CENTRAL EUROPE AUTOMOTIVE REPORT

COVERING THE
CENTRAL EUROPEAN AUTOMOTIVE INDUSTRY

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™

CZECH REPUBLIC

Rising Production Levels; Big Investments in Components Sector

Market Highlights:

On September 10, 1996, truck maker **Avia, J.S.C.'s** business name was changed to **Daewoo Avia, J.S.C.** The company is 50.2% owned by a consortium consisting of **Daewoo Heavy Industries Ltd.** and **Steyr-Daimler-Puch AG.** [*For more on Daewoo Avia, see Opportunity Spotlight on Page 8*]

From October 1, 1996, **Daewoo Avia** will produce trucks with engines meeting EURO II standards. In mid 1997, the company will introduce the transitional truck model A75. Production of a completely new model in the 4.5-9 ton total weight category will begin in 1999.

Daewoo Avia expects to record a profit in 1996. Deals are pending for the sale of 300 trucks to Daewoo's Romania car manufacturing factory **Rodae Automobile S.A.**, and 1000 trucks to its plant in Poland, **Daewoo-FSO**. Trucks sold in the Poland deal will probably be in semi or complete knock-down form.

As of September 1996, **ITT Automotive Czech Republic** will have 131 employees at its Jicin factory. The factory was opened in June 1995 with 57 workers. Production of boosters and tandem master cylinders for **Opel**, **Saab**, and **Volvo** started in April 1996. Certifications have been received from Opel and **Volkswagen**, and certification from **Toyota** is expected soon. Products are transported from Jicin to ITT Automotive plants in Germany, Spain, and France. The Jicin operation expects to double its turnover in 3 years.

On September 3, 1996, **Skoda, automobilova a.s.** opened its new plant in Mlada Boleslav for the production of the medium-class Octavia model. Skoda plans to produce about 5,000 Octavias until the end of 1996 to be sold mainly in the Czech and Slovak Republics, where the model will appear on November 15. For 1997, production of 64,000 Octavias is planned, with 90,000 scheduled in 1998. The new factory, which includes a paint shop, will enable Skoda to raise its production to more than 300,000 cars annually as early as 1997.

On October 10, 1996, **Motokov International** plans to sign a new 3-year contract for the exclusive distribution of **Zetor** tractors outside the Czech Republic. Zetor is expected to be privatized by the end of this year. Motokov is also involved in discussions with machinery maker **Skoda Plzen** to distribute its products through Motokov's international network of daughter companies. [*for more on Motokov International, see Spotlight on page 8*]

A new passive safety laboratory will be opened in Mlada Boleslav by the **Motor Vehicle Research Institute (UVMV)** at the end of October 1996. The lab will have testing

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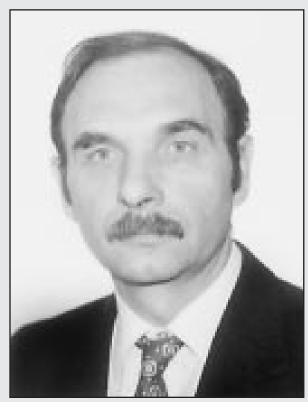
Czech Republic

PROFILE

Automotive Research Institute Adapts to Changing Market

*Founded in 1952, the Motor Vehicle Research Institute ("UVMV") operated as a central supporting institute for research and development activities of the Czechoslovak automotive industry. Today, Prague-based UVMV provides R&D, technical assistance, and approval testing for Czech and foreign companies in the automotive industry. Privatization of the company took place in January, 1993, and two-thirds of its shares are owned by **TUV Bayern Holding, A.G.** UVMV has a staff of 140 employees, 45% of which are engineers. The company's profits have risen from CZK 3.5 million in 1995 to approximately CZK 9 million in 1996. Vladimir Volak is the Managing Director of UVMV.*



Vladimir Volak

CEAR: What services can UVMV provide for companies involved in the automobile industry?

Volak: We operate in two basic fields. First is approval testing according to ECE-UN regulations and EEC directives. We can deliver certificates for both legal systems, as we are the daughter company of the German company

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The mission of the Central Europe Automotive Report is to provide market, investment, and business information that can lead to joint venture, greenfield investment, and product distribution opportunities in the automotive sectors of Slovenia, Hungary, Czech Republic, Slovak Republic, Poland, Bulgaria, and Romania. The Central Europe Automotive Report intends for its information to be used to increase foreign investment in the Central European auto sector; improve the availability, quality, and competitiveness of products and raw materials available to Central European auto manufacturers and suppliers; strengthen existing Central European companies by introducing foreign capital, technology, and expertise; and provide opportunities for auto manufacturers and suppliers to expand their markets.

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ul. L. Derera 2, I./48
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Feature Country *Continued From page 1*

capabilities for crashes (including side impact "crab" tests), airbags, and restraint systems for adults and children. [*for more on UVMV, see this month's Profile interview on page 1*]

For the period January 1, 1996 through August 31, 1996, **Opel C&S spol. s.r.o**, the Prague-based importer and distributor of Opel/G.M. cars and products, sold 6,697 new cars and 541 commercial vehicles. In 1995, C&S sold 6,658 cars and 865 commercial vehicles in the Czech Republic.

The Czech Vehicle Market Vehicle production in 1995 included 208,490 cars, 6,980 trucks, 929 buses, and 2,640 special purpose vehicles. Compared with figures for 1991, car production was up 21%, trucks down 70%, buses down 44%, and special purpose vehicles up 129%. Sixty-six percent of the cars, 40% of the trucks, 47% of the buses, and 1% of the special purpose vehicles were exported in 1995. That same year the Czech Republic had 3,113,476 registered cars and delivery vans, compared with 2,435,645 in 1991. New registrations numbered 175,307 in 1995.

Imports Almost 60 foreign manufacturer's representatives import cars and commercial vehicles into the Czech Republic. Imports of cars have grown from 20,619 in 1993 to 44,420 in 1995. According to Zdenek Lnenicka, Secretariat Director of the Car Importers Association, 55,000 imports are expected in 1996, with this figure rising to 70,000 in 1997. "But we have strong competition with **Skoda's** new Octavia and there's the question of used car imports," said Lnenicka. New cars and used cars are not subject to the same regulations in the Czech Republic. Used cars, for example, don't have to meet emission standards, said Lnenicka. "We don't have enough force to change the situation, to have the same standards for new and used cars," he added.

The Czech Parts & Components Market The **Volkswagen Group's** DEM 1.4 billion purchase of 70% of **Skoda automobilova a.s.** has already improved the Czech parts and components supplier base. Part of VW's long-term strategy is to build up first and second tier suppliers and make them a part of VW's global supply network. Czech production costs are estimated to be 15-20% lower than in western Europe.

According to a case study conducted by **CzechInvest**, VW has upgraded Skoda's supply chain by introducing some 60 foreign component suppliers as joint venture partners with Czech firms and encouraging greenfield investments by foreign component manufacturers [*see chart on page 11*]. It is estimated that 10-15 of these foreign-managed components suppliers are first tier suppliers with design and coordination capabilities.

As of November 1995 Skoda had a total of 370 suppliers, of which 186 are Czech, 17 are Slovak, and 167 are foreign suppliers. It is estimated that 1/3 of all Czech-based suppliers are now foreign managed. These 60 foreign managed Czech companies supply around 50% of all the inputs used by Skoda in its Felicia model by value, and account for the majority of A-rated suppliers.

