

Troschke, Manuela; Zeitler, Andreas

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Privatisation and corporate governance in Kazakhstan and Uzbekistan: insights from a corporate survey in food and light industries

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**Privatisation and Corporate Governance
in Kazakhstan and Uzbekistan:
Insights from a Corporate Survey
in Food and Light Industries**

Manuela TROSCHKE and Andreas ZEITLER



**OSTEUROPA-INSTITUT
MÜNCHEN**

Scheinerstr. 11
D-81679 München
Telefon: 089/99 83 96-0
Telefax: 089/98 10 110
E-Mail: oei@oei-muenchen.de
Internet: www.oei-muenchen.de

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Abstract

This paper presents the results from a private sector survey among companies of the food industry in Kazakhstan and Uzbekistan as well as of the light industry in Uzbekistan. It provides microeconomic evidence on the change in the companies' ownership structure resulting from the privatisation programmes as well as the development in more recent years. The privatisation of companies was more profound in Kazakhstan than in Uzbekistan where the state still retained larger shares in its companies and even managed to re-increase its stakes due to strategic considerations. While the data confirm and prove the extent of the insider privatisation in Kazakhstan, Uzbek companies' ownership got more dispersed and company insiders play a very subordinate role. The use and design of manager contracts in these two countries does not turn out to feature basic incentive components on a broad scale as in the case of the Chinese management contracts contradicting the hypotheses of a similar application in Uzbekistan's de facto state enterprises. Company control was highly transferred into the responsibility of corporate bodies in both countries though state interference in the companies' affairs remains an important aspect of doing business, especially in Uzbekistan. The companies face further obstacles which hinder and retard the development of a sound private corporate sector, especially a high tax burden and bureaucratic red tape, macroeconomic instability, lack of finance and an inadequate provision of infrastructure. The state, especially in Uzbekistan, still intervenes in the private sector in favour of selected companies which improves these companies' perception about the role of the state. On the other hand, this state behaviour prevents or at least delays the dissolution of the inherited structural and corporate distortions which would improve corporate efficiency and would be essential for a successful transition to a market economy.

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1 Introduction

Privatisation experiences in the transition countries have been mixed. In this respect, two insights from the debate on the effectiveness of privatisation seem to be most important for the Central Asian Republics (CARs). The first is that positive effects of privatisation seem to be much harder to achieve the further east a transition country is located. This only refers to the transition countries of Central and Eastern Europe (CEE) and the Former Soviet Union (FSU) and leaves the CARs as the most eastern peripheral region. This relationship is primarily explained by the will and capability of governments to implement the necessary reforms (Nellis, 1999). This is confirmed by a cross-country study by Sachs, Zinnes and Eilat (2000) who find no automatic positive growth effect of privatisation but suggest that this is present if privatisation is accompanied by in-depth institutional reforms. The second insight is that “some of the fastest large-scale privatizers (e.g., Russia, Ukraine, and the Czech Republic) experienced a decline or slow growth after privatization in the 1990ies, while some of the fastest growing transition economies in the 1990ies (e.g., China, Poland and Slovenia) were among the slowest to privatize” (Hanousek, Kocenda, Svejnar, 2004, p.1).

In this regard, the theoretical background for a comparison between Kazakhstan and Uzbekistan stems from the discussion about the different transition paths of China and Russia, the two most populous transition economies. While China is regarded as a slow and gradual reformer resulting in an miraculous economic success story, the Russian Federation chose a big-bang reform strategy and experienced a U-shaped development of economic activity, i.e. a harsh decline followed by a resource-driven recovery. In this respect and although both countries evolved from the dissolution of the Soviet Union in 1991, Kazakhstan is often viewed as a blueprint of Russia and Uzbekistan is compared to China as following some kind of an Asian reform path (Klugman, 1998, Pomfret, 2001 and 2003, Spechler, 2000). The initial economic development during transition underpinned this view as Uzbekistan avoided a harsh economic decline. More recent growth data point the other way as Kazakhstan outpaces Uzbekistan due to its mineral wealth.

Corporate governance problems¹ accruing from the separation of ownership and control have been extensively studied for Russia and China. But with regard to their smaller Central Asian counterparts, data availability restricted their contribution to this debate. This study provides information which addresses to fill in this gap. The paper introduces the basic results from a detailed firm-level survey conducted among 31 Kazakh enterprises active in the food industry and 77 Uzbek companies, 38 of them active in the food industry as well as 39 from the light industry sector. While the results are based on a rather limited set of observations, the survey is exceptional in providing very detailed microeconomic evidence on the corporate development in these two most important CARs. This detailed information will be revealed in a comparative perspective of the two countries and the different sectors as well as over time. The data were col-

¹ For a survey of corporate governance, see Shleifer and Vishny (1997).

lected for three different points in time and thus along two periods of time: the year of privatisation or 1997 (in case no change of ownership had taken place until that year), the year 2000 and the latest available data point in 2003 or 2004.²

The study is structured as follows. Chapter 2 provides information on the questionnaire, its structure as well as some problems with its development and conduction. Chapter 3 presents characteristics of the surveyed firms, their location and industry, their company sizes, as well as the timing and extent of privatisation and the use and design of manager contracts. Chapter 4 reveals insights into the development of company control and state interference in relation to the property share of the state. Chapter 5 investigates business problems faced by the companies both according to a general question and a more detailed analysis of different problem areas. This comprises all sorts of problems with the judiciary, the bureaucracy and resulting unpredictability and insecurity as well as problems with finance and competition. Some performance indicators, restructuring efforts And the development of wages and wage spreads within the companies will be revealed in Chapter 6. Chapter 7 concludes.

² For simplicity reasons, these dates will in the coming text be mostly referred to as year of privatisation, 2000 and 2003. In the case of 2003, all data about the performance of the companies as reported in their financial statements (including the number of employees) as well as about the property structure, restructuring efforts and the development of wages, are based on this year while data on the current perception of the respondent refer to the survey date at some point in the second or third quarter of the year 2004. This concerns the questions of Section 3.5 (manager contracts) and Chapter 4 (company control and state interference).

2 The Questionnaire

The questionnaire was primarily designed to reveal information about the processes of privatisation in these two countries as well as about the use and incentive components of manager contracts. It provides data on the performance of the companies since privatisation and on the control of and the extent of state interference in the enterprises. The questionnaire generates a comprehensive picture about the firms' development and impeding factors since privatisation and enables to check for important aspects of companies in transition. It aims to compare corporate outcomes over time and between the two CARs, Kazakhstan and Uzbekistan. These aims drove the selection of the companies. Food and light industries were chosen in order to concentrate on local corporate developments and phenomena and to secure a favourable return.

2.1 Development of the Questionnaire

The questionnaire was created in several steps during the first half of 2004. The original version of the questionnaire was written in German. It was subsequently translated into Russian which brought about some problems. Some Russian expressions are differently applied in Kazakhstan and Uzbekistan and the recordance of balance sheet positions varies between the two countries. The more, some answering possibilities for questions concerning the control and the managerial structure of Kazakh enterprises are not relevant for the Uzbek companies and vice versa and lead to misinterpretation. These insights led to consequent changes in the questionnaires as did consultations with the local cooperation partners, the Economic Research Institute (ERI) in Almaty, Kazakhstan, and the Center for Effective Economic Policy (CEEP) and the Ministry for Privatization in Taschkent, Uzbekistan, and test surveys conducted with a small sample of directly chosen firm representatives of some surveyed companies. As a result, the survey design was highly adapted to local standards concerning the comprehensibility of the questions and the preparedness and possibility to reveal information on the companies. Nonetheless, the questionnaires for the two countries were kept as similar as possible with identical ordering and numbering. On behalf of the Uzbek cooperation institute, an additional part of questions concerning the firm's knowledge of the stock market in Taschkent was added to the Uzbek questionnaire the results of which are not presented in this paper.

2.2 Structure of the Questionnaire

The questionnaire consists of 52 questions divided into five parts

- **Economic characteristics:** The first three questions of the questionnaire address the issue of firm performance since privatisation or the year 1997. The first question reveals data on revenues, profits, average wages and the number of employees for the years of the earliest privatisation (or alternatively 1997), 2000 and 2003 as recorded in the firms' financial statements. Additionally, Kazakh companies were asked to provide information on labour productivity and Uzbek companies on actual costs. The other two questions concern the subjective assessment of the firm's respondent about the development of the firm's economic characteristics in the periods from privatisation to 2000 and 2000-2003 and his expectations for the next three years 2004-2007 in comparison to 2000-2003.
- **Structure of ownership and control:** This part contains six questions and provides information about the privatisation process, the resulting legal form of the private company as well as possible transformations, and the structure of ownership in the year of privatisation as well as 2000 and 2003. It reveals information about the person(s) or institution(s) controlling important business tasks and the extent of control exerted by the state.
- **Restructuring and wage development:** Seven questions ask about the restructuring efforts of the companies in certain areas as well as the development of wages and wage disparities within the company.
- **Managerial structure and incentives:** This part was designed to reveal insights into the incentive structure for the manager(s) of the company as laid down in available manager contracts and its corresponding implementation approximated by the personal changes in the board of directors.
- **Problems of business operation:** This last part of the overall questionnaire contains 23 questions concerning the problems the companies face in their business environment. One general question provides insights on problems along a list of 13 different areas and asks to evaluate their extent on a four choice scale ranging from no to major obstacle which is commonly used in this context. The ongoing questions more specifically refer to problems in the fields of the judicial system, the bureaucracy, and problems with financing, competition and the unpredictability of laws and regulations.

The next three sections present the results starting with basic characteristics of the surveyed firms.

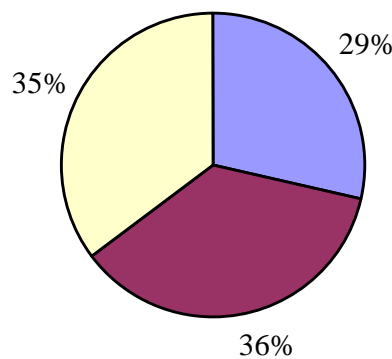
3 Characteristics of the Surveyed Firms

This chapter demonstrates the differences of the responding enterprises according to location (Kazakhstan or Uzbekistan) and industry (food industries in Kazakhstan and Uzbekistan, light industry for Uzbekistan only), company size in terms of the number of employees, the time and extent of privatisation, the resulting property structures and the use and design of manager contracts.

3.1 Location and Industry

The surveys were conducted among 31 firms in Kazakhstan and 77 firms in Uzbekistan. More than two thirds (71.3%) of the surveyed firms are located in Uzbekistan, the smaller but on the other hand more populous country. All Kazakh firms are exclusively active in the food (processing) industry while the Uzbek firms are almost equally divided among the food (processing) and light industries, 39 and 38 enterprises respectively. Figure 1 presents the relative distribution among the firms according to their location and industrial activity.

Figure 1: **Shares of Subsamples according to Country and Industry**



■ Kazakhstan, Food Industry ■ Uzbekistan, Food Industry ■ Uzbekistan, Light Industry

Despite the limited number of companies, they account for 15% of the sectoral employment in Kazakhstan in the year 2003 and more than 20% of output in the two in-

dustrial sectors in Uzbekistan. The 29 Kazakh companies reporting data on their workforce employed 9,218 people constituting slightly more than 15% of the 60,800 employees in the Kazakh food industry.³ 36 of the surveyed Uzbek companies of the food industry generated combined revenues of 176.6 billion UZS in 2003 and thus 23.4% of the total 756 billion UZS in that sector. The combined output of 37 of the surveyed enterprises of the light industry amounted to 184 billion UZS in 2003 or 32.4% of the total 568 billion UZS in that sector.⁴

3.2 Company Size

As can be seen in Table 1, the Uzbek firms are on average bigger than their Kazakh counterparts in terms of their number of employees. Among the Uzbek companies, the firms active in the light industry sector are much bigger than the ones of the food industry whose average size comes closer to the average Kazakh firm. Over time, the average firm in the whole sample became smaller. It lost on average 299 or 29% of its employees between the year of privatisation (or 1997) and 2000 and 82 or 12% between 2000 and 2003.⁵ The diminishing average company size is heavily due to the decrease among the Uzbek companies of the light industry sector. While the Uzbek food companies slightly lost in size as well (especially between the year of privatisation and 2000), their Kazakh counterparts increased their number of employees, especially between the years 2000 and 2003.⁶

³ The companies of the Uzbek sample employed 12,778 people in the food and 37,819 people in the light industry, both values being based on 28 companies in each industrial sector. Labour figures for the whole industrial sectors are not available for Uzbekistan.

⁴ Total revenues in the Kazakh food industry amounted to 13.9 billion KZT in 2003.

⁵ These two mean differences refer to the firms reporting data for both points in time of the respective periods, i.e. 80 between privatisation and 2000 and 101 between 2000 and 2003. As such, they do not coincide with the values reported in Table 1 which indicate a reduction of 352 or 35% in the number of employees between privatisation and 2000 and 89 or 13.5% between 2000 and 2003.

⁶ Note that the number of firms which reported data on their number of employees increased over time. Among the 79 companies for which we have data for all three points in time, the average number of employees decreases from 1028 in the year of privatisation (or 1997) to 625 in 2003, i.e. a bit less dramatically. Among the three subgroups of companies, Kazakhstan Food increases less profoundly from 225 to 276 employees on average (while it even slightly lost between privatisation and 2000), Uzbekistan Food decreases even more from 415 to 292 while Uzbekistan Light decreases less, from 2235 to just 1213. After all, the basic statements about the development of company size do not change.

Table 1: **Company Size: Means of the Number of Employees**

	1997		2000		2003	
	Mean	N.O.*	Mean	N.O.*	Mean	N.O.*
Whole Sample	1010	81	658	102	569	105
Kazakhstan Food	230	24	252	28	318	29
Uzbekistan Food	409	28	389	38	336	38
Uzbekistan Light	2235	29	1258	36	995	38

*N.O. refers to the number of observations and varies between the years

The characterisation of firm size is conducted along three groupings which can be found in Table 2 and are often used this way (see e.g. Brunetti, Kisunko, Weder, 1997). The number of small firms in the sample with less than 50 employees increases over time as the average Uzbek company decreases.⁷ In Kazakhstan, the number of big companies decreased while the small and medium-sized companies became more pronounced and even increased the average firm size as a whole. The bigger Uzbek companies are highly concentrated in the medium- and large-scale categories. The light industry sector almost exclusively consists of big companies with more than 200 employees.

Table 2: **Company Size: Number of Firms according to Employment Size Categories**

	less than 50 employees			50 - 200 employees			more than 200 employees		
	1997	2000	2003	1997	2000	2003	1997	2000	2003
Whole Sample	6	7	15	19	33	32	56	62	58
Kazakhstan Food	4	5	6	10	16	15	10	7	8
Uzbekistan Food	2	2	5	7	12	12	19	24	21
Uzbekistan Light	0	0	4	2	5	5	27	31	29

3.3 Privatisation

Both countries started their privatisation procedures soon after their independence at the end of the year 1991. Kazakhstan relied on a series of privatisation programmes each designed for two consecutive years and differing in the preferred group of new owners. While the early privatisation in 1991/92 favoured the labour collective, 1993 until 1995 saw the wave of mass privatisations. Starting with 1996, the prevailing method for changing ownership became auctions and insider (manager and employee) buy-outs. Uzbekistan started with small-scale privatisations in 1992/93. After introducing a law

⁷ Note again that the number of firms reporting data increased over time. However, this does not affect the outcomes as the companies which did not report all three observations are relatively evenly spread among the three company sizes.

establishing priorities in the privatisation course in 1994, companies active in construction, engineering as well as food and light industries were chosen to be the primary targets of the privatisation process.

With regard to the surveyed companies, all of them reported having been privatised since 1992 (Table 3).⁸ While the Kazakh firms were smoothly privatised along the years (with no privatisations taking place between 2001 and 2002)⁹, the privatisation of Uzbek companies in both sectors peaked in the year 1994, due to the affiliation to a certain sector.

Table 3: **Privatisation: Number of Firms according to the Year of Privatisation**

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2003	Total
Whole Sample	5	5	57	14	8	3	5	3	4	2	106
Kazakhstan Food	5	2	4	2	5	2	4	3	2	2	31
Uzbekistan Food		1	22	11	3	1			1		39
Uzbekistan Light		2	31	1			1		1		36

Table 4: **Privatisation: Number of Firms according to Company Size Categories and Year of Privatisation**

	Emp. Size	1992	1993	1994	1995	1996	1997	1998	1999	2000	2003	Total
Whole Sample	< 50			3	1	1		1				6
	50-200	1	4	5	3	2	2	2				19
	> 200	3	1	37	8	3	1		2		1	56
Kazakhstan Food	< 50			1	1	1		1				4
	50-200	1	2	1	1	2	1	2				10
	> 200	3		1		2	1		2		1	10
Uzbekistan Food	< 50			2								2
	50-200		1	3	2		1					7
	> 200			11	7	1						19
Uzbekistan Light	< 50											
	50-200		1	1								2
	> 200		1	25	1							27

⁸ Two Uzbek companies from the light sector industry did not fill in the year of privatisation. However, their data about the property structure reveal that they have been (partly) privatised, i.e. that some share of ownership was transferred into private hands.

⁹ It should be noted that one Kazakh firm specified being privatised in the year 1993 but retained a state ownership of 100% until 2003. As such, privatisation does not necessarily mean that some share of the company is transmitted into private ownership but that the company is basically transformed into a new legal entity. However, in all other cases this included some transfer of ownership stakes in private hands.

There is no evidence that company size affected the timing of privatisation in the three groups of companies. While the early privatisation of the bigger Uzbek companies generates an overall negative relationship among company size and the timing of privatisation, there are no signs in our data that Kazakhstan initially preferred small-scale privatisations, as can be seen in Table 4.

3.4 Ownership structure

An important aspect of the survey was to trace the changes in the property structure since the privatisation. Some introductory insights into the privatisation processes of these two CARs may be helpful. First, Kazakhstan is widely viewed as a fast reformer among the CARs with profound progress in small- and large-scale privatisation. Uzbekistan is rated as a slow or gradual reformer among the CARs. In comparison to Kazakhstan, it shows less progress in privatisation although the gap is smaller than in other reform areas.¹⁰ As a first consequence, we expect to find a faster and deeper decline in state shares among the Kazakh companies while the Uzbek state retreats to a lower extent. Second, Kazakhstan is widely viewed to have pursued a deep insider privatisation like Russia. The prevailing privatisation methods as specified by the EBRD were direct sales and voucher privatisation. Especially as a result of the rapid mass privatisation programmes the companies became controlled by management insiders with detrimental consequences for corporate governance and restructuring (Frensch and Nowak, 2003). The aim of the survey was to reveal microeconomic evidence on the extent and depth of the insider privatisation and the relative importance of the two groups of insiders, the managers and the employees. We thereby expect the insiders to be the most important beneficiaries of the privatisation in Kazakhstan. Third, the institutional vacuum in Kazakhstan with a weak legal protection of minority shareholders seems to have benefited the managers which have a clear information advantage over the employees. As such, we expect the ownership shares of the managers to increase over time to the detriment of the employees' stakes. Forth, the beneficiaries of the Uzbek privatisation are not as straightforward as in Kazakhstan. The EBRD specifies MEBOs (Management and Employee Buy-outs) and direct sales as the predominating methods of privatisation. Although these methods should favour insiders as well, we do not expect them to have played an equally important role in the Uzbek privatisation process as in Kazakhstan. This stems from the prevailing social aspects of the reform agenda in Uzbekistan favou-

¹⁰ The EBRD indices rate the progress along certain reform areas for the transition countries, ranging between 1 and 4 with a higher value denoting further reform progress. While the overall picture clearly confirms Kazakhstan's lead in its overall reform efforts over Uzbekistan, Kazakhstan only wins by a narrow margin for its two privatisation indices. Kazakhstan's index of small-scale privatisation scores 4 from 1997 up to 2005 (latest available year), its large-scale equivalent 3 since 1996. On the other hand, Uzbekistan's privatisation progress is rated at 3 for small-scale and 2.7 for large-scale privatisation, both since 1995 (see EBRD Transition Reports, various years).

ring equality and the avoidance of disorder (similar to the levels observed in Kazakhstan and the Russian Federation) due to a firmer state.

