLTEX Kereskedelmi Vállalat	327
Duna Élelmiszerkeresk. Váll.	1035
Duna-Tisza Közi Állami Épip.Váll.	872
EFG Épip.Fémszerk.és Gépgyár V.	59
Építőipari Gépesítő Vállalat	1436
Észak-Budai Vendéglátó Váll.	370
Észak-Pesti Vendéglátó Vállalat	171
FÉG Fegyver-és Gázkészülékgyár	1572
GARZON Butorgyár	171
Gépipari Elektromos Karb.Váll./GELKA/	476
Győr m.Állami Épip. Vállalat	1897
Győr-Sopron M.Iparcikk Ker.V.	479
Győri Autójavító Vállalat	229
Győri Közúti Építő Vállalat	502
Harmónia Kereskedelmi Vállalat	90
Hazai Fésűfonó és Szövőgyár	914
Kaposvári Közúti Épip.Váll.	205
Kecskeméti Közúti Építő V.	225
Keletmagyaró.Állami Épip.V.	602
Keravill Kereskedelmi V.	908
Kéziszerszámgyár	627
KISKUN Cipőgyár	232
Kőfaragó és Épületszobrászip.V.	565
Kohászati Alapanyagelőkészítő V.	936
Korona Kereskedelmi Vállalat	192
Kossuth Nyomda	1479
Magyar Gyapjúfonó és Szövőgyár	315
Nyirtex Fonó-szövő Leányvállalat	14
Öntészeti Szolgáltató Vállalat	81
Paletta Kereskedelmi V.	470
Pannónia Szőrmekikész.Konf.és Ker.	325
Pápai Textilgyár	361
Pest m.Közúti Építő Vállalat	180
Révai Nyomda	417
Szabolcs Cipőgyár	69



Enterprises	Shareholder's fund million HUF	
Szabolcs-Szatmár M. Építő és Szerelő V.		76
Sigma Kereskedelmi Vállalat		323
Tapolcai Szigetelőanyaggyár		313
Vác és Környéke Élelmiszer kisk. V.		345
Vas m. Állami Építő Váll.		679
VASÉRT Vállalat		1185
Veszprém M. Vendéglátó V.		306
Vetőmagtermeltető és ért. V.		1628
VIDIA Kereskedelmi Vállalat		752
Visoram Szemüvegkeretgyár		45
Zalaegerszegi Közüti Építő V.		224
Total:	58	35412
Subtotal:	85	82451

### 13. Potential participants in the privatization program

Enterprises	Shareholder's fund million HUF
Agrikon Mezőg.és Élelm.ip.Ggy.V.	1182
Alföldi Cipőgyár	58
Április 4.Gépipari Művek	1296
Baranya Kereskedelmi V.	382
Baranya M. Tanácsi Magas- és Mélyép V.	164
BORSODI Ércelőkészítőmű	1928
Budapesti Édességbolt V.	99
DÉLTEX Kereskedelmi Vállalat	327
Duna Élelmiszerkeresk. Váll.	1035
EFG Épip.Fémszerk.és Gépgyár V.	59
Építőipari Gépesítő Vállalat	1436
Észak-Budai Vendéglátó Váll.	370
Észak-Pesti Vendéglátó Vállalat	171
FÉG Fegyver-és Gázkészülékgyár	1572
GARZON Butorgyár	171
Gépipari Elektromos	
Karb.Váll./GELKA/	476
Győr-Sopron M.Iparcikk Ker.V.	479
Győri Autójavító Vállalat	229
Harmónia Kereskedelmi Vállalat	90
Hazai Fésűfonó és Szövőgyár	914
Kéziszerszámgyár	627
KISKUN Cipőgyár	232
Kőfaragó és Épületszobrászip.V.	565
Kohászati Alapanyagelőkészítő V.	936
Korona Kereskedelmi Vállalat	192
Kossuth Nyomda	1479
Magyar Gyapjúfonó és Szövőgyár	315
Öntészeti Szolgáltató Vállalat	81
Pannónia Szőrmekikész.Konf.és Ker.	325
Pápai Textilgyár	361
Révai Nyomda	417
Szabolcs Cipőgyár	69
Szabolcs-Szatmár M.Építő és Szerelő V.	76
Sigma Kereskedelmi Vállalat	323
Tapolcai Szigetelőanyaggyár	313
Vác és Környéke Élelmiszer kisk.V.	345
VASÉRT Vállalat	1185
Veszprém M.Vendéglátó V.	306
Vetőmagtermeltető és ért.V.	1628
VIDIA Kereskedelmi Vállalat	752
<b>Total:</b>	<b>41</b> 22965

#### 14. Enterprises in the privatization program of the wine sector

Enterprises	Book value shareholder's fund million HUF/1
Economic associations:	
- Kecskemétvin RT	1185
- Pannonvin RT	738
- Promontorvin RT	579
State owned enterprises:	
- Hungarovin	1566.03
- Délalföldi pincegazdaság	598
State owned agricultural enterprises:	
- Balatonboglári Mezőgazdasági Kombinát	1292.62
- Szekszárdi Mezőgazdasági Kombinát	1121.97
- Hosszúhegyi Mezőgazdasági Kombinát	2233.96
- Izsáki Államigazdaság	676.15
- Helvéciai Államigazdaság	590.72
- Kiskörösi Államigazdaság	703.90
- Kiskunhalasi Államigazdaság	1186.38
- Badacsonyi Államigazdaság	591.37
- Móri Államigazdaság	400.00
- Soproni Államigazdaság	269.48
Total:	15 14467

## 15. Companies involved in the construction industry program

Enterprises	Book value of shareholder's fund million HUF	Estimated value during transaction million HUF
Győriterv	35.2	50
Szolnokterv	23.9	80
EVITERV	139.9	150
KOGÉPTERV	261.7	300
IPARTERV	161.0	600
KIPTERV	88.1	100
VIZITERV	280.5	300
ÉPBER	80.8	300
MÜBER	32.3	50
KOMBER	18.0	20
Kaposvári Közmű Ép. Váll.	185.8	250
Zalaegerszegi Közmű Ép. Váll.	214.2	250
Kecskeméti Közmű Ép. Váll.	208.0	250
Pest megyei Közmű Ép. Váll.	140.0	250
Győri Közmű Ép. Váll.	299.1	250
KEVIÉP	302.6	400
DUVIÉP	265.8	300
Dél-Dunántúli VIÉP	343.0	400
VIZÉP	624.7	700
KIPSZER Vállalatok	997.2	1000
Vas megyei ÁÉV	679.5	700
Komárom megyei ÁÉV	750.4	500
Tolna megyei ÁÉV	545.4	500
Borsod megyei ÁÉV	653.2	500
DÉLÉP	1182.4	1000
Győr megyei ÁÉV	1890.0	2000
Szolnok megyei ÁÉV	560.9	500
KEMÉV	602.2	600
ALTERRA	1161.7	1500
23. sz. ÁÉV	454.0	100
BULAV	504.1	600
BETONUT	1151.6	2000
Gép és Felvonószerelő	511.4	1000
ÉGSZI	903.0	1500
ETV	42.4	10
Total:	35	16281.1
		19010

## 16. State property owned by the State Property Agency

On 31 December, 1990	Million HUF
On December 31 (book value, together with insurance companies and financial inst.)	71,475.1
Upto 7 January, 1991	
- without insurance companies, financial institutions	57,622.5
- together with insurance companies, financial institutions	80,984.5
Upto 8 February, 1991	
- without insurance companies, financial institutions	69,153.2
- together with insurance companies, financial institutions	92,515.2
Upto 28 March, 1991	
- without insurance companies, financial institutions	70,752.2
- together with insurance companies, financial institutions	94,114.2
Upto 29 April, 1991	
- without insurance companies, financial institutions	71,611.6
- together with insurance companies, financial institutions	94,973.6

## 17. Privatisation Incomes

Year 1990

in 1000 HUF

1. Sale	623,507
2. Preprivatisation income	53,110

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Total:	676,617
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Year 1991(upto 30 April)

in 1000 HUF

1. Proceeds from property (payments of the retail trade units)	156,937
2. Rental fee (KAGE plc + payment of a retail trade unit)	4,807
3. Sale (together with income from the interest)	4,362,655

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Total:	4,524,399
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## 18. State property owned by the State Property Agency

In decreasing order according to the proportion of votes  
(29 April, 1991)

### A. Associations without financial institutions and insurance companies

	SPA particip. million HUF	SPA share of million HUF	Voting the SPA %
MAHART Rt.	3,710	3,710	100
VOLÁN TEFU Rt.	1,774	1,774	100
Zalaegerszegi Hűtőipari Kft.	764	764	100
IDEX Rt.	529	529	100
Ganz Árammérő Gyár Kft.	470	470	100
Üvegipari Gép- és Szerszámgyár Kft.	258.5	258.5	100
ERFATERV Kft.	49.4	49.4	100
DIMAG Rt.	11,396.1	11,390.2	99.9
Vegyépszer Rt.	2,032	2,030	99.9
Paletta-Ex Kft.	460.4	455.8	99
KORONA Nagyker. és Szolg. Rt.	310.2	300	96.7
FOKA Rt.	2,032	1,950	96
TRITEX Rt.	403.6	376.7	93.3
Tisza Cipő Rt.	1,850.8	1,717.9	92.8
Biogal Gyógyszergyár Rt. társ.nál maradó	3,090	618	
Richter Gedeon Rt.		2,245	92.6
KALIBER Kft.	12,417	11,490	92.5
Váci Nyomda Kft.	195	180	92.3
HUNICOOP Rt.	32.9	29.6	90
Statiquim Kiadó Kft.	149.5	132	88.3
Haldex Rt.	232	202	87.1
DEKO Rt.	293.9	254.8	86.7
társ.nál maradó	2,153	409	
ROYAL Bútorker Rt.		1,438	85.8
INVESTOR Rt.	1,305.6	1,116	85.5
Villanyszerelőip. Rt.	2,925	2,400	82
Pécsi Agroker Rt.	2,069.2	1,666.6	80.5
Kecskeméti Borg.Komb. társ.-nál maradó	752.9	577.3	76.7
Borsodi Sörgyár	1,120.6	187.2	
MŰÁRT Rt.		656.9	75.3
Hajdúsági Cukorgyár	1,800	1,338	74.3
Generál Autójav. és Ker. Kft.	1,250	928.9	74.3
	4,450	3,100	69.7
	42.1	29.1	69.1

	SPA particip. million HUF	SPA share of million HUF	Voting the SPA %
Styl Ruhagyár Rt. társ.nál maradó	481	66.8 264.6	68.9
Petőházi Cukorgyár Rt. társ.nál maradó	3,790.5	530.7 2,035.2	67.7
Zalaegersz. Ruhagyár Rt. társ.nál maradó	579.4	91 87.8	65.4
KAPOSCUKOR Rt. társ.nál maradó	2,570	354 1,305.5	64.6
Pannonvin Rt. társ.nál maradó	750	150 330	64
DÉLKER Rt. társ.nál maradó	1,831	293 856	62.7
IBUSZ Rt.	1,200	738.9	1.6
COMPACK-DOUWE EGBERTS Rt.	7,500	4,311.7	57.5
CHINOIN Rt.	4,000	2,100	52.5
Debreceni Bútoripari és Ker. Rt.	160	76.4	47.7
GySEV Rt.	1,125.8	514.9	45.7
Pécsi Építő Kft. társ.nál maradó	527	52.7 173.3	42.9
Petőfi Nyomda Rt. társ.nál maradó	978	160.2 247.8	41.7
Debreceni Magas-, Mély- és Útépítő Rt.	586.6	228.1	38.9
Egri Útépítő Rt.	480	90	39.6
ARBAU Építő Kft.	808	317.5	39.3
Ácsi Cukorgyár Rt. társ.nál maradó	760	120 148	35.2
GÉPFET Kft. társ.nál maradó	29	1.2 4.8	31.6
CARBON Rt. társ.nál maradó	420	42.6 84.3	30.2
Közúti Beruházó Kft. társ.nál maradó	136.7	22.8 13.7	26.7
Promontorvin Rt. társ.nál maradó	580.5	100 265.4	17.2
Volkswagen Kft.	141.4	23.3	16.5
Co-Nexus Rt.	53.4	6	11.2
Győri Keksz Kft.	1,828.7	73.1	4.0
Középülettervező Rt.	357	12.4	3.5
KAGE Rt.	588.8	244	-
<b>A Total</b>	<b>92.571,5</b>	<b>71.611,6</b>	



B. Financial institutions and insurance companies

	SPA particip. million HUF	SPA share of million HUF	Voting the SPA %
Állami Biztosító Rt.	2,000	2,000	100
Hungária Biztosító Rt.	3,700	1,887	51
Ált. Értékgorg. Bank Rt.	1,000	500	50
Magyar Hitelbank Rt.	13,983	6,900	49.3
Magyar Külker. Bank Rt.	7,125	3,150	44.2
Budapest Bank Rt.	6,585	2,750	41.7
Orsz. Ker. és Hitelb. Rt.	12,590	4,400	34.9
Ybl Bank Rt.	1,160	300	25.8
Ált. Vállalk. Bank Rt.	2,220.5	520	23.4
Postabank Rt.	4,000	805	20.1
Ipari Fejl. Bank Rt.	3,200	150	4.7
<b>B. Total</b>	<b>57.563,5</b>	<b>23.362</b>	
<b>A and B Total</b>	<b>150.135</b>	<b>94.973,6</b>	

**19. Economic associations transformed or  
1 March, 1990 under SPA's supervisor**

Names of the enterprises	Founding ministry	Basic capital million HUF	Property in the Voting share million HUF	Voting share of the SPA %
Ácsi Cukorgyár Rt.	MA	760	268	35
Pannonvin Rt.	MA	750	480	64
Promontorvin Rt.	MA	580	365	17.2
Kalocsakörnyéki Agráripari Rt.	MA	534	244	-
MAHART Rt.	MTC	3,710	3,710	100
VOLÁN TEFU Rt.	MTC	1,774	1,774	100
GySEV Rt.	MTC	1,126	515	46
Investor Kereskedelemfejl. Rt.	MTC	2,925	2,400	82
IBUSZ Rt.	MIT	1,200	739	62
Biogal Gyógyszergyár Rt.	MIT	3,090	2,863	93
Chinoín Gyógyszergyár Rt.	MIT	3,000	2,700	90
DIMAG Rt.	MIT	11,396	11,390	100
Ganz Árammérő Gyár Kft.	MIT	470	470	100
Styl Ruhagyár Rt.	MIT	481	331	69
Zalaegerszegi Ruhagyár Rt.	MIT	579	379	65
Debreceni Bútoripari és Ker. Rt.	MIT	160	76	65
Vegyépszer Rt.	MIT	2,032	2,030	100
<b>Total I</b>		<b>34,576</b>	<b>30,734</b>	<b>-</b>

*Pénzüintézetek, biztosítók*

Általános Értékforgalmi Bank Rt.	MF	1,000	500	50
Általános Vállalkozási Bank Rt.	MF	2,221	520	23
Budapest Bank Rt.	MF	6,585	2,750	42
Ipari Fejlesztési Bank Rt.	MF	3,200	150	5
Magyar Hitelbank Rt.	MF	13,983	6,900	49
Magyar Külkereskedelmi Bank Rt.	MF	7,125	3,150	44
Orsz. Keresk. és Hitelbank Rt.	MF	12,590	4,400	35
Postabank és Takarékpénztár Rt.	MF	4,000	805	20
Ybl Építőipari Innovációs Bank Rt.	MF	1,160	300	26
Állami Biztosító Rt.	MF	2,000	2,000	100
Hungária Biztosító Rt.	MF	3,700	1,887	51
<b>Total II</b>		<b>57,564</b>	<b>23,362</b>	<b>-</b>

<b>TOTAL AMOUNT OF RECEIVED PROPERTY</b>	<b>92,131</b>	<b>54,096</b>	<b>-</b>
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MF Ministry of Finance  
MA Ministry of Agricultural  
MTC Ministry of Transportation and Communication  
Mit Ministry of Industry and Trade

