Comparison of industrial transformation models

in the new Member States

European Economic and Social Committee

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Preface by
Mr Joost van Iersel,

Chairman, CCMI

The European Economic and Social Committee's Consultative Commission on Industrial Change embarked upon a unique journey early in 2008. The CCMI decided to examine the economic development in ten new EU-member states, especially from the point of view of industrial sectors, following the fall of the communist regimes. Thus three public hearings were organized in Ljubljana, Budapest and Sofia, where prominent academic professors and representatives of various industrial sectors attended as speakers. These hearings examined Slovenia, Romania, the Czech Republic, Hungary, Poland, Estonia, Bulgaria, Latvia, Lithuania and Slovakia. You are holding the findings of these three hearings in your hand.

The CCMI wanted to have answers to questions like: how did these countries manage the transition to market economy, looking also at the drawbacks, tensions and problems experienced in the course of this transformation process? What successes and failures can they call their own, and what are the defining factors that have resulted in them? What can be learnt from each other to manage restructuring, industrial change and transition in general in a better manner? Are there any best practices, and if so, could they be exchanged, transferred from one country to another?

Another very important aim was to see how EU-accession influenced the development of the economy and especially industrial changes. Therefore, the CCMI examined the effects of preparations for EU-membership on the industrial sectors ("before"), and looked closely at the developments in the period since the date of accession ("after"). Is there a palpable progress that can directly be linked to the EU-membership? The "before" and "after" developments were examined in the light of the Lisbon strategy goals.

The presentations at the hearings have shown that the transition process was extremely different in each country. The reforms were based on the level of centralization, economic structure as well as on the attitude for reforms within the population. We have found that direct industrial policy (in the sense of direct support of particular sector) was used only rarely. There were even signs of no real industrial policy in certain countries. Industrial policy was basically concentrated on indirect support of the general economic environment. Building of strong private and competitive sectors, attracting the foreign direct investments and setting the set of codes securing good entrepreneur's behavior were the key issues. This process was not an easy task; it naturally came to some disturbances. Misusing of market power or

not really transparent privatisation practices occurred in each country. But on the whole, the transition process can be considered as a success story in all of these countries, resulting in EU-accession.

I invite you to study our report and to make good use of it; we hope that the CCMI can contribute to a better understanding of the economic development in the new member states and that this report will complement the Commission's communication on "Five years of an enlarged EU", which aims to assess the economic implications of enlargement for old and new Member States in order to identify strengths and weaknesses and the implications in terms of policies.

I wish you pleasant reading.

Joost van Iersel
Chairman, CCMI

Comparison of industrial transformation models in the new Member States

Report drafted under the co-ordination of Mr. Vladimir Kvetan, delegate of the CCMI

Introduction

In 2008, the EESC's CCMI held a series of seminars aimed at garnering information about the major milestones in the change of economic principles in the countries of Central and Eastern Europe. The prime aim was to pinpoint the key political and economic decisions that put in place the industrial structure these countries have today. Three hearings were held in 2008: in Ljubljana, Budapest and Sofia. Each seminar profiled three countries (four in the case of Sofia) and each was divided into academic and practice sessions. In the academic part, economists and the movers behind economic reforms set out the major landmarks in the transition process in their countries. The practical part illustrated the impact of economic transformation on a chosen sector of the economy. This brochure is based on the presentations delivered at the hearings by experts in particular fields.

The first seminar took place in Ljubljana, Slovenia, in March 2008. The topic was industrial transformation in that country, the Czech Republic and Bulgaria. Jože Mencinger, now professor at Ljubljana University and deputy prime minister and minister for economic affairs during the changes, tackled the economic transformation in his country. The Romanian experience was presented by the dean of the Faculty of Financial Management and Accountancy at Bucharest's Spiru Haret University, Professor Gheorghe Zaman. Transformation in the Czech Republic was covered by the rector of Prague's University of Economics and Management, Professor Milan Žák. The practical section scrutinised the effects of economic transformation on the chemical industry. The Czech Republic was represented by Josef Zbořil, member of the EESC/CCMI and of the Confederation of Industry of the Czech Republic. Samo Hribar Milič, general manager of the Slovene Chamber of Commerce and Industry, looked at his country's chemical industry. He was seconded by Vanda Pečjak, vice-president of the Association of Employers of Slovenia. She highlighted how the economic changes had affected Slovenian workers. The evolution and state of the Romanian chemical sector were described by the president of the Terapia independent trade union, Angela Pop.

Held in Budapest, Hungary, in April 2008, the second hearing dealt primarily with the economic transition in the host country, Poland and Estonia. The practical segment focused on the construction industry. The academic part was opened by Professor Péter Ákos Bod of the Faculty of Economic Policy at Budapest's University of Economic Sciences. He was trade and industry minister from 1990 to 1991 and governor of the Hungarian central bank and from 1991 to 1994. The changes in Poland were set out by Michał Górzyński, an economist at the Centre for Social and Economic Research (CASE). Alari Purju, professor at the Estonian Business School and former advisor to the minister for economic affairs, gave an insight into his country's experiences of economic transformation. Overviews of the situation in the building sector in the various countries were provided by János Nagy of Alba Geotrade Zrt, Edward Szwarc, Vice-president of the Polish Association of Construction Industry Employers, and Professor Roode Liias of Tallinn University of Technology.

The third hearing was held at the beginning of October 2008 in Sofia, Bulgaria. The headline issue here was the transformation of the industrial sector in Bulgaria, Lithuania, Latvia and Slovakia. Speakers were the director of the Institute of Economics of the Bulgarian Academy of Sciences, Mitko Dimitrov, and the director of the Institute of Economics of the Latvian Academy of Sciences, Raita Karnīte. Jekaterina Rojaka, Senior Analyst at DnB NORD Bank's Economic Research Unit, related Lithuania's experience and Jaroslav Vokoun of the Institute of Economics of the Slovak Academy of Sciences ran through the model of industrial transformation in Slovakia. Discussion in the practical section looked at the electrotechnical industry. Speakers here were Rumen Atanasov, President of the Bulgarian Association of Electrical Engineering and Electronics, Bronius Rasimavičius, President of the Lithuanian National Association of the Electrotechnical Industry, and Ján Oravec of the Slovak National Union of Employers. Jevgenija Stalidzane of the board of the Free Trade Union Confederation of Latvia and president of "Energy", the Latvian energy workers' trade union, set out the impact of economic transformation on Latvian workers.

