German Economic Transition

Corporate Governance in the
Centralized Decentralization:
corporate governance in transitional economies
B. East Germany

Corporate governance and decision making in the transition period captured the essence of macroeconomic processes. It created a framework for the transition, but also highlighted the need for appropriate steps. In some respects, this analogy is inappropriate for the observed phenomenon; however, in other respects, it is both practical and relevant. The dual control system, as described by Jensen and Ruback (1983) and others, where the individual firm is the focus, and the corporate control as developed by Management (1995), Jensen and Ruback (1993), and others, are critical.

Corporation Governance in the German Economic Transition
Iernal Control of the THA: Below. Lh imply the consensus emerged in the subsequent legislative process. See "Ex-

Historically, the original law enacting the institution did not set a time

in 1945. In 1947, the Land reform, which nationalized all land holdings
large-scale nationalization of private property began in the Soviet Zone
Soon after the four zones in occupied Germany had been established.

Structure before 1999

Some Determinants of Economic

Forming economies:

mean of the relevance of the East German experience for other trans-
transition. The final section offers some interpretations and an assess-
agency. The sixth section describes the pattern of the privatization
a description of the external control mechanisms of the privatization
Governing issues during the transition process, and is followed by
half of the Berlin Wall. The fourth section analyzes in detail corporate
1999. The third section sketches the economic development after the
survey of the evolution of the corporate sector in East Germany before
This chapter is organized as follows. The next section gives a brief

A preliminary assessment of

the THA" below, describe these features in some detail and provides
limiting the pressure from public interest groups. (External Control of
given a high degree of independence from government and parliament,
agency's and its environment were limited. Second, the agency was
so that expected rents from long-term collateral between the
the public process exhibits two highly complementary features, which, I will
The institutional development in the East German privatization

interest groups under its supervision.

and Ilcul1993). A privatization agency is likely to be captured by the
by the firms they are supposed to regulate (see Slicker 1971 and Laffon
class control. Just as government regulatory agencies can be "captured"
Proportionately 30 percent of the total workforce of the GDR at that time, estimated to be about 20 million, were employed in industry and 20 percent in construction.

The data are based on the Statistical Register of Business of the GDR as of June 30, 1990, provided by the Wirtschaftskammer der DDR (Trade Chamber of the GDR).

For 90 percent of total employment in industry and 20 percent in construction, there were more than 2,000 employees, and a total of 4,000 employees had less than 500 employees, and only 17 percent of the employees were male. By June 30, 1990, there were 27 million people employed in industry, and the largest group of employees were economically controlled companies.

The most important were the 150 centrally controlled companies. The second largest were the 20 domestically owned companies.

In 1987, the remaining private companies (approximately 1,100) were divided into small and medium-size companies (TVA, 1993).

In 1972, the remaining private companies were divided into small and medium-size companies. In particular, the district governments (see Figure 8.1) were the primary decision-making bodies, but smaller units were usually overseen by the planning ministers. The larger companies were directly subordinated to one of the three main companies. The creation of large conglomerates through the combination of smaller companies was intensified through the creation of large companies, the concentration of the GDR (Deutsche Demokratische Republik, DDR).

From October 7, 1949, the constitution of the GDR (Deutsche Demokratische Republik, DDR) came into force, in 1950 the first five-year plan (Fünfjahresplan) was adopted, and in 1951 the ruling Socialist Party decreed the building of socialism. In 1955 more than 70 percent of the GDR's gross national product was produced by small and medium-size companies. In 1964, a three-tier pattern of state-owned enterprises (Unternehmensberatung, VEBs) was replaced by a four-tier pattern of people-owned businesses (volk- und bestimmungsmäßige Wirtschaft, VEBs).

From 1964 on, the central government planned and coordinated economic, regional, and social development. The government was the largest company. On October 7, 1949, the constitution of the GDR (Deutsche Demokratische Republik, DDR) came into force, in 1950 the first five-year plan (Fünfjahresplan) was adopted, and in 1951 the ruling Socialist Party decreed the building of socialism. In 1955 more than 70 percent of the GDR's gross national product was produced by small and medium-size companies. In 1964, a three-tier pattern of state-owned enterprises (Unternehmensberatung, VEBs) was replaced by a four-tier pattern of people-owned businesses (volk- und bestimmungsmäßige Wirtschaft, VEBs).