**20. First portfolio package**  
(managed from the first quarter of 1991)

Association	Share capital	SPA share	Shares kept by the association	Voting share of the SPA
	million HUF	million HUF	million HUF	%
Pécsi Agroker	752.9	115.5	461.8	76.7
Pécsi Építő Kft.	527.0	52.7	173.3	42.9
Egri Útépítő Kft.	480.0	190.0	-	39.6
Székesfehérvári Közúti Építő Kft. (ARBAU)*	808.0	317.5	-	39.3
CARBON Rt.	420.0	42.6	84.3	30.2
<b>Total</b>	<b>2,987.9</b>	<b>718.3</b>	<b>719.4</b>	

**21. Second portfolio package**  
(managed from the 3rd quarter of 1991)

Association	Share capital	SPA share	Shares kept by the association	Voting share of the SPA
	million HUF	million HUF	million HUF	%
KALIBER Kft.	195.0	180.0	-	92.3
HUNICOOP Rt.	149.5	132.0	-	88.3
STATIQUUM Kiadó Kft.*	232.0	202.0	-	87.1
HALDEX Rt.	293.9	254.8	-	86.7
ROYAL Bútorker Rt.*	1,305.6	1,116.0	-	85.5
ZAKO Rt.	579.4	91.0	287.8	65.4
DÉLKER Rt.	1,831.0	293.0	856.0	62.7
DEBMUT Rt.*	586.6	228.1	-	38.9
<b>Total:</b>	<b>5,173.0</b>	<b>2,496.9</b>	<b>1,143.8</b>	

\* Registration is in process

**22. First property management group**  
(managed from the 4th quarter of 1991)

Association	Share capital million HUF	SPA share million HUF	Shares kept by the association million HUF	Voting share of SPA %
Kabai Cukorgyár Rt.*	4,450.0	3,100.0	-	69.7
Petőházi Cukorgyár Rt.*	3,790.0	530.7	2,035.2	67.7
KAPOSCUKOR Rt.	2,570.0	354.0	1,305.5	64.6
Ácsi Cukorgyár Rt.	760.0	120.0	148.0	35.2
<b>Total</b>	<b>11,570.0</b>	<b>4,104.7</b>	<b>3,488.7</b>	

**23. Association in individual property management**  
(3rd-4th quarter of 1991)

Association	Share capital million HUF	SPA share million HUF	Shares kept by the association million HUF	Voting share of SPA %
FOKA Rt.*	2,032.0	1,950.0	-	96.0
Tisza Cipő Rt.	1,850.8	1,717.9	-	92.8
Biogal Gyógyszergyár Rt.	3,090.0	618.0	2,245.0	92.6
INVESTOR Rt.	2,925.0	2,400.0	-	82.0
<b>Total</b>	<b>9,897.8</b>	<b>6,685.9</b>	<b>2,245.0</b>	

\* Registration is in process

## 24. Associations in the First Privatisation Program

Association	Share capital million HUF	SPA share million HUF	Shares kept by the association million HUF	Voting share of the SPA %
VOLÁN TEFU Rt.	1,774.0	1,774.0	-	100.0
IDEX Rt.	529.0	529.0	-	100.0
TRITEX Rt.	403.6	376.7	-	93.3
Richter Gedeon Rt.	12,417.0	11,490.0	-	92.5
IBUSZ Rt.	1,200.0	738.9	-	61.6
<b>Total</b>	<b>16,323.6</b>	<b>14,908.6</b>	<b>-</b>	

## 25. Companies under registration process

Name of the company	Founding capital million HUF	Share of the State Property Agency million HUF	Share of the property remaining with the limiteda company million HUF	Propotion of the Satte Property Agency's votes %
Zalaegerszegi Hűtőipari Kft.	764.0	764.0	-	100.0
Üvegipari Gép- és Szerszámgyár Kft.	258.5	258.5	-	100.0
Váci Nyomda Kft.	32.9	29.6	-	90.0
Villany szerelőipari Rt.	2,069.2	1,666.6	-	80.5
Borsodi Sörgyár Rt.	1,800.0	1,338.0	-	74.3
Generál Kft.	42.1	29.1	-	69.1
Compact-Douwe Egberts Rt.	7,500.0	4,311.7	-	57.5
Középülettervező Rt.	357.0	12.4	-	3.5
MŰÁRT Rt.	1,250.0	194.0	734.9	74.3
<b>Total</b>	<b>14,073.7</b>	<b>8,603.9</b>	<b>734.9</b>	

## 26. Summary Table

Association	Share capital  millio HUF	SPA share  millio HUF	Shares kept by the association millio HUF
First portfolio package	2,987.9	718.3	719.4
Second portfolio package	5,173.0	2,496.9	1,143.8
First collective package	11,570.0	4,104.7	3,488.7
Limited companies given to trusts	9,897.8	6,685.9	2,245.0
<b>Subtotal:</b>	<b>29,628.7</b>	<b>14,005.8</b>	<b>7,596.9</b>
Number of limited companies the registration of which is in process	14,073.7	8,603.9	734.9
Financial institutions, insurance companies	57,563.5	23,362.0	-
Companies involved in the First Privatisation Program	16,323.6	14,908.6	-
Other	32,545.5	22,540.3	3,221.2
<b>Total:</b>	<b>150,135.0</b>	<b>83,420.6</b>	<b>11,553.0</b>

## 27. Preprivatisation table

(Upto 16 May, 1991))

	Catering	Trade	Service industry	Total
Number of businesses offered for auction up to the present	73	96	15	184
Number of businesses not sold	42	40	7	89
Number of business sold	31	56	8	95
Purchase of businesses for cash	8	19	4	31
Credit	24	37	4	65

### Income from preprivatisation

	Total Proceeds 1000 HUF	Privatisation expenses 1000 HUF	Share of self government 1000 HUF	Share of the SPA (paying back state debt.) 1000 HUF
From the sale of businesses	373,825	12,046	167,079.5	194,719.5
From the sale of shareholdings of limited companies	16,200	70	-	16,130
Other income	328,991	-	-	328,991
<b>Total:</b>	<b>719,016</b>	<b>12,116</b>	<b>167,079.5</b>	<b>539,840.5</b>

## 27/A Preprivatisation Program Directorate of the State Property Agency

Practical information  
(main general data)  
concerning  
the implementation  
of Law  
LXXIV. 1990

	May 15 1991	May 24 1991	May 31 1991	June 15 1991	June 30 1991	July 31 1991	August 27 1991
Number of companies having registered reports	366	366	366	367	367	371	371
Number of businesses having registered reports:	10,024	10,028	10,033	10,034	10,054	10,170	10,193
- real estate	2,909	2,909	2,909	2,909	2,909	2,915	2,918
- leasing right to premises	7,115	7,119	7,124	7,125	7,145	7,255	7,275
Prepared to privatisation	4,105	4,817	5,009	5,090	5,097	5,279	4,983
Property evaluations has been carried out	1,033	1,040	1,052	1,153	1,411	1,580	1,936
- is being announced	799	911	961	1,114	1,210	1,233	1,471
Number of AUCTIONS I carried out	184	260	356	418	491	687	832
Number of AUCTIONS I carried out	0	0	3	3	12	16	21
Total:	184	260	359	21	503	703	853
Sold business on auctions	95	151	186	203	272	429	511
Other way of privatization	4	4	4	4	4	4	4
Total number of business sold	99	155	190	207	276	433	515
Gross sum of sale prices (HUF)	373,081,000	593,033,000	725,112,000	803,054,000	1,102,219,000	1,602,710,000	1,829,952
Reserve price of business sold	621,879,931	686,784,799	910,172,585	1,008,494,711	1,260,861,000	1,371,811,000	1,447,741
Sale prices as a percentage of the reserve price	116.6%	117.1%	121.1	122.9%	127.11%	126.32%	126.40%
Percentage of the successful auctions	52.9%	49.2%	54.9%	57.6%	61.6%	60.0%	60.4%
Sale - for cash	62	64	69	94	172	203	214
- on credit	124	139	203	222	257	275	297
- real estate	19	47	60	63	70	81	115
- leasing right for premises	76	104	126	138	202	235	314
In the sale schedule further items are planned	4,010	4,666	4,819	4,883	4,821	4,877	4,846
- in 1991	2,510	2,536	2,489	2,476	2,438	2,260	2,159
- in 1992	1,172	1,178	1,171	1,160	1,166	1,039	1,075
- from 1993	1,137	1,169	1,161	1,241	1,242	1,237	1,235
- possibility of sale has not been examined yet (legal, record keeping, etc.)	2,485	2,383	2,394	2,325	2,231	2,210	2,237
* Units operating privately condominium: cooperative ownership							
not liable to privatisation	2,543	2,565	2,567	2,630	2,664	2,970	2,977



## 28. List of building in downtown office building program

- 1055 Budapest, Bajcsy Zs. út 57.  
Area: 3.278 m<sup>2</sup>  
AGROTEK Mezőgazdasági Termelőeszköz Kereskedelmi Vállalat
- 1054 Budapest, Széchenyi rkp. 3.  
Area: 5.438 m<sup>2</sup>  
ERŐTERV Erőmű- és Hálózattervező Vállalat
- 1051 Budapest, Nádor u. 11.  
Area: 2.728 m<sup>2</sup>  
ELEKTROIMPEX Magyar Külkereskedelmi Vállalat
- 1051 Budapest, Nádor u. 21.  
Area: 2.923 m<sup>2</sup>  
METRIMPEX Magyar Műszeripari Külkereskedelmi Vállalat
- 1056 Budapest, Váci u. 38.  
Area: 17.098 m<sup>2</sup>  
MOGŰRT Gépjármű Külkereskedelmi Vállalat
- 1027 Budapest, Csalogány u. 23.  
Area: 1.561 m<sup>2</sup>  
ÉTV Építésügyi Továbbképző Vállalat
- 1052 Budapest, Deák F. u. 10.  
Area: 3.954 m<sup>2</sup>  
Középülettervező Vállalat
- 1051 Budapest, Arany J. u. 24.  
Area: 6.264 m<sup>2</sup>  
Ipari Informatikai Központ
- 1054 Budapest, Kozma F. u. 3.  
Area: 2.300 m<sup>2</sup>  
Vegyipari Termelőeszközkereskedelmi Vállalat (VEGYTEK)
- 1075 Budapest, Asbóth u. 9/11.  
Area: 3.622 m<sup>2</sup>  
Tervezés-fejlesztési és Technikai Építészeti Intézet (TIPUSTERV)
- 1075 Budapest, Madách I. tér 4.  
Area: 3.281 m<sup>2</sup>  
Lakó- és Kommunális Épület Tervező Vállalat (LAKOTERV)
- 1052 Budapest, Deák F. u. 10.  
Area: 3.954 m<sup>2</sup>  
Ipari Épülettervező Vállalat (IPARTERV)

## 29. Employees' ownership

Name of the limited company	Founding capital million HUF	Employees' property million HUF	%	Applied solution and concession
IBUSZ*	1200	40		rconcession for paying in installments
CHINOIN	4000	300	7.5	concession for paying in installments and discount
GRABOPLAST	1400	50	3.6	concession for paying in installments and discount
Villanyszerelő- ipari Vállalat	2069.2	121.5	5.9	employees are owners as small investors transformation of property bonds (the issue of free employees' shares is to be expected)
Tisza Cipőgyár	1850.8	200		Employees's shares sold by the State Property Agency are obtainable from the founding capital by payment of 10% of their nominal value. This has to be paid in a lump sum, the rest over 3 years.
		0.5		
Szerencsi Cukorgyár	1750	175	10.0	Free employees's shares
Szolnoki Cukorgyár	3600	115	3.1	Exchange of property bond
AMFORA*	1350	85		with a 50% discount by way of transformation of the property bond
		90		
		180	13.3	
BÖRKER*		80		The State Property Agency provides employees's shares at a 50% discount from the surplus above the founding capital
		145		
OFOTÉRT*			10.0	Employees' shares which can be issued from the surplus above the founding capital The provision of employees's shares at a 50% discount from the surplus above the founding capital
		150		

\* Planned share of employees from the planned transformation in process

## 29. Employees' ownership

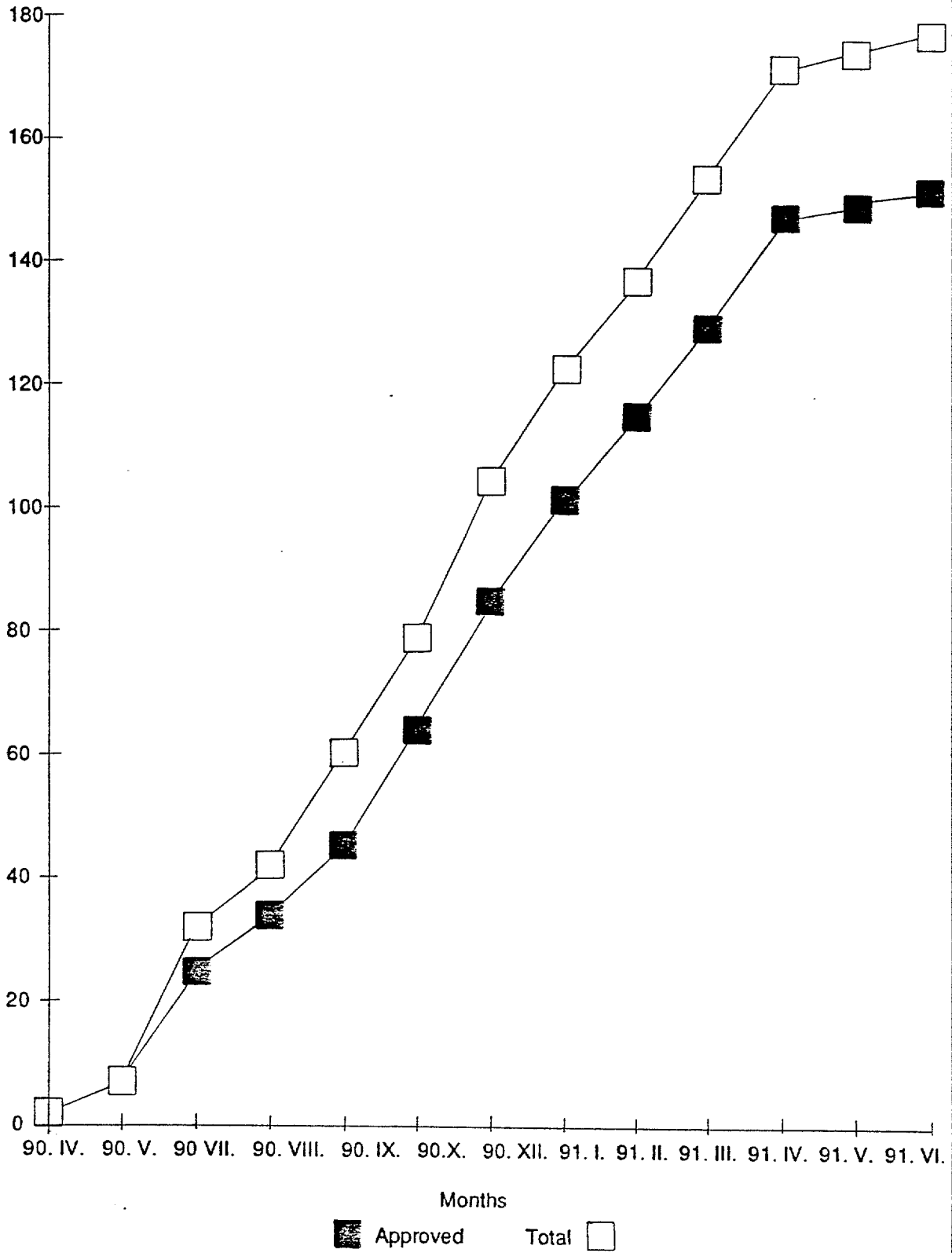
Name of the limited company	Founding capital million HUF	Employees's property million HUF	%	Applied solution and concession
DÉLKER	1831	80	4.3	concessions as regards price and payment in installments; employees must pay 60% of the nominal value of the shares; 20% of this is a deposit, the remainder to be paid in installments over 3 years from the annual dividend.
KNER	950	16.3	1.7	to be debited from the founding capital to be raised later; 50% free, the remainder with a concession for payment in installments.
DOMUS	1733	20	1.15	free
KÖZTI	313	160	51.0	with a 50% discount (pay for one and receive two).
CAOLA	3260	326	10.0	maximum concession 163 million HUF
ÉSZAKKÖ	470	16	3.4	being out by employees.
PANNONPLAST*			5.0	installment concession over 6 months
	2.6			transformation of property bonds into normal shares
	87.9			transformation of property bonds into employees shares.
BUSZESZ*	2571			employees pay 10% of the nominal value of the shares.
Richter Gedeon Rt	12417	740		transformation of property bonds:
		60	6.4	free divided into priority shares
				free divided into purchased normal shares
Pécsi Bőrgyár*			3.0	
Egri Utépítő RT**	480	58	10.0	employees's shares
Kaposvári Cukorgyár**	2570	308.4	10.0	employees's shares
Petőfi Nyomda**	978	117	10.0	employees's shares
Petőházi Cukorgyár**	3791	455	10.0	employees's shares
Pécsi Agroker	751	12.2	1.6	normal shares

\*\* Opportunity provided by the law, it depends on the decision of the limited company.

