

Digging deeper

Entering a new era of consolidation

Trailblazers needed

Why are entrepreneurs hard to find in CEE?

Green dream

Moving towards a low-carbon world

Switching tactics

Why CEE creditors should follow London's lead

Transform

Issue 5/Spring 2010

Insight for CEE's business leaders

Aiming high

How CEE's leaders are navigating the new climate

Rethink
Strategic planning

Reshape
Risk assessment

Result Seeing in the dark

Our challenge is to chart a safe course to success through good times and bad, without knowing which future will come to pass.

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PRICEWATERHOUSECOOPERS 

Winning in action



A new year often prompts a new outlook but I'm certain that, like me, business owners, managers and executives throughout the region will not forget 2009 in a hurry. Most of last year resembled a rollercoaster ride as we helped clients re-engineer their businesses and navigate the turmoil. Working closely with some and watching many more begin to emerge still standing, looking stronger and able to cope with the market, were the highlights of my year.

Consequently, I believe that 'Winning in Action' will be a major theme of 2010. It's a theme I spoke about when I recently hosted a conference in Budapest for PwC partners. While no leader will do anything to undermine the long-term viability of their operations, organisations need the actions they take today to generate results as swiftly as possible.

Decisions have not been easy. You all know of organisations that have had to undergo restructurings – headcounts have been cut, balance sheets restructured and executives replaced by a new generation that can live with constant change. These new leaders are forging their reputations during these tough times.

They will be judged not just on how they cut costs but also on how they grow, whether that be through consolidation or by spotting and exploiting a niche in the market, as many entrepreneurs across our region are doing every day. Private investors are re-emerging too – leaders who can demonstrate the potential of their companies will be the ones to win backing.

So despite the market's travails, there remains no shortage of great opportunities for entrepreneurs and leaders to transform their organisations and industries.

It is the job of PwC to be a partner to them, adding real and sustainable value, however difficult the situation. That is the essence of Winning in Action.

Mike Kubena

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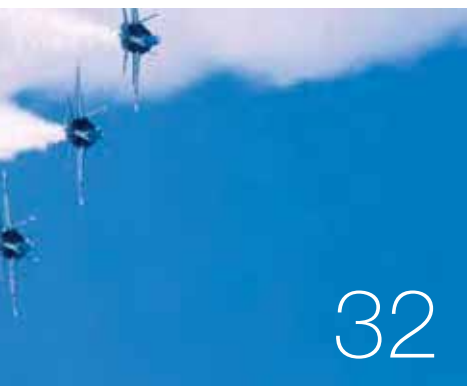
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Taking the pulse

How do organisations motivate their employees, especially during a financial crisis? It's a question that prompted PwC to conduct its first CEE and CIS-wide *HR Pulse Survey* to find out how HR teams had responded to the downturn over the past year and to gauge the morale of employees.

Responses from nearly 600 companies across 20 countries revealed that around a quarter of companies are reducing headcount while nearly half are reining in their promotion plans compared to 2008. There were striking differences along industry

lines. "Comparing different sectors on reductions in headcount, a higher percentage of companies in production and publishing had to make reductions compared with, say, pharmaceuticals," says Stephen Quick, HR consulting leader at PwC Russia. There were some differences along geographical lines too. Employers in Central Europe seem to have made more drastic reductions than in Russia and CIS, for example.

How have such cost-saving measures affected employees? Quick says 41% of employers did have concerns that these measures had a negative effect on the way they were perceived by employees.

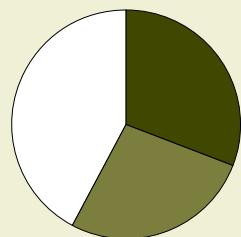
As a result, he believes, more companies are exploring ways of improving employee engagement.

"Pay is the biggest bill for most organisations," says Quick. "To get the best return on their investment, employers need to know what they can do to retain employees. Initiatives such as employee surveys mean they can be better informed about what's working well and what's not. Bonuses are still important, but there is less money in the pot so that's partly what is driving employers to take a fresh look at other methods of motivating employees, such as training and development."

For more details about PwC's CEE & CIS HR Pulse Survey, contact Stephen Quick at stephen.quick@ru.pwc.com.

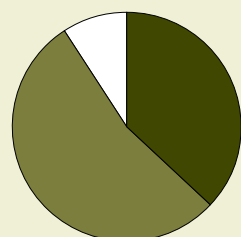
CEE & CIS HR Pulse Survey – key findings (all countries)

Headcount variation

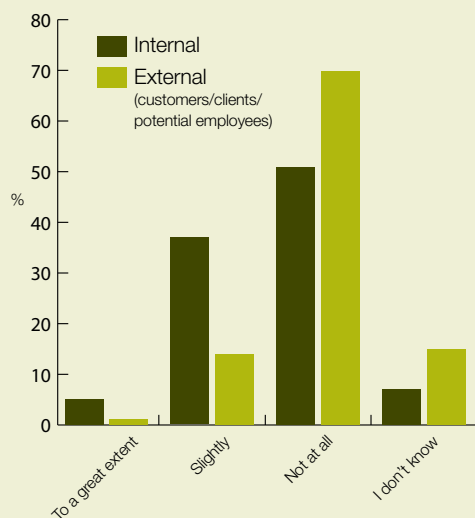


■ Increase 31%
■ Decrease 27%
■ Stay the same 42%

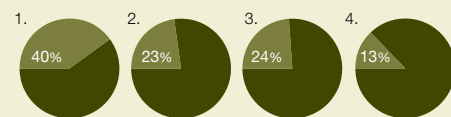
Base pay measures



■ Stay the same 37%
■ Increase 54%
■ Decrease 9%



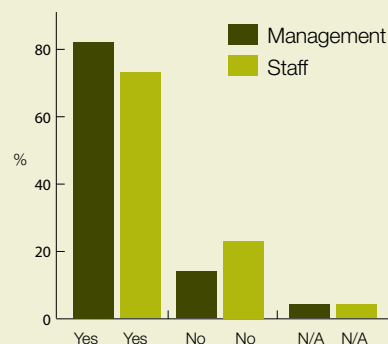
Do you think your company's reputation was negatively affected by the HR measures taken in the past six months?



Promotion plans for 2009

1. Same as in 2008
2. Much less than in 2008 (more than 10% less)
3. Slightly less than in 2008 (up to 10% less)
4. More than in 2008

Is variable pay correlated with company performance?





EVERYTHING COUNTS

Little gestures can help to boost employee morale too. Practising what it preaches, PwC has introduced various small-scale initiatives in some of its bases across the region. In the rooftop coffee bar of its Prague office, for example, every Friday beer is served for free from 5pm onwards. In Moscow, the firm is introducing a number of features in its new offices in the White Square Office Centre. On the 10th floor – dubbed ‘the people floor’ – staff will have access to a Wellness Centre, boasting a doctor’s surgery, massage rooms and a quiet area. The pièce de résistance is the PwC Club Room – 800 square metres of dining area with tables, soft seating, plasma screens, a roof terrace, two bars and a central kitchen where staff can unwind over subsidised food and drink. “The idea is to provide a comfortable facility to keep people engaged and make them more efficient in their roles,” says Richard Gregson, the PwC partner in charge of the office move.

ISTOCK

Hard landing, but still intact

A recent assessment of the economic threats facing CEE countries suggests that Ukraine has the highest mountain to climb as the region seeks to pull itself out of recession.

The PwC report – *Hard Landing: Central and Eastern Europe Facing the Global Crisis* – identifies three major threats to the successful economic recovery of CEE countries: potential difficulties in finding external financing; the threat of a serious internal financial crisis; and a high dependence on the economic wellbeing of overseas countries.

The report says these threats are at their most severe in Ukraine, while they are only moderate in Poland, the Czech Republic, Russia, Slovakia and Slovenia (see chart, below).

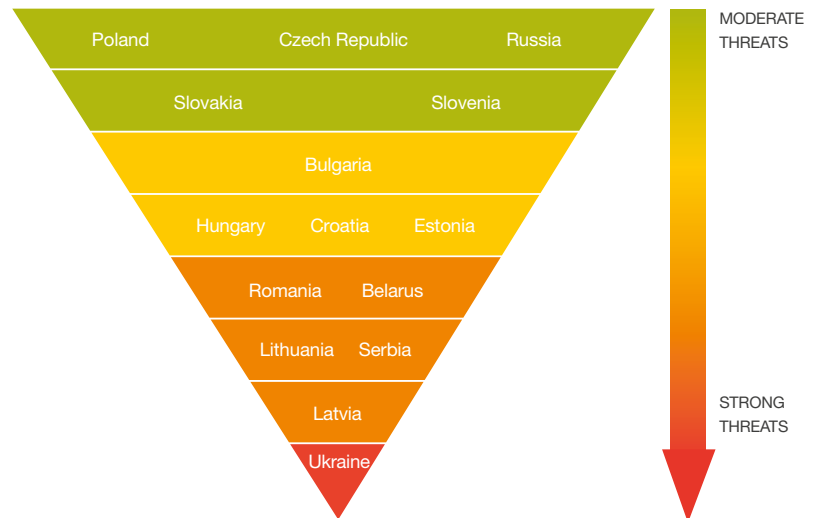
Inconsistent economic reforms, an overheated economy, a low credit rating and political instability have converged to make Ukraine more vulnerable to the

major threats than its CEE neighbours. However, Professor Witold Orłowski, chief macroeconomic adviser with PwC Poland, and author of the report, says there is some regionwide cause for optimism: “The economies of the region share many similarities, and most of all, they are facing similar challenges, and are strongly interdependent. Often, today’s risks are tomorrow’s opportunities. If we take proper advantage of these opportunities, the region will soon return to a path of strong economic growth.”

To do so, Professor Orłowski says the region’s governments need to forge ahead with a number of difficult reforms that will boost CEE’s global competitiveness and its attractiveness as an investment destination.

For more details about *Hard Landing: Central and Eastern Europe Facing the Global Crisis*, contact Professor Witold Orłowski at witold.orlowski@pl.pwc.com.

MODERATE INTERNAL AND EXTERNAL THREATS



STRONG INTERNAL AND EXTERNAL THREATS

Company leaders across CEE are stepping up efforts to link business strategy and operational performance in a bid to improve the way they manage their businesses, according to a new PwC survey.

Linking business strategy and operational performance is a practice commonly known as 'corporate performance management' or CPM. CPM programmes typically focus on financial and operational planning, execution, reporting and evaluation.

Nearly 400 companies responded to PwC's European *CPM Survey: How Do You Manage Your Business?* – 143 from CEE and 241 from Western Europe. The survey found that companies felt they were spending too much time on non-value-creating activities such as data collection, calculation and reconciliation rather than making decisions based on that data to benefit the business. Non-value-creating activities take up 59% of time available – respondents said they wanted to reduce that to 33%.

Respondents also revealed that business intelligence (BI) technology – which provides snapshots of how the business is performing – was helping to improve the quality of data delivery.

The survey found that more fundamental barriers to successful CPM exist in many companies, including complex organisational hierarchies, missing responsibilities and undefined escalation rules.

"CPM is not about implementing KPIs or a BI solution. In fact, that



Beyond the basics

might just give you a headache," says Marc Gössi, a PwC partner specialising in CPM. "But it is about rigorous focus on the strategic value drivers delivering your objectives and full alignment of structure, people and technology with strategy."

In addition, CPM gives managers better visibility across the business. It also delivers improved profitability, although there are various estimates of how much. According to a study by technology research firm IDC, companies can generate a 112% return on investment over five years, while recovering average costs of \$4.5m within 1.6 years.

Strategic elements of CPM programmes have been PwC's area of expertise for some time but following the firm's acquisition of Paragon Consulting Group – a global CPM consultancy – it is now also able to

implement CPM software solutions. Paragon's bases in Singapore, Dubai, Istanbul and London allow it to serve clients in Asia, the Middle East, the Mediterranean and Europe.

When it comes to the prevalence of CPM, CEE is catching up with the rest of the world very quickly, says David Jones, director of Paragon. "These companies have the benefit of not having a lot of legacy processes and systems that act as a drag on the pace of change." Jones believes the expansion through cross-border acquisitions of many CEE-based companies will be the trigger for a growth in demand for CPM solutions as those firms deal with integrating disparate systems and processes. The challenge, he says, will be helping companies to understand what CPM can do for them and how quickly it can produce significant returns.

"Companies were spending time on non-value-creating activities like data collection rather than making decisions based on that data"

С днем рождения!*

New home: PwC Russia marks its 20th anniversary with a move to new offices in Moscow's White Square Office Centre



As PwC celebrates its 20th anniversary in Russia, it is worth remembering how far the company and the country have come in that time. In September 1989, both Price Waterhouse and Coopers & Lybrand boasted representative offices in Moscow manned by a handful of hardy expatriates.

Wind forward two decades, and the merged PwC employs more than 2,000 people spread across six Russian branches, including new offices in Kazan, Ekaterinburg and Vladikavkaz.

Peter Gerendasi has seen the firm change before his eyes. The native Hungarian emigrated to Australia as a young boy, returning to Budapest in 1995 with PwC, heading up the firm's CEE and CIS tax and legal services division from 2002. In January 2007, he moved to Moscow to head up the wider Russian market, taking the reins from Mike Kubena, who became partner in charge of CEE.

Gerendasi is keen to point to the firm's Russian growth potential and the increasing 'Russification' of the company's domestic operations. "We take pride in the fact that as we celebrate our 20th anniversary, the majority of our partners are now Russian nationals, and that we have Russians sitting on our leadership team."

The future in a carbon-rich country of 140 million people acting as a bridge between centres of power in the East and the West is virtually limitless.

** Happy birthday!*

Mostly good, some bad

Reports of CEE's economic woes have probably been exaggerated



DANIEL THORNILEY

The consensus view is that emerging markets are pulling the global economy out of the depths of a near-global depression. But having been the blue-eyed boys of the global financial markets from 2003 to mid-2007, emerging Europe is now depicted as a major global loser and a weak link in global emerging markets. Why waste time and money in CEE when you can make a packet in China, India and Asia?

The good and the bad times are probably both exaggerated. CEE has taken massive strides in the past 20 years. The region and the quality of life of tens of millions have been transformed for the better but, clearly, mistakes were made and much remains undone.

FIRST, THE GOOD NEWS

For starters, 10 countries have been integrated into the European Union (EU); some have joined the euro and others will join in 2013-14. The global financial crash and the vulnerability of local currencies convinced many in the region that it is time to get into monetary union; many sceptics changed their minds. The perversities of the Maastricht entry criteria at a time of virtual deflation will mean delays; nevertheless, Hungary, Poland and the Czech Republic should be in by 2014.

