THE PRIVATIZATION PROCESS IN KOSOVO: PERFORMANCE OF SOCIALLY OWNED ENTERPRISES

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Abstract

Privatization has been ongoing for the last decade and continues in many countries. The importance of privatization as part of government policies concludes with the most empirical studies as an essential process to move from a centrally planned economy to a competitive market economy, and firms that underwent the process improve after the privatization. However, few studies have measured the performance of firms after the privatization process in Kosovo. This privatization process in Kosovo followed three important privatization methods, spin-offs, special spin-offs, and liquidation. The companies privatized through the spin-offs were sold to the highest bidder. However, selected companies through special spin-offs were considered companies with a high economic impact and employed many employees sold through contracts.

The study sample consists of 24 socially owned enterprises privatized in Kosovo. Therefore, we examined their overall performance using the methodology from the existing literature. Therefore, results will be consistent with our hypothesis that firms with extended planning and stable environment improve faster in their overall performance.

Keywords: socially owned enterprises; privatization; United Nations Mission in Kosovo;

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Introduction

During the last millennium, privatization started to emerge in developed countries. Furthermore, this process followed in the new millennium as an economic practice to move faster from a centrally planned economy to a market economy. Additionally, Kosovo was introduced to the privatization process following massive support from the World Bank, IMF, and EU. The privatization process in Kosovo followed many disputes following the disputes with Serbia claiming ownership of the SOEs. However, the process started in 2003 and is continuing, and in 2021 was stopped following the arrival to power of the extreme rights.

Therefore, the privatization process in Kosovo can be pre-defined in two eras, the UNMIK era and the post-UNMIK era, since after 2008, the country declared its independence. Therefore, the economic reforms in Kosovo started in 2003, and firstly it was closely monitored by UNMIK following the 12/44 resolution, but after 2008, Kosovo was fully independent and started its economic reforms.

The privatization process in Kosovo accounted for around 500 SOEs after the devastation; only one-third were fully operational. The SOEs were fully operational during the 1980s, but following the events of the 1990s that will be explained later, followed by the deprecation of assets and technologies and the changes happening in the region, left these enterprises with limited capacity or fully closed. After the 1999s war in Kosovo, the UN ruled the country following Resolution 1244 according to Security Council Resolution. Following the direction of the World Bank and many other institutions, UNMIK started privatization as early as 2000. However, soon the process was halted following the disputes for ownership.

This study examines the success of privatization on firm-level performance during the period from 2003 to 2021. Our sample includes companies privatized with the special-spin offs. This study will use the same methodology used in Megginson, Nash, and Van Randenborgh (1994); in the end, we will use the results of this study to analyze firm-level performance.

1 Privatization in Kosovo

Kosovo gained independence on 17 February 2008 but had a long history of politics and wars. For the first time, Kosovo gained autonomy in 1963 while being part of the former Yugoslavia. Furthermore, in 1973 the autonomy of Kosovo gained more rights putting Kosovo on par with other countries under Yugoslavia, such as Serbia, Croatia, Slovenia, and Macedonia (Pavlovic, 2013). For that reason, Kosovo, since 1973, had its constitution, parliament, and other legal frameworks to function as a state. The socially owned enterprises under the former Yugoslavia were given to manage under the Socialist Autonomous of Kosovo (Pavlovic, 2013).

Additionally, all the changes happened to ensure a place for the Kosovars in the Socialists state of Yugoslavia. In 1989 with Slobodan Milosevic receiving power and leading the socialist party, Kosovo was stripped from all the benefits, and all the SOEs were transferred to Serbia (Brossard & Vidal, 2001; Malcolm, 1998). With the growing fear that Serbia would lose Kosovo same, like Slovenia, Bosnia, and Croatia, they started depopulating Kosovo and populating it with the Serbian population. These actions led to the well-known Kosovo War that lasted almost two years.