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Historically the emergence of the Kombinat coincided with the wave of conglomerate mergers in the Western World, in particular the United States, at the end of the 1960s (cf., for example, Schofer 1988).

Figure 8.1. Socialist Governance

Corporate Governance in Transitional Economies

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Truman's proposal was strongly opposed by the German Chancellor, Konrad Adenauer, and other West German leaders. However, the crisis in the West German economy and the threat of a political crisis in the West German government led to a change in West German policy. On November 9, 1989, the Berlin Wall wasfall, and on October 3, 1990, the GDR ceased to exist, joining the Federal Republic of Germany in the new German state. After 1989, the economic and political development of Germany was characterized by a rapid transition to market-oriented economic reforms and political liberalization. The former East German economy was highly centralized and inefficient, with a large state sector and limited private enterprise. While this was necessary to stabilize the transition, it also led to economic inefficiencies and a lack of competitiveness. The transition to a market economy was accompanied by significant economic hardship, but also by a rapid increase in economic growth and prosperity. The reunification of Germany presented both opportunities and challenges, and the process of integration continues to this day.
On July 1, the Treaty on Currency, Economic, and Social Union (GESA) between the two parts of Germany came into force. Under the agreement, a holding company was to be incorporated as a public institution according to West German law and designated in a decentralized fashion as possible. "The THA" was given the explicit task of privatizing the people-owned firms. The main purpose of the law was to reduce, by means of property privatization, the entrepreneurial activity of the state as fast as is possible. On June 17, the government passed the "Thüringensetz". From July 1, the government transferred to the new government of the "Thüringensetz" and gradually overwore economic unification with the West.

After the decision of March 18, the movement toward a market transfer of previous owners (THA 19930)

A wave of privatizations started in August 1992, followed by a wave of privatizations in September. By the end of September, the privatization of companies that had been nationalized in parallel to this effort of privatizations, the law of March 7 was in force. The power of the government is now directed toward restructuring the economy. The power of the government is now directed toward restructuring the economy. Although impaired by a plethora of technical and institutional problems, this wave of privatizations is expected to create joint structures, born out of the need to break the old, market failures, and more than 200 companies were dissolved. This wave of privatizations is expected to create joint structures, born out of the need to break the old, market failures, and more than 200 companies were dissolved. This wave of privatizations is expected to create joint structures, born out of the need to break the old, market failures, and more than 200 companies were dissolved.
12. The most famous example is the attempted self-privatization of the former

ion (Staatsbank Düsseldorf) in 1991.

ional employment in East Germany in the third quarter of 1990, was 8.6 mil-

1. Some authors put the initial number of THA firms at 8,000. The figure

of THA firms with credit institutions of DM 104 billion.

1990 in East Germany: 12

(see, for example, Phelps and others 1993) and had begun to develop in

the transition process in many other Eastern European countries

with early attempts at asset stripping and self-privatization, which

The liquidation of control allowed the THA's supervisory board to intervene directly.

German managers in the THA's supervisory board, and in the following days the East

were replaced by Western managers, and in the following days the East

German unification on October 3, all 15 branches of the regional branches

would oversee the remaining firms (see figure 8-2). On the day after

firms with more than 1,500 employees, and the 15 regional branches

would oversee the remaining firms (see figure 8-2). On the day after

As of July 1, the THA owned approximately 8,500 firms with

immediate bankruptcy of East German firms.

DM 2.4 billion of liquidity credits from Western banks to prevent the

overnight interest rate. From July to September alone, the THA guaranteed

firms found themselves indebted by approximately DM 130 billion

because this rate also applied to corporate balance sheets. Fast East German

banks, 14,101 employees, 11 of which had been in the West.

The fall of Berlin Wall was already in charge of the new, non-structured and well-defined decentralized management with a hierarchically clear

Kuhnt, former head of Hochofen AG, Dormund, determined the

of East Germany, as well as accepting the DM as its currency.

ormative in the German Economic Transition.

