In Mickiewicz, T (ed) Corporate Governance and Finance in Poland and Russia, Palgrave Macmillan, London and New York, pp. 91-118, Chapter 5

THE RISE AND FALL OF A CENTRAL EUROPEAN ENTERPRISE - THE CASE OF 'ELEKTRIM'[1]

Piotr Jaworski and Slavo Radosevic
School of Slavonic and East European Studies
University College London

Elektrim's final product is shares'
Elektrim ex-CFO Piotr Mroczkowski,
Global Finance, February 1997, p. 23

1. Introduction

During the period of command economy (i.e. before 1990), Elektrim operated as one of the largest Polish foreign trade organisations which, during the course of transition, became a conglomerate. Since the transition Elektrim S.A. has manufactured cables, power, provided telecom services, (mobile and fixed), and has been in process of divesting a host of unrelated businesses. In 2000 Elektrim was the biggest manufacturing private company in Poland in terms of market capitalisation and the second largest publicly traded company after TPSA (the national telecom company), with the maximum price of shares at the level of 72,90 PLN on March 20, 2000. Two years later, this former blue chip company struggled to survive with the share price reaching its minimum of 1,14 PLN on June 6, 2002. In 2005, its shares oscillated in the range of 4 to 7 PLN [inwestycje.elfin.pl and gielda.onet.pl].

[1] This chapter builds on our previous study on Elektrim (see Radosevic, 2001). However, this is not only its updating but what we consider a definite interpretation of Elektrim's evolution and outcomes in the light of its history of the last 15 years. See S. Radosevic, D.E. Yoruk and D. Dornisch, The Issues of Enterprise Growth in Transition and Post-transition Period: The Case of Polish 'Elektrim'. *Centre for the Study of Social and Economic Change in Europe Working Paper Series No. 1*, April available at: http://www.ssees.ac.uk/economic.htm

Elektrim's case has a wider relevance for understanding the growth and slowdown of enterprises in central and eastern Europe. It illustrates the changing pattern of growth of enterprises between the transition and post-transition periods. Elektrim had grown primarily through conglomeration in the early transition period. Subsequently, Elektrim has started to focus on a few core areas (telecommunications, cables, energy). The strategic shift to telecommunications has been based on partnerships with foreign firms. Analysing these strategies helps us to understand the key factors behind its troubles.

First, we provide a background for the analysis of Elektrim by pointing to factors that led to the transformation of the Polish ex–foreign trade organisations (FTOs) into conglomerates, of which Elektrim was a good example. Than we present the reasons for problems encountered by the firm after ten years of its operation in market environment and than summarise the current state of affairs. Next section highlights several analytical issues that are important for understanding the growth and decline of the Central and East European (CEE) enterprises in the light of Elektrim's case.

2. Transformation of FTOs into conglomerates

Elektrim is one of the seven Polish ex-foreign trade organisations (FTOs) that in the transition period transformed themselves into conglomerates. Out of more than 40 FTOs in 1989, around a dozen have managed to survive and grow in the market context including the 'big seven', which include Elektrim, along with Agros Holding, Animex, Mostostal Export, Universal, Rollimpex, and Stalexport. Although they are all conglomerates, they differ in the degree to which they are focused, with Mostostal Export and Universal being the least focused.

During the communist era, FTOs were the main intermediaries between foreign markets and domestic producers of export goods, the latter being basically reduced to production units. Moreover, they had a monopoly over any international transaction. For example, Elektrim was monopolist in selling electrical equipment and turnkey power systems produced by Polish enterprises. This led to an accumulation of expertise in foreign trade organisations and knowledge about foreign markets as well as about what domestic producers could deliver. Furthermore, the FTOs hired employees, who were relatively well prepared for operation in the free-market environment. Before 1990, the economic education was divided according to the division of socialist economy into five branches: internal trade, organisation of production, finance and statistics, theoretical economics and foreign trade. The latter prepared staff for the FTOs and the international market environment, while the other branches were bound only with internal economy, teaching mainly socialist economy and management. Moreover, only selected higher education institutions had foreign trade departments and the limits on number of students there were usually four times higher than at other, “centrally planned” departments. These factors made the graduates of foreign trade departments and subsequent employees of FTOs a kind of “socialist management elite”.

FTOs have also accumulated diverse engineering skills through participation in large turnkey projects in COMECON and Third World countries. With the dismantling of trade barriers in 1990 and the loss of monopoly positions in their respective branches, FTOs found themselves in an ambiguous situation. On the one hand, they lost their privileged status of indispensable intermediary, but on the other hand, they had accumulated experience in operating in foreign markets and had strong local knowledge of the value and competencies of domestic producers.

Three factors played an important role in the survival of FTOs as well as in their growth and transformation into conglomerates [*Wall Street Journal*, 1996]. First, when the Polish economy opened in the early 1990s they had accumulated foreign currency reserves - a huge advantage when compared to cash stripped domestic producers at that time. The value of these reserves was greatly increased through strong zloty depreciation. This enabled them to use accumulated foreign currency reserves to buy up many of the firms they represented, as well as to invest into banking.

Second, the seven largest Polish FTOs were floated on the Warsaw Stock Exchange, where the share prices were rising fast after floatation in 1993 and 1994. This enabled them to get additional cash and bring into their respective groups their traditional suppliers and other companies that were seriously undervalued. In 1995, their shares accounted for a third of the total value of the Polish stock market, excluding banks [*The Economist*, 1995].

Third, trading groups flourished thanks to large windfall profits either as a result of being reimbursed overpaid taxes from 1990 or from one-time asset sales.

These three factors explain why certain FTOs have managed to survive and then to grow, especially given ample opportunities to buy cheap assets via privatisation. To some extent, they also explain the strategy of transformation into conglomerations: financial resources together with managerial skills were something lacking in the other parts of the former centrally planned economy.

Furthermore, it seems that the nature of the business environment, in particular the market uncertainty in the early transition period and the undeveloped market infrastructure, was such that conglomeration was perceived as the optimum strategic option for both, the former FTO's as well as the acquired companies. This led companies to diversify in order to cope with the uncertainty of domestic markets. As Mr. Mroczkowski, ex-Chief Finance Officer of Elektrim put it 'diversification gave security' [*Wall Street Journal*, 1996]. In addition, the undeveloped financial system, scarce management skills and the generally undeveloped institutional systems of the market economy suggested conglomeration not only a viable but also a desirable strategic option. A business analyst, Martin Taylor, from Baring Asset Management, London, put it this way: 'Given the choice, I would always choose a pure producer …. But because of the inefficiencies of the Polish economy, there is a place for conglomerates now' [*Wall Street Journal*, 1996].

However, the internal advantages of conglomerates were not sufficient to sustain their growth. In "the post transition" period (second half on 1990s) the institutional factors that drove conglomeration in CEE earlier did not operate any more. The advantages of large business groups in terms of easier access to financial capital disappeared. Nor the advising their member firms with regard to exports or the creation of domestic brands did offer competitive advantage. Weak financial standing of former FTOs led to search for new investors, including foreign, which not always resulted in expected positive results.

In case of relative market insulation the operation as a big group was also easier from the political point of view. The sheer size of the groups enabled easier access to government through preferential status in receiving licences in areas like telecoms, or in the form of 'certification requirements'. In short, they had advantages in nurturing so called 'network capital'. But with the increased openness of the Polish economy and of the financial system as well as the marketing infrastructure development these advantages disappeared. Even as early as in 1995, some subsidiaries were able to raise capital just as easily as the Elektrim itself [*Economist*, 1995]. With the stabilisation of markets and departure form a period of market uncertainty, diversification of lines of businesses became a problem.

Elektrim's management was aware of all these processes and tried to focus on wide telecommunication industry. But the expertise of its management, which was an asset in conglomerate period, turned out not to be useful when the in-depth industry-specific expertise was needed. The so called generic managers, who were able to coordinate companies as different as food and heavy machinery producers, were not able to manage specific industry in deeper manner: general management capabilities turned to be insufficient for running successfully neither a highly diversified business nor a specialised entity in an open and competitive economy.

