

OWNERSHIP AND CONTROL OF POLISH CORPORATIONS*

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Abstract

With the company-level data on listed and unlisted companies we analyse ownership and control of Polish corporations. We find that voting control in listed corporations is remarkably concentrated with the median size of the largest block amounting to 39,5%. A sustainable concentration trend has been observed over the whole last decade. Other companies and individuals/families (mostly founders) dominate among the largest block-holders of Polish corporations. Banks' involvement in control is below common expectations. It is also observed that – especially in smaller firms – managerial ownership is quite large. Frequently, managers are also the company founders and first or second largest block-holder. The extent of ownership and control separation is very modest with dual-class shares being the most popular device to leverage control over ownership; control through subsidiaries is applied to a lesser extent. The presence of large blockholders in listed corporations puts the minority rights and conflict of interests among stakeholders on the top of the policy agenda. Our analysis shows that the Polish capital market may be in desperate need of improvement in this respect.

Keywords: ownership, control, corporate governance, Poland

1. Introduction

For the last 20 years Polish enterprises have been a playground for deep and wide institutional changes including, first of all, ownership and control. The background of these changes as well as their outcomes has varied significantly over time. Both politically forced re-arrangement of control without ownership changes and market driven reforms affecting ownership (privatisation) and (for some enterprises to a lesser extent) control rescheduling could be observed within this period of time.

The first shift in enterprise control can be traced back to the beginning of the 1980s. The political pressure exerted on government by the free trade union movement resulted in a significant separation of control over the state-owned enterprises from ownership. Formally, the control was split among the State Treasury, a quasi-supervisory board dominated by employees (a so-called employees' council) and a general assembly of employees. This control rescheduling experiment lasted for about 10 years and brought mixed results. In general, control over

managers was tightened and in numerous cases improvements in performance were evident. However within the world of soft budget constraints the managers' secrecy was still enormous. This, for instance, resulted in a huge appropriation of enterprises' assets within so called "shadow privatisation" taking place since 1988. The experiment also created a strong and politically influential employees' self-governance movement.

With the introduction of the stabilisation plan in 1990 (so-called Balcerowicz's plan) the set of incentives for enterprises was dramatically changed. Withdrawal of subsidies and opening up of the economy forced the enterprises to adjust to market signals. The control over enterprises was additionally (formally) extended to banks and suppliers who could force them into bankruptcy. These changes in control arrangements were further supplemented by privatisation schemes.

The goal of this paper is to shed some light on ownership and control of Polish public corporations. We begin with an overview of mandatory transpar-

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ency provisions that are fundamental for thorough study of control concentration and arrangements. In subsequent paragraphs we report on existing studies on corporate control in Poland and then provide data on voting control concentration, its evolution over last decade, and most common control structures that are used by blockholders.

The paper is generally of descriptive nature but we believe it is a good starting point for further research on corporate governance in Poland. Among the most urgent issues – we think – there is to see if different control structures result in different corporate performance, and whether large block-holders take advantage of weak law enforcement. It would also be interesting to analyse the policy mix that led to the observed ownership and control patterns.

2. Ownership transparency

The adoption of Transparency Directive¹ by European Union in late 80s was a breakthrough in providing access to reliable data on corporate ownership. With the mounting general interest in corporate governance theme this encouraged a strand of research that resulted in most comprehensive study on European ownership and control patterns (Barca, Becht 2001).

Although transparency of the stock market in Poland was at the heart of its founders, it took a couple of years to work out a model of transparency which in general fits to the Transparency Directive (TD) standards. It can't be said, however, that the law on public trading in securities fully absorbs all major provisions of TD.

The Law on Public Trading in Securities was passed in March 1991. Since that time there have been 3 important amendments with the last one in force since January 2001². The first regulation (in force from 1991 to 1994) defined 6 thresholds for disclosing ownership stakes: 10%, 20%, 33%, 50%, 66%, 75% of voting rights. This was almost exactly in line with article 4 of TD, but the group definition left much to be determined. It referred only to the situation of the controlling entity (second indent in art. 7 of TD and the definition from art. 8). Disclosing thresholds were significantly tightened in 1994. The first threshold was lowered to 5%, the next one remained at 10%. All investors had to report each +/- 2% (or more) transaction(s) above that level. Group definition remained unchanged. In 2000 legislators left the disclosure thresholds practically unchanged³ but improved group definition by expanding notifica-

tion requirements for acquisitions realised through other parties acting in concert. Since then the group definition reflects most of the indents of art. 7 of TD, however indirectly.

The general picture of the notification process looks as follows. Any shareholder acquiring, exceeding or falling below the stipulated thresholds is obliged - to inform the company (issuer), the Securities and Exchange Commission and the Antimonopoly Office - within 7 days of the transaction⁴. The information should include the amount of shares owned and percentage share in cash flow and total votes. Then the issuer should immediately pass this information to the Stock Exchange and the Polish Press Agency (a nationwide information agency). A wide public distribution of information is the last stage. This is done by means of newspapers and direct access to an electronic reporting system, which is run by the Securities and Exchange Commission.

Public access to blockholding information is satisfactory as transactions are publicly reported and the current shareholders structure for each company is available both on paper and in electronic format (from some websites). Access to historical, cumulative information is rather problematic. Except for a commercial, electronic data base available from Notoria Publisher no cumulative information is publicly available, however the PSEC is probably in possession of such a breakdown.

