Article by the High Representative, Wolfgang Petritsch:”A Free Market Requires a Change of Thinking”

Just at the end of October a Swiss firm Lemano Trading Co. (LTC) bought the TKM textile company in Mostar. TKM manufactures thread. It got into difficulties several years ago because it was uncompetitive. A state-owned company, it lacked the money to invest in new machinery, which would allow it to produce more cheaply and more efficiently. In 2000, faced with continuing losses, it closed down and laid off its workers. TKM, though, still had considerable value – even after it had stopped operating. It had factory space, machinery and a list of workers and managers who knew how to run the factory and operate the equipment. What TKM lacked was cash to upgrade the equipment, retrain the workers and market the product more aggressively. This is what LTC brought to the table. It committed 5 million DM to the Mostar company – and now TKM and its employees are back in business. The original workers, more than 200 of them, have got their jobs back and there is a strong possibility that new jobs will be created.

The TKM story has a happy ending. It is a happy ending that may become more common as the privatisation process in Bosnia and Herzegovina picks up speed, and companies here begin successfully to attract domestic and international investment. In the coming months the pace and the scale of privatisation will increase to a degree that will set the stage at last for the real economic transformation of BiH. I use the term “set the stage” because this transformation isn’t going to happen by itself, as if by magic. Successful privatisation requires a change of thinking. When a company is privatised the hard work begins: it has to adapt to the conditions of the free market, and adapting can be painful before it is profitable.

Around eighty large companies in the Federation and fifty in the RS are currently being sold or are being prepared to be offered for sale. These companies occupy key positions in the economy, either because they employ a lot of people, or because other companies depend on them for business. The sale of these companies will generate as much as two thirds of all the cash likely to be raised by the State through privatisation.

About 45 percent of all small and medium-sized companies earmarked for sale have already been sold. By the end of 2002, the bulk of the remaining 55 percent will have been sold. Overall, by the end of next year a full two thirds of all companies that have been earmarked for privatisation will have been privatised.

Privatisation in other transition economies has been a hugely complicated undertaking producing mixed results. In BiH, the process has been made even more difficult as a result of the chaos and economic dislocation caused by the war.

Many of the problems have now been addressed, however. International advisors have been appointed to help with the sale of large companies – their job is to get the best deal, in terms of investment, technology transfer and cash, for BiH, and to ensure that everything is done in a fair and transparent manner.

The difficult post-war transition, from a centrally-planned model to a free market, has necessitated a fundamental change of thinking, right across the board. Many people, of course, are taking time to become accustomed to this. Indeed, some people are still waiting for the revival of the old industrial conglomerates, hoping that they will once again employ thousands of workers just as they used to. Very often, people assume that these giant companies, once the pillars of the economy, must still be extremely valuable. The truth is that those which survive and eventually prosper will do so only by transforming themselves in fundamental ways – adopting new methods of production and marketing and introducing new products and services. In the case of many companies this will mean laying off workers. However, a successful transition to the free market will produce more and more small and medium-sized companies, which in turn means that more and more new jobs will be created.

In the free market, the competitive delivery of goods and services is the only thing which distinguishes a successful company from an unsuccessful one.

A successful company generates profits and creates jobs. An unsuccessful one doesn’t. It has little do to with a firm’s history or its name; it has everything to do with its efficiency.

Till now, people have been asked to embrace the free market, yet the market itself has failed to deliver many tangible economic benefits. The privatisation process has been in that sense a disappointment. Inevitable difficulties have been compounded by basic flaws in the economic system. For example, until this year, the absence of an efficient commercial banking system severely hampered privatisation since potential domestic investors could not get credit to buy shares or invest in newly-privatised companies. While this is still a problem, the commercial banking sector is becoming increasingly responsive to the needs of entrepreneurs.

In the final analysis, there is not enough cash in Bosnia and Herzegovina to provide all the newly-privatised companies with the investment they need in order to buy new equipment and introduce new products and services. Some of the funds necessary to inject life into the market must come from abroad – and the era of massive international aid is over. So entrepreneurs must attract foreign direct investment (FDI). TKM is one recent example of successful FDI. Others include the Birac aluminium plant in Zvornik, which was sold at the end of October to the Lithuanian investment bank Ukio. Ukio acquired 64% of Birac for a long-term investment commitment of 10 million KM. The paper company Celex in Banja Luka was successfully tendered and the final sales contract with a Slovakian investor was signed at the beginning of November 2000. The Slovenian-backed Prevent company in Visoko recently bought 42% of the UNIS/Volkswagen joint venture in BiH and plans to manufacture 30,000 to 35,000 cars here, the bulk of which will be exported, and Fabrika Cementa Lukavac was sold to Alas International of Austria in October 2001.

In my own country there was a spirited debate during the 1970s over the advisability of encouraging foreign companies to invest heavily in Austrian firms. Many people feared that this would result in foreigners "buying up" our national wealth. Yet in the transition from the post-war nationalised economy to the successful market-oriented model we have today, it was vital to attract funds from abroad. Foreign money brought with it foreign technology and foreign expertise. This created local jobs and local opportunities. The modern economy is global, not national, and increasingly the financial ownership of companies reflects this. The foreign investment which poured into Austria in the seventies and eighties helped transform the country's productive base. The same can happen in Bosnia and Herzegovina. A look at comparative unemployment and FDI figures for Bosnia and Herzegovina and its neighbours is instructive. BiH now attracts US$14 per capita in FDI, while Croatia attracts US$299 per capita. If you look at the unemployment statistics; in BiH currently estimated at 40 percent, whilst in Croatia the figure is 13 percent, the link between FDI and employment is clear.

Privatisation and FDI go hand in hand. They are instruments of wealth creation which have proved themselves in other countries making the transition to a free market. This fact will be worth remembering in the coming months.