According to the CzechInvest study, "Skoda has further room to put increased pressure on its component suppliers to reduce unit prices and is increasingly awarding long-term contracts and demanding real price reductions over time."

CZECH REPUBLIC

FACTS & FIGURES

Form of Government: Parliamentary Democracy
Prime Minister: Vaclav Klaus
Capital: Prague
Population: 10.3 million
Labor Force: 5.3 million
Land Area: 78,645 sq. km.
Borders: Austria, Slovakia, Poland, Germany
Ports: Decin, Prague, Usti nad Labem
Highways: 55,890 km.
Railways: 9,434 km
Major Industrial Branches: Fuels, ferrous metallurgy, machinery & equipment, coal, motor vehicles, glass, armaments
Main Imports: electrical engineering, iron, steel, office equipment, data processing machines, raw materials, paper & paper products, cars
Main Exports: iron, steel, textiles, cars, electrical engineering
Customs Free Zones: Prague (4), Zlin (2), Ostrava, Pardubice, Hradec Kralove, Cheb, Trinec
Currency: Crown (USD 1 = CZK 26.6)

Other findings of the CzechInvest case study:

•Skoda's Czech-based component suppliers are now fully integrated into VW's global supplier sourcing network and the Czech manufacturer has full access to all VW Group suppliers.

•Skoda maintains a group of about 30 full-time staff to help its Czech suppliers create improvements as part of a continuous improvement program. The group originally focused on specific remedial solutions, e.g. helping suppliers change workers' break patterns, restructuring the work process, and optimizing material flows. It has now moved on to broader issues of cost control.

•Great improvements have been made in the four years between 1992-1995 to introduce lean production techniques inside Czech component suppliers. When the first audit of Czech suppliers was made in 1991 only two firms made the top category A status, assessed by VW as equivalent to ISO 9000 status. Three years later this number has increased dramatically and it is estimated that 35-50% of all local suppliers have attained this status.

•The transformation of category C suppliers to category B status has mainly involved improving and increasing the technology used in their production and control. The least-advanced suppliers now generate less than 10% of total inputs.

•The average contract size per component supplying company has risen most substantially for Czech-based suppliers, rising from approximately CZK 60 million per supplier in 1992 to just over CZK 86 million in 1995. The figures for foreign and Slovak suppliers dropped marginally.

•Component supplier contracts for Skoda are increasingly awarded in the same way as in the west. According to VW, Czech-sourced components are generally cheaper than those from comparable suppliers in nearby Poland.

•Skoda traditionally made many components in-house. Under VW's direct control in-house production is still often

Continued on page 11

REGIONAL SPECIAL REPORT

BANKING & FINANCING UPDATE

Slovakia

New Rules in Slovakia Restrict Loans Faced with surprisingly high recent money supply increases (M2), the **National Bank of Slovakia** has responded with restrictive actions to stave off higher inflation. The bank increased the minimum reserves requirement and enacted several administrative measures to reduce the money supply. The increase in M is partly due to the huge increase in foreign exchange loans. Loans are being made in foreign currency to companies who take advantage of the arbitrage opportunities created by the large interest rate gap between the Slovak crown (BRIBID 12.5%) and foreign currencies (FIBOR 3.1%).

The central bank has warned that if these measures don't reduce M2, the bank will resort to even harsher measures. Bank industry insiders speculate that such measures might include a direct limitation on the amount of loans banks can provide or a devaluation. On January 1, 1997, the new National Bank accounting rules for foreign exchange assets and liabilities go into effect. "Right now, we're not issuing any loans in foreign exchange until we find out the rules," said Tim Stephens of **Tatra Banka** in Bratislava.

Fierce Competition Competition for quality clients "is very hard," said Niels Lundorff, Vice Chairman of the Board for **Bank Austria** in Bratislava. With five new foreign banks coming into the market over the past two years, competition for customers is fierce and spreads are squeezed. Not only are there more banks on the market, but local banks have become more competitive by improving their technical sophistication and the education level of their people. "We see a very high professional level here," said Lundorff. Despite the tough competition, Lundorff said there are still opportunities in Slovakia. "Privatized companies in general need [investment] financing and many foreign companies start production in Slovakia due to the low [labor] costs," he said. "They are all looking for an efficient banking partner."

Auto Leasing Company One of the Best Credits The auto financing company **Skofin spol. s.r.o.** is, according to a banker in Bratislava, "one of the best credits in this market." The banker noted that margins on Skofin loans are thin, but that reflects the quality of the credit. Skofin is reportedly receiving bids from six banks for long-term funding which will probably have a term of 3-5 years.

Financing for Dealership A SK 100 million, 4-year, 14% bond issue was floated in August of 1996 by **Drukos spol. s.r.o.**, a **Volkswagen**, **Audi**, and **Skoda** dealership in Banska Bystrica. The company is looking to raise another SK 300 million by issuing a series of SK 100 million, 2 or 3-year bonds. The bonds will be structured like loans and interest will be paid over the life of the bond. According to one banker, these unique instruments may be difficult to sell to investors. The company is reportedly raising capital through these bonds because of difficulty finding bank financing. Dealerships are a "risky business from a credit perspective," said the banker.

Czech Republic

Transparency of Markets Improving The Czech financial markets are becoming more transparent. According to Emilio Peregrini, Deputy General with **ABN-AMRO** bank in Prague, there has been a "dramatic improvement" in market transparency in the last two years. Nonetheless, he noted, there's still not the same level of reliable financial reporting as found in western markets.

Competition Tough as Big Borrowers Resort to Foreign Markets As in the other Central European markets, competition in the Czech banking industry is ferocious. There are some 50 domestic and foreign banks looking for business in the Czech Republic. To make matters worse, said one banker, quality borrowers such as **Skoda** do not raise money locally. Although Skoda is expanding its production facilities in the Czech Republic, much of its financing is raised in Germany. Furthermore, historically strong companies such as truck makers **Tatra** and **Liaz** are facing difficult financial circumstances.

Automotive Companies Favor Bank Debt "Generally speaking, automotive companies lean towards bank debt," said Kent Holt of **ING Baring Capital Markets** in Prague. "It's easy to understand and involves one on one negotiations." Bank debt also involves much lower fixed costs than, say, floating a bond issue. The bond market in the Czech Republic is active but has been defined by a small group of issuers, primarily banks and big industrial companies. New 11.5% reserve requirements for bank bond issues are likely to deter banks from raising money in the bond market.

Companies Introduce New Instruments ING Baring is introducing innovative products into the market, especially commercial paper instruments. "We're interested in the automotive market," said Holt. "It offers lots of potential." The commercial paper market in the Czech Republic is developing along normal lines, but the current tax structure is keeping paper from becoming a truly marketable instrument. As a result, much of the paper is placed abroad.

Slovenia

Slovenia's Leasing Market Heats Up Over 70 Slovenian companies are engaged in leasing as a registered activity and most of these companies provide auto leasing. Many leasing companies are connected with Slovenian bank subsidiaries. Leasing costs are high in Slovenia, but growing competition between local and foreign leasing companies should reduce prices and increase the number and quality of services offered by leasing companies. According to Janko Koren, General Manager of **Avtomontaza-bus** in Ljubljana, "the car and bus leasing business is booming, and this is a good development for us." Avtomontaza-bus introduces its customers to banks or leasing companies who can assist the customer with financing. ■

"This plant is a milestone for the next hundred years of automobile production not only here in Mlada Boleslav, but in the entire Czech Republic." Skoda Chairman Ludvik Kalma referring to Skoda's new plant built to produce the Octavia model in the Czech Republic.