3. Existing evidences on ownership & control in Poland

The economic transition in Central and Eastern Europe has brought the attention of many international and domestic researchers, resulting in a large strand of literature on privatisation, corporate restructuring and institution building. However, the way that Polish corporations are owned and controlled has not been deeply analysed so far.

The first evidence on ownership structure is reported in Belka et al. (1995). He found that in 23 out of 200 analysed enterprises ownership was concentrated. The largest shareholder usually held about 50% of shares with a tendency towards 70%-85%. The ownership was additionally limited to a very narrow circle. In a few cases, ownership was shared by two partners (50/50 or 49/51). Eight out of 23 corporations were in the hands of senior managers and/or employees, 10 were controlled by private individuals and 10 by foreign or joint venture entities. The position of managers and employees in privatised corporations was further investigated. In 22 out of 40 cases managers and other employees together held a dominant position among shareholders. Managers owned on average 21.6% of shares compared to 48.8% in employees' hands. Domestic private banks (average shareholding of 3%), investment

¹ Transparency Directive of 12 December 1988 (88/627/EEC).

² In fact in 1997 the new act was introduced as the previous one (covering also open-ended funds) and was divided into: the law on public trading in securities and the law on investment funds.

³ Slightly higher interval for notification (plus 5% instead of 2%) was introduced for the OTC market.

⁴ Formally 4 days after transaction registration, which should take place within 3 days of the transaction.

funds, individuals and firms were reported among minority shareholders. Belka et al. (1995) concludes that the position of managers in governance of privatised enterprises was very strong.

The relationship between various issues of corporate restructuring and ownership is documented in a number of extensive international, comparative studies (Frydman et al. 1999, 2000). Privatisation is most effective when control is sold to an outside investor rather than managers or employees (Frydman et al. 1999). In general, firms controlled by an outsider restructure and grow faster than those owned by insiders. This is mostly attributed to the incentive effect rather than the human capital effect (Frydman et al. 2000).

Research conducted by domestic researchers focused mostly on employees and management-led privatisation (so called "direct privatisation"). Gardawski (2000) finds that the majority of companies analysed have an outside owner. In 18% of the cases, he/she owned on average 65% of shares. Domestic corporations, banks, foreign investors and managers hold on average 33%, 15%, 26%, 26% of shares respectively. Kozarzewski (1999) focused specifically on companies that were privatised through employees leasing contracts⁵.

In an extensive study he documented that employee shareholdings declined over time while managers and outsiders leveraged their positions. The biggest increase in corporate shareholding was observed in the case of outsiders (4.5 times in 1995 compared to the early 1990s). In 1995, in 38% of the analysed companies, an outside investor held at least 20% of shares, in next 50% outsiders were among the top ten shareholders. The pace of ownership concentration depended mostly upon industry, company size and profitability.

Moreover Kozarzewski (1999) reports that there was no free market for employees' shareholdings; those who were real initiators of a privatisation plan (usually managers) were strongly opposed to uncontrolled transfer of control to outsiders (and even insiders). Trading in employee shares was therefore heavily regulated by managers and/or supervisory boards. In 87% of company statutes any sale usually required a written approval from the management board or supervisors or existing shareholders had the right to buy the shares first. In spite of all these measures and management opposition, ownership concentration finally took place, however, managers – to some extent – achieved their goals: "protection devices" when applied significantly lowered the size of outsider shareholding.

4. Corporate control in listed corporations

The public capital market – although much smaller than in developed countries – offers a good starting point for analysing ownership and corporate control in Poland. With its more than two hundred corporations it is responsible for about 20% of industrial and financial enterprise turnover and 3.4% of total employment. Its capitalisation amounts up to 18% of GDP; it offers some variety of enterprises in terms of branches, size and origin.

For the purpose of this research, a database was compiled covering almost the whole decade of 1991-2000. It includes ownership and control data for 190 non-financial corporations listed on the WSE and 20 from the OTC market. The data from previous years was used to analyze how the patterns of ownership and control have evolved over time. It should be remembered, however, that the number of public corporations evolved significantly over time in Poland. In 1995 there were only 21 corporations and just 9 in 1991.

The data come from mandatory disclosures. Due to the fact that a voting block was not well defined in Polish law⁶ the notification practice lagged behind the disclosure philosophy stipulated in the Transparency Directive. Even after recent amendments, voting (shareholder) agreements do not require notification unless one party increases his/her stake and anyway such combined notification is quite difficult to enforce. Blocks owned by founders and family members are usually notified separately, however they may be treated as a single voting block.

Because of that we had to improve the "quality" of data by making some "manual" corrections. This could, of course, result in (unintentional) over- or under- consolidations of shares.

Firstly, shares owned by private firms, which were in turn controlled by individuals were directly attributed to these individuals.

Secondly, we consolidated shares owned by members of one family into one block. Generally, shares owned by founders were not consolidated.