The strategy of co-operation with foreign investors together with focusing on ”new economy” business resulted in subsequent troubles for the company. Especially that after the bubble, there was a huge slump in share prices of the "digital" companies. This, together with economic slow-down of the Polish economy made the Elektrim almost bankrupt.

3. Elektrim: a history of growth

Elektrim was established in 1948 as a foreign trade organization. Like other FTOs, until 1989 it had a monopoly to trade internationally in its own range of products. The crucial decision for Elektrim after 1989 was to shift from being a trading organisation into becoming also a production company. This quick grasp of the need to migrate from trading to manufacturing was seen in retrospect as being very important for Elektrim to be 'a step ahead of rest of the game' [*Business Central Europe*, 1994]. As Elektrim's Chief Finance Officer, Piotr Mroczkowski, explains it 'To stay in business we had to stop being solely an agent. We had to go for vertical integration and get control of producing what we had been selling' [*Global Finance*, 1997]. Elektrim entered production mainly by taking over some 25 enterprises in the course of Poland's privatisation process for which it paid around $300m from a strong cash flow in the early 1990s, when assets were inexpensive. It made a profit by selling shares in companies it had bought cheaply from the state, an activity close to that of investment banking. CS First Boston estimates that Elektrim earned 19m zlotys ($8.37m), about a fifth of its pre-tax profit, from selling financial assets in 1994 [*Economist*, 1995]. Its assets even included yoghurt factories, milk plants, fruit drinks manufacture, pig farms and chicken feed processing [Dawson, 2000 January].

During this (second) period the main feature of Elektrim's growth was conglomeration. Elektrim bought many of the concerns it had been representing, including most of Poland's cable manufacturers, which have been growing due to the expanding domestic market and exports to Germany and elsewhere. At the end of 1993 Elektrim had a stake in 87 companies concentrated in five sectors. Its management wish was to expand. Acquisitions were seen as essential to build market power. As one of its chief executives, Mr Muszynski, explained: 'If you are late on the train the foreign capital will buy in'[*Wall Street Journal*, 1994] .

Despite the fact that Elektrim's acquisitions were haphazard they were largely in five main areas: power generation equipment, electrical machinery and apparatus, cables, lightning equipment and telecommunications. However, it also had assets in agriculture and food processing, in cement and construction and in seven different banks (1995). The underlying strategy behind the conglomeration in the 1990s was 'to use privatisation to integrate vertically' and to transform Elektrim into a 'vehicle for acquisitions of core business suppliers' (Piotr Mroczkowski, Elektrim's the then Chief Finance Officer) [*Wall Street Journal*, 1994]. The idea was that the Elektrim should operate as a restructuring agent or a 'network organiser' by pursuing a "hands on" approach to restructure newly acquired subsidiaries. In the mid-1990s the strategy was to model Elektrim on Japan's Mitsubishi and Sumitomo groups. Like them, Elektrim planned to spin off shares in subsidiaries to suppliers, creating a corporate network bound by commercial ties [*Economist*, 1994].

However, this strategy was not followed for long. Instead of building diversified business group, in 1999 the company entered a third stage, which can be described as consolidation, and focusing. According to Piotr Czarnowski of Elektrim, this shift was driven by a variety of factors among which the most important were: the lack of transparency of the conglomerate, inefficiencies in the allocation of capital among different businesses, lack of expertise in many newly acquired business segments, changes triggered by disclosure problems and by investors demanding streamlining and focusing. Its new Chief Executive Officer, Barbara Lundberg, reinforced the strategy cautiously initiated by former CEO Andrzej Skowroński of focusing on three core business: telecommunications, power generating equipment and cables, with strong expansion in telecommunications as a starting point. This included take-overs of local operators and acquisitions of shares in telecom companies.

One of the key components of this new strategy was to invest in mobile telecom. But the outcome turned out to be the main reason of dismissing Mr Skowroński. In 1996, Elektrim secretly agreed to sell a 6.5% stake in PTC (Era GSM) to Kulczyk Holding. The price Elektrim agreed was close to its nominal price and the latter was not made public until the sale was about to take place. This 6.5% was supposed to compensate Kulczyk, a Polish tycoon, for the role he played in talks with the company's other partners. Although not complaint with the rules concerning the stock exchange companies, this transaction and its secrecy was more a result of informal way of managing the company by Mr Skowroński than a deliberate attempt not to reveal information to the investors [Gadomski, 2002]. Furthermore, in 1996 investment in mobile telecommunication was a risky business: even American analytics did not foresee a market for this service, which resulted in relative late development of mobile technology in the US. The business plan for PTC assumed first profits to appear in five years. The situation was completely different at the time when the transaction with Mr Kulczyk was revealed in October 1998, when the shares were already valued at $165 million. Finally Kulczyk agreed to $25 million in compensation. The PTC case was the immediate reason to dismiss Mr Skowroński. On the demand of international fund managers the President and Deputy President of Elektrim were forced to resign.

The foreign investors appeared in Elektrim in May 1997, when the firm issued convertible bonds worth 550 million PLN sold by the Merrill Lynch on international markets. As we have acknowledged earlier this coincided with the growth of Polish economy and resulting optimism of the international investors. The foreign investors aimed at close control of firms in which they invested: managers who were too independent and “spoke different business language” had to be dismissed and new “MBA language speaking” had to be hired. Moreover, after Russian crises, investors were afraid of loosing money, also in the other emerging markets. The fate of Elektrim CEO was similar to the fate of other FTO’s CEOs:

- in June 1998 CEO of Impexmetal Mr Edward Wojtulewicz (57 years old) was dismissed by main shareholders, Japanese investment bank Nomura and American investement fund Templeton, who replaced him with Nomura’s employee Jacek D. Krawiec.
- in October 1998 Kredyt Bank PBI dismissed Witold Pereta (63 Years old), CEO of Animex and replaced him with Jerzy Milewski
- In October 1998 Kredyt Bank together with Templeton dismissed Grzegorz Tuderek (60 years old) and replaced him with Marek Michałowski [Grzeszak 1999].

All four CEOs except Skowroński, who was 52, were in their late fifties or early sixties, working for many years for their FTO’s. Furthermore, they restructured their firms in the early years of transformation and brought them to the Warsaw Stock Exchange. And finally all of them were dismissed at the same time, on the initiative of foreign investors.

The dismissal of Mr Skowroński paved the way for the entry of the new CEO, Mrs. Lundberg. New CEO was trusted by the international investors and her moves were seen as an example of a new kind of managerial practices in the Polish economy. The extent of changes was described by Mrs. Lundberg’s advisor Piotr Czarnowski who stated: "This is a completely different organisation. There is no other Polish company that has transformed itself in an eight to ten-month time-frame and invested $1.7bn in one year alone." [*Business Central Europe*, 2000]. Speaking the same language as the foreign investors, and being educated in Western-style generic management institutions, Mrs Lundberg seemed to be the best suited person to focus the activity of the firm.

Barbara Lundberg became new CEO in February 1999, two months after Andrzej Skowroński resigned. She speeded up consolidation by selling-off 70 of its non-core subsidiaries out of total 100, only in 1999. In accordance with its new focusing strategy, Elektrim was selling-off assets that did not fit its new focus on the telecoms, energy or cable sectors. It concluded a deal to sell 80 such subsidiaries. In June 1999, jointly with Clifton Consulting, Elektrim set up Warsaw Equity Holdings, a holding company in which it has a 15% share, the remainder falling to Clifton Consulting, which was entitled to 20% of the proceeds from the sale of any assets [Dawson, 2000 January]. Elektrim obtained $62.7m from the transaction and was reduced to 28 firms following the deal. [Polish Press Agency, 1999]. Subsequently Elektrim sold 15% of shares in Warsaw Equity Holding.