Second, East and West Germany were peacefully reunited, even if many 'Ossis' still bear grudges. West Germany poured huge amounts of money into rebuilding and subsidising the East, which may be one factor holding back other sectors of the German economy, including personal consumption: so there has been a cost.

Third, people's lives have improved remarkably, but one should not be taken in by the glitz of the capital cities where the nouveau riche are congregated: Warsaw is

not 'Poland' and Budapest is not 'Hungary'. Western companies can miss this point, as most of their consumers – and their local staff – are located in the capital or the second city.

And finally, the EU has been a driver for political stability and slow-but-steady institutional improvement, and for ensuring greater transparency in tax and legislative matters. Nothing is perfect (just as in Greece or Italy), but the trend is inexorably in the right direction.

BUT WHAT WAS CEE'S ACHILLES' HEEL?

The weak spot for the region (including Russia and Ukraine) was that corporate and personal retail debt levels shot up too high and too quickly. When the market turned, CEE was left exposed. Rating agency Moody's issued a report in February 2009 that caused local currencies to accelerate downwards. In very simplified terms, the report implied that with \$1.5trn of debt and about \$400bn to pay in 2009, the whole region was on the verge of bankruptcy, which would pull down all the Austrian and some German banks, and ensure the collapse of those economies as well as the whole of CEE. The region was on the brink.

However, it became clear that the International Monetary Fund, World Bank, EU and European Central Bank would not abandon the region, and that the Austrian banks would not simply pull out, leaving CEE to its fate. It quickly became apparent that uncontrolled defaults would not be allowed (not even in Ukraine); currencies stabilised and the worst was over.

Did CEE open up its banking and financial markets too quickly? The answer until June 2008 was no; the answer today is probably yes. But everyone else, except China, fell into the same trap. China has survived the global crisis best because it kept control of its banks and currency; the country implemented a fiscal expansion and put credit behind it.

With 80% of local banks owned by Western ones, CEE was most vulnerable to the global banking collapse. In addition, many bank customers in the region took out low-interest-bearing mortgages in Swiss francs and euros in 2005-08; this looked very clever back then, but millions of people have seen their mortgage payments spike as local currencies fell 5-20%. The good news is that local currencies overall have stabilised and rallied; their medium-term outlook is for steady appreciation, thanks to convergence and EU membership.

Questions have been raised about whether Romania and Bulgaria were allowed into the EU prematurely. One can rightly question the move. However, EU entry has ensured



“The human resource skill set in CEE is probably the best in the world. Companies operating in the region consistently state this”

political stability and protected these two markets from the worst of the global crash.

Former Yugoslavia looks pacified for now, but the societies were ripped apart while the West stood to one side; people have been traumatised for generations to come. It is unlikely that more of these countries will join the EU soon, due in large part to accession fatigue in EU institutions and among the EU population. Croatia could possibly join in 2014-15, but this now seems unlikely; Serbia's chances are even more remote.

GDP on average in the main markets will be down 4-5% in 2009 and will then grow about 2.5% in 2010. It is then expected to pick up to 3-4% per annum in 2011 and through to 2014. The real winner is Poland, which was the best-performing economy in the whole of Europe at the end of June 2009. The country went into the crisis in a strong position and has fared remarkably well: it will be one of the few manufacturing nations of the world posting positive growth (1.3%) in 2009 and then a steady 1.8% in 2010.

There are other silver linings. In addition to a reasonably good savings ratio, activity in the black/grey market is bolstering economic activity. It may not be something the West supports, but it does go some way to explaining why some corporations post better results than the macroeconomies would suggest.

EU funding is having a noticeably positive effect on the region, boosting the quality of public infrastructure, governance and commerce. Weak currencies will ensure a strong export market, and the wage differential is still marked enough to attract companies that want to set up manufacturing plants there. In fact, the labour equation in CEE can prove just as attractive as in China for companies that want to supply Europe, when transportation costs are considered.

Finally, the human resource skill set in CEE is probably the best in the world. Companies operating in the region consistently state this. The Soviet educational system was exported to the region after 1948 and this extremely good model was superimposed on to already sound existing systems in core Central Europe (Hungary, Poland and then Czechoslovakia). Learning through discipline and solid skills in the hard subjects of maths, science and engineering was a feature of the region's human resources. As long as a wave of management training and marketing degrees doesn't change this, CEE economies have many reasons to be cheerful. ■

Daniel Thorniley is president of DT-Global Business Consulting in Vienna, Austria.

WORLD LEADERS, WORLD CHALLENGES

All eyes recently turned to Davos, as business and political leaders gathered for the World Economic Forum's annual meeting. The forum's focus in 2010 was on six areas: making economies stronger, mitigating global risks, ensuring sustainability, enhancing security, creating a values framework and building effective institutions.

Has this allayed the concerns of CEOs whose confidence about business prospects plummeted in 2009? PwC released its *13th Annual Global CEO Survey* at Davos, and the findings reflected a more positive outlook for 2010. This year, 31% of CEOs described themselves as "very confident" of achieving revenue growth over the next 12 months, up 10% on 2009. The prevailing atmosphere is one of cautious optimism but lessons have been learned the hard way. Companies are addressing risk assessment and management, with more CEOs intending to change their risk management process than any other element of their strategy, organisation or business model.

As we reflect on these findings and the discussions at Davos, *Transform* asks four leading figures to comment on how well business and political leaders have handled the economic crisis, and what they should focus on next.



Sergei Guriev

Rector
New Economic School, Moscow

"In their response to the global financial crisis, political leaders have, in a sense, outperformed expectations. While coordination between different governments' strategies has been lacking, everyone expected the outcome to be much worse. That said, the situation is still not good. Governments still need to focus on post-crisis development, namely how to resolve global financial imbalances and how to improve regulation of the financial sector.

The main risk is that this post-crisis development loses momentum. The good news is that the US, which remains

the global superpower in most cases, is now much more multilateralist and much more interested in cooperation. However, the danger is that President Barack Obama's domestic agenda will distract him from these global priorities.

The greatest priority is to sort out the financial services sector. Regulation should be improved and then we have to figure out how not to kill the incentives for financial innovation. Too much government control over the financial system will damage restructuring and growth.

As for business leaders, they need to work with their respective governments and show a certain degree of self-restraint and conservatism in the way they manage their risks. Many of the companies that failed badly during the downturn were too focused on the short-term outlook and took too much risk. The private sector should think about how it can produce longer-term performance incentives for employees.

This latest downturn has been very painful for this part of the world. While the former Soviet Union got hit by the fall in oil prices, CEE was hit by the seizing up of capital outflows. In both cases, it was a great shock. Yet this does not imply that the whole free market model is bad. Some areas need work – improving the regulation of banks, expanding social safety nets and reinforcing the IMF's role as the creditor of last resort – but the crisis doesn't mean we have to go back to the Soviet system or quit the European Union. Most people don't even talk about that but some do. Crises do happen but you have to be prepared for them. It's important not to panic."

The New Economic School was established in Moscow 17 years ago and is a centre of economic research and education in post-communist countries.

"The main risk is that this post-crisis development loses momentum"

SERGEI GURIEV, NEW ECONOMIC SCHOOL, MOSCOW

The long slog: political leaders may have helped steer economies in the right direction following the global economic crisis, but many challenges lie ahead





Martin Novak

CFO
CEZ Group

“The downturn has affected business and governments in different ways but both have suffered a decline in revenues. Governments are facing rising levels of state budget deficits just as they need more cash to support their banking sectors and industrial companies. At the same time, many business leaders are watching their revenues slide very quickly.

Business leaders have responded in a fairly expected way and have started to take any measures they can to improve efficiency. These are the companies that will survive the crisis and be more efficient when they emerge the other end.

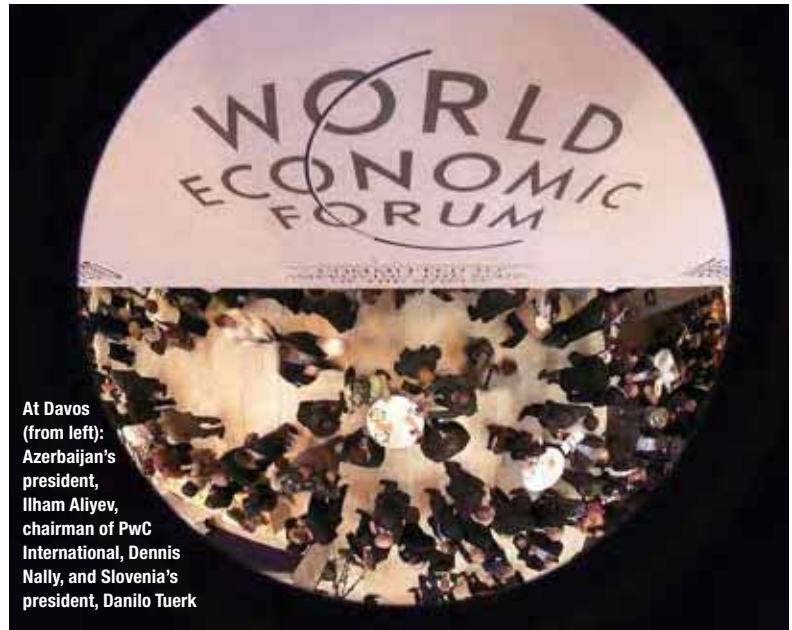
One of the key lessons companies should take away is the risk of using too much debt to fund fast expansion on the assumption that demand for their product or service will always go up. When this doesn't happen, there is really nowhere to go. Firms should use this knowledge when they plan for future growth.

CEZ has been impacted by the recession too. The biggest issue for us is the decline in electricity prices accompanied by the decline in consumption. Due to diligent risk management, we have hedged ourselves against fluctuations in electricity and currency prices three years ahead so we have not been impacted so dramatically. The only impact came from the part of electricity volume that was not purchased by our industrial customers and we were forced to resell it at a lower price. Compared to overall earnings, the effect was not material.

Governments have supported the financial sector by investing billions of dollars and euros. While original thinking may have been that a sizeable company or bank that is not able to survive should fail and go bankrupt, that is just not politically feasible these days. Governments could not let half of the banking sector disappear. They should deal with the level of debt that mounted and prepare plans to privatise all those institutions that are now state-owned.

Business leaders should be focusing on the recovery. Many companies were significantly hit so business leaders of those companies that survive in a reasonable shape will have many opportunities to redefine their product or service markets and possibly acquire complementary companies at discounted prices. For companies that were severely impacted, they should now be looking at building up their order books again.

One pitfall to bear in mind, however, is overestimating the speed of the recovery. Optimism is very important, but companies should also think about more neutral scenarios in terms of growth in the near future. Companies should



At Davos (from left): Azerbaijan's president, Ilham Aliyev, chairman of PwC International, Dennis Nally, and Slovenia's president, Danilo Tuerk



establish effective risk management practices if they don't have them yet. That way, companies can survive when the next recessionary wave comes.”

CEZ Group is a Czech Republic-based electricity generator. It is among the 10 largest energy companies in Europe.



Michael Sauer

CEO and managing partner
Visor Holding

“To restart the global economy, we need to get the consumer back spending as soon as possible so we need to address the unemployment problem across the West, and CEE for that matter.

Although government responses to the downturn have been different from region to region, across the board they have done a pretty good job. The initial responses may not have taken into account the magnitude of the crisis and, in

“When you go out and help an industry directly, you have a better chance of saving jobs”

MICHAEL SAUER, VISOR HOLDING

retrospect, the full policy responses were a little slow. That said, all the measures that have been taken in an attempt to get the economy going again – financial support to get liquidity back into the system and the deleveraging of banks, for example – are starting to work.

The US has just gone through an earnings season and all those who reported came out with good earnings – predominantly by cutting costs, which means they are making money but the top-line growth isn't there.

That's why we need to get people back into work and back in the shops. Governments need to think about whether they are spending the resources they have in the right places. Some administrations have pumped money into their stock markets – I don't think that's the right way to support a system. When you go out and help an industry directly – as the US and many European governments have been doing with their automotive sectors – you have a better chance of saving jobs.

Businesses can only go so far on their own. Access to credit is extremely limited, especially in CEE, due to the deleveraging of the banking sector and its new-found risk aversion. I believe we could see more banking problems in Russia and Eastern Europe. Only around 42-50% of banks have deleveraged. If asset prices stay up and there's liquidity in the market, then there won't be a big problem but if we see a second liquidity crunch, a lot of people could get hurt.

There is no single thing a business can do to avoid this, but it often boils down to having good banking relationships. Government help will go some way to easing the pressure on banks but it's not necessarily the responsibility of governments to go out and take care of all banks' problems. They don't have enough funds to solve all the problems so they have to be selective. Governments are doing their best although, in retrospect, we could have had better oversight.

This financial crisis was driven by greed but I don't think it was just the greed of bankers driven by the prospect of large bonuses. Everyone appeared to like the economic growth that was being driven by easy credit and high leverage and, while the going was good, nobody wanted to get off the bandwagon.”

Visor Holding is a Kazakhstan-based private equity firm, specialising in emerging markets.



Stephen King

Group chief economist
HSBC

“The big challenge today is trying to think about how the world will look in two to three years' time, bearing in mind that policies in the West are becoming increasingly austere. The legacy of this global financial crisis is incredibly high government borrowing and incredibly low interest rates.

The world economy looks better but one shouldn't underestimate the amount of life support it's currently on – what has happened over the course of the past two to three years in terms of policy stimulus is phenomenal. That stimulus will have to be withdrawn at some point and, when it is, I think we will find that the initial bounce in economic activity isn't really prolonged and we will end up with a much flatter growth profile in the West over the next few years.

How will other parts of the world, particularly some of the emerging markets, cope with that flatter, austere, rather dull environment? I think they will continue to do quite well. I think that will happen because emerging markets will increasingly trade with each other and borrow and lend to each other. So we will see new links established between emerging world countries that we haven't seen in such great size before.

“The world economy looks better but one shouldn't underestimate the amount of life support it's currently on”

STEPHEN KING, HSBC

Also, because US interest rates have been very low, investors will be borrowing in dollars and looking to invest elsewhere in the world – that will also be a very positive story for emerging markets.

Sustaining this growth will be a challenge though. Policymakers must ensure they don't go down the protectionist route. The biggest risks to globalisation and economic development tend to be political rather than economic. Bad decisions taken by policymakers who reflect local fears rather than the global reality have to be avoided.