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The split of Teunland companies into marketable units was facilitated by the so-called „Spaltenungsgesetz“ (splitting law) of May 4, 1991. A law that facilitated the THA was assigned in re-tailing companies by the so-called „Spaltenungsgesetz“. During the subsequent process of re-distributing the Kohalein, it was determined which firms were able to be transferred to no buyers could be found, and which could be restored. The evaluation of the THA 1992, p. 22. The evaluation determined which firms were to be transferred to a group of up to 8.000 firms. The evaluation committee (austauschgesellschaft) was accompanied by a three-year corporate strategy and were evaluated. For its initial report, the THA recommended the following products:

- Small firms
- Large firms
- Regional offices
- Supervisory boards

As a basis for future operations, the THA recommended these firms to be evaluated.
0.35 million commuters to West Germany (Statistisches Bundesamt 1994). Employment of qualification programs, 0.8 million in early retirement, and 1.2 million. The difference is explained by the 0.6 million in publicly funded training. Officially, in the second half of 1993 unemployment in East Germany was estimated by Sinn and Sinn (1993),

"The measurement of GDP in the GDR is subject to well-known distortion", forced to take on peculiar, the large financial and environmental liabilities the THA has been burdened with, have endangered its viability. The THA’s restructuring and privatization tasks—in particular for a description of the state of East German firms and the difficulties ahead—could be at favorable terms during this period" (Willer 1993).

"Well-informed buyers, who were interested in specific parts of the Kom-

By early summer of 1991, the THA had largely consolidated its 500 percent between June 1990 and June 1991 (see figure 8-3) by merging its 9.3 million employees to West Germany 3 million 1993, when the transition to a market economy had improved to have reached its dramatic scale. Between the first half of 1990 and the second half of 1993, the THA’s restructuring and privatization process, which has seen the THA’s largest and most significant transfer of assets (GDP) fell by 35 percent. By mid-1993, the THA’s restructuring and privatization process, which has seen the THA’s largest and most significant transfer of assets (GDP) fell by 35 percent. Between early 1990 and the end of 1991, "For years, the THA’s restructuring and privatization processes..."

By this time, the East German economy had experienced a depression. By July 1, 1990, a DM 79.9 billion—only on September 29, 1992, 15

The consolidation of the THA’s structure and the preparation of
Figure 8.3: Employment Trends

Source: Transitional Data, author's calculation.

Note: East: Old federal states and abroad

From the West From the East

Higher Management

Management Board

Total Employment

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An excellent reference for the evolution of the THA's structure is Selbel (1993). This figure includes provisions for future liabilities, for example, DM 20 billion for the cleaning and repair of nuclear sites and coal mines.

19. The THA's board goals were defined by the Treuhand Act: its two board and management board had been newly appointed. Two weeks later, the supervisory board of the THA was staffed by government bureaucrats. Two weeks earlier, the supervisory board had appointed approximately 440 employees; an improvised, many regional, and entrepreneurial activity of the state as fast as far as possible. It was the Treuhand Act's task to reduce the Treuhand to its owner.

Centralized Oversight: The Treuhand

If it is expected to show a deficit of DM 7.75 billion, shear, including provisions for future financial and environmental liabilities, the authority of the Ministry of Finance, the THA's existing balance, and so on. The THA's board will be continued until the end of 1996 by a federal agency under a new act (contract monitoring, representation), and so on. The Ministry of Finance, the block of the THA's power, the THA's power. The THA will cease to exist in its present form. It is estimated that the THA will cease to exist in its present form. It is estimated that the THA will cease to exist in its present form. It is estimated that the THA will cease to exist in its present form.

the law, the dynamics of the firm. Although formally in breach of the law, the concept of subholdings in favor of a more concentrated organizational structure is in line with the German Anciens, all under the control of a central board. Within days several subholdings integrated into the old industry ministries, next to several supervisory boards, who subsequently replaced the old management. After a few weeks, the structure of the company had to adjust to the new president. The management seemed to be incapable of defining its organizational form and the priorities in building up its new structure.

22. Numbers are based on the preliminary evaluation of questionnaires re-

processed by 8 percent between July 1990 and July 1991 (Dyck 1992). See
below.

21. The share of Westeners on THA firm management boards rose from ap-


The privatization process, however, created another problem. The THA came
issue of Homeoffice 1991). The relatively slow start of the pri-

national structure (see Willimon 1979), after several months it adopted a

decentralized organization—exemplified with a similar unitary organ-

the center had initially—after the decision to drop the plan for

the most appropriate organizational form of the THA center. While

considerable amount of much as possible, the structure were the

On the other hand, at least as important in the structure were the

than its efforts.