Elektrim’s share ownership of Chemia Polska was reduced to 21.16% of the total votes (Feb 1998). In 1997 the Dutch group, Campina Melkunie, acquired Elektrim Food, a specialist in yoghurt and dairy dessert production, for an undisclosed sum. In its heyday Elektrim had an 8% of share of the Polish dairy market, but its companies in this sector were in the red, running at around only half of actual capacity. Interlektra of Luxembourg bought 3 of Elektrim’s motor producing subsidiaries for PLN 58m ($14.19m). The Luxembourgians were paying PLN 43m ($10.52m) for 99.94% of the motor producer Celma, another PLN 9m ($2.2mn) for 67.398% of a similar firm, Besel, and a further PLN 6m ($ 1.47m) for 100% of the shares of Elektrim Motor (Jan 2000). The acquisition of Celma was contingent on Celma's purchase from Elektrim of the holding's 69% stake in Indukta, another electric machinery factory. [Prawo i Gospodarka, 2000].

Parallel to selling the unrelated businesses, Mrs. Lundberg initiated a huge process of investment in telecommunication industry. In first three months of her reign Elektrim invested more than $1.1 billion and increased its debt by several billion dollars [Gadomski, 2002].

The two year period of 1999-2000 seemed to be the most successful in the company history. Elektrim aimed to become a telecommunication group, a competitor to TP SA, the national telecom company, and an operator delivering a full range of telecommunication services. It also intended to continue its operation related to the production of complete energy objects and their refurbishment. The plans were to raise the effectiveness of cable companies by a way of further restructuring but 'without too much investment' [Elektrim, 2000]. By 2000 Elektrim's assets became concentrated in telecoms, energy and cables with only 3.7% of assets in other businesses (table 2).

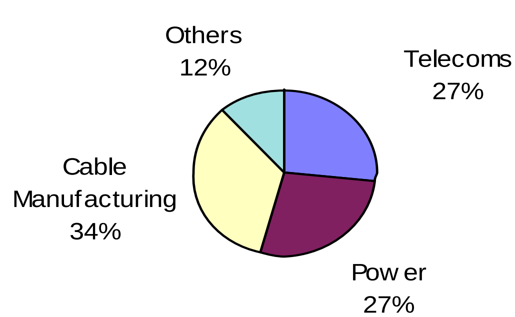
Table 2: Elektrim's assets in 2000

Busines	**Electrim's stake in it**	**Value of stake (Zl m)**
Elektrim (holding company)		420
	Telecoms	
Elektrim Telekomunikacja	51%	4,805
Fixed line telephony	87%	1,340
	Power	
PAK (electricity generation)	38.5%	935
Elektrim Megadex	97.3%	67
Rafako	49.9%	52
Mostostal Warsawa	28.4%	36
Energomontaz Polnoc	37%	31
	Cable	
Elektrim Kable	70.5%	788
Others		325
Total		8,798
Total parent debt	2,892	

Source: Radosevic et al (2001) based on Erste Bank, Central European, July/August 2000, p. 26

In terms of sales, three major segments had similar shares with other business amounting to 12% (Figure 1, below).

Figure 1: Consolidated Net Sales Revenues by Business Segments



Source: ET Annual Report , 2000

Source: Radosevic et al (2001) based on ET Annual Report, 2000

The growth of Elektrim has been accompanied by strong growth in its market capitalization. Elektrim was the first company listed on Warsaw Stock Exchange in 1992, with a share price of 0.35 Polish zloty. In 1996, it was valued at around $620m [Times, 1996]. By January 1997 the share price had risen to 31 Zloty, bringing Elektrim's market capitalisation to $700m, and making it the largest non-bank market-capital stock on the Warsaw exchange. In 1999, its market value rose to $912.81 million. The highest market value, amounted to $1,5 billion in March 2000. At that time, its shareholders were mainly institutional investors (85%). (See Table 3).

Table 3: Elektrim's largest investors in 1999

Institution	**Country**	**$m value held**	**% of Equity**
Bank Austria	Austria	79	6.1
Capital International	USA	67	6.9
Emerging markets Growth Fund	Malayasia	66	6.8
Merrill Lynch Mercury Asset Mgmt	United Kingdom	49	5.1
Schroder Investment Mgm (Hong Kong)	China	48	4.9
Barring Asset Management	United Kingdom	35	3.6
Fleming Investment Management	United Kingdom	31	3.2
Schroder Investment Management	United Kingdom	27	2.8
Capital Research & Management	USA	26	2.7
Dresdner Bank Investment Management	Germany	21	2.1
Other large investors		111	12.3

Source: Radosevic et al (2001) based on Carson Group, Central Euroepan, July/August 2000, p. 25.

On the asset side, the structure is presented in Table 4. In 2000 it had five major groups of subsidiaries: telecommunications, power, cable manufacturing, internet and others.

Table 4: Elektrim SA major subsidaries

Telecommunications
ET Telekomunikcja Sp.
(51%, Vivendi 49%)
- Bresnan International Partners (Poland) L.P. (100% ET)
- Polska Telefonia Cyfrowa Sp zoo
Era GSM (51% ET)
RST El-Net SA (92%)
Polish Phonesat Sp (93.39%)
Telefonia Regionalna Sp (99.39%)
Elektrim Tv-Tel Sp (100%)

Internet
VPN - Service Sp (former NASK Service Sp) (85%)
Inter Net Polska Sp (85%)
CT Creative Team Sp (60%)
Easy Net SA (50%)
AGS New Media Sp (505)

Cable Manufacturing
Elektrim - Kable SA (70.49%)

ELEKTRIM SA

Power
Elektrim - Megadex SA (98.41%)
Rafako SA (49.9%)
ZE PAK SA (38.46%)
Elektrim - Volt SA (100%)
Gielda Energii SA (10%)

Others
Warsaw Equity Holding Sp
Mostostal Warszawa SA
Makler Market Sp
Enelka Ltd
Trasza Swietokyzyska Sp

Source: Elektrim Annual Report, 2000

Notes: Elektrim shares in brackets unless stated otherwise; ET = Elektrim Telekomunikacja.
Source: Radosevic et al (2001)

4. The Anatomy of failure

However, these were last minutes of the glory. In less than two years from the peak market value, on September 19, 2002 the Economist wrote:

…privatised Elektrim was the brightest star in the Polish firmament, cherished by patriots who hoped it would be their national champion. In the past week, due in part to the unforeseen consequences of nationalistic "Poland first" policies, the telecoms and power conglomerate filed for bankruptcy and fired its management for the umpteenth time. [Economist 2002].

These words were written just after the market value of Elektrim plunged to $23.815 million (March 2002). In December previous year the company had defaulted on convertible bonds of 440 million Euro. Preliminary accepted restructuring agreement was cancelled which led to bankruptcy filling in September 2002. The troubles were an unintentional result of the policy of Ms Lundberg, at that time already no longer a CEO. She was dismissed on May 15, 2001. The strategy of stepping into the internet sector failed. The "new technology sector" boom disappeared leaving Elektrim with internet firms, which in majority went bankrupt, being bought earlier by Elektrim for a high price [Elektrim internet site]. Also telecommunication activities did not turn out to be successful. Some of the deals were cancelled as part of restructuring attempt, but the firm had to pay huge compensations. In general, the assets bought turned out to be overpaid. For example Brensan International Partners controlling Cable TV operator Aster City was bought for $325 million when Zygmunt Solorz, owner of the first private Polish TV operator "Polsat" wanted to pay only $170 millions. These moves increased the liabilities of the Elektrim to almost 6.2 billion PLN in one year [Gadomski, 2002].

This was not the only risky game that Eletrim played under the management of Ms Lundberg. The highly indebted company, which recorded a loss since 1998, played hazardous corporate game with two international players: German Deutsche Telekom (DT) and French Vivendi. Before 1999 DT was seen as the strategic investor in the Elektrim. The pearl in the crown of Elektrims assets, Polska Telefonia Cyfrowa (PTC), Poland's top mobile company, was owned jointly by DT and Elektrim, the latter owning 51% stake. The Germans, blocked by Polish telecommunications law from owning a majority stake, were in the process of increasing their share of the PTC to 45%. They pushed for control of Elektrim's telecoms subsidiary once the law changed. Elektrim resisted and the negotiations fell through[2].