Czech Republic

LEGAL ADVISOR

PROTECTING PATENTS IN THE CZECH REPUBLIC

The current Czech patent law was adopted by the Czechoslovak Federation in 1991. The Czech Republic has allowed this law to remain in effect as it is in line with long standing international patent accords. Additionally, the Czech Republic is a member of the Patent Cooperation Treaty (herein "PCT"). Thus, international patent applications of Czech businesses, citizens, or residents may be filed from within the Czech Republic at the Czech Patent Office.

Patent Prerequisites: Patents are granted by the Czech government for inventions which:

(a) possess novelty;
(b) represent a progressive, innovative advance; and
(c) possess industrial utility.

The litmus test under Czech patent law for novelty is whether or not such an invention represents the "current status of technology." Should the invention represent merely a minor advance from this "current status," then the invention is not eligible for patent protection. Additionally, Czech patent law states that an invention is deemed to be representative of technology's "current status" if information in relation to such invention was not public more than six months prior to the filing of the application. With respect to the issue of industrial utility, Czech law requires that a patentable invention must be capable of being "used repeatedly for economic activities."

Inventions which do not qualify for patent protection are:

(a) discoveries, scientific theories, and mathematical activities;
(b) minor improvements to an existing good;
(c) plans, rules, and mechanisms of intellectual actions;
(d) computer programs; and
(e) presentations of information.

As is true with international patent legislation, intellectual discoveries which have not been translated into a concrete, economic "good" are not awarded patents under Czech patent law. Furthermore, any inventions that are deemed to be in conflict with the best interests of the population, such as those inventions deemed to be contrary to public morale and public interests or harmful to the environment, are exempt from patent protection.

Characteristics of a Czech Patent: A patent filed within the Czech Republic has a duration of 20 years from the date of the filing of the petition. Fees are levied by the Patent Office for the maintenance of an existing patent. *Czech law only grants patent rights to those claims that are made in the approved patent application.* Any additional features of the invention not stated in the application are excluded from patent protection.

Czech law allows for the licensing and assignment of patent rights. Any assignment or licensing of a patent may only be by written agreement which must be filed with the Patent Office to be effective. In the event that a patent has multiple holders, then the consent of each holder must be obtained in order to properly conclude an assignment or licensing agreement. The income from such assignment or license must be distributed to the patent holders on an individual basis.

In the event that an invention results from a standard employment relationship, the employer maintains the right to the patent. Upon the development of a patentable product, the employee may petition the employer to surrender this right. Should three months expire after the deliverance of such petition to the employer, then the employee receives the right to pursue patent protection for the invention. In the event that an employee claims a patent without notification of the employer, then that patent claim is void.

Publication, Filing, and International Patents: All patents filed with the Patent Office are published in the Patent Office's publication, the "Vestník". Typically, patent applications are published in the Vestník 18 months after the expiration of that application's priority date. In accordance with international patent standards, the Czech Republic uses a "first-to-file" system. *Patent applications of Czech citizens are not prioritized over those of non-Czech citizens.*

An extensive evaluation of the application by the Patent Office is a prerequisite to the granting of the patent. This examination must be requested by the applicant no later than 36 months after the filing of the application.

International patent applications: Applications prepared according to PCT protocol may be filed by American businesses, citizens, and residents using the U.S. Patent and Trademark Office as a Receiving Office. It is the duty of the Receiving Office to verify that the application meets the PCT protocol requirements, to collect transmission fees for international applications, and to transmit copies of international applications to the International Bureau and the International Searching Authority which are located in Switzerland.

Reports on patent searches conducted by the International Searching Authority are transmitted to the International Bureau, which in turn publishes international applications in the International Gazette and transmits international applications and their accompanying documentation to the national offices designated in the international application.

All patent applications received by the Czech Patent Office, whether they are filed from the Czech Republic or are received from the International Bureau, must be submitted in Czech. In accordance with the standard Czech legal procedure regarding the admission of translated documents, these translations must be certified by an official translator. The Patent Office may reject a foreign PCT application if the subject of the application has already been introduced to the Czech marketplace prior to the filing of the application.

A foreign PCT application that is granted a Czech patent is afforded the same protection under Czech law as Czech patents, including the right to collect damages resulting from demonstrated patent infringement. *If a foreign patent-holder does not seek patent protection in the Czech Republic by filing a valid application with the Patent Office for patent rights, then that individual shall not receive such protection in the Czech Republic.*

Todd Coop, a Legal Research Assistant with the law firm Baker & McKenzie in Prague, prepared this article. ■

CENTRAL EUROPE AUTOMOTIVE REPORT

To Our Readers:

Ronald F. Suponcic, Jr.
Publisher

Jeffrey A. Jones, Esq.
Editor-in-Chief

The Czech Republic's vehicle industry is enjoying the benefits of significant foreign investment. Volkswagen's long-term commitment to the Czech market is evident in the recent opening of the new plant in Mlada Boleslav to produce the Skoda Octavia model. Skoda plans to produce 350 million cars annually in the Czech Republic by 1997. Truck-maker Daewoo AVIA expects to manufacture up to 95,000 vehicles annually in the Czech Republic by the year 2000. The company also plans to conduct much of the research and development for its new line of trucks in the Czech Republic.

And the investment doesn't stop with the big vehicle manufacturers. It extends deep into the Czech parts and components industry. A quick look at the chart on page 11 gives an indication of the scope of investment in the components industry. Local manufacturers have received vital foreign capital and technological expertise, benefiting themselves as well as the vehicle manufacturers who want to increase the number of their local suppliers. According to a case study conducted by CzechInvest, as of the end of 1995 about 50% of Skoda's suppliers were based in the Czech Republic, providing annual inputs valued at CZK 16 billion.

The Czech automotive market is moving fast and many opportunities exist for cooperation between industry players. See this month's Opportunity Spotlight for a review of just a few of those opportunities

As always, please contact us with any requests you have for coverage of specific topics in future issues. The Central Europe Automotive Report is designed to provide you with the information you need to understand and succeed in the dynamic Central European automotive industry. ■

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We are the only publication to focus entirely on covering the automotive sector in this region.

Czech Republic

FOCUS ON INVESTMENT

INVESTMENT TIPS/RECENT LEGISLATIVE CHANGES AFFECTING INVESTMENT

Investors should be aware that corporate formalities in the Czech Republic are much more bureaucratic than they may be elsewhere. Depending on the investment vehicle, multiple approvals may be required, ranging from trade licenses and Czech-language tests to local permits for environmental or construction purposes.

The Czech Republic held Parliamentary elections May 31 to June 1 of this year. As these elections are the very first for the Czech Republic (prior elections having been as the Czech and Slovak Federated Republic), investors watched closely whether there would be evidence of stability or reaction. The result was stability, in the form of a minority coalition government: Prime Minister Vaclav Klaus retained his position as leader of the governing coalition, following agreement with the main opposition party, Milos Zeman's Social Democratic Party.