The second important decision in the early phase of the THA was

sion, there was room for discretionary strategic choices.

In contrast to its policy in its early phase, the THA used local man-

which grew from 42 in July 1990 to 250 in July 1991 (see figure 8-3),

work force of the THA center (which grew from 122 to 1,564 within

we highlight two main elements reflected in the enormous growth of the

institutional development. As we also mentioned above, the THA was

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funds available, one could have arrived at these observations even more.

transacted, transactions.

percentage refers to the number of transactions.

States, and THA for the Recovery Board (Bundesfinanz 1991).


smaller and less active. Suppose that the THA had chosen to auction

middle period, and declining sales during an extended筹建 period.

form of sales initially, relatively quickly, steady sales in the

resulting graph has a slight

25. The resulting graph has a slight

an estimated 4 percent. In 1991, sales had been sold, it will still hold another 6.5 percent, and in

companies had been sold, it will hold another 38 percent of its stock at a relatively steady, fast

loans, it sold another 38 percent of its stock at a relatively steady, fast

Development of its internal structure, the THA sold less than 20 percent

within the first year of its existence, when it put emphasis on the de-

replaced in the time series of company sales, shown in Figure 8.5.

The THA’s choice of its organizational strategy is quite clearly

unchanged, that is, unlikely that this agreement induced more than

1991, and privatization was performed so energetically from the

division of roles between government and THA was so well defined by

THA, the THA acknowledged its responsibility. CRITIC CONSULTATION AMONG THE FEDERAL GOVERNMENT, THE HEADS OF THE NEW

agreement, and in the overwhelming portion of the formally state-owned firms

EAST GERMANY, WHEN THE EAST GERMANY ECONOMY BEGAN TO CO-

under increasing public pressure to undertake “regional structural

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of firms, in particular, were used by the ITHA only twice and for a specific group.

Thus policy would have been closer to the Czech and the attempted
of possible employment consequences of such policies.
27. See Akerlof, Rose, Yellen, and Hessensius 1991 (section 5) for a discussion
during the process. 28
its organizational structure with lower priority and on a lesser scale
leave the restructuring of the firms entirely to their buyers, and establish
lines proposed by Sin and Siny (1993) and Dolon and Roland (1992),
lines break the stock-flow constant of mass privatizations along the
firms; rather than rely on extended bilateralnegot-

Source: Teubingensia, author’s calculations.

Note: “Firm solid” fully or majority privatized or transferred to local
authors, “liquidations” liquidation completed or in progress.

Figure 8-5. Evolution of Teubingensia firms and liquidations
Number of Firms

(%) of total stock

Phms sold
Liquidations
32. In view of the disastrous unemployment situation in East Germany, this is
Bundesversicherungsministerium 1994; Sinn and Sinn 1999). As a result, this would have increased the demand for labor in the private sector. However, the
impeded any possible policy changes. In practice, this led to a significant delay in the privatization process. The

3. One particular feature of the German privatization process, however,
Cabinet 1994.

30. On the problem of the optimal speed of restructuring, see Aghion and

31. Even under the actual policy of the THA, these efforts were quite visible.

Governance structure of the resulting organization. The question of
governance structure of the resulting organization will discussed in more detail the
By all accounts, the THH was fully operative by the early summer.

a more frequently voiced complaint has been that the THH received too little and privatized too fast. 32
A more frequently voiced complaint has been that the THH received too little and privatized too fast. 32
Looking back at the history of the German public debate, too slowly has not been in the forefront in the German public debate.

4. The question of whether the THA sold off its stock
of privatization partners. 4 The question of whether the THA sold off its stock
of privatization partners. 4 The question of whether the THA sold off its stock

5. Stock is available, and that other strategies would have led to other price-

6. A general feature of building a strong core on the THA's actual strategy was only one of several strategic

whether such a front-loaded strategy would have been sufficient is
whether such a front-loaded strategy would not have been sufficient is

over all share of liquidations at the end.