But in December 1999 the company chose new strategic partner – Vivendi, which was to invest in Elektrim Telekomunikacja $1.2 billion dollars and receive 49% of shares. Vivendi (renamed Societe Generals des Eaux, a French company and the world's largest water company) employed 193,000 people, with assets of $43.1bn and revenues of

[2] In Feb 1999, Elektrim disclosed that it had signed a preliminary agreement with DT in October 1998 whereby DT would acquire a 26% stake in El-Net. On May 19, 1999 Elektrim announced it had broken off talks with DT about the potential purchase by the Germans.

$28.6bn at that time [UNCTAD, 1999]. In the previous 20 years Vivendi diversified into telecommunications, media and several other activities. Its activities include water distribution (Cie Generale des Eaux), thermal energy supply (Blanzy Ouest), building and heavy public construction projects (SGE), waste management (CGEA Onyx), transport (CGEA Transport), electrical energy services (Cie Generale de Travaux et d'Installations Electriques), real estate (Compagnie Generale d'Immobilier et de Services), telecommunications (Cegetel) and publishing and multimedia (HAVAS) activities. Vivendi was a major shareholder in Cegetel, the number two telecom company in France, second behind the incumbent France Telecom, offering fixed and mobile telephony, as well as internet access. Vivendi streamlined its organisation during 1997, disposing of 334 companies in the health, cable television, laundry, restaurant and car parking sectors. The group consisted of 3371 companies in December 1998, of which 1394 were located abroad.

However, Deutsche Telekom claimed the right to 3% of the 15.8% PTC shares purchased by Elektrim in August 1999 from minority shareholders. Also, it claimed it had right of first refusal on some of the shares. It blocked the transfer of Elektrim’s stake in PTC to its subsidiary and took the case to court. Elektrim maintained that DT's refusal to agree to the transfer of shares was a violation of the Shareholders Agreement and was damaging to Elektrim as it blocked the restructuring of Elektrim’s telecom sector development with Vivendi's support. Elektrim offered a defence to the State Telecom and Postal Inspectors PITIP as to its transfer of shares to PTC, which was challenged in court in August 1999 by DT. Elektrim also announced that it intended to submit a motion against the German firm for irregularities over PTC.

As a result, DT stopped the Vivendi investment, blocked debt financing and threatened to force Elektrim into default on its massive short-term debt payments [Europe, 2000]. For a time, it looked as if the Germans would take over. In order to secure the deal Elektrim had to sell a larger stake. Fortunately for Elektrim, Vivendi stepped in by investing $1.2bn, including $250m in cash, to clean up Elektrim’s balance sheet. In exchange, the French got a 49% stake in Elektrim Telekomunikacja and, indirectly, ownership of 25% of PTC.

In the meantime, DT failed initially to prove legal credibility to its claims to pre-emptive rights to PTC shares. A Warsaw court dismissed the claim by DT, which argued that, as a shareholder in PTC, it had first refusal right on any shares that existing partners wanted to sell. DT claimed that it had the right to buy any shares on offer up to a ceiling, which would have maintained the existing proportions between the remaining shareholders. Elektrim stated in court that DT did not have the necessary approvals to make purchase of the additional shares. In response DT submitted a motion to the Court of Arbitration in Vienna. Elektrim has since agreed to abide by the Viennese court's decision. The arbitration was part-financed by Vivendi. At stake was Elektrim key asset: PTC shares constituted as much as 85% of the parent company's valuation [Business Central Europe, 2000].

Subsequently, Vivendi tried to gain control over PTC: by transferring its shares from Elektrim to its subsidiary Elektrim Telekomunikacja (ET) in December 1999[3] together with increasing of the share capital of the latter by almost PLN 9 bln ($2.25bn) to PLN 10 bln ($2.5bn) [FT.com, 1999, June 10] and taking over 49% stake in the ET. At the same time Vivendi converted its earlier loan of the amount of $615m into an equity stake in the ET. This gave Vivendi control over PTC by holding a 50% of stake[4] [*Polish News Bulletin*, 1999]. Vivendi guaranteed to increase its investment to over $1.2bn, which constituted an initial immediate payment of $150m and a second payment of the of $100m.

However, the battle for control over PTC was far from over. DT has increased its 22.5% stake in PTC to 45% by acquiring MediOne International, a subsidiary of the US Media One Group [Dawson, 2000 January]. DT paid between $1bn and $1.2bn for the stake in PTC. In 1999 DT controlled 45% of PTC, fighting via the courts for another 3% against Elektrim [FT.com, 1999][5.]

In December 2001 Elektrim made another U-turn, returning to partnership with the DT and signed a letter of intent to sell 51% (and thus strategic and operational

[3] 47.99% of shares of PTC were transferred.
[4] As part of this deal, the Elektrim has sold Vivendi 50% in a Carcom Warsaw SA that holds 1.9% of the PTC. After the capital raising operations and sale of Carcom shares in Elektrim, Elektrim and Vivendi hold 50% each of the nominal capital and voting rights at Carcoms shareholders meeting.
[5] DT is also present in the two Hungarian mobile phone operators Wester Radiotelefon and Westel 900, which at 58% has the largest market share in Hungary.

control) of its fixed-line and data transmission companies to Deutsche Telekom for $180 million.[6] As a result Vivendi claimed in its case against Elektrim in the London Court of International Arbitration that relations/negotiations with Elektrim have reached an deadlock and in accordance made a set of far-reaching demands concerning Elektrim's telecommunications operations, including (1) that Elektrim transfers its shares in VPN Service and Inter-Net Polska to the Elektrim Telekomunikacja joint venture company, (2) that Elektrim discontinue negotiations or any contracting with Deutsche Telekom concerning fixed telephony, (3) that Vivendi is enabled to sell its shares in Elektrim Telekomunikacja to Elektrim for a market price *(Rzeczpospolita 2001).*[7] [8] The collapse of the partnership between Elektrim and Vivendi was made public in February 2001. Vivendi (1) brought suit in an international arbitrage court in London against Elektrim for breach of the investment agreement from December 1999 and (2) asked a Polish regional court to prevent sale of Elektrim's assets, where the latter would prevent Vivendi from "undertaking its rights as a majority shareholder" in the joint telecoms holding (Reuters 2001).

Elektrim publicly denied the validity of Vivendi's claims, asserting that Vivendi never availed the procedure for resolving a conflict/impasse between the sides, which would involve consultations between the Directors General of the two companies. Moreover, it claimed that (1) Elektrim was not obligated to conduct its Internet operations under the Elektrim Telekomunikacja umbrella; (2) that Vivendi conducted "in bad faith lengthy negotiations concerning the acquisition of a stake in Elektrim S.A.'s fixed-line businesses for more than 12 months although it was obliged to present a serious proposal in this respect on or before February 14, 2000"[9]; (3) that it would be in

[6] These companies are RST El-Net SA, Telefonia Regionalna Ltd., Elektrim Tv-Tel Ltd, Internet Polska Ltd., VPN Service Ltd and Polish Phonesat Ltd.

[7] As defined in the Investment Contract, this would involve each partner selecting an investment bank who would undertake a valuation of the shares involved, which would then be the purchase price for Elektrim.

[8] Vivendi's appeal in the Polish regional court was made primarily to keep Elektrim from taking any actions on the sale of shares to Deutsche Telekom before the process in the London Court could be completed. The Polish court has denied Vivendi's appeal.

[9] Moreover, Elektrim has gone further and claimed the following with regard to the fixed telephony operations: "Vivendi has recently attempted in unauthorized fashion to block the important cooperation agreements between Aster City Cable and El-Net, which constitutes an unjustified attempt at limiting the ability of Elektrim to conduct business in the area of fixed telephony. The Investment Agreement clearly foresees the possibility of cooperation and market-based contracting between companies from the Elektrim Telekomunikacja group and with other companies affiliated with Elektrim, including Aster City and El-

the interest of the involved sides to attempt to resolve the impasse using the provisions in the Investment Agreement before initiating the share-sellback process [Elektrim 2001].