With this period of austerity in the West, unemployment will be relatively high, which means it will be relatively easy to try to find scapegoats elsewhere in the world. It's not so difficult to argue that if, say, China is growing at around 8-10% a year, it becomes an obvious scapegoat for pressure groups in the US or the UK to blame. So protectionism has to be avoided. Business leaders need to get this message across as clearly as possible because they have a vested interest in making sure that protectionism does not come through.” ■

A man with short brown hair, wearing a dark suit jacket, a light blue and white striped shirt, and a dark tie with light-colored diagonal stripes, is shown from the chest up. He is looking slightly to the right of the camera with a serious expression. The background is dark with some out-of-focus light spots.

“Romania cannot
come out of the
crisis by itself”

BACK ON TRACK

Bogdan Dragoi, Secretary of State at Romania's Ministry of Public Finance, explains how reforms are helping the economy return to its high-growth journey

INTERVIEW: EILA RANA

Bogdan Dragoi has had no shortage of challenges to tackle since returning to Romania's Ministry of Public Finance as Secretary of State a year ago. (He had previously held the position between 2006 and 2007 before leaving to do a stint as General Director of the Economic Department, Municipality of Bucharest.) Financing a 2009 budget deficit of 7.3% in a financial crisis is tough but it's even tougher when a degree of political uncertainty, though to be expected ahead of elections, is thrown into the mix. Romanians returned to the polls just before Christmas after President Traian Basescu and his rival – Mircea Geoana – tied with just over 30% of the vote each in November elections. The political limbo has made foreign investors nervous, forcing Dragoi to turn to the domestic market for help. Credit ratings agencies are also concerned that political uncertainty and a shrinking economy could make Romania a high-risk bet. On top of all that, Dragoi has been forced to bat off claims that Romania has failed to properly absorb millions of euros' worth of pre-accession funds received from the European Union (EU).

Dragoi is undeterred, however. In addition to tackling government bureaucracy, he is overseeing reforms designed to rein back public spending and tackle the budget deficit. In the hope that his reforms will have gone some way to restoring investor confidence, he is also starting to test market appetite for longer-term government bonds. He told *Transform* how he is helping to get the Romanian economy back on its feet.

The EBRD expects Romania's economy to have shrunk by about 8% in 2009 after strong growth of 7.1% in 2008. What is driving this decline and how is it impacting the country?

This is due to a contraction of investment and consumer spending, offset to a certain extent by an improvement in

net exports. Our economy is a small, open one, which is sensitive to the wider developments in the EU and the world economy. We expect a gradual recovery, with an estimated 0.5% gain in real GDP in 2010.

What sort of measures are you putting in place to ensure this growth continues beyond 2010?

The government first needs to put its own house in order. We need to spend public funds more efficiently and restructure the administrative apparatus. Moreover, we have to continue to improve performance on tax collection and reduce tax evasion. And we should promote cautious policies accompanied by structural reforms in the pensions and wages areas.

The Romanian fiscal system has competitive advantages – the main two being the flat income tax and the profit tax, both at 16%. However, frequent changes in law and insufficient regulation are key factors that have to be addressed. Moreover, key reforms have to be implemented in the state-owned enterprises to reduce their losses and allow a cut in the subsidies and transfers from the state budget. Overall, a move from current spending to capital spending is needed.

Romania recently took receipt of €300m, the first tranche of a €1bn loan from the World Bank. Can you talk us through the policies these funds will be used for?

According to public debt legislation, the money can be used for budget deficit financing but subject to the fulfilment of certain conditions in key reform areas (unitary pay law, fiscal responsibility law, pension legislation).

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The government assumed responsibility in September for three of these laws. The unitary pay law, which has already been approved by Parliament, will be gradually implemented to reduce the public sector wage bill from 9.4% to 7% of GDP by 2015. And progress has been made towards a final draft of fiscal responsibility and pension legislation. Under the fiscal responsibility law, legislation is expected to be passed to standardise the costs of local government and remove extreme local disparities in areas such as staff numbers.

We are also enacting legislation to create a unified system of public sector pensions and we are looking at a number of improvements in social policy. Measures will be taken to streamline the social assistance programme and, in July 2009, the minimum guaranteed income was increased by 15%. Legislation to improve health services and introduce a co-payment concept in health benefits is being finalised, while a public health awareness campaign will be launched nationwide. We are also seeking to improve the quality of, and access to, education.

In the financial services sector, corporate debt restructuring guidelines will soon be published, aimed at supporting the business environment in the context of the current economic crisis to avoid recourse to court insolvency intervention.

A recent European Commission (EC) report revealed that Romania had failed to absorb €169m from €3bn-worth of EU pre-accession funds. Why did this occur and how is the government ensuring funds are used effectively in future?

First of all, the EC report mentions that it is possible for Romania not to absorb €169m from the pre-accession funds. It is not clear how the €169m figure was calculated as, at the time the report was published in July 2009, projects using 2005 and 2006 funds were still in progress. The amount of 2008 pre-accession funds not awarded stood at less than €100m and, for previous years, more

than 90% of funds were used. The fact that certain projects were completed under budget actually spells savings of pre-accession funds and should not be marked as “not absorbed”.

The lower take-up of funds in 2008 was mainly prompted by changes in the EC’s approach, which led to delays in launching tenders and in concluding contracts within the constraints of procurement rules.

On the other hand, the Commission mentioned delays in implementation. Pre-accession projects not finalised during the implementation period still can and will be finalised by the beneficiaries and, therefore, the amounts allocated from pre-accession funds are still to be considered eligible.

So the amount of pre-accession funds that has not been awarded versus the entire allocation indicates a rather good absorption rate. As for the efficient use of community funds in the future, the phasing out of pre-accession assistance is carefully monitored by the Romanian authorities and the sustainability of the funded projects is ensured.

The EU funds were intended for a range of development projects including unemployment projects, labour training, regional development, corporate modernisation, infrastructure, healthcare and education. What are the government’s priorities among these projects and how do you intend to fund them now?

All these development sectors are priorities for Romania and are clearly spelled out in the National Strategic Reference Framework and in the Operational Programmes approved by the EC in 2007. As such, there is no need to choose between them. Funding those types of projects in the future will follow the same rules as at present.

There are plenty of predictions about the outlook for the Romanian economy but what is your personal view?

Romania cannot come out of the crisis by itself but will do so with the global economy, with a similar gap as at the time of entering the crisis – two quarters. In my opinion, the government is responsible for improving perceptions regarding the country’s risk and restoring the confidence of the international community in the Romanian economy.

The Romanian government is expecting economic growth to have a favourable impact on public revenues and, taking into account measures to cut expenditure, will close 2010 on a deficit of below 6% of GDP, down from the 7.3% set for 2009, and move forward with a downward trend in the following years to prepare for adoption of the euro.

More efficient public spending – particularly in the area of pensions and pay – will be key to this overall process. ■

“The government needs to put its own house in order. We need to spend public funds more efficiently and restructure the administrative apparatus”

STRIKING A BALANCE

Transform asks some of CEE's leading businessmen how they are tackling the short-term demands of the downturn alongside the need to plan for long-term growth

INTERVIEWS: CHRISTIAN DOHERTY



The impact of the economic slowdown is still being felt across CEE, challenging even the best companies in the region. Short-term issues of liquidity, access to finance and cost reduction have come to the fore. But have short-term measures trumped long-term strategy? Are firms in danger of losing sight of their longer-term goals to either cash in on fleeting opportunities or satisfy the market's demand for immediate payback?

We sat down with the chief executives of three of CEE's biggest corporate players to find out how they are juggling short-term demands with long-term growth.

Q: What sort of short-term demands has the downturn placed on your business and how has that affected long-term growth strategies?

NH: A few months ago I think the answer would have been far different. Back then we were focused on internal management and addressing the need for strong financial management. But I think the situation is now changing to one of how to position the business for growth again.

It has been difficult: we run a large distribution business, and we were feeling the change in the markets. Russia has seen a boom in the auto sector in the past few years. But in the current situation, there has been pressure on working capital. That has required the reinvention of management to deal with the slowdown. So there has been a change in management thinking.

As performance is looking better and the economic situation improving, some of the more important issues are more about returning to the long-term plans we had in the first place.

PB: Thankfully, we weren't hit too hard by the slowdown because 80% of our business in Poland is based on



THE PARTICIPANTS: WHO'S WHO

Peter Baudrexl is a lifelong Siemens employee. He joined in 1971 and has held senior positions in the planning, finance and consultancy arms of the business. He has worked across the globe and, since 2004, has been the chief executive of Siemens in Poland.

Nick Hawkins is CEO of the ROLF Group of Companies in Russia. ROLF is the leading automotive retailer in the country and Hawkins is in charge of the ongoing development of

the group's operations, which involves managing a number of new business initiatives as well as maintaining senior relationships with commercial and financial partners. Prior to joining ROLF, he was a partner at PwC Russia.

Pavol Lancaric completed his PhD in economics at the University of Bratislava before working in various senior roles within the Slovakian government. After spells at Deloitte and Globtel, he was appointed general manager of Orange Slovakia in 1999.

"We have a much longer perspective, which makes it easier to adjust and adapt"

PETER BAUDREXL, SIEMENS POLAND

infrastructure, which is a long-term business. Second, it's supported by European Union money flowing into Poland. So the downturn's worst effects are limited to some parts of our industrial business, especially the products business. But fortunately that only accounts for around 15-20% of our total revenues.

PL: Short or long term, the customer is most important – they must be in the centre of everything we do, so that means trying to answer people's needs.

Our short-term priority has been to launch projects and services to address that need. For example, we launched a bill insurance scheme designed for those who lose their job or fall into long-term unemployment. Fundamentally, we have to adapt all of the cost structures and processes of the company so that any impact isn't felt by the customer.

Q: Some commentators have suggested that the short-termism of the markets has forced many companies to turn their attention away from long-term performance and growth. Have you found this to be the case in your experience?

PL: It hasn't fundamentally changed the business, but we are investing more carefully than in the past. That is because the return on several investments is likely to be slower than it used to be. Of course that shouldn't impact on long-term strategy, but there are items of our capital expenditure that we may postpone. And we will do that if necessary, unless it is something that would impact on the quality of service that we provide to our customers.

NH: We're a private company, and as such we benefit from not having those market pressures. Thankfully, we have a shareholder who has always taken

a long-term view of the development of the business. We look at the annual picture of course, but in the context of a rolling three- or five-year plan.

In the past year, we deviated from that to deal with the obvious market issues. And now we're looking in detail at how we can get back to that plan.

PB: Siemens in Poland is a private company, entirely owned by Siemens AG. That means we have no need to communicate directly to shareholders or analysts, and we don't have the media rounds or quarterly results.

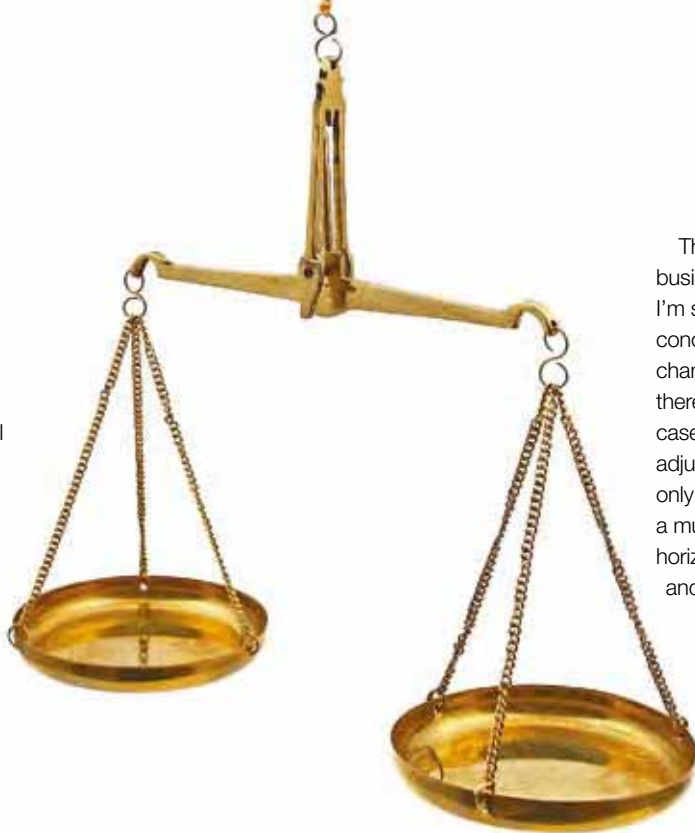
But we do still have to report our progress: our main audience is the decision-makers in the infrastructure businesses that we work with. So that's where we communicate. It is our job to keep them close to communicate the latest in technology.

Q: Do you feel that company success should be judged on long-term performance rather than quarterly numbers? If so, are you trying to encourage this philosophy within your own organisation?

PL: I think it's a dual process. If we were suffering heavy short-term losses for too long, we'd be in the position of not being able to answer the long-term challenges from the market. So we need to work hard on that.

On the other hand, when is the future? It is now, surely. So we have to concentrate efforts on the issues coming up soon. So for example, we faced a substantial decrease of revenues last year. Happily that won't necessarily lead to a drop in profitability, at least in terms of EBITDA on our total revenues. But it means we need to manage our internal processes better. I believe that if we were to concentrate solely on short-term measures, we would get out of the crisis weaker than otherwise.

NH: Out of necessity we've had to be fairly short term in the past year, for sure. The circumstances demanded



"We look at the annual picture, but in the context of a three- or five-year plan"

NICK HAWKINS, ROLF

that things like headcount reduction, cost rationalisation, the extension of financing all became part of the day-to-day strategy. So that's a bit different from quarterly results presentations, but the focus has had to become a lot more short term during the past year.

PB: For us, there are two types of business – the long-term infrastructure projects in energy, rail and so on, and the shorter cycle focused on products. The latter only accounts for 15% of our businesses, and we've been able to adjust our capacity in terms of the sales force, the administration function and so on to the new level of demand.

The same is true if the infrastructure business begins to decline. After all, I'm sure that following 2012 [and the conclusion of the European football championships in Poland and Ukraine], there will be change in demand. In that case, we'll have to make the same adjustments as anyone else would. The only advantage we have is that we have a much longer perspective and time horizon. That makes it easier to adjust and adapt because we will know well in advance that changes are coming. Frankly, if the projects don't get commissioned today then we can plan for that in two years' time.

Q: How are you encouraging long-term performance, what sort of challenges is this posing and are you starting to see this strategy deliver any positive results?

PB: There's no desire to change our strategy. That's for the simple reason that we are a technology company but we are not in a short-term business. Think about how long it takes to develop a new generation of trains or power stations: these are very long-term investments.