Figure 1 & 2 shows how the notification looks in practice. For Ryszard Krause controlling Kompap (Plc.) we used the stake 41%, however he officially notified only 31%, as his stake in another public company Prokom Software, being also shareholder in Kompap, was below 50%. For Sobiesław Zasada (Plc.) we attributed a family stake of 81% of cash flow rights and 90% of voting rights, however the biggest notified stake was 42%/57% of Sobiesław Zasada Ltd.

⁵ This was the most popular way to privatise small and even medium size state owned enterprises. It consisted of legal (but not physical) dissolution of an enterprise and leasing its assets to a company formed by employees.

⁶ The previous amendment to the law on public trading in securities, which came into force at the beginning of 2001 improved the situation in this respect.

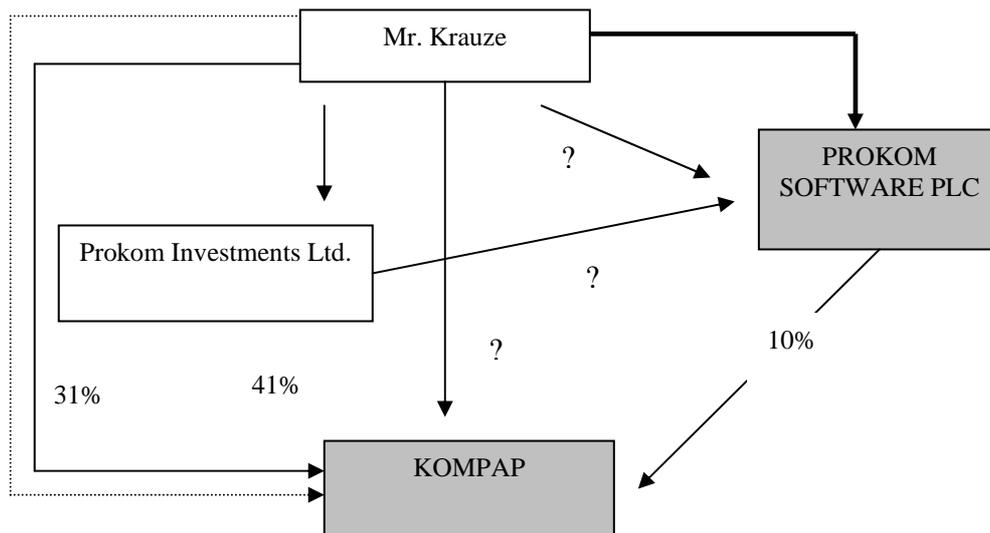


Figure 1. Notification and control over Kompap SA (question mark means that stake is not disclosed)

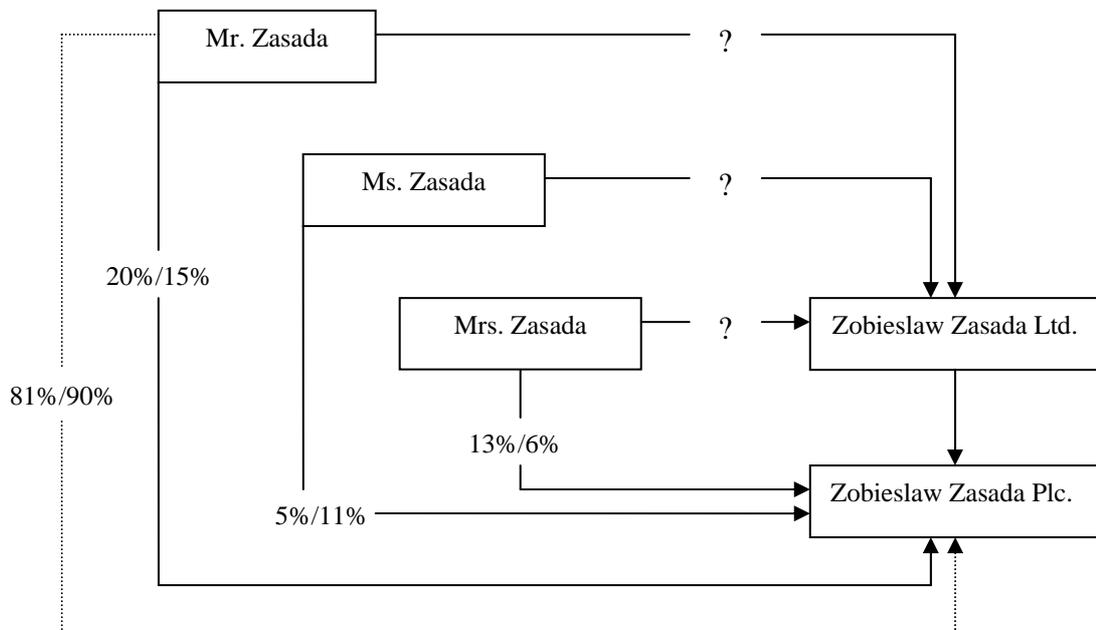


Figure 2. Notification and control over Zasada SA (question mark means stake not disclosed)

The results reported in table 1 reveal significant concentration of corporate control in Poland. In the case of 161 out of 210 corporations one shareholder owned at least 25% of the votes, in 75 corporations one shareholder owned at least 50% of the votes. The median size of the largest block amounts to 39.5% of votes (and 37.2% of cash flow rights). After consolidation of shares owned by individuals, assumed to be founders of a company, the median size goes up from 39.5% to 45.8%⁷. The median size of the sec-

ond, third and fourth blocks is 10.4%, 5% and 0% of voting rights respectively. Without blocks owned by the state or national investment funds⁸ these figures drop to 9.6% and 0%. This shows that the control of the largest blockholder is hardly contestable.

