

Privatization in Former East Germany

Lauren Bloomstein



Introduction

As a result of the ravages of Hitler, Stalin, and 30 years of isolation after the construction of the Berlin Wall, East Germany had been reduced to a virtual third-world nation in comparison with West Germany. (Borneman, pp. 8- 14) Despite their proximity, years of communist rule on one side and a free-market economy on the other created vast differences between the two: lifestyle, prosperity, demographics, productivity, resources and their utilization, mechanization, and opportunity. ("No Escape," pp. 6-7) High unemployment and increased taxes following reunification placed great strain on the German people. (Kinzer, p. A14)

One of the factors contributing to the building of the Berlin Wall in 1961 was the continuing exodus from the East. As a consequence of intolerable living conditions and attempts to collectivize the farmlands, 200,000 East Germans fled in 1960, 54,000 more than in 1959. (McAdams, pp. 48-49) After an additional 30 years of isolation in a socialistic state, the East Germans had lost their ability to think independently. The older ones were more willing to accept authoritarian rule, since they lacked the ambition and ability to take risks. The East Germans were also "noticeably less worldly and sophisticated than West Germans... more subdued..." (Ardagh, 1987, pp. 338-39) Following reunification differences in outlook became more apparent. They were jealous of the Westerners' prosperity and did not understand why more was not given to them. (Kinzer p. A14) The younger ones migrated West in search of a better life. (Hall, p. 31) Their exodus created higher unemployment and greater job competition in the West. In the long run this may help hold down wages, thereby preventing increases in manufacturing costs, and may result in more competitiveness in the international market.

Had there not been a migration of younger people from East to West, the unemployment rate in the East would undoubtedly be higher. This migration has resulted in an increase in the proportion of elderly in the population of Eastern Germany, accompanied by a very low birth rate in the East. ("Germany's Mezzogiorno," p. 10)

As the Eastern German population continues to age, a growing number will become even more dependent on the government. A smaller Eastern work force and higher unemployment in both the East and West have put a greater strain on the government. ("No Escape," p. 5) Higher unemployment has also resulted in more welfare recipients, with the final impact being higher taxes. (Kinzer, p. A14)

The entire unification process is a unique occurrence. With the sudden global demise of communism, the former communist bloc nations have fallen into turmoil. As precipitous as it may have appeared to many, the seeds of destruction had been growing for a considerable time. Governments no longer were able to subsidize insolvent industries, production had declined, products were substandard, equipment

outmoded and in disrepair, and pollution was severe. As a result of inept management, communist nations were no longer functional. With no government left to run the state-owned enterprises, new owners had to be found. Just as the communists had nationalized industry, now the reverse-privatization was occurring.

In this essay, I first explain privatization in a general sense. I then discuss Treuhand, the agency established to privatize the industry of the former East Germany - its characteristics, accomplishments, and the criticisms it has encountered. I conclude by emphasizing the success of Treuhand and its contribution not only to a strong unified Germany, but to the entire world.

Privatization

What is privatization? Simply put, privatization is the process by which a state either wholly or partially divests itself of state-owned enterprises. New ownership may be any of the forms recognized in a market economy: individual ownership, partnership, or corporate (stock) ownership. In addition, the state may wish to retain a partial interest. It may make sense to divide a large industry into smaller components, either to prevent monopolies or to simplify the privatization process. In the case of a totally unsalvageable industry, it may be necessary to shut the business down and dispose of the assets, equipment, and physical plant in the most expedient manner possible. ("Treuhandanstalt: The Chance...", p. 9)

Rationale for Privatization

The major reason for privatizing is to reduce the cost of running government and to improve the quality of products and services, thereby enabling an economy to become more competitive and more prosperous. Privatization also brings in additional funds which can aid in reducing an internal deficit or an external debt. (Lieberman, pp. 5-6) These are not new ideas. Privatization has been achieved in South America, Mexico and the United States. In many, if not all, of these situations, cost savings is the main objective. In Eastern and Central Europe, the objectives of privatization included the introduction of a market economy, increased economic efficiency, the establishment of democracy, and increased government revenues. (Dhanji, p. 1)

Methods of Privatization

Privatization occurs when a state no longer wishes to control an industry. Ownership is then transferred to a non-governmental owner. The issues to be addressed by those conducting the privatization are present ownership, future ownership, compensation to the current owner, and the consequences of the transfer. There were several modes of privatization in Eastern and Central Europe used to privatize industries.

Holding companies can be established to implement privatization. Properly managed, this method can make for an orderly and equitable transition. However, there is the risk that the holding company may lack the expertise or may not act in a conscientious manner. Also, internal privatization transfers ownership to employees of the company. Finally, external privatization gives ownership of the company to persons or entities (corporations, etc.) outside the enterprise. (Dhanji, pp. 14-24) External privatization includes distributing shares of a company to all citizens and selling shares to domestic, foreign, or institutional investors (e.g., banks, stock funds, insurance funds, pension funds, and universities).