1. From centrally planned economy to free market

Developments in the countries of Central and Eastern Europe at the end of the 1980s showed that centrally planned economies and communist societies were untenable. The unsustainability of a society managed along these lines ushered in fundamental and dramatic qualitative changes. Events made it imperative for these countries to transform their political and economic foundations. It was a period when society clamoured for political plurality, private ownership and a market-oriented economy. Time would reveal that the political system was relatively easy to rebuild. Changing to a market economy was incomparably more difficult.

It was a process unique in history. There was no road map for those fashioning the new economic reality. Each country had to choose its own path and how far and how quickly it sought to carry out reforms. These reforms had to take into account the position the particular countries were starting from – the level of development, the industrial makeup, the degree of centralisation and, not least, the mood of the country.

After the first years of transformation, participation in a new civil society as part of a broader European area became the overriding goal. In time, joining the European Union became the main aim of the reforms. This was crowned with success with the EU accession in 2004 of the Czech Republic, Estonia, Lithuania, Latvia, Hungary, Poland, Slovenia and Slovakia. Two years later, in 2006, Bulgaria and Romania followed them in joining the union of cooperation and prosperity in Europe that the European Union embodied.

The paramount aim of the transformation process was to restore the balance of a real economy. International division of labour, planned targets, relatively cheap raw materials and other inputs for industry and almost no competition: all of this had engendered an unwieldy, obsolete and labour-intensive form of industrial production. A new industrial structure had therefore to be installed which would take its place in a new competitive environment within the EU. The crucial element, then, was to transform industry as the economic backbone of these countries' development. Despite grave economic difficulties as transformation got under way, all the countries managed to raise their GDP in the course of time, mainly through pushing up industrial output. An influx of Foreign Direct Investment (FDI), which helped to boost their general economic ranking in the world, was another important engine.

Our prime goal here is to provide an overview of events in the new Member States during the last twenty years and to show what lies behind their success. The intention is to help readers who are not from the «Eastern Bloc» countries to understand the enormous efforts made by economic policy makers and society as a whole which led to the emergence of a normal market economy. Those who come from these countries will be able to compare the different guises the transformation process took. They will also discover whether some reforms could have been handled better and, equally, whether they had anywhere been an unqualified success.