⁷ For this checking in 5 cases we also consolidated into one block shares owned by several different parties acting in our view in concert in order to omit the need to announce a

public tender after purchasing more than 10% of voting rights within less than 3 months.

⁸ Financial intermediaries set up for the purpose of mass privatisation scheme.

Table 1. Blockholding in Poland in % (as at end of 2000)

item	1 st Largest	2 nd Largest	3 rd Largest	4 th largest
Average	44,6	15,6	9,4	7,7
Q1	25,4	5	0,0	0,0
Q2 (median)	39,5	10,4	5,0	0,0
Q3	60,3	18,5	8,6	5,2
Q4	99,7	40,6	20,1	18,3

Source: own computations

Cumulative distribution of the largest voting blocks (figure 3) indicates a very modest concentration of voting blocks around four levels (The figures report the fraction of companies with the largest blocks minus the values reported on the vertical axis. The 45% line reflects a uniform density of firms by voting blocks.

The first one is 29%-33.5% of voting rights (26 corporations). This may reflect the unwillingness of shareholders to break through the 33% level which requires consent from the Polish Securities and Exchange Commission (PSEC) and the fact that in companies taking part in the mass privatisation program, the leading fund obtained a 33% stake. The importance of the 33% limit may also be observed in previous years, since up to the beginning of 1998

crossing that threshold required a tender (bid) for acquiring all the outstanding shares of the company (now the mandatory tender offer applies when crossing the 50% level).

Other concentration levels are: 40.9-43.5% (11 companies), 49.5-50% (6 companies), and 74.1-75.7% (11 companies). The concentration around 75% level is most likely caused by PSEC policy to limit or slow down the process of de-listing. The PSEC unwritten policy was to subordinate the consent to cross the 50% threshold upon a promise that the investor would not increase his/her stake to over 75% (according to company law, 25% of votes at shareholder meeting is a blocking stake – changes to the statute and new share issues require a $\frac{3}{4}$ majority).

The largest shareholder (end of 2000)

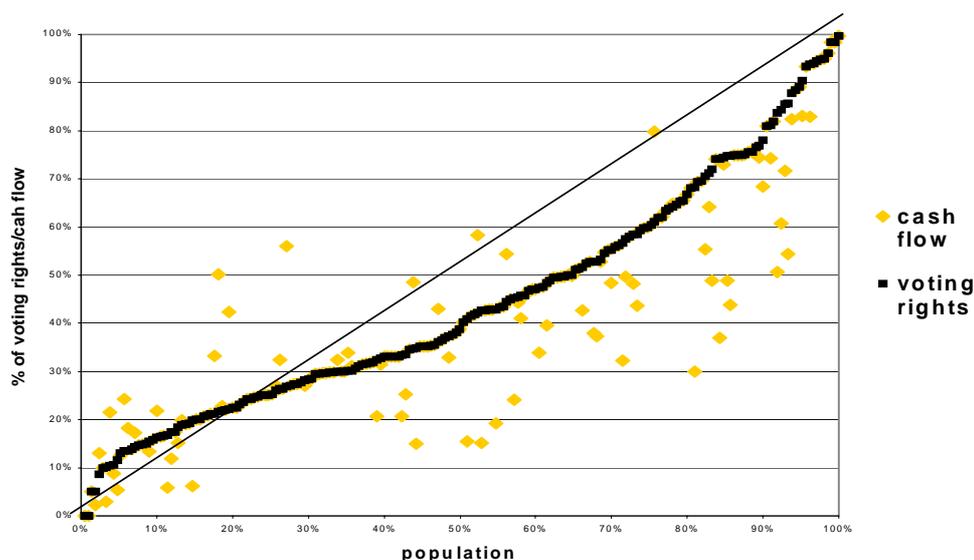


Figure 3. Distribution of the largest blockholder

Polish public corporations are most frequently in the hands of other corporations (also other public companies) and individuals (families). These groups were responsible for about 39.4% and 30.8% respectively of the biggest blocks. Additionally, individuals owned 1/3 of all disclosed blocks (corporations – 27.6%). Financial institutions – mostly national investment funds and equity funds – owned 14% of all the biggest blocks. At the end of the ownership list there were the State Treasury and other state entities

with 9.1%, and surprisingly, banks with only 6.3% of all the biggest blocks.

The average size of blocks owned by a physical person is about 40.6%. This figure, we suppose, should be slightly higher because since the blocks owned by founders were not consolidated. The average size of blocks owned by domestic (Polish) non-listed firms is very similar to that above – 43.5%, while in the case of public corporations it is much higher – 54.2%.

We observed a significant difference in the size of blocks in the hands of foreign investors – 67%. This difference is also evident in the case of the second largest blocks – 24% for foreign investors compared to 15.1% and 15.8% for individuals and private corporations respectively. Much smaller differences in block size are observed in the case of domestic and foreign financial institutions – for the largest blocks, the average for domestic investors was 31.2% compared to 35.5% for foreign. For the second and the third largest blocks, the differences were insignificant.