And of course our customers expect a long-term, well-planned approach – we can't just sell them a train and walk away. We have to think about warranty, support, spare parts in 10 or 20 years. So our business is, by its nature, orientated to the long term and it will continue to be.

PL: We don't concentrate our activities purely on the short term. We're continually trying to adapt our processes and scrutinise what we do. We do believe that the crisis will ease soon, and while the uptick won't be immediate it will come, so we need to be ready for the post-crisis period.

And we certainly hope to emerge stronger. Internally, we have been able to find reserves in various places, whether in terms of headcount or

better productivity of labour or capital expenditure. And we also believe that the liquidity crisis might even be helpful. Some things cost less than they otherwise might. Some suppliers are prepared to reduce their unit pricing in order to keep jobs or orders, for example. So if there's a chance to spend wisely, we can accelerate. And when that changes, we use the brake.

NH: There has been a cultural change for management. Before, we were heavily reliant on the sales function to drive the business forward. But then in a declining market, financial managers tend to gain the upper hand. Tellingly, that process has made the organisation a lot more robust, and now it's a question of how we start relaxing some of those financial management restrictions and allow the sales function to once again flex its muscles and get the business going again without releasing too many of the constraints we've put in place to survive the downturn. ■

Christian Doherty is a financial journalist, specialising in corporate governance, risk and accountancy issues.



"Our short-term priority has been to launch services that address customers' needs"

PAVOL LANCARIC,
ORANGE SLOVAKIA

FLEXIBILITY, INNOVATION AND GOOD MANAGEMENT

If anyone knows how to steer an organisation through challenging times, Dinu Patriciu does. The former chairman and CEO of Rompetrol – the Romanian oil services company headquartered in Amsterdam – led its transformation from a state-owned asset to a major European oil company with turnover of around \$7bn. Today Patriciu is chairman of the board of Dinu Patriciu Holdings (DPH), a Swiss-based holding company that he fully owns. DPH has over \$1bn in assets and focuses on private equity, real estate and portfolio investments.

The current short-term focus of many companies does not surprise Patriciu. In fact, he says it's an inevitable state of affairs for listed companies but he warns that too many of them operate on this share-price short-term cycle. "Quarterly earnings reports can easily drive the company and prevent decisions that need to be taken to ensure long-term success," he says.

Patriciu reckons his own long-term approach has allowed him to see the downturn as an opportunity, acquiring a number of assets at attractive prices. However, he says timelines for planned exits or approaches to other investors remain unsettled for now. "This is normal in these times. My view is that flexibility, innovation and good management will always be rewarded and we will see companies that display these characteristics emerge strongly from the current economic situation."

These are principles that Patriciu has tried and tested over many years. "For me, as a long-term, hands-on investor, business is about having a vision and creating value based on that vision. The challenge



"Having a diversified portfolio allows us to focus on a variety of long-term opportunities"

DINU PATRICIU, DPH

is to deliver the full potential of a project and for this you need to have the best people involved. This is what I believe creates shareholder value. So I believe in recruiting blue-chip management teams. This is what I did at Rompetrol and it is a principle I have applied to all my other businesses." Each time, Patriciu has incentivised and motivated his management teams for the long term.

Today, Patriciu is focusing efforts on certain areas of business development: real estate, alternative energy, banking and media and communications. He believes the diversified portfolio approach will allow him to build long-term opportunities that will deliver positive growth for DPH after the downturn.

Growth can be achieved in any climate.

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MARK OKES-VOYSEY

The new normality

The region's businesses have used the downturn to get healthy – now they are in a better position to grasp the growth opportunities 2010 will present

At least the lounges in the region's airports are once again filling up with owners and executives. Some of the regular faces who charged around the region in better times have been replaced by a different set of people, emerging from this financial crisis, seeking a new generation of opportunities.

The questions on everyone's lips are: have their operations restructured enough to take advantage of the green shoots and will the trickle of deals increase exponentially in 2010?

Piloting businesses when there is so little visibility makes for a particularly challenging journey. Owners and executives are working harder than ever to navigate the global downturn. In our own region, it is inspiring to see the number of leaders who demonstrate deep wells of resilience and determination to ensure their firms emerge in as fit a state as possible to take advantage of any opportunities that 2010 may present.

The best ones have completed their restructuring programmes and have strong, sustainable business platforms. They are now investing additional time and energy in opportunities internationally, not just in the West, but also further east and south into India, China and parts of Africa.

Everyone accepts the potential for China to dominate the business agenda during the second decade of the 21st century so executives from CEE are spending ever larger quantities of time there to examine the angles for their operations. For some it is about reviewing their supply chain, for others it is a sourcing story and for many others it comes down to exploring potential new markets.

PHOTOLIBRARY

As a consequence of the financial meltdown, leaders and executives have reviewed and are reviewing operations – with an open mind – and re-examining new ways of working. Armed with underlying data and fresh perspectives from restructuring experts, leaders are able to start conversations with “I know” rather than “I think”, ahead of taking the difficult cost-cutting decisions that have been so important to ensure survival.

Other themes need addressing. What impact will a fluctuating oil price have in 2010? And when should leaders put mergers and acquisitions back on the agenda? Vendors of good businesses have become much more realistic about their pricing expectations and those who are not running sound operations are looking for safe harbours in these tempestuous times.



“In the new normality, businesses have learned to live with uncertainty”

2010 should be a better year than the past 12 months. A new normality has emerged in which businesses have learned to live with uncertainty. Finance functions have had to become stronger and more rigorous and this enables businesses to make better decisions about how they seize upon the opportunities for different types of growth in times to come.

The key watchwords of today are conservative, caution and diligence as leaders consider their moves carefully. There will be no shortage of opportunities in 2010, and there may even be a mini mergers and acquisitions boom in our region as activity levels grow, led by those willing to seize the moment. ■

Mark Okes-Voysey is managing partner of PwC's advisory practice in CEE.

Reeling off the names of homegrown entrepreneurs is a tough ask in a country such as the Czech Republic. Petra Kursova, secretary general of the Czech Venture Capital Association, struggles to come up with even a handful. Petr Kellner, the legendary investor valued by Forbes at \$6bn, easily springs to mind, but beyond that, she just about recalls a company that makes hospital beds, a software firm called Unicorn and Unimex, a travel conglomerate. Czech entrepreneurs aren't celebrities, she explains. Apart from Kellner, they are unknown by the public.

"If you want to know the Czech words for venture capital and angel investors I can't tell you as we don't have them. We use the words in English. There is no direct translation. It is so new for Czech people," Kursova says. So new, in fact, that young Czechs rarely want to be entrepreneurs. "After 1989, the first wave of development was driven by large foreign firms which came here to take advantage of a skilled workforce prepared to work for low wages," says Prague-based Steef Klop of PwC. "Firms like Bosch came to the Czech

Republic and employed 6,000 people. It was good for the country. But it meant that young people preferred a career path with these employers to becoming an entrepreneur. It is still true that in Prague the goal of bright young people is to work for a multinational. If you want to find entrepreneurs you have to look to the regions, to Ostrava and Brno."

Klop says that even if Czechs want to start a business, they will find it hard. "The availability of finance is on the lowest level there could be, seriously terrible," he says. "If you ask Czech business owners about their biggest concern, the first thing they say is that there is no access to money. Banks are reluctant to lend – even more so during the current crisis. There is very little venture capital and scarcely any funding for early-stage firms. The only way to finance a business is to look to your inner circle of family and friends."

And yet there are entrepreneurs in the Czech Republic. In fact, across CEE, against the odds, quietly, entrepreneurs are flourishing. They rarely get their stories published. Like an underground movement, they meet in cafes and on social networking sites to discuss ideas.

SPREADING THE SPIRIT

CEE is not a region renowned for entrepreneurship. But talented networks of individuals – and one trailblazing Baltic state – are bringing it into the mainstream

WORDS: CHARLES ORTON-JONES

"The Czech market alone is too small for us. We are more ambitious than that"

MICHAL BLAHA, ONTHEROAD



Michal Blaha

OnTheRoad, Czech Republic

Czech entrepreneur Michal Blaha's record shows why he commands respect among younger compatriots eager to break into business. He founded his first company, an internet consultancy, in 1995 while still at university. His next venture was a search engine and portal called Atlas, which is still the second biggest in the Czech Republic. Blaha sold it to Warburg Pincus for \$15m in 2008. He has also founded a Netflix-style DVD rental service and a mobile marketing agency. Currently, he runs OnTheRoad, a social networking dotcom based in Prague.

Blaha openly admits that it is not easy to be an entrepreneur in the Czech Republic: "The government doesn't care about us. They only think about multinationals as they have more money. It isn't easy to set up a company. To be honest, things are getting worse and worse."

Czechs still lack enthusiasm for running their own business, he says. "They lack courage. Most are afraid of what they might lose. Maybe it is a little different in the internet sector, as start-up costs are so low, you can start a company in your spare time at the weekend."

Despite all the difficulties, Blaha says there is a growing entrepreneurial scene. "Prague is small so we all know each other," he explains. "I think there are 200 entrepreneurs in the internet sector here, of which perhaps 50 are successful. There is a social life for us. Events are hosted by First Tuesday [a networking forum for technology entrepreneurs]. They used to be once a month. Now they put on meetings and conferences three times a week."

Blaha, for one, is making huge strides. OnTheRoad is only nine months old and already has 15,000 users. Travellers post itineraries, videos and diaries. The site has been localised into English, German and Czech, and Blaha says Japanese, French and Spanish versions are just around the corner. "We would like half a million users in two years," he says. He has a marketing director based in Seattle to address the international market. "The Czech market alone is too small for us. We are more ambitious than that."

PORTRAIT: VOJTECH VIK

Joakim Helenius

Trigon Capital, Estonia

For the most convincing testimony of Estonia's hunger for business, meet Joakim Helenius. He is the region's foremost financial entrepreneur, having founded Trigon Capital, the biggest merchant bank in the Baltics. A Finn by birth, Helenius toured the world with his diplomat father as a child, attended Cambridge University and then headed off to Wall Street. In 1992 he founded Trigon Capital. Today, Trigon boasts offices in eight cities in Eastern Europe and one in Almaty, Kazakhstan. It has a fund management division with \$1bn in assets, a real estate arm, provides the full suite of corporate finance services and has major agricultural holdings. Helenius owns 56%.

Helenius runs his empire from Estonia and is a convincing spokesman for the country. "Estonia is a great success story," he says. "Even with the fall in GDP of 16% this year, it has managed to grow at a long-term average of 5%. That's remarkable. And as Estonia has no significant external debt, it can incentivise entrepreneurs and investors through the tax system. It will be the superstar of the recovery. Everyone is distracted by the bad headlines of falling GDP, and they have missed what a fantastic story Estonia is."

There is an international perspective, he says, which distinguishes the national outlook. The infrastructure is superb, he adds. "Estonia has everything it needs to be an economic success. Shipping is easy as Tallinn is a major harbour. The railways are the same gauge as Russia, so goods can be shipped East without unloading from one train to another." The tax regime is particularly attractive. "Political decisions relating to tax have been very business friendly," he says.

Helenius forecasts the fast-growth sector will be manufacturing. "Swedish and Finnish manufacturers want to outsource locally. They outsourced to China, and this overstretched their global supply chain. Estonia is in the perfect position to offer outsourced manufacturing services to these firms. We will see significant reindustrialisation over the next five to 10 years. Trigon is positioning itself for this." In fact, we should expect Estonian success stories in all sectors, he believes. "Estonian entrepreneurs are optimists. They are certain they can achieve great things. The potential is so great."

PORTRAIT: TIIT VEERMÄE



"Estonia can incentivise investors through the tax system. It will be the superstar of the recovery"

JOAKIM HELENIUS, TRIGON CAPITAL

Michal Blaha is one such trailblazer. A serial entrepreneur, he runs OnTheRoad, a social networking dotcom based in Prague. He is well known on the Czech entrepreneurial scene and is regarded as a mentor to eager young Czechs. "When they need advice, they ask me. I'm meeting another entrepreneur on Monday," he says. "He asked me for a chat so we are going for a beer. That's how we do things in Prague." (See case study on p.27.)

NO MONEY

Blaha and his fellow entrepreneurs are proving that, although life may be tough in the Czech Republic, it is possible to thrive. But why is it so hard? The reason is lack of cash. European Venture Capital Association statistics show the scale of the problem. Early-stage capital invested across CEE in 2008 was €53m. By contrast, the UK alone invested more than seven times this amount in early-stage firms. Seed funding – essential for identifying commercial opportunities – is scarcely detectable (see table, right). Only Poland reported investment at the seed level – €3m-worth.

Lack of money is crippling the emergence of entrepreneurs. In Latvia, the impact is clear. For example, at the country's highly respected Institute of Organic Synthesis, Professor Ivars Kalvins is the author of a long list of valuable patents. But he is unable to develop them himself. Instead, they are sold to multinationals that commercialise them. At Connect Latvia, the organisation tasked with helping Latvian entrepreneurs develop their ideas, there is frustration about this situation. Connect Latvia manager Elmars Baltins says: "Talented researchers like Professor Kalvins are forced to outsource their knowledge, giving away the work of their brains to international companies. We don't have funding in Latvia to help potential entrepreneurs like Professor Kalvins to develop their

research. It is not a good situation."

Worse, the lack of support for potential entrepreneurs such as Professor Kalvins means that Latvia is failing to create role models for young people. Baltins says: "We have no famous entrepreneurs. Even the word is a problem. Under socialism, the only word we had was 'businessman', which was not a desirable word. It was like being called a 'speculator'. Today many people have the same negative attitude."

Baltins is working to change this situation by introducing established entrepreneurs to those just starting out. He can call on a few top-class names such as Normunds Bergs, the founder of microwave radio manufacturer SAF Tehnika, a man Baltins lightheartedly calls the "Donald Trump of Latvia". Ilmars Osmanis, founder of Hanzas Elektronika, is another and Peteris Rucevskis, founder of optical researcher Algorego, is a third. These men offer inspiration and advice to young entrepreneurs. No matter how bad the economy and how tight the finance, they prove it is possible to build fast-growth companies in Latvia.