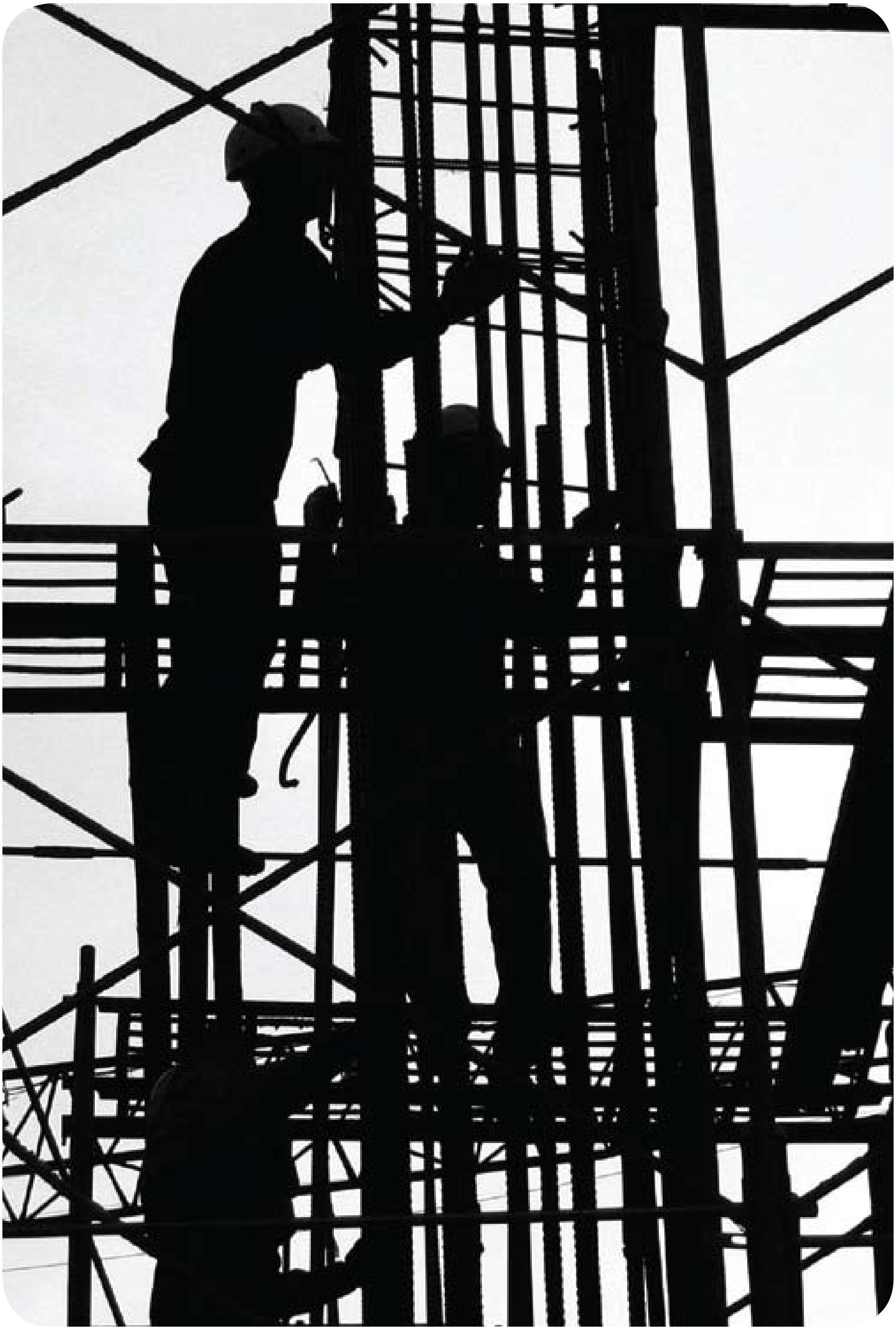
2. Different historical backgrounds

Each of the Eastern Bloc countries set out upon the transformation process along a different path. The way reforms were to be carried out depended on the measure of centralisation, the structure of the economy and how much support there was generally for its transformation. More than a half of the new Member States came into existence at the beginning of the 1990s and this was an important element in the process. These countries had to bring in their own changes and create the institutions that would direct the implementation of reforms.

What most determined the starting position was the degree of centralisation. On the one hand, there were countries such as Czechoslovakia, Romania and Bulgaria, which had entirely centralised economies. As part of the USSR, the Baltic countries were similarly placed. In these countries, all the means of production were in the hands of the state. It determined the volume and price of output, controlled the financial flows and shared out the profit. For forty years, there was no private sector. As a result, any entrepreneurial know-how and ability had almost died out. The economic changes in these countries were all the more difficult since an independent and decentralised network of small and medium-sized enterprises had to be created anew. On the other hand, we have countries such as Slovenia, Hungary and Poland. Here a partial private sector continued to operate and so the traditions of ownership had not been severed. It mostly comprised agriculture and small businesses, mainly in retail and services. Slovenia even had some large independent self governing companies.

There were manifest differences in the level of economic development and industry in these countries. In this respect, they fall into three categories. The Balkan countries Bulgaria and Romania had little developed industrial production to speak of, with most industry dating from the post-war period. New companies were often set up without any underlying economic concept. When they were built, scant attention was paid to whether there were sufficient raw materials or energy in the area. A major shortcoming was the lack of adequate connections between primary suppliers and the production of finished goods. Large plants were often built near labour forces and became their sole employer. The position of Central European countries such as Slovenia, the Czech Republic, Hungary, Poland and Slovakia differed slightly. They had inherited an advanced industrial sector from before the war which gave them a sound technological hinterland. Production was concentrated in industrial hubs with the necessary infrastructure. Output here had traditionally found markets in Western Europe. These countries built up a new post-war industry on a system of social planning. The Baltic countries had been one of the industrially and technologically advanced parts of the USSR. On the other hand, they were too small to compete very effectively in new markets.

The post-communist countries had to redefine their approach to foreign trade. Before transformation was launched, their economies had been interlinked within COMECON. They cooperated under a system of planned division of labour on an international scale. At the same time, however, there was a significant demand for both investment and consumer products from Western Europe. Liberalisation of foreign trade turned out to be the key lever of economic transformation. It triggered a sizeable boost in imports from Western Europe and, at the same time, a drop in exports to the COMECON countries. Despite the lower costs of domestic products, demand for them fell sharply. In these circumstances, companies opted to place their products in other markets, despite the greater difficulty in finding customers.



The arrival of new countries on the map of Europe was an important factor in the economic transformation of Central and Eastern Europe. The Baltic countries broke away from the USSR, Slovenia gained its independence from Yugoslavia and Czechoslovakia divided into two sovereign countries. The reasons for these scissions, however, were different. The Baltic countries had become part of the USSR in the 1940s following the Molotov – Ribbentrop Pact. At the end of the 1980s, Perestroika and economic transformation fuelled a desire for independence and they declared independence in 1991. Save for some minor hostilities in Lithuania in January 1991, they broke away peacefully. In Czechoslovakia, the situation was different again, with each part of the federation taking its own path to economic transformation. The problem came to head mostly because of disagreement about the principles, powers and status of the two republics and the federation. The political dimension of this "divorce" can be presented by not having a plebiscite. The communist regime in Yugoslavia was toppled at the start of 1990. Shortly afterwards, Slovenia and Croatia took their first steps towards independence. The Slovenians vote for it in a referendum and it was declared on 25 June 1991. A ten-day war broke out the day after. The Yugoslav People's Army moved into Belgrade after Slovenia had mounted stiff resistance. The battle then shifted to Croatia. Having secured their independence, these countries had now not only to tackle economic transformation, but also the additional challenge of creating the necessary institutions and introducing and stabilising a new currency.

If they were to embark upon the course of economic transformation, privatisation was inevitable. They also had to deregulate prices and foreign trade and ensure a freely convertible currency. The intention was for privatisation to create a big enough private sector and hence a competitive business landscape. Price deregulation was to address price imbalances in goods and services. One of the key requirements was to streamline the tax system and extend it to cover staples. The state also had to relinquish central price controls. Opening up foreign trade was likewise intended to boost competition. This, together with a freely convertible currency, ushered in free crossborder trade in goods and services.

Each of the post-communist countries embarked upon the transformation process in its own way. Poland and Czechoslovakia charted a radical reform path. Countries such as Slovenia opted for a gradual approach. Some, such as Romania, went for a combination of the two.

3. Different privatisation methods

The main task of industrial transformation was to reconfigure the ownership of the means of production. State-owned companies had to be turned into private firms to make them more efficient and supple. A new structure of small and medium-sized companies was created to this end. The post-communist countries differed markedly not only in the degree of centralisation, but also in the form of privatisation. Let us turn, then, to what privatisation looked like in the various countries.

In Bulgaria,

the process took off in 1992, with a number of methods being used. One frequently employed was "pool" privatisation. This involved selling off large concerns mainly to international privatisation agencies. These used the PATA programme, which operated on the basis of privatisation funds financed by the countries of the European Union. Alongside this programme, international consultancies funded by USAID and the World Bank also took part in privatisation. There were also public share offerings in state companies on the stock market. The privatisation agency arranged direct sales and auctions. Many SMEs were privatised through management-employee buy-outs (MEBOs). Individual ministries launched tenders to privatise small and medium-sized enterprises for which they were responsible. Privatisation vouchers were used for various transactions, including MEBOs. Competition was allowed between potential buyers with either cash or vouchers. Individuals could apply directly or through privatisation funds.

