

## Companies of Special National Interest in Croatia

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**For the first time in its history Croatian Parliament is debating the operations of companies of special national interest. Sixty nine companies with a labour force of over 100,000 are concerned. Of this number, in 2009 28 companies made a profit of 1 billion and 41 a loss of 4.5 billion kuna. For most of the companies, plans for privatisation should be drawn up, including the withdrawal of government representatives from their management structures. The current government deserves praise for having been the first to place the problem of the financing and the financial sustainability of these companies on the agenda of Parliament.**

The objective of this paper is to set out the main features of the Government's report on the operations of companies of special national concern for 2009.<sup>1</sup> The report is in the parliamentary procedure, and thus for the first time since the acquisition of independence Parliament will debate on the financial operations of companies in which the government has equity of from 20 to 100%.

The report contains an analysis of the business operations of 69 companies/groups that have a special status in line with the Decision of the Croatian Parliament concerning a list of companies of special national interest (*Official Gazette* 132/2009, 56/2010). The government is the majority owner in 21 of these companies. In short, these are companies that in 2009 employed 110,504 people, had expenditures of 76.8 billion kuna and revenue of 74.1 billion kuna, in 2009 making a net loss (after taxation) of 3.5 billion kuna. Twenty eight companies made a pre-tax profit of 1 billion kuna, and 41 a net loss after taxation of 4.5 billion kuna.

According to its importance for the Croatian economy and its future development this is probably, after the budget, the second fundamental financial report. The report should provide a framework for dialogue in Parliament, as well as among the parliamentary parties, concerning the future strategy of privatisation and the withdrawal of government involvement in companies that are not of primary national importance.

We should mention that some of the reports of these companies are accessible on the pages of the capital market (Zagreb Stock Exchange) and the Financial Agency and are published yearly on the Government's own site. Unfortunately, the specialised and general public has not assigned enough importance to the information that exists nor have the analyses of the financial operations of companies of special national interest been the topic of any reasonably deep and adequately supported public debates unhampered by narrowly political concerns.

Although all governments to date (often in closed session) have debated these reports, Parliament, the principal representative body of the citizenry, has not had that privilege. Data in the report are founded on official data from basic main financial reports of companies/groups for 2009 and 2008, operational reports for 2009, decisions made by companies on how to distribute profit made, or how to cover the losses made, and on data of the Financial Agency.

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<sup>1</sup> The full text of the report (with tables of 196 pp.) is publicly available on the Web site of the Croatian Parliament [<http://www.sabor.hr/Default.aspx?art=35628>].

Because some of the companies did not hold board meetings there was a technical problem in the collection and integration of the financial reports. In line with the provisions of Article 50 of the Law on Amendments to the Companies Law (*Official Gazette* 137/2009) a board meeting has to be held in the first eight months of the business year (by August 31 at the latest), but not all the companies held board meetings by the statutory deadline.

The report refers to a motley spread of companies from all branches of the economy, but particularly from the power industry, agriculture, tourism, shipbuilding and the financial sector (one insurance company and two state-owned banks). Some of these companies are quoted on the ZSE, and so it is strange that they should also be on the list of companies of special national interest. These are in fact companies that are also the main users of government guarantees.

A review of these companies shows that the influence of the government (exerted through equity and management) has been retained in spite of all the privatisations in the last twenty years. The report can be characterised as a preliminary credit analysis showing that a considerable number of these companies have structural problems. And because of these problems, commercial banks and international financial institutions have to think hard as to whether there is any sense in maintaining credit lines until restructuring is carried out, and not over the long term, but as fast as possible. The results of the report are in fact an excellent opportunity for the Government to come out clearly about the status of most of the companies in which the government has a stake of less than 25%, as well as of companies that irrespective of the size of the government's equity are a burden on the central government budget and on the taxpayer. For years now some of these companies have contributed nothing to the growth of GDP in spite of their privileged positions of "natural" monopolists, while the government has additionally gone to bat for their credit liabilities by issuing guarantees.

What the report is missing are concrete proposals and conclusions concerning future steps in the restructuring and privatisation of the companies. In an optimistic scenario, such conclusions and recommendations could be the outcome of well-supported debate in Parliament, which should be of assistance in the profiling of a clearer vision of the status the companies and future steps to be taken in their restructuring and privatisation. The integrity of the document is to an extent distorted because of the absence of information about guarantees that have been issued and are still active (since they are off-balance-sheet records), for this information would provide an insight into the real scale of state aid to these companies. The report is also partially lacking since it does not contain information about members of the boards of supervision and the management structures. The quality of the report would have been considerably improved if the financial reports of the companies had been appended (balance sheets and profit and loss accounts). But these are only lesser and technical problems that are partially result of the poor professional capacity of the boards of management of the individual companies that did not hold their board meetings in time and did not provide timely and standardised information. Unfortunately, until this day not a single government has laid down the framework for or strategy of the privatisation and sale of the minority holdings in companies that might, were there no interference from representatives of the government in the management bodies, become attractive for investors in the capital market. The withdrawal of state equity from companies that do not primarily provide public goods and services would be an excellent signal for greater capital market activity. This would be sure to provide stability and would ensure investors and majority private owners new outlooks not only for investment but also for further restructuring of the companies.

The Report might be used by Government and Parliament to:

- define clearly a framework for the privatisation of companies in which the government has minority holdings and a plan of withdrawing representatives of government from the supervisory and management structures of the companies;
- define criteria for obtaining the status of company of special national interests (one might wonder why Vupik, Podravka and Končar are of special national interest while Konzum, Našicecement, Magma, Siscia and so on are not);
- evaluate the costs and benefits and expected financial effect of a potential privatisation of some of the companies of special national interest, and to determine the order for (strategy of) privatisation while laying down steps for the resolution of structural problems in the financing and financial viability of existing companies;
- introduce rewards for present and future members of boards of management according to the financial performance of the companies. Success in creating greater profit – which as well as being retained in the companies should also be paid into the government budget – should be rewarded, but the opposite also holds true, and those who do not contribute to the achievement of the primary mission of a company should be penalised by salary reductions and indeed dismissal.

I believe that the positive effect of the publication of a systematic analysis of companies of special national interest will reflect on representatives of local government units, mainly of cities. City authorities and their assemblies should also, by analysis of companies in majority ownership, determine priority companies for the provision of public utility services, and should privatise companies in activities that are not within the primary focus of the public but of the private sector.