This corporate game was played in the period when the Polish economy slowed down, which was a disadvantage for Elektrim, which was a far more capital constrained than its foreign partners. After 7% growth, the time of near stagnation came at the beginning of the new millennium. This adversely affected the construction sector, on which the firm was relying and was accompanied by the mentioned earlier crash of the "new economy" internet market. The strategy of high debt financing together with the involvement in legal dispute with stronger international partners was very risky in the times of economic prosperity but turned to be disastrous under economic slowdown. The mixture of negative net profit of -1.2 billion PLN with assets of almost 15 billion PLN and almost 11 billion PLN of liabilities for 2000 (Table 5) under slowing down economy had to result in big financial troubles. In *The Economist* words:
"By the time it came to its senses and realised that it had to relinquish majority control of PTC in order to stay afloat, the telecoms boom had turned to bust, while its two jilted partners, Vivendi and Deutsche Telekom, had their own problems to attend to." [Economist 2002].

The financial situation of Elektrim was negatively affected by the move of Ms Lundberg which was made in June 1999, when Elektrim sold convertible bonds worth 430 million Euro. Under actual share price of 40 PLN the option price was 64 PLN. The move was presented as a way of financial restructuring hoping that the bonds would be converted into shares. Unfortunately, after the end of the "telecommunications boom" the prices of Elektrim shares were much lower and these bonds were claimed at end of 2001, what became a direct reason for the bankruptcy claim.

5. The Rescue

Net" (Elektrim press release, "Stanowisko Elektrima SA w sprawie Umowy Inwestycyjnej z Vivendi," 2/25/01).

2002 was very a very difficult year for the firm: Elektrim almost bankrupted and changed CEO several times. Mr Waldemar Siwak nominated in May 2001 as the successor of Ms Lundberg was replaced by Mr Dariusz Krawiec in February 2002. In April Mr Maciej Radziwiłł became new CEO only to be replaced in September by Mr Wojciech Janczyk. The latter was finally replaced in May 2003 by Mr Piotr Nurowski, who has occupied this post until the time of writing this chapter.

In order to rescue the firm, Elektrim Kable, Port Praski and some smaller entities were sold for 100 million PLN. These money together with 491 million Euro paid by the Vivendi for the equity in Elektrim Telekomunikacja were used for repaying majority of the creditors but not the owners of the convertible bonds. The latter claimed their money back in December 2000 and were offered repayment of only 60% [Gadomski, 2002]. The offer was refused and subsequent claim for bankruptcy was filled in January 2001. However, in October 2002, Elektrim reached the restructuring agreement worth $503million providing for exchange defaulted bonds for new bonds maturing at the end of 2005 and repayment of $54.2 million by June 2003 [Business Eastern Europe, 2002].

Table 5. Elektrim's annual reports 2000-2005 (current PLN)

Annual Report	**2000**	**2001**	**2002**	**2003**	**2004**	**2005***
Net Earnings:	5,565,319	3,625,985	2,487,411	2,243,439	1,921,797	406,148
Operational Profit:	-278,665	-481,685	-160,897	-14,119	19,085	100,128
Gross Profit:	-1,201,722	-538,014	-616,482	-439,552	790,610	1,637
Net Profit:	-1,078,041	-462,547	-699,437	-344,139	816,598	-9,592
Net flows:	-567,827	624,946	-432,549	80,929	-107,952	-47,769
- operational activity:	432,587	781,046	-127,309	-89,656	-113,194	24,478
- investment activity:	-17,780	717,984	-122,133	-83,730	5,191	-22,236
- financial activity:	-982,634	-874,084	-183,107	254,315	51	-50,011
Assets:	14,910,962	7,574,164	6,325,481	6,062,422	5,771,268	5,655,216
Liabilities and reserves:	10,677,420	5,587,904	5,323,239	5,392,491	4,255,980	4,235,559
Long term liabilities:	5,759,136	231,024	1,998,776	2,538,454	464,635	832,368
Short term liabilities:	3,383,133	3,380,896	1,527,686	1,435,048	3,078,199	3,403,191
Own Capital:	1,050,461	639,267	-73,643	-426,399	453,759	1,419,657
Share capital:	83,770	83,770	83,770	83,770	83,770	83,770
Number of shares:	83,770	83,770	83,770	83,770	83,770	83,770
Book value per share:	12.54	7.63	-0.88	-5.09	5.42	16.95
Earning per share:	**-12.87**	**-5.52**	**-8.35**	**-4.11**	**9.75**	**-0.12**

*First quarter
Source: gielda.onet.pl

Between 2000 and 2001 the assets of the Elektrim were halved from almost 15 billion PLN to 7.5 billion PLN. This was accompanied also by the halving of the liabilities from almost 11 billion PLN to little more than 5.5 billion (Table 5). This trend continued after 2001 at a slower pace and finally it resulted in focusing only on two sectors in 2005: mobile telecommunications and power (see Table 7.) Due to huge asset sell-out (Table 6) combined with the bankruptcies of the internet companies, the structure of the company became much simpler. Paradoxically, because of the troubles, the company focused mainly on its initial area of expertise: power. The Elektrim was rescued but at cost of a considerable downsizing.

Table 6. Major Elektrim disinvestments 2002-2004

Date	Seller	Company sold	Buyer	Value
19.02.2002	Elektrim S.A.	Elektrim Kable S.A.		$110 mln
25.12.2002	Elektrim Telekomunikacja	Aster Polska Warszawskie Sieci Kablowe RTK Autocom Autorom ZTP S.A.	Consortium of Hicks Muse Tate & Furst, Emerging Markets Partnership and Argus Capital Partners	110 mln EUR
27.02.2003	Elektrim Telekomunikacja	Telefonia Polska Zachód Elektrim TV-Tel	EVL Poland	73mln. PLN
30.06.2003	Elektrim Telekomunikacja	EL-Net El	BRE Bank	
28.01.2004	Elektrim S.A.	Mostostal Warszawa SA		
15.07.2004	Elektrim S.A.	DM Penetrator	DM Penetrator S.A., In the name of third parties	65.600 shares for 1,52 PLN each

Source: Elektrim's announcements at gielda.onet.pl.

The ownership situation of the "pearl in the crown", PTC, was also not simple. Its ownership structure was not stable. According to the Economist Intelligence Unit (2005):

Elektrim is seeking to dispose of its share in mobile operator PTC. However, Elektrim's PTC shareholding is held jointly with Vivendi (France), and the two firms have so far not been able to agree mutually acceptable terms with Deutsche Telekom, which currently holds the other 49% of PTC. PTC itself is eastern Europe's largest mobile operator; it had about 7.5m customers in mid-2004, and generated net profits of PLN347m in the first half of 2004.

In 2003 the German Telecom offered 1.1bn Euro for ET's stake in PTC, but the deal fell through when Vivendi and Elektrim could not agree on how to divide the cash (Business Eastern Europe, Aug 23rd 2004). In December 2004, Arbitration Court in Vienna decided that 48% of PTC did not belong to the Elektrim Telekomunikacja but to the Elektrim itself. This was subsequently approved by Polish court in February 2005 and as a result, Elektrim itself became 51% owner of the PTC. This made Vivendi to claim 2.2 billion Euro from DT in Paris Commercial Court in May as a compensation for earlier investment in the Elektrim Telekomunikacja. In addition, Vivendi asked for the shares of PAK owned by Elektrim Telekomunikacja, as the compensation in the legal procedure in

July 2005, but they were transferred to Inwestycje Polskie and moved out of Elektrim control. Furthermore, at the end of June 2005, Elektrim called DT to sell 45% of PTC as a fulfilment of earlier agreement, but on the other hand in July 2005, Elektrim was banned from selling its 48% stake by a Warsaw court.