Privatisation kicked off in 1991 as part of a broad package of restructuring reforms put forward by the Czechoslovak government. It took three basic forms. Restitution sought to return property nationalised in 1948 to its owners and reinstate continuity of ownership. This served mainly to privatise small companies and real estate, including agricultural land. The aim of the small privatisation scheme was to create a network of SMEs in craft industries, retail and services. This decentralised the large national networks to which these undertakings belonged at the time. Privatisation of small companies was effected primarily through public auctions and tenders. The large privatisation scheme was used for big industrial companies. Resting primarily on vouchers, it stimulated the capital market and sought to show the public how such markets worked. Once vouchers had been distributed, a two-tier capital market was created. One level was the stock exchange, the other the RM systém company and the securities exchange. This market was to enable trading in the shares of companies that could not be listed on the stock exchange.

In Estonia,

privatisation took three forms. Firstly, ownership was extended to as much of the country's population as possible through redistribution. Then, restitution returned as much confiscated property as possible to its original owners or their heirs. Another step was the reform of ownership to create an environment conducive to production. Privatisation came to an end in the country in 2000. Most of the companies were sold in open tenders, the method chosen by the authors of transformation to find key owners for industrial enterprises. The new owners could come from any country. Only a minimum of shares was sold using vouchers. In the main, there was no right to transfer property to workers or employers. Small companies were privatised in the small privatisation scheme, which began in March 1991. The prime instruments were direct auctions, sale of property to insiders, competition based on business plans or sales of shares in property.

In Hungary,

The privatisation process also falls into three stages. The first was the spontaneous privatisation of the years 1989 – 1990. Here private interests were favoured and the period was one of rampant corruption and scant transparency. This detrimental course was reversed in 1992 with the foundation of the Hungarian State Holding Company. A number of preferred schemes were implemented and property was even given away. The most frequently used instrument was the "existence loan", which Hungary's citizens could take out at commercial banks and which had a rate of interest below the level of inflation. These loans could then be used to buy state property. The entire privatisation system in the country changed in 1994. The coalition of liberals and socialists set out a clear philosophy for the process. This consisted in an accelerated liquidation of state assets by selling for cash in a bid to entice foreign investors. The final stage of privatisation was launched in 1998, by which time only troubled companies remained in state ownership. It was given a fillip by efforts to cut the public finance deficit.

Latvia

made a conscious decision to rule out citizenship as a criterion for privatisation. Any individual or company was allowed to buy state property. Privatisation was to be achieved by selling off property and nothing could be transferred without payment. Direct sales and vouchers were the prime methods. The latter were introduced in 1992 and permitted owners to acquire companies, shares in them, or real estate. Workers could acquire at most 20% of shares in a company using privatisation vouchers. In exceptional cases, management could acquire up to 25% of shares. The state retained a certain stake in companies that were of strategic importance.

In Lithuania,

vouchers were the main method of privatisation. Unlike Czechoslovakia, where these were used as securities, in Lithuania they could only be passed on to relatives. They were used not only for privatising companies, but also for housing and land. 60% of industrial companies were privatised using investment vouchers. The rest of the property was sold for cash.

In Romania,

three particular techniques dominated privatisation: manager-employee buy-outs (MEBOs), the Mass Privatisation Programme (MPP) and the sale of share packages to outside entities. From the outset, the plan was to mainly use sell-offs to privatise, even though the law on privatisation had endorsed the MEBO method, since it favoured managers and workers. The Mass Privatisation Programme was adopted only in 1995, when a greater effort to speed up privatisation was announced.

In Poland,

privatisation got under way in 1990. The main stress was on ensuring it was done not only quickly but also well. Two primary goals were pursued – systemic and economic. The systemic aim was to bring about a change in ownership. The economic aim focused on making privatised companies more efficient. Three main privatisation techniques were used. The indirect (capital) approach was based on turning state-owned organisations into companies. The state coffers could then sell the shares of these companies through public offers, tenders, invitation and open negotiation. The second method was direct sales. These were used mainly for privatising SMEs. The state did not dictate what legal form these companies should take. They could privatise by selling the whole operation, by transferring company assets or by selling to the employees. Investment vouchers were one means used in mass privatisation.

In Slovenia,

privatisation focused on transforming state holdings into independent companies. The main tool here was the “privatisation equation”: $(10 + 10 + 20 + (1\text{-}x)*40) + (20 + x*40) = 100$. Ten percent was moved into a pension fund, a further ten percent into a restitution fund and twenty percent went to the workers concerned. Forty percent remained in public hands or was transformed using a value put on a parameter x. The remaining twenty percent went into a development fund. At the heart of the system was the value attributed to the parameter x, which determined how much was left in public ownership. For small and prospering companies, x was set at one, meaning that the whole forty percent was privatised as an independent company by managers and workers. For large faltering companies, the value of x was set at nought, meaning that the state retained the whole. For other companies, the value was set somewhere in between and these were privatised using vouchers.

the privatisation scenario had been written at the very start of the transformation period, when it was still part of Czechoslovakia. The aim of restitution was to share out property confiscated from original owners by the socialist government. The small privatisation scheme sought to bring into being a large group of small and medium-sized manufacturers and services, while the large privatisation scheme was to transfer ownership of large concerns. Vouchers were the main method used in the latter. The first wave began in Czechoslovakia in 1991. A systematic change occurred, however, once the country had split. Privatisation through vouchers became privatisation through bonds, with vouchers being replaced by government bonds which could then be used to purchase shares on the capital market. Most companies slated for privatisation in the second wave were sold off directly and the public favoured redeeming matured bonds. The point of this move was to create a strong tier of wealth-creators in the country. The meagre influx of foreign capital meant that only a few companies went to foreign buyers in the years 1993 to 1998. However, the rules on privatisation changed in the latter year, significantly boosting support for strategic foreign investment.