All of these modes have been utilized to privatize the former communist bloc countries with varying

degrees of success. Another form of internal privatization, politely termed "spontaneous privatization," occurs when management perceives that government is incapable of interfering and assumes control of the company, justifying its actions on the grounds that those who work the land own the land. For example, because many generations passed since land in the Soviet Union had been privately owned, there was no chance that claims of prior ownership existed. Also, "land" was loosely interpreted to include buildings and industry on the land. (Lieberman, p. 21)

Not waiting for ownership and leadership to be assumed by unknown opportunists, Germany placed the state-owned enterprises of the former East Germany under the control of a single holding company, the Treuhandanstalt (Treuhand). Treuhand utilized all forms of privatization - except for spontaneous privatization and the outright giveaway to effectively privatize the entire East German economy.

Treuhandanstalt

Treuhand came into existence by a resolution of the Council of Ministers on March 1, 1990, under the Modrow government of East Germany. The original agency was composed of 15 branch offices and approximately 600 employees. (Treuhandanstalt: Working..., pp. 8-9) On March 18, 1990, the first freely contested election in East Germany took place, which paved the way for deMaiziere to become the prime minister. (Darnton, pp. 24-26) On June 17, 1990, the East German Parliament under deMaiziere passed the Treuhandgesetz, or Trusteeship Act, which formally charged Treuhand with the responsibility for privatizing East German industry. (Treuhandanstalt: Working..., pp. 8-9) When East Germany and West Germany merged on July 1, 1990, and assumed the constitution and currency of West Germany, Treuhand was commissioned as the official privatizing agency. Roughly two-thirds of its members were former East German representatives and one-third West German representatives. (Treuhandanstalt: Promoting..., p. 5)

Purpose

When first established by East German on June 17, 1990, Treuhand had four goals. The first stipulated removal of government interference in commerce by reducing the commercial activity of the state as rapidly and extensively as possible through privatization. The second established that maintaining existing jobs and creating new ones was of paramount importance by keeping as many companies as possible competitive. The third expanded the restructuring of East Germany to include real estate, but limited it to commercial use. The fourth goal was to grant depositors the legally vested right to a share in the state-owned asset to offset the unfavorable currency conversion rate on June 2, 1990.

(Treuhandanstalt Promoting..., p. 5) It is not clear who "depositors" are, but it is presumed that this was an attempt to safeguard against a giveaway of East German assets.

Organization

When originally established by the now defunct East Germany, Treuhand had 200 employees. At the peak of operation its rank swelled to 4,000 full-time employees plus 400 full-time consultants, mostly of West German origin, distributed among 15 regional offices and headquarters in Berlin. During the initial stages of organizing and "gearing up," experienced managers from large corporations were lent to Treuhand. These temporary managers who offered considerable expertise, were gradually replaced by newly hired full-time personnel. Also on loan were senior tenured bureaucrats from German governmental agencies. An additional group included senior managers nearing retirement or retired managers who had been persuaded to assist this special cause. Attracting younger staff members was not difficult since the lure of good pay and the opportunity to make high-level contacts, held great appeal. (Dodds, pp. 5-12)

Philosophy

In 1948 when Ludwig Erhard, an economic associate to Prime Minister Adenauer made the bold and controversial decision to end wage controls, price controls, and rationing, West Germany shifted from a command economy to a market economy. (Craig, p. 43) Given this precedent, it was reasonable to remove the command structure as expeditiously as possible from East Germany in 1990. Treuhand attempted to do this and still provide a "soft landing" for those people who had been under the East German rule for forty years. Dr. Detlev Rohwedder, the first director of Treuhand, succinctly stated the philosophy of Treuhand as rapid privatization, resolute restructuring, and careful closure. Treuhand felt that an aggressive approach to selling the formerly state-owned enterprises could be expected. To carry out the conversion, Treuhand first assumed ownership and control of the entire inventory of state-owned enterprises and then disposed of them. When unable to sell a business in existing form or return a company to a prior owner, measures were taken to encourage a sale (e.g., restructure to smaller units, offer financial incentives, etc.). If still unable to sell the business, termination or closure would be conducted prudently. (Treuhandanstalt: Promoting... p. 6) To conduct the sale of the formerly state-owned enterprises, Treuhand was guided by certain principles. For example, Treuhand encouraged foreign investment because this would reduce the cost that the Germans would have to bear. One of the greatest obstacles was the resolution of prior claims by either the owners or the heirs who made claims to land, businesses, and non-commercial real estate. Treuhand also sought to improve infrastructure as quickly as possible. (Treuhandanstalt, The Chance... pp. 4-5) To preserve jobs, Treuhand made concessions relative to sale price, tax abatements, and environmental cleanup. (Dodds, pp. 9-11) Additionally, Treuhand addressed the problem that some businesses were overstaffed and, despite the commitment to save jobs, reductions were needed. To lessen the subsequent impact of unemployment, Treuhand subsidized wages, often as much as 90 percent, and also provided benefits for the unemployed. (Treuhandanstalt, The Chance... pp. 5-7) It attempted to retrain workers and provide youth with skills by establishing training centers in the Eastern states. (Kappler, p. 413) Treuhand granted flexibility for those purchasing an entire enterprise, individual subsidiaries, or parts of assets by price negotiations based on prospective purchasers providing job and investment guarantees. (Treuhandanstalt, The Chance..., pp. 12-13) However, it frowned upon opportunists who sought quick profits by purchasing and then dismantling one of their holdings. (Dodds, pp. 23-24) Finally, Treuhand encouraged management buyout plans, either by existing managers, new managers, or a combination of the two. (Treuhandanstalt, The Chance.... pp. 17-18)