## 29. Employees' ownership

Name of the limited company	Founding capital million HUF	Employees's property million HUF	%	Applied solution and concession
Volkswagen Obudai Autójavító	116.4	116.4	100.0	complete buy out by employees
Borsodi Sörgyár	1800	216	10.0	employees's shares
COMPACK	7500	375	5.0	employees's shares
Gardénia	626	40	6.0	employees's shares
GENERÁL Autójavító	42.1	5 6.3	10.0 12.5	employees's shares concessionary purchase
Hajdúsági Cukorgyár**	4450	534	10.0	employees's shares
Alfa Élelmiszer és Vegyárú Ker. V.	2642	100	3.8	employees's shares
Bácska Ker. V.	216	21.6 32.4 75.6	10.0 15.0 35.0	employees's shares 50% concession full price buy out
Paletta Ker. Váll.	457	68.6	15.0	50% concession
<b>Total:</b>		<b>4309.9</b>		
<b>Sum Total:</b>		<b>5782.3</b>		

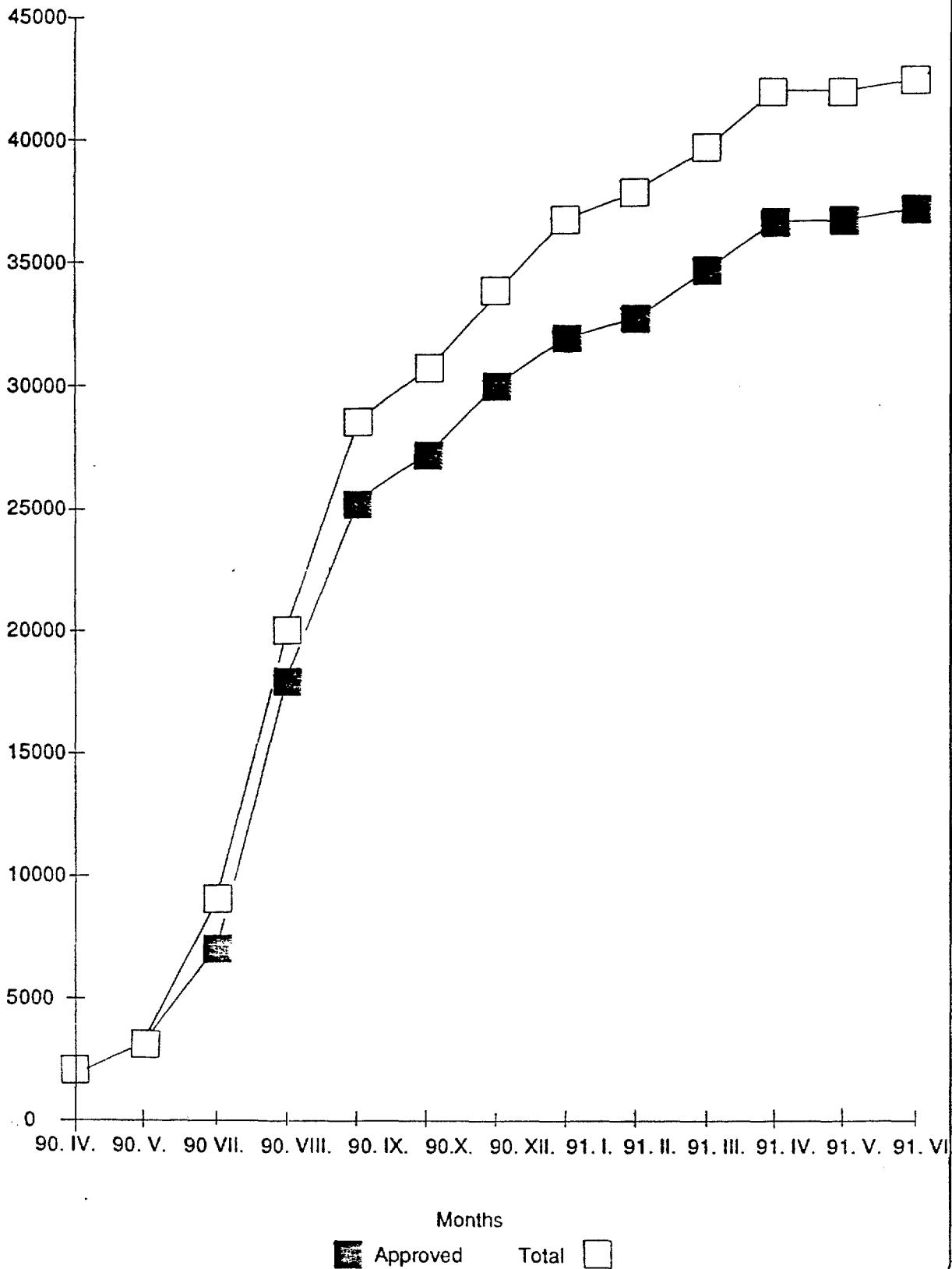
Table 30  
 Number of transactions carried out under the property  
 protection law (accumulated)



195

Table 31

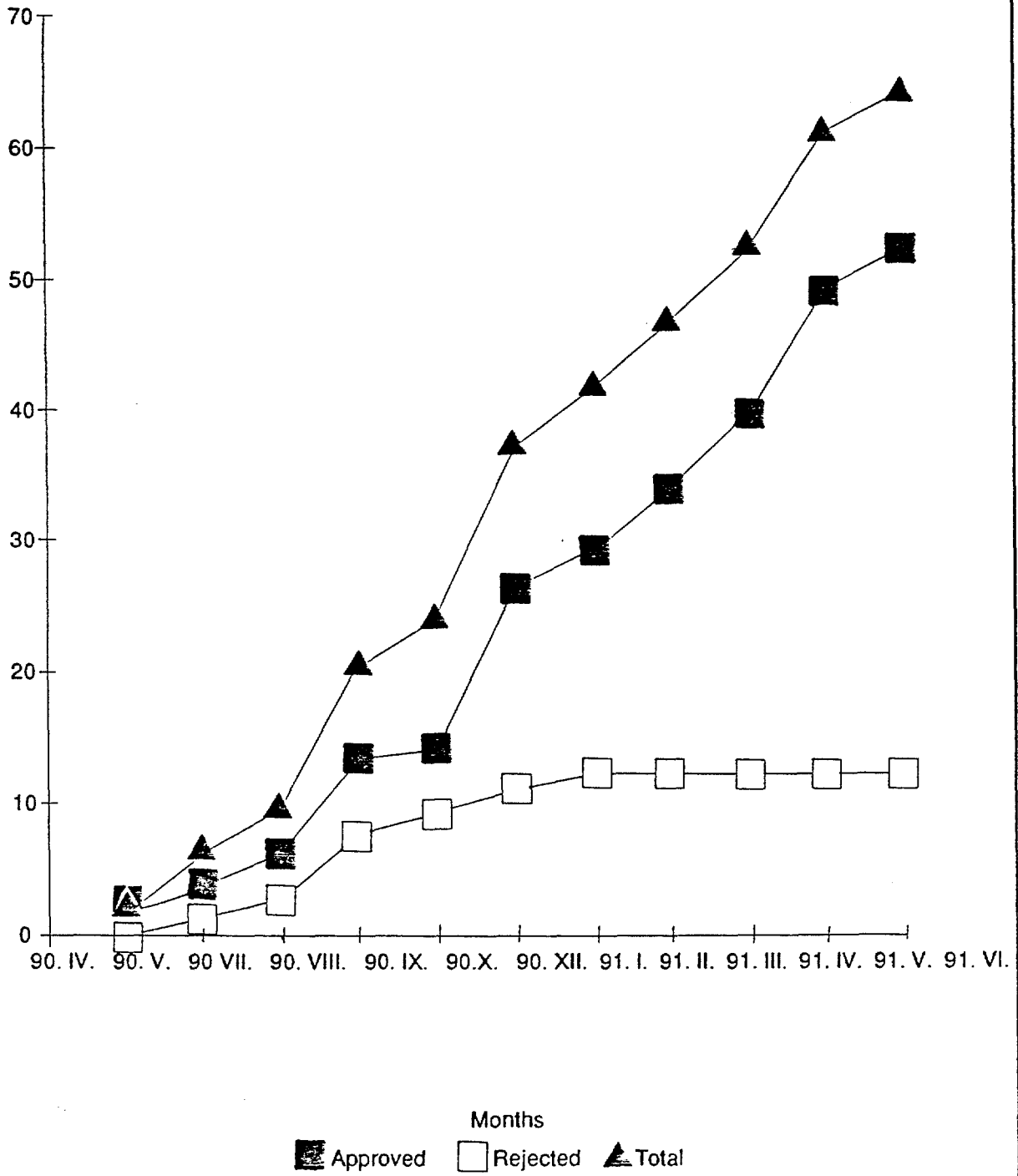
Value of transactions carried out under the property protection law according to the contracts (accumulated)



196

Table 32

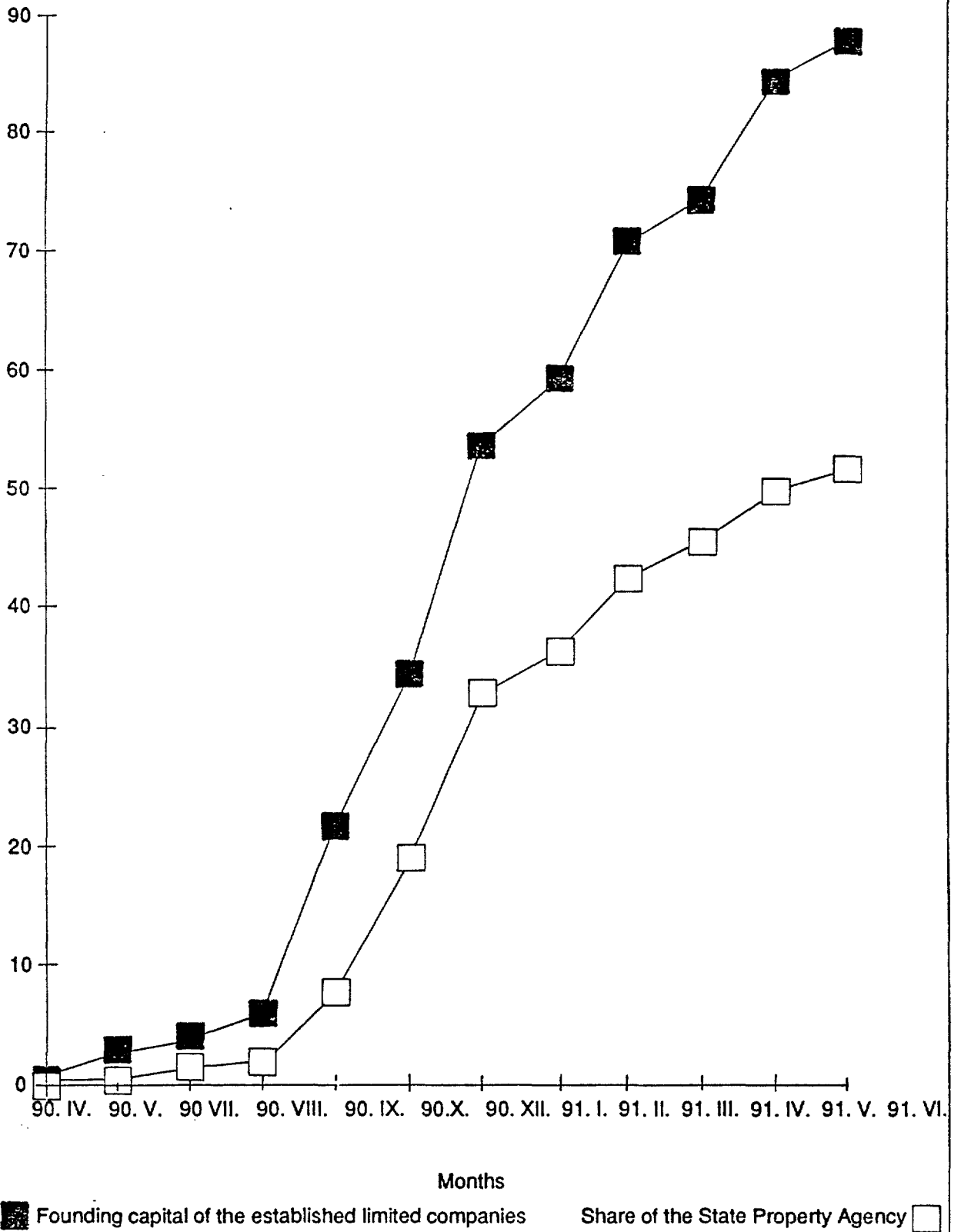
Number of transactions carried out under the transformation law (accumulated)



197

Table 33

Value of transactions carried out under the transformation law according to the contracts (accumulated)



198



## I

### PRIVATIZATION: AN IDEA SEARCHING FOR A DEFINITION

Privatization is a concept that has continuing and constructive use when it is applied in a broad context. The unprecedented scale of Privatization in Central Europe makes helpful a further examination of the concept.

A competitive free market economy is the objective of much of the change in Central Europe and Privatization is a synonym that further defines that end. Privatization (with a capital P) must not be limited to use as a means. If it is restricted to describing the detail of carrying out the steps that move you toward the Privatization ideal, the word can confuse and does not clarify.

For instance if you simply gave away every state enterprise to private individuals you would "privatize" your assets but you would not necessarily have Privatized your system. The Privatization concept does not stop with ownership transfer. It continues to be a necessary lens through which to view the economic system even if you have achieved full nominal asset ownership transfer to the private sector.

There are words that more precisely describe most of the processes that underpin and are subsumed by Privatization; Companies Act, Investment code, Independent Accounting Standards, liquidation, joint ventures, management agreements, asset sales, private ownership, etc. However the term Privatization does help communicate when properly used and can be an anchor upon which many related ideas can rely.

## II

### PRIVATIZATION: THINGS IT IS

#### Privatization: Is individual responsibility

Privatization is aimed at the goal of removing the detailed management of a society's economy from the government's hands and placing it predominantly into the hands of private individuals. These individuals, acting as owner, consumer, shareholder etc. create the market forces that balance the economy.

Privatization has profound assumptions built into it about limiting the role of the state and increasing the requirement for the individual to make choices that effect his private, particularly economic, life. You don't privatize for its own sake, you are instead committing yourself to achieve greater economic and social efficiency through constraining the role of Government and increasing the responsibilities of the individual. You are decentralizing the decision making process particularly at the operating level of the economy and the remaining centralized decisions are to be taken with that first premise in mind.

### Privatization: Is a vision and a political process

Privatization is part of a vision, a philosophical, political, economic and social vision. It is not a uniform vision in its detail and timing from setting to setting. What is the route for instance to Privatization in Hungary may be different in detail and timing from what can and should happen in Poland. The nature and extent of the shared vision of the nation and the degree to which that vision can and should encompass (at a given point in time) some or all of the many definable parts of the Privatization process is a difficult call.

That Privatization is a "political process" is the shorthand way of assigning to the realm of the art of leadership the responsibility for the choosing the appropriate implementation steps and their timing to achieve the Privatization vision. More precisely the success of the process is dependent on a leadership's commitment to the Privatization vision which they achieve through the art of doing what is politically possible.

The minimum requirement is that the political and technocratic leadership of the nation use as one of the tests of a given action or lack of it, its effect on the Privatization process. This shared vision and screen for the nation's decision making should yield the necessary consistency; tax laws that support taking ownership risk, property laws that are clear and secure, investment laws that are simple and competitive, company registration procedures that are rapid and efficient, environmental guidelines that are fair and reflect international standards, and yes even the transfer of the management and ownership of government assets and services into private hands - which by itself is the small "p" privatization.