1.1 The UNMIK era (2000-2008)

The "peace-building and state-building" mission started operating in Kosovo when the war ended; their primary mission was to revitalize the country's economy since it has been facing a decade of violent protests and wars (Knudsen, 2010). In 2000, almost all the SOEs in Kosovo lacked funds to operate, and essential information about them was taken from the archives in Serbia (Mulaj I., 2007). The classic solution to this was privatization since it would bring revenues to the government, decrease the budget deficit, and help them save money. In return, the SOEs will be sold to interested investors, which will help them revitalize, increase efficiency, increase competitiveness in the market, and, most importantly, have direct access to investment funds that were highly needed.

Therefore, with the advice of international institutions, respectively World Bank, IMF, USAID, and UNMIK, several reports were published concluding that the only approach to the revitalization of the economy of Kosovo was privatization. World Bank published several articles indicating that it favors privatization and encouraged UNMIK to start the necessary work to proceed with it (World Bank 2001a). World Bank (2001b) indicated that it supports the UN to create the legal framework so that the country's economy can transition to a private-based economy.
Furthermore, general and specific arguments were published that supported the process of privatization in Kosovo. Starting with the financial funds from privatization, Foreign currency and attracting foreign investors.

Next, the economic professionals argued that it would help economic growth, effectiveness, and competitiveness and maximize the profit of enterprises because SOEs needed an influx of funds (Dobra B, de Vries S M, 2016). The social arguments were that privatization would restore and hand out state property to the entire population, thus increasing employment and reducing the power and pressure of the government (World Bank, 2001b). Furthermore, the political arguments suggested that privatization would reduce the influence of the state, and Kosovo would consolidate itself as a fully democratic country with an open economy.

Lastly, the most potent argument was that privatization would help create a free market that would reduce the influence of the state. The UNMIK started preparing the legal framework and planning for privatization by combining several methods used by other countries that already went through the privatization process (KIPRED 2005). The UN administration and the international institutions were convinced that privatization in Kosovo was the only solution.

Therefore, in June 2002, these institutions created the Kosovo Trust Agency (UNMIK regulation 2002 / 12). They described the KTA as follows:

> *The KTA has been established to preserve or enhance the value, viability, and corporate governance of socially owned and public enterprises in Kosovo. For Socially Owned Enterprises, the KTA initiates 'Spin-off s' and Liquidation, its preferred procedures for privatization. (http://kta-kosovo.org/html/index.php)*

1.2 Methods of Privatization

Privatization was regarded as a saving grace for the development of the Kosovo economy; therefore, on 15 May 2003, KTA started with the transformation of SOEs into private enterprises. Even though the groundwork was laid and models of past privatization were analyzed, the board of directors decided not to follow past models used in CEE countries but proceeded with full privatization. KTA introduced the following methods: Regular Spin-Off, Special Spin-Off, and Liquidation. (KTA, SOE division, 2002)

1.2.1 Regular Spin-Off

The Regular Spin-Off introduced the tender rules, which involved that KTA could create new companies in the form of a Joint Stock Company or LLC and transfer to these companies part of all assets of the old companies. Liabilities would not be transferred but stay part of the old SOE companies. A certain amount of shares would be held by KTA so that a fair value would be received. The KTA also considers the proposed activities, investments, and employment as foreseen with the selling contract. Furthermore, Regular Spin-Off always chooses the highest offer. (KTA, SOE division, 2002)

1.2.2 Special Spin-Off

Special Spin-off is also another method of privatization used in Kosovo. It is special compared to the methods used in Europe. Therefore, compared to Spin-Off, the Special Spin-Off considers other conditions explained in the Rule of tenders, such as the number of employed persons, investment by potential investors, and continuation of the same activities. The investors are evaluated based on these criteria: 50 percent of the score from the offered price, 25 percent of the score investment, and 25 percent based on the job they offer. (PAK, 2008)

1.2.3 Liquidation

The last method KTA uses for privatization is directed to companies judged that their survival in the market is at risk. Therefore, KTA starts the procedures to sell immediately so that they can salvage the remaining value from these enterprises. KTA administers all revenues received by liquidation. This method in Kosovo has rarely been used. (KTA, SOE division, 2002) hence they feared that such practices would hurt the economy and employment. Post and Telecom of Kosovo remain under the state's management. The company has been declining in value because of many scandals, over-employment of family members involved in politics, and lack of investment.