When evaluating an offer, Treuhand followed specific criteria. Job guarantees were essential. Treuhand also sought an investor with knowledge of the industry, a plan to train employees, and a willingness to invest capital into the company rather than depend on Treuhand for funding. The purchaser also had to plan to continue operating the business and not dismantle the company by selling off assets and land separately. Finally, it was essential for the investor to have a strategy that would carry for the next three to five years. (Freymark) With these reasonable guidelines established, Treuhand converted the East German command economy to a market economy.

The East German Economy

When Westerners entered East Germany after the fall of the Berlin Wall, it became apparent why the centrally planned, command economy had failed. Although East Germany was reportedly in better shape than other Eastern Bloc nations, in general its industries could not compete with those in the West. There was little demand for inferior Eastern products. Furthermore, by artificially setting the value of the ost mark and deutsche mark at 1:1, Eastern prices were non-competitive. (Prior to unification the actual rate of exchange of the ost mark for the deutsche mark had been approximately 6: 1.) The communists had not invested adequately in maintaining and upgrading their businesses. Half of the

industrial machinery was at least ten years old, and 20 percent was at least twenty years old. This had happened because the government maintained solvency by taxing the profits out of the businesses, leaving no money for reinvestment. (Reier, p. 48) East German infrastructure also was inadequate. Roads were incapable of handling the volume of cars and industrial traffic. Telecommunication lines and equipment were substandard. Environmental damage was so severe that it was deemed necessary to phase in the stringent standards of the West gradually. At the time of unification, 80 percent of electricity was produced from highly polluting lignite (brown coal). (Treuhandanstalt: the Chance..., pp. 7-8)

Bitterfield is called by its residents "the dirtiest city in Europe," and with good cause. It is the center of the East German chemical industry. Smokestacks bellow noxious lignite smoke everywhere. Respiratory diseases are common, and there is a high incidence of cancer. The local picnic spot is called "Silver Lake," its name derived from its color due to the chemicals in it. "Silver Lake" is not the only polluted body of water. One third of East German rivers are dead. The air is no better; in many cities pollution exceeds the safe limit 10 to 100 times. (Long, pp. 18-21).

The organization of the former East German economy included businesses which were large horizontally- or vertically-integrated Kombines, state-owned and centrally controlled. Only two percent of the labor force were outside the socialized sector and consisted mostly of artisans, farmers and small store owners. Prior to the collapse of the East, two-thirds of foreign trade was with other planned economies, such as the Soviet Union. With most of its trading partners in collapse, goods piled up in storage and employment dropped by 18 percent. (Kurian, p. 222)

Treuhand's Activities

In only four years, Treuhand succeeded in converting the entire economic structure of the former East Germany from a command economy to a market economy, resulting in revitalization and growth in the East. When Treuhand began functioning in October 1990, it assumed responsibility for over 8,000 combines and state-owned enterprises, which represented 97 percent of all of East German industry. (Treuhandanstalt: Working for..., p. 8) The remaining 3 percent of industry was already private industry. The combines were eventually separated into smaller units for purposes of privatization. By the end of 1994, Treuhand had privatized approximately 98 percent of companies, businesses, and industries in the Eastern states. In all, 119 large and medium-sized former state-owned enterprises were closed, and 3,340 have been, or are in the process of being liquidated as of December 1994, when Treuhand ceased to function. (Focus on.... p. 2)