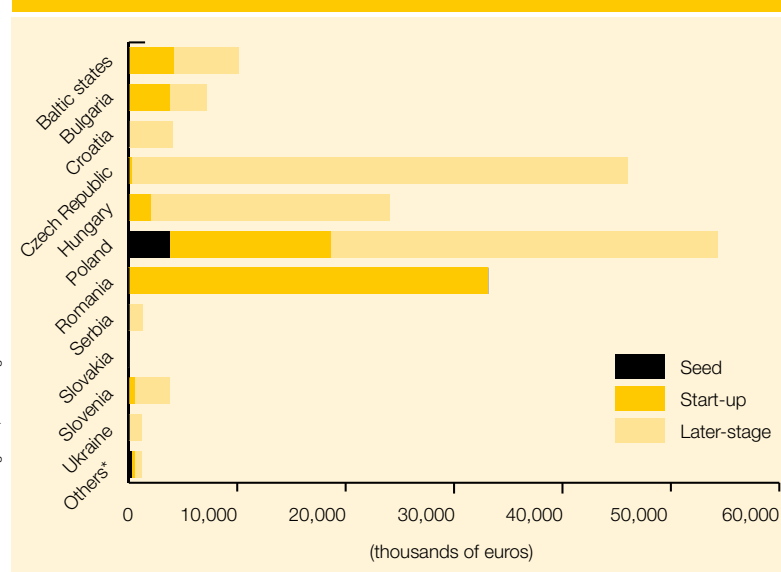
THE ESTONIAN MIRACLE

Other CEE nations have similar stories. Some, such as Lithuania and Romania, are behind the average. Poland offers a more favourable environment for entrepreneurs. But only one country can genuinely be considered an exception – Estonia.

The list of Estonian entrepreneurs is long and distinguished. There is Toomas Annus, founder of construction company Merko. Annus founded Merko in 1990 and is now one of the richest men in Estonia. There is real estate developer Margus Reinsalu; hotelier Toonart Raask; the architect of Hansabank's extraordinary rise, Indrek Neivelt; computer builder and investor Allan Martinson; and casino operator Armin Karu, who starred in Estonia's version of *The Apprentice*. Below the super-rich level, there is a rich vein of less well-known names, focused strongly in the software and mobile telecoms sector.

Why is there a peculiar abundance of Estonian entrepreneurs? Proximity to its cultural sister, Finland, is one reason.

VENTURE CAPITAL INVESTED IN CEE IN 2008



* Bosnia and Herzegovina, Montenegro and Macedonia

Source: EVCA Central and Eastern Europe Statistics 2008

Finland's influence on modes of thinking, and its role as Estonia's biggest trade partner, have helped the latter to leap ahead. There is also a political reason: low tax and an entrepreneur-friendly government have been important. The third and crucial reason is Skype.

Estonian programmers wrote the software behind Skype. As the firm grew, programmers dominated the top management positions. When Skype was sold to eBay for \$2bn, share options resulted in a windfall for Estonian Skypers, which is now working as rocket fuel for the economy.

Toivo Annus, Priit Kasesalu, Ahti Heinla and Jaan Tallinn – four Estonians who were with Skype from the start – are using the money from the sale to invest in Estonian start-ups. Their vehicle, Ambient Sound Investments, is providing seed capital and early-stage capital where very little existed before.

Margus Uudam is Ambient's head of private equity. He has €100m to invest and is finding no shortage of start-ups to back. "We have such a strong interest in technology in Estonia. We are providing the money and knowledge to commercialise this expertise." Ambient is prepared to back any business, as long as it has good technology at its core. In its portfolio of 30 firms, it has United Cats and Dogs, a social networking site for pet owners; Oskando, which builds GPS devices for logistics firms; Modesat, an industrial-grade modem manufacturer; and a string of biotech firms. It's a diverse list, showcasing the best Estonia has to offer.

"Skype is doing to Estonia what Nokia did for Finland," explains Uudam. "In Finland, you find that one in three entrepreneurs has a Nokia background, and the money used to back start-ups was created by Nokia. Here we have Skype. And Skype did something else for us. It showed us the scale of our ambition. Skype was a global business. It showed Estonians

that we need to think globally." Uudam recognises that Estonian inventors don't always have the experience to head up a fast-growth company. "We have the attitude that technical people are best at focusing on technical issues, so we bring in external managers. Estonia is a tiny market, just 1.5 million people, so we need to think internationally. This is why we often recruit foreign CEOs. Having an American CEO means the start-up will have an international outlook."

To date, Ambient has invested €15m. "We aren't running out of money," says Uudam. He emphasises that he is open to proposals from anywhere. "No one and no country are excluded." Entrepreneurs from cash-starved neighbours take note.

At PwC Estonia, Teet Tender says he supports the view that Estonia can produce a plethora of great businesses. But, he warns, they will need strong professional support. "Estonian entrepreneurs are too shy to ask for help," he observes. "There is just no culture of consultants there. They want to find solutions on their own. Often they turn to professionals for advice when it is already too late. I would like to see Estonia improve its structure of administrators and business help."

He says that, with the right support, Estonia's entrepreneurs can be the engine of prosperity. "When you don't have natural resources like oil and gas, you need entrepreneurs all the more. Small businesses are what drive the economy. In Estonia I see young people who want to study business. They understand entrepreneurship."

Even better, Estonia can provide a model for other CEE nations on how to encourage entrepreneurship. ■

Charles Orton-Jones is a freelance business journalist, specialising in entrepreneurship and small businesses.

Lars Mach

Goliath, Estonia

Where would a German entrepreneur with British technology found his business? Lars Mach chose Tartu, Estonia's second city. "I came here 10 years ago to work for a UN wind power project," he says. "I was attracted by the international outlook of Estonia, which is similar to Scandinavia, and the lack of corruption. The people have such an interest in technology. You find pensioners using their mobile phones to make payments and they use the internet to file tax returns. When I go to Germany, the stuff they think is innovative seems old to me because I live in Estonia. It's such an exciting country."

Mach is the tycoon behind Goliath, a wind turbine manufacturer that claims to be able to produce ultra-light and gearboxless turbines. The technology is the brainchild of Professor Ed Spooner of the University of Durham in the UK. The plan is to research, design and build the turbines in Estonia. "Our long-term plan is to own a production line here," says Mach. "At the moment we are building a demonstration machine. It is being assembled right now, and we can start to run tests. At first the manufacturing will be outsourced. Wind turbines aren't the sort of thing you can build in China. They are too big and cost too much to ship. Being in Estonia means we are close to our target markets."

Mach even found finance in Estonia: "I went all over the world looking for investors. I went to North America and across Europe. In the end, we found investors at home." The Estonian Development Fund, a national venture capital fund, bought 21% of Goliath for €250,000m. The co-investor was PowerDrive, which took an equal stake for the same sum.

Mach urges fledgling entrepreneurs to consider relocating to Estonia to take advantage of low tax, low overheads and the abundance of low-cost, high-quality labour. "Salaries here are very attractive," he says. "There is a strong tradition of technical excellence, so you can hire great people. And Estonia really wants to attract entrepreneurs who add value in industries like manufacturing. If you come here, you will discover a lot of open doors."

"I went all over the world looking for investors. In the end, we found them at home"

LARS MACH, GOLIATH





HIGH FLYERS

Europe is in need of active investors. Could a team from Slovakia be the answer?

WORDS: KIMBERLY ROMAINE

Rewind five years and few would have guessed that Slovakia would be the first new European Union (EU) member state to adopt the euro. In fact, few would have guessed that this small, young country would even have joined the EU.

Yet Slovakia, which only gained independence in 1993 following the dissolution of Czechoslovakia, tends to be full of surprises. Three years ago, it achieved the highest sustained growth rate in the EU – an impressive 10.4%. The story of Slovakia's growth is one of perseverance and, at times, of overcoming adversity.

It was out of this country and against this backdrop that Penta Investments developed – and its successes can be compared to those achieved by its home nation.

Founded as a securities trader in 1994, Penta has grown to become one of CEE's most prolific private

equity investors. It is run by a team of five partners – Marek Dospiva, Jaroslav Hascak, Martin Kusik, Jozef Oravkin and Jozef Spirko.

The firm has clocked up 44 investments over its 16-year history, and manages €2.3bn of assets. Nearly half – 20 – of the private equity deals have been realised, generating an average internal rate of return of 50% – well above the 20% average most fund managers achieve in Western Europe.

THE RIGHT ENVIRONMENT

"We are very entrepreneurial and would like to remain that way," says Hascak. "The way we invest creates a highly competitive environment inside the businesses we back. We also aim to encourage knowledge sharing within our organisation, for example through new information systems or strong back-office teams. This provides a balancing force with

the 'aggressive' and competitive investment professionals."

Much of Penta's success is down to its hands-on approach to investment management. "Penta has largely invested in non-cyclical industries, so its portfolio is in very good shape," says Miroslav Bratrych, partner at PwC in Prague. "They are very active in improving profitability in the businesses they back. They improve both their own infrastructure and that of the portfolio companies."

In 2006, Penta made a tidy profit on its investment in Severomoravske vodovody a kanalizace Ostrava (SmVaK), Moravia's largest water company. SmVaK's value increased shortly after Penta took the helm. "We are strongly engaged on a day-to-day basis with our acquisitions, particularly in the first 100 days," Hascak says. As a result of its active ownership, Penta sold SmVaK just two years after its investment to a Spanish trade buyer

THE PARTNERS



Marek Dospiva

Dospiva manages and develops a portfolio of private equity investments in utilities, aerospace and retail, as well as real estate projects. He is currently overseeing the business development of Aero Vodochody, and the expansion of Zabka, originally a Polish retail chain, to other CEE markets.

Hascak is managing partner in Penta's private equity division, and is currently overseeing the firm's healthcare and energy investments, such as Dovera, the biggest private health insurer in Slovakia, and the energy holding group, PPC Energy Group. He has been involved with most of Penta's significant investments.



Jaroslav Hascak



Martin Kusik

Kusik is responsible for several investments in telecommunications, entertainment and retail. He is currently overseeing the expansion and business development of the largest CEE sport betting chain, Fortuna Group, the start-up telco operator in the Czech Republic, MobilKom/U:fon and Stream in Poland.

Oravkin is managing partner in Penta's real estate division, and he is also active in private equity investments. He specialises in private banking, the metal industry and transport. He is currently overseeing the development of Privatbanka and the exit from aluminium foundries, Svalco and ZSNP.



Jozef Oravkin



Jozef Spirko

Spirko is responsible for investments in manufacturing, the metal industry and food processing. He is currently managing the consolidation and restructuring of Penta's meat processing holding, Carnibona, including the Debrecen and Mecom Groups. He was involved in the restructuring of ZSNP.

for €190m – netting a tidy profit of €175m (see box on p.35).

Attaining majority stakes in the businesses Penta backs is crucial to enabling this active ownership and resultant high returns.

“After securing control, we have a very clear corporate governance structure, drawing boundaries between the actions of Penta, the project team and the company's management,” says Hascak.

Last year, the firm gained majority control over Slovak health insurance company Apollo, in which it already had a significant minority stake. At the beginning of the year, Apollo merged with complementary player Dovera zdravotna poisťovna (Dovera), another Penta portfolio company, creating a giant with 1.5 million customers.

TIMING ISN'T EVERYTHING

The profit Penta turned on the SmVaK deal in just two years may have increased its internal rate of return, but it is unusual for the investor to offload an asset that quickly.

That is because a major factor differentiating Penta from other private equity investors is its funding structure: Penta's five partners each invest in the business, instead of third-party money being committed by institutional investors from around the world, as most private equity firms are funded. This evergreen nature of its capital base means it is free from the shackles of an institutional investor base, which tends to exert pressure to deploy and return capital quickly instead of waiting for optimal timing.

“Though this issue of funding has often been brought up, we believe that having this structure gives us a lot of freedom in our operations and decision-making,” says Hascak. “We are not forced to exit from our investment if the conditions are not favourable as the investment horizon is

not limited and managed by the rules of fundraising,” he explains.

That said, Penta has so far very cleverly timed most of its investments, achieving hold periods on a par with buyout houses that rely on third-party funding. But Hascak admits: “Having only our own evergreen fund does mean we are more limited in capital resources, which remains a constant challenge for our organisation.”

BEYOND CEE

The strategy may be unusual, but it clearly works. Having conquered Slovakia – Penta is one of the country's largest employers, with portfolio companies comprising 25,000 jobs – the firm set its sights further afield. It first expanded at the millennium, when it branched out into neighbouring Czech Republic. Today it has offices in Moscow and Warsaw as well. It is now looking to the West: Penta aims to be a top mid-market investor in Europe by 2013, upping its target deal size to €100m-€250m. The firm also aims to double its equity to €3bn by 2012.

While any expansion involves challenges, Penta is better placed than most to overcome them. “Normally, access to capital is a difficulty, but Penta is very liquid, meaning it is better placed to take advantage of opportunities as they arise in today's market of depressed valuations,” says Bratrych.

The investment strategy will also prove beneficial, particularly when entering markets that have been burned by short-termism. “Penta acts as a cross between a strategic and financial buyer. It is very hands-on, similar to a strategic player; however, it has also proved it is very capable of exiting businesses profitably, like financial buyers,” says Bratrych.

Free from the constraints of third parties holding the purse strings, and



“Penta acts as a cross between a strategic and financial buyer”

MIROSLAV BRATRYCH, PwC, CZECH REPUBLIC

TURNING WATER INTO WINE

Penta's track record in owning businesses is impressive. The firm made a tidy profit on its investment in SmVaK, Moravia's largest water company, in 2006. Attracted by the stable cash flows a leading utility can provide, Penta launched a bid to buy the business from AWG, SmVaK's majority owner since 1999. AWG agreed the sale and further shares were acquired from minority owner Ondo, ultimately giving Penta 98.5% ownership. The value of the business increased shortly after Penta took the helm, as the backer introduced debt to the capital structure, with Citibank leading a bank syndicate to provide a €70m loan.

A year after taking ownership of SmVaK, Penta worked with Citibank to lead a formal refinancing, consisting of 10-year bonds worth €80m. The move helped relieve SmVaK of cash constraints by deferring repayment of the principal on the loans. Additionally, the private equity firm extracted €8m by selling off non-core assets. Overall, Penta helped the company to increase its margins by 10% annually in the first two years of Penta's stewardship.

During this time, international interest in infrastructure assets was skyrocketing, with most institutions launching dedicated funds and prolific buyout investor Guy Hands publicly predicting: “By 2008, all the water companies in Britain will be owned by private equity.” In response, the price of infrastructure assets ballooned – great news for anyone already holding them. As a result of the clever timing of Penta's investment, and its active ownership, Penta sold SmVaK just two years after its investment for a €175m profit.

as seasoned hands-on investors, Penta is well placed to export its expertise beyond CEE. “We are in the process of transforming from a local player to international,” Hascak says. “Our mid-term goal is to expand our activities outside the Central and Eastern European region and thus to be one of the most significant investment groups in the mid-sized

market in Europe.” Years ago, there may have been doubts that a five-strong team from a nascent country could achieve such status, but if it continues along its impressive growth trajectory, and that of its home country, it may just be conceivable. ■

Kimberly Romaine is editor-in-chief of unquote”.