The various privatisation techniques have three common denominators. The first is restitution, which returned confiscated property to original owners. This sought to offset at least in part the wrongs perpetrated at a time of compulsory nationalisation and restore continuity and property rights. In many instances, however, the property returned had only a residual book and economic value. The small privatisation scheme, mostly in the shape of direct sell-offs and auctions, was intended to create a broad palette of small and medium-sized companies.

There were major differences in how large companies were privatised. These lay primarily in the degree of management and worker involvement. In countries such as Slovenia and Romania, most companies were privatised using MEBO, whereas this was the exception rather than the rule in the Czech Republic and Slovakia. The approach to privatisation by foreign capital also differed. Whereas the Baltic countries opened up to foreign investment from the outset, the countries of central Europe focused on creating a domestic wealth-creating tier and set store in protecting domestic investors.

While privatisation succeeded in redistributing property, it also had its drawbacks. These often involved extreme decapitalisation and deindustrialisation. In many cases, turning a quick profit came before any attempt to sustain company growth. New owners were prone to asset stripping. Sadly, it was in countries where preference had been given to domestic buyers that this happened. Czech commentators on economic transformation referred to this as "tunnelling". The inexperience of new managements in running companies in a market economy and worldwide competition led to deindustrialisation. Low labour productivity and waning demand for domestic products at home jeopardised the performance of companies. The introduction of competition mechanisms itself made for difficulties. The cost of raw materials and labour soared, leading to higher final costs. This bit into the competitiveness of goods on foreign markets. Poor transparency and corruption often plagued the privatisation process. In many cases, foreign investors privatised only to wrest control of the market and then shut down the company they had bought.

Although these privatisation methods differed from country to country, the result was almost the same. Everywhere, a strong private stratum was created. In some, however, such as Romania and Slovenia, state ownership still plays an important role. Although some countries strongly favoured domestic owners, over time they also allowed foreign entities into their markets. All in all, privatisation was a success in the end: not, however, in terms of ensuring an equable redistribution of property, but in creating a significant private sphere with substantial market potential. The key policy for industrial change was to create a sound competitive environment. Market forces and the attitude of new owners ensured the demise of companies that were not viable in such an environment. On the other hand, promising companies emerged that joined forces in the new economic reality and became very sound and competitive entities.

4. Foreign direct investments restructured the economy

Economic transformation had to include the transformation of manufacturing processes, which were in the main outdated. Many companies required an influx of new technologies and managerial skills. Privatisation by domestic owners merely redistributed ownership, thus creating a new tier of owners of manufacturing capacity. It did nothing to improve it. There was still a lack of physical capacity in the company sphere and the banking sector. Companies were hard put to secure loans or other external sources to transform their technological infrastructure. In many instances, new proprietors were allied with political groupings and had no clear idea how to run a company. International cooperation offered a way out. Strategic foreign partners and foreign direct investments were given the go-ahead.

The main precept of foreign direct investment is to attract real capital[1], new technologies, managerial skills and markets. Not all countries were willing to open their investment markets to foreign investors. Nor were foreign investors immediately enamoured of all countries. However, two types of investments can be generally distinguished: privatisation investments and acquisitions and green-field investments.

When it came to the former, people often expected nothing but benefits and they were confounded by what actually happened. Those behind the new economy hoped in the main for new technologies, management methods and markets. This was naturally associated with increased labour productivity and improvement in production, leading in turn to fewer jobs and often unpopular changes in the manufacturing process. Since most of the new owners were international companies, improving manufacturing processes involved division of labour at the level of large networks. Foreign investors often used domestic companies to penetrate the market in question, thus shoving up imports.

1. The actual finances of the new owner

Employment shrank as labour productivity increased. In the socialist system, production had been labour-intensive because labour was cheap. Superfluous jobs had been created to realise the idea of full employment. The new owners decide to remedy such unwelcome phenomena and banish "hidden unemployment" from their companies.

Many new owners opted to focus uniquely on core areas of production. In the socialist period, large enterprises had been established that produced a broad range of goods and provided a raft of services. These companies had an extensive horizontal structure. They provided not only a diversified product range, but also in-company services such as cleaning, maintenance and transport. New owners pared down the structure of the organisation and dispensed with redundant production. This they hived off to small and medium-sized companies and subsidiaries. They reconfigured their choice of supply companies to extract maximum benefit.

Quite often, foreign owners abused their position in the domestic market. They capitalised on the great demand in the post-communist countries at the start of transformation for products "made in the west". New owners took over the entire production and marketed it under their own brand. People ended up buying the same product as before, but with a different and more appealing label. As a result, domestically owned companies seeking to preserve their brand had less demand for their products.

Despite these downsides, at the end of the day foreign investment was a success. The post-communist countries attracted investment with low labour costs, skilled workers and, not infrequently, direct government support, though this was not always effective enough. This investment built up manufacturing companies in the countries in question. New jobs and production capacity were created. It brought new technologies and greater added value into manufacturing. It also boosted the output of suppliers and subcontractors.

Each economy had a different attitude to foreign investment. While Slovenia and the Baltic countries opened up to it at the very onset of transformation, the Czech Republic and Slovakia initially turned their backs. Over time, however, these more introverted countries also came to have higher expectations of such investment and they began to look for strategic partners for their companies.

Let us turn to the investment timeline. The start of the transformation process was dominated by portfolio and privatisation investment and acquisitions. Many foreign companies first put their capital into post-communist countries and then cautiously edged into new territories. Green-field investment only began once the economic and political environment in these countries had stabilised and the process of EU accession was underway.

Direct investments also differed as to their country of origin. Geographical, historical and industrial considerations were paramount here. The Scandinavian countries were very active in the Baltics. In central Europe, the biggest investors were Germany, Austria and the Netherlands. The Balkans attracted a lot of investment from the countries of Western Europe.