Ownership structure analysis also revealed – not surprisingly – that in many medium sized corporations and even larger ones there exists an overlapping of three roles: a founder – blockholder - manager. In about 35 cases, it was noted that managers held blocks of shares ranging from 5% up to 93% with an average block of 28.5%. Moreover, in 20 corporations the blocks owned by managers were simultaneously the largest ones and in 10 cases the second largest. In the majority of these cases managers belonged to a narrow group of founders. The group of “founder-manager” corporations comprised mostly of companies developed from private start-ups. Only four companies originated from privatisation.

In value terms the ownership of Polish public companies looks different. Foreign investors are major players with a 14.6% share in market capitalisation (in the case of strategic investors), and 5.3% in the case of financial investors.

The second position belongs to the State Treasury and other state entities (state-owned enterprises, state-owned banks, municipalities, foundations) which altogether have a 12.5% share. Individuals (families) and corporations – the most common blockholders – represent 10.2% and 6.3% of market capitalisation.

Finally, banks – very passive in blockholding – are again passive players in value terms (1.2% share in capitalisation). The same refers to other domestic financial institutions (0.6%), although we think this situation will change dramatically as the pension funds sector is quickly growing in size⁹.

5. Separation of ownership and control

The available data allowed analysing how and to what extent control is separated from ownership. The overall picture is far from the separation patterns observed in Western Europe.

The extent of separation as well as the range of separation devices is - in general - very modest. Polish corporate law provides four general legal devices that may be used to leverage control over cash flow stakes:

- dual class shares (preferred shares)
- voting cap
- statutory provisions providing specified preferences to a particular shareholder (so called golden share)
- non-voting shares (introduced since 2001).

Control can also be leveraged through hierarchical structures (pyramids), cross shareholdings, acquisitions through subsidiaries and dependent entities. To shield specifically from hostile take-overs, except for the above authorised capital (introduced since the beginning of 2001) and purchase of company share (only up to 10% of shares) may be used.

Our analysis shows that preferred shares with multiple voting rights are the most common device to leverage control over cash flow rights. 79 corporations out of 210 (i.e. 37.6%) have issued preferred shares; these are mainly smaller companies founded by individuals or companies privatised through management and employee buy-outs. In the majority of cases (81%) the maximum preference allowed by law was used - five votes attached to one share. Surprisingly not always the largest shareholder had more votes than cash flow rights - this happened in 11.5% of the cases. “Positive” separation existed (more votes than cash flow rights) in 25.5% of the largest blocks. In 63% the number of votes equalled cash flow rights. The extent of separation measured by the number of votes per share amounted to an average of 1.5. In about 40 corporations the control exerted with preferred shares could not be contestable as they represented more than 50% of all voting rights. For instance the founders of Bakoma (dairy products) – Mrs and Mr Komorowski – control together through dual class shares 61% of votes with a two times lower share in cash flow.

In several cases the real separation could be much deeper than revealed in the notifications. The case of Agros (figure 4) is a good example in this respect. This large food processing company was controlled by TIGA – a privatisation vehicle set up by employees and managers of former state-owned enterprise. Thanks to preferred shares (one share – five votes) TIGA controlled 81.4% of Agros Holding votes, while its stake in cash flow was only 47.5%. In fact full control of Agros should be assigned to Zofia Gaber (the company’s director before privatisation and then the president of the management board), who was the largest owner of TIGA with a 18,5% stake and the chairwoman of TIGA supervisory board. This type of privatisation scheme frequently allowed managers of the former SOEs to gain privileged positions. Because of the legal loopholes it was also possible to take control of Agros by buying (non-listed) TIGA and avoiding a mandatory bid.

⁹ There are about 20 pension funds investing in Poland since pension reform inception in 1999. At the end of year 2000 they managed \$ 2.5 bln.

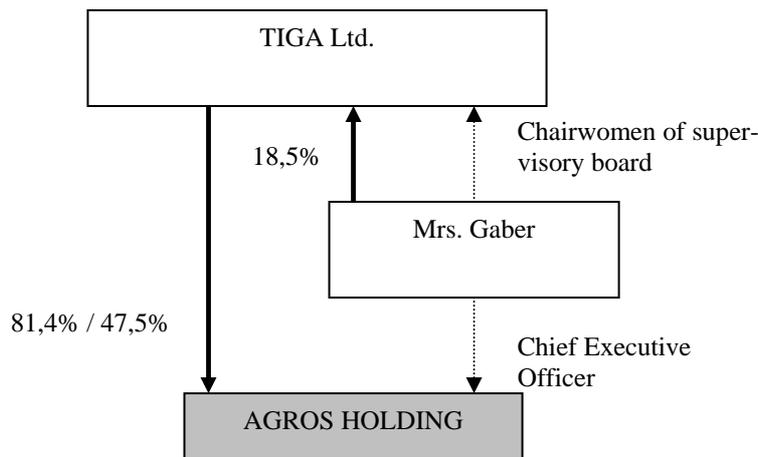


Figure 4. Control over Agros (leveraged through preferred shares)