Despite popular support for Klaus's fast free market reforms, the greater presence of Social Democrats has likely softened Klaus's stance toward government restraint in regulation and enforcement. For example, the government has not placed the energy, gas, and heating companies on the block, as was expected, as there has been concern expressed that any price regulation issues should be resolved first. Investors generally applaud this choice in principle, but complain that no apparent steps have been taken toward drafting the regulation. As a result, there is some concern that the Czechs have lost the momentum displayed earlier in their transformation. The ruling coalition denies any need for concern on this point, saying that it intends for the Czech economy to be more highly privatized than other Western European economies.

The first Senate elections are to be held in September 1996. While the Social Democrats may make a better showing in these elections, the Senate has limited power to propose or veto legislation adopted by the lower house of the Czech Parliament.

Investors who are considering entry into traditionally regulated sectors (energy, telecommunications, banking, securities, insurance, and others), or whose investments in another sector will require approvals or other dealings in those areas, should take several steps to identify the current state of regulation, and to scout out potential future changes. These include the following:

Traditional due diligence in identifying current laws, regulations, and decrees which touch on price restrictions, disclosure of information, reporting requirements, and the like, should be supplemented with attention to upcoming changes.

Investors in traditionally regulated sectors should explore whether changes are being proposed, and the scope and extent of such regulation. Potential areas of change include proposed legislation, enforcement policies, potential new regulatory bodies, and changes following admission into the OECD and prior to admission into the European Union. Proposals are on the table for a US-style Securities and Exchange Commission and price structure regulation in the energy sector, among others.

Routine enforcement has not been a significant concern for investors in the Czech Republic, as the free-market approach of the Czech Government has been expressed as a hands-off approach. The new Government will likely be less restrained.

Meetings with regulators and potential regulators are recommended. Once an investor has completed researching the available background information, and even if the size and scope of investment is modest, it may be advisable to meet with government regulators in the Ministry of Finance, Ministry of Trade and Industry, and other relevant Ministries. This is especially advisable if any government approvals are required. As the Ministry of Finance is headed by a member of Klaus's party, Industry and Trade is headed by a member from another coalition party, an investor is likely to encounter differing advice and responses from each of the Ministries.

Assistance from local investor partners may be invaluable to an investor, especially in first identifying useful sources of information. Investors from Western Europe and the US should be aware, however, that Czech investors and entrepreneurs are not sensitive to the degree of attention to detail demanded by investors elsewhere.

Recent legislative changes affecting investment: In April, the Parliament passed extensive changes to the Commercial Code (which provides for corporate entities such as limited liability companies and joint-stock companies), the Securities Act, the Stock Exchange Act, and the Investment Companies and Funds Act.

Earlier in the Spring, the Parliament also passed significant changes to the Bankruptcy Code. In general, these changes were meant to provide for greater transparency of shareholdings and transactions in the financial marketplace and to limit entrepreneurs' abilities to "loot" their corporations for private gain. As a practical matter, the new amendments have also placed greater disclosure requirements on corporate entities and provided for additional liabilities for those on management and supervisory boards. New provisions include the following:

- Requirement to offer to buy-out minority shareholders following certain block acquisitions
- Reporting requirements for those holding over ten percent of a publicly traded company
- Greater public access to shareholding information
- Requirements to buy-out minority share holders if a company de-lists or goes private
- Broader preemptive rights for shareholders
- Enhanced shareholder rights and diminished board freedoms
- Stricter non-competition rules for board members and certain management executives
- Additional liabilities for directors and management executives
- Requirement that investment companies and funds be joint-stock companies

These amendments represent several hundred pages of new legislation. In addition, many of the provisions are unclear and none of them have been tested in the courts.

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Czech Republic

OPPORTUNITY SPOTLIGHT

This month's Opportunity Spotlight features 4 Czech companies interviewed by the Central Europe Automotive Report. Opportunities exist for cooperation with these companies in the form of supply agreements, technical development assistance, and distribution agreements.

Daewoo Avia, J.S.C.

Light-truck maker Daewoo Avia is 50.2% owned by a consortium consisting of South Korean **Daewoo Heavy Industries Ltd.** and Austrian **Steyr-Daimler-Puch AG**. The consortium has been the majority owner of Avia since August 1995. The company's facility in the Czech Republic handles production, research and development, sales, service and repair, and special modifications of vehicles. In 1995, 4,000 trucks were sold, giving Daewoo Avia an 80% market share in the Czech Republic.

DAEWOO-AVIA Production & Sales (January - August 1996)

Production of AVIA Trucks	(units)	2,492
Total AVIA Truck Sales	(units)	2,403
Total AVIA Truck Exports	(units)	657
DAEWOO Car Sales	(units)	2,937
Sales Revenues	(CZK million)	1,802
	(USD million)	69.3

Source: Daewoo-AVIA

Production Cabins, chassis, and engines for platform trucks and vans are produced in the Czech Republic. Truck superstructures are purchased from other manufacturers. In the future, the Czech Republic facility may produce engines for companies within the Daewoo Group; by the year 2000, engine production capacity will be 70,000 units. It was recently decided by Daewoo that the Czech Republic, not Korea or England, will be the center for development of its new truck models. "We are the center of development for these trucks," said Jiri Kyncl, Head of Public Relations at Daewoo Avia.

Strategic Goals/New Models One of the company's strategic goals is the development and production of trucks in the 4.5-9 ton total weight category. Daewoo Avia will be the only manufacturer of trucks in this category within the Daewoo Group. By the year 2000, the company plans to commit USD 350 million for development of the new models and reconstruction of its factory. These models will be introduced in 1999, will feature a new cabin, and planned yearly production capacity is 30-50 thousand units by the year 2000. Whether Steyr engines will be used is still under consideration. Studies conducted by Avia indicate that the engine they use now can be modified to meet EURO III standards. The trucks will be built for the world market and delivered through the Daewoo sales network.

Daewoo Avia's A 75 model, which will be produced in mid-1997, represents the last major innovation of the existing Avia line. The truck will feature a new chassis, riveted frame, disc front brakes, 17.5 inch wheels, an engine with 85 kW of power that meets EURO II standards, rigid front axle, and a tilt cabin. Right hand steering will also be available for export.

Exports "We must export to survive," said Kyncl. With 354 Avia trucks exported to the Slovak Republic in 1995, the Slovak Republic became the largest Avia importer. The company expects to sell 1/3 of its production to Central and Eastern Europe, 1/3 to Western Europe and North Africa, 5000 units to South Korea, and the remainder to other Asian countries and South America. Trucks are exported in semi-knockdown form to Poland and Uzbekistan.

Early in 1996 Daewoo Avia met with groups of Daewoo dealers from Asia, the Middle East, and South America and informed them about what was available for export. The company also requested from the dealers marketing studies about their respective regions.

Car Importing From the beginning of 1996, Daewoo Avia has been the exclusive importer and distributor of Daewoo cars for the Czech Republic. In 1996, Daewoo Avia expects to sell 5,000 cars and to have total sales revenues of more than USD 185 million.

Suppliers Daewoo Avia currently has many traditional suppliers, but is willing to change to new suppliers to find the right price, quality, and flexibility. The company is still selecting suppliers for important parts and components. "Free competition" is the rule, said Kyncl. The company is trying to focus on domestic suppliers. Kyncl noted that "Daewoo is ready to help suppliers with any technical or capacity problems."