5. The industrial policy agenda

Economic theory recognises two types of industrial policy. Direct industrial policy refers to exerting influence directly upon industry as such. This policy's instruments focus on developing a certain sector of industrial output. The second type of industrial policy impinges upon economic processes indirectly. Its instruments foster a favourable economic environment for industrial production to flourish.

The first type of industrial policy was used only rarely during economic transformation. In many countries in transition, a particular industry or sector of the economy served to preserve social harmony. This was mostly where the unions were strong or the production process was heavily reliant on manual work. The main sectors here were mining, energy and railways. They were only marginally affected by transformation and the main aim was to safeguard them from substantial change. Governments sought to stave off privatisation and avoid the use of lay-offs to increase labour productivity. In organisations that were making losses on a large scale, programmes were introduced to wind production down gradually in a bid to minimise the social fallout. Natural wastage took precedence over dismissals. At the heart of the policy was a broad range of support, including covering company losses.

The second type of industrial policy was more commonly employed during the transformation period. It was geared to fostering a conducive economic environment for industrial growth and involved setting up the appropriate institutions and legislation for a normal competitive environment.

By introducing standards, legislation safeguarded ownership, equality of opportunity, free-market behaviour and free domestic and foreign trade. Legislation also protected economic competition, as did institutions overseeing the soundness of the competitive environment and consumer rights and protection. A raft of legislation came into force to govern respect for the environment. A well-functioning financial sector emerged, without which the business environment could not have worked. The banking system in each of the post-communist countries was stabilised so that it could provide loans and thus help industry to develop. Introducing new currencies and maintaining their strength played a large part in the growth of national economies.

When the post-communist countries embarked upon economic transformation, nobody knew what their future would be. Transparency was poor and opportunities were abused. Then again, such things are common at times of change. After the initial years of seeming chaos, the situation settled down. The new economic reality is one of prosperity and growth. From the long-term perspective, economic transformation has been a success. Market forces have sent to the wall only those companies that were incapable of surviving in the new economic reality. On the other hand, the industrial sectors that survived are competitive and contribute to the economic growth of the whole of the European Union.

6. Demand for skilled workers remains

Economic transformation and qualitative changes in the economy have inevitably been reflected in the labour market. This is radically different from what it was under a centrally planned economy. At that time, the right to work meant in effect an obligation to do so. The centrally planned economy was one of full employment. This inevitably meant overstaffing, hidden unemployment and low labour costs. The economic transformation put the spotlight on labour productivity and the efficiency of invested resources. The labour market had to respond to supply and demand. Unemployment was a new phenomenon in the post-communist economies and a major downside of the economic transformation. Social protection and support instruments had to be introduced in consequence. A range of instruments was thus brought in to stimulate employment and offset the hardships of redundancy.

Table 1

Selected population indicators

	Total population (in thousands)			Economic dependency index			Economic dependency index (young people)			Economic dependency index (elderly)		
	1990	2000	2007	1990	2000	2007	1990	2000	2007	1990	2000	2007
BG	8 767	8 669	8 595	88,4	80,1	75,9	52,3	41	34,9	36,1	39,1	41
CZ	10 362	10 305	10 313	89,8	71,3	70,5	56,3	40,1	35,3	33,5	31,2	35,2
EE	1 571	1 568	1 555	86,3	87,8	79,5	54,6	48,5	40,4	31,8	39,4	39,1
LV	2 668	2 658	2 643	84,3	86,7	77,8	52,3	47,5	38,5	32,1	39,2	39,3
LT	3 694	3 702	3 706	85,4	87,5	79,2	55,8	51,8	42,6	29,6	35,7	36,6
HU	10 375	10 373	10 374	88	77,7	75,3	52,5	41,9	37,5	35,5	35,8	37,8
PL	38 038	38 183	38 309	90	81,2	68,6	62	51,2	39	28	30	29,6
RO	23 211	23 192	22 810	90	82,6	72,8	60,6	48	39,3	29,4	34,6	33,5
SI	1 996	2 000	1 999	77,8	73,1	69,1	50,1	40,2	33,7	27,7	32,9	35,4
SK	5 288	5 311	5 296	93,2	77	66,4	64,7	49,7	39,2	28,5	27,2	27,2
Total	**105 963**	**973 105**	**105 602**									

Source: Eurostat

The European Union enlargements in 2004 and 2006 swelled its population by more than 105 million people from countries that had undertaken economic transformation. Romania and Poland were the most populous. Slovenia and the Baltics added least to the EU population. Generally speaking, population trends in these countries are stable. As in the other European countries, the population is gradually ageing. This is clear from the degree of economic dependency. That for the elderly contributes more to the overall growth of this indicator than that for the young. This means that a gradual convergence in population trends can also be expected in the new EU countries.

Table 2

Selected labour market indicators

	Employment (in thousands)		Rate of growth (2000-2007)	Unemployment level (%)					
				Total		Men		Women	
	2000	2007		2000	2007	2000	2007	2000	2007
BG	2794,7	3252,6	16,4%	16,4	6,9	16,7	6,5	16,2	7,3
CZ	4681,3	4922	5,1%	8,7	5,3	7,3	4,2	10,3	6,7
EE	572,5	655,3	14,5%	12,8	4,7	13,8	5,4	11,7	3,9
LV	943,7	1118	18,5%	13,7	6	14,4	6,4	12,9	5,6
LT	1404	1534,2	9,3%	16,4	4,3	18,6	4,3	14,1	4,3
HU	3829,1	3926,2	2,5%	6,4	7,4	7	7,1	5,6	7,7
PL	14525,7	15240,5	4,9%	16,1	9,6	14,4	9	18,2	10,4
RO	10652,8	9353,3	-12,2%	7,3	6,4	8	7,2	6,5	5,4
SI	900,7	985,2	9,4%	6,7	4,9	6,5	4	7	5,9
SK	2101,6	2357,7	12,2%	18,8	11,1	18,9	9,9	18,6	12,7
Total	**42406,1**	**43345**	**2,2%**						

Source: Eurostat, VZPS (LFS)

The labour market in these countries has undergone radical transformation, with marked improvements over the past seven years. Economies have seen growth stabilised, helped in large measure by indications of success in EU accession. All the countries saw employment rise during this period, with the sole exception of Romania, which recorded a 12% drop in labour demand and so bucked the general trend. Most progress in employment growth was registered in Lithuania and Bulgaria. The lowest unemployment rates for those of working age are in Lithuania and Slovenia. There are significant differences in employment rates between the sexes in several countries, with the Baltic countries showing a positive trend regarding equal employment levels. In Latvia, joblessness is actually higher among men than women. The labour market has made significant progress in recent times, despite serious difficulties at the outset, and employment is now increasing, which is a clear sign of economies developing on the right lines.