In the last phase of the privatization process, possibly with a higher
value of the residual portfolio, which have resulted in lower sales rates
and the exhaustion of deeply profitable matches and uncertainty over the
the exhaustion of deeply profitable matches and uncertainty over the

29. At the same time, this effect would have been reinforced by the lack of experience
29. At the same time, this effect would have been reinforced by the lack of experience

In the privatization agency, through its ability to do so. The most probable
more strongly from front-loaded evolution of sales. The most probable
29. Such an approach, by all expectations, would have led to a much

in the relationship between task forces and regional offices. In practice, these forces were less than smooth because of agency problems. In one view, the external redress of the THA has neither the task force nor political commitment. The THA, as well as the external consultant function.

I have been pointed out repeatedly by the THA, as an example of the management experience and contacts. Therefore, the consulting function, management know-how, and to some extent, external, external consultants, who were usually-teams of experts, who were usually located around a senior, large firms. The additional layer of control below the center, larger firms that are endowed with supervisory boards of THA-controlled firms other than actively involved in the restructuring process, contributing financial know-how, sometimes technical, but in some cases, more or less on a quarterly basis. As of August 1991, there were twenty such directors, designated "industrial directorate" (Industrieverband) responsible for the respective TTHA management board, and regular issues were dealt with by the TTHA's management board, and regular issues were dealt with by the TTHA's management board. In addition, the supervisory board of each center, major questions concerning the THA, and the regional boards of the THA, were decided directly by the supervisory board of each center.

For TTHA-controlled by the center, major questions concerning the THA, and the regional boards of the THA, were decided directly by the supervisory board of each center. 33. The organizational change initiated by the president in the next section

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Schwalbach (1993), were judged to be more or less prominent after restructuring (Gleiss and
Utting, and LeSage) to be absolutely invaluable. The remaining 72.8 percent
of operating balance sheets found 9 percent to be viable without much restruc-
ture or operating balance sheets found 8 percent to be viable without much restruc-
ture of operating balance sheets found 8 percent to be viable without much restruc-
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ture of operating balance sheets found 8 percent to be viable without much restruc-

37. Recall the division of responsibilities between the center and regional
realizations of authority.

38. A bureaucratic organization such as the Techno-Annas, for example, Fisher, Hax, and Schindehk (1994), p. 3, share traits that are much
more economic observers, free from political pressures, go even further.
38. A bureaucratic organization such as the Techno-Annas, for example, Fisher, Hax, and Schindehk (1994), p. 3, share traits that are much
more economic observers, free from political pressures, go even further.

Because the center judged less than 10 percent of its firms to be
early large number.

Under the THA’s policy, the most important decision for each
must be considered to be strongly centralized.

Social economic environment, the THA’s governance of larger firms,
and management influence. According to these criteria, executives
will use four criteria to evaluate this structure: the extent of company
restructuring, the supervision of corporate planning; company break-ups,
and how lower-level planning is controlled by the center. Here, the
center is the principal yardstick to judge the THA’s governance.

In this respect, the principal yardstick to judge the THA’s governance
has been hierarchal and characterized by high levels of political risk to its executive, its governance structure has
been hierarchal. The more interest in the THA’s governance, and the size of its holdings, the more executive.

It is clear, however, that because of the company’s size of its holdings, the more executive.

Corporate Governance in Transitional Economies
Corporation Governance in the German Economy Transition

...
Externtal Control of the THA

1992 for a comprehensive analysis.)

Visors boards (THA 1992, p. 24)

Directly, and an additional 300 were replaced in companies with super-
active management control. In 1992 the THA dismissed 300 top managers
cases were solved. In this early phase, the THA maintained a policy of
September 1990 and July 1991 alone, the THA dismissed 1,400
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Although many of the immediate problems
Accordingly, the THA's board of directors, the THA has used this control right very actively,
but rather on shareholders' behalf, the THA provides management of joint-stock companies—and hence many
elements of corporate control. Although the German Stock Company
defines for transitional economies, it still constitutes an important
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corporation law, including more extensive references, see Banks 1993.

47. For a brief description of the role of the supervisory board in Germany and the position of the executive board, see, for example, Christ and Schwappach 1993.


49. This is according to the guidelines of August 1991. The figures have changed slightly since then (see, for example, Christ and Schwappach 1993).

50. In practice, the placement of THA bonds is undertaken in close cooperation with the Ministry of Finance. The budgetary (THA 1994a, p. 28).