Employees The company has approximately 2,200 employees. Average wages in 1995 were 8,596 Czech crowns. The average wage increase from 1995-1996 for all workers at Daewoo Avia was 20%.

Biggest Challenges Developing the new truck model for production in 1999, organizational reconstruction, and employee development.

Renascoop spol. s.r.o.

Renascoop is the distributor for the Hungarian wheel rim manufacturer **Ples**. The company has distributed for Ples for four years and covers the Czech and Slovak Republics. Rims are distributed to truck manufacturer **Skoda Liaz**, and trailer makers **BSS Metaco** and **Panav**. Renascoop sells approximately 1/4 of Ples's production, which amounts to 15,000 rims sold in the Czech Republic, and 8,000 rims sold in the Slovak Republic. According to Renascoop's director Jan Remes, the company is interested in talking with other companies about distributing products in the Czech and Slovak Republics.

Praga

Praga is a privatized producer of special heavy vehicles (municipal maintenance trucks and off-road transport trucks) and mechanical gearboxes for trucks, buses, tractors, and special vehicles. The company also designs and produces special teeth generating tools and gear replacement parts. Praga employs 1200 workers.

Financial Outlook The company has yearly turnover of 1.4 billion Czech crowns and expects a profit in 1996 of CZK 60 million. Considering that Praga suffered a CZK 150 million loss in 1994, the figures for 1996 are impressive. "A major reason for the improvement in profit has been a rationalization of our business, cutting costs, streamlining," said Dr. Jiri Hynek, Praga's Marketing Director and Chairman of the Board of Directors.

Production & Sales Plan Production and sale of gearboxes and replacement parts are the focus of Praga's current activities. Praga's traditional markets are in the east, including Russia and the Ukraine. The company is striving to improve its business in Poland, Serbia, Hungary, Romania, and Western markets. "We think our gearboxes are good enough for the western markets, including the U.S.," said Hynek. "Our prices are competitive in the West."

Capacity "We can increase our capacity," said Hynek. Capacity exists for 20,000 transmissions, and current production is 8,000. "We would be interested in exploring other alternatives to use that capacity," said Hynek. "We're on the lookout for new opportunities."

Suppliers Eighty-percent of Praga's raw materials are purchased in the Czech Republic. Hynek noted that they find the best prices for supplies in the Czech Republic, "even when compared to Russia."

Customers Daewoo Avia is one of Praga's biggest customers for gearboxes. Praga's success, therefore, is closely tied to Daewoo's production plans. Praga also sells to Czech truck maker **Skoda Liaz** and Czech bus maker **Karosa**.

Praga's 1995 Commercial Vehicle Production & Sales

Model	Engine	Production	Local Sales	Exports
UV 80	Avia	8	7	1
UV 80	Avia	1	1	—
UV 80	Deutz	12	12	—
UV 80	Deutz	2	2	—
Total		**23**	**22**	**1**

Source: Praga

Biggest Challenges Expanding into new markets, and finding reasonably priced loans.

Motokov International Ltd.

Motokov International, a privatized holding company, is a part of the Motokov group of companies. The Motokov group includes approximately 30 companies, many of which are involved in the import, export, and distribution of vehicles and vehicle parts and accessories. **Motokov, a.s.**, the group's mother company, acts as the exclusive importer and distributor for **Hyundai**, **Jaguar**, and **CASE IH** agriculture tractors and harvesters. A Motokov group company in the Czech Republic is the exclusive importer and distributor of **Citroen** cars. A special Motokov division exports **Tatra** trucks, **Liaz** trucks, and **CKD** tramways. Motokov, a.s. owns 50% of Motokov International.

Tractor Distribution The distribution of Czech-made **Zetor** tractors and agriculture machinery is the main activity of several Motokov International daughter companies. The tractors are exported from the Czech Republic directly to MI daughter companies in Europe, the U.S., and Canada. According to Jiri Marek, Area Director for Motokov International, Zetor tractors face strong competition in the U.S. and Canada. "Prices are not as advantageous as they were," he said. The company keeps in continuous contact with the Zetor factory to keep their prices at competitive levels.

"We are also trying to reduce our costs in these countries," said Marek. One way they reduce their financial costs is by asking the factory to extend their credit arrangement from 12 months to 18 months, thereby eliminating the need to borrow in the local markets. Marek noted that they also focus on quality to save warranty costs.

Distribution Opportunity Motokov International is open to distributing other products through its network. "We can distribute everything that moves," said Marek, "from bicycles to trucks." Motokov International also imports tires, motorcycles, and Italian and Indian-made tractors.

Motokov International Sales (1/1/96 - 8/31/96)

Item	Units	Turnover (mil. CZK)
Tractors*	2,755**	1,801
Trucks*	42	94
Agriculture Machines*	1,277	96
Passenger Cars	4,199	1,515
Motorcycles	914	34
Tires	—	319
Others Goods	—	268
Total		**4,127**

*including spare parts
**does not include sale of 556 Zetor trucks in Poland by Moto-Zetor, owned by Motokov a.s.
Source: Motokov International

Turnover Turnover for Motokov International in 1995 was approximately CZK 6 billion, and turnover for the Motokov Group was CZK 9 billion.

New Markets In 1996, Motokov International established a joint venture in Poland that will assemble 1000 Zetor trucks by the end of the year. The company is also preparing another joint venture in Poland for the distribution of **Liaz** trucks. ■

Czech Republic

Passenger Car (PC) & Light Commercial Vehicle (LCV) Sales in the Czech Republic by Car Importers Association (CIA) Members (January - August 1996)

	PC		LCV		Total		CIA
Make	**Units**	**Share in CIA**	**Units**	**Share in CIA**	**Units**	**Share in CIA**	**Position**
Audi	522	1.15%			522	0.97%	17
BMW	356	0.78%			356	0.66%	20
Citroen	711	1.56%	1052	12.47	1763	3.26%	11
Daewoo	2945	6.46%			2945	5.45%	7
Daihatsu	150	0.33%	31	0.37%	181	0.34%	23
Fiat	4777	10.48%	283	3.36%	5060	9.37%	4
Ford	5122	11.24%	1818	21.55%	6940	12.85%	2
Honda	1190	2.61%			1190	2.20%	14
Hyundai	1633	3.58%	453	5.37%	2086	3.86%	9
Chrysler	259	0.57%			259	0.48%	21
Jaguar	22	0.05%			22	0.04%	29-30
KIA	504	1.11%	115	1.36%	619	1.15%	16
Lada	1515	3.32%			1515	2.81%	12
Lnd/Rng Rover	24	0.05%	6	0.07%	30	0.06%	28
Mazda	2349	5.16%	390	4.62%	2739	5.07%	8
Mercedes	257	0.56%	214	2.54%	471	0.87%	19
Mitsubishi	332	0.73%	187	2.22%	519	0.96%	18
Nissan	716	1.57%	267	3.17%	983	1.82%	15
Opel	6697	14.70%	541	6.41%	7238	13.40%	1
Peugeot	1095	2.40%	857	10.16%	1952	3.61%	10
Proton	22	0.05%			22	0.04%	29-30
Renault	3971	8.71%	699	8.29%	4670	8.65%	5
Rover	142	0.31%			142	0.26%	24
SAAB	52	0.11%			52	0.10%	27
SEAT	3022	6.63%	101	1.20%	3123	5.78%	6
Subaru	128	0.28%			128	0.24%	26
Suzuki	199	0.44%	14	0.17%	213	0.39%	22
Toyota	1129	2.48%	277	3.28%	1406	2.60%	13
Volvo	134	0.29%			134	0.25%	25
VW*	5591	12.27%	1130	13.40%	6721	12.45%	3
*without L80							
TOTAL CIA	**45566**	**100.00%**	**8435**	**100.00%**	**54001**	**100.00%**	
OTHERS							
Skoda	55095	54.70%	2894	24.03%	57989	51.43%	
Tavrija	0	0.00%			0	0.00%	
Tatra	47	0.05%			47	0.04%	
AVIA Trend	7	0.01%			7	0.01%	
TAZ			527	4.38%	527	0.47%	
Skoda Elcar			34	0.94%	34	0.06%	
Lublin-PL			62	1.72%	62	0.11%	
Nysa			90	2.50%	90	0.15%	
Total Others	**55149**	**54.76%**	**3607**	**29.95%**	**58756**	**52.11%**	
Total Others + CIA	**100715**	**100.00%**	**12042**	**100.00%**	**112757**	**100.00%**	
CIA Share		**45.24%**		**70.05%**		**47.89%**	