Conclusively, the aim of this survey was to get microeconomic evidence about the deepness of the insider privatisation in Kazakhstan and reveal information about the new owners as well as persisting state shares in Uzbekistan. The presentation of the survey results will be pursued as following. After introducing some basic information about the survey question and the ownership groups, we will trace the decline in state shares emphasising the difference between Kazakhstan and Uzbekistan. The beneficiaries of privatisation will be presented separately for the two countries tracing the extent and development of the Kazakh insider privatisation and identifying the dispersion of private ownership along certain groups of owners in Uzbekistan.

The question for this section asked the firms about the resulting property structure in the year of privatisation (or in 1997) as well as 2000 and 2003. They had to specify the shares held by different owner group categories: the state, private persons with information about shares of two groups of company insiders (insider group 1, the managers, and insider group 2, the employees), legal persons and foreign share holders of any kind.¹¹ The presentation of the ownership structure is pursued along three categories of ownership stakes: up to 25%, more than 25% and up to 50%, and more than 50% for the different owner groupings.¹² Every company thus belongs to one of these ownership share categories for every owner category mentioned above.

Figure 2 shows the division of ownership among the whole sample. The ownership structure is specified by the percentage of firms in the three categories recorded for the different owner groups and the three points in time respectively. The upper three bars show that the state shares in the companies are decreasing since the privatisation of the enterprises. This is not only driven by the ongoing privatisation process in Kazakhstan

¹¹ The subgroups were chosen to be as simple and exclusively as possible in order to reveal data about the exact division of ownership in the companies. However, the answers were not as exclusively as we wanted. A Kazakh company reported both a 100% ownership of a private and legal person in a single year which was assumed to be just totally held by a private person. On the other hand, the ownership shares did not always sum up to 100% for the Uzbek companies. One reason was that the Uzbek questionnaires asked for the property share in companies' "unsold" stocks as well. As these stocks are de facto still owned and, more importantly, its control rights executed by the state, the shares were combined wherever they helped to reduce or fill the gap to a total distribution of ownership (shares of "unsold" stocks range on average between 16% (2003) and 24% (2000) for the 9-12 Uzbek companies over the three time periods). On the other hand, shares among the ownership groupings added up to more than 100% in some cases indicating that, as for the Kazakh company specified above, the groupings may overlap. Nevertheless, though we cannot assume that these two effects cancel each other out, the data are used nevertheless as most deviations are small and the data about the shares of the state are very reliable as these data were filled in by the Uzbek partner who conducted the survey and governs the state shares in the companies.

¹² The division was undertaken in broad accordance with legal arrangements about the possibility of state intervention according to its share. The division more reflects the Uzbek system which specifies different degrees of company control along state shares of 0-25%, 26-31%, 32-50% and more than 51% with the middle groups taken together due to the amount of observations and for simplicity reasons. In Kazakhstan, the boundaries are set along the shares of 0-32%, 33-51% and more than 51%. However, the different groupings used here just affect one Kazakh enterprise with a state share of 30% at all three points in time.

since 2000¹³, but also by declining state shares in Uzbekistan where all except for two companies had already experienced some kind of ownership transmittance into private hands before the year 2000. The decline in state ownership and thus the extent of privatisation was much more profound in Kazakhstan than in Uzbekistan. All but three Kazakh enterprises were totally privatised until 2003. The remaining three firms report a state share of 30%, 50% and 100% respectively and continuously since privatisation. In Uzbekistan, the state retained some share in all but six of the surveyed enterprises, four of them active in the food industry and the other two in the light industry. Among the others, the Uzbek state mostly holds a 25% ownership stake of the companies making them count in the lowest of the three categories. However, the state still has the majority stake (51%) in eight companies of the food processing industry in 2003 (see Figure 4), but in none of the light industry (see Figure 5), which seems to be due to strategic reasons.

Contrary to what one would expect in privatising transition countries, state shares did not only decline in Uzbekistan, but also increased due to strategic considerations. This was especially obvious and far-reaching for companies in the food processing industry. Five out of 39 companies reported their state shares increasing again from a low of 25% to an absolute majority stake of 51%. This was initiated by a presidential decree and thus due to strategic reasons as the state or its agencies wanted to keep tighter control of certain food-processing industries, especially the production of alcoholic beverages. The same happened, albeit at a much lower scale and extent, to nine companies in the light industry which saw their state shares increase again to mostly 25%. This also explains the increase in company numbers with higher state shares shown in Figure 5. On the other hand, it indicates the arbitrariness and unreliability of the Uzbek state in the handling of private property rights. Company stakes seem to be easily adjustable to state requirements as almost all the increases helped to cross some threshold of further control of the company.

The striking difference among the two countries turns out to be the resulting new owner groups obtaining the company shares from the state. As expected, Kazakhstan's privatisation in the food processing industry turns out to be an insider privatisation with insiders, managers and employees and thus a subgroup of private (domestic) persons, gaining the highest shares in corporate ownership (see Figure 3). Of the 31 companies, 23 end up entirely in the hands of domestic private persons in 2003. In the case of 20 firms, these private persons exclusively constitute insiders. There is a small indication that the privatisation pattern changed over time. The increase in the ownership share of private persons between the year of privatisation (or 1997) and 2000 is accompanied by rising insider stakes which is to a large degree driven by the two privatisations in 2000. This pattern does not exist between the years 2000 and 2003 (see Figure 3). The two latest Kazakh privatisations among the surveyed firms in 2003 did not constitute insider privatisations (only a 10% stake in one company was taken up by insider group 2, the employees), but almost exclusively benefited agents external to these companies (private persons (100%) in one case and

¹³ If a company had not been privatised prior to the year 2000, the first observation (year of privatisation or 1997) refers to the year 1997 in which the state still totally owned that company. A 100% state share also results for the second observation for the year 2000 if the company was only privatised in a subsequent year which was the case for two Kazakh companies. As such, a reduction in the state shares over time is also influenced by the ongoing privatisation process, especially in Kazakhstan.

legal persons (90%) in the other). This means that the preferred method of privatisation might have changed in more recent years turning away from the high priority of insiders, though the evidence among the surveyed firms is admittedly very small.

With regard to the overall distribution of insider shares among the two groups, ownership is equally divided among managers and employees in five companies (four of them exclusively owned by the two insider groups). Insider group 2, the employees, received on average a higher share in the companies via the privatisation, 39.3% in comparison to 27.5% for insider group 1 (managers). Figure 3 also shows that the employees have lost out some of their ownership stakes over the years. This happened in ten of the Kazakh companies and in one case the managers even took the whole 50% stake gained by insider group 2 via the company's privatisation.¹⁴ In most cases, however, the change in property comprised 5%. The other two owner categories, legal persons and foreigners, play a very subordinate role in comparison to the insiders. Most recently, legal persons gained majority stakes in four Kazakh companies and minority stakes in two of them. With regard to foreign ownership, none of the surveyed Kazakh companies features a foreign investor as most of the foreign direct investment in Kazakhstan is concentrated in the resource-extracting industries.

In Uzbekistan, ownership became much more dispersed among the owner groups after privatisation. As already noted, the state retained much larger shares in its companies, though these were on average decreasing over time (see Figures 4 and 5). Private persons became the biggest owner group and slightly increased their share from an average of 38.55% in the year of privatisation to 39.32% in 2003. In comparison to Kazakhstan, however, these private persons are to a much larger degree external to the companies. Insiders just played a subordinate role both at the first stages of privatisation and also in the subsequent ownership changes. This especially holds with regard to the managers. The ownership share of insider group 1 does not cross the 25% threshold except for one company with a stake of almost 76% in 2003 which only reported data for this single year. This explains the small increase of average holdings of managers from 1.5% in the year of privatisation to 2.1% in 2003 as well as the incidence that another outstanding ownership share of this group was reduced from 24% to just 9.9% between 2000 and 2003. While there are nine Kazakh companies without any shareholdings by managers in 2003, this figure is 13 for Uzbek companies in the food industry and even 22 in the light industry. Otherwise, most shares are negligibly small. As such, managers constituted a very minor receiving group of company owners in the Uzbek privatisation process. On the other hand, insider group 2, the employees, received a much larger share in its companies than the managers. Their stakes, fostered by new privatisation laws, declined enormously since the first privatisation steps from an average of 26.3% to just 11% in 2003. Although the employees constituted a large receiving group of company stakes in the early privatisation efforts, their importance has dwindled since then losing out around eight percentage points on average both between the year of privatisation and 2000 and between 2000 and 2003.

¹⁴ This could, of course, be due to the change of the characterisation of a single person who used to be an employee and became a manager.

Figure 2: Property Structure – Whole Sample

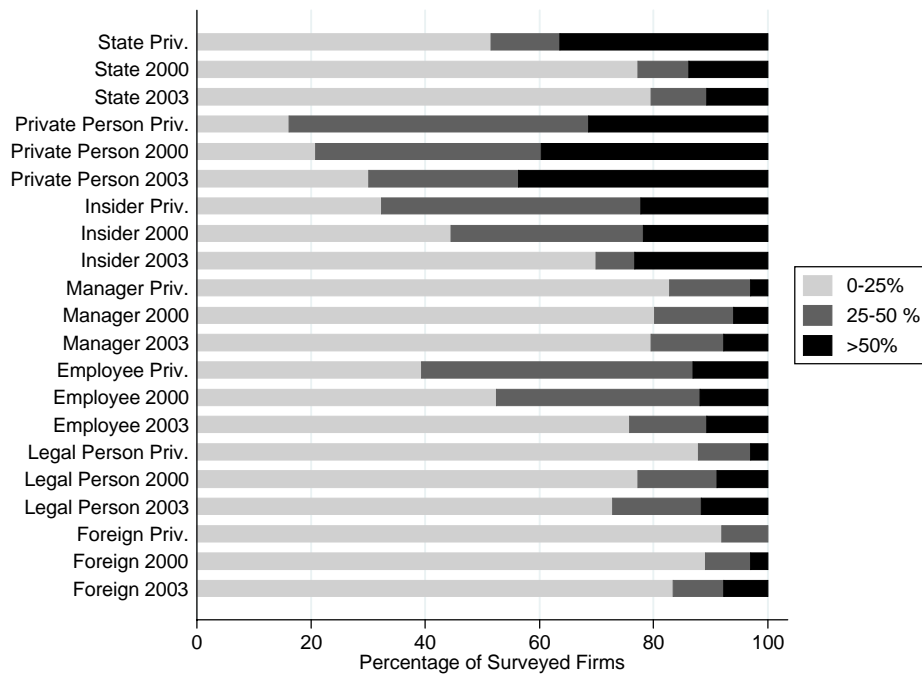


Figure 3: Property Structure – Kazakhstan Food Industry

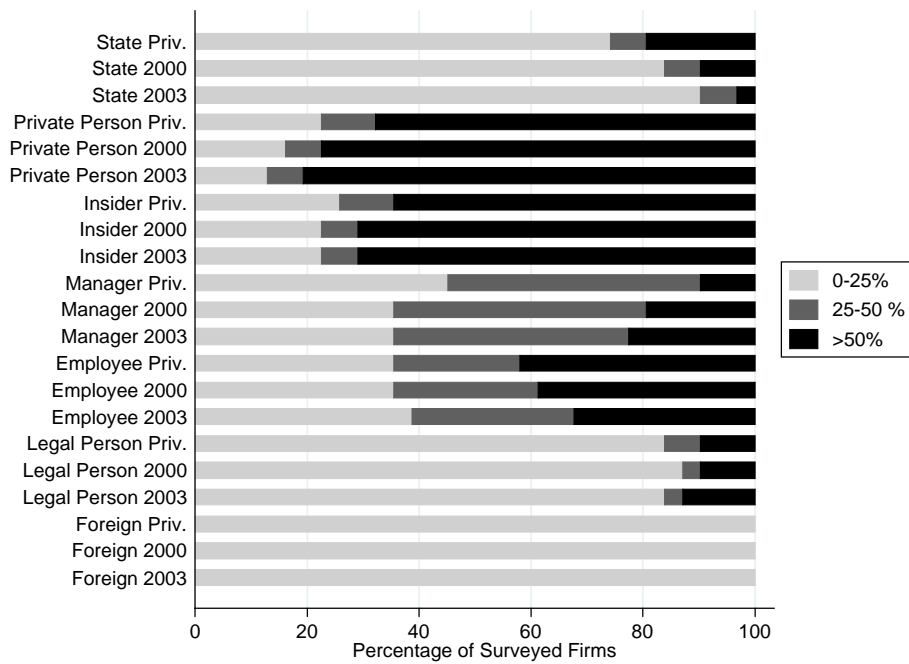


Figure 4: **Property Structure – Uzbekistan Food Industry**

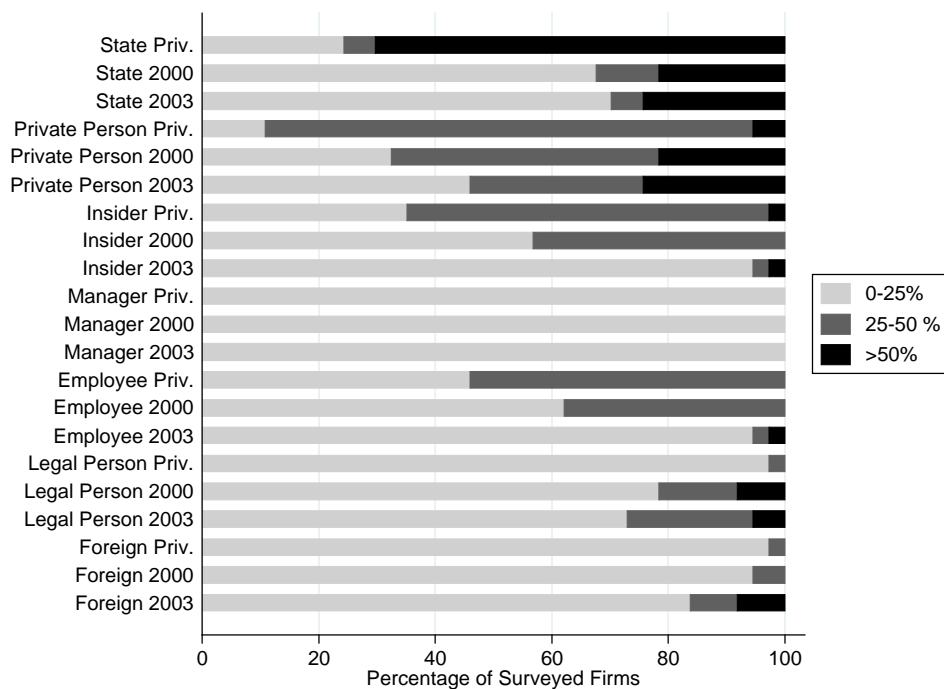
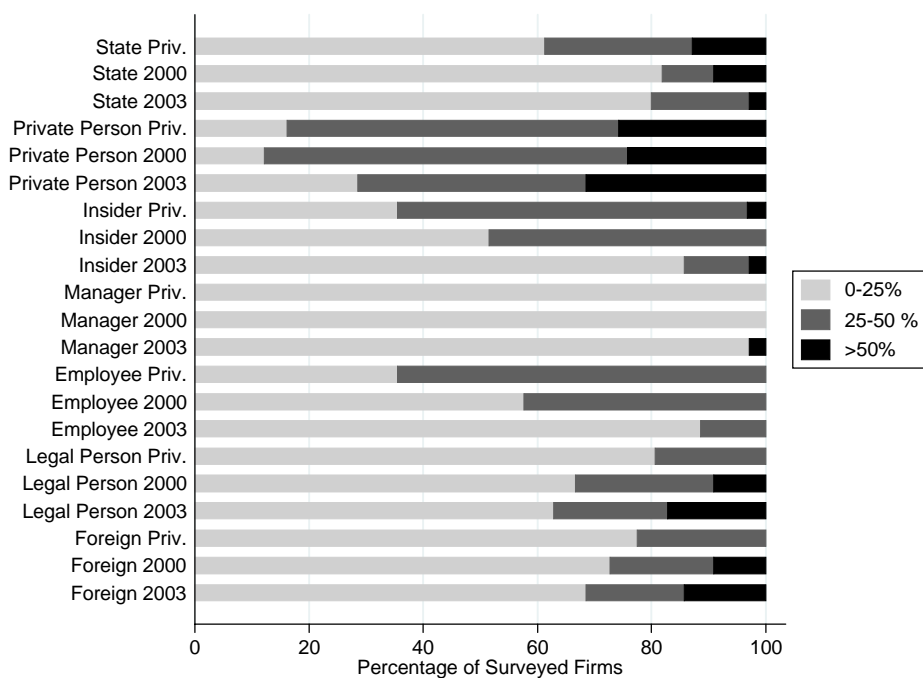


Figure 5: **Property Structure – Uzbekistan Light Industry**



The development of insider ownership turns out to be very similar for the food and light industry. The stakes of insider group 2 are taken up by all other owner groups: external private persons, legal persons and foreigners. External private persons hold on average slightly bigger shares in companies of the food-processing industry while legal persons and foreigners play a bigger role in the light industry.

On the whole, the data confirmed that the privatisation process was more profound in Kazakhstan than in Uzbekistan where the state retained on average larger and in many cases majority stakes in its companies. The more, the data provide microeconomic evidence on the depth of the insider privatisation in Kazakhstan. Equity shares in the Uzbek companies got much more dispersed among the different owner categories with insiders, especially the managers, just playing a very subordinate role.

3.5 Manager Contracts

A section of the questionnaire was devoted to the subject of manager contracts.¹⁵ The aim was to find out about the use and design of manager contracts. These may include incentive components in order to address the agency problems accruing from the separation of finance and management or of ownership and control. Agency problems rise with a firm's demand for external finance and thus in some relation to the company size. These problems increase with the degree of ownership dispersion as single owners have less incentives to engage in costly screening of the management since free rider problems are higher. These problems are more pronounced in less favourable institutional environments which fail in the legal protection of property rights or discriminate against certain groups of owners (e.g. minority shareholders or people with missing political or other connections). Manager contracts may help to align the personal interests of the management with those of the investors or owners. This is possible if the incentive component of the management's remuneration is substantial and sanctions are set and enforceable in case of bad performance (Shleifer and Vishny, 1997).

Manager contracts are viewed as a key component in increasing the efficiency of Chinese state enterprises (see e.g. Groves et al. (1995) and Li (1997)). China's corporate success relied on the implementation of economic reforms that improved the incentives for its state-owned enterprise. This included reforms in the field of competition and de-

¹⁵ It should be noted that the term manager contracts was used in order to refrain from the expression management contracts which, in the economic literature, denotes a certain form of contract with a distinct set of incentives. Manager contract in our case just refers to some non-specified form of contract among a manager and the company owners. This simple form was chosen in order to avoid misconceptions for the survey respondents. However, the aim was to address the question if these manager contracts contain incentive components similar to those of management contracts, i.e. remuneration schemes dependent on firm's performance and sanctions. The results will be presented in the ongoing text and reveal that the incentive components are very limited or mostly non-existent. Thus, the use and design of manager contracts in Kazakhstan's food and Uzbekistan's food and light industries do not support the notion that these may resemble the management contracts used in China.

regulation. The transition countries of CEE and CIS basically more relied on privatisation in order to increase the efficiency of their enterprises. This process mostly took part without an amelioration of the institutional environment regarding the firms. In this context, Uzbekistan puts less emphasis on privatisation (see previous section), but can be considered to follow the Chinese way of improving corporate incentive structures.