51. This is in line with the Ministry of Finance and the Bundesbank (THA 1994a, p. 28).

52. The supervisory board (Vertretergremien) modeled along the lines of corporation law, Ministry supervision is complemented by that of a super-visory board (Vertretergremien).

53. Reconciling the THA's hitherto legal status between public and private law, Ministry supervision is complemented by that of a super-

54. On the operational level, the Ministry must approve all restrictive decisions involving volumes above DM 100 million. In practice, the Ministry's role is limited to confirming the THA's budgetary volumes.

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56. The THA is required to include in its annual report a concise financial statement that provides a more extensive reference to the financial statements. The THA is required to include in its annual report a concise financial statement that provides a more extensive reference to the financial statements. The THA is required to include in its annual report a concise financial statement that provides a more extensive reference to the financial statements. The THA is required to include in its annual report a concise financial statement that provides a more extensive reference to the financial statements. The THA is required to include in its annual report a concise financial statement that provides a more extensive reference to the financial statements.
The role of Parliament in controlling the THA generally has been

yielded too much to THA interests. The compromise that was agreed

on in May 1994 took these concerns fully into account. Given the

extent of the Federal Accounting Office’s influence on the grounds that

a group of employers (eun sale) with representatives from various

stronger represented than the Federal Government. Directors of

the two largest German states, and the trade unions (four seats) are both

expressed through the governments of

by the Federal Government by January 1, 1991. The Regional

Figure 8-6 shows the composition of the supervisory board as appointed

been at least as important as its control function. The supervisory

In practice, the advisory function of the supervisory board has

agreement. To this end, it is regularly informed by the management

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Hence, probably the most important control mechanism of the THA has been time. Although the Tribunal Act of June 1990 had not been specific about the timing of the THA’s activity, a consensus soon emerged that the THA was to be in operation with a finite life. The Independent for the Appropriate decisions” (Kohl 1992).

The Federal Republic of Germany—will do everything to guarantee this. The Federal Government—and, most of all, I myself, as the Chancellor of the Federal Government—and, most of all, I myself, as the Chancellor of the Federal Republic of Germany—will do everything to guarantee this. The Federal Government and the THA: “The THA can fulfill these tasks.

The European picture that emerges from this analysis is one of the TEE supervisory board to open its files to the committee. The committee initiated a suit in the Constitutional Court to force the committee deemed necessary. In March 1994, members of the...
only 9.7 percent perceived decreases in external influence.

1997. Only 9.7 percent perceived decreases in external influence, down from 16.9 percent in 1991. This may reflect the perception of the THA's decreased influence on the external environment.

The THA's success in the external environment has been very critical. The THA's ability to influence the external environment is an important factor in the THA's top management. Without a clear understanding of how the THA's influence process works, the THA's decision-making process is likely to be less effective.

The THA's top management and policymakers play a critical role in understanding the THA's influence process. While the THA's influence process is complex, policymakers and top management must work together to ensure that the THA's influence is maximized.

In a first, and still preliminary, assessment, this institutional mechanism is seen as helping to improve the THA's influence process. However, more work needs to be done to fully understand how the THA's influence process works and how it can be improved.

In conclusion, the THA's influence process is complex and requires careful attention. Policymakers and top management must work together to ensure that the THA's influence is maximized.

Ministry of Finance.
Decentralized Ownership: Privatization

The bill effectively prohibits the life of an institution that was
purchasing a population of predominantly small firms in the East.

picture is that of a rather wide range of buying firms in the West undertaken by small to medium-size West German firms; the general annual turnover of more than DM 2 billion. Taking into account that many of the smaller transactions not recorded in this sample were million. On the other hand, 79 percent of all acquiring firms had acquired firms in the sample had annual turnover of less than DM 50 million. In this sample were all firms in this takeover wave. On the one hand, 78 percent of all clearly exhibit the extreme asymmetry between acquiring and acquired firms. Despite the same selection bias toward larger companies, the data the THA had privatized or reprivatized 18,729 businesses by business.

Source: Treuhandanstalt.
Note: Total = 2,922 million.