Golden share is a statutory provision which awards a particular shareholder (usually the founder) extra corporate privileges – for instance the right to nominate a member(s) of the supervisory or management boards. This device is most frequently identified with large privatization deals and the State Treasury will to retain control over strategic decisions and the composition of governing bodies in a company. To our surprise we found such a device in a number of statutes of corporations not originating from privatization. In the above mentioned Bakoma the statute gives Mr and Mrs Komorowski the right, irrespectively of the amount of shares held, to nominate 3 out of 5 members of the supervisory board including chairman (and also to set the chairman's remuneration). Moreover, the chairman of the management board is elected not by the whole supervisory board, as usual, but by its chairman alone. In Prokom Software – the largest software producer and system integrator in Poland– its founder Mr. Krauze has the right to nominate 3 out of 5 members of the supervisory board including the board chairman. In another firm – Computerland – the right to nominate 2 out of 7 members of the supervisory board is awarded to a shareholder who has held the largest stake of shares (at least 5%) for the longest period of time (no shorter than 6 months).

Leveraging control through hierarchical structures (pyramids) seems to be much less popular than preferred shares. We noted the appearance of this device only in 6 cases. A good example of such hierarchical structure is the economic "empire" of Jan Kulczyk, the richest man in Poland and one of the richest in Central and Eastern Europe. Jan Kulczyk and his wife possess, through two private (non-listed) entities (Kulczyk Holding and Kulczyk Privatstiftung registered in Austria), significant stakes in: Warta S.A. (Plc.) – the second largest insurer in Poland – Polish Telecom TP S.A. (both are among the biggest corporations listed on the Warsaw Stock

Exchange), and many others. Another example could be Mr Ryszard Krauze who controls - through Prokom Investment (private) and the above-mentioned Prokom Software (public) – a large variety of other corporations, including: Wirtualna Polska (Wirtual Poland – the largest portal) and Softbank (a public corporation providing sophisticated software for banks). In about 20 cases it was observed that control was leveraged through own-share purchase executed by subsidiaries. In 8 corporations the block owned by a subsidiary was the largest one with an average size of 22%; in 5 cases it was the second largest (average size 13%).

Wawel – a candy and chocolate maker – has two subsidiaries, WIK and DOT, which hold together 20% votes of Wawel. Wawel itself is controlled by Mr Malek (21% of votes), who is also chairman of the supervisory board. Altogether, directly and indirectly, Mr Malek controls 41% of votes. Compared to previous years the subsidiaries are now employed more frequently, while cross shareholdings are less common (only 2 cases). The leverage action undertaken through subsidiaries could be additionally supported through purchase of own shares by the corporation in question. Since January 2001 any corporation is allowed to buy up to 10% of its own shares to "...defend against direct, significant damage to a company"¹⁰. So far we have not registered any case where such a device was employed.

In some corporate statutes voting cap was found to be used as a control device and a handy solution to defend against a take-over threat. In the media group Agora no shareholder can execute more than 20% of votes (except for holders of preferred shares), unless they have at least 75% as a result of a mandatory bid for all outstanding shares. A similar solution was introduced by Computerland. According to our re-

¹⁰ Before January 2001 a corporation was not allowed to buy own shares.

view of statutes, the utilization of voting cap is not predominant. Since the beginning of 2001, authorized capital has been introduced by a new company law. It provides for management (upon decision of GSM) to issue – within 3 years - new shares of total value not exceeding $\frac{3}{4}$ of existing share capital. This measure was introduced to improve company ability to tap the market at the right time. However, it can also be used as an anti-take-over device, especially if the management authorization allows the issue of shares without pre-emptive rights. It is too early to judge the popularity of this device among public corporations. So far only in a couple of corporations have shareholders agreed on authorized capital.

6. Evolution of control concentration

The above data on blockholding refer to the end of the year 2000. It is also worth to look at the concen-

tration evolved over the whole decade (tables 2 and 3, figure 5). In 1991, with few public companies on the market, concentration of voting control was very moderate. The median size of the largest block (shareholder) amounted to 18% and Q4 to 47%. In the case of the second largest blockholder it was 10% and 17.8% respectively. Since that time a systematic increase in the size of blocks has been observed although the pattern of concentration has varied. Between 1991 and 1996 an upward trend was very slow with two years (1993 and 1996) of de-concentration. Since 1996 the concentration process has accelerated. The cumulative distribution of firms by voting blocks was getting closer to the 45% threshold. Referring to distribution and concentration levels, it is worth noticing that in 1996 at almost 76% of public companies the largest shareholder had less than 33% of voting rights compared to 56% in 1998 and only 44% in 2000.

Table 2. Evolution of Control Concentration (largest blockholder in %)

Item/year	2000	1999	1998	1997	1996	1995	1994	1993	1992	1991
Q1	25,4	24,2	20,4	17,7	14,9	17,2	12,8	12,	17,5	7,5
Q2 (Median)	39,5	37,4	32,3	29,4	23,6	26,4	25	20,1	25,4	17,9
Q3	60,3	58	54,6	47,6	33,2	47,5	49,3	30,5	40,0	36,2
Q4 (max)	99,7	99,7	95,3	91,3	91,3	97	93,8	65,	47,2	47,2
Average	44,6	42,9	38,8	34,3	31,1	34,1	33,1	25,2	29,4	27,9
Number of observations	210	185	164	111	65	48	34	19	13	8
Number of blocks	208	183	159	107	64	47	34	18	12	6