The PAK (power generation) was another major project. In the beginning of 2005, Elektrim possessed almost 42% in the venture while the Polish State Treasury has 50%. In the privatisation agreement Elektrim was required to build new electric block Pątnów II.. Up till now Eletrim invested in PAK 210 million Euro but there were problems with securing finance of 350 million Euro for completion of the project, for which Elektrim was blamed and the State Treasury asked the arbitration court to cancel the privatisation agreement in March 2003. Finally, one month later, the amicable settlement was reached and the construction was restarted. The finance was provided by the consortium consisted of Canadian banks and EBRD (227 million euro to be paid back in 15 years), National Environmental Fund (226 million PLN, which is 50 million euro) and one of Polsat Group Company (90 million euro), which contribution was treated as own resources of Elektrim. The project should be completed in 2007. However, on June 16, 2005 Elektrim transferred majority of its shares to Embud, its daughter company as a compensation for the credit provided to PAK by the Embud two years earlier. Than, on August 2, the Embud shares were transferred to Inwestycje Polskie (IP) controlled by Mr Solorz, at present, major shareholder of Elektrim. Therefore, by late 2005, IP effectively owned 40% of PAK through Embud and Elektrim lost its control over the venture.

Table 7. Elektrim's structure in the middle of 2005

Elektrim SA

Power

100%

Elektrim Volt

exports and imports high and low voltage equipment, transformer stations, transmission lines, electric energy, lightning equipment and other goods. In 2000 Elektrim-Volt concluded first contracts for delivery of energy in Poland worth 180 million PLN. Than in 2001 and 2002 for almost 900 million PLN and 1,3 billion PLN reaching more than 10% of Polish energy delivery market.

49,9%

Rafako

one of the major Polish designer, constructor and maintenance provider of power equipment. Its main clients are Polish and foreign power plants constructors. The firm mainly delivers steam boilers (35%), spare parts to them and to other power equipment (30%) and air filters (30%). [gielda.onet.pl].

98,7%

Elektrim Megadex

Megadex is involved in the construction projects in the energy and environment, feasibility studies of investments, design of objects, developer services, organisation of tenders, arrangement of financial structures and individual delivery of plant and installation works, as well as complete turnkey delivery of energy and ecology objects [Elektrim, 2000 #7].

10%

Giełda Energii SA (Energy Exchange)

The firm emerged as a result of the liberalisation of the Polish electricity market in 1999 It was established in November 1999 by the winning consortium led by Elektrim. and the power exchange coordinates transactions in physical delivery and settlements from 30 June 2000. The main shareholder is the Treasury, owning almost 23.5% of equity. The consortium consists of another 18 partners, which the main is Elektrim.

Going out of and into Elektrim Telekomunikacja

48%

Era GSM

One of the three Polish digital mobile telephony network. At the end of 2004 the firm had over 8.6 million clients, which consisted almost 40% of the market and was about 7 p.p. ahead of the two other competitors: Polkomtel (Plus) and Centertel (Idea). In 1996, Elektrim, as the leading shareholder in a consortium which included Deutsche Telekom (DT), when it won the right to operate one of two new mobile telephone licences in Poland [Dawson, 2000 January #28].
The shareholders: Elektrim S.A. – 48.0%, T-Mobile Deutschland GmbH – 22.5%, MediaOne International B.V. – 22.5%, Polpager Sp. z o. o. – 4.0%, CARCOM Warszawa Sp. z o.o. – 1.9% and Elektrim Autoinvest S.A. – 1.1%.

Transferred out of Elektrim to IP

38,5%

PAK

In March 1999 consortium consisting of three Elektrim-controlled construction companies (Megadex, Mostostal Warsaw and Energomontaz Polnoc) bought a 20% stake for $87.9m in the lignite fired 2700MW power generating company Patnow Adamow Konin (PAK). The consortium raised PAK's equity by $100m increasing its stake to 38.46%[1]. The take-over was part of a bid by a consortium, which included also the US CalEnergy. The investor pledged to maintain the present employment level for the time of reconstruction and modernisation of the firm. PAK provides 11% of Poland's electricity and is the second largest Polish power generating company. In 1997, PAK's sales reached $320m and after tax profits of $9m. Over 10 years (1999-2008), the consortium is expected to invest $1bn in the reconstruction and modernisation of PAK's old power blocks and in reducing environmental pollution.

The problems of PAK had a chain effect on another Elektrim's company: Megadex. Troubles started with the problems in Pątnów II construction. The firm was a main executor of the project. Because of the payment problems, the company accumulated debt of 53 million PLN, almost two times of the capital of the firm, owned to the Treasury only and did not pay several other building constructors. In February 2002 Treasury preliminary won in the court the battle for 53 million PLN mentioned, but the company appealed. On the other hand the agreement to continue the construction of Pątnów II excluded the Megadex from the game, hiring Canadian SNC Lavalin as a main executor. The future of Megadex does not look promising as of 2005.

There was also consolidation on the investors side. From 10 main players in 1999, through 7 in 2003, Elektrim ended up with only 4, with one strategic investor PAI Media (controlled by Mr Solarz) owning little more than a third (see table 8.).

Table 8. Main investors in 2003 and 2005 (% of equity).

Investor	**March 2003**	**July 2005**
PAI Media SA (Former Polsat Media SA)	9,55%	34.83 %
Vivendi Universal SA	10,04%	15.04 %
TCF Sp. z o.o.	8,08%	8.08 %
Schroder Investment Management Ltd.	4,43 %	4.43 %
Merrill Lynch & Co. Inc	4,16 %	-
BRE Bank SA	20,31 %	-
Zbigniew Jakubas, Multico and Multico - Press	7,61 %	-
Others	35,64%	37.62 %

Source: gielda.onet.pl

Polsat Media started to increase the equity holdings in Elektrim in February 2003. First it bought 9,55% (from Mr Jakubas), than more in August and November same year and then in June 2004 (respectively additional 9.81%, 5.5 %, 3.05% and 5.73%), becoming the main investor in the Elektrim.

6. Analytical issues

Elektrim belongs to a group of large domestically controlled CEE enterprises that operated in the socialist period and which have managed to survive in the free market era. Elektrim, foreign trade organisation during the socialist period, tried to expand in the transition period and failed. We should ask why this blue chip became almost bankrupt and whether this was fate was unavoidable.

Here we highlight analytical issues that link Elektrim's case to the broader literature on corporate and industrial change, related to the CEE region in particular. We want to raise several analytically and theoretically relevant questions which are based on the case study of Elektrim.

6.1 The management

Elektrim entered the new era after transformation of 1989 relatively well equipped with the managerial skills. Of course these were not managerial skills earned in the free-market environment but on the other hand, its staff was trained at the foreign trade faculties of Polish economic schools and earned some experience in the practical foreign trade operations (see Section 2 above). The president Andrzej Skowroński, who led the firm in the times of change, earned very good experience in the East (two years in Moscow office) as well as trading with the West. In Elektrim since the 1978, he also knew the company very well. His education was formally concluded with his PhD in International Economic Relations.