### Privatization: Must be a shared vision

The advent of individual political freedom is difficult to integrate into Central European cultures in spite of its wide spread nominal acceptance. Adding its natural corollary, individual economic freedom, moves into an area where the consensus is still forming. Without a consensus and the related political will to support it, the Privatization vision will suffer corruption and subsequent disfavor. Each culture can integrate Privatization into its process of change, each however has its own appropriate pace.

For instance the consensus in Hungary is that the present appropriate focus of the revolution underway in Hungary is economic. The revolution in Czechoslovakia is still broadly perceived within Czechoslovakia as principally a political and social phenomena. It is therefore no surprise that the strength of the political and social will in the two environments to support the detailed implementation steps of the Privatization vision are very different. As a result the institutional changes relating to land title, the reduction of government subsidies, the pace of reduction and ultimate limit of government's role are on quite different tracks with different timetables in the two nations. Both approaches are correct if they work within their respective settings. Only hindsight will be able to judge if the differing approaches actually worked equally well or at all.

While there is no text book answer on how a given culture can achieve the economic and social ends included in the Privatization vision, it is very clear that unless there is a consensus as to what is happening, particularly during a period of economic stress and hardship, that the Privatization vision is at risk.

### Privatization: Requires communication

Privatization is a relatively new phenomena and very sensitive to what happens as the process moves forward. In the Hungarian case the vision has been cast as a centerpiece of the process of change. The delicate task of leadership is to forge what can be done when it can be done and move ahead. As important is the requirement that the technocratic keepers of the vision broadly disseminate the victories and ramifications of the process and continually define what it means and is coming to mean.

There is a constant need to increase the information level and support of the Privatization vision. If there is a rule to adhere to in Privatization it is to communicate; often, clearly, and consistently. Infrequent, imprecise, or an inconsistent communications strategy can do great damage. Poor communications even with real achievements can also be a recipe for disaster. The linkage between communications, accountability, transparency, and involving society in the process of privatization must be deliberate and constantly reinforced.

### Privatization: Institutionalizes pragmatism

Interestingly the rule governing the interaction of parts of the Privatization equation: Does it work? Does it support and advance the direction of the process? Is it necessary to the process?, is the same as the one that must underlie a competitive market economy namely responsiveness. Moving in the direction of a privatized economy requires feedback and rapid response to that feedback or there is a risk of stalling the process. If a producer in a competitive market economy stops responding to his customers he can be stalled in short order. That is the rule, that is why it works.

Privatization is national culture and transaction specific. What is "works" in Hungary at a point may not "work" in Poland at the same or any time. While one enterprise deserves liquidation the next may merit public listing. The test in all instances is what can be achieved. It is the market in the widest sense that decides

### Privatization: Assumes that change is the norm

The core of Privatization is that it allows individuals to make the bulk of the economic decisions in the society. The assumption is that individuals will be more successful on average in recognizing and adapting to changes than a centralized state. (In Central Europe this belief is footnoted with 40 plus numbing years of experience with the reverse assumption) Privatization assumes that change is the norm and that the process must permit change to occur rapidly and at the least cost.

If Privatization assumes change is the norm then Privatization is actually a dynamic and continuing process not an event or definite series of events. If the tax laws of the major market economies come in ring binders, is that some indication that something is still going on? If the public subsidies explicit in the Common Agricultural Policy (CAP) confounds both the EC "wanna bes" in the former COMECON and EFTA and the EC "wanna sells" like the USA and Australia then the border lines of the meaning and practice of the "Privatization" idea are still under negotiation.

### III

#### PRIVATIZATION: THE MECHANICS

##### Privatization: Central Europe, the need to change the system

Privatization is being embraced -with varying degrees of conviction- in Central Europe because government managed command economies could not make (or would not let) an economy work. In Central Europe the Privatization vision's objectives encompass both the establishment of the complex interrelated support system that make a competitive market economy function and undertaking the individual transactions and putting in place the laws that help it happen.

In Central Europe the economic and to a large part the social system is being constructed anew. The individual steps along the way range from changes in the accounting law to transparency in government. To constrain the meaning of the word Privatization to transferring control of an enterprise to private managers/operators thus excluding rewriting the tax laws -corporate and individual-, opening markets to competition, and many other vital links, misses major components of the concept.

##### Privatization: Not just deal making

Selling enterprises, mergers & acquisitions, legal due diligence, valuations, bankruptcy laws, companies acts, independently verified accounts according to uniform standards, all have a place in Privatization but each has no exclusive claim on the word.

Privatization has very limited meaning and marginal usefulness without a realization that Privatization concerns achieving a proper and changing interrelationship of many variables within a broad economic and social framework.

If you simply sell nominal control of assets to a private individual but tax him out of existence, make it impossible to buy raw materials or sell goods, give him no ability to deal with his inputs -labor, land, capital, ideas, etc.- and call the transfer of control of the asset "privatization" then you have defined the Privatization phenomena such that it will self destruct.

If you open entry into an industry like tourism and make presently government owned agencies function (or fail) alongside and in unsubsidized competition with the private sector, you may have "Privatized" the industry though you haven't sold a bit of it.

Which is Privatization?

### Privatization: How to measure a point of view

As much of life is measured by what is achieved, people focus on "transactions" to define Privatization. There is a great deal to be said for managing Privatization against objectives and scorecards; number of enterprises sold, investment dollars received. Managing Privatization against its objectives is explicit in the conditionality concept of the World Bank and the IMF among others. But it deserves underlining that the IMF and World Bank scorecard expands the Privatization and market economy scorecard to include the tough transactions; revised tax codes, financial sector reform in its many forms, revised accounting standards, the control of inflation, and fiscal responsibility.

The problem with transactions is they can become an end in themselves and statistics can mislead and worse. The "body count" mentality can cause a significant skewing of resource commitment away from necessary means and into short term ends with not surprising long-term poor results. A command economy that govern's its private sector to failure can give you the private sector ownership statistics and an economic failure. A voucher system can be heralded as creating statistical owners where it only continues the tradition of the "ownership of the people" which has turned out to be non-ownership. A public monopoly sold as a private monopoly with no attention to the continuing problem of no competition is a misleading statistic. In short the statistical game in Privatization can be as damaging or useful as in any other situation and it must be carefully used and managed.

### Privatization: Assets not going concerns

The most common transaction related misconception is that successfully privatizing an asset necessarily involves selling it as a going concern. From the standpoint of Privatization objectives a liquidation, with or without a bankruptcy, can be viewed as equally successful. The objective of Privatization in any sales transaction is to place non-productive (or productive for that matter) government owned and/or managed assets by whatever means into play where their use will be determined by market forces.

The Privatization assumption, when focussed on the transfer of control over assets -land, labor, capital, etc.- is that the Government has a well documented record as a poor asset manager. The private sector seems to, on average, manage such assets more efficiently. If not more efficiently then at least not at the cost of the general population via government subsidies!

### Privatization: restructuring it isn't

If the going concern sale is the most common misconception that tries to limit Privatization, "restructuring" is the most inappropriate idea that tries to get its nose into the Privatization tent.

Restructuring is classically cast as a necessary precondition to an enterprises privatization so that a fair price or a smooth transition can be realized. Sounds good, now let's look for the devil in the fine print.

If the restructuring goal is to position the enterprise for sale; order its financial house by undertaking professional audits, clearly establish title status and the condition of assets, clearly define liabilities and perhaps begin to resolve liabilities -actual or contingent- that may impinge on a sale, start dealing with issues like worker retraining or redundancies, maybe you are on track.

What are restructuring Trojan horses that would be pleased to fly the Privatization banner but in fact delay actual privatization and add to its cost?

Strategic/Infant Industry: The industry is critical to the survival, defense, or whatever of the nation. If raising this argument doesn't keep the industry off of the Privatization hit list the argument is that unless it is restructured for possible placement in the private sector as a strong going concern the state will suffer. Thus we must recapitalize it, build the new assembly line, launch the new product innovation that was planned. Thus business as usual, same place, same people, same rules, the nation's money their brains. This is usually coupled with the infant industry protection argument never mind if the enterprise's problem is rather more precisely geriatric than infant.

The Privatization vision says we need new brains that are spending their own money. Let whoever has the money do the restructuring. The general population has already paid more than its dues.

Truly Strategic Industry: They do exist, though what so qualifies may change over time. The Central European situation is that most such large industries are very complex horizontally and vertically integrated operations with "congenerics" to their core industry (which may be for instance telecommunications) like pubs, car rental agencies, and major employee holiday resort complexes. While the industry may be strategic and may be due some support for various reasons, it may well have parts that could well benefit from privatization and/or no support nor continued subsidization. The telecommunications example may have certain core activities that the government may wish to keep under its direct control but there are many areas that can be controlled at much less expense through licensing and regulation thus avoiding new investment cost and control problems.

Polish the family silver: The enterprise represents an investment of the state of xxx, xxx, xxx and to get that plus a deserved premium you need to bring it up to standard so that you can sell it at the best price (if indeed you are foolish enough to want to sell such a valuable item). Somehow the managers or founding ministry or enterprise have now found the market secret that will enable them with a few more xxx,xxx,xxx s to create the perfect package for sale in the market. The privatization vision says we haven't got it right before, what's changed? No new money.

Save jobs\*: The enterprise employs xx,000 voters (a delightful newly rediscovered problem in Central Europe). You must keep them working and restructure to do that. The privatization vision may quite fairly say for those who must foot significant bills to pay the relatively few that it is probably cheaper to pay them unemployment and retrain them both in the short and long term.

\* The employment issue however must be dealt with sensitively and appropriately It must be dealt with early, often, systematically, and fairly. The socially responsible "safety net" is a critical component of Privatization with the capital P.

#### IV

#### PRIVATIZATION: THE PRIVATE SECTOR IS HUMAN

Privatization isn't an "ism". It observes only that there is a high correlation between a competitive privately controlled market economy and economic and social growth and prosperity. Privatization does not presuppose to give "capitalism", "fascism" or any other "ism" its particular endorsement. It most particularly does not presuppose that just because something arises from the private sector it should be embraced. We have noted Privatization is focussed on trying to make several things happen. It endorses that a government should govern and help set the rules of play. To make the point it is worth while noting some examples of where governance was needed to protect Privatization from the private sector!

#### EXAMPLES:

1

Modest Proposal: A strong international competitor in the oil industry proposes that in return for an exclusive market position it will gradually manage a national petroleum industry support company out of bad times. They argue that the support company for the first few years will not be able to compete technically or even in price with similar companies from other markets and needs a strong protected local market position. In short the private sector makes the infant industry argument and offers in return for a few more years low technology high priced support for the nation's oil industry that they will try to turn-around an indigenous operation.

Privatization vision response: Competition is part of the game. The same problem exists in a government or private monopoly that doesn't have to compete. Why should our economy continue to have to subsidize high cost low quality work to the detriment of our industrial base? Make me a better deal.

Modest Proposal: A very strong air carrier from a nearby country proposes to integrate the national carrier into its network, increasing flight frequency, integrating the air fleets, and providing maintenance and aircrews within their existing system. They are willing to pay a very full price.

Privatization vision response: We welcome value added and competition. A carrier from outside the region with a strong technical capability wants to build us into a regional hub for service, maintenance, and aircrew training. They are willing to pay a reasonable price and commit to a long term investment strategy. By comparison the regional carrier's Modest Proposal is viewed in part as a preemptive anticompetitive move.

Modest Proposal: A financing consortium proposes to purchase a large, nationally important and apparently viable operation in a growth industry. They propose to bring in management teams, which they will find, and recapitalize, breakup, or do whatever is required to make the operation work. Their price appears to be market.

Privatization vision response: What is the value added you propose? Where in your team is the demonstrated industry expertise and commitment to make the operation viable? How is what you proposed different from an LBO of the type that is typically followed by asset stripping to pay you out with a subsequent resale of the remainder with no attention to the underlying assets? The nation wants the assets better used now. There is no reason to allow a bonus to be paid for undervalued asset to a non-operator who is most unlikely to reinvest it in the operation.



PRIVATIZATION - CONCLUSIONS

Privatization is a broad and evolving vision. It focuses on making individuals decide their economic actions rather than governments. Privatization, like the market process it supports, must be dynamic, responsive and pragmatic.

Moving a nation in the direction of the Privatization vision is a interactive communication and education process. The political will and skill to manage the movement of the nation toward the new vision is the most important part of the process. This political management is highly communications dependent.

For a nation Privatization is meant to achieve the effective responsible management of assets. Privatization is not transactions alone and transactions alone may not be Privatization. Ownership alone is not a measure, but the linkage of ownership to responsibility and the power to act usually is.

There is no textbook on how to Privatize a nation. There are signposts, processes, transactions, and laws that can advance the process if appropriately used at the proper time.

Privatization is focussed and pragmatic. If it doesn't make sense, don't do it, restructuring is typically a case in point. Because something is private means its good is not a reasonable assumption. Privatization does not endorse the concept that all private is good and everything else is bad. Privatization does hold a very clear and important role for government as a governor. Privatization has a very low opinion of government as an owner/manager.

THE AUTHOR: Charles G. Twyman is a privatization consultant working for the international accounting/consulting firm Deloitte and Touche. He has a development economics academic background and commercial and merchant banking professional experience gained mostly in the third world. He has been involved in executing privatization programs for over 5 years, first in Africa and currently as a policy advisor within the Hungarian privatization agency. The present article distills some of his thoughts on Privatization as he has seen and helped it develop.

So much for theory. Let's look at a cases and see if the strands of a privatization vision and the complex interrelationship of means to achieve that vision can be viewed in a real world context. I propose using Hungary as an example. It is committed to dramatic economic reform with privatization as a focus. It is the reform leader in Central Europe. It has set out in concrete legislation and government programs how it hopes to achieve its economic vision. Most encouragingly the Hungarian people, of the countries of Central Europe, appear to have the best developed distrust of Government combined with significant individual self-confidence albeit overlain by Hungary's well developed pessimism. The end result is a willingness to get through what will be a difficult transition period if it achieves getting their lives back in their own hands. The question of how much difficulty they can sustain and what is the correct public/private mix is still open and evolving -as it is in the USA and UK among other places-. There is a consensus that what was shall not be again.

Hungary's economic revolution has been underway for some time. The pragmatic Hungarian with their significant lack of respect for anything non-Hungarian and particularly Russian initiated key reforms and allowed the development of alternative Hungarian thinking and practices even while the nominal system wasn't changed. The "peaceful revolution" which culminated in free parliamentary elections and the 23 May 1990 set out "The strategic goal of the government's programme is to restore economic freedom to people in their individual and collective life and to reconstruct their communities - - - A central feature, in fact the foundation stone of the government's economic policy, is privatization:"

There is a strong political consensus that privatization of the economy "...and the adjustment capacity of the entrepreneurs." is the lasting foundation for economic growth.

MEMORANDUM

TO :USAID Representative in Budapest, Mr. David Cowles  
FROM :State Property Agency, Long Term Adviser, Charles G. Twyman  
DATE :29 August, 1991

REFERENCE: Example of close field cooperation of US aid Efforts

BACKGROUND: The U.S. Government (USG) has been supporting through the United States Agency for International Development (USAID) the privatization agency of the Government of Hungary (GOH) the State Property Agency (SPA) since before its formal inception. This assistance initially launched by the U.S. Embassy in Budapest has consisted of training, equipment, technical assistance to design and implement a training program, a Management Information System, a Long Term Advisor (LTA), public information and other Technical Assistance (TA).

TRAINING REQUEST: Some months ago the SPA requested assistance of the USG through USAID to fund training at the International Law Institute (ILI) (a school well known to USAID) in Washington D.C.