Among the surveyed firms, 84 or almost 80% of the responding 106 companies reported about the existence of manager contracts. Contrary to our expectations, while 87.1% of the Kazakh companies make use of manager contracts, only 76% of the Uzbek companies do so. This is due to a relatively low share of 67,5% using contracts among the Uzbek firms in the food industry. According to the above considerations, one would expect the use of manager contracts to increase with the size of the company as agency problems might increase.¹⁶ However, Table 5 reveals that there is no evidence that the use of manager contracts increases with the size of the firms. The table lists the percentage shares of companies with manager contracts according to categories of company size and of ownership shares of different groups in the year of privatisation (or 1997).¹⁷ Except for the companies of the Uzbek light sector industry, the use of manager contracts is even highest among the smallest companies.¹⁸

With regard to owner groups, the picture concerning the use of manager contracts is not very coherent. There is no sign that any ownership group in Kazakhstan preferably introduced manager contracts, no matter how big the overall stake of this group.¹⁹ In Uzbekistan, the usage of manager contracts increases with a foreign ownership share. The reason behind it could be a single strategic investor with incentives to control the company's management. However, the higher usage by domestic private persons re-

¹⁶ This implies that the need for external finance proportionately increases with the number of employees, thereby assuming a fixed capital-labour input ratio and a similar relative need for external finance sources among the enterprises.

¹⁷ We thereby assume that the use of manager contracts is influenced by the initial company size and ownership structure resulting from the privatisation (or in some Kazakh cases even before privatisation). As already described, both the sizes of the companies as well as the ownership structure vary a lot between the different years. However, the relative use of manager contracts does not vary over time among the Kazakh and Uzbek companies of the food-processing industry and only slightly decreases for the Uzbek companies in the light industry (from 87.1% (see Table 5) to 84.9% in 2000 and 85.7% in 2003). The more, the number of observations in some of the categories is very small (compare with the findings of previous sections). As such, a change of a company into a category with few observations may lead to a high change in the share of companies with manager contracts. As a consequence, the findings are not very robust and have to be dealt with cautiously. However, the overall picture about the use of manager contracts according to these variables does not change very dramatically with regard to underlying year.

¹⁸ The usage of manager contracts among companies with less than 50 employees is 100% in the year of privatisation for the Kazakh and Uzbek companies of the food-processing industry. However, the values are lower for 2000 and 2003 as the average company became smaller. While the relative use of contracts remains highest among the smallest companies in Uzbekistan, it even became smallest in Kazakhstan though the figures became very equal among the different company sizes. There is no real evidence that the use of manager contracts increases with the size of the firms.

¹⁹ Outstanding usage (100%) of manager contracts is shown among the companies with a 25-50% stake of some ownership groups. However, the total coverage is just reflected by two or three companies in these cases.

ported in Table 5 does not turn out to be stable over time. The usage of contracts increases with the state share in Kazakhstan and for the Uzbek companies of the light industry. However, the results are based on very few observations. The finding may nevertheless hint that the state uses manager contracts rather complementary to the size of its ownership stake in the company. As a bigger investor, the state also has a higher incentive to influence the management of the company. As higher Kazakh state shares in 1997 coincide with a later privatisation, it may rather mean that the usage increased in more recent privatisation processes which led to higher outside ownership (compare with last section).

Table 5: Shares of Companies with Manager Contracts according to Company Size and Ownership Groups in the Year of Privatisation or 1997 (in %)

	Whole Sample				Kazakhstan Food				Uzbekistan Food				Uzbekistan Light			
	All	<50	50-200	>200	All	<50	50-200	>200	All	<50	50-200	>200	All	<50	50-200	>200
<i>Company size (employees)</i>	81	100	63.1	85.2	83.3	100	70	90	76.9	100	57.1	82.4	82.8		50	85.2
<i>Ownership Group Categories</i>	All	0-25%	25-50%	>50%	All	0-25%	25-50%	>50%	All	0-25%	25-50%	>50%	All	0-25%	25-50%	>50%
State Share	80.4	80.4	83.3	79.4	87.1	82.6	100	100	68.6	77.8	0	70.8	87.1	79	100	100
Private Persons' Share	80.4	81.3	76	87.1	87.1	85.7	100	85.7	68.6	50	69	100	87.1	100	83.3	87.5
Insiders' Share	80.4	73.3	82.2	86.4	87.1	87.5	100	85	68.6	54.6	73.9	100	87.1	81.8	89.5	100
Insiders' 1 Share	80.4	80	85.7	66.7	87.1	92.9	85.7	66.7	68.6	68.6			87.1	87.1		
Insiders' 2 Share	80.4	73	85.1	84.6	87.1	81.8	100	84.6	68.6	60	75		87.1	81.8	90	
Legal Persons' Share	80.4	81.2	77.8	66.7	87.1	88.5	100	66.7	68.6	70.6	0		87.1	88	83.3	
Foreigners' Share	80.4	80.9	75		87.1	87.1			68.6	67.7	100		87.1	91.7	71.4	

The table reports the share of companies with manager contracts. The values are recorded for the whole sample, Kazakhstan food and Uzbekistan food and light as well as, among them, according to categories based on company size (all, <50, 50-200, >200 employees) and according to ownership group categories listed in the first column and according to their ownership shares (0-25%, 25-50%, >50%).

Another question concerned the monitoring of the compliance with the manager contracts. The list of possible monitoring agents specified in the questionnaire differed among the two countries according to consultations with the partner institutes. Most of the Kazakh companies (12) chose the manager himself to monitor his own compliance, followed by the board of managers (5), the general assembly (4), the council of directors (3) and others (3).²⁰ In Uzbekistan, the main response was the supervisory board (34),

²⁰ The figures in brackets refer to the absolute amount of observations among the companies which specified to have a manager contract. Some companies selectively answered questions of this section without

followed by the biggest shareholder (22) and a group of shareholders (1). According to our results, company supervision turns out to be better suited in Uzbekistan than in Kazakhstan.

Against this background, the results from the questions hinting at the incentive components of the manager contracts are very disappointing. As already noted, the interests of owners and managers can only be aligned if incentives are strong enough, i.e. if the remuneration of the managers is dependent on good performance. While most of the companies (91.5%) still specified that the remuneration of managers was part of the manager contracts, only 68.3% included a bonus scheme and even only 26.3% provided sanctions in case of bad performance.

Additionally, respondents were asked to specify the managers' remuneration along certain types: fixed wage²¹, fixed wage plus share in profits (or other premium dependent on corporate results), fixed wage plus equity stake, share in profits, equity stake, profits minus rent (fixed-rent contracts, manager pays a rent and receives the profits), or other form. These types provide a wide range of answering possibilities and refer to insights from studies of China as well as to insights from development economics about the incentive effect of land rental contracts which is easily applicable for the manager contracts. According to these insights, incentives increase with the dependence of managers' pay on the performance of their companies.²² As such, incentives are almost absent if the managers are paid a fixed wage.

Figure 6 reveals that 66% of the companies (66 out of 100) remunerate their managers according to fixed wages, and even 71.4% or 25 of the Uzbek companies in the light industry do so.²³ Only 32% of the companies reported about using some kind of share-

confirmation of the existence of a manager contract. In order to refrain from purely selective answering, these companies were left out of this analysis.

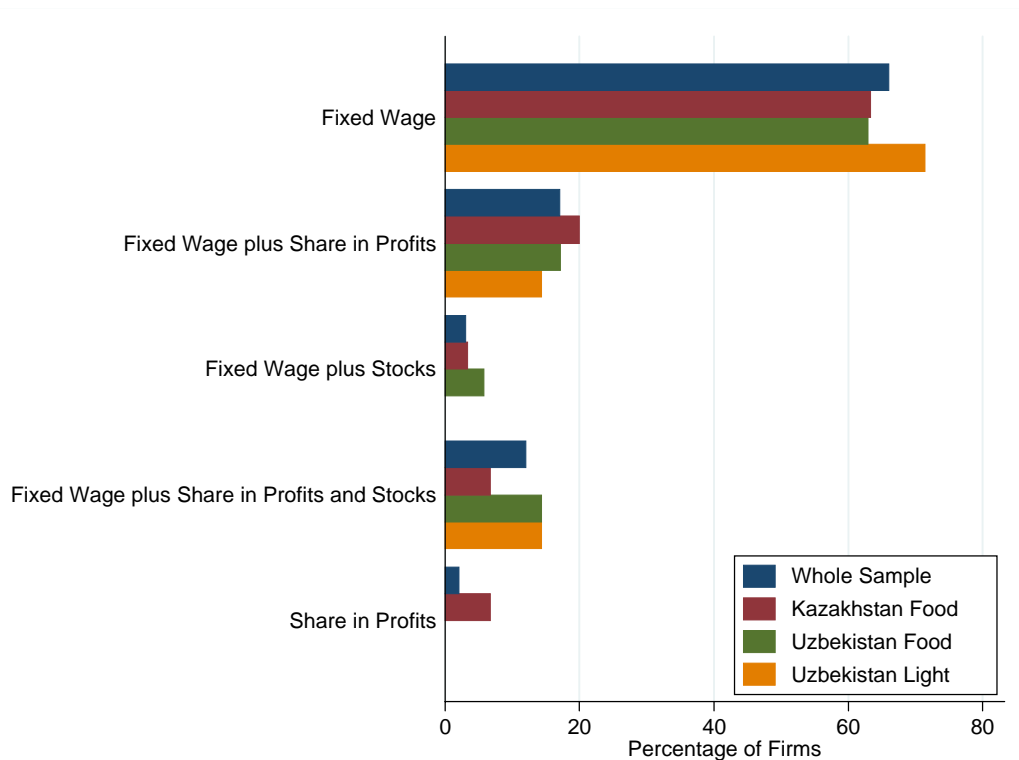
²¹ This category includes fixed wages plus premiums which are not dependent on corporate performance. This category was specifically addressed to filter out contracts with non-performance related premiums, e.g. depending on age or locality, as these constitute a very common form of bonus which does not pose any form of incentive to improve the performance of the company.

²² According to these insights from principle-agent-theory, fixed-wage contracts only provide the right incentives if the effort of the manager (the agent) is totally observable by the owner (the principle) and the contract conditional on the observed effort which can be ruled out in the context of manager contracts. With asymmetric information about the effort of the managers, the right incentives are set by a fixed-rent contract. In this case the manager receives the profits from his efforts and pays a fixed rent to the owner. A less than total share of profits generates Marshallian inefficiency as the managers faces less than optimal incentive to engage in efforts to increase the performance of the company. On the other hand, another source of inefficiency sets in if the manager is more risk averse than the owner. The balancing of these two inefficiencies leads to an efficient second-best option, a share-profit (sharecropping in terms land rental contracts) contract. For more detailed information about land rental contracts and their efficiency, see e.g. Ray (1998).

²³ The results refer to 100 enterprises responding on this question though only 79 of them also reported about the existence of manager contracts. Just referring to the 79 companies with contracts, 53 specify wage contracts as their form of managers' remuneration which even constitutes 67.1%. This already indicates that the results are very similar for these two subsamples indicating that the pattern of managers' remuneration does not differ among companies which reported about the use of manager contracts and those which did not.

profit contract, most of them in kind of a fixed wage plus a share in profits. Very few enterprises rely on stocks or equity as a sole incentive factor, but the combination of a share in profits and stocks is used in twelve companies, more frequently in Uzbekistan (five of them each in the Uzbek food and light industry). Additionally, two Kazakh companies even specified their managers' remuneration to consist solely of a share in profits. This constitutes the form of contract (or the way of management remuneration) most in line with generating the right incentives for managers.

Figure 6: **Manager Contracts – Percentage of Firms according to Managers' Remuneration**



Interestingly, this sort of incentive contracts is exclusively used by two Kazakh companies which were totally privatised in 1992 and 1994, i.e. relatively early in Kazakh terms, and whose shares were taken up by insiders (especially insider group 2, the employees) and judicial persons. In Kazakhstan, the usage of incentive components increases with a decreasing share of state ownership and an increasing share of private persons (see Table 6). For these Kazakh companies, these owners constitute insiders with a relatively more important impact of insider group 2, the employees. This relationship does not change for the years 2000 and 2003 as the table only presents data for the

year of privatisation.²⁴ On the other hand, a relationship between the contracts' usage of incentive components and ownership shares is not confirmed for the Uzbek companies of the food industry for the year of privatisation. That changes for the years 2000 and 2003. Though for these companies, an increasing ownership share of judicial persons seems to be the driving force behind the incorporation of management incentives.

Table 6: Number of Firms according to the Type of Management Remuneration and along Ownership Share Categories of the State and Private Persons

<i>State Share Category in Year of Privatisation</i>	Whole Sample			Kazakhstan Food			Uzbekistan Food			Uzbekistan Light		
	<25%	25-50%	>50%	<25%	25-50%	>50%	<25%	25-50%	>50%	<25%	25-50%	>50%
Fixed Wage	26	10	25	11	2	6	4	1	15	11	7	4
Fixed Wage plus Share in Profits	13		3	6			3		3	4		
Fixed Wage plus Stocks	1		2	1					2			
Fixed Wage plus Share in Profits and Stocks	5	1	4	2				1	4	3		
Share in Profits	2			2								
<i>Private Persons' Share Category in Year of Privatisation</i>	<25%	25-50%	>50%	<25%	25-50%	>50%	<25%	25-50%	>50%	<25%	25-50%	>50%
Fixed Wage	14	31	16	7	2	10	2	17	1	5	12	5
Fixed Wage plus Share in Profits		8	8			6		5	1		3	1
Fixed Wage plus Stocks	1	1	1			1	1	1				
Fixed Wage plus Share in Profits and Stocks		7	3			2		5			2	1
Share in Profits		1	1		1	1						

With regard to other incentive components in managers' remuneration characteristics, only 17 or 16.8% of all companies and 13 or 15.9% of those with manager contracts specified to incorporate sanctions for the management in case of bad performance which is an important ingredient in the Chinese manager contracts (see e.g. Groves et al. (1995) and Li (1997)).

All in all, the survey data only offer very weak evidence that manager contracts provide some kind of incentive component for the managers to improve the productivity and effectiveness of their enterprises. Most manager contracts did not feature a single incentive component. They rather turn out to constitute simple labour contracts specifying a fixed wage for the managers. This is supported by the fact that the specified type of management remuneration did not differ among companies that reported about the existence of a manager contract and those that denied it.

²⁴ The findings still hold among the restricted subsample of companies specifying the use of manager contracts, as the values in the text and Table 6 refer to all companies reporting on this answer, even if the company neglected the use of a manager contract.

4 Control of and Problems for the Companies

The transition from a planned to a market economy constitutes a rapidly changing political and economic environment for the companies. A massive reduction in the inherently immense and mutual interactions among the state or its agencies and its firms transforms the problems and obstacles faced by the companies in doing their businesses. The privatisation process was supposed to support the reduction of state-companies' interactions via the direct transmittance of ownership into private hands. But the state still retained shares in some of its companies, and on a larger scale and to a greater extent in Uzbekistan than in Kazakhstan. In case of incomplete ownership transmission, the usage of incentive-increasing manager contracts could have been a substitute for reducing the direct influence of the state. But the use of contracts in Uzbekistan (as well as in Kazakhstan) does not seem to fulfil this purpose. The close ties between the state and its companies that have been built for a long time and became manifold and intrinsic to the system will not dissolve in a few years.

A whole chapter of the questionnaire is each devoted to insights about who came to control the companies after privatisation and which problems and obstacles they face in their rapidly changing environment. With regard to the time horizon, the questions only addressed the situation in 2000 and 2003 as perceptions about the past tend to get biased over time.

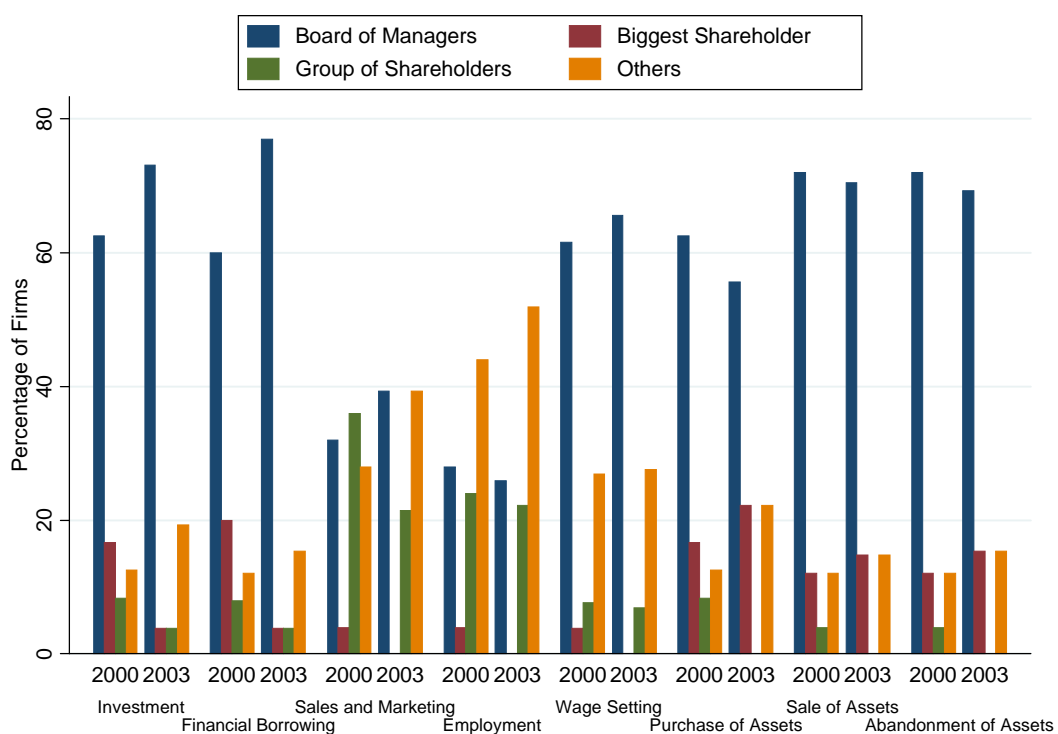
4.1 Company Control

One question asked the respondents to specify the (group of) persons who control the company along certain specified areas of corporate decision making: investment, financial borrowing, sales and marketing, employment, wage setting, and purchase, sale and abandonment of corporate assets. This reflects a wide range of corporate control in order to identify the differing importance of certain agents for the company. The specification of these agents differed between Kazakhstan and Uzbekistan as certain groups which are very relevant in corporate matters in one country would have confused the respondents of the other country, and vice versa. Managers and shareholders, the most important agents with regard to corporate decision making, were listed in both countries. Additionally, the respondents were free to add other types of controlling bodies.

The results are recorded in Figures 7, 8 and 9, for the company groups Kazakhstan Food, Uzbekistan Food and Uzbekistan Light respectively and separately. The figures present the percentage of firms which specified one of the possible corporate agents to control a certain area of decision making, both in the year 2000 and at the time of completing the questionnaire (specified as 2003). In both countries, the board of managers or directors turns out to be the most important agent in corporate decision making, and this predomi-

nance increased over time.²⁵ The managers thereby predominantly control the areas of investment and finance. While only 6 of 26 companies in 2000 and of 31 in 2003 report every decision-making area to be controlled by the board of managers, 11 and 12 in the respective years do so with regard to investment and finance, comprising investment, financial borrowing and purchase, sale and abandonment of corporate assets. The other areas are more than proportionately influenced by shareholders as well. In comparison to the investment and finance categories this control was exerted by a group of shareholders and not only the biggest one.