Table 9. Elektrim's CEO 1987-2005

President	Period	Age*	Education	Experience
Andrzej Skowroński	1987 - Dec 1998	40	MSc Szczecin Technical University PhD in International Economic Relations	Until 1978 academic career From 1978 in Elektrim including 2 years in a representative Office in Moscow (1985-87)
Barbara Lundberg	Feb 1999 – May 2001	46	Wharton School, Pennsylvania University Jackson College, Tufts University.	1977–83 Exxon Enterprises than McGraw-Hill. 1983–86 Alan Patricof Associates, Inc., 1986-90 Kidder Peabody Co., Inc. 1990 Polish-American Enterprise Fund Second half of '90: Enterprise Investors
Waldemar Siwak	May 2001 – Feb 2002	31	MA in Banking and Finance Warsaw School of Economics	1991-1996 dealer in Polish Financial Institutions 1996-2000 International Financial Institutions in London: Carnegie Emerging Markets, Peregrine Securities and ABN AMRO Equities (UK) Ltd Since 2000 ABN AMRO Securities (Polska) S.A
Dariusz Jacek Krawiec	Feb 2002 – Apr 2002	35	MA in Economics and Organisation of Foreign Trade Poznan Economics University (1992)	Before 1997 dealer in Bank Pekao SA and than consultant at Ernst & Young and Price Waterhouse 1997 - 1998 Nomura International plc London 1998 - 2002 CEO Impexmetal
Maciej Radziwiłł	Apr 2002 – Sep 2002	41	MA in Sociology MA in Marketing and Management Warsaw University MBA Illinois University at University of Warsaw	1987-1990 assistant professor in Institute of Sociology of Warsaw University 1990-1991 International Privatisation and Financial Markets Development Fund 1991-1993 NBS Bewe Rogerson. 1993-1994 Creditanstalt Securities SA 1994-1995 Credit Suisse First Boston (Polska) Sp. z o.o 1995 -1998 Union Bank of Switzerland. 1998 - 2002 CEO Cresco Finacial Advisors Sp. z o.o.
Wojciech Janczyk	Sep 2002 – May 2003	38	MsC King's College MBA Imperial College	1985-1987 L.E.K. Partnership, 1987-1989 OC&C Ltd 1989 1991 director of Corporate Finance Department in Swiss Bank Corporation London 1991- I 2001 BMF SA I 2001- VIII 2002 Vice Minister of Infrastructure
Piotr Nurowski	May 2003 up till time of writing	57	LLB Warsaw University	1973-1980 President of Polish Association of Light Athletics 1981- 1991 Ministry of Foreign Affairs 1981-1984 – first secretary of Embassy in Moscow 1984-1986 Department of Asia and Pacific and Australia 1986-1991 Councillor of Embassy in Rabat, Morocco 1991 - 1992 PZ SOLPOL

*At the time of becoming the CEO.

Sources: Elektrim's announcements at gielda.pl and Polityka Dzial Kadr

The situation was characteristic also for other CEO's of other Polish FTOs as well as for their employees. In case of economy which was autarkic to some extent, and with the domestic enterprises being only production units with no intent to market their products [Smith, 2000], the knowledge of FTO's management resulted in competitive advantage, a strategic resource that could be combined with other assets to enhance value. This "transaction" took a form of acquisition of domestic enterprises as the FTO's were one of the few entities, which had financial resources inherited from the time of centrally planned economy. Elektrim's knowledge of the Polish manufacturing companies that it worked with helped it to circumvent informational problems associated with the efficiency of take-overs. Also, the management of Elektrim encompassed general management expertise and capabilities that were relatively scarce in the transition years in Poland. Finally, its preferential access to bureaucracy and policy makers, especially important in telecom, gave it great advantages over independent firms.

From the outside, the initial transformation of Elektrim might look like establishing a company like Mitsubishi, Sumitomo and Mitsui - Japanese industrial groups led by trading companies (former zaibatsu). However, the business history of Elektrim suggests it did not want to operate as a network organiser or the core of a new industrial group where individual diversified firms would find significant advantages in exploiting intra-group externalities in cheaper finance, secure demand and supply, etc. In many respects the frenzy of acquisitions from the early-1990s suggest that Elektrim behaved like some other CEE tycoons who put the opportunity to 'build empires' over the profitability of individual operations or over the exploitation of synergies among intra-group firms.

There is a literature that suggests that in emerging markets or economies with undeveloped market institutions, business groups like Elektrim may have significant advantages over focused enterprises [Khanna, 1997][Palepu, 1999]. The advantages of industrial groups have been analysed also in economies with developed market institutions [Kester, 1992][Jacquemin, 1982]. The underlying factors behind the growth of diversified business groups are in multi-market power, related resources, informational imperfections, entrepreneurial scarcity and policy distortions in the emerging market environment [Khanna, 1998][Palepu, 1997]. These factors have played an important part in explaining Russian industrial financial groups [Petkoski, 1997]. The case of Elektrim suggests that some of the factors that work in favour of such groups are relevant in explaining its initial growth. The grouping of unrelated businesses has helped Elektrim to gain market power and improve access to outside capital. Moreover, to help finance its growth, Elektrim moved into banking. It founded a medium sized commercial bank and owned stakes of up to 11% in four others. However, most of these were too small to be of much use.

The beginning of 1990s in Poland were the times of fast and uncertain changes and the post-transformational recession. Foreign investors involvement in the Polish economy remained small as it was perceived as unstable and not secure enough for regular transactions and allowing only for minor speculative inflows. That implied a firm like Elektrim faced little competition when it was bidding for under priced privatised assets. However, since the 1993 Polish economy returned to the growing path, regaining its 1989 GDP level in 1996 and continuing fast growth of more than 5% annually. This attracted foreign investors to this emerging economy and the inflow of FDI increased considerably.

There were also changes in the domestic management. Firms and their managers learned how to operate in the domestic as well as in the foreign markets. This stripped the Elektrim of the main competitive advantage.

The changes in management observed in the Polish economy were also bound with the new generation of middle level managers educated in the Polish economic schools after 1989. They started their career also in the FTOs introducing to some extent new management culture. However, these changes were not fully accommodated by the 'old' managers, even those, who had been accustomed to the foreign trade practices before 1989. The best example of such problems was Elektrim case of PTC and Kulczyk (see Section 3).

The shift from conglomeration to focusing was a sign that, as we pointed out, many of these advantages did not operate any more in the Polish economy. Companies were able to access capital under similar terms as a large business group, markets for management skills had developed and the market environment became more stable. However, the aggressive strategy of Ms Lundberg was only possible because of the high trust provided to her by the foreign investors and subsequent lack of willingness to admit that this confidence was a costly mistake, leading to the bankruptcy. The experience of Ms Lundberg was shaped in the venture capital institutions, especially foreign, and was not well suited for the conditions of big Polish enterprise in need of focusing its activities.

The subsequent CEOs were educated in the free market environment in Poland or abroad. They were relatively young and bound with international investors earlier, like Mr Karwiec, who was designated as CEO by Nomura to the Impexmetal. Their role was to rescue the company and avoid bankruptcy. This task was accomplished by Wojciech Jańczyk, who was send to Elektrim by the BRE Bank. From managerial perspective, we can say that being a graduate of London University he also gained his experience in Polish environment working for public as well as for private sector. This nomination marked also the return to the more active role of the Polish shareholders and withdrawal of foreign investment funds.

The clear mark of the next era was a nomination of Piotr Nurowski as a CEO by the main Polish strategic investor (Polsat Media owned by Polish businessman Zygmunt Solorz, also the owner of the private television Polsat). The new CEO was well established in the old socialist period, working for the Ministry of Foreign Affairs as well as in the new free market period, working for Solorz. To the same extent we can compare his experience to Mr Skorowński's but with additional 15 years of free market training [Mizerski, 2005].

Thus, the stabilisation period coincides with the return of Polish strategic investor and focusing on the initial area of expertise – energy. Here, PTC could be treated as an asset, although frozen by the legal dispute as of 2005, which could potentially finance the main area - energy. However, the action of transferring the PAK out of Elektrim in late 2005, mentioned before, could suggest that Elektrim still faces bankruptcy and partition, as the strategy of the Polish dominant owners is unclear, with some best assets being transferred out of the firm.

The current situation is similar to the other former FTO – Impexmetal, which concentrated again on its initial area: metallurgy. In 2005 it was bought by the internal investor Boryszew Group owned by Roman Karkosik. The new owner delegated his manager Sławomir Masiuk for the post of new CEO with the task to restructure the holding. The Boryszew-Impexmetal group is going to concentrate on packaging through its two pillars: Boryszew as a provider of plastic components and Impexmetal as a provider of aluminium components. However, at the time of writing this firm is much more stable, while the fate of Elektrim is very uncertain.