The total costs -transport, tuition, per-diem- is about US\$26,306 for three students. The transport cost is borne for two of the students by the World Bank (WB) as the SPA is dovetailing a WB contracting course to the end of the ILI course. (The WB is funding the SPA at the level of US\$10.5 million for assistance with major privatization transaction related costs which costs -if paid with WB funds- must be paid in accord with WB contracting requirements)

The two ILI courses (Foreign Investment Negotiation and International Arbitration) were identified by the USAID funded training consultants and the Director of the SPA's legal department as being well suited to the needs of the SPA's senior legal staff. These course represent their day to day work and a perfect fit into the training and investment realities in Hungary. (The SPA has training funding for European based training from the Economic Community's (EC) PHARE grant program, however US based training cannot be funded through PHARE. The US is a preferred investor in Hungary and the largest single investor in Hungary in total amount. In addition the Hungarians have a preference for US based training as the feel the US business and legal approach is closer to the model they want to develop than much of what is available in Europe presently)

CURRENT SITUATION: The USG now has a USAID Representative in Budapest (USAIDRepB) in place. USAID has some programs in place intended to assist the privatization effort being undertaken by the GOH. Some of these programs stem from long standing requests for assistance from the GOH and are being continued and augmented in response to the significantly privatization focussed formal program request of February 1991 by the GOH to the USG. Other programs are new efforts based on that request. The professionals on the ground working on various parts of the privatization issue know each other and are working together to achieve the USG's common objective.

The contract vehicles in place are:

1. A LTA contract in place at the SPA with its related TA That contract is fully committed and expires on 26 Spt. 1991. It has not been renewed though it is under consideration. The contractor is Deloitte & Touche (D&T). The LTA is Charles Twyman. The LTA, D&T, USAIDRepB, the US Embassy in Budapest, USAID Washington, the ILI, and the Hungarian American Enterprise Fund (HAEF) and the SPA are known to each other and have worked together.
2. The Privatization and Restructuring Indefinite Quantity Contract (IQC). D&T is one of the designated contractors. D&T is well known to all the players in this scenario. USAID and the contractors in the IQC are trying to figure out how it works.
3. The HAEF Technical Assistance funding. The HAEF knows the SPA, the US Embassy Budapest, USAID Washington, the USAIDRepB, the LTA and D&T, and the ILI, well.

PROBLEM: The USAIDRepB was advised by USAID Washington on 28 August PM 1991, after an extended monolog, that there was no funding vehicle in place within USAID which could make training available of the type envisaged in the request in Hungary or in fact anywhere in Eastern Europe. The situation was summarized that the D&T contract was caught up in the contract review process (as it has been for several months), the IQC -in spite of its intended flexible design- has been judged not usable for such training purposes, and no other vehicle is on line.

THE FIRST TWO STUDENTS WERE SCHEDULED TO DEPART ON 1 SPT. THEIR WORK SCHEDULES AND PERSONAL AFFAIRS WERE ORGANIZED AROUND THE ANTICIPATED TRAINING.

SOLUTION:

1. 15:00 Budapest on 28 August the USAIDRepB confirmed to the HAEF that USAID could not directly fund the SPA's training request and endorsed the request.
2. The LTA prepared a formal training proposal for the HAEF.
3. The HAEF reviewed the proposal in Budapest and Washington and confirmed their willingness to fund by a call at 23:30 PM Budapest time 28 August to the LTA's residence. The HAEF's response both in their Budapest and Washington offices was rapid, understanding and thorough, they accepted the problem, understood it and helped solve it.
4. Based on the LTA's call following the HAEF commitment D&T Washington (benefitting from the time difference) laid the ground work with the ILI and organized the mechanics of assisting the students in Washington and effecting the required payments pending receipt of an acceptable funding commitment from the HAEF.
5. 29 August The US embassy's consular section assured the USAIDRepB office that they would facilitate the Visa issuance which they did without a problem. The USAIDRepB's office involved itself directly in the visa document completion and in clearing the way.
6. The HAEF prepared the appropriate documentation, D&T reviewed and approved it. Time 16:25 Budapest 29 August.
7. Upon completion of the documentation the LTA personally paid for the ticket for one of the students (the other being paid by WB) and personally made per diem advances to the two departing students.

CONCLUSION:

1. In Hungary there is a willingness to cooperate on the delivery of the USG's aid assistance. That cooperation will be continued.
2. It would appear a more systematic way to respond to appropriate US based training requests from the SPA or other organizations in Hungary or elsewhere in Central Europe is in order.
3. Pleased to have worked on this with you. However it is hard on the nerves of all the players to do it this way.

13 August, 1991

Mr. David Cowles  
A.I.D. Representative to Hungary  
United States Agency For International Development

Dear Mr. Cowles,

I was pleased to meet with you once again. Much has happened in Hungary's privatization program since our first meeting at the IDTI privatization course in 1989 and I enjoyed bringing you up to date and outlining areas where the US Government might continue to assist the State Property Agency (SPA).

In the February request for assistance from the Government of the Republic of Hungary addressed to the United States of America, we discussed several areas of interest, some are continuations of efforts that you have initiated and others are new projects. I would like to summarize them for you as an aide memoir so that we can begin to followup quickly. I will reference the February request item that relates as is appropriate.

CONTINUING EFFORTS: -The following are efforts that have been initiated and for which we request continuing assistance-

- a. The SPA wishes to reiterate its continuing interest in Having Mr. Twyman's services available. (Project 16)
- b. We are looking forward to having the assistance of a long term advisor in our spontaneous and investor initiated privatization operations. (Project 12)
- c. We wish to conclude our MIS project and move into the implementation and training phases. (Project 2)
- d. We very much need the support of a financial team to help us manage our contract work. (Project 7)
- e. We are still in need of the equipment that we had indicated a need for previously. Some of the new initiatives I mention below also require equipping as well. (Project 2)
- f. We continue to require advisory support to systematize our in-house training program. (Project 16)
- g. We require financial assistance to handle our US based training needs. (Project 5)
- h. Our coordination effort with the MIER and other key ministries we wish to continue. (Project 18)
- i. Our Public Relations effort needs considerable continuing assistance as we should now go into the action phase of the work previously initiated. This is most urgent. (Project 3)
- j. We need continuing support in producing materials to support privatization and promote investment. (Project 17)

NEW INITIATIVES: -The following are new privatization initiatives in Hungary for which we request support-

a. Under the new compensation law the SPA must organize and administer the Hungarian voucher system. The Hungarian voucher system initiative is tied to is new compensation law. The voucher system will have the effect of creating a very large pool of capital seeking good equity investments in privatizing government enterprises. This will be the largest single pool of investment capital created in Hungary to date with significant ramifications for the development of financial and capital markets.

The basis for the vouchers is that compensation for nationalization etc. is paid for with vouchers which represent a share in state enterprises (if held) or can be used in payment for the purchase of privatized operations within certain guidelines, or can be sold in a secondary market (which will be encouraged and supported).

There is an urgent need to design, equip, staff, train etc. the voucher organization with a particular skill need for the administering of the system and for the management and support of the secondary trading market in vouchers. (Project 1 and Project 7)

b. The SPA is attempting to speed up the privatization process by decentralizing and privatizing it. This program will start on September 1, 1991 and it is expected to impact around 1000 enterprises within a relatively short time frame. The new program is called the "self privatization program. The concept is that the SPA will designate a group of consulting firms in Hungary as qualified to advise the smaller enterprises on designing and executing a privatization strategy. If an approved consulting firm undertakes a privatization the SPA undertakes to approve it essentially without review except after the fact as a quality control on the consultants.

There is an urgent need to design, equip, staff, train etc. the self privatization organization. In addition a facility to fund some part of the consultants costs for this effort is very much needed. (Projects 22, 23 and 24 and Project 1 and Project 7)

c. In the course of the privatization program the SPA is left with considerable residual shareholdings that it would desire to sell. It would like to establish one or a series of unit trust type operations to privatize these shareholdings and pioneer the unit trust concept in Hungary. We would request assistance in undertaking this effort. (Project 30 and Project 1 and 7)

d. The Government of Hungary has significant warranty exposure in its various privatization undertaking concluded and proposed. The SPA is tasked with establishing a unit to track, adjudicate, and fund this exposure. This is a major continuing undertaking. We would request assistance in establishing such an operation. (Project 21)

f. The privatization effort in Hungary needs a dramatically expanded and sophisticated enterprise data base management system to enable it to serve the needs of government policy makers, various analytical needs, the needs of investors, and the post privatization analysis need. We have initiated such work in the equipping and MIS project at the SPA (Project 2) which we are linking into the investment promotion agency (Project 18) this data base effort requires expansion. (Project 28, 2, and 18)

g. The SPA needs access to funds to pay for brief enterprise and sector studies (pre-privatization reviews) to give a policy paper analysis as to what is "doable" before it commits itself to a sector or enterprise privatization strategy and the related costs. This must be on a rapid response basis and span the range of skills. (Project 4)

I believe this will give us enough to work on in coming weeks! I very much look forward to our continued cooperation. Please feel free to call on me at any time to follow up on these or other topics of mutual interest.

Sincerely,



TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-31 October, 1990

SUMMARY:

October, the initial month of the long term contract phase of the project, was principally a month of exit briefings of the United States Government (USG) at various levels and locations, entrance and long term contact briefings in Hungary, and donor agency follow-up. The critical State Property Agency (SPA) activity was the First Privatization Program (FPP) launch follow-up activity. As important was the SPA's effort to come to terms with its parliament approved revised and expanded responsibilities which include directing the privatization of approximately 16,000 small retail outlets and an expansion of its role as the named government shareholder in transformed government enterprises.

MAIN AREAS OF ACTIVITY:

- Exit briefed Ambassador Barry's office outlining the strategic objective of the project and discussed coordination.
- Exit briefed USAID desk and contract officers beginning to tie the detailed tactical and strategic objectives to budget line items and TA.
- Entrance briefed the US Embassy discussing future cooperation.
- Entrance briefed Hungary's small business office (SBA) and discussed continuing cooperation.
- Entrance briefed the Hungarian Banker's Association (HBA) and discussed areas of mutual interest.
- Entrance briefed the new Economic Community (EC) Poland Hungary Aid for the Recovery of the Economy (PHARE) mission in Budapest and continued the dialogue with PHARE Brussels to resolve funding problems.
- Tried to assist the SPA in growing organizationally to accommodate the processes they had committed themselves to in the FPP.

PROBLEMS IDENTIFIED:

- The HBA requires support if it is to help train Hungarian bankers in privatization related activities.
- The Hungarian SBA initiative is very understaffed and underfunded and its present mandate is unclear.
- The EC/PHARE is frustrated with the Government of Hungary's (GOH) slowness in responding to the PHARE program's bureaucratic requirements which must precede any disbursement.
- The USG is currently trying to formulate a pragmatic and action oriented aid policy response to the changes in Eastern Europe.
- The FPP's organization requirements are putting appropriate stress on the SPA's structure. The FPP is unfunded.
- The issue of how to deal with the 16,000 small enterprises and the shareholding issue is being postponed. No funds, no time.

RECOMMENDATIONS/SOLUTIONS:

- Continue to work with the HBA and the SBA to help them interact with the SPA and get donor support.
- Try to support the EC/PHARE's requirements from within and help the GOH structure itself to better deal with donor agencies in areas of absorbable assistance.
- Continue working with the USG to help define an appropriate program.
- Seek funding for the FPP and the retail privatizations.

## SPECIFIC TASKS

Progress during the period 1-31 October, 1990

1. Help Define the Operational Framework of the SPA:  
The needs of the FPP and the imminence of donor funding meant organizational changes must be initiated.
2. Help Prepare a Funding Strategy for the SPA's Activities:  
The interlocking needs of privatization in Hungary and the SPA was further defined with weaknesses identified.
3. Help Define the Organizational Needs of the Privatization Process:  
Internal SPA organizational weaknesses have emerged and are being dealt with. Hungary's structural and organizational needs were further explored.
4. Help Define the Initial and Longer Term Organizational Structure of the SPA:  
Accommodations to the needs of the FPP, the new mandates, and the needs of the donor agencies were begun.
5. Help Define the Office and Equipment Requirements of the SPA:  
Sheer lack of equipment continues to put a strain on the SPA as do temporary and scattered quarters.
6. Help Define the Personnel Requirements of the SPA:  
The SPA's personnel needs, particularly advisers, is still difficult to define given their difficulty in absorbing what they have. Local needs are more definable with training and experience being the roadblocks.
7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:  
Funding is the roadblock, the SPA's basic training needs are clear.
8. Help Define the Prioritization of Privatization Activities:  
The lack of funding and GOH mandated priorities are currently putting the SPA in a reactive mode however their basic priority "get on with it" is correct.
9. Help Define the Critical Privatization Program Linkages in the Economy:  
Work with the SBA, the NBH and various donors is clarifying the interdependencies in the Hungarian privatization process.
10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:  
This major project awaits the clearer definition of linkages and the right donor/Hungarian recognition of the problem.
11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:  
An initiative to formalize an investor driven "spontaneous privatization" route was begun.
12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:  
Identification of tools to support the program was continued: Management Information System (MIS) needs, public and investor communications strategy, strategic planning and team building, tight organizational control.

TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-30 November, 1990

SUMMARY;

November, the second month of the long term contract phase of the project, was principally a month of confirming the need for and then designing technical assistance support packages for the SPA. Following up on the equipment delivery support, and initiating the accounting, public information, and MIS activities. The SPA's final documentation for its EC PHARE funding was completed and discussions with the World Bank were initiated on funding FPP and some portion of future programs. The SPA commenced detailed negotiations with the advisers selected under the FPP.

MAIN AREAS OF ACTIVITY:

- The D&T project partner made key visits with the LTA to the Deputy Chairman of the SPA, the US Embassy, within the SPA, to the Hungarian Bankers Association, and to the DRT office in Budapest.
- The scopes of work for the initial TA support packages were agreed with the SPA for onward presentation to USAID.
- The initial TA was launched: Accounting, MIS, Public Relations line support.
- The equipment delivery and utilization support was continued.
- The EC/PHARE budgetary and documentary packages were delivered to accelerate the PHARE funds disbursement.
- UNIDO's activities with the SPA were advanced in SPA/GOH/UNIDO meetings
- The World Bank approved in principal the funding of the FPP (about \$4,000,000) and a portion of subsequent 1991 programs (\$25-35 mil.)
- Representational work continued: Sara Lee, Allied Signal, Tarmac, SGS, Dartmouth College exchange program, Hungarian American Enterprise Fund

PROBLEMS IDENTIFIED:

- The SPA's funding needs are critical and are continuing to dramatically hamper their development and functioning.
- The rudimentary level of technical knowledge of MIS and LAN systems at the SPA was identified.
- The public information problem continues with contradictory announcements on privatization issues from various Government agencies.
- The organizational weakness of the SPA (unclear communications channels, no set chain of command, untrained personnel) continue to create problems exacerbated by no permanent quarters, no equipment, no funds for training, changes in GOH mandates, and a heavy detail workload.

RECOMMENDATIONS/SOLUTIONS:

- Move funding into the absolute priority position
- Expand the teaching component of the MIS exercise and expand the follow-up both for the MIS and the equipment installation and utilization.
- Concentrate resources on the public information issue to seize the initiative.
- Try to establish organizational structure flowing from the needs of the funding side of the SPA's activities.

## SPECIFIC TASKS

Progress during the period 1-30 November, 1990

1. Help Define the Operational Framework of the SPA:

The MD approved a precise operating guideline for the PHARE funding control which will serve as the core for budgeting discipline and medium term planning.

2. Help Prepare a Funding Strategy for the SPA's Activities:

The MD approved a starting a systematic gathering of transaction costing data to tie into the budgeting procedure which is a prerequisite to obtaining funding.

3. Help Define the Organizational Needs of the Privatization Process:

The funding and budgeting control procedures will help resolve some of the SPA's structural organizational needs particularly transparency.

4. Help Define the Initial and Longer Term Organizational Structure of the SPA:

Until the SPA is fully operational at its current site with it's equipment in place fine tuning the organizational structure will be difficult though the basic needs have been identified.

5. Help Define the Office and Equipment Requirements of the SPA:

The initial needs have been defined, getting them in place is time consuming. Additional equipment requirements have been outlined to USAID and in the PHARE budget. The delivery of the equipment to be funded by both donors is required to complete the initial equipping. If the PHARE funding delivery delay continues other support will have to be sought.

6. Help Define the Personnel Requirements of the SPA:

Until the SPA is housed and equipped and resolves certain organizational problems its ability to digest additional skilled personnel is limited. Problem solving TA properly structured is absorbable and essential.

7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:

Needs defined, funding awaited.

8. Help Define the Prioritization of Privatization Activities:

The lack of funding and GOH mandated priorities are currently putting the SPA in a reactive mode however their basic priority "get on with it" is correct.