Approximately 14,000 state-owned enterprises of the former East Germany were eventually privatized (Focus on..., p. 2), including facilities given to municipalities and businesses returned to rightful owners who had been victimized by the Nazis and communists subsequent to 1949. (Dodds, pp. 35-36) The latter proved to be one of the most challenging and difficult problems for privatization and was overcome in March 1991 with the Transfer of Assets Act, which gave priority to jobs and investment over prior claims. In keeping with the Treuhand philosophy of rapid, expedient action, local authorities could immediately use properties, pending final resolution (Treuhandanstalt: Working for..., p. 15) Ultimately, Treuhand took the position that investment and jobs were the primary concern. Former owners, unwilling or unable to proceed under these premises, would be compensated for their property by Treuhand. (Treuhandanstalt: Promoting the New Germany, p. 9)

One fifth of the privatizations were management buyouts, and 92 percent of the businesses were taken over by Germans, representing 80 percent of cash investment. (Freymark) Foreign investors generally were large, highly visible companies, such as Dow Chemical, Coca-Cola, McDonald's, Philip Morris,

and General Motors. As of October 1994, DoA Chemical and Gazprom of Russia were preparing to invest in Buna, a polyolefin plastics manufacturer. ("Company News..." p. D3) Although foreign investment accounted for only 8 percent of the businesses, the cash invested accounted for 20 percent of the investment in the region. (Freyemark)

In addition to selling businesses, Treuhand also sold buildings and land. In East Germany much of the social structure had fallen under the company umbrella. This included vacation time, health care, cultural activities, day care and education, housing, etc. (Cohen, p. 1) Treuhand transferred administration to the community. (Focus on..., pp. 2-3)

When state-owned enterprises were unsaleable, Treuhand restructured them and invested the necessary capital to increase their attractiveness to buyers and make them saleable. (Focus on..., pp. 2-3) One notable example was Eko Stahl AG in Eisenhüttenstadt, the largest steel producer in the Eastern states. The Treuhand agency invested DM 500 million (\$318.5 million) during four years of efforts to privatize Eko Stahl. This included the building of a continuous-casting hot-rolling mill. (Cohen, p. D1) By so doing, Eko Stahl personnel director Peter Neumann predicted steel could be produced at 80 percent of the cost of other steel producers. Treuhand's efforts were successful, and Eko Stahl was sold to Cockerill Sambre S.A. shortly before Treuhand's mandate expired. (Penson, p. 46)

Privatization contracts included guarantees of employment by contractual promises to hire or keep existing employees, totaling 1.5 million jobs. Integral to many contracts were guarantees of capital investment, totaling DM 180 billion. (Focus on..., p. 2) Treuhand sought to obtain true market value for each venture, but market value was sometimes difficult, if not impossible, to assess. The conversion to deutsche marks at 1:1 or 1:2 for ost marks heavily favored those in a cash position, since the conversion on the open market prior to the unification was one deutsche mark for six ost marks. Those in a cash position tripled their cash. Those with debt tripled their debt. In former East Germany, the government shifted its debt onto individual firms. Thus, the books of these companies sometimes showed considerable debt owed to state-owned banks of the former East Germany. It then became the responsibility of the successor agency to refinance this debt. (Dodds, p. 19) In order to make these companies attractive to buyers, price concessions were given in exchange for job guarantees and/or promises to invest capital. Other incentives included tax abatements and wage subsidies. Treuhand recognized that some companies were overstaffed and were sympathetic to both prospective buyers and the staff about to be let go. Often, Treuhand authorized the state to pay up to 90 percent of part-time and unemployed workers' salaries. The cost of environmental clean-up was sometimes shared by Treuhand. (Treuhandanstalt: the Chance..., p. 7) If detoxification costs were prohibitive, Treuhand supported moving the operation to a "green field" site. The long term objective was to create a strong economy. (Dodds, p. 11) Through its activities, Treuhand experienced failure as well as success. And in the cases presented below, I will show how the privatization of a trucking company resulted in closure, while a compact disk manufacturer experienced a fresh start and a refrigerator manufacturer was saved.

Pilz the Trucker - A Case for Closure

After fifty years of "milking" an industry, it is not always possible to resurrect it. Such was the case with Transmercur GmbH, a trucking company with headquarters in Leipzig. After Treuhand took over, Eberhard Pitz was asked to head up Tyansmercur and "find a Western partner." He had previously been technical director of the predecessor organization, VEB Handelstransport, but refused to assume the role of director. Pitz and Treuhand inherited a fleet of 700 trucks, most of which were more than 14 years old with no spare parts available. (Glouchevitch, pp. 190-91)

As a manager under East German control, Pitz said that management had little power or control. Under

the socialist system, the working man and working woman were very important. Therefore, the party heads were essential in the workers' movement. This left the manager in the middle, responsible for meeting production goals but lacking power to discipline unproductive employees or implement changes. Realizing this, employees shunned positions of responsibility. (Glouchevitch, p. 192)