Source: own computations

Table 3. Evolution of Control Concentration (second largest blockholder in %)

Item/year	2000	1999	1998	1997	1996	1995	1994	1993	1992	1991
Q1	5,0	5,1	5,2	5,2	5,2	5,1	1,1	0,0	0,0	0,0
Q2 (Median)	10,4	10,1	9,9	10,0	8,8	7,5	5,5	10,0	5,5	10,0
Q3	18,5	17,2	16,5	15,4	13,1	14,1	10,2	10,1	10,4	10,1
Q4 (max)	40,6	40,6	40,0	39,6	34,9	34,9	25	25,0	20,0	17,8
Average	15,6	14,8	14,2	13,5	11,6	11,3	9,7	12,7	10,7	11,6
Number of observations	210	185	164	111	65	48	34	19	13	8
Number of blocks	161	143	130	88	52	40	25	13	5	5

Source: own computations

The consolidation trend needs further investigation as the changes in ownership and control patterns may reflect new companies coming to the market or it may be also the case that some companies were

subject to concentration while others were able to disperse ownership and control. Both the decreasing number of newcomers and value of the IPO market in 1998-2000 strongly support the consolidation hypothesis. The period of 1997-1999 was also a time of

many tender offers on the market. The amendment to the law on public trading in securities shifted the threshold for mandatory bids from 33% to 50% thus reflecting both pressure of the consolidation trend and the authorities' hope that this move would slow the process of company withdrawal from the market. The de-concentration periods in 1993-1996 may be

reflections of the strong market performance (bullish markets) which attracted new share issues and decreased the stakes of founders.

However, 1997 with its record number of new public companies and IPO market value draws a question with this argument.

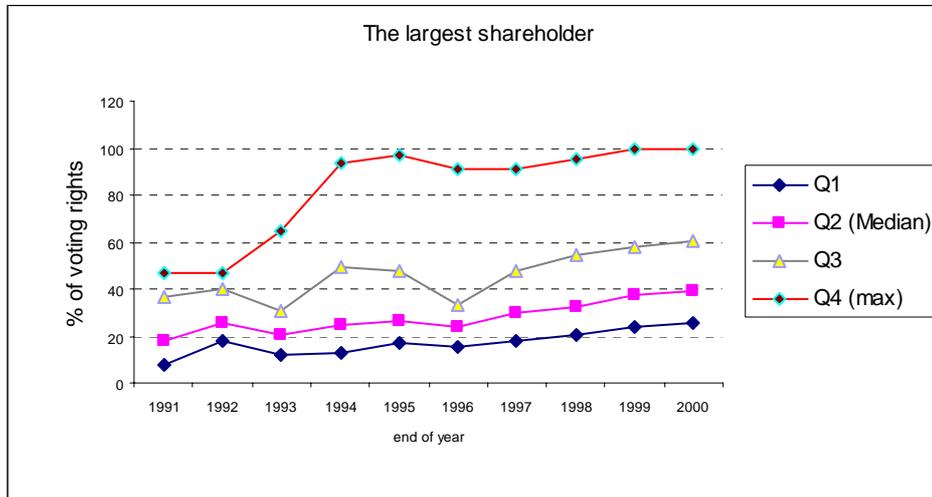


Figure 5. Evolution of control concentration (1991-2000)

What were the reasons for the overall consolidation trend? Corporate governance literature suggests the following answers. La Porta et al (1996) suggests that ownership concentration is the investors "response" to poor protection of shareholder rights. In fact in recent years several cases of expropriation of minorities took place – ranging from opportunistic manager behavior, tunneling and self-dealing by strategic investors, failures to provide the public with important information about company, insider trading and paying the minorities significantly lower prices than the ones paid for controlling stakes. The investors' perception of protection and especially enforcement of minorities' rights is rather poor.

Poor enforcement of minorities' rights made the consolidation of ownership and control inevitable, as it addresses the problem of unaccountable managers – evident when owners are dispersed (Shleifer and Vishny 1986).

However, part of the process was caused by changes in privatization strategies – combining flotation with a sale to the so-called strategic investor. Poor enforcement allowed strategic investors and other blockholders to extract private benefits at the expense of minority shareholders. Additionally, very often the prices offered to minorities by strategic investors were very unfair. The liquidity of these companies was also affected. On the other hand, new family companies entering the market were not able to attract new institutional investors – partly because of their size (low liquidity) and partly because of their unwillingness to transfer control to the market, and poor management.

The weak shareholder protection argument may be somewhat justified by the difference in the size of blocks owned by domestic and foreign investors. The average size for the largest blocks owned by foreign strategic investors is much higher (67%) than those owned by domestic companies or individuals (43.5% and 40.6% respectively¹¹). This difference is also evident in the case of the second largest block. Foreigners with weak knowledge and access to courts and judges prefer bigger blocks to execute their rights than domestic investors usually more familiar with a local legal system. The same situation is reported in Russia where legal protection of shareholders is very poor (Shleifer & Vishny 1996).

The opportunism of Polish managers was responsible for at least a part of the concentration trend. In the short history of the Polish stock market there were many examples of empire building and high managerial remuneration contracts – especially among former state owned companies privatised through IPO. Many of them within a couple of years were turned into over-diversified conglomerates. All of these corporations entered into heavy restructuring (including firing "old" managers, many of them were directors of these companies before privatisation) in the wake of pressure from foreign strategic or institutional investors.