9. Help Define the Critical Privatization Program Linkages in the Economy:

A closer working relationship with the Ministry of International Economic Affairs was initiated to help better focus donor coordination. Several of these linkages are proving essential to be formalized if there is to be any significant national privatization program success apart from only transaction undertaken.

10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:

Progress is being made toward an appropriate donor/Hungarian recognition of the problem. Very shortly the problem will be support resources to deal with the problem.

11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:

The booklet "Information on the Privatization of State Owned Enterprises 1990" has now been completed as a first major step at making information formally available to those undertaking spontaneous privatizations. Technical inputs by the LTA provided some impetus to its tidy completion.

12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:

As the negotiations with the individual professional advisers for the FPP move forward, the advisers strategies -in several cases involving ESOPs, preference shares, golden share type solutions to problems- are serving as hands on training on the utilization of specialized tools.

TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-31 December, 1990

SUMMARY;

December, the third month of the long term contract phase of the project was principally a month of focussing on Hungary's privatization programs funding needs World Bank (WB), EC/PHARE, and USG. In addition the equipment installation and MIS programs were well advanced, the accounting package was essentially completed, the public affairs strategy work was launched. The SPA announced its Second Privatization Program (SPP) launch. The SPA moved (at last) into its permanent quarters. Almost all of the advisor's for the FPP will be designated by the end of December.

MAIN AREAS OF ACTIVITY:

- The SPA announced its pending launch of the SPP. The launch is not on track and will be effectively postponed until January.
- A needs summary for Hungary's privatization program from the SPA's viewpoint was prepared for the GOH for discussions with the USG.
- Hungary's EC/PHARE 1992 program budget efforts were participated in with the outcome that the SPA may have to assume a more active role to keep the discussions coordinated and on track. A desire of the EC/PHARE to coordinate their aid efforts with the US as the other big grant donor was established.
- The computer system technician from USAID PRE was coordinated with on the SPA's equipment needs and the problems of taking delivery. A second visit for early January was scheduled.
- The requirement and timing for the MIS was firmly established and work was begun in the US and in Budapest.
- The initial round of public affairs strategy interviews were conducted by Sawyer Miller.
- The computer driven accounting package to track donor funds was designed and completed. The training and follow-up phase start in January.
- Representational work continued: Rosten (Treasury), Barry (State), Lewis (USAID), French Hill (Treasury), IFC (new Budapest office director), US Embassy (various and often), Sundstrand, Hungarian American Enterprise Fund (HAEF), Harvard (USAID funded) pension fund study, White & Case.

PROBLEMS IDENTIFIED:

- The coordination needs for Hungary's national donor management strategy as involves its economic restructuring, particularly privatization, requires skill and resource commitment or it will bottleneck the process.
- Further PHARE program disbursement delays mean further privatization program endangering postponements of training, advisor engagement (legal and other), needed equipment etc.
- The first major personnel restructure at the SPA significantly refocused resources. The basic built in problems of lack of training and coherence continue but will require the commitment of presently unavailable resources to relieve.

RECOMMENDATIONS/SOLUTIONS:

- Help the SPA assume a proactive role in the donor agency management process.
- Attempt to focus rapid response donor facilities on the present national level problems. TA support teams. Funds pools for skills purchases.
- Continue to focus short term support facilities to meet the SPA's organizational needs. Team and Strategy building and definition!

## SPECIFIC TASKS

Progress during the period 1-31 December 1990

1. Help Define the Operational Framework of the SPA:

The accounting (near completion) and MIS (design phase underway) work is moving ahead well. This works eventual integration into the SPA will be the test.

2. Help Prepare a Funding Strategy for the SPA's Activities:

The need is now recognized at the national and SPA level and the strategic coordination can begin. Many of the project needs are readily identifiable but the coordination of the efforts and their absorption are at issue. The national effort is critical to the SPA's efforts.

3. Help Define the Organizational Needs of the Privatization Process:

The current internal restructure reorganized personnel resources based on their observed strengths over the past few months. Tying this group together now that they are properly housed and 1/2 equipped is the short term challenge. Longer term getting them to internalize the responsibility for the privatization process will be essential.

4. Help Define the Initial and Longer Term Organizational Structure of the SPA:

Until the SPA is fully operational at its current site with its equipment in place, fine tuning the organizational structure will be difficult though the basic needs have been identified.

5. Help Define the Office and Equipment Requirements of the SPA:

Early January work will take this a step further. It is anticipated that the expanded responsibilities of the SPA and the related manpower increase will require a significant equipment input.

6. Help Define the Personnel Requirements of the SPA:

A period of organizational stabilization is now required to allow the internal needs to become self-evident. Short term TA to support the learning process and to support particular tasks (the 16,000 small enterprise project) is the appropriate active step.

7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:

Needs defined, funding awaited.

8. Help Define the Prioritization of Privatization Activities:

The SPA continues in a largely reactive mode still constrained by a lack of funding to get its work done right and move into a guiding role.

9. Help Define the Critical Privatization Program Linkages in the Economy:

The major linkage at the level of donor financing has been established. It is projected the other major linkages, interministerial and others will follow.

10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:

The need for a plan has been recognized. This initiative appears to require a nationwide effort if the SPA is to succeed. It's beginning.

11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:

In the presence of a strong political will to move forward and a subsidy cutting economic environment, the SPA's relatively small size and specialized and compartmented structure is proving a most effective way to build a reliance on the Spontaneous (market) process in privatization in Hungary.

12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:

At the present the LTA is essentially off-line for this type activity on a transaction basis on other than an informal basis. However, he is deeply involved in helping the SPA and Hungary learn how to think through, fund, manage and derive benefit from technical assistance as a specialized tool to accelerate the process toward the national privatization objective.

TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-31 January, 1991

SUMMARY:

January, the fourth month of the long term contract phase of the project was principally a month of focussing on the donor and development agency support to Hungary's privatization and restructuring effort. The initial installation of the local area network (LAN), the first phase of the management information system (MIS) design, the final phase of the public relations (PR) strategy, and the completion of the donor bookkeeping system were accomplished. The First Privatization Program (FPP) advisors were announced.

MAIN AREAS OF ACTIVITY:

- The Second Privatization Program (SPP) is still on hold.
- Involvement in the preparation of the Government of Hungary's (GOH) request to the United States Government (USG) for technical assistance (TA) became a significant support effort. The necessity of much of the requested support for the success of the privatization program required getting it on track.
- Similar involvement for the same reason to try to get the GOH's efforts coordinated as regards the EC PHARE program both at the national level and internally within the SPA left me glad to be American but wishing I could speak Hungarian!
- The LAN installation went well with only the expected number of problems, each being unexpected. A clear need for continuing technical support and training was identified and additional equipment needs were analyzed.
- The MIS design was well received. The SPA's desire to accelerate implementation will put a great deal of pressure on what is achievable.
- The bookkeeping system went live with the initial ECU 2,742,000 deposit entered.
- The PR strategy work identified the expected lack of a clear image as to what the role of the SPA was and the direction of Hungary's privatization program. A simultaneous review by a Hungarian American Enterprise Fund (HAEF) consultant essentially identified the same basic problems.
- Representational work continued: Mansbach (OPIC), AMCHAM, Elicker (HAEF consultant), Rocas (UNIDO), EC PHARE (various), Bankers Trust, White & Case, Sundstrand.

PROBLEMS IDENTIFIED:

- The coordination needs for Hungary's national donor management strategy and this need and anticipated effect on Hungary's Privatization and economic restructuring effort is becoming critical.
- The operational aspects of the PHARE program must be addressed to get it started.
- The lead time in the delivery of donor funds is crippling the SPA given its need to react within a market environment and from a maturing and learning organizational base.

RECOMMENDATIONS/SOLUTIONS:

- Continue to focus support and try to guide the process until appropriate assistance is brought to bear.
- A creative solution to getting a fast disbursing funding line in place at the SPA has to be found.

## SPECIFIC TASKS

Progress during the period 1-31 January 1991

1. Help Define the Operational Framework of the SPA:

The donor accounting (completed), MIS (initial design phase complete) and the LAN installation (initial work done) are on schedule.

2. Help Prepare a Funding Strategy for the SPA's Activities:

A major effort was undertaken during the month to help design the national and SPA strategy for US funding, the national and SPA strategy for the EC PHARE funding and the SPA's World Bank funding strategy. Working these strategies through to the project stage will be the challenge.

3. Help Define the Organizational Needs of the Privatization Process:

The SPA is now in place in permanent quarters with the need becoming self-evident to organize around the systematic requirements of the funding sources. The MIS effort, the new office of the financial administrator, and the pressures to accelerate the privatization process are forcing the SPA to streamline its organization.

4. Help Define the Initial and Longer Term Organizational Structure of the SPA:

Fine tuning the organizational structure and beginning a systematic training program can begin as the initial EC money is in position.

5. Help Define the Office and Equipment Requirements of the SPA:

The SPA is now in permanent quarters, the MIS and LAN emplacement efforts are well underway and a professional needs assessment should be completed by mid-February. Significant additional equipment needs are emerging as is a requirement for on-the-ground equipment and systems support.

6. Help Define the Personnel Requirements of the SPA:

The SPA's internal needs are becoming more self-evident. Three long term advisor positions and two retainer positions have been identified. Training and new personnel needs are being defined.

7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:

The systematic design of a training program will take some time but it should be begun this month.

8. Help Define the Prioritization of Privatization Activities:

The SPA continues in a reactive mode. The new head of the Active Privatization unit is beginning a prioritization exercise with the help of the LTA which should start bearing fruit.

9. Help Define the Critical Privatization Program Linkages in the Economy:

The major linkage at the level of donor financing has been established. The interministerial linkages are forming.

10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:

A plan has been designed and projects identified. The project design phase should be launched soon. It's beginning. Good progress.

11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:

In the presence of a strong political will to move forward and a subsidy cutting economic environment, the SPA's relatively small size and specialized and compartmented structure is proving a most effective way to build a reliance on the Spontaneous (market) process in privatization in Hungary. More can be done and will in coming months particularly in the area of investment promotion.

12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:

The long term advisor is deeply involved in helping the SPA and Hungary learn how to think through, fund, manage and derive benefit from technical assistance as a specialized tool to accelerate the process toward the national privatization objective.



TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-28 February, 1991

SUMMARY:

During February, the fifth month of the long term contract phase of the LTA focussed on funding requests, briefings, and studies for various donor and development agencies. Ongoing support of specific tasks underway within the SPA continued. The second phase of the management information system (MIS) design was undertaken, the local area network (LAN) and the computer training and technical support persons were put in place. The public relations strategy piece was presented to the SPA's Board and Management. Assistance was provided in launching consultancy efforts in the Ministry of International Relations (MIER) in the areas of donor coordination and investment promotion were undertaken.

MAIN AREAS OF ACTIVITY:

- Donor coordination: a large World Bank mission, the follow on consultancy effort supporting the EC PHARE mission, and the USAID Private Sector Officer for the Office of European Affairs each spent several days in the SPA. With each the requested support of the SPA was discussed in project detail and with each their respective role in the overall financing of the SPA was made clear.
- The SPA has requested accelerations of the MIS and LAN programs. The next phases of the MIS and the training of the on-site personnel began. The delivery of subcontracted technical support has freed the SPA's computer staff of some of their duties allowing them to fully concentrate on the MIS and LAN activities.
- The PR Strategy was well and constructively received and an Action Plan was requested for the next phase. The interesting results of the In Depth Interview process both inside and outside the SPA clearly signposted the way to an appropriate strategy.
- The Investment Development advisor to help the MIER coordinate its investment promotion efforts with the privatization program began his work.
- The SPA Project Director visited the SPA. His visit was followed by proceeded the on-site work of the D&T project coordinator. The later visitor, besides undertaking several specific tasks, was able to think through several specific task and other problems with the LTA, USAID and the SPA.
- Representational work continued with calls from: US Embassy (several), Brownstein Zeidman Schomer, Sunstrand, Barrett Chasin, IFC, Standard Chartered, Tucker, Nomura, OPIC, Bankers Trust, Bear Stearns, EEC, World Bank, Canadian Embassy, Lockheed, USAID.

PROBLEMS IDENTIFIED:

- The need for a strategy definition for the SPA arose several times and is emerging as a significant issue.
- The need to get the donors together and to get the government's donor coordination efforts up to speed became more evident.
- The advanced stage of the needs of Hungary vs. the process requirements of the donors is all the more clearly requiring some bridging solutions.

RECOMMENDATION/SOLUTIONS:

- USAID and World Bank should initiate informal consultation at the working level in Washington DC. A visit to Brussels by USAID at the Project Officer level would be most useful.
- Work will continue to get fast response facilities in place for clearly defined needs.

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## SPECIFIC TASKS

Progress during the period 1-28 February 1991

1. Help Define the Operational Framework of the SPA:

MIS (second design phase begun), EC PHARE Financial Administrator in place.

2. Help Prepare a Funding Strategy for the SPA's Activities:

The SPA's funding strategy at the project design level was presented to the EC, World Bank, and USAID. In addition a UNIDO effort was taken a step further. A funding gap project piece was undertaken to identify the SPA's anticipated funding shortfalls under various scenarios.

3. Help Define the Organizational Needs of the Privatization Process:

The PR strategy piece, the HAEF/Elicker piece, each in their own way further underlined the need for strategy clarification. The donor's efforts to put together long term projections for the privatization effort add additional emphasis. The MIS effort continues. The pressures to accelerate the privatization process continue.

4. Help Define the Initial and Longer Term Organizational Structure of the SPA:

Some training has been contracted and begun.

5. Help Define the Office and Equipment Requirements of the SPA:

The additional equipment needs are being defined.

6. Help Define the Personnel Requirements of the SPA:

The long term advisory positions have been confirmed in donor requests.

7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:

The systematic design of a training program will take some time but it needs to be begun quickly.

8. Help Define the Prioritization of Privatization Activities:

The SPA continues in a reactive mode. The new head of the Active Privatization unit is beginning a prioritization exercise which in conjunction with the Ministry of Trade and Industry's segmentation exercise and other initiatives to specifically include strategic planning, this should fall into place.

9. Help Define the Critical Privatization Program Linkages in the Economy:

The major linkage at the level of donor financing has been established. The interministerial linkages are forming. The MIER/Investment Promotion/SPA work is underway. The temporary USAID contractor is in place in the MIER/Donor coordination office.

10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:

A plan has been designed and projects identified. The project design phase should be launched soon. It's beginning. Good progress.

11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:

In the presence of a strong political will to move forward and a subsidy cutting economic environment, the SPA's relatively small size and specialized and compartmented structure is proving a most effective way to build a reliance on the Spontaneous (market) process in privatization in Hungary. More can be done and will in coming months particularly in the area of investment promotion.

12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:

The long term advisor is deeply involved in helping the SPA and Hungary learn how to think through, fund, manage and derive benefit from technical assistance as a specialized tool to accelerate the process toward the national privatization objective.

TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-31 March, 1991

**SUMMARY:**

During March, the sixth month of the long term contract phase of the project, the LTA focussed on tying together various efforts underway into a reorganization and institutional development program recommendation to the Managing Director of the SPA. The basic LAN installation activities have been concluded and a systematic future equipment needs assessment was researched. The initial recommendations of the MIER investment promotion/SPA project were reviewed and implementation begun. The cash needs analysis done for the World Bank (WB) team resulted in a WB committment of the requested US\$10.5 mil.. The USAID's office setup team was welcomed.

**MAIN AREAS OF ACTIVITY:**

- Institutional Development: Starting with the WB's supportive analysis of the needs of the SPA, at the SPA MD's request, an outline program for insitutional restructuring and development was proposed as a starting point for formal strategic positioning of the SPA. This program would be designed to tie the SPA together and define it. The practical execution of this program should form the core the LTA's activity in coming months.
- LAN: The final stage of organizing the LAN installation was concluded and a refined additional equipment needs assessment was prepared.
- MIS: Design work on the next phase proceeded with actual programming set to begin.
- Investment Promotion/SPA coordination: The initial summary recommendations were reviewed and accepted within the MIER. SPA/MIER senior management liaison commenced and operating level discussion were initiated.
- SPA Public Relations: The software and hardware purchased for their use was made operational and produced its first work. Coordination efforts continued. Significant additional support is merited.
- Donor coordination: Reviews of the draft WB and EC proposals for SPA support were prepared and discussed. The European Bank for Recovery and Development's proposed country strategy and its privatization support components were also reviewed. Assistance as required was made available to the USAID office. The Citizens Democracy Corp proposal was refined and the MBA corp proposal circulated at the SPA.
- Representational work continued with calls from: U.S. Embassy, Citizens Democracy Corp, MBA Corp., Coca Cola, the Urban Institute, the Ministry of International Economic Relations, the First National Bank of Chicago, the World Bank, Price Waterhouse, AMEG, SGS, Bear Stearns, and USAID

**PROBLEM IDENTIFIED:**

- The strategy issue is now properly subsumed in the institutional development issue which will become a donor agency theme in coming months. This is a supportive development that should encourage appropriate followup within the SPA.