Beyond the aging trucks, Pilz had other problems. Because of the possibility of prior claims, Transmercur had no clear claim to the land on which its offices and depots were built. With no collateral, Pilz was unable to secure financing for a management buyout. Additionally, with the increasing demand for West German goods, Western supermarket chains quickly opened up in the East and used their own trucking companies rather than local delivery services. Pilz was unable to export local products because there was no demand, and the currency revaluation overpriced local goods. Furthermore, Pilz was required to comply with West German law. For example, fresh produce had to be stored and shipped refrigerated to safeguard against spoilage. He leased 40 refrigerated trucks and built a refrigerated storage depot, but still was unable to succeed. (Glouchevitch, p. 193)

The sad story here was not that of Mr. Pilz; he had a good reputation and had already refused lucrative offers out of loyalty to Transmercur. The tragedy was that 600 of 1,000 workers had already been laid off, and the company would probably be closed in the near future. (Clouchevitch, p. 194).

Since Treuhand was not in the business of simply giving away businesses, a reasonable evaluation of its value had to be placed on Transmercur before privatizing. As with most state-owned enterprises in a socialist economy, Transmercur was locally managed, with no authority. The state made all decisions and allocations, Further, the state often shifted deficits to the company to make the government appear solvent and the company inefficient. (Glouchevitch, p. 194) The bookkeeping system was a charade.

There had not been clear title to the land and the 14-year-old trucks were fully depreciated. This left Transmercur with no tangible assets, questionable accounts, an aggressive new manager, and a payroll of 1,000 employees. As Pilz had pointed out: "We should have wiped out all the companies and started from scratch..." Of course, had this been done without first attempting to salvage Transmercur, 1,000 workers would have accused Treuhand of being insensitive, uncaring, and too quick to close the business. (Glouchevitch, p. 194)

The Transmercur example illustrates some of the obstacles and criticisms faced by Treuhand. The obstacles included lack of accurate financial data, the possible claims of pre-war owners, remote and uninvolved management, and environmental contamination worse than had been anticipated (Glouchevitch p. 189). Numerous criticisms included demand for job creation and retraining programs, additional incentives for potential investors, and ceasing the continual closure of factories (Ardagh, 1991, p. 433).

There are alternative explanations for the unsuccessful privatization. The arrival of West Germans created tensions in the East. The West German citizens arrived in large numbers flaunting, as some alleged, their knowledge and skills. Although it was acknowledged that the East embraced the constitution, laws and economics of the West, East Germans felt that everything was happening too fast and that they had been made to feel inferior. In all likelihood this was unavoidable since the Westerners did understand the Western laws and the Western economy better than the East Germans. On the other hand, the West Germans were irked by what they perceived as the slowness and laziness of the East Germans. As a result of working in a structure where supplies were erratic and shortages common, the East Germans were not accustomed to working at the Western pace. (Ardagh, 1991, pp. 447-48)

Pitz the Compact Disc Manufacturer: A Fresh Start

An example of the setting up of a successful business is that of Reiner Pilz, an East German compact disc manufacturer, who migrated to the West and became prosperous. He sought to return to his homeland and built a factory in the town of Suhl, in a joint venture with Robotron VEB, an East German computer and office equipment manufacturer. Suhl is a quiet town in the forested Thuringen hills with a minimal tourist business. Some industry exists there, most notably a shotgun manufacturer. Incredibly, the town vetoed Pilz's business proposition on the grounds that the proposed site was too close to a rifle range used to train Olympic athletes. (Giouchevitch, p. 195)

However, Bruno Endter, mayor of Albrechts bei Suhl, a village of 1,000 people five miles away, saw the opportunity to create 300 new jobs. He contacted a Robotron executive and a deal was struck. Pilz was able to realize his dream of returning to East Germany, and the East Germans gained 300 badly needed jobs. (Glouchevitch, pp. 195-98) The mindset of the people of Suhl was so far removed from the dynamics of a market economy that it becomes apparent that some people are unemployable as long as they seem to be content trying to feed their families with the medals of their rifle team. Fortunately, however, at least some East Germans were able to see beyond the Thuringen trees and consider the whole forest.