Table 3

Changes in employment structure according to NACE
(absolute differences 1998 – 2007, in thousands)

	BG	CZ	EE	LV	LT	HU	PL	RO	SI	SK	Total
A+B	-52	-91	-26	-77	-126	-87	-480	-1897	-12	-82	-2930
C	-7	-32	n.a.	n.a.	n.a.	-11	-44	-94	-4	-19	-206
D	91	65	2	-18	-20	-42	261	-332	-19	61	48
E	2	-21	-7	-3	-11	-35	-46	-64	2	-13	-194
F	132	-25	36	73	72	105	29	234	8	33	696
G+H+I	142	-34	13	77	71	167	351	170	18	73	1047
J+K	87	107	17	49	37	125	405	127	27	79	1060
L-P	77	131	12	26	20	64	234	111	53	28	757
Total	**472**	**100**	**41**	**132**	**48**	**286**	**711**	**-1744**	**74**	**159**	**278**

Source: Eurostat

Table 4

Composition of unemployed according to NACE (% of total)

	BG	CZ	EE	LV	LT	HU	PL	RO	SI	SK	Total
AB	8,1%	4,7%	6,4%	6,2%	14,1%	13,1%	19,1%	35,2%	12,9%	5,6%	17,8%
C	1,2%	1,4%	n.a.	0,6%	0,5%	0,7%	2,1%	1,4%	0,6%	0,9%	1,4%
D	25,2%	37,3%	27,8%	30,3%	23,6%	19,6%	26,9%	25,1%	36,0%	35,5%	28,1%
E	2,0%	1,9%	2,0%	2,1%	2,3%	2,5%	1,8%	2,2%	1,4%	2,3%	2,0%
F	9,6%	11,9%	16,7%	11,4%	15,1%	15,0%	9,0%	8,6%	7,9%	13,3%	10,1%
G-L	29,6%	30,7%	35,0%	36,5%	35,9%	37,8%	30,0%	22,6%	29,0%	31,7%	29,4%
M-Q	24,4%	12,1%	12,2%	12,8%	8,6%	11,3%	11,2%	4,8%	12,2%	10,8%	11,1%

Source: Eurostat

Table 5

Change in gross added value according to NACE
(mil EUR, change 1998 – 2007)

	BG	CZ	EE	LV	LT	HU	PL	RO	SI	SK
A+B	354	7658	7179	4078	5349	11742	2186	1762	272	8927
C+D+E	2657	14081	13243	6996	13334	12741	5808	9035	12051	14194
F	3149	7464	8115	5743	7287	4693	7835	12016	16302	7614
G+H+I	3076	13910	13415	11246	12231	8228	7141	10404	12640	13256
J+K	5176	20042	30794	26167	21090	24137	5031	25648	20655	19819
L-P	2032	9081	8490	7075	4959	11068	5053	8082	6399	8307
Total	**2929**	**12854**	**13172**	**10366**	**10458**	**11953**	**6351**	**8493**	**11846**	**12795**

Source: Eurostat

Table 6

Structure of gross added value (as a % of total)

	BG	CZ	EE	LV	LT	HU	PL	RO	SI	SK	Total
A+B	6,2%	2,4%	2,8%	3,3%	5,3%	4,0%	4,3%	7,5%	2,0%	2,9%	4,3%
C+D+E	24,1%	32,6%	21,3%	13,6%	23,3%	25,0%	23,2%	26,4%	27,5%	30,3%	25,8%
F	8,2%	6,3%	9,1%	8,4%	10,0%	4,6%	7,9%	10,3%	7,0%	6,7%	7,6%
G+H+I	24,4%	24,6%	26,9%	33,0%	31,5%	21,8%	27,9%	26,0%	22,5%	26,6%	26,2%
J+K	22,0%	17,3%	23,3%	23,5%	14,7%	22,6%	18,4%	14,9%	21,6%	17,8%	18,5%
L-P	15,1%	16,8%	16,6%	18,2%	15,1%	22,0%	18,3%	15,1%	19,4%	15,8%	17,7%

Source: Eurostat

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The way the structure of the labour market evolves is critical for transition economies, since it mirrors changes in the structure of the economy as a whole. In agriculture, the increase in labour productivity, the drop in output and even the sector's partial collapse in some countries was reflected in a slump in jobs in the sector. The extraction industry was also hit by plummeting output following the closure of loss-making enterprises. This impacted adversely on the total number of workers in this branch. When it comes to the processing industry, there are stark differences between countries. Demand for labour in Romania, for example, was worst hit by economic transformation. Poland, by contrast, had the highest rise of employment in this sector. Market services, a branch that only began to emerge at the time of economic transformation, was the sector of the economy that notched up the highest growth. Much of this growth can be put down to outsourcing. While company services had been seen prior to transformation as part of the production operation, they later broke away and became separate service entities.

Despite the fact that employment trends indicate a major step forward, joblessness remains a serious problem. Changes in the structure of the economy are the main factor in unemployment trends. Many rural areas have witnessed a drop in labour demand in agriculture. Industry is also battling with problems. The open labour market in the European Union entices capable young professionals to seek work in more developed countries. Many of the new Member States are contending with a brain drain and, in some cases, an exodus of manual labour. This means they will soon be facing a new problem: lack of skilled labour for some sectors.