Two factors – we tend to believe – allowed for managerial opportunism to develop in the early 1990s. Firstly – privatisation strategies employed by the state combined with the underdeveloped capital

¹¹ The second figure would be slightly higher if we combined stakes owned by founders into one block.

market (a lack of domestic institutional investors). Many state-owned enterprises were privatised through IPO (sometimes with significant stakes left in state hands) while managers and employees gained a privileged position in privatisation due to political reasons. Many enterprises, which later were publicly listed, were privatised by management and employee buy-outs. Therefore the position of managers became very strong. The second factor was weak competition - at the beginning of the 1990's many product markets, although formally liberalised, were still protected by monopolies and (declining) tariffs. Domestic rivalry was non-existent and inflow of FDI quite thin due to an unstable and discouraging economic environment. The competition was thus unable to force corporations to market adjustments in a short time, especially if they inherited a monopolistic position. This situation created room for managers of public, formerly state-owned corporations (which constituted the largest fraction of public corporations) to engage in ineffective expansion projects.

Besides political motivation and eagerness to create more efficient corporate structures, the change in privatisation strategies - in favour of strategic investors - may be attributed to the Zingales (1994) proposition on a control premium attached to large blocks of shares.

We suppose - although it needs further testing - that the State Treasury's willingness to cash and capture premiums for control engendered the preference to sell large stakes to strategic investors, rather than to disperse the ownership on the market (through IPO).

Figure 6 presents the structure of some privatisation IPOs over the last decade. The lower side of the plot represents the fraction of shares reserved for sale to a dispersed public (physical persons or legal enti-

ties), and the upper, darker part the shares reserved *expressis verbis* for one (strategic) investor or left in state hands for further disposal (usually for sale to one investor. The fraction of shares left in state hands usually included shares reserved for restitution purposes and for financing pension reform. Altogether it was about 10% of shares of each IPO). It can be noticed that relations of both fractions of shares changed over time. In the first half of the 1990's privatisation IPOs were structured with the preference for ownership dispersion. For example, in the case of Kable, Próchnik, Polifarb Cieszyn about 80% of the shares in each company were sold to the market by the Ministry of Privatisation. In the mid-1990s the economic climate in Poland improved enough (GDP growth in 1995 amounted to 7%) to allow the Ministry of Privatisation thus to gain better prices as well as to privatize much bigger companies than before. Simultaneously the policy makers realised that privatisation could be a very efficient source of budgetary revenues - the only source of money to cover the high costs of structural reforms (pension, health service reform, etc.).

In that situation the Ministry of Privatisation was unable (due to technical reasons) to increase the pace of privatisation and therefore decided (maybe unintentionally) to increase revenues through cashing out and capturing premium for control. This could be achieved only by selling large blocks of shares to a single investor, so they applied different strategies of combined selling of a company to the market and to a strategic investor. In a few cases they sold the stakes still possessed in privatised companies already introduced to the public market (TPSA, BPH, Pekao and other banks) or they have an option to do so (KGHM, PKN). In the case of PZU (the biggest Polish insurer) the sale to the strategic investor (Eureka) took place before the announced IPO.

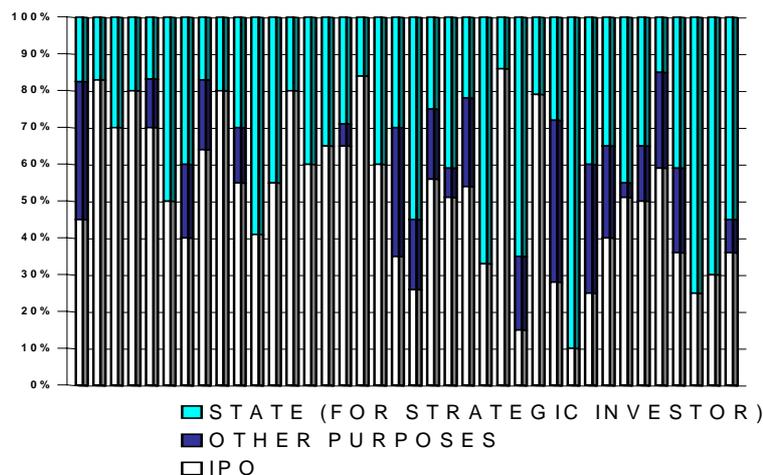


Figure 6. Structure of some privatization IPOs (1991-1999)

Conclusions

Three broad conclusions can be drawn based on control data presented above.

Firstly, corporate control in Polish listed corporations is concentrated to an extent that is observed in most of European continental countries including European transition countries; however the separation of ownership and control is rather modest; large blockholders are almost alone major players at corporate arena.

Secondly, the concentration of corporate power developed steadily through the whole last decade in spite of the initial declarations to build up Anglo-Saxon (i.e. with dispersed and widespread shareholders base) style stock market.

Thirdly, having in mind the above one can speculate about policy mix that might have resulted in such concentration as well as prevailing agency conflicts (controlling versus minority shareholders). These speculations can be also extended to the (un-easy) future of the stock exchange.

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