Source: CIA, September 16, 1996

Central Europe In 1996-97

1996

Nov. 6-10 — **Nitra, Slovakia** Int'l Plastics Exhibit (including injection equipment)

Nov. 7-10 — **Wroclaw, Poland** Fair of Electronics, Telecom, & Electrical Eng'g

Nov. 13-16 — **Warsaw, Poland** Int'l Fair of Tools & Machinery

Nov. 19-22 — **Poznan, Poland** Investment Opportunities in Polish Cities

Nov. 19-21 — **Bratislava, Slovakia** Metal Surfaces Treatment Technology & Materials

Nov. 21-23 — **Bydgoszcz, Poland** Int'l Fair of Polyurethanes

Nov. 23-25 — **Szczecin, Poland** Int'l Specialist Fair of Transport & Forwarding

Nov. 28-30 — **Olsztyn, Poland** Electronics Fair

1997

April 25-30 — **Poznan, Poland** International Fair of the Automotive Industry

April — **Celje, Slovenia** Car & Maintenance Fair

April — **Ljubljana, Slovenia** Fair of Farm Vehicles & Supplementary Equip.

Czech Republic

FOREIGN INVESTMENT IN THE CZECH COMPONENT INDUSTRY

Investor	Czech Partner	Component	Origin	Form
Avon	Rubena	rubber parts	UK	joint venture
Bosch	ABS-ASR	brake systems	Germany	acquisition
Bosch	Motor Jikov	air-brakes	Germany	joint venture
Continental	Barum	tires	Germany	acquisition
Ford	Autopal	lights, heat exchangers	USA	acquisition
Goetze	Buzuluk	piston rings	Germany	joint venture
Hagen Technik	Akuma	batteries	Germany	acquisition
Hayes Wheels	Autokola	wheels	USA	acquistion
Hella	—	headlights	Germany	greenfield
ITT Automotive	—	—	USA	acquisition
Johnson Controls	OPMP	seat frames	USA	acquisition
Kelsey-Hayes	Nova Hut	wheels	USA	joint venture
Knorr	Ateso	hydraulic brakes	Germany	joint venture
Kolbenschmidt	Metal	engine components	Germany	acquisition
Leistritz	Autometall	exhaust systems	Germany	joint venture
Lucas	Autobrzdy	brakes	UK	joint venture
Magna	Volant	steering wheels	Canada	acquisition
Magna	—	seat & brake parts	Canada	greenfield
Packard-Electric	Azbestos	cable harnesses	USA	acquisition
Pelzer	—	carpets	Germany	greenfield
Porsche	—	parts	Germany	greenfield
RHW Stadthagen	Lecotex	—	Germany	joint venture
Rockwell Automotive	RABS	axles/wheels	USA	acquisition
Schade KG	—	parts	Germany	—
Siemens	—	cables	Germany	greenfield
Tenneco	—	mufflers	USA	acquisition
TRW	CKD	switches, relays	USA	acquisition
TRW	—	valves	USA	acquisition
TRW	TRW Repov	fasteners	USA	acquisition
Turner & Newell	Osinek	brake linings	UK	acquisition
VDO	PAL	instruments	Germany	acquisition

Source: VW, CzechInvest

Feature Country *Continued From Page 3*

better organized than the local supply industry. Internally-produced components include engine components and gearboxes from Skoda's aluminum foundry and drop-forged camshafts, gears, and axle components.

More study findings:

• As a result of the 6-year upgrading process, by 1997 the Czech Republic will be left with a reduced number of well qualified component suppliers capable of exporting directly to manufacturers in Poland.

• Foreign-managed suppliers will dominate in two areas, first as first-tier systems suppliers, and second as suppliers of heavy multi-part and electronic components that made their debut in the Felicia range (e.g. air-conditioning systems, ABS, and power steering).

• Some Czech companies have the opportunity to become world-class suppliers of sub-systems and components within the supply chains of world-class systems suppliers. A growing number of Czech component companies are exporting into the VW Group network. In 1995, the total amount came to more than DEM 100 million. This figure will rise dramatically in the next 2-3 years.

• In the near-term, VW will investigate sourcing components from Poland and Hungary.

• Skoda's management noted that Czech wages are approximately one-tenth of German wages, while wages in Russia are one-tenth of Czech levels. The eventual sourcing of components for the VW Group from within the ex-Soviet Union is only a matter of time. Component projects would have to be self-financing at the start so that the foreign partner could reinvest one part of the profit into upgrading the plant.

"I drove it over the test track and I really like it. It accelerates well, it is comfortable and I would say it is a very good car."
Czech Republic President Vaclav Havel after test driving Skoda's new Octavia model.

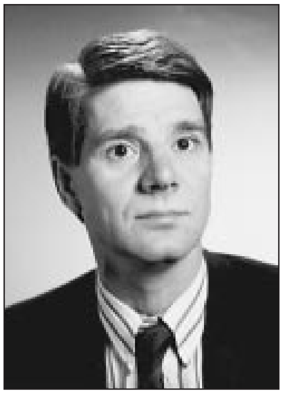
Sources: CzechInvest, Car Importers Association, Automotive Industry Association of the Czech Republic

Continued on page 15

Czech Republic

ACCOUNTING & FINANCE

TAXES AND CUSTOMS UPDATE



Hugo van der Zee

Relatively small funds are allocated by the government in the state budget to help finance new production facilities. There are no tax incentives in the form of reduced taxes for starting businesses, and no special incentives exist for manufacturing activities.

The general income tax rate for legal persons is 39% for 1996. Over the past several years the income tax rate has steadily decreased, a trend which is expected to continue. There are no local taxes.

Tax losses can be carried forward for seven years in any portions the enterprise considers optimal. With a decreasing rate of income tax, it is advisable to utilize the tax loss as soon as possible.

A notable investment incentive is the possibility of deducting 10% of the input price of new machinery and equipment from the income tax base of the enterprise for the year in which such equipment is put into operation. This in effect enables companies to depreciate 110% of the input price of most assets. If, however, such asset is sold or leased in the following three years the amount of the 10% investment deduction must be returned by adding it to the tax base.