2 Methodology

2.1 Research and Objectives

The theory of privatization is a widely spread practice used by developed countries to create new revenue streams. This practice was extensively used after the 1990s. With the fall of the centrally planned economy, transnational countries started moving to a market economy. Privatization as a model has had many methods that country has tried their best to be successful and move faster.

Kosovo, similarly to other countries, has gone through privatization to transition from a centrally planned economy during Yugoslavia to a market-share economy after the conflict that ended in 1999. Political issues in Kosovo have made the privatization process does not complete to this day. Therefore, since many factors play a role in Kosovo's transformation, it is interesting to assess whether the privatization methods used in Kosovo were successful.

Additionally, the main objective of this literature will be to assess the performance of the socially owned enterprise’s pre- and post-privatization. It is necessary to conclude that companies that were privatized with special-spin-off are the ones that can be considered. Furthermore, another interesting fact is that several large SOEs still are under the management of the government; therefore, measuring the performance of those that have gone through the privatization process will give us better insight into whether the privatization process was successful. Therefore, our main research goals will be:

- Assessing the impact of privatization on firm-level performance of the privatized socially owned enterprises pre- and post-privatization era.

2.2 Methodology

The methodology that will be used in our study is the Megginson (1994) that was used in many other studies. The basis of this methodology is to test the profitability, operating efficiency, capital investment, output, employment, leverage, and dividend to sales.

The first researchers to give us a deeper insight into privatization's effects on Megginson, W. L., Robert C., and Matthias V. (1994) analyzed a sample of 61 privatized companies from 18 countries. The data set covered a period from 1961-1989. The authors in their studies compared three years post-privatization and vice versa. They considered financial and operating ratios. The results from their empirical analysis proved their hypothesis. The companies in post-privatization had an increase in sales, efficiency, profit, and investment. Furthermore, the companies did not experience any labor losses; they had a 10% increase. Additionally, changes were seen at the managerial level, improving the company's performance. Therefore, according to empirical results from the study, privatization positively affects enterprises.

Similarly, D'Souza J. and Megginson (1999) used the same methodology to test companies that were privatized from 1990 to 1999; like the search above, the dataset of 85 companies concluded that an increase in sales, profit, and capital and no downsizing in labor the authors concluded that a competitive market helps companies faster recover and compete with other companies in a free market. Another study that used the Megginson methodology was Boubakri, N. and Jean, C. (1998). similarly, they concluded that in a competitive market, the companies experienced rapid growth, thus increasing the capital expenditures because of increased sales and total assets. The labor force was not affected and only showed a significant increase. Their methodology included comparing financial and operating ratios for three years in pre- and post-privatization.

The most important part of the dissertation is the methodology. According to Megginson (1994), most governments adopt different privatization methods with a clear understanding of what they want to achieve. Besides revenues, it is a clear indicator that privatization happens; privatization is implemented to improve operating and financial performance. The government expects the following results:

- Increase in profit
- Increase in efficiency
- Increase in capital investments
- Maintain the labor

From the literature review written below, we have seen that most studies have implemented the Megginson (1994) method. This method provides insight into the difference between pre and post-privatization firm performance. Therefore, the following chapter of this dissertation will lay down the groundwork of the research methodology and the procedures that will be followed to examine the overall performance of the company's pre and post privatized in Kosovo.