Figure 7: **Company Control in Kazakhstan – Food Industry**

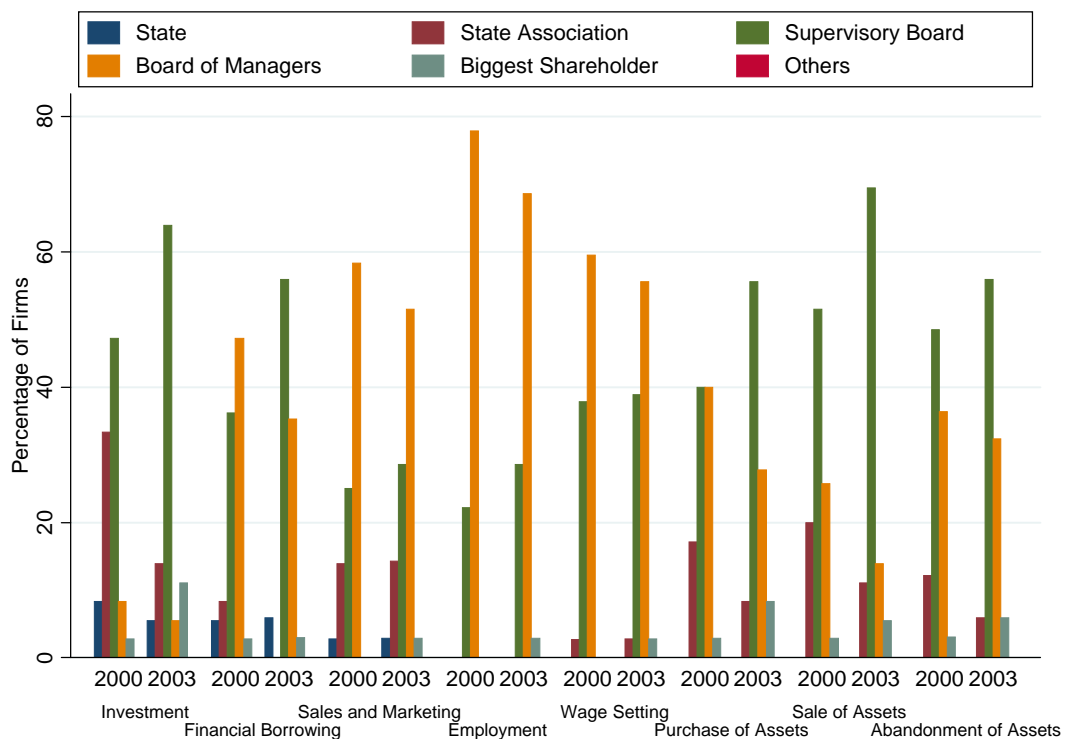


In Uzbekistan, the boards of managers and supervisory boards more than proportionately control the areas of financial borrowing, sales and marketing, employment and wage setting. 25 (11 active in the food and 14 in the light industry) of 70 companies report that these areas are mainly controlled by these corporate agents. On the other hand, other controlling groups are important as well, and some of them are external to the companies. The supervisory board constitutes an important controlling agent in some companies' decisions on investment and the administration of assets. According to

²⁵ In Kazakhstan, this even includes most of the companies in the free category "Others" as this mostly constitutes a single manager or director (in contrast to the specification in the questionnaire of the board of managers or directors as a pre-specified controlling agency).

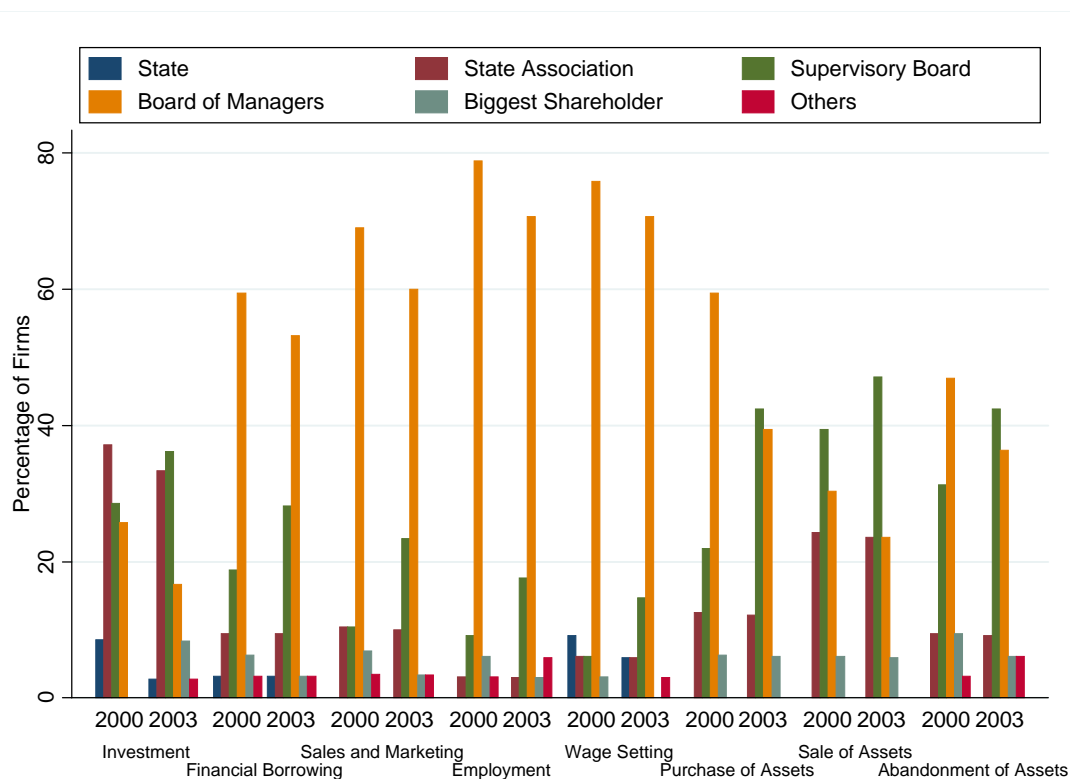
the survey results, the state plays only a minor role in company control, especially in Kazakhstan and in terms of direct state interference in Uzbekistan. But in fact, the appropriate state associations (former industrial ministries) still exert the main control over certain areas of company's decision making in Uzbekistan, especially with regard to investment and the administration of assets. These associations reduced their company control among the companies between 2000 and 2003, relatively more so according to the perception among the firms of the food industry.

Figure 8: **Company Control in Uzbekistan – Food Industry**



Company control now highly rests in the hands of corporate bodies, at least if the statements and perceptions conform to reality. This independence of the companies to determine their own fate increased in more recent years. Though the influence of the state turned out to be minor so far, this topic deserves some further investigation.

Figure 9: **Company Control in Uzbekistan – Light Industry**



4.2 State Interference in Company Control

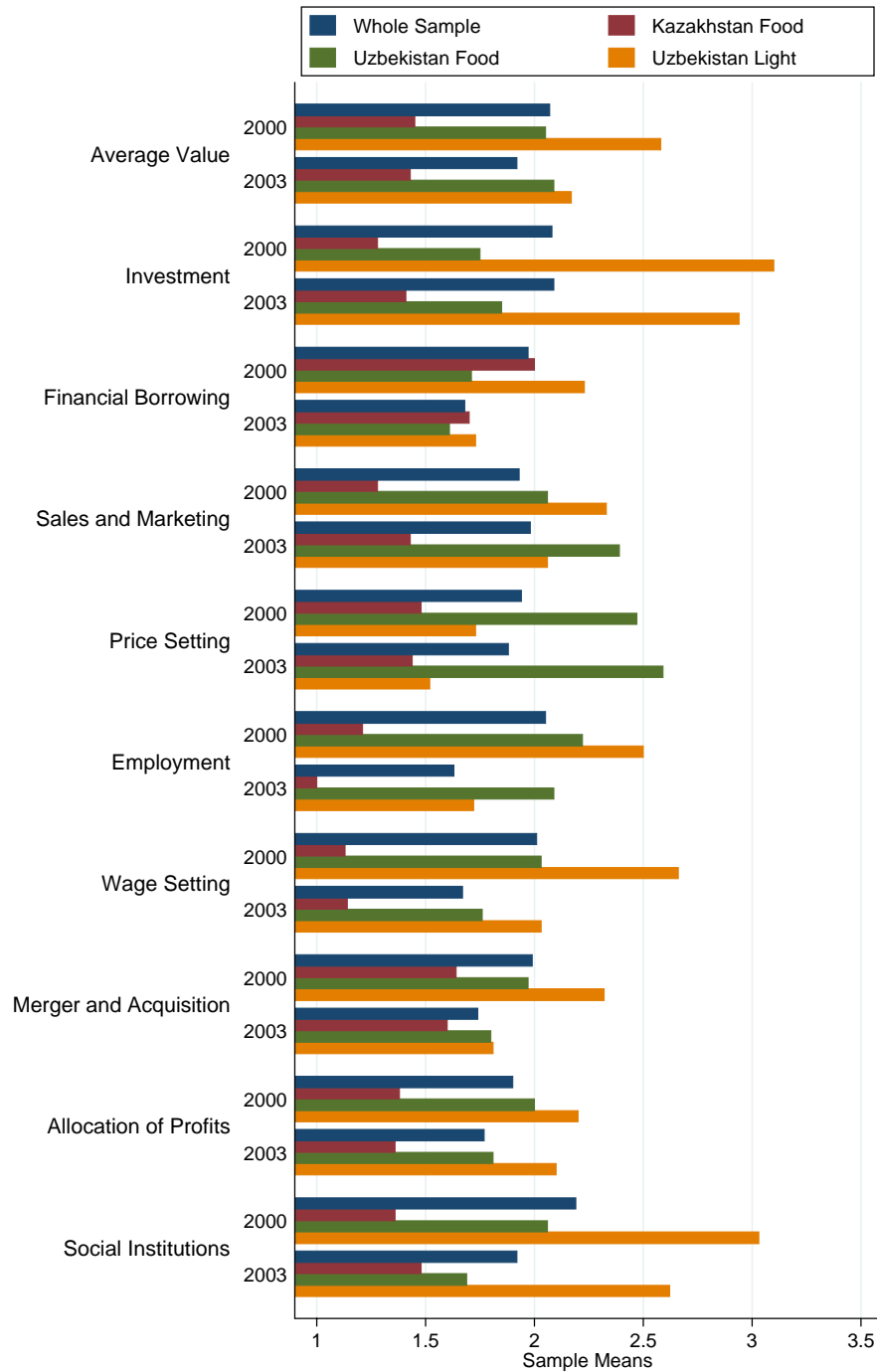
The extent of state control or interference in a wide range of the decision making process in a company was separately addressed in another question. During the socialist past, firms were publicly owned and de facto controlled by the state and its agencies. The extent of state control should therefore decrease with the deepening privatisation process. Additionally, politicians and state agencies will adapt to their diminishing roles in company affairs as time passes by.

The question was subdivided into nine categories or areas of firms' decision making: investment, financial borrowing, sales and marketing, price setting, employment, wage setting, merger and acquisition, the allocation of profits, and social institutions. In order to capture the recent development of state control, the companies were asked to report their perceived state control for 2000 and 2003/2004 according to six ordinal categories.²⁶ The ordinal vari-

²⁶ The analysis is based on the recent development of state interference as assessments of the past get biased over time. While the perception about the development over the last three to four years with the year 2000 as a useful benchmark should not constitute a big problem, the assessment of the situation in the year of privatisation seemed too long ago in order to receive unbiased answers.

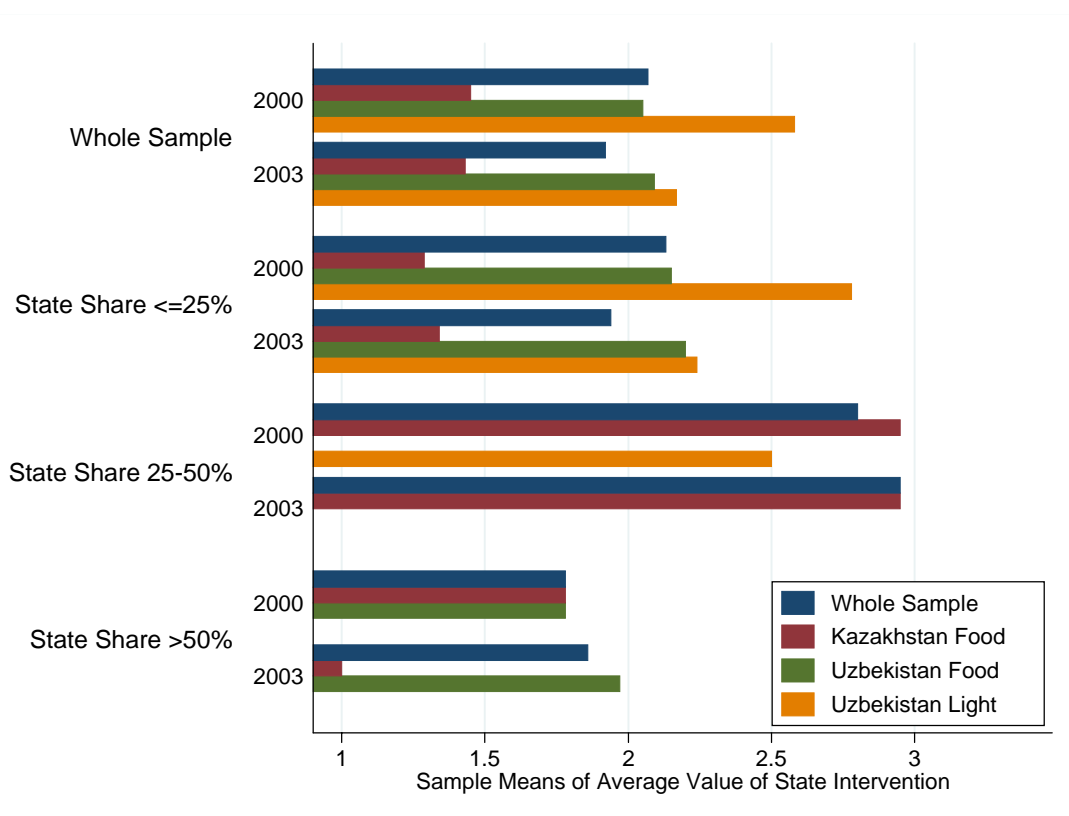
ables range between 1 denoting no state control (the state “never” interferes) and 6 denoting total state control (the state “always” interferes). Variables were constructed to capture average values of state interference in the different decision-making dimensions for the years 2000 and 2003/2004 respectively, giving equal weight to the different dimensions.

Figure 10: **State Interference in Company Control**



As can be seen in Figure 10, the average state control variable expectedly falls from 2.07 to 1.92 over the period, with 2 being defined as modest control or “infrequent” state interference. This is highly driven by a lower perceived interference among the companies of the Uzbek light industry sector which mostly recorded the most state control except for price setting at both points in time and sales and marketing in 2003 as well as decreases in every dimension of decision making. On the other hand, their counterparts of the food industry even reported a slight increase in overall state control which they felt for decisions about investments, sales and marketing as well as price setting. Even the Kazakh enterprises which are subject to the lowest state control on average in accordance with the deeper privatisation process reported an increasing state control in certain dimensions of decision making (investment, sales and distribution, social institutions) in recent years. The recent increase in state control in some areas seems to contradict the expectation that politicians and state agencies increase their respect for the autonomy of the enterprises over time indicating that old habits might still prevail in certain areas.

Figure 11: **State Interference according to State Share**



Declining state interference in accordance with declining state shares in the companies is not smoothly confirmed by Figure 11 recording the degree of perceived state intervention along the three categories of state shares. The highest interference on average turns out to be felt by the companies with a medium-sized state share of between 25% and 50%

of equity. Companies with higher state shares of more than 50% record the lowest values. It should be noted that the number of companies in these two categories became very small (13 of 91 in 2000 and 11 of 92 in 2003). As such, this may only be seen as a hint at an inverted-U-shaped relationship between the property share of the state in its companies and its intervention in the companies' affairs.²⁷ This is not in line with the expectation of a proportionately increasing relationship. The explanation may be that the perception of state intervention decreases with the state share as state involvement gets more and more legitimate. On the other hand, it can also be that the state share acts as a form of substitute to direct interference, e.g. via closer connections between state representatives and managers. Nevertheless, the data provide weak evidence that privatisation reduced the manifold interactions among the state and its companies in the form of reduced state intervention. But the evidence is based on a cross-sectional comparison among the companies according to their differing ownership structure instead of a clear reduction in state interference over time. The observed level of state intervention in these countries still poses a problem for the companies in that it impedes their properly market-based development.

4.3 Problems for the Companies

This section aims to identify the key problems or obstacles faced by the companies. A proper business environment is essential for the development of the corporate sector. This encompasses a wide range of reasoning. It starts with the importance of clearly defined and enforced property rights as well as other laws, rules and regulations that have an impact on corporate behaviour. Equally important are the interactions with other private or public firms, e.g. with regard to competition and financing. And last but not least, certainty and predictability play a major role in this context as these determine the time horizon for the companies' decisions and actions. As most of this institutional environment for the companies is shaped by the state and its agencies, this includes the comprehensive forms of interactions among the state and the firms.

²⁷ This inverted-U-shaped relationship between the state property share and state interference turns out to be rather robust among the whole sample. A simple linear relationship between these two variables turns out to be positive and significant at least at the 10% level, both separately for 2000 and 2003 and using simple and robust OLS estimation techniques. This means that a higher state share increases state intervention as perceived by the companies. The property share held by insiders seems to be even more important in reducing state intervention than the state share is in increasing it. The latter variable loses its significance by controlling for the first variable. On the other hand, the estimation models including the state property share variable and its squared values show very significant impacts on the degree of state intervention. The linear variable has a positive, the quadratic term a negative coefficient confirming the inverted-U-relationship. And this is robust to the inclusion of many control variables including the property shares held by other groups. Besides the state and insider shares, other variables seem to matter as well. The time span since privatisation measured as the years since privatisation until 2003 (the year of the latest recorded privatisation) has a negative impact on and thus reduces state intervention even in combination with the linear impact of the state share. This is in line with the expectation that the state totally controlled its companies during the socialist past and cannot be expected to reduce its controlling function overnight.

The more, the last 15 years included dramatic changes of the institutional environment for the companies in Kazakhstan and Uzbekistan. Nevertheless, and the role of the state should have turned from an all-determinative into a guiding entity. In this respect, the political and resulting institutional vacuum is widely viewed as a main factor behind the failure of the privatisation process in the CIS countries (for Russia, see Black, Kraakman, Tarassova, 2000). As such, this chapter also documents how the Kazakh and Uzbek companies assess part of the missing institutional framework and its resulting economic anomalies like outright official corruption in terms of problems or obstacles to pursue their business operations.

The questionnaire included a wide range of questions about the problems and obstacles for the firms. While this section refers to a general question, the following subsections provide a more detailed analysis along the following problems for the companies: unreliability and inconsistency of the judicial system, impeding bureaucratic red tape and taxes, problems with of finance, and competition, unpredictability and uncertainty about changes in laws and regulations.