Falling into place

Industry consolidation in CEE is set to continue apace. To deliver real value, deal-makers will have to do more than the traditional transactional due diligence

WORDS: LEV HOLUBEC

CEE CONSOLIDATES

Markets in Russia, Ukraine and other emerging CIS countries can expect to see robust trends of consolidation over the next three to four years. The main driver of consolidation is the heavily fragmented state of markets in the provinces, which are serviced by a large base of companies that often lack scale. Consolidation will occur not just within the provinces of these countries but also cross-border, both within CIS and CEE. This applies to banks, private healthcare, retail and telecoms. With increased regulation and capital requirements, the banking sector will consolidate by itself, particularly in Russia, where as many as half of existing banks will face closure or takeover as they may not be able to strengthen their balance sheets sufficiently.

Opportunity knocks when an industry consolidates. No question about it. Unite a number of smaller, independent entities from a fragmented industry and the result promises big returns through economy of scale, greater geographic reach and a much more formidable competitor. Scale and reach offer the consolidated entity the opportunity to provide higher value through broader service and product offerings.

A number of consolidations have created tremendous size, efficiency and market value over the past century. Affected industries range from telecoms, banking and paper through to office supplies and funeral services.

Sadly for some, however, consolidations do not always realise the full potential their promoters and managers predict. In some instances, a poorly formulated execution plan is the culprit, in others the plan's execution falls short. In still others, shoddy transitions leave customers, suppliers and employees wondering what will happen to them. They leave, fearing the worst.

Today, more and more companies in fragmented, converging industries are under competitive pressure, requiring them to quickly transform into more efficient and broader-service enterprises, often across country borders, just to remain solvent.

The first global economic crisis of the 21st century exacerbates the need to transform for solvency. The combination of difficult economic conditions, required speed of transition and radical change has made consolidation more complex than ever. To meet the challenge, companies need to attract strong

management and implement strategic and operational changes to adequately reinvent themselves. This requires capital that, when available, is often beyond the reach of individual companies. The only viable solution is to build a value proposition with other players in the industry and to find funding together, based on the value to be delivered through their consolidation hypothesis.

Thus, with the promise of quickly generating and delivering significant deal value as the basis for the consolidating deal(s), the heat has been turned up on managers of new consolidations to meet or exceed performance projections.

EXCEEDING EXPECTATIONS

Unfortunately, those managers – coming as they often do from the different, smaller and single territory companies being rolled up – seldom have the experience, desire and resources to achieve what they are being asked. The challenge is exacerbated by the unfamiliar scale of the new company, making the transition tough for even the most experienced managers.

They need to focus on the new company's critical success factors, have change management experience to integrate the disparate parts and form a new, smoothly functioning team. They must also be free to take critical, rock-the-boat actions, which are often both difficult and unpopular.

Successfully combining an industry consolidation (or “roll-up”) is a lot like undertaking a major change initiative at a large corporation. It has all the same ingredients: people, information, culture, processes, technology, and more.

SYNERGIES IN TELECOMS

When a top national mobile operator wanted to buy a leading broadband provider to gain access to the broadband and associated services market on a nationwide scale, it asked PwC to perform financial, tax and commercial due diligence. PwC was also asked to assist in a review of the synergies between the buyer and the target.

PwC provided a detailed analysis of the target's projections for its individual businesses and customer segments; analysed and quantified potential upsides and downsides to the projections; reviewed the synergy plans and advised on size and timing. As a result, the buyer was able to include synergies in its valuation.

The bad news is that more than half of major change initiatives fail in organisations that are in a “steady state” – a state more placid and predictable than a roll-up. The failures are often due to employees' resistance to change, reinforced by management's lack of communication, vision and commitment to the change.

The numbers get worse with a single acquisition – the simplest form of M&A. In these circumstances, management needs to fully understand, embrace and communicate the scope of the change, from a strategic to a task level, to ensure that the resources of the stakeholders are used efficiently to effectively facilitate their objectives.

Since simple, steady-state change initiatives are more likely to succeed than merger-related change, it is logical to assume that consolidations – the combining of several unrelated entities – have an even lower rate of

would mitigate some of the problems with consolidations. But it usually is not designed to deal with integration. It is not about the entire deal – from concept to post-roll-up integration – but about the narrower business of getting the deal done.

Transactional due diligence focuses on assessing the integrity and quality of financial and operating information for each target company, as well as other factors impacting valuation risk and structure. The “traditional”

“Speed of transition and radical change made consolidation more complex”

success. A roll-up, by nature, must coordinate multiple companies with different cultures, value systems, management styles, processes and technologies. The factors that make steady-state change and one-company acquisitions difficult are even more of a challenge in roll-ups.

You might think that traditional transactional due diligence alone

objective of this evaluation phase is to learn enough about the target companies to make a ‘go’ or ‘no-go’ decision. If the decision is to ‘go’, the objective is also to nail the right price and structure.

When the evaluation phase is limited to such transactional due diligence, when no other plans to address integration issues are in place – as is often the case with consolidations – managers of newly rolled-up companies immediately find themselves focused only on fighting fires. It is not pretty and it is frequently fatal. They do not spend time developing, scrutinising or challenging

the value of the consolidation, developing a plan to capitalise on it, much less figuring out how to manage the change in the newly created entity.

A STEP FURTHER

The answer is to look beyond transactional due diligence to the entire deal, to take a holistic view to ensure the deal succeeds. That means more detailed analysis of the specific synergies before the deal closes. It

means focusing on pre-closing and post-closing risk. It means stabilising initial business operations and building the business foundation of the new company so that it can realise its promised value as soon as possible. It means tidying up the reporting processes of all parties involved immediately upon the deal closing.

PwC refers to this process of planning and execution as operational due diligence (ODD). ODD provides the buyer with a detailed and structured cross-company approach for timely follow-up of risks and opportunities. Some of those key matters to consider are identified through traditional transactional due diligence, others are discovered as a result of ODD work.

It is worth repeating: opportunity knocks when an industry consolidates. Yet history has a way of repeating itself and too many times consolidations have not delivered on the promise of expected big returns. The market has become wiser and now requires that consolidations demonstrate they can consistently create value in a controlled manner.

The good news is that with the right approach, many, many more consolidations can meet their objective of industry transformation and create high value in the process. It requires detailed integration plans, complemented by actions and resources to execute those plans intelligently, to stabilise operations and drive value. For the much higher odds of success, it is worth it. ■

Lev Holubec is a partner in PwC's advisory practice in Ukraine.

OPERATIONAL DUE DILIGENCE: WHAT IS KEY?

- Establishing a financial reporting structure for the short term and identifying a desired structure for the longer term.
- Assisting management in developing processes to accurately forecast and budget consolidated revenues, earnings and cash flow.
- Closing the books in a coordinated, timely manner.
- Measuring and developing processes to manage working capital.
- Aligning and/or understanding the implications of costing and pricing procedures.
- Identifying, communicating and preparing information-system capacity and capital requirements.
- Identifying key employees and key accounts and developing retention plans.
- Identifying and managing human resource matters, including salaries, severance and benefits.
- Navigating through legal and structural pitfalls such as compliance with purchase agreements post-closing.
- Building a corporate governance and management structure.
- Communicating across organisational boundaries.
- Building the desired management skill set.



THE GREEN LEAP FORWARD

Climate change concerns may not be top of CEE's agenda, but the more pressing issue of national energy security will force it to deliver on green fuel

WORDS: SCOTT PAYTON

Billed by political pundits as the most important international summit in the history of mankind, December's United Nations Climate Change Conference in Copenhagen – also known as “COP15” – was tasked with no less than heading off an environmental catastrophe. The majority of the 193 nations around the table wanted to walk away with a legally binding roadmap for global greenhouse gas emissions reductions between 2012 and 2050 – with interim targets for 2020.

COP15 was crucial in fighting the environmental and socioeconomic effects of climate change because the existing global agreement, the Kyoto Protocol, expires in 2012.

In the end, for many the summit ended with a whimper rather than a bang. Behind closed doors, the leaders of the US, China, India, Brazil and South Africa negotiated the Copenhagen Accord – a commitment “to reduce global emissions so as to hold the increase in global temperature below 2°C” and to achieve the “peaking of global and national emissions as soon as possible”.

While the Accord finally unites the US and China on climate change – something the Kyoto Protocol failed to do – it is not legally binding and is vague on how it will achieve its goals. The summit closed with a “recognition” of the Accord rather than an approval, which would have required unanimous support. UN Secretary General Ban Ki-moon has called for the Accord to be turned into a legally binding treaty this year, although there is no provision for this in the existing deal.

GREEN DRIVERS

Even if COP15 only went some way to achieving a legally binding agreement, CEE governments and companies face a future in which climate change is higher up the commercial and sociopolitical agenda than ever before. How ready are they?

Burak Dalgin, vice president for Europe at Darby Overseas Investments, says that green innovation in CEE has lagged behind other parts of Europe and the US. “The first reason is the proximity of natural gas and the ability to dig cheap coal in the region,” he says. Second, in the post-Soviet era, economic growth has been the number one goal. “Only after joining the EU, or hitting certain income levels, are these countries prioritising environmental issues,” Dalgin explains.

Irena Pichola, sustainable business solutions practice leader at PwC Poland, says that this has certainly been the case in her country: “The environmental challenge in Poland lies mainly in the characteristics of the energy industry, which is heavily dependent on coal generation, given the abundant supplies of this fossil fuel in the country. This, combined with the steady growth of the economy, positions Poland on a challenging road with regard to addressing climate change.”

Despite this, Poland and other CEE countries have started to make progress along the road to a lower carbon world. The EU's “20-20-20” targets are a key driver. These oblige member states to reduce greenhouse gas emissions by 20% of 1990 levels; increase renewable energy generation by 20%; and cut energy consumption by 20% by 2020. The European Bank for Reconstruction and Development (EBRD) is also driving eco-innovation through its Renewable Development Initiative.

However, Clifford Aron, principal of GreenMax Capital Advisors, an energy and environmental finance expert, believes that CEE governments' direct support for renewable energy is being driven primarily by national energy security needs, rather than international climate change policies. “While the EU legislative framework provides the overall impetus for growth in the introduction of renewable energies, the enthusiasm with which each country pursues policies at the national level, which actually

implement EU directives effectively, depends upon national leaders' perceptions of energy threats overall," he says. "Green for green's sake isn't enough." Aron cites Poland as an example. "For years, there was a lag in companies' ability to get renewable energy projects permitted and interconnected. Then, around the middle of 2007, the Polish government realised that it was facing a substantial shortfall in energy capacity. Suddenly, wind energy looked like a very attractive solution for meeting growth in energy demand."

Concerns about energy security also dictate the uptake of green energy initiatives in other CEE countries. Romania lags



"Ukraine has the most attractive green tariff of all of Europe. Energy diversification is a clear energy security issue"

CLIFFORD ARON, GREENMAX CAPITAL ADVISORS

CLEAN CATALYST

PwC is acting as an adviser on climate change mitigation activity across the CEE region, while practising what it preaches in its own operations, says Douglas Grier, a manager in the sustainability and climate change practice at PwC Russia. "We are actively working at reducing our own CO₂ footprint through a range of initiatives and measuring all of our emissions in order to gauge our emissions-reduction performance with a plan to set further reduction targets once our baseline has been set," he explains. "All this allows us to set an example for other organisations and shows it makes good business sense."

In several key regions around the world, PwC is also supporting the Carbon Disclosure Project (www.cdproject.net), a global initiative representing more than 475 investors designed to collate data on the carbon emissions of the world's major companies. Grier says: "I'm working on the first stand-alone Russian Carbon Disclosure Project

report right now. We have seven Russian survey respondents this year, which is up from zero last year."

He and his colleagues are also participating in a joint initiative by the Confederation of British Industry (CBI) and the Russian Union of Industrialists and Entrepreneurs (RSPP), focused on sharing expertise regarding energy efficiency and climate change mitigation activity between Russia and the UK.

In addition, PwC is advising Russian airlines on their compliance requirements under the European Union's Emissions Trading System. "It is crucial for airlines to address this issue if they are to retain their licence to operate within the EU," says Grier. "We can help companies to develop their strategy, their reporting systems, and to ensure that they comply with all aspects of EU legislation regarding emissions."

The UN's Climate Change Conference has raised awareness of environmental issues across CEE. "It has highlighted many of the opportunities that the climate change agenda presents to CEE companies, as well as the challenges," says Grier.

Read best practice guidelines on greenhouse gas reporting for companies at www.corporatereporting.com

behind many of its neighbours in wind energy development, even though it has "the second best wind resources in the region" because it does not suffer from a "thirst for energy", Aron says. In contrast, in recent years the Turkish government has created a regulatory environment more conducive to the rollout of new wind projects than that of Romania.

In Ukraine, policymakers have created "the most attractive green tariff in all of Europe", says Aron – this time in response to fears about rising gas prices. "Energy diversification is a clear energy security issue for Ukraine," he says. Dalgin agrees that energy security is the primary driver of green projects in CEE, adding that it is becoming a more powerful driver than ever. "Most CEE states are reliant on one or two producers of natural gas. So they want to diversify their energy sources – and renewable energy is an obvious alternative."

CEE countries' appetite for green innovation may have grown recently, but the global financial crisis has slowed the implementation of many renewable energy projects. "Only the premium renewable energy sites look attractive today," says Aron. Budget deficits resulting from the financial crisis are the biggest hurdles facing anyone in CEE trying to launch a green project. "Many of these technologies, including solar, are heavily subsidised by the government. So they will always face a trade-off between what makes economic sense for the country in the short term, and what makes strategic sense for the country in the long term," says Dalgin.

ENCOURAGING INNOVATION

Despite these hurdles, Dalgin says that CEE governments can continue to nurture green technologies in three key ways. The first is through 'purchase guarantees' – which oblige grid operators to purchase all renewable energy that domestic firms produce. Second, governments can provide cash subsidies in the form of 'green bonuses' or fixed minimum prices for renewable energy. Third, they can subsidise the domestic development of renewable energy equipment. Are CEE governments doing enough? "In general, I think that things are moving in the right direction," says Dalgin.