8. Conclusions

We cannot do justice to the difficulty and complexity of the transformation process here. What we can say, however, is that on the whole developments in the countries of central and eastern Europe, in the Baltic countries and in the Balkans, brought about important changes in the very foundations of the economy at the beginning of the 1990s. The EESC's CCMI organised a series of seminars aimed at shedding light on how industrial policy affected the production sector. Each country had a different transformation script based on its position at the outset, the structure of its economy and the general mood of the population regarding the reforms. Three basic instruments for creating a new economic reality can be observed. Privatisation was intended to create a new structure of ownership in the economy. Then it was to create a favourable economic climate. Foreign direct investments provided new capital, technology, managerial skills and markets. In no country was the transformation process painless. Privatisation was often marked by poor transparency and corruption. On many occasions, personal interests were put before the prosperity of all and sustainable growth. In some instances, foreign investment led to a slump in output and demand for labour. No country went through the transformation process unscathed. Now, however, each has many benefits to show for it. Despite the pain it involved, the transformation period had its positive role to play. This is a success story proven by the accession of these countries to the European Union. Normal economies and prosperous development are part of that story.

General information on the Consultative Commission on Industrial Change (CCMI)

The role of the European Economic and Social Committee (EESC) in promoting a structured dialogue on industrial change in the EU

The European Economic and Social Committee's Consultative Commission on Industrial Change (CCMI) combines over 50 years of experience with consultative dialogue gained from the European Coal and Steel Community's Consultative Committee with a wide-ranging composition and remit to produce a body unique to the European institutions. It is a new kind of model for discussion/dialogue of policy issues between different actors in the field of industrial change.

The CCMI looks at industrial change issues across a wide spectrum of sectors. As such, it offers added value to the work of the EESC as a whole. It is of particular value to those new Member States currently undergoing the process of industrial change and its new composition, created at the end of 2004, reflects this fact in the form of significant representation from these countries.

The CCMI is more than just a repository of lessons learnt in the past. In keeping with the subjects it treats, the role of the CCMI is to look to the future. The emphasis is on anticipation, pre-emption and analysis so as to ensure positive common approaches to the management of industrial change from an economic, social, territorial and environmental point of view. The CCMI promotes co-ordination and coherence of Community action in relation to the main industrial changes in the context of the enlarged EU and advocates balance between the need for socially acceptable change, environmentally sustainable production and the retention of a competitive edge for EU industry.

Background

In view of the expiry of the ECSC Treaty on 23 July 2002, the Industry Council of 18 May 2002 asked the European Commission to submit its ideas on the future of structured dialogue in the areas covered by this Treaty.

In its Communication of 27 September 2000 (COM(2000) 588 final), drawn up in close consultation with the EESC, the Commission proposed the creation of a specific structure within the Committee that would not only permit the retention of valuable expertise built up during the ECSC years and the continuation of structured dialogue in the areas of coal and steel, but would be expanded gradually, ultimately to cover all issues relating to industrial change in an enlarged EU.

Creation

With regard to the content of this major extension of the EESC's consultative role, the Commission stresses its *"determination to examine the development of ECSC structured dialogue in a firmly future-based perspective"*. The ECSC's unique "*experience - notably in the fields of social consensus, industrial restructuring and research - will enhance the EESC's ability to play an active role in modernising the European economy and making it more competitive"*[2].

The other European institutions supported these proposals and provided the EESC with the resources needed to run this new body, which was set up on 24 October 2002 by the Committee's Plenary Assembly.

Composition

The CCMI is made up of 48 EESC members and 48 external delegates, drawing on a wide range of knowledge and experience gained in a variety of socio-occupational organisations in various sectors affected by the modernisation of the economy. The Chairman of the CCMI is a member of the EESC and the Co-Chairman is a delegate. The delegate body is divided into three categories (employers, employees, various interests), similar to the structure of the three EESC groups. Following the enlargement to 27 Member States and given the particularly appropriate nature of the CCMI's expertise to the new Member States, the new CCMI composition includes a high proportion of members and delegates from these countries.

2. COM(2000) 588 final

Mission

The creation of the CCMI opened up new avenues. The EESC is now able to draw up opinions as part of a direct structured dialogue between its members and representatives of the sectors and interest groups affected by industrial change. This permits the examination of problems in all their complexity – from an economic and social angle, in relation to environmental protection or sustainable development. They are dealt with as part of the normal EU decision-making process by means of referrals from the institutions (including requests for exploratory opinions) or own-initiative opinions, which the Committee believes are necessary to influence developments in the EU.

Remit and means of setting out its views

The CCMI's remit:

- continues to cover those areas of the coal and steel industries and their production and consumption chains in which the Community is active;
- has been progressively extended to the handling of industrial change in other sectors of activity and its repercussions on employment, social and structural policy measures, aid and competition policy, research and technological development, environmental and sustainable development policy, energy policy, trade policy;
- includes a particular emphasis on the challenges posed by industrial change in the new Member States.

The CCMI can express its views through mandatory opinions under the terms of the Treaty, optional and exploratory opinions at the request of the European Parliament, the Council and the Commission, as well as own-initiative opinions, information reports and the holding of conferences and hearings.

It maintains a close working relationship with the other EU institutions and agencies and with organisations across the whole range of issues linked to industrial change.

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In 2008, the EESC's CCMI held a series of seminars aimed at garnering information about the major milestones in the change of economic principles in the countries of Central and Eastern Europe. The prime aim was to pinpoint the key political and economic decisions that put in place the industrial structure these countries have today. In this brochure you can read the conclusions of the seminars.

European Economic and Social Committee

˝Visits and Publications˝ Unit

For further information, please contact:

Rue Belliard 99
1040 Bruxelles/Belgique
Tél. +32 25469604
Fax +32 25469764

www.eesc.europa.eu

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