A general question asked for the respondents' perception of the cumbersomeness along a wide range of spheres encompassing political as well as economic factors that have been identified as potential problems for companies. These embrace unjustified state interference, the tax burden, regulations, bureaucracy, corruption, the unreliability of the judicial system and the police, crime and theft, organised crime, problems with inflation (macroeconomic instability), problems with finance, infrastructure deficits (e.g. electricity, roads), interference of state associations (only Uzbekistan) and political instability (only Kazakhstan). A summary score was obtained for each company by calculating the unweighted average across all dimensions except the country-specific ones. As not all companies have reported answers on every dimension, this average contains data for the companies with at least three observations for one point in time. For comparative reasons, another average was calculated which only contains a value if answers along all categories were reported for a single year.

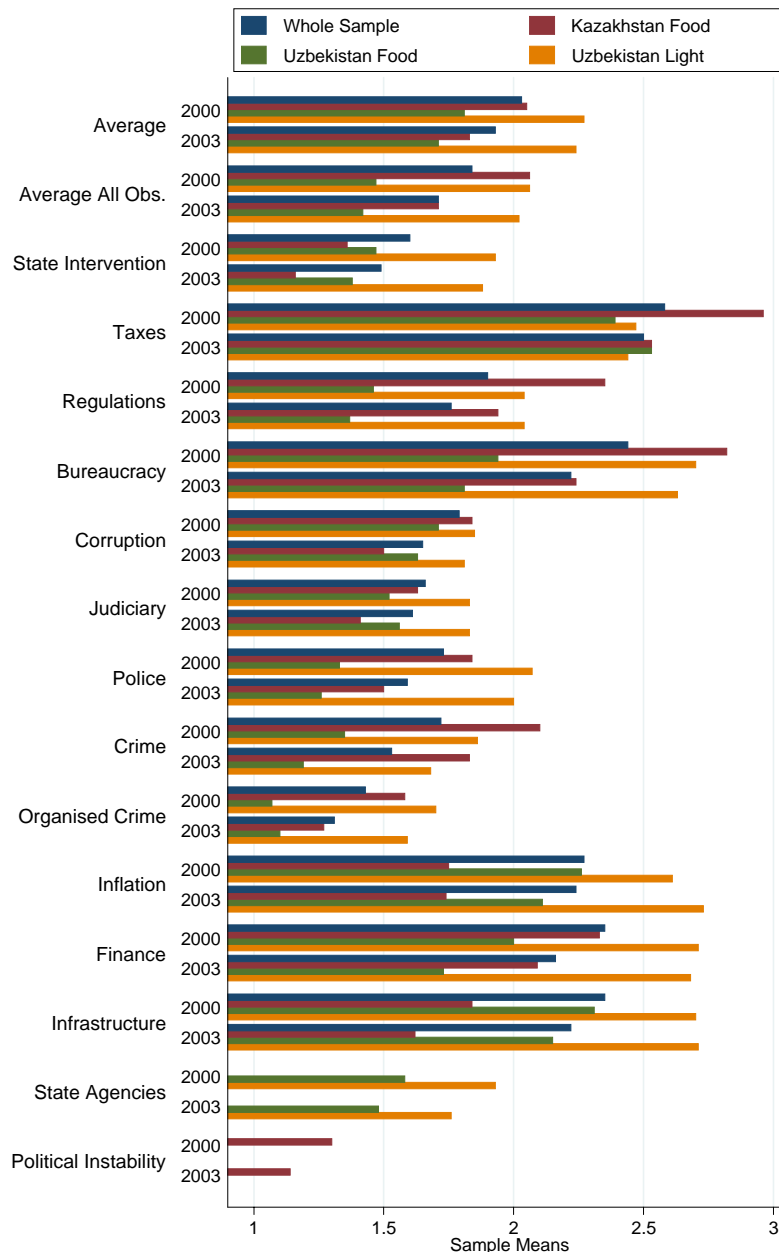
Figure 12 reports the means for the two different averages both for the years 2000 and 2003 as well as the means for the separate sub-areas. These means are recorded for the whole sample as well as for the subsamples, the companies of the Kazakh and Uzbek food-processing industry and the Uzbek light industry. As in the case of other surveys, e.g. the Business Environment and Enterprise Performance Survey (BEEPS), the respondents were able to rate their perceptions along four different categories denoted as 1 to 4 while a lower value refers to a minor problem or obstacle.

As can be seen in Figure 12, the first average value declines from a mean of 2.03 in the year 2000 to 1.93 in 2003 which means a slight improvement of the institutional environment or investment climate in recent years.²⁸ The improvement was felt the most

²⁸ This may, however, be influenced by the differing number of companies reporting on this question among the two years. While the average for 2000 rests on 88 companies, 95 responded for the more current date of 2003. However, among the 87 companies that answered for both points in time, the average decline was 0.101 and thus only slightly smaller than the value of 0.104 (or 0.1) referred to in the text. The difference evolves as disproportionately more Kazakh companies are affected (their responding in-

among the Kazakh companies whose average sinks beneath the overall mean while the Uzbek companies of the light industry not only recorded the highest dissatisfaction but also the smallest decrease, even in absolute terms.

Figure12: **Problems for the Companies - Basic Result**



creased from 24 to 27 between 2000 and 2003) which also recorded a disproportionately higher improvement of the institutional environment among the 23 companies with both observations and the other four companies felt even more comfortable.

The second average, which is based on fewer observations due to the restriction of complete data availability in the subcategories, also shows an improvement in the institutional environment between 2000 and 2003. The average mean falls from 1.84 to 1.71, i.e. the companies reporting more freely are more satisfied with the institutional environment they work in. The question of which average better reflects the overall situation and development of problems depends on the assumption why some companies chose to answer selectively. On the one hand, it may be that these companies just chose to report on their most significant obstacles. In this case, the first average would unjustifiably worsen the overall impression about the extent of the problems. On the other hand however, most of the selected answers are concentrated on the upper categories and on less delicate ones like taxes indicating a different selection bias. And as most of the companies chose to answer the different categories rather equally, the incorporation of the observations would rather be justified. The second average changes the overall picture among the three subsamples in the way that the Kazakh companies' complaints about the institutional environment resemble the ones for the Uzbek light industry in 2000 but improve much more until 2003.

Comparing the results among the Kazakh and Uzbek companies of the food industry, Kazakhstan scores worse than Uzbekistan. This is in line with the findings based on survey data like the BEEPS in these countries (see EBRD, 1999 and 2005)²⁹. The Transition Report 1999 explains this perception gap by a different relevance towards market economy institutions and thus resulting obstacles from their improper functioning which are perceived as less relevant in countries with little transition progress. According to our data however, this gap narrows sharply between 2000 and 2003 as the Kazakh companies' perception improved in recent years. The same result occurs for the overall average including the companies with selective choices.

This provides a hint that the perception gap may also be driven by the companies' cautiousness to report freely about the cumbersomeness of certain institutional conditions. As noted by the Transition Report 2005, the unwillingness to speak openly to interviewers may be higher in oppressive political environments like in Uzbekistan. Another explanation concerns the positive role of the state for some or all of the companies in its territory. In countries with a small private sector and less competition, companies may perceive it advantageous to act in a business environment in which the state intervenes on their behalf. This factor may help to explain the difference among the two surveyed industrial sectors in Uzbekistan. The companies of the light industry with their lower state shares may benefit less from the state's helpfulness in its corporate affairs. Indeed, support of the state agencies is rated more positively by the Uzbek companies, and among them much more so in case of the food industry (see Section 4.3.2). The more a company rates either the central or local government as supportive, the lower the complaints about the problems. This relationship furthermore holds among the whole

²⁹ It should be noted that the categories asked for differ among the BEEPS and our survey as our choice was more adapted to local problems. As such, we specifically asked for inflation instead of the macro-economy as a whole. And instead of policy stability and law and order we more specifically referred to corruption, the police, crime and organised crime – problems that are highly visible for outside visitors. The more, we included the problem of unjustified state intervention and problems with bureaucracy.

sample as well as for the Uzbek companies separately.³⁰ In this context, the ownership stake held by the state may have an impact on the extent of the problems as well. A higher state share reduces the company's willingness to complain. Or it may alter the perception of the scale of the problem in a positive way, as in the case of lower complaints about state interference in company control. However, this relationship between the state share and the perception of problems is not confirmed by the data. And the connection between the state share and its support in corporate affairs as an indirect link from ownership to problems is very weak.

With regard to the results from the perceived problems faced by the companies, much of the variation across the countries and, in the Uzbek case, industries stems from certain problem dimensions (see Figure 12). The biggest obstacles for doing business turn out to be the tax burden and the bureaucracy.³¹ This especially holds for the Kazakh companies in 2000 and also shows up for problems with regulations (albeit at a lower scale), but the problem of bureaucracy is much less pronounced among their Uzbek counterparts in the food industry. Especially in the case of the tax burden, this category may serve as an easy and even selective target of complaints. The same may apply to the other outstanding obstacles, inflation, financing and infrastructure, which score especially bad among the biggest complaining group, the Uzbek companies of the light industry sector, and show no improvement.³² In contrast, complaints about problems with unjustified state intervention, corruption, the judiciary and the police (as well as crime and its organised form) are lowest among the problem areas for the whole sample and the three subgroups. These constitute the dimensions where certain people or groups could be most offended which might reduce the respondents' willingness to answer openly. These sorts of problems may have even become institutionalised and thus do not prevail or are not perceived as problems as companies got used to them. There are, however, a few exceptions scoring a middle-scaled problem average, like crime in Kazakhstan and problems with the police for the Uzbek light industry companies.

The next five subsections more profoundly examine certain dimensions of obstacles. The investigation starts with a problem dimension which on average occurred to be a minor obstacle so far, the judiciary.

³⁰ According to OLS regressions for the year 2003 (or better at the time of the questioning in 2004), this relationship is highly significant at the 99% level for either the support from the central or the local government, both among the whole sample as well as for the Uzbek companies and even among the industrial groups (among the Uzbek companies of the food industry just significant at the 95% level. With regard to the aid from state agencies, in Uzbekistan, the relationship is significant at the 95% level among the Uzbek companies but loses its significance after the introduction of an industry dummy. Nonetheless, there is stark evidence that the perception about the supportiveness of state agents affects the companies' views about the extent of their problems.

³¹ Taxation is found to be the major obstacle among all transition countries as reported by the Transition Report 2005 (EBRD, 2005). In contrast to our results however, this problem area (together with problems resulting from an inappropriate provision of infrastructure) is also identified as showing the most progress between 1999 and 2005.

³² On the other hand, the averages for the companies of the light industry are above the overall averages in every dimension except for the tax burden. And furthermore, problems with finance and infrastructure may be due to their bigger company sizes and other industry-specific factors.

4.3.1 Problems with the Judiciary

The judiciary plays a crucial role for the economy in securing property rights and guarding economic transactions. In order to secure a proper functioning of a market economy, rules and laws have to be set in a clear and consistent manner and have to be enforced by a fair and predictable judiciary.³³ A well designed regulatory business environment gets undermined if the enforcement of rules and laws is dependent on peoples' personal connections or their ability to bribe enforcing agencies.

The questions of this section address the problems of a difficult acquisition of information on the relevant laws and regulations for a firm and of the inconsistency and unpredictability of laws. The more, the section investigates the reliability of the judicial system with regard to the proper enforcement of both contracts and property rights. Another question addresses the reliability of the judiciary per se for the years 2000 and 2003 with regard to different aspects of the improper behaviour of courts and judges: unfairness, dishonesty and corruption, slowness, expensiveness or non-affordability, and ineffectiveness.

The results are shown in Figure 13 recording the percentage of firms which ticked answering possibilities (3) or (4), the two worst categories out of four.³⁴ With regard to the results on the first four and more common questions, the overall perception of the judiciary does not seem too bad. Only between 22% and 32% of the responding firms opted for the two negative answering possibilities and, among them, between 14% and 26% chose category (3). While most of the Kazakh companies turn to inconsistency and unpredictability of laws as their biggest problem with the judiciary, the Uzbek companies more complain about the improper enforcement of property rights. This might have been a result of the arbitrary increases in the companies state shares as noted in Chapter 3.4.³⁵

³³ The Transition Report 2005 examines the extensiveness and effectiveness of corporate governance laws in transition countries. Interestingly and contrary to expectation, good legislation in terms of internationally recognised principles (the extensiveness of laws is based on a comparison to a benchmark issued by the OECD) does not necessarily coincide with a high degree of enforceability concerning the legal framework for redress of minority shareholders. Effectiveness in this case turns out to be a problem among all the CIS countries, particularly in the two CARs investigated in this paper as well as the Ukraine. On the other hand, the extensiveness of corporate governance legislation is rated as highly compliant for Kazakhstan and medium compliant for Uzbekistan (see EBRD, 2005).

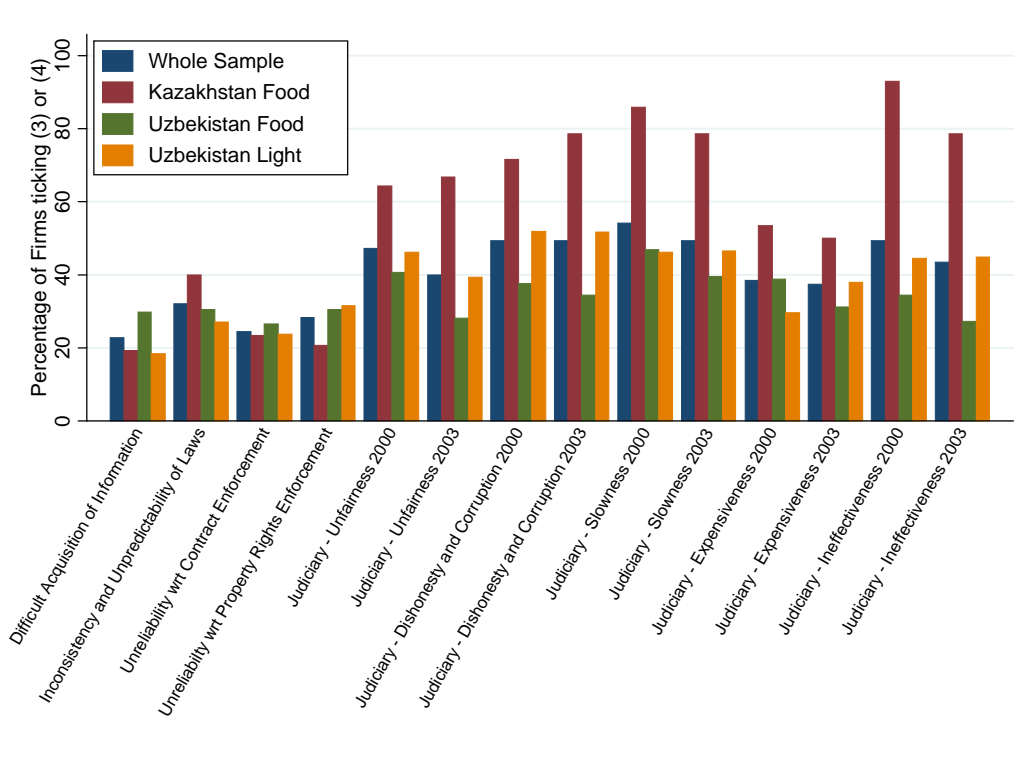
³⁴ Most of the questions in this and the coming subsections about the problems for the companies specify four answering possibilities. In order to prevent a negative bias, the questions do not forestall a problematic aspect and the answering possibilities were evenly split among positive and negative possibilities. In that sense, answering possibility (1) denotes "positive", (2) "rather positive", (3) "rather negative" and (4) "negative" with positive and negative in accordance with the underlying aspect of the question, e.g. simple and difficult or consistent and inconsistent. With regard to the question about the reliability of the judiciary, the answering possibilities refer to the frequency of good behaviour with (1) always, (2) frequently, (3) infrequently and (4) never e.g. fair or honest behaviour of courts and judges.

³⁵ However, the responses among the affected Uzbek companies are very mixed. While two of these companies in the light sector rated the judiciary as "unreliable" towards the enforcement of property rights and five of both sectors as "rather unreliable", one opted for "rather reliable" and the other six even for the best category. This implies that the relationship between a loss of private company share and the enforce-

The negative responses recorded in Figure 13 are concentrated among the more specific questions about the behaviour of courts and judges, especially among the Kazakh companies. The average percentage of firms being discontent with the judiciary varies between 37% and 54%. The results differ a lot among the countries and sectors and over time. Kazakh enterprises stand out in their negative evaluation of their judiciary. Ineffectiveness scores highest, followed by slowness, although the discontent diminished between 2000 and 2003. The opposite holds with regard to unfairness, dishonesty and corruption. In all these categories, dissatisfaction increased in recent years. Even for the best judicial area, affordability, discontent still hovers around 50%.

The Uzbek counterparts of the food-processing industry once again constitute the most satisfied group (except for slowness and expensiveness in 2000). Their dissatisfaction is decreasing in every regard. They see the biggest problem in the slowness of the judicial system. The companies of the light sector view dishonesty and corruption as the bigger obstacle and complain highly about the judiciary's ineffectiveness. Although their dissatisfaction is smaller than for the Kazakh companies, their problems are more profound. The Uzbek firms relatively more often opted for the worst answering possibility (4) except for ineffectiveness which turned out to be the major problem for the Kazakh companies.

Figure 13: Problems with the Judiciary



ment of property rights by the judiciary does not seem to be very straightforward for the Uzbek companies. However, the increases in state shares may still have happened via buy-outs and thus with respect to

4.3.2 Problems with Bureaucracy

Privatisation was expected to create profit incentives which would revive the faltering transition economies. But “profit incentives to restructure privatised business and create new ones could be swamped by the burden on business imposed by a combination of (among other things) a punitive tax system, official corruption, organised crime, and an unfriendly bureaucracy” (Black, Kraakman, Tarassova, 2000, p. 1731). Bureaucracy hampers the evolution and development of companies due to market entry barriers and over-regulation.

Privatisation was therefore also expected to lower the incentives of the state to engage in the preferential treatments of some of its companies. But as in the case of other interactions among the state and its companies, the reductions in the active role of the state is supposed to take time. On the other hand, the resulting possibility of state support for the firms can play an important role in an economic environment which is characterised by the incompleteness and imperfection of various markets. This especially holds with regard to the acquisition of raw materials and intermediate goods as well as credit or other forms of capital and with regard to the access to markets (McMillan, 1997, Whiting, 1996). As such, this section reveals insights into the support and problems stemming from the direct contact between the state and its companies as well as via laws, rules and regulations.

The first question for this section asked the companies to rate their perception about the support of the state along three kinds of state agents: the central government, local governments, and state associations (only for Uzbekistan)³⁶. In accordance with the theoretical considerations about the incompleteness of various markets, the supportive aspect was asked along four categories: the acquisition of energy, of raw materials as two important inputs for production, the acquisition of bank credit in order to value the state’s role in access to capital and, finally, the state’s support in the companies’ sales and marketing as facilitated access to markets. The respondents were able to choose from four answering possibilities: (1) helpful, (2) rather helpful, (3) rather repressive, (4) repressive. The results are presented in Figure 14 recording the percentage of firms ticking answering possibilities (1) and (2), i.e. which perceive the state bodies as (rather) helpful.

The figure reveals that the helpfulness is much more evident for Uzbekistan. This confirms the active role of the Uzbek state in its corporate sectors and the higher restrictions on corporate liberties that were also found for the depth of state interference (see Section 4.2). This finding is in line with the theoretical considerations. As the Uzbek state retained larger shares in its companies, it has a higher incentive to engage in company support. But as already noted in the last Section, the data do not confirm any clear relationship between the state share and the companies’ perception of support.