Multinational corporations operating in CEE are also



GREEN ENERGY ACROSS CEE

Geography, geology and meteorology play the major roles in determining the green energy potential of different CEE states. "Almost every country has at least one renewable energy advantage, be it biomass, solar, geothermal, wind and so on," says Burak Dalgin, vice president for Europe at Darby Overseas Investments, which has made green technology investments in CEE as well as South Korea, India

and Brazil. "Turkey, for example, is a very nice fit for wind and sun, while certain parts of Poland are very good for wind."

The European Bank for Reconstruction and Development, which runs a renewable development initiative across the CEE region, has conducted an extensive review of renewable energy potential by country. These are the green energy strengths that the bank has identified:



Albania: ☀️	Hungary: 🌿
Armenia: 🌿🌿	Kazakhstan: ☀️🌿🌿🌿🌿
Bosnia/Herzegovina: 🌿	Poland: 🌿🌿
Bulgaria: 🌿🌿🌿🌿	Romania: 🌿🌿🌿
Croatia: 🌿🌿	Russia: 🌿🌿🌿🌿
Czech Republic: 🌿🌿🌿	Slovakia: 🌿🌿🌿
Estonia: 🌿🌿	Slovenia: 🌿
Georgia: 🌿🌿🌿	Ukraine: 🌿🌿🌿🌿
KEY: ☀️ Solar 🌿 Biomass 🌊 Hydro 🌿 Wind ⚡ Geothermal	

pushing in the right direction, adds Agnieszka Rum, sustainable business solutions consultant at PwC Poland. "For example, after meeting energy consumption reduction goals of 10% in the previous two years, pharmaceuticals group GSK is seeking to reduce total energy use by 5% this year, and energy consumption per unit of sales by 45% by the year 2015, while Bel, a French cheese producer, is conducting life cycle assessment (LCA) studies to identify emission reduction opportunities. In conducting assurance of sustainability reports, we at PwC are often requested to verify CO₂ emissions of a given company."




"Reducing emissions for most companies in the region is still a small part of a larger game"

IRENA PICHOLA, PwC, POLAND

that other factors will play a more important role: "Renewable energy development will continue to be driven in emerging market countries by factors other than climate change considerations. Yes, there is legislation, directives and other obligations to meet, but the enthusiasm with which this is done will be down to domestic energy requirements."

Yet Dalgin believes COP15 may have a more direct impact on green innovation and development in CEE. "In general, CEE is lagging behind EU standards in renewable energy. Despite the Copenhagen summit's perceived failings, it will be a good driver to push these countries to make more progress in this area," he says. ■

Scott Payton is a regular contributor to numerous publications including Spectator Business, The Spectator and Financial Management.



What's blowing in the wind?

Most of us know that the world's energy demand is growing at a rate that requires wind, solar, bio-fuels and other alternative energy sources to be included in the fuel mix going forward. Energy and utilities companies are expanding their renewable portfolios and investments in new technologies to reduce carbon, increase efficiency and reduce costs.

PricewaterhouseCoopers advises companies on corporate, investment and emissions trading strategy as well as on the impact of the regulatory environment, government subsidies and incentives and tax regimes. Please contact one of our energy and sustainability leaders today or visit us at www.pwc.com/energy.

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PRICEWATERHOUSECOOPERS 



The future is shared

CEE is fast becoming a choice location for shared service centres. If they are not part of your business strategy, you are not at the races, says Romek Lubaczewski

The past year has been the busiest for a decade in the world of shared service centres (SSCs). Business leaders, initially content to batten down the hatches and weather the worst of the global financial crisis, are beginning to plan for the future again and implement more efficient, and hopefully recession-proof, business models. Unable to squeeze front-end costs any further, companies are now looking for internal solutions in a bid to cut expenditure. As a result, back-office inefficiencies have come under increased scrutiny. The opportunity to reduce costs while improving quality by switching to a shared services strategy is proving too good to miss for many businesses.

SSCs centralise support functions such as finance, IT and HR, which have traditionally been duplicated across the divisions and locations of a single group. Bringing duplicate support services together produces economies of scale that reduce costs and increase efficiency. Centralisation is also seen as the catalyst to standardise and simplify processes, which helps eliminate errors and improve service quality.

Low labour costs and inward investors' increasing confidence in the local talent pool have combined to place CEE at the centre of the boom in shared services. Pan-European companies and global companies with pan-European operations see the region as a prime location

for SSC development. Demand is set to continue to rise as Western multinationals in particular look to the East for value for money. More centres will spring up with ever-diversifying workloads. HR, general administration and specialised services such as insurance claims processing will join more traditional services such as finance and IT as shared services becomes the battleground for differentiation between industry rivals.

However, change programmes on this large scale are rarely plain sailing. Senior management must plan carefully to ensure a seamless transition to an SSC model. Communication is all-important. Job losses are a common consequence of shared service strategies, which makes it crucial that all communication to outgoing staff and the remaining workforce is consistent, open and on message to maintain morale. HR involvement from the start prevents the spread of rumours and ensures messages are communicated at the right time. Geographical relocation can also prove taxing for inexperienced companies. External expertise can help.

Finally, it's important to remember that SSCs are not a strategy in themselves, they are a means to achieving a more fundamental strategy of cost efficiency and improving service quality.

Shared services may not always be the right option for every company but it should at least be a consideration in the strategic planning process because, rest assured, your competitors will be thinking about it too. ■

“Low labour costs and confidence in the talent pool place CEE at the centre of the boom”

Romek Lubaczewski is PwC consulting leader for Poland and the SSC/BPO leader for CEE. For more on SSCs, see p.53

STRESS RELIEF

Struggling under a mountain of distressed debt, lenders in CEE are seeking solutions

Most people cannot think of many similarities between Budapest and Bangkok. Stuart King is not among them. He is a managing director in PwC's Distressed Debt Group, leading the proposition in Europe and Latin America. The team got its start in Asia during the region's financial crisis in the late 1990s. Since then, the group – now also active in Europe, the UK and the Americas – has managed the sale and acquisition of hundreds of portfolios of underperforming and non-performing loans covering all asset classes, as well as equity stakes in financial institutions, allowing lenders to realise value on distressed debt and “non-core” assets. For investors, the team also provides valuation and due diligence services.

Across CEE, demand for advice on dealing with distressed debt is rising among both buyers and sellers. And the nature of the problems allows PwC's team to bring its global experience to bear. The rising tide of sour Swiss franc-denominated loans in Hungary, for example, reminds King of the raft of US dollar loans in Thailand in the late 1990s. “When the baht collapsed, it looked a lot like what's happening in CEE today,” he says.

Of course, the current crisis in CEE is not strictly comparable to a crash halfway around the world more than 10 years ago. Nonetheless, those with experience limited to Western Europe or the US may struggle to understand the dynamics of distressed debt portfolios in Europe's East.

DELAYED EFFECT

The problem of non-performing loans in CEE is likely to get worse before it gets better. Lenders have already been hit by a sharp rise in defaults, particularly in the Baltics, Ukraine and Russia (see chart, opposite). Analysts at Deutsche Bank note that non-performing loans typically lag behind the business cycle by at least six months, so even though economies are

PHOTOLIBRARY



expected to recover gradually, distress levels should continue to rise. The Deutsche Bank analysts forecast peaks of non-performing loans as a share of total loans at up to 10% in Poland, Hungary and the Czech Republic; 20% in South East Europe; 25% in the Baltics; 30% in Russia; and an eye-watering 45% in Ukraine.

Lenders are scrambling for solutions. In an October 2009 report, the IMF urged “decisive measures” to deal with non-performing assets at banks in CEE, including “debt restructurings to share the burden of losses with international creditors”. For the sour loans that have sat on banks’ balance sheets the longest, a sale to specialist distressed debt investors is one way to realise value from the assets, King says. He adds that some investors “trade and manage these types of portfolios for a living”. Last year, PwC was involved in Poland’s largest-ever sale of a non-performing portfolio, a deal involving unpaid principal loans of PLN1.4bn for Bank Pekao.

“Every day we hear about more money being raised to buy distressed assets across Europe,” King notes. According to Hedge Fund Research, investors in distressed assets gained more than 16% in the first nine months of the year. A broad-based index of hedge funds’ investments in CEE, meanwhile, gained 30% in the same period. The intersection of these two categories is attracting interest from a wide range of investors.

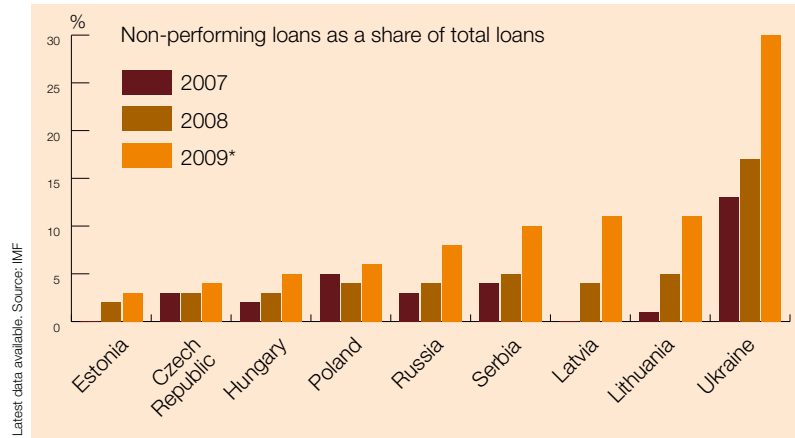
But even if demand is rising fast, the supply of troubled loans is growing even faster. Investors, therefore, can afford to be choosy. In the recent past, sales of distressed loan portfolios were often conducted via auctions, with purchases almost assured. Now investors tend to negotiate on a bilateral basis, conduct much more extensive due diligence on portfolios and pay closer attention to the terms and conditions of any sale.

Given that the credit crisis has rendered many historical benchmarks on valuation and collection of little use, this wariness is understandable. To overcome it, lenders must give potential investors more information and legal certainty. Advisers who can offer a full-suite service, including portfolio analysis and valuation, electronic data room and overall investor management, commercial input into legal sale documents and deal-closing services are finding willing clients in lenders that may not have the time or resources necessary to maximise the chances of a successful sale.

LENDERS, KEEPERS

The answer to lenders’ problems is not always a sale, however, as the scope for restructuring and recovery among recently defaulted borrowers is higher than for older overdue loans. Nonetheless, King urges caution on ramping up internal teams to work out defaulted loans. “We remind these institutions that their resources are best allocated to more profitable parts of the business, such as recently defaulted

RISING TIDE



“We started in Asia and a lot of investors followed us into Europe”

STUART KING, PwC

borrowers, loan origination or product development,” he says. Weighing up the options available to lenders comes more easily to those with experience of boom-and-bust cycles elsewhere. In addition to its Asian experience, the Distressed Debt Group at PwC played a major role in opening the market for foreign investors in Greece, Turkey, Brazil, etc. In less developed markets, PwC often works with international organisations such as the IMF to set up asset management companies and “bad banks”, and to assist with the creation of frameworks for monitoring and resolving non-performing loans.

PwC takes a proactive approach to loan portfolio sales, bringing ideas to lenders. In markets where distressed debt sales are still rare, as they are in much of CEE, local relationships are crucial. The same is true for the buy side: as PwC focuses increasingly on CEE – along with advisers and investors around the world – the rapport built up with investors over the years comes in handy. “We started in Asia and a lot of investors followed us into Europe. Like many investors and sellers, we too are global in our approach, leveraging off our extensive network of local offices,” King says. Whether it is Barcelona or Bucharest, he says, “investors and sellers alike know that we will use a consistent and independent sale process depending on the asset class and size of the portfolio – it gives them comfort.” For lenders, borrowers and investors, this is a commodity in short supply. ■



Club rules

Why CEE's banking community needs to agree on a multi-creditor work out approach

WORDS: HUGO GREEN AND DONALL O'SHEA

What do London, Bangkok, Jakarta and Istanbul have in common? They all have ‘multi-creditor work out’ approaches named after them. The economic and liquidity crisis that hit the UK in the early 1990s and the Far East, including Thailand and Indonesia, in the late 1990s, and then Turkey in 2002, led to the development of recognised approaches to multi-creditor work out being adopted in those countries.

Such work outs are effectively an out-of-court settlement between management of a distressed or defaulting company and their major creditors (usually only banks with no involvement of small creditors) based on a plan to reduce indebtedness. Although the approaches developed differ subtly from each other, all have the London Approach as a common reference point.

Considerable efforts have been invested into learning the lessons of these, and earlier, recessions. In particular, Insol International – a global federation of national associations of accountants and lawyers specialising in turnaround and insolvency – formulated its ‘Principles of Best Practice for Multi-Creditor Work Outs’ which, with the endorsement of, among others, the World Bank, can still be regarded as statements of best practice for multi-creditor work outs. The World Bank in its ‘Principles for Effective Creditor Rights and Insolvency Systems’ put forward policy suggestions which, if implemented by countries and regulators, would further facilitate work out practice.

AGREED RULES

With a well-established international consensus on what constitutes best practice, there are some common rules that govern a typical multi-bank work out.

First, a meeting between all the creditor banks is convened. This should be at the behest of the distressed debtor, whose directors will have sought independent advice on what should be done. However, it could be convened by a bank following a default by a debtor. The purpose of the first all-bank meeting is typically threefold: agreement on the appointment of a lead bank; on the appointment of investigating accountants or consultants; and on a lending standstill, whereby the banks stop demanding repayment of loans for an agreed period to allow for a measured consideration of a debtor’s problems.

The lead bank is usually the one with the largest credit exposure and typically the debtor’s day-to-day transaction bank. It takes a coordination role, ensuring that creditors are informed and, more importantly, ensuring that the work out process maintains momentum.

Experience shows the onerous nature of the position of lead bank is not to be underestimated.

Alongside the investigating accountants, a law firm is also appointed to act for the banks.

TO THE RESCUE

With agreement to a lending standstill in place, the rapid collection of the fullest possible information relating to the debtor’s position is undertaken and shared (on a confidential basis) among the concerned parties in order to find a way forward.

Initially, this information is used to report to banks on whether short-term support is justified. If this is approved, the information helps the debtor to develop restructuring plans and allows the banks’ advisers to review and report on the situation. The advisers’ recommendations in turn allow banks to agree an extension of their support pending the outcome of negotiations on a rescue package.

Rescue package negotiations are typically led by the lead bank acting on behalf of the other banks. At this stage, advisers are critical in ensuring that the end

“Banks should take the opportunity now”

JANUSZ SEKOWSKI, PwC, POLAND

result is achievable and is not likely to lead to further default. The outcome of such negotiations would then be ratified by the banks. Final stages include the revision and completion of necessary documentation and the subsequent monitoring (usually by reporting accountants) of the implementation of the agreed plan.