Tax depreciation of assets is regulated by the Income Taxes Act which identifies five categories of assets: i) 4 years for personal cars and vans up to 1.5 tons, office equipment, software, communication equipment; ii) 8 years for machines and tools, cranes, trucks, furniture; iii) 15 years for metal structures, vessels, elevators, air-conditioners, patents; iv) 30 years for wooden or plastic buildings, pipelines; and v) 45 years for buildings.

The accelerated method of depreciation is predominant among enterprises in the Czech Republic. The law also excludes some assets from tax depreciation, among them notably know-how invested into the company by a shareholder when he has acquired it without consideration.

The Czech Income Tax Act contains a special provision on arms-length pricing. Pursuant to the provision the tax administrator is empowered to adjust the economic result of the taxpayer if the prices agreed between *economically and personally linked* subjects differ from the prices which would have been agreed to between independent subjects in normal commercial relations under similar conditions.

Persons are *economically or personally related* if:

a) they participate directly or indirectly in management, control, or equity of the other party (which means ownership of more than 25% of shares in basic capital or voting rights);

b) the same physical or legal persons directly or indirectly participate in management control or equity of both parties; or

c) they are personally related physical persons (relatives).

Czech tax authorities are very inexperienced in exercising transfer-pricing rules and to the best of our knowledge there have been no rulings concerning this matter yet.

The Czech tax system does not have any group taxation provisions that allow for the aggregation of losses and profits arising in companies under joint control. There are, however, provisions reducing the burden of double taxation of the net profit of an enterprise if it pays out dividends. Relief is provided in two ways. First, one half of the tax withheld while paying dividends can be deducted from the tax base of the enterprise paying the dividends in the year when such withholding took place. Second, the tax base subjected to withholding tax is reduced proportionately if three enterprises are consecutively involved in paying out the dividends (i.e. enterprise A pays dividends to B, and B pays dividends to C), on the condition that B has at least a 20% share in A, and C has at least a 20% share in B. *This provision is not applicable if enterprise C receiving dividends from B is seated abroad.*

VAT is charged by the customs authority without regard to the country from which the goods are imported. Goods are generally subject to 22% VAT and services to 5% VAT. The VAT does not apply to exports from the Czech Republic. International transport is also not subject to VAT.

Excise taxes apply to selected goods (hydrocarbon fuels and lubricants, spirits, beer, wine, and tobacco products) upon importation or release from inventory by a local producer.

A customs union exists between the Czech Republic and the Slovak Republic, which means that only VAT is charged when goods originating in Slovakia are imported into the Czech Republic.

Free trade agreements exist between the Czech Republic and the following countries: EU members, Poland, Hungary, Slovenia, Romania, and Bulgaria. These agreements stipulate a reduction of customs duty rates for most goods. Duties are abolished for some goods, and gradually reduced for others. Protocols to the agreements set out the rules for defining the origin of goods.

The agreement with the EU removes or reduces the import duties on products imported and originating from EU member countries. The special reduced rates are phased in over a period of years and at the end of the period a 0% import duty applies. For example, the rate applied to most passenger vehicles was 18% in 1994, 14.4% in 1995, and will be 10.8% in 1997. In 1999 it will be lowered to 7.2% and finally reduced to 0% in 2001.

Foreign physical and legal persons are not allowed to purchase and hold real estate in the Czech Republic. Czech legal entities 100% owned by foreigners, however, are not subject to the same restriction.

Hugo van der Zee is a partner in charge of the Tax Department at Deloitte & Touche's office in Prague. Ivan Hruskovic also contributed to this article. ■

Czech Republic

CASE STUDY: PRIVATIZATION OF AVIA

The following case study was prepared by ***Creditanstalt Securities, a.s.*** *in Prague. In December 1994, Creditanstalt was appointed as financial advisor by a consortium comprising* ***Daewoo Heavy Industries*** *and* ***Steyr-Daimler-Puch AG*** *("Daewoo-Steyr") to advise on participation in the National Property Fund ("NPF") tender of shares in truck manufacturer* ***AVIA, J.S.C.*** *and on the acquisition by the consortium of sufficient additional shares to achieve a 51% controlling position in AVIA. Daewoo-Steyr succeeded in submitting the winning tender for the AVIA shares and today holds a 50.2% interest in AVIA.*

The Transaction

In 1995 the NPF offered under a multi-criteria tender 34% of the shares of AVIA, the Czech light-weight truck manufacturer. There are three large truck makers in the Czech Republic: AVIA, heavy truck producer **Tatra,** and middle-weight truck manufacturer **Skoda Liaz**. AVIA had already been subject to voucher privatization, pursuant to which the majority of its shares were held by Czech individuals and by Czech voucher privatization funds.

The Objective

There were two main objectives in developing a successful bid. First, to prepare a business plan that would be both politically acceptable and in line with the consortium's strategy for AVIA. Second, to offer a price which would be attractive for the NPF and which would at the same time allow a sufficient return on investment for the consortium.

Obstacles

Prejudice Czech government bodies are often prejudiced in favor of Czech, as opposed to foreign, bidders. Furthermore, Steyr was in a particularly vulnerable position since it had shown an interest in acquiring 51% of AVIA in the past, but then had withdrawn from discussion.

Time Pressure There was little more than a month within which to mount a tender submission for the consortium. Detailed meetings with decision-makers had to be undertaken within this period to assess what criteria the decision-makers felt most important in the bid submission, together with a detailed analysis of the target company to allow for the preparation of a business plan and valuation.

Uncertainty About Acquiring a Majority The bid submitted by the consortium to the NPF had to be phrased in such a way that it was conditional upon the consortium acquiring sufficient extra shares from voucher privatization funds to ensure majority control of AVIA. Moreover, discussions had to be undertaken simultaneously with voucher funds to negotiate the purchase of their AVIA shareholdings conditional upon the success of the NPF tender.

Cultural Differences Great care had to be taken to bridge the cultural differences and requirements existing between the consortium members, the NPF, and other tender decision-makers.

Czech Language All the tender documents had to be submitted in Czech. The majority of the individuals representing the NPF, AVIA, and the investment funds did not speak English or German.

Lobbying of Other Bidders Influential domestic parties were interested in AVIA including a group close to **Skoda Plzen** (the largest Czech industrial holding group) and the management of AVIA.

Reasons for Success of the Daewoo-Steyr Bid

Relationship Management
Relationships were managed on three fronts. First, discussions were held with Czech governmental bodies involved and with the NPF. Lobbying at the governmental level included communications with Vaclav Klaus, the Prime Minister, by Dr. Schmid-Chiari, the Chairman of Creditanstalt Bankverein.

Second, on-going discussions with the management of AVIA were held regarding views on a business plan, contingent liabilities, and trade unions.

Third, negotiations were conducted with the key voucher privatization shareholders in AVIA to provide for the acquisition of sufficient extra shares to provide control of AVIA assuming success in the tender. All the these functions were conducted in close consultation with Daewoo-Steyr to ensure client control of the project.

Business Plan Three issues in the business plan were crucial. First, there was a plan to invest CZK 9 billion until 2000. Production would increase seven-fold as a result within six years and sales would increase 12-fold from CZK 2 billion in 1994 to CZK 24 billion in 2000.

Second, AVIA's export capability would be enhanced through its ability to use Daewoo-Steyr's export and service network.

Third, Czech suppliers on components would be preferred. The document was carefully worded in the Czech language so as not to provide an unconditional commitment to implement the business plan.