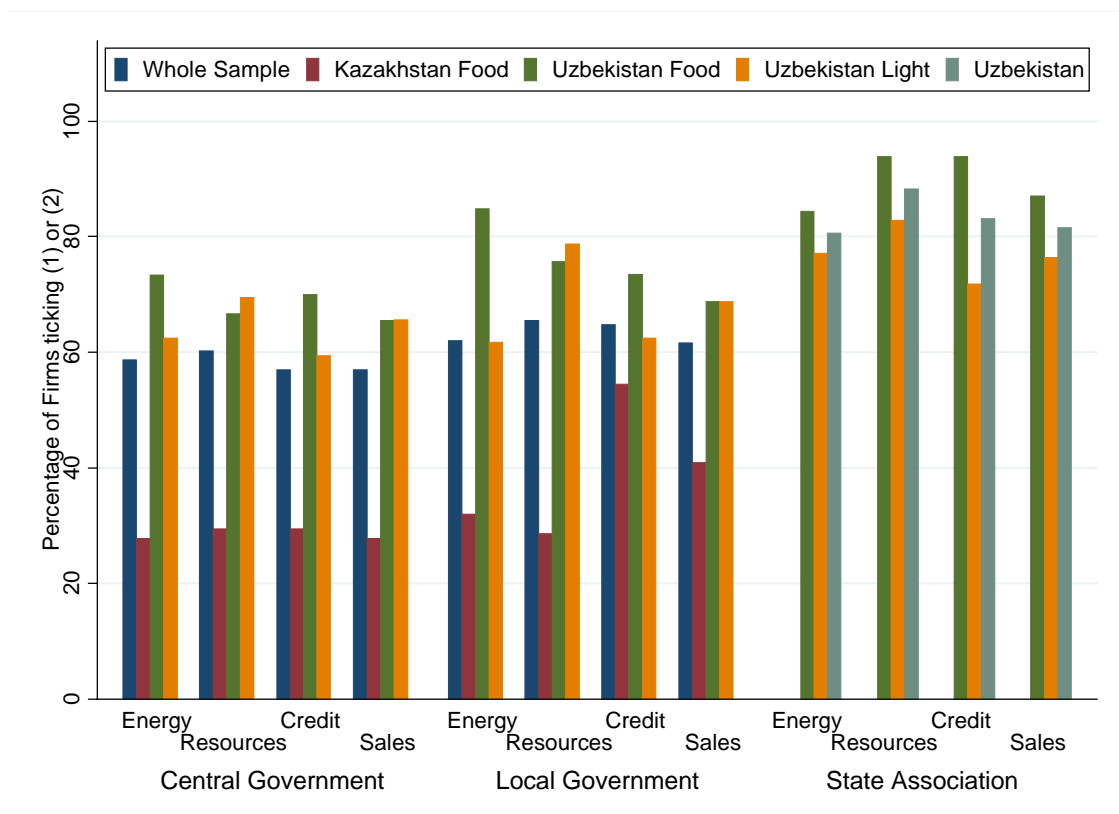
private property rights.

³⁶ The state associations, the former industrial ministries, have been abolished in Kazakhstan after its independence.

This indicates that this connection is based on many other factors as well, e.g. the political connections of the companies' managers.

The figure reveals that in both countries the local governments are perceived as more supportive than the central government. Even in Kazakhstan, the local government is important in the allocation of credit and, in comparison to the other categories, also perceived as more helpful for the access to markets. For the Uzbek companies, this especially holds for the access to raw materials. In the case of the food companies, this also turns out to be the case for the access to energy. State associations constitute the most supportive agents for the Uzbek companies in general and the ones of the food industry in specific. Conclusively, while the state still plays a much larger role in corporate Uzbekistan, it has retrieved to a larger degree in Kazakhstan.

Figure 14: **State Support for the Companies by different State Agents in 2004**

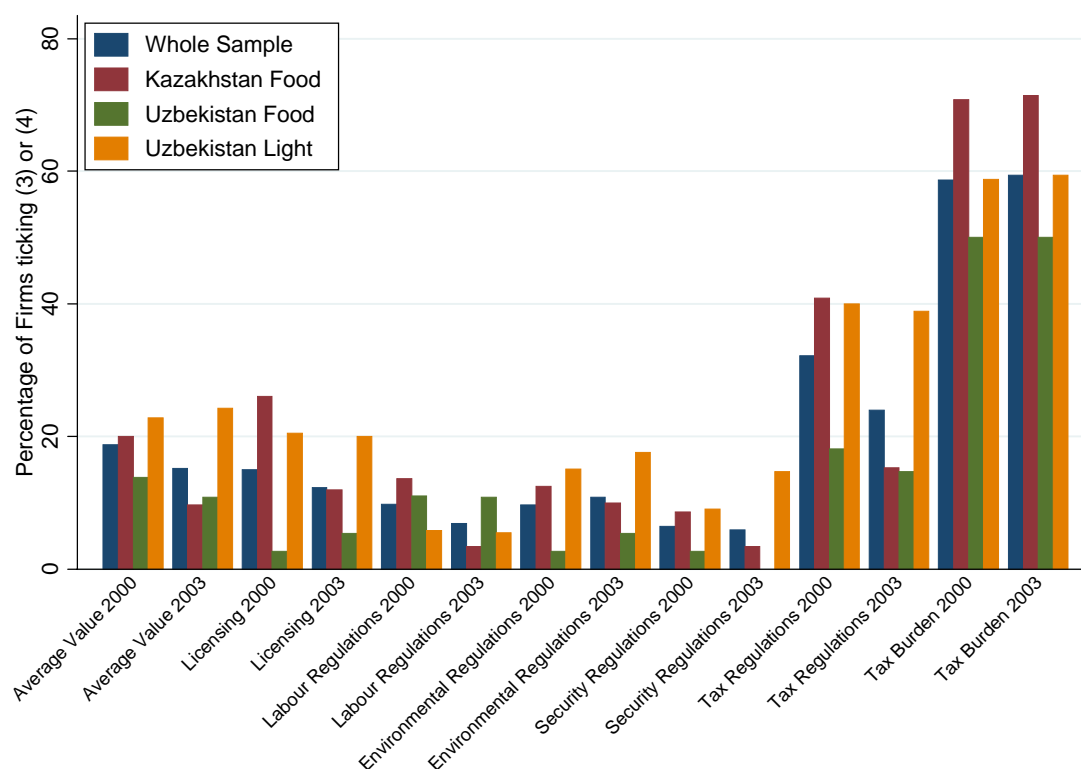


Turning to the negative factors of the bureaucracy, Figure 15 reveals the results for bureaucratic problems showing the percentage of firms ticking the two worst answering possibilities (3) and (4). The figure records an average value over the following categories as well as their separate frequencies: licensing, working regulations, environmental regulations, security regulations (fire protection etc.), tax regulations, tax burden. The regulatory framework is perceived the most problematic among the Uzbek companies of the light industry. These problems slightly increased between 2000 and 2003 due to ris-

ing problems with environmental and security regulations. The regulatory burden decreases in the food industries of both Kazakhstan and Uzbekistan. Among the categories, the biggest problem is found to be the high tax burden and keeps stable between 2000 and 2003.

While the overall picture looks bleaker for Kazakhstan than for Uzbekistan, the problem is deeper in the latter country. The Uzbek companies more often refer to the tax burden as a “bigger obstacle”, the worst answering possibility (4), while the Kazakh companies mostly rate it as a “moderate obstacle”. Tax regulations constitute the second biggest obstacle though they appear to have improved enormously in Kazakhstan in recent years. The other regulatory areas seem to pose only minor obstacles. The resulting problems are perceived to have decreased over time except for the small deterioration of problems from environmental regulations in Uzbekistan. Conclusively, the regulatory framework does not seem to pose too high an obstacle for the companies in Kazakhstan and Uzbekistan, maybe except for tax regulations. The companies might simply be used to a regulated environment and, consequently, do not perceive it as a bigger problem.

Figure 15: **Problems with Bureaucracy – Rules and Regulations**

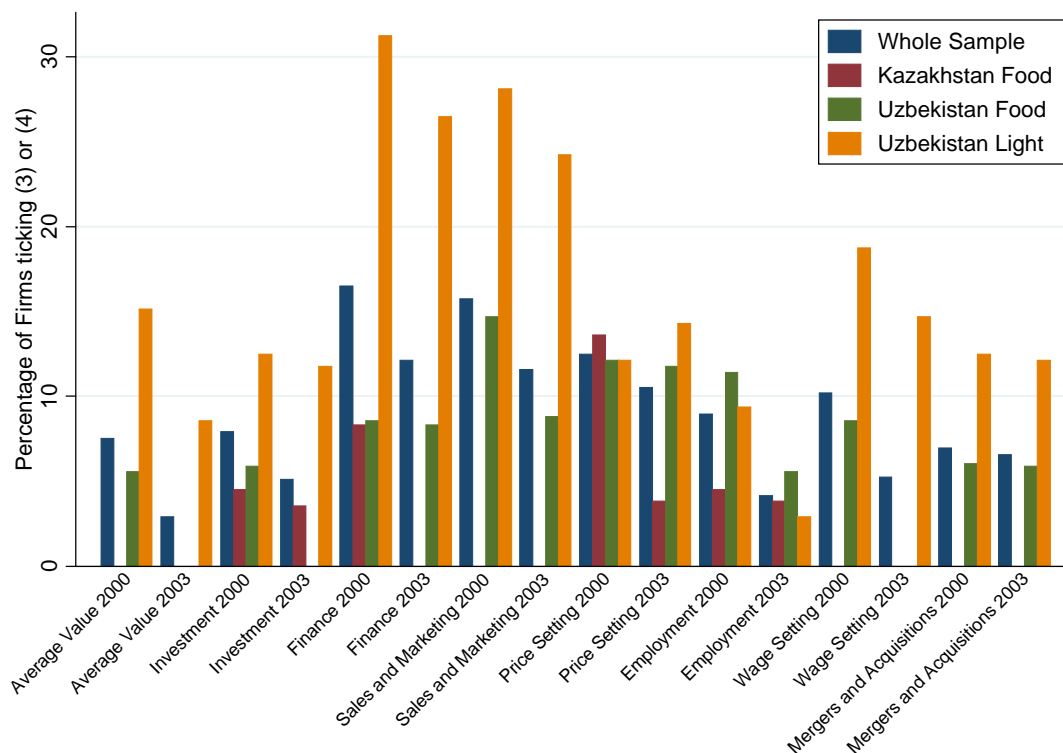


This picture is confirmed by the results from another question about the extent of the resulting constraints in the companies’ decision making due to the existing state laws and regulations. The respondents were asked to rate the constraints along the following

categories: investment, finance, sales and marketing, price setting, employment decisions, wage setting, and mergers and acquisitions. Figure 16 reports the percentage of firms ticking the worst two answering possibilities along the separate categories as well as for an average value. Only a few Kazakh companies report to be constrained with regard to investment, price setting and employment decisions as well as finance in the year 2000. According to the average values, no Kazakh company feels constrained by the bureaucracy which results from the very good perception of totally missing constraints in some categories as sales and marketing, wage setting and mergers and acquisitions.

In Uzbekistan, only very few of the counterparts in the food industry end up with an average value of 2.5 or more in the year 2000 and none of them any more in 2003. According to the separate values, Uzbek firms feel a little more constrained in their decision making. This is especially the case for the firms in the light sector industry and in the fields of finance as well as sales and marketing. The overall picture still confirms that laws, rules and regulations are not perceived as major constraints and that the situation is improving.

Figure 16: **Problems with Bureaucracy - Constraints in Decision Making due to Rules and Regulations**



4.3.3 Problems with Finance

An important aspect for companies in transition countries is to raise capital in order to undertake the necessary restructuring and expansion of old firms and the set-up of new ones. This section reveals insights into the cumbersomeness resulting from the banking system and the resulting capital constraints for the companies. As was already shown at the beginning of Chapter 4, problems with finance constitute serious obstacles for companies in Kazakhstan and Uzbekistan, especially for the larger firms of the Uzbek light industry. State bodies are still supportive in gaining access to credit, especially for the Uzbek companies of the food industry. For the results of this section, the companies were asked to rate the financial system of their country and its development over the last three years. Two questions addressed the recordation, disclosure and the audit of financial statements of the companies. A further question asked to rate the requirements of the banks with regard to the companies' accessibility to credit.

On the whole, the financial system is rated rather badly among the companies. 18 of the 97 responding companies perceive it to be "bad" and 25 opted for "rather bad". Among the sectors, the Uzbek firms of the light industry gave the worst values with 10 out of 35 companies perceiving their financial system as "bad" and 9 as "rather bad". This may be due to their size and the resultingly bigger demand for external capital. The results for the Kazakh enterprises are highly concentrated on the medium answering possibilities with 10 out of 27 firms rating the financial system as "rather bad" and 9 as "rather good". The Uzbek companies of the food industry mostly view the financial system as "good" (12 out of 35) and "rather good" (10). This may be due to their preferential access via the support of state bodies (see previous Section 4.3.2). The same sectoral division turns out for the development of the financial system over the last three years. The overall judgement, however, was much better with 63% of all companies perceiving the financial system as "improved" or "rather improved".³⁷

With regard to financial statements, 88 of 102 companies reported to prepare and issue them on a regular basis, i.e. at least once a year.³⁸ Another 13³⁹ firms, 7 of them and thus relatively more from Kazakhstan, responded to do that on an irregular basis and one Uzbek company in the food industry reports to prepare non at all. 89 out of 99 companies reported that their financial statements are audited by external auditors.

Banks and other creditors contribute to the bleak assessment of the financial system as can be seen in Figure 17. The firms were asked to rate certain aspects of bank credit as no (1), minor (2), moderate (3) or major (4) obstacle: collateral requirements, administrative

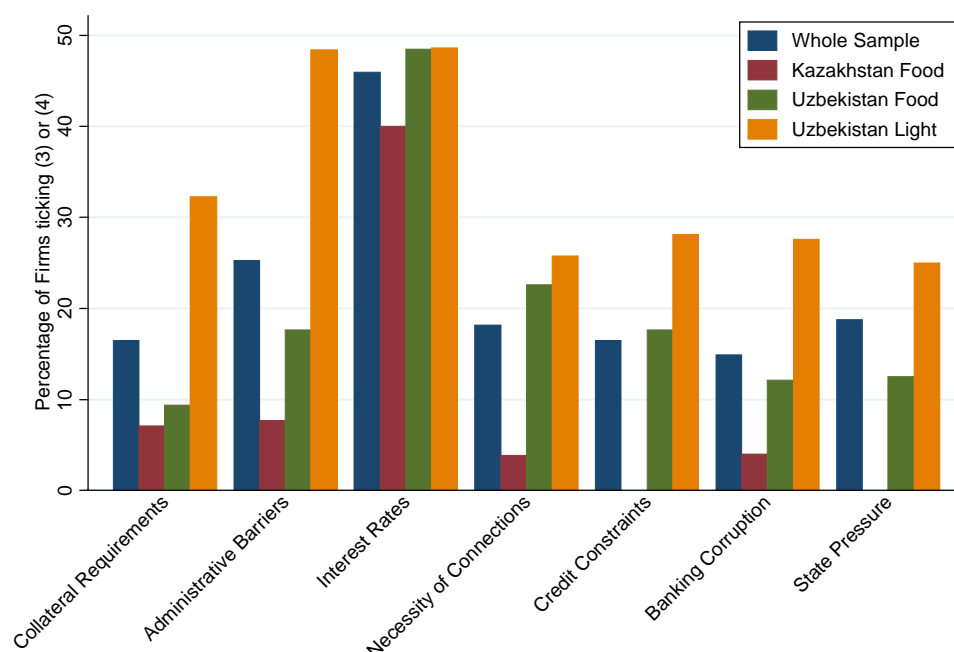
³⁷ The Transition Report 2005 reported that finance is seen as one of the major constraints by many firms in the transition countries which made it a greater obstacle than in mature market economies. However, the perceived difficulties in obtaining credit have declined between 1999 and 2005 as financial systems have expanded which narrowed the gap to mature market economies.

³⁸ The companies in these two countries are actually supposed to issue financial statements on a regular basis according to the national laws on joint stock companies.

³⁹ One Uzbek company from the food-processing industry reported to issue financial statements both on a regular as well as irregular basis which is just counted in the first category.

barriers, interest rates, necessity of connections, credit constraints, corruption among bank officials, and state pressure (only for Uzbekistan). Almost half of the Uzbek companies and 40% of the Kazakh companies perceive interest rates to be a moderate or major obstacle which turns out to be the major problem for the access to credit.⁴⁰ The Uzbek companies in general and once again specifically the ones of the light industry see their banking system in a worse shape than the Kazakh companies. Among the latter, also about half of them perceive the banking administrative barriers as a problem for their company in order to be able to collect credit. The big obstacle of high interest rates points at a low degree of competition among banks in these two countries. This in return impedes further corporate development and restructuring activities.

Figure 17: **Problems with Finance – Access to Credit**



The banking sector in Uzbekistan is much more unreformed and less developed than in Kazakhstan.⁴¹ We therefore expect credit rationing and the old habits of preferential access to capital to be much more prevalent in Uzbekistan than in Kazakhstan. Some

⁴⁰ The Transition Report 2005 (EBRD, 2005) reports the same result for the transition countries as a whole. The cost of finance turned out the most important constraint to credit, e.g. rather than the need for collateral.

⁴¹ The EBRD reports an index of banking sector reform and an index of reform of the non-bank financial sector. The slow reform progress and backwardness with regard to the banking sector is expressed by Uzbekistan's score of 1.7 with only one upgrade in 1995 from the initial value of 1.0. In contrast, Kazakhstan's reform development was continuously upgraded from 2.3 at the end of the 1990ies to 3.0 since 2003. The gap is much closer for the index of reform of non-bank financial institutions where Kazakhstan's score amounts to 2.3 and Uzbekistan's to 2.0 while both values kept unchanged since 2000.

evidence is given by the results from the other impeding factors of the banking sector. These do not turn out to be seriously constraining for most of the companies. But some companies, especially and for some categories only the Uzbek ones, do report about problems as corruption of banking officials, the necessity of connections and state pressure and even specify to be credit constrained. These do not only constitute severe obstacles but also affect between 18.8% of the Uzbek companies in case of state pressure and even 24.2% of them with regard to the necessity of connections. As these pose high impediments to the development of a sound corporate sector, there is much room as well as accumulated need to reform the banking sector, particularly in Uzbekistan, in order to increase capital efficiency and overall productivity.

4.3.4 Competitive Situation

Competition is one of the main driving forces for an efficient allocation and use of capital in and among firms, both in static as well as dynamic perspective. This creates a trade-off for the consequences of competitive pressures on the companies' performance. In a static perspective, strong competition does not allow for inefficiencies in the use of a company's resources as this may lead to the bankruptcy of the firm. But with regard to the dynamics of firm development, the rivalry between firms reduces a company's profits and thus the means and incentives for restructuring efforts and innovation. This leaves an ambiguous relationship between competition and performance and points the way that a perfectly competitive market structure is not necessarily the most desirable one. In the dynamic perspective however, market power may only be transitory as successful innovations are copied and new ones introduced (EBRD, 1999).