Underlying the London Approach – and indeed others that have followed – is the need for a body or institution that is sufficiently powerful to provide overarching leadership to ensure that such programmes lead to the rehabilitation of the economy, while at the same time mitigating “collateral damage” during the work out process and avoiding the more dramatic consequences if attempts at work out fail, leading to bankruptcy and liquidation.

The real question is why – even though approaches and frameworks are available and can be applied – there seems to be a gap between what one would expect to be practice and reality. We asked three PwC partners in the region for their thoughts.



Petr Smutny

Partner, PwC
Czech Republic

“In the Czech Republic there is definitely a need to adopt an approach that is comparable to the work out practices developed elsewhere. The Czech banking sector has about €34bn in commercial debt today. About €2bn of that (6%) is non-performing loans and the figure is expected to go up to about €4bn this year. Many of the bigger facilities are syndicated loans and there is no accepted procedure in place for banks to deal with a growing problem.

It boils down to the newness of the situation after a sustained period of economic growth. Market players, including regulators and courts, were not prepared for a wave of distressed debts. Banks, for their part, lack a critical mass of qualified work out personnel on the ground to professionally manage the situation. Equally, as in other countries in our region, insolvency laws are relatively new, largely untested and at the same time not well understood or consistently applied. However, the biggest obstacle for the business community in coming up with a standardised approach to out-of-court work outs is a lack of trust between the parties involved.

Experience shows that in some cases it is likely that lenders will opt for an out-of-court restructuring. However,

“Work out successes will speed up the introduction of a London Approach”

PETR SMUTNY, PwC, CZECH REPUBLIC

the reality at the moment is that often matters are left too late – sometimes because parties cannot come to an agreement banks opt to withdraw their facilities, recovering what they can from their loans by way of bankruptcy.

That is far from an ideal situation. Nobody wants a spate of bankruptcies, especially when it concerns companies that have a decent chance of recovering.

But there are some positive signs. For example, we have just found a buyer for a major distressed company. We are restructuring the company and its debt and the numerous creditors are happy. This was a complex case, but it showed that despite the difficulties, it's possible to find a solution that suits everyone.

A ‘club rules’ approach for CEE is necessary and clearly it's in everyone's interests: banks, debtors, courts, regulators and the economy as a whole.”



The London Approach: banks in CEE need to cooperate to agree a common multi-creditor work out



Janusz Sekowski

Director, PwC
Poland

“Poland's financial community had the opportunity to set out an even-handed loan work out procedure after the country's slowdown in the early 2000s. But the years of prosperity after 2003 meant banks' focus switched to sales. So we now see work out departments, which don't have dedicated restructuring teams, are not seeking out-of-court solutions or are not engaging in open dialogue with other lenders.

In a situation where there is no dialogue between parties and there is little goodwill, an independent adviser can help to get communication going. Even if there is a duty of care to one party (either to banks or debtors), advisers are usually seen as being objective and giving a balanced point of view.

In our experience, there is a tendency in a default situation for parties to look only at the legal aspects. But advisers help focus the discussions on the broader facts and figures – ie, what makes sense from a business perspective. This helps people come to an acceptable, workable solution.

In Poland there is no standardised work out approach *per se*, although some do try to apply something approximating the London Approach. However, the crux of the matter is establishing mutual trust. Confidentiality of banking information and who pays for external advisers are other obstacles to bringing in experts. It is important to recognise that the London Approach was facilitated by the Bank of

England – at that time the UK financial regulator – and the same is true for the other approaches mentioned. All were supported by powerful but independent bodies, which were willing to provide leadership, guidance and occasionally the threat of more formal measures, with the objective of ensuring that the work outs were successful and contributed to the revitalisation of the broader economy. Regulators in Poland could play such a role.

But action needs to be taken sooner rather than later. If you look at past downturns in Poland around 2000, banks were rarely prepared to come to any agreement. However, the situation now is much more serious than then. So now is the time to do it. This is something that will happen in time and once the public can see some success stories.

I've just closed one such success story, restructuring an indebted company that had technically and legally been made bankrupt. But by working with the four banks involved, we gave it a clean bill of health. Now the recoveries for banks and other lenders should be much higher than if they had continued with the bankruptcy liquidation."



Speranta Munteanu
Senior director, PwC
Romania

"Insolvency in Romania is effective, fast and inexpensive. This is in stark contrast to enforcement proceedings which, if contested, could run for years. As a result, in Romania one would have thought that the threat of insolvency would provide an incentive to debtors to develop and negotiate out-of-court restructurings with their creditors, and in this regard the development of a common approach would be beneficial.

Surprisingly, despite the above, we've recently seen cases in which debtors have filed for protection from their creditors with the intention of using insolvency procedures to help them renegotiate their positions and, in particular, take shelter from interest payments and penalties that would otherwise be payable to banks. Banks for their part wish to avoid this on a large scale and find solutions that do not freeze their income streams. Indeed, we know of a number of cases where banks, acknowledging the need to refinance particular debtors, got together as clubs to look for solutions to cover the finance needed and restructure certain debtors.

These clubs have, however, largely been unsuccessful, with discussions between parties often going on for more than a year and then failing. Such failures can be typically attributed to a lack of experience among the parties concerned and an absence of accepted rules of the road

– in particular, guidance on issues such as new money and how to restructure existing exposure and set new risk levels. Equally common in such situations was that banks did not appoint advisory firms to give objective and independent views of a debtor's state of affairs. At the same time, the regulatory authorities were typically also not involved.

The result of such failures has been to make banks think twice about the merits of multi-lateral approaches. Now it's time for the regulatory authorities, banks and banking associations to provide leadership on the development of a process because under the current 'trial and error' approach if a consensus ever were to emerge, it would be too late.

I am relatively optimistic, however, as banks appear to be still interested. At restructuring training sessions I run, I cover out-of-court work outs and when I mention the approaches developed elsewhere, and in particular the London Approach, it generates a lot of positive feedback and interest."

The message is straightforward: in multi-creditor cases, out-of-court work outs are usually better than bankruptcy. In other words, banks and debtors will sooner or later have to work out. The question is when, and how? And when they do restructure, banks must be sure they do it properly. "Amend and pretend" solutions will be no solutions at all. ■

Hugo Green is a director in the business recovery services practice of PwC Slovakia and has more than 25 years' experience in restructuring, work out and financial advisory. Donall O'Shea is the PwC contributing editor for Transform.

BRIDGING THE GAP BETWEEN THEORY AND PRACTICE

What is required:

- Establishment of a regional Creditors' Framework Agreement
- Regulators (central banks) agree to support the implementation of such initiatives and act as leaders
- Collectively, these may enable a practice of work outs in the region to be developed, thereby enabling debt burdens to be restructured and growth to return once more

The issues that need to be addressed and overcome include:

- Inertia; banks are at present perhaps in denial about the problems hitting their loan portfolios
- The fear that banks have of each other
- Short-termism among stakeholders, who do not see or recognise that the benefits of cooperation outweigh the costs of not doing so

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*Kennedy, "Global Crisis and Recovery Consulting Marketplace 2009-2012";
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Sharing the spoils

Multi-listed Czech mining company OKD is the largest producer of hard coal in Central Europe. When it realised its HR and finance functions were not efficient enough, it called in PwC

WORDS: MATT FARQUHARSON

OKD has enjoyed impressive growth since starting life as a state mining company at the end of the Second World War. After being privatised in the early 1990s, it has recently listed in Prague, Warsaw and on the London Stock Exchange. It is the largest producer of hard coal in Central Europe, the only one in the Czech Republic, and, in 2008, had a turnover of €1.6bn and more than 18,000 staff.

As often happens, OKD's scale came with some inefficiency. "OKD has several subsidiaries and mines, and each of those had their own finance function," explains Jiri Halouzka, PwC advisory partner in the Czech Republic. "In its head office, finance was performed in several different departments. Obviously, this was very inefficient: invoices were approved in one place, put on to the system in another and it was difficult to put meaningful management information together quickly. This was important, because OKD is part of New World Resources, which is quoted in London and Prague." The firm's human resources (HR) function faced similar troubles, but on a smaller scale.

PwC was asked to help make these systems more efficient. For Miloslava Trginova, OKD's chief financial and HR officer, the choice of partner came down to finding a company with experience of similar projects that would "avoid mistakes". Over six months, PwC



"Everything is done in one electronic location rather than papers flying around everywhere"

JIRI HALOUZKA, PwC, CZECH REPUBLIC

analysed the HR and finance functions, benchmarking these against peers and looking at the processes and structures. "It became clear that the only way efficiency and effectiveness could be increased was through a shared service centre," says Halouzka.

While the finance function was more complex, similar principles applied and everything that could be centralised was. "That doesn't mean they're always in one physical location, it just means that while mainly in one place, with a new electronic document workflow everything is done in one electronic location rather than papers flying around everywhere," says Halouzka.

This change didn't come without its challenges, however. "We had concerns that the transfer of the administrative part of the finance function might cause a communication breakdown between operations and the shared service centre, with a loss of operations workers' responsibility for the impact of their own decisions on accounting and taxes," Trginova explains. "Now, after the first year of operation, these concerns have been mitigated."

The benefits have been significant. "We have lower operating costs, with the number of finance employees reduced by 20% [to 114], and we've achieved a significant increase in productivity," she says. "The shared service centres are faster, leaner and more flexible." That means management information is much more accurate and timely, which enables managers to make decisions more effectively. "The group can also present their results much faster, which increased shareholder value."

And there is more to come, says Halouzka: "The core team is still in place, working on 'continuous improvement' – trying to make things even more efficient." ■

Matt Farquharson is a business and consumer journalist.

THE WORLD ECONOMIC FORUM GLOBAL COMPETITIVENESS INDEX 2009-2010

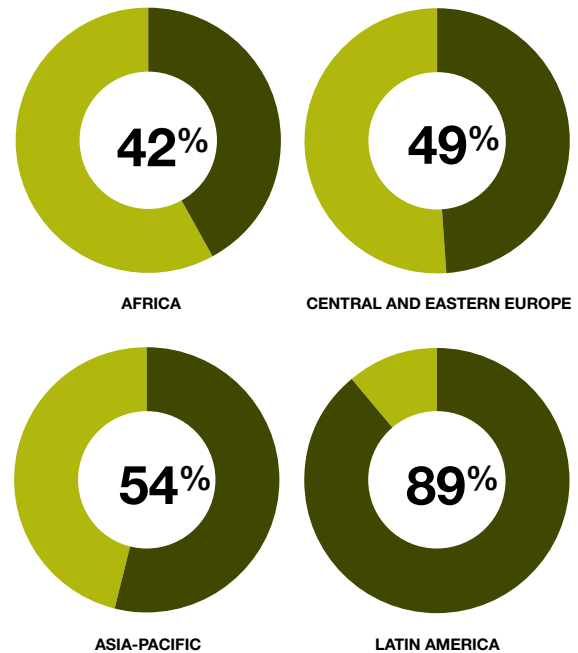
The effects of the current economic difficulties have fed through to the World Economic Forum's latest Global Competitiveness Index.

Across CEE, countries that have found the downturn the most challenging, including Ukraine and the Baltic states, have seen their rankings fall while the likes of the Czech Republic and Poland continue to climb the global index.

Each country's rank/score is based on an assessment of its competitiveness in 12 areas, including institutions, infrastructure and macroeconomic stability.

COUNTRY/ECONOMY	2009-2010 RANK	2009-2010 SCORE	2008-2009 RANK
Czech Republic	31	4.67	33
Estonia	35	4.56	32
Slovenia	37	4.55	42
Poland	46	4.33	53
Slovakia	47	4.31	46
Azerbaijan	51	4.30	69
Lithuania	53	4.30	44
Hungary	58	4.22	62
Montenegro	62	4.16	65
Russian Federation	63	4.15	51
Romania	64	4.11	68
Kazakhstan	67	4.08	66
Latvia	68	4.06	54
Croatia	72	4.03	61
Ukraine	82	3.95	72
Macedonia	84	3.95	89
Georgia	90	3.81	90
Albania	96	3.72	108
Armenia	97	3.71	97
Bosnia and Herzegovina	109	3.53	107
Kyrgyz Republic	123	3.36	122

Source: World Economic Forum



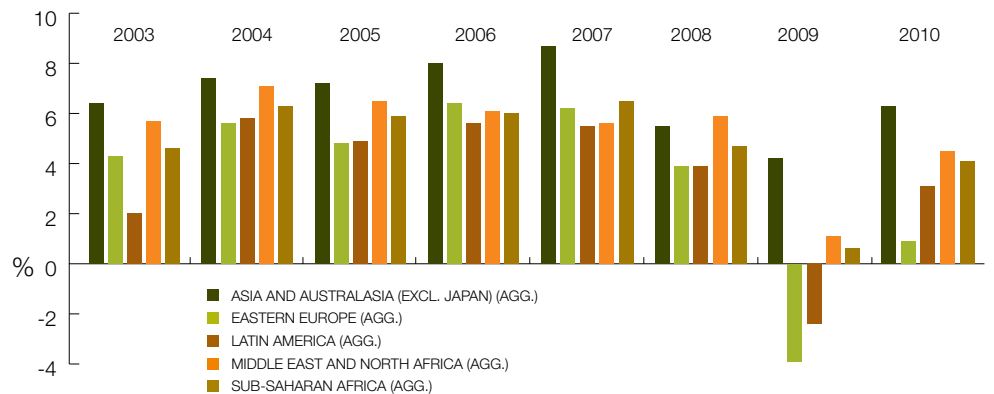
Source: idmarkets.com

Global outlook: Value of FDI (Jan-Aug 09 v Jan-Aug 08)

Foreign direct investment (FDI) flows to emerging markets have decreased considerably over the past year, affecting job generation and consumer spending in those economies. CEE has seen one of the biggest falls. Between January and August 2009, it attracted just 49% of the FDI it attracted during the same period in 2008.

Real GDP growth in emerging markets (%)

CEE is forecast to make a modest return to positive growth compared to other emerging markets in 2010 after falling furthest into negative growth in 2009. The region's weaker GDP growth is down to a number of factors including a high degree of trade and capital market integration, largely foreign-owned banking sectors and a big increase in private sector foreign currency debt, according to the Economist Intelligence Unit.



Source: Economist Intelligence Unit

Financial Advisory Firm of the Year in Eastern Europe



ACQ Finance Magazine has ranked PricewaterhouseCoopers (PwC) as Financial Advisory Firm of the year in Eastern Europe and Financial Due Diligence Advisor of the year in Russia.

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