2.3 Data

Methods of privatization limit our research for future researchers. In the case of Kosovo, there is potential to analyze the companies privatized with spin-offs. We will examine the companies privatized with special-spin offs to have accurate results. Our data sample will consist of enterprises privatized between the periods 2003 to 2015. Therefore, our observation will be divided into three blocks: the pre-privatization period, the year of privatization, and the post-privatization period.

Furthermore, we will start by obtaining the PAK initial offering when it was privatized – which represents the financial position of these enterprises and years of financial data for these enterprises. Hence, it was more complicated after we obtained post-privatization data since companies did not want to cooperate. However, with the help of PAK, we obtained the annual reports for these companies; in some cases, it was limited. Furthermore, Kosovo is harder since annual reports are not listed in secondary sources.

By undergoing all the procedures to filtrate the data, we have obtained sample data from 25 companies. From our data analysis for the sample of 25 companies (PAK 2019). From our data analysis: 50% of the companies in the data sample are from the trade sector, 10.6% production sector, 34.9% service sector, and 4.5% are corporations, all privatized with special spin-offs (PAK 2019).

2.4 Research Methodology

Moreover, the analysis examined in this dissertation will indicate if there is a difference between pre-privatization and post-privatization periods. Therefore, we will use the Megginson (1994) method for this analysis since most studies have used a similar method. It will leave an open door for future researchers to compare the results of Kosovo with other countries from Eastern Europe. Therefore, we will use the same empirical proxies for each Kosovo enterprise for seven years. The seven years will be divided into three parts:

- Year 0 will be excluded since its pre- and post-privatization ownership.
- Years -1 to -3 will be the pre-privatization period.
- Years +1 to +3 will be the post-privatization period.

Table 1: Testable Proxies

Characteristics	Proxies	Prediction
Profitability	Return on Sales = Net Income / Sales	Increase
	Return on Assets = Net Income / Total Assets	Increase
	Return on Equity = Net Income / Total Equity	Increase
Operating Efficiency	Sales Efficiency = Sales / Total Employment	Increase
	Net Income Efficiency = Net Income / Total Employment	Increase
Capital Investment	Capital Expenditure to Sales = Capital Expenditure / Sales	Increase
	Capital Expenditure to Assets = Capital Expenditure / Assets	Increase
Employment	Total Employment = Total Number of Employees	Decrease
Leverage	Debt to Assets - Total Debt / Total Assets	Decrease
Dividend to Sales	Divided/ Sales	Increase

Source: author

Therefore, to test our methodology, we need seven years of data for each company to test our proxies. Therefore, we will take three years before and three years after the privatization and exclude the year the company was privatized because it includes both public and private. After computing the means, we will use the Wilcoxon signed-rank test to test the significance of changes in the variable.

2.5 Empirical Results

In this part of the research paper, we will discuss the results. The total sample of results consists of 25 firms privatized through the special-spin offs can be seen in the following table.

Table 2: Empirical Results

Variables	N	Mean Before (Median)	Mean After (Median	Mean Change (Median)	Wilcoxon Z-statistic	Percentage of Firms that Changed as predicted
Profitability						
Return on Sales	25	0.14 (0.07)	0.22 (0.08)	0.079 (0.01)	1.28*	0.69
Return on Assets	25	0.052 (0.05)	0.072 (0.06)	0.02 (0.01)	2.61***	0.72

Return on Equity	25	0.171 (0.16)	0.181 (0.175)	0.01 (0.015)	1.02		0.55
Efficiency							
Sales Efficiency	24	0.94 (0.90)	1.107 (1.135)	0.167 (0.235)	3.9***		0.8
Net Income Efficiency	23	0.606 (0.565)	1.234 (1.15)	0.628 (0.585)	3.47***		0.77
Capital Investment							
Capital Investment to Sales	25	0.25 (0.18)	0.28 (0.20)	0.03 (0.02)	0.8*		
Employment							
Total Employment	25	6,263	5,893	-370			1.0
Leverage							
Total Debt to Total Assets	23	-	-	-	-	-	
Dividends							
Dividend to Sales	20	0.0107 (0.0015)	0.0287 (0.02)	0.018 (- 0.0215)	2.76***		0.71

Source: authors

2.5.1 Profitability

Similarly to Megginson's methodology, the most significant change can be seen in the profitability of the companies we measured through the Return on Sales, Assets, and Equity. We can see a difference in the average (mean), showing us that firms post-privatization produced positive results in terms of profitability. From our sample, we can see that 69% of the firms experienced increased profitability. Furthermore, the z-score significant test suggests that the change is big enough for the results to be statistically significant.