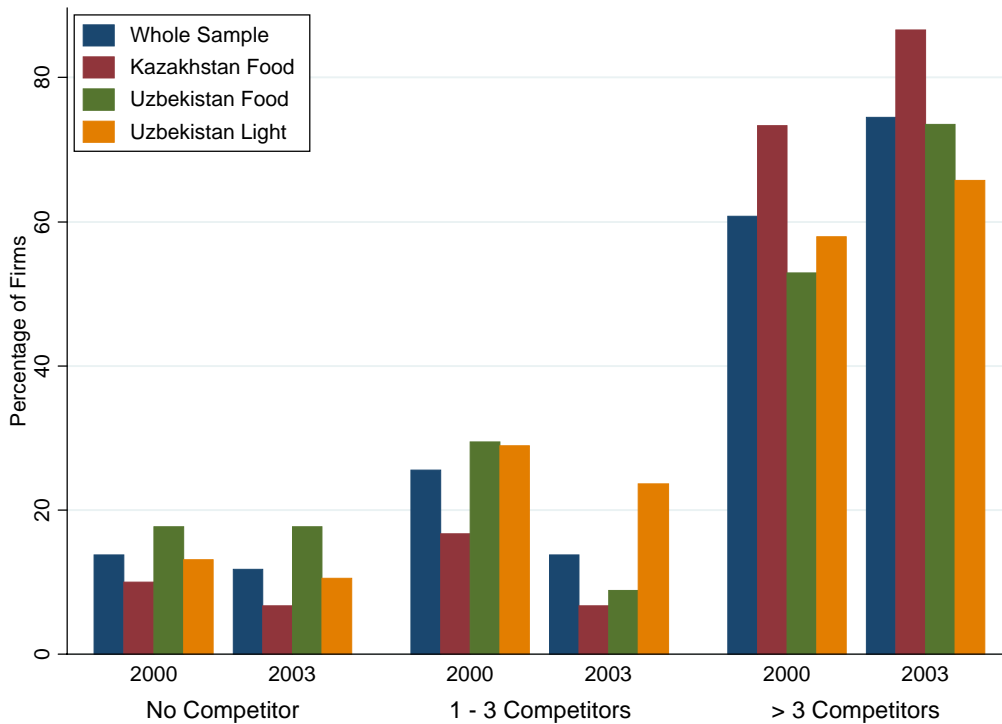
With regard to a successful privatisation process in transition economies, competition is another factor of the institutional framework which was missing to a large degree. This institutional vacuum left the scope for an inefficient use of resources as well as low incentives for the restructuring of firms and innovations. As such, the problem with regard to the transition countries seems to be rather too less competition than too much.

Three questions were addressed in order to judge the competition environment of the companies. Two of them referred to the competitive situation, current and in 2000, the other to the behaviour of the competitors. The companies' competition environment is rated along the number of rivals in the firms' main product market. Among the responding 102 companies, 12 (14) reported to have no competitor in the year 2003 (number in brackets refer to 2000), 14 (26) to deal with between one and three rivals, and 76 (62) to operate in a market with more than three competitors. These results are presented in Figure 18 depicting the percentage of firms along the three competition categories and the two years. Competition turns out to be rather strong, even more so in Kazakhstan than in Uzbekistan, which is not necessarily unexpected given the industrial sectors they operate in and the low industrial diversification of the CARs. Most of the Uzbek companies in the light sector industry engage in cotton- or silk-processing tasks.

Missing competition could have been a selection criteria in the privatisation processes for a higher state ownership in monopolistic companies. But there is only limited evidence that competition relates to the ownership stake held by the state. Only 2 out of 11 (18.2%) companies with state majority stakes have no competitor in 2003 (values for 2000: 23% or 3 out of 13), whereas 13.2% or 10 out of 76 majority state owned companies faced fierce competition from more than three rivals (values for 2000: 15.1% or 11 out of 73). As such, the preponderance to be a monopolistic company is only slightly higher for those with state majority ownership stakes.

Figure 18 reveals that competition increased over time. While the Kazakh food industry and the Uzbek light industry both lost a monopolist, most of the market changes occurred in the way that companies with up to three competitors saw their number of rivals increasing. This happened for 4 companies of the Kazakh food, 7 of the Uzbek food and 5 of the Uzbek light industry, while one Kazakh firms and two Uzbek light industry firms experienced a competitive change in the opposite direction. One Kazakh company even saw its monopolistic status eroding to more than three rivals in the market. This company also specified that it rates the behaviour of these new competitors as “incorrect” or “unfair” which was asked for in a third question about the competition environment. Overall, the Uzbek companies rated the behaviour of their competitors in a much friendlier manner. 59% of firms among the food-processing and 46% among the light industry sector opted for a “correct” relationship. On the other hand, 50% of the Kazakh companies allotted their rivals a “rather incorrect” and 14% an even “incorrect” behaviour.

Figure 18: **Competitive Situation**



This less unfair competition behaviour of rivals in Uzbekistan may stem from the stricter organisation of companies under the state associations (former industrial ministries), which have been abolished in Kazakhstan. In this way, the organisational structure of the industries may reduce the competitive pressures in Uzbekistan. As already noted, competition does not necessarily have an unambiguously good or negative impact on economic development. Given the high necessity to improve the allocation of the factors of production in transition, competition could bolster that process presuming that the institutional environment does not prevent the entry of new and exit of old firms.

4.3.5 Problems with Unpredictability of Laws, Rules and Regulations

Security about the future progression of laws, rules and regulations plays a key role for business development. Uncertainty and unpredictability hurt the evolution of the private sector as irreversible investments, especially the long-term kinds, are put on hold. This becomes costly in terms of aggregate investment⁴² and thus in terms of economic development.

Some of the negative aspects of uncertainty with regard to the future enforcement of property rights have already been studied in Section 4.3.2. This section, in contrast, comprises 6 questions and investigates the uncertainties in doing business with regard to changes in laws, rules and regulations. This is an especially important aspect for the transition countries as the political circumstances as well as the institutional framework have changed rather quickly since the 1990ies. The questions of this section asked about the frequency of unexpected and of retroactive changes in laws, rules and regulations, and about the preceding notification and participation of enterprises in the rule-changing process. Figure 19 presents the percentage of firms ticking the worst two out of four answering possibilities. The figure confirms that the companies in Kazakhstan and Uzbekistan operate in a rather unpredictable and unreliable political environment. 43% of the companies specified that changes in laws, rules and regulations were “frequently” or even “regularly” unpredictable. With regard to retroactive changes of policies, around 30% of the companies reported about their frequent existence. On the other hand, the development of the predictability of policy changes in recent years has been rated best among the Kazakh companies as only very few companies opted for a bad evaluation as depicted in Figure 19.

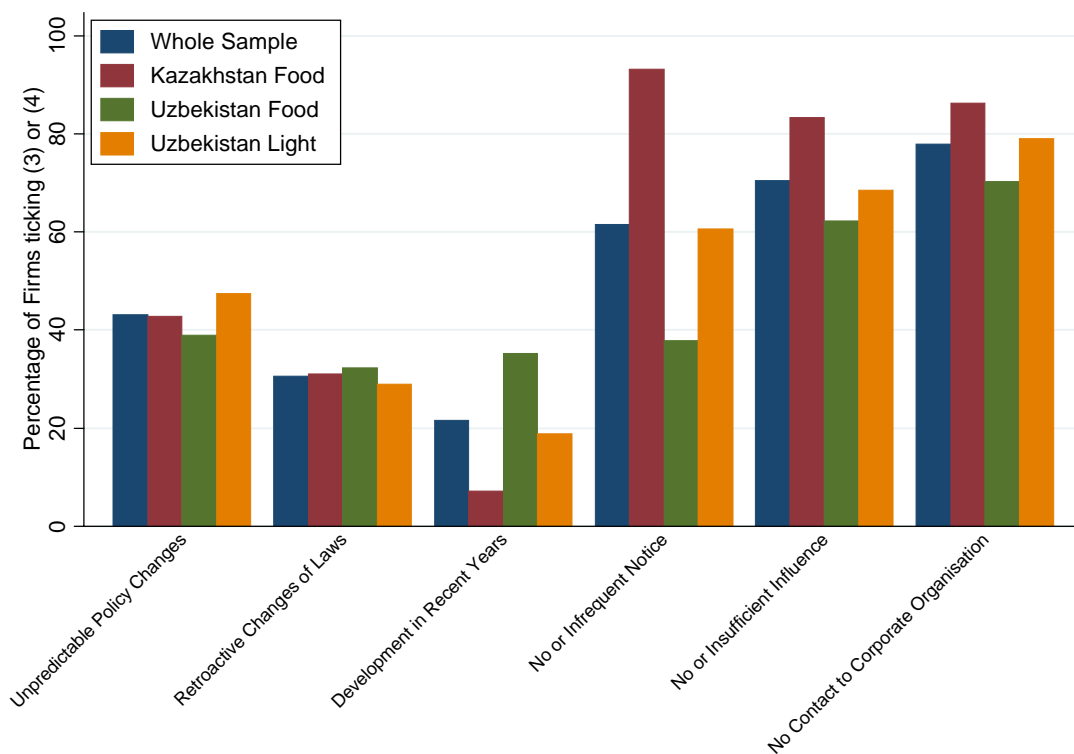
With regard to the frequency of unpredictable and retroactive policy changes, the complaining companies are relatively evenly split among the three subgroups and thus among the countries as well. This contrasts with the results for an insufficient information about policy changes as well as the possibility of the firms to influence these changes. Kazakh companies stand out as feeling more uninformed and less influential than the Uzbek companies, especially the Uzbek counterparts of the food industry. The

⁴² For the theory of irreversible investment, see e.g. Dixit and Pindyck, 1994.

same holds for the missing contact of the enterprises to corporate organisations in order to bundle their impact on the further evolution of the regulatory framework.

After all, the companies in these two countries face highly volatile and unpredictable institutional environments which they have to cope with. Even if they got used to it, unpredictability and insecurity hampers the proper development of the corporate sector as these pose a clear disadvantage against countries with better and more reliable institutional environments.

Figure 19: **Problems with Unpredictability and Insecurity in 2004**



5 Performance

The improvement of corporate performance was one of the main goals of privatisation in transition countries. Privatisation lowers the political ambitions to provide soft budget constraints for the companies which was a big source of corporate inefficiencies in socialist times (see e.g. Kornai, 1992). Private owners are expected to pursue performance-oriented goals as they are less influenced by political and social considerations. Privatisation therefore was thought to improve the application and thus the productivity of the factors of production in the companies and thus ameliorate their allocation in the economy. The more, harder budget constraints should set firmer incentives to engage in innovations and further productivity increases. As a consequence, corporate transition to market-oriented production should be accompanied by a high degree of restructuring in the firms as their inherited capital stocks were obsolete and the use of labour skewed along ideological socialist considerations. The engagement in restructuring should also lead to performance gains albeit this could occur with a certain time lag.

5.1 Restructuring Efforts

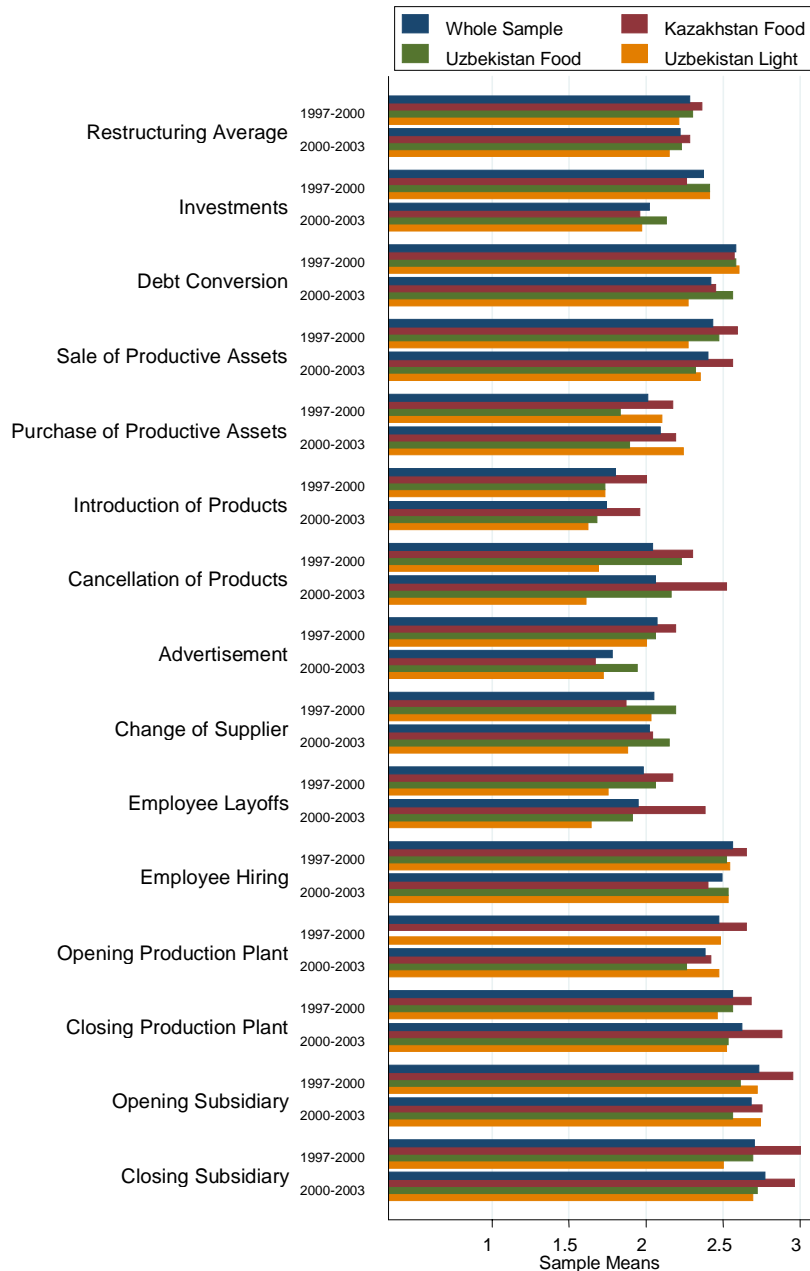
The survey respondents have been asked to rate the frequency of their companies' efforts to engage in restructuring for the time periods between privatisation (or 1997) and the year 2000 and between 2000 and 2003 along three answering possibilities: (1) often, (2) seldom, and (3) never. The data thus rest on perceptions in describing the restructuring efforts of the firms which were recorded for the following 14 categories (pairs separately): investment, conversion of debts, sale and purchase of productive assets, introduction and cancellation of a product (line), advertisement, change of supplier, employee layoffs and hiring, opening and closure of production plant, opening and closure of a branch or subsidiary.

Figure 20 provides the means for the whole sample and the three subsamples along these different categories and an unweighted average value.⁴³ Astonishingly and contrary to the demands of a corporate and institutional environment in transition, average restructuring efforts have a mean value of more than 2. That means that average restructuring among the firms and among the restructuring categories has been pursued less often than "seldom". Admittedly, some of the restructuring efforts constitute long-term decisions of the companies which do not frequently feature on corporate agendas. But nevertheless, restructuring efforts were rather weak and their frequency slightly de-

⁴³ The average value was calculated as the unweighted mean over the different categories. As the data availability varies between some of the companies, a few average values which were based on less than five observations per time period were dropped.

creased for the latter time period between the years 2000 and 2003 (or up to the date of the questioning in 2004).⁴⁴

Figure 20: **Performance of the Companies – Frequency of Restructuring Efforts**



⁴⁴ This reduction in restructuring efforts may be due to a shorter time span as the latter time period is shorter for most of the companies than the first which depends on the year of privatisation (see Section 3.3).

Among the subsamples, restructuring was pursued most frequently among the Uzbek companies of the light industry followed by their national counterparts in the food-processing industry. Kazakh companies reported the lowest average efforts for both consecutive periods. The biggest differences among the three subsamples and along the described order are to be found for the cancellation of a product (line) and worker layoffs for the more recent time period with no signs that these had been pursued more profoundly in Kazakhstan in the preceding period. On the other hand, Kazakhstan slightly leads the restructuring list with regard to new investments. With regard to the introductory words as well as considerations from preceding chapters, factors external to the firms may explain these differences. The institutional changes in Kazakhstan have been faster than in Uzbekistan and may have triggered a faster adaptation to market needs which of course reduces the restructuring necessities in more recent years.

The differences among the different categories are in line with the expected frequency of restructuring in firms. As more illiquid assets are replaced less frequently, production plants as well as branches and subsidiaries get seldom closed nor opened. Interestingly, the more liquid asset debt is rather rarely converted or restructured as well. The hiring of new employees gets as rarely pursued as the opening of a new production plant as perceived by the respondents. Although these two restructuring efforts may of course be related, the recorded restructuring of debt and employees seems to be rather low in contrast to the expectations and needs resulting from the transition to market forces. But positively in this respect, productive assets are more frequently purchased than sold⁴⁵ and investment activity picks up in more recent years.

5.2 Performance Indicators

Restructuring is an important aspect for the improvement of a company's future performance. The questionnaire included two questions about the performance of the companies. The first referred to performance indicators as reported in their financial statements which most of them reported to issue on a regular basis and to be audited externally (see Section 4.3.3). These performance indicators should provide evidence about the microeconomic development of the food industries in Kazakhstan and Uzbekistan and the light industry in Uzbekistan. We are thus able to compare the development of the same industrial sector among two countries as well as the developments of two different sectors in a single country, i.e. in Uzbekistan. The second question asked the respondents to rate the development of revenues, profits, employment, liabilities and receivables for the periods privatisation until 2000, 2000 until 2003 and for the consecutive three years, 2004 until 2007.

⁴⁵ Though the old productive assets may just not be worth selling.

Table 7: Descriptive Statistics for the Performance Indicators

	Kazakhstan Food			Uzbekistan			Uzbekistan Food			Uzbekistan Light		
	Mean	StD	N.O.	Mean	StD	N.O.	Mean	StD	N.O.	Mean	StD	N.O.
Revenues Priv.	243539	449578	20	6784.88	18121.6	49	2658.84	2301.51	22	10146.8	23996.7	27
Revenues 2000	275039	851284	25	2627.90	5354.8	71	2931.26	4494.76	36	2315.87	6167.6	35
Revenues 2003	415292	1260890	24	2917.11	6225.4	73	2897.29	4058.64	36	2936.4	7842.0	37
Revenues per Employee Priv.	633.30	667.12	19	5.020	6.250	48	7.999	7.797	22	2.498	2.819	26
Revenues per Employee 2000	663.21	672.69	25	4.167	6.037	71	7.318	7.187	36	0.925	0.721	35
Revenues per Employee 2003	830.50	897.67	24	4.369	5.872	73	7.072	7.043	36	1.739	2.512	37
Profits Priv.	31845	110694	20	513.79	1960.81	51	192.46	291.09	24	799.40	2671.86	27
Profits 2000	38540	86404	26	144.91	584.82	70	72.91	107.74	36	221.14	831.37	34
Profits 2003	58700	132434	26	51.52	205.29	71	57.75	130.84	35	45.46	259.96	36
Profits per Employee Priv.	119.88	293.64	18	0.2580	0.3408	51	0.409	0.372	24	0.124	0.247	27
Profits per Employee 2000	117.40	185.22	25	0.1010	0.1345	70	0.152	0.129	36	0.047	0.120	34
Profits per Employee 2003	166.50	220.96	25	0.0659	0.1273	71	0.117	0.158	35	0.016	0.055	36
Average Wage Priv.	9912	8963	21	28261	25953	42	20168	25748	14	32307	25547	28
Average Wage 2000	10846	8851	28	14078	6877	62	16394	7499	28	12174	5756	34
Average Wage 2003	12108	8334	28	20717	16632	62	24153	18833	27	18066	14437	35
Number of Employees Priv.	230	251	24	1338	2300	57	409	345	28	2235	2961	29
Number of Employees 2000	252	359	28	812	1492	74	389	301	38	1258	2037	36
Number of Employees 2003	318	449	29	666	1264	76	336	298	38	995	1711	38
Labour Productivity Priv.	1667	1570	14									
Labour Productivity 2000	2103	1642	17									
Labour Productivity 2003	2551	2091	17									
Actual Costs Priv.				5848	15503	50	2620	4249	24	8827	20862	26
Actual Costs 2000				1555	3825	69	1182	1224	37	1987	5476	32
Actual Costs 2003				2004	5099	72	1367	1766	37	2677	7076	35

Means, standard deviations (StD) and numbers of observation (N.O.) for the listed performance variables

Values are recorded in real terms and in local currency terms: thousands of KZT for Kazakhstan and millions of UZS for Uzbekistan

The results are presented in Table 7. It records the means and standard deviations of revenues, revenues per employee, profits, average wages, as well as of labour productivity for Kazakh and self-costs for Uzbek companies. The values are denoted in local currency terms, in thousands of KZT in Kazakhstan and millions of UZS in Uzbekistan. In order to facilitate the comparison over time, the nominal figures are diverted into real

values based on the year 2000.⁴⁶ The more, Table 8 presents annual average growth rates of overall revenues as well as revenues per employee.