6.2 The international investors

The institutional framework features strongly determining the modes of growth of enterprises. Within this perspective it is useful to distinguish between three basic modes of growth in any enterprise: generic expansion; mergers & acquisitions; and networks (alliances) (see Peng and Heath, 1996). Undercapitalised enterprises with limited management capabilities have difficulty in growing through generic expansion. Among the top companies in CEE, there were only few new private firms in 1990s and early 2000s. Mergers and acquisitions were limited to foreign investors who have the funds for take-overs, and to domestic companies like Elektrim. The difficulties that Elektrim had to overcome to grow independently have been confirmed through its difficulty in remaining a sustainable independent player rejecting the takeover of key assets by Deutsche Telecom and later on Vivendi.

Unfortunately, handling of the relations with two strong international investors with contradictory interests turn out devastating for the Elektrim. The management problems resulted from this were analysed in the previous section. In case of finance, joint venture with Vivendi could give Elektrim access to much needed capital and expertise in the telecommunication sector. Instead it provoked long lasting legal battle with Deutsche Telekom. Even Elektrim licences giving it access to the telecom market, which the company hoped to trade for access to finance and technology turned to be illusionary in the situation where it became the battle ground between the two big external players.

This legal struggle is an immediate reason of difficulties of the company. Its only healthy part: energy, was either transferred to another entity (PAK) or suffered from know-down effects which in fact undermined all future activities (Megadex). As of 2005, Elektrim seems to be a hostage of its PTC ownership and its only reason for existence may be the unresolved conflict between Deutche Telkom, Vivendi and Mr Solorz, all of them struggling to get independent control over the whole PTC.

The cases of alliances in CEECs (Radosevic, 2004) suggests that the balance between generic expansion, alliances (networks), and M&A as modes of growth, reflects differences in firms' abilities to control technology, access to market and finance. Elektrim's access to the domestic market enabled it to trade it for access to capital. But this opportunity was lost because of the risky expansion strategy followed by the wrongly designed international game plan. If we take a look into the other former FTO, we can conclude that there were possibilities to grow effectively, either at slower pace using only domestic capital (the Impexmatal, see section 7.1); or choosing one strategic investor and selling its access to market (the case of Animex).

However, the underlying most important problem in case of Elektrim was lack of strong strategic investor in the expansion phase:

Moreover, unlike owners with a vested interest in maximizing profits, professional managers gain little from direct profit maximization. They will not be interested in profit maximization per se or the maximization of shareholder value as an end in itself. Rather, they seek to maximize their own *power, prestige and affluence. Such motivations are more closely aligned with the growth of the firm.* [Dunn, 2005].

Yet, as we can clearly see in the case of Elektrim, an independent growth strategy may be very risky, especially if it focuses on new technology industries, which may follow an initial boom and bust cycle. The management of Elektrim was not controlled well enough by any shareholders with clear long-term vision of the company's future. Therefore, main role was played by the management. Their visions were not coherent and often changed completely: from wide diversification to selective focusing together with huge investment. From a strategic perspective, large block shareholders may not allow for a poor strategy, such as diversification, to evolve into poor performance, therefore decreasing the magnitude of restructuring [Gibbs, 1993; Hoskisson et al., 1994]. On should stress however, that in the case of Russia, Filatotchev *et al.* [2001] argue that *large-block shareholding is negatively associated with the firm's investment and performance, and this relationship does not depend on the identity of controlling shareholders.* The difference results from the fact that unlike Poland, in the latter case, we see the environment, which does not adequately protects minority shareholders, creating very different incentives for dominant stakeholders.

Thomsen et al. [2000] argues that institutional investors, who are relatively wealthy have strong preference for portfolio management and diversification. This could be in line with the initial period of activity of Ms Lundberg and support she had from the side of financial investors making her CEO. The story of Elektrim supports also another of his thesis, namely that corporate owners are likely to emphasize business transactions and growth instead. As the example the initial period of Mr Skowronski and final, of Mr Nurowski, could serve.

We can also notice one connection with resource-dependence theory stating that not all outside directors could have a have a positive impact on firms performance. Peng [2004] suggests *that only affiliated (mostly institutional) directors play a positive role*. (…) *In contrast, non-affiliated (mostly individual) investors have no influence on performance (...) only resource-rich outsiders such as institutional directors are likely to contribute to firm performance, and that resource-poor outsiders such as individual directors, despite their presumed incentive to influence management per agency theory logic, may be unable to contribute*. In case of Elektrim Barbara Lundberg and Piotr Nurowski could be seen as examples of this theory.

Table 10. Elektrim Evolution –Development Dimensions

	Stage 1 Foreign Trade Organization	Stage 2 Production/ Trade Holding	Stage 3 Aggressive growth	Stage 4 Rescue	Stage 5 Stabilisation
	1945 -1990	(1990-1997)	1998-2001	2002-2003	2003-2005
Management	Old socialist; Polish	Foreign Trade graduates accustomed to free market environment; Polish	Internationally educated; Foreign	Internationally educated; Polish	Old Polish but trained in the new business environment
Owners with main influence	State	State and private internal	International Financial Institutions	International Financial Institutions with increasing role of Polish investors	Polish investors and International investors (Specialised holdings)
Main Functional Area	Trading	Production	Infrastructure	Undecided	Infrastructure
Business Strategy	Exclusive Intermediation	Opportunistic Conglomeration	Diversified Specialization	Assets sale	Narrow specialisation
Relations between key stakeholders	Role-Exclusivity in foreign trade	Implicit Sponsorship of stock market manoeuvrings	Emerging Conflict	Conflict	Conflict resolution
International Relations	Russian connection	Buffering by state/limited foreign ownership	Majority diversified foreign ownership Emerging Conflict	Conflict	Inherited Conflict
Corporate Governance	State ownership	Commercialization/some state ownership	Fully private; number of key owners: 8-10	Fully private; number of key owners (5-7)	Fully private- number of key owners (4)
Organizational structure	Unitary organization	Holding	Multi-divisional corporation	Holding	Holding
Primary Objectives	--Intermediating deals; --Bargaining over the plan and resources with the state administration	--Building financial management skills; --Building internal governance mechanisms in select business areas; --Cooperating in Cables (initial specialization); and telecom (ERA GSM - initial diversification)	--Telecoms (fixed, cellular, internet); --Energy; --Centralizing business/ investment strategy; --Profit-centre creation; --Narrowing of the portfolio --Alliance-building and financing projects	Survival	- Energy - Mobile telecommunication

Source: authors except stages 1 and 2 which are partly based on Radosevic et al (2001)

The fate of Elektrim is still undecided as of late 2005. As we have seen, at the time of writing, paradoxically, the main reason of its continuing existence is the complex nexus of ownership disputes, in particular over PTC equity it controls. The question is whether it is enough to survive and for how long this situation would last? Although the firm is still on the market, its days seem to be counted.

It also seems that this fate was not unavoidable. Other former FTOs chose different strategies and now have good prospects for future development. The problem of Elektrim resulted from a combination of wrong managerial strategies, which arguably, resulted from the lack of strategic investor, who could have influenced the firm's management. This, together with market difficulties resulted in situation, which does not provide much hope for the future. The deadlock, which keeps Elektrim alive could be easily ended with the agreement of main actors: two international investors: Vivendi plus Deutche Telkom and domestic one – Mr Solorz. With it in place, the case of Elektrim and Elektrim itself will cease to exist.

Post Scriptum

In the time of preparation of the publication, until spring 2006, Elektrim have still existed. PTC shares were transferred there and back: first to Mega Investments and then back to Elektrim Telekomunikacja due to the court order settling the complaint of DT. However, the management board established by Mega Investements does not allow DT nominated "old-new" board to carry on their responsibilities. On the other hand DT covers current operational costs of PTC, what is declared illegal by the Mega Investment Board. DT also sued Elektrim Investments and PTC to transfer 48% of disputed shares in International Arbitration Panel in Vienna. The broad dispute still involves the same three parties: two international – Vivendi and DT plus Mr. Solorz and is far from resolving.

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