**RECOMMENDATION/SOLUTION:**

- The D&T/USAID SPA effort should continue to focus on the institutional development issue as the theme of their support.

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SPECIFIC TASKS  
Progress during the period 1-31 March 1991

1. Help Define the Operational Framework of the SPA:

An institutional development program detailing the necessary core initiatives was circulated and discussed.

2. Help Prepare a Funding Strategy for the SPA's Activities:

The SPA has accepted the need to appoint an appropriately qualified Hungarian Chief Financial Officer whose principle activity would be coordinating donor funding, planning, budgeting and control.

3. Help Define the Organizational Needs of the Privatization Process:

The ever broader recognition of the need to systematize the SPA's activities and organization is resulting in a useful focussing on long recommended steps to make organization a part of the SPA.

4. Help Define the Initial and Longer Term Organizational Structure of the SPA:

Specific areas requiring development have been outlined.

5. Help Define the Office and Equipment Requirements of the SPA:

The additional equipment needs definitions, US and EC sourced, have been completed.

6. Help Define the Personnel Requirements of the SPA:

The long term advisory positions have been confirmed in donor requests. New positions and an organizational restructuring has been recommended.

7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:

The training program design phase awaits funding confirmation.

8. Help Define the Prioritization of Privatization Activities:

The new head of the Active Privatization units sector focused strategy for the next several launches is going forward for board review. The practical market realities of such an approach have not been fully thought through. The national prioritization exercise continues.

9. Help Define the Critical Privatization Program Linkages in the Economy:

The major linkages at the level of donor financing has been established. The WB, EC, and EBRD are working closely together, the US Government needs to be brought into the program particularly at the informal working level. The interministerial linkages are forming. The MIER/Investment Promotion/SPA linkage is being formalized

10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:

The EC's project design phase is underway, the WB's design has been submitted, USAID is considering entering the project design phase. The SPA has accepted the need to formalize the function of coordinating these efforts. The Ministry of International Economic Relations donor coordination office is now staffed and beginning to function. Good progress.

11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:

The systematic focus on investment promotion and the reliance on the privatization process in Hungary on the market driven rather the government initiated transactions continues to be the proper track and broadening common need recognition.

12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:

The long term advisor continued his support in this area focussing some effort during the period on the area of residual SPA asset sales, the development of unit trusts and investment companies, and related issues.

TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-30 April, 1991

**SUMMARY:**

During April, the seventh month of the long term contract phase of the project, the LTA worked through the details of reorganization needs with the SPA with particular attention on the practical constraints. The training program design moved forward as the internal board called for its conclusions. MIS programming is now well underway. The PR and publications efforts are gradually having an effect. A heavy representational load was assumed as the line directors became more deeply involved in transaction detail. Work with the new USAID Hungary office head designee began. The Prague visit was arranged.

**MAIN AREAS OF ACTIVITY:**

- Institutional Development: The inability of the SPA to significantly increase staff or offer free market competitive salaries is blocking their efforts to build the required skill pool to manage their financial responsibilities under EC and WB. Contracting this and other services under senior SPA direction is the answer at this point.
- LAN: The new LAN manager is integrating well. Getting all the equipment on line and people trained is the next step. The next step is completing the equipping of the SPA in line with their needs.
- MIS: Programming was begun and initial work demonstrated, design work and further programming module design continues.
- Investment Promotion/SPA coordination: Document exchanges have commenced. The MIS work is awaited.
- SPA Public Relations: The basic PR strategy has been accepted. Execution is awaited. Coordination efforts continue as the problem of decentralized press contact becomes more of a problem.
- Prague/Warsaw trips: Prague is arranged, Warsaw underway
- Donor coordination: Assistance was made available to the USAID office particularly to give David Cowles (in many ways the initiator of the SPA support activities) an update. The Citizens Democracy Corp proposal was accepted. The MBA corp proposal was stopped by the SPA's unwillingness to pay a competitive local salary.
- Representational work continued with calls from: U.S. Embassy, Citizens Democracy Corp, MBA Corp., Pepsi Cola, the Commerce Department, the Ministry of International Economic Relations, Sawyer Miller, The IFC, Gates Rubber, OPIC, Reuters, El Pais, A Polish Government Delegation, USAID and others.

**PROBLEM IDENTIFIED:**

- How to implement the required institutional development.

**RECOMMENDATION/SOLUTION:**

- The D&T/USAID SPA effort should continue to focus on the institutional development issue as the theme of their support.

**WORK PLAN:**

- 1. Support D&T/USAID efforts to deliver appropriate support to the SPA, commence implementation as required.
- 2. Complete the Prague exchange visit
- 3. Finish the training program design
- 4. Organize the IDTI class attendees
- 5. Initiate MIS work at the MIER
- 6. Support bank analysis activities of the SPA

SPECIFIC TASKS  
Progress during the period 1-31 April, 1991

1. Help Define the Operational Framework of the SPA:  
The practical implementation problems of the institutional development program were discussed and the contracting solution accepted.
2. Help Prepare a Funding Strategy for the SPA's Activities:  
The problem of how to get an appropriately staffed unit in place to support a SPA Chief Financial Officer was addressed.
3. Help Define the Organizational Needs of the Privatization Process:  
After recognition of the need comes resolution, that will take a while but it is underway.
4. Help Define the Initial and Longer Term Organizational Structure of the SPA:  
An outline has been accepted.
5. Help Define the Office and Equipment Requirements of the SPA:  
The additional equipment needs definitions, US and EC sourced, have been completed, the first EC equipment was delivered.
6. Help Define the Personnel Requirements of the SPA:  
With the needs defined getting the personnel funded, identified and in place is now slowly underway.
7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:  
The training program design is underway.
8. Help Define the Prioritization of Privatization Activities:  
The national prioritization exercise continues.
9. Help Define the Critical Privatization Program Linkages in the Economy:  
The major linkages at the level of donor financing has been established. The WB, EC, and EBRD are working closely together, the US Government needs to be brought into the program particularly at the informal working level. The interministerial linkages are forming. The MIER/Investment Promotion/SPA linkage is formalized
10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:  
The challenge is now to get the coordination apparatus working so that it adds value to the process. The donors' tendency to call for coordination and then not do it is matched by the recipient's various operating entities desire to deal directly.
11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:  
The systematic focus on investment promotion and the reliance on the privatization process in Hungary on the market driven rather the government initiated transactions continues to be the proper track and broadening common need recognition.
12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:  
Some assistance in the area of dealing with Bank privatization issues was initiated.

TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-31 May, 1991

**SUMMARY:**

During May, the eighth month of the long term contract phase of the project, the LTA completed the Czech Privatization Agency visit, concluded the Polish Privatization Agency visit arrangements, supervised the completion and presentation in draft form of the training program, completed the details of sending an SPA officer to a training program at First Chicago, got the IDTI course visa and other details started, laid more groundwork for MIS coordination with the MIER, and continued a full representational schedule. In addition the project manager visited from Washington helping properly shape the LTA's efforts for the coming months with efforts focussed on definining with the SPA the areas of required assistance.

**MAIN AREAS OF ACTIVITY:**

- The visit with the Czech Ministry of Privatization went well with particularly useful lessons learned from the Czech small unit privatization process. The imminent Czech elections and the linking of the restitution and the privatization efforts with the added feature of a voucher system made it an interesting equation to study with the technicians. It is hoped that reciprocal visits can be initiated.
- The Polish visit got well on track with the critical meetings arranged and dates set working closely with DRT Poland.
- The training program was crafted into an immediatly useful form and became, while still in draft, the basic training policy and practice document for the SPA. Key training components and their likely sources and funding requirements were identified and efforts were initiated to get them in place. The US sourced IDTI training, legal training, and other items particularly OJT opportunities through the CDC and others were integrated with EC funded and sourced efforts. Full training organizaion implementation is the next required phase.
- The initial programming of the MIS is in the debugging phase. The follow-on work is awaited.
- The public relations program launch is still awaiting funding but interim support in preparation of the annual parliamentary report and various press announcements and conferences was continued.
- A financial management strategy for the SPA was refined and accepted.
- Representational activity: Ministry of International Economic Relations, Citizens Democracy Corp, Hungarian American Enterprise Fund, USAID, GAO, International Executive Service Corp, Pioneer Seed, English Speaking Valuation Assn. (speech), Chemonics, World Bank, British Know How Fund, Financial Services Volunteer Corp., Washington Post, and others

**PROBLEM IDENTIFIED:**

- The institutional development required to manage a most active and successful privatization program is the most urgent requirement.

**RECOMMENDATION/SOLUTION:**

- Continued D&T/USAID support of the institutional development issue.

**WORK PLAN:**

- 1. Complete Polish exchange visit.
- 2. Complete training program design phase.
- 3. Complete IDTI course team preparation.
- 4. Initiate "100 Questions" brochure preparation activities.
- 5. Support Parliamentary report activities.
- 6. Continue financial management backstopping.

## SPECIFIC TASKS

Progress during the period 1-31 May, 1991

1. Help Define the Operational Framework of the SPA:

The progress on the MIS, Training Program, and Financial Management Plan contributed to the operational framework's evolution

2. Help Prepare a Funding Strategy for the SPA's Activities:

The problem of how to get an appropriately staffed unit in place to support a SPA Chief Financial Officer was addressed through a formalized proposal which has been approved.

3. Help Define the Organizational Needs of the Privatization Process:

The public relations program, the Czech trip, the 1st. Chicago training program, the training plan each contributed to defining and resolving the organizational needs of the SPA.

4. Help Define the Initial and Longer Term Organizational Structure of the SPA:

The role of financial management was defined this month as were the training needs.

5. Help Define the Office and Equipment Requirements of the SPA:

The additional equipment needs definitions, US and EC sourced, have been completed. The final USAID component is awaited.

6. Help Define the Personnel Requirements of the SPA:

Needs were further defined in the financial management and training programs.

7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:

The training program was drafted and reviewed and accepted to go to final form.

8. Help Define the Prioritization of Privatization Activities:

The national prioritization exercise continues. The program outline for the next twelve months as part of the annual Parliamentary report will be completed in June and will clarify many of the specific objectives.

9. Help Define the Critical Privatization Program Linkages in the Economy:

The MIER/Investment Promotion/SPA linkage was furthered by additional efforts on the MIS linkage and the joint publications program.

10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:

The financial management and the related budgetting and planning process is a systematic step in the right direction.

11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:

The systematic focus on investment promotion and the reliance of the privatization process in Hungary on the market driven rather the government initiated transactions continues to be the proper track and broadening common need recognition.

12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:

The Czech and proposed Polish trips will help understand privatization program variants particularly the voucher issue and linkages to the compensation issue.



TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-30 June, 1991

SUMMARY:

During June, the ninth month of the long term contract phase of the project, the LTA completed the Polish Privatization Agency visit, reviewed the final training program presentation and began the detailed financing planning of the program, sent the IDTI team on its way with appropriate preparatory work in hand, provided guidance and coordination on the structuring of the "100 questions" brochure, prepared a parliamentary report summary for the donor agencies, and continued financial stop-gapping. Involvement in a key privatization effort was begun.

MAIN AREAS OF ACTIVITY:

- The visit with the Polish Ministry of State for Ownership Change (MOC) was excellent particularly as the Hungarian team headed by Lajos Bokros (one of the principal architects of the Hungarian program) spent an evening with Kryzysztof Lis, a principal architect of the Polish program. The voucher system briefing by the Touche Ross design team and discussions the role the upcoming elections have had on the direction, pace, and limitations of the program were most valuable.
- The final report for the training program design project was reviewed, and submitted for formal SPA acceptance.
- The IDTI team was briefed, and helped in designing an agenda for how they could best utilize the IDTI program with related team building sessions. Preparatory materials were gathered, written and reviewed. The team left.
- The MIS initial programming phase is about ready for SPA data entry.
- The initial visit by the "100 questions" brochure team was managed and the initial phases planned. Coordination with the MIER and others was taken further.
- Work with the annual Parliamentary report was continued. The internal summary the LTA prepared was passed to the USAID office.
- As financial management isn't happening, further efforts to get things rolling were initiated.
- The LTA's experience with airline and aircraft financing has made him a useful part of the just formed SPA team for the MALEV (the national air carrier) privatization national steering committee.
- Representational activity: USAID Warsaw, GAO (joint with USAID Budapest), Department of State senior economic policy advisor for Hungary, Coopers & Lybrand briefing on Hungary's privatization program in support of USAID program in Yugoslavia, First Chicago country risk analysis team, Interkiln, AIG, William & Mary researcher (US Embassy introduction), Harvard Business School researcher (WB introduction), Price Waterhouse privatization case study shortlist team (USAID introduction), World Bank

PROBLEMS IDENTIFIED:

- Institutional development is still the key issue. Financial management problems are becoming critical.

RECOMMENDATION/SOLUTION

- Continue D&T/USAID support of the institutional development issue. Try to initiate rapid response assistance in the financial management area.

WORK PLAN:

- 1. Complete Czech and Polish trip and FNBC training reports.
- 2. Debrief IDTI team and get their product. Obtain valuation.
- 3. Take "100 question" brochure further.
- 4. Coordinate stop-gap financial management assistance.
- 5. Coordinate MIS team work.
- 6. Plan next step needs in training program.
- 7. Integrate activities into arrival of USAID Budapest Representative.

## SPECIFIC TASKS

Progress during the period 1-30 June, 1991

1. Help Define the Operational Framework of the SPA:  
The Czech and Polish visits led to modifications in the SPA's Operation Framework, training delivery is having the same effect.
2. Help Prepare a Funding Strategy for the SPA's Activities:  
The problem of how to get an appropriately staffed unit in place to support a to be named SPA Chief Financial Officer was addressed through a short term effort being initiated.
3. Help Define the Organizational Needs of the Privatization Process:  
The public relations program, the Polish trip, and the "100 Questions" brochure initiative, each contributed to defining and resolving organizational needs of the SPA.
4. Help Define the Initial and Longer Term Organizational Structure of the SPA:  
The training program and MIS's progress both impact this area.
5. Help Define the Office and Equipment Requirements of the SPA:  
The additional equipment needs definitions, US and EC sourced, have been completed. The final USAID component is awaited.
6. Help Define the Personnel Requirements of the SPA:  
Needs have been defined in the financial management, MIS, and training programs.
7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:  
The training program was submitted. Further training (IDTI) in accord with the plan was initiated and the First Chicago trained officer returned.
8. Help Define the Prioritization of Privatization Activities:  
The national prioritization exercise continues. The program outline for the next twelve months as part of the annual Parliamentary report was completed. The Government's endorsement or modifications are awaited. Specific support on the MALEV transaction will have its effect on the national prioritization.
9. Help Define the Critical Privatization Program Linkages in the Economy:  
The MIER/Investment Promotion/SPA linkage was furthered by additional efforts on the MIS linkage and the joint "100 Questions" publications program. The First Chicago training course which included two Hungarian bankers created a practical and mutual interest linkage between these banks and a senior line SPA officer. A followon joint financial analysis training undertaking is being discussed.
10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:  
The financial management and the related budgetting and planning process was a systematic step in the right direction. No significant progress during this period.
11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:  
The focus on investment promotion and the privatization process being market driven rather than principally government initiated continues to be the proper track and broadening common need recognition. The "100 Questions" project and data base integration directly supports this.
12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:  
The Czech and Polish trips helped the SPA's understanding of privatization program variants particularly the voucher issue and linkages to the compensation issue and the role of various political agendas. ESOP's and management incentive program's will be likely features of the MALEV transaction. Similarly some complex financing will come into play.

TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-31 July, 1991

SUMMARY:

During July the tenth month of the long term contract phase of the project, the LTA completed the Polish and Czech trip reports, received and reviewed the First Chicago and IDTI reports and debriefed the participants, helped take the "100 Questions" brochure further, initiated the stop-gap financial assistance, coordinated the completion of the training brochure and the definition of the next phase of the training program, and worked with the MIS team. The LTA worked with the new USAID representative to begin to coordinate efforts under the Restructuring and Privatization IQC to avoid overlap with the efforts of other donors and programs involved in the SPA. The LTA helped the SPA begin to organize its "self-privatization" program, and prepare for its voucher system role under the Compensation Act.

MAIN AREAS OF ACTIVITY:

- The Polish and Czech trip reports were circulated within the SPA for comment, revised and then finalized. They form an interesting if brief snapshot summary of each country's privatization program.
- The First Chicago training report and debrief found the course had some excellent skills to teach particularly in the financial analysis part of the course, some of the more sophisticated lessons were inappropriate.
- The IDTI course while well organized with excellent materials and presentors is organized around nations in the policy-forming phase of the privatization process. As Hungary, and most nations, are past that the course no longer has great immediate relevance.
- The "100 questions" investment brochure was taken into the mock up stage and is scheduled to be used in the upcoming Prime Minister visit to Canada and the United States. The Investment promotion office has asked for help beyond the brochure as this will be their initial official involvement in a major promotional activity.
- The MIS is about ready to be installed. The hope is to have it in place in September depending on funding. The MIS team coordinated with the MIER's investment office.
- The training manual was completed and the next phase has been outlined. Legal training in line with the training manual's plan was requested from USAID while some of the initial PHARE funded training was committed to.
- The new USAID representative has been formally introduced to the SPA and several areas of support discussed. The USAID offices plan is to coordinate the deliveries of aid to the SPA so that the various efforts don't needlessly overlap.
- The SPA's new areas of activity in their new self-privatization program and Hungary's compensation voucher system will require substantial organizational spinoffs. These two activities represent two major new Hungarian privatization and financial market initiatives.
- Representational activity: USAID Hungary, USAID Washington, WB Operations Evaluation Department, Morgan Stanley, Western Petroleum, American Society of Appraisers, PW International, Guardian Europe, US Treasury, HAEF, MIER, Ministry of Trade and Industry, US Embassy, Hungarian Foundation for Enterprise Promotion, Nomura, US Trade Representative, etc.

PROBLEMS IDENTIFIED:

-Institutional development is still a key issue. Financial management problems are critical. New initiatives need rapid response support.

RECOMMENDATION/SOLUTION

-Continue D&T/USAID support of the institutional development issue. Try to initiate rapid response assistance in the financial management area and the self privatization and voucher system programs.

WORK PLAN:

- 1. Work with USAID to initiate support activities from the local office.
- 2. Support Canadian/US investment promotion trip, do TDW.
- 3. Take "100 question" brochure further.
- 4. Coordinate stop-gap financial management assistance complete TDW.
- 5. Coordinate MIS team work.
- 6. Prepare TDW for next step needs in training program.
- 7. Work on SPA budget, help new financial director get established.

## SPECIFIC TASKS

Progress during the period 1-31 July, 1991

1. Help Define the Operational Framework of the SPA:

The new self-privatization initiative and the new Financial Director will change the operational setup of the SPA as will the financial management assistance.

2. Help Prepare a Funding Strategy for the SPA's Activities:

The financial management assistance is beginning and the Financial Director will be at work on 15 August. The annual donor budget cycle has begun with its initial submission by 1 September. The strategy for the 1992 must be derived.

3. Help Define the Organizational Needs of the Privatization Process:

The public relations program, the new self-privatization program, the needs of the voucher system, the warranty servicing needs, and the unit trust type activities are all new areas of organizational support need identified and being defined by the SPA and the LTA.

4. Help Define the Initial and Longer Term Organizational Structure of the SPA:

The training program and MIS's progress both impact this area as have the investment coordination activity and the design of the new self-privatization and other initiatives.

5. Help Define the Office and Equipment Requirements of the SPA:

The additional equipment needs definitions, US and EC sourced, have been completed. The final USAID component is awaited. However the new initiatives will require their own equipping and systems support.

6. Help Define the Personnel Requirements of the SPA:

Needs have been defined in the financial management, MIS, and training programs as well as initial definitions in the new initiative areas.

7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:

The training program was submitted. Further training (IDTI) in accord with the training plan was completed and legal training requested.

8. Help Define the Prioritization of Privatization Activities:

The national prioritization exercise continues. The self-privatization program to accelerate the program has been announced and the compensation voucher system must be implemented such that it complements the privatization process.

9. Help Define the Critical Privatization Program Linkages in the Economy:

The MIER/Investment Promotion/SPA linkage was furthered by additional efforts on the MIS linkage and the joint "100 Questions" publications program.

10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:

The financial management and the related budgetting and planning process was a systematic step in the right direction. With new USAID funds coming to the table meaningful coordination in several areas can be initiated.

11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:

The focus on investment promotion and the privatization process being market driven rather than principally government initiated continues to be the proper track and broadening common need recognition. The "100 Questions" project and data base integration directly supports this. The new self-privatization initiative is an imaginative and systematic response to this task requirement and the voucher system should provide significant capital investor support to the privatization process.

12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:

The Czech trip led almost directly to the design of the new self-privatization program. The Polish and Czech voucher systems have lessons good and bad for Hungary. ESOP's and management incentive program's are now well regulated features of Many transactions.

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MEMORANDUM

TO :Robin Mcphail  
FROM :Chick Twyman  
DATE :7 August, 1991

REF :Visitors, July 1991

Barson Marsteller, Mary Foerster, GM Central Europe

Ministry of Trade and Industry, Merenth, Andras, Directorate General of Energy Policy, Head of Department

Schroders, Claudia Pendred

Ministry of Transport & Communications, Gyula Partos, Director Genl. Sect. of Telecommunications

Guardian Europe, Jean Ries GM, Guardian Glass Hungary

The Center for Private Enterprise Development, William Holstein

US Treasury Dept., David JOy, Kateringa Sloniewsky

Know How Management Consulting Co (Managers in Hungary of the IESC), Paul Vida, Pres. and CEO

MBA Enterprise Corp., Jack Belamin, Director

Hungarian American Enterprise Fund, Alec Tomlinson, Charles Huebner, Paul Marer

USAID Hungary, David Cowles, Liz Chaney, Carol Morrison, etc.

US Embassy, Jeff Feltman, Don Grabenstetter, Richard Baltimore, Edward Gotchef, Howard Clark

PW Intl, David s. Coco, Intl. Privatization Group

American Society of Appraiser, John Clark

Western Petroleum Services Intl., Davar Katic

O.R. Bengur, Bengur & Co.

Morgan Stanley & Co., William Birch Jr., MD

World Bank, Farroka Najmabadi, Wafa Faiimi Abdelati, Robert S. Myer, Shymudus Banerji, Sanjuya Callas

Purina Hagen, Harrison Givens, Director Hungary

USAID, Robert F. Ichord Jr.

US Dept of Energy, Denis Dwyer, Leonard Rogers

Frankfurter Allgemeine, Jacqueline Hemard

Intl. Bus. & Tech Cons. Inc., Jayant Kalotra

Booz Allen & Hamilton Inc., Heather Burns V.P.

Hungarian Foundation for Enterprise Promotion, Richard Guilford

Nomura, Helen Norwood

Zoltan Pozmany

MNS, Paul Sachs, Mart Bakal

DRT Romania - M. Hicks

Citibank Hungary, MD Winchester, Igas Katalin, Treasury

Office of the US Trade Representative, Carla Hill

TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-31 August, 1991

SUMMARY:

During August the eleventh month of the long term contract phase of the project, the LTA dealt in detail with the possible next phase of the project, sent two SPA lawyers to the US for training with Hungarian American Enterprise (HAEF) funding. The LTA assisted in the continuation of the training department support, assisted in the stop-gap financial support, and tried to avoid project damage caused by lack of funding to support various ongoing efforts (MIS, PR, Financial Support, Training). The LTA spent considerable time helping the SPA define their warrant and self-privatization program needs.

MAIN AREAS OF ACTIVITY:

- The LTA assisted by the project administrator prepared the Task Definition Worksheets (TDW) for the small balance of the funding in the current contract and worked with the USAID Representative in Budapest to define the prioritization of work in the next phase of the Project. The way the SPA project, the Privatization IQC, and HAEF funding would be orchestrated to derive the most effective utilization of each was explored.
- The investment brochure completion was effected by the editor's vacation and the papal visit PR activities preempting the local agency's time. The MIER apparently in not to be directly involved in the PM visit so the absolute urgency of the brochure is now reduced.
- The MIS is about ready to be installed. The final work awaits funding. The SPA is upset about the delay.
- The Training Department support was initiated.
- The HAEF and all the field participants responded well to the last minute discovery that USAID Washington could not fund US based training and we had to scramble to find funding for Legal training in DC for two SPA legal staff in Negotiating Foreign Investment.
- The new USAID Representative in Budapest worked closely with the LTA and the D&T team to work out the details of the next phase work with the SPA as outlined in the SPA's 13 August, 1991 letter.
- The SPA's new self-privatization program and Hungary's compensation warrant system needs were further defined.
- Some considerable time was spent on establishing the status of the present contract in support of the SPA
- Representational activity: USAID Hungary, USAID Washington, US Embassy Budapest, Ministry of International Economic Relations: Donor Coordination Unit and Investment Unit, UNDP, Chicago Tribune

PROBLEMS IDENTIFIED:

- USAID must decide on whether it will continue the SPA support program.

RECOMMENDATION/SOLUTION

- Either a policy decision coupled with contracting followup or an effort to make a gracious withdrawal of support is in order.

WORK PLAN:

- 1. Complete basic work for 1 year report.
- 2. Conclude current efforts.
- 3. Support next phase activities as appropriate.



## SPECIFIC TASKS

Progress during the period 1-31 August, 1991

1. Help Define the Operational Framework of the SPA:  
The new Financial Director is in place and was briefed.
2. Help Prepare a Funding Strategy for the SPA's Activities:  
The annual donor budget cycle has begun but the priority is now being given to the Hungarian budget negotiations as that is proving problematic. The donor funding issues unpredictability is a continuing problem.
3. Help Define the Organizational Needs of the Privatization Process:  
The new self-privatization program, the needs of the warrant system, and areas of organizational support needs were clarified in TDWs.
4. Help Define the Initial and Longer Term Organizational Structure of the SPA:  
The training program and MIS's stalled progress both impact this area as do the design of the new self-privatization and warrant initiatives.
5. Help Define the Office and Equipment Requirements of the SPA:  
The final USAID equipment component is awaited. The new initiatives will require their own equipping and systems support.
6. Help Define the Personnel Requirements of the SPA:  
Needs have been defined in the financial management, MIS, and training programs as well as initial definitions in the new initiative areas.
7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:  
The training department support was initiated, two lawyers were sent for training in the USA with HAEF support.
8. Help Define the Prioritization of Privatization Activities:  
The national prioritization exercise continues. The self-privatization program to accelerate the program has been announced and the compensation warrant system must be implemented such that it complements the privatization process.
9. Help Define the Critical Privatization Program Linkages in the Economy:  
The MIER donor coordination unit was met with to discuss Hungary's donor strategy in the privatization area.
10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:  
Further support was planned for. Funding is awaited.
11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:  
The focus on investment promotion and the privatization process being market driven rather than principally government initiated continues to be the proper track and broadening common need recognition. The "100 Questions" project and data base integration directly supports this. The new self-privatization initiative is an imaginative and systematic response to this task requirement and the warrant system should provide significant capital investor support to the privatization process.
12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:  
The Warrant system's definition and how to contract out the core of the Self-Privatization programs start-up were creative initiatives in this area.

TECHNICAL ASSISTANCE TO THE  
STATE PROPERTY AGENCY OF HUNGARY  
USAID CONTRACT NO. ANE-0002-C-00-0047-00  
USAID PROJECT NO. 180-0002-3-0183107

Long Term Advisor's Progress Report

PERIOD: 1-30 September, 1991

SUMMARY:

During September the twelfth month of the long term contract phase of the project, the LTA dealt simultaneously with the possible next phase and closing the project down should the project not be extended. One more SPA lawyer (making a total of 3) was sent to the US for training with Hungarian American Enterprise (HAEF) funding. The LTA assisted in the continuation of the training department support, assisted in the stop-gap financial support, and continued trying to avoid project damage caused by lack of funding to support various ongoing efforts (MIS, PR, Financial Support, Training).

MAIN AREAS OF ACTIVITY:

-The LTA helped the Project Administrator draw together the deliverables for the first twelve months of the project. The LTA completed the core of the report for the first twelve months' activities. The LTA began drawing together the materials for the October briefing trip to Washington DC (USAID and the State Department) and London (EBRD).

-The investment brochure final draft was reviewed.

-The Training Department part time support was continued.

-The third and last HAEF funded SPA lawyer was sent for Legal training in negotiation with foreign investors in DC.

-Close coordination with the USAID Representative in Budapest continued to work out the details of the next phase work with the SPA and the October DC visit.

-The SPA's new self-privatization program and Hungary's compensation warrant system needs were further defined and teaming possibilities reviewed.

-Some considerable time was spent on establishing the status of the present contract in support of the SPA

-The Senior Partner from DRT International (Ian Appleby) overseeing the activities of DRT's worldwide operations was briefed.

--Representational activity: USAID Hungary, USAID Washington, US Embassy Budapest, Ministry of International Economic Relations: Donor Coordination Unit and Investment Unit, World Bank

PROBLEMS IDENTIFIED:

-USAID must decide on whether it will continue the SPA support program.

RECOMMENDATION/SOLUTION

-Either a policy decision coupled with contracting followup or an effort to make a gracious withdrawal of support is in order.

WORK PLAN:

- 1. Complete basic work for 1 year windup.
- 2. Continue laying groundwork for 2nd. year effort.
- 3. Support next phase activities as appropriate.

## SPECIFIC TASKS

Progress during the period 1-30 September, 1991

1. Help Define the Operational Framework of the SPA:  
The new Financial Director was introduced to the accounting systems support team.
2. Help Prepare a Funding Strategy for the SPA's Activities:  
The annual donor budget cycle continues. The EC PHARE management reorganization within its SPA project continued. Work continued advising the SPA on the USAID and World Bank components of their funding with some mechanical support of the EC effort.
3. Help Define the Organizational Needs of the Privatization Process:  
The new self-privatization program, the needs of the warrant system, and areas of organizational support were tentatively teamed pending funding support.
4. Help Define the Initial and Longer Term Organizational Structure of the SPA:  
The training program, financial management, and MIS's stalled progress impact this area as do the design of the new self-privatization and warrant initiatives.
5. Help Define the Office and Equipment Requirements of the SPA:  
The final USAID equipment component is awaited. The new initiatives will require their own equipping and systems support.
6. Help Define the Personnel Requirements of the SPA:  
Needs have been defined in the financial management, MIS, and training programs as well as initial definitions in the new initiative areas.
7. Help Define the Training Needs of the SPA and Help Initiate an Appropriate Training Program:  
The training department support was continued, one more lawyer was sent for training in the USA with HAEF support.
8. Help Define the Prioritization of Privatization Activities:  
The national prioritization exercise continues. The self-privatization program to accelerate the program has been announced and the compensation warrant system must be implemented such that it complements the privatization process.
9. Help Define the Critical Privatization Program Linkages in the Economy:  
The MIER donor coordination unit coordination continued.
10. Help Establish a Plan to Define and Manage the Technical Assistance Requirements of the Privatization Program:  
Further support was planned for. Funding is awaited.
11. Help Integrate Spontaneous Privatization, the SPA and the GOH's Privatization Program:  
The focus on investment promotion and the privatization process being market driven rather than principally government initiated continues to be the proper track and broadening common need recognition. The "100 Questions" project and data base integration directly supports this. The new self-privatization initiative is an imaginative and systematic response to this task requirement and the warrant system should provide significant capital investor support to the privatization process.
12. Help the GOH and the SPA Understand the Role of ESOPs and Specialized Tools That May Have a Suitable Role in the Privatization Program:  
The Warrant system's definition and how to contract out the core of the Self-Privatization programs start-up are creative initiatives in this area.