Average revenues as well as average revenues per employee slightly increased in Kazakhstan between the year of privatisation and 2000 and highly increased in the latter period between 2000 and 2003.⁴⁷ While volatility increased among the overall revenues, this is highly due to the change in relative company sizes as the standard deviations in relation to the means are very stable over time for the values per employee. However, the average annual growth rates in Table 8 confirm this for overall revenues. With regard to revenues per employee however, the growth rates are rather similar for the two periods implying a more steady increase over time. The more, the development of revenues was accompanied by a corresponding change in employment and the positive correlation is increasing over time.⁴⁸

In Uzbekistan, revenues dropped between the year of privatisation and 2000. In the case of the companies of the light industry, the decrease was dramatic even if the sharp decrease in employment in this sector is accounted for (see Section 3.2 and Table 7). The drop in overall revenues is influenced by the increasing number of companies as the

⁴⁶ The conversion in real terms was carried out along changes (end-year) in consumer prices in Kazakhstan and Uzbekistan as reported in the latest editions of the EBRD Transition Reports. The end-year inflation rates are similar to the annual average counterparts in Kazakhstan but are significantly lower in Uzbekistan in more recent years. That implies that the performance changes between 2000 and 2003 may be skewed downwards. However, the nominal values in 2003 are nevertheless diverted by a factor of 1.6935 in Uzbekistan and 1.2114 in Kazakhstan. The performance indicators reported for the year of privatisation or 1997 are discounted according to the resulting year and thus differently. As inflation during the middle years of the 1990ies has been tremendously high in these two countries as well as the whole of the CIS, the discounting factors vary a lot between the years which has an impact on the comparability of the resulting real performance values among the firms. The more, the conversion neglects the development of relative prices in the countries as it is based on overall consumer prices and not on prices of the specific goods of the companies or sectors. That aggravates the comparability between the Uzbek companies of the food-processing and light industries. However, disaggregated price indicators are hard to come by for these countries.

⁴⁷ The number of observations once again changes over time which aggravates the comparability of the results. The picture does not change for the 19 and 18 companies reporting on data for revenues and revenues per employee respectively. Among them, means and standard deviations are slightly higher in all three points in time. Some of the observations constituted severe outliers which were eliminated in order to prevent their extraordinary impact on the descriptive statistics. This was carried out for revenues and wages while the outliers were identified according to their values per employee assuming that there is some upper limit in the variation of this figure among the companies. The eliminated values constituted severe outliers in this regard which led us to doubt the correctness of these data points. With regard to the data on revenues, this affected three Kazakh (one only reported a value for the year of privatisation and another one only for 2003) and two Uzbek companies from the food-processing industry. In the case of the two Uzbek companies, only the values for the year of privatisation (in both cases 1994) were dropped as the revaluation created extremely high real values. With regard to average wages, data for three Kazakh companies were dropped for the year of privatisation as this was 1992 and the revaluation created suspicious values. In Uzbekistan, data were eliminated for ten companies of the food and three of the light industry. Most of them seem to constitute rough assessments which got highly skewed by the transformation into real values.

⁴⁸ The correlation coefficient between annual growth rates of revenues and annual growth rates of employment is 0.51 for the period year of privatisation (or 1997) and 2000 and 0.80 for the period 2000 until 2003. The same happened in Uzbekistan albeit at a lower degree of correlation.

additional firms are smaller which increases the average revenues per employee in 2003. Among the companies of the food industry, the increase in the number of observations improves the development of revenues as recorded in Table 7. Among the 22 companies with data available for every point in time, average revenues drop to 2278 (2266) million UZS in 2000 (2003). Average revenues per employee keep on falling to 6.83 million UZS in 2000 and to 6.06 million UZS in 2003. As such, the Uzbek food companies fared worse than their Kazakh counterparts in terms of revenues.⁴⁹ Average annual growth rates of revenues in the Uzbek food industry are negative for both periods (see Table 8) as the smaller companies fare worse than their bigger counterparts.

A similar picture between Kazakhstan and Uzbekistan evolves with regard to profits. While Kazakh companies reported on a sharp increase in profits between 2000 and 2003, both in overall and per employee terms, Uzbek companies on average saw their profitability plummet in real terms. While the number of firms suffering losses decreased from 5 in the year of privatisation via 6 in 2000 to only 3 in 2003 in Kazakhstan, the number of Uzbek companies in the red increased from 3 in the year of privatisation and in 2000 to 11 in 2003.

Average real wages slightly increased in Kazakhstan over time. In Uzbekistan, they halved between the year of privatisation and 2000 which was mainly driven by the larger decrease among the companies of the light industry. Real wages rebounded between 2000 and 2003 though their average noticeably remained below the initial level from the mid-1990ies. This may again be influenced by the transformation to real values though the obvious outliers have been removed (see footnote 47). Otherwise, labour productivity on average increased among the Kazakh companies. And actual costs got trimmed in Uzbekistan over time coming along with the reduction in the labour force.

Table 8: Descriptive Statistics for the Annual Growth Rates of Selected Performance Indicators

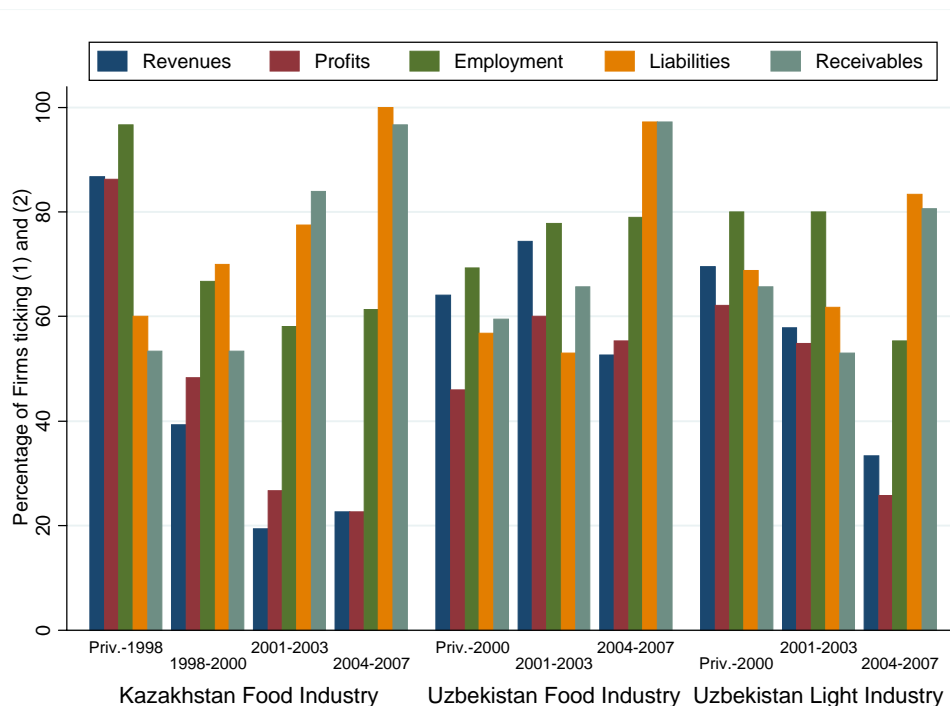
	Whole Sample			Kazakhstan Food			Uzbekistan Food			Uzbekistan Light		
	Mean	StD	N.O.	Mean	StD	N.O.	Mean	StD	N.O.	Mean	StD	N.O.
Revenues Priv.-2000	-7.845	20.25	68	0.932	21.68	20	-4.741	17.355	22	-17.22	18.105	26
Revenues 2000-2003	0.447	23.38	95	8.511	18.19	24	-7.743	21.671	36	3.341	26.056	35
Revenues per Employee Priv.-2000	-0.408	23.25	66	3.491	20.98	19	2.101	20.921	22	-5.578	26.55	25
Revenues per Employee 2000-2003	6.593	21.46	95	4.374	10.70	24	-1.526	17.897	36	16.47	26.32	35

Means, standard deviations (StD) and numbers of observation (N.O.) of the average annual growth rates of revenues and revenues per employee for two periods of time: the year since privatisation until 2000, 2000 until 2003

⁴⁹ This may be influenced by the conversion into real values as the Uzbek companies were privatised earlier and their performance values correspondingly more heavily revalued with regard to the year of privatisation.

The annual average growth rates as well as their variations among the company groups imply that the development of the companies within the industrial sectors was very different. This is confirmed by the companies' perceptions about the development of the performance indicators asked for in the second question. Figure 21 reports the percentage of firms ticking the worse two out of four answering possibilities denoting a decreasing or stagnant development along the performance categories.⁵⁰ The perception changes a lot over time⁵¹ as well as between the company groups. Most interestingly, the good performance of the Kazakh companies, being revealed by the performance data so far, was perceived as relatively bad by the respondents after privatisation. With regard to the development of revenues, the share of pessimistic respondents of companies drops from 86.7% before 1998 to only 19.4% for the period 2001-2003, all referring to a decreasing development. The future assessment (the period 2004-2007) looks even brighter as 22.6% of enterprises expect revenues to keep stable and not a single one examines a negative trend. The assessment of the Uzbek companies is very mixed. Among them however, the firms of the light industry rate their future outlook much more brightly than their counterparts of the food industry.

Figure 21: Performance Indicators – Assessment of Past and Future Development



⁵⁰ The connection of the answering possibilities and their assessment is not straightforward for all performance categories. E.g. with regard to the development of liabilities, a stagnant or even decreasing trend of course cannot be rated unambiguously as “worse” than a decreasing trend.

5.3 Development of Wages and Wage Differentiation

Another section of the questionnaire referred to the development of real wages and wage spreads within the companies. In the socialist past, the remuneration of the factor labour was heavily influenced by ideology. As a consequence, wage inequalities were kept very low. They could be expected to increase sharply during the transition to market-based remuneration schemes. On the aggregate level, wage inequality was already found to have risen dramatically in the transition countries (see Flemming and Micklewright, 2000, and Milanovic, 1998 and 1999). Our results present micro-level evidence for the development of real wages and wage spreads in Kazakhstan and Uzbekistan. These are based on the statements of the companies' respondents and have to be taken with caution.⁵²

More of the companies reported on an increase of wages for both employees and managers than on a decrease or stagnation. The more, the companies' specifications about the wage developments of the two types of company staff took place in a respective manner as can be seen in Figure 22.⁵³ As expected, wage spreads increased during transition. This holds for both the spread between the highest and lowest wages as well as for the wage gap between managers and employees (denoted as wage spread 2 in Figure 22). Not surprisingly, the development of both wage spreads turns out to be the same.⁵⁴ In comparison to the Uzbek companies, only a minority of the Kazakh enterprises saw their wage gaps increasing while most of the others opted for a stagnant development. There is evidence that the increase in the wage spread has been substantial though the answers varied a lot among the companies and have to be taken with caution as most of them are estimates. On average, the spread between highest and lowest wages increased by 89.3% between the year of privatisation and 2000 and by 87.7% between 2000 and 2003 although only 20% of the responding companies estimated the same

⁵¹ Note that the time periods are different between Kazakhstan and Uzbekistan. The different specification of the Kazakh questionnaire resulted from the fact that the country was heavily affected by the Russian financial crises in 1998.

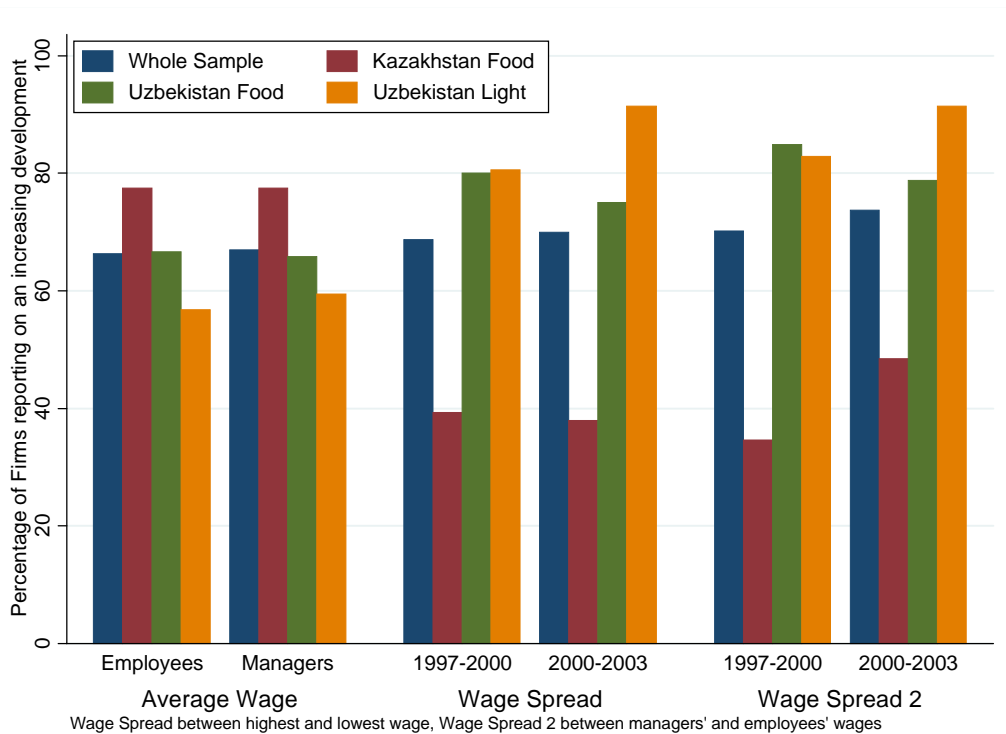
⁵² Although the questionnaire specified to base the answers on real wages, it is not always evident if the concept of real values was understood by all respondents. These doubts were already confirmed by the test interviews conducted before the actual survey. Consequently and as will be shown, the answers varied considerably among the companies. However, that does not affect the more interesting results about the development of wage spreads. On the other hand, the assessment of the development of wages may be skewed in favour of increasing wages.

⁵³ The different shares in Figure 22 for the two Uzbek company groups are based on one single company in each group. One Uzbek company in the food industry estimated that the wages of the employees increased while the managers' remuneration decreased. In contradiction, it also reported on an increasing wage gap between these two professional groups. On the other hand, an Uzbek company of the light industry specified that the wages of managers increased while it was indifferent about the direction of change with regard to the wages of employees.

⁵⁴ The figure implies that a bigger share of companies reported on an increasing wage spread between managers and employees than between the highest and lowest wages in Uzbekistan and in Kazakhstan for the period 2000-2003. However, this results from fewer respondents on the wage gap between managers and employers instead of absurd answers.

magnitude for both periods.⁵⁵ The corresponding values for the wage spread between managers and employees increased by 88% for the first and 62.5% for the second period.⁵⁶ The increase in the wage gap between managers and employees was smaller in recent years and much smaller than the increase in the overall wage gap.⁵⁷

Figure 22: **Development of Wages and Wage Spreads**



⁵⁵ The means are based on 63 and 64 observations respectively. Among the few companies reporting on a declining wage spread, this decreased by an average of 21% for the first and 24% for the second period, being based on only 10 and 4 observations respectively.

⁵⁶ The means are based on 63 and 67 observations respectively.

⁵⁷ This finding is independent from the companies reporting the same values for the two different wage spreads. Their share is very similar for both periods at around 40%.

6 Conclusion

This paper presented the results from a corporate sector survey among companies of the food industries in Kazakhstan and Uzbekistan and of the light industry in Uzbekistan. The survey was addressed to collect microeconomic evidence about the privatisation process and the use and design of manager contracts. The survey data proved that privatisation was much more profound in Kazakhstan than in Uzbekistan where the state retained larger shares in its companies. The data confirmed the insider privatisation among the Kazakh firms of the food industry and provided detailed information about the shares of two insider groups. While employees and managers received almost equal shares in their company in the early privatisation processes, since then the employees lost out to the benefit of the managers. The stakes in the Uzbek companies got much more dispersed among the different kinds of owners. The managers only became subordinate stakeholders.

With regard to manager contracts, there was no difference between the two countries. Despite their wide usage, incentive components with regard to the managers' remuneration as well as sanctions in case of bad performance were only very rarely included. We found no evidence that manager contracts might have increased the incentives and performance of the companies as was the case in China. While the proof of the Kazakh insider privatisation confirms its similarity with the Russian Federation, the corporate evidence for Uzbekistan just reinforces the slowness of the reform progress as reported in the economic literature but does not support its resemblance to China.

The insights from the privatisation process in both CARs were related to the resulting control structures as well as state interference in the companies' affairs. Company control was recorded to have been transferred into the hands of corporate bodies in most areas of decision making. The interference of the state is still felt considerably among the companies in both CARs, especially in Uzbekistan. Average state interference declined in more recent years confirming the consideration that it takes time for the state in transition countries to change its status. This trend was only very weak and not confirmed for all company groups. State intervention increased with the state share. But surprisingly, the data rather confirmed an inverted-U instead of a proportional relationship as interference increased for a state share between 25 and 50% but decreased thereafter.

The survey confirmed the ample evidence of problems faced by companies in transition countries. As in other transition countries, the tax burden turned out to be perceived as the biggest obstacles for doing business in two CARs. To some extent, the data confirm the finding that companies in less reformed and transformed transition economies draw a more content picture about their institutional environment. However, this seems to be due to the supportive aspects of the state for selected companies. As the state acts on behalf of these firms, their perception about the problems accruing from state regulation etc. becomes more positive. As a result, state bodies are viewed as much more supportive in Uzbekistan than in Kazakhstan. This state behaviour reinforces the impor-

tance of connections and preferential treatments and hampers the overall development of a vibrant corporate sector.

We found evidence on the unreliability of the judiciary and further problems with bureaucratic regulations. With regard to problems of finance, high interest rates turned out to pose the biggest obstacle to the development of a properly functioning financial market. Preferential treatment of well-connected enterprises by financial institutions remains much more prevalent in Uzbekistan than in Kazakhstan indicating the strong need for further reforms in Uzbekistan in order to decrease its backwardness. Competition increased in recent years in both countries but, due to a higher degree of organisation among the companies, is rated as more fair in Uzbekistan. Overall, the companies still act in highly unpredictable and insecure institutional environments constituting an obstacle to the development of a more dynamic corporate sector.

Restructuring was found to have taken place on a small scale given that companies in transition should have lots of scope to improve their efficiency. With regard to the performance indicators, corporate development in Kazakhstan turned out to have been much more favourably than in Uzbekistan. Especially in the Uzbek light industry firms experienced high decreases in revenues and employment after the privatisation.

7 References

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