2.5.2 Efficiency

In terms of efficiency, when we measured sales compared to total employment and net income compared to total employment, we can see that there is a significant increase in the average (mean) from 0.94 to 1.07 in terms of sales efficiency and 0.606 and 1.234 in terms of net income efficiency for the period 3-year before privatization and 3-years after the privatization, The results are big enough for the statistically significant. Furthermore, the results show a considerable increase in post-privatization gains.

2.5.3 Capital Investment

As explained above, the special-spin offs method of privatization is a method used for big companies given to new owners through negotiations; therefore, the capital investment in the company is positive because investors are obligated to invest a certain amount every year for the restructuring of the company Therefore, capital expenditures increased post-privatization because the company needed to invest in building and equipment since the companies had depreciated assets and technology because of the war the investors invest money for the company to fully functional.

2.5.4 Employment

As expected, post-privatization, the labor force in the company decreased. At the same time, this proxy was calculated through the number of employees when the company went into privatization and the number of employees that remained after 3-years of privatization. The amount of money invested in new technology by the employees reduced the number of employees in the company. Furthermore, further analysis suggests that during centrally planned economies, the companies hired employees without needing them; therefore, post-privatization investors new restricted companies and technological advancement needed fewer employees.

2.5.5 Leverage

Another critical piece of information is why the total debt compared to total assets was not calculated because of the special spin-off method used in Kosovo. The Privatization Agency in Kosovo, when selling a company through special spin-offs, creates a new company (newco) in the form of a joint stock company where all the assets of the old company are transferred. However, the liabilities of the old enterprise are not transferred to the new enterprise.

2.5.6 Dividend to Sales

Our analysis and the Wilcoxon test suggest that the changes are big enough for the results to be statistically significant, meaning the post-privatization dividend payments measured in our analysis increase.

Conclusion

This study compares the pre- and post-privatization companies privatized in Kosovo through the period 2003-2021 through the methods of special spin-offs. The data sample consists of 25 companies. Throughout our research, we managed to identify significant changes in profitability, efficiency, capital investment, employment, and dividend payment. Similarly to other authors, we got similar results. We document changes that proved our prediction when it came to the proxies that were being measured. Furthermore, we believe that total employment, as measured above, will decrease post-privatization, as concluded in other studies.

After conducting thorough research, it has become apparent that privatization in Kosovo has significantly impacted various aspects of the country's economy and society.

Specifically, selling state-owned enterprises to private investors has resulted in job losses, increased economic inequality, and limited public control over key industries.

Furthermore, the privatization process has been marred by corruption and lack of transparency, with some investors benefiting unfairly from insider information and connections to government officials. This has led to a perception among many Kosovo citizens that the privatization process has been unfair and has failed to deliver promised benefits.

Despite these challenges, some proponents of privatization argue that it has brought much-needed investment and expertise to Kosovo, helping to modernize industries and improve efficiency. However, the specific details of the privatization process in Kosovo must be carefully examined and evaluated to ensure that it genuinely serves all citizens' interests and promotes long-term economic growth. Research is essential for understanding important matters, including this study. By exploring this topic and discovering new perspectives, we can find solutions to challenges and narrow the problems or benefits of privatization on different topics. This research can influence future studies in this area. Ultimately, the insights gained can contribute to future research in conducting comprehensive and objective research to gain a more nuanced understanding of privatization and its role in shaping the future of a country.

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