Figure 8.7: Evolution of Work Force of THA Firms, January 1, 1991
East of the West, the problem of corporate governance has been shifted from the smaller, family-oriented firms to larger, publicly traded firms. This change is evident in the distribution of acquired firms. In East Germany, 1991, 1992, and 1993, the number of acquired firms increased significantly compared to the previous years. The figure shows the distribution of acquired firms by turnover, with a significant increase in the number of firms with turnovers between 100 and 500 million DM, and a decrease in firms with turnovers below 50 million DM.

would buy THA.This would allow DM 1 billion. One year later, banks had
fully promissed the German Chancellor in January 1993 that the banks
would buy THA. This was the German Chancellor's promise to the German Banking
Association, the president of the German Banking Association, the president, with respect to equity participation. Under increasing
pressure from the West, the banks showed interest in the process. Puhlmann, et al.
Furthermore, through the transition process, banks showed their
chambers of commerce, friends from the West, and, finally, banks.
most advice came from professional consultants, followed by local
quarter of all respondents obtained no consultation at all. Of the rest,
seven percent of all respondents obtained no consultation at all. Of the rest,
seven percent of all respondents obtained no consultation at all. Of the rest, a
relatively minor role in advising new firms. More than a
prayed a relatively minor role in advising new firms. More than a
(1993), who reports for a sample of small business start-ups that banks
transition. This is consistent with the empirical finding by Puhlmann,
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mortgage and screening by banks. In the earlier phase of the economic
and Reiter (1985),
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conclude

Conclusions

not served on the THA management board, West German banks neither held seats on the THA supervisory board and Mayer (1992). Yet, it is interesting to note that representatives of Conclusions for THA branches and firms, and through their primary by consulting the THA, banks contributed substantially to the reconstruction of THA firms' support. Such representatives not to be their business. 38 In contrast, pre-
Germany.

However, the major part of the transfers from the West—which were far apart from all other transitional economies in quantitative terms—were legal and administrative structures. First, the large market transfers; second, the transfer of human capital; and third, the availability of an advanced and reliable educational system. Third, in this specific context, the specific nature of the German case. There are three major factors that have been unique to the German case. When assessing what this specific transformation experience can imply for other economies in transition, it is useful to first identify why. The first three elements of institutional design have supported this distribution of regional problems, industry structure, and ownership.

60. These issues are emphasized in Dornbusch and Wolf 1993 and Carlin and Naylor 1992. Carlin 1993, however, rightly points to the severe and sometimes

particularly disturbing—large firms prior to privatization. Central—ICD

The major implication of this policy has been the possibility of

potent governance imposed on the East German economy by the West.

Corporate Governance in the German Economic Transition

... by supervisory boards. Under German company law such management the activity of the THA concerns the management of firms governed by supervisory boards. A piece of legislation that directly impacted these concerns has often been voiced with respect to environmental laws and regulations. May hinder rather than promote the emergence of entrepreneurial activity (see Bundeswirtschaftsministerium 1991). Have been argued that the provision of a large set of highly regulated insinu-...
62. For relevant case studies see, for example, Die Wirtschaft 1993.

Fowler, this formal supervision may be more convenient for the main
and if the state proves to be a generous owner and permitting con-
is no clear commitment to the completion of the privatization program
level managers. Jensen and Ruback 1983) may easily degenerate into
the Hungarian "centralization" strongly of minun 1991 (see Voska
the Hungarian "centralization" strongly of minun 1991 (see Voska
have been more important in the commu-
variations strategy of centralized decentered decentralization, it does not appear that its pre-
tremely privileged material conditions; it does not appear that it is pu-
Hence, although the East German transition took place under ex-
highly able to establish authoritative business contacts in the meantime, was
reached bilateral bargaining, and the East German, not having been
the sales contract. In several cases negotiations broke down after pro-
also in regard to the restitutions or liquidation decisions included in
ration with the THA, not only with respect to the takeover price, but
involutions. This often put them in a strong bargaining position in nevo-
consultants on supervisory boards. West German firms often
firms to establish business links with East German counterparts, and
downside, because it was already common in 1991 for West German
defined by Western companies—has also had its
The strong inflow of human capital from the West—often provided
example of a piece of legislation introduced to curb these transfers
managers that opposed THA plans. The Splitting Act of 1991 is an
processes to obtain information from management or simply to seek
have been several cases in which the THA had to go into lengthy legal
direct means of imposing his or her will on the management. There
is responsible only to the supervisory board, and thus the power has no

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