Operation Bootstrap: Building a Better Refrigerator

A third case involves Foron, a former East German refrigerator manufacturer which was given another chance. Like Transmercur and many other Eastern companies, Foron was suffering from outdated technology. Treuhand had judged Foron to be unsalvageable and decided to close it. However, Foron had been working on producing a refrigerator free of atmosphere-damaging fluorocarbons. Treuhand therefore invested \$3.4 million in Foron, and it was privatized in late 1992 in a joint venture with a London-based fund, the East German Investment Trust which purchased 47 percent of the company. West Germans, Berlin Kapital-Management GmbH., bought 26 percent of Foron. The remaining 27 percent was purchased by four Foron managers. (Protzman, 1994, p. DI)

Monetary and Social Costs

The costs of privatizing the former East Germany were high. The net cost was DM 270 billion (\$174.3 billion). Expenditures totaled DM 344 billion (\$222 billion) and included debt payoffs of the former state-owned enterprises, environmental cleanup, subsidies, and unemployment benefits, with debt payoffs and subsidies being the largest components. Treuhand collected DM 74 billion (\$47.7 billion) in revenues. Anticipated costs of DM 69 billion (\$38.2 billion) to finance successor agencies are also included in these figures. (Focus on..., p. 4)

The impact of these costs on the West German states has been enormous. Taxes in Germany have already increased ten times between 1993 and July 1995 (Shales, P. A8), and Provisions have been made to amortize the cost over the next thirty years. (Kappler, P. 233) In 1990 East German consumption resulted in a boom in the economy. (Giouchevitch, pp. 188- 89) However, a year later, the economy was faltering. The government raised taxes to help finance the cost of reunification and the inflation rate increased. ("Will Germany's Boom..." P. 73) By the end of 1994, inflation was 4.2 percent. ("German Inflation Up," P. D4)

Taxes and inflation were not the only problems. Unemployment also rose. As industries in the former East Germany were privatized, the work force decreased. The overall unemployment rate for Germany at the end of 1994 stood at 9.6 percent, the highest in forty-five years. (Whitney, 1994, P. A3) In August 1995, it was reported in the Wall Street Journal that as a result of a very strong mark and the highest wage costs in the world, companies such as Volkswagen AG and Daimler Benz Aerospace AG have

been attempting to reduce their labor costs, resulting in higher unemployment. (Marshall, "Jobless..." P. A5) Unyielding unions have negotiated wage increases higher than the inflation rate. (Marshall, "International: Germany Sees..." P. A10) Another observer states that the unemployment rate appears to be "leveling off," but feels that many of the unemployed Eastern Germans may never be re-employed. (Shlaes, P. A8)

Criticisms of Treuhand

There has been no dearth of criticism of reunification. For example, Treuhand has been accused of being too eager to finish the task and of restructuring companies inadequately. (Balasubramanyam, P. 83) However, other Germans felt the process was too slow and that the guidelines were vague. Some claimed Treuhand tried too hard to save unsalvageable businesses (Glouchevitch, pp. 189-94) and worked too extensively to sustain "obsolete" companies, but was also too quick to close businesses. ("Hand of Kindness..." P. 71) Some alleged Treuhand privatized with inexperienced staff who allowed ruthless entrepreneurs to seize unbelievable bargains in East Germany. (Glouchevitch, p. 189) There was also some sentiment that Treuhand attracted little foreign investment and that tax increases were required because of the overly generous unemployment policies of the East. (Balasubramanyam, p. 83) However insignificant some of these criticisms may appear in retrospect, emotions became very intense, so much so that the director of Treuhand, Detlev Karsten Rohwedder, was assassinated in his home on April 1, 1991. (McAdams, pp. 219-20) Rohwedder's deputy, Brigit Breuel, succeeded him and remained director until privatization was completed. (Treuhandanstalt: Working..., p. 31)

Privatization After Treuhand

As Treuhand was preparing to close its doors, privatization without Treuhand was gaining momentum in Germany. The German Parliament (Bundestag) has approved plans to privatize the postal service, Lufthansa Airlines, and Deutsche Telekom. ("German Privatization Plan," p. D5) On September 13, 1994, Lufthansa announced that 65 percent of its stock would be offered to private investors. A second offering would later fully privatize the airline. ("Lufthansa to Sell Shares," p. D18) In October 1994, Goldman Sachs began offering shares of Deutsche Telekom, the state telephone monopoly. (Nash, p. A4) As with Lufthansa, Deutsche Telecom was not profitable, and the Bundestag was hoping to save money and to improve the efficiency of both industries.

Conclusion

Treuhand has been described as "born out of chaos, and destined to be phased out without ever functioning normally." (Dodds, 7) However, Treuhand functioned in a manner consistent with the basic Rohwedder philosophy: rapidly privatize; preserve jobs as much as possible; protect human and property rights; encourage investment of capital, both domestic and foreign; establish educational programs; and generate conditions that would permit the Eastern states to work toward attaining economic parity with the West. As there was little to start with, virtually the entire industry of the former East Germany has been, or is in the process of being, rebuilt. Mr. Pilz, the trucker, retrospectively concluded that Transmercury should have been shut down. Perhaps he was correct. However, had this kind of thinking become pervasive, Eko Stahl and Foron would also have been closed. Although criticisms had merit in specific instances, overall Treuhand certainly succeeded. No doubt many jobs were lost, but there really was not enough work to justify the large labor force. To ease the transition, generous unemployment benefits and opportunities for retraining were provided. In addition, the sentiments of the townspeople of Suhl, who valued the sanctity of their Olympic rifle range more highly than the opportunity to create 300 new jobs, must not be forgotten.