Negotiations with other Shareholders To ensure a majority for Daewoo-Steyr, the four largest voucher privatization fund shareholders were approached to sell their stakes. After separate negotiations, a commitment was obtained from three of them to sell their stakes to Daewoo-Steyr conditional upon winning the tender. ■

Czech Economic Indicators

	1996
GDP Growth (IQ)	4.3%
Industrial Output (I-IIQ)	8.2%
Inflation (July)	9.4%
Unemployment (July)	3.0%
Trade Balance (USD mil.)	-3117
Avg. Wage Increase (IQ)	
Nominal	17.4%
Real	7.9%
Exchange Rate (Sept.)	USD 1=CZK 26.60
New Credit Average	
Interest Rate (July)	13.82%
Average Interbank Deposit	
Interest Rate (July)	
7 day	12.58%
3 month	12.80%
6 month	12.86%

Source: Czech National Bank

***Profile** Continued From Page 1*

TUV Bayern. Second is R&D support for manufacturers. We can provide them with the design of individual parts, components, or systems. And then, naturally, we can provide them with development testing. In some special fields we are able to deliver the whole project solution. For example, in the past we [handled] the complete design and calculation project for a Skoda car gearbox and took over a substantial part of the development testing.

For the time being, unfortunately, we don't have such a big project and it results from the developments here in Central Europe. From 1989, all our manufacturers, Skoda, **Liaz**, **Tatra**, **AVIA**, **Karosa**, practically stopped their R&D projects because it was necessary to reconstruct or modify their corporations and they looked for [foreign] partners. At that time 70-80% of our market virtually collapsed. In 1988-89, we had approximately 630 people. [Now] we have 140 to 150. Before that time we had approximately 80% of our turnover from R&D activities and 20% from approval testing. For the time being the percentage of these two components is about 40% testing and 60% R&D. We are trying to increase the turnover of our development services.

CEAR: What other projects have you worked on?

Volak: We have [recently] developed a whole muti-purpose vehicle for the Czech manufacturer **Agromotor**, from the first sketch and calculations to the prototyping.

We cooperate with all manufacturers in the development of their vehicles from a passive safety point of view. We develop restraint systems and provide them with the full-range of passive safety testing. For example, we developed a special mathematical method for simulation of the airbag operation. We can calculate for our customers the movement of the air in the combustion chamber. For injection systems it means the distribution of individual sprays of a nozzle with respect to the combustion chamber and configuration. New projects, we cooperate with one German company [in the] design of engines using CAD/CAM. CAD/CAM is a new field of work for us.

CEAR: How do you plan to regain lost business, through marketing, or developing new areas of expertise such as CAD/CAM?

Volak: We try to, naturally, keep our business contacts with our former main business partners, the automotive manufacturers. And we offer them our new products, [such as] the ultra-light airplane engine or CAD/CAM design. We try to keep our eyes on their development needs and help them. For approval testing we are concentrated on upgrading our testing facilities simultaneously with the new standards. For example, we are preparing for the opening of our new passive safety laboratory. Our laboratory is equipped at VW standards set for the year 2005. It's necessary to provide our customers with the opportunity to test and develop products in advance [of new legal requirements].

CEAR: How can a company use your testing services?

Volak: We will work out a normal contract with them, on a contract basis. We guarantee to all our customers [confidential] testing. And because we are a member of the **TUV Bayern** group, [which] has approximately 30 daughter companies all over the world, we are fully acquainted with the legal requirements in the different markets. Even for very special markets, for example, like Israel. We can provide certificates [through] sister companies for all markets.

CEAR: Why should a company come to you if they have a design project or need a product tested?

Volak: [Regarding] the passive safety laboratory, we are in direct competition with the Western European passive safety laboratories and with **NAMI** in Moscow. Our business advantage is that we are close to our manufacturers and we can provide them with complex support at a decent price.

CEAR: What are your advantages for research and development?

Volak: Mainly promptness and decent prices. But on the other side, I believe the main advantage of this institute is that we can cope with the big projects. We are engine experts, passive safety experts, driving safety experts, CAD/CAM experts, gearbox experts. We can cope with the complex tasks from the beginning. From the design, during the testing, and in the approval period as well.

CEAR: Why are your costs so attractive?

Volak: Personnel costs. We use, and must use, the same equipment as other competitive companies.

CEAR: What advice would you give to a company that needs to have its product tested and certified for the Czech Republic?

Volak: I believe from an approval certificate point of view, this market is absolutely open. Manufacturers coming to the Czech Republic have no substantial problems with the approval of their products. Some 90%, maybe more, of our approval system is virtually compatible with Western Europe.

CEAR: What trends do you see in the Czech automotive industry that affect how you do business?

Volak: It depends on the automotive manufacturers. Skoda, I believe, is for the time being a well established manufacturer. There is **AVIA**, majority-owned by **Daewoo**. I must confess that it is not clear now what the European strategy is of Daewoo. For our institute it will be most interesting [to see] where will be sited their development division. I believe that it wouldn't be a bad decision if they had a substantial part of their development department here in Prague. For example, **Mercedes Benz** established in Prague a new development center for car engines, approximately one year ago.

CEAR: Any other interesting trends you are watching?

Volak: Everything depends on the development of the market. The plans of all manufacturers depend on the political and business developments mainly in the [Central and] Eastern parts of Europe.

CEAR: Where will UVMV be in 5 years?

Volak: We will be fully up to the level of Western European companies. We <u>must</u> be at these levels. A lot of people and manufacturers think that, [since] our main business advantage is the low wages and salaries, [we can] provide them [with] prices 50% [below Western European prices]. It's nonsense. We must use the same technology and I'm afraid that after five years the wages and salaries will be nearly the same as in Western Europe. We must make use of this period to upgrade our services to be fully competitive. We refused during the privatization procedure the offer of our authorities to provide us with some security. We wanted to go into competition and try to survive. For the time being I believe we will survive well. ■

Investment *Continued From Page 7*

Accordingly, investors should not presume that their local partners can fully inform them about the effects of these changes, and should seek expert guidance when dealing with corporate matters, shares and securities instruments, and when chasing debtors on the brink of bankruptcy.

This article was prepared by Diane Ruth Holt from the Central European Advisory Group, a legal and consulting firm in Prague. ■

To report news of acquisitions, joint ventures, sales contracts, new offices, or job changes write to Opportunity Spotlight, CEAR at 4800 Baseline Rd. Suite E104-340, Boulder, CO 80303 USA, or E-Mail to cetmllc@ibm.net.

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Feature Country *Continued From Page 11*

Tips from Insiders:

- ▲ With the low unemployment rate of about 3%, investors face tough competition for the best employees, managers, and outside assistance
- ▲ Heavy profit taxation in the Czech Republic impedes business expansion
- ▲ Laborers in the components industry are demanding wage increases of 3-5% annually
- ▲ Expect more consolidation in the Czech truck industry

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U.S. partner sought for Czech producer of crankshafts (various sizes up to 2500 mm lengths) for purpose of contract manufacturing. Company is supplier to producers of engines for trucks, tractors, ships, & stationary aggregates. 1996 turnover expected to be USD 20 million.	————	Jan Vesely IESC	tel: (42 2) 2499-3170 fax: (42 2) 2499-3176
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Jan Vesely is with the International Executive Service Corps office in Prague.

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