Treuhand has readily admitted that some mistakes were made. There was alleged dishonesty on the part of some Treuhand employees. Political pressure was exerted, and occasionally controls were inadequate. Especially in the early days of privatization, Western entrepreneurs practiced some "spontaneous privatization," unbeknownst to Treuhand. (Dodds, p. 17) However, as of January 1995, only six cases of fraud were in litigation out of a total of approximately 14,000 privatized companies. (Focus on..., pp. 5-6)

There is general agreement that the cost of privatization to taxpayers was high. However, given the prevalent socialistic philosophy, it was inconceivable that some German citizens should receive less social assistance than others. Many West Germans felt the East Germans were receiving too much aid, with the West paying the price and receiving nothing in return. The additional funds needed were generated by tax increases and issuance of bonds, which permitted the costs to be amortized over a 30 year period.

It appears that Treuhand did in fact perform the task with which it was charged. It privatized or closed well in excess of 90 percent of the state-owned enterprises of the former East Germany, assisted in creating an infrastructure to support these privatized industries, and was successful in creating new jobs. Training facilities were established to train young workers and retrain older workers. Capital, both West German and foreign, is flowing into the region. True to its word, Treuhand stopped operating on December 31, 1994, allaying fears that it would become another layer of bureaucracy, resembling the socialist structure it was created to dismantle.

However, there has been great discontent among the unemployed. Unwilling to comprehend that the totalitarian state was bankrupt, many have placed the blame for unemployment on Treuhand and the West. For these malcontents there is no answer. It is unfortunate that those who have suffered may never see the successes.

The prospects for Germany's future are bright. With the declining birth rate in the East, the potential work force is growing less rapidly or even declining; this will eventually lower the unemployment rate. As Eastern industry continues to grow, it is probable that workers will begin to migrate to the former East Germany, seeking job opportunities and homes close to work. Despite the present discontent, high unemployment, and high national debt, the future looks very promising for Germany, in particular the East. With outdated technology replaced, the Eastern states may in time even surpass the Western states economically. (Freymark)

Treuhand has written another chapter for future economics textbooks. Never before has the economy of a modern nation been changed so dramatically in a planned and peaceful manner. As economic efficiency is sought through privatization, it makes sense to evaluate Treuhand's achievements and relevance to other situations, notably the remainder of the Communist Bloc. With East Germany reconstructed, there is the opportunity to assist in the reconstruction of the rest of the former Communist Bloc, as the unified Germany has the expertise, experience, and Eastern Bloc contacts. (Freymark)

Privatization occurs in both market economies and command economies. In both types of systems, the goals are the same - cost savings and enhanced efficiency. The effect of privatizing is to remove a layer of bureaucracy, bringing management closer to production. Further, as the industry is removed from the protective umbrella of the state, it becomes more subject to forces of the market economy. Thus, the state-owned enterprise always functions in a command economy. Then privatization, whether in a command economy or a market economy, is always a shift to a market economy. However, for privatization to be worthwhile it must be cost-effective and must include costs of social services to catch the casualties.

References:

- Ardagh, John. *Germany and the Germans*. New York: Harper & Row, 1987.
- Ardagh, John. *Germany and the Germans After Unification: New Revised Edition*. New York: Penguin Books, 1991.
- Balasubramanyam, V. N. "The Treuhandanstalt, FDI and Employment in Germany." *International Journal of Manpower*. Volume 15, No. 6, 1994, pp. 72-84.
- Borneman, John. *After the Wall*. New York: Basic Books, Inc., 1991.
- Cohen, Roger. "A Plant Too Big for Germany to Close." *New York Times*, March 3, 1993, p. D3.
- "Company News; Dow Is Said to Be Near an Eastern German Purchase." *New York Times*, October 19, 1994, p. D3.
- Cowell, Alan. "Only Economic Jitters Unite Germans." *New York Times*, October 3, 1995, p. A10.
- Craig, Gordon A. *The Germans*. New York: Penguin Books USA, Inc., 1982.
- Darnton, Robert. *Berlin Journal: 1989-1990*. New York: W.W. Norton & Company, 1991.
- Dhanji, Farid, and Branko Milanovic. "Privatization in Eastern and Central Europe." *Policy, Research, and External Affairs Working Papers*. September 1991, Washington, DC: World Bank.
- Dodds, Paul, and Gerd Wachter. *Privatization Contracts with the Treuhandanstalt*. Cologne: Federal Office of Trade Information, 1993.
- Focus on... *The Treuhandanstalt*. New York: German Information Center, January 1995.
- Freyemark, Topsten. Personal Communication, August 30, 1995.
- Fuhrman, Peter. "The German Disease." *Forbes*, March 30, 1992, p. 42.
- "German Inflation Up." *New York Times*, January 14, 1994, p. D4.
- "German Privatization Plan." *New York Times*, July 11, 1994, p. D5.
- "Germany's Mezzogiorno." *The Economist*, May 21, 1994, pp. 10, 27-28.
- Glouchevitch, Philip. *Juggernaut*. New York: Simon & Schuster, 1992.
- Hall, John, and Udo Ludwig. "East Germany's Traditional Economy." *Challenge*, September-October 1994, pp. 26-32.
- "Hand of Kindness. Is Germany's Treuhandanstalt a Good Thing?" *The Economist*, March 21, 1992, p. 71.
- Haydon, Tome and Ivette Mendez. "Gone Private." *Star-Ledger*, July 8, 1995, p. 1.
- "Jobless East Germans." *New York Times*, February 6, 1992, p. D21.
- Kappler, Arno, and Adriane Grevel, eds. *Facts About Germany*. Frankfurt: Societats-Veriag, 1993.
- Kinzer, Stephen. "A Wall of Resentment Now Divides

Germany." *New York Times*, October 14, 1994, pp. A1, 14.

Kornai, Janos. "The Principles of Privatization in Eastern Europe." *The Economist*, Volume 140, No. 2, 1992, pp. 153-76.

Kurian, George Thomas. *Encyclopedia of the Second World*. New York: Facts on File, 1991, pp. 216-25.

Lieberman, Ira W. *Lehigh University Seminar on Liberalization, Integration, and Privatization: Latin America and Eastern Europe Compared*. Draft March 8, 1993.

Long, Robert Emmet, ed. *The Reference Shelf Volume 64, Number 1: The Reunification of Germany*. New York: The H. W. Wilson Company, 1992.

"Lufthansa to Sell Shares." *New York Times*, September 13, 1994, p. D 18.

Marshall, Matt. "International: Foggy Data Hint at German Slowdown; Indicators Lose Precision, But Problem Looks Real." *Wall Street Journal*, August 1, 1995, p. A10.

Marshall, Matt. "Jobless Growth Creates Divide in Germany; Firms Clash with Unions Over Work Force Cuts, Compensation Issues." *Wall Street Journal*, September 8, 1995, p. A5.

McAdams, A. James. *Germany Divided*. Princeton: Princeton University Press, 1993.

"More Germans Jobless." *New York Times*, November 5, 1992, p. D6.

Nash, Nathaniel C. "Goldman Wins Big Role in German Sale." *New York Times*, November 26, 1994, p. A39.

"No Escape." *The Economist*, May 21, 1994, pp. 5-8.

Penson, Stuart. "An Industrial Core in East Germany." *New Steel*, February 1995, p. 46.

Protzman, Ferdinand. "Germans Foresee a Sluggish Year." *New York Times*, January 30, 1992, p. D9.

Protzman, Ferdinand. "Germany's Take Up Approval of Pact on Economic Union." *New York Times*, May 14, 1990, p. A1.

Protzman, Ferdinand. "Privatization in the East Is Wearing the Germans." *New York Times*, August 12, 1994, p. D1.

Reier, Sharon. "Breaking with Big Brother." *Finance World*, March 5, 1991, pp. 46-47.

Shlaes, Amity. "Germany Buys Itself a Miracle." *Wall Street Journal*, July 6, 1995, p. A8.

Smirnoff, Steven R. "Privatization in Russia." *Business Forum*, Volume 19, Nos. 1 & 2, Winter/Spring 1994, pp. 36-37.

Treuhandanstalt: *Promoting the New Germany*. Bonn: Treuhandanstalt Abteilung Öffentlichkeitsarbeit (Publisher], c. 1991.

Treuhandanstalt: *The Chance of the 90's. Investing in Eastern Germany*. Treuhandanstalt publication, C. 1991.

Treuhandanstalt: *Working for Rapid Privatization, Resolute Restructuring, Careful Closure*. Bonn: Federal Ministry of Finance, October 1991.

Whitney, Craig R. "Germans Five Years Later: Bitter and Still Divided." *New York Times*, June 24, 1994, p. A3.

"Will Germany's Boom Turn to Bust?" *The Economist*,

November 23, 1991, p. 73.